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WRITTEN TESTIMONY OF
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United States House of Representatives Committee on Financial Services Subcommittee on Digital Assets, Financial Technology and Inclusion

IN A HEARING ENTITLED
The Future of Digital Assets: Identifying the Regulatory Gaps in Digital Asset Market Structure

Chairman Hill, Ranking Member Lynch, and Members of the Subcommittee:

My name is Joshua Rivera and I serve as General Counsel of Blockchain Capital, a venture capital firm focused on digital assets technology. I am a lawyer by training and practice, and have represented traditional global financial institutions in various financial transactions including capital markets, financings, mergers and acquisitions and asset management. I have also represented eSports and gaming, life sciences, media and advertising and technology firms in various capital markets and venture transactions, both in the traditional financial sector and the digital assets industry. Upon learning about Bitcoin and Ethereum in early 2017, I began to study how blockchain technology could facilitate value creation and value transfer in open ecosystems that do not rely on intermediaries for their viability. This was new; something traditional financial ecosystems were not capable of. Technology like this could powerfully democratize access to financial and other types of value generation and retention while providing new platforms for innovation. Since then, I have worked exclusively on legal issues related to blockchain technology and the digital assets industry.

Thank you for the opportunity to testify about both the incredible opportunities — and immense challenges — that the digital assets industry, and the blockchain technology that underpins it, presents to an innovative American marketplace. My message for you today is that the industry wants to work with you, our elected representatives in Congress, and regulators on developing appropriate market structure regulation for addressing the novel challenges and opportunities of this technology. This regulation should be narrowly-tailored, a top legislative priority and focused initially on the business models that we currently understand well, such as centralized service providers. This will allow innovation to flourish and give the United States the ability to compete for global leadership in a burgeoning industry.

Blockchain Capital manages approximately $2 billion in assets and has invested in more than 100 portfolio companies, protocol teams and projects in the digital assets industry. Our team fields approximately 1,500 proposal decks and pitches each year from entrepreneurs building in the industry, providing us with a unique macro perspective on industry developments. We have a 30,000-foot view of all parts of the digital assets ecosystem, including the infrastructure supporting the foundation of the industry, the increasingly sophisticated applications facilitating new use cases and the critical compliance solutions being developed to aid institutions and agencies to engage with this industry responsibly.

The U.S. proudly maintains the world's most liquid, fair and efficient financial markets. The venture capital industry plays an integral role in facilitating these robust and deep markets, particularly in funneling funding to promising enterprises with high growth potential, creating market efficiencies for investors in more mature markets, such as public equities markets. As you would expect, America leads the world in venture financing, which has also provided a critical source of capital and jobs. A recent study shows that job creation at venture capital-funded companies grew 960% between 1990 and 2020. This job growth outpaced non-venture capital-backed companies by eight times. This job creation benefits the entire nation (not just major financial centers), as 62.5% of employment at these venture capital-backed companies occurs outside of the states of California, New York and Massachusetts, where venture funding is most concentrated.

Venture investors have the great privilege of creating opportunities for entrepreneurs and innovators to take risks in new fields from agriculture to public health to environmental tech. The freedom to explore innovation via venture financing has led to enormous advancements, positioning the United States as an innovation leader across myriad sectors over the past 50 years. In this position, venture capitalists have the very first perspective on innovations that hold great promise and those that may not work out or those that may require additional time and resources to develop further. The knowledge and expertise that venture investors gain over time provide greater certainty to later stage market participants, including fully mature public markets. As venture capitalists, it is our job to understand how a burgeoning industry is developing better than anyone else, and we take that responsibility seriously.

How Blockchain Technology Enhances Our Society

The current financial system is overly reliant on intermediaries, a paradigm that constrains innovation. It is sometimes subject to conflicts of interest, creates central points of attack or failure and provides continued examples of mismanagement or outright breaches of bedrock fiduciary duties. While these centralized entities do provide important services and infrastructure, including allowing strangers to transact safely with each other, the net benefit to society is limited by their sclerotic control over market access, consumer-facing innovation and role in suppressing efficient solutions to current market frictions. The U.S. consumer credit rating system provides a prime example of the inefficient and flawed systems that can arise out of overly intermediated value systems. Monopolized by three ratings bureaus, this system is often ineffective and exclusionary to people who need safe and affordable access to credit.

It is not only legacy financial systems that suffer from centralization. Social media and content creation platforms demonstrate the vast dangers of centralized intermediation. Social media enterprises like Facebook and Twitter have leveraged the free and instantaneous transfer of data pioneered by the internet, not to democratize participation in value creation, but to monopolize it, commoditizing the users of these platforms themselves and extracting value from them. Similarly, artistic platforms like Spotify and YouTube have successfully scaled access to music and video content from millions of creators globally only to retain the lion's share of value generated on those platforms away from the very same creators, artists and musicians.

Blockchain technology creates alternative solutions to the services and infrastructure controlled by these intermediaries. In the case of financial ecosystems, blockchain networks can be accessed anywhere in the world, by anyone with an internet connection. Using these networks, participants can transfer any amount of money to virtually any location in the world, 24 hours a day, 7 days a week, 365 days a year, with instantaneous settlement, at much lower cost to the user. An immediately obvious use case leveraging this broad-reaching and inexpensive characteristic is global remittance payments. Under traditional payments infrastructure, remittances can be up to two to three times the costs that are achieved utilizing digital assets.

Even beyond remittances, we have backed entrepreneurs leveraging the efficiency of value transfer on blockchain networks to provide blue collar workers with affordable earned wage access, allowing them an alternative to predatory payday lenders while also granting them unique opportunities to build credit.

For musicians seeking to build communities around the music they create, we have backed builders that allow artists to publish their content to decentralized networks where fans of their music can contribute to their financial success and enjoy access to the value their music generates rather than forfeiting financial gain to a centralized platform, like Spotify. We have also engaged with builders democratizing access to decentralized video streaming protocols which allow video content creators more efficient means of producing and earning income from their artistic endeavors.

These examples form only a fraction of the vast innovations benefitting existing financial and social structures in our society. Such open access and cost-efficient utility stand in stark contrast to the barriers to entry that our legacy financial institutions and centralized social structures erect, disenfranchising many would-be participants in the process. These institutions continue to rely on systems that were built for an earlier era of commerce, ponderous technology that often does not fit with the global, always-on nature of the 21st century economy. In contrast, blockchain technology is such a technology for this moment in time.

How Should We Engage with this Innovation?

The fundamental innovation afforded by blockchain networks — to allow anyone, anywhere to participate in commerce or other systems of value, without an intermediary — is a novel and fundamental shift from the traditional way in which financial markets are organized and regulated. Never before have we been able to, at scale, facilitate disintermediated transactions, obviating the hazards of centralized intermediation. While some are critical of the notion that new concepts, new rules, and new regulations are needed to address this shift, it is clear that legacy methods of financial regulation, which focus primarily on the actions of intermediaries, do not adequately address this new paradigm.

Clinging to rules that were designed around centralized actors in hopes that they will also regulate decentralized actors is an ineffective regulatory strategy and stifles innovation. Value ecosystems where transactions are facilitated by open-source software in transparent and verifiable actions, where discretionary decision-making is not entrusted to a person or a firm, require new regulatory frameworks that both promote the novel benefits and opportunities of this technology while carefully addressing the unique risks it presents. Rather than fear this new ability, we suggest that policymakers meet the challenge of designing new regulations that are fit-for-purpose and avoid applying traditional modes of thinking.

Unfortunately, some regulatory agencies have largely ignored this fundamental innovation and instead suggested that existing frameworks are both appropriate and easily accessible to the digital assets industry. We have heard time and again that blockchain companies need only “come in and register.” However, this call rings hollow as these regulators have failed to offer thoughtful pathways to compliance and have chosen instead to rely predominantly on a campaign of enforcement. Innovators have a right to rely on regulators to do the hard work of understanding and adapting to new technologies, and many firms have engaged with regulators in good faith only to be met with silence, or worse, enforcement actions. Enforcement against a fledgling industry should not be that industry’s primary expectation. Because it is in this case, the vast majority of the law-abiding American citizens building in the digital assets industry are dissuaded from innovating in the U.S.

A Better Way Forward

We often hear the perception that participants, investors and founders in the digital assets industry do not want to be regulated. This is false. A great number of participants, myself included, have sought to engage with regulators for years in a collaborative attempt to set out rules of the road that will provide appropriate regulation while also allowing for continued innovation. While there have been some rulemaking efforts, particularly recently, these efforts have not come early or often enough, and unfortunately have been made with almost no meaningful industry engagement. The undesirable outcome has been rule proposals that are largely unworkable both from the perspective of technological implementation and desired policy outcomes. Apart from these infrequent efforts, we are concerned that there is a growing sentiment among many of expressly preferring not to to create regulation in the hopes that the technology will "go away" (offshore) or "die" (cease being developed) if it is not legitimized by regulation. But we are convinced that this technology will not go away or die; it is, by design, operationally resilient and expansive, and the innovators creating it are sincerely passionate to continue their work. We must work with this innovation, not against it.

Other jurisdictions, including major global financial and commercial centers like the United Kingdom, Singapore, the European Union and Japan have taken a drastically different approach towards blockchain technology, making space for the industry to grow in these respective countries while implementing reasonable safeguards to protect users. Indeed, with the recent passage of the EU's landmark Markets in Crypto-Assets licensing regime, the bloc is now better positioned to attract digital assets startups and investors compared to the increasingly hostile environment in the United States. While many U.S. regulators have remained dismissive of this technology and the markets it has produced, other countries' regulatory agencies have leaned in, engaging businesses in good faith efforts to understand how progress can be made.

According to recently published data from PitchBook, the share of venture capital funding for blockchain startups in the EU surpassed the allocation for U.S. firms for the first time in the first quarter of this year. This is, sadly, not a surprise. Why would an investor commit to a country that has seemingly harbored a posture of disregard for the technology, at best, or outright hostility, at worst? In stark contrast to the warnings of some in the U.S. regarding the contagion potential wrought by crypto markets, other countries are welcoming would-be U.S innovators with a greater willingness to provide clarity and opportunity. This is a devastating policy outcome, one that the United States may not be able to recover from, and something every member of this subcommittee should actively seek to avoid.

Tailored Regulation is Critical for the Digital Assets Industry

The world-changing innovations provided by digital assets have only scratched the surface of innovative potential. We are on the cusp of the next wave of technological change, but the United States must act quickly to keep it here at home.

Tailored, fit-for-purpose rules for this nascent industry are critical — and must protect consumers while also promoting innovation. Industry stands ready to work with you on this balanced approach, ensuring that the U.S. remains a leader — as it often is — in all vanguard fields of innovation, especially the blockchain industry.