

Subject: File No. SR-NYSEArca-2019-01
From: SAM AHN

This comment is my 12th on bitcoin and my 2nd at this proposal. All my writings on bitcoin, including this, are somehow related to intrinsic value. My previous comments can be found at these links:

- Link 1: <https://www.sec.gov/comments/sr-cboebzx-2018-040/srcboebzx2018040-4206251-172835.htm>
- Link 2: <https://www.sec.gov/comments/sr-nysearca-2017-139/nysearca2017139-4221685-172898.htm>
- Link 3: <https://www.sec.gov/comments/sr-cboebzx-2018-001/cboebzx2018001-4226785-172988.htm>
- Link 4: <https://www.sec.gov/comments/sr-nysearca-2018-02/nysearca201802-4240462-173003.pdf>
- Link 5: <https://www.sec.gov/comments/sr-cboebzx-2018-040/srcboebzx2018040-4274529-173133.pdf>
- Link 6: <https://www.sec.gov/comments/sr-cboebzx-2018-040/srcboebzx2018040-4530331-176071.pdf>
- Link 7: <https://www.sec.gov/comments/sr-cboebzx-2018-001/cboebzx2018001-4581773-176242.pdf>
- Link 8: <https://www.sec.gov/comments/sr-cboebzx-2019-004/srcboebzx2019004-4934624-178449.pdf>
- Link 9: <https://www.sec.gov/comments/sr-cboebzx-2019-004/srcboebzx2019004-5180412-183546.pdf>
- Link 10: <https://www.sec.gov/comments/sr-cboebzx-2019-004/srcboebzx2019004-5318047-183890.pdf>
- Link 11: <https://www.sec.gov/comments/sr-nysearca-2019-01/srnysearca201901-5524009-185228.pdf>

This one is a rebuttal to another comment dated 06/11/2019, and its main body is reports on my surfing to regulatory agencies. I made the surfing in search of a regulatory feature which I will detail later under the first **red headline**, in response to the Applicants' comment at Link 12 hereunder:

Link 12: <https://www.sec.gov/comments/sr-nysearca-2019-01/srnysearca201901-5661639-185789.pdf>

The Applicants' comment at Link 12 above was their answer to a question in Release No. 34-85854 dated May 14, 2019 at Link 13 hereunder:

Link 13: <https://www.sec.gov/rules/sro/nysearca/2019/34-85854.pdf>

The Commission's question mentioned in the preceding paragraph is:

(Quote 1) To what extent, if at all, do recent developments in the bitcoin futures market—namely, the cessation of new bitcoin futures contract trading on the Chicago Futures Exchange—affect commenters' analysis of these questions?

I am not answering this question. I am arguing against the Applicant's presumption, which is the critical link in the logic of Link 13 above: that bitcoin futures market is a regulated market. Said presumption is seen, for example, in the following argument:

(Quote 2) In the Winklevoss Order⁴, the SEC laid two pathways by which a bitcoin ETF could satisfy the requirements of Exchange Act 6(B)(5), which focuses on market

manipulation. One of those pathways was for the listing exchange of the ETF to enter into a surveillance sharing agreement with a regulated market of significant size.

Bitwise has argued in multiple documents filed with the SEC, including “Economic and Non-Economic Trading in Bitcoin: Exploring the Real Spot Market for the World’s First Digital Commodity,” a white paper submitted to the SEC on May 24, 2019 (the “Bitwise White Paper”),⁵ that the **regulated bitcoin futures market** satisfies this requirement.

I am opposed to the presumption that bitcoin futures market is regulated, because bitcoin futures market is not regulated with all the regulatory features required, in the context of surveillance sharing agreement, by the SEC.

The Regulatory Feature required by the SEC

The SEC regulates security futures as to what the base securities (underlying the futures) are, besides how the security futures are being traded. This regulatory feature is mandated by Securities Act of 1933, as summarized at Link 14 below:

Link 14 (the SEC): <https://www.sec.gov/answers/about-lawsshtml.html#secact1933>

(Quote 3) Often referred to as the “truth in securities” law, the Securities Act of 1933 has two basic objectives: • requires that investors receive financial and other significant **information concerning securities** being offered for public sale and • prohibit deceit, misrepresentations, and other fraud in the sale of securities.

The SEC’s regulation is all about disclosure, which should be truthful without deceits, misrepresentations or other fraud about **what it is.**

Securities, including ETF’s and security futures, can be based on debts, businesses or commodities. The value of a debt instrument comes from owing by the issuer. The value of an ownership share comes from performance of the business it represents. The value of a commodity comes, for example, from its utility and scarcity. Most of the time, the utility of a commodity is so apparent that nobody is interested in any disclosure about it.

What is special with bitcoin is that its value is not easily recognizable. As bitcoin is a commodity, its value may have to come from, for example, its utility and scarcity. We all know its scarcity, but where is its utility? If not utility, where does the value of bitcoin come from? A regulation without a good answer to these questions cannot meet the requirements in Quote 3 above.

Bitcoin’s utility is often said to be its function as money, but the applicants did not say it. Instead, they introduced us to literatures and regulatory agencies. I reported my surfing to the literatures in Links 7, 8 and 11 above. Now, I am reporting my surfing to regulatory agencies.

Regulatory Agency 1: the CFTC over bitcoin futures

The Applicants of this proposal, in their letter at Link 12 above, presumed that bitcoin futures were regulated. They did not tell how and by whom those bitcoin futures are being regulated, but we know that the CFTC regulates bitcoin futures traded in two or so exchanges. Let's have a look at the way the CFTC regulates bitcoin futures:

Link 15: https://www.cftc.gov/sites/default/files/idc/groups/public/@newsroom/documents/file/bitcoin_factsheet120117.pdf

The document at Link 15 above starts with:

(Quote 4) On Friday, December 1, 2017, the Chicago Mercantile Exchange Inc. (CME) and the CBOE Futures Exchange (CFE) **self-certified** new contracts for bitcoin futures products and the Cantor Exchange **self-certified** a new contract for bitcoin binary options.

The meaning of self-certification is explained here:

Link 16: <https://www.cftc.gov/IndustryOversight/ContractsProducts/ListingProcedures/index.htm>

(Quote 5) 17 CFR 40.2 permits designated contract markets (DCMs) to list products for trading **without prior CFTC approval** by filing a written self-certification with the CFTC.

Quote 5 is based on Commodity Exchange Act (CEA), which is a part of Title 7 of USC (Agriculture). Chapter 1 of the title is about "Commodity Exchanges," of which definition part is 7 USC 1a. The definition of 'Commodity trading advisor' reads:

(Quote 6) 7 USC 1a(12)(D) Advisors: The Commission, by rule or regulation, may include within the term "commodity trading advisor", any person advising **as to the value of commodities or issuing reports or analyses concerning commodities** if the Commission determines that the rule or regulation will effectuate the purposes of this paragraph.

The underlined part may mean that, the CFTC has an advisor who can explain the value of bitcoin. But what is said in the document at Link 17 hereunder is quite disappointing.

Link 17: <https://www.cftc.gov/PressRoom/PressReleases/pr7654-17>

(Quote 7) As with all contracts offered through Commission-regulated exchanges and cleared through Commission-regulated clearinghouses, the completion of the processes described above is not a Commission approval. **It does not constitute a Commission endorsement of the use or value of virtual currency products or derivatives.** It is incumbent on market participants to conduct appropriate due diligence to determine the particular appropriateness of these products, which at times have exhibited extreme volatility and unique risks.

The underlined part of Quote 7 is a disclaimer. The law of Quote 6 above did not mandate the CFTC to examine the value of a commodity. The CFTC may be incapable of finding the value of bitcoin. We don't know who else on earth is capable of it. Bitcoin is something new, and we do not have a law that can be called something like "Commodities Act," in parallel with "Securities Act of 1933," to tell us how we can trace the source of bitcoin's value – its utility or something else.

The CFTC did say something about what bitcoin is, in Page 2 of the document at Link 15 above, but it is not out of the thoughts of the CFTC. It is an excerpt from IRS Notice 2014-21:

(Quote 8) Although precise definitions on virtual currency offered by others are varied, an IRS definition provides us with a general idea: • "Virtual currency is a digital representation of value that functions as a medium of exchange, a unit of account, and/or a store of value. • In some environments, it operates like 'real' currency . . . but it does not have legal tender status [in the U.S.]. • Virtual currency that has an equivalent value in real currency, or that acts as a substitute for real currency, is referred to as 'convertible' virtual currency. Bitcoin is one example of a convertible virtual currency. • Bitcoin can be digitally traded between users and can be purchased for, or exchanged into, U.S. dollars, Euros, and other real or virtual currencies."

Three places in Quote 6 drew my attention. First, was it how the IRS defined bitcoin? Second, was there "or" in the original document? Third, did the IRS think bitcoin could ever have legal tender status outside of the US?

Regulatory Agency 2: the IRS behind the CFTC

With those question above in mind, I looked for the original IRS document:

Link 18 (IRS): https://www.irs.gov/irb/2014-16_IRB#NOT-2014-21

The IRS said something like Quote 6 above, but it did not define that way. In Notice 2014-21, the IRS said:

(Quote 9) The Internal Revenue Service (IRS) is aware that "virtual currency" may be used to pay for goods or services, or held for investment.

Virtual currency is a digital representation of value that functions as a medium of exchange, a unit of account, and/or a store of value. In some environments, it operates like "real" currency — i.e., the coin and paper money of the United States or of any other country that is designated as legal tender, circulates, and is customarily used and accepted as a medium of exchange in the country of issuance—but it does not have legal tender status in any jurisdiction.

Virtual currency that has an equivalent value in real currency, or that acts as a substitute for real currency, is referred to as "convertible" virtual currency. Bitcoin is one example of a

convertible virtual currency. Bitcoin can be digitally traded between users and can be purchased for, or exchanged into, U.S. dollars, Euros, and other real or virtual currencies.

For a more comprehensive description of convertible virtual currencies to date, see **Financial Crimes Enforcement Network (FinCEN)** *Guidance on the Application of FinCEN's Regulations to Persons Administering, Exchanging, or Using Virtual Currencies* (FIN-2013-G001, March 18, 2013).

The expression “or” was correctly transferred, making both agencies correct to the extent that bitcoin cannot function as a medium of exchange and a unit of account at the same time. I wrote on this point at Link 5 at the beginning of this comment. It is also linked hereunder, for easier reading.

Link 5: <https://www.sec.gov/comments/sr-cboebzx-2018-040/srcboebzx2018040-4274529-173133.pdf>

More specifically, however, bitcoin cannot be a unit of account. I wrote in this point at Link 6 above and hereunder, by showing nine examples of money creation.

Link 6: <https://www.sec.gov/comments/sr-cboebzx-2018-040/srcboebzx2018040-4530331-176071.pdf>

Therefore, IRS Notice 2014-21 could have been more useful had it not been for “**a unit of account,**” in Quote 9 above.

Next, the CFTC failed to transfer IRS wording about the jurisdiction. The IRS said that bitcoin is not a legal tender “in any jurisdiction.” Not that it is not a legal tender (only) in the U.S. On this point, the IRS was correct, but the CFTC was not confident.

Lastly, the CFTC failed to catch that the IRS was not defining bitcoin with Notice 2014-21. The notice was written for the purpose of deciding how to tax bitcoin-related transactions.

(Quote 10) This notice describes how existing general tax principles apply to transactions using virtual currency. The notice provides this guidance in the form of answers to frequently asked questions.

Then, in Page 2 of Link 18 above, the IRS implies that **bitcoin is not money**:

(Quote 11) Under currently applicable law, virtual currency is not treated as currency that could generate foreign currency gain or loss for U.S. federal tax purposes.

The IRS was not interested in defining bitcoin. Rather, it passed the burden of telling **what bitcoin is** to the FinCEN, as underlined in Quote 9 above.

Regulator 3: the FinCEN behind the IRS

The applicants of this proposal, in Page 20 of Release No. 34-85854, listed the regulatory actions of the FinCEN like this:

(Quote 12) For instance, the nine exchanges that are regulated by the U.S Department of Treasury's FinCEN division as Money Services Businesses are charged with various responsibilities including:

- Identifying people with ownership stakes or controlling roles in the MSB;
- Establishing a formal Anti-Money Laundering (AML) policy in place with documentation, training, independent review, and a named compliance officer;
- Having strict customer identification and verification policies and procedures;
- Filing Suspicious Activity Reports (SARs) for suspicious customer transactions;
- Filing Currency Transaction Reports (CTRs) for cash-in or cash-out transactions greater than \$10,000; and
- Maintaining a five-year record of currency exchanges greater than \$1,000 and money transfers greater than \$3,000.

Those six points enumerated above can be called regulation, but none of them, again, is about **what bitcoin is**. The FinCEN does not regulate anything about what bitcoin is, even in its new Guidance issued in May 2019:

Link 19: <https://www.fincen.gov/sites/default/files/2019-05/FinCEN%20Guidance%20CVC%20FINAL%20508.pdf>

Rather, the FinCEN clarifies what bitcoin is **not**. In Page 7 of the Guidance at Link 19 above, it clarifies that it is not money:

(Quote 13) The term "virtual currency" refers to a medium of exchange that can operate like currency but **does not have all the attributes of "real" currency, as defined in 31 CFR 1010.100(m), including legal tender status**. CVC is a type of virtual currency that either has an equivalent value as currency, or acts as a substitute for currency, and is therefore a type of "value that substitutes for currency."

The underlined part points out deficiencies of bitcoin as a money, "including" absence of legal tender status. This implies that there are some other deficiencies. We can find another deficiency in the text of the reference law:

(Quote 14) 31CFR 1010.100(m) Currency. The coin and paper money of the United States or of any other country that is designated as legal tender and that circulates and is customarily used and accepted as a medium of exchange **in the country of issuance**. Currency includes U.S. silver certificates, U.S. notes and Federal Reserve notes. Currency also includes official foreign bank notes that are customarily used and accepted as a medium of exchange in a foreign country.

The underlined five words draws our attention because bitcoin does not have a country of issuance. This is a crucial deficiency in comparison to regular fiat monies. Federal Reserve notes are obligations of the US under 12 USC 411. Bitcoins are nobody's obligations of any country. That makes a big difference between bitcoin and regular currencies.

The FinCEN is clear about what bitcoin is not. It looks not interested in what it is.

A Precedent Theory: Bitcoin Futures vs. Dry Bulk Freight Futures

While the Applicants of this proposal hang on regulated-ness of bitcoin futures market, the applicants of another proposal (SR-CboeBZX-2019-004) hang on a "precedent" called Dry Bulk Freight Futures. Quote 15 below is from Page 8 of Release No. 34-85119 at Link 20 hereunder:

Link 20 (Release 34-85119) : <https://www.sec.gov/rules/sro/cboebzx/2019/34-85119.pdf>

(Quote 15): Looking(Subject) at the limited instances in which the Commission has included in the record for an approval order an affirmative statement about a "significant regulated market" provides(Verb) some insight(Object 1), but very little specificity(Object 2) as to how the standard is applied to proposals that are approved. Of particular interest is the approval order for the Breakwave Dry Bulk Shipping ETF (the "Shipping Futures ETF") which is designed to provide exposure to the daily change in the price of dry bulk freight futures: an ETP that provides exposure to a unique underlying instrument with no direct precedent for approval.

The first sentence is difficult to comprehend. As my misunderstanding of that sentence can lead me to an erroneous argument, I had to clarify how I understood it by inserting the sentence elements in the parentheses. It looks to me like saying "Looking at something provides some insight but very little specificity," I can be wrong with that.

The background of dry bulk freight futures is explained at Link 21 below:

Link 21 (DAT): <https://www.oceanfinance.gr/wp-content/uploads/The-development-of-shipping-related-derivatives-markets-in-Shanghai-Pudong-excl.-Authors.pdf>

Now we find that dry bulk freight futures are based on prices of standardized units of transportation services. As the value of transportation service has been known to us for many thousand years, there is no issue as to what dry bulk freight is. Therefore, dry bulk freight futures will no way be precedent to bitcoin futures.

Conclusion

A few regulatory agencies were somehow regulating the trading and/or using bitcoin or bitcoin futures, I could not find any agency regulating about the disclosure of **what bitcoin is**. The source of its value is still unknown to us. Bitcoin futures market cannot be deemed regulated enough to meet the requirements in Quote 3 above.