

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-57847; File No. SR-ISE-2008-29)

May 21, 2008

Self-Regulatory Organizations; International Securities Exchange, LLC; Order Approving Proposed Rule Change Relating to the Price Improvement Mechanism

I. Introduction

On March 20, 2008, the International Securities Exchange, LLC (“ISE”) filed with the Securities and Exchange Commission (“Commission”), 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> a proposed rule change to allow members to enter orders into the Price Improvement Mechanism (“PIM”) at a price that matches the national best bid or offer (“NBBO”) when the ISE market is inferior to the NBBO. The proposed rule change was published for comment in the Federal Register on April 14, 2008.<sup>3</sup> The Commission received one comment letter regarding the proposal.<sup>4</sup> This order approves the proposed rule change.

II. Description of the Proposal

The PIM currently allows certain ISE members to enter two-sided orders (“Crossing Transaction”) for execution at a price that improves upon the NBBO.<sup>5</sup> The customer side of these orders is then exposed to other members to give them an opportunity to participate in the trade at the proposed cross price or better. The Exchange proposes to extend the application of

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

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

<sup>3</sup> See Securities Exchange Act Release No. 57632 (April 8, 2008), 73 FR 20079.

<sup>4</sup> See letter from Lisa J. Fall, General Counsel, Boston Options Exchange (“BOX”), to Nancy M. Morris, Secretary, Commission, dated May 14, 2007 (“BOX Comment”).

<sup>5</sup> See Securities Exchange Act Release No. 50819 (December 8, 2004), 69 FR 75093 (December 15, 2004) (approving rules implementing the PIM).

the PIM to permit a member to enter an order (“Agency Order”) into the PIM at a price that is equal to the NBBO when the ISE’s best bid or offer (“ISE BBO”) is inferior to the NBBO. When the ISE BBO equals the NBBO, the member will continue to be required to enter a price at least one cent better than the NBBO.<sup>6</sup>

The Commission received one comment letter regarding the proposed rule change.<sup>7</sup> The commenter expresses concern that ISE’s proposal would lead to greater rates of internalization and reduced amounts of price improvement being made available to public customers on ISE, especially to small orders under 50 contracts.<sup>8</sup> The commenter further believes that the proposal would reduce the incentive for market participants to quote at the NBBO on ISE.<sup>9</sup>

### III. Discussion and Commission Findings

After carefully considering the proposal and the comment submitted, the Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange<sup>10</sup> and, in particular, the requirements of Section 6 of the Act.<sup>11</sup> Specifically, the Commission finds that the proposed rule change is consistent with Section 6(b)(5) of the Act,<sup>12</sup> which requires, among other things, that the rules of a national securities exchange be designed to promote just and equitable

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<sup>6</sup> See ISE Rule 723(b)(1).

<sup>7</sup> See BOX Comment, supra note 4.

<sup>8</sup> Id. at 1 and 5.

<sup>9</sup> Id. at 4.

<sup>10</sup> 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).

<sup>11</sup> 15 U.S.C. 78f.

<sup>12</sup> 15 U.S.C. 78f(b)(5).

principles of trade, remove impediments to and perfect the mechanisms of a free and open market and a national market system and, in general, to protect investors and the public interest.

The Commission believes that the proposal will continue to provide customers with an opportunity for price improvement over the NBBO. The Commission notes that once a Crossing Transaction is submitted into the PIM auction, the Crossing Transaction may not be cancelled.<sup>13</sup> Therefore, the Agency Order submitted to the PIM auction when ISE's BBO is not equal to the NBBO will be guaranteed an execution price of at least the NBBO and, moreover, will be given an opportunity for execution at a price better than the NBBO.

The Commission does not agree with the concerns raised by the commenter. Under the proposal, the PIM will continue to provide an opportunity for customer orders to receive an execution at a price better than NBBO. All orders entered into the PIM will continue to be exposed to all ISE members before the submitting member can execute against the Agency Order. Moreover, the Commission believes the proposal may increase the likelihood of members entering Agency Orders into the PIM because the member will only be required to guarantee an execution at the NBBO when ISE's BBO is not equal to the NBBO, which would provide additional customer orders an opportunity for price improvement over the NBBO. The proposal also may encourage increased participation in a PIM by ISE members willing to trade with an agency order at the NBBO but not better than the NBBO. Increased participation by ISE members would decrease the proportion of an Agency Order that would be internalized by the submitting member.<sup>14</sup>

The Commission thus believes that ISE's proposal is consistent with the requirements of the Act.

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<sup>13</sup> See ISE Rule 723(b)(3).

<sup>14</sup> See ISE Rule 723(d)(4).

IV. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,<sup>15</sup> that the proposed rule change (File No. SR-ISE-2008-29), be, and it hereby is, approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>16</sup>

Florence E. Harmon  
Deputy Secretary

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<sup>15</sup> 15 U.S.C. 78s(b)(2).

<sup>16</sup> 17 CFR 200.30-3(a)(12).