



INVESTMENT COMPANY INSTITUTE

CRAIG S. TYLE
GENERAL COUNSEL

June 19, 2003

Mr. Jonathan G. Katz
Secretary
Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, DC 20549-0609

*Re: Commission Request For Comment on Nasdaq Petition Relating to the
Regulation of Nasdaq-Listed Securities (File No. S7-11-03)*

Dear Mr. Katz:

The Investment Company Institute¹ appreciates the opportunity to comment on the Securities and Exchange Commission's concept release regarding the regulation and trading of Nasdaq-listed and exchange-listed securities.² The Concept Release is in response to a petition from the Nasdaq Stock Market requesting that the Commission take certain actions to respond to, according to Nasdaq, the greater fragmentation of trading and regulation in Nasdaq-listed securities. In particular, Nasdaq requests that the Commission, among other things, establish uniform trading rules and address the exchanges' costs of regulation and self-regulatory structure.

The issues raised by the Concept Release are important ones, both for the proper functioning of the securities markets and the development of the future market structure. Given the short time frame to address these complex issues, however, we will focus our comments on the issue most directly impacting our members – the debate over uniform trading rules.

Nasdaq requests that the Commission act immediately to establish uniform trading rules because of its concern that investors are potentially harmed by the lack of such rules. The Institute believes that uniform trading rules governing certain issues, such as those that go to the core of investor protection principles and that are designed to prevent violations of the securities laws, can prove beneficial to the securities markets and investors. For example, we agree with Nasdaq that the Commission should ensure

¹ The Investment Company Institute is the national association of the American investment company industry. Its membership includes 8,688 open-end investment companies ("mutual funds"), 556 closed-end investment companies, 110 exchange-traded funds and 6 sponsors of unit investment trusts. Its mutual fund members have assets of about \$6.475 trillion, accounting for approximately 95% of total industry assets, and 90.2 million individual shareholders.

² Securities Exchange Act Release No. 47849 (May 14, 2003), 68 FR 27721 (May 20, 2003) ("Concept Release").

that all markets have rules adequate to address, among other things, activities prohibited by the Exchange Act, market manipulation, and compliance with the limit order display and firm quote rules. If the lack of uniformity in these areas, as well as in other areas such as rules relating to order audit trail information, are hindering the detection of securities laws violations, the Commission should reexamine these issues and determine if uniform rules would best protect investors.

Uniform trading rules for all aspects of trading, however, could hinder competition and act to the detriment of investors. We have already seen examples of this, as evidenced by certain rules in place today. For example, in the listed market, each market participating in the Intermarket Trading System ("ITS") is required to adopt a trade-through rule substantially the same as the trade-through rule in the ITS Plan (the plan governing the terms of the intermarket linkage). These "uniform" rules, however, have arguably created barriers to competition and have impeded efficient trade execution.

While we still believe that, in the long-term, intermarket price/time priority should be implemented, given the disparities that exist among markets in terms of technology, trade-through rules can serve to protect less efficient markets at the expense of more efficient trading venues. We therefore believe that allowing automatic execution participants to trade through manual participants in the listed market for a *de minimis* amount, is an idea worthy of consideration. As the Commission stated in its order granting a similar exemption from the trade-through rules for certain exchange-traded funds,³ the ITS trade-through provisions were designed both to encourage market participants to display their trading interest and to help achieve best execution for customer orders in exchange-listed securities. The trade-through rule, in its current form, does not further either of these goals.⁴ A *de minimis* exemption to the trade-through rules can help address the problem of forcing an investor to send its order to a market that, for example, is slow in executing orders.⁵ Such an exemption also would provide investors with a choice as to whether they want to execute their trades at the market with the best price, or execute their trade in a different market if they believe speed or certainty of execution, for example, were more important for a particular trade.⁶

³ Securities Exchange Act Release No. 46428 (August 28, 2002). *See also* Securities Exchange Act Release No. 47950 (May 30, 2003) (extension of *de minimis* exemption for exchange-traded funds).

⁴ SEC Commissioner Atkins, in a recent speech, stated that "the ITS trade-through rule may in fact prevent individual investors and professional traders from obtaining an execution that meets their needs." Speech by SEC Commissioner Atkins before the American Enterprise Institute, May 7, 2003.

⁵ This could harm an investor as orders displayed in other markets could be cancelled while it is waiting for the first order to be executed.

⁶ The Commission also requests comment on how it should address any regulatory gaps that can arise when trading in the same security is fragmented across different SROs and what may be the best self-regulatory model for the markets. While we do not have a definitive view at this time as to the best approach, as we have previously stated, we believe there should be at least a strict separation of the self regulatory role from the marketplace it oversees. *See* Letter from Matthew P. Fink, President, Investment Company Institute, to Arthur Levitt, Chairman, Securities and Exchange Commission, dated October 13, 1999.

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The Institute appreciates the opportunity to comment on the Concept Release. Any questions regarding our comments may be directed to the undersigned at 202-326-5815 or to Ari Burstein at 202-371-5408.

Sincerely,



Craig S. Tyle
General Counsel

cc: The Honorable William H. Donaldson
The Honorable Paul S. Atkins
The Honorable Roel C. Campos
The Honorable Cynthia A. Glassman
The Honorable Harvey J. Goldschmid

Annette L. Nazareth, Director
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