

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-58401; File No. SR-ISE-2008-63)

August 21, 2008

Self-Regulatory Organizations; International Securities Exchange, LLC; Notice of Filing of Proposed Rule Change Relating to the Price Improvement Mechanism

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 July 31, 2008, the International Securities Exchange, LLC (the “Exchange” or the “ISE”) 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 the Exchange. 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 Exchange proposes to modify its Price Improvement Mechanism (PIM) auction eligibility requirements to eliminate the requirement that there be at least three market makers quoting the relevant series. The text of the proposed rule change is available on the Exchange’s Web site (<http://www.ise.com>), at the principal office of the Exchange, and at the Commission’s Public Reference Room.

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

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

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

In order to provide additional opportunities for price improvement, the Exchange proposes to expand the PIM auction process. The Exchange's PIM permits Electronic Access Members ("EAMs") to provide penny price improvement for agency orders.³ ISE's current rules require, among other things, that an EAM enter an order into the PIM only when there are at least three market makers quoting in the options series. The Exchange is now proposing to eliminate this requirement.

The Exchange does not believe that orders should be denied the benefits of the PIM auction simply because there may be less than three ISE market makers quoting in a particular series. The Exchange believes this is a reasonable modification designed to provide additional flexibility for members to obtain executions on behalf of their customers while continuing to provide a meaningful, competitive auction.

In support of its proposal, the Exchange notes the ISE and other options exchanges already have provisions within their rules that permit price improvement in non-standard increments without a condition that there be a minimum number of market makers quoting in the particular series. For example, ISE has electronic auction mechanisms for crossing agency order with facilitation or solicited orders (referred to as the "Facilitation Mechanism" and "Solicited Order Mechanism") in "split price" increments (e.g., \$1.025, \$1.05 and \$1.075 for series trading

³ A crossing transaction consists of an order the EAM represents as agent and a counter-side order. The counter-side order may represent interest for the EAM's own account or interest the EAM may have solicited from one or more parties, or both.

in \$0.05 increments. The Facilitation and Solicited Order Mechanisms do not require that there be any minimum number of ISE market makers quoting in the particular series.⁴ Further, the Chicago Board Options Exchange (“CBOE”) has an electronic auction mechanism for crossing agency orders for 500 contracts or more with solicited orders (referred to as the “Solicitation Auction Mechanism”) in increments as small as \$0.01. This CBOE Solicitation Auction Mechanism does not require that there be any minimum number of CBOE market makers quoting in the particular series.⁵ Finally, the NASDAQ Options Market (“NOM”) has a procedure that permits a member who enters an agency order in penny increments (which is then rounded and displayed at the standard increment price) to enter a contra-side order in penny increments after the agency order has been exposed at the rounded price for three seconds. This NOM crossing procedure does not require that there be any minimum number of NOM market makers quoting in the particular series.⁶

⁴ See ISE Rule 716.

⁵ See CBOE Rule 6.74B.

⁶ When using the NOM crossing procedure to achieve an execution in penny increments, there is no requirement that there be any NOM market makers quoting the particular series or that they even be aware that the initiating NOM member is attempting to cross an order in an undisplayed penny increment. For example, a NOM member could enter an agency limit order to buy at \$1.03 that is rounded and displayed at \$1.00, wait three seconds, then enter a principal or solicited order to sell at \$1.03. Although the initiating member knows it has entered an agency order to buy at \$1.03, other market participants would only see the size of the agency order displayed on the bid at \$1.00. See NOM Chapter IV, Section 5, Chapter VI, Sections 7(b) and 10, and Chapter VII, Sections 6 and 12. The Exchange understands that NOM’s method of crossing orders in non-standard increments differs from ISE’s PIM in so much as PIM will allocate the initiating Member a certain minimum participation entitlement if certain conditions are met (e.g., after public customer orders, 40% of the order is allocated to the initiating Member if its single-price submission equals the best price), whereas NOM does not have any such participation entitlement. However, the Exchange does not believe this distinction is dispositive to our proposal to eliminate the requirement that there be a minimum number of quoters for a PIM auction. In this regard, we note that participation entitlements already apply to the ISE Facilitation and Solicited Order Mechanisms and the CBOE Solicitation Auction Mechanism. See ISE Rule 716 and CBOE Rule 6.74B. The

Because these other mechanisms are currently able to offer price improvement in a non-standard increment without a minimum quoter requirement, the Exchange believes it is essential for competitive reasons to be able to offer the same opportunities for price improvement on ISE through the PIM.

2. Statutory Basis

The Exchange believes the proposed rule change is consistent with Section 6(b) of the Act⁷ in general and furthers the objectives of Section 6(b)(5) of the Act⁸ in particular in that it is designed to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, 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. In particular, the proposed rule change will allow members to guarantee executions and provide additional price improvement opportunities to their customer's orders. The Exchange believes this is a reasonable modification designed to provide additional flexibility for members to obtain executions on behalf of their customers while continuing to provide a meaningful, competitive auction.

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

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

Exchange also notes that an Agency Order displayed through ISE's PIM process will receive the benefit of any price improvement received during the auction, whereas an agency order displayed on NOM generally will not get any price improvement beyond its limit price (using the example above, once displayed at the rounded price the agency order to buy will generally only execute at \$1.03, not better).

⁷ 15 U.S.C. 78f(b).

⁸ 15 U.S.C. 78f(b)(5).

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

The Exchange has not solicited, and does not intend to solicit, comments on this proposed rule change. The Exchange has not received any unsolicited written comments from members or other interested parties.

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

Within 35 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the Exchange consents, the Commission will:

- (A) by order approve such proposed rule change, or
- (B) institute proceedings to determine whether the proposed rule change should be disapproved.

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:

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-ISE-2008-63 on the subject line.

Paper comments:

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

All submissions should refer to File Number SR-ISE-2008-63. 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 on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of such filing also will be available for inspection and copying at the principal office of the ISE. 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-ISE-2008-63 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.⁹

Florence E. Harmon
Acting Secretary

⁹ 17 CFR 200.30-3(a)(12).