



January 19, 2000

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

Re: Options Linkage Plan

Dear Mr. Katz:

In Release No. 34-42029 (the "Release"), the Commission ordered the four options exchanges to act jointly with the International Securities Exchange LLC ("ISE") to discuss, develop and submit for Commission approval a plan to link the options markets. The ISE is pleased to comply with the requirements of the Release by enclosing the attached plan (the "Linkage Plan") for the Commission's consideration. Because the Commission has not yet formally approved the ISE's application for registration as a national securities exchange, we are not yet able to execute the Linkage Plan. However, it is our intention to sign the document immediately upon our registration. It is our understanding that the Linkage Plan we are submitting is identical to the plan being submitted by the American Stock Exchange LLC and the Chicago Board Options Exchange, Inc.

Over the last 90 days we have worked diligently and in good faith with the four other exchanges in an attempt to submit a single plan acceptable to all the parties. We have achieved consensus on almost all outstanding issues, and the five participants generally have agreed to establish an options market linkage that is far superior to any linkage currently in existence. Specifically, we propose linking the automated trading systems of the exchanges and providing for unparalleled access and efficiency between markets. The linkage also will provide for "trade-through" protection for customers. Based on presentations that various vendors made to the linkage development group, we believe that the linkage can be implemented at a reasonable cost and in a timely manner. We strongly believe that the Linkage Plan we are submitting fully complies with all the requirements the Commission imposed in the Release.

The one primary issue that remains outstanding deals not with the linkage itself, but with a related market structure issue: whether there should be mandatory routing of customer orders based on strict "price-time" priority. In a letter dated December 10, 1999 to Chairman Levitt, we explained in great detail why we did not believe mandatory price-time routing was appropriate. After submitting that letter, we have continued to work with the other exchanges in an

attempt to forge a compromise on this issue. Our goal has been to provide for some level of "centrality" in the market to protect customer orders, while maintaining a competitive market structure that benefits investors, and encourages the entry of new exchanges, such as the ISE, into the market.

Unfortunately, in the time allotted to us we have not yet been able to resolve this issue and agree to a compromise. However, in the last few days we believe that seeds to a possible compromise have been planted. Specifically, we propose that the Commission authorize continued negotiations on a Linkage Plan containing the following provisions:

- Member firms could continue to route orders to their exchange(s) of choice;
- If an exchange is quoting at the best bid or offer, as the case may be, when it receives that order (regardless of which exchange first quoted at that price), the receiving exchange would be free to execute that order;
- If the exchange that receives the order is not quoting at the best bid or offer when it receives the order, a market maker on that exchange still could "step up" to match the inside market for the customer; however, if a market maker does "step up," it would need to provide, on a complaint basis, specified protection to customer limit orders on the books of the other markets that are at the best bid or offer; and
- If the exchange that receives the order determines not to "step up," but to route an order through the linkage representing the customer order, such linkage order would be routed based on price-time priority.

We understand that this proposal raises numerous questions and issues that the exchanges would need to resolve. For example, we believe that this provision should apply only to market maker "step up" situations, and should not apply to crosses or any other trade in which an incoming order is executed against customer orders on the receiving exchange. We also recognize that we will have to define the specific level of customer protection available for "matching trades," and the complaint mechanism that would govern that process. However, we believe that if all the exchanges can agree to these concepts, we will be able to work through the procedures to implement the concepts in a relatively short time frame.

Again, we appreciate the opportunity to submit the Linkage Plan to the Commission. We believe that the exchanges have made great progress in working toward a Linkage Plan and we believe that the plan we have submitted is

a significant step toward the adoption of a uniform plan. We look forward to the opportunity to continuing our efforts in this area.

Sincerely,

David Krell
President and Chief Executive Officer

Attachment

cc: The Honorable Arthur Levitt
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Robert L.D. Colby, Esq.

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