POSA Staking Industry Principles

The Proof of Stake Alliance (POSA) is urging the crypto staking industry to align around best practices in order to ensure consumer protection and responsible innovation in the staking space. In recent years, proof of stake (PoS) blockchains have grown to include 19 of the top 20 smart contract platforms with millions of users globally, representing a market cap of over $250 billion USD as of September 2023.[1] This level of adoption should be a welcome innovation – in proof of stake, as an alternative to proof of work, validators don't have to dedicate massive amounts of computing power to validate transactions and secure the network.[2]

Instead, while it varies from blockchain to blockchain, validators temporarily commit (or "stake") their tokens in order to build the blockchain and create new tokens. Validators' activities include proposing new blocks to the blockchain that are verified by other validators, verifying blocks that other validators have proposed, agreeing on the state of the chain, finalizing collections of blocks for permanent inclusion on the blockchain, and other technical activities. Validators keep the network secure, accurate, and current across the entire network of globally distributed computers.

---

[1] This reflects the market cap of the top 35 PoS assets. Staked, The State of Staking, Q4 2023.

[2] Validators are rewarded with the new tokens by the relevant protocol smart contract as long as they stake the network's governance token, maintain protocol uptimes, and correctly participate in the network. For more on proof of stake, including key definitions, see for example, Peter Van Valkenburgh, "What is Staking?"; Matt Corva and Bill Hughes, "Staking is Data Validation, Not Investment".

Though in recent years the term staking has been co-opted to refer to a number of different activities, it's important to understand that staking is not simply the act of "locking up" tokens.[3] Staking is about securing PoS blockchains, which depend on the technology for their security and accuracy. Staking thus should be distinguished from activities like yield farming and lending, which do not concern blockchain security.[4]

Staking is a purely technical activity, which means any actor that wishes to stake must take on the responsibility of participating in this technical process. Users that hold a stakeable token (like ETH, SOL, or AVAX) and wish to participate in a Proof of Stake network (like Ethereum, Solana, or Avalanche) can choose to stake themselves or may place their tokens with a technical Staking-as-a-Service Provider. Staking-as-a-Service providers expand the pool of available stakers. These providers do the technical work of running validators and associated infrastructure, thereby enabling users without the necessary time or infrastructure to participate in Proof of Stake networks, for which, in certain cases, they charge users a portion of the rewards that the users may earn for providing useful work to the network. This is similar to how AWS allowed developers the ability to easily build internet applications without maintaining in-house servers.[5]

---

[3] See, for example, SEC v. RICHARD J. SCHUELER, a/k/a RICHARD HEART, HEX, PULSECHAIN, and PULSEX, pg 7. "Hex's so-called "staking" mechanism does not involve validating transactions on the blockchain. On the Hex.com website, Heart analogized his so-called "staking" process to conventional interest payments and investment returns." True staking involves the participation in network validation and governance, whereby stakers and validators commit resources to ensure the security of a blockchain network.

[4] Staking worthy of the name is often called "protocol staking" or "consensus staking." Other activities, like yield farming or lending, typically involve users receiving payments for storing or transferring certain digital assets to a third party who then uses the assets for a variety of activities, some of which may entail considerable risk.

[5] The proof of stake network will typically reward the validator with newly created tokens and a portion of the transaction fees (staking rewards) in accordance with the rules of the algorithm, for so long as the validator remains online and operates in accordance with the blockchain's technical and participation requirements.

In the years since the launch of the first natively proof of stake blockchains, many technical service providers have commercialized services surrounding staking. In 2020, we issued our first set of industry principles in an effort to align this burgeoning industry around best practices. Since then, the industry has grown and matured. In order to update our principles, we recently met with and gathered feedback from many key participants in these ecosystems. Our collective goal is to ensure that staking is better understood, and that technical services related to staking and block production are treated similarly to operating any other technical service providers. We need to ensure that those who participate in proof of stake ecosystems by providing these services are properly recognized as offering technical services, separate and distinct from engaging in financial activities, and that consumer protection remains paramount as the number of PoS token holders grows year over year. As such, we anticipate updating these principles over time, as proof of stake ecosystems continue to grow and mature.

With these goals in mind, POSA urges service providers and key ecosystem participants to adopt the following industry-driven principles going forward, as staking continues to mature as a technical and commercialized service:

Principle I: Service providers should communicate clearly to ensure that users have all the information necessary to make informed decisions.

- **Be clear about the services being provided and disclose all relevant information to stakers —** Stakers that do not choose to run hardware and/or software themselves have the choice to engage a technical Staking as a Service Provider. Service providers should be clear as to whether they are enabling the user to engage in self-custodial

software-as-a-service staking, delegated custodial staking, or smart contract-facilitated liquid staking. Like all technical service providers, where possible staking service providers should provide adequate disclosures and information in their terms of service. These may include but are not limited to slashing risk, obligations of the service provider, and legal rights of the staker.

● **Use Accurate Terminology and Refrain from Investment Advice** — A service provider should not make any recommendations as to whether or not a market participant should purchase a particular proof of stake digital asset. The service provider also should make no representations to market participants as to potential appreciation in the value of the staked digital asset. Service providers and/or those providing marketing materials on behalf of public protocols should avoid using words such as "interest" or "dividend," which may be confused for their financial meanings. POSA suggests the use of more accurate terminology such as "Block Reward" or "Staking Reward."

● **Focus on Operational Staking Posture and Processes Instead of the Ability to Earn Enhanced Rewards —** A service provider should not market a user's ability to earn "enhanced" rewards in excess of protocol rewards, or claim to have a competitive advantage outside what is earned natively from the protocol.

● **Have a Clear Fee Schedule —** A service provider should provide users with a clear fee schedule and other relevant terms and conditions that outline exactly how much of the user's rewards the staking provider will accrue.

Principle II: Users should control whether and how much of their assets to stake

- **User Opt-In** — A service provider should require that each user opt-in to either native or liquid staking and should not stake a user's assets without such user's affirmative action or consent.

- **Focus on Providing Access to the Protocol & User Ownership of Staked Assets** — A service provider should focus on its service of providing access to the protocol and highlight that the user is and remains the owner of the underlying staked asset (plus any staking rewards).

Principle III: Service providers should have explicitly delineated responsibilities.

- **Do not manage or control liquidity for users** — A technical service provider should not determine or manage the amount of a user's staked assets to provide users with liquidity. Each user should be able to determine the exact amount of their tokens that are staked.

- **Do Not Provide Guarantees on the Amount of Rewards Earned** — A service provider should not provide any guarantees or make any commitments to users as to the amount of staking rewards to be earned from a given protocol pursuant to the service relationship. The service provider should provide clarity surrounding the fees for their own technical services, but also make clear that the provider has no control over the overall staking reward rate for the applicable proof of stake protocol, as such rate is determined by the protocol itself. Service providers may note an estimated reward rate based on historical

experience, but should make clear that rewards are determined by the protocol, which the service provider has no control over and may change over time for various reasons. The provider should also make clear that rewards are distributed in the native token of the protocol and that there can be no assurance of the value of that asset relative to any other crypto asset or fiat currency.

Given the prevalence of proof of stake, and the current regulatory climate in the United States, the relevance of these staking industry principles has been amplified. Focusing on areas such as emphasizing security and participation, refraining from investment advice, using non-financial terminology, and not providing guarantees on rewards earned, these forward-looking principles are aimed at aligning organizations around best practices, fostering self-regulation, and effectively communicating with regulators to ensure a proper understanding of staking as a technical service, separate and distinct from financial activities. We hope to set the industry standard for self-regulation, allowing proof of stake networks and the ecosystems that support them to thrive responsibly.