CBOE
CHICAGO BOARD OPTIONS EXCHANGE

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April 7, 2010

Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-0609

Re: SR-ISE-2009-35 (Qualified Contingent Cross)

Dear Ms. Murphy:

The Chicago Board Options Exchange, Incorporated ("CBOE") submits this letter in connection with the captioned matter in which the Commission's Division of Trading and Markets approved, pursuant to delegated authority, an International Securities Exchange ("ISE") rule filing to adopt a Qualified Contingent Cross mechanism ("QCC"). On March 17, 2010, the Commission placed in the public comment file a March 1, 2010 memorandum prepared by the Division of Risk, Strategy, and Financial Innovation ("RiskFin") concerning certain option execution data and analysis. The Commission also extended the period of time for submitting statements in support of or in opposition to the Division of Trading and Market's delegated action in the QCC matter until April 7, 2010. This letter sets forth CBOE's views on the RiskFin memorandum.

The stated purpose of RiskFin's review was "to determine if large-sized orders are broken up more frequently on an electronic exchange as compared to certain floor-based exchanges". The study concluded that the "analysis did not confirm ISE's contention that large orders are broken-up less frequently on floor-based exchanges, though certain data did provide support for ISE's position".

While we appreciate that the study's conclusions are favorable to CBOE's position, we want to make clear that we believe the study was unnecessary. The pages and pages of submissions from numerous parties in this matter can really be distilled into a simple policy question for the Commission to decide: *is it appropriate and beneficial to investors for an options exchange to allow members to cross orders (including orders that might not otherwise have priority), without any exposure to the marketplace or any semblance of transparency?*

If the answer is "yes", then such an answer would seem to be in conflict with many Commission initiatives in recent months and years that seek to bolster fairness and transparency in the markets. If the answer is "no", then ISE should be required to expose these orders just as CBOE and the other options exchanges do, and ISE should not get special treatment.

ISE has claimed that it needs QCC to compete with floor-based exchanges. Despite ISE's incessant complaining about trading floors, the fact remains that when orders are traded in open outcry they are exposed to the market. *Every single time* an order is represented in a trading crowd, it is exposed and it is possible for other market participants to participate on a trade and provide price improvement. The ISE QCC proposal does not, and cannot, offer any exposure or transparency. The trading floor equivalent of the ISE proposal would allow floor brokers to cross orders from their booths, offices, or homes without ever venturing into a trading crowd and without exposure of any sort to any other market participants.

ISE's references to trading floors are an attempt to distract from the real policy issue that is at hand. This has been ISE's strategy from the start when it proposed the QCC mechanism as some sort of order type that was necessary to comply with the pending new intermarket linkage. The overwhelming majority of that rule filing was spent discussing the new linkage, which was curious given the fact that QCC has absolutely nothing to do with order protection or trade-throughs and the new intermarket linkage continues to have the same exemption for stock-option transactions that existed under the old linkage plan. In subsequent submissions to the Commission, ISE has attacked execution statistics offered by CBOE as well as perceived trade-throughs on CBOE and Phlx. Indeed, ISE has discussed just about everything except the merits of QCC and whether QCC benefits investors.

We will not restate all that we have discussed in our previous submissions, instead we refer you to our Petition where we explain why approval of QCC was inappropriate. We also refer you to our subsequent submissions where we, among other things, list the numerous existing methods to execute stock-option orders (both electronically and manually) and we explain how QCC provides no benefit to investors or the options marketplace generally, but unfairly provides plenty of benefits to internalizers and those seeking to facilitate internalizers such as Ballista Securities, an options ATS partially owned by ISE.

Below we provide more specific feedback on the RiskFin study and offer additional observations relating to QCC:

- The study, which attempts to verify if orders get "broken-up" more on floor-based exchanges than electronic exchanges, only analyzes data from three out of seven options exchanges that were in operation at the time of the study: CBOE, ISE, and Phlx. We do not understand why it makes sense to limit the study to three exchanges. Limiting the study to ISE and the two exchanges ISE complains about might suit ISE (ironically, in this case it did not), but it does not seem like a complete way to assess order executions in the options markets.

- The study assumes that what can be extracted from COATS data as "multiple executions" actually represents multiple contras. That is an incorrect assumption.

The same contra party can trade against an order via multiple executions (e.g. at different price points).

- We are very troubled by the fact that the study created a third size tier. QCC applies to orders greater than 500 contracts, yet the study analyzed data under 500 contracts, from 500 to 1999 contracts, and 2000 contracts and higher. We fail to see what that third tier has to do with QCC. We hope it is not an attempt to create a fallback threshold where QCC trades would be allowed. Unless there is information on this point not available to CBOE, it seems the use of 2000 contracts as a new tier was a purely arbitrary endeavor and it is entirely possible that an analysis of orders greater than 5000 or 7000 or any number could yield different results. The percentages provided in the study indicate that for trades of 2000 contracts and greater, 74% of trades on CBOE involved "multiple executions", and for 88% of trades on ISE involved "multiple executions".[1] That 14 point difference is inconsequential compared to the 70+ point difference that would exist if QCC were adopted for orders greater than 2000 contracts because ISE's 88% would drop towards zero.

- The study appears to include 1-lot orders, which obviously cannot get broken-up.

- Footnote 4 of RiskFin's memorandum references an email from ISE to SEC staff regarding statistics submitted by ISE in connection with this matter. That email and those statistics were never provided to CBOE. Are there other submissions from ISE that have not been made part of the public record?

- Throughout this process, ISE has attacked the quality of order exposure on trading floors. This is despite the fact that we have refuted those assertions with meaningful data, and despite the fact that monthly statistics posted on the website of Ballista Securities highlight the "exchange step-in" rate for orders routed through Ballista and executed on ISE as lower than trading floor "step-in" rates.

  After our initial Statement in Opposition, we noticed that Ballista ceased updating its website with monthly statistic reports (perhaps to avoid disseminating information that was harmful to the QCC position of its owner ISE). However, right before we submitted our January 20, 2010 letter responding to ISE's December 16, 2009 letter (which was never sent to us) we noticed that Ballista finally resumed posting these statistics. As we mentioned in our December 16, 2009 letter, those newer Ballista statistics were not helpful to the ISE QCC position. We now have observed that Ballista is posting monthly statistics again, but is no longer including information related to "exchange step-in". If ISE is so harmed by a lack of QCC, then why do all of these monthly reports by Ballista through December 2009 show the opposite, and why has Ballista ceased disclosing information related to exchange step-in since January 2010?

[1] We note that in the 500 to 1999 contract tier, CBOE and ISE had identical percentages.

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The simple policy question before the Commission is whether crossing without any exposure is appropriate and beneficial for investors, and whether such unfettered crossing would adversely impact the options markets. Despite the substantial rhetoric on this matter, it is obvious that QCC does not benefit investors. Moreover, it creates a disincentive to competitively quote and dampens transparency in the options markets. Even if ISE's hollow allegations about losing business were relevant to the central policy question in this matter, there is no evidence that ISE is at any sort of disadvantage when it comes to large order interaction.

We remain hopeful that the Commission will disapprove the QCC filing and we appreciate the Commission's consideration of our views in this matter. If you have any questions regarding this letter or if you would like additional information, please contact me at 312-786-7310 or Angelo Evangelou at 312-786-7464.

Sincerely,

Edward J Joyce

cc: The Honorable Mary L. Schapiro, Chairman
The Honorable Luis A. Aguilar, Commissioner
The Honorable Kathleen L. Casey, Commissioner
The Honorable Troy A. Paredes, Commissioner
The Honorable Elisse B. Walter, Commissioner
Robert W. Cook, Division of Trading and Markets
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