



THE EXPANDED

ETF

ECOSYSTEM

Transparent and Semi-Transparent ETFs



INTRODUCTION

The exchange-traded fund (“ETF”) ecosystem consists of a web of interlocking entities and relationships that help ensure ETFs can be bought and sold smoothly throughout the day. A key feature of traditional ETFs has been their transparency—the fact that they disclose their holdings each day—but with the introduction of new structures and models, this is beginning to change.

As the ETF universe has continued to grow, new entrants to the space and new approaches to ETF structures have received SEC approval, including semi-transparent ETFs. These new ETFs selectively disclose portfolio holdings information to the public on a schedule similar to traditional actively-managed mutual funds while still striving to maintain market and net asset value parity. This is accomplished through the use of alternative methods of signaling the value of an ETF’s portfolio to the market.

The goal of this guide is to serve as a comprehensive companion to the expanded ETF ecosystem, encompassing both traditional passive ETFs as well as these new semi-transparent models that are beginning to see the light of day.



Part 1

The Original Transparent ETF Ecosystem

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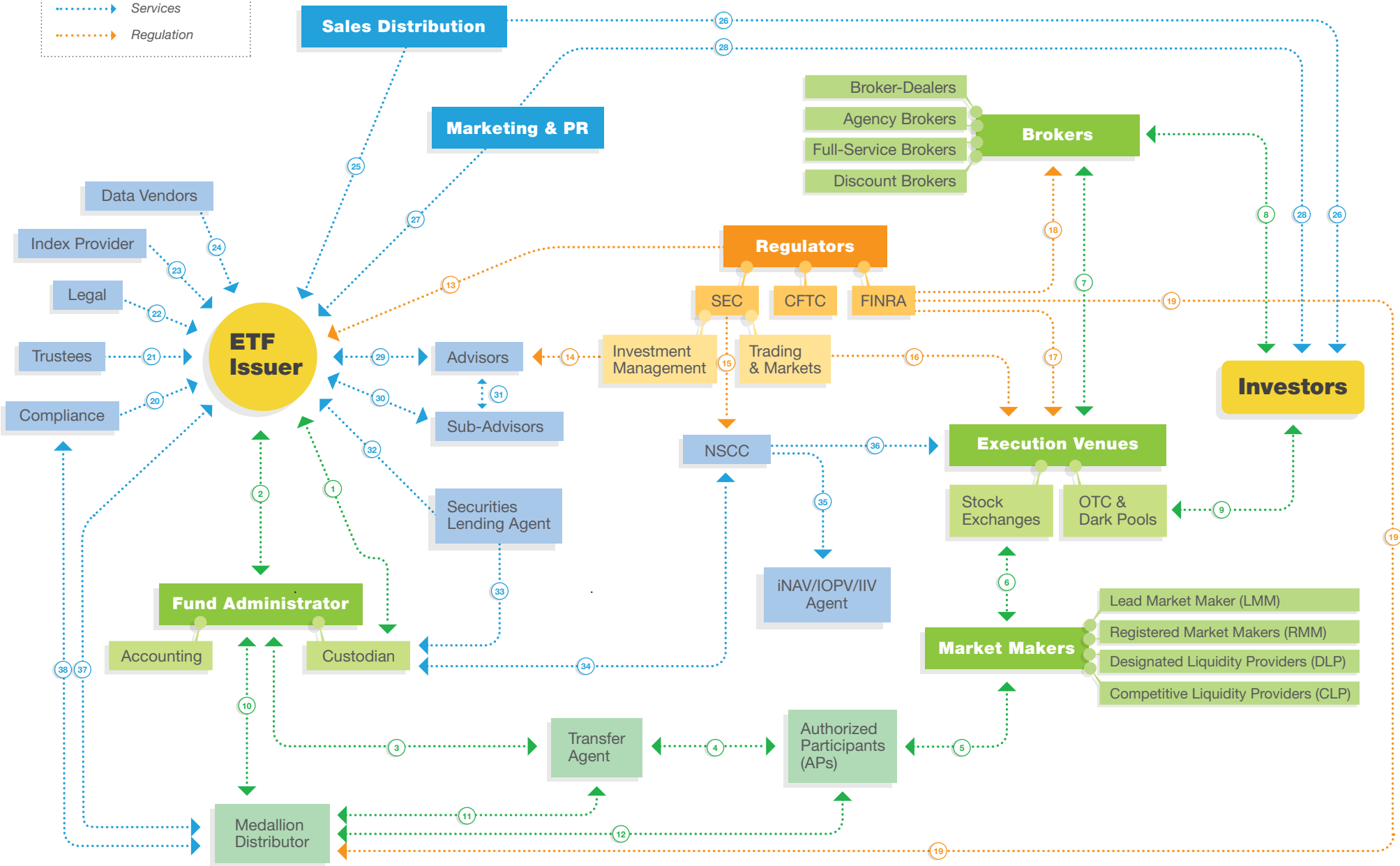
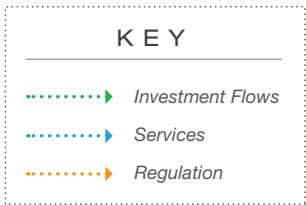
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THE ORIGINAL TRANSPARENT ETF ECOSYSTEM



Please see following page for step descriptions. For full definitions of ecosystem entities, please see the glossary on pages 14 and 15.



KEY

- 1 The **ETF issuer** communicates the fund's market trades as well as details of the creation/redemption basket to the **Custodian**, who in turn provides safekeeping of the assets, as well as providing the ETF Issuer with an aggregate snapshot of the portfolio.
- 2 The **ETF Issuer** and **Accounting/Custody** work together to process and settle creation/redemption activity when there are orders.
- 3 When a creation or redemption order is processed, **Accounting/Custody** processes the underlying basket and the transfer agent processes the ETF shares.
- 4 In some operating models, the **Authorized Participant** places orders on the **Primary Market** with the **Transfer Agent** instead of directly with the **Distributor**.
- 5 **Authorized Participants** may buy or sell excess shares to the market through market participants. **Market Makers** may engage **Authorized Participants** to facilitate creations or redemptions.
- 6 **Market Makers** provide ETF liquidity by posting double-sided quotes on the national **Stock Exchanges**.
- 7 **Brokers** who wish to buy or sell retail quantities of ETF shares will facilitate these transactions on the **Secondary Market** through one of the national **Exchanges**.
- 8 **Investors** who wish to invest in ETFs will engage with a **Broker**, who buys or sells shares on their behalf.
- 9 Large **Institutional investors** may buy or sell ETF shares on the **Secondary Market** through alternative trading venues such as **OTC (Over-the-Counter)** and **Dark Pools**.
- 10 When a creation or redemption order is processed, the **Medallion Distributor** approves the order and provides final order details to **Accounting/Custody**.
- 11 The **Medallion Distributor** provides the **Transfer Agent** with creation/redemption activity for record keeping, and the **Transfer Agent** maintains this data for the use of the **Medallion Distributor** in shareholder communications.
- 12 **Authorized Participants** initiate creation and redemption activity on the **Primary Market** through **Medallion Distributor** systems, and the Medallion Distributor provides confirmations to Authorized Participants.
- 13 ETF Issuers operate under various rules and regulations including the **SEC** for asset management activities, **FINRA** for sales activities, and the **CFTC** when certain derivatives are involved.
- 14 The **Investment Management** division of the **SEC** monitors the **Investment Advisor** to ensure compliance with multiple federal regulations.
- 15 The **NSCC (National Securities Clearing Corporation)** is regulated by the **SEC**.
- 16 The **Trading and Markets Division** of the **SEC** monitors and works alongside **Execution Venues** to ensure efficient, transparent markets, as well as overall capital market integrity.
- 17 **FINRA** regulates member **brokerage** firms and **exchanges**.
- 18 **FINRA** monitors **Brokers** to ensure federal regulations are being followed. It also seeks to protect **Investors** from unscrupulous sales tactics.
- 19 As a FINRA-member broker-dealer, the **Medallion Distributor** interacts with FINRA on behalf of the **ETF Issuer**.
- 20 **Compliance** monitors the **ETF issuer** and funds for compliance with regulations, policies, and procedures.
- 21 The **Trustees** monitor vendors and the general management of the trust to ensure shareholders' rights and interests are being protected.
- 22 The **Legal** team assists the **ETF Issuer** with contracts and provides general counsel. It also sets the agenda for regular and special meetings of **Trustees**.
- 23 The **Index Provider** transmits daily index constituents to the **ETF** for the purpose of tracking the portfolio.
- 24 **Data Vendors** communicate various data points such as securities pricing, corporate action information, and website informatics to the **ETF Issuer** and its service providers.
- 25 The **Sales Distribution** team of an ETF issuer is usually in-house, but can be outsourced to a 3rd party.
- 26 The **Sales Distribution** team works to sell the ETF to **Investors**.
- 27 **Marketing and PR** sets messaging strategy as well as methods of communicating the **ETF Issuer's** products to investors.
- 28 **Marketing and PR** communicates key information about the ETF to **Investors** by shaping branding, educational content, and messaging, as well as arranging media opportunities and appearances.
- 29 The investment **Advisor** monitors and manages the day-to-day operations of the **ETF** and its other service providers.
- 30 A **Sub-advisor**, if engaged, manages all or part of the investment portfolio of the **ETF**.
- 31 A **Sub-advisor** may be engaged on behalf of the primary investment **advisor** to manage some, or all, of the portfolio's assets.
- 32 The **Securities Lending Agent** acts as agent of the **Fund** to manage the lending of portfolio securities. This service generally does not start until the fund has some scale.
- 33 The **Custodian** and **Securities Lending Agent** work in tandem to facilitate the borrowing of securities with proper record-keeping.
- 34 The **Custodian** transmits creation/redemption baskets nightly to the **NSCC** (National Securities Clearing Corporation) who then disseminates it to all member firms including back to the custodian.
- 35 The **NSCC** (National Securities Clearing Corporation) transmits ETF constituents to the **IOPV** (Indicative Optimized Portfolio Value) calculation agent each morning to generate estimated intra-day share price.
- 36 The **NSCC** (National Securities Clearing Corporation) transmits official creation/redemption basket to **Exchanges** for public dissemination.
- 37 The **ETF Issuer** appoints the **Medallion Distributor** as a Service Provider of the Trust.
- 38 The **Medallion Distributor** is a function of the **ETF Issuer's Compliance**, as it is tasked with reviewing and approving all ETF marketing materials prior to use for compliance with **SEC** and **FINRA** advertising rules.



Part 2

The Semi-transparent ETF Ecosystem

Since actively managed ETFs seek to generate alpha—outperform a benchmark—through security selection and innovative weighting schemes, many money managers have been reluctant to adopt the traditional ETF structure because it demands a transparency that could expose proprietary security selection and weighting methodologies to the public. Moreover, since large ETFs' holdings are disclosed each trading day, and their rebalances occur on a regular basis, transparent ETFs open themselves up to “front running” whereby traders bid up the price of an ETF's underlying holdings with the foreknowledge that the ETF itself will need to purchase those shares for a rebalance.

For asset managers who wish to harness the advantages of the ETF structure—including its tax efficiency and intraday tradability—but want to avoid some of its pitfalls, semi-transparent ETFs may offer a solution. With a few minor exceptions, semi-transparent ETFs utilize all of the same structures and relationships as fully transparent ETFs. They are mostly distinguished from fully transparent ETFs by the methods utilized to signal the value of the ETF's underlying portfolio.

MODEL	METHOD	NOTES
Blue Tractor	Shielded Alpha	Holdings and weightings are disclosed, but disclosed weightings deviate 10% from actual weightings.
Eaton Vance	ClearHedge	Discloses a basket of liquid interests designed to have a high degree of correlation to the fund itself. The ETF's actual holdings and weightings are shielded from public view. A swap administration agent stands ready to issue new swaps every second over the course of the trading day, which can be used to swap the performance of the actual underlying securities.
Fidelity	Tracking Basket	Discloses a Tracking Basket designed to closely track the daily performance of the ETF's actual portfolio. The ETF's actual holdings and weightings are shielded from public view.
New York Stock Exchange	Proxy Portfolio	Discloses a proxy portfolio designed to recreate the daily performance of the actual portfolio using a factor model analysis of the ETF's actual portfolio. The ETF's actual holdings and weightings are shielded from public view.
Precidian	ActiveShares	Trusted agents, also known as authorized participant representatives (APRs) use confidential accounts to execute creations and redemptions for authorized participants.
T. Rowe Price	Proxy Portfolio	A proxy portfolio is disclosed to the public, with holdings that exhibit a high correlation to the fund's true underlying holdings.



Part 2A

Proxy Portfolios

While some approaches to semi-transparent ETFs utilize additional entities and relationships, the semi-transparent ETF models on this page use the existing ETF ecosystem's entities and relationships as-is. Instead, to partially shield their respective underlying holdings from public view, these models have made changes to the way that disclosures of a given ETF's holdings are communicated to the public.

Blue Tractor: Shielded Alpha

Blue Tractor's model seeks to protect the fund manager's alpha by hiding the exact weightings of a fund's holdings. The model discloses 100% of the ETF basket's holdings with a 90% asset value overlap. What this means in practice is that the disclosed individual holdings' weightings will vary slightly from the actual weightings. For example, Company X may be disclosed as a 1.8% weighting, when in reality it is a 2.2% weighting.

Fidelity: Tracking Basket

Fidelity's Tracking Basket model does not disclose the actual underlying holdings of the ETF. Instead, it discloses a "tracking basket" which is designed to closely track the daily performance of the ETF, without revealing its actual underlying holdings. The tracking basket consists of select recently disclosed portfolio holdings and ETFs that convey information about the types of financial instruments utilized by the fund that are not fully represented by Strategy Components. Each business day, the model also publishes a Tracking Basket Weight Overlap which helps investors understand how similar the tracking basket's holdings are, in percentage terms, to the actual portfolio.

New York Stock Exchange: Proxy Portfolio

The NYSE model also does not disclose the true underlying holdings of the ETF. Instead, it discloses a Proxy Portfolio which is intended to reflect the risk characteristics and economic exposures of the Actual Portfolio on any given trading day and is also intended to perform in a manner substantially identical to the Actual Portfolio. The Proxy Portfolio is generated by performing a factor analysis on the actual portfolio, which is shielded from public view. The factor analysis utilizes three sets of factors or analytical metrics: market-based factors, fundamental factors, and industry/sector factors.

T. Rowe Price: Proxy Portfolio

T. Rowe Price's model does not disclose the underlying holdings of the ETF. Instead, the fund discloses a Proxy Portfolio to the public. Designed to be highly correlated to the true underlying portfolio of the ETF itself, the Proxy Portfolio derives its holdings through fundamental and statistical relationships and is intended to have a substantial overlap between its holdings and the actual portfolio.



Part 2B

The Modified ETF Ecosystem

Unlike Proxy Portfolio ETFs, the following two models make alterations to the existing ETF ecosystem with new entities and relationships to shield their holdings from public view.

Eaton Vance: ClearHedge

Instead of disclosing the actual underlying holdings of the ETF, Eaton Vance's ClearHedge model discloses liquid interests designed to have a high degree of correlation to the fund itself. The ClearHedge model also adds another entity, a Swap Administration Agent, to the ETF ecosystem. The Swap Administration Agent interacts with both the ETF issuer and market makers, issuing swaps every second of the trading day which can be used to swap the performance of the actual underlying securities. The updated illustration and key on the following two pages show where this new entity fits into the existing ecosystem.

Precidian: ActiveShares

Similar to mutual funds, ActiveShares are required to reveal their holdings on a quarterly basis at a minimum, however managers may choose to reveal holdings more frequently.

Precidian's ActiveShares model adds a new entity to the ETF Ecosystem: the Authorized Participant Representative (APR). Since the ETF's underlying holdings are not disclosed throughout the day, the APR acts as a Trusted Agent, interfacing directly with the ETF issuer and Authorized Participants on the Primary Market. Additionally, ActiveShares publish Verified Intraday Indicative Values (VIV) every second. The updated illustration and key on the following two pages show where this new entity fits into the existing ecosystem.

KEY

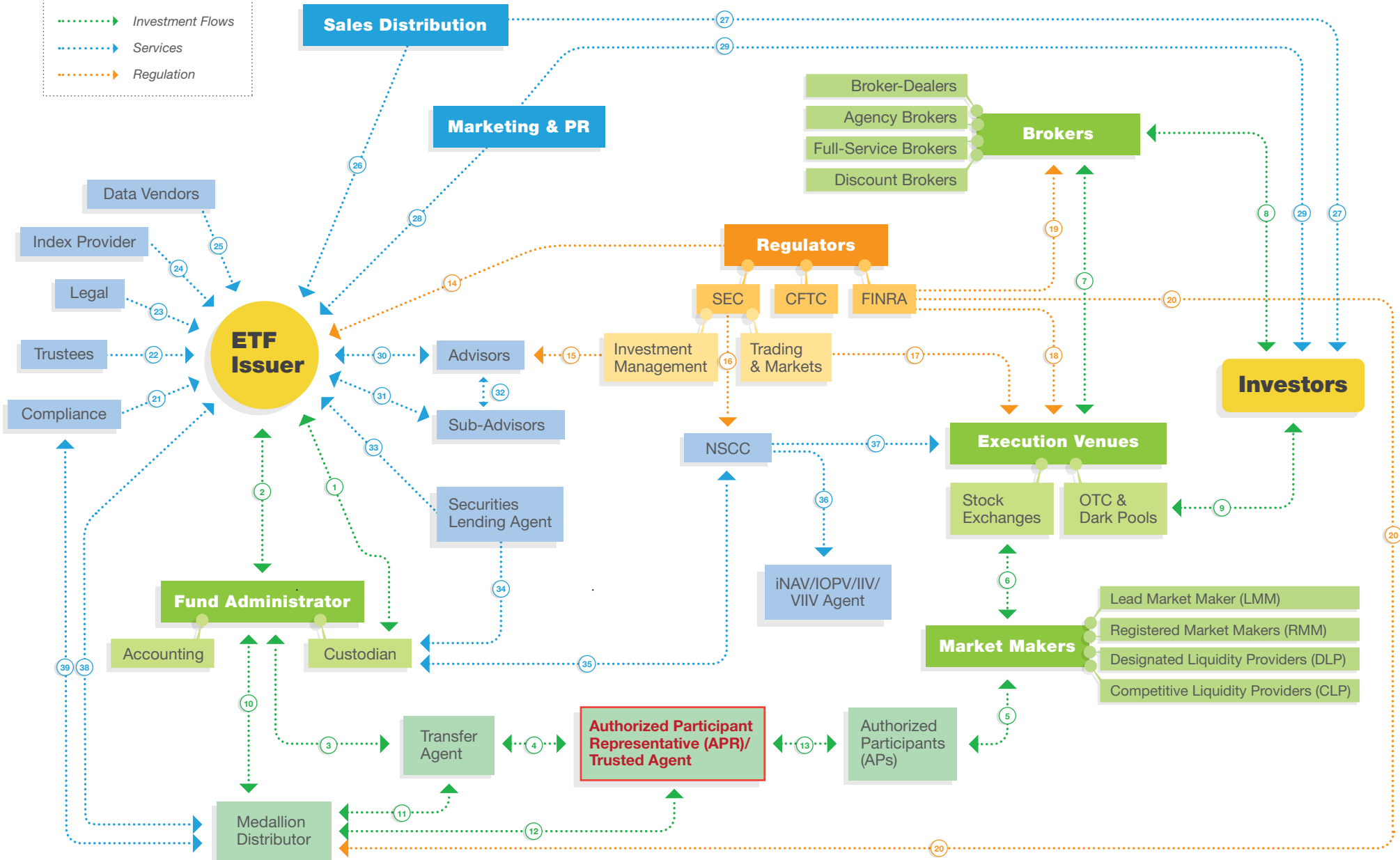
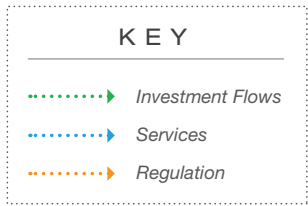
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THE SEMI-TRANSPARENT ETF ECOSYSTEM

ActiveShares by Precidian



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- 13 The **Authorized Participant Representative (APR)** discloses to the **Authorized Participants (APs)** the cash required to process a creation order. For redemptions, the **Fund Sponsor** delivers a basket of securities to the **APR** who then provides the **AP** with the net cash.
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CONCLUSION

As they explore their options, asset managers should keep in mind that these models are novel products that will require firms to meet new compliance obligations that stem from their exemptive orders. If the market loses confidence in the different hedging mechanisms that each model utilizes, the models will fail.

Firms interested in utilizing such models need to be sure they have the ability to produce the necessary data and get it to market. Firms will also be required to keep a close eye on how their products are trading, both to ensure that they are putting enough information into the market and that they are meeting reporting obligations under their exemptive applications which require reporting certain events up to a fund board on short notice – something you don't see with traditional transparent ETFs.

Innovative new models for semi-transparent ETFs have arisen as the ETF ecosystem continues to evolve and mature. This guide has sought to clarify what separates each of the new semi-transparent ETF models apart from one another, and to help identify potential opportunities in the space. Although the ETF industry is no longer in its infancy, the advent of semi-transparent ETFs shows that there is still plenty of room for innovation in the space.

GLOSSARY

Accounting Firm that calculates daily NAV.

Advisors Entity that manages the investments of the ETF as defined in the prospectus.

Agency Brokers Brokers only acting as agent on behalf of customers and not as principal trader for their own account.

Authorized Participants Entities that transact in the primary market by creating and redeeming new ETF shares, which can then be sold in the secondary market.

Authorized Participant Representative (APR)/Trusted Agent The Authorized Participant Representative (APR)'s core responsibility is to keep the contents of the ETF basket secret. The APR has an agreement with the ETF stating it cannot disclose or misuse material nonpublic information and is secured with additional safeguards and monitoring.

Broker-Dealers A firm that buys and sells securities for its own account as well as selling to customers.

Brokers General term describing individual or firm that buys and sells securities on behalf of investors.

CFTC Commodity Futures Trading Commission - US government agency that regulates the futures and options markets.

Compliance Internal and external groups that monitor, detect, and prevent misconduct of rules designed by regulators.

Custodian Firm that holds records of asset ownership as well as facilitating instructions for corporate actions.

Data Vendors Firms that provide various data to vendors including pricing data, market data, data to populate the fund website, and more.

Discount Brokers Brokers typically only offering bare-bones execution services without research and personalized advice.

FAs Financial Advisers (FAs) typically operate through a broker dealer, are regulated by FINRA, and fall under the suitability rules.

FINRA Financial Industry Regulatory Authority - A self-regulating organization that oversees organizations that facilitate the buying and selling of securities.

Full-Service Brokers Brokers providing research and advice to clients in addition to executing trades.

Fund Administrator Firm that provides legal, business, and financial support services to assist the ETF in operating as an ongoing entity.

iNAV/IOPV (Indicative Optimized Portfolio Value)/IIV (Intraday Indicative Value)/vIIV (Verified Intraday Indicative Value) Agent A real-time calculation that estimates per share value of an ETF throughout the trading day. For semi-transparent ETFs using Precidian's ActiveShares approach, Verified Intraday Indicative Value (vIIV) is published every second. For contrast, transparent ETFs' Intraday Indicative Values (IIVs) are published every 15 seconds. Prior to launch, the fund sponsor will need to establish NAV divergence thresholds/spreads and report regularly on these to the board.

Index Provider Firm that generates the investment portfolio strategy, which will be the basis for the ETF's investments.

Institutional General term describing investors who invest on behalf of other investors, which are often, from a sales perspective, segregated for their unique needs and constraints.

Investment Management The Investment Management division of the SEC works to protect investors through asset management industry regulation.

Legal Internal and external groups that advise and protect companies as related to business law.

LMM/DLP/CLP Different listing exchanges' names for the entities that agree to provide simultaneous bid and ask quotes to ensure liquidity and an orderly market. These entities have clearly defined quoting obligations and incentives that must be met on an ongoing basis.

Marketing & PR Group or firm that provides sales collateral, educational content, and advertising in support of asset-gathering and the sales force.

Medallion Distributor Serves as the underwriter for new shares. Also facilitates dealer agreements and 12b-1 fees, if applicable.

GLOSSARY

NSCC National Securities Clearing Corporation - the centralized security depository in the United States.

OTC & Dark Pools Execution venues which allow larger buy side firms to transact while preserving some anonymity.

Primary Market Also known as the new issues market, this is where buyers can transact directly with the issuers.

Registered Market Makers Entity that may provide bid and ask quotes for an ETF but does not have the same obligations or incentives as the Lead Market Maker.

Retail General term describing individual investors investing for their own account or through an adviser.

RIAs Registered Investment Advisers (RIAs) typically operate through a state or SEC registered Adviser under the Adviser's Act, are regulated by the state or SEC, and fall under the 40 Act fiduciary standard.

Sales Distribution A firm's sales team, whose job is to raise assets in an ETF by educating and selling to financial intermediaries and investors.

SEC Securities and Exchange Commission - US government agency that oversees the financial markets to protect shareholders and create capital market integrity.

Secondary Market This is where investors trade previously issued securities among themselves, without involving the issuers.

Securities Lending Agent Financial entity that is willing to pay to borrow the underlying securities in the fund.

Self-Directed Individuals making their own investment decisions.

Stock Exchanges Markets where individual equity securities, including ETFs, can be bought and sold.

Sub-advisors Firm hired by advisor to manage all, or a portion of, an ETF's investment portfolio based on its specific objectives.

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