Knight

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November 28, 2011

Ms. Elizabeth M. Murphy
Secretary
Office of the Corporate Secretary
Securities and Exchange Commission
100 F Street, N.W.
Washington, D.C. 20549-1090

Re: Securities Exchange Act Release No. 34-65672
File No. SR-NYSE-2011-55; Notice of Rule Filing of Rule Change Proposing a One-Year Pilot Program Adding New Rule 107C To Establish a Retail Liquidity Program To Attract Additional Retail Order Flow to the Exchange for NYSE and Amex-Listed Securities

Dear Ms. Murphy:

Knight Capital Group, Inc.[1] ("Knight") welcomes the opportunity to comment on the above referenced New York Stock Exchange ("NYSE") proposal to establish a Retail Liquidity Program ("the Liquidity Program") filed with the Securities and Exchange Commission ("SEC" or "Commission"),[2] as well as the concurrently filed request for exemptive relief pursuant to Rule 612(c) of Regulation NMS ("Exemptive Request").[3] The Liquidity Program seeks to attract retail order flow to the NYSE through the provision of price improvement from undisplayed sub-penny orders posted by professional Retail Liquidity Providers ("RLPs") on the NYSE book.

Knight fully supports market initiatives designed to provide greater price competition for retail orders. The U.S. equity market is the most effective marketplace in the world as a result of on-going innovation, prudent regulation and an unrelenting competitive dynamic. As a result, retail investors have never had better equity execution quality and access to the marketplace. Indeed, the NYSE correctly notes in its Exemptive Request:

> The Exchanges continue to fully embrace fair competition among exchanges and other market centers and acknowledge the positive trading experience that retail investors enjoy in today's marketplace.[4]

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[1] Knight Capital Group, Inc., through its subsidiaries, is a major liquidity center for foreign and domestic equities, fixed income securities, and currencies. On active days, Knight can execute in excess of 10 million trades, with volume exceeding 15 billion shares. Knight's clients include more than 3,000 broker/dealers and institutional clients. Knight employs more than 1,400 people worldwide. For more information, please visit: www.knight.com.
[2] SEC Release No. 34-6572 (November 2, 2011). Our comments are equally applicable to a related filing made by NYSE Amex LLC: SEC Release No. 34-65671; SR-NYSEAMEX-2011-84 (November 2, 2011).
[3] NYSE Application for Exemptive Relief (October 19, 2011).
[4] See NYSE Application for Exemptive Relief, pp 1-2 (October 19, 2011).

The "positive experience" enjoyed by retail investors today is the culmination of years of rigorous competition and sensible, well-vetted regulation. As such, this "positive experience" must remain sacrosanct when considering any change to equity market structure – especially some of the more profound changes contemplated by the current filing. Again, we support the NYSE's efforts to establish a program that will provide greater price competition for retail orders. When market centers compete on a level playing field, it inures to the benefit of investors.

However, there are a number of important issues raised by the Liquidity Program that require careful analysis and consideration before being approved. As more fully described below, certain components of the NYSE proposal have the potential to cause significant changes to U.S. equity market structure. As such, we respectfully urge the Commission to extend the comment period until a broad cross-section of the market can examine and consider the implications of these significant changes. We respectfully submit that 30 days is not nearly enough time for market participants and the Commission to gather the necessary data and analyze the market impact of the proposal. In addition, the implications to long-standing industry rules and regulations need to be carefully considered, as well as the fairness of the proposal as it relates to maintaining a level playing field for all market participants.

The current NYSE proposal has broad and sweeping implications which we submit the SEC should carefully consider, including the impact on fundamental tenets of Regulation NMS. When one considers that the comment period for Regulation NMS extended over a one-year period, 30 days for the current proposal is simply not enough time to responsibly consider and comment on these issues.

The following is a brief list of potential market structure concerns raised by the Liquidity Program:

A. Sub-Penny Ranking of Orders

One of the more significant issues raised by the proposed Liquidity Program is the impact on Rule 612 of Regulation NMS (i.e., the "sub-penny rule"). Rule 612 prohibits (among other things):

> …market participants from displaying, ranking, or accepting quotations in NMS stocks that are priced in an increment of less than $0.01, unless the price of the quotation is less than $1.00.[5]

As one of the more actively debated components of Regulation NMS, Rule 612 was the subject of several comment letters. Thus, material changes to this rule, like those contemplated by the Liquidity Program, require careful consideration.

[5] See Regulation NMS Adopting Release, SEC Release No. 34-51808, p. 29 (June 9, 2005).

For example, the Liquidity Program effectively calls for the reduction of the tick size mandated by Rule 612 from $0.01 to $0.001. If the Commission were inclined to move in this direction, it is very likely that all market centers (lit and dark) would immediately seek similar relief so as to keep the competitive landscape on a level playing field. To proceed in any other manner would be tantamount to conveying to the NYSE a pricing convention monopoly. Thus market participants need to have an appropriate amount of time to consider the issues associated with changing this long-standing minimum price variant ("MPV") and to provide comprehensive comment before the Commission renders its final decision. For example, moving to a $0.001 MPV effectively takes the NMS market from 100 price points between each dollar level to 1,000 price points. Market participants need to consider the impact that will have on a number of factors including trading technologies and capacity, operational costs, execution quality, liquidity and gaming.[6]

B. Best Execution Challenges

The NYSE filing also raises a number of important best execution issues. For example, the NYSE proposal contemplates that the NYSE will provide a Retail Liquidity Identifier ("RLI") when it has a resting (undisplayed) order from an RLP (or non-RLP) between the NYSE's best displayed bid and offer. This raises a number of questions, including:

1. Will broker/dealers be required to subscribe to this NYSE proprietary data feed?
2. If they do, will they be required to route orders to the NYSE when they receive an RLI?
3. If multiple market centers provide price improvement, and have a similar RLI, would market participants be required to sweep all liquidity inside the spread before executing at the NBBO?
4. If a competing market center provided price improvement of $0.001 or better, would the NYSE be required to send its retail order to that venue for execution?
5. Would executing an order at the NBBO, without considering potential RLI interest, be contrary to notions of best execution?
6. Since the underlying RLP orders are resting on the NYSE book, should these RLI's be part of the consolidated quote so that investors can see them as well?

The answers to these questions and others should be considered prior to moving forward with such an important change.

C. Access Fees

If the NYSE is granted an exception to Rule 612 as discussed above, a market-wide move to a $0.001 tick size is inevitable. If such a market structure were to be adopted, access fees of up to $0.003 would need to be immediately addressed. As we have previously noted:

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[6] In fact, in its Exemptive Request, the NYSE notes that, "...sub-penny trading and pricing could potentially result in undesirable market behavior." See NYSE Application for Exemptive Relief, footnote 6 (October 19, 2011).

> Access fees have been at the core of nearly every debate that has taken place around market structure for almost two decades – taking hold after the SEC Order Handling Rules were adopted in 1996. It was certainly not anticipated at that time, when spreads were multiples of what they are now, that this "communications charge" would become such a large component of the cost associated with a trade, or a profit center which had become the basis for routing and trading practices. As spreads have narrowed over the years, a $0.003/share access fee has become a significant cost associated with the trade. Indeed, in a one penny spread environment, access fees have the effect of increasing the economic spread by 60% (assuming $0.003 on each side of the quote).[7]

This issue becomes significantly exacerbated with a $0.001 MPV, increasing the economic spread by 600%.

D. Manning Protection

Under FINRA Rule 5320, market making firms cannot trade ahead of resting customer orders unless they trade at prices at least $0.01 better than the resting order (i.e., "Manning protection"). This is tied directly to the one penny MPV for NMS stocks priced more than $1.00.[8] Another potential by-product of a move to sub-penny increments is the impact on Manning protection. For example, assume the NYSE BBO is 10.01 x 10.02. A non-RLP, who also handles retail customer orders, posts a Retail Price Improvement ("RPI") bid at $10.015 for 500 shares. If that RPI is hit with an eligible retail order, the non-RLP buys 500 shares at $10.015. However, if that same non-RLP holds a customer limit order to buy 500 shares at $10.01, under current Manning protection requirements the non-RLP would be obligated to sell the 500 shares to its client at $10.01 – losing $0.005 per share (or $2.50) on this order. This "reverse Manning" scenario could occur thousands of times each day.

As such, one of two things could occur:

1. Certain market makers will be limited in their participation in the Liquidity Program (limiting the potential of price improvement opportunities for retail investors); or
2. Amendments to FINRA Rule 5320 would need to be considered in light of the new MPV.

E. Market Data

As noted above, moving toward a $0.001 tick size would significantly increase message traffic and corresponding market data, requiring a comprehensive analysis of the capacity and bandwidth of industry trading technologies.

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[7] See Knight's Comment Letter Relating to SEC Release No. 34-61358 (Concept Release) dated April 25, 2010, citing the SEC's Order Execution Obligations, Release No. 34-37619A (September 6, 1996), footnote 272.
[8] See FINRA Rule 5320.

F. The "Two-Tier" System

Under Regulation ATS, an alternative trading system ("ATS") has broader freedom to limit access to its venue and often does not display its order book. However, the ATS must revert to exchange rules if it garners market share above a specified threshold.[9] The NYSE Liquidity Program does not appear to be subject to this requirement. Thus maintaining a limited access dark pool outside of Regulation ATS could have the effect of creating a two-tier market.

G. Retail Certification

Retail Member Organizations ("RMOs") will have to require each of their broker/dealer clients to certify – and to get *their* clients to certify – that their order flow will conform to the definition of "Retail" as specified by the Liquidity Program. The certification will then have to be carefully monitored and re-affirmed at least annually. The rule proposal states that a retail order is, "an agency order that originates from a natural person…" This raises concerns about the feasibility of securing the requisite certifications and the operational burden this will impose on all participants in surveilling this activity.

From a gaming perspective, this program could drive professional traders to move activities into retail accounts where they could access the price improvement opportunities designed for the retail investor.

H. Level Playing Field

As we noted above, in order to ensure that the NYSE is not granted a pricing convention monopoly, we submit that the Commission should consider whether a more broad-based application of the proposal among a wider group of market participants is appropriate. In light of this, we query whether it would be more appropriate for such a shift in market structure to be an SEC driven rule change, subject to thorough comment and analysis, rather than a rule proposal of a single market participant.

Conclusion

To reiterate, Knight fully supports the NYSE initiatives to promote pricing competition for retail orders.

However, the NYSE Liquidity Program raises a number of very important market-structure issues that market participants and the Commission need to carefully consider. Several regulations and industry practices are directly impacted by the NYSE proposal. Accordingly, the potential for unintended consequences is significant.

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[9] See Rule 301 of Regulation ATS.

Therefore, extending the comment period to consider these and a myriad other potential issue is imperative. We respectfully request the Commission allow for considerate and complete analysis, as well as robust discussion through a sensible and thorough comment process.

We welcome the opportunity to discuss our comments with the Commission.

Respectively submitted,

Leonard J. Amoruso

cc. SEC Chairman Mary L. Schapiro
SEC Commissioner Elisse B. Walter
SEC Commissioner Luis A. Aguilar
SEC Commissioner Troy A. Paredes
SEC Commissioner Daniel M. Gallagher
Robert W. Cook, Director, SEC Division of Trading and Markets
Duncan L. Niederauer, Chief Executive Officer, NYSE
Lawrence Leibowitz, Chief Operating Officer, NYSE