June 8, 2004

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-2004-089 – Proposed Amendments to Require Price Improvement to Limit Orders in Certain Circumstances

Dear Ms. England:

Pursuant to Rule 19b-4, enclosed please find the above-numbered rule filing. Also enclosed is a 3-l/2" disk containing the rule filing in Microsoft Word 7.0 to facilitate production of the Federal Register release.

If you have any questions, please contact Andrea Orr, Office of General Counsel, Regulatory Policy and Oversight, at (202) 728-8156; e-mail andrea.orr@nasd.com. The fax number of the Office of General Counsel is (202) 728-8264.

Very truly yours,

Barbara Z. Sweeney
Senior Vice President
and Corporate Secretary

Enclosures

File No. SR-NASD-2004-089
Consists of 21 Pages
June 8, 2004

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C.

Form 19b-4

Proposed Rule Change

by

NATIONAL ASSOCIATION OF SECURITIES DEALERS, INC.

Pursuant to Rule 19b-4 under the
Securities Exchange Act of 1934

1. <u>Text of Proposed Rule Change</u>

(a) Pursuant to the provisions of Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"), the National Association of Securities Dealers, Inc. ("NASD") is filing with the Securities and Exchange Commission ("SEC" or "Commission") a proposed rule change to require members to provide price improvement to customer limit orders in certain circumstances and to expand the application of IM-2110-2 to exchange-listed securities. Below is the text of the proposed rule change. Proposed new language is underlined; proposed deletions are in brackets.

* * * * *

IM-2110-2. Trading Ahead of Customer Limit Order

(a) General Applications

To continue to ensure investor protection and enhance market quality, <u>NASD's</u> [the Association's] Board of Governors is issuing an interpretation to <u>NASD</u> [the] Rules [of the Association] dealing with member firms' treatment of their customer limit orders in Nasdaq <u>and exchange-listed</u> securities. This interpretation, which is applicable from 9:30 a.m. to 6:30 p.m. Eastern Time, will require members acting as market makers to handle their customer limit orders with all due care so that market makers do not "trade ahead" of those limit orders. Thus, members acting as market makers that handle customer limit orders, whether received from their own customers or from another member, are prohibited from trading at prices equal or superior to that of the limit order without executing the limit order. [Such orders shall be protected from executions at prices that are superior but not equal to that of the limit order.] In the interests of investor protection, NASD [the Association] is eliminating the so-called disclosure "safe harbor" previously established for members that fully disclosed to their customers the practice of trading ahead of a customer limit order by a market-making firm.[1]

Rule 2110 [of the Association Rules] states that:

A member, in the conduct of his business, shall observe high standards of commercial honor and just and equitable principles of trade.

Rule 2320, the Best Execution Rule, states that:

In any transaction for or with a customer, a member and persons associated with a member shall use reasonable diligence to ascertain the best inter-dealer market for the subject security and buy or sell in such a market so that the resultant price to the customer is as favorable as possible to the customer under prevailing market conditions.

Interpretation

The following interpretation of Rule 2110 has been approved by the Board:

A member firm that accepts and holds an unexecuted limit order from its customer (whether its own customer or a customer of another member) in a Nasdaq or exchange-listed security and that continues to trade the subject security for its own market-making account at prices that would satisfy the customer's limit order, without executing that limit order, shall be deemed to have acted in a manner inconsistent with just and equitable principles of trade, in violation of Rule 2110, provided that[, until September 1, 1995, customer limit orders in excess of 1,000 shares received from another member firm shall be protected from the market maker's executions at prices that are superior but not equal to that of the limit order, and provided further, that] a member firm may negotiate specific terms and conditions applicable to the acceptance of limit orders only with respect to limit orders that are: (a) for customer accounts that meet the definition of an "institutional account" as that term is defined in Rule 3110(c)(4); or (b) 10,000 shares or more, unless such orders are less than $100,000 in value. In the event that a member acting as market maker trades ahead of an unexecuted customer limit order at a price that is better than the unexecuted limit order, such member is required to execute the limit order at the price received by the member or better. Nothing in this interpretation, however, requires members to accept limit orders from any customer.

By rescinding the safe harbor position and adopting this interpretation, NASD [the Association] wishes to emphasize that members may not trade ahead of their customer limit orders in their market-making capacity even if the member had in the past fully disclosed the practice to its customers prior to accepting limit orders. NASD [The Association] believes that, pursuant to Rule 2110, members accepting and holding unexecuted customer limit orders owe certain duties to their customers and the customers of other member firms that may not be overcome or cured with disclosure of trading practices that include trading ahead of the customer's order. The terms and conditions under which institutional account or appropriately sized customer limit orders are accepted must be made clear to customers at the time the order is accepted by the firm so that trading ahead in the firm's market making capacity does not occur. [For purposes of this interpretation, a member that controls or is controlled by another member shall be considered a single entity so that if a customer's limit order is accepted by one affiliate and forwarded to another affiliate for execution, the firms are considered a single entity and the market making unit may not trade ahead of that customer's limit order.]

As outlined in NASD Notice to Members 97-57, the minimum amount of price improvement necessary in order for a market maker to execute an incoming order on a proprietary basis when holding an unexecuted limit order for a Nasdaq security trading in fractions, and not be required to execute the held limit order, is as follows:

- If actual spread is greater than 1/16 of a point, a firm must price improve an incoming order by at least a 1/16 . For stocks priced under $10, (which are quoted in 1/32 increments) the firm must price improve by at least 1/64 .
- If actual spread is the minimum quotation increment, a firm must price improve an incoming order by one-half the minimum quotation increment.

For Nasdaq securities authorized for trading in decimals pursuant to the Decimals Implementation Plan For the Equities and Options Markets, the minimum amount of price improvement necessary in order for a market maker to execute an incoming order on a proprietary basis in a security trading in decimals when holding an unexecuted limit order in that same security, and not be required to execute the held limit order, is as follows:

1) For customer limit orders priced at or inside the best inside market displayed in Nasdaq, the minimum amount of price improvement required is $0.01; and

2) For customer limit orders priced outside the best inside market displayed in Nasdaq, the market maker must price improve the incoming order by executing the incoming order at a price at least equal to the next superior minimum quotation increment in Nasdaq (currently $0.01).

NASD [The Association] also wishes to emphasize that all members accepting customer limit orders owe those customers duties of "best execution" regardless of whether the orders are executed through the member's market making capacity or sent to another member for execution. As set out above, the Best Execution Rule requires members to use reasonable diligence to ascertain the best inter-dealer market for the security and buy or sell in such a market so that the price to the customer is as favorable as possible under prevailing market conditions. NASD [The Association] emphasizes that order entry firms should continue to routinely monitor the handling of their customers' limit orders regarding the quality of the execution received.

(b) and (c) No change.

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1 For purposes of [the pilot program expanding]the operation of certain Nasdaq transaction and quotation reporting systems and facilities [in SR-NASD-99-57]during the period from 4 p.m. to 6:30 p.m. Eastern Time, members may generally limit the life of a customer limit order to the period of 9:30 a.m. to 4 p.m. Eastern Time. If a customer does not formally assent ("opt-in") to processing of [their]the customer's limit order(s) during the extended hours period commencing after the normal close of the Nasdaq market, limit order protection will not apply to that customer's order(s).

* * * * *

(b) Not applicable.

(c) Not applicable.

2. Procedures of the Self-Regulatory Organization

(a) The proposed rule change was approved by the Board of Directors of NASD Regulation, Inc. at its meeting on April 21, 2004, which authorized the filing of the rule change with the SEC. Counsel for The Nasdaq Stock Market and NASD Dispute Resolution have been provided an opportunity to consult with respect to the proposed rule change, pursuant to the Plan of Allocation and Delegation of Functions by NASD to its Subsidiaries. The NASD Board of Governors reviewed the proposed rule change at its meeting on April 22, 2004. No other action by NASD is necessary for the filing of the proposed rule change. Section 1(a)(ii) of Article VII of the NASD By-Laws permits the NASD Board of Governors to adopt NASD Rules without recourse to the membership for approval.

NASD will announce the effective date of the proposed rule change in a Notice to Members to be published no later than 60 days following Commission approval. The effective date will be 90 days following publication of the Notice to Members announcing Commission approval.

(b) Questions regarding this rule filing may be directed to Andrea Orr, Assistant General Counsel, Office of General Counsel, Regulatory Policy and Oversight, at (202) 728-8156.

3. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

(a) Purpose

Interpretive Material (IM) 2110-2, Trading Ahead of Customer Limit Order (commonly referred to as the "Manning Interpretation") generally prohibits a member from trading for its own account at prices that would satisfy a customer's limit order, unless the member immediately thereafter executes the customer limit order.[1] The legal underpinnings for the

[1] For example, if a member bought 100 shares at $10 when holding customer limit orders in the same security to buy at $10 equaling, in aggregate, 1000 shares, the member is required to fill 100 shares of the customer limit orders. Rule 6440(f)(2) imposes similar requirements with respect to the receipt of customer limit orders in exchange-listed securities traded over-the-counter.

Manning Interpretation are a member's basic fiduciary obligations and the requirement that it must, in the conduct of its business, "observe high standards of commercial honor and just and equitable principles of trade."[2]

The Manning Interpretation is designed to ensure that customer limit orders are executed in a fair manner by prohibiting a member firm from trading ahead of customers' limit orders in its principal capacity without executing the customer limit order. The Interpretation currently, however, only requires that a member that "trades ahead" of a customer limit order execute the customer limit order at its limit price. If the member trades ahead of a customer limit order and receives a better price than the unexecuted customer limit order, the Manning Interpretation currently would not obligate the member to pass along the better price it received; it need only fill the customer limit order at the limit price.

NASD believes that where a member trades at a price better than an unexecuted customer limit order, the member should be required to pass along such price improvement to the unexecuted customer limit order. Accordingly, NASD is proposing to prohibit a member from trading for its own account in a Nasdaq or exchange-listed security[3] at a price that is better than an unexecuted customer limit order in that security, unless the member immediately thereafter executes the customer limit order at the price, at which it traded for its own account or better.

In recognition that the proposed rule change may alter the way that many members handle customer orders, NASD believes that it is important to provide members with adequate

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2 See NASD Rule 2110.

3 Rule 6440(f)(2) currently prohibits members from trading ahead of their customer limit orders in exchange-listed securities traded over-the-counter. To ensure consistency in the application of limit order protection to Nasdaq and exchange-listed securities, NASD also is proposing to apply explicitly its Manning Interpretation to exchange-listed securities. NASD will recommend to Nasdaq that it consider deleting Rule 6440(f)(2), in light of the proposed application of IM-2110-2 to exchange-listed securities.

time to develop and implement systems to comply with the proposed rule change. Therefore, NASD is proposing an implementation date of 90 days after the issuance of a Notice to Members announcing SEC approval of the proposed rule change.

In addition, NASD also is proposing technical changes to the Manning Interpretation to delete language contained in the rule text that is no longer necessary. Specifically, as part of a proposed expansion of the Manning Interpretation in 1994, the Manning Interpretation included a phase-in period which expired on September 1, 1995.[4] Prior to that time period, the Manning Interpretation permitted member firms to handle member-to-member limit orders that were larger than 1,000 shares more liberally (such limit orders were only required to be protected from executions at prices that were superior but not equal to that of the limit order). Given that the phase-in period has expired, NASD is proposing to delete the rule text related to the phase-in period or that was necessary only when the Manning Interpretation did not apply to member-to-member limit orders. In addition, NASD is proposing to delete certain unnecessary rule text contained in footnote one relating to a Nasdaq pilot program expanding the operation of certain Nasdaq transaction and quotation reporting systems and facilities during the period from 4 p.m. to 6:30 p.m. Eastern Time. This Nasdaq pilot program became a permanent program in 2003 and this footnote text inadvertently was not deleted as part of the rule filing making the pilot permanent.[5] Finally, NASD no longer refers to itself or its subsidiary, NASD Regulation, Inc., using its full corporate name, “the Association,” “the NASD” or “NASD Regulation, Inc.” Instead, NASD uses “NASD” unless otherwise appropriate for corporate or regulatory reasons.

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4 See Exchange Act Release No. 35751 (May 22, 1995), 60 FR 27997 (May 26, 1995) (File No. SR-NASD-94-62).

5 See Exchange Act Release No. 47308 (February 6, 2003), 68 FR 28 (February 11, 2003) (File No. SR-NASD-2003-14).

Accordingly, the proposed rule change replaces several references to "Association" in the text of the proposed rule change with "NASD."

(b) Statutory Basis

NASD believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act, which requires, among other things, that NASD's rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest. NASD believes that the proposed rule change will improve treatment of customer limit orders and enhance the integrity of the market.

4. <u>Self-Regulatory Organization's Statement on Burden on Competition</u>

NASD does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act, as amended.

5. <u>Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others</u>

Written comments were neither solicited nor received.

6. <u>Extension of Time Period for Commission Action</u>

NASD does not consent at this time to an extension of the time period for Commission action specified in Section 19(b)(2) of the Act.

7. <u>Basis for Summary Effectiveness Pursuant to Section 19(b)(3) or for Accelerated Effectiveness Pursuant to Section 19(b)(2)</u>

Not applicable.

8. <u>Proposed Rule Change Based on Rules of Another Self-Regulatory Organization or of the Commission</u>

Not applicable.

9. Exhibits

1. Completed notice of proposed rule change for publication in the Federal Register.

Pursuant to the requirements of the Securities Exchange Act of 1934, NASD has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized.

NASD, INC.

BY:____
Barbara Z. Sweeney, Senior Vice President and
Corporate Secretary

Date: June 8, 2004

EXHIBIT 1

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-   ; File No. SR-NASD-2004-089)

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by National Association of Securities Dealers, Inc. Relating to Proposed Amendments to Require Limit Order Protection

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")[1] and Rule 19b-4 thereunder,[2] notice is hereby given that on   , the National Association of Securities Dealers, Inc. ("NASD"), filed with the Securities and Exchange Commission ("SEC" or "Commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by NASD. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. SELF-REGULATORY ORGANIZATION'S STATEMENT OF THE TERMS OF SUBSTANCE OF THE PROPOSED RULE CHANGE

NASD is proposing to require providing price improvement to customer limit orders under the circumstances described herein and to expand the application of IM-2110-2 to exchange-listed securities. Below is the text of the proposed rule change. Proposed new language is in italics; proposed deletions are in brackets.

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1 15 U.S.C. 78s(b)(1).

2 17 CFR 240.19b-4.

IM-2110-2. Trading Ahead of Customer Limit Order

(a) General Applications

To continue to ensure investor protection and enhance market quality, NASD's [the Association's] Board of Governors is issuing an interpretation to NASD [the] Rules [of the Association] dealing with member firms' treatment of their customer limit orders in Nasdaq and exchange-listed securities. This interpretation, which is applicable from 9:30 a.m. to 6:30 p.m. Eastern Time, will require members acting as market makers to handle their customer limit orders with all due care so that market makers do not "trade ahead" of those limit orders. Thus, members acting as market makers that handle customer limit orders, whether received from their own customers or from another member, are prohibited from trading at prices equal or superior to that of the limit order without executing the limit order. [Such orders shall be protected from executions at prices that are superior but not equal to that of the limit order.] In the interests of investor protection, NASD [the Association] is eliminating the so-called disclosure "safe harbor" previously established for members that fully disclosed to their customers the practice of trading ahead of a customer limit order by a market-making firm.[1]

Rule 2110 [of the Association Rules] states that:

A member, in the conduct of his business, shall observe high standards of commercial honor and just and equitable principles of trade.

Rule 2320, the Best Execution Rule, states that:

In any transaction for or with a customer, a member and persons associated with a member shall use reasonable diligence to ascertain the best inter-dealer market for the subject security and buy or sell in such a market so that the resultant price to the customer is as favorable as possible to the customer under prevailing market conditions.

Interpretation

The following interpretation of Rule 2110 has been approved by the Board:

A member firm that accepts and holds an unexecuted limit order from its customer (whether its own customer or a customer of another member) in a Nasdaq or exchange-listed security and that continues to trade the subject security for its own market-making account at prices that would satisfy the customer's limit order, without executing that limit order, shall be deemed to have acted in a manner inconsistent with just and equitable principles of trade, in violation of Rule 2110, provided that[, until September 1, 1995, customer limit orders in excess of 1,000 shares received from another member firm shall be protected from the market maker's executions at prices that are superior but not equal to that of the limit order, and provided further, that] a member firm may negotiate specific terms and conditions applicable to the acceptance of limit orders only with respect to limit orders that are: (a) for customer accounts that meet the definition of an "institutional account" as that term is defined in Rule 3110(c)(4); or (b) 10,000 shares or more, unless such orders are less than $100,000 in value. In the event that a member acting as market maker trades ahead of an unexecuted customer limit order at a price that is better than the unexecuted limit order, such member is required to execute the limit order at the price received by the member or better. Nothing in this interpretation, however, requires members to accept limit orders from any customer.

By rescinding the safe harbor position and adopting this interpretation, NASD [the Association] wishes to emphasize that members may not trade ahead of their customer limit orders in their market-making capacity even if the member had in the past fully disclosed the practice to its customers prior to accepting limit orders. NASD [The

Association] believes that, pursuant to Rule 2110, members accepting and holding unexecuted customer limit orders owe certain duties to their customers and the customers of other member firms that may not be overcome or cured with disclosure of trading practices that include trading ahead of the customer's order. The terms and conditions under which institutional account or appropriately sized customer limit orders are accepted must be made clear to customers at the time the order is accepted by the firm so that trading ahead in the firm's market making capacity does not occur. [For purposes of this interpretation, a member that controls or is controlled by another member shall be considered a single entity so that if a customer's limit order is accepted by one affiliate and forwarded to another affiliate for execution, the firms are considered a single entity and the market making unit may not trade ahead of that customer's limit order.]

As outlined in NASD Notice to Members 97-57, the minimum amount of price improvement necessary in order for a market maker to execute an incoming order on a proprietary basis when holding an unexecuted limit order for a Nasdaq security trading in fractions, and not be required to execute the held limit order, is as follows:

- If actual spread is greater than 1/16 of a point, a firm must price improve an incoming order by at least a 1/16 . For stocks priced under $10, (which are quoted in 1/32 increments) the firm must price improve by at least 1/64 .

- If actual spread is the minimum quotation increment, a firm must price improve an incoming order by one-half the minimum quotation increment.

For Nasdaq securities authorized for trading in decimals pursuant to the Decimals Implementation Plan For the Equities and Options Markets, the minimum amount of price improvement necessary in order for a market maker to execute an incoming order on a proprietary basis in a security trading in decimals when holding an unexecuted limit order in that same security, and not be required to execute the held limit order, is as follows:

1) For customer limit orders priced at or inside the best inside market displayed in Nasdaq, the minimum amount of price improvement required is $0.01; and

2) For customer limit orders priced outside the best inside market displayed in Nasdaq, the market maker must price improve the incoming order by executing the incoming order at a price at least equal to the next superior minimum quotation increment in Nasdaq (currently $0.01).

NASD [The Association] also wishes to emphasize that all members accepting customer limit orders owe those customers duties of "best execution" regardless of whether the orders are executed through the member's market making capacity or sent to another member for execution. As set out above, the Best Execution Rule requires members to use reasonable diligence to ascertain the best inter-dealer market for the security and buy or sell in such a market so that the price to the customer is as favorable as possible under prevailing market conditions. NASD [The Association] emphasizes that order entry firms should continue to routinely monitor the handling of their customers' limit orders regarding the quality of the execution received.

(b) and (c) No change.

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1 For purposes of [the pilot program expanding]the operation of certain Nasdaq transaction and quotation reporting systems and facilities [in SR-NASD-99-57]during the period from 4 p.m. to 6:30 p.m. Eastern Time, members may generally limit the life of a customer limit order to the period of 9:30 a.m. to 4 p.m. Eastern Time. If a customer does not formally assent ("opt-in") to processing of [their]the customer’s limit order(s) during the extended hours period commencing after the normal close of the Nasdaq market, limit order protection will not apply to that customer's order(s).

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II. SELF-REGULATORY ORGANIZATION'S STATEMENT OF THE PURPOSE OF, AND STATUTORY BASIS FOR, THE PROPOSED RULE CHANGE

In its filing with the Commission, NASD included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. NASD has prepared summaries, set forth in Sections (A), (B), and (C) below, of the most significant aspects of such statements.

(A) Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

Interpretive Material (IM) 2110-2, Trading Ahead of Customer Limit Order (commonly referred to as the "Manning Interpretation") generally prohibits a member from trading for its own account at prices that would satisfy a customer's limit order, unless the member immediately thereafter executes the customer limit order.[3] The legal underpinnings for the Manning Interpretation are a member's basic fiduciary obligations and the requirement that it must, in the conduct of its business, "observe high standards of commercial honor and just and equitable principles of trade."[4]

The Manning Interpretation is designed to ensure that customer limit orders are executed in a fair manner by prohibiting a member firm from trading ahead of customers' limit orders in its principal capacity without executing the customer limit order. The Interpretation currently,

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3 For example, if a member bought 100 shares at $10 when holding customer limit orders in the same security to buy at $10 equaling, in aggregate, 1000 shares, the member is required to fill 100 shares of the customer limit orders. Rule 6440(f)(2) imposes similar requirements with respect to the receipt of customer limit orders in exchange-listed securities traded over-the-counter.

4 See NASD Rule 2110.

however, only requires that a member that "trades ahead" of a customer limit order execute the customer limit order at its limit price. If the member trades ahead of a customer limit order and receives a better price than the unexecuted customer limit order, the Manning Interpretation currently would not obligate the member to pass along the better price it received; it need only fill the customer limit order at the limit price.

NASD believes that where a member trades at a price better than an unexecuted customer limit order, the member should be required to pass along such price improvement to the unexecuted customer limit order. Accordingly, NASD is proposing to prohibit a member from trading for its own account in a Nasdaq or exchange-listed security[5] at a price that is better than an unexecuted customer limit order in that security, unless the member immediately thereafter executes the customer limit order at the price, at which it traded for its own account or better.

In recognition that the proposed rule change may alter the way that many members handle customer orders, NASD believes that it is important to provide members with adequate time to develop and implement systems to comply with the proposed rule change. Therefore, NASD is proposing an implementation date of 90 days after the issuance of a Notice to Members announcing SEC approval of the proposed rule change.

In addition, NASD also is proposing technical changes to the Manning Interpretation to delete language contained in the rule text that is no longer necessary. Specifically, as part of a proposed expansion of the Manning Interpretation in 1994, the Manning Interpretation included

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5 Rule 6440(f)(2) currently prohibits members from trading ahead of their customer limit orders in exchange-listed securities traded over-the-counter. To ensure consistency in the application of limit order protection to Nasdaq and exchange-listed securities, NASD also is proposing to apply explicitly its Manning Interpretation to exchange-listed securities. NASD will recommend to Nasdaq that it consider deleting Rule 6440(f)(2), in light of the proposed application of IM-2110-2 to exchange-listed securities.

a phase-in period which expired on September 1, 1995.[6] Prior to that time period, the Manning Interpretation permitted member firms to handle member-to-member limit orders that were larger than 1,000 shares more liberally (such limit orders were only required to be protected from executions at prices that were superior but not equal to that of the limit order). Given that the phase-in period has expired, NASD is proposing to delete the rule text related to the phase-in period or that was necessary only when the Manning Interpretation did not apply to member-to-member limit orders. In addition, NASD is proposing to delete certain unnecessary rule text contained in footnote one relating to a Nasdaq pilot program expanding the operation of certain Nasdaq transaction and quotation reporting systems and facilities during the period from 4 p.m. to 6:30 p.m. Eastern Time. This Nasdaq pilot program became a permanent program in 2003 and this footnote text inadvertently was not deleted as part of the rule filing making the pilot permanent.[7] Finally, NASD no longer refers to itself or its subsidiary, NASD Regulation, Inc., using its full corporate name, “the Association,” “the NASD” or “NASD Regulation, Inc.” Instead, NASD uses “NASD” unless otherwise appropriate for corporate or regulatory reasons. Accordingly, the proposed rule change replaces several references to “Association” in the text of the proposed rule change with “NASD.”

2. Statutory Basis

NASD believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act, which requires, among other things, that NASD's rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles

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6 See Exchange Act Release No. 35751 (May 22, 1995), 60 FR 27997 (May 26, 1995) (File No. SR-NASD-94-62).

7 See Exchange Act Release No. 47308 (February 6, 2003), 68 FR 28 (February 11, 2003) (File No. SR-NASD-2003-14).

of trade, and, in general, to protect investors and the public interest. NASD believes that the proposed rule change will improve treatment of customer limit orders and enhance the integrity of the market.

(B) Self-Regulatory Organization's Statement on Burden on Competition

NASD does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act, as amended.

(C) Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

Written comments were neither solicited nor received.

III. DATE OF EFFECTIVENESS OF THE PROPOSED RULE CHANGE AND TIMING FOR COMMISSION ACTION

Within 35 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

A. by order approve such proposed rule change, or

B. institute proceedings to determine whether the proposed rule change should be disapproved.

IV. SOLICITATION OF COMMENTS

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change as amended is consistent with the act. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, N.W., Washington, D.C. 20549. Comments may also be submitted electronically at the following e-mail address: rule-comments@sec.gov. All comment letters should refer to File No. SR- NASD-2004-089. This file number should be included on the subject line if e-mail is used. To help us process and review comments more efficiently, comments should be sent in hardcopy or by e-mail but not by both methods. Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Room. Copies of such filing will also be available for inspection and copying at the principal office of NASD. All submissions should refer to the file number in the caption above and should be submitted by [insert date 21 days from the date of publication].

For the Commission, by the Division of Market Regulation, pursuant to delegated authority, 17 CFR 200.30-3(a)(12).

Margaret H. McFarland
Deputy Secretary