

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-53862; File No. SR-ISE-2006-23)

May 24, 2006

Self-Regulatory Organizations; International Securities Exchange, Inc.; Notice of Filing and Immediate Effectiveness of Proposed Rule Change and Amendment No. 1 Thereto Relating to Cancellation Fee Changes

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 May 1, 2006, the International Securities Exchange, Inc. ("ISE" or "Exchange") filed with the Securities and Exchange Commission ("Commission") the proposed rule change concerning the Exchange's cancellation fee as described in Items I, II, and III below, which Items have been prepared by the ISE. On May 18, 2006, the ISE submitted an amendment to the proposed rule change ("Amendment No. 1").³ The ISE has filed the proposed rule change as one establishing or changing a due, fee, or other charge imposed by the ISE under Section 19(b)(3)(A)(ii) of the Act⁴ and Rule 19b-4(f)(2) thereunder,⁵ which renders the proposal effective upon filing with the Commission. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ The purpose of Amendment No. 1 was to clarify the application of the proposed cancellation fee in the Notes section of the Exchange's Schedule of Fees and to include in that section an exception for the cancellation of orders that improved the Exchange's disseminated quotes at the time the orders were entered. This exception, described below, was discussed in the purpose section of the filing, but was not set forth in the text of the Schedule of Fees.

⁴ 15 U.S.C. 78s(b)(3)(A)(ii).

⁵ 17 CFR 240.19b-4(f)(2).

I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

The ISE proposes to amend its Schedule of Fees regarding its cancellation fee. The text of the proposed rule change is available on the Exchange's Internet website (http://www.iseoptions.com/legal/proposed_rule_changes.asp), at the principal office of the ISE, 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 ISE 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 ISE 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 this proposed rule change is to amend the ISE's cancellation fee. Through June 2005, the Exchange charged Electronic Access Members ("EAMs") \$1 per order canceled in excess of the number of orders executed. In File No. SR-ISE-2005-31 ("Fee Amendment"), the Exchange amended that fee in a rule change effective on filing pursuant to Section 19(b)(3)(A) of the Act.⁶ To address problems the Exchange encountered in applying the cancellation fee, the Fee Amendment applied the fee: (1) on the cancellation activity of each of an EAM's customers (including itself when it self-

⁶ See Securities Exchange Act Release No. 52177 (July 29, 2005), 70 FR 45457 (August 5, 2005) (File No. SR-ISE-2005-31).

clears), rather than the aggregate activity of all of an EAM's customers; and (2) on a per-contract, rather than a per-order basis.

Upon the Exchange's filing of the Fee Amendment, the Commission received a number of comment letters raising objections to the proposal. According to the Exchange, based on those comment letters, the Commission staff informed the ISE that it believed that the proposed fee should be subject to formal comment pursuant to Section 19(b)(2) of the Act. Accordingly, the Exchange submitted File No. SR-ISE-2005-36, which reinstated the cancellation fee as it was in effect prior to the submission of the Fee Amendment. The Exchange thereafter submitted File No. SR-ISE-2005-37 (the "19(b)(2) Fee Amendment"), a proposed rule change pursuant to Section 19(b)(2) of the Act to implement the same change that had previously been adopted in the Fee Amendment. The Exchange is withdrawing the 19(b)(2) Fee Amendment filing and submitting the instant filing.

Since the inception of the cancellation fee (except during the month of July 2005), the Exchange has charged EAMs \$1 per order canceled in excess of the number of orders executed.⁷ Recognizing that order cancellations often happen in large numbers, the purpose of the fee was to ease congestion in the ISE Order Routing System ("IORS") and to fairly allocate costs among members according to system use. According to the Exchange, experience shows that two limitations are preventing the fee from fully achieving its intended effect. First, the ISE applies the fee to the aggregate number of orders a clearing EAM cancels on behalf of itself and its customers, which tends to mask the activity of the EAM's particular customers who are responsible for the cancellations.

⁷ See Securities Exchange Act Release No. 46189 (July 11, 2002), 67 FR 47587 (July 19, 2002) (File No. SR-ISE-2002-16).

Second, because the Exchange applies the fee on a per order basis, firms have adjusted trading activity solely to avoid this fee by executing small orders to offset the cancellation of larger orders. ISE states that, if anything, this increases message traffic as firms enter more small orders to mask their order cancellations.

To address these concerns, the ISE first proposes to charge a clearing EAM based on the cancellation activity of each of its customers (including itself when it self-clears). The Exchange has enhanced its systems so that it now can identify the specific broker-dealer customers of a clearing EAM who enters and cancels orders. This will allow the Exchange to identify and charge for cancellation activity beyond aggregate numbers. The ISE similarly will be able to provide clearing EAMs with the information necessary for them to pass through resulting cancellation charges to their customers.⁸

Further, for purposes of calculating the number of trades that may offset cancellations, the Exchange proposes to consider all orders executed by the same firm in the same series on the same side of the market at the same price within 30 seconds as only one execution. The Exchange believes that this will remove the incentive for an EAM to enter multiple orders in rapid succession. To ensure that the Exchange covers only activity that is truly excessive and inappropriately uses bandwidth and system capacity, the Exchange proposes to exclude from the cancellation fee orders that improve ISE's disseminated quotation at the time the orders were entered.

⁸ The Exchange notes that this is similar to how the NYSE Arca, Inc. now imposes its cancellation fee. See Securities Exchange Act Release No. 49802 (June 3, 2004), 69 FR 32391 (June 9, 2004) (File No. SR-PCX-2004-31).

2. Statutory Basis

The basis for the proposed rule change is the requirement under Section 6(b)(4) of the Act⁹ that an exchange have an equitable allocation of reasonable dues, fees, and other charges among its members and other persons using its facilities. The ISE states that, in particular, these fees would permit the Exchange to recover capacity costs more equitably from among its members.

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

The proposed rule change does not impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act.

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

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

Because the foregoing proposed rule change, as amended, establishes or changes a due, fee, or other charged imposed by the Exchange, it has become effective pursuant to Section 19(b)(3)(A) of the Act¹⁰ and Rule 19b-4(f)(2)¹¹ thereunder. At any time within 60 days of the filing of the proposed rule change the Commission may summarily abrogate such proposed rule change if it appears to the Commission that such action is

⁹ 15 U.S.C. 78f(b)(4).

¹⁰ 15 U.S.C. 78s(b)(3)(A).

¹¹ 17 CFR 19b-4(f)(2).

necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act.¹²

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 No. SR-ISE-2006-23 on the subject line.

Paper comments:

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

All submissions should refer to File No. SR-ISE-2006-23. 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 Web site (<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

¹² For purposes of calculating the 60-day period within which the Commission may summarily abrogate the proposed rule change under Section 19(b)(3)(C) of Act,

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 inspection and copying in the Commission's Public Reference Room. 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 No. SR-ISE-2006-23 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹³

Nancy M. Morris
Secretary

¹³ the Commission considers the period to commence on May 18, 2006, the date on which the ISE submitted Amendment No. 1. See 15 U.S.C. 78s(b)(3)(C).

¹³ 17 CFR 200.30-3(a)(12).