

August 26, 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-2004-130 – Amendments to Rule 2320(g) and Rule 3110(b)(2) Relating to Foreign Securities

Dear Ms. England:

Pursuant to Rule 19b-4, enclosed please find the above-numbered rule filing. Also enclosed is a 3-1/2" 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,

Marc Menchel
Executive Vice President
and General Counsel

Enclosures

cc: Nancy Sanow
Michael J. Gaw

File No. SR-NASD-2004-130
Consists of 23 Pages
August 26, 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. Text of Proposed Rule Change

(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 amend Rule 2320(g) (the “Three Quote Rule”) and the corresponding recordkeeping requirements under Rule 3110(b)(2) to exclude from the Three Quote Rule’s coverage transactions in foreign securities of a foreign issuer that is a part of the FTSE World Index Series. Below is the text of the proposed rule change. Proposed new language is underlined; proposed deletions are in brackets.

* * * * *

2320. Best Execution and Interpositioning

(a) through (f) No change.

(g) (1) Except as provided in subparagraph (3) below, [Unless two or more priced quotations for a non-Nasdaq security (as defined in the Rule 6700 Series) are displayed in an inter-dealer quotation system that permits quotation updates on a real-time basis,] in any transaction for or with a customer pertaining to the execution of an order in a non-Nasdaq security (as defined in the Rule 6700 Series), a member or person associated with a member, shall contact and obtain quotations from three dealers (or all dealers if three or less) to determine the best inter-dealer market for the subject security.

(2) No change.

(3) The requirements described in subparagraph (1) above shall not apply:

(A) when two or more priced quotations for a non-Nasdaq security are displayed in an inter-dealer quotation system that permits quotation updates on a real-time basis; and

(B) to any transaction pertaining to the execution of an order in a non-Nasdaq security of a foreign issuer that is a part of the FTSE World Index Series if such transaction is executed during the regular business hours of the foreign market for the foreign security and no trading halt or other similar trading or quoting restriction is in effect in the foreign market for such foreign security.

(4) Definitions

For purposes of this paragraph (g): [,]

(A) T[t]he term “inter-dealer quotation system” means any system of general circulation to brokers or dealers that regularly disseminates quotations of identified brokers or dealers.

(B) [(4) For purposes of this paragraph,] T[t]he term “quotation medium” means any inter-dealer quotation system or any publication or electronic communications network or other device that is used by brokers or dealers to make known to others their interest in transactions in any security, including offers to buy or sell at a stated price or otherwise, or invitations of offers to buy or sell.

(5) No change.

* * * * *

3110. Books and Records

(a) No change.

(b) Marking of Customer Order Tickets

(1) No change.

(2) A person associated with a member shall indicate on the memorandum for each transaction in a non-Nasdaq security, as that term is defined in the Rule 6700 Series, the name of each dealer contacted and the quotations received to determine the best inter-dealer market; however, the requirements of this subparagraph shall not apply if the member can establish and has documented that:

(A) two or more priced quotations for the security are displayed in an inter-dealer quotation system, as defined in Rule 2320(g), that permits quotation updates on a real-time basis for which NASD [Regulation] has access to historical quotation information; or

(B) the transaction is effected in compliance with Rule 2320(g)(3)(B).

(c) No change.

* * * * *

(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 July 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 had an opportunity to review the proposed rule change at its meeting on July 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 amendments to 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 30 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, NASD at (202) 728-8156.

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

(a) Purpose

The Three Quote Rule originally was adopted on May 2, 1988,¹ as an amendment to NASD's best execution interpretation and generally requires that members that execute transactions in non-Nasdaq securities² on behalf of customers contact a minimum of three dealers (or all dealers if three or less) and obtain quotations, if there are fewer than two quotations displayed on an inter-dealer quotation system that permits quotation updates on a real-time basis. The Three Quote Rule is intended to create a standard to help ensure that members fulfill their best execution responsibilities to customers when engaging in transactions in non-Nasdaq securities, particularly transactions involving relatively illiquid securities with non-transparent prices. The Three Quote Rule is a minimum standard, and compliance with the

¹ See Exchange Act Release No. 25637 (May 2, 1988).

rule, in and of itself, does not mean a member has met its best execution obligations.

Since the adoption of the Three Quote Rule, the market for non-Nasdaq securities has changed significantly. NASD has found that under certain circumstances, the Three Quote Rule often can hinder, rather than further, investor protection by causing significant delays in obtaining executions of customer orders. For example, in 2000, NASD amended the Three Quote Rule to eliminate the requirement to contact three market makers when there are at least two priced quotations displayed in an inter-dealer quotation system that permits quotation updates on a real-time basis.³ NASD concluded that, where there were two transparent, firm quotes, the costs associated with delayed executions resulting from compliance with the Three Quote Rule were not outweighed by the benefits of obtaining three telephone quotes.

Similar concerns have been raised with respect to the Three Quote Rule's application in the area of orders in foreign securities of foreign issuers. Certain members and other interested parties had raised concerns that the Three Quote Rule was unnecessary and potentially harmful to the customer's best interests when a member, using reasonable diligence, has determined that the best market for a foreign security is a foreign market where the securities trade with sufficient liquidity and transparency.

NASD staff agreed that the protections of the Three Quote Rule may not be necessary with respect to all orders in foreign securities. In fact, the SEC, in its approval order granting NASD exemptive authority with respect to the Three Quote Rule, specifically indicated that

² As defined in the Rule 6700 Series, a non-Nasdaq security means any equity security that is neither included in The Nasdaq Stock Market nor traded on any national securities exchange.

³ See Exchange Act Release No. 43319 (September 21, 2000), 65 Fed. Reg. 58589 (September 29, 2000) (File No. SR-NASD-00-20). This rule change also alleviated the corresponding recordkeeping requirements under Rule 3110(b)(2) where NASD could validate and confirm compliance with applicable requirements directly through its internal historical data.

exemptive relief may be appropriate for transactions executed on a foreign exchange.⁴ The SEC stated that exemptive relief may be appropriate in such circumstances because the foreign exchange may constitute the best market for securities that are listed on that market and the time delay involved in contacting three dealers may, therefore, hinder a member from obtaining best execution for the customers.⁵

Accordingly, NASD is proposing amendments that would exclude from the Three Quote Rule's coverage transactions effected in foreign securities of foreign issuers that are part of the FTSE World Index Series.⁶ The proposed rule change would not require that the transaction be executed on a foreign market so as not to limit the member's ability to determine, in fulfilling its best execution obligations, that a better execution would be obtained off the foreign market. However, to qualify for the exemption, the transaction must be executed during regular business hours of the foreign market for the security and no trading halt or other similar trading or quotation restriction may be in effect in the foreign market for such foreign security.⁷

NASD has selected the FTSE World Index Series in part because the SEC staff has deemed the foreign securities that are listed on this index as having a "ready market" and

⁴ See Exchange Act Release No. 39266 (Oct. 22, 1997), 62 Fed. Reg. 56217 (Oct. 29, 1997).

⁵ Id.

⁶ The Financial Times and the London Stock Exchange operate the FTSE World Index Series, which is a subset of the FTSE Global Equity Index Series. The FTSE World Index Series include 30 different countries and approximately 2,381 stocks (approximately 1,744 of which are stocks of foreign issuers). See Exhibit 2 for a detailed description of the criteria used to determine the FTSE World Index.

⁷ Contingent upon approval of the proposed rule change, NASD staff plans to withdraw all existing exemptions it has granted to the Three Quote Rule that relate to foreign securities. NASD staff has granted seven exemptions for customer transactions in Canadian securities executed on a Canadian exchange on an agency or riskless principal basis. (See, e.g., Letter to Mr. Kenneth W. Perlman, General Counsel, Mayer Schweitzer, Inc. from Alden S. Adkins, Senior Vice President and General Counsel.)

therefore eligible to receive comparable favorable treatment to U.S. equity securities under the securities haircut⁸ provisions of the SEC's net capital rule.⁹ In addition, the Federal Reserve Board recognizes this index for determining whether stocks are eligible for margin treatment.¹⁰ NASD believes that the criteria used in determining the composition of the index helps to ensure that the securities trade with a high degree of liquidity, consistency, and price transparency, thereby offering investors with protections similar to that which the Three Quote Rule is intended to provide.

Importantly, while the proposed rule change would not require a member to obtain three quotes in connection with transactions in foreign securities that are part of the FTSE World Index Series, members would continue to be required to comply with their best execution obligations under Rule 2320, and to the extent applicable, their suitability obligations under Rule 2310.

The proposed rule change also would provide a corresponding exclusion to the recordkeeping requirements set forth in Rule 3110(b)(2) relating to the Three Quote Rule if the member can establish and document its reliance on this exclusion. Rule 3110(b)(2) requires that members indicate on the order ticket for each transaction in a non-Nasdaq security the name of each dealer contacted and the quotations received to determine the best inter-dealer market as

⁸ The SEC's net capital rule requires broker-dealers, when computing net capital, to deduct from their net worth certain percentages of the market value of their proprietary securities positions, commonly referred to as "haircuts." Haircuts are calculated under paragraphs (c)(2)(vi), (c)(2)(vii), and applicable appendices of the standard net capital rule, SEC Rule 15c3-1.

⁹ 1993 SEC No-Act LEXIS 967 (Aug. 13, 1993).

¹⁰ For similar reasons, NASD has a proposal pending at the SEC that would allow members to calculate on their own a higher options position limit without obtaining prior approval from NASD staff for conventional equity options overlying securities listed on the FTSE World Index Series. (See SR-NASD-2004-084)

required by the Three Quote Rule.

In addition, NASD no longer refers to its subsidiary, NASD Regulation, Inc., using its full corporate name, “NASD Regulation” or NASD Regulation, Inc.” Instead, NASD uses “NASD” unless otherwise appropriate for corporate or regulatory reasons. Accordingly, the proposed rule change replaces one reference to “NASD Regulation” in the text of the proposed rule change with “NASD.”

Finally, 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 30 days following publication of the Notice to Members announcing Commission approval.

(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 reduce the time and effort necessary in contacting three dealers in orders for foreign securities of certain foreign issuers where it has been demonstrated that such securities are trading with sufficient liquidity and price transparency.

4. 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.

5. 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.

6. Extension of Time Period for Commission Action

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. Basis for Summary Effectiveness Pursuant to Section 19(b)(3) or for Accelerated Effectiveness Pursuant to Section 19(b)(2)

Not applicable.

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

Not applicable.

9. Exhibits

1. Completed notice of proposed rule change for publication in the Federal Register.
2. Summary of the criteria used to construct the FTSE World Index Series.

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

BY: _____
Marc Menchel, Executive Vice President and
General Counsel
NASD, Regulatory Policy and Oversight

Date: August 26, 2004

EXHIBIT 1

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34- ; File No. SR-NASD-2004-130)

Self-Regulatory Organizations; Notice of Filing of Proposed Rule Change by National Association of Securities Dealers, Inc. Relating to Amendments to Rule 2320(g) and 3110(b)(2)

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 amend Rule 2320(g) (the “Three Quote Rule”) and the corresponding recordkeeping requirements under Rule 3110(b)(2) to exclude from the Three Quote Rule’s coverage transactions in foreign securities of a foreign issuer that is a part of the FTSE World Index Series. Proposed new language is in italics; proposed deletions are in brackets.

* * * * *

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

2320. Best Execution and Interpositioning

(a) through (f) No change.

(g) (1) Except as provided in subparagraph (3) below, [Unless two or more priced quotations for a non-Nasdaq security (as defined in the Rule 6700 Series) are displayed in an inter-dealer quotation system that permits quotation updates on a real-time basis,] in any transaction for or with a customer pertaining to the execution of an order in a non-Nasdaq security (as defined in the Rule 6700 Series), a member or person associated with a member, shall contact and obtain quotations from three dealers (or all dealers if three or less) to determine the best inter-dealer market for the subject security.

(2) No change.

(3) The requirements described in subparagraph (1) above shall not apply:

(A) when two or more priced quotations for a non-Nasdaq security are displayed in an inter-dealer quotation system that permits quotation updates on a real-time basis; and

(B) to any transaction pertaining to the execution of an order in a non-Nasdaq security of a foreign issuer that is a part of the FTSE World Index Series if such transaction is executed during the regular business hours of the foreign market for the foreign security and no trading halt or other similar trading or quoting restriction is in effect in the foreign market for such foreign security.

(4) Definitions

For purposes of this paragraph (g): [,]

(A) T[t]he term “inter-dealer quotation system” means any system of general circulation to brokers or dealers that regularly disseminates quotations of identified brokers or dealers.

(B) [(4) For purposes of this paragraph,] T[t]he term “quotation medium” means any inter-dealer quotation system or any publication or electronic communications network or other device that is used by brokers or dealers to make known to others their interest in transactions in any security, including offers to buy or sell at a stated price or otherwise, or invitations of offers to buy or sell.

(5) No change.

* * * * *

3110. Books and Records

(a) No change.

(b) Marking of Customer Order Tickets

(1) No change.

(2) A person associated with a member shall indicate on the memorandum for each transaction in a non-Nasdaq security, as that term is defined in the Rule 6700 Series, the name of each dealer contacted and the quotations received to determine the best inter-dealer market; however, the requirements of this subparagraph shall not apply if the member can establish and has documented that:

(A) two or more priced quotations for the security are displayed in an inter-dealer quotation system, as defined in Rule 2320(g), that permits quotation

updates on a real-time basis for which NASD [Regulation] has access to historical quotation information; or

(B) the transaction is effected in compliance with Rule 2320(g)(3)(B).

(c) No change.

* * * * *

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

The Three Quote Rule originally was adopted on May 2, 1988,³ as an amendment to NASD's best execution interpretation and generally requires that members that execute transactions in non-Nasdaq securities⁴ on behalf of customers contact a minimum of three dealers (or all dealers if three or less) and obtain quotations, if there are fewer than two quotations displayed on an inter-dealer quotation system that permits quotation updates on a real-time basis. The Three Quote Rule is intended to create a standard to help ensure that

³ See Exchange Act Release No. 25637 (May 2, 1988).

⁴ As defined in the Rule 6700 Series, a non-Nasdaq security means any equity security that is neither included in The Nasdaq Stock Market nor traded on any national securities exchange.

members fulfill their best execution responsibilities to customers when engaging in transactions in non-Nasdaq securities, particularly transactions involving relatively illiquid securities with non-transparent prices. The Three Quote Rule is a minimum standard, and compliance with the rule, in and of itself, does not mean a member has met its best execution obligations.

Since the adoption of the Three Quote Rule, the market for non-Nasdaq securities has changed significantly. NASD has found that under certain circumstances, the Three Quote Rule often can hinder, rather than further, investor protection by causing significant delays in obtaining executions of customer orders. For example, in 2000, NASD amended the Three Quote Rule to eliminate the requirement to contact three market makers when there are at least two priced quotations displayed in an inter-dealer quotation system that permits quotation updates on a real-time basis.⁵ NASD concluded that, where there were two transparent, firm quotes, the costs associated with delayed executions resulting from compliance with the Three Quote Rule were not outweighed by the benefits of obtaining three telephone quotes.

Similar concerns have been raised with respect to the Three Quote Rule's application in the area of orders in foreign securities of foreign issuers. Certain members and other interested parties had raised concerns that the Three Quote Rule was unnecessary and potentially harmful to the customer's best interests when a member, using reasonable diligence, has determined that the best market for a foreign security is a foreign market where the securities trade with sufficient liquidity and transparency.

⁵ See Exchange Act Release No. 43319 (September 21, 2000), 65 Fed. Reg. 58589 (September 29, 2000) (File No. SR-NASD-00-20). This rule change also alleviated the corresponding recordkeeping requirements under Rule 3110(b)(2) where NASD could validate and confirm compliance with applicable requirements directly through its internal historical data.

NASD staff agreed that the protections of the Three Quote Rule may not be necessary with respect to all orders in foreign securities. In fact, the SEC, in its approval order granting NASD exemptive authority with respect to the Three Quote Rule, specifically indicated that exemptive relief may be appropriate for transactions executed on a foreign exchange.⁶ The SEC stated that exemptive relief may be appropriate in such circumstances because the foreign exchange may constitute the best market for securities that are listed on that market and the time delay involved in contacting three dealers may, therefore, hinder a member from obtaining best execution for the customers.⁷

Accordingly, NASD is proposing amendments that would exclude from the Three Quote Rule's coverage transactions effected in foreign securities of foreign issuers that are part of the FTSE World Index Series.⁸ The proposed rule change would not require that the transaction be executed on a foreign market so as not to limit the member's ability to determine, in fulfilling its best execution obligations, that a better execution would be obtained off the foreign market. However, to qualify for the exemption, the transaction must be executed during regular business hours of the foreign market for the security and no trading halt or other similar trading or quotation restriction may be in effect in the foreign market for such foreign security.⁹

⁶ See Exchange Act Release No. 39266 (Oct. 22, 1997), 62 Fed. Reg. 56217 (Oct. 29, 1997).

⁷ Id.

⁸ The Financial Times and the London Stock Exchange operate the FTSE World Index Series, which is a subset of the FTSE Global Equity Index Series. The FTSE World Index Series include 30 different countries and approximately 2,381 stocks (approximately 1,744 of which are stocks of foreign issuers). See Exhibit 2 for a detailed description of the criteria used to determine the FTSE World Index.

⁹ Contingent upon approval of the proposed rule change, NASD staff plans to withdraw all existing exemptions it has granted to the Three Quote Rule that relate to foreign securities. NASD staff has granted seven exemptions for customer transactions in Canadian securities executed on a Canadian exchange on an

NASD has selected the FTSE World Index Series in part because the SEC staff has deemed the foreign securities that are listed on this index as having a “ready market” and therefore eligible to receive comparable favorable treatment to U.S. equity securities under the securities haircut¹⁰ provisions of the SEC’s net capital rule.¹¹ In addition, the Federal Reserve Board recognizes this index for determining whether stocks are eligible for margin treatment.¹² NASD believes that the criteria used in determining the composition of the index helps to ensure that the securities trade with a high degree of liquidity, consistency, and price transparency, thereby offering investors with protections similar to that which the Three Quote Rule is intended to provide.

Importantly, while the proposed rule change would not require a member to obtain three quotes in connection with transactions in foreign securities that are part of the FTSE World Index Series, members would continue to be required to comply with their best execution obligations under Rule 2320, and to the extent applicable, their suitability obligations under Rule 2310.

The proposed rule change also would provide a corresponding exclusion to the recordkeeping requirements set forth in Rule 3110(b)(2) relating to the Three Quote Rule if the

agency or riskless principal basis. (See, e.g., Letter to Mr. Kenneth W. Perlman, General Counsel, Mayer Schweitzer, Inc. from Alden S. Adkins, Senior Vice President and General Counsel.)

¹⁰ The SEC’s net capital rule requires broker-dealers, when computing net capital, to deduct from their net worth certain percentages of the market value of their proprietary securities positions, commonly referred to as “haircuts.” Haircuts are calculated under paragraphs (c)(2)(vi), (c)(2)(vii), and applicable appendices of the standard net capital rule, SEC Rule 15c3-1.

¹¹ 1993 SEC No-Act LEXIS 967 (Aug. 13, 1993).

¹² For similar reasons, NASD has a proposal pending at the SEC that would allow members to calculate on their own a higher options position limit without obtaining prior approval from NASD staff for conventional equity options overlying securities listed on the FTSE World Index Series. (See SR-NASD-2004-084)

member can establish and document its reliance on this exclusion. Rule 3110(b)(2) requires that members indicate on the order ticket for each transaction in a non-Nasdaq security the name of each dealer contacted and the quotations received to determine the best inter-dealer market as required by the Three Quote Rule.

In addition, NASD no longer refers to its subsidiary, NASD Regulation, Inc., using its full corporate name, “NASD Regulation” or NASD Regulation, Inc.” Instead, NASD uses “NASD” unless otherwise appropriate for corporate or regulatory reasons. Accordingly, the proposed rule change replaces one reference to “NASD Regulation” in the text of the proposed rule change with “NASD.”

Finally, 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 30 days following publication of the Notice to Members announcing Commission approval.

(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 of trade, and, in general, to protect investors and the public interest. NASD believes that the proposed rule change will reduce the time and effort necessary in contacting three dealers in orders for foreign securities of certain foreign issuers where it has been demonstrated that such securities are trading with sufficient liquidity and price transparency.

(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 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-2004-130. 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

EXHIBIT 2

The FTSE World Index Series is a subset of the FTSE Global Equity Index Series. A summary of the criteria used to construct the FTSE Global Equity Index Series Universe is below.

Criteria for Country inclusion

The following criteria must be met before a country can be included in the FTSE Global Equity Index Series:

- Permission for direct equity investment by non-nationals
- Availability of accurate and timely data
- Non-existence of any significant exchange controls which would prevent the timely repatriation of capital or dividends
- The demonstration of significant international investor interest in the local equity market
- Existence of adequate liquidity in the market

A country's classification as Developed, Advanced Emerging or Emerging is dependent on the following:

<i>Primary Factors</i>	<i>Secondary Factors</i>
• Data quality: availability & timeliness • Free flow of foreign exchange • GDP (per capita) • Market breadth: number of eligible constituents • Market depth: number of industrial sectors • Reliable price information • Stock market capitalization vs GDP • Unrestricted/low restrictions on foreign investment	• Efficient settlement systems • Liquidity – minimum stock market turnover • Market maturity • Membership of economic group or common currency block • Total stock market capitalization

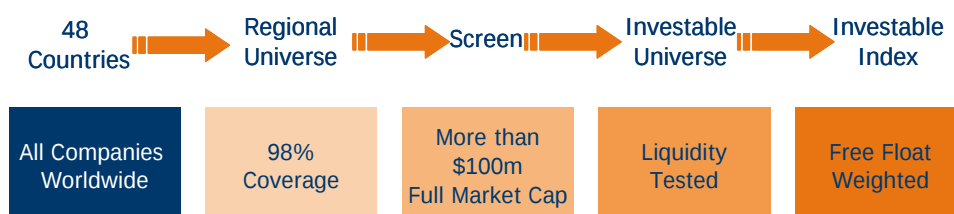
Regional Universe

The 48 eligible countries are grouped into seven Regional Universes. Yearly Index Reviews and the Large, Mid and Small Cap cut are all carried out at regional level.

Regions			
Asia Pacific ex Japan	Developed Europe	Emerging Europe	Japan
Latin America	Middle East & Africa	North America	

Construction Methodology

The stocks in the FTSE All-World Index Series are subjected to four steps to ensure each stock



is eligible to meet investors' needs:

- Coverage** Companies in the bottom 2% of each geographical region (see above) by full market capitalization are excluded. 98% coverage of each region is retained as the universe for constituents of the FTSE Global Equity Index Series.
- Size** Companies with a full market capitalization of less than US\$100 million are excluded.
- Liquidity** Constituents must trade at least 0.5% of their shares in issue in eight out of twelve months prior to review. Non-constituents must trade at least 0.5% of their shares in issue in ten out of twelve months prior to review to enter the index.
- Free Float** Finally, we apply our free float methodology.

Free float	Index weighting
0-5%	Ineligible
>5%-15%	Actual*
>15%-20%	20%
>20%-30%	30%
>30%-40%	40%
>40%-50%	50%
>51%-75%	75%
>75%	100%

* Companies will have actual free float rounded up to the next whole number.

Index Construction

To create the Large, Mid and Small Cap Indices each regional universe is cut as follows:

	Largest/Next	Turnover Bands
--	--------------	----------------

			In	Out
	Large Cap	70%	68%	72%
	Mid Cap	20%	86%	92%
	Small Cap	10%	97%	99%
	Total Index	100%	97%	99%

Regional Reviews

An independent committee of leading market professionals govern the FTSE Global Equity Index Series. Committee members are responsible for deciding on the treatment of complex corporate actions as well as reviews and any necessary changes to the Ground Rules.

The FTSE World Index

The FTSE World Index is made up of those countries with a status of Developed or Advanced Emerging, and those securities classified as Large Cap or Mid Cap.