

Congress of the United States

Washington, DC 20515

February 6, 2024

The Honorable Janet Yellen
Secretary
US Department of Treasury
1500 Pennsylvania Avenue NW
Washington, D.C. 20220

Dear Secretary Yellen:

Following the collapse of FTX, the House Committees on Agriculture and Financial Services (Committees) embarked on a historic effort to craft legislation providing increased regulatory oversight over the digital asset markets. The Financial Innovation and Technology Act for the 21st Century (FIT21) would provide federal regulators with clear authority over the digital asset spot markets and ensure the customer protections seen in the current financial regulatory structure apply to intermediaries and digital asset-related activities. The Committees engaged in this effort to address the many limitations of digital asset regulations under current law, including a lack of clarity on the treatment of certain digital assets, the lack of sufficient disclosures and other protections for digital asset market customers, and the lack of federal oversight of non-security digital asset intermediaries.

The Financial Stability Oversight Council (FSOC) has issued repeated warnings about the lack of oversight of the digital asset markets and identified the same gaps we sought to address in our legislation.¹ In its 2022 Report on Digital Asset Financial Stability Risks and Regulation, FSOC identified several gaps which were reiterated in FSOC's 2022 and 2023 annual reports²:

- Limited direct oversight of the spot market for digital assets that are not securities;
- Opportunities for regulatory arbitrage; and
- Whether vertically integrated market structures can and should be accommodated under existing laws and regulations.

In 2021, Securities and Exchange Commission (SEC) Chair Gensler identified some of these same gaps as it relates to trading platforms, specifically stating, "I think it's only Congress that could really address it, it'd be good to consider – if it was – if you asked my thoughts, to

¹ Financial Stability Oversight Council's Report on Digital Asset Financial Stability Risks and Regulation (Oct. 3, 2022), available at <https://home.treasury.gov/system/files/261/FSOC-Digital-Assets-Report-2022.pdf>.

² 2023 Financial Stability Oversight Council Annual Report, available at <https://home.treasury.gov/system/files/261/FSOC2023AnnualReport.pdf>; 2022 Financial Stability Oversight Council Annual Report, available at <https://home.treasury.gov/system/files/261/FSOC2022AnnualReport.pdf>.

consider whether to bring greater investor protection to the crypto exchanges.”³ The same week, Chair Gensler emphasized, “while the [SEC’s] sister agency, the Commodity Futures Trading Commission (CFTC), has some limited anti-fraud and anti-manipulation authority, there is no federal authority to actually bring a regime to the crypto exchanges... [the SEC] will be working with Congress, if they see fit to try to bring some protection for people who want to invest in this asset class.”⁴

To highlight the gaps, Bitcoin and Ether have not been recognized as securities. Bitcoin has long been viewed as a commodity, starting with CFTC successfully pursuing enforcement cases⁵ on that basis in 2015.⁶ Ether was also recognized as a commodity by former CFTC Chairman Heath Tarbert in 2019,⁷ a position confirmed again by Chairman Behnam in 2023.⁸ Because these underlying assets are not securities, neither the CFTC nor SEC has the authority to register and regulate trading platforms or other intermediaries engaged in spot transactions in both of these digital assets. Today, multiple CFTC-registered futures exchanges list both Bitcoin and Ether futures as commodity futures contracts.⁹

One concern not raised by the 2022 report was the lack of clarity describing the circumstances in which a digital asset is not offered as part of an investment contract. Despite Chair Gensler’s assertion that “the vast majority of crypto tokens likely meet the investment contract test,”¹⁰ courts have taken a more nuanced view of the law. Several questions remain regarding the SEC’s analysis as it relates to digital assets that may have been initially offered as part of an investment contract.

Last year, in testimony before the House Committee on Financial Services, you stressed the importance of FSOC’s recommendations, stating “[t]here are some gaps like spot markets for

³ SEC Chairman Gensler Remarks before the United States House Financial Services Committee (May 6, 2021), available at <https://financialservices.house.gov/calendar/eventsingle.aspx?EventID=407974>.

⁴ “SEC Chairman Gary Gensler says more investor protections are needed for bitcoin and crypto markets” *CNBC* (May 7, 2021), available at <https://www.cnbc.com/2021/05/07/cnbc-exclusive-cnbc-transcript-sec-chairman-gary-gensler-speaks-with-cnbc-squawk-box-today.html>.

⁵ While the CFTC’s enforcement authority extends to both commodity spot market and derivatives markets transactions, participants, and intermediaries, where the CFTC has the authority to police for fraudulent and manipulative activity, the CFTC currently does not have regulatory authority over spot market transactions or intermediaries in the non-security digital asset spot markets.

⁶ In *The Matter of Coinflip, Inc.*, CFTC Docket No. 15-29 (Sep. 17, 2015), available at <https://www.cftc.gov/sites/default/files/idc/groups/public/@lrenforcementactions/documents/legalpleading/enfcoinfliprorder09172015.pdf>.

⁷ Daniel Roberts, “CFTC says cryptocurrency ether is a commodity, and ether futures are next,” *YahooNews!* (Oct. 10, 2019) available at <https://finance.yahoo.com/news/cftc-says-cryptocurrency-ether-is-a-commodity-and-is-open-to-ether-derivatives-133455545.html>.

⁸ Jesse Hamilton, “U.S. CFTC Chief Behnam Reinforces View of Ether as Commodity,” *CoinDesk*, (Mar. 28, 2023) available at <https://www.coindesk.com/policy/2023/03/28/us-cftc-chief-behnam-reinforces-view-of-ether-as-commodity/>.

⁹ Designate Contract Market Products (last accessed on February 5, 2024) available at <https://www.cftc.gov/IndustryOversight/IndustryFilings/TradingOrganizationProducts>.

¹⁰ SEC Chair Gary Gensler Remarks before the Piper Sandler Global Exchange & Fintech Conference (Jun. 8, 2023) available at <https://www.sec.gov/news/speech/gensler-remarks-piper-sandler-060823>.

crypto assets that are not securities.”¹¹ In June of 2023, Chairman Behnam testified before the House Committee on Agriculture further emphasizing, “[t]he events over the past year bring added urgency to these recommendations. The bankruptcy of several large digital asset platforms erased billions of dollars in customer funds. Multiple large market participants allegedly engaged in manipulative and abusive trading activity, including through opaque arrangements with affiliated trading platforms, undermining confidence in these nascent markets. Cybersecurity vulnerabilities continue to be exploited in weekly hacks, resulting in billions of dollars in lost funds.”¹²

Moreover, in January 2024, Chairman Behnam reiterated his call for spot market oversight, declaring “[t]he concerns I have publicly voiced for the better part of six years regarding the digital asset commodity spot market have only become magnified. The need for federal legislation over cash market digital assets has never been more critical, and I will continue my call for action.”¹³ We could not agree more with you and Chairman Behnam.

To address these gaps, the Committees worked together to introduce and advance FIT21. In doing so, the Committees engaged with several members of FSOC for feedback. The legislation provides the CFTC with jurisdiction over non-security digital asset spot markets and clarifies the SEC’s jurisdiction over digital assets offered as part of an investment contract. Most importantly, FIT21 imposes robust customer protections on all entities required to be registered with the SEC and CFTC.

Over a year after the collapse of several digital asset firms and the associated customer losses, digital asset firms continue to operate despite the ongoing gaps in federal oversight. FIT21 provides comprehensive oversight of the spot market for digital assets that are not securities, and closes the gaps repeatedly identified by FSOC.

To further understand how FSOC is facilitating coordination and communication between the SEC and CFTC as it relates to federal oversight of the spot market for digital assets that are not securities, please respond to the questions outlined below.

1. According to the 2018 FSOC Annual Report, the Digital Assets Working Group was established in 2017 “to facilitate coordination among U.S. financial regulators regarding these markets” and to examine “issues related to digital assets and distributed ledger technology, including financial institutions’ exposures to digital assets, potential cybersecurity and operational risks related to these assets, illicit activity undertaken with digital assets, and international coordination on these topics.”¹⁴ While the 2022 Annual

¹¹ Treasury Secretary Janet Yellen Remarks before the United States House Financial Services Committee (Jun. 13, 2023), available at <https://financialservices.house.gov/calendar/eventsingle.aspx?EventID=408850>.

¹² CFTC Chairman Rostin Behnam Remarks before United States House Committee on Agriculture (Jun. 6, 2023), available at https://www.cftc.gov/PressRoom/SpeechesTestimony/opabehnam36#_ftn2.

¹³ Keynote of CFTC Chairman Rostin Behnam at the ABA Business Law Section Derivatives & Futures Law Committee Winter Meeting (Jan. 26, 2024), available at <https://www.cftc.gov/PressRoom/SpeechesTestimony/opabehnam41>.

¹⁴ 2018 Financial Stability Oversight Council Annual Report, available at <https://home.treasury.gov/system/files/261/FSOC2018AnnualReport.pdf>.

Report provides some limited information on the activities of the Working Group in that year, it is not clear what it focused on in prior years. Please provide documentation detailing the Working Group meetings held from 2017 to 2023, agencies represented for each meeting, and topics discussed at each meeting.

2. Given the SEC’s assertion that digital assets may not themselves be securities, and the district court’s holding in *SEC vs. Ripple Labs, Inc.*, that the digital asset at issue was not itself a security, could you clarify FSOC’s assertion that the securities laws must apply to all “crypto-asset issuers” and any secondary transactions with the “crypto-asset?”
3. Chair Gensler has declared that “the vast majority of crypto tokens likely meet the investment contract test.”¹⁵ However, the final investment contract analysis is backwards looking, made by a court after the transaction in question has been completed. How does this reactive legal authority provide adequate protection for customers, in the absence of comprehensive legislation?
4. The Council notes that large parts of the crypto-asset ecosystem are covered by the existing regulatory structure. Collectively, two digital assets alone – Bitcoin and Ether – make up approximately 60% of the market. Is it the view of FSOC that both Bitcoin and Ether are not securities?
5. As FSOC has emphasized, a regulatory gap exists in spot markets for digital assets that are commodities and not securities. But today, the CFTC has anti-fraud and anti-manipulation authority over non-security digital asset transactions, as well as authority over derivatives contracts where a non-security digital asset is the underlying asset. Given the existing authorities of the CFTC over segments of the non-security digital asset market, is it the Council’s view that expanding the CFTC’s jurisdiction to encompass the spot market in non-security digital assets is appropriate?

We appreciate your attention to this request. Please respond no later than February 20, 2024.

Sincerely,



Patrick McHenry
Chairman
House Committee on Financial Services

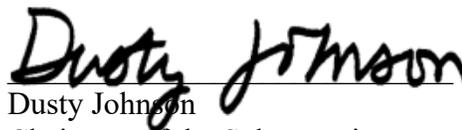


Glenn “GT” Thompson
Chairman
House Committee on Agriculture

¹⁵ See Gensler, supra note 10.



French Hill
Chairman of the Subcommittee on
Digital Assets, Financial Technology
and Inclusion



Dusty Johnson
Chairman of the Subcommittee on
Commodity Markets, Digital Assets,
and Rural Development

cc:

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