

Securities Law Alert

KEY DEVELOPMENT IN SHAREHOLDER LITIGATION

Second Circuit: Decentralized Crypto-Exchange Transactions Plausibly Alleged to Be Domestic Under *Morrison*

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On March 8, 2024, the Second Circuit reversed and remanded a district court’s dismissal of a putative securities fraud class action alleging that a decentralized online crypto-exchange violated federal and state securities laws by promoting, offering and selling tokens that were not registered as securities. *Williams v. Binance*, 2024 U.S. App. LEXIS 5616 (2d Cir. 2024) (Nathan, J.). The Second Circuit held that plaintiffs plausibly alleged that the transactions were domestic transactions, under *Morrison v. National Australia Bank*, 561 U.S. 247 (2010), because they became irrevocable within the U.S. The court found that two transactional steps gave rise to an inference that irrevocable liability occurred in the U.S. First, the transactions were matched—and therefore became irrevocable—on U.S.-based servers. Second, plaintiffs transacted on the exchange from the U.S. and their buy orders became irrevocable when they were sent, pursuant to the exchange’s Terms of Use.

Background and Procedural History

The exchange is an online platform where various crypto-assets can be purchased and sold. Soon after it was founded in China in 2017 it moved its titular headquarters to Malta. However, the exchange rejects having any physical headquarters in any geographic jurisdiction. Plaintiffs bought tokens on the exchange and subsequently sued it after their trading prices fell. Plaintiffs alleged that the exchange violated Section 12(a)(1) of the Securities Act by unlawfully promoting, offering, and selling tokens that were not registered as securities.¹ The district court dismissed plaintiffs’ claims concluding that they constituted an impermissible extraterritorial application of securities law under *Morrison*. Plaintiffs appealed.

Irrevocable Liability Was Incurred in the U.S.

The Second Circuit held that each of the district court’s bases for dismissing plaintiffs’ claims were erroneous. The court stated that “[p]laintiffs have adequately alleged that their claims involved domestic transactions because

¹ Plaintiffs also sought rescission of contracts they entered into with the exchange under Section 29(b) of the Exchange Act, alleging that it sold securities without being registered as a securities exchange or broker-dealer. Plaintiffs also asserted claims under various Blue Sky laws.

they became irrevocable within the United States and are therefore subject to our securities laws.” Under *Morrison*, the Supreme Court interpreted the Exchange Act as applying only to “[1] securities listed on domestic exchanges, and [2] domestic transactions in other securities.” The Second Circuit explained that “to sufficiently allege the existence of a domestic transaction in other securities, plaintiffs must allege facts indicating that irrevocable liability was incurred or that title was transferred within the United States.” The court continued that “[i]rrevocable liability attaches when parties become bound to effectuate the transaction or enter into a binding contract to purchase or sell securities.” The court explained that “[t]o determine whether a transaction is domestic, courts must therefore consider both when and where the transaction became irrevocable.”

The court acknowledged that determining where a transaction became irrevocable is “particularly difficult” when an exchange claims to have no physical location. However, citing *Federal Housing Finance Agency v. Nomura Holding America*, 873 F.3d 85 (2d Cir. 2017), the court pointed out that “irrevocable liability may attach in more than one location.” The court then held “that irrevocable liability was incurred in the United States because Plaintiffs plausibly alleged facts allowing the inference that the transactions at issue were matched on U.S.-based servers.” The court concluded it was appropriate to locate the matching of transactions where the exchange had its servers in the absence of an official locus of the exchange. Further, the court found that the fact that plaintiffs alleged that their purchase orders were submitted from U.S. locations rendered it more plausible that the trades at issue were matched over servers located in the U.S., as opposed to servers located elsewhere.

The court also held that plaintiffs plausibly alleged that the transactions were domestic for a second reason. The court explained that “[b]ecause [the exchange] disclaims having any location, Plaintiffs have plausibly alleged that irrevocable liability attached when they entered into the Terms of Use with [the exchange], placed their purchase orders, and sent payments from the United States.” The court noted that pursuant to the exchange’s Terms of Use, plaintiffs’ buy orders became irrevocable when they were sent. The court explained that “we have particular reason to consider other factors that our cases have found relevant to the irrevocable liability analysis” because the exchange disclaims having any physical location. Under these circumstances, the court explained that it would consider “facts concerning the formation of the contracts, *the placement of purchase orders*, the passing of title, or the exchange of money to determine when and where an investor becomes irrevocably bound to complete a transaction.”

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