

## Regulatory Information Circular – 2001-03

**To:** ISE Market Makers

**Date:** March 1, 2001

**Re:** “Trade or Fade” Policy

The Securities and Exchange Commission has mandated certain exchange-wide changes to the Trade or Fade rules in an effort to standardize the treatment of quotations across the options markets. These changes become effective on April 1, 2001, when the SEC's "Firm Quote Rule" (Rule 11Ac1-1 under the Exchange Act) becomes applicable to the options markets.

ISE Rule 804(d)(2) provides that market makers must either trade with a non-customer order up to the displayed size of their quotes or “change their quotes to reflect that the previously displayed quote is no longer available.” Absent a change in the underlying security price, when a market maker's quotation is automatically moved as a result of a non-customer order, it is inconsistent with the trade-or-fade rule for the market maker to immediately requote at the previous price.<sup>1</sup> Such immediate re quoting does not comply with the requirement of the rule that the quote “reflect that the previously displayed quote is no longer available.” Previously, the ISE advised market makers that they could not, after “fading,” requote at the same price 15 seconds. (RIC 2000-7 (August 16, 2000).) Exceptions to this requirement allowed a re quoting at the same price if (i) there was movement in the underlying stock or (ii) if another market maker established a quote at the previous price and the market maker who faded matched that price.

The application of the SEC's Firm Quote Rule changes these policies. Specifically, as of April 1<sup>st</sup>, a market maker may not requote at the same price within 30 seconds (as opposed to the current 15 seconds) of being automatically moved as a result of the trade-or-fade process, barring unusual market conditions. Additionally, the market maker electing to fade his/her bid or offer may not reinstate his/her bid or offer for at least 30 seconds even if the ISE's best bid or offer returns to the previous price as a result of another participant's quote or limit order. A market maker will continue to be allowed to requote at the same price within this 30 second period to reflect a corresponding movement in the underlying security.

For further information on the "trade-or-fade" rule, or if you have any questions, please contact Pat Gillespie at 212-897-0130, Associate Director, Trading Analysis, or Jim Sampson, Director Market Surveillance and Regulation at 212-897-0235.

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<sup>1</sup> In the ISE's electronic market, the trade-or-fade rule is accomplished as follows: A market maker pre-sets parameters to indicate how much of the displayed size of a quote it would be willing to trade with non-customer orders. If there is insufficient non-customer size available to execute a non-customer order entirely at the displayed price, the quote is automatically moved down (for a bid) and up (for an offer).