

SEC Prepares Regulatory Review into the Exchange Traded Fund Industry

By Alexander Baptiste, J.D. Candidate 2018 | November 8, 2016

The Securities and Exchange Commission (SEC) is preparing for a full-scale review of the exchange-traded fund (ETF) industry, an unnamed source told the [Financial Times](#) in an article published October 20, 2016.

[Exchange-traded funds](#) are a form of mutual fund that trade like a stock, with pricing information that is continuously updated. Following their conception in 1993, ETFs have grown exceedingly popular in the financial industry. According to a report published by accounting and consulting firm PricewaterhouseCoopers (PwC), the global assets under management at these funds have grown from \$1.5 trillion at the end of 2010, to \$3 trillion at the end of 2015. In their report, PwC projected that the collective assets under management at these funds could reach \$8 trillion by 2021.

The popularity of ETFs can be [attributed](#) to their utility of providing a liquid vehicle for passive, broad-market investing. Another selling point of these funds is that they provide investors with the ability to trade niche assets as though they were U.S. exchange-listed stock, including bonds, commodities, and foreign equities.

The SEC's review of the ETF industry is partly due to the fact that these funds were at the center of wild equity trading in 2015. On August 24, 2015, a global selloff in equities saw the S&P 500 decline by four percent, the FTSE 100 and Dax fall by five percent, and the Shanghai Stock Exchange Composite plunge by over eight percent. This instance of chaotic trading tripped market circuit breakers, which halted trading in individual stocks and ETFs on U.S. exchanges over 1,000 times. As a result, some index-tracking ETFs fell far below the value of the indices they track. From this instance of abnormal trading, the SEC took note of how interconnected ETFs appear to be with the underlying stocks as well as the futures market. In this review, the SEC is expected to conduct a full-scale examination of the ETF industry and project any consequences to the stock market that might arise from the exorbitant growth of ETFs.

Up until recently, the SEC has reviewed the ETF industry in bits and pieces. In 2014, a small group of employees across the SEC's divisions were tasked with investigating the industry itself. According to a source briefed on this matter, the SEC is now "laying the groundwork for a bigger review."

In a speech earlier this year, SEC chair Mary Jo White addressed the rapid growth of ETFs, and hinted that an expansive review may be forthcoming. In the wake of the stock market slide in August of 2015, White has singled out ETFs for "enhanced attention," stating in May that the SEC "has taken a number of initial actions to share [its] thinking on these issues, and further regulatory steps beyond additional disclosures may be needed to address some of these issues."