Testimony of Timothy G. Massad

Subcommittee on Digital Assets, Financial Technology and Artificial Intelligence of the Committee on Financial Services U.S. House of Representatives

"The Golden Age of Digital Assets: Charting a Path Forward"

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Committee Chairman Hill, Committee Ranking Member Waters, Subcommittee Chairman Steil, Subcommittee Ranking Member Lynch, members of the Subcommittee and staff, I am honored to be testifying before you today.

I am currently a Research Fellow, and Director of the Digital Assets Policy Project, at the Mossavar-Rahmani Center for Business and Government at the Harvard Kennedy School. I am also an independent consultant. I was the chairman of the Commodity Futures Trading Commission from 2014 to 2017. I served at the U.S. Treasury Department from 2009 to 2014, primarily as the Assistant Secretary for Financial Stability, where I oversaw the Troubled Asset Relief Program. Prior to my government service, I was a partner at the law firm of Cravath, Swaine & Moore LLP. The views I express are my own and do not represent the views of the Harvard Kennedy School.

Since 2014, when under my leadership the CFTC declared bitcoin to be a commodity, I have spoken and written about the need to improve regulation of digital assets. This has included appearances before the House Financial Services Committee and other committees of Congress. For several years now, I have spoken and written about how the United States needs to create a regulatory framework for stablecoins.

I believe digital assets and tokenization technology could be very valuable in numerous ways. They could potentially be used for a variety of financial transactions and processes, in ways that might generate greater efficiency, growth, choice, opportunity and financial inclusion. But although it has been sixteen years since bitcoin was launched, we have not yet seen that much use that has generated real world value.

The stated purpose of the President's Executive Order on "Strengthening American Leadership in Digital Financial Technology" is to "support the responsible growth and

use of digital assets, blockchain technology, and related technologies."[1] The question is how to fulfill those words. Will we create legal frameworks that encourage responsible development of digital technology in ways that create social utility, or frameworks that mostly encourage more speculative activity and more of the types of abuses we have seen far too much of to date?

The crypto industry has been characterized by a primary focus on speculative activity as well as tokens and applications that have little social utility. There have been rampant abuses, fraud, manipulation, failures to protect consumers, and the use of this technology for financial crime and evasion of sanctions. It is also true that the absence of a clear regulatory framework has caused some institutions to refrain from making investments that might lead to applications of greater utility. I believe that both the problems we have seen to date, and the failure to develop more useful applications, is in large part due to the absence of a strong regulatory framework—one that provides adequate consumer and investor protection and minimizes those risks. Yes, we need clarity of rules. But we need the right rules.

I will discuss how we accomplish that.

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Stablecoins and the STABLE Act[2]

Stablecoins are the most useful application of blockchain and digital asset technology to date. While their primary use has been for trading crypto, they could be very important as a general means of payment. Whether that happens will be for the market to determine, not the government. But it will only happen if we create a regulatory framework that puts the "stable" into stablecoins.

Two and a half years ago, Professor Howell Jackson of Harvard Law School, Professor Dan Awrey of Cornell Law School and I wrote a detailed paper on how this could be done by our bank regulators under existing law.[3] We did so because the stablecoin market was already large and growing, and there were significant risks that needed to be addressed. A framework would also enable the private sector to realize their potential. But there was little sign then that Congress would take action.

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[1] United States, Executive Office of the President [Donald J. Trump]. Executive Order 14178: Strengthening American Leadership in Digital Financial Technology. 23 January 2025. *Federal Register*, vol. 90, no. 20, pp. 8647-8650 ("Executive Order 14178").

[2] United States, Congress, House, Committee on Financial Services. *STABLE Act of 2025* [Discussion Draft]. House Financial Services Committee Press Release, 5 February 2025 ("STABLE Act").

[3] Jackson, Howell E., Massad, Timothy G., and Awrey, Dan. "How We Can Regulate Stablecoins Now—Without Congressional Action." *Hutchins Center Working Paper*, no. 76, August 2022 ("Howell et al. (2022)").

I am therefore pleased to see the growing support within Congress for such a measure, and for the Subcommittee's apparent intention to make stablecoin legislation the priority relative to other digital asset issues.

The legislation detailed for this hearing has many features I support. To name just a few critical ones, these include requiring full reserves for tokens and investing those reserves in a conservative manner, as well as limitations on the activities of an issuer. But there are many, many areas where it is deficient, and where it could lead to dangerous risks. Moreover, the legislation is substantially weaker in many respects than what I understand was negotiated between Republican and Democratic members' staffs last fall.

I will highlight some of the principal deficiencies:

Insufficient Standards and Supervision for State-Chartered Issuers. While the legislation provides for both federal and state-chartering of stablecoin issuers, as we have for banks, it is unlike our banking regime in terms of making sure the overall regulatory framework is sufficient. The provisions that pertain to state-chartered nonbank issuers create many gaps, weaknesses, and risks. These arise in multiple ways, the first being the chartering process itself, where there is no coordination between federal and state authorities, and no ability for federal review of or input into state standards.

Even with respect to basic standards of capital, liquidity, and risk management required of federally-chartered issuers—which are not strong enough, as noted below—the legislation allows state authorities to set their own standards, thus creating the possibility of much weaker standards for these state-chartered issuers.

There is also no ongoing federal supervision of state-chartered entities. It is only in "exigent" circumstances, and in that case only "after no less than 5 days prior written notice," that a federal regulator has any power to take action. The inadequacy of such a provision in the digital world is all too obvious.

Since there is no size limitation on a state-chartered entity,[4] there could easily be one of systemic importance that federal authorities are powerless to do anything about until it is far too late. Under our financial system, state authorities do not have the tools to address such a situation. If stablecoins can indeed become globally important

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[4] I note that there is a size limit in the GENIUS Act introduced in the Senate, but at $10 billion in assets, it is far too high unless there are stronger standards for chartering and ongoing federal oversight. *See* United States, Congress, Senate, Committee on Banking, Housing, and Urban Affairs. *GENIUS Act of 2025*. Senate Committee on Banking, Housing and Urban Affairs Press Release, 4 February 2025 ("GENIUS Act").

as a means of payment and as a way to promote the dollar, surely the foundation should not be a potentially confusing array of fifty state laws of varying standards and no federal oversight.

We cannot expect consumers to engage in due diligence to know which stablecoins are the "safest," nor do we want them to, if we want to see this sector grow. We must create a framework that gives people confidence that any stablecoin is in fact worth $1, not one in which that might depend on the particular state standards. Nor will state authorities have the ability to deal with the possible contagion or collateral effects of a failure of a large stablecoin issuer. (A failure of one large stablecoin issuer could, for example, lead to failures of other stablecoin issuers especially if business models and permitted investments are similar, as well as to failures of other types of financial institutions that interact with the issuer.[5]) While a state chartering path can be made to work, it should not separate supervisory authority from the federal authorities that have responsibility for the monetary system and financial stability.

It is my understanding that there was bipartisan agreement last fall on a better approach that provided for, among other things, registration by state-chartered issuers with the Federal Reserve Board in a process that would be open to public comment. The agreement also provided for ongoing supervision by the Board.

Insufficient Authority to Regulate. This is a new and rapidly developing sector, and it will develop in ways we cannot predict. Therefore, the legislation needs to give regulators sufficient authority and discretion to develop appropriate rules and standards and to be able to respond to new circumstances and risks as they emerge. Unfortunately, the STABLE Act fails in that regard. This can be seen in numerous places. For example, the STABLE Act severely limits the ability of federal regulators to review an application. That review is limited to an applicant's ability to comply with particular provisions of the act and not even the entire act. The STABLE Act also gives applicants far more ability to contest a regulator's rejection of an application despite the more limited scope of review.

Similarly, it limits the ability of regulators to develop rules to the areas of reserves, capital, liquidity, risk management, and safety and soundness. Those are indeed important, but regulators should have the ability to develop rules that pertain to the Act as a whole, including important areas such as compliance with the Bank Secrecy Act and the Gramm-Leach-Bliley Act.

[5] See also the discussion below under "Failure to Address Bankruptcy."

Even in the specific areas where federal regulators can write rules as noted above, their authority is constrained in an unusual way. For example, it is vital to have capital and liquidity requirements in addition to requiring full reserves for tokens. Capital is necessary particularly in the event of losses unrelated to investment of the reserves—such as an operational or systems failure or a cyberattack. Liquidity rules are important to ensure adequate ability to meet redemptions—particularly since investments in repurchase agreements are allowed which may not be sufficiently liquid. But rather than simply directing regulators to develop appropriate capital and liquidity requirements (as I understand was agreed to last fall), the STABLE Act says those requirements (in the case of capital) "may not exceed what is sufficient to ensure the … issuer's ongoing operations" and (in the case of liquidity) "may not exceed what is sufficient to ensure … financial integrity."[6] While these revisions might not sound unreasonable, in practice they will likely lead to litigation by applicants and issuers who do not like a regulator's decision, and to protracted disputes.

Moreover, with respect to these requirements and any other risk management requirements, the STABLE Act ***requires*** Federal regulators to "tailor or differentiate among permitted payment stablecoin issuers on an individual basis or by category."[7] While regulators should have the discretion to do so, they should not be required to do so. This too will provoke litigation and protracted disputes and unnecessarily limit the authority of regulators. This is hardly a recipe for clarity and certainty of regulation.

As I noted earlier, this is a new and rapidly developing technology, and it has implications globally. None of us can predict what risks or circumstances will arise. The new stablecoin framework that we design will also operate in the shadow of the Supreme Court's decision in the Loper Bright case.[8] Therefore, instead of explicitly constraining authority, and providing language that enhances the ability of rejected applicants or disgruntled issuers to challenge regulators, the legislation should explicitly provide sufficient authority and discretion for regulators to respond to whatever risks and circumstances arise. To be clear, the Loper Bright decision *invites* Congress to delegate authority; it does not prohibit it. If ever there were a case where that is needed, where we do not want courts making judgements about complex, technical issues—such as whether there has been sufficient "tailoring" of rules or whether capital and liquidity requirements are "in excess" —it is here.

Failure to Address Bankruptcy. The legislation does not address the bankruptcy of a stablecoin issuer. This means that the standard corporate bankruptcy process would

[6] STABLE Act, Section 4(a)(4)(A).
[7] STABLE Act, Section 4(a)(4)(B).
[8] United States, Supreme Court. *Loper Bright Enterprises v. Raimondo*. *United States Reports*, vol. 603, 28 June 2024.

likely apply. A petition for a Chapter 11 reorganization would trigger the application of the automatic stay and begin a process that could take years. That is simply too slow for a stablecoin issuer, just as it is for a bank. The automatic stay means holders cannot redeem their tokens until the conclusion of the process. The conventional process creates far greater risk of collateral damage, where the issuer's bankruptcy can lead to other firms defaulting. It would also mean token holders would have an unsecured claim that is *pari passu* with all other unsecured debt claims. They must go to court to recover, but would share the reserves that are supposed to back tokens one-for-one with all other unsecured creditors, thus creating doubt that they would get paid back in full.

The legislation should create a dedicated resolution process. That process should ensure that holders get their money back as soon as possible. That process should be fast so that we minimize collateral damage. It should involve the appointment of a dedicated receiver, and it should be designed to work for federal and state-chartered issuers. States do not write their own bankruptcy laws, so while a state-chartered issuer might be able to create a trust structure that reduces some of the risks related to a standard corporate bankruptcy process, we would be better off to create a process that will minimize risks and damage for both federal and state-chartered issuers.[9]

It is my understanding that the fall bipartisan agreement included having a dedicated resolution process that involved the appointment of a receiver such as the FDIC or the NCUA.

As noted above with respect to the use of trusts, there are other measures that might help minimize the consequences of a bankruptcy, such as structural subordination of assets. Similarly, holders claims can be "prioritized," as in the GENIUS Act.[10] But these measures are not as good. For example, a holder with a "prioritized" claim would still need to bring an action to recover money and would still be subject to the automatic stay.

In addition, even stating that holders claims are "prioritized" may be illusory. Under the STABLE Act (and the GENIUS Act), issuers are entitled to pledge assets as collateral to secure a repo transaction for the purpose of creating liquidity. Participants to repo transactions have super-priority in bankruptcy. As my colleague Professor Dan Awrey has explained, they may be able to seize reserve assets without even having to create a post-bankruptcy claim.

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[9] For a general discussion of risks of bankruptcy, see Howell et al. (2022), p. 5; Awrey, Dan. "Money in the Shadow of Bankruptcy." *Beyond Banks: Technology, Regulation, and the Future of Money*. Princeton University Press, 2025.

[10] GENIUS Act, Section 9.

The risk created by this ability to pledge is substantial. One can imagine a Bear Stearns-like scenario where a stablecoin issuer is facing liquidity pressures. It could enter into a repo contract covering a large part—or even all—of its reserves to generate liquidity. But news of the contract could put further pressure on its liquidity as customers anticipate that there will be fewer reserve assets available for distribution post-bankruptcy. Thus, subjecting stablecoin issuers to bankruptcy while letting them pledge assets for liquidity purposes exposes holders to greater risk.[11]

Moreover, users of other stablecoins might fear that other issuers will do (or might have already done) the same thing, in light of market conditions, similarity of business models, and equivalent restrictions on assets and activities. This could create conditions for the type of contagion we saw after the failure of the Reserve Primary Fund in September 2008 (the money market fund which had less than 1.5% of its assets in Lehman commercial paper at the time that Lehman filed for bankruptcy). Litigation related to its failure continued until September 2013.[12]

If we really want to promote stablecoins as a viable general means of payment, then creating an appropriate bankruptcy process supports that goal. It can give users of stablecoins more confidence about using them.

Failure to Adequately Address the Risks of Financial Crime and Evasion of Sanctions. Although the legislation makes clear that the Bank Secrecy Act or BSA applies to stablecoin issuers, the provision is not sufficient to address the risks related to financial crime and evasion of sanctions. For one thing, the STABLE Act doesn't give Federal authorities the power to develop appropriate rules to implement its requirements, as these may need to be customized.

The BSA is designed for centralized intermediaries. While a stablecoin issuer is a centralized intermediary, one need not interact with a stablecoin issuer to acquire, transfer, redeem or otherwise cash out a stablecoin. Thus, imposing requirements on stablecoin issuers pertaining to anti-money laundering (AML) and combatting financial terrorism (CFT) is not sufficient. One need not even interact with another centralized intermediary, such as a so-called "off ramp" or "on-ramp" that itself might also be subject to the BSA—that is, crypto trading platforms or other entities on which one may acquire a stablecoin or redeem or sell it for fiat currency.

While the existing BSA/AML/CFT framework imposes compliance obligations on covered institutions, the actors and services within the digital asset world do not always fall within its categories. Stablecoins are transferred on decentralized

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[11] I am grateful to Professor Awrey for our discussions on these issues.
[12] Raymond, Nate. "Settlement Reached in Reserve Primary Fund Lawsuit." *Reuters*, 7 September 2013.

blockchains, and transfers can be made from one self-hosted wallet to another. The "Travel Rule" adopted by the Financial Action Task Force extends the regulatory perimeter by requiring centralized entities to share or obtain information about transferors and transferees, but that only extends the perimeter one "hop" in the best case. Moreover, there are intermediaries in jurisdictions that do not comply with such rules or do a poor job enforcing compliance. It is easy to create a crypto exchange in a non-compliant jurisdiction at which stablecoins could be transferred, thus creating a means for money laundering.

This legislation—as well as any other regulatory framework for digital assets—needs to be far more creative and comprehensive in addressing these risks. We need to expand the regulatory perimeter to include other actors and services in the DeFi world, and expand the methods for addressing these risks. There have been many suggestions in this regard as well as innovations by other countries in their frameworks.[13] None of that appears to be reflected in this legislation. The legislation should address the risks that self-hosted wallets pose. (The legislation appears to address self-hosted wallets only in the customer protection section.) It should require stablecoin issuers to aggressively monitor all transactions on chain and freeze accounts of suspicious parties. It could give the Office for Foreign Asset Control explicit extraterritorial jurisdiction over transactions in stablecoins pegged to the dollar as they generally would have over dollar transactions. And it should encourage the development of other technologies that might assist in addressing this risk (such as being able to program stablecoin smart contracts to reject transactions of parties that have not been vetted by an appropriate authority).

There have been recent reports of the use by terrorists of stablecoins to evade sanctions and launder money.[14] It is impossible to know with any certainty the scale of such activity. As the digital asset and stablecoin market grows, however, it is likely to grow, absent sufficient steps to prevent it. Whether stablecoins can become a widely used means of payment turns in large part on whether we can adequately address this risk.

Failure to Address Affiliate Relationships. While the STABLE Act limits the activities of a stablecoin issuer to those directly pertaining to stablecoins, there are no

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[13] *See*, *e.g.*, Adeyemo, Wally. "Remarks by Deputy Secretary of the Treasury Wally Adeyemo at the 2023 Blockchain Association's Policy Summit." 2023 Blockchain Association's Policy Summit, 29 November 2023; Hall, Eric, et al. "December Brings Flurry of Treasury Activity Against Virtual Currency Services." *DLA Piper*, 19 December 2023; Rettig, Rebecca, et al. "Genuine DeFi as Critical Infrastructure: A Conceptual Framework for Combating Illicit Finance Activity in Decentralized Finance." *SSRN*, accessed on 7 February 2025.

[14] *See*, *e.g.*, Berwick, Angus and Ben Foldy. "Inside the Russian Shadow Trade for Weapons Parts, Fueled by Crypto." *Wall Street Journal*, 1 April 2024 ("'Inside the Russian Shadow Trade,' *Wall Street Journal*"); Berwick, Angus and Ian Talley. "Hamas Needed a New Way to Get Money From Iran. It Turned to Crypto." *Wall Street Journal*, 12 November 2023 ("'Hamas Needed a New Way to Get Money From Iran,' *Wall Street Journal*").

restrictions on the entities that could own an issuer or on its affiliate relationships, or on transactions with those affiliates. While one can debate whether to import wholesale the restrictions of the Bank Holding Company Act, we must address the risks of concentration of power, the separation of banking and commerce, and affiliate relationships.

With respect to affiliate relationships, we should consider transactions and arrangements that pose conflicts of interest. What types of transactions should be permitted between a stablecoin issuer and its parent entity? Can a crypto trading platform favor a particular stablecoin in which it has an economic interest? Can an affiliate use the data acquired by a stablecoin issuer for other purposes? The legislation is completely silent about such issues, nor does it appear to give regulators any ability to develop rules to address such concerns.

The risk that big technology companies might become stablecoin issuers and thereby acquire even more data about us should be obvious. Indeed, there is nothing in this legislation that would prevent Meta, formerly Facebook, from relaunching its Libra proposal. One can easily imagine that Meta could find a state to grant a charter, perhaps because the state wanted to attract Meta's business. (Meta already holds money transmission licenses in 48 states.[15]) It could then operate without federal oversight.

Failure to Address Third Party Vendors and Contracted Services. The legislation also does not appear to address the risks that third party vendors and contracted services might pose, nor is it clear whether regulators would have the power to do so in the absence of any mention of the issue, since their power to implement rules is limited as noted above. It is my understanding that the bipartisan agreement reached last fall included provisions addressing this issue.

Lack of Enforcement Power. In light of the fact that the stablecoin market is already sizeable, the STABLE Act is a bit like putting a lock on the barn door after the horses have left. That is, it fails to address in a meaningful way the risks that already exist in the market. Tether is and has always been the largest stablecoin issuer, with a market capitalization today of $142 billion.[16] Tether is incorporated offshore. For years now, many commentators and officials have expressed concerns about its practices, including the nature of its investments, its lack of transparency, and the use of Tether for money laundering and evasion of sanctions.[17] It is not clear whether the STABLE

[15] "Money Transmitter Licenses." *Meta*, accessed on 7 February 2025.
[16] "Tether Market Cap." *CoinMarketCap*, accessed on 7 February 2025.
[17] *See*, *e.g.*, New York State, Office of the Attorney General. *Attorney General James Ends Virtual Currency Trading Platform Bitfinex's Illegal Activities in New York.* New York State Attorney General Press Release, 23 February 2021; Prentice, Chris. "Crypto Firms Tether, Bitfinex to Pay $42.5 [Million] to Settle U.S. CFTC

Act would affect Tether or the dominance of its stablecoin. Although the legislation says it is "unlawful for any person other than a permitted payment stablecoin issuer to issue a stablecoin for use by any person in the United States,"[18] there are no specific enforcement provisions or penalties attached to that language. The legislation should include such provisions and it should give the Attorney General enforcement power. It should explicitly have extraterritorial application (with explicit penalties and Attorney General enforcement power), or else the courts might rule that it does not. In addition, it should prohibit trading platforms from listing unauthorized stablecoins, so that there is no doubt as to legislative intent. The jurisdictional issue—how to define platforms that should be subject to such a provision—can be addressed in the manner I have discussed below under "Decentralization and Market Structure."

Of course, even if such enforcement provisions are added, the state chartering path might offer a way for a stablecoin issuer that cannot or does not wish to meet federal requirements to remain in business without changing any practices. An issuer might persuade a state to design regulations to accommodate the issuer's registration, particularly if the issuer brought business to that state. Tether is an extremely profitable firm and surely has the ability to offer such inducements.[19]

No Prohibition on Payment of Interest. The STABLE Act does not prohibit an issuer from paying interest on a stablecoin. To date, there has been a substantial disincentive for issuers to pay interest because a stablecoin might then be deemed a security. But the legislation would eliminate this disincentive because it explicitly says stablecoins are not securities. We should tread carefully as we are in the early days of this market. We should either prohibit the payment of interest or at least empower regulators to do so. The payment of interest could make stablecoins an investment option and not just a payment mechanism. It could lead to the creation of financial products similar to money-market funds, only this time they could be chartered and supervised by each of the fifty states.

Investments of Reserves. I agree with the STABLE Act's limitation on investments to essentially high quality liquid assets. I wish to suggest a few modifications:

- *Central Bank Reserves*. The language includes "central bank reserves."[20] It is not limited to U.S. dollar central bank reserves, even though all other categories of investments are dollar-based. Assuming the intent is

Charges." *Reuters*, 15 October 2021; "Inside the Russian Shadow Trade," *Wall Street Journal*; "Hamas Needed a New Way to Get Money From Iran," *Wall Street Journal*; Faux, Zeke. "A Thin Crust of Ice." *Number Go Up*. Crown Currency, 2023.

[18] STABLE Act, Section 3.

[19] *See* Kharif, Olga. "Tether Sees $10 Billion in Net Profits for 2024." *Bloomberg*, 20 December 2024.

[20] STABLE Act, Section 4(a)(1)(A)(v).

to permit only U.S. dollar central bank reserves, it should be revised. (While the STABLE Act is not well suited to encouraging non-dollar based stablecoins, and I assume its drafters did not intend to do so, if it wishes to do so, one should at least say "central bank reserves in the same currency as the stablecoin.")

Moreover, a stablecoin issuer can only hold central bank reserves if the Federal Reserve permits it to have a master account, and the Federal Reserve has taken the position that it does not currently have the authority to do so. While there are many issues as to whether the Federal Reserve should do so that deserve full consideration, in a process that involves public comment, the STABLE Act should give the Federal Reserve the *authority* to do so. Again, while there are multiple issues that should be considered before permitting stablecoin issuer master accounts, investing reserves in U.S. dollar central bank reserves would eliminate any risk related to intermediation.

- *Repurchase Transactions*. Issuers are permitted to invest in repurchase transactions with a maturity of seven days or less that are backed by Treasury securities.[21] Query whether that is desirable since such instruments can be highly illiquid for a participant that does not have access to the Federal Reserve discount window.

- *Absence of language on diversification and concentration of risk*. The STABLE Act does not say anything about diversification of investments. We should not overlook the lessons of the failure of Silicon Valley Bank, when a stablecoin issuer had a huge amount of deposits in a single bank, most of which was uninsured. While regulators have authority to issue rules related to reserves, general language directing regulators to address issues of diversification, by type of investment as well as recipient, should be included. The legislation need not and should not set specific requirements. But a general direction and authorization is needed particularly given the risks noted above with respect to regulators' constrained authority and the possibility that state rules vary from federal requirements.[22]

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[21] STABLE Act, Section 4(a)(1)(A)(iv).
[22] See above under "Insufficient Standards and Supervision for State-Chartered Issuers" and "Insufficient Authority to Regulate."

Decentralization and Market Structure

I would also like to make a few comments on decentralization in light of the Subcommittee's proposed legislation to require a study of decentralization by the SEC, the CFTC, and the Treasury, as well as the focus on decentralization in relation to market structure regulation. This is a key concept in the Financial Innovation and Technology Act for the 21st Century (FIT 21), which I assume the Subcommittee will later consider.

Blockchain and smart contracts offer the potential to automate certain functions and reduce the role of traditional intermediaries exercising discretion. However, the term "decentralization" and "DeFi" are used to describe all sorts of protocols, processes and services taking place in the crypto universe that vary tremendously with respect to the degree to which they are automated, decentralized or distributed, or with respect to the degree to which firms or human actors exercise control or discretion. DeFi protocols and services often have what some in the academic community have called "centralization vectors"—that is, ways in which there is some degree of control or discretion, including administrative keys that permit modification of code or restricting access.[23] It is also the case that there may be an automated protocol but a related service provided by a firm or person in which discretion and control are being exercised. Therefore, the term "decentralization" is of little value. We need more precise analysis and language to determine whether and how regulations might need to be adjusted.

In addition, calling something "decentralized" or "DeFi" should not be an exemption from regulation. On the contrary, we should look at the processes being performed or the services being provided and consider what are the best ways to achieve the regulatory goals that are nevertheless present. While automation and ability for users to control assets may reduce certain types of risks that are often the targets of regulation, they may introduce others, and in any event we must still ensure that the regulatory goals of consumer and investor protection, market integrity and transparency, financial stability, or prevention of financial crime are achieved.

A simple example is to imagine a "decentralized" or automated platform for the trading of Treasury securities that becomes a dominant, and indeed systemically important, platform given the importance of that market. Even if such a platform truly was automated and not subject to the control of a human operator, we would still want to make sure various regulatory goals were achieved.

[23] Shuler, Katrin, et al. "On DeFi and On-Chain CeFi: How (Not) to Regulate Decentralized Finance." *Journal of Financial Regulation*, vol. 10, no. 2, 2024.

When it comes to market structure, I do not think the concept of "decentralization" is the proper way to distinguish between tokens that should be considered securities and those that should be considered commodities, or the way to draw the line between the jurisdiction of the SEC and that of the CFTC. It is difficult to measure and not a good indicia of whether the securities law or commodities law framework should apply.

The FIT 21 Act in particular proposes a way to delineate jurisdiction between the agencies that is based on decentralization, how a digital asset is acquired, and who holds the digital asset. It is a very complicated test that is difficult to apply. Among other things, the classification of a token could change over time—not simply from a restricted security to a digital commodity, but back again. The "self-certification" process is an invitation for abuse. It is not clear there would even be sufficient information to apply the test accurately, and the decentralization component of the test has metrics that hardly seem "decentralized." The application of the test could also fracture the market with respect to any individual token—some might be commodities and some securities. It would not bring the regulatory clarity that its proponents claim.

Moreover, it could undermine our capital markets generally, by making it easy to evade the regulation that has been a foundation of their strength and attractiveness globally. The issue is not only that we must make sure the SEC retains authority for digital assets that have indicia of investment contracts. There is the risk that stocks, bonds and other securities could be wrapped in a digital token issued on a decentralized blockchain in an attempt to avoid securities law regulation altogether. Thus, the legislation could create the risk of wholesale regulatory arbitrage for securities of all sorts.

We should proceed carefully in addressing the market structure question. I am pleased that the Subcommittee is considering stablecoins first. I think it is critical to get legislation pertaining to stablecoins done and then build on that. It is a product that is critical to digital assets and has great potential, as discussed above. What regulators learn in addressing this market will be useful as we think about other aspects of digital asset regulation. I also think we should tackle the market structure question by bringing the SEC and CFTC together. I am pleased to see the Subcommittee suggest a joint committee of the two agencies in one of its legislative proposals.

I have previously called for such an approach. Former SEC Chair Jay Clayton (a Trump appointee) and I proposed that the two agencies get together to develop joint

rules for the crypto market.[24] Professor Howell Jackson and I also wrote a paper detailing how the two agencies could develop joint rules through a self-regulatory organization.[25] (I use the term SRO consistent with our laws—which is entities that are overseen in numerous ways by the regulator, as described in our paper. I do not mean simply an organization of industry representatives that claims it can regulate participants.)

Another way to provide a regulatory framework and some clarity to the market without drastically revising the securities laws is as follows: Congress would assign responsibility for regulating the "spot" market for tokens that are not securities to the CFTC, but it would not revise the definition of securities. It would also not define a new category of "digital commodities" that are deemed not to be securities. Instead, it would give the CFTC authority over any trading platform that trades bitcoin or ether. That would be a simple way to establish jurisdiction over the market—it is easy to identify such platforms, and there is no significant platform that does not trade those tokens. It would prescribe some core principles and direct the CFTC to develop rules to implement such principles—like prevention of fraud and manipulation, prevention or minimization of conflicts of interest, protection of customer assets, disclosure to investors, reporting requirements, and so forth. It would also mandate that those rules should apply not only to the trading of bitcoin and ether, but to ***all other tokens*** listed on the platform. That is critical to achieving full investor protection. It would further specify, however, that the platforms are not to trade securities, and that the CFTC and SEC should consult to determine if a token is a security. If a token is deemed a security, it would be removed from the platform (and required to be traded on a securities platform) unless the SEC agreed otherwise. There would be provisions to deal with disagreements between the agencies.

This would create an immediate framework for regulation that protects investors without rewriting the securities laws. It could be seen as a permanent or interim solution. As the market develops and we gain more knowledge, the approach could be refined. But it could very quickly bring investor protection to the market without undermining decades of securities laws and without creating more questions than answers.

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[24] *See* Clayton, Jay and Timothy Massad. "How to Start Regulating the Crypto Markets—Immediately." *Wall Street Journal*, 4 December 2022; Clayton, Jay and Timothy Massad. "A Path Forward for Regulating Crypto Markets." *Wall Street Journal*, 7 July 2023.

[25] *See* Massad, Timothy G. and Howell E. Jackson. "How to Improve Regulation of Crypto Today—Without Congressional Action—and Make the Industry Pay For It." *Hutchins Center Working Paper*, no. 79, October 2022.

I would like to make comments on two other issues in the Executive Order, as the Subcommittee may be asked to consider these issues in the future, one being the crypto stockpile and the other concerning the language prohibiting a CBDC.

Bitcoin Strategic Reserve or Crypto Stockpile

The working group created by the Executive Order is directed to "evaluate the potential creation and maintenance of a national digital asset stockpile and propose criteria for establishing such a stockpile, potentially derived from cryptocurrencies lawfully seized by the Federal Government through its law enforcement efforts."[26]

I believe the creation of a crypto stockpile is a bad idea for several reasons, as is the idea of a bitcoin strategic reserve. The President suggested the latter during the campaign, and some have gone even further by suggesting that not only should the government hold on to bitcoin it seizes but also the government should actually buy more bitcoin.

Assets seized through law enforcement efforts are typically sold in auctions or returned to the victims of the crimes which led to the seizures. I do not believe we should make an exception and hold on to crypto. It would create an unlevel playing field in this regard, and there is no good argument in its favor.

The expectation that prices of crypto will appreciate is not a good reason to retain what we seize or to buy more. There is no assurance prices will appreciate, of course. Crypto prices have been extremely volatile and there are plenty of examples of tokens that shot up in price only to later crash (e.g., FTT (the FTX token), or Luna, the token backing the Terra stablecoin that collapsed). A better argument can be made on that basis for holding on to equity securities that the government seizes—they have a longer and more consistent record of appreciating in price and are just as easy to store, but the government should not retain, or generally invest in, those either.

There is no strategic reason for the government to hold on to bitcoin or other crypto tokens. Doing so would not serve an important use case as there is with oil, for which we created a strategic reserve. It is also neither necessary nor desirable to create such a stockpile or reserve to advance the country's leadership in this technology. The way to do that is to create legal frameworks that allow for responsible private sector innovation. It is more likely that government investment would distort policy choices and create risks of conflicts and corruption. Finally, the idea that a bitcoin reserve

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[26] Executive Order 14178.

would support the dollar or the monetary system has been thoroughly debunked by George Selgin at the Cato Institute and others.[27]

Executive Order Language on a CBDC

The Executive Order language concerning a CBDC also raises concerns.

I recognize there are strong views on the subject of a retail CBDC among the members of this Subcommittee and I do not wish to focus on that issue. However, if we want the private sector to develop digital asset and blockchain technology to facilitate tokenization of assets of real value, and utilize atomic settlement so that transactions involving such assets settle instantly and efficiently on chain, the federal payments infrastructure operated by the Federal Reserve must be compatible. Banks (and other payment institutions that might be granted access to the system in the future) must be able to settle the digital asset transactions of their customers in a compatible and efficient manner. While settlement between banks is already electronic, of course, there may be systems improvements that are necessary to facilitate interbank settlements involving their respective on-chain atomic settlement transactions.

In addition, the dollar is the primary currency for international trade and transactions. With the growth of stablecoins and digital assets as well as fast payment systems generally around the world, we must make sure that the technology for cross-border payments flowing through the federal payments infrastructure remains at the cutting edge. That does not require the issuance of a CBDC that individuals would hold. But it may mean allowing the Federal Reserve to continue to do necessary research and development.

Unfortunately, the language in the Executive Order has such breadth that it raises concerns as to whether any such research and development can continue. That is because it defines a CBDC very broadly, as "a form of digital money or monetary value, denominated in the national unit of account, that is a direct liability of the central bank," and it prohibits "any action to establish, issue, or promote CBDCs within the jurisdiction of the United States or abroad" and any "plans or initiatives" related to the creation of a CBDC.[28]

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[27] Selgin, George. "The 'Digital Gold' Fallacy, or Why Bitcoin Can't Save the US Dollar." *Cato Institute*, 29 November 2024. *See also* Carter, Nic. "I Don't Support a Strategic Bitcoin Reserve, and Neither Should You." *Bitcoin Magazine*, 30 December 2024.
[28] Executive Order 14178.

If the Subcommittee wants to bring about a golden age of digital assets, it should make sure our core payments infrastructure can handle it.

Finally, I know that many are opposed to a retail CBDC because they are concerned the government would use that technology to monitor transactions of individuals, collect data on individuals, target political opponents, or even censor transactions. We have witnessed an unprecedented seizure of the Treasury payment system recently in a manner that creates many of the same risks. That system is critical to the operation of the government and our economy. Approximately 90% of all government payments flow through that system. Approximately 1.3 billion payments, having a value of over $6 trillion, were made last year. Tens of millions of individuals depend on it for direct payments or for payments made by institutions paid through that system. Access to that system is normally limited to a handful of people even within Treasury. But in this case, a few young programmers who had no prior experience with the system or even working in the government obtained access. While the courts have at least temporarily limited their access,[29] the seizure creates risks similar to those that many worry would come with a retail CBDC. It creates the possibility that payments could be stopped or "edited" notwithstanding the absence of legal authority to do so, thereby usurping the power of Congress. It creates the risk that huge quantities of data on individuals could be harvested and used in inappropriate ways. It poses additional serious risks—including simply interfering with or damaging the system in such a way that payments are disrupted, or undermining confidence in a manner that negatively affects the credit and standing of the United States. I am grateful that the Ranking Member of the Committee, the Ranking Member of the Subcommittee and other members protested this action.

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The Trump Meme Coins

Finally, although the Trump meme coins are not part of the Subcommittee's agenda, they cannot be ignored when the Subcommittee's desire is to chart a path toward a "golden age" of crypto. It is difficult to imagine an action that the President could take which would be more contrary to the spirit and opening words of the Executive Order, issued just a few days later, which is to "promote United

[29] *See* United States, United States District Court for the District of Columbia. *Alliance for Retired Americans v. Bessent* [Court Order]. Docket no. 25-0313, 6 February 2025; United States, United States District Court for the Southern District of New York. *State of New York v. Trump* [Court Order]. Docket no. 25-1144, 8 February 2025. *See also* United States, United States District Court for the District of Columbia. *Alliance for Retired Americans v. Bessent* [Complaint]. Docket no. 25-0313, 3 February 2025; United States, United States District Court for the Southern District of New York. *State of New York v. Trump* [Complaint]. Docket no. 25-1144, 7 February 2025.

States leadership in digital assets" and "responsible growth and use of digital assets."[30] One does not have to be a digital assets expert to understand why the issuance of the meme coins contradicts the spirit of that order and was plainly wrong. It was a money grab and a conflict of interest. The potential for conflicts of interest will also continue over time. Companies and countries looking to curry favor with the Administration or seeking government action may believe it is in their interest to purchase the coins to show their support. That risk is heightened by the structuring of the issuance, because additional tokens will be released over the next four years which will presumably generate additional revenue to the Trump Organization, which creates incentives for others to push up the price.

It is a black eye for digital assets. It is exactly the kind of speculative behavior that we have seen too much of and it reinforces many of the negative perceptions of digital assets. It is simply, as one observer said, a "classic meme-coin pump and dump scheme."[31]

Conclusion

I share your desire to chart a path to a "golden age" of digital assets. It is an exciting and promising technology. I believe that path requires a regulatory framework that is not only clear, but adequately addresses the issues I have talked about today (and others). The United States created an excellent regulatory framework for securities markets beginning in the 1930s, one that remains a model for countries around the world and has been a foundation for our markets to become the most important in the world. We can do the same here.

[30] Executive Order 14178.
[31] Khalili, Joel. "The Trump Memecoin's 'Money-Grab' Economics." *Wired*, 20 January 2025 (citing Interview with Jacob Silverman).