Via Electronic Submission and Mail

October 13, 2014

Ms. Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549-0609

Re: AMEX Options Fee Filing – 34-72469/SR NYSEMKT -2014-52

Dear Ms. Murphy:

The options Market Maker Firms who have signed this letter ("we" or "the MM firms") wish to address a matter relating to the NYSE-MKT ("AMEX") rule filing referenced above. Specifically, we are concerned with the growing trend of exchanges imposing oversized transaction fees on market makers (MMs) when they compete with the facilitation side to pre-matched auction crosses. While the AMEX's "Customer Best Execution Auction" ("CUBE") fee is neither the highest nor the lowest among exchanges, it furthers and promotes the trend of these anti-competitive fees. If allowed to expand unabated, the collective impact of these fees will become a significant burden on competition[1]. This matter needs broad discussion, and the CUBE filing provides a good starting point.

The fee in question, ***commonly known as a "break-up fee"***, is essentially a fee designed to hamper traders (primarily MMs) from competing on auction crosses. Its purpose is to help internalizing facilitators more often be the full, or almost full, contra-side to cross orders with customers (so-called "clean-crosses"). We believe some internalizers are already realizing a participation rate of over 70% on their crosses in one or more auctions (as a percent of overall contracts placed for a broad mix of orders over a sustained period of time). These high internalization rates are being met in a discriminatory manner at the expense of competition from MMs. The problem ahead is that these fees may lead to a substantial decline in the execution quality of options overall on all exchanges.

[1] Over 90% of displayed option liquidity is currently provided by option MMs through competitive quoting.

A break-up fee is not a stand-alone fee, but rather, it is viewed as the net cost of an auction Responder fee coupled with applicable auxiliary fees/rebates such as: maker/taker fees, marketing fees (PFOF) and withholding of tier discounts. Given the complexities that go into calculating these fees, most market participants are unaware of the degree by which some exchanges penalize MMs for competing against clean cross facilitators. In this regard, the Fee Chart below compiles home-MM fees applicable to the various option auctions. For comparison sake, the "Auction Fee" column for MMs (i.e., the break-up fee) is shown next to the column for the "Regular Fee" that MMs pay/receive when their displayed quotes are taken. There is also a column showing the net difference between Auction Fees and Regular Fees, as well as a column for the much smaller "Initiator Fee".

Exchange 'Mechanism'	**Category**	**Auction Fee (Range) For MM Responders +/- Make Fee + PFOF**	**Regular Fee (Range) For MMs +/- Make Fee + any PFOF**	**Break-Up Difference**	**Initiator Fee**
NYSE Amex 'CUBE'	Penny	(0.55)	(0.26) to (0.45)	(0.29) to (0.10)	(0.05)
NYSE Amex 'CUBE'	NonPenny	(0.90)	(0.66) to (0.85)	(0.24) to (0.05)	(0.05)
CBOE 'AIM'	Penny	(0.28) to (0.48)	(0.28) to (0.48)	0.00	(0.05)
CBOE 'AIM'	NonPenny	(0.68) to (0.88)	(0.68) to (0.88)	0.00	(0.05)
PHLX 'PIXL'	Penny	(0.42) to (0.55)	(0.42) to (0.47)	0.00 to (0.08)	(0.05) to (0.07) [2]
PHLX 'PIXL'	NonPenny	(0.87) to (1.08)	(0.92) to (1.00)	(0.05) to (0.08)	(0.05) to (0.07) [2]
PHLX 'PIXL'	Select [3]	(0.25) to (0.55)	(0.25) to (0.47)	0.00 to (0.08)	(0.05) to (0.07) [2]
MIAX 'PRIME'	Penny	(0.45)	(0.30) to (0.42)	(0.15) to (0.03)	(0.05)
MIAX 'PRIME'	NonPenny	(0.90)	(0.75) to (0.87)	(0.15) to (0.03)	(0.05)
ISE 'PIM'	Penny	(0.45)	(0.10) to +0.20	(0.35) to (0.65)	(0.03) to (0.05) [4]
ISE 'PIM'	NonPenny	(0.45)	(0.85) to (0.92)	+0.40 to +0.47	(0.03) to (0.05) [4]
ISE 'PIM'	Penny	(0.45)	(0.10) to +0.20	(0.35) to (0.65)	(0.20) [5]
ISE 'PIM'	NonPenny	(0.45)	(0.85) to (0.92)	+0.40 to +0.47	(0.20) [5]
ISE Gemini 'PIM'	Penny	(0.49)	+0.30 to +0.38	(0.79) to (0.87)	(0.20)
ISE Gemini 'PIM'	NonPenny	(0.86)	+0.40 to +0.49	(1.26) to (1.35)	(0.20)
BOX 'PIP'	Penny	(0.65) [6, 8]	(0.43) to (0.65) [7]	(0.22) to 0.00	(0.03) to (0.25)
BOX 'PIP'	Penny	(1.05) [6, 9]	(0.43) to (0.65) [7]	(0.40) to (0.62)	(0.03) to (0.25)
BOX 'PIP'	NonPenny	(0.65) [6, 8]	(0.88) to (1.10) [7]	(0.23) to (0.45)	(0.03) to (0.25)
BOX 'PIP'	NonPenny	(1.05) [6, 9]	(0.88) to (1.10) [7]	(0.17) to +0.05	(0.03) to (0.25)

[2] For less than 1,000 contracts
[3] Symbols: AAPL, BAC, EEM, FB, FXI, IWM, QQQ, TWTR, VXX, and XLF
[4] For 100 or less contracts
[5] For 101 or more contracts
[6] Responding orders pay the Fee for Adding Liquidity
[7] Maker orders pay Fee for Adding Liquidity
[8] Where trade price is less than $3.00
[9] Where trade price is greater than or equal to $3.00

The Auction Fee for home-MMs, which constitutes the break-up fee, includes: the Responder Fee, plus or minus any maker/taker amounts, plus any PFOF or MM rebate/tier impacts. Therefore, assessing break-up fees involves some complicated mixing and matching of assorted and related fees. Using CUBE as an example, while MMs do not incur PFOF charges when responding to a CUBE Order they are ineligible for volume tiers and fee caps when they do. When a high Responder Fee is added to the mix, the net result is an oversized break-up fee that discourages MMs from competing with clean crosses. The CUBE's break-up fee looms ever larger when compared to the modest "Initiator Fee". A high differential in this regard is typical for exchange auctions that impose oversized break-up fees. If there was any remaining doubt about auctions with oversized break-up fees courting internalizers at the expense of MMs, one need only consider that such auctions also routinely pay high rebates to initiators for each customer side order that does *not* trade with the assigned facilitator. In the case of CUBE, it is $0.40 for Penny Pilot options and $0.80 for non-Penny Pilot options.

Most contracts placed for clean-crossing in auctions with oversized break-up fees occur at the NBBO – and therefore not at "real" price improvement levels. On this point, it is misleading for an exchange with an oversized break-up fee to refer to its auction as a price-improvement auction if the majority of its auction contracts trade at the NBBO price. What makes matters worse in this regard is that auctions are best positioned to attract clean-cross orders if the respective exchange is displaying a quote worse than the NBBO – thereby leaving room to cross at an improved price on that exchange but not improving the NBBO price. Attracting clean-cross order flow to an auction is not a suitable reason for imposing break-up fees that discourage competition and encourage markets wider than the NBBO.

The related and equally disturbing concern is that break-up fees may not only serve to make quotes wider on the respective exchanges, they may also cause the NBBO itself to become much wider. We believe this occurs at some point where such fees become pervasive enough to undermine the overall competitive structure in options. Moreover, we believe market-wide "quote quality" can suffer even when break-up fees are imposed by just a few exchanges, if the fees cause an appreciable amount of customer order flow to be directed to less competitively quoted markets.

The reason quote quality can suffer under such circumstances is because MMs usually contemplate the amount of non-professional customer order flow they expect to interact with when assessing how tight and liquid to make their quotes. They quote more aggressively when they have the reasonable expectation that they will be able to compete fairly for participation in less risky trades – and of course retail customer orders are usually viewed as less risky. The ability to compete fairly also translates into more chances for MMs to acquire risk-reducing natural hedges and off-sets. These opportunities, in turn, serve in symbiotic fashion to generate tighter and more liquid quotes from the MMs. If break-up fees lead to much fewer opportunities to compete for customer order flow, the risk-reward balance will shift MMs away from the normal quoting process. In short, MMs will be less willing to risk tight and liquid quotes to attract customer order flow if they expect that much of the sought-after order flow will be sent to auctions with oversized break-up fees for clean crossing.

The issue of oversized break-up fees hurting the quality of markets across all options exchanges is a relatively new concern. In the past, exchanges would strive to keep MM fees reasonable because helping MMs display tight quotes also helped attract customer order flow. As MMs have historically provided over 90% of displayed option liquidity, exchanges have kept to the belief that discouraging them from competing in their market would be antithetical to the success of that marketplace – until now. The negative impact oversized break-up fees have on the NBBO grows with each new break-up fee added and raised by exchanges. And, of course, higher rates are normally adopted effective-upon-filing, which means that exchanges can raise their fees in quick fashion[10].

While assessed as pennies-per-contract, break-up fees nonetheless impact quote quality significantly. MMs usually calculate quote values to a fraction of a penny and then round to the next incremental value away from calculated fair value (e.g., up a penny for offers and down a penny for bids in penny classes). Thus, a new net MM fee of $0.30 would likely cause MMs to quote a full penny away from the calculated fair value approximately 30% of the time. As most MM executions in penny classes occur at prices reflecting only a few pennies of "edge" value, a fee that causes them to alter their interest by one penny 30% of the time will very often determine whether a customer receives an execution at a better or worse trading increment. Of course when this happens these penny differences translate into multiple dollar differences per order for respective customers.

[10] Given the quick fashion by which fee changes occur, we make no claim to the total accuracy of the Fee Chart; though we believe the chart to be accurate as of a recent trade date.

Fortunately, for now, most customer volume executed in auctions occurs in auctions that do not impose oversized break-up fees. The concern, of course, is that these exchanges will eventually be forced by competitive pressures to follow suit and adopt oversized break-up fees. In this connection, the more that oversized break-up fees successfully bring contract volume to the respective exchanges, the more we expect other exchanges will be forced to adopt such fees. Before that has a chance to occur, we recommend that the Securities and Exchange Commission ("the SEC" or "the Commission") perform an impact-analysis of all break-up fees and explore the surrounding issues in detail.

Specifically, we recommend that the Commission assess the impact of break-up fees in the context of determining where levels become discriminatory and anti-competitive. This process should include investigating: (i) whether "real" price improvement for customers (i.e., giving a customer a price better than the NBBO) is diminished in the presence of an oversized break-up fee; (ii) whether MMs tend to show less competitive quotes on exchanges where oversized break-up fees are present and (iii) at what point can we expect oversized break-up fees (if left unabated) to lead to much wider and less liquid option quotes overall.

While the first two points above should be easily determinable from exchange records, the third point does require some prognostication. Nonetheless, this third point needs to be carefully analyzed before break-up fees become completely embedded in our market structure. The longer it takes to address the issue, the greater the chance that oversized break-up fees will become blithely accepted as business-as-usual. Indeed, the current situation poses the classic boiling-frog concern – where the skewering of execution quality may be so gradual that it escapes regulatory scrutiny in the early stages. We have already seen how blind deference to legacy practices has shielded the fact that block crosses routinely occur at dubious prices on traditional floor exchanges[11]. Thus, we recommend that the Commission address the fee impact on MM quoting now. As some exchanges are *not* in favor of over-sized break-up fees, the SEC should inquire with all exchanges whether they believe over-sized break-up fees have led, or will lead, to a demoralization of quoting by MMs and execution quality for customers. It is certainly well worth exploring with all exchanges – and the sooner the better.

[11] Petition on Rulemaking to the SEC "Option Floor Crosses" filed on April 22, 2013

We do not mean to suggest that price-improvement auctions are inherently flawed and have no place in the options market. To the contrary, in the absence of oversized break-up fees, the execution processes for auction ~~trades provides amp~~le and valuable opportunity for MMs to price improve and otherwise contribute liquidity to the benefit of customers. In this regard, not surprisingly, the quoting and matching processes themselves are employed in a similar fashion by the various exchanges. For example, using the description by the AMEX in its CUBE filing, the process works as follows: a Trading Permit holder (the "Initiator") can place an agency order at a guaranteed execution price (the "customer order") by submitting the order along with an off-setting contra-side order representing principal interest (the "facilitator") whereupon the Exchange will notify other market participants by way of a Request-for-Response so that they may place orders to compete in a sub-second CUBE auction with the facilitator (the "Responders"). Without oversized break-up fees, this process seemingly provides an excellent way to garner price improvement and added liquidity for customers.

Thus, as the auction process (without break-up fees) obviously has merit in serving the public interest, it raises the question of who stands to benefit when break-up fees are added – other than the exchanges and the clean-cross facilitators. The answer, of course, is that everyone else suffers. MMs suffer from the loss of opportunity to compete on trades against customer order flow. Customers suffer from the loss of competition from the MMs. And capital markets in general, while already suffering from these fees, will eventually suffer greatly from the wider and less liquid overall quotes that break-up fees create, which we expect will get worse each time an exchange adopts or raises such a fee.

The higher the break-up fee, the more impact the fee has on diminishing the quality of execution. In this regard, the BOX's PIP auction appears to have the highest break-up fee. Rather than mix and match related fees in a more balanced approach, the BOX instead combines multiple fees unfavorable to MMs under one auction roof. That is, the PIP combines a high Responder fee with a high Maker-fee (i.e., it imposes its normal maker-fee on MM auction responders). When adding these fees together, the net result is an extremely over-sized break-up fee. Moreover, while the PIP break-up fee endangers execution quality in penny class options, it is worse for non-penny options. No doubt, should every exchange auction adopt a break-up fee structure similar to that of PIP, market-wide liquidity would be drastically reduced.

The more that MMs are unfairly denied to compete as auction Responders, the higher the internalization rate for clean-cross facilitators will grow. But high rates themselves are not necessarily the problem. High rates due to break-up fees are distinguishable from high rates sometimes achieved from competitive trading and, in this regard, we do not mean to impugn the process where facilitators competing on a level playing field achieve high participation rates. When fair competition is present, the execution quality for customers overall improves notwithstanding the participation rate. The point is that high rates that result from the inability of MMs to compete on a fair and reasonable basis is what hurts investors and the market place overall. A related point of interest is that the high rates achieved for clean cross internalizers due to break-up fees are normally much higher than the rates usually achieved by open and fair competition among MMs and other facilitators.

Although internalization rates in excess of 70% (seemingly attainable on one or more auctions with oversized break-up fees) are not guaranteed, they can be quasi-guaranteed when the anti-competitive protection bestowed on initiators in the form of break-up fees is very high. In this connection, these rates are an extreme departure from the 40% that has served as the de facto guarantee-ceiling for many years. It is perplexing that, throughout the years, the SEC has been a steadfast defender against those attempting to raise the 40% guarantee-ceiling. Indeed, quite often the SEC has wisely reminded the industry that larger guarantees could lead to larger problems – including the discouragement of MMs from competing with their tightest possible quotes. While surprising to see the SEC depart from the position it maintained for so long, it is more so surprising that exchanges are being allowed to circumvent the 40% ceiling through the back-door process of over-sized break-up fees.

From our vantage point, the 40% ceiling is more critical now than ever. With about a dozen demutualized exchanges vying for order flow, it is no wonder that certain exchanges are doing what they can in this regard to attract clean-crosses. Yet, if left unabated, wider and less liquid quotes will be the legacy effect of these fees. The inescapable conclusion is that oversized break-up fees lead to high-levels of internalization by opportunistic facilitators. This, we believe, will in turn lead to wider and less liquid quotes. In the end, universally applied high break-up fees would not just shift participation from home-MMs to internalizing facilitators – they would appreciably reduce execution quality across all exchanges.

The prospect of exchanges picking winners and losers in options by blocking certain parties from competing fairly is antithetical to the operating principles of exchanges registered under Section 6 of the "34 Act. In particular, we believe oversized break-up fees are inconsistent with Section 6(b)(5) of the '34 Act in the way they discriminate against MM participation and competition to a degree that is harmful to public investors.

The Commission should assess the impact of these fees and the ability of exchanges to meet their statutory obligation to protect the interest of customers in this regard. So far, the exchanges with oversized break-up fees have had little to say on the salient points. When submitting their respective break-up fee filings, they largely ignored the market impact issues we discuss herein, thereby allowing for the presumption that investors will continue to enjoy the same level of MM competition for their orders. They ignored that over-sized break-up fees may mean that many liquidity providing MMs will see their overall customer-participation rates go down significantly. They did not attempt to explain the potential impact to their quote quality when and if this happens. None spoke to the possibility that denying MMs the ability to compete on fairly equal terms may lead to wider and less liquid quotes either on their exchange or any other exchange.

In conclusion, oversized break-up fees are not in the public interest. They are both discriminatory and anti-competitive toward MMs and, if left to grow unabated, will widen quotes across the market and decrease execution quality significantly for customers. These fees harm competition by unfairly and disproportionately favoring internalizers over competitive MMs. The Commission should assess the impact of these fees on customers, and the markets, by evaluating break-up fees on all exchanges and take the steps to safeguard the high level of competitiveness that has well served the options market for so long.

Should you have any questions with respect to this letter, please feel free to contact any of us signed below. Again, thank you for this opportunity to respond.

/Signatures on following page/

Sincerely,

Gerald D. O'Connell – CRO
Susquehanna International Group, LLP ____________

John Kinahan – CEO
Group One Trading, LP ____________

Daniel Overmyer – Head of Compliance
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cc: Steve Luparello, Division of Trading and Markets
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