

## (Crypto) Exchanges as Regulators By Yesha Yadav

This Article explores the role of private exchange oversight in crypto-market regulation. It is well-established that exchanges exercise expansive powers to police securities markets. As self-regulatory organizations, exchanges have evolved to occupy a complex place as overseers within the larger regulatory architecture. On the one hand, they offer expert, experienced monitoring, and disciplinary power by controlling access to and use of a critical economic resource. On the other, they possess various conflicts of interest, as commercial for-profit firms, that diminish their ability to offer credible, intense enforcement where they are called to act against their commercial interests.

This Article analyzes the viability of private exchange governance as a mode of oversight in crypto markets. It makes three points. First, like traditional platforms, crypto exchanges represent essential actors within the growing ecosystem with distinctive expertise, sophistication, network effects and the capacity to exclude malicious players from a critical resource. Secondly, crypto exchanges have powerful incentives to provide quality oversight. Importantly, crypto exchanges diverge from their traditional counterparts in the degree of centralization they institutionalize. Whereas traditional exchanges rely on networks of intermediaries like clearinghouses and custodians to support trading, crypto exchanges generally internalize these functions in-house. By maintaining various layers of trading and settlement within their firm, they cannot externalize risk and thus have a lot to lose by allowing weak oversight and indiscipline on their platform. Thirdly, this Article examines the drawbacks of crypto exchange oversight by identifying unique aspects of crypto exchange design that can work to stymie sound supervision and policing. Notably, crypto exchanges have evolved to offer a suite of complex and innovative products to their users that can lower their incentives to undertake intense enforcement. Further, their costs of supervision are high, further limiting their incentives to act. In particular, widespread use of off-chain settlement on exchange-trades, and the resulting incompleteness of underlying blockchains, increases the information costs facing exchanges and introduces insurmountable data gaps that exchanges cannot fill without thick cooperation across venues.

In concluding, this Article explores pathways to increase the incentives for crypto-exchange oversight. It focuses on a number of tools, including the development of private industry standards for exchange governance, a liability regime for exchanges that fail to exercise sound discipline of their venues, and the development of an oversight regime for exchanges themselves to set core standards for crypto-exchange supervision.