SECURITIES AND EXCHANGE COMMISSION
(Release No. 34-94006; File No. SR-NYSEArca-2021-37)

January 20, 2022

Self-Regulatory Organizations; NYSE Arca, Inc.; Order Disapproving a Proposed Rule Change to List and Trade Shares of the First Trust SkyBridge Bitcoin ETF Trust under NYSE Arca Rule 8.201-E

I.   INTRODUCTION

On May 6, 2021, NYSE Arca, Inc. ("NYSE Arca" or "Exchange") filed with the

Securities and Exchange Commission ("Commission"), pursuant to Section 19(b)(1) of the

Securities Exchange Act of 1934 ("Exchange Act")[1] and Rule 19b-4 thereunder,[2] a proposed rule

change to list and trade shares ("Shares") of the First Trust SkyBridge Bitcoin ETF Trust

("Trust") under NYSE Arca Rule 8.201-E (Commodity-Based Trust Shares). The proposed rule

change was published for comment in the Federal Register on May 27, 2021.[3]

On July 7, 2021, pursuant to Section 19(b)(2) of the Exchange Act,[4] the Commission

designated a longer period within which to approve the proposed rule change, disapprove the

proposed rule change, or institute proceedings to determine whether to disapprove the proposed

rule change.[5] On August 20, 2021, the Commission instituted proceedings under Section

19(b)(2)(B) of the Exchange Act[6] to determine whether to approve or disapprove the proposed

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1   15 U.S.C. 78s(b)(1).

2   17 CFR 240.19b-4.

3   See Securities Exchange Act Release No. 91962 (May 21, 2021), 86 FR 28646 (May 27, 2021) ("Notice"). Comments on the proposed rule change can be found at: https://www.sec.gov/comments/sr-nysearca-2021-37/srnysearca202137.htm.

4   15 U.S.C. 78s(b)(2).

5   See Securities Exchange Act Release No. 92333, 86 FR 36826 (July 13, 2021).

6   15 U.S.C. 78s(b)(2)(B).

rule change.[7] On November 15, 2021, the Commission designated a longer period for

Commission action on the proposed rule change.[8]

This order disapproves the proposed rule change. The Commission concludes that NYSE Arca has not met its burden under the Exchange Act and the Commission's Rules of Practice to demonstrate that its proposal is consistent with the requirements of Exchange Act Section 6(b)(5), and in particular, the requirement 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."[9]

When considering whether NYSE Arca's proposal to list and trade the Shares is designed to prevent fraudulent and manipulative acts and practices, the Commission applies the same standard used in its orders considering previous proposals to list bitcoin[10]-based commodity trusts and bitcoin-based trust issued receipts.[11] As the Commission has explained, an exchange

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[7]   See Securities Exchange Act Release No. 92714, 86 FR 47662 (Aug. 26, 2021).

[8]   See Securities Exchange Act Release No. 93570, 86 FR 64975 (Nov. 19, 2021).

[9]   15 U.S.C. 78f(b)(5).

[10]   Bitcoins are digital assets that are issued and transferred via a decentralized, open-source protocol used by a peer-to-peer computer network through which transactions are recorded on a public transaction ledger known as the "bitcoin blockchain." The bitcoin protocol governs the creation of new bitcoins and the cryptographic system that secures and verifies bitcoin transactions. See, e.g., Notice, 86 FR at 28646-47.

[11]   See 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 FR 37579 (Aug. 1, 2018) (SR-BatsBZX-2016-30) ("Winklevoss Order"); 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 FR 12595 (Mar. 3, 2020) (SR-NYSEArca-2019-39) ("USBT Order"); Order Disapproving a Proposed Rule Change To List and Trade Shares of the WisdomTree Bitcoin Trust Under BZX Rule 14.11(e)(4), Commodity-Based Trust Shares, Securities Exchange Act Release

that lists bitcoin-based exchange-traded products ("ETPs") can meet its obligations under

Exchange Act Section 6(b)(5) by demonstrating that the exchange has a comprehensive

surveillance-sharing agreement with a regulated market of significant size related to the

underlying or reference bitcoin assets.[12]

The standard requires such surveillance-sharing agreements since they "provide a

necessary deterrent to manipulation because they facilitate the availability of information needed

to fully investigate a manipulation if it were to occur."[13] The Commission has emphasized that it

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No. 93700 (Dec. 1, 2021), 86 FR 69322 (Dec. 7, 2021) (SR-CboeBZX-2021-024) ("WisdomTree Order"); Order Disapproving a Proposed Rule Change to List and Trade Shares of the Valkyrie Bitcoin Fund under NYSE Arca Rule 8.201-E (Commodity-Based Trust Shares), Securities Exchange Act Release No. 93859 (Dec. 22, 2021), 86 FR74156 (Dec. 29, 2021) (SR-NYSEArca-2021-31) ("Valkyrie Order"); Order Disapproving a Proposed Rule Change to List and Trade Shares of the Kryptoin Bitcoin ETF Trust under BZX Rule 14.11(e)(4), Commodity-Based Trust Shares, Securities Exchange Act Release No. 93860 (Dec. 22, 2021), 86 FR 74166 (Dec. 29, 2021) (SR-CboeBZX-2021-029) ("Kryptoin Order"). See also 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 FR 16247 (Apr. 3, 2017) (SR-NYSEArca-2016-101) ("SolidX Order"). The Commission also notes that orders were issued by delegated authority on the following matters: 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 FR 43934 (Aug. 28, 2018) (SR-NYSEArca-2017-139) ("ProShares Order"); 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 FR 43923 (Aug. 28, 2018) (SR-CboeBZX-2018-001) ("GraniteShares Order"); 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 FR 64539 (Nov. 18, 2021) (SR-CboeBZX-2021-019).

[12] See USBT Order, 85 FR at 12596. See also Winklevoss Order, 83 FR at 37592 n.202 and accompanying text (discussing previous Commission approvals of commodity-trust ETPs); GraniteShares Order, 83 FR at 43925-27 nn.35-39 and accompanying text (discussing previous Commission approvals of commodity-futures ETPs).

[13] See Amendment to Rule Filing Requirements for Self-Regulatory Organizations Regarding New Derivative Securities Products, Securities Exchange Act Release No.

is essential for an exchange listing a derivative securities product to enter into a surveillance-sharing agreement with markets trading the underlying assets for the listing exchange to have the ability to obtain information necessary to detect, investigate, and deter fraud and market manipulation, as well as violations of exchange rules and applicable federal securities laws and rules.[14] The hallmarks of a surveillance-sharing agreement are that the agreement provides for the sharing of information about market trading activity, clearing activity, and customer identity; that the parties to the agreement have reasonable ability to obtain access to and produce requested information; and that no existing rules, laws, or practices would impede one party to the agreement from obtaining this information from, or producing it to, the other party.[15]

In the context of this standard, the terms "significant market" and "market of significant size" 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.[16] A surveillance-sharing agreement must be entered into with a "significant market" to assist in detecting and deterring manipulation of the

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40761 (Dec. 8, 1998), 63 FR 70952, 70959 (Dec. 22, 1998) ("NDSP Adopting Release"). See also Winklevoss Order, 83 FR at 37594; ProShares Order, 83 FR at 43936; GraniteShares Order, 83 FR at 43924; USBT Order, 85 FR at 12596.

[14]   See NDSP Adopting Release, 63 FR at 70959.

[15]   See Winklevoss Order, 83 FR at 37592-93; Letter from Brandon Becker, Director, Division of Market Regulation, Commission, to Gerard D. O'Connell, Chairman, Intermarket Surveillance Group (June 3, 1994), available at https://www.sec.gov/divisions/marketreg/mr-noaction/isg060394.htm.

[16]   See Winklevoss Order, 83 FR at 37594. This definition is illustrative and not exclusive. There could be other types of "significant markets" and "markets of significant size," but this definition is an example that will provide guidance to market participants. See id.

ETP, because a person attempting to manipulate the ETP is reasonably likely to also engage in trading activity on that "significant market."[17]

Consistent with this standard, for the commodity-trust ETPs approved to date for listing and trading, there has been in <u>every</u> case at least one significant, regulated market for trading futures on the underlying commodity—whether gold, silver, platinum, palladium, or copper—and the ETP listing exchange has entered into surveillance-sharing agreements with, or held Intermarket Surveillance Group ("ISG") membership in common with, that market.[18] Moreover, the surveillance-sharing agreements have been consistently present whenever the Commission has approved the listing and trading of derivative securities, even where the underlying securities were also listed on national securities exchanges—such as options based on an index of stocks traded on a national securities exchange—and were thus subject to the Commission's direct regulatory authority.[19]

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[17]   See USBT Order, 85 FR at 12597.

[18]   See Winklevoss Order, 83 FR at 37594.

[19]   See USBT Order, 85 FR at 12597; Securities Exchange Act Release No. 33555 (Jan. 31, 1994), 59 FR 5619, 5621 (Feb. 7, 1994) (SR-Amex-93-28) (order approving listing of options on American Depository Receipts ("ADRs")). The Commission has also required a surveillance-sharing agreement in the context of index options even when (i) all of the underlying index component stocks were either registered with the Commission or exempt from registration under the Exchange Act; (ii) all of the underlying index component stocks traded in the U.S. either directly or as ADRs on a national securities exchange; and (iii) effective international ADR arbitrage alleviated concerns over the relatively smaller ADR trading volume, helped to ensure that ADR prices reflected the pricing on the home market, and helped to ensure more reliable price determinations for settlement purposes, due to the unique composition of the index and reliance on ADR prices. See Securities Exchange Act Release No. 26653 (Mar. 21, 1989), 54 FR 12705, 12708 (Mar. 28, 1989) (SR-Amex-87-25) (stating that "surveillance-sharing agreements between the exchange on which the index option trades and the markets that trade the underlying securities are necessary" and that "[t]he exchange of surveillance data by the exchange trading a stock index option and the markets for the securities comprising the index is important to the detection and deterrence of intermarket manipulation."). And the Commission has required a surveillance-sharing agreement even when approving options

Listing exchanges have also attempted to demonstrate that other means besides surveillance-sharing agreements will be sufficient to prevent fraudulent and manipulative acts and practices, including that the bitcoin market as a whole or the relevant underlying bitcoin market is "uniquely" and "inherently" resistant to fraud and manipulation.[20] In response, the Commission has agreed that, if a listing exchange could establish that the underlying market inherently possesses a unique resistance to manipulation beyond the protections that are utilized by traditional commodity or securities markets, it would not necessarily need to enter into a surveillance-sharing agreement with a regulated significant market.[21] Such resistance to fraud and manipulation, however, must be 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.[22] No listing exchange has satisfied its burden to make such demonstration.[23]

In its proposed rule change to list and trade Shares, NYSE Arca contends that approval of the proposal is consistent with Section 6(b)(5) of the Exchange Act, in particular Section 6(b)(5)'s requirement that the rules of a national securities exchange be designed to prevent

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based on an index of stocks traded on a national securities exchange. See Securities Exchange Act Release No. 30830 (June 18, 1992), 57 FR 28221, 28224 (June 24, 1992) (SR-Amex-91-22) (stating that surveillance-sharing agreements "ensure the availability of information necessary to detect and deter potential manipulations and other trading abuses").

[20] See USBT Order, 85 FR at 12597.

[21] See Winklevoss Order, 83 FR at 37580, 37582-91 (addressing assertions that "bitcoin and bitcoin [spot] markets" generally, as well as one bitcoin trading platform specifically, have unique resistance to fraud and manipulation); see also USBT Order, 85 FR at 12597.

[22] See USBT Order, 85 FR at 12597.

[23] See supra note 11.

fraudulent and manipulative acts and practices and to protect investors and the public interest.[24] As discussed in more detail below, NYSE Arca asserts that the proposal is consistent with Section 6(b)(5) of the Exchange Act because the Exchange has a comprehensive surveillance-sharing agreement with a regulated market of significant size,[25] and there exist other means to prevent fraudulent and manipulative acts and practices that are sufficient to justify dispensing with the requisite surveillance-sharing agreement.[26]

Moreover, although NYSE Arca recognizes the Commission's focus on potential manipulation of bitcoin ETPs in prior disapproval orders, NYSE Arca states that the Commission should also consider the direct, quantifiable investor protection issues in determining whether to approve the proposal.[27] Specifically, NYSE Arca believes that the proposal would give U.S. investors access to bitcoin in a regulated and transparent exchange-traded vehicle that would act to limit risk to U.S. investors by: (i) reducing premium and discount volatility; (ii) reducing management fees through meaningful competition; (iii) reducing risks associated with investing in operating companies that are imperfect proxies for bitcoin exposure; and (iv) providing an alternative to custodying spot bitcoin.[28]

In the analysis that follows, the Commission examines whether the proposed rule change is consistent with Section 6(b)(5) of the Exchange Act by addressing: in Section III.B.1 assertions that other means besides surveillance-sharing agreements will be sufficient to prevent fraudulent and manipulative acts and practices; in Section III.B.2 assertions that NYSE Arca has

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[24]   See Notice, 86 FR at 28660-61.

[25]   See id. at 28656-58.

[26]   See id. at 28658.

[27]   See id. at 28650.

[28]   See id. at 28649.

entered into a comprehensive surveillance-sharing agreement with a regulated market of significant size related to bitcoin; and in Section III.C assertions that the proposal is consistent with the protection of investors and the public interest.

Based on the analysis, the Commission concludes that NYSE Arca has not established that other means to prevent fraudulent and manipulative acts and practices are sufficient to justify dispensing with the requisite surveillance-sharing agreement. The Commission further concludes that NYSE Arca has not established that it has a comprehensive surveillance-sharing agreement with a regulated market of significant size related to bitcoin. As discussed further below, NYSE Arca repeats various assertions made in prior bitcoin-based ETP proposals that the Commission has previously addressed and rejected—and more importantly, NYSE Arca does not respond to the Commission's reasons for rejecting those assertions but merely repeats them. As a result, the Commission does not find that the proposed rule change is consistent with the statutory requirements of Exchange Act Section 6(b)(5).

The Commission again emphasizes that its disapproval of this proposed rule change does not rest on an evaluation of whether bitcoin, or blockchain technology more generally, has utility or value as an innovation or an investment. Rather, the Commission is disapproving this proposed rule change because, as discussed below, NYSE Arca has not met its burden to demonstrate that its proposal is consistent with the requirements of Exchange Act Section 6(b)(5).

II.   DESCRIPTION OF THE PROPOSED RULE CHANGE

As described in more detail in the Notice,[29] the Exchange proposes to list and trade the

Shares of the Trust under NYSE Arca Rule 8.201-E, which governs the listing and trading of

Commodity-Based Trust Shares on the Exchange.

The investment objective of the Trust will be for the Shares to reflect the performance of

the value of bitcoin, less the Trust's liabilities and expenses.[30] The Trust will not seek to reflect

the performance of any benchmark or index. In order to pursue its investment objective, the

Trust will seek to purchase and sell such number of bitcoin so that the total value of the bitcoin

held by the Trust is as close to 100 percent of the net assets of the Trust as is reasonably

practicable to achieve.[31]

The Shares would represent units of fractional undivided beneficial interest in, and

ownership of, the Trust. The Trust will hold only bitcoins, which the Bitcoin Custodian will

custody on behalf of the Trust. The Trust generally will not hold cash or cash equivalents;

however, the Trust may hold cash and cash equivalents on a temporary basis to pay extraordinary

expenses.[32]

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[29]   See Notice, supra note 3. See also Registration Statement on Form S-1/A, dated May 6, 2021 (File No. 333-254529), filed with the Commission on behalf of the Trust ("Registration Statement").

[30]   See Notice, 86 FR at 28652. First Trust Advisors L.P. is the sponsor of the Trust, and Delaware Trust Company is the trustee. The sub-adviser for the Trust is SkyBridge Capital II, LLC ("Sub-Adviser"). The Bank of New York Mellon ("Administrator") is the transfer agent and the administrator of the Trust. The bitcoin custodian for the Trust is NYDIG Trust Company LLC ("Bitcoin Custodian"). See id. at 28646.

[31]   See id. at 28652.

[32]   See id. at 28652, 28654. The Administrator acts as custodian of the Trust's cash and cash equivalents. See id. at 28654. While the Trust may from time to time incur certain extraordinary, non-recurring expenses that must be paid in U.S. dollars or other fiat

The net asset value ("NAV") of the Trust will be determined in accordance with Generally Accepted Accounting Principles as the total value of bitcoin held by the Trust, plus any cash or other assets, less any liabilities including accrued but unpaid expenses. The NAV of the Trust will be determined as of 4:00 p.m. E.T. on each day that the Shares trade on the Exchange ("Business Day").[33] The Trust will use the CF Bitcoin US Settlement Price ("Reference Rate") to calculate the Trust's NAV.

The Reference Rate is administered by CF Benchmarks Ltd. ("Benchmark Administrator") and serves as a once-a-day benchmark rate of the U.S. dollar price of bitcoin (USD/BTC), calculated as of 4:00 p.m. E.T.[34] The Reference Rate aggregates the trade flow of several bitcoin platforms during an observation window between 3:00 p.m. and 4:00 p.m. E.T. into the U.S. dollar price of one bitcoin at 4:00 p.m., E.T. The current constituent bitcoin platforms of the Reference Rate are Bitstamp, Coinbase, Gemini, itBit, and Kraken ("Constituent Platforms"). In calculating the Reference Rate, the methodology creates a joint list of all "Relevant Transactions"[35] from the Constituent Platforms. The methodology divides this list into

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currency, such events would only impact the amount of bitcoin represented by a Share of the Trust. See id. at 28655.

[33] The Trust's daily activities will generally not be reflected in the NAV determined for the Business Day on which the transactions are effected (the trade date), but rather on the following Business Day. See id. at 28654.

[34] According to NYSE Arca, the Reference Rate is based on materially the same methodology (except calculation time) as the Benchmark Administrator's CME CF Bitcoin Reference Rate ("CME CF BRR"), which was first introduced on November 14, 2016, and is the rate on which bitcoin futures contracts are cash-settled in U.S. dollars on the Chicago Mercantile Exchange ("CME"). See id. at 28654.

[35] According to the Exchange, a "Relevant Transaction" is any cryptocurrency versus U.S. dollar spot trade that occurs during the observation window between 3:00 p.m. and 4:00 p.m., E.T., on a Constituent Platform in the BTC/USD pair that is reported and disseminated by a Constituent Platform through its publicly available Automatic

a number of equally sized time intervals and calculates the volume-weighted median trade price for each of those time intervals.[36] The Reference Rate is the equally weighted average of the volume-weighted median trade prices of all intervals.[37]

The Trust's website, as well as one or more major market data vendors, will provide an intra-day indicative value ("IIV") per Share updated every 15 seconds, as calculated by the Exchange or a third party financial data provider during the Exchange's Core Trading Session (9:30 a.m. to 4:00 p.m. E.T.). The IIV will be calculated by using the prior day's closing NAV per Share as a base and updating that value during the Exchange's Core Trading Session to reflect changes in the value of the Trust's NAV during the trading day.[38]

The Trust will issue and redeem Shares to authorized participants on an ongoing basis in blocks of 50,000 Shares ("Creation Units"). The creation and redemption of Creation Units will be effected in "in-kind" transactions based on the quantity of bitcoin attributable to each Share. The creation and redemption of Creation Units require the delivery to the Trust, or the distribution by the Trust, of the number of bitcoins represented by the Creation Units being created or redeemed.[39]

Programming Interface ("API") and observed by the Benchmark Administrator. See id. at 28655.

[36] According to the Exchange, a volume-weighted median differs from a standard median in that a weighting factor, in this case trade size, is factored into the calculation. See id. at 28655 n.64.

[37] See id. at 28654-55.

[38] See id. at 28659.

[39] See id. at 28658-59.

III.   DISCUSSION

A.   The Applicable Standard for Review

The Commission must consider whether NYSE Arca's proposal is consistent with the

Exchange Act. Section 6(b)(5) of the Exchange Act 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."[40] Under the Commission's Rules of

Practice, the "burden to demonstrate that a proposed rule change is consistent with the Exchange

Act and the rules and regulations issued thereunder . . . is on the self-regulatory organization

['SRO'] that proposed the rule change."[41]

The description of a proposed rule change, its purpose and operation, its effect, and a

legal analysis of its consistency with applicable requirements must all be sufficiently detailed

and specific to support an affirmative Commission finding,[42] and any failure of an SRO to

provide this information may result in the Commission not having a sufficient basis to make an

affirmative finding that a proposed rule change is consistent with the Exchange Act and the

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[40]   15 U.S.C. 78f(b)(5). Pursuant to Section 19(b)(2) of the Exchange Act, 15 U.S.C. 78s(b)(2), the Commission must disapprove a proposed rule change filed by a national securities exchange if it does not find that the proposed rule change is consistent with the applicable requirements of the Exchange Act. Exchange Act Section 6(b)(5) states that an exchange shall not be registered as a national securities exchange unless the Commission determines that "[t]he rules of the exchange are designed to prevent fraudulent and manipulative acts and practices, to promote just and equitable principles of trade, to foster cooperation and coordination with persons engaged in regulating, clearing, settling, processing information with respect to, and facilitating transactions in securities, 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; and are not designed to permit unfair discrimination between customers, issuers, brokers, or dealers, or to regulate by virtue of any authority conferred by this title matters not related to the purposes of this title or the administration of the exchange." 15 U.S.C. 78f(b)(5).

[41]   Rule 700(b)(3), Commission Rules of Practice, 17 CFR 201.700(b)(3).

[42]   See id.

applicable rules and regulations.[43] Moreover, "unquestioning reliance" on an SRO's

representations in a proposed rule change is not sufficient to justify Commission approval of a

proposed rule change.[44]

B. **Whether NYSE Arca Has Met its Burden to Demonstrate That the Proposal Is Designed to Prevent Fraudulent and Manipulative Acts and Practices**

    (1)   Assertions That Other Means Besides Surveillance-Sharing Agreements Will Be Sufficient to Prevent Fraudulent and Manipulative Acts and Practices

As stated above, the Commission has recognized that a listing exchange could

demonstrate that other means to prevent fraudulent and manipulative acts and practices are

sufficient to justify dispensing with a comprehensive surveillance-sharing agreement with a

regulated market of significant size, including by demonstrating that the bitcoin market as a

whole or the relevant underlying bitcoin market is uniquely and inherently resistant to fraud and

manipulation.[45] Such resistance to fraud and manipulation must be novel and beyond those

protections that exist in traditional commodities or securities markets.[46]

NYSE Arca asserts that certain aspects of the market for bitcoin help to mitigate the

potential for fraud and manipulation in connection with bitcoin pricing.[47] Specifically, according

to NYSE Arca, the significant liquidity in the bitcoin spot market and the impact of market

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[43]   See id.

[44]   Susquehanna Int'l Group, LLP v. Securities and Exchange Commission, 866 F.3d 442, 447 (D.C. Cir. 2017) ("Susquehanna").

[45]   See USBT Order, 85 FR at 12597 n.23. The Commission is not applying a "cannot be manipulated" standard. Instead, the Commission is examining whether the proposal meets the requirements of the Exchange Act and, pursuant to its Rules of Practice, places the burden on the listing exchange to demonstrate the validity of its contentions and to establish that the requirements of the Exchange Act have been met. See id.

[46]   See id. at 12597.

[47]   See Notice, 86 FR at 28658.

orders on the overall price of bitcoin have made attempts to move the price of bitcoin

increasingly expensive over the past year.[48] The Exchange states that, in January 2020, for

example, the cost to buy or sell $5 million worth of bitcoin averaged roughly 30 basis points

(compared to 10 basis points in February 2021) with a market impact of 50 basis points

(compared to 30 basis points in February 2021). For a $10 million market order, the cost to buy

or sell was roughly 50 basis points (compared to 20 basis points in February 2021) with a market

impact of 80 basis points (compared to 50 basis points in February 2021). NYSE Arca contends

that, as the liquidity in the bitcoin spot market increases, it follows that the impact of $5 million

and $10 million orders will continue to decrease.[49]

The Exchange's assertions about the bitcoin market do not constitute other means to

prevent fraud and manipulation sufficient to justify dispensing with the requisite surveillance-

sharing agreement. First, the data furnished by NYSE Arca regarding the cost to move the price

of bitcoin, and the market impact of such attempts, are incomplete. NYSE Arca does not provide

meaningful analysis pertaining to how these figures compare to other markets or why one must

conclude, based on the numbers provided, that the bitcoin market is costly to manipulate.

Further, NYSE Arca's analysis of the market impact of a mere two sample transactions is not

sufficient evidence to conclude that the bitcoin market is resistant to manipulation.[50] Even

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[48]　　See id.

[49]　　See id.

[50]　　Aside from stating that the "statistics are based on samples of bitcoin liquidity in USD (excluding stablecoins or Euro liquidity) based on executable quotes on Coinbase Pro, Gemini, Bitstamp, Kraken, LMAX Exchange, BinanceUS, and OKCoin during February 2021," the Exchange provides no other information pertaining to the methodology used to enable the Commission to evaluate these findings or their significance. See Notice, 86 FR at 28658 n.91.

assuming that the Commission agreed with NYSE Arca's premise, that it is costly to manipulate the bitcoin market, and it is becoming increasingly so, any such evidence speaks only to establish that there is some resistance to manipulation, not that it establishes <u>unique</u> resistance to manipulation to warrant dispensing with the standard surveillance-sharing agreement.[51]

Moreover, NYSE Arca does not sufficiently contest the presence of possible sources of fraud and manipulation in the bitcoin spot market generally that the Commission has raised in previous orders, which have included: (1) "wash" trading; (2) persons with a dominant position in bitcoin manipulating bitcoin pricing; (3) hacking of the bitcoin network and trading platforms; (4) malicious control of the bitcoin network; (5) trading based on material, non-public information (such as plans of market participants to significantly increase or decrease their holdings in bitcoin; new sources of demand for bitcoin; the decision of a bitcoin-based investment vehicle on how to respond to a "fork" in the bitcoin blockchain), or based on the dissemination of false and misleading information; (6) manipulative activity involving the purported "stablecoin" Tether (USDT); and (7) fraud and manipulation at bitcoin trading platforms.[52]

In addition, NYSE Arca does not address risk factors specific to the bitcoin blockchain and bitcoin platforms described in the Trust's Registration Statement that undermine its assertions about the bitcoin market. For example, the Registration Statement acknowledges that "platforms on which users trade bitcoin are relatively new and, in some cases, largely unregulated, and, therefore, may be more exposed to fraud and security breaches than

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[51]   <u>See</u> USBT Order, 85 FR at 12601.

[52]   <u>See</u> USBT Order, 85 FR at 12600-01 & nn.66-67 (discussing J. Griffin & A. Shams, <u>Is Bitcoin Really Untethered?</u> (October 28, 2019), <u>available</u> <u>at</u> <u>https://ssrn.com/abstract=3195066</u> and published in 75 J. Finance 1913 (2020)); Winklevoss Order, 83 FR at 37585-86; Valkyrie Order, 86 FR at 74160.

established, regulated exchanges for other financial assets or instruments;" that the bitcoin blockchain could be vulnerable to a "51% attack," in which a malicious actor(s) or botnet that controls a majority of the processing power dedicated to mining on the bitcoin network may be able to alter the bitcoin blockchain on which the bitcoin network and bitcoin transactions rely; that the nature of the assets held at bitcoin platforms makes them "appealing targets for hackers" and that "a number of bitcoin platforms have been victims of cybercrimes;" that "in 2019 there were reports claiming that 80-95% of bitcoin trading volume on [bitcoin platforms] was false or non-economic in nature;" and that, over the past several years, bitcoin trading platforms "have been closed due to fraud and manipulative activity, business failure or security breaches."[53]

NYSE Arca also asserts that other means to prevent fraud and manipulation are sufficient to justify dispensing with the requisite surveillance-sharing agreement. The Exchange states that the Reference Rate, which is used to determine the value of the Trust's bitcoin and NAV, is itself resistant to manipulation based on the Reference Rate's methodology.[54] The Reference Rate mitigates the effects of potential manipulation of the bitcoin market because the Reference Rate is exclusively based on Constituent Platforms.[55] According to the Exchange, the capital necessary to maintain a significant presence on any Constituent Platform would make manipulation of the Reference Rate unlikely.[56] The Exchange, moreover, asserts that "[b]itcoin trades in a well-arbitraged and distributed market", and "[t]he linkage between the bitcoin markets and the presence of arbitrageurs in those markets means that the manipulation of the

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[53]   See Registration Statement at 16, 18, 20-21.

[54]   See Notice, 86 FR at 28658.

[55]   See id. at 28661.

[56]   See id.

price of bitcoin on any Constituent Platform [(and, as implied by the Exchange, the Reference

Rate)] would likely require overcoming the liquidity supply of such arbitrageurs who are

potentially eliminating any cross-market pricing differences."[57]

Simultaneously with the Exchange's assertions regarding the Reference Rate, the

Exchange also states that, because the Trust will engage in in-kind creations and redemptions

only, the "manipulability of the Reference Rate [is] significantly less important."[58] The

Exchange elaborates further that, "because the Trust will not accept cash to buy bitcoin in order

to create or redeem Shares, the price that the Sponsor uses to value the Trust's bitcoin is not

particularly important."[59] According to NYSE Arca, when authorized participants create Shares

with the Trust, they would need to deliver a certain number of bitcoin per Share (regardless of

the valuation used), and when they redeem with the Trust, they would similarly expect to receive

a certain number of bitcoin per Share.[60] As such, NYSE Arca argues that, even if the price used

to value the Trust's bitcoin has been manipulated, the ratio of bitcoin per Share does not change,

and the Trust will either accept (for creations) or distribute (for redemptions) the same number of

bitcoin regardless of the value.[61] This, according to NYSE Arca, not only mitigates the risk

associated with potential manipulation, but also discourages and disincentivizes manipulation of

the Reference Rate because there is little financial incentive to do so.[62]

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[57]   See id.

[58]   See id. at 28658.

[59]   See id.

[60]   See id.

[61]   See id.

[62]   See id.

Based on assertions made and the information provided, the Commission can find no basis to conclude that NYSE Arca has articulated other means to prevent fraud and manipulation that are sufficient to justify dispensing with the requisite surveillance-sharing agreement. The record does not demonstrate that the proposed methodology for calculating the Reference Rate would make the proposed ETP resistant to fraud or manipulation such that a surveillance-sharing agreement with a regulated market of significant size is unnecessary.[63]

NYSE Arca has not shown that its proposed use of a number of equally-sized time intervals over the observation window between 3:00 p.m. and 4:00 p.m., E.T., to calculate the Reference Rate would effectively be able to eliminate fraudulent or manipulative activity that is not transient. Fraud and manipulation in the bitcoin spot market could persist for a "significant duration."[64] The Exchange does not connect the use of such partitions to the duration of the effects of fraud and manipulation in the bitcoin spot market.[65] Thus, the Exchange fails to establish how the Reference Rate's methodology eliminates fraudulent or manipulative activity that is not transient.[66]

Moreover, the record does not demonstrate that the Benchmark Administrator's reliance solely on the Constituent Platforms to calculate the Reference Rate make the proposed ETP resistant to fraud or manipulation. For example, even assuming, as the Exchange asserts, that the

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[63]   The Commission has previously considered and rejected similar arguments about the valuation of bitcoin according to a benchmark or reference price. See, e.g., SolidX Order, 82 FR at 16258; Winklevoss Order, 83 FR at 37587-90; USBT Order, 85 FR at 12599-601; WisdomTree Order, 86 FR at 69326-28; Valkyrie Order, 86 FR at 74160-63; Kryptoin Order, 86 FR at 74172-73.

[64]   See USBT Order, 85 FR at 12601 n.66; see also id. at 12607.

[65]   See WisdomTree Order, 86 FR at 69327.

[66]   See USBT Order, 85 FR at 12607.

capital necessary to maintain a significant presence on any Constituent Platform make the Reference Rate resistant to manipulation, the Exchange has not assessed the possible influence that spot platforms not included among the Constituent Platforms would have on bitcoin prices used to calculate the Reference Rate. As discussed above, the Exchange has not sufficiently addressed the presence of possible sources of fraud and manipulation in the broader spot market previously raised by the Commission or by the Trust's Registration Statement.[67] Accordingly, to the extent that trading on platforms not directly used to calculate the Reference Rate affects prices on the Constituent Platforms, the characteristics of those other platforms – where various kinds of fraud and manipulation from a variety of sources may be present and persist – may affect whether the Reference Rate is resistant to manipulation.

Likewise, the Commission is unpersuaded by NYSE Arca's assertion that arbitrage across bitcoin markets makes it unlikely that the price of bitcoin on the Constituent Platforms would be manipulated. Here, the Exchange provides insufficient evidence to support its assertion of price arbitrage across bitcoin platforms and does not take into account that a market participant with a dominant ownership position would not find it prohibitively expensive to overcome the liquidity supplied by arbitrageurs and could use dominant market share to engage in manipulation.[68]

In addition, the Exchange's assertions about the Reference Rate are contradicted by the Registration Statement, which states that "the [Reference Rate] has a limited history and there are limitations with the price of bitcoin reflected there."[69] The Registration Statement further

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67   See supra notes 52-53 and accompanying text.

68   See, e.g., Winklevoss Order, 83 FR at 37584; USBT Order, 85 FR at 12600-01.

69   See Registration Statement at 35.

states that "platforms on which users trade bitcoin. . . may be more exposed to fraud and security breaches than established, regulated exchanges for other financial assets or instruments, which could have a negative impact on the performance of the Trust."[70] The Constituent Platforms are a subset of the bitcoin platforms currently in existence. Although the Sponsor raises concerns regarding fraud and security of bitcoin platforms in the Registration Statement, which would include the Constituent Platforms, the Exchange does not explain how or why such concerns are consistent with its assertion that the use of the Reference Rate mitigates the effects of potential manipulation of the bitcoin market.

NYSE Arca also does not explain the significance of the Reference Rate's purported resistance to manipulation to the overall analysis of whether the proposal to list and trade the Shares is designed to prevent fraud and manipulation. Even assuming that the Exchange's argument is that, if the Reference Rate is resistant to manipulation, the Trust's NAV, and thereby the Shares as well, would be resistant to manipulation, the Exchange has not established in the record a basis for such conclusion. That assumption aside, the Commission notes that the Shares would trade at market-based prices in the secondary market, not at NAV, which then raises the question of the significance of the NAV calculation to the manipulation of the Shares.

The Exchange's arguments are also contradictory. While arguing that the Reference Rate is resistant to manipulation, the Exchange simultaneously downplays the importance of the Reference Rate in light of the Trust's in-kind creation and redemption mechanism.[71] The Exchange points out that the Trust will create and redeem Shares in-kind, not in cash, which renders the NAV calculation, and thereby the ability to manipulate NAV, "significantly less

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70   See id. at 18.

71   See supra notes 58-62 and accompanying text.

important."[72] The Trust will not accept cash to buy bitcoin in order to create Shares or sell bitcoin to pay cash for redeemed Shares. Accordingly, in NYSE Arca's own words, the price that the Sponsor uses to value the Trust's bitcoin "is not particularly important."[73] If the Reference Rate that the Trust uses to value the Trust's bitcoin "is not particularly important," it follows that the Reference Rate's resistance to manipulation is not material to the Shares' susceptibility to fraud and manipulation. As the Exchange does not address or provide any analysis with respect to these issues, the Commission cannot conclude that the Reference Rate aids in the determination that the proposal to list and trade the Shares is designed to prevent fraudulent and manipulative acts and practices.

The Commission thus concludes that the Exchange has not demonstrated that its use of the Reference Rate makes the proposed ETP resistant to manipulation. While the proposed procedures for calculating the Reference Rate using only prices from the Constituent Platforms are intended to provide some degree of protection against attempts to manipulate the Reference Rate, these procedures are not sufficient for the Commission to dispense with the requisite surveillance-sharing agreement with a regulated market of significant size.

Finally, the Commission finds that NYSE Arca has not demonstrated that in-kind creations and redemptions provide the Shares with a unique resistance to manipulation. The Commission has previously addressed similar assertions.[74] As the Commission stated before, in-

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[72]   See Notice, 86 FR at 28658 ("While the Sponsor believes that the Reference Rate used to value the Trust's bitcoin is itself resistant to manipulation based on the methodology described above, the fact that creations and redemptions are only available in-kind makes the manipulability of the Reference Rate significantly less important.").

[73]   See id.

[74]   See Winklevoss Order, 83 FR at 37589-90; USBT Order, 85 FR at 12607-08.

kind creations and redemptions are a common feature of ETPs, and the Commission has not

previously relied on the in-kind creation and redemption mechanism as a basis for excusing

exchanges that list ETPs from entering into surveillance-sharing agreements with significant,

regulated markets related to the portfolio's assets.[75] Accordingly, the Commission is not

persuaded here that the Trust's in-kind creations and redemptions afford it a unique resistance to

manipulation.

> (2)   Assertions That NYSE Arca Has Entered Into a Comprehensive
> Surveillance-Sharing Agreement with a Regulated Market of Significant
> Size

As NYSE Arca has not demonstrated that other means besides surveillance-sharing

agreements will be sufficient to prevent fraudulent and manipulative acts and practices, the

Commission next examines whether the record supports the conclusion that NYSE Arca has

entered into a comprehensive surveillance-sharing agreement with a regulated market of

significant size relating to the underlying assets. In this context, the term "market of significant

size" includes a market (or group of markets) as to which (i) 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 (ii) it is unlikely that trading in the ETP would be the

predominant influence on prices in that market.[76]

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[75]   See, e.g., iShares COMEX Gold Trust, Securities Exchange Act Release No. 51058 (Jan. 19, 2005), 70 FR 3749, 3751-55 (Jan. 26, 2005) (SR-Amex-2004-38); iShares Silver Trust, Securities Exchange Act Release No. 53521 (Mar. 20, 2006), 71 FR 14969, 14974 (Mar. 24, 2006) (SR-Amex-2005-072).

[76]   See Winklevoss Order, 83 FR at 37594. This definition is illustrative and not exclusive. There could be other types of "significant markets" and "markets of significant size," but this definition is an example that provides guidance to market participants. See id.

In its proposal, NYSE Arca asserts that the CME, either alone as the sole market for bitcoin futures or as a group of markets together with the Constituent Platforms, is a "market of significant size."[77] As the Commission has stated in the past, it considers two markets that are members of the ISG to have a comprehensive surveillance-sharing agreement with one another, even if they do not have a separate bilateral surveillance-sharing agreement.[78] Accordingly, based on the common membership of NYSE Arca and the CME in the ISG,[79] NYSE Arca has the equivalent of a comprehensive surveillance-sharing agreement with the CME. However, while the Commission recognizes that the Commodity Futures Trading Commission ("CFTC") regulates the CME futures market,[80] including the CME bitcoin futures market, and thus such market is "regulated" in the context of the proposed ETP, the record does not, as explained further below, establish that the CME bitcoin futures market, either alone as the sole market for bitcoin futures or as a group of markets together with the Constituent Platforms, is a "market of significant size" as that term is used in the context of the applicable standard here.

(a)   Whether There is a Reasonable Likelihood That a Person Attempting to Manipulate the ETP Would Also Have to Trade on the CME Bitcoin Futures Market, Alone or Together with Constituent Platforms, to Successfully Manipulate the ETP

The first prong in establishing whether the CME bitcoin futures market constitutes a "market of significant size" is the determination that there is a reasonable likelihood that a

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[77]   See Notice, 86 FR at 28656-58, 28661.

[78]   See Winklevoss Order, 83 FR at 37580 n.19.

[79]   See Notice, 86 FR at 28656.

[80]   While the Commission recognizes that the CFTC regulates the CME, the CFTC is not responsible for direct, comprehensive regulation of the underlying bitcoin spot market. See Winklevoss Order, 83 FR at 37587, 37599. See also infra notes 125-127 and accompanying text.

person attempting to manipulate the ETP would have to trade on the CME bitcoin futures market to successfully manipulate the ETP.[81]

NYSE Arca notes that the CME began to offer trading in bitcoin futures in 2017.[82] According to NYSE Arca, nearly every measurable metric related to CME bitcoin futures contracts, which trade and settle like other cash-settled commodity futures contracts, has "trended consistently up since launch and/or accelerated upward in the past year."[83] For example, according to NYSE Arca, there was approximately $28 billion in trading in the CME bitcoin futures in December 2020 compared to $737 million, $1.4 billion, and $3.9 billion in total trading in December 2017, December 2018, and December 2019, respectively.[84] Additionally, CME bitcoin futures traded over $1.2 billion per day in December 2020 and represented $1.6 billion in open interest compared to $115 million in December 2019.[85] Similarly, NYSE Arca contends that the number of large open interest holders[86] has continued to increase, even as the price of bitcoin has risen, as have the number of unique accounts trading CME bitcoin futures.[87]

In addition, NYSE Arca states that there was approximately $4.321 billion in trading volume and $2.582 billion in open interest in CME bitcoin futures as of April 7, 2021, compared

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81 See Winklevoss Order, 83 FR at 37594.

82 According to NYSE Arca, each contract represents five bitcoin and is based on the CME CF BRR. See Notice, 86 FR at 28651.

83 See id.

84 See id.

85 See id.

86 NYSE Arca represents that a large open interest holder in CME bitcoin futures is an entity that holds at least 25 contracts, which is the equivalent of 125 bitcoin. According to NYSE Arca, at a price of approximately $30,000 per bitcoin on December 31, 2020, more than 80 firms had outstanding positions of greater than $3.8 million in CME bitcoin futures. See id. at 28652 n.60.

87 See id. at 28652.

to $433 million in trading volume and $238 million in open interest as of February 26, 2020.[88] NYSE Arca states that the growth of the CME bitcoin futures market has coincided with similar growth in the bitcoin spot market and that the market for CME bitcoin futures is rapidly approaching the size of markets for other commodity interests.[89] NYSE Arca concludes that, as the CME bitcoin futures market continues to develop and more closely resemble other commodity futures markets, it can be reasonably expected that the relationship between the CME bitcoin futures market and the bitcoin spot market will behave similar to other future/spot market relationships, including periods where a lead-lag relationship between the CME bitcoin futures market and bitcoin spot market exists.[90]

NYSE Arca also asserts that the CME is the primary market for bitcoin futures and "compares favorably" with other markets that were deemed to be markets of significant size in past precedents.[91] In particular, NYSE Arca states that the bitcoin market is similar to the gold market and that the CME is similarly situated to COMEX with respect to gold ETPs.[92] Namely, the Exchange states that, when the Commission approved the listing of gold ETPs and other commodity trust ETPs, rather than requiring surveillance-sharing agreements with the relevant OTC markets, the Commission relied on the surveillance-sharing agreements between the listing exchange and the regulated markets for trading futures on the underlying commodity.[93]

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[88]   See id. at 28657.

[89]   See id.

[90]   See id. at 28657-58.

[91]   See id. at 28656.

[92]   See id. at 28656-57.

[93]   See id. at 28657.

In addition, NYSE Arca asserts that a would-be manipulator of bitcoin prices would be reasonably likely to do so through the CME bitcoin futures market in order to take advantage of the leverage inherent in trading futures contracts.[94] The Exchange argues that, given the tremendous growth in the spot bitcoin market since 2019, the chances of succesfully deploying a manipulative scheme are "increased exponentially" if a would-be manipulator can affect the CME bitcoin futures market (and thus the spot market) by posting only the minimum margin required.[95] According to the Exchange, because the CME bitcoin futures market is the "cheapest" route to manipulate bitcoin, it is highly likely such manipulators would attempt to do so there rather than any spot market.[96]

Further, NYSE Arca maintains that, due to the decentralized nature of the bitcoin network, bitcoin manipulators would be much more likely to attempt to manipulate a limited number of futures markets rather than attempt simultaneous executions on potentially dozens of different spot bitcoin platforms.[97] NYSE Arca states that, even if a would-be manipulator does attempt to manipulate bitcoin across platforms, such a scheme would also necessarily include some attempt to manipulate the price of bitcoin futures, including the CME.[98]

The record does not demonstrate that there is a reasonable likelihood that a person attempting to manipulate the proposed ETP would have to trade on the CME bitcoin futures market to successfully manipulate the proposed ETP. The Exchange's assertions about the size

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[94]   See id. at 28657.

[95]   See id. The Exchange states that, as of April 12, 2021, the initial margin required in connection with CME bitcoin futures for the April 2021 contract ranged from 42% to 38%. See id. at 28657 n.88.

[96]   See id. at 28657.

[97]   See id.

[98]   See id.

of the CME bitcoin futures market, including the trading volume and open interest of, and

number of large open interest holders and unique accounts trading in, CME bitcoin futures, and

its assertion that the CME is the primary market for bitcoin futures, do not establish that the

CME bitcoin futures market is of significant size. While NYSE Arca provides data showing

absolute growth in the size of the CME bitcoin futures market, it provides no data relative to the

concomitant growth in either the bitcoin spot markets or other bitcoin futures markets (including

unregulated futures markets). Morover, even if the CME has grown in relative size, as the

Commission has previously articulated, the interpretation of the term "market of significant size"

or "significant market" depends on the interrelationship between the market with which the

listing exchange has a surveillance-sharing agreement and the proposed ETP.[99] NYSE Arca's

recitation of data reflecting the size of the CME bitcoin futures market and its unsupported claim

that the CME is the primary market for bitcoin futures are not sufficient to establish an

interrelationship between the CME bitcoin futures market and the proposed ETP.[100]

Further, the econometric evidence in the record for this proposal also does not support the

conclusion that an interrelationship exists between the CME bitcoin futures market and the

bitcoin spot market such that it is reasonably likely that a person attempting to manipulate the

proposed ETP would also have to trade on the CME bitcoin futures market to successfully

manipulate the proposed ETP.[101] The Exchange asserts that the relationship between the CME

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[99] See USBT Order, 85 FR at 12611.

[100] See id. at 12612.

[101] See id. at 12611. Listing exchanges have attempted to demonstrate such an "interrelationship" by presenting the results of various econometric "lead-lag" analyses. The Commission considers such analyses to be central to understanding whether it is reasonably likely that a would-be manipulator of the ETP would need to trade on the CME bitcoin futures market. See id. at 12612.

bitcoin futures market and the bitcoin spot market "can be reasonably expected" to behave similarly to other future/spot market relationships, including periods where a lead-lag relationship between the CME bitcoin futures market and bitcoin spot market exists,[102] but the only data NYSE Arca presents to support its "expectation" is the growth in and current size of the CME bitcoin futures market. NYSE Arca's "expectation", without any supporting evidence or analysis, constitutes an insufficient basis for approving a proposed rule change in circumstances where, as here, the Exchange's assertion would form such an integral role in the Commission's analysis.[103]

Likewise, the Exchange's comparison of the bitcoin spot market to the gold spot market is inapposite and does not establish the CME bitcoin futures market's significance. First, the Exchange provides no data or analysis to support its assertion that the bitcoin market is similar to the gold market or that the COMEX gold futures market is similar to the CME bitcoin futures market. Further, as discussed above, for the commodity-trust ETPs approved to date for listing and trading, including where the underlying commodity is gold, there has been in every case at least one significant, regulated market for trading futures.[104] The Exchange's unsupported assertions that the bitcoin market is similar to the gold market or that the CME is similarly situated to COMEX with respect to futures does not establish that the CME bitcoin futures market is a significant market or that it is reasonably likely that an actor attempting to manipulate the price of the proposed ETP's assets would have to trade in the CME bitcoin futures market.

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[102]   See Notice, 86 FR at 28657-58.

[103]   See Susquehanna, 866 F.3d at 447.

[104]   See Winklevoss Order, 83 FR at 37594.

The Exchange also asserts that it is "highly likely" that would-be manipulators of bitcoin prices would attempt to do so in the CME bitcoin futures market because it is the "cheapest" route to manipulate bitcoin.[105] However, the only data the Exchange provides to support its assertion is the initial margin requirement for CME bitcoin futures as of April 12, 2021.[106] The Exchange does not provide any additional data or analysis to support its conclusions or any examples that would demonstrate that such assertions are reasonable. Furthermore, the Exchange does not provide any information on the margin requirements for bitcoin futures markets other than the CME. As stated above, "unquestioning reliance" on an SRO's representations in a proposed rule change is not sufficient to justify Commission approval of a proposed rule change.[107]

Indeed, although the Exchange implies that the "cheapest" route to manipulate bitcoin price is through CME bitcoin futures because of its margin requirement, other bitcoin futures platforms require even less margin than the CME. For example, the contract specifications for a bitcoin futures contract on BitMex (XBTUSD) specifies a maximum initial leverage ratio of 100-to-1,[108] meaning that the required margin for bitcoin futures on BitMex is 1% of the notional value of the open contract position versus, according to the Exchange, 38% to 42% for CME

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[105] See Notice, 86 FR at 28657.

[106] See supra note 95.

[107] See supra note 44.

[108] See https://www.bitmex.com/app/contract/XBTUSD (last visited Dec. 1, 2021). Other unregulated platforms that trade bitcoin futures have similar margin requirements. For example, Deribit has an initial minimum margin requirement of 1% for bitcoin futures. See https://legacy.deribit.com/pages/docs/futures (last visited Dec. 1, 2021). Binance has an initial minimum margin requirement of 2% for trading bitcoin futures. See https://www.binance.com/en/support/announcement/34801a0c405a4b058f9ae18a1a34cad 3 (last visited Dec. 1, 2021).

bitcoin futures.[109] Thus, applying the Exchange's logic, it would appear to be "cheaper," i.e., require less capital commitment, to manipulate the bitcoin price using bitcoin futures traded on BitMex or other unregulated futures platforms rather than the CME, given the lower margin requirements on such unregulated platforms. The Exchange, however, does not address the significance of other futures markets' lower margin requirements to its assertion that a person attempting to manipulate the ETP would also have to trade on the CME bitcoin futures market.

Similarly, although the Exchange asserts that, due to the decentralized nature of the bitcoin network, bitcoin manipulators would be more likely to attempt to manipulate a limited number of bitcoin futures markets rather than attempt simultaneous executions on potentially dozens of different bitcoin spot platforms, NYSE Arca provides no evidence to back up its assertions. The Exchange also claims that, even if a would-be manipulator does attempt to manipulate bitcoin across platforms, such a scheme would also necessarily include some attempts to manipulate the price of bitcoin futures, including the CME. The Exchange, however, does not explain, or provide supporting evidence to establish, why one must "necessarily" conclude such outcome, especially as it relates to the CME. In other words, even assuming that the Commission concurred with the Exchange's premise that a would-be manipulator would attempt to manipulate the ETP by trading on the bitcoin futures market, the Exchange does not explain why such manipulator would do so specifically on the CME.

NYSE Arca also asserts that the CME, if not alone as the sole market for bitcoin futures, then together with the Constituent Platforms, is a "market of significant size." The Exchange argues that, because CME bitcoin futures are cash-settled by reference to a final settlement price based on the CME CF BRR, anyone attempting to manipulate the CME CF BRR would have to

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109   See Notice, 86 FR at 28657 n.88

trade on the Constituent Platforms, and the resulting manipulative trading patterns would be

detectable by the Benchmark Administrator and the CME because of the CME's and the

Benchmark Administrator's oversight of the Constituent Platforms.[110] The Exchange, moreover,

states that each Constituent Platform must: (1) enter into a data sharing agreement with the

CME; (2) cooperate with inquiries and investigations of regulators and the Benchmark

Administrator; and (3) submit each of its clients to its Know-Your Customer ("KYC")

procedures.[111] As a result, in the case of any suspicious trades, the CME and the Exchange would

be able to discover all material trade information, including the identities of the customers

placing the trades.[112]

The Commission is not persuaded by the Exchange's arguments. The Exchange does not

explain the significance of its assertions, including its assertion that the CME and the Benchmark

Administrator would be able to detect manipulative trading patterns on the Constituent

Platforms, in the overall analysis of whether there is a reasonable likelihood that a person

attempting to manipulate the proposed ETP would have to trade on the CME bitcoin futures

market to successfully manipulate the ETP.[113] In other words, even assuming that the

Commission concurs with NYSE Arca's assertion that the CME and the Benchmark

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[110] See Notice, 86 FR at 28657. The Exchange states that because the CME CF BRR is based
solely on price data from the Constituent Platforms, manipulating the CME CF BRR
must necessarily entail manipulating the price data at one or more Constituent Platforms.
The Exchange also states that the CME CF BRR calculation agent receives trading data
from the Constituent Platforms through its API. See id. at 28657 nn.85-86.

[111] See id. at 28657.

[112] See id.

[113] As further discussed below, the Commission finds that the level of regulation of the
Constituent Platforms, including the oversight by the CME and the Benchmark
Administrator, is not equivalent to the obligations, authority, and oversight of national
securities exchanges or futures exchanges and therefore is not an appropriate substitute.
See infra notes 118-132 and accompanying text.

Administrator can detect manipulation on the Constituent Platforms because CME bitcoin futures are cash-settled by reference to the CME CF BRR, the Exchange does not establish how this aids in the determination that either the CME bitcoin futures market, alone or together with the Constituent Platforms, is a significant market with respect to bitcoin. Moreover, the Exchange provides nothing to support its assertion that, to manipulate the CME CF BRR, the would-be manipulator would have to trade on the Constituent Platforms. Similar to the discussion above with respect to Constituent Platforms and the Reference Rate, the Exchange has not assessed the possible influence that spot platforms not included among the Constituent Platforms would have on the spot price of bitcoin on the Constituent Platforms and bitcoin prices used to calculate the CME CF BRR. To the extent that trading on platforms not directly used to calculate the CME CF BRR affects prices on the Constituent Platforms, transactions on those other platforms could affect the CME CF BRR.

Furthermore, even assuming that the record does establish that the CME, together with the Constituent Platforms, is a market of significant size, NYSE Arca acknowledges that it has not entered into a surveillance-sharing agreement with any of the Constituent Platforms.[114] As the Commission has previously stated, a surveillance-sharing agreement with a regulated, significant market facilitates the ETP listing exchange's ability to obtain the necessary information to detect and deter manipulative misconduct.[115] Although NYSE Arca states that the Constituent Platforms must enter into a data sharing agreement with the CME, and the CME and NYSE Arca, by virtue of their ISG membership, have a comprehensive surveillance-sharing agreement with one another, NYSE Arca does not have a surveillance sharing agreement with

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[114]   See Notice, 86 FR at 28656 n.72.

[115]   See Winklevoss Order, 83 FR at 37549.

any of the Constituent Platforms.[116] Accordingly, the Exchange fails to provide a basis for the

Commission to conclude that it has entered into a comprehensive surveillance-sharing agreement

with a regulated market of significant size relating to the underlying assets.[117]

The Constituent Platforms, moreover, are not "regulated." The level of regulation of the

Constituent Platforms is not equivalent to the obligations, authority, and oversight of national

securities exchanges or futures exchanges and therefore is not an appropriate substitute.[118]

National securities exchanges are required to have rules that are "designed to prevent fraudulent

and manipulative acts and practices, to promote just and equitable principles of trade, to foster

cooperation and coordination with persons engaged in regulating, clearing, settling, processing

information with respect to, and facilitating transactions in securities, 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."[119] Moreover, national securities exchanges

must file proposed rules with the Commission regarding certain material aspects of their

operations,[120] and the Commission has the authority to disapprove any such rule that is not

consistent with the requirements of the Exchange Act.[121] Thus, national securities exchanges are

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[116]   See Notice, 86 FR at 28657.

[117]   See, e.g., USBT Order, 85 FR at 12614-15.

[118]   See id., 85 FR at 12603-05.

[119]   See 15 U.S.C. 78f(b)(5).

[120]   17 CFR 240.19b-4(a)(6)(i).

[121]   Section 6 of the Exchange Act, 15 U.S.C. 78f, requires national securities exchanges to register with the Commission and requires an exchange's registration to be approved by the Commission, and Section 19(b) of the Exchange Act, 15 U.S.C. 78s(b), requires national securities exchanges to file proposed rules changes with the Commission and provides the Commission with the authority to disapprove proposed rule changes that are not consistent with the Exchange Act. Designated contract markets ("DCMs") (commonly called "futures markets") registered with and regulated by the CFTC must

subject to Commission oversight of, among other things, their governance, membership

qualifications, trading rules, disciplinary procedures, recordkeeping, and fees.[122]

The Constituent Platforms, on the other hand, have none of these requirements (none are

registered as a national securities exchange).[123] While the Exchange asserts that the Constituent

Platforms must submit their clients to KYC procedures, such requirements are fundamentally

different from the Exchange Act's requirements for national securities exchanges.[124] In addition,

although the Commission recognizes that the CFTC maintains some jurisdiction over the bitcoin

spot market, under the Commodity Exchange Act, the CFTC does not have regulatory authority

over bitcoin spot trading platforms, including the Constituent Platforms.[125] Except in certain

limited circumstances, bitcoin spot trading platforms are not required to register with the CFTC,

and the CFTC does not set standards for, approve the rules of, examine, or otherwise regulate

bitcoin spot markets.[126] As the CFTC itself stated, while the CFTC "has an important role to

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comply with, among other things, a similarly comprehensive range of regulatory principles and must file rule changes with the CFTC. See, e.g., Designated Contract Markets (DCMs), CFTC, available at http://www.cftc.gov/IndustryOversight/TradingOrganizations/DCMs/index.htm.

[122] See Winklevoss Order, 83 FR at 37597.

[123] See 15 U.S.C. 78e, 78f.

[124] See USBT Order, 85 FR at 12603. The Commission has previously concluded that such KYC policies and procedures do not serve as a substitute for, and are not otherwise dispositive in the analysis regarding the importance of having a surveillance sharing agreement with a regulated market of significant size relating to bitcoin. For example, KYC policies and procedures do not substitute for the sharing of information about market trading activity or clearing activity and do not substitute for regulation of a national securities exchange. See USBT Order, 85 FR at 12603 n.101.

[125] See USBT Order, 85 FR at 12604.

[126] See id.

play," U.S. law "does not provide for direct, comprehensive Federal oversight of underlying Bitcoin or virtual currency spot markets."[127]

And while NYSE Arca asserts that the Constituent Platforms must enter into data sharing agreements with the CME, it does not provide any information on the scope, terms, or enforcement authority for such data sharing agreements. Nor has NYSE Arca put any information in the record as to whether and how it would use or enforce such agreements. Moreover, such agreements are contractual in nature and do not satisfy the regulatory requirements or purposes of national securities exchanges and the Exchange Act. The CME (and the CFTC, as discussed above) does not have regulatory authority over the spot bitcoin trading platforms,[128] and, while the CME is regulated by the CFTC,[129] the CFTC's regulations do not extend to the Constituent Platforms by virtue of such contractual agreements.

Further, although NYSE Arca states that the Constituent Platforms must cooperate with inquiries and investigations of regulators and the Benchmark Administrator, it does not describe the scope of such requirements or what authority the Benchmark Administrator or regulators would have to compel the platforms' cooperation or provide meaningful supporting evidence of the extent of such cooperation. Moreover, the Benchmark Administrator does not itself exercise governmental regulatory authority. Rather, the Benchmark Administrator is a registered,

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[127] See Winklevoss Order, 83 FR at 37599 n.288 (quoting CFTC Backgrounder on Oversight of and Approach to Virtual Currency Futures Markets (Jan. 4, 2018), at 1, available at https://www.cftc.gov/sites/default/files/idc/groups/public/@newsroom/documents/file/backgrounder_virtualcurrency01.pdf).

[128] See supra notes 125-127 and accompanying text.

[129] See supra note 80 and accompanying text.

privately-held company in England.[130] The Benchmark Administrator's relationship with the

Constituent Platforms is based on their participation in the determination of reference rates, such

as the Reference Rate. While the Benchmark Administrator is regulated by the UK FCA as a

benchmark administrator, the UK FCA's regulations do not extend to the Constituent Platforms

by virtue of their trade prices serving as input data underlying the Reference Rate.[131]

Further, the oversight performed by the Benchmark Administrator serves a fundamentally

different purpose as compared to the regulation of national securities exchanges and the

requirements of the Exchange Act. While the Commission recognizes that the Benchmark

Administrator's oversight functions may be important for ensuring the integrity of the Reference

Rate, such requirements do not imbue either the Benchmark Administrator or the Constituent

Platforms with regulatory authority similar to that the Exchange Act confers upon self-regulatory

organizations such as national securities exchanges.[132]

The Commission accordingly concludes that the information provided in the record does

not establish a reasonable likelihood that a would-be manipulator of the proposed ETP would

have to trade on the CME bitcoin futures market to successfully manipulate the proposed ETP.

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[130] See https://blog.cfbenchmarks.com/legal/ (stating that the Benchmark Administrator is authorized and regulated by the UK Financial Conduct Authority ("UK FCA") as a registered Benchmark Administrator (FRN 847100) under the EU benchmark regulation, and further noting that the Benchmark Administrator is a member of the Crypto Facilities group of companies which is in turn a member of the Payward, Inc. group of companies, and Payward, Inc. is the owner and operator of the Kraken Exchange, a venue that facilitates the trading of cryptocurrencies). The Commission notes that the Kraken is one of the Constituent Platforms underlying the Reference Rate.

[131] See USBT Order, 85 FR at 12604. The Benchmark Administrator is also not required to apply certain provisions of EU benchmark regulation to the Constituent Platforms because the Reference Rate's input data is not "contributed." See Benchmark Statement, at 5 available at https://docs-cfbenchmarks.s3.amazonaws.com/CME+CF+Benchmark+Statement.pdf.

[132] See 15 U.S.C. 78f(b).

Moreover, NYSE Arca has not entered into a surveillance-sharing agreement with the Constituent Platforms, and the Constituent Platforms are not "regulated" markets. Accordingly, the information in the record also does not establish that the CME bitcoin futures market, alone or together with the Constituent Platforms, is a "market of significant size" with respect to the proposed ETP or that NYSE Arca has a surveillance-sharing agreement with such a market.

> (b) Whether It is Unlikely that Trading in the Proposed ETP Would Be the Predominant Influence on Prices in the CME Bitcoin Futures Market or Constituent Platforms

The second prong in establishing whether a market (or group of markets) constitutes a "market of significant size" is the determination that it is unlikely that trading in the proposed ETP would be the predominant influence on prices in that market.[133] As discussed above, NYSE Arca asserts that CME, either alone as the sole market for bitcoin futures or as a group of markets together with the Constituent Platforms, satisfies this prong.[134]

First, NYSE Arca asserts that trading in the Shares would not be the predominant force on prices in the CME bitcoin futures market (or spot market) because of the significant volume in the CME bitcoin futures market, the size of bitcoin's market capitalization, which is approximately $1 trillion, and the significant liquidity available in the spot market.[135]

To support its assertion about the growth of the CME bitcoin futures market, NYSE Arca states that there was approximately $4.321 billion in trading volume and $2.582 billion in open interest in CME bitcoin futures as of April 7, 2021, compared to $433 million in trading volume and $238 million in open interest as of February 26, 2020.[136] Based on these figures, NYSE Arca

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[133]   See Winklevoss Order, 83 FR at 37594; USBT Order, 85 FR at 12596-97.

[134]   See Notice, 86 FR at 28656.

[135]   See id. at 28657.

[136]   See id. at 28657.

concludes that, as the CME bitcoin futures market continues to develop, it can be reasonably expected that the relationship between the bitcoin futures market and bitcoin spot market will behave similarly to other future/spot market relationships, including periods where a lead-lag relationship between the bitcoin futures market and bitcoin spot market exists.

NYSE Arca also provides that, according to February 2021 data, the cost to buy or sell $5 million worth of bitcoin averages roughly 10 basis points with a market impact of 30 basis points.[137] For a $10 million market order, the cost to buy or sell is roughly 20 basis points with a market impact of 50 basis points. Stated another way, NYSE Arca states that a market participant could enter a market buy or sell order for $10 million of bitcoin and only move the market 0.5 percent.[138] NYSE Arca further asserts that more strategic purchases or sales (such as using limit orders and executing through OTC bitcoin trade desks) would likely have less obvious impact on the market, which is consistent with MicroStrategy, Tesla, and Square being able to collectively purchase billions of dollars in bitcoin.[139] Thus, NYSE Arca concludes that the combination of CME bitcoin futures' important role in price discovery, the overall size of the bitcoin market, and the ability for market participants (including authorized participants creating and redeeming in-kind with the Trust) to buy or sell large amounts of bitcoin without significant market impact, will help prevent the Shares from becoming the predominant force on pricing in either the bitcoin spot or the CME bitcoin futures market.[140]

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[137]   See id. at 28658. According to NYSE Arca, these statistics are based on samples of bitcoin liquidity in U.S. dollars (excluding stablecoins or Euro liquidity) based on executable quotes on Coinbase Pro, Gemini, Bitstamp, Kraken, LMAX Exchange, BinanceUS, and OKCoin during February 2021. See id. at 28658 n.89.

[138]   See id. at 28658.

[139]   See id.

[140]   See id.

NYSE Arca also provides the results from a study conducted by the Benchmark

Administrator ("CF Benchmarks Analysis") to determine the extent of "slippage" (i.e., the

difference between the expected price of a trade and the price at which the trade was actually

executed), which the Exchange states offers further evidence that trading in the Shares is

unlikely to be the predominant influence in the bitcoin spot market.[141] According to NYSE Arca,

the CF Benchmarks Analysis simulated the purchase of 50 bitcoins a day for 686 days (an

amount chosen specifically to replicate hypothetical trades by an ETP) and found that the

maximum amount of slippage on a particular day was 0.3%, with the remainder of values

between 0% and 0.15%.[142] According to NYSE Arca, the CF Benchmarks Analysis demonstrates

that the slippage in the study could be described as having been largely negligible or, at most,

minor during the observation period.[143]

The record does not demonstrate that it is unlikely that trading in the proposed ETP

would be the predominant influence on prices in the CME bitcoin futures market or the spot

market, including the Constituent Platforms.[144] As the Commission has already addressed and

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[141]   See id. at 28658 & n.90 (citing CF Benchmarks, "An Analysis of the Suitability of the
         CME CF BRR for the Creation of Regulated Financial Products," December 2020 ("CF
         Benchmarks Analysis"), available at: https://docsend.com/view/kizk7rarzaba6jxf).

[142]   See id. at 28658.

[143]   See id.

[144]   See USBT Order, 85 FR at 12613-14. The Exchange asserts that the CME, either alone as
         the sole market for the bitcoin futures or as a group of markets together with the
         Constituent Platforms, is a "market of significant size." As noted above, the second prong
         in establishing whether a market (or group of markets) constitutes a "market of
         significant size" is the determination that it is unlikely that trading in the proposed ETP
         would be the predominant influence on prices in that market. The Exchange states
         throughout its filing that trading in the Shares would not be the predominant influence on
         prices in the CME bitcoin futures market or spot market rather than the Constituent
         Platforms. See supra notes 135, 140, and 141 and accompanying text. Since the
         Constituent Platforms are a subset of the the bitcoin spot platforms currently in existence,

rejected one of the bases of NYSE Arca's assertion—CME bitcoin futures' role in price discovery[145]—it will only address below the other bases—the overall size of, and the impact of buys and sells on, the bitcoin market and slippage.

NYSE Arca's assertions about the potential effect of trading in the Shares on the CME bitcoin futures market and bitcoin spot market are general and conclusory, repeating the aforementioned trade volume of the CME bitcoin futures market, and providing general statements about the size and liquidity of the bitcoin spot market as well as the market impact of a large transaction in the spot market, without any analysis or evidence to support these assertions. For example, there is no limit on the amount of mined bitcoin that the Trust may hold. Yet NYSE Arca does not provide any information on the expected growth in the size of the Trust and the resultant increase in the amount of bitcoin held by the Trust over time, or on the overall expected number, size, and frequency of creations and redemptions—or how any of the foregoing could (if at all) influence prices in the CME bitcoin futures market or the spot market.

Moreover, in the Trust's Registration Statement, the Sponsor acknowledges that there is no limit on the number of bitcoins that the Trust may acquire and that the Trust itself may have an impact on the supply and demand of bitcoins. Specifically, the Registration Statement states that the if the number of bitcoins acquired by the Trust is large enough relative to global bitcoin supply and demand, further creations and redemptions of Shares could have an impact on the supply of and demand for bitcoins and that such an impact could affect the price of bitcoin in U.S. dollars.[146] Although the Trust's Registration Statement concedes that the Trust could impact

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the Commission's analysis with respect to the spot market applies equally to the Constituent Platforms.

[145] See supra notes 102-103 and accompanying text.

[146] See Registration Statement at 21.

the price of bitcoin, NYSE Arca does not address this in the proposal or discuss how impacting

the price of bitcoin can be consistent with the assertion that the Shares are unlikely to be the

predominant influence on the prices of the CME bitcoin futures market or the spot market. Thus,

the Commission cannot conclude, based on NYSE Arca's statements alone and absent any

evidence or analysis in support of NYSE Arca's assertions, that it is unlikely that trading in the

ETP would be the predominant influence on prices in the CME bitcoin futures market or the spot

market.

The Commission also is not persuaded by NYSE Arca's assertions about the minimal

effect a large market order to buy or sell bitcoin would have on the bitcoin market.[147] While

NYSE Arca concludes by way of a $10 million market order example that buying or selling large

amounts of bitcoin would have insignificant market impact, the conclusion does not analyze the

extent of any impact on the CME bitcoin futures market, the market that the Exchange, in the

proposal, argues is the significant market under consideration. Even assuming, however, that

NYSE Arca is suggesting that a single $10 million order in bitcoin would have immaterial

impact on the prices in the CME bitcoin futures market, this prong of the "market of significant

size" determination concerns the influence on prices from trading in the proposed ETP, which is

broader than just trading by the proposed ETP. While authorized participants of the Trust might

only transact in the bitcoin spot market as part of their creation or redemption of Shares, the

Shares themselves would be traded in the secondary market on NYSE Arca. The record does not

discuss the expected number or trading volume of the Shares, or establish the potential effect of

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[147] See Notice, 86 FR at 28659 ("For a $10 million market order, the cost to buy or sell is roughly 20 basis points with a market impact of 50 basis points. Stated another way, a market participant could enter a market buy or sell order for $10 million of bitcoin and only move the market 0.5%.").

the Shares' trade prices on CME bitcoin futures prices, or the spot market prices. For example, NYSE Arca does not provide any data or analysis about the potential effect the quotations or trade prices of the Shares might have on market-maker quotations in CME bitcoin futures contracts and whether those effects would constitute a predominant influence on the prices of those futures contracts.

Similarly, although NYSE Arca cites to the CF Benchmark Analysis as evidence that trading in the Shares is unlikely to be the predominant influence in the bitcoin spot market, NYSE Arca states that the simulation in the analysis was done specifically to replicate hypothetical trades by an ETP. The study further states that the simulation was performed to "represent a large [b]itcoin trade of the kind that institutional traders might need to undertake for a major client, or that an issuer of a financial product (such as an ETF or a derivative) would be required to execute in order to facilitate trading of that product."[148] As discussed above, this prong concerns the influence on prices from trading in the proposed ETP. Under the proposal, the Shares themselves would be traded in the secondary market on NYSE Arca, and the CF Benchmark Analysis does not discuss the effect of the trade prices of ETP shares or other bitcoin derivatives on the bitcoin market, or more importantly, CME bitcoin futures market. Likewise, the CF Benchmark Analysis only analyzes the prices of hypothetical bitcoin spot transactions as compared to the CME CF BRR – a spot price index – and does not analyze the extent of any impact of such hypothetical transactions on prices in the CME bitcoin futures market specifically.

Thus, because NYSE Arca has not provided sufficient information to establish both prongs of the "market of significant size" determination, the Commission cannot conclude that

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[148]   See CF Benchmark Analysis, at 16.

the CME bitcoin futures market, either alone as the sole market for bitcoin futures or as a group of markets together with the Constituent Platforms, is a "market of significant size" such that NYSE Arca would be able to rely on a surveillance-sharing agreement with the CME to provide sufficient protection against fraudulent and manipulative acts and practices.

The requirements of Section 6(b)(5) of the Exchange Act apply to the rules of national securities exchanges. Accordingly, the relevant obligation for a comprehensive surveillance-sharing agreement with a regulated market of significant size, or other means to prevent fraudulent and manipulative acts and practices that are sufficient to justify dispensing with the requisite surveillance-sharing agreement, resides with the listing exchange. Because there is insufficient evidence in the record demonstrating that NYSE Arca has satisfied this obligation, the Commission cannot approve the proposed ETP for listing and trading on NYSE Arca.

C. Whether NYSE Arca Has Met Its Burden to Demonstrate That the Proposal Is Designed to Protect Investors and the Public Interest

NYSE Arca contends that, if approved, the proposed ETP would protect investors and the public interest. However, the Commission must consider these potential benefits in the broader context of whether the proposal meets each of the applicable requirements of the Exchange Act.[149] Because NYSE Arca has not demonstrated that its proposed rule change is designed to prevent fraudulent and manipulative acts and practices, the Commission must disapprove the proposal.

NYSE Arca asserts that, with the growth of U.S. investor exposure to bitcoin through OTC bitcoin funds, so too has grown the potential risk to U.S. investors.[150] Specifically, NYSE

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[149] See Winklevoss Order, 83 FR at 37601. See also GraniteShares Order, 83 FR at 43931; ProShares Order, 83 FR at 43941; USBT Order, 85 FR at 12615.

[150] See Notice, 86 FR at 28649.

Arca argues that premium and discount volatility, high fees, insufficient disclosures, and technical hurdles are exposing U.S. investors to risks that could potentially be eliminated through access to a bitcoin ETP.[151] As such, the Exchange believes that approving this proposal (and comparable proposals) represents an opportunity for U.S. investors to gain exposure to bitcoin in a regulated and transparent exchange-traded vehicle that limits risks by: (i) reducing premium and discount volatility; (ii) reducing management fees through meaningful competition; (iii) providing an alternative to custodying spot bitcoin; and (iv) reducing risks associated with investing in operating companies that are imperfect proxies for bitcoin exposure.[152]

According to NYSE Arca, OTC bitcoin funds are generally designed to provide exposure to bitcoin in a manner similar to the Shares. However, unlike the Shares, NYSE Arca states that "OTC [b]itcoin [f]unds are unable to freely offer creation and redemption in a way that incentivizes market participants to keep their shares trading in line with their NAV and, as a result, shares of OTC [b]itcoin [f]unds frequently trade at a price that is out-of-line with the value of their assets held."[153] NYSE Arca represents that, historically, OTC bitcoin funds have traded at a significant premium to NAV.[154] Although the Exchange concedes that trading at a

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[151] See id. NYSE Arca states that while it understands the Commission's previous focus on potential manipulation of a bitcoin ETP in prior disapproval orders, it believes that "such concerns have been sufficiently mitigated and may be outweighed by the growing and quantifiable investor protection concerns related to OTC [b]itcoin [f]unds." See id.

[152] See id.

[153] See id. NYSE Arca also states that, unlike the Shares, because OTC bitcoin funds are not listed on an exchange, they are not subject to the same transparency and regulatory oversight by a listing exchange. NYSE Arca further asserts that the existence of a surveillance-sharing agreement between NYSE Arca and the CME bitcoin futures market would result in increased investor protections for the Shares compared to OTC bitcoin funds. See id. at 28649 n.44.

[154] See id. at 28649. NYSE Arca further represents that the inability to trade in line with NAV may at some point result in OTC bitcoin funds trading at a discount to their NAV,

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premium or a discount is not unique to OTC bitcoin funds and not inherently problematic, NYSE Arca believes that it raises certain investor protections issues. First, according to NYSE Arca, investors are buying shares of a fund for a price that is not reflective of the per share value of the fund's underlying assets.[155] Second, according to NYSE Arca, because only accredited investors, generally, are able to purchase shares directly from the issuing fund at NAV (in exchange for either cash or bitcoin) without having to pay the premium or sell into the discount, these investors that are allowed to purchase directly with the fund are able to hedge their bitcoin exposure as needed to satisfy holding requirements and collect on the premium or discount opportunity.[156] NYSE Arca argues, therefore, that the premium in OTC bitcoin funds essentially creates a transfer in value from retail investors to more sophisticated investors.[157] NYSE Arca further asserts that the risk of manipulation of a bitcoin ETP is also present in and potentially magnified by OTC bitcoin funds.[158]

NYSE Arca also asserts that exposure to bitcoin through an ETP presents advantages for retail investors compared to buying spot bitcoin directly.[159] NYSE Arca asserts that, without the advantages of an ETP, an individual retail investor holding bitcoin through a cryptocurrency

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which has occurred more recently with respect to one prominent OTC bitcoin fund. According to NYSE Arca, while that has not historically been the case, and it is not clear whether such discounts will continue, such a prolonged, significant discount scenario would give rise to nearly identical potential issues related to trading at a premium. See id. at 28649 n.45.

[155]   See id. at 28650.

[156]   See id.

[157]   See id.

[158]   See id.

[159]   See id.

trading platform lacks protections.[160] NYSE Arca explains that, typically, retail platforms hold

most, if not all, retail investors' bitcoin in "hot" (Internet-connected) storage and do not make

any commitments to indemnify retail investors or to observe any particular cybersecurity

standard.[161] Meanwhile, a retail investor holding spot bitcoin directly in a self-hosted wallet may

suffer from inexperience in private key management (e.g., insufficient password protection, lost

key, etc.), which could cause them to lose some or all of their bitcoin holdings.[162] NYSE Arca

represents that the Bitcoin Custodian would, by contrast, use "cold" (offline) storage to hold

private keys, meet a certain degree of cybersecurity measures and operational best practices, be

highly experienced in bitcoin custody, and be accountable for failures.[163] In addition, NYSE

Arca explains that retail investors would be able to hold the Shares in traditional brokerage

accounts, which provide SIPC protection if a brokerage firm fails.[164] Thus, with respect to

custody of the Trust's bitcoin assets, NYSE Arca concludes that, compared to owning spot

bitcoin directly, the Trust presents advantages from an investment protection standpoint for retail

investors.[165]

NYSE Arca further asserts that a number of operating companies engaged in unrelated

businesses have recently announced investments as large as $1.5 billion in bitcoin.[166] Without

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[160]   See id.

[161]   See id.

[162]   See id.

[163]   See id. at 28650-51. NYSE Arca represents that the Sub-Adviser has previously conducted substantial due diligence on the capabilities of the Bitcoin Custodian. See id. at 28651 n.54.

[164]   See id. at 28651.

[165]   See id.

[166]   See id.

access to bitcoin ETPs, NYSE Arca argues that retail investors seeking investment exposure to bitcoin may purchase shares in these companies in order to gain the exposure to bitcoin that they seek.[167] NYSE Arca contends that such operating companies, however, are imperfect bitcoin proxies and provide investors with partial bitcoin exposure paired with additional risks associated with whichever operating company they decide to purchase.[168] NYSE Arca concludes that investors seeking bitcoin exposure through publicly traded companies are gaining only partial exposure to bitcoin, without the full benefit of the risk disclosures and associated investor protections that come from the securities registration process.[169]

NYSE Arca also states that investors in many other countries, including Canada, are able to use more traditional exchange listed and traded products to gain exposure to bitcoin, disadvantaging U.S. investors and leaving them with riskier, more expensive, and less regulated

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[167]   See id.

[168]   See id.

[169]   See id.

means of getting bitcoin exposure.[170] NYSE Arca anticipates that with the addition of more

bitcoin ETPs in non-U.S. jurisdictions expected to grow, such risks will only continue to grow.[171]

NYSE Arca further asserts that several funds registered under the Investment Company

Act of 1940 ("1940 Act") have effective registration statements that contemplate bitcoin

exposure through a variety of means, including through investments in bitcoin futures contacts

and through OTC bitcoin funds and that it is anticipated that other 1940 Act funds will begin to

pursue bitcoin through other means.[172] NYSE Arca asserts that these funds that have already

invested in bitcoin instruments have no reported issues regarding custody, valuation, or

manipulation of the instruments held by these funds.[173] NYSE Arca argues that, while these

funds offer investors some means of exposure to bitcoin, the current offerings fall short of giving

investors an accessible, regulated product that provides concentrated exposure to bitcoin.[174]

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[170] See Notice, 86 FR at 28649. NYSE Arca represents that the Purpose Bitcoin ETF, a retail bitcoin-based ETP launched in Canada, reportedly reached $421.8 million in assets under management in two days and has achieved $993 million in assets as of April 14, 2021, demonstrating the demand for a North American market listed bitcoin ETP. NYSE Arca contends that the demand for the Purpose Bitcoin ETF is driven primarily by investors' desire to have a regulated and accessible means of exposure to bitcoin. NYSE Arca further represents that the Purpose Bitcoin ETF offers a class of units that is U.S. dollar denominated, which could appeal to U.S. investors. NYSE Arca argues that without an approved bitcoin ETP in the U.S. as a viable alternative, U.S. investors could seek to purchase these shares in order to get access to bitcoin exposure. NYSE Arca believes that, given the separate regulatory regime and the potential difficulties associated with any international litigation, such an arrangement would create more risk exposure for U.S. investors than they would otherwise have with a U.S. exchange-listed ETP. See id.

[171] See id.

[172] See id.

[173] See id.

[174] See id.

In essence, NYSE Arca asserts that the risky nature of a direct investment in the underlying bitcoin and the unregulated markets on which bitcoin and OTC bitcoin funds trade compel approval of the proposed rule change. In addition, NYSE Arca essentially argues that, unlike other regulated products available, the Shares would offer more concentrated exposure to bitcoin and should therefore be approved.

The Commission disagrees. Pursuant to Section 19(b)(2) of the Exchange Act, the Commission must approve a proposed rule change filed by a national securities exchange if it finds that the proposed rule change is consistent with the applicable requirements of the Exchange Act—including the requirement under Section 6(b)(5) that the rules of a national securities exchange be designed to prevent fraudulent and manipulative acts and practices—and it must disapprove the filing if it does not make such a finding.[175] Thus, even if a proposed rule change purports to protect investors from a particular type of investment risk, such as the susceptibility of an asset to loss or theft, or to provide more efficient exposure to an asset class than another product, the proposed rule change may still fail to meet the requirements under the Exchange Act.[176]

Here, even if it were true that, compared to trading in unregulated bitcoin spot markets or OTC bitcoin funds, trading a bitcoin-based ETP on a national securities exchange provides some additional protection to investors, or that the Shares would provide more concentrated exposure to bitcoin than other products on the market, the Commission must consider this potential benefit in the broader context of whether the proposal meets each of the applicable requirements of the

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[175]   See Exchange Act Section 19(b)(2)(C), 15 U.S.C. 78s(b)(2)(C).

[176]   See SolidX Order, 82 FR at 16259; WisdomTree Order, 86 FR at 69334.

Exchange Act.[177] As explained above, for bitcoin-based ETPs, the Commission has consistently required that the listing exchange have a comprehensive surveillance-sharing agreement with a regulated market of significant size related to bitcoin, or demonstrate that other means to prevent fraudulent and manipulative acts and practices are sufficient to justify dispensing with the requisite surveillance-sharing agreement. The listing exchange has not met that requirement here. Therefore the Commission is unable to find that the proposed rule change is consistent with the statutory standard.

Pursuant to Section 19(b)(2) of the Exchange Act, the Commission must disapprove a proposed rule change filed by a national securities exchange if it does not find that the proposed rule change is consistent with the applicable requirements of the Exchange Act—including the requirement under Section 6(b)(5) that the rules of a national securities exchange be designed to prevent fraudulent and manipulative acts and practices.[178]

For the reasons discussed above, NYSE Arca has not met its burden of demonstrating that the proposal is consistent with Exchange Act Section 6(b)(5),[179] and, accordingly, the Commission must disapprove the proposal.[180]

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[177] See supra note 149. The Commission notes that the proposed rule change does not relate to a product regulated under the 1940 Act. The Commission considers the proposed rule change on its own merits and under the standards applicable to it. Namely, with respect to this proposed rule change, the Commission must apply the standards as provided by Section 6(b)(5) of the Exchange Act, which it has applied in connection with its orders considering previous proposals to list bitcoin-based commodity trusts and bitcoin-based trust issued receipts.

[178] See 15 U.S.C. 78s(b)(2)(C).

[179] 15 U.S.C. 78f(b)(5).

[180] In disapproving the proposed rule change the Commission has considered its impact on efficiency, competition, and capital formation. See 15 U.S.C. 78c(f).

D. Other Comments

The Commission received a comment letter that addressed the general nature and value of bitcoin.[181] Ultimately, however, additional discussion of this topic is unnecessary, as it does not bear on the basis for the Commission's decision to disapprove the proposal.

IV. CONCLUSION

For the reasons set forth above, the Commission does not find, pursuant to Section 19(b)(2) of the Exchange Act, that the proposed rule change is consistent with the requirements of the Exchange Act and the rules and regulations thereunder applicable to a national securities exchange, and in particular, with Section 6(b)(5) of the Exchange Act.

IT IS THEREFORE ORDERED, pursuant to Section 19(b)(2) of the Exchange Act, that proposed rule change SR-NYSEArca-2021-37 be, and hereby is, disapproved.

By the Commission.

J. Matthew DeLesDernier

Assistant Secretary

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[181]   See letter from Sam Ahn, dated June 4, 2021.