

You're listening to TechTank, a bi weekly podcast from the Brookings Institution exploring the most consequential technology issues of our time from racial bias in algorithms to the future work tech take takes big ideas and makes them accessible thanks for joining our Brookings TechTank Podcast I'm Darrell West senior fellow in the Center for Technology Innovation at the Brookings Institution today we're going to dive into the future outlook for the cryptocurrency landscape Donald Trump selection could set the stage for a sweeping policy overhaul fueled by his ambitious plans to make the United States the crypto capital of the world from a potential national bitcoin reserve to pro crypto regulations the sector is gearing up for a transformative period under Trump's leadership we're seeing the rise of bold proposals that could turn crypto into a mainstream asset boost institutional adoption and drive crypto prices to new heights it's not all smooth sailing because critics argue that this vision erodes regulatory oversight and weakens efforts to police money laundering and terrorist financing with a Republican controlled Congress the stakes are set for dramatic changes in crypto policy in the overall crypto landscape joining us today to discuss these issues is Aaron Klein he is a senior fellow at the center on regulation and markets at the Brookings Institution and he specializes in financial regulation in financial innovation.

Erin welcome to our TechTank Podcast. Hey thanks it's great to be back nice to have you again so we'll drive right in Donald Trump has said that he would like to make the United States the crypto capital of the planet how realistic is that vision well I mean to some degree it's realistic because it's already there there's more crypto held in by a U. S. based companies for clients the number one holder big coin in the world is Coinbase I by some estimates it's about ten percent of total crypto is there that's that's an American company other top companies like Blackrock in MicroStrategy have a lot of crypto assets the United States government by some estimates one percent of all big coin is already held by the United States government R. the question that I would say is what does that mean what does it mean to be the crypto capital of the world do you want to be the gold capital of the world do you want to be the stock bond capital of the world do you want to be the tobacco capital of the world these have all been used as payment instruments in the past and and I think sometimes lost enough in the humble blue is what exactly is crypto and why is it so valuable and that's something that I don't think Trump has any vision for or explanation there of.

So with Trump in office what changes should we expect from regulatory agencies like the securities and exchange commission or the treasury department regarding crypto oversight well the securities exchange commission has been very active in in policing what they think are as malfeasance in the crypto market and let me just step back and explain something that uniquely American the rest of the world regulates what we call capital markets with one regulator only in America do we have

to the securities and exchange commission which regulates stocks and bonds and the commodities future trading committee which regulates commodities options and derivatives and there's been a major debate about whether crypto is a security regulated by the SEC commodity regulated by the CFTC Congress has tried to weigh in on this and is found itself somewhat gridlock with generally speaking the SEC being a little more aggressive in policing what it thinks is malfeasance the Trump administration view seems to be our cabinet M. torrent let the market work deregulate let folks acting trade you can see this through some of the Republican appointees on the SEC who were in the minority who oppose many of the SEC's actions the opposition falls generally into two logical frameworks are the first is it is not a security and the SEC is never adequately defined what makes cryptos acuity or which cryptos are securities verse which are commodities because again all crypto assets are not the same and the way they're structured can have important legal and regulatory differences the second is these activities have been going on for a long time and why are you finding them right now.

There was just an action a couple days ago with the Republican nominee's opposed it and said this this person has been conducting the same business model for ten years how can you say just today that they've been in in error and not fail to register when they've been doing this for ten years and you didn't say that was a problem in the past so I think a new Trump regulated regulatory control will generally dial back the enforcement and dial back the claims that see crypto is a security that needs to be right regulated and registered in accordance with the securities and exchange commission's rules actually that's a very interesting now regardless of whether it's the SEC or the CFTC that ends up regulating crypto you just mentioned the possibility of trouble dialing back in for Smith what would that look like what would that actually mean for the market place if he tried to lighten the regulatory oversight well I mean we just you know we would start with less enforcement actions last season this is less orders to register last fines fewer investigations one thing folks happy she should understand is the way we regulate banks in this country is called prudential regulation regulators go in and examine banks and make sure that the banks are doing what they say their assets are where they are there loans or deposits their capital I accept your capital markets are regulated on the basis of conduct or market regulation this is very different so nobody's going in to broker dealers and assessing their capital management earnings liquidity right there just checking that their conduct is proper they're they're making ties in trade so it's much more of a regulatory regime that's reactive that if it sees something wrong it acts it finds it puts in enforcement actions but it's not R. prudential so you know in that space the simplest thing to do is just not to police the market is much is just check you are not in not proactively have investigations not look it malfeasance you know what figure that the buyers and sellers are sophisticated enough I am not investigate other things

they can do is not require registration so under the securities and exchange commission rules something called the how we test is a court case decided it basically says this is what makes something a security and if you're trading in securities you need to register with the SEC yeah W. and I can trade lunches back and forth those are assets they're hardly securities right if you and I traded stocks back and forth that might be a little bit different.

So what makes something you what makes something at the security versus an asset obverse also a distinction of a commodity so I think what you'll find here is a dial back you'll find speeches from regulators you'll find potentially commission votes attempting to define what is or isn't it fits under the Howey test and and you'd most likely find that it is possible that Congress could act with the Republican controlled Congress and make some of these decisions for the agency's so does sound like it's going to be a very active time on the administrative side now you just mentioned our Congress I'd like to get your views there so what can we expect from a house and Senate that now is going to be controlled by Republicans in regard to a possible crypto legislation and I would note that many crypto related firms and individuals spent millions backing pro crypto congressional candidates and they actually were very successful in electing them how might this shape the legislative agenda in the coming years yeah look I think there's going to be a real push for crypto legislation out whether it's in all crypto or just focuses on stable coin I think you're gonna see a lot of Republican support the issue at first really cleave the parties in both directions I Trump in his first term was hardly a crypto cheerleader I he he he was very skeptical I he didn't put any real pro crypto regulations specifically there nor did he kind of with the Republican Party into a crypto frenzy in his first term and many Republicans were inherently skeptical of crypto for a variety of reasons not the least of which is the large role the Chinese government may or may not be playing in many of these crypto markets as well as the Russian government and other international our criminal agencies North Korea who funds a lot of its government through the crypto market in the role of crypto and malfeasance and so Congress was kind of deadlocked now I think what you're seeing is more Republicans fall in line with Trump who saw crypto as a campaign issue.

So this is where I'm a little skepticism. Trump promises a lot of things on the campaign he promised to cap credit card interest rates at ten percent nobody believes he's going to do that in fact he I he he's going to deregulate interest rates of it to the extent possible for high cost payday loans and and other things like that to consumers in two thousand sixteen capitalizing on the wave of disk consent from Bernie Sanders Trump promised to bring back glass Steagall and break up the big banks of course as soon as he got into office he passed the regulation to make regulation simpler and less for large banks so you know they don't take Trump at his word because he's broken it

repeatedly when it comes to financial regulation op but if he does lean in on this and I think he chose this issue very wisely are politically because crypto is very popular among young men particularly young men of color who see this as an opportunity to make money I and and get wealthy is an investment in a way that the stock or bond market doesn't corporate bonds are very large but at one time the federal reserve found like a zero percent holding of corporate bonds among African Americans not zero point one but just zero as personal wealth building instruments so I think you know the the reason Trump leaned into crypt on the campaign trail was political not economic it was smart politics and it's been noticed on people on the hill so I think there could be a bi partisan crypto bill I usually bankrupt banking laws require bipartisan agreement there are as long as the Senate filibuster remains are they'll be some fierce opposition in Congress senator Elizabeth Warren is probably one of the biggest crypto skeptics in Congress and she'll be the senior Democrat on the banking committee this is because center centered around the prior senior Democrat chairman was defeated in large part due to crypto money that you just described and that influx of crypto money that helped defeat senator brown in Ohio has been noticed by other Democrats who in the past many it several of whom have partnered with Republicans on legislative proposals so I think there's a crypto bill to be had in Congress it'll be bi partisan probably get sixty five to seventy votes in the Senate maybe seventy five as high and could easily passed the house it'll take a little bit of time in the details of that will will have to get flushed out well I am really impressed not just that you are making a prediction about legislative passage but you're projecting the exact number of votes that is going out on a limb but you have a lot of expertise in this area I really respect your judgment in these areas well you know there although I'll tell you a funny insight on that I worked as a chief economist on the Senate banking committee for many years and when we were doing probably the most famous bell I worked on the economic emergency stabilization act which everybody would call tarp failed in front of the house the first time we brought it up the house didn't know how to count their votes the stock market collapse the financial crisis was in full of fact we worked out stop we brought the bill back this time to the Senate to vote first and I ran a pool on the floor of the Senate with all the most senior Senate staff White House staff who been working nonstop on this we all try to predict the vote count we were somewhere in the mid sixties to low seventies and I believe it passed with seventy four votes which was higher than any single staffer in the pool of I don't know twenty twenty five of us who'd been working nonstop on this bill had predicted so there's a there gets to be a funny dynamic eyes observed in the Senate which is when something's gonna pass anyways people tend to vote for it at the very end even something with tarp which was a dangerous and politically damaging vote they tended to lean for it you know when something breaks we start in the election right when when when something breaks one way it tends to break all that way no that is a great story about

tarpon I definitely remember of that time period and the the ups and downs of passing that and I do have a sense of I think you're right that the political environment has changed fairly substantially on the in the crypto area so you know perhaps the odds of a bipartisan bill actually is going up yeah.

I think I think you'll get that bipartisan bill but I think you'll see senator Warren lead a group of Democrats and maybe a small number of Republicans to go on the record of being skeptical about crypto because again what really is crypto good for yeah I do hear a lot of skepticism from progressive Democrats so I would expect a number of them to oppose this kind of legislation so I'm curious about tax policy in regard to virtual currency transactions just in terms of how tax policy is applied to crypto what happens with income taxes in capital gains taxes with that crypto assets what's the status of that right now this is incredibly important because if you go back in time crypto was originally sold as a payment instrument it was gonna be this thing that simultaneously was an asset and a means of payment you know there's a famous person about pizza with with big point early in and it's like a five million dollar pizza now by current valuation R. that was largely put an end to buy a couple things one the technology itself is not very conducive for payments visa can process way more transactions per second than bitcoin camp the nature of the blockchain breaks down a little bit when you're trying to ten globally process the quantity of transactions that at a credit card system can process to the treasury department the regulation decided that crypto was an asset and it needed to be capped taxed as capital gains so here's something probably you've never thought of their own and folks listing have it we know the dollar goes up and down in value right on a global basis the dollar can rise ten percent in a year but nobody pays a capital gains tax on the fact that their dollar appreciated in the global currency market right you eat the the the physical currency we hold is not considered an asset for that now if you are buying and selling dollars as commodities and assets on a trading platform then you would pay a capital gains tax what they did with crypto was a basically said any purchase or sale of crypto triggers a capital gain tax or loss in this mated administratively incredibly challenging to use crypto to transact imagine if you're in a store and you're buying the store is selling stuff in recording crypto and then it has to record not just when it's sold but the value of that crypto at the moment it received it and then when it goes to say spot pay its suppliers are paid to employees in crypto it has to calculate the cost of that crypto when it did it and match it to the cost of the crypto when it purchased it and that would create a capital gain or capital loss now we've seen how wildly volatile crypto is is an asset so the record keeping the tax consequences the actual cost of it all made the use of crypto currency as a payment mechanism essentially unworkable other countries have tried this like outside the door which may be Quinn legal tender without this type of regime have also found that it didn't work as a payment but in the United States eliminating that tax

consequence could open the door for the attempt to use crypto Morris payments and that was still done through regulation which the treasury department.

I could do without Congress congressional oversight it would also create a tax windfall for folks and administrative problem since most people of use crypto as an asset if they would then try to make purchases using it to escape tax taxable liabilities you know it could create quite a tax complications but it it is an issue that's out there that I don't think most people are fully appreciated that it's a regulatory decision made back in the Obama administration when crypto was was pretty new well it sounds like the Texan goal will be crucial to watch in a key thing for people to pay attention to so thanks for explaining that issue your bid proposals to establish a national strategic bit coin reserve what would that look like in is this a good idea so it would look like any asset are you by some estimates the United States government has one percent of all beat coins currently out there also this idea that the United States government does not have big coin is false these big ones have been seized are from various criminal activities some some level of payment I'm not entirely clear how the government got all of it but the U. S. has a bunch this model is basically based off the U. S. oil are petroleum reserve which is cool read it is a back when the United States was a heavy net importer of oil keep in mind now we produce more oil than we consume were net exporter but it was done to stop things like the seventies oil boycotts from foreign countries in the Gulf region they jacked up the price of oil and cause economic instability here so I mean what would it look like it looks like the United States government buying a bunch of big point in holding it why I sound highly clear to me the price of bitcoin doesn't impact the US economy in any way shape or form on a macro level that I can understand you know it seems to me to be a concerning idea that the U. S. government would be signaling that it should be buying any asset Bob you know we the U. S. government generally does not interfere in markets picking at winners and losers it's very strange to me that this idea the Republican Party says it's for free markets and opposes the government picking winners and losers why buy big point why not buy Ethereum why not buy this script why not buy that it seems to me very much weighing in the scale on that the other issue is it's one thing that I'm here to to to own crypto there's also a question of processing on the blockchain right one of the things that crypto currencies involves is a blockchain recordation system that involves some level of depending on the crypto proof proof of ownership or proof of stake and he the contest the system is meant to be honest because it's decentralized and anybody I you need fifty one percent of the chain to agree to a transaction to change the to record the transaction well you know there been people that have been concerned that Chinese bitcoin miners and other folks affiliated with the government have at various points how the majority of the court or other crypto Janes I could do that so maybe there's an argument that

this involves making sure that that the that the chain it has integrity although it's unclear to me why it has ownership I'll just end with one last story Jerrold I do you know where the gold in Fort Knox comes from because that's an asset the United States has we don't call it a gold reserve but we do the United States has a bunch of gold in Fort Knox pretty famously do you know where it comes from the answer is no I do not know where it comes from so so I did not either into I was at the treasury department and we were chasing down a bunch of things involving the debt ceiling and like one of the things the treasury department has to do is figure out where like where out what all the assets are of the United States government so the the the gold in Fort Knox is an asset to the treasury department and it comes from when we were taken off the gold standard in all gold currency was pulled out of circulation and the currency was pulled out of circulation and then substituted with fiat currency not backed by gold and the gold was melted and put in bars and the treasury secretary needed a place to store the bars and there is is empty for in Kentucky and they said Hey we got this amazing Kentucky in an empty fort called Knox do you guys want to put your gold there treasury said sure you know gold is heavy if you ever held a bar gold I like I have you realize it's very heavy so the gold in Fort Knox comes from melting down our currency when we took gold out of the physical currency it does not come from any moment where the United States created a strategic gold reserve to handle fluctuations in gold prices were to go long gone gold as a as an investment strategy well I love that Fort Knox story it's a great illustration of a point of history that probably most people don't know so thanks for letting us in on that how might other countries respond if the United States moves towards a more crypto friendly policy.

Well I mean one they may do the same a lot one thing I appreciated when I served in the treasury department was people around the world look up to the United States I had more than one global foreign officials say so why are you doing you're modeling your system this way they say well that's how you have your system and I say yeah I'm not sure that's how I build it from scratch and he said well we just thought of it worked if the US did it must be the right answer I mean there's tremendous global leadership we've developed by being the strongest economy and being the biggest economic and military power in in the world for many generations now also I think there may be a rush in in that regard and and that you know it can be a concern if you get back again to the fundamental prior which is what is the purpose of crypto currency why is this have value what is that one of the long term consequences of it what are the integrity of the market and what is its relationship to the U. S. dollar the United States enjoys incredible advantages by the dollar being the world reserve currency economic advances advantages foreign policy military advantages you know look when Russia invaded Ukraine the first thing we did was kick rush hour off of the global payment system and we could do that because the global payment system needs dollars and there's only one

place on earth that can create a United States dollar which is the United States government or government chartered entity so are you know I I I think people would be wise to appreciate that the government U. S. government leadership makes a big difference I also think that's why crypto was targeted the U. S. government one question you need to ask yourself is why is it why is cryptocurrency spending this much money in our elections why are crypto pouring money into our elections to elect candidates into elective office to imac crypto friendly policies it's a this is an investment this is an asset the people who made this investment are doing it because they think they're going to get a massive return on investment that the government actions are gonna be incredibly profitable for the holders of crypto that's what's motivating this and it sounds like they're right if things move in the direction which we anticipate the our allies can be very positive for that sector I let me close until it is it I'll just say like I'm an economist in the long term there has to be a fundamental correlation of the value of the asset I may be old enough now where I'm still scarred by the subprime mortgage crisis but I just remember people saying you know house nationally housing values couldn't fall in you would just say why and they would say because it hasn't happened since the depression and you say okay but it can happen right and sure enough it did you can pump up the value of any asset by attracting new buyers in Cannes training constraining the supply the supply of many cryptos is fundamentally constrained as a result of the algorithm unless the out unless the holders of the algorithm collectively change their mind but ultimately as an economist the asset ought to be correlated with its fundamental value and you have to ask what is the fundamental value proposition on any individual cryptocurrency let alone the asset class yup that definitely makes a lot of sense now if Trump follows through on his seeming promises what could the US crypto industry look like by the end of his term what a look the dollar values of all these things could look higher certainly you asset valuation could go up there could be new coins that have been brought into market I mean one of the issues here is is a very low barrier to entry to creating a new crypto a new cryptocurrency and then everybody's just trying to get out in front of what the new one is to take to get that initial market valuation you've seen people close to the president like Ilan mosque promote their own coins at various points I and so you could see new cryptos coming and not just that you could also see the U. S. government offering its imprimatur tour to certain cryptos whether it's a theory on whether it's big point you could see some of those things on the more extremists all right you know the more moderate you could just see a reduction in enforcement actions the growth of more crypto trading you could see greater adoption there's already been very large penetration of of crypto currency in certain age brackets.

For example according to a pew study seventeen percent of adults say they've traded in current crypto already twenty five percent of men and ten percent of women twenty nine percent of adults below the age

of thirty only eight percent of the adults above the age of fifty do you begin to see this break down twenty three percent of African Americans only fourteen percent of whites so you've seen a very different break down here and you could see these types of of our things changes more and different investors those are very different figures that if I talk to you about who's invested in bought individual stocks or bonds or a different different asset classes well that is a fascinating a gender gap in crypto trading so appreciate your sharing that information with us so I want to thank Aaron Klein for sharing his thoughts with us their tremendous I insights on his part you can follow our TechTank blog for analysis of technology innovation policy in general you can find that at Brookings dot EDU thank you very much for training in thank you for listening to tech take a series a round table discussions and interviews with technology experts and policy makers for more conversations like this subscribe to the podcast and sign up to receive the tech take newsletter for more research and analysis from the Center for Technology Innovation.