Fact Sheet

Setting the Record Straight on Crypto, FTX and Sam Bankman-Fried, and Financial Regulators

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Updated November 29, 2022

1. The fiction of crypto was visible to all who wanted to see & weren’t blinded by cash or the pixie dust of “innovation” claims

No one should be shocked by FTX’s demise. The fiction (if not fraud) of crypto and its collapse were not hard to see as long as you weren’t on the payroll of FTX/crypto (directly or indirectly) and didn’t let FOMO and greed cloud your judgment. Not only did Better Markets see it and very vocally talk about it for more than a year now (including face-to-face with FTX’s former CEO Sam Bankman-Fried [SBF] and his high-paid team), but no less an authority than JP Morgan’s CEO Jamie Dimon clearly saw it (calling it “worthless” in 2021 and in 2022 saying “They are decentralized Ponzi schemes, and the notion that it’s good for anybody is unbelievable”). Ironically, Dimon got bullied into silence by his financial industry colleagues who wanted to get some of the crypto cash for themselves before the crash. As detailed below, the SEC and banking regulators also clearly understood the fraud of crypto, although the CFTC Chair decided to become a crypto cheerleader in an attempt to expand CFTC jurisdiction (even at the expense of gutting the SEC’s ability to properly regulate the capital markets).

The many crypto investors, enablers and legitimizers weren’t “seduced” by FTX and SBF as they now claim. They were just willing to accept whatever a billionaire with a “vision” said without doing the most basic due diligence or asking the most obvious questions if they thought it would make them rich. As Upton Sinclair said long ago, “it is difficult to get a man to understand something when his salary depends on his not understanding it.” FTX/SBF/crypto spent enormous amounts of money to make sure many people (including smart and influential people who should have known better) had gigantic financial incentives to not understand, see or question the fiction and fraud that is crypto.

As was made clear in our meeting with Sam Bankman-Fried and his team, where we asked tough factual questions that were not answered satisfactorily, it really didn’t take much to see that there wasn’t much to that “vision” other than hope, smoke, and the desire to make a quick buck (in fact, lots and lots of bucks). Unlike the many blue-chip investors like Sequoia Capital, who dreamed of dollars rather than do due diligence, we didn’t see either an “awesome” or “intimidating” intellect. They could have, as we did, reject that money (“$1 million or more” in our case), ask the tough questions, see that there wasn’t much there, and oppose their attempts to rip off retail customers, destabilize the markets, and gain access to the core of the financial system. To this day there is no valid use case for crypto, and no amount of personality cult or hype will change that fact.
2. **We don’t need new legislation or regulation; we need politicians to fully fund the SEC and to publicly support them in cracking down on the crypto industry**

Too many (again, who should know better) are still repeating industry talking points that the FTX collapse shows that new legislation and regulation is needed. That is not true. The current laws and rules are fully adequate to address the lawlessness going on in crypto. It has been estimated that around 80% of the crypto tokens comfortably fall within the longstanding, clear, black letter law definition of a security (around since 1933) and the remaining fall within the equally longstanding definition of commodity (around since 1936). The problem is that the crypto industry refuses to comply with the securities and commodities laws (that exist to protect investors, customers and financial stability) and, therefore, the vast majority of crypto products are unregistered securities and commodities being traded on unregistered exchanges.

The SEC (already spread thin policing all the capital markets) has used a significant amount of its limited resources to crack down on crypto, while staffing up to get the expertise necessary to fight crypto which is aggressively opposing everything the agency is doing on this front. (This began under Trump’s Republican SEC Chair Jay Clayton and continued under Biden’s Chair Gensler – yes, the SEC’s enforcement program against crypto has been bipartisan because the mission of the SEC is nonpartisan: to protect investors and markets.) However, throughout these efforts, no one has come to the defense of the SEC; in fact, the industry’s purchased allies have relentlessly bashed and attacked the SEC from all sides. The fact is that when the SEC has taken enforcement actions even against the most blatant crypto Ponzi and pump-and-dump schemes, the industry claim they are engaging in illegitimate “regulation by enforcement” and their financially backed political allies attack the SEC, attempting to pressure them into backing off. That has to stop. (That isn’t to say the SEC has been perfect and we have criticized them for not doing more, but, under the circumstances, particularly the relentless political pressure and interference, the SEC has done an admirable job.)

Those elected officials who are supposed to promote the public interest need to surge resources to the SEC and banking regulators so that they can enforce existing laws and rules. This should be a no-brainer given the loss of $2.5+ trillion, widespread lawlessness, illegality (if not criminality) laid bare over the last 12 months. (Yes, narrow, limited legislation is needed to regulate the crypto spot market and a couple of other aspects, but those “gaps” are small compared to the vast authority regulators already have and need to use more broadly and aggressively, no matter how much the CFTC wants to exaggerate the gap.

3. **Complying with existing SEC rules is not the problem; crypto’s refusal to comply with the law is the problem**

The problem is not, as Coinbase and others claim, that registering with the SEC “is not possible.” It is entirely possible, but crypto does not want to register because then crypto would have to comply with the customer/investor protection and financial stability rules like every other legitimate business. That would require crypto to, for example, (a) ensure disclosures and representations were fully accurate and materially complete (i.e., truthful transparency), (b) have systems and controls to protect customer assets, prevent internal theft and external hacks, etc., (c) eliminate conflicts of interests or mitigate them while fully disclosing them, (d) maintain accurate books and records, (e) have robust and effective management, risk, legal and
compliance programs, (f) be subject to routine examinations and supervision by the SEC and SROs like FINRA, and (g) have margin, liquidity, capital, etc., to fulfill all their obligations and prevent contagion in the event of severe volatility, significant losses, and crashes as we’ve been seeing for almost a year now. Complying with those regulations is entirely possible, but that would interfere with crypto’s profit maximizing predatory business model and it would reveal the Ponzi scheme that is at the core of the entire industry, as JP Morgan’s Jamie Dimon has highlighted.

4. Crypto is a lawless industry by choice

Rather than being a legitimate business that constructively engages with regulators and complies with the laws and rules as other legitimate companies do, crypto’s chosen strategy is to fight against regulators and regulation, while trying to get the easiest regulator and most favorable legislation. Sure, some in the industry said they wanted to “engage” with regulators (on terms they dictate) and even wanted to be regulated (albeit as little as possible), but the clear strategy has always been to just break the law and at the same time buy as many politicians as possible to get special interest legislation that would give it the weakest, most friendly possible regulator and regulation. They wanted the form and appearance of regulation without the substance of real regulation. That’s why the industry keeps pushing for the CFTC to be its regulator: the CFTC is the smallest and least funded financial regulator. Crypto believed it would be the easiest to capture, dominate, manipulate, and keep defanged. Confirming that view, the CFTC has been only too happy to join the industry in what is little more than a transparent jurisdiction-expanding power grab. The shamelessness of this reached its apogee when the CFTC’s Chairman not only de facto endorsed pending legislation that could have crippled the SEC’s ability to police the capital markets (the Lummis/Gillibrand bill), but also claimed that Bitcoin would double in price if his agency was its regulator.

Of course, a financial regulatory agency should not be an industry cheerleader concerned with boosting the price of particular financial product - that’s what industry-fawning financial regulators did in the early 2000s, which contributed to the 2008 crash. Sadly, the 2008 crash also shows why crypto’s strategy of lawlessly fighting existing regulators and trying to buy special interest legislation is not irrational and, in fact, has recent precedents: the financial industry did that in the 1990s. After similar money-soaked influence campaigns, the financial industry knowingly broke the Glass Steagall Act to get it repealed, which happened in 1998 and which enabled the super-sizing of banks and proliferation of too-big-to-fail firms, and, in 2000, got the Orwellian named Commodities Futures Modernization Act (CFMA) passed, which deregulated derivatives. Both of those special interest laws served the short-term profit maximizing interests of the industry but endangered the financial system and economy and led to the catastrophic financial crash in 2008.

5. Regulators prevented the crypto collapse from becoming a financial crisis and crash that precipitated bailouts

Regulators at the banking agencies and the SEC withstood enormous political and industry pressure to allow crypto access into the core of the financial and banking system. The only reason the ongoing crypto carnage hasn’t turned into a financial crisis, crash and bailouts is because those regulators did not allow those interconnections, which is what happened with subprime in the early 2000s leading directly to the 2008 crash.
No one should misunderstand: the pressure on those regulators was unimaginable, coming from (a) the crypto industry, (b) Wall Street’s biggest banks and finance more broadly who were salivating at the prospects of being a quick billionaire like SBF, and (c) the hundreds of political allies throughout Washington all purchased with crypto cash. Because those regulators held the line (again, on a bipartisan basis under Trump and Biden), crypto has operated parallel to, but not very interconnected with the core of the financial and banking system.

If that had happened, either via legislation or if the regulators cracked under the pressure, then there would almost certainly have been a catastrophe. After all, more than $2.5 trillion of value has been vaporized in less than 12 months and widespread illegal if not criminal conduct has been repeatedly exposed. If the leading industry legislation (the Lummis/Gillibrand bill) had been enacted in 2021 prior to the Bitcoin peak in November and the industry had been therefore legitimized with the appearance but not the reality of regulation, the crypto industry would have access to the Federal Reserve’s payments system, master accounts, etc. At the same time, the banking industry would almost assuredly have gone on a buying, selling, and trading crypto spree (with multiple layers of derivatives created, packaged and distributed throughout the world). Those deep and broad interconnections (which no doubt would have included large amounts of highly leveraged crypto products on the balance sheets of the too-big-to-fail banks) would have resulted in the crypto carnage spreading widely, with FTX’s collapse in particular igniting a contagion that would have quickly rippled throughout the financial system, just like the subprime-ignited crash in 2008. Moreover, if crypto and its allies like blue chip Fidelity had gotten their way, crypto would also have been stuffed into Main Street Americans’ retirement and pension accounts. As bad as it is that investors and customers have lost trillions of dollars, it pales in comparison to the damage that would have been inflicted if the country also suffered a financial crash that included untold amounts of losses in retirement accounts.

6. The CFTC failed to properly regulate crypto in general and FTX in particular

Not all financial regulators deserve to be praised; in fact, the CFTC appears to have failed miserably here. Rather than aggressively regulating crypto and skeptically scrutinizing its claims, the CFTC has spent most of its time cheerleading the industry and trying to expand its jurisdiction rather than worrying about investor, customer, and markets protections. In addition to the highly questionable conduct and statements of the CFTC Chairman discussed above in paragraph 4 (as well as de facto endorsing legislation precipitously), it appears to have been grossly deficient in scrutinizing the claims and conduct of FTX US Derivatives LLC (formerly LedgerX, a subsidiary of FTX US), which is a U.S. derivatives clearing organization licensed, regulated, and supervised by the CFTC (now in bankruptcy). The CFTC appears to have entirely missed what now appears to be multiple profound failures at FTX to meet fundamental corporate governance standards (including multiple reports of commingling of funds, gross mismanagement, conflicts of interest, improper relationship with affiliates like Alameda, etc.) if not also outright illegal conduct.

One would think that if the CFTC had been conducting even minimal supervision or examination of FTX, indications of these deficiencies and failures would have been identified and remedied or enforcement action would have been taken. Instead, the CFTC was working overtime to consider and appeared to be on its way to approving FTX’s application to radically change the structure of clearing organizations by reducing the layers of protections for clearinghouse resilience and permitting customers to be auto-liquidated 24/7/365. Yet, this CFTC- licensed and regulated entity, which has filed for bankruptcy protection, appears to have been
effectively insolvent or on the verge of collapse under the CFTC’s nose, in addition to and presumably at least in part due to having fatal risk, management, legal, and compliance flaws. (It is not yet clear how much of this was done by, through, or with the knowledge or participation of FTX US rather than FTX international or other affiliates, but, regardless, there appears to have been more than enough red flags flying high or just under the surface for a minimally competent CFTC to be alerted to very significant problems.)

7. **Crypto is still a danger and looking for a legislative bailout**

Even after the loss of $2.5+ trillion, widespread illegal conduct, the collapse of FTX, and the collapse or near-collapse of many other firms, the crypto industry is still pushing baseless arguments to save its businesses and get a legislative bailout. While Bankman-Fried and FTX may have been the face of crypto in Washington over the last few years, they were not alone in spending lots of time and money to influence the policymaking process. There are still dozens if not hundreds of lawyers and lobbyists working behind the scenes in much less visible roles for the industry and trying to bend the laws and rules to their favor.

In particular, they are now claiming that FTX’s collapse shows (a) the need for crypto-specific legislation and (b) the regulators especially the SEC failed by being hostile to the industry and (at the same time) by not enforcing the law aggressively enough. The baselessness of these industry talking points is clear: (a) they assume, incorrectly, that the supposed legislation would actually properly regulate crypto and protect investors, consumers, and financial stability (highlighted by claims that the laws would establish genuine “regulatory guardrails”), and (b) the industry has aggressively fought – and continues to fight - the SEC at every opportunity, slowing and obstructing the agency’s effort to enforce the law against it.

At this point, virtually any legislation would be a bailout for two reasons. First, the industry is seeking a legislative and regulatory “blessing” to grow the crypto business, which, as Bankman-Fried believed, “would usher in a wave of investment from traditional players scared off by the industry’s Wild West reputation.” Without the legitimacy that comes from virtually any legislation, the crypto death spiral will likely continue. Second, it wants and needs access to the federal safety net (meaning bailouts when they get in trouble) either directly by legislation that requires such access or by legislative provisions that enable interconnection with the banking system which would allow at a minimum indirect bailout.

While the disheveled, super-casual and earnest everyman that Sam Bankman-Fried presented himself to be may be gone, the rest of the industry is still working the dark corners of Washington to bend the laws and rules to benefit them, including those now sporting a reassuring suit-and-tie like the CEO of Coinbase. Sartorial differences aside, they are largely after the same things: minimal legislation and regulation to legitimize and expand their crypto businesses; weak oversight and enforcement to maximize profits; and interconnections with the banking system so that they can be bailed out when trouble strikes. The 2008 crash showed how bad that can be and responsible public officials should not let that happen again.

8. **The revolving door of former public officials selling out their public service and unlimited campaign contributions continues to corrupt policymaking**

The crypto industry is following the financial industry’s standard playbook of using all the levers of the influence
industry to buy special treatment for its special interests at the expense of the public interest. That means buying as many lawyers, lobbyists, PR flacks, academics, advocates, and influencers as possible, much of that detailed here. It also includes spending enormous amounts on media advertising and “sponsorships” to maximize highly favorable if not one-sided media coverage which engenders yet more advertising and sponsorship spending. Setting up “trade groups” and other front groups to push the industry’s messaging and goals is also part of the strategy. The key to that influence campaign is to buy as many former public officials and regulators as possible to gain access to their expertise, inside knowledge, and networks developed when they were supposedly working in the public interest. The importance of those revolving door hires cannot be overstated because they not only enable ready access to current policymakers and regulators, but also to the inside knowledge that enables crypto to precisely tailor and target their strategies to be optimally successful. That inside knowledge combined with connections is what makes revolving door hires so valuable and pernicious. Of course, that is all supported by the hundreds of millions of dollars spent on campaign contributions, which opens even more doors for the revolving door hires walk through. Without all that, crypto would not have the influence and access necessary to hijack the public agenda and subordinate the public interest to their special interests. Dealing with this legal corruption should be the highest priority.

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