

Public Security Opinion

Hello,

I appreciate the opportunity that Hester Pierce presented to the public in her “There Must Be Some Way Out of Here” publication. I took the time to review this and other publications in an attempt to understand the issues at hand and see if current real world processes and purchasing rights can overlap into the questions laid out in crypto. There is no question that Real World Assets (RWA) are quickly becoming normalized and widespread. There is still very little clarification and process on how these real world assets can be titled, held, and sold using digital asset representation without breaking current security laws.

I am hoping the attached document can help drive the conversation in creating distinction between current regulatory issues surrounding digital assets backed by RWAs both fractionalized and not, and how these digital assets represent ownership with the rights to equity and returns.

The suggestion that I am making is based on the idea that the ability for an owner of a RWA backed digital asset to vote on the undeniably significant tasks, decentralization of personally owned RWA backed digital assets, and having an available secondary community driven marketplace all play an important role in determining the factors that make a RWA backed digital asset a security or not. While this is based towards RWA backed digital assets I do believe that defining and clearing up what is considered an enterprise or complex scheme could help other non RWA projects.

Thank you,
Zack Dane

Disclosure: *The following is my personal opinion on what could help answer the security question of Real World Asset (RWA) backed digital assets. The information in this document is based on the statements labeled “There Must Be Some Way Out of Here” written and presented by commissioner Hester Peirce and the Framework for “Investment Contract” Analysis of Digital Assets. I am not an attorney or a legal scholar but merely a member of the public with extensive knowledge and experience in real estate, automotive, and financial services industries. Everything written below is based on documentation that was provided to the public from the SEC on this subject and my personal experience in regulation in the previously mentioned fields.*

Questions from: There must be some way out of here

Below are a few answers to the questions presented by commissioner Pierce.

5. Should the security status of certain categories... Yes. These categories, I believe, will help the most with Web3 adoption from Web2 users. They could also hold the key to many of the regulations for other non-stable coin projects because they are so close to real world assets and rules that already exist. This could be the easier bridge to gap at first.

8. Should the Commission develop tailored disclosure....Yes. I believe that a distinction between a RWA backed asset vs a speculative or enterprise driven asset should have separate disclosures. The disclosure process should be far less intensive for RWAs that are easily verifiable through county records or other publicly available data sources. If the RWA backed offerings are leveraged then an extra level of disclosure should be required regarding the loan, the terms, and who responsible for the final obligation.

9. Does Regulation A under the Securities Act... Yes it is imperative. Based on my opinion and our attorney's. The Reg A/A+ exemptions should be much more widely available and less of a fight in order to obtain. Definitely require more disclosures than a Reg CF but don't make it overly expensive and difficult to navigate.

Can we use any of the following information to help clarify:

- How can we update local and county records using their current outdated processes and our new technology?
- How do we utilize the current real world recording and titling process to help the consumer verify the ownership of the titled RWA that the entity represents?
- Would the commission consider an exception when dealing with unleveraged single asset entities (LLC or similar) as a vehicle for transferring titled RWA ownership through digital assets?
- Can we clarify how much involvement needs to happen by a group, or DAO, to meet or exceed the necessary tasks required to answer the "efforts of others" argument in regard to RWA backed digital assets?
- Can this layout help define what broker-dealer thresholds would look like? Pooled entities vs individual RWA entities, fractionally owned or not?
- Could this type of ownership registration transfer help layout groundwork for DAO owned business?
- By using digital representations of ownership, fractionalized or not, in unleveraged single asset entities, could we help create a verifiable asset titling process (real world and on chain) that can be used by digital lenders to verify the current ownership status of the underlying RWA?

Could there be various classes of digital assets that require some form of initial and/or continuing documentation filing? Regarding RWA backed digital assets and the self custodial ownership of them, could it be broken up into 4 categories:

- Titled Personal - Individually owned RWAs that require titling at the local and/or state level (real estate, vehicle, boat, etc..)
- Titled Fractional - Fractional ownership that uses a managing member or AP to be the registered agent and carry out the tasks voted on by the group or DAO.
- Non-titled Personal - Physical assets that don't require registration, owned by a single person
- Non-titled Fractional - Physical assets that don't require registration, owned and managed by a DAO or group

Titled RWAs should be placed into pass through legal entities to:

- Shield owners, fractional or whole, from liability,
- Create another level of ownership verification to protect consumers,
- Easier to change the registered agent when a digital asset transfers then retitling the asset

Is the fractionalized sale of this legal entity to the general public using a digital token as representation of ownership rights considered a security? And if so what does registration of individual RWAs and their digital representations of ownership look like?

Would the sale of a digital asset representing the ownership and rights of a single asset entity, fractionalized or not, from peer-to-peer be a security?

Non-Titled RWAs should be physically verified and certified by 3rd party registries:

- Collectables or things that need to be verified as authentic or one of a kind
- Open registries are becoming more available to help curb fraud

Outline of potential talking points that, I believe, could help draw a line on how we can allow people to list, buy and sell whole and fractional RWAs without being considered a security:

- Using single asset entities (LLC or similar) for titled RWAs to create a verifiable real world entity to help with customer protection,
- Defining "routine tasks" to better clarify the depth of involvement required by the surrounding community, DAO, in order to determine if the "Reliance of others" prong of the Howie test can be clarified with regard to digital ownership of RWAs, fractional or not,
- Create a SEC approved digital single asset entity submission process outlining the details of the RWA, the issuing and original AP or Managing Member, its legal filings

(LLC or similar), and any additional information that connects the ownership of the RWA, the legal entity it rests in, and the digital representations of its ownership.

- Digital assets that are backed by real world assets (RWAs) whose ownership is leveraged with a loan, lien, or other financial obligation are still subject to interpretation as they create a complex and/or undeniably significant task in the success of the enterprise,
- Selling NFTs or other digital forms of fractionalized RWA ownership may not be a security upon initial sale or on a secondary marketplace, if:
 - There is no loan, lien or financial obligation on the underlying RWA or its legal entity,
 - The managerial efforts, decisions, which affect the failure or success of the enterprise are made by the owner or fractional owners after initial customer purchase,
 - A fully functioning marketplace for secondary sales and trading is available and operational before any tokens are sold, whole or fractionalized,
 - The marketplace host only provides, makes comments on, current and past historical data and market trends. The host does not provide or advertise speculative investment advice.
 - A set number of digital assets need to be registered on a publicly accessible blockchain network to verify its authenticity and ownership record. Any attempts to alter the fixed number of ownership fractions after the first one has been minted will result in becoming a security as share of ownership and valuations have been altered, changed, as a direct result the customer is financially affected.
 - The titled RWA backed digital asset must contain the information of the legal entity that directly owns the underlying asset in order to help verify its authenticity. Non-titled RWAs do not require government oversight and should be purchased with caution and due diligence from the buyer. No different than buying on eBay.
 - Any member of the ownership group can perform the tasks, or easily hire readily available contractors, required to maintain the entity and underlying asset.
Example: Property managers, realtors, and maintenance contractors are easily accessible via the internet to anyone. Qualifying for financing is not.
 - Income from the sale of the digital asset does not go towards the enhancement of the RWA or the real world legal entity surrounding it,
 - All tasks performed by the AP are predefined, listed in the operating agreement, and are limited to any action that is considered a “ministerial or routine task”,

- Any income derived from the renting or leasing of the RWA for its intended use, that is subject to distribution across all digital asset owners, is from activities that are determined when the asset is placed into commission. Any income that is derived from anything other than its predetermined use, could create questions that are still subject to interpretation as they create a complex and/or undeniably significant task in the success of the enterprise,
- The RWA may have an ownership life that is predetermined before the asset is placed into commission. *Example: This asset will be sold at the 10 year mark if the current owner(s) don't vote to sell before then.*

Reliance on the efforts of others

Deciding which tasks are routine.

One of the arguments set forth by crypto and the *Howie Test* has been, are you relying on the efforts of a 3rd party? Recently this has been brought into question because of the idea that a DAO alone would be able to answer that. One such case, *SEC v. Koscot Interplanetary, Inc.*, 497 F.2d 473, 483 n.15 (5th Cir. 1974), gave use the ruling that: If the AP provides efforts that are "*the undeniably significant ones, those essential managerial efforts which affect the failure or success of the enterprise,*" and the AP is not merely performing ministerial or routine tasks, then there likely is an investment contract.

This decision allows us to now consider the meaning of these "ministerial or routine tasks" and how they can clear the definition of a security or not when looking at RWA backed digital assets.

Webster Dictionary defines the term routine as a "habitual or mechanical performance of an established procedure". This definition helps determine what a "routine task" could be defined as. According to "Framework for "Investment Contract" Analysis of Digital Assets" one of the test points listed under "Reliance on the efforts of others" brings into question:

- Are those efforts "*the undeniably significant ones, those essential managerial efforts which affect the failure or success of the enterprise,*"[\[14\]](#) as opposed to efforts that are more ministerial in nature?

There will always have to be someone at the wheel. When dealing with RWAs, a level of real world responsibility will need to be maintained in order to upkeep the asset. These definitions can be based on the "generally agreed upon tasks" required to conduct the operations, determined by the field or industry that the asset is part of.

Can anyone in the group take over the responsibilities with little skill and readily available information? If this responsibility can be passed to other members, through a simple majority vote, the menial or "ministerial or routine tasks" or the basic duties that are required to manage a RWA, and they are willing to accept the fiduciary responsibilities, and legal repercussions that may stem from being the AP, then there is no reason it should be a security.

In order to achieve a level of self custodial decentralization for an organization or entity then someone has to be able to come and do the job on behalf of everyone. Without someone at the wheel, the project will crash and the asset will be worthless.

But if the general operations surrounding the basic upkeep requires extensive knowledge and expertise to conduct, then it may be considered an “enterprise” and could be considered a security. The question is, can anyone do this with reasonable knowledge and easily obtainable services? If there is a loan, lien, or other financial obligation that the AP is responsible to pay for or take care of and failure to do so results in the asset defaulting then that becomes a financial decision on behalf of the group and would be considered a task that is “the undeniably significant ones, those essential managerial efforts which affect the failure or success of the enterprise.”

Example: Property managers have generally agreed upon tasks to perform and fiduciary responsibilities to uphold based on established industry functions. Before services are commenced, a management agreement is signed outlining the predetermined procedures that they will conduct on behalf of the owner(s). Some of these tasks include:

- General administrative activities of collecting rent, posting legal notices, and maintaining document records,
- Listing and showing the property to prospective lessors / renters
- Giving showing and property condition updates to owners
- Coordinating maintenance and providing past and current performance data

Additional tasks that can be considered “undeniably significant” are anything that have to do with financial decisions or the creation of other monetary obligations beyond what is required to maintain or upkeep the asset. Some of these “undeniably significant” tasks include:

- Moving forward with an eviction,
- Deciding to raise rent, re-rent or sell the home on behalf of the owners or investors,
- Major remodels or renovations that increase the value of the asset,
- Financial decisions that would result in a loan, lien, or other financial obligation.

The decision making authority by the property management company or asset manager or AP, on behalf of the entity, extends only to the decisions that are pre-approved and/or that require action in order to protect and/or maintain the value and functionality of the asset held within the entity, fractionalized or not. All other activities that are considered to be “efforts that are ‘the undeniably significant ones, those essential managerial efforts which affect the failure or success of the enterprise,’ are voted on by the group or DAO and carried out by the current AP or managing member.

Define - RWA backed digital asset vs Enterprise backed digital asset

Titled RWA backed digital assets can be held in a pass-through entity to help shield the owner from potential lawsuits and various other issues. RWAs need to be titled in the real world using regulations and procedures set forth by the local and state governments. Digitally titling ownership interests of RWAs will simply be an additional step in the purchase process that will

provide people with the ability to buy and sell their ownership anywhere, anytime, while recording their transaction for public record.

What I am challenging is that there is a difference between a legal entity hosting an asset that requires basic upkeep, and a complex enterprise or scheme that requires advanced decision making to maintain or grow its value.

If the entity is owned out right, the amount of work required to maintain its upkeep is easily definable. If the AP or Managing Member makes major financial decisions on the asset or decides to sell the asset on behalf of the group, they then become an investment advisor and are potentially violating securities laws.