

Kluwer Arbitration Blog

Crypto Arbitration: A Survival Guide

Edward Taylor (Shearman & Sterling LLP), Jennifer Wu (Pinsent Masons LLP), and Zach Li (AlixPartners LLP) · Thursday, September 29th, 2022

As the Crypto Winter's chilling effect continues to be felt across the crypto sector, with crypto assets having declined in value by approximately **US\$ 2 trillion** since their 2021 peak, international arbitrations over disputes related to crypto assets ("Crypto Arbitrations") look set to multiply in 2022. This post provides an introduction to the types of challenges, whether legal, practical or valuation related, that arise in Crypto Arbitrations.

Decrypting Crypto Disputes

Crypto disputes come in all shapes and sizes. Some may raise novel legal issues such as what law applies to a blockchain transaction in the absence of a governing law clause or whether a binding dispute resolution clause can be embedded in a smart contract.

However, where the disputing parties' relationship is governed by a traditional contract, which will frequently be the case, lawyers will already be familiar with many classes of crypto disputes, and the legal issues they raise, because they also arise in the context of other types of disputes:

- investment (e.g., seed capital and venture capital investments in crypto platforms; shareholder disputes associated with such investments);
- financial transactions (e.g., margin calls against traders and/or forced close-outs of trades by crypto exchanges; failure of crypto platforms to return non-fungible tokens ('NFTs') or other crypto assets provided as collateral for loans of cryptocurrencies);
- supply of services (e.g., service outage claims by crypto exchange users);
- sale of goods (e.g., defective, or delayed supply of, bitcoin mining equipment);
- fraud and mis-selling (e.g., misrepresentations as to the nature or value of reserve assets behind 'stablecoins');
- outstanding debts (e.g., failure of crypto hedge funds to repay loaned crypto assets); and
- intellectual property (e.g., use of artworks for NFTs without copyright licences).

Although the substantive legal issues that arise in crypto disputes may therefore be familiar to lawyers, the same will often not be true of disputed factual issues. For example, input from industry experts may be required for lawyers to understand how a DeFi platform's risk management system operates and whether it is in line with market practice. Accordingly, like in construction disputes, lawyers may find it necessary to obtain expert advice to fully evaluate the

merits of their client's case.

Crypto Arbitration Challenges

Many crypto businesses include arbitration agreements in their contracts. This is unsurprising, both conceptually and practically. Conceptually, crypto's decentralised ethos sits well with arbitration's focus on party autonomy and (relative) freedom from national court interference. Practically, the features that make arbitration well-suited to resolving cross-border disputes apply equally to crypto disputes, including procedural flexibility, neutrality, confidentiality, the ability to appoint arbitrators with relevant experience and, subject to the public policy point described below, international enforceability of awards.

Crypto Arbitrations can nevertheless be challenging for lawyers and their clients. Examples of five challenges are set out below.

1. Crypto Regulation, Arbitrability and Public Policy

Mainland China, Russia and Qatar, among other jurisdictions, have banned crypto assets or heavily regulated their use. If a Crypto Arbitration is seated in such a jurisdiction, or enforcement of an award is sought there, national courts may rule that crypto disputes are not arbitrable or deny enforcement of awards on public policy grounds. Indeed, in 2020, a court in Mainland China set aside an award concerning a cryptocurrency dispute on public policy grounds.¹⁾ Similarly, in 2021, an appellate court in Greece confirmed a court of first instance's judgment that had refused enforcement of an award denominated in bitcoin on public policy grounds.²⁾

Sometimes such risks may be mitigated through careful drafting of a party's request for relief. For example, depending on the jurisdiction, requesting an award of damages quantified in fiat currency of equivalent value to the crypto currency in dispute, rather than the crypto currency itself, may reduce the likelihood of enforcement being denied.

2. Identifying the Correct Counterparty to the Arbitration

Crypto businesses are sometimes organised and operated in an opaque manner. It may not be apparent, based on publicly available information, whether a business uses a conventional corporate structure (e.g., parent company / subsidiary relationship) or even the jurisdiction(s) in which it is based.

This can create challenges for Crypto Arbitrations, including with respect to identifying the parties to the arbitration agreement and their role, if any, in the dispute. For example, [Binance's User Terms](#) contain an arbitration agreement between the user and "Binance Operators", explored further [here](#). This open-ended definition includes but is "not limited to legal persons (including Binance UAB), unincorporated organizations and teams that provide Binance Services and are responsible for such services". When a dispute arises, Binance's User Terms make the claimant party responsible for determining the "counterparties" to the dispute "depending on the specific services you [the claimant] use and the particular actions that affect your rights or interests". Absent joint and several liability, arbitrating against the wrong party could lead to a tribunal rejecting an otherwise valid claim.

Once the correct party or parties have been identified, thought should also be given to their ability to ultimately satisfy an award for damages since the Crypto Winter has negatively impacted many crypto businesses' finances. Arbitrating against a party on the verge of financial collapse may be of limited use.

3. *Securing Interim Measures Over Crypto Assets*

Crypto businesses' main assets are generally not traditional assets, like real estate, but crypto assets. Interim measures can therefore be essential in Crypto Arbitrations given the potential for crypto assets to be dissipated in seconds, with only a few mouse-clicks.

While the legal issue of whether crypto assets are "*property*" remains controversial in many jurisdictions, this has not stopped courts in Hong Kong³⁾ and Singapore⁴⁾ from granting proprietary injunctions over crypto assets. English courts have also been prepared to grant injunctions over crypto assets.⁵⁾ Indeed, the English courts have shown an admirable willingness to embrace technology in the context of crypto disputes, including by allowing proceedings to be served via an NFT on the blockchain.⁶⁾

Emergency arbitration may also offer a viable method for obtaining interim measures over crypto assets, particularly where emergency arbitrators are prepared to grant urgent 'preliminary orders'.⁷⁾

4. *Valuation Challenges*

Valuing crypto currencies can be straightforward since there are frequently readily available quoted prices similar to observable commodity prices. However, difficult issues can arise where the crypto currency is illiquid, including with respect to the bid-ask spread and purchase price premium.

Valuing crypto businesses may also pose problems. One key challenge is the lack of comparable publicly listed companies with sufficient and robust financial information to conduct a market-based valuation. Taking the crypto exchange industry as an example, the only major publicly listed exchange is Coinbase and its market observed pricing data only goes back to 14 April 2021 when it was publicly listed.

Another key challenge is assessing a crypto business' future prospects at the valuation date and identifying corresponding implications on the key value drivers. For example, in an exchange, higher trading volume will generate higher transaction revenue and profit, resulting in a higher valuation. Forecasting future trading volumes may not be straightforward where the valuation date falls in a period of significant market volatility as seen during the Crypto Winter.

Indeed, with the sharp decline in cryptocurrency values since 2021, the choice of valuation date can significantly impact the quantification of damages. Similarly, given this market volatility, the damages available under a tort claim may be very different from those under a contractual claim given the different measures of damages that can apply to such claims.

5. *Arbitration Rules and Class Actions*

Most institutional arbitration rules are already sufficiently flexible to allow arbitrators to adapt procedures suitable for Crypto Arbitrations. However, their limits are already being tested in

certain respects, with one hot topic being class-action style disputes. For example, when a crypto exchange experiences an outage, there may be hundreds of impacted parties, each with a relatively small claim against the exchange. Class-actions could help address access to justice concerns in these situations since it would otherwise be uneconomical for each individual party to bring a separate arbitration. Whether the creative application of joinder and consolidation mechanisms in arbitration rules, for example, can accommodate class-actions remains to be seen.

Conclusion

Crypto Arbitration is still at an early stage of development. This post has identified several challenges but others will undoubtedly emerge over the coming months as arbitral tribunals and national courts are exposed to more crypto disputes. It will be interesting to see how these challenges are addressed and also how much traction competitors to traditional arbitration, like decentralized blockchain-based arbitration services such as [Kleros](#) (explored [here](#)), can gain in the burgeoning crypto dispute market.

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- ?7 See *Prime Finance Arbitration Rules 2022*, Article 25(7).

This entry was posted on Thursday, September 29th, 2022 at 8:46 am and is filed under [Crypto](#), [Cryptocurrency](#), [Technology](#)

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