

Dear BATS Customers and Members of the Trading Community,

The current equity market structure is under attack, brought on by a handful of politicians and some of the mainstream media who argue that the US system is fundamentally broken. Based largely on misunderstanding and perhaps other less forgivable reasons, these opponents are calling for major reviews, repairs, and outright intervention.

Many of us have spent the last several months defending the US equity market structure, a mature and interconnected market that has reduced trading costs to all time lows, narrowed bid/ask spreads, and revolutionized fair access for retail investors, institutional traders, and professional traders alike. This same market system also proved wholly resilient through one of the most challenging times in market history.

An old adage says, “the best defense is a good offense”, and that’s the opportunity presented to the industry by the SEC’s recent equity market structure Concept Release. This well-balanced 74 page document is primarily a list of questions and request for evidence surrounding several key market structure topics. Taking an active role in working through the Concept Release process is a way for our industry to go on the offense against those that would seek to regulate and/or tax the securities industry out of existence.

We are encouraged by the initial stage of this process and believe that the document will serve as the framework for industry debate on many important topics in the months ahead. It is critical, however, for all those with a stake in the equity markets to get involved in supporting the SEC’s effort to conduct a rational, detailed, and well-evidenced review.

The SEC has made it clear that it is looking for data, where available, as the foundation for answers and responses to the questions presented in the Concept Release. Again, this is an important opportunity for those in the industry to come forward with evidence to support their positions. Those outside the industry, who have differing opinions, are likely to have a difficult time bringing forward compelling arguments based on the lack of hard evidence. Politicians and media channels have been postulating that things are broke mostly through supposition and scary sound bites. The constructive approach put forward by the SEC will force all parties involved in the debate to use a more analytical and data centric approach to make their arguments.

BATS doesn’t believe the equities markets are broken. To the contrary, we would argue that the US equity markets were a shining model of reliability and healthy function during what some are calling one of the most challenging and difficult times in recent market history. Looking back over the last several years, including the fall of 2008 through spring of 2009, the markets were operational every day, reference prices were always available, customers were able to trade 100% of the time, and liquidity was plentiful throughout the trading day every day. While asset values did fall significantly, which is what doomsayers from outside the industry are focusing on, the existing equity market structure did not cause or exacerbate the fall.

Of course the current regulatory structure isn’t perfect, nor has it ever been or will it ever be, so we are supportive of ongoing efforts to optimize regulation in conjunction with the evolution of the underlying dynamics in our markets.

BATS is preparing a comment letter to the Concept Release, and we encourage every participant in the equity markets to do the same. None of us can afford to sit back and take a purely passive or defensive posture. Too much is at stake. The US has the most efficient, fair, and transparent equity market system in the world, and we all have a responsibility to defend it against the current, unsubstantiated outside attacks. Responding to the SEC Concept Release with hard evidence is a way to go on the offense, to protect what we know is working and to preserve our current equity markets against *baseless sound bites* from those who don't fully understand the markets.

There are a large number of discussion points in the SEC's Concept Release, and below I have addressed just a few, at a very high level, to provide a sense of where the BATS will stand in its formal comment letter. These are some of the *rational sound bites* I hope will come out on top when the dust settles:

Trading strategies should not be categorized and weighed against some kind of moral yard stick. Trading strategies are as diverse as are the individual personalities who trade and invest in the markets. As long as trading strategies comply with regulatory guidelines, and regulatory compliance is constantly monitored and enforced, we shouldn't try to qualify some strategies as good and some strategies as bad. Competition among market participants is a foundational element of our market's historical success. *Qualifying* trading strategies is best left to competitive forces.

Co-location is not bad. As long as co-location is monitored for fair access related to all participants that want to put their decision making systems close to exchange systems, the practice provides both direct and indirect benefits for all market participants. Co-location reduces message latency, and as latency is reduced, so is trading risk. As risk is reduced, so then are bid/ask spreads, for all participants. Co-location increases the efficiency of trading, and all participants realize the benefits of unfettered close proximity to exchange platforms.

An ATS is separate and unique from an Exchange. In rare cases, an Alternative Trading System (ATS) grows up to be an exchange (like BATS did), but in most cases an ATS will not follow the path to become a registered exchange. In the latter case, we shouldn't put too much "weight" on ATS entities, but should attempt to find a balance of responsibility that correlates to the relative size of the ATS. In our view, an ATS with 0.05% market share should not have the same regulatory weight as one that has 3% market share. An ATS that has, say 5% market share, is starting to look a lot like a large public market and perhaps should begin to carry the incremental weight of its peer registered exchanges. In other words, regulatory obligations, public quoting requirements and fair access provisions might be better implemented as a sliding scale based on the relative success (i.e. market share) each platform achieves. This will ensure that new competition can continue to enter the arena and challenge those ahead of them, spurring continuous innovation and efficiency for our industry.

High Frequency Trading (HFT) isn't one thing, its all things. Nearly all trading activity in the US equity market system comes through high speed computers and fiber optic connections. Even most retail orders come from internet terminals with broadband access to a retail broker's

data center that packages up FIX orders on behalf of the retail customer and submits them through servers co-located with each exchange. From the inside looking out, i.e. from an exchange's perspective, substantially all inbound subscriber connections exhibit many, if not all, of the attributes that have recently been labeled High Frequency Trading. Today's markets are simply more connected, more efficient, and handle more transaction volume than most people understand. Misguided attempts to regulate those basic elements that underpin the entire market infrastructure are likely to have long term, profoundly harmful ramifications on our capital markets.

Resist the urge even to use the *HFT* label, since the label itself is driving the fundamental misunderstanding. Similar to your firm's "Restricted *Stock* List", put High Frequency Trading on your firm's "Restricted *Word* List". If you want to put a label on it, call it "Trading and Market Automation", or *TMA*. The automation of trading in the US equity markets has increased liquidity, decreased spreads, lowered transaction costs, and reduced the time necessary to trade, for all participants. These benefits have directly benefited numerous market participants, particularly retail and institutional investors who are paying historically low trading costs to interact with the market with speed and certainty never imagined even a decade ago.

There are many other topics and sub-topics that will be debated through this process and we look forward to being an active participant in these debates. Clearly there will be many disagreements among market participants on the topics that will surface through the Concept Release process. That's a good thing, as long as everybody who has a stake in the matter steps up and participates. Let the best data win!

As always, your comments and feedback are welcome.

Sincerely,
Joe Ratterman

Chairman, President and CEO
BATS ... Making Markets Better