of specialist registrations in UTP securities to ensure that the Exchange's institutional interests are protected. As proposed, the Market Quality Committee could take certain actions against a UTP specialist if it finds that a UTP specialist's performance is inadequate.

II. Discussion

The Commission finds that the proposed rule change, as amended, is consistent with the Act and the rules and regulations promulgated thereunder applicable to a national securities exchange, and, in particular, with the requirements of section 6(b)[9] of the Act. Specifically, the Commission finds that approval of the proposed rule change is consistent with section 6(b)(5)[10] of the Act because it is designed to promote just and equitable principles of trade, and, in general, to protect investors and the public interest by encouraging good performance and competition among markets and specialists.

Specialists play a crucial role in providing stability, liquidity, and continuity to the trading of securities. Among the obligations imposed upon specialists by the Exchange, and by the Act and the rules thereunder, is the maintenance of fair and orderly markets in their designated securities.[11] To ensure that specialists fulfill these obligations, it is important that the Exchange develop and maintain procedures and policies for monitoring the performance of specialists. Furthermore, it is critical that these procedures and policies explicitly provide for the actions to be taken against specialists whose performance proves to be inadequate. The Commission believes that the proposed rules should provide the Amex with the ability to monitor specialists trading securities pursuant to UTP and take appropriate action in the event that such a specialist's performance proves to be inadequate.

Because the proposed rule change, as amended, institutes a new process for evaluating the performance of specialists that trade securities pursuant to UTP and because the Commission is approving amendments, which relate to the composition of the Market Quality Committee, on an accelerated basis, the Commission believes that the proposal should be approved on a pilot basis through April 5, 2003.[12] The Commission expects the Amex to report to the Commission about its experience with the new performance evaluation process in any future proposal it files to extend the effectiveness of the proposed rule or approve it on a permanent basis.

Moreover, the Commission, pursuant to section 19(b)(2)[13] of the Act, finds good cause for approving Amendment Nos. 3, 4, and 5 prior to the thirtieth day after the date of publication of notice thereof in the **Federal Register**. The Commission believes that granting accelerated approval to Amendment Nos. 3, 4, and 5, on a pilot basis, will enhance immediately the Amex's self-regulatory abilities for the benefit of investors generally. Enhancing such abilities in a timely fashion is critical because Amex UTP specialists currently are trading securities pursuant to UTP and the Amex should be enabled to regulate such activity effectively.

III. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning Amendment Nos. 3, 4, and 5, including whether the amendments are consistent with the Act. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549–0609. 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 the Amex. All submissions should refer to File No. SR–Amex–2002–19 and should be submitted by November 29, 2002.

IV. Conclusion

It is therefore ordered, pursuant to section 19(b)(2) of the Act,[14] that the proposed rule change (SR–Amex–2002–19), as amended, is hereby approved on a pilot basis through April 5, 2003.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.[15]

Margaret H. McFarland,

Deputy Secretary.

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[9] 15 U.S.C. 78f(b). In approving this proposal, the Commission has considered the proposed rule's impact on efficiency, competition and capital formation. 15 U.S.C. 78c(f).

[10] 15 U.S.C. 78f(b)(5).

[11] *See* 17 CFR 240.11b–1.

[12] The Commission notes that this is the date on which the UTP Allocations Committee Pilot will expire.

[13] 15 U.S.C. 78s(b)(2).

[14] 15 U.S.C. 78s(b)(2).

[15] 17 CFR 200.30–2(a)(12).

SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–46757; File No. SR–NASD–2002–155]

Self-Regulatory Organizations; National Association of Securities Dealers, Inc.; Notice of Filing and Immediate Effectiveness of a Proposed Rule Change to Extend a Pilot That Permits SuperSOES to Trade Through the Quotations of UTP Exchanges That Do Not Participate in the Nasdaq National Market Execution Service

October 31, 2002.

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 October 31, 2002, the National Association of Securities Dealers, Inc. (''NASD''), acting through its subsidiary, The Nasdaq Stock Market, Inc. (''Nasdaq''), filed with the Securities and Exchange Commission (''SEC'' or ''Commission'') the proposed rule change as described in Items I and II below, which Items have been prepared by the NASD. The NASD filed the proposal pursuant to section 19(b)(3)(A)[3] of the Act, and Rule 19b–4(f)(6) thereunder,[4] which renders the proposal effective on filing with the Commission.[5] 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

There is no new language. The pilot rule language is as follows:

4710. Participant Obligations in NNMS

(a)–(e) No Change.

(f) UTP Exchanges.

(i) A UTP Exchange may voluntarily participate in the NNMS System according to the approved rules for the

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

[2] 17 CFR 240.19b–4.

[3] 15 U.S.C. 78s(b)(3)(A).

[4] 17 CFR 240.19b–4(f)(6).

[5] Nasdaq asked the Commission to waive the 5-day pre-filing notice requirement and the 30-day operative delay. See Rule 19b–4(f)(6)(iii), 17 CFR 240.19b–4(f)(6)(iii).

NNMS System if it executes a Nasdaq Workstation Subscriber Agreement, as amended, for UTP Exchanges.

(ii) If a UTP Exchange does not participate in the NNMS System, the UTP Exchange's quote will not be accessed through the NNMS, and the NNMS will not include the UTP Exchange's quotation for order processing and execution purposes.

(iii) For purposes of this rule the term ''UTP Exchange'' shall mean any registered national securities exchange that has unlisted trading privileges in Nasdaq-listed securities pursuant to the Joint Self-Regulatory Organization Plan Governing the Collection, Consolidation and Dissemination Of Quotation and Transaction Information For Exchange-Listed Nasdaq/National Market System Securities Traded On Exchanges On An Unlisted Trading Privilege Basis (''Nasdaq UTP Plan'').

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

In its filing with the Commission, the 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. Nasdaq 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 [6]

Nasdaq is proposing to extend an existing pilot, which specifies that if a UTP Exchange elects not to participate in SuperSOES, SuperSOES will not include the UTP Exchange's quotation for order processing and execution purposes.[7] Nasdaq believes that this will be the final extension of this pilot for the SuperSOES system because Nasdaq anticipates completing its transition to the Nasdaq Order Display and Collection Facility, commonly known as ''SuperMontage,'' in early December of 2002. Nasdaq seeks to extend the pilot until February 28, 2003, or until Nasdaq completes the transition of its execution systems from SuperSOES to SuperMontage whichever is earlier. Rule language effectuating this pilot program is already in place for SuperMontage.[8]

Background. On January 14, 2000, the Commission approved a rule change to establish the Nasdaq National Market Execution System (''NNMS'') and to modify Nasdaq's SelectNet Service with respect to Nasdaq National Market (''NNM'') securities.[9] On July 30, 2001, NNMS and the changes to SelectNet were implemented for all NNM issues. As approved and implemented, Nasdaq market participants can use two systems to trade NNM issues: a reconfigured Small Order Execution System (''SOES'')—the NNMS—and a reconfigured SelectNet system. SuperSOES is an automated execution system that allows the entry of orders for up to 999,999 shares.[10] By removing the size and capacity restrictions from its principal automatic execution system, Nasdaq intended for most of the orders executed through Nasdaq's systems to migrate to SuperSOES. Consistent with that approach, access to SelectNet was limited to certain types of non-liability orders that require negotiation with the receiving market participant.[11]

As was the case with SOES, Nasdaq market makers are required to participate in SuperSOES and, therefore, to accept automatic execution against their displayed quotations. However, UTP Exchanges are not required to accept automatic executions. Whereas Nasdaq can require, by rule, that its member ECNs provide immediate response to an inbound SelectNet order, it has no authority to extend that requirement to a UTP Exchange. As a result, without the implementation of the instant pilot, if a UTP Exchange was alone at the best bid/best offer for a particular security, that UTP Exchange could cause SuperSOES to stop processing orders in that security and hold those orders in queue for up to 90 seconds.

In such a case, if after 90 seconds, a SuperSOES market participant did not join the current best bid/best offer, or the UTP Exchange did not move its quote, SuperSOES would return the orders that were in queue and the system would shut down for that security. The system would only resume once the UTP Exchange moved its quote away from the inside. Nasdaq believes that such delays would adversely affect Nasdaq's ability to ensure the proper functioning of its market through a major Nasdaq market system, and to enable market participants to obtain executions for their customers.

Pilot Description. To address these problems, Nasdaq proposed, and the Commission approved, a pilot to amend NASD Rule 4710 to require that UTP Exchanges that choose to trade Nasdaq securities through Nasdaq market systems either participate fully in the automatic executions through SuperSOES, or have their quotations removed from the SuperSOES execution and order processing functionality. Specifically, if a UTP Exchange elects not to participate in SuperSOES, SuperSOES will trade through the UTP Exchange's quote. Nasdaq believes that this should prevent a UTP Exchange that is not otherwise accessible via SuperSOES from effectively shutting down the market in that security. [12]

UTP Exchanges that choose not to participate in SuperSOES would be accessible by telephone as contemplated in the Nasdaq UTP Plan,[13] or via a mutually agreed-upon alternative bilateral link created by the UTP Exchange.[14] Nasdaq welcomes the opportunity to explore the possibility of bilateral linkages, which Nasdaq anticipates could be formed via separate agreement between Nasdaq and the exchange(s).

Nasdaq proposed the pilot for a number of reasons. First, significant changes in market conditions have resulted in the need for Nasdaq, via SuperSOES, to increase the speed of

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[6] The NASD requested that the Commission correct various verbiage inconsistencies and delete extraneous purpose language from the proposal. Telephone discussion between Jeffrey S. Davis, Associate General Counsel, Nasdaq, and Terri Evans, Assistant Director, and Christopher Stone, Attorney, Division of Market Regulation, Commission (October 31, 2002).

[7] The temporary approval of the pilot expires October 31, 2002. *See* Exchange Act Release No. 46016 (May 31, 2002), 67 FR 39457 (June 7, 2002).

[8] *See* Securities Exchange Act Release No. 46343 (August 13, 2002), 67 FR 53822 (August 19, 2002).

[9] *See* Exchange Act Release No. 42344 (January 14, 2000), 65 FR 3987 (January 25, 2000).

[10] SOES was limited to small agency orders for customers.

[11] As originally proposed, market participants were permitted to enter into the modified SelectNet only: (1) Those orders that specify a minimum acceptable quantity for a size that is at least 100 shares greater than the posted quote of the receiving market participant; or (2) All-or-None orders that are at least 100 shares in excess of the displayed bid/offer size. Since the original proposal, the SEC has also approved the entry of non-liability, inferior-priced orders through SelectNet.

[12] The Nasdaq UTP Plan governs the trading of Nasdaq-listed securities pursuant to unlisted trading privileges. Subsection (b) of Section IX of the Nasdaq UTP Plan states, in pertinent part, that Plan participants ''shall have direct telephone access to the trading desk of each Nasdaq market participant in each [e]ligible [s]ecurity in which the [p]articipant displays quotations.'' *See* Section IX, Market Access, of the Nasdaq UTP Plan.

[13] We note that this currently is the method that the Cincinnati Stock Exchange has elected to use for trading Nasdaq securities under the Nasdaq UTP Plan.

[14] This proposal would not preclude a UTP Exchange from forming a link with Nasdaq outside Nasdaq's market system or the parameters of an NMS plan.

executions and improve the access of all market participants to the full depth of a security's trading interest. The volume and speed at which trading occurs in Nasdaq have increased dramatically since SuperSOES was first proposed nearly two and a half years ago. Market participants demand and require the ability to access liquidity at the best prices instantaneously. SuperSOES is a significant improvement over prior Nasdaq execution systems, and has become the backbone of Nasdaq's marketplace by providing market participants with a more efficient trading platform as evidenced by faster executions, higher fill rates, larger orders, and prices at the best bid or best offer.

Nasdaq wants to ensure that the market in a particular security does not shut down—thereby harming investors and the market—if there is an unresponsive UTP Exchange setting the current best bid/best offer for that security. Nasdaq recognizes the importance of maintaining price priority and ensuring that market participants receive the best possible price in the market. As such, SuperSOES was originally designed not to trade through the best quote that appears in the Nasdaq montage. However, that premise assumed all quotes would be immediately accessible.[15] SuperSOES must be able to continue operating when a particular quote is not accessible by market participants. To that end, if a UTP Exchange chooses not to participate in SuperSOES, and that UTP Exchange sets the inside bid or ask, Nasdaq will enable SuperSOES not to include that UTP Exchange's quotation for order processing and execution.

Participation in SuperSOES by a UTP Exchange is a voluntary action by each exchange. Nasdaq is not obligated to provide UTP Exchanges with access to any of Nasdaq's proprietary systems. Nasdaq's voluntary action, designed to improve efficiency and maintain an orderly market, should not become an opportunity for a Nasdaq competitor to harm the ability of Nasdaq to improve its markets.

Overall, Nasdaq believes it was appropriate to alter the terms under which a UTP Exchange participates in The Nasdaq Stock Market to address all of the concerns described in this proposal. For the same reasons, it is important to continue the pilot program to preserve the status quo as additional UTP Exchanges prepare to commence trading Nasdaq securities.

2. Statutory Basis

Nasdaq believes that the proposed rule change is consistent with the provisions of section 15A(b)(6) of the Act,[16] in that the proposal is designed to facilitate transactions in securities, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest. In particular, Nasdaq believes that modifying SuperSOES to trade through quotations of non-automatic execution UTP Exchanges is necessary for the fair and orderly operation of The Nasdaq Stock Market by helping to reduce the potential for order queuing or for system stoppages, when a UTP Exchange's quote is inaccessible and is alone at the best bid or best offer.

B. Self-Regulatory Organization's Statement on Burden on Competition

Nasdaq 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

Because the foregoing proposed rule change does not:

(i) Significantly affect the protection of investors or the public interest;

(ii) impose any significant burden on competition; and

(iii) become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate, it has become effective pursuant to section 19(b)(3)(A) of the Act[17] and Rule 19b–4(f)(6), thereunder.[18] At any time within 60 days of the filing of the proposed rule change, the Commission may summarily abrogate the rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act.

Nasdaq has requested that the Commission waive the 5-day pre-filing notice requirement and the 30-day operative delay. The Commission believes that waiving both the 5-day pre-filing notice requirement and the 30-day operative delay is consistent with the protection of investors and the public interest. Acceleration of the operative date will permit the NASD pilot to continue in operation without interruption. Nasdaq states that the pilot reduces the potential for a shut down in Nasdaq's automatic execution systems. Nasdaq's inability to maintain the status quo during that period would create unnecessary, harmful uncertainty. For these reasons, the Commission designates the proposal to be effective and operative upon filing with the Commission.[19]

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposal is consistent with the Act. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 Fifth Street, NW., Washington, DC 20549–0609. 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 the filing will also be available for inspection and copying at the principal office of the NASD. All submissions should refer to File No. SR–NASD–2002–155 and should be submitted by November 29, 2002.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.[20]

Margaret H. McFarland,

Deputy Secretary.

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[15] Order Entry ECNs are not subject to inbound automatic executions in SuperSOES. However, as NASD members, Order Entry ECNs are subject to NASD Rules and the enforcement and disciplinary powers granted therein. As non-members, UTP Exchanges are not subject to the same regulatory infrastructure.

[16] 15 U.S.C. 78*o*–3(b)(6).

[17] 15 U.S.C. 78s(b)(3)(A).

[18] 17 CFR 240.19b–4(f)(6).

[19] For purposes only of accelerating the operative date of this proposal, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

[20] 17 CFR 200.30–3(a)(12).