SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-58224; File No. SR-ISE-2007-94)

July 25, 2008

Self-Regulatory Organizations; International Securities Exchange, LLC; Order Granting Accelerated Approval of a Proposed Rule Change as Modified by Amendments No. 1 and 3 Thereto Relating to Reduction of Certain Order Handling and Exposure Periods from Three Seconds to One Second

## I. Introduction

On October 5, 2007, the International Securities Exchange, LLC ("ISE" or "Exchange"), filed with the Securities and Exchange Commission ("Commission") pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")[1] and Rule 19b-4 thereunder,[2] a proposed rule change to reduce certain order exposure times from three seconds to one second. On December 4, 2007, ISE filed Amendment No. 1 to the proposed rule change. On May 22, 2008, ISE filed Amendment No. 2 to the proposed rule change and withdrew this Amendment on May 29, 2008. On June 23, 2008, ISE filed Amendment No. 3 to the proposed rule change. The proposed rule change, as modified by Amendments No. 1 and 3, was published for comment in the Federal Register on July 3, 2008.[3] The Commission received one comment on the proposal.[4] This order approves the proposed rule change, as modified by Amendments No. 1 and 3, on an accelerated basis.

## II. Description of the Proposal

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1 15 U.S.C. 78s(b)(l).

2 17 CFR 240.19b-4.

3 See Securities Exchange Act Release No. 58041 (June 26, 2008), 73 FR 38263 ("Notice").

4 See letter from Lisa J. Fall, General Counsel, Boston Options Exchange ("BOX"), to Nancy M. Morris, Secretary, Commission, dated May 14, 2008 ("BOX Comment").

The Exchange proposes to reduce the order handling and exposure periods contained in Exchange Rules 716 (Block Trades), 717 (Limitations on Orders), 723 (Price Improvement Mechanism for Crossing Transactions), and 811 (Directed Orders) from three seconds to one second.

Rule 716 contains the requirements applicable to the execution of orders using the Block Order Mechanism, Facilitation Mechanism, and Solicited Order Mechanism. The Block Order Mechanism allows members to obtain liquidity for the execution of a block-size order, whereas the Facilitation and Solicited Order Mechanisms allow members to enter block-size cross transactions. Rule 723 contains the requirements applicable to the execution of orders using the Price Improvement Mechanism ("PIM"). The PIM allows members to enter cross transactions of any size. Orders entered into any of these mechanisms currently are exposed to all market participants for three seconds, giving participants an opportunity to enter additional trading interest before the orders are automatically executed.

Rule 717 requires members to expose agency orders to the marketplace before executing them as principal[5] or executing them against orders solicited from other members.[6] Under Rule 717, an order can be exposed either by entering it onto the Exchange and waiting at least three seconds before entering the contra-side proprietary or solicited order, or by utilizing the various mechanisms that have an exposure period built into the functionality.

Rule 811 contains the requirements applicable to the handling and execution of Directed Orders. A Directed Market Maker is required to enter Directed Orders into the PIM or release

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5 Rule 717(d).

6 Rule 717(e). The Exchange proposes to make a non-substantive clean-up of Rule 717(e) to specify that members can use the Facilitation Mechanism to execute solicited crosses. The Facilitation Mechanism rule was amended earlier this year to allow members to enter solicited crosses, and Rule 717(e) should have been updated at that time. See Securities Exchange Act Release No. 55557 (March 29, 2007), 72 FR 16838 (April 5, 2007).

the order to the Exchange's limit order book within three seconds of receipt.[7] Additionally, there are three instances when a Directed Order is exposed to all market participants for three seconds after being released to the Exchange's limit order book: (i) before a Directed Order is matched against the Directed Market Maker at the national best bid or offer ("NBBO");[8] (ii) before executing a Directed Order against the Directed Market Maker's Guarantee;[9] and (iii) before being given to the Primary Market Maker for handling where the Directed Market Maker is also the Primary Market Maker.[10] Finally, if a Directed Order is placed on the Exchange's limit order book, the Directed Market Maker is not permitted to enter a proprietary order to execute against the Directed Order during the three seconds following the release of the Directed Order.

Under the proposal, all of the three-second exposure periods referred to above would be reduced to one second.

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[7] Rule 811(c)(3). If the Directed Market Maker fails to do so within three seconds, the Exchange's system automatically releases the order. Rule 811(c)(3)(ii).

[8] If a Directed Market Maker is quoting at the NBBO at the time it releases a Directed Order, the Directed Market Maker is last in priority, and the order is exposed to all market participants before the Directed Order is executed against the Directed Market Maker's quote.

[9] If the Directed Market Maker is quoting at the NBBO on the opposite side of the market from a Directed Order at the time the Directed Order is received by the Directed Market Maker, and the Directed Order is marketable, the Exchange's system will automatically guarantee execution of the Directed Order against the Directed Market Maker at the price and the size of the Directed Market Maker's quote. Rule 811(d).

[10] As provided in Rule 714, when the Exchange's best bid or offer is inferior to another exchange, incoming marketable customer orders are handled by the Primary Market Maker pursuant to Rule 803(c), which requires the Primary Market Maker to either execute the order at a price that matches the NBBO or attempt to obtain the better price for the customer according to the Linkage rules contained in Chapter 19.

The Commission received one comment letter regarding the proposed rule change.[11] The commenter expresses concern that the combined effect of the proposed rule change and another ISE proposal[12] 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.[13]

## III. Discussion and Commission Findings

After carefully reviewing the proposed rule change and the comment submitted, the Commission finds that the proposal is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange.[14] In particular, the Commission finds that the proposed rule change is consistent with Section 6(b)(5) of the Act,[15] which, among other things, requires that the rules of a national securities exchange be designed to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating 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. The Commission also finds that the proposed rule change is consistent with Section 6(b)(8) of the Act,[16] which requires that the rules of an exchange not

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11 See BOX Comment, supra note 4.

12 The BOX Comment, supra note 4, was submitted in connection with SR-ISE-2008-29. In SR-ISE-2008-29, the ISE proposed to allow members to enter orders into the PIM at a price that matches the NBBO when the ISE market is inferior to the NBBO. The Commission approved SR-ISE-2008-29. See Securities Exchange Act Release No. 57847 (May 21, 2008), 73 FR 30987 (May 29, 2008).

13 See BOX Comment, supra note 4.

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

15 15 U.S.C. 78f(b)(5).

16 15 U.S.C. 78f(b)(8).

impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

The Commission believes that, given the electronic environment on ISE, reducing each of the exposure periods from three seconds to one second as proposed could facilitate the prompt execution of orders, while continuing to provide market participants with an opportunity to compete for exposed bids and offers. To substantiate that ISE members could receive, process, and communicate a response back to the Exchange within one second, the Exchange stated that it distributed a survey to ISE members that regularly participate in orders executed through the mechanisms that would be affected by the proposal. ISE stated that the survey results indicated that it typically takes, at most, 110 milliseconds, for members to receive, process, and respond to broadcast messages related to the various mechanisms. According to the ISE, members who responded to the survey also indicated that reducing the exposure period to one second would not impair their ability to participate in orders executed through the mechanisms.[17] Accordingly, the Commission believes that it is consistent with the Act for ISE to reduce the order handling and exposure times discussed herein from three seconds to one second.

The Commission does not agree with the concerns raised by the commenter. Based on the ISE's statements regarding the survey results, the Commission believes that market participants should continue to have opportunities to compete for exposed bids and offers within a one second exposure period.

[17] The ISE stated that all of the eight members that responded to the specific timing questions, and two of the three members that did not answer the specific timing questions, indicated that reducing the crossing exposure timer to one second would not impair their ability to participate in ISE crossing orders. The ISE stated that one member responded that it could not measure the specific times and indicated that it would prefer to keep the exposure periods at three seconds. See Notice.

The Commission finds good cause to approve the proposed rule change prior to the thirtieth day after publication for comment in the Federal Register. The Commission notes that the proposed rule change was noticed for the full comment period and no additional comments were received.[18] The Commission also notes that the proposed rule change is substantially similar to a recently approved proposal submitted by the Chicago Board Options Exchange, Incorporated[19] and the Commission believes that ISE has provided reasonable support for ISE's belief that ISE market participants would continue to have an opportunity to compete for exposed bids and offers if exposure periods were reduced to one second. Therefore, the Commission finds good cause, consistent with Section 19(b)(2) of the Act,[20] to approve the proposed rule change on an accelerated basis.

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[18] The BOX Letter was received prior to the publication of the Notice. See BOX Comment, supra note 4.

[19] See Securities Exchange Act Release No. 58088 (July 2, 2008), 73 FR 39747 (July 10, 2008).

[20] 15 U.S.C. 78s(b)(2).

IV. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,[21] that the proposed rule change (SR-ISE-2007-94), as modified by Amendments No. 1 and 3, be, and hereby is, approved on an accelerated basis.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[22]

Florence E. Harmon
Acting Secretary

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[21] 15 U.S.C. 78s(b)(2).

[22] 17 CFR 200.30-3(a)(12).