

April 29, 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:

I write on behalf of Grayscale Investments, LLC, sponsor of the Grayscale Bitcoin Trust (BTC), in support of the proposal by NYSE Arca Inc. pursuant to Rule 19b-4 under the Securities Exchange Act of 1934 (as amended, the “Exchange Act”) to list shares of BTC under NYSE Arca Rule 8.201-E as an exchange-traded product (“ETP”).¹

The Commission has no basis for the position that investing in the derivatives market for an asset is acceptable for investors while investing in the asset itself is not. But having permitted the listing of multiple Bitcoin futures ETPs in the last several weeks, that is the policy decision the Commission would announce were it to deny NYSE Arca’s application to list BTC.

* * *

BTC holds Bitcoin valued at approximately \$39.7 billion as of October 29, 2021,² representing approximately 3.4% of outstanding Bitcoin and making BTC the largest Bitcoin investment fund in the world.³ Since September 2013, BTC has offered direct exposure to the Bitcoin spot market through a familiar and convenient product that does not burden investors with the risk and expense of direct digital asset custody and trading. BTC is a reporting issuer that has been subject to the requirements of Section 13 of the Exchange Act since January 2020.⁴ Because Bitcoin is not a “security” for purposes of the

¹ In this letter, we use the generic term “ETP” to cover exchange-traded investment vehicles that are required to register under the Investment Company Act of 1940 (as amended, the “1940 Act”), also commonly referred to as “exchange-traded funds” or “ETFs,” as well as those, like BTC, that are not subject to the registration requirements of the 1940 Act.

² Grayscale Investments, LLC, *Grayscale Bitcoin Trust Fact Sheet* at 2 (Nov. 2021) (“BTC Fact Sheet”), <https://grayscale.com/wp-content/uploads/2021/11/GBTC-Trust-Fact-Sheet-November-2021.pdf>.

³ Based on Bloomberg L.P. terminal search for AUM of all “Bitcoin Funds.”

⁴ See BTC Fact Sheet at 1; see also Grayscale Bitcoin Trust, Am. No. 1 to Registration Statement on Form 10 (Form 10-12G/A), at 2 (Dec. 31, 2019); Notice of Filing of Proposed Rule Change to List and Trade Shares of Grayscale Bitcoin Trust (BTC) under NYSE Arca Rule 8.201-E, Securities and Exchange Act Release 93504 (Nov. 2, 2021), 86 Fed. Reg. 61,804, 61,805 n.7 (Nov. 8, 2021) (SR-NYSEArca-2021-90) (the “Proposal”).

Investment Company Act of 1940 (as amended, the “1940 Act”), BTC is neither required nor eligible to register as an investment company under the 1940 Act.⁵

Shares of BTC are currently offered to accredited investors within the meaning of Regulation D under the Securities Act of 1933 (as amended, the “Securities Act”).⁶ Once such investors have held their shares for the requisite holding period pursuant to Rule 144 under the Securities Act, they have the ability to resell them through transactions on the OTCQX Best Market (“OTCQX”), an over-the-counter marketplace operated by OTC Markets Group that is not registered with the Commission as a national securities exchange.⁷ Shares of BTC have been quoted on OTCQX since March 2015,⁸ and in the 12 months ended October 31, 2021, trading in BTC shares accounted for more transactions, by dollar volume, than any other security so quoted.⁹ Today, BTC shares are available to investors through broker transactions and are held in more than 600,000 retail and institutional brokerage accounts in all 50 states.¹⁰

Despite BTC’s appeal and wide availability, it is not yet eligible to offer continuous share redemptions and creations, which is the mechanism ETPs employ to align share trading prices with underlying asset prices. As a result, BTC shares usually trade at discounts below or premiums over the net asset value of the Bitcoin it holds, and these discounts and premiums have at times been substantial.¹¹

In order to operate BTC as a traditional ETP with minimal variations between share trading prices and the value of its Bitcoin holdings, Grayscale has sought for several years to list its shares on NYSE Arca. NYSE Arca first filed a Rule 19b-4 application for this purpose in 2017, but voluntarily withdrew it after the Commission rejected similar applications on bases that Grayscale and NYSE Arca determined were likely applicable to BTC.¹²

Amid signs of an evolution in the Commission’s thinking on Bitcoin-related products, NYSE Arca filed the pending Rule 19b-4 application on October 19, 2021.¹³ But three weeks later, on November 12, 2021, the Commission, by the Division of Trading and Markets acting pursuant to delegated authority,¹⁴ disapproved another national securities exchange’s Rule 19b-4 application to list shares of a competing spot Bitcoin

⁵ See, e.g., Letter from Brent J. Fields, Assoc. Dir., Disclosure Rev. and Acct. Off., SEC, to Jacob E. Comer, Cipher Techs. Mgmt. LP, at 1 (Oct. 1, 2019), <https://www.sec.gov/Archives/edgar/data/1776589/999999999719007180/FILENAME1.PDF> (disagreeing that Bitcoin is a security and stating that “because [the fund] intends to invest substantially all of its assets in bitcoin as currently structured, it does not meet the definition of an ‘investment company’ under the Investment Company Act and it has inappropriately filed on Form N-2”).

⁶ Grayscale Bitcoin Trust, Annual Report for the Fiscal Year Ended Dec. 31, 2020 (Form 10-K), at 1 (Mar. 5, 2021) (“BTC 2020 Annual Report”).

⁷ BTC 2020 Annual Report at 3, 66; see also *Fast Answers, National Securities Exchanges*, SEC (July 14, 2021), <https://www.sec.gov/fast-answers/divisionsmarketregmrexchangesshtml.html> (last visited Nov. 25, 2021) (not listing OTCQX on list of registered national securities exchanges).

⁸ Proposal, 86 Fed. Reg. at 61,805 n.7; BTC 2020 Annual Report at F-7.

⁹ *OTCQX Current Market – Most Active*, OTC Markets Group, Inc. (Nov. 26, 2021, 5:25 PM), <https://www.otcmkt.com/market-activity/current-market/QX/active/dollarVolume>.

¹⁰ Broadridge Financial Solutions, Inc. share range analysis conducted by Grayscale for BTC, finding approximately 630,000 account holders as of September 30, 2021, as cited in the Letter from Congressmen Tom Emmer and Darren Soto to Chair Gensler (Nov. 3, 2021) https://emmer.house.gov/_cache/files/b/6/b6170d87-c56c-40a3-960a-60a619c02b65/63C9D652A62FF6119A2D0B117D655732.congressional-letter-to-sec-on-bitcoin-etfs.pdf; see also *SDBA Indicators Q3 2021 Report 4*, Charles Schwab (Sept. 30, 2021), <https://workplacefinancialservices.schwab.com/resource/sdba-indicators-q3-2021-report>.

¹¹ From May 5, 2015 to October 31, 2021, the maximum single-day premium of the closing price of BTC shares quoted on OTCQX over the value of its Bitcoin holdings was 142% and the average of all daily premiums was 37%; the maximum single-day discount below the value of its Bitcoin holdings was 21% and the average of all daily discounts was 12%; and the average of all single-day premiums and discounts was a premium of 32%. See Grayscale Bitcoin Trust, Quarterly Report for the Quarter Ended Oct. 31, 2021 (Form 10-Q), at 19-20 (Nov. 5, 2021).

¹² BTC 2020 Annual Report at 52; see also, e.g., Order Disapproving a Proposed Rule Change, as Modified by Amendment No. 1, Relating to the Listing and Trading of Shares of the SolidX Bitcoin Trust Under NYSE Arca Equities Rule 8.201, Securities Exchange Act Release No. 80319 (Mar. 28, 2017), 82 Fed. Reg. 16,247 (Apr. 3, 2017) (SR-NYSEArca-2016-101) (“SolidX Order”).

¹³ Proposal, 86 Fed. Reg. at 61,805.

¹⁴ The Commission has exercised its authority under Rule 431 of the Rules of Practice to review the Division’s decision. See Letter from J. Matthew DeLesDernier, Assistant Sec’y, Commission, to K. Murray, V.P. & Assoc. Gen. Counsel, Cboe Global Mkts, at 1 (Nov. 12, 2021), <https://www.sec.gov/rules/sro/cboebzx/2021/34-93559-20211112-cboebzx-order-disapproving-a-proposed-rule-change.pdf>. For the reasons set forth herein, we respectfully urge the Commission to reverse the Division’s decision concurrently with its approval of NYSE Arca’s pending Proposal.

ETP, stating that it had not found the other exchange's proposal to be consistent with the requirements of the Exchange Act and the rules and regulations thereunder.¹⁵ Despite differences between the competing spot Bitcoin ETP and BTC,¹⁶ the rationale laid out in the Commission's November 12, 2021 disapproval order could be applied to BTC. We believe this rationale failed adequately to take account of significant regulatory and competitive developments since 2017 when the Commission first considered, and denied, a national securities exchange's application to list and trade shares of a spot Bitcoin ETP.¹⁷ These developments include, most importantly, the Commission's recent decision to permit trading of ETPs registered under the 1940 Act that provide indirect exposure to Bitcoin through investments in the Bitcoin futures markets—the first of which began trading the same day NYSE Arca filed the pending Rule 19b-4 application.¹⁸

The Commission's prior disapprovals of Rule 19b-4 applications covering spot Bitcoin ETPs, including the November 12, 2021 disapproval order, were each premised on a conclusion that the listing exchange had not demonstrated that the risks of fraud and market manipulation in the underlying Bitcoin market were sufficiently addressable to permit the exchange to list a spot Bitcoin ETP consistent with its responsibilities under Section 6(b)(5) of the Exchange Act.¹⁹ That section requires that the listing exchange's rules be "designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, . . . and, in general, to protect investors and the public interest; and . . . not [be] designed to permit unfair discrimination between customers, issuers, brokers, or dealers[.]"²⁰ Although the Commission has articulated various showings a listing exchange could make, in theory, to meet its Section 6(b)(5) burden, as discussed below no exchange seeking to list a spot Bitcoin ETP has ever been able to satisfy the Commission's criteria.²¹

* * *

In the years since the Commission began denying Rule 19b-4 applications for spot Bitcoin ETPs, Bitcoin has exploded in popularity as an investment asset.²² Yet there remains no way for U.S. investors to gain access to the Bitcoin market through an ETP whose trading prices closely reflect spot Bitcoin trading prices. Until very recently, investors wishing to gain Bitcoin exposure in any form at all have had to invest directly by purchasing Bitcoin through digital asset trading platforms subject to varying degrees of consumer

¹⁵ Order Disapproving a Proposed Rule Change to List and Trade Shares of the VanEck Bitcoin Trust under BZX Rule 14.11(e)(4), Commodity-Based Trust Shares, Securities Exchange Act Release No. 93559 (Nov. 12, 2021), 86 Fed. Reg. 64,539 (Nov. 18, 2021) (SR-CboeBZX-2021-019) ("VanEck Order").

¹⁶ For example, BTC and the VanEck Bitcoin Trust use different index rates, based on data from differing groups of digital asset trading venues, to value their Bitcoin holdings.

¹⁷ SolidX Order, 82 Fed. Reg. at 16,247.

¹⁸ See *infra* note 49.

¹⁹ See, e.g., SolidX Order, 82 Fed. Reg. at 16,247 ("As discussed further below, the Commission is disapproving this proposed rule change because it does not find the proposal to be consistent with Section 6(b)(5) of the Exchange Act, which requires, among other things, that the rules of a national securities exchange be designed to prevent fraudulent and manipulative acts and practices and to protect investors and the public interest."); Order Setting Aside Action by Delegated Authority and Disapproving a Proposed Rule Change, as Modified by Amendments No. 1 and 2, To List and Trade Shares of the Winklevoss Bitcoin Trust, Securities Exchange Act Release No. 83723 (July 26, 2018), 83 Fed. Reg. 37,579, 37,604-05 (Aug. 1, 2018) (SR-BatsBZX-2016-30) ("Winklevoss Order") (similar); Order Disapproving a Proposed Rule Change To List and Trade the Shares of the GraniteShares Bitcoin ETF and the GraniteShares Short Bitcoin ETF, Securities Exchange Act Release No. 83913 (Aug. 22, 2018), 83 Fed. Reg. 43,923, 43,923 (Aug. 28, 2018) (SR-CboeBZX-2018-001) ("GraniteShares Order") (similar); Order Disapproving a Proposed Rule Change To List and Trade the Shares of the ProShares Bitcoin ETF and the ProShares Short Bitcoin ETF, Securities Exchange Act Release No. 83904 (Aug. 22, 2018), 83 Fed. Reg. 43,934, 43,935 (Aug. 28, 2018) (NYSEArca-2017-139) ("ProShares Order") (similar); Order Disapproving a Proposed Rule Change, as Modified by Amendment No. 1, To Amend NYSE Arca Rule 8.201-E (Commodity-Based Trust Shares) and To List and Trade Shares of the United States Bitcoin and Treasury Investment Trust Under NYSE Arca Rule 8.201-E, Securities Exchange Act Release No. 88284 (Feb. 26, 2020), 85 Fed. Reg. 12,595, 12,596 (Mar. 3, 2020) (SR-NYSEArca-2019-39) ("Wilshire-Phoenix Order") (similar); VanEck Order, 86 Fed. Reg. at 64,539 (similar).

²⁰ 15 U.S.C. § 78f(b)(5).

²¹ See *infra* § I.B.

²² See Raynor de Best, *Bitcoin price from October 2013 to November 19, 2021*, Statista (Nov. 19, 2021), <https://www.statista.com/statistics/326707/bitcoin-price-index/>.

protection regulation; to acquire indirect exposure through Bitcoin derivatives markets or perhaps through investing in operating companies active in the cryptocurrency space; or to invest through private placements or over-the-counter purchases of funds holding Bitcoin but whose shares trade at discounts or premiums to spot prices because they are not eligible to operate continuous creation and redemption programs.

In August 2021, the Commission began to signal a newfound willingness to permit Bitcoin futures ETPs registered under the 1940 Act to list shares on national securities exchanges,²³ and to date three ETPs have done so.²⁴ These ETPs are therefore able to offer retail and other investors indirect access to Bitcoin through the derivatives markets—*despite the derivatives markets' exposure to the identical risks of spot market fraud and manipulation that heretofore have stood in the way of Commission approval of spot Bitcoin ETPs.*

It is of course foundational that the Commission—like any other federal regulatory agency—must treat like situations alike absent reasoned justification;²⁵ indeed, this principle is reflected in the text of Section 6(b)(5) itself, which forbids exchanges from maintaining rules that unfairly discriminate between issuers. Bitcoin futures ETPs registered under the 1940 Act and spot Bitcoin ETPs that are not required or eligible to be so registered are the same in all relevant respects, but based on the analysis in the November 12, 2021 disapproval order, the Commission is treating them differently. Although the Commission cited investor protections afforded by the 1940 Act as justification for disparate treatment,²⁶ the 1940 Act's protections do not address and thus are not relevant to the concern the Commission has repeatedly invoked to deny Rule 19b-4 applications for spot Bitcoin ETPs like BTC: market manipulation and fraud in the underlying Bitcoin market.

In view of the Commission's new approach to Bitcoin futures ETPs, we believe that rejecting NYSE Arca's Rule 19b-4 application on grounds similar to those articulated in the November 12, 2021 disapproval order would unfairly discriminate against BTC and its shareholders in violation of Section 6(b)(5) of the Exchange Act and would constitute arbitrary and capricious action within the meaning of Section 706(2)(a) of the Administrative Procedure Act (as amended, the "APA").

We therefore respectfully urge the Commission to approve NYSE Arca's proposal to list and trade BTC.

I. Background

A. Grayscale Bitcoin Trust

BTC is the largest and most liquid Bitcoin investment fund in the world.²⁷ Shares of BTC have been quoted on the OTCQX since 2015.²⁸ BTC's sponsor, Grayscale Investments, LLC, is the world's largest digital currency asset manager, with more than \$55 billion in assets under management as of October 29, 2021 and an operational track record dating to September 2013.²⁹

²³ Gary Gensler, Chair, SEC, *Remarks Before the Aspen Security Forum*, SEC (Aug. 3, 2021), <https://www.sec.gov/news/public-statement/gensler-aspen-security-forum-2021-08-03>.

²⁴ ProShares Bitcoin Strategy ETF (BITO); VanEck Bitcoin Strategy ETF (XBTF); Valkyrie Bitcoin Strategy ETF (BTF).

²⁵ See *infra* note 57.

²⁶ See VanEck Order 86 Fed. Reg. at 64,552-53; see also Gensler, *supra* note 23 ("When combined with the other federal securities laws, the '40 Act provides significant investor protections. Given these important protections, I look forward to the staff's review of such filings, particularly if those are limited to these CME-traded Bitcoin futures.").

²⁷ Proposal, 86 Fed. Reg. at 61,815.

²⁸ *Id.* at 61,805 n.7, 61,815; BTC 2020 Annual Report at F-7; see also BTC Fact Sheet at 2.

²⁹ BTC Fact Sheet at 1.

BTC's shares are registered under Section 12(g) of the Exchange Act, and BTC is subject to ongoing public reporting requirements pursuant to Section 13 of the Exchange Act.³⁰ In accordance with its obligations as a public company, and as required by Commission rules, BTC regularly discloses material information to its investors through Commission filings. Because BTC's assets consist solely of Bitcoin, the proceeds from the sale of Bitcoin, and any related incidental rights arising from its Bitcoin holdings,³¹ none of which generally constitutes a security under the 1940 Act, BTC is not required, or even permitted, to register as an investment company under that Act.³²

BTC values its Bitcoin holdings based on the CoinDesk Bitcoin Price Index (XBX) (formerly known as the Tradeblock XBX Index), which draws price and volume data from multiple digital asset trading platforms satisfying the index provider's minimum standards for reliability and security³³ in order to generate representative pricing for the Bitcoin spot market while minimizing the impact of anomalous, fraudulent or manipulative trading activities occurring on individual platforms.³⁴ BTC makes available on its website information regarding its holdings and value, the price of its shares, and other quantitative data related to its assets.³⁵

BTC's investment objective is for the value of its shares to reflect the value of the underlying Bitcoin it holds, determined by reference to the XBX index, less expenses and other liabilities.³⁶ However, because BTC shares are not currently listed on a national securities exchange and BTC is therefore not permitted to operate an ongoing creation and redemption program, arbitrage opportunities resulting from differences between the price of the shares and the price of Bitcoin are not available to keep the price of BTC's shares closely linked to the XBX index price for Bitcoin.³⁷ As a result, BTC's shares are usually quoted on the OTCQX at a premium over, or discount to, the value of BTC's Bitcoin holdings.³⁸

B. The Commission's handling of spot Bitcoin ETP Rule 19b-4 applications

Responding to growing investor demand,³⁹ industry participants have for years been keenly focused on bringing spot Bitcoin ETPs to market. In order to accomplish this, a national securities exchange proposing to list and trade a spot Bitcoin ETP must obtain the Commission's approval of an application filed pursuant to Rule 19b-4. The NYSE Arca proposal that is the subject of this letter is the latest in a series of Rule 19b-4 applications that national securities exchanges have made to list and trade spot Bitcoin ETPs. However, proposals for spot Bitcoin ETPs have until now faced uniform failure at the Commission.⁴⁰

The Commission has explained its rejection of all prior Rule 19b-4 spot Bitcoin ETP applications as grounded in the requirements of Section 6(b)(5) of the Exchange Act, which "requires in relevant part that the rules of a national securities exchange must be designed 'to prevent fraudulent and manipulative acts

³⁰ *Id.*; see also *supra* note 4.

³¹ Proposal, 86 Fed. Reg. at 61,805.

³² See *supra* note 5.

³³ Proposal, 86 Fed. Reg. at 61,812, 61,819. These exchanges are referred to in the Proposal as "U.S.-Compliant Exchanges," which are defined as exchanges in the global exchange market for the trading of Bitcoins that hold themselves out as compliant with applicable U.S. federal and state licensing requirements and practices regarding AML and KYC regulations. *Id.* at 61,812 n.28.

³⁴ *Id.* at 61,813.

³⁵ *Id.* at 61,817.

³⁶ *Id.* at 61,805.

³⁷ See BTC 2020 Annual Report at 2-3, 21, 53.

³⁸ *Id.* at 2, 53; see also *id.* at 1-2; see also *supra* note 11.

³⁹ Telis Demos, *ETFs Could Rock the Bitcoin World*, Wall Street Journal (Apr. 12, 2021), <https://www.wsj.com/articles/etfs-could-rock-the-bitcoin-world-11618227019> (noting "indicators of big potential demand" for Bitcoin-linked ETPs).

⁴⁰ See *supra* note 19.

and practices,’ and ‘to protect investors and the public interest.’⁴¹ The Commission has stated that an exchange may demonstrate compliance with this statutory mandate by either:

- (1) entering into “a comprehensive surveillance-sharing agreement with a regulated market of significant size related to the underlying or reference bitcoin assets,”⁴² or
- (2) “establish[ing] that the underlying market inherently possesses a unique resistance to manipulation beyond the protections that are utilized by traditional commodity or securities markets,” although “[s]uch resistance . . . must be novel and beyond those protections that exist in traditional commodity markets or equity markets[.]”⁴³

Regarding the first method of demonstrating compliance with Section 6(b)(5), the Commission has not quantified how large a market must be to qualify as “significant,” and instead has defined the requirement in such a general and conclusory manner as to leave Rule 19b-4 applicants guessing about what evidence is necessary to gather and present to the Commission. In the Commission’s view, a “significant market” would “include a market (or group of markets) as to which (a) there is a reasonable likelihood that a person attempting to manipulate the ETP would also have to trade on that market to successfully manipulate the ETP, so that a surveillance-sharing agreement would assist in detecting and deterring misconduct, and (b) it is unlikely that trading in the ETP would be the predominant influence on prices in that market.”⁴⁴ When presented with evidence, the Commission has repeatedly found that the various spot Bitcoin markets proposed as “significant” do not meet this standard—either because those trading venues do not account for a sufficiently large volume of Bitcoin trading, or are insufficiently regulated, or both.⁴⁵ A number of national securities exchanges have proposed that trading in Bitcoin futures on the Chicago Mercantile Exchange (“CME”) qualifies as a “significant market” for purposes of a spot Bitcoin ETP. Each time, however, the Commission has rejected the proposition, finding the CME Bitcoin futures market too small or insufficiently linked to pricing in the spot Bitcoin market or the spot Bitcoin ETP the Commission was assessing.⁴⁶

Regarding the second method of demonstrating compliance with Section 6(b)(5), the Commission has consistently rejected showings that the Bitcoin spot market demonstrates inherent resistance to fraud and manipulation. Without ever defining what features would actually satisfy the alternative standard of “inherent,” “novel” and “unique” protections that exceed those of more traditional markets, the Commission has repeatedly found that the Bitcoin spot market does not meet these requirements. As the Commission has acknowledged, “[n]o listing exchange” seeking to list a spot Bitcoin ETP ever “has satisfied its burden to make such a demonstration.”⁴⁷

While the Commission may have a clear vision of what facts a national securities exchange should adduce to show a “reasonable likelihood” that a malefactor would have to trade in a particular market in order to manipulate the ETP, and simultaneously demonstrate the “unlikelihood” that trading in the ETP would be the “predominant influence” on prices in that market, or to show a market’s “inherent,” “novel” and “unique” protections that surpass those of other markets, the Commission has not explained what it has in mind. The result, intentionally or not, is that satisfaction of the Section 6(b)(5) standard that the Commission applies to

⁴¹ Wilshire-Phoenix Order, 85 Fed. Reg. at 12,598 (quoting Section 6(b)(5)).

⁴² VanEck Order, 86 Fed. Reg. at 64,540.

⁴³ *Id.*

⁴⁴ *Id.*

⁴⁵ Winklevoss Order, 83 Fed. Reg. at 37,597-598; Wilshire-Phoenix Order, 85 Fed. Reg. at 12,614-15.

⁴⁶ *E.g.*, VanEck Order 86 Fed. Reg. at 64,546-47; Wilshire-Phoenix Order, 85 Fed. Reg. at 12,614; Winklevoss Order, 83 Fed. Reg. at 37,601.

⁴⁷ VanEck Order, 86 Fed. Reg. at 64,541.

spot Bitcoin Rule 19b-4 applications is a matter to be judged on a case-by-case basis in the simple discretion of the Commission and its staff.

C. Recent shift in the Commission's approach

In August 2021, the Commission began to signal a shift in approach to Bitcoin-linked ETPs. Speaking at the Aspen Security Forum on the subject of cryptocurrencies, the Commission's Chair stated:

I anticipate that there will be filings with regard to exchange-traded funds (ETFs) under the Investment Company Act ('40 Act). When combined with the other federal securities laws, the '40 Act provides significant investor protections.

Given these important protections, I look forward to the staff's review of such filings, particularly if those are limited to these CME-traded Bitcoin futures.⁴⁸

Since the Chair's remarks, three ETPs investing in CME Bitcoin futures contracts have begun trading on national securities exchanges. ProShares Bitcoin Strategy ETF (BITO) began trading on NYSE Arca on October 19, 2021. Next, Valkyrie Bitcoin Strategy ETF (BTF) began trading on The Nasdaq Stock Market on October 22, 2021. Most recently, VanEck Bitcoin Strategy ETF (XBTF) began trading on the Cboe BZX Exchange on November 16, 2021. Because these Bitcoin futures ETPs invest in futures contracts as well as a portfolio of fixed-income securities, each is subject to regulation and registered as an investment company under the 1940 Act.⁴⁹

Each of these Bitcoin futures ETPs invests in futures contracts traded on the CME and priced according to the CME CF Bitcoin Reference Rate.⁵⁰ The CME reference rate, in turn, is determined according to pricing data collected from digital asset trading platforms that include all but one of those currently incorporated into the CoinDesk Bitcoin Price Index (XBX) used by BTC, various of which are incorporated as well into indices used by other spot Bitcoin ETPs rejected by the Commission.⁵¹ Because the CME reference rate is based upon substantially the same Bitcoin pricing data from digital asset trading platforms as the XBX index and indices used by other proposed spot Bitcoin ETPs, both the Bitcoin futures ETPs and the spot Bitcoin ETPs, including BTC, are exposed to the same risks relating to pricing data quality from these digital asset trading platforms. Despite being subject to identical risks—*same data, same risks*—none of the Bitcoin futures ETPs was required to satisfy the Section 6(b)(5) hurdle that the Commission has erected for spot Bitcoin ETPs. And as discussed above, just three weeks after the Bitcoin futures ETPs began trading, the Commission once again rejected a Rule 19b-4 application filed by a spot Bitcoin ETP on the now-familiar grounds that the listing exchange had failed to demonstrate satisfaction of the Section 6(b)(5) standard.⁵²

⁴⁸ Gensler, *supra* note 23.

⁴⁹ See ProShares Trust, Registration Statement (Oct. 15, 2021) at 4-5; Valkyrie Bitcoin Strategy ETF, Registration Statement (Oct. 20, 2021) at 4; VanEck ETF Trust, Registration Statement (Oct. 27, 2021) at 3.

⁵⁰ See ProShares Trust, Registration Statement (Oct. 15, 2021) at 4; Valkyrie Bitcoin Strategy ETF, Registration Statement (Oct. 20, 2021) at 3; VanEck ETF Trust, Registration Statement (Oct. 27, 2021) at 2, 15.

⁵¹ Compare CF Benchmarks, *CME CF Cryptocurrency Pricing Products, Constituent Exchanges List* at 3, <https://docs-cfbenchmarks.s3.amazonaws.com/CME+CF+Constituent+Exchanges.pdf> (last updated Oct. 28, 2019) (listing Bitstamp, Coinbase, Gemini, and Kraken (and previously itBit) as constituent exchanges) with Proposal, 86 Fed. Reg. 61,808 (listing Bitstamp, Coinbase Pro, Kraken and LMAX Digital as constituent exchanges for XBX). The non-overlapping digital asset trading platform used by the CME's index—Gemini—was the reference index utilized by a spot Bitcoin ETP that the Commission disapproved in a prior order on the grounds that the national securities exchange proposing to list that ETP had "not demonstrated that the Gemini Exchange and the Gemini Auction are resistant to manipulation." Winklevoss Order, 83 Fed. Reg. at 37,589. In its most recent disapproval order from earlier this month, the Commission noted that the reference index for the spot Bitcoin ETP at issue were "the same constituent platforms as the CME CF Bitcoin Reference Rate," VanEck Order, 86 Fed. Reg. at 64,541 n.32, yet the Commission still found "no basis to conclude" that these underlying platforms were sufficiently resistant to fraud and manipulation so as to permit listing approval, *id.* at 64,545.

⁵² VanEck Order, 86 Fed. Reg. at 64,539.

The only logical explanation for the curious inconsistency afforded these competing products is a bureaucratic artifact. The successful Bitcoin futures ETPs were able to sidestep the heretofore-unattainable Section 6(b)(5) standard applied to spot Bitcoin ETPs because of a series of accommodations made by the Commission beginning in 2016 that permit national securities exchanges to use generic listing standards to list and trade shares of 1940 Act-registered ETPs without having to follow the Rule 19b-4 approval process.⁵³

Unsurprisingly, the Bitcoin futures ETPs have been well received by the market for offering a convenient and familiar way for U.S. investors to gain exposure to an emerging asset class.⁵⁴ But while permitting the listing and trading of Bitcoin futures ETPs without requiring *any* showing that investors in such products are insulated from the risks of fraud and manipulation in the underlying Bitcoin market, the Commission has continued to apply its vague and discretionary Section 6(b)(5) standard to deny listing approval to the spot Bitcoin ETPs pursuant to Rule 19b-4. The Commission has not offered any meaningful explanation for its differential treatment of these competing products—and the irony that the successful ETPs invest in the very same CME futures market that has failed to qualify as a “significant market” in the Commission’s Rule 19b-4 analysis has gone unacknowledged.

The Commission’s November 12, 2021 spot Bitcoin ETP disapproval order attempted in a cursory way to address the inconsistency between its decision to permit trading of Bitcoin futures ETPs and its continued denial of listing approval for spot Bitcoin ETPs.⁵⁵ Overlooking the proverbial elephant in the room, the order merely stated that it was not evaluating “a product regulated under the 1940 Act” or one with “the same underlying holdings as the Bitcoin Futures ETFs,” and therefore did not need to consider those issues in ruling on the application to list a spot Bitcoin ETP.⁵⁶

II. The Exchange Act and the APA require the Commission to treat BTC similarly to Bitcoin futures ETPs

Having allowed Bitcoin futures ETPs registered under the 1940 Act to begin trading in recent weeks, the Commission may not deny listing approval for BTC by insisting upon a different, vague and evidently impossible-to-meet standard for spot Bitcoin ETPs. Doing so not only would be fundamentally unfair to BTC

⁵³ See 17 C.F.R. § 240.19b-4(e)(1) (providing that “[t]he listing and trading of a new derivative securities product by a self-regulatory organization shall not be deemed a proposed rule change” if the Commission has approved the SRO’s rules, procedures and listing standards for the relevant product class and the SRO has a surveillance program for the product class); Notice of Filing of Amendment No. 2 and Order Granting Accelerated Approval of a Proposed Rule Change, as Modified by Amendment No. 2, to Adopt NYSE Arca Rule 5.2–E(j)(8) Governing the Listing and Trading of Exchange-Traded Fund Shares, Securities Exchange Act Release No. 88625 (Apr. 13, 2020), 85 Fed. Reg. 21,479, 21,480, 21,487 (Apr. 17, 2020) (SR–NYSEArca–2019–81) (approving NYSE Arca generic listing rules pursuant to Rule 19b-4(e) for ETFs authorized to operate pursuant to Rule 6c-11 under the 1940 Act, 17 C.F.R. § 270.6c-11); Notice of Filing of Amendment No. 2 and Order Granting Accelerated Approval of a Proposed Rule Change, as Modified by Amendment No. 2, to Adopt BZX Rule 14.11(l) Governing the Listing and Trading of Exchange-Traded Fund Shares, Securities Exchange Act Release No. 88566 (Apr. 6, 2020), 85 Fed. Reg. 20,312, 20,313, 20,320-21 (Apr. 10, 2020) (SR–CboeBZX–2019–097) (same, as to Cboe BZX); Notice of Filing of Amendment No. 4 and Order Granting Accelerated Approval of a Proposed Rule Change, as Modified by Amendment No. 4, to Adopt Nasdaq Rule 5704 Governing the Listing and Trading of Exchange Traded Fund Shares, Securities Exchange Act Release No. 88561 (Apr. 3, 2020), 85 Fed. Reg. 19,984, 19,984-85, 19,991 (Apr. 9, 2020) (SR–NASDAQ–2019–090) (same, as to Nasdaq); see also Order Granting Approval of a Proposed Rule Change To Amend Nasdaq Rule 5735 To Adopt Generic Listing Standards for Managed Fund Shares, Securities Exchange Act Release No. 78918 (Sept. 23, 2016), 81 Fed. Reg. 67,033, 67,033, 67,036 (Sept. 29, 2016) (SR–NASDAQ–2016–104) (approving Nasdaq generic listing rules for “Managed Fund Shares” that “are issued by actively managed exchange-traded funds (‘ETFs’) that do not seek to replicate the performance of a specified index of securities”); Order Approving a Proposed Rule Change, as Modified by Amendment No. 6, To Amend BATS Rule 14.11(i) to Adopt Generic Listing Standards for Managed Fund Shares, Securities Exchange Act Release No. 78396 (July 22, 2016), 81 Fed. Reg. 49,698, 49,699, 49,702 (July 28, 2016) (SR–BATS–2015–100) (same as to BATS); Order Granting Approval of Proposed Rule Change, as Modified by Amendment No. 7 Thereto, Amending NYSE Arca Equities Rule 8.600 to Adopt Generic Listing Standards for Managed Fund Shares, Securities Exchange Act Release No. 78397 (July 22, 2016), 81 Fed. Reg. 49,320, 49,321, 49,324-25 (July 27, 2016) (SR–NYSEArca–2015–110) (same, as to NYSE Arca).

⁵⁴ See, e.g., Michael Wursthorn, *First Bitcoin Futures ETF Rises in Trading Debut*, Wall Street Journal (Oct. 19, 2021, 5:27 PM), https://www.wsj.com/articles/first-bitcoin-futures-etf-rises-in-trading-debut-11634656217?mod=article_inline; Tanaya Macheel, *First bitcoin futures ETF to make its debut Tuesday on the NYSE*, ProShares says, CNBC (Oct. 18, 2021, 8:52 AM), <https://www.cnbc.com/2021/10/18/first-bitcoin-futures-etf-to-make-its-debut-on-the-nyse-tuesday-proshares-says.html>.

⁵⁵ VanEck Order, 86 Fed. Reg. at 64,552.

⁵⁶ *Id.*

and its shareholders, but would violate the Section 6(b)(5) injunction against unfair discrimination among issuers, and constitute arbitrary and capricious administrative action in violation of the APA.

Under the APA, the Commission must treat similarly situated products similarly unless it has a reasonable basis for disparate treatment.⁵⁷ “Indeed, a federal agency ‘can be said to be at its most arbitrary’ when it ‘treat[s] similar situations dissimilarly.’”⁵⁸ In permitting the listing and trading of 1940 Act-registered Bitcoin futures ETPs, the Commission has explicitly found that the national securities exchange rules authorizing this activity are “designed to prevent fraudulent and manipulative acts and practices” and that allowing trading in these products is consistent with the public interest and investor protection. As discussed below, 1940 Act registration—a status the Commission has determined is not available to BTC⁵⁹—supplies no basis for holding spot Bitcoin ETPs to a standard from which Bitcoin futures ETPs are exempt. The arbitrariness of this difference in treatment is underscored by one simple, indisputable fact: *Bitcoin pricing, whether in the spot or futures market, is determined in the digital asset trading platforms where supply and demand interact.* Indeed, there is almost complete overlap in the underlying Bitcoin digital asset trading platforms that supply pricing information for the reference indices used by both the CME Bitcoin futures market and BTC, as well as other spot Bitcoin ETPs whose listing applications the Commission has disapproved on grounds that the same platforms were insufficiently resistant to fraud and manipulation.⁶⁰

As a result, the risks of fraud and manipulation in the Bitcoin market impacting spot Bitcoin ETPs are indistinguishable from those same risks impacting futures Bitcoin ETPs. While the Commission has cited and relied on these risks as the basis for rejecting spot Bitcoin ETPs, it has found these risks to be irrelevant to its approval of Bitcoin futures ETPs. Explaining this contradiction by reference to Bitcoin futures ETPs’ status under the 1940 Act is a red herring. As discussed below, the 1940 Act offers no protections against fraudulent and manipulative trading in the underlying Bitcoin market beyond the salutary disclosure protections of the Securities Act and the Exchange Act, which apply with as much force to BTC as they do to Bitcoin futures ETPs.

Other than 1940 Act status, the Commission has offered no justification for applying a vague and apparently unattainable standard to spot products while applying a different and more relaxed standard—or possibly no standard at all—to competing futures products. And even if the Commission believes that 1940 Act-style regulation of spot Bitcoin ETPs should be in place before a national securities exchange’s listing rules can comply with Section 6(b)(5), it is well within the Commission’s power to promulgate such regulations. The Commission certainly may not simultaneously insist upon 1940 Act-style regulation for spot Bitcoin ETPs while denying them the ability to submit to such regulation, on an elective basis or otherwise.⁶¹

A. Regulation under the 1940 Act does not justify treating Bitcoin-linked ETPs differently from each other

Regulation of Bitcoin futures ETPs under the 1940 Act provides no basis for treating them differently from competing products such as BTC; registration or non-registration under the 1940 Act simply is not relevant to the question of whether the Commission should authorize a spot Bitcoin ETP. The 1940 Act does not address fraud or manipulation in markets for underlying investments, but instead seeks “to remedy certain

⁵⁷ *Kirk v. Comm’r SSA*, 987 F.3d 314, 321 (4th Cir. 2021) (“A fundamental norm of administrative procedure requires an agency to treat like cases alike.”) (quoting *Westar Energy, Inc. v. Fed. Energy Reg. Comm’n*, 473 F.3d 1239, 1241 (D.C. Cir. 2007)).

⁵⁸ *Kirk*, 987 F.3d at 321 (quoting *Steger v. Def. Inv. Serv. Dep’t of Def.*, 717 F.2d 1402, 1406 (D.C. Cir. 1983)).

⁵⁹ See *supra* note 5.

⁶⁰ See *supra* note 51 and accompanying text.

⁶¹ *Id.* For example, while the Commission did not base its November 12, 2021 disapproval order on the fact that 1940 Act ETPs are subject to ongoing examination and inspection, the Commission could if it thought proper propose rules subjecting commodity ETPs to this oversight process. That it has not done so suggests that it perceives no such need for commodity ETPs.

abusive practices in the management of investment companies” to protect investors in those companies.⁶² Section 1(b) of the 1940 Act identifies the abusive practices at which it is aimed: (1) “failure to provide adequate, accurate information to prospective investors and shareholders in investment companies”; (2) self-interested management at the expense of investors; (3) “use of unsound, misleading, and unsupervised accounting practices”; and (4) “changes in the character of the company’s business without the consent of the shareholders.”⁶³

Such abuses were to be eliminated by achieving five basic objectives: “(1) adequate safeguards for investors in the distribution and sale of investment company securities, (2) honest, unbiased management of investment companies, (3) “greater participation in management” by investors, (4) “creation and maintenance of adequate feasible capital structures of such companies, and (5) transmittal of adequate financial statements and promulgation of uniform accounting rules.”⁶⁴ To meet these goals, the 1940 Act among other things requires registration of the investment company,⁶⁵ limits the number of “interested persons” that can serve on an investment company’s board,⁶⁶ regulates investment advisory fees,⁶⁷ and caps borrowing by the investment company.⁶⁸ Notably, the 1940 Act does not seek to regulate the assets in which investment companies invest. As the Fifth Circuit Court of Appeals long ago concluded, “The history and whole pattern of the Investment Company Act convinces us that Congress . . . intended to deter mismanagement of investment companies for the protection of investment company security holders . . . not to regulate the management of companies in which investment companies put their funds.”⁶⁹

Thus, regulation provided by the 1940 Act does not address the Commission’s rationale for disapproving spot Bitcoin ETPs under its two-pronged Section 6(b)(5) test, which is plainly based on the risks of fraud and manipulation in the underlying Bitcoin market.⁷⁰ For example, the 1940 Act’s protections against self-interested managers are entirely unrelated to the grounds on which the Commission has rejected prior listing proposals for spot Bitcoin ETPs; the Commission has not suggested that manager-related concerns have played any role in its prior denials. Likewise irrelevant are the 1940 Act’s requirements for disclosing financial statements and investment policies. The Commission has never cited a lack of information about a proposed spot Bitcoin ETP’s holdings as a basis for denying listing approval; to the contrary, the Commission has acknowledged that spot Bitcoin ETPs provide significant disclosure with respect to their holdings.⁷¹ And reports on fund holdings required by the 1940 Act supply no basis for treating Bitcoin futures ETPs differently from spot Bitcoin ETPs, because the disclosure requirements of the Securities Act and the Exchange Act would be equally applicable to listed shares of a spot Bitcoin ETP.

The absence of any meaningful connection between the 1940 Act and the Commission’s stated concerns with spot Bitcoin ETPs was revealed in its November 12, 2021 order rejecting a spot Bitcoin ETP, which noted in passing that the spot Bitcoin ETP was not registered under the 1940 Act and had different

⁶² *Option Advisory Serv., Inc. v. SEC*, 668 F.2d 120, 121 (2d Cir. 1981).

⁶³ *Herpich v. Wallace*, 430 F.2d 792, 815 (5th Cir. 1970) (citing 15 U.S.C. § 80a-1(b)).

⁶⁴ *Id.* at 816.

⁶⁵ 15 U.S.C. § 80a-8(a).

⁶⁶ 15 U.S.C. § 80a-10(a).

⁶⁷ 15 U.S.C. §§ 80a-35(b), 80a-36.

⁶⁸ 15 U.S.C. § 80a-18(f)(1).

⁶⁹ See *Herpich*, 430 F.2d at 816-17.

⁷⁰ *Infra* § II.B.

⁷¹ See, e.g., Winklevoss Order, 83 Fed. Reg. at 37,584. The Commission has labeled “unpersuasive” arguments that such disclosure would reduce the ability of market participants to manipulate bitcoin prices. *Id.* at 37,584-85. Among other things, the Commission has concluded that because there is no authoritative and accurate source for Bitcoin pricing and trading, and Bitcoin spot market prices already differ from one another, having an additional transparent source for Bitcoin pricing such as an ETP is unlikely to make manipulation of bitcoin prices less likely. *Id.*

underlying holdings from Bitcoin futures ETPs, but failed to say *why* those differences mattered.⁷² Similarly, when asked whether a lack of “problems with fraud or manipulation” with 1940 Act products linked to Bitcoin futures justified the Commission’s approval of futures products while forbidding spot-market products, the Commission’s Chair observed that the 1940 Act provides investor protections, but cautioned that a Bitcoin futures ETP is “still a highly speculative asset class and listeners should understand that underneath this, it still has that same aspect of volatility and speculation.”⁷³ The Commission thus has yet to provide a reasoned basis for treating Bitcoin futures ETPs differently from spot Bitcoin ETPs based on 1940 Act registration. Unexplained agency statements, of course, carry no weight under the APA.⁷⁴

B. Bitcoin futures ETPs and spot Bitcoin ETPs do not present meaningfully different risks of fraud and manipulation

Disparate treatment of competing spot Bitcoin and Bitcoin futures ETPs cannot be justified by differences between spot and futures Bitcoin markets because the Commission has never found there to be any meaningful difference in the risk of fraud or manipulation between the two markets. To the contrary, the Commission has specifically found that the Bitcoin digital asset trading platforms that contribute pricing data to the CME futures market’s reference index “have none of the[] requirements” necessary to mitigate the risks of fraud and manipulation.⁷⁵ And as the Commission’s Division of Investment Management has emphasized, Bitcoin futures are themselves “highly speculative investment[s],” and investors should “consider the volatility of Bitcoin and the Bitcoin futures market, as well as the lack of regulation and potential for fraud and manipulation in the underlying Bitcoin market”⁷⁶—highlighting that both spot Bitcoin and Bitcoin futures present this investment risk. The Commission has, understandably, never before suggested that investing in a futures market for an asset is inherently safer than investing in the asset itself, but that is the position it would be taking in denying NYSE Arca’s application to list BTC after having allowed exchange trading in multiple Bitcoin futures ETPs.

If anything, derivatives markets present additional opportunities for manipulation on top of spot markets—which is why the derivatives markets have an additional layer of federal regulation to begin with. Although regulation of the Bitcoin futures market by the Commodity Futures Trading Commission (“CFTC”) provides important protections for investors in futures products, it does not justify differential treatment for Bitcoin futures ETPs and spot Bitcoin ETPs. Even with regulation by the CFTC, limiting ETP exposure to Bitcoin futures does not address the risk of manipulation of underlying Bitcoin spot market prices—unless the Commission’s view is that CFTC regulation is adequate for all Bitcoin spot markets, including those in which BTC invests. To the contrary, each time an exchange has argued that CFTC approval of CME-traded Bitcoin futures could mitigate the Commission’s perceived market manipulation concerns, the Commission has rejected that position.⁷⁷ The Commission has instead observed that the CFTC has no authority to oversee underlying Bitcoin spot markets, and that the scope of its regulatory authority to approve futures

⁷² VanEck Order, 86 Fed. Reg. at 64,552. The Division also questioned whether the amendments to Cboe’s proposal raising these concerns had been timely filed, *id.*, an issue not applicable to NYSE Arca’s Proposal here.

⁷³ *CNBC Transcript: SEC Chair Gary Gensler Speaks with CNBC’s “Squawk on the Street” Today*, CNBC (Oct. 19, 2021, 11:36 AM), <https://www.cnbc.com/2021/10/19/cnbc-transcript-sec-chair-gary-gensler-speaks-with-cnbc-s-squawk-on-the-street-today.html>. Chair Gensler also referenced obliquely the CFTC regulation of the CME. As discussed below, that is likewise not a basis to distinguish the futures product from the spot product.

⁷⁴ See *Ill. Pub. Telecomms. Ass’n v. Fed. Comm’n Comm’n*, 117 F.3d 555, 564 (D.C. Cir. 1997) (“The FCC’s *ipse dixit* conclusion, coupled with its failure to respond to contrary arguments resting on solid data, epitomizes arbitrary and capricious decisionmaking.”) (citing *Motor Vehicle Mfrs. Ass’n v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 46-57 (1983)); *Bus. Roundtable v. SEC*, 647 F.3d 1144, 1155 (D.C. Cir. 2011) (SEC acted arbitrarily in basing decision on *ipse dixit*).

⁷⁵ VanEck Order, 86 Fed. Reg. at 64,545; see also *supra* note 51 and accompanying text.

⁷⁶ *Staff Statement on Funds Registered Under the Investment Company Act Investing in the Bitcoin Futures Market*, SEC Division of Investment Management Staff (May 11, 2021), <https://www.sec.gov/news/public-statement/staff-statement-investing-bitcoin-futures-market#>.

⁷⁷ See, e.g., Winklevoss Order, 83 Fed. Reg. at 37,587, 37,599.

products is more limited than the Commission’s own authority with respect to approving the listing and trading of ETPs.⁷⁸ Among other things, the Commission has emphasized that:

- the Bitcoin futures contracts trading on CME were approved through “self-certification”;
- although the CFTC provided “heightened review” of the self-certifications, it expressly made no “judgments about the underlying [Bitcoin] spot market;” and
- the CFTC’s analysis was limited to the specific products CME had proposed and applied the standard of whether such products “were readily susceptible to manipulation,” which is a different standard from that of the Commission: whether the underlying Bitcoin prices are “inherently” or “uniquely” resistant to manipulation.⁷⁹

In short, the Commission has already concluded, when evaluating spot Bitcoin ETPs under Rule 19b-4, that the features of Bitcoin futures trading on CME do *not* provide sufficient assurance against fraud and manipulation, even taking CFTC regulation into account. How the Commission reached a different conclusion in cases of Bitcoin futures ETPs is thus a mystery, but it is clear that any such “internally inconsistent” reasoning violates the APA.⁸⁰

C. The Commission’s standard for approving the listing of spot Bitcoin ETPs is arbitrary and, in practice, impossible to meet

The Commission has never stated what—if any—standard it is applying in its analysis of Bitcoin futures ETPs. But it is evident that the Commission has not required the sponsors of Bitcoin futures ETPs to demonstrate that their products meet the standard that the Commission applies to their competitors. Because if the Commission *did* require futures ETPs to meet the same standard, they too would fail. This is a classic case of treating like cases differently, in violation of the APA,⁸¹ as well as allowing the rules of national securities exchanges to impermissibly discriminate among issuers, in violation of the Exchange Act.

But even putting aside the unfairness of treating spot Bitcoin ETPs differently from their competitors, the standard that the Commission has set for approving the listing of any Bitcoin ETPs under its case-by-case Rule 19b-4 framework is so ill-defined and unachievable as to be arbitrary. As described above, the Commission has set forth two theoretical avenues for listing exchanges to demonstrate compliance with Section 6(b)(5)’s requirement that their rules be designed to prevent fraud and manipulation. First, it has said that an exchange may show that it “has a comprehensive surveillance-sharing agreement with a regulated market of significant size related to the underlying or reference bitcoin assets.”⁸² The Commission has never quantified a “significant market” or “market of significant size”; moreover, it has repeatedly found that no “regulated significant market” for Bitcoin exists under its definition—*not even the CME market in which Bitcoins futures ETPs invest*—rendering illusory any supposed option to enter into a suitable surveillance-sharing agreement. Under the APA, agency action cannot be “vague and indecisive” and must

⁷⁸ See., e.g., *id.*

⁷⁹ See, e.g., *id.*; see also Wilshire-Phoenix Order, 85 Fed. Reg. at 12,604.

⁸⁰ *Bus. Roundtable*, 647 F.3d at 1153.

⁸¹ See *Kirk*, 987 F.3d at 321.

⁸² VanEck Order, 86 Fed. Reg. at 64,540.

afford regulated entities a “principled way” to meet the agency’s requirements.⁸³ But for spot Bitcoin ETPs, the Commission has established a standard that it acknowledges cannot be met.⁸⁴

The Commission’s second path for demonstrating compliance with Rule 6(b)(5)—showing “that the underlying [Bitcoin] market inherently possessed a unique resistance to manipulation beyond the protections that are utilized by traditional commodity or securities markets”⁸⁵—has proved equally elusive. The Commission has insisted on proof of market resistance to fraud and manipulation that is “novel and beyond those protections that exist in traditional commodity markets or equity markets for which the Commission has long required surveillance-sharing agreements in the context of listing derivative securities products.”⁸⁶ The Commission, however, has never defined or specified what would actually constitute “unique resistance to manipulation” that is “beyond the protections of the traditional commodities and equities markets,” nor has the Commission explained what it means for resistance to be “inherent” or “novel” in this context.

Multiple exchanges have attempted to meet this standard, arguing among other things that index pricing would be based on the CME’s manipulation-resistant CF Bitcoin Reference Rate,⁸⁷ that “the geographically diverse and continuous nature of bitcoin trading render it difficult and prohibitively costly to manipulate the price of bitcoin,”⁸⁸ and that “[f]ragmentation across bitcoin platforms, the relatively slow speed of transactions, and the capital necessary to maintain a significant presence on each trading platform” make it especially resistant to manipulation.⁸⁹ But the Commission has found in every instance that the justifications are insufficient to satisfy Section (6)(b)(5): the Commission’s “unique,” “inherent” and “novel” protections standard evidently cannot be satisfied. Under the APA, however, “[i]mpossible requirements imposed by an agency are perforce unreasonable: ‘Conditions imposed by [the] order are . . . unreasonable by virtue of being impossible to meet.’”⁹⁰

D. Disparate treatment of Bitcoin futures ETPs and spot Bitcoin ETPs would limit competition and investor choice while harming investors

The Exchange Act tasks the Commission both with promoting open, competitive markets and investor protection.⁹¹ In carrying out this mandate, the Commission has recognized that expansion of investor choice is a factor in determining whether an exchange’s proposed rule changes to list a new product would be consistent with the requirements of the Exchange Act.⁹² Continued disparate treatment of Bitcoin futures ETPs and spot Bitcoin ETPs would harm—rather than protect—investors by limiting their choices without a

⁸³ *Rapoport v. SEC*, 682 F.3d 98, 107 (D.C. Cir. 2012) (quoting *SEC v. Chenery Corp.*, 332 U.S. 194, 197 (1947)).

⁸⁴ The Commission has acknowledged that its unattainable standard might change in the future, “[o]ver time, [if] regulated bitcoin-related markets . . . continue to grow and develop” or “conditions otherwise change in a manner that affects the Exchange Act analysis.” Winklevoss Order, 83 Fed. Reg. at 37,580.

⁸⁵ Wilshire-Phoenix Order, 85 Fed. Reg. at 12,597.

⁸⁶ *Id.*; Winklevoss Order, 83 Fed. Reg. at 37,582.

⁸⁷ Wilshire-Phoenix Order, 85 Fed. Reg. at 12,597.

⁸⁸ VanEck Order, 86 Fed. Reg. at 64,542.

⁸⁹ *Id.*

⁹⁰ *Alliance for Cannabis Therapeutics v. Drug Enforcement Admin.*, 930 F.2d 936, 940 (D.C. Cir. 1991) (quoting *D.C. Transit Sys., Inc. v. Washington Metropolitan Area Transit Comm’n*, 466 F.2d 393, 402 (D.C. Cir. 1972)) (alterations in original).

⁹¹ 15 U.S.C. § 78f(b)(5) (“The rules of the exchange are designed to . . . remove impediments to and perfect the mechanism of a free and open market and a national market system, and, in general, to protect investors and the public interest.”); 15 U.S.C. § 78c(f) (“Whenever pursuant to this chapter the Commission is engaged in rulemaking, or in the review of a rule of a self-regulatory organization, and is required to consider or determine whether an action is necessary or appropriate in the public interest, the Commission shall also consider, in addition to the protection of investors, whether the action will promote efficiency, competition, and capital formation.”).

⁹² See, e.g., Order Granting Approval of a Proposed Rule Change, as Modified by Amendment No. 2, to Amend Certain Rules to Accommodate the Listing and Trading of Micro Flex Index Options and to Make Other Clarifying and Non-Substantive Changes, Securities Exchange Act Release No. 93122 (Sept. 24, 2021), 86 Fed. Reg. 54,269, 54,274 (Sept. 30, 2021), (SR-CBOE-2021-041) (“The Commission believes that the proposed rule change is consistent with the Act because it would provide investors with additional investment choices . . .”).

reasoned basis. Investors effectively would be limited to futures-based products, even though they face the same risks of fraud and manipulation as spot-based products, while presenting certain structural disadvantages that investors may wish to avoid. For example, Bitcoin futures ETPs are potentially subject to greater costs and additional risks than spot Bitcoin ETPs because futures products are subject to monthly roll-costs, which are incurred when the ETP has to sell the (typically lower-priced) front month contract before expiration and buy the (typically higher-priced) next month's contract. Because of embedded interest or storage costs, each future month's contract is typically more expensive, effectively causing the futures ETP to repeatedly sell low and buy high.⁹³ One analysis showed that over the last year, a futures ETP would have lost 28% of its value just on roll costs (effectively, fees and expenses being equal, a spot ETP would have performed around 28% better).⁹⁴

Similarly, the CME Bitcoin futures market is subject to position limits that restrict the number of Bitcoin futures positions that a Bitcoin futures ETP can hold.⁹⁵ These position limits can cause a Bitcoin futures ETP to experience liquidity problems or losses, or have to halt new creations, denying investors who wish to participate the ability to do so, or increase its fixed-income portfolio and thereby introducing tracking error by diluting its exposure to Bitcoin.⁹⁶ Alternatively, the CME may have to raise position limits to accommodate increased demand in the absence of a spot Bitcoin ETP alternative, potentially increasing the concentration of economic power of a few large market participants in the Bitcoin futures markets and reducing the resiliency of those markets against manipulation.⁹⁷ These risks—that Bitcoin futures ETPs could be constrained by position limits and that the CME may raise those limits—are not purely speculative; indeed, both have already occurred since the first Bitcoin futures ETP began trading.⁹⁸ Restricting investors *only* to Bitcoin futures ETPs while denying access to competing spot Bitcoin ETPs would therefore more likely harm, rather than protect, U.S. investors.

E. The Commission is not a merit regulator

Finally, a decision to continue disallowing spot Bitcoin ETPs would enmesh the Commission in merit regulation, contrary to its mandate. The Exchange Act does not authorize the Commission to regulate the

⁹³ Michael J. Casey, *Why a Bitcoin Futures ETF is Bad for Investors*, CoinDesk (last updated Oct. 22, 2021 at 4:29 PM), <https://www.coindesk.com/policy/2021/10/22/why-a-bitcoin-futures-etf-is-bad-for-investors/>; Omkar Godbole, *Dying for a Bitcoin Futures ETF? Watch Out for 'Contango Bleed'*, CoinDesk (last updated Oct. 20, 2021 at 3:29 PM), <https://www.coindesk.com/markets/2021/10/11/dying-for-a-bitcoin-futures-etf-watch-out-for-contango-bleed/> (explaining that futures markets normally experience "contango" dynamic, where "prices on longer-dated contracts . . . trade above those on shorter-dated contracts" due to storage costs and interest rates); Michael Wursthorn, *A Bitcoin ETF Is Here. What Does That Mean for Investors?*, Wall Street Journal (Oct. 19, 2021, 6:59 PM), https://www.wsj.com/articles/a-bitcoin-etf-is-almost-here-what-does-that-mean-for-investors-11634376601?mod=series_cryptobitcoindogecoin ("Some crypto enthusiasts complain that futures-based ETFs won't track bitcoin perfectly because of the costs of buying and selling futures contracts and other concerns. They contend that investors in bitcoin futures ETFs could be saddled with substandard performance if crypto keeps rising."); *see also, e.g.*, Valkyrie Bitcoin Strategy ETF, Registration Statement (Oct. 20, 2021) at 11 (explaining roll-cost risk applicable to Bitcoin futures ETP and stating that "[t]he costs associated with rolling bitcoin futures typically are substantially higher than the costs associated with other futures contracts and may have a significant adverse impact on the performance of the Fund").

⁹⁴ Casey, *supra* note 93; *see also* David Z. Morris, *Contango Conmigo: Why a Bitcoin Futures ETF Could Be a Bloody Ride*, CoinDesk (Oct. 20, 2021, 12:21 PM), <https://www.coindesk.com/policy/2021/10/20/contango-conmigo-why-a-bitcoin-futures-etf-could-be-a-bloody-ride/> (stating that current roll cost on Bitcoin futures is 17% according to one analyst and predicting Bitcoin futures to underperform spot Bitcoin by 8.4% annually).

⁹⁵ *See CME Bitcoin Futures Frequently Asked Questions*, CME Group (Apr. 1, 2020), <https://www.cmegroup.com/education/bitcoin/cme-bitcoin-futures-frequently-asked-questions.html#> (noting position limits of 4,000 contracts and position accountability limit of 5,000 contracts).

⁹⁶ *See, e.g.*, ProShares Trust, Registration Statement (Oct. 15, 2021), at 6 (noting that if CME position limits prevent fund from obtaining exposure to Bitcoin futures contracts, "the Fund may not be able to achieve its investment objective and may experience significant losses"); *id.* at 13 (noting that "accountability levels [and] position limits . . . may contribute to a lack of liquidity and have a negative impact on Fund performance," and stating that "during periods of illiquidity, "it may be difficult or impossible for a Fund to buy or sell futures at desired prices or at all"); Valkyrie Bitcoin Strategy ETF, Registration Statement (Oct. 20, 2021), at 4, 14 (noting that fund's investment in Bitcoin "will be limited by the position limits established by the [CME]," and that position limits may force fund to alter its investment mix or require "commodity contract positions . . . to be liquidated at disadvantageous times or prices"); VanEck ETF Trust, Registration Statement (Oct. 27, 2021) at 2, 5 (same).

⁹⁷ *See, e.g.*, VanEck ETF Trust, Registration Statement (Oct. 27, 2021) at 36 (noting that "position limit rules are designed to prevent any one participant from controlling a significant portion of the market").

⁹⁸ *See, e.g.*, Shanny Bassar, *CME to Increase Bitcoin Position Limits*, MarketsMedia (Oct. 27, 2021), <https://www.marketsmedia.com/cme-to-increase-bitcoin-position-limits/>; Jamie Gordon, "ProShares bitcoin ETF risks hitting futures contract limit after breaking record to \$1bn," ETF Stream (Oct. 22, 2021), <https://www.etfstream.com/news/proshares-bitcoin-etf-risks-hitting-futures-contract-limit-after-breaking-record-to-1bn/>.

suitability of an asset class, such as Bitcoin, or particular securities, such as BTC shares, relative to competing assets and securities.⁹⁹ As Commissioner Peirce observed in dissenting from an earlier spot Bitcoin ETP denial, “[t]he concerns underlying the disapproval order go to the merits of bitcoin—and thus the bitcoin-based ETP at issue here—as an investment.”¹⁰⁰ With multiple Bitcoin futures ETPs now trading on national securities exchanges, continued adherence to the Commission’s previous approach to spot Bitcoin ETPs would appear to reflect a simple preference for one type of investment over another.

* * *

For the reasons set forth above, we respectfully request that the Commission approve NYSE Arca’s proposal to list and trade BTC.

Very truly yours,



⁹⁹ See, e.g., SEC, SEC Submits Report to Congress on Investment Companies, Exchange, Release No. 4766 (Dec. 2, 1966) (noting that the Commission’s report “of course, makes no attempt to assess the merits of investment company securities relative to other media of investment”); accord, Lynn E. Turner, Chief Accountant, SEC, “Charting a Course for High Quality Financial Reporting,” Remarks at the European FASB-SEC Financial Reporting Conference, 2000 WL 307581, at *1 (“The Securities and Exchange Commission (‘SEC’) does not regulate by passing on the merits of securities offerings. Rather, SEC regulation aims to maintain fair and orderly markets and to protect investors by requiring securities issuers to make full and fair disclosure of all material information, so that investors have a basis for making informed decisions.”); see also *Malack v. BDO Seidman, LLP*, 617 F.3d 743, 752 (3d Cir. 2010) (“The securities laws enacted by Congress in the 1930s were not intended to create a scheme of investors’ insurance or to regulate directly the underlying merits of various investments.” (citation and alteration omitted)).

¹⁰⁰ Dissent of Commissioner Hester M. Peirce to Release No. 34-83723, File No. SR-BatsBZX-2016-30 (July 26, 2018), <https://www.sec.gov/news/public-statement/peirce-dissent-34-83723>.