SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-52723; File No. SR-NASD-2005-128)

November 2, 2005

Self-Regulatory Organizations; National Association of Securities Dealers, Inc.; Notice of Filing of Proposed Rule Change to Establish Rules Governing the Operation of the INET 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 November 1, 2005, the National Association of Securities Dealers, Inc. ("NASD"), through its subsidiary, The Nasdaq Stock Market, Inc. ("Nasdaq"), filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by Nasdaq. 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 the Substance of the Proposed Rule Change

Nasdaq intends to purchase INET ATS, Inc. ("INET"), operator of the INET ECN (the "INET System" or "System"). Nasdaq proposes to establish rules governing the operation of the INET System and fees for System services. Below is the text of the proposed rule change. Proposed new language is underlined.

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

[2]   17 CFR 240.19b-4.

4950. INET SYSTEM

4951. Definitions

Unless stated otherwise, the terms described below shall have the following meaning:

(a) The terms "The INET ECN System," "INET System," or "System," shall mean the automated system owned and operated by INET, which is owned and operated by The Nasdaq Stock Market, Inc., which enables Participants to execute transactions in System securities, to have reports of the transactions automatically forwarded to the appropriate National Market Trade Reporting System for dissemination to the public and the industry, to "lock in" these trades by sending both sides to the applicable clearing corporation(s) designated by the System Participant(s) for clearance and settlement, and to provide System Participants with sufficient monitoring and updating capability to participate in an automated execution environment.

(b) The term "System Securities" shall mean Nasdaq Market Center eligible securities as that term is defined in NASD Rule 4701(s) and ITS Securities securities as defined in NASD Rule 5210(c).

(c) The term "Participant" shall mean an entity that fulfills the obligations contained in NASD Rule 4952 regarding participation in the System.

(d) The term "Nasdaq Market Center" shall mean the automated system owned and operated by The Nasdaq Stock Market, Inc. pursuant to NASD Rule 4700 Series.

(e) The term "System Book Feed" shall mean a data feed for System eligible securities.

(f) The term "normal unit of trading" shall mean one hundred (100) shares.

(g) The term "mixed lot" shall mean an order that is for more than a normal unit of trading but not a multiple thereof.

(h) The term "odd-lot" shall mean an order that is for less than a normal unit of trading.

(i) The term "Immediate or Cancel" or "IOC" shall mean, for limit orders so designated, that if after entry into the System the order (or a portion thereof) is not marketable, the order (or unexecuted portion thereof) shall be canceled and returned to the entering Participant.

(j) The term "Market Day" or "Limit Day" shall mean, for orders so designated, that if after entry into the System, the order is not fully executed, the order (or the unexecuted portion thereof) shall remain available for potential display/execution until 4:00 p.m. Eastern Time on the day it was submitted unless cancelled before then by the entering party.

(k) The term "Extended Day" shall mean, for orders so designated, that if after entry into the System, the order is not fully executed, the order (or unexecuted portion thereof) shall remain available for potential display and/or execution until 8:00 p.m. Eastern Time.

(l) The term "Expire Time" shall mean, for orders so designated, the time until which the System will hold the order for potential execution.

(m) The term "Limit Order" shall mean an order to buy or sell a stock at a specified price or better.

(n) The term "Market Order" shall mean an un-priced order to buy or sell a stock at the market's current best price. A Market Order may have a limit price beyond which the order shall not be executed.

(o) The term "Discretionary Order" shall mean an order that has both a displayed price and size, as well as a non-displayed discretionary price range, at which the entering party, if necessary, is also willing to buy or sell. The non-displayed trading interest is not entered into the System book but is converted to an IOC order equal in size to the displayed size and priced at the most aggressive price in the discretionary price range when displayed shares become available or an execution takes place at any price within the discretionary price range. The generation of this

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IOC order is accompanied by the cancellation of the displayed portion of the Discretionary Order. If more than one Discretionary Order is available for conversion to an IOC order, the system will convert all such orders at the same time and priority will be given to the first IOC order(s) that reaches the trading interest on the other side of the market. If an IOC order is not executed in full, the unexecuted portion of the order is automatically re-posted and displayed in the System book with a new time stamp, its original displayed price, and its non-displayed discretionary price range.

(p) The term "Reserve Order" shall mean a limit order that has both a round-lot displayed size as well an additional non-displayed share amount. Both the displayed and non-displayed portions of the Reserve Order are available for potential execution against incoming orders. If the round-lot displayed portion of a Reserve Order is reduced to less than 100 shares, the System will replenish the display portion from reserve up to at least a single round-lot amount. A new timestamp is created for the replenished portion of the order each time it is replenished from reserve, while the reserve portion retains the time-stamp of its original entry.

(q) The term "Pegged Order" shall mean, for orders so designated, an order that, after entry, has its price automatically adjusted by the System in response to changes in the national best bid or offer ("NBBO"), as appropriate. A Pegged Order can specify that its price will equal the inside quote on the same side of the NBBO ("Primary Peg") or the opposite side of the NBBO ("Market Peg"). In addition, Pegged Orders may also establish their pricing relative to the NBBO by the selection of one or more $0.01 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.

(r) The term "Displayed Order" shall mean, for limit orders so designated, an order that is displayed in the System, in whole or in part, and is available for potential execution against all incoming orders until executed in full or cancelled.

(s) The term "Non-Displayed Order" shall mean, for limit orders so designated, an order that is not displayed in the System, but nevertheless remains available for potential execution against all incoming orders until executed in full or cancelled.

(t) The term "Minimum Quantity Order" shall mean, for orders so designated, an order that requires that a specified minimum quantity of shares be obtained, or the order is cancelled. Minimum Quantity Orders may only be entered with a time-in-force designation of Immediate or Cancel.

4952. System Participant Registration

(a) Participation in INET requires current registration with the System and is conditioned upon the Participant's initial and continuing compliance with the following requirements:

(1) execution of a System Subscriber Agreement;

(2) satisfaction of INET new account policy and procedure requirements;

(3) membership in, or an access arrangement with a participant of, a clearing agency registered with the Commission that maintains facilities through which System compared trades may be settled;

(4) acceptance and settlement of each System trade that the System identifies as having been effected by such Participant, or if settlement is to be made through another clearing member, guarantee of the acceptance and settlement of such identified System trade by the clearing member on the regularly scheduled settlement date;

(5) compliance with all applicable rules and operating procedures of the Association and the Commission.

(6) In addition to the above, on or before 60 days after the System becomes a facility of Nasdaq, all System Participants shall be members of the Association.

4953. Order Entry Parameters

(a) INET System Orders

(1) General - An INET System order is an order that is entered into the System for display and/or execution as appropriate. Such orders are executable against marketable contra-side orders in the System as set forth in NASD Rule 4955.

(A) All INET System Orders shall indicate whether they are a Market Order or Limit Order and shall indicate if they are a buy, short sale, short-sale exempt, or long sale. INET Systems Orders can be designated as Immediate or Cancel ("IOC"), Market Day or Limit Day ("DAY"), Extended Day ("XDAY"), or Expire Time ("ExT").

(B) An INET System order may also be designated as a Reserve Order, a Pegged Order, a Non-Displayed Order, a Minimum Quantity Order, or a Discretionary Order.

(2) Short Sale Compliance- INET System orders to sell short shall not be executed if the execution of such an order would violate Regulation SHO under the Exchange Act, NASD Rule 3350 or, for routed orders, the rules of the applicable self-regulatory organization governing short selling or, in the case of ITS Securities, Rule 10a-1 under the Exchange Act.

(3) Routing – All INET System orders entered by participants directing or permitting routing to other market centers shall be routed for potential display and/or execution as set forth in NASD Rule 4956.

4954. Entry and Display of Orders

(a) Entry of Orders—Participants can enter orders into the System, subject to the following requirements and conditions:

(1) Participants shall be permitted to transmit to the System multiple orders at a single as well as multiple price levels. Each order shall indicate the amount of reserve size (if applicable).

(2) The System shall time-stamp an order which shall determine the time ranking of the order for purposes of processing the order.

(3) Orders can be entered into the System (or previously entered orders cancelled) between the hours 7:00 a.m. to 8:00 p.m. Eastern Time.

(A) Exception: Orders entered prior to 9:30 a.m. Eastern Time, or after 4:00 p.m. Eastern Time, seeking to be routed to either the New York or American Stock Exchanges shall be rejected.

(B) Exception: Pegged and Market Orders may only be entered between 9:30 a.m. and 4:00 p.m. Eastern Time.

(b) Display of Orders-- The System will display orders submitted to the System as follows:

(1) System Book Feed—orders resident in the System will be displayed via the System Book Feed.

(2) Best Priced Order Display - For each System Security, the best priced order to buy and sell resident in the System will be displayed via the National Stock Exchange. The System's display of its orders in the National Stock Exchange shall not continue beyond September 30, 2006.

(3) Exceptions--The following exceptions shall apply to the display parameters set forth in paragraphs (1) and (2) above:

(A) Odd-lots, Mixed Lots, and Rounding--The System Book Feed shall be capable of displaying trading interest in odd-lot, round lot and mixed-lot amounts and, for orders price under $1.00, in sub-penny increments

(B) Minimum Increments —The minimum trading increments for the System shall be set forth in NASD Rule 4962.

(C) Reserve Size--Reserve Size shall not be displayed in the System, but shall be accessible as described in NASD Rule 4955.

(D) Discretionary Orders — The discretionary portion of Discretionary Orders shall be made available for execution only upon the appearance of contra-side marketable trading interest, and shall be executed pursuant to NASD Rule 4955 and NASD Rule 4951(o).

(E) Non-Displayed Orders—Non-Displayed Orders are not displayed in the System, and have lower priority within the System than an equally priced

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Displayed Order, regardless of time stamp, and shall be executed pursuant to NASD Rule 4955.

(F) Trade-Through Compliance and Locked or Crossed Markets– If, at the time of entry, a Displayed Order in an exchange-listed security that the entering party has elected not to make eligible for routing would lock the market, it will be converted by the System into a Non-Displayed Order. If, at the time of entry, a similar Displayed Order would cross the market or would cause a trade-through violation, the order will be converted by the System to a Non-Displayed Order and re-priced to the current low offer (for bids) or to the current best bid (for offers). Such Non-Displayed Orders will be cancelled by the System if the market moves through the price of the order after the order is accepted.

4955. Order Processing

(a) INET Book Order Process

INET System orders shall be executed through the INET Book Order Process as set forth below:

(1) Default Execution Algorithm - Price/Time -- The System shall execute equally priced or better priced trading interest within the System in price/time priority in the following order:

(A) Displayed Orders;

(B) Non-Displayed Orders, the reserve portion of Reserve Orders, in price/time priority among such interest;

(C) The discretionary portion of Discretionary Orders as set forth in NASD Rule 4951(o).

(2) Decrementation – Upon execution, an order shall be reduced by an amount equal to the size of that execution.

(3) Price Improvement – any potential price improvement resulting from an execution in the System shall accrue to the taker of liquidity.

Example:

Buy order resides on INET book at 10.

Incoming order to sell priced at 9 comes into INET System

Order executes at 10 (seller get $1 price improvement)

4956. Routing

(a) INET Order Routing Process

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

(A) Exchange-Listed Routing Options

The System provides five routing options for orders in exchange-listed securities. Of these five, only two – DOT Immediate and DOT Alternative - are 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. The five System routing options for NYSE and/or Amex listed orders are:

(i)   DOT Immediate ("DOTI") – under this option, after checking the INET System for available shares, orders are sent directly to the NYSE or the AMEX as appropriate. When checking the INET

book, the System will seek to execute at the better price of either the limit price specified in the order, or the best price displayed at that time at the NYSE. If no liquidity is available in the INET System, the order will be routed directly to the NYSE or AMEX at the limit order price. This option may only be used for orders with time-in-force parameters of either DAY, IOC, or market-on-open/close. Only limit orders may be used with this option.

(ii)   DOT Alternative ("DOTA") – under this option, after checking the INET System for available shares, orders are sent to other available market centers for potential execution before the destination exchange. Any un-executed portion will thereafter be sent to the NYSE or AMEX, as appropriate, at the order's original limit order price. This option may only be used for orders with time-in-force parameters of either DAY, IOC, or market-on-open/close. Only limit orders may be used with this strategy.

(iii)   Reactive Electronic Only ("STGY") – under this option, after checking the INET System for available shares, orders are sent to other available market centers for potential execution. When checking the INET book, the System will seek to execute at the price it would send the order to a non-INET destination market center. If shares remain un-executed after routing, they are posted on the INET book and are not sent to the NYSE or AMEX. Once on the INET book, should the order subsequently be locked or

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crossed by another accessible market center, the System shall route the order to the locking or crossing market center for potential execution. 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.

(iv)   Electronic Only Scan ("SCAN") – under this option, after checking the INET System for available shares, orders are sent to other available market centers for potential execution. When checking the INET book, the System will seek to execute at the price it would send the order to a non-INET destination market center. If shares remain un-executed after routing, they are posted on the INET book and are not sent to the NYSE or AMEX. Once on the INET book, should the order subsequently be locked or crossed by another accessible 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.

(v)   Aggressive Electronic Only ("SPDY") - under this option, after checking the INET System for available shares, orders are sent to other available market centers for potential execution. When

checking the INET book, the System will seek to execute at the

price it would send the order to a non-INET destination market

center. If shares remain un-executed after routing, they are posted

on the INET book and are not sent to the NYSE or AMEX. Once

on the INET 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. 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.

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) Nasdaq-Listed Routing Options

The STGY, SPDY, and SCAN options are the only routing options provided by the System for

orders in Nasdaq-listed securities not sought to be directed to either the NYSE or AMEX.

(C) Priority of Routed Orders

Regardless of the routing option selected, orders sent by the INET System to other markets do not retain time priority with respect to other orders in INET's System and the System shall continue to execute other orders while routed orders are away at another market center. Once routed by the System, an order becomes subject to the rules and procedures of the destination market including, but not limited to, short-sale regulation and order cancellation. If a routed order is subsequently returned, in whole or in part, that order, or its remainder, shall receive a new time stamp reflecting the time of its return to the System.

4957. Clearance and Settlement

All transactions executed in the System shall be cleared and settled by and between the System Participant and INET, through a registered clearing agency using a continuous net settlement system.

4958. Obligation to Honor System Trades

(a) If a Participant, or clearing member acting on a Participant's behalf, is reported by the System, or shown by the activity reports generated by the System, as constituting a side of a System trade, such Participant, or clearing member acting on its behalf, shall honor such trade on the scheduled settlement date.

(b) INET and/or Nasdaq shall have no liability if a Participant, or a clearing member acting on the Participant's behalf, fails to satisfy the obligations in paragraph (a).

4959. Compliance with Rules and Registration Requirements

(a) Failure by a Participant to comply with any of the rules or registration requirements applicable to it and its use of the System shall subject such Participant to censure, fine, suspension or revocation of its registration as Participant or any other fitting penalty under the

Rules of the Association, or such other action, up to and including termination of access to the System.

(b) If a Participant fails to maintain a clearing relationship, or to honor its obligations under NASD Rule 4958, it shall have its access to the System restricted until such time as a clearing arrangement is reestablished and/or the Participant meets its obligation to honor System trades.

(c) The authority and procedures contained in paragraph (b) do not otherwise limit the Association's authority, contained in other provisions of the Association's Rules, to enforce its rules or impose any fitting sanction.

4960. Anonymity

(a) Transactions executed in the System shall be cleared and settled with INET. The transaction reports produced by the System will indicate the details of the transactions, and shall not reveal contra party identities other than INET.

(b) INET shall reveal a Participant's identity in the following circumstances:

(1) when the National Securities Clearing Corporation ("NSCC") ceases to act for a participant, or the Participant's clearing firm, and NSCC determines not to guarantee the settlement of the Participant's trades;

(2) for regulatory purposes or to comply with an order of an arbitrator or court;

(3) no later than the end of the day on the date a trade was executed, when the participant's order has been decremented by another order submitted by that same Participant; or

(4) if both Participants to the transaction consent.

4961. Clearly Erroneous Transactions

Commencing no later than 60 days after the System becomes a facility of Nasdaq, all matters related to clearly erroneous transactions executed in the System shall be initiated and adjudicated pursuant to NASD Rule 11890.

4962. Minimum Quotation Increment

The minimum quotation increment in the INET System for quotations of $1.00 or above in Nasdaq-listed securities and in securities listed on a national securities exchange shall be $0.01. The minimum quotation increment in the INET System for quotations below $1.00 in Nasdaq-listed securities and in securities listed on a national securities exchange shall be $0.001.

4963. Normal Business Hours

The INET System operates from 7:00 a.m. to 8:00 p.m. Eastern Time on each business day.

4964. Limitation of Liability

The Association and its subsidiaries, as well as Nasdaq and INET and their subsidiaries, shall not be liable for any losses, damages, or other claims arising out of the System or its use. Any losses, damages, or other claims, related to a failure of the System to deliver, display, transmit, execute, compare, submit for clearance and settlement, adjust, retain priority for, or otherwise correctly process an order, Quote/Order, message, or other data entered into, or created by, the System shall be absorbed by the member, or the member sponsoring the customer, that entered the order, Quote/Order, message, or other data into the System. Notwithstanding the foregoing, the System may, within it sole discretion and for a period of time not to exceed 60 days after the System becomes a facility of Nasdaq, compensate users for losses arising out of the System or its use.

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7010. System Services

(a) - (v) **No Change.**

(w) INET System Order Execution

(1) For a period of time not to exceed 60 days after INET becomes a facility of Nasdaq, the following charges shall apply to the use of the order execution services of Nasdaq's INET System by Participants for:

NASDAQ-listed securities

Order Execution

Non-Directed Order that accesses the Quote/Order of a market Participant through Nasdaq's INET System:

 Charge to Participant entering order:

Average daily shares of liquidity provided through Nasdaq's INET System by the Participant during the month:	
Greater than 60 million shares accessed or routed and 5 million shares provided	$0.0027 per share executed
Greater than 40 million shares but less than 60 million shares accessed or routed and 5 million shares provided	$0.0028 per share executed
Less than 5 million shares provided or less than 40 million shares accessed or routed	$0.0030 per share executed

Credit to Participant providing liquidity:

Average daily shares of liquidity provided
through Nasdaq's INET System by the
Participant during the month:

Greater than 30 million shares provided or greater than 30 million shares accessed or routed or greater than 50 million shares combined provided, accessed or routed	$0.0025 per share executed
Less than or equal to 30 million shares provided and less than or equal to 30 million shares accessed or routed and less than or equal to 50 million shares combined provided, accessed, or routed	$0.002 per share executed
Any order that matches against another order of the same Participant	$0.00025 per share per side.

Routed Orders

Any other order entered by a Participant that is routed outside of Nasdaq's INET System	$0.0025 per share executed

AMEX-listed stocks

Order Execution

Non-Directed Order that accesses the Quote/Order of

a market Participant through Nasdaq's INET System:

Credit to Participant entering order:	$0.001 per share executed
Charge to Participant providing liquidity:	$0.0009
Any order that matches against another order of the same Participant	No charge

Routed Orders

Any order entered by a Participant that is routed outside of Nasdaq's INET System through DOT	$0.01 per share executed
Any order entered by a Participant that is routed outside of Nasdaq's INET System other than through DOT	$0.0035 per share executed

AMEX-listed ETFs

Order Execution

Non-Directed Order that accesses the Quote/Order of

a market Participant through Nasdaq's INET System:

Charge to Participant entering order:

Average daily shares of liquidity provided through Nasdaq's INET System by the Participant during the month:

Greater than 60 million shares accessed or routed and 5 million shares provided	$0.0027 per share executed
Greater than 40 million shares but less than 60 million shares accessed or routed and 5 million shares provided	$0.0028 per share executed
Less than 5 million shares provided or less than 40 million shares accessed or routed	$0.0030 per share executed

Credit to Participant providing liquidity:

Average daily shares of liquidity provided through Nasdaq's INET System by the Participant during the month:	
Greater than 30 million shares provided or greater than 30 million shares accessed or routed or greater than 50 million shares combined provided, accessed or routed	$0.0025 per share executed
Less than or equal to 30 million shares provided and less than or equal to 30 million shares accessed or routed and less than or equal to 50 million shares combined provided, accessed, or routed	$0.002 per share executed
Any order that matches against another order of the same Participant	$0.00025 per share per side.

Routed Orders

Any order entered by a Participant that is routed outside of Nasdaq's INET System through DOT	$0.01 per share executed
Any order entered by a Participant that is routed	$0.0035 per share

outside of Nasdaq's INET System other than   executed

through DOT

NYSE-listed stocks

Order Execution

Non-Directed Order that accesses the Quote/Order of

a market Participant through Nasdaq's INET System:

    Credit to Participant entering order: $0.001 per share

                                                executed

    Charge to Participant providing liquidity: $0.0009

Any order that matches against another order of the   No charge

same Participant

Routed Orders

    Any order entered by a Participant that is routed $0.0005 per share

    outside of Nasdaq's INET System through DOT   executed

    Any order entered by a Participant that is routed $0.0015 per share

    outside of Nasdaq's INET System other than   executed

    through DOT

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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. <u>Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change</u>
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> 1. <u>Purpose</u>

Background

On April 22, 2005, Nasdaq entered into definitive agreements to purchase INET, a registered broker-dealer and member of the NASD[3], and operator of the INET System. Nasdaq states that, once formally purchased by Nasdaq, the INET System would immediately become a "facility" of a national securities association subject to the standards set forth in Sections 15A[4] and 19(b)(1)[5] of the Act and would be required to operate pursuant to formal system rules approved by the Commission. In order to ensure that such rules are in place at the time of closing, Nasdaq has filed this proposed set of INET System rules for Commission review and approval that includes a description of the INET System, its various features, fees, and order processing methods. Nasdaq proposes that these rules would be implemented immediately upon

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[3]   Nasdaq states that, as a member of the NASD, INET is, and remains, subject to all NASD Rules applicable to its activities as a broker-dealer. In addition, INET would continue to participate in market surveillance and audit trail programs conducted by Nasdaq, the NASD, and other self-regulatory organizations. INET would continue to act as a counter-party to all trades taking place in its system, for anonymity as well as clearance and settlement purposes. INET would also continue to provide outbound order routing services to other market centers for its subscribers.

[4]   15 U.S.C. 78o-3.

formal closing of the Nasdaq/INET transaction, and in no event more than two weeks after

Commission approval.[6]

<h2 style="text-align:center"><u>The INET System</u></h2>

1. Order Display/Matching System

The INET System allows subscribers to enter market and priced limit orders to buy and

sell Nasdaq and exchange-listed securities. According to Nasdaq, such orders may be in round-

lots, mixed-lots, or odd-lots of any size up to 999,999 shares. Nasdaq states that INET acts only

as an agent on behalf of its subscribers and engages in no proprietary trading save that necessary

to correct system errors. Subscribers may enter multiple orders at single or multiple price levels.

Subscribers have the option to have a portion of their order held in reserve and not displayed to

the marketplace. INET, in turn, makes available to System subscribers and market data vendors

a data feed of all displayable orders on both the bid and offer side of the market (excluding

reserve size share amounts) for all price levels at which shares are available within its System.

INET currently provides its best top-of-file prices, and other prices, to the National Stock

Exchange ("NSX"). In this filing, Nasdaq proposes rules under which INET would be permitted

to continue to provide its best-priced orders to the NSX until the end of the third quarter

of 2006.[7] At any time prior to that date, Nasdaq may file with the Commission a rule proposal to

move the INET System's best-priced orders, and other orders including up to full depth of book,

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[5]   15 U.S.C. 78s(b)(1).

[6]   Nasdaq states that it will provide to the Commission formal written notice of the closing
date of the transaction. Such closing date shall be the start date for the calculation of any
temporary time period referred to in this filing. Nasdaq states that it will thereafter
submit rule filings to include such closing date in its rules.

[7]   Nasdaq states that, as is the case today, INET would remain subject to all applicable rules
and regulations of the NSX.

to the Nasdaq Market Center for display, routing, and execution purposes. If filed, Nasdaq states that it would seek immediate effectiveness of the proposal. In addition, INET would continue to accept sub-penny prices in $0.001 increments for securities priced under $1.00 a share. Such sub-penny prices are viewable via the System data feed.

2. Access Standards

Nasdaq states that, to obtain access to the INET System as a system participant, a user must execute an INET subscriber agreement and be a participant in, or have an access arrangement with a participant in, a Commission-registered clearing agency. In addition, the INET subscriber must also agree to:

a. comply with all applicable rules of the NASD and the Commission; and

b. accept all INET System trades identified by the System as being effected by the subscriber.

According to Nasdaq, INET also currently provides access to approximately 70 non-NASD member broker-dealers. Nasdaq states that it intends, for a period of time not to exceed 60 days after the formal close of the Nasdaq/INET transaction, to continue to provide such entities with sponsored access to the INET System under generally the same terms and conditions they enjoy today. This would be accomplished through contractual agreements between INET and such subscribers. Nasdaq states that, within 60 days after the formal closing of the Nasdaq / INET transaction, all participants in the INET System must be NASD members.

3. Order Types

The INET System makes available to subscribers several order types. These order types are described below.

Limit Order - an order to buy or sell a stock at a specified price or better.

Market Order - an un-priced order to buy or sell a stock at the market's current best price. A market order may have a limit price beyond which the order shall not be executed.

Reserve Order - a limit order that has both a round-lot displayed size as well as an additional non-displayed share amount. Both the displayed and non-displayed portions of the Reserve Order are available for potential execution against incoming orders. If the round-lot displayed portion of a Reserve Order is reduced to less than 100 shares, the System would replenish the display portion from reserve up to at least a single round-lot amount.

Pegged Order - a limit order that, after entry, has its price automatically adjusted by the System in response to changes in the national best bid or offer ("NBBO"), as appropriate. A Pegged Order can specify that its price will equal the inside quote on the same side of the NBBO ("Primary Peg") or the opposite side of the NBBO ("Market Peg"). In addition, Pegged Orders may also establish their pricing relative to the NBBO by the selection of $0.01 offset amounts that would adjust the price of the order by the offset amount selected.

Example Primary Pegged Order:

The market is $10.00 bid - $10.01 offer. INET receives a non-route Primary Pegged buy order. INET would post the order at $10.00. If the inside bid moves to $10.01, INET would modify the Pegged Order to the $10.01 bid price. A new time stamp is created at the time of this modification. If a sell order is subsequently entered at $10.01 or lower, the pegged order would execute at $10.01.

Example Market Pegged Order:

The market is $10.00 bid – $10.01 offer. INET receives a Market Pegged buy order. INET would post the order at $10.01. If the inside offer moves to $10.02, INET would modify

the Pegged Order to the $10.02 offer price. A new time stamp is created at the time of this modification.

Displayed Order - a limit order that is displayed in the System, in whole or in part, and is available for potential execution against all incoming orders until executed in full or cancelled.

Non-Displayed Order - a limit order that is not displayed in the System, but nevertheless remains available for potential execution against all incoming orders until executed in full or cancelled.

Minimum Quantity Order - an order that requires that a specified minimum quantity of shares be obtained, or the order is cancelled. Minimum Quantity Orders may only be entered with a time-in-force designation of IOC.

Example Minimum Quantity Order:

The market is $10.00 bid – $10.01 offer. INET receives an order to buy 1000 shares, Minimum Quantity of 500 shares, at $10.01. This order can only have a time in force of IOC. The INET book has 2 sell orders each for 300 shares at $10.01. INET executed 600 shares at $10.01 (in two lots) and cancels the remaining 400 shares back.

Discretionary Order - an order that has both a displayed price and size, as well as a non-displayed discretionary price range, at which the entering party, if necessary, is also willing to buy or sell. The non-displayed trading interest is not entered into the System book but is converted to an IOC order equal in size to the displayed size and priced at the most aggressive price in the discretionary price range when displayed shares become available or an execution takes place at any price within the discretionary price range. The generation of this IOC order is accompanied by the cancellation of the displayed portion of the Discretionary Order. If more than one Discretionary Order is available for conversion to an IOC order, the system would

convert all such orders at the same time and priority would be given to the first IOC order(s) that reaches the trading interest on the other side of the market. If an IOC order is not executed in full, the unexecuted portion of the order would be automatically re-posted and displayed in the System book with a new time stamp, its original displayed price, and its original non-displayed discretionary price range.

Example:

INET receives a Discretionary buy order, with a displayed limit price of $10.00 and a display quantity of 1000 shares and a discretionary price range of up to $15.00. INET posts the order as 1000 shares at $10.00. Thereafter, another market participant posts another offer to buy at 300 shares at $11.00, creating a buy market as follows:

Display	Reserve	Price	Discretionary Price Range
300	0	$11.00	None
1000	0	$10.00	$11.00-$15.00

Thereafter, another market participant enters a sell order for 500 shares at $11.00. The resulting executions are as follows:

1. 300 shares execute immediately at $11.00.

2. 200 shares to sell at $11.00 is posted to the book.

3. Both the execution at $11.00 and the posting of the display price of $11.00 are events that trigger the processing of the discretionary portion of the Discretionary Order.

4. INET would cancel the 1000 display portion of the Discretionary Order and send an IOC order for 1000 shares priced at $15.00 to the displayed 200 shares priced at $11.00.

5. The 200 shares would execute at $11.00, and the 800 share remainder of the Discretionary Order would be placed back into the INET book at its original order price of $10.00. If there were multiple Discretionary Orders available to interact with the 200 shares, all such orders would be activated at the same time by the INET system and whichever IOC order(s) first reached the 200 shares would get the execution.

4. Time in Force Designations

Orders entered into the INET System may be designated by the entering party to remain in force and available for display and/or potential execution for varying periods of time. Unless cancelled earlier, once these time periods expire, the order (or the unexecuted portion thereof) is returned to the entering party. These "time in force" designations are described below:[8]

Immediate or Cancel (IOC) - limit orders with this designation execute immediately at the limit price if shares are available. If no shares are available, the orders are immediately

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[8]   In addition, Nasdaq states that the System also supports On-Open and On-Close order types for orders being routed directly to the NYSE, AMEX, and Nasdaq Market Center. According to Nasdaq, these orders are not supported or executed within the INET System itself. Instead, these order formats are designed for processing at their destination market.

cancelled. If partially executed, un-executed remainders of these orders are immediately

cancelled.

Market Day or Limit Day (DAY) - limit orders with these designations (or the

unexecuted portions of such orders) are held by the INET System and remain available for

potential display/execution until 4:00 p.m. Eastern Time on the day they are submitted unless

cancelled before then by the entering party. If not executed by 4:00 p.m., the order is cancelled

and sent back to the entering party.

Expire Time (ExT) - limit orders with this designation are held by the system for

potential execution until the expiration of the specific time period indicated by the entering

party, including time periods outside of normal market hours.

Extended Day (XDAY) - limit orders with this designation (or the unexecuted portions of

such orders) are held by the INET System and remain available for potential execution until

8:00 p.m. Eastern Time.

The INET System operates between the hours of 7:00 a.m. and 8:00 p.m. Eastern Time.

Orders with the above time in force designations may be entered into the INET System, or

previously entered orders cancelled, starting at 7:00 a.m. Eastern Time. Only orders with the

XDAY designation would be retained by the system after 4:00 p.m. Eastern Time, with all other

order types being cancelled back to the entering party.

5. Routing

The INET System provides the capability to route orders to other available market

centers. Routing functionality is available to System users between the hours of 7:00 a.m. and

8:00 p.m. Eastern Time. In general, the System provides users with five optional routing

strategies for exchange-listed securities. These strategies are summarized below:

DOT Immediate (DOTI)

After checking the INET System for available shares, orders are sent directly to the New York Stock Exchange ("NYSE") via the DOT system. When checking the INET book, the System looks to execute at the better price of either the limit price specified in the order, or the best price displayed at that time at the NYSE. If no liquidity is available in the INET System the order is routed directly to the NYSE via DOT at the limit order price for posting. A similar process is followed for orders in stocks listed on the American Stock Exchange ("AMEX"). This strategy may only be used for orders with time-in-force parameters of either DAY, IOC, or market-on-open/close.

Example of DOTI Routable Order:

The current NBBO is $10.00 bid x $10.02 offer. Offer size is as follows: 300 shares INET displayed, 200 shares INET non-displayed, 100 shares PCX, 200 shares NYSE. Participant A enters a buy order for 1000 shares at $10.02. The System would first IOC INET for 1000 shares at $10.02. Participant A would execute against 300 shares at $10.02 displayed and the 200 shares non-displayed. The System would route the remaining 500 shares to NYSE. Participant A would receive 200 shares from NYSE. The remaining 300 shares would reside on the NYSE book, per routing instructions.

DOT Alternative (DOTA)

After checking the INET System for available shares, the order would be sent to various available market centers for potential execution. Any remaining un-executed portion would thereafter be sent to the NYSE or AMEX, as appropriate, at the limit order price for posting. This strategy may only be used for orders with time-in-force parameters of either DAY, IOC, or market-on-open/close.

Example of DOTA Routable Order:

The current NBBO is $10.00 bid x $10.02 offer. Offer size is as follows: 300 shares INET displayed, 200 shares INET non-displayed, 100 shares PCX, 200 shares NYSE. Participant A enters a buy order for 1000 shares at $10.02. The System would first IOC INET at $10.02. Participant A would execute against 300 shares at $10.02 displayed and the 200 shares non-displayed. The System would route the remaining shares to PCX. Participant A would receive 100 shares from PCX. The System would then route 400 shares to the NYSE. Participant A would receive 200 shares from the NYSE. The remaining 200 shares would reside on the NYSE book, per routing instructions.

SCAN/STGY/SPDY

In all of these routing options, after checking the INET System for available shares, orders would be sent to various available market centers for potential execution. For all these options, when checking the INET book, the System would look to execute at the price it would send the order to the non-INET destination market center and, if any shares remain un-executed after routing, they are posted on the INET book and are not sent to the NYSE or AMEX for posting.

Once returned to the INET book after routing, an order with the SCAN designation would <u>not</u> be routed out to an accessible market center that subsequently locks or crosses the SCAN order. Orders with STGY and SPDY would be routed to an accessible market center that subsequently locks or crosses the STGY or SPDY order. While both STGY and SPDY orders would route to locking or crossing markets, the SPDY order would be re-priced by the System to match on then being displayed on the same side of the market by the locking or crossing market center (<u>i.e.</u>, a buy order to the bid and a sell to the offer).

With the exception of the Minimum Quantity Order type, all time-in-force parameters and order types may be used with the STGY, SCAN, and SPDY routing options. Nasdaq states that orders routed by INET to another market do not retain time priority with respect to other orders in INET's System and INET continues to execute other orders while the routed order is away at another market. Nasdaq states that, once routed by INET, an order becomes subject to the rules and procedures of the destination market including, but not limited to, short-sale regulation, and order cancellation. According to Nasdaq, orders routed to a destination market that are subsequently returned in whole or in part to the System would have their time priority based on the time they are returned to the System.

Example of STGY Routable Order:

The current NBBO is $10.00 bid x $10.02 offer, size 200 shares at the Nasdaq Market Center. INET has a non-display offer of 500 shares at $10.01. Participant A enters an order onto INET to buy 1000 shares at $10.02. The System would first IOC the INET book for any potential orders at or better than the limit price. Participant A would execute 500 shares on INET at $10.01 (the non-display order on the book). The System would then route the order to the Nasdaq Market Center at $10.02. 200 shares execute at the Nasdaq Market Center at $10.02. 300 shares of the order remain unexecuted, and are entered onto the INET book at $10.02. 5 seconds later, PCX enters the market with an offer of $10.02. The System would cancel the order off the book, and route 300 shares at $10.02 to PCX. PCX executes 300 shares at $10.02. Participant A receives an execution for the remaining 300 shares in the order.

Example of STGY Routable Order (Crossed Market):

The current NBBO is $10.01 bid x $10.00 offer. INET has 500 shares on the offer at $10.00. PCX has 300 shares on the offer at $10.00. Participant A enters a market order to buy

1000 shares. The System would price the order at $10.00 and IOC the INET book.

Participant A would receive 500 shares at $10.00. The System would route the remaining shares

to PCX. Participant A would receive 300 shares at $10.00 from PCX. After attempting to

exhaust the quotes, the remaining 200 shares would be posted to the INET book at $10.00.

Example of SCAN Routable Order:

The current NBBO is $10.00 bid x $10.02 offer, size 200 shares at the Nasdaq Market

Center. INET has a non-display offer of 500 shares at $10.01. Participant A enters an order

onto INET to buy 1000 shares at $10.02. The System would first IOC the INET book for any

potential orders at or better than the limit price. Participant A would execute 500 shares on

INET at $10.01 (the non-display order on the book). The System would route the order off the

book with the remaining shares of the order, 500, to the Nasdaq Market Center at $10.02.

200 shares execute at the Nasdaq Market Center at $10.02. 300 shares of the order remain

unexecuted, and are entered onto the INET book at $10.02. 5 seconds later, PCX enters the

market with an offer of $10.02. The System would not route the order to PCX, but would keep

the order on the INET book, per Participant A's routing instructions.

Example of SPDY Routable Order (Crossed Market):

The current NBBO is $10.01 bid x $10.00 offer. INET has 500 shares on the offer at $10.01. PCX has 300 shares on the offer at $10.00. Participant A enters a market order to buy 1000 shares. The System would price the order at $10.01 and IOC the INET book. Participant A would receive 500 shares at $10.01. The System would route the remaining 500 shares to PCX. Participant A would receive 300 shares at $10.00 from PCX. The remaining 200 shares would be posted to the INET book at $10.01.

Other

Nasdaq states that 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.

6. Execution Algorithm

Nasdaq states that the INET System has an execution algorithm based on price/time priority. For each order, among equally-priced or better-priced trading interest, the System executes against available contra-side displayed share amounts in full, in price/time priority, before then moving to any non-displayed shares which are likewise executed in price/time priority. Below are examples of this algorithm:

Displayed Order:

The current NBBO is $10.00 bid x $10.02 offer. Participant A enters a display order on INET to buy 1000 shares at $10.01. NBBO is changed to $10.01 x $10.02. Participant B sees the 1000 share order at $10.01 and enters an order to sell 500 shares at $10.01. The orders match at $10.01, with 500 shares matched. NBBO remains at $10.01 x $10.02 with the size on the bid decremented to 500 shares, the amount of shares matched.

Limit Order (with Reserve):

The current NBBO is $10.01 bid x $10.02 offer. Participant A enters an order to buy 1000 shares, display 200, at $10.01. INET bid is $10.01, 200 displayed, 800 non-displayed. Participant B enters a display buy order for 1000 shares at $10.01. INET bid is $10.01, 1200 displayed, 800 non-displayed. Participant C enters an order to sell 1500 shares at $10.01. Participant C receives executions against orders as follows: Participant A executes 200 shares at $10.01; Participant B executes 1000 shares at $10.01 (display order receives priority over non-display even though non-display order was there first); Participant A executes 300 shares from non-display portion. Participant C has executed a total of 1500 shares. Participant B has executed all 1000 of its shares. Participant A has 200 shares remaining in its order, and is now displayed, per original instructions.

Routable Order:

The current NBBO is $10.00 bid x $10.02 offer, size 200 shares at the Nasdaq Market Center. INET has a non-display offer of 500 shares at $10.01. Participant A enters an order onto INET to buy 1000 shares at $10.02. The system would first IOC the INET book for any potential orders at or better than the limit price. Participant A would execute 500 shares on INET at $10.01 (the non-display order on the book). The System would then route the order off the book with the remaining shares of the order, 500, to the Nasdaq Market Center at $10.02. 200 shares execute at the Nasdaq Market Center at $10.02. 300 shares of the order remain unexecuted, and are entered onto the INET book at $10.02.

7. Clearly Erroneous Trade Procedures

Nasdaq states that currently, INET adjudicates clearly erroneous trade disputes for executions taking place exclusively within its System. While generally reviewing clearly erroneous trade claims in response to subscriber requests, INET currently reserves the right to take action on its own initiative if it determines that a trade is clearly erroneous and needs to be modified or cancelled. INET currently also reserves the right to refuse to review potentially erroneous transactions that are brought to its attention more than 20 minutes after execution. In the normal course, INET limits its clearly erroneous review to INET System trades that execute at prices that are certain percentages away from the National Best Bid/Offer at the time of execution. These percentages are provided below:

Execution Price Range Away from NBBO

$3 and under	10%
Over $3 and under $10	5%
$10 to $30	3%
Over $30	$1 or more

Nasdaq is proposing to continue the above process for a period of 60 days after the formal close of the Nasdaq/INET transaction. During that interim period, Nasdaq states that it would prepare to incorporate INET into the current clearly erroneous process of Nasdaq and Brut, which is governed by NASD Rule 11890. Nasdaq states that this interim period would ensure that sufficient notice is provided to System subscribers about their rights and obligations related to clearly erroneous trades under NASD Rule 11890, as well as allow Nasdaq to train incoming INET staff to properly process such requests. Prior to 60 days after the formal close of the Nasdaq/INET transaction, Nasdaq states that it would file with the Commission a rule

proposal making INET's clearly erroneous process specifically subject to NASD Rule 11890.

Nasdaq states that it will seek immediate effectiveness of that filing.

8. Other System Standards

Nasdaq is also proposing to establish standards regarding operational issues between the

Nasdaq Market Center and INET. For example, Nasdaq is proposing rules for the INET System

codifying standards regarding the obligation of users to honor system trades and the removal of

users for failing to maintain a required clearing relationship.[9] While Nasdaq is proposing that

INET have in place at closing a general limitation of liability rule, Nasdaq is also proposing that

INET continue, for a period of time not to exceed 60 days after the formal close of the

Nasdaq/INET transaction, to have the discretion to accommodate users of the System for losses

arising out of the System or its use. Before the end of that time period, Nasdaq states that it will

file a rule proposal with the Commission so that the System's future accommodation of users

would be subject to the same standards already in place for the Nasdaq Market Center and

Nasdaq's Brut Facility[10]. Nasdaq is also proposing to establish rules governing the anonymity

provided by the system, as well as rules governing minimum quote increments. Nasdaq states

that the System's anonymity standards and proposed minimum quote increment standards are

substantially similar to those in place in the Nasdaq Market Center and Nasdaq's Brut Facility

and also provides for allowing sub-penny quotes in securities priced under $1.00.

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[9]   See proposed NASD Rules 4958 and 4959.

[10]   See NASD Rule 4705(j) and proposed NASD Rule 4964.

9. Pricing

Nasdaq is also proposing the creation of a fee and rebate schedule for the INET System.

Nasdaq states that, with exception of eliminating fee rates discounts based on the use of the

services of the Instinet broker-dealer, this fee and rebate schedule is the same as the one

applicable to current INET subscribers.[11] Nasdaq proposes that this fee schedule remain in place

for a period of time not to exceed 60 days after the formal close of the Nasdaq/INET transaction.

Before the termination of such 60-day period, Nasdaq will file with the Commission an

integrated fee and rebate structure governing the use of all Nasdaq's main trading systems (i.e.,

the Nasdaq Market Center, Nasdaq's Brut Facility, and Nasdaq's INET System).

10. Trade-Through Compliance and Locked and Crossed Markets

Nasdaq states that, in order to ensure compliance with the trade-through rule for listed

securities[12], the INET system checks the prices of orders in listed securities that are not made

eligible for routing by the entering party before and after an order is entered in the System. The

process is described in further detail below:

At Order Entry - At the time of order entry, every order would be checked to ensure that

it does not lock or cross the market, or cause an execution at a price that would constitute a

violation of the trade-through rule. If an order locks the market, it would be turned into a non-

display order so as not to quote a locked market. If an order crosses the market, or would cause

a trade-through violation, it would be re-priced to the current low offer (for bids) or to the

current best bid (for offers), and turned into a non-display order so as to not quote a locked

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11   See proposed NASD Rule 7010(w).

12   See Section (8)(d) of the Plan for the Purpose of Creating and Operating an Intermarket
        Communications Linkage Pursuant to Section 11A(a)(3)(B) of the Act.

market. Any non-display order that crosses the market would be re-priced to the current low offer (for bids) or to the current best bid (for offers).

Example:

The National Best Bid in a listed security is $83.55. INET Subscriber enters a non–route order to sell at $83.54. The INET system would automatically re-price the order to $83.55 and change it to non-display.

<u>After Order Entry</u> - An non-routable order entered for display would not be affected by the trade-through rule after it is accepted. To prevent trade-throughs, however, a non-display non-routable order however, may be cancelled from the INET book with the reason code if the market moves through the price of the order after the order is accepted.

Example:

The National Best Bid in a listed security is $83.55. INET Subscriber enters a non-display non-route order to sell at $83.55. The National Best Bid in the security becomes $83.56. The non-display order to sell at $83.55 would be cancelled since it cannot be executed without causing a trade-through violation.

Nasdaq states that INET's re-pricing and conversions to non-display of orders are done with the knowledge of System subscribers and only takes place in connection with orders that subscribers have elected not to make eligible for routing.

11. Integration Plan

Upon the closing of the INET transaction, Nasdaq will be the owner and operator of three separate trading systems, the Nasdaq Market Center, Nasdaq's Brut Facility, and Nasdaq's INET System. For a period of time after the close, Nasdaq states that it will continue to separately operate these systems, with each system providing distinct order-display, execution, and routing

services. Orders entered and displayed in a particular system shall have time-priority only with regard to other orders in that same system. For a period of time ending no later than September 30, 2006, the INET System would continue to post its top-of-file quotes through the facilities of NSX.

Nasdaq's long-term vision is to have all of its systems integrated into a single technology platform that would further enhance execution quality for market participants. As part of that consolidation plan, soon after the formal close of the Nasdaq/INET transaction, Nasdaq states that it anticipates that it will merge the INET broker-dealer into Nasdaq's Brut broker-dealer and that Brut as a single broker dealer would operate both ECNs as separate systems, with separate order processing and execution. As such, the NYSE would continue to serve as the designated examining authority for financial responsibility purposes for Nasdaq's broker-dealer. Nasdaq states that there would continue to be no priority in one system for orders entered into the other.

According to Nasdaq, the next step in its current plan is to combine all of its three execution systems into a single trading platform. Nasdaq states that it expects to accomplish this process sometime before the end of the third quarter of 2006. As part of this process, Nasdaq would also combine all three of its system books into a single integrated book where all orders interact and have time-priority against each other. Nasdaq anticipates transitioning quotation and execution activity from its systems and other market centers to its single system in phases.

Once Nasdaq's single integrated system is operational and fully populated, Nasdaq states that it expects to continue to operate a broker-dealer to act as Nasdaq's outbound access broker dealer to reach orders displayed in other market centers.[13]

2.   Statutory Basis

Nasdaq believes that the proposed rule change is consistent with the provisions of Section 15A of the Act,[14] in general, and Section 15A(b)(6) of the Act,[15] in particular, in that it is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, remove impediments to a free and open market and a national market system, and, in general, to protect investors and the public interest.

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. Nasdaq states that its proposed operation of the INET System must be viewed against the backdrop of today's competitive and dynamic market structure. According to Nasdaq, the Commission's action in approving the Order Handling Rules, Regulation ATS, the creation of NASD's Alternative Display Facility ("ADF"), and the recent approval of Regulation NMS[16] provide increased

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[13]   Changes to text made pursuant to phone conversation between Thomas P. Moran, Associate General Counsel, Nasdaq, and John C. Roeser, Assistant Director, Division of Market Regulation, Commission, on November 2, 2005.

[14]   15 U.S.C. 78o-3.

[15]   15 U.S.C. 78o-3(b)(6).

[16]   See Securities Exchange Act Release Nos. 37619A (August 29, 1996), 61 FR 48290 (September 6, 1996) (Order Handling Release); 40760 (December 8, 1998), 63 FR 70844 (December 22, 1998) (Regulation ATS Release); 46249 (July 24, 2002), 67 FR 49822 (July 31, 2002) (ADF Release); and 51808 (June 9, 2005), 70 FR 37496 (June 29, 2005) (Regulation NMS Release).

opportunities for market participants to compete vigorously for the trading of U.S. equity securities.

Nasdaq states that the combination of Regulation NMS's articulation of a framework that obligates market participants to seek the best price and the availability of technology to display and reach that price ensures that all market centers will be able to compete by offering the best price. Nasdaq believes that the dynamic market structure and the incentives that led to the creation of entities such as the INET System ensure that all market centers will continue to innovate and compete to serve their customers, and that new competitors will be able to enter if they believe it would be profitable for them to do so. In this dynamic competitive environment, Nasdaq believes that its operation of the INET System will not place any burden on competition.

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

No written comments were either solicited or received.

III.   <u>Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action</u>

Within 35 days of the date of publication of this notice in the <u>Federal Register</u> 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 Nasdaq 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.   <u>Solicitation of Comments</u>

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:

<u>Electronic comments</u>:

- 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-NASD-2005-128 on the subject line.

<u>Paper comments</u>:

- Send paper comments in triplicate to Jonathan G. Katz, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-9303.

All submissions should refer to File Number SR-NASD-2005-128. 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 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 such 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-NASD-2005-128 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.[17]

Jonathan G. Katz
Secretary

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[17]   17 CFR 200.30-3(a)(12).