

April 18, 2022

Re: File No. SR-NYSEArca-2021-90

Rel. No. 34-93504

Notice of Filing of Proposed Rule Change to List and Trade Shares of Grayscale Bitcoin Trust (BTC) under NYSE Arca Rule 8.201-E

(November 2, 2021)

Ms. Vanessa Countryman  
Secretary  
Securities and Exchange Commission  
100 F Street NE  
Washington, DC 20549-0609

Dear Ms. Countryman:

On behalf of our client Grayscale Investments, LLC, sponsor of the Grayscale Bitcoin Trust (BTC), we write in response to a recent development that bears on the Commission's consideration of the above-referenced proposal to list shares of BTC under NYSE Arca Rule 8.201-E.

On April 6, 2022, the Commission, by the Division of Trading and Markets acting pursuant to delegated authority, approved NYSE Arca's proposal to list and trade shares of the Teucrium Bitcoin Futures Fund,<sup>1</sup> an exchange-traded product ("ETP") not registered under the Investment Company Act of 1940 (as amended, the "1940 Act"). The Teucrium ETP invests exclusively in Bitcoin futures contracts traded on the Chicago Mercantile Exchange, Inc. ("CME"),<sup>2</sup> and the related approval order is the first time the Commission has approved a Bitcoin ETP and expressly determined that listing the product is consistent with the requirements of Section 6(b)(5) of the Securities Exchange Act of 1934 (as amended, the "Exchange Act").<sup>3</sup>

We believe the Teucrium order confirms the fundamental point made in our November 29, 2021 letter in support of the above-referenced proposal: when it comes to approving ETPs, there is no basis for treating spot Bitcoin products differently from Bitcoin futures products.<sup>4</sup>

*First*, the Teucrium order confirms that 1940 Act registration is not a basis for the Commission to approve one product and reject another.<sup>5</sup> As we discussed in our November 2021 letter, the Commission has never

<sup>1</sup> Order Granting Approval of a Proposed Rule Change, as Modified by Amendment No. 2, to List and Trade Shares of the Teucrium Bitcoin Futures Fund under NYSE ARCA Rule 8.200-E, Commentary .02 (Trust Issued Receipts), Securities Exchange Act Release No. 94620 (Apr. 6, 2022), 87 Fed. Reg. 21,676 (Apr. 12, 2022) (SR-NYSEArca-2021-53) ("Teucrium Order").

<sup>2</sup> *Id.* at 21,676 & n.9; *id.* at 21,678.

<sup>3</sup> *Id.* at 21,677-78, 21,684.

<sup>4</sup> Letter from Davis Polk & Wardwell LLP on behalf of Grayscale Investments, LLC to Vanessa Countryman, Sec'y, SEC, at 1 (Nov. 29, 2021) (our "November 2021 letter"), <https://www.sec.gov/comments/sr-nysearca-2021-90/smysearca202190-9410842-262990.pdf>.

<sup>5</sup> See *id.* at 9-11.

explained why 1940 Act registration should matter for purposes of approving a Bitcoin ETP under Exchange Act § 6(b)(5).<sup>6</sup> The Teucrium order makes clear that it does not.

*Second*, the Teucrium order shows that Bitcoin futures products and spot Bitcoin products face identical risks from fraud and manipulation of Bitcoin prices. As we observed in our November 2021 letter, the reference rate for the CME Bitcoin futures market and the pricing indices that BTC and other spot Bitcoin products use to value their shares are based on the same data: trading prices reported on the same Bitcoin trading platforms.<sup>7</sup> Because both spot and futures-based Bitcoin products face exposure to the same underlying Bitcoin market,<sup>8</sup> any fraud or manipulation in the underlying market will affect both products in the same way. The existence of these risks therefore cannot serve as justification for denying approval to one product once approval for the other product has been granted.

The Teucrium order reflects plainly the Commission's recognition that the CME bitcoin futures market is not insulated from potential risks of fraud and manipulation in the underlying Bitcoin market. In approving the Teucrium ETP, the Commission took pains to "disagree[] with much of [NYSE] Arca's reasoning" about the Bitcoin futures market's separation from the underlying Bitcoin market.<sup>9</sup> The Teucrium order explicitly rejected arguments that Bitcoin futures prices "are not specifically materially influenced by other [B]itcoin markets" or that there is a "lack of connection between the CME [B]itcoin futures contracts and spot [B]itcoin trading platforms."<sup>10</sup> To the contrary, per the order, "the Commission is not persuaded that the market for CME [B]itcoin futures contracts 'stands alone,' has a 'lack of connection' with, and is 'not specifically materially influenced' by, other [B]itcoin markets; nor that it is 'the primary, if not the lone determinant, of its valuation.'"<sup>11</sup> The order likewise rejects the suggestion that the Teucrium ETP's net asset valuation formula "insulates the NAV from activity in other [B]itcoin markets, given that there is nothing that prevents the trade prices that contribute to the daily settlement price from themselves being influenced by activity in other [B]itcoin markets."<sup>12</sup>

Nevertheless, the Commission approved the Teucrium proposal after finding that doing so is consistent with Exchange Act § 6(b)(5)'s standards—including the prevention of fraud and manipulation. Having determined that any potential risks of fraud and manipulation in the underlying Bitcoin markets do not preclude approval of the Teucrium ETP, the Commission cannot now justify disapproving the BTC ETP proposal. The Commission's prior disapprovals of spot Bitcoin ETPs have not identified any distinct and significant additional risk of fraud and manipulation that is somehow specific to spot Bitcoin ETPs, and none exists.<sup>13</sup>

And, of course, Section 6(b)(5) also prohibits exchanges from having rules that "permit unfair discrimination" between issuers.<sup>14</sup> NYSE Arca, the listing exchange for Teucrium, also seeks to list BTC. A

<sup>6</sup> November 2021 letter, *supra* note 4, at 10-11.

<sup>7</sup> *Id.* at 7 & n. 51.

<sup>8</sup> *Id.* at 11.

<sup>9</sup> Teucrium Order, 87 Fed. Reg. at 21,679.

<sup>10</sup> *Id.* (cleaned up).

<sup>11</sup> *Id.* at 21,680.

<sup>12</sup> *Id.*

<sup>13</sup> Indeed, Section 19 of the Exchange Act itself forecloses the Commission from disapproving the BTC proposal based on any risks of fraud and manipulation in the Bitcoin spot market. Under Section 19, the "Commission shall approve" an exchange's proposed rule change if it finds that the proposed change is consistent with Exchange Act requirements. 15 U.S.C. § 78s(b)(2)(C)(i). In light of the Teucrium order's finding that any spot market risks of fraud and manipulation do not render a Bitcoin ETP listing proposal inconsistent with the Exchange Act, the Commission has no discretion to disapprove BTC on that basis. *see, e.g., Ass'n of Civilian Technicians, Mont. Air Ch. No. 29 v. Fed. Labor Rels. Auth.*, 22 F.3d 1150, 1153 (D.C. Cir. 1994) ("The word 'shall' generally indicates a command that admits of no discretion on the part of the person instructed to carry out the directive.").

<sup>14</sup> 15 U.S.C. § 78f(b)(5); *see also* November 2021 letter, *supra* note 4, at 8-9.

Commission order disapproving the *same exchange's* application to list BTC over concerns with the underlying Bitcoin market would create the unfair discrimination that Section 6(b)(5) prohibits.<sup>15</sup>

*Third*, and finally, the Teucrium order shows that the “significant market” test does not effectively advance Exchange Act interests and therefore should be retired.

In evaluating various applications to list spot Bitcoin ETPs, the Commission has taken the position that to comply with Section 6(b)(5), the exchange generally must demonstrate that it has “a comprehensive surveillance-sharing agreement with a regulated market of significant size related to the underlying or reference [B]itcoin assets.”<sup>16</sup> As we discussed in our November 2021 letter, the Commission’s reluctance to quantify the size a market must achieve to be “significant,” and its reluctance to articulate discernible standards for determining whether the market has the requisite linkage to the ETP’s assets, renders this test subjective, arbitrary and effectively unachievable.<sup>17</sup> But even setting aside these flaws, the Commission’s approach to the “significant market” test in the Teucrium order shows that the test does not further the basic purpose of Section 6(b)(5) of the Exchange Act: ensuring that exchange rules are “designed to prevent fraudulent and manipulative acts and practices.”

The Commission determined that the CME is a “significant market” for the Teucrium ETP because all of its futures contracts trade on the CME.<sup>18</sup> In the words of the order, the CME “is the *same* market on which these assets trade”<sup>19</sup>—meaning that the “significant market” test is little more than a tautology when it comes to an ETP investing in derivatives that trade in a market regulated by the Commodity Futures Trading Commission. Despite extensive discussion of the Commission’s view that the Bitcoin futures market is exposed to risks of fraud and manipulation in the underlying Bitcoin market, the order sets those concerns aside merely because of the presence of another regulator—a regulator whom the Commission has observed does not meaningfully regulate the underlying Bitcoin market.<sup>20</sup> In defining the relevant market as the CME and determining that this satisfies the “significant market” test, the order simply accepts that CFTC regulation is an adequate answer to the question of whether the rules of the exchange are designed to prevent fraudulent and manipulative acts and practices. And the order does so, despite the Commission having made clear in other contexts that CFTC regulation does not apply Exchange Act standards or substitute for the Commission’s own broader regulatory authority.<sup>21</sup>

Applying the “significant market” test in this manner therefore allows the Commission to sidestep the actual question: whether approving an exchange’s proposal to list an ETP is consistent with the factors laid out in Exchange Act § 6(b)(5). Agency action is arbitrary and capricious “if the agency has relied on factors which Congress has not intended it to consider, entirely failed to consider an important aspect of the problem, [or] offered an explanation for its decision that runs counter to the evidence before the agency.”<sup>22</sup> If NYSE Arca’s BTC proposal were disapproved based on the “significant market” test, without an independent evaluation of the proposal’s compliance with Section 6(b)(5) in light of the Teucrium ETP’s satisfaction of

<sup>15</sup> The Administrative Procedure Act prohibits agencies not only from acting in an “arbitrary and capricious” manner, but also from acting, among other things, “not in accordance with law” or “in excess of statutory . . . authority[] or limitations.” 5 U.S.C. § 706(2).

<sup>16</sup> November 2021 letter, *supra* note 4, at 6 (citation omitted). The Commission has also stated that an exchange could satisfy the requirements of Section 6(b)(5) if it could show that the underlying market were “inherently” or “uniquely” resistant to manipulation. *Id.* As we explained previously, this alternate inquiry is effectively standardless and no exchange has ever made the required showing to the Commission’s satisfaction. *Id.* at 6-7, 13.

<sup>17</sup> *See id.* at 5-7, 12-13.

<sup>18</sup> Teucrium Order, 87 Fed. Reg. at 21,678.

<sup>19</sup> *Id.* at 21,678-79.

<sup>20</sup> *See* November 2021 letter, *supra* note 4, at 11-12 & nn. 78-79.

<sup>21</sup> *See id.*

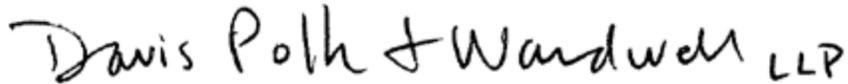
<sup>22</sup> *Motor Vehicle Mfrs. Ass’n of U.S., Inc. v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983); *see* 5 U.S.C. § 706(2)(A).

the statutory standard, we believe the action would be inconsistent with the requirements of both the Exchange Act and the Administrative Procedure Act.

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For the reasons set forth above and in our November 2021 letter, we respectfully request that the Commission approve NYSE Arca's proposal to list and trade BTC.

Very truly yours,

A handwritten signature in black ink that reads "Davis Polk & Wardwell LLP". The signature is written in a cursive, professional style.

Davis Polk & Wardwell LLP

Joseph A. Hall

Paul S. Mishkin

Zachary J. Zweihorn

Daniel J. Schwartz