

10 Key Questions that Must Be Answered Regarding the Senate Agriculture Committee's Crypto Legislation that FTX Endorsed

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Whether one supports or opposes the Senate Agriculture Committee's FTX-endorsed Digital Commodities Consumer Protection Act (the "Sen Ag Bill"), below are ten key issues and questions raised by the bill that should be considered.

1. The Sen Ag Bill would confer legitimacy on

- a) **crypto, a product/system that does little if anything to support real economic activity;**
- b) **registered digital commodity platforms that are subsidiaries of larger crypto platforms currently knowingly and intentionally violating other laws and regulations (including KYC, AML/BSA, sanctions evasion, and securities laws);**
- c) **the expansion of the lightly regulated shadow banking system and invite regulatory arbitrage; and**
- d) **increased interconnection with the traditional banking system, increasing the risk of contagion, crashes and Federal Reserve/taxpayer bailouts.**

First, after more than a decade of promises, there is still [no independently verifiable use case for crypto to support any real economic activity](#). In fact, just the opposite has happened: the industry has proved itself full of charlatans and criminals relentlessly engaging in predatory and criminal conduct. FTX is just the latest example in a very long list.

Second, the CFTC has and will continue to have limited authority to reach beyond its regulated entities, resulting in CFTC-registered subsidiaries of companies like FTX likely being compliant with CFTC rules and regulations, while affiliates and the parent company remain unregulated. In effect, this bill would reward bad behavior by legitimizing a company's CFTC-regulated subsidiary – which may in fact follow the rules – while the parent company and other affiliates engage in reckless, predatory, and perhaps criminal behavior. The CFTC is currently arguing that this is exactly what FTX just did.

Third, by conferring legislative legitimacy on such platforms with much less regulation than other financial firms, the Sen Ag Bill expands the shadow banking system and invites if not guarantees regulatory arbitrage where yet more risk migrates from the more regulated financial system into the shadows.

Fourth, once it has legislative and regulatory legitimacy (which will happen if this bill passes), banks will do more business with crypto firms and bank holding companies will create crypto subsidiaries (that will engage directly in crypto activities as well as create, trade and hold innumerable crypto-related derivatives). As a result, the core of the banking system will become increasingly interconnected with the crypto industry, which makes contagion much more likely, which will directly threaten the stability of the financial system. Imagine if crypto was deeply interconnected with the traditional banking system starting in Nov. 2021 and there had then been a loss of more than two-thirds of value (more than \$2 trillion) over the last year, numerous banks would almost certainly have



been under extreme stress and, like the many crypto firms going bankrupt now, could well have failed. Would the Federal Reserve then have intervened and bailed out those banks and nonbanks as it did in 2008? Given all that, does it make sense to confer legislative legitimacy on such an industry and financial activity?

2. The Sen Ag Bill limits SEC authority by expanding the definition of “commodity,” will result in significantly more litigation, and invites regulatory arbitrage.

There is a broad consensus that Bitcoin is a commodity. However, there is an ongoing debate over whether Ether is a commodity or a security under existing laws. The Sen Ag Bill nevertheless asserts as a matter of law and for all time that Ether is a commodity. By resolving the ongoing legal dispute that way, the bill expands the definition of commodity, restricts the historic definition of securities, and will result in endless litigation because the longstanding legal test for securities will have to be changed to take account of this legislative action. If the bill as drafted becomes law, the financial industry can be expected to start creating products that look like Ether to avoid and challenge SEC jurisdiction. Given that, should the Sen Ag Bill preempt the ongoing legal dispute and declare Ether a digital commodity as a matter of law even though doing so will limit the jurisdiction of the SEC and result in litigation and regulatory arbitrage?

3. The Sen Ag Bill does not provide an express investor protection mandate.

The CFTC regulates commodity and derivatives markets, which historically are overwhelmingly dominated by very large institutions with very little retail investor participation. As a result, the CFTC’s role has mostly been a referee between very large and very well-funded purchasers and producers fully capable of protecting their own interests when seeking price discovery and hedging. However, the crypto industry is targeting retail traders who are likely to experience significant volatility and suffer losses in markets dominated by sophisticated institutions (even if they are not allowed to auto-margin and auto-liquidate 24/7/365 as FTX sought to do with their clearly [reckless application to the CFTC](#)). Given the almost certain influx of potentially millions of retail investors into these institutional markets, should the CFTC have an express, clear mandate to protect investors, and be required to enact rules implementing that mandate, including those related to how crypto products are marketed and sold to retail investors?

4. The Sen Ag Bill would result in the violation of the CEA’s critically important prohibition on “excess speculation.”

The Commodity Exchange Act (CEA) explicitly prohibits “excess speculation” because – unlike equity markets -- speculation is only allowed in commodities markets to the limited extent that it facilitates actual producers and purchasers to engage in price discovery and hedging, which is [critical for the delivery of vital commodities to every American when needed and at prices that reasonably reflect supply and demand](#). This provision is critical to ensure that speculators do not overwhelm commodity markets, increase volatility, drive up prices, cause boom-bust cycles, and threaten shortages of vital commodities. Given that the Sen Ag Bill will open a pathway for millions of retail investors in innumerable commodity markets – all of whom will be speculating and none of whom will be taking actual delivery of any commodities – in violation of the CEA, can and, if so,



how can the inevitable excess speculation be limited to protect commodity markets as well as the American people?

5. The Sen Ag Bill expressly includes two specific financial products, which is unprecedented.

The bill expressly identifies Bitcoin and Ether and declares as a matter of law for all time that they are digital commodities. It is unprecedented for a statute to identify a specific financial product by name because, once included in a statute, that product is legislatively frozen in time. In stark contrast, financial products as well as their labeling and uses frequently change over time, often dramatically, as Ether recently changed from proof-of-work to proof-of-stake. Given that, should the Sen Ag Bill include and codify specific financial products or digital commodities given that it is impossible to know how those financial products will change over time in the future?

6. The Sen Ag Bill allows crypto exchanges to self-certify their products and sell them to retail investors without adequate independent protections, review, or approval, which would also make it extremely difficult for the SEC to challenge self-certified digital commodities that are in fact securities.

Self-certification is an avenue for financial firms to quickly get their latest products into the markets and in front of retail investors usually without any significant review or oversight. Crypto exchanges have an economic incentive to list as many products as possible. Inevitably, the self-certification proposed in the Sen Ag Bill would be very widely used by crypto commodity issuers and platforms. Given the industry's history of breaking or ignoring clearly applicable and longstanding securities and commodities laws, it is only reasonable to assume some will use this process to self-certify products as digital commodities when they are in fact securities. Given the crypto industry is at war with the SEC and desperately wants the weaker CFTC as its regulator, this will result in digital commodity platforms wrongly, either by "accident" or purposefully, self-certifying securities products that trade on their platforms as "digital commodities." As if that wasn't bad enough, this will also create an additional barrier for the SEC to overcome in determining a product is a security, which would harm investors if they are allowed to quickly be offered to investors through self-certification without the SEC having the time or potentially even the knowledge to have input into the review process. Given that, should such self-certification be allowed at all or should an independent financial regulatory agency (fully funded to do this properly) be required to review and, if appropriate, approve products before they are pitched to unsuspecting investors, and should the CFTC be required to provide the SEC with notice and a meaningful opportunity in the self-certification process to raise an objection as to whether the product is in fact a security or not?

7. The Sen Ag Bill preempts state registration requirements.

The state pre-emption clauses in the Sen Ag Bill would likely greatly limit the ability of state regulators to



provide enhanced oversight of crypto commodities and other tokens, including securities. As happened with predatory subprime mortgages in the years before the 2008 financial crash, there are states that provide or might want to provide greater consumer, investor and financial stability protections for their citizens. In fact, New York does that now with its BitLicense, which protected the citizens of New York from the FTX collapse. If New York law was preempted as the Sen Ag Bill would do, untold numbers of New Yorkers would have joined the millions if not tens of millions from other states losing billions of dollars. Given that, should any legislation set a floor not a ceiling, ensuring that all states and markets meet sufficient common minimum standards, while not impeding the ability of state regulators to take additional action or measures if state elected officials determine that to be appropriate?

8. The Sen Ag Bill de facto makes the CFTC (the smallest, least funded, least capable and most capture-able financial regulator) the primary regulator for crypto, which is what FTX and many others in the crypto industry have been relentlessly lobbying for.

The CFTC is one-sixth the size of the SEC; has limited investor protection legislative mandates, capabilities, and experience; has a customer-protection culture, not an investor-protection culture; does not require issuer disclosures; and lacks critical order routing practices and best execution requirements, among other standard investor and market protections. Additionally, the existing CFTC regulatory framework was established, designed, and implemented to facilitate hedging, price discovery, and trading strategies between large, sophisticated entities and financial institutions whereas trading in crypto has much larger retail participation more comparable to stock trading. Yet, despite the fact that an estimated 80% of existing cryptocurrencies would comfortably fall under the longstanding definition of a security, the Sen Ag Bill would effectively make the CFTC the primary regulator of an industry that primarily offers de facto securities for sale to retail investors. Does that make sense?

9. The Sen Ag Bill ignores the reality that existing crypto exchanges offer more than just digital commodities to retail customers and refuses to acknowledge the presence of securities on their platforms.

Crypto exchanges currently facilitate the trading of dozens if not hundreds of different crypto tokens on their platforms, many of which are unquestionably unregistered securities. The bill only governs a small number of these offerings, namely digital commodities, which would give the illusion of regulation while these exchanges simultaneously offer lots of unregistered securities in violation of the securities laws on the same platform. That would seem to guarantee investor confusion if not exploitation, among other things. Given that, should the Sen Ag Bill explicitly state that all crypto tokens that do not clearly meet the definition of a digital commodity must be treated as a security, subject to existing securities laws and regulations, and registered with the SEC or that their legal right to offer digital commodities is automatically revoked?



10. While the Sen Ag Bill provides for some increased funding, the CFTC will need significantly greater funding, time, personnel and expertise to come close to accomplishing the claimed goals of the bill.

The CFTC has been chronically underfunded and has less than 700 employees (whereas the SEC has approximately 4,500 employees). Frankly, the CFTC lacks the resources necessary to do the many jobs it is currently mandated to do by statute. There is little, if any, hope for the CFTC to also undertake regulating, supervising, and policing the vast, novel, and growing crypto industry in addition to their current duties. While there are funding provisions in the Sen Ag Bill, they are grossly inadequate and have too many restrictions. Additionally, protecting consumers, investors and financial stability would seem to require any authorizing legislation to be *conditioned upon the appropriation and receipt of funds by the CFTC* as well a phased implementation over a sufficiently long time period to ensure that it has the personnel, technology, and expertise to actually do the new work and not be overwhelmed by the crypto industry. Given that, should the CFTC's funding be dramatically increased, any limitations eliminated, and required phase-in to ensure that it can both accomplish its current statutory mandates as well as its new responsibilities?

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