



INTERNATIONAL SECURITIES EXCHANGE.

60 Broad Street, New York, NY 10004
TEL: 212 943-2400
FAX: 212 425-4926
www.ise.com

August 10, 2012

Elizabeth M. Murphy
Secretary
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-0609

Re: File No. SR-ISE-2012-22

Dear Ms. Murphy:

We submit this letter in response to the U.S. Securities and Exchange Commission's ("SEC" or "Commission") order instituting proceedings to determine whether to approve or disapprove the captioned proposed rule change, as amended, of the International Securities Exchange, LLC ("ISE" or "Exchange").¹ That filing proposed the listing and trading on ISE of cash-settled options based on the ISE Max SPY™ Index ("Max SPY Index").²

As explained in the Max SPY Filing and in our two responses to comments on that filing,³ the Max SPY Index is a new index product designed to represent 10 times the value of the published share prices in the SPDR® S&P 500® ETF Trust (the "Trust"). We propose to trade options on the Max SPY Index that will be P.M. cash-settled, and that will have European-style exercise provisions ("Max SPY Options"). There are no significant legal issues regarding our proposal to Max SPY Options. Rather, we unfortunately find ourselves in the midst of a proceeding in which a competitor exchange, the Chicago Board Options Exchange ("CBOE"), is misusing the regulatory process to suppress competition. CBOE clearly views the proposed Max SPY Options as likely to attract interest from investors who currently trade in CBOE's monopoly SPX option products ("SPX Options").

¹ Securities Exchange Act Release No. 67225 (June 20, 2012), 77 FR 38100 (June 26, 2012) (hereinafter, the "Order").

² Securities Exchange Act Release No. 66614 (March 16, 2012), 77 FR 16883 (March 22, 2012) (the "Max SPY Filing," regarding the trading of "Max SPY Index Options").

³ Letters dated May 4, 2012 and June 15, 2012 ("Second Comment Letter," together "Comment Letters"), from Michael Simon, Secretary, ISE. We incorporate by reference those two comment letters into this letter.

This is not the first time this tactic has been employed. CBOE's licensor S&P, acting as a proxy for CBOE, sought to prevent ISE from trading options on the SPDR® S&P 500® ETF Trust ("SPY Options"). The federal courts rejected that effort and held that ISE was entitled to trade SPY options even if that product would draw trading volume from SPX Options.⁴ Undeterred, CBOE now is engaged in a full-court press – without legal merit – to prevent us from trading a companion product to SPY Options. Our proposal meets all the requirements of the Securities Exchange Act of 1934, as amended ("Exchange Act"), and we respectfully request that the Commission not permit CBOE to continue its endless delaying tactics. Thus, we urge the Commission to approve the filing.

Below we first respond to the latest in a string of irrelevant issues CBOE raised in its last comment letter on this proposal before the institution of these proceedings. We then explain how the filing fully complies with the Exchange Act and why the Commission promptly should approve the proposal.

Response to CBOE's Third Comment Letter on the Max SPY Filing

In its third comment letter on the Max SPY Filing,⁵ CBOE raised questions regarding the timing of the information that will be necessary for ISE to make the settlement calculation. Specifically, CBOE stated its view that the information on which ISE would rely to compute its net asset value ("NAV") of the SPY ETF would not be available until 8:00 p.m., hours after ISE's stated deadline in computing the NAV. CBOE thus concludes that ISE's proposal "continues to mislead investors about how the Proposed Options would settle."

CBOE again has failed to raise an issue of any concern. ISE will use data distributed from the prior night by the National Securities Clearing Corporation, which is made widely available to market participants and commonly used to determine the intraday indicative value of the Trust shares during the current day. As we have represented, on a continuing basis ISE will make available to the general public the exact methodology used to calculate the settlement value of the Max SPY Index.

Response to the Order

We previously have addressed all of the expressed concerns with respect to the Max SPY Filing. Nevertheless, ISE wishes to respond to each of the SEC's requests for comment in the Order. Set forth below are the SEC's questions from the Order, along with our response to each question.

⁴ *Dow Jones & Co., Inc. v. Int'l Sec. Exch., Inc.*, 451 F.3d 295 (2d Cir. 2006).

⁵ Letter from Edward T. Tilly, President and Chief Operating Officer, CBOE, dated June 19, 2012.

There is No Potential for Market Disruption if Trading Begins Prior to Exhaustion of Judicial Challenges

What are commenters' views as to whether market disruption and harm to investors would occur if the Commission were to approve the proposed rule change before all judicial challenges to the lawfulness of the proposed options under state law have been resolved? In light of the Exchange's representation that it would not start trading the proposed options until the Illinois Circuit Court rules on the motion to enforce the Injunction, and its representation regarding the potential mechanisms to ensure an orderly wind down of trading in the event that ISE is enjoined from offering the product after trading has already begun, do commenters believe any harm would result if the Exchange started trading the proposed options before all judicial challenges to the lawfulness of the proposed options under state law have been resolved? Why or why not?

CBOE has instituted proceedings in Illinois seeking to enjoin ISE from trading Max SPY Options through a "Motion to Enforce Permanent Injunction."⁶ The permanent injunction to which CBOE refers restrained ISE from trading SPX Options and options on the Dow Jones Industrial Average – but not any other option product. ISE believes that these proceedings have no merit and has opposed the motion. However, to resolve doubts ISE has committed that it will not begin trading of this instrument until the Illinois Circuit Court rules on the pending motion. We strongly believe that the Illinois court will deny this motion, permitting us to begin trading. If so, it is possible, though highly unlikely, that an appeals court subsequently could reverse that decision, enjoining ISE from further offering this product for trading after it commences trading, and after investors establish open interest in the product.

In the event of such an injunction, ISE has represented that it would seek to have the Illinois court permit ISE to continue to offer a market for closing-only transactions for so long as it takes all open interest to be wound down in an orderly manner. ISE has systems, rules, and procedures in place that would permit such a closing-only orderly wind down. We cannot imagine that the Illinois court would refuse to permit such a closing-only market to permit the winding down of positions created during the lawful trading of the product prior to the issuance of the injunction on appeal.

Moreover, even if the court did deny a closing-only market, there are adequate rules and procedures in place, at both the exchange level and the clearing level, to handle that situation and to allow for an orderly wind down of any open interest. For example, The Options Clearing Corporation ("OCC") has by-laws and rules that, in the case of index options, permit it to create and use a "replacement index" to close out the open interest.⁷ So even in the extremely

⁶ *Chicago Board Options Exch., et al. v. Int'l Sec. Exch., LLC, et al*, Case No. 06 CH 24798 (Circuit Court, Cook County, Ill.).

⁷ See Article XVII, Section 3 of the OCC By-Laws.

unlikely doomsday scenario painted by CBOE, a process exists that protects investors and winds down open interest in an orderly manner. As an added precautionary measure, to alert investors to this highly unlikely scenario, ISE will work with OCC to insert a "litigation risk" discussion into the ODD. Since this scenario is not novel, such description would be substantially similar to the litigation risk language that was included in prior versions of the ODD with respect to Index Participation products.

We emphasize that, despite CBOE's protestations otherwise, investors are not facing a risk unique to this product. There have been multiple cases in the past whereby a market becomes unavailable for the continued trading of a product in which there is open interest. With respect to equity options, when a listed company declares bankruptcy, all the options exchanges may delist options on the stock, in which case there would be no available market to close the open interest. Investors with open positions then would wait until expiration and either will be assigned or not, according to OCC's rules and procedures. In this circumstance, there is no opportunity for investors to trade out of their positions, since there is no available market. While not ideal, this is a risk that options investors assume and it is not unique to this product.

In raising this "litigation risk," CBOE is simply trying to delay our trading of Max SPY Options. CBOE appears fully prepared to take any measure, no matter how meritless, to prevent ISE from trading this product, and will do whatever it can to draw out legal proceedings. The Commission has never required exhaustion of all legal challenges before approving a product, and CBOE has provided no legal basis for the Commission to institute such a policy.

ISE Has Provided All Necessary Information Regarding the Settlement Value of Max SPY Options

As outlined above, the Exchange has provided additional detail about how it intends to calculate the settlement value for options on the ISE Max SPY Index. What are commenters' views as to whether the Exchange should provide additional clarity in the filing regarding the calculation methodology for the settlement value of options on the ISE Max SPY Index to mitigate concerns regarding the potential for investor confusion? Please be specific in your response.

We could not have been clearer in describing how the settlement value for Max SPY Options will be calculated. Indeed, we have provided the actual arithmetic formula together with an accompanying narrative description. We will display this information on a dedicated page of our website. ISE thus has provided a completely-transparent, plain English, continuous, virtual "how-the-product-will-be-settled" manual. There is nothing confusing, ambiguous, or inappropriate about ISE's settlement calculation method. The formula is clear and transparent, and at all times will be displayed on ISE's website.

ISE Will Be Appropriately Calculating the Value of the Max SPY Index

As noted above, the Exchange would calculate the value of the ISE Max SPY Index by reference to the traded prices of SPY, times ten, at all times. However, the settlement value of the options on the ISE Max SPY Index would be calculated by reference to the NAV of SPY, as calculated by the Exchange, on a per share basis, times ten. What are commenters' views of the impact, if any, of the differences between the calculation of the settlement value of the proposed options and the value of the ISE Max SPY Index itself on investor understanding of the options on the ISE Max SPY Index? Do commenters believe that the differences between the calculation of the settlement value of the proposed options and the value of the ISE Max SPY Index itself could cause investor confusion? Please explain why or why not.

We have discussed in our Comment Letters that there is nothing novel about an options product having differing intraday and settlement values. This will not cause investor confusion. The most striking example of this involves CBOE's flagship index product, SPX Options, and its corresponding special opening quotation ("SOQ"). According to CBOE's product specifications, the SPX settlement value is calculated using the opening prices of the index components, regardless of when they open. If a component stock does not open for trading, the prior day's closing value is used. By using different inputs, there is a very high likelihood of the SPX settlement value differing from the current SPX index level. In fact, this "close-but-different" approach that CBOE uses would appear to be more confusing to investors than the concerns CBOE has raised regarding our Max SPY Options. However, we believe that investors understand these differences, and that there is no confusion in either case.

First, there is uncertainty as to when the SOQ settlement value for SPX will be distributed. The settlement value is not published until all stocks in the index have opened or until the end of the day. The result is that the settlement value can be published within seconds, minutes, or hours after the equity markets have opened, or even after the equity markets have closed. Yet it does not appear that investors find this confusing.

Second, even if the SOQ settlement value for SPX were published within minutes of the opening price of SPX, the values will almost always differ, sometimes greatly. The opening price of SPX is based on the current prices of the index components at the opening of trading, regardless of whether the components have opened. On the other hand, the SOQ settlement value uses the opening prices of component stocks sometime after the SPX opening print. This can result in a settlement value that is greatly different from the SPX opening value because individual component stocks can exhibit significant price movements (*i.e.*, "gaps") during that time. This could result in investor confusion where the settlement value is unexpectedly different from the opening index value, especially if they are both published around the same time. But yet again, there is no evidence of investor confusion.

Finally, the SOQ process could be viewed as misleading because it can result in a settlement value that is not actionable when compared to the current index level. Investors have little, if any, chance to transact at the settlement value price, whereas the current index level reflects recent prices of the index component stocks. Investors apparently do not find this confusing either.

The Exchange has reviewed all SOQ values over the prior five years. Every instance of the daily SOQ calculation has diverged from the opening price of SPX. Yet the popularity of SPX Options make clear that investors do not find the SOQ confusing. In this regard, we note that the Chicago Mercantile Exchange has on its website a detailed explanation of how the SOQ works.⁸ We plan to do exactly the same in explaining the Max SPY settlement value.

The Max SPY Index's proposed settlement value process is not analogous to CBOE's SOQ process, and thus eliminates potential confusion. First, the Max SPY Index's proposed settlement value will always be established after the primary markets close on the last trading day of the expiring contract. This avoids the potential confusion of having two index values published at the same time. Second, there will be little uncertainty as to when ISE's settlement value will be published because the inputs are based, in part, on the closing prices of the Trust's portfolio stocks and because the settlement value will have to be submitted to OCC before 6:30PM ET.

Finally, NYSEArca publishes an intraday indicative value for the Trust every 15 seconds, which is an estimate of the Trust's NAV. The value is available publically through most major market data vendors and can be used as an additional reference for investors on expiration day. According to the NYSEArca website: "The Intraday Indicative Value is designed to give investors a sense of the relationship between a basket of securities that are representative of those owned in the ETF and the share price of the ETF on an intraday basis."⁹ Given the history of the SOQ and our proposed disclosure for our product, we see no reason investors would find the straight-forward manner in which we will calculate the settlement value of Max SPY Options confusing.

Only CBOE is Confused by Differences Between the Calculation of the Settlement Value of the Options and the Value of the Max SPY Itself

If commenters believe that the differences between the calculation of the settlement value of the proposed options and the value of the ISE Max SPY Index itself could cause investor confusion, what are commenters' views as to whether the steps that ISE has proposed to take to provide investors with information about the product would be sufficient to mitigate such concerns?

⁸ <http://www.cmegroup.com/education/files/Understanding-the-SOQ-2011-11-04.pdf>.

⁹ <http://www.amex.com/etf/Glossary/Gloss.htm>.

In developing this product we consulted with industry participants to develop a simple, understandable, and transparent process for establishing the settlement value. Since it is our obvious goal to create a successful product, it would be against our interests to create any level of confusion. The only party that appears confused as to the settlement value of the Max SPY Options is the CBOE. The only two letters the Commission has received from commentators not directly involved in this proceeding have voiced strong support for our proposal.¹⁰ Indeed, the KOR Letter specifically stated that “there will be no investor confusion over the calculation methodology” and that “KOR does not believe that there will be any confusion as the ISE plans ample disclosure publicly available on their website.”¹¹

As stated above, CBOE’s claim of confusion is not genuine. Rather, it is simply an attempt to delay our introduction of this new product. We have detailed in both of our comment letters the steps we will be taking to provide investors with information on the product. This includes providing a full description of Max SPY Options in our rules, devoting a page of our website to this product, and providing all necessary information in the Options Disclosure Document (“ODD”).

There is No Potential for Investor Confusion By Characterizing These Options as to What They Are: Options on the Max SPY Index

Do commenters believe that the characterization of the proposed options as options on the “ISE Max SPY Index” would have the potential to cause investor confusion? If so, why? If not, why not? If so, what are commenters’ views on whether any potential confusion would be sufficiently mitigated by the steps that ISE has proposed to take to provide investors with information about the product?

ISE believes that investors will know and understand what they are buying and selling: options on the Max SPY Index. ISE has clearly described and defined the Max SPY Index in both the Max SPY™ Filing and subsequent Comment Letters. As noted, it is our goal to offer investors a popular, transparent product. In order to achieve that goal, it is to our advantage to provide as much information to the investing public as possible. While we remain open to all suggestions as to how to provide investors with relevant information on this product, ISE will, at a minimum, do the following:

¹⁰ Letters dated April 2, 2012, from Janet McGinness, Executive Vice President and General Counsel, NYSE Euronext, and August 6, 2012, from Christopher Nagy, President, KOR Trading LLC (“KOR Letter”).

¹¹ KOR Letter at 2 and 3. Moreover, there is an extremely vibrant market in Trust shares. Thus, normal market arbitrage activities will help ensure that there are no material deviations in the value of the Trust shares versus the net asset value of the trust.

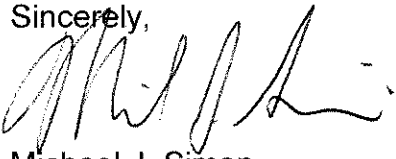
- ISE will work with OCC to amend the ODD to provide a clear and unambiguous description of the product, as well as any unique risks associated with it. This will include, among other things, a clear description of the fact that the Max SPY Index contains only one component and that there is a separate settlement value for the Max SPY Index.
- ISE will display the contract specifications for Max SPY Options on its website.
- ISE will create a special website page devoted exclusively to this product, which will describe in plain English all of the terms of this product, including how the index is calculated and how it is settled.
- ISE will follow the same marketing process it follows for all of its other new products, which process is designed to promote awareness and a clear understanding of the product.
- ISE will post on its website, and distribute to members, a notice any time the value of the Trust shares deviates materially – either in the amount of the deviation or the time of the deviation – from the Max SPY Index price.

As far as we are aware, no developer of a new product has committed to provide investors with this much information in this many formats. The ODD is the primary educational product for such complicated instruments as: options on variability indexes; options on strategy-based indexes; options on dividend indexes; options on debt instruments (including price-based options, index-based options, and yield-based options); and credit-default options. In contrast, we are proposing a simple product, an option on an index with one underlying instrument, a widely-traded ETF. We believe that the ODD, along with our other proposed methods of disclosure, will ensure that investors have all the information they need to understand the product.

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For the reasons set forth above, we respectfully request that the Commission approve the proposed rule filing. If you have any additional questions, or if we can be of further assistance in this matter, please do not hesitate to contact us.

Sincerely,



Michael J. Simon
Secretary