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Regulatory Alert

Regulatory Insights for Financial Services

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Regulation Crypto Assets: SEC Proposed Rules

KPMG Regulatory Insights

- *Clarification: Explains that the "security" at issue is the covered investment contract rather than the underlying crypto asset itself; clarifies also when a covered investment contract ceases to exist and becomes subject to the proposed safe harbor.*
- *Fit-for-Purpose: Establishes an offering framework specifically tailored to covered investment contracts involving crypto assets which may reduce compliance costs for issuers and potential delays related to regulatory uncertainty.*
- *Regulatory Runway: Extended duration (four years) of the startup exemption is intended to "provide issuers with a regulatory runway during which they could attempt to fulfill their representations or promises to engage in essential managerial efforts under covered investment contracts" while ensuring that investors remain sufficiently protected and informed.*
- *State Preemption: Preemption of state securities law registration and qualification requirements proposed for covered investment contracts offered under the Regulatory Crypto Asset exemptions, including certain secondary market transactions.*
- *Market Structure: The SEC continues to support Congressional efforts to codify a comprehensive market structure framework (e.g., the CLARITY Act); changes to the proposal are possible should legislation pass this year. The CFTC has also stated that it will "move swiftly" to establish rules for the cryptocurrency market if legislation does not pass.*

The Securities and Exchange Commission (SEC or Commission) proposed new rules to be set forth in a new regulation, "Regulation Crypto Assets," to create a "tailored offering regime" for certain investment contracts involving crypto assets. The proposed rules are intended to facilitate capital formation within crypto asset markets while, at the same time, ensuring that investors are adequately protected and provided with the information needed to make informed investment decisions. Key provisions of the proposal include:

- Definition of terms
- Tailored disclosure requirements
- Registration exemptions for startups and fundraising
- Safe harbor for certain investment contracts
- Federal preemption of state securities law registration requirements

The proposed rules build on the Commission's March 2026 Interpretive Release, which clarifies how the federal securities laws apply to certain crypto assets and transactions involving crypto assets.

The Commission requests comments on the proposed rules no later than October 20, 2026.

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Definition of Terms

An objective of Regulation Crypto Assets is to establish a common vocabulary and framework for market participants. The SEC states that clear definitions are important given that crypto assets are a "relatively novel and highly technological asset class." Certain definitions, specifically those for "covered investment contract," "covered transaction," and "crypto asset" would be foundational to Regulation Crypto Assets.

Key proposed definitions include:

— **Associated crypto application:** The smart contract or similar executable software program that is deployed to an "associated crypto network" and within which such crypto asset may be used for the transmission or storage of value or for which the crypto asset facilitates access or participation.

— **Associated crypto network:** The blockchain or similar distributed ledger technology network on which such crypto asset is generated, minted, or mined; includes the particular network to which a crypto asset is "native" and on which records regarding ownership of and transactions in that crypto asset are recorded.

— **Covered investment contract:** A contract, transaction, or scheme that constitutes an investment contract, provided that the investment contract meets the following requirements:
  - A crypto asset is subject to the investment contract.
  - Such crypto asset is not a security.
  - No asset other than such crypto asset (including any security or non-security asset) is subject to the investment contract.

— **Covered transaction:** Used only in the context of a startup exemption (discussed below), would be defined as an offer, sale, or other distribution of a covered investment contract, including, but not limited to:
  - Any public or private offering, including a distribution, of a covered investment contract in one or a series of capital raising transactions.
  - Any public or private offering, including a distribution and transactions referred to as "airdrops,"(see Background below) of a covered investment contract in one or a series of transactions in exchange for, in recognition of, or as incentive for past or future use of an associated crypto network or associated crypto application, or as a reward or incentive for conducting activities primarily related to operating, governing, or securing an associated crypto network or associated crypto application.

— **Crypto asset:** Any digital representation of value that is recorded on a cryptographically-secured distributed ledger.

— **Subject crypto asset:** A crypto asset that is subject to a covered investment contract.

Tailored Disclosure Requirements

Issuers offering covered investment contracts would be subject to "principles-based" disclosure requirements intended to give issuers the flexibility to tailor disclosures to their particular facts and circumstances. In general, the information provided would be required to:

— Be presented in "clear, concise, and understandable language."

— Address the current stage of development of the issuer, the subject crypto asset, and the associated crypto network or associated crypto application, delineating any forward-looking or future plans of development.

— Be consistent with the issuer's public statements in its established public communication channels (e.g., its website or official social media accounts) and promotional materials (e.g., whitepapers) relating to material aspects of the issuer, the subject crypto asset, and the associated crypto network or associated crypto application.

Issuers would be subject to disclosure requirements covering non-financial, narrative information (referred to in the proposed regulation and related forms as Rule 103(b)), as appropriate, relating to material aspects of a covered investment contract, including:

Disclosure Requirements	Description
Covered investment contract	Terms of the covered investment contract, including the issuer's representations or promises to engage in essential managerial efforts under the covered investment contract
Offering	Terms of the offering
Subject crypto asset	Description of the name and the security, economics and allocations of the subject crypto asset
Management, related persons, and conflicts of interest	The issuer's management, related persons, and conflicts of interest
Associated crypto network/application; plan of development	The associated crypto network or associated crypto application and the issuer's plan of development, including progress made
Security; source code	The security of the subject crypto asset and the associated crypto network or associated crypto application, including architecture, network protocols and functionality
Subject crypto asset	Economics and allocations
Governance	The subject crypto asset's and associated crypto network's or associated crypto application's governance mechanisms, smart contract governance mechanisms, and permissions
Subject crypto asset ecosystem	The subject crypto asset's current and anticipated ecosystem
Risk factors	Factors that make an investment in the offering speculative or risky

Registration Exemptions for Startups and Fundraising

The SEC proposes two exemptions from the registration requirements of section 5 of the Securities Act of 1933 (see Background below) – the startup exemption and the fundraising exemption. Both exemptions would be available only for offers and sales of covered investment contracts, would be subject to the disclosure requirements detailed above (Rule 103(b)), and would remain subject to federal antifraud and antimanipulation provisions of the federal securities laws.

Startup Exemption: A one-time, non-exclusive exemption available to eligible issuers (e.g., an entity, an individual, or a group of individuals or entities (i.e., does not have to be a legal entity)) that would permit the issuer to offer up to $5 million in covered investment contracts over a four-year period.

Issuers utilizing the startup exemption would be required to publicly file a notice of reliance with the SEC on a new form titled "Form NOR" and to make periodic updates. No later than four years after filing Form NOR, issuers would be required to publicly file a new form titled "Form TR" to indicate when they have ceased relying on the startup exemption.

Fundraising Exemption: A two-tier, non-exclusive exemption available to eligible issuers (e.g., an entity organized in the U.S, 50 percent of officers/directors are U.S. citizens, not a development stage company), that would permit the issuer to offer and sell covered investment contracts (referred to as eligible securities) in a 12-month period.

Issuers relying on this exemption would be required to publicly file offering statements consisting of the same principles-based narrative disclosures as the startup exemption (Rule 103(b)), a discussion of the issuer's financial condition, and financial statements.

— **Tier 1:** Allows offerings of up to $20 million of covered investment contracts, including no more than $6 million offered by selling securityholders who are affiliates of the issuer.
— **Tier 2:** Allows offerings of up to $75 million of covered investment contracts, including no more than $22.5 million offered by selling securityholders who

are affiliates of the issuer. Required to provide audited financial statements.

Under the rule, the portion of the aggregate offering price attributable to securities of selling securityholders would not be permitted to exceed 30 percent of the aggregate offering price of a particular offering in (i) the issuer's first offering under this exemption or (ii) subsequent offerings under this exemption that are qualified within one year of the qualification date of the issuer's first offering. In addition, for purposes of the Tier 1 and Tier 2 offering limits, the amount of eligible securities sold by the issuer and the amount sold by its affiliates would be aggregated together.

No offer of securities may be made unless an offering statement has been filed with the Commission. Offering statements filed under Regulation Crypto Assets would utilize a new form, titled "Form 1- CRYPTO."

Issuers that have qualified Tier 1 or Tier 2 offerings under the fundraising exemption would be subject to ongoing periodic reporting requirements and would be required to file semiannual, annual, and current reports on proposed new forms, Form 1-SC, Form 1-KC, and Form 1-UC, respectively. Issuers would be required to publicly file Form TR to indicate when they have ceased relying on the fundraising exemption.

Investment Contract Safe Harbor

The investment contract safe harbor would provide that a covered investment contract will be deemed to have ceased to exist, and the crypto asset that was subject to the covered investment contract will be deemed not to constitute or represent or to be subject to such investment contract for purposes of the Securities Act and the Exchange Act, if certain conditions are satisfied.

An issuer of a covered investment contract would satisfy the investment contract safe harbor if it has met both of the following:

- Completed or otherwise permanently ceased all essential managerial efforts that it represented or promised it would engage in under the covered investment contract and is not making and does not intend to make any new representations or promises to engage in essential managerial efforts with respect to the underlying crypto asset.
- Made a public filing through Form TR certifying that it has satisfied the conditions of the safe harbor and provides an analysis supporting that certification.

The SEC retains the right to challenge whether the issuer has satisfied the safe harbor conditions.

The investment contract safe harbor would be available to any issuer that satisfies its conditions, including those that utilize the startup exemption or the fundraising exemption. The SEC notes, however, that even if an issuer has not satisfied the investment contract safe harbor, a crypto asset may nonetheless not be subject to an investment contract under the *Howey* test (see Background below).

Preemption of State Registration and Qualification Requirements

The SEC is proposing to add a new definition of "qualified purchaser" under section 18(b)(3) of the Securities Act, which would effectively preempt state securities law registration and qualification requirements with respect to offers and sales of covered investment contracts made pursuant to an exemption in Regulation Crypto Assets (i.e., the startup or fundraising exemption).

With respect to secondary market transactions by any person other than an issuer, underwriter, or dealer, the proposed amendments would preempt state securities law registration and qualification requirements for covered investment contracts, provided the issuer:

- Has satisfied the requirements of an exemption under Regulation Crypto Assets with respect to such covered investment contract.
- Remains subject to, and is current with respect to, such exemption's disclosure and filing requirements and/or periodic reporting obligations, as applicable.

For more information, please contact Laura Byerly or Stefan Cooper.

Background

Airdrops

The SEC's March 2026 Interpretive Release, defines "airdrop" as a means for crypto asset issuers to disseminate their crypto assets in exchange for no or nominal consideration. Issuers may airdrop a crypto asset by transferring its crypto asset to specific cryptographic wallets or other addresses.

Securities Act of 1933

The Securities Act of 1933 (the Securities Act) is the primary U.S. law that governs how securities are offered to investors and requires all offers and sales of securities to be registered with the SEC unless they qualify for specific statutory or regulatory exemptions.

Specifically, under section 5 of the Securities Act, it requires issuers to file a registration statement with the SEC and disclose detailed information to potential investors prior to selling the securities publicly. The Securities Act also provides exemptions that allow certain types of securities offerings to be exempt from the registration process based on the method of sale (i.e., exempt transactions) including Regulation A, Regulation D, and Regulation Crowdfunding.

Howey Test

Established by the Supreme Court in *SEC v. W.J. Howey Co.*, the "Howey test" is an analysis used to determine whether a transaction qualifies as an investment contract and falls within the purview of the federal securities law. Under the Howey test, an "investment contract" exists when there is the investment of money in a common enterprise with a reasonable expectation of profits to be derived from the efforts of others. Whether a particular digital asset at the time of its offer or sale satisfies the Howey test depends on the specific facts and circumstances. The Howey test applies to any contract, scheme, or transaction, regardless of whether it has any of the characteristics of typical securities. The focus of the Howey test is not only on the form and terms of the instrument but also on the surrounding circumstances and the manner in which it is offered, sold, or resold.

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