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17 CFR Part 240

Custody of Digital Asset Securities by Special Purpose Broker-Dealers

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Security Exchange Commission
100F Street NE
Washington, DC 20549-1090

To Commission,

The Commission's proposal for allowing Special Purpose Broker Dealers for custody of digital asset securities in an allotted time frame is productive to the growth and innovation of the US capital markets. It's very important that the Commission allows an innovative open environment for US broker dealers with the regulatory stability of the Customer Protection Rule for public confidence. Although the current regulations are made for historical capital markets, innovations in technology has allowed to eliminate a few steps in how assets are created, trades are cleared, risks are minimized, and regulatory confidence are conducted today.

Commission Request for Comments:

1. Currently the industries best practices for protecting against theft, loss, and unauthorized or accidental use of private keys necessary for accessing and transferring digital asset securities is the use of requiring various types of multi factor authentication (MFA), a combination of MFA, cold storage vaults with time delays, and/or offering unhosted wallets. The industry best practices for generating, safekeeping, and using private keys have been seen with the private key hidden from view unless the user requests it to be seen. This is similar to bank account numbers hidden online until a user requests it to be seen. This feature is very common in most US crypto exchanges.

2. The industries best practices to address events that could affect a broker dealer's custody of digital asset securities such as a hard fork, airdrop, or 51% attack is due diligence on any new digital asset security. Some of these issues are unforeseen but due diligence will help minimize future risks. Current due diligence is seen regularly with any broker dealer with private equity offerings and under writings. Hard forks,

airdrops, staking, and 51% attacks would be an issue to disclose at the client account opening on how these events would be handled in the future. If other unforeseen events occur, the broker dealer can disclose within a reasonable time on how they will be resolved or actions conducted.

3. The processes, software and hardware systems, or other formats or systems that are currently available to broker dealers to create, store, or use private keys and protect them from loss, theft, or unauthorized or accidental use can be seen with specialty crypto wallet providers or proprietary wallets with storage and security focused. An example of a specialty crypto wallet can be seen with Fireblocks and a proprietary crypto wallet can be seen with Coinbase.

4. The accepted practices (or model language) with respect to disclosing the risks of digital asset securities and the use of private keys is similar to current disclosures banks and broker dealers currently use regarding terms of service, disclosures, asset risks, and passwords.

5. The Commission should not expand this position in the future to include other businesses such as traditional securities and/or non-security digital assets because they have multiple clearing partners which currently don't use this type of public/private key technology. If this were to be expanded into non-security digital assets, clearing firms, NSCC/DTC, and existing regulations for Reg ATS would have to be changed. The redundancy would eliminate the need for some of these entities.

6. The differences between clearance and settlement of traditional securities and digital assets which could lead to higher or lower clearance and settlement risks for digital assets as compared to traditional securities would be:

   A. Instead of traditional T+3, clearance and settlement is seconds to hours depending on the blockchain.
   B. This blockchain speed in itself eliminates T+3 clearing risk or intraday risk exposure to the broker dealer.
   C. A broker dealers exposure to open positions is the biggest risk a broker dealer can have. This can be seen with broker dealers, clearing firms, or exchange failures.

7. The specific benefits and/or risks a broker-dealer operating a digital asset alternative trading system that the Commission should consider for any future measures it may take would be the benefits of blockchain transparency which is a method of a real time audit. This can help eliminate the need for reporting to a Trade Reporting Facility (TRF), Order Audit Trail System (OATS), and Trade Reporting Compliance Engine (TRACE) as required by FINRA defined by Reg NMS. Also, because digital asset securities are so new, there should be an exemption to Reg NMS. Reg NMS will prohibit this new asset class innovation and growth from a compliance and market structure position.

   Because of these enhanced benefits that digital asset securities bring, there are risks because of it's ease of use and security. But keep in mind, there is a trade off with this new technology with it’s added benefits. These added benefits from digital asset securities will benefit regulation, US capital markets, and consumer confidence.

Sincerely,

JEFF MARTINEZ

Jeff Martinez
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