



DIVISION OF  
TRADING AND MARKETS

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

September 25, 2020

Ms. Kris Dailey  
Vice President, Risk Oversight & Operational Regulation  
Financial Industry Regulatory Authority (“FINRA”)  
One World Financial Center  
200 Liberty Street  
New York, NY 10281

Re: ATS Role in the Settlement of Digital Asset Security Trades

Dear Ms. Dailey:

Your staff has asked about the application of the Joint Staff Statement<sup>1</sup> issued on July 8, 2019 by the staffs of the Division of Trading and Markets, U.S. Securities and Exchange Commission and the Office of General Counsel, Financial Industry Regulatory Authority (“FINRA”) to registered broker-dealers (“broker-dealer operator”) operating alternative trading systems (“ATSS”)<sup>2</sup> that trade digital asset securities.<sup>3</sup>

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<sup>1</sup> Division of Trading and Markets, U.S. Securities and Exchange Commission (“Commission”), and Office of General Counsel, FINRA, Joint Staff Statement on Broker-Dealer Custody of Digital Asset Securities, available at <https://www.sec.gov/news/public-statement/joint-staff-statement-broker-dealer-custody-digital-asset-securities>. The Joint Staff Statement represents staff views of the Division of Trading and Markets and FINRA. The Joint Staff Statement is not a rule, regulation, guidance, or statement of the Commission or FINRA, and the Commission and FINRA’s Board neither approved nor disapproved its content. The Joint Staff Statement does not alter or amend applicable law and has no legal force or effect.

<sup>2</sup> An ATS is a trading system that meets the definition of an “exchange” under federal securities laws but is not required to register as a national securities exchange if the ATS complies with the conditions to the exemption provided under Rule 3a1-1(a)(2) of the Securities Exchange Act of 1934 (“Exchange Act”). *See* 17 CFR 242.300(a) (defining an alternative trading system) and CFR 242.3a1-1(a)(2) (the exemption from the definition of an exchange for an ATS). An ATS that is required to comply with Regulation ATS must register with the Commission as a broker-dealer. *See* 17 CFR 242.301(b)(1).

<sup>3</sup> For purposes of this no-action letter, the term “digital asset” refers to an asset that is issued and/or transferred using distributed ledger or blockchain technology, including, but not limited to, so-called “virtual currencies,” “coins,” and “tokens.” A digital asset may or may not meet the definition of a “security” under the federal securities laws. For the purposes of this no-action letter, a digital asset that is not a security is referred to as a “non-security digital asset” and a digital asset that is a security is referred to as a “digital asset security.”

## I. Background

The Joint Staff Statement discussed staff views on, among other things, investor protection concerns related to a broker-dealer's ability to comply with aspects of Rule 15c3-3<sup>4</sup> under the Exchange Act with respect to digital asset securities. In particular, the Joint Staff Statement discussed paragraph (b) of Rule 15c3-3, under which the broker-dealer must obtain and maintain physical possession or control of all fully paid or excess margin securities carried by a broker-dealer for the account of customers,<sup>5</sup> as well as the potential difficulties in complying with this provision due to the nature of digital asset securities.

The Joint Staff Statement described several non-custodial activities involving digital asset securities, including where an ATS matches the orders of buyers and sellers of digital asset securities and the trades are either settled directly between the buyer and seller, or the buyer and seller give instructions to their respective custodians to settle the transactions. In either case, a broker-dealer operator does not guarantee or otherwise have responsibility for settling the trades and does not at any time exercise any level of control over the digital asset securities being sold or the cash being used to make the purchase (e.g., the ATS does not place a temporary hold on the seller's wallet or on the buyer's cash to ensure the transaction is completed). In effect, this non-custodial ATS model involves a four-step process:

- Step 1 - the buyer and seller send their respective orders to the ATS;
- Step 2 - the ATS matches the orders;
- Step 3 - the ATS notifies the buyer and seller of the matched trade; and
- Step 4 - the buyer and seller settle the transaction bilaterally, either directly with each other or by instructing their respective custodians to settle the transaction on their behalf.

Since the issuance of the Joint Staff Statement, several broker-dealers seeking to operate an ATS that trades digital asset securities have asserted that the four-step process described above increases operational and settlement risks. Instead, they prefer the following process (the "Three-Step Process"):

- Step 1 - the buyer and seller send their respective orders to the ATS, notify their respective custodians of their respective orders submitted to the ATS, and instruct their respective custodians to settle transactions in accordance with the terms of their orders when the ATS notifies the custodians of a match on the ATS;
- Step 2 - the ATS matches the orders; and

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<sup>4</sup> See 17 C.F.R. 240.15c3-3.

<sup>5</sup> See 17 CFR 240.15c3-3(b).

Step 3 - the ATS notifies the buyer and seller and their respective custodians of the matched trade and the custodians carry out the conditional instructions.

The custodians would then settle the trade on behalf of the buyer and seller based on the instructions received in Step 1. As with the four-step process, the broker-dealer operator does not guarantee or otherwise have responsibility for settling the trades and does not at any time exercise any level of control over the digital asset securities being sold or the cash being used to make the purchase (e.g., the ATS does not place a temporary hold on the seller's wallet or on the buyer's cash to ensure the transaction is completed) other than by notifying the custodians for the buyer and seller, and the buyer and seller, of the match. Broker-dealers seeking to operate an ATS assert that the primary benefit of the three-step settlement process is that it would reduce operational and settlement risk.

Broker-dealers seeking to operate an ATS under the Three-Step Process have made additional statements regarding the terms of their respective operations to address concerns that they may be viewed as holding or controlling customer property. Broker-dealers seeking to operate an ATS trading digital asset securities have stated that: (1) the broker-dealer would maintain a minimum of \$250,000 in net capital; (2) the agreements between the broker-dealer and its customers clearly state that the broker-dealer does not guarantee or otherwise have responsibility for settling the trades; (3) the broker-dealer would establish and maintain reasonably designed procedures to assess whether a digital asset security was offered and sold initially pursuant to an effective registration statement or an available exemption from registration, and whether any secondary transactions of the digital asset security on or through the ATS are made pursuant to an effective registration statement or an available exemption from registration; and (4) the transactions in digital asset securities otherwise comply with the federal securities laws.

## II. Response

Based on the facts and analysis set forth above, Division staff will not recommend enforcement action to the Commission under Section 15(c)(3) of the Exchange Act and Rule 15c3-3 thereunder if, under the circumstances listed below, a broker-dealer operating an ATS that trades digital asset securities uses the Three-Step Process described above:

- (1) The broker-dealer operator maintains a minimum of \$250,000 in net capital;
- (2) The agreements between the broker-dealer operator and its customers clearly state that the broker-dealer operator does not guarantee or otherwise have responsibility for settling the trades;
- (3) The broker-dealer operator has established and maintains reasonably designed procedures to assess whether a digital asset security was offered and sold initially pursuant to an effective registration statement or an available exemption from registration, and whether any secondary transactions of the digital asset security on or through the ATS are made pursuant to an effective registration statement or an available exemption from registration; and

- (4) The transactions in digital asset securities otherwise comply with the federal securities laws.

This position solely addresses an ATS trading digital asset securities under the circumstances set forth in this letter and does not otherwise address broker-dealer custody or control of digital asset securities under Rule 15c3-3. The position of the staff is based strictly on the facts and circumstances discussed in your request, and any different facts or circumstances might require a different response. Furthermore, this response expresses the staff's position regarding enforcement action only and does not purport to express any legal conclusions on the questions presented. The staff expresses no view with respect to any other questions that the proposed activities may raise, including the applicability of any other federal or state laws, or self-regulatory organization rules. This position is subject to modification or revocation by the staff at any time.

If you have any questions, please call me at (202) 551-6573.

Sincerely,

Elizabeth Baird  
Deputy Director