

GRAPH GRAIL AI LEGAL OPINION

GraphGrail Ai Token

Token Legal Design

After undertaking a thorough legal analysis of the GAI token and the accompanying documents such as GraphGrail Ai Whitepaper and Token Sale Agreement, the following was established.

GraphGrail Ai is planned to be artificial intelligence platform for the blockchain built on the basis of natural language processing technologies with a marketplace of decentralized applications, which is going to operate with the help of its own token called “GAI”. Tokens are planned to be used as a payment method in the GraphGrail Ai ecosystem and be of utility nature.

GAI tokens will be required in order to get an access to the unique content. For the business client segment, the use of the platform assumes reference to a blockchain protocol through the GAI Token for gaining access to: Platform tools; Raw and processed data; Proven solutions and trained neural networks; Requests for work by rated users of the platform; Leaving comments with ratings of solutions. This is not possible without using Tokens, which are the internal currency of the project.¹

Tokens GAI will be paid to participants for the creation, improvement and testing of language models. Tokens will be paid to data markers for their work, the testers and voters, who monitor the quality of models and the community.

To access the platform, a business representative will need to buy from the exchange 5,000 to 10,000 Tokens. Businesses will be able to spend Tokens for purchasing internal platform services, such as collection, cleaning, data marking, custom settings for training neural network, etc.²

GAI Token is a utility Token and acts as the internal currency within the system. For the Token, the business customer of the NLP end product gains access to the system and the ability to

¹ GraphGrail Ai Whitepaper p. 26

² GraphGrail Ai Whitepaper p. 31

³ GraphGrail Ai Whitepaper p. 34

quickly order and receive a solution, such as software development of the application and the markup of data for it.³

In summary, GAI tokens will act as the means of payment within the GraphGrail Ai Ecosystem since they play the role of the inside unit of accounting. As such, GAI tokens will be used as a way of paying for services offered on the platform and to get an access to the unique content. GAI tokens are also planned to become one of the main payment methods within the GraphGrail Ai Ecosystem. outside GraphGrail Ai ecosystem. GAI tokens cannot be used in any other way, which means that they do not possess the necessary qualities of currency or a measure of value. This type of token can, therefore, generally be classed as a utility token.

Token Utility

GAI token can be characterized as a utility token since it serves the role of the only payment method within the GraphGrail Ai Ecosystem. Every purchase, sale, exchange, or any other transaction on the platform will require the use of GAI tokens.

GAI token, therefore, offers utility from holding, obtaining and spending the token. Utility is derived from the fact that there is a clear and compelling reason for GAI token to exist - it enables the use of services on the platform by performing the key integral function of the platform's inside currency. Thus, we conclude that there is a compelling reason for the native digital asset to exist and that the main purpose is token distribution to a numerous quantity of clients for purchasing services which platform provides.

US Securities Laws Background

Background

By way of a background, U.S. Securities and Exchange Commission ("SEC) has a three-part mission: protection of investors, maintenance of fair, orderly and efficient markets and facilitation of capital formation. In order to implement its mission SEC has quite a wide mandate on reviews and enforcement actions it may undertake in upholding its mission.

On 25 July 2017, it was announced that SEC issues investigative report concluding that DAO tokens were, in fact, securities.⁴ The idea behind DAO was to create a decentralized autonomous venture fund. The SEC came to a conclusion that DAO tokens were securities that are regulated as a matter of the U.S. securities regulation because the enterprise was essentially a pooled investment vehicle. The reason being the nature of the DAO token that

⁴ "Report of Investigation Pursuant to Section 21(a) of the Securities Exchange Act of 1934: The Dao," SEC Release No. 34-81207 (July 25, 2017), (<https://www.sec.gov/litigation/investreport/34-81207.pdf>).

gave investors a right to vote on the projects that should be funded and receive profits from those projects as a return on their investments.

It is important to note, that U.S. securities regulation does not regulate the investment instrument as such, but the transactions that relate to it, which is why it is crucial to analyse whether a transaction may involve a security by way of applying the *Howey Test*⁵ described below. If that is the case, then the transaction has to be registered subject to the available securities exemption. Registration, in turn, entails disclosure of certain information including description of security being offered and information about company's management.

Violation of registration requirements can lead to holding the person, who offers or sale securities without any registration, liable in respect of the person purchasing such security from. The security purchaser may then sue to recover the consideration paid for such security with interest thereon, less the amount of any income received thereon, upon the tender of such security, or for damages if he no longer owns the security (*Sec. 12 of Securities Act of 1933 of the USA*).

Is GAI Token a Security?

In the context of tokens and ICO, the relevant test applied by the U.S. Courts is the *Howey Test*. It is used to determine whether an instrument qualifies as an 'investment contract' as defined by federal and state securities laws.

In the case of *United Housing Foundation, Inc. v Forman (1975)*, The U.S. Supreme court summarized the test the following way:

"the basic test for distinguishing the transaction from other commercial dealings is whether the scheme involves an investment of money in a common enterprise with profits to come solely from the efforts of others. . . This test, in shorthand form, embodies the essential attributes that run through all of the Court's decisions defining a security. The touchstone is the presence of an investment in a common venture premised on a reasonable expectation of profits to be derived from the entrepreneurial or managerial efforts of others. By profits, the Court has meant either capital appreciation resulting from the development of the initial investment, . . . or a participation in earnings resulting from the use of investors' funds, . . . In such cases, the investor is "attracted solely by the prospects of a return" on his investment. . . By contrast, when a purchaser is motivated by a desire to use or consume the item purchased. . . - the securities laws do not apply."

Based on the above and later cases, that have expanded the term "money" to include investments of assets other than money, we can deduce 3 key parts to the *Howey* test:

⁵ Securities and Exchange Commission v. W. J. Howey Co., 328 U.S. 293 (1946) case.

1. It is an investment of money or other tangible or definable consideration
2. The investment of money is in a common enterprise
3. There is an expectation of profits from the investment, which comes solely from the efforts of others

Applying the test above to GAI tokens, we find the following:

1. It is an investment of money or other tangible or definable consideration

GAI tokens are sold for several cryptocurrencies Ethereum and Bitcoin. We therefore consider this factor to be satisfied.

2. The investment of money is in a common enterprise

The law on the “common enterprise” element is somewhat unclear and not easily susceptible to analysis.

However, there are three approaches to define whether common enterprise exists:

- under the horizontal approach, a common enterprise is deemed to exist where multiple investors pool funds into an investment and the profits of each investor correlate with those of the other investors;
- under the narrow vertical approach, a common enterprise exists, if the profits of investor are tied to the promoter;
- under the broad vertical approach, a common enterprise exists, if the success of investor depends on the promoter’s expertise.

We do not consider this factor to be satisfied, as the profits or rights of investors do not depend on the investments of other investor, and exchange of cryptocurrency to GAI tokens is more akin to buying the rights to access and use the GraphGrail Ai ecosystem, than to receiving some type of investment interest.

3. There is an expectation of profits from the investment, which comes solely from the efforts of others

In our case as GAI tokens are used only as the inside unit of accounting that can be used to receive the services available through the GraphGrail Ai ecosystem, there is no direct interrelation between investing into tokens and expectation of profits from such an

investment. GAI tokens can only be used within the GraphGrail Ai Ecosystem, which essentially negates the possibility of them being considered as money or measure of value. The GAI tokens grant their holders the right to utilize the system, thus we see token holders as active participants, like licensees. Based on that, we therefore do not consider this factor to be satisfied.

Summary

As we see in our case the only one factor of the Howey test that is satisfied, in our opinion, is “the investment of money or other tangible or definable consideration”. Other two factors we consider not to be satisfied. For token to be considered a security all three elements have to be present, thus, there is a low risk that the GAI tokens will fall under the definition of securities according to the U.S. federal and state laws.

Legal Risks Associated with GAI Token

Generally, if tokens are listed on crypto exchanges, there is a risk of speculating on them and using them merely for getting the profit. There may arise an expectation of the increase in value of tokens, due to their secondary trading.

However, the said does not contain risks for tokens to be considered as securities since:

1. there still will be no common enterprise;
2. increases in the value due to the secondary trading are derived both from the issuer of tokens (the owner of the system) and the token holder, so profits obtained from token trading cannot be considered as such, that come solely from the efforts of others.

GraphGrail Ai Token Growth potential, market demand and the support of the platform given by its users.

Here we consider GAI Tokens in the light of the projects’ business model and establish what is the driving demand for GAI Tokens and whether such tokens are likely to be of a high demand on the market.

World statistics show that in 2017 the Artificial Intelligence worth \$2,5 billion and predicts the revenues by 2025 at a rate of \$ 59 billion.

Artificial Intelligence market grows rapidly but it has few fundamental problems.

The first one is the lack of the sufficient data. Every company solves the problem of searching for datasets, data analytics, machine learning and the practice of neural networks usage using its own resources. There are no datasets in public domains.

The second problem is that there is no single full-cycle service on the market that provides the possibility of creating linguistic models without programming. Companies should hire special programmers and it takes from 5 to 12 months for one subject area.

GraphGrail Ai is going to solve these fundamental problems and provides a simple interface for creating a domain model and subsequent machine learning. There are no comparable products on the market as of yet.

First of all, on the GraphGrail AI platform anyone will be able to create and train neural networks for various tasks without special knowledge with an easy-to-use constructor. Expected that business executives, startup owners, developers, data-science experts and many others will have the ability to create custom applications for integration into their services and applications.

Second point is an important feature of the platform that provides a full cycle of work with data, from collection and markup all the way to the final result.

Currently, the service is used for analysis in business and government agencies. It performs tasks like analyzing business products, searching for agitation or illegal statements.

The target markets are banking sector, retail, digital, biotech and medicine, security and law enforcement.

GraphGrail AI team is going to create Artificial Intelligence (AGI), which would be open to the entire community, controlled and enhanced by the efforts of developers from all over the world. Blockchain technology is able to realize this goal. New system will allow to check the quality of data markup by the community on blockchain, the system will provide a foundation for trust and a decentralized nature of the interaction of participants.

Users from all over the world without special knowledge will have the opportunity to earn on the platform by creating, improving and voting for language models. To do this, the project implements the GAI (Graphgrail + AI - Artificial intelligence) Token based on the Ethereum blockchain network.

Users will be able to monetize their activities on the platform by creating and selling their linguistic applications.

To sum up, GraphGrail Ai Ecosystem will consist of three key elements: the universal designer of language applications - the GraphGrail Ai Designer; the ecosystem of crowdsourcing data markup and the enrichment of data-sets - the GraphGrail Ai LabelLance; and the marketplace of ready-made applications – the GraphGrail Ai Marketplace. As already stated, GAI is a token

of the utility nature, which serves as the only payment method within the GraphGrail Ai Ecosystem and acts as an access to the unique content on the platform.

Since GAI tokens play an integral part in the GraphGrail Ai Ecosystem by being the inside method of payment and a unit of reward, GAI tokens act as the fuel designed to incentivize users to interact with GraphGrail Ai Ecosystem and make profit. It can, therefore, be concluded that this type of utility token is likely to be of a high demand on the market since it lies in the core of every product or service that GraphGrail Ai ecosystem delivers.

GraphGrail Ai Ecosystem provided by the balance of supply and demand for the services and requests from business clients. This ensures more customers and more people on data markup and a larger segment coverage each of which requires custom language models.

Businesses will be able to spend Tokens for purchasing internal platform services, such as collection, cleaning, data marking, custom settings for training neural network, etc. The more participants in the system and the more orders are placed in the application marketplace, the greater the benefit the business brings to the platform, providing a long-term foundation.

The number of GAI tokens will be strictly limited. At the end of token sale, no more GAI tokens will be ever issued.

The above information suggests that the limited quantity of tokens means that the demand will rise once the quantity of tokens would no longer be able to meet the demand.

Overall, in the light of the above, we conclude that the value of GAI Tokens are likely to increase since they are backed up by a strong business model as inferred from the GraphGrail Ai Whitepaper.

Final Conclusion

Based on the analysis above, we conclude that GAI Tokens are legitimate, likely to be of a high demand on the market and, thus, can be listed on the established cryptocurrency exchange platforms.