

SEC Proposing New Rules to Prevent Repeat of May 6th “Flash Crash”

The SEC is contemplating new rules in response to the so-called flash crash of May 6, 2010. During that crash, the drop in the Dow Jones Industrials Average (Dow) briefly wiped out more than \$1 trillion in the market value of stocks. The Dow later recovered but still finished the day down 347 points.



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One of the first proposed rules being considered by the SEC is to allow U.S. stock exchanges to briefly halt the trading of some stocks that have big price swings to help avoid market plunges. Under the plan, trading of any Standard & Poor's 500 stock that rises or falls 10 percent or more would be halted for five minutes. These rules, known as "circuit breakers," would be applied if the price swing occurs between 9:45 AM and 3:35 PM ET.

A second proposed rule would require U.S. stock exchanges to create a consolidated audit trail of trading information. The proposal will initially cover all National Market System stocks and listed options and requires exchanges and their members to send quote and order information to a newly-created central repository as close to real-time as possible. Currently, there is no single database on order and execution data for U.S. securities. Regulatory bodies are required to consolidate a vast amount of data from disparate market participants to reconstruct an unusual market event or monitor suspicious trading activity.

Finally, the SEC may require greater disclosure of the distance between high-speed computers and big exchanges' data centers. Traders often position their computers close to the data centers, a practice called co-location, which can cut their trade times by milliseconds. High-frequency traders can make money by exploiting stock indexes that don't immediately reflect falling or rising prices of their component stocks. Their critics say split-second trading without human supervision is a recipe for disaster.

The rules are expected to begin in the following weeks, possibly as soon as mid-June, under a six-month pilot program agreed to by exchanges and regulators, but, as of this writing, the plan has not been made public. It was not known when an official announcement will be made.

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