

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-63342; File No. SR-BYX-2010-001)

November 18, 2010

Self-Regulatory Organizations; BATS Y-Exchange, Inc.; Notice of Filing of Amendment No. 1 and Order Granting Accelerated Approval to Proposed Rule Change, as Modified by Amendment No. 1, to Amend BYX Rule 11.8, Entitled “Obligations of Market Makers”

I. Introduction

On September 27, 2010, BATS Y-Exchange, Inc. (“BYX” or the “Exchange”), filed with the Securities and Exchange Commission (“Commission”), pursuant to Section 19(b)(1)<sup>1</sup> of the Securities Exchange Act of 1934 (“Act”), and Rule 19b-4 thereunder,<sup>2</sup> a proposed rule change to amend its rules to enhance minimum quoting standards for market makers registered with the Exchange. The purpose of this rule change is to require equity market makers to post continuous two-sided quotations within a designated percentage of the inside market to eliminate market maker “stub quotes,” that are so far away from the prevailing market that they are not intended to be executed (such as an order to buy at a penny or sell at \$100,000).

The proposed rule change was published for comment in the Federal Register on October 15, 2010.<sup>3</sup> In addition, BYX filed an Amendment No. 1 to the proposed rule change.<sup>4</sup> The Commission received no comments on the proposed rule change. The

---

<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. 63068 (October 8, 2010), 75 FR 63528 (SR-BYX-2010-001).

<sup>4</sup> The Exchange filed Amendment No. 1 on November 8, 2010. Amendment No. 1 modifies the proposal so that a market maker is not expected to enter a quote based on the prior day’s last sale at the commencement of regular trading hours if there is no National Best Bid (“NBB”) or National Best Offer (“NBO”). As

Commission is publishing this notice and order to solicit comments on Amendment No. 1 and to approve the proposed rule change, as amended, on an accelerated basis.

## II. Description of the Proposal

On May 6, 2010, the U.S. equity markets experienced a severe disruption.<sup>5</sup> Among other things, the prices of a large number of individual securities suddenly declined by significant amounts in a very short time period, before suddenly reversing to prices consistent with their pre-decline levels. This severe price volatility led to a large number of trades being executed at temporarily depressed prices, including many that were more than 60% away from pre-decline prices and subsequently broken.

As noted in the May 6 Staff Report, executions against stub quotes represented a significant proportion of broken trades on May 6. To address this aspect of the events of May 6, in coordination with the Commission, in addition to the Exchange, nine of the national securities exchanges and the Financial Industry Regulatory Authority, Inc. (“FINRA”) filed proposals to address stub quotes by introducing minimum quoting

---

amended, in such a circumstance, the quoting obligation would commence as soon as there has been a regular-way transaction on the primary listing market in the security, as reported by the responsible single plan processor. In addition, the Amendment modifies the proposal so that a market maker’s quoting obligation shall be suspended during a trading halt, suspension or pause, and shall not recommence until after the first regular-way transaction on the primary listing market following that halt, suspension or pause, as reported by the responsible single plan processor. Finally, so that the markets may coordinate implementation upon approval of the proposed rule changes, BYX stated in Amendment No. 1 that the planned implementation date for the proposed rule change would be December 6, 2010.

<sup>5</sup> The events of May 6 are described more fully in the report of the staffs of the Commodity Futures Trading Commission (“CFTC”) and the Commission, titled Report of the Staffs of the CFTC and SEC to the Joint Advisory Committee on Emerging Regulatory Issues, “Findings Regarding the Market Events of May 6, 2010,” dated September 30, 2010 (“May 6 Staff Report”).

standards for market makers.<sup>6</sup> Those proposals were approved by the Commission on November 5, 2010.<sup>7</sup>

The BYX proposal is substantively identical to the market maker quotation requirements that were previously approved by the Commission for the nine national securities exchanges and FINRA. The proposal requires market makers to maintain continuous two-sided quotations throughout the trading day<sup>8</sup> that are within a certain percentage band of the national best bid and offer (“NBBO”). These requirements apply to all NMS stocks<sup>9</sup> during normal market hours. For stocks subject to the individual

---

<sup>6</sup> See Securities Exchange Act Release Nos. 62945 (September 20, 2010), 75 FR 58460 (September 24, 2010) (SR-BATS-2010-025); 62954 (September 20, 2010), 75 FR 59305 (September 27, 2010) (SR-BX-2010-66); 62951 (September 20, 2010), 75 FR 59309 (September 27, 2010) (SR-CBOE-2010-087); 62949 (September 20, 2010), 75 FR 59315 (September 27, 2010) (SR-CHX-2010-22); 62953 (September 20, 2010), 75 FR 59300 (September 27, 2010) (SR-FINRA-2010-049); 62950 (September 20, 2010), 75 FR 59311 (September 27, 2010) (SR-NASDAQ-2010-115); 62952 (September 20, 2010), 75 FR 59316 (September 27, 2010) (SR-NSX-2010-12); 62948 (September 20, 2010), 75 FR 58455 (September 24, 2010) (SR-NYSE-2010-69); 62947 (September 20, 2010), 75 FR 58453 (September 24, 2010) (SR-NYSEAmex-2010-96); 62946 (September 20, 2010), 75 FR 58462 (September 24, 2010) (SR-NYSEArca-2010-83).

<sup>7</sup> See Securities Exchange Act Release No. 63255 (November 5, 2010), 75 FR 69484 (November 12, 2010) (SR-BATS-2010-025; SR-BX-2010-66; SR-CBOE-2010-087; SR-CHX-2010-22; SR-FINRA-2010-049; SR-NASDAQ-2010-115; SR-NSX-2010-12; SR-NYSE-2010-69; SR-NYSEAmex-2010-96; SR-NYSEArca-2010-83).

<sup>8</sup> As noted, Amendment No. 1 modifies the BYX proposal so that the quoting obligation would commence as soon as there has been a regular-way transaction on the primary listing market in the security, as reported by the responsible single plan processor. The Amendment also modifies that the market maker’s quoting obligations shall be suspended during a trading halt, suspension or pause, and shall not re-commence until the first-regular way print on the primary listing market following that halt, suspension or pause, as reported by the responsible single plan processor. See *supra* note 4. The BYX amendment is substantively identical to the amendments filed by the nine national securities exchanges and FINRA in connection with their filings.

<sup>9</sup> See 17 CFR 242.600 (defining NMS stock as “any NMS security other than an

stock circuit breaker pilot program (i.e., stocks that are included in the S&P 500, stocks that are included in the Russell 1000, and certain exchange-traded products),<sup>10</sup> market makers must enter quotes that are not more than 8% away from the NBBO. A quote that is entered at or within 8% away from the NBBO is allowed to drift a certain additional amount away from the NBBO before it must be adjusted by the market maker. However, if the NBBO moves to a point such that the quote is 9.5% away from the NBBO, that quote must be adjusted so that it is no further than 8% away from the NBBO. During times in which a single-stock circuit breaker is not applicable (i.e., before 9:45 a.m. and after 3:35 p.m.), market makers for such securities must maintain a quote no further than 20% away from the NBBO. Similar to the requirements when the single-stock circuit breakers are in effect, a market maker's quote may drift an additional 1.5% away from the NBBO without adjustment (i.e., until it is 21.5% away from the NBBO), at which point it would need to be adjusted to a quote no further than 20% away from the NBBO. In the absence of an NBBO, the same percentages apply, but the market maker must use the consolidated last sale instead of the NBBO.

For securities that are not subject to the single-stock circuit breakers, market makers must maintain quotes that are no more than 30% away from the NBBO. Like securities subject to the single-stock circuit breakers, if the NBBO moves to a point such

---

option” and NMS security as “any security or class of securities for which transaction reports are collected, processed, and made available pursuant to an effective transaction reporting plan, or an effective national market system plan for reporting transactions in listed options”).

<sup>10</sup> See Securities Exchange Act Release Nos. 62283 (September 10, 2010), 75 FR 56608 (September 16, 2010); 62884 (September 10, 2010), 75 FR 56618 (September 16, 2010).

that the quote is 31.5% away from the NBBO, the quote must be adjusted to a quote no further than 30% away from the NBBO.

Nothing in the BYX proposal precludes a market maker from voluntarily quoting at price levels that are closer to the NBBO than required under the proposal.

The planned implementation date for the proposed rule change is December 6, 2010.

BYX also proposed an optional functionality to automatically update market makers' quotes. Upon the request of a market maker, the BYX system would automatically enter and adjust quotes in accordance with the proposed quotation requirements. If a market maker cancelled the quotations entered by BYX through this functionality, the market maker would remain responsible for complying with the minimum quotation requirements imposed by the new rule.

### III. Commission Findings

The Commission finds that the proposed rule change implementing enhanced market maker quotation standards is consistent with the requirements of the Act and the rules and regulations thereunder applicable to national securities exchanges. In particular, the Commission finds that the proposal is consistent with Section 6(b)(5) of the Act,<sup>11</sup> which, among other things, requires that the rules of national securities exchanges 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

---

<sup>11</sup> 15 U.S.C. 78f(b)(5).

protect investors and the public interest.<sup>12</sup> The Commission also believes that the proposal is consistent with Section 11A(a)(1) of the Act<sup>13</sup> in that it seeks to assure fair competition among brokers and dealers and among exchange markets.

By requiring market makers to maintain quotes that are priced within a broad range around the NBBO, the proposed rule should help assure that quotations submitted by market makers to an exchange, and displayed to market participants, bear some relationship to the prevailing market price, and thus should promote fair and orderly markets and the protection of investors. In addition, by precluding market makers from submitting “stub” quotes that are so far away from the prevailing market price that they are not intended to be executed, the proposed rule should reduce the risk that trades will occur at irrational prices. As noted above, a large number of trades were executed at irrational prices on May 6, 2010 and were ultimately broken. In this respect, the proposal also should promote the goals of investor protection and fair and orderly markets. Finally, because BYX is proposing a rule that, in conjunction with the rules of the other national securities exchanges and FINRA, creates uniform rules with respect to these market maker quoting obligations, the proposed rule change as a whole will assure these baseline standards are applied throughout the equity markets.

The Commission also finds that the functionality proposed by the Exchange is consistent with Section 6(b)(5) of the Act,<sup>14</sup> which, among other things, requires that the rules of national securities exchanges be designed to prevent fraudulent and manipulative

---

<sup>12</sup> In approving the proposed rule change, the Commission notes that it has considered the proposed rule’s impact on efficiency, competition, and capital formation. 15 U.S.C. 78c(f).

<sup>13</sup> 15 U.S.C. 78k-1(a)(1).

<sup>14</sup> 15 U.S.C. 78f(b)(5).

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 functionality should assist market makers on BYX in maintaining continuous, two-sided limit orders within the prescribed limits in the securities in which they are registered to satisfy their new quoting obligations.

IV. Accelerated Approval

The Commission also finds good cause, pursuant to Section 19(b)(2) of the Act,<sup>15</sup> for approving the proposed Amendment No. 1 on an accelerated basis. The amendment reflects the concern that the proposed market maker quoting obligations should not apply during times when market makers should be permitted to absorb material information affecting a security for which they are registered as a market maker, whether before or during the trading day, i.e., until there has been a regular-way transaction on a security's primary listing market or during a trading halt. Approving the amendment on an accelerated basis would allow these provisions to be effective as of the implementation date of the new market maker requirements.

V. Solicitation of Comments

Interested persons are invited to submit written data, views and arguments concerning the foregoing, including whether Amendment No. 1 to the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

---

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

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](mailto:rule-comments@sec.gov). Please include File Number SR-BYX-2010-001 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-BYX-2010-001. 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 Room, 100 F Street, NE., Washington, DC 20549, on official business days between the hours of 10 a.m. and 3 p.m. Copies of such filings also will be available for inspection and copying at the principal office of the Exchange. 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-BYX-2010-001 and should be submitted on or before [insert 21 days from publication in the Federal Register].

VI. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,<sup>16</sup> that the proposed rule change (SR-BYX-2010-001), as modified by Amendment No. 1, be, and hereby is, approved on an accelerated basis.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>17</sup>

Florence E. Harmon  
Deputy Secretary

---

<sup>16</sup> 15 U.S.C. 78s(b)(2).

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