



SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-78396; File No. SR-BATS-2015-100)

Self-Regulatory Organizations; BATS Exchange, Inc.; Order Approving a Proposed Rule Change, as Modified by Amendment No. 6, to Amend BATS Rule 14.11(i) to Adopt Generic Listing Standards for Managed Fund Shares

July 22, 2016

I. Introduction

On November 18, 2015, BATS Exchange, Inc. (now known as Bats BZX Exchange, Inc., “Exchange” or “BZX”)¹ filed with the Securities and Exchange Commission (“Commission”), pursuant to section 19(b)(1) of the Securities Exchange Act of 1934 (“Act” or “Exchange Act”)² and Rule 19b-4 thereunder,³ a proposed rule change to amend Rule 14.11(i) by, among other things, adopting generic listing standards for Managed Fund Shares. The proposed rule change was published for comment in the **Federal Register** on November 25, 2015.⁴

On January 4, 2016, the Commission designated a longer period within which to approve the proposed rule change, disapprove the proposed rule change, or institute proceedings to determine whether to disapprove the proposed rule change.⁵ On February 9, 2016, the Exchange filed Amendment No. 1 to the proposed rule change, which replaced the originally filed proposed

¹ In March 2016, BATS changed its name from “BATS Exchange, Inc.” to “Bats BZX Exchange, Inc.” See Securities Exchange Act Release No. 77307 (Mar. 7, 2016), 81 FR 12996 (Mar. 11, 2016) (SR-BATS-2016-25) (publishing notice of the name change to Bats BZX Exchange, Inc.).

² 15 U.S.C. 78s(b)(1).

³ 17 CFR 240.19b-4.

⁴ See Securities Exchange Act Release No. 76478 (Nov. 19, 2015), 80 FR 73841.

⁵ See Securities Exchange Act Release No. 76820, 81 FR 989 (Jan. 8, 2016). The Commission designated February 23, 2016 as the date by which the Commission shall either approve or disapprove, or institute proceedings to determine whether to disapprove, the proposed rule change. See *id.*

rule change in its entirety. On February 11, 2016, the Exchange both filed and withdrew Amendment No. 2 to the proposed rule change. On February 11, 2016, the Exchange also filed Amendment No. 3 to the proposed rule change.⁶ On February 17, 2016, the Exchange filed Amendment No. 4 to the proposed rule change.⁷

On February 22, 2016, the Commission issued notice of filing of Amendments No. 1, 3, and 4 to the proposed rule change and instituted proceedings under section 19(b)(2)(B) of the Act⁸ to determine whether to approve or disapprove the proposed rule change, as modified by Amendments No. 1, 3, and 4.⁹ In the Order Instituting Proceedings, the Commission solicited

⁶ Amendment No. 3 deletes from the proposal the following two statements: (1) “Such limitation will not apply to listed swaps because swaps are listed on swap execution facilities (“SEFs”), the majority of which are not members of ISG[;]” and (2) “Such limitation would not apply to listed swaps because swaps are listed on SEFs, the majority of which are not members of ISG.” Amendment No. 3 also corrects an erroneous statement in Item 11 to indicate that an Exhibit 4 was included in Amendment No. 1. Amendment No. 3 is available at: <http://www.sec.gov/comments/sr-bats-2015-100/bats2015100-3.pdf>.

⁷ Amendment No. 4 deletes from the proposal the following sentence: “Thus, if the limitation applied to swaps, there would effectively be a cap of 10% of the portfolio invested in listed swaps.” Amendment No. 4 also amends two representations as follows (added language in brackets): The Exchange or FINRA, on behalf of the Exchange, will communicate as needed regarding trading in Managed Fund Shares [and their underlying components] with other markets that are members of the ISG, including all U.S. securities exchanges and futures exchanges on which the components are traded[, or with which the Exchange has in place a CSSA.] In addition, the Exchange or FINRA[,] on behalf of the Exchange[,] may obtain information regarding trading in Managed Fund Shares [and their underlying components] from other markets that are members of the ISG, including all U.S. securities exchanges and futures exchanges on which the components are traded, or with which the Exchange has in place a CSSA.” Amendment No. 4 is available at: <http://www.sec.gov/comments/sr-bats-2015-100/bats2015100-4.pdf>.

⁸ 15 U.S.C. 78s(b)(2)(B).

⁹ See Securities Exchange Act Release No. 77202, 81 FR 9889 (Feb. 26, 2016) (“Order Instituting Proceedings”). Specifically, the Commission instituted proceedings to allow for additional analysis of the proposed rule change’s consistency with section 6(b)(5) of the Act, which requires, among other things, that the rules of a national securities exchange be “designed to prevent fraudulent and manipulative acts and practices, to

comments to specified matters related to the proposal.¹⁰ On May 20, 2016, the Commission designated a longer period for Commission action on the proposed rule change.¹¹

On June 3, 2016, the Exchange filed Amendment No. 5 to the proposed rule change, which replaced Amendment No. 1 (as further modified by Amendments No. 3 & 4) to the proposed rule change.¹² The Commission issued a notice of the filing of Amendment No. 5 on June 7, 2016 and solicited comments on the modified proposal.¹³ On July 21, 2016, the Exchange filed Amendment No. 6 to the proposed rule change,¹⁴ which amended and replaced the Amendment No. 5 to the proposed rule change.

promote just and equitable principles of trade,” and “to protect investors and the public interest.” See id., 81 FR at 9897.

¹⁰ See id.

¹¹ See Securities Exchange Act Release No. 77871, 81 FR 33567 (May 26, 2016) (designating July 22, 2016 as the date by which the Commission must either approve or disapprove the proposed rule change).

¹² See Securities Exchange Act Release No. 78005, 81 FR 38247, 38248 (June 13, 2016) (“Notice”). Amendment No. 5 is available at: <http://www.sec.gov/comments/sr-bats-2015-100/bats2015100-5.pdf>.

¹³ See Notice, supra note 12.

¹⁴ In Amendment No. 6, the Exchange added the following representations: (1) on a periodic basis, and no less than annually, the Exchange will review the Managed Fund Shares generically listed and traded on the Exchange under BATS Rule 14.11(i) for compliance with that rule and will provide a report to its Regulatory Oversight Committee presenting the findings of its review; and (2) on a quarterly basis, the Exchange will provide a report to the Commission staff that contains, for each ETF whose shares are generically listed and traded under BATS Rule 14.11(i): (a) symbol and date of listing; (b) the number of active authorized participants (“APs”) and a description of any failure by either a fund or an AP to deliver promised baskets of shares, cash, or cash and instruments in connection with creation or redemption orders; and (c) a description of any failure by an ETF to comply with BATS Rule 14.11(i). The Exchange also modified proposed BATS Rule 14.11(i)(4)(C) to read: “The Exchange may approve Managed Fund Shares for listing pursuant to Rule 19b-4(e) under the Act. Components of a series of Managed Fund Shares listed pursuant to Rule 19b-4(e) shall satisfy the criteria set forth within this Rule 14.11(i) upon initial listing and on a continual basis. The Exchange will file separate proposals under Section 19(b) of the Act before the listing

The Commission has not received any comments on the proposed rule change, as modified by Amendment No. 5. This order approves the proposed rule change, as modified by Amendment No. 6.

II. Description of the Proposal, as Modified by Amendment No. 6

BATS Rule 14.11(i) governs the listing and trading of Managed Fund Shares on the Exchange. Managed Fund Shares are issued by exchange-traded funds (“ETFs”) that are actively managed and do not seek to replicate the performance of a specified index of securities.

Under its current rules, the Exchange must file separate proposals under section 19(b) of the Act before listing a new series of Managed Fund Shares.¹⁵ The Exchange proposes to adopt generic listing standards so that the Exchange may list Managed Fund Shares that satisfy the applicable criteria by submitting notice pursuant to Rule 19b-4(e) under the Act, rather than by filing a proposed rule change under section 19(b).¹⁶

and trading of a series of Managed Fund Shares with components that do not satisfy the criteria set forth within this Rule 14.11(i) or components other than those specified below.” In the Commission’s view, the changes to proposed rule text of Rule 14.11(i)(4)(C) are not substantive. Amendment No. 6 is available at: <https://www.sec.gov/comments/sr-bats-2015-100/bats2015100-6.pdf>. Because Amendment No. 6 does not materially alter the substance of the proposed rule change or raise unique or novel regulatory issues, Amendment No. 6 is not subject to notice and comment.

¹⁵ See BATS Rule 14.11(i)(2)(A).

¹⁶ 17 CFR 240.19b-4(e). Rule 19b-4(e) permits self-regulatory organizations to list and trade new derivatives products that comply with existing SRO trading rules, procedures, surveillance programs and listing standards, without submitting a proposed rule change under Section 19(b). See Securities Exchange Act Release No. 40761 (Dec. 8, 1998), 63 FR 70952 (Dec. 22, 1998).

A. The Proposed Generic Listing Standards

The Exchange's proposed listing standards establish requirements for the various types of assets that may be held in the portfolio of a generically listed, actively managed ETF ("Portfolio").

1. Equity Portfolio Components

Proposed BATS Rule 14.11(i)(4)(C)(i) establishes the criteria applicable to the equity securities included in a Portfolio. Equity securities include the following securities: U.S. Component Stocks, which are defined in BATS Rule 14.11(c)(1)(D); Non-U.S. Component Stocks, which are defined in BATS Rule 14.11(c)(1)(E); Derivative Securities Products, which are defined in BATS Rule 14.11(c)(3)(A)(i)(a); Linked Securities, which are securities eligible for listing on the Exchange under BATS Rule 14.11(d), and each of the equivalent security types listed on another national securities exchange. Additionally, proposed Rule 14.11(i)(4)(C)(i) provides that no more than 25% of the equity weight of the Portfolio can include leveraged or inverse-leveraged Derivative Securities Products or Linked Securities and that, to the extent a Portfolio includes convertible securities, the equity securities into which such securities are converted must meet the criteria of this Rule 14.11(i)(4)(C)(i) after converting.

Proposed BATS Rule 14.11(i)(4)(C)(i)(a) would require that U.S. Component Stocks (except as mentioned below) meet the following criteria initially and on a continuing basis:

- (1) component stocks (excluding Derivative Securities Products and Linked Securities) that in the aggregate account for at least 90% of the equity weight of the Portfolio (excluding Derivative Securities Products and Linked Securities) each shall have a minimum market value of at least \$75 million;

- (2) component stocks (excluding Derivative Securities Products and Linked Securities) that in the aggregate account for at least 70% of the equity weight of the Portfolio (excluding Derivative Securities Products and Linked Securities) each shall have a minimum monthly trading volume of 250,000 shares, or minimum notional volume traded per month of \$25,000,000, averaged over the previous six months;
- (3) the most heavily weighted component stock (excluding Derivative Securities Products and Linked Securities) must not exceed 30% of the equity weight of the Portfolio, and, to the extent applicable, the five most heavily weighted component stocks (excluding Derivative Securities Products and Linked Securities) must not exceed 65% of the equity weight of the Portfolio;
- (4) where the equity portion of the Portfolio does not include Non-U.S. Component Stocks, the equity portion of the Portfolio shall include a minimum of 13 component stocks; provided, however, that there would be no minimum number of component stocks if (a) one or more series of Derivative Securities Products or Linked Securities constitute, at least in part, components underlying a series of Managed Fund Shares, or (b) one or more series of Derivative Securities Products or Linked Securities account for 100% of the equity weight of the Portfolio of a series of Managed Fund Shares;
- (5) except as provided in proposed BATS Rule 14.11(i)(4)(C)(i)(a), equity securities in the Portfolio must be U.S. Component Stocks listed on a national securities exchange and must be NMS Stocks as defined in Rule 600 of Regulation NMS; and

- (6) American Depositary Receipts (“ADRs”) may be exchange traded or non-exchange traded, but no more than 10% of the equity weight of the Portfolio shall consist of non-exchange traded ADRs.

Proposed BATS Rule 14.11(i)(4)(C)(i)(b) requires that Non-U.S. Component Stocks must meet the following criteria initially and on a continuing basis:

- (1) Non-U.S. Component Stocks each shall have a minimum market value of at least \$100 million;
- (2) Non-U.S. Component Stocks each shall have a minimum global monthly trading volume of 250,000 shares, or minimum global notional volume traded per month of \$25,000,000, averaged over the last six months;
- (3) the most heavily weighted Non-U.S. Component Stock shall not exceed 25% of the equity weight of the Portfolio, and, to the extent applicable, the five most heavily weighted Non-U.S. Component Stocks shall not exceed 60% of the equity weight of the Portfolio;
- (4) where the equity portion of the Portfolio includes Non-U.S. Component Stocks, the equity portion of the Portfolio shall include a minimum of 20 component stocks; provided, however, that there shall be no minimum number of component stocks if (a) one or more series of Derivative Securities Products or Linked Securities constitute, at least in part, components underlying a series of Managed Fund Shares, or (b) one or more series of Derivative Securities Products or Linked Securities account for 100% of the equity weight of the Portfolio of a series of Managed Fund Shares; and

- (5) each Non-U.S. Component Stock shall be listed and traded on an exchange that has last-sale reporting.

2. Fixed Income Portfolio Components

Proposed BATS Rule 14.11(i)(4)(C)(ii) establishes criteria for fixed income securities that are included in a Portfolio. Fixed income securities are debt securities¹⁷ that are notes, bonds, debentures, or evidence of indebtedness that include, but are not limited to, U.S. Department of Treasury securities (“Treasury Securities”), government-sponsored entity securities (“GSE Securities”), municipal securities, trust preferred securities, supranational debt and debt of a foreign country or a subdivision thereof, investment grade and high yield corporate debt, bank loans, mortgage and asset backed securities, and commercial paper.¹⁸ To the extent that a Portfolio includes convertible securities, the fixed income securities into which such securities are converted shall meet the criteria of proposed BATS Rule 14.11(i)(4)(C)(ii) after converting.¹⁹ Under proposed BATS Rule 14.11(i)(4)(C)(ii), fixed income securities that are part of a Portfolio must satisfy the following criteria initially and on a continuing basis:

- (1) components that in the aggregate account for at least 75% of the fixed income weight of the Portfolio must each have a minimum original principal amount outstanding of \$100 million or more;

¹⁷ Debt securities include a variety of fixed income obligations, including, but not limited to, corporate debt securities, government securities, municipal securities, convertible securities, and mortgage-backed securities. Debt securities include investment-grade securities, non-investment-grade securities, and unrated securities. Debt securities also include variable and floating rate securities. See Amendment No. 6, supra note 14, at 52, n.27.

¹⁸ See proposed BATS Rule 14.11(i)(4)(C)(ii).

¹⁹ See id.

- (2) no component fixed-income security (excluding Treasury Securities and GSE Securities) shall represent more than 30% of the fixed income weight of the Portfolio, and the five most heavily weighted fixed income securities in the Portfolio (excluding Treasury Securities and GSE Securities) shall not in the aggregate account for more than 65% of the fixed income weight of the Portfolio;
- (3) a Portfolio that includes fixed income securities (excluding exempted securities) shall include a minimum of 13 non-affiliated issuers, provided, however, that there shall be no minimum number of non-affiliated issuers required for fixed income securities if at least 70% of the weight of the Portfolio consists of equity securities as described in BATS Rule 14.11(i)(4)(C)(i);
- (4) Component securities that in aggregate account for at least 90% of the fixed income weight of the Portfolio must be: (a) from issuers that are required to file reports pursuant to sections 13 and 15(d) of the Act; (b) from issuers each of which has a worldwide market value of its outstanding common equity held by non-affiliates of \$700 million or more; (c) from issuers each of which has outstanding securities that are notes, bonds, debentures, or evidence of indebtedness having a total remaining principal amount of at least \$1 billion; (d) exempted securities as defined in section 3(a)(12) of the Act; or (e) from issuers that are a government of a foreign country or a political subdivision of a foreign country; and
- (5) non-agency, non-GSE, and privately issued mortgage-related and other asset-backed securities shall not account, in the aggregate, for more than 20% of the weight of the fixed income portion of the Portfolio.

3. Cash and Cash Equivalents in Portfolios

Proposed BATS Rule 14.11(i)(4)(C)(iii) provides that a Portfolio may include cash and cash equivalents. Cash equivalents are defined as short-term instruments with maturities of less than 3 months.²⁰ The Exchange defines short-term instruments to include the following: (1) U.S. Government securities, including bills, notes and bonds differing as to maturity and rates of interest, which are either issued or guaranteed by the U.S. Treasury or by U.S. Government agencies or instrumentalities; (2) certificates of deposit issued against funds deposited in a bank or savings and loan association; (3) bankers' acceptances, which are short-term credit instruments used to finance commercial transactions; (4) repurchase agreements and reverse repurchase agreements; (5) bank time deposits, which are monies kept on deposit with banks or savings and loan associations for a stated period of time at a fixed rate of interest; (6) commercial paper, which are short-term unsecured promissory notes; and (7) money market funds.²¹ BATS does not propose to limit to the amount of cash or cash equivalents that may be held in a Portfolio.²²

4. Derivative Portfolio Components

Proposed BATS Rule 14.11(i)(4)(C)(iv) establishes listing criteria for the portion of a Portfolio that consists of listed derivatives such as futures, options, and swaps overlying commodities, currencies, financial instruments (e.g., stocks, fixed income securities, interest rates, and volatility), or a basket or index of any of the foregoing. The Exchange does not propose to limit the percentage of a Portfolio that may be composed of such holdings, provided

²⁰ See proposed BATS Rule 14.11(i)(4)(C)(iii).

²¹ See proposed BATS Rule 14.11(i)(4)(C)(iii)(b).

²² See proposed BATS Rule 14.11(i)(4)(C)(iii)(a).

that, in the aggregate, at least 90% of the weight of holdings in listed derivatives (calculated using the aggregate gross notional value) must, on both an initial and continuing basis, consist of futures, options, and swaps for which the Exchange may obtain information via the ISG from other members or affiliates or for which the principal market is a market with which the Exchange has a comprehensive surveillance sharing agreement (“CSSA”).²³ Additionally, the aggregate gross notional value of listed derivatives based on any five or fewer underlying reference assets shall not exceed 65% of the weight of the Portfolio (including gross notional exposures), and the aggregate gross notional value of listed derivatives based on any single underlying reference asset shall not exceed 30% of the weight of the Portfolio (including gross notional exposures).²⁴

Proposed BATS Rule 14.11(i)(4)(C)(v) establishes a limit on OTC derivatives: no more than 20% of the weight of the Portfolio may be invested in OTC derivatives.²⁵ The Exchange notes that, for purposes of calculation this limitation, a portfolio’s investment in OTC derivatives will be calculated as the aggregate gross notional value of the OTC derivatives.

Proposed BATS Rule 14.11(i)(4)(C)(vi) provides that, to the extent that listed or OTC derivatives are used to gain exposure to individual equities and/or fixed income securities, or to indexes of equities and/or fixed income securities, the aggregate gross notional value of such exposure shall meet the criteria set forth in proposed BATS Rules 14.11(i)(4)(C)(i) and 14.11(i)(4)(C)(ii), respectively.

²³ See proposed BATS Rule 14.11(i)(4)(C)(iv)(a).

²⁴ See proposed BATS Rule 14.11(i)(4)(C)(iv)(b).

²⁵ OTC derivatives include: forwards, options, and swaps overlying commodities, currencies, financial instruments (e.g., stocks, fixed income securities, interest rates, and volatility), or a basket or index of any of the foregoing. See proposed BATS Rule 14.11(i)(4)(C)(v).

B. Other Aspects of the Proposal

1. Disclosed Portfolio

The daily dissemination of a Disclosed Portfolio²⁶ is required under current BATS Rule 14.11(i)(4)(B)(ii)(a), but its contents are not specified. The Exchange proposes to amend the definition of “Disclosed Portfolio” to require that the website for each series of Managed Fund Shares listed on the Exchange, including all Managed Fund Shares currently listed and traded on the Exchange, disclose the following information in the Disclosed Portfolio, to the extent applicable: ticker symbol, CUSIP or other identifier, a description of the holding, identity of the asset upon which the derivative is based, the strike price for any options, the quantity of each security or other asset held as measured by select metrics, maturity date, coupon rate, effective date, market value, and percentage weight of the holding in the portfolio.

2. Investment Objective

The Exchange proposes to add as an initial listing criterion applicable to all Managed Fund Shares (including those that are generically listed) the requirement that Managed Fund Shares must have a stated investment objective, which shall be adhered to under “Normal Market Conditions.”²⁷ The Exchange would define “Normal Market Conditions” as circumstances including, but not limited to the absence of: trading halts in the applicable financial markets generally; operational issues causing dissemination of inaccurate market information or systems

²⁶ BATS defines “Disclosed Portfolio” for purposes of its Managed Fund Shares listing rule as the identities and quantities of the securities and other assets held by the Investment Company that will form the basis for the Investment Company’s calculation of net asset value at the end of the business day. See BATS Rule 14.11(i)(3)(B).

²⁷ See proposed BATS Rule 14.11(i)(4)(A)(iii).

failure; or force majeure type events such as natural or man-made disaster, act of God, armed conflict, act of terrorism, riot or labor disruption, or any similar intervening circumstance.²⁸

3. Intraday Indicative Value (“IIV”)

The Exchange proposes to modify a continued listing criterion for all Managed Fund Shares to require that the IIV be widely disseminated by one or more major market data vendors at least every 15 seconds during Regular Trading Hours, as defined in BATS Rule 1.5(w),²⁹ rather than during all times that Managed Fund Shares trade on the Exchange.

C. Additional Representations of the Exchange Applicable to the Listing and Trading of Managed Fund Shares

In support of the proposed rule change, the Exchange represents that:

(1) Generically listed Managed Fund Shares will conform to the initial and continued listing criteria under Rule 14.11(i)(4)(A) and (B).³⁰

(2) The Exchange’s surveillance procedures are adequate to continue to properly monitor the trading of the Managed Fund Shares in all trading sessions and to deter and detect violations of Exchange rules. Specifically, the Exchange intends to utilize its existing surveillance procedures applicable to derivative products, which will include Managed Fund Shares, to monitor trading in the Managed Fund Shares.³¹

(3) Prior to the commencement of trading of a particular series of Managed Fund Shares, the Exchange will inform its Members in an information circular of the special characteristics and risks associated with trading the Managed Fund Shares, including procedures

²⁸ See proposed BATS Rule 14.11(i)(3)(E).

²⁹ See proposed BATS Rule 14.11(i)(4)(B)(i).

³⁰ See Amendment No. 6, supra note 14, at 24.

³¹ See id. at 24-25.

for purchases and redemptions of Managed Fund Shares, suitability requirements under Rule 3.7, the risks involved in trading the Managed Fund Shares during the Pre-Opening and After Hours Trading Sessions when an updated IIV will not be calculated or publicly disseminated, how information regarding the IIV and Disclosed Portfolio is disseminated, prospectus delivery requirements, and other trading information. In addition, the information circular will disclose that the Managed Fund Shares are subject to various fees and expenses, as described in the registration statement, and will discuss any exemptive, no-action, and interpretive relief granted by the Commission from any rules under the Act. Finally, the Bulletin will disclose that the NAV for the Managed Fund Shares will be calculated after 4 p.m. ET each trading day.³²

(4) The issuer of a series of Managed Fund Shares will be required to comply with Rule 10A-3 under the Act for the initial and continued listing of Managed Fund Shares, as provided under Rule 14.10(c)(3).³³

(5) BATS has represented that: (1) on a periodic basis, and no less than annually, the Exchange will review the Managed Fund Shares generically listed and traded on the Exchange under BATS Rule 14.11(i) for compliance with that rule and will provide a report to its Regulatory Oversight Committee presenting the findings of its review; and (2) on a quarterly basis, the Exchange will provide a report to the Commission staff that contains, for each ETF whose shares are generically listed and traded under BATS Rule 14.11(i): (a) symbol and date of listing; (b) the number of active authorized participants (“APs”) and a description of any failure by either a fund or an AP to deliver promised baskets of shares, cash, or cash and instruments in

³² See id. at 25.

³³ See id.

connection with creation or redemption orders; and (c) a description of any failure by an ETF to comply with BATS Rule 14.11(i).³⁴

(6) Prior to listing pursuant to proposed amended Rule 14.11(i), an issuer would be required to represent to the Exchange that it will advise the Exchange of any failure by a series of Managed Fund Shares to comply with the continued listing requirements, and, pursuant to its obligations under section 19(g)(1) of the Exchange Act, the Exchange will surveil for compliance with the continued listing requirements. If a series of Managed Fund Shares is not in compliance with the applicable listing requirements, the Exchange will commence delisting procedures under Exchange Rule 14.12.³⁵

III. Discussion and Commission Findings

After careful review, the Commission finds that the Exchange's proposal to amend its Rule 14.11(i) to, among other things, adopt generic listing criteria, is consistent with the Act and the rules and regulations thereunder applicable to a national securities exchange.³⁶ In particular, the Commission finds that the proposed rule change, as modified by Amendment No. 6, is consistent with section 6(b)(5) of the Act,³⁷ which requires, among other things, that the Exchange's rules 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.

³⁴ See id. at 25-26.

³⁵ See id. at 27-28.

³⁶ In approving this proposed rule change, the Commission has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

³⁷ 15 U.S.C. 78f(b)(5).

In support of its proposal, the Exchange states that its proposed requirements for Managed Fund Shares are based in large part on the generic listing criteria currently applicable to Index Fund Shares.³⁸ As a general matter, the Commission believes that this is an appropriate approach with respect to underlying asset classes covered by the existing generic standards, because the mere addition of active management to an ETF portfolio that would qualify for generic listing as an index-based ETF should not affect the portfolio's susceptibility to manipulation or the availability of arbitrage between the ETF and its underlying portfolio. Below, the Commission addresses the proposed criteria for each of the asset classes encompassed within the generic listing standards.

Equity Holdings. With respect to the equity holdings of a Portfolio, the proposed criteria closely track the existing standards for Index Fund Shares, with four relevant differences. First, while the generic listing criteria for Index Fund Shares do not permit the inclusion of any non-exchange-traded ADRs in the underlying index,³⁹ the proposed generic criteria for Managed Fund Shares would permit an ETF to hold up to 10% of the equity weight of the Portfolio in non-exchange-traded ADRs. This proposed provision, however, is consistent with standards that the Commission has approved for specific ETFs listed and traded as Managed Fund Shares.⁴⁰ Moreover, the Commission believes that the proposed requirement that at least 90% of the equity portion of a Portfolio consist of domestic equity securities (a category that includes ADRs) for

³⁸ See Amendment No. 6, supra note 14, at 63.

³⁹ The Commission notes, however, that a portfolio underlying Index Fund Shares nevertheless may contain non-exchange-listed ADRs because the portfolio need not consist only of index components.

⁴⁰ See, e.g., Securities Exchange Act Release No. 72679 (July 28, 2014), 79 FR 44878 (Aug. 1, 2014) (SR-NYSEArca-2014-71); Securities Exchange Act Release No. 67277 (June 27, 2012), 77 FR 39554 (July 3, 2012) (SR-NYSEArca-2012-39).

which the Exchange may obtain transaction data should both deter manipulation of generically listed Managed Fund Shares and permit the Exchange to investigate any instances of manipulation.

Second, the proposed standards would differ slightly from the existing generic standards for Index Fund Shares with respect to Non-U.S. Component Stocks. The proposed standards would provide that all Non-U.S. Component Stocks in a Portfolio must have a minimum market value of at least \$100 million. By contrast, the generic listing criterion for Index Fund Shares requires only 90% of the Non-U.S. Component Stocks (excluding Derivative Securities Products) included in an index to meet the same minimum market-value threshold.⁴¹ Additionally, under the proposal, all Non-U.S. Component Stocks included in a Portfolio must have a minimum global monthly trading volume of 250,000 shares, or minimum global notional volume traded per month of \$25,000,000, averaged over the previous six months.⁴² By contrast, only 70% of the weight of an index (excluding Derivative Securities Products) underlying generically listed Index Fund Shares must satisfy the same monthly volume thresholds.⁴³ The Commission believes that the proposed provisions should reduce the extent to which Managed Fund Shares holding Non-U.S. Component Stocks may be susceptible to manipulation.

Third, while the Exchange's existing generic listing standards for index-based ETFs do not apply concentration limits to an index's exposure to specified exchange-traded products (called "Derivative Securities Products"), which have concentration limits or price transparency

⁴¹ See BATS Rule 14.11(c)(A)(3)(ii)(a).

⁴² The Commission approved a listing rule that contained these heightened market capitalization and trading volume requirements. See Securities Exchange Act Release No. 75023 (May 21, 2015), 80 FR 30519 (May 28, 2015) (SR-NYSEArca-2014-100).

⁴³ See BATS Rule 14.11(c)(A)(3)(ii)(b).

requirements within their own listing standards, proposed BATS Rule 14.11(i)(4)(C)(ii) would also deem Portfolio concentration limits not to apply to holdings of specified exchange-traded notes (called “Linked Securities”). The Commission believes that this change should not increase the susceptibility of Managed Fund Shares to manipulation because Linked Securities, like Derivative Securities Products, have asset-exposure concentration limits and requirements promoting price transparency within their own listing standards, and both Derivative Securities Products and Linked Securities are listed and traded on national securities exchanges (which are all members of ISG), publicly provide information about listed Derivative Securities Products and Linked Securities, and provide trading and price information and other quantitative data for investors and other market participants..

And fourth, under current generic listing standards, index-based ETFs cannot seek inverse returns greater than 300% of the performance of their reference index, and there is no limit on positive leverage versus an index. By contrast, the proposed standards would impose an absolute cap – 25% – on the amount of an ETF’s portfolio that could be invested in leveraged or inverse-leveraged ETPs. The Commission believes that a limitation on the overall use of leveraged ETFs is consistent with section 6(b)(5) of the Act because it will limit the extent to which the performance of a generically listed, actively managed ETF can be tied to a product whose performance over periods of longer than one day can differ significantly from its stated daily performance objective.⁴⁴

Fixed Income Holdings. With respect to the fixed income components of a Portfolio, the standards proposed by the Exchange are based in large part on the standards in BATS Rule

⁴⁴ Cf. SEC Investor Alert, Leveraged and Inverse ETFs: Specialized Products with Extra Risks for Buy-and-Hold Investors, available at <https://www.sec.gov/investor/pubs/leveragedetfs-alert.htm>.

14.11(c)(4) for the components of fixed income indexes underlying Index Fund Shares, with three relevant differences. First, proposed BATS Rule 14.11(i)(4)(C)(ii)(c) does not require a minimum number of non-affiliated issuers for fixed income securities in the portfolio if at least 70% of the weight of the portfolio consists of equity securities as set forth in BATS Rule 14.11(i)(4)(C)(i). Second, proposed BATS Rule 14.11(i)(4)(C)(ii)(e) would prohibit non-agency, non-GSE, and privately issued mortgage-related and other asset-backed securities components of a Portfolio from constituting, in the aggregate, more than 20% of the weight of the fixed income portion of the Portfolio.⁴⁵ And third, The proposed standards would make explicit that convertible bonds would both (a) have to meet the criteria for fixed-income holdings and (b) be convertible into equities that would meet the criteria for equity holdings.

The Commission believes that, taken together, the proposed requirements for the fixed income portion of a Portfolio are reasonably designed to ensure that a substantial portion of a Portfolio consists of fixed income securities for which information is publicly available and, when applied in conjunction with the other applicable listing requirements, will permit the listing and trading only of Managed Fund Shares that are sufficiently broad-based to minimize the potential for manipulation. The Commission also believes that these provisions should help ensure that the fixed income portion of a Portfolio consists of assets for which available intra-day values allow market participants to identify and capitalize upon arbitrage opportunities, which in

⁴⁵ The Commission notes that it has approved listing and trading rules for specific ETFs listed as Managed Fund Shares that limit holdings of non-agency asset-backed securities to 20% of the value of the fund's portfolio. See, e.g., Securities Exchange Act Release No. 74297 (Feb. 18, 2015), 80 FR 9788 (Feb. 24, 2015) (SR-BATS-2014-056); Securities Exchange Act Release No. 75566 (July 30, 2015), 80 FR 46612 (Aug. 5, 2015) (SR-NYSEArca-2015-42).

turn should help keep the intra-day prices of generically listed Managed Fund Shares reasonably aligned with the intra-day values of their underlying assets.

Cash and Cash Equivalents. With respect to cash and cash equivalents to be held in a Portfolio, the Commission believes that the proposed standards appropriately define the type of short-term instruments that would qualify as such holdings.

Derivatives Holdings. With respect to derivatives of any type included in a Portfolio, proposed BATS Rule 14.11(i)(4)(C)(vi) provides that, to the extent they are used to gain exposure to individual equities or fixed income securities, or to indexes of equities or fixed income securities, the total notional exposure to the underlying instruments – whether achieved through cash instruments or derivative instruments – must meet the numerical and other criteria set forth in proposed BATS Rule 14.11(i)(4)(C)(i) and 14.11(i)(4)(C)(ii), as applicable. The Commission believes that this provision should make Portfolios less susceptible to manipulation by preventing circumvention of the quantitative and other requirements applicable to equity and fixed income security components of a Portfolio.

With respect to listed derivatives, the proposal would allow a generically listed ETF to use listed derivatives to achieve 100% of its Portfolio exposure, provided that, in the aggregate, at least 90% of the weight of holdings in futures, exchange-traded options, and listed swaps consists of futures, options, and swaps for which: (1) the Exchange may obtain information from other ISG members or affiliate members; or (2) the principal market is a market with which the Exchange has a CSSA.⁴⁶ Additionally, BATS represents that it (or FINRA on its behalf) will

⁴⁶ See Amendment No. 6, supra note 14, at 66. The Exchange also states that: (1) a fund's investments in derivatives, including listed derivatives, would be subject to limits on leverage imposed by the Investment Company Act of 1940, 15 U.S.C. 80a-1 ("1940 Act"); (2) to limit the potential risk associated with a fund's use of derivatives, a fund

communicate regarding, and obtain trade information as needed for, the underlying exchange-listed instruments whose principal market is either an ISG member or a market with which BATS has a CSSA.⁴⁷ The Commission believes that these provisions should both deter potential manipulation and permit BATS to investigate suspected manipulation of generically listed Managed Fund Shares that use listed derivatives. Additionally, the Commission believes that the price transparency of listed derivatives should enable market participants to identify and execute arbitrage strategies that will tend to equalize the market price of generically listed Managed Fund Shares with the value of the underlying Portfolios. The Commission also notes that proposed BATS Rule 14.11(i)(4)(C)(iv)(b) imposes concentration limits on the use of listed derivatives. The Commission believes that this limitation should make Portfolios that contain listed derivatives less susceptible to manipulation.

With respect to OTC derivatives, proposed BATS Rule 14.11(i)(4)(C)(v) would permit a Portfolio to include OTC derivatives, but would limit the amount of such derivatives to 20% of the fund's assets, thereby ensuring that the preponderance of a fund's investments would not be in derivatives that are not listed and centrally cleared. The Commission believes that this limit is sufficient to mitigate the risks associated with price manipulation because at least 80% of a Portfolio would consist of: cash and cash equivalents; listed derivatives, of which 90% by portfolio weight would be traded on a principal market that is a member of ISG; and equity

will segregate or “ earmark ” assets determined to be liquid by a fund in accordance with the 1940 Act (or, as permitted by applicable regulation, enter into certain offsetting positions) to cover its obligations under derivative instruments; (3) a fund's investments will not be used to seek performance that is the multiple or inverse multiple (i.e., 2Xs or 3Xs) of a fund's broad-based securities market index (as defined in Form N-1A). See id. at 70.

⁴⁷ See id. at 72.

securities or fixed income instruments subject to numerous restrictions designed to prevent manipulation and ensure pricing transparency.

The Commission notes that, in addition to proposing the listing criteria described above for specific asset classes, the Exchange has committed to conduct an ongoing compliance review of the ETFs that are generically listed as Managed Fund Shares. Specifically, the Exchange has represented that, no less than annually, it will review the Managed Fund Shares generically listed and traded on the Exchange under BATS Rule 14.11(i) for compliance with that rule and will provide a report to its Regulatory Oversight Committee presenting the findings of its review. The Exchange has also committed to provide, on a quarterly basis, a report to the Commission staff that contains, for each ETF whose shares are generically listed and traded under BATS Rule 14.11(i): (a) the symbol and date of listing; (b) the number of active APs and a description of any failure by either a fund or an AP to deliver promised baskets of shares, cash, or cash and instruments in connection with creation or redemption orders; and (c) a description of any failure by an ETF to comply with BATS Rule 14.11(i).⁴⁸ The Commission believes that the quarterly report provided by the Exchange will assist the Commission in using public data to review the trading characteristics of ETFs listed under these generic standards.⁴⁹

The Commission also notes that, prior to listing pursuant to BATS Rule 14.11(i), an issuer would be required to represent to the Exchange that it will advise the Exchange of any failure by a series of Managed Fund Shares to comply with the continued listing requirements,

⁴⁸ See id. at 25-26.

⁴⁹ The Commission also notes that all Managed Fund Shares listed pursuant to BATS Rule 14.11(i), including generically listed Managed Fund Shares, are included within the definition of “security” or “securities” as those terms are used in the BATS Rules. See BATS Rule 14.11(i)(2). Accordingly, Managed Fund Shares are subject to the full set of rules and procedures that govern the trading of securities on the Exchange. See Amendment No. 6, supra note 14, at 42.

and, pursuant to its obligations under section 19(g)(1) of the Act, the Exchange will surveil for compliance with the continued listing requirements. If a series of Managed Fund Shares is not in compliance with the applicable listing requirements, the Exchange will commence delisting procedures under Exchange Rule 14.12.⁵⁰

The Commission believes that the proposed generic listing criteria, taken together, should promote the listing only of Managed Fund Shares that are not susceptible to manipulation. Additionally, the proposed generic listing standards as a whole should ensure that Portfolios are composed predominantly of instruments for which available intra-day values allow market participants to identify and capitalize upon arbitrage opportunities, which in turn should help keep the intra-day prices of generically listed Managed Fund Shares reasonably aligned with the intra-day values of their underlying assets.

For the reasons discussed above, the Commission finds that the proposed generic listing standards for Managed Fund Shares are consistent with section 6(b)(5) of the Act.⁵¹

In addition, BATS proposes changes to Rule 14.11(i) that apply to all Managed Fund Shares (i.e., both funds listed generically under the proposed standards and funds listed pursuant to individual 19b-4 filings by the Exchange). Specifically, the Exchange proposes to specify the information that must be included in the Disclosed Portfolio disseminated by each actively managed ETF. Previously approved listing rules for specific ETFs listed as Managed Fund Shares have included identical disclosure requirements.⁵² The mandatory disclosures include information that market participants can use to value an actively managed ETF's holdings intra-

⁵⁰ See Amendment No. 6, supra note 14, at 27-28.

⁵¹ 15 U.S.C. 78f(b)(5).

⁵² See, e.g., Securities Exchange Act Release No. 72666 (July 3, 2014), 79 FR 44224 (July 30, 2014) (SR-NYSEArca-2013-122).

day, which should facilitate arbitrage opportunities that should help keep the intra-day prices of Managed Fund Shares reasonably aligned with the intra-day values of their underlying assets.

The Exchange also proposes to amend the continued listing requirement in BATS Rule 14.11(i)(4)(B)(i), which is applicable to all Managed Fund Shares, to require dissemination of an IIV at least every 15 seconds during Regular Trading Hours, as defined in BATS Rule 1.5(w).

The Exchange states that this requirement would be consistent with the IIV dissemination requirement for Index Fund Shares as well as representations made in support of approved proposals to list and trade shares of specific ETFs listed and traded as Managed Fund Shares.⁵³

The Commission also notes that the IIV dissemination during Regular Trading Hours is also required for all Managed Trust Securities.⁵⁴

Finally, the Exchange proposes to add as an initial listing criterion applicable to all Managed Fund Shares (including those that are generically listed) the requirement that Managed Fund Shares must have a stated investment objective, which shall be adhered to under “Normal Market Conditions,” defined as circumstances including, but not limited to, the absence of: trading halts in the applicable financial markets generally; operational issues causing dissemination of inaccurate market information or systems failure; or force majeure type events such as natural or man-made disaster, act of God, armed conflict, act of terrorism, riot or labor disruption, or any similar intervening circumstance.⁵⁵ The Commission believes that this proposed change is consistent with previous Commission approvals of specific ETFs listed as Managed Fund Shares.

⁵³ See Amendment No. 6, supra note 14, at 29.

⁵⁴ See BATS Rule 14.11(e)(10)(E)(ii)(a).

⁵⁵ See proposed BATS Rule 14.11(i)(3)(E).

For the foregoing reasons, the Commission finds that the proposed rule change, as modified by Amendment No. 6, is consistent with section 6(b)(5) of the Act⁵⁶ and the rules and regulations thereunder applicable to a national securities exchange.

IV. Conclusion

IT IS THEREFORE ORDERED, pursuant to section 19(b)(2) of the Act,⁵⁷ that the proposed rule change (SR-BATS-2015-100), as modified by Amendment No. 6 thereto, be, and it hereby is, approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.⁵⁸

Brent J. Fields,
Secretary.

⁵⁶ 15 U.S.C. 78f(b)(5).

⁵⁷ 15 U.S.C. 78s(b)(2).

⁵⁸ 17 CFR 200.30-3(a)(12).

