

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-94814; File No. SR-NYSE-2022-04)

April 28, 2022

Self-Regulatory Organizations; New York Stock Exchange LLC; Order Instituting Proceedings to Determine Whether to Approve or Disapprove a Proposed Rule Change to Amend Rules 5P, 5.2(j)(8)(e), 8P, and 98

On January 14, 2022, New York Stock Exchange LLC (“Exchange” or “NYSE”) filed with the Securities and Exchange Commission (“Commission”), 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> a proposed rule change to permit the listing and trading of certain exchange-traded products (“ETPs”) that overlie one or more NMS Stocks listed on the Exchange. The proposed rule change was published for comment in the Federal Register on January 31, 2022.<sup>3</sup> On March 9, 2022, pursuant to Section 19(b)(2) of the Act,<sup>4</sup> the Commission designated a longer period within which to approve the proposed rule change, disapprove the proposed rule change, or institute proceedings to determine whether to disapprove the proposed rule change.<sup>5</sup> The Commission has received no comment letters on the proposal. This order institutes proceedings under Section 19(b)(2)(B) of the Act<sup>6</sup> to determine whether to approve or disapprove the proposed rule change.

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

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

<sup>3</sup> See Securities Exchange Act Release No. 94053 (Jan. 25, 2022), 87 FR 4982 (“Notice”).

<sup>4</sup> 15 U.S.C. 78s(b)(2).

<sup>5</sup> See Securities Exchange Act Release No. 94392, 87 FR 14592 (Mar. 15, 2022). The Commission designated May 1, 2022 as the date by which it should approve or disapprove, or institute proceedings to determine whether to disapprove, the proposed rule change.

<sup>6</sup> 15 U.S.C. 78s(b)(2)(B).

## I. Summary Description of the Proposal<sup>7</sup>

The Exchange proposes to amend its rules regarding side-by-side trading, which is the trading of an equity security and its related derivative product at the same physical location. Specifically, the Exchange proposes to exclude from its listing prohibitions in NYSE Rules 5P and 8P<sup>8</sup> shares of an ETP that independently satisfies the quantitative generic listing criteria set forth in NYSE Rules 5.2(j)(3), Supplementary Material .01(a), NYSE Rule 5.2(j)(6)(B)(I); or proposed Rule 5.2(j)(8)(e)(1)(B), as well as shares of an ETP that independently satisfies the generic listing criteria set forth in NYSE Rules 8.100, Supplementary Material .01(a)(A) or 8.600, Supplementary Material .01(a).<sup>9</sup>

The Commission previously approved integrated market making and side-by-side trading for “broad-based” exchange traded funds, Trust-Issued Receipts, and related options.<sup>10</sup>

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<sup>7</sup> For a complete description of the proposed rule change, see Notice, supra note 3.

<sup>8</sup> NYSE Rules 5P and 8P generally prohibit the Exchange from listing shares of an ETP that “has any component NMS Stock that is listed on the Exchange or that is based on, or represents an interest in, an underlying index or reference asset that includes an NMS Stock listed on the Exchange. NMS Stock is defined in Rule 600 of Regulation NMS, 17 CFR 242.600(b)(48) as “any NMS security other than an option.” “NMS Security” means any security or class of securities for which transaction reports are collected, processed, and made available pursuant to an effective transaction reporting plan, or an effective national market system plan for reporting transactions in listed options.” 17 CFR 242.600(b)(47). “NMS Security” refers to “exchange-listed equity securities and standardized options, but does not include exchange-listed debt securities, securities futures, or open-end mutual funds, which are not currently reported pursuant to an effective transaction reporting plan.” See Question 1.1 in the “Responses to Frequently Asked Questions Concerning Large Trader Reporting,” available at: <https://www.sec.gov/divisions/marketreg/large-trader-faqs.htm>.

<sup>9</sup> Shares of Active Proxy Portfolio Shares and Managed Portfolio Shares, which are issued by funds whose portfolios are not fully transparent, already are exempted from the general prohibition. See NYSE Rule 8P.

<sup>10</sup> See Securities Exchange Act Release No. 46213, 67 FR 48232 (SR-Amex-2002-21); see also Securities Exchange Act Release No. 62479 (July 9, 2010), 75 FR 41264 (July 15, 2010) (SR-Amex-2010-31) (approving side-by-side trading and integrated market making

According to the Exchange, under Commission precedent, (1) integrated market making and side-by-side trading in both the ETP and related options is permissible – with no additional requirement for information barriers or physical or organizational separation – where the ETP is “broad-based,” i.e., not readily susceptible to manipulation; (2) an ETP is broad-based when its the individual components are sufficiently liquid and well-capitalized and the product is not over-concentrated; and (3) to determine whether an ETP is broad-based, the Commission has relied on an exchange’s listing standards.<sup>11</sup> In support of its proposal, the Exchange analyzes aspects of its existing – and in the case of Exchange-Traded Fund Shares, its proposed – listing criteria for shares of the specified ETPs and concludes that they are sufficiently “broad-based” to address potential manipulation concerns arising out of trading those shares on the same physical trading floor as one or more underlying NYSE-listed securities.<sup>12</sup>

The Exchange also proposes to amend a rule regarding integrated market making,<sup>13</sup> which is the practice of the same person or firm making markets in an equity security and its related derivative product. NYSE assigns each of securities it lists to a Designated Market Maker (“DMM”), and trading is on the floor of the Exchange. Integrated market making could be implicated if NYSE starts listing ETPs with an underlying NYSE Component Security because each ETP would be assigned to a DMM and that DMM also may be assigned one or more NYSE Component Securities that underlie the ETP’s underlying index or portfolio. The Exchange

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in the QQQ ETF and certain of its component securities where the QQQs met the composition and concentration measures to be classified as a broad-based ETF).

<sup>11</sup> See Notice, supra note 3, 87 FR at 4983.

<sup>12</sup> See id., 87 FR at 4984-85

<sup>13</sup> Current NYSE Rule 98(c)(6) prohibits DMM units from operating as a specialist or market maker on the Exchange in “related products” unless specifically permitted in Exchange rules.

proposes to narrow the definition of “related products” to exclude derivative instruments that overlie ETPs listed under NYSE Rules 5.2(j)(3), Supplementary Material .01(a); 5.2(j)(6)(B)(I); 5.2(j)(8)(e)(1)(B); 8.100, Supplementary Material .01(a)(A); 8.600 Supplementary Material .01(a); 8.601; or 8.900.

While informational advantage is a concern with respect to integrated market making,<sup>14</sup> the Exchange asserts that there are sufficient safeguards in place to prohibit the misuse of material nonpublic information by a member organization that operates a DMM unit. Specifically, the Exchange asserts that Rule 98 contains narrowly tailored restrictions to address that DMMs while on the floor may have access to certain floor-based non-public information and requires DMM units to maintain procedures and controls to prevent the misuse of material, non-public information that are effective and appropriate for that member organization.<sup>15</sup>

According to the Exchange, trading on the Exchange is subject to a comprehensive regulatory program that includes a suite of surveillances and routine examinations that review trading by DMMs and other market participants on the Exchange’s trading floor, including surveillances designed to monitor for trading ahead and manipulative activity.<sup>16</sup> To assist Exchange surveillance of DMM trading activity, a member organization operating a DMM unit must daily provide the Exchange with net position information in DMM securities by the DMM unit and any independent trading unit of which it is part for such times and in the manner prescribed by the Exchange pursuant to Rule 98(c)(5).<sup>17</sup> In addition, routine examinations are

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<sup>14</sup> See Securities Exchange Act Release No. 46213, supra note 10, 67 FR at 48235.

<sup>15</sup> See id., 87 FR at 4986.

<sup>16</sup> See id., 87 FR at 4987.

<sup>17</sup> See id.

conducted consistent with the current exam-based regulatory program associated with Rule 98 that reviews member organizations operating DMM units for compliance with the above-described policies and procedures to protect against the misuse of material nonpublic information.<sup>18</sup> Lastly, the Exchange asserts that DMM market making activity is not materially different from market making on other exchanges and that these existing programs are reasonably designed to address any concerns that may be raised by the trading of the specified listed ETPs that have underlying NYSE Component Securities.<sup>19</sup>

II. Proceedings to Determine Whether to Approve or Disapprove SR-NYSE-2019-54 and Grounds for Disapproval Under Consideration

The Commission is instituting proceedings pursuant to Section 19(b)(2)(B) of the Act<sup>20</sup> to determine whether the proposed rule change should be approved or disapproved. Institution of such proceedings is appropriate at this time in view of the legal and policy issues raised by the proposed rule change. Institution of proceedings does not indicate that the Commission has reached any conclusions with respect to any of the issues involved. Rather, as described below, the Commission seeks and encourages interested persons to provide comments on the proposed rule change.

Pursuant to Section 19(b)(2)(B) of the Act,<sup>21</sup> the Commission is providing notice of the grounds for disapproval under consideration. The Commission is instituting proceedings to allow for additional analysis of the proposed rule change's consistency with Section 6(b)(5) of the Act, which requires, among other things, that the rules of a national securities exchange be "designed

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<sup>18</sup> See id.

<sup>19</sup> See id.

<sup>20</sup> 15 U.S.C. 78s(b)(2)(B).

<sup>21</sup> Id.

to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade,” and “to protect investors and the public interest.”<sup>22</sup>

The Commission asks that commenters address the sufficiency of the Exchange’s statements in support of the proposal, which are set forth in the Notice, in addition to any other comments they may wish to submit about the proposed rule change. In particular, the Commission seeks comment on the following questions and asks commenters to submit data where appropriate to support their views.

1. What are commenters’ views generally on whether the Exchange’s proposal to implement side-by-side trading and integrated market making for certain ETPs to be listed and traded on the Exchange is consistent with Section 6(b)(5) of the Act, which requires that the Exchange’s rules be designed to, among other things, prevent fraudulent and manipulative acts and practices?
2. Do the quantitative generic listing criteria of current Rules 5.2(j)(3), Supplementary Material .01(a) (applicable to Investment Company Units), 5.2(j)(6)(B)(I) (applicable to Equity Index-Linked Securities), and proposed Rule 5.2(j)(8), as well as the generic listing criteria of current NYSE Rules 8.100 (applicable to Portfolio Depositary Receipts) and 8.600 (applicable to Managed Fund Shares) adequately address the concerns reflected in the “broad-based” test previously articulated by the Commission with respect to side-by-side trading and integrated market making?<sup>23</sup> If not, why? Should the Commission consider other factors in reviewing side-by-side trading and integrated market making?

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<sup>22</sup> 15 U.S.C. 78f(b)(5).

<sup>23</sup> See supra note 10.

3. What are commenters' views about whether the proposed changes to Rule 98 to exclude the specified ETPs listed on the Exchange from the definition of "related products" would remove impediments to and perfect the mechanism of a free and open market and a national market system? Do commenters agree that such changes would facilitate the assignment of listed ETPs, including ETPs with underlying NYSE Component Securities that meet the specified listing rules in Rules 5P and 8P, to DMMs and permit DMMs to trade such listed ETPs consistent with existing Rules governing DMM trading? If so, why? If not, why not?
4. What informational advantage (if any) over other market participants with respect to trading an ETP or its underlying securities might a DMM (or other member) obtain as a result of the proposed implementation of side-by-side trading and integrated market making for ETPs with underlying NYSE Component Securities? What concerns, if any, do commenters have about the potential for a DMM (or other member) to misuse material, non-public information?

### III. Procedure: Request for Written Comments

The Commission requests that interested persons provide written submissions of their views, data, and arguments with respect to the issues identified above, as well as any other concerns they may have with the proposal. In particular, the Commission invites the written views of interested persons concerning whether the proposal is consistent with Section 6(b)(5) or any other provision of the Act, or the rules and regulations thereunder. Although there do not appear to be any issues relevant to approval or disapproval that would be facilitated by an oral

presentation of views, data, and arguments, the Commission will consider, pursuant to Rule 19b-4, any request for an opportunity to make an oral presentation.<sup>24</sup>

Interested persons are invited to submit written data, views, and arguments regarding whether the proposal should be approved or disapproved by [insert date 21 days from publication in the Federal Register]. Any person who wishes to file a rebuttal to any other person's submission must file that rebuttal by [insert date 35 days from publication in the Federal Register]. The Commission asks that commenters address the sufficiency of the Exchange's statements in support of the proposal, in addition to any other comments they may wish to submit about the proposed rule change.

Comments 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 e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-NYSE-2022-04 on the subject line.

Paper comments:

- Send paper comments in triplicate to Secretary, Securities and Exchange Commission, 100 F Street, NE, Washington, DC 20549-1090.

All submissions should refer to File Number SR-NYSE-2022-04. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your

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<sup>24</sup> Section 19(b)(2) of the Act, as amended by the Securities Act Amendments of 1975, Pub. L. 94-29 (June 4, 1975), grants the Commission flexibility to determine what type of proceeding – either oral or notice and opportunity for written comments – is appropriate for consideration of a particular proposal by a self-regulatory organization. See Securities Act Amendments of 1975, Senate Comm. on Banking, Housing & Urban Affairs, S. Rep. No. 75, 94th Cong., 1st Sess. 30 (1975).



comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website (<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 website 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 also will be available for inspection and copying at the principal office of the Exchange. All comments received will be posted without change. Persons submitting comments are cautioned that we do not redact or edit personal identifying information from comment submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR-NYSE-2022-04 and should be submitted by [insert date 21 days from date of publication in the Federal Register]. Rebuttal comments should be submitted by [insert date 35 days from date of publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>25</sup>

J. Matthew DeLesDernier  
Assistant Secretary

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<sup>25</sup> 17 CFR 200.30-3(a)(57).