

GROUP ONE

T R A D I N G

September 26, 2022

Ms. Vanessa A. Countryman
Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, D.C. 20549-1090

Re: Exemption for Certain Exchange Members (No. S7-05-15)

Dear Ms. Countryman,

Group One Trading, LP (“Group One”) respectfully submits this letter to express its views on specific aspects of the filing of the U.S. Securities and Exchange Commission’s (“SEC” or “Commission”) re-proposed amendments (the “Proposal”) to a rule under the Securities Exchange Act of 1934 (“Act” or “Exchange Act”) that exempts certain registered brokers or dealers from membership in a registered national securities association (“Association”). Group One is a proprietary option market making firm that is currently a member of all sixteen registered U.S. option exchanges and relies on the “proprietary trading exclusion” under Rule 15b9-1 to remain exempt from Association membership. As applied to option market makers, Group One believes that: 1) the re-proposed amendments are too broad, in that they fail to distinguish between firms that conduct customer business and those that do not, 2) market making firms are already heavily regulated and surveilled, and Association membership does not provide FINRA with any trading data that is not already available and used by them, and 3) without any benefit, the proposal is left to be judged on its costs, which are significant.

Requiring Association Membership Subjects Option Market Making Firms To Rule Sets Unrelated To Their Business

Group One and other option market making firms do not have customers, but the Proposal would require these firms to join FINRA and become subject to many rules that are wholly unrelated to their business. For example, FINRA has entire sections of its rulebook dedicated to Communications with the Public, Suitability Obligations, Transactions with Customers, and the Permissible Use of Customers’ Securities. Option market making firms engage in none of these activities. Group One believes that the

individual exchanges and their SROs are best positioned to conduct regulatory oversight of trading activity on the individual option exchanges. The exchanges have specifically tailored their rules to the business conducted on each exchange and are in the best position to identify behavior inconsistent with those rules. The Proposal states, “Importantly, FINRA has the expertise regarding off-exchange trading, but under these RSAs, for non-FINRA members that trade off-exchange and are members of different exchanges, FINRA applies the rules of the different exchanges using the exchanges’ interpretations of those rules. This can result in different interpretations and FINRA registration would promote consistent interpretations and efficiencies in enforcement and regulation with respect to this growing part of the market.” As it applies to option market makers specifically, Group One respectfully disagrees and believes that, rather than promoting consistent interpretations, FINRA registration would only add an additional interpretation and there is no guarantee of consistency given that the FINRA rule book is in large part designed for the oversight of broker-dealers conducting a customer business.

Additionally, much of the Proposal focuses on TRACE reporting for non-FINRA members that trade U.S. Treasury Securities. Group One does not transact in this market and cannot comment on the value of this enhanced trade reporting; however, assuming that enhanced trade reporting is appropriate, Group One believes that there are more narrowly tailored approaches to address this reporting gap that do not involve forcing FINRA registration on firms conducting activity unrelated to U.S. Treasury Securities trading.

FINRA Already Has Full Access to All Trade Data, and Currently Conducts Surveillance Based On That Data

All of Group One’s trading activity takes place either on an exchange where the firm is itself a member or, as in the case for its equity trading activity conducted to hedge its option market making activity, through another broker-dealer that is a FINRA member. The FINRA member executing equity trades on behalf of Group One may do so on an equity exchange or via an off-exchange mechanism, but those transactions are all reported and visible to FINRA through the member performing the execution, and FINRA has jurisdiction over that member and that activity. In fact, it is acknowledged throughout the Proposal that FINRA already has a full view into all of the trading activity conducted by Group One and other option market makers through the Consolidated Audit Trail. Furthermore, all such trading activity—including stock trading that occurs on a venue where the Firm is not a member—is already subject to surveillance in the context of audits and regulatory examinations of option market making firms, as the examiners appropriately see the stock activity as inextricably intertwined with option activity. Group One fields many questions on its stock trading activity in a typical regulatory exam, covering such stock-specific topics as Regulation SHO short sale regulations and obligations, anticipatory hedging, market access controls related to equity activity, and procedures related to the implementation and supervision of algorithmic equity trading activity.

The Costs of Mandated Association Membership Do Not Outweigh the Benefits

Group One believes that the costs of direct, FINRA-membership-based jurisdiction far outweigh the benefits as they pertain to the trading activity of option market makers. As the Proposal acknowledges,

the FINRA membership process is cumbersome and expensive. The membership process takes approximately six months and, once approved, a new member is subject to high fees – the Proposal estimates that the median ongoing cost for non-FINRA member firms would be \$2,742,664. Section 3(f) of the Exchange Act requires the Commission, whenever it engages in rulemaking pursuant to the Exchange Act, to consider whether an action is necessary or appropriate in the public interest and whether the action would promote efficiency, competition, and capital formation. Group One believes that an estimated cost of \$2,742,664 represents a significant barrier to entry in an industry that has already seen declining numbers of market making firms, and is therefore neither necessary nor appropriate in the public interest and that the approval of a proposal imposing those costs would not promote efficiency, competition, and capital formation--particularly in light of the fact that the Proposal imposes a set of rules primarily designed for broker-dealers that handle customer business, and the Proposal does not provide FINRA with any trading related data to which they do not already have access for option market making firms.

Option Market Making Firms Currently Pay Their Fair Share of Regulatory Fees

Finally, Group One and other option market making firms are already subject to fees that are used to fund regulatory programs. Option market making firms are responsible for paying a regulatory fee to whichever SRO is their designated examining authority (“DEA”). Group One’s DEA is Cboe and the firm is therefore subject to Cboe’s “DPM’s and Firm Designated Examining Authority Fee” at a rate of \$0.60 per \$1,000 of gross revenue. Other SROs have similar fees in place.

The Proposal, in notes 30 and 228, acknowledges that FINRA serves as the DEA for the majority of member firms but does not specifically address whether or not FINRA would become the DEA for new members that would join as a result of the Proposal.

In the event that the Commission does pursue and adopt the Proposal, Group One requests that the Commission either re-assess the current fees as they apply to option market making firms or ensure that FINRA serves as the DEA for these new members to ensure these firms are not paying duplicative regulatory fees.

Conclusion

Group One supports the Commission’s efforts to enhance transparency across the securities market; however, Group One does not believe that the Proposal furthers that objective. The option markets generally, and option market makers in particular, are already well regulated and FINRA has a full view directly into all option market maker trading activity through the CAT. It is acknowledged throughout the Proposal that FINRA already has the necessary surveillance capability and that enforcement for improper activity is not a problem, even going so far as to highlight in footnote 140:

See, e.g., Statement of Robert W. Cook, President and CEO, FINRA, “Equity Market Surveillance Today and the Path Ahead” (Sep. 20, 2017), available at <https://www.finra.org/media-center/speechestestimony/equity-market-surveillance-today-and-path-ahead> (stating that FINRA makes referrals to the Commission or other authorities if the target of an investigation

is beyond the collective jurisdiction of FINRA and the exchanges, and that in a prior year FINRA's market regulation department made over 500 referrals to the Commission on behalf of FINRA and its exchange clients related to potential abusive trading strategies or other rule violations). FINRA also could refer such a matter to an exchange where the firm is a member or, as discussed above, potentially address the matter through an RSA if covered by the terms of the RSA."

For the reasons detailed above, Group One does not believe that any regulatory benefit will be achieved by the Proposal, and unfortunately it has clear costs to be borne by option market making firms—firms that are already shrinking in number. Group One urges the Commission to preserve the current exemptions from registration that have provided option market participants with the flexibility to evolve and ensure that the U.S. option market is among the most liquid and competitive markets in the world.

Sincerely,

A handwritten signature in black ink that reads "John Kinahan". The signature is written in a cursive, flowing style.

John Kinahan
Chief Executive Officer
Group One Trading, LP