

the proposed primary peg order type, and that it is hardcoded conditionality based on pre-determined, objective factors.³² In addition, as the Commission observed in the IEX Form 1 Approval, other exchanges offer both discretion and pegging functionalities, including the combination of both of those functionalities in a single order type, and thus an order type that offers both discretion and pegging features is not novel.³³

Importantly, the Commission notes that the Exchange's amended primary peg order type would remain a non-displayed order type, like all of the Exchange's pegged order types, including the discretionary peg order type.³⁴ Thus, the proposed amended primary peg order type, with its added discretionary and crumbling quote determination functionalities, should not impact the Exchange's dissemination of a protected quotation, which must be displayed,³⁵ or market participants' ability to execute against the Exchange's protection quotation, and does not appear otherwise designed to impede the mechanism of a free and open market. Accordingly, the Commission believes that the proposed amendments to the Exchange's primary peg order type are consistent with the Act and, in particular, the Section 6(b)(5) requirement that a national securities exchange's rules be designed to promote just and equitable principles of trade, remove impediments to and perfect the mechanism of a free and open market and a national market system, and protect investors and the public interest.³⁶

The Commission also believes that the proposed amendments to the Exchange's price sliding process for primary peg orders and discretionary peg orders in locked or crossed markets are consistent with the Act. The Exchange has stated that its existing approach to price sliding for such orders

³² See proposed Rule 11.190(b)(8) and Rule 11.190(g); see also IEX Form 1 Approval, *supra* note 28, at 41153.

³³ See IEX Form 1 Approval, *supra* note 28, at 41153; see also, e.g., Nasdaq Rule 4703(g); NYSE Arca Equities Rule 7.31P(h)(3). In addition, as the Exchange has noted, primary pegged orders on other exchanges may be pegged to prices less aggressive than the near-side primary quote. See Notice, *supra* note 3, at 90036–37; see also, e.g., BZX Rule 11.9(c)(8)(A).

³⁴ See Rules 11.190(a)(3) and (b)(8)(H). The Commission also notes that primary pegged orders on other exchanges may be non-displayed. See, e.g., BZX Rule 11.9(c)(8)(A).

³⁵ See 17 CFR 242.600(b)(57) and (58).

³⁶ The Commission notes that the Exchange would be required to submit a proposed rule change pursuant to Section 19(b) of the Act prior to implementing any changes to the proposed primary peg order type.

in locked or crossed markets is unnecessarily complicated, without any material benefit, and that the proposed amendments to the approach would remove the variability of a primary peg order's booked price in locked or crossed market situations, and make the Exchange's rules more clear and transparent.³⁷ The Commission believes these changes should help lessen the complexity in the Exchange's price sliding rules, which may reduce the potential for investor confusion as to how primary peg and discretionary peg orders would price slide in locked or crossed markets, and thereby help protect investors and the public interest consistent with Section 6(b)(5) of the Act. In addition, the proposed amendments appear to be consistent with the requirements of Rule 610(d) of Regulation NMS which, among other things, requires that the rules of a national securities exchange be reasonably designed to assure the reconciliation of locked or crossed quotations in an NMS stock.³⁸

Lastly, the Commission believes that the Exchange's proposed technical change to conform certain terminology in its proposed rules is intended to enhance the clarity of its rules, which should reduce the potential for investor confusion, and thereby help protect investors and the public interest consistent with Section 6(b)(5) of the Act.

IV. Conclusion

It is therefore ordered, pursuant to Section 19(b)(2) of the Act,³⁹ that the proposed rule change (SR–IEX–2016–18) be and hereby is approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.⁴⁰

Eduardo A. Aleman,

Assistant Secretary.

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SECURITIES AND EXCHANGE COMMISSION

[Release No. 34–80225; File No. SR–ISE–2017–02]

Self-Regulatory Organizations; International Securities Exchange, LLC; Order Approving Proposed Rule Change, as Modified by Amendment No. 1, To Amend the Exchange Opening Process

March 13, 2017.

I. Introduction

On January 13, 2017, 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 (“Act”),¹ and Rule 19b–4 thereunder,² a proposed rule change to amend the Exchange's opening process. The proposed rule change was published for comment in the **Federal Register** on January 27, 2017.³ On March 3, 2017, the Exchange filed Amendment No. 1 to the proposed rule change.⁴ The Commission received no comment letters on the proposed rule change. This order approves the proposed rule change, as modified by Amendment No. 1.

II. Description of the Proposal, as Modified by Amendment No. 1

The Exchange proposes to delete the entirety of current ISE Rule 701 and replace the current Exchange opening process with an opening process reflected in proposed ISE Rules 701 and 715(t).⁵ The new opening process is

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b–4.

³ See Securities Exchange Act Release No. 79887 (February 2, 2017), 82 FR 9090 (“Notice”).

⁴ In Amendment No. 1, the Exchange provided clarifying details to its proposal, including: (i) Expanding its proposed definition of “Quality Opening Market”; (ii) clarifying that only Public Customer interest is routable during the Opening Process; (iii) clarifying that when routing orders during the Opening Process the Exchange will do so based on price/time priority of routable interest; and (iv) clarifying that the proposed opening rule will not provide for after-hours trading rotations. The Exchange also made technical corrections and revisions to the proposed rule text for readability and consistency. Amendment No. 1 amends and replaces the original filing in its entirety. Because Amendment No. 1 does not materially alter the substance of the proposed rule change or raise unique or novel regulatory issues, it is not subject to notice and comment. The amendment is available at: <https://www.sec.gov/comments/sr-ise-2017-02/ise201702.htm>.

⁵ The Exchange represents that this proposed rule change is being made in connection with a technology migration to a Nasdaq, Inc. (“Nasdaq”) supported architecture called INET which is utilized on The NASDAQ Options Market LLC,

Continued

³⁷ See Notice, 81 FR at 90037.

³⁸ See 17 CFR 242.610(d).

³⁹ 15 U.S.C. 78s(b)(2).

⁴⁰ 17 CFR 200.30–3(a)(12).

similar to the process used by Phlx,⁶ as well as the new opening process recently adopted by ISE Gemini, LLC (“ISE Gemini”).⁷ The Exchange’s current and proposed opening processes are described below.⁸

A. Current Exchange Opening Process

Currently, a Primary Market Maker (“PMM”) on ISE initiates the “trading rotation” in a specified options class.⁹ The Exchange may direct that one or more trading rotations be employed on any business day to aid in producing a fair and orderly market.¹⁰ For each rotation, except as the Exchange may direct, rotations are conducted in the order and manner the PMM determines to be appropriate under the circumstances.¹¹ The PMM, with the approval of the Exchange, has the authority to determine the rotation order and manner or deviate from the rotation procedures.¹² Such authority may be exercised before and during a trading rotation.¹³ Additionally, two or more trading rotations may be employed simultaneously, if the PMM, with the approval of the Exchange, so determines.¹⁴

Pursuant to ISE Rule 701(b), the opening rotation for each class of options is held promptly following the opening of the market for the underlying security.¹⁵ In the event the underlying security has not opened within a reasonable time after 9:30 a.m. Eastern

Time, the PMM reports the delay to the Exchange and an inquiry is made to determine the cause of the delay.¹⁶ The opening rotation for the affected options series is then delayed until the market for the underlying security has opened, unless the Exchange determines that the interests of a fair and orderly market are best served by opening trading in the options contracts.¹⁷

Currently, in connection with a trading rotation, ISE Rule 701(c) specifies how transactions may be effected in a class of options after the end of normal trading hours. A trading rotation may be employed whenever the Exchange concludes that such action is appropriate in the interests of a fair and orderly market.¹⁸ The decisions to employ a trading rotation in non-expiring options are disseminated prior to the commencement of such rotation and, in general, the Exchange will commence no more than one trading rotation after the normal close of trading.¹⁹ If a trading rotation is in progress and the Exchange determines that a final trading rotation is needed to assure a fair and orderly market close, the rotation in progress will be halted and a final rotation will begin as promptly as possible.²⁰ Finally, any trading rotation in non-expiring options conducted after the normal close of trading may not begin until five minutes after news of such rotation is disseminated by the Exchange.²¹

B. Proposed New Opening Process

1. Opening Sweep

At the outset, the Exchange proposes to adopt a new order type, “Opening Sweep”, for the new opening process.²² Proposed Rule 701(b)(1)(i) states that a Market Maker assigned to a particular option may only submit an Opening Sweep if, at the time of entry, that Market Maker has already submitted

and maintains a Valid Width Quote.²³ Opening Sweeps may be entered at any price with a minimum price variation applicable to the affected series, on either side of the market, at single or multiple price level(s), and may be cancelled and re-entered.²⁴ A single Market Maker may enter multiple Opening Sweeps, with each Opening Sweep at a different price level.²⁵ If a Market Maker submits multiple Opening Sweeps, the system will consider only the most recent Opening Sweep at each price level submitted by such Market Maker in determining the Opening Price (described below).²⁶ Unexecuted Opening Sweeps will be cancelled once the affected series is open.²⁷

2. Interest Included in the Opening Process

The first part of the Opening Process determines what constitutes “eligible interest”. The Exchange proposes that eligible interest during the Opening Process²⁸ will include Valid Width Quotes,²⁹ Opening Sweeps, and orders.³⁰ Quotes, other than Valid Width Quotes, will not be included in the Opening Process.³¹ All-or-None Orders that can be satisfied, and the displayed and non-displayed portions of Reserve Orders, are considered for execution and in determining the Opening Price throughout the Opening Process.³² The system will aggregate the size of all eligible interest for a particular participant category at a particular price level for trade allocation purposes pursuant to Rule 713.³³ Only Public Customer interest is routable during the Opening Process.³⁴

Market Maker Valid Width Quotes and Opening Sweeps received starting at 9:25 a.m. Eastern Time, or 7:25 a.m. Eastern Time for U.S. dollar-settled

NASDAQ PHLX LLC (“Phlx”) and NASDAQ BX, Inc. *See id.*

⁶ *See* Phlx Rule 1017. *See also* Securities Exchange Act Release No. 79274 (November 9, 2016), 81 FR 80694 (November 16, 2016) (SR–Phlx–2016–79).

⁷ *See* ISE Gemini Rules 701 and 715(t). *See also* Securities Exchange Act Release No. 10952 (February 10, 2017), 82 FR 10952 (February 16, 2017) (SR–ISEGemini–2016–18).

⁸ In connection with the new opening process, the Exchange proposes to adopt a new “Definitions” section in proposed Rule 701(a), similar to Phlx Rule 1017(a), to define several terms that are used throughout the opening rule. Proposed Rule 701(a) will define: ABBO, “market for the underlying security,” Opening Price, Opening Process, Potential Opening Price, Pre-Market BBO, Quality Opening Market, Valid Width Quote, and Zero Bid Market. For definitions of these terms, *see* Notice *supra* note 3 at 9091.

⁹ *See* ISE Rule 701(a).

¹⁰ *See* ISE Rule 701(a)(1).

¹¹ *See* ISE Rule 701(a)(2).

¹² *See* ISE Rule 701(a)(3).

¹³ *See* ISE Rule 701(a)(3).

¹⁴ *See* ISE Rule 701(a)(4).

¹⁵ *See* ISE Rule 701(b)(2). For purposes of ISE Rule 701(b)(2), the “market for the underlying security” is either the primary listing market, the primary volume market (defined as the market with the most liquidity in that underlying security for the previous two calendar months), or the first market to open the underlying security, as determined by the Exchange on an issue-by-issue basis and announced to the membership on the Exchange’s Web site. *See id.*

¹⁶ *See* ISE Rule 701(b)(3).

¹⁷ *See id.* Additionally, the Exchange may delay the commencement of the opening rotation in any class of options in the interests of a fair and orderly market. *See* ISE Rule 701(b)(4).

¹⁸ *See* ISE Rule 701(c)(1). The factors that may be considered include, but are not limited to, whether there has been a recent opening or reopening of trading in the underlying security, a declaration of a “fast market” pursuant to ISE Rule 704, or a need for a rotation in connection with expiring individual stock options or index options, an end of the year rotation, or the restart of a rotation which is already in progress. *See id.*

¹⁹ *See* ISE Rule 701(c)(2).

²⁰ *See* ISE Rule 701(c)(3).

²¹ *See* ISE Rule 701(c)(4).

²² The Exchange proposes to define an “Opening Sweep” as a Market Maker order submitted for execution against eligible interest in the system during the Opening Process pursuant to proposed Rule 701(b)(1). *See* proposed Rule 715(t).

²³ All Opening Sweeps in the affected series entered by a Market Maker will be cancelled immediately if that Market Maker fails to maintain a continuous quote with a Valid Width Quote in the affected series. *See* proposed Rule 701(b)(1)(i).

²⁴ *See* proposed Rule 701(b)(1)(ii).

²⁵ *See id.*

²⁶ *See id.* The Exchange proposes to define “Opening Price” by cross-referencing proposed Rule 701(h) and (j). *See* proposed Rule 701(a)(3).

²⁷ *See id.*

²⁸ The Exchange proposes to define “Opening Process” by cross-referencing proposed Rule 701(c). *See* proposed Rule 701(a)(4).

²⁹ The Exchange proposes to define “Valid Width Quote” as a two-sided electronic quotation submitted by a Market Maker that consists of a bid/ask differential that is compliant with ISE Rule 803(b)(4). *See* proposed Rule 701(a)(8).

³⁰ *See* proposed Rule 701(b).

³¹ *See id.*

³² *See id.*

³³ *See* proposed Rule 701(b)(2).

³⁴ *See* proposed Rule 701(b).

foreign currency options, are included in the Opening Process.³⁵ Orders entered at any time before an option series opens are included in the Opening Process.³⁶

3. Opening Process and Reopening After a Trading Halt

The Exchange proposes that the Opening Process for an option series will be conducted pursuant to proposed Rules 701(f)–(j) on or after 9:30 a.m. Eastern Time, or on or after 7:30 a.m. Eastern Time for U.S. dollar-settled foreign currency options, if: (1) The ABBO,³⁷ if any, is not crossed; and (2) the system has received, within two minutes (or such shorter time as determined by the Exchange and disseminated to membership on the Exchange's Web site) of the opening trade or quote on the market for the underlying security³⁸ in the case of equity options, or the receipt of the opening price in the underlying index in the case of index options, or market opening for the underlying security in the case of U.S. dollar-settled foreign currency options, any of the following: (i) A PMM's Valid Width Quote; (ii) the Valid Width Quotes of at least two Competitive Market Makers ("CMM"); or (iii) if no PMM's Valid Width Quote nor two CMMs' Valid Width Quotes within such timeframe, one CMM's Valid Width Quote.³⁹

For all options, the underlying security, including indexes, must be open on the primary market for a certain time period as determined by the Exchange for the Opening Process to commence.⁴⁰ The Opening Process will

stop and an option series will not open if the ABBO becomes crossed or a Valid Width Quote(s) pursuant to proposed Rule 701(c)(1) is no longer present.⁴¹ Once each of these conditions no longer exists, the Opening Process in the affected option series will recommence.⁴² The Exchange would wait for the ABBO to become uncrossed before initiating the Opening Process to ensure that there is stability in the marketplace as the Exchange determines the Opening Price.⁴³

Proposed Rule 701(c)(3) states that the PMM assigned to a particular equity option must enter a Valid Width Quote not later than one minute following the dissemination of a quote or trade by the market for the underlying security or, in the case of index options, following the receipt of the opening price in the underlying index. The PMM assigned to a particular U.S. dollar-settled foreign currency option must enter a Valid Width Quote not later than one minute after the announced market opening.⁴⁴ Furthermore, a CMM that submits a quote pursuant to proposed Rule 701 in any option series when the PMM's quote has not been submitted will be required to submit continuous, two-sided quotes in such option series until such time the PMM submits a quote, after which the Market Maker that submitted such quote will be obligated to submit quotations pursuant to ISE Rule 804(e).⁴⁵

Proposed Rule 701(d) states that the procedure described in proposed Rule 701 will be used to reopen an options series after a trading halt.⁴⁶ If there is a trading halt or pause in the underlying security, the Opening Process will recommence irrespective of the specific times listed in proposed Rule 701(c)(1).⁴⁷ Unlike the current ISE opening rule, the proposed new opening process does not provide for after-hours trading rotations.⁴⁸

4. Opening With a BBO (No Trade)

Under proposed Rule 701(e), the Exchange will first see if the option series will open for trading with a BBO. If there are no opening quotes or orders that lock or cross each other and no

routable orders locking or crossing the ABBO, the system will open with an opening quote by disseminating the Exchange's best bid and offer among quotes and orders ("BBO"), unless all three of the following conditions exist: (i) A Zero Bid Market;⁴⁹ (ii) no ABBO; and (iii) no Quality Opening Market.⁵⁰

A "Quality Opening Market" is a bid/ask differential applicable to the best bid and offer from all Valid Width Quotes defined in a table to be determined by the Exchange and published on the Exchange's Web site.⁵¹ The calculation of Quality Opening Market is based on the best bid and offer of Valid Width Quotes. The differential between the best bid and offer are compared to reach this determination. The allowable differential, as determined by the Exchange, takes into account the type of security (for example, Penny Pilot versus non-Penny Pilot issue), volatility, option premium, and liquidity. The Quality Opening Market differential is intended to ensure the price at which the Exchange opens reflects current market conditions.

If all three of the conditions described above exist, the Exchange will calculate an Opening Quote Range ("OQR") pursuant to proposed Rule 701(i) (described below) and conduct the Price Discovery Mechanism ("PDM") pursuant to proposed Rule 701(j) (described below).⁵² The Exchange believes that when these conditions exist, further price discovery is warranted.⁵³

5. Opening With a Trade

If there are Valid Width Quotes or orders that lock or cross each other, the system will try to open with a trade. Proposed Rule 701(h) provides that the Exchange will open the option series with a trade of Exchange interest only at the Opening Price, if any of the following conditions occur: (1) The Potential Opening Price (described below) is at or within the best of the highest bid and the lowest offer among Valid Width Quotes ("Pre-Market BBO")⁵⁴ and the ABBO; (2) the Potential Opening Price is at or within the non-zero bid ABBO if the Pre-Market BBO is crossed; or (3) where there is no ABBO, the Potential Opening

³⁵ See proposed Rule 701(c).

³⁶ See *id.*

³⁷ The Exchange proposes to define "ABBO" as the Away Best Bid or Offer. See proposed Rule 701(a)(1). The ABBO does not include ISE's market. See Notice, *supra* note 3, at 9091.

³⁸ The Exchange proposes to define "market for the underlying security" as either the primary listing market or the primary volume market (defined as the market with the most liquidity in that underlying security for the previous two calendar months), as determined by the Exchange by underlying and announced to the membership on the Exchange's Web site. See proposed Rule 701(a)(2).

³⁹ See proposed Rule 701(c)(1). The Exchange represents that it anticipates initially setting the timeframe during which a PMM's Valid Width quote or the presence of at least two CMMs' Valid Width Quotes will initiate the Opening Process at 30 seconds. See Notice, *supra* note 3, at 9092–93 n.18. The Exchange represents that it will provide notice of the initial setting to Members and provide notice if the Exchange determines to reduce the timeframe. See *id.*

⁴⁰ See proposed Rule 701(c)(2). Proposed Rule 701(c)(2) stipulates that this time period will be no less than 100 milliseconds and no more than 5 seconds. The Exchange represents that it will set the timer initially at 100 milliseconds and will issue a notice to provide the initial setting and will

thereafter issue a notice if it were to change the timing. See Notice, *supra* note 3, at 9092. If the Exchange were to select a time not between 100 milliseconds and 5 seconds, it will be required to file a rule proposal with the Commission. See *id.*

⁴¹ See proposed Rule 701(c)(5).

⁴² See *id.*

⁴³ See Notice, *supra* note 3, at 9093.

⁴⁴ See proposed Rule 701(c)(3).

⁴⁵ See proposed Rule 701(c)(4).

⁴⁶ See proposed Rule 701(d).

⁴⁷ See *id.*

⁴⁸ See Amendment No. 1, *supra* note 4.

⁴⁹ The Exchange proposes to define the term "Zero Bid Market" as where the best bid for an options series is zero. See proposed Rule 701(a)(9).

⁵⁰ See proposed Rule 701(e).

⁵¹ See proposed Rule 701(a)(7).

⁵² See *id.*

⁵³ See Notice, *supra* note 3, at 9093.

⁵⁴ See proposed Rule 701(a)(6). The Exchange states that the Pre-Market BBO would not include orders. See Amendment No. 1, *supra* note 4.

Price is at or within the Pre-Market BBO which is also a Quality Opening Market.

To undertake the above described process, the Exchange will calculate the Potential Opening Price by taking into consideration all Valid Width Quotes and orders (including Opening Sweeps and displayed and non-displayed portions of Reserve Orders), except All-or-None Orders that cannot be satisfied, and identify the price at which the maximum number of contracts can trade (“maximum quantity criterion”).⁵⁵

Under proposed Rule 701(g)(1), when two or more Potential Opening Prices would satisfy the maximum quantity criterion and leave no contracts unexecuted, the system would take the highest and lowest of those prices and takes the mid-point. If such mid-point cannot be expressed as a permitted minimum price variation, the mid-point will be rounded to the minimum price variation that is closest to the closing price for the affected series from the immediately prior trading session. If there is no closing price from the immediately prior trading session, the system will round up to the minimum price variation to determine the Opening Price.⁵⁶ Further, if any value used for the mid-point calculation would cross either the Pre-Market BBO, or the ABBO, then, for the purposes of calculating the mid-point, the Exchange will use the better of the Pre-Market BBO or ABBO as a boundary price and will open the option series for trading with an execution at the resulting Potential Opening Price.⁵⁷ The Exchange states that the purpose of these boundaries is to help ensure that the Potential Opening Price is reasonable and does not trade through other markets.⁵⁸

If two or more Potential Opening Prices for the affected series would satisfy the maximum quantity criterion and leave contracts unexecuted, the Opening Price will be either the lowest executable bid or highest executable offer of the largest sized side.⁵⁹ This is designed to base the Potential Opening Price on the maximum quantity of contracts that are executable.⁶⁰ Furthermore, the Potential Opening Price calculation will be bounded by the

better away market price that cannot be satisfied with the Exchange routable interest.⁶¹ According to the Exchange, this would ensure that the Exchange would not open with a trade that would trade through another market.⁶²

6. Price Discovery Mechanism

If the Exchange has not opened with a BBO or trade pursuant to proposed Rule 701(e) or (h), the Exchange will conduct a PDM pursuant to proposed Rule 701(j) to determine the Opening Price. According to the Exchange, the purpose of the PDM is to satisfy the maximum number of contracts possible by applying wider price boundaries and seeking additional liquidity.⁶³

Before conducting a PDM, however, the Exchange will calculate the OQR under proposed Rule 701(i). The OQR, which is used during PDM, is an additional boundary designed to limit the Opening Price to a reasonable price and reduce the potential for erroneous trades during the Opening Process.⁶⁴

To determine the minimum value for the OQR, an amount, as defined in a table to be determined by the Exchange, will be subtracted from the highest quote bid among Valid Width Quotes on the Exchange and on the away market(s), if any, except as provided in proposed Rule 701(i)(3) and (4).⁶⁵ To determine the maximum value for the OQR, an amount, as defined in a table to be determined by the Exchange, will be added to the lowest quote offer among Valid Width Quotes on the Exchange and on the away market(s), if any, except as provided in proposed Rule 701(i)(3) and (4).⁶⁶ If one or more away markets are collectively disseminating a BBO that is not crossed, however, and there are Valid Width Quotes on the Exchange that are executable against each other or that are executable against the ABBO, then the minimum value of the OQR will be the highest away bid and the maximum value will be the lowest away offer.⁶⁷ Additionally, if there are Valid Width Quotes on the Exchange that are executable against each other, and there is no away market disseminating a BBO in the affected option series, the minimum value of the OQR will be the lowest quote bid among Valid Width

Quotes on the Exchange and the maximum value will be the highest quote offer among Valid Width Quotes on the Exchange.⁶⁸

The Exchange will use the OQR to help calculate the Opening Price. For example, if there is more than one Potential Opening Price possible where no contracts would be left unexecuted, any price used for the mid-point calculation, pursuant to proposed Rule 701(g)(1), that is outside of the OQR will be restricted to the OQR on that side of the market.⁶⁹ Other instances that implicate the OQR are described below.

During PDM, the Exchange will take into consideration the away market prices in calculating the Potential Opening Price. For example, if there is more than one Potential Opening Price possible where no contracts would be left unexecuted and the price used for the mid-point calculation is an away market price, pursuant to proposed Rule 701(g)(3), the system will use the away market price as the Potential Opening Price.⁷⁰ Moreover, proposed Rule 701(i)(7) provides that if the Exchange determines that non-routable interest can execute the maximum number of contracts against Exchange interest, after routable interest has been determined by the system to satisfy the away market, then the Potential Opening Price will be the price at which such maximum number of contracts can execute—excluding the interests to be routed to an away market.⁷¹

After the OQR is calculated, the system will broadcast an Imbalance Message for the affected series⁷² to attract additional liquidity and begin an “Imbalance Timer,” not to exceed three seconds.⁷³ The Imbalance Timer will be for the same number of seconds for all options traded on the Exchange, and each Imbalance Message will be subject to an Imbalance Timer.⁷⁴ The Exchange may have up to four Imbalance Messages which each run its own Imbalance Timer pursuant to the PDM process.⁷⁵

⁶⁸ See proposed Rule 701(i)(4).

⁶⁹ See proposed Rule 701(i)(5).

⁷⁰ See proposed Rule 701(i)(6).

⁷¹ The system will route Public Customer interest in price/time priority to satisfy the away market. See proposed Rule 701(i)(7).

⁷² Imbalance Message includes the symbol, side of the imbalance (unmatched contracts), size of matched contracts, size of the imbalance, and Potential Opening Price bounded by the Pre-Market BBO.

⁷³ See proposed Rule 701(j)(1). The Exchange represents that it will issue a notice to provide the initial setting of the Imbalance Timer and would thereafter issue a notice if it were to change the timing. See Notice, *supra* note 3, at 9095 n.32.

⁷⁴ See proposed Rule 701(j)(1).

⁷⁵ See Notice, *supra* note 3, at 9100.

⁵⁵ See proposed Rule 701(g).

⁵⁶ See proposed Rule 701(g)(1).

⁵⁷ If the Exchange has not yet opened and the above conditions are not met, an Opening Quote Range (as described below) will be calculated pursuant to proposed Rule 701(i), and thereafter, the Price Discovery Mechanism described in proposed Rule 701(j) below will commence. See proposed Rule 701(h)(3)(i)(B)(II).

⁵⁸ See Notice, *supra* note 3, at 9094.

⁵⁹ See proposed Rule 701(g)(2).

⁶⁰ See Notice, *supra* note 3, at 9094.

⁶¹ See proposed Rule 701(g)(3).

⁶² See Notice, *supra* note 3, at 9094.

⁶³ See Notice, *supra* note 3, at 9095.

⁶⁴ See Notice, *supra* note 3, at 9094.

⁶⁵ See proposed Rule 701(i)(1).

⁶⁶ See proposed Rule 701(i)(2).

⁶⁷ See proposed Rule 701(i)(3). Proposed Rule 701(i)(3) further notes that the Opening Process will stop and an options series will not open if the ABBO becomes crossed pursuant to proposed Rule 701(c)(5).

Proposed Rule 701(j)(2), states that any new interest received by the system will update the Potential Opening Price. If during or at the end of the Imbalance Timer, the Opening Price is at or within the OQR, the Imbalance Timer will end and the system will open with a trade at the Opening Price if the executions consist of Exchange interest only without trading through the ABBO and without trading through the limit price(s) of interest within the OQR, which is unable to be fully executed at the Opening Price. If no new interest comes in during the Imbalance Timer and the Potential Opening Price is at or within the OQR and does not trade through the ABBO, the Exchange will open with a trade at the end of the Imbalance Timer at the Potential Opening Price.

If the option series has not opened pursuant to proposed Rule 701(j)(2) described above, the system will concurrently: (i) Send a second Imbalance Message with a Potential Opening Price that is bounded by the OQR (and would not trade through the limit price(s) of interest within the OQR which is unable to be fully executed at the Opening Price) and includes away market volume in the size of the imbalance to participants; and (ii) initiate a Route Timer, not to exceed one second.⁷⁶ As proposed, the Route Timer will operate as a pause before an order is routed to an away market. The Exchange states that the Route Timer is intended to give participants an opportunity to respond to an Imbalance Message before any opening interest is routed to away markets and thereby maximize trading on the Exchange.⁷⁷ If during the Route Timer, interest is received by the system which would allow the Opening Price to be within the OQR without trading through away markets and without trading through the limit price(s) of interest within the OQR which is unable to be fully executed at the Opening Price, the system will open with trades at the Opening Price, and the Route Timer will simultaneously end. The system will monitor quotes received during the Route Timer and make ongoing changes to the OQR and Potential Opening Price to reflect them.

Proposed Rule 701(j)(3)(iii) provides that, if no trade occurs pursuant to proposed ISE Rule 701(j)(3)(ii), when the Route Timer expires, if the Potential Opening Price is within the OQR (and would not trade through the limit price(s) of interest within the OQR that is unable to be fully executed at the Opening Price), the system will

determine if the total number of contracts displayed at better prices than the Exchange's Potential Opening Price on away markets ("better priced away contracts") would satisfy the number of marketable contracts available on the Exchange. The Exchange will then open the option series by routing and/or trading on the Exchange, pursuant to proposed Rule 701(j)(3)(iii) paragraphs (A) through (C).

Proposed Rule 701(j)(3)(iii)(A) provides that, if the total number of better priced away contracts would satisfy the number of marketable contracts available on the Exchange on either the buy or sell side, the system will route all marketable contracts on the Exchange to such better priced away markets as an Intermarket Sweep Order ("ISO") designated as Immediate-or-Cancel ("IOC") order(s) and determine an opening BBO that reflects the interest remaining on the Exchange. The system will price any contracts routed to away markets at the Exchange's Opening Price. The Exchange states that routing away at the Exchange's Opening Price is intended to achieve the best possible price available at the time the order is received by the away market.⁷⁸

Proposed Rule 701(j)(3)(iii)(B) provides that, if the total number of better priced away contracts would not satisfy the number of marketable contracts on the Exchange, the system will determine how many contracts it has available at the Opening Price. If the total number of better priced away contracts plus the number of contracts available at the Exchange's Opening Price would satisfy the number of marketable contracts on the Exchange on either the buy or sell side, the system will contemporaneously route, based on price/time priority of routable interest, a number of contracts that will satisfy such away market interest, and trade available contracts on the Exchange at the Opening Price. The system will price any contracts routed to away markets at the better of the Opening Price or the order's limit price pursuant to proposed Rule 701(j)(vi)(C)(3)(ii). The Exchange states that this proposed rule is designed to maximize execution of interest on the Exchange or away markets.⁷⁹

Proposed Rule 701(j)(3)(iii)(C) provides that, if the total number of better priced away contracts plus the number of contracts available at the Opening Price plus the contracts available at away markets at the Exchange's Opening Price would satisfy the number of marketable contracts on

the Exchange, either the buy or sell side, the system will contemporaneously route, based on price/time priority, a number of contracts that will satisfy such away market interest (pricing any contracts routed to away markets at the better of the Opening Price or the order's limit price), trade available contracts on the Exchange at the Opening Price, and route a number of contracts that will satisfy interest at other markets at prices equal to the Opening Price. The Exchange states that routing at the better of the Opening Price or the order's limit price is intended to achieve the best possible price available at the time the order is received by the away market and that routing at the order's limit price ensures that the order's limit price is not violated.⁸⁰

Proposed Rule 701(j)(4) provides that the system may send up to two additional Imbalance Messages⁸¹ (which may occur while the Route Timer is operating) bounded by the OQR and reflecting away market interest in the volume. After the Route Timer has expired, the processes in proposed Rule 701(j)(3) will repeat (except no new Route Timer will be initiated).

7. Forced Opening

Proposed Rule 701(j)(5) describes the process that occurs if the steps described above have not resulted in an opening of the options series. After all additional Imbalance Messages have been broadcast pursuant to proposed Rule 701(j)(4), the system will open the series by executing as many contracts as possible by: (i) Routing to away markets at prices better than the Opening Price for their disseminated size; (ii) trading available contracts on the Exchange at the Opening Price bounded by the OQR (without trading through the limit price(s) of interest within the OQR which is unable to be fully executed at the Opening Price); and (iii) routing contracts to away markets at prices equal to the Opening Price at their disseminated size. In forced opening, the system will price any contracts routed to away markets at the better of the Opening Price or the order's limit price. Any unexecuted contracts from the imbalance not traded or routed will be cancelled back to the entering participant if they remain unexecuted and priced through the Opening Price. Otherwise such orders will remain in the order book.

⁸⁰ See Notice, *supra* note 3, at 9100–01.

⁸¹ The Exchange notes that the first two Imbalance Messages always occur if there is interest which will route to an away market. See Notice, *supra* note 3, at 9096 n.37.

⁷⁶ See proposed Rule 701(j)(3).

⁷⁷ See Notice, *supra* note 3, at 9096–97.

⁷⁸ See Notice, *supra* note 3, at 9100–01.

⁷⁹ See *id.*

Proposed Rule 701(j)(6) provides that, to the extent possible, the system will execute orders at the Opening Price that have contingencies (such as without limitation, All-or-None, and Reserve Orders) and non-routable orders such as “Do-Not-Route” or “DNR” Orders.⁸² The system will only route non-contingency Public Customer orders, except that the full volume of Public Customer Reserve Orders may route.

Proposed Rule 701(j)(6)(i) provides that the system will cancel: (i) Any portion of a Do-Not-Route Order that would otherwise have to be routed to the exchange(s) disseminating the ABBO for an opening to occur, (ii) an All-or-None Order that is not executed during the opening and is priced through the Opening Price; and (iii) any order that is priced through the Opening Price. All other interest will remain in the system and be eligible for trading after opening. The Exchange states that it cancels these orders since it lacks enough liquidity to satisfy these orders on the opening.⁸³ In addition, the Exchange believes that participants would prefer to have these orders returned to them for further assessment rather than have them entered into the order book at a price which is more aggressive than the price at which the Exchange opened.⁸⁴

8. Other Provisions

Proposed Rule 701(k) provides that during the opening of the option series, where there is a possible execution, the system will give priority first to Market Orders⁸⁵ then to resting Limit Orders⁸⁶ and quotes. Additionally, the allocation provisions of ISE Rule 713 and the Supplementary Material to that rule apply with respect to other orders and quotes with the same price. Finally, proposed Rule 701(l) provides that upon the opening of the option series, regardless of an execution, the system will disseminate the price and size of the Exchange’s best bid and offer.

9. Implementation

The Exchange states that it intends to begin implementation of the proposed rule change in the second quarter of 2017.⁸⁷ The Exchange represents that migration of the Exchange system to Nasdaq INET technology will be on a symbol by symbol basis and that the Exchange will issue an alert to Members to provide notification of the symbols

that will migrate and the relevant dates.⁸⁸

III. Discussion and Commission Findings

After careful review, the Commission finds that the proposed rule change, as modified by Amendment No. 1, is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange.⁸⁹ In particular, the Commission finds that the proposed rule change is consistent with Section 6(b)(5) of the Act,⁹⁰ which requires, among other things, that the rules of a national securities exchange be designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in facilitating transactions in securities, 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 Exchange proposes to delete in its entirety the current opening process and replace it with an opening rotation similar to the process in place on its affiliated exchanges, Phlx and ISE Gemini. In making this change, the Exchange delineates, unlike in the current, more opaque rule, detailed steps of the opening process. By providing more clearly each sequence of the opening process, the Commission notes that the proposed rule helps market participants understand how the new opening rotation will operate. To that extent, the new opening process may promote transparency, reduce the potential for investor confusion, and assist market participants in deciding whether to participate in ISE’s opening rotation. Further, if they do participate in the new opening process, the proposed rule may help provide market participants with the confidence and certainty as to how their orders or quotes will be processed.

Further, the Commission believes that the proposed rule change is designed to promote just and equitable principles of trade by seeking to ensure that option series open in a fair and orderly manner. For example, the Commission notes that the proposed rule change is designed to mitigate the effects of the underlying security’s volatility as the overlying

option series undergoes the opening rotation. Specifically, the proposed rule provides for a range of no less than 100 milliseconds and no more than 5 seconds in order to ensure that the Exchange has the ability to adjust the period for which the underlying must be open on the primary market before the opening process commences. Moreover, the Commission notes that the proposed rule provides an orderly process for handling eligible interests during the opening rotation, while seeking to avoid opening executions at suboptimal prices. For instance, the new process ensures that the Exchange will not open with the Exchange’s BBO if there is a Zero Bid Market, no ABBO, and no Quality Opening Market. Likewise, the Exchange will not open an option series with a trade unless one of the following conditions is met: (1) The Potential Opening Price is at or within the Pre-Market BBO and the ABBO; (2) the Potential Opening Price is at or within the non-zero bid ABBO if the Pre-Market BBO is crossed; or (3) where there is no ABBO, the Potential Opening Price is at or within the Pre-Market BBO which is also a Quality Opening Market. Finally, while the new opening process attempts to maximize the number of contracts executed on the Exchange during such rotation, including by seeking additional liquidity, if necessary, the Commission notes that the new opening process, unlike the current process, takes into consideration away market interests and ensures that better away prices are not traded through. For these reasons, the Commission believes that the proposed rule change, as modified by Amendment No. 1, is consistent with the Act.

IV. Conclusion

It is therefore ordered, pursuant to Section 19(b)(2) of the Exchange Act,⁹¹ that the proposed rule change (SR-ISE-2017-02), as modified by Amendment No. 1, be, and it hereby is, approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.⁹²

Eduardo A. Aleman,
Assistant Secretary.

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⁸² See ISE Rule 715(m).

⁸³ See Notice, *supra* note 3, at 9101.

⁸⁴ See *id.*

⁸⁵ See ISE Rule 715(a).

⁸⁶ See ISE Rule 715(b).

⁸⁷ See Notice, *supra* note 3, at 9090.

⁸⁸ See *id.* For a more detailed description of the proposed rule change, see Notice, *supra* note 3.

⁸⁹ 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).

⁹⁰ 15 U.S.C. 78f(b)(5).

⁹¹ 15 U.S.C. 78s(b)(2).

⁹² 17 CFR 200.30-3(a)(12).