

The Island ECN



The Island ECN

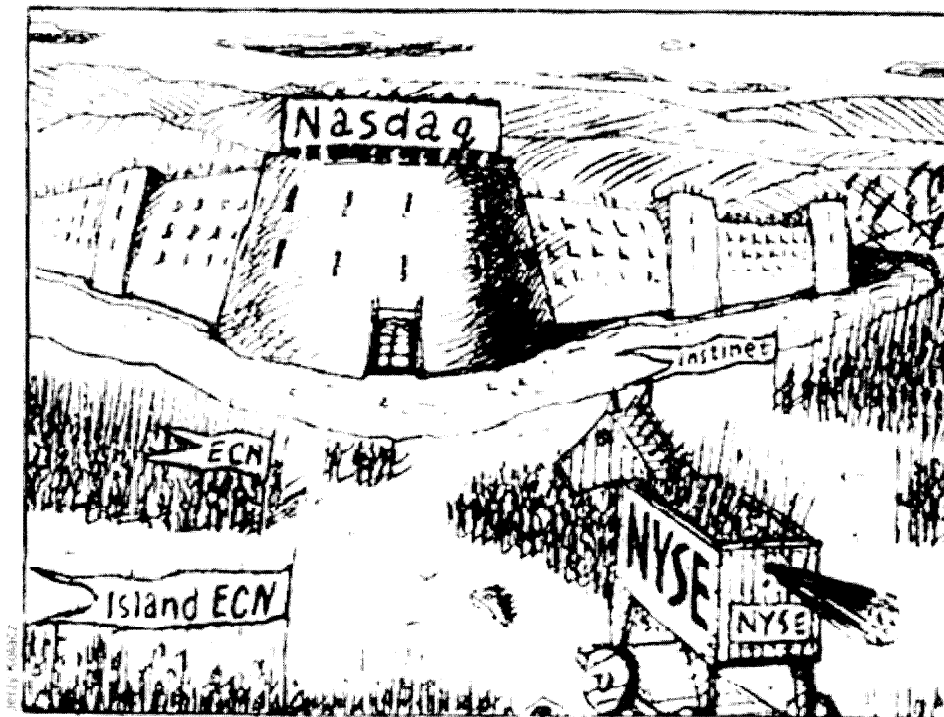
Island Highlights

- Founded in 1996, the Island is the fastest growing ECN and the second largest ECN after Instinet. Accounts for almost 12% of Nasdaq's daily trade volume.
- Over 200 brokerage firms are direct subscribers, virtually all others over SelectNet.
- Transacts \$5 billion in volume and matches over 100 million shares daily.
- The first ECN to offer extended hours trading for individuals. Currently Island is open from 8:00am-8:00pm.



The Island ECN

The Landscape



Source: Wall Street Journal



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Order Handling Rules Bring Sweeping Changes

- The Order Handling Rules: Two main components:
 1. ***Limit Order Display Rule*** - customer limit orders that better a market maker's own quote must then be reflected in that market maker's quote, or forwarded to another entity that will display the order
 2. ***Amended Quote Rule with the Electronic Communications Network (ECN) Alternative*** - market makers cannot place one quote in Nasdaq and a different one into an ECN, unless the ECN makes its best prices viewable and accessible to all Nasdaq market participants



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Structural Change Creates Opportunity

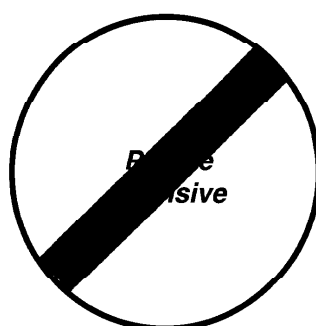
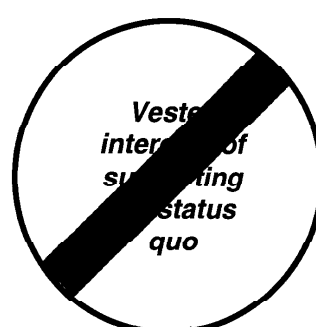
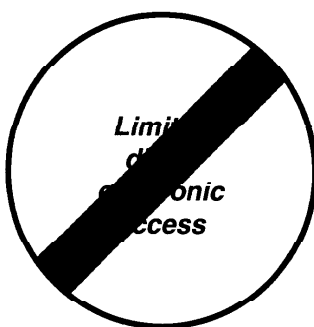
What is an ATS/ECN?

Alternative Trading Systems (ATS) allow for two market participants to meet directly without an intermediary. The systems are owned and operated by third parties. ECNs are a subset of ATSS. ECNs are differentiated by other ATSS in that they continuously disseminate firm, accessible orders. There are currently nine ECNs which all function as limit order books following price-time priority.



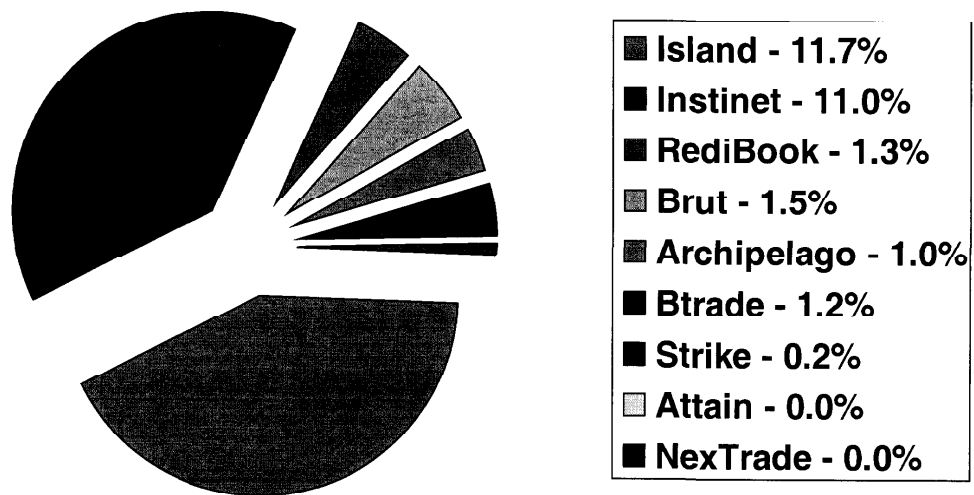
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What's Wrong With The Old System



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**ECNs Represented 28.0% of all
Nasdaq Trades: September 1999**



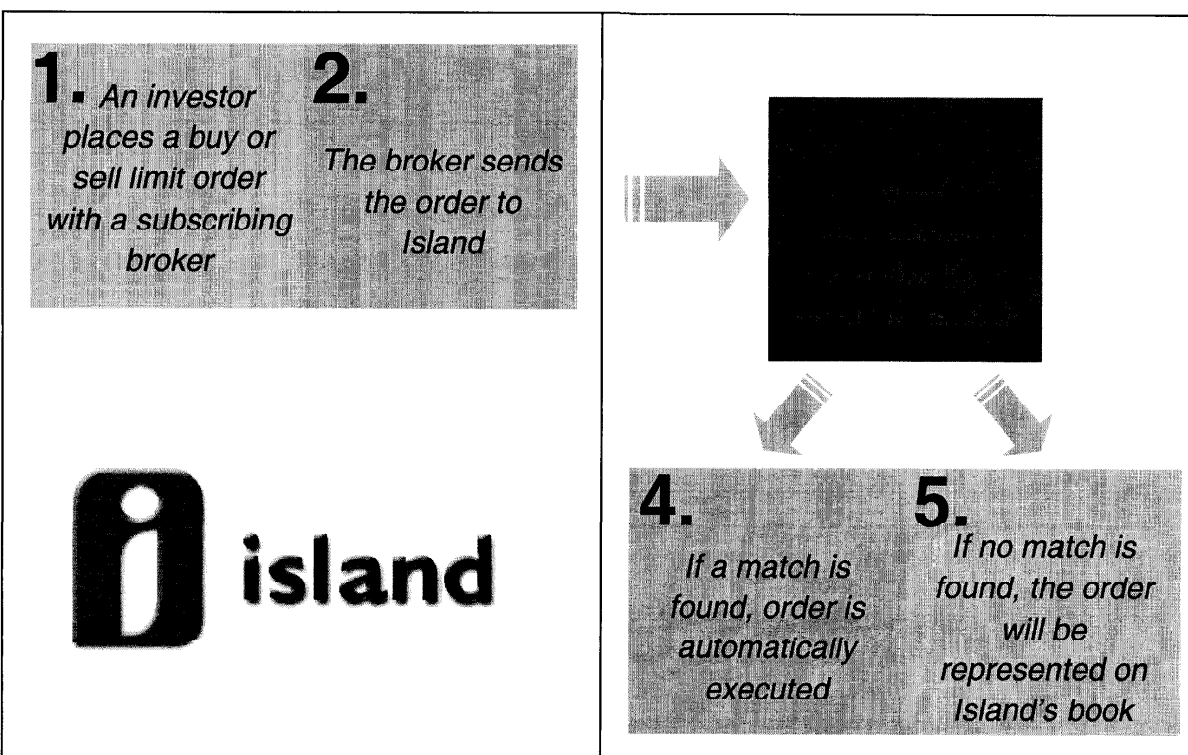
Source: NASD



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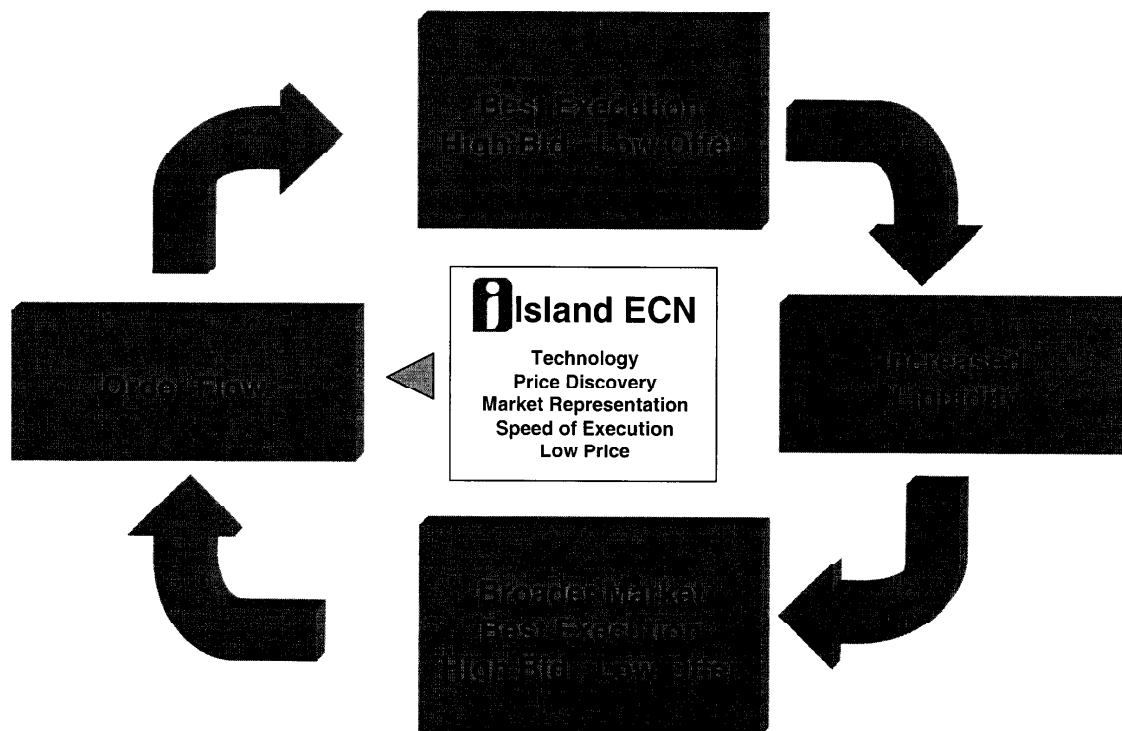
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How Island Works: Powerful Simplicity



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Virtuous Cycle



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Fairness

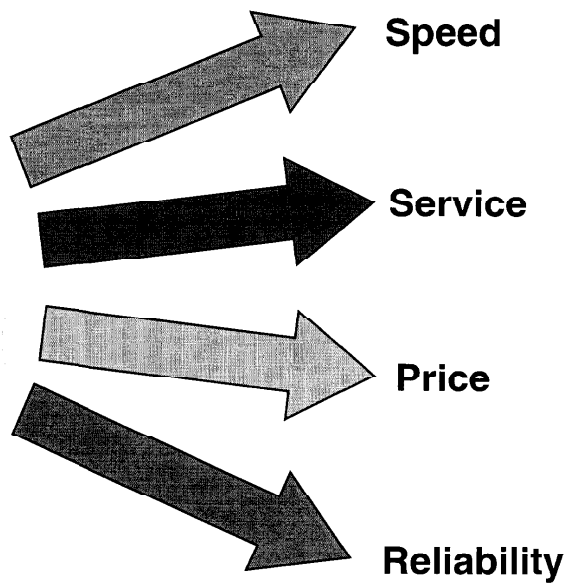
- Limit order book available to all, real-time on Web
- Anonymity preserved throughout process
- Open architecture platform
- Direct electronic access - no middleman
- Only limit orders accepted
- Auction market
- Competition for investor's order



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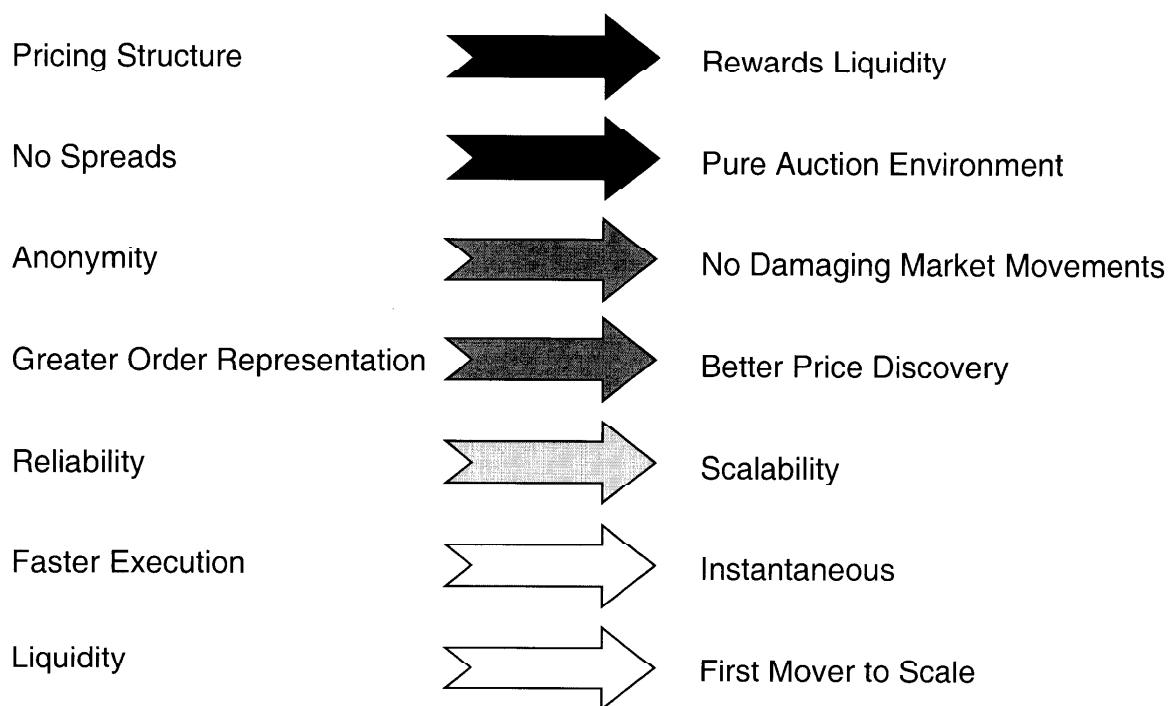
Island's Advantages

**Island competes for
orders based on:**



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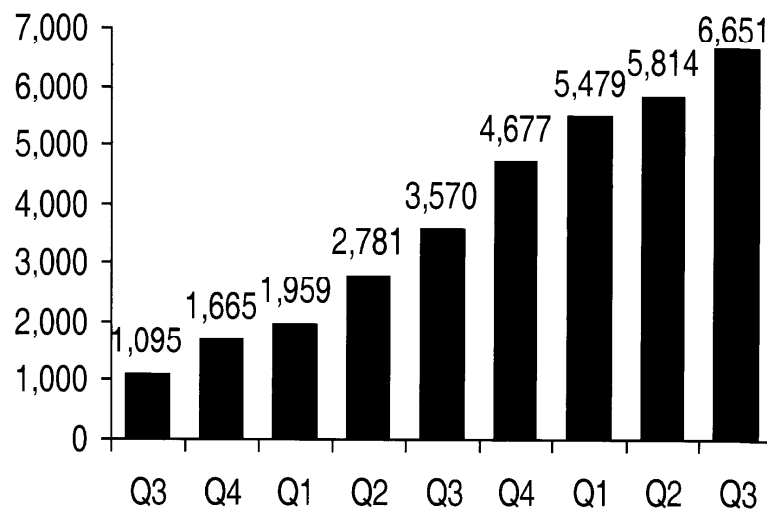
Island's Advantages



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Historical Growth

Shares Executed by Island
Q3 1997 - Q3 1999 (Shares in Millions)



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Why Volumes will Continue to Surge



The diagram features a central dark oval containing the text 'Emerging and Future Trends'. Below this oval, five text elements are arranged: 'Movement to shorter settlement cycles' and 'Decimalization' are positioned higher and further apart, while 'Extended trading hours', 'Wider global access to U.S. markets', and 'Broadband Internet access' are positioned lower and closer together. Two large, light-gray, textured triangular shapes are placed on the left and right sides of the lower three text elements, pointing towards the center.

Emerging and Future Trends

*Movement
to shorter
settlement
cycles*

Decimalization

*Extended
trading
hours*

*Wider global
access to U.S.
markets*

*Broadband
Internet
access*



The Island ECN

Growing Liquidity

- Island often drives the National Best Bid and Offer.
- In many of the most active Nasdaq stocks, Island is the number one daily market participant ahead of all other market makers and ECNs.

September 1999

| <i>Stock</i> | <i>Volume</i> | <i>Rank</i> | <i>% of Total Volume</i> |
|--------------|---------------|-------------|--------------------------|
| AMZN | 58,700,731 | 1 | 18% |
| YHOO | 34,219,474 | 1 | 19% |
| INTC | 33,616,165 | 1 | 6% |
| EBAY | 31,044,560 | 1 | 23% |
| QCOM | 26,948,793 | 1 | 18% |
| CMGI | 19,386,346 | 1 | 18% |

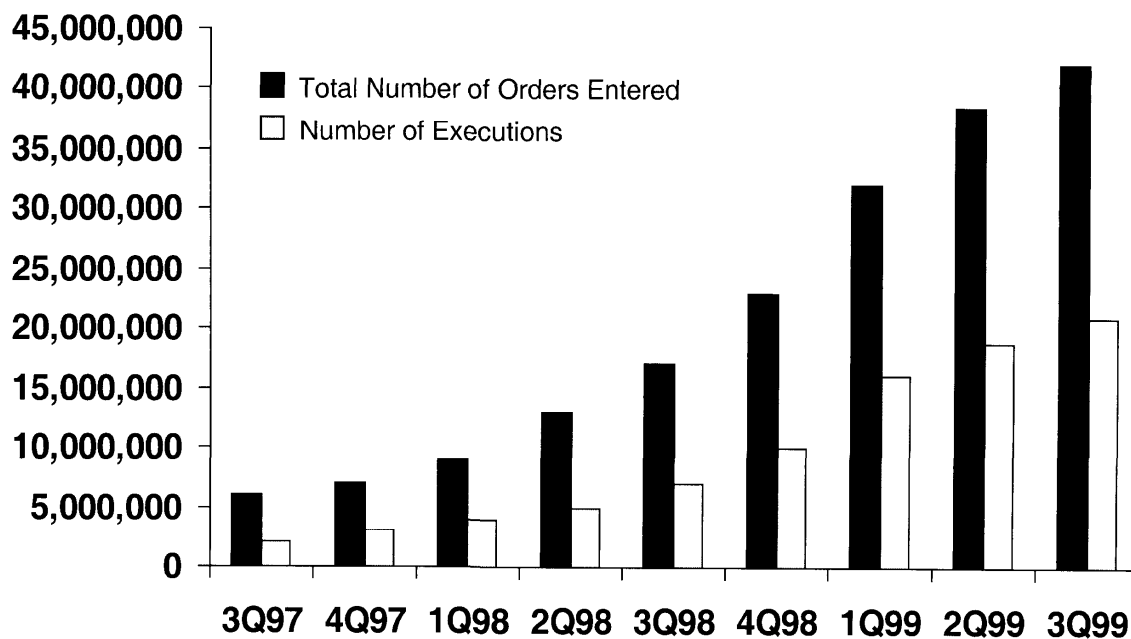
Source: NasdaqTrader.com



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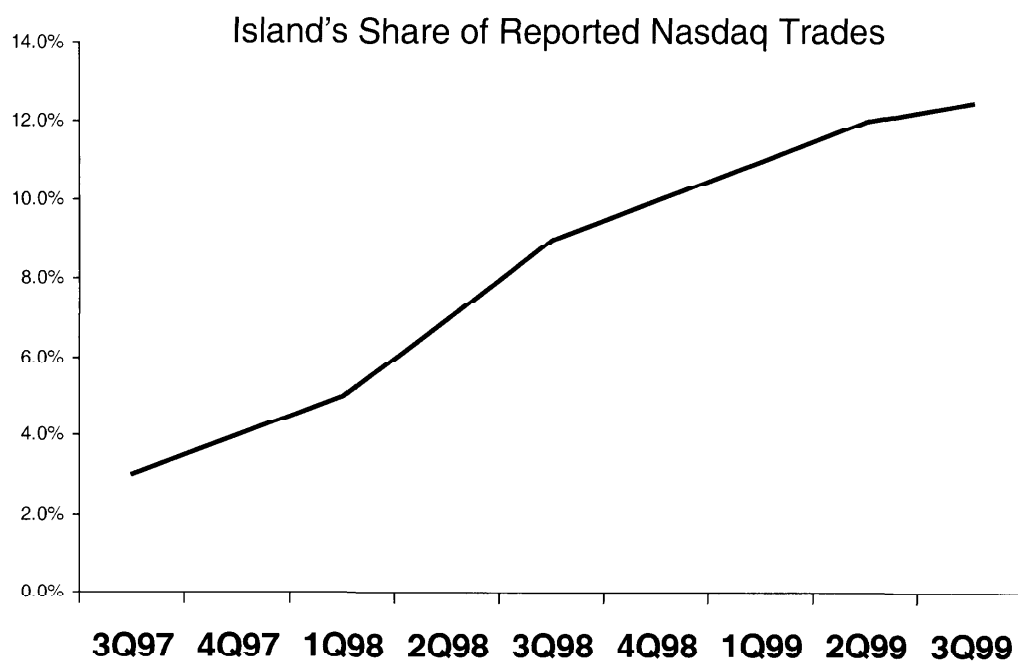
Growing Liquidity

Orders Entered and Executions



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Rising Market Share



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Drivers of Future Growth

Customers

- Current customer base
- New sales-generated customers including broker/dealers and institutions
- Strategic broker/dealer partners

New Business Lines

- Institutional services
- Trading in NYSE and American Stock Exchange listings
- After-hours trading
- Market data (conditional upon Island becoming an exchange)



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Exchange Related Considerations

Exchange Filing

- Island applying to become a self-regulated stock exchange

Why?


- To benefit from impartial regulation
- To match orders for NYSE-listed stock

Next Steps

- Developing regulatory infrastructure
- Holding discussion with SEC
- Anticipating careful SEC review



The Island ECN

| | | | |
|--|-----------|------------------|-----------|
| Island Book - Microsoft Internet Explorer | | | |
| island home | | system stats | help |
|  INTC | | GET STOCK | |
| | | INTC | go |
| LAST MATCH | | TODAY'S ACTIVITY | |
| Price | 79 3/16 | Orders | 10,625 |
| Time | 15:39:31 | Volume | 1,591,774 |
| BUY ORDERS | | SELL ORDERS | |
| SHARES | PRICE | SHARES | PRICE |
| 1,000 | 79 9/64 | 400 | 79 1/4 |
| 200 | 79 9/64 | 1,000 | 79 1/4 |
| 1,000 | 79 9/64 | 600 | 79 5/16 |
| 1,000 | 79 33/256 | 300 | 79 31/64 |
| 300 | 79 1/8 | 488 | 79 1/2 |
| 200 | 79 1/8 | 15 | 79 5/8 |
| 1,000 | 79 1/8 | 20 | 79 3/4 |
| 100 | 79 1/8 | 100 | 79 15/16 |
| 200 | 79 | 30 | 80 |
| 100 | 79 | 120 | 80 1/4 |
| 50 | 79 | 400 | 80 5/16 |
| 125 | 78 3/4 | 200 | 80 7/16 |
| 500 | 78 3/4 | 17 | 80 1/2 |
| 2,000 | 78 5/8 | 26 | 80 1/2 |
| 500 | 78 5/8 | 100 | 80 1/2 |
| (67 more) | | (115 more) | |
| As of 15:39:33 | | | |



The Island ECN

Future Challenges to Island

The Move Upmarket

- Began serving Niche Market (technologically sophisticated investors) and now must serve more mainstream market participants.
 - Odd Lots
 - FIX
 - Front-end
 - Increase staff to add additional services



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www.island.com



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