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

In the Matter of the Inquiry of LETITIA JAMES, Attorney General of the State of New York,

Petitioner,

—*against*—

iFINEX INC., BFXNA Inc., BFXWW INC., TETHER HOLDINGS LIMITED, TETHER OPERATIONS LIMITED, TETHER LIMITED, TETHER INTERNATIONAL LIMITED,

Respondents.

Index No.: 450545/2019

AFFIRMATION OF STUART HOEGNER

STUART HOEGNER, hereby affirms this 30 day of April, 2019, under the penalties of perjury under the laws of New York, which may include a fine or imprisonment, that I am physically located outside the geographic boundaries of the United States, Puerto Rico, the United States Virgin Islands, or any territory or insular possession subject to the jurisdiction of the United States, that the following is true, and I understand that this document may be filed in an action or proceeding in a court of law:

1. I am an attorney licensed in Canada and the United States. I became General Counsel of Bitfinex in 2016, and became General Counsel of Tether in 2016 (collectively, the "Companies"). Between 2014 and 2016, I had worked on an hourly basis for the Companies. As used in this Affidavit, "Bitfinex" refers to iFinex Inc., BFXNA Inc., and BFXWW Inc., collectively, and "Tether" refers to Tether Holdings Limited, Tether Operations Limited, Tether Limited and Tether International Limited, collectively.

2. I make this Affidavit in support of the Companies' Motion, by Order to Show Cause, to Vacate or Modify the *Ex Parte* Order dated April 24, 2019 and for an Immediate Stay of the Order. Except where indicated otherwise, the information in this Affidavit is based on my personal knowledge and the exhibits are true copies of the originals.

Bitfinex and Tether

3. iFinex Inc. ("iFinex") is a privately-held financial technology company, incorporated in the British Virgin Islands, that operates a virtual currency trading platform operating under the business name of Bitfinex. Bitfinex is among the largest virtual currency trading platforms in the world. It was founded in 2012, and it is the world's largest exchange by volume for trading Bitcoin against the U.S. Dollar. BFXNA and BFXWW are wholly-owned subsidiaries of iFinex that are incorporated in the British Virgin Islands. BFXNA is registered with FinCen as a Money Services Business and does not service U.S. customers (except under the narrow restrictions and conditions contained in Bitfinex's terms of service), and BFXWW provides services to other international customers.

4. Tether Limited is a privately-held financial technology company incorporated in Hong Kong that operates a platform to store, send, and make purchases of a digital token known as tether (₮), and is also responsible for issuing tether. To "issue" tether, at the relevant times, is generally understood to mean to send tether tokens to Bitfinex or a customer of Tether in exchange for an equivalent amount of fiat currency. For example, Tether may issue 10,000,000 U.S. dollar tethers to Bitfinex by transmitting that amount from Tether's digital "wallet" to Bitfinex's wallet. In exchange, Bitfinex would transfer $10,000,000 to Tether via account transfer or wire.

5. Tether Holdings Limited is incorporated in the British Virgin Islands and is the holding company for Tether Limited, as well as for Tether Operations Limited and Tether International Limited.

6. Tethers are a form of "stablecoins," which means their value is pegged to traditional currency (U.S. Dollars, Euros, or Japanese Yen). With certain restrictions, tethers can be redeemed on a one-to-one basis for the traditional currency in which they are denominated. For example, 1 U.S. dollar tether ("USD₮") is redeemable by Tether at $1.00, subject to Tether's terms of service.

7. Stablecoins such as tether provide significant utility in the virtual currency market, allowing users to convert cash into virtual currency, and to anchor (or tether) the value of virtual currency to the price of traditional fiat currencies like the U.S. dollar, the Euro, and the Yen. As one example of such a transaction, a virtual currency trader may exchange $1,000 into 1,000 U.S. dollar tethers. The value of those tethers (and by association, their equivalent value in traditional currency) is intended to remain "stable," differentiating it from virtual currencies (e.g., bitcoin) which can widely fluctuate in value.

8. Tethers also provide a medium of exchange across a wide range of virtual currency trading platforms that is often more convenient than traditional currency (referred to in the industry as "fiat" currency). For example, the trader referenced above may transfer their 1,000 U.S. dollar tethers to different virtual currency exchanges, where they can be used to buy and sell other virtual currencies. When the trader wishes to exchange their tethers back to fiat, he or she can then dispose of them at a variety of virtual currency exchanges for traditional currency.

9. Stablecoins such as tether are generally not bought for investment purposes, and the main function of stablecoins is to facilitate other virtual currency transactions. In this way, there is no expected "profit" from a stablecoin; their reason to exist is to be redeemable at exactly par by Tether—no more—so that they can be used as a medium of exchange.

10. Consequently, it is generally inappropriate to characterize tether as an "investment" or those who hold them as "investors." For the same reason that the use of a U.S. dollar as a medium of payment for goods and services does not make one an investor in the United States government (the entity that issues USD), the recipient of a tether is not an investor in Tether (the entity that issues USD₮).

Banking Relationships for Bitfinex and Tether

11. It is well-established in the industry that virtual currency exchanges and businesses face significant challenges in identifying and maintaining traditional banking relationships. For example, in a March 3, 2019 article entitled "Why Crypto Companies Still Can't Open Checking Accounts," Bloomberg writers discussed the heavy compliance burden placed upon banks seeking to provide services to virtual currency businesses, noting that: "[e]ntrepreneurs in the digital-assets industry from New York to Hong Kong say that even as some attract investment from multibillion-dollar institutions like Singapore's sovereign wealth fund, they are routinely refused basic banking services by the likes of HSBC Holdings Plc and JPMorgan Chase & Co." *See* Alastair Marsh and Silla Brush, *Why Crypto Companies Still Can't Open Checking Accounts*, Bloomberg (Mar. 3, 2019) (copy attached as Ex. A).

12. Bitfinex and Tether have similarly encountered significant institutional resistance among financial service providers.

13. As one example of this, from approximately 2015 through in or about March 2017, the Companies held accounts with a number of well-established Taiwanese banks (*e.g.*, Hwatai Commercial Bank, KGI Bank, First Commercial Bank, and Taishin Bank). Wells Fargo was a correspondent bank for those banks, facilitating their transfer of money internationally using the Society for Worldwide Interbank Financial Telecommunication ("SWIFT") network. In or about March 2017, Wells Fargo unilaterally suspended its service of wire transfers from the Companies' bank accounts at the Taiwanese banks to their customers, creating an immediate threat to the Companies' ability to transfer funds to and from their customers.

14. In light of such difficulties, Bitfinex and Tether have continued throughout their history to seek long-term relationships with traditional financial institutions, while concurrently relying on third-party payment processors. (Broadly speaking, a "payment processor" is a third party that facilitates financial transactions between parties.)

15. As a supplement to its relationships with other financial institutions, Bitfinex established a relationship with payment processor known as Crypto Capital in or about January 2015. Bitfinex strengthened its relationship with Crypto Capital in the immediate aftermath of the Wells Fargo service disruption. Indeed, in or about 2017 and 2018, Crypto Capital processed hundreds of millions of dollars' worth of transactions on behalf of Bitfinex.

16. In light of Crypto Capital's provision of once reliable payment-processing services, Bitfinex opened additional accounts with Crypto Capital in or about 2017 through in or about 2018 for the purpose of processing Euro, Pound Sterling, and Japanese Yen,

among other currencies. Likewise, Bitfinex entrusted Crypto Capital with increasing amounts of funds.

17. On information and belief, in or about mid-2018, other virtual currency trading platforms purportedly using Crypto Capital began to experience delays in Crypto Capital's processing of withdrawal requests.

18. In or about August 2018, Crypto Capital continually represented to senior executives of Bitfinex that funds held with Crypto Capital had been the subject of a partial governmental seizure, and were expected to be released imminently. Since this time, at least one governmental entity has confirmed that it was involved in the seizure of Crypto Capital funds.

19. Notwithstanding the foregoing, Crypto Capital continued to provide payment-processing services to Bitfinex through approximately October 2018. As recently as April 2019, Crypto Capital representatives continued to respond promptly to requests for information and documents from Bitfinex.

20. Out of an abundance of caution, in or about January and February 2019, Bitfinex proactively and voluntarily informed the Office of the New York Attorney General ("OAG"), as well as various U.S. federal law enforcement agencies,[1] of its issues and concomitant concerns with Crypto Capital. On information and belief, those federal agencies have since been investigating Crypto Capital on a non-public basis at the time of OAG's application and press release regarding this matter.

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[1] The Companies have a long history of consistent cooperation with law enforcement agencies, such as the Department of Justice, the Commodity Futures Trading Commission, the Federal Bureau of Investigation, the Internal Revenue Service, the Department of Homeland Security, the Secret Service, the Financial Crimes Enforcement Network, and numerous state regulatory agencies. Internationally, the Companies have likewise consistently cooperated with such law enforcement agencies as Interpol and Europol.

The Companies' Good-Faith Solution

21. Beginning in or about August 2018 and continuing through in or about November 2018, Bitfinex entered into a series of transactions whereby tethers issued by Tether to Bitfinex were purchased through account transfers between Bitfinex and Tether's accounts at Crypto Capital. Throughout these transactions, all U.S. Dollar tethers issued or redeemed were reserved by an equivalent amount of value in U.S. Dollars. Additionally, customer requests to purchase, sell, or redeem for cash value U.S. Dollar tether continued unabated.

22. Likewise, the Companies also engaged in a series of transfers of fiat currency previously deposited with Crypto Capital from Bitfinex's account to Tether's account there. In turn, Tether transferred equivalent amounts to Bitfinex between the Companies' respective accounts at a Deltec Bank & Trust Limited.

23. At the time, the Companies believed that withdrawals at Crypto Capital would resume, and the Companies would once more have unencumbered access to the funds entrusted to Crypto Capital. It is only with the benefit of hindsight and Monday morning quarterbacking that OAG now claims that the transfers were inadequate, or that some undefined harm *might* have occurred then (or now) were every holder of the more than $2 billion in U.S. Dollar tether in circulation to redeem their tether at once.

24. In any event, it was for the protection of the virtual currency market that, when in December 2018, senior executives of Bitfinex grew concerned that Crypto Capital might fail to return funds held there, the Companies began to proactively negotiate a credit facility through which Tether would extend Bitfinex a secured, revolving line of credit of up to $900 million.

25. Separate, independent counsel were retained for each of Bitfinex and Tether. White & Case LLP represented Tether and Herbert Smith Freehills represented Bitfinex. Over the next three months, the credit facility was negotiated and memorialized. While OAG purports to wonder what "benefit[s] would accrue to Tether, or holders of tethers, from this transaction," the obvious answer is that Tether, and holders of tether, have a keen interest in ensuring that one of the dominant trading platforms of tethers has sufficient liquidity for normal operations. Further, as the companies are known to be affiliated, disruption to Bitfinex's operations would naturally risk creating negative spillover to Tether, as well.

26. The chief document governing this transaction was the Credit Facility agreement attached to OAG's application to the Court.

27. To be clear, without any obligation or request to do so, counsel for Bitfinex and Tether voluntarily disclosed the nature of the transaction approximately one month before it was closed, providing OAG a general overview of the anticipated deal. It is only now, more than a month after the credit facility was finalized, that OAG seeks to enjoin Bitfinex's use of the credit facility for the ostensible protection of holders of Tether.

28. Yet it was for the protection of Tether that the amounts transferred from Bitfinex's Crypto Capital account to Tether's Crypto Capital account (totaling $675 million) were incorporated into the credit facility, and deducted from the $900 million of credit made available to Bitfinex. Put differently, the credit facility obligated Bitfinex to repay Tether the amounts held in Tether's Crypto Capital account on commercially reasonable terms (i.e., a term of three years and an interest rate of 6.5%). Further utilization requests have been submitted to Tether since the credit facility was implemented, totaling $75 million. The

credit facility further provides clear terms governing future requests by Bitfinex to utilize any portion of the remaining $150 million line of credit, and provides terms for the repayment of such amounts.

29. As shown in the balance of the 229 pages of transaction documents produced to OAG, the credit facility agreement was further executed in compliance with the Companies' respective corporate governance policies. OAG seemingly does not claim otherwise. A separate 33-page Share Charge agreement pledged 60,000,000 shares of iFinex to Tether as a condition precedent to entering into the credit facility.

30. In short, the foregoing terms cannot be legitimately reconciled with OAG's claim that Bitfinex simply "offloaded" its potential liability onto Tether. Moreover, through provision of a line of credit to Bitfinex, the Companies have ensured that the market has continued to have uninterrupted access to liquid funds through the Bitfinex virtual currency exchange. In this way, OAG's demand that Bitfinex be enjoined from drawing upon the line of credit pending the completion of OAG's investigation cannot be seen to "protect[] legitimate traders on the Bitfinex platform."

<u>Tether's Updated Disclosures</u>

31. In February 2019, well before the line of credit transaction closed, Tether updated the disclosures on its website to specify that its reserves "may include other assets and receivables from loans made by Tether to third parties, which may include affiliated entities." (Ex. B, at 6 (Item 1.1.32).) The website also made clear that that risks in buying tether included risks associated with the reserves: "Assets backing digital assets such as Tether Tokens, including loan receivables owed to Tether, are subject to the risk of default, insolvency, inability to collect, and illiquidity." (Ex. C, at 2 (Item 7).)

32. The industry press covered these changes. For example, in March 2019, Bitcoin Magazine published an article under the headline, "Tether Updates Website, Says USDT Backed by 'Reserves,' Not Just Cash." (Ex. D.) The same day, Marketwatch published an article with the headline, "Tether reverses claim of 100% dollar backing, sparking criticism." (Ex. E.) For whatever alleged "criticism" the disclosure engendered, however, the markets remained confident in tether, as it continued to trade at par (*i.e.*, $1 for every U.S. Dollar Tether, or USDT) or above after the reporting. (Ex. F, at 2 (data from cryptocompare website showing closing price of tether at $1.00 and $1.01 on March 14 and 15, 2019, respectively).)

<u>Tether Holders Are Not At Risk</u>

33. Neither the updated disclosure nor the line of credit transaction itself has impeded Tether's ability to process redemptions. As of the date I am signing this affidavit, Tether has cash and cash equivalents (short term securities) on hand totaling approximately $2.1 billion, representing approximately 74 percent of the current outstanding tethers.[2] Between December 2018 and April 29, 2019, the average daily fiat redemption has been $566,066.00, with the largest being $24.2 million. The vast majority of redemption requests of Tether are for less than $1 million. Even if Bitfinex fully draws on the remaining amount of the line of credit, the reserves will still be just below $2 billion, representing approximately 68% percent of the current outstanding tethers.

34. Beyond Tether's cash on hand, additional reserves are available, though in less liquid form. That Tether does not now keep liquid, cash reserves equal to 100 percent of the outstanding tethers is not only disclosed to customers, but hardly a novel concept. Commercial banks operate under a "fractional reserve" system whereby they keep cash on

[2] This excludes such things as tethers in quarantine.

hand representing only a small fraction of customer deposits, deploying the rest via investments. According to the Federal Reserve website, the banks must keep cash reserves representing, at most, only 10 percent of their liabilities. (Ex. G, at 1.) Tether's cash is far more than that, and the company has never lacked the funds to process a redemption.

35. Market participants appear to understand that tether is not at risk. The Attorney General's *ex parte*, highly inflammatory, and misleading application was widely covered in the press, including an article in the *Wall Street Journal*. *See* Paul Vigna, *Bitfinex Used Tether Reserves to Mask Missing $850 Million, Probe Says*, Wall Street Journal (April 25, 2019) (copy attached as Ex. H). This coverage resulted in an approximate loss of $10 billion across dozens of cryptocurrencies within *one hour*. *See* Ryan Browne & Eustance Huang, *Cryptocurrencies shed $10 billion in an hour on worries over 'stablecoin' tether*, CNBC (April 26, 2019) (copy attached as Ex. I). Nonetheless, market confidence in U.S. Dollar tether remained strong, as tether continued to trade at $0.99 (a $0.01 discount). (Ex. F, at 2.) The volume of trading was far higher than normal, which shows that tether holders who thought the news was grounds to sell had a highly-liquid market in which to do so. Since the news, tether has processed redemptions with no interruption.

OAG's Misleading Application

36. OAG's application contains numerous mischaracterizations and omissions that undercut its request for injunctive relief.

37. First, OAG's representation to the court that "Crypto Capital's inability or unwillingness to return any of the funds made it impossible for Bitfinex to honor its client's withdrawal requests," is incorrect. Bitfinex continued through 2018 to honor customer withdrawal requests using its other financial service providers, and continues to provide

38. Second, bank statements produced to OAG showing hundreds of millions of dollars in Bitfinex's other accounts contradict OAG's representation that "all or almost all of Bitfinex's funds" were held at Crypto Capital during the relevant period.

39. Third, it is simply wrong for OAG to state that Bitfinex is treating Tether's reserves as Bitfinex's "corporate slush fund," or to imply that fiat currency backing outstanding tethers is being rapidly depleted such that *ex parte* injunctive relief was necessary. To the contrary, as discussed, the Companies have addressed the Crypto Capital issue in a manner that: 1) provides Bitfinex with additional liquidity to process normal customer demands; and 2) provides Tether with commercially reasonable protections for the funds made available to Bitfinex.

The Preliminary Injunction is Needlessly Disruptive to Bitfinex

40. In my view, the OAG's preliminary injunction serves no useful purpose. Far from protecting tether holders — who at all times have been adequately capitalized and fully able to redeem — the OAG has succeeded only in spreading misinformation to the markets. On the other side of the ledger, freezing Bitfinex's access to the credit line is highly disruptive and will only serve to reduce liquidity on hand to satisfy the needs of Bitfinex's customers and impede the normal operation of Bitfinex's business.

Stuart Hoegner