

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-60147; File No. SR-ISE-2009-35)

June 19, 2009

Self-Regulatory Organizations; International Securities Exchange, LLC; Notice of Filing of Proposed Rule Change Relating to Qualified Contingent Cross Orders

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the “Act”),¹ and Rule 19b-4 thereunder,² notice is hereby given that, on June 15, 2009, the International Securities Exchange, LLC (“Exchange” or the “ISE”) filed with the Securities and Exchange Commission (the “SEC” or the “Commission”) the proposed rule change as described in Items I, II, and III below, which items have been prepared by the self-regulatory organization. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

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

The Exchange is proposing a Qualified Contingent Cross Order. This rule would be effective contemporaneously with the effectiveness of the rules implementing the Order Protection and Locked/Crossed Market Plan (“Plan”).³ The text of the proposed rule change is available on the Exchange’s Internet website at <http://www.ise.com>, at the Exchange 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 self-regulatory organization included statements concerning the purpose of, and basis for, the proposed rule change and discussed any comments it

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Filing No. SR-ISE-2009-27 (“Linkage Rules”).

received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. The self regulatory organization has prepared summaries, set forth in sections A, B, and C below, of the most significant parts 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 filing is to provide for Qualified Contingent Cross Orders. The Exchange is proposing such an order type in conjunction with the Linkage Rules. Those rules, together with the underlying Plan, are based on Regulation NMS under the Securities Exchange Act of 1934, as amended (“Act”), and the rules implementing that regulation. Among other things, the Plan requires that its parties “establish, maintain and enforce written policies and procedures . . . that are reasonably designed to prevent Trade-Throughs...”⁴ A Trade-Through is a transaction in an options series at a price that is inferior to the best price available in the market.⁵ Among other things, the Linkage Rules contain provisions designed to prevent Trade-Throughs.⁶

The Plan will replace the Plan for the Purpose of Creating and Operating an Intermarket Option Linkage (“Old Plan”), and the Linkage Rules will replace the ISE’s current rules implementing the Old Plan. The Old Plan and the ISE’s current rules provide a limited Trade-Through exemption for “Block Trades,” defined to be trades of 500 or more contracts with a premium value of at least \$150,000.⁷ However, as with Regulation NMS, the Plan does not provide a Block Trade exemption. The Exchange believes that the loss of the Block Trade

⁴ Section 5(a) of the Plan.

⁵ Section 2(21) of the Plan.

⁶ Proposed Rule 1901.

⁷ Old Plan Sections 2(3) and 8(c)(i)(C); ISE Rule 1902(d)(2).

exemption will adversely affect the ability of its members to effect large trades that are tied to stock.⁸ Thus, the Exchange is proposing the Qualified Contingent Trade Order as a limited substitute for the Block Trade exemption, to be implemented contemporaneously with the Linkage Rules.

While Regulation NMS does not provide a Block Trade exemption from Trade-Through liability, the Commission, by order, has provided Trade-Through relief for “Qualified Contingent Trades” (“QCTs”).⁹ The QCT Release provides an exemption from Trade-Through liability in the equity market for multi-component, fully-hedged trades where one order is contingent on the execution of one or more additional orders. Building on this concept, we propose that when an ISE member effects a QCT trade in a Regulation NMS Stock that the member be permitted to cross the options leg of the trade on the ISE immediately upon entry if the order is for at least 500 contracts, is part of a QCT, and is executed at a price at least equal to the national best bid or offer (“NBBO”).

We propose to define a QCT trade substantively identical to the Commission’s definition in the QCT release. Thus, the trade would have to meet the following conditions:

- At least one component must be an NMS Stock;

⁸ Both the Old Plan and the Plan have a Trade-Through exemption for “Complex Trades,” including options trades tied to stock. See Old Plan section 7(c)(iii)(G), and Plan section 5(b)(viii). However, and while not free from doubt, the common application of that exemption has been to apply it only to trades announced to exchange members as a single trade at a net price. As so interpreted, that exemption would cover only trades executed in the ISE’s “Complex Order Mechanism.” See ISE Rule 722.

⁹ Release No. 34-57620 (April 4, 2008) (the “QCT Release”). That release superseded a release initially granting the Qualified Contingent Trade exemption, Release No. 34-54389 (August 31, 2006).

- All the components must be effected with a product price contingency that either has been agreed to by all the respective counterparties or arranged for by a broker-dealer as principal or agent;
- The execution of one component must be contingent upon the execution of all other components at or near the same time;
- The specific relationship between the component orders (e.g., the spread between the prices of the component orders) must be determined by the time the contingent order is placed;
- The component orders must bear a derivative relationship to one another, represent different classes of shares of the same issuer, or involve the securities of participants in mergers or with intentions to merge that have been announced or cancelled; and
- The transaction must be fully hedged (without regard to any prior existing position) as a result of other components of the contingent trade.¹⁰

ISE will adopt policies and procedures to ensure that members use the Qualified Contingent Cross Order properly. First, we will require members to properly mark all Qualified Contingent Cross Orders as such. In addition, we will institute surveillance procedures to identify that the member executed the stock leg of the transaction at or near the same time as the options leg.

We believe that the Qualified Contingent Cross Order is necessary to facilitate the execution of large stock/options combination orders. Broker-dealers can execute these orders in

¹⁰ Consistent with the QCT Release we would require that the member demonstrate that the transaction is fully hedged using reasonable risk-valuation methodologies. See the QCT Release at note 9.

various ways, such as on the ISE's complex order book.¹¹ However, broker-dealers often seek the flexibility to execute the various legs of such orders in different markets, and may seek to execute the options leg alone on the ISE. Under the Plan, and without a Block Trade exemption, it will be extremely difficult for ISE members to effect the execution of the options leg on the ISE.

The Contingent Trade Order will address those concerns by permitting the member to provide its customer a net price for the entire trade, and then allowing the member to execute the options leg of the trade on the ISE at a price at least equal to the NBBO while using the CQT [sic] exemption to effect the trade in the equities leg at a price necessary to achieve the net price. While there is no exposure for price improvement for the options leg of a stock-option order with our proposed Qualified Contingent Cross Order, that order must be executed at the NBBO or better,[sic]. Moreover, since the price of a stock-options order is a net price derived from the price of the options leg and the price of the stock leg, we believe it is reasonable for any potential improvement of the net price to originate from the execution of the stock leg. On balance, we believe that providing members with the certainty that they can execute the options legs of these large complex orders for their customers, coupled with the flexibility members have with respect to the price at which the equity legs are executed, will provide customers with the flexibility needed to achieve their investment objectives.

2. Statutory Basis

The basis under the Act for this proposed rule change is the requirement under Section 6(b)(5) that an exchange have rules that are designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to remove impediments to and

¹¹ See ISE Rule 722, Supplementary Material .01 and .02.

perfect the mechanism for a free and open market and a national market system, and, in general, to protect investors and the public interest. In particular, the proposal will facilitate the ability of ISE members to execute large options orders that are tied to stock in an efficient manner, while also protecting the national market system against trade-throughs.

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

Within 35 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

(A) By order approve such proposed rule change, or

(B) Institute proceedings to determine whether the proposed rule change should be disapproved.

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 Number SR-ISE-2009-35 on the subject line.

Paper comments:

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

All submissions should refer to File Number SR-ISE-2009-35. 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, 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 will also be available for inspection and copying at the principal office of the self-regulatory organization. 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-2009-35 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.¹²

Florence E. Harmon
Deputy Secretary

¹² 17 CFR 200.30-3(a)(12).