May 11, 2022

Via Electronic Delivery

Mr. Christopher J. Kirkpatrick
Secretary of the Commission
Commodity Futures Trading Commission
Three Lafayette Centre
1155 21st Street, NW
Washington, DC 20581

Re: LedgerX LLC d/b/a FTX US Derivatives ("FTX US") Request to Amend DCO Order of Registration (IF 22-001)

Dear Mr. Kirkpatrick:

Paradigm Operations LP ("Paradigm")[1] appreciates the opportunity to provide written comments to the Commodity Futures Trading Commission ("CFTC" or the "Commission") in connection with the filing by FTX US to amend its order of registration as a Derivatives Clearing Organization ("DCO").

Paradigm supports a regulated, competitive cryptocurrency market. The FTX US application to offer direct-to-customer margin will benefit consumers by dispersing market power of incumbent exchanges more widely. Further, approval of the FTX US application will reduce the over-reliance on the current gatekeepers to trading markets. For the reasons described below, we respectfully urge the Commission to approve the FTX US application.

I. The CFTC is Well Positioned to Provide Market Oversight of Cryptocurrency Markets

Although no federal agency holds exclusive jurisdiction over the trading of digital assets, the CFTC is well positioned to oversee FTX's activity as a DCO with direct clearing relationships.

The CFTC's Workload Permits Focus on Emerging Technology

[1] Paradigm is an investment firm focused on supporting emerging crypto/Web3 companies and protocols. The support offered by Paradigm ranges from technical (mechanism design, smart contract security, engineering) to operational (recruiting, regulatory strategy) hands on assistance for emerging crypto projects. Paradigm utilizes a multi-stage approach, investing in crypto-assets and businesses from the earliest stages of idea formation through maturity. Paradigm is an investor in FTX US's parent company. For more information, please see https://www.paradigm.xyz/.

The CFTC has demonstrated to be years (in some cases, more than a decade) ahead of the Securities and Exchange Commission ("SEC") in terms of critical rulemakings required in response to the 2008 financial crisis. The CFTC has largely completed rulemakings under the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank"). The CFTC has finalized 79 rules, exemptive orders and guidance actions,[2] enabling it to focus on newer issues and address the need for regulatory oversight of emerging financial products. By contrast, the SEC is still proposing and receiving comment on Dodd-Frank rules that have yet to be adopted since the law's passage in 2010,[3] with new proposals being published as recently as last month.[4]

The SEC's list of outstanding rulemakings dating back to 2010 is only part of the agency's portfolio. The SEC's mandate, which is broader than the CFTC's, covers a number of other important areas in addition to issues covered by the CFTC.[5] While these issues are all part of the SEC's mission to protect investors; maintain fair, orderly, and efficient markets; and facilitate capital formation, the substantive areas range from Treasury market reform, JOBS Act implementation, examinations of broker-dealers and investment advisers, special purpose acquisition companies, credit rating agencies, consolidated audit trail, and insider trading rules, among many, many, other things.

The CFTC Has a Demonstrated History of Understanding and Promoting Innovation

The CFTC has a long history of promoting innovation in its regulatory philosophy, positioning it well to oversee the introduction of new products rooted in emerging technologies. In its 2022-2026 Strategic Plan, the CFTC states that it must "*keep pace and take the lead, when appropriate, to encourage responsible innovation*" and "*will emphasize and enforce industry compliance so that our markets remain not only innovative, but fair*."[6]

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[2] CFTC, Final Rules, Guidance, Exemptive Orders & Other Actions, *available at* https://www.cftc.gov/LawRegulation/DoddFrankAct/Dodd-FrankFinalRules/index.htm.

[3] *See* Testimony of Chair Gary Gensler Before the United States Senate Committee on Banking, Housing, and Urban Affairs (September 14, 2021), *available at* https://www.sec.gov/news/testimony/gensler-2021-09-14 (Indicating that part of his agenda seeks to finalize some of the remaining Dodd-Frank rules, asking staff for recommendations on how the SEC can finalize mandates to "stand up the regime established under the Dodd-Frank Act.")

[4] *See* Rules Relating to Security-Based Swap Execution and Registration and Regulation of Security-Based Swap Execution Facilities, RIN 3235-AK93 (proposed April 6, 2022 and not yet published in the Federal Register), *available at* https://www.sec.gov/rules/proposed/2022/34-94615.pdf.

[5] There are almost 50 rulemaking items listed on the SEC's rulemaking agenda. *See* Office of Information and Regulatory Affairs, Agency Rule List - Fall 2021, *available at* https://www.reginfo.gov/public/do/eAgendaMain?operation=OPERATION_GET_AGENCY_RULE_LIST&currentPub=true&agencyCode=&showStage=active&agencyCd=3235&csrf_token=2B7460B98B542518D39A37A6F699DD95730935F3BF99E6EF2A6BDC57A63548E490A4A50997D5E09C0C2732DCE16D2FBFA853.

[6] Commodity Futures Trading Commission *Strategic Plan 2022-2026*, (April 1, 2022), *available at* https://www.cftc.gov/media/7081/CFTC2022_2026StrategicPlan/download ("As derivatives markets continue to evolve, the CFTC remains committed to being the global standard for sound derivatives regulation by ensuring that derivatives markets are responsive to emerging risks, technologies, and trends through supporting legislation, promulgating rules, issuing guidance, and establishing policies that promote innovation and protect market participants, users, and the economy. The Commission holds itself accountable to work with market participants domestically and abroad to ensure the U.S. derivatives markets are efficient, competitive, and free from fraud, manipulation, and other disruptive or abusive practices.").

In addition, Chairman Behnam noted in recent remarks to Congress that "*a core purpose of the Commodity Exchange Act is the promotion of 'responsible innovation and fair competition among boards of trade, other markets and market participants*.'"[7] This commitment to addressing difficult issues is critical to bring stability to new, rapidly changing technology, and will benefit consumers and the economy as a whole.

II. The FTX US Model Would Provide More Choices for Investors and Therefore Increase Competition

Approval of the FTX US application will provide investors greater choice among trading venues. The vast majority of trading volumes on U.S. derivatives exchanges is brokered by just a few intermediaries. This structure perpetuates a concentration of market power, contrary to the stated goals of past and current administrations to diffuse it.

The need to disperse market power is especially evident with regards to cryptocurrencies, namely Bitcoin ("BTC") and Ether ("ETH") futures, which are commonly exchange-traded. By contrast, BTC and ETH futures continue to be the sole province of several established centralized incumbent financial exchanges, particularly because of the challenges new market entrants face trying to capture market share. This is evidenced by the lack of available substitutes to achieve prominent volumes. In effect, the established power of current incumbents has made it all but impossible for a new competitor to emerge that can truly challenge them. This slows growth and innovation in this industry, harming all participants.

FTX US's direct access model enables ease of access to prices and liquidity for retail investors, including through mobile applications. This, and other features, should lead to demand, volume, and liquidity, providing market participants with an alternative to incumbent exchanges, and adding both efficiency and competition to the marketplace. Encouraging participation from new entrants will support better pricing for users and promote the creation of new products and services.

The FTX US model will also give investors the choice to access markets directly, without relying on a financial institutions. Working alongside the CFTC, FTX US has worked to ensure that investor protections normally afforded by FCMs are still present. This will permit ordinary retail investors to safely access products previously available only to the most well-resourced investors or through the use of intermediaries. Specifically, protections that have traditionally been provided by exchanges, such as risk disclosure, AML/KYC compliance, and market integrity through rigorous surveillance, will now be provided directly by FTX US' platform when accessed by their users.

While intermediaries will be allowed to access the market on behalf of their customers, those customers will no longer depend on those intermediaries for access. Market participants will have a choice.

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[7] *See* Testimony of Chairman Rostin Behnam Regarding the "State of the CFTC" before the U.S. House of Representatives Committee on Agriculture, March 31, 2022, *available at* https://www.cftc.gov/PressRoom/SpeechesTestimony/opabehnam22 (citing 7 U.S.C. § 5(b)).

III. The FTX US Model Would Reduce Systemic Risk

FTX's request for an amended DCO registration order to permit it to clear non-intermediated, margined products should be granted because it would reduce systemic risk by leveraging innovative technology to avoid credit shocks and reduce intermediary credit-risk. FTX's model allows for participants' margin to be calculated every 30 seconds on a rolling 24-7 basis and for collateral to be automatically liquidated in 10% increments until the margin requirement is met. Compared to the traditional system where margin is calculated on a T+1 or T+weekend basis and collateral liquidated entirely, the FTX model reduces the potential of large credit shocks such as those evidenced in the nickel market of the London Metal Exchange. During the financial crisis of 2008, the fact that markets were closed for the majority of each day and over the weekend resulted in shocking and wrenching valuation and price shifts when markets reopened, to the detriment of all market participants and the financial system as a whole. If we had 24/7 real-time rolling margin calculations in 2008, the grueling month of September 2008 might well have been more orderly and the credit markets would have been able to better weather that storm.

The ability to trade assets 24 hours a day, 7 days a week requires a continuous risk and margin model. For markets where price action in the underlying spot market is constantly occurring or is influenced by world events, it is especially risky for intermediaries to extend credit overnight and over weekends.

With less intermediation of markets, as offered by FTX US, the number of interconnection risks between financial institutions in the overall market ecosystem is minimized. This also helps to minimize the "too big to fail" systemic-risk concerns that policymakers have continuously addressed since the 2008 financial crisis. The simplicity of the direct-to-investor market structure also reduces other operational risks compared to other models. The FTX US structure presents fewer risks to the platform, to the end investor, and makes it easier for the platform to manage risk overall.

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In summary, we fully support the FTX US request to amend its DCO registration. For the reasons detailed above, we urge the Commission to approve this request as soon as possible. If the Commission has any questions or comments, please do not hesitate to contact Justin Slaughter at justin@paradigm.xyz.

Respectfully Submitted,

Justin Slaughter
Policy Director
Paradigm