



BATS February 2012 Options Market Update

Dear BATS members and members of the trading community,

The year of the dragon has dawned; the 2012 Olympics are still months away. Yet it appears that, at least in the U.S. Options markets, the games have already begun.

In January the SEC held a first of its kind SRO Outreach Conference, bringing together all 15 of the different self-regulatory bodies that it oversees. There, it was pointed out numerous times that collectively the SROs filed over 2,000 rule filings in 2011. If the outbreak of activity that the nine exchanges have generated recently is any indication, the options exchanges alone may surpass that number in 2012, *just in fee changes*. Volume incentive programs are changing, rebates are climbing, take fees are shifting, break up fees that have been on and off (and on and off) are back on again. Job security for those charged with maintaining options routing tables has never been higher.

There are potent reasons behind the myriad of fee changes that we're seeing in the options markets. With cash volumes down and volatility low, options volumes are stagnant. January was the third down month in a row (November off 2% Year over Year (YoY), December off 6% YoY and January off 11% YoY as measured by OCC cleared contracts). While there are still plenty of macro drivers for growth of the options industry, with less flow currently going around, the exchanges must compete that much harder for their members' volume.

At the same time, volume continues to shift between market models. More volume is being done as part of complex strategies. Volume in the complex order books is up. The same is true of volume being done in the various price improvement mechanisms. Finally, as the structure of the options markets continues to evolve, more volume is being done in both make-take and price-time markets. Tighter spreads and greater fragmentation of liquidity are forcing members to evolve and adapt.

With all of the activity around fees in the options markets – some of it controversial – we encourage the Commission to revisit its proposal from April 2010 that relates to fee caps. Looking closely at this issue and the related issues of step-ups and payment for order flow can only help ensure the long-term structural integrity of the options markets.

TCV Rather Than Fixed Tiers

Part of the way that BATS has positioned its options exchange bears highlighting in the current market environment. Our volume tiers are based on Total Consolidated Volume (TCV) rather than fixed at an arbitrary level. When there is depressed industry volume, increased economics on BATS are achievable at a threshold that members can still achieve. On BATS Options, members who have contract volume (add and remove combined, regardless of capacity) equal to 1% TCV have Customer capacity rebates as high as \$.42 per contract paired with a Customer take rate that drops as low as \$.28 per contract.

In addition to TCV tiers, we continue to offer innovative *Market Quality* Incentives, NBBO Setter rebates and our Quoting Incentive Program (QIP). At the 1% TCV level Pro Customer, Firm and Market Maker capacity orders achieve an NBBO Setter incentive of as much as \$.10 per contract that adds to

their competitive base rebate as high as \$.32 per contract. And all members, regardless of volume tier, can gain even higher rebates (+\$.03/\$.05 per contract) by participating in our Quoting Incentive Program.

Grow With Us

In January, we made another important change to our strategic options pricing and how we measure member activity on BATS Options. As a relatively new options market we realize that not every member can come in and achieve a significant TCV level out of the gates. Rather than penalizing these members, our “Grow With Us” pricing allows members that are increasing their activity to enjoy half of the economics of the next TCV volume tier that they’re working toward. By increasing their activity by as little as five basis points of TCV a month, a member can significantly lower their take rates while increasing the rebate and incentive dollars they are earning. If industry volumes are at 16 million contracts per day, it takes as little as an increase of 8 thousand contracts per day to achieve a significant economic benefit. As a competitive and growing market, we’re asking members to keep their eye on the ball and participate with our growth.

BATS Listings

Looking outside of options, one of the biggest developments in the equities market in January was the launch of primary listings on BATS. The first listing (ENOR) launched on January 24th and was followed by seven more ETFs in the next two weeks. It’s worth noting all these ETFs are from BlackRock, Inc’s iShares ETF business, the world’s largest manager of ETFs. More important than the birth of a new primary listing exchange are the innovations in the listings program that BATS has included to make the process of bringing new issues to market better.

The recently approved BATS Competitive Liquidity Provider (CLP) Program creates a new set of incentives for market participants to provide liquidity and quote aggressively in securities which are listed on BATS. The program specifically incentivizes both quoting frequency at the NBBO and quoted size at the NBBO, and has the potential to improve the market quality of securities that participate in the CLP Program. CLP is open to all BATS Market Makers who wish to compete for the quoting incentive on a BATS-listed security and want to help us make markets better in this exciting new arena for BATS.

For more information on anything and everything related to Listings on BATS, please visit:

<http://www.batstrading.com/listings/>

In Closing

2012 is off to an interesting start. Please reach out and let us know, through your account manager or our trade desk what else we can do to help you grow your business. Your feedback is important as we continue to work to Make Markets Better.

Jeromee Johnson

VP, Head of US Options

BATS...Making Markets Better