United States Senate

WASHINGTON, DC 20510

March 11, 2024

The Honorable Gary Gensler
Chairman
Securities and Exchange Commission
100 F Street NE
Washington, DC 20549

Dear Chairman Gensler:

We write to urge the Securities and Exchange Commission (SEC) to take steps to protect investors following its recent approval of the listing and trading of certain spot bitcoin exchange-traded products (ETPs).

The SEC's approvals have provided a green light for Wall Street to sell volatile cryptocurrency investments to ordinary Americans through their brokerage and retirement accounts.

Given the significant and unique risks posed by cryptocurrency, it is critical that Americans receive accurate, comprehensive information about bitcoin ETPs. In a recent review by FINRA, roughly 70% of brokers' communications with retail investors regarding cryptocurrency violated fair disclosure rules. In some cases, brokers' communications falsely equated cryptocurrency with cash; in others, they provided misleading explanations of cryptocurrency's risks. These alarming deficiencies raise significant concerns that brokers and advisers may now provide incomplete or deceptive information about bitcoin ETPs to retail investors.

The naming and marketing of many bitcoin ETPs appear to obfuscate important characteristics about these investments. In SEC filings and other investor documents, sponsors commonly refer to bitcoin ETPs as bitcoin "exchange-traded funds" or "ETFs." Although it may seem like a small distinction, this purposeful confusion of terminology is troubling because bitcoin ETPs are different in critical ways from mutual funds and ETFs.

Because bitcoin ETPs are not subject to the substantive and structural protections under the Investment Company Act of 1940, they are not subject to restrictions on harmful practices that apply to most investment funds marketed to retail investors, including mutual funds and ETFs. These include a fiduciary duty, limits on leverage, custody requirements, corporate governance requirements, prohibitions on conflicted practices, restrictions on fees and expenses chargeable to investors, and examination by the SEC. The use of terms such as "Fund" or "ETF" imply that the full protections of the Investment Company Act would apply, but unfortunately, they do not.

We appreciate that these ETPs have several basic investor protections, which apply to any security that is registered with the SEC. These include public disclosure of risks and conflicts of interest, as well as general prohibitions on fraud and manipulation. However, retail investors should be made aware of how the ETPs differ from more common funds with which they may have experience.

We urge the SEC to take several specific steps under its existing authority to address these issues: (1) carefully scrutinize brokers' and advisers' communications regarding bitcoin ETPs to ensure investors receive complete and accurate information about these products; (2) examine brokers and advisers that recommend cryptocurrency ETPs to ensure they are, in fact, acting in the best interests of their clients, as required by SEC rules; and (3) ensure that bitcoin ETPs do not use inappropriate and confusing naming conventions in SEC filings and other investor documents. These steps would help protect investors from fraud and abuse, which may be enabled by the current light-touch regulatory regime applicable to bitcoin ETPs.

Finally, we believe the SEC should strictly limit the precedential application of these approvals. While the bitcoin market has displayed serious weaknesses, it is nonetheless far more established and scrutinized than the market for any other cryptocurrency. However vulnerable bitcoin may be to fraud and manipulation, markets for other cryptocurrencies are far more exposed to misconduct.

We do not believe that other cryptocurrencies show the trading volumes or integrity to support associated ETPs. Nor do we believe that markets for futures on other cryptocurrencies are likely to demonstrate the tight correlation with spot markets that would enable meaningful market surveillance to deter and detect bad actors.

Retail investors would face enormous risks from ETPs referencing thinly traded cryptocurrencies or cryptocurrencies whose prices are especially susceptible to pump-and-dump or other fraudulent schemes. The Commission is under no obligation to approve such products, and given the risk, it should not do so.

Thank you for your attention to this matter and we look forward to your response.

Sincerely,

Jack Reed
United States Senator

Laphonza Butler
United States Senator