

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-73261; File No. SR-ISE-2014-43]

### Self-Regulatory Organizations; International Securities Exchange, LLC; Notice of Filing of Proposed Rule Change Amending Its Information Barrier Rules

September 30, 2014.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the "Act"),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on September 15, 2014, the International Securities Exchange, LLC (the "Exchange" or the "ISE") filed with the Securities and Exchange Commission ("Commission") the proposed rule change, as described in Items I and II 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 International Securities Exchange, LLC (the "Exchange" or the "ISE") is proposing to amend its Rules 810 (Limitations on Dealings) and 717 (Limitations on Orders). The text of the proposed rule change is available on the Exchange's Web site (<http://www.ise.com>), at the principal office of 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 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 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 Exchange is proposing to amend its Rules 810 (Limitations on Dealings)

and 717 (Limitations on Orders) governing information barriers. Specifically, the Exchange is proposing to amend the portion of the rules that address the limitation on the flow of information between a member's Electronic Access Member ("EAM") unit, which handles the customer/agency side of the business, and its affiliated Primary Market Maker ("PMM") and/or Competitive Market Maker ("CMM") (jointly, "market makers") unit, which handles the proprietary side of the business.

ISE adopted its Rule 810 (Limitations on Dealings) on February 24, 2000<sup>3</sup> and over the years, the Exchange has frequently been asked by its members to provide guidance as to what information can be shared between an EAM and its affiliated market maker business under Rule 810.<sup>4</sup> The Exchange's position on this issue has always been that the information barrier between the EAM unit and its affiliated market maker unit must restrict the flow of information in both directions. As so interpreted, (i) the EAM unit cannot know where and at what price its affiliated market makers are quoting and, therefore, cannot use that information to influence their routing decisions, and (ii) the market makers cannot know what customer orders its affiliated EAMs are handling as agent and, therefore, cannot use that information to influence their quotations.

The Exchange is now proposing to amend its Rule 810 to allow EAMs to know where and at what price its affiliated market makers are either quoting or have orders on the order book<sup>5</sup> and to use that information to influence their routing decisions. As such, an EAM may route an order that it is handling on an agency basis to the ISE where its affiliated market maker is either quoting or has an order on the order book so that the two orders immediately interact. The Exchange posits that these such members, in the context of risk management<sup>6</sup> and consistent with the protections against the misuse of material nonpublic

information,<sup>7</sup> should be able to consider the outstanding quotes of their affiliated market maker units for the purposes of calculating net positions and making routing decisions to increase the member's interaction rate between its EAM unit and affiliated market making unit(s). Further, the Exchange asserts that a member should be able to integrate its market makers' positions and quoting information with its EAM unit(s) because this proposal, in tandem with existing ISE conduct rules,<sup>8</sup> ISE's review and approval of the information barrier procedures submitted by market makers that will be conducting Other Business Activities,<sup>9</sup> ISE's ongoing surveillances for manipulative conduct, and FINRA's exam program that reviews such members compliance with such policies and procedures, should provide a regulatory framework that guards customer interests and protects against the misuse of material nonpublic information, while increasing the operational flexibility of ISE members.

ISE Rule 717(d) and (e) requires members to expose certain orders entered on the limit order book for at least one second before executing them as principal or against orders that were solicited from other broker-dealers. This requirement applies when the EAM is handling both sides of a trade and not when an EAM is handling a marketable order as agent and is routing that order to execute against a quote/order resting on the order book. Accordingly, when customer order(s) that an EAM is handling as agent executes against an affiliated market maker's quote or order, it appears as though the EAM was in fact handling both sides of the trade, and did not comply with the order exposure requirements of ISE Rule 717(d) and (e). However, because the Exchange does not publicly identify the member that entered an order on the limit order book, orders from the same

<sup>7</sup> See, e.g., 15 U.S.C. 78o(g). Section 15(g) of the Securities and Exchange Act of 1934 (the "Act") requires every broker or dealer to "establish, maintain, and enforce written policies and procedures reasonably designed, taking into consideration the nature of such broker's or dealer's business, to prevent the misuse . . . of material, nonpublic information by such broker or dealer or any person associated with such broker or dealer."

<sup>8</sup> See, e.g., ISE Rules 400 (Just and Equitable Principles of Trade), 401 (Adherence to Law), 405 (Manipulation), 408 (Prevention of the Misuse of Material, Nonpublic Information) and 713 (Priority of Quotes and Orders).

<sup>9</sup> ISE Rule 810 defines "Other Business Activities" as meaning, (1) conducting an investment or banking or public securities business; (2) making markets in the stocks underlying the options in which it makes markets; (3) handling listed options orders as agent on behalf of Public Customers or broker-dealers; or (4) conducting non-market making proprietary listed options trading activities.

<sup>3</sup> See Securities Exchange Act Release No. 34-4255 [sic]; File No. 10-127 (February 24, 2000).

<sup>4</sup> Rule 810 currently permits market makers to provide its affiliated EAM, upon request, the same general quotation information that it would provide to an unaffiliated entity. The intent of that provision was an attempt in 2000 to replicate a floor-based market, in which a broker could ask a floor-based specialist general information on the market.

<sup>5</sup> According to Rule 805(b)(1)(i) and (ii) market makers may only have orders on the order book in option classes to which they are not appointed.

<sup>6</sup> See, e.g., 17 CFR Part 240.15c3-5 (Risk Management Controls for Brokers or Dealers with Market Access).

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

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

firm may inadvertently execute against each other as a result of being entered by disparate persons and/or systems at the same member firm. Therefore, when enforcing Rule 717(d) and (e), the Exchange has never considered the inadvertent interaction of orders from the same firm within one second to be a violation of the exposure requirement.

On September 20, 2011 the Exchange codified this longstanding policy in Supplementary Material .06 to Rule 717,<sup>10</sup> which currently specifies that members can demonstrate that orders were entered without knowledge of a pre-existing order on the book represented by the same firm by providing evidence that effective information barriers between the persons, business units and/or systems entering the orders onto the Exchange were in existence at the time the orders were entered.<sup>11</sup> This rule requires that such information barriers be fully documented and provided to the Exchange upon request.<sup>12</sup>

Given the proposed change to ISE Rule 810, the Exchange is also proposing to make a corresponding change to Supplementary Material .06 to Rule 717 to specify that orders from the same member's EAM unit and its affiliated PMM and/or CMM unit may interact within one second without being a violation of the order exposure requirement of paragraph (d) and (e) of Rule 717 when the firm can demonstrate that the customer order that it routed was marketable, the EAM was not handling the affiliated market maker quote/order and the affiliated market maker quote/order was in existence at the time the customer order(s) were entered into the ISE's system.

The Exchange believes that adopting these rule changes will allow for the Exchange to provide its membership with increased operational flexibility while keeping intact the original purpose of the rule, which was intended to prevent market makers from using customer order flow information to influence their quotations. The Exchange believes that allowing

information to flow from the market maker to the EAM would not compromise the integrity of our market, nor would it introduce customer harm, as discussed in more detail above. Additionally, the Exchange believes that market quality will not be eroded due to these changes because the information barrier preventing the flow of information from the EAM to its' affiliated market maker remains unchanged, meaning, market makers will continue to be unable to adjust their quotes either to intercept or avoid orders since that side of the barrier remains in force.

## 2. Statutory Basis

The basis under the Act for this proposed rule change is the requirement under Section 6(b),<sup>13</sup> in general, and Section 6(b)(5)<sup>14</sup> in particular, 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 for a free and open market and a national market system, and, in general, to protect investors and the public interest. In particular, the Exchange believes that amending its rules to allow information to flow from the market maker to the EAM would not compromise the integrity of the market as the information barrier preventing the flow of information from the EAM to its affiliated market maker remains unchanged. Meaning, a market maker cannot be privy to nonpublic information about incoming customer orders and adjust their quotations in response. The Exchange also believes that this rule change will not introduce customer harm as this change does not impact the order protection rules applicable to an EAM handling an order as agent,<sup>15</sup> but rather allows the EAM to route to a specific destination to interact with its affiliated market makers' quotations or orders in the same manner that the EAM would route orders to access quotes and orders of market makers that it is not affiliated with. In addition, members will continue to be subject to federal and Exchange requirements for protecting material nonpublic order information.<sup>16</sup>

Additionally, the Exchange notes that the rule will still require that member organizations maintain and enforce policies and procedures reasonably designed to ensure compliance with applicable federal securities laws and

regulations and with Exchange rules. Such written policies and procedures will continue to be subject to oversight by the Exchange and therefore allowing information to flow from the market makers to their affiliated EAMs should not reduce the effectiveness of the Exchange rules to protect against the misuse of material nonpublic information. Rather the Exchange believes that a member should be able to integrate its market makers' positions and quoting information with its EAM unit(s) because this proposal, in tandem with existing ISE conduct rules,<sup>17</sup> ISE's review and approval of the information barrier procedures submitted by market makers that will be conducting Other Business Activities, ISE's ongoing surveillances for manipulative conduct, and FINRA's exam program that reviews such members compliance with such policies and procedures, should provide a regulatory framework that guards customer interests and protects against the misuse of material nonpublic information. The proposed changes do not alter a member's best execution duty to get the best price for its customer and, therefore, the Exchange does not believe that the proposed changes provided any advantage or disadvantage to customers or the markets in general.

### *B. Self-Regulatory Organization's Statement on Burden on Competition*

The Exchange does not believe that the proposed rule change will impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. However, the Exchange believes that Rule 810 currently imposes a burden on competition for the Exchange because it requires market makers that engage in Other Business Activities to operate in a manner that the Exchange believes is more restrictive than necessary for the protection of investors to the public interest. The Exchange believes that the proposed rule change is pro-competitive because it is consistent with how other national securities exchanges are currently interpreting their rules and should provide greater flexibility to allow member firms to make routing decisions based on the same information across multiple markets.

### *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

<sup>10</sup> See Securities Exchange Act Release No. 65361 (September 20, 2011), 76 FR 59472 (September 26, 2011) (SR-ISE-2011-42).

<sup>11</sup> The Exchange conducts routine surveillance to identify instances when an order on the limit order book is executed against an order entered by the same firm within one second.

<sup>12</sup> The Exchange reviews information barrier documentation to evaluate whether a member has implemented processes that are reasonably designed to prevent the flow of pre-trade order information given the particular structure of the member firm. Additionally, information barriers are reviewed as part of the Exchange's examination program, which is administered by the Financial Industry Regulatory Authority ("FINRA") pursuant to a regulatory services agreement.

<sup>13</sup> 15 U.S.C. 78f(b).

<sup>14</sup> 15 U.S.C. 78f(b)(5).

<sup>15</sup> See note 7.

<sup>16</sup> See 15 U.S.C. 78o(g) and ISE Rule 408.

<sup>17</sup> See note 7.

unsolicited written comments from members or other interested parties.

**III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action**

Within 45 days of the publication date of this notice in the **Federal Register** or within such longer period up to 90 days (i) as the Commission may designate 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 or disapprove 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. The Commission requests comments, in particular, on the following:

1. If the proposed rule change is approved, an EAM will be able to know where and at what price its affiliated market makers are either quoting or have orders on the order book and to use that information to influence its routing decisions. Do commenters agree with the Exchange's assertion that the proposed rule change will not introduce customer harm, as this change does not impact the order protection rules applicable to an EAM handling an order as agent? Do commenters have a view on whether permitting EAMs to make routing decisions, based on knowledge of an affiliated market maker's quotes, would impact the execution quality and handling of customer orders? Please explain.

2. Given that EAMs must maintain policies and procedures that are reasonably designed to ensure against the misuse of material, nonpublic information pursuant to ISE Rule 408, do commenters have any views regarding a proposed rule that would permit an EAM to have non-public information about where and at what price its affiliated market maker is either quoting or has orders on the order book?

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 Email to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File No. SR-ISE-2014-43 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-2014-43. This file number should be included on the subject line if email 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 Commissions 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 Web site 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 such filing also will be available for inspection and copying at the principal office of the ISE. 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-2014-43 and should be submitted by October 27, 2014.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>18</sup>

**Kevin M. O'Neill,**

*Deputy Secretary.*

[FR Doc. 2014-23701 Filed 10-3-14; 8:45 am]

**BILLING CODE 8011-01-P**

**SMALL BUSINESS ADMINISTRATION**

**[Disaster Declaration #14136 and #14137]**

**Washington Disaster #WA-00047**

**AGENCY:** Small Business Administration.

**ACTION:** Notice.

**SUMMARY:** This is a notice of an Administrative declaration of a disaster for the State of Washington dated 09/29/2014.

<sup>18</sup> 17 CFR 200.30-3(a)(12).

*Incident:* Central Washington Firestorm.

*Incident Period:* 07/09/2014 through 08/05/2014.

**EFFECTIVE DATE:** 09/29/2014.

*Physical Loan Application Deadline Date:* 11/28/2014.

*Economic Injury (EIDL) Loan Application Deadline Date:* 06/29/2015.

**ADDRESSES:** Submit completed loan applications to: U.S. Small Business Administration, Processing and Disbursement Center, 14925 Kingsport Road, Fort Worth, TX 76155.

**FOR FURTHER INFORMATION CONTACT:** A. Escobar, Office of Disaster Assistance, U.S. Small Business Administration, 409 3rd Street SW., Suite 6050, Washington, DC 20416.

**SUPPLEMENTARY INFORMATION:** Notice is hereby given that as a result of the Administrator's disaster declaration, applications for disaster loans may be filed at the address listed above or other locally announced locations.

The following areas have been determined to be adversely affected by the disaster:

*Primary Counties:* Okanogan.

*Contiguous Counties:*

Washington: Chelan, Douglas, Ferry, Grant, Lincoln, Skagit, Whatcom.

The Interest Rates are:

	Percent
<i>For Physical Damage:</i>	
Homeowners With Credit Available Elsewhere .....	4.375
Homeowners Without Credit Available Elsewhere .....	2.188
Businesses With Credit Available Elsewhere .....	6.000
Businesses Without Credit Available Elsewhere .....	4.000
Non-Profit Organizations With Credit Available Elsewhere ...	2.625
Non-Profit Organizations Without Credit Available Elsewhere .....	2.625
<i>For Economic Injury:</i>	
Businesses & Small Agricultural Cooperatives Without Credit Available Elsewhere .....	4.000
Non-Profit Organizations Without Credit Available Elsewhere .....	2.625

The number assigned to this disaster for physical damage is 14136 5 and for economic injury is 14137 0.

The State which received an EIDL Declaration # is Washington. (Catalog of Federal Domestic Assistance Numbers 59002 and 59008)

Dated: September 29, 2104.

**Maria Contreras-Sweet,**  
*Administrator.*

[FR Doc. 2014-23808 Filed 10-3-14; 8:45 am]

**BILLING CODE 8025-01-P**