

SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34-65134; File No. SR-NYSEArca-2011-23)

August 15, 2011

Self-Regulatory Organizations; NYSE Arca, Inc.; Order Granting Approval of Proposed Rule Change to List and Trade Shares of ProShares Short VIX Short-Term Futures ETF, ProShares Short VIX Mid-Term Futures ETF, ProShares Ultra VIX Short-Term Futures ETF, ProShares Ultra VIX Mid-Term Futures ETF, ProShares UltraShort VIX Short-Term Futures ETF, and ProShares UltraShort VIX Mid-Term Futures ETF under NYSE Arca Equities Rule 8.200, Commentary .02

I. Introduction

On April 28, 2011, 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”)<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> a proposed rule change to list and trade shares (“Shares”) of ProShares Short VIX Short-Term Futures ETF, ProShares Short VIX Mid-Term Futures ETF (“Short Funds”), ProShares Ultra VIX Short-Term Futures ETF, ProShares Ultra VIX Mid-Term Futures ETF (“Ultra Funds”), ProShares UltraShort VIX Short-Term Futures ETF, and ProShares UltraShort VIX Mid-Term Futures ETF (“UltraShort Funds” and, together with the Short Funds and Ultra Funds, the “Funds”) under NYSE Arca Equities Rule 8.200, Commentary .02. The proposed rule change was published in the Federal Register on May 17, 2011.<sup>3</sup> The Commission received no comments on the proposal. On July 1, 2011, the Exchange submitted a request to extend the Commission’s action date for the proposed rule change to August 15, 2011. This order grants approval of the proposed rule change.

II. Description of the Proposal

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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. 64470 (May 11, 2011), 76 FR 28493 (“Notice”).

The Exchange proposes to list and trade the Shares pursuant to NYSE Arca Equities Rule 8.200, Commentary .02, which permits the trading of Trust Issued Receipts. ProShare Capital Management LLC (“Sponsor”), a Maryland limited liability company, serves as the Sponsor of ProShares Trust II (“Trust”) and is a commodity pool operator and commodity trading advisor.<sup>4</sup> Brown Brothers Harriman & Co. serves as the administrator (“Administrator”), custodian, and transfer agent of the Funds and their respective Shares. SEI Investments Distribution Co. serves as Distributor of the Shares. Wilmington Trust Company, a Delaware banking corporation, is the sole trustee of the Trust.

The Funds seek, on a daily basis, to provide investment results (before fees and expenses) that correspond to the inverse of the daily performance, a multiple of the daily performance, or an inverse multiple of the daily performance of a benchmark that seeks to offer exposure to market volatility through publicly traded futures markets. The benchmark for ProShares Short VIX Short-Term Futures ETF, ProShares Ultra VIX Short-Term Futures ETF, and ProShares UltraShort VIX Short-Term Futures ETF is the S&P 500 VIX Short-Term Futures Index, and the benchmark for ProShares Short VIX Mid-Term Futures ETF, ProShares Ultra VIX Mid-Term Futures ETF, and ProShares UltraShort VIX Mid-Term Futures ETF is the S&P 500 VIX Mid-Term Futures Index (each, an “Index,” and, collectively, the “Indexes”).<sup>5</sup> The Funds will take long (in the case of the Ultra Funds) and short (in the case of the Short and UltraShort Funds) positions in futures contracts based on the Chicago Board Options Exchange (“CBOE”) Volatility Index (“VIX”) and, under limited circumstances, swap agreements (as described

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<sup>4</sup> The Funds have filed a registration statement on Form S-3 under the Securities Act of 1933. See Post-Effective Amendment No. 4 dated April 13, 2011 (File No. 333-163511) to the Trust’s Registration Statement on Form S-3 (“Registration Statement”).

<sup>5</sup> Standard & Poor’s Financial Services LLC, the index sponsor with respect to the Indexes, is not a broker-dealer and has implemented procedures designed to prevent the use and dissemination of material, non-public information regarding the Indexes.

below), to pursue their respective investment objectives. Each Fund also may invest in cash or cash equivalents such as U.S. Treasury securities or other high credit quality short-term fixed-income, or similar securities that may serve as collateral for the futures contracts and swap agreements.

Specifically, each Fund seeks to achieve its investment objective by investing under normal market conditions<sup>6</sup> in VIX futures contracts traded on the CBOE Futures Exchange (“CFE”) (“VIX Futures Contracts”) such that each Fund has exposure intended to approximate the inverse of the daily performance, a multiple of the daily performance, or an inverse multiple of the daily performance of its respective Index at the time of the net asset value (“NAV”) calculation. In the event position accountability rules are reached with respect to VIX Futures Contracts, the Sponsor may, in its commercially reasonable judgment, cause such Fund to obtain exposure through swaps referencing the relevant Index or particular VIX Futures Contracts, or invest in other futures contracts or swaps not based on the particular VIX Futures Contracts if such instruments tend to exhibit trading prices or returns that correlate with the Indexes or any VIX Futures Contract and will further the investment objective of such Fund.<sup>7</sup> The Funds may also invest in swaps if the market for a specific futures contract experiences emergencies or

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<sup>6</sup> The term “under normal conditions” includes, but is not limited to, the absence of extreme volatility or trading halts in the futures markets or the financial markets generally; operational issues causing dissemination of inaccurate market information; or force majeure type events such as systems failure, natural or man-made disaster, act of God, armed conflict, act of terrorism, riot or labor disruption or any similar intervening circumstance.

<sup>7</sup> To the extent practicable, the Funds will invest in swaps cleared through the facilities of a centralized clearing house.

disruptions that prevent a Fund from obtaining the appropriate amount of investment exposure to the affected VIX Futures Contracts directly or to other futures contracts.<sup>8</sup>

If the Short Funds are successful in meeting their objectives, their values (before fees and expenses) should gain approximately as much on a percentage basis as their respective Index when it declines on a given day. Conversely, their values (before fees and expenses) should lose approximately as much on a percentage basis as their respective Index when it rises on a given day. If the Ultra Funds are successful in meeting their objectives, their values (before fees and expenses) should gain approximately twice as much on a percentage basis as their respective Index when it rises on a given day. Conversely, their values (before fees and expenses) should lose approximately twice as much on a percentage basis as their respective Index when it declines on a given day. If the UltraShort Funds are successful in meeting their objectives, their values (before fees and expenses) should gain approximately twice as much on a percentage basis as their respective Index when it declines on a given day. Conversely, their values (before fees and expenses) should lose approximately twice as much on a percentage basis as their respective Index when it rises on a given day.

Each of the Funds uses investment techniques that include the use of any one or a combination of VIX Futures Contracts and may, if applicable, include swap agreements. The Funds' investment techniques may involve a small investment relative to the amount of investment exposure assumed and may result in losses exceeding the amounts invested. Such techniques, particularly when used to create leverage, may expose the Funds to potentially

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<sup>8</sup> The Sponsor will attempt to mitigate the Funds' credit risk by transacting only with large, well-capitalized institutions using measures designed to determine the creditworthiness of a counterparty. The Sponsor will take various steps to limit counterparty credit risk, as described in the Registration Statement.

dramatic changes (losses or gains) in the value of their investments and imperfect correlation between the value of the investments and the security or Index.

The Funds do not seek to achieve their stated investment objective over a period of time greater than one day because mathematical compounding prevents the Funds from perfectly achieving such results. Accordingly, results over periods of time greater than one day typically will not be a simple inverse correlation (-100%), multiple correlation (+200%), or multiple inverse correlation (-200%) of the period return of the corresponding Index and may differ significantly.

Each Fund is not actively managed by traditional methods, which typically involve effecting changes in the composition of a portfolio on the basis of judgments relating to economic, financial, and market considerations with a view toward obtaining positive results under all market conditions. Rather, the Sponsor will seek to cause the NAV to track the inverse of the daily performance, a multiple of the daily performance, or an inverse multiple of the daily performance of an Index, even during periods in which the benchmark is flat or moving in a manner which causes the NAV of a Fund to decline. The Sponsor will use a mathematical approach to determine the type, quantity, and mix of investment positions that it believes should produce returns consistent with each Fund's objective. The Sponsor will rely upon a pre-determined model to generate orders that result in repositioning the Funds' investments in accordance with their respective investment objectives.

#### VIX Futures Contracts

The Indexes are comprised of, and the value of the Funds will be based on, VIX Futures Contracts. VIX Futures Contracts are measures of the market's expectation of the level of the

VIX at certain points in the future and will behave differently than current or spot VIX values.<sup>9</sup>

The Funds are not linked to the VIX, and in many cases the Indexes, and by extension the Funds, could significantly underperform or outperform the VIX. While the VIX represents a measure of the current expected volatility of the S&P 500 over the next 30 days, the prices of VIX Futures Contracts are based on the current expectation of what the expected 30-day volatility will be at a particular time in the future (on the expiration date). The VIX Futures Contracts trade from 8:20 a.m. Eastern Time (“E.T.”) to 4:15 p.m. E.T.

### The Indexes

The Indexes act as a measure of volatility as reflected by the price of certain VIX Futures Contracts (“Index Components”), with the price of each VIX Futures Contract reflecting the market’s expectation of future volatility. Each Index seeks to reflect the returns that are potentially available from holding an unleveraged long position in certain VIX Futures Contracts. Unlike the Indexes, the VIX, which is not a benchmark for any Fund, is calculated based on the prices of put and call options on the S&P 500, which are traded on the CBOE.

The S&P 500 VIX Short-Term Futures Index employs rules for selecting the Index Components and a formula to calculate a level for the Index from the prices of these components. Specifically, the Index Components represent the prices of the two near-term VIX futures months, replicating a position that rolls the nearest month VIX Futures Contract to the

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<sup>9</sup> VIX is the ticker symbol for the CBOE Volatility Index, a popular measure of implied volatility. According to the Registration Statement, the goal of the VIX is to estimate the implied volatility of the S&P 500 over the next 30 days. A relatively high level of the VIX corresponds to a more volatile U.S. equity market as expressed by more costly options on the S&P 500 Index. The VIX represents one measure of the market’s expectation of the volatility over the next 30 day period. It is a composite value of options on the S&P 500 Index. The formula used to calculate the composite value utilizes current market prices for a series of out-of-the-money calls and puts for the front month and second month expirations.

next month VIX Futures Contract on a daily basis in equal fractional amounts. This results in a constant weighted average maturity of one month. The roll period begins on the Tuesday prior to the monthly VIX Futures Contracts settlement date and runs through the Tuesday prior to the subsequent month's VIX Futures Contract settlement date.

The S&P 500 VIX Mid-Term Futures Index also employs rules for selecting the Index Components and a formula to calculate the level of the Index from the prices of these components. Specifically, the Index Components represent the prices for four contract months of VIX Futures Contracts, representing a market-based estimation of constant maturity, five month forward implied VIX values. The S&P 500 VIX Mid-Term Futures Index measures the return from a rolling long position in the fourth, fifth, sixth and seventh month VIX Futures Contracts and rolls continuously throughout each month while maintaining positions in the fifth and sixth month contracts. This results in a constant weighted average maturity of five months.

Because the Indexes incorporate the process of rolling futures positions on a daily basis, and the Funds, in general, also roll their positions on a daily basis, the daily roll is not anticipated to be a significant source of tracking error between a Fund and its respective Index. The Indexes are based on VIX Futures Contracts and not the VIX, and as such neither the Funds nor the Indexes are expected to track the VIX. The level of each Index is calculated in accordance with the method described in the Registration Statement and will be published at least every 15 seconds both in real time from 9:30 a.m. to 4:15 p.m. E.T. and at the close of trading on each Business Day by Bloomberg L.P. and Reuters.<sup>10</sup>

Additional information regarding the Funds and the Shares, investment strategies, risks,

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<sup>10</sup> A "Business Day" means any day other than a day when any of the NYSE, NYSE Arca, CBOE, or CFE or other exchange material to the valuation or operation of the Funds, or the calculation of the VIX, options contracts underlying the VIX, VIX Futures Contracts, or the Indexes is closed for trading.

creation and redemption procedures, Indexes, VIX Futures Contracts, calculation and dissemination of NAV, fees, portfolio holdings, disclosure policies, distributions and taxes, availability of information, trading rules and halts, and surveillance procedures, among other things, can be found in the Notice and Registration Statement, as applicable.<sup>11</sup>

### III. Discussion and Commission's Findings

The Commission has carefully reviewed the proposed rule change and finds that it is consistent with the requirements of Section 6 of the Act<sup>12</sup> and the rules and regulations thereunder applicable to a national securities exchange.<sup>13</sup> In particular, the Commission finds that the proposal is consistent with Section 6(b)(5) of the Act,<sup>14</sup> which requires, among other things, that the Exchange's rules be designed 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. The Commission notes that the Shares must comply with the requirements of NYSE Arca Equities Rule 8.200 and Commentary .02 thereto to be listed and traded on the Exchange.

The Commission finds that the proposal to list and trade the Shares on the Exchange is consistent with Section 11A(a)(1)(C)(iii) of the Act,<sup>15</sup> which sets forth Congress' finding that it is in the public interest and appropriate for the protection of investors and the maintenance of fair and orderly markets to assure the availability to brokers, dealers, and investors of information

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<sup>11</sup> See Notice and Registration Statement, supra notes 3 and 4, respectively.

<sup>12</sup> 15 U.S.C. 78f.

<sup>13</sup> In approving this proposed rule change, the Commission notes that it has considered the proposed rule's impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

<sup>14</sup> 15 U.S.C. 78f(b)(5).

<sup>15</sup> 15 U.S.C. 78k-1(a)(1)(C)(iii).

with respect to quotations for and transactions in securities. Quotation and last-sale information regarding the Shares will be disseminated through the facilities of the Consolidated Tape Association. The level of each Index will be published at least every 15 seconds both in real time from 9:30 a.m. to 4:15 p.m. E.T. and at the close of trading on each Business Day by Bloomberg L.P. and Reuters. In addition, an updated Indicative Optimized Portfolio Value (“IOPV”), which is an indicator of the value of the VIX Futures Contracts and cash and/or cash equivalents less liabilities of a Fund, will be calculated. NYSE Arca will calculate and disseminate every 15 seconds throughout the NYSE Arca Core Trading Session (9:30 a.m. to 4:00 p.m. E.T.) an updated IOPV. The IOPV will be published on the NYSE Arca’s website and be available through on-line information services such as Bloomberg and Reuters. Further, the Funds will provide website disclosure of portfolio holdings daily and will include, as applicable, the notional value (in U.S. dollars) of VIX Futures Contracts, other financial instruments, if any, cash equivalents, and amount of cash held in the portfolio of the Funds. The intra-day, closing, and settlement prices of the Index Components are also readily available from the websites of the CFE ([www.cfe.cboe.com](http://www.cfe.cboe.com)), automated quotation systems, published or other public sources, or on-line information services such as Bloomberg or Reuters. The specific contract specifications for component futures underlying the Indexes are also available on such websites, as well as other financial informational sources. The CFE also provides delayed futures information on current and past trading sessions and market news free of charge on its website. The NAV for each Fund will be calculated by the Administrator once a day at 4:15 p.m. E.T. The Exchange will make available on its website daily trading volume of each of the Shares, closing prices of such Shares, and number of Shares outstanding. The Funds’ website, [www.proshares.com](http://www.proshares.com), will display the end of day closing Index levels and NAV.

The Commission further believes that the proposal to list and trade the Shares is reasonably designed to promote fair disclosure of information that may be necessary to price the Shares appropriately and to prevent trading when a reasonable degree of transparency cannot be assured. The Commission notes that website disclosure of the portfolio composition of the Funds will occur at the same time as the disclosure by the Funds of the portfolio composition to Authorized Participants so that all market participants are provided portfolio composition information at the same time. In addition, if the Exchange becomes aware that the NAV with respect to the Shares is not disseminated to all market participants at the same time, the Exchange will halt trading in the Shares until such time as the NAV is available to all market participants. Further, the Exchange may halt trading during the day in which an interruption to the dissemination of the IOPV, the value of an Index, the VIX, or the value of the underlying VIX Futures Contracts occurs. If an interruption to the dissemination of the IOPV, the value of an Index, the VIX, or the value of the underlying VIX Futures Contracts persists past the trading day in which it occurred, the Exchange will halt trading no later than the beginning of the trading day following the interruption.<sup>16</sup> Trading in the Shares will be subject to NYSE Arca Equities Rule 8.200, Commentary .02(e), which sets forth certain restrictions on Equity Trading Permit (“ETP”) Holders acting as registered Market Makers in Trust Issued Receipts to facilitate surveillance. The Exchange represents that Standard & Poor’s Financial Services LLC, the index sponsor with respect to the Indexes, is not a broker-dealer and has implemented procedures designed to prevent the use and dissemination of material, non-public information regarding the Indexes.

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<sup>16</sup> Trading may also be halted because of market conditions or for reasons that, in the view of the Exchange, make trading in the Shares inadvisable. These may include: (1) the extent to which trading is not occurring in the underlying futures contracts; or (2) whether other unusual conditions or circumstances detrimental to the maintenance of a fair and orderly market are present.

The Exchange further represents that the Shares are deemed to be equity securities subject to the Exchange's existing rules governing the trading of equity securities. In support of this proposal, the Exchange has made additional representations, including:

- (1) The Funds will meet the initial and continued listing requirements applicable to Trust Issued Receipts in NYSE Arca Equities Rule 8.200 and Commentary .02 thereto.
- (2) The Exchange has appropriate rules to facilitate transactions in the Shares during all trading sessions.
- (3) The Exchange's surveillance procedures are adequate to properly monitor Exchange trading of the Shares in all trading sessions and to deter and detect violations of Exchange rules and applicable federal securities laws. In addition, with respect to any Fund's holdings of futures contracts traded on exchanges, not more than 10% of the weight of such futures contracts in the aggregate shall consist of components whose principal trading market is not a member of the Intermarket Surveillance Group or is a market with which the Exchange does not have a comprehensive surveillance sharing agreement.
- (4) Prior to the commencement of trading, the Exchange will inform its ETP Holders of the suitability requirements of NYSE Arca Equities Rule 9.2(a) in an Information Bulletin. Specifically, ETP Holders will be reminded in the Information Bulletin that, in recommending transactions in the Shares, they must have a reasonable basis to believe that (a) the recommendation is suitable for a customer given reasonable inquiry concerning the customer's investment objectives, financial situation, needs, and any other information known by such

member, and (b) the customer can evaluate the special characteristics, and is able to bear the financial risks, of an investment in the Shares. In connection with the suitability obligation, the Information Bulletin will also provide that members must make reasonable efforts to obtain the following information: (i) the customer's financial status; (ii) the customer's tax status; (iii) the customer's investment objectives; and (iv) such other information used or considered to be reasonable by such member or registered representative in making recommendations to the customer. In addition, the Information Bulletin will reference the FINRA Regulatory Notices regarding sales practice and customer margin requirements implemented by FINRA, applicable to FINRA members, with respect to leveraged ETFs (which include the Shares) and options on leveraged ETFs.<sup>17</sup> ETP Holders that carry customer accounts will be required to follow the FINRA guidance set forth in these notices.

- (5) Prior to the commencement of trading, the Exchange also will inform its ETP Holders in an Information Bulletin of the special characteristics and risks associated with trading the Shares. Specifically, the Information Bulletin will discuss the following: (a) the risks involved in trading the Shares during the Opening and Late Trading Sessions when an updated IOPV will not be calculated or publicly disseminated; (b) the procedures for purchases and redemptions of Shares in Creation Baskets and Redemption Baskets (and that Shares are not individually redeemable); (c) NYSE Arca Equities Rule 9.2(a), which imposes a duty of due diligence on its ETP Holders to learn the essential facts relating to every customer

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<sup>17</sup> See FINRA Regulatory Notices 09-31 (June 2009), 09-53 (August 2009) and 09-65 (November 2009) ("FINRA Regulatory Notices").

prior to trading the Shares; (d) the requirement that ETP Holders deliver a prospectus to investors purchasing newly issued Shares prior to or concurrently with the confirmation of a transaction; and (e) trading information.<sup>18</sup>

- (6) The Funds must be in compliance with NYSE Arca Equities Rule 5.3 and Rule 10A-3 under the Act.<sup>19</sup>
- (7) A minimum of 100,000 Shares for each Fund will be outstanding as of the start of trading on the Exchange.

This approval order is based on the Exchange's representations.<sup>20</sup>

For the foregoing reasons, the Commission finds that the proposed rule change is consistent with Section 6(b)(5) of the Act<sup>21</sup> and the rules and regulations thereunder applicable to a national securities exchange.

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<sup>18</sup> As noted above, the Information Bulletin will further advise ETP Holders that FINRA has implemented increased customer margin requirements applicable to leveraged ETFs (which include the Shares) and options on leveraged ETFs, as discussed in the FINRA Regulatory Notices. See supra, note 17.

<sup>19</sup> 17 CFR 240.10A-3.

<sup>20</sup> The Commission notes that it does not regulate the market for futures in which the Fund plans to take positions, which is the responsibility of the Commodity Futures Trading Commission ("CFTC"). The CFTC has the authority to set limits on the positions that any person may take in futures. These limits may be directly set by the CFTC or by the markets on which the futures are traded. The Commission has no role in establishing position limits on futures, even though such limits could impact an exchange-traded product that is under the jurisdiction of the Commission.

<sup>21</sup> 15 U.S.C. 78f(b)(5).

IV. Conclusion

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Act,<sup>22</sup> that the proposed rule change (SR-NYSEArca-2011-23) be, and it hereby is, approved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>23</sup>

Elizabeth M. Murphy  
Secretary

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<sup>22</sup> 15 U.S.C. 78s(b)(2).

<sup>23</sup> 17 CFR 200.30-3(a)(12).