Stop that Bitcoin!

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Nicholas Towers provides a handy introduction to injunctive relief against cryptoassets

IN BRIEF

- A rough and ready explanation of what 'cryptoassets' are for the non-technical novice.
- The practicalities of obtaining injunctive relief over cryptoassets such as Bitcoin and NFTs based on how and where they are controlled.
- Summary of the relevant case law on cryptoassets constituting property in English law.

Tulips or technological revolution? The correct answer is that it doesn't matter, because if one of the 200 million people around the world who own cryptoassets has a problem, they will instruct a lawyer who knows what they are and how to deal with them. This two-part article seeks to provide a gentle introduction to the concept for lawyers in the context of interim injunctive relief.

As a rapidly evolving technology, the basket of cryptoassets will inevitably expand and change over the coming years. For the time being, and for the purpose of proprietary injunctions, the most common are 'pure' cryptocurrencies, the best-known being Bitcoin and Ethereum, and then non-fungible tokens (NFTs), which are tokens built on a cryptocurrency network and which can represent tangible or intangible things.

What are they?

Being able to assist a client with a cryptocurrency-related injunction does not require excessive technical or programming knowledge. By way of very brief introduction, cryptoassets are scarce digital assets, based on cryptography, which exist on a particular kind of system which is analogous to a database. Within that database are *addresses*, which can hold and deal with the actual tokens or 'cryptocurrency' of that database, similar to a bank account having a balance. So a particular Bitcoin address might hold 0.05 *Bitcoin*, a particular Ethereum address might hold 1 *Ether*. Each address is controlled by a string of code called a private key. Functionally, the private key is a bit like the 16 digits, expiry date and three-digit card security code (CSC) on a bank card, because if a person has these, they can execute transactions for that bank account.

Private keys can be stored by simply writing them down on a piece of paper, though various software and hardware systems are available.

What is essential to understand is that a cryptoasset like Bitcoin is not controlled by a single entity, but instead exists through a huge global network of independent operators who neither know nor trust each other. This means that an individual Bitcoin transaction cannot be censored unless at least half of that global network agrees, which for practical purposes will never happen. At a bank, a single employee or computer can say 'no' if there is a freezing injunction against the account holder or simply because the transaction looks a bit unusual. It also means that it is impossible to reverse a cryptoasset transaction, whether it is illegitimate or not.

Are proprietary injunctions even available?

English law is more than capable of dealing with the concept of cryptoassets. Despite not fitting neatly within traditional definitions, Bitcoin and other cryptoassets have been repeatedly recognised as being property by the English courts, albeit only in the context of first instance decisions on interim relief.

In *AA v Persons unknown* [2019] EWHC 3556 (Comm), Bryan J accepted that cryptoassets met the test for property set out in *National Provincial Bank Ltd v Ainsworth* [1965] AC 1175, a decision echoed by Butcher J in *Ion Science Ltd v Persons Unknown* (unreported, 21 December 2020), also citing the UK Jurisdiction Taskforce's 'Legal statement on cryptoassets and smart contracts', and again in *Danisz v Persons Unknown and another* [2022] EWHC 280 (QB), [2022] All ER (D) 107 (Jan). There is now a fairly established trend which would likely only be reversed by a High Court judge making a decision after full trial.

Cryptoassets are also treated as being located where the owner is domiciled (*Ion Science Ltd* at [15]).

Practicalities

Just like the balance of a bank account is not cash sitting in a vault, a cryptoasset held by an address is not sitting on a computer server or USB drive and cannot be physically seized. It is just code in a database. If the defendant is a person unknown, or if they reside overseas (or flee the jurisdiction), there is relatively little that an English court can do to coerce them.

However, a significant benefit of most cryptoassets is that because the databases are public, every single transaction ever made can be scrutinised. There are companies specialising in tracing the flow of cryptocurrency assets, allowing for swift applications to court—which are inevitably without notice because cryptoassets can be transferred away with a few clicks, 24 hours a day.

In addition, cryptoassets frequently come into the hands of a law-abiding third party, for several reasons. First, the number of people who control a Bitcoin or Ethereum address by holding their own private keys are very limited; it is easy to irreversibly lose cryptoassets, and much easier to have a third-party custodian hold the cryptoassets instead.

Second, most wrongdoers want to realise their ill-gotten gains by converting cryptoassets into cash, and the easiest way to do that is through cryptocurrency exchanges, which provide marketplaces for the exchange of currency and cryptocurrencies. Crucially, when someone sends a cryptoasset to an exchange, they are transferring it from their address to an address for which the exchange has the private keys. Therefore, all the depositor now has is an IOU. As such, if a reputable exchange receives notice of an injunction, or is the subject of one directly, it can freeze the user's account, preserving the cryptoassets before they can be moved away. Since many exchanges have Know Your Customer (KYC) requirements, they can also identify account holders and point to bank accounts where withdrawals are sent.

In *Danisz*, a *Bankers Trust* order required the exchange Huobi to disclose the identity of the account holder, and in *Fetch.ai Ltd and another company v Persons Unknown Category A and others* [2021] EWHC 2254 (Comm), Judge Pelling QC made a *Bankers Trust* order against a Cayman Islands company in the Binance cryptocurrency exchange group, and a *Norwich Pharmacal* order against a UK group company.

What about NFTs?

NFTs are currently mostly used for artwork, but an NFT is not a digital picture itself—it is a piece of code creating a token on a network such as Ethereum, which can be linked to a digital object (a picture, music or video), or a real-world object, or even an intangible right such as membership of a club. This is a nascent type of cryptoasset which is likely

to expand beyond artwork in the coming years, but for the time being the greatest value is in artistic NFTs. Many of these are extremely valuable, akin to the fine art market: the top 20 highest individual NFT sales range from $US5.4m to $US69.3m.

There have not been any definitive judicial statements that NFTs amount to property in English law, but in *Osbourne v Persons Unknown and another* [2022] EWHC 1021 (Comm), again an interim relief claim, the court considered it was at least realistically arguable that they are (see 'NFTs as property: what next?', *NLJ*, 13 May 2022, p13 for further analysis of this decision). Given that an NFT is just a token on a network, like Bitcoin or Ether, there does not seem to be any reason in principle why an NFT would not be property.

Artistic NFTs are generally not stored on exchanges, with the vast majority of owners taking on the responsibility of self-custody (or, for very high-value pieces, professional custodial services). However, despite the general absence of third-party custodians, there are still methods by which NFTs can be practically, if not actually, frozen to prevent disposal.

This is because while NFTs are typically held by users, they are predominantly bought and sold through online marketplaces, which provide a user interface that makes buying and selling NFTs easy, for a percentage fee. The biggest platform is OpenSea, which reported total sales volume of $US13bn in 2021. An NFT owner puts an NFT up for sale, stating the purchase price and authorising the transfer to any third party who pays that price.

If OpenSea is notified that an NFT has been stolen, it will freeze a particular NFT and no longer allow it to be sold on their platform. This is what recently happened in Singapore, where a valuable NFT (Bored Ape #2162) which had been used as collateral for a loan was 'frozen' by court order after a dispute arose. There was nothing to stop the person controlling the address holding the NFT from dealing with it, but they cannot do so through OpenSea, which publicly flagged the item as being suspicious. This dramatically reduces the pool of potential buyers.

As a result, NFTs, in their present form of use, are quite susceptible to injunctive relief. This was put into practice *Osbourne v Persons Unknown*. The claimant held an Ethereum address which contained certain 'Boss Beauties' NFTs. A malicious party gifted several other NFTs to that address in September 2021 and then something—it is not clear from the judgment what—caused two NFTs to be transferred to a third party. A claim was brought against the unknown thief, and against OpenSea (the trading name of Ozone Networks), and injunctive relief was granted. OpenSea, whether as a result of the court order or not, froze the NFTs.

OpenSea was made subject to a *Bankers Trust* order on the basis that the wallets to which the NFTs were transferred were 'controlled or administered by [OpenSea]', and that OpenSea likely had KYC information on the controllers of the wallet. This appears to be inaccurate because OpenSea does not control or administer wallets, nor does it have any KYC requirements. However, users can add an email address to their OpenSea account to receive notifications about sales etc, which could theoretically be linked to an identifiable individual. For example, a thief might use the same email address on OpenSea (which has no KYC) and on the exchange Coinbase (which does have KYC), and could be identified that way.

Stablecoins

In addition to Bitcoin, Ethereum and others, there is a niche category of cryptoassets called 'stablecoins' which are cryptocurrencies whose value is pegged to a currency, most commonly the US dollar. The top 10 USD stablecoins have a market capitalisation of $US160bn, most of which are ostensibly redeemable for cash, commodities or other cryptoassets. Part of the function of these cryptoassets is to avoid banks or credit cards in every transaction. They also allow international transactions denominated in USD (or EUR or GBP) to take place almost instantly, 24/7, and at very low cost, between users who do not have USD-denominated bank accounts.

However, these cryptoassets are typically heavily centralised, meaning that they are controlled by a single entity which may have the power to freeze funds: In response to US government sanctions, Circle, which operates the second largest stablecoin USDC, recently blacklisted several addresses holding USDC linked to a transaction mixing/anonymisation service. This means that the USDC in those addresses is frozen. In theory if a person has their USDC stolen they could apply for a proprietary injunction, and even if the USDC is held in a private address to which only the wrongdoer has the keys, Circle could freeze the funds. The same would apply for the providers of other popular stablecoins such as Tether (USDT) and Binance (BUSD).

Conclusion

Obtaining injunctive relief against cryptoassets, from Bitcoin to NFTs, is not a dark art limited to shadowy super coder-solicitors, despite their technical nature and novelty. While there are clearly some practical hurdles, there are also significant advantages because, given their public nature and traceability, monitoring and rapidly responding to disposals is far easier than with traditional assets, which relies on disclosure from banks and HM Land Registry, which often comes too late. **NLJ**

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