

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-62524; File No. SR-BATS-2010-008)

July 16, 2010

Self-Regulatory Organizations; BATS Exchange, Inc.; Order Approving Proposed Rule Change, as Modified by Amendment No. 1 Thereto, to Amend BATS Rules 2.5 and 17.2 to Establish a Registration Requirement for Principals

I. Introduction

On April 9, 2010, BATS Exchange, Inc. (“BATS” or “Exchange”) filed with the Securities and Exchange Commission (“Commission”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹ and Rule 19b-4 thereunder,² a proposed rule change to amend its registration requirements in Rules 2.5 and 17.2. The proposed rule change was published for comment in the Federal Register on April 29, 2010.³ The Commission received one comment letter on the proposal.⁴ The Exchange responded on June 29, 2010.⁵ On June 30, 2010, the Exchange submitted Amendment No. 1 to the proposed rule change.⁶ This order approves the proposed rule change as modified by Amendment No. 1.

II. Description of the Proposal

BATS proposes to amend BATS Rule 2.5, entitled “Restrictions,” to require each Exchange member to register with the Exchange: (i) at least two principals to supervise

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Securities Exchange Act Release No. 61960 (April 22, 2010), 75 FR 22668.

⁴ See letter from Joan C. Conley, Senior Vice President and Corporate Secretary, Nasdaq OMX, to Elizabeth M. Murphy, Secretary, Commission, dated May 20, 2010 (“Nasdaq Comment Letter”).

⁵ See letter from Eric J. Swanson, Senior Vice President and General Counsel, BATS Exchange, Inc., to Elizabeth M. Murphy, Secretary, Commission, dated June 29, 2010 (“BATS Response Letter”).

⁶ Amendment No. 1 is a technical amendment and thus not subject to notice and comment.

Authorized Traders of the member (subject to certain exceptions), one of whom must be the member's chief compliance officer, and (ii) at least one financial and operations principal.⁷

BATS Rule 2.5

BATS Rule 2.5 states that the General Securities Representative exam ("Series 7") is required for registration with the Exchange as an Authorized Trader. The term "Authorized Trader" is defined as "a person who may submit orders (or who supervises a routing engine that may automatically submit orders) to the Exchange's trading facilities on behalf of his or her member or sponsored participant." Accordingly, all traders that participate in the routing of orders to the Exchange, including proprietary traders, are required to be registered with the Exchange and Series 7 qualified. The term Authorized Trader includes a trader that submits orders, or supervises a routing engine that automatically submits orders, to the Exchange's equities platform, options platform, or both.

With this rule change, BATS proposes to require each member to register with the Exchange at least two principals qualified as General Securities Principals⁸ ("Series 24") (subject to certain exceptions) to supervise the member's Authorized Traders and one principal qualified as a Limited Principal–Financial and Operations ("Series 27") to supervise the financial and operational activities of the member ("FINOP"). In addition, the proposal would require each chief compliance officer designated on Schedule A of Form BD to register with the Exchange as a Series 24 qualified principal.⁹

⁷ The Exchange also proposes a technical amendment to BATS Rule 17.2(g)(4) to eliminate language that will become unnecessary due to the changes to BATS Rule 2.5.

⁸ In order to register as a principal, one must first be registered as a representative.

⁹ In Amendment No. 1, the Exchange amended this portion of its rule to more closely mirror the rules of other SROs that require the chief compliance officers of their members to be registered. See, e.g., NASDAQ Rule 1022(a); NASDAQ BX Rule 1022(a); FINRA Rule 1022(a); NYSE Arca Equities Rule 6.18(d). The amendment also deleted a

BATS proposes certain exceptions to the requirements that a member register two Series 24 qualified principals and one Series 27 qualified principal. First, the Exchange proposes that any member with 25 or fewer Authorized Traders that meets the definition of a “proprietary trading firm,” have at least one Series 24 registered principal. Second, under the proposed rule, the Exchange may waive the requirement to register two Series 24 qualified principals if the member can conclusively indicate that a waiver is warranted under the circumstances. With respect to the FINOP requirement, the Exchange may waive the requirement to register a Series 27 qualified FINOP if such registration is not required by the member’s designated examining authority.¹⁰

BATS Rule 17.2

Any member that conducts business on the Exchange as an Options Member is required by BATS Rules 17.1(b) and 17.2(g) to register an Options Principal with the Exchange who is responsible for that Member’s options related activities on the Exchange. The Options Principal must qualify by passing the Registered Options Principal exam (“Series 4”). Accordingly, the proposed rule makes clear that paragraph (d) does not apply to a member that solely conducts business on the Exchange as an Options Member, and thus, that such a member is not also required to register Series 24 qualified principals with the Exchange.

In addition to adopting the principal registration requirements described above, the Exchange proposes modifications to Interpretation and Policy .02, which currently requires

definition of “customer” for purposes of proposed paragraph (g) that would have permitted a firm to have broker-dealer customers and still qualify as a “proprietary trading firm” for the purpose of the rule.

¹⁰ BATS indicated that it did not want to independently require a member to have a FINOP. All members of BATS must be members of another SRO. See BATS Rule 2.5(4). The Commission understands that the vast majority of BATS members are also members of FINRA. All members of FINRA that are subject to Rule 15c3-1 under the Act must have a FINOP.

Authorized Traders to complete continuing education requirements similar to those required by other national securities exchanges. Due to the addition of the principal registration requirements described above and the recent addition of an options principal requirement, the Exchange proposes to clarify that all Authorized Traders, principals, financial/operations principals and options principals are subject to continuing education requirements in order to maintain registration with the Exchange.¹¹

Deadline for Compliance

The Exchange has proposed a compliance date of September 30, 2010.

III. Comment Letter and BATS's Response

The Commission received one comment letter on the proposed rule change.¹² The commenter believed that BATS's requirement to register Authorized Traders is narrower than FINRA Rule 1031 which addresses registration of representatives. The commenter expressed concern that BATS's registration requirements for Authorized Traders excepted other associated persons that FINRA requires to be registered, and that only those persons supervising Authorized Traders would be required to register as a principal. The commenter also questioned BATS's requirement to register at least one FINOP, citing FINRA Rule 1022(b) which requires any person with a FINOP's responsibilities to register, including the chief financial officer.

In the BATS Response Letter,¹³ BATS explained that its registration rules, in particular, were tailored to ensure the qualification and competence of individuals responsible for sending orders to BATS and their supervisors. However, BATS stated that its rules, overall, apply to its

¹¹ The Exchange thus proposes to delete language from BATS Rule 17.2(g)(4) that states that an options principal is subject to continuing education requirements.

¹² See supra note 4.

¹³ See supra note 5.

members and their associated persons, not just Authorized Traders and those supervising them. In addition, BATS explained that, under its proposed rule, a FINOP is responsible for ensuring that a member firm complies with applicable financial and operational requirements, including those relating to the submission of financial reports and the maintenance of books and records. BATS stated that it is not requiring the chief financial officer to assume this responsibility as this person may not be the best person suited to be a FINOP, and is instead allowing the member firm to decide who needs to be registered as a FINOP.

The Commission believes it is reasonable for BATS to limit the application of its registration, examination, and continuing education requirements to those associated persons who conduct a securities business through BATS or who supervise such activity. BATS has represented that the scope of these requirements encompasses all associated persons entering orders at BATS, which the Commission believes provides appropriate breadth of coverage.

IV. Discussion and Commission Findings

The Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange.¹⁴ Specifically, the Commission finds that the proposal is consistent with Section 6(b)(5) of the Act,¹⁵ which requires, among other things, that the rules of a national securities exchange be designed to prevent fraudulent and manipulative acts and practices, 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. The Commission believes that the proposed rule change is also consistent with Section

¹⁴ In approving this proposed rule change, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

¹⁵ 15 U.S.C. 78f(b)(5).

6(c)(3)(B) of the Act,¹⁶ which authorizes exchanges to prescribe standards of training, experience and competence for persons associated with exchange members, and gives exchanges the authority to bar a natural person from becoming a member or a person associated with a member, if the person does not meet the standards of training, experience and competence prescribed in the rules of the exchange. The Commission believes that the changes proposed by BATS to its rules will enhance the ability of member firms to comply with the Exchange's rules as well as with the Federal Securities laws.

Specifically, broker-dealers are required to supervise the activities of their associated persons.¹⁷ The associated persons of broker-dealers must register with the exchanges. Broker-dealers and exchanges have responsibilities under the Act with respect to statutorily disqualified persons who seek to associate with a member firm.¹⁸

In order to meet its obligations under Section 6 of the Act¹⁹ to enforce compliance by member firms and their associated persons with the Act, the rules thereunder, and the exchange's own rules, an exchange must have baseline registration and examination or qualification requirements for all persons conducting business on an exchange, as well as for those supervising such activity. In addition, most SROs have continuing education requirements for registered persons which help ensure that associated persons are up to date on changes to rules and regulations that govern their activities. Furthermore, an exchange must know if an

¹⁶ 15 U.S.C. 78f(c)(3)(B).

¹⁷ See Section 15(b)(4)(E) of the Act.

¹⁸ See Section 6(c)(2) of the Act and Rule 19h-1 under the Act.

¹⁹ Section 6 requires exchanges to have the ability to enforce compliance by their members and associated persons with the federal securities laws and with their own rules. 15 U.S.C. 78f.

associated person of a member firm is subject to a statutory disqualification.²⁰ This information is elicited by the Uniform Application for Securities Industry Registration or Transfer (“Form U4”), which is used by most exchanges and FINRA to register associated persons.

The Commission believes that the requirement that firms have a minimum of two principals responsible for oversight of Authorized Traders and activity on BATS who must be registered and pass the Series 24 exam should help BATS strengthen the regulation of its member firms. Requiring a minimum of two persons, both of whom meet specified proficiency standards, should help ensure that member firms have adequate supervision, and that those overseeing member firms are prepared for the responsibility. The nature of the firm, however, may dictate that more than two principals are needed to provide appropriate supervision. In addition, the Commission believes that requiring chief compliance officers and any employee operating in the capacity of a FINOP to register with the Exchange as principals and take either the Series 24 or Series 27, respectively, is appropriate based on the heightened level of accountability inherent in the duty of overseeing compliance by an Exchange member, and in the oversight and preparation of financial reports and the oversight of those employed in the financial and operational capacities at each firm.

The Commission believes BATS’s proposed exceptions from the above requirements are appropriate. The Commission notes that a member seeking a waiver from BATS’s FINOP requirement must prove that it has satisfied the financial and operational requirements of its

²⁰ In addition, the Commission believes that it is important to ensure that information, such as whether an associated person is subject to a statutory disqualification, is available to exchanges and other regulators, including the Commission and the state securities regulators, through FINRA’s Central Registration Depository System (“WebCRD”) as well as members of the public through BrokerCheck, which derives information from WebCRD.

designated examining authority applicable to registration.²¹ Additionally, any member seeking an exception from BATS's requirement that each firm have two principals must provide evidence that conclusively indicates to the Exchange that only one principal is necessary. The Commission expects this authority to be used sparingly as principals are charged with oversight of the operations of member firms, and provide the first line of defense in ensuring that member firms are complying with the rules of the exchange as well as the federal securities laws.

Additionally, the Commission believes that the proposed rule change is consistent with the principles of Section 11A(a)(1)²² of the Act in that it seeks to assure fair competition among brokers and dealers and among exchange markets. The Commission believes that the proposed rule will promote uniformity of regulation across markets, thus reducing opportunities for regulatory arbitrage. BATS' proposed rule change helps ensure that all persons conducting a securities business through BATS are appropriately supervised, as the Commission expects of all SROs. In addition, the exceptions to the general rules in BATS's proposed rule change are substantively the same as exceptions provided to similar rules at other SROs.

Finally, the Commission believes that the compliance date proposed by the Exchange of September 30, 2010 will provide the Exchange's members adequate time to pass any qualification examinations necessary to become compliant with the proposed rules.

²¹ See footnote 10 *infra*.

²² 15 U.S.C. 78k-1(a)(1).

VI. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,²³ that the proposed rule change (SR-BATS-2010-008), as modified by Amendment No. 1, be, and hereby is, approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.²⁴

Florence E. Harmon
Deputy Secretary

²³ 15 U.S.C. 78s(b)(2).

²⁴ 17 CFR 200.30-3(a)(12).