

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-68788, File No. SR-BATS-2012-046)

January 31, 2013

Self-Regulatory Organizations; BATS Exchange, Inc.; Order Approving Proposed Rule Change to Modify BATS Rule 11.23 relating to Auctions of Exchange-Listed Securities

I. Introduction

On December 6, 2012, 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”),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> a proposed rule change to amend its rules governing auctions conducted by the Exchange for securities listed on the Exchange. The proposed rule change was published for comment in the Federal Register on December 20, 2012.<sup>3</sup> The Commission received no comment letters regarding the proposal. This order approves the proposed rule change.

II. Description of the Proposed Rule Change

The Exchange has proposed to amend BATS Rule 11.23, which governs auctions conducted by the Exchange for securities listed on the Exchange.<sup>4</sup> These auctions include: (1) an opening auction (“Opening Auction”); (2) a closing auction (“Closing Auction”); (3) an auction in the event of an initial public offering (“IPO Auction”); and (4) an auction in the event of a halt of trading in a security (“Halt Auction”) (collectively referred to as “Exchange

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<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> See Securities Exchange Act Release No. 68442 (December 14, 2012), 77 FR 75459 (December 20, 2012) (“Notice”).

<sup>4</sup> See Securities Exchange Act Release No. 65619 (October 25, 2011), 76 FR 67238 (October 31, 2011) (order approving proposed rule change by BATS to adopt rules applicable to auctions conducted by the Exchange for exchange-listed securities).

Auctions”).<sup>5</sup> In connection with the Exchange Auctions, BATS offers the BATS Auction Feed, which provides recipients with uncompressed real-time data regarding the current status of price and size information related to Exchange Auctions.<sup>6</sup>

A. Change to the Definition of Collar Price Range

The Exchange has proposed to amend BATS Rule 11.23(a)(6) to amend the definition of “Collar Price Range” to incorporate the Exchange’s numerical guidelines for clearly erroneous executions under BATS Rule 11.17(c)(1).<sup>7</sup> Currently, BATS Rule 11.23(a)(6) sets the Collar Price Range at 10% of the Volume Based Tie Breaker<sup>8</sup> below and above the BATS Best Bid (“ZBB”) and BATS Best Offer (“ZBO”),<sup>9</sup> the National Best Bid (“NBB”) and National Best Offer (“NBO”), or the Final Last Sale Eligible Trade,<sup>10</sup> depending on market conditions at the

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<sup>5</sup> See id.

<sup>6</sup> See id.

<sup>7</sup> See Notice supra note 3, at 76 FR 75460.

<sup>8</sup> BATS Rule 11.23(a)(23) defines “Volume Based Tie Breaker” as the midpoint of the BATS Best Bid or BATS Best Offer (“ZBBO”) for a particular security. In the event that there is either no ZBB or ZBO for the security, the National Best Bid and Offer (“NBBO”) will be used if there is at least one limit order on either the Continuous Book or the Auction Book. In the event that there is no NBB or NBO for the security or no limit orders on the Continuous Book and the Auction Book, the price of the Final Last Sale Eligible Trade will be used. See infra note 10 (defining “Final Last Sale Eligible Trade”). BATS Rule 11.23(a)(1) defines the “Auction Book” as all Eligible Auction Orders on the BATS Book. BATS Rule 11.23(a)(7) defines “Continuous Book” as all orders on the BATS Book that are not Eligible Auction Orders.

<sup>9</sup> See BATS Rule 11.23(a)(24)(defining the ZBB and ZBO). BATS Rule 11.23(a)(24) defines the BATS Best Bid or BATS Best Offer as “ZBBO.”

<sup>10</sup> See BATS Rule 11.23(a)(9) defines “Final Last Sale Eligible Trade” as the last trade occurring during Regular Trading Hours on the Exchange if the trade was executed within the last one second prior to either the Closing Auction or, for Halt Auctions, trading in the security being halted. Where the trade was not executed within the last one second, the last trade reported to the consolidated tape received by BATS during Regular Trading Hours and, where applicable, prior to trading in the security being halted will be used. If there is no qualifying trade for the current day, the BATS Official Closing Price from the previous trading day will be used.

time of the auction.<sup>11</sup> The Exchange has proposed to base its Collar Price Range on numerical guidelines for clearly erroneous rules under BATS Rule 11.17(c)(1), which would be determined as follows: where the Collar Midpoint is \$25.00 or less, the Collar Price Range shall be the range from 10% below the Collar Midpoint to 10% above the Collar Midpoint; where the Collar Midpoint is greater than \$25.00 but less than or equal to \$50.00, the Collar Price Range shall be the range from 5% below the Collar Midpoint to 5% above the Collar Midpoint; and where the Collar Midpoint is greater than \$50.00, the Collar Price Range shall be the range from 3% below the Collar Midpoint to 3% above the Collar Midpoint.<sup>12</sup> According to the Exchange, the proposed rule change would provide greater transparency and certainty in Exchange Auctions by helping reduce the possibility that an auction would occur at a price that would qualify as a clearly erroneous under BATS Rule 11.17(c)(1) and limit the volatility in auction prices.<sup>13</sup>

#### B. Change to the Determination of the Auction Price

The Exchange has proposed to amend BATS Rule 11.23 to change how the Exchange determines the price for Exchange Auctions. Currently, to determine the auction price for an Exchange Auction, the Exchange first looks to whether there is at least one limit order either: (1) on the Continuous Book or Auction Book for Opening Auctions and Closing Auctions; or (2)

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<sup>11</sup> See Notice supra note 3, at 76 FR 75460.

<sup>12</sup> See id. The Exchange has proposed to define “Collar Midpoint” in BATS Rule 11.23(a)(6) as the Volume Based Tie Breaker for all applicable auctions, except for IPO Auctions in Exchange Traded Products (as defined in Rule 11.8, Interpretation and Policy .02(d)(2)), for which the Collar Midpoint will be the issue price. See also Notice supra note 3, at 76 FR 75460.

<sup>13</sup> The Exchange noted that the modified Collar Price Range would not necessarily prevent all clearly erroneous executions from occurring as the Collar Price Range will be based on the Collar Midpoint and the numerical guidelines for clearly erroneous executions are based on the Reference Price, which is equal to the consolidated last sale immediately prior to the execution(s) under review. See Notice supra note 3, at 76 FR 75460 n. 7.

among Eligible Auction Orders for IPO and Halt Auctions.<sup>14</sup> Where there is at least one limit order, then the auction will occur at a price level within the Collar Price Range, where applicable, that maximizes the number of shares executed in the auction. In the event that there are no limit orders on the Continuous Book and Auction Book for Opening Auctions or Closing Auctions or among Eligible Auction Orders for IPO or Halt Auctions, the Exchange would use a default price, which currently is the Final Last Sale Eligible Trade for Opening Auctions, Closing Auctions, and Halt Auctions, and the issuing price for an IPO Auction.

The Exchange proposes two changes to Rule 11.23 relating to the determination of the auction price in certain circumstances. The first change modifies when the Exchange will use a default price for executions in Exchange Auctions. The second change modifies the Exchange's default price for Opening Auctions and Closing Auctions.

Regarding the first change, the Exchange has proposed<sup>14</sup> to amend BATS Rules 11.23(b)(2)(B), 11.23(c)(2)(B), and 11.23(d)(2)(C) to provide that, prior to determining the price for an Exchange Auction, the Exchange will look to whether there is at least one limit order from each side that would participate in the Exchange Auction. The Exchange has proposed that where no limit orders from either or both sides would participate in the Exchange Auction, the Exchange Auction would occur at a default price, as modified in the description below with respect to Opening Auctions and Closing Auctions.

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<sup>14</sup> See BATS Rule 11.23(a)(9) defines "Eligible Auction Orders" as any Market-On-Open, Limit-On-Open, Late-Limit-On-Open, Market-On-Close, Limit-On-Close, or Late-Limit-On-Close that is entered in compliance with its respective cutoff for an Opening Auction or Closing Auction, any regular hours order prior to the Opening Auction, any limit or market order not designated to exclusively participate in the Closing Auction entered during the Quote-Only Period of an IPO Auction, and any limit or market order not designated to exclusively participate in the Opening Auction or Closing Auction entered during the Quote-Only Period of a Halt Auction.

In the second change to Rule 11.23, the Exchange has proposed to amend BATS Rules 11.23(b)(2)(B) and 11.23(c)(2)(B) to use the Volume Based Tie Breaker as the default price instead of the Final Last Sale Eligible Trade for Opening Auctions and Closing Auctions. By using the Volume Based Tie Breaker as the default price, the Exchange would first look to the current market, if available, to determine the auction price before using the Final Last Sale Eligible Trade. Specifically, the Exchange would first look to the ZBBO to determine the auction price for a particular security. In the event that there is either no ZBB or ZBO, the Exchange would use the NBBO to determine the auction price for the Opening Auction or Closing Auction, if there is at least one limit order on either the Continuous Book or the Auction Book. Where there is either no NBBO for the security or no limit orders on the Continuous Book and the Auction Book, the Exchange would use the Final Last Sale Eligible Trade as the auction price for an Opening Auction or Closing Auction.

C. Limitation on Information Published in connection with IPO and Halt Auction Data

The Exchange has also proposed to amend BATS Rule 11.23(d)(2)(A) (Publication of BATS Auction Information) in two ways. First, the Exchange has proposed to clarify that BATS Rule 11.23(d)(2)(A) applies to IPO Auctions as well as Halt Auctions. Second, the Exchange has proposed to amend BATS Rule 11.23(d)(2)(A) to provide that the Exchange will only disseminate the lesser of the Reference Buy Shares<sup>15</sup> and the Reference Sell Shares,<sup>16</sup> rather than disseminate both pieces of information, in auction information messages sent through BATS

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<sup>15</sup> BATS Rule 11.23(a)(18) defines “Reference Buy Shares” as the total number of shares associated with buy-side Eligible Auction Orders that are priced equal to or less than the Reference Price.

<sup>16</sup> BATS Rule 11.23(a)(21) defines “Reference Sell Shares” as the total number of shares associated with sell-side Eligible Auction Orders that are priced equal to or less than the Reference Price.

Data Feed.<sup>17</sup> The Exchange has represented that this proposal is designed to prevent market participants from possibly gaming an IPO or Halt Auction.<sup>18</sup> Specifically, the Exchange is concerned that the dissemination of both Reference Buy Shares and Reference Sell Share information could allow a market participant to discern the exact amount of liquidity available at a given price level on both sides of the IPO or Halt Auction Book.<sup>19</sup> Because market participants are permitted to enter orders in IPO and Halt Auctions up until the auction occurs, the Exchange believes that a market participant could use both the Reference Buy Shares and Reference Sell Shares to potentially manipulate the price of the auction.<sup>20</sup> By disseminating only the lesser of the Reference Buy Shares and Reference Sell Shares associated with IPO and Halt Auctions, the Exchange believes that a market participant would not be able to manipulate an IPO or Halt Auction because the market participant would not have complete knowledge of liquidity available on both sides of the auction book simultaneously.<sup>21</sup>

#### D. Market Regular Hours Orders

The Exchange has proposed to amend Rule 11.23(a)(22) to provide that any unexecuted portion of a market Regular Hours Only (“RHO”) order is immediately cancelled following any

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<sup>17</sup> See Notice supra note 3, at 76 FR 75461.

<sup>18</sup> See id.

<sup>19</sup> See id.

<sup>20</sup> See id.

<sup>21</sup> See Notice supra note 3, at 76 FR 75461. The Exchange notes such gaming concerns do not exist in the Opening Auctions and Closing Auctions for two reasons. First, the Exchange represents that auction information messages for Opening Auctions and Closing Auctions do not provide complete information about the auctions as such messages do not include information relating to the Continuous Book. Second, information messages for Opening Auctions and Closing Auctions are not disseminated until two minutes and five minutes prior to the auction, respectively, at which point market participants are prohibited from modifying or canceling any Eligible Auction Orders entered in the Auction Book.

Exchange Auction in which it was eligible to participate.<sup>22</sup> The Exchange stated that this proposed rule change would clarify that a market RHO order would either execute or be cancelled, which the Exchange believes would be consistent with the behavior of all other market orders entered on the Exchange.<sup>23</sup>

### III. Discussion

After careful consideration of the proposed rule change, the Commission finds that the proposal is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange.<sup>24</sup> The Commission believes that the proposed rule change is consistent with Section 6(b) of the Act, in general, and Section 6(b)(5) of the Act, in particular, in that it is designed to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and 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.

The Commission believes that the proposed changes to the Collar Price Range definition are consistent with Section 6(b)(5) of the Act. The Exchange notes that (1) this proposed change provides greater transparency and certainty in Exchange Auctions by reducing the possibility that an auction would occur at a price that would qualify as clearly erroneous and cancelled under the Exchange's rules and (2) by narrowing the Collar Price Range, the proposed rule change will

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<sup>22</sup> See Notice supra note 3, at 77 FR at 75460. BATS Rule 11.23(a)(22) defines a RHO order as a BATS order that is designated for execution only during Regular Trading Hours, which includes the Opening Auction, the Closing Auction, and IPO/Halt Auctions.

<sup>23</sup> See Notice supra note 3, at 77 FR at 75460.

<sup>24</sup> 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).

help limit the volatility in auction prices. The Commission notes that the proposed changes to the definition of the Collar Price Range are based on the numerical guidelines for clearly erroneous executions under BATS Rule 11.17(c)(1). For these reasons, the Commission believes that the proposed changes to the Collar Price Range definition are consistent with the Act.

The Commission believes that the proposed changes to how the Exchange determines the auction price are consistent with Section 6(b)(5) of the Act. The Exchange notes that the proposed changes regarding when the Exchange will use a default price would aid in price discovery and help to prevent erroneous executions by ensuring that a single limit order on one side of an auction that might not participate in the Exchange Auction cannot on its own determine the auction price. In addition, the Exchange notes that revisions to the default price for Opening Auctions and Closing Auctions would also aid in price discovery and help to reduce the likelihood of executions in auctions occurring at prices out of line with existing market conditions. For these reasons, the Commission believes that these proposed changes are consistent with the Act.

The Commission also believes that the proposal to disseminate only the lesser of the Reference Buy Shares and the Reference Sell Shares in auction information messages for IPO and Halt Auctions is consistent with Section 6(b)(5) of the Act. The Exchange has represented that this proposal is designed to prevent market participants from possibly gaming an IPO or Halt Auction, as it would hinder a market participant from being able to discern the exact amount of liquidity available at a given price level on both sides of the IPO or Halt Auction Book. In this way, the Exchange believes that the proposal should make it more difficult for a market participant to use auction information to manipulate an IPO or Halt auction. For this reason, the Commission believes that the proposed rule change is consistent with the Act.



Finally, the Commission believes that the proposed change to provide that any unexecuted portion of a market RHO order is immediately cancelled following any Exchange Auction in which it was eligible to participate should clarify the operation of market RHO Auction Orders, as noted by the Exchange. As such, the Commission believes this proposed change is also consistent with the Exchange Act.

III. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,<sup>25</sup> that the proposed rule change (SR-BATS-2012-046) be, and hereby is, approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>26</sup>

Kevin M. O'Neil  
Deputy Secretary

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<sup>25</sup> 15 U.S.C. 78s(b)(2).

<sup>26</sup> 17 CFR 200.30-3(a)(12).