

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-66808; File No. SR-BATS-2012-013)

April 13, 2012

Self-Regulatory Organizations; BATS Exchange, Inc.; Order Approving a Proposed Rule Change to Amend BATS Exchange, Inc. Rule 2.12 to Make Permanent the Pilot Program that Permits BATS Exchange, Inc. to Receive Inbound Routes of Equities Orders through BATS Trading, Inc., BATS Exchange's Routing Broker-Dealer, from BATS-Y Exchange, Inc.

I. Introduction

On March 8, 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 requesting permanent approval of the Exchange's pilot program that permits the Exchange to receive inbound routes of equities orders through BATS Trading, Inc. ("BATS Trading"), the Exchange's routing broker-dealer, from BATS Y-Exchange, Inc. ("BATS-Y"). The proposed rule change was published for comment in the Federal Register on March 14, 2012.<sup>3</sup> The Commission received no comment letters regarding the proposed rule change. This order approves the proposed rule change.

II. Background

BATS Trading is a broker-dealer that is a member of the Exchange and is permitted to provide members of BATS-Y optional routing services to other market centers.<sup>4</sup> BATS Trading

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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. 66571 (March 12, 2012), 77 FR 15153 ("Notice").

<sup>4</sup> BATS Trading operates as a facility of BATS-Y that provides outbound routing from BATS-Y to other market centers, subject to certain conditions. See Securities Exchange Act Release No. 62716 (August 13, 2010), 75 FR 51295 (August 19, 2010) (File No. 10-

is owned by BATS Global Markets (“Corporation”). The Corporation also owns two registered securities exchanges – the Exchange<sup>5</sup> and BATS-Y.<sup>6</sup> Thus, BATS Trading is an affiliate of the Exchange and BATS-Y.

On September 9, 2010, the Exchange filed an immediately effective proposed rule change to, among other things, permit the Exchange to receive inbound routes of orders that BATS Trading routes in its capacity as a facility of BATS-Y on a pilot basis ending October 15, 2011.<sup>7</sup> On September 29, 2011, the Exchange filed an immediately effective proposed rule change to extend the pilot period six months ending April 15, 2012.<sup>8</sup> The Exchange now seeks permanent approval of this inbound routing pilot.<sup>9</sup>

### III. Discussion and Commission Findings

After careful review, the Commission finds that the proposed rule change is consistent with the requirements of the Act and the rules and regulations thereunder applicable to a national securities exchange.<sup>10</sup> Specifically, the Commission finds that the proposed rule change is consistent with Section 6(b)(1) of the Act,<sup>11</sup> which requires, among other things, that a national

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198) (Order granting the exchange registration of BATS-Y Exchange, Inc.) (“BATS-Y Approval Order”).

<sup>5</sup> See Securities Exchange Act Release No. 58375 (August 18, 2008), 73 FR 49498 (August 21, 2008) (File No. 10-182) (order granting the exchange registration of BATS Exchange, Inc.).

<sup>6</sup> See generally BATS-Y Approval Order, supra note 4.

<sup>7</sup> See Securities Exchange Act Release No. 62901 (September 13, 2010), 75 FR 57097 (September 17, 2010) (SR-BATS-2010-024) (“Inbound Router Notice”).

<sup>8</sup> See Securities Exchange Act Release No. 65516 (October 7, 2011), 76 FR 63977 (October 14, 2011) (SR-BATS-2011-040).

<sup>9</sup> See Notice, supra note 3.

<sup>10</sup> In approving this proposed rule change, the Commission has considered the proposed rule’s impact on efficiency, competition and capital formation. 15 U.S.C. 78c(f).

<sup>11</sup> 15 U.S.C. 78f(b)(1).

securities exchange be so organized and have the capacity to carry out the purposes of the Act, and to comply and enforce compliance by its members and persons associated with its members, with the provisions of the Act, the rules and regulation thereunder, and the rules of the Exchange. Further, the Commission finds that the proposed rule change is consistent with Section 6(b)(5) of the Act,<sup>12</sup> which requires, among other things, that the rules of a national securities exchange be designed to prevent fraudulent and manipulative acts and practices; to promote just and equitable principles of trade; to foster cooperation and coordination with persons engaged in regulating, clearing, settling, and 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. Section 6(b)(5) also requires that the rules of an exchange not be designed to permit unfair discrimination among customers, issuers, brokers, or dealers.

Recognizing that the Commission has previously expressed concern regarding the potential for conflicts of interest in instances where a member firm is affiliated with an exchange to which it is routing orders, the Exchange previously implemented limitations and conditions to BATS Trading's affiliation with the Exchange to permit the Exchange to accept inbound orders that BATS Trading routes in its capacity as a facility of BATS-Y, on a pilot basis.<sup>13</sup> The Exchange now seeks to make this pilot permanent. Specifically, the Exchange states it is in compliance with the following limitations and conditions:<sup>14</sup>

- The Exchange shall enter into a plan pursuant to Rule 17d-2 under the Exchange Act with a non-affiliated self-regulatory organization (“SRO”) to relieve the Exchange of

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<sup>12</sup> 15 U.S.C. 78f(b)(5).

<sup>13</sup> See Inbound Router Notice, 75 FR at 57097.

<sup>14</sup> See Notice, 77 FR at 15154.

regulatory responsibilities for BATS Trading with respect to rules that are common rules between the Exchange and the non-affiliated SRO, and enter into a regulatory contract (“Regulatory Contract”) with a non-affiliated SRO to perform regulatory responsibilities for BATS Trading for unique Exchange rules.

- The Regulatory Contract shall require the Exchange to provide the non-affiliated SRO with information, in an easily accessible manner, regarding all exception reports, alerts, complaints, trading errors, cancellations, investigations, and enforcement matters (collectively “Exceptions”) in which BATS Trading is identified as a participant that has potentially violated Exchange or Commission Rules, and shall require that the non-affiliated SRO provide a report, at least quarterly, to the Exchange quantifying all Exceptions in which BATS Trading is identified as a participant that has potentially violated Exchange or Commission Rules.
- The Exchange, on behalf of the Corporation, shall establish and maintain procedures and internal controls reasonably designed to ensure that BATS Trading does not develop or implement changes to its system on the basis of non-public information regarding planned changes to Exchange systems, obtained as a result of its affiliation with the Exchange, until such information is available generally to similarly situated member organizations of the Exchange in connection with the provision of inbound order routing to the Exchange.
- The Exchange may furnish to BATS Trading the same information on the same terms that the Exchange makes available in the normal course of business to any other member organization.

The Exchange believes that by meeting the above-listed conditions it has set up mechanisms that

protect the independence of the Exchange's regulatory responsibility with respect to BATS Trading, and has demonstrated that BATS Trading cannot use any information that it may have because of its affiliation with the Exchange to its advantage.<sup>15</sup>

In the past, the Commission has expressed concern that the affiliation of an exchange with one of its members raises potential conflicts of interest, and the potential for unfair competitive advantage.<sup>16</sup> Although the Commission continues to be concerned about potential unfair competition and conflicts of interest between an exchange's self-regulatory obligations and its commercial interest when the exchange is affiliated with one of its members, for the reasons discussed below, the Commission believes that it is consistent with the Act to permit BATS Trading, in its capacity as a facility of BATS-Y, to provide inbound routing to the Exchange on a permanent basis instead of a pilot basis, subject to the other conditions described above.

The Exchange has proposed four ongoing conditions applicable to BATS Trading's inbound routing activities in its capacity as a facility of BATS-Y, which are enumerated above. The Commission believes that these conditions mitigate its concerns about potential conflicts of interest and unfair competitive advantage. In particular, the Commission believes that a non-

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<sup>15</sup> See id.

<sup>16</sup> See, e.g., Securities Exchange Act Release Nos. 54170 (July 18, 2006), 71 FR 42149 (July 25, 2006) (SR-NASDAQ-2006-006) (order approving Nasdaq's proposal to adopt Nasdaq Rule 2140, restricting affiliations between Nasdaq and its members); 53382 (February 27, 2006), 71 FR 11251 (March 6, 2006) (SR-NYSE-2005-77) (order approving the combination of the New York Stock Exchange, Inc. and Archipelago Holdings, Inc.); 58673 (September 29, 2008), 73 FR 57707 (October 8, 2008) (SR-Amex-2008-62) (order approving the combination of NYSE Euronext and the American Stock Exchange LLC); 59135 (December 22, 2008), 73 FR 79954 (December 30, 2008) (SR-ISE-2009-85) (order approving the purchase by ISE Holdings of an ownership interest in DirectEdge Holdings LLC); and 59281 (January 22, 2009), 74 FR 5014 (January 28, 2009) (SR-NYSE-2008-120) (order approving a joint venture between NYSE and BIDS Holdings L.P.).

affiliated SRO's oversight of BATS Trading,<sup>17</sup> combined with a non-affiliated SRO's monitoring of BATS Trading's compliance with the Exchange's rules and quarterly reporting to the Exchange, will help to protect the independence of the Exchange's regulatory responsibilities with respect to BATS Trading.

V. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,<sup>18</sup> that the proposed rule change (SR-BATS-2012-013) be, and hereby is, approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>19</sup>

Kevin M. O'Neill  
Deputy Secretary

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<sup>17</sup> This oversight will be accomplished through a 17d-2 Agreement. See Inbound Router Notice, 75 FR at 57097.

<sup>18</sup> 15 U.S.C. 78s(b)(2).

<sup>19</sup> 17 CFR 200.30-3(a)(12).