

purpose of order handling and execution.²⁶

Amendment No. 5 is purely a technical amendment, as its substance was published for notice and comment in Amendment Nos. 3 and 4. With Amendment No. 5, NASD took the substance of Amendment Nos. 3 and 4 and placed that information in IM-2320.

IV. Discussion and Commission Findings

The Commission has reviewed carefully the proposed rule change, the comment letters, and NASD's response to the comments, and believes that NASD has responded appropriately to the concerns raised by the commenters. The Commission finds that the proposed rule change, as amended, is consistent with the requirements of the Act and rules and regulations thereunder applicable to a national securities association, and, in particular, with Section 15A(b)(6) of the Act, which requires, among other things, that the rules of a national securities association be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest.²⁷ Regarding the commenters' assertion that a recipient broker-dealer's compliance with the terms and conditions of the order, as communicated by the originating broker-dealer, solely, should constitute satisfaction of the duty of best execution with regard to routed orders, the Commission believes that such compliance should be considered a significant factor in determining if the recipient broker-dealer has met its duty of best execution, but should not be the sole factor to consider. In Amendment Nos. 3 and 4, NASD addressed the concerns raised by commenters. In response to issues raised by the BMA, NASD changed the terminology of the proposed rule change, replacing "market center" with "market" and stating that it will interpret the term broadly. Additionally, the Commission notes that the Best Execution Rule currently applies to the bond markets.²⁸ NASD indicated in its amendment how it intends to apply the factors in the rule that provide evidence of reasonable diligence in the context of the bond market, and how it will interpret price

in connection with debt. In Amendment No. 4, NASD made a clear distinction between a member's duties when acting as provider of liquidity versus acting as an order handler for another broker-dealer. The Commission believes that the revisions clarify how the rule applies in the context of the debt market. Furthermore, the Commission notes that, at the time NASD adopted its Best Execution Rule, the equity markets were subject to a regulatory regime similar to the one under which the bond markets operate today.²⁹ The Commission expects that the NASD will take into account the structure and operation of the debt markets when applying the rule to debt market participants.

With regard to the commenters' claim that the proposal would create an unfair competitive disparity between otherwise similarly situated market centers that execute orders on an electronic agency basis, the Commission notes that electronic communications networks ("ECNs") are subject to a different regulatory regime than SROs. ECNs are broker-dealers by definition, and must be members of an SRO; consequently ECNs are subject to SRO rules. Moreover, the Commission believes the proposed rule change, as amended, will not unfairly affect ECN operations.

With respect to the commenters' concern that implementation of this proposal should be delayed until after the Commission has adopted guidance under the trade through proposal of Regulation NMS, the Commission notes that the Commission adopted Regulation NMS subsequent to the commenters filing their comment letters.

Finally, the Commission views markup obligations and the duty of best execution as separate and distinct requirements. NASD Rule 2320(f) states that best execution obligations "do not relate to the reasonableness of commission rates, markups or markdowns which are governed by Rule 2440 and IM-2440."

V. Conclusion

It is therefore ordered, pursuant to Section 19(b)(2) of the Act,³⁰ that the

proposed rule change (SR-NASD-2004-026), as modified by Amendment Nos. 1-5, be, and it hereby is, approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.³¹

Nancy M. Morris,
Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-54334; File No. SR-NASD-2006-097]

Self-Regulatory Organizations; National Association of Securities Dealers, Inc.; Notice of Filing and Immediate Effectiveness of Proposed Rule Change To Extend a Pilot Program That Increases Position and Exercise Limits for Certain Equity Options

August 18, 2006

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")¹ and Rule 19b-4 thereunder,² notice is hereby given that on August 10, 2006, the National Association of Securities Dealers, Inc. ("NASD") filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I and II below, which Items have been prepared by NASD. NASD has filed the proposal as a "non-controversial" rule change pursuant to Section 19(b)(3)(A) of the Act³ and Rule 19b-4(f)(6) thereunder,⁴ which renders it 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

NASD proposes to amend NASD Rule 2860 to extend a pilot program increasing certain options position and exercise limits. The text of the proposed rule change is available on NASD's Web site (<http://www.nasd.com>), at NASD's principal office, and at the Commission's Public Reference Room.

³¹ 17 CFR 200.30-3(a)(12).

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ 15 U.S.C. 78s(b)(3)(A).

⁴ 17 CFR 240.19b-4(f)(6).

²⁶ See footnote 9, *supra*.

²⁷ 15 U.S.C. 78o-3(b)(6). In approving this proposed rule change, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

²⁸ See footnote 24, *supra*, and Exempted Securities Order.

²⁹ As NASD notes, in 1968 when the Best Execution Rule was adopted, the market for equity securities was much different than it is today. For example, there was no consolidated tape and thus no readily available trade or quotation information. Market makers in over-the-counter securities conducted transactions via telephone, after checking prices either in the pink sheets or by information they obtained using the telephone. In addition, there was no requirement to report transactions to NASD within 90 seconds.

³⁰ 30 15 U.S.C. 78s(b)(2).

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

In its filing with the Commission, NASD 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. NASD 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

NASD proposes to amend NASD Rule 2860 to extend a pilot program until March 1, 2007 (unless extended) increasing position and exercise limits for both standardized and conventional options ("Pilot Program").⁵ Unless extended, the Pilot Program will expire on September 1, 2006.⁶ NASD believes that the Pilot Program should be extended so that it may continue without interruption for the same reasons that are discussed in the Pilot Program Notice.

2. Statutory Basis

NASD believes that the proposed rule change is consistent with the provisions of Section 15A(b)(6) of the Act,⁷ which requires, among other things, that NASD's rules must be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest. The proposed rule change is being made so that the Pilot Program, which achieves these goals as discussed in the Pilot Program Notice, may continue without interruption.

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

NASD 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, as amended.

⁵ See Securities Exchange Act Release No. 51520 (April 11, 2005), 70 FR 19977 (April 15, 2005) (notice of filing and immediate effectiveness of SR-NASD-2005-040) ("Pilot Program Notice").

⁶ See Securities Exchange Act Release No. 53346 (February 22, 2006), 71 FR 10580 (March 1, 2006) (notice of filing and immediate effectiveness of SR-NASD-2006-025).

⁷ 15 U.S.C. 78o-3(b)(6).

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

Written comments were neither solicited nor received.

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

Because the forgoing rule change does not: (1) Significantly affect the protection of investors or the public interest; (2) impose any significant burden on competition; and (3) become operative for 30 days after the date of this filing, or such shorter time as the Commission may designate, it has become effective pursuant to Section 19(b)(3)(A) of the Act⁸ and Rule 19b-4(f)(6) thereunder.⁹

A proposed rule change filed under 19b-4(f)(6) normally may not become operative prior to 30 days after the date of filing.¹⁰ However, Rule 19b-4(f)(6)(iii)¹¹ permits the Commission to designate a shorter time if such action is consistent with the protection of investors and the public interest. NASD provided the Commission with written notice of its intent to file this proposed rule change at least five business days prior to the date of filing the proposed rule change. In addition, NASD has requested that the Commission waive the 30-day pre-operative delay. The Commission believes that waiving the 30-day pre-operative delay is consistent with the protection of investors and in the public interest because it will allow the Pilot Program to continue uninterrupted.¹²

At any time within 60 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 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. Comments may be submitted by any of the following methods:

⁸ 15 U.S.C. 78s(b)(3)(A).

⁹ 17 CFR 240.19b-4(f)(6).

¹⁰ 17 CFR 240.19b-4(f)(6)(iii).

¹¹ *Id.*

¹² For the purposes only of waiving the pre-operative delay, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

Electronic Comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to rule-comments@sec.gov. Please include File No. SR-NASD-2006-097 on the subject line.

Paper Comments:

- Send paper comments in triplicate to Nancy M. Morris, Secretary, Securities and Exchange Commission, Station Place, 100 F Street, NE., Washington, DC 20549-1090.

All submissions should refer to File No. SR-NASD-2006-097. 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, please use only one method. The Commission will post all comments on the Commission's Internet Web site (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for inspection and copying in the Commission's Public Reference Room. Copies of such filing will also be available for inspection and copying at the principal office of NASD. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File No. SR-NASD-2006-097 and should be submitted on or before September 18, 2006.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹³

Nancy M. Morris,
Secretary.

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¹³ 17 CFR 200.30-3(a)(12).