

May 10, 2001

Ms. Katherine A. England
Assistant Director
Division of Market Regulation
Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549-1001

**Re: File No. SR-NASD-00-33 – Amendments to NASD Rule 3340 to
Prohibit Publication of Quotations or Indications of Interest in a Security
During a Trading Halt; Response to Comment Letter**

Dear Ms. England:

NASD Regulation, Inc. (“NASD Regulation”) is submitting this letter in response to a comment letter received by the Securities and Exchange Commission (“SEC” or “Commission”) following publication in the *Federal Register* of SR-NASD-00-33, as amended. The NASD is proposing to amend NASD Rule 3340 to prohibit publication of quotations or indications of interest in a security during a trading halt.

Background

The proposed rule change amends NASD Rule 3340 to prohibit members or associated persons from, directly or indirectly, effecting any transaction or publishing a quotation, a priced bid and/or offer, an unpriced indication of interest, or a bid or offer accompanied by a modifier to reflect unsolicited customer interest, in any security as to which a trading halt is currently in effect. Rule 3340 focuses on prohibiting specific conduct. Accordingly, Rule 3340 is not directly tied to the Nasdaq market, or to a particular Nasdaq quotation or execution facility.

The Commission received one comment letter from Island ECN, Inc. (“Island”) on the proposed rule change. The SEC has requested that NASD Regulation address the issues raised in Island’s comment letter. Island asserts that NASD Regulation has not fully considered the implications of the proposed rule change. Specifically, Island requests clarification about how

Nasdaq's market resumption process will operate with respect to the proposed rule change. In addition, Island seeks to have system changes made to SelectNet to prevent the entry of an order during a trading halt and would like Nasdaq to develop a fully automated method to alert members of trading halts.

Discussion

The proposed rule change will not affect the resumption process for Nasdaq National Market Securities ("NNM") and Nasdaq SmallCap ("SCM") securities. Nasdaq MarketWatch will continue to provide notice of a trading halt to members through the Nasdaq Workstation. Contemporaneously, all quotes for the security at issue will be eliminated from the Nasdaq workstation interactive area. Nasdaq's MarketWatch Department will continually update the status of the trading halt and will notify members of the exact time the trading halt will end. In addition, Nasdaq MarketWatch will notify members that they can begin entering quotations in anticipation of the end of the trading halt (the "grace period"). Quotations entered during this grace period are designated as closed by displaying a "g" symbol next to each quotation. The quotations remain closed until the trading halt has ended, at which time the "g" symbol is removed and quotations become firm. This resumption process is used by Nasdaq MarketWatch for NNM and SCM securities exclusively.¹ Nasdaq MarketWatch does not use this process for OTC Bulletin Board securities or securities traded over-the-counter in the third market.

Island asserts that it would be more efficient if the SelectNet system were modified to prevent the entry of orders during a trading halt, instead of adopting the proposed rule change to address the problem of trading during a halt. NASD Regulation has forwarded Island's comment letter to Nasdaq. Nonetheless, regardless of whether Nasdaq makes the suggested changes to SelectNet, it is a member's responsibility to ensure compliance with NASD rules. Moreover, NASD Regulation believes that the proposed rule change is necessary. Modifying SelectNet to prevent members from entering orders into one particular trading facility may be appropriate as a supplemental measure, but there must be a fundamental prohibition of the conduct covered by the proposal.

Finally, Island recommends that Nasdaq be required to develop an official and automated method to alert members of trading halts. In support of this request, Island cites two occasions where incorrect or delayed messages regarding the status of trading halts were posted on the Nasdaq News Frame. It is NASD Regulation's understanding that incorrect or delayed

¹ NASD Regulation would not consider the entry of closed quotations into Nasdaq for NNM and SCM securities, in conformity with Nasdaq's resumption process, a violation of Rule 3340.

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messages regarding the status of trading halts are relatively infrequent. Nonetheless, we have referred this matter to Nasdaq for its consideration.

In conclusion, NASD Regulation believes that the proposed rule change protects investors and the public interest by ensuring the integrity of quotations. Accordingly, NASD Regulation requests that the Securities and Exchange Commission approve this rule filing as consistent with Section 15A(b)(6) of the Securities Exchange Act of 1934.

NASD REGULATION, INC.

BY: _____
Jeffrey S. Holik
Vice President and
Acting General Counsel