

Global Digital Asset & Cryptocurrency Association

Advancing the Industry - Protecting Consumers - Promoting the Public Interest

global-dca.org

VIA ELECTRONIC SUBMISSION

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The Financial Stability Board
Centralbahnplatz 2
CH-4002 Basel
Switzerland
fsb@fsb.org

Re: Response to Request for Consultation on FSB's Proposed Framework for the International Regulation of Crypto-Asset Activities

The Global Digital Asset & Cryptocurrency Association (“GDCA”) welcomes the opportunity to comment on the Financial Stability Board’s (“FSB”) proposed framework for the international regulation of crypto-asset activities (the “Framework”).¹ GDCA applauds the process undertaken by the FSB to solicit public engagement on this important topic, and welcomes the opportunity to be part of the ongoing dialogue. When the FSB published the framework on October 11, 2022, it cited market events in the earlier part of the year that had exposed “a number of structural vulnerabilities” in crypto-asset markets and related businesses. Indeed, events like the collapse of the Terra/Luna project, the fall of Three Arrows Capital, and other events highlighted the need for significant standards setting, professionalization, regulation, and reform across the digital asset space. Within a month of the publication of the FSB’s framework, FTX collapsed. While still unfolding and while facts are still coming to light, the FTX collapse appears to be a perfect illustration of the need for a comprehensive, coordinated, international approach to the regulation of crypto-asset related activities within CeFi.

Long before the recent round of failures and market turmoil, GDCA has been calling for just such an approach. GDCA was formed in 2020 by a group of industry professionals who believed that in order to succeed long term, the crypto-assets industry needed strong self-regulation and a regulatory framework designed to build public trust, foster market integrity and maximize economic opportunity for all participants. The scholarship about the efficacy of self-regulatory organizations (“SROs”) to regulate financial markets is clear: Regulators in the U.S. and abroad can only do so much. For crypto-asset markets to reach their full potential, to appropriately monitor for and mitigate financial stability risks, and to ensure that users and financial markets as a whole are not adversely affected by crypto-asset markets, a strong SRO is needed. GDCA agrees with much of what the FSB included in its Framework. But the most glaring omission was a strong call

¹ <https://www.fsb.org/wp-content/uploads/P111022-3.pdf>.

for an SRO in the space.²

In light of the recent turmoil, where does GDCA believe the industry should go from here? GDCA has proposed a number of core principles,³ most of which are broadly consistent with the themes expounded in the Framework, which GDCA believes the industry should adopt through voluntary agreement or via regulation that is overseen by an industry SRO, and reinforced by attributes inherent to blockchain and distributed ledger technologies underpinning the virtual asset industry.

They are:

- **PROTECTION OF CUSTOMER ASSETS AND FULL DISCLOSURE:** Digital asset intermediaries must publicly disclose whether customer assets are segregated from the funds of their own proprietary businesses, where assets are held and how they are invested or leveraged, along with associated risks, so customers and counterparties can evaluate these conditions and make their own decisions. Plain disclosure about the use of customer funds must be included in terms and conditions or customer agreements. Transactions with affiliates must be conducted on standard commercial terms and conditions and must be disclosed to the public fully and in a timely manner. Disclosure obligations must correspond to customer type and sophistication.
- **STRONG GOVERNANCE AND SYSTEM OF CHECKS AND BALANCES:** Key functions must be designed so that no individual(s) has ultimate authority over, nor can unilaterally transfer customer funds. Such designs should appropriately reflect the risks and governance needs of the different services and products that are rendered. This tailored approach helps account for the differences between firms, such as those that directly custody customer funds and those that do not, and mitigates the risk of overregulating and hampering innovation. Independent audits should attest and demonstrate whether controls are sufficient and must be administered through a credentialed, trusted and reputable third-party. C-Suite executives must answer to a Board of Directors and be under heavy obligations to ensure that they are satisfactorily overseeing these activities and following established policies and internal controls.
- **LIQUIDITY RESERVES:** Sufficient liquidity and liquid reserves should be maintained. Firms must disclose whether proprietary reserves are put aside as a buffer to cover losses of customer funds.
- **ENTERPRISE RISK MANAGEMENT AND STRESS TESTING:** Firms must deploy sophisticated risk modeling techniques to stress test their financial wherewithal in the case of volatile market conditions, lack of liquidity and a once in a lifetime catastrophic event. Basic fundamental financial risk management procedures is the only way to ensure that a business can survive difficult economic conditions and stressed liquidity. Firms should also ensure comprehensive anti-money laundering and financial crimes compliance (AML/FCC) controls in keeping with US and global requirements and best practices.

² The only reference to an SRO appears in the Framework at page 58: “A few authorities noted self-regulation may support the regulation of crypto-assets, especially given the evolution of the market and technical expertise.”

³ https://global-dca.org/wp-content/uploads/2022/11/FINAL_GDCA-Open-Letter-to-Industry46.pdf.

- **PROPER BOOKS AND RECORDS:** Firms must create and maintain financial books and records so that audit firms or regulators, if applicable, may conduct effective audits and examinations.
- **INDEPENDENT AUDIT:** Above financial and compliance obligations must be subject to regulatory and financial audits. Audit and certification standards must be established as a way to demonstrate that firms are in compliance with the core principles.

GDCA hopes to continue to engage with the FSB, as well as policymakers in the U.S. abroad, to ensure that any regulation adopted is consistent with the above principles, and is properly designed to further the goals of fostering innovation, customer protection, and protecting financial stability.

I. Introducing GDCA

The Global Digital Asset and Cryptocurrency Association (“GDCA”) is a global, voluntary Self-Regulatory Association for the digital asset and cryptocurrency industry. It was established to guide the evolution of digital assets, cryptocurrencies, and the underlying blockchain technology within a regulatory framework designed to build public trust, foster market integrity and maximize economic opportunity for all participants. In defining the membership base, GDCA has sought to ensure representation from the many actors comprising and adjacent to the digital assets and cryptocurrency ecosystem. Our broad-based membership pulls from all facets of the ecosystem, and includes spot and derivative exchanges, proprietary trading firms, investors, asset managers, brokerage firms, custodians, decentralized technology organizations, banks, legal firms, audit firms, insurance professionals, academics, consultants, and others. GDCA is now made up of approximately 80 entities from around the world, most of which are based in the U.S.

The inclusion of all aspects of the digital asset ecosystem (direct firms as well as peripheral) is an intentional design choice as it allows for (a) building capacity amongst key peripheral industries necessary to the responsible elaboration of the industry (i.e., financial reporting, auditing, legal, and insurance). If these industries themselves are not well equipped and are not able to provide high quality services to the digital asset industry this provides potential for weakness in both a jurisdiction’s regulatory and self-regulatory model.

Certain requirements must also be met prior to admission as a GDCA member. These early requirements represent the first steps towards self-regulation and enforcement on behalf of the industry. Key components of the onboarding process include:

- Self-attestation of alignment with the GDCA’s Code of Conduct;
- Screening against US OFAC Sanctions (SDN and organizational listing);
- Disclosure of corporate governance structure (i.e., ownership);

- Organizational AML / KYC systems in place⁴

The requirement for formal onboarding and commitment prior to membership serves to both vet emerging members as well as to help shape their perspectives on self-regulation and orientation in economy and society. The onboarding process permits GDCA to gain insight into the candidate firm's leadership commitment, corporate governance and business profile. Additionally, formal onboarding provides an opportunity to raise awareness with the prospective firm on the value of self-regulation as a method of resilient business development.

To fulfill its mission, the GDCA devises standards and consensus-based solutions designed to address the major challenges facing the digital asset and cryptocurrency industry. GDCA operates a principle-based approach to self-regulation that is aligned with existing global standards, including the ISO standards framework and the Financial Action Task Force and the Rulebook as related to global AML/FCC.⁵ Standards and guidance are not positioned as 'requirements' that must be followed, but rather as the 'key steps in a pathway' for ensuring the longevity and global competitiveness of a member firm's business. Compliance and alignment with standards and guidance also contribute to the health of the association 'community' and overarching industry development. Likewise, we collaborate with stakeholders around the world, industry leaders and policymakers to support the growth of the global digital economy, including to:

- Advocate for a regulatory environment that facilitates innovation and protects consumers, stakeholders, and the broader public interest;
- Provide education, training, certification, and other resources to build human and technical capacity;
- Provide thought leadership and facilitate industry engagement; and
- Oversee our members through a self-regulatory mechanism that is guided by principles of accountability, integrity, and transparency to promote the highest professional and ethical standards.

II. Specific Responses

Recommendation 1: Regulatory Powers and Tools

The FSB recommends that authorities in each jurisdiction should “have the appropriate powers and tools, and adequate resources to regulate, supervise, and oversee crypto-asset activities and markets, including cryptoasset issuers and service providers.” The GDCA broadly agrees with this

⁴ For relevant companies - self-attestation of existence and alignment with GDCA AML / KYC requirements and completion and signature of checklist for those entities which handle crypto is needed.

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<https://docs.google.com/document/d/1SswHBZ1pwuIUcePeFe8czOoAOaHE78ij4okXuQq5OW0/edit#heading=h.4ohf25mn2gie>

recommendation. In order for cryptoasset markets to thrive, and in order for the transformative underlying technologies to continue to develop, there should be a clear match between the “laws on the books” in any jurisdiction, and the enforcement of those laws, and as such it is important for regulators to be appropriately resourced towards accomplishing their remits.

By contrast, in the U.S. for example, the SEC’s enforcement activities regarding cryptoassets have been “scattershot.” Market participants are led to believe, based on statements from SEC Chair Gensler, that nearly *every* cryptoasset trading in centralized exchanges and circulating among U.S. participants, is an illegal unregistered security. Yet, the SEC has brought enforcement actions for failure to register as a security against a small fraction of those projects. Millions of Americans are using products and services that the SEC appears to believe are illegally administered. Whether this is the result of a flawed and overinclusive interpretation of the law by the SEC, or whether this is the result of a lack of enforcement or rulemaking resources at the SEC is beside the point. Either way, there should not be a mismatch between a regulator’s belief about what the law requires, and what is happening in the markets. Such a mismatch creates confusion and uncertainty in the market, and hampers innovation and investment.

This does not mean, however, that the highest level of regulation is appropriate or required for all digital assets-related activities. In the U.S., for example, banks have the highest level of regulation, with multiple prudential regulators overseeing every aspect of a bank’s activity. Most activities regarding cryptoassets do not require this level of oversight. Regulators in the U.S. and abroad should not automatically default to the highest level of regulation simply because their regulators already possess the structures and frameworks appropriate to banks and similar institutions.

Likewise, given the expansiveness of the digital asset industry, its speed of development, and its coverage of security tokens, payment tokens, stablecoins and more, government regulators would face difficulty in staying abreast of all industry developments and will lag in the development and adoption of proper tools to enact oversight. For these reasons, it is recommended that voluntary and formal self-regulation efforts continue to design and build to complement government regulatory efforts as well as to steward responsible development of the industry.

Recommendation 2: General Regulatory Framework

The FSB recommends that national authorities should “apply effective regulation, supervision, and oversight to cryptoasset activities and markets – including crypto-asset issuers and service providers – proportionate to the financial stability risk they pose, or potentially pose, in line with the principle ‘same activity, same risk, same regulation.’”

GDCA has two principal concerns with this recommendation and the FSB’s discussion of it. First, as noted above, the mantra “same activity, same risk, same regulation” should not be interpreted

as shorthand for: “authorities should regulate all crypto-asset related activities like you would regulate a bank.” There are a multitude of reasons as to why all crypto-assets should not be treated the same as other traditional regulated products in banking specifically. However, if such guidance reflects the diversity of financial services activities beyond traditional banking that do necessitate—and currently have in place—authorities for appropriate oversight (e.g. exchanges, securities, trading, etc.) such regulatory approaches would be more relevant and apply to digital assets in the same way they do for traditional services. Importantly, as stated above, additionally, consideration should be given to the underlying attributes of technologies that facilitate digital assets in their enablement of essential risk, security and compliance protocols required.

As one example, GDCA was pleased that the Framework included an acknowledgment of the growing importance of DeFi protocols. Because of the unique characteristics of DeFi, we believe DeFi-related activity should not be treated the same as activities on a centralized, custodial venue. Arguably, a decentralized exchange offers a similar function to that of a centralized exchange: both are venues where users can trade crypto assets against each other. But these decentralized, blockchain-based protocols present vastly different risks as compared to the traditional models regulators are familiar with and call for a different regulatory scheme.

With a DeFi protocol, users (typically) custody their own funds, and the risk of the exchange absconding with customer money is lessened. As such, a centralized exchange (like FTX) presents a host of risks and potential issues that a decentralized exchange or other protocol does not. (DeFi has its own risks, including hacks, technological failure, and others) that are less salient for centralized venues. Put another way: “Traditional financial regulation largely is based on pursuing policy objectives via the regulation of financial intermediaries that typically custody assets or clear transactions. Because the decentralized finance ecosystem establishes trust via rules-based, encoded protocols maintained by numerous independent parties around the world instead of intermediating financial institutions, this traditional regulatory approach does not transpose onto, or account for the features of, the DeFi ecosystem.”⁶

GDCA believes that regulation should be tailored not only to the activities and practices being conducted and associated attendant risks, but the essential qualities of the underlying technology that address these risks should also be considered. Regulators in the U.S., Europe, and elsewhere are studying DeFi and making determinations about what kinds of regulations are needed there. Governments should continue this process and not rush to impose inappropriate regulatory frameworks on something they are only beginning to understand and that is developing on an ongoing basis.

Likewise, adoption of crypto assets and its use cases, in some cases, remains speculative, while others are more established and well understood. While consumers may purchase crypto assets

⁶ [Cite- DeFi Alliance Principles]

that share similar activity and characteristics to traditional financial instruments, their usage may ultimately vary drastically in the long-run or in light of future competition (Including from TradFi), and even external macroeconomic and geopolitical events. As such, the mantra “same activity, same risk, same regulation” may not be fitting if limited to bank-centric activities and may present an overgeneralized approach to regulation that in and of itself distorts consumer speculation and adoption trends. In other words, the associated activities and attendant regulatory other measures should be commensurate to address the actual risks posed by those activities, as we see with regulations focused across a diverse array of financial services such as exchange activities, securities, customer versus principal trading, investing, payments, and a myriad of other financial activities.

Second, GDCA is concerned that the recommendation does not adequately account for giving the industry the space it needs for innovation to occur and for blockchain technology to fully develop and for its various use cases to be explored. The Framework references “past approaches to technological change.” Authorities in the U.S. and abroad did not seek to implement “comprehensive regulatory rules and policies” with respect to the Internet in its early years, which arguably is a reason why the technology has developed to the state it is in today.

GDCA believes that an appropriate balance between regulation and innovation is eminently achievable. The key to such a result is to narrowly identify those products and activities that fall within regulatory bounds, and clearly exclude the rest. As such, GDCA has long called for a clear and complete **digital asset taxonomy** that, for example, would characterize digital assets into token types. GDCA agrees: if a digital asset is truly a “security token,” as defined by a clear and objective test not premised only on subjective interpretations and Supreme Court cases from the 1940s (i.e., the famous *Howey* case), it should be treated like a security and subject to the same panoply of laws that a non-tokenized security is subject to. But if a protocol or asset does not fall within a specific proscribed category it should be free from regulation that would otherwise constrain its true intent or be misguided or implemented.

Recommendation 3: Cross-border cooperation, coordination and information sharing

GDCA strongly agrees with and supports the FSB’s third recommendation: that “Authorities should cooperate and coordinate with each other, both domestically and internationally, to foster efficient and effective communication, information sharing and consultation in order to support each other as appropriate in fulfilling their respective mandates and to encourage consistency of regulatory and supervisory outcomes.” Though, the evolving nature of digital assets and its innate global reach creates barriers to ensuring all global jurisdictions - including emerging markets - have the appropriate capacity and resources needed to coordinate and communicate at both the local and international level.

Perhaps the most challenging problem facing the digital assets industry today is the fact that while regulation is national, blockchain—indeed web-based applications more broadly— is global. Transactions, value, and information all move seamlessly across jurisdictions, in ignorance of national borders. Yet, national authorities have dramatically inconsistent approaches to regulation of the same assets or activity. This leads to some products and services being unavailable in certain jurisdictions, regulatory arbitrage, or users and businesses simply ignoring regulators.

As such, an SRO that takes a principles-based approach to regulation that focuses on activities and practices is best suited to both maximize international communication and cooperation. An SRO can facilitate international and intra-agency communication by evaluating, on an ongoing basis, its MoUs and relationships with relevant local and international agencies to ensure the provision of information. Further, around the world, standards and guidance are set using a principles-based approach. Given the desire to not only set legal and regulatory requirements for the U.S., but also to act as a replicative model and influence standards setting around the world – a principles based approach lends itself more naturally to global acceptance, adoption and replication. This approach, may also help to minimize the ability of firms off-shoring to gain advantage from jurisdictional legal and regulatory arbitrage. Further, we believe a sector-driven approach—in particular through an SRO framework that represents and whose membership includes companies across multiple regulatory and jurisdictional frameworks, couple with proactive governance mechanisms and policy frameworks—is the most comprehensive and practical manner in which to enable consistency of approach and adherence to common standards of self-governance.

Cross-border cooperation and information sharing will, over time, support a harmonization and consistency of regulatory approaches. Today, national regulators lack clear mechanisms to engage in cooperation and information sharing. GDCA would support the adoption and creation of multiple tools and vectors to increase this beneficial activity. Such tools will serve as the foundation for an effective international approach to regulation and can also serve to address coordination pain-points across the industry, including the need for more cooperation in conducting criminal investigations.

Recommendation 4: Governance

The FSB recommends that authorities should “require that crypto-asset issuers and service providers have in place and disclose a comprehensive governance framework. The governance framework should be proportionate to their risk, size, complexity and systemic importance, and to the financial stability risk that may be posed by activity or market in which the crypto-asset issuers and service providers are participating. It should provide for clear and direct lines of responsibility and accountability for the functions and activities they are conducting.”

GDCA, overall, agrees with and supports the FSB's fourth recommendation. As was noted above, there needs to be clear standards and requirements that reflect and are in alignment with the specific risk profiles, characteristics, and significance of the involved parties. For example, there are crypto companies that are heavily relied upon by both institutional and retail customers, such as companies that render crypto custodial services. The significant role that these companies play for the industry may position them as single points of failure. In such instances, an event that poses any risks to the operation and feasibility of the company may have an outsized negative downstream impact on its dependencies and a cascading impact across the crypto industry and potentially those industries adjacent to it.

As such, GDCA believes that as a *first* step towards developing appropriate governance frameworks, there needs to be an understanding of which companies, products and services are core components of the cryptocurrency industry. This can be aided through the development of robust risks and financial metrics that, among many things, adequately capture the potential impact to secondary and tertiary dependencies. By taking this approach, a governance framework and its standards and requirements can be appropriately developed and assigned based on the degree to which the party at hand is core to the industry, and driven to the specific activities and practices undertaken by market participants and those that warrant specific regulatory requirements. In continuing with the example above, firms that custody assets for their customers would, presumably, be held to a stricter set of standards and requirements than those companies that do not. It is likely that comprehensive governance frameworks will ultimately reflect the degree to which a company serves as an intermediary between their customers and the assets they manage for their customers.

Recommendation 5: Risk Management

GDCA agrees that over time, regulation should require comprehensive enterprise risk management frameworks and controls. GDCA agrees, however, that any required frameworks should be “proportionate to the risk, size, complexity, and systemic importance, and to the financial stability risk that may be posed by the activity or market in which they are participating.”

GDCA has urged its members and firms in the industry to voluntarily adopt sound risk management practices, and is collaborating with thought leaders in the industry on standards and best practices. GDCA believes that voluntary adoption is the best way for the industry to coalesce around specific risk management practices that are purpose fit for the industry, best protect customers, and limit contagion risk and financial instability.

As the FSB recognizes, before governments require specific risk management practices, like specific policies, procedures, outside auditors, etc., the interconnectedness of crypto to the wider financial system and risks to global financial instability should be considered. Governments should

not impose too much too early in the way of comprehensive risk management requirements on our growing industry, at the risk of squelching innovation and limiting the benefits that blockchain technology offers. Today, as recognized in the Framework, crypto-asset markets are not yet deeply interconnected with the wider financial system. As Treasury Secretary Yellen recently recognized, FTX was “not deeply integrated with our banking sector and, at this point, [its collapse] doesn’t pose broader threats to financial stability.” Until such time as interconnectedness increases, governments should move cautiously and deliberately, in favor of 1) leveraging the tools inherent to the technologies and operating protocols underpinning virtual asset activities that ‘build in’ compliance, transparency, governance and risk management controls and 2) proactive efforts by industry to drive self-governance that serve to complement the intents of regulation by effectively empowering the sector to ensure governance in a cross-border services environment.

Recommendation 6: Data collection, recording and reporting

The FSB recommends that “authorities, as appropriate, should require that crypto-asset issuers and service providers to have in place robust frameworks for collecting, storing, safeguarding, and the timely and accurate reporting of data, including relevant policies, procedures and infrastructures needed, in each case proportionate to their risk, size, complexity and systemic importance. Authorities should have access to the data as necessary and appropriate to fulfill their regulatory, supervisory and oversight mandates.”

GDCA generally agrees with the perceived intention and reasoning behind this recommendation. Though, it is likely that much of the data collection, at least as far as it pertains to company governance and processes, will be simultaneously addressed through the other FSB recommendations.

However, as a note, GDCA also wants to emphasize that regulation that pertains to data collection, recording and reporting may already exist, and in fact do exist for all regulated entities—bank and nonbank alike—across both prudential and financial crimes compliance domains. Before adopting new requirements, GDCA recommends that any such existing regulation be referenced and analyzed for its applicability as it pertains to the crypto industry. In the event that existing regulation is applicable, efforts should focus on harmonizing and extending its use case to crypto prior to pursuing further regulation.

Special consideration should also be taken for instances in which existing regulation may be overreaching and not applicable to crypto, or as stated earlier, where the attributes of virtual asset networks, technologies and decentralized applications have built in risk, governance and security capabilities. Likewise, in instances where new regulation is proposed, its necessity and feasibility should be thoroughly analyzed and vetted not only at the company level but also at the protocol

(blockchain) level - which may rely on a structural software and coding design that can ultimately render such proposed regulation obsolete or inapplicable.

Recommendation 7: Disclosures

GDCA agrees that certain participants in the digital assets industry should be required to make clear, specific, and comprehensive disclosures of their products, services, and operations. However, consistent with the discussion above concerning, some protocols and products are by their very nature fully transparent, and requiring teams to make formulaic or boilerplate disclosures would not materially aid in protecting or informing consumers. Fully transparent, decentralized protocols that operate without a core team do not carry the same risks of self-dealing and informational asymmetries that a product sold by a closely-held corporation might carry.

Recommendation 8: Addressing financial stability risks arising from interconnections and interdependencies

The FSB recommends that authorities should “identify and monitor the relevant interconnections, both within the crypto-asset ecosystem, as well as between the crypto-asset ecosystem and the wider financial system. Authorities should address financial stability risks that arise from these interconnections and interdependencies.”

GDCA strongly agrees with and supports the FSB’s eight recommendations. Though, it believes that addressing the underlying risks and concerns can be simultaneously achieved through the execution and further development of GDCA’s previous comments regarding FSB’s fourth recommendation.

As was noted above, certain companies, products and services may serve as single points of failure for the industry. In such instances, an event that poses any risks to the operation and feasibility of the company may have an outsized negative downstream impact on its dependencies and a cascading impact across the crypto industry and potentially those industries adjacent to it. As such, there needs to be an understanding of which companies, products and services are core components of the crypto industry. This can be aided through the development of robust risks and financial metrics that, among many things, adequately capture the potential impact to secondary and tertiary dependencies.

In the U.S., Section 804 of the Dodd–Frank Wall Street Reform and Consumer Protection Act (DFA) provides the Financial Stability Oversight Council (FSOC) the authority to identify and classify traditional financial market utilities as systemically important. Such designation is derived from the forecasted financial impact that can result from a potential failure or disruption of said utility. In such instances, these entities are classified as Systemically Important Financial Market

Utilities (SIFMUs). SIFMUs are then subject to further regulatory oversight, particularly as it pertains to risk standards.

It is highly unlikely that similar financial risks in the crypto industry currently exist, but it may very well arise in the future. Authorities stand to benefit from exploring the applicability of similar SIFMU designation to address any such future risks in crypto. Though, this should be in line and consistent with the unique characteristics of the institutions across the crypto industry.

Recommendation 9: Comprehensive regulation of crypto-asset service providers with multiple functions

GDCA agrees that over time, authorities “should ensure that crypto-asset service providers that combine multiple functions and activities, for example crypto-asset trading platforms, are subject to appropriate regulation, supervision and oversight that comprehensively address the risks associated with individual functions and the risks arising from the combination of functions, including requirements regarding separation of certain functions and activities, as appropriate.”

The recent fallout from the event(s) involving the commingling of user funds between FTX and Alameda Research is a primary example for the need to adopt such comprehensive regulation. Both companies technically, or at least on paper, functioned and operated independently. However, decision making heavily involved individual(s) from both companies and functioned similarly to having vastly different business units under a single unregulated entity. While investigations into the fallout of both companies are still ongoing, the outcome highlights the need for proper regulation in instances in which two seemingly “separate” business activities are taking place under the supervision of a single entity or individuals, and in instances where conflicts of interest may exist.

Though, GDCA believes that such regulation should not come at the expense of market competition and technological innovation. Improperly implementing this type of regulation may hamper the ability for incumbent crypto and non-crypto companies to expand their service offerings. It may also stand to create preemptive regulatory requirements that serve as barriers that impede new companies from entering the market entirely. As such, an appropriate balance is needed between having comprehensive regulation and the timing and appropriateness of its implementation.

GDCA’s Chief Recommendation: An Empowered, International SRO

As noted above, the most glaring omission from the FSB’s Framework is the failure to appropriately recognize the important role of industry self-governance to financial stability. We believe regulators should work together on frameworks for the eventual establishment of a cross-

cutting self-regulatory organization (SRO) that would interface with and be overseen by national regulators.

Self-regulation has long been a hallmark of U.S. financial markets. Indeed, in 1859, the Governor of Illinois signed legislation granting the Chicago Board of Trade self-regulatory authority over its members, marking the first effort by the government to formalize self-regulation in the derivatives markets.⁷ Today, SROs play a critical role in regulating U.S. financial markets. Scholars, regulators, and market participants have come to understand and appreciate the benefits of a strong SRO overseen by government regulators, chiefly in the person of the National Futures Association (NFA) for the futures industry and the Financial Industry Regulatory Authority (FINRA) for the securities industry.⁸ The U.S. model for industry self-governance has been exported around the world, and is now recognized in the International Organization for Securities Commission (IOSCO) Model for Effective Self-Regulation⁹ as well as the IOSCO Objectives and Principles of Securities Regulation.¹⁰

In order to effectively regulate the emerging digital asset industry, regulators must have up-to-date expertise and understanding as well as staff with close proximity to the industry as the pace of evolution and change is unparalleled. Further, the regulating entity must have a high degree of responsiveness and ability to flexibly and nimbly respond to changes in the global marketplace as new products, services and technologies are evolving daily. Finally, given the inherent cross-border nature of the digital asset industry, the regulating entity needs to be intrinsically global - able to engage and cooperate with global jurisdictional and international peers rapidly, efficiently, and effectively. All of these challenges clearly point in the direction of an SRO, which could work closely with and inform government, serving as the “bridge” between a fast-evolving industry and regulators seeking to protect the public interest.

Benefits of industry self-regulation in the form of an SRO include: efficiency and cost savings to taxpayers with a self-funded private organization, the development of knowledge and expertise, speed and flexibility, trust and participation by market participants, swifter enforcement, and supporting responsible innovation.

⁷ See Heath P. Tarbert, *Self-Regulation in the Derivatives Markets: Stability Through Collaboration*, Northwestern University School of Law, Journal of International Law and Business (March 1, 2021), available at <https://jilb.law.northwestern.edu/issues/self-regulation-in-the-derivatives-markets-stability-through-collaboration/> (hereinafter “Tarbert”).

⁸ See generally Saule T. Omarova, Rethinking the Future of Self-Regulation in the Financial Industry, 35 Brook. J. Int’l L. 665, 695 (2010). (arguing that SROs are in the best position to address the two principal regulatory challenges currently facing governments around the globe: the increasing complexity and global nature of financial transactions and instruments).

⁹ Report of the SRO Consultative Committee of the International Organization of Securities Commissions. Model for Effective Self-Regulation. (2000).

¹⁰ IOSCO Objectives and Principles of Securities Regulation. Principles for Self-Regulation. 3,5 (2017). <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD561.pdf>.

Of course, some of the most effective industry self-governance is not government sponsored. The cryptocurrency industry has made strides in recent years towards self governance. For example, GDCA today is seeking to become an SRO for the Digital Assets Industry. In the design of its governance structure and function, the GDCA has sought to model itself in alignment with IOSCO principles. Today, all full members must sign on to a Code of Conduct prior to joining the GDCA membership that requires, among other things, ethics and conflict-of-interest policies and a commitment to good business practices and compliance.¹¹ Over time, GDCA seeks to evolve into a more empowered and comprehensive organization that promulgates rules and practices for its members to mutually agree to.

ADDITIONAL CONSIDERATIONS

Equitable Application of Global Requirements and Regulations

Given the diversity of country contexts (i.e., size, level of development, capacity) throughout the world, it will be important for any forthcoming global requirements and regulations around digital assets to take into consideration the level of development of the jurisdiction. As opposed to advancing an equal application of requirements across all jurisdictions, there should be reflection and consideration of how and in what manner equitable application of requirements may be achieved. This should be balanced in regards to risk and the need for effective consumer protection, but at the same time should be tailored to recognize the varying needs for economic growth, domestic industry development, and job creation. In particular, legal and regulatory requirements should be balanced to ensure emerging countries should not be overly burdened as they seek to grow and develop their economies. For such countries - especially those in the Global South - strong economic growth, domestic industry development and job creation will not only have implications for national stability and progress but for broader prosperity.

Nurturing Small and Medium Enterprise (SME) Growth

Any forthcoming global requirements and regulations should nurture the role held by Small- and Medium Enterprises (SMEs) in economy and society. According to the World Bank, SMEs play a major role in most economies, particularly in developing countries.¹² SMEs account for the majority of businesses worldwide and are important contributors to job creation and global economic development. They represent about 90% of businesses and more than 50% of employment worldwide. Formal SMEs contribute up to 40% of national income (GDP) in emerging economies. These numbers are significantly higher when informal SMEs are included. According to World Bank estimates, 600 million jobs will be needed by 2030 to absorb the growing global workforce, which makes SME development a high priority for many governments

¹¹ <https://global-dca.org/code-of-conduct/>

¹² <https://www.worldbank.org/en/topic/sme/finance>

around the world. In emerging markets, most formal jobs are generated by SMEs, which create 7 out of 10 jobs. Further, as noted by the World Bank's Siddhartha Raja and Luc Christiaensen, digital technology is transforming the organization and location of production, and thus the future of work. Technology creates opportunities (leapfrogging), to generate jobs, increase earnings and inclusion within a given country. To take maximum advantage and counter the threat of rising global inequality, their research suggests that developing countries need to: (1) address bottlenecks in technology access; (2) invest in skills and (3) create an enabling environment¹³. In regards to this last recommendation, the Global DCA recommends approaching global requirements or recommendations around digital assets in a manner which nurtures SME development in the digital asset industry with a view towards economic growth and development. Regulation and legislation should be right-sized to ensure digital asset industry SMEs are not overly burdened, can develop and contribute to job creation and economic growth and can support resilient and globally competitive industry evolution.

Supporting Financial Inclusion and Access to Finance for Traditionally Unbanked / Underbanked Populations

Globally, there are an estimated 3.5 billion people who are excluded (unbanked or underbanked) from the traditional financial system.¹⁴ The reasons behind financial exclusion vary, but these include insufficient funds to operate an account (e.g., minimum balance requirements for traditional banking accounts), religious reasons, costs of financial services relative to income (excessive fees, overage charges, etc.), physical proximity to traditional banking institutions, as well as a lack of necessary personal ID (passport, driver's license). Although increasing financial sector participation and access to finance requires a multi-pronged approach (including education and community engagement), technological innovations and the opportunities presented by digital assets to bridge this gap should not be overlooked—in fact we would strongly encourage that regulatory efforts. When reflecting on global requirements and regulations, the FSB should seek to foster balanced regulations which advance digital asset development and support consumers' access to financial products and services in innovative ways through new applications and approaches.

GDCA appreciates the opportunity to comment on this important proposal.

Sincerely,

Michael D. Frisch

¹³ Raja, Siddhartha; Christiaensen, Luc. 2017. The Future of Work Requires More, Not Less Technology in Developing Countries. Jobs Notes; No. 2. World Bank, Washington, DC. © World Bank. <https://openknowledge.worldbank.org/handle/10986/27934> License: CC BY 3.0 IGO

¹⁴ Deloitte. "Can Blockchain Accelerate Financial Inclusion Globally?" <https://www2.deloitte.com/content/dam/Deloitte/lu/Documents/technology/lu-blockchain-accelerate-financial-inclusion.pdf>

Michael D. Frisch
Chairman, Public Policy and Regulation Committee,
Global Digital Asset and Cryptocurrency Association

Gabriella Kusz
CEO,
Global Digital Asset and Cryptocurrency Association

Antonio Flores*
Project Manager – Fellow,
Global Digital Asset and Cryptocurrency Association

Amit Sharma
Founder and CEO,
FinClusive Capital

Nina Kaplan,
Chair,
New Jersey Digital Assets Working Group

Andrew Gunderman,
Co-Founder,
Coherence Finance Inc.

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