



July 14, 2023

## COURT DELIVERS SPLIT-DECISION ON RIPPLE

A federal judge has delivered a split-decision on the Ripple Labs XRP token, providing some mixed clarity on the question of whether digital tokens are or can be securities. *SEC v. Ripple Labs, Inc.*, No. 1:20-cv-10832-AT-SN (S.D. N.Y., filed July 13, 2023). Judge Torres concluded that an XRP token is a security when sold by Ripple directly to sophisticated institutional investors capable of understanding that such tokens are “speculative value propositions,” meeting the test for an “investment contract,” but not a security when sold to “programmatically investors” (the broader public) on secondary markets (digital asset exchanges). Judge Torres noted that many statements cited by the Securities Exchange Commission (“SEC”) may not have been shared with the general public who might not know whether they were buying from Ripple or third parties in an even (bid/ask) exchange. (Additional XRP were distributed in various contexts for goods or services or as funding for initiatives.)

The SEC alleged that the defendants violated Section 5 of the Securities Act of 1933 by selling XRP as an “investment contract”, a form of security. In citing the controlling test from *SEC v. W.J. Howey Co.*, Judge Torres noted that the Supreme Court held that under the Securities Act, an investment contract is “a contract, transaction[,] or scheme whereby a person [(1)] invests his money [(2)] in a common enterprise and [(3)] is led to expect profits solely from the efforts of the promoter or a third party” (328 U.S. 293, 298–99 (1946) (emphasis added)) and that in analyzing whether a contract, transaction, or scheme is an investment contract, “form should be disregarded for substance and the emphasis should be on economic reality” and the “totality of circumstances” (*Tcherepnin v. Knight*, 389 U.S. 332, 336 (1967)). Judge Torres concluded that, based on the totality of circumstances, reasonable institutional investors would have purchased XRP with the expectation that they would derive profits from Ripple’s efforts insofar as they reasonably expected that Ripple would use the capital it received from its sales to them to improve the XRP ecosystem and thereby increase the price of XRP. The general public, however, could not reasonably expect the same insofar as they did not know whether their payments went to Ripple to support Ripple’s efforts or went to a disinterested third party. (Other distributions of XRP failed the “investment of money” prong of the Howey test insofar as no money or other

tangible and definitive consideration was exchanged.)

This public/institutional investor distinction may help lift the cloud hanging over similar digital tokens in the marketplace and allow for a greater adoption of digital tokens as payment options. See, e.g., our ALERTS of [April 15, 2022](#); see also *The Cryptocurrencies on Their Way to Becoming a Trust Payment Alternative?*, 38 BANKING & FIN. SERV. REP., (Jan. 2019); *Virtual Currency: A Commodity, Property, Security or Payment Substitute?*, 37 BANKING & FIN. SERV. REP., (July 2018). Shortly after the *Ripple* decision was issued, Coinbase, the largest U.S. digital asset exchange, started trading XRP on its platform.

✧ *Mike Tomkies and Mercedes Ramsey*

**LOOKING FOR A STATE LAW CREDIT CARD COMPLIANCE RESOURCE?** We publish an easy-to-use online reference that summarizes state consumer lending and other consumer protection laws. Our CREDIT CARD DIGEST is organized topically, covers laws applicable to credit card programs of federally and state-chartered financial institutions from an out-of-state issuer perspective and includes an analysis of statute applicability. Card issuers, marketers, servicers and merchants should find this an invaluable resource for program development and regulatory compliance. **Contact us for details.**

Darrell L. Dreher  
[ddreher@dtlaw.com](mailto:ddreher@dtlaw.com)

Elizabeth L. Anstaett  
[eanstaett@dtlaw.com](mailto:eanstaett@dtlaw.com)

Mercedes C. Ramsey  
[mramsey@dtlaw.com](mailto:mramsey@dtlaw.com)

Susan L. Ostrander  
[sostrander@dtlaw.com](mailto:sostrander@dtlaw.com)

2750 HUNTINGTON CENTER  
41 S. HIGH STREET  
COLUMBUS, OHIO 43215  
TELEPHONE: (614) 628-8000 FACSIMILE: (614) 628-1600  
[WWW.DTLAW.COM](http://WWW.DTLAW.COM)

To see previously sent ALERTS, visit our website at [www.dtlaw.com](http://www.dtlaw.com)

To decline future ALERTS, please contact us at [ALERTS@DLT.LAW.COM](mailto:ALERTS@DLT.LAW.COM). This ALERT has been prepared for informational purposes only. It does not constitute legal advice and does not create an attorney-client relationship.

Michael C. Tomkies  
[mtomkies@dtlaw.com](mailto:mtomkies@dtlaw.com)

Judith M. Scheiderer  
[jscheiderer@dtlaw.com](mailto:jscheiderer@dtlaw.com)

Robin R. De Leo  
[robin@deher-la.com](mailto:robin@deher-la.com)