June 21, 2010

Elizabeth M. Murphy
Secretary
Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549-1090

RE: Proposed Amendments to Rule 610 of Regulation NMS; Release No. 34-61902; File No. S7-09-10

Ms. Murphy:

BATS Exchange, Inc. ("BATS") appreciates the opportunity to comment on the above referenced proposed rules related to access to quotations in the listed options markets and fees related to such access. BATS operates the third largest registered equities exchange in the United States, executing on its single book approximately 11% of the daily equity market volume. BATS serves the European market through its London based, FSA-authorized subsidiary, BATS Europe, which operates a Multilateral Trading Facility for European securities. Most recently, on February 26th, 2010, BATS launched a US equity options market, BATS Options.

BATS supports the modifications to Rule 610(a) of Regulation NMS proposed by the Commission. The Commission should be applauded for focusing on ensuring, for all market participants, fair and non-discriminatory access to the US equity options exchanges and their liquidity. More, the introduction of an all-in fee cap for accessing an options exchange's best price fills a significant gap in the current regulatory structure. The adoption of these rules will also remove a key objection to another important Commission proposal – the Elimination of Flash Order Exception from Rule 602 of Regulation NMS[1] - and we suggest that while the Commission continues its broader market structure review, it moves forward *without delay* with the elimination of flash and step-ups, immediately after the adoption of an option exchange access fee cap.

1 Elimination of Flash Order Exception from Rule 602 of Regulation NMS; Proposed Rule; Securities Exchange Act Release No. 60684 (September 18, 2009), 74 FR 48632 (September 23, 2009) (File No. S7-21-09) (the "Flash Order Proposal").

Discussion

The US equity options markets are in a state of dramatic flux and rapid evolution. At the same time that we have new exchanges coming online[2], other exchanges are introducing new classifications of customers[3] and the pricing changes are coming fast and furious. More than simple pricing changes, we are seeing wholesale shifts of the incentives and charges in the options market places. In the last six months both Nasdaq OMX PHLX and the ISE have introduced, for some securities, maker-taker pricing on top of their customer-priority pro-rata allocation models. This competitive positioning between the exchanges continues to bring new benefits and enhanced efficiencies to all market participants.

A. Risks Posed by Lack of a Fee Cap

As noted by commenters to other previous actions (Citadel's Petition for Rule Making[4] and NYSE Arca's Proposed Rule Change Amending its Schedule of Fees[5]) and highlighted most recently by the Commission's proposal to eliminate flash and step up orders[6], the lack of an exchange fee cap for access to options exchanges' best prices poses certain risks to the efficient operation of the options markets.

- Without a fee cap, an options exchange could charge an exorbitant fee while acting as a "toll booth" between price levels. A market with an exorbitant fee would be the last market routed to, but as their quotation would still be protected, the price must be cleared at the high-priced market before the other exchanges could trade at a new price level.

- Without a fee cap, an options exchange could levy a distortive access fee. Any access fee of greater than $0.99 per contract, while appearing in the consolidated quote as a better price, would cause an execution at an "all-in" net worse price.

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2 In addition to the launch of BATS Options on Feb 26th, CBOE received approval for C2 on December 10th, 2009; see Securities Exchange Act Release No. 61152 (December 10, 2009), 74 FR 66699 (December 16, 2010) (File No. 10-191).

3 See, e.g., Securities Exchange Act Release No. 61864 (April 7, 2010), 75 FR 19443 (April 14, 2010) (SR-NYSEAmex-2010-26).

4 Letter from John C. Nagel, Managing Director and Deputy General Counsel, Citadel Investment Group L.L.C., to Nancy M. Morris, Secretary, Commission, dated July 15th, 2008 (File No. 4-562).

5 Securities Exchange Act Release No. 58295 (August 4, 2008), 73 FR 46681 (August 11, 2008) (SR-NYSEArca-2008-75).

6 See Flash Order Proposal, supra note 1.

- The wider the disparity in access fees between different exchanges, the less informative, accurate and useful are the displayed prices of the exchanges.

Through the implementation of the proposed access fee cap, a structure similar to the fee cap currently in place for the equities, the Commission can address all of these issues. It is clear; a fee limitation supports the integrity of the price protection requirement of existing trade-through rules.

B. PFOF and Step-ups

Payment for order flow ("PFOF") is when a market maker offers inducements to brokers that direct orders to the market maker. To support payment for order flow programs, many exchanges have adopted fees on market makers to facilitate their members' payment for order flow. The Commission has noted many times that PFOF raises potential conflicts of interest and that reliance on payment for orders may pose a threat to aggressive quotation competition[7]. While these issues and concerns are absolutely valid, the Commission accurately states in its proposal that "Payment for order flow fees are not fees imposed by an exchange on incoming orders for executing against an exchange's quotation." [8] As such, PFOF does not pose the same risks and issues as a lack of fee cap discussed above.

This does not mean that the Commission should ignore PFOF. In the past, the Commission has taken the stance that other competitive and structural forces can address many of the concerns related to PFOF. This includes competition between exchanges and their different market models. More, by continuing to move forward with programs like the Options Penny Pilot the Commission has created an environment where market forces pressuring and compressing PFOF rates.

Step-up auctions are an important crutch for PFOF programs. They enable firms that provide order flow to route their orders to markets that are *not* displaying the most competitive price. The introduction of an options exchange access fee eliminates the strongest and most logical argument in favor of keeping step-up auctions in place. The Commission needs to continue to foster competition between exchanges by eliminating step-ups concurrently with the introduction of these proposed fee caps.

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7 Options Concept Release; Securities Exchange Act Release No. 49175 (February 3, 2004), 69 FR 6124 (February 9, 2004) (File No. S7-07-04).

8 Proposed Amendments to Rule 610 of Regulation NMS; Securities Exchange Act Release No. 61902 (April 14, 2010), 75 FR 20738, 20748 (April 20, 2010) (File No. S7-09-10).

Cap Level and Applicability

The Commission has proposed a flat fee cap of $0.30 per contract and based this proposed fee level on several factors, including the desire to be consistent with the maximum fee limit for NMS stocks. As the most recent options exchange to begin trading, BATS currently charges $0.30 per contract to remove liquidity from our order book and we believe that we can effectively compete, innovate and drive the markets forward within a fee limit set at any level between $0.30 and $0.99. There are several points that BATS would like to reinforce as the Commission evaluates further the appropriate level at which to set the cap.

- An "all-in" fee cap at $0.99 or less will ensure that an apparently better priced quotation does in fact offer net economic benefit to an order routing firm.

- Access fees in excess of the $0.30 proposed limit have been charged and used to subsidize liquidity provider rebates. These rebates have incented aggressive quoting and helped tighten spreads and put pressure on payment for order flow.

- "Licensing fees", "Index surcharges" and options regulatory fees ("ORF") are common additional charges applied when accessing an exchange's best bid or offer. While some of these charges are applicable only in certain products, they have the same impact on "all-in" access cost as any other sort of access fee. As such, they should clearly fall within the scope of this rule.

We believe that the most important thing that the Commission can do when setting the cap level is to keep the structure simple and apply it universally. The cap should be an "all-in" cap. In its proposal, the Commission noted the wide disparity in the level of fees charged by the options exchanges. More than that, the fee structures are exceedingly complex, with the fee schedules of some exchanges comprising multiple pages. Anything the Commission can do to help simplify this complexity for investors and trading firms is good for the markets. A simple "all-in" cap will reinforce the informative and useful nature of *all* options quotations.

Conclusion

BATS supports the introduction of the access fee limits for accessing an options exchange's best price. An "all-in" fee cap will foster efficient access to the options markets and reinforce that the competitive forces at work today, creating a beneficial trading environment for all investors and trading firms.

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BATS appreciates the opportunity to comment on the Commission's proposal. Please feel free to contact me if you have any questions in connection with matter.

Sincerely,

Jeromee Johnson
Vice President, Market Development

Cc: The Hon. Mary L. Schapiro, Chairman
The Hon. Kathleen L. Casey, Commissioner
The Hon. Elisse B. Walter, Commissioner
The Hon. Luis A. Aguilar, Commissioner
The Hon. Troy A. Paredes, Commissioner
Robert W. Cook, Director, Division of Trading and Markets
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