

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-52148; File No. SR-NASD-2005-56)

July 28, 2005

Self-Regulatory Organizations; National Association of Securities Dealers, Inc.; Order Approving Proposed Rule Change and Amendment No. 1 thereto Eliminating the Directed Order Process in the Nasdaq Market Center

On April 21, 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"), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> a proposed rule change to eliminate the Directed Order Process in the Nasdaq Market Center. On May 2, 2005, Nasdaq filed Amendment No. 1 to the proposed rule change. The proposed rule change was published for comment in the Federal Register on May 16, 2005.<sup>3</sup> The Commission received no comments on the proposal.<sup>4</sup>

The Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a registered securities association.<sup>5</sup> In particular, the Commission believes<sup>5</sup> that the proposed rule change is consistent

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<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> See Securities Exchange Act Release No. 51668 (May 11, 2005), 70 FR 25869 ("Notice").

<sup>4</sup> The Commission notes that Nasdaq also proposed to eliminate the Directed Order Process in File No. SR-2004-181. The Commission has received one comment letter on that proposal. See letter to Jonathan G. Katz, Secretary, Commission, from Mary Yeager, Assistant Secretary, New York Stock Exchange, dated January 10, 2005. The comment letter raised issues regarding Nasdaq's application to register as a national securities exchange and did not specifically address any issues relating to the elimination of the Directed Order Process. The Commission expects Nasdaq to file an amendment to File No. SR-NASD-2004-181 to reflect the Commission's approval of this proposed rule change.

<sup>5</sup> In approving this proposal, the Commission considered the proposed rule's impact on efficiency, competition and capital formation. 15 U.S.C. 78c(f).

with Section 15A(b)(6) of the Act<sup>6</sup> 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.

Nasdaq proposes to eliminate the Directed Order Process from the Nasdaq Market Center. The Directed Order Process, which replicates the SelectNet functionality that pre-dated the implementation of the Nasdaq Market Center, operates independent of the Non-Directed Order Process. Specifically, the Directed Order Process is used by members to negotiate trades and allows orders to be executed at prices inferior to the best prices displayed in the Nasdaq Market Center. In addition, because the Directed Order Process is not integrated within the order execution algorithm for the Non-Directed Order Process, Directed Order trades are executed without consideration of the price-time priority of orders in the Non-Directed Order Process.

Because the Directed Order Process allows orders to bypass limit orders that have price priority and/or time priority, its elimination will enhance the protection of limit orders in the Nasdaq Market Center. Accordingly, the Commission believes that this proposed rule change may result in increased liquidity. In addition, the Commission notes that Nasdaq represented that it believes that it is now appropriate to retire the Directed Order Process from the Nasdaq Market Center in light of the recent elimination of Nasdaq's pre-open Trade-or-Move requirements which obligated market participants to send Directed Orders containing a Trade-or-Move message.

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<sup>6</sup> 15 U.S.C. 78q-3(b)(6).

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,<sup>7</sup> that the proposed rule change (File No. SR-NASD-2005-056) be, and hereby is, approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>8</sup>

Margaret H. McFarland  
Deputy Secretary

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<sup>7</sup> 15 U.S.C. 78s(b)(2).

<sup>8</sup> 17 CFR 200.30-3(a)(12).