



# Advance Notice on Upcoming DAO Regulation

## ADVANCE NOTICE OF PROPOSED RULEMAKING (ANPRM) ON DECENTRALIZED AUTONOMOUS ORGANIZATIONS (DAO)

### CATAWBA DIGITAL ECONOMIC ZONE ZONE AUTHORITY COMMISSION June 1st 2022

The Catawba Indian Nation, through its General Council, has recently approved the creation of the [Catawba Digital Economic Zone](#) (CDEZ). The CDEZ is a special economic zone under the sovereignty of the Catawba Nation, built to service Web3 companies. It was [passed into law on February 19th](#) through the GEZ Civil Ordinance, which established a civil code for the CDEZ. The CDEZ features a best-in-class legal code, streamlined company registration platform, and an agile regulatory body, making it one of the most competitive jurisdictions for digital industries.

The CDEZ is governed by a Zone Authority, which is in charge of creating and enforcing regulations. As part of its duties as a regulatory authority, the Zone Authority may request information for upcoming regulations in the form of an **Advance Notice of Proposed Rulemaking (ANPRM)** pursuant to Section 303 of the CDEZ's Administrative Procedures Regulation.

An ANPRM is a preliminary notice stating that the Zone Authority is considering regulatory action before it develops a fully detailed proposed rule. It describes the general area that is subject to regulation and asks for public comment on the issues and alternatives being discussed. Below you can find the Zone Authority's ANPRM on a Decentralized Autonomous Organization (DAO) Regulation.

### **Purpose of the ANPRM**

The goal of this ANPRM is to solicit relevant information from the industry, existing DAOs, DAOs in formation, developers, practitioners, regulators, legal teams, web3 companies and blockchain users that may be relevant for drafting a DAO Regulation. The Zone Authority invites the public to comment on the issues discussed below.

### **Channels**

The Zone Authority accepts public comments through its Discord Server, website form and email. The relevant links and addresses can be found at the bottom of this ANPRM.



## 1. What is a DAO?

DAOs are blockchain-based, decentralized, distributed organizations, shaped more as a network than a traditional corporate hierarchy or pyramid. DAOs are organized via smart contracts. They are a way for parties with a mutual goal to coordinate, share resources, and distribute benefits. Even without traditional hierarchical structures, DAOs can provide democratic mechanisms of decision making. They also provide novel ways of structuring membership shares, voting rights, and contributions, compared to traditional organizations. DAOs can use tokens to vote, incentivize and pay members, among many other activities normally performed by organizations.

## 2. How are DAOs currently regulated?

Several jurisdictions have approved DAO regulations, including Wyoming, Tennessee, the Marshall Islands, Malta, Idaho, New Jersey. Among these, Wyoming is seen as the leading jurisdiction.

In July 2021, Wyoming was the first US state to legally recognize DAOs as separate legal entities.<sup>1</sup> The WY DAO Law addressed a core problem with existing DAOs; Namely, without a legal entity form, DAOs would default into general partnership. This means that its members would be jointly and severally liable. Wyoming corrected this by bringing DAOs under its Limited Liability Company (LLC) act and considering DAOs a type of LLC<sup>2</sup>. In March 9, 2022, Wyoming amended its DAO Supplement<sup>3</sup>, after detecting initial drawbacks and aiming to correct some of its initial shortcomings. Some of the issues revised and modified by the DAO Amendment to the initial regulation include but are not limited to the following:

- Quorum

The original DAO Law establishes that a quorum shall require not less than a majority of the membership interest entitled to vote. Nonetheless, it previously defined the majority of members as the approval of more than 50% of the membership interest in a vote for which a quorum of members is participating.

The amendment to the DAO Supplement allows a DAO to establish its definition of a quorum within its articles of organization or operating agreement by determining the minimum threshold of a DAOs total membership that is eligible to participate in a specific vote and no longer

---

<sup>1</sup> <https://www.wyoleg.gov/2021/Introduced/SF0038.pdf>

<sup>2</sup> The Wyoming DAO Law was designed as a supplement of the LLC Act. Therefore, the WY DAO regulation is an underlying application of the LLC Act to the extent not inconsistent with the DAO provisions.

<sup>3</sup> <https://www.wyoleg.gov/Legislation/2022/SF0068>



subjecting the quorum to the approval of more than 50% of participating membership interests.

- Member Managed vs. Algorithmically managed.

Initially the DAO Law established the option for the DAO to be established as member managed or algorithmically managed. If not specified, it would default to member-managed. The amendment states that the articles of organization shall establish how the DAO shall be managed and, if algorithmically-managed, to what extent.

- Voting Rights

The DAO Law contained a default rule on voting rights. The law states that membership interests in a member-managed DAO are calculated by dividing a member's contribution of digital assets to the DAO by the total amount of digital assets contributed to the DAO at the time of a vote. The amendment applies the pro-rata rule to all DAOs, not just to member-managed ones. If members do not contribute digital assets to the DAO as a prerequisite to becoming a member, each shall possess 1 membership interest and is entitled to 1 vote. Furthermore the amendment describes membership interest as a member's ownership right in a DAO, which may be determined by articles of organization or operating agreement or ascertainable from a blockchain on which the organization relies to determine a member's ownership right.

- Changes to Smart Contracts

The DAO Law initially stated that for an algorithmically managed DAO, the underlying smart contracts must be able to be updated, modified, or otherwise upgraded. The amendment clarifies that the management of the DAO shall be vested in its members and any applicable smart contracts, and that all smart contracts utilized by the DAO shall be capable of being updated, modified, or otherwise upgraded. This would allow immutable smart contracts for DAOs with some degree of member management.

- Dispute Resolution

The original Law did not include content on dispute resolution. The amendment to the DAO Law establishes the requirement for the articles of organization or smart contracts to include provisions regarding dispute resolution. The founding members are therefore required to include mechanisms of dispute resolution from the very beginning.

- Information Rights

The DAO Law did not give its members the right to separately inspect or



copy records of a DAO or for the organization to have obligation to furnish information concerning its activities, financial condition or other circumstances. Nonetheless, the amendment clarified that the information is only not available to the extent the information is available on an open blockchain.

After this ANPRM, the Zone Authority could adopt DAO Regulation with the purpose of recognizing DAOs as one of the business entity types included under Title VII of the GEZ Civil Ordinance. As seen in the Wyoming case, the CDEZ could regulate DAOs as type of LLC, and therefore make them subject to Title VII, Ch. 7 of the Civil Ordinance, which incorporates, without changes, the Uniform Law Commission's (ULC) Uniform Limited Liability Company Act (2013).

As seen above, Wyoming DAO Regulation is a useful and important point of reference for a potential CDEZ DAO Regulation, especially given that WY has already done amendments on its initial rule. The Zone Authority wishes to know what can be improved over Wyoming and other existing DAO frameworks across the world.

Alternatively, the CDEZ could consider DAOs as a type of Cooperative, as seen in Colorado, which would make them fall under Title VII, Ch. 8 of the Civil Ordinance, Uniform Limited Cooperatives Act (2013), also by the ULC. Commenters can propose other potential business entity types can be found in the Civil Ordinance, Title VII. Also of relevance is Title VI, Ch. 10, which covers digital assets.

### **3. Considerations on proposed regulation on DAO Advance Notice of Proposed Rulemaking.**

The following are Questions for the General Public and all interested parties in participating in the rulemaking process.

The comments on the subject of the proposed rulemaking as well as the answers to the questions below, will be received through the following Channels, until July 15, 2022.

[DISCORD CHANNEL](#)

[Online Form](#)

Email: [daos@zoneauthority.io](mailto:daos@zoneauthority.io)

### **4. Questions**

The following questions for comment are generally intended to collect information about a potential rule that would apply for all DAOs incorporated in the Catawba Digital Economic Zone.



## General

1. Why should there be a DAO regulation?
2. What are the main current problems DAOs face that can be addressed by regulations?
3. What would you like to find in a DAO regulation that no other regulator currently provides?

## Comparative

4. What country or state has the best DAO regulation?
5. What are the advantages and disadvantages of the Wyoming DAO LLC regulation compared to the regulations adopted in other states or jurisdictions?

## Wyoming

6. What are the problems with the current Wyoming DAO regulations?
7. In what ways are the amendments to the WY DAO regulation sufficient or incomplete to sort out the problems evidenced so far with Wyoming's DAO regulation?

## Structure

8. What legal structure has been best for DAOs so far?
9. Does COALA's Model Law provide a solid regulatory framework for DAOs? And why?
10. What are the strengths and disadvantages of regulating DAOs as cooperatives rather than LLCs?
11. In what ways would it be more or less effective to regulate DAOs as UNAs (Unincorporated Non-profit Associations) than LLCs?
12. What would be the implications and challenges for the CDEZ as a regulator to regulate DAOs as Unincorporated Non-Profit Associations?
13. What is the ideal DAO structure in the LLC context to solve DAO's main tax and securities challenges?

## Foundation



14. What would be the implications of requiring that a DAO's articles of organization include a publicly available identifier of any smart contract directly used to "manage, facilitate or operate" the DAO?
15. How, and if, should the CDEZ exercise oversight of the quality of said publicly available identifier?
16. What are the advantages and/or risks of having an Operating Agreement on the blockchain available to the public?
17. To what degree should the DAO regulation allow for the possibility of an algorithmically managed DAO?

### **Pseudoanonymity**

18. How should KYC pseudonymity be regulated if included as component of the CDEZ DAO framework?

### **KYC and Registered Agents**

19. What would be the implications on the single point of contact for DAOs in the CDEZ being a registered agent?
20. Should DAOs have a point of contact other than the registered agent with the CDEZ?
21. How should the CDEZ conduct KYC, and to which/how many members of DAOs should it conduct KYC?

### **Quorum**

22. How should quorum be defined in the CDEZ DAO framework? (I.e. based on who participates and when they participate, defining a specific time to vote -48 hours- or should this rather be open to each DAO)

### **Membership & Management**

23. Should the CDEZ allow DAOs to appoint managers in member-managed DAOs?
24. Does the appointment of managers in member-managed DAOs strip away the members fundamental rights in the DAO?
25. How should the CDEZ deal with appointing managers and how does this affect the fiduciary duties of the members and the appointed managers?
26. Should algorithmically managed DAOs be able to update, modify or



upgrade their underlying smart contracts? Should smart contracts for DAOs allow for some degree of member management?

27. How should the CDEZ regulate how DAOs disclose to what extent they will be algorithmically managed or fully automated?

## **Securities**

28. Does a DAO imply the issuance of governance tokens?
29. Does the centralized management of a DAO trigger the application of federal securities law?
30. Does the member-managed character of the DAO eliminate reliance on others as understood by the Howey Test and therefore is not dealing in securities in that regard?
31. How can the CDEZ allow the issuance of tokens within a DAO and be compliant with the offering of securities subject to regulation by the U.S. Securities and Exchange Commission (SEC)?
32. If the CDEZ moves forward with the Wyoming utility token exemption, would utility tokens be subject to securities law?

## **Other**

33. What additional questions should be asked?

## **Regulatory Planning and Review**

This advance notice of proposed rulemaking is a substantive, non-significant regulatory action under Section 303 of the CDEZ's Administrative Procedures Regulation, and has not been reviewed by the Zone Authority Attorney.

## **Conclusion**

With this ANPRM, the Zone Authority seeks input on the questions set forth above and related topics.

The Zone Authority welcomes comments on all aspects of the ANPRM, and other topics related to DAO regulations not included here. All interested parties are encouraged to provide their views.

## **By the Zone Authority**

Dated: June 1st , 2022.



---

Sam Trimnal

A handwritten signature in blue ink, appearing to read "S. Trimnal".

Chairman  
Zone Authority Commission.

Public Commenting Channels:

Comments may be submitted:

- 1) Via Discord on the Catawba Digital Economic Zone [Discord Channel](#)
- 2) By filling out the following [form](#)
- 3) By sending an email to [daos@zoneauthority.io](mailto:daos@zoneauthority.io)