SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-72254; File No. SR-ISE-2014-26)

May 27, 2014

Self-Regulatory Organizations; International Securities Exchange, LLC; Notice of Filing and Immediate Effectiveness of Proposed Rule Change Regarding Complex Orders

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the "Act"),[1] and

Rule 19b-4 thereunder,[2] notice is hereby given that on May 20, 2014 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 the Substance of the Proposed
        Rule Change

The Exchange proposes to amend its rules to adopt additional price protections for

complex orders executed on the Exchange. The text of the proposed rule change is available on

the Exchange's Web site 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

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[1]   15 U.S.C. 78s(b)(1).

[2]   17 CFR 240.19b-4.

in Item IV below. The self-regulatory organization 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

The purpose of the proposal is to enhance the Exchange's complex order functionality by

adopting additional price protections for complex orders executed on the Exchange. The

Exchange provides in its rules several complex order protections that currently exist in the

trading system.[3] Today, under Supplementary Material .07(b) to Rule 722, the trading system

rejects any complex order strategy where all legs are to buy if it is entered at a price that is less

than the minimum price, which is calculated as the sum of the ratio times $0.01 per leg.[4]

Further, Supplementary Material .07(c) to Rule 722 provides price protection for vertical spreads

where the trading system today rejects a vertical spread order (i.e., an order to buy a call (put)

option and to sell another call (put) option in the same security with the same expiration but a

higher (lower) strike price) when entered with a net price of less than zero, and prevents the

execution of a vertical spread order at a price that is less than zero when entered as a market

order to sell.[5]

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[3]　　See Rule 722, Supplementary Material .07.

[4]　　For example, an order to buy 2 calls and buy 1 put would have a minimum price of $0.03. If such an order were entered at a price of $0.02, it would not be executable, as a price of zero would have to be assigned to one of the legs of the order.

[5]　　The vertical spread price check does not apply to complex orders executed in the Facilitation Mechanism, Solicited Order Mechanism and Price Improvement Mechanism. Complex orders executed in these mechanisms are two-sided orders where the contra-side order is willing to trade with the agency order at an agreed upon price thus removing the risk that the order was executed erroneously or at an erroneous price.

The Exchange now proposes to enhance existing price protections for certain complex orders and quotes. The Exchange recognizes two complex order strategies that could cause undue risk to market participants. In order to address these strategies, the Exchange proposes to implement functionality that prevents these complex order strategies from trading at prices outside of pre-set limits. This proposal will apply only to vertical spread orders and quotes and to calendar spread orders and quotes. With this proposed rule change, the trading system will ensure that neither of these strategies trade outside of quantifiable values by more than a pre-set amount.

While the Exchange has developed functionality where the trading system rejects vertical spreads when entered with a net price of less than zero and prevents the execution of a vertical spread order at a price that is less than zero when entered as a market order to sell, the trading system does not currently reject orders and quotes that are priced above the maximum value of this strategy. These orders and quotes trade at prices that are more than the maximum value of the strategy. With this proposal, the Exchange will allow this price protection to be adjusted by a pre-set value. As a result, the trading system will reject vertical spread orders when entered with a net price of less than zero (minus a pre-set value) and will prevent the execution of a vertical spread order at a price that is less than zero (minus a pre-set value) when entered as a market order to sell. The Exchange will establish a common pre-set value as an amount not to exceed $1.00 which will apply across all options classes. For example, assume the market for a January 30 call is 1.00 x 1.20 and for a January 31 call it is 0.95 x 1.15. Suppose the pre-set value for a minimum price check for vertical spreads is established by the Exchange as $0.10. A vertical spread order consisting of a sale of one January 30 call and the purchase of one January 31 call priced at ($0.11) will be rejected by the trading system because the limit price of this order is

below the pre-set value of ($0.10). A vertical spread market order to sell, i.e., sale of one January 30 call and the purchase of one January 31 call priced at the market, will be prevented from trading with individual bids and offers because the resulting trade, i.e., sale of January 30 call at $1.00 and purchase of January 31 call at $1.15, will result in a net price of ($0.15), which is below the pre-set value of ($0.10).

The Exchange also proposes to implement functionality where the trading system will reject a vertical spread order when entered with a net price greater than the value of the higher strike price minus the lower strike price (plus a pre-set value) and will prevent the execution of a vertical spread order at a price that is greater than the value of the higher strike price minus the lower strike price (plus a pre-set value) when entered as a market order to buy. The Exchange will establish a common pre-set value as the lesser of (i) an amount not to exceed $1.00, and (ii) a percentage of the difference between strike prices not to exceed 10%, which will apply across all options classes. For example, assume the market for a January 20 call is 10.55 x 10.70 and for a January 25 call it is 5.35 x 5.50. Suppose the pre-set value for a maximum price check of vertical spreads is established by the Exchange as the lesser of $0.10 and 5%. The maximum price for a vertical spread order consisting of the purchase of one January 20 call and the sale of one January 25 call is $5.10, which is calculated as the lesser of the difference between the strike prices plus the pre-set buffer, or $5.10, and the difference between the strike prices plus the pre-set buffer percentage of the strike prices difference, or $5.25. The trading system will therefore accept a vertical spread order consisting of a purchase of one January 20 call and the sale of one January 25 call priced at $5.00 but will reject a vertical spread order priced at $5.15. A vertical spread market order to buy, i.e., purchase of one January 20 call and sale of one January 25 call priced at the market, will be prevented from trading with individual bids and offers because the

resulting trade, i.e., purchase of January 20 call at $10.70 and sale of January 25 call at $5.35, will result in a net price of $5.35, which is above the maximum price of $5.10.

A calendar spread is an order to buy a call (put) option with a longer expiration and to sell another call (put) options with a shorter expiration in the same security at the same strike price. A buyer of a calendar spread would buy a longer expiration and sell a shorter expiration in the same security at the same strike price while a seller of a calendar spread would sell a longer expiration and buy a shorter expiration in the same security at the same strike price. With this proposal, the Exchange proposes to implement functionality where the trading system will reject a calendar spread order when entered with a net price of less than zero (minus a pre-set value), and will prevent the execution of a calendar spread order at a price that is less than zero (minus a pre-set value) when entered as a market order to sell. The proposed price protection for calendar spreads will protect both buyers and sellers of calendar spreads. The Exchange will establish a common pre-set value as an amount not to exceed $1.00 which will apply across all options classes. For example, assume the market for a February 30 call is 1.00 x 1.20 and for a January 30 call it is 0.95 x 1.15. Suppose the pre-set value for a minimum price check of calendar spreads is established by the Exchange as $0.10. An order to sell a calendar spread consisting of a sale of one February 30 call and the purchase of one January 30 call priced at ($0.11) will be rejected by the trading system because the limit price of this order is below the pre-set value of ($0.10). A market order to sell a calendar spread consisting of a sale of one February 30 call and the purchase of one January 30 call priced at market, will be prevented from trading with individual bids and offers because the resulting trade, i.e., sale of February 30 call at $1.00 and purchase of January 30 call at $1.15 will result in a net price of ($0.15), which is below the pre-set value of ($0.10).

For purposes of the price protections set forth in Rule 722, Supplementary Material .07(c)(1) and in proposed Rule 722, Supplementary Material .07(c)(3), the Exchange will set a common pre-set value not to exceed $1.00 to be applied uniformly across all classes. For purposes of the price protections set forth in proposed Rule 722, Supplementary Material .07(c)(2), the Exchange will set a common pre-set value of (1) an amount not to exceed $1.00 and (2) a percentage of the difference between strike prices not to exceed 10% to be applied uniformly across all classes.

The Exchange notes, however, that there may be a need to adjust these values. For example, the Exchange may determine at some future point in time to adjust the established pre-set value for all options classes. Any change to the established pre-set value will be within the parameters prescribed in the rules and will be communicated to Exchange Members via circular.

The Exchange believes adopting a buffer is reasonable because while market participants may in certain situations be willing to trade a strategy beyond its minimum value, these trades could occur at erroneous prices without a cap. The Exchange's ability to adjust the pre-set value will provide market participants greater flexibility to execute their trading strategies as it will allow market participants to execute vertical and calendar spreads even if the strategy is priced outside its intrinsic value.

The proposed price checks will not apply to complex orders executed in the Facilitation Mechanism, Solicited Order Mechanism and Price Improvement Mechanism. Complex orders executed in these mechanisms are two-sided orders where the contra-side order is willing to trade with the agency order at an agreed upon price thus removing the risk that the order was executed erroneously or at an erroneous price.

2.   Statutory Basis

The Exchange believes that its proposal is consistent with Section 6(b) of the Securities

Exchange Act of 1934 (the "Act")[6] in general, and furthers the objectives of Section 6(b)(5) of

the Act[7] in particular, in that it is designed to promote just and equitable principles of trade, to

remove impediments to and perfect the mechanism for a free and open market and a national

market system, and, in general, to protect investors and the public interest. The Exchange

proposes to adopt the price protections described in the interest of protecting investors and to

assure fair and orderly markets on the Exchange.

As discussed above, the Exchange believes that rejecting vertical spread orders that are

entered at a price greater than their intrinsic value and preventing the execution of such orders at

a price greater than their intrinsic value when they are entered as a buy market order protects

investors from executing these orders at erroneous prices. The Exchange further believes that

rejecting calendar spread orders that are entered at a negative price also protects investors from

executing orders that were likely entered in error, and that preventing the execution of such

orders at negative prices when they are entered as a sell market order, protects investors from

paying to sell a strategy when they expected to receive payment for selling the strategy.

The Exchange notes, however, that in certain situations, market participants willingly

want to execute certain trading strategies even if such trades occur outside their intrinsic value or

at seemingly erroneous prices. The Exchange believes it is appropriate to provide market

participants flexibility to allow them to execute these trading strategies and therefore to adopt a

buffer to permit the execution of such trading strategies. The Exchange believes it is reasonable

to adopt a buffer to give the Exchange the ability to adjust the pre-set value uniformly across all

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[6]   15 U.S.C. 78f(b).

[7]   15 U.S.C. 78f(b)(5).

options classes in the event the Exchange believes a different pre-set value is more appropriate.

Finally, the Exchange notes that it provides these protections for the benefit of, and in

consultation with, its members. The Exchange believes the proposed rule change will help the

Exchange to maintain a fair and orderly market, and provide a valuable service to investors.

      B.   <u>Self-Regulatory Organization's Statement on Burden on Competition</u>

The proposed rule change specifies circumstances in which the trading system does not

provide an automatic execution in the interest of protecting investors against the execution of

erroneous orders or the execution of orders at erroneous prices. As such, the proposal does not

impose any burden on competition.

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

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.   <u>Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action</u>

Because the foregoing proposed rule change does not significantly affect the protection of

investors or the public interest, does not impose any significant burden on competition, and, by

its terms, does not become operative for 30 days from the date on which it was filed, or such

shorter time as the Commission may designate, it has become effective pursuant to Section

19(b)(3)(A)[8] of the Act and Rule 19b-4(f)(6)[9] thereunder. The Exchange provided the

Commission with written notice of its intent to file the proposed rule change, along with a brief

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[8]   15 U.S.C. 78s(b)(3)(A).

[9]   17 C.F.R. 240.19b-4(f)(6).

description and text of the proposed rule change, at least five business days prior to the date of filing the proposed rule change.

At any time within 60 days of the filing of the proposed rule change, the Commission summarily may temporarily suspend such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act.

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-2014-26 on the subject line.

Paper comments:

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

All submissions should refer to File Number SR-ISE-2014-26. 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 website (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 website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington DC, 20549, 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 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-ISE-2014-26, 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.[10]

Kevin M. O'Neill
Deputy Secretary

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[10] 17 CFR 200.30-3(a)(12).