SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-63002; File No. SR-ISE-2010-81)

September 28, 2010

Self-Regulatory Organizations; International Securities Exchange, LLC; Order Granting Approval of Proposed Rule Change Relating to Trading Options on a Reduced Value of the DAX Index, Including Long-Term Options

I. Introduction

On August 3, 2010, the International Securities Exchange, Inc. (the "Exchange" or the "ISE") filed with the Securities and Exchange Commission (the "Commission"), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the "Act"),[1] a proposed rule change to amend its rules to trade options on a reduced value DAX Index. The proposed rule change was published for comment in the Federal Register on August 18, 2010.[2] The Commission received no comment letters on the proposed rule change. This order approves the proposed rule change.

II. Description

The Exchange proposes to amend certain of its rules to allow the listing and trading of options on the Mini DAX, which represents 1/10th of the full value of the DAX Index. In addition to options on the Mini DAX, the Exchange proposes to list long-term options on the Mini DAX (the "Mini DAX LEAPS").[3] Options on the Mini DAX will be A.M. cash-settled and will have European-style exercise provisions.

Index Design and Composition

The DAX Index is a capitalization-weighted index where the weight of any individual component is proportional to its respective share in the total market capitalization of all the

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

2 See Securities Exchange Act Release No. 62703 (August 12, 2010), 75 FR 51134.

3 Under ISE Rule 2009(b), "Long-Term Index Options Series," the Exchange may list long-term options that expire from 12 to 60 months from the date of issuance.

components. The DAX Index consists of the 30 most highly liquid and capitalized German stocks ranked by float-adjusted market capitalization.[4] The management board of Deutsche Börse AG ("DBAG") decides whether changes are to be made to the composition of the index on an annual basis in September but also performs quarterly reviews of the components' free float.

Index Calculation and Index Maintenance

Index levels for options on the Mini DAX will be calculated by DBAG or its agent, and disseminated by ISE every 15 seconds during the Exchange's regular trading hours to market information vendors via the Options Price Reporting Authority ("OPRA").[5] The level of the DAX Index reflects the float-adjusted market value of the component stocks relative to a particular base period and is computed by dividing the total market value of the companies in each index by its respective index divisor.[6]

The DAX Index is calculated using the last traded price of the component securities. If a component security does not open for trading, the price of that security at the close or the index on the previous day is used in the calculation.[7]

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4 Float-adjusted market capitalization (as opposed to an unadjusted methodology) refers to the number of free-float shares available multiplied by the share price. A "free-float" index methodology usually excludes shares held by strategic investors by way of cross ownership, government ownership, private ownership and restricted share ownership.

5 The Exchange shall also disseminate these values to its members.

6 A divisor is an arbitrary number chosen at the starting date of an index to fix the index starting value. The divisor is adjusted periodically when capitalization amendments are made to the constituents of the index in order to allow the index value to remain comparable over time. Without a divisor the index value would change when corporate actions took place and would not reflect the true value of an underlying portfolio based upon the index.

7 The DAX Index is published daily and is available real-time on ThomsonReuters, Bloomberg, and other market information systems which disseminate information on a real time basis.

The DAX Index is currently updated on a real-time basis from 9 a.m. to 5:45 p.m. (Frankfurt time), which generally corresponds to 3 a.m. to 11:45 a.m. (New York time). The Exchange, or its agent, shall disseminate Mini DAX Index values via OPRA or major market data vendors between 3 a.m. and 11:45 a.m. (New York time). After 11:45 a.m. (New York time), the Exchange, or its agent, shall disseminate a static value of the Mini DAX until the close of trading each day.

The DAX Index is monitored and maintained by DBAG. DBAG makes all necessary adjustments to the indexes to reflect component deletions, share changes, stock splits, stock dividends (other than an ordinary cash dividend), and stock price adjustments due to restructuring, mergers, or spin-offs involving the underlying components.

The DAX Index is subject to a full review and, if necessary, ordinary adjustments are made once a year in September, where all components are screened for eligibility and ranked based on liquidity and market capitalization. Quarterly reviews are also performed in March, June, September and December, where components' free float levels are reviewed and extraordinary adjustments may be made. If a component company is deleted from the DAX Index between reviews as a result of a merger, takeover or other corporate action, the highest ranking company will replace it in the index.

The Exchange has represented that it will monitor the DAX Index on a quarterly basis. The Exchange will notify the staff of the Division of Trading and Markets of the Commission by filing a proposed rule change pursuant to Rule 19b-4 and will cease to list any additional series for trading, if, with respect to the DAX Index: (i) the number of securities in the DAX Index drops by $1/3^{rd}$ or more; (ii) 10% or more of the weight of the DAX Index is represented by component securities having a market value of less than €50 million; (iii) 10% or more of the weight of the DAX Index is represented by component securities trading less than 20,000 shares per day; or (iv) the largest component security accounts for more than 15% of the weight of the DAX Index or the largest five components in the aggregate account for more than 50% of the weight of the DAX Index.

The Exchange will also notify the staff of the Division of Trading and Markets of the Commission immediately in the event DBAG ceases to maintain and calculate the DAX Index, or in the event values of the DAX Index are not disseminated every 15 seconds by a widely available source. In such cases, the Exchange will not list any additional series for trading and will limit all transactions in the options to closing transactions for the purpose of maintaining a fair and orderly market and protecting investors.

Contract Specifications

The Mini DAX is a broad-based index. Options on the Mini DAX are European-style and A.M. cash-settled. The Exchange's standard trading hours for broad-based index options (9:30 a.m. to 4:15 p.m., New York time), as set forth in ISE Rule 2008(a), will apply to the trading of options on the Mini DAX.

The Exchange proposes to list options on the Mini DAX in the three consecutive near-term expiration months, plus up to three successive expiration months in the March cycle. For example, consecutive expirations of January, February, March, plus June, September, and December expirations would be listed.[8]

The Exchange proposes to set minimum strike price intervals for Mini DAX options at 1 point intervals. The minimum tick size for series trading below $3 shall be $0.05, and for series trading at or above $3 shall be $0.10.

[8] See Rule ISE 2009(a)(3).

Exercise and Settlement Value

Options on the Mini DAX will expire on the Saturday following the third Friday of the expiration month. Trading in options on the Mini DAX will normally cease at 4:15 p.m. (New York time) on the Thursday preceding an expiration Saturday. The index value for exercise of the Mini DAX options will be calculated by DBAG based on the Xetra intra-day auction prices for each of the component companies. That value is also used as the basis for settlement of DAX Index futures and options contracts traded on Eurex.

The intra-day auction occurs between 1:00 p.m. and 1:05 p.m. (German time) on the third Friday of the expiration month, which generally corresponds to 7 a.m. to 7:05 a.m. (New York time). Therefore, because trading in the expiring contract months will normally cease on a Thursday at 4:15 p.m. (New York time), the index value for exercise will be determined the day after trading has ceased, i.e., during the Friday afternoon Xetra trading session, or generally by 7:05 a.m. (New York time). If no price is established for a component company during the Xetra intraday auction, then the next available price is used. If no price is available by the end of the Xetra trading session then the last price available is used for calculation. When the auction is finished, the index values are disseminated as the settlement values. The settlement values are widely disseminated through major market data vendors including ThomsonReuters and Bloomberg.

If the Frankfurt Stock Exchange is closed on the Friday before expiration, but the ISE remains open, then the last trading day for expiring Mini DAX options will be moved earlier to Wednesday as if the ISE had had a Friday holiday. The settlement index value used for exercise will be calculated during Xetra's intra-day auction on Thursday morning.

Position Limits

For options on the Mini DAX, the Exchange proposes to establish aggregate position limits at 250,000 contracts on the same side of the market, provided no more than 150,000 of such contracts are in the nearest expiration month series. Additionally, under ISE Rule 2006, an index option hedge exemption for public customers may be available which may expand the position limit up to an additional 750,000 contracts.[9] Furthermore, proprietary accounts of members may receive an exemption of up to 500,000 contracts for the purpose of facilitating public customer orders.[10]

Exchange Rules Applicable

Exchange rules that are applicable to the trading of options on broad-based indexes will also apply to the trading of Mini DAX options.[11] Specifically, the trading of Mini DAX options will be subject to, among others, Exchange rules governing margin requirements and trading halt procedures for index options.

The Exchange proposes to apply broad-based index margin requirements for the purchase and sale of options on the Mini DAX. Accordingly, purchases of put or call options with nine months or less until expiration must be paid for in full. Writers of uncovered put or call options must deposit / maintain 100% of the option proceeds, plus 15% of the aggregate contract value (current index level x $100), less any out-of-the-money amount, subject to a minimum of the option proceeds plus 10% of the aggregate contract value for call options and a minimum of the option proceeds plus 10% of the aggregate exercise price amount for put options.

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9 The same limits that apply to position limits shall apply to exercise limits for these products.

10 See ISE Rule 413(c).

11 See ISE Rules 2000 through 2012.

The trading of options on the Mini DAX shall be subject to the same rules that presently govern the trading of Exchange index options, including sales practice rules, margin requirements, trading rules, and position and exercise limits. In addition, long-term option series having up to sixty months to expiration may be traded.[12] The trading of long-term Mini DAX options shall also be subject to the same rules that govern the trading of all the Exchange's index options, including sales practice rules, margin requirements, and trading rules.

Chapter Six of the Exchange's rules is designed to protect public customer trading and shall apply to the trading of options on the Mini DAX. Specifically, ISE Rules 608(a) and (b) prohibit Members from accepting a customer order to purchase or write an option unless such customer's account has been approved in writing by a designated Options Principal of the Member.[13] Additionally, ISE's Rule 610 regarding suitability is designed to ensure that options are only sold to customers capable of evaluating and bearing the risks associated with trading in this instrument. Further, ISE Rule 611 permits members to exercise discretionary power with respect to trading options in a customer's account only if the Member has received prior written authorization from the customer and the account had been accepted in writing by a designated Options Principal. ISE Rule 611 also requires designated Options Principals or Representatives of a Member to approve and initial each discretionary order on the day the discretionary order is entered. Finally, ISE Rule 609, Supervision of Accounts, Rule 612, Confirmation to Customers, and ISE Rule 616, Delivery of Current Options Disclosure Documents and Prospectus, will also apply to trading in of options on the Mini DAX.

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12 See Rule 2009(b)(1). The Exchange is not listing reduced value LEAPS on the Mini DAX pursuant to Rule 2009(b)(2).

13 Pursuant to ISE Rule 602, Representatives of a Member may solicit or accept customer

Capacity

The Exchange has represented that it has the necessary systems capacity to support new options series that will result from the introduction of options on the Mini DAX, including LEAPS.

Surveillance

The Exchange has represented that it has an adequate surveillance program in place for options traded on the Mini DAX. Index products and their respective symbols are integrated into the Exchange's existing surveillance system architecture and are thus subject to the relevant surveillance processes. Further, both ISE and the Frankfurt Stock Exchange, operated by DBAG, are members of the Intermarket Surveillance Group ("ISG"). Through its membership in the ISG, ISE may obtain trading information via the ISG from other exchanges who are members or affiliates of the ISG.

III. Discussion

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.[14] Specifically, the Commission finds that the proposal is consistent with Section 6(b)(5) of the Act,[15] which requires, among other things, that the rules of a national securities exchange be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, 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.

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orders for FCOs.

14 In approving this proposed rule change, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation.

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

As a national securities exchange, the ISE is required, under Section 6(b)(1) of the Act,[16] to enforce compliance by its members, and persons associated with its members, with the provisions of the Act, Commission rules and regulations thereunder, and its own rules. In addition, brokers that trade Mini DAX options will also be subject to best execution obligations and FINRA rules.[17] Applicable exchange rules also require that customers receive appropriate disclosure before trading Mini DAX options.[18] Furthermore, brokers opening accounts and recommending options transactions must comply with relevant customer suitability standards.[19]

The trading of options on the Mini DAX will be subject to the same rules that currently govern the trading of Exchange index options, as will the trading of long-term Mini DAX options. The Commission believes that the listing rules proposed by ISE are consistent with the Act. One point strike price intervals for Mini DAX options should provide investors with flexibility in the trading of Mini DAX options and further the public interest by allowing investors to establish positions that are better tailored to meet their investment objectives. The listing of options on a reduced value should provide an opportunity for investors to hedge, or speculate on, the market risk associated with the stocks comprising the DAX Index, and with the reduction in the value of the DAX Index, investors will be able to use this trading vehicle while extending a smaller outlay of capital. This may attract additional investors, and, in turn, create a more active and liquid trading environment.

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16 15 U.S.C. 78f(b)(1).

17 See NASD Rule 2320.

18 See ISE Rule 616.

19 See ISE Rule 610. See also ISE Rulebook Chapter Six for rules designed to protect

The Commission notes that index levels for options on the Mini DAX will be calculated by DBAG, or its agent, and updated on a real time basis, and will be disseminated by ISE at 15-second intervals to market information vendors via OPRA.

The Commission believes that the Exchange's proposed position and exercise limits for Mini DAX Options are appropriate and consistent with the Act. The Commission also notes that ISE has represented that it has an adequate surveillance program to monitor trading of Mini DAX Options and intends to apply its existing surveillance program to support the trading for these options.

Finally, the Commission believes that the proposal strikes a reasonable balance between the Exchange's desire to offer a wider array of products with the need to avoid unnecessary proliferation of options series and the corresponding increase in quotes. In approving the proposed rule change, the Commission has relied on the Exchange's representation that it has the necessary systems capacity to support the new options series that will be listed under this proposal. This approval order is conditioned on ISE's adherence to this representation. The Commission expects the Exchange to continue to monitor for options with little or no open interest and trading activity and to act promptly to delist such options. In addition, the Commission expects that ISE will monitor the trading volume associated with the additional options series listed as a result of this proposal and the effect of these additional series on market fragmentation and on the capacity of the Exchange's, OPRA's, and vendors' automated systems.

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public customer trading that shall apply to the trading of options on the Mini DAX.

IV. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,[20] that the proposed rule change (SR-ISE-2010-81) be, and hereby is, approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[21]

Florence E. Harmon
Deputy Secretary

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

21 17 CFR 200.30-3(a)(12).