



ORDER EXECUTION SERVICES HOLDINGS, INC.
194 Nassau Street, Suite 30, Princeton, NJ 08542

October 2, 2006

Ms. Nancy M. Morris
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: SR-CBOE-2006-70, Amendment Number One

Dear Ms. Morris:

Order Execution Services Holdings, Inc. (“OES”) submits to the Securities and Exchange Commission (“Commission”) this comment letter regarding the Chicago Board Options Exchange, Incorporated (“CBOE”) rule change, SR-CBOE-2006-70, to adopt new rules in order to implement a new electronic trading system called STOC. OES believes that the CBOE in its filing is redefining the definition of an exchange to include capabilities that currently are required to be performed by a broker-dealer. As a result, OES requests the Commission to reconsider its previous approval on an accelerated basis of SR-CBOE-2006-70 in its current form.

OES is concerned that the Commission chose to approve this filing on an accelerated basis rather than publish it for comment and allowing reasonable public consideration prior to its decision. It appears to OES that the Commission may have better served the interests of investors and the securities industry by being more prudent and publishing the Amendment for comment without granting accelerated approval.

In the CBOE’s proposed rule change its Rule 52.10 contains Interpretations and Policies .01 (b):

As provider of the Routing Services, the Exchange will determine the logic that determines when, how, and where orders are routed away to other trading centers.
(Emphasis added by OES)

OES asserts that this rule will make the CBOE, through its powers to use discretion on when, how, and where orders are routed (and thus make best execution judgments), an agent to its members with fiduciary responsibilities. The definitions found in the Exchange Act establishes that the purpose of an exchange to be a market place that brings together buyers and sellers so that these parties can agree on the terms of a trade, and



furthermore that a broker-dealer is the party that acts as an agent for the buyer or seller of a trade. An exchange is a market place and a broker-dealer is an agent. Therefore, OES asserts that the CBOE needs a facility broker-dealer through which it can make discretionary routing decisions.

The CBOE proposes in Rule 52.10 to provide its routing services pursuant to the terms of three separate agreements. Although these contracts include an agreement between the CBOE and each member on providing routing services, the member does not have the authority to grant the CBOE the ability to provide broker-dealer services where it acts as a discretionary agent that determines order handling terms of a trade when it is an exchange. OES believes that the CBOE and the Commission erred in their efforts to contractually establish in a chain of agreements the apparent legal capability to provide routing services between three parties and a technology provider, when they failed to recognize that an exchange does not have the authority to make discretionary routing decisions because it crosses the definition of an exchange over into the definition of a broker-dealer.

The Commission addressed many facets of what are the definitions of exchanges versus what are alternative trading systems and broker-dealers in Reg ATS. The Commission revised its Rule 3b-16 to define exchange to mean any organization, association, or group of persons that: (1) brings together the orders of multiple buyers and sellers; and (2) uses established, non-discretionary methods under which such orders interact with each other, and that the buyers and sellers entering such orders agree to the terms of a trade. In addition, the Commission changed Rule 3b-16 to exclude certain systems, including those that merely route orders to other facilities for execution. Reg ATS helped the Commission adapt what is generally understood to be an exchange to reflect changes brought about by automated trading, but it continued to reflect the concept that an exchange brings together buying and selling interests.

It requires that the exchange brings together orders and trading interests entered on its system or represented to its system users. Therefore, it seems to say that the exchange's facilities have to bring both the buyer and seller together to trade based on acceptable terms. The "bring together" does not include an external buyer or seller. The Commission also required that the methods to bring the parties together have to be non-discretionary. The Commission's position and requirements support the point that in order to have discretion, the handler of the order needs to be an agent, and agents are broker-dealers not exchanges. The Commission also said it intended for "established, non-discretionary methods" to include methods that dictate the terms of trading among buyers and sellers entering orders into the exchange's system.

The Commission stated that, "Rules that merely supply the means of communication with a system ... do not satisfy this element of Rule 3b-16." OES asserts that the CBOE's outbound routing services: (1) does not bring together a buyer and seller within their system, and (2) is a means of communication with another market center's system.



In the Reg ATS Approval Order the Commission uses an example of block trading desks using discretion in determining how to execute a customer's order, and the discretion may include "shopping" the order around in an attempt to find contra-side interest at the order's terms. The outbound router services of the CBOE will have similar discretion when it is deciding how to route an order when multiple market centers are simultaneously displaying the best price, and it makes a choice(s) using "smart" routing logic to determine where to route the order. The CBOE will be making as an agent best execution routing decisions. The Commission did not appear to consider this level of discretion to fall within Rule 3b-16.

The Commission also addressed that a trading system that falls within the interpretation of "exchange" is a system where it matches two orders and routes them to another exchange for execution. The outbound router services of the CBOE only have one side of a trade, and that is a buy order or a sell order. This classification does not match the current interpretation of an exchange.

Excerpt from Reg ATS: Systems Excluded From Rule 3b-16

The Proposing Release specifically excluded from the proposed, revised interpretation of "exchange" several types of activities that could be considered traditional brokerage activities: order routing systems, dealer quotation systems, and internal broker-dealer order management and execution systems. Commenters widely agreed that automated broker-dealer functions should not be encompassed in the meaning of "exchange." The Commission agrees. (Emphasis added by OES)

The Commission does not believe that these routing systems meet the two-part test in paragraph (a) of Rule 3b-16 because they do not bring together orders of multiple buyers and sellers. Instead, all orders entered into a routing system are sent to another execution facility. In addition, routing systems do not establish non-discretionary methods under which parties entering orders interact with each other.

OES asserts that these last two paragraphs, which were extracted from Reg ATS, establish that routing systems are broker-dealer functions and cannot be performed solely by an exchange. OES would also argue that an order routed away needs to have both an agent representing its interest, and using fiduciary discretion to seek an execution that is in the order's best interest.

A number of exchanges have responded to the outbound routing challenges of Reg NMS and their new exchange trading models. Many of these exchanges have proposed new rules that include an exchange facility (as defined in Section 3(a)(2) of the Exchange Act) broker-dealer responsible for acting as agent and making routing decisions (as fully defined and controlled by the affiliated exchange). OES believes that the Commission's rules, interpretations and precedent of previous decisions all support the requirement for a



facility broker-dealer to perform the agent role making discretionary decisions on how to best handle a member's order. As described, the CBOE should be required to establish as part of its order routing services a facility broker-dealer through which the CBOE will determine when, how and where orders are routed. Otherwise, this accelerated approval order from the Commission on this rule by the CBOE will redefine an exchange to include broker-dealer responsibilities. The long-term consequences of this decision could dramatically alter the securities industry.

OES appreciates this opportunity to submit to the Commission our views on this filing, and we welcome the ability to further participate in future discussions or deliberations related to the Commission's decision on this matter. Please feel free to contact me at (609) 430-4979, or by email at mbarth@tradeoes.com.

Sincerely,

Michael A. Barth
Senior Vice President
Exchanges and Market Centers
Order Execution Services Holdings, Inc.