

**Boston Options Exchange
Chicago Board Options Exchange
International Securities Exchange
NASDAQ Options Market
NASDAQ OMX PHLX
NYSE Amex
NYSE Arca
The Options Clearing Corporation**

September 22, 2009

Ms. Elizabeth Murphy
Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549-1090

Re: File No. S7-08-09

Dear Ms. Murphy:

The Boston Options Exchange, the Chicago Board Options Exchange, the International Securities Exchange, NASDAQ Options Market, NASDAQ OMX PHLX, NYSE Amex, NYSE Arca, and The Options Clearing Corporation (“the Options Exchanges”) appreciate the opportunity to provide additional comment on File No. S7-08-09 (the “Release” or “Proposing Release”) which proposes amendments to Regulation SHO, the Securities and Exchange Commission’s (“Commission”) primary regulation governing short sales.¹ The Commission has re-opened the comment period on the Release to provide an opportunity to comment on one aspect of that Release, an alternative price test that would allow selling only at a price above the current national best bid (“alternative uptick rule”) as a permanent price test restriction or in conjunction with a circuit breaker.² The Release notes that the alternative uptick rule would be more restrictive than the other price tests proposed by the Commission because it would not allow short sales to get immediate execution even in a rising market.³ In recognition of the more restrictive nature of the alternative uptick rule, the Commission sought comment on the importance of a market maker exception in this context.⁴

¹ Securities Exchange Act Release No. 59748 (April 10, 2009), 74 Fed. Reg. 10842 (April 20, 2009).

² Securities Exchange Act Release No. 60509 (August 17, 2009), 74 Fed. Reg. 42033 (August 20, 2009).

³ 74 Fed. Reg. 42034.

⁴ 74 Fed. Reg. 42035, 42036.

The Options Exchanges filed a comment letter on the original Release focusing on the impact of the proposed restrictions on short sales on options market makers, and all of the comments and arguments should be considered to be incorporated by reference in this letter.⁵ Our comment letter noted that the Commission proposed an options market maker exception in its trading halt alternative and strongly urged the Commission to maintain that exception if it chose to adopt that alternative. In addition, the Options Exchanges stated our strong belief that an exception for options market makers is essential if the Commission chose to restrict short sales by adopting any of the other alternatives proposed in the original Release. Without an exception for options market makers who are short selling to hedge the exposure that arises from bona fide market making, we asserted that these alternatives would significantly harm the ability of options market makers to respond to customer demand with narrow bid/ask spreads and ample liquidity. The result would be harm to investors.

The restrictive nature of the alternative uptick rule makes it even more vital that the Commission adopt an options market maker exception if it chooses to adopt this approach on either on a market-wide and permanent basis or applies it to a particular security in conjunction with a circuit breaker. Moreover, we note that adoption of such an exception would be consistent with the Commission's current approach in Regulation SHO, as well as the Commission's prior emergency orders from the summer and fall of 2008 imposing: (i) requirements to borrow or arrange to borrow prior to effecting short sales; (ii) enhanced close-out requirements; and (iii) a ban on short sales in certain financial companies. Indeed, even during such periods of market stress, the Commission clearly recognized that exceptions for options market makers were essential "to permit market makers to facilitate customer orders in a fast-moving market"⁶ and "to permit market makers to continue to provide liquidity to the markets."⁷ The Options Exchanges feel strongly that these important investor-protection goals can equally only be realized by the Commission incorporating an options market maker exception in the proposed alternative uptick rule. Furthermore, it would be incongruous for the Commission to recognize the necessity of an exception from short sale restrictions during times of market stress and to provide an exception from the Regulation SHO locate requirement, but not include similar relief from a price test restriction, especially given the Commission's own stated reservations on the overall effectiveness of price tests.

⁵ Letter to Elizabeth Murphy, Secretary, SEC from Boston Options Exchange, Chicago Board Options Exchange, International Securities Exchange, NASDAQ Options Market, NASDAQ OMX PHLX, NYSE Amex, NYSE Arca, and The Options Clearing Corporation (June 22, 2009).

⁶ Securities Exchange Act Release No. 58190 (July 18, 2008), 73 FR 42837 (July 23, 2008) (emergency order imposing borrow or arrange to borrow requirement).

⁷ Securities Exchange Act Release No. 58592 (September 18, 2008), 73 FR 55169 (September 24, 2008) (emergency order banning short selling in designated financial companies).

If the Commission decides to adopt the alternative uptick rule, we strongly urge it to also adopt an options market maker exception modeled on the market maker exemption from the NASD bid test that was in effect prior to Commission's elimination of all short sale price test restrictions.⁸ As described in more detail in our June 22 comment letter, that exemption applied to "exempt hedge transactions" by "qualified options market makers" that are registered with a "qualified options exchange," as those terms were defined in the exemption.⁹ At the time that the Commission considered whether to approve the exemption, it noted that that in light of the safeguards proposed in conjunction with the exemption, the NASD did not believe that the exemption would "subsume or eviscerate the effectiveness of the NASD's short sale rule."¹⁰ Adoption of a similar exception for options market makers to the proposed alternative uptick rule would both minimize the potential adverse impacts of that rule on the options markets and provide appropriate conditions to ensure that only bona fide market making is captured by the exception. Such an exception could also be informed by and incorporate prior guidance provided by the Commission in the context of Regulation SHO.¹¹

The Options Exchanges would also like to restate the request made in our prior comment letter that all "short sales" (under a broad interpretation of the definition of such term in Regulation SHO) that may result from assignments and exercises (whether or not automatic) be excepted from the proposed alternative uptick rule, or any other any circuit breaker halt or price test that may ultimately be adopted. Again, while it is possible that the Commission did not mention a specific exception for exercises and assignments due to the fact that the price test would otherwise not apply to the after hours market, when exercises and assignments would occur, we would request that the Commission make clear that it did not intend to capture exercises and assignments. As noted in our original comment letter, other considerations that merit not capturing exercises and assignments under any price test restrictions include the fact that they take place at a fixed strike price that is not determined in relation to the current market price, and are expressly excepted from trade reporting. This fact, and the resulting conclusion that exercises and assignments could not have a depressing impact on the price of a security, was the reason why exercises and assignments were not covered by the former Rule 10a-1 price test.

The Options Exchanges again commend the Commission for the thoughtful, deliberative approach that it is taking on the important issue of whether to reinstate short sale price tests, and if so, what approach would best restore investor confidence while maintaining market efficiency. The Commission's re-opening of the comment period on the Release

⁸ Securities Exchange Act Release No. 34277, 59 Fed. Reg. 34885 (July 7, 1994).

⁹ Id.

¹⁰ Id.

¹¹ See, e.g., Securities Exchange Act Release No. 58775, 73 Fed. Reg. 61690, 61698 (October 17, 2008) (providing guidance on the definition of bona-fide market making in the context of the Reg. SHO locate requirement.)

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to provide a full opportunity to comment on all of the alternatives under consideration is further evidence of that approach. The potential impact of the additional restrictions on short sales that the Commission is weighing justifies the thought and care of the current process. Finally, the significant and effective actions that the Commission has already taken to restrict potentially abusive short selling lessen the urgency to decide whether further action is necessary.¹²

Thank you again for the opportunity to comment on the Commission's proposal to restrict short sales by adopting a market wide alternative uptick rule or a security specific alternative uptick rule as part of a circuit breaker. If you would like to discuss any of the issues raised in this letter, please contact Susan Milligan at The Options Clearing Corporation at (202) 756-1972.

Sincerely,

Boston Options Exchange
Chicago Board Options Exchange
International Securities Exchange
NASDAQ Options Market
NASDAQ OMX PHLX
NYSE Amex
NYSE Arca
The Options Clearing Corporation

cc: James A. Brigagliano
Daniel Gallagher

¹² These actions include the Commission's recent decision to finalize Rule 204 which imposes strict delivery requirements for all equity securities. Exchange Act Release No. 60388 (July 27, 2009), 74 Fed. Reg. 38266 (July 31, 2009). Our June 22 letter describes additional actions that the Commission has recently taken to address potentially abusive short selling. Comment Letter at 2, 3.