Chamber of Digital Commerce
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September 27, 2021

Via electronic submission (submissions@banking.senate.gov)

Senator Pat Toomey
Ranking Member
U.S. Senate Committee on Banking, Housing, and Urban Affairs
534 Dirksen Senate Office Building
Washington, D.C. 20510

Re: Request for Information on Clarifying Laws Around Cryptocurrency and Blockchain Technologies (August 26, 2021)

Dear Senator Toomey:

The Chamber of Digital Commerce (the "Chamber") appreciates the opportunity to comment on the U.S. Senate Banking Committee's request for information regarding ideas and legislative proposals designed to ensure that federal law supports the development of emerging cryptocurrency and open blockchain network technologies, while continuing to protect "crypto investors" (the "Request for Information").[1]

The Chamber is the world's leading trade association representing the digital asset and blockchain industry. Our mission is to promote the acceptance and use of digital assets and blockchain technology, and we are supported by a diverse membership that represents the industry globally. Through education, advocacy, and close coordination with policymakers, regulatory agencies, and industry across various jurisdictions, our goal is to develop a pro-growth legal environment that fosters innovation, job creation, and investment. We represent the world's leading innovators, operators, and investors in the blockchain ecosystem, including leading edge startups, software companies, global IT consultancies, financial institutions, and investment firms.

[1] Toomey Requests Feedback on Clarifying Laws Around Cryptocurrency and Blockchain Technologies (August 26, 2021).

Founded in 2014 with a guiding principle of industry compliance, the Chamber continues to forge compliance-focused initiatives, in addition to advocating for clear and concise regulatory action and rulemaking. The Blockchain Alliance, one of its first initiatives, features technical assistance and information-sharing resources in crime prevention; although founded just a few years ago in 2015, it now serves over 100 international government and commercial entities, including the Securities and Exchange Commission.[2] The Chamber also conducts resource-intensive efforts to promote industry compliance under federal securities law, in addition to providing educational and technical assistance to policy makers.[3]

A. Better Policy Approach Towards Blockchain Technology and Digital Assets

In your Request for Information, you state that:

> "Not only might cryptocurrency and blockchain technologies be as revolutionary as the internet, they also have the potential to build wealth and financial independence for individuals who are empowered to engage in financial transactions directly with each other, free from oft-costly middlemen. That's why it's important Congress gets this right and ensures the United States remains at the forefront of cryptocurrency and fintech innovation. I am hopeful the broad array of legislative proposals I receive will help in crafting thoughtful legislation."

We could not agree more and believe that a thoughtful and innovative regulatory approach to the emerging cryptocurrency and open blockchain technology industry is critical to the overall economic primacy of the United States.

We believe that emerging cryptocurrency, digital asset and open blockchain network technologies offer immense possibilities for business, government, and consumers. These include the opportunity for extraordinary economic growth and a safer and more secure Internet. Its ability to improve processes, increase cost-efficiency, and promote transparency in numerous industries is reforming the ways in which companies conduct business. For example, emerging cryptocurrency and open blockchain network technologies can enable the provision of financial services and access to the unbanked and underbanked through faster and cheaper remittances and digital identity solutions. The following are examples of these types of innovations:

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[2] The Blockchain Alliance's mission is to combat criminal use of blockchain technology. *See* BLOCKCHAIN ALLIANCE

[3] One example of such is the Token Alliance, which launched amid a token distribution spike in 2017, and issued a series of informational tools for both industry members and policy makers to ensure informed decision-making in tokenized network and application activity. The Token Alliance is an initiative of the Chamber co-chaired by former SEC and CFTC regulators dedicated to fostering best practices for the responsible growth of tokenized networks and applications. *See* *Token Alliance*, CHAMBER OF DIGITAL COMMERCE

- Payment providers operating in South America and Africa use bitcoin and other open blockchain cryptocurrencies to charge commissions as low as 1% versus the commission rates of 5% or higher typically charged by incumbents.[4]
- Historically disadvantaged communities are increasingly selling non-fungible tokes ("NFTs") on open blockchains, which has expanded economic opportunity. Just 1% of art auction spending over the last ten years related to works by African Americans, of which half is attributable to a single individual, but between January 2020 and March 2021 alone, 58 black artists sold a combined 513 pieces of NFT artwork for a combined value of over $700,000.[5]
- Major financial companies have used Ethereum, a popular open blockchain, as the foundation from which to build private blockchain solutions used for trial "digital dollars" currently being piloted. The prevalence of the U.S. dollar on open blockchain networks can advance U.S. economic and national security interests.[6]

The potential of these technologies, however, is being felt in many industries beyond financial services, such as healthcare, supply chain management, energy, transportation, insurance, voting, and many others. For example, research focused on medical and health care applications have found that blockchain not only catalyzes the interactions among players but also facilitates the formation of the ecosystem life cycle, and that a collaborative network linked by blockchain may play a critical role in value creation, transfer, and sharing among the health care community.[7]

Several prominent companies are testing blockchain solutions and investigating blockchain uses for their supply chains:

- Blockchain company Everledger partnered with IBM to create a blockchain solution to ensure diamonds are ethically sourced.[8] Everledger has also branched out into other industries by developing blockchain solutions for the fashion industry, electronics producers, and electric vehicle manufacturers.[9]
- Walmart, Carrefour, Nestle and Dole have partnered with IBM on a trial blockchain system that tracks food products through their respective supply chains.[10]

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[4] https://restofworld.org/2021/crypto-remittances/

[5] https://news.artnet.com/the-long-road-for-african-american-artists/african-american-art-market-data-1350998; https://www.theguardian.com/artanddesign/2019/sep/19/female-art-women-underrepresented-museums-auctions-study https://www.coindesk.com/these-black-artists-say-nfts-help-them-monetize-their-work

[6] https://media.consensys.net/j-p-morgan-is-using-ethereum-to-launch-a-digital-u-s-dollar-heres-what-it-means-for-blockchain-64f0fe3e55bc

[7] Blockchain in Health Care Innovation: Literature Review and Case Study from a Business Ecosystem Perspective

[8] Everledger's Pioneering Blockchain Work for Diamonds

[9] Everledger Industry Solutions

[10] IBM Food Trust: A new era in the world's food supply

- Amazon boasts managed blockchain solutions for supply chain and other business applications that integrate Hyperledger Fabric, an umbrella of blockchain management tools developed by the Linux Foundation.

By 2023, it is projected that 30% of manufacturing companies with more than $5 billion in revenue will be engaging with blockchain technologies.

Blockchain technology is a distributed ledger or record of transactions that enables the execution of smart contracts. It serves as the foundation upon which many applications can be built, much like how the Internet underpins multiple use-cases such as e-mail, e-commerce, and business processes. Its characteristics enable faster, more efficient transactions, eliminating the need for multiple intermediaries and the possibility for inadvertent or manual errors across numerous locations or geographies. Blockchain is a cryptographically secure platform ideal for storing assets and ownership information and will serve as the foundation or "rails" for other technologies, like the Internet of Things ("IoT") and artificial intelligence. It is clear that blockchain is a revolutionary breakthrough technology, allowing us to create infrastructure towards an Internet of Value (or "for intelligent value transfer networks").

Some of the most promising social benefits of emerging cryptocurrency and open blockchain network technologies have yet to come and there is a dynamic market ecosystem developing that policymakers should be mindful not to stamp out. Recently, there has been considerable growth in decentralized finance ("DeFi") markets. DeFi is a broad term that refers to decentralized finance alternatives to traditional services that are generally built on open source blockchains. Today, banks act as gatekeepers to accessing many financial services and profit from overdraft and ATM withdrawal fees[11] that are largely borne by minorities.[12]

DeFi promises to address this model by removing traditional gatekeepers and lowering costs to anyone with access to a cell phone. A key component of helping these benefits come to fruition depends upon the existence of stablecoins, which carry great promise to help revolutionize the payments sphere given the combination of their stable value and digital, nearly instantaneous transferability.

While technological progress is clear, it does not automatically follow that the United States will maintain its pre-eminence in the blockchain sector. The United States needs a dynamic, open regulatory environment for emerging cryptocurrency and open blockchain network technologies in order to become a leader in blockchain technology more broadly. As you recently noted, China's ongoing crackdown on cryptocurrencies is a huge opportunity for the United States.[13]

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[11] In 2020 alone, banks amassed over $30 billion in overdraft fees.
[12] A recent study showed that in the U.S. white people paid an average of $5.29 per month in bank fees, while black people paid $12.30 per month and Hispanic people paid $15.85 per month in average fees.
[13] Senator Pat Toomey, Twitter (September 2021), https://twitter.com/SenToomey/status/1441398415712129024

We note that other major industrialized nations are already making significant advances in promoting and adopting this technology, making a hard run to be the leaders, and obtain the economic value, of this industry. For example:

- Paving the way for the Swiss stock exchange, SIX Swiss Exchange ("SIX"), to go live with a marketplace for digital assets,[14] in September 2021, the Swiss Financial Market Supervisory Authority, FINMA, granted regulatory approval for SIX's new SDX bourse, which will operate on distributed ledger technology, as well as approval to operate a central securities depository for digital assets.

- After several years of planning, in October 2021, the French city of Verneuil-sur-Seine announced that its residents would be able to vote using blockchain technology in a consultation over a 50-year-old road project through their Avosvotes application, an app based on the Tezos blockchain. When voting on the proposal, individuals' identities were verified manually, and proof of any particular vote was made available in the form of a certificate stored on the blockchain.[15]

Blockchain technology has enormous potential for innovation and economic growth, but this potential will not be realized in the United States without widespread support of policymakers for emerging cryptocurrency markets and open blockchain networks – the ecosystem where the early-stage innovation that inspires corporate blockchain solutions is taking place.

B. Guiding Principles for Government

As the Chamber has noted repeatedly over the past few years, there is a critical need for a comprehensive, coordinated, pro-growth approach to developing blockchain technology in the United States.[16] We believe that emerging cryptocurrency and open blockchain network technologies are particularly important, and encourage Congress to embrace the following principles:

Encourage Innovation by the Private Sector

The private sector was a leader in developing the Internet in the 1990s and 2000s and should be a leader in developing the next generation Internet, which will be built on emerging cryptocurrency, digital asset and open blockchain network technologies. The United States cherishes entrepreneurship and innovation, and we should encourage and support these qualities as we head into the next generation of technological development.

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14 Swiss stock exchange gets regulatory approval for digital token offering (September 2021)
15 French municipality accepting blockchain voting for road project (October 2020)
16 Chamber of Digital Commerce National Action Plan for Blockchain (February 2019)

Emerging cryptocurrency, digital asset and open blockchain network technologies require the open regulatory framework that enabled the U.S. to become a leader in the Internet economy.[17] Regulation that is too restrictive or that does not consider the potential for future innovations will stymie the growth of this industry and scuttle government efforts to remain a leader in, and keep pace with, technological development.

Bringing Enforcement Actions Against Clear Violations of Law while Avoiding Regulation by Enforcement

While it is important for regulators to adopt an adaptive regulatory approach that does not impede innovation, it is equally important for regulators to pursue bad actors. Regulators should avoid, however, letting enforcement actions become a go-to source of guidance, and instead work with industry collaboratively so that there are clear rules of the road.[18]

Industry must have clearly articulated and binding rules promulgated by regulators regarding the application of law to blockchain-based applications and tokens before bringing enforcement actions. Public statements, whether made public through the press or in formal speeches, are helpful but are not official statements of application by an agency. If an agency intends to enforce its laws in new and innovative ways, it must first notify industry stakeholders of its intent to do so and make clear through formal adopted guidance and rules the way in which existing law applies.

Any Regulation Should be Based on the Function Performed, Not the Technology

Virtual currency and digital asset-related statutes and regulations should emphasize function. New rules and statutes should not be based on the type of technology itself but, rather, the use or activity involving the technology.

Prevent a Regulatory Patchwork while Embracing Federalism

Projects and companies involving emerging cryptocurrency and open blockchain network technologies are oftentimes multi-jurisdictional. The federal government should allow states to be laboratories of innovation, and at the same time, work to streamline a regulatory patchwork at the federal level that emerges as agencies try to claim turf over this emerging ecosystem. Congressional efforts should allow for policy experimentation at the state-level while also allowing creating viable paths for emerging cryptocurrency and open blockchain network projects to operate nationally through streamlined federal regulation.

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[17] White House, "The Framework for Global Electronic Commerce" (July 1997)
[18] *U.S. Securities and Exchange Commission Public Statement*: In the Matter of CoinSchedule (July 2021)

Any Necessary Regulation or Law Should be Clear, Predictable, and Developed with Future Innovations in Mind

Technology changes rapidly. As such, laws and regulations should be drafted with the intent to endure future iterations and not focus solely on one technology or application. For example, the Electronic Signatures in Global and National Commerce Act ("ESIGN" Act) and state Uniform Electronic Transactions Acts ("UETA") were written to validate electronic signatures and records and to be agnostic to the technology used. The same principles should be considered when developing future rules for emerging cryptocurrency, digital asset and open blockchain network technologies.

Study and Understand the Unique Attributes of Blockchain Technology and Digital Tokens

Emerging cryptocurrency, digital asset and open blockchain network technologies can be complex. Government stakeholders must take the time to learn how these technologies work, their strengths and weaknesses, and how those attributes can create new mechanisms for enabling the provision of products and services by governments and businesses, as well as enabling better access to consumers.

C: PROPOSALS FOR CONSIDERATION

As with any new innovation, emerging cryptocurrency, digital asset and open blockchain network technologies may pose opportunities and risks that are not well understood. However, a rational approach to policymaking and regulation can help ensure that the benefits of a new technology come to fruition while maintaining existing protections for consumers.

Regulating this innovative space will require addressing many of the same problems found in traditional finance, including consumer protection, fraud, money laundering, and other financial crime, and overall financial stability. Policymakers and regulators can enforce existing rules to protect against bad actors, while providing adequate regulatory guidance, relief, or changes that enable helpful innovation to flourish. To achieve these ends, we propose the following policy recommendations:

1) <u>Ensure regulatory coordination</u>

Disparate guidance from the Securities and Exchange Commission ("SEC"), the Commodities Futures Trading Commission ("CFTC"), and other federal agencies is making it increasingly challenging and costly for emerging cryptocurrency, digital asset and open blockchain network projects to stay in compliance with relevant regulations as they grow. Agencies should focus on categories of activities that fit within their area of jurisdiction, rather than expecting one agency to assume the role of regulating all types of open blockchain network and emerging cryptocurrency projects.

To that end, we believe that it is critically important that the Senate pass the Eliminate Barriers to Innovation Act of 2021 ("H.R. 1602"),[19] which has passed the House of Representatives and now awaits the Senate. The bill was introduced by House Financial Services Committee Ranking Member Patrick McHenry (R-NC) with Chairman Stephen Lynch (D-MA) of the Financial Technology Task Force and would form a joint CFTC And SEC working group on digital assets to help provide clarity in what is a security and what is a commodity among digital assets. The working group would be composed of public and private representatives to study and issue a report to Congress.

2) Develop a clear application of the definition of "security" to digital assets

To date, the SEC has failed to provide adequate guidance on the application of the "Howey Test" to digital assets. While it has provided some guidance,[20] when presented with other opportunities to further clarify its thinking, the SEC has refused to do so or has done so in a piecemeal fashion.[21]

Worryingly, contrary to the guiding principles set forth above, the SEC appears to be pursuing a pathway of providing clarity through enforcement cases and conclusory public statements. As was highlighted very recently, the SEC has threatened litigation against a firm seeking guidance on a new financial product offering and SEC Chair Gensler has commented that stablecoins "may well be securities" without providing justification.[22]

With respect to stablecoins, as you noted in a September 14th hearing with SEC Chair Gensler,[23] stablecoins do not easily fit with the Supreme Court's definition of a security.[24] We agree. Many stablecoins, particularly those whose primary purpose is a payment method and that are backed by cash and cash equivalents, should not be classified as a security due to the lack of an expectation of profit. Stablecoins should also not be regulated as money market funds given that they are not interest-bearing or used as a passive investment.

There are several proposals that would help address this definitional uncertainty. For example, the implementation of a safe harbor along the lines of SEC Commissioner Peirce's "Token Safe Harbor Proposal 2.0" (the "Token Safe Harbor") by regulation or statute would be a constructive step that would facilitate innovation while maintaining standards and disclosure requirements for new products. The "Token Safe Harbor Proposal" would provide a three-year period for blockchain developers to launch and

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19 H.R.1602: Eliminate Barriers to Innovation Act of 2021
20 *U.S. Securities and Exchange Commission:* Framework for 'Investment Contract' Analysis of Digital Assets, April 2019
21 "We nevertheless are disappointed 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." https://www.sec.gov/news/public-statement/peirce-roisman-coinschedule
22 *Coinbase Blog: The SEC has told us it wants to sue us over Lend. We don't know why. (September 2021)*
23 *Oversight of the U.S. Securities and Exchange Commission: Hearing before the Senate Banking Committee*, 117th Cong. (2021)
24 *SEC v. Howey Co.,* 328 U.S. 293, 299 (1946)

mature their projects before being subject to full SEC regulation. This proposal would allow developers[25] to focus on growing their nascent projects, while still requiring regular disclosures to the SEC and a formal exit memo at the end of the three-year period.[26] The Chamber is currently working with a range of interested industry participants, including legislators and regulators, on a slightly varied version of the Token Safe Harbor that will provide a clear framework for determining whether a token is a security once the three-year period has expired.

An alternative solution to SEC action would be for Congress to pass the bipartisan Securities Clarity Act[27] that we believe provides the best path forward to address the question of which digital assets are securities. This legislation clarifies that an investment contract, such as a digital asset, is distinct from the securities offering it may have been part of.[28] We believe it strikes the right balance of providing helpful clarity while still being technology neutral and limited in scope.

3) Clarify how custody rules apply to digital assets

The SEC, the Office of Comptroller of the Currency ("OCC"), and state regulators each have differing custody requirements for digital assets. At the federal level, the SEC and OCC have taken helpful steps in the form of guidance from the OCC and limited no-action relief from the SEC.[29] At the state level, Wyoming passed a bill allowing for banks to provide custodial services for digital assets.[30] While such steps have been welcome, we hope that they portend more significant steps in the future.

Providing clarity on how the custody rules apply to digital assets, and allowing the traditional, regulated financial system to interact with digital assets, will provide a safer arena for consumers to navigate the digital asset ecosystem.

4) Clarify tax guidance and accounting standards

Over the past five years, the Internal Revenue Service ("IRS") has significantly increased enforcement actions against taxpayers who transact in digital assets. But, while ratcheting up its enforcement, the IRS has not provided meaningful guidance on how to comply with tax rules since 2014.

[25] *U.S. Securities and Exchange Commission Public Statement:* Token Safe Harbor Proposal 2.0 (April 2021) Defined as: "Not economically or operationally controlled and is not reasonably likely to be economically or operationally controlled or unilaterally changed by any single person, entity, or group of persons or entities under common control, except that networks for which the Initial Development Team owns more than 20% of Tokens or owns more than 20% of the means of determining network consensus cannot satisfy this condition."
[26] *U.S. Securities and Exchange Commission Public Statement:* Token Safe Harbor Proposal 2.0 (April 2021)
[27] *H.R.4451 - Securities Clarity Act117th Congress (2021-2022)*
[28] *Press Release: Emmer Introduces Legislation to Provide Clarity for Digital Assets Under Securities Law* (September 2020)
[29] *Office of the Comptroller of the Currency News Release:* Federally Chartered Banks and Thrifts May Provide Custody Services for Crypto Assets (July 2020)
[30] *Sixty-Fifth Legislature of the State of Wyoming 2019 General Session:* SF0125 - Digital assets-existing law

This disparity creates risk for taxpayers seeking to comply with the laws, wastes IRS audit resources, dampens commercial activity and economic recovery, and stifles U.S. innovation.

In May, the Chamber published a tax policy framework that could be utilized as a basis for legislation that identifies key areas where the IRS must issue more guidance for taxpayers on lending, information reporting, foreign bank account reporting, characterization of digital assets, and proof of stake protocols.[31] It also sent a letter to the IRS on the application of the Foreign Account Tax Compliance Act ("FATCA") to digital assets.[32]

In addition. the Chamber recently responded to the Financial Accounting Standards Board ("FASB")'s Invitation to Comment on FASB's Future Agenda consultation. [33] As we state in that response, we believe that cryptocurrencies represent the next evolution in increasing efficiency of financial and non-financial transactions. Due to pervasive impact, exponential increase in market capitalization and adoption of digital assets, the accounting for cryptocurrencies and digital assets is the most critical new financial reporting issue facing users and preparers of Generally Accepted Accounting Principles ("GAAP") financial statements, and that setting clear accounting standards for companies that hold digital assets on balance sheets must be top priority for FASB. We also urged the board of FASB to add standard setting for digital assets and cryptocurrency on their near-term agenda.

In our response, signed by more than fifty of the Chamber's members, we demonstrate the rapid growth of digital asset ownership by both public and private companies across virtually all industry lines. We believe that clarity in financial reporting for this highly pervasive financial asset is imperative in maintaining clear, relevant, and transparent financial reporting for the investors and other stakeholders in U.S. companies reporting ownership of digital assets.

5) Ensuring regulation does not stifle innovation in stablecoins

Stablecoins carry great promise to revolutionize the payments sphere given the combination of their stable value and digital, instantaneous transferability. U.S. financial regulators have announced their intent to develop rules for stablecoins,[34] and we would caution against hastily crafted rules that have the effect of stifling innovation in this evolving space. For example, some states allow virtual currency businesses, including stablecoin issuers, to be classified as trust companies.[35] These regulations come with

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[31] Chamber of Digital Commerce Principles and Framework for Appropriate Digital Asset Tax Policy in the United States (May 2021)
[32] Chamber of Digital Commerce Letter to IRS on Application of FATCA to Digital Assets (May 2021)
[33] Chamber of Digital Commerce Response to Financial Accounting Standards Board invitation to comment on FASB future agenda (September 2021)
[34] Press Release, U.S. Department of the Treasury, Readout of the Meeting of the President's Working Group on Financial Markets to Discuss Stablecoins (July 19, 2021) (declaring the "need to act quickly to ensure there is an appropriate U.S. regulatory framework in place").
[35] *e.g., Organization of a Trust Company for the Limited Purpose of Exercising Fiduciary Powers, New York Department of Financial Services* (last visited September 24, 2021)

requirements to manage reserves conservatively, addressing a primary concern of regulators.[36] Any proposed federal legislation related to stablecoins should consider existing state laws and regulation that already addresses stablecoin concerns.

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The Chamber greatly appreciates the opportunity to comment on the Request for Information and appreciates the Committee's consideration of the above comments and concerns. Please feel free to contact us with any questions regarding our comments.

Very Truly Yours,

Perianne Boring
Founder and President

Teana Baker-Taylor
Chief Policy Officer

[36] *e.g., Wyoming Division of Banking, supra* note 2 (requiring SPDIs to maintain "unencumbered level 1 high-quality liquid assets valued at 100% or more of their depository liabilities").