

Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of the filing also will be available for inspection and copying at the principal office of BYX. 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-2013-022 and should be submitted on or before July 26, 2013.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>14</sup>

**Kevin M. O'Neill,**

*Deputy Secretary.*

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## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-69889; File No. SR-BATS-2013-035]

### Self-Regulatory Organizations; BATS Exchange, Inc.; Notice of Filing of a Proposed Rule Change, as Modified by Amendment No. 1 Thereto, To Amend the Competitive Liquidity Provider Program

June 28, 2013.

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 June 17, 2013, 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. On June 24, 2013, the Exchange submitted Amendment No. 1 to the proposed rule change.<sup>3</sup> The Commission is publishing this notice to solicit comments on the proposed rule change, as modified by Amendment No. 1 thereto, from interested persons.

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

The Exchange filed a proposal to add an Interpretation and Policy .03 to Rule 11.8 entitled "Competitive Liquidity Provider Program for Exchange Traded Products" to incentivize competitive and aggressive quoting by market makers registered with the Exchange ("Market Makers")<sup>4</sup> in Exchange-listed ETPs.<sup>5</sup> The Exchange is also proposing to make a corresponding amendment to Interpretation and Policy .02 to Rule 11.8, entitled "Competitive Liquidity Provider Program" in order to reflect the proposal to remove ETPs listed on the Exchange from the existing Competitive Liquidity Provider Program.

As proposed, the Competitive Liquidity Provider Program for Exchange Traded Products (the "Program") set forth in Interpretation and Policy .03 to Rule 11.8 will be effective for a one year pilot period beginning from the date of implementation of the program. During the pilot, the Exchange will periodically provide information to the Commission about market quality with respect to the Program.

The text of the proposed rule change is available at the Exchange's Web site 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 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.

<sup>4</sup> As defined in BATS Rules, the term "Market Maker" means a Member that acts as a market maker pursuant to Chapter XI of BATS Rules.

<sup>5</sup> As proposed in Interpretation and Policy .03 (b)(4) to Rule 11.8, the term "ETP" includes Portfolio Depository Receipts, Index Fund Shares, Trust Issued Receipts, and Managed Fund Shares, which are defined in Rule 14.11(b), 14.11(c), 14.11(f), and 14.11(i), respectively, which the Exchange may propose to expand in the future as it adds products which may be listed on the Exchange. Any such expansion would require the Exchange to file a proposal with the Commission under Rule 19b-4 of the Act.

### (A) Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

#### 1. Purpose

#### Background

On August 30, 2011, the Exchange received approval of rules applicable to the qualification, listing and delisting of securities of issuers on the Exchange.<sup>6</sup> More recently, the Exchange received approval to operate a program that is designed to incentivize certain Market Makers registered with the Exchange as Competitive Liquidity Providers to enhance liquidity on the Exchange in all Exchange-listed securities (the "CLP Program").<sup>7</sup> The Exchange subsequently adopted financial incentives for the CLP Program<sup>8</sup> and thereafter amended certain components of the CLP Program, including financial incentives and quoting requirements for Competitive Liquidity Providers in the CLP Program.<sup>9</sup>

The purpose of this filing is to propose new Interpretation and Policy .03 to Rule 11.8, which is based substantially on the CLP Program, that seeks to incentivize certain market makers registered with the Exchange as Competitive Liquidity Providers ("CLPs") to enhance liquidity on the Exchange in certain ETPs listed on the Exchange and thereby qualify to receive part of a daily rebate pursuant to the Program (a "CLP Rebate"). The Exchange is also proposing to make several related amendments to existing Interpretation and Policy .02 to Rule 11.8 in order to remove ETPs from the CLP Program so that it applies only to corporate issues.

Proposed Interpretation and Policy .03 to Rule 11.8 will be effective for a one year pilot period. The pilot period will commence when the Program is implemented by the Exchange and a CLP Company,<sup>10</sup> on behalf of a CLP

<sup>6</sup> See Securities Exchange Act Release No. 65225 (August 30, 2011), 76 FR 55148 (September 6, 2011) (SR-BATS-2011-018).

<sup>7</sup> See Securities Exchange Act Release No. 66307 (February 2, 2012), 77 FR 6608 (February 8, 2012) (SR-BATS-2011-051).

<sup>8</sup> See Securities Exchange Act Release No. 66427 (February 21, 2012), 77 FR 11608 (February 27, 2012) (SR-BATS-2012-011).

<sup>9</sup> See Securities Exchange Act Release Nos. 67854 (September 13, 2012), 77 FR 58198 (September 19, 2012) (SR-BATS-2012-036) and 69190 (March 20, 2013), 78 FR 18384 (March 26, 2013) (SR-BATS-2013-005).

<sup>10</sup> As defined in proposed Interpretation and Policy .03(b)(2) to Rule 11.8, the term "CLP Company" means the trust or company housing the ETP or, if the ETP is not a series of a trust or company, then the ETP itself.

<sup>14</sup> 17 CFR 200.30-3(a)(12).

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

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

<sup>3</sup> In Amendment No. 1, the Exchange made technical corrections and amended the proposed rule text to clarify that any CLP Security listed on the Exchange shall be eligible for the CLP Program for the first six months that it is listed on the Exchange, regardless of the ETP's CADV (as such terms are defined below).

Security,<sup>11</sup> and one or more related market makers are accepted into the Program in respect of a security listed pursuant to the Program. The pilot program will, unless extended, end one year after implementation. During the pilot, the Exchange will submit monthly reports to the Commission about market quality with respect to the Program. The monthly reports will endeavor to compare, to the extent practicable, securities before and after they are in the Program, including those securities that “graduate” from the Program, and will include information regarding the Program which will enable the Exchange and the Commission to better analyze the effectiveness of the Program, such as: (1) Rule 605 metrics;<sup>12</sup> (2) volume metrics; (3) number of CLPs in target securities; (4) spread size; and (5) availability of shares at the NBBO. The Exchange will endeavor to provide similar data to the Commission about comparable ETPs that are listed on the Exchange that are not in the Program; and any other Program related data requested by the Commission for the purpose of evaluating the efficacy of the Program. The Exchange will post the monthly reports on its Web site. The first report will be submitted within sixty days after the Program becomes operative.

#### Competitive Liquidity Provider Program for Exchange Traded Products

The Exchange is proposing to adopt a new rule titled “Competitive Liquidity Provider Program for Exchange Traded Products” as Interpretation and Policy .03 to Rule 11.8. The Program is designed to promote market quality in CLP Securities<sup>13</sup> by allowing a CLP Company to list an eligible CLP Security on the Exchange and, in addition to paying the standard (non-CLP) listing fee as set forth in the fee schedule, a Sponsor<sup>14</sup> may pay a fee (a “CLP Fee”) in order for the CLP Company, on behalf of a CLP Security, to participate in the Program, which will be credited to the BATS General Fund. The Exchange will then pay the CLP Rebate out of the BATS General Fund in order to incentivize CLPs in the CLP Security to

quote aggressively in the CLP Security by providing a CLP Rebate to one or more CLPs that make a quality market in the CLP Security pursuant to the Program.<sup>15</sup>

The Exchange believes that the Program will be beneficial to the financial markets, to market participants including traders and investors, and to the economy in general. First, the Program will encourage narrow spreads and liquid markets in securities that generally have not been, or may not be, conducive to naturally having such narrow spreads and liquidity. These securities may include less actively traded or less well known ETPs that are made up of securities of less well known or start-up companies as components.<sup>16</sup> Second, in rewarding market makers that are willing to help to develop liquid markets for CLP Securities subject to the Program,<sup>17</sup> the Program would benefit traders and investors by encouraging more quote competition, narrower spreads, and greater liquidity. Third, the Program will lower transaction costs and enhance liquidity in both ETPs and their components, making those securities more attractive to a broader range of investors. In so doing, the Program will help companies access capital to invest and grow.

#### Securities Eligible for the Program

The Exchange is proposing that any CLP Company, on behalf of a CLP Security, shall be eligible for the Program, as long as: (i) The Exchange has accepted the Program application of

<sup>15</sup> The enhanced market quality (e.g. liquidity) would, as discussed below, be identical to the existing CLP Quoting Requirements in Interpretation and Policy .02(g) to Rule 11.8. These standards include, for example, posting at least five round lots in a CLP Security at the NBB or NBO at the time of a SET in order to have a Winning Bid SET or Winning Offer SET, respectively, as well as requiring that a CLP is quoting at least a round lot at a price at or within 1.2% of the CLP's bid (offer) at the time of the SET in order to have a Winning Bid (Offer) Set. The two CLPs that have the most Winning Bid SETs and the two Eligible CLPs with the most Winning Offer SETs in a given CLP Security will split the CLP Credit on a pro-rata basis. Proposed Interpretation and Policy .03(i) to Rule 11.8.

<sup>16</sup> These small companies and their securities (whether components of listed products like ETPs or direct listings) have been widely recognized as essential to job growth and creation and, by extension, the health of the economy. Being included in a successful ETP can provide the stocks of these companies with enhanced liquidity and exposure, enabling them to attract investors and access capital markets to fund investment and growth.

<sup>17</sup> By imposing quality quoting requirements to enhance the quality of the market for CLP Securities, the Program will directly impact one of the ways that market makers manage risk in lower tier or less liquid securities (e.g. the width of bid and offer pricing).

the CLP Company with respect to the CLP Security and the Exchange has accepted the Program application of at least one CLP in the CLP Security; (ii) the CLP Security meets all requirements to be listed on the Exchange as an ETP; (iii) the CLP Security meets all Exchange requirements for continued listing at all times the CLP Security participates in the Program; (iv) while the CLP Security is participating in the Program, on a product-specific Web site, the CLP Company is indicating that the product is in the Program and provides a link to the Exchange's Program Web site; and (v) the security has a consolidated average daily volume (“CADV”) of less than 1 million shares for at least one of the past three calendar months, however, any CLP Security listed on the Exchange shall be eligible for the Program for the first six months that it is listed on the Exchange, regardless of the ETP's CADV.<sup>18</sup>

#### Application

The Exchange is proposing that any entity that wishes to participate in the Program must submit an application in the form prescribed by the Exchange, which includes both CLP Companies on behalf of a CLP Security and CLPs.<sup>19</sup>

#### CLPs

To become a CLP, a Member must submit a CLP application form with all supporting documentation to the Exchange. As is currently the case for membership applications to join the Exchange and applications to register as market makers on the Exchange, Exchange personnel in the Exchange's membership department will process such applications. Exchange personnel will determine whether an applicant is qualified to become a CLP based on the qualifications described below. After an applicant submits a CLP application to the Exchange, with supporting documentation, the Exchange shall notify the applicant Member of its decision. If an applicant is approved by the Exchange to receive CLP status, such applicant must establish connectivity with relevant Exchange systems before such applicant will be permitted to trade as a CLP on the Exchange. In the event an applicant is disapproved by the Exchange, such applicant may seek review under Chapter X of the Exchange's Rules governing adverse action and/or reapply for CLP status at least three (3) calendar months following the month in which the

<sup>18</sup> Proposed Interpretation and Policy .03(d)(1) and (d)(3) to Rule 11.8.

<sup>19</sup> Proposed Interpretation and Policy .03(c)(1) to Rule 11.8.

<sup>11</sup> As defined in proposed Interpretation and Policy .03(b)(3) to Rule 11.8, the term “CLP Security” means an issue of or series of ETP securities issued by a CLP Company that meets all of the requirements to be listed on the Exchange pursuant to Rule 14.11.

<sup>12</sup> 17 CFR 242.605.

<sup>13</sup> The Exchange notes that CLP Securities do not encompass derivatives on such securities.

<sup>14</sup> As defined in proposed Interpretation and Policy .03(b)(5) to Rule 11.8, Sponsor means the registered investment adviser that provides investment management services to a CLP Company or any of such adviser's parents or subsidiaries.

applicant received the disapproval notice from the Exchange. Chapter X of the Exchange's Rules provides any persons who are or are about to be aggrieved by an adverse action taken by the Exchange with a process to apply for an opportunity to be heard and to have the complained of action reviewed.<sup>20</sup>

To qualify as a CLP, a Member will be required to be a registered Market Maker in good standing with the Exchange consistent with Rules 11.5 through 11.8. Further, the Exchange will require each Member seeking to qualify as a CLP to have and maintain: (1) Adequate technology to support electronic trading through the systems and facilities of the Exchange; (2) one or more unique identifiers that identify to the Exchange CLP trading activity in assigned CLP Securities;<sup>21</sup> (3) adequate trading infrastructure to support CLP trading activity, which includes support staff to maintain operational efficiencies in the Program and adequate administrative staff to manage the Member's participation in the Program; (4) quoting and volume performance that demonstrates an ability to meet the CLP quoting requirement in each assigned CLP Security on a daily and monthly basis; (5) a disciplinary history that is consistent with just and equitable business practices; and (6) the business unit of the Member acting as a CLP must have in place adequate information barriers between the CLP unit and the Member's customer, research and investment banking business.<sup>22</sup> These requirements are identical to those of the existing CLP Program.<sup>23</sup>

#### Withdrawal and Renewal

The Exchange is proposing that any entity that wishes to withdraw from the Program must provide written notice to the Exchange, however, the requirements for CLPs and CLP Companies on behalf of CLP Securities are different, as further explained below.

#### CLPs

A CLP may withdraw from the status of a CLP by providing written notice to

<sup>20</sup> Proposed Interpretation and Policy .03(g) to Rule 11.8.

<sup>21</sup> As proposed, a Member may not use such unique identifiers for trading activity at the Exchange in assigned CLP securities that is not CLP trading activity, but may use the same unique identifiers for trading activity in securities not assigned to a CLP. If a Member does not identify to the Exchange the unique identifier to be used for CLP trading activity, the Member will not receive credit for such CLP trading.

<sup>22</sup> Proposed Interpretation and Policy .03(f) to Rule 11.8.

<sup>23</sup> See Interpretation and Policy .02(c) and (e) to Rule 11.8.

the Exchange. Such withdrawal shall become effective when those CLP Securities assigned to the withdrawing CLP are reassigned to another CLP. After the Exchange receives the notice of withdrawal from the withdrawing CLP, the Exchange will reassign such CLP Securities as soon as practicable but no later than thirty (30) days after the date said notice is received by the Exchange. In the event the reassignment of CLP Securities takes longer than the 30-day period, the withdrawing CLP will have no obligations under this Interpretation and Policy .03 and will not be held responsible for any matters concerning its previously assigned CLP Securities upon termination of this 30-day period.<sup>24</sup>

#### CLP Securities

A CLP Company may, on behalf of a CLP Security, after being in the Program for not less than two consecutive quarters, but less than one year, voluntarily withdraw from the Program on a quarterly basis. The CLP Company must notify the Exchange in writing, not less than one month prior to withdrawing from the Program. The Exchange, however, does retain discretion to allow a CLP Company to withdraw from the Program earlier than required above. In making such decision, the Exchange may take into account the volume and price movements in the CLP Security; the liquidity, size quoted, and quality of the market in the CLP Security; and any other relevant factors. After a CLP Security is in the Program for one year or more, the CLP Company may voluntarily withdraw from the Program on a monthly basis, so long as the CLP Company notifies the Exchange in writing not less than one month prior to withdrawing from the Program.<sup>25</sup>

After a CLP Company, on behalf of a CLP Security, is in the Program for one year, the Program and all obligations and requirements of the Program will automatically continue on an annual basis unless: (1) The Exchange terminates the Program by providing not less than one month prior notice of intent to terminate or the pilot Program is not extended or made permanent pursuant to a proposed rule change subject to filing with or approval by the Commission; (2) the CLP Company withdraws from the Program pursuant to the withdrawal rules described above; or (3) the CLP Company is terminated

<sup>24</sup> Proposed Interpretation and Policy .03(h) to Rule 11.8.

<sup>25</sup> Proposed Interpretation and Policy .03(c)(2) to Rule 11.8.

from the Program pursuant to subsection (n) of the proposal.<sup>26</sup>

#### CLP Company Fees

A CLP Company seeking to participate in the Program shall incur an annual basic CLP Fee of \$30,000 per CLP Security. The basic CLP Fee must be paid to the Exchange prospectively on a quarterly basis.<sup>27</sup>

A CLP Company may also incur an annual supplemental CLP Fee per CLP Security. The basic CLP Fee and supplemental CLP Fee, when combined, may not exceed \$100,000 per year. The supplemental CLP Fee is a fee selected by a CLP Company on an annual basis, if at all. The supplemental CLP Fee must be paid to the Exchange prospectively on a quarterly basis. The amount of the supplemental CLP Fee, if any, will be determined by the CLP Company initially per CLP Security and will remain the same for the period of a year. The Exchange will provide notification on its Web site regarding the amount, if any, of any supplemental CLP Fee determined by a CLP Company per CLP Security.<sup>28</sup>

The CLP Fee is in addition to the standard (non-CLP) Exchange listing fee applicable to the CLP Security and does not offset such standard listing fee.<sup>29</sup> For a CLP Security housed by a CLP Company that has a Sponsor or Sponsors, the CLP Fee with respect to the CLP Security shall be paid by the Sponsor or Sponsors of such CLP Security. The Exchange will prospectively bill each CLP Company for the quarterly CLP Fee for each CLP Security.<sup>30</sup> CLP Fees (both basic and

<sup>26</sup> Interpretation and Policy .03(n) to Rule 11.8 states that the Program will terminate with respect to a CLP Security under the following circumstances: (A) A CLP Security sustains a CADV of one million shares or more for three consecutive months, however, any CLP Security listed on the Exchange shall be eligible for the Program for the first six months that it is listed on the Exchange, regardless of the ETP's CADV; (B) A CLP Company, on behalf of a CLP Security, withdraws from the Program, is no longer eligible to be in the Program pursuant to this rule, or its Sponsor ceases to make CLP Fee payments to the Exchange; (C) A CLP Security is delisted or is no longer eligible for the Program; or (D) A CLP Security does not, for two consecutive quarters, have at least one CLP that is eligible for CLP Rebate. It should be noted, however, that termination of a CLP Company, CLP Security, or CLP does not preclude the Exchange from allowing re-entry into the Program where the Exchange deems such re-entry as proper.

<sup>27</sup> Proposed Interpretation and Policy .03(d)(2)(A) to Rule 11.8.

<sup>28</sup> Proposed Interpretation and Policy .03(d)(2)(B) to Rule 11.8.

<sup>29</sup> Proposed Interpretation and Policy .03(d)(2)(C) to Rule 11.8. The CLP Fee with respect to an ETP shall be paid by the Sponsor(s) of such ETP.

<sup>30</sup> Proposed Interpretation and Policy .03(d)(2)(D) to Rule 11.8.

supplemental) will be credited to the BATS General Fund.

#### CLP Quoting Requirements

CLPs are subject to both a daily quoting requirement in order to be eligible to receive financial incentives and a monthly quoting requirement in order to remain qualified as a CLP. These quoting requirements are identical to the quoting requirements of the Exchange's existing CLP Program.<sup>31</sup> Any CLP that meets the daily quoting requirement set forth below will be eligible to receive a portion of the CLP Rebate for each day's quoting activity. A CLP that does not meet the CLP monthly quoting requirement is subject to the non-regulatory penalties described below.

The Exchange will continue to measure the performance of a CLP in CLP Securities by calculating Size Event Tests ("SETs") between 9:25 a.m. and 4:05 p.m. on every day on which the Exchange is open for business. The Exchange will measure each CLP's quoted size, excluding odd lots, at the NBB and NBO at least once per second to determine SETs. The CLP with the greatest aggregate size at the NBB at each SET (a "Bid SET") will be considered to have a winning Bid SET (a "Winning Bid SET"). Separately, the CLP with the greatest aggregate size at the NBO at each SET (an "Offer SET") will be considered to have a winning Offer SET (a "Winning Offer SET").<sup>32</sup>

In order to meet the daily quoting requirement, a CLP must have Winning Bid SETs or Winning Offer SETs equal to at least 10% of the total Bid SETs or total Offer SETs, respectively, on any trading day in order to be eligible for any CLP Rebate (each such CLP, an "Eligible CLP") for a CLP Security, as is also required under the existing CLP Program.<sup>33</sup> Eligible CLPs will be ranked according to the number of Winning Bid SETs and Winning Offer SETs each trading day, and only the Eligible CLP or Eligible CLPs ranked number one and the Eligible CLP or Eligible CLPs ranked number two in each of the Winning Bid SETs and Winning Offer SETs will receive the CLP Rebate.<sup>34</sup>

In order to meet the monthly quoting requirements, a CLP must be quoting at

the NBB or the NBO 10% of the time that the Exchange calculates SETs.<sup>35</sup>

As is also required under the Exchange's existing CLP Program, a CLP must be quoting, at a minimum, five round lots (usually 500 shares), excluding odd lots, of the CLP Security, at the NBB or NBO, respectively, at the time of a SET in order to have a Winning Bid SET or a Winning Offer SET. Such quoting requirements will be measured by utilizing the unique identifiers that the Member has identified for CLP trading activity.<sup>36</sup> In addition, during Regular Trading Hours<sup>37</sup> a CLP must also be quoting at least a displayed round lot offer, excluding odd lots, at a price at or within 1.2% of the CLP's bid at the time of the SET in order to have a Winning Bid SET.<sup>38</sup> Similarly, during Regular Trading Hours, a CLP must be quoting at least a displayed round lot offer, excluding odd lots, at a price at or within 1.2% of the CLP's offer at the time of the SET in order to have a Winning Offer Set.<sup>39</sup>

For purposes of calculating whether a CLP is in compliance with its CLP quoting requirements, the CLP must post displayed liquidity in round lots in its assigned CLP Securities at the NBB or the NBO.<sup>40</sup> A CLP may post non-displayed liquidity; however, such liquidity will not be counted as credit towards the CLP quoting requirements. The CLP shall not be subject to any minimum or maximum quoting size requirement in assigned CLP Securities apart from the requirement that an order be for at least one round lot. The CLP quoting requirements will be measured by utilizing the unique identifiers that the Member has identified for CLP trading activity. CLPs may only enter orders electronically directly into Exchange systems and facilities designated for this purpose. All CLP orders must only be for the proprietary account of the CLP Member.

#### CLP Rebate

As described above, pursuant to the Program, the Exchange will measure the performance of CLPs in CLP Securities by calculating SETs between 9:25 a.m. and 4:05 p.m. on every day on which the Exchange is open for business. Each

day, one quarter of the total annual CLP Fees (basic and supplemental combined) for the CLP Security divided by the number of trading days in the current quarter will constitute the total CLP Rebate for the CLP Security. For instance, where the total CLP Fees for a CLP Security is \$64,000 and there are 64 trading days in the current quarter, the total CLP Rebate for the CLP Security would be \$250 [(\$64,000/4)/64].<sup>41</sup>

Accordingly, the two Eligible CLPs with the most Winning Bid SETs will split half of the daily CLP Rebate for the CLP Security on a pro rata basis and the two Eligible CLPs with the most Winning Offer SETs will split half of the daily CLP Rebate for the CLP Security on a pro rata basis.<sup>42</sup> Specifically, the Exchange is proposing to determine the portion of the CLP Rebate that a CLP receives based on the number of each CLP's Winning Bid (Offer) SETs as a percentage of total Winning Bid (Offer) SETs between the two CLPs with the most Winning Bid (Offer) SETs. For instance, where CLP1 has 6,000 Winning Bid (Offer) SETs, CLP2 has 4,000 Winning Bid (Offer) SETs, and CLP3 has 3,000 Winning Bid (Offer) SETs, CLP1 would be allocated 60% of half of the daily CLP Rebate [6,000/(6,000+4,000)] and CLP2 would be allocated 40% of the half of the daily CLP Rebate [4,000/(6,000+4,000)]. Using the example above, CLP1 would receive \$75 [(\$250/2)×.6] and CLP2 would receive \$50 [(\$250/2)×.4]. In the event that there is only one Eligible CLP for the bid (offer) portion of the CLP Rebate for a CLP Security, such Eligible CLP will receive 100% of the bid (offer) half of the CLP Rebate. In the event that multiple CLPs have an equal number of winning SETs, the CLP with the highest executed volume in the CLP Security will be awarded the applicable portion of the CLP Rebate. Where no CLPs are eligible for the bid or offer portion of the CLP Rebate, no CLP Rebate will be awarded to any CLP and no refund will be provided.<sup>43</sup>

#### Assignment of CLP Securities

The Exchange, in its discretion, will assign to the CLP one or more CLP Securities for CLP trading purposes. The Exchange shall determine the number of CLP Securities assigned to each CLP. The Exchange, in its discretion, will assign one (1) or more CLPs to each CLP Security subject to the Program,

<sup>31</sup> See Interpretation and Policy .02(g) to Rule 11.8.

<sup>32</sup> Proposed Interpretation and Policy .03(i)(1) to Rule 11.8.

<sup>33</sup> See Interpretation and Policy .02(g)(1)(A) to Rule 11.8.

<sup>34</sup> Proposed Interpretation and Policy .03(i)(1)(A) to Rule 11.8.

<sup>35</sup> Proposed Interpretation and Policy .03(i)(1)(B) to Rule 11.8.

<sup>36</sup> Proposed Interpretation and Policy .03(i)(4) to Rule 11.8.

<sup>37</sup> As defined in BATS Rule 1.5(w), the term "Regular Trading Hours" means the time between 9:30 a.m. and 4:00 p.m. Eastern Time.

<sup>38</sup> Proposed Interpretation and Policy .03(i)(5) to Rule 11.8.

<sup>39</sup> *Id.*

<sup>40</sup> Proposed Interpretation and Policy .03(i)(2) to Rule 11.8.

<sup>41</sup> Proposed Interpretation and Policy .03(m)(1) to Rule 11.8.

<sup>42</sup> *Id.*

<sup>43</sup> *Id.*

depending upon the trading activity of the CLP Security.<sup>44</sup>

#### Non-Regulatory Penalties

If a CLP fails to meet the CLP quoting requirements, the Exchange may impose certain non-regulatory penalties. First, if, between 9:25 a.m. and 4:05 p.m. on any day on which the Exchange is open for business, a CLP fails to meet its daily quoting requirement by failing to have at least 10% of the winning SETs for that trading day, the CLP will not be eligible to receive the CLP Rebate for that day's quoting activity in that particular assigned CLP Security. Second, if a CLP fails to meet its monthly quoting requirement for three (3) consecutive months in any assigned CLP Security, the CLP will be at risk of losing its CLP status. Thus, the Exchange may, in its discretion, take the following non-regulatory actions: (i) revoke the assignment of the affected CLP Security(ies) and/or one or more additional unaffected CLP Securities; or (ii) disqualify a Member's status as a CLP.<sup>45</sup>

The Exchange shall determine if and when a Member is disqualified from its status as a CLP. One (1) calendar month prior to any such determination, the Exchange will notify the CLP of such impending disqualification in writing. If the CLP fails to meet the monthly quoting requirements as described above for a third consecutive month in a particular CLP Security, the CLP may be disqualified from CLP status. When disqualification determinations are made, the Exchange will provide a disqualification notice to the Member informing such Member that it has been disqualified as a CLP.<sup>46</sup> In the event a Member is disqualified from its status as a CLP, such Member may re-apply for CLP status. Such application process shall occur at least three (3) calendar months following the month in which such Member received its disapproval or disqualification notice. Further, in the event a Member is determined to be ineligible for the CLP Rebate for failure to meet its daily quoting obligation or is disqualified from its status as a CLP, such Member may seek review under Chapter X of the Exchange's Rules governing adverse action.<sup>47</sup> As noted above, Chapter X of the Exchange's Rules provides any persons who are or are about to be aggrieved by an adverse

action taken by the Exchange with a process to apply for an opportunity to be heard and to have the complained of action reviewed.

#### Web Site Disclosures

In order to provide transparency into the Program, including CLPs, CLP Companies, and the CLP Securities that are listed on the Exchange, the Exchange proposes to provide notification on its Web site regarding the following: (i) acceptance of a CLP Company, on behalf of a CLP Security, and a CLP into the Program; (ii) the total number of CLP Securities that any one CLP Company may have in the Program; (iii) the names of CLP Securities and the CLP(s) in each CLP Security, the dates that a CLP Company, on behalf of a CLP Security, commences participation in and withdraws or is terminated from the Program, and the name of each CLP Company and its associated CLP Security or Securities; (iv) a statement about the Program that sets forth a general description of the Program as implemented on a pilot basis and a fair and balanced summation of the potentially positive aspects of the Program as well as the potentially negative aspects and risks of the Program, and indicates how interested parties can get additional information about products in the Program; and (v) the intent of a CLP Company, on behalf of a CLP Security, or CLP to withdraw from the Program, and the date of actual withdrawal or termination from the Program.<sup>48</sup>

In addition, a CLP Company that, on behalf of a CLP Security, is approved to participate in the Program shall issue a press release to the public when the CLP Company, on behalf of a CLP Security, commences or ceases participation in the Program. The press release shall be in a form and manner prescribed by the Exchange, and, if practicable, shall be issued at least two days before commencing or ceasing participation in the Program. The CLP Company shall dedicate space on its Web site, or, if it does not have a Web site, on the Web site of the Sponsor of the CLP Security, that (i) includes any such press releases, and (ii) provides a hyperlink to the dedicated page on the Exchange's Web site that describes the Program.

#### Consistency With Regulation M

Rule 102 of Regulation M prohibits an issuer from directly or indirectly attempting "to induce any person to bid for or purchase, a covered security during the applicable restricted period"

unless an exemption is available.<sup>49</sup> For the reasons discussed below, the Exchange believes that exemptive relief from Rule 102 should be granted for the Program.

First, the Exchange notes that the Commission and its staff have previously granted relief from Rule 102 to a number of exchange traded products ("Existing Relief") in order to permit the ordinary operation of such exchange traded products.<sup>50</sup> In granting the Existing Relief, the Commission has relied in part on the exclusion from the provisions of Rule 102 provided by paragraph (d)(4) of Rule 102 for securities issued by an open-end management investment company or unit investment trust. In granting the Existing Relief from Rule 102 to other types of exchange traded products, for which the (d)(4) exception is not available, the staff has relied on (i) representations that the fund in question would continuously redeem exchange traded product shares in basket-size aggregations at their NAV and that there should be little disparity between the market price of an exchange traded product share and the NAV per share and (ii) a finding that "[t]he creation, redemption, and secondary market transactions in [shares] do not appear to result in the abuses that Rules 101 and 102 of Regulation M were designed to prevent."<sup>51</sup> The crux of the Commission's findings in granting the Existing Relief rests on the premise that the prices of exchange traded product shares closely track their per-share NAVs. Given that the Program neither alters the derivative pricing nature of ETPs nor impacts the arbitrage opportunities inherent therein, the conclusion on which the Existing Relief is based remains unaffected by the Incentive Program. In this regard, most ETPs that would be eligible to participate in the Program would have previously been granted relief from Rule 102.

Second, the Program requires, among other things, that a CLP make two-sided quotes during Regular Trading Hours in

<sup>49</sup> Rule 102 provides that "[i]n connection with a distribution of securities effected by or on behalf of an issuer or selling security holder, it shall be unlawful for such person, or any affiliated purchaser of such person, directly or indirectly, to bid for, purchase, or attempt to induce any person to bid for or purchase, a covered security during the applicable restricted period" unless an exception is available. See 17 CFR 242.102.

<sup>50</sup> See, e.g., Letter from James A. Brigagliano, Acting Associate Director, Division of Market Regulation, to Stuart M. Strauss, Esq., Clifford Chance US LLP (October 24, 2006) (regarding class relief for exchange traded index funds).

<sup>51</sup> See Rydex Specialized Products LLC, SEC No-Action Letter (June 21, 2006).

<sup>44</sup> Proposed Interpretation and Policy .03 (j)(1) to Rule 11.8.

<sup>45</sup> Proposed Interpretation and Policy .03 (l)(1) to Rule 11.8.

<sup>46</sup> Proposed Interpretation and Policy .03(l)(2) to Rule 11.8.

<sup>47</sup> Proposed Interpretation and Policy .03(l)(3) to Rule 11.8.

<sup>48</sup> Proposed Interpretation and Policy .03(o) to Rule 11.8.

order to have a winning set. The Program is not intended to raise ETP prices, but rather to improve market quality. In light of the derivative nature of ETPs, the Exchange does not expect that CLPs will quote outside of the normal quoting ranges for these products as a result of the CLP Rebate, but rather would quote within their normal ranges as determined by market factors. Indeed, the Program would not create any incentive for a CLP to quote outside such ranges.

Finally, the staff of the Exchange, which is a self-regulatory organization, would be interposed between the issuer and the CLP, administering a rules-based program with numerous structural safeguards described in the previous sections. Specifically, both CLPs and CLP Companies would be required to apply to participate in the Program and to meet certain standards. CLP Companies could not cause any fee to be paid to a CLP under the Program. The Exchange would collect the CLP Fees and credit them to the Exchange's General Fund. A CLP would be eligible to receive a CLP Rebate, again, from the Exchange's General Fund, only after it qualified for the CLP Rebate, as described above. Such qualification standards are set and monitored by the Exchange. Application to, continuation in, and withdrawal from the Program would be governed by published Exchange rules and policies, and there would be extensive public notice regarding the Program and payments thereunder on both the Exchange's and the CLP Company's Web sites. Given these structural safeguards, the Exchange believes that payments under the Program are appropriate for exemptive relief from Rule 102.

In summary, the Exchange believes that exemptive relief from Rule 102 should be granted for the Program because, for example: (1) The Program would not create any incentive for a CLP to quote outside of the normal quoting ranges for the ETPs included therein; (2) the Program has numerous structural safeguards, such as the application process for CLP Companies and CLPs, the interpositioning of the Exchange between CLP Companies and CLPs, and significant public disclosure surrounding the Program; and (3) the Program does not alter the basis on which Existing Relief is based and, furthermore, most ETPs that would be eligible to participate in the Program would have previously been granted relief from Rule 102.<sup>52</sup>

<sup>52</sup> The Exchange notes that the Commission granted a limited exemption from Rule 102 of Regulation M to The NASDAQ Stock Market LLC

## Surveillance

The Exchange believes that its surveillance procedures are adequate to properly monitor the trading of all securities trading on the Exchange, including ETPs participating in the Program, during all trading sessions, and to detect and deter violations of Exchange rules and applicable federal securities laws. The Exchange may obtain information via the Intermarket Surveillance Group ("ISG") from other exchanges who are members or affiliates of the ISG or with which the Exchange has entered into a comprehensive surveillance sharing agreement,<sup>53</sup> and from listed CLP Companies and public and non-public data sources such as, for example, Bloomberg.

## Changes to Interpretation and Policy .02 to Rule 11.8

The Exchange is also proposing to make certain changes to Interpretation and Policy .02 to Rule 11.8 that correspond with the addition of Interpretation and Policy .03. These changes are designed to remove any part of the CLP Program described in Interpretation and Policy .02 that relates directly to ETPs and to make clear that ETPs are not covered by Interpretation and Policy .02 to Rule 11.8. Specifically, the Exchange is proposing to: (i) Change the title from "Competitive Liquidity Provider Program" to "Competitive Liquidity Provider Program for Corporate Issues"; (ii) delete section (d)(2) in order to make clear that ETPs are not eligible for the CLP Program; (iii) delete the last two sentences of section (h)(2) that relate specifically to the assignment of CLPs to ETPs participating in the CLP Program; and (iv) delete text in section (k)(1) related to financial incentives for ETPs.

## 2. Statutory Basis

The Exchange believes that its proposal 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

("Nasdaq") for a program similar to the Exchange's proposed Program. See Securities Exchange Act Release No. 69196 (March 20, 2013), 78 FR 18410 (March 26, 2013) (Order Granting a Limited Exemption From Rule 102 of Regulation M Concerning the NASDAQ Market Quality Program Pilot Pursuant to Regulation M Rule 102(A)) (the "Nasdaq Exemption"). The Nasdaq Exemption includes certain conditions related to, among other things, notices to the public and disclosures with respect to Nasdaq's program. The Exchange notes that if the Commission were to provide exemptive relief from Rule 102 of Regulation M for the Program, it may include similar conditions.

<sup>53</sup> For a list of the current members and affiliate member of ISG, see [www.isgportal.com](http://www.isgportal.com).

requirements of Section 6(b) of the Act.<sup>54</sup> In particular, the proposal is consistent with Section 6(b)(4) and 6(b)(5) of the Act,<sup>55</sup> because it would provide for the equitable allocation of reasonable dues, fees, and other charges among Members and issuers and other persons using any facility or system which the Exchange operates or controls, and it is designed to promote just and equitable principles of trade, 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 goal of the Program is to incentivize Members to make high-quality, liquid markets, which supports the primary goal of the Act to promote the development of a resilient and efficient national market system. The Program will enhance quote competition, improve liquidity on the Exchange, support the quality of price discovery, promote market transparency, and increase competition for listings and trade executions, while reducing spreads and transaction costs. Maintaining and increasing liquidity in Exchange-listed securities will help raise investors' confidence in the fairness of the market and their transactions.

Each aspect of the Program adheres to and supports the Act. First, the Program promotes the equitable allocation of fees and dues among issuers. The Program is completely voluntary in that it will provide an additional means by which issuers may relate to the Exchange, while not eliminating the ability to list ETPs without participation in the Program. Issuers can supplement the standard listing fees with those of the Program, which the Exchange believes to be consistent with the Act. While the Program will result in higher fees for issuers that choose to participate, the issuers receive significant benefits for participating, including greater liquidity, tighter spreads, and lower transaction costs for their investors. Additionally, issuers will have the ability to withdraw from the Program after an initial commitment if they determine that participation is not beneficial. In that case, the withdrawing issuers will automatically revert to the basic listing fee for ETPs.

The Program also represents an equitable allocation of fees and dues among Market Makers. Again, the Program is completely voluntary with respect to Market Maker participation in that it will provide an additional means

<sup>54</sup> 15 U.S.C. 78f(b).

<sup>55</sup> 15 U.S.C. 78f(b)(4) and (5).

by which members may qualify for a CLP Rebate in a manner nearly identical to the existing CLP Program, without eliminating any of the existing means of qualifying for incentives on the Exchange. Currently, the Exchange employs multiple fee arrangements, including the CLP Program, to incentivize Market Makers to maintain high quality markets or to improve the quality of executions. Market Makers that choose to undertake increased burdens under the Program will be rewarded with increased rebates, while those that do not undertake such burdens will receive no added benefit. Where a CLP determines that the burdens imposed by the Program outweigh the benefits provided, the CLP may provide the Exchange with notice of withdrawal and will be withdrawn from the program in no longer than thirty days.

Additionally, the Program establishes an equitable allocation of CLP Rebates among Market Makers that choose to participate and fulfill the obligations imposed by the rule. If one Market Maker fulfills the bid (offer) obligations, bid (offer) portion of the CLP Rebate will be distributed to that CLP; if multiple CLPs satisfy the standard, the CLP Rebate will be distributed pro rata to the two CLPs with the most Winning Bid (Offer) SETs, as described above. In other words, all of the benefit of the CLP Rebate will flow to the highest-performing Market Makers, provided that at least one Market Maker fulfills the obligations under the proposed rule.

The Program is designed to avoid unfair discrimination among Market Makers and issuers. The proposed rule contains objective, measurable standards that the Exchange will apply with care. These standards will be applied equally to ensure that similarly situated parties are treated similarly. This is equally true for inclusion of issuers and Market Makers, withdrawal of issuers and Market Makers, and termination of eligibility for the Program. The standards are carefully constructed to protect the rights of all parties wishing to participate in the Program by providing notice of requirements and a description of the process. The Exchange will apply these standards with the same care and experience with which it applies the many similar rules and standards in the Exchange's rules.

In contrast to the extensive benefits of the Program, the participation of a CLP Company in the Program is substantially limited, by design. In this regard, a CLP Company is limited to making only the following determinations regarding the Program: Whether to participate in the

Program; what CLP Security should be in the Program; what firms will participate in developing and funding the CLP Security; when the CLP Security should exit the Program; and the level of Supplemental Fees, if any, that should be applied. The CLP can never influence how, when, or the specific amount that a CLP receives as credit for making a market in a CLP Security. These functions are performed solely by the Exchange according to standards set forth in the Program.

The Exchange notes that it operates in a highly competitive market in which market participants can readily favor competing venues if they deem fee levels at a particular venue to be excessive, or rebate opportunities available at other venues to be more favorable. Accordingly, the listing fees and rebates are constrained by the active competition for listings in ETPs and for market making. If a particular exchange charges excessive fees for listing, ETPs will choose to list elsewhere. Similarly, if an exchange fails to incent market makers to provide sufficient liquidity, participants will likely shift their order flow to other venues. Accordingly, the exchange charging excessive listing fees or providing insufficient rebates for market maker would likely not accomplish the goals of the Program. As such, the Exchange believes that this competitive dynamic imposes powerful restraints on the ability of any exchange to charge unreasonable fees for listing or provide insufficient rebates for market making activity.

The Exchange also notes that the Program, as proposed, is substantially similar to the existing functionality provided under the CLP Program. The Exchange believes that the CLP Program has been very beneficial to market participants, including investors, issuers, and Market Makers, by providing increased market quality in the form of tighter spreads and deeper liquidity. The Exchange believes that the proposed Program will enjoy similarly positive results to the benefit of issuers, investors in CLP Securities, and the financial markets as a whole.

*(B) Self-Regulatory Organization's Statement on Burden on Competition*

Exchange does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act, as amended. To the contrary, the Exchange believes that the proposal will increase competition in both the listings market and in competition for market makers. The Program will promote competition in the listings market by providing

issuers with a vehicle for paying the Exchange additional fees in exchange for incentivizing tighter spreads and deeper liquidity in listed securities. While the Program closely resembles the existing CLP Program, the proposed modifications are a response to the competition from other markets that either have or are developing similar programs, including Nasdaq<sup>56</sup> and NYSE Arca Equities, Inc.<sup>57</sup>

The Exchange also believes that the proposed changes will enhance competition among participants by creating incentives for market makers to compete to make better quality markets. By requiring both that market makers meet the quoting requirements and also to compete for the CLP Rebate, the quality of quotes on the Exchange will improve. This, in turn, will attract more liquidity to the Exchange and further improve the quality of trading in CLP Securities, which will also act to bolster the Exchange's listing business. As mentioned above, this proposal is in response to similar programs at or in development at other markets.

*(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 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 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 proposal, as modified by Amendment No. 1 thereto, is consistent with the Act. Comments

<sup>56</sup> See Securities Exchange Act Release No. 69195 (March 20, 2013), 78 FR 18393 (March 26, 2013) (SR-NASDAQ-2012-137).

<sup>57</sup> See Securities Exchange Act Release No. 69335 (April 5, 2013), SR-NYSEARCA-2013-34 (March 21, 2013).



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 email to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File No. SR-BATS-2013-035 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 No. SR-BATS-2013-035. This file number should be included on the subject line if email 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 Web site (<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 Web site 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 the filing will also 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 No. SR-BATS-2013-035 and should be submitted on or before July 26, 2013.

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

**Kevin M. O'Neill,**  
*Deputy Secretary.*

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<sup>58</sup> 17 CFR 200.30-3(a)(12).

## SECURITIES AND EXCHANGE COMMISSION

[Release No. 34-69890; File No. SR-NSCC-2013-05]

### Self-Regulatory Organizations; National Securities Clearing Corporation; Order Approving Proposed Rule Change To Require That All Locked-In Trade Data Submitted to It for Trade Recording Be Submitted in Real-time

June 28, 2013.

#### I. Introduction

On April 30, 2013, the National Securities Clearing Corporation ("NSCC") filed with the Securities and Exchange Commission ("Commission") the proposed rule change SR-NSCC-2013-05 pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 ("Act")<sup>1</sup> and Rule 19b-4 thereunder.<sup>2</sup> On May 14, 2013, NSCC filed with the Commission Amendment No. 1 to the proposed rule change.<sup>3</sup> The proposed rule change was published for comment in the **Federal Register** on May 20, 2013.<sup>4</sup> The Commission received one comment letter to the proposed rule change.<sup>5</sup> For the reasons discussed below, the Commission is granting approval of the proposed rule change.

#### II. Description

NSCC filed the proposed rule change to require that all locked-in trade data submitted to NSCC for trade recording be submitted in real-time,<sup>6</sup> and to prohibit pre-netting<sup>7</sup> and other

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

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

<sup>3</sup> In Amendment No. 1, NSCC corrected a typographical error in the text of its Rules & Procedures ("Rules") related to the proposed rule change.

<sup>4</sup> Release No. 34-69571 (May 14, 2013), 78 FR 29408 (May 20, 2013).

<sup>5</sup> Comment letter from Kermit Kubitz dated June 10, 2013, <http://www.sec.gov/comments/sr-nscc-2013-05/nscc201305.shtml>. The commenter supports the proposed rule change's requirement "to submit trades without any pre-processing . . ." and believes that, "any cost associated with submitting higher volumes of data from limiting pre-netting is small compared to the risks and costs of inaccurate data which might result from submission of other than accurate trade data."

<sup>6</sup> The term "real-time," when used with respect to trade submission, in any format and by any communication method acceptable to NSCC.

<sup>7</sup> According to NSCC, any pre-netting practices include: (i) "summarization" (i.e., a technique in which the clearing broker nets all trades in a single CUSIP by the same correspondent broker into fewer submitted trades); (ii) "compression" (i.e., a technique to combine submissions of data for multiple trades to the point where the identity of the party actually responsible for the trades is masked); (iii) netting; and (iv) any other practice

practices that prevent real-time trade submission, as discussed below.

#### *Proposal Overview*

According to NSCC, the majority of all transactions processed at NSCC are submitted on a locked-in basis by self-regulatory organizations ("SRO") (including national and regional exchanges and marketplaces), and Qualified Special Representatives ("QSR").<sup>8</sup> Currently, NSCC data reveals that almost all exchanges<sup>9</sup> and some QSRs submit trades executed on their respective markets in real-time, representing approximately 91% of the locked-in trades submitted to NSCC today. The rule change will require that all locked-in trades submitted for trade recording by SROs and QSRs be submitted to NSCC in real-time.<sup>10</sup>

NSCC will also prohibit Pre-netting practices that preclude real-time trade submission. NSCC states that typically, Pre-netting is done on a bilateral basis between a QSR and its customer, both NSCC Members. According to NSCC, Pre-netting practices disrupt NSCC's ability to accurately monitor market and credit risks as they evolve during the trading day. Therefore, NSCC will prohibit Pre-netting activity on the part of entities submitting original trade data on a locked-in basis.<sup>11</sup> The rules of NSCC's affiliate Fixed Income Clearing Corporation ("FICC") currently prohibit such activity, and this rule change will align NSCC's trade submission rules with those of FICC.<sup>12</sup>

that combines two or more trades prior to their submission to NSCC (collectively, "Pre-netting").

<sup>8</sup> QSRs are NSCC members ("Members") that either (i) operate an automated execution system where they are always the contra side of every trade, (ii) are the parent or affiliate of an entity operating such an automated system, where they are the contra side of every trade, or (iii) clear for a broker-dealer that operates such a system and the subscribers to the system acknowledge the clearing Member's role in the clearance and settlement of these trades.

<sup>9</sup> One executing market with very low trade volume does not yet submit trades in real-time.

<sup>10</sup> Files submitted to NSCC by The Options Clearing Corporation ("OCC") relating to option exercises and assignments (Procedure III, Section D—Settlement of Option Exercises and Assignments) will not be required to be submitted in real-time. OCC's process of assigning option assignments is and will continue to be an end-of-day process.

<sup>11</sup> Trades executed in the normal course of business between a Member that clears for other broker-dealers, and its correspondent, or between correspondents of the Member, which correspondent(s) is not itself a Member and settles such obligations through such clearing Member (i.e., "internalized trades") are not required to be submitted to NSCC and shall not be considered to violate the Pre-netting prohibition.

<sup>12</sup> See, e.g., GSD Rule 11 (Netting System), Section 3 ("All trade data required to be submitted to the Corporation under this Section must be submitted on a trade-by-trade basis with the