

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-54613; File No. SR-NASDAQ-2006-043)

October 17, 2006

Self-Regulatory Organizations; The NASDAQ Stock Market LLC; Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Modify the Operations of its Recently-Approved “Single Book” Execution System

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 10, 2006, The NASDAQ Stock Market LLC (“Nasdaq”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I and II below, which Items have been prepared by Nasdaq. Nasdaq has filed the proposal pursuant to Section 19(b)(3)(A) of the Act³ and Rule 19b-4(f)(6) thereunder,⁴ which renders the proposal effective upon filing with the Commission. 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

Nasdaq proposes to modify the operations of its recently-approved “Single Book” execution system.⁵ Nasdaq states that, through quality control and testing, and feedback from the trading community, it has identified five modifications to the operation and rules governing the Single Book system that would improve the fair and orderly operation of the Nasdaq market.

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 Securities Exchange Act Release No. 54155 (July 14, 2006), 71 FR 41291 (July 20, 2006) (File No. SR-NASDAQ-2006-001) (approving the “Single Book Proposal”). See also Securities Exchange Act Release No. 53583 (March 31, 2006), 71 FR 19573 (April 14, 2006) (File No. SR-NASDAQ-2006-001) (“Single Book Proposal”).

Specifically, Nasdaq is proposing five changes: (1) establishing a Pegged Order based upon changes to the Nasdaq Market Center inside, an order type that is currently available in the Nasdaq Market Center; (2) clarifying how certain order routing strategies would operate with respect to the New York Stock Exchange (“NYSE”) and American Stock Exchange (“Amex”) markets; (3) eliminating vestigial references to individual Nasdaq market participants – as opposed to the Nasdaq exchange – participating in the ITS system; (4) adopting the adjustment of open orders process currently approved and in use in the Nasdaq Market Center, rather than the one currently used in the INET system; and (5) reflecting the changes to the Nasdaq rules that have been approved since the Single Book Proposal was approved on July 14, 2006.

Nasdaq has designated this proposal as non-controversial. Nasdaq has requested that the Commission waive the 30-day pre-operative waiting period contained in that rule. Nasdaq states that, if such waiver is granted by the Commission, this rule proposal, which is effective upon filing with the Commission, would become operative upon the launch of the Single Book execution system (which Nasdaq currently expects to occur on October 16, 2006), pursuant to Exchange Act Rule 19b-4(f)(6). Below is the text of the proposed rule change. Proposed new language is underlined and proposed deletions are in [brackets].

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4120. Trading Halts

(a) No Change.

(b) Procedure for Initiating a Trading Halt

(1) – (6) No Change.

(7) (A) A trading halt initiated under Rule 4120(a)(1), (4), (5) or (6) shall be terminated when Nasdaq releases the security for trading. Prior to terminating the halt, there will

be a 5-minute [Quotation] Display Only Period during which market participants may enter quotations and orders in that security in Nasdaq systems. At the conclusion of the 5-minute [Quotation] Display Only Period, the security shall be released for trading unless Nasdaq extends the [Quotation] Display Only Period for an additional 1-minute period pursuant to subparagraph (C) below. There shall be a period of between zero and 15 seconds (randomly selected) at which point the [Quotation] Display Only Period shall end and trading shall resume pursuant to Rule [4703] 4753.

(B) A trading halt initiated under Rule 4120(a)(7) shall be terminated when Nasdaq releases the security for trading. Prior to terminating the halt, there will be a 15-minute [Quotation] Display Only Period during which market participants may enter quotes and orders in that security in Nasdaq systems. At the conclusion of the 15-minute [Quotation] Display Only Period, the security shall be released for trading unless Nasdaq extends the [Quotation] Display Only Period for one, two or three additional 5-minute [Quotation] Display Only Periods pursuant to subparagraph (C) below. At the conclusion of the [Quotation] Display Only Period(s), there shall be an additional delay of between zero and 15 seconds (randomly selected) and then trading shall resume pursuant to Rule [4703] 4753.

(C) If at the end of a [Quotation] Display Only Period, Nasdaq detects a Liquidity Imbalance in the security, Nasdaq will extend the [Quotation] Display Only Period as permitted under subparagraphs (A) and (B) above. Liquidity Imbalances shall be established when: 1) the Current Reference Prices, as defined in Rule 4752(a)(2)(A), disseminated 15 seconds and immediately prior to the end of the Display Only Period differ by greater than (i) 10 percent or (ii) 50 cents (whichever is greater), or 2) all buy or sell market orders will not be executed in the cross.

[1. the Inside Match Prices, as defined in Rule 4703(a)(2), disseminated 15 seconds and immediately prior to the end of the Quotation Only Period differ by greater than (i) 10 percent or (ii) 50 cents (whichever is greater); or

2. the Halt Cross would execute at a price at which higher-priced marketable orders to buy or lower-priced marketable orders to sell would remain unexecuted.]

(8) No Change.

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4751. Definitions

(a) – (e) No Change.

(f) The term “Order Type” shall mean the unique processing prescribed for designated orders that are eligible for entry into the System, and shall include:

(1) – (3) No Change.

(4) “Pegged Orders” are orders that, after entry, has their price automatically adjusted by the System in response to changes in either the Nasdaq Market Center inside bid or offer or bids or offers in the national market system, as appropriate. A Pegged Order can specify that its price will equal the inside quote on the same side of the market (“Primary Peg”) or the opposite side of the market (“Market Peg”). A Pegged Order may have a limit price beyond which the order shall not be executed. In addition, Pegged Orders may also establish their pricing relative to the appropriate bids or offers by the selection of one or more offset amounts that will adjust the price of the order by the offset amount selected. A new timestamp is created for the order each time it is automatically adjusted.

(5) – (8) No Change.

(g) – (i) No Change.

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4758. Order Routing

(a) Order Routing Process

(1) The Order Routing Process shall be available to Participants from 7:00 a.m. until 8:00 p.m. Eastern Time, and shall route orders as described below:

(A) Exchange-Listed Routing Options. The System provides four routing options for orders in exchange-listed securities. Of these four, only DOT is available for orders ultimately sought to be directed to either the New York Stock Exchange (“NYSE”) or the American Stock Exchange (“AMEX”). The System also allows firms to send individual orders to the NYSE Direct + System, and to elect to have orders not be sent to the AMEX. Except as noted below in SPDY, routed pegged orders in securities listed on another exchange, the System will consider the quotations of accessible markets. The four System routing options for NYSE and/or Amex listed orders are:

(i) No Change.

(ii) Reactive Electronic Only (“STGY”) – under this option, after checking the System for available shares, orders are sent to other available market centers for potential execution, per entering firm’s instructions. When checking the book, the System will seek to execute at the price it would send the order to a destination market center. If shares remain unexecuted after routing, they are posted on the book [and are not sent to the NYSE or AMEX]. Once on the book, should the order subsequently be locked or crossed by another accessible market center, the System shall route the order to the locking or crossing market center for potential execution in order to resolve the locked or crossed market. With the exception of the Minimum Quantity order type, all time-in-force parameters and order types may be used in

conjunction with this routing option. This process is one of the routing strategies allowed by the System for all securities.

(iii) Electronic Only Scan (“SCAN”) – under this option, after checking the System for available shares, orders are sent to other available market centers for potential execution, per entering firm’s instructions. When checking the book, the System will seek to execute at the price it would send the order to a destination market center. If shares remain un-executed after routing, they are posted on the book [and are not sent to the NYSE or AMEX]. Once on the book, should the order subsequently be locked or crossed by another market center, the System will not route the order to the locking or crossing market center. With the exception of the Minimum Quantity order type, all time-in-force parameters and order types may be used in conjunction with this routing option. This process is one of the routing strategies allowed by the System for all securities and shall be used for routing ITS Commitments.

(iv) Aggressive Electronic Only (“SPDY”) – under this option, after checking the System for available shares, orders are sent to other available market centers for potential execution, per entering firm’s instructions. When checking the book, the System will seek to execute at the price it would send the order to a destination market center. If shares remain un-executed after routing, they are posted on the book [and are not sent to the NYSE or AMEX]. Once on the book, should the order subsequently be locked or crossed by another accessible market center, the System shall route the order to the locking or crossing market center for potential execution in order to resolve the locked or crossed market. Market orders with the SPDY designation will, during a locked or crossed market, have their price adjusted by the System to match the best price displayed on the same side of the market as the market order (i.e., a buy order to the bid, a sell to the offer). If the order is for a security eligible for a de

minimis exception to the trade-through rule set forth in Section 8 (d)(i) of the ITS Plan, the System will ignore AMEX prices when adjusting the SPDY order during a locked or crossed market. With the exception of the Minimum Quantity order type, all time-in-force parameters and order types may be used in conjunction with this routing option. This process is one of the routing strategies allowed by the System for all securities.

(B) – (C) No Change.

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4759. ITS Commitments

Until such time as Nasdaq withdraws from the ITS Plan, Quotes and Orders that are eligible for ITS will be processed by the System and routed to the appropriate Non-Nasdaq Participant Market as an ITS Commitment in accordance with the requirements of the ITS Plan and all applicable Nasdaq rules. Nasdaq shall participate in the ITS Plan as set forth below.

(a) No Change.

(b) Inbound ITS Commitments

(1) If the ITS Commitment contains an obvious error, the Nasdaq Market Center will decline it. For purposes of this Rule, a transaction may have an obvious error in any term, such as price, number of shares or other unit of trading, or identification of the security[, or if a specific commitment to trade has been executed with the wrong Nasdaq Market Maker].

(2) – (3) No Change.

(c) Outbound Commitments: Any “commitment to trade,” which is transmitted by [an]Nasdaq [Participant]to another Non-Nasdaq ITS Participant Market through ITS, shall be firm and irrevocable for the period of thirty seconds following transmission by the sender. All such commitments to trade shall, at a minimum:

(1) – (6) No Change.

(d) No Change.

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4761. Adjustment of Open Quotes and/or Orders

[The Nasdaq Market Center will automatically purge all open quotes and/or orders in all Nasdaq Market Center eligible securities resident in the system in response to issuer corporate actions related to a dividend, payment or distribution, on the ex-date of such actions, except where a cash dividend or distribution is less than one cent (\$0.01).]

The Nasdaq Market Center will automatically adjust the price and/or size of open quotes and/or orders in all Nasdaq Market Center eligible securities (unless otherwise noted) resident in the system in response to issuer corporate actions related to a dividend, payment or distribution, on the ex-date of such actions, except where a cash dividend or distribution is less than one cent (\$0.01), as follows:

(a) Quotes — All bid and offer side quotes shall be purged from the system.

(b) Sell Orders — Sell side orders in Nasdaq-listed and NYSE-listed securities shall not be adjusted by the system and must be modified, if desired, by the entering party, except for reverse splits where such sell side orders shall be purged from the system. Sell side orders in Amex-listed securities shall be adjusted in accordance with the procedures set forth below for Buy Orders in the event of a Stock Dividend or Stock Split.

(c) Buy Orders — Buy side orders shall be adjusted by the system based on the particular corporate action impacting the security (i.e. cash dividend, stock dividend, both, stock split, reverse split) as set forth below:

(1) Odd lot orders in ITS Securities that result from partial execution rather than order entry shall be canceled rather than adjusted.

(2) Cash Dividends: Buy side order prices shall be first reduced by the dividend amount and the resulting price will then be rounded down to the nearest penny unless marked “Do Not Reduce”.

(3) Stock Dividends and Stock Splits: Buy side order prices shall be determined by first rounding up the dollar value of the stock dividend or split to the nearest penny. The resulting amount shall then be subtracted from the price of the buy order. Unless marked “Do Not Increase”, the size of the order shall be increased by first, (A) multiplying the size of the original order by the numerator of the ratio of the dividend or split, then (B) dividing that result by the denominator of the ratio of the dividend or split, then (C) rounding that result to the next lowest share.

(4) Dividends Payable in Either Cash or Securities at the Option of the Stockholder: Buy side order prices shall be reduced by the dollar value of either the cash or securities, whichever is greater. The dollar value of the cash shall be determined using the formula in paragraph (2) above, while the dollar value of the securities shall be determined using the formula in paragraph (3) above. If the stockholder opts to receive securities, the size of the order shall be increased pursuant to the formula in subparagraph (3) above.

(5) Combined Cash and Stock Dividends/Split: In the case of a combined cash dividend and stock split/dividend, the cash dividend portion shall be calculated first as per section (1) above, and stock portion thereafter pursuant to sections (2) and/or (3) above.

(6) Reverse Splits: All orders (buy and sell) shall be cancelled and returned to the entering firm.

(d) Open buy and sell orders that are adjusted by the system pursuant to the above rules, and that thereafter continuously remain in the system, shall retain the time priority of their original entry.

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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, Nasdaq 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

On July 14, 2006, the Commission approved SR-NASDAQ-2006-001,⁶ a proposal to create an integrated execution facility – the “Single Book” – from Nasdaq’s three current facilities: the Nasdaq Market Center⁷; the Brut ECN; and the INET ECN. Nasdaq states that, through quality control and testing, and feedback from the Nasdaq community, it has identified five minor modifications to the operation and rules governing the Single Book that would improve the fair and orderly operation of the Nasdaq market.

(1) Nasdaq is proposing to modify Nasdaq Rule 4751(f)(4) to re-establish a Pegged Order based upon changes to the Nasdaq Market Center inside, an order type that is currently available

⁶ See supra note 5.

⁷ References to the Nasdaq Market Center refer to the current NASDAQ execution system as opposed to the future execution system.

in the Nasdaq Market Center.⁸ As stated in Amendment 1 to the Single Book Proposal, Nasdaq originally focused on providing order types then available in the INET system, including Pegged Orders pegged to quotes and orders in the national market system other than in Nasdaq.⁹ Nasdaq has determined that the having the ability to choose between Pegged Order based upon changes to the Nasdaq inside quotation or changes to the national best bid or offer would be a valuable tool for Nasdaq participants and that it would be relatively simple to revise this order type in the Single Book. Nasdaq states that the proposed Pegged Order would operate exactly as it is currently approved in the Nasdaq Market Center.

(2) Nasdaq is proposing to eliminate language from Nasdaq Rule 4758(a)(1)(A)(ii), (iii), and (iv) that Nasdaq states improperly indicates that orders in NYSE and Amex securities will not be routed to the NYSE and Amex. In fact, after NYSE and Amex have implemented their anticipated electronic trading platforms, Nasdaq states that those routing strategies – STGY, SCAN, and SPDY – may result in an order being routed to those markets. However, as stated in paragraph (a)(1)(A) of that rule, only the DOT routing strategy is used for orders that are directed by a participant to those markets. In addition, Nasdaq is proposing to add language to paragraph (a)(1)(A)(iii) stating that the SCAN routing strategy would be used to route Intermarket Trading System (“ITS”) commitments to the appropriate ITS exchanges.

(3) When Nasdaq begins operating as a national securities exchange for the purposes of trading NYSE and Amex securities, it will do so as a consolidated whole rather than as a collection of individual market participants. In the Single Book Proposal, Nasdaq systematically eliminated most references to individual market participant conduct in the System. It appears, however, that Nasdaq failed to eliminate several vestigial references in Nasdaq Rule 4759(c) to

⁸ See Nasdaq Rule 4701(mm).

⁹ See Nasdaq Rule 4951(q) and Single Book Proposal at 19592.

individual Nasdaq market participants – as opposed to the Nasdaq exchange – participating in the ITS system. Nasdaq is proposing to eliminate those references now, without otherwise changing that rule or Nasdaq’s obligations under the ITS Plan.

(4) In the Single Book Proposal, Nasdaq proposed to adopt via Nasdaq Rule 4761 the INET process of purging open orders when a corporate event such as a stock split or dividend occurred, and to abandon the Nasdaq Market Center methodology for adjusting such open orders. After further dialogue with industry participants, Nasdaq has determined that many Nasdaq members prefer the current Nasdaq Market Center methodology for adjusting open orders rather than purging them because those members have not programmed their systems to adjust such orders themselves. By adopting the existing Nasdaq Market Center rule, Nasdaq Rule 4715, Nasdaq states that it would be relieving members of the burden of reprogramming their systems because the adjustment of orders will occur automatically within Nasdaq’s system. Nasdaq believes it can modify this rule without burdening any of its other members because members that do not want Nasdaq to adjust their open orders in the event of a corporate action can choose simply to cancel their open orders at the end of the trading day.

(5) On July 28, 2006, Nasdaq submitted SR-NASDAQ-2006-019 which modified, among others, Nasdaq Rule 4120.¹⁰ Nasdaq states that these modifications took effect on August 1, 2006, when Nasdaq began operating as a national securities exchange. In order to create a fully-transparent record of the development of the Nasdaq rule manual, Nasdaq believes it is necessary to demonstrate how the current rule, including the changes established in SR-NASDAQ-2006-019, differ from the rule approved in the Single Book Proposal and how the current rule would change when the Single Book system is implemented. Therefore, Nasdaq is proposing to modify

¹⁰ Securities Exchange Act Release No. 54248 (July 31, 2006), 71 FR 44738 (August 7, 2006) (File No. SR-NASDAQ-2006-019).

the Nasdaq rule currently in effect to reflect changes that have already been approved in connection with the Single Book Proposal or that are required for use when the Single Book System is operational. Nasdaq states that the proposed changes to Nasdaq Rule 4120 are designed to re-establish the rule language already approved with respect to the Single Book Proposal and are therefore non-substantive.

2. Statutory Basis

Nasdaq believes that the proposed rule change is consistent with the provisions of Section 6 of the Act,¹¹ in general, and with Sections 6(b)(5) of the Act,¹² in particular, in that the proposal is designed to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating 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; and are not designed to permit unfair discrimination between customers, issuers, brokers, or dealers, or to regulate by virtue of any authority conferred by the Act matters not related to the purposes of the Act or the administration of the exchange.

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.

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.

¹¹ 15 U.S.C. 78f.

¹² 15 U.S.C. 78f(b)(5).

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

The foregoing proposed rule change is subject to Section 19(b)(3)(A)(iii) of the Act¹³ and Rule 19b-4(f)(6) thereunder¹⁴ because the proposal: (i) does not significantly affect the protection of investors or the public interest; (ii) does not impose any significant burden on competition; and (iii) does not become operative prior to 30 days after the date of filing or such shorter time as the Commission may designate if consistent with the protection of investors and the public interest; provided that Nasdaq has given the Commission notice of its intent to file the proposed rule change, along with a brief description and text of the proposed rule change, at least five business days prior to the date of filing of the proposed rule change, or such shorter time as designated by the Commission. Nasdaq states that it would make this rule proposal operative upon the launch of the Single Book system.

Nasdaq has satisfied the five-day pre-filing requirement and has requested that the Commission waive the 30-day pre-operative delay. Nasdaq states that it has carefully planned a detailed and thorough testing and roll-out schedule for the Single Book system, and has coordinated that schedule with numerous industry participants. Nasdaq states that to disrupt that schedule would cause substantial inconvenience for all involved and delay the launch of a process that Nasdaq believes would dramatically improve the Nasdaq Stock Market, whereas a delay would benefit none. The Commission believes that this proposal contains modifications to the Single Book rules that provide useful clarifications or represent modifications substantially similar to rules currently in effect at Nasdaq. The Commission believes that waiving the 30-day pre-operative delay is consistent with the protection of investors and the public interest because such waiver would permit Nasdaq to begin operation of its Single Book system under its current

¹³ 15 U.S.C. 78s(b)(3)(A)(iii).

¹⁴ 17 CFR 240.19b-4(f)(6).

roll-out schedule. For this reason, the Commission designates the proposed rule change to be effective upon filing with the Commission.¹⁵ The Commission notes that Nasdaq intends to make the proposed rule changes operative upon the launch of the Single Book execution system.

At any time within 60 days of the filing of such proposed rule change the Commission may summarily abrogate such 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.

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. Comments may be submitted by any of the following methods:

Electronic comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to rule-comments@sec.gov. Please include File Number SR-NASDAQ-2006-043 on the subject line.

Paper comments:

- Send paper comments in triplicate to Nancy M. Morris, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-NASDAQ-2006-043. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all

¹⁵ For the purposes only of waiving the 30-day pre-operative delay, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

comments on the Commission's Internet Web site (<http://www.sec.gov/rules/sro.shtml>). 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 also will be available for inspection and copying at the principal office of Nasdaq. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-NASDAQ-2006-043 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹⁶

Nancy M. Morris
Secretary

¹⁶ 17 CFR 200.30-3(a)(12).