

## Speech

---

# Prepared Remarks of Gary Gensler On Crypto Markets

## Penn Law Capital Markets Association Annual Conference



**Chair Gary Gensler**

**Washington D.C.**

**April 4, 2022**

Thank you. It's great to be with you all at this event, particularly as the University of Pennsylvania is my alma mater. I was over at Wharton, and what I knew of the law school is that the library stacks were a great place to study. It was so quiet there, though I don't know if that's still the case.

As is customary, I'd like to note that my views are my own, and I'm not speaking on behalf of the Commission or SEC staff.

Today, you've invited me to talk about the roughly \$2 trillion crypto markets.

In February, you all might have noticed Super Bowl ads for several crypto platforms. This wasn't the first time we'd seen some new innovations getting air time on the biggest TV event of the year.

Seeing these ads reminded me that, in the lead-up to the financial crisis, subprime lender AmeriQuest advertised in the Super Bowl. It went defunct in 2007. A few years before that, according to Axios, "Fourteen dotcom companies advertised during the 2000 Super Bowl, most of which are now defunct."<sup>[1]</sup> I know many in the audience may just have been young children at the time, but the internet was relatively new back in 2000. The dot-com bubble burst, though, created significant tremors in our markets.

Ads, thus, don't equal credibility. In crypto, there is lots of innovation, but plenty of hype. As in other start-up fields, many projects likely could fail. That's simply part of the entrepreneurial spirit in the U.S.

The SEC's remit is overseeing the capital markets and our three-part mission: protecting investors, facilitating capital formation, and maintaining fair, orderly, and efficient markets. Within the policy perimeter, regulators also care about guarding against illicit activity, a role that is so important to us and our partners at the Department of the Treasury and the Department of Justice; and about financial stability, which is important to all financial regulators.

There's no reason to treat the crypto market differently just because different technology is used. We should be technology-neutral.

So I'd like to mention three areas related to the SEC's work in this area: platforms, stablecoins, and crypto tokens.

### **Platforms**

First are the crypto trading and lending platforms, whether they call themselves centralized or decentralized (DeFi).

These platforms have scale, recently trading crypto worth more than \$100 billion a day.<sup>[2]</sup>

The crypto market is highly concentrated, with the bulk of trading taking place on only a handful of platforms. Amongst crypto-only exchanges, the top five platforms make up 99 percent of all trading, and just two platforms make up 80 percent of trading. In crypto-to-fiat transactions, 80 percent of trading is on five trading platforms.<sup>[3]</sup> Similarly, the top five DeFi platforms account for nearly 80 percent of trading on those platforms.<sup>[4]</sup>

Furthermore, these platforms likely are trading securities. A typical trading platform has dozens of tokens on it, at least. In fact, many have well in excess of 100 tokens. As I'll address later, many of the tokens trading on these platforms may well meet the definition of "securities." While each token's legal status depends on its own facts and circumstances, given the Commission's experience with various tokens that are securities, and with so many tokens trading, the probability is quite remote that any given platform has zero securities.

Thus, I've asked staff to work on a number of projects related to the platforms.

First is getting the platforms themselves registered and regulated much like exchanges. Congress gave us a broad framework with which to regulate exchanges. These crypto platforms play roles similar to those of traditional regulated exchanges. Thus, investors should be protected in the same way.

The U.S. has the greatest capital markets because investors have faith in them. We have rules with respect to safeguarding market integrity, protecting against fraud and manipulation, and facilitating capital formation. If a company builds a crypto market that protects investors and meets the gold standard of our market regulations, then customers will be more likely to trust and have greater confidence in that market.

In my view, regulation both protects investors and promotes investor confidence, in the same way that traffic laws protect drivers and promote driver confidence. It's at the core of what makes markets work.

Some have asked if the current exemptions for so-called alternative trading systems (ATs) could be generally available to crypto platforms. ATs for the equity and fixed income markets, though, are generally used by institutional investors. This is quite different than crypto asset platforms, which have millions and sometimes tens of millions of retail customers directly buying and selling on the platform without going through a broker. Thus, I've asked staff to consider whether and how the protections that are afforded to other investors on exchanges with which retail investors interact should apply to crypto platforms.

Second, crypto platforms currently list both crypto commodity tokens and crypto security tokens, including crypto tokens that are investment contracts and/or notes. Currently, the venues that the SEC oversees solely trade securities. Thus, I've asked staff to consider how best to register and regulate platforms where the trading of securities and non-securities is intertwined. In particular, I've asked staff to work with the Commodity Futures Trading Commission (CFTC) on how we jointly might address such platforms that might trade both crypto-based security tokens and some commodity tokens, using our respective authorities.

The third area is around crypto custody. Unlike traditional exchanges, currently centralized crypto trading platforms generally take custody of their customers' assets. Last year, more than \$14 billion of value was stolen.<sup>[5]</sup> I've asked staff how to work with platforms to get them registered and regulated and best ensure the protection of customers' assets, in particular whether it would be appropriate to segregate out custody.

Further, unlike traditional securities exchanges, crypto trading platforms also may act as market makers and thus as principals trading on their own platforms for their own accounts on the other side of their customers. I've thus

asked staff to consider whether it would be appropriate to segregate out market making functions.

As it relates to crypto lending platforms, we recently charged BlockFi with failing to register the offering of its retail crypto lending product, among other violations.<sup>[6]</sup> The settlement made clear that crypto markets must comply with time-tested securities laws, such as the Securities Act of 1933 and the Investment Company Act of 1940. It further demonstrates the Commission's willingness to work with crypto platforms to determine how they can come into compliance with those laws.

BlockFi agreed to attempt to bring its business into compliance with the Investment Company Act, and its parent company announced that it intends to register under the Securities Act of 1933 the offer and sale of a new lending product.

### **Stablecoins**

The second area is the \$183 billion (and growing) stablecoins market.<sup>[7]</sup> Outside of use on crypto platforms, stablecoins generally are not used for commerce. Generally, you're not using them to get a cup of coffee at Good Karma on your way to class from Center City. They are not issued by a central government and are not legal tender.

Stablecoins, though, in offering features similar to and potentially competing with bank deposits and money market funds, raise three important sets of policy issues.

First, stablecoins raise public policy considerations around financial stability and monetary policy. Such policy considerations underlie regulations that banking regulators have with respect to deposits and that we at the SEC have with respect to money market funds and other types of securities. Many of those issues are discussed in the recent President's Working Group Report.<sup>[8]</sup> For instance, what backs these tokens so we can make sure that these holdings can actually be converted to dollars one-to-one? Further, stablecoins are so integral to the crypto ecosystem that a loss of the peg or a failure of the issuer could imperil one or more trading platforms, and may reverberate across the wider crypto ecosystem.

Second, stablecoins raise issues on how they potentially can be used for illicit activity. Stablecoins primarily are used for crypto-to-crypto transactions, thus potentially facilitating platforms and users avoiding or deferring an on-ramp or off-ramp with the fiat banking system. Thus, the use of stablecoins on platforms may facilitate those seeking to sidestep a host of public policy goals connected to our traditional banking and financial system: anti-money laundering, tax compliance, sanctions, and the like.

Third, stablecoins raise issues for investor protection. Stablecoins were first adopted and continue to be dominantly used on crypto trading and lending platforms. About 80 to 85 percent of trading and lending on these platforms involves stablecoins. When trading on a platform, the tokens actually often are owned by the platforms, and the customers just have a counterparty relationship with the platform. The three largest stablecoins were created by trading or lending platforms themselves, and U.S. retail investors have no direct right of redemption for the two largest stablecoins by market capitalization. There are conflicts of interest and market integrity questions that would benefit from more oversight.

### **Tokens**

Then, thirdly from a policy perspective are all the other crypto tokens. The fact is, most crypto tokens involve a group of entrepreneurs raising money from the public in anticipation of profits — the hallmark of an investment contract or a security under our jurisdiction. Some, probably only a few, are like digital gold; they may not be securities. Even fewer, if any, are actually operating like money.

When a new technology comes along, our existing laws don't just go away.

In the 1930s, Congress painted with a broad brush the definition of a security. Our laws have been amended many times since then, Congress has painted with an even wider brush, and the Supreme Court has weighed in numerous times. They've all said, basically, to protect the public against fraud, to protect the public against

scammers, people raising money from the public had to register and make basic disclosures with a cop on the beat: the SEC.

You might wonder: how might a crypto token be a security?

The Supreme Court's 1946 Howey Test, which was about orange groves, says that an investment contract exists when there is the investment of money in a common enterprise with a reasonable expectation of profits to be derived from the efforts of others.<sup>[9]</sup>

My predecessor Jay Clayton said it, and I will reiterate it: Without prejudging any one token, most crypto tokens are investment contracts under the Howey Test. Even before the Howey test, in the first several years of our federal securities laws, some entrepreneurs were notified that they had to register their offerings of chinchillas, whiskey warehouse receipts, oyster beds, and live silver foxes as securities offerings,<sup>[10]</sup> as "the purported sale of the... property was merely camouflage and not the substance of the transaction."<sup>[11]</sup>

Today, many entrepreneurs are raising money from the public by selling crypto tokens, with the expectation that the managers will build an ecosystem where the token is useful and which will draw more users to the project.

Thus, it is important that we work to get crypto tokens that are securities to be registered with the SEC. Issuers of crypto tokens that are securities must register their offers and sales of these assets with the SEC and comply with our disclosure requirements, or meet an exemption. Issuers of all kinds across a variety of markets successfully register and provide disclosures every day. If there are, in fact, forms or disclosure with which crypto assets truly cannot comply, our staff is here to discuss and evaluate those concerns. Any token that is a security must play by the same market integrity rulebook as other securities under our laws.

### Conclusion

In conclusion, new technologies come along all the time; the question is how we adjust to that new technology. But make no mistake: We already live in a digital age. That's not what's new here. We already can buy a cup of coffee with money stored in an app on our smartphones. The days of physical stock certificates ended decades ago. There's nothing new about people raising money to fund their projects. Crypto may offer new ways for entrepreneurs to raise capital and for investors to trade, but we still need investor and market protection.

We already have robust ways to protect investors trading on platforms. And we have robust ways to protect investors when entrepreneurs want to raise money from the public.

We ought to apply these same protections in the crypto markets. Let's not risk undermining 90 years of securities laws and create some regulatory arbitrage or loopholes.

Thank you.

---

[1] See "No crypto champs crowned during Super Bowl" (Feb. 15, 2022), *available at* <https://www.axios.com/crypto-super-bowl-ads-532f2a00-25e5-43c1-8e01-82198a2467bc.html>.

[2] See CoinMarketCap, *available at* [www.coinmarketcap.com](http://www.coinmarketcap.com).

[3] See The Block, *available at* <https://www.theblockcrypto.com/data/crypto-markets/spot>.

[4] See The Block, *available at* <https://www.theblockcrypto.com/data/decentralized-finance/dex-non-custodial>.

[5] See Chainalysis, "Crypto Crime Trends for 2022: Illicit Transaction Activity Reaches All-Time High in Value, All-Time Low in Share of All Cryptocurrency Activity" (Jan. 6, 2022), *available at* <https://blog.chainalysis.com/reports/2022-crypto-crime-report-introduction/>.

[6] See SEC, "BlockFi Agrees to Pay \$100 Million in Penalties and Pursue Registration of its Crypto Lending Product" (Feb. 14, 2022), *available at* <https://www.sec.gov/news/press-release/2022-26>.

[7] See The Block, *available at* <https://www.theblockcrypto.com/data/decentralized-finance/stablecoins>.

[8] See The President's Working Group on Financial Markets, the Federal Depository Insurance Corporation, and the Office of the Comptroller of the Currency, "Report on Stablecoins" (Nov. 2021), *available at* [https://home.treasury.gov/system/files/136/StableCoinReport\\_Nov1\\_508.pdf](https://home.treasury.gov/system/files/136/StableCoinReport_Nov1_508.pdf).

[9] See SEC, "Framework for 'Investment Contract' Analysis of Digital Assets," *available at* <https://www.sec.gov/corpfin/framework-investment-contract-analysis-digital-assets>.

[10] See New York Times, "Asks SEC Registry of 480 Chinchillas" (July 5, 1940), *available at* <https://timesmachine.nytimes.com/timesmachine/1940/07/06/113098735.html?pageNumber=19>.

[11] See "Sixth Annual Report of the Securities and Exchange Commission" (Fiscal Year Ended June 30, 1940), *available at* [https://www.sec.gov/about/annual\\_report/1940.pdf](https://www.sec.gov/about/annual_report/1940.pdf).