

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-79811; File No. SR-ISE-2017-01)

January 17, 2017

Self-Regulatory Organizations; International Securities Exchange, LLC; Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Amend the Schedule of Fees

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”),¹ and Rule 19b-4 thereunder,² notice is hereby given that on January 3, 2017, the International Securities Exchange, LLC (“ISE” or “Exchange”) 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 Substance of the Proposed Rule Change

The Exchange proposes to amend the Schedule of Fees as described in more detail below.

The text of the proposed rule change is available on the Exchange’s Website at <http://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 in Item IV below. The Exchange has prepared summaries, set forth in sections A, B, and C below, of the most significant aspects of such statements.

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

A. Self-Regulatory Organization’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

The purpose of the proposed rule change is to amend the Exchange’s Schedule of Fees to eliminate, for all symbols other than FX symbols, the \$0.20 per contract fee applicable to Professional Customers³ for the initiating or contra side of Qualified Contingent Cross (“QCC”) orders or orders executed in the Solicitation Mechanism (“Solicitation” orders). The proposed rule change will lower the rebates that the Exchange provides to members acting as agent when Professional Customers trade with other Professional Customers and when they trade with Priority Customers for QCC and other solicited crossing orders⁴ to the same per contract rates and volume tiers that the Exchange presently provides to members acting as agent when Priority Customers⁵ trade with other Priority Customers for such orders.

As set forth in ISE Rule 715(j), a QCC is an option order type that allows members to cross at least 1,000 contracts without exposure, as long as: (i) the agency/originating side of the trade consists of an order of at least 1,000 contracts and (ii) the order is part of a Qualified Contingent Trade (“QCT”). As is further set forth in the Supplementary Material to ISE Rule 715, a QCT is a transaction consisting of two or more component orders, executed as agent or principal, where: (a) at least one component is an NMS Stock, as defined in Rule 600 of

³ A “Professional Customer” is a person or entity that is not a broker/dealer and is not a Priority Customer. See ISE Rule 100(37C).

⁴ As used herein, the phrase “other solicited crossing orders” refers to solicited crossing orders executed in the Solicitation, Facilitation, and Price Improvement Mechanisms.

⁵ Under ISE Rule 100(37A), a “Priority Customer” is a person or entity that: (i) is not a broker or dealer in securities; and (ii) does not place more than 390 orders in listed options per day on average during a calendar month for its own beneficial account(s). Pursuant to ISE Rule 713, Priority Customer orders are executed before other trading interest at the same price.

Regulation NMS under the Exchange Act of 1934; (b) all the components are effected with a product or price contingency that either has been agreed to by all respective counterparties or arranged for by a broker-dealer as principal or agent; (c) the execution of one component is contingent upon the execution of all other components at or near the same time; (d) the specific relationship between the component orders (e.g., the spread between the prices of the component orders) is determined by the time the contingent order is placed; (e) the component orders bear a derivative relationship to one another, represent different classes of shares of the same issuer, or involve the securities of participants in mergers or with intentions to merge that have been announced or cancelled; and (f) the transaction is fully hedged (without regard to any prior existing position) as a result of other components of the contingent trade. The Commission first approved the QCC order type for ISE on February 24, 2011.⁶

Today, the Exchange assesses a fee of \$0.20 per contract to Professional Customers for QCC and other solicited crossing orders.⁷ It does not assess a fee for such orders to Priority Customers.⁸ The Exchange proposes to eliminate the fee it charges to Professional Customers for QCC and Solicitation orders.

The Exchange also pays rebates on QCC and other solicited crossing orders once specified volume thresholds are met during each month.⁹ The existing rebate schedule and corresponding explanatory notes are as follows:

A. QCC and Solicitation Rebate

⁶ See Securities Exchange Act Release No. 63955 (Feb. 24, 2011), 76 FR 11533 (Mar. 2, 2011) (SR-ISE-2010-73).

⁷ See ISE Schedule of Fees, updated Nov. 1, 2016, at 6, available at https://www.ise.com/assets/documents/OptionsExchange/legal/fee/ISE_fee_schedule.pdf (“ISE Fee Schedule”).

⁸ See *id.*

⁹ See *id.* at 12.

- Members using the Qualified Contingent Cross (QCC) and/or other solicited crossing orders, including solicited orders executed in the Solicitation, Facilitation or Price Improvement Mechanisms, will receive rebates according to the table below for each originating contract side in all symbols traded on the Exchange. Once a Member reaches a certain volume threshold in QCC orders and/or solicited crossing orders during a month, the Exchange will provide rebates to that Member for all of its QCC and solicited crossing order traded contracts for that month. The applicable rebates will be applied on QCC and solicited crossing order traded contracts once the volume threshold is met. Members will receive the Non-“Customer to Customer” rebate for all QCC and/or other solicited crossing orders except for QCC and solicited orders between two Priority Customers. QCC and solicited orders between two Priority Customers will receive the “Customer to Customer” rebate or “Customer to Customer” Rebate PLUS, respectively. The volume threshold and corresponding rebates are as follows:
- Non-“Customer to Customer” and “Customer to Customer” volume will be aggregated in determining the applicable volume tier.

Originating Contract Sides	Non-“Customer to Customer” Rebate	“Customer to Customer” Rebate	“Customer to Customer” Rebate PLUS*
0 to 99,999	\$0.00	\$0.00	\$0.00
100,000 to 199,999	(\$0.05)	(\$0.01)	(\$0.05)
200,000 to 499,999	(\$0.07)	(\$0.01)	(\$0.05)
500,000 to 699,999	(\$0.08)	(\$0.03)	(\$0.05)
700,000 to 999,999	(\$0.09)	(\$0.03)	(\$0.05)
1,000,000+	(\$0.11)	(\$0.03)	(\$0.05)

*PLUS rebate is for Members with total monthly unsolicited originating Facilitation contract side volume of 175,000 or more.

As set forth in this schedule, the Exchange presently provides rebates to members acting as agents for QCC trades involving Professional Customers (both Professional-to-Professional and Professional-to-Priority trades) in accordance with the “Non-‘Customer to Customer’” schedule for all qualifying executed QCC and solicited crossing orders, while it provides rebates to members acting as agents for such trades involving all Priority Customers (Priority-to-Priority trades) in accordance with the “Customer to Customer” or “Customer to Customer Rebate Plus” schedules.¹⁰ The Exchange proposes to modify its rebate schedule to state that QCC and other solicited crossing orders between Professional Customers or between Professional Customers and Priority Customers will qualify for rebates in accordance with the “Customer to Customer” or “Customer to Customer Rebate Plus” schedules.

¹⁰ See id.

The proposed changes would treat Professional Customers and Priority Customers the same with respect to fees for QCC and Solicitation orders. It would also treat QCC and other solicited crossing orders involving all Professional Customers, all Priority Customers, and a mix of Priority and Professional Customers the same with respect to rebates. The Exchange believes that it is not necessary to differentiate Professional Customers and Priority Customers for these purposes because QCC and Solicitation orders are not executed pursuant to a priority scheme.¹¹ Moreover, because of the size of these orders, the sophistication of the investors involved, and the complexity of the transactions, there is little practical difference between Priority Customers and Professional Customers with respect to QCC and Solicitation orders.

The Exchange also proposes to eliminate transaction fees for Professional Customers engaged in QCC and Solicitation orders as a means of attracting more such orders to the Exchange and to retain the business of Professional Customers vis-à-vis competing exchanges that do not presently charge Professional Customers such fees.¹² The Exchange notes that a recent modification to the ISE Rules caused many of its Priority Customers to be re-classified as

¹¹ ISE Rules provide that if, at the time a QCC or Solicitation order is entered, a Priority Customer order exists on the Exchange's order book, then in certain instances, the QCC or Solicitation order will be cancelled or the order will be executed against the Priority Customer order. See Rules 716(e) & 721. These Rules do not suggest that in this instance, the Priority Customer would receive execution priority because such a trade would be executed outside of the QCC or Solicitation Mechanism. We also note that the transaction fee schedule applicable to QCC and Solicitation orders would not apply to this trade.

¹² See NYSE AMEX Options Fee Schedule, effective Dec. 15, 2016, at https://www.nyse.com/publicdocs/nyse/markets/amex-options/NYSE_Amex_Options_Fee_Schedule.pdf; NYSE Arca Options Fees and Charges, effective Nov. 3, 2016, at https://www.nyse.com/publicdocs/nyse/markets/arca-options/NYSE_Arca_Options_Fee_Schedule.pdf; NASDAQ PHLX LLC Pricing Schedule, at <http://www.nasdaqtrader.com/Micro.aspx?id=phlxpricing>.

Professional Customers.¹³ Whereas these Customers, as Priority Customers, previously incurred no fees for executing QCC and Solicitation orders, they will incur such fees going forward as Professional Customers absent the proposed rule change.

To the extent that the Exchange proposes to eliminate fees for its Professional Customers that execute QCC and Solicitation orders, the rationale for providing rebates is diminished for QCC and other solicited crossing orders involving Professional Customers trading with other Professional Customers and with Priority Customers. Accordingly, the Exchange proposes to reduce the levels of rebates it provides for QCC and other solicited crossing orders involving Professional Customers trading with other Professional Customers and with Priority Customers to the same levels as it provides to such trades involving two Priority Customers.

2. Statutory Basis

The Exchange believes that its proposal is consistent with Section 6(b) of the Act,¹⁴ in general, and furthers the objectives of Sections 6(b)(4) and 6(b)(5) of the Act,¹⁵ in particular, in that it provides for the equitable allocation of reasonable dues, fees and other charges among members and issuers and other persons using any facility, and is not designed to permit unfair discrimination between customers, issuers, brokers, or dealers.

The Commission and the courts have repeatedly expressed their preference for competition over regulatory intervention in determining prices, products, and services in the securities markets. In Regulation NMS, while adopting a series of steps to improve the current market model, the Commission highlighted the importance of market forces in determining

¹³ See Securities Exchange Act Release No. 34-78788 (Sept. 8, 2016), 81 FR 63252 (Sept. 14, 2016) (SR-ISE-2016-19).

¹⁴ 15 U.S.C. 78f(b).

¹⁵ 15 U.S.C. 78f(b)(4) and (5).

prices and SRO revenues and, also, recognized that current regulation of the market system “has been remarkably successful in promoting market competition in its broader forms that are most important to investors and listed companies.”¹⁶

Likewise, in NetCoalition v. Securities and Exchange Commission (“NetCoalition”),¹⁷ the D.C. Circuit upheld the Commission’s use of a market-based approach in evaluating the fairness of market data fees against a challenge claiming that Congress mandated a cost-based approach.¹⁸ As the court emphasized, the Commission “intended in Regulation NMS that ‘market forces, rather than regulatory requirements’ play a role in determining the market data . . . to be made available to investors and at what cost.”¹⁹

Further, “[n]o one disputes that competition for order flow is ‘fierce.’ . . . As the SEC explained, ‘[i]n the U.S. national market system, buyers and sellers of securities, and the broker-dealers that act as their order-routing agents, have a wide range of choices of where to route orders for execution’; [and] ‘no exchange can afford to take its market share percentages for granted’ because ‘no exchange possesses a monopoly, regulatory or otherwise, in the execution of order flow from broker dealers’”²⁰ Although the court and the SEC were discussing the cash equities markets, the Exchange believes that these views apply with equal force to the options markets.

¹⁶ See Securities Exchange Act Release No. 51808 (June 9, 2005), 70 FR 37497, 37499 (June 29, 2005).

¹⁷ See id. at 534-535.

¹⁸ See id. at 534.

¹⁹ See id. at 537.

²⁰ See id. at 539 (quoting Securities Exchange Act Release No. 59039 (December 2, 2008), 73 FR 74770, 74782-83 (December 9, 2008) (SR-NYSEArca-2006-21)).

It is reasonable to no longer assess a transaction fee for Professional Customer QCC and Solicitation orders and to pay a reduced rebate on Professional Customer orders because the distinction that necessitated the differentiation as between Priority Customer and Professional Customer orders is not meaningful with respect to QCC and Solicitation orders.

QCC orders are orders to buy or sell at least 1,000 contracts.²¹ These large-sized contingent orders are complex in nature and have a stock-tied component, which requires the option leg to be executed at the NBBO or better. The parties to a contingent trade are focused on the spread or ratio between the transaction prices for each of the component instruments (i.e., the net price of the entire contingent trade), rather than on the absolute price of any single component. Also, no Priority Customer priority exists with respect to QCC Orders as with orders transacted within the order book. Permitting Professional Customer orders to be treated similar to Priority Customer orders with respect to this order type may attract more QCC and Solicitation orders to the Exchange because the Exchange would no longer assess a QCC or Solicitation order transaction fee for Professional Customer orders.

Further, the Exchange recently amended its definition of a Professional Customer to add specificity with respect to the manner in which the volume threshold will be calculated to determine if orders should be treated as Professional Customer.²² Currently, members are required to review their Customers' activity on at least a quarterly basis to determine whether orders that are not for the account of a broker-dealer should be represented as Priority Customer orders or Professional Customer orders.²³ The Exchange anticipates that the specificity added to

²¹ See ISE Rule 715(j).

²² See supra note 13.

²³ Orders for any customer that had an average of more than 390 orders per day during any month of a calendar quarter must be represented as Professional Orders for the next calendar quarter. Members will be required to conduct a quarterly review and make any

the Professional Customer definition may cause current market participants that mark orders as “Priority Customer” to be required to mark those orders as “Professional Customer” instead as the calendar quarter comes to a close. Thus, orders that these market participants would have marked as “Priority Customer,” and that would not have been subject to a QCC transaction fee, would, in absence of this proposal, be marked “Professional Customer” and incur a QCC transaction fee. With this proposal, such Professional Customer orders would not be assessed a QCC transaction fee.

The Exchange believes that no longer assessing a QCC transaction fee for Professional Customer orders and paying a reduced QCC rebate on Professional Customer-to-Professional Customer and Professional Customer-to-Priority Customer orders is equitable and not unfairly discriminatory because QCC and Solicitation orders are distinctive from transactions executed within the order book. Whereas orders executed within the order book grant Priority Customers execution priority over other market participants, QCC and Solicitation orders do not grant execution priority.²⁴ Insofar as the rationale for distinguishing between Priority Customers and Professional Customers was to prevent market professionals, which have access to sophisticated trading systems with functionality unavailable to retail Customers, from taking advantage of retail Customers’ execution priority over non-retail Customer orders,²⁵ this rationale does not

appropriate changes to the way in which they are representing orders within five days after the end of each calendar quarter. While Members only will be required to review their accounts on a quarterly basis, if during a quarter the Exchange identifies a customer for which orders are being represented as Priority Customer Orders but that has averaged more than 390 orders per day during a month, the Exchange will notify the Member and the Member will be required to change the manner in which it is representing the customer’s orders within five days. See 81 FR at 63253, n.4.

²⁴ See supra note 11.

²⁵ See Securities Exchange Act Release No. 57254 (Feb. 1, 2008), 73 FR 7345, 7346 n.7 (Feb. 7, 2008).

apply to QCC or Solicitation orders. As the Commission noted when it approved the QCC order type on the Exchange:

The Commission believes that those customers participating in QCC Orders will likely be sophisticated investors who should understand that, without a requirement of exposure for QCC Orders, their order would not be given an opportunity for price improvement on the Exchange. These customers should be able to assess whether the net prices they are receiving for their QCC Order are competitive, and who will have the ability to choose among broker-dealers if they believe the net price one broker-dealer provides is not competitive. Further, broker-dealers are subject to a duty of best execution for their customers' orders, and that duty does not change for QCC Orders.²⁶

Thus, because of the size of the orders, the sophistication of the investors involved, and the complexity of the transactions, pricing differentiation between Priority Customer and Professional Customer orders is unnecessary with respect to QCC and Solicitation orders.

With respect to distinguishing Professional Customer orders from other Non-Customer participant orders, the Exchange notes that these other market participants are distinct from Professional Customers for purposes of assessing QCC transaction fees. With respect to Firm Proprietary and Non-ISE Market Makers, for example, these market participants are eligible for a Crossing Fee Cap of \$75,000 per month.²⁷ These participants are not subject to QCC transaction fees once the Crossing Fee Cap is met in a given month.²⁸ Market Makers are eligible for fee discounts, on a tiered basis, for regular orders in non-select symbols.²⁹

Insofar as the Exchange proposes to eliminate the fees it charges to Professional Customers for QCC and Solicitation orders, the Exchange believes that it would no longer be equitable to pay rebates at existing levels to members acting as agent when Professional

²⁶ See Securities and Exchange Act Release No. 63955 (February 24, 2011), 76 FR 11533 (March 2, 2011) (SR-ISE-2010-73).

²⁷ See ISE Fee Schedule, supra note 7, at 17.

²⁸ See id.

²⁹ See id. at 6-7, 12-13.

Customers trade with Priority Customers and other Professional Customers for QCC and other solicited crossing orders. Thus, the Exchange proposes to reduce these rebates to the same levels as those it pays for QCC orders involving Priority Customers trading with other Priority Customers.

Finally, the Exchange notes that the Commission recently approved a similar proposal by Phlx to eliminate its QCC transactions fees and rebates for its professional customers.³⁰

B. Self-Regulatory Organization's Statement on Burden on Competition

The Exchange does not believe that the proposed rule change will impose any burden on competition not necessary or appropriate in furtherance of the purposes of the Act. In terms of inter-market competition, the Exchange notes that it operates in a highly competitive market in which market participants can readily favor competing venues if they deem fee levels at a particular venue to be excessive, or rebate opportunities available at other venues to be more favorable. In such an environment, the Exchange must continually adjust its fees to remain competitive with other exchanges and with alternative trading systems that have been exempted from compliance with the statutory standards applicable to exchanges. Because competitors are free to modify their own fees in response, and because market participants may readily adjust their order routing practices, that the degree to which fee changes in this market may impose any burden on competition is extremely limited.

The initial purpose of the distinction between a Priority Customer order and a Professional Customer order was to prevent market professionals, which have access to sophisticated trading systems that contain functionality not available to retail Customers, from taking advantage of Priority Customer priority, where retail Customer orders are given execution

³⁰ See Securities Exchange Act Release No. 34-77673 (Apr. 14, 2016), 81 FR 249009 (Apr. 21, 2016) (SR-Phlx-2016-51).

priority over Non-Customer orders. Professional Customer orders are identified based upon the average number of orders entered for a beneficial account.³¹

QCC orders are by definition large-sized contingent orders that have a stock-tied component. The parties to a contingent trade are focused on the spread or ratio between the transaction prices for each of the component instruments (i.e., the net price of the entire contingent trade), rather than on the absolute price of any single component. Treating Priority Customer orders and Professional Customer orders in the same manner in terms of pricing with respect to QCC and Solicitation orders does not provide any advantage to a Professional Customer. The distinction does not create an opportunity to burden competition, for the reasons stated herein with respect to execution priority as well as the reasons below.

With respect to distinguishing Professional Customer orders from other Non-Customer participant orders, the Exchange notes that these other market participants are distinct from Professional Customers for purposes of assessing QCC transaction fees. With respect to Firm Proprietary and Non-ISE Market Makers, for example, these market participants are eligible for a Crossing Fee Cap of \$75,000 per month.³² These participants are not subject to QCC transaction fees once the Crossing Fee Cap is met in a given month.³³ Market Makers are eligible for fee discounts, on a tiered basis, for regular orders in non-select symbols.³⁴ Also, Priority Customer-to-Professional Customer orders do not impose an undue burden on intra-market competition for the reasons explained herein.

³¹ See supra note 25.

³² See ISE Fee Schedule, supra note 7, at 17.

³³ See id.

³⁴ See id. at 6-7, 12-13.

The Exchange's proposal does not place an undue burden on inter-market competition because the QCC order type is similar on other options exchanges and these exchanges may also file to eliminate the distinction between Priority Customers and Professionals for the QCC order type.³⁵ The Exchange notes that the Commission recently approved a similar proposal by Phlx to eliminate both its QCC transactions fees and its rebates for its professional customers.³⁶

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

No written comments were either solicited or received.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

The foregoing rule change has become effective pursuant to Section 19(b)(3)(A)(ii) of the Act, 20 and subparagraph (f)(2) of Rule 19b-4 thereunder,²¹ [sic] because it establishes a due, fee, or other charge imposed by ISE. At any time within 60 days of the filing of such 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. If the Commission takes such action, the Commission shall institute proceedings to determine whether the proposed rule should be approved or disapproved.

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:

³⁵ See supra note 12.

³⁶ See supra note 30.

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-2017-01 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-2017-01. 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 the filing also will be available for inspection and copying at the principal office 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-2017-01 and should be submitted by [insert date 21 days from the date of publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.³⁷

Eduardo A. Aleman
Assistant Secretary

³⁷ 17 CFR 200.30-3(a)(12).