

Required fields are shown with yellow backgrounds and asterisks.

Page 1 of * 74	SECURITIES AND EXCHANGE COMMISSION WASHINGTON, D.C. 20549 Form 19b-4		File No.* SR - 2014 - * 020	Amendment No. (req. for Amendments *)
Filing by NASDAQ Stock Market Pursuant to Rule 19b-4 under the Securities Exchange Act of 1934				
Initial * <input checked="" type="checkbox"/>	Amendment * <input type="checkbox"/>	Withdrawal <input type="checkbox"/>	Section 19(b)(2) * <input checked="" type="checkbox"/>	Section 19(b)(3)(A) * <input type="checkbox"/>
			Section 19(b)(3)(B) * <input type="checkbox"/>	
Pilot <input type="checkbox"/>	Extension of Time Period for Commission Action * <input type="checkbox"/>	Date Expires * <input type="text"/>	Rule <input type="checkbox"/> 19b-4(f)(1) <input type="checkbox"/> 19b-4(f)(4) <input type="checkbox"/> 19b-4(f)(2) <input type="checkbox"/> 19b-4(f)(5) <input type="checkbox"/> 19b-4(f)(3) <input type="checkbox"/> 19b-4(f)(6)	
Notice of proposed change pursuant to the Payment, Clearing, and Settlement Act of 2010			Security-Based Swap Submission pursuant to the Securities Exchange Act of 1934	
Section 806(e)(1) * <input type="checkbox"/>	Section 806(e)(2) * <input type="checkbox"/>	Section 3C(b)(2) * <input type="checkbox"/>		
Exhibit 2 Sent As Paper Document <input type="checkbox"/>	Exhibit 3 Sent As Paper Document <input type="checkbox"/>			
<b>Description</b>				
Provide a brief description of the action (limit 250 characters, required when Initial is checked *).				
<input type="text" value="A proposed rule change relating to listing and trading of Exchange-Traded Managed Fund shares."/>				
<b>Contact Information</b>				
Provide the name, telephone number, and e-mail address of the person on the staff of the self-regulatory organization prepared to respond to questions and comments on the action.				
First Name *	<input type="text" value="Jonathan"/>	Last Name *	<input type="text" value="Cayne"/>	
Title *	<input type="text" value="Associate General Counsel"/>			
E-mail *	<input type="text" value="jonathan.cayne@nasdaqomx.com"/>			
Telephone *	<input type="text" value="(301) 978-8493"/>	Fax	<input type="text" value="(301) 978-8472"/>	
<b>Signature</b>				
Pursuant to the requirements of the Securities Exchange Act of 1934,				
has duly caused this filing to be signed on its behalf by the undersigned thereunto duly authorized.				
(Title *)				
Date	<input type="text" value="02/14/2014"/>	<input type="text" value="Executive Vice President and General Counsel"/>		
By	<input type="text" value="Edward S. Knight"/>	<input type="text"/>		
(Name *)				
NOTE: Clicking the button at right will digitally sign and lock this form. A digital signature is as legally binding as a physical signature, and once signed, this form cannot be changed.				
<input type="button" value="Persona Not Validated - 1383935917270"/>				

SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

For complete Form 19b-4 instructions please refer to the EFFF website.

**Form 19b-4 Information \***

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The self-regulatory organization must provide all required information, presented in a clear and comprehensible manner, to enable the public to provide meaningful comment on the proposal and for the Commission to determine whether the proposal is consistent with the Act and applicable rules and regulations under the Act.

**Exhibit 1 - Notice of Proposed Rule Change \***

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The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO]-xx-xx). A material failure to comply with these guidelines will result in the proposed rule change being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)

**Exhibit 1A- Notice of Proposed Rule Change, Security-Based Swap Submission, or Advance Notice by Clearing Agencies \***

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The Notice section of this Form 19b-4 must comply with the guidelines for publication in the Federal Register as well as any requirements for electronic filing as published by the Commission (if applicable). The Office of the Federal Register (OFR) offers guidance on Federal Register publication requirements in the Federal Register Document Drafting Handbook, October 1998 Revision. For example, all references to the federal securities laws must include the corresponding cite to the United States Code in a footnote. All references to SEC rules must include the corresponding cite to the Code of Federal Regulations in a footnote. All references to Securities Exchange Act Releases must include the release number, release date, Federal Register cite, Federal Register date, and corresponding file number (e.g., SR-[SRO]-xx-xx). A material failure to comply with these guidelines will result in the proposed rule change, security-based swap submission, or advance notice being deemed not properly filed. See also Rule 0-3 under the Act (17 CFR 240.0-3)

**Exhibit 2 - Notices, Written Comments, Transcripts, Other Communications**

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Exhibit Sent As Paper Document

Copies of notices, written comments, transcripts, other communications. If such documents cannot be filed electronically in accordance with Instruction F, they shall be filed in accordance with Instruction G.

**Exhibit 3 - Form, Report, or Questionnaire**

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Exhibit Sent As Paper Document

Copies of any form, report, or questionnaire that the self-regulatory organization proposes to use to help implement or operate the proposed rule change, or that is referred to by the proposed rule change.

**Exhibit 4 - Marked Copies**

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The full text shall be marked, in any convenient manner, to indicate additions to and deletions from the immediately preceding filing. The purpose of Exhibit 4 is to permit the staff to identify immediately the changes made from the text of the rule with which it has been working.

**Exhibit 5 - Proposed Rule Text**

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The self-regulatory organization may choose to attach as Exhibit 5 proposed changes to rule text in place of providing it in Item I and which may otherwise be more easily readable if provided separately from Form 19b-4. Exhibit 5 shall be considered part of the proposed rule change.

**Partial Amendment**

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If the self-regulatory organization is amending only part of the text of a lengthy proposed rule change, it may, with the Commission's permission, file only those portions of the text of the proposed rule change in which changes are being made if the filing (i.e. partial amendment) is clearly understandable on its face. Such partial amendment shall be clearly identified and marked to show deletions and additions.

1. Text of Proposed Rule Change

(a) Pursuant to the provisions of Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> The NASDAQ Stock Market LLC (“Nasdaq” or the “Exchange”) is filing with the Securities and Exchange Commission (“Commission”) a proposed rule change to permit the listing and trading under proposed Nasdaq Rule 5745 of the shares of a proposed new type of open-end management investment company registered under the Investment Company Act of 1940, as amended (“1940 Act”), called an Exchange-Traded Managed Fund (“ETMF”). Proposed Nasdaq Rule 5745 would also permit trading pursuant to unlisted trading privileges (“UTP”) of ETMFs that are listed on other national securities exchanges. The shares of an ETMF are collectively referred to herein as “ETMF Shares” or “Shares.”

(b) and (c) Not applicable.

2. Procedures of the Self-Regulatory Organization

The Board of Directors of the Exchange approved the submission of this proposed rule change on December 4, 2013. No other action by the Exchange is necessary for the filing of the rule change.

Questions regarding this rule filing may be directed to Jonathan F. Cayne, Associate General Counsel, Nasdaq, at (301) 978-8493 (telephone) or (301) 978-8472 (fax).

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<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

3. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

a. Purpose

The Exchange proposes to adopt Nasdaq Rule 5745 for the purpose of permitting the listing and trading of ETMF Shares. Similar to Managed Fund Shares as defined in Nasdaq Rule 5735,<sup>3</sup> ETMF Shares would be issued in specified aggregate unit quantities in return for a deposit of a specified basket of securities and/or a cash amount with a value equal to the product of the ETMF's net asset value per Share ("NAV") and the number of Shares issued. When aggregated in the same specified unit quantities, ETMF Shares could be redeemed in exchange for a specified basket of securities and/or cash with a value per Share equal to the ETMF's NAV. Unlike Managed Fund Shares, ETMF Shares would trade on Nasdaq using a new trading protocol called "NAV-Based Trading." In NAV-Based Trading, all bids, offers and execution prices would be expressed as a premium/discount (which may be zero) to the ETMF's next-determined NAV (*e.g.*, NAV-\$0.01; NAV+\$0.01). An ETMF's NAV would be determined each business day, normally as of 4:00 p.m. Eastern Time. Trade executions using NAV-Based Trading would be binding at the time orders are matched on Nasdaq's facilities, with the transaction prices contingent upon the determination of the ETMF's NAV at the end of the business day.

Proposed Listing Rules for Exchange-Traded Managed Fund Shares

Proposed Nasdaq Rule 5745(b)(1) provides that Nasdaq will file separate proposals under Section 19(b) of the Act before the listing of ETMF Shares. Proposed

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<sup>3</sup> The Commission approved Nasdaq Rule 5735 in Securities Exchange Act Release No. 57962 (June 13, 2008), 73 FR 35175 (June 20, 2008) (SR-NASDAQ-2008-039).

Nasdaq Rule 5745(b)(2) provides that transactions in ETMF Shares will occur during Nasdaq's Regular Market Session through 4:00 p.m.<sup>4</sup> Proposed Nasdaq Rule 5745(b)(3) provides that ETMF Shares will trade on Nasdaq at market-determined premiums or discounts to the next-determined NAV, and that the minimum price variation for quoting and entry of orders in ETMF Shares will be \$0.01. Proposed Rule Nasdaq 5745(b)(4) provides that Nasdaq will implement written surveillance procedures for ETMF Shares. Proposed Nasdaq Rule 5745(b)(5) provides that, for ETMF Shares based on an international or global portfolio, the statutory prospectus or the application for exemption from provisions of the 1940 Act for such series of ETMF Shares must state that such series must comply with the federal securities laws in accepting securities for deposit and satisfying redemptions with securities, including that the securities accepted for deposit and the securities used to satisfy redemption requests are sold in transactions that would be exempt from registration under the Securities Act of 1933 ("Securities Act").

Proposed Definitions. Proposed Nasdaq Rule 5745(c)(1) defines the term "ETMF Share" as a security that: (1) represents an interest in a registered investment company organized as an open-end management investment company that invests in a portfolio of securities and other assets selected and managed by the ETMF's investment adviser consistent with the ETMF's investment objectives and policies; (2) is issued in specified aggregate unit quantities in return for a deposit of a specified portfolio of securities and/or a cash amount with a value per Share equal to the ETMF's NAV; (3) when aggregated in the same specified unit quantities, may be redeemed in exchange for a

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<sup>4</sup> Nasdaq Rule 4120(b)(4) defines the Regular Market Session as the trading session from 9:30 a.m. to 4:00 p.m. or 4:15 p.m. ETMF Shares will trade until 4:00 p.m.

specified portfolio of securities and/or cash with a value per Share equal to the ETMF's NAV; and (4) is traded on a national securities exchange using NAV-Based Trading.

In addition, proposed Nasdaq Rule 5745(c)(2) defines the term "Intraday Indicative Value" ("IIV") as the estimated indicative value of an ETMF Share based on current information regarding the value of the securities and other assets held by the ETMF. Proposed Nasdaq Rule 5745(c)(3) defines the term "Composition File" as the specified portfolio of securities and/or cash that an ETMF will accept as a deposit in issuing ETMF Shares and the specified portfolio of securities and/or cash that an ETMF will deliver in a redemption of ETMF Shares. The current Composition File will be disseminated through the National Securities Clearing Corporation ("NSCC") once each business day before the open of trading in ETMF Shares on Nasdaq on such day. To maintain the confidentiality of current portfolio trading, an ETMF's Composition File generally will not be a pro rata reflection of the ETMF's securities positions. Each security included in the Composition File will be a current holding of the ETMF, but the Composition File generally will not include all of the securities in the ETMF's portfolio or match the weightings of the included securities in the portfolio. The Composition File also may consist entirely of cash, in which case it will not include any of the securities in the ETMF's portfolio.

Proposed Nasdaq Rule 5745(c)(4) defines the term "Reporting Authority" as Nasdaq, an institution or a reporting service designated by Nasdaq as the official source for calculating and reporting information relating to such series of ETMF Shares, including, but not limited to, the IIV, the amount of any cash distribution to holders of ETMF Shares, NAV, the Composition File or other information relating to the issuance,

redemption or trading of ETMF Shares. A series of ETMF Shares may have more than one Reporting Authority, each having different functions.

Initial and Continued Listing. Proposed Nasdaq Rule 5745(d) sets forth the initial and continued listing criteria applicable to ETMF Shares.<sup>5</sup> Proposed Nasdaq Rule 5745(d)(1)(A) provides that, for each series of ETMF Shares, Nasdaq will establish a minimum number of ETMF Shares required to be outstanding at the time of commencement of trading. In addition, under proposed Nasdaq Rule 5745(d)(1)(B), Nasdaq must obtain a representation from the issuer of each series of ETMF Shares that the NAV for such series will be calculated on each business day that the New York Stock Exchange is open for trading and that the NAV will be made available to all market participants at the same time. Under proposed Nasdaq Rule 5745(d)(1)(C), the Reporting Authority that provides the Composition File must implement and maintain, or be subject

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<sup>5</sup> An investment adviser to an ETMF would be registered under the Investment Advisers Act of 1940 (the “Advisers Act”). As a result, the investment adviser and any subadviser and their related personnel would be subject to the provisions of Rule 204A-1 under the Advisers Act relating to codes of ethics. This Rule requires investment advisers to adopt a code of ethics that reflects the fiduciary nature of the relationship to clients as well as compliance with other applicable securities laws. Accordingly, procedures designed to prevent the communication and misuse of non-public information by an investment adviser must be consistent with Rule 204A-1 under the Advisers Act. In addition, Rule 206(4)-7 under the Advisers Act makes it unlawful for an investment adviser to provide investment advice to clients unless such investment adviser has (i) adopted and implemented written policies and procedures reasonably designed to prevent violation, by the investment adviser and its supervised persons, of the Advisers Act and the Commission rules adopted thereunder; (ii) implemented, at a minimum, an annual review regarding the adequacy of the policies and procedures established pursuant to subparagraph (i) above and the effectiveness of their implementation; and (iii) designated an individual (who is a supervised person) responsible for administering the policies and procedures adopted under subparagraph (i) above. The Exchange represents that, for initial and/or continued listing, an ETMF must be in compliance with Rule 10A-3 under the Act. 17 CFR 240.10A-3.

to, procedures designed to prevent the use and dissemination of material non-public information regarding the ETMF's portfolio positions and changes in positions.

Proposed Nasdaq Rule 5745(d)(2)(A) provides that each series of ETMF Shares could continue to be listed and traded if the IIV for the ETMF Shares is widely disseminated by one or more major market data vendors at intervals of not more than 15 minutes during the Regular Market Session when the ETMF Shares trade on Nasdaq. Proposed Nasdaq Rule 5745(d)(2)(B) provides that Nasdaq will consider the suspension of trading in, or removal from listing of, a series of ETMF Shares under any of the following circumstances: (1) if, following the initial twelve-month period after commencement of trading on the Exchange of a series of ETMF Shares, there are fewer than 50 beneficial holders of the series of ETMF Shares for 30 or more consecutive trading days; (2) if the ETMF's IIV or NAV is no longer calculated or if its IIV, NAV or Composition File is no longer available to all market participants at the same time; (3) if the ETMF has failed to submit any filings required by the Commission or if Nasdaq is aware that the ETMF is not in compliance with the conditions of any exemptive order or no-action relief granted by the Commission with respect to the series of ETMF Shares; or (4) if such other event shall occur or condition exists which, in the opinion of Nasdaq, makes further dealings on Nasdaq inadvisable.

Proposed Nasdaq Rule 5745(d)(2)(C) provides that, if the IIV of a series of ETMF Shares is not being disseminated as required, Nasdaq may halt trading during the day in which the interruption to the dissemination of the IIV occurs. If the interruption to the dissemination of the IIV persists past the trading day in which it first occurred, Nasdaq will halt trading no later than the beginning of the trading day following the interruption.



In addition, if the Exchange becomes aware that the NAV with respect to a series of ETMF Shares is not calculated on each business day that the New York Stock Exchange is open for trading and disseminated to all market participants at the same time, it will halt trading in such series until such time as the NAV is available to all market participants. If Nasdaq becomes aware that the Composition File with respect to a series of ETMF Shares is not disseminated to all market participants at the same time, it will halt trading in such series until such time as the Composition File is available to all market participants.

In addition, proposed Nasdaq Rule 5745(d)(2)(D) provides that, upon termination of an ETMF, the ETMF Shares issued in connection with such entity must be removed from listing on Nasdaq. Proposed Nasdaq Rule 5745(d)(2)(E) provides that voting rights must be as set forth in the applicable ETMF prospectus.

Additional Provisions. Proposed Nasdaq Rule 5745(e) provides that neither Nasdaq, the Reporting Authority nor any agent of Nasdaq shall have any liability for damages, claims, losses or expenses caused by any errors, omissions or delays in calculating or disseminating any of the following: the current portfolio value; the current value of the securities and other assets required to be deposited in connection with issuance of ETMF Shares; the amount of any dividend-equivalent payment or cash distribution to holders of ETMF Shares; NAV; the Composition File; or other information relating to the purchase, redemption or trading of ETMF Shares, resulting from any negligent act or omission by Nasdaq, the Reporting Authority or any agent of Nasdaq, or any act, condition or cause beyond the reasonable control of Nasdaq, its agent or the Reporting Authority, including, but not limited to, an act of God, fire, flood,

extraordinary weather conditions, war, insurrection, riot, strike, accident, action of government, communications or power failure, equipment or software malfunction, or any error, omission or delay in the reports of transactions in one or more underlying securities.

Proposed Nasdaq Rule 5745(f) applies only to series of ETMF Shares that are the subject of an order by the Commission exempting such series from certain prospectus delivery requirements under Section 24(d) of the 1940 Act and are not otherwise subject to prospectus delivery requirements under the Securities Act. Nasdaq will inform its members regarding application of Proposed Nasdaq Rule 5745(f) to a particular series of ETMF Shares by means of an information circular prior to commencement of trading in such series. Under the proposed rule, Nasdaq requires that members provide to all purchasers of a series of ETMF Shares a written description of the terms and characteristics of those securities, in a form prepared by the open-end management investment company issuing such securities, not later than the time a confirmation of the first transaction in such series is delivered to such purchaser. In addition, members shall include such a written description with any sales material relating to a series of ETMF Shares that is provided to customers or the public. Any other written materials provided by a member to customers or the public making specific reference to a series of ETMF Shares as an investment vehicle must include a statement in substantially the following form: “A circular describing the terms and characteristics of (the series of ETMF Shares) has been prepared by the (open-end management investment company name) and is available from your broker. It is recommended that you obtain and review such circular before purchasing (the series of ETMF Shares).” A member carrying an omnibus account

for a non-member broker-dealer is required to inform such non-member that execution of an order to purchase a series of ETMF Shares for such omnibus account will be deemed to constitute agreement by the non-member to make such a written description available to its customers on the same terms as are directly applicable to members under this rule. Upon request of a customer, a member shall also provide a prospectus for the particular series of ETMF Shares.

Proposed Nasdaq Rule 5745(g) provides that, if the investment adviser to an ETMF issuing Shares is a registered broker-dealer or affiliated with a broker-dealer, such investment adviser shall erect a “fire wall” between the investment adviser and the broker-dealer personnel or broker-dealer affiliate, as applicable, with respect to access to information concerning the composition and/or changes to such ETMF’s portfolio holdings. Personnel who make decisions on the ETMF’s portfolio composition must be subject to procedures designed to prevent the use and dissemination of material nonpublic information regarding the applicable ETMF portfolio.

#### Other Proposed Rule Changes

The Exchange also proposes to amend: (1) Nasdaq Rule 4120(a)(9) and (10) to add provisions applicable to ETMF Shares with respect to trading halts; (2) Nasdaq Rule 4120(b)(4)(A) and (E) to modify certain defined terms to include references to ETMF Shares; (3) Nasdaq Rule 5615(a)(5) and IM-5615-4 to add references to ETMFs for purposes of certain corporate governance requirements; and (4) Nasdaq Rule 5940(a) and

(b) to add references to ETMF Shares to those securities already covered under the rule relating to both entry fees and annual fees.<sup>6</sup>

Key Features of ETMF Shares

Open-End Registered Investment Company. An ETMF Share means a security that represents an interest in an open-end investment company registered under the 1940 Act that invests in a portfolio of securities and other assets selected and managed by its investment adviser consistent with its investment objectives and policies and which is traded on a national securities exchange using NAV-Based Trading.

1940 Act Exemptive Relief. The 1940 Act contemplates management investment companies that either (1) issue redeemable securities (*i.e.*, open-end investment companies) or (2) do not issue redeemable securities (*i.e.*, closed-end investment companies). ETMF Shares are redeemable, but only in large blocks of shares, not individually. Because exchange-traded funds (“ETFs”) issuing Managed Fund Shares (“Active ETFs”) do not fit neatly into either the open-end category or the closed-end category, Active ETFs have had to seek exemptive relief from the Commission to permit registration as an open-end investment company. ETMFs share some key structural features with Active ETFs, including creations and redemptions only in large blocks of shares, and require exemptive relief from the Commission from substantially the same provisions of the 1940 Act.

Creations and Redemptions. As with Managed Fund Shares, ETMF Shares will be issued and redeemed on a daily basis at NAV<sup>7</sup> in specified blocks of Shares called

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<sup>6</sup> The Exchange also proposes to make certain other minor technical changes to these rules unrelated to ETMFs. Specifically, the Exchange proposes to amend Rule 4120(a)(9), (b)(4)(A), and (b)(4)(E) to include appropriate references to various derivative securities defined in Rule 5711.

“Creation Units.” Creation Units may be purchased and redeemed by or through “Authorized Participants.”<sup>8</sup> Purchases and sales of Shares in amounts smaller than the number of Shares required for a Creation Unit may be effected only in the secondary market through NAV-based transactions, as described below, and not directly with the ETMF.

As with Active ETFs, the creation and redemption process for ETMFs may be effected “in kind,” in cash, or in a combination of securities and cash. Creation “in kind” means that the Authorized Participant—usually a brokerage house or large institutional investor—purchases the Creation Unit with a basket of securities equal in value to the aggregate NAV of the Shares in the Creation Unit. When an Authorized Participant redeems a Creation Unit in kind, it receives a basket of securities equal in value to the aggregate NAV of the Shares in the Creation Unit.

Composition File. As defined in proposed Nasdaq Rule 5475(c)(3), the Composition File is the specified portfolio of securities and/or cash that an ETMF will

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<sup>7</sup> As with other registered open-end investment companies, the NAV of ETMF Shares generally would be calculated daily Monday through Friday as of the close of regular trading on the New York Stock Exchange, normally 4:00 p.m. Eastern Time. NAV would be calculated by dividing the ETMF’s net asset value by the number of ETMF Shares outstanding. Information regarding the valuation of investments in calculating the ETMF’s NAV would be contained in the registration statement for the ETMF Shares.

<sup>8</sup> “Authorized Participants” would be either: (1) “participating parties,” *i.e.*, brokers or other participants in the Continuous Net Settlement System of the NSCC, a clearing agency registered with Commission and affiliated with the Depository Trust Company (“DTC”), or (2) DTC participants, which in either case have executed participant agreements with the ETMF’s distributor and transfer agent regarding the creation and redemption of Creation Units. Investors would not have to be Authorized Participants in order to transact in Creation Units, but must place an order through and make appropriate arrangements with an Authorized Participant for such transactions.

accept as a deposit in issuing a Creation Unit of ETMF Shares, and the specified portfolio of securities and/or cash that an ETMF will deliver in a redemption of a Creation Unit of ETMF Shares. The Composition File will be disseminated through the NSCC once each business day before the open of trading in ETMF Shares on such day. Because ETMFs seek to preserve the confidentiality of their current portfolio trading program, the Composition File generally will not be a pro rata reflection of the ETMF's securities positions. Each security included in the Composition File will be a current holding of the ETMF, but the Composition File generally will not include all of the securities in the ETMF's portfolio or match the weightings of the included securities in the portfolio. Securities that the investment adviser to the ETMF is in the process of acquiring for the ETMF generally would not be represented in the Composition File until their purchase has been completed. Similarly, securities that are held in the ETMF's portfolio but in the process of being sold may not be removed from the Composition File until the sale program is substantially completed. ETMFs creating and redeeming Shares in kind would use cash amounts to supplement the in-kind transactions to the extent necessary to ensure that Creation Units are purchased and redeemed at NAV. The Composition File also may consist entirely of cash, in which case it will not include any of the securities in the ETMF's portfolio.<sup>9</sup>

NAV-Based Trading. Because ETMF Shares will be listed and traded on the Exchange, ETMF Shares will be available for purchase and sale on an intraday basis, like

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<sup>9</sup> In determining whether an ETMF will issue or redeem Creation Units entirely on a cash basis, the key consideration will be the benefit that would accrue to the ETMF and its investors. For instance, in bond transactions, the investment adviser to the ETMF may be able to obtain better execution than Authorized Participants because of the investment adviser's size, experience and potentially stronger relationships in the fixed-income markets.

shares of conventional ETFs and other listed securities. Different from conventional ETF share trading, however, ETMF Shares would be purchased and sold in the secondary market at prices based on the next-determined NAV. All bids, offers and execution prices would be expressed as a premium/discount (which may be zero) to the ETMF's next-determined NAV (e.g., NAV-\$0.01, NAV+\$0.01). An ETMF's NAV would be determined each business day, normally as of 4:00 p.m. Eastern Time. Trade executions would be binding at the time orders are matched on Nasdaq's facilities, with the transaction prices contingent upon the determination of NAV.

- *Trading Premiums and Discounts.* ETMF Share prices would be quoted throughout the day relative to NAV. The premium or discount to NAV at which ETMF Share prices are quoted and transactions are executed would vary depending on market factors, including the balance of supply and demand for ETMF Shares among investors, transaction fees and other costs in connection with creating and redeeming Creation Units of ETMF Shares, competition among market makers and other arbitrageurs, the ETMF Share inventory positions and inventory strategies of market makers and other arbitrageurs, and the volume of ETMF Share trading. Reflecting these and other market factors, prices for ETMF Shares in the secondary market may be above, at or below NAV.

- *Transmitting and Processing Orders.* Member firms would utilize existing order types and interfaces to transmit ETMF Share bids and offers to Nasdaq, which would process ETMF Share trades like trades in shares of conventional ETFs and other listed securities. In the systems used to transmit and process transactions in ETMF Shares, Nasdaq expects an ETMF's next-determined NAV to be represented by a proxy

price (*e.g.*, 100.00) and a premium/discount of a stated amount to the next-determined NAV to be represented by the same increment/decrement from the proxy price used to denote NAV (*e.g.*, NAV-\$0.01 would be represented as 99.99; NAV+\$0.01 as 100.01).<sup>10</sup>

To avoid potential investor confusion, Nasdaq would work with member firms and providers of market data services to seek to ensure that representations of intraday bids, offers and execution prices for ETMFs that are made available to the investing public follow the “NAV-\$0.01/NAV+\$0.01” (or similar) display format, rather than displaying proxy prices. Nasdaq expects all ETMFs listed on the Exchange to have a unique identifier associated with their ticker symbols, which would indicate that their Shares are traded using NAV-Based Trading. Nasdaq makes available to member firms and market data services certain proprietary data feeds (“Nasdaq Data Feeds”) that are designed to supplement the market information disseminated through the consolidated tape (“Consolidated Tape”). The Exchange would use a Nasdaq Data Feed to disseminate intraday price and quote data for ETMFs in real time in the “NAV-\$0.01/NAV+\$0.01” (or similar) display format. Member firms could use the Nasdaq

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<sup>10</sup> Order transmission and processing systems currently in common use by exchanges and member firms are generally not designed to accommodate pricing arrangements, such as NAV-Based Trading, in which bids, offers and execution prices are determined by reference to a price or value that is unknown at the time of trade execution. Compared to the alternative of building and maintaining (and requiring member firms to build and maintain) a dedicated NAV-Based Trading order transmission and processing system, the Exchange believes that the proposed approach (using, for processing purposes, a proxy price to represent next-determined NAV) offers major advantages in terms of cost, efficiency and time to implement. To convert proxy prices used to represent intraday bids, offers and execution prices into prices expressed in relation to the next-determined NAV, member firms would subtract from the reported proxy price (*e.g.*, 99.99) the proxy for NAV (*e.g.*, 100.00) and inserting “NAV” in front of the calculated number expressed in dollars (*e.g.*,  $99.99 - 100.00 = -0.01$ , expressed as “NAV-\$0.01”).



Data Feed to source intraday ETMF prices for presentation to the investing public in the “NAV-\$0.01/NAV+\$0.01” (or similar) display format. Alternatively, member firms could source intraday ETMF prices in proxy price format from the Consolidated Tape and use a simple algorithm to convert prices into the “NAV-\$0.01/NAV+\$0.01” (or similar) display format.

- *Intraday Reporting of Quotes and Trades.* All ETMF bids, offers and trade executions would be reported intraday in real time by the Exchange to the Consolidated Tape<sup>11</sup> and separately disseminated to member firms and market data services through a Nasdaq Data Feed. The Exchange would also provide the member firms participating in each ETMF Share trade with a contemporaneous notice of trade execution, indicating the number of ETMF Shares bought or sold and the executed premium/discount to NAV.<sup>12</sup>

- *Final Trade Pricing, Reporting and Settlement.* All executed ETMF Share trades would be recorded and stored intraday by Nasdaq to await the calculation of the ETMF’s end-of-day NAV and the determination of final trade pricing. After the Reporting Authority calculates an ETMF’s NAV and provides this information to the Exchange, Nasdaq would price each ETMF Share trade entered into during the day at the ETMF’s NAV plus/minus the trade’s executed premium/discount. Using the final trade price, each executed ETMF Share trade would then be disseminated to member firms and

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<sup>11</sup> Due to systems limitations, the Consolidated Tape would report intraday execution prices and quotes for ETMFs using a proxy price format. As noted, Nasdaq would separately report real-time execution prices and quotes to member firms and providers of market data services in the “NAV-\$0.01/NAV+\$0.01” (or similar) display format, and otherwise seek to ensure that representations of intraday bids, offers and execution prices for ETMFs that are made available to the investing public follow the same display format.

<sup>12</sup> All orders to buy or sell an ETMF Share that are not executed on the day the order is submitted will be automatically cancelled as of the close of trading on such day.

market data services through the Nasdaq Data Feed used to report ETMF Share trades, and confirmed to the member firms participating in the trade to supplement the previously provided information to include final pricing. After the pricing is finalized, Nasdaq would deliver the ETMF Share trading data to NSCC for clearance and settlement, following the same processes used for the clearance and settlement of trades in conventional ETFs and other exchange-traded securities.

Portfolio Disclosure and ETMF Share Trading Efficiency. As required for traditional open-end investment companies, ETMFs would disclose their full portfolio positions at least quarterly, with a delay (not to exceed 60 days) to limit opportunities for other market participants to engage in predatory trading practices that might harm fund shareholders.<sup>13</sup>

Rule 5735 requires Active ETFs to disclose publicly their full portfolio positions at least once daily. The purpose of this requirement is to provide Active ETF market makers with the portfolio information needed to hedge the intraday market risk they assume as they take inventory positions in connection with their market making activities. In conventional ETF trading, a condition to maintaining a tight relationship between market trading prices and contemporaneous underlying portfolio values is that market makers have sufficient information regarding portfolio positions to enable them to

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<sup>13</sup> See 17 CFR 249.332; 17 CFR 274.130. In adopting the requirement for quarterly portfolio disclosure with not more than a 60 day delay, the Commission noted that it took seriously concerns that more frequent portfolio disclosure and/or a shorter delay for release of this information might expand the opportunities for other market participants to engage in predatory trading practices that harm fund shareholders. Shareholder Reports and Quarterly Portfolio Disclosure of Registered Management Investment Companies, Securities Exchange Act Release No. 49333 (Feb. 27, 2004). As with traditional mutual funds, an ETMF could elect to provide more frequent disclosure of portfolio positions, if appropriate.

earn reliable arbitrage profits by entering into long (or short) positions in ETF shares and offsetting short (or long) positions in the underlying holdings (or a suitable proxy).

In ETMF trading, by contrast, a market maker assumes no intraday market risk in connection with its inventory positions because all ETMF Share transaction prices are based on the next-determined NAV. Whether an ETMF's underlying value goes up or down over the course of a trading day will not affect how much profit a market maker earns by selling (or buying) ETMF Shares in the market at a net premium (discount) to NAV, and then purchasing (redeeming) an offsetting number of ETMF Shares at the end of the day in transactions with the ETMF. No intraday market risk means no requirement for intraday hedging, and therefore no associated requirement for portfolio disclosure to maintain a tight relationship between ETMF Share trading prices and NAV.

The arbitrage that connects ETMF trading prices to NAV is effected at the end of each trading day when a market maker or other arbitrageur purchases (or redeems) Creation Units of ETMF Shares through an Authorized Participant to offset the net amount of ETMF Shares it has sold (bought) over the course of the trading day, and buys (sells) the quantity of Composition File instruments corresponding to the number of Creation Units purchased (redeemed). An ETMF market maker that purchases (or redeems) a Creation Unit at the end of a trading day to offset its net intraday sales (purchases) of a Creation Unit quantity of ETMF Shares will earn arbitrage profits to the extent that it either sells (buys) Shares at an aggregate premium (discount) to NAV or buys (sells) a Creation Unit-equivalent quantity of Composition File instruments at an aggregate discount (premium) to their end-of-day values, and the net amount of ETMF premium (discount) plus Composition File instruments discount (premium) exceeds the

transaction fee that applies to a purchase (redemption) of a Creation Unit of ETMF Shares.<sup>14</sup>

Different from ETFs trading in conventional intraday markets, ETMFs offer market makers an arbitrage profit opportunity that does not depend on either corresponding intraday adjustments in fund share and underlying portfolio positions or the use of a hedge portfolio to manage intraday market risk. A “perfect arbitrage” in an ETMF requires only that market makers holding short (or long) positions in ETMF Shares accumulated intraday transact with the ETMF to purchase (redeem) a corresponding number of Creation Units of ETMF Shares, buy (sell) the equivalent quantities of Composition File instruments at market-closing or better prices, and offload any remaining sub-Creation Unit ETMF Share inventory through secondary market transactions by the market close.<sup>15</sup>

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<sup>14</sup> The arbitrage mechanism is simplified for cash creations and redemptions. An ETMF market maker that purchases (or redeems) a Creation Unit in cash to offset its net intraday sales (purchases) of a Creation Unit quantity of ETMF Shares will earn arbitrage profits to the extent that it sells (buys) ETMF Shares in the secondary market at an aggregate premium (discount) to NAV that exceeds the transaction fee that applies to a cash creation (redemption) of a Creation Unit of ETMF Shares.

<sup>15</sup> Market makers are expected generally to seek to minimize their exposure to price risk in ETMF Shares by holding little or no overnight inventory. Establishing Creation Unit sizes for ETMFs that are somewhat smaller (*i.e.*, in a range of 5,000 to 50,000 Shares) than is customary for ETFs should support efficient arbitrage between an ETMF’s trading prices and NAV by facilitating tighter market maker inventory management. To the extent that market makers hold small positions in ETMF Shares overnight, they are expected to aggregate such holdings with other risk positions and transact at or near the market close to buy or sell offsetting positions in appropriate, broad-based hedging instruments. Such hedging of overnight inventory risk on a macro basis does not require disclosure of non-Composition File portfolio positions.

Because the arbitrage mechanism that underlies ETMF trading is simpler, more reliable and exposes market makers to less risk than ETF arbitrage, market makers should require less profit inducement to establish and maintain markets in ETMF Shares than in similarly constituted ETFs, thereby enabling ETMFs to routinely trade at smaller premiums/discounts and narrower bid-ask spreads. Further, because the arbitrage mechanism that underlies efficient trading of ETMFs does not involve portfolio positions that are not included in the Composition File, the need for full portfolio transparency to achieve tight markets in ETMF Shares is eliminated.

Recognizing the potential harm to shareholders of disclosing portfolio trading information on a current basis (and the absence of a need for such information to maintain tight trading markets using NAV-Based Trading), proposed Nasdaq Rule 5745 would not require daily portfolio disclosure or specify a minimum level of correspondence between an ETMF's portfolio positions and its Composition File.

Intraday Indicative Value. For each series of ETMF Shares, an estimated value of an individual ETMF Share, defined in proposed Nasdaq Rule 5745(c)(2) as the "Intraday Indicative Value," would be widely disseminated by one or more major market data vendors at intervals of not more than 15 minutes throughout the Regular Market Session when ETMF Shares trade on the Exchange. The IIV would be based on current information regarding the value of the securities and other assets held by an ETMF.<sup>16</sup> Unlike Nasdaq Rule 5735, which requires dissemination of IIVs every 15 seconds for Managed Fund Shares, proposed Nasdaq Rule 5745 would not require the dissemination

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<sup>16</sup> IIVs disseminated throughout each trading day would be based on the same portfolio as used to calculate that day's NAV. Like Managed Fund Shares, ETMFs will reflect purchases and sales of portfolio positions in their NAV the next business day after trades are executed.

of an IIV on such a frequent basis. Dissemination of IIVs plays a different, and lesser, role in NAV-Based Trading of ETMF Shares than in conventional ETF trading. For Managed Fund Shares (and ETFs generally), the primary purpose of IIVs is to provide retail investors with a measure of the contemporaneous underlying value of a fund's positions, allowing them to assess the reasonableness of trading prices in relation to underlying value. For ETMF Shares, NAV-Based Trading provides investors with a direct measure of the relationship between trading prices and NAV (*e.g.*, NAV-\$0.01, NAV+\$0.02) and, using limit orders, a means for controlling the premium or discount to NAV at which they trade shares. The purpose of IIVs in NAV-Based Trading is to enable investors to estimate the next-determined NAV so they can determine the number of ETMF Shares to buy or sell if they want to transact in an approximate dollar amount (*e.g.*, if an investor wants to acquire approximately \$5,000 of an ETMF, how many Shares should the investor buy?).<sup>17</sup> For this purpose, dissemination of IIVs at intervals of

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<sup>17</sup> Because, in NAV-Based Trading, prices of executed trades are not determined until the reference NAV is calculated, buyers and sellers of ETMF Shares during the trading day will not know the final value of their purchases and sales until the end of the trading day. An ETMF's registration statement, website and any advertising or marketing materials will include prominent disclosure of this fact. Although IIVs may provide useful estimates of the value of intraday trades, they cannot be used to calculate with precision the dollar value of the ETMF Shares to be bought or sold. An IIV of an ETMF will generally differ from NAV to the extent that the value of the ETMF's portfolio holdings change intraday between the time the IIV is calculated and the end of the trading day. The fact that an investor placing an order to purchase or sell ETMF Shares would not know the trade price at the time the order is entered is similar to certain existing order types in conventional share trading. For standard market orders, trading prices are not known until the order executes. For market-on-close orders, trading prices are not established until the end of the trading day. In addition, for purchases and sales of share quantities of mutual funds, an investor does not know the transaction value until NAV is calculated at the end of the day. Member firms may have different systems for communicating these trade characteristics to their customers and for ensuring that customers have sufficient resources to engage in these trades.

not more than 15 minutes should generally be sufficient. More frequent dissemination of IIVs may increase fund costs without apparent benefit and could focus unwarranted investor attention on these disclosures. Moreover, for certain strategies, more frequent IIV disclosure could provide unintended information about current portfolio trading activity to market participants who possess the requisite analytical capabilities, computation power and motivation to reverse engineer the ETMF's portfolio positions. As proposed, an ETMF would be permitted to disseminate IIVs at intervals of less than 15 minutes, but would not be required to do so to maintain trading on the Exchange.

Availability of Information. Prior to the commencement of market trading in ETMF Shares, each ETMF will be required to establish and maintain a public website through which its current prospectus may be downloaded. The website will include additional ETMF information updated on a daily basis, including most recent NAV. The Composition File will be disseminated through the NSCC before the open of trading in ETMF Shares on Nasdaq on each business day. Consistent with the disclosure requirements that apply to traditional open-end investment companies, a complete list of current ETMF portfolio positions will be made available at least once each calendar quarter, with a reporting lag of not more than 60 days. ETMFs may provide more frequent disclosures of portfolio positions at their discretion.

Reports of ETMF Share transactions will be disseminated to the market and delivered to the member firms participating in the trade contemporaneous with execution.

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Member firms may require that a cash buffer be maintained in a customer's account relative to the current value of the security to be purchased. Alternatively, customers may have margin accounts or arrangements with their broker-dealer to provide for payment subsequent to trade execution, but prior to trade settlement.

Once an ETMF's daily NAV has been calculated, Nasdaq would price each ETMF Share trade entered into during the day at the ETMF's NAV plus/minus the trade's executed premium/discount. Using the final trade price, each executed ETMF Share trade would then be disseminated to member firms and market data services through the Nasdaq Data Feed used to report ETMF Share trades, and confirmed to the member firms participating in the trade to supplement the previously provided information to include final pricing.

Information regarding NAV-based trading prices and volumes of ETMF Shares will be continually available on a real-time basis throughout each trading day on brokers' computer screens and other electronic services. The previous trading day's closing price and volume information for the ETMF Shares will be published daily.

Exchange Listing. Nasdaq intends to enter into a license agreement to allow for the listing and trading of ETMF Shares on the Exchange.<sup>18</sup> ETMF Shares listed on the Exchange may trade pursuant to UTP on other national securities exchanges that have obtained appropriate licenses, adopted applicable exchange rules and developed systems to support NAV-Based Trading. Fees collected by the Exchange in connection with the listing and trading of ETMF Shares will comply with the statutory requirements set forth in the Act.

#### Trading Halts

The Exchange may consider all relevant factors in exercising its discretion to halt or suspend trading in ETMF Shares. Nasdaq will halt trading in ETMF Shares under the

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<sup>18</sup> Aspects of ETMFs and NAV-Based Trading are protected intellectual property subject to issued and pending U.S. patents held by Navigate Fund Solutions LLC ("Navigate"), a wholly owned subsidiary of Eaton Vance Corp. Nasdaq would enter into a license agreement with Navigate to allow for NAV-Based Trading on the Exchange of ETMFs that have themselves entered into license agreements with Navigate.



conditions specified in Nasdaq Rules 4120, as proposed to be amended, and in proposed Nasdaq Rule 5745(d)(2)(C), as discussed above. Additionally, Nasdaq may cease trading ETMF Shares if other unusual conditions or circumstances exist which, in the opinion of Nasdaq, make further dealings on Nasdaq detrimental to the maintenance of a fair and orderly market. To manage the risk of a non-regulatory ETMF Share trading halt, Nasdaq has in place back-up processes and procedures to ensure orderly trading. Because, in NAV-Based Trading, all trade execution prices are linked to end-of-day NAV, buyers and sellers of ETMF Shares should be less exposed to risk of loss due to intraday trading halts than buyers and sellers of conventional ETFs and other exchange-traded securities.

#### Trading Rules

Nasdaq deems ETMF Shares to be equity securities, thus rendering trading in ETMF Shares to be subject to Nasdaq's existing rules governing the trading of equity securities. Nasdaq will allow trading in ETMF Shares from 9:30 a.m. until 4:00 p.m. Eastern Time.<sup>19</sup> As provided in proposed Nasdaq Rule 5745(b)(3), the minimum price variation for quoting and entry of orders in ETMF Shares traded on the Exchange will be \$0.01.

#### Surveillance

The Exchange represents that trading in ETMF Shares will be subject to the existing trading surveillances, administered by both Nasdaq and the Financial Industry Regulatory Authority, Inc. ("FINRA") on behalf of the Exchange, which are designed to

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<sup>19</sup> See, supra note 4.

detect violations of Exchange rules and applicable federal securities laws.<sup>20</sup> The Exchange represents that these procedures are adequate to properly monitor trading of ETMF Shares on the Exchange and to deter and detect violations of Exchange rules and applicable federal securities laws.

The surveillances referred to above generally focus on detecting securities trading outside their normal patterns, which could be indicative of manipulative or other violative activity. When such situations are detected, surveillance analysis follows and investigations are opened, where appropriate, to review the behavior of all relevant parties for all relevant trading violations.

FINRA, on behalf of the Exchange, will communicate as needed with other markets and other entities that are members of the Intermarket Surveillance Group (“ISG”)<sup>21</sup> regarding trading in ETMF Shares, and in exchange-traded securities and instruments held by ETMFs, and FINRA may obtain trading information regarding such trading from other markets and other entities. In addition, the Exchange may obtain information regarding trading in ETMF Shares, and in exchange-traded securities and instruments held by ETMFs, from markets and other entities that are members of ISG, which includes securities and futures exchanges, or with which the Exchange has in place a comprehensive surveillance sharing agreement.

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<sup>20</sup> FINRA provides surveillance of trading on the Exchange pursuant to a regulatory services agreement. The Exchange is responsible for FINRA’s performance under this regulatory services agreement.

<sup>21</sup> For a list of the current members of ISG, *see* [www.isgportal.org](http://www.isgportal.org). The Exchange notes that not all components of an ETMF’s portfolio may trade on markets that are members of ISG or with which the Exchange has in place a comprehensive surveillance sharing agreement.

In addition, the Exchange also has a general policy prohibiting the distribution of material non-public information by its employees.

#### Information Circular

Prior to the commencement of trading in an ETMF, the Exchange will inform its members in an Information Circular of the special characteristics and risks associated with trading the ETMF Shares. Specifically, the Information Circular will discuss the following: (1) the procedures for purchases and redemptions of ETMF Shares in Creation Units (and noting that ETMF Shares are not individually redeemable); (2) Nasdaq Rule 2111A, which imposes suitability obligations on Nasdaq members with respect to recommending transactions in ETMF Shares to customers; (3) how information regarding the IIV is disseminated; (4) the requirement that members deliver a prospectus to investors purchasing ETMF Shares prior to or concurrently with the confirmation of a transaction; and (5) information regarding NAV-Based Trading protocols.

In addition, the Information Circular will advise members, prior to the commencement of trading, of the prospectus delivery requirements applicable to the ETMF. Members purchasing ETMF Shares from the ETMF for resale to investors will deliver a summary prospectus to such investors. The Information Circular will also discuss any exemptive, no-action and interpretive relief granted by the Commission from any rules under the Act.

The Information Circular also will reference that the ETMF is subject to various fees and expenses described in its registration statement. The Information Circular will also disclose the trading hours of the ETMF Shares and the applicable NAV calculation

time for the ETMF Shares. The Information Circular will disclose that information about the ETMF Shares will be publicly available on the ETMF's website.

Information regarding ETMF trading protocols will be disseminated to Nasdaq members in accordance with current processes for newly listed products. Nasdaq intends to provide its members with a detailed explanation of NAV-Based Trading through a Trading Alert issued prior to the commencement of trading in ETMF Shares on the Exchange.

b. Statutory Basis

Nasdaq believes that the proposal is consistent with Section 6(b) of the Act<sup>22</sup> in general, and Section 6(b)(5) of the Act<sup>23</sup> in particular, in that it is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in facilitating transactions in securities, and to remove impediments to and perfect the mechanism of a free and open market and a national market system. Nasdaq also believes that imposition of an initial entry fee and an annual fee in connection with the listing of ETMF Shares under proposed Nasdaq Rule 5940 is consistent with Section 6(b)(4) of the Act<sup>24</sup> in that it provides for the equitable allocation of reasonable dues, fees and other charges among members and issuers and other persons using any facility or system that the Exchange operates or controls.

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<sup>22</sup> 15 U.S.C. 78f(b).

<sup>23</sup> 15 U.S.C. 78f(b)(5).

<sup>24</sup> 15 U.S.C. 78f(b)(4).

The Exchange believes that the proposed rule change is designed to prevent fraudulent and manipulative acts and practices in that ETMF Shares would be listed and traded on the Exchange pursuant to the initial and continued listing criteria in proposed Nasdaq Rule 5745. The Exchange believes that its surveillance procedures are adequate to properly monitor the trading of ETMF Shares on Nasdaq and to deter and detect violations of Exchange rules and the applicable federal securities laws. If the investment adviser to an ETMF is a registered broker-dealer or affiliated with a broker-dealer, such investment adviser shall erect a “fire wall” between the investment adviser and the broker-dealer personnel or broker-dealer affiliate, as applicable, with respect to access to information concerning the composition and/or changes to the ETMF’s portfolio holdings. The Exchange may obtain information via ISG from other exchanges that are members of ISG or with which the Exchange has entered into a comprehensive surveillance sharing agreement, to the extent necessary.

The proposed rule change is designed to promote just and equitable principles of trade and to protect investors and the public interest. The Exchange will obtain a representation from each issuer of ETMF Shares that the NAV per ETMF Share will be calculated on each business day that the New York Stock Exchange is open for trading and that the NAV will be made available to all market participants at the same time. In addition, a large amount of information would be publicly available regarding ETMFs and ETMF Shares, thereby promoting market transparency. An IIV will be disseminated by one or more major market data vendors at intervals of not more than 15 minutes during trading on the Exchange. Prior to the commencement of market trading in ETMF Shares, each ETMF will be required to establish and maintain a public website through

which its current prospectus may be downloaded. The website will include additional ETMF information updated on a daily basis, including the most recent NAV. The Composition File will be disseminated through the NSCC before the open of trading in ETMF Shares on each business day. A complete list of current ETMF portfolio positions will be made available at least once each calendar quarter, with a reporting lag of not more than 60 days. ETMFs may provide more frequent disclosures of portfolio positions at their discretion.

Transactions in ETMF Shares will be reported to the Consolidated Tape, disseminated to member firms and market data services through the Nasdaq Data Feed used to report ETMF Share trades, and reported to the member firms participating in the trade contemporaneous with execution. Once an ETMF's daily NAV has been calculated and the final price of its intraday Share trades has been determined, Nasdaq will disseminate final pricing information through the Nasdaq Data Feed used to report ETMF Share trades and deliver a confirmation with final pricing to the transacting parties. Information regarding NAV-based trading prices and volumes of ETMF Shares traded will be continually available on a real-time basis throughout each trading day on brokers' computer screens and other electronic services. The previous trading day's closing price and volume information for the ETMF Shares will be published daily. Because ETMF Shares will trade at prices based on the next-determined NAV, investors will be able to buy and sell individual Shares at a known premium or discount to NAV that they can limit by transacting using limit orders. NAV-Based Trading provides a level of trading cost transparency and control that is normally not achievable in conventional ETF trading. Trading in ETMF Shares would be subject to proposed Nasdaq Rules

5745(d)(2)(B) and (C), which provide for the suspension of trading or trading halts under certain circumstances, including if, in the view of the Exchange, trading in ETMF Shares becomes inadvisable.

The proposed rule change is designed to perfect the mechanism of a free and open market and, in general, to protect investors and the public interest. Proposed Nasdaq Rule 5745 will permit the listing and trading of a new type of exchange-traded product that can provide investors with access to a broad range of active strategies in a structure that provides the cost and tax efficiencies and shareholder protections of ETFs, while removing the requirement for portfolio transparency to ensure a tight relationship between market trading prices and NAV. Because proposed Nasdaq Rule 5745 would not require ETMFs to publish portfolio positions daily, ETMFs are expected to have broad appeal among active managers who seek to make their strategies available in an exchange-traded structure, but have not embraced Active ETFs due to concerns about the adverse effects of publicly disclosing portfolio trading information on a daily basis.

For the above reasons, Nasdaq believes the proposed rule change is consistent with the requirements of Section 6(b)(5) of the Act.

With respect to the imposition of initial entry fees and annual fees for the listing of ETMF Shares under proposed Nasdaq Rule 5940, Nasdaq believes that the proposed fees are reasonable and equitably allocated. Nasdaq notes that the proposed fees would be in the same amount as the entry fees and annual fees that apply to Portfolio Depository Receipts, Index Fund Shares and Managed Fund Shares, which, like ETMF Shares, are exchange-listed shares of investment companies registered under the 1940 Act.

Accordingly, Nasdaq believes the proposed rule change is consistent with the requirements of Section 6(b)(4) of the Act.

4. Self-Regulatory Organization's Statement on Burden on Competition

The Exchange does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. In fact, the Exchange believes that the introduction of ETMFs would promote competition. ETMFs would permit investment managers that have been unwilling to sponsor Active ETFs to introduce actively managed exchange-traded investment companies with features that could be attractive to investors. The Exchange believes that the NAV-Based Trading of ETMF Shares would provide investors with an ability to control trading costs in a way that is not normally available in conventional ETF trading. These developments could significantly enhance competition to the benefit of the markets and investors.

Nasdaq intends to enter into a license agreement to allow for the listing and trading of ETMF Shares.<sup>25</sup> ETMF Shares listed on the Exchange may trade pursuant to UTP on other national securities exchanges that have obtained appropriate licenses, adopted applicable exchange rules and developed systems to support NAV-Based Trading. Fees collected by the Exchange in connection with the listing and trading of ETMF Shares will comply with the statutory requirements set forth in the Act. Nasdaq believes that this proposal would enable a unique investment product to begin trading in a regulated exchange environment and thereby provide additional trading choices to the benefit of investors, including retail investors.

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<sup>25</sup> As noted above, aspects of ETMFs and NAV-Based Trading are protected intellectual property subject to issued and pending U.S. patents.



5. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others  
Written comments were neither solicited nor received.
6. Extension of Time Period for Commission Action  
Not applicable.
7. Basis for Summary Effectiveness Pursuant to Section 19(b)(3) or for Accelerated Effectiveness Pursuant to Section 19(b)(2)  
Not applicable.
8. Proposed Rule Change Based on Rules of Another Self-Regulatory Organization or of the Commission  
Not applicable.
9. Security-Based Swap Submissions Filed Pursuant to Section 3C of the Act  
Not applicable.
10. Advance Notices Filed Pursuant to Section 806(e) of the Payment, Clearing and Settlement Supervision Act  
Not applicable.
11. Exhibits
  1. Form of Notice of the Proposed Rule Change for the Federal Register.
  5. Text of Proposed Rule Change

**EXHIBIT 1**SECURITIES AND EXCHANGE COMMISSION  
(Release No. 34- ; File No. SR-NASDAQ-2014-020)

February \_\_, 2014

Self-Regulatory Organizations; The NASDAQ Stock Market LLC; Notice of Proposed Rule Change Relating to Listing and Trading of Exchange-Traded Managed Fund Shares

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”),<sup>1</sup> and Rule 19b-4 thereunder,<sup>2</sup> notice is hereby given that on February 14, 2014, The NASDAQ Stock Market LLC (“Nasdaq” or the “Exchange”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in in Items I, II, and III below, which Items have been prepared by Nasdaq. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Self-Regulatory Organization’s Statement of the Terms of Substance of the Proposed Rule Change

Pursuant to the provisions of Section 19(b)(1) of the Act,<sup>3</sup> and Rule 19b-4 thereunder,<sup>4</sup> Nasdaq is filing with the Commission a proposed rule change to list and trade under proposed Nasdaq Rule 5745 the shares of a proposed new type of open-end management investment company registered under the Investment Company Act of 1940, as amended (“1940 Act”), called an Exchange-Traded Managed Fund (“ETMF”), and to amend related references under Nasdaq Rules 4120, 5615 (and IM-5615-4) and 5940.

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<sup>1</sup> 15 U.S.C. 78s(b)(1).

<sup>2</sup> 17 CFR 240.19b-4.

<sup>3</sup> 15 U.S.C. 78s(b)(1).

<sup>4</sup> 17 CFR 240.19b-4.

The text of the proposed rule change is available at <http://nasdaq.cchwallstreet.com/>, at Nasdaq's principal office, and at the Commission's Public Reference Room.

II. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, Nasdaq included statements concerning the purpose of, and basis for, the proposed rule change. The text of these statements may be examined at the places specified in Item IV below, and is set forth in Sections A, B, and C below.

A. Self-Regulatory Organization's Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

1. Purpose

The Exchange proposes to adopt Nasdaq Rule 5745 for the purpose of permitting the listing and trading of ETMF Shares. Similar to Managed Fund Shares as defined in Nasdaq Rule 5735,<sup>5</sup> ETMF Shares would be issued in specified aggregate unit quantities in return for a deposit of a specified basket of securities and/or a cash amount with a value equal to the product of the ETMF's net asset value per Share ("NAV") and the number of Shares issued. When aggregated in the same specified unit quantities, ETMF Shares could be redeemed in exchange for a specified basket of securities and/or cash with a value per Share equal to the ETMF's NAV. Unlike Managed Fund Shares, ETMF Shares would trade on Nasdaq using a new trading protocol called "NAV-Based Trading." In NAV-Based Trading, all bids, offers and execution prices would be

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<sup>5</sup> The Commission approved Nasdaq Rule 5735 in Securities Exchange Act Release No. 57962 (June 13, 2008), 73 FR 35175 (June 20, 2008) (SR-NASDAQ-2008-039).

expressed as a premium/discount (which may be zero) to the ETMF's next-determined NAV (*e.g.*, NAV-\$0.01; NAV+\$0.01). An ETMF's NAV would be determined each business day, normally as of 4:00 p.m. Eastern Time. Trade executions using NAV-Based Trading would be binding at the time orders are matched on Nasdaq's facilities, with the transaction prices contingent upon the determination of the ETMF's NAV at the end of the business day.

Proposed Listing Rules for Exchange-Traded Managed Fund Shares

Proposed Nasdaq Rule 5745(b)(1) provides that Nasdaq will file separate proposals under Section 19(b) of the Act before the listing of ETMF Shares. Proposed Nasdaq Rule 5745(b)(2) provides that transactions in ETMF Shares will occur during Nasdaq's Regular Market Session through 4:00 p.m.<sup>6</sup> Proposed Nasdaq Rule 5745(b)(3) provides that ETMF Shares will trade on Nasdaq at market-determined premiums or discounts to the next-determined NAV, and that the minimum price variation for quoting and entry of orders in ETMF Shares will be \$0.01. Proposed Rule Nasdaq 5745(b)(4) provides that Nasdaq will implement written surveillance procedures for ETMF Shares. Proposed Nasdaq Rule 5745(b)(5) provides that, for ETMF Shares based on an international or global portfolio, the statutory prospectus or the application for exemption from provisions of the 1940 Act for such series of ETMF Shares must state that such series must comply with the federal securities laws in accepting securities for deposit and satisfying redemptions with securities, including that the securities accepted for deposit and the securities used to satisfy redemption requests are sold in transactions that would be exempt from registration under the Securities Act of 1933 ("Securities Act").

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<sup>6</sup> Nasdaq Rule 4120(b)(4) defines the Regular Market Session as the trading session from 9:30 a.m. to 4:00 p.m. or 4:15 p.m. ETMF Shares will trade until 4:00 p.m.

Proposed Definitions. Proposed Nasdaq Rule 5745(c)(1) defines the term “ETMF Share” as a security that: (1) represents an interest in a registered investment company organized as an open-end management investment company that invests in a portfolio of securities and other assets selected and managed by the ETMF’s investment adviser consistent with the ETMF’s investment objectives and policies; (2) is issued in specified aggregate unit quantities in return for a deposit of a specified portfolio of securities and/or a cash amount with a value per Share equal to the ETMF’s NAV; (3) when aggregated in the same specified unit quantities, may be redeemed in exchange for a specified portfolio of securities and/or cash with a value per Share equal to the ETMF’s NAV; and (4) is traded on a national securities exchange using NAV-Based Trading.

In addition, proposed Nasdaq Rule 5745(c)(2) defines the term “Intraday Indicative Value” (“IIV”) as the estimated indicative value of an ETMF Share based on current information regarding the value of the securities and other assets held by the ETMF. Proposed Nasdaq Rule 5745(c)(3) defines the term “Composition File” as the specified portfolio of securities and/or cash that an ETMF will accept as a deposit in issuing ETMF Shares and the specified portfolio of securities and/or cash that an ETMF will deliver in a redemption of ETMF Shares. The current Composition File will be disseminated through the National Securities Clearing Corporation (“NSCC”) once each business day before the open of trading in ETMF Shares on Nasdaq on such day. To maintain the confidentiality of current portfolio trading, an ETMF’s Composition File generally will not be a pro rata reflection of the ETMF’s securities positions. Each security included in the Composition File will be a current holding of the ETMF, but the Composition File generally will not include all of the securities in the ETMF’s portfolio

or match the weightings of the included securities in the portfolio. The Composition File also may consist entirely of cash, in which case it will not include any of the securities in the ETMF's portfolio.

Proposed Nasdaq Rule 5745(c)(4) defines the term "Reporting Authority" as Nasdaq, an institution or a reporting service designated by Nasdaq as the official source for calculating and reporting information relating to such series of ETMF Shares, including, but not limited to, the IIV, the amount of any cash distribution to holders of ETMF Shares, NAV, the Composition File or other information relating to the issuance, redemption or trading of ETMF Shares. A series of ETMF Shares may have more than one Reporting Authority, each having different functions.

Initial and Continued Listing. Proposed Nasdaq Rule 5745(d) sets forth the initial and continued listing criteria applicable to ETMF Shares.<sup>7</sup> Proposed Nasdaq Rule 5745(d)(1)(A) provides that, for each series of ETMF Shares, Nasdaq will establish a

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<sup>7</sup> An investment adviser to an ETMF would be registered under the Investment Advisers Act of 1940 (the "Advisers Act"). As a result, the investment adviser and any subadviser and their related personnel would be subject to the provisions of Rule 204A-1 under the Advisers Act relating to codes of ethics. This Rule requires investment advisers to adopt a code of ethics that reflects the fiduciary nature of the relationship to clients as well as compliance with other applicable securities laws. Accordingly, procedures designed to prevent the communication and misuse of non-public information by an investment adviser must be consistent with Rule 204A-1 under the Advisers Act. In addition, Rule 206(4)-7 under the Advisers Act makes it unlawful for an investment adviser to provide investment advice to clients unless such investment adviser has (i) adopted and implemented written policies and procedures reasonably designed to prevent violation, by the investment adviser and its supervised persons, of the Advisers Act and the Commission rules adopted thereunder; (ii) implemented, at a minimum, an annual review regarding the adequacy of the policies and procedures established pursuant to subparagraph (i) above and the effectiveness of their implementation; and (iii) designated an individual (who is a supervised person) responsible for administering the policies and procedures adopted under subparagraph (i) above. The Exchange represents that, for initial and/or continued listing, an ETMF must be in compliance with Rule 10A-3 under the Act. 17 CFR 240.10A-3.

minimum number of ETMF Shares required to be outstanding at the time of commencement of trading. In addition, under proposed Nasdaq Rule 5745(d)(1)(B), Nasdaq must obtain a representation from the issuer of each series of ETMF Shares that the NAV for such series will be calculated on each business day that the New York Stock Exchange is open for trading and that the NAV will be made available to all market participants at the same time. Under proposed Nasdaq Rule 5745(d)(1)(C), the Reporting Authority that provides the Composition File must implement and maintain, or be subject to, procedures designed to prevent the use and dissemination of material non-public information regarding the ETMF's portfolio positions and changes in positions.

Proposed Nasdaq Rule 5745(d)(2)(A) provides that each series of ETMF Shares could continue to be listed and traded if the IIV for the ETMF Shares is widely disseminated by one or more major market data vendors at intervals of not more than 15 minutes during the Regular Market Session when the ETMF Shares trade on Nasdaq. Proposed Nasdaq Rule 5745(d)(2)(B) provides that Nasdaq will consider the suspension of trading in, or removal from listing of, a series of ETMF Shares under any of the following circumstances: (1) if, following the initial twelve-month period after commencement of trading on the Exchange of a series of ETMF Shares, there are fewer than 50 beneficial holders of the series of ETMF Shares for 30 or more consecutive trading days; (2) if the ETMF's IIV or NAV is no longer calculated or if its IIV, NAV or Composition File is no longer available to all market participants at the same time; (3) if the ETMF has failed to submit any filings required by the Commission or if Nasdaq is aware that the ETMF is not in compliance with the conditions of any exemptive order or no-action relief granted by the Commission with respect to the series of ETMF Shares; or

(4) if such other event shall occur or condition exists which, in the opinion of Nasdaq, makes further dealings on Nasdaq inadvisable.

Proposed Nasdaq Rule 5745(d)(2)(C) provides that, if the IIV of a series of ETMF Shares is not being disseminated as required, Nasdaq may halt trading during the day in which the interruption to the dissemination of the IIV occurs. If the interruption to the dissemination of the IIV persists past the trading day in which it first occurred, Nasdaq will halt trading no later than the beginning of the trading day following the interruption. In addition, if the Exchange becomes aware that the NAV with respect to a series of ETMF Shares is not calculated on each business day that the New York Stock Exchange is open for trading and disseminated to all market participants at the same time, it will halt trading in such series until such time as the NAV is available to all market participants. If Nasdaq becomes aware that the Composition File with respect to a series of ETMF Shares is not disseminated to all market participants at the same time, it will halt trading in such series until such time as the Composition File is available to all market participants.

In addition, proposed Nasdaq Rule 5745(d)(2)(D) provides that, upon termination of an ETMF, the ETMF Shares issued in connection with such entity must be removed from listing on Nasdaq. Proposed Nasdaq Rule 5745(d)(2)(E) provides that voting rights must be as set forth in the applicable ETMF prospectus.

Additional Provisions. Proposed Nasdaq Rule 5745(e) provides that neither Nasdaq, the Reporting Authority nor any agent of Nasdaq shall have any liability for damages, claims, losses or expenses caused by any errors, omissions or delays in calculating or disseminating any of the following: the current portfolio value; the current



value of the securities and other assets required to be deposited in connection with issuance of ETMF Shares; the amount of any dividend-equivalent payment or cash distribution to holders of ETMF Shares; NAV; the Composition File; or other information relating to the purchase, redemption or trading of ETMF Shares, resulting from any negligent act or omission by Nasdaq, the Reporting Authority or any agent of Nasdaq, or any act, condition or cause beyond the reasonable control of Nasdaq, its agent or the Reporting Authority, including, but not limited to, an act of God, fire, flood, extraordinary weather conditions, war, insurrection, riot, strike, accident, action of government, communications or power failure, equipment or software malfunction, or any error, omission or delay in the reports of transactions in one or more underlying securities.

Proposed Nasdaq Rule 5745(f) applies only to series of ETMF Shares that are the subject of an order by the Commission exempting such series from certain prospectus delivery requirements under Section 24(d) of the 1940 Act and are not otherwise subject to prospectus delivery requirements under the Securities Act. Nasdaq will inform its members regarding application of Proposed Nasdaq Rule 5745(f) to a particular series of ETMF Shares by means of an information circular prior to commencement of trading in such series. Under the proposed rule, Nasdaq requires that members provide to all purchasers of a series of ETMF Shares a written description of the terms and characteristics of those securities, in a form prepared by the open-end management investment company issuing such securities, not later than the time a confirmation of the first transaction in such series is delivered to such purchaser. In addition, members shall include such a written description with any sales material relating to a series of ETMF

Shares that is provided to customers or the public. Any other written materials provided by a member to customers or the public making specific reference to a series of ETMF Shares as an investment vehicle must include a statement in substantially the following form: “A circular describing the terms and characteristics of (the series of ETMF Shares) has been prepared by the (open-end management investment company name) and is available from your broker. It is recommended that you obtain and review such circular before purchasing (the series of ETMF Shares).” A member carrying an omnibus account for a non-member broker-dealer is required to inform such non-member that execution of an order to purchase a series of ETMF Shares for such omnibus account will be deemed to constitute agreement by the non-member to make such a written description available to its customers on the same terms as are directly applicable to members under this rule. Upon request of a customer, a member shall also provide a prospectus for the particular series of ETMF Shares.

Proposed Nasdaq Rule 5745(g) provides that, if the investment adviser to an ETMF issuing Shares is a registered broker-dealer or affiliated with a broker-dealer, such investment adviser shall erect a “fire wall” between the investment adviser and the broker-dealer personnel or broker-dealer affiliate, as applicable, with respect to access to information concerning the composition and/or changes to such ETMF’s portfolio holdings. Personnel who make decisions on the ETMF’s portfolio composition must be subject to procedures designed to prevent the use and dissemination of material nonpublic information regarding the applicable ETMF portfolio.

### Other Proposed Rule Changes

The Exchange also proposes to amend: (1) Nasdaq Rule 4120(a)(9) and (10) to add provisions applicable to ETMF Shares with respect to trading halts; (2) Nasdaq Rule 4120(b)(4)(A) and (E) to modify certain defined terms to include references to ETMF Shares; (3) Nasdaq Rule 5615(a)(5) and IM-5615-4 to add references to ETMFs for purposes of certain corporate governance requirements; and (4) Nasdaq Rule 5940(a) and (b) to add references to ETMF Shares to those securities already covered under the rule relating to both entry fees and annual fees.<sup>8</sup>

### Key Features of ETMF Shares

Open-End Registered Investment Company. An ETMF Share means a security that represents an interest in an open-end investment company registered under the 1940 Act that invests in a portfolio of securities and other assets selected and managed by its investment adviser consistent with its investment objectives and policies and which is traded on a national securities exchange using NAV-Based Trading.

1940 Act Exemptive Relief. The 1940 Act contemplates management investment companies that either (1) issue redeemable securities (*i.e.*, open-end investment companies) or (2) do not issue redeemable securities (*i.e.*, closed-end investment companies). ETMF Shares are redeemable, but only in large blocks of shares, not individually. Because exchange-traded funds (“ETFs”) issuing Managed Fund Shares (“Active ETFs”) do not fit neatly into either the open-end category or the closed-end category, Active ETFs have had to seek exemptive relief from the Commission to permit

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<sup>8</sup> The Exchange also proposes to make certain other minor technical changes to these rules unrelated to ETMFs. Specifically, the Exchange proposes to amend Rule 4120(a)(9), (b)(4)(A), and (b)(4)(E) to include appropriate references to various derivative securities defined in Rule 5711.

registration as an open-end investment company. ETMFs share some key structural features with Active ETFs, including creations and redemptions only in large blocks of shares, and require exemptive relief from the Commission from substantially the same provisions of the 1940 Act.

Creations and Redemptions. As with Managed Fund Shares, ETMF Shares will be issued and redeemed on a daily basis at NAV<sup>9</sup> in specified blocks of Shares called “Creation Units.” Creation Units may be purchased and redeemed by or through “Authorized Participants.”<sup>10</sup> Purchases and sales of Shares in amounts smaller than the number of Shares required for a Creation Unit may be effected only in the secondary market through NAV-based transactions, as described below, and not directly with the ETMF.

As with Active ETFs, the creation and redemption process for ETMFs may be effected “in kind,” in cash, or in a combination of securities and cash. Creation “in kind” means that the Authorized Participant—usually a brokerage house or large institutional

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<sup>9</sup> As with other registered open-end investment companies, the NAV of ETMF Shares generally would be calculated daily Monday through Friday as of the close of regular trading on the New York Stock Exchange, normally 4:00 p.m. Eastern Time. NAV would be calculated by dividing the ETMF’s net asset value by the number of ETMF Shares outstanding. Information regarding the valuation of investments in calculating the ETMF’s NAV would be contained in the registration statement for the ETMF Shares.

<sup>10</sup> “Authorized Participants” would be either: (1) “participating parties,” *i.e.*, brokers or other participants in the Continuous Net Settlement System of the NSCC, a clearing agency registered with Commission and affiliated with the Depository Trust Company (“DTC”), or (2) DTC participants, which in either case have executed participant agreements with the ETMF’s distributor and transfer agent regarding the creation and redemption of Creation Units. Investors would not have to be Authorized Participants in order to transact in Creation Units, but must place an order through and make appropriate arrangements with an Authorized Participant for such transactions.

investor—purchases the Creation Unit with a basket of securities equal in value to the aggregate NAV of the Shares in the Creation Unit. When an Authorized Participant redeems a Creation Unit in kind, it receives a basket of securities equal in value to the aggregate NAV of the Shares in the Creation Unit.

Composition File. As defined in proposed Nasdaq Rule 5475(c)(3), the Composition File is the specified portfolio of securities and/or cash that an ETMF will accept as a deposit in issuing a Creation Unit of ETMF Shares, and the specified portfolio of securities and/or cash that an ETMF will deliver in a redemption of a Creation Unit of ETMF Shares. The Composition File will be disseminated through the NSCC once each business day before the open of trading in ETMF Shares on such day. Because ETMFs seek to preserve the confidentiality of their current portfolio trading program, the Composition File generally will not be a pro rata reflection of the ETMF's securities positions. Each security included in the Composition File will be a current holding of the ETMF, but the Composition File generally will not include all of the securities in the ETMF's portfolio or match the weightings of the included securities in the portfolio. Securities that the investment adviser to the ETMF is in the process of acquiring for the ETMF generally would not be represented in the Composition File until their purchase has been completed. Similarly, securities that are held in the ETMF's portfolio but in the process of being sold may not be removed from the Composition File until the sale program is substantially completed. ETMFs creating and redeeming Shares in kind would use cash amounts to supplement the in-kind transactions to the extent necessary to ensure that Creation Units are purchased and redeemed at NAV. The Composition File

also may consist entirely of cash, in which case it will not include any of the securities in the ETMF's portfolio.<sup>11</sup>

NAV-Based Trading. Because ETMF Shares will be listed and traded on the Exchange, ETMF Shares will be available for purchase and sale on an intraday basis, like shares of conventional ETFs and other listed securities. Different from conventional ETF share trading, however, ETMF Shares would be purchased and sold in the secondary market at prices based on the next-determined NAV. All bids, offers and execution prices would be expressed as a premium/discount (which may be zero) to the ETMF's next-determined NAV (e.g., NAV-\$0.01, NAV+\$0.01). An ETMF's NAV would be determined each business day, normally as of 4:00 p.m. Eastern Time. Trade executions would be binding at the time orders are matched on Nasdaq's facilities, with the transaction prices contingent upon the determination of NAV.

- *Trading Premiums and Discounts.* ETMF Share prices would be quoted throughout the day relative to NAV. The premium or discount to NAV at which ETMF Share prices are quoted and transactions are executed would vary depending on market factors, including the balance of supply and demand for ETMF Shares among investors, transaction fees and other costs in connection with creating and redeeming Creation Units of ETMF Shares, competition among market makers and other arbitrageurs, the ETMF Share inventory positions and inventory strategies of market makers and other arbitrageurs, and the volume of ETMF Share trading. Reflecting these and other market

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<sup>11</sup> In determining whether an ETMF will issue or redeem Creation Units entirely on a cash basis, the key consideration will be the benefit that would accrue to the ETMF and its investors. For instance, in bond transactions, the investment adviser to the ETMF may be able to obtain better execution than Authorized Participants because of the investment adviser's size, experience and potentially stronger relationships in the fixed-income markets.

factors, prices for ETMF Shares in the secondary market may be above, at or below NAV.

- *Transmitting and Processing Orders.* Member firms would utilize existing order types and interfaces to transmit ETMF Share bids and offers to Nasdaq, which would process ETMF Share trades like trades in shares of conventional ETFs and other listed securities. In the systems used to transmit and process transactions in ETMF Shares, Nasdaq expects an ETMF's next-determined NAV to be represented by a proxy price (*e.g.*, 100.00) and a premium/discount of a stated amount to the next-determined NAV to be represented by the same increment/decrement from the proxy price used to denote NAV (*e.g.*, NAV-\$0.01 would be represented as 99.99; NAV+\$0.01 as 100.01).<sup>12</sup>

To avoid potential investor confusion, Nasdaq would work with member firms and providers of market data services to seek to ensure that representations of intraday bids, offers and execution prices for ETMFs that are made available to the investing public follow the "NAV-\$0.01/NAV+\$0.01" (or similar) display format, rather than displaying proxy prices. Nasdaq expects all ETMFs listed on the Exchange to have a

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<sup>12</sup> Order transmission and processing systems currently in common use by exchanges and member firms are generally not designed to accommodate pricing arrangements, such as NAV-Based Trading, in which bids, offers and execution prices are determined by reference to a price or value that is unknown at the time of trade execution. Compared to the alternative of building and maintaining (and requiring member firms to build and maintain) a dedicated NAV-Based Trading order transmission and processing system, the Exchange believes that the proposed approach (using, for processing purposes, a proxy price to represent next-determined NAV) offers major advantages in terms of cost, efficiency and time to implement. To convert proxy prices used to represent intraday bids, offers and execution prices into prices expressed in relation to the next-determined NAV, member firms would subtract from the reported proxy price (*e.g.*, 99.99) the proxy for NAV (*e.g.*, 100.00) and inserting "NAV" in front of the calculated number expressed in dollars (*e.g.*,  $99.99 - 100.00 = -0.01$ , expressed as "NAV-\$0.01").

unique identifier associated with their ticker symbols, which would indicate that their Shares are traded using NAV-Based Trading. Nasdaq makes available to member firms and market data services certain proprietary data feeds (“Nasdaq Data Feeds”) that are designed to supplement the market information disseminated through the consolidated tape (“Consolidated Tape”). The Exchange would use a Nasdaq Data Feed to disseminate intraday price and quote data for ETMFs in real time in the “NAV-\$0.01/NAV+\$0.01” (or similar) display format. Member firms could use the Nasdaq Data Feed to source intraday ETMF prices for presentation to the investing public in the “NAV-\$0.01/NAV+\$0.01” (or similar) display format. Alternatively, member firms could source intraday ETMF prices in proxy price format from the Consolidated Tape and use a simple algorithm to convert prices into the “NAV-\$0.01/NAV+\$0.01” (or similar) display format.

- *Intraday Reporting of Quotes and Trades.* All ETMF bids, offers and trade executions would be reported intraday in real time by the Exchange to the Consolidated Tape<sup>13</sup> and separately disseminated to member firms and market data services through a Nasdaq Data Feed. The Exchange would also provide the member firms participating in each ETMF Share trade with a contemporaneous notice of trade execution, indicating the number of ETMF Shares bought or sold and the executed premium/discount to NAV.<sup>14</sup>

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<sup>13</sup> Due to systems limitations, the Consolidated Tape would report intraday execution prices and quotes for ETMFs using a proxy price format. As noted, Nasdaq would separately report real-time execution prices and quotes to member firms and providers of market data services in the “NAV-\$0.01/NAV+\$0.01” (or similar) display format, and otherwise seek to ensure that representations of intraday bids, offers and execution prices for ETMFs that are made available to the investing public follow the same display format.

<sup>14</sup> All orders to buy or sell an ETMF Share that are not executed on the day the order is submitted will be automatically cancelled as of the close of trading on such day.



• *Final Trade Pricing, Reporting and Settlement.* All executed ETMF Share trades would be recorded and stored intraday by Nasdaq to await the calculation of the ETMF's end-of-day NAV and the determination of final trade pricing. After the Reporting Authority calculates an ETMF's NAV and provides this information to the Exchange, Nasdaq would price each ETMF Share trade entered into during the day at the ETMF's NAV plus/minus the trade's executed premium/discount. Using the final trade price, each executed ETMF Share trade would then be disseminated to member firms and market data services through the Nasdaq Data Feed used to report ETMF Share trades, and confirmed to the member firms participating in the trade to supplement the previously provided information to include final pricing. After the pricing is finalized, Nasdaq would deliver the ETMF Share trading data to NSCC for clearance and settlement, following the same processes used for the clearance and settlement of trades in conventional ETFs and other exchange-traded securities.

Portfolio Disclosure and ETMF Share Trading Efficiency. As required for traditional open-end investment companies, ETMFs would disclose their full portfolio positions at least quarterly, with a delay (not to exceed 60 days) to limit opportunities for other market participants to engage in predatory trading practices that might harm fund shareholders.<sup>15</sup>

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<sup>15</sup> See 17 CFR 249.332; 17 CFR 274.130. In adopting the requirement for quarterly portfolio disclosure with not more than a 60 day delay, the Commission noted that it took seriously concerns that more frequent portfolio disclosure and/or a shorter delay for release of this information might expand the opportunities for other market participants to engage in predatory trading practices that harm fund shareholders. Shareholder Reports and Quarterly Portfolio Disclosure of Registered Management Investment Companies, Securities Exchange Act Release No. 49333 (Feb. 27, 2004). As with traditional mutual funds, an ETMF could elect to provide more frequent disclosure of portfolio positions, if appropriate.

Rule 5735 requires Active ETFs to disclose publicly their full portfolio positions at least once daily. The purpose of this requirement is to provide Active ETF market makers with the portfolio information needed to hedge the intraday market risk they assume as they take inventory positions in connection with their market making activities. In conventional ETF trading, a condition to maintaining a tight relationship between market trading prices and contemporaneous underlying portfolio values is that market makers have sufficient information regarding portfolio positions to enable them to earn reliable arbitrage profits by entering into long (or short) positions in ETF shares and offsetting short (or long) positions in the underlying holdings (or a suitable proxy).

In ETMF trading, by contrast, a market maker assumes no intraday market risk in connection with its inventory positions because all ETMF Share transaction prices are based on the next-determined NAV. Whether an ETMF's underlying value goes up or down over the course of a trading day will not affect how much profit a market maker earns by selling (or buying) ETMF Shares in the market at a net premium (discount) to NAV, and then purchasing (redeeming) an offsetting number of ETMF Shares at the end of the day in transactions with the ETMF. No intraday market risk means no requirement for intraday hedging, and therefore no associated requirement for portfolio disclosure to maintain a tight relationship between ETMF Share trading prices and NAV.

The arbitrage that connects ETMF trading prices to NAV is effected at the end of each trading day when a market maker or other arbitrageur purchases (or redeems) Creation Units of ETMF Shares through an Authorized Participant to offset the net amount of ETMF Shares it has sold (bought) over the course of the trading day, and buys (sells) the quantity of Composition File instruments corresponding to the number of

Creation Units purchased (redeemed). An ETMF market maker that purchases (or redeems) a Creation Unit at the end of a trading day to offset its net intraday sales (purchases) of a Creation Unit quantity of ETMF Shares will earn arbitrage profits to the extent that it either sells (buys) Shares at an aggregate premium (discount) to NAV or buys (sells) a Creation Unit-equivalent quantity of Composition File instruments at an aggregate discount (premium) to their end-of-day values, and the net amount of ETMF premium (discount) plus Composition File instruments discount (premium) exceeds the transaction fee that applies to a purchase (redemption) of a Creation Unit of ETMF Shares.<sup>16</sup>

Different from ETFs trading in conventional intraday markets, ETMFs offer market makers an arbitrage profit opportunity that does not depend on either corresponding intraday adjustments in fund share and underlying portfolio positions or the use of a hedge portfolio to manage intraday market risk. A “perfect arbitrage” in an ETMF requires only that market makers holding short (or long) positions in ETMF Shares accumulated intraday transact with the ETMF to purchase (redeem) a corresponding number of Creation Units of ETMF Shares, buy (sell) the equivalent quantities of Composition File instruments at market-closing or better prices, and offload

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<sup>16</sup> The arbitrage mechanism is simplified for cash creations and redemptions. An ETMF market maker that purchases (or redeems) a Creation Unit in cash to offset its net intraday sales (purchases) of a Creation Unit quantity of ETMF Shares will earn arbitrage profits to the extent that it sells (buys) ETMF Shares in the secondary market at an aggregate premium (discount) to NAV that exceeds the transaction fee that applies to a cash creation (redemption) of a Creation Unit of ETMF Shares.

any remaining sub-Creation Unit ETMF Share inventory through secondary market transactions by the market close.<sup>17</sup>

Because the arbitrage mechanism that underlies ETMF trading is simpler, more reliable and exposes market makers to less risk than ETF arbitrage, market makers should require less profit inducement to establish and maintain markets in ETMF Shares than in similarly constituted ETFs, thereby enabling ETMFs to routinely trade at smaller premiums/discounts and narrower bid-ask spreads. Further, because the arbitrage mechanism that underlies efficient trading of ETMFs does not involve portfolio positions that are not included in the Composition File, the need for full portfolio transparency to achieve tight markets in ETMF Shares is eliminated.

Recognizing the potential harm to shareholders of disclosing portfolio trading information on a current basis (and the absence of a need for such information to maintain tight trading markets using NAV-Based Trading), proposed Nasdaq Rule 5745 would not require daily portfolio disclosure or specify a minimum level of correspondence between an ETMF's portfolio positions and its Composition File.

Intraday Indicative Value. For each series of ETMF Shares, an estimated value of an individual ETMF Share, defined in proposed Nasdaq Rule 5745(c)(2) as the "Intraday

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<sup>17</sup> Market makers are expected generally to seek to minimize their exposure to price risk in ETMF Shares by holding little or no overnight inventory. Establishing Creation Unit sizes for ETMFs that are somewhat smaller (*i.e.*, in a range of 5,000 to 50,000 Shares) than is customary for ETFs should support efficient arbitrage between an ETMF's trading prices and NAV by facilitating tighter market maker inventory management. To the extent that market makers hold small positions in ETMF Shares overnight, they are expected to aggregate such holdings with other risk positions and transact at or near the market close to buy or sell offsetting positions in appropriate, broad-based hedging instruments. Such hedging of overnight inventory risk on a macro basis does not require disclosure of non-Composition File portfolio positions.

Indicative Value,” would be widely disseminated by one or more major market data vendors at intervals of not more than 15 minutes throughout the Regular Market Session when ETMF Shares trade on the Exchange. The IIV would be based on current information regarding the value of the securities and other assets held by an ETMF.<sup>18</sup> Unlike Nasdaq Rule 5735, which requires dissemination of IIVs every 15 seconds for Managed Fund Shares, proposed Nasdaq Rule 5745 would not require the dissemination of an IIV on such a frequent basis. Dissemination of IIVs plays a different, and lesser, role in NAV-Based Trading of ETMF Shares than in conventional ETF trading. For Managed Fund Shares (and ETFs generally), the primary purpose of IIVs is to provide retail investors with a measure of the contemporaneous underlying value of a fund’s positions, allowing them to assess the reasonableness of trading prices in relation to underlying value. For ETMF Shares, NAV-Based Trading provides investors with a direct measure of the relationship between trading prices and NAV (*e.g.*, NAV-\$0.01, NAV+\$0.02) and, using limit orders, a means for controlling the premium or discount to NAV at which they trade shares. The purpose of IIVs in NAV-Based Trading is to enable investors to estimate the next-determined NAV so they can determine the number of ETMF Shares to buy or sell if they want to transact in an approximate dollar amount (*e.g.*, if an investor wants to acquire approximately \$5,000 of an ETMF, how many Shares should the investor buy?).<sup>19</sup> For this purpose, dissemination of IIVs at intervals of

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<sup>18</sup> IIVs disseminated throughout each trading day would be based on the same portfolio as used to calculate that day’s NAV. Like Managed Fund Shares, ETMFs will reflect purchases and sales of portfolio positions in their NAV the next business day after trades are executed.

<sup>19</sup> Because, in NAV-Based Trading, prices of executed trades are not determined until the reference NAV is calculated, buyers and sellers of ETMF Shares during the trading day will not know the final value of their purchases and sales until the

not more than 15 minutes should generally be sufficient. More frequent dissemination of IIVs may increase fund costs without apparent benefit and could focus unwarranted investor attention on these disclosures. Moreover, for certain strategies, more frequent IIV disclosure could provide unintended information about current portfolio trading activity to market participants who possess the requisite analytical capabilities, computation power and motivation to reverse engineer the ETMF's portfolio positions. As proposed, an ETMF would be permitted to disseminate IIVs at intervals of less than 15 minutes, but would not be required to do so to maintain trading on the Exchange.

Availability of Information. Prior to the commencement of market trading in ETMF Shares, each ETMF will be required to establish and maintain a public website through which its current prospectus may be downloaded. The website will include additional ETMF information updated on a daily basis, including most recent NAV. The

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end of the trading day. An ETMF's registration statement, website and any advertising or marketing materials will include prominent disclosure of this fact. Although IIVs may provide useful estimates of the value of intraday trades, they cannot be used to calculate with precision the dollar value of the ETMF Shares to be bought or sold. An IIV of an ETMF will generally differ from NAV to the extent that the value of the ETMF's portfolio holdings change intraday between the time the IIV is calculated and the end of the trading day. The fact that an investor placing an order to purchase or sell ETMF Shares would not know the trade price at the time the order is entered is similar to certain existing order types in conventional share trading. For standard market orders, trading prices are not known until the order executes. For market-on-close orders, trading prices are not established until the end of the trading day. In addition, for purchases and sales of share quantities of mutual funds, an investor does not know the transaction value until NAV is calculated at the end of the day. Member firms may have different systems for communicating these trade characteristics to their customers and for ensuring that customers have sufficient resources to engage in these trades. Member firms may require that a cash buffer be maintained in a customer's account relative to the current value of the security to be purchased. Alternatively, customers may have margin accounts or arrangements with their broker-dealer to provide for payment subsequent to trade execution, but prior to trade settlement.

Composition File will be disseminated through the NSCC before the open of trading in ETMF Shares on Nasdaq on each business day. Consistent with the disclosure requirements that apply to traditional open-end investment companies, a complete list of current ETMF portfolio positions will be made available at least once each calendar quarter, with a reporting lag of not more than 60 days. ETMFs may provide more frequent disclosures of portfolio positions at their discretion.

Reports of ETMF Share transactions will be disseminated to the market and delivered to the member firms participating in the trade contemporaneous with execution. Once an ETMF's daily NAV has been calculated, Nasdaq would price each ETMF Share trade entered into during the day at the ETMF's NAV plus/minus the trade's executed premium/discount. Using the final trade price, each executed ETMF Share trade would then be disseminated to member firms and market data services through the Nasdaq Data Feed used to report ETMF Share trades, and confirmed to the member firms participating in the trade to supplement the previously provided information to include final pricing.

Information regarding NAV-based trading prices and volumes of ETMF Shares will be continually available on a real-time basis throughout each trading day on brokers' computer screens and other electronic services. The previous trading day's closing price and volume information for the ETMF Shares will be published daily.

Exchange Listing. Nasdaq intends to enter into a license agreement to allow for the listing and trading of ETMF Shares on the Exchange.<sup>20</sup> ETMF Shares listed on the

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<sup>20</sup> Aspects of ETMFs and NAV-Based Trading are protected intellectual property subject to issued and pending U.S. patents held by Navigate Fund Solutions LLC ("Navigate"), a wholly owned subsidiary of Eaton Vance Corp. Nasdaq would enter into a license agreement with Navigate to allow for NAV-Based Trading on

Exchange may trade pursuant to UTP on other national securities exchanges that have obtained appropriate licenses, adopted applicable exchange rules and developed systems to support NAV-Based Trading. Fees collected by the Exchange in connection with the listing and trading of ETMF Shares will comply with the statutory requirements set forth in the Act.

#### Trading Halts

The Exchange may consider all relevant factors in exercising its discretion to halt or suspend trading in ETMF Shares. Nasdaq will halt trading in ETMF Shares under the conditions specified in Nasdaq Rules 4120, as proposed to be amended, and in proposed Nasdaq Rule 5745(d)(2)(C), as discussed above. Additionally, Nasdaq may cease trading ETMF Shares if other unusual conditions or circumstances exist which, in the opinion of Nasdaq, make further dealings on Nasdaq detrimental to the maintenance of a fair and orderly market. To manage the risk of a non-regulatory ETMF Share trading halt, Nasdaq has in place back-up processes and procedures to ensure orderly trading. Because, in NAV-Based Trading, all trade execution prices are linked to end-of-day NAV, buyers and sellers of ETMF Shares should be less exposed to risk of loss due to intraday trading halts than buyers and sellers of conventional ETFs and other exchange-traded securities.

#### Trading Rules

Nasdaq deems ETMF Shares to be equity securities, thus rendering trading in ETMF Shares to be subject to Nasdaq's existing rules governing the trading of equity securities. Nasdaq will allow trading in ETMF Shares from 9:30 a.m. until 4:00 p.m.

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the Exchange of ETMFs that have themselves entered into license agreements with Navigate.



Eastern Time.<sup>21</sup> As provided in proposed Nasdaq Rule 5745(b)(3), the minimum price variation for quoting and entry of orders in ETMF Shares traded on the Exchange will be \$0.01.

### Surveillance

The Exchange represents that trading in ETMF Shares will be subject to the existing trading surveillances, administered by both Nasdaq and the Financial Industry Regulatory Authority, Inc. (“FINRA”) on behalf of the Exchange, which are designed to detect violations of Exchange rules and applicable federal securities laws.<sup>22</sup> The Exchange represents that these procedures are adequate to properly monitor trading of ETMF Shares on the Exchange and to deter and detect violations of Exchange rules and applicable federal securities laws.

The surveillances referred to above generally focus on detecting securities trading outside their normal patterns, which could be indicative of manipulative or other violative activity. When such situations are detected, surveillance analysis follows and investigations are opened, where appropriate, to review the behavior of all relevant parties for all relevant trading violations.

FINRA, on behalf of the Exchange, will communicate as needed with other markets and other entities that are members of the Intermarket Surveillance Group (“ISG”)<sup>23</sup> regarding trading in ETMF Shares, and in exchange-traded securities and

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<sup>21</sup> See, supra note 6.

<sup>22</sup> FINRA provides surveillance of trading on the Exchange pursuant to a regulatory services agreement. The Exchange is responsible for FINRA’s performance under this regulatory services agreement.

<sup>23</sup> For a list of the current members of ISG, *see* [www.isgportal.org](http://www.isgportal.org). The Exchange notes that not all components of an ETMF’s portfolio may trade on markets that

instruments held by ETMFs, and FINRA may obtain trading information regarding such trading from other markets and other entities. In addition, the Exchange may obtain information regarding trading in ETMF Shares, and in exchange-traded securities and instruments held by ETMFs, from markets and other entities that are members of ISG, which includes securities and futures exchanges, or with which the Exchange has in place a comprehensive surveillance sharing agreement.

In addition, the Exchange also has a general policy prohibiting the distribution of material non-public information by its employees.

#### Information Circular

Prior to the commencement of trading in an ETMF, the Exchange will inform its members in an Information Circular of the special characteristics and risks associated with trading the ETMF Shares. Specifically, the Information Circular will discuss the following: (1) the procedures for purchases and redemptions of ETMF Shares in Creation Units (and noting that ETMF Shares are not individually redeemable); (2) Nasdaq Rule 2111A, which imposes suitability obligations on Nasdaq members with respect to recommending transactions in ETMF Shares to customers; (3) how information regarding the IIV is disseminated; (4) the requirement that members deliver a prospectus to investors purchasing ETMF Shares prior to or concurrently with the confirmation of a transaction; and (5) information regarding NAV-Based Trading protocols.

In addition, the Information Circular will advise members, prior to the commencement of trading, of the prospectus delivery requirements applicable to the ETMF. Members purchasing ETMF Shares from the ETMF for resale to investors will

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are members of ISG or with which the Exchange has in place a comprehensive surveillance sharing agreement.

deliver a summary prospectus to such investors. The Information Circular will also discuss any exemptive, no-action and interpretive relief granted by the Commission from any rules under the Act.

The Information Circular also will reference that the ETMF is subject to various fees and expenses described in its registration statement. The Information Circular will also disclose the trading hours of the ETMF Shares and the applicable NAV calculation time for the ETMF Shares. The Information Circular will disclose that information about the ETMF Shares will be publicly available on the ETMF's website.

Information regarding ETMF trading protocols will be disseminated to Nasdaq members in accordance with current processes for newly listed products. Nasdaq intends to provide its members with a detailed explanation of NAV-Based Trading through a Trading Alert issued prior to the commencement of trading in ETMF Shares on the Exchange.

## 2. Statutory Basis

Nasdaq believes that the proposal is consistent with Section 6(b) of the Act<sup>24</sup> in general, and Section 6(b)(5) of the Act<sup>25</sup> in particular, in that it is designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in facilitating transactions in securities, and to remove impediments to and perfect the mechanism of a free and open market and a national market system. Nasdaq also believes that imposition of an initial entry fee and an annual fee in connection with the listing of ETMF Shares

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<sup>24</sup> 15 U.S.C. 78f(b).

<sup>25</sup> 15 U.S.C. 78f(b)(5).

under proposed Nasdaq Rule 5940 is consistent with Section 6(b)(4) of the Act<sup>26</sup> in that it provides for the equitable allocation of reasonable dues, fees and other charges among members and issuers and other persons using any facility or system that the Exchange operates or controls.

The Exchange believes that the proposed rule change is designed to prevent fraudulent and manipulative acts and practices in that ETMF Shares would be listed and traded on the Exchange pursuant to the initial and continued listing criteria in proposed Nasdaq Rule 5745. The Exchange believes that its surveillance procedures are adequate to properly monitor the trading of ETMF Shares on Nasdaq and to deter and detect violations of Exchange rules and the applicable federal securities laws. If the investment adviser to an ETMF is a registered broker-dealer or affiliated with a broker-dealer, such investment adviser shall erect a “fire wall” between the investment adviser and the broker-dealer personnel or broker-dealer affiliate, as applicable, with respect to access to information concerning the composition and/or changes to the ETMF’s portfolio holdings. The Exchange may obtain information via ISG from other exchanges that are members of ISG or with which the Exchange has entered into a comprehensive surveillance sharing agreement, to the extent necessary.

The proposed rule change is designed to promote just and equitable principles of trade and to protect investors and the public interest. The Exchange will obtain a representation from each issuer of ETMF Shares that the NAV per ETMF Share will be calculated on each business day that the New York Stock Exchange is open for trading and that the NAV will be made available to all market participants at the same time. In

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<sup>26</sup> 15 U.S.C. 78f(b)(4).

addition, a large amount of information would be publicly available regarding ETMFs and ETMF Shares, thereby promoting market transparency. An IIV will be disseminated by one or more major market data vendors at intervals of not more than 15 minutes during trading on the Exchange. Prior to the commencement of market trading in ETMF Shares, each ETMF will be required to establish and maintain a public website through which its current prospectus may be downloaded. The website will include additional ETMF information updated on a daily basis, including the most recent NAV. The Composition File will be disseminated through the NSCC before the open of trading in ETMF Shares on each business day. A complete list of current ETMF portfolio positions will be made available at least once each calendar quarter, with a reporting lag of not more than 60 days. ETMFs may provide more frequent disclosures of portfolio positions at their discretion.

Transactions in ETMF Shares will be reported to the Consolidated Tape, disseminated to member firms and market data services through the Nasdaq Data Feed used to report ETMF Share trades, and reported to the member firms participating in the trade contemporaneous with execution. Once an ETMF's daily NAV has been calculated and the final price of its intraday Share trades has been determined, Nasdaq disseminate final pricing information through the Nasdaq Data Feed used to report ETMF Share trades and deliver a confirmation with final pricing to the transacting parties. Information regarding NAV-based trading prices and volumes of ETMF Shares traded will be continually available on a real-time basis throughout each trading day on brokers' computer screens and other electronic services. The previous trading day's closing price and volume information for the ETMF Shares will be published daily. Because ETMF

Shares will trade at prices based on the next-determined NAV, investors will be able to buy and sell individual Shares at a known premium or discount to NAV that they can limit by transacting using limit orders. NAV-Based Trading provides a level of trading cost transparency and control that is normally not achievable in conventional ETF trading. Trading in ETMF Shares would be subject to proposed Nasdaq Rules 5745(d)(2)(B) and (C), which provide for the suspension of trading or trading halts under certain circumstances, including if, in the view of the Exchange, trading in ETMF Shares becomes inadvisable.

The proposed rule change is designed to perfect the mechanism of a free and open market and, in general, to protect investors and the public interest. Proposed Nasdaq Rule 5745 will permit the listing and trading of a new type of exchange-traded product that can provide investors with access to a broad range of active strategies in a structure that provides the cost and tax efficiencies and shareholder protections of ETFs, while removing the requirement for portfolio transparency to ensure a tight relationship between market trading prices and NAV. Because proposed Nasdaq Rule 5745 would not require ETMFs to publish portfolio positions daily, ETMFs are expected to have broad appeal among active managers who seek to make their strategies available in an exchange-traded structure, but have not embraced Active ETFs due to concerns about the adverse effects of publicly disclosing portfolio trading information on a daily basis.

For the above reasons, Nasdaq believes the proposed rule change is consistent with the requirements of Section 6(b)(5) of the Act.

With respect to the imposition of initial entry fees and annual fees for the listing of ETMF Shares under proposed Nasdaq Rule 5940, Nasdaq believes that the proposed

fees are reasonable and equitably allocated. Nasdaq notes that the proposed fees would be in the same amount as the entry fees and annual fees that apply to Portfolio Depository Receipts, Index Fund Shares and Managed Fund Shares, which, like ETMF Shares, are exchange-listed shares of investment companies registered under the 1940 Act.

Accordingly, Nasdaq believes the proposed rule change is consistent with the requirements of Section 6(b)(4) of the Act.

B. Self-Regulatory Organization's Statement on Burden on Competition

The Exchange does not believe that the proposed rule change will result in any burden on competition that is not necessary or appropriate in furtherance of the purposes of the Act. In fact, the Exchange believes that the introduction of ETMFs would promote competition. ETMFs would permit investment managers that have been unwilling to sponsor Active ETFs to introduce actively managed exchange-traded investment companies with features that could be attractive to investors. The Exchange believes that the NAV-Based Trading of ETMF Shares would provide investors with an ability to control trading costs in a way that is not normally available in conventional ETF trading. These developments could significantly enhance competition to the benefit of the markets and investors.

Nasdaq intends to enter into a license agreement to allow for the listing and trading of ETMF Shares.<sup>27</sup> ETMF Shares listed on the Exchange may trade pursuant to UTP on other national securities exchanges that have obtained appropriate licenses, adopted applicable exchange rules and developed systems to support NAV-Based Trading. Fees collected by the Exchange in connection with the listing and trading of

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<sup>27</sup> As noted above, aspects of ETMFs and NAV-Based Trading are protected intellectual property subject to issued and pending U.S. patents.

ETMF Shares will comply with the statutory requirements set forth in the Act. Nasdaq believes that this proposal would enable a unique investment product to begin trading in a regulated exchange environment and thereby provide additional trading choices to the benefit of investors, including retail investors.

C. Self-Regulatory Organization's Statement on Comments on the Proposed Rule Change Received from Members, Participants, or Others

Written comments were neither solicited nor received.

III. Date of Effectiveness of the Proposed Rule Change and Timing for Commission Action

Within 45 days of the date of publication of this notice in the Federal Register or within such longer period (i) as the Commission may designate up to 90 days of such date if it finds such longer period to be appropriate and publishes its reasons for so finding or (ii) as to which the Exchange consents, the Commission shall: (a) by order approve or disapprove such proposed rule change, or (b) institute proceedings to determine whether the proposed rule change should be disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic comments:

- Use the Commission's Internet comment form (<http://www.sec.gov/rules/sro.shtml>); or
- Send an e-mail to [rule-comments@sec.gov](mailto:rule-comments@sec.gov). Please include File Number SR-NASDAQ-2014-020 on the subject line.



Paper comments:

- Send paper comments in triplicate to Elizabeth M. Murphy, Secretary, Securities and Exchange Commission, Station Place, 100 F Street, NE, Washington, DC 20549-9303.

All submissions should refer to File Number SR-NASDAQ-2014-020. This file number should be included on the subject line if e-mail is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission's Internet website <http://www.sec.gov/rules/sro.shtml>.

Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission's Public Reference Room, 100 F Street, NE, Washington, DC 20549, on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of the filing also will be available for inspection and copying at the principal office of Nasdaq. All comments received will be posted without change; the Commission does not edit personal identifying information from submissions. You should submit only information that you wish to make available publicly.

All submissions should refer to File Number SR-NASDAQ-2014-xxx and should be submitted on or before [insert date 21 days from publication in the Federal Register].

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.<sup>28</sup>

Kevin M. O'Neill  
Deputy Secretary

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<sup>28</sup> 17 CFR 200.30-3(a)(12).

**EXHIBIT 5**

Proposed new language is underlined; proposed deletions are in brackets.

**4120. Limit Up-Limit Down Plan and Trading Halts**

(a)

(1) – (8) No Change

(9) may halt trading in a series of Portfolio Depository Receipts, Index Fund Shares or Managed Fund Shares (as defined in Rules 5705 and 5735, respectively), Index-Linked Exchangeable Notes, Equity Gold Shares, Trust Certificates, Commodity-Based Trust Shares, Currency Trust Shares, Commodity Index Trust Shares, Commodity Futures Trust Shares, Partnership Units, and Managed Trust Securities (as defined in Rule 5711(a) - (h) and (j), respectively), or ETMF Shares (as defined in Rule 5745) listed on Nasdaq if the Intraday Indicative Value (as defined in Rule 5705 for Portfolio Depository Receipts or Index Funds Shares, Rule 5711(a) for derivative securities defined in Rule 5711(a), (b), and (d) – (h), Rule 5711(j) for Managed Trust Securities, Rule 5735 for Managed Fund Shares, or Rule 5745 for ETMF Shares) or the index value applicable to that series is not being disseminated as required, during the day in which the interruption to the dissemination of the Intraday Indicative Value or the index value occurs. If the interruption to the dissemination of the Intraday Indicative Value or the index value persists past the trading day in which it occurred, Nasdaq will halt trading no later than the beginning of the trading day following the interruption. Nasdaq may also exercise discretion to halt trading in a series of Portfolio Depository Receipts, Index Fund Shares, [ or] Managed Fund Shares, Index-Linked Exchangeable Notes, Equity Gold Shares, Trust Certificates, Commodity-Based Trust Shares, Currency Trust Shares, Commodity Index Trust Shares, Commodity Futures Trust Shares, Partnership Units, Trust Units (as defined in Rule 5711(i), Managed Trust Securities, Currency Warrants (as defined in Rule 5711(k)), or ETMF Shares based on a consideration of the following factors: (A) trading in underlying securities comprising the index or portfolio applicable to that series has been halted in the primary market(s), (B) the extent to which trading has ceased in securities underlying the index or portfolio, or (C) the presence of other unusual conditions or circumstances detrimental to the maintenance of a fair and orderly market.

(10) shall halt trading in Derivative Securities Products (as defined in Rule 4120(b)(4)(A)) for which a net asset value ("NAV") (and in the case of Managed Fund Shares under Rule 5735, a Disclosed Portfolio, and in the case of ETMF Shares under Rule 5745, a Composition File) is disseminated if Nasdaq becomes aware that the NAV (or in the case of Managed Fund Shares, the Disclosed Portfolio, or in the case of ETMF Shares, the Composition File) is not being disseminated to all market participants at the same time.

Nasdaq will maintain the trading halt until such time as Nasdaq becomes aware that the NAV (or in the case of Managed Fund Shares, the Disclosed Portfolio, or in the case of ETMF Shares, the Composition File, as applicable) is available to all market participants or, in the case of Derivative Securities Products traded on Nasdaq pursuant to unlisted trading privileges, until such time trading resumes in the listing market.

(11) – (12) No Change

(b) Trading Halts for Trading of Certain Derivative Securities Products on Nasdaq Pursuant to Unlisted Trading Privileges

(1) – (3) No Change

(4) Definitions. For purposes of this Rule:

(A) Derivative Securities Product means a series of Portfolio Depository Receipts, Index Fund Shares, Managed Fund Shares, ETMF Shares, or Trust Issued Receipts (as defined in Rules 5705, 5735, 5745, and 5720, respectively), a series of Commodity-Related Securities (as defined in Rule 4630), securities representing interests in unit investment trusts or investment companies, Index-Linked Exchangeable Notes, Equity Gold Shares, Trust Certificates, Commodity-Based Trust Shares, Currency Trust Shares, Commodity Index Trust Shares, Commodity Futures Trust Shares, Partnership Units, Trust Units, Managed Trust Securities, or Currency Warrants (as defined in Rule 5711(a) - (k)), or any other UTP Derivative Security (as defined in Rule 5740).

(B) – (D) No Change

(E) Required Value shall mean (i) the value of any index or any commodity-related value underlying a Derivative Securities Product, (ii) the indicative optimized portfolio value, intraday indicative value, or other comparable estimate of the value of a share of a Derivative Securities Product updated regularly during the trading day, (iii) a net asset value in the case of a Derivative Securities Product for which a net asset value is disseminated, and (iv) a [d]Disclosed [p]Portfolio in the case of a Derivative Securities Product that is a series of [m]Managed [f]Fund [s]Shares, as defined in Rule 5735, or Managed Trust Securities, as defined in Rule 5711(j), [actively managed exchange-traded funds for which a disclosed portfolio is disseminated] and a Composition File in the case of a Derivative Securities Product that is a series of ETMF Shares, as defined in Rule 5745.

(c) No Change

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**5615. Exemptions from Certain Corporate Governance Requirements**

(a)

(1) – (4) No change

**(5) Management Investment Companies**

Management investment companies (including business development companies) are subject to all the requirements of the Rule 5600 Series, except that management investment companies registered under the Investment Company Act of 1940 are exempt from the Independent Directors requirement, the Compensation Committee requirement, the Independent Director Oversight of Director Nominations requirement, and the Code of Conduct requirement, set forth in Rules 5605(b), (d) and (e) and 5610, respectively. In addition, management investment companies that issue [are ]Index Fund Shares, [and ]Managed Fund Shares, and Exchange-Traded Managed Fund Shares, as defined in Rules 5705(b), [and ]5735, and 5745, are exempt from the Audit Committee requirements set forth in Rule 5605(c), except for the applicable requirements of SEC Rule 10A-3.

***IM-5615-4. Management Investment Companies***

*Management investment companies registered under the Investment Company Act of 1940 are already subject to a pervasive system of federal regulation in certain areas of corporate governance covered by 5600. In light of this, Nasdaq exempts from Rules 5605(b), (d), (e) and 5610 management investment companies registered under the Investment Company Act of 1940. Business development companies, which are a type of closed-end management investment company defined in Section 2(a)(48) of the Investment Company Act of 1940 that are not registered under that Act, are required to comply with all of the provisions of the Rule 5600 Series. Management investment companies that issue [are ]Index Fund Shares, [and ]Managed Fund Shares, and Exchange-Traded Managed Fund Shares are exempt from the Audit Committee requirements set forth in Rule 5605(c), except for the applicable requirements of SEC Rule 10A-3.*

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**5745. Exchange-Traded Managed Fund Shares (“ETMF Shares”)**

(a) Nasdaq will consider listing ETMF Shares that meet the criteria of Rule 5745.

(b) Applicability. Rule 5745 is applicable only to ETMF Shares. Except to the extent inconsistent with Rule 5745, or unless the context otherwise requires, the rules and procedures of the Board of Directors shall be applicable to the trading on Nasdaq of such

securities. ETMF Shares are included within the definition of “security” or “securities” as such terms are used in the Rules of Nasdaq.

(1) Nasdaq will file separate proposals under Section 19(b) of the Act before the listing of ETMF Shares.

(2) Transactions in ETMF Shares will occur during the Regular Market Session through 4:00 p.m.

(3) NAV-Based Trading. ETMF Shares will trade on Nasdaq at market-determined premiums or discounts to the ETMF’s next-determined net asset value per share. All bids, offers and execution prices will be expressed as a premium/discount (which may be zero) to the next-determined net asset value per share (“NAV-Based Trading”). The minimum price variation for quoting and entry of orders in ETMF Shares is \$0.01. Trade executions will be binding at the time that orders are matched, with the transaction price contingent upon the next-determined net asset value per share. After the Reporting Authority calculates the net asset value, Nasdaq will price each transaction at the agreed premium or discount to net asset value and deliver the trading data for clearance and settlement.

(4) Surveillance Procedures. Nasdaq will implement written surveillance procedures for ETMF Shares.

(5) Creation and Redemption. For ETMF Shares based on an international or global portfolio, the statutory prospectus or the application for exemption from provisions of the Investment Company Act of 1940 for the series of ETMF Shares must state that such series must comply with the federal securities laws in accepting securities for deposits and satisfying redemptions with securities, including that the securities accepted for deposits and the securities used to satisfy redemption requests are sold in transactions that would be exempt from registration under the Securities Act of 1933.

(c) Definitions. The following terms as used in the Rules shall, unless the context otherwise requires, have the meanings herein specified:

(1) ETMF Share. The term “ETMF Share” means a security that (a) represents an interest in a registered investment company (“ETMF”) organized as an open-end management investment company that invests in a portfolio of securities and other assets selected and managed by the ETMF’s investment adviser consistent with the ETMF’s investment objectives and policies; (b) is issued in a specified aggregate unit quantity in return for a deposit of a specified portfolio of securities and/or a cash amount with a value per ETMF Share equal to the ETMF’s net asset value; (c) when aggregated in the same specified unit quantity, may be redeemed for a specified portfolio of securities and/or cash with a value per ETMF Share equal to the ETMF’s net asset value; and (d) is traded on Nasdaq using NAV-Based Trading.

(2) Intraday Indicative Value. The term “Intraday Indicative Value” is the estimated indicative value of an ETMF Share based on current information regarding the value of the securities and other assets held by the ETMF.

(3) Composition File. The term “Composition File” means the specified portfolio of securities and/or cash that an ETMF will accept as a deposit in issuing ETMF Shares, and the specified portfolio of securities and/or cash that an ETMF will deliver in a redemption of ETMF Shares. The Composition File will be disseminated through the National Securities Clearing Corporation once each business day before the open of trading in ETMF Shares on Nasdaq on such day. To maintain the confidentiality of current portfolio trading, an ETMF’s Composition File generally will not be a pro rata reflection of the ETMF’s securities positions. Each security included in the Composition File will be a current holding of the ETMF, but the Composition File generally will not include all of the securities in the ETMF’s portfolio or match the weightings of the included securities in the portfolio. The Composition File also may consist entirely of cash, in which case it will not include any of the securities in the ETMF’s portfolio.

(4) Reporting Authority. The term “Reporting Authority” in respect of a particular series of ETMF Shares means Nasdaq, an institution, or a reporting service designated by Nasdaq as the official source for calculating and reporting information relating to such series of ETMF Shares, including, but not limited to, the Intraday Indicative Value, the amount of any cash distribution to holders of ETMF Shares, net asset value per share, and the Composition File or other information relating to the issuance, redemption or trading of ETMF Shares. A series of ETMF Shares may have more than one Reporting Authority, each having different functions.

(d) Initial and Continued Listing — ETMF Shares will be listed and traded on Nasdaq subject to application of the following criteria:

(1) Initial Listing — Each series of ETMF Shares will be listed and traded on Nasdaq subject to application of the following initial listing criteria:

(A) For each series, Nasdaq will establish a minimum number of ETMF Shares required to be outstanding at the time of commencement of trading on Nasdaq.

(B) Nasdaq will obtain a representation from the issuer of each series of ETMF Shares that the net asset value per share for the series will be calculated on each business day that the New York Stock Exchange is open for trading and that the net asset value per share will be made available to all market participants at the same time.

(C) The Reporting Authority that provides the Composition File must implement and maintain, or be subject to, procedures designed to prevent

the use and dissemination of material non-public information regarding the ETMF's portfolio positions and changes in the positions.

(2) Continued Listing — Each series of ETMF Shares will be listed and traded on Nasdaq subject to application of the following continued listing criteria:

(A) Intraday Indicative Value. The Intraday Indicative Value for the ETMF Shares will be widely disseminated by one or more major market data vendors at intervals of not more than 15 minutes during the Regular Market Session when the ETMF Shares trade on Nasdaq.

(B) Suspension of trading or removal. Nasdaq will consider the suspension of trading in or removal from listing of a series of ETMF Shares under any of the following circumstances:

(i) if, following the initial twelve-month period after commencement of trading on Nasdaq of a series of ETMF Shares, there are fewer than 50 beneficial holders of the series of ETMF Shares for 30 or more consecutive trading days;

(ii) if the value of the Intraday Indicative Value or the net asset value is no longer calculated, or if the Intraday Indicative Value, net asset value or Composition File is no longer available to all market participants at the same time;

(iii) if the ETMF issuing the ETMF Shares has failed to file any filings required by the Commission or if Nasdaq is aware that the ETMF is not in compliance with the conditions of any exemptive order or no-action relief granted by the Commission with respect to the series of ETMF Shares; or

(iv) if such other event shall occur or condition exists which, in the opinion of Nasdaq, makes further dealings on Nasdaq inadvisable.

(C) Trading Halt. If the Intraday Indicative Value of a series of ETMF Shares is not being disseminated as required, Nasdaq may halt trading during the day in which the interruption to the dissemination of the Intraday Indicative Value occurs. If the interruption to the dissemination of the Intraday Indicative Value persists past the trading day in which it first occurred, Nasdaq will halt trading no later than the beginning of the trading day following the interruption. In addition, if Nasdaq becomes aware that the net asset value per share with respect to a series of ETMF Shares is not calculated on each business day that the New York Stock Exchange is open for trading and disseminated to all market participants at the same time, it will halt trading in such series until such time as the net asset value per share is available to all market participants. In addition, if Nasdaq becomes aware that the Composition File with respect to a series of ETMF Shares is not disseminated to all market participants at the same



time, it will halt trading in such series until such time as the Composition File is available to all market participants.

(D) Termination. Upon termination of an ETMF, Nasdaq requires that ETMF Shares issued in connection with such entity be removed from listing on Nasdaq.

(E) Voting. Voting rights shall be as set forth in the applicable ETMF prospectus.

(e) Limitation of Liability. Neither Nasdaq, the Reporting Authority, nor any agent of Nasdaq shall have any liability for damages, claims, losses or expenses caused by any errors, omissions or delays in calculating or disseminating any current portfolio value; the current value of the securities and other assets required to be deposited in connection with issuance of ETMF Shares; the amount of any dividend equivalent payment or cash distribution to holders of ETMF Shares; net asset value per share; the Composition File; or other information relating to the purchase, redemption or trading of ETMF Shares, resulting from any negligent act or omission by Nasdaq, the Reporting Authority or any agent of Nasdaq, or any act, condition or cause beyond the reasonable control of Nasdaq, its agent or the Reporting Authority, including, but not limited to, an act of God, fire, flood, extraordinary weather conditions, war, insurrection, riot, strike, accident, action of government, communications or power failure, equipment or software malfunction, or any error, omission, or delay in the reports of transactions in one or more underlying securities.

(f) Disclosures. The provisions of this subparagraph apply only to series of ETMF Shares that are the subject of an order by the Securities and Exchange Commission exempting such series from certain prospectus delivery requirements under Section 24(d) of the Investment Company Act of 1940 and are not otherwise subject to prospectus delivery requirements under the Securities Act of 1933. Nasdaq will inform its members regarding application of the provisions of this subparagraph to a particular series of ETMF Shares by means of an information circular prior to commencement of trading in such series.

Nasdaq requires that members provide to all purchasers of a series of ETMF Shares a written description of the terms and characteristics of those securities, in a form prepared by the open-end management investment company issuing such securities, not later than the time a confirmation of the first transaction in such series is delivered to such purchaser. In addition, members shall include such a written description with any sales material relating to a series of ETMF Shares that is provided to customers or the public. Any other written materials provided by a member to customers or the public making specific reference to a series of ETMF Shares as an investment vehicle must include a statement in substantially the following form: "A circular describing the terms and characteristics of (the series of ETMF Shares) has been prepared by the (open-end management investment company name) and is available from your broker. It is recommended that you obtain and review such circular before purchasing (the series of ETMF Shares)."

A member carrying an omnibus account for a non-member broker-dealer is required to inform such non-member that execution of an order to purchase a series of ETMF Shares for such omnibus account will be deemed to constitute agreement by the non-member to make such a written description available to its customers on the same terms as are directly applicable to members under this rule.

Upon request of a customer, a member shall also provide a prospectus for the particular series of ETMF Shares.

(g) If the investment adviser to an ETMF issuing ETMF Shares is a registered broker-dealer or is affiliated with a broker-dealer, such investment adviser shall erect a “fire wall” between the investment adviser and the broker-dealer personnel or broker-dealer affiliate, as applicable, with respect to access to information concerning the composition and/or changes to such ETMF’s portfolio holdings. Personnel who make decisions on the ETMF’s portfolio composition must be subject to procedures designed to prevent the use and dissemination of material nonpublic information regarding the applicable ETMF portfolio.

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#### **5940. Exchange Traded Products**

##### **(a) Entry Fee**

(1) When a Company submits an application for listing a series of Portfolio Depository Receipts, Index Fund Shares, [ or] Managed Fund Shares, or ETMF Shares on the Nasdaq Global Market, it shall pay to Nasdaq a listing fee of \$5,000 (which shall include a \$1,000 non-refundable application fee).

(2) – (4) No Change

##### **(b) Annual Fee**

(1) The issuer of a series of Portfolio Depository Receipts, Index Fund Shares, [ or] Managed Fund Shares, or ETMF Shares listed on The Nasdaq Global Market shall pay to Nasdaq an annual fee calculated on total shares outstanding according to the following schedule:

Schedule – No Change

(2) – (3) No Change

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