

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-54644; File No. SR-ISE-2004-17)

October 23, 2006

Self-Regulatory Organizations; International Securities Exchange, Inc.; Order Approving a Proposed Rule Change and Amendment No. 1 Thereto Relating to Market Maker Orders

I. Introduction

On May 26, 2004, the International Securities Exchange, Inc. (“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 proposal to eliminate the restriction on Electronic Access Members (“EAMs”) representing ISE market maker orders, provided that such orders are identified as orders for the account of an ISE market maker. The Exchange filed Amendment No. 1 with the Commission on August 14, 2006.³ The amended proposal was published for comment in the Federal Register on September 14, 2006.⁴ The Commission received no comments on the proposal. This order approves the proposal, as amended.

II. Description of the Proposal

The Exchange proposes to amend ISE Rule 717(g) to eliminate the restriction on EAMs representing ISE market maker orders, provided that such orders are identified as orders for the account of an ISE market maker. Currently, under ISE Rules, EAMs generally are not permitted to represent orders for the account of an ISE market maker. In its filing with the Commission, the Exchange stated that it initially included this restriction in its rules due to a system limitation.

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ Amendment No. 1 replaced and superceded the original filing in its entirety.

⁴ See Securities Exchange Act Release No. 54415 (September 7, 2006), 71 FR 54321.

Specifically, allowing ISE market makers to enter orders through another member instead of directly might have created an opportunity for ISE market makers to avoid certain limitations on market maker trading contained in the Exchange's Rules.⁵

The Exchange represents that it has developed the capability for EAMs to mark orders to show that they are for the account of an ISE market maker. A marked order can be tracked through the Exchange's surveillance system as if it were directly entered by the market maker. Therefore, the Exchange proposes to eliminate the prohibition against EAMs entering orders for the account of ISE market makers in most circumstances. However, the proposal would continue to prohibit an EAM from entering an order solicited from an ISE market maker into the Solicited Order Mechanism and the Price Improvement Mechanism—functionalities that are designed to expose solicited transactions to the market—if the market maker is assigned to the options class that is the subject of the order.⁶

III. Discussion

After careful review, 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.⁷ In particular, the Commission believes that the proposal is consistent with the requirements of Section 6(b)(5) of the Act,⁸ which requires, among other

⁵ See, e.g., ISE Rule 805 (Market Maker Orders).

⁶ This limitation on entering orders solicited from market makers assigned to the options class was included in a rule change by the CBOE (the "Automated Improvement Mechanism" or "AIM") recently approved by the Commission. See Securities Exchange Act Release No. 53222 (Feb. 3, 2006), 71 FR 7089 (Feb. 10, 2006). The execution of solicited transactions through AIM is similar to the execution of orders through the ISE's Price Improvement Mechanism.

⁷ 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).

⁸ 15 U.S.C. 78f(b)(5).

things, that the rules of a national securities exchange be designed to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transaction 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 notes that ISE's proposal should permit EAMs to represent orders of ISE market makers without compromising the Exchange's ability to surveil their trading activity. Thus the proposal should not impact the Exchange's execution of its regulatory obligations. In addition, the proposed provision prohibiting an EAM from entering an order solicited from an ISE market maker into the Solicited Order Mechanism and the Price Improvement Mechanism in that ISE market maker's assigned class would permit those two functionalities to remain mechanisms for exposing solicited transactions to the competition of the marketplace.

IV. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,⁹ that the proposed rule change (File No. SR-ISE-2004-17), as amended, is approved.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹⁰

Nancy M. Morris
Secretary

⁹ 15 U.S.C. 78s(b)(2).

¹⁰ 17 CFR 200.30-3(a)(12).