

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-55367; File No. 4-529)

February 27, 2007

Program for Allocation of Regulatory Responsibilities Pursuant to Rule 17d-2; Order Approving and Declaring Effective a Plan for the Allocation of Regulatory Responsibilities Between the International Securities Exchange, LLC and the National Association of Securities Dealers, Inc.

Notice is hereby given that the Securities and Exchange Commission (“Commission”) has issued an Order, pursuant to Sections 17(d)¹ and 11A(a)(3)(B)² of the Securities Exchange Act of 1934 (“Act”), granting approval and declaring effective an amended and restated plan for the allocation of regulatory responsibilities (“Plan”) that was filed pursuant to Rule 17d-2 under the Act³ by the International Securities Exchange, LLC (“ISE”) and the National Association of Securities Dealers, Inc. (“NASD”) (together with ISE, the “Parties”).⁴

Accordingly, NASD shall assume, in addition to the regulatory responsibility it has under the Act, the regulatory responsibilities allocated to it under the Plan. At the same time, ISE is relieved of those regulatory responsibilities allocated to NASD under the Plan.

I. Introduction

Section 19(g)(1) of the Act,⁵ among other things, requires every self-regulatory organization (“SRO”) registered as either a national securities exchange or registered securities association to examine for, and enforce compliance by, its members and persons associated with its members with the Act, the rules and regulations thereunder, and the SRO’s own rules, unless

¹ 15 U.S.C. 78q(d).

² 15 U.S.C. 78k-1(a)(3)(B).

³ 17 CFR 240.17d-2.

⁴ See Securities Exchange Act Release No. 55057 (January 8, 2007), 72 FR 2040 (January 17, 2007) (“Notice”).

⁵ 15 U.S.C. 78s(g)(1).

the SRO is relieved of this responsibility pursuant to Section 17(d)⁶ or 19(g)(2)⁷ of the Act. Section 17(d)(1) of the Act⁸ was intended, in part, to eliminate unnecessary multiple examinations and regulatory duplication for those broker-dealers that maintain memberships in more than one SRO (“common members”).⁹ With respect to a common member, Section 17(d)(1) authorizes the Commission, by rule or order, to relieve an SRO of the responsibility to receive regulatory reports, to examine for and enforce compliance with applicable statutes, rules, and regulations, or to perform other specified regulatory functions.

To implement Section 17(d)(1), the Commission adopted two rules: Rule 17d-1¹⁰ and Rule 17d-2¹¹ under the Act. Rule 17d-2 permits SROs to propose joint plans for the allocation of regulatory responsibilities, other than financial responsibility rules, with respect to their common members. Under paragraph (c) of Rule 17d-2, the Commission may declare such a plan effective if, after providing for notice and comment, it determines that the plan is necessary or appropriate in the public interest and for the protection of investors, to foster cooperation and coordination among the SROs, to remove impediments to, and foster the development of, a national market system and a national clearance and settlement system, and is in conformity with the factors set forth in Section 17(d) of the Act. Upon effectiveness of a plan filed pursuant to

⁶ 15 U.S.C. 78q(d).

⁷ 15 U.S.C. 78s(g)(2).

⁸ 15 U.S.C. 78q(d)(1).

⁹ See Securities Act Amendments of 1975, Report of the Senate Committee on Banking, Housing, and Urban Affairs to Accompany S. 249, S. Rep. No. 94-75, 94th Cong., 1st Session 32 (1975).

¹⁰ 17 CFR 240.17d-1. Rule 17d-1 authorizes the Commission to name a single SRO as the designated examining authority (“DEA”) to examine common members for compliance with the financial responsibility requirements imposed by the Act, or by Commission or SRO rules.

¹¹ 17 CFR 240.17d-2.

Rule 17d-2, an SRO is relieved of those regulatory responsibilities for common members that are allocated by the plan to another SRO.

On January 17, 2007, the Commission published notice of the Plan filed by ISE and NASD.¹² The Commission received no comments on the Plan. The Plan is intended to replace and supersede the current 17d-2 plan between NASD and ISE and all prior amendments thereto in their entirety,¹³ and is intended to reduce regulatory duplication for firms that are common members of ISE and NASD. The text of the Plan allocates regulatory responsibilities among the Parties with respect to common members. Included in the Plan is an attachment (the “ISE Certification of Common Rules,” referred to herein as the “Certification”) that lists every ISE rule and federal securities law and rule and regulation thereunder for which, under the Plan, NASD would bear responsibility for examining, and enforcing compliance by, common members.

II. Discussion

The Commission finds that the proposed Plan is consistent with the factors set forth in Section 17(d) of the Act¹⁴ and Rule 17d-2(c) thereunder¹⁵ in that the proposed Plan is necessary or appropriate in the public interest and for the protection of investors, fosters cooperation and coordination among SROs, and removes impediments to and fosters the development of the national market system. In particular, the Commission believes that the proposed Plan could

¹² See Notice, supra note 4.

¹³ The Parties currently operate pursuant to a 17d-2 plan in which NASD has assumed certain inspection, examination, and enforcement responsibility for common members with respect to certain applicable laws, rules, and regulations (the “current NASD-ISE 17d-2 plan”). See Securities Exchange Act Release Nos. 42668 (April 11, 2000), 65 FR 21048 (April 19, 2000) (File No. 4-431) (notice of filing); 42815 (May 23, 2000), 65 FR 34762 (May 31, 2000) (File No. 4-431) (approval order).

¹⁴ 15 U.S.C. 78q(d).

¹⁵ 17 CFR 240.17d-2(c).

reduce unnecessary regulatory duplication by allocating to NASD certain responsibilities for common members that would otherwise be performed by both ISE and NASD. Accordingly, the proposed Plan promotes efficiency by reducing costs to common members. Furthermore, because ISE and NASD will coordinate their regulatory functions in accordance with the Plan, the Plan should promote investor protection.

The Commission notes that, under the Plan, ISE and NASD have allocated regulatory responsibility for all ISE rules that are substantially similar to NASD rules in that ISE's rule would not require NASD to develop one or more new examination standards, modules, procedures, or criteria in order to analyze the application of the rule, or a dual member's activity, conduct, or output in relation to such rule ("Common Rules"). These Common Rules are specifically listed in the Certification. In addition, under the Plan, the NASD would assume regulatory responsibility for any provisions of the federal securities laws and the rules and regulations thereunder that are set forth in the Certification.¹⁶

The Plan further provides that NASD shall not assume regulatory responsibility, and ISE will retain full responsibility, for: (1) surveillance and enforcement with respect to trading activities or practices involving ISE's own marketplace; (2) registration pursuant to ISE's applicable rules of associated persons (i.e., registration rules that are not Common Rules); (3) ISE's duties as a DEA under Rule 17d-1 of the Act;¹⁷ and (4) any rules of ISE that do not qualify as Common Rules, except that NASD shall be responsible for such rules with respect to any ISE member that operates as a facility, acts as an outbound router for ISE, and is a member of NASD

¹⁶ As proposed currently, however, there are no federal securities rules listed on the Certification. Therefore, at present, ISE has not been relieved of any regulatory responsibilities, pursuant to the Plan, for any provisions of the federal securities laws and the rules and regulations thereunder.

¹⁷ 17 CFR 240.17d-1.

(“Router Member”).¹⁸ Apparent violations of any ISE rules by any Router Member will be processed by NASD, and NASD will conduct any enforcement proceedings. The effect of these provisions is that regulatory oversight and enforcement responsibilities for any Router Member will be vested with NASD. These provisions should help avoid any potential conflicts of interest that could arise if ISE was primarily responsible for regulating its affiliated outbound router.¹⁹

According to the Plan, ISE will perform a review of the Certification, at least annually, or more frequently if required by changes in either the rules of ISE or NASD, to add ISE rules not included on the then-current list of Common Rules that are substantially similar to NASD rules (i.e., new rules that qualify as Common Rules or existing rules that have been amended so that they now qualify as Common Rules); delete ISE rules included in the then-current list of Common Rules that are no longer substantially similar to NASD rules (i.e., amended rules that cease to be Common Rules); and confirm that the remaining rules on the list of Common Rules continue to be ISE rules that are substantially similar to NASD rules. NASD will then confirm in writing whether the rules listed in any updated list are Common Rules as defined in the Plan. Under the Plan, ISE will also provide NASD with a current list of dual members and shall update the list no less frequently than once each quarter.

The Commission is hereby declaring effective and approving a plan that, among other things, allocates regulatory responsibility to NASD for the oversight and enforcement of all ISE rules that are substantially similar to the rules of NASD for common members of ISE and

¹⁸ Currently, ISE Route LLC is the only Router Member.

¹⁹ In a separate proposed rule change relating to the adoption of rules to govern its electronic trading system for equities, ISE represented that it would enter into a 17d-2 agreement with NASD to delegate to NASD all regulatory oversight and enforcement responsibilities with respect to the ISE’s outbound routing facility pursuant to applicable laws (i.e., the Plan). See Securities Exchange Act Release No. 54528 (September 28, 2006), 71 FR 58650, 58654 (October 4, 2006) (SR-ISE-2006-48).

NASD. Therefore, modifications to the Certification need not be filed with the Commission as an amendment to the Plan, provided that the Parties are only adding to, deleting from, or confirming changes to ISE rules in the Certification in conformance with the definition of Common Rules provided in the Plan. However, should ISE or NASD decide to add an ISE rule to the Certification that is not substantially similar to an NASD rule; delete an ISE rule from the Certification that is substantially similar to an NASD rule; or leave on the Certification an ISE rule that is no longer substantially similar to an NASD rule, then such a change would constitute an amendment to the Plan, which must be filed with the Commission pursuant to Rule 17d-2 under the Act and noticed for public comment.²⁰

The Plan also permits ISE and NASD to terminate the Plan, subject to notice, for various reasons. The Commission notes, however, that while the Plan permits the Parties to terminate the Plan, the Parties cannot by themselves reallocate the regulatory responsibilities set forth in the Plan, since Rule 17d-2 under the Act requires that any allocation or re-allocation of regulatory responsibilities be filed with the Commission.²¹

III. Conclusion

This Order gives effect to the Plan filed with the Commission in File No. 4-529. The Parties shall notify all members affected by the Plan of their rights and obligations under the Plan.

²⁰ The Commission also notes that the addition to (or eventual deletion from) the Certification of any federal securities laws, rules, and regulations for which NASD would bear responsibility under the Plan for examining, and enforcing compliance by, common members, would constitute an amendment to the Plan.

²¹ The Commission notes that paragraphs 4 and 13 of the Plan reflect the fact that NASD's responsibilities under the Plan will continue in effect until the Commission approves the termination of the Plan.

IT IS THEREFORE ORDERED, pursuant to Sections 17(d) and 11A(a)(3)(B) of the Act, that the Plan in File No. 4-529, between ISE and NASD, filed pursuant to Rule 17d-2 under the Act, is approved and declared effective.

IT IS THEREFORE ORDERED that ISE is relieved of those responsibilities allocated to the NASD under the Plan in File No. 4-529.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.²²

Florence E. Harmon
Deputy Secretary

²² 17 CFR 200.30-3(a)(34).