SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-59066; File No. SR-ISE-2008-78)

December 8, 2008

Self-Regulatory Organizations; International Securities Exchange, LLC; Order Approving Proposed Rule Change Relating to Quoting Obligations for Competitive Market Makers

I. Introduction

On October 21, 2008, the International Securities Exchange, LLC ("ISE" or "Exchange") filed with the Securities and Exchange Commission ("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 relating to the Exchange's quoting obligations for Competitive Market Makers ("CMMs"). The proposed rule change was published for comment in the Federal Register on November 3, 2008.[3] The Commission received no comments on the proposal. This order approves the proposed rule change.

II. Description of the Proposal

The Exchange proposes to amend ISE Rules 713, 804 and 805 to change the quoting obligation for the Exchange's CMMs. ISE currently requires CMMs to participate in the opening and maintain continuous quotations in all of the series of at least 60 per cent of the options classes in the bin or 60 classes, whichever is less. In addition, if a CMM chooses to quote any series of an options class above and beyond this minimum requirement, it must then maintain continuous quotations in all of the series of that class throughout that trading day. In September 2007, the Exchange initiated a pilot to reduce the quoting obligations for CMMs in 20

---

1 15 U.S.C. 78s(b)(1).

2 17 CFR 240.19b-4.

3 See Securities Exchange Act Release No. 58861 (October 27, 2008), 73 FR 65432 (the "Notice").

options classes.[4] Under the Pilot, CMMs were required to maintain quotations in only 60 per cent of the series of an options class overlying the pilot program securities. The Pilot recently expired and the Exchange now proposes to change the quoting requirements for CMMs on a permanent basis.

The Exchange does not believe that the reduced quoting obligations adopted as part of the Pilot have had any negative effect on the quality of its markets.[5] Therefore, ISE proposes to adopt the 60 per cent standard for all options series on a permanent basis, except for CMMs that receive preferenced order flow. The Exchange proposes that a CMM will be required to maintain continuous quotations in at least 90% of the series of any option class in which it receives preferenced orders.

The Exchange also proposes to lower the minimum number of options classes that a CMM is required to quote from 60 to 40. The Exchange believes that lowering the requirement will attract additional market making participants on the ISE.

Finally, the Exchange proposes to amend Rule 805 (Market Maker Orders) regarding the percentage of volume a CMM may execute in options to which it is not appointed. Specifically, Rule 805 currently provides that a CMM may execute up to 25% of its volume in options classes to which it is not appointed. Because the Exchange is lowering the number of appointed classes in which a CMM is required to quote, the Exchange believes it is appropriate to base the 25%

---

4 See Securities Exchange Act Release No. 56444 (September 14, 2007), 72 FR 54089 (September 21, 2007) (Order Granting Approval of SR-ISE-2007-45 Relating to a Quote Mitigation Plan for Competitive Market Makers) (the "Pilot").

5 According to the Exchange, in practice, market makers simply widen their quotations when they do not want to trade in a particular series, so requiring them to maintain continuous quotations in all series merely increases capacity requirements for the market makers.

allowance on volume that is executed while a CMM is actually fulfilling its market maker quotation obligations.

III. Discussion and Commission Findings

After careful review, the Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange.[6] In particular, the Commission finds that the proposal is consistent with Section 6(b)(5) of the Act,[7] which requires that an exchange have rules designed 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.

The Commission believes that the proposed rule change, which is intended to reduce the number of options quotations required to be submitted without adversely affecting the quality of the Exchange's markets, is consistent with the Act. The Commission notes that the Exchange has operated a one-year Pilot program that reduced the quoting obligations for CMMs and during the Pilot period the Exchange did not observe any adverse effect on its market.[8] The Commission believes it is appropriate to adopt the modified quotation obligations for CMMs on a permanent basis. In addition, the Commission believes that it is appropriate to reduce the quoting obligations of a CMM because the percentage of volume a CMM may execute in options

---

[6] In approving this proposed rule change, the Commission notes that it has considered the proposed rule's impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

[7] 15 U.S.C. 78f(b)(5).

[8] The Commission notes that it has already approved internal quote mitigation strategies on other exchanges that relieve some market makers of the obligation to quote every series of every class to which they are appointed. See Phlx Rule 1014(b)(ii)(D)(1) and Amex Rule 994(c)(iv).

classes to which it is not appointed will be based on volume that is executed in those options classes in which a CMM maintains continuous quotes in fulfillment of its obligations as a market maker.

Finally, the Commission believes that it is appropriate to impose a higher continuous quoting requirement on CMMs who receive preferenced order flow because such CMMs receive the benefit of enhanced allocation rights and therefore should assume an increased obligation to provide continuous quotations. The Commission notes that a similar quotation standard for preferred market makers was previously adopted on another exchange.[9]

---

9 See CBOE Rule 8.13(b)(iii) (requiring a preferred market-maker to provide continuous electronic quotes in at least 90% of the series of each class for which it receives preferred market-maker orders).

IV. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,[10] that the proposed rule change (SR-ISE-2008-78) be, and hereby is, approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[11]

Florence E. Harmon
Acting Secretary

---

10 15 U.S.C. 78s(b)(2).

11 17 CFR 200.30-3(a)(12).