

SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-67558; File No. SR-BATS-2012-030)

August 1, 2012

Self-Regulatory Organizations; BATS Exchange, Inc.; Notice of Filing of Proposed Rule Change to Amend BATS Rule 14.11, Entitled “Other Securities”

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act” or “Exchange Act”),¹ and Rule 19b-4 thereunder,² notice is hereby given that, on July 20, 2012, BATS Exchange, Inc. (“Exchange” or “BATS”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the Exchange. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Self-Regulatory Organization’s Statement of the Terms of Substance of the Proposed Rule Change

The Exchange proposes to amend Rule 14.11, entitled “Other Securities,” to modify the criteria for certain securities listed on BATS Exchange as Index Fund Shares. The text of the proposed rule change is available at the Exchange’s website at <http://www.batstrading.com>, at the principal office of the Exchange, and at the Commission’s Public Reference Room. The proposed rule text can be found in Exhibit 5.

II. Self-Regulatory Organization’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the Exchange included statements concerning the purpose of, and basis for, the proposed rule change and discussed any comments it received on the proposed rule change. The text of these statements may be examined at the places specified

¹ 15 U.S.C. 78s(b)(1).

² 17 CFR 240.19b-4.

in Item IV below. The Exchange has prepared summaries, set forth in Sections A, B, and C below, of the most significant parts of such statements.

A. Self-Regulatory Organization’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

Proposal to Amend Index Fund Shares Rules

The Exchange proposes certain changes to Rule 14.11(c), relating to Index Fund Shares, to conform the Exchange’s listings criteria for Index Fund Shares with the analogous criteria in place for NYSE Arca Equities, Inc. (“NYSE Arca”).³ Specifically, the Exchange proposes to amend Exchange Rule 14.11(c) (“Index Fund Shares”) to: (1) modify the weight and volume requirement for component stocks comprising the applicable index or portfolio for any U.S. index or portfolio and any international or global index or portfolio upon which Index Fund Shares are based; (2) exclude Index Fund Shares, Portfolio Depositary Receipts, Trust Issued Receipts, and Managed Fund Shares (collectively, “Derivative Securities Products”)⁴ when applying the quantitative generic listing criteria in Rule 14.11(c); and (3) modify the minimum number of component stocks for any U.S. index or portfolio and any international or global index or portfolio upon which Index Fund Shares are based to adopt certain exceptions for any index or portfolio that is partially or wholly comprised of Index Fund Shares or other Derivative Securities Products.

³ The Exchange notes that NYSE Arca uses the term Investment Company Units to describe the same products that the Exchange calls Index Fund Shares.

⁴ Rule 14.11 includes criteria for derivative securities that may be listed or traded on the Exchange, such as Portfolio Depositary Receipts, Trust Issued Receipts, and Managed Fund Shares.

Rule 14.11(c)(3) provides that the Exchange may approve a series of Index Fund Shares for listing and trading pursuant to Rule 19b-4(e)⁵ under the Act if such series satisfies the criteria set forth in that rule. The Exchange proposes to amend Rule 14.11(c)(3) to amend the index weight requirements and adopt notional volume traded per month⁶ to the initial listing standards for Index Fund Shares, commonly referred to as exchange-traded funds. The Exchange proposes to amend the minimum component stock weight requirement for monthly trading volumes from 90% to 70% of the weight of the underlying index. In addition, the Exchange proposes to adopt an alternative notional volume traded per month.

Currently for U.S. component stock indexes, Rule 14.11(c)(3)(A)(i)(b) provides that component stocks that in the aggregate account for at least 90% of the weight of the index or portfolio each shall have a minimum monthly trading volume during each of the last six months of at least 250,000 shares. The Exchange proposes to amend the minimum component stock weight requirement from 90% to 70% of the weight of the underlying index or portfolio. Further, the Exchange is proposing to adopt an average minimum trading volume requirement of 250,000 shares over a six-month period instead of in each of the last six months and to adopt a notional volume traded per month of \$25,000,000 averaged over the last six months as an option for meeting the listing requirements.

⁵ 17 CFR 240.19b-4(e). Rule 19b-4(e) provides that the listing and trading of a new derivative securities product by a self-regulatory organization (“SRO”) shall not be deemed a proposed rule change, pursuant to Rule 19b-4(c)(1), if the Commission has approved, pursuant to Section 19(b) of the Exchange Act, the SRO’s trading rules, procedures, and listing standards for the product class that would include the new derivatives securities product, and the SRO has a surveillance program for the product class.

⁶ The notional volume traded per month is the number of shares traded in a calendar month multiplied by the monthly closing price.

Currently for international or global indexes, Rule 14.11(c)(3)(A)(ii)(b) provides that component stocks that in the aggregate account for at least 90% of the weight of the index or portfolio each shall have a minimum worldwide monthly trading volume during each of the last six months of at least 250,000 shares. The Exchange proposes to amend the minimum component stock weight requirement from 90% to 70% of the weight of the underlying index or portfolio. Further, the Exchange is proposing to adopt an average minimum trading volume requirement of 250,000 shares over a six-month period instead of in each of the last six months and to adopt a worldwide notional volume traded per month of \$25,000,000 averaged over the last six months as an option for meeting the listing requirements. Further, the Exchange proposes to clarify that the component stock trading volumes are determined on a global basis.

With regard to the Exchange's proposal to amend the minimum component stock weight requirement for monthly trading volumes from 90% to 70% of the weight of the underlying index, the Exchange believes the proposed standard reasonably ensures that securities with substantial monthly trading volumes account for a substantial portion of the underlying index and, when applied in conjunction with the other applicable listing requirements, remain sufficiently broad-based in scope to minimize potential manipulation. The Exchange notes that the Commission has previously approved the listing and trading of exchange-traded funds based upon indices that were composed of stocks that did not meet the 90% monthly trading volume weight, but were above the proposed 70% monthly trading volume weight criteria.⁷ In addition,

⁷ See Securities Exchange Act Release No. 46306 (August 2, 2002), 67 FR 51916 (August 9, 2002) (SR-NYSE-2002-28) (approving the following funds for trading pursuant to unlisted trading privileges on NYSE: (1) Vanguard Total Stock Market VIPERs; (2) iShares Russell 2000 Index Funds; (3) iShares Russell 2000 Value Index Funds; and (4) iShares Russell 2000 Growth Index Fund); Securities Exchange Act Release No. 55953 (June 25, 2007), 72 FR 36084 (July 2, 2007) (SR-NYSE-2007-46) (approving listing on

this standard would conform to existing NYSE Arca requirements approved by the Commission.⁸

With respect to adopting, as an alternative to monthly trading volume, the notional volume traded for each of the last six months to the initial listing standards for both domestic and international indexes, the Exchange believes that notional volume traded averaged per month is a better measure of the liquidity of component stocks of the underlying index or indexes. Specifically, notional volume nullifies the volume discrepancies that generally occur between low priced and high priced stocks.⁹

With respect to adopting a six-month average, instead of in each of the last six-months, criterion for volume and notional volume, the Exchange believes that the averaged six-month period is a better indicator of the current liquidity on an index and serves to eliminate seasonal volume fluctuations of component securities. Further, investors, exchange-traded fund issuers, and third-party index sponsors would also benefit from the Exchange's ability to list – without the delay associated with a stand-alone rule filing – Index Fund Shares based on a broader group of indexes promoting competition.

NYSE of HealthShares Orthopedic Repair Exchange-Traded Fund); and Securities Exchange Act Release No. 56695 (October 24, 2007), 72 FR 61413 (October 30, 2007) (SR-NYSEArca-2007-111) (approving listing on NYSE Arca of HealthShares Ophthalmology Exchange-Traded Fund).

⁸ See NYSE Arca Rule 5.2(j)(3), Commentary .01(a)(A) and (B); see also Securities Exchange Act Release No. 61240 (December 24, 2009), 75 FR 168 (January 4, 2010) (SR-NYSEArca-2009-101) (approving proposed rule change to amend NYSE Arca Equities Rule 5.2(j)(3)).

⁹ For example, a stock priced at \$10 per share that trades 2,500,000 shares in a month has a notional volume of \$25,000,000. Conversely, a stock priced at \$100 per share that trades 250,000 shares in a month has a notional volume of \$25,000,000.

The Exchange also proposes to exclude Derivative Securities Products when applying the quantitative listing requirements of Rule 14.11(c)(3)(A)(i)(a), (b), and (c) and 14.11(c)(3)(A)(ii)(a), (b), and (c) relating to listing of Index Fund Shares based on a U.S index or portfolio or an international or global index or portfolio, respectively. Component stocks in the aggregate, excluding Derivative Securities Products, would be required to meet the criteria of these provisions. Thus, for example, when determining the component weight for the most heavily weighted stock and the five most heavily weighted component stocks for an underlying index that includes a Derivative Securities Product, the weight of any Derivative Securities Products included in the underlying index or portfolio would not be considered.

In addition, the Exchange proposes to modify the requirement in Rule 14.11(c)(3)(A)(i)(d) that an index or portfolio shall include a minimum of 13 component stocks for an index or portfolio that includes Derivative Securities Products. Specifically, the Exchange proposes that there shall be no minimum number of component stocks if (a) one or more series of Index Fund Shares or Portfolio Depositary Receipts (as defined in Exchange Rule 14.11(b)) constitute, at least in part, components underlying a series of Index Fund Shares, or (b) one or more series of Derivative Securities Products account for 100% of the weight of the index or portfolio. Thus, for example, if the index or portfolio underlying a series of Index Fund Shares includes one or more series of Index Fund Shares or Portfolio Depositary Receipts, or if it consists entirely of other Derivative Securities Products, then there would not be required to be any minimum number of component stocks (i.e., one or more components would be acceptable). However, if the index or portfolio consists of Derivative Securities Products other than Index Fund Shares or Portfolio Depositary Receipts (e.g., Managed Fund Shares) as well as securities

that are not Derivative Securities Products (e.g., common stocks), then there would have to be at least 13 components in the underlying index or portfolio.

In addition, the Exchange proposes to modify the requirement in 14.11(c)(3)(A)(ii)(d) that an index or portfolio shall include a minimum of 20 component stocks for an international or global index or portfolio that includes Derivative Securities Products. Specifically, the Exchange proposes that there shall be no minimum number of component stocks if (a) one or more series of Index Fund Shares or Portfolio Depositary Receipts (as defined in Exchange Rule 14.11(b)) constitute, at least in part, components underlying a series of Index Fund Shares, or (b) one or more series of Derivative Securities Products account for 100% of the weight of the index or portfolio. Thus, for example, if the index or portfolio underlying a series of Index Fund Shares includes one or more series of Index Fund Shares or Portfolio Depositary Receipts, or if it consists entirely of other Derivative Securities Products, then there would not be required to be any minimum number of component stocks (i.e., one or more components would be acceptable). However, if the index or portfolio consists of Derivative Securities Products other than Index Fund Shares or Portfolio Depositary Receipts (e.g., Managed Fund Shares) as well as securities that are not Derivative Securities Products (e.g., common stocks), then there would have to be at least 20 components in the underlying index or portfolio.

The Exchange believes it is appropriate to exclude Derivative Securities Products from the generic criteria specified above for Index Fund Shares and to adopt the above-described exceptions in so far as Derivative Securities Products that may be included in an index or portfolio underlying a series of Index Fund Shares are themselves subject to specific listing and continued listing requirements of the national securities exchange on which they are listed. Such Derivative Securities Products would have been listed and traded on a national securities

exchange pursuant to a filing submitted pursuant to Section 19(b)(2)¹⁰ or 19(b)(3)(A)¹¹ of the Act, or would have been listed by a national securities exchange pursuant to the requirements of Rule 19b-4(e)¹² under the Act. Finally, Derivative Securities Products are derivatively priced, and, therefore, it is not necessary to apply the generic quantitative criteria (market capitalization, trading volume, index or portfolio component weighting) applicable to non-Derivative Securities Products (e.g., common stocks) to such products.

In addition to the changes set forth above, the Exchange proposes to correct a typographical error in Rule 14.11(c)(4), where there currently are two sub-sections (c)(4)(B). The Exchange proposes to change the second reference to (c)(4)(C).

General Provisions

To the extent not specifically addressed in the proposed rules, the following general provisions of the Exchange's rules will continue to apply to all subject securities affected by the proposed rules ("securities").

Information Circular

Prior to the commencement of trading, the Exchange will inform its Members in an Information Circular of the special characteristics and risks associated with trading the securities. Specifically, the Information Circular will discuss the following: (1) the procedures for purchases and redemptions of the securities (and/or that the securities are not individually redeemable); (2) Exchange Rule 3.7, which imposes suitability obligations on Exchange Members with respect to recommending transactions in the securities to customers; (3) how

¹⁰ 15 U.S.C. 78s(b)(2).

¹¹ 15 U.S.C. 78s(b)(3)(A).

¹² 17 CFR 240.19b-4(e).

information regarding the Intraday Indicative Value is disseminated; (4) the risks involved in trading the securities during the Pre-Opening¹³ and After Hours Trading Sessions¹⁴ when an updated Intraday Indicative Value will not be calculated or publicly disseminated; (5) the requirement that Members deliver a prospectus to investors purchasing newly issued securities prior to or concurrently with the confirmation of a transaction; and (6) trading information.

In addition, the Information Circular will advise Members, prior to the commencement of trading, of the prospectus delivery requirements applicable to the securities. Members purchasing securities for resale to investors will deliver a prospectus to such investors. The Information Circular will also discuss any exemptive, no-action, and interpretive relief granted by the Commission from any rules under the Act.

In addition, the Information Circular will reference that the securities are subject to various fees and expenses described in the registration statement. The Information Circular will also disclose the trading hours of the securities and, if applicable, the Net Asset Value (“NAV”) calculation time for the securities. The Information Circular will disclose that information about the securities and the corresponding indexes, if applicable, will be publicly available on the website for the securities.

Trading Rules

The Exchange deems the securities to be equity securities, thus rendering trading in the securities subject to the Exchange’s existing rules governing the trading of equity securities. The securities will trade on the Exchange from 8:00 a.m. until 5:00 p.m. Eastern Time. The Exchange has appropriate rules to facilitate transactions in the securities during all trading

¹³ The Pre-Opening Session is from 8:00 a.m. to 9:30 a.m. Eastern Time.

¹⁴ The After Hours Trading Session is from 4:00 p.m. to 5:00 p.m. Eastern Time.

sessions. The minimum price increment for quoting and entry of orders in equity securities traded on the Exchange is \$0.01, with the exception of securities that are priced less than \$1.00 for which the minimum price increment for order entry is \$0.0001.¹⁵

Surveillance

The Exchange believes that its surveillance procedures are adequate to address any concerns about the trading of the securities on the Exchange. Trading of the securities on the Exchange will be subject to the Exchange's surveillance procedures for derivative products, including the securities. The Exchange may obtain information via the Intermarket Surveillance Group ("ISG") from other exchanges who are members or affiliates of the ISG¹⁶ or with which the Exchange has entered into a comprehensive surveillance sharing agreement. The Exchange has a general policy prohibiting the distribution of material, non-public information by its employees.

¹⁵ See, e.g., Rule 11.11(a). Regulation NMS Rule 612, Minimum Pricing Increment, provides:

a. No national securities exchange, national securities association, alternative trading system, vendor, or broker or dealer shall display, rank, or accept from any person a bid or offer, an order, or an indication of interest in any NMS stock priced in an increment smaller than \$0.01 if that bid or offer, order, or indication of interest is priced equal to or greater than \$1.00 per share.

b. No national securities exchange, national securities association, alternative trading system, vendor, or broker or dealer shall display, rank, or accept from any person a bid or offer, an order, or an indication of interest in any NMS stock priced in an increment smaller than \$0.0001 if that bid or offer, order, or indication of interest is priced less than \$1.00 per share.

c. The Commission, by order, may exempt from the provisions of this section, either unconditionally or on specified terms and conditions, any person, security, quotation, or order, or any class or classes of persons, securities, quotations, or orders, if the Commission determines that such exemption is necessary or appropriate in the public interest, and is consistent with the protection of investors.

¹⁶ For a list of the current members and affiliate members of ISG, see www.isgportal.com.

Trading Halts

With respect to trading halts, the Exchange may consider all relevant factors in exercising its discretion to halt or suspend trading in the securities. Trading in the securities may be halted because of market conditions or for reasons that, in the view of the Exchange, make trading in the securities inadvisable. These may include: (1) the extent to which trading in the underlying asset or assets is not occurring; or (2) whether other unusual conditions or circumstances detrimental to the maintenance of a fair and orderly market are present. In addition, trading in the securities will be subject to trading halts caused by extraordinary market volatility pursuant to Rule 11.18 or by the halt or suspension of the trading of the current underlying asset or assets.

If the applicable Intraday Indicative Value, value of the underlying index, or the value of the underlying asset or assets (e.g., securities, commodities, currencies, futures contracts, or other assets) is not being disseminated as required, the Exchange may halt trading during the day in which such interruption to the dissemination occurs. If the interruption to the dissemination of the applicable Intraday Indicative Value, value of the underlying index, or the value of the underlying asset or assets persists past the trading day in which it occurred, the Exchange will halt trading no later than the beginning of the trading day following the interruption. In addition, if the Exchange becomes aware that the NAV with respect to a series of the securities is not disseminated to all market participants at the same time, it will halt trading in such series until such time as the NAV is available to all market participants.

Suitability

Currently, Exchange Rule 3.7 governs Recommendations to Customers (Suitability). Prior to the commencement of trading of any inverse, leveraged, or inverse leveraged securities, the Exchange will inform its Members of the suitability requirements of the Exchange Rule 3.7

in an Information Circular. Specifically, Members will be reminded in the Information Circular that, in recommending transactions in these securities, they must have a reasonable basis to believe that (1) the recommendation is suitable for a customer given reasonable inquiry concerning the customer's investment objectives, financial situation, needs, and any other information known by such Member, and (2) the customer can evaluate the special characteristics, and is able to bear the financial risks, of an investment in the securities. In connection with the suitability obligation, the Information Circular will also provide that Members must make reasonable efforts to obtain the following information: (1) the customer's financial status; (2) the customer's tax status; (3) the customer's investment objectives; and (4) such other information used or considered to be reasonable by such Member or registered representative in making recommendations to the customer.

In addition, FINRA has implemented increased sales practice and customer margin requirements for FINRA members applicable to inverse, leveraged, and inverse leveraged securities and options on such securities, as described in FINRA Regulatory Notices 09-31 (June 2009), 09-53 (August 2009) and 09-65 (November 2009) ("FINRA Regulatory Notices"). Members that carry customer accounts will be required to follow the FINRA guidance set forth in the FINRA Regulatory Notices. The Information Circular will reference the FINRA Regulatory Notices regarding sales practice and customer margin requirements for FINRA members applicable to inverse, leveraged, and inverse leveraged securities and options on such securities.

The Exchange notes that, for such inverse, leveraged, and inverse leveraged securities, the corresponding funds seek leveraged, inverse, or leveraged inverse returns on a daily basis, and do not seek to achieve their stated investment objective over a period of time greater than

one day because compounding prevents the funds from perfectly achieving such results. Accordingly, results over periods of time greater than one day typically will not be a leveraged multiple (+200%), the inverse (-100%), or a leveraged inverse multiple (-200%) of the period return of the applicable benchmark and may differ significantly from these multiples. The Exchange's Information Circular, as well as the applicable registration statement, will provide information regarding the suitability of an investment in such securities.

2. Statutory Basis

The rule change proposed in this submission is consistent with the requirements of the Act and the rules and regulations thereunder that are applicable to a national securities exchange, and, in particular, with the requirements of Section 6(b) of the Act.¹⁷ Specifically, the proposed change is consistent with Section 6(b)(5) of the Act,¹⁸ because it is 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 facilitating transactions in securities, and to remove impediments to, and perfect the mechanism of, a free and open market and a national market system. The Exchange believes that the proposed rules will facilitate the listing and trading of additional types of exchange-traded products on the Exchange that will enhance competition among market participants, to the benefit of investors and the marketplace. In addition, the listing and trading criteria set forth in the proposed rules are intended to protect investors and the public interest.

The Exchange's listing requirements as proposed herein are at least as stringent as those of another national securities exchange and, consequently, the proposed rule change is consistent

¹⁷ 15 U.S.C. 78f(b).

¹⁸ 15 U.S.C. 78f(b)(5).

with the protection of investors and the public interest. Additionally, the proposal is designed to prevent fraudulent and manipulative acts and practices, as all of the proposed new products are subject to existing Exchange trading rules, together with surveillance procedures, suitability, and prospectus requirements, and requisite Exchange approvals, all set forth above.

The proposal is also designed to promote just and equitable principles of trade by way of initial and continued listing standards which, if not maintained, will result in the discontinuation of trading in the affected products. These requirements, together with the applicable Exchange equity trading rules (which apply to the proposed products), ensure that no investor would have an unfair advantage over another respecting the trading of the subject products. On the contrary, all investors will have the same access to, and use of, information concerning the specific products and trading in the specific products, all to the benefit of public customers and the marketplace as a whole.

Furthermore, the proposal is designed to remove impediments to and perfect the mechanism of a free and open market and a national market system by adopting listing standards that will lead ultimately to the trading of the proposed new products on the Exchange, just as they are currently traded on other exchanges. The Exchange believes that individuals and entities permitted to make markets on the Exchange in the proposed new products should enhance competition within the mechanism of a free and open market and a national market system, and customers and other investors in the national market system should benefit from more depth and liquidity in the market for the proposed new products.

B. Self-Regulatory Organization's Statement on Burden on Competition

The Exchange does not believe that the proposed rule change imposes any burden on competition.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

The Exchange has neither solicited nor received written comments on the proposed rule change.

III. Date of Effectiveness of the Proposed Rule Changes and Timing for Commission Action

Within 45 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding, or (ii) as to which the self-regulatory organization consents, the Commission will:

- A. by order approve or disapprove the proposed rule change; or
- B. institute proceedings to determine whether the proposed rule change should be disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to rule-comments@sec.gov. Please include File Number SR-BATS-2012-030 on the subject line.

Paper comments:

- Send paper comments in triplicate to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-BATS-2012-030. This file number should be

included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (<http://www.sec.gov/rules/sro.shtml>). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Section, 100 F Street, NE, Washington, DC 20549, on official business days between 10:00 a.m. and 3:00 p.m. Copies of the filing will also be available for inspection and copying at the Exchange's principal office. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that

you wish to make available publicly. All submissions should refer to File Number SR-BATS-2012-030 and should be submitted on or before [insert date 21 days from publication in the Federal Register].

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

Kevin M. O'Neill
Deputy Secretary

¹⁹ 17 CFR 200.30-3(a)(12).