July 10, 2017

VIA E-MAIL

Mr. Brent J. Fields
Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549-1090

Re: **Notice of Filing of Amendment No. 2 to a Proposed Rule Change to Adopt Rules for an Open-Outcry Trading Floor, Rel. 34-80720 (SR-BOX-2016-48)**

Dear Mr. Fields:

CTC Trading Group, LLC ("CTC")[1] appreciates the opportunity to comment in response to the third version of the BOX Options Exchange LLC ("BOX") filing (the "Proposal") to adopt rules for an open-outcry trading floor.[2] We note that BOX has amended its filing to partially remediate certain specific concerns raised in our prior letters. However, as we stated in our original letter of December 31, 2016,[3] our objections to certain details of the open-outcry process described in Proposal, while important, remain secondary to our broader concerns regarding the investor protection issues raised by opening *any* new open-outcry trading floor—and these concerns, which are significant, remain unaddressed by BOX. Below, we briefly reiterate these points, and raise other substantial concerns with the Proposal.

1. Broad Concerns About the Launch of Any New Multi-List Options Floor Remain Unaddressed

In the latest version of the Proposal, BOX introduces a new requirement that no Floor Broker may execute a trade unless a Market Maker is present. While this is a small step in the right direction, as we have consistently stated, a *robust* Market Maker population must be required before any trading floor is permitted to begin operating *de novo*. The presence of a single human Market Maker anywhere on the trading floor—which would suffice to satisfy BOX's newly-proposed, mild requirement—is a far cry from meeting this standard. We again respectfully suggest that the simplest and most effective method for ensuring robust Market Maker participation would be to eliminate the need to staff a new physical

[1] CTC was established in January 1998. CTC's business focus is trading in the capacity of an options market maker across asset classes and geographies, and it is currently a registered broker-dealer and a member of the Chicago Board Options Exchange, the C2 Options Exchange, NYSE Arca Options, NYSE Amex Options (NYSE MKT), the International Securities Exchange, and Nasdaq Phlx.

[2] *See* Rel. 34-80720 (SR-BOX-2016-48).

[3] *See* two prior comment letters from CTC available at https://www.sec.gov/comments/sr-box-2016-48/box201648-1458314-130203.pdf and https://www.sec.gov/comments/sr-box-2016-48/box201648-1701572-149973.pdf

trading floor entirely—given electronic trading technology readily available in 2017, **opening a new open-outcry trading floor requiring in-person participation to provide price improvement serves only to impose an artificial barrier to entry for market participants** through the need to hire, train, and support additional personnel and floor-specific technology at substantial cost. (Instead, if BOX truly wishes to open an open-outcry trading floor in the hopes of providing *additional* liquidity, it could simply require all open-outcry orders to undergo a final, brief electronic exposure period—along the lines of price improvement auction functionality already available on BOX's electronic market today—to provide an opportunity for further price improvement from firms not represented in person.)[4]

Further, in the event that one or more market making firms choose not to staff the new floor (which would almost certainly be the case, given the small volumes traded on BOX), a liquidity vacuum will be created, facilitating "venue shopping." This practice occurs when institutions seeking to internalize order flow in multiply-listed options (or who solicit a chosen counterparty for a customer's order in exchange for commission payment)—and therefore prefer not to trade with third-party Market Makers who might provide price improvement—seek the venue with the lowest rate of Market Maker participation, and choose to execute trades there whenever possible, thereby depriving investors of the opportunity for superior executions. We respectfully submit that **by approving any new trading floor, the SEC would be tacitly supporting the exacerbation of this "venue shopping" practice as a means to circumvent order exposure and price improvement opportunities.** (Of course, investors will never know the extent of the resulting indirect costs, since they won't be told how much better their executions *might* have been if not for the existence of an underpopulated new trading floor.)

As we have pointed out previously, there are no substantive benefits to offset this investor harm. Additional trading floors for multiply-listed options create no new liquidity—only a small number of firms currently staff all four existing options floors, and we are aware of no new entrants planning to enter the space. As a result, opening a new floor will only spread existing liquidity providers more thinly, and force current market participants to incur greater costs to provide liquidity with the same capital base. CTC, for example, would certainly not provide more total liquidity by staffing another floor—instead, the average amount of liquidity available per trading floor would necessarily be reduced, as BOX's decision to open a trading floor in no way increases CTC's total capital or risk tolerance. The same is certainly true of other market making firms: simply opening a trading floor does not create liquidity out of thin air. The direct result will be wider bid-ask spreads, to the further detriment of investors.

2. Approving the Proposal Would Have Severe Policy Consequences

As we have stated previously, approval of the Proposal would very likely result in a number of copycat proposals from other SROs seeking to make the same flawed argument BOX has made—namely, that if the SEC is prepared to permit the opening of one new trading floor, it must therefore allow the opening of any number of additional trading floors with identical rule sets. Approving the Proposal would therefore open the floodgates for every options SRO to launch nearly-empty "trading floors" in disused office space and broom closets (MIAX, MIAX Pearl, ISE, ISE Gemini, ISE Mercury, Nasdaq BX, NOM, C2,

[4] This approach, which we have consistently advocated since submitting a petition for rulemaking (the "Petition") jointly with Citadel Securities, LLC and Susquehanna International Group, LLC in 2013, would obviate the concerns expressed above, and ensure the maximum opportunity for investors to receive the best price for their orders. We reaffirm our support for this solution, and point again to the Petition for details.

Bats BZX, and Bats EDGX could all presumably copy this filing), engendering serious fragmentation of liquidity, imposing significant new costs on market making firms by obliging them to staff every floor or incur large opportunity costs, and harming investors by facilitating "venue shopping" by firms looking to internalize order flow at the expense of price improvement opportunities. We respectfully submit that this outcome, which would be a direct and highly probable result of approving the Proposal (in fact, several exchange executives have represented to us directly that they would "of course" file to open new trading floors if the Proposal were approved), would be entirely at odds with the Act.

3. <u>The Proposed Book Sweep Size Feature Remains Detrimental to Investor Protection And Would Unfairly Discriminate Against Resting Orders in the BOX Book</u>

The proposed "book sweep size" mechanism, regarding which we have raised concerns in our prior letters, remains part of the revised Proposal. This proposed feature would allow brokers to enter a maximum number of priority contracts in the BOX Book—including Public Customer bids and offers, and better-priced orders which would otherwise provide price improvement to a Qualified Open Outcry ("QOO") Order—with which a QOO Order would interact. Any QOO Order that would exceed this maximum level of book interaction would be rejected, depriving book interest of an execution opportunity.

As we have pointed out, compared to the obvious alternative of simply sweeping the book up to the full size of the QOO Order, this proposed feature can only result in more order rejects, less price improvement to QOO Orders from better-priced bids and offers in the book, and less book volume executing. It therefore remains paradoxical that BOX continues, in the revised Proposal, to claim—entirely without evidence—that this feature would "aid Floor Brokers in having *more* of their executions accepted by the Trading Host and will [provide] a tool to *assist Floor Brokers in executing orders* when there is priority interest on the BOX Book," adding, "the book sweep size will provide *increased* opportunity for orders on the BOX Book to be executed" and that the mechanism "will *increase* the opportunity for orders on the Trading Floor to interact with interest on the BOX Book" (emphasis added). With respect to each statement quoted here, the Proposal would in fact do precisely the opposite of what BOX has written.

We pointed out in our past letters that these representations are false. BOX has not addressed these concerns, instead simply pointing to the rules of another exchange and stating that "it shall be considered conduct inconsistent with just and equitable principles of trade for any Floor Broker to use the book sweep size for the purpose of violating the Floor Broker's duties and obligations". But copying another exchange's rule text is not sufficient to demonstrate consistency with the Act, and *ex post facto* regulatory supervision is not a sufficient remedy for providing a mechanism that is detrimental to investor protection. Indeed, it is unclear how this feature does anything *other* than hamper Floor Brokers' ability to comply with their obligations.

The solution remains straightforward and obvious: QOO Orders should, of course, sweep all available priority and better-priced interest, then the balance should execute in full. Capping the book sweep size prevents orders from executing in circumstances where there is a known ability for a Floor Broker's order to be filled, and possibly at a better price. By providing this mechanism, BOX would actively enable and encourage its participants' non-compliance with their best-execution obligations, and unfairly

discriminate against investors with executable orders resting in the BOX Book, in direct contravention of Section 6(b)(5) of the Act.

4. *Ex Post Facto*, Non-Public Data Disclosure is Inadequate to Legitimize the Proposal

CTC respectfully submits that it remains the responsibility of any SRO seeking approval to open a new trading floor to affirmatively demonstrate that doing so does not violate the Act's appropriate requirements to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest. Given the material public policy and investor protection issues raised above, BOX must meet a very high standard in providing data and argumentation explaining how opening a new trading floor would be consistent with these requirements of the Act—but it has not done so. BOX's commitment that it would share certain data regarding the functioning of its floor confidentially with the SEC on an *ex post facto* basis is inadequate. In order to demonstrate that opening a new open outcry trading floor would not be in contravention of the explicit requirements of the Act, BOX must produce detailed and compelling data supporting its claims that opening a new trading floor would enhance liquidity and price discovery *in advance* of opening any floor. As we noted in our first letter,

> This data should be accompanied by a rigorous published analysis demonstrating that any proposed new trading floor would enhance liquidity and price discovery for investors as determined by the [cited] metrics. In the case of the BOX Proposal, if it is not possible for BOX to produce a similar analysis supporting its contention that an additional trading floor would provide meaningful liquidity and thereby serve investors and the public interest, then we respectfully submit that BOX will not have demonstrated that the Proposal is consistent with the Act.

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For all the reasons cited above, we again encourage the Commission to disapprove the Proposal, and any similar proposal that would open a new multiply-listed options trading floor, absent both (1) persuasive and publicly-available supporting data and (2) robust processes such as a mandatory electronic exposure mechanism to encourage liquidity provision and price improvement, protect investors and the public interest, and remove—rather than introduce—impediments to the operation of the national market system. Given the current advanced state of exchange technology, the days of introducing new open-outcry trading venues due solely to exchange operators' view that doing so will advance their own competitive interests—at the expense of investor protection—should be behind us.

Should you have any questions with respect to this letter, or any of the topics referenced above, we would welcome the opportunity to discuss it further. We very much appreciate the opportunity to respond.

Sincerely,

Steve Crutchfield
Head of Market Structure

cc: Ms. Heather Seidel, Acting Director, Division of Trading and Markets
Mr. David S. Shillman, Associate Director, Division of Trading and Markets
Mr. John Roeser, Associate Director, Division of Trading and Markets