



July 1, 2016

Brent Fields  
Secretary  
Securities and Exchange Commission  
100 F. Street N.E.  
Washington, D.C. 20549-1090

**RE: Exchange Act Release No. 77117, File No. SR-NYSEArca-2016-08 (the  
“Proposal”)**

Dear Mr. Fields:

Bats Global Markets, Inc. (“Bats”) appreciates the opportunity to comment on the Proposal. Bats operates four registered national securities exchanges in the U.S. for the trading of equity securities, including ETPs, as well as two options markets in the U.S., and a recognized investment exchange in Europe. There are 30 unique registered market makers across its four equity trading platforms, 28 of which make markets in ETPs. Bats BZX Exchange is a listing venue for ETPs, and currently lists 95 ETPs and has 24 registered market makers in ETPs. In addition, Bats is the number one exchange operator for the trading of ETPs, with its four equity exchanges accounting for 24.5% of the daily trading volume in ETPs, more than any other exchange group. As such, Bats is acutely interested in exchange-listed actively managed products with less frequent than daily portfolio disclosure (“Semi-Transparent Active ETFs”) and the regulatory structure in place around them.

Since first being introduced in 1993, the total assets under management in U.S. ETPs has grown to \$2.2 trillion and eight of the top ten most heavily traded products on Bats’ equity trading platforms are ETPs. Based on an average operational cost (including direct and indirect portfolio fees and external client costs) of 0.41% and 0.28% in equity and bond mutual funds, respectively, and 0.15% and 0.14% for equity and bond ETPs, respectively, investors currently save more than \$5.2 billion annually by investing in ETPs rather than in mutual funds in operational costs alone. These numbers assume that portfolio management fees across traditional mutual fund and ETP wrappers remain constant and also don’t include the tax benefits of investing in ETPs as compared to mutual funds. Looking at the assets currently held in mutual funds (\$8.26 trillion in equity and \$3.57 trillion in bond), and assuming the same operational costs, investors stand to save more than \$26 billion dollars annually in operational costs alone as the next generation of ETPs are introduced to compete with mutual fund products.

Bats believes that Semi-Transparent Active ETFs represent the next generation of ETPs and that, rather than applying opaque regulatory standards for Semi-Transparent Active ETFs, the Commission needs to publicly set standards for the industry to follow. In particular, Bats believes that the Commission needs to clarify its position on numerous issues related to Semi-Transparent Active ETFs, including: what constitutes adequate market making support, including both the number of market makers and their ability to make a market; what is the standard for reviewing reverse engineering and evaluating reverse engineering risk; and the frequency with

which an intraday NAV equivalent must be disseminated. Bats is not aware of the Commission establishing or using any such standards for the listing of other transparent ETPs, closed-end funds, or even corporate securities. As an example, Berkshire Hathaway A shares are very similar in structure to Semi-Transparent Active ETFs and typically trade with a spread of approximately 0.0608%. Would the Commission propose to use 0.0608% as the standard for adequate market making support because investors are already permitted to pay that spread when they invest in Berkshire Hathaway A shares? Bats does not present this example to advocate that the Commission apply Berkshire Hathaway A shares as the standard, but rather to highlight that there are many regulatory standards that are being applied in an opaque manner that should be open for public discussion.

With that background in mind, Bats intends its comments to reflect its broad support of the various types and structures of all Semi-Transparent Active ETFs, provided that they meet certain standards established by the Commission, and focuses its comments below primarily on the benefits to investors of Semi-Transparent Active ETFs, market making in Semi-Transparent Active ETFs, and reverse engineering a Semi-Transparent Active ETF portfolio.

#### I. A Semi-Transparent Active ETF Structure is in the Best Interest of Investors

SEC approval and the subsequent growth of ETPs in the U.S. market has greatly benefited investors of all ages by providing broad and inexpensive access to products with lower account minimums that simplify portfolio diversification and new and innovative portfolio strategies. The Commission stands as the last obstacle to a vast expansion of these investor benefits through the introduction of Semi-Transparent Active ETFs. To this point, listing and trading Semi-Transparent Active ETFs on national securities exchanges will similarly reduce costs and increase accessibility as compared to comparable products. Bats believes that, much like other ETPs developed before Semi-Transparent Active ETFs, as these products begin listing and trading on an exchange, the expense ratio for these products as compared to non-exchange listed products will decrease significantly. This will save investors millions of dollars through decreased fees and improved long-term performance. Further, being listed on an exchange will immediately allow all investors with a brokerage account to buy or sell any Semi-Transparent Active ETF. In order to realize these benefits, however, the products must trade in the same manner as existing ETPs in order to minimize the implementation cost within existing market infrastructure and, perhaps more importantly, to avoid investor confusion about pricing and the mechanics of trading the products. In addition to encouraging broader acceptance and adoption of Semi-Transparent Active ETFs, trading in the same manner as existing ETPs will allow for true intraday trading activity without exposure to volatility between the time an execution is agreed upon and the time that NAV is calculated.

#### II. Making a Market in Semi-Transparent Active ETFs

As highlighted above, Bats requests additional detail about the standard of review and the process used in determining whether market makers will be able to make a market in Semi-Transparent Active ETFs and firmly believes that such standards should be fully transparent. In drafting this comment letter, Bats solicited input from numerous ETP market makers about their

ability to make markets in Semi-Transparent Active ETFs. Based on their feedback, the record is clear that market makers can make a market in these products and are absolutely willing to make a market in these products. Furthermore, market makers clearly stated that making a market in these products is similar and perhaps simpler than making markets in foreign-based ETPs that hold instruments without reliable pricing information available during U.S. market hours. Others noted that making a market in Semi-Transparent Active ETFs would be analogous to existing daily disclosed portfolio actively managed products because such funds are able to make large position changes intraday that would cause the portfolio (and thus NAV) to diverge significantly from the previous day's disclosed portfolio. Similarly, another market maker made comparisons to making a market in closed-end funds as well as pricing NAV trades for clients. The overarching theme is that ETP market makers already make markets in products that they view as having similar risk and trading profiles as Semi-Transparent Actively Managed ETFs and could make markets in these products.

Bats notes that even if one assumes that market makers aren't able to make tight markets and spreads will be significantly wider in Semi-Transparent Active ETFs than in other ETPs, a point that Bats isn't willing to concede, such wider spreads (or the cost to buy or sell the product) should be evaluated in conjunction with the reduction in expense ratios highlighted above. As these products are generally designed to be bought and held long-term, the impact on an investor's returns of the difference in cost of buying and selling a product will likely be minimal compared to that of the difference in expense ratios over the entirety of the holding period.

### III. Reverse Engineering a Semi-Transparent Active ETF Portfolio

Bats again requests that the Commission provide additional detail about the standard of review and process employed to determine the potential for reverse engineering the portfolio of a Semi-Transparent Active ETF. Such clearly enumerated standards are necessary in order for issuers to dedicate the resources to develop products with the certainty that they will not be prevented from coming to market based on an amorphous reverse engineering concern. Bats also notes that there is a tension between the ability to reverse engineer the portfolio of a Semi-Transparent Active ETF and the ability for market makers to make tight markets in the products and encourages the Commission to keep that tension in mind when evaluating both standards. If the Commission truly believes that these portfolios should be impossible to reverse engineer, Bats believes that the Commission should consider establishing a sample portfolio process in which an issuer provides a sample portfolio that the Commission would attempt to reverse engineer. If they are unable to reverse engineer the portfolio within some degree of accuracy, then the product should overcome any reverse engineering concerns.

Broadly speaking, assuming that a firm could reverse engineer the portfolio of a Semi-Transparent Active ETF, Bats believes that the time and resources necessary to do so would only make economic sense in very high volume products and would be a significantly less profitable endeavor in buy and hold type of products that are likely to have lower trading volumes like Semi-Transparent Active ETFs. Regardless, there would be a self-policing effect because an issuer would only bring a product to market as a Semi-Transparent Active ETF where the portfolio manager wants to prevent public disclosure of a strategy. If firms were able to reverse

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engineer the portfolio of a Semi-Transparent Active ETF, the structure immediately loses its largest benefit and issuers would either issue such products without listing on an exchange (and retain the ability to disclose less frequently without fear of reverse engineering) or list them on an exchange as an actively managed product with daily portfolio disclosure.

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Bats appreciates the opportunity to comment on the Proposal and more broadly on Semi-Transparent Active ETFs. As discussed above, Bats believes that Semi-Transparent Active ETFs represent the next generation of ETPs and Commission approval is the only remaining obstacle keeping the myriad benefits highlighted above, including millions of dollars in savings, from investors. Bats would welcome the opportunity to provide the Commission with any additional information that it might find useful or to further discuss any of the issues raised herein.

Sincerely,



Eric Swanson  
General Counsel & Secretary

Cc: The Honorable Mary Jo White, Chair  
The Honorable Michael S. Piwowar, Commissioner  
The Honorable Kara M. Stein, Commissioner  
Stephen Luparello, Director, Division of Trading and Markets