

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-54113; File No. SR-ISE-2006-24)

July 7, 2006

Self-Regulatory Organizations; International Securities Exchange, Inc.; Order Approving a Proposed Rule Change and Amendment No. 1 Thereto and Notice of Filing and Order Granting Accelerated Approval to Amendments No. 2 and 3 Thereto to Permit the Listing and Trading of Quarterly Options Series

I. Introduction

On May 2, 2006, the International Securities Exchange, Inc. (“ISE” or “Exchange”) 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 initiate a one-year pilot program that would allow the Exchange to list and trade options series that expire at the close of business on the last business day of a calendar quarter (“Quarterly Options Series”). The Exchange filed Amendment No. 1 with the Commission on May 17, 2006.³ The amended proposal was published for comment in the Federal Register on June 1, 2006.⁴ No comments were received regarding the amended proposal. The Exchange filed Amendments No. 2 and 3 with the Commission on July 6, 2006, and July 7, 2006, respectively.⁵ This notice and order approves the proposed rule change and Amendment No. 1

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ In Amendment No. 1, a partial amendment, the Exchange made minor modifications to the proposed rule text.

⁴ See Securities Exchange Act Release No. 53857 (May 24, 2006), 71 FR 31246 (“Notice”).

⁵ In Amendment No. 2, a partial amendment, the Exchange modified the provision of the proposed rule text under which the Exchange may list additional strike prices for Quarterly Options Series. In Amendment No. 3, a partial amendment, the Exchange modified the proposed rule text to provide that the Exchange may list Quarterly Options Series with strike prices that are within \$5.00 from the closing price of the underlying security on the preceding trading day. See discussion in Part II, infra.

thereto, solicits comment on Amendments No. 2 and 3, and approves Amendments No. 2 and 3 on an accelerated basis.

II. Description of Proposed Rule

ISE proposes to amend its rules to establish a pilot program to list and trade Quarterly Options Series, which would expire at the close of business on the last business day of a calendar quarter (“Pilot Program”). Under the proposal, the Exchange could select up to five approved options classes⁶ on which Quarterly Options Series could be opened. A series could be opened on any business day and would expire at the close of business on the last business day of a calendar quarter. The Exchange also could list and trade Quarterly Options Series on any options class that is selected by another exchange that employs a similar pilot program. For each class selected for the Pilot Program, the Exchange would list series that expire at the end of the next four consecutive calendar quarters, as well as the fourth quarter of the following calendar year.

Quarterly Options Series listed on currently approved options classes would be P.M. settled and, in all other respects, would settle in the same manner as do the monthly expiration series in the same options class.

The strike price for each series would be fixed at a price per share, with two strike prices above and two strike prices below the value of the underlying security at about the time that a Quarterly Options Series is opened for trading on the Exchange. The interval between strike prices on Quarterly Options Series would be the same as the interval between strike prices for series in the same options class that expire in accordance with the normal monthly expiration cycles. In Amendment No. 3, the Exchange proposes rule text providing that the series listed by

⁶ Quarterly Options Series may be opened on indexes or on Exchange Traded Funds that satisfy the applicable listing criteria under ISE rules.

the Exchange under the Pilot Program would have strike prices that are within \$5.00 from the closing price of the underlying security on the preceding trading day.

The proposal would permit the Exchange to open for trading additional Quarterly Options Series of the same class when the Exchange deems it necessary to maintain an orderly market, to meet customer demand, or when the market price of the underlying security moves substantially from the initial exercise price or prices. In Amendment No. 2, the Exchange proposes rule text that provides that any additional series opened for trading by the Exchange would be priced within \$5.00 of the closing price of the underlying security on the preceding trading day.

ISE proposes that the Pilot Program extend one year from the date the Exchange first initiates trading in a Quarterly Options Series, which, as per the proposed rules, would be no later than July 24, 2006.⁷

III. Discussion

After careful review, the Commission finds that the proposal, as amended, 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 believes that the proposal is consistent with the requirements of Section 6(b)(5) of the Act,⁹ which requires, among other things, that the rules of a national securities exchange be designed to remove impediments to and perfect the mechanism of a free and open market and a national market system, to promote just and equitable principles of trade, and, in general, to protect investors and the public interest.

⁷ See ISE Proposed Rules 504, Supplementary Material .03, and 2009, Supplementary Material .02.

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).

The Commission believes that allowing the Exchange to list and trade Quarterly Options Series, under the terms described in the Exchange's proposal, should provide investors with new means of managing their risk exposures and carrying out their investment objectives. The Commission notes that the Pilot Program limits the series that may be opened pursuant to the Pilot Program by requiring them to have strike prices within \$5.00 of the closing price of the underlying security on the preceding trading day. The Commission believes this restriction should allow the exchange to offer a wider array of investment opportunities, while minimizing the impact on quotation message traffic. The Commission also notes that the proposal requires the Exchange to closely monitor the trading and quotation volume associated with the additional options series created under the Pilot Program and the effect of these additional series on the capacity of the Exchange's, OPRA's, and vendors' systems.¹⁰

Pursuant to Section 19(b)(2) of the Act,¹¹ the Commission finds good cause for approving the amended proposal prior to the thirtieth day after the publication of Amendments No. 2 and 3 in the Federal Register. Amendments No. 2 and 3 modify the proposed rule text by placing restrictions on the series the Exchange may open for trading in an approved class. Any series opened for trading pursuant to the Pilot Program would have strike prices within \$5.00 of the closing price of the underlying security on the preceding trading day. This restriction is modeled after the identical provision previously approved as part of the Exchange's \$1 Strike Pilot Program, and thus raises no new issues of regulatory concern.¹² The Commission finds

¹⁰ If the Exchange were to propose an extension, expansion, or permanent approval of the Pilot Program, the Exchange would be required to submit a report on the Pilot Program to the Commission at least 60 days prior to the Pilot Program expiration date. See Notice, *supra* note 4, at 31248.

¹¹ 15 U.S.C. 78s(b)(2).

¹² See ISE Rule 504(g).

good cause to accelerate approval of the amended proposal because it believes this restriction should help to minimize the Pilot Program's impact on quotation message traffic.

IV. Solicitation of Comments Concerning Amendments No. 2 and 3

Interested persons are invited to submit written data, views, and arguments concerning Amendments No. 2 and 3, including whether it 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 Number SR-ISE-2006-24 on the subject line.

Paper comments:

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

All submissions should refer to File Number SR-ISE-2006-24. 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 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 such 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-2006-24 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

V. Conclusion

For the foregoing reasons, the Commission finds that the proposed rule change, as amended, is consistent with the requirements of the Act and the rules and regulations thereunder.

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,¹³ that the proposed rule change (File No. SR-ISE-2006-24), as amended, is approved, and that Amendments No. 2 and 3 thereto are approved on an accelerated basis, as a pilot program for a one-year period commencing on the day the Exchange first initiates trading in a Quarterly Options Series, which, as per the proposed rules, would be no later than July 24, 2006.¹⁴

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.¹⁵

Nancy M. Morris
Secretary

¹³ Id.

¹⁴ See ISE Proposed Rules 504, Supplementary Material .03, and 2009, Supplementary Material .02.

¹⁵ 17 CFR 200.30-3(a)(12).