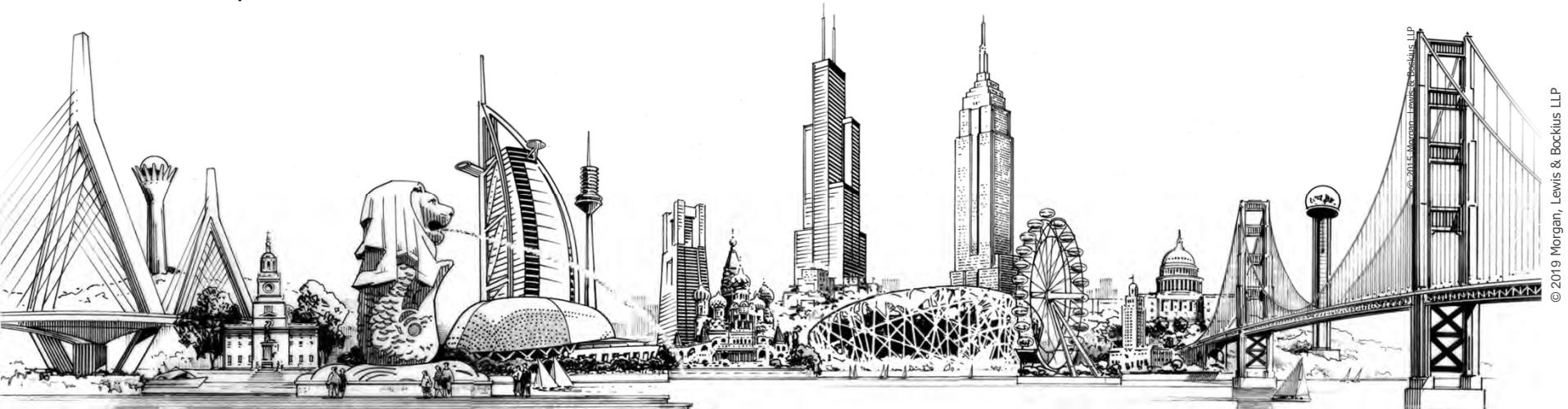


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THE NEW ETF RULE

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Overview of the Rule and Our Presentation

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Effective Date and Phase-In; Effect on Existing Orders

- Adopted: September 25, 2019
- Published in Federal Register: October 24, 2019
- Effective Date: December 23, 2019 (60 days after publication)
- Compliance Date: December 22, 2020 (one year after effective date)
- Existing orders will be rescinded (caveat for fund-of-funds relief)
- SEC staff requesting that pending applications be withdrawn

ETFs Eligible to Rely on the Rule

- Available to certain ETFs organized as “open-end” companies
- Not available to unit investment trusts (e.g., SPDR S&P 500 ETF)
- Not available to leveraged or inverse ETFs
- Not available to ETFs structured as share class of a multi-class fund
- Not available to non-transparent or semi-transparent ETFs
- Not applicable to ETPs that are not subject to the 1940 Act (e.g., currency funds, commodity pools, physical metals funds)

Treatment of Passive and Actively-Managed ETFs

- Unlike exemptive orders, the Rule makes no distinction between these two types of ETFs
- Passive ETFs will not have to track a “securities-based” index
- Passive ETFs will not have to invest at least 80% of their total assets in index components (be mindful of “names rule” issues though)
- Actively-managed ETFs will have the ability to use custom baskets to manage portfolio trades
- All ETFs relying on the Rule will have to be fully transparent, a change for certain passive ETFs

Self-Indexing ETFs

- What is a self-indexing ETF?
- How, if at all, does the Rule address self-indexing ETFs?
 - Rules-based index
 - Provide the index at no cost to the ETF
 - Firewalls – generic listing rules

Conditions: Website Disclosure - Overview

- Portfolio holdings information
- NAV calculation and the disclosed portfolio
- Daily ETF metrics
- Median bid/ask spread

Conditions: Website Disclosure – Portfolio Holdings

- ETFs relying on the Rule must be fully transparent
- Holdings information must be posted before the open of trading on the exchange
- What holdings information must be disclosed?
- How does the final Rule differ from the proposed Rule?
- Are an ETF's baskets required to be disclosed on the website? What about the "cash balancing amount"?

Conditions: Website Disclosure – NAV Calculation

- The portfolio holdings that form the basis for the next calculation of NAV must be the ETF's holdings as of the close of business on the prior business day
- This effectively means that ETFs relying on the Rule will use T+1 accounting
- Effect on ETFs that strike a NAV more than once per day?

Conditions: Website Disclosure – Daily ETF Metrics

- NAV per share as of end of prior business day
- Market price as of end of prior business day
- Premium or discount to NAV as of end of prior business day
 - “Premium or discount” definition
 - Table, most recently completed calendar year and calendar quarter(s) since that year (or life of ETF if shorter)
 - Line graph, most recently completed calendar year and calendar quarter(s) since that year (or life of ETF if shorter)
 - Narrative disclosure if premium or discount is greater than 2% for more than 7 consecutive business days
- What about Intra-Day Indicative Value (aka IIV, iNAV, IOPV)?

Conditions: Website Disclosure – Median Bid/Ask Spread

- What is the bid/ask spread?
- Show the median bid/ask spread over a rolling 30-calendar-day period (instead of for the last fiscal year as proposed)
- Use NBBO to calculate the median
 - SEC expects this to promote uniformity
- Eliminated the requirement to have an interactive active calculator on the website designed to allow investors to customize hypothetical bid/ask spread calculations to their specific investing situation

Prospectus Disclosure Requirements

- Apply to all ETFs, not just those relying on the Rule
- Narrative disclosures
 - Streamlined and moved after fee table
 - Added a requirement to disclose that an investor may incur bid/ask spread costs when buying or selling shares in the secondary market
 - Eliminated the proposed Q&A requirement in the fee table section
- Quantitative disclosures
 - Median bid/ask spread for most recently completed fiscal year, unless the ETF is following the Rule's website disclosure requirements
 - Historical premium and discount information in both annual reports and prospectuses, unless the ETF is following the Rule's website disclosure requirements
- Eliminated requirements to specify the number of shares in a creation unit and to make fuller disclosure if the ETF's creation unit size is less than 25,000 shares

Conditions: Basket Construction Procedures

- What is a “basket” and what is a “custom basket” under the Rule?
- Rule levels the playing field for actively-managed ETFs, as compared to passive ETFs
- SEC concerns about baskets – dumping and cherry-picking
- General basket construction procedures
 - Govern the construction of baskets and the process used for acceptance of baskets
 - Non-pro rata baskets (e.g., omitting positions, representative sampling, index rebalancings)

Conditions: Custom Basket Construction Procedures

- May use “custom baskets” if policies and procedures :
 - i. set forth detailed parameters for the construction and acceptance of custom baskets (methodology) and describe ETF’s approach for testing compliance with these policies to be in the best interest of the ETF and its shareholders; and
 - ii. specify the titles or roles of employees of the ETF’s investment adviser who are required to review each custom basket for compliance.
- ETFs should establish a process for making any revision to, or deviation from, these parameters
- Procedures should include reasonable controls designed to prevent inappropriate differential treatment among APs

Odds and Ends

- T-1 Orders
- Creation Unit Sizes
- Corporate Events
- Exchange-Listed Requirement
- Fund-of-Funds Exemptive Relief
- Board Responsibilities

Exemptive Relief Provided by the Rule

- Shares Trade at Market Prices
 - Exemptions from Section 22(d) of the 1940 Act and Rule 22c-1 thereunder to permit secondary market trading of ETF shares at market-determined prices
- Affiliated Transactions
 - Exemptions from Sections 17(a)(1) and (a)(2) of the 1940 Act with regard to the deposit and receipt of baskets by a person who is an affiliated person of an ETF because of 5% ownership of the ETF's voting securities, or 5% ownership of an affiliated ETF's voting securities
- Additional Time for Delivering Redemption Proceeds
 - Exemption from Section 22(e) of the 1940 Act permits an ETF to delay redemptions up to 15 days (but, as soon as practicable) for foreign issuers that trade outside the U.S. when foreign jurisdictions make delivery infeasible (e.g. local market holiday)
 - Proposal included a ten-year sunset, which was discarded in the final Rule
- ETFs are "open-end" companies under Section 5(a)(1) of the 1940 Act and ETF shares are "redeemable securities" within the meaning of Section 2(a)(32) of the 1940 Act
 - Allowing ETF shares to fit exemptions for "redeemable securities" under Reg M, Rule 10b-17 under the Exchange Act, and for ETFs to fit Rule 11d1-2 under the Exchange Act
 - Applies to all ETFs, not just those that fit the Rule

Capital Markets Considerations and Exchange Act Relief

- The SEC separately published relief under the Exchange Act for broker-dealers with respect to ETFs relying on the Rule
- Section 11(d)(1) (margin/credit on new issuances) and Rule 11d1-2
- Rule 10b-10 (confirms)
- Rules 15c1-5 and 15c1-6 (disclosure of control relationship with issuer and disclosure of participation/interest in distribution)
- Rule 14e-5 (transacting in securities subject to a tender offer)

Capital Markets Considerations and Exchange Act Relief

- More ETFs will come to market (some from new sponsors) because the Rule reduces timing and price barriers
- Wider use of custom baskets will become consistent over time as market practices develop among applicable ETFs
 - ETFs may seek input from APs while designing and implementing procedures
- Underwriter status and affiliated person issues remain
- AP agreements and procedural infrastructure will largely continue as-is
- ETFs may seek input from APs and market makers to meet premium/discount website disclosure requirements

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John McGuire counsels clients on investment company and investment adviser regulatory issues and related issues affecting broker-dealers and transfer agents. He also assists clients with forming and acquiring investment companies and investment advisers. John routinely handles matters involving the establishment, representation, and counseling of exchange traded investment companies (ETFs), their advisers, and listing markets.

Additionally, John advises clients on regulatory and transactional matters, including development of new products and services; federal and state registration and compliance issues; Securities and Exchange Commission (SEC), FINRA, and state investigations and enforcement actions; mergers and acquisitions involving investment companies and investment advisers; interpretive and “no-action” letter requests; SEC exemptive orders; and related matters. John previously worked on some of the key ETF legal milestones, including the first fixed-income ETFs, the first 12(d)(1) relief for ETFs, actively managed ETFs, leveraged and inverse ETFs, and the first ETF in a master-feeder structure.

Before entering private practice, John served on the staff of the SEC in its Investment Management Division. He regularly speaks at industry conferences and has authored or co-authored several articles covering a wide variety of securities regulatory issues and the books *Mutual Fund Regulation and Compliance Handbook* and *Regulation of Exchange-Traded Funds*.

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Chris regularly counsels clients on organizing, registering and operating investment companies. He assists investment companies and their advisers with the development of new products and services, the design of compliance programs, and the structure and negotiation of mergers and acquisitions. He works with regulators on behalf of his clients to obtain interpretive and “no-action” guidance as well as exemptive relief. He also advises boards of directors, including independent directors, on their duties under federal and state law. His clients include passive and active ETFs, multiple series and multi-class funds, funds of funds, manager of managers funds, alternative strategy funds and insurance-dedicated funds.

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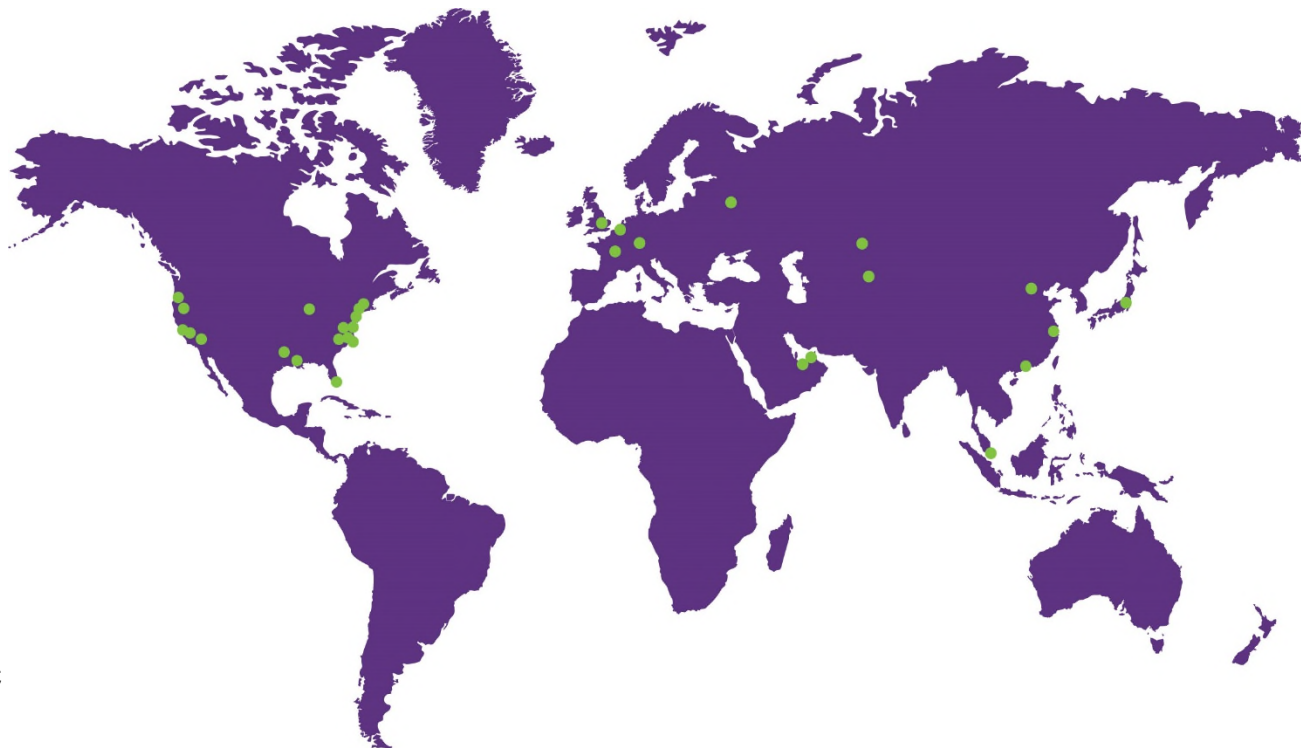
Jack O'Brien counsels registered and private funds and fund managers in connection with organizational, offering, transactional, and compliance matters. He regularly works with a variety of different fund structures, including open-end and closed-end funds, exchange-traded funds, and hedge funds. He also counsels investment adviser and broker-dealer clients on various matters, particularly with respect to registration and disclosure, marketing regulations, pay-to-play issues, and transactions in exchange-traded funds.

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