

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-53621; File No. SR-CBOE-2006-32)

April 10, 2006

Self-Regulatory Organizations; Chicago Board Options Exchange, Incorporated; Notice of Filing and Order Granting Accelerated Approval of Proposed Rule Change and Amendment No. 1 Thereto to List for Trading Options on the iShares MSCI Emerging Markets Index Fund

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 April 5, 2006, the Chicago Board Options Exchange, Incorporated (“CBOE” or “Exchange”) 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 the Exchange. On April 6, 2006, the CBOE filed Amendment No. 1 to the proposed rule change.³ The Commission is publishing this notice and order to solicit comments on the proposal from interested persons and to approve the proposed rule change, as amended, on an accelerated basis.

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

The Exchange proposes to list and trade options on the iShares MSCI Emerging Markets Index Fund (“Fund Options”). The text of the proposed rule change is available on the Exchange's Web site (<http://www.cboe.com>), at the Office of the Secretary, CBOE and at the Commission.

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ In Amendment No. 1, the Exchange agreed to list Fund Options subject to a sixty-day pilot program. During this period, the Exchange agrees to use its best efforts to obtain a comprehensive surveillance agreement with the Bolsa Mexicana de Valores (“Bolsa”) and will regularly update the Commission on the status of its negotiations with Bolsa.

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. The text of these statements may be examined at the places specified in Item III below, and is set forth in Sections A, B, and C below.

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

1. Purpose

The Exchange seeks approval to list for trading on the Exchange options on the iShares MSCI Emerging Markets Index Fund ("Fund"). The Exchange currently has in place initial listing and maintenance standards set forth in CBOE Rules 5.3.06 and 5.4.08, respectively ("Listing Standards") that are designed to allow the Exchange to list and trade options on funds structured as open-end investment companies, such as the Fund.⁴ The request for approval is based on the Exchange's determination that the Fund meets substantially all of the Listing Standard requirements, and for the requirements that are not met, sufficient mechanisms exist that would provide the Exchange with adequate surveillance and regulatory information with respect to the Fund.

As provided in the Fund's prospectus, the Fund is an open-end investment company that is designed to hold a portfolio of securities that track the MSCI Emerging Markets Index

⁴ CBOE Rules 5.3.06 and 5.4.08 set forth the initial listing and maintenance standards for registered investment companies (or series thereof) organized as open-end management investment companies, unit investment trust or other similar entities traded on a national securities exchange or through the facilities of a national securities exchange ("Exchange-Traded Funds"); see approval order for SR-CBOE-97-45 (Securities Exchange Act Release No. 40166 (July 2, 1998), 63 FR 37430 (July 10, 1998)).

("Index").⁵ The Fund employs a "representative sampling" methodology to track the Index, which means that the Fund invests in a representative sample of securities in the Index that have a similar investment profile as the Index.⁶ Securities selected by the Fund have aggregate investment characteristics (based on market capitalization and industry weightings), fundamental characteristics (such as return variability, earnings valuation and yield), and liquidity measures similar to those of the Index. The Fund generally invests at least 90% of its assets in the securities of the Index or in American Depositary Receipts ("ADRs") and Global Depositary Receipts ("GDRs") representing such securities. In order to improve portfolio liquidity and give the Fund additional flexibility to comply with the requirements of the U.S. Internal Revenue Code and other regulatory requirements and to manage future corporate actions and index changes in smaller markets, the Fund also has the authority to invest the remainder of its assets in securities that are not included in the Index or in ADRs and GDRs representing such securities. The Fund may invest up to 10% of its assets in other MSCI index funds that seek to track the performance of equity securities of constituent countries of the Index. The Fund will not concentrate its investments (i.e., hold 25% or more of its total assets in the stocks of a particular

⁵ As provided on the Web site of Morgan Stanley Capital International Inc. ("MSCI") (www.msci.com), which is the entity that created and currently maintains the Index, the Index is a capitalization-weighted index whose component securities are adjusted for available float and must meet objective criteria for inclusion in the Index. The Index aims to capture 85% of the publicly available total market capitalization in each emerging market included in the Index. As of March 28, 2006, the Index was comprised of 832 constituents with the top five constituents representing the following weights: 4.19%, 2.09%, 2.06%, 1.72%, and 1.63%. The Index is rebalanced quarterly, calculated in U.S. Dollars on a real time basis, and disseminated every 60 seconds during market trading hours.

⁶ The Fund is comprised of 271 securities as of March 28, 2006. Samsung Electronics Co LTD GDR Registered, a South Korean security, has the greatest individual weight at 5.61%. The security with the smallest weight is Metropolitan Bank & Trust Co, a Thailand security, at 0.01%. The aggregate percentage weighting of the top 5, 10, and 20 securities in the Fund are 18.22%, 28.18%, and 43.74%, respectively.

industry or group of industries), except that, to the extent practicable, the Fund will concentrate to approximately the same extent that the Index concentrates in the stocks of such particular industry or group of industries. The Exchange believes that these requirements and policies prevent the Fund from being excessively weighted in any single security or small group of securities and significantly reduce concerns that trading in the Fund could become a surrogate for trading in unregistered securities.

Shares of the Fund ("Fund Shares") are issued in exchange for an "in kind" deposit of a specified portfolio of securities, together with a cash payment, in minimum size aggregation size of 150,000 shares (each, a "Creation Unit"), as set forth in the Fund's prospectus.⁷ The Fund issues and sells Fund Shares in Creation Unit sizes through a principal underwriter on a continuous basis at the net asset value per share next determined after an order to purchase Fund Shares and the appropriate securities are received. Following issuance, Fund Shares are traded on an exchange like other equity securities, and equity trading rules apply. Likewise, redemption of Fund Shares is made in Creation Unit size and "in kind," with a portfolio of securities and cash exchanged for Fund Shares that have been tendered for redemption.

The Exchange notes that the maintenance listing standards set forth in Rule 5.4.08 for options on open-end investment companies do not include criteria based on either the number of shares or other units outstanding or on their trading volume. As explained in SR-CBOE-97-03,⁸ the absence of such criteria is justified on the ground that since it should always be possible to create additional shares or other interests in open-end investment companies at their net asset

⁷ See approval order for SR-Amex-2001-45 (Securities Exchange Act Release No. 44990, note 16) (October 25, 2001), noting that local restrictions on transfers of securities to and between certain kinds of investors exist in certain foreign markets that preclude in-kind creation and redemptions of Exchange-Traded Funds).

⁸ See Securities Exchange Act Release No. 40166 (July 2, 1998), 63 FR 37430 (July 10, 1998).

value by making an in-kind deposit of the securities that comprise the underlying index or portfolio, there is no limit on the available supply of such shares or interests. The Exchange states that this process should make it highly unlikely that the market for listed, open-end investment company shares could be capable of manipulation, since whenever the market price for such shares departs from net asset value, arbitrage will occur. Similarly, since the Fund meets all of the requirements of the Listing Standards except as described below, the Exchange believes that the same analysis applies to the Fund.

The Exchange has reviewed the Fund and determined that it satisfies the Listing Standards except for the requirement set forth in CBOE Rule 5.3.06(A), which requires the Fund to meet the following condition: "any non-U.S. component securities of the index or portfolio on which the Units are based that are not subject to comprehensive⁹ surveillance agreements do not in the aggregate represent more than 50% of the weight of the index or portfolio." The Exchange currently has in place comprehensive surveillance agreements with foreign exchanges that cover 49.76% of the securities in the Fund. One of the foreign exchanges on which component securities of the Fund are traded and with which the Exchange does not have a comprehensive surveillance agreement is the Bolsa. The percentage of the weight of the Fund represented by these securities is 7.54%.

The Exchange understands that the Commission has been willing to allow an exchange to rely on a memorandum of understanding entered into between regulators in the event that the exchanges themselves cannot enter into a surveillance agreement. The Exchange had previously attempted to enter into a surveillance agreement with Bolsa around the time when the Exchange

⁹ The Exchange inadvertently omitted reference to the word "comprehensive" in Rule 5.3.06(A). Telephone conference between Bill Speth, Director of Research, Exchange, and Florence Harmon, Senior Special Counsel, Division of Market Regulation, Commission, on April 7, 2006.

sought approval to list for trading options on the CBOE Mexico 30 Index in 1995, which was comprised of stocks trading on Bolsa.¹⁰ Since Bolsa was unable to provide a surveillance agreement, the Commission allowed the Exchange to rely on the memorandum of understanding executed by the Commission and the Comision Nacional Bancaria y de Valores (“CNBV”), dated as of October 18, 1990 (“MOU”). The Commission noted in the Approval Order that in cases where it would be impossible to secure an agreement, the Commission relied in the past on surveillance sharing agreements between the relevant regulators. The Commission further noted in the Approval Order that pursuant to the terms of the MOU, it was the Commission's understanding that both the Commission and the CNBV could acquire information from and provide information to the other similar to that which would be required in a surveillance sharing agreement between exchanges, and therefore, should CBOE need information on Mexican trading in the component securities of the CBOE Mexico 30 Index, the Commission could request such information from the CNBV under the MOU.¹¹

The Exchange has recently contacted Bolsa with a request to enter into a comprehensive surveillance agreement. Since Bolsa is still reviewing the document, the Exchange is uncertain whether the same barriers that prevented Bolsa from entering into an information sharing agreement approximately ten years ago still exist today. In this regard, the Exchange requests

¹⁰ See Securities Exchange Act Release No. 36415 (October 25, 1995), 60 FR 55620 (November 1, 1995). Telephone conference between Bill Speth, Director of Research, Exchange, and Florence Harmon, Senior Special Counsel, Division of Market Regulation, Commission, on April 7, 2006 (correcting citation).

¹¹ The Exchange also states that the Commission noted if securing an information sharing agreement is not possible, an exchange should contact the Commission prior to listing a new derivative securities product. The Commission also noted that the Commission may determine instead that it is appropriate to rely on a memorandum of understanding between the Commission and the foreign regulator. See Securities Exchange Act Release No. 40761 (December 8, 1998), 63 FR 70952 (December 22, 1998).

permission to rely for a sixty-day pilot period on the MOU entered into between the Commission and the CNBV for purposes of satisfying its surveillance and regulatory responsibilities for the component securities in the Fund that trade on Bolsa until the Exchange is able to secure a surveillance agreement with Bolsa. During this period, the Exchange has agreed to use its best efforts to obtain a comprehensive surveillance agreement with Bolsa, which shall reflect the following: (i) express language addressing market trading activity, clearing activity, and customer identity; (ii) Bolsa's reasonable ability to obtain access to and produce requested information; and (iii) based on the comprehensive surveillance agreement and other information provided by Bolsa, the absence of existing rules, laws, or practices that would impede the Exchange from obtaining foreign information relating to market activity, clearing activity, or customer identity, or, in the event such rules, laws, or practices exist, they would not materially impede the production of customer or other information. The Exchange also represents that it will regularly update the Commission on the status of its negotiations with Bolsa.

2. Statutory Basis

CBOE believes the proposed rule change is consistent with the Act¹² and the rules and regulations under the Act applicable to a national securities exchange and, in particular, the requirements of Section 6(b) of the Act.¹³ Specifically, the Exchange believes the proposed rule change is consistent with the Section 6(b)(5)¹⁴ requirements that the rules of an exchange be designed to promote just and equitable principles of trade, and to protect investors and the public interest.

¹² 15 U.S.C. 78a et seq.

¹³ 15 U.S.C. 78(f)(b).

¹⁴ 15 U.S.C. 78(f)(b)(5).

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

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

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

Written comments on the proposed rule change were neither solicited nor received.

III. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change, as amended, is consistent with the Act. Comments may be submitted by any of the following methods:

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 Number SR-CBOE-2006-32 on the subject line.

Paper comments:

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

All submissions should refer to File Number SR-CBOE-2006-32. 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 also will be available for inspection and copying at the principal offices of the Exchange. 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 Number SR-CBOE-2006-32 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

IV. Commission's Findings and Order Granting Accelerated Approval of the Proposed Rule Change

The Commission finds that the proposed rule change, as amended, is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange.¹⁵ In particular, the Commission finds that the proposed rule change, as amended, is consistent with Section 6(b)(5) of the Act,¹⁶ which requires that an exchange have rules designed, among other things, to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and in general to protect investors and the public interest.

The listing of the Fund Options does not satisfy CBOE Rule 5.3.06(A), which requires that: "any non-U.S. component securities of the index or portfolio on which the Units are based that are not subject to comprehensive surveillance agreements do not in the aggregate represent more than 50% of the weight of the index or portfolio." Although the Commission has been willing to allow an exchange to rely on a memorandum of understanding entered into between

¹⁵ In approving this rule change, the Commission notes that it has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

¹⁶ 15 U.S.C. 78f(b)(5).

regulators where the listing SRO finds it impossible to enter into an information sharing agreement, it is not clear that that CBOE has exhausted all avenues of discussion with foreign markets, including Bolsa, in order to obtain such an agreement. Indeed, with regard to Bolsa, conditions may have changed in the time period since CBOE last raised the issue with Bolsa in 1995 such that Bolsa now would be able to entering a comprehensive surveillance agreement with CBOE.

Consequently, the Commission has determined to approve CBOE's listing and trading of Fund Options for a sixty-day pilot period during which time CBOE may rely on the MOU with respect to Fund components trading on Bolsa. During this period, the Exchange has agreed to use its best efforts to obtain a comprehensive surveillance agreement with Bolsa, which shall reflect the following: (i) express language addressing market trading activity, clearing activity, and customer identity; (ii) Bolsa's reasonable ability to obtain access to and produce requested information; and (iii) based on the comprehensive surveillance agreement and other information provided by Bolsa, the absence of existing rules, laws, or practices that would impede the Exchange from obtaining foreign information relating to market activity, clearing activity, or customer identity, or, in the event such rules, laws, or practices exist, they would not materially impede the production of customer or other information. The Exchange also represents that it will regularly update the Commission on the status of its negotiations with Bolsa. In approving the proposed rule change, the Commission notes that CBOE currently has in place surveillance agreements with foreign exchanges that cover 49.76% of the securities in the Fund and that the Index upon which the Fund is based appears to be a broad-based index.

The Exchange has requested accelerated approval of the proposed rule change. The Commission finds good cause, consistent with Section 19(b)(2) of the Act,¹⁷ for approving this proposed rule change before the thirtieth day after the publication of notice thereof in the Federal Register. The Exchange has agreed to use its best efforts to obtain a comprehensive surveillance agreement with the Bolsa during a sixty-day pilot period in which the Exchange will rely on the MOU.

V. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,¹⁸ that the proposed rule change (SR-CBOE-2006-32), as amended, is approved on an accelerated basis for a sixty-day pilot period ending on June 9, 2006.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹⁹

Nancy M. Morris
Secretary

¹⁷ 15 U.S.C. 78s(b)(2).

¹⁸ Id.

¹⁹ 17 CFR 200.30-3(a)(12).