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April 7, 2010

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-2009-35

Dear Ms. Murphy:

The International Securities Exchange, LLC ("ISE") appreciates the opportunity to comment on the March 1, 2010 Division of Risk, Strategy, and Financial Innovation ("Division") memorandum on the ISE's Qualified Contingent Cross ("QCC") proposal.[1] The Memorandum discusses certain data collected from the Consolidated Options Audit Trail System, or "COATS," regarding the break-up of QCC-eligible orders and the competitive implications of our QCC proposal. The Memorandum concludes that the Division's "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."

Before discussing the specific analysis in the Memorandum, we believe it is important to place the analysis in context.[2] In this regard, the QCC is our attempt to establish a competitive process for members to effect large options trades that are tied to stock in an automated environment. As we stated in our March 1st letter:

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[1] Memorandum dated March 1, 2010 from the Division to Files entitled "ISE Qualified Contingent Cross Order Proposal (SR-ISE-2009-35)" (the "Memorandum").

[2] In this letter we do not recite the entire history of the QCC proceeding or all of our stated positions on this matter. Rather, in addition to our initial rule proposal and the Commission order approving that proposal, we refer the Commission to the following previous ISE submissions on the matter: Letter from Michael J. Simon, Secretary and General Counsel, ISE, dated August 20, 2009; Brief in Support of International Securities Exchange, LLC's Motion to Lift the Commission Rule 431(e) Automatic Stay of Delegated Action Triggered by Chicago Board Options Exchange, Incorporated's Notice of Intention to petition for Review, September 11, 2009; Reply Brief in Support of International Securities Exchange, LLC's Motion to Lift the Commission Rule 431(e) Automatic Stay of Delegated Action Triggered by Chicago Board Options Exchange, Incorporated's Notice of Intention to petition for Review, September 22, 2009; Letter from Michael J. Simon, Secretary and General Counsel, ISE, dated December 16, 2009 (December 16th Letter); and Letter from Michael J. Simon, Secretary and General Counsel, ISE, dated March 1, 2010 ("March 1st Letter").

If a member seeks liquidity through the participation of other traders on a floor, the floors can accommodate such trading. On the other hand, if a member has arranged a large tied-to-stock trade and seeks to effect the cross without intervention, the member similarly can seek to cross that trade on a floor that is willing to accommodate the member. We only seek the ability to compete in this floor-dominated market, offering automation and efficiency.

As this makes clear, participants in the options market may seek supplemental liquidity for large trades, and thus may actively seek markets where other participants are available to join in large trades. Thus, we would expect there to be a significant proportion of large trades in all markets in which there are multiple participants. However, market participants also spend significant time and effort to arrange large trades, in which case they likely will seek to execute cleanly in a cross, with little if any opportunity for break-up. The core of the ISE's position is that floor-based exchanges now have the ability to offer both trading environments, while the all-electronic ISE does not have a viable crossing mechanism to compete with de facto floor-based crossing procedures.

With this background, we believe that the Division's analysis strongly supports our case that the QCC is an appropriate and necessary competitive tool for the ISE. The most critical statistic in determining whether exchange members can effect a trade without being broken up is how often large trades are executed in a single execution. For the largest trades (2,000 or more contracts), the analysis shows that only 12 percent of such trades are executed without break-up on the ISE, while the percentages on the Chicago Board Options Exchange ("CBOE") and NASDAQ OMX PHLX ("Phlx") are more than twice as high (26 percent and 29 percent, respectively).

As striking as these numbers are, we believe this significantly underestimates the degree to which large orders are executed without break-up on floor-based exchanges compared to electronic exchanges like the ISE. The Division notes that its sample data included many trade types that would not be eligible for our QCC. For example, it included all executions, and not just crosses. And while QCCs will be limited to orders tied to stock, the Division's sample was not so limited. Of most importance, the Division's data was not limited to equity option orders, but also included index option orders.

As we explained in our December 16th letter, the most heavily traded of the CBOE's index options are listed exclusively on the CBOE, where there are strict limits on electronic trading. Thus, a significant amount of trading in these options is effected in a floor-based open outcry trading environment, where there is more likely to be member interaction with incoming orders. In these cases, there are no markets competing with the CBOE, and thus options market participants have no choice but to bring their orders in these products to the CBOE.

The CBOE's exclusive products are very actively-traded, and the inclusion of this trading in the data distorts the extent to which there is "break-up" of large crosses in the CBOE's hybrid market. Indeed, the top three exclusive products on the CBOE (the SPX, VIX and OEX) represented over 22 percent of the CBOE's entire volume in the first quarter of 2010, with the SPX alone accounting for over 16 percent of the CBOE's volume in that period.

The CBOE also has confirmed that the inclusion of trading in these heavily-traded exclusive products seriously inflates the degree of crowd participation in large order executions. The CBOE initially claimed that 48 percent of orders of 500 or more contracts involved more than one contra-party, that is, received trading crowd participation.[3] We challenged that statistic in our December 16th letter, noting that it appeared to include index option trades, which we believed would inflate the amount of crowd participation. The CBOE responded that when it limited its analysis to equity options in multiply-listed instruments, only 21.27 percent of the large orders involved trading crowd participation, less than half the amount claimed in its initial letter.[4]

Thus, we believe that the Division's analysis showing that 26 percent of CBOE's large orders (2,000 or more contracts) were executed without break-up significantly understates the ability of CBOE members to effect clean crosses in QCC-eligible instruments. When the CBOE limited its analysis to the relevant instruments, its claimed interaction rate for large orders – 48 percent – shrunk by more than half, to under 22 percent. It is thus likely that excluding index options from the Division's analysis would significantly increase the number of CBOE's large orders that were executed without break-up.[5]

With respect to the effects on competition of our inability to offer the QCC , the Division notes that we submitted statistics to the Commission showing a decrease in on our market share in large trades.[6] The Memorandum's discussion of competition focuses on the number of orders executed in single and multiple executions before and after the start date for the new distributive linkage, when we lost the "block exemption" for large trades. While the Division's numbers speak for themselves, it is critical for the Commission to appreciate the impact on our market share in these orders due to our inability to implement the QCC. With the implementation of the new linkage and the lack of a competitive

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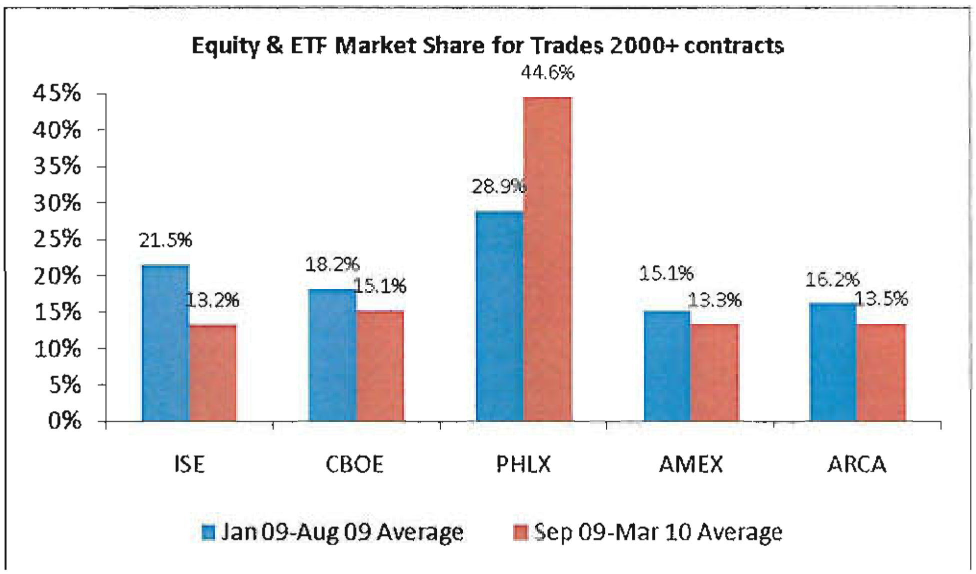
[3] Statement of Chicago Board Options Exchange, Incorporated in Opposition to the Division of Trading and Market's Approval of Rule Under Delegated Authority dated December 3, 2009.
[4] Letter dated January 20, 2010 from Angelo Evangelou, Assistant General Counsel, CBOE, to Elizabeth Murphy, Secretary, Commission.
[5] We do not have a floor-based open outcry system, and we have little if any volume in our exclusively-traded products. Thus, no adjustment to the Division's ISE statistics is necessary.
[6] E-Mail dated September 30, 2009, from Michael J. Simon, Secretary and General Counsel, ISE, to Elizabeth K. King, Associate Director, Division of Trading and Markets, Commission (September Statistics).

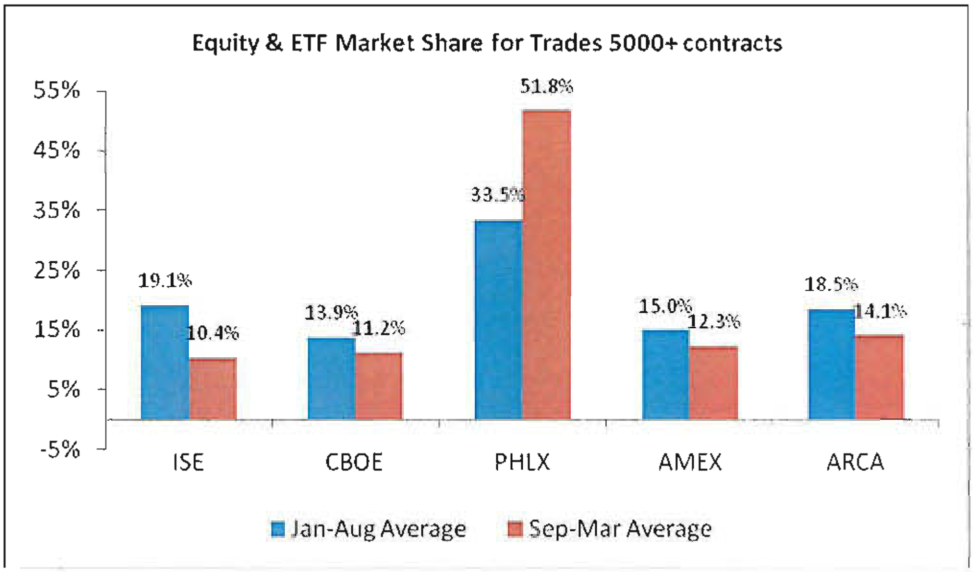
crossing mechanism on the ISE, members simply executed more of their large trades elsewhere.

We have updated the September Statistics, and these revised numbers starkly indicate how our inability to offer the QCC has harmed our competitive posture. We compare the eight months before distributive linkage (January to August 2009) to the seven months after the new linkage began and we lost the ability to provide a competitive crossing vehicle (September 2009 to March 2010). Again, while the Division's data indicate that the nature of the large executions that remain on the ISE has not changed significantly, it is clear that members are not bringing their large crossing trades to the ISE in the absence of the QCC. Specifically:

- For trades of 2000 contracts or more in equity and ETF options (thus not including the CBOE's exclusive index options), ISE had a 21.5 percent market share prior to distributive linkage and only a 13.2 percent market share thereafter. Phlx was the major beneficiary, going from 28.9 percent to 44.6 percent. No other exchange had a meaningful change in market share between these two periods. We show this graphically below:



- For the largest trades, those of 5000 contracts or more in equity and ETF options, the difference was even more striking. ISE's market share decreased from 19.1 percent to 10.4 percent, again with the Phlx being the major benefactor, going from 33.5 percent to 51.8 percent, with the other exchanges showing minor decreases in market share. Again, we show this graphically as:



The statistics show how the advent of distributive linkage, coupled with the loss of the block exemption and our inability to offer the QCC, crippled our crossing business. The ISE was unique as the only fully-electronic exchange that had established a viable crossing business that was able to compete with the floor-based exchanges. That business has evaporated. We will be able to compete in this arena only if the Commission endorses the Division of Trading and Market's approval of the QCC.

We again thank the Commission for the opportunity to comment on the Memorandum and on the QCC proposal generally. We respectfully request that the Commission affirm the Division of Trading and Market's approval of the QCC. If the Commission or staff have any further questions on this matter, please do not hesitate to contact us.

Sincerely,

Michael J. Simon,
Secretary

cc: Hon. Mary L. Schapiro, Chairman
Hon. Luis A. Aguilar, Commissioner
Hon. Kathleen L. Casey, Commissioner
Hon. Troy A. Paredes, Commissioner
Hon. Elisse B. Walter, Commissioner
Robert Cook, Director, Division of Trading and Markets
James Brigagliano, Deputy Director, Division of Trading and Markets
Elizabeth King, Associate Director, Division of Trading and Markets