Cipher Technologies Management LP
600 Steamboat Rd Greenwich CT 06830 USA
t +1 203 769 7800 w cipher.tech

13 May 2019

Dalia Blass
Director
Division of Investment Management
U.S. Securities and Exchange Commission
100 F Street NE
Washington, DC 20549-1090

Re: Staff Letter: Engaging on Fund Innovation and Cryptocurrency-related Holdings (January 18, 2018) (the "Staff Letter")

Dear Ms. Blass:

Cipher Technologies Bitcoin Fund is today registering with the Securities and Exchange Commission (the "SEC") as a closed-end interval fund under the Investment Company Act of 1940 (the "1940 Act") and filing a registration statement for the public offering of its shares under the Securities Act of 1933. As requested by your colleagues on the staff of the SEC (the "Staff") at a meeting last Friday, we are concurrently submitting this letter in response to relevant portions of the Staff Letter.[1]

In the Staff Letter, you raised several concerns for sponsors contemplating the introduction of a registered investment company investing primarily in cryptocurrencies and/or cryptocurrency-related instruments, including valuation, liquidity, custody, arbitrage, and market manipulation. This letter addresses the concerns raised in the Staff Letter, insofar as they are relevant to our proposed fund.[2] We believe the concerns raised by the Staff Letter have appropriate answers, particularly (i) when viewed in the context of a closed-end fund operating as an interval fund and (ii) in light of industry and market developments since the release of the Staff Letter.

<u>Valuation</u>

We agree with the Staff that valuation of portfolio assets is very important to registered investment companies. For interval funds, valuation determines fund performance, what investors pay for interval fund shares, and what investors receive when they elect for their shares to be repurchased. While the Staff Letter correctly notes that the valuation of cryptocurrencies such as bitcoin traded in the spot markets present some novel issues such as forks and airdrops (which we address briefly below), we believe current industry best practices in valuation are sufficient to adequately deal with an asset like bitcoin. Bitcoin is the least nascent and most broadly traded cryptocurrency in the world, and while it has historically had highly volatile periods of trading, such volatility has relaxed in 2018 and 2019, and bitcoin has enjoyed recent periods of trading with less volatility than many investments currently available to investors, such as various active ETFs.

As an investment company, the proposed interval fund would account for its investments in bitcoin[3] as an "other investment". Accordingly, consistent with FASB ASC 946-325, it would value initial acquisitions of bitcoin at their transaction prices and would subsequently value such bitcoin holdings at fair value. Fair valuation determinations would

1. Staff Letter: Engaging on Fund Innovation and Cryptocurrency-related Holdings, SEC No-Action Letter (Jan. 18, 2018), *available at* https://www.sec.gov/divisions/investment/noaction/2018/cryptocurrency-011818.htm.
2. The Staff Letter appears to have been directed principally at mutual funds and exchange-traded funds, but certain of the considerations raised may also be relevant to interval funds. On the other hand, some of the concerns raised in the Staff Letter are of limited relevance to our proposed fund. For example, our fund will not be listed for trading on a securities exchange, and so the ETF-related arbitrage concerns expressed in the Staff Letter do not apply to our fund. Likewise, our fund will not be open-ended, and therefore the concerns regarding liquidity and daily redeemability expressed in the Staff Letter are of less significance for our fund. Additionally, the only cryptocurrency-related asset in which our fund proposes to invest is bitcoin. As more fully set forth in this letter, we believe that some of the concerns expressed in the Staff Letter are less relevant to bitcoin than they may be to certain other cryptocurrency assets.
3. We do not address in this letter valuation of the proposed interval fund's current income-generating investments, such as portfolio asset lending, covered call writing, and futures contracts, but we would be pleased to discuss our views on those investments with you.

be made in accordance with FASB ASC 820. The difficulty posed by ASC 820 for bitcoin, in our opinion, is actually not a lack of effective information, but an abundance of effective information. Bitcoin is actively traded on numerous global trading platforms and over-the-counter markets, utilizing numerous bitcoin-to-fiat-currency pairings and bitcoin-to-other-cryptocurrency pairings. This breadth and depth of trading makes identification of a principal market or most advantageous market difficult, and this difficulty is compounded by the fact that the proposed interval fund may effect its spot trades across multiple platforms and markets. For these reasons, and for purposes of consistency in valuation approach, we currently prefer to use the XBX index maintained by TradeBlock for bitcoin fair valuation purposes.[4] The XBX index value is based on pricing data pulled from a number of leading bitcoin trading platforms and markets that the proposed interval fund is likely to use for transaction purposes, and is continuously volume weighted, price variance weighted, and inactivity adjusted by a proprietary algorithm.[5] We believe this approach is consistent with ASC 820's guidance to consider the relevance and reliability of observed prices and to prioritize observable inputs.[6]

The Staff Letter also raised questions regarding a fund's potential treatment of "forks" and "airdrops". If a hard fork of the bitcoin blockchain network occurred, then the proposed interval fund generally would retain the asset represented on the legacy blockchain network, except in the unlikely event that there is no acceptance of the legacy blockchain network (in which case the asset represented by the new blockchain network would be retained). Whether the asset represented by the new blockchain network would be recognized at all would depend on whether it trades on at least one trading platform to which the interval fund has access. If not, the interval fund would not recognize the new asset. If so, the fund generally would dispose of the new asset in a manner taking into account pricing, relative liquidity, and tax efficiency and reinvest the proceeds of such disposition in the legacy blockchain network asset (in this circumstance, bitcoin).[7] The fund would approach new assets acquired through airdrops, if any, in a similar manner. The precise accounting for the new assets (time of recognition, cost basis, etc.) would be determined in close consultation with the fund's independent registered public accounting firm.

The proposed interval fund would maintain robust valuation policies and procedures that would address each of the above issues. The proposed interval fund's board would regularly review these policies and procedures and, as appropriate, update them in response to changing conditions and technological developments.

We also note here one potential advantage of the proposed interval fund structure – weekly calculation of fund NAV. While mutual funds and ETFs are required to calculate NAV daily, and ETFs have an additional need to frequently publish intraday indicative values, Rule 23c-3 permits interval funds to calculate NAV once per week, except in proximity to its periodic repurchase dates. We believe that the reduced frequency of required NAV calculations for an interval fund would permit the proposed interval fund to better take into account all relevant information and perform a rigorous weekly fair valuation process, which would help to mitigate the potential for errors in daily NAV calculations.

Liquidity

The Staff Letter notes important considerations regarding liquidity for mutual funds and ETFs as they relate to cryptocurrency investing, namely the need for liquidity to support daily redemptions, the relatively new requirement to implement a liquidity risk management program under Rule 22e-4, and the effective 15% cap on illiquid securities in an open-end fund's portfolio. We note that, as a closed-end investment company, the proposed interval fund would not

4. This view may change over time as other bitcoin indexes are developed, as bitcoin trading platforms develop and mature, or for other reasons, and in any event would be the subject of continuous conversations with the board of trustees of the proposed interval fund, including its independent trustees.

5. Based on its publicly-published information, we understand that (i) exchanges with greater liquidity receive a higher weighting in the index, which, among other things, helps to mitigate the effect of volume spikes during off-peak trading hours; (ii) data points are discretely weighted in proportion to their variance from the rest of the cohort, such that as the price at a particular trading platform diverges from the rest of the data points, its influence on the index consequently decreases; and (iii) stale ticks on any particular trading platform are penalized, such that if a trading platform does not have recent trading data, its weighting is gradually reduced until it is de-weighted entirely, and if trading activity resumes, the corresponding weighting for that constituent is gradually increased until it reaches the appropriate level.

6. We would initially categorize bitcoin as a Level 2 asset, though that view may change as the bitcoin trading markets continue to mature and develop, and particularly if regulated exchanges eventually emerge as dominant players in the global trading markets.

7. A relevant example would be the August 2017 hard fork that created Bitcoin Cash. In that case, the proposed interval fund would have disposed of its Bitcoin Cash and used the proceeds to acquire additional bitcoin.

be subject to Rule 22e-4 or any explicit or effective cap on illiquid securities in its portfolio and would not be subject to daily redemptions. The proposed fund's initial registration statement contemplates quarterly repurchase offers and anticipates that such repurchase offers will initially be for 5% of the fund's outstanding shares. We believe the fund's interval fund structure significantly mitigates the Staff's concerns regarding cryptocurrency liquidity.

However, Rule 23c-3 requires that from the time an interval fund sends a repurchase request notification to shareholders until the repurchase pricing date, a percentage of the fund's assets equal to at least 100% of the repurchase offer amount must consist of assets that can be sold or disposed of in the ordinary course of business, at approximately the price at which the fund has valued the investment, within a period equal to the period between a repurchase request deadline and the repurchase payment deadline (or assets that mature by such repurchase payment deadline), and also requires the board of an interval fund to adopt written procedures reasonably designed to ensure such liquidity. The bitcoin spot market is highly liquid, with average daily trading volume in the hundreds of millions to billions of dollars, a multitude of trading platforms and over-the-counter markets globally, and several active market makers. Accordingly, we believe that under normal market circumstances, the proposed interval fund could rely on its portfolio of bitcoin holdings to satisfy its Rule 23c-3 liquidity requirements. However, in the event that market circumstances changed in a relevant quarter, the initial registration statement of the proposed fund reserves the ability to hold high quality, short-term securities specifically for the purposes of satisfying the fund's Rule 23c-3 liquidity requirements. Because the proposed interval fund would be required to satisfy repurchase requests only quarterly, and only for a limited portion of its outstanding shares, we would not expect the holdings of such high quality, short-term securities to impair the ability of the proposed interval fund to pursue its investment strategy.

Custody

The proposed interval fund would custody its bitcoin with a bank in accordance with Section 17(f) of the 1940 Act. While the Staff Letter observed that the Staff was, at that time, aware of no custodians providing fund custodial services for cryptocurrencies, that has changed significantly since the Staff Letter was issued. Several institutions organized as state banking institutions or otherwise have emerged to provide institutional quality custody services to funds in the cryptocurrency space, including new institutions specific to the digital asset ecosystem, such as Gemini, Bitgo, and Coinbase, and traditional institutions such as Fidelity. We believe the security infrastructure and protections offered by these institutions are sufficient to address the concerns articulated in the Staff Letter, and we would of course be pleased to discuss the specifics of the proposed interval fund's contemplated third-party custody arrangements with you and your colleagues.

Arbitrage

The Staff Letter raised a number of relevant questions related to the requirements of exemptive orders specific to ETFs and their use of arbitrage mechanisms to limit market price discounts to net asset value; however, we do not address those concerns here given that the proposed interval fund would not be subject to such requirements.

Potential Manipulation and Other Risks

We have reviewed and are familiar with the concerns expressed by the SEC and its Chairman that were cited in the Staff Letter, as well as the concerns expressed by the Chairman and others in various forums since the issuance of the Staff Letter. We are also familiar with the concerns articulated by the SEC regarding the application of §6(b)(5) of the Securities Exchange Act of 1934 to proposed rule changes by certain exchanges to accommodate listings of bitcoin-focused ETPs.[8] As an initial matter, we note that, because the proposed interval fund does not propose to list its shares on an exchange, §6(b)(5) does not apply.

However, we also address broader concerns regarding market manipulation in cryptocurrency markets. While we cannot rule out the possibility of market manipulation in the cryptocurrency spot markets, we believe there are several

8. As noted by the SEC, that section requires in relevant part 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". *See* 15 U.S.C. §78f(b)(5).

factors that help to mitigate this concern, at least for bitcoin. As noted in prior response letters,[9] the U.S. Commodity Futures Trading Commission (the "CFTC") has encouraged various bitcoin spot markets to enter into surveillance sharing agreements and to police the spot market. It appears that such efforts, and, in our view, the desire of certain bitcoin trading platforms to be perceived as more reputable than alternative trading platforms, are succeeding. It was reported earlier this year, for example, that Nasdaq has licensed its proprietary surveillance technology to seven different cryptocurrency exchanges to date.[10] Certain policies, procedures and features of the proposed interval fund should also mitigate the risk of investor harm related to possible manipulative conduct in cryptocurrency markets. First, the proposed interval fund would limit its cryptocurrency investments to bitcoin, which trades in a broader array of markets, with greater transparency and visibility, than certain other cryptocurrency markets. Second, prior to transacting on behalf of the proposed interval fund, on any bitcoin trading platform or in any over-the-counter markets, and on an ongoing basis, we will conduct our own due diligence and will utilize only those exchanges and markets that satisfy our standards.

With respect to the possible risk that manipulation in an underlying market could affect the price at which shares of the proposed interval fund are issued or repurchased, we have also observed from our recent experience that aberrational price moves (for example, over weekends during thinly traded hours) are generally quickly "corrected" when normal trading hours resume or are isolated to particular platforms. The fact that the proposed fund will value shares only weekly, will issue shares only monthly, and will repurchase shares only quarterly further reduces the risk that investors in the fund would be adversely affected by possible manipulation in underlying markets.

It is also important to distinguish between short-term price moves that one might consider aberrational due to market activities, on the one hand, and the creation and maintenance of an artificial price for an asset, on the other hand. The latter is generally the concern of market manipulation inquiries in similar circumstances.[11] As discussed with the Staff, in the case of bitcoin, any attempt to establish and maintain an artificial price would require the coordinated deployment of an immense amount of capital across a multitude of global trading platforms over a significant period of time. In any event, the relevant consideration for a registered investment company such as the proposed interval fund is whether the risk of any such manipulation is adequately disclosed, and we believe that the disclosure in the initial registration statement for the proposed fund adequately addresses the risks of investments in bitcoin, including the risk of market manipulation.

The Staff Letter also discussed suitability determinations for investors in registered investment companies investing in cryptocurrencies. We believe that a bitcoin-focused interval fund, while certainly not suitable for everyone, is potentially suitable for a wide range of investors, including many retail investors. A bitcoin-focused interval fund could be a valuable addition to many retail and institutional investors' portfolios in that bitcoin is highly uncorrelated to traditional asset classes (equities, fixed income, commodities) broadly, and the introduction of an appropriate amount of bitcoin exposure to an investment portfolio could accordingly help to diversify an investor's risk streams and return drivers, which in turn could mitigate an investor's exposure to single events affecting multiple asset classes (for example, the bear market of 2007-2009). The proposed interval fund's initial registration statement sets forth extensive risk disclosures relative to investments in digital assets, as well as an explanation of bitcoin itself, which we believe are readily understandable by institutional investors, investment advisers, registered broker-dealers, and retail investors. Suitability determinations by broker-dealers for retail clients, we believe, would be likely to focus on the client's total investable assets, total investment in the proposed fund as a proportion of total investable assets, liquidity needs, capacity to absorb a loss of principal, existing investment allocation, risk tolerance, and other relevant factors. In our view, a suitability determination for the proposed interval fund would be significantly less complicated than a suitability determination for, as examples, leveraged or inverse ETFs.

---

9. *See* Letter from Jan van Eck and Gabor Gurbacs to Dalia Blass (Jul. 20, 2018), *available at* https://www.sec.gov/divisions/investment/van-eck-associates-innovation-cryptocurrency.pdf.

10. Michael del Castillo, Nasdaq Is Now Working With 7 Cryptocurrency Exchanges (2019), https://www.forbes.com/sites/michaeldelcastillo/2019/01/30/nasdaq-is-now-working-with-7-cryptocurrency-exchanges/#1d96085c2472 (last visited May 11, 2019).

11. *See, e.g.,* CFTC v. Wilson, No. 13 Civ. 7884, 2018 WL 6322024 (Nov. 30, 2018) (dismissing an action brought by the U.S. Commodity Futures Trading Commission and focusing in part on the creation of an artificial price as a required element to show manipulation).

We would also observe, as have others previously, that those retail investors, or institutional investors that may be acting on the ultimate behalf of beneficiaries that are retail in nature (*e.g.*, pension plans), who are of a mind to acquire access to bitcoin typically find a way to do so, generally by creating individual accounts and trading directly in the bitcoin spot markets. The proposed interval fund will afford a well-regulated alternative to such investors, including important protections provided under the 1940 Act, such as a majority-independent board, limitations on leverage, and restrictions on affiliated transactions.

* * * * *

We believe that our proposed interval fund strikes an appropriate balance of offering investors exposure to bitcoin through a regulated and familiar registered investment company vehicle while also addressing or sufficiently mitigating the concerns articulated in the Staff Letter. We believe it also affords the SEC an opportunity to act in accordance with its rules and its statutory missions of protecting investors, maintaining fair, orderly, and efficient markets, and facilitating capital formation, in this case by embracing technological innovations in financial services. We look forward to continuing our conversations with the Staff and the Commissioners.

Sincerely,

Gerald T. Banks
Founder and Managing Partner

Jacob E. Comer
Head of Regulatory and Compliance

Cc: The Honorable Jay Clayton
The Honorable Robert J. Jackson, Jr.
The Honorable Hester M. Peirce
The Honorable Elad L. Roisman