



December 2, 2013

Elizabeth M. Murphy
Secretary
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, D.C. 20549-0609

Dear Ms. Murphy:

Group One Trading, L.P., ("Group One") would like to thank the Securities and Exchange Commission ("SEC") for providing us the opportunity to comment on the NASDAQ OMX PHLX ("PHLX") proposal to amend Rules 1064 and 1080 and make specific the interpretation of the number and size of counterparties to a qualified contingent cross order. Group One is one of the largest, privately held equity options market makers in the United States. Group One makes markets in over 2,600 individual issues, provides a significant amount of liquidity on every major US based equity options exchange and has a presence on all four exchange floors. Group One appreciates the effort by PHLX to provide clarity on Rules 1064 and 1080 and encourages all exchanges to continue to provide as much clarity as possible; however, Group One believes that the proposed interpretation related to qualified contingent cross ("QCC") orders is inconsistent with the original QCC rule filing and that the new interpretation expands the reach of QCC well beyond the original intent.

To begin with, Group One feels that QCC as originally proposed is inconsistent with the goals of an efficient marketplace in that it reduces both transparency and price discovery. By granting a facilitating broker the ability to cross an order without market exposure, it effectively eliminates the requirement that a broker provide best execution to the customer. There are orders that trade electronically through QCC every day that Group One, or some other liquidity provider, would have price improved if given the opportunity. This isn't conjecture; this is based on actual observations made on a daily basis. Every day brokers represent orders on the trading floors and request quotes from the market makers in the trading crowd. If the market makers in the crowd respond with a larger size than the broker is willing to give up or with a better price than the broker anticipated, then the broker frequently leaves the crowd without trading and a short time later the order prints electronically through QCC. These orders are not trading at the best possible price available in the marketplace. This is simple supply and demand. If there is too much interest from the market makers in the crowd, then it stands to reason that the broker should attempt to price improve the order. Instead, this simple supply and demand dynamic is ignored and the order is traded electronically through QCC, a mechanism which does not offer the ability for price improvement, and one in which the competing market makers, whom the broker knew had an

interest in participating, are unable to even respond. The proposed expansion in the PHLX rule filing only stands to exacerbate that concern.

As with SEC rulemaking¹, Group One believes that high-quality economic analysis is also an essential part of SRO rulemaking. In this case, PHLX's proposed expanded interpretation of QCC will affect the efficiency and competition in the market place, but PHLX has not yet provided an analysis of the economic impact of this proposal. At this point, the expanded interpretation of QCC is not only contrary to the intent of the original proposal, but the exchange has also failed to provide a justification for this new, expanded interpretation. Group One believes that this new interpretation will be detrimental to the marketplace because it allows self-interested parties to circumvent their best execution duties which harms customers by allowing those self-interested parties to trade at prices that are inferior to what they would be in an open and competitive marketplace.

In the rule filing, PHLX makes it clear that this new interpretation is not what was originally contemplated by pointing to the original definition in the International Securities Exchange ("ISE") comment letter and referencing the "seemingly clear statement requiring a single order of at least 1,000 contracts on each side of a QCC Order." That seemingly clear statement by Michael Simon in the ISE comment letter says, "Nothing could be clearer in our proposed rule: proposed ISE Rule 715(j) defines QCC as 'an order to buy or sell at least 1,000 contracts that is identified as being part of a qualified contingent trade....' This means what it says, that there must be an order to buy or sell 1,000 contracts that is part of a QCC – not two 500 orders, not two 500 legs, not anything but an order to buy or sell at least 1,000 contracts."² In 2010, when the merits of the original QCC proposal were being debated, several comments, Group One's included³, contained the argument that granting approval of QCC would push the industry in the direction of more and more frictionless crosses. If market participants are now allowed to combine five separate 200 lots orders to meet the "order to buy or sell at least 1,000 contracts" requirement, the scope of the rule has been radically expanded. Group One's contention that the initial approval of this rule would just be the tip of the iceberg is no longer hypothetical as we are now debating the merits of expanding the reach of QCC and allowing more frictionless crosses.

In addition, this expanded interpretation now opens up QCC to the solicited market and allows brokers to cross trades without exposure. QCC was originally both designed and pitched as a way to help facilitate the execution of institutional orders, but this expanded interpretation will reach far beyond the original design. While Group One believes that there is an inherent conflict of interest with a broker facilitated order that is crossed without market exposure, that exposure is at least somewhat limited by the fact that the facilitating party should have the best interest of the customer in mind when pricing the order. However this new interpretation now adds an additional conflict of interest by opening up QCC to solicited orders that are crossed without market exposure. In a solicited cross scenario, the broker receives the order and goes to outside parties to find pricing. A solicited order does not have the same level of price protection because the economics for the representing broker change dramatically if

¹ http://www.sec.gov/divisions/riskfin/rsfi_guidance_econ_analy_secrulemaking.pdf

² <http://www.sec.gov/comments/sr-ise-2010-73/ise201073-9.pdf>

³ <http://www.sec.gov/comments/sr-ise-2010-73/ise201073-5.pdf>

a non-solicited market maker wants to participate on or price improve the order. If a broker can solicit counterparties who will all pay a commission to participate on the trade, then the executing broker has very little incentive to expose the order to market makers that will potentially price improve the order because, in doing so, the market makers may end up participating on some or all of the trade and the broker does not collect commission on that portion. As an example, a broker may collect more commission from Parties A and B than other counterparties, so the broker gets paid more by going directly to Parties A and B and having those two parties interact with the entire order rather than showing the transaction to a wider audience. Parties A and B have no fiduciary responsibility to the initiating customer, and the broker is now conflicted by the fact that he or she will collect significantly more if Parties A and B trade the entire order. If Parties A and B are willing to pay \$2.00 per contract to the broker, and the next best participant pays \$0.50, the broker will collect four times as much if Parties A and B are willing to trade the entire order which the broker is representing. Under this expanded interpretation, the broker is incentivized to just fill the order and cross it as quickly as possible to collect commission on both sides without seeking out price improvement for the customer. This dynamic clearly fails the economic analysis test as multiple mechanisms already exist whereby a broker can make this trade and expose it to the marketplace.

Group One continues to support the efforts by the exchanges to increase the clarity of their rules; but, for all of the reasons set forth above, Group One is opposed to this proposal set forth by PHLX and believes that the expanded interpretation of QCC will have a negative impact on both customer execution quality and the market place as a whole.

Group One appreciates the opportunity to comment on this rule proposal and we are happy to discuss these views further with the Commission and its staff.

Respectfully submitted,

/s/ Benjamin Londergan
Benjamin Londergan
Chief Executive Officer
Group One Trading, L.P.