



# *FedFin Client Report*

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Wednesday, April 10, 2023

## **HFSC-Ag Hearing Splits on Party Lines Over Need for New Crypto Framework**

**Client Report: CRYPTO43**

### **Executive Summary**

Today's joint HFSC-House Ag hearing on assessing crypto's regulatory gaps saw bipartisan calls for Congressional action, but none on what that should be done. HFSC Chairman McHenry (R-NC) and HFSC Republicans pressed strongly for a new regulatory framework to ensure regulatory certainty and draw clear lines between the SEC and CFTC. HFSC Ranking Member Waters (D-CA) indicated that cryptoassets did not warrant an entirely new construct, instead favoring targeted legislation on issues such as stablecoins. House Ag Members on both sides of the aisle agreed that the CFTC should be given authority over spot markets and additional resources, but did not directly address giving the SEC broader authority as proposed in the Senate Ag sweeping [crypto bill](#). While this joint approach to digital assets is unprecedented, the GOP leadership's decision to strip the SEC of some of the authority it claims and to craft a new regulatory category for some digital products faces stiff odds against enactment.

### **Analysis**

#### ***Opening Statements***

HFSC Chairman McHenry, the Chairmen of each committee's digital asset subcommittee, and Ranking Member Caraveo (D-CO) emphasized the importance of cooperation between the two committees and pushed for a new legislative framework. Ranking Rep. Lynch (D-MA) differed from his House Ag counterpart, arguing that a carve-out for digital assets is redundant and crypto firms need to comply with existing laws.

#### ***Testimony***

Witnesses represented Republic Crypto, Wilmer Cutler Pickering Hale and Dorr LLP, Kraken, the Web3 Foundation, Georgetown University, and the NYSE. All cited the lack of regulatory clarity as the primary as a primary concern. Some also claimed the US was falling behind other jurisdictions and the loss of innovation and jobs necessitated rapid action.

#### ***Q&A***

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- **Security vs. Commodity:** House Ag Chairman Thompson (R-PA) described the current process that differentiates between securities and commodities as “unclear, unworkable, and impractical.” Chairman Johnson (R-SD) emphasized the importance of drawing a clear line for regulators between a security and a commodity, asking under what conditions a digital asset is fully commoditized. The witness representing Wilmer Cutler Pickering Hale and Dorr LLP noted that existing derivatives markets and past regulatory enforcement actions are helpful clues, but crafting an exact line is difficult. Rep. Steil (R-WI) asked if it is correct to assume that the “efforts of others” requirement in the Howie Test is triggered when digital asset holders contribute to the development of a network, with the witness representing Kraken stating that it likely does not. Reps. Timmons (R-SC) asked if it is possible for national securities exchanges to list both Bitcoin – a consensus commodity – and a security under current law, to which the witness representing Kraken stated it was not possible. Rep. Molinaro (R-NY) asked if an SEC regulated exchange did, would it complicate CFTC enforcement authority. The law-firm witnesses stated that it would. Rep. Nickel (D-NC) asked the Kraken witness if SEC guidance would aid exchanges in determining if an asset is a security; he replied that it would.
- **Disclosures:** Rep. Hill (R-AR) asked what features of digital assets are not captured by the current disclosure regime and how intermediaries could provide that information. The witness representing Kraken stated that many technical aspects that users demand are not required to be disclosed and that exchanges like Kraken can facilitate disclosures through the data they collect on digital asset offerings.
- **International Competition:** Reps. McHenry, Lucas (R-OK), and Jackson (D-IL) argued that the US falling behind major jurisdictions such as the EU and the UK is costing jobs and innovation. Rep. Steil asked the witness from the Web3 Foundation how the EU’s crypto environment differs from the US, with the witness replying that regulatory certainty is the most impactful difference.
- **SEC Registration:** Rep. Torres (D-NY) argued that SEC registration is unduly difficult and “not just a form on a website.” After the witness from Kraken stated that it had zero digital assets registered with the SEC, Reps. Casar (D-TX) and Sherman (D-CA) voiced concern that existing investor protections are not in place because there are exchanges that should be registered that are not.
- **DeFi:** Reps. Davidson (R-OH) and Torres (D-NY) stated that regulations should account for a digital asset’s level of decentralization, with Mr. Torres arguing that there should be a process that transfers a digital asset from securities to commodities regulation as it decentralizes.
- **Fraud:** Rep. Foster (D-IL) argued that maintaining a well-regulated crypto market would

be virtually impossible with the frequency of fake and fraudulent trades without traceable digital ID's. Rep. Davidson asked how to reconcile self-custody with know-your-customer rules; the witness representing Kraken claimed they are not incompatible and that exchanges are best suited to providing that information.

- **Financial Inclusion:** Citing crypto's negative returns over the past five years, Rep. Casten (D-IL) stressed that crypto is not suited for bridging the racial wealth gap.
- **(SRO):** Chairman Thompson asked if a joint SEC-CFTC SRO would benefit enforcement; the witness representing the law firm claimed that approach would take too long and that defining the jurisdictional line would be faster and more efficient.