CHAMBER OF DIGITAL COMMERCE

February 25, 2022

The Honorable Maxine Waters, Chairwoman
The Honorable Patrick McHenry, Ranking Member
U.S. House Committee on Financial Services
2129 Rayburn House Office Building
Washington, DC 20515

Re: Policy Recommendations for Digital assets, Blockchain Technology, and Decentralized Finance

Dear Chairwoman Waters, Ranking Member McHenry, and House Financial Services Committee Members,

The Chamber of Digital Commerce (the "Chamber") and its members appreciate your willingness to engage with the industry on the future of digital assets, including cryptocurrency, and we are encouraged by the Committee's keen interest in learning more about the potential benefits blockchain technology is bringing to society as well as understanding the potential risks and balanced approaches to mitigate them.

Established in 2014 as the world's first and largest blockchain trade association, the Chamber's mission is to promote the acceptance and use of digital assets and blockchain technology. We are supported by a diverse membership that represents the blockchain industry globally, including more than 200 of the world's leading startups, software companies, financial institutions, and investment firms, as well as other market participants, including digital asset mining firms. Membership is open to all companies committed to supporting and growing this thriving marketplace.

We appreciate this opportunity to share our perspective on some of the critically important issues being considered by the Committee, including the characteristics of assets traded on digital asset trading platforms, decentralized finance ("DeFi"), consumer protection, financial stability, environmental implications, and ransomware, and to highlight our view on how digital assets, blockchain technology, and DeFi offer consumers important alternatives. Specifically, we discuss:

- the value proposition of digital assets and the benefits and risks of DeFi;
- policy debates around systemic risk, consumer protection, ransomware, and;
- the environmental impact of digital asset mining.

Finally, we include several policy recommendations that we believe acknowledge the global benefits of digital assets while maintaining critical market and consumer protections.

Executive Summary

We would welcome the opportunity to establish an ongoing dialogue with you, and all Members of the Committee, to better understand your concerns, as well as share our resources with you to ensure that you have a rich and nuanced understanding of the crucial benefits to society that digital assets can enable.

Through our broad and extensive membership, we work closely with industry experts who are tackling these challenges today, and we regularly facilitate topic specific briefings at the Committee level to demonstrate the future opportunities we could realistically expect to achieve if innovation is not stifled.

- The lack of regulatory clarity around the regulatory treatment of tokens and the fluidity around each agencies' regulatory purview in the United States has the potential to limit the ability to adequately oversee the inherent risk with the digital asset markets, ensure market integrity and mitigate consumer risk.

- We believe that digital assets and stablecoins have the potential to help fight global poverty by making cross-border payments faster and more affordable.

- Decentralized Financial services (or, DeFi) have the potential to offer basic financial services at a lower cost, without bias, and with better accessibility for unbanked and underbanked individuals.

- Digital token offerings enable greater access to capital raising for early-stage technology projects, which also has the potential to provide support for women and minority founders who have historically been overlooked and underserved by traditional venture capitalists.

- Certain digital tokens, like Non-Fungible Tokens, are today expanding economic opportunity in entirely new ways, which will play a significant role in the evolution of the future of marketplaces, the Internet and the emerging metaverse.

- Blockchain technology has the potential to allow users to verify their digital identities online while maintaining control over sensitive personal data in healthcare, financial services and elsewhere.

- Cryptocurrencies do play a role within ransomware. However, the increase in ransomware is not being driven by cryptocurrencies, rather a lack of adequate cybersecurity and limited information sharing. Open-source blockchain technology and increased information sharing with the cryptocurrency ecosystem has the strong potential to reduce the effectiveness of cryptocurrencies as an illicit payment mechanism for bad actors.

Finally, we present several recommendations for how a balanced approach to policy making and regulation can help ensure that the benefits of this new technology come to fruition while maintaining existing protections for consumers.

Understanding the Characteristics of Digital Assets

Our existing financial system relies on outdated legacy infrastructure that requires multiple intermediaries to facilitate financial transactions. Blockchain technology allows for the peer-to-peer transmission of digital assets, which has the potential to enable a more inclusive financial system, with greater security and consumer protection.

Payments and U.S. Dollar backed stablecoins

Digital assets and stablecoins have the potential to help fight global poverty by making cross-border payments faster and more affordable. Today, a typical remittance fee can be as high as 10.9% per transaction,[1] and the World Bank estimates that "[g]lobally sending remittances costs an average of 6.38% of the amount sent.[2] In addition, international money transfers can take anywhere from 1 to 5 business days depending on the banks involved, the destination country, bank hours of operation, and currency conversions needed.[3] In contrast, payments providers operating in South America and Africa using bitcoin and other open cryptocurrencies charge transaction commissions as low as 1%.[4] Since analysts expect that the remittance market will grow by $200 billion to over $900 billion by 2026, lower fees will ensure that more funds go to workers and their families.[5]

Domestically, the lack of a real-time, 24 hours a day payment system in the United States forms the basis for why Americans pay approximately $26 billion in overdraft and high-cost check cashing fees each year.[6] Under the United States' existing legacy payment system, settlement can take anywhere from hours to days, leading individuals to use check cashers or payday lenders to receive real time access to funds. On the other hand, the instantaneous transfer of value enabled by blockchain technology has the potential to reduce and potentially eliminate overdraft risk. Unfortunately, efforts to use digital assets to improve payments systems in the United States are being impeded by a lack of clear regulatory guidance on how digital tokens should be classified – either as a payment instrument or as a security. A recent speech by SEC Chair Gensler suggests, in fact, that he

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[1] "Bitcoin gains traction as vehicle for sending remittances home to Mexico," *Mexico News Daily*, May, 2021.

[2] "Remittance Prices Worldwide," The World Bank, March 2021.

[3] Cecilia Hendrix, "How long do international money transfers take?," *Western Union*, April 5, 2021.

[4] Andalusia Knoll Soloff, "The new wave of crypto users: migrant workers," *Rest of World*, April 26, 2021.

[5] Polly Jean Harrison, "Global Remittance Market is Expected to Grow by $200 Billion by 2026," *The FinTech Times*, June 29, 2021.

[6] Aaron Klein, "The fastest way to address income inequality? Implement a real-time payment system," *Brookings Institution*, January 2, 2019.

views certain stablecoins to be securities.[7] In most cases, however, stablecoins would appear not to be securities, but rather to be payments instruments.[8]

We support a regulatory approach towards stablecoins that not only provides clarity, but also does not classify these payments-oriented stablecoins as securities, and thereby subject to a regulatory regime not currently used for regulating payments instruments. If an appropriate regulatory framework is provided for stablecoins, we believe that new market intermediaries will emerge to provide services to expedite when and how working families receive payroll funds, send remittances, and pay bills in a much less expensive way than currently offered by existing intermediaries. These types of developments have the potential to lower the costs currently experienced by lower income Americans and provide greater access to payments services to the 7.1 million U.S. households that are unbanked[9].

Utility tokens & data ownership

Digital assets provide solutions for many more use cases than just payments. While bitcoin is fundamentally a digital commodity that can be used as a payments instrument,[10] research on similar digital assets around the globe shows that the dominant feature of digital assets is access to platform services.[11] Many digital assets are utility tokens, which are purchased to be used for a consumptive purpose, offering holders the ability to access a network's services or participate in a community. These "utility tokens" can form the foundation of systems that track real assets or offer privacy-protecting technology services (e.g., credit rating and cloud storage). They are distinctly different from digital assets that meet the SEC definition of a security, which are purchased as an investment.[12]

Utility tokens have the potential to play an important role in granting consumers greater ownership of their own financial data. Taking note of Chairwoman Waters' support for the Biden Administration's Executive Order on Promoting Competition in the American Economy

[7] "Prepared Remarks of Gary Gensler, Chair of the Securities and Exchange Commission, Before the American Bar Association Derivatives and Futures Law Committee Virtual Mid-Year Program," Securities and Exchange Commission, July 21, 2021.

[8] "DLT has allowed for the creation of new digital forms of money and payment systems that could serve novel purposes and extend some of the well-known economic and regulatory issues with past innovations into the digital realm. Existing stablecoins such as Tether, USD Coin and Maker's Dai aim to serve as a means of settlement for automated financial products. They offer also offer the possibility of so-called "smart" contracts, i.e. self-executing code, and possibilities for "programmable money."" Douglas Arner, Raphael Auer and Jon Frost, "BIS Working Papers, Stablecoins: risks, potential and regulation," Bank for International Settlements, November 2020.

[9] "How America Banks: Household Use of Banking and Financial Services," FDIC, October 19, 2020.

[10] In the Matter of: Coinflip, Inc., d/b/a Derivabit, and Francisco Riordan, CFTC Docket No. 15-29. 2015 WL 5535736, September 17, 2015.

[11] Robert Greene and David Lee Kou Chen, "Singapore's Open Digital Token Offering Embrace: Context & Consequences," *The Journal of the British Blockchain Association*, June 28, 2019.

[12] "Understanding Digital Tokens: Market Overviews and Guidelines for Policy Makers and Practitioners," Chamber of Digital Commerce, July 2018, 22.

("Competitiveness EO"),[13] we understand that she shares our concern that consumer financial data is often inadequately protected and secured and misused by intermediaries.

Services built upon utility tokens and blockchain technology can give consumers more control over their data and reduce financial fraud.[14] For example, Chamber members such as IBM, Burst IQ, and Ontology are leveraging blockchain technology to allow users to verify their digital identities online while maintaining control over sensitive personal data in healthcare, the auto industry, financial services and elsewhere.[15] These innovations provide competitive opportunities that align with the goals of the Executive Order.

Low-cost, more equitable access to fundraising for technology projects

Outside of the United States, open digital token offerings (i.e., where a portion of the tokens developed are available to the public) have lowered the costs of blockchain-based technology projects to raise funds. Notably, in the United Kingdom and Singapore, regulators have warned of the consumer protection risks associated with such token offerings, but at the same time have emphasized that the regulatory framework clearly permits the sale of digital assets as part of the launch of an open blockchain project.[16] In the United States, however, a regulatory crackdown on open digital token offerings has forced entrepreneurs to rely upon traditional fundraising channels – such as venture capital. Women and minorities face especially challenging circumstances in raising capital. Data shows that in the first half of 2021, only 2% and 1.2% of venture capital dollars went to firms founded by women and black entrepreneurs, respectively.[17]

Allowing for digital token offerings in the U.S. could help expand greater access to early-stage technology projects, and potentially levels the playing field for women and minority entrepreneurs. Data shows that minorities are adopting digital tokens at a higher rate than other demographics,[18] suggesting that minorities would be better served by a capital structure that utilizes digital assets.

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[13] Elizabeth Warren, "Warren Statement On President Biden's Effort to Promote Competition, Bolster Antitrust Enforcement," July 9, 2021.

[14] "How Blockchain Could Disrupt Banking," *CBInsights*, February 11, 2021.

[15] IBM has developed a blockchain based platform that has been used by businesses, universities, and others to manage digital identities. "Blockchain for digital identity and credentials," IBM, last accessed November 3, 2021. Burst IQ has created a platform for personalized healthcare identities. Burst IQ, Company, accessed November 4, 2021. Ontology's decentralized identity application is being used in various leading consumer products including Mercedes-Benz vehicles. Ontology, "Over 1.5 Million Users Now Managing Their Digital Identity Using ONT ID, Ontology's Decentralized Identity Application," September 9, 2021.

[16] Robert Greene and David Lee Kou Chen, "Singapore's Open Digital Token Offering Embrace: Context & Consequences," *The Journal of the British Blockchain Association*, June 28, 2019.

[17] Diane Wong, "Reflecting On Our Progress: One Year Since The Launch Of Diversity Spotlight," *Crunchbase*, August 16, 2021.

[18] According to a recent Harris Poll survey, 13% of whites, 18% of African Americans, and 20% of Hispanics own cryptocurrencies. Akayla Gardner, "Black Americans Are Embracing Stocks and Bitcoin to Make Up for Stolen Time," Bloomberg, April 13, 2021.

Non-fungible tokens

Another increasingly popular category of digital assets are non-fungible tokens (NFTs), which can be thought of as digital collectible. NFTs provide an excellent example of how digital assets can expand economic opportunity. Historically disadvantaged communities are increasingly selling non-fungible tokens 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, half of which is attributable to a single individual[19].

However, 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.[20] In addition, several organizations have formed to promote the work of black artists in the digital space.[21] Similar efforts are being made to expand inclusivity in art through NFTs for women,[22] transgender youth,[23] and other traditionally marginalized groups. Here again, regulatory clarity is critical – a lack of guidance from the SEC as to whether, and why, NFTs could be considered securities has the potential to stifle innovation and prevent NFTs from continuing to enable economic equity.

As described above, the current use cases of digital assets are already helping create a more inclusive and dynamic economy. Over time, this technology has the potential to transform the infrastructure underpinning much of our online economy. However, further growth in this area faces significant legal and regulatory headwinds. At a basic level, there is uncertainty about how digital assets fit within the traditional definitions of “security,” “commodity,” and “currency.” Apart from definitional issues, there is a lack of regulatory guidance about how financial intermediaries can interact with these assets while meeting obligations around custody, anti-money laundering (“AML”) and know your customer (“KYC”), tax, accounting and other existing regulatory requirements. With this disintermediating technology, regulatory uncertainty can also fall heavily on the end user. In particular, the lack of clarity around the tax treatment of digital assets creates a strong disincentive to participate in this new ecosystem.

The Benefits and Risks of Decentralized Finance

Some of the most promising social benefits of digital assets have yet to be introduced. For example, DeFi could ultimately result in significant improvements in social equity and financial inclusion. ‘DeFi’ is a broad term that refers to decentralized finance alternatives to traditional services that are generally built on open source blockchains.

[19] Charlotte Burns and Julia Halperin, For African American Artists, the Market Remains Woefully Unbalanced, *Sotheby's.com*, February 2019

[20] Cuy Sheffield, “Why I'm Collecting Black Crypto Art,” Medium, Dec. 21, 2020 (citing One/Off data).

[21] One/Off, About, accessed November 3, 2021. Black NFT Art, About, accessed November 3, 2021.

[22] Marris Adikwu, “How Women Are Carving Out a Space in the NFT Market,” *Vogue*, March 2021.

[23] Dan Avery, “Transgender teen's crypto art series fetches $2.16 million at Christie's,” *NBC News*, July 2021.

Putting DeFi in context

While instances of questionable activity, including fraud, in DeFi have increased in dollar terms, as a percentage of overall DeFi activity, this activity is relatively miniscule. In 2021, funds sent from illicit wallets to DeFi protocols represented less than 1% of the total $150 billion market cap of DeFi.[24] The growth in legitimate DeFi activity illustrates a focused commitment by the industry to ensure consumer protection and adherence to a self-established regulatory framework. It also highlights the readiness of consumers to embrace DeFi solutions that provide greater ownership of their own money and control over their financial future, while dramatically lowering the cost of financial services.

As you also know, fraud is not unique to DeFi or to digital assets. The SEC and the CFTC consistently bring a stream of enforcement cases against Ponzi and precious metals schemes, for example. Wherever fraud exists, regulators must take all necessary steps necessary to combat it. Notably, as the DeFi industry develops, more sophisticated surveillance and market intelligence tools will provide the ability to better monitor and combat fraudulent activity in DeFi markets.

Lowering the cost and increasing the availability of basic financial services

In the United States, approximately 46 million people, representing 18% of the adult population, are either unbanked or underbanked.[25] The underbanked tend to be less educated, less wealthy, and more diverse than the fully banked.[26] Unbanked and underbanked Americans must often settle for low-interest or non-interest bearing savings rates coupled with high fees.[27] In 2020 alone, banks amassed over $30 billion in overdraft fees.[28] In addition, banks, both traditional and digital, earn significant revenue from charging fees when a customer uses an out of network ATM.[29]

As you are likely aware, bank fees are disproportionately borne by minorities.[30] This fee disparity may help explain a recent Harris poll where a large proportion of minorities and LGBTQ people in the United States indicated that they feel that the banking system has

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[24] Money laundering conducted using DeFi in 2021 totaled $900 million, according to Chainalysis. "2022 Crypto Crime Report," Chainalysis, 2022, p. 12. In 2021, the total DeFi market cap was estimated to be $150 billion. CoinGecko, "Yearly Report 2021," January 21, 2022, p. 31.

[25] "Economic Well-Being of US Households in 2020," Board of Governors Federal Reserve System, May 2021, 45.

[26] *Ibid.*

[27] "The FinHealth Spend Report 2021," *Financial Health Network*, 2021.

[28] Annie Nova, "Banks will collect more than $30 billion in overdraft fees this year. Here's how to avoid them," *CNBC* (Dec. 1, 2020).

[29] Andrew Pentis, "Bank ATM Fees: How Much Do Banks Charge and How Can I Avoid Them?," *ValuePenguin*, August 2021. *See also,* Kia Kokalitcheva, "Scoop: Chime's fee income," *Axios*, January 2021.

[30] A recent study showed that in the United States, 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. Mary Wisniewski, "Survey: While checking fees vary wildly by race and age, Americans stay loyal to their banks," *Bankrate*, January 15, 2020.

treated them unfairly.[31] Minorities and LGBTQ people are adopting cryptocurrencies at a higher rate than other demographics.[32]

DeFi has the potential to offer basic financial services at a lower cost, without bias, and with better accessibility for unbanked and underbanked individuals relative to existing intermediaries. Policymakers have acknowledged the potential for digital assets to serve the unbanked.[33] DeFi offers particular benefits, such as the ability to self-custody digital assets and to effect lower cost payments and remittances.

Protecting Consumers

The unique benefits offered by DeFi and digital assets relative to existing products and services explained above hinge upon the application of an appropriate regulatory framework. The Chamber strongly believes that rooting out bad actors and prosecuting fraud and manipulation in the digital asset and DeFi markets is important to ensuring sound, trustworthy markets. It is important to understand, however, that the vast majority of digital asset transactions, products, and platforms involving U.S. persons operate within the framework of existing regulations, despite a degree of uncertainty around some of those regulations.

The SEC already has authority to regulate digital assets that meet the definition of a security, as well as the exchanges and brokers that facilitate the trading of such securities. The SEC has used this authority to bring a growing number of high-profile enforcement cases against issuers of digital assets for failure to register their offerings as securities transactions.[34] It has also brought cases against market participants for failure to register as a broker,[35] failure to register offerings of swaps to non-eligible contract participants,[36] and failure to disclose compensation when promoting a security.[37] SEC Chair Gensler has also noted the SEC has authority to regulate DeFi projects that may involve securities.[38] However, despite claims to the contrary, the SEC's rules as they relate to digital assets are, in some cases, not technology-neutral and the industry has repeatedly requested that the

[31] Nicholas Pongratz, "Crypto Adoption Higher Among Minorities, LGBTQ in USA," *Beincrypto*, August 2021.
[32] *Ibid.*
[33] Jonathan Ponciano, "Sen. Warren Says Crypto Could Solve Big Banks' 'Enormous Failure' Of Not Serving Millions Of Low-Income Americans," *Forbes*, July 28, 2021.
[34] "SEC Charges Blockchain Company for $6.3 Million Unregistered ICO," Securities and Exchange Commission, August 12, 2019. *See also* "SEC Orders Blockchain Company to Pay $24 Million Penalty for Unregistered ICO," September 30, 2019. *See also* "Company Settles Unregistered ICO Charges After Self-Reporting to SEC," Securities and Exchange Commission, February 20, 2019.
[35] "SEC Sanctions Operator of Bitcoin-Related Stock Exchange for Registration Violations," Securities and Exchange Commission, December 8, 2014.
[36] "SEC Charges App Developer for Unregistered Security-Based Swap Transactions," Securities and Exchange Commission, July 13, 2020.
[37] "Actor Steven Seagal Charged With Unlawfully Touting Digital Asset Offerings," Securities and Exchange Commission, February 27, 2020.
[38] Dave Michaels and Paul Kiernan, "Crypto's 'DeFi' Projects Aren't Immune to Regulation, SEC's Gensler Says," *The Wall Street Journal*, August 19, 2021.

SEC provide clear and binding guidance on a range of issues on how and when its rules apply to digital assets.

In fact, the Chamber, many of our members, and other industry advocates have engaged extensively with the SEC (and other financial regulators) to request clear rulemaking and binding interpretive guidance on the application of existing securities and derivatives requirements to digital assets.[39]

Despite these efforts, significant uncertainty remains as to when a digital asset should be deemed a security, a commodity or neither, as well as how to custody of digital assets, how to meet clearing and settlement requirements, and issues regarding the registration process of an exchange or alternative trading system (ATS) that facilitate secondary transactions in digital assets that the SEC deems to be securities.[40] Without this guidance, firms operating in the digital asset space have been hampered by a lack of certainty as to how they can operate while meeting the SEC's requirements.

We respectfully disagree with Chair Gensler's assertion that in the absence of SEC authority over digital asset trading platforms, "there's really no protection around fraud or manipulation."[41] The CFTC has fraud and anti-manipulation enforcement authority over the spot market for commodities,[42] which include digital assets such as bitcoin and ether, as well as regulatory authority of the derivatives markets, which includes registered derivatives exchanges.[43] This authority extends into DeFi markets,[44] and has been used by the CFTC to bring enforcement cases.[45] Digital asset trading platforms are also subject to state-level money transmitter and payments laws and many cryptocurrency businesses have also been required to register and report to the Financial Crimes Enforcement Network ("FinCEN") as money servicing businesses.[46]

The Chamber continues to stand ready to work with the SEC and other financial regulators on these issues.

Finally, it is important to note that market participants have taken the lead in instilling greater transparency for investors and integrity within these markets through the development of

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[39] Token Alliance, "Considerations and Guidelines for Securities and Non-Securities Tokens," Token Alliance, August 2019. *See also* "Considerations and Guidelines for Securities and Non-Securities Tokens," Chamber of Digital Commerce, August 2019.

[40] Commissioner Hester Peirce, "In the Matter of Poloniex," Securities and Exchange Commission, August 2021.

[41] Nikhilesh De, "SEC Chair Gary Gensler Recommends Congress Regulate Crypto Exchanges," *CoinDesk*, May 2021.

[42] "CFTC Jurisdiction Over Cryptocurrency: Implications for Industry Participants," *White & Case*, November 2019.

[43] 7 U.S.C. § 6.

[44] Commissioner Dan M. Berkovitz, "Climate Change and Decentralized Finance: New Challenges for the CFTC," CFTC, June 8, 2021.

[45] "CFTC Orders Coinbase to Pay $6.5 Million for False, Misleading, or Inaccurate Reporting and Wash Trading," CFTC, March 19, 2021.

[46] Marco Santori, "What is Money Transmission and Why Does it Matter*,"* *CoinCenter*, April 7, 2015.

industry best practices,[47] advancement of compliance services related to blockchain analytics,[48] market and communication surveillance,[49] and tax compliance.[50]

Systemic Risk and Global Regulation

The Chamber appreciates the President's Working Group on Financial Markets ("PWG") focus on stablecoins and the recent PWG report and recommendations. We note the guidance that Congress act promptly to enact legislation to ensure that payment stablecoins and payment stablecoin arrangements are subject to a federal framework on a consistent and comprehensive basis, and that such legislation should address additional concerns about systemic risk and concentration of economic power.

Notably, other international regulators and standard setting bodies have yet to determine that cryptocurrencies and other digital assets currently pose a systemic risk, including the Bank of England's Deputy Governor[51] and the Financial Stability Board (FSB).[52] While the digital asset market is evolving quickly, and it is certainly appropriate to monitor risks, we believe that such a conclusion would be unwarranted in today's market.

By size, cryptocurrencies' market capitalization of approximately $2 trillion equals just 1.9% of the market for equities[53] and 1.6% of the market for bonds.[54] To date, this market is largely dominated by retail investors,[55] and traditional financial institutions have yet to embrace digital assets broadly.[56] This is due to many factors, but among the most significant is the regulatory uncertainty highlighted above.

The PWG also noted that while Congressional action is urgently needed to address the risks inherent in payment stablecoins, and in the absence of such action, the Financial Stability Oversight Council should consider steps to address the risks outlined in their report. In our recent letter to the President's Working Group on Financial Markets,[57] which we submitted to this Committee for consideration on February 8, 2022, we explain why stablecoins are not

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[47] "Proof of Reserves: The Practioner's Guide to an Emerging Standard for Increasing Trust and Transparency in Digital Asset Platform Services," Chamber of Digital Commerce, 2021.

[48] "Top Crypto Asset Compliance and Risk Management Startups," *Tracexn*, July 18, 2021.

[49] Joe Schifano, "Crypto Surveillance-Regulators Take Digital Assets Seriously," *Eventus Systems*, July 2021.

[50] "Tax & Compliance Automation for Virtual Asset Service Providers," *SOVOS*, accessed October 8, 2021.

[51] Ryan Browne, "Cryptocurrencies don't yet pose a threat to financial stability, Bank of England's Cunliffe says," *CNBC*, July 14, 2021 (quoting Bank of England Deputy Governor Jon Cunliffe: "[t]he speculative boom in crypto is very noticeable but I don't think it's crossed the boundary into financial stability risk").

[52] In the first quarter of 2018, the FSB discussed potential financial stability implications from crypto-assets. The FSB agreed that crypto-assets do not pose a material risk to global financial stability at this time, but supported vigilant monitoring in light of the speed of developments and data gaps. "Crypto-assets: Report to the G20 on work by the FSB and standard-setting bodies," Financial Stability Board, July 16, 2018.

[53] "Capital Markets Fact Book," *SIFMA*, 2021, 43.

[54] *Ibid.*

[55] Caitlin McCabe, "Small Traders Pile Back Into Cryptocurrencies," *The Wall Street Journal*, April 14, 2021.

[56] Emily Graffeo, "78% of institutional investors are not planning on investing in cryptocurrencies," *Markets Insider*, March 3, 2021.

[57] "Letter from Perianne Boring, Founder and President, and Teana Baker-Taylor, Chief Policy Officer, to the President's Working Group on Financial Markets," Chamber of Digital Commerce, October 18, 2021.

systemically important and outline a regulatory framework that is better suited for stablecoins than FSOC designation.

Given the nascent nature of the digital asset markets, we believe a more constructive role for FSOC would be to coordinate financial regulators' efforts to understand how digital asset markets function and to determine whether additional guidance or regulation is needed. Critically, FSOC members should identify ways to maintain technology neutral regulation that does not unfairly disadvantage a new technology such as blockchain. In short, we encourage regulators to embrace the principle of same activity, same risk, same regulation. Where new technology poses new or different risks, those risks, where appropriate, can be addressed through many existing federal and state supervisory frameworks. However, where new technology reduces risk, these reduced risks should also be recognized in the regulatory standards that apply to the activity.

Regulators are only beginning to understand the risks inherent to the digital asset markets. A rush to promulgate new regulations without thoughtful consideration could impede a promising technology and place the United States at a competitive disadvantage to other countries that are taking a more balanced approach to digital assets. Moreover, it is important to consider that the disintermediating nature of cryptocurrencies and DeFi could result in competitive pressure on large, incumbent financial institutions, thereby reducing allowances made for financial incumbents deemed too big to fail and improving financial stability.

Ransomware & Financial Crime

Although one increasingly discussed risk often associated with cryptocurrencies is ransomware, ransomware is not a new phenomenon. The first documented ransomware attack took place in 1989, [58] and in the early 2000s, far before the first bitcoin was mined, criminal organizations began to leverage ransomware.[59] Ransomware payments have taken many forms over the past few decades, including through wire transfers, prepaid debit cards, gift cards, cash payments, and other forms of value.[60] Unfortunately, the use of cryptocurrency is the newest iteration of this scheme.

The true scope of the problem of ransomware is unknown. Uniquely, however, the transparency of public blockchains makes it possible to track ransomware payments in cryptocurrency, as highlighted by the recent ransomware attack on Colonial Pipeline. In that example, using blockchain analytics tools, the FBI was able to trace and track the flow of funds from the victim to the cybercriminals and then seize the funds.[61] As one FBI field agent put it to the Wall Street Journal – "you can't hide behind cryptocurrency."[62] Other

[58] Danny Palmer, "30 years of ransomware: How one bizarre attack laid the foundations for the malware taking over the world," *ZDNet*, December 19, 2019.

[59] Fabio Palozza, "The Origin of Ransomware and Its Impact on Businesses," *Radware Blog*, October 4, 2018.

[60] J.P. Koning, "Fighting Ransomware Doesn't Require Banning Cryptocurrency," *American Institute for Economic Research*, May 2021.

[61] David Uberti, "How the FBI Got Colonial Pipeline's Ransom Money Back," *The Wall Street Journal*, June 2021.

[62] *Ibid.*

forms of ransomware payments such as wire transfers, debit cards, and cash are difficult—if not impossible—to measure, trace and recoup.

We can, however, estimate that ransomware conducted via cryptocurrency demands represents a very small fraction of total financial crime. The UN estimates that the amount of money laundered globally in one year is 2% to 5% of global GDP, or $800 billion to $2 trillion in current U.S. dollars.[63] By comparison, according to Chainalysis data[64], cryptocurrency transactions sent from illicit addresses accounted for just 0.05% of all cryptocurrency transaction volume in 2021,[65] or 0.4% to 1% of money laundered globally.[66]

Digital assets, including stablecoins, which are inherently built on transparent, neutral networks, offer law enforcement the ability to more efficiently identify and trace illicit activity. Moreover, because these networks are not leveraged, they are not "too big to fail." By creating a policy environment whereby payments increasingly rely upon digital assets, we believe policymakers can increase the likelihood that those who commit financial crimes will get caught and reduce the money laundering risks that exist due to the lack of effective AML/KYC policies and controls available today.

Ultimately, to combat ransomware, we encourage policymakers to take actions to bolster the United States' cyber readiness, including through increased funding and information sharing, improving the government's capability to analyze public blockchains, and by cracking down on bad actors (both government and non-government) globally.

Environmental Impact

We note that Committee Members have voiced concerns about the environmental impact of bitcoin mining. Like the traditional financial industry,[67] ensuring the functionality and integrity of digital assets results in energy use. However, digital asset mining brings with it unique benefits to the United States that should not be overlooked. Namely, it is creating jobs and helping to spur more sustainable energy practices.

The digital asset mining industry is increasingly using renewable energy to power its operations. Today, for example, estimates of bitcoin mining companies' use of renewable energy ranges from 39%[68] to as high as 58%.[69] For comparison, in 2020, renewable energy

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63 "Money Laundering," *United Nations Office of Drug & Crime*, accessed November 3, 2021.

64 *Ibid* at 11.

65 "2022 Crypto Crime Report," *Chainalysis*, 2022, p. 10.

66 *Ibid* at 11.

67 While bitcoin's novel protocol sets it apart from traditional payment systems, policymakers should bear in mind that traditional payments systems have a carbon footprint as well. Banks, for instance, have branches, ATMs, offices, and computer systems, all of which contribute to their carbon footprint.

68 "3rd Global Cryptoasset Benchmarking Study," *University of Cambridge Judge Business School*, September 2020.

69 "Bitcoin Mining Council Survey Confirms Sustainable Power Mix," *Bitcoin Mining Council*, 2021.

sources accounted for about 12% of total energy consumption in the United States.[70] Some of this can be attributed to a recent exodus of digital asset mining from China and into the United States resulting in a rapid increase of sustainable energy use.

This increased reliance on renewable energy use is also due to miners helping reduce waste and inefficiencies in energy markets. Digital asset miners have sought out locations where energy is 'stranded' because it cannot reach an end user. Miners' use of hydroelectric[71] and geothermal[72] power is an example of this. Bitcoin miners are also helping reduce waste and carbon emissions in fossil fuel industries as well. For example, bitcoin miners are traveling to oil fields to use natural gas that drillers are unable to transport and typically vent into the atmosphere as methane in a process called "flaring."[73] Methane is a much more powerful greenhouse gas than carbon, and reducing the practice of flaring helps lessen the environmental impact of drilling.[74] Pressure from government and the private sector to reduce carbon emissions overall, will likely continue to propel miners to innovate and seek out renewable and lower carbon-intensive energy sources.

Digital asset mining has also helped create new jobs in states across the country, including Washington, New York, North Carolina, Montana, Texas, and North Dakota.[75] In many cases, these mining companies have chosen to locate operations in areas devastated by deindustrialization and in rural communities, helping reinvigorate those local economies.[76]

With the appropriate policies, the United States has the chance to be a world leader in supporting an industry that will underpin the next evolution in financial services infrastructure while helping propel advances in sustainable energy.

A Better Policy Approach Towards Digital Assets and DeFi

As with any new innovative technology, digital assets may pose opportunities and risks that are not well understood. However, a rational and balanced approach to policy making and regulation can help ensure that the benefits of a new technology come to fruition while maintaining existing protections for consumers. Examples of successfully applying this approach include the development of the Internet, Voice Over Internet Protocol ("VOIP"), and other revolutionary technologies. Today, measured policymaking is necessary to fulfill

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70 "How much of U.S. energy consumption and electricity generation comes from renewable energy sources?," U.S. Energy Information Administration, last modified May 14, 2021.

71 Kate Rooney, "An old Alcoa plant in Upstate New York is going to be converted into one of the world's largest bitcoin mining centers," *CNBC,* June 5, 2018.

72 *Ibid*. *See also* Jamie Crawley, "El Salvador Mines First Bitcoin With Volcanic Energy," *Coindesk*, October 2021.

73 Laila Kearney, "Oil drillers and Bitcoin miners bond over natural gas," *Reuters*, May 21, 2021.

74 "Bitcoin miners help US oil producers cut flaring," *Argus*, October 8, 2021.

75 Taras Kulyk, "Mining Digital Assets Creates Opportunities For Institutional Investors And Communities Alike," *Core Scientific*, March 9, 2021.

76 Matthew De Saro, "Ponderay Newsprint Mill Reopens as Crypto Mining Operation," *Beincrypto*, last modified September 16, 2021. Kate Rooney, "An old Alcoa plant in Upstate New York is going to be converted into one of the world's largest bitcoin mining centers," *CNBC,* June 5, 2018.

the promise of DeFi and digital assets to create a financial system that is faster, cheaper, safer and more inclusive.

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, regulators should consider these policy recommendations:

1) Ensure regulatory coordination

Disparate guidance from the SEC, CFTC, and other regulatory agencies has made it extremely challenging and costly for digital asset and DeFi projects to maintain compliance with applicable regulations as they develop. As suggested above, a constructive role for FSOC to play would be to coordinate the efforts of financial regulators to understand how digital asset and DeFi markets function and to determine whether additional guidance or regulation are needed, and if so, which agency is the appropriate regulator. Critically, FSOC members should consider how to maintain technology neutral regulation that does not unfairly disadvantage new products enabled by blockchain technology.

To this end, the Chamber has urged policymakers and regulators to adopt a comprehensive regulatory plan to support the development of blockchain technology.[77]

2) Develop a clear regulatory framework that defines "digital assets" versus "digital asset securities"

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,[78] 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.[79]

Worryingly, 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[80] and SEC Chair Gensler has commented that stablecoins "may well be securities"

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[77] "National Action Plan for Blockchain," Chamber of Digital Commerce, February 2019.

[78] Framework for "'Investment Contract' Analysis of Digital Assets," Securities and Exchange Commission, July 14, 2021.

[79] Commissioners Hester M. Peirce and Elad L. Roisman, "In the Matter of Coinschedule," Securities and Exchange Commission, July 14, 2021. "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."

[80] Paul Grewal, "The SEC has told us it wants to sue us over Lend. We don't know why," *Coinbase Blog*, September 7, 2021.

without providing justification.[81] However, many stablecoins, particularly those whose primary purpose is to act as a payment method and backed by cash and cash equivalents, should not be classified as a security due to the clear lack of an expectation of profit associated with these digital assets. 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 SEC Commissioner Peirce's "Token Safe Harbor Proposal 2.0" (the "Token Safe Harbor Proposal"), or something similar, would be a constructive step that would facilitate innovation while maintaining standards and disclosure requirements for new products.[82] The Token Safe Harbor Proposal would provide a three-year period for blockchain developers to launch and mature their projects before being subject to full SEC regulation. The Safe Harbor Proposal also exempts from the definition of a security project that has reached network maturity.[83] This proposal would allow developers 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.[84]

An alternative solution to SEC action would be for Congress to pass the bipartisan Securities Clarity Act[85] which provides a clear framework to address the question of which digital assets are securities. This legislation clarifies that a digital asset, in some cases, is distinct from the original securities offering it may have been part of.[86] We believe it strikes the right balance of providing helpful clarity while still being technology neutral and limited in scope.

Another bipartisan legislative effort we support that could help address this issue is H.R. 1602, the "Eliminate Barriers to Innovation Act of 2021", sponsored by Ranking Member McHenry and co-sponsored by Committee Members Representatives Lynch, Budd and Davidson. We were encouraged to see this bill pass the House of Representatives and look forward to the Senate undertaking the bill for consideration. We believe establishing a joint CFTC-SEC working group composed of public and private stakeholders to undertake analysis of the current regulatory structure and recommendations about standards, best practices, and ways to improve the efficacy of these markets would be highly beneficial in beginning to resolve some of the regulatory fragmentation which exists today.

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81 *Hearing Before the Senate Banking, Housing, and Urban Affairs Committee,* 117th Cong., September 14, 2021.

82 Commissioner Hester M. Peirce, "Token Safe Harbor Proposal 2.0," April 13, 2021.

83 *Ibid.* (Defining network maturity as when the network is either i) "[n]ot 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", or ii) "[f]unctional, as demonstrated by the holders' use of Tokens for the transmission and storage of value on the network, the participation in an application running on the network, or otherwise in a manner consistent with the utility of the network").

84 *Ibid.*

85 Securities Clarity Act, H.R. 4451, 117th Cong. (2021).

86 Congressman Tom Emmer, "Emmer Introduces Legislation to Provide Clarity for Digital Assets Under Securities Law," September 24, 2020.

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 custodial 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.[87] At the state level, Wyoming passed a bill allowing for banks to provide custodial services for digital assets.[88] While such steps have been welcome, we hope that they portend more significant steps in the future.

Providing continued clarity on how existing 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) Leverage digital assets and blockchain technology to bolster AML/KYC compliance

Money laundering transactions involving cryptocurrencies are only a fraction of the total value of assets laundered. Moreover, the traceability feature of blockchain technology has proven to facilitate regulators in tracking down money launderers.[89]

Technological developments are facilitating innovation with the potential to significantly enhance KYC compliance. These developments could allow for the establishment of a formal "digital KYC utility" that would verify customer identities across market participants, rather than the current approach of requiring entities serving end-users to obtain and verify the name, date of birth, physical address, and telephone number before onboarding a client.[90] A digital KYC utility could enhance compliance with AML/KYC regulations and permit firms to more efficiently identify potential indicia of illegal behaviors.[91]

More broadly, policymakers should encourage the development of portable digital identities. Portable digital identities allow consumers to access one system for identity verification and utilize the power of the blockchain to transport that identity and access services across firms.[92] Not only will this drastically improve access to services for consumers, but it will also result in less opportunity for identity fraud.

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87 "Interpretive Letter #1170," Office of the Comptroller of the Currency, July 22, 2020. *See also* 17 C.F.R. pt. 240.

88 Wyo. Stat. Ann. § 34-29-101 – § 34-29-105.

89 Uberti, *supra* note 71.

90 Letter from Perianne Boring, President, to Kenneth Blanco, FinCEN Director, Chamber of Digital Commerce, November 26, 2019.

91 *Ibid.*

92 Husayn Kassi, "Portable Identity: giving us control of our digital lives," *Forbes,* October 28, 2019

5) 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, despite the fact that it has not provided meaningful guidance around digital assets and tax rules since 2014.

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

In May 2021, 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.[93] It also sent a letter to the IRS on the application of the Foreign Account Tax Compliance Act ("FATCA") to digital assets.[94]

In addition, the Chamber recently responded to the Financial Accounting Standards Board (FASB)'s Invitation to Comment on FASB's Future Agenda consultation. [95] As we state in that response, we believe that digital assets 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 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 type of 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.

Through the comment process, FASB received a significant response of 522 comment letters. Of these 522 responses, 445 (85% of the respondents) commented solely and exclusively on accounting standards for digital assets, providing feedback on the pervasive impact of digital assets and the need to prioritize standards setting. More than 50% of the respondents indicated that standard setting for digital assets should be considered as the highest priority for FASB. The Chamber understands that the FASB Board will consider the impact of this feedback in upcoming meetings in setting scope and priorities in standard

[93] "Principles and Framework for Appropriate Digital Asset Tax Policy in the United States," Chamber of Digital Commerce, May 14, 2021.

[94] Letter from Amy Davine Kim, Chief Policy Officer, to IRS Assistant Secretary Mazur, Commissioner Rettig, and Acting Chief Counsel PaulLetter from Amy Davine Kim, Chief Policy Officer, to the IRS, Chamber of Digital Commerce, May 14, 2021.

[95] Letter from Perianne Boring, Founder and President, to Financial Accounting Standards Board, Chamber of Digital Commerce, November 26, 2019.

setting and is encouraged by recent statement made by the FASB Chair Richard Jones, who stated “We sometimes accelerate projects, particularly when there’s significant investor interest in an emerging issue.”[96]

Accordingly, the Chamber of Digital Commerce will continue to work with FASB to assure this crucial standard setting is on the agenda and prioritized accordingly because 2022 is going to be a pivotal year. It is clear from the FASB survey that there is demand to address accounting standards for digital assets. At the same time, the U.S. and other countries seem poised to develop clear policy frameworks for digital assets. It is important that all invested in the growth of the digital asset ecosystem continue to work to increase this momentum to bring certainty to the marketplace for innovators and investors alike.

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We appreciate the opportunity to engage with you and your staff on these critical issues. We hope to continue the conversation and find ways we can work with you to help advance financial inclusion, consumer protection, social equity, and other worthwhile policy goals through a balanced policy approach to digital assets.

Very truly yours,

Perianne Boring
Founder and President

Teana Baker-Taylor
Chief Policy Officer

[96] FASB Targets new Long-Term Agenda, Rules on Expense Disclosure in 2022, Wall Street Journal, January 2022.