



December 6, 2022

Vanessa A. Countryman  
Secretary  
U.S. Securities and Exchange Commission  
100 F Street, NE  
Washington, DC 20549-1090

**Re: Petition for Rulemaking – Digital Asset Issuer Registration and Reporting**

Dear Ms. Countryman:

Coinbase Global, Inc. (“Coinbase”) is filing a comment in response to our July 21, 2022 petition for rulemaking on digital asset securities Regulation (“Petition”).

As we explained in our Petition, the U.S. does not currently have a functioning market for crypto securities, and in particular investment contracts involving digital assets (“ICDAs”). A key inhibitor to such a market is the lack of a workable set of regulatory requirements for prospective digital asset issuers to register offerings deemed to involve an investment contract and make corresponding disclosures in compliance with securities laws. Issuers and investors would benefit from clear rules adapted to ICDAs that promote compliance and foster safe and transparent practices, including by providing investors with information material to evaluating ICDAs.

In our comment today, we propose a framework (attached as an appendix) designed to achieve this. If implemented, we believe it would create a reasonable and clear path for digital asset developers to raise capital from U.S. investors, provide a disclosure foundation to make ICDAs eligible for trading through SEC-registered intermediaries and platforms, and thus create the necessary economic incentive for a vibrant secondary market in digital asset securities with strong investor protections.

Our views are based on our extensive work with digital asset development teams and years of making asset listing decisions based on legal, compliance, and information security considerations. As we explain in more detail below, the needs of ICDA investors differ substantially from investors in traditional securities because the purpose of ICDAs and the manner in which an ICDA issuer typically offers digital assets is substantially different than an initial public offering of traditional securities. Accounting for these differences in an appropriately tailored registration and reporting regime would better protect investors, provide workable guidance to issuers, and give the SEC greater insight into the health and viability of the market itself.

## Digital Assets – And ICDA – Are Different

Although federal securities laws have recognized “investment contracts” since 1933, SEC rules focus primarily on traditional debt and equity, and do not address the unique features of investment contracts. ICDA, which incorporate distributions of digital assets, present an additional layer of new features that do not exist in any other class of securities. Recognizing that ICDA are different from traditional securities is critical to establishing a proper regulatory framework. Below we describe three properties of these assets that need to be accounted for in order to establish a workable and effective registration and reporting regime.

### 1. Different information informs investment decisions

Investors in ICDA require different information than what is found in traditional securities disclosures for companies issuing debt and equity. Unlike an equity stake in a company, an ICDA does not give the holder any residual economic interest in the issuer. So, while traditional securities reflect the value of the issuer as a whole, and depend on the issuer’s financial well-being, ICDA reflect the value of a specific digital asset project, which can depend on factors that are not specifically enumerated in securities disclosure requirements under regulation S-K. These factors center on the technical details about the protocol or networks on which the digital asset operates, how the code may be updated or changed, or how transactions are validated. A principles-based disclosure approach for ICDA-specific disclosures can, to some extent, accommodate these differences, but there is also an opportunity to organize and report disclosures as a standardized schedule of decision-useful information. We provide examples of how this could work in our proposed framework, which calls for disclosure of information about the ICDA issuer, the investment contract, and the underlying digital asset.

### 2. Digital Assets Have Intrinsic Utility

An ICDA involves the sale of digital assets that are often designed to be used in exchange for goods or services on a decentralized network. In contrast, traditional securities represent a claim on the profitability of the corporate issuer, but otherwise have no intrinsic use or consumptive value. For example, a share of Apple stock is not needed to operate an iPhone, while digital assets are often needed to, among other things, execute smart contracts on blockchain protocols and/or applications. In many cases, continuous operation of blockchain protocols requires the programmatic distribution of digital assets, for example, as an economic incentive or reward given to protocol participants for securing or validating transactions on a blockchain. This utility makes a digital asset an integral part of the operation of the protocol even if the ICDA separately also has the qualities of an investment. An important implication is that the intrinsic utility of a digital asset can only be fully realized when they are held and used outside the confines of a securities dealer, bank, or other qualified custodian. That is, using or

transferring the underlying digital asset to access or transact over a good or service should not be viewed as always involving a securities transaction.

### 3. Control Can Become Decentralized Over Time

One of the primary goals of many digital asset development teams is to eventually relinquish control over their protocol to a community of users. In practice this means that after the project is operational and reaches a critical mass of users, the team's practical control over the live protocol and digital asset diminishes significantly, if not entirely. An initial sponsor of the protocol may dissolve or disaffiliate from the protocol initially (e.g., by relinquishing IP rights to a separately managed and owned, arm's length entity) or otherwise relinquish control gradually over time.

Regardless of the path to decentralization, digital assets can live and thrive without their issuer. In contrast, traditional securities like debt and equity are inextricably tied to the viability of an issuer as a going concern.

Critically, for an ICDA, there comes a point where the original development team may not have a unique ability to modify or influence the functionality of the digital asset or protocol and/or application on which it functions. At this time, the development team is no longer in a position to be the primary source of decision-useful information to digital asset holders. Indeed, once this transition occurs, the information asymmetries that existing securities laws are designed to alleviate disappear. Instead, the value of the digital asset, and implied return on capital from holding it, flows from the use and efforts of a community of users. Therefore, after this point, there is limited to no continued benefit to market participants in requiring the ICDA issuer to file reports with the SEC.

### Path to a Workable and Effective Registration and Reporting Framework

The unique features of ICDA's pose certain challenges to the existing securities law frameworks. But these challenges are not insurmountable. Our proposed disclosure framework provides a path for sale of ICDA's to the general public and to make the ICDA's eligible for trading through SEC-registered intermediaries and platforms. Importantly, this framework accounts for the fact that the goal of many ICDA issuers is to develop protocols or networks that eventually operate without any ongoing effort on their part.

Our proposed framework for ICDA's depends on some overarching considerations.

- A principles-based approach to disclosures for ICDA's must be augmented with a publicly disclosed, standardized set of requirements and expectations to facilitate a streamlined issuance, trading, and reporting process – one that accommodates the practical realities of small development teams that do not plan to grow into large organizations.

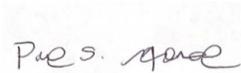
- The disclosure regime must define an *ex ante* set of conditions whereby reporting is no longer required. Without a specified exit process, there will not be sufficient incentive for the vast majority of ICDA issuers to enter a US registration framework, driving innovation offshore.
- The criteria for exiting SEC reporting following the issuance of an ICDA must be clear enough that issuers can reasonably exit through a notice and self-certification process. The trigger for exit should be the point at which the issuer is no longer exercising essential managerial control over the project, or its ongoing involvement with the project otherwise no longer meets the definition of an investment contract security.
- To enable use and consumption of digital assets underlying the ICDA at all times during the protocol development, an issuance and reporting regime that enables secondary market trading should not unduly impede the self custody, transfer, or use of the digital assets.
- While our focus here is on issuer offers and sales of ICDA's and ongoing reporting, we note that it is equally important for the SEC to develop a workable and effective regulatory regime for trading platforms to transact in ICDA's, which similarly does not exist today. Given that the SEC has consistently stated that SEC-registered platforms cannot facilitate trading in digital asset securities not offered and sold pursuant either to an effective registration statement or exemption from registration, providing a path toward registration of ICDA offerings is a necessary prerequisite to compliant secondary market trading. We refer to our petition on the broader set of issues and questions that require action.

We are broadly encouraged by the statements the Chair has made about flexibility the Commission could use to address digital asset disclosures, e.g.,:

*“Given the nature of crypto investments, I recognize that it may be appropriate to be flexible in applying existing disclosure requirements. Tailored disclosures exist elsewhere — for example, asset-backed securities disclosure differs from that for equities.”<sup>1</sup>*

It is in the spirit of this suggestion that we are proposing our framework.

Sincerely,



Paul Grewal  
Chief Legal Officer  
Coinbase Global, Inc.

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<sup>1</sup> [https://www.sec.gov/news/speech/gensler-sec-speaks-090822#\\_ftnref12](https://www.sec.gov/news/speech/gensler-sec-speaks-090822#_ftnref12)

# Appendix

## Proposed ICDA Disclosure Framework

*The proposal below would apply only to investment contracts involving digital assets (ICDAs) that are issued on a blockchain or distributed ledger. The proposal is not intended to be applicable to equity, debt or other types of traditional securities merely issued in digital form.<sup>2</sup>*

### ICDA OFFERING DISCLOSURE

An ICDA issuer seeking to offer and sell digital assets to the general public would be required to file with the SEC an initial disclosure including the following information: (1) Issuer-Related Disclosures; (2) Investment Contract Disclosures; (3) Digital Asset-Specific Disclosures:

#### (1) Issuer-Related Disclosure

(Aligned with disclosure requirements in Regulation S-K or AB to elicit comparable but more appropriately tailored information)

- Security transactional and risk factor information
  - Offering summary (S-K 503)
  - Intended use of proceeds (S-K 504)
  - Determination of offering price (S-K 505)
  - Plan of distribution (S-K 508)
  - Material risks related to the offering (General and Specific) (S-K 105)
- Business description (e.g., S-K 101 + reg AB)
  - Business experience in the digital asset space
  - Information related to management and capitalization
  - Relationships with affiliated entities and other transactional parties (AB)
  - Material roles and responsibilities related to the digital asset, its development deployment and post-launch supporting activities (AB)
  - Permissible and restricted activities related to the protocol and/or digital assets (AB)
- Digital asset holder information (including lockups and release schedules, pricing, and discounts)

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<sup>2</sup> The term ICDA does not include an asset that provides the holder of the asset with any of the following rights in a business entity: (i) a debt or equity interest in that entity; (ii) liquidation rights with respect to that entity; (iii) an entitlement to an interest or dividend payment from that entity; (iv) a profit or revenue share in that entity *solely* from the entrepreneurial or managerial efforts of others; or (v) any other financial interest in that entity. These exclusions are consistent with those set forth in the proposed Lummis-Gillibrand Responsible Financial Innovation Act.

- Issuer digital asset holdings and rights (new)
- Digital assets authorized for issuance under compensatory digital asset plans (S-K 201)
- Digital asset holdings (and rights to digital assets) of management and owners (or affiliated owner groups) of more than 5% of digital assets (S-K 403)
- Representations and warranties (reg AB)
  - Representations and warranties relating to the digital assets, remedies available against transactional parties for such reps/warranties, and information on how any transaction agreements can be modified or amended and/or whether there are any material claims that other parties may have on the digital assets
- Financial disclosures and MD&A
  - To the extent material to the ICDA investment, issuer financial statements covering the two most recently completed fiscal years or such shorter period as the issuer has been in existence (reg S-X)
  - MD&A focused on issuer capital deployed to develop the digital asset and protocol and/or application over the period covered by the financials (S-K 303)

## (2) Investment Contract Disclosure

(Relevant disclosures not specifically elicited by existing rules)

- **Description of Investment** – Information about the investment opportunity or common enterprise
  - Initial and ongoing rights and obligations associated with the investment contract
  - How investors could expect profits from the issuer’s managerial efforts
  - Anticipated future development, including features, integrations, functionality, etc. (“Key Milestones”)
- **Relevant transactional parties** – to the extent applicable and material
  - Any entity (other than the issuer) responsible for significant development efforts related to the digital asset (AB)
  - Key digital asset-related service providers material to the asset or offering

## (3) Digital Asset-Specific Disclosures

(Information specific to the operation of the digital asset or protocol)

- **Digital Asset Functionality** – Commercial and operational information about the digital asset and the protocol on which it will function
  - Technical description of the digital asset and the protocol on which it will function (e.g. consensus mechanism, on-chain components, smart contracts, etc.)

- Intended and actual functionality of the digital asset and the protocol on which it will function
  - Calculations underpinning distribution of digital asset rewards, if any, whether through staking, reallocation of network fees, or some other mechanism
  - Results of any third-party security and code audits completed
  - Risk factors related to the digital asset or protocol on which it will function that may materially affect the digital asset’s functionality and/or utility
- **Digital Asset Economics (“Tokenomics”)** – Digital asset supply and distribution information, pricing, lockups, and release schedules
    - Initial supply and any contemplated or potential changes in digital asset supply
    - Digital assets distributed via consensus mechanism
    - Digital assets distributed to:
      - Issuing entity, sponsor and/or foundation, community, or other
- **Schedule Digital Asset (“DA”)** – A standardized schedule of common, digital asset-specific information that is material to understanding the operation of the digital asset and protocol and/or application in which it functions.<sup>3</sup> This information provided by issuers should be comparable across projects and protocols. See example items below.

## ICDA SECONDARY MARKET DISCLOSURE

ICDA issuers that previously sold ICDA’s other than through the ICDA Offering Disclosure framework would be required to provide an initial disclosure for the ICDA’s to be eligible for trading through an SEC-registered intermediary or platform, including on a National Securities Exchange, through a broker-dealer on an alternative trading system (ATS), or OTC quotations.

- Information contained in the ICDA Offering Disclosure would satisfy this requirement. However, an ICDA Secondary Market Disclosure would not need to include the disclosures listed under the section “Security Transactional Summary and Risk Factors”.

## ONGOING DISCLOSURES

Ongoing disclosures should be a part of any ICDA Offering Disclosure or ICDA Secondary Market Disclosure framework and would be required until the issuer has filed a Closing Certification. The following disclosures would be required only to the extent they are material to a continued understanding of the ICDA:

- Annual updates to the following information from the ICDA Offering Disclosure or ICDA Secondary Market Disclosure

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<sup>3</sup> These disclosures could be presented on schedule analogous to Schedule AL, used with offerings conducted pursuant to Regulation AB.

- Issuer-Related Disclosures
  - Business description
  - Digital asset holder information
  - Financial disclosures and MD&A
- Investment Contract Disclosures
  - Progress towards completing Key Milestones anticipated in Investment Contract Disclosures and any new anticipated milestones
- Asset-Level Disclosures
  - Results of digital asset audits
  - Digital asset functionality
  - Digital Asset Economics
  - Schedule DA
- Material event reporting
  - Any fundamental change to the digital asset or protocol or any event impacting the ongoing viability of the project or issuer
    - E.g. hacks, breaches, and other cyber security events; digital asset and/or protocol mergers; departure of key personnel; material modification to rights of digital asset holders; issuer change of control
  - This would not require disclosure of routine, ministerial changes (e.g., regular code updates)

## **PREEMPTION OF STATE LAW**

Offers and sales of ICDA's pursuant to any ICDA Offering Disclosure framework are not subject to state securities laws registration and qualification requirements.

## **SUFFICIENCY OF INFORMATION**

The initial and ongoing disclosure provided pursuant to any ICDA Offering Disclosure or ICDA Secondary Market Disclosure framework would satisfy the specified information requirements of Exchange Act Rule 15c2-11(b) and adequate current public information requirements of Securities Act Rule 144(c).

## **DISCLOSURE RESPONSIBILITY OF ISSUER-AFFILIATED ENTITIES**

Consistent with market practice in certain other asset classes (e.g. asset-backed securities), the issuance of an ICDA may involve one or more affiliated entities. Only one entity would be responsible for the required disclosures (referred to herein as the “issuer”) and should be the entity providing the essential ongoing managerial services related to the digital asset and protocol and/or application. The ICDA issuer may not necessarily be the same legal entity that mints or distributes the digital asset.

## **DIGITAL ASSET TRANSFERABILITY AND USE**

Nothing in this disclosure framework should be construed as limiting the ability of a holder of a digital asset purchased in an ICDA transaction to self custody, freely transfer or use the digital asset for consumptive or other utility purposes.

- The issuer’s contractual reps and warranties related to the digital asset transfer with the digital asset to subsequent purchasers

## **CLOSING CERTIFICATION**

In the event an ICDA issuer no longer exercises essential managerial functions for or control over a digital asset, or the digital asset no longer otherwise meets the definition of a security, the ICDA issuer may file a Closing Certification with the SEC, attesting that such criteria have been met.

- The Closing Certification would not affect the remedial rights of any party to an ICDA transaction.
- Consistent with the requirements of Exchange Act Rule 12g-4:
  - An issuer’s duty to file reports with the SEC shall be suspended upon filing of the Closing Certification
  - The SEC would have 90 days to review and respond to a Closing Certification
  - If Closing Certification is subsequently withdrawn or denied, the issuer would be required to file all reports which would have been required had the Certification not been filed

## **SCHEDULE DA**

(non exhaustive list of potentially applicable Schedule DA disclosures)

### **Governance and Control**

- Identify parties that:
  - Organize and implement protocol features and changes thereto
  - Coordinate social media, marketing, and press relations
  - Can change digital asset supply and/or release schedules
  - Have access to MNPI
  - Own IP rights and affiliation with issuer
  - Are responsible for code audits
- Description of any decentralized governance over the protocol or digital asset
  - Voting eligibility requirements
  - Distribution of voting power
  - Description of what can be controlled by the decentralized governing body
- Protocol development
  - Scope and number of third party contributions to project, including the number of third party developers and dApps
  - Frequency and number of code contributions in code repository
  - Process for code change implementation
  - Specify ongoing development efforts

### **Computation**

- Number of participants providing hash power to and operating nodes on the protocol and/or application upon which the digital asset functions
- Measure of computational power (hash rate), including any limit on the number of transactions that can be verified on a blockchain network in a given block
- Process and eligibility to create How nodes are created and how open access is to node participation, including estimated costs to operate a node and basis for estimate
- Estimated cost to successfully attack the network and basis for estimate
- Number of blockchain wallet choices available to an end user for purposes of interactions with the protocol and/or application
- Software licensing information, including whether code base underlying digital asset, protocol and/or application are published as open source software

### **Economic considerations**

- Insider, affiliates, early contributor digital asset ownership
- Market capitalization and liquidity of digital asset

- Degree of digital asset in circulation compared to total digital asset supply, digital assets locked and/or digital assets available for staking
- Description of network transaction fees
- Funding releases or rewards for developers, employees, contributors, etc.
- Efforts for exchange listing(s), market making, airdrops, etc.
- Number and list of known exchanges where digital asset is listed (centralized or decentralized)

**Potential additional information**

- Network layers and cross-chain integrations
- Number of network forks