August 8, 2022

VIA ONLINE SUBMISSION

Re: Comments of Engine Advocacy Regarding *Ensuring Responsible Development of Digital Assets*.

Engine is a non-profit technology policy, research, and advocacy organization that bridges the gap between policymakers and startups. Engine works with the government and a community of thousands of high-technology, growth-oriented startups across the nation to support the development of technology entrepreneurship through economic research, policy analysis, and advocacy on local and national issues. We appreciate the opportunity to submit this response to the Department of Treasury. Startups are major drivers of innovation and emerging technology, and they make valuable contributions to economic and job growth and U.S competitiveness.[1]

Earlier this year, President Joe Biden released an executive order on Ensuring Responsible Development of Digital Assets to help propel the U.S. into the future global financial system. The administration's push to maintain leadership in the digital currency landscape while also protecting consumers and businesses is commendable. While critics dismiss the digital assets space, falsely claiming that use of digital assets is limited to illegal activity, digital assets have become a legitimate tool for companies to raise capital and build their user base.

Engine is a staunch advocate for creating a regulatory framework that encourages startups to employ digital assets and spur innovation. The current uncertainty regarding how to distribute digital assets to investors and users in a manner consistent with federal law has plagued businesses within the industry. Subsequently, startups and small businesses have substantial obstacles in their path towards successfully integrating digital assets into their business model. Given the rapid growth of digital assets and the variety of companies and users in the ecosystem, regulators need to update rules to account for the complexity of the industry.

**Adoption to Date and Mass Adoption**: What developments in technology, products, services, or markets account for the current adoption of digital assets? Are there specific statutory, technology, or infrastructural developments that would facilitate further adoption?

[1] *See, e.g.*, *The Economic Impact of High-Growth Startups*, Kauffman Foundation (June 7, 2016) https://www.kauffman.org/wp-content/uploads/2019/12/PD_HighGrowth060716.pdf.

## I. Startups need clearly defined regulations for utilizing digital assets in order to further improve expansion.

The rapid growth of digital assets and the variety of startups involved in the ecosystem has expanded, making it a $3 trillion industry[2] with hundreds of uses. This growth has incentivized startups to build their businesses utilizing various digital assets such as utility tokens, stablecoins, and cryptocurrencies. In order to sustain growth, policymakers must implement a clear regulatory framework to support mass adoption, increased economic expansion, and innovation.

The ongoing questions about whether digital assets are classified as securities has caused confusion and trepidation around investing in and utilization of digital assets. Tokens have varying applications, so policymakers must take a multi-pronged approach to determine how different kinds of digital assets should be regulated. Under the Howey Test, many digital assets do not meet the elements of a security. Many tokens, although an investment of money, are not accrued from the efforts of others but rather from the cryptocurrencies' usefulness on the network.[3] Efforts to regulate all digital assets as securities are ill advised, since many fall outside the scope of what securities laws were intended to monitor and are unlikely to cause the kinds of harms that securities laws aim to mitigate. Early-stage startups often need to distribute their tokens widely in order to build a functioning network, getting tokens in the hands of users to build up network effects and raising funds to scale their products. Without regulatory clarity, startups and users may be forced out of the sector for fear of the higher regulatory burdens under securities law and the consequences pertaining to illegal securities offerings.

The lack of clear regulation has been most noticeably damaging in the *SEC v. Coinbase* litigation. Presently, the SEC is pursuing litigation against Coinbase for nine specific digital assets that the agency claims should be considered securities.[4] This case comes after the SEC also charged Ripple and two of its founders with earning $1.3 billion in an unregistered securities offering.[5] Creating a regulatory framework through enforcement actions instead of creating clear rules will discourage startups seeking to enter the digital assets space.

Unclear reporting requirements also hinder mass adoption of digital assets as they make it more difficult for consumers—who drive innovation in the market through continued usage—to participate in the space. Proposals like the Virtual Currency Tax Fairness Act, which would exclude

[2] Joanna Ossinger, T*he World's Cryptocurrency Is Now Worth More Than $3 Trillion,* (Nov. 8 2021), https://time.com/6115300/cryptocurrency-value-3-trillion/

[3] Letter from Engine to Senator Patrick Toomey on the need for regulatory clarity in the cryptocurrency market. (September 27, 2022) https://static1.squarespace.com/static/571681753c44d835a440c8b5/t/615625bc6fcf166cf2889fd3/1633035708837/Engine+Crypto+Letter+to+Sen+Banking+Committee.pdf

[4] Faryar Shirzard, *The Crypto Securities Market Is Going To Be Unlocked But First We Need Workable Rules*, (July 21, 2022), https://blog.coinbase.com/the-crypto-securities-market-is-waiting-to-be-unlocked-but-first-we-need-workable-rules-c0ba63eabab3

[5] SEC Press Release, *SEC Charges Ripple and Two Executives with Conducting $1.3 billion Unregistered Securities Offering*, (Dec. 20, 2020) https://www.sec.gov/news/press-release/2020-338

up to $200 of gains from gross income for tax reporting purposes, would ease reporting burdens for consumers and help advance mass adoption.

While regulators sort out these policy questions, sandboxes provide a solution for startups who can benefit from a learning environment to get their products and services off the ground without the looming threat of regulatory action hanging over them. Policymakers should consider creating regulatory sandboxes, and they have several potential models to look to, including in the European Union and several states. By offering businesses an opportunity to dialogue with policymakers, startups in their early stages would be better equipped to navigate regulatory challenges and avoid enforcement actions.

**<u>Opportunities for Consumers, Investors, and Businesses</u>**: What are the main opportunities for consumers, investors, and businesses from digital assets? For all opportunities described, please provide data and specific use cases to date (if any). In your responses, please consider the Creation of new types of financial products and contracts.

## II. Startups are creating innovative ways to use digital assets and need regulatory clarity to continue doing so.

Startups are able to use digital assets in order to access capital and build their business model. And other small businesses can benefit from using digital assets to engage in things like low-cost cross-border transfers and managing payments in real-time.[6] As described above, policymakers should pursue changes that make it easier for businesses to participate in the digital asset market, both as issuers and as users.

Clear rules would improve the adoption and uses for digital assets and improve opportunities for domestic innovation. Storj is an Atlanta-based decentralized cloud storage provider that utilizes its own digital token to encourage users to share storage space on their devices.[7] "Most people have spare room on their disk drives—as many as 90% of all drives are severely underutilized. With Storj, they can rent out the unused space and get compensated with a digital token," Storj CEO Ben Golub explained. According to Golub, policymakers need to "consider the broader global regulatory landscape" when writing rules of the road. "Doing so will help policymakers protect American consumers, bolster U.S. competitiveness, and ensure that the U.S. remains the best place to start a company."

Another startup in Engine's network, Miami-based CitiQuants, leverages cities' data and has created a tokenized stock that allows cities to sell traded tokens on an exchange. "This is similar to how cities sell municipal bonds to fund their services," CitiQuants CEO Philip Peters explained.[8] "This model allows cities, for the first time, to capitalize themselves and increase public investments

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[6] Shai Bernstein and Christian Catalini. How Digital Currencies Can Help Small Businesses, (May 25, 2022) https://hbr.org/2022/05/how-digital-currencies-can-help-small-businesses

[7] *#StartupsEverywhere profile: Ben Golub, Founder and CEO, Storj*, Engine (October 8, 2021), https://www.engine.is/news/startupseverywhere-atlanta-ga-storj

[8] *#StartupsEverywhere profile: Philip Peters, Founder and CEO, CitiQuants,* Engine (October 9, 2020), https://www.engine.is/news/startupseverywhere-miami-fla-citiquants

by using tokenized equity." Peters encouraged policymakers to "embrace and accelerate decentralized blockchain policy" to remain competitive globally. "The U.S. is lagging behind, and other countries are way ahead of us," he said.

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Thank you for the opportunity to provide feedback to the Department of Treasury on needed clarity for digital assets. While we are excited to see interest in addressing critical gaps in this regulatory space, we implore regulators to be mindful of any affects legislative and regulatory efforts may have on startups in the industry. As always, we are happy to serve as a resource, including through providing feedback on any proposals through the lens of the startup perspective, or by facilitating conversations with startups themselves.