

Crypto Exchange Obtains Favorable Ruling in Arbitration of Claims over Alleged Trading Losses

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This past month, a California district court granted a motion to compel arbitration of various claims by customers of cryptocurrency exchange platform, Coinbase Global, Inc. (“Coinbase”), finding that Coinbase’s User Agreement, which contains a broad arbitration provision, including a delegation clause that delegates questions of arbitrability to the arbitrator. ([Donovan v. Coinbase Global, Inc.](#), No. 22-02826 (N.D. Cal. Jan. 6, 2023)).

Unlike some electronic contracting disputes, which turn on whether the user had adequate notice of the terms and manifested consent to such terms (a ruling which often involves an examination of a site or app’s screen display and whether the user is reasonably presented with notice that completing a transaction will bind the user to terms of service), the account holders in this case did not dispute that they had agreed to the User Agreement, rather they argued that the arbitration provision and delegation clauses were unconscionable and unenforceable.

Back in May 2022 a putative group of Coinbase account holders brought various claims against defendants over certain allegedly misleading statements and subsequent actions taken with respect to a stablecoin (GYEN), touted as “the first regulated digital JPY” and offered by co-defendant GMO-Z.com Trust Co., Inc. (“GMO-Z”) (which had previously been [issued a conditional BitLicense](#) by the New York Department of Financial Services). GYEN opened for trading on Coinbase in November 2021 but suffered fluctuations of value, allegedly causing financial losses to investors and prompting the claims against the defendants.

In response, Coinbase moved to compel arbitration of the claims, and in a recent decision, a California district court granted Coinbase's motion, ruling that the Coinbase User Agreement delegated arbitrability questions to the arbitrator; however, the co-defendant and stablecoin issuer GMO-Z, a nonparty of the Coinbase User Agreement, was unsuccessful in seeking to compel arbitration under the agreement, with the court rejecting the argument that the agreement extended such rights to a non-signatory. ([Donovan v. Coinbase Global, Inc.](#), No. 22-02826 (N.D. Cal. Jan. 6, 2023)).

The issue before the court was whether there was ample evidence that the parties delegated arbitrability questions to the arbitrator. Since arbitrability must be determined first, the court does not reach plaintiffs' allegations that the arbitration agreement as a whole is unconscionable. The Coinbase User Agreement includes a delegation clause that delegates questions of arbitrability to the arbitrator: "The arbitrator shall have exclusive authority to resolve any Dispute, including, without limitation, disputes arising out of or related to the interpretation or application of the Arbitration Agreement, including the enforceability, revocability, scope, or validity of the Arbitration Agreement or any portion of the Arbitration Agreement...." The court also noted that the User Agreement incorporates the American Arbitration Association ("AAA") rules, which grant the arbitrator "the power to rule on his or her own jurisdiction." Thus, the court stated that, based on the foregoing, the parties "agreed to arbitrate arbitrability," and that unless the court finds that the delegation clause is unconscionable, as Plaintiffs contended, or subject to another applicable contract defense, the court would enforce the delegation clause.

Both parties advanced dueling arguments on the procedural unconscionability issue: the Plaintiffs argued that the User Agreement was an adhesion contract that was recently amended and that the delegation clause was buried in lengthy text and not called out explicitly in a pop-up box when users agreed to the amended terms; Coinbase countered that when the terms were amended, users were alerted and prompted to review the terms before continuing using Coinbase and that users were free to reject the terms and consult the Help page about how to close their account and move their funds elsewhere. The court agreed with Coinbase, finding that, all in all, Coinbase was not the only option for cryptocurrency services and that even though Coinbase's amendments to the delegation clause were not explicitly spelled out in a pop-up box to users, the provision in the User Agreement was "clearly labeled" in bold print. The court also found that Plaintiffs failed to demonstrate substantive unconscionability. Therefore, the court ruled that delegation provision was enforceable, and that that Plaintiffs' challenges to arbitrability were delegated to the arbitrator.

As far as the co-defendant, GMO-Z's separate motion to compel arbitration, the court rejected its argument that Plaintiffs were bound to arbitrate their claims against GMO-Z as per the Coinbase arbitration agreement under the doctrine of equitable estoppel. The court noted that under California law, a nonsignatory may compel arbitration under the doctrine of equitable estoppel where a plaintiff's claims against the non-signatory are "based on the same facts and are inherently inseparable" to those against a signatory. Here, according to the court, the User Agreement contained "clear-cut" language showing an intent to arbitrate disputes between the signatories only (Specifically, section 1.1 of the arbitration agreement states: "Subject to the terms of this Arbitration Agreement, **you and Coinbase agree...**") (emphasis added). As such, GMO-Z's motion to compel arbitration was denied, but the court, in its discretion, entered a stay of all proceedings pending resolution of the Coinbase arbitration.

The court's decision in the *Donovan* case highlights why online entities and marketplaces, including digital asset services and crypto exchanges, take great care in drafting terms of use and user policies. Any platform or app might process thousands or even millions of transactions and it is inevitable, particularly in the current challenging crypto winter, that a customer might suffer unexpected losses due to transactions involving third party digital assets. Thus, such services typically rely on disclaimers, limitations of liability, and, in this case, a carefully-worded arbitration clause.

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