May 10, 2000

Mr. Jonathan G. Katz
Secretary
Securities and Exchange Commission
450 Fifth Street NW
Washington, DC 20549

Re: File No. 4-430; Release No. 34-42685; Decimal Pricing

Dear Mr. Katz:

The International Securities Exchange LLC ("ISE") appreciates the opportunity to comment on alternative ways to implement decimal pricing. As we previously stated in a letter to Chairman Levitt dated March 21, 2000:

> We believe that it is critical for the industry to convert to decimal pricing in an efficient manner. To achieve this goal, we believe that the transition should be uniform for all securities, and that the transition process should be as short as possible. The longer that securities trade in two different structures, the greater the potential there is for investor confusion.

Our position remains unchanged. We continue to believe that having a prolonged period in which securities trade in two pricing regimens will confuse investors and will produce inefficiencies in the market. It also would create an environment prone to operational errors. We urge the Commission to resist pressure to accelerate the decimalization timetable. We believe that the Commission should oversee a process that results in full decimal pricing at the earliest reasonable time in a manner that protects investors and the nation's capital markets.

Decimalization Timetable

We understand that the National Association of Securities Dealers, Inc. ("NASD") has established March 31, 2001 as the earliest date by which it can be ready for full decimal pricing. Considering that the NASD is one of this country's primary markets for underlying stocks, and assuming that the NASD's date is firm, we believe that the Commission and the industry must consider the date that the NASD will be prepared for decimal trading, currently March 31st, as the end-point for full decimalization. Thus, we believe that the Commission's focus should be to set a timetable that works backwards from that date to establish both a testing schedule and the date to begin the phase-in process.

For the reasons discussed at length in our March 21, 2000 letter and summarized below, we believe that the phase-in process should be as short as possible, and certainly no longer than three months. Thus, we suggest that the move to decimal pricing begin in early January, 2001 and end on the date the industry is fully prepared for decimal trading. The industry should use the period of September through December of 2000 to finalize its testing and other preparations for decimalization, including investor education. Extending the phase-in period for more than three months would raise serious investor protection concerns and would unnecessarily jeopardize the health and vitality of our capital markets.

Concerns Regarding an Extended "Pilot"

The Commission requests comment on two alternative decimal phase-in proposals. The first proposal, "Dual Pricing" would have all exchange-listed securities trade in decimals by September 4, 2000, with all Nasdaq securities trading in decimals by March 31, 2001. The second proposal, "Decimals Pilot," would begin (rather than end) the phase-in period for exchange-listed stocks (and options on such stocks) on September 4, 2000, again ending with full decimalization for all securities on March 31, 2001. The Commission asks a number of questions regarding these proposals. It also seeks comment on: the "feasibility" of these approaches; possible alternatives to these approaches; and the risk of investor confusion in taking these approaches.

We see little difference in the Dual Pricing and Decimals Pilot proposals. Of most importance, both would result in a phase-in period of seven months. We assume that both approaches may be "feasible" from a technical standpoint. As for the ISE, we will be capable of trading any and all securities in decimals on September 4, 2000, assuming that there is adequate time to test our systems internally and for all market participants to test on an industry-wide basis.[1] However, we believe that the Commission is focusing on the wrong issue when it asks whether these approaches are "feasible." We believe that accelerating the decimalization process to commence trading in some or all exchange-listed securities by September 4th (and thus mandating a seven-month phase-in process), while perhaps "feasible," is neither reasonable nor practical.

There are a number of reasons that argue strongly in favor of limiting any phase-in period:

- Investor Confusion: During any phase-in period, investors will need to enter orders in two different pricing structures. It is unrealistic to expect investors to be expert in the trading markets of every security, and to enter orders in the

[1] As we noted in our March 21st letter, we will begin operations on May 26, 2000. As we move towards our launch, we are focusing all our attention and resources on that effort. Post launch, we will take the necessary steps to join the industry testing process. While our trading system is "decimal ready," we are in the process of installing and testing the software necessary for us to phase in decimal trading while continuing to trade some securities in fractions.

appropriate increments. Thus, there will be no way to avoid at least some limit orders entered in the wrong pricing structure during the phase-in process. However, by keeping this period as short as possible, it will be possible to limit the time period during which such mispricing will happen.

- Dual Functionality: During the phase-in period, exchanges, broker-dealers and other market participants will need to support two pricing structures. Any period in which the industry must engage in such extraordinary procedures increases workloads and produces an environment prone to error. While there should be strong policy reasons first to create such an environment, there should be even stronger policy reasons if such a period is to be extended longer than absolutely necessary. As discussed below, there are no policy reasons dictating an extended phase-in period.

- Effect on the Options Markets: If listed securities trade in decimals and Nasdaq securities trade in fractions, the options markets will be facing a choice between two alternatives that appear equally unattractive: We can move to full decimalization in all our options, including options on Nasdaq securities, which will continue to trade in fractions. However, this would lead to investor confusion as market participants would, for seven months, need to correlate stock prices trading in fractions and option prices on the same stock that are trading in decimals.[2] Alternatively, we could continue to trade options on Nasdaq securities in fractions, while we trade options on listed securities in decimals. This would result in seven months of investor confusion and dual functionality concerns discussed above.

- Capacity: The members of the investment community are working as expeditiously as possible to increase their systems' capacity to address the general growth in trading and quotation volume, as well as to handle the anticipated further growth that will flow from decimalization. Extending the pilot by having it start seven months before the targeted end-date will only exacerbate the capacity concerns inherent in decimal trading.

We recognize the need to phase-in decimal trading. However, for the reasons discussed, the Commission's goal should be to establish the shortest possible period to accomplish the conversion. Given the March 31st "anchor," the sole focus of the phase-in period should be to reach that date in as expeditious and safe a manner as possible.

The only basis for a possible extended phase-in period appears to be Congressional interest in having decimalization begin for exchange-listed securities on September 4th. While we appreciate the legislative concern that decimal pricing not be unduly delayed, the reality of the situation is that the NASD will not be ready for full decimalization until some time next year. The

[2] Similarly, we could continue to trade all options in fractions, while listed stocks trade in decimals. However, this would give rise to the same concerns, while further delaying the full implementation of decimal pricing.

Commission's focus should not be on September 4, 2000, when only a few securities would be trading in decimals. Rather, the Commission should focus on the date that the NASD will be fully prepared for decimal trading, and ensuring that the industry successfully accomplishes the move to full decimal pricing by that date with as few problems and dislocations as possible.

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We urge the Commission to move cautiously in this area and not to take action that would confuse investors or jeopardize our markets. We believe that phasing in decimal pricing from during the first quarter of 2001 is the most prudent and reasonable course for the Commission to pursue.

We again thank the Commission for the opportunity to comment on this issue. If you have any questions on our letter, or if we can be of further assistance, please do not hesitate to call us.

Yours very truly,

Michael J. Simon
Senior Vice President and General Counsel