Re: Request for Comment on Novel ETFs (File No. S7-2026-24)

Commissioners:

Please accept my feedback on the questions raised in this Request for Comment. I appreciate this opportunity to provide feedback and believe these types of questions are ripe to ask every few years.

-'40 Act Lawyer

1. Would a Novel ETF meet the Subjective Test by "hold[ing] itself out" as an "investment company," and/or as "engaged primarily, or propos[ing] to engage primarily, in the business of investing, reinvesting, or trading in securities," notwithstanding that its principal investment strategy is to invest in assets that may not be securities? Is there a need for greater clarity about this aspect of the Subjective Test? Why or why not?

   It is not clear what regulatory concern would justify preventing a company from electing to be regulated under the Investment Company Act of 1940. If a company voluntarily seeks to be subject to the Act's investor-protection framework, it is unclear why the Commission should restrict that choice.

   In my view, the more significant concern arises in circumstances where Investment Company Act registrants face fewer regulatory or disclosure obligations, or enjoy broader distribution channels, than '33 Act only funds. In addition, I believe the Investment Company Act should be revised so that any restriction applicable to investment securities applies uniformly to all investments held by an Investment Company Act fund.

   Further, all funds, whether regulated solely under the Securities Act of 1933 or under both the 1933 and 1940 Acts, should be required to file on the N Forms and follow the associated disclosure framework, subject to review by the Division of Investment Management. Investors generally do not understand the distinction between funds regulated under the 1940 Act and those that are not, nor should they be expected to do so.

2. Why would a Novel ETF with a principal investment strategy to invest in assets that are not securities seek to register as an investment company and be regulated as such (rather than as, for example, an exchange-traded commodity trust or some other type of ETP)?

   Investors generally do not understand the distinction between Investment Companies and funds regulated solely under the Securities Act of 1933. Historically, one of the key differences related to limits on leverage. Today, however, investors often turn to Investment Company Act funds precisely to

obtain leverage. For example, a spot bitcoin product is regulated only under the Securities Act, while a 2X product is registered under the Investment Company Act.

ETFs regulated solely under the Securities Act (spot ETPs) should not need to exist. They exist today only because this structure is the sole available means for investors to obtain exposure to crypto assets and commodities through a brokerage account. Investors should be able to hold any type of investment in a brokerage account, regardless of whether it is a security. The regulatory framework should make this process easy and convenient for investors. The only use case for spot ETPs is for physical commodities where investors cannot meaningfully take possession and store physical commodities such as oil or gold bars.

3. When evaluating whether a Novel ETF meets the Subjective Test, should the Commission continue to apply the Tonopah Factors? Are there different or additional factors the Commission should consider or emphasize in its analysis of a Novel ETF? Why or why not?

I would add an explicit marketing test to the Toponah factors.

Significant deference should be given to companies in assessing these factors. The staff should not be the arbiter; it is the registrant that is on the hook, it should be their determination to make.

4. Would a Novel ETF that holds on an unconsolidated basis "securities" (i.e., shares or other equity interests) issued by one or more wholly-owned subsidiaries that are not themselves primarily invested in securities meet the Subjective Test, notwithstanding that its principal investment strategy is to invest in assets that are not securities? Why or why not? Under what circumstances, if any, should the Commission consider investments in securities issued by wholly-owned subsidiaries (or by other subsidiaries generally consolidated with the issuer) to comprise part of a securities investment business under the Subjective Test? Should the analysis differ for holding companies that are engaged in various operating businesses through wholly-owned and majority-owned subsidiaries? Why or why not?

The standard should look through any structural or organizational contrivances. The Commission should also work with the Internal Revenue Service to eliminate the tax-driven need for such structures. If a fund must hold commodities or derivatives through a controlled foreign corporation in order to maintain favorable tax treatment, the IRS should allow that treatment without requiring the use of a CFC. This would create efficiencies and improve transparency for investors.

5. Do the assets and strategies of Novel ETFs present any questions regarding: a) the functioning of the ETF arbitrage mechanism and related secondary trading activity that supports it; b) investor protection; c) the maintenance of fair, orderly, and efficient markets, as well as any unique challenges to market surveillance necessary to support the ETF's listing; or d) other structural or operational issues? Why or why not?

Do not allow companies that invest > 15% of assets in Pre-IPO companies to launch until 3 days after the IPO when markets settle.

Limit leverage to 2X for open end funds.

Do not allow investments in prediction market ETFs, particularly those with an all-of-nothing payout. This is, in essence, an extreme form of leverage.

It also seems that crypto and other novel ETFs are frequently subject to trading halts. This suggests they are not ripe for trading. See https://www.cboe.com/markets/us/equities/notices/halts.

6. Should rule 6c-11 be amended to address these or other questions with respect to Novel ETFs? For instance, should the Commission consider amendments addressing new portfolio requirements, such as minimum holdings in securities, restrictions from using certain strategies or investing in certain asset classes, or criteria such as specific diversification requirements, concentration limits, or issuer-specific limits? Why or why not? Or should the rule be amended to exclude certain assets or investment strategies? Why or why not?

Limit leverage to two times for all open-end funds. Any such requirement should apply uniformly to both mutual funds and ETFs. To accomplish this, the Commission should include an explicit two-times leverage limit, in addition to the 200 percent VAR test, in rules 18f-2, 18f-3, 18f-4, and 6c-11, ensuring that all funds are covered. Derivatives also should not be permitted to be included in the designated reference portfolio.

Investments in prediction-market ETFs should not be permitted, particularly those with all-or-nothing payout structures, because these instruments function as an extreme form of leverage. Such products could be addressed by requiring the use of the Absolute VAR test, as no appropriate reference portfolio exists.

Significant exposure to crypto assets and commodities likewise should not be permitted within an ETF structure, although I acknowledge that it may be too late to reverse the current trajectory. Significant exposure to

non-securities should also not be permitted in an ETF wrapper, or at a minimum, should not be permitted automatically through rule 6c-11.

I appreciate it may be hard to put the cork in the bottle, but these funds are still a small minority of funds and assets, so now is the time. There should be no grandfathering.

7. Should the Commission consider any steps to help investors better understand the features of Novel ETFs? Are there steps the Commission could consider to help investors understand what distinguishes Novel ETFs from other ETFs?

Some ETFs, such as leveraged ETFs and defined outcome funds, require enhanced disclosures, including more timely website updates. The rules should be revised to mandate such disclosures where appropriate.

In addition, the summary prospectus for ETFs should briefly describe what information is available on the fund's website—such as premiums and discounts and daily holdings—and should include a direct link to the specific webpage where that information can be found.

8. Some ETPs that are not investment companies (e.g., exchange-traded commodity trusts) may use the term "ETF" (or "fund") in their name or label themselves as ETFs. How do investors interpret this, and are there any implications for investor clarity?

Investors do not know what the Investment Company Act is or what it does. So there is little chance of investor confusion.

I have not seen evidence that the spot crypto and commodity ETPs are less safe than '40 Act ETFs.

I do believe that all ETPs should file on Form N-1A and use the N-1A filing framework (e.g., rules 24f-2, 485, 497, 482, 156, etc.).

9. Amendments to rule 6c-11 (such as new portfolio conditions) could affect how the generic listing standards apply to a Novel ETF. Should this interplay between rule 6c-11 and the generic listing standards inform any analysis of potential changes to the rule? Are there other ways in which rule 6c-11 could be amended or other Commission action taken to better facilitate innovation while protecting investors, maintaining fair, orderly, and efficient markets, and facilitating capital formation?

Limit leverage to 2X for <u>all</u> open-end funds (including mutual funds).

Do not allow investments in prediction market ETFs, particularly those with an all-of-nothing payouts. This is, in essence, an extreme form of leverage.

10. Certain post-effective amendments filed under rule 485, including those for certain Novel ETFs, may raise issues that may be challenging to address within the rule's currently prescribed timeframes. Should the 75-day and 60-day automatic effectiveness periods be extended for Novel ETFs? If yes, for how long? If not, why not?

    75 days reems reasonable. While novel ETFs raise significant issues, there are not that many unique novel ETFs. For example, with the 3x, 4x and 5x funds, there were 400+ funds, but they all raised the same issue. The same goes for crypto ETF and prediction market ETFs. The disclosure staff will fill any amount of time you give them.

11. Should effectiveness be automatically tolled for a Novel ETF if a registrant fails to respond to staff comments within a specified period (e.g., five business days) before effectiveness? Why or why not?

    No.

    There is no legal requirement to respond to comments.

    The staff often provides comments late, particularly since their reduced staff and the 2025 government shutdown.

12. While registrants may voluntarily delay effectiveness under rule 485, should the rule be amended to enable the Commission to delay effectiveness of a Novel ETF on its own initiative? If yes, how should the amended rule be structured, under what circumstances should the Commission be able to delay effectiveness, and what if any limits or notice requirements should apply?

    This seems appropriate. However:

    - **The SEC must ensure that all similarly situated funds are treated consistently.**
    - **The SEC must also preserve any legitimate first-mover advantage, recognizing that some registrants may be able to resolve issues more quickly than others.**
    - **Notice should be provided at least two business days prior to effectiveness.**
    - **Any such action should be taken publicly.**
    - **A delay should be permitted to apply only to certain funds within a multi-fund filing, where appropriate.**

13. Some market participants have raised questions about Novel ETFs seeking to become effective before an asset class or instrument is available for investment. Is additional clarity needed regarding rule 485(a) with respect to a Novel ETF becoming effective before its investment strategy can be implemented? Why or why not?

This issue is difficult, although I agree with the general principle that funds should not be launched before the underlying asset is readily available. Traditionally, funds are given time to ramp up their portfolios before they must comply with their investment policies. For example, the Names Rule provides funds with 180 days to come into compliance.

A fund cannot make misleading statements regarding its strategy. It must be clear about whether, and how, it is obtaining exposure before the underlying instrument becomes available. In some cases, such as with pre-IPO companies, exposure may be obtained through alternative means, including swaps tied to perpetual futures.

It is also important to distinguish between a registration statement becoming effective and a fund actually launching or listing. Effectiveness does not necessarily mean that the fund is trading. Moreover, ETFs must go effective prior to launch in order to complete exchange-listing requirements and to engage authorized participants and market makers.

14. If the automatic effectiveness periods were extended, would registrants experience unnecessary delays in responding to market demand?

There should be little concern so long as the timetables are clearly layed out and applied fairly.

15. Should the Commission consider mechanisms for early engagement for Novel ETFs (e.g., a pre-filing consultation process or confidential draft registration statements) that would allow the staff and sponsors of Novel ETFs to work together on potential issues before the sponsor makes a public filing? If so, should we publicly report on these consultations to provide for a measure of accountability in the process? For example, should we report how many such consultations occur, how long they take, and how many result in public filings?

Early engagement is not helpful as it does not hold a registrant's place in line. In addition, the staff (both the Disclosure Office and Chief Counsel's Office) does not move with any urgency until it has a live filing. That is one redeeming quality of rule 485(a), it forces the staff to move with urgency.

The few times I tried to engage with the staff on a prefiling basis, they said they needed to see the level of detail that would be in a live filing before discussing potential issues (and they will not look at draft filings).

Draft registration statements might help for closed-end funds, but are less helpful for filings relying on rule 485(a). Instead, 485(a) filings for new series should also have the option of being filed confidentially for some period of time as the 485(a) clock runs. Confidentiality is less necessary for open and running funds as funds typically give 60 days notice before making significant changes (thanks to Rule 35d-1).

16. Are there other ways rule 485(a) could be modified to better support innovation, while protecting investors, maintaining fair, orderly, and efficient markets, and facilitating capital formation?

One question to consider is whether the disclosure review program remains necessary. Although it occasionally identifies significant issues that counsel may have overlooked, most comments are minor. Given that the disclosure requirements are well established and the industry has more than eighty-five years of experience with the statute, it is worth asking whether disclosure reviews for filings that become effective automatically are still needed.

The staff should also more liberally permit template filing relief (under rule 485(b)(1)(vii)). For example, in the case of single-stock funds (including two-times, short, covered-call, and auto-callable structures), once the staff has reviewed the initial filing, a rule 485(a) filing should not be required for subsequent funds using different reference assets, provided those assets are U.S.-listed stocks or ETFs.

17. Do market participants have concerns about competitive pressures that may incentivize sponsors to submit filings for Novel ETFs quickly and in rapid succession? If so, could such competitive pressures result in rushed or incomplete filings or the filing of many ETFs that never launch? Could such competitive pressures cause sponsors to attempt to repurpose unused series to take advantage of shorter waiting periods resulting in an unfair treatment of funds? Should we amend rule 485 to specifically address these concerns? Why or why not? For example, should the Commission amend its rules to require upfront payment of a minimum registration fee that may be subsequently offset by redemptions under rule 24f-2?

Yes. This is a significant problem. At present, there is no effective mechanism to innovate and maintain a first-mover advantage. With the rise of AI, competing products can be copied and filed with extraordinary speed. I suggest the following:

- **Require filings to be complete, and frequently suspend the effectiveness of filings that are not complete. (It seems curious that the staff seems willing to do this with N-14s under rule 488, but not under rule 485.) This should include situations in which filers attempt to obscure their "secret sauce." For example, several 3x, 4x, and 5x ETFs represented that they used swaps to obtain 3x, 4x, and 5x exposure on both the upside and downside. I understand that no fund intended to operate in this manner because doing so would plainly violate rules 18f-4 and 6c-11. Rather, they sought to avoid revealing their true plans to competitors, such as using prepaid options. This undermines the purpose of public filings and weakens the review process.**
- **Make clear that all repurposed funds—whether pre-effectiveness, pre-launch, or even post-launch if held only by affiliates—require a new 75-day filing, and that rule 497 is not available for such changes. An alternative approach is to require 75 days for all 485(a) filings.**
- **If a fund abuses the filing process, amend rule 485 to allow the Commission to remove that filer from rule 485 eligibility and require reliance on section 8(c), including the submission of a POS 8C filing that must be accelerated. This tool should be used liberally.**
- **Keep all rule 485(a) filings non-public for 30 days after filing, except for those requiring acceleration.**
- **Publicly call out bad actors and team up with the exchanges to hold up bad actors.**

Requiring an up-front filing fee does not address the underlying issue if filers can simply offset that fee against their other filing fees.

18. Should the Commission allow rule 485(a)(2) filings to remain nonpublic for part of the 75-day period to promote innovation and reduce imitative filings? Why or why not? If yes, for how long?

Yes! In addition, you must maintain the line and not just the order, but also the timing. If the first filing is being asked to BXT such that the second filer can catch up to the first, you are not solving the problem. Treat everybody fairly and maintain the queue (and it timing.. if a fund has a 2 week lead, it should keep the 2 week lead so long as it is timely in its responses to staff comments).

Perhaps you need a novel ETF taskforce comprised of your disclosure, chief counsel and analytics office to more quickly rundown the issues with these novel funds so they can be resolved in 75 days.

19. To encourage filing only fully developed new series, should rule 485(a) require a fund's board or authorized signatories specifically to identify each new series included in the filing? Why or why not?

This is an interesting idea. However. this will give larger turnkey shops whose boards are nearly full-time employees a leg up over other funds whose board meet quarterly.

Funds are clever. You may just see funds include a laundry list of plausible funds, such at for every crypto, singly stock, ETF plausible all filed as an appendix. If you develop new filing rules, bring together a group of clever folks and see how they can test and bend the rules. This applies to filings rules, as well as 18f-4 and 6c-11. The industry can be quite clever… particularly during a pro-business administration.

20. Certain ETFs may be able to allocate assets to markets or strategies before newly registering funds pursue similar exposures, due to the discretion they have sought to retain over their investment practices. How should the Commission balance permitting investment flexibility with the need to preserve a fair and orderly registration process and to ensure investors are protected?

I do not have a solution for this other than to require an up-and-running fund to be subject to a 75 day review period just as new funds are (or move new funds to a 60 day clock).

This also does not work for changes made by rule 497.

I assume this question is aimed at the SpaceX launch how one up-and-running ETF jumped the line. The good news is this does not happen that often and to drastically changing a strategy on investors raises fiduciary duty questions.

21. Should the Commission take action with respect to funds that become effective but never launch? For example, should the Commission amend its rules to provide that such funds would be automatically deregistered after a defined period (e.g., 6 months)? Why or why not?

If repurposed funds are required to wait 75 days (as I suggest above), then what is the concern here? I suppose deregistering after 2 years of inactivity would help clean up the record. Six months is too short as sponsors may be waiting for a market upturn, for volatility to pass, or for an asset class to become available.

22. Should the Commission develop additional mechanisms to address unresolved staff comments? For instance, should funds be required to disclose material unresolved staff comments, similar to the approach used for certain closed-end funds and Form 10-K and Form 20-F filers? Would such disclosure be useful to investors and other market participants? Why or why not?

This could be helpful. However, this should not go in the summary prospectus and tailored shareholder report, particularly for more complex issues.

There would need to be a mechanism to determine which comments qualify as unresolved. I assume funds could also disclose their rebuttal.

23. Is there a need for greater clarity about how our rules apply when a material investment strategy change is made for a Novel ETF during the review process or before launch? Should rule 485 be amended to explicitly require a new 75-day or 60-day rule 485(a) filing for changes that are not made in response to staff comments?

A material change should trigger a new 75-day period. This is the only way to ensure a fair and transparent process. At present, material changes are communicated only to the staff through correspondence and do not become public until they appear in a rule 485(b) filing. That approach is inadequate. Material changes must be disclosed publicly and must be subject to the required waiting period.

24. Some registrants seek to make material changes to a Novel ETF's investment strategy after the effectiveness of the registration statement but before, at, or shortly after launch. For example, questions have arisen about material pre-launch changes made to a Novel ETF through a rule 497 filing rather than by a rule 485(a) amendment. Is additional clarity needed about rules 485 or 497 in light of these questions? Alternatively, should rule 485 be amended to automatically suspend or delay the effectiveness of a registration statement for a Novel ETF when a material pre- or at-launch change occurs?

Material changes made before at or shortly after launch should require a 75 day reviewable 485(a) filing. The Commission should make this view clear to the industry. As I state above, if registrants do not comply, they should be kicked out of rule 485 and be required to file a POS 8C and seek acceleration.

25. Rule 485 allows the Commission to suspend a registrant's ability to file under rule 485(b) if it appears the registrant has not complied with the applicable conditions of the rule or

to suspend the effective date of a rule 485(a) filing that is materially incomplete or inaccurate. Should the Commission consider changes to this rule? For example, should the circumstances under which the Commission may suspend a post-effective amendment be expanded? Should the Commission have the authority to suspend the effectiveness of a specific post-effective amendment, or of a particular series within that amendment, after it has become effective? Should the Commission condition the use of rule 6c-11 on compliance with filing requirements, or reserve the ability to suspend the use of rule 482 advertisements?

If a fund abuses the filing process, amend rule 485 to allow the Commission to remove that filer from rule 485 eligibility and require reliance on section 8(c), including the submission of a POS 8C filing that must be accelerated. This tool should be used liberally.

The Commission should expand its suspension authority to apply regardless of whether a filing has already become effective, so long as the fund has not yet launched. If the staff believes that the disclosures are inaccurate, misleading, or non-compliant with the federal securities laws, the Commission should be able to act immediately. Non-compliance with he federal securities laws should preclude a filing from becoming effective (just like the staff would not accelerate a filing if there was a potential violation of the federal securities laws). The staff should not be required to wait until launch and then pursue enforcement action; it should be able to prevent violations before the fund comes to market.

Suspending the use of rule 482 for folks repurposing funds by 497 is interesting and may be worth considering. Depending on your E-delivery proposal says, I wonder if folks will need 482 or could just rely on rule 34b-1. So, be sure to consider that as well.

26. Should the Commission consider changes to the ETF disclosure regime because of questions that Novel ETFs may raise? Should the Commission consider heightened disclosure requirements for certain Novel ETFs?

Some ETFs, such as leveraged ETFs and defined outcome funds, require enhanced disclosures, including more timely website updates. The rules should be revised to mandate such disclosures where appropriate.

In addition, the summary prospectus for ETFs should briefly describe what information is available on the fund's website—such as premiums and

discounts and daily holdings—and should include a direct link to the specific webpage where that information can be found.

27. Are there additional reforms the Commission should consider to help facilitate innovation, while protecting investors, maintaining fair, orderly, and efficient markets, and facilitating capital formation?

The SEC should also revise Rule 6c-11 to require an undertaking that the registrant consents to registration statement liability under Section 11 of the Securities Act. Unlike mutual funds, ETF investors (other than authorized participants) are denied standing to sue issuers under Section 11 of the Securities Act for defective registration statements because they typically purchase shares on the secondary market rather than in initial offerings.

The Commission should consider updating its positions on concentration and diversification to reflect how funds operate in 2026 and how investors generally understand these concepts. It is unreasonable that an S&P 500 fund could be required to characterize itself as non-diversified, or that a Maryland municipal bond fund would not be viewed as concentrated. In addition, many funds have investment policies, such as concentration policies or Names Rule policies, that reference their underlying index. For example, if a fund concentrates to the extent that its reference index concentrates, it should be required to obtain shareholder approval to change its index, because the index is effectively embedded in the policy. Without such a requirement, a Drone Index ETF could change to a Cannabis Index ETF without shareholder approval, which would not be appropriate.

Disclosure:

- **As you state above, funds are using a lot of contrivances such as CFCs. Does this under-the-hood disclosure need to be in the summary section?**
- **The SEC is also requiring too much disclosure for tokenized funds. They are asking for tons of information in the summary section. This information is more ripe for the back of the prospectus or SAI. After all, there are risks to the conventional approach to recordkeeping and that approach isn't described to investors anywhere in the disclosure forms.**
- **The SEC also requires a ton of ETF specific disclosures. These may have been real risks 15 years ago, but I have not seen most of them ever realized. The staff should work with the industry to cut the risks. It is unnecessary and clogging up the risk disclosures and obscuring more relevant risks.**

Jurisdiction:

- **The SEC needs to take control of all derivatives tied to individual securities and groups of securities (such as indices). The SEC should not yield its authority to the CFTC. The CFTC is ill-equipped to handle securities products and you should avoid instances of regulatory arbitrage. If investors can get exposure to stocks (include pre-IPO companies) and indices on hyperliquid and trade 24x7, and it is outside the SEC's jurisdiction, the SEC may as well fold-up shop.**