October 1, 2018

Via Electronic Submission

rule-comments@sec.gov
Brent J. Fields, Secretary
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: File No. S7-15-18
Comments on Proposal Related to Exchange-Traded Funds

Dear Mr. Fields:

WisdomTree Asset Management, Inc. ("WisdomTree") appreciates the opportunity to submit comments to the Securities and Exchange Commission (the "SEC" or "Commission") on its recent proposed Rule 6c-11 (the "Proposed Rule") under the Investment Company Act of 1940 (the "Investment Company Act") that would enable exchange-traded funds ("ETFs") that satisfy certain conditions to operate without obtaining an exemptive order under the Investment Company Act.[1] WisdomTree is currently the 7th largest sponsor of ETFs in the United States. WisdomTree helped to pioneer the concept of fundamentally weighted ETFs through proprietary methodologies, while also becoming a leader in emerging and frontier markets ETFs and foreign currency hedged ETFs, and introduced some of the first actively managed ETFs, including the industry's first managed futures ETF. These strategies, among others used by WisdomTree ETFs, evidence WisdomTree's innovation in ETFs. As a leader in establishing innovative ETFs, WisdomTree believes it has a unique perspective on the Proposed Rule.

WisdomTree strongly believes, and its ETFs have demonstrated, that ETFs provide significant benefits to investors by offering efficient investment options that do not pose excessive risks. ETFs have proliferated since first offered over 25 years ago. Further, the industry and investors have learned a great deal about these products, which has led to significant innovation and asset growth. The existing regulatory regime has not kept pace with such innovation and the wide variety of ETF strategies and investments, and, because of the piecemeal approach of granting individual exemptive orders, has led to inconsistent requirements among ETF sponsors. WisdomTree applauds the

[1] *Exchange-Traded Funds*, Investment Company Act Release No. 33140 (June 28, 2018) (the "Proposing Release").

Commission's effort to modernize the existing framework to keep pace with innovation in the industry.

I. Executive Summary

WisdomTree appreciates the Commission's efforts to eliminate unnecessary regulatory burdens on ETFs and is supportive of the effort to "create a consistent, transparent, and efficient regulatory framework for ETFs."[2] In particular, we strongly support the Commission's efforts associated with basket composition and flexibility, which facilitates management strategies that minimize transaction costs and enhance tax efficiency, among other benefits, which are in the best interests of shareholders. The comments below are designed to refine the Proposed Rule to make it even more effective in accomplishing its stated goals, including that of providing useful information to investors.

We summarize our key points below:

(1) The Proposed Rule is intended to create a more efficient regulatory framework by, among other things, (a) removing arbitrary distinctions between index-based and actively managed ETFs, (b) eliminating a requirement to disseminate intraday indicative values ("IIV"), (c) refraining from prescribing a specific basket size, and (d) providing a principles-based approach that allows all ETFs flexibility in basket composition, subject to appropriate policies and procedures. We agree that each of these efforts will be beneficial and represent a step forward.

However, certain of these requirements are reflected in relief obtained by ETFs under the Securities Exchange Act of 1934 (the "Exchange Act") and associated rules, as well as in exchange listing standards applicable to ETFs. The Proposing Release clarifies that a security issued by an ETF is a "redeemable security" for purposes of Regulation M under the Exchange Act, which provides some harmonization and is appreciated. However, until other remaining regulatory requirements stemming from the Exchange Act and exchange listing standards are made consistent with the standards set forth in the Proposed Rule, it will be impossible for the efficiencies discussed in the Proposing Release to be fully realized. The Commission should therefore take steps to facilitate consistent flexibility in these other regimes.

(2) An important policy concern underlying many aspects of the Proposing Release and the current operation of ETFs is transparency. WisdomTree agrees that transparency, in many respects, is useful and indeed necessary to promote efficient capital markets activities, and to provide important information to shareholders who purchase shares on the secondary market. Providing too much information, however, can sometimes be

[2] *Id.* at 6.

counterproductive and confusing to investors, and at the same time burdensome and costly for ETF sponsors to produce. We explain below that certain disclosure requirements included in the Proposed Rule would not be useful to investors and could potentially lead to confusion, such as the requirement to publish each basket and expanded bid-ask disclosure.

(3) The Proposed Rule would disproportionately and negatively impact ETFs holding foreign securities. First, the Proposed Rule's requirements requiring the publication of portfolio holdings and basket information in advance of order acceptance from an authorized participant would seem to preclude "T-1 orders," which have become commonplace for certain types of ETFs, particularly those ETFs investing in foreign securities, and are beneficial for investors, as further described below. Second, the Proposed Rule provides only temporary relief from Section 22(e) of the Investment Company Act on the assumption that settlement cycles are shortening worldwide. The Proposed Rule should eliminate the arbitrary sunset provision and instead leave the flexibility in place until such time as settlement cycles actually shorten sufficiently. Third, WisdomTree strongly believes that the continued imposition of a two percent limit on redemption fees is not beneficial for shareholders in ETFs that invest in foreign securities because of the potential for excessive dilution. These items should be revised or addressed, as applicable, in the final rule.

These and other comments are explained more fully below.

II. The Proposed Rule Effectively Eliminates Arbitrary Historical Distinctions and Other Operational Requirements, But to Fully Realize the Benefits of These Changes the Requirements for Relief Under the Exchange Act and Listing Standards Must Be Aligned with the Proposed Rule

A. The Distinction Between Index-Based and Actively Managed ETFs

As the sponsor of one of the first actively managed ETFs, WisdomTree understands the historical evolution that gave rise to the initial distinction between index-based and actively managed ETFs. WisdomTree has managed many index-based ETFs (particularly those using proprietary methodologies) since 2006 and actively managed ETFs since 2008. Our experience with these different types of ETFs informs our conclusion that, in many respects, ETFs operate similarly irrespective of whether they are index-based or actively managed. We further note that there were distinctions between those index-based ETFs that use third-party index providers and those, like many WisdomTree ETFs, that use affiliates to provide the indexes (known as "self-indexing"). The Proposing Release acknowledges that "some index-based ETFs with affiliated index providers are required to [provide portfolio transparency] pursuant to their exemptive orders . . . [and e]arlier relief granted to ETFs with affiliated index providers did not require full portfolio transparency, but included conditions that were intended to address potential conflicts of interest."[3] We strongly support the Commission's effort to eliminate the arbitrary distinctions between actively managed and index-based ETFs (self-indexed or otherwise), as WisdomTree believes that there is no benefit to shareholders associated with the varying conditions. However, like other ETF sponsors similarly situated, WisdomTree has experienced increased compliance costs associated with the different requirements. We therefore agree that this approach "would provide a level playing field among those market participants,"[4] and "would help to provide a more consistent and transparent regulatory framework for ETFs organized as open-end funds."[5]

The Commission sought comment on several aspects related to the potential separate treatment of index-based ETFs, ETFs with affiliated index providers, and actively managed ETFs. As noted above, WisdomTree agrees that there is no reason to maintain the historical distinctions between these types of ETFs. WisdomTree also does not believe it is necessary to maintain the requirement that index-based ETFs tie their portfolio composition to the index or that an index be securities-based. An index-based ETF is already, through the pursuit of its investment objective, inclined to hold a sizable percentage of its portfolio in securities included in its benchmark index, and an index-based ETF would similarly be inclined to hold other assets that may be included as part of a broader index composition under the Proposed Rule. Further, an ETF may be able to track its index more efficiently by holding similar or proxy instruments than by holding 80% of its assets in component securities. We also do not see the necessity for self-indexed ETFs to have information barriers in place. Advisers are already required to adopt policies designed to prevent portfolio information from being misappropriated.[6] Any additional requirements on index-based ETFs, regardless of whether the index provider is affiliated with the adviser, would perpetuate the distinctions between index-based and actively managed funds that the Commission has acknowledged serve no meaningful purpose.

B. Inconsistency between the Proposed Rule and Other Regulatory Requirements

While the Proposed Rule goes a long way towards streamlining regulatory requirements for ETFs generally, and achieving the goal of imposing consistent requirements for index-based and actively managed ETFs, the Proposed Rule fails to address the lingering requirements, including certain distinctions between actively managed and index-based ETFs, which are reflected in (i) the relief granted under the Exchange Act, as well as (ii) the requirements in the generic listing standards imposed by

[3] *Id.* at note 66.
[4] *Id.* at 26 (including within this discussion the removal of extra conditions that were imposed on ETFs with affiliated index providers (in earlier such orders) or full portfolio transparency (in later orders)).
[5] *Id.* at 27.
[6] *See* Section 204A of the Investment Advisers Act of 1940 and Rule 204A-1 thereunder.

the various exchanges (*i.e.*, NYSE Arca, Cboe BZX, and NASDAQ). Addressing these requirements and distinctions in related regulatory regimes would further the Commission's goal of facilitating consistency in the operation of these ETFs and reflect the Commission's findings that such conditions, while well-intended, actually serve no regulatory or meaningful investor protection purpose.

For example, the class relief letter issued to index-based ETFs addressing a number of rules under the Exchange Act would continue to require a minimum number of component securities in the applicable index, weighting requirements, component security liquidity thresholds, and a minimum basket size requirement, none of which appear in the Proposed Rule.[7] WisdomTree appreciates that the Proposed Rule makes Regulation M relief self-executing by stating unequivocally that ETF shares should be excepted from these rules as shares issued by open-end investment companies,[8] but relief under other Exchange Act rules would continue to be required.[9] The Commission should harmonize the conditions necessary for Exchange Act relief.

Further to this point, the Exchange Act relief, as well as various provisions of the listing requirements, treat index-based and actively managed ETFs differently. While the Proposed Rule eliminates distinctions between index-based ETFs that use a third-party index provider and those that are self-indexed, the listing requirements, if left unchanged, would continue to require self-indexed ETFs to maintain a "firewall" that separates index personnel and portfolio managers. The Proposing Release acknowledges that these distinctions serve no valid regulatory purpose, and therefore any differences in the way index-based and actively managed ETFs are treated either under the Exchange Act or in the listing standards should be eliminated, consistent with the Proposed Rule.

Similarly, the Proposed Rule eliminates the requirement imposed by exemptive orders that the IIV, the per share value of an ETF's portfolio holdings, be disseminated at least every 15 seconds throughout the trading day. As the Commission acknowledges, these values are of little utility to market making and other capital markets activity – market participants typically use their own proprietary models, and actual trading activity requires more frequent information. However, the ETF listing standards, if left unchanged, still would continue to require the IIV to be widely disseminated. WisdomTree agrees that the IIV dissemination requirement is not necessary and it

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[7] *See, e.g.*, Letter from Stuart M. Strauss, Clifford Chance US LLP, to James A. Brigagliano, Acting Associate Director, Office of Trading Practices and Processing, Division of Market Regulation (Oct. 24, 2006) (requesting exemptive, interpretive, or no-action relief from Rules 10a-1; 10b-17; and 14e-5; Rules 101 and 102 of Regulation M and Rule 200(g) of Regulation SHO, all promogulated under the Exchange Act).
[8] Proposing Release at 39.
[9] *See id.* (discussing the eligibility for a self-executing exemption in Regulation M, but not addressing Exchange Act Rule 14e-5 and Rule 200(g) of Regulation SHO (or other regularly requested relief noted in Proposing Release note 14)).

encourages the Commission to work with the exchanges expeditiously to revise their rules as well to eliminate any requirement to disseminate the IIV.

WisdomTree also agrees with the elimination of minimum creation unit requirements. Exemptive applications have historically included a representation that creation units will consist of large aggregations of shares (*e.g.*, 25,000 shares).[10] Although this minimum has been reduced to 10,000 shares in certain cases, the need for a minimum threshold was reinforced by additional disclosure required by Form N-1A if baskets consist of fewer than 25,000 shares.[11] The Proposed Rule does not include such a requirement nor do the proposed amendments to Form N-1A. WisdomTree agrees that impediments to smaller baskets should be eliminated because the liquidity of certain types of ETFs will benefit from smaller creation units. Specifically, smaller baskets may make it less expensive for authorized participants to provide liquidity, which serves to minimize bid-ask spreads and premiums/discounts. Nonetheless, such smaller baskets would not be consistent with Exchange Act class relief for at least some ETFs.[12] WisdomTree believes that the relief under the Exchange Act should be harmonized with the Proposed Rule in this respect as well.

C. Basket Flexibility

Basket flexibility is the clearest example of the disparate relief provided to market participants, which experience varying degrees of flexibility depending on when they obtained exemptive relief.[13] Recent exemptive orders have provided strict limitations on when creation and redemption baskets may deviate from each other or deviate from a *pro rata* representation of an ETF's portfolio. WisdomTree strongly agrees with the principles-based approach taken in the Proposed Rule that allows all ETFs flexibility in basket composition, subject to appropriate policies and procedures.

Custom baskets permit ETFs the flexibility for creation and redemption baskets to deviate from each other and from *pro rata* representation of the ETF's portfolio. Current requirements applicable to certain ETFs force such ETFs' portfolio managers to use cash to restructure portfolios; the flexibility incorporated into the Proposed Rule will enable the use of in-kind baskets for such ETFs to accomplish the same restructuring and thus will minimize transaction costs. In addition, the flexibility will enable portfolio managers to use the basket process to enhance tax efficiency. In both respects, the best interests of shareholders will be served.[14]

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[10] This number has varied across many different applications and has generally decreased in more recent applications.
[11] Form N-1A, Item 3 – Instruction 1(e)(ii), Item 6(c)(ii), Item 11(g), and Item 27 – Instruction 1(e)(ii).
[12] *See, e.g., supra* note 7.
[13] Proposing Release at 90 (discussing evolution of basket requirements over time).
[14] *See* Proposing Release at 92.

Under the Proposed Rule, custom basket flexibility is permitted if the ETF adopts policies and procedures that "set forth detailed parameters for the construction and acceptance of custom baskets that are in the best interests of the ETF and its shareholders."[15] This condition seems to be a reasonable means of ensuring that baskets are customized to advance shareholder interests instead of the interests of authorized participants.

However, the Proposed Rule also requires the policies and procedures to "specify the titles or roles of the employees of the exchange-traded fund's investment adviser who are required to review each custom basket for compliance with those parameters."[16] In our view, this requirement seems overly prescriptive. Further, it is not clear that a sub-adviser's personnel could fulfill this role under the Proposed Rule when such personnel may be most closely involved with basket construction, including custom baskets. An ETF's policies and procedures under Rule 38a-1 designate a chief compliance officer and are subject to a board's oversight. We believe that custom basket procedures should be subject to the same standards under Rule 38a-1 as any other policies and procedures and should not be singled out in this fashion. We therefore do not believe that the inclusion of such information is necessary.

III. The Disclosure Requirements Included in the Proposed Rule Should be Limited to Information that is Useful to Investors

The Proposing Release makes clear that transparency is essential to the efficient operation of ETFs. WisdomTree agrees that certain types of information serve the important purposes of informing investors about the nature of the ETF and the costs of trading ETF shares. However, WisdomTree believes that the disclosure requirements imposed by the Proposed Rule are broader than necessary to accomplish these goals, or are more appropriately sourced from broker-dealers (as applicable), and would impose unnecessary costs on ETF sponsors. Moreover, certain requirements are, in our view, counterproductive in that they may lead to investor confusion. We outline our specific concerns below.

A. Portfolio and Basket Transparency

The standard industry practice is for ETFs to disclose on their website a full schedule of portfolio holdings and the percentage of the ETF comprised by each security, on a daily basis. This information provides investors with a complete picture of how the ETF invests its assets and pursues its investment strategy. However, the Proposed Rule also would require an ETF to prominently disclose on its website the basket "that will apply to orders for the purchase or redemption of creation units each business day."[17] This information is not necessary for investors who are purchasing shares on the

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[15] Proposed Rule 6c-11(c)(3)(i)(A).
[16] Proposed Rule 6c-11(c)(3)(i)(B).
[17] Proposing Release at 88.

secondary market; it is information that is relevant to authorized participants and market makers. Moreover, the posted basket may differ from the current portfolio, which could create confusion for investors. This is particularly true if the ETF decides to use custom baskets on a particular day and therefore may be in the position of having to post numerous baskets. WisdomTree does not believe that daily transparency into basket activity serves any purpose for retail investors and simply adds information without a corresponding benefit. The Commission should therefore require basket transparency only for authorized participants that actually need the information in connection with legitimate capital markets activity.

Additionally, the Proposing Release states that the portfolio holdings information must be presented and contain the information prescribed by Article 12 of Regulation S-X. These requirements are applicable to fund financial statements. Article 12 generally requires for investments in securities of unaffiliated issuers the (i) name of issuer and title of issue, (ii) the balance held at the close of the period and the number of shares or principal amount, as applicable, and (iii) the value of each item at the close of the period. These items are generally innocuous, but footnotes embedded in these provisions require detailed categorization by investment type, industry, and country or geographic region. In addition, Article 12 requires that fair valued and non-income producing securities need to be identified. These more nuanced items are appropriate for financial statements. However, financial statements contain significant detail beyond what is necessary for investors to receive on a daily basis. While WisdomTree acknowledges that certain prescriptive information may be necessary, the level of detail requested is not warranted. WisdomTree therefore recommends that the daily portfolio holdings schedule be simplified to include the name of the security, the size of the positions, the percentage exposure to such security, and its value.

B. Bid-Ask Spread Disclosure

The Proposing Release includes revisions to Form N-1A that would require certain information about the bid-ask spread to be disclosed on the ETF’s website and in its prospectus. The Proposing Release seeks to amend Form N-1A to require disclosure of the “median bid-ask spread” for the most recent fiscal year and calculations showing the bid-ask spread impact for 25 “round trips” using the “mid-range spread cost” and the “high-end spread cost,” each as defined therein.[18] Form N-1A would also require disclosure directing investors to an ETF’s website, which would be required to post the ETF’s net asset value, market price, premiums and discounts, *and* an interactive calculator “to determine how the bid-ask spread would impact [an investor’s] specific investment.”[19]

[18] A round trip is a purchase and sale transaction. The high-end spread cost is using the 95th and 5th percentiles.
[19] Proposing Release at 155.

WisdomTree is skeptical that the proposed Form N-1A bid-ask information will be useful to investors given how stale that information will be, particularly in the face of rapidly changing market conditions. It seems unnecessarily burdensome and costly to require that ETF sponsors aggregate such stale information, which is not under the control of the ETF and is only available through third party vendors that may provide different outputs, and then subject such information to a complex calculation methodology. It would be more meaningful for an investor to go directly to the source of the bid and the offer – the broker-dealer. WisdomTree believes that bid-ask spread information is best accessed from an investor's broker-dealer, which will yield the most reliable source of current market information. Accordingly, in our view, the prospectus should explain what spreads are and direct investors to obtain current information from their broker-dealer.

Considering these concerns, if the Commission determines that certain bid-ask spread information must be provided by the ETF, then WisdomTree believes that the information, in limited form, should appear on the ETF's website where it can be kept current (to the extent possible) and meaningful. For instance, daily website reporting of the midpoint between the bid and ask from the close of the previous trading day would provide investors with current information and relative context based on more recent market conditions. Maintaining certain limited information about bid-ask spreads on an ETF's website would be more relevant than prospectus data to a person trying to assess trading costs before buying and selling shares of an ETF on any given day.

Similar to the discussion regarding bid-ask disclosure above, the proposed calculator to show the effect of the bid-ask spread on a potential transaction is an item that is more applicable to the brokerage function and incorporates information beyond the control of the ETF. The proposed calculator is best suited for a broker-dealer to provide because a retail investor must purchase shares through his or her broker-dealer. Execution information should not become a requirement of an ETF. Moreover, it seems anomalous to require an ETF to include a "calculator" for trading costs when other issuers with exchange-traded securities and mutual funds are not so required: IBM and GE are not required to include a calculator on their investor page for determining the costs of purchasing their shares through a third party, nor are any mutual fund providers required to include a calculator on their websites for investors to determine purchasing costs associated with a mutual fund, such as the impact of front-end sales loads.

C. Premium or Discount

The Proposed Rule would require the ETF's website to disclose: (i) the prior business day's premium or discount; (ii) a table showing the number of days the ETF traded at a premium or discount during the most recent calendar year and most recent calendar quarters; (iii) a line graph showing the premiums or discounts during the most recent calendar year and most recent calendar days; and (iv) disclosure of factors that contribute to a premium or discount that is over two percent for more than seven consecutive trading days (if that occurs).

The premium or discount is defined as the difference between the market price of ETF shares at the time of the net asset value calculation and the net asset value. The Proposed Rule defines the term "market price" to mean "(i) the official closing price of an exchange-traded fund share; or (ii) *if it more accurately reflects* the market value of an exchange-traded fund share at the time of which the exchange-traded fund calculates current net asset value per share, the price that is the midpoint."[20] The use of midpoint should not be limited to a subjective determination that it "more accurately reflects" market value. The midpoint is used in many instances in relation to the operation of ETFs and should be a permitted standard for "market price" in any context, so long as the ETF discloses which method it uses.

Generally, WisdomTree agrees that investors should receive certain information about premiums and discounts because it illustrates for the investor another aspect of an ETF's share price and also how effectively the arbitrage function limits differences between the share price and its net asset value. However, the amount of detail in the Proposed Rule is excessive and too detailed to be meaningful. Specifically, WisdomTree does not believe that the table showing the number of days the ETF traded at a premium or discount during the most recent calendar year and most recent calendar quarters is necessary. WisdomTree believes that the line graph alone would be sufficient to illustrate how the ETF's shares tend to correlate (or not) with their net asset value. Moreover, WisdomTree believes that the two percent trigger for additional disclosure is arbitrary, and it may have different import depending on the nature of the securities in which the ETF invests. WisdomTree believes that it would be more meaningful to require ETFs to include clear disclosure regarding the general market factors that may cause the share price to deviate from the net asset value generally (such disclosure is already commonly discussed in ETF prospectuses). Additionally, the tendency of an ETF to experience any two percent or greater premium or discount over an extended period could also be derived from the same line graph.

IV. Certain Provisions and/or Lack of Relief Would Disproportionately and Negatively Impact ETFs Holding Foreign Securities

The Proposed Rule would have a disproportionate and negative impact on ETFs holding foreign securities or having exposure to foreign markets, particularly emerging market and frontier market ETFs. WisdomTree has extensive experience in emerging market and frontier market ETFs (equity, debt and currency strategies),[21] which has

[20] Proposed Rule 6c-11(a).
[21] WisdomTree currently has over fifteen emerging/frontier market equity, debt or currency strategy ETFs in operation with over $5 billion in assets, including WisdomTree's first emerging market equity ETF which launched in 2007.

provided us with a unique perspective on how certain of these elements may effect such ETFs.

A. T-1 Orders

The Proposed Rule would seem to preclude "T-1 orders," whereby orders are placed by an authorized participant during a prescribed window after the U.S. market closes, such as between 4:01 pm ET and 5:30 pm ET, and are processed at the next day's net asset value. This order process is common for ETFs, particularly those ETFs that invest in or have exposure to certain emerging and frontier markets, which transact in cash due to limitations in such markets for transferring securities in-kind (among other reasons). Currently, standard ETF exemptive relief provides that "[e]ach Business Day, before the open of trading on the Listing Exchange, the Fund will cause to be published through the NSCC the names and quantities of the instruments comprising the Deposit Instruments and the Redemption Instruments, as well as the estimated Cash Amount (if any), for that day." However, the Proposing Release states that the published basket (along with the ETF's portfolio holdings) "must be disclosed before the opening of trading of the ETF's shares *and before the ETF begins accepting orders for the purchase or redemption of creation units to be priced based on the ETF's next calculation of NAV*."[22] Considering that basket information is not available until after the T-1 order window (*e.g.*, between 6:00 pm ET to 8:00 pm ET), this requirement will disrupt existing practices relating to ETFs that invest in or have exposure to foreign markets, and particularly emerging and frontier markets. For example, the use of a T-1 order policy allows the ETF's portfolio manager to consider, prepare for and place trades overnight for emerging market securities that are not transferable in-kind to more closely correspond to the next day's net asset value for such ETFs, which also facilitates efficient arbitrage activity for such ETFs. To transact otherwise, such as via a T order, would introduce uncertainty as to trading execution because the authorized participant's cash would have exposure extending to the opening (or beyond) of the applicable foreign market the next morning. Such uncertainty, coupled with potentially higher transaction costs ultimately borne by an authorized participant, could be expected to lead to wider bid-ask spreads and greater premium/discounts for such ETFs. Further, authorized participants and portfolio managers have become accustomed to these order windows, and they work well to facilitate index tracking and effective arbitrage activity. Any change that would require a delay in accepting such orders would be disruptive and could have unknown consequences. In our view, these challenges are not justified by the proposed earlier timing of basket/holdings publication in relation to order taking, particularly when such ETFs have historically functioned with an effective arbitrage mechanism. We therefore recommend that the Commission require the basket (and portfolio holdings) be published prior to the opening of trading on the exchange, but independent of the ETF's order taking.

[22] Proposing Release at 104 (emphasis added).

B. Settlement Cycles

Section 22(e) generally prohibits an ETF from postponing the date of payment for a redemption for more than seven days. As noted above, the Proposed Rule includes an exemption from Section 22(e) that permits ETFs that include foreign investments to postpone delivery of redemption proceeds beyond seven days but also imposes an arbitrary ten-year expiration date for the relief. Due to the operation of certain foreign markets – particularly certain emerging or frontier markets – a longer period may be necessary. The expiration is premised on the belief "that technological innovation and changes in market infrastructures and operations will lead to further shortening of settlement cycles, although these developments may be gradual."[23] As this statement notes, the process may be gradual. The Proposing Release notes that "ETFs that invest in foreign investments that continue to require more than seven days to deliver redemption proceeds [after the expiration] would have the option of redeeming in cash rather than in-kind once the exemptive relief sunsets. Such ETFs also could request targeted exemptive relief from section 22(e) from the Commission."[24] WisdomTree does not believe the burden should shift to the ETF to alter its business practice or request relief in the event a basic assumption underlying the relief does not materialize. Rather, the relief in the Proposed Rule should be made permanent and only reevaluated upon the actual occurrence of cycles shortening to an adequate level.

C. Transaction Fees

ETF exemptive applications have long contained a restriction noting that "[i]n all cases, such Transaction Fees will be limited in accordance with requirements of the Commission applicable to management investment companies offering redeemable securities," which requirements are embodied in Rule 22c-2 under the Investment Company Act. Rule 22c-2 limits redemption fees to two percent of the value of the redemption proceeds. Imposing the two percent limit on ETF redemptions causes the ETF and its shareholders to absorb all transaction costs in excess of two percent of the value of the redemption proceeds. However, the ETF structure is designed to protect the ETF and its remaining shareholders from the costs triggered by purchases and redemptions by authorized participants. For WisdomTree ETFs, such costs are calculated on a transaction-by-transaction basis to pass on the costs of trading underlying securities to authorized participants and WisdomTree does not believe such ETF transaction costs should be viewed as a "redemption fee." These costs are typically higher when transacting in foreign markets, particularly certain emerging markets and, accordingly, ETFs investing in such markets are those most affected by, or susceptible to, the two percent limit. The operation of Rule 22c-2 to limit an ETF's ability to fully recoup these costs from authorized participants is not beneficial to the ETF or its remaining shareholders and enables an authorized participant to benefit at the expense of the ETF.

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[23] Proposing Release at 57.
[24] *Id.* at note 156.

There are meaningful differences in the operation of ETFs and mutual funds, and the way in which their shares are bought and sold, that warrant reconsideration of the application of Rule 22c-2 to ETFs. Unlike mutual funds, which are purchased and sold by retail investors, ETFs transact in the primary market solely with authorized participants; it is these large financial firms that would bear the cost of any transaction fee over two percent. For mutual funds, it is the retail investor that needs protection from undue financial penalty which necessitates the protections of Rule 22c-2. That policy concern is absent here.

We note that the adopting release for the new liquidity management rules acknowledged that commentators recommended that the two percent limit on ETF transaction costs be eliminated because doing so would, among other benefits, protect ETFs from the dilution associated with transaction costs in excess of two percent. The Commission determined that addressing the ETF transaction costs issue was "beyond the scope of [that] rulemaking."[25] We note that the Proposing Release does not address whether the two percent limit is necessary, or which parties it is designed to protect, but merely states that it is applicable.[26] For the reasons stated above, we believe that ETFs should not be subject to the two percent limit on redemption fees, whether by way of specific relief or by making clear that ETF "transaction costs" as described above are not considered "redemption fees." Accordingly, we respectfully request that the Commission take this opportunity to provide such relief or clarity.

V. Investment Companies Investing in ETFs

WisdomTree urges the Commission to include relief from Section 12(d)(1) of the Investment Company Act that is required to permit investment companies to invest in ETFs in excess of the limits in that statute. In 2008, when the Commission previously

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[25] *Investment Company Liquidity Risk Management Programs*, Investment Company Act Release No. 32315 (Oct. 13, 2016) ("A few commenters also suggested that increasing ETF basket flexibility and eliminating the two percent limitation on redemption fees for ETFs would help enhance ETF liquidity and the orderly and efficient operation of the arbitrage function."). *See* Letter from Dechert LLP to Brent J. Fields, Secretary, Securities and Exchange Commission (Jan. 13, 2016) ("[T]ransaction fees [] are borne by APs and are tied specifically to the incremental costs incurred by the ETF as a result of the cash redemptions…. In contrast to the redemption fees which are the focus of Rule 22c-2, the redemption transaction fees charged by an ETF are not intended to inhibit frequent trading. In fact, unfettered ability of an AP to redeem is critical to the efficiency and effectiveness of the arbitrage process which tends to ensure that shares trade at market prices of or close to NAV." (footnotes omitted)). *See also* Letter from David W. Blass, General Counsel, Investment Company Institute, to Brent J. Fields, Secretary, Securities and Exchange Commission (Jan. 13, 2016) ("Although Rule 22c-2 is intended to inhibit short-term traders from diluting fund shares, an ETF encourages short-term trading of its shares. Indeed, an ETF needs robust trading and arbitrage, through the creation and redemption process, to help keep the market value of its shares aligned with the value of its portfolio. The transaction costs associated with this trading, however, should be borne by the redeeming APs, large institutions that can hedge or pay such costs, rather than the fund").

[26] Proposing Release at 67.

proposed an ETF rule,[27] the proposal included such relief, which would have generally expanded and streamlined the relief contained in current Section 12(d)(1) exemptive orders issued to ETFs. Since that time, the importance of ETFs as an investment tool has continued to increase for all types of investors, including investment companies, that may use ETFs to pursue a variety of investment strategies in a liquid and efficient manner, for hedging and risk management purposes, and to "equitize" cash balances to earn returns in excess of money market rates. During that same time, the Commission has recognized the unique aspects of ETFs in its rulemaking; for example, the recently-issued rule regarding investment company liquidity risk management programs exempts ETFs from certain requirements of the rule.[28] In addition, the Commission included "Fund of Funds Arrangements" in its Spring 2018 – Agency Rule List,[29] however, there are certain aspects of Section 12(d)(1) relief that are unique to ETFs and we believe they warrant attention, at this time, as part of the broader relief provided to ETFs.

VI. Conclusion

WisdomTree appreciates the opportunity to provide comments on the Proposed Rule. WisdomTree believes that the Proposed Rule is a step forward to creating "consistent, transparent, and efficient regulatory framework for ETFs." The Proposed Rule begins to make this true following the patchwork relief provided by the exemptive order process. WisdomTree seeks improvement to the consistency of the regulatory regime across other applicable securities laws and rules to see the efficiencies become possible and for certain modifications to the Proposed Rule when adopted.

Kind regards,

/s/ Ryan M. Louvar

Ryan Louvar
General Counsel

cc: The Honorable Jay Clayton
The Honorable Robert J. Jackson Jr.
The Honorable Hester M. Peirce
The Honorable Elad L. Roisman
The Honorable Kara M. Stein

Ms. Dalia Blass, Director, Division of Investment Management

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[27] *See Exchange-Traded Funds*, Investment Company Act Release No. 28193 (Mar. 11, 2008).
[28] *See supra* note 25.
[29] *See Regulatory Flexibility Agenda*, Investment Company Act Release No. 33045 (Mar. 14, 2018) (approving Agency Rule List *available at* https://www.reginfo.gov/public/do/eAgendaMain?operation=OPERATION_GET_AGENCY_RULE_LIST&currentPub=true&agencyCd=3235&Image58.x=58&Image58.y=).