

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-77246; File No. SR-ISE-2015-30)

February 26, 2016

Self-Regulatory Organizations; International Securities Exchange, LLC; Order Instituting Proceedings to Determine Whether to Approve or Disapprove a Proposed Rule Change to Amend Rule 804(g)

I. Introduction

On November 10, 2015, the International Securities Exchange, LLC (“ISE” or the “Exchange”) filed with the Securities and Exchange Commission (the “Commission”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the “Act”)¹ and Rule 19b-4 thereunder,² a proposed rule change to require Clearing Member³ approval for a market maker to resume trading after the activation of a market-wide speed bump under ISE Rule 804(g). The proposed rule change was published for comment in the Federal Register on November 30, 2015.⁴ On January 13, 2016, the Commission extended the time period within which to approve the proposed rule change, disapprove the proposed rule change, or institute proceedings to determine whether to disapprove the proposed rule change to February 28, 2016.⁵ The Commission did not receive any comments on the proposed rule change. This order institutes

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ A “Clearing Member” is a Member that is self-clearing or an Electronic Access Member that clears transactions executed on or through the facilities of the Exchange for other Members of the Exchange. See ISE Rule 100(a)(8). An “Electronic Access Member” is an Exchange Member that is approved to exercise trading privileges associated with EAM Rights. See Article XIII, Section 13.1(l) of the Second Amended and Restated Constitution of ISE.

⁴ See Securities Exchange Act Release No. 76506 (November 23, 2015), 80 FR 74829 (November 30, 2015) (“Notice”).

⁵ See Securities Exchange Act Release No. 76893 (January 13, 2016), 81 FR 3217 (January 20, 2016).

proceedings under Section 19(b)(2)(B) of the Act⁶ to determine whether to approve or disapprove the proposed rule change.

II. Description of the Proposal

Pursuant to ISE Rule 804(g)(1), the Exchange requires market makers⁷ to provide parameters according to which the Exchange will automatically remove a market maker's quotations in all series of an options class. Additionally, the Exchange requires market makers to provide a market-wide parameter according to which the Exchange will automatically remove a market maker's quotes in all classes when, during a time period established by the market maker, the total number of quote removal events (or "curtailment events") specified in Rule 804(g)(1) and in Supplementary Material .04 to Rule 722 exceed such specified market-wide parameter.⁸ The latter market-wide risk management functionality is known as a "market-wide speed bump" and is available for quotes only on ISE or across both ISE and ISE's affiliated exchange, ISE Gemini, LLC.⁹

Currently, if ISE's trading system removes all of a market maker's quotes because a market-wide speed bump is triggered, the market maker may re-enter the market and resume trading upon notification to the Exchange's Market Operations.¹⁰ The Exchange now proposes to amend ISE Rule 804(g)(2) to require Clearing Member approval before a market maker can

⁶ 15 U.S.C. 78s(b)(2)(B).

⁷ ISE has two categories of market makers: Primary Market Makers ("PMMs") and Competitive Market Makers ("CMMs"). A PMM is appointed to each options class traded on the Exchange but a CMM may or may not be appointed to each such options class. See ISE Rule 802.

⁸ See ISE Rule 804(g)(2).

⁹ Id.

¹⁰ See Notice, supra note 4, at 74830.

resume trading.¹¹ Specifically, following a market-wide speed bump, the proposed rule requires a market maker to notify its Clearing Member(s) when it is ready to resume trading and requires each applicable Clearing Member to inform the Exchange directly when its authorization has been given for the market maker to resume trading.¹² In order to “facilitate a better response time” from Clearing Members, so that a market maker can re-enter the market, the proposal also allows Exchange staff to notify Clearing Member(s) when a market maker’s quotes have been removed pursuant to the market-wide speed bump.¹³

The Exchange believes that it is appropriate to require Clearing Member approval before a market maker can re-enter the market after a market-wide speed bump because the Clearing Member guarantees the market maker’s trades and bears the ultimate financial risk associated with those transactions. The Exchange notes that, while not all market makers are Clearing Members, all market makers require a Clearing Member’s consent to clear transactions on their behalf in order to conduct business on the Exchange.¹⁴ According to the Exchange, the proposed rule change will permit Clearing Members to better monitor and manage the potential risks assumed by a market maker and provide Clearing Members with greater control and flexibility over their risk tolerance and exposure.¹⁵

¹¹ See proposed Rule 804(g)(2).

¹² See id.

¹³ See id.

¹⁴ Each market maker authorized to trade on the Exchange must obtain from a Clearing Member a “Market Maker Letter of Guarantee” wherein the Clearing Member accepts financial responsibility for all Exchange transactions made by the market maker. See ISE Rule 808.

¹⁵ See Notice, supra note 4, at 74830. Under ISE’s current rules, the Exchange may share any Member-designated risk settings in the trading system with the Clearing Member that clears transactions on behalf of the Member. See ISE Rule 706(a).

III. Proceedings to Determine Whether to Approve or Disapprove SR-ISE-2015-30 and Grounds for Disapproval Under Consideration

The Commission is instituting proceedings pursuant to Section 19(b)(2)(B) of the Act¹⁶ to determine whether the proposed rule change should be approved or disapproved. Institution of such proceedings is appropriate at this time in view of the legal and policy issues raised by the proposed rule change, as discussed below. Institution of proceedings does not indicate that the Commission has reached any conclusions with respect to any of the issues involved. Rather, as described in greater detail below, the Commission seeks and encourages interested persons to provide additional comment on the proposed rule change.

Pursuant to Section 19(b)(2)(B) of the Act, the Commission is providing notice of the grounds for disapproval under consideration. The Commission is instituting proceedings because the proposal raises important issues that warrant further public comment and Commission consideration. Specifically, the Commission is instituting proceedings to allow for additional analysis of, and input from commenters with respect to, the proposed rule change's consistency with Section 6(b)(5) of the Act,¹⁷ which requires that the rules of a national securities exchange be designed, among other things, to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, 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.

¹⁶ 15 U.S.C. 78s(b)(2)(B). Section 19(b)(2)(B) of the Act also provides that proceedings to determine whether to disapprove a proposed rule change must be concluded within 180 days of the date of publication of notice of the filing of the proposed rule change. See id. The time for conclusion of the proceedings may be extended for up to 60 days if the Commission finds good cause for such extension and publishes its reasons for so finding. See id.

¹⁷ 15 U.S.C. 78f(b)(5).

Under ISE’s current rules, a market maker must enter continuous quotations for the options classes to which it is appointed.¹⁸ In return, the market maker receives certain benefits, including participation entitlements¹⁹ and an exception from the prohibition in Section 11(a) of the Act.²⁰ As the Commission has stated in the past, a market maker must be subject to sufficient and commensurate affirmative obligations, including the obligation to hold itself out as willing to buy and sell options for its own account on a regular or continuous basis, to justify favorable treatment.²¹ As discussed above, however, the Exchange now proposes to amend ISE Rule 804(g) to require Clearing Member approval before a market maker can resume trading after triggering a market-wide speed bump.

The Exchange justifies the change as appropriate because, “[w]hile in some cases this may result in a minimal delay for a market maker that wants to reenter the market quickly following a market-wide speed bump, the Exchange believes that Clearing Member approval...ensure[s] that the market maker does not prematurely enter the market without adequate safeguards...”²² The Exchange, however, does not provide any basis for its statement that the proposed rule would result in only a “minimal delay” for a market maker seeking to resume quoting. Moreover, the Exchange does not address how the proposal impacts the

¹⁸ See ISE Rule 804(e).

¹⁹ See, e.g., ISE Rule 713.

²⁰ 15 U.S.C. 78k(a).

²¹ See, e.g., Securities Exchange Act Release No. 68341 (December 3, 2012), 77 FR 73065, 73076 (December 7, 2012) (approving the application of Miami International Securities Exchange, LLC for registration as a national securities exchange); Securities Exchange Act Release No. 70050 (July 26, 2013), 78 FR 46622 (August 1, 2013) (approving the application of Topaz Exchange, LLC for registration as a national securities exchange); Securities Exchange Act Release No. 76998 (January 29, 2016), 81 FR 6066 (February 4, 2016) (approving the application of ISE Mercury, LLC for registration as a national securities exchange).

²² See Notice, supra note 4, at 74830.

continuous quoting obligations of market makers. The Commission accordingly believes the proposed rule change raises questions regarding the ability of market makers to meet their quoting obligations and, therefore, whether the proposed rule change is consistent with the requirements of Section 6(b)(5) of the Act.

IV. Procedure: Request for Written Comments

The Commission requests that interested persons provide written submissions of their views, data and arguments with respect to the concerns identified above, as well as any other concerns they may have with the proposed rule change. In particular, the Commission invites the written views of interested persons concerning whether the proposal is consistent with Sections 6(b)(5)²³ or any other provision of the Act, or the rules and regulations thereunder. Although there does not appear to be any issue relevant to approval or disapproval which would be facilitated by an oral presentation of views, data, and arguments, the Commission will consider, pursuant to Rule 19b-4 under the Act,²⁴ any request for an opportunity to make an oral presentation.²⁵

Interested persons are invited to submit written data, views, and arguments regarding whether the proposal should be approved or disapproved by [insert date 21 days from publication in the Federal Register]. Any person who wishes to file a rebuttal to any other person's submission must file that rebuttal by [insert date 35 days from publication in the Federal

²³ 15 U.S.C. 78f(b)(5).

²⁴ 17 CFR 240.19b-4.

²⁵ Section 19(b)(2) of the Act, as amended by the Securities Act Amendments of 1975, Pub. L. 94-29 (June 4, 1975), grants to the Commission flexibility to determine what type of proceeding—either oral or notice and opportunity for written comments—is appropriate for consideration of a particular proposal by a self-regulatory organization. See Securities Act Amendments of 1975, Senate Comm. on Banking, Housing & Urban Affairs, S. Rep. No. 75, 94th Cong., 1st Sess. 30 (1975).

Register]. In light of the concerns raised by the proposed rule change, as discussed above, the Commission invites additional comment on the proposed rule change as the Commission continues its analysis of the proposed rule change's consistency with Sections 6(b)(5) and 6(b)(8),²⁶ or any other provision of the Act, or the rules and regulations thereunder. The Commission asks that commenters address the sufficiency and merit of the Exchange's statements in support of the proposed rule change, in addition to any other comments they may wish to submit about the proposed rule change.

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-2015-30 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-2015-30. 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

²⁶ 15 U.S.C. 78f(b)(5), (b)(8).

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-2015-30 and should be submitted by [insert date 21 days from the date of publication in the Federal Register]. Rebuttal comments should be submitted by [insert date 35 days from date of publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.²⁷

Robert W. Errett
Deputy Secretary

²⁷ 17 CFR 200.30-3(a)(57).