

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-73571; File No. SR-BATS-2014-040)

November 10, 2014

Self-Regulatory Organizations; BATS Exchange Inc.; Order Approving a Proposed Rule Change, as Modified by Amendment No. 1, Modifying Rule 21.7 of BATS Exchange, Inc.

I. Introduction

On September 12, 2014, BATS Exchange, Inc., (“BATS” or the “Exchange”) filed with the Securities and Exchange Commission (the “Commission”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”)¹ and Rule 19b-4 thereunder,² a proposed rule change amending BATS Rule 21.7. The proposed rule change was published for comment in the Federal Register on September 30, 2014.³ On October 10, 2014, the Exchange filed Amendment No. 1 to the proposed rule change.⁴ The Commission received no comments on the proposal. This order approves the proposed rule change, as modified by Amendment No. 1.

II. Description of the Proposal

BATS proposes to amend BATS Rule 21.7 (“Market Opening Procedures”) to modify the process by which the Exchange’s equity options trading platform (“BATS Options”) opens trading at the beginning of the day and after trading halts. Specifically, the BATS proposal

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

³ See Securities Exchange Act Release No. 73203 (September 24, 2014), 79 FR 58845 (“Notice”).

⁴ In Amendment No. 1, the Exchange further clarified the process by which the Exchange’s equity options trading platform opens trading at the beginning of the day and after trading halts. Amendment No. 1 has been placed in the public comment file for SR-BATS-2014-040 at <http://www.sec.gov/comments/sr-bats-2014-040/bats2014040-1.pdf> (See letter from Anders Franzon, VP, Associate General Counsel, BATS, to Secretary, Commission, dated October 16, 2014) and is also available on the Exchange’s website.

would modify the Opening Process⁵ set forth in BATS Rule 21.7 as follows: (1) orders in the Opening Process will be executed based on time priority instead of price-time priority; (2) certain orders that are not executed during the Opening Process will be treated as if they had been entered by a User⁶ rather than canceled; and (3) add certain clarifying language to BATS Rule 21.7 in order to make the Opening Process more clear.⁷ The Exchange is not proposing to amend the process by which orders are entered or the Opening Price is determined or validated.

Currently, after establishing an Opening Price that is also a Valid Price,⁸ orders and quotes in the Exchange's System⁹ that are priced equal to or more aggressively than the Opening Price will be matched based on price-time priority and in accordance with BATS Rule 21.8. Under the current process, all orders and quotes or portions thereof that are matched pursuant to the Opening Process will be executed at the Opening Price. Further, under the current rule, orders that meet the following criteria which are not executed during the Opening Process are cancelled: (i) limit orders that are priced equal to or more aggressively than the Opening Price; and (ii) market orders.¹⁰ Where the Exchange currently opens trading in a series pursuant to BATS Rule 21.7(a)(1)(D) (where there is no NBBO Midpoint, no Print, and no Previous Close at a Valid Price) (a "Contingent Open") and there is at least one price level at which at least one contract of a limit order could be executed, the System similarly cancels all orders that are priced equal to or more aggressively than the midpoint of the most aggressively priced bid and the most

⁵ See BATS Rule 21.7(a) (defining "Opening Process").

⁶ See BATS Rule 16.1(a)(63) (defining "User").

⁷ The Exchange also proposes to add titles to BATS Rule 21.7(a)(1), (2), (3), and (4).

⁸ See BATS Rule 21.7(a)(2) (defining "Valid Price").

⁹ See BATS Rule 1.5(aa) (defining "System").

¹⁰ See Notice, supra note 3, at 58845.

aggressively priced offer.¹¹ The Exchange states that under its current Opening Process, limit orders and quotes that are not executed during the Opening Process or cancelled become eligible for trading on BATS Options immediately following the completion of the Opening Process.¹²

The Exchange proposes to amend its rules in order to match orders for execution in the Opening Process based on time priority rather than price-time priority and in accordance with BATS Rule 21.9. The Exchange believes that handling orders in time priority makes more sense than price-time priority for the Opening Process because, according to the Exchange, the price of an order is not particularly important to the Opening Process, so long as the order is priced at or more aggressively than the Opening Price, which can only be one of three prices: the midpoint of the NBBO; the last regular way print disseminated to the OPRA Plan¹³ after 9:30 a.m.; or the last regular way transaction from the previous trading day as disseminated pursuant to OPRA.¹⁴ According to the Exchange, because the Opening Price is always based on a price-taking process rather than a price-forming process, there is no reason to reward a more aggressive order with priority in the Opening Process.¹⁵ Therefore, the Exchange proposes that all orders and quotes that are priced equal to or more aggressively than the Opening Price will be matched based only on time priority and will be matched until there is no remaining volume or there is an imbalance

¹¹ See id.

¹² See id. The Exchange also notes that, under its current Opening Process, where there are no orders in a series that are matched at the Opening Price, the System will open the series for trading. See id. at 58845-58846.

¹³ See BATS Rule 27.1(15) (defining “OPRA Plan”).

¹⁴ See Notice, supra note 3, at 58846. See also BATS Rule 27.1(14) (defining “OPRA”).

¹⁵ See Notice, supra note 3, at 58846.

of orders that are not executed in whole or in part, at which point all matched orders and quotes will be executed at the Opening Price.¹⁶

The Exchange also proposes to handle all orders that are not executed in the Opening Process in time priority. Specifically, the Exchange proposes to handle such orders in time sequence, beginning with the order with the oldest time stamp and may, in whole or in part, place such orders on the BATS Options Book,¹⁷ cancel the orders, execute the orders, or route the orders in accordance with BATS Rule 21.9.¹⁸ According to the Exchange, all orders that were eligible for execution in the Opening Process that were not executed will be processed ahead of any orders received after the conclusion of the Opening Process.¹⁹ If an order is placed on the BATS Options Book, it will then be subject to the standard price-time priority and subject to BATS Rule 21.8.²⁰ According to the Exchange, the proposed functionality will apply to all orders, including both those orders that are not executed under proposed BATS Rule 21.7(a)(3) and orders in a series that is opening subject to a Contingent Open.²¹ The Exchange states that although it currently cancels any orders that are not executed in the Opening Process that are priced more aggressively than the Opening Price, the Exchange now proposes to simply enter these orders onto the BATS Options Book as described above in order to minimize the number of orders that are cancelled and must be reentered by Users.²² The Exchange notes that all order

¹⁶ See id.

¹⁷ See BATS Rule 16.1(a)(9) (defining “BATS Options Book”).

¹⁸ See Notice, supra note 3, at 58846.

¹⁹ See Amendment No.1 at 3.

²⁰ See Notice, supra note 3, at 58846.

²¹ See id.

²² See id.

protections, including Trade-Through²³ protection and a BATS Market Order²⁴ collar, will apply to orders entered pursuant to proposed BATS Rules 21.7(a)(3) and 21.7(a)(4).

The Exchange also proposes to eliminate the current functionality that cancels orders that are not executed during the Opening Process that fit the following criteria: (i) limit orders that are priced equal to or more aggressively than the Opening Price; and (ii) market orders.²⁵

Further, the Exchange proposes to eliminate the current functionality for a series subject to a Contingent Open where, if there is at least one price level at which at least one contract of a limit order can be executed, the System will cancel all orders that are priced equal to or more aggressively than the midpoint of the most aggressively priced bid and the most aggressively priced offer.²⁶ According to BATS, for many Users, cancelling orders that were entered for participation in the Opening Process negates the advantages of allowing orders to be entered prior to the beginning of regular way trading and the Opening Process.²⁷

Finally, the Exchange proposes certain clarifying changes to its Opening Process rules. For example, the Exchange proposes to add language to Rule 21.7(a)(3) stating that the Opening Process will be performed after the establishment of an Opening Price that is a Valid Price²⁸ and

²³ See BATS Rule 27.1(22) (defining “Trade-Through”).

²⁴ See BATS Rule 21.1(d)(5) (defining “BATS Market Order”).

²⁵ See Notice, supra note 3, at 58846.

²⁶ See id. The Exchange notes that although not cancelling these orders might result in executions at a price that is not the same as the Opening Price that occurs as the orders are handled in time sequence (either on BATS Options or upon routing to another options exchange), these executions would be part of regular way trading and are distinct from the opening execution that occurs as a result of the Opening Process. See id.

²⁷ See id.

²⁸ See BATS Rule 21.7(a)(2) (defining “Valid Price”).

that matches will occur until there is no remaining volume or there is an imbalance of orders.²⁹

The Exchange believes that both of these concepts are implicit in the rule.³⁰

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.³¹ In particular, the Commission finds that the proposed rule change is consistent with Section 6(b)(5) of the Act,³² 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 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 proposed rule change is designed to modify the Exchange's Opening Process for options listed on the Exchange to ensure that BATS Options opens trading in options contracts in a fair and orderly manner. As noted above, the Exchange believes that handling orders in time priority (as opposed to price-time priority) will create a more orderly opening and makes more sense because the price of the order is not particularly important to the Opening Process, provided the order is priced at or more aggressively than the Opening Price. Under such circumstances, the Exchange believes that there is no reason to reward a more aggressive order with priority in the Opening Process. In addition, the Exchange also believes that entering orders in time sequence based on the time of receipt instead of canceling certain orders will create a

²⁹ See Notice, supra note 3, at 58846.

³⁰ See id.

³¹ In approving this proposal, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

³² 15 U.S.C. 78f(b)(5).

more orderly opening because Users will be able to enter orders and quotes prior to the opening of trading and be assured that such orders will either participate in the Opening Process or be handled as if they were entered immediately following the Opening Process. The Exchange believes that these changes will provide market makers and Users greater control and flexibility with respect to entering orders and quotes because they will no longer have to reenter orders that may have been canceled because they were not executed in the opening process.

The Commission believes that the proposed rule change is designed to facilitate the opening of options trading on BATS Options in a fair and orderly manner. Further, the Commission believes that the proposal could benefit investors by providing Users with certainty that orders that are entered prior to the Opening Process will not be cancelled based on market conditions outside of a User's control. The Commission further notes that all order protections, including Trade-Through protection and the BATS Market Order collar, will apply to orders entered pursuant to proposed BATS Rules 21.7(a)(3) and 21.7(a)(4).³³

³³ See Notice, supra note 3 at 58846.

IV. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,³⁴ that the proposed rule change (SR-BATS-2014-040), as modified by Amendment No.1, is approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.³⁵

Kevin M. O'Neill
Deputy Secretary

³⁴ 15 U.S.C. 78s(b)(2).

³⁵ 17 CFR 200.30-3(a)(12).