

Corporate Update

CORPORATE FINANCE

New York AG as Global Crypto Cop

By Jeffrey Alberts

March 30, 2023

The New York Attorney General has recently filed a series of aggressive cases against companies based outside the United States for offering cryptocurrency services to New York residents in a manner that allegedly violates New York law. For example, the AG filed actions in February 2023 against CoinEx and in March 2023 against KuCoin based on these companies allegedly offering cryptocurrency tokens for sale in New York.

While the AG describes its actions as part of an effort to “protect New York investors,” its allegations focus not on harm the foreign companies actually caused investors, but rather on the companies’ failure to comply with various registration requirements, including registering with the state of New York.

Many commentators have questioned whether these actions are valid under New York law, but in this article I would like to consider a different question: Is it in the interest of New Yorkers for the New York AG to aggressively litigate

against foreign companies for violating New York state registration requirements?

After all, if New York can initiate such actions against Chinese companies for failing to register in New York, Guangdong provincial authorities may someday initiate similar actions against New York companies for violations of Guangdong regulations.

Will New Yorkers benefit from an environment in which local governments around the world aggressively impose local regulations on foreign companies?

The AG’s Action Against CoinEx

On Feb. 22, 2023, the AG initiated an action against VINO GLOBAL LIMITED d/b/a COINEX, seeking a permanent injunction, an accounting, restitution, disgorgement, costs, and an order directing CoinEx to implement geo-blocking of New York residents.



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According to documents that the AG submitted to the court, CoinEx was founded in 2017 by Haipo Yang, who holds a Chinese passport and does business in China. CoinEx itself was headquartered in Hong Kong. The AG alleges that people located in over 200 countries and regions used CoinEx's cryptocurrency exchange services.

As to the state of New York, the AG alleges that New York residents were able to exchange four specific cryptocurrency tokens with CoinEx.

The AG further alleged that several of these cryptocurrencies were securities and/or commodities, and therefore offering to sell these cryptocurrencies in New York state required CoinEx to register with the Office of the Attorney General of the State of New York as a commodity broker-dealer and a securities broker-dealer.

The AG also alleged that CoinEx violated the Martin Act by representing itself as an "exchange," when it was not a properly registered securities exchange or commodities exchange.

State Regulatory Overreach?

There are several aspects of the AG's actions that New Yorkers would be likely to view as troubling if the same actions had been taken by a foreign local government against a company based in New York.

First, the AG's allegations do not suggest a concerted effort on the part of CoinEx to target the New York market. The AG does not suggest that CoinEx employs New Yorkers or has offices in New York. The AG does not allege, or rely on, New York residents being a significant percentage of CoinEx's business. Neither does the AG suggest that CoinEx targeted advertising specifically to New York.

The AG's allegations that CoinEx offered to sell tokens in New York appears to be based primarily

on the fact that CoinEx advertised on the world wide web, which can be accessed in New York, and that a New York law enforcement agent was able to open a CoinEx account and engage in a cryptocurrency exchange while located in New York. However, the affidavit submitted by this agent suggests that he did not reveal to CoinEx that he was located in New York and did not purchase cryptocurrency with funds from a bank account in the United States.

A New York company that exchanged cryptocurrencies or blockchain tokens, such as an NFTs, with customers that included residents of a spe-

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cific Chinese province, might well disagree that this should subject them to registration requirements imposed by that Chinese province (especially if, as with registration as a securities exchange, such registration subjects the company to expensive and complex additional regulatory requirements).

Second, the AG's suggestion that CoinEx harmed New York consumers are fairly speculative; they are not the sort of actions that would necessarily appear inherently harmful to a foreign company. For example, the AG alleges that CoinEx "wrongfully represented" itself as a cryptocurrency exchange. However, the AG appears to allege that CoinEx was acting as a cryptocurrency exchange.

What made CoinEx's representation "wrongful," according to the AG, was that CoinEx was not properly registered as a securities exchange or a

commodities exchange. The AG does not allege that CoinEx lied about whether it was registered as an exchange in New York or in the United States.

Similarly, the AG does not allege that CoinEx failed to provide the cryptocurrency services that New Yorkers asked it to perform, or even suggest that it performed those services poorly.

Third, the AG relies on CoinEx's alleged failure to send an employee to New York to testify under oath in response to a subpoena as "prima facie proof that CoinEx has engaged in the fraudulent practices" set forth in the AG's petition.

While there is some legal basis for position, many New Yorkers would be disappointed to learn that a Chinese provincial authority was employing a similar assumption against New Yorkers who chose not to fly to China to testify under oath in Chinese legal proceedings related to registration requirements in a province of China.

Fourth, several of the AG's alleged violations relate specifically to requirements unique to the state of New York. This not only extends to allegations that CoinEx did not register in the state of New York, it also involves applying New York-specific interpretations of widely used legal concepts such as that of a "security."

For example, in addition to relying on the interpretation of a "security" set forth by the U.S. Supreme Court in *S.E.C. v. Howey Co.*, 328 U.S. 293 (1946), the AG independently relies on an even older New York state court decision *In re Matter of Waldstein*, 160 Misc. 763, 767-68 (Sup. Ct, Albany Co. 1936).

The AG's position appears to be that even if the cryptocurrency tokens sold by CoinEx were

not securities under U.S. law, they were securities under New York law. This may be entirely appropriate as a matter of New York law, but again a New York company that understood that it was not required to register something it was selling under the law of China likely would think it was unfair for a Chinese provincial authority to announce that it was interpreting the same word that appeared in a national statute in a different way, relying on a 90-year-old provincial court decision. (I am not suggesting that there is such a distinction in Chinese law; I use the example of China based solely on the CoinEx founder allegedly being a Chinese passport holder.)

Principled Precedent?

Of course, the fact that New York companies might not want to be subject to Chinese law when they sell to Chinese residents does not mean that they should be able to simply ignore that law.

Both China and the United States have a right to protect their citizens from unscrupulous actions by foreign companies. However, one has to ask whether the best way to develop law and regulations that will protect a country's residents who participate in international commerce is through enforcement actions taken by state and provincial authorities based on aggressive interpretations of decades-old state and provincial court decisions.

At some point, New Yorkers are likely to be on the receiving end of such justice, and when that happens, they may well regret the precedent set by the AG's recent actions.