Wolters Kluwer

Whitepaper

2023 capital markets legislative agenda suggests new priorities, compliance issues, and less certain pathways to a blockchain framework

By *Mark S. Nelson, J.D.*

Highlights

- Securities regulation in a divided Congress
- The excise tax on stock buybacks explained
- Discussion of which officers are eligible for exculpation in Delaware
- The potential impact of FTX collapse on future blockchain laws

Inside

Introduction

The year in legislation at both the federal and state levels ranged far, with no central themes, although with the mid-term elections now complete, the lame duck Congress may, through various appropriations bills, address at least a small number of additional topics, such as a possible tax patch for the only federal blockchain law enacted to date. Democrats and Republicans also may seek to shore-up select legislative priorities ahead of a 118th Congress, which will be split between Democrats in the Senate and Republicans in the House. These items and more could be addressed via appropriations legislation to keep the federal government open on or after December 16, 2022, the date the current continuing resolution expires.

Nevertheless, 2022 did have a few legislative highlights with echoes into 2023. For one, The House flipped to GOP control so, going forward, expect more oversight of Biden Administration financial regulators and an emphasis on capital formation bills. Blockchain regulation will likely remain an open question, but several bills introduced in the 117th Congress may suggest a path forward with the CFTC in the forefront albeit with SEC authorities preserved. Scrutiny of the IRS's latest round of funding may beget GOP investigations and GOP criticism may increase regarding the newly enacted corporate minimum tax rate and the excise tax on corporate stock buybacks. Meanwhile, Delaware made news in 2022 by enacting a statute revision that permits companies to amend their certificates of incorporation to exculpate some corporate officers for a limited set of beaches of the duty of care.

House GOP securities law agenda

In the 118th Congress, the Senate will remain under narrow Democratic control, but the House will be controlled by a comparatively narrow GOP majority. As a result, most Biden Administration financial regulator nominees should still expect to win Senate confirmation. However, with few exceptions, legislation that must pass a Senate cloture vote may still be difficult enact.

With respect to a GOP-led House, it is expected that financial regulatory priorities will be significantly different than has been the case for the past several years that Democrats controlled the House, with a likely focus on regulatory oversight. For example, a GOP financial agenda could be characterized by some, or all, of the following:

- A focus on JOBS Act-themed capital formation.
- An increase in the frequency with which heads of federal financial regulatory agencies are called to testify before House committees.

- Pushback against the Fed issuing a central bank digital currency (CBDC).
- Smaller increases in appropriations for many financial regulatory agencies.
- The re-introduction of various repeal bills for Dodd-Frank Act and other recently enacted legislation but which likely would not have veto-proof majorities.
- An expectation that *West Virginia v. EPA*-themed oversight focused on the major questions doctrine, possibly coupled with appropriations policy riders and other anti-"woke" legislation, could seek to bar the SEC and other agencies from finalizing climate risk disclosure and other ESG regulations.

With respect to a GOP-led House, it is expected that financial regulatory priorities will be significantly different than has been the case for the past several years that Democrats controlled the House with a likely focus on regulatory oversight.

Although the House will be controlled by Republicans in the upcoming 118th Congress, it is expected that relevant committee leaders will largely remain the same. In the House Financial Services Committee, Rep. Patrick McHenry (R-NC) would likely become Chair, while current Chair Maxine Waters (D-Calif) would shift to the role of Ranking Member. With respect to the House Agriculture Committee, a similar shift would likely occur, with Glenn "G.T." Thompson (R-Pa) becoming Chair and current Chair David Scott (D-Ga) becoming Ranking Member.

In the Senate, leadership also would likely remain largely the same with Democrats retaining control of the Senate. However, retiring Senate Banking Committee Ranking Member Patrick Toomey (R-Pa) will leave an open position that could be filled by Sen. Tim Scott (R-SC) or Sen. Mike Rounds (R-SD). Senator Sherrod Brown (D-Ohio) would likely remain Chair of the Banking Committee. The Senate Agriculture Committee leadership would likely remain unchanged with Sen. Debbie Stabenow (D-Mich) remaining Chair and Sen. John Boozman (R-Ark) remaining Ranking Member.

Corporate tax developments

On August 16, 2022, President Biden signed into law a narrower version of the Build Back Better Act now known as the Inflation Reduction Act of 2022 (H.R. 5376). While much of the bill emphasizes healthcare and climate change, Biden Administration priorities in these areas are to be paid for by targeted corporate tax increases. The minimum corporate tax, for example, brings the U.S. in line with other nations that, along with the U.S., recently committed to impose a 15 percent global minimum corporate tax. Other provisions impose an excise tax on stock buybacks and boost IRS taxpayer services and enforcement resources. The Inflation Reduction Act or IRA advanced in Congress via the budget reconciliation process and passed the Senate 51-50 with Vice President Kamala Harris breaking the tie, while the bill passed the House 220-207.

IRA enacted without GOP support. President Biden summarized the key tax provisions of the IRA upon singing the bill into law: "We're cutting deficit to fight inflation by having the wealthy and big corporations finally begin to pay part of their fair share." The president added that "[b]ig corporations will now pay a minimum 15 percent tax instead of us—five—55 of them got away with paying zero dollars in federal income tax on $40 billion in profit." President Biden also reiterated that middle- and lower-income taxpayers would not pay more in taxes. "And I'm keeping my campaign commitment: No one—let me emphasize—no one earning less than $400,000 a year will pay a penny more in federal taxes," said President Biden.

Republicans, by contrast, panned the IRA as out of step with current economic conditions in anticipation of a presidential signature. "Democrats' response to the recession they caused is giant job-killing tax hikes and doubling the IRS," said Senate Minority Leader Mitch McConnell (R-KY). "Democrats' response to the energy crisis they've exacerbated is a war on American fossil

fuel to fund Green New Deal giveaways for their rich friends. And their response to the runaway inflation they've created is a bill that experts say will not meaningfully cut inflation at all."

With respect to increased funding for the IRS, Senate Finance Committee Ranking Member Mike Crapo (R-Idaho) suggested that even if taxpayers with incomes under $400,000 pay no more in taxes they may disproportionately be the subject of more frequent IRS audits. "When I offered my amendment to simply make it clear that the $80 billion being given to the IRS--six times its current annual budget—could not be utilized to audit people making less than $400,000, the most they would agree to was to say they did not 'intend' to audit them," said Sen. Crapo. "That's because they know from the analysis of the Joint Committee on Taxation that most underreported income occurs among taxpayers earning less than $200,000 per year, and from the Congressional Budget Office that they cannot collect the $200 billion they are claiming without auditing people making less than $400,000."

Other previous stock buyback proposals would have imposed different non-tax requirements, such as holding periods for top executives, restricting buybacks for companies that do not accord their employees certain job benefits, or would have banned buybacks altogether.

Minimum corporate tax. Further corporate tax reforms have been on Democrats' agenda ever since the GOP-led Tax Cuts and Jobs Act enacted in 2017 lowered corporate rates from a pre-TCJA range of between 15 percent, 25 percent, 34 percent, and 35 percent, to a rate of 21 percent that was effective for taxable years beginning after December 31, 2017. The notion of a minimum corporate tax rate was the product of more recent international negotiations aimed at lessening the impact of global tax haven jurisdictions and is a centerpiece of the IRA.

As a result, Section 10101 of the IRA imposes on applicable corporations a tentative minimum tax of 15 percent (for a corporation that is not an applicable corporation, the tentative minimum tax is zero). In general, an "applicable corporation" is any corporation that has average annual adjusted financial statement income for the specified three-year period in excess of $1 billion.

Stock buybacks. Section 10201 of the IRA imposes a 1 percent excise tax on corporate stock buybacks. Specifically, the tax is levied on the fair market value of any stock of a covered corporation which is repurchased by the corporation during the taxable year. The IRA provision has evolved from earlier forms of the buyback tax contained in the Stock Buyback Accountability Act, which would have imposed a 2 percent excise tax on the value of securities repurchased by a covered corporation. Other previous stock buyback proposals would have imposed different non-tax requirements, such as holding periods for top executives, restricting buybacks for companies that do not accord their employees certain job benefits, or would have banned buybacks altogether.

Under the IRA, a "covered corporation" is defined as a domestic corporation whose stock is traded on an established securities market. A "repurchase" of stock is defined consistent with IRC Section 317(b), which provides that stock is considered redeemed by a corporation if the stock was acquired from a shareholder in exchange for property, regardless of whether the acquired stock was cancelled, retired, or held as treasury stock. The excise tax also applies to any transaction the Treasury Secretary determines to be economically similar to a stock repurchase.

However, the tax on stock buybacks does not apply to: (1) reorganizations; (2) repurchased stock (or equivalent amounts) contributed to an employer-sponsored retirement plan or ESOP; (3) buybacks where the value repurchased does not exceed $1 million; (4) repurchases by a dealer in securities in the ordinary course of business; (5) repurchases by a regulated investment company or REIT; and (6) purchases that are treated as dividends.

The IRA's stock buyback provision becomes effective for repurchases after December 31, 2022.

IRS taxpayer services and enforcement. The IRA also emphasizes IRS modernization and enforcement. The IRA, for example, funds various IRS activities at the following levels over the next decade:

- Taxpayer services—$3.2 billion.
- Enforcement—$45.6 billion.
- Operations support—$25.3 billion.
- Business systems modernization—$4.8 billion.

However, lawmakers intended that the IRA would not increase taxes on any taxpayer or small business with taxable income under $400,000. Lawmakers also intended for the IRA not to increase taxes on any taxpayer not in the top 1 percent of taxpayers.

Delaware officer exculpation

On the state law front, the singular event that stands out in 2022 was Delaware's enactment of legislation that brings corporate officers more in line with corporate directors regarding exculpation from liability for breaches of the fiduciary duty of care. However, unlike director exculpation, companies seeking to amend their certificates of incorporation will need to look to both Delaware's law for service of process on nonresidents and to a company's SEC filings to ensure that they have provided for exculpation of all eligible persons who may be corporate officers.

On July 27, 2022, Delaware Governor John Carney signed into law a bill (SB 273) that amends DGCL Section 102(b)(7) to allow Delaware companies to exculpate corporate officers from liability for breaches of the duty of care. Previously, Delaware law permitted companies to provide for the exculpation of directors only. The officer exculpation provision became effective on August 1, 2022.

The new law provides that a company's certificate of incorporation may contain a provision that eliminates or limits the personal liability of a director *or officer* for monetary damages for breach of fiduciary duty as a director *or officer* (emphasis added). However, the law also lists the situations in which an officer may not be exculpated, including for:

- Breach of the duty of loyalty;
- Acts or omissions not in good faith or which involve intentional misconduct or a knowing violation of law;
- Any transaction from which the officer derived an improper personal benefit; and
- Any action by or in the right of the company.

The officer exculpation provision is more narrowly tailored than the equivalent provision that defines who may be a director of a company.

—Which officers are eligible for exculpation? The new law also provides guidance on who is an officer of a company for purposes of exculpation from liability by referencing another Delaware law that governs service of process on nonresident directors and officers (*i.e.*, the new law treats residents of Delaware as if they were nonresidents). Specifically, the law provides that it applies only to a person who at the time of an act or omission as to which liability is asserted is deemed to have consented to service by the delivery of process to the registered agent of the corporation pursuant to §3114(b) of Title 10 of the Delaware Code. The officer exculpation provision is more narrowly tailored than the equivalent provision that defines who may be a director of a company. A director, for example, may be any person who exercises or performs any of the powers or duties otherwise conferred or imposed upon the board of directors by Delaware law.

Thus, under §3114(b) of Title 10 of the Delaware Code, a person is an "officer" if they fall within two categories of persons:

- If, at any time during the course of conduct alleged in the action or proceeding to be wrongful, the person belonged to either of two groups of individuals:
  - The person was the company's president, CEO, COO, CFO, CLO, controller, treasurer, or chief accounting officer; or
  - The person is identified in an SEC filing because they are or were one of the most highly compensated executive officers of the company;
- The person has, by written agreement with the company, consented to be an officer for purposes of §3114(b) of Title 10 of the Delaware Code.

Who is covered by DGCL Section 102(b)(7)?

As mentioned in the main text, Delaware law is the first place to look for information about which company officers may be eligible under the new exculpation provision. However, it may be necessary to also look at a company's SEC filings on EDGAR to get a complete picture of which officers are eligible for exculpation. Here, company counsel, investors, and other interested persons might start by examining a company's annual proxy statement (***i.e.***, DEF Schedule 14A), which will contain required disclosures about executive compensation, including for some of the officers already mentioned indirectly in Delaware law, such as a company's principal executive officer (PEO) and principal financial officer (PFO). But the Delaware exculpation provision and related Delaware laws also suggest that certain "highly compensated executive officers" are eligible for exculpation. This is where it may be necessary to look at federal securities regulations and disclosures made in a company's annual proxy statement.

Item 8 of Schedule 14A instructs a company to furnish the information required by Item 402 of Regulation S-K. Item 402(a)(3) of Regulation S-K defines "named executive officers" to include a company's PEO and PFO, regardless of compensation level, as well as the three most highly compensated executive officers other than the PEO and the PFO, and up to two additional individuals for whom disclosure would have been provided but for the fact that they were not serving as executive officers of the company in the relevant time period. Three instructions to Item 402(a)(3), with an assist from Exchange Act Rule 3b-7, further refine who is an NEO and, thus, potentially an officer subject to Delaware's exculpation provision:

- Instructions to Item 402(a)(3). 1.—To determine if a person is one of the most highly compensated executive officers, do the following calculation:

  Total compensation for the last completed fiscal year

  MINUS

  The Amount required to be disclosed regarding defined benefit and pension plans and preferential earnings on non-tax-qualified deferred compensation

  - **Disclose** if compensation ≥ $100,000
  - **Do not disclose** (other than for PEO and PFO) if compensation < $100,000

- Instructions to Item 402(a)(3). 2.—It may be necessary to include as an NEO one or more executive officers or employees at a company's subsidiaries. It should be noted that Exchange Act Rule 3b-7 defines "executive officer" to include a company's president, any vice president in charge of a principal business unit, or any officer who performs a policy making function, or any other person who performs similar policy making functions; the rule states that executive officers of a subsidiary are included in the definition if they perform policy making functions for the parent company.

  Instructions to Item 402(a)(3). 3.—According to the instruction, it may be appropriate in limited circumstances to omit disclosure of an individual (other than a PEO or PFO) if that individual is an NEO predominantly because of overseas compensation.

Most of the bills introduced in the 117th Congress emphasize the primacy of the CFTC with one bill, the Digital Commodities Consumer Protection Act (S. 4760), receiving the most attention, with the focus remaining on the Senate version and much less on the two House versions of the bill, one of which is identical and one of which omits provisions on anti-money laundering rules and bankruptcy.

A company seeking to exculpate its officers from liability under amended DGCL Section 102(b)(7) would do so by amending its certificate of incorporation. The law further provides that a company may not exculpate an officer for conduct that occurred before the effective date of the amended DGCL provision. Moreover, the amendment, repeal, or elimination of an exculpation provision for a company's officers would not affect the availability of the exculpation provision before its amendment, repeal, or elimination from the company's certificate of incorporation unless the relevant provision provides otherwise at the time of such act or omission.

The officer exculpation provision and other amendments to the DGCL contained in SB 273 was sponsored by Delaware Senator Kyle Evans Gay (D) and sponsored or co-sponsored by 12 other Delaware senators and representatives.

—Proxy adviser recommendations. This is the time of year when interested persons await the 2023 policy guidelines from the two major shareholder advisory firms ISS and Glass Lewis. And this year takes on some added significance regarding what these firms will say about the new Delaware provision on officer exculpation.

Glass Lewis issued its 2023 Policy Guidelines and took a decidedly wait and see approach to Delaware's officer exculpation provision, which the firm said it would review on a case-by-case basis while further noting that the Delaware law requires affirmative action by a corporation to implement. "We will generally recommend voting against such proposals eliminating monetary liability for breaches of the duty of care for certain corporate officers, unless compelling rationale for the adoption is provided by the board, and the provisions are reasonable," said Glass Lewis.

Initially, ISS announced that it had published for comment its Proposed ISS Benchmark Policy Changes for 2023, which includes a section on officer exculpation. "For the U.S. policy, ISS is proposing to generally recommend 'for' proposals providing for officer exculpation provisions in a company's charter," said ISS. The comment period on the proposed voting policy changes ended November 16, 2022.

ISS later issued its Americas Proxy Voting Guidelines Benchmark Policy Changes for 2023: U.S., Canada, Brazil, and Americas Regional in which it stated that votes on officer exculpation proposals (and other officer and director indemnification provisions) be made on a case-by-case basis. ISS would have voters consider several factors in deciding whether to vote for or against such proposals, including whether the provision would eliminate officers' liability for monetary damages related to violations of the duty of care and whether such proposals would include acts that go beyond carelessness. These and other factors were part of ISS's prior recommendation to vote against broadly-phrased officer and director indemnification proposals but the amended recommendation removed the prior language recommending voting against such proposals in favor of new language recommending that voters consider the several factors identified by ISS. A note to the recommendation cited the change in Delaware's law as a motivating factor in shifting the tenor of the recommendation.

The future of blockchain regulation?

The contours of a future Congressionally-mandated federal regulatory framework for blockchain products and services began to take shape during the 117th Congress. Previously, lawmakers introduced numerous bills with highly parochial aims such as excluding digital assets from the

The Digital Asset Market Structure and Investor Protection Act also would authorize the Fed to issue as legal tender digital versions of Federal reserve notes in addition to current physical Federal reserve notes using distributed ledger technology. With respect to being legal tender, the text of the bill is somewhat disjointed but the phrase "The said notes," immediately follows the apparent referent "digital Federal reserve notes," thus, it would appear that the bill would intend for digital Federal reserve notes to be legal tender. Representatives Bill Foster (D-Ill) and French Hill (R-Ark) have both introduced bills to study the feasibility of central bank digital currencies (CBDCs) and to preserve the U.S. dollar as the primary global reserve currency (See, H.R. 2211 and H.R. 3506). Senators James Lankford (R-Okla) and Mike Lee (R-Utah) have both introduced bills to bar the Fed and Treasury from issuing a CBDC and/or would preserve printed money (See, S. 4831 and S. 4994).

definition of "security" under federal securities regulations or to include digital assets among the assets investors may hold in retirement accounts. And yet the only federal blockchain legislation to become law to date has dealt with the IRS's ability to ensure that persons trading digital assets pay their taxes and that bill is the subject of revision legislation that would narrow the reporting requirement to exclude persons and entities that lie on the periphery of those in the blockchain industry who hold information reportable to the IRS.

The big picture. So, what do lawmakers see as the future of blockchain regulation? Over the last two years, five significant bills have been proposed. Most of the bills introduced in the 117th Congress emphasize the primacy of the CFTC with one bill, the Digital Commodities Consumer Protection Act (S. 4760), receiving the most attention, with the focus remaining on the Senate version and much less on the two House versions of the bill, one of which is identical and one of which omits provisions on anti-money laundering rules and bankruptcy. The DCCPA is sponsored by Senate Agriculture, Nutrition, and Forestry Committee Chair Debbie Stabenow (D-Mich) and Ranking Member John Boozman (R-Ark).

The Lummis-Gillibrand Responsible Financial Innovation Act (S. 4356), sponsored by Sens. Kirsten Gillibrand (D-NY) and Cynthia Lummis (R-Wyo), and the Digital Commodity Exchange Act (H.R. 7614), sponsored by House Agriculture Committee Ranking Member Glenn "GT" Thompson (R-Pa) and committee member Ro Khanna (D-Calif), likewise emphasize the CFTC but with both bills taking a more comprehensive approach to blockchain regulation that, in the case of the Lummis-Gillibrand bill, would also address payments, banking, and interagency coordination, while the Digital Commodity Exchange Act would address additional topics such as stablecoins and the voluntary registration of (and disclosures by) digital commodity developers.

The Digital Asset Market Structure and Investor Protection Act (H.R. 4741), sponsored by Rep. Don Beyer (D-Va), like the Lummis-Gillibrand bill and the Digital Commodity Exchange Act, takes a somewhat more comprehensive approach to blockchain regulation. The Beyer bill would achieve its goals by delaying registration of digital asset securities under federal securities laws and by providing for an off-ramp from SEC regulations for any digital asset security whose issuer had filed a desecuritization certification. The bill also would require the SEC and CFTC to jointly classify major digital assets as either digital assets or digital asset securities. The treatment of digital assets under the CEA would focus on digital asset trade repositories. Additional topics addressed by the bill would include stablecoins, FDIC/NCUA insurance noncoverage, and anti-money laundering rules.

Stablecoins. Although House Financial Services Chair Maxine Waters (D-Calif) and Ranking Member Patrick McHenry (R-NC) were expected to introduce a bill dealing with stablecoins, their effort appears to have been delayed by changes requested by the Treasury Department.

As proposed thus far, three of the five major blockchain bills would address stablecoins. The Lummis-Gillibrand bill would amend the Gramm-Leach-Bliley Act to permit a depository institution to issue and redeem payment stablecoins provided that, among other things, the depository institution maintains high-quality liquid assets of at least 100 percent of the face value of issued payment stablecoins. The bill would further require the Treasury Department to issue rules for sanctions compliance and mandate that government regulators establish rules for competition in the payment stablecoin market. The bill also would address the existence

of other countries' stablecoins by requiring the federal government to develop standards and guidelines for the secure use of a Chinese Yuan on government information technology devices. The use of foreign digital currencies on U.S. government devices is a controversial topic and Sen. Tom Cotton (R-Ark) has introduced a bill to prevent such use by U.S. app stores (See, S. 4313).

The Digital Commodity Exchange Act would permit persons to register with the CFTC as fixed-value digital commodity operators. The term fixed-value digital commodity operator would mean any person engaged in a business that solicits, accepts, or receives funds, property, or other assets from others for the purpose of issuing units of a fixed-value digital commodity or who is registered with the CFTC as a fixed-value digital commodity operator. A fixed-value digital commodity would be defined as a digital commodity that is redeemable for a fixed amount of a fiat currency or another commodity. For purposes of the registration of digital commodity exchanges, which may make available for trading any digital commodity that is not readily susceptible to manipulation, a fixed-value digital commodity would not be readily susceptible to manipulation if the issuer of the fixed-value digital commodity is a registered fixed-value digital commodity operator or is otherwise subject to comparably comprehensive regulation by another federal regulator or by a home country regulator.

The Digital Asset Market Structure and Investor Protection Act would require the Treasury Department to approve or disapprove digital asset fiat-based stablecoins (no grandfathering would be allowed). A digital asset fiat-based stable coin would be defined as a digital asset under the CEA that is pegged or collateralized substantially to the U.S. dollar or one or more fiat currencies.

Reports and studies. The Digital Asset Market Structure and Investor Protection Act would require six reports to be submitted to Congress by multiple agencies. The reports would cover taxation, ransomware, decentralized finance, custody of digital assets and digital asset securities, digital asset trading platforms, and false trade reporting (including wash trading and off-chain transactions). The DCCPA would require the CFTC to report to Congress on energy consumption and sources of energy used in connection with the creation and transfer of the most widely traded digital commodities. The DCCPA also would require the CFTC to report to Congress regarding historically underserved customers participating in digital commodity markets.

The DCCPA—a closer look. This section takes a detailed look at the Digital Commodities Consumer Protection Act or DCCPA for the simple reason that this bill had appeared to be the most likely candidate to advance in this or the next session of Congress, at least until the collapse of crypto trading platform FTX. The main outstanding question about the DCCPA is whether any of its terms could significantly curtail SEC regulation and enforcement in the digital asset space. It should be recalled that SEC leadership across both Democratic and Republican Administrations have now taken the view that almost all digital assets are securities and, thus, the SEC continues to have a strong interest in policing the digital asset marketplace. With respect to stablecoins and CBDCs, it would appear likely that separate legislation would be enacted to address these issues. So, with that said, here is a review of key provisions in the DCCPA.

- ***Definitions—***The DCCPA includes numerous of definitions, including:

Digital commodity	Digital commodity trade	Digital commodity platform
"A fungible digital form of personal property that can be possessed and transferred person-to-person without necessary reliance on an intermediary." Includes Bitcoin, Ether and other cryptocurrencies or virtual currencies. Does not include: (1) interests in physical commodities; (2) securities; (3) CDBCs; (4) with certain exceptions for the CFTC's antifraud authorities, instruments regulated by the CEA other than Section 2(c)(2)(F); and (5) any instrument the CFTC excludes from the definition of digital commodity.	"A purchase or sale of a digital commodity in exchange for—(i) another digital commodity; or (ii) any other consideration." Includes: (1) an offer to enter into a purchase or sale of a digital commodity; and (2) loans of digital commodities. Does not include: with certain exceptions for the CFTC's antifraud authorities, instruments regulated by the CEA other than Section 2(c)(2)(F).	A person that is 1 or more of the following: • Digital commodity broker. • Digital commodity custodian. • Digital commodity dealer. • Digital commodity trading facility.

- ***CFTC jurisdiction—***The DCCPA would grant the CFTC exclusive jurisdiction over digital commodity trades, although this jurisdiction would not extend to digital commodity transactions by merchants or consumers where the digital commodity is used only to buy or sell goods or services. Moreover, several key enforcement provisions in the CEA would apply to digital commodity trades, including: (1) the prohibition of contracts designed to defraud or mislead; (2) the prohibition of various transactions, including spoofing; and (3) the prohibition of manipulation and the providing of false information.

- ***Digital commodity platforms—***The DCCPA would require that a person who acts as any category of digital commodity platform must be registered with the CFTC as that category of digital commodity platform.

Type of digital commodity platform	Description of platform
Digital commodity broker	A person that is engaged, as an identifiable business, in—(i) soliciting or accepting orders on behalf of another person for a digital commodity trade; (ii) accepting digital commodities from another person for the purpose of entering into digital commodity trades; (iii) arranging digital commodity trades on behalf of another person; or (iv) a similar activity, as determined by the Commission.
Digital commodity custodian	A person that, as an identifiable business, maintains possession, custody, or control over digital commodities on behalf of another person, but does not include insured depository institutions or insured credit unions.

Type of digital commodity platform	Description of platform
Digital commodity dealer	A person that—(i) has an identifiable business of dealing in a digital commodity as principal for its own account; (ii) makes a market in a digital commodity; (iii) holds itself out as a dealer in a digital commodity; (iv) has as an identifiable business of buying or selling digital commodities for conversion into other digital commodities, currency, or other consideration; (v) has as an identifiable business of accepting digital commodities from another person (referred to in this clause as a 'depositor') with an obligation to return the digital commodities, consideration linked to the digital commodities, or both to the depositor; or (vi) engages in a similar activity, as determined by the Commission. The term would not include a person solely because that person validates digital commodity transactions.
Digital commodity trading facility	A trading facility that facilitates the execution or trading of digital commodity trades between persons, but the term would not include a person solely because that person validates digital commodity transactions.

The DCCPA would grant the CFTC authority to permit a person to register in more than 1 category of digital commodity platform and to permit registered entities (e.g., swap dealers or futures commission merchants) to register in 1 or more categories of digital commodity platform. The CFTC also would have authority to grant exemptions to, or impose additional requirements on, persons with multiple registrations.

- ***Core principles—***Digital commodity platforms also must adhere to core principles applicable to all digital commodity platforms, while digital commodity trading facilities and digital commodity brokers and dealers must adhere to additional core principles specifically for those categories of digital commodity platforms.

  Among these core principles, for example, is the requirement that digital commodity trading facilities would, among other things, only be allowed to permit transactions in digital commodities that are not readily susceptible to manipulation. The phrase "not readily susceptible to manipulation" is used by the Stabenow-Boozman bill to describe what types of digital commodities may be traded but the bill does not contain the explicit definitional language of other bills that would provide a more direct means to assess an individual digital commodity's susceptibility to manipulation (the Stabenow-Boozman bill does, however, touch upon the subject matter in the context of the disapproval of a digital commodity trading facility's listing of a digital commodity or a digital commodity trading facility's rule or rule amendment).

  By comparison, both the Lummis-Gillibrand Responsible Financial Innovation Act and the Digital Commodity Exchange Act of 2022 similarly provide that a registered digital asset

exchange/digital commodity exchange may make available for trading only digital assets that are "not readily susceptible to manipulation." The Lummis-Gillibrand Responsible Financial Innovation Act and the Digital Commodity Exchange Act of 2022, however, would define "not readily susceptible to manipulation" to mean that a digital asset's transaction history cannot be fraudulently altered or its functionality or operation cannot be materially altered (technically, the bills define "not readily susceptible to manipulation" to bar trading of a digital commodity/digital asset if it is reasonably likely that the digital commodity's/digital asset's transaction history can be fraudulently altered or it is reasonably likely that the functionality or operation of the digital commodity/digital asset can be materially altered).

In making such determination, both the Lummis-Gillibrand Responsible Financial Innovation Act and the Digital Commodity Exchange Act of 2022 provide for consideration of similar factors: (1) the purpose and use of the digital asset; (2) the creation or release process of the digital asset; (3) the consensus mechanism of the digital asset; (4) the governance structure of the digital asset; (5) the participation and distribution of the digital asset; (6) the current and proposed functionality of the digital asset; (7) the legal classification of the digital asset; and (8) any other factor required by the CFTC.

- ***Registration fees—***The CFTC would be authorized to assess and collect fees to recover the costs of registering digital commodity platforms, conducting oversight of digital commodity trades and carrying out education and outreach activities regarding customers participating in digital commodity markets. In setting these fees, the CFTC would have to mull the volume of business of the digital commodity platform and the category of the digital commodity platform. Moreover, the CFTC could not require a digital commodity platform to directly collect from customers, and a digital commodity platform could not directly impose on customers, a per-transaction fee for each digital commodity trade to pay the fees the CFTC is authorized to collect from digital commodity platforms. The CFTC would have to adjust fee rates annually and account for the fees in its budget request to the president. The CFTC would be prohibited from using any fees collected for purposes that are not directly related to the registration of digital commodity platforms, oversight of digital commodity trades, and related education and outreach activities. In the event of a lapse of appropriations, the CFTC could continue to collect fees at the prior fiscal year's rate.

- ***Preemption of state laws—***The registration of a digital commodity platform, an associated person of a digital commodity broker, or an associated person of a digital commodity dealer would operate to preempt state law registration requirements under state laws addressing money transmission, virtual currency, and commodity brokers. However, state antifraud laws would be unaffected by the bill's preemption provision.

- ***Anti-money laundering—***The bill would direct the Treasury Department, in consultation with the CFTC, to issue regulations requiring CFTC-registered digital commodity platforms to submit reports of suspicious transactions under 31 U.S.C. §5318(g).

- ***Effective date—***The effective date or applicability of the bill's provisions would be the effective date of final CFTC rules implementing provisions requiring the registration of digital commodity platforms.

CFTC Chair Rostin Behnam testified before the Senate Agriculture Committee in early December 2022 and suggested that while the CFTC still seeks additional statutory authorities to regulate crypto markets, the DCCPA and related bills could be strengthened to better address a number of topics, including: (1) disclosure requirements; (2) conflicts of interest; (3) custodians; and (4) cybersecurity.

FTX bankruptcy. While the DCCPA appeared to be the main focus of lawmakers as the 2022 mid-term election hiatus approached, the intervening collapse of crypto trading firm FTX now raises a lot of questions (some new, some old) for regulators and lawmakers alike, regarding the broad concern about which government agency should take the lead in regulating crypto firms as well as the more specific concerns about exactly what went wrong at the fast-growing FTX and its U.S. and overseas trading operations and the role played by a related hedge fund.

The role of FTX's former CEO in promoting certain approaches to crypto legislation may also play a role in driving significant changes to the currently proposed crypto bills before any of them move beyond the committee stage. CFTC Chair Rostin Behnam testified before the Senate Agriculture Committee in early December 2022 and suggested that while the CFTC still seeks additional statutory authorities to regulate crypto markets, the DCCPA and related bills could be strengthened to better address a number of topics, including: (1) disclosure requirements; (2) conflicts of interest; (3) custodians; and (4) cybersecurity.

The several bills summarized above vary in their details, but most would give the CFTC explicit authority over crypto spot markets. Critics of these bills, however, have raised concerns that some of the bills may not do enough to prevent the CFTC from using any new authorities to take a closer look at other non-crypto markets or to impose fees on non-crypto firms. The most prominent of these bills do not explicitly purport to alter SEC authorities, but there are equally strong calls to preserve SEC authority as there are to ease SEC rules regarding tokens. The lame duck 117th Congress will have to address numerous funding bills by year end and, although it is remotely possible a re-vamped crypto bill cold move forward, it is also possible that a legislative solution for crypto markets may have to await the next Congress.

Senate Agriculture Committee Chair Stabenow has reiterated the need for federal oversight of crypto markets and for Congress to take action. "The Committee, remains committed to advancing the Digital Commodities Consumer Protection Act to bring necessary safeguards to the digital commodities market. I am working closely with Ranking Member Boozman, our Committee members, and financial regulators to finalize and prepare this legislation for a Committee vote," said Stabenow in a press release as the FTX collapse was unfolding. "Until legislation is enacted, I encourage all financial regulators to use their current authorities to the fullest extent to regulate and prosecute misconduct in these markets."

Likewise, Senate Agriculture Committee Ranking Member Boozman echoed Stabenow's comments by reiterating the need for legislation and urging the CFTC to use its existing antifraud authorities in the crypto space. "In light of these developments, we are taking a top-down look to ensure it [the DCCPA] establishes the necessary safeguards the digital commodities market desperately needs." Boozman added: "Chairwoman Stabenow and I remain committed to advancing a final version of the DCCPA that creates a regulatory framework that allows for international cooperation and gives consumers greater confidence that their investments are safe."

While both Stabenow and Boozman said they remain committed to finalizing the DCCPA, neither appeared to commit to making that happen in a particular time frame.

Senator Lummis, co-author of the Lummis-Gillibrand Responsible Financial Innovation Act, and House FSC Ranking Member Patrick McHenry, both called for clearer rules of the road for crypto

markets. Lummis, referring to FTX, said via press release that "[m]arket manipulation, lending activity, and whether customer funds and assets were appropriately safeguarded are just a few of the many issues my colleagues and I need to consider in the coming days." McHenry, also referring to FTX, said that "[t]he recent events show the necessity of Congressional action. It's imperative that Congress establish a framework that ensures Americans have adequate protections while also allowing innovation to thrive here in the U.S."

The House FSC is planning a December 2022 hearing on the collapse of FTX. A press release announcing the bipartisan hearing indicated that lawmakers may call a number of witnesses, including former FTX CEO Sam Bankman-Fried, representatives of FTX-related hedge fund Alameda Research, and other representatives of FTX and one-time FTX savior Binance.

Tax reporting patch. Senate Banking Committee Ranking Member Patrick Toomey (R-Pa), along with numerous bipartisan co-sponsors, introduced a patch for the cryptocurrency tax reporting provision contained in an infrastructure bill signed into law in 2021. The IRS had obtained John Doe summonses in recent years that allowed the agency to investigate whether persons using some of the major crypto exchanges were accurately reporting their taxes on crypto transactions. The IRS had repeatedly warned that many crypto traders were not paying their full taxes on such trades.

As a result, Congress added a provision to the Infrastructure Investment and Jobs Act to ensure that crypto exchanges report trading data to the IRS. A last-minute attempt by the Senate to amend the reporting provision before the infrastructure bill was voted on failed. Section 80603 of the Infrastructure Investment and Jobs Act applies to "any person who (for consideration) is responsible for regularly providing any service effectuating transfers of digital assets on behalf of another person."

The main concern of those seeking to patch the reporting provision is that the original provision that was enacted into law sweeps too broadly and may require reporting to the IRS by persons or entities that do not possess the type of information that would be required to be reported to the IRS. As a result, the legislative patch (S. 4751) would clarify that Section 80603 does not apply to any person solely engaged in the business of validating transactions or selling hardware or software that solely functions to permit persons to control private keys used to access digital assets.

Senator Ron Wyden (D-Ore) has introduced a similar bill (S. 3249) that is somewhat broader in scope than the Toomey bill. Accordingly, the Wyden bill would also apply to any person solely engaged in the business of "developing digital assets or their corresponding protocols for use by other persons, provided that such other persons are not customers of the person developing such assets or protocols."

Both the Toomey and Wyden bills would further clarify the status of broker-dealers under Section 80603. The reporting provision patch legislation has bipartisan support and could be attached to other must-pass legislation before the end of the 117th Congress.

Looking ahead

Now that Republicans have secured a slim majority in the House, it is expected that the House FSC will conduct more oversight hearings to question Biden Administration financial regulators. Appropriations bills originating in the House also may be expected to contain policy riders on political spending disclosure rules along with a potential new policy rider that would likely bar the SEC from finalizing ESG regulations.

With respect to blockchain regulation and legislation, confusion was initially the dominant theme as the potential regulatory fallout from crypto platform FTX's woes began to take shape. The SEC's Gary Gensler has emphasized the oversight of platforms but has also stated the SEC may need more legislative authorities to fully police crypto platforms. Lawmakers continue to work out the details of what, if any, new authorities Congress may grant the CFTC. Still, it is possible that the failure of FTX will help to focus Congressional efforts to establish at least a partial regulatory framework for blockchain in the next Congress.