



# **(ST-1) Handling of ETF Market Making Incentive Scheme**

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March 2024  
Tokyo Stock Exchange, Inc.  
Ver. 4.3

# Revision History

|        | Version | Revised Page(s) | Summary of Revisions  |
|--------|---------|-----------------|---|
| 2018/2 | 1.0     | -               |   |
| 2018/4 | 1.1     | P3              | Added footnote about effective date of application  |
|        |         | P7、28           | Added footnote about incentive  |
|        |         | P8              | Added note about Announcement   |
|        |         | P16             | Clarified wording about payment   |
|        |         | P17             | Added footnote that tier based on ADV during Jan. – Mar. 2018 is applied until Sep. 2018.   |
| 2018/6 | 1.2     | P3              | Added footnote about newly listed issue   |
|        |         | P7              | Added footnote about payment destination  |
|        |         | P8              | Added footnote about image file of logo   |
|        |         | P27             | Added footnote about newly listed issue, consumption tax and revenue stamp.   |
|        |         | P28             | Added note about total amount of incentive.<br>Added footnote about AUM trigger and grouping condition.   |
| 2019/3 | 2.0     | P12             | Added footnote about exemption from continuous quote obligation<br>“During black-out days, only in case of excessive increase of trading volume, exemption is examined.”  |
|        |         | P14             | Added footnote about cancellation of sign up.<br>“*If average of performance for given ETF in the last 6 months is less than 10%, in principle, sign up for that ETF is canceled. It takes 3months for such market maker to sign up again.” |
|        |         | P22             | Revised note about Acclimation Period<br>- Acclimation period is extended to March 2020<br>- Number of ETFs for Quoting(1) is reduced to <b>No less than 10</b> illiquid ETFs   |
|        |         | P23             | Added slide about Mail RFQ Service  |
| 2019/3 | 2.0     | P29             | Revised Note about sponsored scheme<br>- Lead time for application is reduced from 1month to 2weeks<br>- Multiple conditions on an ETF becomes available  |
|        |         | P31、32          | Added slides about matching funds   |
| 2019/9 | 2.1     | P31             | Revised target ETFs. Deleted P31.   |

# Revision History

|         | Version | Revised Page(s) | Summary of Revisions  |
|---------|---------|-----------------|---|
| 2019/10 | 2.2     | P31             | Added note about quoting time period  |
| 2020/3  | 2.3     | P22             | Extend acclimation period.  |
|         |         | P31             | Revised target ETFs in Ver.2.0 scheme.  |
| 2020/9  | 3.0     | P10             | Deleted Note about acclimation period<br>Revised Note about if obligation not fulfilled<br>- Market makers may be excluded from sign-up ETF or MM if obligation is not fulfilled for a certain period.  |
|         |         | P12             | Revised Note about number of ETFs for quoting<br>- The number of ETFs is changed from 3 patterns to “at least 5 ETFs” under this scheme   |
|         |         | P15             | Revised Note about if obligation not fulfilled<br>- If average performance is lower than 5% over the last 6 months, that ETF will be excluded from sign-up ETF.<br>- If market makers fail to meet the minimum number of quoted ETFs for the last 12 months, the market maker qualification may be revoked. |
|         |         | P21             | Revised Note about number of provision of virtual servers.  |
|         |         | P23             | Deleted this page because of end of acclimation period  |
|         |         | P29             | Added Note about Lead time for Application<br>- For newly listing ETF, it needs to be made at least 1 week before the listing date.   |
| 2021/3  | 3.1     | P24             | Added slide about Fast Market System.   |
|         |         | P32             | Revised target ETFs in Ver.2.0 scheme.  |
| 2021/9  | 3.2     | P32             | Revised target ETFs in Ver.2.0 scheme.  |
| 2021/11 | 3.3     | P23             | Deleted the page about Email RFQ Service due to the termination of the service.   |
| 2022/4  | 3.4     | P10             | Corrected and supplemented errors in sign-up timing, etc.   |
|         |         | P30             | Supplemental information on the description of the matching funds target.   |
|         |         | P31             | New page established with the addition of matching funds coverage.  |

# Revision History

|         | Version | Revised Page(s) | Summary of Revisions  |
|---------|---------|-----------------|---|
| 2022/4  | 3.4     | P10             | Corrected and supplemented errors in sign-up timing, etc.   |
|         |         | P30             | Supplemental information on the description of the matching funds target.   |
|         |         | P31             | New page established with the addition of matching funds coverage.  |
| 2022/6  | 3.5     | P30             | Revised target ETFs in Ver.2.0 scheme.  |
| 2022/12 | 3.6     | P29             | Added that applications for sponsorship of newly listed ETFs must be submitted "... or the first business day of the first month after the listing date".         |
|         |         | P30             | Regarding the priority conditions for sponsored ETFs, state that they are usually in the following order: quantity of executions, quoting time, and sign-up date. |
|         |         | P31             | Revised obligations in some ETFs in Ver.2.0 scheme.   |
| 2023/1  | 3.7     | P10             | Addition of inclusion of leveraged inverse ETFs in the scheme.  |
|         |         | P13, 14         | Addition regarding Obligation to add leveraged inverse ETFs to the scheme.  |
|         |         | P16, 19, 21, 22 | Added that leveraged inverse ETFs are not eligible for incentive offerings  |
|         |         | P25             | Specifies that leveraged inverse ETFs are also exempt from short selling restrictions.  |
|         |         | P30             | Added that leveraged inverse ETFs can be eligible for sponsored scheme.   |
| 2023/6  | 3.8     | P9              | Added that actively managed ETFs are also subject to the scheme.  |
|         |         | P13             | Added a note on how to classify issue types for actively managed ETF obligations.   |
|         |         | P30             | Added that actively managed ETFs can also be eligible for the sponsorship program.  |
|         |         | P32             | Specifies that actively managed ETFs are added as eligible for matching funds   |
| 2023/8  | 3.9     | P31             | Revised target ETFs in Ver.2.0 scheme.  |
| 2023/9  | 4.0     | P31, 33         | Revised target ETFs in Ver.2.0 scheme.  |
| 2023/12 | 4.1     | P31             | Revised sponsored condition in Ver.2.0 scheme.  |
| 2023/12 | 4.2     | P31             | Revised sponsored condition in Ver.2.0 scheme.  |

# Revision History

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|        | Version | Revised Page(s) | Summary of Revisions  |
|--------|---------|-----------------|---|
| 2024/3 | 4.3     | P15             | Change of Obligations for JPX Prime 150 Index to Type A.      |
|        |         | P19             | Partial revision of incentive in proportion to trading value. |
|        |         | P32-35          | Revised sponsored condition in Ver.2.0 scheme.                |

# Positioning of this document

- ETF Market Making Incentive Scheme is defined in TSE Business Regulations, where it states that details of said scheme shall be prescribed separately.
- This document contains the details of the ETF Market Making Incentive Scheme.

## Related Documents

| Detailed Scheme and Operations   | Application/Report Format   |  |
|--|---|--|
|  | Market Maker to TSE   | TSE to Market Maker  |
| <b>ST-1* Handling of ETF Market Making Incentive Scheme</b> *This document<br>(Details and how to apply) | <b>MT-1 Application for designation as MM</b><br>Application to be designated as market maker (MM)          | <b>TM-1 Notification of Designation</b><br>Notice sent by TSE to an MM and/or Trading Participant to inform the recipient(s) of new MM status              |
| <b>ST-2 List of ETFs</b><br>Parameters applied as quoting obligation and incentive                       | <b>MT-2 Application of ETF &amp; Virtual Server</b><br>Application to specify which ETF & VS to market make | <b>TM-2 Market Maker Report</b><br>Report sent by TSE to MMs on daily performance of ETFs under the scheme   |
| <b>ST-3 FAQ</b><br>Frequently asked questions and answers pertaining to this scheme                      | <b>MT-3 Application for contact</b><br>Form to indicate contact for market making                           | <b>TM-3 Notification of Cancellation</b><br>Notice sent by TSE to an MM and/or Trading Participant to inform the recipient(s) of cancellation of MM status |
|  | <b>MT-4 Application for canceling designation</b><br>Application to cancel designation as MM                |  |

\* The application flow is described later.

\* For a while, effective date of any applications from Market Makers/Asset Managers must be the beginning of the month, however, for newly listed issues, applications in the middle of the month will be accepted.

# Positioning of this document (continued)

## Related Documents

| Application/Report Format  |   |
|--|---|
| Asset Manager to TSE   | TSE to Asset Manager  |
| <b>AT-1 NDA</b><br>Non-disclosure agreement between an asset manager (AM) and TSE for the AM requesting TSE to disclose performance reports of MM(s)           | <b>TA-1 Report by ETF</b><br>Report sent by TSE to an AM on daily performance of MM(s) for managed ETFs |
| <b>AT-2 Application to receive report</b><br>Form for an AM to indicate ETFs and its contact for the AM requesting TSE to disclose performance reports         |   |
| <b>AT-3 Sponsored usage contract</b><br>Contract the AM concludes with TSE to use sponsored market making incentive scheme                                     |   |
| <b>AT-4 Application for sponsored market making</b><br>Form that the AM submits to TSE to specify parameters of sponsored market making incentive scheme usage |   |

\* The application flow is described later.

# Table of Contents

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1. Details of ETF Market Making Incentive Scheme
2. Continuous Quote Obligation
3. Incentives
4. Others
5. Sponsored ETF Market Making Incentive Scheme
6. Application Flow



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# 1. Details of ETF Market Making Incentive Scheme

# Overview of this Scheme

- This scheme imposes a continuous quoting obligation and delivers a number of incentives.

| Category  | Item  | Description  |
|---|---|--|
| Target  | All ETFs  | <ul style="list-style-type: none"> <li>• ETNs are not included in this scheme.</li> <li>* Leveraged/Inverse ETFs and actively managed ETFs are also eligible</li> </ul>  |
| Qualifications                                    | Prop Desk of TSE Trading Participant<br>Or<br>Registered Low Latency Trader | <ul style="list-style-type: none"> <li>• Prop Desk of TSE Member Firm (Type 1 Financial Instruments/Foreign Securities Broker)</li> <li>• Agency (Registered as Low Latency Trader)</li> </ul> <p>Either can sign up as an ETF Market Maker. The firm must apply through a TSE trading participant to sign up as an agency market maker.</p> <ul style="list-style-type: none"> <li>• Dedicated Virtual Server is needed.</li> </ul> |
| Obligation<br>(Continuous<br>Quote<br>Obligation) | (1) Number of ETFs for Continuous Quoting                                   | <ul style="list-style-type: none"> <li>• Must show quotes for at least the number of ETFs designated</li> </ul>  |
|   | (2) Quoting Time  | <ul style="list-style-type: none"> <li>• At least 80% of the time during continuous auction. Exempt from obligation during trading halts or Special Quote periods.</li> </ul>  |
|   | (3) Spread & Minimum Quantity   | <ul style="list-style-type: none"> <li>• Depends on type of ETF</li> </ul>   |
| Incentives  | 1. Proportional to Trading Value  | <ul style="list-style-type: none"> <li>• Price rate differs by liquidity (Average Trading Value).</li> </ul>   |
|   | 2. Waiver of Access Fee   | <ul style="list-style-type: none"> <li>• Access fee is partially waived for eligible issues.</li> </ul>  |
|   | 3. Waiver of Virtual Server Fee   | <ul style="list-style-type: none"> <li>• Server fee is partially waived when continuously quoting at least the number of ETFs designated.</li> </ul>   |

\* It is possible to sign up through multiple trading participants. However, it is not possible to do so for a single issue from multiple trading participants. This means that, for example, you would sign up for 20 unique ETFs from trading participant A and a different 10 from trading participant B. In that case, '3. Waiver of Virtual Server Fee' is paid to trading participant whose code is the lowest.

\* Registration as a Low Latency Trader needs to be completed before applying.

\* If Number of ETFs for continuous Quoting is not fulfilled, any incentives including sponsored ones are not provided.

# Overview of this Scheme (Continued)

| Category      | Item                        | Description  |
|---------------|-----------------------------|--|
| Number of MMs | No Limit                    | <ul style="list-style-type: none"> <li>No upper limit on the number of market makers</li> </ul>  |
| Measuring     | By Virtual Server           | <ul style="list-style-type: none"> <li>Must register dedicated virtual server(s) per market maker to allow for measuring of the performance of each market maker</li> </ul>  |
| Other         | Lead time for Application   | <ul style="list-style-type: none"> <li>It takes approx. one week from application to registration.</li> </ul>  |
|               | Announcement                | <ul style="list-style-type: none"> <li>TSE will announce name of market maker via website, etc. upon sign up.</li> <li>TSE will not announce which market maker covers which ETF, but whether market maker is preset.</li> <li>By reporting, Asset managers may be able to be aware that which market maker is registered and performance of their own ETFs</li> </ul> |
|               | Reporting                   | <ul style="list-style-type: none"> <li>TSE sends monthly reports on performance and incentives to trading participant and/or market maker.</li> <li>Asset managers may, after concluding NDA with TSE, also apply to receive monthly reports containing the list of registered market makers and performance.</li> </ul>   |
|               | Feedback                    | <ul style="list-style-type: none"> <li>The market maker provides feedback on how to improve the trading environment.</li> </ul>  |
|               | If Obligation not Fulfilled | <ul style="list-style-type: none"> <li>Market makers may be excluded from sign-up ETF or MM if obligation is not fulfilled for a certain period.</li> </ul>  |

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## 2. Continuous Quote Obligation

# Obligation: Number of ETFs for Continuous Quoting and Quoting Time

## 1 . Number of ETFs for Quoting

- MMs must show quotes in at least 5 ETFs, except for leveraged /Inverse type, in order to satisfy this obligation.

| Course   | Notes  |
|--|--|
| <b>At least 5 ETFs,<br/>Except for leveraged/inverse ETF</b> | <ul style="list-style-type: none"><li>• No restrictions on the type of ETFs, except for leveraged/inverse ETFs (highly liquid ETFs can be included)</li><li>• There is no acclimation period</li></ul> |

## 2 . Quoting Time

- The MM must show quotes for no less than 80% of the time during continuous auction. The MM is exempt from this obligation during trading halts or Special Quote periods.

\*Where there are compelling reasons, such as shutdown of underlying market, quoting obligation is exempted. During black-out days, only in case of excessive increase of trading volume, exemption is examined.

\*Foreign index ETFs are categorized to Type C first. Upon request, individual ETFs may be categorized to Type D. For applied parameters, see "ST-2 List of ETFs".

\* Although the obligation of quoting time is 80%, the system sets the obligation of quoting time as 100% in order to exclude it from incentive eligibility. So even if a MM's fulfillment rate of obligation exceeds 80%, the status will be indicated as "NG" on the performance report, but the actual obligation fulfillment status will be determined based on whether the performance exceeds 80%.

# Obligation (Cont.): Spread and Minimum Quantity

## 3. Spread and Minimum Quantity

- Depending on the ETF type, the MM must display quotes for a sufficient quantity of ETFs within certain spread(s).
- There are stricter spread/quantity requirements for leading ETFs (i.e., tracking Nikkei 225 or TOPIX).

| Type | Issue   | Maximum Bid-Ask Spread<br>(whichever is larger) | Minimum Quantity<br>(one leg) |
|------|---|---|-------------------------------|
| A    | ETFs tracking Nikkei 225, TOPIX, JPX Nikkei 400 or JPX Prime 150<br>(excluding leveraged/inverse type)  | 20 bps OR 2 ticks                               | JPY 30 mil.                   |
| B    | ETFs tracking other domestic stocks, REITs, Bond,<br>Leveraged inverse ETFs tracking domestic stocks, REITs and bonds, and<br>Actively managed ETFs comprised mainly of domestic stocks, REITs and bonds. | 50 bps OR 3 ticks                               | JPY 10 mil.                   |
| C    | Foreign index and commodity ETFs,<br>Leveraged/inverse ETFs that do not fall under type B, and<br>Actively managed ETFs composed mainly of foreign assets and commodities                                 | 50 bps OR 3 ticks                               | JPY 5 mil.                    |
| D    | Individually designated ETFs  | 80 bps OR 4 ticks                               | JPY 5 mil.                    |

# Quote Display Sample

| Offer Volume (Value) | Price           | Bid Volume (Value) |
|----------------------|-----------------|--------------------|
|                      | Offer price 105 |                    |
| 200,000 (20.8 mil.)  | 104             |                    |
| 100,000 (10.3 mil.)  | 103             |                    |
|                      | 102             | 350,000 (35.7 mil) |
|                      | 101 Bid price   |                    |

- With a quote of JPY 30 mil, as more offer quotes pile up, JPY104 (the price to fulfill the obligation) becomes the Offer price.
- MMs can use multiple order/price levels within the spread to fulfill the obligation.

Spread is 2 ticks/194bps\*

\*Spread = (Offer price – Bid price) / Mid (Offer and Bid)

Quote Display Time (%) =  

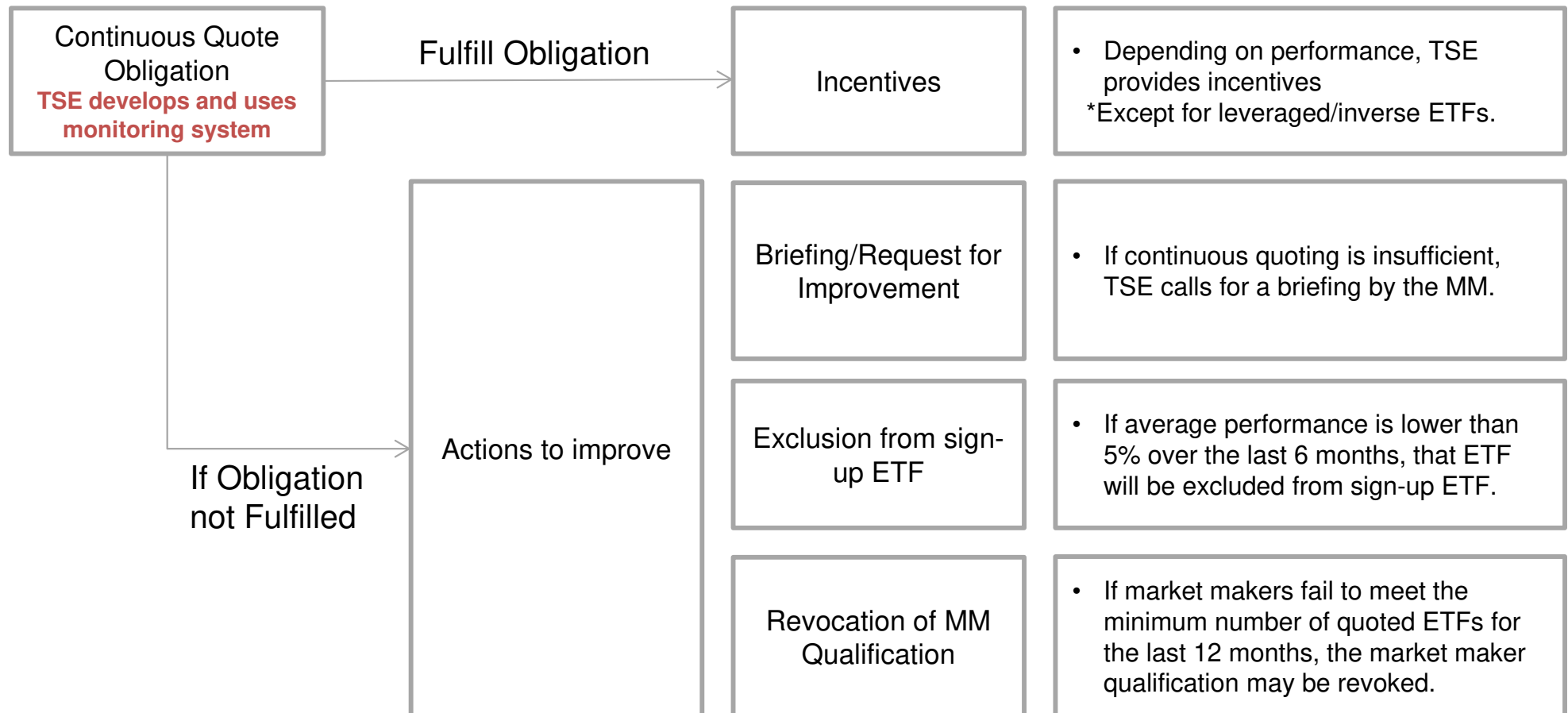
$$\frac{\text{Fulfilling Obligation Period (Micro seconds, Cumulative)}}{\text{Quoting available Period (Micro seconds, Cumulative)}}$$

\*Quote Display is valid during continuous auction hours (excl. trading halts or Special Quote periods).

\*All time measurements are based on arrowhead timestamps for each order. The fulfillment status is determined on a monthly basis.

# Managing MM Qualification

- TSE will monitor each MM's activity by using a newly developed system that allows for measuring MM performance.
- If the MM does not fulfill its obligation, TSE contacts and requests a briefing from the MM, which can result in the exclusion from sign-up ETF and MM.





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## 3. Incentives

# Additional Incentives on ETFs for Diversified Investment

- Higher incentives are provided on ETFs tracking the indices listed below, which are considered essential for diversified investment.

|        | Japan  | World  | Developed   | Emerging   |
|--------|--|--|---|--|
| Equity | —  | <ul style="list-style-type: none"> <li>MSCI ACWI</li> <li>FTSE Global All Cap</li> </ul>                               | <ul style="list-style-type: none"> <li>FTSE Developed</li> <li>FTSE Developed All Cap</li> <li>S&amp;P 500</li> <li>CRSP U.S. Total Market</li> <li>MSCI World</li> <li>MSCI World IMI</li> </ul> | <ul style="list-style-type: none"> <li>MSCI Emerging Markets</li> <li>FTSE Emerging</li> <li>FTSE RAFI Emerging</li> </ul>         |
|        | —  | —  | <ul style="list-style-type: none"> <li>MSCI Europe</li> <li>FTSE Developed Europe All Cap</li> <li>STOXX Europe 600</li> <li>MSCI Pacific</li> </ul>  | <ul style="list-style-type: none"> <li>MSCI AC Asia Pacific</li> </ul>   |
| Bond   | <ul style="list-style-type: none"> <li>NOMURA-BPI Total</li> <li>DBI total</li> <li>NOMURA-BPI JGB</li> <li>Barclays Japan Government Float Adjusted Bond</li> </ul> | <ul style="list-style-type: none"> <li>FTSE World Government Bond</li> <li>Barclays Capital Global Treasury</li> </ul> | <ul style="list-style-type: none"> <li>Bloomberg-Barclays Global Aggregate</li> <li>Barclays U.S. Government Float Adjusted Bond</li> <li>Barclays Euro Government Float Adjusted Bond</li> </ul> | <ul style="list-style-type: none"> <li>JP Morgan GBI EM Global Diversified</li> <li>JP Morgan Emerging Market Bond Plus</li> </ul> |
| REIT   | <ul style="list-style-type: none"> <li>TSE REIT Index</li> </ul>   | —  | <ul style="list-style-type: none"> <li>S&amp;P Developed REIT</li> <li>S&amp;P US REIT</li> <li>S&amp;P European REIT</li> <li>FTSE NAREIT Equity REIT</li> </ul>                                 | —  |

# Incentive 1: Proportional to Trading Value

- When MMs fulfill this obligation, they are provided with incentives based on ETF trading value.
- Leveraged/inverse ETFs are always treated as Tier V and are not eligible for incentive grants.

Incentives for MMs by Tier

| Tier | Average Trading Value in JPY<br>(Continuous auction) | Incentive for Others | (Batch auction or MM's execution against an MM) | Remarks   |
|------|--|----------------------|---|---|
| I    | Less than 100 mil.<br>(Newly Listed)                 | 0.5 bps              | 0.2 bps   | Since trading volumes for less liquid / newly listed ETFs are low, relatively higher incentives are provided. |
| II   | 100 mil. or more, but less than 500 mil.             | 0.25 bps             | 0.2 bps   | MMs can trade ETFs essentially free of charge on issues in this trading volume bracket.                       |
| III  | 500 mil. or more, but less than 1 bil.               | 0.15 bps             | 0.1 bps   | The fee is higher for issues in this trading volume bracket, but some incentives are available.               |
| IV   | 1 bil. or more, but less than 5 bil.                 | 0.1 bps              | 0.1 bps   |   |
| V    | 5 bil. or more                                       |                      |   | There are no incentives for this trading volume bracket and leveraged/inverse ETFs.                           |

\*There are no financial incentives for Tier V issues, but these issues except for leveraged/inverse ETFs do count as issues included in the number of ETFs for quoting. Also, they are subject to other incentives excluding leveraged/inverse ETFs .

\* In case registered Low Latency Trader conducts market making, incentive is provided to TSE trading participant as discount of trading fee.

# Tier Review Cycle


- Tiers are reviewed every three months.
- Announcements are made after the three-month measuring period. New parameters are applied on the following month.

## Sample Schedule

| Dec.     | Jan.                | Feb. | Mar.     | Apr.                | May | Jun.     | Jul.                | Aug. | Sep.     | Oct.                | Nov. | Dec.     |
|----------|---------------------|------|----------|---------------------|-----|----------|---------------------|------|----------|---------------------|------|----------|
| Measure  |                     |      | Announce | Apply New Parameter |     |          |                     |      |          |                     |      | Measure  |
|          |                     |      | Measure  |                     |     | Announce | Apply New Parameter |      |          |                     |      |          |
|          |                     |      |          |                     |     | Measure  |                     |      | Announce | Apply New Parameter |      |          |
| Announce | Apply New Parameter |      |          |                     |     |          |                     |      | Measure  |                     |      | Announce |

## Incentive 2: Waiver of Access Fee

- Currently, TSE charges the access fee in proportion to the number of orders.
- Since MMs have to display continuous quotes at appropriate prices for many issues, incentives based solely on trading value are not sufficient, especially in the case of illiquid issues.

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- ✓ By fulfilling obligation, MMs receive 0.1JPY/order up to 100,000 orders per ETF/day
  - ✓ Applicable on all ETFs the MM signs up for, except for leverage/inverse ETFs

| Product  | Waiver |
|--|--------|
| ETFs other than leveraged/inverse ETFs that have signed up as market maker | Yes    |
| Other ETFs not signed up as market maker or leveraged/inverse ETFs         | No     |
| Underlyings (Stocks, REITs, etc.)  | No     |

## Incentive 3: Provision of Virtual Servers

- Since trading larger amounts of ETFs requires higher capacity, TSE can provide virtual servers free of charge to MMs who sign up for more issues.
- Note that leveraged/inverse ETFs are excluded for this incentive.

| Number of ETFs for Quoting<br>(Excluding leveraged/inverse ETFs) | Number of Free Virtual Servers<br>Type A (200 msg/sec) |
|--|--|
| 20 ETFs  | 2  |
| 30 ETFs  | 3  |
| 40 ETFs  | 4  |
| 60 ETFs  | 6  |
| 80 ETFs  | 8  |
| 100 ETFs   | 10   |
| (For every 20 ETFs over 100)                                     | (2)  |

\*A virtual server is a necessary component for placing orders to TSE.

\*Currently, it costs JPY 90,000/month to use a Type A virtual server (processing capacity of 200 messages per second).

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## 4. Others

# Fast Market System

- When volatility is high, the obligation will be mitigated for a certain period in light of market conditions.

| Item                    | Descriptions  | Remarks  |
|-------------------------|---|--|
| Activation trigger      | Comprehensive decisions based on requests from market makers, AMs and other market participants, as well as market conditions | <ul style="list-style-type: none"> <li>As a general rule, "when Nikkei VI becomes 30 or more or when a majority of market makers request it"</li> <li>However, TSE comprehensively judges based on market conditions, requests from participants, etc.</li> </ul>  |
| Details of Mitigation   | To be mitigated in 2 stages.<br>① Spread doubles as normal<br>② Spreads quadrupled as normal                                  | <ul style="list-style-type: none"> <li>Basically, the mitigation of ① is implemented, but if the high volatility state continues for a long period of time, the mitigation of ② is implemented at the comprehensive judgment.</li> <li>The mitigation of ② is assumed to be triggered when the Nikkei VI is extremely volatile, such as 50 or more.</li> </ul> |
| Term                    | From the date of activation to the date of release  | <ul style="list-style-type: none"> <li>The Fast Market shall be triggered intraday. Declare activation during the day and mitigate obligations from the day of activation.</li> <li>Declare cancellation after the close of the day before cancellation.</li> </ul>  |
| Release trigger         | Comprehensive decisions based on requests from market makers, AMs and other market participants, as well as market conditions | <ul style="list-style-type: none"> <li>As a general rule, "when Nikkei VI falls below 30 for 5 days"</li> <li>However, TSE comprehensively judges based on market conditions and requests from participants, as in the case of the trigger.</li> </ul>   |
| Performance measurement | Measure on a monthly basis, as in normal times  | <ul style="list-style-type: none"> <li>Fast Market is triggered and released on a daily basis, but performance is measured on the basis of 80% of monthly performance, as in normal times.</li> </ul>  |
| Target ETFs             | All ETFs  | <ul style="list-style-type: none"> <li>All ETFs covered by the market-making scheme are covered.</li> </ul>  |
| Scope                   | TSE's obligation and Version2.0.  | <ul style="list-style-type: none"> <li>Sponsored conditions are excluded.</li> </ul>   |



# Reference: Exemption from Short Selling Restriction

- The quotes displayed for the purpose of fulfilling the continuous quote obligation upon sign up as an ETF MM will be handled as indicated in the table below. (The same treatment applies to leveraged/inverse ETFs.)

## Treatment of short selling conducted by ETF MMs

| Applicable statutes on Short Selling Restrictions   | Details  | For short selling by MMs  |
|---|--|---|
| Confirmation, etc. of a Guarantee of Borrowed Securities<br>(Ban of Naked Short Sell)<br><br>Article 26-2-2 | Cannot carry out a short sell without first borrowing  | <b>Exempted</b><br>→ May conduct naked short sell<br>*Must cover for settlement |
| Indication and Confirmation in Cases of Short Selling<br>(Marking)<br><br>Article 26-3                      | Trading Participant must indicate whether it is a short sell or not and similarly verify said fact with entrustor  | <b>Exempted</b><br>→ Can apply "0: Long Sell" classification to any sell orders |
| Prices in the Case of Short Selling (Up-tick Rule)<br><br>Article 26-4                                      | If the stock price drops by 10% or more, the uptick rule applies.  | <b>Exempted</b><br>→ No price test applied                                      |
| Provision, etc. of Information on Short Selling<br>(Reporting)<br><br>Article 26-5                          | If short selling exceeds 0.20% of all listed shares, obligated to report said fact to the exchange; if exceeding 0.50%, the name of the short seller is disclosed. | <b>Exempted</b><br>→ Excluded from outstanding short position                   |

# Reference: Exemption from Short Sell Restriction (continued)

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## Legal Remarks

- \* Exemptions from the short selling rules apply only to ETFs for which the MM has signed up.
- \* Order for Enforcement of the Financial Instruments and Exchange Act (Article 26-2-2 to Article 26-5) & Cabinet Office Ordinance on Restrictions on Securities Transactions, etc. (Article 9 to Article 15) apply to trading.
- \* Short selling conducted by an MM is regarded as the following trading indicated in Cabinet Office Ordinance on Restrictions on Securities Transactions, etc., Article 9-3 (xvii) (Effective from April 1, 2018):  
"among the transactions in which a Member, etc. of the Financial Instruments Exchange conducts Short Selling on his/her own account with regard to the Beneficiary Certificate of an Investment Trust, etc. or Investment Securities or **the transactions in which a Low Latency Trader who has been designated as an entity who places an order pertaining to the following trading concerning Investment Trust Beneficiary Certificates, etc. listed on the Financial Instruments Exchange, pursuant to the rules specified by the Financial Instruments Exchange conducts Short Selling on his/her own account with regard to the Beneficiary Certificate of an Investment Trust, etc. by a means specified by the Financial Instruments Exchange,** set forth in the following sub-items:"

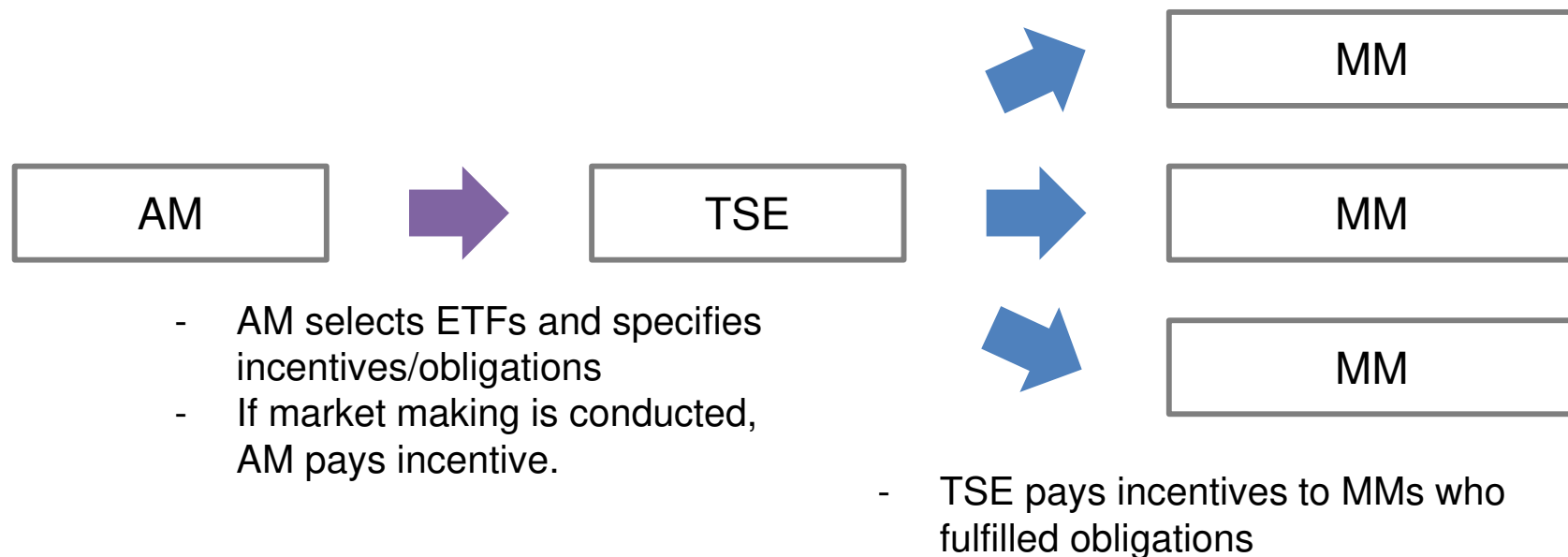
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## 5. Sponsored ETF Market Making Incentive Scheme

# Overview

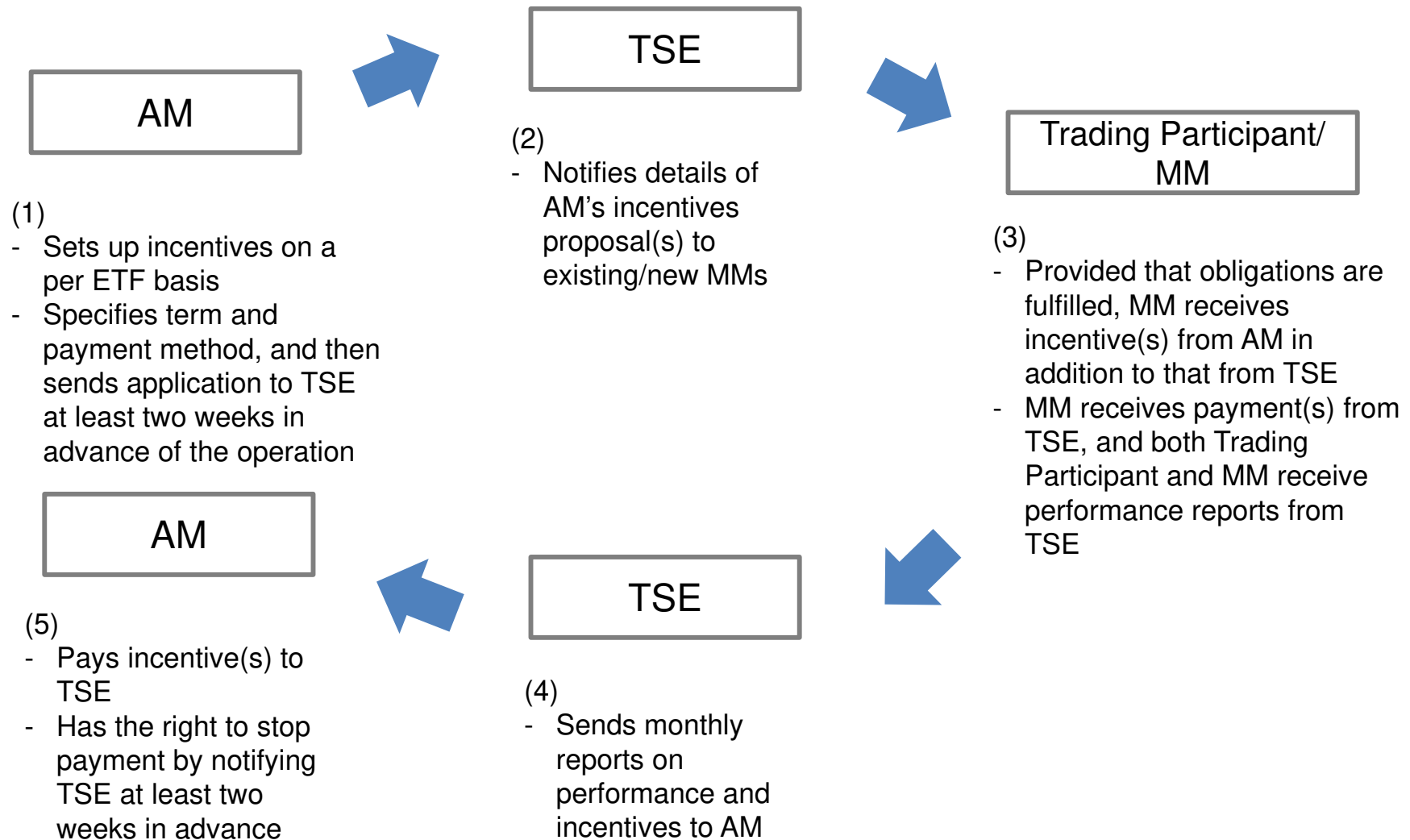
- The scheme involves having **AMs serve as sponsors for additional incentives.**
- In addition to the incentives provided by the exchange, with incentives also coming from AMs, MMs can be more inclined to sign up for seemingly less profitable issues, **raising quoting standards and further improving liquidity** for such ETFs.
- While the non-sponsored scheme by nature offers one-size-fits-all incentives across the board to ensure equal treatment of each ETF, the sponsored scheme has the potential to allow for more customized treatment, including delivering higher incentives for less profitable issues.
- **As a result, ETFs that originally lacked MMs have a greater chance of being brought to listing.**

## Application Process



# Diagram

## Operational Flow of Sponsored ETF Market Making Incentive Scheme



\* The actual application process is described later.

# Details of Sponsored ETF Market Making Incentive Scheme

| Category                   | Item   | Description   |
|----------------------------|--|---|
| Sign up                    | Sign up for ETF Market Making Incentive Scheme<br>(No need for additional sign up) | <ul style="list-style-type: none"> <li>- The Sponsored ETF Market Making Incentive Scheme (sponsored scheme) automatically applies to MMs at the time of sign for the ETFs applicable under the ETF Market Making Incentive Scheme (general scheme); provided, however, that MMs who have not fulfilled the number of ETFs for continuous quoting under the general scheme are not be eligible for incentives even if they fulfill the status of Quote Obligation in the sponsored scheme.</li> </ul> |
| Reporting to Asset Manager | Name of Market Maker<br>Performance of each Market Maker                           | <ul style="list-style-type: none"> <li>- The name of the market maker(s), performance of each market maker and amount of payment with the sponsored scheme will be shared with the asset manager in monthly reports.</li> </ul>   |
| Reporting to Market Maker  | Performance<br>Incentives  | <ul style="list-style-type: none"> <li>- TSE sends a monthly report containing the fulfillment status of the Quote Obligation and incentives to trading participants/MM under the sponsored scheme.</li> <li>- The payment is added to the general scheme incentives.</li> </ul>  |
| Lead time for Application  | At least two weeks<br>(*At least 1 week for newly listing ETF)                     | <ul style="list-style-type: none"> <li>- To ensure there is sufficient time to inform the public, an application needs to be made at least two weeks in advance including application for changes in specifics.</li> <li>- For newly listing ETF, it needs to be made at least 1 week before the listing date or the first business day of the first month after the listing date.</li> </ul>   |
| Publication                | Publicize information via the website, etc.  | <ul style="list-style-type: none"> <li>- After the application of an AM has been accepted, detailed conditions will be made public via the website, etc.</li> </ul>   |

# Items Specified by AMs in the Sponsored ETF Market Making Incentive Scheme

| Category                         | Item   | Description  |
|----------------------------------|--|--|
| Target                           | Any ETFs   | <ul style="list-style-type: none"> <li>The asset manager can choose as little as one ETF from those it is currently managing.</li> <li>*Leveraged/inverse ETFs and Actively managed ETFs can also be eligible.</li> </ul>  |
| Period                           | Three months to one year   | <ul style="list-style-type: none"> <li>In consideration of the preparations taken by the market maker, a minimum of three months is required.</li> <li>The asset manager must reapply in order to specify incentive(s) for a single issue for more than one year.</li> </ul>   |
| Obligation<br>(Quote Obligation) | Maximum Spread (ticks/bps)<br>Amount of quote (JPY)<br>Quoting time period (%)               | <ul style="list-style-type: none"> <li>For each item, asset managers can specify a Quote Obligation that differs from that in the general scheme.</li> </ul>   |
|                                  | Grouping<br>(Setting the Quote Obligation for multiple ETFs)                                 | <ul style="list-style-type: none"> <li>Asset managers can specify the Quote Obligation eligible for incentives only when the Quote Obligation has been fulfilled for multiple ETFs.</li> <li>Asset managers can only select a fixed amount for incentives when designating grouping conditions.</li> </ul>   |
|                                  | AUM trigger  | <ul style="list-style-type: none"> <li>Asset managers can specify a condition in which incentives will be paid to market makers who have fulfilled the Quote Obligation only when their AUMs exceed a certain amount.</li> </ul>   |
| Incentives                       | Total amount of payment<br>– JPY100,000 to 1,000,000/month (per ETF)                         | <ul style="list-style-type: none"> <li>Asset managers specify total amount of monthly incentives for each ETF.</li> <li>It includes incentive set as AUM Trigger.</li> </ul>   |
|                                  | Payment method<br>– Fixed compensation/Trading volume proportional                           | <ul style="list-style-type: none"> <li>Asset managers can select either payment method: a fixed amount (JPY XX per company) or trading volume proportional (market makers eligible for incentives).</li> </ul>   |
|                                  | Maximum Number of Market Makers  | <ul style="list-style-type: none"> <li>Asset managers can specify maximum number of market makers eligible for incentives.</li> </ul>  |
|                                  | Priority conditions<br>- In order of quoting time period/quantity of executions/sign-up date | <ul style="list-style-type: none"> <li>Asset managers specify priority according to the following three conditions to provide incentives: 1) quoting time period, 2) quantity of executions, or 3) sign-up date.</li> <li>When the number of market makers who have fulfilled the Quotation Obligation exceeds the maximum number of market makers, asset managers can first assign priority, and then designate which are to be eligible for incentives.</li> </ul> |

# Matching Funds (1) ETFMM scheme Ver.2.0 - Japanese Equity -

- Additional incentive/obligation will be set for certain period. Maximum number of ETFs will be set per index.
- Matching Funds = TSE will provide equivalent amount of incentive as a sponsor

| Japanese Equity |  | Obligation (Qty./Spread)        | Monthly Incentive<br>(Total of TSE and AM) |                    | Max no.<br>of ETFs |
|-----------------|--|---------------------------------|--|--------------------|--------------------|
| Market          | JPX Prime 150  | JPY100 million/ 2ticks or 20bps | Top2 MMs                                   | JPY 300,000 /month | 1 ETF              |
| Sector          | TOPIX-17 FOODS                                       | JPY30 million/ 3ticks or 25bps  | Top1 MM                                    | JPY 150,000 /month | 1 ETF              |
|                 | TOPIX-17 ENERGY RESOURCES                            | JPY30 million/ 3ticks or 25bps  | Top1 MM                                    | JPY 150,000 /month | 1 ETF              |
|                 | TOPIX-17 CONSTRUCTION & MATERIALS                    | JPY30 million/ 3ticks or 25bps  | Top1 MM                                    | JPY 150,000 /month | 1 ETF              |
|                 | TOPIX-17 RAW MATERIALS & CHEMICALS                   | JPY30 million/ 3ticks or 25bps  | Top1 MM                                    | JPY 150,000 /month | 1 ETF              |
|                 | TOPIX-17 PHARMACEUTICAL                              | JPY30 million/ 3ticks or 25bps  | Top1 MM                                    | JPY 150,000 /month | 1 ETF              |
|                 | TOPIX-17 AUTOMOBILES & TRANSPORTATION EQUIPMENT      | JPY30 million/ 3ticks or 25bps  | Top1 MM                                    | JPY 150,000 /month | 1 ETF              |
|                 | TOPIX-17 STEEL & NONFERROUS                          | JPY30 million/ 3ticks or 25bps  | Top1 MM                                    | JPY 150,000 /month | 1 ETF              |
|                 | TOPIX-17 MACHINERY                                   | JPY30 million/ 3ticks or 25bps  | Top1 MM                                    | JPY 150,000 /month | 1 ETF              |
|                 | TOPIX-17 ELECTRIC APPLIANCES & PRECISION INSTRUMENTS | JPY30 million/ 3ticks or 25bps  | Top1 MM                                    | JPY 150,000 /month | 1 ETF              |
|                 | TOPIX-17 IT & SERVICES, OTHERS                       | JPY30 million/ 3ticks or 25bps  | Top1 MM                                    | JPY 150,000 /month | 1 ETF              |
|                 | TOPIX-17 ELECTRIC POWER & GAS                        | JPY30 million/ 3ticks or 25bps  | Top1 MM                                    | JPY 150,000 /month | 1 ETF              |
|                 | TOPIX-17 TRANSPORTATION & LOGISTICS                  | JPY30 million/ 3ticks or 25bps  | Top1 MM                                    | JPY 150,000 /month | 1 ETF              |
|                 | TOPIX-17 COMMERCIAL & WHOLESALE TRADE                | JPY30 million/ 3ticks or 25bps  | Top1 MM                                    | JPY 150,000 /month | 1 ETF              |
|                 | TOPIX-17 RETAIL TRADE                                | JPY30 million/ 3ticks or 25bps  | Top1 MM                                    | JPY 150,000 /month | 1 ETF              |
|                 | TOPIX-17 BANKS                                       | JPY30 million/ 3ticks or 25bps  | Top1 MM                                    | JPY 150,000 /month | 1 ETF              |
|                 | TOPIX-17 FINANCIALS (EX BANKS)                       | JPY30 million/ 3ticks or 25bps  | Top1 MM                                    | JPY 150,000 /month | 1 ETF              |
|                 | TOPIX-17 REAL ESTATE                                 | JPY30 million/ 3ticks or 25bps  | Top1 MM                                    | JPY 150,000 /month | 1 ETF              |



# Matching Funds (2) ETFMM scheme Ver.2.0 - Foreign Equity -

| Foreign Equity        |                               | Obligation (Qty./Spread)        | Monthly Incentive<br>(Total of TSE and AM) |                    | Max no.<br>of ETFs |
|-----------------------|-------------------------------|---------------------------------|--|--------------------|--------------------|
| Single<br>Country     | S&P500                        | JPY100 million/ 2ticks or 20bps | Top2 MMs                                   | JPY 200,000 /month | 2 ETFs*            |
|                       | NASDAQ100                     | JPY100 million/ 2ticks or 30bps | Top2 MMs                                   | JPY 400,000 /month | 2 ETFs*            |
|                       | Dow Jones Industrial          | JPY100 million/ 2ticks or 30bps | Top2 MMs                                   | JPY 400,000 /month | 2 ETFs*            |
|                       | DAX                           | JPY100 million/ 2ticks or 30bps | Top2 MMs                                   | JPY 200,000 /month | 2 ETFs*            |
|                       | FTSE100                       | JPY100 million/ 2ticks or 30bps | Top2 MMs                                   | JPY 200,000 /month | 2 ETFs*            |
| Multiple<br>countries | EURO STOXX 50                 | JPY100 million/ 2ticks or 30bps | Top2 MMs                                   | JPY 200,000 /month | 2 ETFs*            |
|                       | MSCI Kokusai                  | JPY100 million/ 2ticks or 20bps | Top2 MMs                                   | JPY 200,000 /month | 2 ETFs*            |
|                       | MSCI Emerging                 | JPY100 million/ 2ticks or 40bps | Top2 MMs                                   | JPY 300,000 /month | 2 ETFs*            |
|                       | MSCI ACWI                     | JPY15 million/ 2ticks or 40bps  | Top2 MMs                                   | JPY 300,000 /month | 2 ETFs*            |
| Sector                | S&P500 Communication Services | JPY30 million/ 3ticks or 30bps  | Top1 MM                                    | JPY 200,000 /month | 1 ETF              |
|                       | S&P500 Consumer Discretionary | JPY30 million/ 3ticks or 30bps  | Top1 MM                                    | JPY 200,000 /month | 1 ETF              |
|                       | S&P500 Consumer Staples       | JPY30 million/ 3ticks or 30bps  | Top1 MM                                    | JPY 200,000 /month | 1 ETF              |
|                       | S&P500 Energy                 | JPY30 million/ 3ticks or 30bps  | Top1 MM                                    | JPY 200,000 /month | 1 ETF              |
|                       | S&P500 Financials             | JPY30 million/ 3ticks or 30bps  | Top1 MM                                    | JPY 200,000 /month | 1 ETF              |
|                       | S&P500 Health Care            | JPY30 million/ 3ticks or 30bps  | Top1 MM                                    | JPY 200,000 /month | 1 ETF              |
|                       | S&P500 Industrials            | JPY30 million/ 3ticks or 30bps  | Top1 MM                                    | JPY 200,000 /month | 1 ETF              |
|                       | S&P500 Information Technology | JPY30 million/ 3ticks or 30bps  | Top1 MM                                    | JPY 200,000 /month | 1 ETF              |
|                       | S&P500 Materials              | JPY30 million/ 3ticks or 30bps  | Top1 MM                                    | JPY 200,000 /month | 1 ETF              |
|                       | S&P500 Real Estate            | JPY30 million/ 3ticks or 30bps  | Top1 MM                                    | JPY 200,000 /month | 1 ETF              |
|                       | S&P500 Utilities              | JPY30 million/ 3ticks or 30bps  | Top1 MM                                    | JPY 200,000 /month | 1 ETF              |

\*One ETF each with/without currency hedging

# Matching Funds (3) ETFMM scheme Ver.2.0 - Foreign Bond / REIT -

| Foreign Bond          |                                     | Obligation (Qty./Spread)        | Monthly Incentive<br>(Total of TSE and AM) |                    | Max no.<br>of ETFs |
|-----------------------|-------------------------------------|---------------------------------|--|--------------------|--------------------|
| Single<br>Country     | US Treasury 5-10 years              | JPY100 million/ 2ticks or 20bps | Top2 MMs                                   | JPY 150,000 /month | 2 ETFs*            |
|                       | US Treasury 1-5 years               | JPY100 million/ 2ticks or 15bps | Top2 MMs                                   | JPY 200,000 /month | 2 ETFs*            |
|                       | US Treasury over 10 years           | JPY100 million/ 2ticks or 25bps | Top2 MMs                                   | JPY 200,000 /month | 2 ETFs*            |
|                       | German Government Bond 5-10 years   | JPY100 million/ 2ticks or 25bps | Top2 MMs                                   | JPY 200,000 /month | 2 ETFs*            |
|                       | France Government Bond 5-10 years   | JPY100 million/ 2ticks or 40bps | Top2 MMs                                   | JPY 200,000 /month | 2 ETFs*            |
|                       | UK Government Bond 5-10 years       | JPY100 million/ 2ticks or 40bps | Top2 MMs                                   | JPY 200,000 /month | 2 ETFs*            |
|                       | US municipal bond –Investment grade | JPY100 million/ 2ticks or 40bps | Top2 MMs                                   | JPY 200,000 /month | 2 ETFs*            |
| Multiple<br>countries | FTSE WGBI                           | JPY100 million/ 2ticks or 40bps | Top2 MMs                                   | JPY 300,000 /month | 2 ETFs*            |

| REIT   |                                     | Obligation (Qty./Spread)      | Monthly Incentive<br>(Total of TSE and AM) |                    | Max no.<br>of ETFs |
|--------|-------------------------------------|-------------------------------|--|--------------------|--------------------|
| Sector | TSE REIT Logistics Focus Index      | JPY30 million/ 1tick or 25bps | Top2 MMs                                   | JPY 150,000 /month | 1 ETF              |
|        | TSE REIT Office Focus Index         | JPY30 million/ 1tick or 25bps | Top2 MMs                                   | JPY 150,000 /month | 1 ETF              |
|        | TSE REIT Residential Focus Index    | JPY30 million/ 1tick or 25bps | Top2 MMs                                   | JPY 150,000 /month | 1 ETF              |
|        | TSE REIT Hotel & Retail Focus Index | JPY30 million/ 1tick or 25bps | Top2 MMs                                   | JPY 150,000 /month | 1 ETF              |

\*One ETF each with/without currency hedging

# Matching Funds (3) ETFMM scheme Ver.2.0 - Foreign Bond / REIT -

| <b>Active</b>                  |  | Obligation (Qty./Spread)                        | Monthly Incentive<br>(Total of TSE and AM) |                       | Max no.<br>of ETFs |
|--------------------------------|--|---|--|-----------------------|--------------------|
| <b>No category designation</b> | <b>Actively managed ETFs*<br/>(in order of listing)</b>  | JPY10 million/<br>(Spread is set by each ETF)   | Top2 MMs                                   | JPY 200,000<br>/month | 10 ETFs            |
| <b>Category designation</b>    | <b>Actively managed ETFs targeting domestic public and corporate bonds (excluding only gov. bonds)</b> | JPY100 million /<br>(Spread is set by each ETF) | Top2 MMs                                   | JPY 200,000<br>/month | 2 ETFs             |
|                                | <b>Actively managed ETFs for foreign equities</b>  | JPY100 million /<br>(Spread is set by each ETF) | Top2 MMs                                   | JPY 200,000<br>/month | 2 ETFs             |
|                                | <b>Actively managed ETFs for REIT</b>  | JPY50 million /<br>(Spread is set by each ETF)  | Top2 MMs                                   | JPY 200,000<br>/month | 2 ETFs             |

\* Active managed ETFs (in the order of listing) will end by the end of August 2024. Other conditions shall, in principle, be set for a period of 6 months and shall be reviewed periodically.

\* Obligation (spread) is a predetermined number of ticks or spread, whichever is wider.

\* AMs and TSE will contribute same amount.

\* Obligations for Quoting time shall be 80% for all categories.

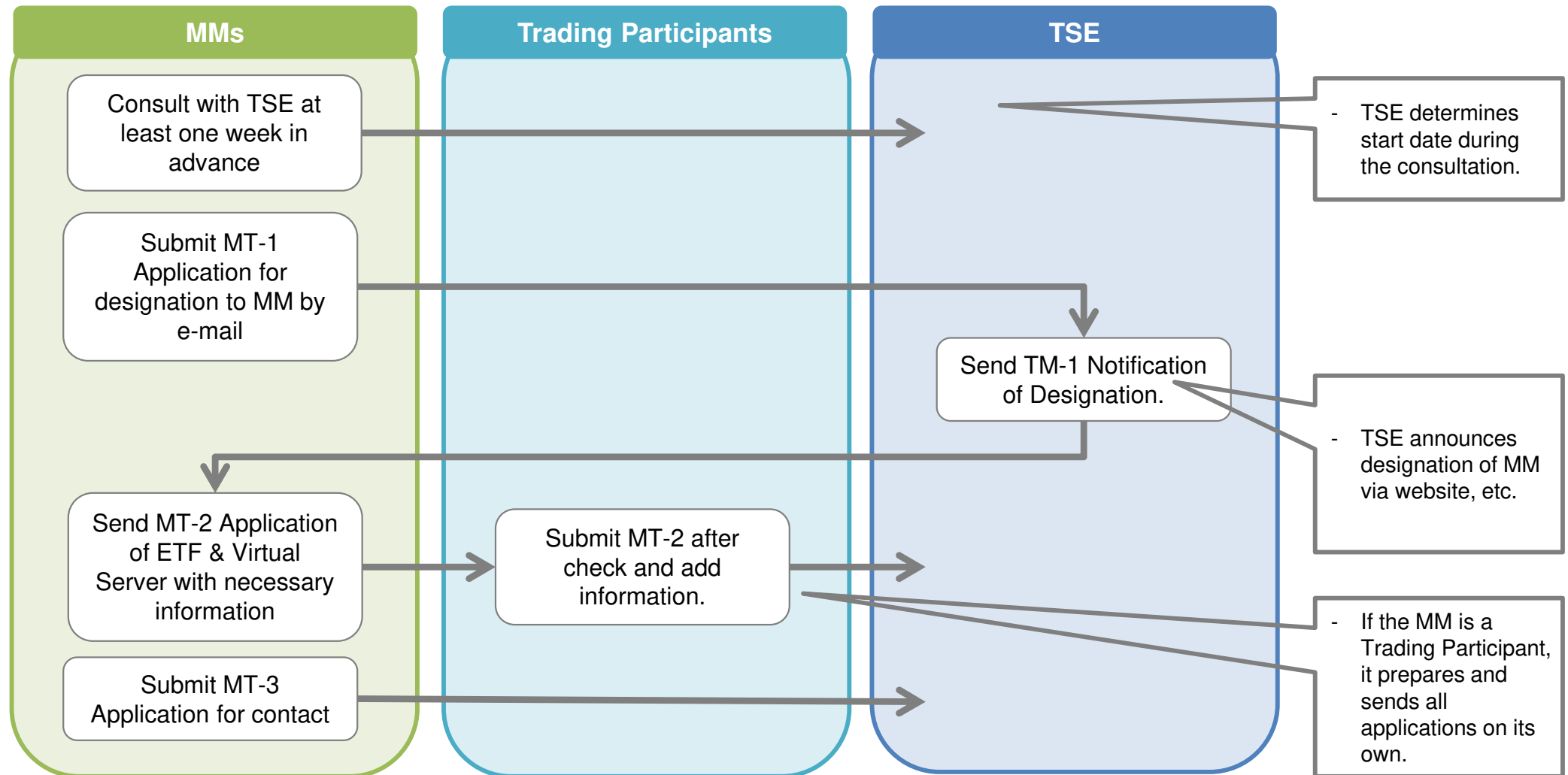
\* Unless otherwise noted, priority conditions shall be in order of trading volume, quoting time, and sign-up date.

So, if 3 or more MMs satisfy the Obligations, the ranking of MM is selected based on trading volume. If the trading volume is also the same, the MM with the longer quotation time is selected.

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## 6. Application Flow

# Application flow: Application and Designation by MMs



# Application Flow: by AMs

- The AMs that receive reports must conclude A-1 and submit A-2; and, those who use the sponsored scheme, must also conclude A-3 and submit A-4 in addition to A-1 and A-2.

