Decrypting Cryptocurrencies: Why Borderless Currencies May Benefit from Borderless Dispute Resolution

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Cryptocurrency is a term that is becoming increasingly familiar. But how many of us have considered its implications for the world we live in—let alone for the practice of international arbitration?

Cryptocurrencies—essentially digital cash—and the blockchain technology on which they are built, have the potential to revolutionise the way funds are raised, traded and stored. Cryptocurrency transfers are not only faster, simpler, and less expensive than those offered by many financial services companies, but processing cryptocurrency transactions is also far cheaper than the cost of many traditional payment systems.

In June 2017, the total market capitalisation for all cryptocurrencies surpassed US$100 billion, while trading between cryptocurrencies has grown to in excess of US$2 billion a day. So mainstream have cryptocurrencies become that a number of international law firms have confirmed that, in principle, they would accept payment of their fees in cryptocurrency.

With the proliferation in the use—and potential abuse—of cryptocurrencies, the possibility for disputes can only increase—and with it, the need for an effective and efficient means of "off-blockchain" dispute resolution.

Decrypting cryptocurrencies

Cryptocurrencies are digital currencies. But unlike a fiat currency, the value of which is backed by a third-party institution (such as a central bank), cryptocurrencies are a decentralised digital asset represented by line items on a distributed public ledger called blockchain. Instead of relying on a financial institution to record transactions, blockchain leverages the resources of large peer-to-peer networks to verify and confirm each cryptocurrency transaction.

Blockchain ledgers are described as "distributed" because financial information is stored across multiple sites (which can be anywhere in the world), without the need for a central administrator. Every time a cryptocurrency transaction is made, that transaction is verified, confirmed and stored on a cryptographically secure public ledger—or "block"—that is linked to the preceding block, thus creating the blockchain. The blockchain is replicated across the entire network of peers, thus allowing parties to transact securely without a third-party intermediary.

The largest—and most widely known—cryptocurrency remains bitcoin, which was invented in 2009 by the still unidentified Santoshi Nakamoto. However, there are now over 900 different digital currencies, with bitcoin now representing less than half the world's total cryptocurrency value.

Initial Coin Offerings and other potential cryptocurrency disputes

One of the most innovative and growing uses of cryptocurrencies is as a means to crowdfund investment capital via an Initial Coin Offering (ICO).

In an ICO, a company sells digital coins or tokens in exchange for payment in cash or an established cryptocurrency. The coin or token may function like a share, giving its owner an equity stake in the issuing company, with voting rights and a right to dividends. Alternatively, coins may operate more like points earned in a retailer loyalty programme, enabling their owner to access particular features (for example, goods or services) offered by that company.

In either case, like a share, the value of the coin or token can increase if the business is successful. In theory, it can then be traded globally on exchanges that handle cryptocurrencies. And as with any venture where funds are put at risk by investors, uncertainties as to the allocation of that risk, or the basis on which the risk was assumed, can give rise to disputes.

For instance, in order to attract investment, a company launching an ICO will provide certain information about its business, which may include an offering memorandum or prospectus, in some respects comparable to an offering circular issued by a company engaging in a rights or bond issue. Arbitration clauses could be the logical dispute resolution mechanism to include in such documents.

It is not just a possible breach of the terms and the conditions of these memoranda that could give rise to a claim. The manner in which an ICO is conducted also has the potential to form the basis of a dispute.

To take a recent example, in an ICO conducted earlier this year, network congestion resulting from high subscriber demand prompted the issuing company to keep the offering open for longer that it had initially planned. This resulted in complaints from early investors who argued that, in consequence, the funds raised had been allowed to succeed the issuer's capped target, with the effect of decreasing the value of the coins purchased prior to reaching that target. Again, given the international profile of ICO investors, arbitration could provide the most effective means of resolving such disputes.

The potential for cryptocurrency disputes does not stop at ICOs. Despite the security provided by end-to-end encryption, there remains the possibility for disputes arising out of failures in the underlying blockchain system itself. Last year, in a high-profile hacking incident involving the popular Ethereum cryptocurrency platform, a hacker siphoned off millions of dollars worth of cryptocurrency contributed by investors. Investors who suffer harm arising from similar failures in the blockchain underlying their cryptocurrency investments may naturally wish to seek damages from the platform provider.

Finally, while uncertainty remains as to whether cryptocurrency-based economic activities can be classified as "investments" for the purposes of the existing investment arbitration regime, the rush of certain States to regulate—and even ban—cryptocurrency investment means that investment arbitration may well yet be deployed as a means to resolve regulatory disputes.

Arbitration as a means of resolving cryptocurrency disputes

Although the cryptocurrency industry is still relatively nascent, it has the potential for significant growth. As some cryptocurrency providers have already recognised, disputes arising from borderless

currencies may be best served by a commensurately borderless form of international dispute resolution.

Not only does international arbitration offer a neutral alternative to domestic courts and result in an award that is enforceable in 157 countries under the New York Convention, it also allows cryptocurrency issuers and investors to choose expert decision-makers equipped to deal with technically complex disputes, as well as protect the confidentiality of sensitive proprietary information. Indeed, arbitral rules could be specifically tailored to suit the peculiarities of cryptocurrency disputes, just as they have been for, amongst other things, intellectual property disputes and disputes arising from the space industry.

However, a recent survey by the Silicon Valley Arbitration and Mediation Center suggests that while lawyers in the tech sector are increasingly likely to use international arbitration over litigation—with key benefits identified as specialist expertise, time to resolution, and increased privacy—only 35% had actually used arbitration in their last claim, compared to 44% for litigation and 37% for mediation.

There is, therefore, a pressing need for arbitration practitioners to promote the benefits of arbitration to the tech community, including those involved in developing and investing in cryptocurrencies. As a starting point, there would appear to be scope to develop model arbitration clauses tailored to cryptocurrency disputes, and to ICOs in particular, and to examine what (if any) modifications to institutional rules may be required to accommodate such disputes better. This could include, for example, providing for a list of specialist arbitrators able to handle the unique questions generated by cryptocurrency-related disputes. These might include complex conflict of laws issues, arising from the tension between international law, domestic regulatory regimes and the governing law of any relevant contractual agreement(s).