



June 13, 2023

By Electronic Submission

Vanessa A. Countryman
Secretary
U.S. Securities and Exchange Commission
100 F Street N.E.
Washington, D.C. 205499-1090

**Re: Re-Opening of Comment Period for Amendments to Exchange Act Rule 3b-16
Regarding the Definition of "Exchange"
File Number S7-02-22**

Dear Ms. Countryman:

Payward, Inc., d/b/a/ Kraken ("Kraken") submits this letter in response to the request for comments by the U.S. Securities and Exchange Commission ("SEC" or "Commission") regarding its proposal to amend the definition of "exchange" in Rule 3b-16 (the "Proposed Rule") under the Securities Exchange Act of 1934 (the "Exchange Act"), as further expanded upon in the Supplemental Information and Reopening of Comment Period for Amendments Regarding the Definition of "Exchange" (the "Supplemental Release").¹

Kraken's primary business is the operation of an online cryptocurrency platform. Kraken's operations in the United States are carried out through Payward Ventures, Inc., a Money Services Business registered with the Financial Crimes Enforcement Network (Registration No. 31000239561651).

Kraken has concerns regarding the Proposed Rule. Many of these have been shared by other commenters. Specifically:

1. The Commission's authority to prohibit trading of non-securities is not clear - we believe that the Commission acts in excess of its statutory authority in proposing to prohibit exchanges and alternative trading systems ("ATs") from trading non-security crypto assets;
2. The Commission should defer to Congress on the question of where non-securities may be traded, particularly as Congress is currently deliberating this very question; and
3. The Proposed Rule fails to evaluate the likely economic implications the Commission must assess, and the costs and benefits of its proposed prohibition on the trading of non-security crypto assets on exchanges and ATs. The failure to carry out this economic assessment would go against the Commission's own stated best practices, and may cause the Proposed Rule to violate the requirements of the Administrative Procedure Act ("APA").

To address these concerns, we respectfully request that the Commission withdraw the Proposed Rule until the apparent deficiencies in statutory authority can be adequately addressed, and until a thorough economic analysis of the Proposed Rule's implications has been undertaken.

¹ 88 FR 29448 (May 5, 2023).

I. The Commission Lacks the Authority to Prohibit the Trading of Crypto Non-Securities on Exchanges and ATSS

The Proposed Rule would require crypto trading platforms that trade securities to register with the Commission as exchanges or as ATSS. The Commission then implies that upon registering as an exchange or ATS, the crypto trading platform must stop trading all non-securities.² The Commission asserts that trading venues that register as exchanges or ATSS must stop trading non-security crypto assets. However, the Commission does not cite any authority for this proposed prohibition, only noting that exchanges currently trade securities for U.S. dollars. We found no such authority in our research.

The question of whether an exchange or ATS can trade non-securities has profound economic significance for crypto trading platforms. A significant volume of the trading on crypto platforms revolves around bitcoin and ether, both of which have been acknowledged to be non-securities by senior Commission personnel.³ Stablecoins are another example of non-securities that are vital to the frictionless functioning of crypto trading platforms — without them, such platforms would be forced to resort to cash-based settlement for trades, slowing settlement times and increasing settlement costs.⁴ Bitcoin, ether, and stablecoins account for approximately half of all trading on Kraken, and are extensively used by every major crypto trading platform in the U.S.

If the trading of crypto non-securities such as bitcoin, ether, and stablecoins (among others) on exchanges and ATSS is prohibited, the Commission must point to clear Congressional authorization for this prohibition given the impact to crypto trading platforms.⁵ The Commission acknowledges that the estimated value of the global market for crypto assets is \$900 billion, and the trading of crypto asset non-securities likely accounts for a sizable majority of this estimate. Thus, the Commission should point to a clear grant of authority before it regulates a sizable market for non-securities.

However, the Commission points to nothing in the text, structure or history of the Exchange Act which would support such a prohibition. Nothing in the Act or its history prohibits the trading of non-securities on exchanges or ATSS. ATSS are regulated as broker-dealers, and many

² *Id.* at 29482, “To the extent that a New Rule 3b-16(a) System enables the trading of crypto asset securities for crypto assets that are not securities, that entity may also incur the cost of having to stop enabling such trades, and the resulting loss of revenue.”

³ With respect to bitcoin, see Neeraj Agrawal, SEC Chairman Clayton: Bitcoin is Not a Security (April 27, 2018). Available at: <https://www.coincenter.org/sec-chairman-clayton-bitcoin-is-not-a-security/>. With respect to ether, see William Hinman, Digital Asset Transactions: When Howey met Gary (Plastic) (June 14, 2018). Available at: <https://www.sec.gov/news/speech/speech-hinman-061418>.

⁴ See The Board of the International Organization of Securities Commissions, IOSCO Decentralized Finance Report (March 2022) at 16-17, noting that “Stablecoins are designed to be a less volatile alternative to other crypto-assets, and, because of their perceived stability, they have become DeFi’s substitute for fiat currency, acting as the “stable” leg in trading transactions involving more or highly volatile crypto-assets or as the “collateral” for lending and borrowing.” Available at: <https://www.iosco.org/library/pubdocs/pdf/IOSCOPD699.pdf>.

⁵ See *West Virginia v. Environmental Protection Agency (EPA)*, 142 S. Ct. 2587 (2022), quoting *Utility Air Regulatory Group v. EPA*, 573 U. S. 302, 324. When an administrative agency “seeks to regulate “a significant portion of the American economy,” or require “billions of dollars in spending” by private persons or entities, it “must point to clear congressional authorization” to do so.

broker-dealers today facilitate transactions in commodities such as gold, silver, or foreign exchange.⁶

If, upon registration as exchanges or ATSS, crypto trading platforms must immediately cease trading non-securities, such cessation would significantly disrupt the crypto asset market and harm consumers. The Commission cannot require crypto trading platforms to forego significant trading revenues and incur substantial logistical costs solely on the basis of assertions that lack statutory, or even common law, authority.

II. The Commission Should Defer to Congress on the Trading of Non-Security Crypto Assets on Exchanges and ATSS

The Commission implicitly proposes to prohibit the trading of crypto asset non-securities on exchanges and ATSS just as Congress is preparing to consider precisely this question. On June 2, 2023, the Chairmen of the House Financial Services Committee and the House Committee on Agriculture jointly released a discussion draft of legislation that would provide a statutory framework for crypto asset regulation.⁷ Among other things, this proposed legislation expressly permits crypto trading platforms to register with both the SEC and Commodity Futures Trading Commission, and to then trade both crypto assets that are securities as well as crypto assets that are not securities.⁸ Similarly, Senators Lummis and Gillibrand introduced comprehensive legislation for crypto asset regulation in June 2022 addressing these same concerns.⁹

The Commission has no jurisdiction over, and no expertise in, the trading of non-securities, whether crypto or otherwise. “When [an] agency has no comparative expertise” in making certain policy judgments, it is presumed that Congress does not task the agency with making such policy judgments.¹⁰ That presumption is reinforced where, as here, Congress is itself preparing to grapple with the issue. We respectfully request the Commission to defer to Congress on the question of where non-security crypto assets may be traded. We also request the Commission clearly demonstrate such deference to Congress by withdrawing crypto related aspects of the Proposed Rule until Congress’s deliberations are complete.

III. The Commission Fails to Adequately Assess the Economic Implications of the Proposed Prohibition on Trading of Crypto Non-Securities

The Commission’s Office of General Counsel recognizes that a comprehensive economic analysis is an essential element of every rulemaking. Among other things, that economic analysis must include an evaluation of the benefits and costs—both quantitative and qualitative—of the proposed

⁶ Consider, for example, the Aberdeen Standard Silver ETF Trust. In its Form 10-K, the Trust names several prominent broker-dealer firms as “Authorized Participants” who routinely transact in silver. See pp. 11 and 12 at <https://www.abrdn.com/docs?documentId=US-050422-168880-6>.

⁷ *McHenry, Thompson, Hill, Johnson Release Digital Asset Market Structure Proposal*, (June 2, 2023). Available at: https://financialservices.house.gov/uploadedfiles/digital_002_xml.pdf.

⁸ See Section 308 of the proposal, which discusses such dual registration.

⁹ *Lummis, Gillibrand Introduce Landmark Legislation To Create Regulatory Framework For Digital Assets*, (June 7, 2022). Available at: <https://www.gillibrand.senate.gov/wp-content/uploads/imo/media/doc/Lummis-Gillibrand%20Responsible%20Financial%20Innovation%20Act%20%5bFinal%5d.pdf>.

¹⁰ *West Virginia v. EPA*, quoting *Kisor v. Wilkie*, 139 S. Ct. 2400 (2019) (slip op., at 17).

rule.¹¹ An analysis of the economic implications of a proposed rule, and its impact on efficiency, competition, and capital formation, is also required by the Exchange Act,¹² and by a number of judicial precedents.¹³ Given the well-established requirement for a thorough economic analysis, it is therefore surprising that the Proposed Rule seems to ignore the actual costs that would be imposed by prohibiting exchanges and ATSs from trading crypto asset non-securities.

The absence of economic data on crypto assets and trading platforms is evident through the Proposed Rule,¹⁴ including when the Commission notes that its proposed prohibition on the trading of crypto asset non-securities will likely have “significant” costs for crypto trading platforms, without providing any further data or analysis.¹⁵

Simply terming costs on crypto trading platforms as “significant” without quantifying these costs further is insufficient for this required analysis. The Commission should consider the costs to crypto trading platforms of ceasing to trade crypto asset non-securities, and contrast these costs with the benefits of uninterrupted and friction-free trading of crypto non-securities assets.

In the Proposed Rule, the Commission proposes a prohibition on the trading of crypto asset non-securities that would likely threaten the continued viability of crypto trading platforms. Even if the Commission has the authority to propose such a prohibition, the Commission must at least undertake the data collection and analysis required to justify this regulatory choice.

* * *

In light of the above concerns, we respectfully request the Commission withdraw the Proposed Rule until these concerns can be properly addressed. We stand ready to work with the Commission towards a more meaningful proposal for crypto asset trading platforms.

Sincerely,

Jonathan Jachym
Global Head of Policy
Payward, Inc.

¹¹ Memorandum to Staff of the Rulewriting Divisions and Offices from RSFI and OGC (March 16, 2012). Available at: https://www.sec.gov/divisions/riskfin/rsfi_guidance_econ_analy_secrulemaking.pdf.

¹² 15 U.S.C. 78c(f).

¹³ *Chamber of Commerce of U.S. v. SEC*, 412 F.3d 133, 143 (D.C. Cir. 2005); *Business Roundtable v. SEC*, 647 F.3d 1144, 1148 (D.C. Cir. 2011); *New York Stock Exchange LLC v. SEC*, No. 19-1042 (D.C. Cir. Jun. 16, 2020); each recognizing the Commission’s “statutory obligation to determine as best it can the economic implications of [a] rule.” See also *Business Roundtable v. SEC*, 647 F.3d 1144, 1148 (DC Cir. 2011); *Motor Vehicle Mfrs. Ass’n of U.S., Inc. v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29, 43 (1983), the Commission must “articulate a satisfactory explanation for its action including a rational connection between the facts found and the choices made.”

¹⁴ See, for example, Supplemental Release at 29470, 29471, 29474, and 29479, noting the absence of data, or the unreliability thereof.

¹⁵ Supplemental Release at 29482.