DENTONS LEE

SEC v. Ripple Labs, Inc : Now what?

1. Introduction:

The Securities and Exchange Commission ("SEC") filed a litigation to the United States District Court Southern District Of New York against RIPPLE LABS, INC., CHRISTIAN A. LARSEN and BRADLEY GARLINGHOUSE on December 22, 2020, claiming that XRP – the virtual currency of Ripple – was supposed to be the subject of the federal securities laws as it constitutes a security but as it failed to conform to such laws, punishment and suspension order for the non-compliance must be rendered. As a response to this complaint (the "Complaint"), Ripple submitted an answer (the "Answer") on January 29, 2021 requesting the court's dismissal of such Complaint by the SEC based on the primary allegation that XRP is not a security.

This document summarizes the gist and details of the request made by Ripple in its Answer on the SEC's Complaint.

2. The Remedies the SEC filed with the court against RIPPLE and the grounds therefor:

In its Complaint dated December 22, 2020, the SEC requested the court to order Ripple's disgorgement of all ill-gotten gains, prohibition of Ripple's issuance of XRP and imposition of civil money penalties on Ripple because Ripple violated the federal securities laws by failing to conform to such laws despite the fact that XRP constitutes a security. The original details of such claim are as follows:

"The Commission seeks a final judgment: (a) permanently enjoining Defendants from violating Sections 5(a) and 5(c) of the Securities Act, pursuant to Section 20(b) of the Securities Act [15 U.S.C. § 77t(b)]; (b) pursuant to Section 21(d)(5) of the Securities Exchange Act of 1934 ("Exchange Act"), (i) ordering Defendants to disgorge their ill-gotten gains and to pay prejudgment interest thereon and (ii) prohibiting Defendants from participating in any offering of digital asset securities; and (c) imposing civil money penalties on Defendants pursuant to Section 20(d) of the Securities Act." (page 3 of the SEC's Complaint)

2. Arguments Raised by RIPPLE and the SEC

For better understanding on the arguments made each by the SEC and Ripple at this point in time, we considered that as the preliminary statement part of Ripple's Answer (summary of the Defendant's claim on pages 1-8 of the Answer; underlined parts below) contains the gist of Defendant Ripple's overall argument, it could help the understanding on Ripple's argument. So, we added such part as direct excerpt and when needed for each argument, we also added the details of each argument from both sides presented in the remainder of the Answer.

1. The Complaint filed by the SEC advances an unprecedented and ill-conceived legal theory— with neither statutory mandate nor congressional authorization — that Ripple's distributions of the virtual currency XRP constitute "investment contract[s]" and thus "securit[ies]" subject to registration under Section

5 of the Securities Act of 1933. 15 U.S.C. § 77b(a)(1). That theory ignores, among many other things, that XRP performs a number of functions that are distinct from the functions of "securities" as the law has understood that term for decades. For example, XRP functions as a medium of exchange— a virtual currency used today in international and domestic transactions — moving value between jurisdictions and facilitating transactions. It is not a security and the SEC has no authority to regulate it as one.

- On this argument, the SEC reveals its opinion that there is no significant non-investment "use" for XRP exists, and Ripple did not sell XRP in the offering for "use" and XRP are not "currency" under the federal securities laws (pages 56 and 59 of the SEC's Complaint).
- In the Complaint, the SEC alleges that XPR had little to no "use" existed until Ripple subsidized some operations related to the use of virtual currency in recent months, and Ripple offered and sold XRP to any person, without restricting offers or sales to persons who had a "use" for XRP (paragraph 87 of the Complaint). Ripple denies such allegations, claiming that the use for XRP was not limited to Ripple's operations or activities (paragraph 87 of the Answer).
- In addition, the SEC alleges that the first potential use that Defendants touted for XRP—to serve as a "universal digital asset" and/or for banks to transfer money—never materialized (paragraph 332 of the Complaint), and not until approximately mid-2018 did Ripple first begin earnestly testing ODL—to date its only product that permits XRP use for any purpose. The potential "users" of ODL that Ripple is targeting are money transmitters (paragraph 333 of the Complaint). However, Ripple denies all such allegations except the use of ODL in the Answer (paragraphs 332 and 333 of the Answer). Also, the SEC alleges that on June 21, 2018, Garlinghouse explained in a public speech that nobody was using XRP to effect cross-border transactions as of that date (paragraph 336 of the Complaint) but Ripple denies such allegations (paragraph 336 of the Answer). Also, the SEC alleges that Ripple announced, for the first time in its history in 2020, that it began selling XRP directly to money transmitters specifically for effecting money transfers through ODL (paragraph 346 of the Complaint). Ripple also denies such allegations and it referred the court to the full text of the document for an accurate and complete record of its contents (paragraph 346 of the Answer).
- In addition, the SEC alleges that throughout the offering, Ripple did not target sales of XRP to people to whom XRP's undeveloped, potential future "uses" could reasonably be expected to appeal and Defendants did not market XRP in such manner (paragraph 349 of the Complaint). Ripple denies such allegations, saying that it is characterizations and legal conclusions (paragraph 349 of the Answer).
- One of the grounds for Ripple's allegation that XRP is not a security under the federal securities laws is that Ripple and XRP entered into a settlement with the DOJ and FinCEN in May 2015 in which the DOJ and FinCEN referred to XRP as a "convertible virtual currency." The SEC rebuts such allegation by stating that XRP is not "currency" under the federal securities laws and XRP has not been designated as legal tender in any jurisdiction and Ripple has never offered or sold XRP as "currency" (paragraphs 355, 356 and 357 of the Complaint). Ripple denies such allegations in the Answer, saying that it is legal conclusions and argued that XRP is a virtual currency.
- To sum up, the SEC considers XRP as a security because XRP – the so-called virtual currency - has practically never been used as currency or for money transfer until recently and Ripple, too, has never market XRP for such use and XRP is not a currency under the federal securities laws. Meanwhile, Ripple, in its Answer, is denying above allegations of the SEC by mentioning the actual transactional uses of XRP.

2. Before this case, no securities regulator in the world has claimed that transactions in XRP must be registered as securities, and for good reason. The functionality and liquidity of XRP are wholly incompatible with securities regulation. To require XRP's registration as a security is to impair its main utility. That utility depends on XRP's near-instantaneous and seamless settlement in low-cost transactions. Treating XRP as a security, by contrast, would subject thousands of exchanges, market-makers, and other actors in the gigantic virtual currency market to lengthy, complex and costly regulatory requirements never intended to govern virtual currencies.

3. In 2015 and again in 2020, the U.S. Department of Justice ("DOJ") and U.S. Department of the Treasury's Financial Crimes Enforcement Network ("FinCEN") determined that XRP is lawfully used and traded in the marketplace as a virtual currency. Those determinations are consistent with the economic reality that XRP functions as a store of value, a medium of exchange and a unit of account — not a share in Ripple's profits. When the DOJ and FinCEN reached those determinations in 2015, the SEC said not a word. Securities regulators in the United Kingdom, Japan, and Singapore have likewise concluded that XRP is a virtual currency not subject to securities regulation. As the U.K. Treasury recently explained, "widely known cryptoassets such as Bitcoin, Ether and XRP" are not securities, but "[e]xchange tokens" that "are primarily used as a means of exchange."

4. The SEC filed this Complaint 8 years after XRP was created, 5 years after the DOJ and FinCEN characterized XRP as a virtual currency, and after more than 2"½ years of investigation during which the SEC allowed Defendants to continue to distribute XRP, allowed the XRP open market to grow, and allowed millions of market participants to rely on the free and efficient functioning of that market. The SEC's filing, based on an overreaching legal theory, amounts to picking virtual currency winners and losers as the SEC has exempted bitcoin and ether from similar regulation. It asks the Court to contradict the findings of the agency's peers in the United States and internationally and subject what has been a global virtual currency to conflicting regulatory regimes on a nation-by-nation basis. It also threatens to damage U.S. competitiveness and innovation, at a time when the United States has national security concerns about China's efforts to control bitcoin and ether mining pools and seize control of the global payments market. And the Complaint's mere filing has caused immense harm to XRP holders, cutting the value of their holdings substantially and causing numerous exchanges, market makers, and other market participants to cease activities in XRP. In bringing a case that alleges an unregistered offering of just over $1.3 billion "from at least 2013," the SEC has already caused more than an estimated $15 billion in damage to those it purports to protect.

- On the other hand, the SEC mentions the differences between XRP and bitcoin in the light of the federal securities laws and alleges in the Complaint that such matters were mentioned by legal memos prepared by a law firm in 2012. The legal memos noted that, unlike with bitcoin, there was a specific entity, Ripple, which is responsible for the distribution of XRP and the promotion and marketing functions of the Ripple Network (paragraphs 287-288 of the Complaint). Ripple denies such allegations, stating that the ultimate conclusion by the counsel who prepared such memos was that XRP did not constitute "securities" under the federal securities laws (paragraphs 287-288 of the Answer).
- The SEC also alleges that certain XRP investors understood this distinction and in an internal email of one Ripple equity shareholder wrote that "that has always been the point. Ripple is controlled by 1 entity rather than through a distributed entity like Bitcoin" (paragraph 288 of the Complaint). Ripple denies such allegation as it lacks sufficient information.

5. Ripple. Founded in 2012, Ripple is a San Francisco-based, privately-held payments technology company that uses blockchain innovation3 (including XRP) to allow money to be sent around the world instantly, reliably, and more cheaply than traditional avenues of money transmission. Ripple is a global company, with nearly 500 employees in 10 offices in the U.S. and around the world, that has worked steadily towards its vision of realizing an "Internet of Value"— a world in which blockchain enables value to move as seamlessly as information.

6. *XRP and the XRP Ledger. XRP is a fast, efficient and scalable digital asset, making it ideal for payment processing. XRP is transacted on the cryptographic XRP Ledger ("XRPL"). XRP was orig*inally designed to be a "better Bitcoin": more secure, because control over the XRPL is more distributed. The XRPL has, over eight years, processed hundreds of millions of payments without dispute. It works independently from Ripple. No one party owns or controls the network of peer-to-peer servers that powers XRPL. Nor does Ripple— or anyone else— control a majority of the third-party validators that adjudicate XRPL transactions.

7. XRP is also significantly more environmentally friendly than bitcoin and ether because it avoids an energy-intensive "mining" process. Bitcoin mining has been estimated to produce approximately 48.5 billion pounds of CO2 emissions per year, whereas XRP validators produce less than 1 million pounds. The computational power needed to mine and validate bitcoin transactions leaves an enormous carbon footprint, as compared to vastly smaller amount of energy consumed by XRP transactions.

8. Ripple did not sell or distribute XRP as an investment contract. Ripple has never offered or sold XRP as an investment. XRP holders do not acquire any claim to the assets of Ripple, hold any ownership interest in Ripple, or have any entitlement to share in Ripple's future profits. Ripple never held an "ICO" (initial coin offering);4 never offered or contracted to sell future tokens as a way to raise money to build an ecosystem; never explicitly or implicitly promised profits to any XRP holder; and has no relationship at all with the vast majority of XRP holders today, nearly all of whom purchased XRP from third parties on the open market.

- However, the SEC is taking quite the opposite position on above matters: The SEC mentions that "XPR was a security in the entire course of provision thereof by Ripple." The SEC's Complaint suggests the definition of a "security" rendered by the United States Supreme Court in the case of SEC v. W.J. Howey Co., 328 U.S. 293, 299 (1946). In such case, the Supreme Court defined that "'security' broadly to embody a flexible rather than a static principle, one that is capable of adaptation to meet the countless and variable schemes devised by those who seek the use of the money of others on the promise of profits" (paragraph 205 of the Complaint).
- To support its allegation that XRP is a security, the SEC listed that: (i) Ripple led investors to reasonably expect that ripple's and its agents' entrepreneurial and managerial efforts would drive the success or failure of ripple's XRP projects; (ii) purchasers of XRP invested into a common enterprise; and (iii) Ripple led investors to reasonably expect a profit from their investment derived from defendants' efforts (pages 36, 45 and 49 of the Complaint).
- The SEC alleges in the Complaint that "sophisticated investors agreed. For example, a hedge fund, to which Ripple sold XRP, explained to the fund's investors this economic reality in offering materials from March 2015: 'The increase in XRP value is heavily dependent on the success of Ripple'" (paragraph 212 of the Complaint) and Ripple denies the above allegations, except that Ripple distributed XRP to such entity (paragraph 212 of the Answer).
- The SEC alleges in the Complaint that "Ripple publicly offered and sold XRP as an investment into a common enterprise that included Ripple's promises to undertake significant entrepreneurial and managerial efforts, including to create a liquid market for XRP, which would in turn increase demand for XRP and therefore its price," adding that Ripple made statements promoting XRP in a variety of publicly available media, including Twitter, YouTube, major financial news networks, industry conferences, etc. (paragraphs 213 and 214 of the Complaint) but Ripple denies all such allegations except that it has made public statements referencing XRP (paragraphs 213 and 214 of the Answer).
- Therefore, the SEC alleges that "based on these representations, Ripple's actions, and the economic reality, XRP investors in the offering had a reasonable expectation of profiting from Ripple's efforts to deploy investor funds to create a use for XRP and bring demand and value to their common enterprise" (paragraph 216 of the Complaint). Ripple denies such allegations, too, and argues that SEC is making limited and inaccurate description on the distribution types of XRP (paragraph 216 of the Answer).
- To sum up, the SEC is alleging that the purchasers of XPR bought XPR for the future profit of XPR price rise instead of seeking any monetary use and it was what Ripple induced them to think so and therefore, XPR is a security. But Ripple is practically denying all such allegations raised by the SEC, arguing that it has never made any promises of future profit.

9. What limited contracts Ripple did enter into with sophisticated, institutional counterparties were not investment contracts, but standard purchase and sale agreements with no promise of efforts by Ripple or future profits. Ripple has no explicit or implicit obligation to any counterparty to expend efforts on their behalf; proceeds of XRP sales are not pooled in a common enterprise; and holders of XRP cannot objectively rely on Ripple's efforts. And Ripple could cease to function tomorrow, but XRP would continue to survive and trade in its fully developed ecosystem.

- On above allegation, the SEC is stating that Ripple expected that most, if not all, institutional sales buyers would sell their XRP into public markets and tried to protect XRP's trading price by limiting the amounts that could be resold during any given time period and by selling at discounts to market prices, Ripple incentivized these buyers to seek to sell their XRP into the public markets in order to realize what was essentially a guaranteed profit (paragraph 106 of the Complaint). On this allegation, Ripple admits that it distributed certain XRP at discounted prices but specifically denies that its sales of XRP were intended to, or did, incentivize buyers to realize a "guaranteed profit," and further denies that its sales of XRP could have provided a "guaranteed profit," given that Ripple could not control movements in the market price of XRP following its sales (paragraph 106 of the Answer).
- As mentioned above, the SEC alleges that Ripple repeatedly stated publicly that they would undertake significant efforts to develop and foster "uses" for XRP, so that banks, financial intermediaries, or other specialized money transmitting businesses would want to buy it, and Ripple also persistently stated publicly that they would take steps to create, promote, and protect the market for trading in XRP and persuade digital asset trading platforms to permit investors to buy and sell XRP and these statements led reasonable investors to expect to profit from Ripple's efforts on behalf of XRP (paragraph 217 of the Complaint). On this, Ripple answers that such allegations are characterizations, containing insufficient citation or attribution and such allegations were denied except the fact that Ripple has made statements referencing use cases and related markets for XRP (paragraph 217 of the Answer).
- In addition, the SEC is alleging that XRP is a security because the purchasers of XRP invested into a common enterprise. The SEC mentions that "the fortunes of XRP purchasers were and are tied to one another, and each depend on the success of Ripple's XRP strategy," adding "in other words, Ripple's success or failure in propelling trading of XRP drives demand for XRP, which will dictate investors' profits or losses." The SEC mentions that "XRP investors stand to profit equally if XRP's popularity and price increase, and no investor will be entitled to a higher proportion of price increases" (paragraphs 265-266 of the Complaint). Ripple denies such allegations by stating that such allegations consist of characterizations and legal conclusions to which no response is required (paragraphs 265-266 of the Answer).
- Also, the SEC is alleging that Ripple pooled the funds it raised in the offering and used them to fund its operations, including to finance building out potential "use" cases for XRP, paying others to assist it in developing a "use" case, constructing the digital platform it promoted, and compensating executives recruited for these purposes. Also, the SEC is alleging that Ripple did not segregate or separately manage proceeds from different XRP purchasers in the offering and the nature of XRP itself made it the common thread among all other XRP holders (paragraph 267 of the Complaint). Ripple also denies such allegations by stating that such allegations consist of characterizations to which no response is required (paragraph 267 of the Answer).
- The SEC is alleging that an official at Ripple has repeatedly and publicly expressed that Ripple's incentives are aligned with other XRP holders'—specifically, as to increasing Ripple's price—because Ripple "holds a huge pile of XRP," including in a statement he made on XRP Chat on May 25, 2017 (paragraph 279 of the Complaint). Ripple also denies such allegations by stating that such allegations consist of characterizations to which no response is required, and referred the court to the full text of the document for an accurate and complete record of its contents (paragraph 279 of the Answer).
- Also, in its Complaint, the SEC is alleging that Ripple also led investors to reasonably expect that they could reap a profit from their investment into XRP, derived from Ripple's and its agents' efforts into their common enterprise. According to the SEC, Ripple did so by, among other things, stating that Ripple's efforts sought to increase "demand" for XRP; assuring investors that Ripple would take steps to protect the market for XRP, including by fostering a readily available XRP trading market; highlighting XRP price increases and at times tying them to Ripple's efforts; and selling XRP to certain institutional investors at discounted prices (paragraph 289 of the Complaint). Ripple also denies such allegations by stating that such allegations consist of characterizations and legal conclusions to which no response is required (paragraph 289 of the Answer).

To sum up, the SEC is alleging that XRP is a security because Ripple induced the buyers to make a reasonable expectation that the success or failure of XRP will depend on Ripple's efforts, and also induced the XRP buyers to have a reasonable expectation that they can enjoy profit from Ripple's efforts and given the circumstances, the nature of XRP purchase was the investment in the common enterprise. Ripple is denying all such allegations in its Answer, stating that such allegations consist of characterizations and is arguing that Ripple's sale of XRP is a simple sale of a product, and the buyers cannot rely on Ripple's efforts.

10. Ripple holds a large percentage of XRP, but that alone does not and cannot render it an investment contract. Many entities own large amounts of commodities and participate heavily in the commodities markets — Exxon holds large quantities of oil, De Beers owns large quantities of diamonds, Bitmain and other Chinese miners own a large percentage of outstanding bitcoin. Such large commodity owners inevitably have interests aligned with some purchasers of the underlying asset. But there is no credible argument that substantial holdings convert those commodities or currencies into securities, nor has any case so held.

11. The Complaint. The Complaint is a sprawling and convoluted effort to allege that Ripple's distributions of XRP (through numerous and varied methods) over a nearly eight-year period constitute a single, unbroken distribution of "investment contracts" subject to registration under Section 5 of the Securities Act.

12. To that end, the Complaint mischaracterizes, misunderstands or ignores the economic realities of XRP, including: (i) that the XRP Ledger is entirely open-source, decentralized, and operates on an enormous scale (more than 1.4 billion transactions globally since 2013) outside of Ripple's control; (ii) that XRP is and long has been a digital asset with a fully functional ecosystem and utility as a bridge currency and other types of currency uses; and (iii) that XRP's price is not and has not been determined by Ripple's activities — instead, the market has for many years priced XRP in correlation with other virtual currencies, most notably bitcoin and ether (which the SEC has publicly stated are not investment contracts). Indeed, as the Complaint admits, Ripple has its own equity shareholders who purchased shares in traditional venture capital funding rounds and who – unlike purchasers of XRP – did contribute capital to fund Ripple's operations, do have a claim on its future profits, and obtained their shares through a lawful (and unchallenged) exempt private offering.

13. The SEC's theory in the Complaint would read the word "contract" out of "investment contract," and stretch beyond all sensible recognition the Supreme Court's test for determining investment contracts in SEC v. W.J. Howey Co., 328 U.S. 293 (1946). As a matter of economic substance, XRP categorically differs from the various instruments and business arrangements that Congress authorized the SEC to regulate— all of which, unlike Ripple, involve "schemes devised by those who seek the use of the money of others on the promise of profits." Howey, 328 U.S. at 299. Every other case in which courts have ruled that transactions involving a digital asset were investment contracts involved an issuer's ICO or other promise of future tokens to raise money to develop a digital-asset product, as well as a contractual relationship between the issuer and asset purchasers. Ripple never held an ICO, never offered future tokens to raise money, and has no contracts with the vast majority of XRP holders.

14. The SEC's Complaint tries to overcome these legal obstacles by mischaracterizing the record. For example:

a. The Complaint characterizes all of Ripple's business transactions involving XRP over eight years, regardless of their nature, purpose, or manner of execution, as a single "Offering"— a claim contradicted by the Complaint's own allegations of Ripple's evolving business strategy and different types of sales and distributions of XRP over time.

b. The Complaint alleges information asymmetries as between Ripple and XRP holders in vague, non-specific terms, but it fails to identify any material information asymmetries and omits Ripple's detailed quarterly reports about Ripple's activities in the XRP market. Nor could any such purported information asymmetries, even if present, transform the sale of a digital asset into a securities offering.

c. The Complaint mischaracterizes advice that Ripple received in 2012, from which a reasonable reader actually would have concluded that Ripple Credits (a past name for XRP) were not a security.

- In its Complaint, the SEC is alleging that Ripple was provided with two legal memos - one around February 2012 and another around October 2012 – from a law firm who was commissioned by Ripple, and such legal memos warned that there was some risk that XRP would be considered an "investment contract" under the federal securities laws depending on various factors (paragraph 53 of the Complaint). However, Ripple denies such allegations and avers that "any reasonable reader of the true and accurate contents of the memorandum would understand that counsel's ultimate conclusion was that Ripple Credits (a past name for XRP) did not constitute "securities" under the federal securities laws (paragraph 53 of the Answer).
- Also, the SEC is alleging that both legal memos warned that XRP was unlikely to be considered "currency" (paragraph 54 of the Complaint), but Ripple argues that those memoranda only purported to compare XRP to fiat currency, and the SEC is mischaracterizing such memos (paragraph 54 of the Answer).

d. The Complaint also misleadingly suggests that Ripple's sales of XRP constituted a significant part of the XRP market, but leaves out that in nearly all periods, such sales constituted less than 0.4% of total XRP transaction volume.

15. The Complaint's overreaching allegations have caused harm not only to Ripple, but also to hundreds of non-parties that integrate XRP into products or offerings or otherwise support XRP and to millions of XRP holders. It is especially important that the Court rapidly determine the most consequential and overarching issue: whether Ripple's current distributions of XRP are "investment contracts" under existing U.S. securities laws. The answer is a resounding no, and reaching that determination quickly is urgently needed to provide clarity to the market.

3. Affirmative Defense

Based on above points and other grounds for defense, Ripple requested the court's dismissal of the Complaint submitted by the SEC. Under the laws of the United States, affirmative defense means a ground for the defense that can exempt a defendant from liability even if all the allegations raised by a plaintiff in its complaint have been substantiated. Ripple listed a total of seven affirmative defenses as follows (pages 90-92 of the Answer of Ripple):

"Ripple alleges, asserts, and states the following defenses as separate and distinct defenses to the Complaint. By virtue of alleging these further defenses, Ripple does not assume any burden of proof, persuasion, or production not otherwise legally assigned to it."

FIRST DEFENSE: FAILURE TO STATE A CLAIM

The Complaint fails to state a claim upon which relief may be granted.

SECOND DEFENSE: XRP IS NOT A SECURITY

Ripple did not violate Section 5 of the Securities Act because XRP is not a security or "investment contract," and Ripple's distributions or sales of XRP are not "investment contracts." No registration was required in connection with any distribution or sale of XRP by Ripple.

THIRD DEFENSE: NO LIKELIHOOD OF FUTURE VIOLATIONS

The relief requested in the Complaint is inappropriate, in whole or in part, because the Complaint fails to allege a reasonable likelihood of future violations by Ripple.

FOURTH DEFENSE: LACK OF DUE PROCESS AND FAIR NOTICE

Ripple did not have, and Plaintiff failed to provide, fair notice that its conduct was in violation of law, in contravention of Ripple's due process rights. Due process requires that laws give a person of ordinary intelligence a reasonable opportunity to know what is prohibited. Here, due to the lack of clarity and fair notice regarding Defendants' obligations under the law, in addition to the lack of clarity and fair notice regarding Plaintiffs' interpretation of the law, Ripple lacked fair notice that its conduct was prohibited.

The lack of fair notice to Ripple was exacerbated when, in May 2015, Ripple entered into a settlement with the U.S. Department of Justice and FinCEN that described XRP as a "convertible virtual currency," and that expressly permitted future sales and distributions of XRP, including in secondary markets, provided they were conducted by a money services business registered with FinCEN and in compliance with federal laws and regulations applicable to money services businesses. Upon information and belief, Plaintiff knew of that 2015 settlement and yet, for years after, Plaintiff provided Defendants with no clear notice that, in Plaintiff's view, Defendants' prospective XRP sales as permitted by the agreement would nevertheless constitute a violation of another federal law.

The lack of fair notice to Ripple was further exacerbated when, in June 2018, Plaintiff's then-Director of Corporation Finance told virtual currency purchasers that the agency did not consider the virtual currencies bitcoin or ether to be securities and would "put[] aside the fundraising that accompanied the creation of [e]ther" and look instead at the "present state of [e]ther." Ripple and other reasonable observers further reasonably understood those remarks to indicate that Plaintiff would permit present-day sales of virtual currencies given the current market conditions for XRP.

FIFTH DEFENSE: EXEMPTION FROM REGISTRATION

Even were the Court to find that XRP constitutes a security or investment contract within Section 5 of the Securities Act, Plaintiff's claim against Ripple is barred in whole or in part because Ripple's distributions or sales of XRP were exempt from the registration requirements of the Securities Act and/or the regulations promulgated thereunder.

SIXTH DEFENSE: LACK OF EXTRATERRITORIAL AUTHORITY

Plaintiff lacks extraterritorial authority over all or some of the transactions alleged in the Complaint that took place outside the United States and/or were made on foreign exchanges.

SEVENTH DEFENSE: STATUTE OF LIMITATIONS

Plaintiff's claim and Plaintiff's request for civil monetary penalties are barred in whole or part by an applicable statute of limitations.

4. Sub-Conclusion

Given the SEC's Complaints and Ripple's Answer, the SEC mainly alleges that XRP is a security in all circumstances under the federal securities laws which naturally requires XRP to be the subject of regulations under such securities laws but as Ripple did not conform to the federal securities laws, it must disgorge all ill-gotten gains and its issuance of XRP must be prohibited and civil money penalties must be imposed. Meanwhile, Ripple is denying all such allegations by considering them as characterizations and legal conclusions, and it also largely denies the facticity of the evidence cited by the SEC when it presented its allegations in the Complaint (direct denial, denial due to the lack of knowledge, denial due to insufficient citation or attribution, etc.) while requesting the court to directly re-examine such submitted evidence.

Therefore, in the present litigation, we determine that the legal judgment on the definition of securities and investigation of facts could be made down the line, which in turn will bring about the result in the end.