Securities Regulation Daily Wrap Up, BLOCKCHAIN—SEC approves bitcoin exchange-traded products (ETPs), (Jan 10, 2024)

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The SEC's approval of bitcoin exchange-traded products provides legal certainty after previous application denials.

Ending months of speculation, the SEC issued an omnibus order approving the listing of 11 exchange-traded products (ETPs) based on bitcoin. The approvals are the first for bitcoin ETPs, meeting pent-up demand after the SEC previously denied several listing applications. The SEC appears to have reconsidered its approach to bitcoin ETPs after the D.C. Circuit vacated the SEC's rejection of an application by Grayscale Investments, finding the SEC did not adequately explain its reasoning (*Self-Regulatory Organizations; NYSE Arca, Inc.; The Nasdaq Stock Market LLC; Cboe BZX Exchange, Inc.; Order Granting Accelerated Approval of Proposed Rule Changes, as Modified by Amendments Thereto, to List and Trade Bitcoin-Based Commodity-Based Trust Shares and Trust Units*, Release No. 34-99306, January 10, 2024).

The approvals resolve significant uncertainty and are likely to boost bitcoin by providing a simpler way for investors to gain exposure.

The order may calm roiled markets, which shot up yesterday when an unknown perpetrator hacked the SEC's X social media account to falsely announce that the agency had approved bitcoin ETPs. The SEC is investigating the hack along with law enforcement authorities.

Previous court ruling. In August 2023, the D.C. Circuit vacated the SEC's rejection of Grayscale Investment's proposed bitcoin exchange-traded product. A panel agreed that the SEC acted arbitrarily and capriciously in failing to explain its different treatment of similar products.

The ruling set the stage for SEC reconsideration.

Gensler support. SEC Chair Gary Gensler said that based on the D.C. Circuit's ruling and other factors, he believes the most sustainable path forward is to approve the listing and trading of spot bitcoin ETP shares.

"If the issuer of a security and the listing exchange comply with the Securities Act, the Exchange Act, and the Commission's rules, that issuer must be provided the same access to our regulated markets as anyone else," said Gensler. He noted that the approvals are limited to bitcoin ETPs and do not pertain to other crypto assets.

Gensler highlighted protections for investors:

1. Sponsors of bitcoin ETPs will be required to provide full, fair, and truthful disclosure about the products.
2. The products will be listed and traded on registered national securities exchanges, which are required to have rules designed to prevent fraud and manipulation and are monitored by the SEC.
3. Existing rules and standards of conduct will apply to the purchase and sale of the approved ETPs, including Regulation Best Interest and fiduciary duties for investment advisers.
4. Commission staff is separately completing the review of registration statements for 10 spot bitcoin ETPs simultaneously, creating a level playing field for issuers and promoting fairness and competition.

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Gensler cautioned, however, that the SEC does not approve or endorse bitcoin itself, nor ETP custody arrangements.

“Though we’re merit neutral, I’d note that the underlying assets in the metals ETPs have consumer and industrial uses, while in contrast bitcoin is primarily a speculative, volatile asset that’s also used for illicit activity including ransomware, money laundering, sanction evasion, and terrorist financing,” said Gensler.

Other commissioner statements. Commissioners Hester Peirce and Mark Uyeda supported the approvals but outlined concerns.

Peirce called the long approval process an “unnecessary, but consequential saga.” She noted that bitcoin-based products have been trading for years under other regulatory regimes, such as bitcoin futures regulated by the CFTC.

Uyeda said he had “strong concerns” about various facets of the SEC’s order, including that the order “invents a novel, previously unarticulated standard to form the basis for approval.”

Bitcoin ETP approvals. The January 10 omnibus order approves listing for the following:

- NYSE Arca: (1) the Grayscale Bitcoin Trust and (2) the Bitwise Bitcoin ETF4 under NYSE Arca Rule 8.201-E (Commodity-Based Trust Shares), and (3) the Hashdex Bitcoin ETF5 under NYSE Arca Rule 8.500-E (Trust Units);
- Nasdaq: (4) the iShares Bitcoin Trust and (5) the Valkyrie Bitcoin Fund;
- BZX: (6) the ARK 21Shares Bitcoin ETF, (7) the Invesco Galaxy Bitcoin ETF, (8) the VanEck Bitcoin Trust, (9) the WisdomTree Bitcoin Fund, (10) the Fidelity Wise Origin Bitcoin Fund, and (11) the Franklin Bitcoin ETF.

SEC social media hack. The SEC issued the approvals one day after someone hacked the SEC’s X social media account to falsely announce that the agency had approved bitcoin ETPs.

On January 9, the SEC’s official account on the X social media platform, @SECgov, posted that the SEC had approved bitcoin exchange-traded funds for listing on national exchanges. As reported by the Washington Post, the post went up shortly after 4 pm ET.

Shortly after, Gensler announced in a personal X post that in fact, the SEC had *not* approved the listing and trading of spot bitcoin exchange-traded products. Gensler stated that the @SECgov account had been compromised and the bitcoin approval post was unauthorized.

X later confirmed that the SEC’s account had been compromised.

Reactions to SEC hack. Several legislators requested information from the SEC about the hack.

Rep. Ann Wagner (R-Mo) posted on X, “Deeply concerned with this alleged hack of the SEC’s Twitter account. This is clear market manipulation that impacted millions of investors. I plan to get more answers from Chair Gensler on this incident.”

Sen. Cynthia Lummis (R-Wyo) posted on X, “Fraudulent announcements, like the one that was made on the SEC’s social media, can manipulate markets. We need transparency on what happened.”

U.S. Sens. JD Vance (R-Ohio) and Thom Tillis (R-NC) sent a joint letter to Gensler requesting answers to six questions. One asked whether the SEC would be able to provide Congress with a report within four business days if the compromised post were the result of a cybersecurity attack.

SEC statement on hacks. An SEC spokesperson provided the following statement on January 10:

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1. The SEC continues to investigate the matter and is coordinating with appropriate law enforcement entities, including the SEC's Office of the Inspector General and the FBI.
2. The unauthorized content on the @SECGov account was not drafted or created by the SEC.
3. We will provide updates on the incident as appropriate.
4. Consistent with existing practice, any Commission action on exchange rule filings would be posted on the relevant section of the SEC's website at https://www.sec.gov/ and then in the Federal Register. As always, that would be the first public indication of a Commission's action.

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