SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-72346; File No. SR-BATS-2014-022)

June 9, 2014

Self-Regulatory Organizations; BATS Exchange, Inc.; Notice of a Proposed Rule Change to Amend the Competitive Liquidity Provider Program

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act"),[1] and Rule 19b-4 thereunder,[2] notice is hereby given that on June 3, 2014, BATS Exchange, Inc. ("Exchange" or "BATS") filed with the Securities and Exchange Commission ("Commission") the proposed rule change as described in Items I, II and III below, which Items have been prepared by the Exchange. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Self-Regulatory Organization's Statement of the Terms of Substance of the Proposed Rule Change

The Exchange is proposing to add an Interpretation and Policy .03 to Rule 11.8 entitled "Supplemental Competitive Liquidity Provider Program for Exchange Traded Products" to incentivize competitive and aggressive quoting by market makers registered with the Exchange ("Market Makers")[3] in Exchange-listed ETPs.[4] The Exchange is also proposing to make a corresponding amendment to Interpretation and Policy .02 to Rule 11.8, entitled "Competitive

1 15 U.S.C. 78s(b)(1).

2 17 CFR 240.19b-4.

3 As defined in BATS Rules, the term "Market Maker" means a Member that acts a as a market maker pursuant to Chapter XI of BATS Rules.

4 As proposed in Interpretation and Policy .03 (b)(4) to Rule 11.8, the term "ETP" includes Portfolio Depository Receipts, Index Fund Shares, Trust Issued Receipts, and Managed Fund Shares, which are defined in Rule 14.11(b), 14.11(c), 14.11(f), and 14.11(i), respectively, which the Exchange may propose to expand in the future as it adds products which may be listed on the Exchange. Any such expansion would require the Exchange to file a proposal with the Commission under Rule 19b-4 of the Act.

Liquidity Provider Program" in order to reflect the sunset of ETPs listed on the Exchange from the existing Competitive Liquidity Provider Program. The Exchange will implement the proposed rule change on a date that will be circulated in a notice from the BATS Trade Desk.

As proposed, the Supplemental Competitive Liquidity Provider Program for Exchange Traded Products (the "Program") set forth in Interpretation and Policy .03 to Rule 11.8 will operate for a one year pilot period beginning from the date of implementation of the program. During the pilot, the Exchange will periodically provide information to the Commission about market quality with respect to the Program.

The text of the proposed rule change is available at the Exchange's website at http://www.batstrading.com, at the principal office of the Exchange, and at the Commission's Public Reference Room.

II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the Exchange included statements concerning the purpose of and basis for the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified in Item IV below. The Exchange has prepared summaries, set forth in Sections A, B, and C below, of the most significant parts of such statements.

(A) Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

Background

On August 30, 2011, the Exchange received approval of rules applicable to the qualification, listing and delisting of securities of issuers on the Exchange.[5] More recently, the Exchange received approval to operate a program that is designed to incentivize certain Market Makers registered with the Exchange as Competitive Liquidity Providers to enhance liquidity on the Exchange in all Exchange-listed securities (the "CLP Program").[6] The Exchange subsequently adopted financial incentives for the CLP Program[7] and thereafter amended certain components of the CLP Program, including financial incentives and quoting requirements for Competitive Liquidity Providers in the CLP Program.[8] On April 17, 2014, the Exchange filed a proposal to create a new lead market maker ("LMM") program (the "LMM Program) in order to incentivize LMMs to provide liquidity in BATS-listed securities through the payment of enhanced rebates and/or reduced fees in the security for which they are an LMM, which it implemented on June 2, 2014.[9]

The purpose of this filing is to propose new Interpretation and Policy .03 to Rule 11.8, which is based substantially on the CLP Program, that seeks to incentivize certain market makers

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5 See Securities Exchange Act Release No. 65225 (August 30, 2011), 76 FR 55148 (September 6, 2011) (SR-BATS-2011-018).

6 See Securities Exchange Act Release No. 66307 (February 2, 2012), 77 FR 6608 (February 8, 2012) (SR-BATS-2011-051).

7 See Securities Exchange Act Release No. 66427 (February 21, 2012), 77 FR 11608 (February 27, 2012) (SR-BATS-2012-011).

8 See Securities Exchange Act Release Nos. 67854 (September 13, 2012), 77 FR 58198 (September 19, 2012) (SR-BATS-2012-036); 69190 (March 20, 2013), 78 FR 18384 (March 26, 2013) (SR-BATS-2013-005); 69857 (June 25, 2013), 78 FR 39392 (July 1, 2013) (SR-BATS-2013-037); 70865 (November 13, 2013), 78 FR 69509 (November 19, 2013) (SR-BATS-2013-057); and 71284 (January 10, 2014), 79 FR 2921 (January 16, 2014) (SR-BATS-2014-002).

9 See Securities Exchange Act Release No. 72020 (April 25, 2014), 79 FR 24807 (May 1, 2014) (SR-BATS-2014-015).

registered with the Exchange as Competitive Liquidity Providers ("ETP CLPs" or "CLPs")[10] to enhance liquidity on the Exchange in certain ETPs listed on the Exchange and thereby qualify to receive part of a daily rebate pursuant to the Program (a "CLP Rebate"). The Exchange plans to implement the Program and the corresponding amendments to existing Interpretation and Policy .02 to Rule 11.8 on a date that will be circulated in a notice from the BATS Trade Desk. The Exchange proposes to maintain existing Interpretation and Policy .02 in its current form until such implementation. The Exchange will notify all interested parties of the implementation date of these changes through a notice distributed to all Members of the Exchange. The Exchange is proposing to provide notice of the implementation date through a notice rather than implementing the changes to the rule immediately upon approval by the Commission in order to provide the Exchange with the flexibility necessary to ensure an uninterrupted transition from the CLP Program to the Program.

The Exchange proposes that the Commission approve the Program for a pilot period of one year from the date of implementation, which shall occur no later than 90 days after Commission approval of this proposal, the date of which will be circulated in a notice from BATS Trade Desk. During the pilot, the Exchange will submit monthly reports to the Commission about market quality with respect to the Program. The monthly reports will endeavor to compare, to the extent practicable, securities before and after they are in the Program, including those securities that "graduate" from the Program or, where no securities have "graduated" from the Program, securities that have "graduated" from comparable programs

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10 As defined in proposed Interpretation and Policy .03 (b)(1) to Rule 11.8, the term "ETP CLP" means a Member that electronically enters proprietary orders into the systems and facilities of the Exchange and is obligated to maintain a bid or an offer at the NBBO in each assigned CLP Security in round lots consistent with paragraph (i) of Interpretation and Policy .03 to Rule 11.8.

at other exchanges to the extent that such securities exist, and will include information regarding the Program which will enable the Exchange and the Commission to better analyze the effectiveness of the Program, such as: (1) Rule 605 metrics;[11] (2) volume metrics; (3) number of CLPs in target securities; (4) spread size; and (5) availability of shares at the NBBO. The Exchange will endeavor to provide similar data to the Commission about comparable ETPs that are listed on the Exchange that are not in the Program; and any other Program related data requested by the Commission for the purpose of evaluating the efficacy of the Program. The Exchange will post the monthly reports on its website. The first report will be submitted within sixty days after the Program becomes operative.

Supplemental Competitive Liquidity Provider Program for Exchange Traded Products

The Exchange is proposing to adopt a new rule titled "Supplemental Competitive Liquidity Provider Program for Exchange Traded Products" as Interpretation and Policy .03 to Rule 11.8. The Program is designed to promote market quality in CLP Securities[12] by allowing a CLP Company[13] to list an eligible CLP Security[14] on the Exchange and, in addition to paying the standard (non-CLP) listing fee as set forth in the fee schedule, a Sponsor[15] may pay a fee (a "CLP Fee") in order for the CLP Company, on behalf of a CLP Security, to participate in the

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11 17 CFR 242.605.

12 The Exchange notes that CLP Securities do not encompass derivatives on such securities.

13 As defined in proposed Interpretation and Policy .03 (b)(2) to Rule 11.8, the term "CLP Company" means the trust or company housing the ETP or, if the ETP is not a series of a trust or company, then the ETP itself.

14 As defined in proposed Interpretation and Policy .03 (b)(3) to Rule 11.8, the term "CLP Security" means an issue of or series of ETP securities issued by a CLP Company that meets all of the requirements to be listed on the Exchange pursuant to Rule 14.11.

15 As defined in proposed Interpretation and Policy .03 (b)(5) to Rule 11.8, Sponsor means the registered investment adviser that provides investment management services to a CLP Company or any of such adviser's parents or subsidiaries.

Program, which will be credited to the BATS General Fund. The Exchange will then pay the CLP Rebate out of the BATS General Fund in order to incentivize CLPs in the CLP Security to quote aggressively in the CLP Security by providing a CLP Rebate to one or more CLPs that make a quality market in the CLP Security pursuant to the Program.[16]

The Exchange believes that the Program will be beneficial to the financial markets, to market participants including traders and investors, and to the economy in general. First, the Program will encourage narrow spreads and liquid markets in securities that generally have not been, or may not be, conducive to naturally having such narrow spreads and liquidity. These securities may include less actively traded or less well known ETPs that are made up of securities of less well known or start-up companies as components.[17] Second, in rewarding market makers that are willing to help to develop liquid markets for CLP Securities subject to the Program,[18] the Program would benefit traders and investors by encouraging more quote competition, narrower spreads, and greater liquidity. Third, the Program will lower transaction costs and enhance liquidity in both ETPs and their components, making those securities more

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16 The enhanced market quality (e.g., liquidity) would, as discussed below, be identical to the existing CLP Quoting Requirements in Interpretation and Policy .02 (g) to Rule 11.8. These standards include, for example, posting at least five round lots in a CLP Security at the NBB or NBO at the time of a SET in order to have a Winning Bid SET or Winning Offer SET, respectively, as well as requiring that a CLP is quoting at least a round lot at a price at or within 1.2% of the CLP's bid (offer) at the time of the SET in order to have a Winning Bid (Offer) Set. Proposed Interpretation and Policy .03 (i) to Rule 11.8.

17 These small companies and their securities (whether components of listed products like ETPs or direct listings) have been widely recognized as essential to job growth and creation and, by extension, the health of the economy. Being included in a successful ETP can provide the stocks of these companies with enhanced liquidity and exposure, enabling them to attract investors and access capital markets to fund investment and growth.

18 By imposing quality quoting requirements to enhance the quality of the market for CLP Securities, the Program will directly impact one of the ways that market makers manage risk in lower tier or less liquid securities (e.g. the width of bid and offer pricing).

attractive to a broader range of investors. In so doing, the Program will help companies access capital to invest and grow.

Securities Eligible for the Program

The Exchange is proposing that any CLP Company, on behalf of a CLP Security, shall be eligible for the Program, as long as: (i) the Exchange has accepted the Program application of the CLP Company with respect to the CLP Security and the Exchange has accepted the Program application of at least one CLP in the CLP Security; (ii) the CLP Security meets all requirements to be listed on the Exchange as an ETP; (iii) the CLP Security meets all Exchange requirements for continued listing at all times the CLP Security participates in the Program; (iv) while the CLP Security is participating in the Program, on a product-specific website, the CLP Company is indicating that the product is in the Program and provides a link to the Exchange's Program website; and (v) the security has a consolidated average daily volume ("CADV") of less than 1 million shares for at least one of the past three calendar months, however any CLP Security initially listed on the Exchange shall be eligible for the Program for the first six months that it is listed on the Exchange, regardless of the ETP's CADV. Notwithstanding the foregoing, the Exchange is proposing that an ETP participating in the Competitive Liquidity Provider Program under Exchange Rule 11.8 Interpretation and Policy .02 (the ".02 Program") shall not be eligible for participation in the Program until and unless such ETP is no longer participating in the .02 Program.[19]

Application

The Exchange is proposing that any entity that wishes to participate in the Program must submit an application in the form prescribed by the Exchange, which includes both CLP

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19 Proposed Interpretation and Policy .03 (d)(1) and (d)(3) to Rule 11.8.

Companies on behalf of a CLP Security and CLPs.[20]

CLPs

To become a CLP, a Member must submit a CLP application form with all supporting documentation to the Exchange. As is currently the case for membership applications to join the Exchange and applications to register as market makers on the Exchange, Exchange personnel in the Exchange's membership department will process such applications. Exchange personnel will determine whether an applicant is qualified to become a CLP based on the qualifications described below. After an applicant submits a CLP application to the Exchange, with supporting documentation, the Exchange shall notify the applicant Member of its decision. If an applicant is approved by the Exchange to receive CLP status, such applicant must establish connectivity with relevant Exchange systems before such applicant will be permitted to trade as a CLP on the Exchange. In the event an applicant is disapproved by the Exchange, such applicant may seek review under Chapter X of the Exchange's Rules governing adverse action and/or reapply for CLP status at least three (3) calendar months following the month in which the applicant received the disapproval notice from the Exchange. Chapter X of the Exchange's Rules provides any persons who are or are about to be aggrieved by an adverse action taken by the Exchange with a process to apply for an opportunity to be heard and to have the complained of action reviewed.[21]

To qualify as a CLP, a Member will be required to be a registered Market Maker in good standing with the Exchange consistent with Rules 11.5 through 11.8. Further, the Exchange will require each Member seeking to qualify as a CLP to have and maintain: (1) adequate technology

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20 Proposed Interpretation and Policy .03 (c)(1) to Rule 11.8.

21 Proposed Interpretation and Policy .03 (g) to Rule 11.8.

to support electronic trading through the systems and facilities of the Exchange; (2) one or more unique identifiers that identify to the Exchange CLP trading activity in assigned CLP Securities;[22] (3) adequate trading infrastructure to support CLP trading activity, which includes support staff to maintain operational efficiencies in the Program and adequate administrative staff to manage the Member's participation in the Program; (4) quoting and volume performance that demonstrates an ability to meet the CLP quoting requirement in each assigned CLP Security on a daily and monthly basis; and (5) a disciplinary history that is consistent with just and equitable business practices[23] These requirements are identical to those of the existing CLP Program.[24]

Withdrawal and Renewal

The Exchange is proposing that any entity that wishes to withdraw from the Program must provide written notice to the Exchange, however, the requirements for CLPs and CLP Companies on behalf of CLP Securities are different, as further explained below.

CLPs

A CLP may withdraw from the status of a CLP by providing written notice to the Exchange. Such withdrawal shall become effective when those CLP Securities assigned to the withdrawing CLP are reassigned to another CLP. After the Exchange receives the notice of withdrawal from the withdrawing CLP, the Exchange will reassign such CLP Securities as soon

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22 As proposed, a Member may not use such unique identifiers for trading activity at the Exchange in assigned CLP securities that is not CLP trading activity, but may use the same unique identifiers for trading activity in securities not assigned to a CLP. If a Member does not identify to the Exchange the unique identifier to be used for CLP trading activity, the Member will not receive credit for such CLP trading.

23 Proposed Interpretation and Policy .03 (f) to Rule 11.8.

24 See Interpretation and Policy .02 (c) and (e) to Rule 11.8.

as practicable but no later than thirty (30) days after the date said notice is received by the Exchange. In the event the reassignment of CLP Securities takes longer than the 30-day period, the withdrawing CLP will have no obligations under this Interpretation and Policy .03 and will not be held responsible for any matters concerning its previously assigned CLP Securities upon termination of this 30-day period.[25]

CLP Securities

A CLP Company may, on behalf of a CLP Security, after being in the Program for not less than two consecutive quarters, but less than one year, voluntarily withdraw from the Program on a quarterly basis. The CLP Company must notify the Exchange in writing, not less than one month prior to withdrawing from the Program. The Exchange, however, does retain discretion to allow a CLP Company to withdraw from the Program earlier than required above. In making such decision, the Exchange may take into account the volume and price movements in the CLP Security; the liquidity, size quoted, and quality of the market in the CLP Security; and any other relevant factors. After a CLP Security is in the Program for one year or more, the CLP Company may voluntarily withdraw from the Program on a monthly basis, so long as the CLP Company notifies the Exchange in writing not less than one month prior to withdrawing from the Program.[26]

After a CLP Company, on behalf of a CLP Security, is in the Program for one year, the Program and all obligations and requirements of the Program will automatically continue on an annual basis unless: (1) the Exchange terminates the Program by providing not less than one month prior notice of intent to terminate or the pilot Program is not extended or made permanent

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[25] Proposed Interpretation and Policy .03 (h) to Rule 11.8.

[26] Proposed Interpretation and Policy .03 (c)(2) to Rule 11.8.

pursuant to a proposed rule change subject to filing with or approval by the Commission; (2) the CLP Company withdraws from the Program pursuant to the withdrawal rules described above; or (3) the CLP Company is terminated from the Program pursuant to subsection (n) of the proposal.[27]

CLP Company Fees

A CLP Company seeking to participate in the Program shall incur an annual basic CLP Fee of $10,000 per CLP Security. The basic CLP Fee must be paid to the Exchange prospectively on a quarterly basis.[28]

A CLP Company may also incur an annual supplemental CLP Fee per CLP Security. The basic CLP Fee and supplemental CLP Fee, when combined, may not exceed $100,000 per year. The supplemental CLP Fee is a fee selected by a CLP Company on an annual basis, if at all. The supplemental CLP Fee must be paid to the Exchange prospectively on a quarterly basis. The amount of the supplemental CLP Fee, if any, will be determined by the CLP Company initially per CLP Security and will remain the same for the period of a year. The Exchange will provide notification on its website regarding the amount, if any, of any supplemental CLP Fee

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27 Interpretation and Policy .03 (n) to Rule 11.8 states that the Program will terminate with respect to a CLP Security under the following circumstances: (A) A CLP Security sustains a CADV of one million shares or more for three consecutive months, however, any CLP Security initially listed on the Exchange shall be eligible for the Program for the first six months that it is listed on the Exchange, regardless of the ETP's CADV; (B) A CLP Company, on behalf of a CLP Security, withdraws from the Program, is no longer eligible to be in the Program pursuant to this rule, or its Sponsor ceases to make CLP Fee payments to the Exchange; (C) A CLP Security is delisted or is no longer eligible for the Program; or (D) A CLP Security does not, for two consecutive quarters, have at least one CLP that is eligible for CLP Rebate. It should be noted, however, that termination of a CLP Company, CLP Security, or CLP does not preclude the Exchange from allowing re-entry into the Program where the Exchange deems such re-entry as proper.

28 Proposed Interpretation and Policy .03 (d)(2)(A) to Rule 11.8.

determined by a CLP Company per CLP Security.[29]

The CLP Fee is in addition to the standard (non-CLP) Exchange listing fee applicable to the CLP Security and does not offset such standard listing fee.[30] For a CLP Security housed by a CLP Company that has a Sponsor or Sponsors, the CLP Fee with respect to the CLP Security shall be paid by the Sponsor or Sponsors of such CLP Security. The Exchange will prospectively bill each CLP Company for the quarterly CLP Fee for each CLP Security.[31] CLP Fees (both basic and supplemental) will be credited to the BATS General Fund.

CLP Quoting Requirements

CLPs will be subject to both a daily quoting requirement in order to be eligible to receive financial incentives and a monthly quoting requirement in order to remain qualified as a CLP. These quoting requirements are identical to the quoting requirements of the Exchange's existing CLP Program.[32] Any CLP that meets the daily quoting requirement set forth below will be eligible to receive a portion of the CLP Rebate for each day's quoting activity. A CLP that does not meet the CLP monthly quoting requirement is subject to the non-regulatory penalties described below.

The Exchange will continue to measure the performance of a CLP in CLP Securities by calculating Size Event Tests ("SETs") between 9:25 a.m. and 4:05 p.m. on every day on which the Exchange is open for business. The Exchange will measure each CLP's quoted size, excluding odd lots, at the NBB and NBO at least once per second to determine SETs. The three

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[29] Proposed Interpretation and Policy .03 (d)(2)(B) to Rule 11.8.

[30] Proposed Interpretation and Policy .03 (d)(2)(C) to Rule 11.8. The CLP Fee with respect to an ETP shall be paid by the Sponsor(s) of such ETP.

[31] Proposed Interpretation and Policy .03 (d)(2)(D) to Rule 11.8.

[32] See Interpretation and Policy .02 (g) to Rule 11.8.

CLPs with the greatest aggregate size at the NBB and the three CLPs with the greatest aggregate size at the NBO at the time of each SET will be considered to have a Winning Bid SET[33] and a Winning Offer SET[34] (collectively, "Winning SETs"), respectively. Where there is a tie, all CLPs with the same aggregate size at the NBB (NBO) will be considered to have a Winning Bid (Offer) SET if there are two or less CLPs that have greater aggregate size at the NBB (NBO). Additionally, all CLPs with a Winning SET will be awarded SET Credits based on the following: all CLPs with the greatest aggregate size at the NBB or NBO will receive three SET Credits; all CLPs with the second greatest aggregate size at the NBB or NBO will receive two SET Credits; and all CLPs with the third greatest aggregate size at the NBB will receive one SET Credit.

For example:

CLP	Shares at NBB
CLP1	1,000
CLP2	900
CLP3	800
CLP4	800

Here, all four CLPs will have a Winning Bid SET because CLP1 and CLP2 are both two of the top three CLPs with the greatest aggregate size at the NBB, while CLP3 and CLP4 are tied at 800 shares and there are only two CLPs that have greater aggregate size at the NBB than 800 shares. CLP1 would receive three Bid SET Credits, CLP2 would receive two Bid SET Credits, and CLP3 and CLP4 would each receive one Bid SET Credit.

However, if CLP3 had 900 shares at the NBB and all other CLPs remained the same, only CLP1, CLP2, and CLP3 would have a Winning SET because CLP2 and CLP3 would be tied and there is only one CLP that has greater aggregate size than 900 shares (CLP1). CLP4

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33 As defined in proposed Interpretation and Policy .03 (i)(1) to BATS Rule 11.8.

34 Id.

would have the fourth greatest aggregate size at the NBB among CLPs and thus would not qualify for a Winning SET. In this instance, CLP1 would receive three Bid SET Credits, CLP2 and CLP3 would each receive two Bid SET Credits, and CLP4 would not receive any Bid SET Credits.

Finally, if CLP1, CLP2, CLP3, and CLP4 all had 1,000 shares at the NBB, the four CLPs would each receive three Bid SET Credits. In this scenario, if another CLP ("CLP5") had 900 shares at the NBB, CLP5 would not qualify for a Winning SET and would not receive any Bid SET Credits because more than two CLPs have greater aggregate size at the NBB than the 900 shares posted by CLP5. The above examples would operate in an identical fashion for the NBO.).[sic][35]

In order to meet the daily quoting requirement, a CLP must have Winning Bid SETs or Winning Offer SETs equal to at least 10% of the total Bid SETs or total Offer SETs, respectively, on any trading day in order to be eligible for any CLP Rebate (each such CLP, an "Eligible CLP") for a CLP Security, as is also required under the existing CLP Program.[36] Eligible CLPs will be ranked according to the number of Bid SET Credits and Offer SET Credits each trading day, and only the Eligible CLP or Eligible CLPs ranked number one and the Eligible CLP or Eligible CLPs ranked number two in each of the Bid SET Credits and Offer SET Credits will receive the CLP Rebate. [37]

In order to meet the monthly quoting requirements, a CLP must be quoting at the NBB or

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[35] Proposed Interpretation and Policy .03 (i)(1) to Rule 11.8.

[36] <u>See</u> Interpretation and Policy .02 (g)(1)(A) to Rule 11.8.

[37] Proposed Interpretation and Policy .03 (i)(1)(A) to Rule 11.8.

the NBO 10% of the time that the Exchange calculates SETs.[38]

As is also required under the Exchange's existing CLP Program, a CLP must be quoting, at a minimum, five round lots (usually 500 shares), excluding odd lots, of the CLP Security, at the NBB or NBO, respectively, at the time of a SET in order to have a Winning Bid SET or a Winning Offer SET. Such quoting requirements will be measured by utilizing the unique identifiers that the Member has identified for CLP trading activity.[39] In addition, during Regular Trading Hours[40] a CLP must also be quoting at least a displayed round lot offer, excluding odd lots, at a price at or within 1.2% of the CLP's bid at the time of the SET in order to have a Winning Bid SET.[41] Similarly, during Regular Trading Hours, a CLP must be quoting at least a displayed round lot offer, excluding odd lots, at a price at or within 1.2% of the CLP's offer at the time of the SET in order to have a Winning Offer Set.[42]

For purposes of calculating whether a CLP is in compliance with its CLP quoting requirements, the CLP must post displayed liquidity in round lots in its assigned CLP Securities at the NBB or the NBO.[43] A CLP may post non-displayed liquidity; however, such liquidity will not be counted as credit towards the CLP quoting requirements. The CLP shall not be subject to any minimum or maximum quoting size requirement in assigned CLP Securities apart from the requirement that an order be for at least one round lot. The CLP quoting requirements will be measured by utilizing the unique identifiers that the Member has identified for CLP trading

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38 Proposed Interpretation and Policy .03 (i)(1)(B) to Rule 11.8.

39 Proposed Interpretation and Policy .03 (i)(4) to Rule 11.8.

40 As defined in BATS Rule 1.5(w), the term "Regular Trading Hours" means the time between 9:30 a.m. and 4:00 p.m. Eastern Time.

41 Proposed Interpretation and Policy .03 (i)(5) to Rule 11.8.

42 Id.

43 Proposed Interpretation and Policy .03 (i)(2) to Rule 11.8.

activity.

CLP Rebate

As described above, pursuant to the Program, the Exchange will measure the performance of CLPs in CLP Securities by calculating SETs between 9:25 a.m. and 4:05 p.m. on every day on which the Exchange is open for business. Each day, one quarter of the total annual CLP Fees (basic and supplemental combined) for the CLP Security divided by the number of trading days in the current quarter will constitute the total CLP Rebate for the CLP Security. For instance, where the total CLP Fees for a CLP Security is $64,000 and there are 64 trading days in the current quarter, the total CLP Rebate for the CLP Security would be $250 [($64,000/4)/64].[44]

Accordingly, the two Eligible CLPs with the most Bid SET Credits will split half of the daily CLP Rebate for the CLP Security ("Bid Rebate"), with the Eligible CLP with the most Bid SET Credits receiving 60% of the daily Bid Rebate and the Eligible CLP with the second most Bid SET Credits receiving 40% of the daily Bid Rebate.[45] Similarly, the two Eligible CLPs with the most Offer SET Credits will split half of the daily CLP Rebate for the CLP Security ("Offer Rebate"), with the Eligible CLP with the most Offer SET Credits receiving 60% of the daily Offer Rebate and the Eligible CLP with the second most Offer SET Credits receiving 40% of the daily Offer Rebate.[46] In the event that there is only one Eligible CLP for the Bid (Offer) Rebate for a CLP Security, such Eligible CLP will receive 100% of the Bid (Offer) Rebate. In the event that multiple Eligible CLPs have an equal number of Bid (Offer) SET Credits, the Eligible CLP with the highest executed volume in the CLP Security will be awarded the greater portion of the

44 Proposed Interpretation and Policy .03 (m)(1) to Rule 11.8.

45 Id.

46 Id.

Bid (Offer) Rebate. Specifically, this means that if the tie is for the most Bid (Offer) SET Credits, the Eligible CLP with the highest executed volume in the CLP Security will receive 60% and the Eligible CLP with the second highest executed volume in the CLP Security will receive 40% and no other Eligible CLPs will receive any portion of the Bid (Offer) Rebate. Similarly, where the tie is for the second most Bid (Offer) SET Credits, the Eligible CLP with the highest executed volume in the CLP Security will receive 40% of the Bid (Offer) Rebate and no other Eligible CLPs with equal or less Bid (Offer) SET Credits will receive any portion of the Bid (Offer) Rebate. Where no CLPs are eligible for the Bid (Offer) Rebate, no Bid (Offer) Rebate will be awarded to any CLP and no refund will be provided.[47]

Assignment of CLP Securities

The Exchange, in its discretion, will assign to the CLP one or more CLP Securities for CLP trading purposes. The Exchange shall determine the number of CLP Securities assigned to each CLP. The Exchange, in its discretion, will assign one (1) or more CLPs to each CLP Security subject to the Program, depending upon the trading activity of the CLP Security.[48] CLPs may only enter orders electronically directly into Exchange systems and facilities designated for this purpose. All CLP orders must only be for the proprietary account of the CLP Member.

Non-Regulatory Penalties

If a CLP fails to meet the CLP quoting requirements, the Exchange may impose certain non-regulatory penalties. First, if, between 9:25 a.m. and 4:05 p.m. on any day on which the Exchange is open for business, a CLP fails to meet its daily quoting requirement by failing to

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[47] Id.

[48] Proposed Interpretation and Policy .03 (j)(1) to Rule 11.8.

have at least 10% of the Winning SETs for that trading day, the CLP will not be eligible to receive the CLP Rebate for that day's quoting activity in that particular assigned CLP Security. Second, if a CLP fails to meet its monthly quoting requirement for three (3) consecutive months in any assigned CLP Security, the CLP will be at risk of losing its CLP status. Thus, the Exchange may, in its discretion, take the following non-regulatory actions: (i) revoke the assignment of the affected CLP Security(ies) and/or one or more additional unaffected CLP Securities; or (ii) disqualify a Member's status as a CLP.[49]

The Exchange shall determine if and when a Member is disqualified from its status as a CLP. One (1) calendar month prior to any such determination, the Exchange will notify the CLP of such impending disqualification in writing. If the CLP fails to meet the monthly quoting requirements as described above for a third consecutive month in a particular CLP Security, the CLP may be disqualified from CLP status. When disqualification determinations are made, the Exchange will provide a disqualification notice to the Member informing such Member that it has been disqualified as a CLP.[50] In the event a Member is disqualified from its status as a CLP, such Member may re-apply for CLP status. Such application process shall occur at least three (3) calendar months following the month in which such Member received its disapproval or disqualification notice. Further, in the event a Member is determined to be ineligible for the CLP Rebate for failure to meet its daily quoting obligation or is disqualified from its status as a CLP, such Member may seek review under Chapter X of the Exchange's Rules governing adverse action.[51] As noted above, Chapter X of the Exchange's Rules provides any persons who are or

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[49] Proposed Interpretation and Policy .03 (l)(1) to Rule 11.8.

[50] Proposed Interpretation and Policy .03 (l)(2) to Rule 11.8.

[51] Proposed Interpretation and Policy .03 (l)(3) to Rule 11.8.

are about to be aggrieved by an adverse action taken by the Exchange with a process to apply for an opportunity to be heard and to have the complained of action reviewed.

Website Disclosures

In order to provide transparency into the Program, including CLPs, CLP Companies, and the CLP Securities that are listed on the Exchange, the Exchange proposes to provide notification on its website regarding the following: (i) acceptance of a CLP Company, on behalf of a CLP Security, and a CLP into the Program; (ii) the total number of CLP Securities that any one CLP Company may have in the Program; (iii) the names of CLP Securities and the CLP(s) in each CLP Security, the dates that a CLP Company, on behalf of a CLP Security, commences participation in and withdraws or is terminated from the Program, and the name of each CLP Company and its associated CLP Security or Securities; (iv) a statement about the Program that sets forth a general description of the Program as implemented on a pilot basis and a fair and balanced summation of the potentially positive aspects of the Program as well as the potentially negative aspects and risks of the Program, and indicates how interested parties can get additional information about products in the Program; and (v) the intent of a CLP Company, on behalf of a CLP Security, or CLP to withdraw from the Program, and the date of actual withdrawal or termination from the Program.[52]

In addition, a CLP Company that, on behalf of a CLP Security, is approved to participate in the Program shall issue a press release to the public when the CLP Company, on behalf of a CLP Security, commences or ceases participation in the Program. The press release shall be in a form and manner prescribed by the Exchange, and, if practicable, shall be issued at least two days before commencing or ceasing participation in the Program. The CLP Company shall

[52] Proposed Interpretation and Policy .03 (o) to Rule 11.8.

dedicate space on its website, or, if it does not have a website, on the website of the Sponsor of the CLP Security, that (i) includes any such press releases, and (ii) provides a hyperlink to the dedicated page on the Exchange's website that describes the Program.

Consistency with Regulation M.

Rule 102 of Regulation M prohibits an issuer from directly or indirectly attempting "to induce any person to bid for or purchase, a covered security during the applicable restricted period" unless an exemption is available.[53] For the reasons discussed below, the Exchange believes that exemptive relief from Rule 102 should be granted for the Program.

First, the Exchange notes that the Commission and its staff have previously granted relief from Rule 102 to a number of exchange traded products ("Existing Relief") in order to permit the ordinary operation of such exchange traded products.[54] In granting the Existing Relief, the Commission has relied in part on the exclusion from the provisions of Rule 102 provided by paragraph (d)(4) of Rule 102 for securities issued by an open-end management investment company or unit investment trust. In granting the Existing Relief from Rule 102 to other types of exchange traded products, for which the (d)(4) exception is not available, the staff has relied on (i) representations that the fund in question would continuously redeem exchange traded product shares in basket-size aggregations at their NAV and that there should be little disparity between the market price of an exchange traded product share and the NAV per share and (ii) a finding

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53 Rule 102 provides that "[i]n connection with a distribution of securities effected by or on behalf of an issuer or selling security holder, it shall be unlawful for such person, or any affiliated purchaser of such person, directly or indirectly, to bid for, purchase, or attempt to induce any person to bid for or purchase, a covered security during the applicable restricted period" unless an exception is available. See 17 CFR 242.102.

54 See, e.g., Letter from James A. Brigagliano, Acting Associate Director, Division of Market Regulation, to Stuart M. Strauss, Esq., Clifford Chance US LLP (October 24, 2006) (regarding class relief for exchange traded index funds).

that "[t]he creation, redemption, and secondary market transactions in [shares] do not appear to result in the abuses that Rules 101 and 102 of Regulation M were designed to prevent."[55] The crux of the Commission's findings in granting the Existing Relief rests on the premise that the prices of exchange traded product shares closely track their per-share NAVs. Given that the Program neither alters the derivative pricing nature of ETPs nor impacts the arbitrage opportunities inherent therein, the conclusion on which the Existing Relief is based remains unaffected by the Incentive Program. In this regard, most ETPs that would be eligible to participate in the Program would have previously been granted relief from Rule 102.

Second, the Program requires, among other things, that a CLP make two-sided quotes during Regular Trading Hours in order to have a Winning SET. The Program is not intended to raise ETP prices, but rather to improve market quality. In light of the derivative nature of ETPs, the Exchange does not expect that CLPs will quote outside of the normal quoting ranges for these products as a result of the CLP Rebate, but rather would quote within their normal ranges as determined by market factors. Indeed, the Program would not create any incentive for a CLP to quote outside such ranges.

Finally, the staff of the Exchange, which is a self-regulatory organization, would be interposed between the issuer and the CLP, administering a rules-based program with numerous structural safeguards described in the previous sections. Specifically, both CLPs and CLP Companies would be required to apply to participate in the Program and to meet certain standards. CLP Companies could not cause any fee to be paid to a CLP under the Program. The Exchange would collect the CLP Fees and credit them to the Exchange's General Fund. A CLP would be eligible to receive a CLP Rebate, again, from the Exchange's General Fund, only after

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55 See Rydex Specialized Products LLC, SEC No-Action Letter (June 21, 2006).

it qualified for the CLP Rebate, as described above. Such qualification standards are set and monitored by the Exchange. Application to, continuation in, and withdrawal from the Program would be governed by published Exchange rules and policies, and there would be extensive public notice regarding the Program and payments thereunder on both the Exchange's and the CLP Company's websites. Given these structural safeguards, the Exchange believes that payments under the Program are appropriate for exemptive relief from Rule 102.

In summary, the Exchange believes that exemptive relief from Rule 102 should be granted for the Program because, for example: (1) the Program would not create any incentive for a CLP to quote outside of the normal quoting ranges for the ETPs included therein; (2) the Program has numerous structural safeguards, such as the application process for CLP Companies and CLPs, the interpositioning of the Exchange between CLP Companies and CLPs, and significant public disclosure surrounding the Program; and (3) the Program does not alter the basis on which Existing Relief is based and, furthermore, most ETPs that would be eligible to participate in the Program would have previously been granted relief from Rule 102.[56]

<u>Surveillance</u>

The Exchange believes that its surveillance procedures are adequate to properly monitor the trading of all securities trading on the Exchange, including ETPs participating in the

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[56] The Exchange notes that the Commission granted a limited exemption from Rule 102 of Regulation M to The NASDAQ Stock Market LLC ("Nasdaq") for a program similar to the Exchange's proposed Program. <u>See</u> Securities Exchange Act Release No. 69196 (March 20, 2013), 78 FR 18410 (March 26, 2013) (Order Granting a Limited Exemption From Rule 102 of Regulation M Concerning the NASDAQ Market Quality Program Pilot Pursuant to Regulation M Rule 102(A)) (the "Nasdaq Exemption"). The Nasdaq Exemption includes certain conditions related to, among other things, notices to the public and disclosures with respect to Nasdaq's program. The Exchange notes that if the Commission were to provide exemptive relief from Rule 102 of Regulation M for the Program, it may include similar conditions.

Program, during all trading sessions, and to detect and deter violations of Exchange rules and applicable federal securities laws. The Exchange may obtain information via the Intermarket Surveillance Group ("ISG") from other exchanges who are members or affiliates of the ISG or with which the Exchange has entered into a comprehensive surveillance sharing agreement,[57] and from listed CLP Companies and public and non-public data sources such as, for example, Bloomberg.

Changes to Interpretation and Policy .02 to Rule 11.8

The Exchange is also proposing to make certain changes to paragraph (d)(2) of Interpretation and Policy .02 to Rule 11.8 that correspond with the addition of Interpretation and Policy .03. These changes are designed to create a sunset period for any ETPs that are participating in the CLP Program pursuant to Interpretation and Policy .02 to Rule 11.8. Specifically, the Exchange is proposing to allow any ETP participating in the CLP Program prior to the implementation of the LMM Program[58] to continue to participate in the CLP Program until the first of: (1) such security has had a CADV of equal to or greater than 2 million shares for two consecutive calendar months during the first three years the security is subject to the CLP Program, provided, however, that any ETP initially listed on the Exchange shall be eligible for the CLP Program for the first six months that it is listed on the Exchange, regardless of the ETP's CADV; (2) such security has been subject to the CLP Program for three (3) years; or (3) December 31, 2014.

2. Statutory Basis

The Exchange believes that its proposal is consistent with the requirements of the Act and

[57] For a list of the current members and affiliate member of ISG, see www.isgportal.com.

[58] See supra note 9.

the rules and regulations thereunder that are applicable to a national securities exchange, and, in particular, with the requirements of Section 6(b) of the Act.[59] In particular, the proposal is consistent with Section 6(b)(4) and 6(b)(5) of the Act,[60] because it would provide for the equitable allocation of reasonable dues, fees, and other charges among Members and issuers and other persons using any facility or system which the Exchange operates or controls, and it is designed to promote just and equitable principles of trade, 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 goal of the Program is to incentivize Members to make high-quality, liquid markets, which supports the primary goal of the Act to promote the development of a resilient and efficient national market system. The Program will enhance quote competition, improve liquidity on the Exchange, support the quality of price discovery, promote market transparency, and increase competition for listings and trade executions, while reducing spreads and transaction costs. Maintaining and increasing liquidity in Exchange-listed securities will help raise investors' confidence in the fairness of the market and their transactions.

Each aspect of the Program adheres to and supports the Act. First, the Program promotes the equitable allocation of fees and dues among issuers. The Program is completely voluntary in that it will provide an additional means by which issuers may relate to the Exchange, while not eliminating the ability to list ETPs without participation in the Program. Issuers can supplement the standard listing fees with those of the Program, which the Exchange believes to be consistent with the Act. While the Program will result in higher fees for issuers that choose to participate,

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[59] 15 U.S.C. 78f(b).

[60] 15 U.S.C. 78f(b)(4) and (5).

the issuers receive significant benefits for participating, including greater liquidity, tighter spreads, and lower transaction costs for their investors. Additionally, issuers will have the ability to withdraw from the Program after an initial commitment if they determine that participation is not beneficial. In that case, the withdrawing issuers will automatically revert to the basic listing fee for ETPs.

The Program also represents an equitable allocation of fees and dues among Market Makers. Again, the Program is completely voluntary with respect to Market Maker participation in that it will provide an additional means by which members may qualify for a CLP Rebate in a manner nearly identical to the existing CLP Program, without eliminating any of the existing means of qualifying for incentives on the Exchange. Currently, the Exchange employs multiple fee arrangements, including the CLP Program, to incentivize Market Makers to maintain high quality markets or to improve the quality of executions. Market Makers that choose to undertake increased burdens under the Program will be rewarded with increased rebates, while those that do not undertake such burdens will receive no added benefit. Where a CLP determines that the burdens imposed by the Program outweigh the benefits provided, the CLP may provide the Exchange with notice of withdrawal and will be withdrawn from the program in no longer than thirty days.

Additionally, the Program establishes an equitable allocation of CLP Rebates among Market Makers that choose to participate and fulfill the obligations imposed by the rule. If one Market Maker is an Eligible CLP, the Bid (Offer) Rebate will be distributed to that CLP; if multiple Market Makers are Eligible CLPs, the Bid (Offer) Rebate will be distributed among the two CLPs with the most Bid (Offer) SET Credits, as described above. In other words, all of the benefit of the CLP Rebate will flow to the highest-performing Market Makers, provided that at least one Market Maker fulfills the obligations under the proposed rule.

The Program is designed to avoid unfair discrimination among Market Makers and issuers. The proposed rule contains objective, measurable standards that the Exchange will apply with care. These standards will be applied equally to ensure that similarly situated parties are treated similarly. This is equally true for inclusion of issuers and Market Makers, withdrawal of issuers and Market Makers, and termination of eligibility for the Program. The standards are carefully constructed to protect the rights of all parties wishing to participate in the Program by providing notice of requirements and a description of the process. The Exchange will apply these standards with the same care and experience with which it applies the many similar rules and standards in the Exchange's rules.

In contrast to the extensive benefits of the Program, the participation of a CLP Company in the Program is substantially limited, by design. In this regard, a CLP Company is limited to making only the following determinations regarding the Program: whether to participate in the Program; what CLP Security should be in the Program; what firms will participate in developing and funding the CLP Security; when the CLP Security should exit the Program; and the level of Supplemental Fees, if any, that should be applied. The CLP can never influence how, when, or the specific amount that a CLP receives as credit for making a market in a CLP Security. These functions are performed solely by the Exchange according to standards set forth in the Program.

The Exchange notes that it operates in a highly competitive market in which market participants can readily favor competing venues if they deem fee levels at a particular venue to be excessive, or rebate opportunities available at other venues to be more favorable. Accordingly, the listing fees and rebates are constrained by the active competition for listings in ETPs and for market making. If a particular exchange charges excessive fees for listing, ETPs will choose to list elsewhere. Similarly, if an exchange fails to incent market makers to provide sufficient liquidity, participants will likely shift their order flow to other venues. Accordingly, the exchange charging excessive listing fees or providing insufficient rebates for market maker would likely not accomplish the goals of the Program. As such, the Exchange believes that this competitive dynamic imposes powerful restraints on the ability of any exchange to charge unreasonable fees for listing or provide insufficient rebates for market making activity.

The Exchange also notes that the Program, as proposed, is substantially similar to the existing functionality provided under the CLP Program. The Exchange believes that the CLP Program has been very beneficial to market participants, including investors, issuers, and Market Makers, by providing increased market quality in the form of tighter spreads and deeper liquidity. The Exchange believes that the proposed Program will enjoy similarly positive results to the benefit of issuers, investors in CLP Securities, and the financial markets as a whole.

(B) Self-Regulatory Organization's Statement on Burden on Competition

The Exchange does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act, as amended. To the contrary, the Exchange believes that the proposal will increase competition in both the listings market and in competition for market makers. The Program will promote competition in the listings market by providing issuers with a vehicle for paying the Exchange additional fees in exchange for incentivizing tighter spreads and deeper liquidity in listed securities. While the Program closely resembles the existing CLP Program, the proposed modifications are a response to the competition from other markets that either have or are developing similar programs, including Nasdaq[61] and NYSE Arca Equities, Inc.[62]

The Exchange also believes that the proposed changes will enhance competition among participants by creating incentives for market makers to compete to make better quality markets. By requiring both that market makers meet the quoting requirements and also to compete for the CLP Rebate, the quality of quotes on the Exchange will improve. This, in turn, will attract more liquidity to the Exchange and further improve the quality of trading in CLP Securities, which will also act to bolster the Exchange's listing business. As mentioned above, this proposal is in response to similar programs at or in development at other markets.

(C) Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants or Others

The Exchange has neither solicited nor received written comments on the proposed rule change.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Within 45 days of the date of publication of this notice in the Federal Register or within such longer period up to 90 days (i) as the Commission may designate if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the self-regulatory organization consents, the Commission will:

(A) by order approve or disapprove such proposed rule change, or

(B) institute proceedings to determine whether the proposed rule change should be disapproved.

IV. Solicitation of Comments

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61 See Securities Exchange Act Release No. 69195 (March 20, 2013), 78 FR 18393 (March 26, 2013) (SR-NASDAQ-2012-137).

62 See Securities Exchange Act Release No. 69335 (April 5, 2013), SR-NYSEARCA-2013-34 (March 21, 2013).

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic Comments:

- Use the Commission's Internet comment form (http://www.sec.gov/rules/sro.shtml); or
- Send an e-mail to rule-comments@sec.gov. Please include File No. SR-BATS-2014-022 on the subject line.

Paper Comments:

- Send paper comments in triplicate to Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File No. SR-BATS-2014-022. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (http://www.sec.gov/rules/sro.shtml). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549-1090, on official business days between the hours of 10:00 am and 3:00 pm. Copies of such filing also will be available for inspection and copying at the principal office of the Exchange. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File No. SR-BATS-2014-022 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.[63]

Kevin M. O'Neill
Deputy Secretary

[63] 17 CFR 200.30-3(a)(12).