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March 13, 2025

VIA EMAIL

Crypto Task Force Chairman and Commissioner Hester M. Peirce
U.S. Securities and Exchange Commission
100 F Street, N.E.
Washington, DC 20549-0213

Re: Recommendations Regarding a Safe Harbor for Certain Airdrops and Incentive-Based Rewards of Network Tokens

Dear Crypto Task Force Chairman and Commissioner Peirce:

Andreessen Horowitz ("a16z" or "we") appreciates the opportunity to provide recommendations regarding the circumstances under which certain public distributions of crypto assets[1]—airdrops and incentive-based rewards of network tokens (as defined below)—should be excluded from federal securities laws. We welcome opportunities to meet with Securities and Exchange Commission ("SEC" or "Commission") staff, answer any questions that the Commission may have, and discuss our comments below in more detail.

We recognize that federal securities laws do not extend to crypto assets that do not constitute securities under the Securities Act of 1933 or transactions of crypto assets that are not otherwise subject to federal securities laws. As a result, federal securities laws already do not apply to many airdrops and incentive-based rewards of crypto assets. However, such determination is subjective and difficult for entrepreneurs, slowing the pace of innovation without providing investor protections. The purpose of this submission is to create clear rules by providing clear criteria for circumstances under which airdrops and incentive-based reward distributions should be excluded from securities laws because they do not give rise to the risks federal securities laws are intended to address. In such cases, Section 5 registration is unwarranted and inappropriate.

This approach is therefore intended to establish limits with respect to the application of federal securities laws to airdrops and incentive-based rewards programs to safeguard them from becoming subject to retroactive application of federal securities laws by regulators. Not all airdrops and distributions of incentive-based rewards will be able to avail themselves of this safe harbor. On the contrary, *only* those airdrops and incentive-based reward programs which *do not* engender the risks that Section 5 was designed to address should be eligible. If effectively crafted, this approach would help fulfill the Commission's mandate of protecting investors, maintaining fair, orderly, and efficient markets, and facilitating capital formation, while also promoting responsible innovation in blockchain technology.

A16z is a venture capital firm that invests in seed, venture, and late-stage technology companies, focused on bio and healthcare, consumer, crypto, enterprise, fintech, and games. A16z currently has more

[1] For the purposes of this discussion, by crypto assets, we mean a digital form of property that is recorded on, and can be possessed and transferred person-to-person, through the use of a blockchain network or other similar technology.

than $74 billion in assets under management across multiple funds, with more than $7.6 billion in committed capital for crypto funds. In crypto, we primarily invest in companies using blockchain technology to develop protocols that people will be able to build upon to launch Internet businesses. Our funds typically have a 10-year time horizon, as we take a long-term view of our investments, and we do not speculate in short-term crypto asset price fluctuations.

I. Introduction

We strongly support the goals of the Commission's Crypto Task Force ("Task Force") to offer guidance on the application of federal securities laws to the crypto asset market and recommend pragmatic policies capable of promoting innovation and protecting investors. As the Task Force carries out its mandate, we urge it to specifically provide clarity on the application of federal securities laws to airdrops and incentive-based reward programs by creating a safe harbor for such crypto asset distributions that meet certain criteria. The goals of this submission are to elucidate the benefits of this approach and to propose conditions for a safe harbor to ensure that it helps fulfill the Task Force's dual mandate of fostering innovation and safeguarding investors in the market for crypto assets.

Crypto assets are often distributed to third parties via airdrops and incentive-based rewards for free or de minimis consideration. These distribution mechanisms are critical to enable blockchain projects to function,[2] but also enable them to achieve decentralization—they not only enable projects to disperse control of the underlying blockchain or smart contract protocol (each, a "blockchain network"), they ensure that the blockchain network can operate autonomously.[3] When a blockchain network achieves decentralization, it provides substantial benefits such as promoting competition, safeguarding freedoms, rewarding stakeholders, reducing information asymmetries, and otherwise mitigating risks for market participants (see Section II). Crucially, because blockchain networks are capable of decentralization, they can function more like public infrastructure than proprietary software, enabling developers to bootstrap a wide variety of applications onto a single network, such as decentralized social media networks, identity management protocols, and video games.

At present, market participants face significant uncertainty when assessing whether a given airdrop or incentive-based reward program constitutes a securities transaction and therefore may require registration under Section 5 of the Securities Act. Subjecting airdrops and incentive-based reward programs to registration is not only unnecessary when certain conditions are met (see Section III), but would also impinge upon a blockchain network's ability to achieve and maintain decentralization because it would force such networks to reintroduce centralized intermediaries in order to comply with the requirements of federal securities laws (see Section II). This would vitiate the essence of blockchain networks, whose fundamental purpose is decentralized operation—operation without human intervention or control. It would also in many cases be incorrect as a matter of law. To be an investment contract, there must be an "investment of money" by the recipient in a common enterprise with a reasonable expectation of profit derived from the efforts of others.[4] But airdrops and incentive-based rewards do not typically

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[2] Tim Roughgarden, *An Axiomatic Approach to Block Rewards*, YouTube (Jul. 2020), https://www.youtube.com/watch?v=WyRyWQwm0x0.
[3] a16z Crypto, *Defining Decentralization: Control* (Mar. 2024), https://a16zcrypto.com/posts/article/defining-decentralization-control/.
[4] *SEC v. W. J. Howey Co.*, 328 U.S. 293 (1946).

require an investment of money—they are free or executed for de minimis consideration—and should not be regulated as securities offerings.

However, in the Commission's 2019 *Framework for "Investment Contract" Analysis of Digital Assets*, the SEC asserted that "[...] an airdrop may constitute a sale or distribution of securities, regardless of whether there is a lack of monetary consideration."[5] For the reasons further elaborated below (see Section III.C.) this position misstates the law, creates confusion for businesses and consumers, and hamstrings innovation. Worse, uncertainty in this area has led to numerous projects excluding U.S. persons, meaning that U.S. regulatory policy has effectively precluded U.S. persons from receiving ownership (for free) of the networks that will underpin the future internet.

Recognizing this lack of clarity and the benefits of airdrops and incentive-based reward programs (as well as the unsuitability of traditional regulatory frameworks for certain airdrops and incentive-based reward programs), recent legislative and regulatory efforts have endeavored to create rules that are fit-for-purpose: mitigating risks while facilitating innovation. H.R. 4763, the Financial Innovation and Technology for the 21st Century Act ("FIT21"),[6] proposed an exemption from Section 5 of the Securities Act of 1933 for issuances of digital assets that meet certain criteria. Commissioner Peirce's Token Safe Harbor Proposal 2.0[7] likewise seeks to provide developers with a "grace period" during which, subject to specific conditions, they would be exempted from the registration provisions of federal securities laws.

In line with these proposals, we strongly recommend that the Commission create a safe harbor for airdrops and incentive-based rewards programs meeting certain conditions. As mentioned above, not all airdrops and distributions of incentive-based rewards will be able to avail themselves of this safe harbor. On the contrary, *only* those airdrops and incentive-based reward programs which *do not* engender the risks that Section 5 was designed to address should be eligible. Importantly though, the failure to meet the conditions specified herein and qualify for the safe harbor should not create a presumption that any given airdrop or incentive-based reward is subject to federal securities laws. Rather, such distributions should be assessed under traditional approaches to the application of the federal securities laws.

II. Airdrops and Incentive-Based Rewards of Network Tokens Help Facilitate Decentralization and Mitigate Risks

Blockchain networks are often started by traditional private development companies ("DevCos"). At a project's inception, DevCos undertake critical tasks including developing and launching a blockchain network. As with traditional tech startups, DevCos also raise capital in private placements of their equity to institutional investors to resource their efforts.

Once development of a blockchain network is substantially advanced and the network is "functional" (see Section III.A.), DevCos typically seek to publicly launch their networks, which is a key step in the real-world deployment of blockchain technological innovation. In the case of layer-1

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[5] SEC, *Framework for "Investment Contract" Analysis of Digital Assets* (Apr. 3, 2019), https://www.sec.gov/files/dlt-framework.pdf

[6] 118th Congress (2023-2025), H.R. 4763 - Financial Innovation and Technology for the 21st Century Act (introduced July 20, 2023), https://www.congress.gov/bill/118th-congress/house-bill/4763.

[7] SEC, Statement on Token Safe Harbor Proposal 2.0 (Apr. 13, 2021), https://www.sec.gov/newsroom/speeches-statements/peirce-statement-token-safe-harbor-proposal-20.

blockchains, this often coincides with the launch of the network token (as defined below). For layer-2 blockchains and smart contract protocols, the network may be live well before launch of the network token. At some point during the development cycle, the generation of the native asset of the network occurs, with a portion of those network tokens then being distributed to employees, investors, advisors, and others subject to extended transfer restrictions.

These crypto assets are intrinsically linked to, and primarily derive their value from or are expected to primarily derive their value from, the programmatic functioning of the network ("network tokens").[8] Network tokens often have embedded utility; they may be used for network operations, to form consensus, to coordinate protocol upgrades, or to incentivize network actions. The networks to which these tokens relate also often (and in most cases should) contain economic mechanisms that drive the value of the token. These may include programmatic purchases, distributions, and other changes to the total token supply via token creation or burning to introduce inflationary and deflationary pressures in service of the network.

In most cases, the public launch of the network token is accompanied by a public distribution for no or de minimis consideration (an "airdrop"), such as historical engagement with or participation on the network. By broadly disseminating its network token via an airdrop, a blockchain network can help mitigate the risk that any single party or commonly orchestrated or centralized group can control the network. In addition, airdrops can drive the network effects of the network and ensure users are able to continue using and building on the network.

Following public launch, many blockchain networks rely on incentive-based reward programs for maintenance and security, which facilitate its autonomous operation. For example, both mining, in the case of Proof-of-Work ("PoW"), and staking, in the case of Proof-of-Stake ("PoS") blockchains, are consensus mechanisms used to ensure network security and incentivize stakeholders to perform operational activities. In a PoS blockchain, transactions are added by "validators," who are similar to "miners," only instead of performing calculations to "mine" new blocks, validators "stake" an amount of crypto assets as a pledge that they will perform validation work honestly. PoS blockchains then programmatically distribute rewards to validators for performing validation services, which are necessary for the system to function.

In addition, incentive-based rewards can be used to drive network effects by incentivizing more user activity that is beneficial to the network and its users.[9] The range of activities incentivized might include providing liquidity to a decentralized finance network, participating in decentralized governance, or posting to a decentralized social media network.

Airdrops and incentive-based rewards are therefore critical for blockchain projects to distribute control and to facilitate autonomy of the network. While these are just two critical aspects of decentralization, they better position the network to pursue decentralization along other measures, including to become permissionless, credible neutral, non-custodial, and economically independent.[10] All

[8] a16z Crypto, *Defining Tokens* (Feb. 2024), https://a16zcrypto.com/posts/article/defining-tokens/.
[9] a16z Crypto, *The Web3 Playbook: Using Token Incentives to Bootstrap New Networks* (Feb. 2024), https://a16zcrypto.com/posts/article/the-web3-playbook-using-token-incentives-to-bootstrap-new-networks/.
[10] Decentralization Research Center, *Designing Policy for a Flourishing Blockchain Industry* (Feb. 2025), https://thedrcenter.org/wp-content/uploads/2025/02/DRC-Designing-Policy-Final.pdf.

of which is to say that airdrops and incentive-based rewards typically are preconditions for blockchain technology to be deployed in practice on a widespread basis.

Once achieved, decentralization engenders myriad benefits:

- **Promoting Competition:** Decentralization enables blockchain networks to be credibly neutral[11] and composable.[12] This ensures that they function like public infrastructure and makes them attractive to build on top of. This then lowers the barrier to entry for anyone wanting to build an Internet business, as it provides the Internet infrastructure upon which they can build. As a result, decentralization promotes competition and the creation of new types of goods and services.

- **Safeguarding Freedoms:** Decentralization necessitates the broad distribution of control of blockchain networks among their stakeholders and ensures that the network effects of such systems accrue to such stakeholders, not just the companies that created them. By limiting the power that can accrue to companies in this manner, decentralization limits corporate power to gatekeep, censor, or otherwise infringe individual liberty. As a result, decentralization safeguards user freedoms as well as ameliorates the agency costs and conflict of interest concerns often associated with centralization.

- **Rewarding Stakeholders:** Decentralization enables the design of systems that prioritize stakeholder involvement – systems that are designed broadly serve the interests of all stakeholders, rather than a certain subset of stakeholders. For example, web3 systems can be designed to more equitably reward users and contributors, rather than being designed to maximise value of shareholders, as is the case with the corporate networks of web2.

In addition to these benefits, decentralization provides substantial protections to market participants by mitigating the risks arising from trust dependencies associated with network tokens, thereby justifying a different regulatory approach from what applies to ordinary securities.[13] Through the lens of a control-based framework for decentralization, network tokens can be insulated from control-related risks.[14] This is critical because whoever controls a system (a company, a network, etc.) controls the risks associated with the underlying asset of that system and can unilaterally affect or structure the risk associated with that asset.[15] Removing control via decentralization means more than just dispersing ownership though; it means eliminating mechanisms of control so that systems are

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[11] See Vitalik Buterin, Credible Neutrality As A Guiding Principle, Nakamoto (Jan. 3, 2020), https://nakamoto.com/credible-neutrality/.
[12] Smart Contract Composability, Ethereum, https://ethereum.org/en/developers/docs/smartcontracts/composability/ (last updated Aug. 15, 2022).
[13] See Miles Jennings, *Defining decentralization: It comes down to control* (Feb. 13, 2025), https://a16zcrypto.com/posts/article/defining-decentralization-control/.
[14] Miles Jennings, Jai Ramaswamy, Scott Walker, Michele Korver, David Sverdlov, & Aiden Slavin, *SEC RFI: A Control-Based Decentralization Framework for Securities Laws,* a16z crypto, (March 13,2025), https://a16zcrypto.com/posts/papers-journals-whitepapers/control-based-decentralization-framework-securities-laws/.
[15] Willa E. Gibson, *Securities as Investments at Risk: A Market Theory of Investment Contracts*, 67 Tul. L. Rev. 981 (1993), https://www.tulanelawreview.org/pub/volume67/issue4/securities-as-investments-at-risk.

autonomous, permissionless, credibly neutral, non-custodial, and economically independent.[16] It also means that participants in decentralized systems are not subject to traditional principal-agent problems and corporate informational asymmetries.

Because blockchain networks are capable of decentralization,[17] they can function more like public infrastructure than proprietary software, enabling them to derive their value from many independent sources, such as market forces, user demand for the underlying network, and the number of developers building on the network, rather than the managerial efforts of a single development team or managerial team. This substantially reduces or eliminates the risks associated with traditional securities where shareholders own shares but depend on directors and officers to set corporate strategy and run the business day-to-day, giving rise not only to information asymmetries but also to the kind of potential agency costs that corporate law addresses. Once decentralization is achieved, such information asymmetries and principal-agent problems do not exist. Consider, for example, Bitcoin and Ether, the value of which is determined independently of the efforts of any controlling party, with Apple stock, the value of which is dependent on the efforts of Apple Inc.'s management team and the performance of its business.

These benefits of decentralization can be achieved without subjecting holders of network tokens to additional risks. Because airdrops and incentive-based rewards are distributed programmatically in exchange for the ongoing performance of services, they do not in general pose the same risks that Section 5 was designed to address (see Section III.D.), and so should not be required to be registered. Further, whatever risks they do pose to token holders can be mitigated through well-tailored conditions unique to the underlying blockchain technology, as another dimension of differentiation as compared to the typical corporate form.

For these reasons, the Commission should, under the circumstances detailed below, exclude airdrops and other incentive based rewards of network tokens that are distributed in exchange for limited consideration from registration under Section 5 of the Securities Act of 1933.

III. Conditions Under Which Airdrops and Incentive-Based Rewards Should be Excluded

While airdrops and incentive-based rewards are key to facilitating and maintaining decentralization as a means of promoting blockchain network and application innovation, the distribution of crypto assets pursuant to these mechanisms may admittedly still pose risks. As such, only distributions that do not give rise to the risks Section 5 of the Securities Act of 1933 is intended to address should be eligible for the safe harbor under consideration. Further, in order to facilitate the ongoing functionality of the blockchain network, the safe harbor should specify that secondary market transactions of network tokens originally distributed in compliance with the safe harbor are similarly excluded from the application of federal securities laws, absent a significant change in circumstances following the qualifying distribution that materially alters the "economic reality" of ongoing transactions in the previously distributed assets.

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[16] Decentralization Research Center, *Designing Policy for a Flourishing Blockchain Industry* (Feb. 2025), https://thedrcenter.org/wp-content/uploads/2025/02/DRC-Designing-Policy-Final.pdf.
[17] Jennings, Ramaswamy, Walker, Korver, Sverdlov, & Slavin, *supra* note 14.

A five-part approach can be used to assess whether an exclusion would be appropriate for a given airdrop or incentive-based reward program. The safe harbor should require that: (1) the distribution is of a network token; (2) the blockchain network with which the network token is intrinsically linked is "functional;" (3) the distribution is broad and equitable; (4) the distribution is effected for limited consideration; and (5) transfer restrictions apply to certain related persons. Only distributions meeting each of these requirements should be excluded.

However, the failure to meet these conditions and qualify for the safe harbor should not create a presumption that any given airdrop or incentive-based reward is subject to securities laws. Rather, such distributions should be assessed under traditional approaches to the application of federal securities.

Each condition for the safe harbor is discussed in detail below.

A. Network Tokens

As a threshold question, only crypto assets that are properly designed and structured as network tokens should qualify for the safe harbor. As described above, networks tokens primarily derive their value or are expected to primarily derive their value from blockchain networks, which are capable of decentralized operation—operation without human intervention or control. This means their trust dependencies are inherently different from ordinary securities, whose value is dependent on systems or sources that are not capable of decentralized operation—centralized systems that require human intervention and control.[18]

Importantly, the investor-protection benefits of decentralization are applicable to a number of types of crypto assets, including "asset-backed tokens" like stablecoins, liquidity provider tokens and liquid staking tokens. But these benefits **cannot** be achieved by "company-backed tokens"—crypto assets that are intrinsically linked to, and primarily derive or are expected to primarily derive their value from, offchain systems or sources that are not capable of decentralized operations. These centralized systems require human intervention and centralized control, and consequently have trust dependencies that are similar to those associated with typical securities. For instance, if a token derives its value from a closed system controlled by a single entity, that entity can unilaterally alter the expected value of the token—the controlling entity could alter the purpose of the token or inflate the supply of the token, or even turn off the entire system, at will. Given such risks, where transactions of such crypto assets would be likely to attract investment, it is difficult to justify a safe harbor from federal securities laws for airdrops and incentive-based rewards that might facilitate the creation of a market that promotes investments in company-backed tokens.[19]

By limiting any safe harbor to network tokens, the Commission can ensure that such safe harbor is not used for assets that more squarely fall within the jurisdiction of the Commission.

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[18] Jennings, Ramaswamy, Walker, Korver, Sverdlov, & Slavin, *supra* note 14.

[19] For more information on company-backed tokens and how they compare to network tokens, see: Miles Jennings, Scott Duke Kominers and Eddy Lazzarin, *Network Tokens vs. Company-Backed Tokens* (March 5, 2025), https://a16zcrypto.com/posts/article/network-tokens-vs-company-backed-tokens/.

B. Functional Network

As a general matter, prior to a blockchain network becoming "functional," the network is de facto controlled by the DevCo and the potential for information asymmetries between the DevCo and network participants is extremely high. Without a functioning network, there is no way to ground expectations about the network's functioning in the observable reality of how the network has functioned in the past or is functioning in the present. With no information about the functioning of the network publicly available, and where there is no actual functioning to observe, promoters could make misleading statements if not subject to appropriate accountability or could withhold valuable information about the network functionality that they control. This subjects recipients of airdrops and incentive-based rewards pre-network functionality to the kind of risk that federal securities laws are geared toward remedying. Further, if a network is not yet functional, investors' and users' dependence on the DevCo in control of the pre-functional network inherently exposes them to considerable risks, including those stemming from the manual performance of operations and the risks of potential mistakes in calculation or data storage, as well as the ability for a controlling DevCo to make unilateral decisions and benefit insiders (including officers, directors, employees, shareholders, investors, advisors and consultants). For these reasons, airdrops and incentive-based rewards associated with blockchain networks that are not functional should not be considered for the safe harbor.[20]

Consequently, only airdrops and incentive-based rewards that are associated with "functional" blockchain networks should be eligible for this safe harbor. This functionality requirement need not rise to the level of requiring a project's entire development roadmap be achieved, but should mandate a baseline functionality which every qualified project should be capable of satisfying. In assessing whether a blockchain network is functional, regulators should require that it exhibits basic operational capacity and is capable of fulfilling its essential purposes absent the intervention of individual actors. This can be evaluated using the network's source code or can be attested to by the DevCo. A functional network is one that enables participants to transact through the updating of the state of the network, including, but not limited to, by transmitting and storing value, taking part in staking or other method of securing the blockchain network, participating in services provided by or an application running on the blockchain network, or partaking in a decentralized governance system.[21]

Importantly, this definition of functionality aligns with key legislative and regulatory proposals. It derives from FIT21 which, in May 2024, passed the U.S. House of Representatives with strong bipartisan support.[22] Likewise, it also aligns with the Token Safe Harbor Proposal 2.0, which would include a requirement to analyze whether a blockchain network is functional.[23] In line with these positions, regulators should seek to determine whether a network is functional to assess whether these exclusions would be appropriate for a given airdrop or incentive-based reward program.

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[20] 118th Congress (2023-2025), H.R. 4763 - Financial Innovation and Technology for the 21st Century Act (introduced July 20, 2023), https://www.congress.gov/bill/118th-congress/house-bill/4763.
[21] Jennings, Ramaswamy, Walker, Korver, Sverdlov, & Slavin, *supra* note 14.
[22] U.S. House Financial Services Committee, *House Passes Financial Innovation and Technology for the 21st Century Act with Overwhelming Bipartisan Support* (May 22, 2024), https://financialservices.house.gov/news/documentsingle.aspx?DocumentID=409277
[23] SEC, *Token Safe Harbor Proposal 2.0* (Apr. 13, 2021), https://www.sec.gov/newsroom/speeches-statements/peirce-statement-token-safe-harbor-proposal-20

C. Broad and Equitable Distribution

Another key consideration is whether the distribution is effected in a broad and equitable manner. Contrary to the goal of decentralization, network token distributions that are limited to a narrow group can, instead, serve to reify and enrich insiders. Inequitable distributions, where insiders received the majority, or a considerable minority, of network tokens, can likewise hold decentralization in abeyance by reinforcing the *voting control* of insiders. Similarly, if concentrated in a single party or group under common control, the dissemination of incentive-based rewards would also serve to undermine decentralization, reintroducing legacy risks such as agency costs, information asymmetries, and trust dependencies.

Thus, this exclusion should only apply to network token distributions that are broad and equitable. Any participant in a blockchain network should be capable of accessing an airdrops or incentive-based reward program. As with the abovementioned "functionality" criteria, this requirement also derives from FIT21, which requires that airdrops and incentive-based rewards be distributed in a wide and equitable manner.[24] Specifically, FIT21 required that airdrops and incentive based rewards be distributed in a broad, equitable, and non-discretionary manner based on conditions capable of being satisfied by any participant in the blockchain network, including as incentive-based rewards: (A) to users of the network token or any blockchain network to which the network token relates; (B) for activities directly related to the operation of the blockchain network, such as mining, validating, staking, or other activity directly tied to the operation of the blockchain network; or (C) to the existing holders of another network token, in proportion to the total units of such other network token as are held by each person.[25]

D. Limited Consideration

A defining feature of airdrops is that they are distributed for free or de minimis consideration. This characteristic is what distinguishes them from traditional sales. Likewise, distributions of network tokens via incentive-based reward programs are not made in exchange for monetary consideration. Rather they programmatically distribute network tokens to participants who support the ongoing maintenance and security of the network, or to users who help to drive network effects of the network. These forms of crypto asset distribution therefore do not pose the same risks as traditional sales. Crypto assets that are distributed in exchange for substantial monetary consideration, on the other hand, engender risks similar to traditional securities transactions, a distinguishing characteristic of which is the investment of financial value as consideration for an economic interest in, or claim to, a business enterprise.

It is also important to note that treating airdrops and incentive-based rewards of network tokens that occur for free or in exchange for de minimis consideration as securities transactions may be inconsistent with *Howey*.[26] The SEC has previously conceived that this investment prong of the *Howey* test could be satisfied by any theoretical benefit, writing that "the investment of 'money' need not take the form of 'cash.'"[27] But this is an overly broad interpretation of the law. To be an investment contract, there

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[24] 118th Congress (2023-2025), H.R. 4763 - Financial Innovation and Technology for the 21st Century Act (introduced July 20, 2023), https://www.congress.gov/bill/118th-congress/house-bill/4763.
[25] *Id.*
[26] *SEC v. W.J. Howey Co.*, 328 U.S. 293 (1946).
[27] SEC, *Framework for "Investment Contract" Analysis of Digital Assets* (Apr. 3, 2019), https://www.sec.gov/files/dlt-framework.pdf

must be an "investment of money" by the recipient in a common enterprise with a reasonable expectation of profit derived from the efforts of others. Although the courts have read *Howey* to not require cash consideration, they all require some form of meaningful consideration. In most airdrops of network tokens, recipients either do nothing to become eligible for the crypto asset, or they take an action that involves no money or meaningful consideration, like simply using the network or "following" a project on social media. They do not pay any money or provide valuable compensation, so no investment of money is made. Similarly, incentive-based rewards of network tokens are not distributed in exchange for meaningful monetary consideration, but rather transmitted for useful work such as securing a blockchain network or driving the network's network effects. In other words, where the user activity giving rise to an airdrop or incentive-based reward is most likely to benefit the network, rather than the DevCo, such activity may even facilitate its decentralization. So, in cases in which there is no payment of money or provision of valuable compensation is made, an airdrop or an incentive-based reward of network tokens should not satisfy the *Howey* test.[28]

Because airdrops and incentive-based rewards of network tokens that occur for free or in exchange for de minimis consideration should not satisfy the *Howey* test, and because they pose negligible risks, they should be eligible for this safe harbor. Recent legislative proposals concur with assessment, with FIT21 enabling end user distributions that do not involve an exchange of "more than a nominal value of cash, property or other assets."[29] Airdrops and incentive-based rewards exchanged for free or de minimis consideration should thus be eligible for this safe harbor, while those that occur in exchange for a more than nominal value of cash, property, or other assets should not. It is important to note that the creation of a liquid market could be viewed as "meaningful consideration" to insiders promoting airdrops. The proposed Safe Harbor should be structured to address this concern.

E. Robust Transfer Restrictions

In July 1999, the Commission brought a number of actions against issuers of "free stock" for violating the registration provisions of federal securities laws. These cases often revolved around dubious actors creating fraudulent companies and offering "free stock" as part of a broader scheme to generate public trading of their shares, boost stock prices and consummate other sales.[30] Many entrepreneurs offered free stock to people who agreed to provide information about themselves or pass information on to others. Seeking to promote their new internet domains, these businesses offered a quid pro quo: bring traffic to the website in exchange for shares. Given the broader context in which the "free stock" was being distributed, the Commission was reasonable in its actions against these schemes—these companies were offering shares in exchange for something of value, an action that would require them to be registered under federal securities laws.[31] In particular, the free distributions generated market interest to the benefit of insiders.

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[28] While this would mean that no safe harbor is required under Section 5 of the Securities Act, given the uncertainty that market participants face in evaluating whether even these airdrops amount to a securities transaction, we urge the Commission to clarify its position by creating a safe harbor along the lines proposed herein.
[29] 118th Congress (2023-2025), H.R. 4763 - Financial Innovation and Technology for the 21st Century Act (introduced July 20, 2023), https://www.congress.gov/bill/118th-congress/house-bill/4763.
[30] SEC, *Administrative Proceeding Against Joe Loofbourrow*, Exchange Act Release No. 41631 (July 21, 1999), https://www.sec.gov/enforcement-litigation/administrative-proceedings/34-41631.
[31] New York Times, *S.E.C. Settles 4 Cases Offering 'Free Stock'* (July 23, 1999), https://www.nytimes.com/1999/07/23/business/sec-settles-4-cases-offering-free-stock.html.

Understandably, the Commission's initial reaction to airdrops and incentive-based reward programs was to view them as posing similar risk as the "Free Stock" cases of the 1990s—these distribution mechanisms can certainly be structured in a manner that subjects investors to similar risks. However, they can also be structured to mitigate the risks the "Free Stock" cases exemplified. The conditions described above help to do so. However, once a DevCo disseminates network tokens via an airdrop the value of its asset may be highly volatile in response to increased demand, giving insiders (including officers, directors, employees, investors, and advisors) the potential opportunity to sell into the market before the value of that network token becomes seasoned and is effectively stabilized by the market.

To guard against such risk, transfer restrictions should be a condition of the safe harbor. Transfer restrictions, or "lockups," prevent holders from selling for a predetermined amount of time. In essence, insiders agree for a given period not to sell, contract to sell, or otherwise transfer or dispose of any crypto asset that it holds. A sufficiently long token lockup (such as the holding periods specified under Rule 144 and Regulation S, one year) can ensure that insiders are effectively restricted from using any asymmetric information and capitalizing on the volatility that may come with an airdrop, thereby protecting consumers and investors. During this restriction window, the network may mature and become decentralized. Once the transfer restrictions have expired, the network token will be more seasoned and its price more effectively stabilized by market forces.

For transfer restrictions to be effective, they must be robust, eliminating the possibility of insiders exploiting asymmetric information by other means. For example, insiders should be restricted from selling crypto assets they receive in any airdrop, as otherwise DevCos could structure further airdrops to enrich insiders. However, the broad and equitable distribution requirements set forth above help to mitigate this risk. More generally, transfer restrictions must be structured such that insiders cannot easily circumvent them.

For these reasons, only airdrops that include robust transfer restrictions for network tokens held by insiders should be eligible for the safe harbor under consideration.

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We greatly appreciate the opportunity to provide comments on these important matters, and we welcome engagement with the SEC on these issues.

Respectfully submitted,

Miles Jennings, General Counsel
a16z crypto

Jai Ramaswamy, Chief Legal Officer
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Scott Walker, Chief Compliance Officer
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