

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-54063]

### Order Pursuant to Section 11A of the Securities Exchange Act of 1934 and Rule 608(e) Thereunder Extending a *De Minimis* Exemption for Transactions in Certain Exchange-Traded Funds From the Trade-Through Provisions of the Intermarket Trading System

June 28, 2006.

This order extends, through February 4, 2007, a *de minimis* exemption to the provisions of the Intermarket Trading System Plan ("ITS Plan"),<sup>1</sup> a national market system plan,<sup>2</sup> governing intermarket trade-throughs that currently is due to expire on June 28, 2006. The *de minimis* exemption was originally issued by the Commission on August 28, 2002<sup>3</sup> and extended on May 30, 2003,<sup>4</sup> on March 3, 2004,<sup>5</sup> on December 3, 2004,<sup>6</sup> and on September 6, 2005.<sup>7</sup>

<sup>1</sup> The self-regulatory organizations ("SROs") participating in the ITS Plan include the American Stock Exchange LLC, the Boston Stock Exchange, Inc., the Chicago Board Options Exchange, Inc., the Chicago Stock Exchange, Inc., the National Stock Exchange, Inc. (formerly the Cincinnati Stock Exchange, Inc.), the National Association of Securities Dealers, Inc. ("NASD"), the New York Stock Exchange, Inc., the Pacific Exchange, Inc., and the Philadelphia Stock Exchange, Inc. (collectively, the "participants"). See Securities Exchange Act Release No. 19456 (January 27, 1983), 48 FR 4938 (February 3, 1983).

<sup>2</sup> Securities Exchange Act of 1934 ("Act") Rule 608(c) (formerly Rule 11Aa3-2(d)), 17 CFR 242.608(c), promulgated under Section 11A, 15 U.S.C. 78k-1, of the Act requires each SRO to comply with, and enforce compliance by its members and their associated persons with, the terms of any effective national market system plan of which it is a sponsor or participant. Rule 608(e) (formerly Rule 11Aa3-2(f)), 17 CFR 242.608(e), under the Act authorizes the Commission to exempt, either unconditionally or on specified terms and conditions, any SRO, member of an SRO, or specified security from the requirement of the rule if the Commission determines that such exemption is consistent with the public interest, the protection of investors, the maintenance of fair and orderly markets and the removal of impediments to, and perfection of the mechanisms of, a national market system.

<sup>3</sup> See Securities Exchange Act Release No. 46428 (August 28, 2002), 67 FR 56607 (September 4, 2002) (the "August 2002 Order"). The August 2002 Order granted relief through June 4, 2003.

<sup>4</sup> See Securities Exchange Act Release No. 47950 (May 30, 2003), 68 FR 33748 (June 5, 2003) (the "May 2003 Order"). The May 2003 Order granted relief through March 4, 2004.

<sup>5</sup> See Securities Exchange Act Release No. 49356 (March 3, 2004), 69 FR 11057 (March 9, 2004) (the "March 2004 Order"). The March 2004 Order granted relief through December 4, 2004.

<sup>6</sup> See Securities Exchange Act Release No. 50795 (December 3, 2004), 69 FR 71445 (December 9, 2004) (the "December 2004 Order"). The December 2004 Order granted relief through September 4, 2005.

<sup>7</sup> See Securities Exchange Act Release No. 52382 (September 6, 2005), 70 FR 53695 (September 9,

Specifically, this order continues the *de minimis* exemption from compliance with Section 8(d)(i) of the ITS Plan with respect to two specific exchange-traded funds ("ETFs"), the Dow Jones Industrial Average ETF ("DIA") and the Standard & Poor's 500 Index ETF ("SPY").<sup>8</sup> By its terms, the September 2005 Order continued the exemption from the trade-through provisions of the ITS Plan of any transactions in the two ETFs that are effected at prices at or within three cents away from the best bid and offer quoted in the Consolidated Quote System ("CQS") through June 28, 2006.

In the Commission's previous orders to issue and extend the *de minimis* exemption,<sup>9</sup> the Commission discussed its basis for determining that the *de minimis* exemption is consistent with the public interest, the protection of investors, the maintenance of fair and orderly markets and the removal of impediments to, and perfection of the mechanisms of, a national market system. In the September 2005 Order, the Commission further noted that:

In March 2004 and in May 2003, the Commission extended the three cent *de minimis* exemption for additional nine-month periods, in order to assess trading data associated with the *de minimis* exemption and to consider whether to adopt the *de minimis* exemption on a permanent basis, to adopt some other alternative solution, or to allow the exemption to expire. As a result of its review of trading data associated with the *de minimis* exemption, the Commission has proposed, as part of its market structure initiatives, Regulation NMS under the Act, which would include a new rule relating to trade-throughs.

On April 6, 2005, the Commission approved Regulation NMS under the Act.<sup>10</sup> In Regulation NMS, the Commission adopted an approach that, among other things, protects only

2005) (the "September 2005 Order"). The September Order granted relief through June 28, 2006.

<sup>8</sup> The Commission limited the *de minimis* exemption to these two securities because they share certain characteristics that may make immediate execution of their shares highly desirable to certain investors. In particular, trading in the two ETFs is highly liquid and market participants may value an immediate execution at a displayed price more than the opportunity to obtain a slightly better price. Unlike prior orders, the December 2004 and September 2005 extensions of the *de minimis* exemption applied only to the DIA and the SPY, and not the QQQ, because, on December 1, 2004, trading of the QQQ transferred from the American Stock Exchange to Nasdaq, and thus trades in the QQQ ceased to be subject to the trade-through provisions of the ITS Plan. Accordingly, an exemption for the QQQ was no longer necessary. See December 2004 Order and September 2005 Order.

<sup>9</sup> See *supra* notes 3 to 7.

<sup>10</sup> See Securities Exchange Act Release No. 51808 (June 9, 2005), 70 FR 37496 (June 29, 2005).

automated quotations and excludes manual quotations from trade-through protection, and renders the *de minimis* exemption unnecessary. Given the significant systems and other changes necessary to implement Rule 610 and Rule 611,<sup>11</sup> the Commission originally established delayed compliance dates for Rule 610 and Rule 611, the first of which was scheduled to begin on June 29, 2006.<sup>12</sup> In the September 2005 Order, the Commission stated that until Regulation NMS is implemented, the reasons for maintaining the *de minimis* exemption in effect continue to be valid, and thus the Commission extended the *de minimis* exemption through June 28, 2006, which was the date before the initial compliance date for Rule 610 and Rule 611.

On May 18, 2006, the Commission extended the compliance dates for Rule 610 and Rule 611 to give trading centers additional time to finalize the development of their new or modified trading systems, and to give the securities industry sufficient time to establish the necessary access to such trading systems.<sup>13</sup> The initial compliance date was extended to a series of five dates, beginning on October 16, 2006, for different functional stages of compliance, with February 5, 2007 (the "Trading Phase Date") being the final date for full operation of Regulation NMS-compliant trading systems for initial trade-through protection under Rule 611, as described in the NMS Extension Release.

Therefore, to maintain the status quo and avoid requiring market participants to make short-term trading or programming changes pending the extended implementation period for Rule 610 and Rule 611 of Regulation NMS, it is appropriate to extend the *de minimis* exemption through February 4, 2007, the day before the Trading Phase Date.<sup>14</sup> The Commission emphasizes, as

<sup>11</sup> Rule 610 generally prohibits national securities exchanges and national securities associations from imposing unfairly discriminatory terms that prevent or inhibit access to quotations, and establishes a limit on access fees, and requires each national securities exchange and national securities association to adopt, maintain, and enforce written rules that prohibit their members from engaging in a pattern or practice of displaying quotations that lock or cross protected quotations. Rule 611 requires trading centers to establish, maintain, and enforce written policies and procedures reasonably designed to prevent the execution of trades at prices inferior to protected quotations displayed by other trading centers, subject to an applicable exception.

<sup>12</sup> See *supra* note 10.

<sup>13</sup> Securities Exchange Act Release No. 53829 (May 18, 2006), 71 FR 30037 (May 24, 2006) ("NMS Extension Release").

<sup>14</sup> The Commission expects most trading centers to be operating consistent with the requirements of Rule 611 by the Trading Phase Date.

it did in the previous orders,<sup>15</sup> that the *de minimis* exemption does not relieve brokers and dealers of their best execution obligations under the federal securities laws and SRO rules.

Accordingly, it is ordered, pursuant to Section 11A of the Act and Rule 608(e) thereunder,<sup>16</sup> that participants of the ITS Plan and their members are hereby exempt from Section 8(d) of the ITS Plan during the period covered by this Order with respect to transactions in DIAs and SPYs that are executed at a price that is no more than three cents lower than the highest bid displayed in CQS and no more than three cents higher than the lowest offer displayed in CQS. This Order extends the *de minimis* exemption from June 29, 2006 through February 4, 2007.

By the Commission.

**Nancy M. Morris,**  
Secretary.

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-54066; File No. SR-BSE-2006-24]

### Self-Regulatory Organizations; Boston Stock Exchange, Inc.; Notice of Filing and Immediate Effectiveness of Proposed Rule Change To Extend a Pilot Program That Allows for No Minimum Size Order Requirement for the Price Improvement Period Process on the Boston Options Exchange

June 29, 2006.

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> notice is hereby given that on June 19, 2006, the Boston Stock Exchange, Inc. ("BSE" or "Exchange") filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I, II and III below, which items have been prepared by BSE. The Exchange has designated the proposed rule change as a "non-controversial" rule change pursuant to Section 19(b)(3)(A)(iii) of the Act<sup>3</sup> and Rule 19b-4(f)(6) thereunder,<sup>4</sup> which renders the proposal effective upon filing with the Commission. The Commission is publishing this notice to

solicit comments on the proposed rule change from interested persons.

#### I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

The text of the proposed rule change is below. Proposed new language is underlined; proposed deletions are in [brackets].

\* \* \* \* \*

#### Chapter V, Section 18

##### Supplementary Material to Section 18

.01 During the extended Pilot Period [from August 7, 2005 to July 18, 2006], there will be no minimum size requirement for Customer Orders to be eligible for the PIP process. During this extended Pilot Period, BOXR will continue to submit certain data, periodically as required by the Commission, to provide supporting evidence that, among other things, there is meaningful competition for all size PIP orders, that there is significant price improvement for all orders executed through the PIP, and that there is an active and liquid market functioning on BOX outside of the PIP mechanism. Any data which is submitted to the Commission by BOXR will be provided on a confidential basis. *The Pilot Period shall expire on July 18, 2007.*

.02 No Change.  
\* \* \* \* \*

#### II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the Exchange included statements concerning the purpose of, and basis for, the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. The Exchange has prepared summaries, set forth in Sections A, B, and C below, of the most significant aspects of such statements.

##### A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

###### 1. Purpose

The purpose of the proposed rule change is to extend a Pilot Program under the Rules of the Boston Options Exchange ("BOX") for an additional year. The Pilot Program allows BOX to have no minimum size requirement for orders entered into the Price

Improvement Period ("PIP") process.<sup>5</sup> The proposed rule change retains the text of Supplementary Material .01 to Section 18 of Chapter V of the BOX Rules and seeks to extend the operation of the PIP Pilot Program until July 18, 2007.

The Exchange notes that the PIP Pilot Program provides small customer orders with benefits not available under the rules of other exchanges. One of the important factors of the PIP Pilot Program is that it guarantees members the right to trade with their customer orders that are less than 50 contracts. In particular, any order entered into the PIP is guaranteed an execution at the end of the auction at a price at least a penny better than the national best bid or offer.

In further support of this proposed rule change, and as required by the Original PIP Pilot Program Approval Order, the Exchange represents that it has been submitting to the Commission a monthly PIP Pilot Program Report, offering detailed data from and analysis of the PIP Pilot Program.

###### 2. Statutory Basis

The Exchange believes that the data demonstrates that there is sufficient investor interest and demand to extend the Pilot Program for another year. The Exchange represents that the proposed rule change is designed to provide investors with real and significant price improvement regardless of the size of the order. Accordingly, the Exchange believes that the proposal is consistent with the requirements of Section 6(b) of the Act,<sup>6</sup> in general, and Section 6(b)(5) of the Act,<sup>7</sup> in particular, in that it is designed to provide price improvement to any order, which is consistent with the public interest and protection of investors from a best execution standpoint. Additionally, the Exchange believes that price improvement to any size order creates competition for the best execution of all orders, without unduly burdening competition.

##### B. Self-Regulatory Organization's Statement on Burden on Competition

The Exchange does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

<sup>5</sup> The Pilot Program is currently set to expire on July 18, 2006. See Securities Exchange Act Release No. 52149 (July 28, 2005), 70 FR 44704 (August 3, 2005). See also Securities Exchange Act Release No. 49068 (January 13, 2004), 69 FR 2768 (January 20, 2004) ("Original PIP Pilot Program Approval Order").

<sup>6</sup> 15 U.S.C. 78f(b).

<sup>7</sup> 15 U.S.C. 78f(b)(5).

<sup>15</sup> See *supra* notes 3 to 7.

<sup>16</sup> 17 CFR 242.608(e).

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

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

<sup>3</sup> 15 U.S.C. 78s(b)(3)(A)(iii).

<sup>4</sup> 17 CFR 240.19b-4(f)(6).