SkyBridge's Bitcoin ETF setback showcases SEC hesitancy

Christopher Faille · January 26, 2022 · 4 minutes read

The Securities and Exchange Commission last week rejected a proposed rule change that would have allowed NYSE Arca to list and trade shares in a fund backed by Bitcoin — specifically the shares of the First Trust SkyBridge Bitcoin ETF Trust.

SkyBridge Capital Founder Anthony Scaramucci told investors not to lever Bitcoin and advocated for investors to ride out the digital currency wave in a CNBC interview from the sidelines of the iConnections Global Alts 2022 event in Miami on Tuesday.

During a digital assets panel moderated by Scaramucci, John D'Agostino, senior advisor of Coinbase, stressed that winners in the space will likely be regulated. "It took commodities futures 40 years to get where Bitcoin is in six," he said, adding that he expects an ETF product to be approved in the next three years, adding that Coinbase and other firms in the space are stepping up the pace of their interactions with the SEC.

Sometimes promoters of particular listings, facing such disappointment, go back to the drawing board: they re-work their initial proposal in a way that may address the SEC's concerns and resubmit. But many observers doubt there is much room for that here.

"Promoters can certainly keep revising as many times as they wish," said John Reed Stark, former chief of the SEC Office of Internet Enforcement, "but the exhaustive SEC order of denial is well-supported and meticulously documented."

Related Articles


A mixed verdict: No real light on Bitcoin's origin
December 20, 2021


Digital mining giant Bitdeer climbs aboard the SPAC Train
November 30, 2021

He contends that "The SEC is on very solid ground and despite the good faith, innovative and earnest efforts of an enterprising and honest SkyBridge group, the SEC seems unlikely to budge on the issue of a Bitcoin ETF, no matter who or how it is presented."

SkyBridge might also, in principle, challenge this decision in court. But that challenge would be an uphill battle. Federal statute says that in the event of such a challenge "the findings of the [SEC] as to the facts, if supported by substantial evidence, are conclusive." This forces a petitioner to meet a daunting burden: to establish that the SEC's decision had no "substantial evidence" in its favor.

The SkyBridge case is one of several Bitcoin-backed ETF/ETPs that the SEC has of late blocked. This blocking order joins the Winklevoss Order in July and the Valkyrie Order last month, among others. On the other hand, the SEC has allowed funds to trade if they are backed by Bitcoin futures contracts. In such a case the underlying asset is regulated by the Commodity Futures Trading Commission.

The most recent example of the distinction, then, is the failure of the petition filed in May 2021 by NYSE Arca, over the listing of the SkyBridge ETF, which is the brainchild of Anthony Scaramucci, a financier whose other major claim to fame is a short (10 day) stint as White House Communications Director in the early Trump administration.

The underlying plan was that the Trust would purchase and sell Bitcoin, and that shares in the Trust would represent units of fractional undivided beneficial interest in, and ownership of, the Trust. The Trust would not generally own cash or cash equivalents, though it may hold cash on a temporary basis to pay extraordinary expenses.

SkyBridge and NYSE Arca maintained that there was a mechanism in place to protect investors and the public interest from fraud, what the SEC has called a "comprehensive surveillance-sharing agreement." The idea is that manipulation typically involves playing two or more markets off against one another.

If there is a reasonable likelihood that a person trying to manipulate the value of shares in SkyBridge Trust at NYSE Arca will also have to manipulate Bitcoin or another derivative on another exchange, covering what the SEC calls a "market of significant size," then the existence of a surveillance-sharing agreement between NYSE Arca and that other exchange will go a long way to deter and prevent the fraud, in pitching their case for the safety of the proposed rule change.

NYSE Arca and SkyBridge observed that both NYSE Arca and the Chicago Mercantile Exchange (CME) are members of the Intermarket Surveillance Group (ISG). This effectively creates a surveillance-sharing agreement between NYSE Arca and CME.

The SkyBridge proposal was filed on May 6 and published for comment on May 27. The SEC instituted proceedings on approval in August. On Nov. 19 it said that it would be taking more time to reach its conclusion.

On Jan. 20, 2022, the SEC announced its conclusion that NYSE Arca has not met its burden under the statute and the SEC's rules of practice to demonstrate that its proposal is consistent with an exchange's duty to "prevent fraudulent and manipulative acts and practices" and to "protect investors and the public interest."

Specifically, the SEC did not agree that the CME's 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."

The CME is not so large a player, that is, that one can presume that someone wanting to manipulate SkyBridge Trust's shares at NYSE Arca would do so by way of playing them off of the Bitcoin futures market.

Accordingly, the ISG/CME connection is not an adequate guard against fraud and the proposing exchange has presented, in the SEC's view, no "other means to prevent fraudulent and manipulative acts and practices … sufficient to justify dispensing with the requisite surveillance-sharing agreement." The proposal was not approved.

SkyBridge did not respond to a request for comment.

Additional reporting by Susan Barreto.

Tags: Crypto

Share

Christopher Faille

Christopher Faille has written on a variety of legal, regulatory, and financial issues for decades. He is the author of "The Decline and Fall of the Supreme Court" (1995), for example, and the coauthor, with David O'Connor, of "Basic Economic Principles" (2000). He was an early reporter with Lipper HedgeWorld and has contributed to Forbes and to the Hedge Fund Law Report.

Login

Log out

Recent


Blackstone AUM soars 42% in 2021
January 27, 2022


Private market investors consider net zero minus the divestment
January 27, 2022


Asia private equity FoFs attracts $2bn
January 27, 2022


Ropes & Gray names alts vet as new partner
January 27, 2022


GTCR closes Strategic Growth fund at $2bn
January 26, 2022

Search ... Search