

MEMO# 29493

November 17, 2015

NYSE Arca Files Proposed Rule Change Relating to "Aberrant" Trades for ETPs

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TO:

ETF (EXCHANGE-TRADED FUNDS) COMMITTEE No. 26-15
ETF ADVISORY COMMITTEE No. 25-15
EQUITY MARKETS ADVISORY COMMITTEE No. 24-15

RE:

NYSE ARCA FILES PROPOSED RULE CHANGE RELATING TO "ABERRANT" TRADES FOR ETPS

The Securities and Exchange Commission has published a notice seeking comments on a NYSE Arca, Inc. proposed rule change regarding the treatment of trade reports for exchange traded products (ETPs) that it determines to be inconsistent with the prevailing market. [\[1\]](#) Comments should be submitted to the SEC 21 days after publication in the Federal Register.

Background

As a result of brief price dislocations, trades in ETPs occasionally occur at prices that deviate significantly from prevailing market prices and/or an investment fund's underlying value, resulting in trades that establish a high, a low, or last sale price for a security that does not reflect price discovery in the fund holdings. The notice suggests that such trades could lead to investor confusion if third party statistics for the ETP inappropriately reflect the very short-term market impact rather than ongoing fund performance.

NYSE Arca currently has a policy to address instances of "aberrant" trades for equity securities generally. The purpose of this proposed rule change is to adopt an additional policy to address instances of "aberrant" trades specific to ETPs traded on NYSE Arca. NYSE Arca believes that the derivatively-priced nature of ETPs necessitates the use of a different, and generally broader, set of circumstances to determine that trades are "aberrant."

Proposal

If NYSE Arca becomes aware (through its own monitoring or through another market, listed ETP issuer, or market participant) of ETP trade prices that do not accurately reflect an ETP's prevailing market or its underlying value, it proposes to apply a new policy pursuant to which it:

- i. may determine to append an "Aberrant Report Indicator" to any trade report with respect to any ETP trade executed on NYSE Arca that it determines is inconsistent with the prevailing market; and
- ii. would encourage vendors and other data recipients not to use prices of trades to which NYSE Arca has appended the Aberrant Trade Indicator in any calculation of an ETP's high, low, or last sale price.

In determining whether to append an Aberrant Report Indicator, the proposed policy would be as follows:

- i. Absent exceptional circumstances, NYSE Arca would determine whether the trade price does not reflect the ETP's prevailing market if the trade occurs at the greater of a minimum of 50 cents (when the previous trade or valid "Reference Price" [\[2\]](#) is \$100 or below) or 50 basis points (when the previous trade or valid Reference Price is over \$100).
- ii. If the conditions in (i) are met, NYSE Arca would determine whether to append an Aberrant Report Indicator upon consideration of all factors related to a trade, including the following:
 - Index changes, reconstitutions and rebalances;
 - News released in the market where the ETP's assets are primarily invested;
 - Changes in availability of ETP creations and/or redemptions;
 - Executions in other derivative instruments tracking the same underlying indices;
 - ETP issuer credit risk changes;
 - Whether the trade price represents a 52-week high or low for the ETP;
 - Whether the trade price reflects a share-split, reorganization or other corporate action;
 - System malfunctions or disruptions;
 - Validity of consolidated tape trades and quotes;
 - General market volatility of market conditions;
 - Historical volume and volatility for the ETP;
 - Material news released pertaining to the ETP;
 - Whether trading in the ETP was recently halted/resumed;
 - Trading bands, collars or circuit breakers;
 - A request from the ETP issuer, provided with documentation of a factual basis for believing that an execution is representative of market impact or trading issues outside of the issuer's control, rather than true price discovery; and
 - Executions otherwise inconsistent with the trading pattern in the ETP.

The notice states that NYSE Arca would consider each of these factors with a view towards maintaining a fair and orderly market and the integrity of reported trade data. If NYSE Arca determines to append the Aberrant Report Indicator to a trade that represented the last sale of that ETP on the exchange during a trading session, NYSE Arca also may determine to remove that trade's designation as the last sale either on the day of the trade or at a later date. This would provide NYSE Arca reasonable time to conduct due diligence regarding the trade, including the consideration of input from markets and other market participants.

Jane G. Heinrichs
Associate General Counsel

endnotes

[1] SEC Release No. 34-76431 (November 12, 2015), available at <http://www.sec.gov/rules/sro/nysearca/2015/34-76431.pdf>.

[2] The “Reference Price” refers to (a) if the primary market for an ETP is open at the time of the trade, the national best bid or offer for the ETP, or (b) if the primary market for an ETP is not open at the time of the trade, the first executable quote or print for the ETP on the primary market after execution of the trade in question. If the circumstances suggest that a different Reference Price would be more appropriate, NYSE Arca would use the different Reference Price. For instance, if the ETP’s national best bid and offer are so wide apart as to fail to reflect the ETP’s market, NYSE Arca might use a trade price or best bid or offer that was available prior to the trade in question as the Reference Price.

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