Direxion
ETFs | Funds

October 1, 2018

Brent J. Fields, Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: File No. S7-15-18: Exchange-Traded Funds

Rafferty Asset Management, LLC ("Direxion") is writing to comment on proposed Rule 6c-11 (the "ETF Rule") under the Investment Company Act of 1940, as amended ("1940 Act").[1] Direxion was founded in 1997 and sponsors approximately 80 exchange-traded funds ("ETFs") and 16 mutual funds with approximately $14 billion in assets under management. Most of the Direxion ETFs are leveraged ETFs, which seek to provide daily returns of up to 300% (long or short) of an underlying index.[2] As one of the limited number of sponsors of leveraged ETFs, our comments focus on the scope and text of the rule as it pertains to leveraged ETFs and on related investor and disclosure matters.

Background

The Direxion ETFs operate in reliance on SEC exemptive orders,[3] which explicitly addressed their leveraged strategies and which were issued upon the Commission having found that the relief requested was "necessary or appropriate in the public interest and consistent with the protection of investors and the purposes fairly intended by the policy and provisions" of the 1940 Act.[4] The Direxion ETFs have consistently complied with the terms and conditions in the Direxion Exemptive Orders. In addition, the Direxion ETFs have worked as represented – both to the Commission at the time that it issued the Direxion Exemptive Orders and to investors.

- Each Direxion ETF's investment objective is to pursue leveraged returns on a benchmark index *on a daily basis.* Thus, each Direxion ETF's exposure is rebalanced daily. There is no incentive or opportunity for a Direxion ETF to have different exposures over time (*i.e.,* no leverage creep) or to assume additional exposures to "make up" for lagging performance.

1 Exchange-Traded Funds, Investment Company Act Release No. 33140 (July 31, 2018), 83 Fed. Reg. 37332 (to be codified at 17 C.F.R. pts. 239, 270, and 274) ("Proposing Release").

2 For purposes hereof, we use the term "leveraged ETFs" as defined in the Proposing Release. *See* Proposing Release at note 70 and surrounding text. In addition, all references to the "Direxion ETFs" are to those Direxion ETFs that are leveraged ETFs.

3 Investment Company Act Release Nos. 28889 (August 27, 2009) (notice) and 28905 (September 22, 2009) (order) (File No. 812-13610) and 28379 (September 12, 2008) (notice) and 28434 (October 6, 2008) (order) (collectively, the "Direxion Exemptive Orders").

4 15 U.S.C. § 80a-6(c).

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- Each Direxion ETF employs a naming convention, which clearly and concisely signals the daily leveraged or inverse nature of its investment objective.[5]

- The Direxion ETFs' full portfolio holdings, including holdings of derivatives contracts, are completely transparent. They are published to the market and disclosed on the Direxion ETFs' website each day before the commencement of trading.

- The Direxion ETFs provide explicit and expansive warnings, including on their prospectus cover page, that they are only appropriate for sophisticated investors who understand the daily leveraged nature of their strategies and the concept of compounding and who intend to monitor their portfolio frequently.[6]

<u>Comments</u>

The ETF Rule would codify for ETFs the exemptive relief that is necessary for them to register and operate under the 1940 Act as open-end management investment companies, provided that they comply with the conditions set forth in the rule. One such condition requires that:

> The exchange-traded fund may not seek, directly or indirectly, to provide returns that exceed the performance of a market index by a specified multiple, or to provide returns that

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[5] The naming convention of the Direxion ETFs is as follows: Direxion + Daily + Underlying Index + Bull (Bear) + 3X + Shares. Thus, for example, our leveraged Direxion ETF that tracks the S&P 500 Index is named the "Direxion Daily S&P 500 Bull 3X Shares," and our inverse Direxion ETF tracking the same index is named the "Direxion Daily S&P 500 Bear 3X Shares." This naming convention conveys that: the Direxion ETFs are short-term (*i.e.*, daily) investment vehicles; they are leveraged (*i.e.*, 3X); they track an index (*e.g.*, S&P 500); and they seek long (*i.e.*, Bull) or short (*i.e.*, Bear) exposure to the Underlying Index.

[6] The Direxion ETFs provide the following disclosure in boldface type on the first page of the summary prospectus immediately below the investment objective:

> The Fund is not suitable for all investors. The Fund is designed to be utilized only by knowledgeable investors who understand the potential consequences of seeking daily leveraged investment results, understand the risks associated with the use of leverage, and are willing to monitor their portfolios frequently. The Fund is not intended to be used by, and is not appropriate for, investors who do not intend to actively monitor and manage their portfolios. An investment in the Fund is not a complete investment program.

Additionally, the following disclosure appears in boldface type at the front of the statutory prospectus and Statement of Additional Information:

> The Funds are not suitable for all investors. The Funds are designed to be utilized only by sophisticated investors, such as traders and active investors employing dynamic strategies.
>
> * * *
>
> Investors who do not understand the Funds or do not intend to actively manage their funds and monitor their investments should not buy the Funds.
>
> If a Fund's underlying index moves more than 33% on a given trading day in a direction adverse to a Fund, a Fund's investors would lose all of their money.

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have an inverse relationship to the performance of a market index, over a fixed period of time.[7]

The Proposing Release explains that this condition is designed to "prevent leveraged ETFs from relying on" the ETF Rule.[8] The Proposing Release seeks comment on whether it is appropriate for the proposed rule to carve out leveraged ETFs. The Proposing Release also seeks comment on whether investors understand leveraged ETFs, particularly better than they did in 2009, and whether leveraged ETFs (presumably to the extent that they were allowed to rely on the rule, as adopted) should be subject to enhanced disclosure requirements. We address these requests for comment in order.

<u>The ETF Rule Should Allow for Leveraged ETFs</u>

We generally support the adoption of the ETF Rule. However, we believe that it would be appropriate for the ETF Rule to encompass leveraged ETFs and allow for their operation in reliance on the rule. The Commission and the market now have more than a decade of experience regulating and investing in leveraged ETFs. During that time period, leveraged ETFs have operated as described in the applications underlying their exemptive orders and as fully disclosed to investors. Accordingly, we believe that the Commission could reasonably determine to allow leveraged ETFs to operate in reliance on the ETF Rule.

We understand, however, that the Commission may have a relatively narrow goal for the ETF Rule – namely, to codify an exemption for "plain vanilla" ETFs.[9] As discussed in a comment letter recently submitted in connection with the Commission's proposal of Regulation Best Interest,[10] Direxion generally agrees with the characterization of leveraged ETFs as "complex" products.[11] Therefore, we do not object to the carve out of leveraged ETFs from the ETF Rule in light of the Commission's goals with regard to the ETF Rule.

<u>The Statistical Data Available Indicates that Most Investors Understand Leveraged ETFs</u>

In the Proposing Release, the Commission seeks comment on whether investors understand leveraged ETFs and whether current suitability requirements are effective. As explained in the Direxion Regulation BI Letter, we believe that the users of Direxion's leveraged ETFs largely do understand the products and use them appropriately, meaning that investor expectations are met. There is significant evidence that supports this view, including: the implied holding period data

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7 Proposed Rule 6c-11(c)(4).

8 Proposing Release at 31 and note 80. *See generally* Proposing Release at Section II.A.3.

9 *See* Commissioner Kara M. Stein, Statement at Open Meeting on Proposed Rule 6c-11 under the Investment Company Act of 1940 Governing Exchange-Traded Funds (June 28, 2018), https://www.sec.gov/news/public-statement/statement-stein-exchange-traded-funds-062818. *See also* Proposing Release at note 70 (stating that leveraged ETFs are only "approximately 1% of al ETF assets").

10 Angela Brickl, Rafferty Asset Management, LLC, Comment Letter on Proposed Regulation Best Interest (August 7, 2018), https://www.sec.gov/comments/s7-07-18/s70718-4186168-172727.pdf ("Direxion Regulation BI Letter") (attached hereto as Exhibit 1).

11 *See* FINRA Regulatory Notice 12-03, Heightened Supervision of Complex Products (January 2012); *see also* FINRA Regulatory Notice 09-31, Non-Traditional ETFs (June 2009) (collectively, the "FINRA Notices").

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provided as part of the Direxion Regulation BI Letter, including the data obtained during periods of index volatility;[12] brokerage firms' access screens that are designed to ensure that investors understand leveraged ETFs when investing in them;[13] the inverse correlation between leveraged ETFs' performance and net shareholder investment (*i.e.*, net creation/redemption);[14] FINRA's regulatory notices to members reminding them of their suitability obligations;[15] and Direxion's emphatic prospectus disclosure and educational efforts. Given these measures, we believe it would be hard for investors *not* to understand that our leveraged ETFs are complex products that are "different" from other ETFs, and we have not seen any recent empirical data or other evidence to the contrary.

Further, we believe that the existing suitability requirements applicable to leveraged ETFs are appropriate and effective. In this regard, as discussed at length in the Direxion Regulation BI Letter, we note that brokers do not have special conflicts of interest or any special financial incentives to sell leveraged ETF shares to investors. The Direxion ETFs do not charge a sales load, which could provide a revenue stream for selling brokers. The Direxion ETFs also do not charge Rule 12b-1 fees, sub-transfer agency fees or shareholder servicing fees and Direxion has not entered into any revenue-sharing arrangements with brokers for the distribution of their shares. In sum, purchases of Direxion ETF shares do not result in additional compensation or conflicts for brokers. As a result, brokers have the same incentives to sell Direxion ETF shares as they do other exchange-traded securities. We refer the Commission to the Direxion Regulation BI Letter for our analyses in this regard.[16]

The Proposing Release seeks comment on what types of investors transact in leveraged ETF shares and how different types of investors utilize leveraged ETFs. As the Commission likely recognizes, ETF sponsors have little to no visibility into their investor population below (a) the Depository Trust Company accountholder who holds ETF shares in book entry form on behalf of brokers and their clients and (b) the authorized participants that transact in creation units. As a result, like other ETF sponsors, Direxion does not have data regarding its beneficial shareholders or their investment strategies.

Direxion Supports Robust Disclosure for Leveraged ETFs

In the Proposing Release, the Commission seeks comment on whether Form N-1A should be amended to require leveraged ETFs to include in their disclosure "charts . . . that explain the potential impact of compounding on an investor's returns." To the extent that the ETF Rule is

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12 *See supra* note 10.

13 *Id.*

14 *Id.* at Appendix B (noting that generally Direxion ETF assets do not increase with positive performance. In fact, 60% of the time when a Direxion ETF's performance is positive, it receives net redemptions and *vice versa*. Similarly when a Direxion ETF's performance is negative, the ETF will have net purchases approximately 60% of the time).

15 *See* FINRA Notices, *supra* note 11.

16 Furthermore, as discussed in the Direxion Regulation BI Letter, brokers arguably have a financial disincentive to sell shares of Direxion ETFs to certain clients as a result of FINRA requiring increased maintenance margin on leveraged ETFs. *See* FINRA Regulatory Notice 09-53, Increased Margin Requirements for Leveraged Exchange-Traded Funds and Associated Uncovered Options (August 2009). *See also* Direxion Regulation BI Letter, *supra* note 10 at 4 (related discussion).

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adopted in a form that allowed for the operation of leveraged ETFs, Direxion would support enhanced disclosure requirements for leveraged ETFs. As discussed above and in the Direxion Regulation BI Letter, Direxion has historically embraced and employed robust disclosure.

* * *

Direxion appreciates the opportunity to comment on the ETF Rule. If there are questions regarding this comment letter, please feel free to contact the undersigned at 646-572-3463.

Respectfully,

Angela Brickl

Angela Brickl
General Counsel

cc: The Honorable Jay Clayton, Chairman
The Honorable Kara Stein, Commissioner
The Honorable Robert Jackson, Commissioner
The Honorable Hester Peirce, Commissioner
The Honorable Elad Roisman, Commissioner
Securities and Exchange Commission
Dalia O. Blass, Director - Division of Investment Management
Securities and Exchange Commission
Daniel D. O'Neill, Chief Executive Officer
Robert D. Nestor, President
Direxion

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Exhibit 1

August 7, 2018

Brent J. Fields, Secretary
Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: File No. S7-07-18: Regulation Best Interest

Dear Mr. Fields:

Introduction

On May 9, 2018, the U.S. Securities and Exchange Commission ("SEC" or "Commission") officially proposed for adoption Regulation Best Interest ("Regulation BI") under the Securities Exchange Act of 1934, as amended ("Exchange Act").[1] The proposing release for Regulation BI ("Proposing Release") makes certain statements and asks related questions about leveraged and inverse exchange-traded funds (collectively, "leveraged ETFs").[2]

Rafferty Asset Management, LLC ("Direxion"), founded in 1997, sponsors approximately 80 exchange-traded funds ("ETFs") and 16 mutual funds with approximately $15 billion in assets under management ("AUM"). Most of the Direxion ETFs are leveraged ETFs, which seek to provide daily returns of up to 300% (long or short) of an underlying index.[3] As ETFs, the Direxion ETFs operate in reliance on SEC exemptive orders,[4] which explicitly addressed their leveraged strategies and which were issued upon the Commission having found that the relief requested was "necessary or appropriate in the public interest and consistent with the protection of investors and the purposes fairly intended by the policy and provisions" of the 1940 Act.[5]

As one of the limited number of sponsors of leveraged ETFs (and mutual funds), we write to comment on the statements in the Proposing Release regarding such products and to address

1 Exchange Act Release 34-83062, 83 Fed. Reg. 21,574, 21,681 (May 9, 2018).

2 Shortly after Regulation BI was proposed, on June 28, 2018, at an open meeting, the Commission proposed for adoption Rule 6c-11 under the Investment Company Act of 1940, as amended ("1940 Act") (Rule 6c-11, the "ETF Rule"). Investment Company Act Release No. 33140 (July 31, 2018) ("ETF Release"). For purposes hereof, we use the term leveraged ETFs as defined in the ETF Release. *See* ETF Release at note 70 and surrounding text.

3 As used in this letter, the term "Direxion ETFs" refers exclusively to the leveraged and inverse leveraged ETFs sponsored by Direxion, and the term "Direxion Shares" refers exclusively to the exchange-traded shares of such (leveraged and inverse leveraged) Direxion ETFs.

4 Investment Company Act Release Nos. 28889 (Aug. 27, 2009) (notice) and 28905 (Sept. 22, 2009) (order) (File No. 812-13610) and 28379 (Sept. 12, 2008) (notice) and 28434 (Oct. 6, 2008) (order) (collectively, the "Direxion Exemptive Orders").

5 15 U.S.C. § 80a-6c.

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related questions. In particular, we write to address the incorrect notion that brokers have special financial incentives to recommend transactions in leveraged ETF shares to clients and, as a consequence, leveraged ETFs shares are frequently purchased based on broker recommendations that are improperly influenced by such financial incentives.[6] In fact, brokers have no different financial incentives to recommend transactions in leveraged ETF shares than in any other exchange-traded security and, in certain circumstances, have considerable disincentives for recommending transactions in leveraged ETF shares. For this reason, given the three tenets of proposed Regulation BI – namely, the disclosure obligation, care obligation and conflict of interest disclosure obligations – we do not believe that transactions in leveraged ETF shares should be considered in the context of the conflict of interest disclosure obligations. Rather, we believe that transactions in leveraged ETF shares should foremost be addressed in the context of the care obligation. We write to explain our view and to express support Regulation BI as it would apply to leveraged ETF shares to the extent that, as adopted, it enhances the alignment between broker recommendations and investors' expressed and informed risk appetites.

<u>Background</u>

As proposed, Regulation BI would provide that,

> A broker, dealer or a natural person who is an associated person of a broker or dealer, when making a recommendation of any securities transaction or investment strategy involving securities to a retail customer, shall act in the best interest of the retail customer at the time the recommendation is made, without placing the financial or other interest of the broker, dealer or natural person who is an associated person of a broker dealer making the recommendation ahead of the interest of the retail customer.[7]

Regulation BI would define a "retail customer" as a "person, or the legal representative of such person, who: (1) receives a recommendation of any securities transaction or investment strategy involving securities from a broker, dealer or a natural person who is an associated person of a broker or dealer, and (2) uses the recommendation primarily for personal, family or household purposes." Under proposed Regulation BI, a broker or dealer or natural person who is associated with a broker or dealer[8] would be deemed to have satisfied its obligation to act in the best interest of a retail customer when making a recommendation if it satisfied three obligations – namely, a disclosure obligation, [9] a care obligation and two conflict of interest disclosure obligations. We focus on the care obligation and the conflict of interest disclosure obligations here.

Pursuant to the care obligation, in making a recommendation, a broker-dealer must exercise reasonable diligence, care, skill and prudence to (i) understand the potential risks and rewards

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6 The Proposing Release, which only explicitly mentions leveraged ETFs in the conflict of interest discussion, assumes that this is the case.

7 Proposed Regulation BI would be adopted at 17 C.F.R. § 240.15*l*-1. *See* § 240.15*l*-1(a)(1).

8 To avoid wordiness, this letter will refer to brokers, dealers and such natural persons as "brokers."

9 Pursuant to the disclosure obligation, prior to or at the time of the recommendation, the broker must reasonably disclose in writing the material facts relating to the scope and terms of the relationship with the retail customer, including all material conflicts of interest associated with the recommendation.

associated with the recommendation, and have a reasonable basis to believe that the recommendation could be in the best interest of at least some retail customers and (ii) have a reasonable basis to believe that the recommendation is in the best interest of a particular retail customer based on that retail customer's investment profile and the potential risks and rewards associated with the recommendation, and (iii) have a reasonable basis to believe that a series of recommended transactions is not excessive and is in the retail customer's best interest when taken together in light of the retail customer's investment profile. The care obligation would substantially codify and potentially enhance brokers' extant suitability obligations.[10]

To date, most regulatory concerns around leveraged ETFs have focused on whether brokers have satisfied their suitability obligations when recommending them to investors.[11] Accordingly, we would have expected the Proposing Release to discuss leveraged ETFs in the context of the care obligation. The Proposing Release, however, does not mention leveraged ETFs in that context.[12]

Instead, the Proposing Release discusses leveraged ETFs solely in the context of the proposed conflict of interest disclosure obligations.[13] These disclosure obligations would apply to broker entities (not their associated persons) and would mandate the establishment, maintenance and enforcement of two types of written policies and procedures –

- one that is "reasonably designed to ***identify, and disclose, or eliminate***, all material conflicts of interest that are associated with recommendations covered by Regulation [BI]" and

- one that is "reasonably designed to ***identify, and disclose and <u>mitigate</u>, or eliminate***, material conflicts of interest arising from financial incentives associated with such recommendations."[14]

With respect to leveraged ETFs, the Proposing Release suggests that "heightened ***mitigation*** measures... may be appropriate… depending on the complexity of the product,"[15] and notes that FINRA has identified suitability and supervisory concerns in connection with complex products, such as leveraged ETFs. In so doing, the Proposing Release suggests that the Commission believes that leveraged ETFs are subject to conflicts of interest arising from brokers' financial incentives to recommend them.

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10 *See* Proposing Release at note 7 (recognizing that the enhancements based by Regulation BI are focused on what is currently required under the Exchange Act and "reflect obligations that already exist under the FINRA suitability rule or have been articulated in related FINRA interpretations and case law").

11 *See* Proposing Release at note 314.

12 *See* Proposing Release at 133-166; *but see* Proposing Release at note 436 and surrounding text (citing to FINRA Rule 2370 "Securities Futures") (in Economic Analysis of proposed Regulation BI).

13 Proposing Release at 176-180.

14 Proposing Release at 167 (emphasis added). The Proposing Release defines a "material conflict of interest" as one "that a reasonable person would expect might incline a broker[] – consciously or unconsciously – to make a recommendation that is not disinterested." Proposing Release at 110.

15 Proposing Release at 179-180 (emphasis added) (citing to Report on FINRA Examination Findings (December 2017), *available at* http://www.finra.org/industry/2017-report-exam-findings)).

Sales of Direxion's Leveraged ETFs are Not Subject to Special Conflicts of Interest

Brokers do not receive special financial benefits for selling Direxion Shares. Direxion Shares do not pay fees pursuant to a distribution plan adopted under Rule 12b-1 under the 1940 Act ("12b-1 fees"); accordingly, brokers do not receive 12b-1 fees in connection with sales of Direxion Shares. Direxion Shares do not pay a sub-transfer agency fee or shareholder servicing fee. Direxion Shares also are not subject to revenue sharing arrangements.[16] In addition, unlike most mutual funds, Direxion Shares are not offered in multiple classes, each of which has a different front-end load, back-end sales load and/or trail commission, resulting in brokers receiving different commission rates for sales of different classes of shares. Moreover, they are not sold by brokers who are affiliated with Direxion and who may, therefore, have a special incentive to distribute them as proprietary products. Further, to the best of our knowledge, brokers do not receive higher commission rates in connection with transactions in leveraged ETF shares. Rather, brokers have the same financial incentive to recommend them to retail customers as they do to recommend shares of Amazon or IBM and/or shares of other ETFs. In short, all of the financial incentives that have traditionally been deemed potentially to create financial conflicts of interest for brokers in connection with sales of mutual fund shares are absent in the case of Direxion Shares.

In fact, brokers arguably have a financial disincentive to sell Direxion Shares to certain clients. By Regulatory Notice 09-53, the Financial Industry Regulatory Authority, Inc. ("FINRA") reduced the ability of brokers to earn interest on leveraged ETF shares held in margin accounts by increasing the maintenance margin requirements for such shares by a factor commensurate with their leverage factor.[17] For example, assuming the standard maintenance margin requirement on a long ETF is 25% of its market value, the maintenance margin requirement applicable to a Direxion ETF that provides 300% leverage is 75% of its market value (three times 25%). As a result, brokers cannot earn as much interest (from margin loans) on leveraged ETFs as on other types of securities. Therefore, arguably, brokers not only lack a financial ***incentive*** to recommend leveraged ETFs to retail customers, they arguably have a financial ***disincentive*** to make such recommendations.[18] For these reasons, the conflict of interest disclosure obligations proposed in Regulation BI for complex products are irrelevant, and should be inapplicable, to leveraged ETFs.

Leveraged ETFs are Complex Products That Are Appropriately Subject to the Care Obligation

We agree with FINRA's historical treatment of leveraged ETFs as complex products. For that reason, we support consideration of leveraged ETFs in the context of the care obligation under proposed Regulation BI. According to the Proposing Release,

> The [c]are [o]bligation is intended to incorporate and enhance existing suitability requirements applicable to broker-dealers under the federal securities laws by, among other things, impose a "best interest" requirements which [the SEC] would interpret to

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[16] Direxion does have revenue sharing arrangements with respect to certain of its conventional ETFs and mutual funds (*i.e.,* ETFs and mutual funds that pursue non-leveraged and non-inverse strategies).

[17] FINRA Regulatory Notice 09-53, Increased Margin Requirements for Leveraged Exchange-Traded Funds and Associated Uncovered Options (August 2009) ("Notice 09-53").

[18] In Notice 09-53, FINRA acknowledges that it is "aware that other securities contain inherent leverage," but does not explicitly apply the requirement to such products.

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> require the broker-dealer not put its own interest ahead of the retail customer's interest, when making recommendations.[19]

In formulating the care obligation in this manner, the Commission implicitly recognized the importance and validity of brokers' suitability obligation, as it exists today. We believe that such suitability obligation successfully stands as an important barrier to retail customers' entry into leveraged ETFs. It is not, however, the only barrier to entry that retail customers face when seeking to invest in leveraged ETFs. As discussed below, investors must also surmount other barriers to entry, which Direxion has encouraged brokers voluntarily to put in place to ensure that transactions in Direxion Shares are entered into knowingly and conscientiously. We discuss both barriers to entry (in order) below as they pertain to leveraged ETFs.

With regard to suitability, FINRA has emphasized the two-part nature of a broker's suitability obligation.

> The first is determining whether the product is suitable for any customer…. With respect to leveraged… ETFs, this means that a firm must understand the terms and features of the funds, including how they are designed to perform, how they achieve that objective, and the impact that market volatility, the ETF's use of leverage, and the customer's intended holding period will have on their performance.
>
> Once a determination is made that a product is generally suitable for at least some investors, a firm must also determine that the product is suitable for the specific customers to whom it is recommended.[20]

With regard to the customer-specific suitability analysis, FINRA has directed brokers to use "reasonable efforts" to obtain relevant information, such as the customer's financial status and investment objectives. FINRA has also indicated that "leveraged ETFs ***typically*** are not suitable for retail investors who plan to hold them for more than one trading session, particularly in volatile markets."[21]

By Regulatory Notice 12-03, FINRA mandated heightened supervision for recommendations of "complex products," including leveraged ETFs.[22] In this regard, FINRA endorsed the adoption of formal written procedures to ensure that complex products are "thoroughly vetted" and that "the right questions are answered before a complex product is recommended to retail investors."

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[19] Proposing Release at 134.

[20] FINRA Regulatory Notice 09-31, Non-Traditional ETFs (June 2009) ("Notice 09-31"). Notice 09-31 also emphasized the importance of supervising and training registered persons about non-traditional ETFs.

[21] Notice 09-31 (emphasis added).

[22] FINRA Regulatory Notice 12-03, Heightened Supervision of Complex Products (January 2012) ("Notice 12-03"). *See also* Notice 09-31.

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As the Commission observed in the Proposing Release,[23] Notice 12-03 requires brokers to consider a client's "investment experience" and "risk tolerance" when making recommendations and further explicitly "encourage[s]" brokers to

> adopt the approach mandated for options trading accounts, which requires that a registered representative have a reasonable basis for believing, at the time of making the recommendation, that the customer has such knowledge and experience in financial matters that he may reasonably be expected to be capable of evaluating the risks of the recommended transaction, and is financially able to bear the risks of the recommended position.

Signaling the stringency of the suitability requirement, however, FINRA has cautioned that such measures, even if implemented, would not supplant a broker's suitability obligation.

We endorse the stringent suitability requirements described for recommendations of Direxion Shares, including the adoption by brokers of written policies and procedures that are appropriate for their business. We echo the sentiments of FINRA's Chief of Enforcement, however, that "[w]ritten procedures are worthless unless accompanied by a program to enforce them."[24] That is to say, there may be only so much that can usefully be prescribed or proscribed by a regulatory body. As the SEC itself has observed, "The best form of investor protection is to clearly understand leveraged… ETFs before investing in them."[25]

Fortunately, the ecosystem for leveraged ETFs has voluntarily adopted investor protection measures that go beyond those that are required by regulation. For example, Direxion has developed a list of recommendations for brokers that allow clients to trade leveraged ETFs.[26] The list includes the following recommendations:

- We encourage the use of alerts when a leveraged… ETF is traded for the first time. There are some key points that should be made during the initial trade request window [including]
    - Leveraged products… provide some multiple of the performance of [a] benchmark[] over a set time frame, typically daily.
    - Leveraged ETFs are suitable only for very experienced, aggressive, sophisticated investors who actively manage their investments daily….

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[23] Proposing Release at note 313.

[24] FINRA Sanctions Oppenheimer & Co. $2.9 Million for Unsuitable Sales of Non-Traditional ETFs and Related Supervisory Failures, FINRA News Release (June 8, 2016). *See also,* Finra Wacks B-D for Unsuitable Sales of Leveraged, Inverse ETFs, Ignites (March 2, 2018); Morgan Stanley Settles Charges Related to ETF Investments, SEC (February 14, 2017).

[25] SEC Investor Alert, "Leveraged and Inverse ETFs: Specialized Products with Extra Risks for Buy-and-Hold Investors," *available at* https://www.sec.gov/investor/pubs/leveragedetfs-alert.htm.

[26] Direxion, Recommendations for Conveying Considerations of Trading Leveraged and Inverse ETFs (attached at Appendix A).

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- We strongly recommend that all investors that wish to trade leveraged ETFs [] proactively indicate (via electronic checkbox or similar method) that they understand these [disclosures] and consider themselves a suitable user of the products before gaining access to the products for trading.

- We recommend that the display of leveraged… ETF position[s] on portfolio holdings screens should carry a footnote link such as the following: 'Notice to monitor this position frequently.'

As a result, in part, of such efforts by Direxion, brokers have widely adopted point of sale hurdles to trades of leveraged ETF shares. For example, one broker requires clients to sign an annual risk disclosure agreement in order to purchase leveraged ETFs. Similarly, another broker requires a client's investment objective to fall into the "most aggressive" category to be eligible to purchase leveraged ETFs.

Direxion has also focused on investor education since its inception, developing and offering educational content to brokers free of charge. In this area Direxion has partnered with brokers to develop educational content regarding leveraged ETFs, including in video, print and self-paced learning module formats. We regard such measures as fairly unprecedented and affirmative steps, taken by both us and brokers, to seek to ensure that the Direxion ETFs attract investments only from investors who understand them and will use them in an informed manner. We have taken these steps because we sincerely believe that they mitigate the likelihood of an uninformed investor investing in the products and reduce investor misuse of them. We further believe that eliminating uninformed investments in the Direxion ETFs is good for our business and, more importantly, is the right thing to do.

Further, as the SEC Staff knows, the Direxion ETFs provide extensive cautionary disclosure – particularly about the effects of leverage and compounding – in their leveraged ETF prospectuses. Direxion's emphatic disclosures begin with the naming convention it has applied, to date, to its leveraged ETFs, which make the names of the Direxion ETFs explicit and informative. Our long leveraged ETFs include the words "Daily" and "Bull" in their names, and our short (or inverse) leveraged ETFs include the words "Daily" and "Bear" in their names. For example, our leveraged S&P 500 index fund is the Direxion Daily S&P 500 Bull 3X Shares, and our inverse S&P 500 index fund is the Direxion Daily S&P 500 Bear 3X Shares. Although we would, of course, prefer for all investors to read the entire prospectus before investing, our naming convention is designed to notify investors that our funds are ***daily leveraged*** investment products.

As indicated by the holding period data in Appendix B, investors seem to understand the short-term nature of an investment in Direxion Shares. Such data shows that the average holding periods of Direxion Shares are substantially shorter than the average holding periods of traditional index ETFs in the same or a similar asset class.[27] In addition, the data shows that flows into the Direxion ETFs are inversely correlated with performance,[28] which is a highly unusual investment pattern but consistent with the theory that the vast majority of Direxion investors actively monitor and manage their investment positions.

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[27] *See* Appendix B at B-1 – B-2.

[28] *See* Appendix B at B-2 – B-3.

Direxion ETFs | Funds

In sum, we believe that the regulatory regime applicable to purchases of Direxion Shares is robust, and we endorse the stringent restrictions that are part of that regime. In addition, we are proud of the voluntary measures we and brokers have taken in an effort to heighten investor protections around all transactions in Direxion Shares, including self-directed transactions. We believe that, collectively, the regulatory and voluntary hurdles to transacting in Direxion Shares work effectively.

In the context of the ETF Rule proposal, however, a concern has nevertheless been raised about investors who buy and hold leveraged ETFs for longer periods. The concern voiced is that such investors must misunderstand the products – apparently because buying and holding leveraged ETF shares *de facto* evidences a misunderstanding and misuse of such products – because investors are necessarily harmed by buying and holding them. This concern has found its greatest expression in FINRA Notice 09-31. There, in light of the daily rebalancing feature of leveraged ETFs, FINRA declared them "unsuitable for retail investors who plan to hold them for longer than one trading session."[29] In making this declaration, FINRA improperly elevated a principal risk of leveraged ETFs into an unavoidable pitfall of them. More specifically, FINRA transformed the risk that losses ***can be*** incurred from compounding by holding leveraged ETF shares into a fact that losses ***are*** incurred from compounding when holding leveraged ETF shares.

Compounding, however, is purely a mathematical phenomenon that can harm, help or hardly impact investors. Contrary to FINRA's declaration, it is not a one-way ratchet that necessarily harms investors. The effect of compounding on investment returns depends largely on market conditions, including whether the market is flat, trending or volatile and whether the market goes up or down after an investor invests in a long leveraged product (*e.g.,* a Direxion Bull ETF) or an inverse leveraged product (*e.g.,* a Direxion Bear ETF).[30] Direxion's prospectuses and website offer ample educational materials with clear examples of how compounding works and the implications of compounding given the market variables described. Even a brief review of such materials clarifies that compounding can neutrally, positively or adversely impact returns.

For example, as of July 31, 2018, the five-year trailing return of the Direxion Daily Financial Bull 3X Shares (FAS) was 281.8% as compared to its benchmark's return of 83.8%. Stated differently, the ETF provided more than 300% of the return of its benchmark for the five-year period due to trending and rising market conditions.[31] As a result, contrary to FINRA's declaration that buying and holding leveraged ETF shares results in losses from compounding, a five-year shareholder in FAS (as of July 31, 2018) would have profited from buying and holding for the period. Accordingly, an investor should not be assumed or deemed to misunderstand and misuse leveraged ETFs – or to be harmed by investing in them – simply because he or she buys and holds

29 Notice 09-31 at note 1 and surrounding text.

30 Direxion's leveraged ETFs are referred to as "Bull ETFs," whereas Direxion's inverse (leveraged) ETFs are referred to as "Bear ETFs."

31 Similarly, the five-year trailing returns (7/31/2013 - 7/31/2018) of the Direxion Daily S&P 500 Bull 3X Shares and Direxion Daily Technology Bull 3X Shares were 324% and 789%, respectively. Each of these Direxion ETFs not only generated strong positive returns, but exceeded 300% of the return of its respective benchmark index. We do not believe that these are outliers or exceptions over the time period represented because the markets were rising and trending. Indeed, under such circumstances, these results are arguably unsurprising.

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shares of them for longer periods. Rather, he or she may have individual reasons for the investment, and conscientiously and legitimately make it.

Appendix C provides additional examples of largely positive returns experienced on long-term investments in various Direxion Bull ETFs. More specifically, Appendix C provides "heat maps" for the five oldest Direxion Bull ETFs. Each pair of heat maps summarizes, for one Direxion Bull ETF, an investor's potential investment return at net asset value ("NAV") for every possible holding period since the ETF's inception as compared to (i) a return of zero and (ii) the return of the unleveraged index. As illustrated by the heat maps, the percentage of holding periods that produced positive returns for the five oldest Bull ETFs was demonstrably greater than the percentage of holding periods that produced negative returns. The result was partially attributable to the secular rising market of the past decade,[32] during which compounding was far from uniformly negative. The data refutes the notion that holding leveraged ETFs for extended periods of time *per se* results in losses and investor harm. It also casts significant doubt on the assumption (or conclusion) that investors hold leveraged ETFs for extended periods of time because they are unsophisticated and do not understand the products.[33] In sum, extended holding periods are simply not an indication of investor misunderstanding or misuse.

Nevertheless, to the extent that the Commission harbors concerns about investor misunderstanding and misuse of leveraged ETFs, we strongly encourage the Commission to grapple with those concerns in the context of Regulation BI, and not in the context of the ETF Rule. In this regard, it is important to recognize that ETFs are no differently situated (with respect to their shareholder base) than corporate issuers, such as Amazon and IBM. Further, like such issuers, ETFs must rely heavily on brokers' compliance with applicable sales practices in connection with transactions in their shares. Accordingly, the Regulation BI proposal is the appropriate forum for the Commission to consider sales practice issues related to all ETFs.

<u>Our Comments and Responses to the Commission's Requests for Comment in the Proposing Release</u>

Direxion believes that current regulatory requirements applicable to recommendations of leveraged ETFs are effective. Nevertheless, to the extent that the Commission determines that the adoption of Regulation BI, as proposed, would enhance investor protections in this area, Direxion supports it. More specifically, Direxion supports enhancements to the existing regulatory framework regarding recommendations of leveraged ETF shares that are designed to align recommendations made by a broker to an investor with that investor's informed and expressed risk appetite.

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32 As shown by the heat maps in Appendix C, the energy sector (as represented by the Direxion Daily Energy Bull 3X Shares (ERX)) has proven to be an exception to the rule that secular markets have risen over the last decade. Nevertheless, as also shown by the heat maps, holding ERX for an extended period led to outperformance, on an absolute basis (compared to zero), approximately 48% of the time and on a relative basis (compared to the unleveraged index) approximately 36% of the time. *See* Appendix C at C-2 – C-11.

33 Note that an investor who bought the Direxion Daily Financial Bull 3X Shares (FAS) in 2011 and held for the past seven years was arguably the savviest of all investors, having earned returns of over 500% over the extended holding period.

In the Proposing Release, the Commission says,

> We… recognize that it may be consistent with a retail customer's investment objectives – and in many cases, in a retail customer's best interest – for a retail customer to allocate investments across a variety of investment products or to invest in riskier or more costly products, such as some … structured products.[34]

In the same vein, the Proposing Release asks,

> Do commenters believe that Regulation [BI] is sufficiently clear that a [broker] may make a recommendation which may result in investor losses due to market or other risks inherent in investing?[35]

We do not believe it is clear from proposed Regulation BI what brokers must do when recommending a leveraged ETF to satisfy their suitability obligation, including to the extent such obligation is enhanced by Regulation BI. We recommend that the Commission provide clarifications in this area. For example, Direxion generally supports restricting access to leveraged ETF shares by accounts that are classified as having a "conservative" investment objective. Similarly, Direxion supports enhancements to the Retail Customer's Investment Profile (as defined in the Proposing Release[36]) to permit brokers, as a matter of course, to collect information regarding the frequency with which a retail customer monitors his or her portfolio and to restrict access to leveraged ETF shares to persons that intend to monitor their portfolios regularly.[37]

The Proposing Release observes,

> Currently, FINRA's heightened suitability requirements for options trading accounts require that a registered representative have a "reasonable basis for believing, at the time of making the recommendation, that the customer has such knowledge and experience in financial matters that he may reasonably be expected to be capable of evaluating the risks of the recommended transaction, and is financial able to bear the risks of the recommended position in the complex product."[38]

The Proposing Release notes that "FINRA has encouraged member firms to take a similar approach in recommending complex products," including leveraged ETFs, to clients.[39] Theoretically, if applied in parallel to transactions by retail customers in leveraged ETF shares, brokers would require registered representatives to have a reasonable basis for believing, at the time of recommending an investment in leveraged ETF shares, that the retail customer has such knowledge

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[34] Proposing Release at 147.

[35] Proposing Release at 161.

[36] Proposing Release at 144.

[37] *See generally,* Proposing Release at 144-149 (discussing the role of the Retail Customer's Investment Profile document in assessing broker compliance with a best interest obligation).

[38] Proposing Release at note 313 (citing FINRA Rule 2360(b)(19)).

[39] Proposing Release at note 313 (citing Notice 12-03).

and experience in financial matters that he or she may reasonably be expected to be capable of evaluating the risks of the leveraged ETF, and be financially able to bear the related risks. Given that FINRA has previously encouraged this approach for complex products, such as leveraged ETFs, we recommend that the Commission research the extent to which brokers have implemented it with respect to recommendations regarding leveraged ETF shares. If the Commission concludes, based on such research, that the approach improves the alignment between brokers' recommendations of leveraged ETF shares and their clients' declared risk appetites, the Commission should work with FINRA to implement the approach for recommendations of leveraged ETF shares.

Further, the Proposing Release asks,

> Are there certain product classes that commenters believe the Commission should outright prohibit? If so, which ones and why?[40]

For a variety of reasons, we do not support an outright prohibition on any particular product or product class. Similarly, we do not support an outright prohibition on certain persons (*e.g.,* those over 60 years of age) or certain types of accounts (*e.g.,* retirement accounts) transacting in any particular product or product class, including leveraged ETFs. With respect to leveraged ETFs in particular, any attempt to outright prohibit them based on the exaggerated concern that investors inappropriately buy and hold them and suffer harm as a result of compounding would fly in the face of available data from the last decade. Further, with respect specifically to the Direxion ETFs, any action by the Commission to outright prohibit them would be inconsistent with the findings made by the Commission in the Direxion Exemptive Orders that the relief requested was "necessary or appropriate in the public interest and consistent with the protection of investors and the purposes fairly intended by the policy and provisions" of the 1940 Act.

In addition, any action to outright prohibit any particular product or product class or to prohibit certain types of investors or accounts from transacting in a particular product or product class would take the Commission far afield from its core strength as a disclosure regulator and into the realm of merit regulation. We do not believe that the federal securities laws, including the 1940 Act, posit the SEC as a merit-based regulator. In this regard, consider that registered investment companies – from mutual funds to business development companies – can pursue investment strategies of all types and with varying degrees of risk, as long as they provide full and fair disclosure to investors and do not violate the 1940 Act by, for example, engaging in self-dealing as represented by Section 17 of the 1940 Act. We strongly encourage the Commission to continue this tradition.

Finally, we strongly encourage the Commission to address any concerns it may harbor about sales practices related to leveraged ETF shares in the context of Regulation BI. In that context, such concerns can be fully and appropriately vetted, unlike in the context of a tangential rulemaking, such as the proposed ETF Rule or another derivatives rule, such as a reproposal of Rule 18f-4 under the 1940 Act. This is the case because, as discussed above, the shares of leveraged ETFs are exchange-traded, like shares of Amazon and IBM. Accordingly, they are susceptible to substantially the same sales practice issues.

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40 Proposing Release at 196.

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*   *   *

Direxion appreciates the opportunity to comment on Regulation BI. If there are questions regarding this comment letter, please feel free to contact the undersigned at [redacted].

Respectfully,

Angela Brickl
General Counsel

cc: The Honorable Jay Clayton, Chairman
The Honorable Kara Stein, Commissioner
The Honorable Robert Jackson, Commissioner
The Honorable Hester Peirce, Commissioner
Securities and Exchange Commission
Dalia O. Blass, Director - Division of Investment Management
Securities and Exchange Commission
Daniel D. O'Neill, Chief Executive Officer
Robert D. Nestor, President
Direxion

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Appendix A

Recommendations for Conveying Considerations of Trading Leveraged and Inverse ETFs
As a leading provider of leveraged ETFs, Direxion is committed to ensuring that all users recognize the unique risks and characteristics of the products. We believe it is important to work closely with broker dealers to promote product education and we encourage brokerage firms to consider implementing certain policies and best practices to promote heightened awareness of the intricacies of leveraged ETFs on the part of their clients that use them.

Trade Window
We encourage the use of alerts when an individual leveraged and inverse ETF is traded for the first time. There are some key points that should be made during the initial trade request window that cover the following:

- Leveraged products are designed to provide some multiple of the performance of their respective benchmarks (or inverse of their performance), over a set time frame, which is typically daily.
- Leveraged ETFs are suitable only for very experienced, aggressive, sophisticated investors who actively manage their investments daily and who understand the risks of using leverage as well as the consequences of investing in securities that use leverage to achieve a daily or monthly objective.
- The performance of leveraged products if held longer than their rebalancing period can differ significantly from the performance (or inverse of the performance) of their target benchmarks or multiple of their target benchmarks over the same period.
- For complete understanding of other risks including correlation, leverage, compounding, market volatility and specific risks regarding each sector, all users should read the prospectus or summary prospectus.

We strongly recommend that all investors that wish to trade leveraged ETFs should proactively indicate (via electronic checkbox or similar method) that they understand these points and consider themselves a suitable user of the products before gaining access to the products for trading. Presenting this certification at the ticker/cusip level is recommended as it will ensure that there is no confusion as to which ETFs seek daily leveraged results.

Portfolio Holdings Screens
We recommend the leveraged/inverse ETF position should carry a footnote link such as the following:

- *Notice to monitor this position frequently*: This ETF seeks daily leveraged investment results and does not seek to achieve its stated objective over a period of time greater than one day. The ETF is designed to be utilized only by knowledgeable investors who understand the potential consequences of seeking daily investment results, the risks associated with the use of leverage and are willing to monitor their portfolio frequently. It's important to monitor this position frequently and rebalance the position in a manner that reflects your exposure and risk tolerance.

Product Page Notice
To continue to remind and differentiate the intricacies of Leveraged ETFs we recommend a prominent link to unique risk overview noted in trade window suggestion above on all product pages.

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Additional Educational Content

Direxion has developed content in several forms (print, video, self-paced learning module) that we believe provides a comprehensive education on leveraged ETFs. We encourage you to reference and utilize this content under your own branding where you feel appropriate. Some examples are shown below and others are available. We are also willing to work with you to develop different or customized materials to help meet your needs. [Click for complete list of educational content]

- **Certification course for understanding unique risks of leveraged ETFs**
  This course is designed to provide you with comprehensive understanding of the composition of leveraged ETFs, the mechanics of how they operate, and the risks associated with them. This course is self-paced and can be completed in one sitting (35 – 60 minutes depending on the existing knowledge of the user), or in multiple sessions. Direxion welcomes all platforms access to this course content to "white label" for incorporating into your sites. A very similar course is also offered by independent securities training course vendor Securities Training Corporation (STC) if you prefer to use their offering.
  You may choose to use this course as a requirement to certify product users before they can gain access to them. The certification could be recorded, providing support regarding investor suitability for your compliance department.
- **Understanding Leveraged ETFs** Educational document available in print form, that explains the composition and risks, with behavioral examples in different market conditions.
- **Leveraged ETF Video Series** - An engaging video depiction of the same points made in the print document mentioned above.
- **Volatility Matters** This content illustrates an actual example of two leveraged ETF's performance in extreme market conditions.

Service and Education Team

We also have a full team of service and support professionals available to help provide support to anyone in your organization. We would welcome a meeting to discuss this with you.

An investor should consider the investment objectives, risks, charges, and expenses of Shares carefully before investing. The prospectus and summary prospectus contain this and other information about Shares. To obtain a prospectus or summary prospectus please visit www.direxioninvestments.com/regulatory-documents. The prospectus and summary prospectus should be read carefully before investing.

There is no guarantee that the funds will achieve their objectives. The Leveraged and Inverse ETFs are not suitable for all investors and should be utilized only by sophisticated investors who understand leverage risk, consequences of seeking Daily leveraged investment results and intend to actively monitor and manage their investments. Investing in the Funds may be more volatile than investing in broadly diversified funds. The use of leverage by a fund means the Funds are riskier than alternatives which do not use leverage.

Risks: An investment in the Funds involves risk, including the possible loss of principal. The Funds are non-diversified and include risks associated with concentration risk that results from the Funds' investments in a particular industry or sector which can increase volatility. The use of derivatives such as futures contracts, forward contracts, options and swaps are subject to market risks that may cause their price to fluctuate over time. The Funds do not attempt to, and should not be expected to, provide returns which are a multiple of the return of the Index for periods other than a single day. For other risks including correlation, leverage, compounding, market volatility, shorting for the Bear funds, and specific risks regarding each sector, please read the prospectus.

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Appendix B

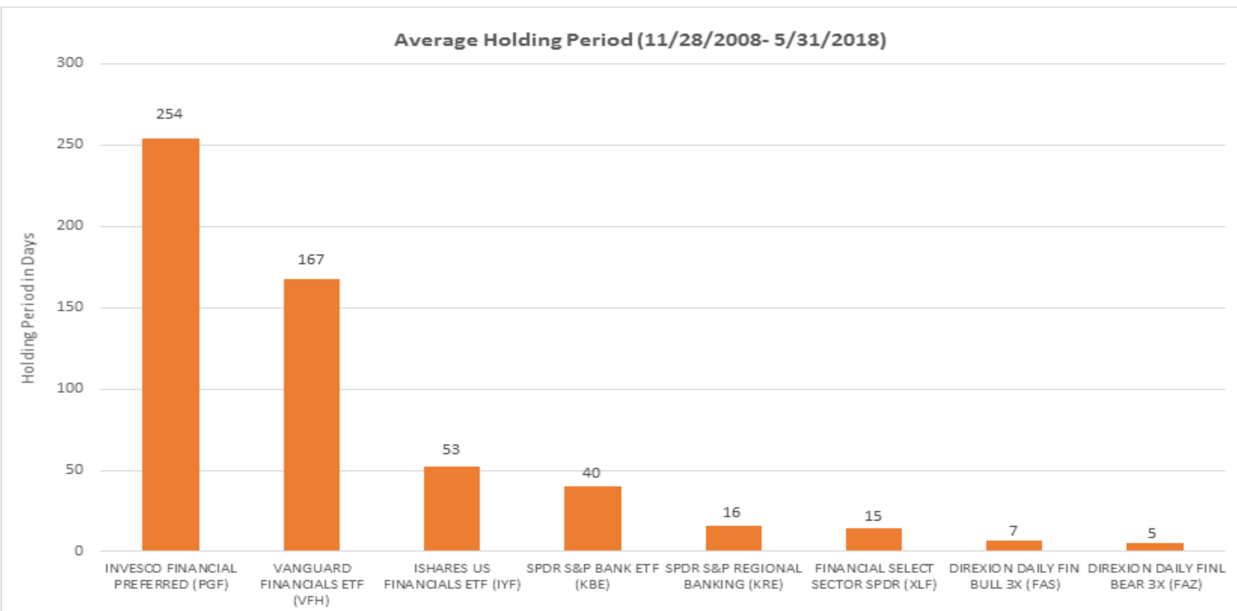
The Available Data Indicates that Investors Understand Leveraged ETFs and Properly Use Them

Direxion (like all ETF sponsors) has access to almost no information about Direxion Shares investors or the activity in any particular (group of) Direxion shareholder's account. Accordingly, Direxion uses publicly available data to confirm that investors understand and are properly using the products. One key measure Direxion reviews in this regard is the average holding period of Direxion Shares as compared to the average holding period of traditional index-based ETFs. As shown in the table below, for calendar year 2017, the average holding period of traditional index-based ETFs dwarfed that of Direxion Shares; and the statistics for the first half of 2018 are substantially the same.[41]

Year	Average Holding Period of Traditional ETFs	Average Holding Period of Leveraged ETFs
2017*	155 days	11 days
2018**	136 days	8 days

*Calculation for January 1 through December 31, 2017 of 754 ETFs.
**Calculation for January 1 through May 31, 2018 of 738 ETFs.

More detailed information on a select group of comparable ETFs is show in the bar graph below.



41 Source: Bloomberg (calculation based on average asset and average daily turnover information for U.S. domiciled ETFs with $100 million or more AUM). *But see* Jackson Statement ("the relatively little evidence we have with respect to holding periods seems to point in the opposite direction") (citing Ilan Guedj, Guohua Li and Craig McCann, Leveraged ETFs, Holding Periods and Investment Shortfalls 12 (2010) ("[t]he percentage of investors that we estimate hold these short term investors longer than a month is quite striking")).

The table and graph uniformly show that average holdings periods for Direxion Shares are substantially shorter than average holding periods for traditional index-based ETF shares.

Further, the average holdings periods of Direxion Shares decrease as the volatility of the relevant market (*i.e.,* the benchmark index of the ETF) increases.

			Since Inception-May 31, 2018		**February 2018**		**Low Vol. (Calendar Year 2017)**		**Taper Tantrum (May 22, 2013-July 1, 2013)**		**Launch and Post Financial Crisis (December 1, 2008- December 31, 2009)**	
Direxion ETFs	Inception Date	Average Assets YTD May 31, 2018	Avg. Holding Period (Days)	Index Vol.	Avg. Holding Period	Index Vol.	Avg. Holding Period (Days)	Index Vol.	Avg. Holding Period (Days)	Index Vol.	Avg. Holding Period (Days)	Index Vol.
S&P 500 Bear 3X	11/5/2008	$282,431,353	5.0	18.09	1.5	27.24	11.0	6.79	4.5	15.95	1.2	32.31
S&P 500 Bull 3X	11/5/2008	$1,080,844,275	4.2	18.09	3.3	27.24	11.1	6.79	2.7	15.95	0.7	32.31
Financial Bull 3X	11/6/2008	$1,974,180,809	6.5	29.03	11.6	28.36	15.5	9.77	2.0	19.07	0.6	66.28
Financial Bear 3X	11/6/2008	$138,836,883	5.0	29.03	5.6	28.36	10.8	9.77	2.1	19.07	0.7	66.28

Source: Bloomberg (Average Holding Period calculation based on average asset and average daily turnover information.) (Index Vol. calculation based on sample standard deviation of the daily index returns multiplied by the square root of the number of periods in one year.)

All of this data supports our view that Direxion investors understand and appropriately use the products.

It has been suggested, however, that average holding period data may be skewed by a (small) group of active traders who trade in and out of shares of the same leveraged ETFs multiple times over the course of the same day.[42] While we acknowledge this possibility, we are not aware of any empirical data to support it.[43]

Further, additional data suggests that Direxion investors monitor their portfolios regularly. In this regard we note that – unlike more traditional ETFs and funds – assets do not flow into the Direxion ETFs following positive performance periods. In fact, when a Direxion ETF's performance has been positive, the Direxion ETF will face net redemptions approximately 60% of the time.

42 *See* Jackson Statement ("The first is that the average holding period for leveraged ETFs is, in fact, relatively short. That may be, since sophisticated institutions trade these products at high speed, but my concern is not about the average holding period in leveraged ETFs.").

43 We are heartened, however, by the Commission's focus on data and would look forward to reviewing such data in partnership with the Commission and Staff. *See generally,* Jackson Statement ("We hope to… study this question – starting with hard empirical data that can tell us whether there are a significant number of retail investors who are exposed to the risks [] described").

Direxion ETFs | Funds

Similarly, when a Direxion ETF's performance has been negative, the ETF will have net purchases approximately 60% of the time.[44]

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[44] Source: Bloomberg for performance and Bank of New York Mellon for Direxion ETF creation and redemption transactions.

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ETFs | Funds

Appendix C

The graphical "heat maps" below are for the five longest operating Direxion Bull ETFs. Each heat map summarizes an investor's potential investment return at NAV for every possible holding period since the cited ETF's inception date.[45] On each heat map, one pixel of color represents the return of one potential holding period for the ETF (*i.e.*, a single, point-in-time-to-point-in-time return) less the return of a Comparison (as defined below). The green shaded pixels reflect holding periods for which the cited ETF's return exceeded the Comparison; red-shaded pixels represent holding periods for which the ETF's return fell short of the Comparison.

Also included are two "Comparisons" for each analyzed Direxion Bull ETF.[46] The first Comparison compares an investor's return in the Direxion Bull ETF for the holding period to a zero percent return; accordingly, red pixels represent a loss in absolute terms, and green pixels represent a gain in absolute terms. The second Comparison compares an investor's return in the Direxion Bull ETF for the holding period to the (frictionless) return of the ETF's unleveraged, benchmark index; accordingly, red pixels represent a return lower than that of the unleveraged, benchmark index (although potentially still an absolute positive return), and green pixels represent a return in excess of the unleveraged, benchmark index (although potentially still a loss in absolute terms).

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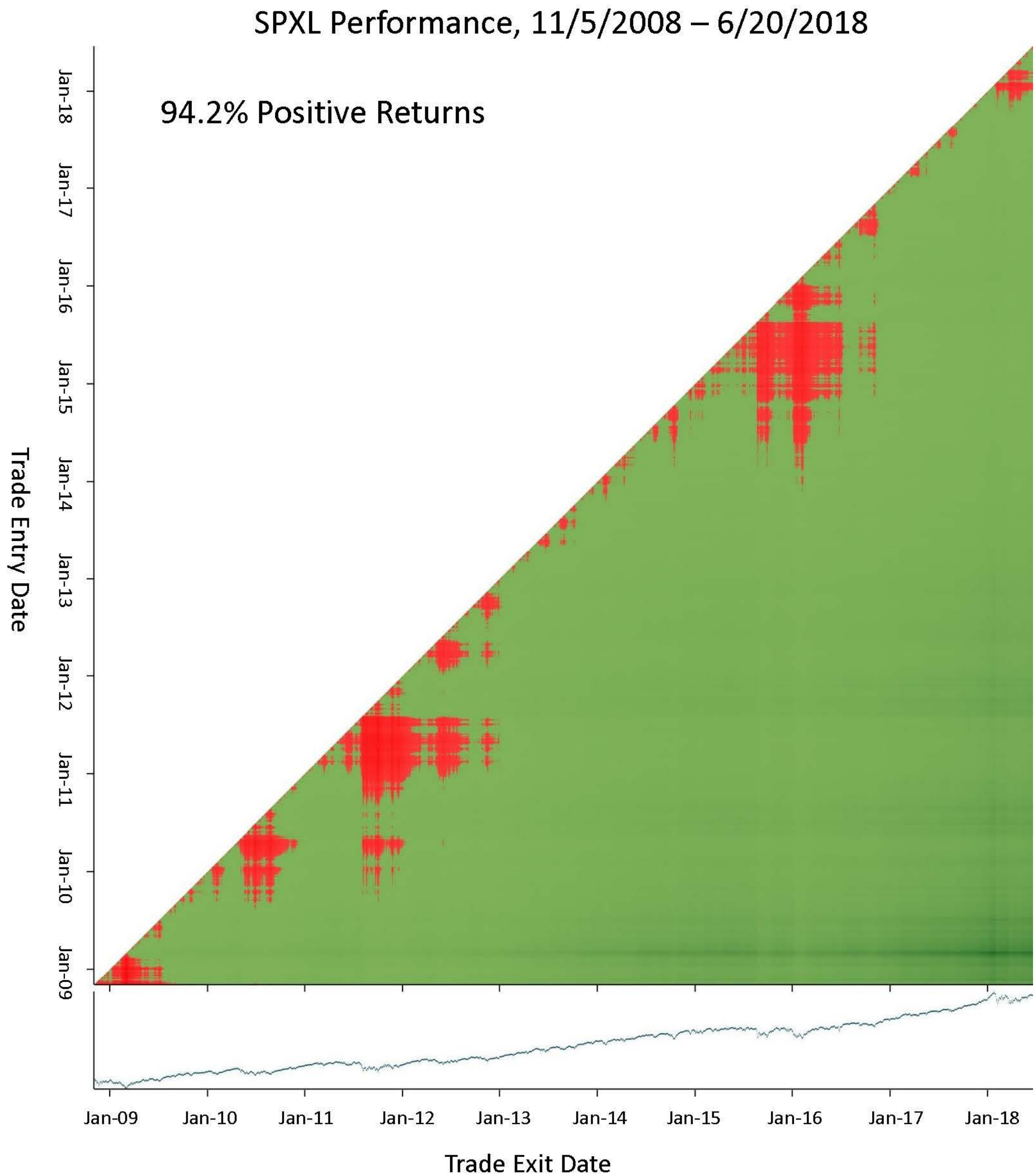
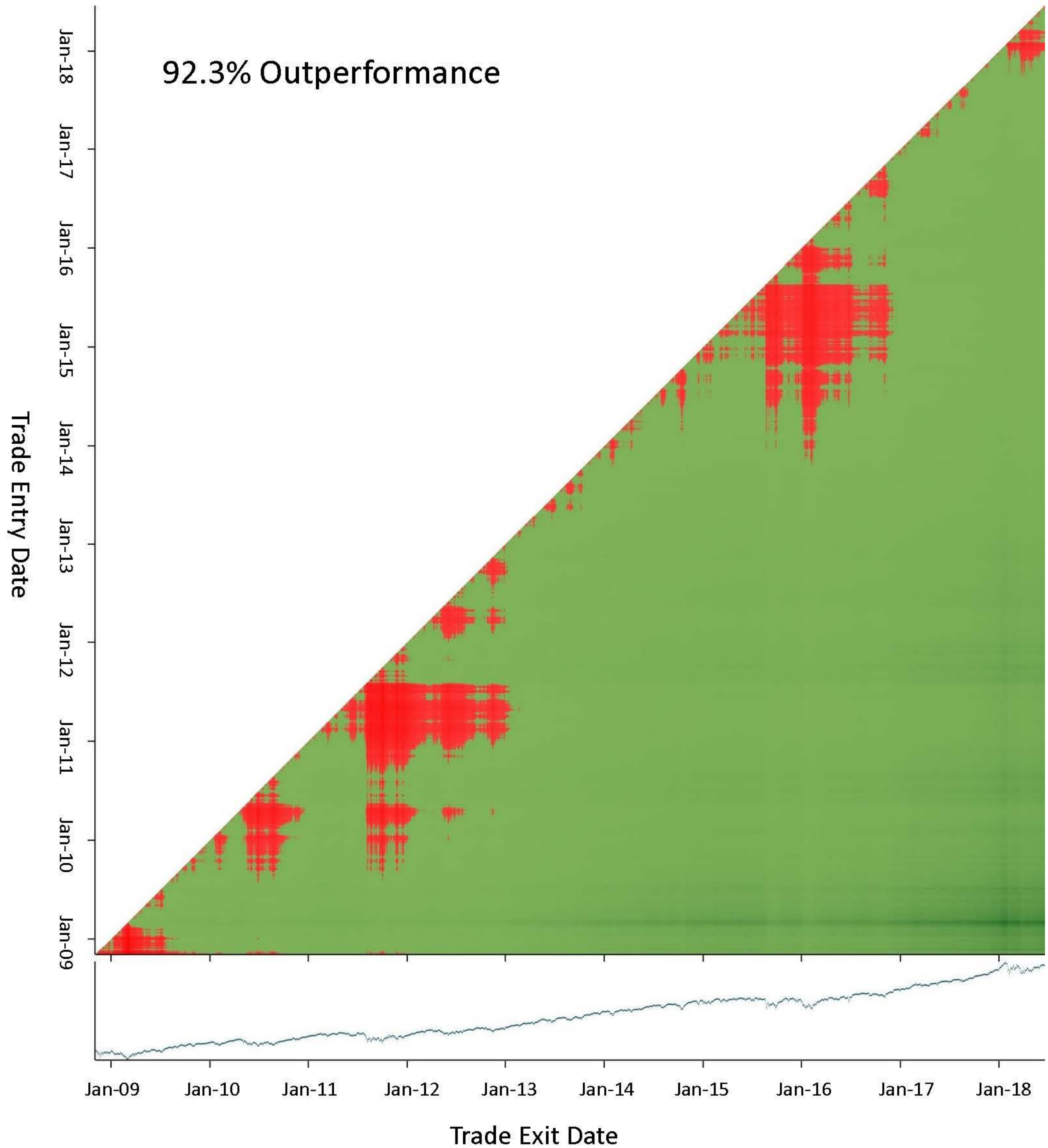
45 Although investors do not transact at NAV but rather at an intra-day market price, we do not have access to such intra-day market data, and the theoretical return permutations based on intra-day market pricing would run into the trillions. Accordingly, we have not sought to provide such data here. Furthermore, investors who hold leveraged ETF shares over extended periods experience the returns at NAV for all but the first and last day of the period. Accordingly, we believe that the heat maps provided present a realistic picture, based on millions of data points, of the investment experience of longer term investors in our products.

46 We can also provide data regarding the Bear ETFs for the same period. We have not done so here because investor losses in the Direxion Bear ETFs were not driven primarily by compounding and volatility, but rather by investors having invested in ETFs that employed short market strategies, whether for hedging purposes or otherwise, in a rising market.

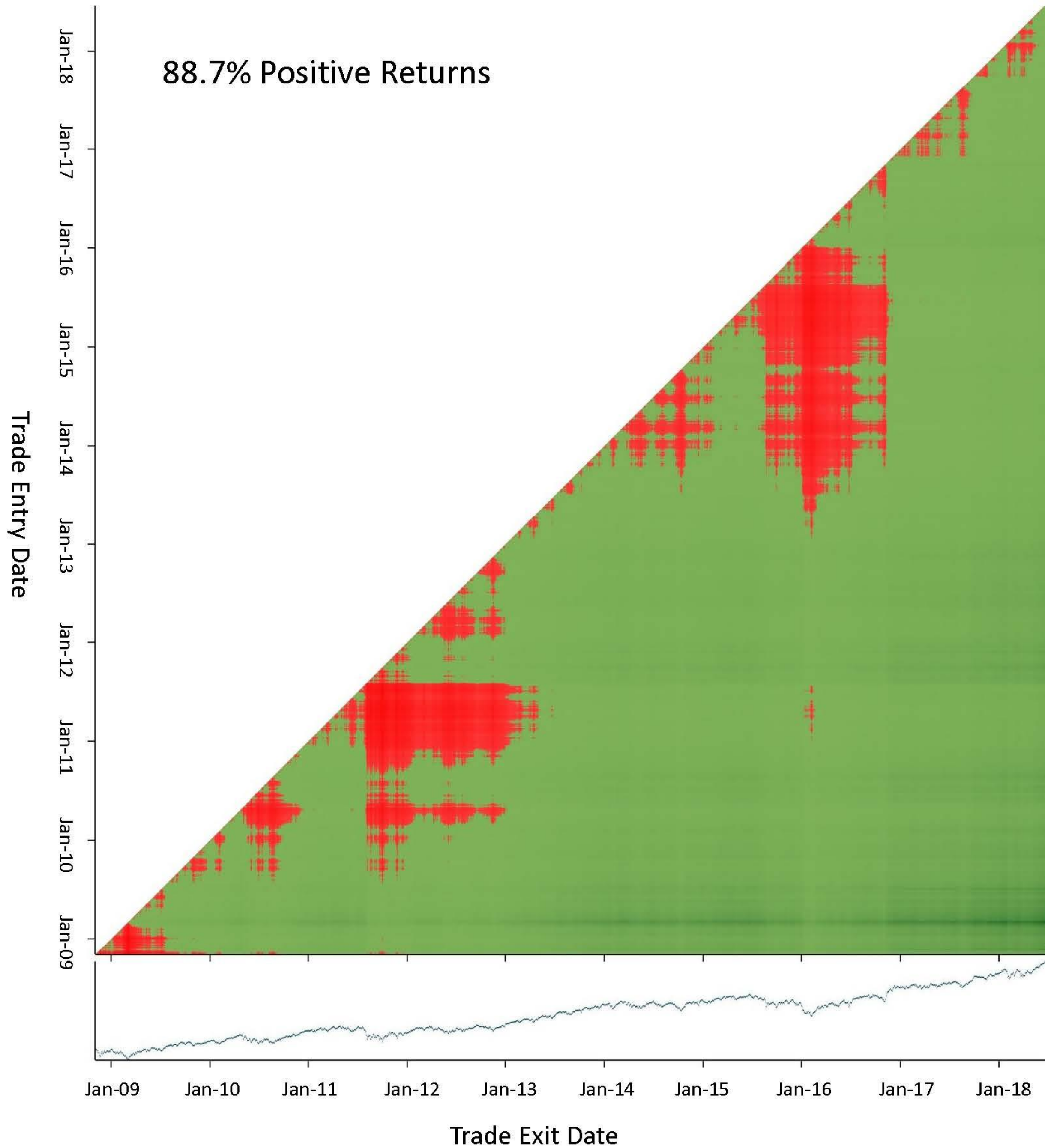


SPXL Performance, 11/5/2008 – 6/20/2018
94.2% Positive Returns
Trade Entry Date
Jan-09
Jan-10
Jan-11
Jan-12
Jan-13
Jan-14
Jan-15
Jan-16
Jan-17
Jan-18
Trade Exit Date

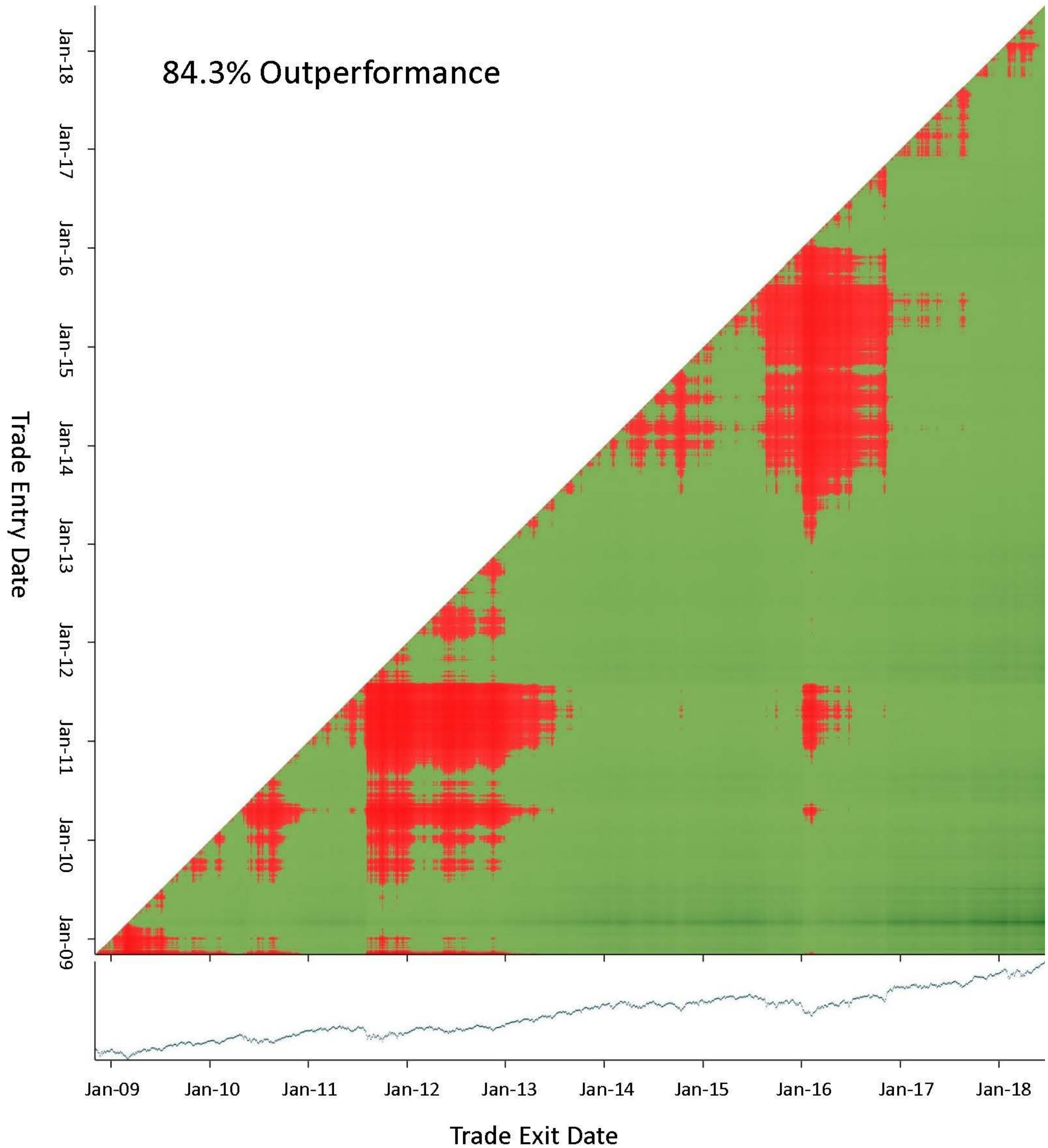
SPXL Outperformance vs. Unlevered Benchmark,
11/5/2008 – 6/20/2018



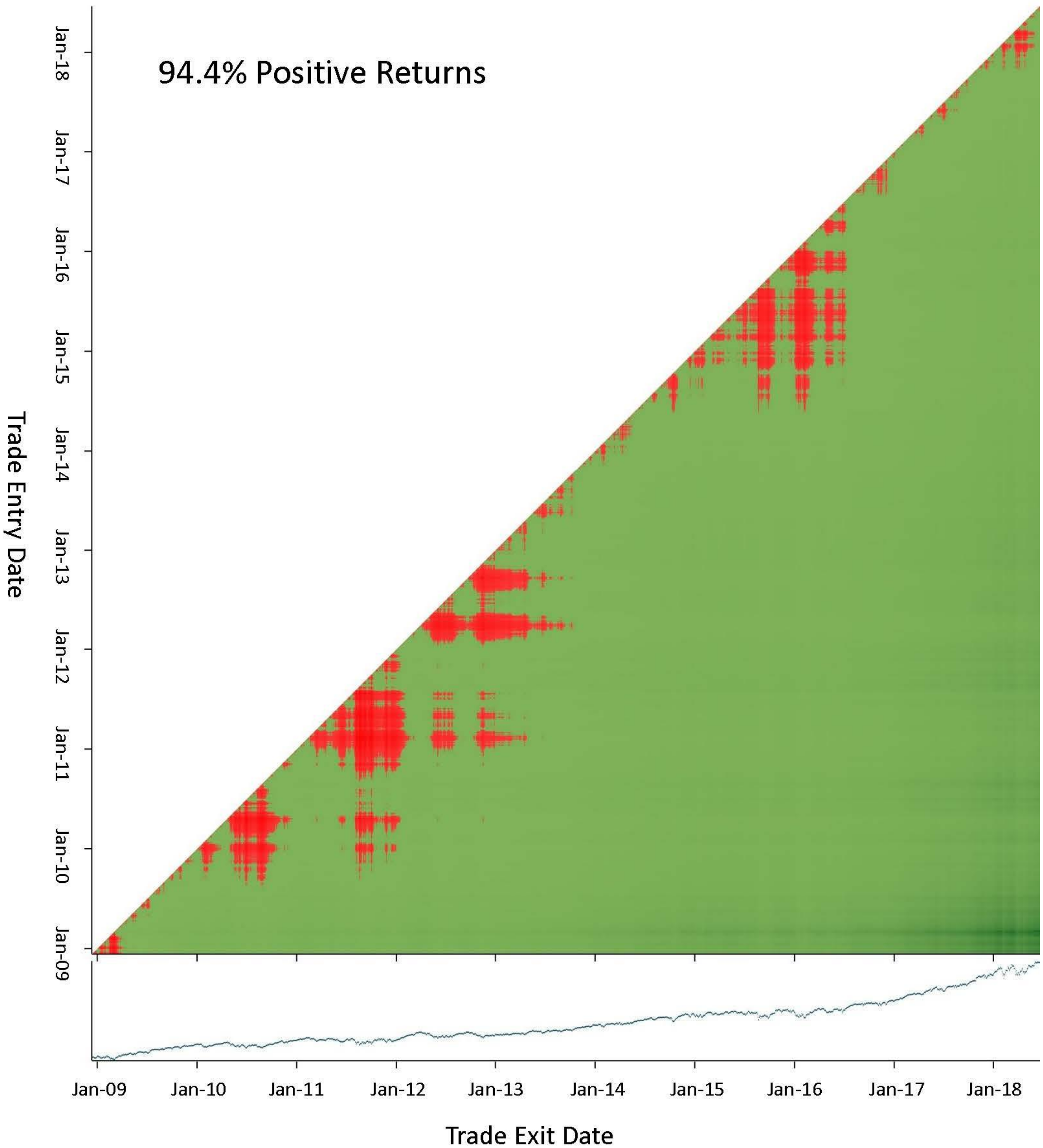
TNA Performance, 11/5/2008 – 6/20/2018



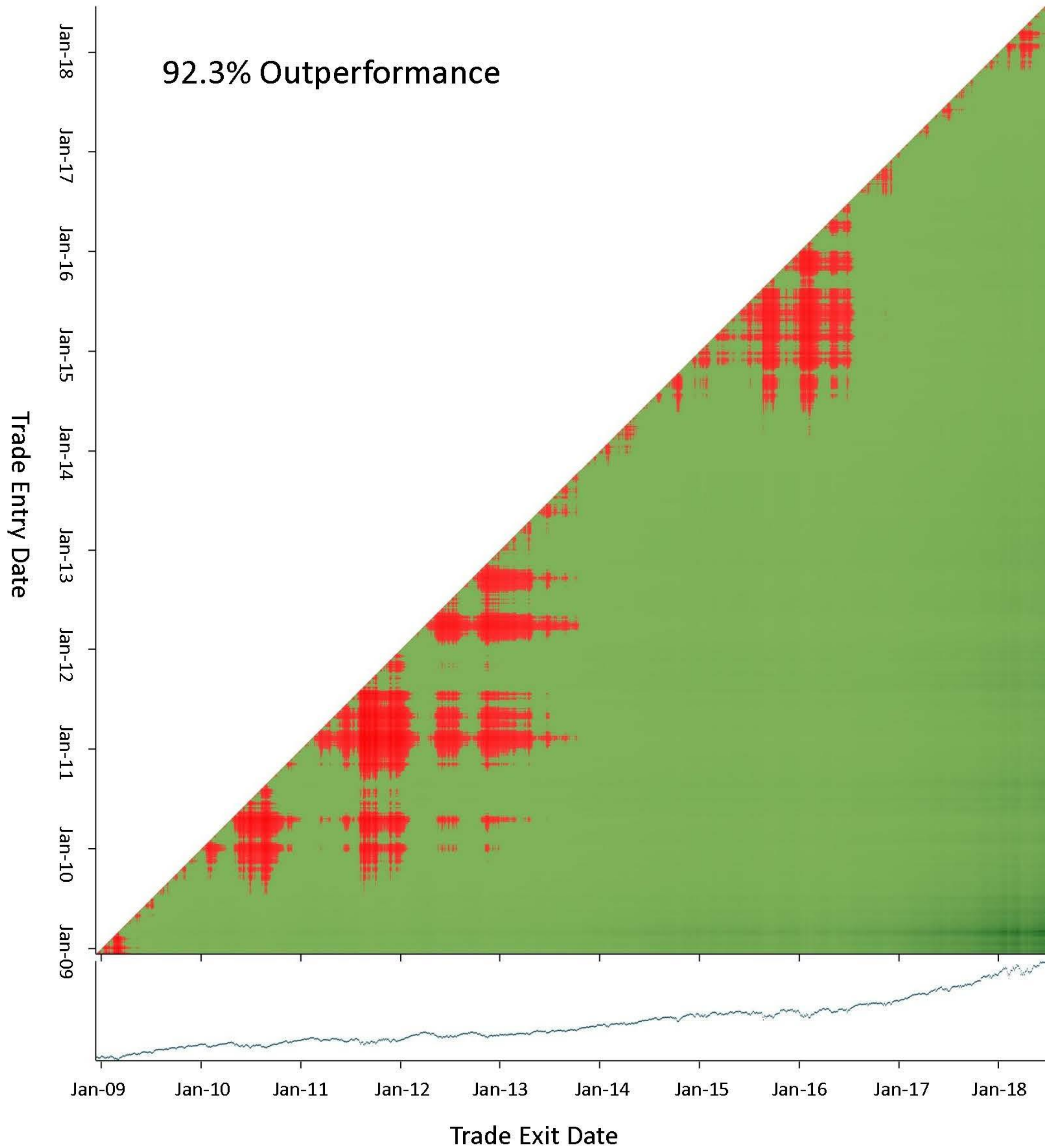
TNA Outperformance vs. Unlevered Benchmark,
11/5/2008 – 6/20/2018

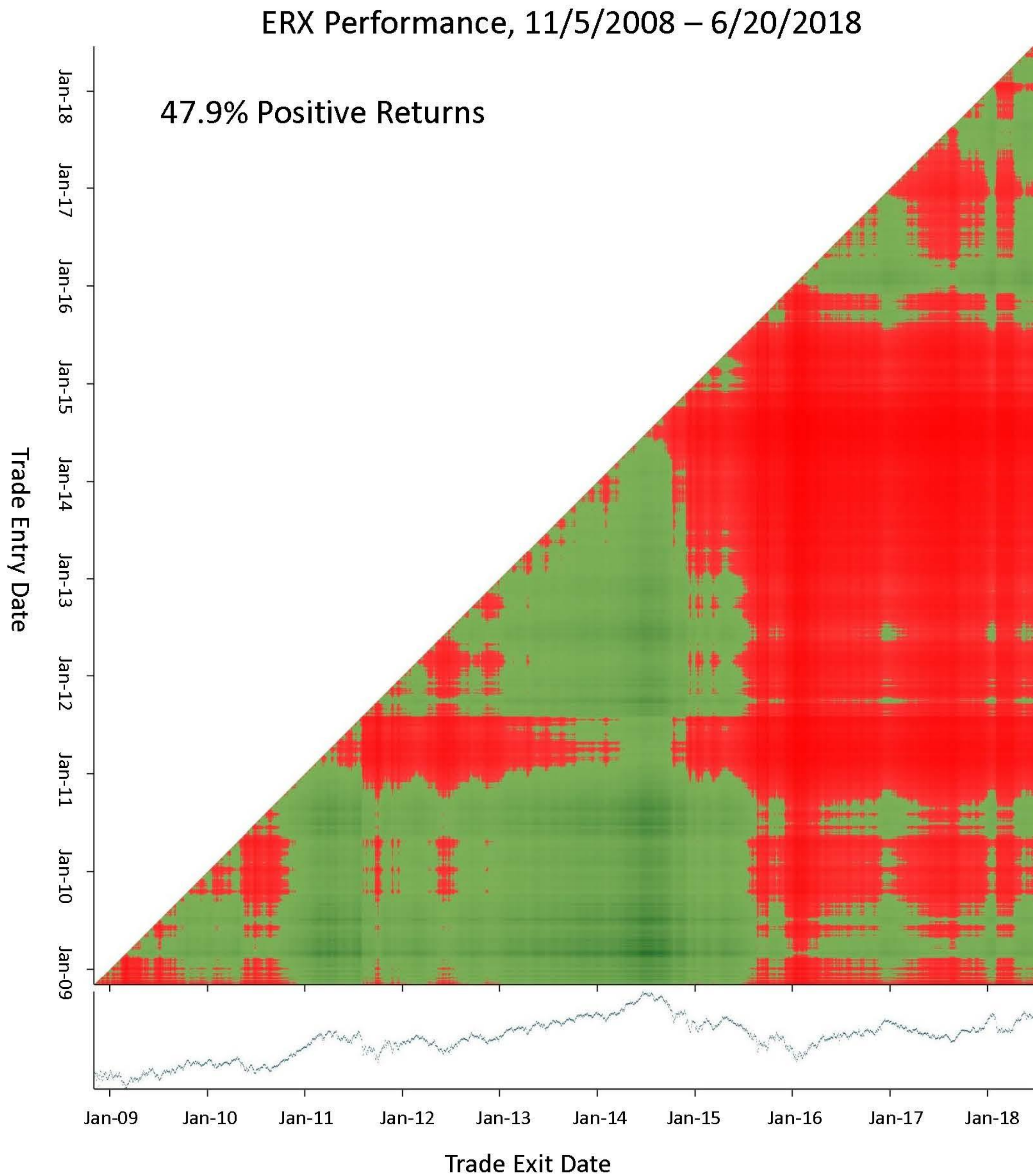


TECL Performance, 12/15/2008 – 6/20/2018

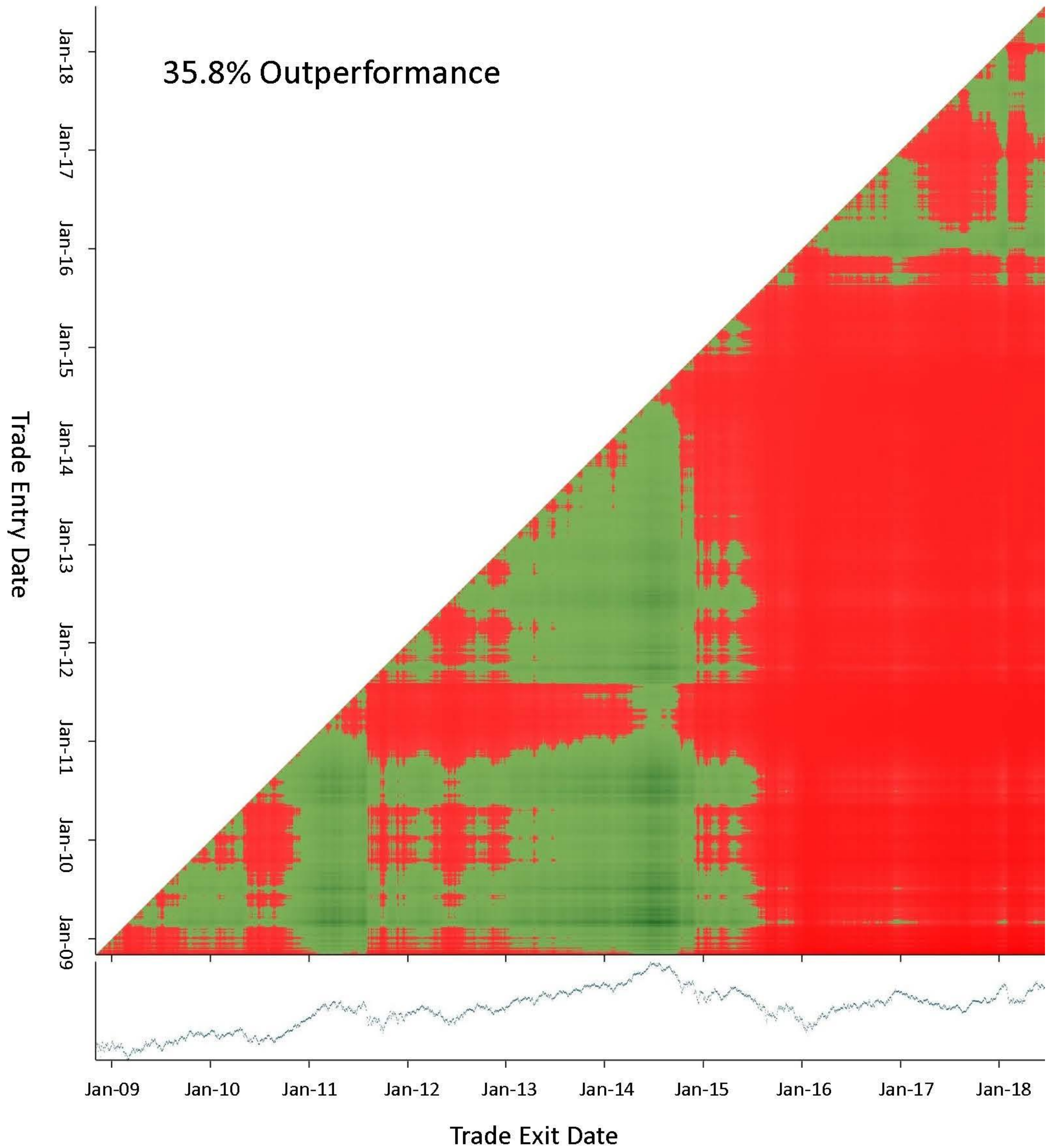


TECL Outperformance vs. Unlevered Benchmark, 12/15/2008 – 6/20/2018

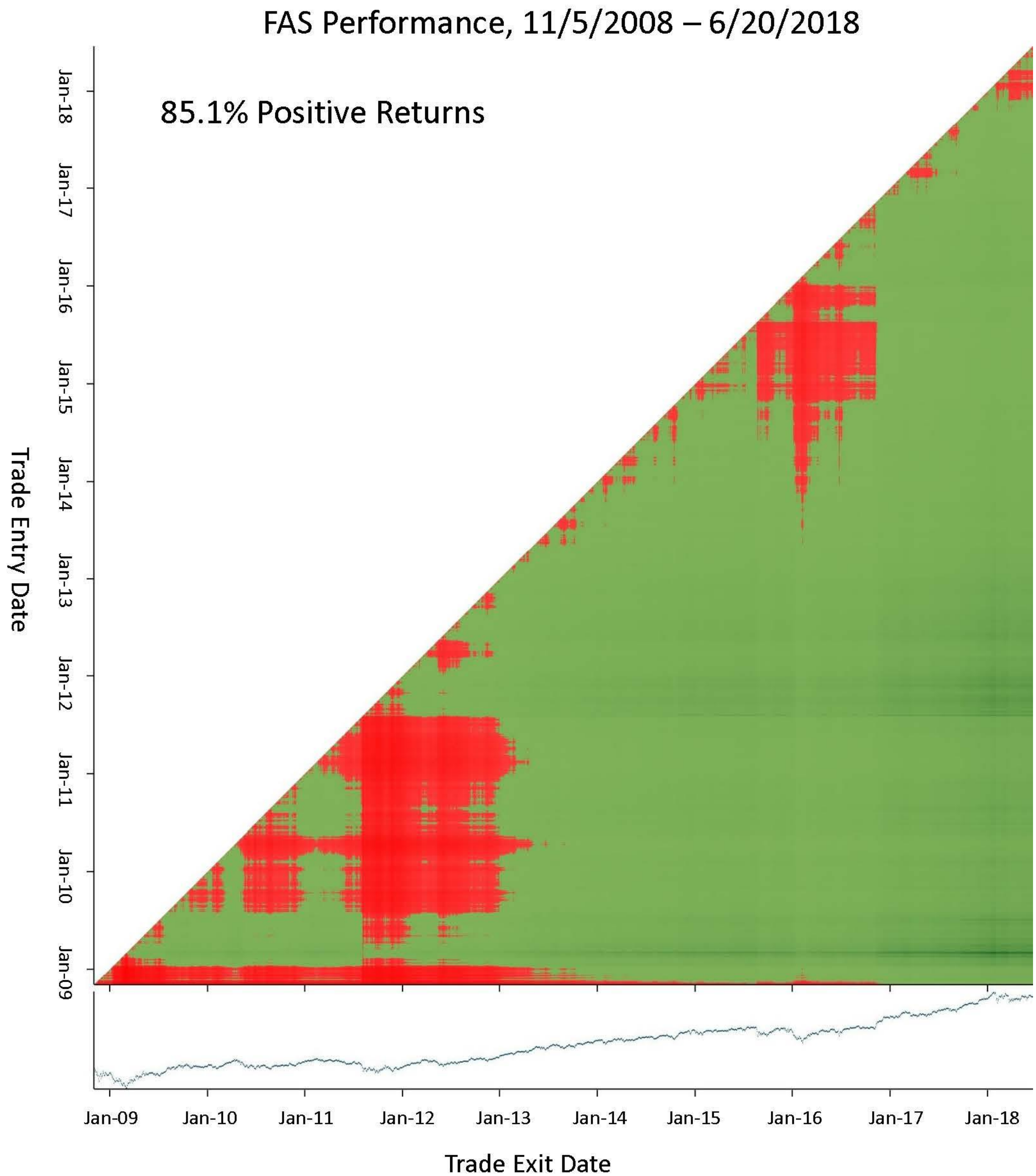



ERX Performance, 11/5/2008 – 6/20/2018
47.9% Positive Returns
Trade Entry Date
Jan-09
Jan-10
Jan-11
Jan-12
Jan-13
Jan-14
Jan-15
Jan-16
Jan-17
Jan-18
Trade Exit Date

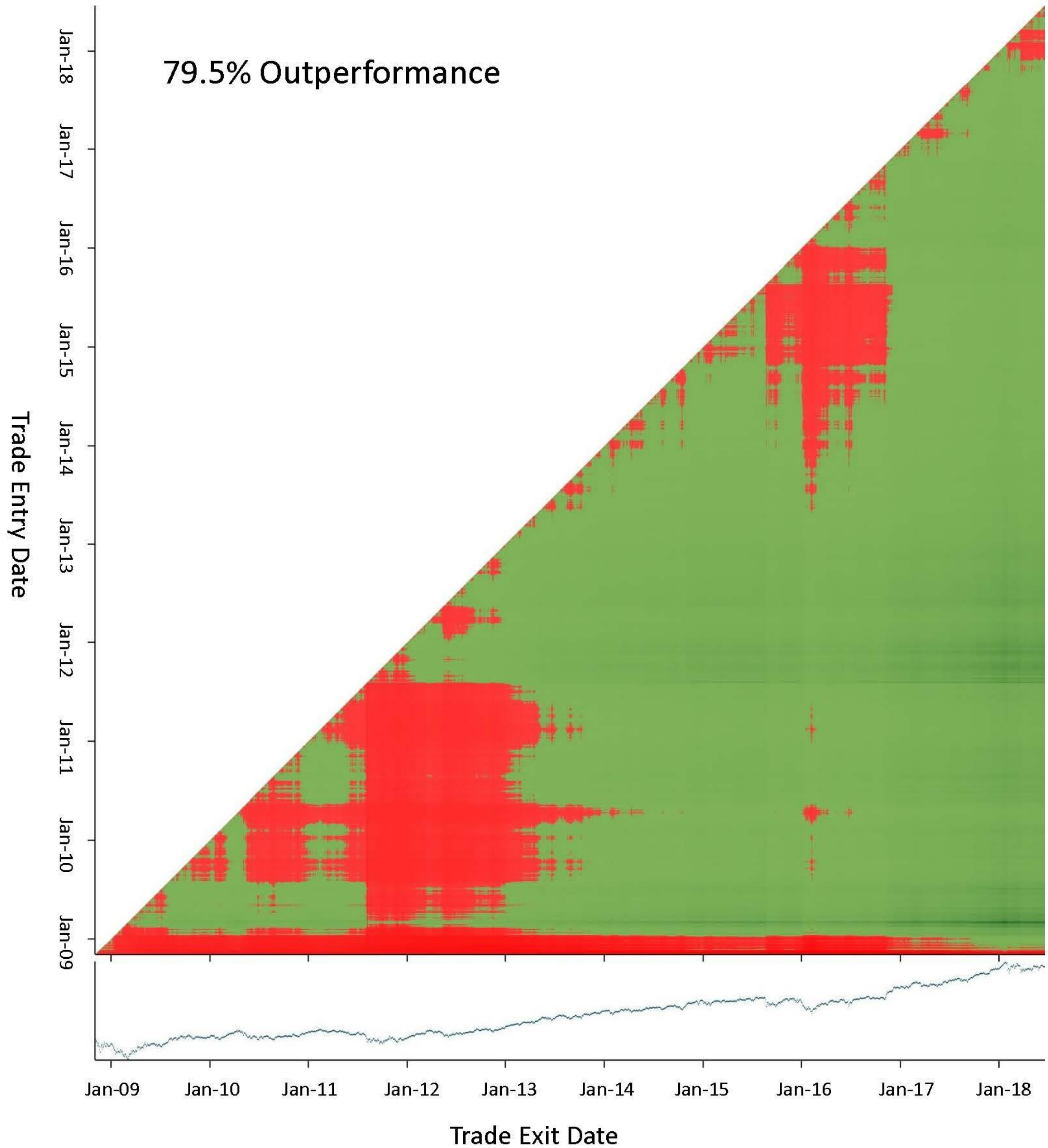
ERX Outperformance vs. Unlevered Benchmark, 11/5/2008 – 6/20/2018



Direxion ETFs | Funds



FAS Outperformance vs. Unlevered Benchmark,
11/5/2008 – 6/20/2018



The following table summarizes the data reflected in the heat maps above.

Direxion ETF	Period of Observation	Percentage of Pixels Reflecting A Positive Return Versus 0%	Percentage of Pixels Representing A Positive Return Versus Unleveraged, Underlying Index
Daily S&P 500 Bull 3X Shares (SPXL)	11/5/08-6/20/18	94.2%	92.3%
Daily Small Cap Bull 3X Shares (TNA)	11/5/08-6/20/18	88.7%	84.3%
Daily Technology Bull 3X Shares (TECL)	12/15/08-6/20/18	94.4%	92.3%
Daily Energy Bull 3X Shares (ERX)	11/5/08-6/20/18	47.9%	35.8%
Daily Financial Bull 3X Shares (FAS)	11/5/08-6/20/18	85.1%	79.5%

Source: Bloomberg