MEMORANDUM

To:	Crypto Task Force Meeting Log
From:	Crypto Task Force Staff
Re:	Meeting with Representatives of Paradigm Operations LP

On February 18, 2025, Crypto Task Force Staff met with the representatives from Paradigm Operations LP.

The topic discussed was approaches to addressing issues related to regulation of crypto assets. Paradigm Operations LP representatives provided the attached documents, which were discussed during the meeting.

TO: Office of Commissioner Hester M. Peirce, U.S. Securities and Exchange Commission
Office of Commissioner Mark T. Uyeda, U.S. Securities and Exchange Commission

FROM: Paradigm Operations LP[1], Multicoin Capital LP[2], Solana Foundation,[3] Electric Capital LP[4]

RE: Crypto Regulatory Reform Recommendations

DATED: January 20, 2025

I. INTRODUCTION

This memorandum outlines certain high-priority crypto regulatory reform recommendations that the U.S. Securities and Exchange Commission (the "**Commission**" or "**SEC**") and its Staff can implement to encourage technological innovation, enhance regulatory predictability and promote vibrant crypto markets within the United States. The regulatory reform recommendations proposed in Section II of this memorandum are simple modifications to the Commission's regulatory scheme designed to better align these regulations with the manner in which crypto networks, protocols and assets operate. Furthermore, the Commission and its Staff can quickly institute these reforms entirely through administrative action and without additional congressional authorization. Consistent with President Donald J. Trump's stated goal of reducing government waste and inefficiency, the regulatory reform recommendations contained herein are intended to help conserve Commission resources and minimize unnecessary use of taxpayer funds to regulate a nascent industry that is largely outside the scope of the U.S. federal securities laws as currently drafted.[5]

We encourage you to refer to this memorandum as a playbook for reversing the damage caused by the outgoing administration's weaponization of the U.S. federal securities laws against the crypto industry and creating pathways for the industry to return to the U.S. and make it the crypto capital of the planet.

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[1] Paradigm is a registered investment adviser that manages funds focused on crypto and related technologies at the frontier. Paradigm invests in, builds, and contributes to companies and protocols with as little as $1M and as much as $100M or more. More information about Paradigm is available online at https://www.paradigm.xyz/.

[2] Multicoin Capital is a thesis-driven registered investment adviser that invests in tokens and companies reshaping entire sectors of the global economy. More information about Multicoin Capital is available online at https://multicoin.capital.

[3] Solana Foundation is a non-profit dedicated to the decentralization, adoption and security of the Solana network.

[4] Electric Capital is a registered investment adviser that manages funds focused on distributed systems, cryptography,cryptocurrencies, and artificial intelligence. More information about Electric Capital is available online at https://electriccapital.com

[5] The U.S. Circuit Court of Appeals for the Third Circuit recently held that the Commission's denial of Coinbase, Inc.'s petition for rulemaking with regard to the applicability of the federal securities laws to crypto assets was arbitrary and capricious and remanded the petition to the Commission for a sufficiently reasoned disposition of Coinbase, Inc.'s petition. See Coinbase, Inc. v. SEC, No. 23-3202 (3d Cir. Jan. 13, 2025) (finding, among other things, that "[t]he SEC repeatedly sues crypto companies for not complying with the law, yet it will not tell them how to comply."). The Commission should evaluate the reform recommendations outlined herein in connection with its further consideration of Coinbase, Inc.'s petition for rulemaking.

II. REFORM RECOMMENDATIONS

A. Issuance

It is imperative that the Commission establish a transparent, appropriately tailored and flexible regulatory framework for the issuance of crypto assets within the U.S. Without clarity as to which crypto assets and crypto asset transactions are subject to registration as "securities" under Section 5[6] of the Securities Act of 1933, as amended (the "**Securities Act**"), firms generally must choose to forgo offers and sales of crypto assets to U.S. persons altogether or limit their offerings to accredited investors. Moreover, the Commission has fostered regulatory uncertainty by suggesting that crypto assets purchased in a primary offering may "embody" the elements of the primary offering such that secondary sales of the crypto asset must be registered with the Commission if not exempt therefrom.[7]

We believe that the regulatory reforms proposed below would enhance regulatory clarity for issuers of crypto assets and create additional opportunities for crypto asset issuers to distribute crypto assets to U.S. persons in compliance with the Securities Act and the Commission's regulations thereunder.

1. *Clarify "Security" Status of Crypto Assets and Transactions in Crypto Assets*

Priority: Very High

A fundamental challenge for crypto market participants is determining whether a given crypto asset or crypto asset transaction meets the definition of a "security" under the U.S. federal securities laws. The Securities Act and the Securities Exchange Act of 1934, as amended (the "**Exchange Act**"), each define the term "security" to include, among other things, any note, stock, transferable share, warrant, right to purchase a security or investment contract.[8] Federal district courts have consistently concluded that many crypto assets are not, in and of themselves, securities, but may be offered and sold as part of an investment contract security.[9] The SEC's Division of Enforcement has nonetheless suggested that crypto assets sold as part of an investment contract may "embody" the investment contract and therefore constitute securities.[10]

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6 15 U.S.C. § 77e(a).

7 SEC Opp'n to Mot. To Dismiss at 28-29, *SEC v. Binance Holdings Ltd., et al.*, No. 1:23-cv-01599-ABJ-ZMF (D.D.C. Nov. 7, 2023), ECF No. 172 (the "**SEC Binance Memo**") ("[t]he crypto assets at issue here are the embodiment of the investment contract.").

8 15 U.S.C. § 77b(a)(1); *id*. § 78c(a)(10). The definition of "security" is "virtually identical" in the Securities Act and the Exchange Act and therefore the U.S. Supreme Court has held that the definitions will be treated as identical "in our decisions dealing with the scope of the term." *Landreth Timber Co. v. Landreth*, 471 U.S. 681, 686 n.1 (1985). For all purposes relevant to this memorandum, the definition of "security" is also substantially similar under the Investment Advisers Act of 1940, as amended (the "**Advisers Act**"), and the Investment Company Act of 1940, as amended (the "**Investment Company Act**").

9 Order, *SEC v. Ripple Labs, Inc., et al.*, No. 1:20-cv-10832-AT-SN (S.D.N.Y. Jul. 13, 2023), ECF No. 874 (the "**Ripple Order**"); Op. & Order, *SEC v. Terraform Labs Pte. Ltd.*, *et al.*, No. 1:23-cv-01346-JSR (S.D.N.Y. Jul. 31, 2023) (the "**Terra Order**"), ECF No. 51; Mem. Op. & Order, *SEC v. Binance Holdings Ltd., et al.*, No. 1:23-cv01599-ABJ-ZMF (D.D.C. June 28, 2024), ECF No. 248 (the "**Binance Order**"); Op. & Order, *SEC v. Coinbase, Inc. et al.*, No. 1:23-cv-04738-KPF (S.D.N.Y.Mar. 27, 2024), ECF No. 105 (the "**Coinbase Order**"); Order, *SEC v. Payward, Inc. et al.*, No. 3:23-cv-06003-WHO (N.D. Cal. Aug. 23, 2024), ECF No. 90.

10 The SEC Binance Memo at 28-29; The Binance Order at 20 ("the SEC's suggestion that the token is 'the embodiment of the investment contract,' as opposed to the *subject* of the investment contract, muddied the issues before the Court, ignored the Supreme Court's directive that the analysis is supposed to be based on the entire set of understandings and expectations surrounding the offering, and unnecessarily invited the defendants' argument that a decision in the government's favor here would somehow encroach on the jurisdiction of the Commodities Futures Trading Commission." (emphasis added)).

To address this critical issue, the SEC's Division of Corporation Finance and Division of Trading and Markets should issue an interpretive release within the first thirty days of a new Commission majority being in office, whereby the Divisions' Staff opine that a fungible or non-fungible crypto asset sold as the *object* or *subject* of an investment contract security is not itself a security within the meaning of the U.S. federal securities laws, unless the crypto asset possesses features that cause the crypto asset itself (*i.e.*, not any particular offer or sale thereof) to independently qualify as a type of security enumerated under the Securities Act, such as an investment contract, note, stock or bond.

The interpretive release should establish clear, bright-line standards that market participants can rely on to determine whether a crypto asset constitutes an investment contract, stock, note or other type of security. In particular, the Divisions' Staff should clarify its position on the applicability of the investment contract definition established by the Supreme Court in *SEC v. W.J. Howey Co.* (also known as the "*Howey* test") to crypto assets.[11] Additionally, the Staff should create clear-cut, principles-based criteria for the "sufficient decentralization" of a crypto network or protocol, a concept introduced by former Director of the SEC's Division of Corporation Finance, William Hinman.[12] Finally, the interpretive release should clarify that crypto assets with meaningful utility or consumptive use are not investment contract securities, consistent with the Supreme Court's reasoning in *United Housing Foundation, Inc. v. Forman*.[13] Any framework for distinguishing which, if any, crypto assets or crypto asset transactions constitute securities should acknowledge that crypto assets have unique properties relative to traditional financial assets, especially in regard to the attendant purchaser expectations, risk factors and availability of public information. We encourage the Commission to consider these unique properties of crypto assets in determining how and when this new asset class will be regulated going forward.

After the Divisions issue the interpretive release, the Commission should consider codifying these principles through a formal rulemaking, particularly to ensure this delineation is sustained by future administrations.

2. *Establish "Airdrop" Safe Harbor*

Priority: High

It is common for crypto software projects to issue crypto assets to software users for free in a so-called "airdrop." In these instances, the issuer typically distributes crypto assets to a software user's digital wallet automatically pursuant to preprogrammed software code or allows the user to claim crypto assets for free as a reward for being an early adopter of the software. The Commission has introduced confusion for these issuers by suggesting that these free distributions of crypto assets to software users constitute "sales" under the Securities Act and are therefore subject to registration to the extent the crypto asset is a security.[14]

Section 2(a)(3) of the Securities Act defines the term "sale" to mean "every contract of sale or disposition of a security or interest in a security, for value."[15] It is well established that broad-based

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[11] *SEC v. W.J. Howey Co.*, 328 U.S. 293 (1946).

[12] William Hinman, Director, Division of Corporation Finance, SEC, "*Digital Asset Transactions: When Howey Met Gary (Plastic)*" (June 14, 2018), https://www.sec.gov/newsroom/speeches-statements/speech-hinman-061418.

[13] *United Housing Foundation, Inc. v. Forman*, 421 U.S. 837, 852-53 (1975).

[14] *Tomahawk Exploration LLC and David Thompson Laurance*, Securities Act Release No. 10530, Securities Exchange Act of 1934 Release No. 83839 (Aug. 14, 2018) ("**Tomahawk Exploration LLC**").

[15] 15 U.S.C. § 77b(a)(3). To be clear, this only applies to securities, and the bulk of crypto assets are not securities.

distributions of securities for free generally do not constitute "sales" or "offers to sell" under the Securities Act because the security is not exchanged "for value." For example, the Staff has reasoned that certain broad-based distributions of securities by employers to employees in accordance with an employee compensation plan are not subject to registration because the employees do not individually bargain to contribute cash or other tangible or definable consideration to such a plan in exchange for the securities and thus have no investment decision to make.[16] Despite the Staff's past adherence to the "no sale" doctrine, the SEC's Division of Enforcement has reasoned in certain enforcement actions that airdrops constitute "sales."[17] This has resulted in industry lawsuits against the Commission, congressional calls for the agency to provide clarity around the application of the Securities Act to crypto asset airdrops and consumer harm to American crypto enthusiasts who were unable to participate in these free distributions of potentially valuable crypto assets.[18] On the final harm, the lack of American consumers to receive airdrops has also meant that the U.S. government has lost valuable tax revenue at a time of very high budget deficits.

To address this uncertainty, the SEC's Division of Corporation Finance and Division of Trading and Markets should prepare for Commission vote a notice of proposed rulemaking that would establish criteria for distributions of crypto assets via airdrops and other free methods (*e.g.*, through video game play or NFT minting) to be safe harbored from characterization as "sales" under Section 2(a)(3) of the Securities Act.[19] We believe that this would create a clear initial path for crypto asset issuers to enter U.S. markets, which the Commission can incrementally expand with future safe harbors, no-action relief and interpretations. As an alternative or in addition to the rulemaking process, the Staff could address the matter through an interpretive release or in a no-action letter.

3. *Amend "Accredited Investor" Definition*

Priority: Medium

Crypto software projects often offer and sell crypto assets or warrants to purchase crypto assets to investors in private placements in accordance with the Rule 506(b) safe harbor under Section 4(a)(2) of the Securities Act.[20] These offerings are generally restricted to accredited investors, thus precluding non-accredited but technologically sophisticated persons from participating.

The definition of "accredited investor" in Rule 501(a) enumerates certain criteria for sophistication, including net worth, income, professional certification and other requirements.[21] These criteria are designed to capture persons with sophistication in regard to financial products, but do not necessarily capture persons with sophistication in regard to technology products. The Commission amended the definition of "accredited investor" during the Biden Administration to address certain professional certifications, designations and other credentials,[22] recognizing that financial criteria alone

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16 *See, e.g.*, *Compass Group PLC*, SEC Staff No-Action Letter (May 13, 1999) at 6.

17 *See*, *e.g.*, Tomahawk Exploration LLC.

18 *See*, *e.g.*, Compl., *Beba LLC et al.*, *v. SEC*, No. 6:24-cv-00153-ADA-DTG (W.D. Tex. Mar. 25, 2024), ECF No. 1; Letter from Rep. Tom Emmer & Rep. Patrick McHenry, to Hon. Gary Gensler, Chairman, SEC (Sept. 17, 2024), https://emmer.house.gov/_cache/files/5/0/50176829-99c6-40ec-87dd-96421f659fd0/58E2521AD98881EC6DB7696DEC1C2A6C.congressionalletter.sec.9.17.24.pdf.

19 15 U.S.C. § 77b(a)(3).

20 17 C.F.R. § 230.506(b).

21 *Id*. § 230.501(a).

22 *See* Accredited Investor Definition, 85 Fed. Reg. 64234.

are not an exhaustive barometer of sophistication and underscoring that there is bipartisan support for expanding the definition.

The SEC's Division of Corporation Finance should propose further amendments to the "accredited investor" definition in Rule 501(a)[23] to add a new category to this definition, which permits natural persons to qualify as accredited investors based on their sophistication in regard to the technology in which they seek to invest. Among the ways persons can demonstrate that they are sophisticated investors under this new category should be by demonstrating that they have played a role in usage of or research in blockchain and crypto, such as persons who are "testnet" participants, validator operators, core contributors to a crypto network or protocol or legal, compliance or financial advisers to the same.

B. Staking

The SEC's Division of Enforcement's previous characterization of proof-of-stake blockchain network users' participation in such networks and engagement of technological service providers to outsource aspects of the staking process as securities transactions undermines the viability of these innovative technologies and services.[24] Staking is a technological process whereby a user of a proof-of-stake blockchain network locks crypto assets within a protocol to contribute to the security of the network and earns additional crypto assets (either as newly created crypto assets or the payment of transaction fees and tips). Network users may choose to engage in "solo" or "at home" staking by configuring and keeping online the requisite hardware device or engage a "staking-as-a-service" provider to operate the hardware on their behalf. In the absence of regulatory clarity in regard to staking and staking services, a significant portion of the validator nodes that support the most popular proof-of-stake blockchain networks is operated outside of the U.S., placing these networks at risk of capture by foreign nations.

We believe that the regulatory reforms proposed below would enable U.S.-based blockchain users and service providers to participate in network consensus within the U.S. without fear of violating the Securities Act.

1. Clarify "Security" Status of Solo Staking

Priority: High

Proof-of-stake blockchain networks cannot function unless users participate in network consensus by operating a validator and pledging crypto assets as stake. The economic mechanism design of such systems facilitates users' trust in the technology in the absence of a central intermediary. The SEC's Division of Enforcement has discouraged U.S. persons from participating in network consensus by characterizing certain staking services and products as securities.[25]

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[23] 17 C.F.R. § 230.501(a).

[24] *See*, *e.g.*, Compl., *SEC v. Payward Ventures, Inc. d/b/a Kraken,* et al., No 3:23-cv-00588-JSC (N.D. Cal. Feb. 9, 2023), ECF No. 1 (the "**Kraken Staking Complaint**"); Compl., *SEC v. Binance Holdings Limited, et al.,* No. 1:23-cv-01599 (D.D.C. June 5, 2023), ECF No. 1 (the "**Binance Complaint**"); Compl., *SEC v. Coinbase, Inc., et al.*, No. 1:23-cv-04738-KPF (S.D.N.Y. June 6, 2023), ECF No. 1 (the "**Coinbase Complaint**"); Compl., *SEC v. Consensys Software Inc.*, No. 1:24-cv-04578-MKB-TAM (E.D.N.Y. June 28, 2024), ECF No. 1 (the "**Consensys Complaint**").

[25] *See*, *e.g.*, the Kraken Staking Complaint; the Binance Complaint; the Coinbase Complaint; the Consensys Complaint.

The SEC's Division of Corporation Finance should issue an interpretive release clarifying that directly staking or delegating staked crypto assets to a validator node as part of a proof-of-stake or delegated proof-of-stake blockchain network, including as part of a custodial staking program, does not constitute an investment contract arrangement. The release should enable U.S. persons to support the security of these proof-of-stake networks by engaging in staking. Moreover, the release should state that any crypto assets earned by a person who operates a validator node or similar device and thus participates in staking or a person who delegates stake to a validator operator in accordance with the proof-of-stake (or delegated proof-of-stake) consensus mechanism of a blockchain network will not be deemed to be offered or sold as part of an investment contract. Alternatively, the Staff could issue a no-action letter memorializing this position.

2. *Provide Guidance that Staking-as-a-Service Providers Are Not Promoting or Selling Securities; Withdraw Staking-as-a-Service Program Lawsuits*

Priority: High

The SEC's Division of Enforcement has brought several enforcement actions against staking-as-a-service providers and software firms providing access to staking services for offering investment contract securities.[26] The Chair of the Commission should deliver a speech opining that staking services by themselves (*i.e.*, where the program provider is *not* generating additional yield, network rewards or engaging in some other non-technical activity to increase returns for stakers) are technology services and do not constitute offers or sales of investment contract securities. Alternatively, the SEC's Division of Corporation Finance could issue interpretive guidance regarding staking-as-a-service providers, provide a no-action letter to a staking-as-a-service provider or seek industry input on staking-as-a-service providers via an advance notice of proposed rulemaking.

Moreover, the SEC's Division of Enforcement should seek Commission approval for the dismissal of all ongoing lawsuits against staking-as-a-service providers. If dismissal cannot be achieved, reasonable settlements should be agreed upon with the parties that have been in litigation with the SEC.

C. Custody

Custody is a principal regulatory and operational challenge for crypto industry participants. While custodial solutions continue to evolve to address industry demands, the regulatory framework governing crypto asset custody does not align with existing crypto market dynamics and the manner in which blockchain networks inherently function. Further, administrative actions have discouraged qualified custodians from offering custodial services for crypto assets, choking off growth in the space.

We believe that the regulatory reforms proposed below would reduce unnecessary regulatory and operational costs on crypto asset custodians and registered investment advisers.

1. *Withdraw SAB 121*

Priority: High

SEC Staff Accounting Bulletin No. 121 ("**SAB 121**") specifies that it would be appropriate for financial institutions to present a liability on their balance sheets to reflect any obligation to safeguard crypto assets for users.[27] As a practical matter, SAB 121 discourages public companies from offering

[26] *Id*.

[27] Staff Accounting Bulletin No. 121, 87 Fed. Reg. 21015 (Apr. 11, 2022).

crypto asset custody services at the risk of taking a capital charge on these custodied assets, which has the practical effect of limiting the number of qualified custodian options available to crypto market participants. Moreover, treatment of customer crypto assets as assets on the balance sheet of the custodian is potentially a violation of GAAP and could result in such customer assets being included in the custodian's bankruptcy estate rather than segregated for customers. Although a bipartisan resolution overturning SAB 121 passed both houses of Congress in May, President Joe Biden vetoed the resolution, and thus SAB 121 remains in effect.[28]

The SEC's Division of Corporation Finance, together with the Office of the Chief Accountant, should issue a Staff Accounting Bulletin rescinding SAB 121 within the first ten days of a new Chair taking office.

2. Withdraw Safeguarding Rule Proposal and Amend Custody Rule

Priority: High

Rule 206(4)-2 (the "**Custody Rule**") under the Investment Advisers Act requires, among other things, that registered investment advisers maintain client "funds and securities" with a "qualified custodian."[29] Notwithstanding ongoing uncertainty and debate surrounding whether crypto assets should be classified as securities, the proposing release for the "Safeguarding Advisory Client Assets" (the "**Safeguarding Rule Proposal**") rule proposal states that "most crypto assets are likely to be funds or crypto asset securities covered by the current [Custody Rule]."[30]

The Safeguarding Rule Proposal seeks to impose onerous obligations on custodians, foreign financial institutions and registered investment advisers, including minimum custodial protections that the Division of Investment Management acknowledges would upend existing custodial arrangements. The Safeguarding Rule Proposal details neither a clear benefit nor attempts to accurately analyze the costs of these changes. For those and other reasons, the Commission should formally withdraw the Safeguarding Rule Proposal.

As a replacement for such proposal, the SEC's Division of Investment Management should propose amendments to the Custody Rule to define "funds" to mean cash and cash equivalents, and establish reasonable exceptions or exemptions from the qualified custodian requirement for any crypto assets subject to the Custody Rule, such as for staking, claiming airdrops, participating in governance and exchange trading. For example, the amendments may permit arrangements where an investment adviser custodies client crypto assets with a qualified custodian and executes exchange transactions through an affiliate of the qualified custodian. Additionally, the rule proposal should include an exemption permitting an adviser to engage in self-custody, subject to certain minimal conditions such as the existence of written risk controls, in the event that the adviser is unable to identify a qualified custodian with suitable capabilities to maintain custody of a particular crypto asset.

3. Withdraw Non-Custodial Digital Wallet Software Provider Lawsuits

Priority: High

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[28] The White House, *A Message to the House of Representatives on the President's Veto of H.J.Res. 109*, (May 31, 2024), https://www.whitehouse.gov/briefing-room/presidential-actions/2024/05/31/a-message-to-the-house-of-representatives-on-the-presidents-veto-of-h-j-res-109/.

[29] 17 C.F.R. § 275.206(4)-2.

[30] Safeguarding Advisory Client Assets, 88 Fed. Reg. 14672,14676 (Mar. 9, 2023).

The SEC's Division of Enforcement has brought lawsuits against certain popular digital wallet software providers for engaging in unregistered "broker"[31] services.[32] At least one federal judge has rejected the Commission's legal theory regarding broker services and concluded that the provision of non-custodial digital wallet software does not constitute broker activity because the software provider does not negotiate terms for transactions, make investment recommendations, arrange financing, hold customer funds, process trade documentation or conduct independent asset valuations.[33] Indeed, non-custodial digital wallet software is simply software that allows the user to access and interact with applications and assets available on a blockchain network.

Accordingly, the SEC's Division of Enforcement should seek Commission approval for the dismissal of all ongoing lawsuits against non-custodial digital wallet software providers. If dismissal cannot be achieved, reasonable settlements, which do not prevent the defendants from operating non-custodial digital wallet businesses, should be agreed upon with the parties that have been in litigation with the SEC.

4. Codify a Software Provider Safe Harbor

Priority: High

Although the Commission has characterized certain software providers as intermediaries subject to registration under the Exchange Act, these software providers offer services that generally operate in a non-intermediated and non-custodial manner akin to web browser or word processing software programs.[34] Such service providers more closely align with the electronic communications services providers that the Staff reasoned were not subject to registration in prior Staff no-action letters.[35] In those instances, the Staff found that the electronic communications services providers, which developed online communication and gateway systems that permitted users to communicate messages and access securities market information, were not engaged in regulated activities, in part, because the providers were not handling customer funds or securities.[36]

To address this apparent divergence in approach to regulating traditional financial market and crypto asset software providers, the SEC's Division of Trading and Markets should issue a rule proposal to clarify that persons who offer non-custodial digital wallet software, smart contract protocols and similar non-custodial software to users do not meet the definition of a "broker," "dealer," "exchange" or "clearing agency" and receive safe harbor from Sections 5, 15(a) and 17A(b) of the Exchange Act, provided that the software provider satisfies certain enumerated requirements, such as the protection of investors.[37]

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[31] Section 15(a) of the Exchange Act prohibits any "broker" from making use of the mails or any means or instrumentality of interstate commerce to "effect any transactions in, or to induce or attempt to induce the purchase or sale of, any security" unless such broker is registered with the SEC, absent an exemption (15 U.S.C. § 78o(a)). Section 3(a)(4) of the Exchange Act defines the term "broker" to mean "any person engaged in the business of effecting transactions in securities for the account of others." (15 U.S.C. § 78c(a)(4)).

[32] *See*, *e.g.*, the Coinbase Complaint; the Consensys Complaint.

[33] The Coinbase Order at 81-82.

[34] *See*, *e.g.*, the Coinbase Complaint; the Consensys Complaint.

[35] *See*, *e.g.*, *Evare, LLC*, SEC Staff No-Action Letter (Nov. 30, 1998); *Charles Schwab & Co., Inc.*, SEC Staff No-Action Letter (Nov. 27, 1996); *Quick America Corp.*, SEC Staff No-Action Letter (June 28, 1993).

[36] *Id*.

[37] 15 U.S.C. § 78e; *id*. § 78o(a); *id*. § 78q-1(b)(1).

5. Crypto Asset Custody Requirements for Broker-Dealers

Priority: Medium

Exchange Act Release No. 34-90788 requires broker-dealers to qualify as a "special purpose broker-dealer" in order to custody crypto assets and restricts such broker-dealers from also providing services in respect of traditional securities and non-security crypto assets.[38] This "special purpose broker-dealer" framework has seen little commercial demand due to the restrictions it places on such broker-dealers and the limited number of crypto asset security products in the market.[39] The Commission should allow firms to opt to use as a custodian either a FINRA member broker-dealer or a federal- or state-chartered trust company or bank, affording firms optionality while ensuring that the underlying custodians are subject to regulatory supervision.

The SEC's Division of Trading and Markets should withdraw Exchange Act Release No. 34-90788, and issue a policy statement clarifying the Staff's position that broker-dealers are authorized to custody both traditional and crypto asset securities (*e.g.*, tokenized real world assets). The Staff should also work with FINRA to provide guidance for FINRA-member firms on the institution of appropriate measures to prepare for compliance with their Exchange Act and member agreement requirements.

D. Secondary Markets

The Commission has hindered the development of secondary markets for crypto assets within the U.S. by maintaining in enforcement actions and proposing releases that crypto asset trading platforms and intermediaries are subject to registration under the Exchange Act, while ignoring industry calls for the Commission to propose amendments to its regulations to accommodate the registration of such platforms and intermediaries. The Commission's regulation-by-enforcement policy is a hidden tax on the industry that undermines its growth within the U.S. and wastes valuable taxpayer dollars on unnecessary lawsuits.

We believe that the regulatory reforms proposed below would reduce unnecessary regulatory burdens and litigation costs imposed on crypto market participants and free up Commission resources to police fraud and manipulation within securities markets.

1. Withdraw Trading Platform Operator Lawsuits

Priority: High

The Division of Enforcement has brought several lawsuits against centralized crypto asset trading platform operators alleging, among other things, that such trading platforms are unregistered national securities exchanges, clearing agencies and brokers.[40] Due to the regulatory uncertainty surrounding the status of crypto assets in the secondary market,[41] as evidenced by the split in federal court decisions, and

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[38] Custody of Digital Asset Securities by Special Purpose Broker-Dealers, Exchange Act Release No. 34-90788 (Dec. 23, 2020) (published in 86 Fed. Reg. 11627 (Feb. 26, 2021)).

[39] As of the date of this memorandum, there are only a handful of "special purpose broker-dealers," including Prometheum Capital and tZERO Digital Asset Securities.

[40] *See*, *e.g.*, the Binance Complaint; the Coinbase Complaint; Compl., *SEC v. Payward Ventures, Inc. d/b/a Kraken et al.*, No. 3:23-cv-06003-WHO (N.D. Cal. Nov. 20, 2023), ECF No. 1.

[41] In the Ripple Order, Judge Torres distinguished between the different types of transactions involving the crypto assets at issue in the case. However, in the Terra Order, Judge Rakoff declined to distinguish between the different types of transactions involving the crypto assets at issue in that case. Although Judge Rakoff noted, like Judge Torres, that crypto assets, in and of themselves, are not necessarily investment contracts, the differing approaches applied by the judges with

the definitional requirement that an "exchange" bring together purchasers and sellers of *securities*, the SEC's Division of Enforcement should seek Commission approval for the dismissal of all ongoing lawsuits against centralized crypto asset trading platform operators. If dismissal cannot be achieved, reasonable settlements that do not prevent the defendants from operating crypto asset trading platforms should be agreed upon with the parties that have been in litigation with the SEC. The Commission should, as appropriate, consider excluding cases that pertain solely to fraud and manipulation.

2. Withdraw Amendments to the Definition of "Exchange"

Priority: High

The Commission's proposed amendments to the definition of "exchange" in Rule 3b-16 under the Exchange Act (the "**Exchange Rule Proposal**"), if finalized, would significantly expand the scope of the definition of "exchange" to capture crypto market participants, including software code deployed on a blockchain network.[42] The Exchange Rule Proposal would, among other things, codify that a "communication protocol system" is an exchange for purposes of the Exchange Act.[43] In that regard, the Exchange Rule Proposal seeks to subject decentralized exchange protocols to the SEC's existing registration and disclosure rules designed for traditional, centralized exchanges. Indeed, prior statements of Commissioners Peirce and Uyeda emphasize the potential wide range and breadth of the proposed amended definition.[44] It would not be feasible for a software developer to register a decentralized exchange protocol, which is a software program that operates on-chain in a vastly different manner than a traditional exchange, in the absence of significant changes to the Commission's regulations or no-action relief. Moreover, the technological design of such software programmatically enforces controls that address many of the underlying policy rationales for regulating traditional exchanges in the first place.

The SEC's Division of Trading and Markets should withdraw its proposed amendments regarding the definition of "exchange" under the Exchange Act.

3. Clarify Rule 144's Application to Investment Contracts

Priority: Medium

Certain primary offerings of crypto assets by software developers to private investors may constitute investment contract securities insofar as the contract, transaction or scheme satisfies the *Howey* test (*e.g.*, because the offering occurs before the associated network is fully functional or decentralized), but the crypto assets that are the object of such investment contract may nonetheless constitute non-securities. It is unclear whether investors who receive crypto assets as part of an investment contract must hold *both* the investment contract and the underlying crypto assets for a minimum holding period to

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respect to different types of transactions in the same crypto asset underscore the regulatory uncertainty surrounding the status of crypto assets in the secondary market.

[42] Amendments Regarding the Definition of "Exchange" and Alternative Trading Systems (ATSs) That Trade U.S. Treasury and Agency Securities, National Market System (NMS) Stocks, and Other Securities, 87 Fed. Reg. 15496 (Mar. 18, 2022); Supplemental Information and Reopening of Comment Period for Amendments Regarding the Definition of "Exchange," 88 Fed. Reg. 29448 (May 5, 2023).

[43] 87 Fed. Reg. 15496, 15498.

[44] Commissioner Hester M. Peirce, *Dissenting Statement on the Proposal to Amend Regulation ATS* (Jan. 26, 2022), https://www.sec.gov/news/statement/peirce-ats-20220126; Commissioner Mark T. Uyeda, *Statement on Supplemental Information and Reopening of Comment Period for Amendments to Exchange Act Rule 3b-16 regarding the Definition of "Exchange"* (Apr. 14, 2023), https://www.sec.gov/newsroom/speeches-statements/uyeda-statement-ats-041423.

be safe harbored from qualifying as an "underwriter" under Section 2(a)(11) of the Securities Act[45] pursuant to Rule 144.[46] As a result, investors have adopted differing approaches to compliance with Rule 144,[47] with some treating crypto assets purchased in an investment contract transaction as part of the investment contract security and holding such crypto assets for the minimum period and others choosing not to do so because the crypto assets themselves are not securities.

The SEC's Division of Corporation Finance should propose amendments to Rule 144[48] to clarify whether a person who receives non-security crypto assets in an investment contract transaction must hold the crypto assets that are the object of the investment contract for the applicable holding period and, if so, whether the holding period of certain crypto asset sale instruments can tack together with associated crypto assets to satisfy Rule 144.[49]

E. Public Investment Vehicles

The Commission has hindered the access of exposure to crypto assets through traditional public investment vehicles, although such products are managed by experienced professionals that are often fiduciaries and have access to institutional grade custody solutions at scale in a way that improves services and reduces costs to investors. Such products also provide written disclosures to investors that identify the material risks of exposure to crypto asset markets.

We believe that such measures have historically harmed the American investing public by removing trusted, known products that are i) wrapped in appropriate disclosures, ii) available in brokerage accounts and iii) managed by experienced professionals with access to institutional-level custody. Furthermore, these measures represent merit regulation, which is outside the scope of the Commission's purview. We believe the following recommendations will correct these wrongs.

1. Withdraw the Engaging on Fund Innovation and Cryptocurrency-related Holdings Letter

Priority: Medium

In 2018, the Director of the Division of Investment Management published the Engaging on Fund Innovation and Cryptocurrency-related Holdings Letter,[50] which prohibited registered investment companies (*i.e.*, mutual funds, business development companies and exchange-traded funds registered under the Investment Company Act) from obtaining almost any direct or indirect exposure to crypto assets. The basis of this prohibition was due to concerns on valuation, liquidity, custody, arbitrage (for ETFs) and manipulation. In 2021, the Division of Investment Management supplemented this letter with a Staff Statement on Funds Registered Under the Investment Company Act Investing in the Bitcoin

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[45] 15 U.S.C. § 77b(a)(11) (an "underwriter" includes any person who purchases a security from an issuer with a view to, or offers or sells for an issuer in connection with, the distribution of the security).

[46] 17 C.F.R. § 230.144.

[47] *Id*.

[48] *Id*.

[49] *Id*.

[50] Letter from Dalia Blass, SEC, to Paul Schott Stevens, Investment Company Institute & Timothy W. Cameron, SIFMA (Jan. 18, 2018), https://www.sec.gov/divisions/investment/noaction/2018/cryptocurrency-011818.htm (Engaging on Fund Innovation and Cryptocurrency-related Holdings).

Futures Market,[51] which permitted a small subset of mutual funds (on a Staff merit review basis) to invest in bitcoin futures markets.

The Staff should withdraw or revisit the logic of both letters, focusing on the existing obligations of registered investment company managers under the applicable rules of the Advisers Act, Investment Company Act and the remaining federal securities laws.

2. *Revisit the Incorrect Interpretation of Section 6(b)(5) as Applied to Commodity-Based Trust Shares*

Priority: Medium

The Division of Trading and Markets has promulgated an interpretation of Section 6(b)(5) of the Exchange Act that creates a purported precondition of a "regulated market of substantial size" for the underlying asset of a commodity-based trust share exchange traded product. The Exchange Act does not provide for such a precondition, nor does it dictate that a U.S. futures market must exist to approve national security exchange rules to list commodity-based trust shares. Commissioner Peirce addressed some of the fallacies of these arguments in her dissent to the first order to establish this requirement.[52]

In addition to Commissioner Peirce's dissent, we note that commodity-based trust shares have several investor protections and benefits (including robust risk disclosure, institution custody, lower transaction costs and availability in familiar forms) for many investors. Furthermore, the Staff has dismissed that a variety of issuers have obtained comprehensive surveillance sharing agreements with U.S. regulated trading platforms, the substance of which satisfy all the requirements of comprehensive surveillance sharing agreements detailed by the Division of Trading and Markets to the Intermarket Surveillance Group in a prior interpretive letter.[53]

The Commission has sought to stifle efforts to launch these trusted commodity-based trust shares products for a decade, predominantly through the denial of Rule 19b-4 applications of the proposed listing national securities exchanges. The Commission should reassess the weaponization and redirection of Section 6(b)(5) beyond its plain interpretive meaning and permit the listing of commodity-based trust shares where the proposed listing exchange has demonstrated reasonable measures to ensure investor protection and the minimum standards required under Section 6(b)(5) at the ETF share level.

3. *Revisit the Prohibition on Commodity Based Trust Share Staking and In-Kind Creates and Redeems*

Priority: Medium

Without reasonable basis, the Division of Trading and Markets prohibited bitcoin and ether ETFs operating as commodity-based trust shares funds from receiving incidental rights (*e.g.*, staking income, airdrops or forked assets) or from engaging in in-kind creations and redemptions.

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[51] Division of Investment Management Staff, *Staff Statement on Funds Registered Under the Investment Company Act Investing in Bitcoin Futures Market* (May 11, 2021), https://www.sec.gov/newsroom/speeches-statements/staff-statement-investing-bitcoin-futures-market.

[52] Commissioner Hester M. Peirce, *Dissent of Commissioner Hester M. Peirce to Release No. 34-83723; File No. SR-BatsBZX-2016-30* (Jul. 26, 2018), https://www.sec.gov/newsroom/speeches-statements/peirce-dissent-34-83723.

[53] Letter from Brandon Becker, SEC, to Gerald D. O'Connell, Philadelphia Stock Exchange (June 3, 1994), https://www.sec.gov/divisions/marketreg/mr-noaction/isg060394.htm (Surveillance Sharing Agreements).

As the Staff's logic was neither detailed nor obvious, the prohibition of these activities seems punitive. For example, both actions were permitted without incident for vehicles that converted into commodity-based trust shares funds (*e.g.*, the Grayscale Bitcoin Trust and Grayscale Ethereum Trust handled airdrops and forked assets and permitted in-kind creations). These funds were required to strip these provisions from their Trust Agreements, registrations statements and associated 19b-4 applications.

While there are mechanical and tax questions around certain incidental rights, the Commission should permit commodity-based trust shares funds to create programs to recognize incidental rights and engage in in-kind creations and redemptions.[54] These programs provide substantial investor and market benefits and the ancillary risks may be easily disclosed.

F. Miscellaneous

1. Enter Memorandum of Understanding with the U.S. Commodity Futures Trading Commission

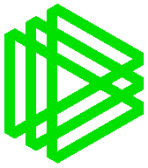
Priority: High

The Commission has yet to meaningfully coordinate with the U.S. Commodity Futures Trading Commission (the "**CFTC**") on crypto market jurisdictional matters. The SEC's Office of Legislative and Intergovernmental Affairs should seek a Commission vote on entering into a memorandum of understanding with the CFTC to define the contours of each agency's regulatory authority over crypto markets within 60 days and until such time as Congress legislates in this area

* * *

We appreciate your consideration of our crypto regulatory reform recommendations and would be pleased to engage with you further on these matters. If you have any questions or would like to discuss these recommendations in more detail, please reach out to Alex Grieve at agrieve@paradigm.xyz.

[54] We understand one Commissioner objected to in-kind creations and redemptions under the pretense that in-kind creations could assist parties in money laundering. This is ill-informed. Instead, requiring cash-only creation and redemption removes FINRA and the SEC from the applicable fund's purchase and sale activity. The SEC does not regulate the operation of a commodity-based trust shares fund, but does regulate the broker-dealers that act as authorized participants to such funds. As a result, the SEC has greater oversight over the sourcing and disposition of in-kind creations and redemptions than the cash system this Commissioner purportedly demanded. In addition, cash-only creation and redemption actually increases the potential for market manipulation, as all inflows and outflows to the ETF triggers purchase and sale activity during the fund's settlement window, while in-kind creation and redemption provides for tax efficient flows that do not necessitate either party engaging in purchase or sale activity.



Via Electronic Submission (crypto@sec.gov)

Crypto Task Force Staff
U.S. Securities and Exchange Commission
100 F Street, NE
Washington, DC 20549-1090

Re: Proposal Regarding the Application of Section 5 of the Securities Act of 1933 to Distributions of Digital Assets via "Airdrops"

I. Introduction

Paradigm Operations LP ("**Paradigm**" or "**we**")[1] appreciates the opportunity to submit this proposal to the U.S. Securities and Exchange Commission's (the "**Commission**") Crypto Task Force regarding the status of certain distributions of digital assets[2] as offers or sales of securities subject to registration with the Commission under Section 5 of the Securities Act of 1933, as amended (the "**Securities Act**").

Digital asset industry participants seeking to distribute digital assets for free or in exchange for minimal consideration to software users in transactions colloquially referred to as "airdrops" must consider whether such transactions constitute an offer or sale of a security.[3] The Commission has yet to provide guidance with respect to the factors that industry participants should consider in determining whether a distribution of a digital asset in such a transaction constitutes an offer or sale of a security and is thereby subject to registration with the Commission.

Paradigm encourages the Commission to provide regulatory clarity to digital asset industry participants that seek to distribute digital assets to software users via airdrops. We outline below

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[1] Paradigm is a registered investment adviser that manages funds focused on crypto and related technologies at the frontier. Paradigm invests in, builds, and contributes to companies and protocols with as little as $1M and as much as $100M or more. More information about Paradigm is available online. *See* Paradigm, https://www.paradigm.xyz/.

[2] The term "digital asset," as used in this proposal, refers to an asset that is issued and transferred using distributed ledger or blockchain technology, including, but not limited to, "crypto assets," "virtual currencies," "coins" and "tokens."

[3] The dearth of clarity with respect to the status of airdrops under the U.S. federal securities laws has culminated in at least one lawsuit against the Commission. *See* Compl., *Beba LLC v. SEC*, No. 6:24-cv-00153-ADA-DTG (W.D. Tex. Mar. 25, 2024), ECF No. 1.

our proposal to the Commission's Crypto Task Force to establish clear regulatory rules of the road for airdrops and create a pathway for digital asset issuers to expand these distributions to include U.S. persons.

This proposal is purposely narrow, and not exhaustive of Paradigm's thinking on the subject of airdrops, nor intended to address whether a digital asset *itself* constitutes a type of security, such as an investment contract. We welcome the opportunity to submit further comment on this issue to the Commission Crypto Task Force.

II. Summary of Relevant Law

An airdrop is a common method of distributing digital assets whereby an issuer provides digital assets free of charge to software users who satisfy certain eligibility criteria. Airdrops may be conducted for a variety of reasons, such as to reward loyal or early users of a particular product, promote an application, build a community, decentralize governance authority over an open-source protocol, or award high-scoring players of a video game, among others. Although most digital assets, such as bitcoin and ether, are not securities, securities may be offered and sold in a digital asset ("tokenized") format and certain digital asset transactions may constitute securities subject to registration with the Commission.

Section 5 of the Securities Act makes it unlawful for any person, directly or indirectly, to make use of any means or instruments of interstate commerce to offer a security for sale unless a registration statement has been filed with the Commission.[4] Section 2(a)(3) defines the term "offer" to mean "every attempt or offer to dispose of, or solicitation of an offer to buy, a security or interest in a security, for value."[5] Section 2(a)(3) also defines the term "sale" to mean "every contract of sale or disposition of a security or interest in a security, for value."[6] Courts have interpreted these terms broadly[7] and reasoned that Congress intended "to embrace a wide range of conduct from initial solicitation or inducement to the actual offer and sale."[8] Given the breadth of these definitions, digital asset industry participants have raised questions to the Commission as to the status of airdrops as offers or sales of securities under the Securities Act.

Over a quarter century ago, the Commission followed a U.S. District Court for the Southern District of New York opinion in concluding that an offer or sale may exist in the absence of monetary value and such a determination looks beyond the provision of monetary consideration.[9]

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4 15 U.S.C. § 77e(c).

5 *Id*. § 77b(a)(3).

6 *Id*.

7 For example, the term "offer to sell" goes well "beyond the common law concept of an offer." *SEC v. Cavanagh*, 155 F.3d 129, 135 (2d Cir. 1998); *In the Matter of Carl M. Loeb, Rhoades & Co.*, 38 S.E.C. 843 (Feb. 9, 1959).

8 *SEC v. Galaxy Foods, Inc*., 417 F. Supp. 1225, 1242–43 (E.D.N.Y. 1976), (citing *SEC v. Chinese Consol. Benev. Ass'n*, 120 F.2d 738 (2d Cir. 1941)), *aff'd*, 556 F.2d 559 (2d Cir. 1977).

9 *See*, *e.g.*, *In the Matter of Joe Loofbourrow*, Securities Act Release No. 7700 (July 21, 1999); *In the Matter of Theodore Sotirakis*, Securities Act Release No. 7701 (July 21, 1999); *In the Matter of Wowauction.com Inc. and Steven Michael Gaddis*, Securities Act Release No. 7702 (July 21, 1999); *In the Matter of Web Works*

The Commission reasoned that a sale may be supported by minimal consideration, such as where the recipient of a security receives the instrument for free in exchange for providing personally identifiable information to an issuer, referring a friend to an issuer's platform or engaging in marketing and promotional activities for an issuer.[10] Importantly, the Commission reached this conclusion in a series of adjudications that involved distributions of common stock, a type of security. The outcome would have been different had the defendants distributed a non-security good to their loyal customers. Indeed, it is common practice for companies to reward loyal customers and users. For example, Microsoft maintains a rewards program called "Microsoft Rewards" whereby its customers can earn "points" by browsing the web using Microsoft's search engine, Bing, or engaging in gameplay via Microsoft's gaming console, Xbox.[11] These points are redeemable for gift cards, sweepstakes entries, nonprofit donations and other items.[12] However, the Section 5 registration requirement is applicable solely to offers or sales of *securities*.

Moreover, the Commission has made clear that distributions of a security whereby the recipient does not individually bargain to contribute cash or other tangible or definable consideration in exchange for a security are not offers or sales of a security subject to registration under the Securities Act.[13] It is a black letter contract law principle that consideration must be "bargained-for" or "sought by the promisor in exchange for his promise and is given by the promisee in exchange for that promise."[14] In turn, the Commission has opined that a grant of stock under an employee benefit plan or similar program does not constitute a "sale" under the Securities Act since employees "do not individually bargain to contribute cash or other tangible or definable consideration to such plans."[15] However, distributions of securities in which there are "both an investment decision and the furnishing of value" are subject to registration as sales of a security.[16] Although the term "value" is not defined in the Securities Act, the Commission's Staff has taken the view that value includes "all ordinary forms of consideration, such as cash, property, services, or the surrender of a legal right."[17] Indeed, the Commission's Staff has determined that a waiver or surrender of a right constituted "value" in the context of the "extremely broad" scope of the term "sale" under the Securities Act.[18]

III. Proposed Interpretation

Marketing.com, Inc. and Trace D. Cornell, Securities Act Release No. 7703 (July 21, 1999); (collectively, the "**Free Stock Cases**"); *SEC v. Harwyn Industries Corp.*, 326 F. Supp. 943 (S.D.N.Y. 1971).

[10] *See*, *e.g.*, the Free Stock Cases.

[11] Microsoft, *Microsoft Rewards*, https://www.microsoft.com/en-us/rewards/about.

[12] *Id*.

[13] Employee Benefits Plans; Interpretations of Statute, 45 Fed. Reg. 8960, 8968 (Feb. 11, 1980).

[14] *See* Restatement (Second) of Contracts § 71 (1981).

[15] Employee Benefits Plans; Interpretations of Statute, 45 Fed. Reg. 8960, 8968 (Feb. 11, 1980).

[16] *Id*. at 8961.

[17] *Id*. at 8969.

[18] *See e.g.*, *Id.*; Letter of Gen. Couns. Discussing the Question of Whether A Sale of A Sec. Is Involved in the Payment of A Dividend., Release No. 929 (July 29, 1936).

The Commission should establish that the distribution of a digital asset—even one that qualifies as a security or object of an investment contract—via an airdrop does not constitute an "offer" or "sale" for purposes of the Securities Act if:

- the issuer or other distributor does not promise to the recipient prior to the distribution of the digital asset that the recipient will be eligible to receive such digital asset (or right to claim such digital asset) based on the recipient's future activity; or

- (a) the issuer or other distributor transfers a digital asset (or provides the right to claim a digital asset) to the recipient based upon the recipient's past activity or satisfaction of certain past-looking eligibility criteria; and (b) the issuer or other distributor does not solicit the recipient to give to the issuer or other distributor fiat currency, digital assets or other monetary consideration in advance of a distribution of digital assets in exchange for airdrop eligibility (or the right to claim an airdrop).[19]

Further, the Commission should opine that for tokens that are not securities, it has no jurisdiction over them and cannot limit or regulate airdrops of them.

IV. Non-Exhaustive Examples

We provide the following non-exhaustive examples of airdrop transactions that should not be deemed to constitute an offer or sale of a security within the meaning of Section 5 of the Securities Act:

- *Example #1*. An issuer distributes a digital asset ("Digital Asset A") to persons who hold a particular type of digital asset ("Digital Asset B") in their digital wallet. Prior to the distribution of Digital Asset A, the issuer did not promise to holders of Digital Asset B that such persons would be eligible to receive any distributions of digital assets.

- *Example #2*. A distributor provides digital assets free of charge to users of a software application who satisfy certain eligibility criteria based upon such users' use of the application. Airdrop eligibility is solely based on the users' use of the application prior to the date of the distribution. Users do not exchange any property or monetary consideration for the digital assets.

- *Example #3*. A software development firm provides digital loyalty points to users of a software application based upon such users' use of the application. The firm does not promise that the points will have any value in the future. The software development firm subsequently announces that the software application will incorporate a native digital asset. An issuer generates the digital asset. Loyalty points holders are able to claim a portion of the software application's digital asset that is determined based upon the holder's loyalty point holdings.

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[19] This would exclude speculative and insubstantial forms of consideration with subjective potential benefit to an issuer, such as inputting a digital wallet address into a website or using a software application. Paradigm submits that such forms of consideration are not "tangible" or "definable."

- *Example #4*. A distributor provides digital assets free of charge to users of a software application who are actively involved in the software application's community, such as persons who join the application's message boards, follow the application's social media account and participate in promotional campaigns.

- *Example #5*. A development company engineers a new software network that utilizes a native digital asset. Prior to deploying the software network (or "mainnet"), the company deploys a testing environment (or "testnet") version of the software and interested users transact via the testnet. Following the initial deployment of the testnet, an issuer announces that persons who use the testnet during a specific period will qualify to participate in an airdrop of the software's native digital asset when the mainnet is fully functional and operational. Upon the launch of the software's mainnet, the issuer provides digital assets to eligible users who claim the digital assets by signing a network transaction through a graphical user interface and paying a transaction fee on the network.

- *Example #6*. A digital asset trading platform operator distributes a digital asset issued by a third-party software developer free of charge to users of the trading platform. Users are subject to the trading platform's standard trading fees. Prior to the distribution, the trading platform operator makes several social media posts that announce the upcoming airdrop and detail the eligibility criteria, which are based on a snapshot of users' trading platform digital wallet activity and holdings.

- *Example #7*. Shortly after launching a new product, the development company enacts a new user acquisition strategy to encourage users of other similar products to try the new product by airdropping free digital assets to those users.

V. Conclusion

Paradigm appreciates the Crypto Task Force's consideration of this proposal. We would be pleased to further engage with the Crypto Task Force as the Crypto Task Force considers whether certain distributions of digital assets via airdrops constitute offers or sales of securities under the Securities Act.