



August 12, 2011

**By Electronic Mail**

Elizabeth Murphy  
Secretary  
Securities and Exchange Commission  
100 F Street, NE  
Washington, DC 20549-1090

Re: *Proposed Rule Change to Amend the BOX Fee Schedule;  
File No. SR-BX-2011-046*

Dear Ms. Murphy:

Citadel LLC (“**Citadel**”)<sup>1</sup> appreciates the opportunity to submit this comment letter in response to the Boston Options Exchange Group, LLC’s (“**BOX**”) rule filing referenced above (the “**Rule Filing**”).<sup>2</sup> The Rule Filing amended the BOX fee schedule for most orders in options executed in a price improvement period (“**PIP**”) by increasing both the initiator credit and the responder fee for each transaction in the PIP from \$0.30 to \$0.75.<sup>3</sup>

The Rule Change reflects the third change to the PIP pricing structure in less than 12 months.<sup>4</sup> This latest amendment increases the fee charged to responders to a PIP auction (“**responders**”) and the credit paid to initiators of a PIP auction (“**initiators**”) by 150%; raising the fee and credit to 300% of those put in place less than one year ago. The Securities and Exchange Commission (the “**Commission**”) should suspend and disapprove the Rule Filing as

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<sup>1</sup> On an average day, Citadel accounts for approximately 8-9% of U.S. listed equity volume, and 25-30% of U.S. listed equity option volume. Founded in 1990, the Citadel group of companies includes an asset management division that principally executes alternative investment strategies across multiple asset classes, and Citadel Securities that includes investment banking, a sales and trading platform, and an industry leading market making franchise. Citadel operates in the world’s major financial centers, including Chicago, New York, London, Hong Kong and San Francisco.

<sup>2</sup> Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Amend the BOX Fee Schedule, Exchange Act Release No. 64981 (July 28, 2011), 76 FR 46858 (Aug. 3, 2011).

<sup>3</sup> The fee schedule was not changed with respect to PIP transactions in QQQQ, SPY, IWM and Penny Pilot Classes where the trade price is less than \$3.00.

<sup>4</sup> See Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Amend Fee Schedule of the Boston Options Exchange Facility, Exchange Act Release No. 62632 (Aug. 3, 2010), 75 FR 47869 (Aug. 9, 2010); Notice of Filing and Immediate Effectiveness of Proposed Rule Change to Amend Fee Schedule of the Boston Options Exchange Facility, Exchange Act Release No. 64198 (Apr. 6, 2011), 76 FR 20426 (Apr. 12, 2011).

discriminatory and unduly burdensome on competition. If BOX would like to press forward with this discriminatory fee structure, the Commission should require that BOX provide data regarding the impact of its two prior responder fee increases to allow proper analysis of the fee's prior discriminatory and competitively burdensome effect and the potential future effect of this exorbitant fee increase.

As Citadel noted in comments to the Commission in response to the first and second of these fee changes,<sup>5</sup> the initiator credit and responder fee scheme are discriminatory and unduly burdensome on competition. While the Rule Filing claims that the purpose of the fee structure is to provide an incentive for market participants to initiate PIP auctions for potential price improvement on their customer orders, the credit and fee scheme discourages anyone other than the initiator from responding to these auctions. This is because an initiator that responds to the PIP auction they themselves initiated is able to offset the fee and credit, while competitive third-party responders must pay the responder fee (in addition to regular trading fees). When an initiator submits an order to the PIP, it expects that, due to the incredibly high price a competitive responder would have to pay to trade against the order, the initiator will be able to internalize it. Competitive responders are essentially required to pay a \$0.75 "break-up fee" to interrupt the initiator's PIP internalization.

At \$0.25 (August 2010) and \$0.30 (April 2011), these fees discouraged third parties from responding to PIP auctions. At \$0.75 per contract, BOX has made it economically prohibitive for anyone other than the initiator to respond. When combined with other trading fees that discriminate by providing volume discounts to initiators but not responders, initiators would now typically enjoy a \$0.90 per contract advantage over responders. When the \$0.75 break-up fee is added to the \$0.25 trading fee, the total fee responders are now required to pay in most option classes is \$1.00 per contract – equal to the full \$0.01 cent per share quoting increment.

When discussing access fees, the Commission recently noted its concerns about the potential for options markets to use their fee structures for discriminatory purposes.<sup>6</sup> The Commission recognized that market forces are not always sufficient to prevent unfair pricing structures that distort the market, and some fees should be limited. In that context, the Commission proposed that options exchanges be limited to charging a maximum of \$0.30 per contract to access a quote. Fees above \$0.30, the Commission noted, could have a "distorting effect" on the market and the ability of market participants to compare quotes. If the

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<sup>5</sup> Comment Letter from John C. Nagel, Managing Director and General Counsel, Asset Management and Markets, Citadel LLC, to Elizabeth Murphy, Secretary, Securities and Exchange Commission (August 30, 2010), available at <http://sec.gov/comments/sr-bx-2010-049/bx2010049-3.pdf>; Common Letter from John C. Nagel, Managing Director and General Counsel, Asset Management and Markets, Citadel LLC, to Elizabeth Murphy, Secretary, Securities and Exchange Commission (May 3, 2011), available at <http://www.sec.gov/comments/sr-bx-2011-020/bx2011020-1.pdf>.

<sup>6</sup> See Exchange Act Release 61902 (Apr. 14, 2010).

Commission believes an access fee greater than \$0.30 is distortive, a break-up fee of \$0.75 (150% *higher*) – is all the more so.

The Rule Filing does not conform to the requirements of Form 19b-4 because it fails to explain the purpose of the rule change or why the rule change is consistent with the requirements of the Securities Exchange Act of 1934 (the “Exchange Act”). Like the prior two rule filings, the Rule Filing makes the unsupported assertion that the fee structure is designed to provide incentive for market participants to submit their customer orders to the PIP and allow those orders to benefit from potential price improvement. However, the Rule Filing does not provide any basis to support this mere assertion. For example, the Rule Filing does not describe the impact of the \$0.25 and \$0.30 that were charged in the past year. If these fees did not provide the incentive BOX expected, why does it assert that a \$0.75 fee will? If the prior fees did provide the anticipated incentives, why is such a large increase necessary?

Citadel believes that these fee increases are not intended to, and will not, incentivize participation in competitive PIP auctions or allow customers to benefit from price improvement. Recent statistics show that the increasing fees BOX charges to break-up a PIP auction are reducing price improvement opportunities for customers and turning PIP and BOX into an NBBO internalization engine. Since February of this year, the average price improvement per contract and average percentage of contracts price improved in PIP auctions has declined every month.

<u>Month (2011)</u>	<u>Monthly Average Price Improvement Per Contract in PIP Auctions<sup>7</sup></u>	<u>Monthly Average Percentage of Contracts Improved in PIP Auctions<sup>8</sup></u>
February	\$0.0102	52%
March	\$0.0098	41%
April	\$0.0092	39%
May	\$0.0077	36%
June	\$0.0063	32%
July	\$0.0062	30%

These statistics support our view that another increase in the break-up fee will further reduce the potential customer benefit from PIP auctions and is solely structured to benefit one group of BOX participants over another, and as such is discriminatory and unduly burdens competition, in violation of the Exchange Act.

<sup>7</sup> Calculated based on daily PIP statistics published on the BOX website. See BOX – Boston Options Exchange, Volume Statistics, *available at* [http://www.bostonoptions.com/volumes\\_en](http://www.bostonoptions.com/volumes_en).

<sup>8</sup> Calculated based on individual BOX PIP messages disseminated by BOX, and NBBO data disseminated by OPRA.

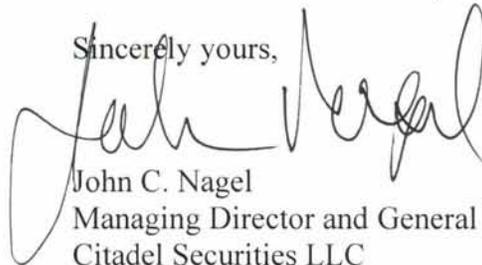
For the foregoing reasons, Citadel respectfully requests that the Commission suspend the operation of the Rule Filing and disapprove it because it unduly burdens competition and is inconsistent with the statutory requirements set forth in sections 6(b)(4), 6(b)(5) and 6(b)(8) of the Exchange Act. Given the frequency of changes to these fees, the incredible size of the current fee increase, and the lack of data provided by BOX to support the claimed basis for its Rule Filing, the Commission should require BOX to subject its rule change proposal to full notice and comment.

If, following any suspension of the Rule Filing as requested above, BOX insists on pressing its breakup fee scheme, before permitting it to do so the SEC should require BOX to provide data showing how the fees and credits have impacted (i) the level of participation in PIP auctions by competitive third-party responders, (ii) the level and frequency of price improvement customers receive, and (iii) rates of internalization. The Commission and market participants should have an opportunity to analyze this data and consider BOX's proposed rule change based on this information.

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If you have any questions, please do not hesitate to contact me at (312) 395-2100.

Sincerely yours,



John C. Nagel  
Managing Director and General Counsel  
Citadel Securities LLC