

August 17, 2015

Submitted via electronic filing: <https://www.sec.gov/rules/other.shtml>

Mr. Brent J. Fields  
Secretary  
U.S. Securities and Exchange Commission  
100 F Street, NE  
Washington, DC 20549

Re: Exchange-Traded Products, Release No. 34-75165; File No. S7-11-15  
Request for Comment on Exchange Traded Products

Dear Mr. Fields:

This letter responds to the request of the Securities and Exchange Commission (the "Commission") for comment on topics related to the listing and trading of exchange-traded products ("ETPs") on national securities exchanges and other matters discussed by the Commission in the above-referenced release ("Release"). We commend the Commission for seeking information and views from members of the public about the use of ETPs as widespread investment options for all segments of the marketplace. We believe that ETPs have found a well-deserved place in the investment strategies of many investors, and that they have a favorable impact on the securities markets. We have found, however, that confusion about the specific regulatory structure of various exchange-traded products has been experienced by both retail investors and investment professionals, that is, which products are classified as ETFs, ETNs, ETCs and ETPs. This is important, because a product's regulatory structure drives many of its investment characteristics, such the tax treatment of its profits and losses. Therefore, our comments discuss the nature and specifics of this confusion, as well as propose a classification system to help prevent confusion in the future.

Here is a simple example of how this confusion permeates the ETP industry. The Release states that "[a]s of December 31, 2014, there were 1,664 U.S.-listed ETPs, and they had an aggregate market capitalization of just over \$2 trillion"<sup>1</sup> However, the ETFGI<sup>2</sup> US ETF and ETP industry insights report dated December 2014, published on January 14, 2015, stated that the US ETF industry had 1,377 ETFs with assets of \$US 1.918 Trillion, and that the US ETF/ETP industry had 1,662 ETFs/ETPs with assets of US

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<sup>1</sup> See, footnote 4 of the Release.

<sup>2</sup> ETFGI LLP has produced data and research on the global ETF and ETP industry since 1997 when there were only 21 ETFs with assets of just US\$ 8 billion. See, <http://www.etfgi.com/index/home>.

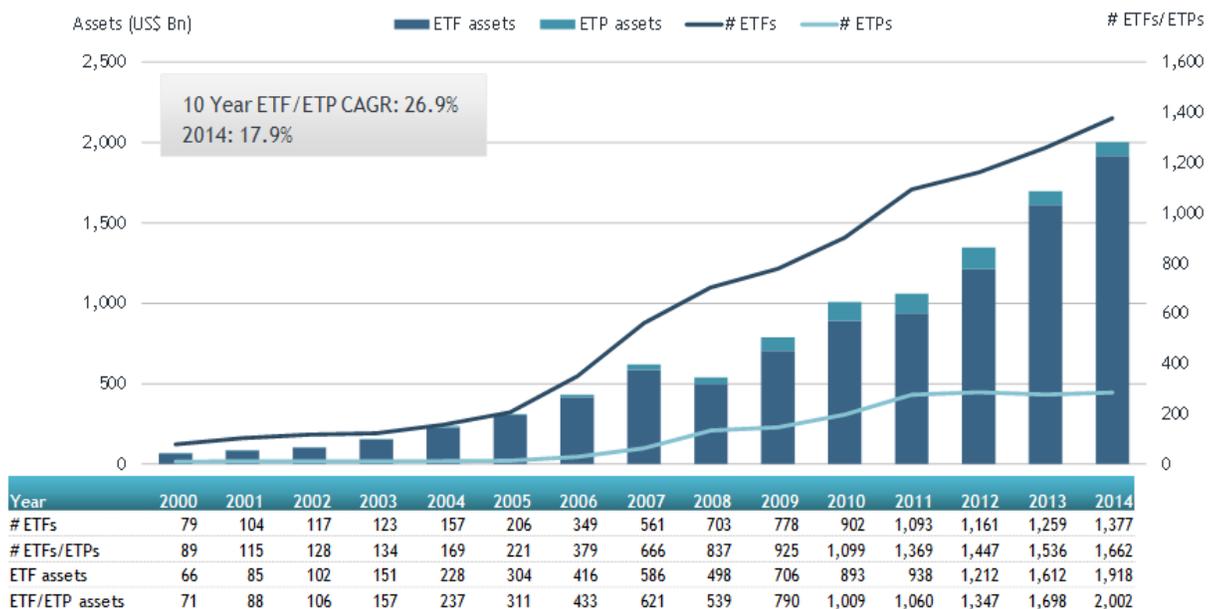
\$2.002 trillion.<sup>3</sup> It appears that the Commission characterized two additional products as ETPs than did ETFGI.

A variety of reasons contribute to this general confusion. These include

1. Websites, advertising and sales literature that do not always clearly identify a product's regulatory structure;
2. News articles and industry commentary that do not mention, or are not clear about, the regulatory structure of a product being described to the general public;
3. Vague or ambiguous labelling that does not state clearly the regulatory structure of a product;
4. References made to a product identifying its tax structure rather than its regulatory structure (e.g., "grantor trust") and
5. "Formal" names of ETPs that are either ambiguous or provide no insight as to a product's regulatory structure. Here are some examples :
  - ◆ *SPDR Gold Trust* is sometimes described as an "ETF" even though it holds physical bullion, not securities, and therefore cannot register as a "fund" (i.e., an investment company under the Investment Company Act of 1940 ("1940 Act"))<sup>4</sup>;
  - ◆ *CurrencyShares Euro Trust* is sometimes accurately described as a "grantor trust", but this tax label does not indicate its regulatory structure<sup>5</sup>;

<sup>3</sup> Source: [www.etfgi.com](http://www.etfgi.com) ETFGI US ETF and ETP industry insights report December 2014 published on January 14, 2015. ETFGI data sourced from ETF/ETP sponsors, exchanges, regulatory filings, Thomson Reuters/Lipper, Bloomberg, publicly available sources and data generated in-house. Note: "ETFs" are typically open-end index funds that provide daily portfolio transparency, are listed and traded on exchanges like stocks on a secondary basis as well as utilising a unique creation and redemption process for primary transactions. "ETPs" refers to other products that have similarities to ETFs in the way they trade and settle but they do not use a mutual fund structure. The use of other structures including grantor trusts, partnerships, notes and depositary receipts by ETPs can create different tax and regulatory implications for investors when compared to ETFs which are funds.

At the end of December 2014, the US ETF industry had 1,377 ETFs, assets of US\$1.918 trillion, from 56 providers on 3 exchanges. At the end of December 2014, the US ETF/ETP industry had 1,662 ETFs/ETPs, assets of US\$2.002 trillion, from 71 providers on 3 exchanges.



<sup>4</sup> See, <http://www.statestreetspdrs.com/precise/files/Asset/SPDRGoldTrustProspectus.pdf>

<sup>5</sup> See, <https://currencyshares.com/products/fxe>.

- ◆ *United States Oil Fund* has been can be accurately described as a “limited partnership, but this tax label does not indicate its regulatory structure<sup>6</sup>;
- ◆ *AccuShares Spot CBOE VIX Down Shares* holds neither a portfolio of assets or securities (only collateral) and its name does not indicate its regulatory structure<sup>7</sup>;
- ◆ *First Trust Brazil AlphaDEX Fund* holds a portfolio of international securities, but its name does not indicate that it is an ETF<sup>8</sup>; and
- ◆ *PowerShares S&P 500 ex-Rate Sensitive Low Volatility Portfolio* holds a portfolio of securities, but its name does not indicate that it is an ETF<sup>9</sup>.

Currently, there are no standardized terms that can be applied to the general and specific types of exchange-traded instruments that are discussed in the Release. The Commission could directly require that one or more solutions to this confusion be implemented; however, these solutions would suffice only to the extent that the problems are caused by ETP issuers, broker-dealers and other securities industry participants subject to Commission jurisdiction. Such solution(s) would not be binding upon members of the press, the general public, commentators, authors, and others not subject to regulation by the Commission.

Therefore, we recommend the following remedial actions that would affect all ETP industry participants alike, including sellers, buyers, commentators, research providers and members of the media:

1. Establishing a standardized list and definitions of product designations and acronyms to be used by all issuers; and
2. Requiring that each issuer include the appropriate designation in the formal name of its product, including in the prospectus.

We believe that this solution will, in effect, provide control to the Commission over all uses of product designations by requiring the formal product name to include the appropriate designation or acronym. We note, however, that the use of the product designation in the formal name of an ETF (defined below) should not be subject to Rule 35d-1 under the 1940 Act (commonly referred to as the “names rule”). We also note that some products currently use their appropriate regulatory structure or its acronym in their formal product name (see examples below).

We believe that the standardized list and definitions of product designations and acronyms should be established and used by all issuers and securities industries professionals. There is more than one methodology that can be used to construct this remedy; we offer our recommendations below as one example of how the remedial actions could be accomplished:

*First*, the generic designation describing the entire class of exchange-traded products discussed in the Release should be termed “*Exchange-Traded Investments*” or “*ETIs*”.

*Second*, every *ETI* must be:

- i. A “security”, as defined in Section 2(a)(1) of the Securities Act of 1933 (“1933 Act”) in the form of a share, note, certificate of interest or other financial instrument;
- ii. Registered with the Commission
  - (x) for offer and sale to the public under Section 5 of the 1933 Act and
  - (y) for trading in the secondary market under Section 12 of the Exchange Act of 1934 (“1934 Act”);

<sup>6</sup> See, <http://www.sec.gov/Archives/edgar/data/1327068/000119312512265421/d335842d424b3.htm>.

<sup>7</sup> See, <http://www.accushares.com/products/vxdn-vix-down-class/prospectus>

<sup>8</sup> See, <http://www.ftportfolios.com/LoadContent/gw4uoqjigr>.

<sup>9</sup> See, <http://hosted.rightprospectus.com/PowerShares/Fund.aspx?cu=73937B563&dt=P&ss=ef>.

- iii. Listed for trading on a “national securities exchange” registered with the Commission under Section 6 of the 1934 Act at current intraday market prices and *not at NAV*;
- iv. Structured with an “arbitrage mechanism” provided by the potential issuance and redemption at NAV by its issuer at the end of each trading day (except for temporary periods occasioned by extra-ordinary circumstances); and .
- v. Supported by more than one market participant (e.g, one market maker and at least one other Authorized Participant).

We note that the proposed generic term “Exchange-Traded Instruments” or “ETIs” (in lieu of ETPs) currently includes 4 distinct types of exchange traded product structures:

1. “Exchange-traded Funds” or “ETFs”;
  - a. Index (or passive) ETFs could be labelled ETFI; and
  - b. Actively managed ETFs could be labelled ETFAs.
2. “Exchange-traded Portfolios” or “ETPs”;
3. “Exchange-traded Commodity Pools” or “ETCs”; and
4. “Exchange-traded Notes” or “ETNs”.

We recommend continuing the use of these categories because they are known to most participants in the ETI marketplace.

*Third: Proposed Definition of an “Exchange-Traded Fund” or “ETF”.* Every ETF must be:

1. A special purpose pooled vehicle structured either as a unit investment trust (“UIT”) or open-end fund (“open-end”) registered as an investment company under Section 8 of the 1940 Act;
2. The issuer of units, shares or interests registered with the Commission for sale under the 1933 Act representing interests in its underlying pool of assets (i.e., provides an “equity stake” in the pool);
3. That passively or actively manages its pooled assets, which are primarily “securities” as defined in Section 2(a)(36) of the 1940 Act;
4. That typically
  - (i) elects to be treated as a “regulated investment company” or a “RIC” under Subchapter M of the Internal Revenue Code; or
  - (ii) is structured as a grantor trust; or
  - (iii) is structured as a limited partnership or another type of tax pass-through arrangement; and
5. Usually has no stated maturity date.

Examples include:

- “SPDR S&P 500 ETF” (UIT/ index /equity portfolio/ RIC);
- “ENHANCED SHORT MATURITY STRATEGY FUND “open-end /active /bond portfolio/ RIC);
- “ULTRAPRO DOW 30”(open-end/ leveraged/ index equity & derivatives portfolio/ RIC);
- “ISHARES S&P 500 INDEX FUND (open-end/ index/ equity portfolio/ RIC);
- “FIRST TRUST TECHNOLOGY AlphaDEX FUND ”(open-end/ index/ equity portfolio/ RIC);
- “ADVISOR SHARES PERITUS HIGH YIELD ETF” (open-end/ active/ debt portfolio/RIC);and
- “POWERSHARES SENIOR LOAN PORTFOLIO”( open-end/ index/ debt portfolio/RIC.

*Fourth: Definition of an “Exchange-Traded Portfolio” or “ETP”.* Every ETP must be:

1. A special purpose pooled vehicle structured as a trust, partnership or another arrangement designed to hold pooled assets such as currencies, precious metals, other physical and intangible commodities, and assets (collectively, "Assets");
2. That is not registered as an investment company under the 1940 Act;
3. Whose units, shares or interests registered under the 1933 Act represent interests in its underlying pool of Assets (i.e., an "equity stake" in the pool);
4. That either passively or actively manages its pooled Assets;
5. Typically elects to be considered
  - (i) a grantor trust,
  - (ii) a partnership, or
  - (iii) another type of tax pass-through arrangement;
6. Is not operated by a commodity pool operator registered with the National Futures Association ("CPO");and
7. Typically has no stated maturity date.

Examples include:

- "GUGGENHEIM CURRENCYSHARES CHINESE RENMINBI TRUST"(currency/passive/grantor trust);
- "SPDR Gold Trust"(gold bullion/passive/grantor trust)

**Fifth:** Definition of an "Exchange-Traded Commodity Pool" or "ETC". Every ETC must be:

1. A special purpose pooled vehicle structured as a trust, partnership or another arrangement that meets the definition of a "commodity pool" under Section 1(a)(10) of the Commodity Exchange Act ("CEA");
2. Designed to principally trade "commodity interests" as defined in Section 1.3 (yy) of the CEA;
3. Operated by a commodity pool operator or advised by a "commodity trading adviser"("CTA") as such terms are defined in Sections 1(a)(11) and 1(a)(12), respectively of the CEA;
4. Not registered under the 1940 Act as an investment company;
5. The issuer of units, shares or interests registered under the 1933 Act which represent interests in its underlying pool of commodity interests(i.e., provides an "equity stake" in the pool);
6. Whose tax treatment varies depending in part upon the type of asset being tracked and
7. Typically has no stated maturity date.

Examples include:

- "UNITED STATES NATURAL GAS FUND LP" (commodity pool/ natural gas futures /index/ taxable as a corporation)
- "DB COMMODITY INDEX TRACKING FUND"(commodity pool/ various commodity futures/ index/ classified as a partnership for tax purposes)
- "NUVEEN LONG/SHORT COMMODITY TOTAL RETURN FUND"(commodity pool/ various commodity futures and options contracts/ index/ classified as a partnership for tax purposes)
- "PROSHARES ULTRA BLOOMBERG CRUDE OIL" (commodity pool/ futures, swaps forwards etc/ daily 2x leverage of index/ classified as a partnership for tax purposes)

**Sixth:** Definition of an "Exchange Traded Note" or "ETN". Every ETN must be:

1. A structured note issued by a financial institution as an unsecured debt instrument and registered with the Commission for sale under the 1933 Act;

2. Which has no underlying pool of assets (i.e., there is no equity stake);
  3. Exposes holders to the credit risk of its financial institution issuer;
  4. Which is designed to pay a return based on the performance of a specified “reference asset”(such as an asset, market index or benchmark, or other investment strategy),
  5. Is not registered under the 1940 Act as an investment company;
  6. Nor is operated by a CPO or advised by a CTA;
  7. Whose tax treatment varies depending upon the type of asset being tracked; and
  8. Has a stated maturity date.
- i. NB. Items iv and v above apply equally to ETNs; that is, if the issuer of an ETN stops issuing new units of the product, it should no longer be considered an ETN.

Examples include:

- o “VELOCITYSHARES 3X INVERSE CRUDE OIL ETN”;
- o -“IPATH EUR/USD EXCHANGE RATE ETN”, and
- o “UBS AG EXCHANGE TRADED ACCESS SECURITIES”.

*Seventh*, we also propose that there should be a hierarchy that identifies the following: Index or Active. Active would encompass “less-transparent active ETIs if/when the Commission permits such products. We believe that the term “non-transparent active” is misleading because if this type of ETI were approved, it would provide portfolio transparency as frequently as a mutual fund.

Followed by Asset Class:

Equity;  
 Fixed Income;  
 Commodity;  
 Currency;  
 Alternative;  
 Mixed;

Followed by Benchmark: identify the name of the specific benchmark the ETI is designed to track, and then the type of benchmark: marketcap, price, equal weight, min vol, etc. For example, there is a need to create a standard industry definition as to what a “Smart Beta” index is, and further it should be noted that it is an Index ETI.

Followed by Replication type:

Fully replicating; or  
 Optimized

*Eighth*, we also suggest that when a new ETI is listed, its issuer should provide to the listing exchange, and such exchange should post on a free public website , a document that describes the ETI including the legal, tax structure and all characteristics of the product.

This proposed document (“product alert”) would include the following details specified below.

Description: The xxx ETI is a 1940 Act regulated exchange-traded fund incorporated in the USA. The Fund seeks investment results that correspond to the performance of the xxx Index.

Security Details

Select one: Index or Active

Exchange Listed

Trading Currency USD

Hedged

Expense ratio (bps)

Share price

NAV

Dividend Frequency Quarterly

Legal Structure Open Ended Fund 1940 Act registered

Tax Structure

Provider

Exchange

Listing Date

Issuer:

Issuer address and phone number

Portfolio manager (s)

Index Provider

Custodian

Law firm

Accounting firm

Replication Type Physical

Replication Method Stocks

Replication Style Optimized

Engage in Securities Lending Yes

Market Makers

Authorized participants

Identifiers:

Bloomberg Price Ticker:

Bloomberg NAV Ticker:

Bloomberg iNAV Ticker:

Bloomberg Index Ticker:

Reuters Price Ticker:

Reuters NAV Ticker:

Reuters iNAV Ticker:

Reuters Index Ticker:

ISIN:

SEDOL:

CUSIP:

Classification:

Asset Class:

Region Exposure:

Country Exposure:

Sector Exposure:

Market Type:

Currency Hedged:

Leverage Type:

Value/Growth:

Dividend/Earnings:  
Actively Managed:  
Socially Responsible:  
Smart Beta:

Provider website  
Exchange website  
Index Provider website  
Regulator website

Detailed holdings analysis

In addition, whenever there is a change to any of the items listed above, the issuer must provide such information in an updated version of the “product alert”, to the listing exchange which will post and disseminate such update on a free public website .

Finally, we suggest that there should be a daily detailed holdings analysis. ETI issuers directly or through their custodians should provide for free in an industry standard format the daily portfolio composition files to research firms, Lead Market Makers and Authorized Participants.

As discussed above, we believe that the ETI industry is sound and beneficial to many investors for many purposes. We thank the Commission for providing us with an opportunity to provide comments on the Release, and we would be happy to provide more information or a more detailed description of our proposed remedy to alleviate industry confusion. Please do not hesitate to contact one or both of us if you have any questions or comments.

Sincerely,

Deborah Fuhr

Managing Partner

ETFGI LLP

60 Gresham Street

London, EC2V 7BB United Kingdom

Mobile [REDACTED]  
[REDACTED]

Kathleen H. Moriarty

Partner

Kaye Scholer LLP

250 West 55th Street | New York, New York 10019-9710

T: [REDACTED] | F: [REDACTED]

[REDACTED] | [www.kayescholar.com](http://www.kayescholar.com)