Act normally does not become operative for 30 days after the date of its filing. However, Rule 19b–4(f)(6)(iii) permits the Commission to designate a shorter time if such action is consistent with the protection of investors and the public interest. The Exchange has asked the Commission to waive the 30-day operative delay so that the proposed rule change may become operative upon filing. The Exchange states that waiver of the 30-day operative delay would allow the Buffer Funds to immediately begin listing and trading on the Exchange and employ its amended investment strategy. The Commission does not believe that any new or novel issues are raised by the proposal.

Moreover, as noted above, apart from modifying the downside protection from 10% to 9%, all other statements and representations made in the Prior Approval would remain true and will apply on a continuous basis. For these reasons, the Commission believes that waiver of the 30-day operative delay is consistent with the protection of investors and the public interest. Accordingly, the Commission hereby waives the operative delay and designates the proposed rule change operative upon filing.

At any time within 60 days of the filing of the proposed rule change, the Commission summarily may temporarily suspend such rule change if it appears to the Commission that such action is necessary or appropriate in the public interest, for the protection of investors, or otherwise in furtherance of the purposes of the Act. If the Commission takes such action, the Commission shall institute proceedings to determine whether the proposed rule change should be approved or disapproved.

IV. Solicitation of Comments

Interested persons are invited to submit written data, views, and arguments concerning the foregoing, including whether the proposed rule change is consistent with the Act. Comments may be submitted by any of the following methods:

Electronic Comments

• Use the Commission’s internet comment form (http://www.sec.gov/rules/sro.shtml); or

• Send an email to rule-comments@sec.gov. Please include File Number SR–ChoeBZX–2018–064 on the subject line.

Paper Comments

• Send paper comments in triplicate to Secretary, Securities and Exchange Commission, 100 F Street NE, Washington, DC 20549–1090. All submissions should refer to File Number SR–ChoeBZX–2018–064. This file number should be included on the subject line if email is used. To help the Commission process and review your comments more efficiently, please use only one method. The Commission will post all comments on the Commission’s internet website (http://www.sec.gov/rules/sro.shtml). Copies of the submission, all subsequent amendments, all written statements with respect to the proposed rule change that are filed with the Commission, and all written communications relating to the proposed rule change between the Commission and any person, other than those that may be withheld from the public in accordance with the provisions of 5 U.S.C. 552, will be available for website viewing and printing in the Commission’s Public Reference Room, 100 F Street NE, Washington, DC 20549 on official business days between the hours of 10:00 a.m. and 3:00 p.m. Copies of the filing also will be available for inspection and copying at the principal office of the Exchange. All comments received will be posted without change. Persons submitting comments are cautioned that we do not redact or edit personal identifying information from comment submissions. You should submit only information that you wish to make available publicly. All submissions should refer to File Number SR–ChoeBZX–2018–064, and should be submitted on or before September 18, 2018.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.  

Eduardo A. Aleman,  
Assistant Secretary.

[FR Doc. 2018–18573 Filed 8–27–18; 8:45 am]

BILLING CODE 8011–01–P

SECURITIES AND EXCHANGE COMMISSION


Self-Regulatory Organizations; NYSE Arca, Inc.; Order Disapproving a Proposed Rule Change To List and Trade the Shares of the ProShares Bitcoin ETF and the ProShares Short Bitcoin ETF

August 22, 2018.

I. Introduction

On December 4, 2017, 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") and Rule 19b–4 thereunder, a proposed rule change to list and trade the shares ("Shares") of the ProShares Bitcoin ETF and the ProShares Short Bitcoin ETF (each a “Fund” and, collectively, the “Funds”) issued by the ProShares Trust II ("Trust") under NYSE Arca Rule 8.200–E, Commentary .02. The proposed rule change was published for comment in the Federal Register on December 26, 2017. The comment period for the Notice of Proposed Rule Change closed on January 16, 2018.

On January 30, 2018, pursuant to Section 19(b)(5) of the Exchange Act, 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 approve or disapprove the proposed rule change. On March 23, 2018, the Commission instituted proceedings under Section 19(b)(2)(B) of the Exchange Act to determine whether to approve or disapprove the proposed rule change. The comment period and rebuttal comment period for the Order Instituting Proceedings closed on April 19, 2018, and May 3, 2018, respectively. Finally, on June 15, 2018, the Commission extended the period for consideration of the proposed rule change to August 23, 2018. As of
August 21, 2018, the Commission had received 13 comments on the proposed rule change. This order disapproves the proposed rule change. Although the Commission is disapproving this proposed rule change, the Commission emphasizes that its disapproval 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, the Exchange 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 the Exchange Act Section 6(b)(5), in particular the requirement that a national securities exchange’s rules be designed to prevent fraudulent and manipulative acts and practices. Among other things, the Exchange has offered no record evidence to demonstrate that bitcoin futures markets are “markets of significance.” That failure is critical because, as explained below, the Exchange has failed to establish that other means to prevent fraudulent and manipulative acts and practices will be sufficient, and therefore surveillance-sharing with a regulated market of significant size related to bitcoin is necessary to satisfy the statutory requirement that the Exchange’s rules be designed to prevent fraudulent and manipulative acts and practices.

II. Description of the Proposal

The Exchange proposes to list and trade the Shares under NYSE Arca Rule 8.200–E, Commentary .02, which governs the listing and trading of Trust Issued Receipts on the Exchange. Each Trust Fund will be a series of the Trust, and the Trust and the Funds will be managed and controlled by ProShare Capital Management LLC (“Sponsor”). Brown Brothers Harriman & Co. will be the custodian and administrator for the Trust. SEI Investments Distribution Co. will serve as the distributor of the Shares (“Distributor”). The Trust will offer Shares of the Funds for sale through the Distributor in “Creation Units.”

According to the Notice, the ProShares Bitcoin ETF’s investment objective will be to seek results (before fees and expenses) that, both for a single day and over time, correspond to the performance of lead-month bitcoin futures contracts listed and traded on either the Cboe Futures Exchange (“CFE”) or the Chicago Mercantile Exchange (“CME”) (”Benchmark Futures Contracts”). This Fund generally intends to invest substantially all of its assets in the Benchmark Futures Contracts, but may invest in other U.S. exchange-listed bitcoin futures contracts, if available (together with Benchmark Futures Contracts, collectively, “Bitcoin Futures Contracts”).

According to the Notice, the ProShares Short Bitcoin ETF’s investment objective will be to seek results, for a single day, that correspond (before fees and expenses) to the inverse of the daily performance of the Benchmark Futures Contract. This Fund generally intends to invest substantially all of its assets through short positions in Benchmark Futures Contracts, but may invest through short positions in Bitcoin Futures Contracts, if available.

The Exchange represents that no more than 10% of the net assets of a Fund in the aggregate invested in Bitcoin Futures Contracts shall consist of Bitcoin Futures Contracts whose principal market is neither a member of the Intermarket Surveillance Group nor a market with which the Exchange does not have a comprehensive surveillance-sharing agreement. Further, according to the Notice, in the event that position, price, or accountability limits are reached with respect to Bitcoin Futures Contracts, each Fund may invest in listed options on Bitcoin Futures Contracts (should such listed options become available) and OTC swap agreements referencing Bitcoin Futures Contracts (collectively, “Financial Instruments”). The Notice also states:

Bitcoin Futures Contracts are a new type of futures contract to be traded on the CFE and CME or other U.S. exchanges (if available). Unlike the established futures markets for traditional physical commodities, the market for Bitcoin Futures Contracts is in the development stage and has very limited trading and operational history. As such, the liquidity of the market for Bitcoin Futures Contracts will depend on, among other things, the supply and demand for Bitcoin Futures Contracts, the adoption of bitcoin and the commercial and speculative interest in the market for Bitcoin Futures Contracts and the potential ability to hedge against the price of bitcoin with exchange-traded Bitcoin Futures Contracts.

The Exchange represents that trading in the Shares of each Fund will be subject to the existing trading surveillances administered by the Exchange, as well as cross-market surveillances administered by FINRA on behalf of the Exchange, which are designed to detect violations of Exchange rules and applicable federal securities laws. The Exchange asserts that these procedures are adequate to properly monitor Exchange trading of the Shares in all trading sessions and to deter and detect violations of Exchange rules and federal securities laws applicable to trading on the Exchange.

III. Discussion

A. The Applicable Standard for Review

The Commission must consider whether the Exchange’s proposal is consistent with Exchange Act Section 6(b)(5), which 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.” 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.’’

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, 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 applicable rules and regulations.

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.

B. Preventing Fraudulent and Manipulative Practices

1. Applicable Legal Standard

To approve the Exchange’s proposal to list the Shares, the Commission must be able to find that the proposal is, consistent with Exchange Act Section 6(b)(5), “designed to prevent fraudulent and manipulative acts and practices.” As the Commission recently explained in an order disapproving a listing proposal for the Winklevoss Bitcoin Trust (“Winklevoss Order”), although surveillance-sharing agreements are not the exclusive means by which an exchange-traded product (“ETP”) listing exchange can meet its obligations under Exchange Act Section 6(b)(5), such agreements are a widely used means for exchanges that list ETPs to meet their obligations, and the Commission has historically recognized their importance.

The Commission has therefore determined that, if the listing exchange for an ETP fails to establish that other means to prevent fraudulent and manipulative acts and practices will be sufficient, the listing exchange must enter into a surveillance-sharing agreement with a regulated market of significant size because “[s]uch agreements provide a necessary deterrent to manipulation because they facilitate the availability of information needed to fully investigate a manipulation if it were to occur.” Accordingly, a surveillance-sharing agreement with a regulated market of significant size is required to ensure that, in compliance with the Exchange Act, the proposal is “designed to prevent fraudulent and manipulative acts and practices.” In this context, the Commission has interpreted the terms “significant market” and “market of significant size” to 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 the ETP listing market 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.

Thus, a surveillance-sharing agreement must be entered into with a “significant market” to assist in detecting and deterring manipulation of the ETP, because someone attempting to manipulate the ETP is reasonably likely to also engage in trading activity on that “significant market.” Although the Winklevoss Order applied these standards to a commodity-trust ETP based on bitcoin, the Commission believes that these standards are also appropriate for an ETP based on bitcoin futures. When approving the first commodity-futures ETPs, the Commission recognized that “[i]nformation sharing agreements with primary markets trading index components underlying a derivative product are an important part of a self-regulatory organization’s ability to monitor for fraudulent and manipulative practices.” And the Commission’s approval orders for commodity-futures ETPs consistently note the ability of an ETP listing exchange to share surveillance information either through surveillance-sharing agreements or through membership by the listing exchange and the relevant futures exchanges in the Intermarket Surveillance Group.

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, 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 applicable rules and regulations.

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.

26 See id.
27 See id.
31 See Winklevoss Order, supra note 28, 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.
36 See Winklevoss Order, supra note 28, 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.
37 Securities Exchange Act Release No. 55029 (Dec. 29, 2006), 72 FR 806, 809–10 (Jan. 8, 2007) (SR–Amex–2006–76) (approval order noted that Amex’s “Comprehensive Surveillance Sharing Agreement with the ICE Futures and the LME, the NYMEX, . . . and membership in the Intermarket Surveillance Group (‘ISG’) creates the basis for the Amex to monitor fraudulent and manipulative practices in the trading of the Shares’’); Securities Exchange Act Release No. 55450 (Sept. 14, 2006), 71 FR 55230, 55236 (Sept. 21, 2006) (SR–Amex–2006–44) (approval order noted that “CME, where the futures contract for each of the current Index components is traded, is a member of the ISG” and that “all of the other trading venues on which the current Index components and CERF’s are traded are members of the ISG”’’); Securities Exchange Act Release No. 56580 (Dec. 3, 2007), 72 FR 69259, 69261 (Dec. 7, 2007) (SR–Amex–2006–96) (approval order noted that Amex has “information sharing agreements with the InterContinental Exchange, the Chicago Mercantile Exchange, and the New York Mercantile Exchange and may obtain market surveillance information from other exchanges, including the Chicago Board of Trade, London Metals Exchange, and the New York Board of Trade through the Intermarket Surveillance Group’’); Securities Exchange Act Release No. 55632 (Apr. 13, 2007), 72 FR 19987, 19988 (Apr. 20, 2007) (SR–Amex–2006–112) (approval order noted that Amex “currently has in place an Information Sharing Agreement with the NYMEX and ICE Futures” and that “if USOF invests in oil derivatives traded on markets such as the Singapore Oil Market, the Exchange represents that it will file a proposed rule change pursuant to Section 19(b) of the Exchange Act, seeking Commission approval of [Amex’s] surveillance sharing agreement with such market’’); Securities Exchange Act Release No. 54013 (June 16, 2006), 71 FR 36372, 36378–79 (June 26, 2006) (NYSE–2006–17) (approval order noted that NYSE’s “comprehensive surveillance sharing agreements with the NYMEX and ICE Futures . . . create the basis for the Amex to monitor for fraudulent and manipulative trading practices”’’ and that “all of the other trading venues on which current Index components and CERF’s are traded are members of the ISG’’).
Commission in those orders did not explicitly undertake an analysis of whether the related futures markets were of “significant size,” the exchanges proposing commodity-futures ETPs on a single reference asset or benchmark generally made representations regarding the trading volume of the underlying futures markets,34 and the market surveillance information, including customer identity information, with respect to transactions occurring on the NYM, the Kansas City Board of Trade, the LME, pursuant to its comprehensive information sharing agreements with each of those exchanges” and that “[a]ll of the other trading venues on which current Index component futures are traded (i.e., ISG’); Securities Exchange Act Release No. 63635 (Jan. 3, 2011), 76 FR 1489, 1491 (Jan. 10, 2011) (NYSEArca–2010–103) (approval order noted that “with respect to Fund components traded on exchanges that are not members of ISG or with which NYSEArca does not have a comprehensive surveillance sharing agreement”); Securities Exchange Act Release No. 66553 (Mar. 9, 2012), 77 FR 15440, 15444 (Mar. 15, 2012) (SR–NYSEArca–2012–14) (approval order noted that NYSEArca “can obtain market surveillance information, including customer identity information, from ICE [Futures] and CME, which are members of the Intermarket Surveillance Group”); Securities Exchange Act Release No. 67223 (June 20, 2012), 77 FR 38117, 38124 (June 26, 2012) (NYSEAmex–2012–24) (approval order noted that NYSEAmex “can obtain market surveillance information, including customer identity information, with respect to transactions occurring on exchanges that are members of ISG, including CME, ICE Futures US, and CME, and the Tokyo Commodity Exchange”); Securities Exchange Act Release No. 67483 (Aug. 17, 2012), 77 FR 55728, 55730 (Aug. 21, 2012) (SR–NYSEArca–2012–15) (approval order noted that “while the Fund may invest in futures contracts or options on futures contracts which trade on markets that are not members of ISG or with which [NYSEArca] does not have in place a comprehensive surveillance sharing agreement, such instruments will never represent more than 10% of the Fund’s holdings”); Securities Exchange Act Release No. 73561 (Nov. 7, 2014), 79 FR 68329, 68330 (Nov. 14, 2014) (NYSEArca–2014–102) (approval order noted that “FINRA may obtain trading information regarding trading in the Shares and Freight Futures from other market entities that are members of ISG or with which [NYSEArca] has in place a comprehensive surveillance sharing agreement” and that “CME is a member of the ISG’); Securities Exchange Act Release No. 82390 (Dec. 22, 2017), 82 FR 61625, 61631, 61634 (Dec. 28, 2017) (NYSEArca–2017–107) (approval order noted that NYSEArca “may obtain information regarding trading in the Shares and Freight Futures from markets and other entities that are members of ISG or with which [NYSEArca] has in place a CSSA’ and that “not more than 10% of the net assets of the Fund represent investments in derivative investments in Freight Futures options or Freight Futures shall consist of derivatives whose principal market is not a member of the ISG or is a market with which [NYSEArca] does not have a CSSA’”)); Securities Exchange Act Release No. 62231 (June 3, 2010), 75 FR 32288 (June 9, 2010) (SR–NYSEArca–2010–222) (notice of proposed rule change included NYSEArca’s representations that: (i) Corn futures volume on Chicago Board of Trade (“CBOT”) for 2008 and 2009 (through November 30, 2009) was 59,754,747, 754,866 contracts, respectively, and as of March 16, 2010, CBOT open interest for corn futures was 1,118,103 contracts, and open interest for near month futures was 447,554 contracts; (ii) the corn futures contract price was $18,337.50 ($3,667.50 per bushel and 5,000 bushels per contract), and the approximate value of all outstanding contracts was $20.5 billion; (iii) as of March 16, 2010, open interest in corn swaps cleared on CBOT was approximately 2,100 contracts, with an approximate value of $38.5 million; and (iv) the position limits for all months is 22,000 corn contracts, and the approximate value of positions if position limits were reached would be approximately $403.5 million (based on the $18,337.50 contract price), Securities Exchange Act Release No. 61918 (Nov. 26, 2009), 75 FR 22663, 22664 n.10 (Apr. 29, 2010); Securities Exchange Act Release No. 63610 (Dec. 27, 2010), 76 FR 199 (Jan. 3, 2011) (SR–NYSEArca–2010–101) (notice of proposed rule change included NYSEArca’s representations that: (i) As of June 14, 2010, there was VIX futures contract open interest on CFE of 88,366 contracts, with a contract price of $25.55 and value of open interest of $2,257,751,300; (ii) total CFE trading volume in 2010 in VIX futures contracts was 1,143,612 contracts, with average daily volume of approximately 3,791 contracts; (iii) total volume year-to-date (through May 31, 2010) was 1,399,709 contracts, with average daily volume of 13,456 contracts, Securities Exchange Act Release No. 63137 (Nov. 16, 2010), 75 FR 71158, 71159 n.9 (Nov. 22, 2010); Securities Exchange Act Release No. 63753 (Jan. 21, 2011), 76 FR 4963 (Jan. 27, 2011) (SR–NYSEArca–2011–10) (notice of proposed rule change included NYSEArca’s representations that: (i) Natural gas futures volume on New York Mercantile Exchange (“NYMEX”) for 2009 and 2010 (through October 29, 2010) was 47,864,639 contracts, and CBOT contracts, respectively; (ii) as of October 29, 2010, NYMEX open interest for natural gas futures was 794,741 contracts, and open interest for near month futures was 47,713 contracts, and the contract price was $40.38 ($4.038 per MMbtu and 10,000 MMbtus per contract), and the approximate value of all outstanding contracts was $32.1 billion; (iv) the position limits for all months is 12,000 natural gas contracts and the total value of contracts if position limits were reached would be approximately $484.56 million (based on the $46.380 contract price); and (v) as of October 29, 2010, open interest in natural gas swaps cleared on NYMEX was approximately 2,604,092 contracts, with an approximate value of $26.4 million (based on the $46.380 contract price), and (vi) as of December 31, 2010, open interest in natural gas swaps cleared on NYMEX was approximately 1,439,013 contracts, with an approximate value of $16,463,384,003 ($4.411 per MMbtu and 2,500 MMbtus per contract), Securities Exchange Act Release No. 63753 (Jan. 21, 2011), 76 FR 4963 (Jan. 27, 2011) (SR–NYSEArca–2011–10) (notice of proposed rule change included NYSEArca’s representations that: (i) Wheat futures volume on CBOT for 2010 and 2011 (through April 29, 2011) was 23,058,783 contracts and 8,860,135 contracts, respectively; (ii) as of April 29, 2011, open interest for wheat futures was 456,851 contracts; (iii) the wheat price contract was $40,062.50 (801.25 cents per bushel and 5,000 bushels per contract), and was approximately $1,936,951,320 in the aggregate value of all outstanding contracts was $18.3 billion; (iv) the position limits for all months was 6,500 wheat contracts and the total value of contracts if position limits were reached would be approximately $260.4 million (based on the $40,062.50 contract price); (v) soybean futures volume on CBOT for 2010 and 2011 (through April 29, 2011) was 36,962,868 contracts and 16,197,385 contracts, respectively; (vi) as of April 29, 2011, open interest for soybean futures was 572,959 contracts; (vii) the soybean price contract was $69,700.00 ($139.4 cents per bushel and 5,000 bushels per contract), and the approximate value of all outstanding contracts was $39.9 billion; (viii) the position limits for all months is 6,500 soybean contracts and the total value of contracts if position limits were reached would be approximately $451 million (based on the $69,700.00 contract price); (ix) sugar futures volume on ICE Futures for 2010 and 2011 (through April 29, 2011) was 27,846,391 contracts and 9,045,069 contracts, respectively; (x) as of April 29, 2011, open interest for sugar futures was 570,948 contracts; (xi) the sugar price contract was $24,920.00 ($22.25 cents per pound and 112,000 pounds per contract), and the approximate value of
Commission was in each of those cases dealing with a large futures market that had been trading for a number of years before an exchange proposed an ETP based on those futures.\textsuperscript{55} And where the Commission has considered a proposed ETP based on futures that had only recently begun trading,\textsuperscript{56} the Commission specifically addressed whether the futures on which the ETP was based—which were futures on an index of well-established commodity futures—were illiquid or susceptible to manipulation.\textsuperscript{57} Accordingly, the Commission examines below whether the


For example, CFTC Chair Glick noted that “futures on crude oil, Brent crude oil, natural gas, heating oil, gasoline, gas oil, live cattle, wheat, aluminum, corn, copper, soybeans, lean hogs, gold, sugar, cotton, red wheat, coffee, standard lead, feeder cattle, zinc, primary nickel, cocoa, and silver.” See Securities Exchange Act Release No. 53659 (Apr. 17, 2006), 71 FR 21074, 21080 (Apr. 24, 2006) (SR–NYSEArca–2006–17) (notice of proposed rule change to list shares of iShares GSCI Commodity-Indexed Trust). The Commission concluded that requirements of Exchange Act Section 6(b)(5) had been met because consideration of the proposal would be addressed by the arbitrage relationship between the new index futures and the existing component futures, as well as the ETLP’s listing exchanges’ comprehensive surveillance-sharing agreements not only with the market for the index futures, but also with the markets for the component futures. See Securities Exchange Act Release No. 54013 (June 16, 2006), 71 FR 36379 (June 26, 2006) (SR–NYSEArca–2006–17) (order approving listing of shares of iShares GSCI Commodity-Indexed Trust). Additionally, the approval order for the ETLP noted that, if the volume in any futures contract that was part of the reference index fell below a specified multiple of production of the underlying commodity, that contract’s weight in the index would decrease. See id. at 36374.
representations by the Exchange, and the comments received from the public, support a finding that the Exchange has entered into a surveillance-sharing agreement with a market of significant size relating to bitcoin, the asset underlying the proposed ETPs, or that alternative means of preventing fraud and manipulation would be sufficient to satisfy the requirement of Exchange Act Section 6(b)(5) that the proposed rule change be designed to prevent fraudulent and manipulative acts and practices.

2. Comments Received

One commenter states that commencing an ETP without allowing the market to adjust to the cash-settled futures products would be akin to “putting the cart before the horse” and seems to be an attempt to appease institutional investors.43

One commenter states that the market for bitcoin derivatives other than bitcoin exchange-traded futures appears to be developing and that financial institutions are reportedly moving toward launching bitcoin-related trading desks and other operations. This commenter believes that the proposed offering of both long and short ETPs raises the possibility that market makers in bitcoin-related derivatives could make two-sided markets if interest in the long and short ETPs is similar in magnitude. The commenter further believes that interest outside of the bitcoin ETPs may be sufficient to motivate market makers to maintain bitcoin derivatives desks.44 In addition, the commenter suggests that questions about bitcoin derivatives markets can be addressed through market depth analyses, discussions with potential bitcoin derivatives liquidity providers, and analyses of order and trade data across CME and CFE to determine the plausibility of simultaneous liquidity collapses on both bitcoin future markets.45

Three commenters assert that there is manipulation in the bitcoin market.46 One commenter states that it is common knowledge that the bitcoin market is being manipulated and asserts that BitConnect, which was recently shut down and had promised risk-free annual returns of up to 120%, is an example of Ponzi and multi-level marketing schemes that are too common. This commenter argues that the Commission should not send the wrong signal to bitcoin manipulators—who, the commenter asserts, currently operate with impunity—by approving a bitcoin ETP.47 Another commenter believes that the volatility of bitcoin trading does not appear to be the result of natural trading and in the long run would prevent true price discovery.48

One commenter asserts that, in an unregulated market, a small minority can manipulate the price of bitcoin and other “altcoins” and that bitcoin and other cryptocurrencies are freely manipulated by players who hold a disproportionate amount of cryptocurrencies or access to fiat currencies. This commenter cites data showing that 4.11% of bitcoin addresses own 96.53% of all the bitcoin in circulation, that the top four addresses control 3.13% of all bitcoin currently in distribution (worth over $4 billion), and that 115 individuals control bitcoin worth over $24 billion.49 In contrast, another commenter states that, although a small number of wallets may own 90% of available bitcoin, exchanges own some of these wallets and may hold bitcoin on behalf of hundreds, thousands, or millions of people.50

One commenter asserts that widespread pump-and-dump schemes organized through the messaging platform “Telegram” are evidence of manipulation.51 This commenter further cites an inquiry by then-New York Attorney General Eric Schneiderman into cryptocurrency exchanges and the use of trading “bots” on those exchanges to manipulate the market, and asserts that such activity can drive prices above fair market value by over 300%. The commenter notes the Kraken exchange’s refusal to cooperate with this inquiry and that this refusal should pose serious questions for investors and the Commission about the Kraken exchange’s operations, particularly after the Kraken exchange recently exited the Japanese market due to regulatory requirements.52

One commenter states that a commonly cited factor mitigating possible susceptibility to manipulation is the securities exchanges’ own surveillance procedures, in addition to the futures exchanges’ surveillance procedures and market surveillance and oversight by the Commodity Futures Trading Commission (“CFTC”). This commenter cites statements by the CFTC that it has the legal authority and means to police certain spot markets for fraud and manipulation through “heightened review” collaboration with exchanges, that exchanges will provide the CFTC surveillance team with trade settlement data upon request, and that the exchanges will enter into information-sharing agreements with spot market platforms and monitor trading activity on the spot markets. The commenter also states that the Gemini exchange has announced that it would use Nasdaq’s market surveillance system to monitor its marketplace.53

This commenter further asserts that market surveillance is generally a prerequisite to identifying potential market manipulation and discourages market manipulation. The commenter believes that the emergence of institutionalized market surveillance on both futures and spot markets is a positive sign for the long-term future of bitcoin markets.54 The commenter suggests that the Commission, in coordination with the CFTC, self-regulatory organizations, bitcoin futures exchanges, and bitcoin spot market platforms, could gather market surveillance data to conduct an independent analysis of trade and settlement patterns and determine whether potentially manipulative trading practices occur on bitcoin spot and futures markets.55

3. Analysis

Unlike previous proposals for bitcoin-based ETPs, the Exchange does not assert here that bitcoin prices or markets are inherently resistant to manipulation. A number of commenters, however, have noted the potential for manipulation in bitcoin markets.56 Instead, the Exchange asserts that its existing surveillance procedures (including its ability to review activity by its members) and its ability to share surveillance information with U.S. futures exchanges are sufficient to meet the requirements of Exchange Act

43 See Desai Letter, supra note 9, at 1.
44 See Desai Letter, supra note 9, at 2.
45 See id. at 2.
46 See Desai Letter, supra note 9, at 1; Fitzgerald Letter, supra note 9, at 1; Kumar Letter, supra note 9.
47 See Kumar Letter, supra note 9.
48 See Malkin Letter, supra note 9, at 1–2.
49 See Fitzgerald Letter, supra note 9, at 1–2.
50 See Rousseau Letter, supra note 9.
51 See Fitzgerald Letter, supra note 9, at 2.
52 See id. at 2.
53 See supra note 41–47 and accompanying text.
Section 6(b)(5). One commenter also asserts that the exchange’s own surveillance procedures, along with market surveillance and oversight by the CFTC, can mitigate manipulation.54

While the Exchange would, pursuant to its listing rules, be able to obtain certain information regarding trading in the Shares and in the underlying bitcoin or any bitcoin derivative through registered market makers,55 this trade information would be limited to the activities of market participants who trade on the Exchange. Furthermore, neither the Exchange’s ability to surveil trading in the Shares nor its ability to share surveillance information with other securities exchanges trading the Shares would give the Exchange insight into the activity and identity of market participants who trade in bitcoin futures contracts or other bitcoin derivatives or who trade in the underlying bitcoin spot markets, where a substantial majority of trading, the Commission concluded in the Winklevoss Order, “occurs on unregulated venues overseas that are relatively new and, generally, appear to trade only digital assets.” 56

Thus, consistent with its determination in the Winklevoss Order,57 and with the Commission’s previous orders approving commodity-futures ETPs,58 the Commission believes that the Exchange must demonstrate that it has in place a surveillance-sharing agreement with a regulated market of significant size related to bitcoin, because “[s]uch agreements provide a necessary deterrent to manipulation because they facilitate the availability of information needed to fully investigate a manipulation if it were to occur.” 59

The Exchange represents that it is able to share surveillance information with CME and CFE, which are bitcoin futures markets regulated by the CFTC, through membership in the Intermarket Surveillance Group.60 Nonetheless, the Commission must disapprove the proposal, because there is no evidence in the record demonstrating that CME’s and CFE’s bitcoin futures markets are markets of significant size.

The Order Instituting Proceedings sought comment on whether the CME and CFE bitcoin futures markets are markets of significant size,61 but the Exchange has not responded to any of the questions in the Order Instituting Proceedings, and the only analysis of the underlying futures markets the Exchange has provided in its proposed rule change are the generic statements that the market for bitcoin futures contracts “has very limited trading and operational history” and that the liquidity of these markets will depend on supply and demand, the adoption of bitcoin, and interest in the market for these futures.62 Thus, there is no basis in the record on which the Commission can conclude that the bitcoin futures markets are markets of significant size. Publicly available data show that the median daily notional trading volume, from inception through August 10, 2018, has been 14,185 bitcoins on CME and 5,184 bitcoins on CFE, and that the median daily notional value of open interest on CME and CFE during the same period has been 10,145 bitcoins and 5,601 bitcoins, respectively.63 But while these futures contract figures are readily available, meaningful analysis of the size of the CME or CFE markets relative to the underlying bitcoin spot market is challenging, because reliable data about the spot market, including its overall size, are unavailable.64

The Commission also notes that in recent testimony CFTC Chairman Giancarlo characterized the volume of the bitcoin futures markets as “quite small.” 65 Additionally, the President and COO of CFE, recently acknowledged in a letter to the Commission staff that “the current bitcoin futures trading volumes on Cboe Futures Exchange and CME may not currently be sufficient to support ETPs seeking 100% long or short exposure to bitcoin.” 66 These statements reinforce the Commission’s conclusion that there is insufficient evidence to determine that the CME and CFE bitcoin futures markets are markets of significant size.

Furthermore, while the Exchange represents that no more than 10% of the net assets of a Fund in the aggregate invested in bitcoin futures contracts will be invested in contracts whose principal market is neither a member of the Intermarket Surveillance Group nor a market with whom the Exchange has a comprehensive surveillance-sharing agreement,67 this does not function as a meaningful limitation where, as here, there is no minimum amount of a Fund’s net assets to be invested in such contracts. According to the Notice, in the event position, price, or accountability limits are reached with respect to bitcoin futures contracts, each Fund may invest in listed options on bitcoin futures contracts (should such listed options become available) and OTC swap agreements referencing bitcoin futures contracts.68 The Notice does not establish any limit on the Funds’ holdings of these other bitcoin-related derivatives; it provides no analysis of the size and liquidity of markets for those derivatives; and it does not discuss whether the Exchange has the ability to share surveillance information

53 See Notice, supra note 3, 82 FR at 61105. 54 See supra notes 48–49 and accompanying text.

This commenter also suggests that the Commission—in coordination with the CFTC, SROs, futures markets, and bitcoin spot platforms—could gather market surveillance data to independently analyze whether manipulative practices occur on bitcoin spot and futures platforms. See supra note 50 and accompanying text. As noted above, however, it is the Exchange that bears the burden to demonstrate that its proposal is designed to prevent fraudulent and manipulative acts and practices. See supra notes 23–26 and accompanying text.

55 See Notice, supra note 3, at 82 FR 61105 (“The Exchange is not informed regarding trading in the Shares, the commodity underlying futures or options on futures through ETP [Exchange Trading Permit] Holders, in connection with such ETP Holders’ proprietary or customer trades which they effect through ETP Holders on any relevant market.”).

56 Winklevoss Order, supra note 28, 83 FR at 37580.

57 See id. at 37591 (finding that “traditional means” of surveillance were not sufficient in the absence of a surveillance-sharing agreement with a regulated market of significant size related to the underlying asset).

58 See supra note 33 and accompanying text (noting previous commodity-futures ETPs where surveillance sharing in place between ETP listing exchange and underlying futures exchanges).


60 See https://www.isoportal.org/isoPortal/public/members.htm (listing the current members and affiliate members of the Intermarket Surveillance Group).

61 See Order Instituting Proceedings, supra note 7, 83 FR at 13539.

62 Notice, supra note 3, 82 FR at 61103; see also supra note 19 and accompanying text.

63 These volume figures were calculated by Commission staff using data published by CME and CFE on their websites.

64 Winklevoss Order, supra note 28, 83 FR at 37601.

65 CFTC Chairman Giancarlo testified: “It is important to put the new Bitcoin futures market in perspective. It is quite small with open interest at the CME of 6,605 bitcoin and at Cboe Futures Exchange (Cboe) of 5,569 bitcoin (as of Feb. 2, 2018). At a price of approximately $7,700 per Bitcoin, this represents a notional amount of about $94 million. In comparison, the notional amount of the open interest in CME’s WTI crude oil futures was more than one thousand times greater, about $170 billion (2,600,000 contracts) as of Feb. 2, 2018.” (note 17 and accompanying text.


67 See supra note 17 and accompanying text.

68 See Notice, supra note 3, 82 FR at 61102; see also supra note 18 and accompanying text.
with the markets for these derivatives. Thus, as to what might be a substantial proportion of the Funds’ portfolios, the Commission is unable to conclude that surveillance-sharing will be available, that the related markets are regulated, or that the related markets are of significant size.

While one commenter suggests that the market for bitcoin derivatives other than exchange-traded futures appears to be developing—and that the offering of long and short bitcoin ETPs “raises the possibility that market makers in Bitcoin derivatives could make two-sided markets if interest in both the long and short ETPs is similar in magnitude”—these speculative statements do not provide a basis for the Commission to conclude that the non-exchange-traded bitcoin derivatives market is now, or may eventually be, of significant size.

The Commission therefore concludes that Exchange has not demonstrated that it has entered into a surveillance-sharing agreement with a regulated market of significant size related to bitcoin, or that, given the current absence of such an agreement, the exchange’s own surveillance procedures described above would, by themselves, be sufficient to satisfy the requirement of Exchange Act Section 6(b)(5) that an exchange’s rules be designed to prevent fraudulent and manipulative acts and practices.69 While CME and CFE are regulated markets for bitcoin derivatives, there is no basis in the record for the Commission to conclude that these markets are of significant size. Additionally, because bitcoin futures have been trading on CME and CFE only since December 2017, the Commission has no basis on which to predict how these markets may grow or develop over time, or whether or when they may reach significant size.

Although the Exchange has not demonstrated that a regulated bitcoin futures market of significant size currently exists, the Commission is not suggesting that the development of such a market would automatically require approval of a proposed rule change seeking to list and trade shares of an ETP holding bitcoins as an asset. The Commission would need to analyze the facts and circumstances of any particular proposal and examine whether any unique features of a bitcoin futures market would warrant further analysis before approval.

C. Protecting Investors and the Public Interest

1. Comments Received

One commenter states that approval of a bitcoin ETP on a U.S.-regulated exchange would protect small traders and increase exposure to a new asset class in a safe manner.71 Another commenter states that if the Commission rejects bitcoin ETPs, it will push investors to unregulated and possibly unsafe environments.72 One commenter believes that, while the Commission should deny the proposed ETPs, it should regulate this environment to stop individual consumers from coming to financial harm.73

One commenter suggests that the Commission could address some of its concerns about the proposed ETPs by working with self-regulatory organizations, and in particular FINRA, to create bitcoin and cryptocurrency-related asset suitability requirements. In addition, this commenter suggests that targeted disclosure requirements could make investors aware of volatility, discourage retail investors from investing more than a small portion of their portfolio in cryptocurrency-related assets, and present historical scenarios to retail investors to demonstrate how an instrument such as a particular bitcoin ETP would have performed over time. This commenter believes that suitability requirements are less prescriptive than an effective ban on a class of product and that they could balance the Commission’s interest in protecting retail investors against its interest in allowing cryptocurrency-related asset markets to continue to develop in regulated markets where the Commission can observe their performance closely.74

Several commenters assert that the Commission should deny the proposed ETPs to help protect the public from exposure to financial risk from an unregulated market.75 One commenter asserts that, while the risk posed by the cash-settled futures products is mostly contained, a bitcoin ETP would expose the public to significant financial risk due to a highly volatile, unregulated, and manipulated market in bitcoin as well as cryptocurrencies in general.76 Several commenters further believe that before the Commission approves a bitcoin ETP, there should be a proper legal and regulatory framework put in place by a suitable governmental body to prevent manipulation and protect the public.77 Another commenter refers to the proposed ETPs as a “house of cards” and expresses concern that the Funds’ attempt to replicate the bitcoin futures markets, which are related to underlying cryptocurrencies that trade on unregulated exchanges, will lead to losses for retail investors, and that the inclusion of an inverse Fund will add to the risk.78

2. Analysis

The Exchange asserts that approval of the proposal would enhance competition among market participants, to the benefit of investors,79 and two commenters assert that approval would protect investors by permitting them to seek exposure to bitcoin through a safer, regulated market.80 Other commenters suggest that the Commission should either seek to regulate the underlying bitcoin markets,81 or should seek to protect investors through disclosure requirements or suitability standards, rather than disapproving a bitcoin-ETP proposal.82

Several other commenters, however, assert that approval of a bitcoin-based ETP would expose investors to risks from unregulated bitcoin markets.83 The Commission acknowledges that, compared to trading in unregulated bitcoin spot markets, trading a bitcoin-based ETP on a national securities exchange may provide some additional protection to investors, but the Commission must consider this potential benefit in the broader context of whether the proposal meets each of the applicable requirements of the Exchange Act. 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.

Thus, even if a proposed rule change would provide certain benefits to...
For the reasons discussed above, the Exchange has not met its burden of demonstrating an adequate basis in the record for the Commission to find that the proposed rule is consistent with Exchange Act Section 6(b)(5), and, accordingly, the Commission must disapprove the proposal.

D. Other Comments

Comment letters also addressed the intrinsic value of bitcoin;\(^84\) the desire of investors to gain access to bitcoin through an ETP;\(^85\) investor understanding about bitcoin;\(^86\) the volatility of bitcoin prices;\(^87\) the regulation of bitcoin spot markets;\(^88\) the operation and valuation of the proposed ETPs;\(^89\) the potential impact of ETPs on the price of bitcoin;\(^90\) and the Commission approval of the proposed Exchange Act Section 6(b)(5).\(^92\) The record before the Commission does not provide a basis for the Commission’s decision to disapprove the proposal.

E. Basis for Disapproval

The record before the Commission does not provide a basis for the Commission to conclude that the Exchange has met its burden under the Exchange Act and the Commission’s Rules of Practice to demonstrate that its proposed rule change is consistent with Exchange Act Section 6(b)(5).\(^92\)

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–2017–139 is disapproved.

For the Commission, by the Division of Trading and Markets, pursuant to delegated authority.\(^93\)

Eduardo A. Aleman, Assistant Secretary.

[FR Doc. 2018–18572 Filed 8–27–18; 8:45 am]

BILLING CODE 8011–01–P

SEcurities and exchange commission


Self-Regulatory Organizations; NYSE National, Inc.: Notice of Filing and Immediate Effectiveness of Proposed Rule Change To Amend Rule 7.31 Relating to Reserve Orders and Re-name Two Order Types

August 22, 2018.

Pursuant to Section 19(b)(1) of the Securities Exchange Act of 1934 (“Act”) and Rule 19b–4 thereunder, notice is hereby given that on August 9, 2018, NYSE National, Inc. (“Exchange” or “NYSE National”) filed with the Securities and Exchange Commission (“Commission”) the proposed rule change as described in Items I, II, and III below, which Items have been prepared by the self-regulatory organization. The Commission is publishing this notice to solicit comments on the proposed rule change from interested persons.

I. Self-Regulatory Organization’s Statement of the Terms of Substance of the Proposed Rule Change

The Exchange proposes to amend Rule 7.31 relating to Reserve Orders and re-name two order types. The proposed rule change is available on the Exchange’s website at www.nyse.com, at the principal office of the Exchange, and at the Commission’s Public Reference Room.

II. Self-Regulatory Organization’s Statement of the Purpose of, and Statutory Basis for, the Proposed Rule Change

In its filing with the Commission, the self-regulatory organization included statements concerning the purpose of, and basis for, the proposed rule change and discussed any comments it received on the proposed rule change. The text of those statements may be examined at the places specified in Item IV below. The Exchange has prepared summaries, set forth in sections A, B, and C below, of the most significant parts of such statements.

A. Self-Regulatory Organization’s Statement of the Purpose of, and the Statutory Basis for, the Proposed Rule Change

1. Purpose

The Exchange proposes to amend Rule 7.31 relating to Reserve Orders and re-name two order types.

Background

Rule 7.31(d)(1) defines a Reserve Order as a Limit or Inside Limit Order with a quantity of the size displayed and with a reserve quantity of the size (“reserve interest”) that is not displayed. The displayed quantity of a Reserve Order is ranked Priority 2—Display Orders and the reserve interest is ranked Priority 3—Non-Display Orders.\(^4\) Rule 7.31(d)(1)(A) provides that on entry, the display quantity of a Reserve Order must be entered in round lots and the displayed portion of a Reserve Order will be replenished following any execution. That rule further provides that the Exchange will display the full size of the Reserve Order when the unfilled quantity is less than the minimum display size for the order. Rule 7.31(d)(1)(B) provides that each time a Reserve Order is replenished from reserve interest, a new working time is assigned to the replenished quantity of the Reserve Order, while the reserve interest retains the working time of original order entry. Pursuant to Rule 7.31(d)(1)(C), a Reserve Order must be designated Day and may be combined with a Limit Non-Routable Order or a Primary Pegged Order.

Rule 7.31(d)(2) defines a “Limit Non-Display Order,” which is a Limit Order that is not displayed and does not route. Rule 7.31(e)(1) defines a “Limit Non-Routable Order,” which is a Limit Order that does not route.

\(^4\) The terms “Priority 2—Display Orders” and “Priority 3—Non-Display Orders” are defined in Rule 7.36(e).