

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-53946; File No. SR-ISE-2006-27]

### Self-Regulatory Organizations; International Securities Exchange, Inc.; Notice of Filing of Proposed Rule Change Relating to Automatic Execution of Non-Customer Orders

June 6, 2006.

Pursuant to section 19(b)(1) of the Securities Exchange Act of 1934, as amended, (“Act”)<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on May 15, 2006, the International Securities Exchange, Inc. (“ISE” or “Exchange”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the Exchange. 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 proposes to amend ISE Rule 714 to provide that incoming Non-Customer Orders will not be automatically executed at prices that are inferior to the best bid or offer on another national securities exchange and to update the rule text with respect to the current handling of “fill-or kill” orders. The Exchange represents that this proposed rule change with respect to the handling of Non-Customer Orders requires the Exchange to implement a systems change that will be implemented by early September 2006. Therefore, this part of the proposed rule change will not be operative until such systems change is implemented.<sup>3</sup> The text of the proposed rule change is as follows, with deletions in [brackets] and additions in *italics*.

#### Rule 714. Automatic Execution of [Public Customer] Orders

(a) [Public Customer Orders to buy or sell options contracts on the Exchange] *Incoming orders that are executable against orders and quotes in the System will be executed automatically by the System; provided that such orders will not be automatically executed by the System at prices inferior to the best bid or offer on another national securities exchange, as those best prices are identified in the System. Public Customer Orders that are not automatically executed will be handled by the Primary Market Maker pursuant to Rule 803(c). Non-Customer Orders that are not automatically executed will be rejected automatically by the System.*

(b) Paragraph (a) shall not apply [to fill-or-kill orders or] in circumstances where a “fast market” in the options series has been declared on the Exchange, or where a “fast market” in the options series has been declared in other markets or where quotations in other markets are otherwise not firm.

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#### 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 Exchange 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 Exchange 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

Currently, ISE Rule 714 provides that Public Customer Orders<sup>4</sup> will not be automatically executed at a price that is inferior to the best bid or offer on another national securities exchange (“NBBO”). The Exchange proposes to amend ISE Rule 714 to clarify the language and to provide that Non-

Customer Orders<sup>5</sup> also will not be automatically executed at prices that are inferior to the NBBO. Under the proposed rule change, ISE Rule 714 will also be amended to specify that Public Customer orders that are not automatically executed because there is a better price on another market will be handled by the Primary Market Maker,<sup>6</sup> while Non-Customer Orders that are not automatically executed will be rejected. Finally, the Exchange proposed to delete the provision stating that orders marked “fill-or-kill” can automatically be executed at prices that are inferior to the NBBO. With the adoption of the intermarket linkage rules, the Exchange modified its system so that a “fill-or-kill” condition would not cause orders to be automatically executed if there were a better price in another market, and this proposed rule change conforms the language of ISE Rule 714 to the Exchange’s current practice.

###### 2. Statutory Basis

The basis under the Act of this proposed rule change is the requirement under section 6(b)(5) of the Act<sup>7</sup> 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 perfect the mechanism of 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 prevent Non-Customer Orders from automatically trading at prices that are inferior to the NBBO.

##### 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.

<sup>5</sup> Under ISE Rule 100(a)(22) and (23), a “Non-Customer” is any person or entity that is a broker or dealer in securities, and a “Non-Customer Order” is an order for the account of a broker or dealer.

<sup>6</sup> ISE Rule 803(c) provides that a Primary Market Maker must address Public Customer Orders that are not automatically executed because there is a displayed bid or offer on another exchange trading the same options contract that is better than the best bid or offer on the Exchange, either (i) by executing a Public Customer Order at a price that matches the best price displayed or (ii) by sending to any other exchange(s) displaying the bet price a Linkage Order(s) according to the rules contained in chapter 19 or (iii) by executing a Public Customer Order at a price one minimum quoting increment inferior to the NBBO and contemporaneously sending a Linkage Order(s) to each exchange(s) disseminating the NBBO according to the Rules contained in Chapter 19.

<sup>7</sup> 15 U.S.C. 78f(b)(5).

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> The Exchange will issue a Regulatory Information Circular notifying members at least five days prior to the operative date of the rule change. The Exchange clarified that it intends that the operative date, rather than the effective date, will be delayed until the required systems change can be implemented. The Exchange further clarified that the delayed operative date applies only to the handling of Non-Customer Orders. These clarifications have been reflected in the preceding text pursuant to the request of the Exchange. E-mail exchange between Kathy Simmons, Deputy General Counsel, Exchange, and Kim Allen, Special Counsel, Commission, Division of Market Regulation (“Division”), on June 6, 2006 (“E-mail exchange”).

<sup>4</sup> Under ISE Rule 100(a)(32) and (33), a “Public Customer” is any person that is not a broker or dealer in securities, and a “Public Customer Order” is an order for the account of a Public Customer. At the Exchange’s request, the Division deleted “or entity” from the preceding sentence, as “entity” isn’t referred to in the Exchange’s definition of “Public Customer.” E-Mail exchange.

*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 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](mailto:rule-comments@sec.gov). Please include File Number SR-ISE-2006-27 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 Number SR-ISE-2006-27. 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-2006-27 and should be submitted on or before July 5, 2006.

For the Commission, by the Division of Market Regulation, pursuant to delegated authority.<sup>8</sup>

**Jill M. Peterson,**

*Assistant Secretary.*

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**BILLING CODE 8010-01-M**

**SECURITIES AND EXCHANGE COMMISSION**

[Release No. 34-53948; File No. SR-ISE-2006-14]

**Self-Regulatory Organizations; International Securities Exchange, Inc.; Notice of Filing of Proposed Rule Change and Amendment No. 1 Thereto Relating to ISE Rule 720**

June 6, 2006.

Pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on March 22, 2006, the International Securities Exchange, Inc. ("ISE" or "Exchange") filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the Exchange. On May 18, 2006, the ISE submitted Amendment No. 1 to the proposed rule change.<sup>3</sup> The Commission is publishing

<sup>8</sup> 17 CFR 200.30-3(a)(12).

<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> In Amendment No. 1, the Exchange amended proposed new supplementary Material .08 to ISE Rule 720 to state that unless all parties to a trade agree otherwise, ISE Market Control may nullify a trade if all parties to a trade fail to receive a trade execution report due to a verifiable system outage. Amendment No. 1 also clarified that the proposed rule change operates under the assumption that a trade has taken place, but due to a system outage, the parties to the trade never received a trade execution report and thus were unaware of the trade having taken place.

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 ISE proposes to amend ISE Rule 720 ("Obvious Error Rule"). The text of the proposed rule change is below. Proposed new language is in *italics*. Proposed deletions are in [brackets].

**Rule 720. Obvious Errors**

The Exchange shall either bust a transaction or adjust the execution price of a transaction that results from an Obvious Error as provided in this Rule. *In limited circumstances, the Exchange may nullify transactions, pursuant to Supplementary Material .08 below.*

(a)-(c) No change.

(d) [(e)] Obvious Error Panel.

(1)-(4) No change.

**Supplementary Material to Rule 720**

.01-.07 No change.

.08 *Unless all parties to a trade agree otherwise, Market Control may nullify a trade if all parties to a trade fail to receive a trade execution report due to a verifiable system outage.*

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**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 Exchange 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 Exchange 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 the proposed rule change is to amend ISE Rule 720 to expand its application. Specifically, ISE proposes to expand its Obvious Error Rule to provide the Exchange with the ability, in limited circumstances, to nullify a transaction when all parties to a trade do not receive a trade execution report<sup>4</sup> due to a system outage. The

<sup>4</sup> A trade execution report is an ISE system message sent to all parties to a trade to inform them