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Via Electronic Submission

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

Dear Commissioner Peirce and Members of the SEC Crypto Task Force:

Re: Response to RFI of Crypto Task Force

The Lido Labs Foundation appreciates the opportunity to engage with the Securities and Exchange Commission’s Crypto Task Force. The Lido Labs Foundation is an independent foundation adjacent to Lido DAO (described below), that provides services to the Lido DAO in regards to the Lido liquid staking protocol.

We set forth below responses to the statement by Commissioner Hester Peirce titled “There Must Be Some Way Out of Here” (released on February 21, 2025), which posed questions concerning statutes and rules that may present challenges to firms seeking to innovate with crypto assets and blockchain technology. This letter serves as a high-level overview responding to two such questions from the perspective of Lido DAO and is designed to form the basis for further conversation. If a more detailed memorandum or a discussion would be helpful to the Crypto Task Force’s mission in making rapid progress to alleviate the legal imprecision and commercial impracticality of the current digital asset regulatory environment, we would welcome the opportunity to either provide additional material for your consideration or schedule a meeting.

Lido DAO is a decentralized autonomous organization that governs the Lido liquid staking protocol (the “Lido Protocol”). The Lido Protocol is comprised of smart contracts which enable users to participate in the security and consensus mechanisms of the Ethereum blockchain. In particular, the Lido Protocol allows a user to “stake” their digital assets upon which the user receives a liquid staking token as a form of receipt for that digital asset that can be freely transferred, traded, or redeemed for the user’s staked digital assets and accrued staking rewards. This process – known as “liquid staking” – is described in more detail below.

Two of the questions posed by Commissioner Peirce concern crypto assets used in functions inherent to the operation of blockchain networks and the status of liquid staking tokens (“LSTs”) under the federal securities laws. This letter addresses (1) the critical functionality of governance tokens to the operation of certain blockchain networks and (2) the appropriate characterization of liquid staking tokens that constitute receipts redeemable for a commodity. We believe that

neither of these types of digital assets implicate the federal securities laws. Please note that we include the questions posed below in italics for your convenience, along with our responses.

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(3) Certain crypto assets are used in a variety of functions inherent to the operation of a blockchain network, such as mining or staking as part of a consensus mechanism or securing the network, validating transactions or other related activities on the network, and paying transaction or other fees on the network. These technology functions may be conducted directly or indirectly, such as through third-party service providers. What types of technology functions are inherent to the operation of a blockchain network? Should the Commission address the status of technology functions under the federal securities laws and, if so, what issues should be addressed?

Background on Blockchain Governance and Governance Tokens

Governance tokens provide a functionality inherent to the operation of certain decentralized blockchain networks. The core promise of blockchain technology is that of decentralization, or distributed ownership and control over public goods on the internet. Historically, decentralization has cost more, produced less, moved slower, and added complexity and redundancy, because technologies to coordinate at scale have not existed. With the introduction of digital assets that provide the holder the direct ability to vote onchain with respect to governance proposals, that paradigm has shifted: governance tokens allow for the empowerment of individuals as part of broad communities, in lieu of enterprises. This enables the creation of decentralized public infrastructure whose maintenance is not dependent on centralized interests.

Many blockchain networks seeking to achieve such decentralization rely on governance tokens to provide community members with programmable, immutable, and verifiable control over the wide variety of goods and services now available on blockchain technologies. While certain prominent blockchains such as Bitcoin and Ethereum rely primarily on offchain governance processes, governance tokens that directly imbue holders with onchain authority over a protocol are an important innovation that allows blockchain projects to rethink established corporate organizational concepts.

A protocol may require a community onchain vote of governance token holders on key parameters such as setting applicable fees and selecting grant recipients to build new protocol features or updates. These types of decisions are well-suited to a decentralized, deliberative process that allows for sufficient time to build consensus as well as the transparency afforded by onchain vote. The onchain votes are directly controlled by software code which can be examined and audited as a part of the deliberation process.

Lido DAO is an example of a decentralized organization that is controlled by holders of its governance token, LDO. Anyone can purchase LDO and thereby participate in Lido DAO. The LDO governance token enables holders to vote on key parameters, upgrade of the Lido Protocol, and operations related to DAO-controlled matters such as governance mechanisms and treasury.

Governance tokens derive their value from their essential utility which allows for distributed community control over a blockchain network and should not be classified as securities.

Fundamentally governance token's value is derived from their utility and the efforts of a diffuse and fluid community rather than an identifiable enterprise. Although many governance tokens are freely tradable and thus can accrue value, the law has long recognized that value accrual that is attributable to the broader marketplace is not recognized under the *Howey* test as sufficient to find the asset to be a security. *SEC v. Belmont Reid & Co.*, 794 F.2d 1388 (9th Cir. 1986). Moreover, the mere potential for speculation on an asset as part of a profit-seeking venture does not render that asset a security. For example, there is a thriving secondary market for season tickets and season ticket licenses to professional sports events – some of which markets are endorsed and facilitated by the issuers of the tickets themselves – yet the Commission has issued no-action letters to ticket issuers such as LA Fan Club, Inc., premised on the principle set forth in *United Housing Foundation, Inc. v. Forman*, 421 U.S. 837 (1975) that assets offered for their actual utility (in this case as season tickets to the sporting event) fall outside the ambit of the securities laws. LA Fan Club, Inc., SEC No-Action Letter (May 19, 2017).

We believe that the same result is appropriate for governance tokens: the crucial utility they provide to the operation of decentralized blockchain networks should be recognized first and foremost, and without other indicia of securities characteristics, transactions in such assets should fall outside the purview of the securities laws.

Aspects of this principle were echoed in the Commission's recent "Staff Statement on Meme Coins" (released on February 27, 2025) which noted that the offer and sale of a meme coin does not constitute an investment contract because the promoter of a meme coin does not promise to pool sale proceeds to develop the coin or a related enterprise, and any expectation of profits derives from factors outside of the promoter's control. Governance tokens fit a similar mold. No investment contract is formed between the purchaser of a governance token and its issuer because the tokenholder's role is an active one as a governance participant, and there is no investment promise made by the issuer. Any expectation of profits derives from the efforts of the governance tokenholders themselves and their control over the enterprise.

Of course, the Commission caveated its statement on meme coins by noting that under the federal securities laws, offers and sales of digital assets labeled as meme coins will be evaluated based on the economic realities of the particular transaction. Similarly, the facts and circumstances surrounding any particular digital asset labeled by its issuer as a "governance token" could result in transactions thereof being characterized as the offer and sale of a security. This evaluation of the economic realities based on the "flexible principle" of *Howey* adaptable to the "countless and variable schemes devised by those who seek the use of the money of others on the promise of profits" should not detract from the Commission affording legitimate governance tokens status as non-securities. *SEC v. W.J. Howey Co.*, 328 U.S. 293 (1946).

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4. Users of liquid staking applications receive a so-called "liquid staking token." This token represents their staked crypto asset, and the token can be used in other activities, all while continuing to participate in the proof-of-stake protocol. Should the Commission address the

status of liquid staking tokens under the federal securities laws, and, if so, what issues should it address?

As we outline below, we believe there are clear reasons why an LST does not constitute or involve a “security” for purposes of the U.S. federal securities laws. With that said, we believe action by the Commission to address the status of LSTs would provide welcome additional clarity and legal certainty to the market.

Background on Liquid Staking Protocols and LSTs

Unlike proof of work networks like Bitcoin, proof of stake networks, such as Ethereum, rely on network participants “staking” crypto assets in order to participate in the security and consensus mechanism of the network via validator nodes. Validators earn rewards for such participation, but their staked crypto assets are subject to the risk of minor penalties in case network-assigned duties are not performed correctly and timely, and larger “slashing” in the case of potential validator misbehavior. Depending on the specific proof of stake network in question, there is typically a minimum required stake in order to activate a validator and withdrawal of crypto assets from staking may be subject to an “unbonding” period. For example, in the case of the Ethereum network, a minimum of 32 ETH are required to activate a validator.

Liquid staking protocols and LSTs reflect an important innovation allowing users to contribute to the security and consensus mechanism of such proof of stake networks while maintaining liquidity, control, and evidence of ownership of their staked crypto assets. With liquid staking, users can stake their crypto assets through a decentralized liquid staking protocol or staking service provider without needing to meet validator required minimum staking amounts, and without tying up the value of their crypto asset. Users receive an LST evidencing, and redeemable for, their staked crypto assets. Such LSTs are freely transferable and can be utilized in other decentralized applications, thus facilitating transferability of value that is not present when staking by directly operating a validator node.

The LST represents the user interaction with smart contract software dedicated to routing ETH to node operators for the purpose of staking. Unlike traditional ETH staking, which requires 32 ETH minimum staking amount, liquid staking allows users to stake an arbitrary amount of ETH and receive LST to represent their staked ETH. The ETH is routed by software to node operators who run validators. The ETH is directed to the same smart contract on Ethereum’s Execution Layer in order for it to be registered and mapped to validators.

Although different liquid staking models for Ethereum have evolved, they can be generally categorized into two categories:

- *Decentralized Liquid Staking.* Decentralized liquid staking solution separates the software from the underlying validation activity. The software functions as neutral middleware, governing the operations conducted on ETH routed through it. The participating node operators have no direct say in the parameters or operations of the onchain software. The software itself separates the validation activity from the user. The Lido Protocol is an example of decentralized middleware software.

- *Centralized Liquid Staking (i.e., Staking Service Provider)*. Centralized liquid staking is typically operated by the underlying centralized node operators, who perform validation activities.

In both categories, the ETH is routed by software to node operators to stake ETH on the Ethereum network.

LSTs can be redeemed for underlying ETH (plus accrued staking rewards) with the liquid staking protocol. The LSTs typically have one of two sources of redemption price in this direct or primary model as follows:

1. *Dynamic or “Rebasing” LSTs*. Under this method, users receive additional LSTs (or the base amount of LSTs held by users is adjusted or “rebased”) as staking rewards accrue over time. The exchange rate at which each unit of the LST token can be redeemed for the relevant staked crypto asset thus remains constant. All of this is performed by software on the liquid staking protocol. An example includes Lido’s stETH liquid staking. The Lido Protocol rebases stETH daily.
2. *Static or Non-Rebasing LSTs*. Under this method, users receive a fixed amount of LST upon supplying the relevant crypto asset to the liquid staking protocol. The amount of LST held by the user remains constant over time, but the exchange rate at which it can be redeemed for the relevant crypto asset increases to account for staking rewards accruing over time. All of this is performed by software on the liquid staking protocol. An example includes Lido’s wstETH liquid staking.

Importantly, under both models the LST trades in secondary markets at prices primarily determined by and highly correlated with the value of the underlying asset and accrued rewards that it represents (i.e., for which it is redeemable). Moreover, any deviation in price between the LST and the underlying asset is attributable to the additional functionality of the LST that allows it to be transferred or, loaned, and therefore any expectation of profits is tied to a liquidity premium established by the market based on the features and function of the liquid staking protocol rather than any efforts of an issuer

An LST is a receipt token akin to a warehouse receipt or certificate in respect of a physical commodity. Where a receipt or certificate is redeemable for an asset that is a commodity and not a security, the receipt or certificate is also not a security.

Once the nature and operation of liquid staking protocols and LSTs is properly understood, it becomes clear that LSTs are simply a form of on-chain receipt or document of title redeemable for users’ staked crypto assets. Where the relevant crypto asset being staked is a commodity, it is also then clear that the issuance of the LST as a receipt token redeemable for a commodity does not implicate security status or the US federal securities laws.

It is well established that the issuance of warehouse receipts, certificates, or other documents of title representing ownership of underlying goods or commodities do not constitute the issuance of a “security” or thereby subject the issuer to registration under the Securities Act. For example, the decision in *Noa v. Key Futures*, 638 F.2d 77 (9th Cir. 1980) and the Commission’s gold bullion warehouse receipt no-action letters make clear that warehouse receipts or

certificates for precious metal commodities, like gold or silver bullion, do not implicate an offering or sale of securities. Similarly, warehouse receipts and shipping certificates have long formed part of the markets for agricultural commodities (e.g., representing title to grain in a silo or warehouse) and energy commodities (e.g., representing entitlements to physical barrels of oil at a storage facility), and carbon credits, which are commodities, are tradable certificates that represent the right to emit one metric ton of carbon dioxide or an equivalent amount of another greenhouse gas.

While novel in technological form, that LSTs are properly understood as receipt terms akin to warehouse receipts is demonstrated by a number of factors, including that (i) LSTs represent and are redeemable for an identified amount of actual staked crypto assets in the liquid staking protocol; (ii) the secondary market trading price of LSTs is closely aligned and highly correlated with the relevant staked crypto asset and the value of accrued rewards; and (iii) LSTs are not acquired on margin, do not provide any embedded leverage, and do not represent a form of synthetic or derivative exposure to the staked crypto asset.

Even if analyzed separately to the relevant crypto asset being staked, LSTs do not constitute a “security” under a Howey analysis

We also believe that an LST does not constitute a “security” even if evaluated under a *Howey* analysis separately from the relevant crypto asset being staked. While not exhaustive, these reasons include:

- There is no expectation of profit on the part of the LST holder beyond the value of the underlying commodity and the rewards earned through the staking of such commodity.
- LST holders are not reliant on any essential or significant managerial efforts of any “other.” The staking rewards are payable by the relevant underlying blockchain network for the efforts of the LST holder – namely, for the staking of their digital assets in contribution to the security and consensus mechanism of the network.
- The role of the liquid staking protocol represents a technical or ministerial function, with the software required to run a validator and participate in staking directly freely available and generally open source.

While we believe these reasons are clear and readily apparent, action by the Commission to address and provide legal certainty as to the application of the U.S. federal securities laws to LSTs would be welcomed by the market given the breadth with which the *Howey* test has been applied to digital assets in recent years (including with respect to the distinct question of custodial staking as a service offerings).

Respectfully submitted,

Sam Kim

Sam Kim
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