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Before the U.S. House of Representatives House Financial Services
Subcommittee on Digital Assets, Financial Technology and Inclusion
"Dazed and Confused: Breaking Down the SEC's Politicized Approach to Digital Assets"
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I. Introduction

Thank you, Chairman Hill, Ranking Member Lynch, and members of the Subcommittee for inviting me to testify today on the U.S. Securities and Exchange Commission's ("SEC" or "Commission") current methods of overseeing the U.S. digital asset markets.

My name is Dan Gallagher. I am Chief Legal, Compliance and Corporate Affairs Officer of Robinhood Markets, Inc. ("Robinhood"). I served as an SEC Commissioner from 2011 to 2015 and Deputy and Co-Acting Director of the SEC's Division of Trading and Markets from 2008 to 2010. I have practiced law in the financial services industry for more than twenty-five years.

Robinhood has a single mission—to democratize finance for all. Millions of Americans—including millions of Robinhood customers—want to participate and are participating responsibly in the digital asset economy. Robinhood provides them broad access to digital asset markets through a low-cost, intuitive platform. Robinhood Crypto, one of Robinhood's wholly owned subsidiaries, allows customers in all 50 states and the District of Columbia, U.S. Virgin Islands, and Puerto Rico to buy, sell, store, and transfer (depending on the jurisdiction) up to 15 cryptocurrencies at low cost without trading commissions, account minimums, or other fees charged by our competitors.[1]

Robinhood Crypto does so with a "Safety-First" mindset, taking a thoughtful, incremental approach to building its cryptocurrency business.[2] For example, despite consistent market demand, Robinhood Crypto has thoughtfully restricted the coins it makes available. It has made difficult choices not to list certain tokens or offer yield-generating products, such as lending and staking, that the Commission has alleged involve investment contracts. And Robinhood has never facilitated ICOs or issued its own native tokens, nor does it engage in proprietary trading.

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[1] Aave (AAVE), Avalanche (AVAX), Bitcoin (BTC), Bitcoin Cash (BCH), Chainlink (LINK), Compound (COMP), Dogecoin (DOGE), Ethereum (ETH), Ethereum Classic (ETC), Litecoin (LTC), Shiba Inu (SHIB), Stellar Lumens (XLM), Tezos (XTZ), Uniswap (UNI), and USD Coin (USDC).

[2] In contrast to many cryptocurrency platforms, Robinhood has extensive experience operating in highly-regulated industries. Robinhood is also federally-registered as a money services business with FinCEN and has subjected itself to extensive state regulation by registering under applicable state laws. Specifically, Robinhood Crypto is licensed in 29 states, the District of Columbia, and Puerto Rico and holds a "BitLicense" from the New York State Department of Financial Services.

For too long, the U.S. digital asset markets and millions of Americans who wish to participate in them have had to contend with innovation-killing federal regulatory uncertainty. This uncertainty is particularly acute in the context of determining which digital assets the SEC deems to be investment contracts requiring SEC registration and how tokens and platforms can become registered with the Commission. Instead of providing regulatory certainty through appropriate rulemaking, the SEC has engaged in regulation by enforcement.

The current Commission's "scorched earth" approach to regulating cryptocurrency has real-world consequences.[3] Regulation by enforcement is bad for American consumers who want greater access to digital assets, bad for innovation in the blockchain and digital asset industries, and bad for the already-eroding competitive position of the U.S. with regard to digital asset markets.

Because the Commission has taken a rigid, hostile approach to cryptocurrency and refused to provide regulatory clarity, U.S. customers have suffered as innovation has moved overseas.[4] This should not be surprising. Many international jurisdictions are doing exactly what the American cryptocurrency industry has been requesting for years: providing regulatory clarity by enacting cryptocurrency-specific regulatory regimes. For example, the Markets in Crypto-Assets Regulation institutes uniform market rules for crypto-assets across the European Union; other jurisdictions have been taking similar steps towards establishing regulatory regimes of their own. The Commission should take steps to implement a clear and workable regulatory regime for digital assets and support policy solutions that encourage Americans to engage in digital asset markets through responsible, appropriately-regulated U.S. firms and not incentivize them to participate through often unregulated or lightly regulated foreign platforms. But it has not done so.

Cryptocurrency is a multi trillion-dollar global market in which tens of millions of Americans participate. And, importantly, the technology underlying this market has the potential to fundamentally transform finance. I strongly believe that Congress is the appropriate body to establish a clear and comprehensive regulatory framework for this important market.

But I would be remiss if I did not point out that, while Congress continues diligently to pursue much needed legislation, the Commission has—and has had since 1996—the authority *now* to establish at least a basic, provisional regulatory regime for digital assets. Specifically, as described in more detail below, the Commission could utilize its existing authority under Section 36 of the Securities Exchange Act of 1934 ("Exchange Act") to create a regulatory framework that could address many (though perhaps not all) of the core issues needed for the SEC to start registering and regularly overseeing platforms that would like to facilitate trading in digital

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[3] *See* Commissioner Hester M. Pierce, "Overdue: Statement of Dissent on LBRY" (Oct. 27, 2023), *available at* https://www.sec.gov/newsroom/speeches-statements/peirce-statement-lbry-102723.

[4] Yaffe-Bellany, David, "Crypto Firms Start Looking Abroad as U.S. Cracks Down," N.Y. Times (June 7, 2023), *available at* https://www.nytimes.com/2023/06/07/technology/crypto-firms-start-looking-abroad-as-us-cracks-down.html#:~:text=Coinbase%2C%20the%20largest%20crypto%20exchange,shut%20down%20its%20U.S.%20operations; *see also* Chipolina, Scott, "US crypto clampdown pushes exchanges to go offshore," Fin. Times (May 16, 2023), *available* at https://www.ft.com/content/10979399-ba25-45b9-b85d-776c1b75bfea.

assets the SEC deems to be investment contracts. This rulemaking could include registration requirements, books-and-records requirements, antifraud protections for consumers, custody requirements, and transaction reporting—all important protections that would have been handy prior to FTX's collapse in 2022. Unfortunately, the current Commission has done nothing to use its existing authority to provide this much needed clarity and instead wistfully calls on cryptocurrency platforms and token issuers to "come in and register."[5]

Robinhood heeded the Chair's call to register—a workstream I call "crypto the hard way"—notwithstanding its current business model and its robust policies to ensure that it does not support digital assets on its platform that the SEC deems to be investment contracts. Robinhood spent significant time, money, and effort to pursue registration as a digital asset special purpose broker-dealer subject to SEC oversight. Robinhood had over a dozen meetings and calls with the SEC over a year and a half to discuss its cryptocurrency business, including its listing process. Robinhood also presented the Staff with a targeted, written request for relief for a registered special purpose broker-dealer that would be able to support transactions in both digital asset commodities and digital assets the SEC deems to be investment contracts in compliance with federal law. While the discussions with the SEC staff were always cordial and often deeply substantive, the staff was generally non-responsive to Robinhood's requests for guidance or feedback on how to move its registration proposal forward.

Rather than issue rules to provide regulatory certainty to an industry craving it, the SEC has instead targeted individual firms, including Robinhood, through regulation by enforcement. This is not the way Americans expect our government to work. As Judge Amy Berman Jackson of the U.S. District Court for the District of Columbia recently stated, "The agency's decision to oversee this billion dollar industry through litigation – case by case, coin by coin, court after court – is probably not an efficient way to proceed, and it risks inconsistent results that may leave the relevant parties and their potential customers without clear guidance."[6] Commissioners Hester Peirce and Mark Uyeda recently echoed this concern in their dissenting statement on the SEC's enforcement action against a dining club that sold non-fungible tokens: "Leaving crypto to be addressed in an endless series of misguided and overreaching cases has been and continues to be a consequential mistake."[7] I couldn't agree more.

II. SEC Registration—A Road to Nowhere

The Commission has long recognized that, as former SEC Chairman Jay Clayton noted in 2018, "the currently applicable regulatory framework for cryptocurrency trading was not designed with

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[5] Wieczner, Jen, "Gary Gensler on Crypto, SPACs, and Robinhood Wall Street's top cop wants to police new finance with old rules," New York Magazine (Sept. 13, 2021), *available at* https://nymag.com/intelligencer/2021/09/gary-gensler-sec-chair-crypto-spacs-robinhood.html; *see also* Testimony of Gary Gensler Before the U.S. Senate Committee on Banking, Housing, and Urban Affairs (Sept. 14, 2021), at 6, *available at* https://www.sec.gov/newsroom/speeches-statements/gensler-2021-09-14 ("I've suggested that platforms and projects come in and talk to us.").

[6] *SEC v. Binance Holdings Ltd., et al.*, Civil Action 23-1599 (ABJ), ECF No. 248 (D.D.C. June 28, 2024), at 21 hereinafter the "Binance Opinion".

[7] SEC Commissioners Peirce and Uyeda Dissent to Commission Action re Flyflish Cub, LLC, https://www.sec.gov/newsroom/speeches-statements/peirce-uyeda-statement-flyfish-091624.

trading of the type we are witnessing in mind."[8] Chair Gary Gensler initially appears to have agreed. For example, he testified before Congress in May 2021 that "the exchanges trading in these crypto assets do not have a regulatory framework either at the SEC, or our sister agency, the Commodity Futures Trading Commission."[9] The following year, he appears to have changed his tune.[10] Now Chair Gensler and other members of the SEC Staff simply say that existing rules and regulations do apply, and that legislation is not necessary.[11]

I disagree, as I think most securities lawyers would. The federal securities laws have been remarkably flexible in response to many forms of technological innovation in the financial services space. But they were enacted in the 1930s at a time when the idea of blockchain technology and cryptocurrencies was unimaginable. The rules that exist today, like so many things at the SEC, do not work properly for cryptocurrency. Serious gaps in existing statutes and regulations exist when it comes to digital assets. These gaps will require the need for platforms to obtain exemptive and/or no-action relief, such as the relief granted to Paxos Trust Company, LLC discussed below—relief the Commission under the current leadership is not willing to provide.[12]

The most fundamental problem in digital asset markets is that there is no clear guidance on which transactions in digital assets the SEC deems to be investment contracts.[13] The SEC bases its analysis of whether a digital asset is an investment contract on decades-old Supreme Court cases. The primary case, *SEC v. W.J. Howey Co.*, 328 U.S. 293 (1946), which was decided in 1946, establishes a four-part test to define an "investment contract." There are legitimate questions around whether certain digital asset transactions should be governed by the *Howey* test and, if so, how the test applies to transactions in multiple individual tokens with their own unique characteristics. As my dear friend and mentor, the late Harvey Pitt, SEC Chairman from 2001 to

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8 Testimony of Jay Clayton Before the U.S. Senate Committee on Banking, Housing, and Urban Affairs (Feb. 6, 2018), *available at* https://www.sec.gov/news/testimony/testimony-virtual-currencies-oversight-role-us-securities-and-exchange-commission.

9 *Game Stopped? Who Wins and Loses When Short Sellers, Social Media, and Retail Investors Collide*, Part III, 117th Cong. 1, 12 (May 6, 2021).

10 By at least December 2022, Chair Gensler "fe[lt] that [the SEC] ha[s] enough authority" to require digital asset firms "to come into compliance" with its rules and regulations governing registration. Singh, Kanishka, "SEC chair says crypto intermediaries should comply with law," Reuters (Dec. 7, 2022), *available at* https://www.reuters.com/markets/currencies/sec-chair-says-crypto-intermediaries-should-come-into-compliance-with-law-2022-12-07/.

11 *See* Chair Gary Gensler, "Statement on the Financial Innovation and Technology for the 21st Century Act" (May 22, 2024), *available at* https://www.sec.gov/newsroom/speeches-statements/gensler-21st-century-act-05222024.

12 *See* Paxos Trust Company, LLC No-Action Letter, *available at* https://www.sec.gov/divisions/marketreg/mr-noaction/2019/paxos-trust-company-102819-17a.pdf.

13 *See* "Regulating cryptocurrencies is a national concern, not a political issue, says former SEC Chair Harvey Pitt," CNBC (Dec. 13, 2022), *available at* https://www.cnbc.com/video/2022/12/13/regulating-cryptocurrencies-is-a-national-concern-not-a-political-issue-says-former-sec-chair.html ("It's reminiscent of the old recipe for rabbit stew – first you have to start with a rabbit and it's not clear to me that these are securities.").

2003, said in a 2022 interview, "there is a need here for a concise and considered national policy that lays out the rules of the road."[14]

Further, the SEC has not issued clear guidance on the registration requirements for cryptocurrency platforms and token issuers. In fact, exchanges, market intermediaries, and other market participants are not able to register with the SEC without obtaining additional regulatory relief addressing a number of issues. For example, regulatory relief is needed regarding exchange listing requirements; SEC custody requirements, including capital and accounting requirements for custodians; the trading of non-security digital assets and digital assets the SEC deems to be investment contracts on the same platform; the application of SEC trading rules, such as those under Regulation NMS and Regulation SHO; the application of SEC disclosure rules; and SEC clearing agency and transfer agent requirements.

III. The Current Commission's Approach is Failing the American Public.

Following the SEC's crackdown on fraudulent ICOs in 2018, the prior Commission engaged in a commendable (though ultimately limited) effort to provide tailored relief to the digital asset industry *without* sacrificing important investor protections. Notably, in October 2019, the SEC's Division of Trading and Markets provided "no-action" relief for Paxos' blockchain settlement platform to process transactions for a limited number of broker-dealers in certain listed U.S. equity securities.[15] As a former SEC Commissioner and practitioner, I cannot emphasize enough the importance of the Paxos no-action letter. At a policy level, it demonstrates the proper role of government—allowing for innovation in a controlled manner without sacrificing investor protections. From a practitioner level, it plainly lays out the broad need for regulatory relief if we are to allow SEC-regulated tokens to trade in the U.S.

This short-lived period of innovation at the Commission abruptly ended in 2021. Rather than work with Congress to pass comprehensive legislation governing digital assets or issue a generally applicable rule, the current Commission's approach to addressing digital asset regulatory issues is now largely two-fold: (1) bringing enforcement actions against industry participants; and (2) attempting to shoehorn cryptocurrency into proposed rules primarily addressing other discrete areas of traditional finance. Neither approach brings the regulatory clarity so desperately needed by the industry. And both fail the American public.

Of those two misguided approaches, my main concern for purposes of today's hearing is the fact that the Commission has been asserting sweeping new authority over the entire cryptocurrency industry by bringing enforcement action after enforcement action against industry participants. Over the past year, for example, the Commission has been embroiled in contentious litigation with some of the nation's major digital asset exchanges.[16] The Commission is alleging that,

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[14] *Id*.

[15] *See* Paxos Trust Company, LLC No-Action Letter, *available at* https://www.sec.gov/divisions/marketreg/mr-noaction/2019/paxos-trust-company-102819-17a.pdf

[16] E.g., Press Release, "SEC Charges Kraken for Operating as an Unregistered Securities Exchange, Broker, Dealer, and Clearing Agency" (Nov. 20, 2023), available at https://www.sec.gov/newsroom/press-releases/2023-237; Press Release, "SEC Charges Coinbase for Operating as an Unregistered Securities Exchange, Broker, and Clearing Agency" (June 6, 2023), available at

among other things, they are operating as unregistered national securities exchanges, brokers, dealers, and/or clearing agencies. They are fighting the SEC and defending themselves against the SEC's allegations in court.

Some targets of the SEC's Enforcement Division, Robinhood included, have structured their businesses to operate in full compliance with applicable rules and regulations and have attempted to register with the SEC. Despite the good faith in which Robinhood has conducted its cryptocurrency business, Robinhood faces the potential of an SEC lawsuit for acting as an unregistered broker and clearing firm. In May 2024, Robinhood received a "Wells Notice" from the staff of the SEC's Enforcement Division stating that they have made a "preliminary determination" to recommend that the Commission file an enforcement action against us. This was so even after nearly two years of serious attempts to work with the SEC for regulatory clarity, including our well-known attempt to "come in and register." While I have tremendous respect for the SEC Enforcement staff, who have handled this matter professionally throughout, Robinhood firmly believes that the assets listed on our platform do not fall under the SEC's jurisdiction, and we have made it clear just how weak any case against Robinhood Crypto would be on both the facts and the law.

Such "regulation by enforcement" is, as Commissioner Hester Peirce has called it, "the opposite of a rational regulatory framework."[17] I agree. Put simply, it is a horrible way to govern, goes against fundamental principles of fairness and justice, produces inconsistent outcomes, fosters confusion within the industry, and suffers from significant limitations as a means of setting policy. As House Financial Services Committee Chairman Patrick McHenry has appropriately recognized, "Regulation by enforcement is not sufficient nor sustainable. You're punishing digital asset firms for allegedly not adhering to the law when they don't know it will apply to them."[18] I couldn't agree more.

Courts have started to take notice, too. This past June, federal district court judge Amy Berman Jackson expressed skepticism towards a number of the Commission's legal theories in its case against Binance, and rejected a number of the Commission's claims. In doing so, she did not mince words. "[T]he SEC seemed to speak[] out of both sides of its mouth" at the hearing on the motion to dismiss, Judge Jackson concluded.[19] She also concluded that the SEC's approach represented "a departure from the *Howey* framework that leaves the Court, the industry, and future buyers and sellers with no clear differentiating principle between tokens in the marketplace that are securities and tokens that aren't."[20] Notably, she criticized the SEC's overall approach to regulating the cryptocurrency industry by enforcement:

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https://www.sec.gov/newsroom/press-releases/2023-102; Press Release, "SEC Files 13 Charges Against Binance Entities and Founder Changpeng Zhao" (June 5, 2023), available at https://www.sec.gov/newsroom/press-releases/2023-101.

17 Commissioner Hester M. Peirce, "Outdated: Remarks before the Digital Assets at Duke Conference" (Jan. 20, 2023), *available at* https://www.sec.gov/newsroom/speeches-statements/peirce-remarks-duke-conference-012023.

18 Sutton, Sam, and Declan Harty, "McHenry clashes with SEC's Gensler over crypto crackdown," Politico (Apr. 18, 2023), *available at* https://www.politico.com/news/2023/04/18/mchenry-gensler-crypto-hearing-00092531.

19 Binance Opinion, *supra* note 6, at 42.

20 *Id.* at 43.

> [T]he agency's decision to oversee this billion dollar industry through litigation –case by case, coin by coin, court after court – is probably not an efficient way to proceed, and it risks inconsistent results that may leave the relevant parties and their potential customers without clear guidance.[21]

Judge Jackson's concerns are not simply theoretical. Judicial opinions in the SEC's litigation against digital asset exchanges have themselves reached inconsistent results that leave the industry without clear guidance. Citing Judge Analisa Torres's decision in *SEC v. Ripple Labs, Inc.*, Judge Jackson's opinion in the Binance litigation dismissed the Commission's claims as to secondary market sales of digital assets; however, an earlier opinion in separate litigation by a different judge in a different district allowed similar Commission claims as to secondary market sales of digital assets to proceed.[22] Such inconsistency is a direct product of the Commission's approach to bringing enforcement actions against the major players in the industry at the expense of providing the clear guidance long requested by the entire industry.

IV. The Path Forward

Given the lack of federal regulatory clarity for digital assets, it is no wonder that former SEC Chairman Jay Clayton and former CFTC Chairman Chris Giancarlo called for coordination with Congress in regulating digital assets, and why current CFTC Chairman Rostin Benham has called for Congress to provide additional authority to regulate digital asset markets.[23]

I believe Congress can—and should—do so on a bipartisan basis. As you know, the Financial Innovation and Technology for the 21st Century Act passed the House with overwhelming bipartisan support. I applaud such Congressional efforts to foster the development of blockchain technology and digital asset markets in the U.S. and establish a clear and comprehensive regulatory framework for this important market through tailored, responsible regulation.

The Commission does have a role to play in the meantime, however. Rather than engage in regulation by enforcement, the Commission should heed the industry's call and undertake formal, notice-and-comment rulemaking to establish rules applicable to the entire cryptocurrency industry, at least on a provisional basis. In fact, it should have done so years ago. The Commission should establish a provisional regulatory regime for digital assets using its authority provided by Section 36 of the Exchange Act, which authorizes the Commission to exempt, even conditionally, any person, security, or transaction, or any class or classes of persons, securities, or

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[21] *Id.* at 21.

[22] SEC v. Coinbase, Inc. and Coinbase Global, Inc., No. 1:23-cv-04738-KPF, ECF No. 105 (S.D.N.Y Mar. 27, 2024)

[23] Testimony of Jay Clayton Before the U.S. Senate Committee on Banking, Housing, and Urban Affairs (Feb. 6, 2018), *available at* https://www.sec.gov/news/testimony/testimony-virtual-currencies-oversight-role-us-securities-and-exchange-commission; Testimony of J. Christopher Giancarlo Before the U.S. Senate Committee on Banking, Housing, and Urban Affairs (Feb. 6, 2018), *available at* https://www.cftc.gov/PressRoom/SpeechesTestimony/opagiancarlo37#P21_6885; Testimony of Rostin Behnam Before the U.S. Senate Committee on Agriculture, Nutrition, and Forestry (Dec. 1, 2022), *available at* https://www.cftc.gov/PressRoom/SpeechesTestimony/opabehnam29.

transactions, from any provision or provisions of the Exchange Act or any rule or regulation thereunder, to the extent that such exemption is necessary or appropriate in the public interest, and is consistent with the protection of investors. This is not a theoretical proposition. The Commission used its general exemptive authority in 1998 when it adopted Regulation ATS, for example.[24] The Commission could similarly utilize this Section 36 authority to craft a tailored rule for the cryptocurrency industry, even if only on a provisional basis, that could include registration requirements, books-and-records requirements, antifraud protections for consumers, custody requirements, and transaction reporting. I seriously question, however, whether the current Commission, given its unfortunate track record with respect to rulemakings, is able to do so.

V. Conclusion

Ultimately, it will be up to Congress to rectify the Commission's failure to act to register both tokens and platforms. Only Congress will be able to truly provide the necessary, long-term, comprehensive regulatory clarity for digital assets that would allow token issuers, exchanges, intermediaries, and other market participants to provide products and services their customers want without the constant threat of crippling enforcement action, and would help ensure that the U.S. remains the global leader in responsible blockchain and digital asset innovation, as well as vibrant, appropriately regulated digital asset markets. Nothing is stopping the Commission from moving *now* to provide tailored relief that allows firms to register (even if provisionally) and continue to innovate in the meantime. It has simply chosen—consistently—not to do so.

I want to thank the Subcommittee for holding this important hearing, and I look forward to your questions.

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[24] Regulation of Exchanges and Alternative Trading Systems, Securities Exchange Act Rel. No. 40760, 63 Fed. Reg. 70844, at 70846 (Dec. 22, 1998). The Commission went on to state that the regulation of the markets "should provide sufficient flexibility to ensure that new markets promote fairness, efficiency, and transparency…. The Commission believes that this regulatory approach effectively addresses commenters' concerns while carefully tailoring a regulatory framework that is flexible enough to accommodate the evolving technology of, and benefits provided by, alternative trading systems." *Id.*