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Date: March 15, 2022

SUBJECT: LEGAL OPINION ON "BUSDX" WHITEPAPER – WHETHER BUSDX TOKEN IS A SECURITY OR UTILITY UNDER THE US LAWS

This Legal Opinion has been prepared in an attempt to assess whether BUSDX Token (hereinafter referred to as "**BUSDX**") to be issued by BUSDX Platform (hereinafter referred to as the "**Platform**") is a utility or security under the US Securities laws and regulations in view of the precedents set out by the US Supreme Court.

1. WHAT IS BUSDX TOKEN

We understand from the Whitepaper of the Platform that it allows users to buy and exchange BEP-20 tokens in the form of BUSDX Tokens. We also note that BUSDX is the native token that fuels the Platform's product ecosystem. Users are required to hold/stake/pay with the BUSDX token to access these products. More specifically, BUSDX is a rewards token that was created on the Binance Smart Chain, with a mechanism that distributes 10% rewards in BUSD to holders automatically. BUSD is a 1:1 USD-backed stablecoin approved by the New York State Department of Financial Services (NYDFS), issued in partnership with Paxos.

BUSDX has also developed a staking App and a BUSDX launchpad (Xpad). Users will receive 50% APY in BUSDX while their tokens are staked, while still receiving 10% BUSD rewards. The Platform also plans to promote virtual BUSDXpay system (Xpay), NFT platform (Xnft) other similar systems ("**Services**").

2. TYPES OF TOKENS/COINS UNDER THE US LAW

There are generally four major types of tokens/coins issued namely Protocol, Equity, Security and Utility tokens/coins:

2.1. Protocol Tokens/Coins: The first kind of token/coin is the classic "cryptographic currency". This token/coin is called protocol token/coin because what makes it special is the new or different protocol it uses. It is generally used solely as an alternative currency, wholly digital.

Its underlying blockchain serves nothing more than keeping a ledger of the transactions between token/coin holders. It is usually mined or given away for free at issuance (either by creation of an entirely new network, either via a blockchain split event, a.k.a "airdrop", or via some commercial sites that offer the token/coin in exchange for some commercial participation, a.k.a "faucets"). In its initial digital issuance, this type of token/coin is rarely exchanged for any valuable (sold), since initially it has no underlying or practical value at all.

2.2. Equity Tokens/Coins: These tokens/coins represent ownership of an asset, such as debt or Platform stock. By employing blockchain technology and smart contracts, a startup could forgo a traditional initial public offering (IPO) and instead issue shares and voting rights over the blockchain.

2.3. Security Token/Coins: These token/coins on the other hand are promises for future profit. Security tokens/coins refer to any kind of tradable asset. These tokens/coins are forms of digital assets, the purchase of which entitles the owner with number of rights which are similar to securities such as stocks or bonds. There are three major characteristics for an instrument to be deemed as a security: Voting rights in a general assembly or pertaining to important decisions of an entity, profit sharing such as distributions, and/or a right to claim against the Platform to redeem the instrument in exchange for a value.

Therefore, a security token/coin, for example, might offer voting rights in the issuing entity, or rights in the profits of the issuing entity (or both). The issuing entity might also promise to redeem the token/coin's value when there will be enough capital to do so. These are but examples of rights attached to such tokens/coins, which can be deemed by many jurisdictions throughout the planet to be as securities *per se*, which therefore require to be compliant with the securities laws and regulations. In the United States, security token/coin sales and investments are subject to Securities and Exchange Commission (SEC) securities regulations.

The US Supreme Court in *SEC v. Howey*[1] established the guidelines for whether a financial arrangement involved an investment contract and was subject to securities regulations. According to the Howey Test, an arrangement is a security if it involves "an investment of money and a common enterprise with the expectation of profit, primarily from the efforts of others." Some simple guidelines to determine if the token/coin is a security are as follows:

i) Ownership interest in a legal entity
ii) Equity interest
iii) Share of profits and assets
iv) Status as a creditor or lender

[1] SEC v. Howey Co., 328 U.S. 293 (1946)

v) A token/coin that can be converted into a security token/coin

2.4. Utility Tokens/Coins: Contrary to the above, the Utility tokens/coins do not meet the requirements of the Howey test. Utility Tokens/Coins provide users with access to a product or service. This kind of token/coin is basically a contract for provision of goods or services, to be redeemed by the token/coin holder, once or continuously. In contrast with the protocol tokens/coins which do not have any assets of any kind underlying them and their value is being based purely on mass psychology, the utility token/coin has an actual underlying contractual right. Therefore, its value is determined not only by mass psychology but also by the value of the underlying right attached to it. Therefore, its value is determined not only by mass psychology but also by the value of the underlying right attached to it.

Following are some of the factors to determine if a token/coin is not a security:

i) Develops features for a blockchain or to mine
ii) Use the blockchain and its outputs
iii) Contribute efforts to the blockchain
iv) Sell the products of the blockchain
v) Vote on features and functionality of blockchain

3. ANALYSIS OF THE US SECURITY LAWS AND THE HOWEY TEST

In the U.S, issuing, offering, or selling unregistered securities will be a violation of Section 5 of the Securities Act of 1933, and the issuer can face 5 years of prison. Furthermore, investors may initiate lawsuits under Section 5 and Section 12(a)(1) of the Securities Act of 1933 (or 15 U.S. Code § 77e and § 77l (a)(1)) for damages of selling non-exempted security without registering it. Moreover, the Securities Exchange Act of 1934 gives powers in section 10(b) to federally regulate fraudulent security practices, wherein regulation 17 C.F.R. 240.10b-5 (c) gives investors the right to sue any issuer for fraud or deceit. It should be noted that similar laws apply in many other jurisdictions.

The Securities and Exchange Commission (hereinafter, the "**SEC**"), has issued the "Report of Investigation Pursuant to Section 21(a) of the Securities Exchange Act of 1934: The DAO" (Release No. 81207 / July 25, 2017) wherein a few fundamentals were promulgated. Firstly, SEC has stated that the existing federal securities laws are sufficient to tackle the token/coin issuance.

Secondly, and more importantly, the SEC has pointed out that not all tokens/coins are securities, and that such classification shall be determined on a case-by-case basis. In order to define a token/coin as a security, the SEC has stated that "Howey Test" shall be applied, which indeed was applied by the SEC in that particular DAO project token/coin issuance SEC investigation on which its report was written. Finally, the SEC has treated DAO, an

unincorporated, non-resident, virtual organization, definitely not situated in the U.S, as an entity for which the Securities laws also apply to, and by reference applying the U.S laws to whomever offers or sells securities to U.S persons, no matter in which jurisdiction the issuing entity is incorporated and/or located.

3.1.Form over Substance

Firstly, determining whether a transaction involves a security does not turn on labelling; if we say a particular token/coin is a utility, it does not make the issued token/coin a utility token/coin. Secondly, even if a token/coin has a practical utility use, it does not necessarily preclude the token/coin from being a security – but instead requires an assessment of "the economic realities underlying a transaction." **(United Housing Found., Inc. v. Forman, 421 U.S. 837, 849 (1975) (the "Forman" Case)).**

> *The "test . . . is what character the instrument is given in commerce by the terms of the offer, the plan of distribution, and the economic inducements held out to the prospect" (SEC v. C.M. Joiner Leasing Corp., 320 U.S. 344, 352-53 (1943))*

4. WHETHER BUSDX IS A UTILITY OR SECURITY INSTRUMENT UNDER THE US SECURITIES LAWS AND REGULATIONS?

In order to become a security token there are four conditions that BUSDX Token needs to meet. If BUSDX doesn't meet any of these conditions, it will fall under the category of Utility token. Securities must be registered per Section 5 of the Securities Act of 1933 as stated hereinabove. Of course, that instrument which is not security need not to be registered. Therefore, one must first examine the definition of Security:

> *"(a) Definitions - When used in this subchapter, unless the context otherwise requires— (1) The term "security" means any note, stock, treasury stock, security future, security-based swap, bond, debenture, evidence of indebtedness, certificate of interest or participation in any profit-sharing agreement, collateral trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting-trust certificate, certificate of deposit for a security, fractional undivided interest in oil, gas, or other mineral rights, any put, call, straddle, option, or privilege on any security, certificate of deposit, or group or index of securities (including any interest therein or based on the value thereof), or any put, call, straddle, option, or privilege entered into on a national securities exchange relating to foreign currency, or, in general, any interest or instrument commonly known as a "security", or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing." 15 U.S. Code § 77b*

Similarly, the Securities Exchange Act of 1934 defines a security, in the following fashion:

> *"The term ''security'' means any note, stock, treasury stock, security future, security-based swap, bond, debenture, certificate of interest or participation in any profit-sharing agreement or in any oil, gas, or other mineral royalty or lease, any collateral-trust certificate, preorganization certificate or subscription, transferable share, investment contract, voting trust certificate, certificate of deposit for a security, any put, call, straddle, option, or privilege on any security, certificate of deposit, or group or index of securities (including any interest therein or based on the value thereof), or any put, call, straddle, option, or privilege entered into on a national securities exchange relating to foreign currency, or in general, any instrument commonly known as a ''security''; or any certificate of interest or participation in, temporary or interim certificate for, receipt for, or warrant or right to subscribe to or purchase, any of the foregoing; but shall not include currency or any note, draft, bill of exchange, or banker's acceptance which has a maturity at the time of issuance of not exceeding nine months, exclusive of days of grace, or any renewal thereof the maturity of which is likewise limited." Section 3(a)(10) of the Securities Exchange Act of 1934.*

The U.S Supreme Court has stated that the term "investment contract" in these two definitions is treated as being the same (SEC v. Edwards, 540 U.S. 398 (2004)). So, we can see that the U.S term "security" includes also an "investment contract". An investment contract is an "investment of money in a common enterprise with a reasonable expectation of profits to be derived from the entrepreneurial or managerial efforts of others." (see SEC v. Edwards, 540 U.S. 389, 393 (2004); SEC v. W.J. Howey Co., 328 U.S. 293, 301 (1946); see also the Forman case, at 852-853) (in this work, the "Howey Test").

To be accurate, the Howey Test requires that the profits will be made solely from the efforts of others:

> *"… an investment contract for purposes of the Securities Act means a contract, transaction or scheme whereby a person invests his money in a common enterprise and is led to expect profits solely from the efforts of the promoter or a third party…. Such a definition…permits the fulfillment of the statutory purpose of compelling full and fair disclosure relative to the issuance of the many types of instruments that in our commercial world fall within the ordinary concept of a security…. It embodies a flexible rather than a static principle, one that is capable of adaptation to meet the countless and variable schemes devised by those who seek the use of the money of others on the promise of profits."* **(SEC v. W.J. Howey Co., 328 U.S. 293 (1946))**

5. INTRODUCTION TO THE HOWEY TEST

The HOWEY Test is used as a benchmark to determine whether or not an investment (in the form of a token/coin) is a security. For instance, if an investment meets all four conditions of the HOWEY Test it will be considered as a security. However, in case if a particular investment fails to pass the HOWEY Test or meet even a single criteria out of the four, the token/coin will

be considered as a Utility token/coin.

The Howey test is used to determine whether an instrument qualifies as an "investment contract" for the purposes of the Securities Act: "a contract, transaction or scheme whereby a person invests his money in a common enterprise and is led to expect profits solely from the efforts of the promoter or a third party."

In other words, an investment contract for purposes of the Securities Act means a contract, transaction or scheme, whereby, a person invests his money in a common enterprise and is led to expect profits solely from the efforts of the promoter or a third party, it being immaterial whether the shares in the enterprise are evidenced by formal certificates or by nominal interests in the physical assets employed in the enterprise. The test is whether the scheme involves an investment of money in a common enterprise with profits to come solely from the efforts of others.

An instrument will be treated as a security if all the following are present:

- Investment of Money
- Common Enterprise
- Expectation of Profit
- Through the Efforts of the Promotors

5.1.Application of HOWEY Test on BUSDs

Below is the application of HOWEY TEST on BUSDX Tokens:

i) Investment of Money

One element of the Howey test is the investment of money. Many purchasers of digital tokens/coins use Bitcoin, Ether, or similar cryptocurrencies rather than fiat currency. This does not avoid the condition of the test regarding an investment of money. Jurisprudence is quite clear that an investment of money is not limited to currency, but may also include assets, goods, notes, and other forms of consideration.[2] In *Majors v. South Carolina Securities Commission*[3], court held that an investment of money under *Howey* means that an investor must have committed assets to the enterprise in such a manner as to subject himself to financial loss.[4] Token/coin purchasers, whether using cash, Bitcoin and other cryptocurrencies, or providing an exchange of services, are exposing themselves to financial loss through their purchase. Tokens/Coins are not neither fiat currencies nor are they government backed financial products. Accordingly, from established case law and due to the flexible interpretation of the elements of the Howey test, it would seem that purchases of new digital tokens/coins, by means other than fiat currencies, would still qualify as an investment of money.

It is pertinent to mention that cryptocurrency is not money per se, but on August 6th 2013, the U.S. District Court for the Eastern District of Texas held that Bitcoin is within the definition of "money" for purposes of the rules governing investment contracts – Bitcoin can purchase goods or services, and can be exchanged for conventional government-backed currencies (SEC v. Shavers, No. 4:13-CV-416, 2013 WL 4028182, (E.D. Tex. 2013), reconsideration aff'd, No. 4:13-CV-416, 2014 WL 12622292 (E.D. Tex. 2014).

Since the BUSDX can be purchased by the public with actual money or cryptocurrencies, it may be concluded that the users of the Platform will be investing their money to purchase the BUSDs. Therefore, first condition of a Security Token/coin is fulfilled.

ii) Common Enterprise

In the DAO Report, the SEC did not address this element of the Howey test, other than in passing, and then only to make a declarative statement that token/coin purchasers were investing in a common enterprise. The focus of the common enterprise element is tied to a pooling of funds in contemplation of the expectation of profits, which is addressed in the next section.

In *Continental Marketing Corp.*[5], the court found that Continental was engaged in a common

[2] See, e.g., Int'l Bhd. of Teamsters v. Daniel, 439 U.S. 551, 560 n.12 (1979); *see also* Coinbase et. al., *A Securities Law Framework for Blockchain Tokens, (2016)*, https://www.coinbase.com/legal/securities-law-framework.pdf.
[3] Majors v. S.C. Sec. Comm'n, 644 S.E.2d 710 (S.C. 2007).
[4] Id. at 716; see also Hector v. Wiens, 533 F.2d 429, 432 (9th Cir. 1976); SEC v. Pinckney, 923 F. Supp. 76, 80 (E.D.N.C. 1996).
[5] Continental Marketing Corp. v. SEC, 387 F.2d 466, 469 (10th Cir. 1967).

enterprise, the very heart of which was a chance to invest money through multiple contracts amounting in reality to an "investment contract" within the meaning of the applicable statute. The Continental court further stated that the element of control was not essential to the finding of a common enterprise; rather, emphasis should be placed on the economic realities of the venture and the nature of the investor's participation in said enterprise.

Specifically, the court said, "If [the investor's participation] is one of providing capital with the hopes of a favorable return then it begins to take on the appearance of an investment contract notwithstanding the fact that there may be more than one party or other than a principal party and his agent on the other end of the transaction or transactions." It would seem, then, that unless the underlying network for which the ICO is being held is purely a non-profit, open-source project, the common enterprise element is easily met.

There are two sub-tests for the "Common Enterprise" prong – the horizontal commonality test, and the vertical commonality test, which is being divided into the narrow vertical and the broad vertical. The U.S courts have applied these two tests alternately. The horizontal commonality test, which is the more common test, requires the pooling of assets from multiple investors so that all will share in the profits and risks of the enterprise. i.e., the profits of each investor are similar to those of the other investors.

Both vertical commonality tests require that the investor's fortunes will be tied to the issuer/promoter's success, rather than to the fortunes of its fellow investors; the broad vertical commonality test requires that the well-being of all investors be dependent upon the issuer/promoter's expertise. On the other hand, the narrow vertical commonality test requires that the investors' fortunes be "interwoven with and dependent upon the efforts and success of those seeking the investment ... of third parties" (SEC v. SG Ltd., 265 F.3d 42, sec. 31-35 (1st Cir. 2001)).

The holders of BUSDX Tokens shall be deemed equity holders having mutual share in the profits and risks of the Platform. Therefore, the second condition of Security Token/coin under the Howey test has also met.

iii) Expectation of Profit

Whether the sale of the tokens/coins constitutes a security under Howey will depend in large part on making an "economic reality" assessment with regard to their purpose. Is it usable solely within the network environment for which it is created, or is it fungible and tradable such that its value may increase with the growth or success of the enterprise?

In the SEC case against MA Lundy Associates[6] the court, while emphasizing the economic

[6] SEC v. M.A. Lundy Assocs., 362 F. Supp. 226 (D.R.I. 1973).

realities of the project, cited to established case law under Howey in reaching its decision:

> *The more critical factor is the nature of the investor's participation in the enterprise. If it is one of providing capital with the hopes of a favorable* return then it begins to take on the appearance of an investment contract notwithstanding the fact that there may be more than one party or other than a principal party and his agent on the other end of the transaction or transactions[7]

Accordingly, the court rightly found that the whiskey project was an unregistered sale of securities in violation of § 5 of the 1933 Act.

Contrast this case with cases involving the sales of an interest in residential properties intended for occupancy. In United Housing v. Forman[8], tenants of a massive New York City housing cooperative brought suit against the owners alleging securities fraud and the sale of unregistered securities, among other claims. Right of occupancy in the co-op apartments required the purchase of a number of shares in the co-op which were expressly called "stock." No rights were conferred to the stock owners, other than occupancy; under the lease terms, stock could not be sold for more than their purchase price plus a fraction of the mortgage amortization paid during tenancy. Despite being labeled as stock, the US Supreme Court held that such shares were not securities and did not meet the conditions of Howey.

Writing for the majority, Justice Powell stated that, when viewed in terms of their substance (the economic realities of the transaction) rather than their form, the instruments involved here were not shares of stock in the ordinary sense and conferred none of the normal rights associated with stock or other securities. Following this logic, digital tokens/coins sold for use in established networks that only have utility within those networks, such as loyalty points, game tokens/coins, and the like, might appear less likely to be considered securities.

Moreover, this prong does not merely require the token/coin holders to expect profit, because it seems unreasonable that someone will purchase a service or a good without taking into account the probability that the purchased will increase in value. The expectation of profits from a purchase of any kind of valuable is almost always present. Therefore, it seems that the prong requires not only that there will be an expectation to profit, which is trivial, but also that the purchase of that valuable will be primarily motivated by making profits (upon resale for example), rather than by consuming or using that which was purchased.

The personal consumption is a vital part of considering whether this prong is met or not, wherein it should be examined if the primary motivation of purchasing the token/coin is to profit upon resale, or to use the underlying rights of the token/coin. There are several court

[7] Id. at 238 (quoting Cont'l Mktg. Corp. v. SEC, 387 F.2d 466 (10th Cir. 1967) (referring directly to Howey in making this statement).
[8] *See* United House Found, Inc. v. Forman, 421 U.S. 837, 837 (1975).

cases where this differentiation was stipulated, for example see the Forman Case. Per Forman, it "is an investment where one parts with his money in the hope of receiving profits from the efforts of others, and not where he purchases a commodity for personal consumption or living quarters for personal use".

Upon reviewing the Whitepaper of BUSDX, it appears that although BUSDX holders would be able to stack up their Tokens/Coins and earn a yield in BUSD Tokens for their contribution, however, yet they would not be automatically expecting profit merely by holding the BUSDX Tokens. The primary purpose of such Tokens/Coins is to use them in exchange for the Services offered by the Platform. Like any kind of valuable, the BUSDX holders may hold it to a time where the value of the Token in the market will increase, wherein the holder may sell the Token with profit. Nevertheless, since BUSDX provides a real consideration and functionality, it only seems reasonable (and the token/coin is designed so) that purchasers will use the Token rights for consumption.

In addition to being a tool used for raising funds for the Platform, the BUSDX Tokens will also be used to exchange certain utility Services, which have been highlighted in this Opinion. It means that the purpose of these Tokens are not only to raise capital but also to offer actual services in exchange of these Tokens. Therefore, this prong's requirement of Security Token/coin does not seem to have met.

iv) Through the Efforts of the Promotors

Most courts do not appear to take the "solely from the efforts of others" element of the Howey test literally, focusing instead on the degree of managerial control over an enterprise.[9] Within the context of a blockchain network, the primary factor to consider when determining the degree of managerial control seems to be the extent to which token-holder/coin-holders participate in the development and design of the network and in the core decisions of the enterprise. Simply put, the central question is how much control the investors retain. The greater the control, the less likely you are to have an investment contract.

The analysis is likely to depend on the significance of the efforts of the management team or network designers (the "others") as compared to token/coin purchasers and token/coin miners (the "investors"). In the *SEC v. Glenn W. Turner Enterprises*, the Second Circuit stated that a key factor in its determination was "whether the efforts made by those other than the investor are the undeniably significant ones, i.e. those essential managerial efforts which affect the failure or success of the enterprise."

In the case of BUSDX Platform, however, BUSDX Tokens are not a tool used to expect profits through efforts of the promotors, rather these Tokens provide tools to acquire various Services

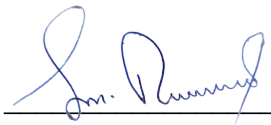
[9] *See, e.g.*, SEC v. Glenn W. Turner Enters., 474 F.2d 476, 482-83 (9th Cir. 1973).

offered by the Platform. Additionally, the holders of BUSDX Tokens would not get anything from the efforts of promotors as they would be using their BUSDX Tokens on various afore-mentioned services. Therefore, the last condition of Security Token – profit must be through the efforts of the promotors – has also not fulfilled.

6. CONCLUSION

It may be concluded that Two out of four conditions of Security Token under HOWEY TEST have not been fulfilled. Therefore, BUSDX Token appears to fall under the category of Utility Token.

Yours Sincerely,



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