International Securities Exchange.

October 29, 2013

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-2013-42

Dear Ms. Murphy:

We submit this letter in response to the comments submitted to the U.S. Securities and Exchange Commission ("Commission") by the Chicago Board Options Exchange, Incorporated ("CBOE")[1] on the above-referenced rule filing in which the International Securities Exchange, LLC ("ISE") proposes to list and trade options on the Nations VolDex index ("VolDex index").[2]

The CBOE Letter states that the VolDex index is not a broad-based index. CBOE notes that because the VolDex index will be based on two options prices at specific times that it should not be designated as a broad-based index. The classification of the VolDex index as a broad-based index is significant for the purpose of determining the applicable position limits, exercise limits and margin requirements, the latter of which we further discuss below.

We find CBOE's position curious since, in fact, CBOE itself sought to designate its proprietary volatility index product, the CBOE Volatility Index® (VIX®) as a broad-based index when it filed to list and trade options on the VIX.[3] Indeed, nowhere in the VIX Filing did CBOE represent that the VIX contains a minimum number of components. CBOE only stated that certain SPX options with "non-zero bid prices" are used as the components in the index to compute the index level, without stating how many series are used or the minimum number of series that would be used. We apply the same logic to the VolDex index that the CBOE employed in the VIX Filing.

[1] Letter from Edward T. Tilly, Chief Executive Officer, CBOE, dated August 23, 2013 ("CBOE Letter").
[2] See Securities Exchange Act Release No. 70059 (July 29, 2013), 78 FR 47041 (August 2, 2013) (Notice for ISE-2013-42).
[3] See Securities Exchange Act Release No. 49563 (April 14, 2004), 69 FR 21589 (April 21, 2004) (Order Granting Approval of SR-CBOE-2003-40) ("VIX Filing").

As with VIX, ISE believes that designating the VolDex index as a broad-based index should not be based simply on the number of components that the index contains, a position that the Commission has previously taken when it approved the VIX Filing. For volatility indexes, such as the VolDex index and the VIX, the more appropriate reference for designation as a broad-based index is to look at the economic exposure that the underlying reference seeks to provide. According to the CBOE, the VIX is a key measure of market expectations of near-term volatility conveyed by options on the S&P 500® Index ("SPX"). The VolDex index provides a corresponding economic exposure in that it measures changes in implied volatility of the SPDR® S&P® ETF ("SPY"), which is a broad-based ETF based on the price and yield of the stocks held in the SPY portfolio. Thus, SPY options, like SPX options, provide investors with economic exposure to a broad market.

It was on the basis of "looking through" to the exposure provided by the underlying reference that the Commission designated VIX as a broad-based index. Given the equivalent breadth of SPY, upon whose pricing the VolDex index is based, ISE now appropriately seeks the same designation for the VolDex index so that it may compete on a level playing field with an existing product by providing investors with an important trading and hedging instrument.

Designating the VolDex index as a broad-based index by looking through to the economic exposure it provides is consistent with the position CBOE took in the VIX Filing. CBOE's justification for giving VIX broad-based index treatment was that the SPX options underlying the VIX are themselves securities and are based on an index that provides exposure to a broad number of underlying securities. ISE asks for a broad-based designation for the VolDex index on an analogous basis: SPY options underlying the VolDex index are themselves securities, and the extensive stock holdings of the SPY fund provides broad market exposure.

The CBOE letter also states that the position limits for the VolDex index are inappropriate and that adopting a position limit regime similar to that of NASDAQ's Alpha Index options is more appropriate.

We believe this is simply CBOE's attempt to throw sand in the gears of competition. NASDAQ's Alpha Index options are based on indexes that intend to measure relative performance of a single equity security (such as AAPL, MSFT or IBM) or another ETF (such as TLT) to the SPY ETF. It is obvious that pairing a single equity security that has a stated position limit against an equity security with no position limit (i.e., SPY) does not imply that options on the combined new index should have zero position limits. VolDex index options are not analogous to Alpha Index options. We believe the position limits for the VolDex index, as proposed, are appropriate once the Commission designates the VolDex index as a broad-based index.

With respect to margin requirements[4] for options on the VoldDex index, the Exchange intends to apply the same margin requirements that are applicable to VIX options on the CBOE. VIX options are subject to the same margin requirements as options on other major broad-based indexes traded on CBOE, such as SPX, Nasdaq-100 Index ("NDX"), and Russell 2000 Index ("RUT").[5] The Exchange believes designating the VolDex index as a broad-based index should also require that they are afforded the same margin treatment as that afforded to VIX, NDX and RUT options to avoid investor confusion.

The Exchange notes that although CBOE has margin rules designed for Individual Stock or ETF Based Volatility Index options,[6] ISE does not believe applying those margin rules to VolDex index options is appropriate. ISE believes that CBOE's margin rules for Individual Stock or ETF Based Volatility Index options is understandable for individual stocks that exhibit volatility which is much higher than that exhibited by the SPY ETF, or when considering ETFs that are much less liquid than the SPY ETF. Indeed, "looking through" to the economic exposure provided by the SPY ETF should equally apply in determining margin requirements for VolDex options considering the SPY ETF's vast liquidity and low volatility relative to other underlying securities, in particular those Individual Stock or ETF Based Volatility Indexes found in CBOE Rule 24.1(bb).[7]

ISE believes that when the VolDex index is appropriately designated as a broad-based index, applying the margin treatment for Individual Stock or ETF Based Volatility Index options to VolDex index options would simply create unnecessary investor confusion. Further, the margin treatment proposed for Individual Stock or ETF Based Volatility Index options extends to just a handful of products that measure the volatility of a single security or a that of a narrow-based index, neither of which accurately describes the VolDex index.

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[4] ISE members are bound by the initial and maintenance margin requirements of either the CBOE of the New York Stock Exchange. See ISE Rule 1202(a).
[5] See VIX Product Specifications at http://www.cboe.com/products/indexopts/vixoptions_spec.aspx. See also NDX Product Specifications as http://www.cboe.com/Products/indexopts/ndx_spec.aspx and RUT Product Specifications as http://www.cboe.com/Products/indexopts/rut_spec.aspx.
[6] See CBOE Rule 12.3, Margin Requirements.
[7] The annualized historical volatility of the SPY ETF for September 27, 2013 was 10.25%, while the volatility for AAPL shares was over 3 times that amount (31.54%) and the volatility for GDX was 5 times that amount (50.61%). These volatility figures are based on Bloomberg 30-day annualized data.

For the reasons set forth above, ISE respectfully requests that the Commission approve the VolDex index 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 and General Counsel