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November 23, 2010

Elizabeth Murphy
Secretary
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549

Re: SR-NYSEArca-2010-90, SR-NYSEArca-2010-80 and SR-NYSEAmex-2010-087; Internalization in the Listed-option Markets

Dear Ms. Murphy:

I. Introduction

LiquidPoint, LLC ("LiquidPoint")[1] appreciates the opportunity to comment on the recent rule filings referenced above and their effect upon internalization in the listed-option markets.

The referenced rule filings and others (including SR-ISE-2010-73 the Qualified Contingent Cross or "QCC") have the effect of allowing exchange members to internalize the execution of client orders. LiquidPoint strongly feels that the Commission should not

[1] LiquidPoint, a wholly owned subsidiary of BNY ConvergEx Group, LLC, specializes in providing derivatives technology and execution solutions for U.S. listed options traders, including institutional customers and other broker-dealers. LiquidPoint provides electronic direct market access to every U.S. options exchange, as well as advanced trading capabilities that include order execution, order management, order routing and optimization, quality assurance review, and a variety of reporting and books and records capabilities. ConvergEx Group is a premier provider of investment technology solutions and global agency brokerage services to institutional clients worldwide. Our three key business lines – investment technologies, liquidity and execution management, and intermediary and clearing services – specialize in providing a full array of leading technologies and an integrated platform of performance driven, global trading capabilities supported by a culture of extraordinary client service.

approve rules for listed-option exchanges that subvert transparent, effective price discovery at the exchanges, as it will do significant harm to the integrity of the listed-option markets. In particular, LiquidPoint wishes to highlight:

- Approvals endorse far-reaching changes to the options industry principles requiring the exposure of all orders to market interaction in order to enhance price discovery and competition.
- These rules allow for increased internalization of listed option executions that is fundamentally detrimental to the quote-driven nature of options markets.
- The value of internalization is not as significant to investors using listed-options as to equity investors.

The listed-option exchanges have traditionally required that their registered liquidity providers be involved in the price discovery process for each transaction to be reported to the Option Clearing Corporation ("OCC"). This approach guarantees exposure of orders to numerous trading interests in the light of the broader marketplace.

There is a trend however, to accommodate liquidity without this broad market exposure through processes that leave price discovery in the dark and allows for order execution internalization. These processes that avoid the light, both proposed and operational, include the "final quote" in open outcry trading (NYSEArca-2010-90), trading against reserve orders (NYSEArca-2010-80 & NYSEAmex-2010-87) and the Qualified Contingent Cross.

The NYSE Arca rule proposal (NYSEArca-2010-90) regarding the manual, floor-based execution (i.e. open outcry) of buy and sell interest represented by the same member avoids critical disclosures to the marketplace. The proposed rule change would allow a Floor Broker to request, without revealing the size of the orders or if any proprietary interest, a final quote for a cross from the Trading Crowd. The Floor Broker may then cross the orders at a price above the highest bid, or below the lowest offer; executing both orders in entirety – though it must be between the National Best Bid/Offer and satisfy any resting orders on that exchange. This request to have liquidity providers make a market without the same information as the representing member, only provides notice that an order has been internalized, should a trade occur – not price discovery.

Two other recent rule proposals (NYSEArca-2010-80 & NYSEAmex-2010-87) allow trading against reserve orders that is another technique for internalizing clients' orders. The reserve order is an exchange order type that displays a portion of a larger order in the public quote with the balance (or "reserve" portion) undisplayed but available for execution if marketable. To prevent disenfranchising the exchanges' registered liquidity providers, rules require one second exposure of an order to the market before the entity that entered the original order may bring contra-party interest to execute against this resting order. However, these proposals (and those of other exchanges) have ruled that once any portion of a reserve order has been exposed for one second, the entire order quantity is considered fully exposed. This allows an exchange member to enter a large reserve order and designate only a very small portion for display. Once the displayed portion has been exposed for one second, contra-party interest for the full, much larger quantity can execute against the resting "fully exposed" order. Since only the member that entered the large reserve order knows the full size, this member is able to effectively internalize the vast majority of the original reserve order. This approach has gained enough popularity that the ISE (who first proposed this notion in rule proposal ISE 2009-61) has automated the process. For example, a member with an agency order to buy 5000 options that it wishes to sell for its proprietary account could enter a buy and sell simultaneously that creates a reserve order to buy 5000 contracts that only displays 1 contract and a sell of 5000 at the given price with an automatic one second delay.

In contrast, certain exchanges also provide automated auctions to provide price discovery when members have both buy and sell interests to represent in the marketplace. These auctions bring transparency and competition by including obligated liquidity providers. If upon conclusion of the auction, contra-party interest at the negotiated price exceeds the available quantity, the member initiating the auction is still rewarded with a guaranteed percentage – generally 40%. These auctions provide an artful compromise among competing interests that maintains the incentive to quote. It is quotes across ***all*** series that allows the continuous creation of liquidity, for the risk mitigation provided by listed-options to investors.

The Commission needs to determine if the internalization of listed-option orders benefits investors with increased liquidity and/or more favorable prices. This determination must not be made based upon experience in the equity markets. A particular equity security has a finite number of units available at any given time. The open interest for the numerous listed-option series overlaying the particular security expands and contracts as investors' risk mitigation needs change. This process can occur because there are obligated liquidity providers quoting all the related "term insurance policies" provided by the option contract. It is the relationship between the various option contracts that provides the incentive to quote – option market makers want their quote to be taken because the risks can be effectively managed using related options. This elegant and effective risk transference is being hobbled by the reduced incentive to quote all option series when listed-option exchanges encourage internalization through various means (as cited above) or when orders are incented at the expense of quotes. The equity market structure gives market participants flexibility in finding the finite liquidity of equity securities. The listed-option market is not constrained by finite liquidity when there is incentive to quote all series.

If there is a concern that disenfranchising those liquidity providers with regulatory obligations to provide two-sided quotes will reduce liquidity in all but the most active listed-option series, then the orders should not be incented at the expense of quotes. If there is a belief that transparency and competition provide the most effective price discovery, which is what the industry has consistently heard from the Securities and Exchange Commission, then the existing, *inclusive* exchange automated auctions deserve regulatory support – not internalization.

The "final quote" rule proposal (NYSEArca-2010-90), the reserve order display rules (ISE 2009-61, NYSEArca-2010-80 & NYSEAmex-2010-87) and the Qualified Contingent Cross (ISE 2010-73) have the common theme of allowing an exchange member to internalize listed-option orders without full exposure to the marketplace. LiquidPoint respectfully submits that internalization without full exposure should not be part of the listed-option market structure, because it prevents the contributions of obligated quoting market participants, which in turn completely undercuts the liquidity needed for the risk mitigation role played by options. Rather, the existing exchange automated auctions should be encouraged because they provide the transparency vital to price discovery and the quoting of all option series, while allowing investors to benefit from the additional liquidity that initiates these auctions.

Sincerely,

AJ Saliba

Anthony J. Saliba
Chief Executive Officer
LiquidPoint, LLC