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Via Email: rule-comments@sec.gov

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

Re: Notice of Proposed Amendments to Exchange Act Rule 3b-16 Regarding the Definition of “Exchange”; Regulation ATS for ATSS That Trade US Government Securities, NMS Stocks, and Other Securities; Regulation SCI for ATSS That Trade US Treasury Securities and Agency Securities (Release No. 34-94868; File No. S7-02-22)

Dear Ms. Countryman:

The Blockchain Association¹ and the DeFi Education Fund² submit these additional comments in response to the Securities and Exchange Commission’s (“**SEC**”) notice of proposed rulemaking to amend the interpretation of the definition of “exchange” in Rule 3b-16 under the Securities Exchange Act of 1934 (“**Exchange Act**”) and to make certain other amendments to

¹ The Blockchain Association is a nonprofit organization dedicated to improving the public policy environment for public blockchain networks so that they can develop and prosper in the United States. We endeavor to educate policymakers, courts, law enforcement, and the public about blockchain technology and the need for regulatory clarity to allow for a more secure, competitive, and innovative digital marketplace. The Association is comprised of over 80 industry leaders who are committed to responsibly developing and supporting public blockchain networks fueled by cryptocurrencies. Our diverse membership reflects the wide range of this dynamic market and includes crypto exchanges, custodians, software developers, early-stage investors, trading firms, and others supporting the crypto ecosystem.

² The DeFi Education Fund is a nonpartisan advocacy group based in the United States with a mission to educate policymakers about the benefits of decentralized finance and to achieve regulatory clarity for the DeFi ecosystem.

Regulation ATS and Regulation SCI under the Exchange Act (“**Proposal**”).³ We share the Commission’s overall goals of leveling the competitive landscape and promoting investor protection in light of technological developments and thank the Commission for its extension of the extremely truncated comment period initially provided to the public on the Proposal.⁴

* * *

Achieving policy objectives in light of new technologies and innovations regularly forces the consideration, development, and adoption of novel regulatory approaches. The United States’ dynamic market economy produces all manner of novel solutions to old problems — “new ways of doing things” — which require dynamic responses to accomplish long-standing public policy objectives.⁵

Regardless of the ever-changing means through which people access and participate in the U.S. securities markets, “our central question” remains: “When new technologies come along and change the face of finance, how do we continue to achieve our core public policy goals?”⁶ To that end, since the enactment of its foundational statutes in the 1930s, the SEC has consistently adapted its regulations in response to innovations in the United States’ dynamic financial markets.⁷ All the while, the securities regime’s core objectives — protecting investors, maintaining fair and orderly markets, and facilitating capital formation — have rightfully remained constant.

³ See Amendments Regarding the Definition of “Exchange” and Alternative Trading Systems That Trade U.S. Treasury and Agency Securities, National Market System Stocks, and Other Securities, 87 Fed. Reg. 15496 (Mar. 18, 2022) (to be codified at 17 C.F.R. pts. 232, 240, 242, 249).

⁴ We note, however, that the Commission’s brief extension of the comment period still does not provide an adequate opportunity to address the substance of the Proposal for at least two reasons. First, given the extraordinary breadth of the Proposal and the fundamental changes that it would make to the securities markets, sixty days is insufficient to fully evaluate and comment on the Proposal. Second, given the lack of clarity in the Proposal itself — for example, by failing to address its impact in the context of digital asset markets — a meaningful comment would require additional explanation from the Commission, not merely additional time.

⁵ See Gary Gensler, Chair, Sec. & Exch. Comm’n, *Prepared Remarks at the Exchequer Club of Washington, D.C.: Dynamic Regulation for a Dynamic Society* (Jan. 19, 2022) (quoting Sec. & Exch. Comm’n, Report of Special Study of Securities Markets of the Securities and Exchange Commission, Part 1, H.R. Doc. No. 95, pt. 1, at IV (1963)), https://www.sec.gov/news/speech/gensler-dynamic-regulation-20220119#_ftn2.

⁶ *Id.*

⁷ See Hester Peirce, Comm’r, Sec. & Exch. Comm’n, *Remarks Before the University of Central Florida’s Inaugural Fintech Summit: Is that a Fish Behind the Wheel?* (Apr. 1, 2022), https://www.sec.gov/news/speech/peirce-remarks-fintech-summit-040122#_ftn22 (“Recently, however, we proposed to free firms from technology that was state-of-the art in 1997, so that they could use today’s technology, which enables much better monitoring of activity.”).

These principles have guided the securities regulatory regime through a century of innovations, innovations that could not have been fathomed by the 73rd Congress.⁸

Adaptable regulatory frameworks founded on constant bedrock principles create a virtuous cycle: they maximize the immense potential of permissionless innovation in our dynamic society while still achieving core objectives via flexible responses.⁹ The U.S. financial markets' preeminence was surely built (in part) via this "flywheel" of innovation in markets and innovation in regulation. This approach has not only benefited U.S. investors and businesses, but also "contributed to America's geopolitical standing around the globe."¹⁰ We must not abandon it.

Failing to adjust regulations to new technologies threatens to create gaps in investor protection and capital formation, and it undermines the preeminence of the United States' financial markets. Establishing by regulation a single acceptable way of solving problems hampers the very dynamism that has led to their competitive advantages. Because regulatory frameworks cannot foresee innovations, and are rarely the source of innovation themselves, failing to adapt them in light of "new ways of doing things" will lead to stasis. It would entrench in perpetuity the current state of affairs as the only acceptable state of affairs, to the detriment of United States markets and investors.

For regulations to vindicate the policy objectives motivating them, they must adapt to *how* an activity is conducted. While both car and airline manufacturers produce vehicles for the same reason — to provide transportation — cars and airlines facilitate transportation in distinct ways. Fortunately, the regulations applicable to car manufacturers and airline manufacturers are responsive to the functional differences through which the vehicles transport people. The same concept is often adopted in the regulation of financial services (e.g., the regulation of checks vs. credit cards) and is especially relevant in the case of decentralized finance protocols.

Decentralized finance ("**DeFi**") protocols join the United States' long history of innovative approaches to conducting well-established financial activities. DeFi software protocols do not change the reasons *why* people and businesses seek financial services — to generate returns, price and hedge risks, make payments, etc. However, these protocols have fundamentally changed *how* people and businesses can access and conduct financial activities. DeFi protocols' "peer-to-peer nature and resulting ability to create alternatives to traditional and centralized financial market infrastructures, products or services"¹¹ represent "a paradigmatic shift in financial

⁸ See Securities Act of 1933, Pub. L. No. 73-22, 48 Stat. 74 (1933) (codified as amended at 15 U.S.C. § 77a).

⁹ See Gary Gensler, Chair, Sec. and Exch. Comm'n, *Address at the Annual Conference on Financial Market Regulation: A Century with a Gold Standard* (May 6, 2022), <https://www.sec.gov/news/speech/gensler-acfmr-20220506> ("Markets don't stand still. Our disclosure and transparency rules can't stand still, either. Thus, over the generations, the Commission often has updated disclosure and transparency regimes.").

¹⁰ *Id.*

¹¹ International Organization of Securities Commissions, *IOSCO Decentralized Finance Report*, at 2, OR01/2022 (2022), <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD699.pdf>;

see also International Monetary Fund, *Shockwaves from the War in Ukraine Test the Financial System's Resilience*, Global Financial Stability Report, at 73 (Apr. 2022),

services provisioning and promises to be one of the most disruptive applications of blockchain-fuelled decentralization.”¹² They are “a novel phenomenon.”¹³

Because DeFi protocols represent a major development in how financial activities can be accessed and conducted, “it is obvious that simply copying traditional regulatory approaches in a decentralized environment may not be an option, since [these approaches] have traditionally focused on intermediaries that play a central role in the [traditional] financial system.”¹⁴ Because

<https://www.imf.org/en/Publications/GFSR/Issues/2022/04/19/global-financial-stability-report-april-2022> (“Decentralized finance refers to financial applications—called “smart contracts”—processed by computer code on blockchains, with limited or no involvement of centralized intermediaries.”);

European Commission, Directorate-General for Financial Stability, Financial Services and Capital Markets Union, *European Financial Stability and Integration Review 2022*, at 43 (Apr. 7, 2022), https://ec.europa.eu/info/sites/default/files/european-financial-stability-and-integration-review-2022_en.pdf (“[D]ecentralised finance. . . is a newly emerging form of autonomous financial intermediation in a decentralised digital environment power by software – ‘smart contracts’ on public blockchains.”);

Organization for Economic Cooperation and Development, *Why Decentralised Finance Matters and the Policy Implications*, at 15 (2022), <https://www.oecd.org/daf/fin/financial-markets/Why-Decentralised-Finance-DeFi-Matters-and-the-Policy-Implications.pdf> (“Decentralised Finance or ‘DeFi’ seeks to provide traditional financial services involving crypto-assets (i.e. mimicking the ‘CeFi’ or centralized finance market) in an open, decentralized, permissionless way.”).

¹² EU Blockchain Observatory and Forum, *Decentralised Finance (DeFi)*, at 38 (2022), https://www.eublockchainforum.eu/sites/default/files/reports/DeFi%20Report%20EUBOF%20-%20Final_0.pdf.

¹³ *Id.*

¹⁴ European Commission, Directorate-General for Financial Stability, Financial Services and Capital Markets Union, *European Financial Stability and Integration Review 2022*, at 59 (Apr. 7, 2022), https://ec.europa.eu/info/sites/default/files/european-financial-stability-and-integration-review-2022_en.pdf;

see also Organization for Economic Cooperation and Development, *Why Decentralised Finance (DeFi) Matters and the Policy Implications* (2022), <https://www.oecd.org/daf/fin/financial-markets/Why-Decentralised-Finance-DeFi-Matters-and-the-Policy-Implications.pdf> (“Some of the characteristics of DeFi may be incompatible with existing regulatory frameworks, particularly given that the current framework is designed for a system that has financial intermediaries at its core. As the existence of intermediaries is contrary to the very essence of decentralized finance, it can be difficult to identify parties involved that can be assessed or regulated, making it challenging to supervise DeFi constructs with the existing oversight architecture. Enforcement of existing regulation could also be difficult to apply given the absence of identified accountable entity in some arrangements. The absence of regulatory/supervisory access points in decentralized DeFi systems is one of the key policy questions that remains to be overcome.”);

International Organization of Securities Commissions, *IOSCO Decentralized Finance Report*, at 36, OR01/2022 (Mar. 2022), <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD699.pdf> (finding

“the existence of intermediaries is contrary to the very essence of decentralized finance,” it will be “challenging to supervise DeFi constructs with the existing oversight architecture.”¹⁵ Unfortunately, the Proposal seeks to do just that.

The Proposal fails to adapt to — let alone acknowledge¹⁶ — the fundamentally new ways in which individuals can conduct asset exchanges using DeFi protocols. Instead, it would improperly apply regulations designed for intermediating exchanges like the New York Stock Exchange to software or software developers.¹⁷ By adopting a static regulatory response to a “paradigmatic” technological development in financial services, the Proposal, unfortunately, will not accomplish the laudable objectives motivating its consideration.

Needless to say, software cannot comply with regulatory obligations; only “persons” with the capacity to modify their own behavior are “regulateable.” But the developers of open-source software are also improper targets for the Proposal. They lack the capacity to modify the code they have developed after it is launched to comply with regulations designed for intermediating financial institutions. In turn, the Proposal’s adoption would, at best, entrench the traditional structure of securities exchanges as the only “acceptable” way for U.S. investors to exchange securities, abandoning the Commission’s long and august history of adapting its regulatory approach in response to the emergence of new technologies and the principle that “no regulation can be static in a dynamic society.”¹⁸ At worst, imposing exchange regulations on software developers would amount to a *de facto* ban on merely “making available” such software

disintermediation “...eliminates market participants that have traditionally acted as gatekeepers, performing central roles of ensuring investor protection and market integrity... Absent these intermediaries – and without appropriate substitute mechanisms – the risk for investor and market harm may be exacerbated.”);

International Monetary Fund, *Shockwaves from the War in Ukraine Test the Financial System’s Resilience*, Global Financial Stability Report, at 82 (Apr. 2022), <https://www.imf.org/en/Publications/GFSR/Issues/2022/04/19/global-financial-stability-report-april-2022> (noting that DeFi “render[s] the traditional approach to regulation ineffective.”).

¹⁵ Ana Badour et al., *OECD Publishes Report on Implications and Policy Considerations of Decentralised Finance (DeFi)*, McCarthy Tétrault LLP (Feb. 10, 2022), https://www.mccarthy.ca/en/insights/blogs/techlex/oecd-publishes-report-implications-and-policy-considerations-decentralised-finance-defi#_ftn12 (citing Organization for Economic Cooperation and Development., *Why Decentralised Finance (DeFi) Matters and the Policy Implications* (2022), <https://www.oecd.org/daf/fin/financial-markets/Why-Decentralised-Finance-DeFi-Matters-and-the-Policy-Implications.pdf>).

¹⁶ The Proposal does not reference DeFi protocols or digital assets directly.

¹⁷ See Hester M. Peirce, Comm’r, *Dissenting Statement of Hester M. Peirce in Response to Release No. 34-88284; File No. SR-NYSEArca-2019-39*, Sec. & Exch. Comm’n (Feb. 26, 2020), <https://www.sec.gov/news/public-statement/peirce-dissenting-statement-34-88284>.

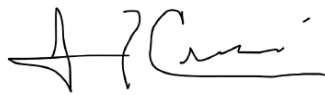
¹⁸ Sec. & Exch. Comm’n, Report of Special Study of Securities Markets of the Securities and Exchange Commission, Part 1, H.R. Doc. No. 95, pt. 1 (1963), https://www.sechistorical.org/collection/papers/1960/1963_SSMkt_Chapter_01_1.pdf.

within the United States, improperly imperiling U.S. citizens' First Amendment-protected rights to write and publish code.¹⁹

Moreover, the adoption of such a static approach to regulating a dynamic technological development will not protect investors, facilitate capital formation, or maintain orderly markets. It would not prevent U.S. users from accessing DeFi protocols, if that were the Commission's ultimate (if ill-advised) goal. DeFi protocols "allow people to come together to trade crypto-assets through automated open-source protocols that are outside the control of any person."²⁰ This means that DeFi protocols will remain accessible to any U.S. user with an internet connection in perpetuity, regardless of whether the Proposal is adopted.

In short, for the Commission to achieve its core policy objectives in the context of DeFi protocols, it must find another way — in collaboration with the U.S. stakeholders supporting and building this technology, rather than in opposition to them. The Blockchain Association and the DeFi Education Fund appreciate the opportunity to provide this additional comment with respect to this important rulemaking. We and our counsel are available to meet and discuss these matters, or to respond to any additional questions, at the Commission's convenience.

Sincerely,



Jake Chervinsky
Head of Policy
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Miller Whitehouse-Levine
Policy Director
DeFi Education Fund

cc: The Hon. Gary Gensler, SEC Chair
The Hon. Hester M. Peirce, SEC Commissioner
The Hon. Allison Herren Lee, SEC Commissioner
The Hon. Caroline A. Crenshaw, SEC Commissioner

¹⁹ See, e.g., *Bernstein v. U.S. Dep't. of State*, 922 F. Supp. 1426 (N.D. Cal. 1996); Justin S. Wales and Richard J. Ovelmen, *Bitcoin is Speech: Notes Toward Developing the Conceptual Contours of Its Protection Under the First Amendment*, 74 U. Mia L. Rev. 204 (2019), <https://repository.law.miami.edu/umlr/vol74/iss1/6>.

²⁰ Hester M. Peirce, Comm'r, *Is that a Fish Behind the Wheel? Remarks before the University of Central Florida's Inaugural FinTech Summit*, Sec. & Exch. Comm'n (Apr. 1, 2022), <https://www.sec.gov/news/speech/peirce-remarks-fintech-summit-040122>.