

The background of the cover is a collage of financial and global imagery. It includes several overlapping line charts and candlestick patterns in shades of blue and white. A green diagonal line runs from the top left towards the bottom right, separating the Cboe logo area from the main title area. In the bottom left corner, there is a faint, dotted map of the world. The overall color palette is dominated by blue and white, with green accents.

A Path Forward for Digital Asset Trading Regulation

May 2022

Cboe Global Markets (Cboe) has been at the forefront of financial market innovation since its inception in 1973.¹ We believe that market innovation best serves investors when accompanied by clear, effective, and efficient regulation. As it relates to the digital asset industry, technological innovation will continue to play an important role in accelerating solution generation; however, regulatory progress is equally critical to the continued maturation of the ecosystem.

The core of the U.S. financial regulatory system has been built through a process of thoughtful, iterative improvements that have long-supported investor protection, transparency, and market resiliency. These are hallmarks of a fair and honest system and are at the very heart and

strength of the U.S. financial system. If we are thoughtful, pragmatic, and solution-driven our regulatory framework can be a key strength of the digital asset ecosystem.

What follows are actionable recommendations that are achievable in the near-term. These recommendations, if adopted, will help serve as an important on-ramp or entry-point for existing and future digital asset entrepreneurs while unlocking the promise of regulated trading venues to drive innovation, promote transparency, and protect investors.

Cboe Digital

Cboe has long been committed to investor protection, transparency, and fair and orderly markets. Cboe's acquisition of ErisX (soon to be rebranded as Cboe Digital) is an extension of these values. ErisX was designed and built with regulatory compliance and operational integrity at the fore. ErisX today operates a trusted and transparent cash market that operates in 51 U.S. jurisdictions, a regulated futures exchange (DCM) and a regulated clearing house (DCO). Together, as Cboe Digital, we will pursue a vision for the digital asset ecosystem that promotes our shared values.

¹ Cboe is one of the world's largest exchange operators and is a leading provider of cutting-edge trading and investment solutions. Cboe operates regulated venues in the US, Canada, EU, UK, Japan, and Australia and offers a diverse range of products, including, equities; options; futures; FX; ETFs/ETNs; market data solutions; and investor education. As the creator of listed options and nearly every options product innovation of note (equity options; index options; LEAPs; FLEX options, and Nanos), Cboe sets the standard for options and volatility trading through product innovation, trading technology, and investor education. Cboe's S&P 500 Index Options (SPX) ADV of 1.4 million contracts (2021) represents over half a trillion dollars in notional risk transfer every day.

Summary

In spite of ongoing efforts to clarify how the current regulatory framework is to be applied to the digital asset ecosystem, uncertainty remains – particularly with respect to what is or is not a security and the obligations that flow from this determination. This continued uncertainty has ongoing implications for investors and hinders innovation. Cboe understands that this definitional clarity may not be forthcoming in the immediate future; regardless, the recommendations below represent improvements that are within reach for policymakers. Cboe's aim is to reduce regulatory uncertainty, increase transparency and promote investor protection while providing entrepreneurs a clear path to innovate. Cboe recommends policymakers take concrete steps to support these objectives by pursuing the below initiatives, which are actionable in the near-term and would drive further and positive maturation of the digital asset ecosystem:

CFTC Oversight of Spot Trading of Digital Asset Commodities

We recommend Congress enact legislation that provides the Commodity Futures Trading Commission (CFTC) with direct oversight of the spot trading market for digital asset commodities.

Extending the CFTC's general anti-fraud and manipulation enforcement authority to include direct oversight of digital asset commodity spot trading would enhance investor protection as digital asset commodities represent the largest market capitalization of all digital assets. This would also complement the CFTC's existing oversight authority of digital asset commodity derivatives.

Adaptive Alternative Trading System (ATS) Model

We recommend the Securities and Exchange Commission (SEC) take action to allow an SEC-registered ATS to offer spot trading of digital assets including those that may not be securities.

This would serve broader policy objectives by incentivizing unregulated spot trading venues to come into the regulatory fold; counter the ongoing definitional uncertainty with respect to what is or is not a security; and, with adequate cooperation arrangements between the SEC and CFTC, enhance regulatory oversight of digital

assets while improving transparency to the benefit of investors. To streamline efficiency, a platform should be allowed to dually-register as an SEC-licensed ATS as well as a CFTC-licensed venue. Concomitant enhancements (via SEC rulemaking or relief) are also advisable to allow broker-dealers to efficiently and effectively hold digital assets and fully support investors.

Spot Bitcoin ETFs

We recommend the SEC approve spot Bitcoin ETFs to harness legacy national securities exchanges to promote transparency and investor protection.

At present, investors seeking to gain exposure to digital assets such as Bitcoin are largely doing so via spot Bitcoin or indirectly via non U.S. exchange traded products, high premium OTC Bitcoin funds, Bitcoin futures held in ETFs, or public companies serving as a proxy for direct Bitcoin exposure. This current framework hinders traditional, regulated equity exchanges in the U.S. from effectively serving digital asset investors. Approving a U.S. spot Bitcoin ETF that directly holds Bitcoin would allow investors to gain Bitcoin exposure via the most regulated, transparent, and mature equity market in the world. This would serve as an important test case in approving subsequent ETF applications offering exposure to digital assets beyond Bitcoin.

Core Beliefs

Intelligent regulation is paramount and a key component of a properly functioning market.

Prioritizing investor protection and investor education breeds confidence in markets, without which, there can be no capital formation process.

Intelligent regulation benefits investors. Markets benefit from rules that ensure investors are treated fairly while allowing entrepreneurs to develop creative solutions to meet investor needs. While there is no panacea, the most beneficial regulations are flexible in approach but clear in application. They provide necessary guardrails by which we can safely interact with new and novel systems.

Intelligent regulation is efficient and targeted. It is necessary for regulation to strike an appropriate balance between supporting innovation and competition, which directly benefits investors, and ensuring there is sufficient investor protection and transparency. Robust, yet flexible, principle-based regulatory frameworks can help markets flourish.

Targeted regulatory enhancements are helpful. Meaningful regulatory evolution is natural and in large part achievable through existing authorities. We strongly believe that targeted, interim steps can be taken to increase regulatory certainty, transparency, and investor protection to the benefit of all investors.

Transparent, regulated venues are a critical part of any sound market.

Regulated venues that match buyer and seller in a transparent, fair, and orderly manner better serve investors by upholding the integrity of markets and breeding investor confidence.

Value-add intermediation remains a vital component of the digital asset marketplace.

Contrary to claims that the promise of digital assets lies in absolute disintermediation, thoughtful, value-add intermediation is more important than ever. From KYC/AML protections to tax reporting services and robust custody arrangements, the digital asset investor needs tools that solve real problems in the ecosystem. Many of these tools will be offered by intermediated experts that provide real-world solutions and real value to investors.

Inter-regulator cooperation is critical. In addition to ensuring regulators maintain an ongoing dialogue with market participants, it is of upmost importance that there is cooperation and clear jurisdictional lines amongst and between regulators. Jurisdictional ambiguities are a hinderance to the development of new products, new markets, and innovation – and must be avoided.

Current Regulatory Environment

Digital assets and blockchain technology have advanced significantly in recent years, driving accelerated digital asset adoption and significant investment. While digital assets remain a small fraction of the market capitalization of the U.S. stock market, the tremendous growth of the digital asset ecosystem demonstrates that digital assets and blockchain technology are an impressive technological innovation that the U.S. should embrace.

Authorities have made meaningful strides to provide additional clarity on how current rules and regulations govern our interaction with these new and novel digital asset systems. The U.S. Office of the Comptroller of the Currency (the OCC) has made clear that federally chartered banks are able to provide custody services for cryptocurrencies and other digital assets. The Internal Revenue Service has issued guidance explaining how particular aspects of the tax code apply to certain digital assets. These are but a few examples of important steps that have been taken to further our understanding and help the digital asset industry navigate the *current* regulatory framework.

Much work has also been done to consider the best, *future* regulatory framework. President Biden issued an Executive Order on Ensuring Responsible Development of Digital Assets.² The Presidents Working Group on Financial Markets (PWG), FDIC, and OCC also issued a

Report on Stablecoins.³ The U.S. Treasury Financial Crimes Enforcement Network (FinCEN) has released extensive guidance regarding the applicability of the Bank Secrecy Act (BSA). The Board of Governors of the Federal Reserve System published a report on central bank digital currencies.⁴ Policymakers are holding important hearings and asking pertinent questions about the impacts of this technology. Legislators have taken steps to propose legislation to bring additional regulatory clarity, and to close gaps in our current framework.

However, despite these efforts, uncertainty remains. The application of existing guidance on what is or is not a security is not easily applied to the nuances of the digital asset ecosystem, resulting in a state of regulatory limbo for many projects. There remains a patchwork of federal guidance and state-by-state regulations that creates a complicated, opaque regulatory structure that is difficult to navigate and obfuscates investor protection responsibilities. Ultimately, this uncertainty is a roadblock to progress and has ongoing implications for investors, entrepreneurs, and capital formation. The ultimate goal should be to reduce ambiguity while promoting balanced regulation that provides a clear road map for entrepreneurs and legacy infrastructures to support innovation while maintaining important safeguards to protect investors.

² <https://www.whitehouse.gov/briefing-room/presidential-actions/2022/03/09/executive-order-on-ensuring-responsible-development-of-digital-assets/>

³ <https://home.treasury.gov/news/press-releases/jy0454>

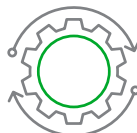
⁴ <https://www.federalreserve.gov/publications/files/money-and-payments-20220120.pdf>

Recommendations

Unlock the Efficiency, Resiliency, and Safety of Regulated Venues



To protect digital asset investors



To drive innovation and U.S. competitiveness



To serve as an on-ramp for entrepreneurs

The immediate opportunity is targeted, meaningful progress. The desired end state is a comprehensive, robust, pragmatic regulatory framework that can be navigated by investors and entrepreneurs alike. The pace of change is accelerating. In order to ensure U.S. financial markets can efficiently protect investors and drive innovation we recommend policymakers take the below steps.

A. Adopt legislation that provides the CFTC with direct oversight over spot trading of digital asset commodities.

Adopting legislation that provides the CFTC with direct oversight of spot trading of digital asset commodities would better serve investors and allow Congress to help shape the digital asset trading ecosystem.

Currently, the global digital asset ecosystem is dominated by opaque venues residing outside of the U.S. Many of these venues operating from undisclosed headquarter locations, attract millions of investors (including U.S. investors), and drive global digital asset prices. There are those who would prefer reduced regulation in order for U.S. venues to better compete in the global digital assets marketplace. However, we believe the U.S. can and should be a leader in promoting proper regulation for the benefit of investors and market integrity. U.S. financial markets and our collective investing strength have great power to mold the future. There are venues already voluntarily applying relevant aspects of CFTC principles to their spot trading venues (including ErisX). We encourage Congress and the CFTC to further support these venues and help safeguard U.S. investors by

adopting a licensing regime and relevant ruleset to govern spot trading venues offering digital asset commodities.

It is natural for the CFTC to be the primary regulator of cash digital asset commodities. The CFTC is already the primary regulator of U.S. commodity derivatives and has fraud and manipulation enforcement authority to protect the integrity of the cash market. While the CFTC does not currently have direct oversight authority of cash markets, Chair Benham has also rightfully noted that carrying out the CFTC's role of ensuring the integrity of the derivatives market requires the CFTC to gain a deep understanding of the underlying cash market. For some years now the CFTC has been dutifully carrying out this mission as it relates to digital assets and has exercised its fraud and manipulation enforcement authority to help safeguard the digital asset derivatives marketplace. Bringing spot venues into the regulatory fold would give the CFTC more tools, knowledge, and experience to ensure the integrity of the digital asset derivatives market and thereby carry out its existing fraud and manipulation authority. This would also enable the CFTC to directly support investors and market integrity by ensuring venues on which they transact are transparent, financially sound, and operate with proper governance.

As Chair Benham has noted, currently “there is no one regulator, either state or federal, with sufficient visibility into digital asset commodity trading activity to fully police conflicts of interest and deceptive trading practices impacting retail customers.”⁵ We support changing this dynamic.

Extending the CFTC’s authority in this limited but meaningful way is a powerful and achievable step. Combined with robust cooperation with the SEC there is no reason why U.S. markets cannot be a leading voice in shaping the global digital asset ecosystem and protecting investors. Importantly, this recommendation need not implicate the current definitional uncertainty of what is or is not a security. Moreover, as Chair Behnam has noted, the majority of the market capitalization of the cash market in digital assets is from digital asset commodities (primarily Bitcoin and Ethereum). Improving oversight of cash markets for these assets alone would be a marked improvement. Determining the exact boundaries of what is or is not a security or commodity should be addressed in a long-term regulatory framework. In the meantime, building regulatory certainty around spot digital asset markets is a positive step for investors.

B. Provide guidance, issue no action relief, or engage in rulemaking to allow an SEC-registered ATS to offer spot trading of digital assets including those that may not be securities and those that are subject to CFTC regulation.

We believe the SEC should facilitate spot trading of digital assets on registered and regulated platforms. An SEC-licensed venue tailored for trading of digital asset securities as well as allowing trading of digital assets for which a classification is unclear, would be an important step towards stabilizing regulatory oversight of digital asset platforms and ensuring investors that their trades are occurring on trusted, transparent, and regulated venues.

Allowing such venues to also register with the CFTC in connection with digital asset commodity trading or digital asset commodity derivative trading would maximize efficiencies for platform operators, their customers, and investors. This construct would counter the ongoing definitional uncertainty with respect to what is or is not a security; serve broader policy objectives by incentivizing unregulated spot trading venues to come into the regulatory fold; and would enhance SEC and CFTC oversight of digital asset trading while enhancing transparency to the benefit of investors.

Notwithstanding the regulatory progress of recent years, there remains much confusion about what is or is not a security in the digital asset ecosystem. This has ongoing implications for the manner in which trading venues offer digital assets. Responsible platforms attempting to offer non-security digital assets are forced to rely on legal opinions and a patchwork of state-by-state money transmission laws or bespoke, state licensure requirements. All the while, non-U.S. platforms with opaque operations or unknown headquarters, gain millions of customers at the expense of many U.S.-based domestic venues that have pursued the responsible, transparent, regulated path.

The application of existing guidance on what is or is not a security is not easily applied to the nuances of the digital asset ecosystem. The lack of a crystallized definition leaves us with a patchwork regulatory structure that is neither simple to navigate nor efficient in the long-term. More importantly, it does not provide investors with sufficient information to fully understand the risks and opportunities of the entities and products with which they interact in the digital asset ecosystem. While ongoing litigation may ultimately provide some additional precedential guidance, it is unlikely to be decisive in the near-term. Regardless, subsequent projects undoubtedly will challenge our precedential understanding of what is or is not a security and how the regulatory framework should be applied to

⁵ <https://www.cftc.gov/PressRoom/SpeechesTestimony/opabehtnam20>

specific projects. Thus, our recommendation is to allow venues that desire to offer trading in digital asset securities or digital assets for which there is not full clarity on whether it is or isn't a security, to trade on an ATS.

We are encouraged by Chair Gensler's recent comments indicating that he has instructed SEC staff to work with CFTC staff on how to jointly address platforms that may trade both digital asset securities and commodities, including how best to register and regulate these platforms.⁶ While most jurisdictions have a single regulator (which is ideal), we are of the view that both agencies can and will work together productively, as they have for many years in other areas (e.g., security futures).

In the near-term or to the extent digital asset commodities cash markets remain unregulated, we believe an ATS license giving venues the option to offer digital securities and digital asset commodities (as well as digital assets for which there is ambiguity as to whether the asset is a security or commodity or neither) would serve as a powerful incentive to ensure that platforms are properly regulated. As previously noted, the global digital asset marketplace is currently dominated by opaque, unregulated venues residing outside the U.S. that offer all digital assets and attract millions of customers but offer little in the form of transparency or investor protection. We believe offering venues a realistic path to building regulated platforms that can - at its discretion - provide access to digital asset securities or all digital assets will encourage more venues to come into the regulatory fold as they seek to attract more U.S. customers. This would allow the collective investment strength of the U.S. to serve as a powerful driving force and help level the playing field between U.S. venues pursuing safe and responsible progress vs. unregulated non-U.S. venues.

If, consistent with our recommendation, the CFTC attains direct oversight of cash markets in digital asset

commodities, the SEC would oversee an adaptive ATS model and the CFTC would oversee cash markets of digital asset commodities. Under this framework venues would have complete business model flexibility to: a) offer securities or ambiguous digital assets via an SEC regulated ATS; b) offer digital asset commodities via a CFTC regulated platform; or c) maintain a single platform with dual license to offer all digital assets. The latter structure would allow digital asset platforms to build a single, digital asset architecture, rather than bifurcating architecture based on whether a digital asset is or is not a security. This would reduce costs, allow flexibility and scalability, and allow venues to create powerful solutions for various types of digital assets.

In our view, the SEC can and should facilitate a regulated platform that allows for consistent trading of all digital assets. In addition to the above reasons, this would serve as an important building block for future regulatory developments and would in fact serve as on-ramp for future entrepreneurs. The creation of a new project and the listing of a digital asset could be supported and funneled through a well-known regulatory structure applicable to ATSs. As there becomes more clarity with respect to what is or is not a security (and further clarity on issuance, disclosures, exemptions, listing requirements when a token is deemed a security), this ATS framework may serve as gateway for current and future digital asset entrepreneurs. The ATS-licensed platform would serve as a logical place for relevant digital asset disclosures and would help reduce risk to consumers that arises when a digital asset is offered for trading and subsequently deemed a security. For example, rather than entirely halting trading when an existing asset is deemed a security, which results in frozen assets or obligates investors to transfer assets to unregulated venues, the regulated platform could aid the transition of the asset to a security listing segment or manage a more structured wind-down process that helps limit the impact to investors.

⁶ <https://www.sec.gov/news/speech/gensler-remarks-crypto-markets-040422>

We note that in support of this arrangement it would be beneficial for the guidance, no action relief, or rulemaking to consider additional enhancements to allow broker-dealers to efficiently and effectively hold digital assets and fully support investors.

C. Harness legacy, regulated exchanges by approving a spot Bitcoin ETF

Since Cboe's first rule filing proposal in 2016 to list an exchange-traded product to provide exposure to Bitcoin in the U.S., the market capitalization of Bitcoin has grown from approximately \$10 billion to surpassing \$1 trillion for much of 2021. This is due in large part to the accelerating adoption of digital assets by asset managers, corporates, pension funds, endowments, insurers, and fund managers. Market participants have taken great strides to embrace Bitcoin and digital assets, which has greatly expanded the digital asset ecosystem. As previously noted, great regulatory strides have also been made.

Unfortunately, despite these developments, access for U.S. retail investors to gain exposure to Bitcoin remains primarily limited to acquiring spot Bitcoin; acquiring shares of publicly traded companies with the hopes they will serve as a proxy to

Bitcoin; acquiring Bitcoin futures ETFs, which have ongoing rolling costs that reduce investor returns; or entering OTC Bitcoin funds with high fees and volatile premiums and discounts. Meanwhile, investors in many other countries, including Canada, are able to use more traditional, cost-effective ETFs via Bitcoin ETFs holding Bitcoin directly. This disadvantages U.S. investors.

Not only does the lack of access to a regulated U.S. spot Bitcoin ETF potentially harm investors, but this also prevents traditional, legacy regulated equity exchanges from better serving digital asset investors. In effect, the lack of an approved spot Bitcoin ETF is preventing investors from accessing the most regulated, transparent, and mature equity market in the world when seeking to gain exposure to Bitcoin in a known wrapper. Instead, investors must transact on unregulated venues that do not have the long history of robust regulation and investor protection offered by legacy equity markets.

We strongly believe it is time to harness the power of regulated exchanges to promote transparency and investor protection by approving a spot Bitcoin ETF and explore additional spot ETFs for mature digital assets.

Conclusion

The above steps do not require grand-scale legislation or rulemaking to have a positive impact on the investor experience and should be pursued now. Longer term the goal should be a pragmatic, comprehensive, and robust regulatory framework that can be navigated by investors and entrepreneurs alike. Clear statutory definitions, jurisdictional boundaries, and disclosure requirements are hallmarks of such a framework.

We look forward to working with policymakers and others to achieve this beneficial end state.