

How Ripple Final Judgment Fits In Broader Crypto Landscape

By **Joanna Wasick, Robert Musiala and Teresa Goody Guillén** (September 3, 2024)

On Aug. 7, the U.S. District Court for the Southern District of New York issued its judgment in U.S. Securities and Exchange Commission v. Ripple Labs Inc., marking the end — for now — of district court proceedings in the highly watched litigation.[1]

The court declined to impose disgorgement and prejudgment interest, but it imposed a \$125,035,150 civil penalty on Ripple for its securities law violations — an amount far less than the approximately \$2 billion sought by the SEC as the total amount of civil penalty, disgorgement and prejudgment interest.

The court also issued a permanent injunction prohibiting Ripple from violating Section 5 of the Securities Act by selling a security in the absence of an exemption or an effective registration statement. When read with the court's summary judgment decision, this injunction should not preclude Ripple from selling XRP — the native token on the Ripple blockchain — through blind programmatic sales or paying XRP to third parties as compensation.

The case will likely be appealed, and a number of external factors may affect the overall impact of the holding on the digital assets industry, including ongoing cases in other federal courts and potential lawmaking being considered by Congress and the executive branch.

The judgment marks a milestone in the case and solidifies key holdings from the court's July 13, 2023, summary judgment decision.[2]

The Ripple Final Judgment

In December 2020, the SEC sued Ripple and two of its executives, Bradley Garlinghouse and Christian Larsen, alleging that their sale of XRP constituted unregistered offers and sales of securities that violated provisions of the Securities Act.

In its decision on the parties' motions for summary judgment,[3] the court classified the XRP transactions at issue into four distinct categories and applied the test derived from the U.S. Supreme Court's 1946 decision in SEC v. W. J. Howey Co. to each category to determine whether each was an investment contract and which is a type of security under federal securities laws.

Specifically, the court held that

- Ripple's institutional sales of XRP pursuant to written contracts to known institutional purchasers, such as hedge funds, on-demand liquidity customers and other institutional buyers, were investment contracts;



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- Ripple's programmatic sales of XRP on digital asset exchanges, which were both blind (i.e., neither Ripple nor the buyer knew the other's identity) and programmatic (e.g., sold through the use of trading algorithms) were not investment contracts;
- Ripple's payment of XRP to third parties, such as to employees as compensation and to developers to further develop the ecosystem, were not investment contracts; and
- Blind sales of XRP on digital asset exchanges by the Ripple executives in their individual capacities were not investment contracts.

The court thus granted summary judgment to the SEC on claims against Ripple based on the first category of transactions, but granted summary judgment to the defendants on claims based on the other three.[4]

The court's final judgment imposed a permanent injunction prohibiting Ripple and "other persons in active concert or participation" with Ripple from selling any security without an exemption or an effective registration statement. Read in the context of the court's summary judgment, the injunction effectively prohibits Ripple and affiliated persons from engaging in further institutional sales — through formal contracts with known sophisticated buyers — of XRP unless the sales are specifically treated as sales of securities and comply with Section 5 of the Securities Act.

The injunction does not apply to the other categories of XRP sales, which the court previously found were not investment contracts. The court's final judgment also imposed a \$125,035,150 civil penalty on Ripple for its securities law violations related to its institutional sales of XRP.

Of note, the court did not address Ripple's ongoing sales of XRP through its on-demand liquidity service, but it did consider them in deciding to issue the permanent injunction. In doing so, the court found that those sales demonstrated "Ripple's willingness to push the boundaries of the [summary judgment] Order[, thus] evinc[ing] a likelihood that it will eventually (if it has not already) cross the line." Should those ongoing sales be found to be investment contracts, they may constitute Section 5 violations themselves and a violation of the permanent injunction.

Now that the judgment is entered, the SEC — which tried and failed to appeal on an interlocutory basis after the summary judgment decision — will likely file an appeal to the U.S. Court of Appeals for the Second Circuit. Ripple may also seek to appeal the court's ruling on institutional sales.

Impact on the Digital Assets Industry

The judgment will have a broad impact on the continuing development of U.S. digital assets law. Regardless of how the law develops, the Ripple district court decision was the first to hold that blind sales and blind programmatic sales of digital assets are not securities, even

if deemed securities in other circumstances. And it has already been explicitly relied upon by another district court outside the Second Circuit that rendered a similar decision — the U.S. District Court for the District of Columbia's June 28 decision in SEC v. Binance, which read, "The Court is inclined to agree with the approach of the court in Ripple Labs."

More developments are sure to come. In brief, all three branches of the U.S. government are now actively grappling with the issues at stake in SEC v. Ripple. This means that in addition to the likely appeal to the Second Circuit, the Ripple holding's effect on the digital asset industry may be affected by a number of parallel actions currently happening in the judicial, legislative and executive branches.

Three key pending cases are SEC v. Coinbase Inc.,^[5] SEC v. Binance Holdings Ltd.^[6] and SEC v. Payward Inc.^[7] In all three cases, the SEC brought charges against major U.S. cryptocurrency exchanges alleging violations of the U.S. securities laws. In all three cases, the SEC's claims arising out of secondary market token sales survived motions to dismiss.

The key events in each will occur after discovery, when the parties likely move for summary judgment and the respective court issues a decision that could either support, contradict or distinguish the Ripple court's ruling that Ripple's blind programmatic sales and individuals' blind sales of XRP on digital asset exchanges were not investment contracts.

SEC v. Coinbase

The SEC's 2023 complaint against Coinbase in the Southern District of New York — the same court as SEC v. Ripple — alleges that since 2019, Coinbase has operated as an unregistered broker, unregistered exchange and unregistered clearing agency in violation of the Exchange Act, and that through its "staking" program, Coinbase offered and sold unregistered securities in violation of the Securities Act.^[8] The SEC's allegations hinge on its argument that at least some of the digital asset transactions on Coinbase's platform and through related services constitute "investment contracts."

In March 2024, the district court issued a decision denying in part Coinbase's motion for judgment on the pleadings, and finding that the SEC sufficiently alleged that Coinbase operated as an unregistered intermediary of securities and engaged in the unregistered offer and sale of securities through its staking program. In a victory for Coinbase and the crypto industry, the court dismissed the SEC's claim that Coinbase acted as an unregistered broker by making its unhosted wallet software available to customers.

SEC v. Binance

Similar to its action against Coinbase, in SEC v. Binance,^[9] the commission alleged that Binance violated the Securities Act and the Exchange Act by offering and selling digital assets without a registration statement and operating digital asset trading platforms without registering as an exchange, broker-dealer or clearing agency.^[10]

On June 28, the D.C. district court issued an opinion and order granting in part and denying in part Binance's motion to dismiss. Here, the court found that the SEC had sufficiently pled that initial and subsequent sales of tokens that the defendant issued itself — i.e., BNB — were investment contracts when sold by the defendant.

However, the court explicitly agreed with the reasoning applied in Ripple and rejected the SEC's argument that if a token sold in an initial sale is an investment contract, so too are sales of the same token to the secondary market. It thus found that the SEC had not pled

that sales of BNB by secondary market participants were investment contracts.

However, the court did conclude that the SEC plausibly alleged that the defendant's staking and vault programs were offered and sold as investment contracts, and that, therefore, the SEC plausibly alleged the defendant failed to register as an exchange, broker-dealer and clearing agency. The court declined to address whether sales of non-BNB tokens on the defendant's exchange were investment contracts as well.

SEC v. Payward

Finally, in SEC v. Payward, the SEC filed a complaint on Nov. 20, 2023, in the U.S. District Court for the Northern District of California, alleging — similar to its allegations in Coinbase and Binance — that the crypto exchange Kraken, Payward's commercial name, violated the Exchange Act by operating a digital asset trading platform without registering as an exchange, broker-dealer or clearing agency.[11]

The court denied Payward's motion to dismiss in full. In its Aug. 23 decision, the court emphasized that the analysis for whether a secondary market transaction constitutes an offer or sale of an investment contract is the same as the analysis for primary market sales. In both instances, the "determinative factor" is not the platform on which the sale was made — e.g., an exchange — but rather "the reasonable expectations of the individual initiating the transaction" as shown in the totality of the circumstances and the economic reality of the transaction.

The court found that the SEC plausibly alleged that the investors in the tokens offered on Kraken possessed an expectation of profits from the efforts of others that they derived from the promoters' representations that Kraken republished and reasserted on its platform. However, the court noted that "[w]hether or not the record ultimately supports that allegation will be revealed through discovery."

If one, two, or all three of SEC v. Coinbase, SEC v. Binance, and SEC v. Payward reach final judgment, the cases will affect digital assets case law, similar to SEC v. Ripple. And the district court decisions may be ultimately upended if appealed to the U.S. Courts of Appeals for the Second Circuit, District of Columbia Circuit and Ninth Circuit, respectively. These judgments and appeals may very well all occur during a pending appeal in SEC v. Ripple.

Legislative and Executive Branch Initiatives

Simultaneous with the above court cases, Congress is currently considering multiple introduced and draft bills that would define the legal status of digital assets in various contexts.

These include the Financial Innovation and Technology for the 21st Century, or FIT21, Act; the Payment Stablecoin Act; draft cryptocurrency legislation authored by retiring Sen. Debbie Stabenow, D-Mich., chair of the Senate Agriculture, Nutrition and Forestry Committee, which has jurisdiction over the U.S. Commodity Futures Trading Commission; and legislation to expand application of the Bank Secrecy Act, anti-money laundering and know-your-customer regimes to the crypto industry.

It would be challenging for Congress to act on one or more of these bills after the November election, even with the recent and very public support of the crypto industry by Senate Majority Leader Chuck Schumer, D-N.Y., as Congress is scheduled to be in session for approximately 24 days after the election until the end of the year.

The FIT21 Act is particularly notable because it passed the House of Representatives in May with a strong bipartisan vote of 279-136, including 71 votes from Democrats. The Payment Stablecoin Act may also gain momentum in 2025 due to the recent passage of the European Union's Markets in Crypto-Assets regulation, which, among other things, created a regulatory framework for fiat-backed stablecoins in the EU that became effective in June.

The outcome of the upcoming U.S. presidential and congressional elections may also alter the crypto agenda in Congress and will likely affect the stance that the SEC, the CFTC and other executive agencies take toward the crypto industry. These developments in the legislative and executive branches may very well play out in 2025 as the SEC v. Ripple, SEC v. Coinbase, SEC v. Binance and SEC v. Payward cases proceed in the federal courts.

There could also be new SEC and CFTC chairs and a change in the SEC's litigation strategy depending on the outcome of the presidential election.

Crypto Marches On

The Ripple judgment means that Ripple — one of the most successful and well-capitalized crypto companies in the U.S. — is able to continue expanding its business both in the U.S. and abroad. While the future of digital assets law in the U.S. remains murky, it is clear that the crypto industry will maintain its fast pace of evolution and push the boundaries of technology, finance and law.

As the industry continues to innovate, legal professionals and all three branches of government will have ongoing opportunities to help shape the future of digital assets and Web3.

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[1] SEC v. Ripple Labs Inc., No. 20 Civ. 10832 (AT), 2024 WL 3730403 (S.D.N.Y. Aug. 7, 2024).

[2] SEC v. Ripple Labs Inc., 682 F. Supp. 3d 308 (S.D.N.Y. 2023).

[3] <https://www.bakerlaw.com/insights/ripple-decision-makes-waves-finding-some-xrp-sales-not-securities/>.

[4] Note that the court had found there was a genuine issue of material fact precluding summary judgment on the SEC's aiding and abetting claims against Larsen and Garlinghouse; however, the parties subsequently stipulated to dismissal of those claims in October 2023.

[5] <https://www.sec.gov/newsroom/press-releases/2023-102>.

[6] <https://www.sec.gov/newsroom/press-releases/2023-101>.

[7] <https://www.sec.gov/newsroom/press-releases/2023-237>.

[8] SEC v. Coinbase Inc., No. 23 Civ. 4738 (KPF), 2024 WL 1304037 (S.D.N.Y. March 27, 2024).

[9] SEC v. Binance Holdings Limited, No. 23-1599 (ABJ), 2024 WL 322974 (D.D.C. June 28, 2024).

[10] Binance also involves several issues that are not raised in Coinbase or Ripple.

[11] Order, SEC v. Payward Inc., No. 23-cv-06003-WHO, ECF 90 (N.D. Cal. Aug. 23, 2024).