

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-72730; File No. SR-BYX-2014-013)

July 31, 2014

Self-Regulatory Organizations; BATS Y-Exchange, Inc.; Notice of Filing and Immediate Effectiveness of a Proposed Rule Change to Amend Rule 11.24(a)(2) to Include Riskless Principal Orders to the Types of Orders that May Qualify as Retail Orders under the Retail Price Improvement Program

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the “Act”),¹ and Rule 19b-4 thereunder,² notice is hereby given that on July 24, 2014, BATS Y-Exchange, Inc. (the “Exchange” or “BYX”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I and II below, which Items have been prepared by the Exchange. The Exchange has designated this proposal as a “non-controversial” proposed rule change pursuant to Section 19(b)(3)(A) of the Act³ and Rule 19b-4(f)(6)(iii) thereunder,⁴ which renders it effective upon filing with the Commission. 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 the Substance of the Proposed Rule Change

The Exchange proposes to amend Exchange Rule 11.24(a)(2) to include riskless principal orders to the types of orders that may qualify as Retail Orders under the Exchange’s Retail Price Improvement Program (the “RPI Program”). The Exchange has designated this proposal as non-

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ 15 U.S.C. 78s(b)(3)(A).

⁴ 17 CFR 240.19b-4(f)(6)(iii).

controversial and provided the Commission with the notice required by Rule 19b-4(f)(6)(iii) under the Act.⁵

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

The Exchange proposes to amend Exchange Rule 11.24(a)(2) to include riskless principal orders to the types of orders that may qualify as Retail Orders under the Exchange's RPI Program.⁶ The Exchange established the RPI Program in an attempt to attract retail order flow to the Exchange by potentially providing price improvement to such order flow.⁷ Under the RPI Program, all

⁵ 17 CFR 240.19b-4(f)(6)(iii).

⁶ The Exchange notes that in order to qualify as a Retail Order, a riskless principal order must satisfy the criteria set forth in FINRA Rule 5320.03.

⁷ See Securities Exchange Act Release No. 68303 (November 27, 2012), 77 FR 71652 (December 3, 2012) ("RPI Approval Order") (SR-BYX-2012-019). See also Securities Exchange Act Release No. 71249 (January 7, 2014), 79 FR 2229 (January 13, 2014) (SR-BYX-2014-001) (Notice of Filing and Immediate Effectiveness extending pilot period until January 31, 2015).

Exchange Users⁸ are permitted members to submit Retail Price Improvement Orders (“RPI Orders”)⁹ which are designed to provide potential price improvement for Retail Orders in the form of non-displayed interest that is better than the national best bid that is a Protected Quotation (“Protected NBB”) or the national best offer that is a Protected Quotation (“Protected NBO”, and together with the Protected NBB, the “Protected NBBO”).¹⁰ The Exchange believes that the RPI Program promotes competition for retail order flow by allowing Exchange Users to submit RPI Orders to interact with Retail Orders.

Exchange Rule 11.24(a)(2) currently defines a Retail Order as, “an agency order that originates from a natural person and is submitted to the Exchange by a Retail Member Organization, provided that no change is made to the terms of the order with respect to price or side of the market and the order does not originate from a trading algorithm or any other computerized methodology.” The Exchange believes that its definition of a Retail Order is unnecessarily restrictive compared to

⁸ A “User” is defined “as any member or sponsored participant of the Exchange who is authorized to obtain access to the System.” BYX Rule 1.5(cc).

⁹ A “Retail Price Improvement Order” is defined in Rule 11.24(a)(3) as an order that consists of non-displayed interest on the Exchange that is priced better than the Protected NBB or Protected NBO by at least \$0.001 and that is identified as such. See Rule 11.24(a)(3).

¹⁰ The term Protected Quotation is defined in BYX Rule 1.5(t) and has the same meaning as is set forth in Regulation NMS Rule 600(b)(58). The terms Protected NBB and Protected NBO are defined in BYX Rule 1.5(s). The Protected NBB is the best-priced protected bid and the Protected NBO is the best-priced protected offer. Generally, the Protected NBB and Protected NBO and the national best bid (“NBB”) and national best offer (“NBO”, together with the NBB, the “NBBO”) will be the same. However, a market center is not required to route to the NBB or NBO if that market center is subject to an exception under Regulation NMS Rule 611(b)(1) or if such NBB or NBO is otherwise not available for an automatic execution. In such case, the Protected NBB or Protected NBO would be the best-priced protected bid or offer to which a market center must route interest pursuant to Regulation NMS Rule 611.

that of other exchanges because it does not include “riskless principal orders” in its definition.¹¹ The Exchange believes that its comparatively narrow definition may create confusion among the Exchange’s Members,¹² preventing Members from participating in the RPI Program. In addition, the Exchange believes that the restrictiveness of the Exchange’s definition may inadvertently put the Exchange at a competitive disadvantage in relation to other exchanges that provide a less restrictive definition of a Retail Order.

Accordingly, the Exchange proposes to amend the definition of a Retail Order in under Rule 11.24(a)(2) to include riskless principal orders to the types of orders that may qualify as Retail Orders.¹³ The Exchange proposes to amend Rule 11.24(a)(2) to define a Retail Order as, “an agency order or riskless principal that meets the criteria of FINRA Rule 5320.03 that originates from a natural person and is submitted to the Exchange by a Retail Member organization, provided that no change is made to the terms of the order with respect to price or side of market and the order does not originate from a trading algorithm or any other computerized methodology” (emphasis added).¹⁴

¹¹ The Exchange notes that other market centers include “riskless principal orders” as part of their definitions of “Retail Orders.” See, e.g., Securities Exchange Act Release No. 68937 (February 15, 2013), 78 FR 12397 (February 22, 2013) (SR-NASDAQ-2012-129); Securities Exchange Act Release No. 69103 (March 11, 2013), 78 FR 16547 (March 15, 2013) (SR-NYSE-2013-20); Securities Exchange Release No. 69104 (March 11, 2013), 78 FR 16556 (March 15, 2013) (SR-NYSEMKT-2013-22); and Securities Exchange Act Release No. 69378 (April 15, 2013), 78 FR 23617 (April 19, 2013) (SR-EDGX-2013-13).

¹² The term “Member” is defined as “any registered broker or dealer that has been admitted to membership in the Exchange. A Member will have the status of a “member” of the Exchange as that term is defined in Section 3(a)(3) of the Act. Membership may be granted to a sole proprietor, partnership, corporation, limited liability company or other organization which is a registered broker or dealer pursuant to Section 15 of the Act, and which has been approved by the Exchange.” See Exchange Rule 1.5(n).

¹³ The Exchange notes that in order to qualify as a Retail Order, a riskless principal order must satisfy the criteria set forth in FINRA Rule 5320.03.

¹⁴ The Exchange notes that it will amend its attestation form for Members designating Retail Orders to conform to these new requirements. The definition of Retail Order

The Exchange believes that, for purposes of determining whether an order should qualify as a Retail Order, there is no substantive difference between an agency order and a riskless principal order that meets the requirements of FINRA Rule 5320.03. A riskless principal transaction is a transaction in which a Member, after having received an order to buy (sell) a security, purchases (sells) the security as principal and, contemporaneously, satisfies the original order by selling (buying) as principal at the same price. Generally, a riskless principal transaction involves two orders, the execution of one being dependent upon the receipt or execution of the other; thus, there is no “risk” in the interdependent transactions when completed. Unlike a riskless principal transaction, an agency order is entered directly in the System¹⁵ by a Member on behalf of a customer. Ultimately, however, the results of a riskless principal transaction and an agency order are the same: the customer receives an execution while the involved Member acts as an intermediary to effect the transaction.¹⁶

The Exchange believes that the requirement that the entry of such riskless principal orders satisfy FINRA Rule 5320.03 provides sufficient protection against Members submitting orders for their own account to the Exchange. A Member entering a riskless principal transaction will have to, contemporaneously with the execution of the customer’s order, submit a report identifying the trade as riskless principal to FINRA. Additionally, the Member will need to have written policies and procedures to ensure that riskless principal transactions comply with applicable FINRA rules. The policies and procedures, at a minimum, must require that the customer order be received prior to the

under Rule 11.24(a)(2) will continue to state that a Retail Order is an Immediate or Cancel (“IOC”) Order and shall operate in accordance with paragraph (f) of Rule 11.24 and that a Retail Order may be an odd lot, round lot, or mixed lot.

¹⁵ The term “System” is defined as “the electronic communications and trading facility designated by the Board through which securities orders of Users are consolidated for ranking, execution and, when applicable, routing away.” Exchange Rule 1.5(aa).

¹⁶ A principal transaction differs from both a riskless principal transaction and an agency order in that it is an order for the principal account of the entering Member.

offsetting principal transaction, and that the offsetting principal transaction is at the same price as the customer order exclusive of any markup or markdown, commission equivalent, or other fee, and is allocated to a riskless principal or customer account in a consistent manner and within 60 seconds of execution. Additionally, the Member must have supervisory systems in place that produce records that enable the Member and FINRA to reconstruct accurately, readily, and in a time-sequenced manner all Retail Orders that are entered on a riskless principal basis.

The Exchange believes that the Member must also ensure that non-Retail Orders from customers are not included with the Retail Orders as part of a riskless principal transaction. The above requirements ensure that despite the procedural differences between the execution of a riskless principal transaction and an agency order, the only difference will be the procedure in which the transactions are effected and not the result.

The Exchange further believes that clarifying that riskless principal orders that meet the requirements of FINRA Rule 5320.03 are able to be submitted as Retail Orders on the same basis as agency orders will enable Members, and in turn, their retail customers, to benefit from the price improvement opportunities available under the Exchange's RPI Program.

2. Statutory Basis

The Exchange believes that its proposal is consistent with Section 6(b) of the Act¹⁷ in general, and furthers the objectives of Section 6(b)(5) of the Act¹⁸ in particular, in that it is designed to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in facilitating transactions in securities, 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.

¹⁷ 15 U.S.C. 78f(b).

¹⁸ 15 U.S.C. 78f(b)(5).

The Exchange believes that the proposed rule change promotes just and equitable principles of trade because it will ensure that riskless principal orders that meet the requirements of FINRA Rule 5320.03 will have the same opportunity to be submitted as Retail Orders as agency orders. As discussed above, there is no functional distinction for purposes of Retail Orders between an order entered by a Member on an agency basis and one entered on a riskless principal basis. The Exchange believes that the proposed change would tend to reduce any potential discrimination between similarly situated customers or brokers by ensuring that the ability of retail customers to benefit from the use of Retail Orders and price improvement opportunities available under the Exchange's RPI Program does not depend on a distinction in capacity that is not meaningful for purposes of submitting Retail Orders. As a result of the change, a retail customer would be able to in the RPI Program utilizing Retail Orders without regards to whether the Member enters the order on a riskless principal or agency basis.

The Exchange believes that the proposed rule change will remove impediments to and perfect the mechanism of a free and open market and a national market system because it will clarify that riskless principal orders that meet the requirements of FINRA Rule 5320.03 are eligible to be submitted as Retail Orders on the same basis as agency orders. By allowing all orders that are functionally equivalent to agency orders to be submitted as Retail Orders, the proposed change would potentially stimulate further competition for retail order flow because it is similar to the definition of retail order available on other exchanges.¹⁹

The Exchange believes that the proposed change would protect investors and the public interest by expanding the access of Members to the RPI Program offered by the Exchange as

¹⁹ See Footnote 4 of the EDGX Exchange, Inc. ("EDGX") fee schedule available at <http://www.directedge.com/Trading/EDGXFeeSchedule.aspx> (last visited July 16, 2014); NASDAQ Stock Market LLC Rule 4780(a)(2); New York Stock Exchange, Inc. Rule 107C(a)(3)' and NYSE MKT LLC Rule 107C(a)(3).

well as the access of the public to an exchange sponsored alternative to broker-operated internalization venues. In this regard, the Exchange believes that maintaining or increasing the proportion of Retail Orders in exchange-listed securities that are executed on a registered national securities exchange (rather than relying on certain available off-exchange execution methods) would contribute to investors' confidence in the fairness of their transactions and would benefit all investors by deepening the Exchange's liquidity pool, supporting the quality of price discovery, promoting market transparency and improving investor protection.

B. Self-Regulatory Organization's Statement on Burden on Competition

The Exchange does not believe that the proposed rule change will impose any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. The Exchange believes that the amendment, by increasing the level of participation in the RPI Program, will increase the level of competition around retail executions such that retail investors would receive better prices than they currently do on the Exchange and potentially through bilateral internalization arrangements. The Exchange believes that the transparency and competitiveness of operating a program such as the RPI Program on an exchange market would result in better prices for retail investors and benefits retail investors by expanding the capabilities of the Exchange to encompass practices currently allowed on non-exchange venues. In addition, by allowing all orders that are functionally equivalent to agency orders to be submitted as Retail Orders, the proposed change would potentially stimulate further competition for retail order flow because it is similar to the definition of retail order available on other exchanges.²⁰

²⁰

Id.

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

The Exchange has filed the proposed rule change pursuant to Section 19(b)(3)(A) of the Act²¹ and Rule 19b-4(f)(6)²² thereunder. Because the foregoing proposed rule change does not: (i) significantly affect the protection of investors or the public interest; (ii) impose any significant burden on competition; and (iii) become operative for 30 days from the date on which it was filed, or such shorter time as the Commission may designate, it has become effective pursuant to Section 19(b)(3)(A) of the Act²³ and subparagraph (f)(6) of Rule 19b-4 thereunder.²⁴

A proposed rule change filed under Rule 19b-4(f)(6) normally does not become operative for 30 days after the date of filing.²⁵ However, Rule 19b-4(f)(6)(iii) permits the Commission to designate a shorter time if such action is consistent with the protection of investors and the public interest.²⁶ The Exchange has asked the Commission to waive the 30-day operative delay so that the proposal may become operative immediately upon filing. The Exchange believes that waiving the 30-day operative delay is consistent with the protection of investors and the public

²¹ 15 U.S.C. 78s(b)(3)(A).

²² 17 CFR 240.19b-4(f)(6). In addition, Rule 19b-4(f)(6)(iii) requires the Exchange to give the Commission written notice of the Exchange's intent to file the proposed rule change, along with a brief description and text of the proposed rule change, at least five business days prior to the date of filing of the proposed rule change, or such shorter time as designated by the Commission. The Exchange has satisfied this requirement.

²³ 15 U.S.C. 78s(b)(3)(A).

²⁴ 17 CFR 240.19b-4(f)(6).

²⁵ 17 CFR 240.19b-4(f)(6)(iii).

²⁶ Id.

interest because such waiver would allow riskless principal orders meeting the requirements of FINRA Rule 5320.03 to immediately qualify as retail orders, and thereby allow more Exchange members to benefit from the price improvement opportunities available under the Exchange's RPI Program. The Exchange also believes that waiving the 30-day operative delay would enable the Exchange to remain competitive with other market centers by providing an additional choice to its members as to where they send retail orders on a riskless principal basis. The Exchange notes that several other exchanges presently include riskless principal orders within their definition of a retail order.²⁷ The Commission believes that waiving the 30-day operative delay is consistent with the protection of investors and the public interest. Therefore, the Commission hereby waives the 30-day operative delay and designates the proposal operative upon filing.²⁸

At any time within 60 days of the filing of the proposed rule change, the Commission summarily may temporarily suspend such rule change if it appears to the Commission that such action is: (i) necessary or appropriate in the public interest; (ii) for the protection of investors; or (iii) otherwise in furtherance of the purposes of the Act.²⁹ If the Commission takes such action, the Commission shall institute proceedings to determine whether the proposed rule change should be approved or disapproved.³⁰

²⁷ See, e.g., Securities Exchange Act Release Nos. 68937 (February 15, 2013), 78 FR 12397 (February 22, 2013) (SR-NASDAQ-2012-129); 69103 (March 11, 2013), 78 FR 16547 (March 15, 2013) (SR-NYSE-2013-20); 69104 (March 11, 2013), 78 FR 16556 (March 15, 2013) (SR-NYSEMKT-2013-22); and 69378 (April 15, 2013), 78 FR 23617 (April 19, 2013) (SR-EDGX-2013-13).

²⁸ For purposes only of waiving the 30-day operative delay, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

²⁹ 15 U.S.C. 78s(b)(3)(C).

³⁰ Id.

IV. Solicitation of Comments

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 Number SR-BYX-2014-013 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 Number SR-BYX-2014-013. 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, on official business days between the hours of 10:00 a.m. and 3:00 p.m. 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 Number SR-BYX-2014-013, 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.³¹

Kevin M. O'Neill
Deputy Secretary

³¹ 17 CFR 200.30-3(a)(12).