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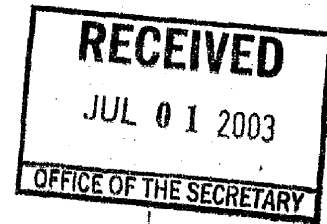
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June 30, 2003

Via Facsimile and Federal Express

Mr. Jonathan G. Katz
Secretary
U.S. Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549



Re: Securities Exchange Act Release No. 47849

Dear Mr. Katz:

87-11-03

The Chicago Board Options Exchange, Incorporated ("CBOE") hereby submits its comments on the Nasdaq Stock Market, Inc. ("Nasdaq") petition concerning the regulation of Nasdaq-listed securities.

Background

As stated in the captioned release, Nasdaq is requesting that the Securities and Exchange Commission (the "Commission"): require all markets trading Nasdaq securities to establish uniform trading rules to ensure equal surveillance and enforcement of those rules, order that the exchanges' collective costs of regulation (of trading in Nasdaq securities) be aggregated and deducted from the market data revenue collected pursuant to the UTP Plan, and identify exchanges that do not have "sufficient" rules, order audit trails, surveillance, and examination programs and prohibit such exchanges from continuing to trade Nasdaq securities. The Nasdaq petition also suggests that a single regulator (the **NASD**) be responsible for a majority of the regulation of trading in Nasdaq securities, and that the single regulator should be funded by all markets trading Nasdaq securities. Finally, in the release, the Commission requests comments on whether the regulatory concerns raised by Nasdaq for Nasdaq-listed securities apply to the marketplaces for exchange-listed stocks and options.

Generally

CBOE is commenting because, as an options exchange with a significant regulatory presence, CBOE is particularly concerned **about** any potential implications for the listed options regulatory structure arising out of the Nasdaq petition. CBOE believes that many of the concerns identified **by** Nasdaq could also apply to the trading of any multiply-listed securities, including listed options. CBOE believes, for example, that there is unequal regulation by markets that trade listed options, just as Nasdaq believes there is unequal regulation by the markets that trade Nasdaq securities. In some cases, CBOE believes that this inequality **of** regulation can create a

competitive disadvantage to those exchanges that regulate their marketplace more rigorously. However, unlike Nasdaq, CBOE supports expanding the use of existing tools and enhancing self-regulatory organization ("SRO") and Commission coordination to strengthen surveillance and to achieve more uniform regulation of the securities markets. While for some types of conduct (e.g. insider trading), it may make sense to have a single entity conduct surveillance for the entire options industry, we do not believe that a mandated across-the-board single regulator is the answer to achieving consistent regulation.

Uniform Enforcement of Rules

In the release, the Commission requests feedback related to Nasdaq's position on the need for uniform trading rules and surveillance in the markets that trade Nasdaq securities. While CBOE does not trade **Nasdaq** securities and is not commenting on the regulatory structure for Nasdaq securities, **we** agree that it is possible for markets that trade the same products to regulate in manners that are not entirely consistent. In the options markets, in certain areas some exchanges are likely to surveil for certain conduct differently than other exchanges and there appears to be a disparity in the manner in which some similar and/or identical rules are enforced. Clearly, inconsistent regulation is troublesome and ultimately works to the **detriment of** investors and fair competition. However, we believe uniform regulation can be achieved without the imposition of a single self-regulator, and in a way that can preserve the competitive and creative benefits brought on by multiple regulators.

CBOE is not suggesting that self-regulation **by the** options exchanges be identical in all **areas**. The market models of the options exchanges differ in a number of respects. Consequently, the oversight provided by each exchange necessarily will be tailored to the particular design of its market. Nevertheless, there are many rules that are common to **all** options exchanges irrespective of market model as well as SEC rules that apply across all options exchanges. It is in these areas that the **lack** of uniform and consistent surveillance and enforcement across options exchanges pose significant problems.

CBOE feels that the Commission can play a significant role in achieving greater uniform SRO regulation for common rules by providing interpretive guidance prior to the implementation of new Commission rules, as well as by establishing guiding principles on a variety of areas that affect all SROs. Additionally, there should be enhanced coordination of SRO regulatory efforts through the Intermarket Surveillance Group ("ISG") and through the use of Commission Rule 17d-2 agreements.

The Commission is uniquely positioned to facilitate uniform regulation among SROs. To a great extent, the Commission's Division of Market Regulation and Office of Compliance Inspections and Examinations ("OCIE") already do this. However, increased proactive guidance by these offices, apart from the inspection process, would greatly benefit efforts to effect consistent and uniform regulation. CBOE believes it would be valuable for the Commission staff to conduct forums with regulatory personnel from the various SROs that would be affected **by** a new Commission rule or interpretation in advance of implementation of such rule or interpretation to clarify how the Commission expects the rules to be enforced. Indeed, it would greatly benefit the ISG participants **if** a segment of every ISG meeting involved Commission staff

providing or restating the Commission's views on the manner in which a particular rule should be enforced.¹

CBOE also supports greater use of Staff Legal Bulletins by the Commission's Division of Market Regulation. These bulletins are useful in providing guidance in matters that are subject to interpretation- something that is important and necessary in order to achieve satisfactory uniform regulation. By way of example, Commission guidance on the enforcement of the Firm Quote Rule at the time the options exchanges were adopting the rule would have been greatly beneficial and may have helped avoid significant confusion over the application of the rule to the options markets. Similarly, Commission guidance on uniform enforcement of rules relating to the internalization of options orders is needed now and would benefit the marketplace and avoid regulatory arbitrage.

With sufficient guidance from the Commission on how to regulate common exchange rules **and** the federal securities laws, the **ISG** would be ideally situated to help reinforce uniform regulation by SROs. The primary purpose of the ISG is to enhance coordination of regulatory efforts by markets trading securities. The ISG provides a useful forum for discussion of regulatory issues and trends and, more important, for the sharing of information. Its members communicate on a daily basis and it has proven invaluable in facilitating numerous intermarket regulatory efforts. Nevertheless, CBOE acknowledges that the ISG's efforts could be improved to allow SROs to attain more consistent and uniform regulation of laws and rules that **apply** across markets. By agreeing that greater regulatory uniformity is a worthy objective, the ISG participants, with Commission guidance, can focus more on achieving consistent enforcement of common rules.

To the extent it makes sense for an SRO to transfer regulatory obligations for certain functions to another SRO, Rule 17d-2 allows any two or more SROs to allocate regulatory responsibility (upon declaration by the Commission that the allocation plan is effective). Consequently, SROs can, and do, assign certain portions of their regulatory responsibilities to other SROs for consideration. Thus, if an exchange has an established history of effective surveillance in a particular area, other SROs may seek to establish a 17d-2 agreement to allocate responsibility for that area to that exchange. CBOE believes SROs should utilize Rule 17d-2 agreements with more frequency, and would welcome Commission encouragement in this regard.

Single Market Regulator

Nasdaq asserts that the establishment **of** a single market regulator with regulatory oversight over all markets trading Nasdaq securities is the best solution for correcting inconsistencies in the regulation of trading in Nasdaq securities. CBOE does not believe that a mandated single self-regulator across all markets is the only approach to address inconsistencies in regulation.

In general, CBOE feels that the establishment of an all-encompassing single regulator model for trading in multiply listed securities is not prudent. The Commission is already responsible for regulating the various securities markets and the adoption of a single regulator would only add another layer of regulatory bureaucracy and effectively create a second Commission. Further, we do not believe it is in the best interest of fair competition to create a

¹ Although the release notes that the Commission does not have direct oversight of the ISG, CBOE believes that by virtue of the fact that the Commission is the regulatory body for all of the ISG members, the Commission has significant authority over ISG activities.

regulatory monopoly. To deny capable SROs from regulating their own markets seems to be directly in conflict with the entire concept of self-regulation. More important, **if** the stated goal of Nasdaq is to achieve uniform regulation, CBOE notes that the suggestions in this letter would achieve this goal without abandoning the concept of self-regulation and the significant unique regulatory perspectives resident at each and every SRO. Accordingly, CBOE does not support the concept of a mandated across-the-board single market self-regulator with regulatory authority over all SROs.

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CBOE would be glad to discuss these comments with individual members of the Commission and **its** staff. Any questions regarding this letter should be directed to Timothy Thompson, Senior **Vice** President - Market Regulation, at 312-786-7135 or the undersigned.

Sincerely,



Edward J. Joyce

cc: Chairman William Donaldson
Commissioner Paul **S.** Atkins
Commissioner Roel C. Campos
Commissioner Cynthia **A.** Glassman
Commissioner Harvey J. Goldschmid
Annette Nazareth, Director, Division of Market Regulation
Lori Richards, Director, Office of Compliance Inspections and Examinations