CITADEL

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Mr. Jonathan G. Katz
Secretary
United States Securities
and Exchange Commission
100 F Street, NE
Washington, DC 20549-9303

Re: File Number SR-CBOE-2005-63

Dear Mr. Katz:

Citadel Derivatives Group LLC ("Citadel Derivatives")[1] submits this letter in response to the proposed rule amendments by the Chicago Board Options Exchange ("CBOE") contained in File Number SR-CBOE-2005-63 (the "Proposed Rule Amendments"). Citadel Derivatives is one of the most active listed options market makers in the United States and is a market maker on five of the six options exchanges, including the CBOE. The CBOE intends to amend its rules applicable to the nullification and adjustment of equity options transactions. We oppose the Proposed Rule Amendments because they would force CBOE market makers retroactively to trade during the opening rotation at prices that they were not quoting and at which they did not want to trade, thereby punishing them for having provided the best prices available on the CBOE. We believe that such a result is contrary to just and equitable principles of trade and will reduce competition by providing a disincentive to quote aggressively at the opening of trading. Accordingly, we believe the Proposed Rule Amendments are inappropriate and inconsistent with Section 6(b)(5) of the Securities Exchange Act.

The traditional price protections associated with the Intermarket Linkage Plan and trade-through rules do not apply to transactions during the opening rotation. *See, e.g.,* CBOE Rule 6.83(b)(5)-(6). This lack of protection results from two factors. First, an exchange that is not yet open cannot send a linkage order to an exchange that is open. Second, one exchange cannot know what another exchange is quoting at a point in time at which the other exchange is just then establishing its initial prices for the day and has not yet disseminated quotes. As a result, there is a risk that orders received during or prior to the opening rotation may be filled at worse prices than they might receive at another exchange or after the opening rotation is complete.

[1] Citadel Derivatives is an affiliate of Citadel Investment Group, L.L.C. which, with its affiliates, operates one of the world's largest alternative investment firms. On an average day, Citadel affiliates account for approximately 3% of the daily volume on the NYSE and Nasdaq.

By the Proposed Rule Amendments, the CBOE seeks to protect customers from that risk by reallocating it to CBOE market makers, at least where the price differential is sufficiently large to constitute an "obvious error" (even though no error is involved at all). Specifically, where a CBOE market maker's quote trades against a customer order during the opening rotation and that price turns out to be inferior to a price that existed at another exchange, the CBOE Market Maker must accept a price adjustment to match the price of the leading competing exchange, up to the lesser of the number of contracts quoted by the CBOE market maker and the competing exchange. The effect of this rule will be to punish the CBOE market maker who had been quoting the best price on the CBOE by forcing him to trade at a price at which he did not want to trade in the first place and at which he was not even mistakenly quoting. Such a punitive measure is inappropriate given that the market maker has done nothing wrong. In addition, it will be counterproductive because it will encourage CBOE market makers to quote as widely as possible during opening rotations. This will help them avoid trading during that period and therefore avoid being forced to accept transactions at prices they did not quote.

The Proposed Rule Amendments also create irrational distinctions between those customer orders that will get the benefit of adjustment and those that will not. Under the proposal, customers whose trades were far enough away from the leading competing exchange to be the numerical equivalent of obvious errors will have their trades adjusted but customers whose trades were just inside obvious error parameters will not. Given that no error is involved at all, it is inappropriate to rely on obvious error standards and thereby create an irrational distinction among similarly situated customers.

The most appropriate way to protect customers from the risk inherent in the opening rotation is for the CBOE itself to pay the cost of making customers whole. That would be an appropriate recognition that the problem is caused by the CBOE and current market structure rather than by the individual actions of CBOE market makers.

For the foregoing reasons, we urge the Commission to reject the Proposed Rule Amendments.

Thank you for your consideration.

Sincerely,

Matthew Hinerfeld
Managing Director and
Deputy General Counsel
Citadel Investment Group, L.L.C.
On behalf of Citadel Derivatives Group LLC