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May 13, 2020

Sent via email

We are writing on behalf of BlackRock, Inc., Charles Schwab Investment Management, Inc., Fidelity Investments, Invesco Ltd., State Street Global Advisors and The Vanguard Group, Inc. to ask for Exchanges support in implementing a solution to categorize certain exchange traded investment products ("ETPs") in a manner that more accurately reflects their inherent complexities, risks and structural features, as more fully described below.

Background:

Investors' use of exchange traded funds ("ETFs") has advanced dramatically since the first United States ETF launch in 1993. Both institutional and retail investors have recognized that "traditional" ETFs that track stock or bond indices or baskets of assets offer a diversity of potential investment exposures at low cost, along with outstanding transparency and exchange liquidity. Globally, ETF assets under management have expanded from $79 billion in 2000 to $5.1 trillion in March 2020. In the United States markets, ETF assets under management have grown from approximately $70 billion in 2000 to approximately $3.5 trillion by March 2020. During this same period, the number of ETF products outstanding on United States Exchanges has grown from 95 to over 2,000.[1]

As of December 2018, retail investors represent approximately 37% of outstanding US ETF AUM, with institutional investors such as banks, insurance companies and investment funds representing the balance.[2]

The Need for Appropriate Identification and Categorization of Exchange Traded Products:

The rapid growth of ETF assets under management demonstrates that both retail and institutional investors have found ETFs to be an attractive investment product. However, along with this growth, the market has also seen a proliferation of more structurally complex ETPs as well as ETPs with different risk profiles and more narrowly tailored investment objectives. Examples of these more complex ETPs include products such as exchange traded notes ("ETNs") and levered and inverse ETPs.

Notwithstanding that these ETPs pose very different risks to holders than traditional index or basket tracking ETFs, many use the term ETF to describe their offerings. Likewise, many Exchanges categorize or otherwise identify these products as ETFs without distinction to their very different risk profiles. In fact, "ETF" has become a blanket term used by product sponsors, Exchanges, investors, the financial press and even regulators to describe many products that have a wide range of different structures and risks.[3]

[1] Markit, BlackRock as of April 27, 2020. Excludes exchange-traded commodity, exchange-traded note, exchange-traded mutual fund and NextShares assets.
[2] Deutsche Bank, "Who Uses ETFs & Why: The DB Institutional ETF Ownership Guide" (May 2019).
[3] See, for example, Rachel Evans and Carolina Wilson, "The ETF's Wonky Cousin Can Trip Up a Sophisticated Investor" Bloomberg February 4, 2019; and Simon Constable, "Could Some VIX-

We note that the Financial Industry Regulatory Authority ("FINRA") has previously issued guidance on sales practices related to ETFs that offer leverage and/or that are designed to perform inversely to the index or benchmark they track.[4] FINRA's guidance in this area has reminded its member firms of the importance of their sales practice obligations in connection with leveraged and inverse ETPs. Moreover, the Securities and Exchange Commission recently proposed a rule governing sales practices for broker-dealers and investment advisers relating to these types of products.[5]

This regulatory focus as well as certain recent market events serve to underscore the importance of ensuring our markets operate in a manner that ensures investors understand the very different risks and considerations that these increasingly complex ETPs pose to investors. For example, crude oil market declines in April 2020 and the equity market sell-off in February 2018 highlight the different risk profiles associated with different types of ETPs and amplify the potential pitfalls of investor confusion around the nature of the product identification as an ETF. In April 2020, the dramatic decline in oil prices resulted in a 3x levered long crude oil-linked exchange-traded note being delisted with an expected value of zero dollars per note.[6] Likewise, a steep drop in equity benchmarks in February 2018 coinciding with a large one-day increase in the VIX level resulted in several inverse VIX ETPs suffering declines in excess of 90%.[7]

In our view, there is a need for clearer identification and categorization of ETPs in order to help ensure that investors understand that certain ETPs have greater embedded market and structural risks and more complexity than others.

Specifically, we believe that certain ETPs with complex structures and/or certain embedded risks should be identified and categorized by Exchanges at the data feed level (via exchange listing rules or otherwise) as exchange-traded notes ("ETNs"), exchange-traded commodities ("ETCs") or exchange-traded instruments ("ETIs") rather than as ETFs. Set forth below are definitions of ETF, ETN, ETC and ETI that we believe appropriately describe these products.

Related Funds Go Poof in a Day" Wall Street Journal September 4, 2017 (identifying an ETN as a "fund").

[4] See FINRA Regulatory Notice 09-31.

[5] See SEC Release No. 34-27607

[6] The price decline reflected the embedded economics and risks of this ETN; it performed as expected but with volatility and market risks significantly different than unlevered index tracking ETFs. Barclays exercised its issuer call option, which allows the issuer to call the ETN at its discretion. See Barclays Press Release (April 20, 2020), *Barclays announces the redemption of the iPath® Series B S&P GSCI® Crude Oil Total Return Index ETNs ("the ETNs") and the suspension of further sales and issuance of the ETNs*, available at https://barxis.barcap.com/file.app?action=shared&path=iPath/US/Press/Barclays%20suspends%20further%20creations%20for%20OIL%20ETN.pdf

[7] While these products performed as designed, the dramatic jump in the VIX prompted the closure of an inverse VIX ETN by its sponsor under the terms detailed in the ETN's prospectus (a so-called "event acceleration"). See Credit Suisse AG Press Release (Feb. 6, 2018), *Credit Suisse AG Announces Event Acceleration of its XIV ETNs*, available at https://www.credit-suisse.com/corporate/en/articles/media-releases/credit-suisse-announces-event-acceleration-xiv-etn-201802.html

Categories of Exchange-Traded Products:

ETF	**Exchange-Traded Fund**	• A registered open-end management investment company under the Investment Company Act (operating under Rule 6c-11 or an applicable SEC ETF exemptive order) that: (i) in the normal course issues (and redeems) creation units to (and from) authorized participants in exchange for a basket and a cash balancing amount (if any); and (ii) issues shares that are listed on a national securities exchange and traded at market-determined prices; • Includes funds that transact on an in-kind basis, on a cash basis, or both; and • Excludes ETNs, ETCs and ETIs (as defined below).
ETN	**Exchange-Traded Note**	• A debt security issued by a corporate issuer (i.e., not issued by a pooled investment vehicle) that is linked to the performance of a market index and trades on a securities exchange; • May or may not be collateralized, but in either case, depends on the issuer's solvency to deliver fully to expectations; and • Excludes products that seek to provide a leveraged or inverse return, a return with caps on upside or downside performance or "knock-out" features.
ETC	**Exchange-Traded Commodity**	• A pooled investment vehicle with shares that trade on a securities exchange that invests primarily in assets other than securities and financial futures; • The primary investment objective of an ETC is exposure to traditional commodities and non-financial commodity futures contracts; and • May hold physical commodities (e.g., precious metals) or invest in non-financial commodity futures or commodity-based total return swaps.
ETI	**Exchange-Traded Instrument**	• Any pooled investment vehicle, debt security issued by a corporate issuer, or similar financial instrument that trades on a securities exchange that has embedded structural features designed to deliver a return other than the full unlevered positive return of the underlying index or exposure (for example, products that seek to provide a leveraged or inverse return, a return with caps on upside or downside performance or "knock-out" features); or • All products not captured by the ETF, ETN or ETC classification fall under ETI.

It is important that Exchanges, in its regulatory and oversight role, play a part in helping to ensure that complex and levered products are not confused with more traditional investment products which are widely used by retail investors to access the stock, bond and other markets. Proper identification and categorization of ETFs, ETNs, ETCs and ETIs will better enable investors to make informed investment decisions with respect to exchange-traded products and ensure the continued growth of ETFs as an efficient, cost-effective and non-complex tool for investors to access markets.

We appreciate Exchanges support in this initiative and look forward to working together to implement a solution.

Sincerely,

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About SPDR Exchange Traded Funds
SPDR ETFs are a comprehensive family spanning an array of international and domestic asset classes. SPDR ETFs are sponsored by affiliates of State Street Global Advisors. The funds provide investors with the flexibility to select investments that are aligned to their investment strategy. Recognized as an industry pioneer, State Street created the first US listed ETF in 1993 (SPDR S&P 500® – Ticker SPY) and has remained on the forefront of responsible innovation, as evidenced by the introduction of many ground-breaking products, including first-to-market launches with gold, international real estate, international fixed income, and sector ETFs. For more information, visit www.ssga.com/etf.

About State Street Global Advisors
For four decades, State Street Global Advisors has served the world's governments, institutions and financial advisors. With a rigorous, risk-aware approach built on research, analysis and market-tested experience, we build from a breadth of active and index strategies to create cost-effective solutions. As stewards, we help portfolio companies see that what is fair for people and sustainable for the planet can deliver long-term performance. And, as pioneers in index, ETF, and ESG investing, we are always inventing new ways to invest. As a result, we have become the world's third-largest asset manager with US $2.69 trillion* under our care.

**This figure is presented as of March 31, 2020 and includes approximately $51.62 billion of assets with respect to SPDR products for which State Street Global Advisors Funds Distributors, LLC (SSGA FD) acts solely as the marketing agent. SSGA FD and State Street Global Advisors are affiliated.*

Important Information

Investing involves risk including the risk of loss of principal.

ETFs trade like stocks, are subject to investment risk, fluctuate in market value and may trade at prices above or below the ETFs net asset value. Brokerage commissions and ETF expenses will reduce returns.

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Expiration date: 05/31/2021