Knight

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Nancy M. Morris
Secretary
U.S. Securities and Exchange Commission
100 F Street, NW
Washington, D.C. 20549

Re: File No. SR-NASD-2005-095
National Association of Securities Dealers, Inc., Notice of Filing or Proposed Rule Change and Amendment No. 2 Thereto Relating to Sub-Penny Restrictions for Non-NASDAQ Over-the-Counter Equity Securities
Release No. 34-53024 (December 27, 2005)

Dear Ms. Morris:

Knight Capital Group, Inc. (Knight)[1] welcomes the opportunity to offer our comments to the Securities and Exchange Commission (Commission) on the recent rule filing of the National Association of Securities Dealers, Inc. (NASD) in which the NASD proposes to amend NASD Rule 6750 to impose restrictions on the display of quotations orders in sub-penny increments for non-Nasdaq over-the-counter (OTC) equity securities. In the current amendment (Amendment No. 2), the NASD proposes to eliminate the requirement of Rule 6450(c) – i.e., the requirement that a participant ATS or ECN reflect non-subscriber access fees in their posted quotes on the OTC Bulletin Board (OTCBB).

Knight respectfully opposes this proposal, and requests that the Commission reject Amendment No. 2.

One of the key purposes of the rule proposal was for the OTCBB market to adopt sub-penny rules similar to those found in the Regulation NMS. As a threshold matter, it is difficult to reconcile the OTCBB market with the standards articulated in Regulation NMS, since securities listed on the OTCBB have efficiently traded in sub-penny

[1] Knight is the parent company of Knight Equity Markets, L.P., Knight Capital Markets LLC, and Knight Equity Markets International Ltd., Direct Trading Institutional, L.P., and Direct Edge ECN LLC, all of whom are registered broker-dealers. Knight and its affiliates, make markets in equity securities listed on Nasdaq, the OTC Bulletin Board, and the New York Stock Exchange, American Stock Exchange, both in the United States and Europe. Knight also owns an asset management business for institutional investors and high net worth individuals through its Deephaven subsidiary. Knight is a major liquidity center for the Nasdaq and listed markets. As a dealer, we make markets in nearly all equity securities. On active days, Knight executes in excess of one million trades, with volume exceeding one billion shares. Knight's clients include approximately 600 broker-dealers and 800 institutional clients. Currently, Knight employs more than 700 people.

increments for several years. Indeed, it is fairly well-recognized that less liquid securities trade in increments smaller than a penny, so as to help generate the requisite interest needed to satisfy investor demands for liquidity.

Today, the OTCBB is a robust and competitive market. In fact, as of December 2005, more than 3,200 companies were listed and more than 34 billion shares traded on the OTCBB.[2] Market participants compete in a fair and transparent manner, and all quotes reflect "true" pricing – i.e., access fees are reflected in the quotations. Thus, there are no "hidden" fees, and the price you see is the price you get.

On July 28 2005, the NASD proposed to change its Rule 6750, and then followed with Amendment No. 1 on August 17, 2005.[3] Since the rule applied equally to all, it generated little public comment. The ARCA ECN (ARCA), however, did submit a comment letter.[4] ARCA stated, in part, that the fees charged by an ECN or ATS are often less than the newly proposed price increment of one penny. Thus, it appeared inconsistent to require an ECN or ATS to reflect its sub-penny access fee, but prohibit sub-penny quoting. Interestingly, we are aware of no ECN or ATS that has chosen to incorporate a non-subscriber fee into their published quote. Nevertheless, it was this comment letter that appears to have led to the filing of Amendment No. 2.

We submit that Amendment No. 2 will undoubtedly lead to a number of unintended and dramatic consequences which will be detrimental to market participants and public investors. In essence, this amendment will allow an ECN or ATS to charge access fees to non-subscribers in the OTCBB, but will not require that they display those fees in their quotation. This will immediately cause an "unlevel" playing field in the OTCBB market, as only an ATS or ECN will be given an unfettered license to charge in this marketplace. Although Knight owns an ECN that will stand to benefit from this proposal (Direct Edge ECN), we oppose strongly this rule filing because the harm to the marketplace and investors will far outweigh any benefit derived from charging undisplayed access fees.

Knight has long held the view that if access fees are permitted to be charged, then they should be displayed. This is particularly relevant in the OTCBB market. Quotations at the same price have vastly different economic implications. When an ECN and a market maker are both at the inside market, the net price provided by the ECN is inferior to the price of the market maker by the size of the access fee. This fee distorts the price/time auction by permitting an ECN with an inferior price to have parity with a market maker providing a better net price.

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[2] Source: OTCBB.com

[3] SEC Release 34-52280.

[4] See, Letter of Kevin J.P. O'Hara, Chief Administrative Officer & General Counsel, Archipelago Trading Services, (September 23, 2005).

Further, this amendment may also lead to the proliferation of activities designed to game the market and investor orders. By way of example, market participants could opportune the market by placing quotes that would lock markets in stocks where the trading increment is lower than the access fee. Thus, in markets that trade in four decimal spots (e.g., $0.0002 x 0.0009), an access fee is $0.003 could be several times the cost of the security itself. The impact on the OTCBB market could be enormous. Consider the fact that as of January 20, 2006, 17 of the top 20 most active stocks (by volume) on the OTCBB traded in prices lower that $0.003 per share – many of them trading at prices of $0.0009 or lower. Thus, 17 of the 20 most actively traded securities would be permitted to have undisclosed access fees which would greatly exceed the actual price of the security -- some by as much as 10 times or more. As of January 20, 2006, these 17 securities accounted for more than 70% of the total volume reported on the OTCBB.[5] Accordingly, the potential negative impact of Amendment No. 2 cannot be overstated.

We believe that two choices exist which will insure a level playing field for all market participants and investors alike. One, continue the status quo. That is, allow the OTCBB to continue to operate as it has for the last several years, quoting in sub-penny increments and requiring that a participating ATS or ECN reflect non-subscriber access fees in their posted quote. Alternatively, restrict sub-penny quoting as proposed in the NASD's initial filing, but require ECN and ATS participants to incorporate sub-penny, non-subscriber fees in their published quote. In effect, reject Amendment No. 2. In either case, the Commission can insure full price and cost transparency to investors, as well as prevent any unintended, harmful gaming of investor orders.

Conclusion

We commend the NASD for its efforts to improve the OTCBB market, but reiterate that proper measures must be taken to insure full transparency and a level playing field for all market participants and investors.

Thank you again for providing us with the opportunity to comment on this rule proposal. Knight would welcome the opportunity to discuss our comments with the Commission.

Sincerely yours,

Leonard J. Amoruso

[5] Source: OTCBB.com

cc: Chairman Christopher Cox
Commissioner Paul S. Atkins
Commissioner Roel C. Campos
Commissioner Cynthia A. Glassman
Commissioner Annette L. Nazareth
Robert L. D. Colby, Deputy Director, Division of Market Regulation
Robert R. Glauber, NASD Chairman and CEO
Mary L. Schapiro – NASD Vice Chairman