



## SECURITIES AND EXCHANGE COMMISSION

(Release No. 34-73203; File No. SR-BATS-2014-040)

September 24, 2014

Self-Regulatory Organizations; BATS Exchange, Inc.; Notice of Filing of a Proposed Rule Change to Rule 21.7 of BATS Exchange, Inc.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (the “Act”),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on September 12, 2014, BATS Exchange, Inc. (the “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 the Substance of the Proposed Rule Change

The Exchange filed a proposal to amend Rule 21.7, entitled “Market Opening Procedures” in order 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.

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.

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

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

<sup>2</sup> 17 CFR 240.19b-4.

proposed rule change. The text of these statements may be examined at the places specified 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

The purpose of the proposed rule changes is to amend BATS Rule 21.7 in order to amend the Opening Process<sup>3</sup> by executing orders in the Opening Process based on time priority instead of price-time priority, treating orders that are not executed during the Opening Process as if they had just been entered by a User<sup>4</sup> rather than cancelling certain orders, and adding certain clarifying language to the Rule in order to make the Opening Process more clear. The Exchange is also proposing to add titles to BATS Rule 21.7(a)(1), (2), (3), and (4) in order to make the rule text easier to follow. The Exchange is not proposing to amend the process by which orders are entered or the Opening Price<sup>5</sup> is determined or validated.

Currently, after establishing an Opening Price that is also a Valid Price,<sup>6</sup> orders and quotes in the System<sup>7</sup> 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. All orders and quotes or portions thereof that are matched pursuant to the Opening Process will be executed at the Opening Price. Where orders that meet the following criteria are not executed during the Opening Process, they will be cancelled: (i) limit orders that are priced equal to or more

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<sup>3</sup> Opening Process is defined in BATS Rule 21.7(a).

<sup>4</sup> User is defined in BATS Rule 16.1(a)(63).

<sup>5</sup> Opening Price is defined in BATS Rule 21.7(a)(1).

<sup>6</sup> Valid Price is defined in BATS Rule 21.7(a)(2).

<sup>7</sup> System is defined in BATS Rule 1.5(aa).

aggressively than the Opening Price; and (ii) market orders. Where the Exchange is going to open trading in a series pursuant to 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 will similarly 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. Limit orders and quotes that are not executed during the Opening Process or cancelled as set forth above shall become eligible for trading on BATS Options immediately following the completion of the Opening Process. Finally, where there are no orders in a series that are matched at the Opening Price, the System will open the series for trading.

The Exchange is proposing 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 Rule 21.9. The Exchange believes that handling orders in time priority makes more sense than price-time priority for the Opening Process because the price of the 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 Plan<sup>8</sup> after 9:30 a.m.; or the last regular way transaction from the previous trading day as disseminated pursuant to OPRA.<sup>9</sup> 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. Thus, the Exchange is proposing that all orders and quotes that are priced equal to or more aggressively than the Opening Price be matched based only on time priority and will be matched until there is no

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<sup>8</sup> OPRA Plan is defined in BATS Rule 27.1(15).

<sup>9</sup> OPRA is defined in BATS Rule 27.1(14).

remaining volume or there is an imbalance 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.

Further, the Exchange is also proposing to handle all orders that are not executed in the Opening Process in time priority. Specifically, the Exchange is proposing 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,<sup>10</sup> cancel the orders, execute the orders, or route the orders in accordance with Rule 21.9. If an order is placed on the BATS Options Book, it will then be subject to the standard price-time priority and subject to Rule 21.8. This proposed functionality will apply to all orders, including both those orders that are not executed under proposed Rule 21.7(a)(3) and orders in a series that is opening subject to a Contingent Open. While the Exchange currently cancels any orders that are not executed in the Opening Process that are priced more aggressively than the Opening Price, the Exchange is proposing to simply enter these orders on to the BATS Options Book as described above in order to minimize the number of orders that are cancelled and must be reentered by Users. The Exchange notes that all order protections, including Trade-Through<sup>11</sup> protection and a BATS Market Order<sup>12</sup> collar, will apply to orders entered pursuant to proposed Rule 21.7(a)(3) and 21.7(a)(4).

The Exchange is also proposing to eliminate the current functionality of cancelling 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. Further, the Exchange is proposing 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

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<sup>10</sup> BATS Options Book is defined in BATS Rule 16.1(a)(9).

<sup>11</sup> Trade-Through is defined in BATS Rule 27.1(22).

<sup>12</sup> BATS Market Order is defined in BATS Rule 21.1(d)(5).

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. While not cancelling these orders might result in executions at a price that is not the same as the Opening Price that occur 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. 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. As such, the Exchange is proposing this functionality in order to provide Users with the 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.

Finally, the Exchange is proposing to clarify its rules around the Opening Process. Specifically, the Exchange is proposing 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 Price<sup>13</sup> and that matches will occur until there is no remaining volume or there is an imbalance of orders, both of which it believes are implicit, but will make the rule text more clear. The Exchange is also proposing to add titles to Rules 21.7(a)(1) through (4) in order to make the rule text easier to follow. The Exchange is also proposing to delete Rule 21.7(a)(5), which states that where no orders are matched at the Opening Price, the System will open the series for trading because such situation will be covered by proposed Rule 21.7(a)(3), as described above.

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<sup>13</sup> Valid Price is defined in BATS Rule 21.7(a)(2).

## 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.<sup>14</sup> Specifically, the proposed change is consistent with Section 6(b)(5) of the Act,<sup>15</sup> because it is designed 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 Exchange believes that the Opening Process for options listed on the Exchange will help to ensure that BATS Options opens trading in options contracts in a fair and orderly manner. Specifically, the Exchange believes that handling orders in time priority will both create a more orderly opening and makes more sense than price-time priority for the Opening Process because the price of the order is not particularly important to the Opening Process, so long as the order is priced at or more aggressively than the Opening Price and, as such, there is no reason to reward a more aggressive order with priority in the Opening Process.

The Exchange also believes that entering orders in time sequence based on the time that they were received instead of cancelling certain orders will create a more orderly opening because Users will enter orders and quotes prior to the opening of trading that they know will either participate in the Opening Process or be handled as if they were entered immediately following the Opening Process and, more importantly, will not be cancelled, unless otherwise instructed by the User.

Modifying the Opening Process will also provide Market Makers and other Users with greater control and flexibility with respect to entering orders and quotes, allowing them to enter

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

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

orders and quotes in advance of the Opening Process that they know will not be cancelled because of market conditions out of the control of the User that entered the order. This simplifies the process for Market Makers and other Users by providing them certainty as to when orders and quotes can be submitted without having to resubmit orders in options series that have been cancelled, which removes impediments to a free and open market and benefits all Users of BATS Options.

As described above, the Exchange believes that the other proposed changes to its rulebook to clarify and add additional detail provides further clarification to Members, Users, and the investing public regarding the functionality of the Opening Process.

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

The Exchange does not believe that the proposed rule change will impose any burden on competition not necessary or appropriate in furtherance of the purposes of the act. To the contrary, the Exchange's current Opening Process in which certain orders and quotes may be cancelled based on market conditions beyond the entering User's control limits competition in that other exchanges are able to accept orders and quotes before trading in options opens that will not be cancelled. Thus, approval of the proposed rule change will promote competition because it will allow the Exchange to offer its Users the ability to enter orders and quotes prior to the opening of trading that will not be cancelled and thus compete with other exchanges for order flow that a User may not have directed to the Exchange if they were not able to enter orders and quotes prior to the open that were not eligible to be cancelled.

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

The Exchange has not solicited, and does not intend to solicit, comments on this proposed rule change. The Exchange has not received any written comments from members or other

interested parties.

### III. Date of Effectiveness of the Proposed Rule Change 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 Exchange consents, the Commission will: (a) by order approve or disapprove such 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](mailto:rule-comments@sec.gov). Please include File Number SR-BATS-2014-040 on the subject line.

#### Paper comments:

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

All submissions should refer to File Number SR-BATS-2014-040. 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 10:00 a.m. and 3:00 p.m. Copies of such filing 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-BATS-2014-040, 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.<sup>16</sup>

Kevin M. O'Neill,  
Deputy Secretary.

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<sup>16</sup> 17 CFR 200.30-3(a)(12).