Bloomberg
TRADEBOOK LLC
Member NASD/SIPC

July 14, 2003

Via e-mail: rule-comments@sec.gov

U.S. Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, DC 20549-0609

Attention: Mr. Jonathan G. Katz, Secretary

Re: SEC File No. SR-NASD-2003-81

Ladies and Gentlemen:

Bloomberg Tradebook LLC ("Bloomberg Tradebook")[1] appreciates the opportunity to comment, in response to the request by the Securities and Exchange

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1 Bloomberg Tradebook operates a proprietary electronic communications network ("ECN") pursuant to Regulation ATS under the Securities Exchange Act of 1934 (the "Exchange Act") and a no-action letter from the staff of the Commission's Division of Market Regulation. Letter from Dr. Richard R. Lindsey to Roger D. Blanc (January 17, 1997), SEC No-Action Letter, 1997 SEC No-Act. LEXIS 55 (the "Bloomberg Tradebook No-Action Letter"). The Bloomberg Tradebook No-Action Letter has subsequently been extended on several occasions. Bloomberg Tradebook is a registered broker-dealer and a member of the National Association of Securities Dealers, Inc. (the "NASD"). Bloomberg Tradebook offers its institutional and broker-dealer customers, and other broker-dealers that access the Tradebook system via private connections and Nasdaq's systems, the opportunity to buy and sell equity securities through use of the BLOOMBERG PROFESSIONAL service (as defined below).

Bloomberg Tradebook is a wholly owned subsidiary of Bloomberg L.P. ("Bloomberg"). Bloomberg is engaged in the business of providing its customers with financial market information, news and analytics via its worldwide electronic network (the "BLOOMBERG PROFESSIONAL™ service"). Bloomberg also serves its broker-dealer and institutional customers' communications needs and facilitates their transaction of business by offering various additional services, including electronic messaging, non-anonymous offerings, bids wanted and equity order routing and indications of interest, and linkages to certain exchanges within and outside the United States. Approximately two million text messages and transaction messages involving billions of dollars of securities are sent and received by Bloomberg customers across the

(Footnote continued)

Commission (the "Commission") in Securities Exchange Act Release No. 47993 (June 5, 2003) on the proposed rule change submitted by the National Association of Securities Dealers, Inc. (the "NASD"), through its wholly controlled subsidiary, The Nasdaq Stock Market, Inc. ("Nasdaq"), relating to quote decrementation in SuperMontage.

Electronic communications networks ("ECNs") submit quotations to SuperMontage and therefore elect to be order-delivery participants. They differ from market makers, which place orders and receive executions. In concept, decrementation is a design feature of SuperMontage that is intended to preserve the continuity of the market and to prevent locked and crossed markets. It does so by deleting from the publicly quoted market the bid or offer of an ECN that has been delivered an order, on the theory that the order either will result in a transaction absorbing some or all of the ECN's quoted quantity or in a permitted rejection of the order because, e.g., the ECN has already bought or sold the amount of stock it had represented in its published quotation or the ECN was in the process of changing its quotation, either of which would constitute an excused failure to accept the order under Exchange Act Rule 11Ac1-1.

The ECN accepting a client order has an obligation to display it in accordance with the Commission's Order Execution Rules, particularly Exchange Act Rule 11Ac1-4. The decrementation process Nasdaq has devised, even with the amendment it now proposes, cuts squarely against that obligation and puts the ECN in the position of losing priority in the order queue, even if it reenters the client order after being "pinged out".

Related to that is the question whether a broker, having best execution duties of its own to its clients, should be able to shirk those duties in bypassing bids and offers posted at the NBBO by ECNs on the basis that the broker is unwilling to pay the ECNs' access fees. The Commission should no longer duck that issue, nor should it allow Nasdaq to decide the issue for the Commission through the decrementation back door.

The question, then, is which interest is to be given priority? If the Commission wishes to abolish all access fees, including those imposed by SuperMontage and all other market centers (e.g., exchanges, ECNs, ATSs, the Alternative Display Facility) that charge access fees, regardless of what the fees are called, the Commission would thereby remove the primary cause of locked and crossed markets. If not, the

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BLOOMBERG PROFESSIONAL service every business day. In addition, we expect in the future to provide access to additional points of liquidity as customer demand dictates.

Commission should not allow Nasdaq to hurt investors who place orders with ECNs that charge the very access fees the Commission allows.

The problems decrementation has created, however, result from access fees ECNs are permitted to charge and the unwillingness of some market participants to pay those fees. ECNs may elect to reject SuperMontage orders selectively for cause, that is, orders that emanate from order-entry firms that refuse to pay their fees.

Given that state of affairs, anomalous results inevitably will occur.[2] On the one hand, if an ECN's published bid or offer were not decremented upon delivery of an order and an ECN rejected a non-paying order-entry firm's order, the still-standing ECN quotation would block any further transactions by the order entrant unless Nasdaq were willing to tolerate locks and crosses or permit trade-throughs. On the other hand, if the order entrant were stopped from making further trades because it would not trade with the ECN's prevailing best bid or best offer, it presumably would go to another venue and Nasdaq would lose the volume. Locks and crosses within Nasdaq would be replaced in such a case by inter-market locks and crosses between, e.g., Nasdaq and the Alternative Display Facility. In short, Nasdaq is substituting inter-market locks and crosses for intra-market locks and crosses.

The current decrementation procedures on SuperMontage unfairly discriminate against ECNs that elect order delivery (all of them have) and provide an opportunity for participants in SuperMontage to "game" the system in ways that ultimately are harmful to investors and to the integrity of the market. The NASD's recent proposed amendment to SuperMontage's decrementation process does not solve this problem.

Under the current rule, before giving effect to the proposed amendment, if an ECN is quoting 1,000 shares and receives an order delivery for 300 shares that it rejects because the order-entry firm or market participant will not pay its access fees, the ECN's entire 1,000-share quotation is "decremented" or "pinged out". If the ECN wishes to reenter the order, it would either lose its time priority and go to the back of the order queue, or be forced to access liquidity rather than provide it, dramatically increasing the cost of effecting the trade on behalf of its client.

There are, in addition, frequent examples of firms, whose orders have been refused by ECNs, taking perverse advantage of decrementation to force the ECN itself to

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2 Access fees charged by ECNs and other market centers create other problems as well, such as creating incentives for payments for order flow, incentives for internalizing, incentives for delaying the publication of quotations and incentives for delaying the execution of orders.

pay an access fee. For example, instead of being the recipient of an access fee of, say, 30 cents per 100 shares on a 1,000-share trade, the ECN and thus its client (to whom the fees are passed through) could become the payer of 30 cents per 100 shares, a swing of $6 on a single trade.

Given the transactional volume ECNs experience, the aggregate effect is considerable. In addition, if an ECN were pinged out on its entire published order, its reserve size would also be pinged out at the same time. That could have a dramatic effect if the pinged-out order were turned into a responding order, since that status would affect any reserve as well. As a result, for example, a client that had a 1,000-share published quotation with a 99,000-share reserve, for a total of 100,000, could find itself having to pay an access fee for the entire 100,000 shares if it were converted into a responding order by the entry of a contra quotation for that entire amount. The participant causing that conversion could be either a market maker or a competing UTP exchange.

Nasdaq's amendment purports to reduce the adverse impact of decrementation on ECNs participating in SuperMontage. In practice, there is no improvement at all. Under the new proposal, Nasdaq would allow order delivery participants to quote multiple "orders" at a single price level, rather than the single quote per price level permitted today. Each "order", however, would be subjected to the same decrementation logic currently in force; a rejection of any portion of an order would result in the removal of each associated quotation in its entirety. Far from solving the fundamental problems posed by decrementation, this proposal simply magnifies them and distributes them across multiple quotations.

The proposed amendment would yield the exact same result for a single order. If an ECN had a single order of 1,000 shares at a price level, a 300-share delivery and rejection (or, for that matter, a 1-share delivery and rejection) would also result in the complete removal of the remaining 700 shares. Nasdaq's amendment would make it possible for the first time to quote multiple, separate orders at a single price level. Each of these orders is treated separately, exactly as they would be under the current rule. For example, if an ECN published two quotations, each for 1,000 shares at the same price level and 300 shares were delivered and rejected, then one of the orders would be entirely deleted from the system. The remaining 1,000-share order would not be affected.

No ECN that quotes in Super Montage breaks its orders up in this manner, nor, to the best of our knowledge, has any ECN requested this change. Since they must maintain their own internal matching engines separate and apart from SuperMontage, ECNs aggregate their trading interests at price levels and handle the allocation of separate orders internally. Therefore, Nasdaq's proposal is of no practical use or benefit for any existing ECN that quotes in Super Montage.

In addition, under both the current rule and the proposed amendment, a firm that knows its orders will be blocked automatically by an ECN whose access fees the firm will not pay can send the 1,000-share order to the ECN, or indeed a much larger order, without risking an execution. As a result, the proposed Nasdaq amendment to the decrementation rule will not have any practical effect since a firm seeking to knock an ECN out of the quote will be able to do so as before regardless of the size of the ECN's published quotation.

We recognize that Nasdaq is interested in not having the access fee issue, which is the root cause of decrementation, stand in the way of an efficient market. Bloomberg Tradebook has long taken the position that access fees are not useful and should be eliminated across the board, including those imposed by SuperMontage and all other market centers (e.g., exchanges, ECNs, ATSs, the Alternative Display Facility).

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We appreciate the opportunity to make our views known to the Commission and the staff and we hope that our letter is helpful. If members of the Commission or of the staff believe we may be of further assistance in these matters, please let us know.

Very truly yours,

BLOOMBERG TRADEBOOK LLC

By: Kim Bang by RDB

cc: The Hon. William H. Donaldson, Chairman
The Hon. Paul S. Atkins, Commissioner
The Hon. Cynthia A. Glassman, Commissioner
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