

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-79733; File No. SR-ISE-2016-26)

January 4, 2017

Self-Regulatory Organizations; International Securities Exchange, LLC; Order Approving a Proposed Rule Change to Modify the Response Times in the Block Mechanism, Facilitation Mechanism, Solicited Order Mechanism, and Price Improvement Mechanism

I. Introduction

On November 8, 2016, the International Securities Exchange, LLC (the “Exchange” or “ISE”) 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 amend ISE Rules 716 (Block Trades) and 723 (Price Improvement Mechanism for Crossing Transactions) to modify the response times in the Block Order Mechanism, Facilitation Mechanism, Solicited Order Mechanism, and Price Improvement Mechanism (“PIM”) from 500 milliseconds to a time period designated by the Exchange of no less than 100 milliseconds and no more than 1 second. The proposed rule change was published for comment in the Federal Register on November 25, 2016.³ No comment letters were received on the proposed rule change. This order approves the proposed rule change.

II. Description of the Proposed Rule Change

ISE Rule 716 (Block Trades) 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 ISE members to obtain liquidity for the

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Securities Exchange Act Release No. 79352 (November 18, 2016), 81 FR 85277 (“Notice”).

execution of a block-size order.⁴ The Facilitation and Solicited Order Mechanisms allow ISE members to enter cross transactions seeking price improvement.⁵ ISE Rule 723 (Price Improvement Mechanism for Crossing Transactions) contains the requirements applicable to the execution of orders using the PIM. The PIM allows ISE members to enter cross transactions of any size. The Facilitation, Solicited Order Mechanisms, and PIM allow for ISE members to designate certain customer orders for price improvement and submit such orders into one of the mechanisms with a matching contra order. Once such an order is submitted, ISE commences an auction by broadcasting a message to all ISE members that includes the series, price, size, and side of the market.⁶ Further, responses within the PIM (i.e., Improvement Orders), are also broadcast to market participants during the auction.

Orders entered into the Block Order Mechanism, Facilitation Mechanism, Solicited Order Mechanism, and PIM are currently exposed to all market participants for 500 milliseconds, giving them an opportunity to enter additional trading interest before the orders are automatically executed. Under the proposal, ISE would determine an exposure period for each of the four mechanisms that is no less than 100 milliseconds and no more than 1 second.⁷

⁴ Block-size orders are orders for 50 contracts or more. See ISE Rule 716(a).

⁵ Only block-size orders can be entered into the Facilitation Mechanism, whereas only orders for 500 contracts or more can be entered into the Solicited Order Mechanism. See ISE Rule 716(d) and (e).

⁶ ISE members may choose to hide the size, side, and price when entering orders into the Block Order Mechanism.

⁷ While the proposed rule change would allow ISE to increase the exposure period up to 1 second, ISE stated that it currently intends to decrease the time period allowed for responses to 100 milliseconds. See Notice, supra note 3, at 85278. ISE further noted that its proposal is consistent with exposure periods permitted in similar mechanisms on other options exchanges. See id. at 85278. See also Securities Exchange Act Release Nos. 76301 (October 29, 2015), 80 FR 68347 (November 4, 2015) (SR-BX-2015-032) and 77557 (April 7, 2016), 81 FR 21935 (April 13, 2016) (SR-Phlx-2016-40).

III. Discussion and Commission's Findings

After careful review, 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.⁸ In particular, the Commission finds that the proposed rule change is consistent with Section 6(b)(5) of the Act,⁹ which requires, among other things, 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, and not be designed to permit unfair discrimination between customers, issuers, brokers, or dealers. The Commission also finds that the proposed rule change is consistent with Section 6(b)(8) of the Act,¹⁰ which requires that the rules of an exchange not 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 of ISE, reducing each of the exposure periods from 500 milliseconds to no less than 100 milliseconds 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 its members could receive, process, and communicate a response back to ISE within 100 milliseconds, ISE stated that it surveyed all ISE members that responded to an auction in the period beginning July 1, 2015 and ending January 15, 2016. Each of the twenty-one members surveyed indicated that they can currently

⁸ 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).

⁹ 15 U.S.C. 78f(b)(5).

¹⁰ 15 U.S.C. 78f(b)(8).

receive, process, and communicate a response back to ISE within 100 milliseconds. To implement the reduced exposure periods and help ensure that ISE's and its members' systems are working properly given the faster response times, ISE will reduce the auction time over a period of weeks, ending at 100 milliseconds. Upon effectiveness of the proposal, and at least six weeks prior to implementation of the proposed rule change, ISE will issue a circular to its members, informing them of the implementation date of the reduction of the auction from 500 milliseconds to the auction time designated by ISE (100 milliseconds) to allow members the opportunity to perform systems changes. ISE also represented that it will issue a circular at least four weeks prior to any future changes, as permitted by its rules, to the auction time.¹¹ In addition, ISE reviewed all executions occurring in the mechanisms by ISE members from March 28, 2016 to April 25, 2016. This review of executions in the mechanisms indicated that approximately 98% of responses that resulted in price improving executions at the conclusion of an auction were submitted within 500 milliseconds. Approximately 94% of responses that resulted in price improving executions at the conclusion of an auction were submitted within 100 milliseconds, and 83% were submitted within 50 milliseconds of the initial order.¹² Furthermore, with regard to the impact of the proposal on system capacity, ISE has analyzed its capacity and represented that it has the necessary systems capacity to handle the potential additional traffic associated with the additional transactions that may occur with the implementation of the reduction in the auction duration to no less than 100 milliseconds.¹³

Based on ISE's statements, the Commission believes that market participants should continue to have opportunities to compete for exposed bids and offers within an exposure period

¹¹ See Notice, supra note 3, at 85279.

¹² See id.

¹³ See id.

of no less than 100 milliseconds and no more than 1 second.¹⁴ Accordingly, the Commission believes that it is consistent with the Act for the Exchange to modify the response times in the Block Mechanism, Facilitation Mechanism, Solicited Order Mechanism, and PIM from 500 milliseconds to a time period designated by the Exchange of no less than 100 milliseconds and no more than 1 second.

IV. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,¹⁵ that the proposed rule change (SR-ISE-2016-26) be, and hereby is, approved.

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

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Assistant Secretary

¹⁴ The Commission notes that the ability to designate such an exposure time period is consistent with the rules of other options exchanges. See supra note 7. See also NASDAQ Phlx Rule 1080(n)(ii)(A)(4) and NASDAQ BX Options Rules Chapter VI, Section 9(ii)(A)(3).

¹⁵ 15 U.S.C. 78s(b)(2).

¹⁶ 17 CFR 200.30-3(a)(12).