

Public Statements & Remarks

Dissenting Statement of Commissioner Caroline D. Pham on DeFi Enforcement Action Involving Uniswap Protocol

September 04, 2024

I respectfully dissent on *In re Universal Navigation Inc.*, a decentralized finance (DeFi) enforcement action involving the Uniswap Protocol^[1] on the Ethereum blockchain, because there is no evidence in the administrative record that describes the specific terms and/or characteristics of the “Leveraged Tokens” as characterized in the settlement order. Without such information, it is not possible to perform an appropriate product legal analysis of the Leveraged Tokens to determine whether they are a CFTC-jurisdictional product, and, therefore, whether the CFTC has the authority to bring this enforcement action in the first place and whether a violation of the Commodity Exchange Act (CEA) or CFTC regulations has actually occurred.

This case is about whether there were leveraged, margined, or financed commodity transactions by persons that are not eligible contract participants (ECPs) and there was no actual delivery of the commodity within 28 days. If so, then that transaction is required to be executed on a futures exchange. But the CFTC’s novel approach today is legally simplistic and conveniently cuts corners to create a pretext for enforcement.

For example, I am puzzled how we can charge the Respondent based upon no evidence beyond the word “leveraged” appearing in the names of these tokens. Consequently, applying the logic of the CFTC’s legal argument, it seems that any commercial transaction to purchase a cow, a bushel of oats, or a barrel of oil that involves the word “financed” and is delivered in 30 days is a violation of Section 4(a) of the CEA pursuant to Section 2(c)(2)(D) and needs to be executed on a futures exchange.^[2] I am skeptical that the CFTC would try to enforce these statutory provisions outside of DeFi—what if the delivery of financed cows was supposed to be within 28 days, but the train was delayed and arrived in 29 days? According to the CFTC’s legal argument in today’s order, those financed cows in the cash market would have to be sold on a futures exchange, not at a cattle stockyard. Obviously, if the CFTC were to broadly apply this strict interpretation of the law, it would have the absurd result of bringing the U.S. economy and global commodity markets to a halt. It is no surprise that the legislative history does not support the CFTC’s novel approach in today’s order.

Further, as I have stated before, I believe it is a violation of the Administrative Procedure Act (APA) for the Commission to establish such sweeping interpretations in an administrative settlement order, rather than engage in notice-and-comment rulemaking, particularly when such interpretations impact a broad swath of the economy. As I have previously stated, “Major questions are best addressed through a transparent process that engages the public to develop appropriate policy with expert input—through notice-and-comment rulemaking pursuant to the APA. Regulatory clarity comes from being out in the open, not in the dark.”[3]

I am concerned that the Commission’s ever-expanding jurisdictional overreach continues to perpetuate a lack of regulatory clarity not only regarding digital assets, but more significantly, for our cash commodity markets where every day, a farmer, rancher, or producer needs to use credit—financing—to grow and produce the food on our dinner tables. Therefore, I must dissent on the basis that this administrative proceeding is both legally unsupported under the CEA and is a violation of the APA, in addition to the serious public policy concerns that this settlement order will create further regulatory uncertainty, put small cash market businesses in jeopardy of violating the law, and stifle American innovation.

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This DeFi case may very well be a regulatory allergic reaction to new technology. But this reaction is not realistic or sustainable. We live in an age of technological transformation that impacts every aspect of our day-to-day lives—from the Now Economy to the Gig Economy and the Creator Economy. This era of human invention and productivity is characterized by increasingly direct connections among ordinary people and the empowerment of the individual with an app as the center of the overall Digital Economy. The world has changed from B2B to B2C to C2C,[4] and there is no turning back the clock.

Emerging technologies like the blockchain and decentralized protocols that enable the direct peer-to-peer connection that underpins the consumer-driven shifts already underway in sectors such as retail, entertainment, and financial services, have the potential to write a brand-new chapter in our Nation’s rich history of ingenuity and opportunity—the embodiment of the American Dream. With technology, anyone with a big idea and access to capital can start a business. This inclusion in the New Economy can lift people and families up and change their circumstances. When opportunity knocks, it makes no sense to slam shut the door.

It is imperative that regulators fully understand and holistically address these significant shifts in market structure through a carefully considered and forward-looking approach that appropriately balances robust protections and guardrails while enabling innovations and technological advancements that promote economic growth and access to markets. I continue to urge that the Commission consider all the tools besides enforcement actions that we can use to develop policy, like my previous suggestions for public roundtables,[5] time-limited pilot programs,[6] and considering the recommendations and reports from the CFTC’s advisory committees,[7] including the Global Markets Advisory Committee (GMAC) that I sponsor. Commissioner Mersinger has also previously shared her views on the Commission’s approach to DeFi.[8]

Undoubtedly, there can be fraud in DeFi markets, as in any marketplace. I believe the CFTC can and should vigorously pursue fraud and manipulation in our markets and bring bad actors to justice. But that is not what this case is about. It is regretful that the Commission’s action today is instead a misguided and rushed attempt to beat the SEC to the punch and claim jurisdiction over DeFi.

[1] The Uniswap Protocol is a “suite of persistent, non-upgradable smart contracts that together create an automated market maker, a protocol that facilitates peer-to-peer market making and swapping of ERC-20 tokens on the Ethereum blockchain,” <https://docs.uniswap.org/concepts/overview> (<https://docs.uniswap.org/concepts/overview>). Automated market makers (AMM) are common in trading and markets, and both U.S. and non-U.S. authorities have regulatory frameworks for the use of AMMs to mitigate risks and ensure market integrity. I have repeatedly stated that the Commission should examine existing regulations applicable to the use of AMMs and algorithmic trading, and consider whether those regulations apply to market operators and market participants that utilize DeFi protocols. To illustrate this point, regulators do not bring enforcement actions against algorithms—regulators bring enforcement actions against those who engage in trading activity in violation of the law, whether algorithms were involved or not. It is the trading activity, not the technology, that matters.

[2] Section 2(c)(2)(D) of the CEA makes reference to certain “retail” commodity transactions that are “leveraged, margined, or financed” and do not result in actual delivery within 28 days. Under the CEA, the definition of “retail” is broad and means persons who are non-ECPs. Accordingly, “retail” encompasses not only individuals, but many small businesses like family farms or small growers, producers, and merchants—commercial end-users that are the bedrock of the U.S. agricultural economy.

[3] Statement of Commissioner Caroline D. Pham on *SEC v. Wahi* (July 21, 2022), <https://www.cftc.gov/PressRoom/SpeechesTestimony/phamstatement072122> (<https://www.cftc.gov/PressRoom/SpeechesTestimony/phamstatement072122>).

[4] Business-to-business (B2B), business-to-consumer (B2C), and consumer-to-consumer (C2C).

[5] Statement of Commissioner Caroline D. Pham on Innovation and Market Structure (Aug. 29, 2024), <https://www.cftc.gov/PressRoom/SpeechesTestimony/phamstatement082924b> (<https://www.cftc.gov/PressRoom/SpeechesTestimony/phamstatement082924b>); CFTC Commissioner Caroline D. Pham and SEC Commissioner Hester M. Peirce, “Making progress on decentralized regulation—It’s time to talk about crypto together,” *The Hill* (May 26, 2022), <https://thehill.com/opinion/congress-blog/3503277-making-progress-on-decentralized-regulation-its-time-to-talk-about-crypto-together/> (<https://thehill.com/opinion/congress-blog/3503277-making-progress-on-decentralized-regulation-its-time-to-talk-about-crypto-together/>).

[6] New Regulatory Sandboxes: A Proposal for a CFTC Pilot Program, Remarks of CFTC Commissioner Caroline D. Pham Before the Cato Institute, *Staying Ahead of the Curve: Crypto Regulation and Competitiveness* (Sept. 7, 2023), <https://www.cftc.gov/PressRoom/SpeechesTestimony/opapham9> (<https://www.cftc.gov/PressRoom/SpeechesTestimony/opapham9>).

[7] The GMAC recently released a digital asset taxonomy as a resource available to policymakers. See <https://www.cftc.gov/PressRoom/Events/opaeventgmac030624> (<https://www.cftc.gov/PressRoom/Events/opaeventgmac030624>). The CFTC’s Technology Advisory Committee (TAC) released a DeFi report, see <https://www.cftc.gov/PressRoom/Events/opaeventtac010824> (<https://www.cftc.gov/PressRoom/Events/opaeventtac010824>), and the CFTC’s Market Risk Advisory Committee (MRAC) has held meetings that included blockchain technology, see <https://www.cftc.gov/About/AdvisoryCommittees/MRAC> (<https://www.cftc.gov/About/AdvisoryCommittees/MRAC>).

[8] *E.g.*, Dissenting Statement of Commissioner Summer K. Mersinger Regarding Enforcement Actions Against: 1) Opyn, Inc.; 2) Deridex, Inc.; and 3) ZeroEx, Inc. (Sept. 3, 2023), <https://www.cftc.gov/PressRoom/SpeechesTestimony/mersingerstatement090723> (<https://www.cftc.gov/PressRoom/SpeechesTestimony/mersingerstatement090723>).

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