

## **Public Statements & Remarks**

### **Remarks of Commissioner Dawn D. Stump Before Texas A&M’s Bitcoin Conference “Innovation and Regulation”**

**April 16, 2021**

#### **Introduction**

Thank you to Professor Korok Ray and Texas A&M University for the kind invitation to participate in this conference. I am happy to be here with you today, even if only virtually. I would much prefer to be back in my home state of Texas to join you in person, but I am nonetheless grateful for the technology that allows me to participate remotely.

Over the course of the conference you have heard others explain various developments in the evolution of bitcoin. Rather than repeat what you have already heard about the tremendous growth and noteworthy interest in bitcoin, my remarks instead will focus on the regulation of bitcoin. There are many federal and state regulators that also have an interest in bitcoin, as well as the entities that trade and custody bitcoin—among the most prominent at the federal level are the Securities and Exchange Commission (SEC), the Office of the Comptroller of the Currency (OCC), the Financial Crimes Enforcement Network (FinCEN), and the Commodity Futures Trading Commission (CFTC or Commission), where I have been privileged to serve as a Commissioner since 2018. Today, my focus is going to be on what we have been doing at the CFTC with respect to bitcoin and digital assets more generally.

Before going any further, I would like to note that the views I express today are my own and not necessarily those of the Commission I am proud to serve upon, nor my fellow Commissioners.

#### **The CFTC’s Regulatory Framework**

The CFTC is perhaps less well known than other financial services regulatory agencies. As our name indicates, we regulate futures contracts—grain futures, energy futures, interest rate futures, etc. And since 2010, after passage of the Dodd-Frank Act,<sup>[1]</sup> the CFTC has also regulated other derivatives products known as swaps. Today, we oversee a \$400 trillion derivatives marketplace.

These derivatives products are used for risk management and/or risk transfer, as well as price discovery for commodities that are an integral part of our daily lives. The CFTC works to ensure that derivatives markets continue serving these risk management and price discovery functions for those who provide us with various goods and services, including farmers feeding the world, pension managers overseeing teacher retirement funds, airlines with fluctuating fuel demands such as that experienced during the Covid-19 pandemic, and mortgage providers offering long-term interest rates for home buyers.<sup>[2]</sup>

#### **The CFTC’s Jurisdiction Over Bitcoin**

*CFTC Regulatory Authority*

The CFTC’s regulatory authority under our authorizing statute, the Commodity Exchange Act (CEA), extends to futures contracts in any commodity, and also includes swaps,<sup>[3]</sup> as well as certain leveraged retail foreign exchange contracts.<sup>[4]</sup> The definition of the term “commodity” in the CEA is very broad—generally defined as goods “in which contracts for future delivery are presently or in the future dealt in.”<sup>[5]</sup> The CFTC has determined that bitcoin fits the legal definition of a “commodity” under the CEA. But treating bitcoin as a commodity is no more surprising or unusual than, say, treating corn, oil, or copper as a commodity, given the breadth of the CEA’s definition of the term “commodity.”

Even though the CFTC has exclusive jurisdiction to regulate futures on commodities, other regulatory bodies may be on the frontline of regulating the underlying commodity itself. For example, the CFTC regulates futures and swaps on interest rates, but the Federal Reserve Board of Governors manages the level of short-term interest rates through its monetary policy. The CFTC regulates natural gas futures and swaps, but the Federal Energy Regulatory Commission regulates the interstate transmission and sale of the underlying natural gas for resale in interstate commerce. Where the underlying is a security, the CFTC regulates certain futures and swaps pursuant to the framework in the CEA and the federal securities laws for allocating jurisdiction between the CFTC and SEC, but in all cases the SEC regulates the underlying securities.

Because this point seems to be confused from time to time, I want to be very clear that the CFTC regulates derivatives associated with the underlying commodities, but not the underlying commodities themselves. In other words, we regulate futures on bitcoin because bitcoin is a commodity—but we do not regulate bitcoin itself, much like we regulate cattle futures because cattle are commodities, but we do not regulate the sale of cattle at auction barns throughout the country.

### *CFTC Enforcement Authority*

As for enforcement activities related to bitcoin (and other digital assets), the CFTC has taken actions against unregistered derivatives exchanges,<sup>[6]</sup> and registered derivatives exchanges that have violated requirements imposed on them by the CEA and CFTC regulations.<sup>[7]</sup> These are the same types of actions the CFTC would take against exchanges offering derivatives involving any other commodity.

You may have seen that just recently, the CFTC brought and settled an enforcement action against a digital asset exchange operator, Coinbase Inc. (Coinbase), for false, misleading, or inaccurate reporting, as well as wash trading by a former employee on Coinbase’s GDAX platform.<sup>[8]</sup> This was a different type of enforcement action because Coinbase is a cash market that has never offered any derivatives products, and thus, as discussed above, falls outside the scope of the CFTC’s regulatory authority under the CEA.<sup>[9]</sup>

It is worth noting at this point that there is a critical distinction between the CFTC’s enforcement authority and the authority we have to conduct day-to-day regulatory oversight. The CFTC’s regulatory authority, as discussed above, is limited to derivatives products such as futures and swaps—as compared to the expanse of our enforcement authority, which is broader.

This is where things get confusing. The CEA does not provide the CFTC with jurisdiction to regulate exchanges or other markets involving cash commodity transactions—be they for corn, oil, or digital assets. While the CFTC does not regulate the underlying cash markets, we do have authority to investigate and prosecute civil enforcement actions in cases of fraud or manipulation in these cash commodity markets—including the bitcoin cash market.<sup>[10]</sup>

Although it may seem odd that an agency not tasked with *regulating* the underlying cash commodity can *bring an enforcement action* concerning the underlying cash commodity, I believe there is a very logical explanation as to what Congress intended here, and I'd like to offer what I view as the rationale. Futures contracts regulated by the CFTC serve a price discovery function. Well-functioning futures (and other derivatives products) rely upon a sound underlying cash market and may reference cash market indexes in their pricing. Therefore, cash market transactions can potentially be part of a scheme to manipulate prices of derivatives products that are regulated by the CFTC. This can occur where, for example, a trader manipulates the cash market for natural gas in order to affect the price of natural gas futures in which the trader has a substantial position.

Congress has recognized these relationships between prices of cash transactions and derivatives products, and thus the CEA provides the CFTC with limited enforcement authority with respect to cash transactions. And this is no different for the cash and derivatives markets for digital assets than for any other commodity.<sup>[11]</sup>

### *The Need for Clarity*

Even with good reason for the broader enforcement authority over bitcoin itself, though, I often worry that the CFTC's exercise of that authority may leave the public with the impression that we are the frontline regulator of cash digital asset markets. This is simply not the case, nor in my opinion is this what the CFTC is best tasked to do. This concerns me for two reasons.

First, I believe it may give the public a false sense of security that when they engage in transactions on cash digital asset trading platforms, they enjoy the protection of CFTC regulatory oversight of digital assets.<sup>[12]</sup> The basis for my concern was illustrated by some of the press coverage of the CFTC's recent enforcement action against the cash exchange Coinbase, such as an article suggesting that the penalty the CFTC imposed on Coinbase "provid[es] further confirmation that the space is regulated."<sup>[13]</sup> This is not the case, and it is incumbent upon the CFTC to make this clear each time we discuss or take action involving digital assets. Only then can these new and innovative products be properly understood and responsibly developed.

Second, I believe it may confuse the public as to what our agency does, and potentially lead to a slippery slope of ever-expanding and ill-defined priorities for the CFTC. I will give an example. During my time working in and around the CFTC, some have suggested that we should regulate things such as benchmarks on cash aluminum, or the cash market for Renewable Identification Numbers (RINs) on every gallon of ethanol produced. This is not what the CFTC is designed to oversee, and regulatory grab is not the objective. We need to stick to what we do best—regulating derivatives products, and involve ourselves in cash commodity markets only to the extent enforcement action is necessary to guard against fraudulent or manipulative conduct that may impact the proper functioning of markets we regulate.

That is, the public should be aware that where cash commodity markets are concerned, limited enforcement authority (anti-fraud/manipulation, as opposed to day-to-day regulatory oversight) is bestowed upon the CFTC as a tool to assist in its primary function of regulating derivatives products, such as futures. However, we are not in the business of regulating bitcoin transactions or the individuals or entities that buy, sell, transfer, or store bitcoin.

## **Innovation & Digital Assets**

Having attempted to clarify any confusion relative to the CFTC's unique role in regulating digital assets, I now want to turn to what truly sets the CFTC apart: Welcoming innovation in financial markets is at the heart of what we do, and I am pleased that we have been at the forefront of innovation with respect to digital assets. It is not an accident that the CFTC is structured to be nimble in order to enable innovation. That was an intentional decision by Congress, and one that I am proud to promote. After all, most all of the contracts listed on the derivatives exchanges we regulate were designed as an innovative solution to an existing problem—even dating back to the 1800s, when grain farmers needed to get grain to processors and processors needed a reliable supply of grain and would arrange for a price in advance, but a lack of delivery or payment often frustrated the process. So, the futures market evolved as an innovative solution.

Now 200 years later, innovation continues to provide solutions and drive demand in our markets. In 2017, the CFTC allowed bitcoin futures contracts to be listed on two futures exchanges.<sup>[14]</sup> Just as has occurred with other commodities, as bitcoin has received more exposure and developed in its utility, the inherent price volatility demands risk management tools and a mechanism for price discovery. Those are the two fundamental purposes of derivatives markets generally—risk management and price discovery.<sup>[15]</sup> Only when an exchange identifies these needs as sufficient to potentially sustain listing the derivatives contract will it seek to do so.

As far as the process for listing futures on digital assets, any new product on a CFTC-regulated exchange can take one of two paths. Exchanges may self-certify compliance with the CEA and CFTC regulations and list the product for trading the following day.<sup>[16]</sup> Alternatively, exchanges can request that the CFTC approve a new product prior to listing, and the CFTC must then approve the product unless the terms and conditions of the product violate the CEA or CFTC regulations.<sup>[17]</sup>

The self-certification process was utilized by the Chicago Mercantile Exchange and CBOE Futures Exchange in 2017, and later by other futures exchanges, to list bitcoin futures.<sup>[18]</sup> This process was deliberately designed by Congress and prior Commissions to give the initiative and option to exchanges to certify new derivatives products without the lengthy CFTC approval process that was required in the Commission's early years.

But self-certification should not be mistaken for hands-off regulatory applications. The CFTC product review teams spend a lot of time with registrants working through those questions we (and the listing exchanges) are obligated to consider. And in fact, we have heightened review methods for digital assets.<sup>[19]</sup> I have found myself, on several occasions, grappling with the application of our process so that it does not exceed the permissible bounds of our assessment—limitations that, as noted above, are designed to avoid impeding innovation and market development. A fact I often need to remind myself.

Some have called into question the self-certification process—and I am always interested in suggestions about how we can make the process more workable. I also would note the responsibility that rests with the exchanges to help assure that the certification process works effectively. But I would caution against dismissing or judging the self-certification process without an eye towards why it exists in the first place, and whether it is preferred to other models in the context of ever-evolving and innovating financial markets.

## **International Developments**

I would like to note that while I may be partial to the CFTC's system of regulation, we do not do so in a bubble. The bitcoin market is a truly global market. The CFTC is a leader in international standard-setting bodies, such as the International Organization of Securities Commissions (IOSCO). While we do not sit on the Financial Stability Board (FSB), our Chairman plays a leadership role in ensuring coordination between IOSCO and the FSB.

As important as the opportunity for setting standards, these fora provide for an equally important dialogue among regulators to better understand each jurisdiction's approach and receptiveness to innovation. It is important to resist generalizing other regulators' positions because the devil is always in the details and sometimes mis-reported. For example, the U.K. Financial Conduct Authority (FCA) is taking a look at the utility of bitcoin among retail investors but seems committed to advancing a framework for institutional investors.[\[20\]](#)

I expect that the U.S. market regulators will continue to be among those that lead on regulatory standards that can responsibly encourage innovation, and to do so we must be active participants around the globe. It is a task that requires many in the federal Government beyond the CFTC—sometimes we lead (say, in the case of our work with IOSCO) and sometimes we support others, such as a few years ago when the G-7 met in France to discuss privacy, money laundering, and consumer protection in the context of digital assets.

The phenomenal growth of digital assets and the proliferation of exchanges for cash digital asset transactions, like many other past market innovations, present unique challenges for various regulators around the globe. It is incumbent upon the entire community of regulators, including the CFTC, to clearly convey the scope—and the limitations—of our role in ensuring that such new innovations can be brought to the public with integrity.

## **XRP Litigation**

There is one final development I want to mention before ending my remarks—litigation involving XRP. As you may know, the SEC recently charged Ripple and two executives with engaging in an illegal securities offering in connection with the digital asset XRP.[\[21\]](#) In its complaint, the SEC alleges that since 2013, the defendants sold more than 14.6 billion XRP tokens worth \$1.38 billion in an unregistered offering.

The question of whether XRP is a security will be crucial. XRP is similar to bitcoin and other digital assets but also different in key respects, which prompted the SEC's investigation. Bitcoin was an open software project launched by a pseudonymous creator calling himself Satoshi Nakamoto. XRP was created, sold initially, and backed by the company known as Ripple.

I am watching the outcome of this case closely because it will help to establish the scope of the SEC's authority in the digital assets space.[\[22\]](#) In this regard, I would like to draw your attention to the important work that has been done by SEC Commissioner Hester Peirce. In a number of speeches that I would encourage you to read, she has addressed the application of the "Howey test" to digital assets.[\[23\]](#) This test refers to the Supreme Court case, *SEC v. Howey*,[\[24\]](#) which provides the framework for determining whether certain assets are securities. I am encouraged by her attempt to create a safe harbor that recognizes both "the need to achieve the investor protection objectives of the securities laws, as well as the need to provide the regulatory flexibility that allows innovation to flourish."[\[25\]](#) I look forward to working with Commissioner Peirce, incoming SEC Chairman Gary Gensler, and the other Commissioners at the SEC and CFTC in applying the agencies' authorities to develop sound public policy with respect to digital assets.

## **Conclusion**

The regulatory application to digital assets, much like the assets themselves, is evolving every day. It is exciting, yet also frustrating to those who seek more certainty. But the incredible transformation in this space requires adaptation and creative thinking, and let's be honest, neither are among a regulator's natural tendencies. This situation reminds me a bit of the many days I spent as a child watching the Texas sky, where clouds move fast such that if you are willing to think creatively you can make out amazing shapes, constantly shifting to tell a great story. On many a long road trip (is there any such thing as a short road trip in Texas?), my brother and I often formed very different stories from the same cloud formations. Sometimes the clouds in Texas quickly develop into devastating storms—and over the years, we have attempted to study, predict, and build safeguards around such events.

That is where the regulatory state of digital assets currently sits: We must enable innovators to think creatively such that the story can evolve, we must acknowledge there will be differences of opinion as to the utility and potential of various products, and we must expect some storms to arise. These are the considerations that should guide us as regulators in exercising the authorities to fulfill our mission such that the market can develop and meet its full potential.

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[1] Dodd-Frank Wall Street Reform and Consumer Protection Act, Public Law 111-203, 124 Stat. 1376 (2010) (Dodd-Frank Act).

[2] See Commissioner Dawn D. Stump, *Maybe Mom's Job is Cool After All: Derivatives Get a Bad Rap, But They Help Keep Hamburgers Affordable*, Roll Call (March 8, 2021), available [here](#). All websites cited herein last checked on April 14, 2021.

[3] CEA Section 2(a)(1)(A), 7 U.S.C. § 2(a)(1)(A). The CEA also provides the CFTC with regulatory authority with respect to certain options transactions. *Id.*

[4] CEA Section 2(c), 7 U.S.C. § 2(c).

[5] CEA Section 1a(9), 7 U.S.C. § 1a(9).

[6] See *In re Coinflip, Inc., d/b/a Derivabit, et al.*, CFTC Docket No. 15-29 (September 17, 2015), available [here](#); *CFTC v. HDR Global Trading Limited, et al.*, Civil Action No. 20-cv-8132 (S.D.N.Y. filed October 1, 2020) (BitMEX), available [here](#).

[7] See *In re TeraExchange LLC*, CFTC Docket No. 15-33 (September 24, 2015) (wash trading and prearranged trading involving a bitcoin swap on a registered swap execution facility), available [here](#).

[8] *In re Coinbase Inc.*, CFTC Docket No. 21-03 (March 19, 2021), available [here](#). See also Concurring Statement of Commissioner Dawn D. Stump Regarding Enforcement Action Against Coinbase, Inc. (March 19, 2021) (Coinbase Concurring Statement), available [here](#).

[9] If Coinbase offered derivatives products, the CEA would require Coinbase to register with the CFTC. Depending on the types of derivatives products offered, the CEA requires that a trading platform obtain CFTC approval to operate as a designated contract market or a registered swap execution facility.

[10] The CEA has always provided the CFTC with certain limited enforcement authority with respect to cash commodity transactions. See, e.g., CEA Section 9(a)(2), 7 U.S.C. § 13(a)(2). This enforcement authority was expanded to some degree by the Dodd-Frank Act. See CEA Section 6(c)(1), 7 U.S.C. § 9(1).

[11] Throughout its history, the CFTC has rightly been judicious, and cautious, about exercising the CEA's enforcement authority in cash markets for commodities for which there is no listed derivatives product traded subject to the CFTC's regulatory authority under the CEA. As I stated in my Concurring Statement in the recent enforcement action against Coinbase, I see no reason why the CFTC should alter that approach for cases involving cash digital asset transactions. See Coinbase Concurring Statement, note 8, *supra*.

[12] Former CFTC Chairman Giancarlo, in congressional testimony, described the practical implications of the distinction between the CFTC's enforcement authority, but lack of regulatory authority, with respect to cash (also sometimes referred to as spot) digital asset markets as follows: "[T]he CFTC does not have authority to conduct regulatory oversight over spot virtual currency platforms or other cash commodities, including imposing registration requirements, surveillance and monitoring, transaction reporting, compliance with personnel conduct standards, customer education, capital adequacy, trading system safeguards, cyber security examinations or other requirements. . . . However, the CFTC DOES have enforcement jurisdiction to investigate through subpoena and other investigative powers and, as appropriate, conduct civil enforcement action against fraud and manipulation in virtual currency derivatives markets and in underlying virtual currency spot markets." Written Testimony of Chairman J. Christopher Giancarlo Before the Senate Banking Committee, Washington, D.C. (February 6, 2018) (emphasis in the original), available [here](#).

[13] Andrew Singer, *Catalytic Event or Unbridled Optimism? Coinbase Approaches Public Listing*, Cointelegraph (March 26, 2021) (citing a senior market analyst at a forex trading company), available [here](#).

[14] By contrast, the SEC has not yet provided investors with access to bitcoin through a product listed and traded on a national securities exchange subject to the SEC's regulatory framework. See Dissenting Statement of Hester M. Peirce in Response to Release No. 34-88284; File No. SR-NYSEArca-2019-39 (February 26, 2020), available [here](#).

[15] See CEA Section 3(a), 7 U.S.C. § 5(a) (derivatives transactions subject to the CEA are affected with a national public interest by providing a means for managing and assuming price risks, discovering prices, or disseminating pricing information through trading in liquid, fair and financially secure trading facilities.).

[16] CEA Section 5c(c)(1), 7 U.S.C. § 7a-2(c)(1); CFTC Rule 40.2, 17 CFR 40.2.

[17] CEA Sections 5c(c)(4)-(5), 7 U.S.C. § 7a-2(c)(4)-(5); CFTC Rule 40.3, 17 CFR 40.3.

[18] More recently, exchanges have used the self-certification process to list ether futures, too.

[19] See Remarks of Chairman J. Christopher Giancarlo to the ABA Derivatives and Futures Section Conference, Naples, Florida (January 19, 2018), available [here](#).

[20] See FCA, *Prohibiting the Sale to Retail Clients of Investment Products that Reference Cryptoassets, Policy Statement PS20/10* (October 2020), available [here](#).

[21] See SEC Press Release 2020-338, *SEC Charges Ripple and Two Executives with Conducting \$1.3 Billion Unregistered Securities Offering* (December 22, 2020), available [here](#).

[22] The outcome of the case could also impact the CFTC's authority with respect to XRP, since CFTC enforcement authorities enacted as part of the Dodd-Frank Act do not apply to securities. See CEA Section 2(a)(1)(H), 7 U.S.C. § 2(a)(1)(H).

[23] See, e.g., SEC Commissioner Hester M. Peirce, *How We Howey*, Remarks, Securities Enforcement Forum, East Palo Alto, California (May 9, 2019), available [here](#). See also William H. Hinman, Director, SEC Division of Corporation Finance, *Digital Asset Transactions: When Howey Met Gary (Plastic)*, Remarks at the Yahoo Finance All Markets Summit: Crypto, San Francisco, CA (June 14, 2018), available [here](#); and Staff of the SEC's Strategic Hub for Innovation and Financial Technology, *Framework for "Investment Contract" Analysis of Digital Assets* (as modified April 3, 2019), available [here](#).

[24] *SEC v. W.J. Howey Co.*, 328 U.S. 293 (1946).

[25] SEC Commissioner Hester M. Peirce, *Running on Empty: A Proposal to Fill the Gap Between Regulation and Decentralization*, Remarks, Chicago, Illinois (February 6, 2020), available [here](#). See also SEC Commissioner Hester M. Peirce, *Token Safe Harbor Proposal 2.0* (April 13, 2021), available [here](#).