SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK

THE PEOPLE OF THE STATE OF NEW YORK, by LETITIA JAMES, Attorney General of the State of New York, Plaintiff, - against - COINSEED, INC., DELGERDALAI DAVAASAMBUU, and SUKHBAT LKHAGVADORJ, Defendants.	Index No.: 450366/2021

PLAINTIFF'S MEMORANDUM OF LAW IN SUPPORT OF ORDER TO SHOW CAUSE FOR A TEMPORARY RESTRAINING ORDER AND PRELIMINARY INJUNCTION AND APPOINTMENT OF A RECEIVER

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Plaintiff Letitia James, Attorney General of the State of New York ("OAG"), respectfully submits this memorandum of law and the accompanying Affirmation of Brian M. Whitehurst ("Whitehurst Aff.") dated May 6, 2021, with exhibits,[1] in support of her order to show cause for a temporary restraining order ("TRO"), a preliminary injunction, and the appointment of a receiver.

PRELIMINARY STATEMENT

OAG is seeking a TRO, a preliminary injunction, and the appointment of a receiver to stop Defendants from engaging in continuing fraud and dissipating the assets of investors. OAG filed an action against Coinseed, Inc. ("Coinseed") and its founder and Chief Executive Officer Delgerdalai Davaasambuu ("Davaasambuu," together with Coinseed "Defendants") on February 17, 2021 after an extensive investigation.[2] OAG has alleged that Defendants conducted an unlawful securities offering, made material misrepresentations to investors about the fees they charged, and the identity and qualifications of the management team, and, over the course of three years, have been investing in and trading commodities in the form of virtual currencies on behalf of their clients without having registered with the State of New York as commodity broker-dealers in violation of General Business Law ("GBL") § 359-e(14) and Executive Law § 63(12).

Since OAG filed the Complaint in this action, Defendants' unlawful conduct has continued. Following the Complaint, Defendants have made unauthorized trades, putting all investors' holdings into virtual currencies that at the time were declining in value, and have prevented the victims from withdrawing any of their funds. In addition, new evidence shows that, in the months leading up to the Complaint, Defendants drained both bank and virtual

[1] Citations herein to "Ex. _" refer to exhibits attached to the Affirmation of Assistant Attorney General Brian M. Whitehurst submitted in support of this Order to Show Cause.

[2] Sukhbat Lkhagvadorj, the former Chief Financial Officer of Coinseed, is also a Defendant in this action by OAG. On April 6, 2021, OAG and Mr. Lkhagvaadorj entered into a settlement agreement which was submitted to the Court (NYSCEF No. 26), and is *sub judice*.

currency accounts that held investor deposits and moved investor assets overseas. To locate and safeguard investor assets, as well as to protect investors from further harm, OAG is seeking a TRO, a preliminary injunction, and the appointment of a receiver.

In the past two months, OAG has received over 130 complaints from investors who have lost access to and control over years of investments and gains due to the Defendants' fraudulent conduct. Investors who weeks ago had portfolios worth over $150,000, now cannot withdraw those gains. Further, the Defendants, without authorization, moved every investors' holdings into one single, extremely volatile virtual currency (named Dogecoin) which rises and falls dramatically in price in a matter of hours on any given day. And still, the Defendants have completely cut off investors' ability to trade in their accounts, withdraw their funds, or otherwise avoid further losses.

To prevent further dissipation of assets and pursuant to GBL § 353-a, OAG asks this Court to issue an order appointing a receiver of all property derived by the Defendants by means of their fraudulent practices, all property that has been comingled with Defendants' property, and ordering Defendants to provide the receiver with all books of account and papers relating to the same.[3] In addition, OAG seeks a TRO ordering Defendants to: (1) halt the offering or selling of commodities and securities, (2) cease all trading, (3) preserve all fiat and virtual currency assets, and (4) preserve all evidence related to this action.

OAG has a strong likelihood of success on the merits in this matter. Defendants operated as unregistered commodity broker-dealers for years in violation of New York law. The absence of a preliminary injunction would result in irreparable harm[4] as Defendants continue to violate the law. Without authorization, and after the filing of the Complaint, Defendants converted investor assets in to a virtual currency that is susceptible to extreme volatility. They did this after

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[3] OAG has identified a potential receiver willing to serve on a pro bono basis to aid the Court.

[4] As discussed herein, the Martin Act and Executive Law § 63(12) have differing standards for preliminary relief in that there is no requirement under § 63(12) of irreparable harm. *See People v. Apple Health & Sports Clubs, Ltd.*, 174 A.D.2d 438, 438-39 (1st Dep't 1991).

secreting investor assets in the run-up to the filing of the Complaint. The balance of equities is squarely in OAG's favor. *See State v. First Investors Corp.*, 156 Misc. 2d 209, 213 (Sup. Ct. N.Y. Cnty. 1992).

I. STATEMENT OF FACTS

A. Defendants Operate an Unregistered Commodity Broker-Dealer

On February 17, 2021, OAG filed a Complaint against Defendants for committing violations of the Martin Act and Executive Law § 63(12) by unlawfully offering and selling securities, unlawfully operating as commodity broker-dealers, and making false and misleading statements about the amount of fees charged and the composition of its management team. (Whitehurst Aff. ¶ 3, *See* "Complaint" NYSCEF No. 2)[5] After the filing, OAG began receiving complaints from investors reporting that Coinseed disabled all withdrawals. (*Id.* ¶ 16.)

Coinseed, a Delaware corporation with its principal place of business in New York (*See* Ex. A) was created by Davaasambuu in or around October 2017. (*Id.* ¶ 7.) Coinseed, a virtual currency investing mobile application, allows investors to round up everyday purchases made on their debit and credit cards and use those extra cents to make micro investments into virtual currencies. (*Id.* ¶ 8.) After an investor establishes an account within the application and links a bank account, Coinseed tracks the investors' debit and credit card purchases. (*Id.*) Once the "round ups" total a minimum dollar threshold the investor's linked bank account is debited and then used to purchase the virtual currency of the investor's choice. (*Id.*)

To convert the U.S. dollar ("USD" or "fiat currency") deposits made by investors into virtual currency, Defendants utilize Gemini, a New York based virtual currency trading platform.

[5] Citations to "Whitehurst Aff. ¶ __." refer to the Affirmation of Assistant Attorney General Brian M. Whitehurst, submitted in support of this Order to Show Cause.

(*Id.* ¶ 9, *See* Ex. C.) On behalf of investors and at investors' direction, Defendants purchased and traded virtual currencies such as bitcoin, litecoin, and ether, amongst others. (*Id.* ¶ 10.) These virtual currencies are commodities under New York law. (*Id.* ¶ 11.) *See* *Matter of James v. iFinex Inc.*, 185 A.D.3d 22, 28 (1st Dep't 2020). Defendants operate as commodity broker-dealers because they trade or sell commodities. (*Id.*, *See* Ex. D.) To be able to trade or sell commodities from or within New York, Defendants are required to register as a commodity broker-dealer with OAG. (*Id.* ¶ 12.) Defendants failed to register as commodity broker-dealers with OAG. (*Id.*, *See* Ex. E.)

Since June 2018, Defendants, on behalf of at least 3,000 investors, including residents of New York State, have deposited at least $1.2 million into Gemini. (*Id.* ¶ 13.) That $1.2 million, through investments into virtual currency, has grown to more than $10 million in value. (*Id.* ¶ 35.)

B. Defendants Limit and then Completely Disable Investor Withdrawals When Investors See Significant Gains in Their Portfolios

In the ordinary course, Defendants trade virtual currencies on behalf of investors, but the investors do not take possession of the virtual currency. (Whitehurst Aff. ¶ 14.) If an investor wants to access or withdraw his/her virtual currency, then he/she must make a USD withdrawal request in the Coinseed mobile application. (*Id.*) Defendants will then satisfy that request by transferring USD from a Coinseed bank account to the investor's bank account.[6] (*Id.*)
Over the past months, the value of bitcoin, and nearly every other virtual currency, has increased exponentially. (*Id.* ¶ 15.) On December 15, 2020, the price of bitcoin was approximately

[6] When there is not a sufficient amount of USD in the bank account to satisfy investor withdrawals, Defendants have the ability to convert virtual currency held on behalf of investors into fiat currency in order to satisfy the investor withdrawal. (Whitehurst Aff. FN 1.)

$19,200 and by February 15, 2021 it rose to over $48,000. (*Id.*) During this same time-period, and since, Coinseed saw an influx of withdrawal requests from investors seeking to realize gains. (*Id.*) Rather than convert virtual currency to fiat currency to honor these requests, Defendants first reduced the daily withdrawal limit from $1,000 a day to $250 a day, and then ultimately disabled withdrawals altogether. (*Id.*)

After initiating this action, OAG received dozens of complaints from investors telling the same story – that Defendants were prohibiting investors from withdrawing their assets. (*Id.* ¶ 16.) For example:

- On February 24, 2021, an investor filed a complaint with OAG stating that since February 18, 2021 he had been trying to withdraw funds from his account, but Coinseed would not honor his withdrawal requests. He reported that he reached out to Coinseed at least ten times about his inability to withdraw, but received no response. (*Id.*)

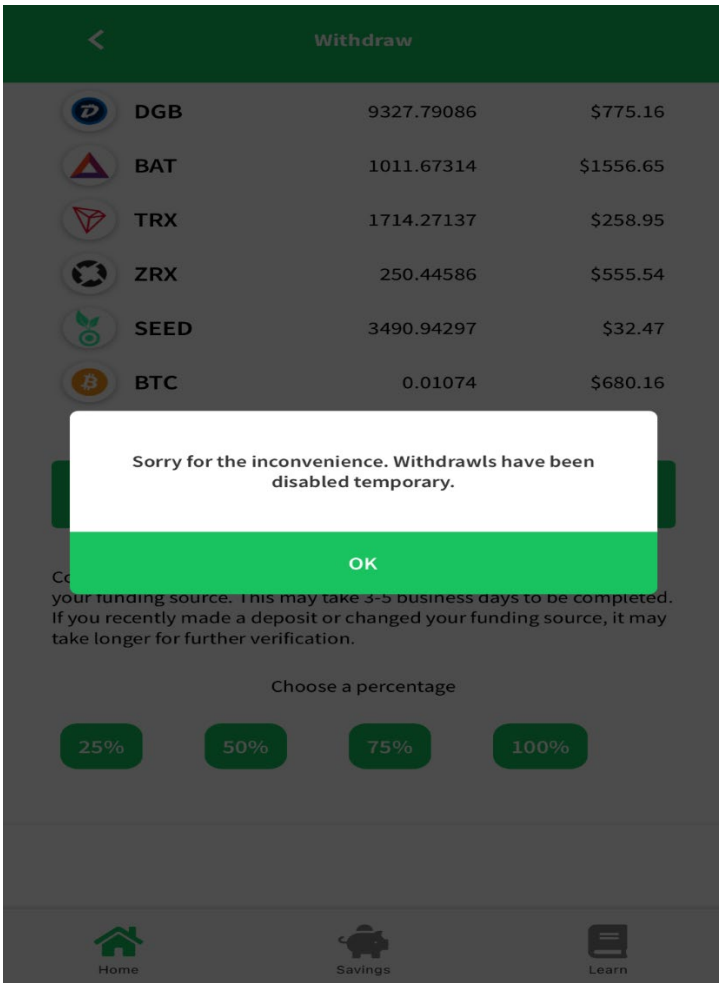
- On March 8, 2021, OAG spoke with an investor who had seen his total investment of $4,500 grow to $14,000, and on January 26, 2021 he was able to make a single withdrawal of $250. After that, his withdrawal requests remained pending, and then withdrawals were "disabled." (*Id.*)

- On March 16, 2021, an investor informed OAG that he had been unable to withdraw any of the value of his investment which totaled $18,000. (*Id.*)

- On March 31, 2021, an investor with about $10,000 deposited into Coinseed, which had a value of $50,000, could not withdraw any funds. (*Id.*)

- On April 15, 2021, an investor who had been using Coinseed since 2018 and deposited around $11,270 was unable to withdraw any of his current $95,405 balance. The investor contacted Coinseed support about the inability to withdraw, but those inquiries went unanswered. (*Id.*)

Of the investors OAG interviewed, all of them reported that whenever they initiated a withdrawal request in the mobile application, a pop-up would appear stating "Withdrawls have been disable temporary" (sic). (*Id.* ¶ 17.)



Numerous investors made multiple attempts to contact Coinseed through the support@coinseed.co email address, to which not a single investor interviewed by OAG had received a response. (*Id.*)

C. Defendants Engage in Unauthorized Transactions and Remove all Functionality from the Application

In addition to disabling withdrawals, Defendants also disabled all trading by investors and engaged in unauthorized trading in investors' accounts. (Whitehurst Aff. ¶ 19, *See* Ex. G.) On its website, Coinseed states: "[Our] Services allow you to open an account to participate that we will manage at your direction" (sic) and further represented that "Coinseed and Coinseed Inc. provide self-directed investors with cryptocurrency services, and does not make

recommendations or offer investment advice of any kind." (*Id.* ¶ 20.) Coinseed has no discretionary authority to trade in investors' accounts. (*Id.* ¶ 19.)

On April 16, 2021, Defendants - without notice or authorization - converted all investor assets into bitcoin, notwithstanding the investor's selection of virtual currency. (*Id.* ¶ 21.) At the same time, Defendants disabled all functionality in the application, so that in addition to not being able to withdraw their money, investors could not even trade out of bitcoin into another virtual currency. (*Id.* ¶ 19.)

Later in the evening on April 16, 2021, Defendants executed another unauthorized trade in all investor accounts. (*Id.* ¶ 22.) Defendants traded the bitcoins for an extremely volatile virtual currency named Dogecoin, which was experiencing a sharp decline in value at that time. (*Id.*)

The unauthorized trades into Dogecoin, executed when it was experiencing a large drop in price, caused investors to lose significant amounts of value from their account balances. (*Id.* ¶ 23.) One complainant reported to OAG that, as a result of the unauthorized trade, his account balance fell from $115,000 to $80,000 – which was a loss at the time of over 30 percent. (*Id.*)

Since April 16, 2021, OAG has received dozens of complaints from investors describing that Defendants conducted these unauthorized trades and transferred all investor assets into Dogecoin. (*Id.* ¶ 24.) The complainants repeatedly stated concerns about losses of their investments, the continued inability to trade, and the ongoing failure of Coinseed to honor withdrawal requests. (*Id.*) For example:

- On April 17, 2021, OAG received a complaint from an investor that Coinseed transferred all his cryptocurrency to Dogecoin without his permission and blocked his ability to withdraw his money. He wrote that he had a $20,000 balance the night before, and the transfer to Dogecoin immediately dropped his balance to $7,000. He was also concerned about his inability to withdraw money and that Coinseed would not respond to his messages. (*Id.*)

- On April 17, 2021, an investor who had a $15,163.97 balance on Coinseed informed OAG that when he attempted to rebalance his investment into Bitcoin Cash, he realized that his holding had been sold without his approval into bitcoin. The next day everything was in Dogecoin. According to the investor, he did not approve or initiate either of these transactions. When he attempted to withdraw his funds, the app informed him that "withdraws [sic] temporarily suspended." (*Id.*)

- On April 18, 2021, an investor informed OAG that he had been using Coinseed since January 2018, and invested approximately $3,800 since that time. The investor had a diverse virtual currency portfolio on Coinseed, including bitcoin, ether, Cardano, and Monero, which grew in value to $24,110 by April 16, 2021. According to the investor, when he logged into his account on April 17, 2021 he saw that without his knowledge or consent, his portfolio had been converted entirely into Dogecoin. This unauthorized transaction caused his balance to fall from $21,400 to around $18,000. The investor also stated that he had been unable to withdraw any of his balance for a few months. (*Id.*)

- On April 18, 2021, an investor informed OAG that over the course of three years he had invested $9,420 into virtual currency through the Coinseed application. On April 16, 2021, his portfolio of bitcoin, ether and Digibyte had grown his account balance to around $45,000. However, according to the investor, on the evening of April 16, 2021, without his permission, Coinseed converted all his holdings to Dogecoin, and the ability to sell or trade currencies were disabled too, leaving the application essentially not functional. (*Id.*)

- On April 28, 2021, an investor submitted a complaint to OAG stating that his entire portfolio, worth over $3,000, had been converted to Dogecoin without his consent. He reported that withdrawals were disabled so he could not access his funds. (*Id.*)

Investors expressed concern about the value of their portfolios due to the unauthorized trades made by Defendants and complained about not being able to safeguard their assets. (*Id.* ¶ 25.) Withdrawals remain disabled by Defendants, and Defendants have failed to restore any functionality to the application, leaving investors unable to trade out of Dogecoin. (*Id.*)

D. Defendants Raid Bank and Virtual Currency Accounts

New evidence additionally shows that Defendants' payment provider terminated its relationship with Coinseed (due to, amongst other things, Coinseed's refusal to honor customer withdrawals). (Whitehurst Aff. ¶ 26.) Defendants also withdrew all remaining USD out of its

corporate bank account, and converted most of the USD into bitcoin and moved the rest to unknown accounts. (*Id.*) Additionally, they moved all remaining virtual currency out of the Coinseed account at Gemini to a foreign, unregulated virtual currency trading platform. (*Id.*)

Since at least 2018, Coinseed contracted with a third-party software provider, Synapse Financial Technologies, Inc. ("SynapseFI") to assist in the execution of investors' USD deposits and withdrawals. (*Id.* ¶ 27.) SynapseFI provided, amongst other things, a ledger which keeps track of investors' total amount of USD deposits and withdrawals. It partners with Evolve Bank & Trust ("Evolve Bank"), a financial institution which held a bank account for Coinseed to execute investors' deposits and withdrawals. (*Id.*)

SynapseFI has reported to OAG that throughout January and the beginning of February 2021, it became increasingly concerned with the lack of communication from Defendants regarding investor withdrawal issues and how investors were affected by them. (*Id.* ¶ 28.) On February 14, 2021, SynapseFI provided notice to Defendants that it was terminating its relationship with Coinseed on March 31, 2021. (*Id.*) That same day Defendants, in an email to Coinseed investors, stated that its relationship with SynapseFI and Evolve Bank would be ending by March 31, 2021, and that Coinseed would be migrating to a new payment provider by that same date. (*Id.* ¶ 29, Ex. H.) Coinseed has not yet identified its purported new payment provider. (*Id.* ¶¶ 29 and 30.)

Since May 2019, Coinseed has held a corporate checking account at Capital One Bank ("Capital One"). (*Id.* ¶ 31.) Coinseed used this account as a "middle-man" between Evolve Bank and Gemini. (*Id.*) In other words, Defendants moved investor deposits from Evolve Bank to the Capital One account, and from time-to-time transferred money to Gemini to purchase virtual currency on behalf of investors. (*Id.*)

Around the time SynapseFI began to express concerns about investor withdrawal issues, Defendants began draining the Gemini and Capital One accounts. (*Id.* ¶ 32.) Between January 6 and 7, 2021, through a number of trades and withdrawals, Defendants removed over $30,000 worth of virtual currency from Gemini, leaving a balance of $1.30. (*Id.*) All activity on Gemini stopped for nine days. (*Id.*, Ex. I.)

Then, on January 16, 2021, Defendants automatically deposited $15,000 into the Gemini account; and on January 19, 2021 Defendants wired $86,000 into the Gemini account. (*Id.* ¶ 33.) Both deposits came from the Capital One account, and Defendants used that money to purchase bitcoins on Gemini. (*Id.*) By January 22, 2021, Defendants had removed all remaining bitcoins, worth over $100,000, from Gemini. (*Id.*) The Gemini account was left with a $5.27 balance. (*Id.*, Ex. I.)

It is unknown where Defendants moved all the virtual currency, but, based on a review of trade data and the public bitcoin blockchain, the majority of bitcoins were moved from Gemini to a wallet address controlled by Defendants, 1NhNsv1BDGHkQVxZqT5QeUAhES1LDa2avm. (*Id.* ¶ 34.) From there, the bitcoins were moved to a wallet address affiliated with a virtual currency trading platform named Binance. (*Id.*) Binance is an unregulated, unregistered foreign trading platform. (*Id.*)

According to withdrawal activity, since at least May 2019, Defendants have used several bitcoin wallet addresses to move virtual currency out of Gemini. (*Id.* ¶ 35.) In total, the current value of bitcoins that flowed through these wallet addresses and that were purchased with Coinseed investor deposits, is around $10 million. (*Id.*) In other words, the current value of investors' holdings, i.e., what would be owed to investors if they withdrew their funds, is around $10 million. (*Id.*) This value has grown from the approximately $1.2 million in actual investor

deposits since May 2019. (*Id.*)

There has been no activity in the Gemini account since January 22, 2021. (*Id.* ¶ 36.) Additionally, the Gemini account has a -$14,994.73 balance after Capital One rejected the January 6, 2021 automatic deposit due to insufficient funds. (*Id.*, Ex. I.)

On February 17, 2021, the same day OAG filed its Complaint, Defendants withdrew the remaining $1,527.64 from the Capital One account, leaving it with a zero balance. (*Id.* ¶ 37, Ex. B.)

E. Defendants' Counsel Withdraws Shortly After OAG Informs Counsel of Defendants' Unauthorized Transactions

As previously reported to the Court by Counsel for Defendants, on April 16, 2021, OAG contacted Counsel, voicing concern about the unauthorized trades and suspension of withdrawals. (Whitehurst Aff. ¶ 38, *See* NYSCEF No. 29.) According to Counsel, he "immediately" reached out to Defendants about the "gravity of the situation," but Defendants would not return any of his communications. (*Id.*) On April 22, 2021, Counsel informed OAG that an Order to Show Cause to be removed as Defendants' counsel in this matter had been filed, which the Court signed on April 23, 2021. (*Id.*) Morrison Cohen LLP is the counsel of record pending the hearing on May 21, 2021. (*Id.*, *See* NYSCEF No. 30.)

II. ARGUMENT

This Court should order preliminary relief under both the Martin Act and Executive Law § 63(12). A preliminary injunction for a violation of the Martin Act is appropriate where, as here: (1) it is likely that OAG will succeed on the merits of its claims; (2) irreparable injury to investors will occur absent a preliminary injunction; and (3) a balancing of the equities favors OAG's position and is in the public interest. CPLR § 6301; *see First Investors*, 156 Misc. 2d at 213. Because the purpose of the Martin Act is to "protect the public interest," the Attorney

General may present "special considerations" as to irreparable injury and how the equities are to be balanced. *State v. Fine*, 72 N.Y.2d 967, 969 (1988).

Under Executive Law § 63(12), OAG is entitled to a preliminary injunction merely upon a showing of "likelihood of success on the merits, and a balancing of the equities in petitioner's favor;" there is no need to offer "proof of irreparable injury." *People v. Apple Health & Sports Clubs, Ltd.*, 174 A.D.2d 438, 438-39 (1st Dep't 1991); *see also People v. P.U. Travel, Inc.*, 2003 N.Y. Misc. LEXIS 2010, at *7-8 (Sup. Ct. N.Y. Cnty. June 19, 2003) ("under federal regulatory statutes which are analogous to the Executive Law . . . an appeals court held that the usual prerequisites for the issuance of preliminary injunction (i.e., showing of irreparable injury) are not required.").[7]

A TRO may be granted pending a hearing for a preliminary injunction where "it appears that immediate and irreparable injury, loss or damage will result unless the defendant is restrained before the hearing can be had." CPLR § 6301. However, to obtain a TRO under Executive Law § 63(12), a showing of irreparable harm is not required. *See People v. Fanduel, Inc.*, No. 453056/15, 2015 N.Y. Misc. LEXIS 4521, at *24, 2015 NY Slip Op 32332(U), (Sup. Ct. N.Y. Cnty. 2015) (granting request for a TRO and holding that "[t]he NYAG is not required to show irreparable harm under Executive Law §63[12], it is implied in the need to prevent the effects of fraudulent and illegal conduct on the general public.").

New York State courts have routinely used Executive Law § 63(12) and the Martin Act to grant equitable relief, such as temporary restraining orders, asset freezes, and other appropriate

[7] *Accord State v. Terry Buick, Inc.*, 520 N.Y.S.2d 497, 500 (Sup. Ct. Dutchess Cnty. 1987) (holding, in the context of granting preliminary injunction sought by OAG, that "[t]raditional concepts of irreparable damage which apply to private parties do not govern this public interest field."); *People v. Empire Prop. Sols., LLC*, 2012 NY Slip Op 30346(U), ¶ 6 (Sup. Ct. Nassau Cnty. 2011) (same).

remedies, to protect investors. *See, e.g.,* *People v. Apple Health & Sports Clubs*, 80 N.Y.2d 803, 807 (1992) (upholding trial court's grant of TRO freezing defendants' bank accounts); *People v. 21st Century Leisure Spa, Int'l*, 153 Misc. 2d 938, 942 (Sup. Ct. N.Y. Cnty. 1991) (enjoining owner of company (via TRO) from transferring, withdrawing, or otherwise disposing of funds in bank accounts); *New York v. Abortion Info. Agency*, 323 N.Y.S.2d 597, 603 (Sup. Ct. N.Y. Cnty. 1971), *aff'd*, 37 A.D.2d 142 (1st Dep't 1971) (enjoining defendants "from transferring or otherwise disposing of corporate assets or property" and appointing receiver to preserve assets); *First Investors Corp*., 156 Misc. 2d at 213 (imposing an asset freeze injunction on the defendants); *People v. Allen*, 2020 N.Y. Misc. LEXIS 443, *7-8, 2020 NY Slip Op 30292(U) (Sup. Ct. N.Y. Cnty., Feb. 4, 2020) (granting preliminary injunction against fund, halting distributions and freezing fund assets).

Here, the order sought by OAG is necessary to preserve the status quo and to safeguard investor assets.

A. OAG Has Demonstrated a Likelihood of Success on the Merits Under Both the Martin Act and Executive Law § 63(12)

OAG has shown an overwhelming likelihood of success on the merits. Here, Defendants were acting as commodity broker-dealers without being registered with the Attorney General as the law requires. This is an incontrovertible fraudulent practice under the statute, and thus a violation of both the Martin Act and Executive Law § 63(12).

1. The Martin Act Requires Commodity Broker-Dealers Transacting in New York To Be Registered with OAG

The Martin Act makes it unlawful to engage in misleading or fraudulent practices in connection with the purchase or sale of securities or commodities (GBL § 352-c). Under the Martin Act, "fraud" and "deceptive acts or practices" are given the widest possible meaning and include "all deceitful practices contrary to the plain rules of common honesty." *People v.*

Federated Radio Corp., 244 N.Y. 33, 37-39 (1926), *accord People v. Lexington Sixty-First Assocs.*, 38 N.Y.2d 588, 595 (1976). "The purpose of the law is to prevent all kinds of fraud in connection with the sale of securities … and to defeat all unsubstantial and visionary schemes in relation thereto whereby the public is fraudulently exploited." *Federated Radio*, 244 N.Y. at 38. OAG is not required to allege scienter or reliance. *State v. Rachmani Corp.*, 71 N.Y.2d 718, 725, n.6 (1988); *State v. Sonifer Realty Corp.*, 212 A.D.2d 366 (1st Dep't 1995).

Section 359-e (14) of the Martin Act provides, in relevant part, that those engaging in the business of buying and selling commodities on behalf of clients, or who offer investment advice in such commodities, in New York must register with OAG. Specifically, Section 359-e(14)(b) provides, in relevant part:

> Any person acting as a commodity broker-dealer, commodity salesperson or commodity investment advisor and any person who manages or supervises any such broker-dealer, salesperson or investment advisor shall file a registration statement with the attorney general as a commodity broker-dealer, commodity salesperson, or commodity investment advisor relating to the activity actually engaged in.

Subsection (a)(iii) defines a "commodity broker-dealer" as follows:

> "Commodity broker-dealer" means any person engaged in the business of selling or offering to sell commodities through commodity contracts to the public within or from the state of New York.

A "commodity contract" is further defined in subsection a(ii) as "any account, agreement or contract for the purchase or sale of, or any option or right to purchase or sell, primarily for speculation or investment purposes and not for use or consumption by the offeree or purchaser, one or more commodities, whether for immediate or subsequent delivery or for storage and whether or not delivery is intended by the parties . . ."

This provision, which was added to the Martin Act almost forty years ago, was intended by the New York State Legislature to require those who operate on the fringes of the legitimate

commodities industry to register with OAG: "This bill is specifically designed to impose a significant sanction on those individuals who seek to straddle the Federal and State regulations" by not registering. *Am. Memorandum for Governor by Attorney General Abrams*, at 1 (Attorney General's Legislative Program (No. 108-83). Whether the provision has been violated is straightforward, as the Legislature recognized. "Proof of engaging in the sale of the commodities and being unregistered would be a relatively simple task." *Id.*

Virtual currency, also referred to as "cryptocurrency," are digital units that are used as a medium of exchange or form of digitally stored value. Last year, the First Department, squarely held that a virtual currency was a "commodity" within the meaning the Martin Act:

> [T]he Martin Act's definition of commodities as including "any foreign currency, any other good, article, or material" (GBL 359–e[14]) is broad enough to encompass [the virtual currency] *tether*. Indeed, federal courts and the Commodities Futures Trading Commission have found that virtual currencies are commodities under the Commodities Exchange Act, which defines the term more narrowly than does the Martin Act . . . .

Matter of James v. iFinex Inc., 185 A.D.3d 22, 28 (1st Dep't 2020) (emphasis in original). Cf. *C.F.T.C. v. McDonnell*, 287 F. Supp. 3d 213, 228 (E.D.N.Y. 2018) (virtual currencies such as bitcoin "fall well-within the common definition of 'commodity' as well as the CEA's definition of 'commodities'); *Lagemann v. Spence*, 18 Civ. 12218 (GBD) (RWL), 2020 U.S. Dist. LEXIS 88066, at *32-33 (S.D.N.Y. May 18, 2020) ("courts in this District have classified cryptocurrency as a 'commodity'."), *citing* *S.E.C. v. Telegram Group Inc.*, No. 19 Civ. 9439, 2020 U.S. Dist. LEXIS 53846, at *3-4 (S.D.N.Y. March 24, 2020) ("Cryptocurrencies . . . are a lawful means of storing or transferring value and may fluctuate in value as any commodity would"); *C.F.T.C. v. Gelfman Blueprint, Inc.*, No. 17 Civ. 07181, 2018 U.S. Dist. LEXIS 207379, at *13-14 (S.D.N.Y. Oct. 2, 2018) ("Virtual currencies such as Bitcoin are encompassed in the definition of 'commodity' under Section 1a(9) of the Act"); *Matter of Coinflip, Inc.*, 2015

WL 5535736, *2, 2015 CFTC LEXIS 20 (Sept. 17, 2015, CFTC Docket No. 15–29) ("The definition of a "commodity" is broad. Bitcoin and other virtual currencies are encompassed in the definition and properly defined as commodities.") (internal citations omitted).

Defendants repeatedly engaged in the business of executing trades, including selling and buying virtual currencies on behalf of investors in the State of New York, for the purpose of investment by creating accounts and by entering into contracts or agreements with New York investors. (Whitehurst Aff. ¶¶ 8-13.) Consequently, Coinseed is and was a commodity broker-dealer under New York law.

Subject to certain exemptions which do not apply to Defendants, subdivision 14(b) of GBL § 359-e and Title 13, N.Y.C.R.R. § 13.2 require that under New York law, any commodity broker-dealer or commodity salesperson "shall file" with OAG a "registration statement." GBL § 359-e (14)(b); 13 N.Y.C.R.R. § 13.2. Failure to register is deemed both a fraudulent practice and a crime. GBL § 359-e (14)(j) and (l), GBL § 352.[8]

Defendants are not registered as commodity broker-dealers as required under the Martin Act. (Whitehurst Aff ¶ 12.)

2. Repeated or Persistent Illegality Including Violation of the Registration Provisions of the Martin Act, Violates Executive Law § 63(12)

Defendants' illegal and fraudulent actions similarly establish a violation of the Executive Law. Executive Law § 63(12) gives OAG the power to bring an action against any person or entity that engages in "repeated fraudulent or illegal acts" or "otherwise demonstrate[s] persistent fraud or illegality in the carrying on . . . or transaction of business." There are thus two categories

[8] *See People v. Credit Suisse Sec. (USA) LLC*, 31 N.Y.3d 622, 631 (2018) (holding that the definition of fraudulent practices includes GBL § 359-e, because "Section 359-e (14) (l) provides: 'A violation of this subdivision shall constitute a fraudulent practice as that term is used in this article' and a specific reference to GBL § 359-e was added to GBL § 352").

of conduct that can subject one to liability under §63(12): acts that are "fraudulent" and acts that are "illegal."

As to "fraud", Executive Law § 63(12) broadly construes fraud "so as to include acts characterized as dishonest or misleading." *People v. Apple Health and Sports Clubs, Ltd.*, 206 A.D.2d 266, 267 (1st Dep't 1994), *dismissed in part, denied in part* 84 N.Y.2d 1004 (1994). Traditional elements of common law fraud such as reliance, actual deception, knowledge of deception, and intent to deceive are not required to establish liability for statutory fraud. *Id.* The test of fraudulent conduct under § 63(12) "is whether the targeted act has the capacity or tendency to deceive or creates an atmosphere conducive to fraud." *State v. Gen. Elect. Co.*, 302 A.D.2d 314, 314 (1st Dep't 2003). Section 63(12) is "meant to protect not only the average consumer, but also "the ignorant, the unthinking and the credulous." *Id.*

As to the illegality prong, an "illegal act" under the statute includes any violation of a federal, state, or local law. *See State v. Princess Prestige*, 42 N.Y.2d 104, 105 (1977); *People v. Empyre Inground Pools, Inc.*, 227 A.D.2d 731, 732-733 (3d Dep't 1996). Specifically, violations of the Martin Act constitute repeated illegality redressable under Executive Law § 63(12). *People v. Allen*, 452378/2019, 2021 N.Y. Misc. LEXIS 468, *20, 2021 NY Slip Op 30334(U) (Sup. Ct. N.Y. Cnty., Feb. 4, 2021).

Here, both categories of Executive Law § 63(12) are satisfied. Failure to register is both fraud and a crime under the Martin Act. By not registering with OAG, as required by New York law, Defendants have engaged in both repeated "fraud" and repeated violations of the Martin Act which constitutes an "illegal act" for purposes of liability under Executive Law §63(12).

B. Irreparable Harm to Investors Will Result if the Injunction is Denied

Investors will be irreparably harmed if Defendants: (i) continue to inhibit investors'

ability withdraw funds and (ii) retain the capacity to make unauthorized trades in investors' holdings. While evidence of irreparable harm is not a necessary element to obtain an injunction under Executive Law § 63(12), the evidence here of irreparable harm is, nonetheless, overwhelming.

Investors had already lost control of their assets when Defendants disabled all trading capabilities and transferred all investor holdings into the extremely volatile and speculative Dogecoin without investor authorization. Furthermore, Defendants have withdrawn all the funds out of Coinseed's Capital One account and transferred all virtual currency out of the New York-based and regulated Gemini platform into an unregulated, foreign Binance platform. This conduct demonstrates that, absent an injunction and the appointment of a receiver, Defendants will continue to make unauthorized trades in investor accounts to the detriment of investors and hide and dissipate investor assets. *See State v. Kozak*, 91 Misc. 2d 394, 395-396 (Sup. Ct. N.Y. Cnty. 1977) (enjoining Martin Act defendants from engaging in the offer or sale of securities and from transferring or disposing of their allegedly fraudulently derived assets where OAG "has shown irreparable injury to the public in the form of fraud and the possibility of financial instability on the part of defendants"); *see also Allen*, 2020 N.Y. Misc. LEXIS 443, at *2 (awarding injunctive relief to OAG and finding that "if the requested injunction is not ordered, Mr. Allen will remain in control of the assets of ACP, and the wind-down of the fund will likely proceed in a manner that furthers Allen's self-interest to the detriment of the Limited Partners.").

Indeed, Defendants traded in virtual currency on behalf of investors without authorization and moved funds out of Coinseed's bank account and virtual currency out of Gemini *after* OAG filed its lawsuit alleging past and continued fraudulent practices. Courts have repeatedly acknowledged that "the commission of past illegal conduct is highly suggestive of the likelihood

of future violations," and is grounds for immediate injunctive relief. *See FTC v. Five-Star Auto Club*, 97 F. Supp. 2d 502, 536 (S.D.N.Y. 2000). Without an order from this Court enjoining trading in investor accounts and placing the control of fiat and virtual currency assets in the hands of a receiver, investors will continue to be defrauded with little chance of recompense.

C. The Balance of Equities Favors Preliminary Relief

Defendants have no compelling equitable interest in continuing to violate the law. The balance of equities favors the issuance of a TRO, a preliminary injunction, and a receiver, because the Martin Act and Executive Law § 63(12) were specifically designed to protect the public, and the equities favor preservation of assets for the benefit of defrauded investors. *See New York v. Smart Apts. LLC*, 959 N.Y.S.2d 890, 898 (Sup. Ct. N.Y. Cnty. 2013) (granting preliminary injunction against an illegal hotel operator and holding that "the equities lie in favor of shutting down an illegal, unsafe, deceptive business, rather than in allowing said business to continue to operate (to defendants' presumed financial advantage)"); *see also First Investors Corp.*, 156 Misc. 2d at 214-215 (granting preliminary injunction and finding that the equities balance in favor of plaintiff, where it appears likely that defendants violated the Martin Act, and plaintiff is attempting to protect public interest).

In an action brought by OAG, "the standards of the public interest not the requirements of private litigation measure the propriety and need for injunctive relief." *People v. Greenberg*, 27 N.Y.3d 490, 497 (2016) (citations omitted).

The proposed TRO and preliminary injunction is tailored to the continuing violations. It would enjoin the Defendants from engaging in illegal and unauthorized trading of virtual currencies and preserve any remaining assets to allow for potential restitution to defrauded investors.

OAG has provided substantial evidence that investors have been unable to withdraw any of their funds for months. Meanwhile, Defendants moved all investor holdings out of virtual currencies of investors' own selection and into the highly speculative Dogecoin. Finally, Defendants are actively moving funds out of Coinseed's bank and virtual currency accounts. A TRO, a preliminary injunction, and appointment of a receiver will protect any remaining assets for investor recovery.

D. Defendants' Repeated Fraudulent Practices Require the Immediate Appointment of a Receiver

The Court should grant the appointment of a receiver pursuant to GBL § 353-a. In pertinent part, § 353-a provides:

> In any action brought by the attorney-general as provided in this article, the court at any stage of the proceedings may appoint a receiver of any and all property derived by the defendant or defendants or any of them by means of any such fraudulent practices, including also all property with which such property has been mingled if such property can not be identified in kind because of such commingling, together with any or all books of account and papers relating to the same. The judgment entered in such action may provide that such receiver shall take title to any or all such property and books of account and papers relating to the same and liquidate such property or any part thereof for the benefit of all persons intervening in the said action and establishing an interest in such property.

The appointment of such a limited receiver, as statutorily expressed, is a matter of judicial discretion not reviewable by the Court of Appeals. *People v. Lexington Sixty-First Associates*, 38 N.Y.2d 588, 595 (1976) (citations omitted); *see also Grenthal v. American Guarantee and Liability Insurance Co.*, 5 Misc.2d 994, 995, 161 N.Y.S.2d 985, 987 (Sup.Ct. N.Y. Co. 1957) (court ordered appointment of Martin Act receiver and noted the limited role as statutorily defined). In the context of determining whether to appoint a receiver, courts have also highlighted that "Article 23-A of the General Business Law is remedial in nature and should be liberally construed in order that its beneficent purpose may, so far as possible, be attained

(*People v Smith Co.*, 230 A.D. 268, 269 (4th Dep't 1930)." *People v. Lexington Sixty-one Assoc.*, 38 N.Y.2d at 595.

In considering an application for preliminary relief of a court-ordered appointment of a receiver under GBL §353(a), one court required a showing of irreparable injury that would both (i) result without a receiver appointment and (ii) be obviated by such appointment. *State v. First Investors Corp.*, 156 Misc. 2d 209, 215 (Sup. Ct. N.Y. Cnty. 1992). The facts here meet and exceed that test. An order simply restraining Defendants from further access to Coinseed's assets would be insufficient to preserve the assets and protect investors. Defendants' repeated past and ongoing fraudulent practices foretell that they will continue to unlawfully dissipate Coinseed's assets. *See FTC v. Five-Star Auto Club*, 97 F. Supp. 2d 502, 536 (S.D.N.Y. 2000) ("the commission of past illegal conduct is highly suggestive of the likelihood of future violations"). Their unauthorized trading of investor assets, blocking investors' ability to make trades in their own accounts, the prolonged failure to withdraw investor funds even after months of investor requests, and the diversion of investor assets to an unregulated foreign virtual currency trading platform fully warrants a receiver. *See Grenthal v. American Guarantee and Liability Ins. Co.*, 161 N.Y.S.2d at 987 (court authorized Martin Act receiver to take control of all property derived by the defendant through fraudulent practices including "all property with which such property has been commingled if such property cannot be identified in kind because of such commingling"). The appointment of a Martin Act receiver to take custody of investor assets pursuant to GBL § 353-a will, in contrast, assure asset preservation and obviate the ongoing injury.

In addition to the statutory receivership remedy provided for in GBL § 353-a, the Court has well established authority to appoint a receiver to protect corporate property from

dissipation, waste, and fraudulent distribution. *See* *Hall v. Vunk*, 248 A.D. 900 (2d Dep't 1936); *Hahn v. Wylie,* 54 A.D.2d 622, 623 (1st Dept 1976) ("receivership pending determination of an action is a conservation and preservation remedy resting in the sound discretion of the court…"); *Lefebvre v. Shea*, 212 A.D.2d 884 (3d Dep't 1995) (granting appointment of receiver where plaintiff demonstrated likelihood that property would be injured or destroyed without receiver and defendants' financial status was insecure); *SEC v. Princeton Economic Intern Ltd*, 73 F. Supp. 2d 420 (S.D.N.Y. 1999) (court issued preliminary injunction and appointed receiver to conserve assets of defendants based on efforts by defendants to hide assets in a foreign jurisdiction and after losing millions in risky currency and commodities trading).

OAG requests the Court consider at least one receiver candidate for this matter, Michelle Gitlitz of Crowell & Moring, LLP, a law firm with experience in virtual currency, blockchain technology, and receivership appointments. (*See* Ex. L.) The receiver candidate has agreed to serve on a pro bono basis. OAG has sought other candidates for consideration by the Court that would be willing to serve in a pro bono capacity and intends to provide any supplemental information to the Court as arises. (Whitehurst Aff. ¶ 40.)

Given the overwhelming evidence of Defendants' illegal actions, the Court may grant the relief requested by Plaintiff without the need for a hearing. *See* *Inc. Vill. of Plandome Manor v. Ioannou*, 863 N.Y.S.2d 241, 242 (2d Dep't 2008).

CONCLUSION

For the above reasons, the Court should treat this matter as essential, grant the requested TRO, issue the proposed Order to Show Cause, and subsequently appoint a receiver and grant Plaintiff's request for a preliminary injunction.

Dated: New York, New York
May 6, 2021

Respectfully submitted,

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Commercial Division Rule 17 Certification

I, Brian M. Whitehurst, an attorney duly admitted to practice law before the Courts of the State of New York, hereby certify that the Memorandum of Law in Support of Plaintiff's Application for a Preliminary Injunction and Appointment of a Receiver complies with the cord count limit set forth in Rule 17 of the Commercial Division of the Supreme Court, as it contains 6999 words excluding the caption, table of contents, table of authorities, and signature block. In preparing this certification, I have relied on the word count of the word-processing system used to prepare this memorandum of law.

Dated: New York, New York
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