

WRITTEN STATEMENT OF

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BEFORE THE U.S. HOUSE FINANCIAL SERVICES COMMITTEE'S
SUBCOMMITTEE ON DIGITAL ASSETS, FINANCIAL TECHNOLOGY,
AND INCLUSION AND THE HOUSE AGRICULTURE COMMITTEE'S
SUBCOMMITTEE ON COMMODITY MARKETS, DIGITAL ASSETS, AND
RURAL DEVELOPMENT

“The Future of Digital Assets: Measuring the Regulatory Gaps in the Digital Asset Market
Structure”

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Thank you, Committee Chairmen McHenry and Thompson, Ranking Members Waters, Lynch, Scott; Subcommittee Chairmen Hill and Johnson, Ranking Member Caraveo, and esteemed members of the Subcommittee for the honor of testifying before you today. My name is Andrew Durgee, and I am an Executive Vice President of OpenDeal Inc., doing business as Republic and a co-founder of its Web3 and blockchain technology cryptocurrency business lines known under the umbrella brand of “Republic Crypto”. In these capacities I oversee Republic’s strategic vision with respect to Web3 technology, as well as sit on various corporate boards as a fiduciary.

Before delving into the substance of regulatory policy with respect to digital assets and for the cryptocurrencies, permit me to tell you more about my background and Republic.

I was born to teenage parents in South Florida. I was fortunate enough to get a scholarship to Saint Andrew’s High School in Boca Raton, Florida. Then I received a scholarship to Worcester Polytechnic Institute in Worcester, Massachusetts where I studied management engineering. I have been in the blockchain industry for over a decade. I was a CEO and Co-Founder of The Coin Tree, one of the first companies working on multi signature security solutions for bitcoin. I later became a partner at TLDR Capital, where we were one of the premier global web3 advisory platforms. I joined Republic in early 2019 to build out Republic Crypto as the first vertically integrated crypto investment bank.

Republic is a global technology firm pioneering the digital transformation of finance. Republic operates prominent private, regulated, investing platforms, making it possible for 2.5+ million community members across 150+ countries to access private market investment opportunities. Combined with our private capital and web3 divisions, Republic unites ambitious builders and investors, empowering them to shape the future.

Today’s hearing builds off prior sessions, including last month’s April 27th hearings, when your Committees heard from business leaders, attorneys and policy advisors. Those earlier hearings were focused on “Measuring the Regulatory Gaps.” But there is another gap relevant to digital assets and cryptocurrencies that I would like to briefly mention: wealth inequality.

Wealth inequality is a global crisis which is particularly acute in the United States; never before has there been such a gap, which can be seen in the current economic realities, steady inflation, moderate job-growth but stagnating wages. Republic’s underlying business goal is to close the gap in ways that are productive, rather than charitable. Through the start of 2023, Republic’s community of users, co-investors, and partners has deployed more than \$2.5 billion into 2,000+ private ventures and projects.

When Republic was founded in 2016, it became one of the first companies to harness the potential of the JOBS Act for investors of all kinds, enabling startup founders to raise capital directly from their communities—and for investors across the world to discover and invest in companies and visions they believed in. In seven years, Republic’s Retail business line,

“Republic Retail”, has helped over 350 businesses raise capital, more than 40 of which have raised over \$1 million, and 14 of which have raised the maximum of \$5 million under recently expanded SEC crowdfunding rules. Republic recently acquired the leading crowdfunding platform and private secondary market in Europe, Seedrs, which is based out of the United Kingdom, to take this mission global.

Where Republic Retail has met the needs of a fast-growing audience of retail investors, the “Republic Capital” business line has supported family offices, high net worth individuals, and other institutional investors with primarily growth-stage investment opportunities. Since its inception in 2017, Republic Capital has facilitated over \$610 million in investments through the end of 2022. It has deployed capital into more than 120 syndicates, and launched multiple closed-ended funds—often co-investing alongside top-tier venture firms like a16z, Founders Fund, and Tribe Capital. With a broad investment strategy across technology, space, and blockchain, some of the most notable investments Republic Capital manages include SpaceX, Avalanche, and Carta.

Independently, these pillars have grown immensely. In 2017, its first full year of operation, Republic Retail facilitated a total investment volume of approximately \$4 million. Since then, this figure has about doubled each year—reaching \$7.8 million in 2018, \$19.5 million in 2019, and \$38.5 million in 2020, the same year the first Republic Note offering open to the public was conducted. In the following two years, the gross transaction volume totaled over \$160 million. Similarly, Republic Capital has grown to manage close to \$1 billion in assets, which include investments in blue-chip space tech brands like Axiom and Firefly.

Republic Crypto, which I lead, offers a range of services that combine to accelerate the growth of web3. It started as an advisory firm, now offers full-fledged blockchain infrastructure solutions, as well as operates an institutional digital asset management division. Our advisory arm is composed of world-class strategists who design digital asset economies, engineer smart contracts, and support public digital asset offerings. We also build and operate blockchain infrastructure, participating in the security of many of the ecosystem’s top protocols. Additionally, Republic Crypto’s digital asset management division helps guide institutional investors through this fast-evolving industry.

Given its founder’s prior career as an attorney, regulatory compliance has long been woven into Republic’s corporate DNA. As the business has become more complex in structure, understandably, a supportive (but complex) legal structure has developed in parallel. Underlying Republic are several semi-autonomous subsidiaries, some with licenses to conduct offerings and sales of securities to both non-accredited and accredited persons in the United States. They include a funding portal, an investment adviser, and a broker-dealer—all of which are subject to oversight by the US Securities and Exchange Commission (SEC) and the Financial Industry Regulatory Authority (FINRA). Republic’s European operations are regulated by the UK Financial Conduct Authority and other subsidiaries are registered with other regulatory agencies.

Across our family of companies, every team member at Republic plays an instrumental role in implementing and growing our digital asset ecosystem. Ours is a group with deep and diverse experience across investments, blockchain, law, engineering, and community building. The Republic team of over 300 full-time team members honed their expertise at reputable tech startups, respected law firms, and leading financial institutions. We are devoted to keeping jobs in the United States and continue positioning our country as the leader of the rapidly evolving digital assets ecosystem. Although recent reports suggesting a ~20% year-over-year drop in US-based protocol developers concern us, Republic remains committed to working with legislators and regulators to propose sensible legislation to prevent a mass offshore exodus and position our country for long term worldwide leadership in crypto.

Republic is perhaps best known as a primary offerings platform, holding coveted regulatory licenses and supporting personnel and infrastructure that enables other companies, mostly early stage companies - startups - to raise capital from the crowd (e.g retail investors) as well as accredited and institutional investors. In short, Republic has two types of end-users, as a founder or executive, you come to Republic to raise money, and as an investor, you come to Republic to find compelling investment opportunities.

Raising money from the crowd under the JOBS Act Regulation Crowd Funding (Reg CF) or Reg A+ is a powerful means of access for those typically left out of some of the greatest forms of wealth creation in the history of the world, venture capital. Before Reg CF, it was almost impossible for a non-accredited investor to invest in private companies, only widening the gap in wealth inequality. Reg CF changes that. In the venture and startup world, the founders and their teams seek to solve a problem or gap in the market. Like these entrepreneurs, you too, members sitting members here today, have the potential to be innovators and visionaries solving a much bigger problem than any one startup does. It is regulatory innovations such as Reg CF that can propel economic well-being and opportunity for all.

Turning to the substance of the hearing, I would like to reiterate that I share the views of those testifying here today and in past hearings who have identified that not all digital assets should be treated as securities throughout their lifecycle, that there is a need for other agencies to regulate digital assets when they are not considered securities. in addition to the SEC, that there is a need for trusted intermediaries, and that innovation should not be regulated out of the United States.

Honorable Members of Congress,

Allow me to provide you with an overview of the three main paths for registering or qualifying a digital asset offering for a registration exemption that includes non-accredited investors under the Securities Act of 1933 (the "1933 Act"). These include qualification, which is not the same level of SEC vetting as a registration, but it does involve significant

vetting. The qualification path includes registration under Regulation A+ pursuant to Form 1-A. Under this path, a company can raise no more than \$75,000,000 in any 12-month period. An offering under a typical IPO by a domestic issuer on Form S-1, and an IPO by a foreign issuer on Form F-1. These registrations do not have fundraising caps but they have material costs to complete and costs associated with continued reporting thereafter.

Reg CF is an exemption from registration and is neither a qualification nor a registration. The SEC does not review offerings pursuant to Reg CF deals, but a public informational filing is made and the registered intermediary, such as a registered crowdfunding portal like Republic. The registered intermediary provides a level of due diligence on the company making the offering and facilitates the offer and sale to ensure investors invest within their investment limits and understand the risks and rewards of private investing. What makes Reg CF so important is the ability for retail investors to participate and for issuers to be able to access the crowd with minimal external or recurring costs, provided there is a trusted intermediary facilitating the deal. To expand access in a regulated market,, expand the crowdfunding cap from \$5 million to \$10 million. Doing so does not increase risk to investors, in fact it may reduce risk by allowing projects to receive larger amounts of funding to pursue their goals, and it makes Reg CF meaningfully more attractive for prospective users of the registration exemption.

For more sophisticated projects or those in need of greater amounts of funds, Reg A+ may be a viable option; Reg A+ currently allows an issuer to raise up to \$75M per annum. To qualify an offering like a Reg A or register an offering, the issuer is required to fill out the appropriate form and submit it to the SEC with other necessary documents, including at least two years of financial statements. The SEC will then review the submission and provide comments that must be addressed through written answers and subsequent amendments to the filed forms. Only after the SEC's comments are fully addressed, and the form is deemed "effective" or "qualified," can the issuer begin selling the securities. For a brief period the SEC was actively doing this with respect to digital assets, however, the current Administration has not qualified a single digital asset offering.

Seeking to provide clarity on the initial issuance and ongoing regulatory status of digital assets, a group of attorneys active in the cryptocurrency and digital asset space drafted an exemption, inspired by Hester Pierce's Safe Harbor. The exemption for offerings and the framework for secondary market disclosure may provide a way to extend the public policy framework of securities laws to digital asset issuances. This could enable the facilitation of capital formation and peer-to-peer transactions while minimizing opportunities for issuers to exploit differences in laws around exempt securities offerings. The focus on issuer disclosures would be retained, but adjusted as necessary to account for the unique risks posed by these decentralized models. The proposed framework would also clarify which digital asset issuances fall beyond the scope of securities laws, subject to specific conditions. Secondary market disclosure requirements would be put in place, with a focus

on insiders, points of control and centralization, and large holders in the market. Additionally, the traditional securities law focus on ongoing issuer reporting obligations, protections for retail investors, and enforcement against bad actors would be maintained. Finally, efforts would be made to harmonize how these assets and the proposed disclosure regime interact with existing securities laws and disclosures, including when a digital asset offering could trigger the registration of an Issuer's equity under Section 12(g) of the Exchange Act.

The exemption could cap the amount that accredited investors can invest. This is smart design to ensure that projects are decentralized. Because digital assets often carry voting features, the more concentrated the digital asset ownership is, the more centralized control over the system is. Furthermore, an exemption could reward decentralization by creating thresholds to meet in order to be exempt from 12(g) registration requirements.

I believe ideas like these should be looked at in crafting legislation and rulemaking to foster the growth of this ecosystem in a responsible manner.

It is worth noting that even if the digital asset distribution is exempt from the registration requirements of the 1933 Act, if the digital assets are deemed "equity" securities and the project meets certain minimum asset and holder requirements, they may still be required to register under the Securities Exchange Act of 1934 (the "1934 Act").

Digital assets registered as securities cannot be traded on existing crypto exchanges, none of which are registered as national securities exchanges, leaving a limited number of ATS platforms and OTC brokers as the primary means of trading. Furthermore, current regulations do not align with the inherently decentralized and disintermediated trading technology of blockchains, further complicating matters. Congress should instruct the SEC to adopt rules and procedures which allow intermediaries to act as brokers or exchanges with respect to digital assets which are securities and exempt parties dealing in non-securities from complying with such rules. In such cases, Congress should consider whether these forums should be regulated by the CFTC. Such potential jurisdictional overlaps call out for Congress to weigh in on, and the SEC must not overstep its bounds and create potentially conflicting regulatory regimes without Congressional direction.

In the traditional centralized model of business (TradFi), corporate enterprises operate in a hierarchical manner with directors and management acting as fiduciaries for shareholders. In this model, the existing regulatory regime effectively addresses the significant risks that come with raising capital.

However, in the decentralized operating models of the digital era, there is no corporate structure, directors, or shareholders. Users operate independently in response to incentive structures within software code, acting in concert in a decentralized fashion based on their

independent judgments and, in some cases, protocol voting rights. This high level of user involvement, self-custody and peer-to-peer transferability of digital assets, and the absence of formal legal entities and fiduciary relationships create entirely different risks. Unfortunately, existing securities law frameworks do not adequately address these risks.

Decentralized exchanges (DEXs) facilitate peer-to-peer transactions of digital assets. A user can exchange their digital asset, such as trading Bitcoin for Ether, without depositing assets with a central authority. DEXs use "smart contracts" to manage asset exchanges, building trust in transactions. Smart contracts autonomously enforce agreements, executing and recording transactions on the blockchain.

Smart contracts also help DEXs maintain liquidity for decentralized transactions. While centralized systems rely on broker-dealers for liquidity, DEXs use Automated Market Makers (AMMs), code-based protocols operating without intermediaries. AMMs incentivize pooling assets in a DEX's smart contracts by rewarding liquidity providers with digital assets representing transaction fees.

Once established, DEXs operate autonomously according to smart contracts and decentralized participation, without requiring a central organization. Decentralized exchange protocols allow trustless, disintermediated digital asset exchanges, forming a crucial foundation for the web3 ecosystem without any central points of failure.

However, due to a lack of legal and regulatory clarity, US-based developers of these promising decentralized autonomous organizations (DAOs) are often either operating them under foreign off-shore foundations or in an entity-less fashion. DAOs are key to the success of Web3 protocols as they provide benefits that help make them competitive against the centralized and vulnerable systems of Web2. Although multiple proposals to fix this have made their way in state legislatures, an overarching solution to keep them onshore is warranted.

Regarding secondary markets, we must also highlight a January 2022 SEC amendment proposal concerning national securities exchanges and alternative trading systems (ATS), accompanied by a strong dissent from Commissioner Hester Peirce. The primary aim of the proposal is to significantly broaden the scope of what constitutes a "securities exchange" and who is required to register as a "securities exchange" or "alternative trading system for securities." In doing so, the proposal would override previous SEC no-action letters and guidance that provided assurance that certain types of systems are not considered exchanges. SEC Chair Gensler's explanation is even more expansive, stating that the changes are intended "to cover platforms for all kinds of asset classes that bring together buyers and sellers." The proposed amendment has been reopened for comment last month. The Proposal mints a new term—"Communication Protocol Systems"—to describe the entities that offer communication protocols and the use of non-firm trading

interest to bring together buyers and sellers of securities. The Commission believes that the term “makes available” is more appropriate to describe these systems because they take a more passive role in providing participants with the means and protocols to interact, negotiate, and come to an agreement.

While the proposal does not mention blockchain, decentralized finance (DeFi), automatic market-making protocols (AMMs), etc., most believe the SEC staff intends for the expanded definition of “exchange” to capture AMMs and Defi, as securities exchanges. Yet the proposal offers no method of registration and reporting that could actually be followed by anyone who arguably “makes available” an AMM protocol or other DeFi system.

The technological operation of decentralized financial systems are not compatible with existing rules and compliance obligations for registered exchanges and ATSS. For instance, a prerequisite for a registered Alternative Trading System (ATS) involves identifying, monitoring, and reporting the orders of its users, referred to as "subscribers," to the SEC. However, it can be argued that entities that facilitate access to Automated Market Makers (AMMs) – whether they are considered miners, software providers, or front-end operators – lack access to such information. Moreover, these facilitators of AMMs, due to their lack of control over the AMMs, possess no means of guaranteeing that securities or digital assets essential to a securities scheme are not traded through the AMMs. Instead, this decision rests solely with the users of the AMMs.

As crypto attorney and legal commentator, Gabriel Shapiro notes, under the SEC’s proposed framework, however, the persons arguably "making available" AMMs could be more persuasively argued by the SEC to have exchange/ATS registration/reporting obligations because:

(a) participation as a liquidity provider in a particular AMM pool can potentially be argued to be a communication of trading interest regarding the digital assets (possibly securities) in that pool; and

(b) the AMM smart contract, or a website providing information about the protocol implemented within such AMM smart contract, can potentially be argued to be a COMMUNICATION PROTOCOL which brings together buyers and sellers through such communications of trading interest.

While there are no easy solutions to regulation technology that is fundamentally different from existing systems and adapting such new technology to existing rules and regulations, the starting point is to identify the component parts:

- The autonomous smart contract

- The deployers of the smart contract (software developers)
- The liquidity providers and AMMs
- The front end websites operator

These parties/components are not all the same. They are disintermediated and often decentralized. To the extent they are centralized, they are more likely to resemble an exchange or ATS, minus the different technology. However, in other instances, it is possible for all of the component parts to be unaffiliated. In those cases, it is clear that if a software developer deployed a smart contract and no longer is involved in its maintenance, they should not be swept into a regulatory compliance regime for an exchange or ATS. Perhaps, in the initial period, they might be able to provide certain transparency disclosures and there could be mandates for a certain standard of code auditing to mitigate the risk of the software code being exploited or hacked.

The smart contract itself, once deployed on the internet, is virtually impossible to stop. The “keys” to modify the contract are either “burned” upon deployment or transferred to governance digital asset holders. Liquidity providers would be able to access those smart contracts. Various industry participants have suggested KYC solutions, at the front-end level or even at the wallet level. These are hotly debated. Such solutions could provide a middle ground, but would not prevent the proliferation of wallets and front ends that do not require KYC to be used or to access a smart contract-based decentralized financial system.

We have seen a number of failures in the traditional financial system. Highly regulated commercial and investment banks failing in orders of magnitude that dwarf the exploits in crypto. Humans fail, and to be fair code developed by humans fail. However, the aim of crypto technology is not intended as the get-rich-quick schemes highlighted in the news. It is intended as an innovation and next iteration of the financial system. One that minimizes the need for trust in a middleman or middlewoman. You and I can send funds to each other and conduct complex financial trades like derivatives through software code that runs on its own. Margin can be automated, as can liquidations.

So proposed measures to regulate defi should include: code audits, transparency reports from the initial developers which would be sunset if they truly decentralize away from managing the technology, thresholds of digital asset ownership for those affiliated with the DeFi system, insurance funds, and perhaps a level of KYC if there is a centralized team that facilitates access to a decentralized system that enables securities trades. There would need to be a framework in which a DeFi system is so decentralized that regulatory obligations sunset off of a party and perhaps onto successor parties if needed..

The SEC must reassess and revise the proposal to explicitly clarify that its intent does not encompass prohibiting the development and implementation of code exclusively designed

for peer-to-peer digital asset trading or websites—including mere block explorers—that solely offer information about interactions that have transpired or could potentially transpire through such code, along with instructions on how to engage with the code. It is implausible for mere coders or website operators to register with FINRA, monitor the identities and transactions of AMM systems operating on decentralized autonomous blockchain systems, or otherwise adhere to the ATS or exchange reporting and registration framework. Consequently, if the new rule were applied to these individuals, it would effectively ban a vast range of technologies and free speech pertaining to those technologies, exceeding the SEC's jurisdiction and resulting in an unconstitutional infringement of our civil and human rights.

It is an undeniable fact that the lack of registered digital asset offerings in the United States is a result of the SEC's failure to provide actionable guidance, issue necessary rules, or engage constructively with the crypto industry to establish a feasible regulatory framework for security digital assets.

Let me provide you with a concrete example to illustrate this point. Even a public company with a class of shares registered with the SEC as prominent as Coinbase has struggled to navigate the regulatory landscape. In the summer of 2022, Coinbase submitted a rulemaking petition to the SEC seeking clarity on unresolved issues necessary for a functioning digital asset market, such as registration as an exchange and staking. Regrettably, the petition went unanswered.

Moreover, in a disconcerting pattern of regulation by enforcement, the SEC recently sent Coinbase a Wells notice concerning activities that the company was actively seeking clarity on through their public rulemaking. This behavior is both unreasonable and counterproductive. It also sends a disheartening message to the ecosystem as a whole: if compliance-minded firms with ample resources like Coinbase supposedly “don't comply” and can't get necessary answers on regulatory clarity, who can? This further drives companies and jobs offshore.

I must emphasize that the assertion that digital asset projects can easily register their digital assets with the SEC today is simply not accurate. In reality, much more is required if the SEC genuinely desires to provide adequate investor protection in the crypto asset arena. Expand on the need for trusted intermediaries for offerings and secondary trading; i.e. mandate the SEC expand what registered brokers and exchanges may do with digital assets, rather than stalling and making those who wish to participate productively look to do business offshore.

Internationally, the United States is falling behind, while Canada has similar treatment of digital assets to the United States, our European counterparts last month approved a

comprehensive and sweeping regulatory framework for crypto assets known as the Markets in Crypto Assets (MiCA). The primary objectives are to promote innovation, protect investors, ensure financial stability, and maintain market integrity. MiCA will come into effect in 2024 or 2025. The main points of the MiCA regulation are as follows:

Classification of Crypto Assets: MiCA defines and classifies crypto assets into three categories - utility digital assets, asset-referenced digital assets, and electronic money digital assets (e-money digital assets). This classification helps establish clear regulatory requirements and responsibilities for different types of crypto assets.

This is the main point that the US must learn. The US and Canadian regulators generally do not recognize utility digital assets as a distinct category of assets that are not securities. Instead, the regulators use the Howey Test and its Canadian counterpart the Pacific Coin test to analyze whether a digital asset is a security, based on facts and circumstances and economic realities. In virtually all cases, the regulators seek to prove that the assets are securities, and in extremely limited cases such as no-action letters for certain stablecoins, has the SEC confirmed that a digital asset is not a security. But that stance on stablecoins seems to be eroding as well. Even in the UK, utility digital assets, digital assets that do not resemble equity or debt instruments, are not regulated as securities.

Issuance and Offering of Crypto Assets: MiCA establishes requirements for issuers of crypto assets, including the need to be a legal entity, draft a whitepaper, and comply with disclosure and transparency requirements. It also outlines provisions for the marketing and offering of crypto assets, especially for asset-referenced and e-money digital assets, to protect investors.

Licensing and Supervision of Crypto-Asset Service Providers (CASPs): MiCA introduces a licensing regime for CASPs, requiring them to obtain authorization from their home Member State's competent authority. The regulation also outlines prudential, governance, and operational requirements for CASPs and establishes a framework for cross-border provision of services.

Market Abuse and Prevention Measures: MiCA includes provisions to prevent market abuse, such as insider trading, market manipulation, and the unlawful disclosure of inside information. It also requires CASPs to implement measures to detect and report suspicious transactions.

Consumer Protection and Anti-Money Laundering (AML) Measures: MiCA emphasizes consumer protection, requiring CASPs to implement adequate policies and procedures to manage conflicts of interest, safeguard client assets, and provide transparent information. Additionally, the regulation strengthens AML and Combating the Financing of Terrorism (CFT) measures by extending existing EU AML/CFT rules to all CASPs.

EU Passport: MiCA introduces an EU-wide passport for crypto-asset issuers and service providers, enabling them to operate across the entire EU with a single authorization, harmonizing the regulatory landscape and promoting cross-border activities.

Additionally, I have met with government officials in Dubai and Abu Dhabi to learn more about their efforts to foster responsible digital assets innovation. At a high level, they are more likely to follow the EU model than the US model. Europe and the Middle East are more harmonized with each other than with the US.

If the United States does not adopt a smarter, more technology-accommodating approach to regulating the digital assets industry, it risks falling behind other regions that have established more technology-friendly environments. The lack of clear and supportive regulation in the United States may deter businesses and investors from engaging in the domestic digital asset market, which could have several adverse consequences. First, it may lead to reduced economic growth as the potential for job creation, tax revenue, and capital investment in the digital asset industry remains untapped. Second, the United States may experience a decline in technological advancements, as innovators and entrepreneurs could relocate to jurisdictions with more competitive regulations, thereby hindering the development of blockchain and digital asset technologies domestically. Finally, the global competitiveness of the United States in the digital assets industry may diminish, as other countries continue to embrace and support the growth of this sector, attracting talent and investment. In order to maintain its position as a global leader in technology and finance, the United States must reconsider its approach to digital asset regulation and create an environment that fosters innovation while protecting consumers and maintaining market integrity.

Thank you for the opportunity to testify before you today. We look forward to continued dialogue and collaboration.