JOHN REED STARK OPENING REMARKS

HEARING ON

"SEC ENFORCEMENT: BALANCING DETERRENCE WITH DUE PROCESS"

BEFORE THE UNITED STATES HOUSE OF REPRESENTATIVES FINANCIAL SERVICES COMMITTEE SUBCOMMITTEE ON CAPITAL MARKETS

TUESDAY, MAY 7TH, 2024

PREPARED STATEMENT

JOHN REED STARK, PRESIDENT, JOHN REED STARK CONSULTING LLC

Chairman Wagner, Ranking Member Sherman, and Members of the Committee: It is my honor and privilege to sit before you today. Thank you for inviting me to testify.

My name is John Reed Stark, and I am the President of John Reed Stark Consulting. I have spent the past 35 years or so working as a lawyer within the intersection of law, business and technology; including 18 years at the SEC (with 11 years as Chief of the SEC's Office of Internet Enforcement). For the past 20 years or so, I have also taught courses on securities regulation and cyber at Georgetown and Duke law schools and spent 5 years working at a leading data breach response and digital forensics firm.

Some catchphrases are awesome like, *May the Force Be With You*. Some catchphrases are hilarious like, *More Cowbell*. And some catchphrases are baseless and misleading like Theranos' mantra that, *One Tiny Drop Changes Everything*. The catchphrase of *SEC Regulation by Enforcement*, which I predict you will hear over and over again today, falls squarely into that last category – just plain false.

Today, I want to focus my remarks specifically on the digital asset industry. I do this both because crypto promoters represent the most important recent example of industry players accusing the SEC of unfairly policing the markets, and also because, in all my years, I have never witnessed such a well-funded, coordinated, and unfounded assault on the SEC and its mission.

Along these lines, the digital asset industry claims that by failing to provide "Fair Notice" of SEC rules to the cryptoverse, the SEC consistently violates the Due Process rights of legitimate crypto-financiers -- and that the SEC is a rogue regulatory outlaw, engaged in a self-serving, politically motivated power-grab, stifling innovation and impeding investor empowerment.

Remarkably, even after the debacles of FTX, BlockFi, Celsius, TerraForm Labs, Voyager and so many other crypto-failures, the digital asset industry continues to repeat these talking points in the vain hope that the more they say it, the more people will believe it.

But what the digital asset industry calls SEC Regulation by Enforcement, the rest of us simply call enforcing the law.

Since 1934, SEC enforcement has addressed emerging issues with common sense and flexibility, and without the benefit, or the hindrance, of detailed prescriptions, including for policing foreign

bribery payments, municipal securities fraud, derivatives scams, unlawful insider trading, fictional prime bank instruments, subprime grifts, non-existent eel farms, bogus ostrich farms and the list goes on.

So-called digital asset investors are betting on the efforts of the promoters and originators of these digital assets. That triggers the '33 Act.

So-called digital asset firms have coopted the nomenclature of the securities industry, calling themselves “exchanges,” “brokers,” and “market-makers,” creating a counterfeit veneer of investment-related assurances, integrity, expertise and regulatory supervision. That triggers the '34 Act.

The SEC enforcement division has had no choice but to act in the face of this conduct. Without the SEC’s vigorous enforcement, these digital financial behemoths will continue to operate in the shadows, with no transparency, no consumer protections and no accountability.

The bottom line is this: The sole Federal regulator charged by Congress to determine what is a security and enforce rules meant to protect investors has determined, through successive, Commissions, led by Republican and Democratic Chairs, that nearly all crypto offerings are securities. And the courts have agreed with the SEC’s analysis, time and time again.

Meanwhile, the promoters of digital assets claim to be champions of a digitally transformative technological revolution that is the future of finance and money. Yet, in an oddly hypocritical twist, when the SEC comes knocking, they argue in court papers that selling digital assets is just like selling baseball cards, American Girl dolls or Beanie Babies.

Digital assets typically have: no cash flow, no yield, no employees, no management, no balance sheet, no product, no service, no history operations, no earnings reports, no proven track record of adoption or reliance, and the list goes on (and on).

How can any financial analyst, let alone any everyday investor, conduct a proper valuation amid such a boundless data vacuum? This is the real reason why it’s difficult for the issuers and intermediaries of these digital assets to register. They would be forced to answer tough questions about why investors should invest in those securities and forced to allow the SEC to examine, inspect and audit their books, records and operations.

Don’t get me wrong. The SEC is far from perfect. There are SEC cases and SEC rules that I believe are unfair, and I agree that SEC respondents should have a right of removal from SEC administrative courts. But on balance, the SEC is a remarkably successful regulatory agency and by enforcing its effective, proven and evolving U.S. securities law framework -- be it in the crpytoverse or elsewhere -- the SEC has not gone rogue, but is instead simply doing its job.

Of course, digital asset advocates may not like the outcome of SEC enforcement policing, but that doesn’t amount to an absence of Due Process and Fair Notice. It just means that the digital asset industry needs to get its act together and adapt to the laws that apply to it — not the other way around.

Thank you and I look forward to answering any of your questions.