

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-49356]

### Order Pursuant to Section 11A of the Securities Exchange Act of 1934 and Rule 11Aa3-2(f) Thereunder Extending a *De Minimis* Exemption for Transactions in Certain Exchange-Traded Funds From the Trade-Through Provisions of the Intermarket Trading System

March 3, 2004.

This order extends, for an additional nine-month period, 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. 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>

The ITS Plan system is an order routing network designed to facilitate intermarket trading in exchange-listed securities among participating SROs based on current quotation information emanating from their markets. Quotations in exchange-listed securities are collected and disseminated by the Consolidated Quote System ("CQS"), which is governed by a national market system plan that the Commission has

<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 11Aa3-2(d), 17 CFR 240.11Aa3-2(d), promulgated under section 11A, 15 U.S.C. 78k-1, of the Act requires each self-regulatory organization ("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 11Aa3-2(f), 17 CFR 240.11Aa3-2(f), 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.

approved pursuant to Rule 11Aa3-2 under the Act.<sup>5</sup> Under the ITS Plan, a member of a participating SRO may access the best bid or offer displayed in CQS by another Participant by sending an order (a "commitment to trade") through ITS to that Participant. Exchange members participate in ITS through facilities provided by their respective exchanges. NASD members participate in ITS through a facility of the Nasdaq Stock Market ("Nasdaq") known as the Computer Assisted Execution System ("CAES"). Market makers and electronic communications networks ("ECNs") that are members of the NASD and seek to display their quotes in exchange-listed securities through Nasdaq must register with the NASD as ITS/CAES Market Makers.<sup>6</sup>

The May 2003 Order granted a *de minimis* exemption from compliance with section 8(d)(i) of the ITS Plan with respect to three specific exchange-traded funds ("ETFs"), the Nasdaq-100 Index ETF ("QQQ"), the Dow Jones Industrial Average ETF ("DIA"), and the Standard & Poor's 500 Index ETF ("SPY").<sup>7</sup> Section 8(d)(i) of the ITS Plan provides that participants should not purchase or sell any security that trades on the ITS Plan system at a price that is worse than the price at which that security is otherwise being offered on the ITS Plan system.<sup>8</sup> By its terms, the May 2003 Order exempts from the trade-through provisions of the ITS Plan any transactions in the three ETFs that are effected at prices at or within three cents away from the best bid and offer quoted in the CQS for a period of nine months, which ends on March 4, 2004.

The three cent *de minimis* exemption allows ITS participants and their members to execute transactions, through automated execution or otherwise, without attempting to access the quotes of other participants when the expected price improvement would not be significant. In providing the three

<sup>5</sup> 17 CFR 240.11Aa3-2.

<sup>6</sup> See Securities Exchange Act Release No. 42536 (March 16, 2000), 65 FR 15401 (March 22, 2000). Market Makers and ECNs are required to provide their best-priced quotations and customer limit orders in certain exchange-listed and Nasdaq securities to an SRO for public display under Commission Rule 11Ac1-1 and Regulation ATS. 17 CFR 240.11Ac1-1 and 242.301(b)(3).

<sup>7</sup> The Commission limited the *de minimis* exemption to these three securities because they share certain characteristics that may make immediate execution of their shares highly desirable to certain investors. In particular, trading in the three 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.

<sup>8</sup> Each ITS participant has adopted a trade-through rule substantially similar to the rule of the ITS Plan. See ITS Plan, section 8(d)(ii); See, e.g., NYSE Rule 15A, NASD Rule 5262.

cent *de minimis* exemption, the Commission believed that, on balance, exempting the specified transactions from the ITS trade-through provisions would provide investors increased liquidity and expand the choice of execution venues, while limiting the possibility that investors would receive significantly inferior prices.<sup>9</sup>

In May 2003, the Commission extended the three cent *de minimis* exemption for an additional nine-months, 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.<sup>10</sup> Over the next several months, the Commission intends to consider proposed Regulation NMS, together with any comments received, and determine whether to adopt the proposed trade-through rule or an alternative.

In view of the foregoing, the Commission believes that an extension of the *de minimis* exemption for an additional nine-month period 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. Depending on the action the Commission takes on proposed Regulation NMS prior to December 4, 2004, the Commission may determine to modify, withdraw, or

<sup>9</sup> See August 2002 Order, *supra* note 3. The Commission's Office of Economic Analysis conducted an analysis of trading in the QQQs in 2002, comparing trading on a day before the *de minimis* exemption was implemented, a day after the exemption was implemented before Island, an ECN, stopped displaying its orders to anyone, even its subscribers (going "dark"), and a day after the exemption was implemented when Island was "dark." The analysis showed that the percent of trades executed outside the NBBO did not increase, and that less than 1% of total trades were executed more than three cents away from the NBBO, after the *de minimis* exemption was implemented. A copy of the analysis is available in File No. S7-10-04.

<sup>10</sup> On February 24, 2004, the Commission proposed Regulation NMS for public comment. Securities Exchange Act Release No. 49325 (February 26, 2004). In part, proposed Rule 611 of Regulation NMS would require certain identified market centers to establish, maintain, and enforce policies and procedures reasonably designed to prevent trade-throughs. Extension of the *de minimis* pilot in no way prejudices or determines what actions the Commission may take with respect to any rule proposal.

extend the *de minimis* exemption. The Commission emphasizes, as it did in the May 2003 Order and in the August 2002 Order, 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 11Aa3-2(f) thereunder,<sup>11</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 QQQs, 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 March 4, 2004 through December 4, 2004.

By the Commission.

Jill M. Peterson,

Assistant Secretary.

[FR Doc. 04-5211 Filed 3-8-04; 8:45 am]

BILLING CODE 8010-01-P

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-49355; File No. SR-SCCP-2004-02]

### Self-Regulatory Organizations; Stock Clearing Corporation of Philadelphia; Notice of Filing and Immediate Effectiveness of Proposed Rule Change Relating to Trade Ticket Adjustment Fees

March 2, 2004.

Pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")<sup>1</sup>, notice is hereby given that on January 29, 2004, the Stock Clearing Corporation of Philadelphia ("SCCP") 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 primarily by SCCP. 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

SCCP proposes to amend its fee schedule by adopting a trade ticket adjustment fee ranging from \$50 to \$300

for each erroneous trade ticket that creates a false margin deficit.<sup>2</sup>

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

In its filing with the Commission, SCCP 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 Items IV below. SCCP has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.<sup>3</sup>

##### 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 amend SCCP's fee schedule to adopt a trade ticket adjustment fee ranging from \$50 to \$300 for each erroneous trade ticket that creates a false margin deficit. Trade ticket adjustments occur whenever a SCCP margin member submits a trade ticket for an adjustment or correction due, for example, to clerical errors or missing or incorrect trade tickets. Incorrect trade tickets may cause a false impression of a margin deficiency and thereby result in a false margin call.

The recalculation of account margin and the correction of incorrect or incomplete trade data using trade ticket adjustments is a manually intensive process that requires special handling and oversight by SCCP staff. Trade ticket adjustments take up considerable SCCP resources expended in researching the source of a trade ticket error. The trade ticket adjustment fee would apply only to those trade ticket adjustments that, prior to correction, resulted in a false margin deficiency in the SCCP margin member's margin account. The new trade ticket adjustment fee was effective on February 1, 2004.

SCCP believes that the proposed rule change is consistent with section 17A(b)(3)(D) of the Act<sup>4</sup> because it provides for the equitable allocation of dues, fees, and other charges.

<sup>2</sup> A copy of SCCP's fee schedule is attached as an exhibit to SCCP's rule filing.

<sup>3</sup> The Commission has modified the text of the summaries prepared by SCCP.

<sup>4</sup> 15 U.S.C. 78q-1(b)(3)(D).

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

SCCP does not believe that the proposed rule change will impose any inappropriate burden on competition.

##### C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received From Members, Participants, or Others

SCCP has not solicited or received written comments on the proposed rule change.

#### III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

The foregoing proposed rule change has become effective pursuant to section 19(b)(3)(A)(ii) of the Act<sup>5</sup> and Rule 19b-4(f)(2)<sup>6</sup> thereunder because it establishes or changes a due, fee, or other charge. At any time within sixty days of the filing of the proposed rule change, the Commission may summarily abrogate such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act.

#### IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Persons making written submissions should file six copies thereof with the Secretary, Securities and Exchange Commission, 450 5th Street NW, Washington, DC 20549-0069. Comments may also be submitted electronically at the following e-mail address: [rule-comments@sec.gov](mailto:rule-comments@sec.gov). All comment letters should refer to File No. SR-SCCP-2004-02. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, comments should be sent in hardcopy or by e-mail but not by both methods. Copies of the submission, all subsequent amendments, all written statements with respect to the rule filing that are filed with the Commission, and all written communications relating to the rule filing between the Commission and any person, other than those that may be withheld from the public in accordance with provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Room in Washington, DC. Copies of

<sup>5</sup> 15 U.S.C. 78s(b)(3)(A)(ii).

<sup>6</sup> 17 CFR 240.19b-4(f)(2).

<sup>11</sup> 17 CFR 240.11Aa3-2(f).

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