

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-90075; File No. SR-NYSEArca-2020-56)

October 2, 2020

Self-Regulatory Organizations; NYSE Arca, Inc.; Order Instituting Proceedings to Determine Whether to Approve or Disapprove a Proposed Rule Change to Amend NYSE Arca Rules 5.2-E(j)(3), 5.2-E(j)(8), 5.5-E(g)(2), 8.600-E, and 8.900-E

On June 18, 2020, NYSE Arca, Inc. (“Exchange” or “NYSE Arca”) filed with the Securities and Exchange Commission (“Commission”), pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act” or “Exchange Act”)<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> a proposed rule change to amend certain listing requirements relating to maintaining a minimum number of beneficial holders and minimum number of shares outstanding. The proposed rule change was published for comment in the Federal Register on July 7, 2020.<sup>3</sup>

On August 17, 2020, 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 proposed rule change. The Commission is issuing this order to institute proceedings pursuant to 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. 89197 (June 30, 2020), 85 FR 40720 (“Notice”).

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

<sup>5</sup> See Securities Exchange Act Release No. 89584, 85 FR 51817 (August 21, 2020). The Commission designated October 5, 2020 as the date by which the Commission shall 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. Description of the Proposal

The Exchange proposes to amend NYSE Arca Rules 5.2-E(j)(3) and 5.5-E(g)(2) (Investment Company Units), 5.2-E(j)(8) (Exchange-Traded Fund Shares), 8.600-E (Managed Fund Shares), and 8.900-E (Managed Portfolio Shares) (collectively, “Fund Shares”) to (1) remove the listing requirement that, following the initial twelve-month period after commencement of trading of a series of Investment Company Units, Exchange-Traded Fund Shares, Managed Fund Shares or Managed Portfolio Shares, respectively, on the Exchange, such series have at least 50 beneficial holders, and (2) replace the existing minimum number of shares requirements<sup>7</sup> with a requirement that a series of Fund Shares have at least one creation unit outstanding on an initial and continued listing basis.<sup>8</sup>

The Exchange believes that the requirement that a series of Fund Shares listed on the Exchange must have at least 50 beneficial shareholders is no longer necessary. The Exchange believes that the requirements of Rule 6c-11 under the 1940 Act and, in particular, the website disclosure requirements of Rule 6c-11(c), together with the existing creation and redemption process, serve to mitigate the risks of manipulation and lack of liquidity that the shareholders requirement was intended to address. The Exchange further believes that requiring at least one creation unit to be outstanding at all times, together with the enhanced disclosure requirements of

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<sup>7</sup> See Commentary .01(d) to NYSE Arca Rule 5.2-E(j)(3) (requiring a minimum of 100,000 shares of a series of Investment Company Units to be outstanding at commencement of trading); NYSE Arca Rule 5.2-E(j)(8)(e)(1)(A) (requiring the Exchange to establish a minimum number of Exchange-Traded Fund Shares to be outstanding at the time of commencement of trading); NYSE Arca Rule 8.600-E(d)(1)(A) (requiring the Exchange to establish a minimum number of Managed Fund Shares to be outstanding at the time of commencement of trading); and NYSE Arca Rule 8.900-E(d)(1)(A) (requiring the Exchange to establish a minimum number of Managed Portfolio Shares to be outstanding at the time of commencement of trading).

<sup>8</sup> The Exchange represents that the term “creation unit” would have the same meaning as defined in Rule 6c-11(a)(1) under the Investment Company Act of 1940 (“1940 Act”).

Rule 6c-11, will facilitate an effective arbitrage mechanism that, for Investment Company Units, Managed Fund Shares, and Exchange-Traded Fund Shares, will provide investors with sufficient transparency into the holdings of the underlying portfolio and help ensure that the trading price in the secondary market remains in line with the value per share of a fund's portfolio. As an example, the Exchange notes that Rule 6c-11(c)(1)(vi) requires additional disclosure if the premium or discount is in excess of 2% for more than seven consecutive days, so that there would be transparency to investors in the event there are indications of an inefficient arbitrage mechanism.

With respect to Managed Portfolio Shares, while these securities do not publicly disclose their portfolio holdings daily and are not eligible to rely on Rule 6c-11, the Exchange believes that the applicable Verified Intraday Indicative Value and other information required to be disseminated in connection with the listing and trading of Managed Portfolio Shares ensures transparency of key values and information, and that such information is sufficient to support an effective arbitrage process, independent of any minimum shareholders requirement.

The Exchange states that the arbitrage mechanism generally causes the market price and the net asset value per share to align, and the functioning of the arbitrage mechanism helps to ensure that the trading price in the secondary market is at fair value. The Exchange further states that the existence of the creation and redemption process, as well as the proposed requirement that at least one creation unit is always outstanding, would ensure that market participants are able to redeem Fund Shares and, thereby, allow the arbitrage mechanism to function properly. The Exchange believes, therefore, that such arbitrage mechanism would obviate the need for a minimum shareholders requirement to support a fair and orderly market in Fund Shares. In addition, the Exchange states that its surveillance procedures for Fund Shares and its ability to

halt trading in Fund Shares in specified circumstances provide for additional investor protections by further mitigating any abnormal trading that would affect the Fund Shares' prices.

II. Proceedings to Determine Whether to Approve or Disapprove SR-NYSEArca-2020-56 and Grounds for Disapproval Under Consideration

The Commission is instituting proceedings pursuant to Section 19(b)(2)(B) of the Act<sup>9</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.

Pursuant to Section 19(b)(2)(B) of the Act,<sup>10</sup> the Commission is providing notice of the grounds for disapproval under consideration. The Commission is instituting proceedings to allow for additional analysis of and input concerning the proposed rule change's consistency with the Act and, in particular, Section 6(b)(5) of the Act, which requires, among other things, that the rules of a national securities exchange be "designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest; and are not designed to permit unfair discrimination between customers, issuers, brokers, or dealers."<sup>11</sup>

The Commission has consistently recognized the importance of the minimum number of holders and other similar requirements in exchange listing standards. Among other things, such listing standards help ensure that exchange listed securities have sufficient public float, investor

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<sup>9</sup> 15 U.S.C. 78s(b)(2)(B).

<sup>10</sup> Id.

<sup>11</sup> 15 U.S.C. 78f(b)(5).

base, and trading interest to provide the depth and liquidity necessary to promote fair and orderly markets.<sup>12</sup>

As discussed above, the Exchange is proposing to (1) remove the listing requirement that, following the initial twelve-month period after commencement of trading of a series of Fund Shares on the Exchange, such series have at least 50 beneficial holders, and (2) replace the existing minimum number of shares requirements with a requirement that a series of Fund Shares have at least one creation unit outstanding on an initial and continued listing basis. In support of its proposal, the Exchange asserts that, for Investment Company Units, Exchange-Traded Fund Shares and Managed Fund Shares, the portfolio and other disclosure requirements of Rule 6c-11 under the 1940 Act, together with the requirement that there be at least one creation unit outstanding, would facilitate efficient arbitrage and mitigate the manipulation and liquidity risks that the minimum number of beneficial holders requirement was intended to address. With respect to Managed Portfolio Shares, the Exchange asserts that the existing requirement to disseminate the Verified Intraday Indicative Value and related information supports an effective arbitrage process and achieves those goals. The Exchange also believes its surveillance procedures and trading halt authority would further mitigate regulatory concerns. The Exchange does not specifically address the proposed elimination of its existing minimum number of shares requirements.

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<sup>12</sup> See, e.g., Securities Exchange Act Release No. 57785 (May 6, 2008), 73 FR 27597 (May 13, 2008)(SR-NYSE-2008-17) (stating that the distribution standards, which includes exchange holder requirements "... should help to ensure that the [Special Purpose Acquisition Company's] securities have sufficient public float, investor base, and liquidity to promote fair and orderly markets"); Securities Exchange Act Release No. 86117 (June 14, 2019), 84 FR 28879 (June 20, 2018) (SR-NYSE-2018-46) (disapproving a proposal to reduce the minimum number of public holders continued listing requirement applicable to Special Purpose Acquisition Companies from 300 to 100).

While the Exchange takes the position that existing disclosure requirements, together with the creation and redemption process, sufficiently mitigate the risks of manipulation and lack of liquidity that the minimum shareholders requirement was intended to address, the Exchange does not explain in any detail the basis for this view, particularly if a series of Fund Shares is permitted to have a very small number of beneficial holders. For example, the Exchange does not address how the arbitrage mechanism will assure Fund Shares with very few holders are sufficiently liquid to support fair and orderly markets. The Exchange also does not discuss potential inefficiencies in the arbitrage mechanism that might occur with illiquid Fund Shares that have very few holders, and the impact that would have on the ability of the arbitrage mechanism to effectively mitigate the risks of manipulation. Further, the Exchange does not address the impact of creation unit size on the efficiency of the arbitrage mechanism (e.g., illiquid Fund Shares with very few holders and a large creation unit size). The Exchange provides no data or analysis to support its position, other than noting the number and size of the creation units for existing series of Fund Shares.

The Exchange provides no specific arguments to support the proposed elimination of its existing minimum number of shares requirements. While the Exchange proposes to replace those requirements with a requirement that a series of Fund Shares have a number of shares outstanding equal to at least one creation unit, the Exchange does not explain why this is an appropriate substitute for its existing standards. Creation unit sizes could be highly variable, since they are determined at the discretion of the issuer of Fund Shares, and the Exchange has not articulated how this new standard would effectively support fair and orderly markets, address the risks of manipulation, and otherwise be consistent with Section 6(b)(5) and other relevant provisions of the Act.

Finally, the Exchange takes the position that its surveillance procedures and trading halt authority for Fund Shares would further mitigate regulatory concerns. The Exchange, however, does not explain in any detail the basis for this view, or how specifically these existing procedures would effectively mitigate the risks addressed by the minimum number of beneficial holders and minimum number of shares requirements the Exchange is proposing to eliminate.

Under the Commission's Rules of Practice, the "burden to demonstrate that a proposed rule change is consistent with the Exchange Act and the rules and regulations issued thereunder...is on the self-regulatory organization ['SRO'] that proposed the rule change."<sup>13</sup> The description of a proposed rule change, its purpose and operation, its effect, and a legal analysis of its consistency with applicable requirements must all be sufficiently detailed and specific to support an affirmative Commission finding, and any failure of an SRO to provide this information may result in the Commission not having a sufficient basis to make an affirmative finding that a proposed rule change is consistent with the Exchange Act and the applicable rules and regulations.<sup>14</sup>

For these reasons, the Commission believes it is appropriate to institute proceedings pursuant to Section 19(b)(2)(B) of the Act to determine whether the proposal should be approved or disapproved.

#### IV. Commission's Solicitation of 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

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<sup>13</sup> Rule 700(b)(3), Commission Rules of Practice, 17 CFR 201.700(b)(3).

<sup>14</sup> See id.

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>15</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, which are set forth in the Notice,<sup>16</sup> 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-NYSEArca-2020-56 on the subject line.

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<sup>15</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).

<sup>16</sup> See supra note 3.



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-NYSEArca-2020-56. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your 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-NYSEArca-2020-56 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>17</sup>

J. Matthew DeLesDernier  
Assistant Secretary

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