Submitted electronically via sec.gov

April 18, 2022

Vanessa Countryman
Secretary
U.S. Securities and Exchange Commission
100 F Street NE
Washington DC 20549-1090


Dear Ms. Countryman:

The Association for Digital Asset Markets (“ADAM”)\(^1\) appreciates the opportunity to comment on the Securities and Exchange Commission (“SEC”) request on the SECs proposed changes to Regulation ATS, Rule 3b-16, and Regulation SCI, all of which are adopted under the Securities Exchange Act of 1934 (“Exchange Act”).\(^2\) As discussed below, while ADAM generally supports the SEC's investor protection and public interest goals, we do not believe that the Proposal, as drafted, advances those goals, at least with respect to the nascent digital asset industry. In particular, the revisions to Exchange Act Rule 3b-16 that would capture a vast array of new technologies, and the persons who develop and advance those technologies, has the real potential of chilling further development in the United States of digital asset technologies at a time when U.S. investors and the U.S. economy cannot afford to take a back to seat to these innovations. While ADAM and its members generally agree that regulation in the digital asset

---

\(^1\)ADAM is a broad-based industry group that includes a wide variety of market participants, including trading platforms, custodians, investors, asset managers, traders, liquidity providers, and brokers. Our members are firms that are active in digital asset markets or seek to participate in those markets. ADAM members include: Anchorage Digital, N.A.; BitGo; BitOoda; BlockFi; BTIG; CMT Digital; CoinFund; Cumberland; Digital Asset Council of Financial Professionals; Dunamis Trading; Eventus Systems; Fireblocks; FTX.com; FTX.us; Hxro Foundation; Galaxy Digital; Genesis; Grayscale; GSR; HRT; Multicoin Capital; Oasis Pro Markets; Parataxis; Paxos; Robinhood Crypto; Sarson Funds; Solidus Capital; Symbiont; Symphony Communications; WisdomTree; and XBTO. ADAM law firm partners include: Anderson Kill; DLA Piper; DLx Law; Mayer Brown LLP; McGonigle, P.C.; and Morgan Lewis.

space can advance investor protections, the public interest, and help maintain the United States’ position as a global leader in financial technology, the wrong approach can leave the United States at a long-term competitive disadvantage as it has in the past. To this end, we encourage the SEC to specifically exclude digital assets as coming the Proposal’s scope and instead work with its fellow regulators to develop a comprehensive approach to the regulation of digital assets.

About ADAM

ADAM is a private, non-profit, membership-based association of firms operating in the digital asset markets and is a standards-setting body and self-governing association committed to promoting market integrity and best practices. ADAM works with leading financial firms, entrepreneurs, and regulators to develop industry best practices that facilitate fair and orderly digital asset markets. In this vein, ADAM’s objectives are to: (1) protect market participants from fraud and manipulation; (2) provide clear standards for efficient trading, custody, and the clearing and settlement of digital assets; (3) encourage professionalism and ethical conduct by market participants; and (4) increase transparency and provide information to the public and governments about digital asset markets. In furtherance of this, ADAM released a principles-based Code of Conduct (Code)4 in late 2019 that sets certain standards of professional conduct for ADAM members. In particular, the Code addresses the following areas:

- Compliance and Risk Management
- Market Ethics
- Conflicts of Interest
- Transparency and Fairness
- Market Integrity
- Custody
- Information Security and Business Continuity
- Anti-Money Laundering and Countering the Finance of Terrorism

Every ADAM member agrees to adhere to the Code of Conduct. The goal is to bring professional standards into the nascent but rapidly-growing digital asset markets, to develop trust in those markets so that they can flourish.

Our members are at the cutting edge of innovation through the use of new technologies, such as blockchain. However, they recognize that proper regulation and conduct are essential to their businesses and to the development of a sustainable marketplace and public trust. They believe that a diverse financial ecosystem is a source of strength, and they aim to use their technology to

---

3 For example, 5G technology is often cited as an example where the U.S. was left behind other jurisdictions because of governmental inaction. See, e.g., https://www.cnbc.com/2022/02/17/us-well-behind-china-in-5g-race-ex-google-ceo-eric-schmidt-says.html

4 The Code is available at http://www.theadam.io/code/.
find new ways of reaching consumers and work within the current financial system to improve efficiencies.\(^5\)

ADAM and its members are committed to working with lawmakers and regulators to promote responsible innovation in the digital asset space in a manner that expands the availability of financial services. We welcome a clear regulatory picture because our members seek full compliance.

**Overview Of Comments**

While ADAM believes that a measured regulatory framework can increase the safety and soundness of the digital asset marketplace, we also believe that regulatory overreach can hinder a promising new technology that have far reaching positive implications. Furthermore, we believe that regulation of the digital asset market raises novel issues that require careful deliberation to the specific factors at hand. In this regard, while ADAM appreciates and respects the SEC’s authority to regulate trading venues as they evolve, ADAM currently cannot support the Proposal in its current form as it applies to so-called Communication Protocol Systems. This is because the proposed revisions to Exchange Act Rule 3b-16 that would capture Communication Protocol Systems within the meaning of an “exchange” could potentially capture the vast majority of digital asset marketplaces. Given the lack of certainty regarding the regulatory status of digital assets and the very notable lack of discussion regarding digital assets in the Proposal, ADAM believes that:

1. The blanket application of the securities exchange regulatory framework to digital assets would be premature and imprudent. In this sense, it is important to consider that not all digital assets are securities, and some digital assets may be securities and defined as such in the future. Still, due to the unique and malleable nature of digital assets, not all exchange requirements will make sense for the trading of digital asset securities. As such, the proposal should expressly exclude digital asset securities until the White House Executive Order on digital assets concludes and Congress produces a legislative public policy framework providing clarity on what digital assets are securities and which are not.

2. There are some legitimate questions as to whether the application of the Proposal to digital assets adheres with the requirements of the Administrative Procedure Act (APA).

3. If adopted as proposed without a carve out for digital assets, the proposed revisions to Exchange Act Rule 3b-16 will hinder innovation, competition, and capital formation in an industry in which the United States cannot afford to cede ground to other countries.

In addition to these comments that are discussed in greater detail below, ADAM and its members are always available to provide information and insights to the SEC and its staff regarding the operation of the digital asset marketplace.

---

Overview of Digital Asset Platforms

Digital asset platforms involve a wide range of stakeholders, including miners and other nodes, that provide actual computing resources recording and verifying a digital ledger, dApp developers that launch distributed applications, users ranging from hobbyists to institutional investors, and off-chain service providers that provide reporting and monitoring services, and cross-chain communication. Digital asset platforms benefit from a number of technical advancements stemming from transparent market information to unique transaction methods, which allows many new types of transactions to occur.

An exciting part of this new technology is “DeFi” or Decentralized Finance. This nascent industry aims to leverage blockchain and other digital asset technology to provide saving, lending, liquidity, and asset transfer services for digital asset users. The added transparency provided by on-chain transactions and open participation is attractive to many users disillusioned with trades in centrally managed, unauditable dark pools, while new and existing financial intermediaries appreciate the opportunity DeFi provides for increased automation and associated efficiencies.

The participants and infrastructure for these projects vary widely, but may include:

- **“dApps” or “Smart Contracts.”** These are autonomous code that function like computer programs shared across the applicable distributed ledger; they can track, process, receive and send network transactions that may (but are not required to) relate to digital assets interoperable with the DeFi platform.

- **“DAOs” or Decentralized Autonomous Organizations.** A special kind of smart contract platform that allows users to control certain aspects of the administration of funds under management by the DAO. For example, in the context of a DeFi platform, a DAO may control features offered on the DeFi platform or the migration of the DeFi platform to a new set of contracts.

- **Governance Tokens.** Tokens issued by smart contracts that allow holders to vote on DAO administration. In addition to voting rights, these tokens may be resold for other digital assets or may have certain powers in respect of the DAO.

- **Stablecoins.** Tokens issued with the aim of maintaining a 1:1 exchange rate (or an approximation thereof) with another asset, such as USD. USDP and USDC are all examples of stablecoins.

- **Oracles:** Reporting services that link information from within or without a blockchain to dApps and smart contracts on the blockchain. Frequently, oracles will report the prices for digital assets, either curated internally or from centralized exchanges.

- **AMM or Automated Market Makers.** Algorithms within smart contracts to provide pricing for buying and selling digital assets managed by the DeFi platform. AMMs may rely on Oracles or may have internal pricing models that may be reactive to arbitrage.

- **“Wrapped” tokens or coins.** Wrapping refers to receiving one digital asset and reissuing it at a 1:1 basis as another "wrapped" form. The wrapped form is typically more compatible
with user wallets and widely available smart contracts. For example, ETH, the native unit on the Ethereum blockchain, is expensive to transact in. wETH is issued by an ERC-20 type smart contract that trades 1:1 with actual ETH and can be traded more easily. wBTC is "wrapped bitcoin" issued by a smart contract on the Ethereum Blockchain when a user sends native BTC to a particular contract on the bitcoin blockchain.

- **Guardians.** Guardians are monitoring programs, like Oracles, that monitor transactions across different blockchains.

- **Staking.** Blockchains or certain DeFi projects may offer rewards or opportunities to pool resources to provide staking services. For example, a blockchain utilizing proof of stake validation lets users participate in verifying the blockchain by staking the native token, providing a reward if they propose and approve valid smart contracts. Users may pool their tokens for shared staking rewards.

- **Nodes.** Nodes typically refer to a computer resource involved in validating transactions or providing information, such as pricing information, to the blockchain (like an Oracle). More generally, nodes also refer to an instance of operating software to interacting with a blockchain, whether as a validator, application or end user.

- **Project Administrators.** Several DeFi projects also provide limited administrative powers to certain trusted individuals, such as the ability to freeze all trading and liquidate assets under management. For some DeFi projects, there are no Project Administrators or the powers granted to those Project Administrators are significantly restricted.

- **Liquidity Providers.** Providers of digital assets for use by a smart contract. Typically, they are compensated via the fees charged by the smart contract or in governance tokens.

Using these and other tools, DeFi projects have created a variety of projects with immense potential. Many projects have innovative pricing models built around trade between like products, nodes that report off-chain exchange prices natively, and other solutions are being developed rapidly. Innovation in this area is proceeding rapidly and globally, with the precise contours of this technology impossible to determine at this time.

**Overview of Proposed Changes to Exchange Definition**

Section 3(a)(1) of the Exchange Act defines an “exchange” as follows:

> [A]ny organization, association, or group of persons, whether incorporated or unincorporated, which constitutes, maintains, or provides a market place or facilities for bringing together purchasers and sellers of securities or for otherwise performing with respect to securities the functions commonly performed by a stock exchange as that term is generally understood, and includes the market place and the market facilities maintained by such exchange.

Persons meeting the definition of an exchange are required by Exchange Act Section 5 to register with the SEC under Exchange Act Section 6. As self-regulatory organizations (SROs),
exchanges registered under Section 6 are subject to a panoply of requirements in Sections 5, 6, and 19 of the Exchange Act.\(^6\)

In light of technological advances that resulted in market participants using non-exchange facilities to effect transactions, the SEC in 1998 adopted Rule 3a-1, Rule 3b-16, and Regulation ATS under the Exchange Act to provide a new framework for regulating venues that, in the SEC’s view, were the equivalent of exchanges.\(^7\) As explained by the SEC in the Proposal, Rule 3b-16 was adopted to further define terms used in the definition of an exchange to capture some of these exchange equivalents operating at the time of the rule's adoption. As currently in effect, paragraph (a) of Rule 3b-16 brings within the definition of "exchange" an organization, association, or group of persons that: (1) brings together the orders for securities of multiple buyers and sellers; and (2) uses established, nondiscretionary methods (whether by providing a trading facility or by setting rules) under which such orders interact with each other, and the buyers and sellers entering such orders agree to the terms of a trade.\(^8\)

As discussed in the Proposal, Rule 3b-16 would specifically be revised as follows:

(a) an organization, association, or group of persons shall be considered to constitute, maintain, or provide “a market place or facilities for bringing together purchasers and sellers of securities or for otherwise performing with respect to securities the functions commonly performed by a stock exchange,” as those terms are used in section 3(a)(1) of the Act, (15 U.S.C. 78c(a)(1)), if such organization, association, or group of persons:

(1) Brings together the orders for securities of multiple buyers and sellers of securities using trading interest; and

(2) Uses \textit{Makes available} established, non-discretionary methods (whether by providing a trading facility or communication protocols or by setting rules) under which such orders buyers and sellers can interact with each other, and the buyers and sellers entering such orders agree to the terms of a trade.

\(^6\) These obligations are onerous, and include such things as: (i) Setting, administering compliance with, and examining for exchange member standards of conduct for exchange member; (ii) coordinating with other SROs with respect to the dissemination of consolidated market data; (iii) generally taking responsibility for enforcing the exchange’s own rules, and the provisions of the Exchange Act and the rules and regulations thereunder; (iv) filing an application for registration on Form 1 and having such application approved by the SEC after notice and comment period; (v) having operational capabilities and being able to comply and enforce compliance by its members, and persons associated with its members, with the federal securities laws and the rules of the exchange; (vi) establishing rules by filing proposed rule changes with the SEC (subject to a notice and comment period), with such rules generally: (a) designed to prevent fraud and manipulation, promote just and equitable principles of trade, and protect investors and the public interest; (b) providing for the equitable allocation of reasonable fees; (c) prohibiting unfair discrimination; (d) not imposing any unnecessary or inappropriate burden on competition; and (e) with very limited exceptions, allowing any broker-dealer to become a member (vii) publicly disclosing important information about national securities exchanges, such as trading services and fees; (viii) establishing and maintaining listing standards for securities; and (ix) generally, and unlike clearing agencies for example, exchanges are only permitted to have broker-dealers as members.


\(^8\) A system currently has to meet both parts of Rule 3b-16(a) to be deemed an exchange.
These revisions are specifically targeted at so-called *Communication Protocol Systems* with the intended effect of greatly expanding the types of platforms that come within the meaning of a securities exchange. In doing so, the proposed amendments add "communication protocols" as an established method that an organization, association, or group of persons can provide to bring together buyers and sellers of securities. In the SEC’s view, systems that bring together buyers and sellers of securities may function as exchange marketplaces of securities without orders or a trading facility for orders to interact. The SEC then stated that communication protocols, which can be applied to various technologies and connectivity, generally use non-firm trading interests as opposed to orders to prompt and guide buyers and sellers to communicate, negotiate, and agree to the terms of the trade.

Although the SEC does not specifically define a Communication Protocol System, it does state that it would include “a system that offers protocols and the use of non-firm trading interest to bring together buyers and sellers of securities.” The SEC further describes these systems as using various technologies and connectivity, generally offering the use of non-firm trading interest and established protocols to prompt and guide buyers and sellers to communicate, negotiate, and agree to the terms of the trade without relying solely on the use of orders. The Proposal further describes certain platforms that currently are outside the scope of exchange regulation but which it views as Communication Protocol Systems, including: (i) “Request-for-Quote” (RFQ) Systems; (ii) so-called stream axes (i.e., indication-of-interest (IOI) systems); (iii) conditional order systems; and (iv) negotiation systems. The SEC further stated that protocols that a system offers may take many forms and could include:

- setting minimum criteria for what messages must contain;
- setting time periods under which buyers and sellers must respond to messages;
- restricting the number of persons to whom a message can be sent;
- limiting the types of securities about which buyers and sellers can communicate;
- setting minimums on the size of the trading interest to be negotiated; or
- organizing the presentation of trading interest, whether firm or non-firm, to participants.

In furtherance of bringing Communication Protocol System within the meaning of a securities exchange, proposed paragraph (e) of Rule 3b-16 would then define a “trading interest” to mean “an order as the term is defined under paragraph (c) of this section or any non-firm indication of a willingness to buy or sell a security that identifies at least the security and either quantity, direction (buy or sell), or price.” The SEC did not articulate how a willingness to buy or sell would be evidenced, or the features that would make an IOI non-firm. The SEC is also deleting the reference to *multiple* buyers and sellers because it believes that the term “multiple” could be misconstrued to mean that RFQ systems, for example, do not meet the criteria of Rule 3b-16(a) because a transaction request typically involves one buyer and multiple sellers or one seller and

---

9 Proposal 5 n.5.

10 Proposal 18-19.
multiple buyers. The SEC is also replacing the phrase “uses established, non-discretionary methods” with the phrase “makes available established, non-discretionary methods.” According to the SEC, this change is designed to capture established, non-discretionary methods that an organization, association, or group of persons may provide, whether directly or indirectly, for buyers and sellers to interact and agree upon terms of a trade.

Importantly, and of particular concern to ADAM, are the SEC’s views regarding the term “makes available.” In the Proposal, the SEC expressed its belief that the term “makes available” would be applicable to Communication Protocol Systems because such systems take a more passive role in providing to their participants the means and protocols to interact, negotiate, and come to an agreement. The SEC further expressed the view that the term "makes available" is intended to make clear that, in the event that a party other than the organization, association, or group of persons performs a function of the exchange, the function performed by that party would still be captured for purposes of determining the scope of the exchange under Exchange Act Rule 3b-16. Further, the SEC stated that using the term "makes available" will help ensure that the investor protection and fair and orderly markets provisions of the exchange regulatory framework apply to all the activities that consist of the system that meets the criteria of Rule 3b-16(a), notwithstanding whether those activities are performed by a party other than the organization that is providing the marketplace.

Notably, and of relevance to this comment letter, the SEC expressed its belief in the Proposal that it is important for any system that falls within the criteria of Rule 3b-16(a) to be subject to the exchange regulatory framework, notwithstanding how thinly traded or novel a security may be, and participants on such systems should be able to avail themselves of the same benefits that participants on registered exchanges or ATSs receive. Although the SEC stated that the proposed amendments to Rule 3b-16(a) do not change the SEC’s interpretation of the statutory definition of “exchange” as applying to all securities, the SEC makes no mention of digital assets in the Proposal, let alone in the economic analysis. The general understanding among market participants and the digital asset industry is that this broad reference to all securities is meant to capture digital assets, potentially not naming which digital asset is a digital asset security, without the benefit of a thorough analysis regarding such instruments.\textsuperscript{11,12}

\textsuperscript{11}In Commissioner Peirce and Commissioner Roisman’s July 14, 2021 dissent, In the Matter of Coinschedule, the Commissioners expressed disappointment that “the Commission’s settlement with Coinschedule did not explain which digital assets touted by Coinschedule were securities, an omission which is symptomatic of our reluctance to provide additional guidance about how to determine whether a token is being sold as part of a securities offering or which tokens are securities.”


\textsuperscript{12}To this end, we note that the SEC has previously adopted rules and rule changes where it retroactively has attempted to apply a rule’s requirements to a class of securities that were not contemplated and which the industry did not include within scope for almost 50 years without objection from the SEC or FINRA. More specifically, the SEC adopted Rule 15c2-11 in the 1971, which addresses a broker-dealer's obligation to have a reasonable basis for believing that issuers of securities being quoted in the OTC market have kept financial and other information current and made it publicly available. Until the SEC adopted amendments to the rule in 2020, the industry generally limited application of Rule 15c2-11 to equity securities without apparent objection from the SEC or FINRA. It was not passing references to fixed-income securities in 2020, and industry concern over the broadened scope of Rule 15c2-11, that the SEC in earnest expressed the view that Rule 15c2-11 applied to fixed-income securities,
Application Of Exchange Regulatory Framework to Digital Assets Is Premature

While we can appreciate the SEC’s goals in bringing so-called Communication Protocol Systems within the regulatory framework applicable to securities exchange, we believe it is entirely premature for the SEC to potentially include digital assets within this framework through a vague reference to the statutory definition of a “security.” This approach is especially premature given that (1) there is still significant uncertainty – exacerbated by the SEC’s shifting views – regarding the extent to which digital assets come within the federal securities laws, (2) the appropriate regulatory treatment of digital assets is still under active consideration by the legislative and executive branches, and (3) due to digital assets’ unique nature, not all exchange requirements make sense for the trading of digital asset securities. As such, the proposal should expressly exclude digital assets until the White House Executive Order review concludes and Congress produces a legislative public policy framework providing clarity on what digital assets are securities and which are not.

As the SEC is well aware, it and its staff have been very active in issuing guidance and bringing enforcement actions related to those digital assets which the SEC views as securities. On its website, it provides a running tally of the various enforcement actions it brought related to digital assets and initial coin offerings, with over 100 actions brought as of the date of this letter according to some industry analysis. While the SEC has brought a great deal of actions, the volume of these actions should not be construed as reflecting a conclusive view regarding the SEC’s authority and jurisdiction over digital assets. In this respect, there has been a shifting landscape regarding the SEC’s exact authority over digital assets that leads to market confusion, but that also can undermine the SEC’s own jurisdicational efforts in this space.

For example, in a widely publicized 2018 speech before the Yahoo Finance All Markets Summit: Crypto, William Hinman, then Director of the SEC’s Division of Corporation Finance, outlined his views regarding the securities analysis undertaken when assessing when a digital asset is construed as a security. In that speech, Director Hinman focused on the manner in which a digital asset is sold, and analyzed those efforts under the investment contract test outlined in SEC v. W.J. Howey Co. and its progeny. Director Hinman then stated that:

…. when I look at Bitcoin today, I do not see a central third party whose efforts are a key determining factor in the enterprise. The network on which Bitcoin functions is operational and appears to have been decentralized for some time, perhaps from inception. Applying the disclosure regime of the federal securities


13 [https://www.sec.gov/spotlight/cybersecurity-enforcement-actions](https://www.sec.gov/spotlight/cybersecurity-enforcement-actions)


laws to the offer and resale of Bitcoin would seem to add little value. And putting aside the fundraising that accompanied the creation of Ether, based on my understanding of the present state of Ether, the Ethereum network and its decentralized structure, current offers and sales of Ether are not securities transactions. And, as with Bitcoin, applying the disclosure regime of the federal securities laws to current transactions in Ether would seem to add little value.

Thus, the industry operated under the assumption that Bitcoin and Ether were not securities. However, as recently as in February 2022, staff from the SEC’s Division of Enforcement have, according to reports, disavowed the Hinman Speech as “personal opinion,” reportedly stating during oral argument in SEC v. LBRY, Inc. that the SEC has not asserted that Bitcoin and Ethereum are not securities. These reports, if accurate, further the main defense in another case that the SEC is currently litigating. In that case, the court denied the SEC’s motion to strike defendant’s affirmative defense that it violated the securities laws, which is the SEC had failed to provide fair notice that its conduct was in violation of law and this in violation of due process. That case has the potential to significantly curtail the SEC's enforcement approach to digital assets if the court agrees that the SEC did not provide market participants with fair notice regarding its views of digital assets. Given that the SEC staff now appear to be distancing the SEC from the Hinman Speech, it is clear that market participants are left further in the dark regarding the SEC’s jurisdiction over digital assets.

Another recent case out of the Southern District of New York dismissed a case against a global crypto exchange and, in the process, questioned timelines to file complaints in court and the jurisdiction of various digital asset providers. In the case, the U.S. District Judge wrote that the investors suing the exchange for losses and failure to disclose risk, in fact, sued too late, having waited more than one year after their purchases. In addition, the judge wrote, “Plaintiffs must allege more than stating that plaintiffs bought tokens while located in the US and that title passed in whole or in part over servers located." This implied that domestic securities laws did not apply because the exchange was not a domestic exchange, even if it used Amazon computer servers and Ethereum blockchain computers in the United States.

---

17 In March 2021, the SEC commenced an action against LBRY for allegedly offering unregistered securities to raise a total of $6.2 million starting in 2016. See SEC v. LBRY, Inc. Civil Action No. 1:21-cv-00260 (D.N.H. filed March 29, 2021). The SEC’s press release regarding this case is available at: https://www.sec.gov/litigation/litreleases/2021/lr25060.htm?utm_medium=email&utm_source=govdelivery. According to the SEC’s complaint, from at least July 2016 to February 2021, LBRY, which offers a video sharing application, sold digital asset securities called "LBRY Credits" to numerous investors, including investors based in the US.

18 https://mobile.twitter.com/LBRYcom/status/1496586670954713090.


22 Crypto exchange Binance wins dismissal of U.S. lawsuit over digital token sales (March 31, 2022)
The uncertainty regarding the SEC’s authority over digital assets, including the SEC staff’s apparent shift regarding the status of Bitcoin and Ethereum, is further complicated by the fact that the status of digital assets is still being actively considered by other branches of government. For instance, in November 2021, the President’s Working Group on Financial Markets (PWG), along with the Federal Deposit Insurance Corporation (FDIC) and the Office of the Comptroller of the Currency (OCC), released a report on the risks and legislative recommendations for stablecoins, a form of digital assets that are designed to maintain a stable value relative to a national currency or other reference assets. Although there were press reports leading up to the publishing of the PWG Report indicating that the SEC won concessions that would have made it the top regulator for stablecoins, the PWG Report stated otherwise. Instead, the report recommended, among other things, that stablecoin issuers be insured depository institutions, effectively recommending that they be subject to banking regulation as opposed to securities regulation. And rather than provide the SEC any additional comfort regarding its authority over digital assets, the PWG Report acknowledged that the SEC and other regulators could have a role in addressing prudential risks associated with stablecoins. If anything, the PWG Report reflects that the status and proper regulatory framework for digital assets is still under active consideration. In addition, the Commodity Futures Trading Commission also has jurisdiction in this space.

These themes were similarly echoed in President Biden’s March 9, 2022 Executive Order outlining his administration’s policy objectives with respect to digital asset regulation. The Executive Order highlights the absence of uniform oversight and standards applicable to the industry, stating that such absence may result in inadequate protections for sensitive financial data, custodial and other arrangements relating to customer assets and funds, or disclosures of risks associated with investments in digital assets. In addition, the Executive Order outlines the six policy objectives of the U.S. with respect to digital assets and notably, does not single out anyone regulatory agency as having primary or significant authority over digital assets. Rather, it encourages coordination among the various agencies in achieving the objectives of the Executive Order, with the SEC listed as one of many agencies that could play a role.

In addition to the executive branch, the legislative branch also is actively considering the appropriate regulatory treatment of digital assets both from an oversight and legislative standpoint. An example of recent oversight questioning was the recent bipartisan letter from the House of Representatives questioning the role of the Division of Enforcement and Division of


26 These policy objectives include: (1) customer, investor and business protections; (2) financial stability and systemic risk mitigation; (3) illicit finance mitigation and national security risks; (4) ensuring continued leadership in the global financial system and economic competitiveness by the U.S.; (5) financial inclusion; and (6) responsible development and use of digital assets.
Examination authorities to obtain information related to cryptocurrency and blockchain firms, which the Representatives questioned if those authorities are better suited to the SEC’s divisions charged with seeking public commentary as part of the rulemaking process. On the legislative side recent efforts include but are not limited to: (1) the Infrastructure Investment and Jobs Act (H.R. 3684); (ii) Digital Asset Market Structure and Investor Protection Act (H.R. 4741); (iii) the Token Taxonomy Act (H.R. 2144), (iv) the Bipartisan Digital Commodity Exchange Act. (v) a foreshadowed bipartisan bill from Senators on the Senate Committee on Banking, Housing, and Urban Affairs and the Senate Committee on Agriculture, Nutrition, and Forestry, and (vi) a number of bills relating to the treatment of stablecoins.

As described above in the "Overview of Digital Asset Platforms" section, there are a variety of platforms in the digital asset space, each with unique characteristics. These characteristics may share similarities with some trading platforms, but they have several differences, such as on-blockchain settlement, different custody considerations, and peer-to-peer exchange. It is unclear how many of these platforms would practically reconcile with a number of SEC rules developed in analog times, requiring paper settlement. Applying a traditional framework without further guidance or a transparent no-action process does not make practical sense.

For the reasons outlined above, we believe that it is premature of the SEC to include digital assets within the scope of the exchange regulatory framework until such time as there is a better understanding regarding the appropriate regulatory approach for such assets.

Proposal Adherence to the Administrative Procedure Act and Other Legal Requirements

ADAM and its members believe that the Proposal, as drafted, raises concerns under the APA and other requirements applicable to agency rulemaking.

As the SEC is well aware, the APA applies to all executive branch and independent agencies and prescribes procedures for agency rulemakings and adjudications. In addition, it outlines standards for judicial review of final agency actions. Section 553 of the APA outlines notice-and-comment rulemaking procedures, and is intended to provide the public with a meaningful opportunity to comment on proposed rules. Although a 30-day comment period is typically regarded as the minimum requirement, the legislative history of the APA indicates that longer periods are warranted for matters “of great importance, or those where the public submission of facts will be either useful to the agency or a protection to the public, should naturally be


 accorded more elaborate public procedures.”

To this end, the Obama Administration recognized the importance of having the meaningful public comment on proposed rulemakings and generally instituted 60-day comment periods. Even longer comment periods are needed where rulemakings are complex or where an agency is engaged in multiple rulemakings at or near the same time. Given that this rulemaking is complex and that the SEC has multiple rulemakings occurring in parallel, ADAM believes that the substantive changes to Rule 3b-16 require at least a 90-day comment period from publication in the Federal Register, a point that ADAM conveyed in its February 2, 2022 letter to the SEC. Simply, without this additional time, ADAM and other commenters are unable to fully provide the information and input that the Proposal itself recognizes are necessary for the SEC to properly understand the impact of its action and to tailor the rule accordingly.

In addition to the inadequate notice-and-comment period, ADAM believes that there are other important respects in which the Proposal departs from the legal requirements governing agency rulemaking. Under the APA, an agency must “make its views known to the public in a concrete and focused form so as to make criticism or formulation of alternatives possible” and “describe the range of alternatives being considered with reasonable specificity.” Here, across more than 650 pages, the SEC makes no mention of digital assets. That is likely because digital assets are not covered by—and should not be covered by—the Proposal. The SEC should make that limitation clear. In fact, in the context of this rulemaking, it would be unreasonable and unlawful for the SEC to issue a final rule that did apply to digital assets. Because the SEC has failed to give “fair notice” that digital assets are within the scope of the proposed rule, it would violate the APA to extend the final rule to such assets.

The SEC’s failure to address digital assets in the text of the Proposal creates other deficiencies in the rule, particular in the SEC’s economic analysis, unless digital assets are plainly excluded. The Exchange Act requires the SEC to determine whether a rulemaking will “promote

---

31 Administrative Procedure Act: Legislative History, S. Doc. No. 248, at 259 (1946)
32 Executive Order 13563, Improving Regulation and Regulatory Review (Jan. 18, 2011), 76 Fed. Reg. 3821 (Jan. 21, 2011); see also Executive Order 12866, Regulatory Planning and Review (Sept. 30, 1993), 58 Fed. Reg. 51735 (Oct. 4, 1993) (“each agency should afford the public a meaningful opportunity to comment on any proposed regulation, which in most cases should include a comment period of not less than 60 days”); Memorandum for the Heads of Executive Departments and Agencies, Modernizing Regulatory Review (Jan. 20, 2021), 86 Fed. Reg. 7223 (Jan. 26, 2021) (“This memorandum reaffirms the basic principles set forth in [Executive Order 12866] and in Executive Order 13563 of January 18, 2011 (Improving Regulation and Regulatory Review), which took important steps towards modernizing the regulatory review process. When carried out properly, that process can help to advance regulatory policies that improve the lives of the American people.”).
36 Portland Cement Ass’n v. EPA, 665 F.3d 177, 192 (D.C. Cir. 2011).
efficiency, competition, and capital formation.” The Exchange Act additionally prohibits any rulemaking that “would impose a burden on competition not necessary or appropriate in furtherance of the purposes” of the statute. Unless the SEC “apprise[s] itself—and hence the public and the Congress—of the economic consequences of a proposed regulation,” the “promulgation of the rule [is] arbitrary and capricious and not in accordance with law.” Here, the SEC’s economic analysis fails even to mention digital assets—let alone assess the impact of the Proposal on this important and growing sector. Given the absence of any analysis to digital assets, it would be unreasonable for the SEC to apply the rule to digital assets. In fact, given the uncertainty the Proposal has created, it would be unreasonable to adopt a final rule without making clear that the rule would not apply to digital assets. If the SEC fails to issue that clarification, the proposed rule would have serious negative repercussions in the digital assets market—economic impacts that the SEC has failed to consider.

The SEC’s failure to address these economic effects in the Proposal constrains the SEC’s ability to address them later in this rulemaking. Under the notice-and-comment requirements of the APA, an agency cannot develop a rule using secret data, which means that “the most critical factual material that is used to support the agency’s position” must be “made public in the proceeding and exposed to refutation.” Consequently, if the SEC decides to address digital assets in a final rule, and it relies on new data to support its analysis of the economic effects, then the SEC must re-open the comment period.

The SEC’s analysis fails to account for other critical issues concerning the Proposal. The economic analysis associated with broker-Dealer and ATS registration is based on traditional broker-dealer business without addressing the cost of registering a digital asset only broker-dealer/ATS. Indeed, notwithstanding that the SEC established a framework by which digital asset-only broker-dealers can register with the SEC, we are not aware of any broker-dealers that have successfully registered under that framework. Perhaps because of this, there has been no analysis to date on the costs of interfacing with FINRA and the SEC on these types of registrations. In addition, the Proposal does not address: (1) the impact on the digital asset industry and discuss affected parties; (2) the high number of digital asset platforms that could potentially be captured; (3) DeFi, Spot markets, and digital asset market making; or (4) the impact on developers of the code, deployers, or interface providers affected.

In addition to a flawed economic analysis, the Proposal lacks a substantive foundation by which it would reasonably capture digital assets and digital asset platforms, and it diverges without explanation from a more measured approach advocated by multiple members of the SEC.

As an initial matter, digital assets are not “securities,” and the law on this issue is still in significant flux. Further, a digital asset marketplace is not an exchange under the plain terms of

---

39 Id. § 78w(a)(2).
40 Bus. Roundtable v. SEC, 647 F.3d 1144, 1148 (D.C. Cir. 2011) (internal quotation marks omitted).
41 Chamber of Commerce v. SEC, 443 F.3d 890, 900 (D.C. Cir. 2006) (internal quotation marks omitted).
the Exchange Act. It is neither a “marketplace” nor a “facility.” These terms contemplate “bringing together” purchases and sales “for the purpose of effecting or reporting” transactions, and thus contemplate the use of firm orders. Extending the definition of “exchange” to cover “communication protocol systems” that facilitate the transmission of non-firm trading interest goes beyond any recognizable definition of an exchange and far exceeds the SEC’s authority—as reflected, among other things, in the Act’s treatment of a “system of communication” as merely an appurtenance of an exchange, not an exchange itself. The overbreadth of the SEC’s definition is also demonstrated by the numerous exceptions that the SEC must give its broad definition.

Moreover, there are serious limitations in how the technology that underpins a digital asset platform can be transferred and effectively used in a formal ATS environment, meaning that the SEC, if it applied the proposed rule to digital assets, would effectively seek to regulate something before it exists and is understood by regulators. This is not efficient and in stark contrast to, for example, RFQ Platforms which have been in existence for some time and which the SEC had decades to study and understand when deciding to bring within the regulatory framework applicable to exchanges. Indeed, this conundrum of sorts appears to capture the essence of Commissioner Hester Peirce’s “catch-22” that she outlined in February 2020 where:

Would-be networks cannot get their tokens out into people’s hands because their tokens are potentially subject to the securities laws. However, would-be networks cannot mature into a functional or decentralized network that is not dependent upon a single person or group to carry out the essential managerial or entrepreneurial efforts unless the tokens are distributed to and freely transferable among potential users, developers, and participants of the network. The securities laws cannot be ignored, but neither can we as securities regulators ignore the conundrum our laws create.

Rather than proceed as is, the SEC should consider postponing the implementation of rules applicable to digital asset platforms until such time as it can consider defining what the current ATS framework would look like for digital assets. Chair Gensler recently shared such observations in his April 4, 2022 speech, where he noted:

Some have asked if the current exemptions for so-called alternative trading systems (ATSs) could be generally available to crypto platforms. ATSs for the equity and fixed income markets, though, are generally used by institutional investors. This is quite different than crypto-asset platforms, which have millions and sometimes tens of millions of retail customers directly buying and selling on the platform without going through a broker. Thus, I’ve asked staff to consider whether and how the protections that are

---

45 See id. §§ 78c(a)(1), (2).
46 See id. § 78c(a)(2).
47 See Chamber of Commerce v. U.S. Dep’t of Labor, 885 F.3d 360, 382 (5th Cir. 2018).
afforded to other investors on exchanges with which retail investors interact should apply
to crypto platforms.49

To this end, we recommend that the SEC give adequate consideration to such things as: (i) the
practical difficulties in actually registering an ATS with the SEC and FINRA, which leads to
increasing use of private placements of digital assets on the blockchain; (ii) the need for digital
asset regulatory expertise and reconciliation of dated rules, including with FINRA, which we
anecdotally understand views digital assets through transfer agent lenses when it comes to
record-keeping and control; (iii) the limitations of the current ATS framework for digital assets,
and in particular, that the framework is biased toward traditional securities offerings and does
make room for clearance and settlement on the blockchain; and (iv) the various technologies at
play as discussed in the section above describing digital platforms.

Proposal will Hinder Innovation, Competition, And Capital Formation

As the SEC is well aware, in addition to protecting investors, part of the SEC's mission to ensure
that its actions are in the public interest and promote capital formation. On this latter point, one
of the reasons that the United States has some of the deepest, most liquid, and most innovative
financial markets in the world is because it embraces technology and forward-thinking.
Unfortunately, we believe that the Proposal as drafted would leave the U.S. behind during the
current global revolution in financial services. More specifically, the Proposal's discussion
regarding what it means to "makes available" and the intention to capture a party that performs
tangential functions to the operation of a purported exchange will create a chilling effect that
would result in developers involved in a digital platform's underlying technology avoiding any
U.S. touchpoint. This will result in these technologies and innovations finding their homes in
jurisdictions that promote and not hinder development and forward-thinking, such as the UK,
which is making Cabinet-level speeches indicating a desire to "lead the way" in digital assets and
the UK "is open for crypto business." 50 To this end, we encourage the SEC to work within the
framework contemplated in the Executive Order to further promote the use and development of
digital assets within the United States.

*   *   *


50 Keynote Speech by John Glen, Economic Secretary to the Treasury, at the Innovate Finance Global Summit
(April 4, 2022)
innovate-finance-global-summit
ADAM appreciates the SEC's consideration of the comments above. ADAM and its members stand ready to answer any questions you may have, and we look forward to continued collaboration with SEC.

Respectfully,

Michelle Bond
Chief Executive Officer
Association for Digital Asset Markets (ADAM)