Date: August 3, 2010

To: Members of BATS Exchange, Inc.

From: Membership Services

Re: **Notice Regarding Member Obligations to Comply with Intermarket Sweep Order Obligations**

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On April 6, 2005, the Securities and Exchange Commission adopted Regulation NMS, a series of initiatives designed to modernize and strengthen the national market system for equity securities. The purpose of this circular is to remind Members of their obligations with respect to the use of intermarket sweep orders ("ISOs") under Regulation NMS and related BATS Exchange Rules.

Background Regarding the Trade-Through Rule

Rule 611 of Regulation NMS (the "Trade-Through Rule") requires trading centers to "establish, maintain, and enforce written policies and procedures that are reasonably designed to prevent trade-throughs on that trading center of protected quotations in NMS stocks" subject to a series of exceptions; one commonly used exception to the Trade-Through Rule is for intermarket sweep orders ("ISOs").

As set forth in BATS Rule 11.9(d)(1), "In order to be eligible for treatment as an Intermarket Sweep Order, the limit order must be marked 'ISO' and *the User entering the order must simultaneously route one or more additional limit orders marked 'ISO,' as necessary, to away markets to execute against the full displayed size of any Protected Quotation for the security with a price that is superior to the limit price of the Intermarket Sweep Order entered in the System*." (Emphasis added.) Rule 11.9(d)(1), related to ISOs, and Rule 11.9(d)(2), related to Directed ISOs, both make clear that it is the entering Member's responsibility, not the Exchange's responsibility, to comply with the requirements of Regulation NMS relating to Intermarket Sweep Orders.

Background Regarding the Locked and Crossed Markets Rule

Rule 610 of Regulation NMS requires, among other requirements, each Self-Regulatory Organization (SRO) to "establish, maintain, and enforce written rules that: (1) Require its members reasonably to avoid (i) Displaying quotations that lock or cross any protected quotation in an NMS stock…." Accordingly, BATS Exchange Rule 11.20(b) states that "[e]xcept for quotations that fall within the provisions of paragraph (d) of this Rule, the System shall not make available for dissemination, and Users shall reasonably avoid displaying, and shall not engage in a pattern or practice of displaying, any quotations that lock or cross a protected quotation, and any manual quotations that lock or cross a quotation previously disseminated pursuant to an effective national market system plan."

Rule 11.20(d)(3), provides an exception to the prohibition against the display of a quotation that locks or crosses a protected quotation to the extent "the User displaying such automated quotation simultaneously routed an intermarket sweep order to execute against the full displayed size of any locked or crossed protected quotation."

Distinction between the ISO Exception to the Trade Through Rule and the ISO Exception to BATS Rule 11.20

The Exchange permits ISOs to be entered with time-in-force parameters of either immediate or cancel ("IOC") or day. IOC ISOs execute against the BATS Book and, if not executed in full, are then cancelled back to the entering User. A Member's IOC ISO order, therefore, could potentially trade-through a protected quotation; accordingly, each Member must comply with the provisions of the Trade-Through Rule and related BATS rules when submitting IOC ISOs. In contrast, day ISOs can post to the BATS Book, potentially locking or crossing a protected quotation, and thus, a Member submitting day ISOs must comply with the provisions of BATS Rule 11.20.

The SEC's Division of Trading and Markets explained the ISO exception to SRO Lock/Cross Rules in the answer to frequently asked question 5.02 from its "Responses to Frequently Asked Questions Concerning Rule 611 and 610 of Regulation NMS." Specifically, answer 5.02 states:

> [T]he ISO exception from the SRO lock/cross rules varies from other ISO exceptions with respect to the scope of protected quotations to which ISOs must be routed. For example, Rule 611(b)(6) requires that ISOs be routed to execute against all protected quotations with **better** prices than the price of the excepted trade-through transaction. The ISO exception to the SRO lock/cross rules, in contrast, requires that ISOs be routed to execute against all protected quotations with a price that is **equal** to the display price (*i.e.*, those protected quotations that would be locked by the displayed quotation), as well as all protected quotations with prices that are better than the display price (*i.e.*, those protected quotations that would be crossed by the displayed quotation).

(Emphasis added.)

The full text of the SEC Division of Trading and Markets Responses to Frequently Asked Questions Concerning Rule 611 and Rule 610 of Regulation NMS can be found at the following link: http://www.sec.gov/divisions/marketreg/nmsfaq610-11.htm

Please contact Membership Services, 913-815-7002, membershipservices@batstrading.com with any inquiries regarding this Regulatory Circular.

The Exchange's Rules are available at: http://www.batstrading.com/resources/regulation/rule_book/BATS_Exchange_Rulebook.pdf