Bakkt Holdings, Inc. (NYSE: BKKT)

General Counsel Highlights Bakkt’s Strong Positioning in an Evolving Regulatory Environment

KEY POINTS

• On February 15, WTR held a fireside chat with Bakkt General Counsel and Secretary Marc D’Annunzio. The conversation can be accessed on demand.

• D’Annunzio highlighted how Bakkt, being born out of Intercontinental Exchange, provides strong infrastructure and pedigree for operating in highly regulated financial markets. This core competency in regulation and process positions Bakkt well for a more regulated crypto market.

• D’Annunzio talked about how the industry in the US is working to grapple legally with what a crypto bankruptcy looks like. Bakkt has designed its platform in a way that maximizes client protection because it mirrors a lot of the traditional financial infrastructure.

• D’Annunzio is currently focused on the regulatory elements of three key efforts. The first is the regulatory approval of the Apex Crypto acquisition, which is expected to be transformational for Bakkt. It will allow the company to scale much more quickly and accelerate its product roadmap.

• The second effort is signing new partners to bring Bakkt’s products to market. As D’Annunzio mentioned, it is certainly the case that the events in the crypto markets over the last several months have caused trepidation, maybe the classic fear, uncertainty, and doubt. Bakkt is still seeing interest in crypto from prospective clients and its regulatory foundation is key to new partners trusting it.

• The third effort is a full-scale government relations effort. Bakkt is meeting with legislators on Capitol Hill and with the various regulatory bodies that touch or want to touch crypto.

KEY STATISTICS

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Source: YCharts, as of February 17, 2023

COMPANY OVERVIEW

Bakkt was formed in 2018, with a vision to connect the digital economy. Its platform operates at the intersection of cryptocurrency (“crypto”), loyalty and rewards, and payments. It is uniquely positioned to enable consumers, brands, and financial institutions to better manage, transact with, and monetize those assets in exciting new ways.

Bakkt’s institutional-grade technology platform is at the core of everything it does. It has thoughtfully built a unique and powerful platform, melding together institutional-grade loyalty services to complement its crypto capabilities.

The Bakkt platform provides end-to-end services for its partners, which includes easily digestible technology services, 24/7 customer support, and marketing playbooks. Bakkt’s customers include consumers, businesses, and institutions.

Businesses leverage Bakkt’s crypto-related capabilities to facilitate new assets acquisition and rewards opportunities for their customers. Its loyalty-related capabilities help businesses deepen their relationships with their customers. Bakkt enables institutions to trade crypto using Bitcoin futures contracts that are traded and cleared on ICE and to store Bitcoin and Ether securely in its custody warehouse.
Marc D’Annunzio has served as General Counsel and Secretary since the Closing. Prior to this role, Mr. D’Annunzio served as General Counsel and Secretary for Opco since May 2019. Mr. D’Annunzio is responsible for our legal, regulatory, compliance and governance matters. Mr. D’Annunzio joined Opco in May 2019 from Alston & Bird LLP, an international law firm, where he practiced in its Payments group. Mr. D’Annunzio has more than 25 years of experience in the payments and loyalty industries, focusing on M&A transactions, strategic alliances, complex commercial relationships (including co-branded and private label card programs, and processing relationships for leading retailers), new product launches, and compliance. He holds a Juris Doctor and a Bachelor of Arts in Economics and History, each from the University of Michigan.
EXECUTIVE DISCUSSION

John Roy: Welcome everyone. I’m Dr. John Roy, Managing Director at Water Tower Research. I’m very pleased today to have the General Counsel and Secretary of Bakkt, Marc D’Annunzio.

For those who don’t know you, could give us your background and what drove you to join Bakkt?

Marc D’Annunzio: I’ve been at Bakkt almost four years, not long after the company closed its initial financing round, as the first General Counsel.

Prior to that, I spent nearly 25 years working in the payments and loyalty business as outside counsel to banks, merchants, transaction processors, retailers, in a lot of different commercial capacities, M&A transactions, large commercial relationships like co-branded card, loyalty card deals, new product launches, international expansion, you name it.

A couple of things drew me to Bakkt. One is really what remains today, which is that I believe that crypto has a lot of transformational potential that frankly traditional financial products have a hard time replicating.

The second thing, which is just as important, is that being born out of Intercontinental Exchange, which operates the New York Stock Exchange and commodities exchanges and clearing houses around the world, made this proposition different to me. The proposition in 2019 was not different than the way that we think about it today, which is that the potential that I’m talking about can only be harnessed and developed in a framework that is clear to consumers, partners, and market participants. Offering these solutions in a regulated and transparent manner is the way that the space is going to move forward.

ICE obviously has decades of experience working in regulated industries, understands those spaces, and understands what traditional investors like and want to see with financial products.

It felt to me and still does today that Bakkt offered maybe the best chance for commercializing those solutions across a broader marketplace and seeing what’s possible within the sector.

John Roy: What have you been working on recently? What’s been keeping you busy? Is it more regulation? Obviously, you guys have announced that you’re going to acquire Apex Crypto.

Marc D’Annunzio: Busy is a relative term in crypto. To say that we’re busy today is certainly a true statement. But I would say three things. As you mentioned, the Apex Crypto acquisition that we announced in November has yet to close, which is not unexpected.

We have got to get regulatory approval from the states that regulate both Bakkt and Apex Crypto, which are effectively all of them.

We’re working through that process diligently. It’s a complicated process. It involves talking to a lot of different regulators about the transaction. But we’re focused on getting it done as quickly as we can and are optimistic that we’ll be able to do that. We’re excited.

The Apex acquisition is going to be transformational for this company. It’s going to allow us to scale much more quickly and accelerate the product roadmap that we’ve already talked about in our public disclosures. We’re looking forward to getting that wrapped up and integrating that business and getting forward.

The second thing is we’re signing new partners to bring our products to market. It is certainly the case that the events in the crypto markets over the last several months have caused trepidation, maybe the classic fear, uncertainty, and doubt.

But what we are seeing, particularly among the partners that we talked to, is that there’s still a lot of interest. They have a lot of interest in crypto. Their consumers have a lot of interest in crypto. If anything, I think they’re just doubly committed to making sure that engagement with crypto is safe and secure. We’re continuing to meet with prospects with the goal of getting them signed and activating those solutions.

The third thing, as you pointed out, is regulation. In recent months, we have begun in earnest, what I would call a full-scale government relations effort. We’re meeting with legislators on Capitol Hill.
We’re also meeting with the various regulatory bodies that touch or want to touch crypto for a couple of reasons. Number one, we think it’s important that they understand who we are and how we come to market and understand our emphasis on security, regulation, and compliance and exposing consumers to crypto in a way that is reliable and safe.

There’s a very active discussion that’s going on about what crypto is, how it should be regulated, who should regulate it, and how quickly that framework can be put into place.

We think we have some important views on all of that and we want to position ourselves as a resource to lawmakers and regulators alike as they grapple a lot of complicated issues in trying to bring a more logical and concise framework to bear for the industry.

We’re in a very early stage with a lot of those discussions, but they’ve gone very positively, and it gives me a lot of optimism that we’re headed in a positive direction.

**John Roy:** How are you guys currently regulated? You have a lot of measures in place already to protect consumers and obviously their crypto?

**Marc D’Annunzio:** We do. I think it’s safe to say that our approach has always been that we want to be as regulated as comprehensively as we can be at any moment in time. Today that looks like a couple of things. Number one, we have an entity, Bakkt Marketplace, which operates the consumer-facing crypto functionality that we embed inside of partner platforms.

Bakkt Marketplace holds a virtual currency license, or BitLicense, as folks like to call it from the State of New York. It’s regulated by the New York Department of Financial Services (NYDFS). It also holds money transmitter licenses broadly throughout the US from virtually every state, which today is how that business generally is regulated.

In addition to Marketplace, we also provide custody through a separate entity in the Bakkt corporate family. That entity, Bakkt Trust Company, is a limited purpose trust company, a single-purpose custody operation that itself is also regulated by the NYDFS.

That entity only does custody, has its own board of directors, and has its own audits and examinations that are specific to the custody function, so separate and apart from the consumer-facing business that Bakkt Marketplace conducts.

From our perspective and the audience may be familiar, there’s obviously a lot being said about crypto in the current environment. But one of the things that Chair Gensler of the SEC has said is that separating exchange functionality from custodian functionality is a very important feature and one that he believes crypto businesses ought to adopt.

We already have that and that is not by accident. I think a lot of the benefit of coming out of ICE is that we had very sage advice as to what traditional financial markets look like and the protections and features that institutional investors like and want to see, and that’s one of them.

In addition to the licenses that I’ve talked about, there are lots of other features about the company and our platform that we think are really best-in-class. That’s not to say that they’re going to be exactly what a new regulatory framework might demand. But based on what exists today, we think we’re well positioned.

I talked about the separate exchange in custody functions. We have regular examinations and audits, SOC 1, SOC 2, you name it. We also, by virtue of the parent company, Bakkt Holdings, being a publicly listed company traded on the New York Stock Exchange, have all the same protections for investors that all public companies have.

We file quarterly and annual financial statements. We have an annual shareholder meeting. Our CEO and CFO, obviously, personally sign the reports that they are required to under Sarbanes-Oxley.

We have internal audit and risk functionalities typical of publicly traded companies, audited financial statements. A lot of additional features that in recent months, you see crypto investors asking for such as, "How do I know that you have reserves? Tell me more about that? What can your auditors produce?" What our auditors produce is what all public company auditors produce, which is what we have to file with the SEC.
In addition to that, there are other features of our platform that we have designed in a manner to give comfort to the partners and consumers that we serve. We are only now in the US beginning to grapple legally with what a crypto bankruptcy looks like. There’s been a lot of concern with some of the other companies about whether investors’ crypto will be respected in the bankruptcy and whether can or will be returned to them.

We’ve designed our platform in a way that we think maximizes those protections because it mirrors a lot of the traditional financial infrastructure. Our consumer terms of use are very clear.

We don’t use consumers’ crypto for lending, hypothecating, or pledging, and we make it clear in those terms that it’s the consumers’ crypto and not our own. We account for it differently on the balance sheet. We also have other features.

We have built into our platform what we call an internal market maker, which effectively is a software engine that is continually monitoring other trusted crypto marketplaces to make sure that the price that we offer customers who transact on our platform is a good price.

It’s a reliable price that comes from somewhere that we can defend. We have a leading syndicate offering cold and warm wallet insurance coverage for crypto that is stored in our custody operation. All the crypto that we offer to consumers, we sell custody. We have control over how it is stored and we have insurance that protects it.

So again, I think there are a lot of features that we think are well designed given the current environment to offer that kind of safety and protection to our partners and to our consumers.

That being said, there’s a ton of discussion about what a new structure might look like. We’re monitoring that. We’re staying abreast of that. Obviously, as the rules change, I think we’re going to be very eager to be a part of that discussion and, ultimately, to be in compliance with whatever new framework may emerge.

John Roy: Speaking of that new framework, what is the current regulatory landscape for crypto and what’s the latest coming out of DC?

Marc D’Annunzio: Yes. It’s active and uncertain.

John Roy: You’re busy.

Marc D’Annunzio: Right. Obviously, what we’ve got is a couple of different things. Congress is evaluating what it needs to do. We are obviously operating in a political environment that is divided. You have a divided Congress and you have a complicated subject matter. These things usually take a while to figure out.

I think Congress is trying to figure out does it need to grant authority to specific agencies to ensure appropriate regulation. There are bipartisan talks around stable coins and trading platforms and consumer protection. Maybe at a high level, all of that is developing. We’ve been a part of that conversation.

At the same time, the regulators are not necessarily waiting for that before they take action. The SEC, in particular, has generated a lot of headlines, certainly in recent months, primarily through enforcement actions that it has taken against crypto companies. There was another one last week around staking.

One of the other things that gets lost a little bit, at least in the crypto industry, is that the CFTC is also very active. More than 20% of the CFTC’s enforcement actions last year had to do with crypto. That doesn’t really show any signs of abating.

Beyond that, because of the verticals that we serve, which include financial institutions, we are also exposed to other regulators. There was recently a joint statement among the Fed, the OCC, the FDIC, all bank regulators that talk about what those regulators want the banks that they regulate, to check off with the regulator before they engage in crypto-related activities, which is a broad definition.

Some would say that this is because there is a legislative vacuum, but the regulators are certainly speaking up and taking action within the authority that they believe that they currently have. The reason that I say that it’s uncertain is because I don’t think it’s been sufficiently resolved who’s able to do what exactly.

You have a little bit of a frenzy because a lot of different regulators care about a lot of the same themes. They have different ways of evidencing that concern. We see a lot of activity, but I’m not
sure that it’s going forward in the most logical way given that there is still an overall framework that could be filled in.

**John Roy:** The regulators are doing some things in the vacuum. Are you meeting with them regularly? Is that something that you guys do a lot with regulators?

**Marc D’Annunzio:** We are meeting both with legislators and regulators. If we start with Capitol Hill, as I said, we have had a number of discussions, and we’ll be continuing those very actively over the coming months.

From those discussions, I think there are a couple of themes that have really resonated and have come out of them. One is that the legislators that we’ve met with are all saying that crypto is not going away.

We see significant interest from partners. Obviously, consumers are still interested. What’s different is you can’t pick up a metaphorical newspaper and read these headlines without having more trepidation about engaging with crypto.

If you don’t know if you’re ever going to see it again, if the company goes bankrupt, obviously, that creates some doubts. What we have seen is that the market is growing up in a way that people are asking about protections that they didn’t really ask about a couple of years ago in a bull market when everything went up.

I believe that a clearer, more comprehensive regulatory framework would help really address some of that uncertainty that we’re seeing in the marketplace. That’s the first thing.

The second thing is that, as I think the FTX debacle has shown, legislators putting their head in the sand is not really a viable alternative because companies will go offshore where there are fewer rules to comply with and consumers will still interact with those platforms. If something bad happens, then something bad happens to American consumers, which ultimately is not in Congress’ interest. I think there’s a realization that action is, in fact, necessary.

The third thing is that we started off this conversation by talking about some of the transformative potential that I think crypto offers. A lot of what people tend to get caught up in is all of the neat use cases that crypto offers, the traditional financial products either cannot offer or have a harder time offering because of their structure. That is all true.

But I also think that that legislators are realizing that some of the failures that have happened over recent months don’t have much to do with any of that. They’re not crypto-specific failures. You’re talking about things like financial statement for all our commingling assets or lack of disclosure consumers about what they’re buying and what the rules are around what they’re buying. And so there are very basic kind of financial markets 101 level issues that need to be addressed at a very basic level.

My own personal view is let’s get that right. Then we can worry about the things that are unique to crypto. But there are lots of things that are not and there are lots of holes in the approach today that probably need to be patched. For purposes of legislative meetings, absolutely. We also have regular interactions with our regulators. As I said, we’re regulated pretty much by every state in the country and so that implicates lots of periodic audits and examinations and ratings and the like.

It also implicates when we do transactions like the Apex transaction and getting consent for that. That involves talking to a regulator about what our future business plan is going to look like once the Apex Crypto business is integrated. It’s a very active and lively dialogue, which candidly is how we like it.

I think based on the way that we think about the business and the way that we go to market, we like to have those discussions because it helps us really advance the proposition that this is how we do business and this is part of the hallmark of the platform that we’ve built.

**John Roy:** What is Bakkt doing about the current environment? There’s so much regulatory uncertainty. Are you being proactive with this?

**Marc D’Annunzio:** Yes. As I said, we are having very regular conversations with legislators and regulators alike. But look, I think we’re focusing a lot of effort on it because we know how important it is for the US to develop a well-thought-out comprehensive and transparent framework for crypto and digital assets.
As I said, I think the potential for getting that wrong or in action is that it takes innovation out of the US into foreign markets. In the last week, both Australia and the UK have put out consultation papers that ask for comment. The early sort of read that we’ve taken from that is that they are thinking about regulation the same way that we are, which is that it is more a function of adapting the existing frameworks to fit crypto than it is crumpling everything up and starting with a blank sheet of paper. But it also shows that those jurisdictions are being very serious about regulating crypto in a thoughtful way.

I think that really puts the onus on the US to do something and to do something sooner rather than later because otherwise I fear that the innovation will happen elsewhere. I don’t think that’s in the best interest of consumers here or the country generally. We really want to see that innovation continue to stay home and want to be a part of the conversation.

**John Roy:** When do you think you’re going to get more clarity? What do you think it will do to help settle everybody down and get people more confidence at crypto is definitely secure, well regulated, under control.

**Marc D’Annunzio:** I mean the second question is much easier to answer than the first. I think it will do a lot. I think it is almost really a condition precedent. It’s the lawyer in me talking to the space developing in the way that it can and it should. Until that clarity comes, certainly on the basis of our experience, it’s just hard to convince people to really engage in crypto in the manner in which they can.

As to when that comes, that’s a harder question. As I say, these are complicated issues that involve a lot of different traditional definitions and agencies, and we’re talking about something new that is a little bit of a square peg, no matter which way you try to put it in and the political environment certainly is not to be ignored.

But again, I think that our experience with the conversations we’ve had so far is that there are a lot of legislators that are well educated about this. They’re educating about the technology. They’re educating about the potential. I think they’re very concerned about getting this right, not just for consumers but for the country, generally.

I’m optimistic. I think the company is optimistic that it will get it right. It will be able to preserve what’s new and transformative about crypto, while still injecting the comfort and the security that frankly the space deserves and that it will require if the innovation is going to happen.

The other thing I would say is that the thing that I try to remember is that Congress and regulators to a significant degree are inherently reactive. The reform tends to follow, certainly in the financial services sector. Reform tends to follow some sort of scandal or crisis or failing and FTX is certainly the case. FTX and the associated failures in crypto have created a lot more urgency to do something because I think everyone understands what happens when you don’t.

What we have seen, though, is that despite those partisan divisions in Washington, there is good evidence that there could be and should be bipartisan agreement. Bipartisan agreement on these issues in the future and hopefully in the very near future. We think it’s important for the space and, again, we are excited to be part of those conversations, which we hope move swiftly.

**John Roy:** You would think that this Congress would want to win?

**Marc D’Annunzio:** Yes, I certainly think that they should, but we’ll see where it goes. I mean, if this were easy, it would have all been done already, and it’s not easy and it involves a lot of stakeholders and a lot of concerns, but it’s certainly not impossible.

My own view is that the US is the leading financial market in the world for a reason. That reason is that we have been successful in preserving innovation and preserving a path forward for development of new technologies and new products and services, while still offering that sort of baseline protection that you kind of need. It’s a different use case for sure, but I’m confident that we can get that right.

**John Roy:** Well, Mark, thank you so much. Investors, if you have any questions, just let us know, and we’ll get them answered. Thanks and have a great day.

**Marc D’Annunzio:** Thanks John. Appreciate it.
In his role at Water Tower Research, Dr. Roy provides cutting-edge equity research coverage of companies building and using technology to drive the modern world. Technology is everywhere, and its impact is only growing. Whether its AI, Blockchain, FinTech, Quantum Computing, Autonomous Vehicles, Cryptocurrencies, or 5G, Dr. Roy has the expertise.

Prior to Water Tower Research, Dr. Roy worked as a lead analyst at UBS, covering IT Hardware, Communications Equipment, and IT Services. During his 20 years covering technology stocks on the sell-side, Dr. Roy was also a lead analyst covering IT Hardware and Nanotechnology at Merrill Lynch; and Alternative Energy, Advanced Materials and Nanotechnology at W.R. Hambrecht, and at Janney Montgomery Scott. Before his sell-side equity research career, Dr. Roy was a lead software architect at J.P. Morgan, an AI sales engineer at Neuron Data, and a systems engineer and AI researcher at Hughes Aircraft.

Dr. Roy holds a Ph.D. in Computer Science from the University of California, Irvine, a MSEE degree from the University of Southern California, and a BSEE degree from the University of California, San Diego where he was a Regents Scholar.
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