

May 12, 2000

Mr. Jonathan G. Katz, Secretary
Securities and Exchange Commission
450 Fifth Street, NW
Washington, D.C. 20549-0609

**Re: Commission Request for Comment on Issues Relating to Market
Fragmentation; Release No. 34-42450; File No. SR-NYSE-99-48**

Dear Secretary Katz:

Please accept this comment letter on behalf of the North American Securities Administrators Association (“NASAA”)¹ regarding the above-referenced concept release (the “Release”). We commend the staff of the Division of Market Regulation for addressing the important issue of whether fragmentation is, or will become, a problem for the U.S. capital markets and allowing public comment on possible scenarios to address fragmentation within the markets.

NASAA supports a market structure that provides investors with full and fair trading access, disclosure and interaction, including increased price competition and reduced transaction costs. Because NASAA’s mission is to protect investors and promote fair and open capital markets, we are concerned about the prospect of fragmentation due to the fast changing landscape of the securities markets brought about by technological transformations and the possible impact fragmentation could have on the markets. Yet, without the threat of competition by other newly-created and technologically advanced markets, the traditional U.S. markets might otherwise have grown stale and offered less opportunity and fewer benefits than we see today. Thus, some fragmentation may be inevitable and even necessary to provide for an element of competition in the markets to create and maintain an incentive for the markets to constantly improve. However, care must be taken that technological changes and alternatives do not overwhelm investors or

¹ NASAA is the association of the 66 state, provincial and territorial securities regulatory agencies of the United States, Canada and Mexico. NASAA serves as a forum for state regulators to work with each other in an effort to protect investors at the grassroots level and to promote fair and open capital markets.

impose undue costs upon them. We agree with the Commission that there must be fair and efficient securities markets for investor protection.

As noted by the Commission in the Release, there are market structure components currently in place to address fragmentation. These include price transparency, intermarket linkages to displayed prices and a broker's duty of best execution. However, as also noted by the Commission, these components have many weaknesses, making them insufficient.

For example, a broker's duty of best execution is based not just on price but also on the certainty and timing of the execution of the trade. Thus, a broker's obligation of "best execution" does not automatically prescribe a particular market center for execution. Also, the current intermarket linkages to displayed prices represent only a small portion of the trading volume in listed equities and Nasdaq equities. For example, as noted in the Release, the Intermarket Trading System (ITS) represents approximately only 2% of total NYSE-listed trades and has limited Electronic Communication Network (ECN) access. Overall, the current system of intermarket linkages does not provide for intermarket time priority, nor intermarket priority for investor limit orders over market makers' trading and, although the intermarket linkages provide access to the best displayed prices, they do not require orders to be routed to the market center displaying best price.

The Commission requests comments on two specific issues in this area: (1) "whether the first trading interest to improve the National Best Bid and Offer ("NBBO") should be entitled to intermarket time priority" and (2) "whether market makers should be prohibited from trading ahead of previously displayed and accessible investor limit orders, no matter where such orders are held in the national market system." NASAA strongly supports both of these premises. In order to expect individual investors to continue to invest in the U.S. capital markets, they must have confidence in the fairness of the markets, which means that they will receive the benefit of their actions including trade execution based upon time priority and at least equal footing with market makers.

Other areas of concern to NASAA are the current practices of internalization and payment for order flow. Although the Commission indicated in the Release that there are benefits associated with these practices, such as increased speed, certainty and cost of execution, NASAA looks forward to seeing the comments and statistics on these issues. Such practices would appear to deter the incentive for price improvement, especially as it relates to payment for order flow because the market center that displays the best price will most likely not get the order flow.

The infusion of technological change into our markets cannot be ignored and will continue to promote competitive forces. If we can harness those forces only as necessary to promote fair and efficient securities markets for all market participants, the markets will continue to flourish and provide opportunities for all. We believe that this Release provides an important opportunity for all interested parties to participate in the evaluation of how to appropriately guide the securities marketplace for the future.

If NASAA can be of further assistance, please do not hesitate to contact me directly at 317-232-6681 or Karen O'Brien, NASAA General Counsel at 202-737-0900.

Respectfully Yours,

Bradley W. Skolnik
NASAA President