

March 18, 2003

Ms. Kathryn L. Beck  
Senior Vice President, General Counsel,  
Chief Regulatory Officer  
Pacific Exchange  
115 Sansome Street  
San Francisco, CA 94104

RE: Vendor Display Rule Requirements and the Upcoming Change to NQDS

Dear Kathryn:

On March 31 the Nasdaq Stock Market, acting as the SIP for the Nasdaq UTP Plan, will discontinue the current NQDS datafeed that contains best bids and offers from all markets and market makers quoting Nasdaq securities. As a result, as of this date quotation data from the Nasdaq Stock Market and the Chx, which participates in SuperMontage; from the ADF; and from exchanges trading Nasdaq securities via UTP and not participating in SuperMontage (the Amex, CSE, and PCX/ARCA) will be carried on three separate datafeeds, called NQDS, OMDF, and UQDF, respectively.

As has been discussed in the UTP Committee, the change to NQDS raises issues concerning both vendor and broker-dealer compliance with Rule 11Ac1-2 (the "Display Rule" or "DR") under the Securities Exchange Act of 1934 (the "Act"). I am writing this letter to clarify what the DR requires of vendors and broker-dealers in an environment without a datafeed that contains quotations from all markets and market makers quoting a Nasdaq security, and to ask that you communicate the contents of this letter to your members sufficiently in advance of March 31 that they will understand what their compliance obligations will be as of that date.

#### *Vendors*

With respect to quotation displays,<sup>1</sup> the DR requires, among other things, that: (1) vendors choosing to provide quotation data either provide a consolidated BBO or a quotation montage (see 11Ac1-2(c)(2)(i)); (2) any consolidated quotation display be equally accessible (see 11Ac1-2(c)(2)(ii)); and (3) any consolidated quotation display not exclude any individual market's quotations, with an exception with respect to third market makers not relevant here (see 11Ac1-2(c)(2)(iv)).

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<sup>1</sup> This letter does not address issues relating to interrogation devices.

The Division believes that a vendor may satisfy its obligation to provide a consolidated quotation display with respect to a Nasdaq-listed security by providing any of the following:

- The NBBO derived from all reporting market centers, including UTP Exchanges, Nasdaq quoting participants, and ADF quoting participants;
- A quotation montage consisting of each Exchange BBO, the Nasdaq BBO, and the ADF BBO; or
- A quotation montage including each Exchange BBO, the individual quotations of each Nasdaq quoting participant, and the individual quotations of each ADF quoting participant.

A vendor may not disseminate a quotation montage for a Nasdaq-listed security (whether as the consolidated quotation display or as a separate quotation montage) that includes the individual quotations of Nasdaq quoting participants, unless the vendor also includes in that quotation montage each Exchange BBO and the individual quotations of each ADF quoting participant. Thus:

- Vendors that propose to disseminate a quotation montage for a Nasdaq-listed security that consists of the individual quotations of market centers represented in the NQDS feed must also include in the same montage the individual quotations of each ADF quoting participant in the OMDF feed; and
- After, March 31, vendors that propose to disseminate a quotation montage for a Nasdaq-listed security consisting of the quotations of Nasdaq and ADF quoting participants must also include in the same montage the BBO of each UTP Exchange from the UQDF feed.

We understand that at least one vendor will not be able to comply with the requirements of the DR with the change to NQDS that will be implemented on March 31. We expect to issue a no-action letter to that vendor in which the Division will indicate that it will not recommend enforcement action against this vendor if that vendor provides its customers that use quotation montages for Nasdaq securities that consist of data other than market center BBOs the ability to retrieve and display quotations from all markets trading a Nasdaq security simultaneously, dynamically, and equally prominently to individual market maker's quotations in that security. Such no-action relief will expire no later than July 31, 2003.

*Broker-Dealers*

11Ac1-2(e) of the DR subjects broker-dealers to the same quotation maintenance and display requirements that apply to vendors, with certain exceptions not relevant here. Therefore, in order to comply with the DR as of March 31, broker-dealers that use quotation montages in Nasdaq securities that contain individual market maker quotations must also integrate into such montages quotation data from all markets trading Nasdaq securities. Broker-dealers that use the data vendor to whom we expect to issue the no-action letter described above, or that use other vendors to whom we may issue similar letters, and the individuals within the firm making quotation or order routing decisions, must maintain and display the data display service described as a condition of the no-action letter. That is, if broker-dealers use a quotation montage that contains individual market maker quotations when entering quotes or routing orders for Nasdaq securities, they must have readily available for retrieval simultaneously, dynamically, and in an equally prominent manner quotations from all markets trading such stocks and the individuals within the firm entering quotations or making order routing decisions must, if they use a quotation montage in performing such functions that contains individual market maker's quotations, actually display simultaneously, dynamically, and equally prominently, quotations from all markets trading Nasdaq securities at the time they are entering quotations or routing orders. Since any DR no-action relief will expire on July 31, 2003, broker-dealer customers of affected vendors will need to obtain and use fully integrated quotation display services by that date to be in compliance with the DR.

*Communications*

We request that you communicate the contents of this letter to your membership as quickly as possible so that they have as much advance notice of this letter as possible prior to March 31, 2003. To allow you to disseminate this letter to your members electronically, we are sending this letter to you electronically.

Sincerely,

Robert L.D. Colby  
Deputy Director