

SHERROD BROWN, OHIO, CHAIRMAN
JACK REED, RHODE ISLAND
ROBERT MENENDEZ, NEW JERSEY
JON TESTER, MONTANA
MARK WARNER, VIRGINIA
ELIZABETH WARREN, MASSACHUSETTS
CHRIS VAN HOLLEN, MARYLAND
CATHERINE CORTEZ MASTO, NEVADA
TINA SMITH, MINNESOTA
KYRSTEN SINEMA, ARIZONA
JON OSSOFF, GEORGIA
RAPHAEL G. WARNOCK, GEORGIA
PATRICK J. TOOMEY, PENNSYLVANIA
RICHARD C. SHELBY, ALABAMA
MIKE CRAPO, IDAHO
TIM SCOTT, SOUTH CAROLINA
MIKE ROLANDS, SOUTH DAKOTA
THOM TILLIS, NORTH CAROLINA
JOHN KENNEDY, LOUISIANA
BILL HAGERTY, TENNESSEE
CYNTHIA M. LUMMIS, WYOMING
JERRY MORAN, KANSAS
KEVIN CRAMER, NORTH DAKOTA
STEVE DAINES, MONTANA

LAURA SWANSON, STAFF DIRECTOR
BRAD GRANTZ, REPUBLICAN STAFF DIRECTOR

United States Senate
COMMITTEE ON BANKING, HOUSING, AND
URBAN AFFAIRS

WASHINGTON, DC 20510-6075

November 30, 2022

The Honorable Janet Yellen
Secretary
U.S. Department of the Treasury
1500 Pennsylvania Ave, NW
Washington, D.C. 20220

Dear Secretary Yellen:

I am concerned about the risks posed to consumers, investors, and the financial system with the collapse of FTX.com and its related entities, including, among others, FTX US (collectively, FTX). As we continue to learn more details, the failure of this crypto exchange brings to mind the litany of financial firm failures due to the combination of reckless risk taking and misconduct. It is crucial that risks in this area are contained and do not spillover into traditional financial markets and institutions, and we draw the correct lessons regarding customer and investor protection.

The Department of the Treasury Report on Crypto-Assets: Implications for Consumers, Investors, and Businesses (Treasury Report) released in September and the Financial Stability Oversight Council Report on Digital Asset Financial Stability Risks and Regulation (FSOC Report) released in October 2022 highlight the potential consumer, investor, and financial stability risks of crypto assets and provide several approaches for Congress and financial regulatory agencies to address legislative and regulatory gaps in the crypto asset markets.

FTX's blowup highlights many of the troubling risks in the crypto asset markets discussed in the FSOC report, including vertically integrated market structures and platforms, opaque affiliated transactions, fragmented and illiquid trading markets, and an overdependence on leverage. Moreover, FTX's connections to other risky crypto firms likely deepened its losses and continue to send shock waves to other entities.

As the bankruptcy filings show, FTX failed to exercise basic corporate controls or risk management over its operations. In addition, FTX relied on its own proprietary crypto token leading to inflated valuations that further fueled irresponsible risk taking.

Although press reports indicate FTX's failure began as a liquidity crunch that quickly exposed an alarming fraud, FTX's business model combined three of the most common hazards in financial markets—leverage, illiquid holdings, and extreme concentration. In the past, that dangerous combination triggered the failure of Long-Term Capital Management, Lehman Brothers and other banks exposed to risky mortgage bonds, and recently, Archegos Capital Management. Each of those failures should have been a lesson to market participants. Unfortunately, that lesson is rarely learned.

In the wake of FTX's implosion, I ask that you coordinate with the other financial regulators to further work on the recommendations from the FSOC Report, including the development of legislation that would create authorities for regulators to have visibility into, and otherwise supervise, the activities of the affiliates and subsidiaries of crypto asset entities. As noted in the FSOC Report, single regulatory agencies currently generally do not have a comprehensive view of crypto asset entities' activities. I look forward to working on such legislation with you and the FSOC agencies.

In addition, I welcome the financial regulators' work to assess the impact of vertical integration in crypto asset markets and any recommendations as to whether additional legislation, or regulation, is needed to address risks and vulnerabilities.

As both reports recommend, I also urge the agencies to vigorously enforce existing laws to address financial stability risks and protect consumers. By using existing supervisory and regulatory authorities to address current and emerging risks, regulators can take on the significant noncompliance with current law among crypto asset firms and minimize, if not eliminate, the opportunities for regulatory arbitrage.

Finally, as the FTX failure makes clear, given crypto asset entities' broad use of proprietary crypto tokens combined with opaque financial arrangements and the reliance on arbitrary valuation and data sources, the financial regulatory agencies should continue to find ways to enhance entity and crypto asset disclosures, market integrity, and transparency.

I appreciate the Treasury Department's coordination of the President's Working Group on Financial Markets to consider the regulation of stablecoins. While Congress continues to consider legislation for stablecoins, I appreciate your input and partnership to develop a broad framework for all crypto assets. Congress and the financial regulators must work to get all of this right. As more crypto failures occur, the age-old adage is more true than ever—if it seems too good to be true, it probably is.

I look forward to working with you.

Sincerely

A handwritten signature in blue ink that reads "Sherrod Brown". The signature is fluid and cursive, with the first name "Sherrod" being more prominent than the last name "Brown".

Sherrod Brown

cc: Hon. Gary Gensler, Chair, Securities and Exchange Commission
Hon. Rostin Behnam, Chair, Commodity Futures Trading Commission
Hon. Jerome Powell, Chair, Board of Governor of the Federal Reserve System
Hon. Todd Harper, Chair, National Credit Union Administration
Hon. Rohit Chopra, Director, Consumer Financial Protection Bureau
Hon. Martin Gruenberg, Acting Chair, Federal Deposit Insurance Corporation
Mr. Michael Hsu, Acting Comptroller, Office of the Comptroller of the Currency