International Insolvency & Restructuring Report 2024/25

capital markets intelligence

cmi

Crypto asset recovery and restructuring: lessons from the Crypto Winter in Singapore

By Manoj Sandrasegara, Lionel Leo, Daniel Liu, Clayton Chong, Adnaan Noor, Eden Li and Muhammed Ismail, Wong Partnership

Singapore has had its fair share of crypto insolvencies in these recent years, a corollary of establishing itself as one of the world's cryptocurrency hubs during the pandemic-era boom. In this article, we examine below how the legal regime in Singapore was deployed in the aftermath of 2022's 'crypto winter'. The developments in the law have wider application beyond the crypto context, and will play a pivotal role in asset tracing, preservation and recovery and debt restructuring strategies moving forward.

Cryptocurrencies have staged a stunning recovery in the first half of 2024, recovering the ground lost during the 'crypto winter' of 2022. Bitcoin has rallied to all-time highs, propelled by record inflows into spot Bitcoin exchange-traded funds launched by the likes of BlackRock and Fidelity Investments. The wider crypto market too has boomed, with the largest 100 coins reportedly up roughly 70 per cent this year.

Does the blistering 'crypto summer' of 2024 portend another 'crypto winter' in an endless seasonal cycle? How has the legal system been deployed to deal with the challenges posed by crypto collapses?

Crypto insolvencies seen in Singapore include Three Arrows Capital (hedge fund), Hodlnaut (bank and exchange services), Babel (lending, asset management and trading), Genesis (lending and borrowing, spot trading, derivatives and custody services), and Zipmex (exchange platform). Many of these cases came before the Singapore courts and provided the courts with the opportunity to address a myriad of issues.

Asset tracing, preservation and recovery

A common theme of cryptocurrency insolvencies, exemplified by cases like FTX, is the lack of accurate record keeping, deficient internal controls and opaqueness around asset ownership and segregation. These factors amplify the risk of misappropriation of assets, and concomitantly, the need for robust tools for asset tracing, preservation and recovery.

Investigative powers

The liquidation of Three Arrows Capital ("**3AC**") illustrates how the Singapore regime can be leveraged on to conduct investigations as part of a cross-border asset tracing strategy. 3AC was a hedge fund incorporated in the British Virgin Islands ("**BVI**"), which at one point managed assets valued in the region of US$10bn. 3AC was placed into liquidation in the BVI. The BVI liquidators sought recognition of the BVI liquidation in Singapore under the UNCITRAL Model Law on Cross-Border Insolvency.

Under the Singapore recognition order, the liquidators applied for and were granted information gathering powers that were co-extensive with those available to a Singapore insolvency officeholder. In particular, the Singapore insolvency legislation that certain third parties have a duty to cooperate with liquidators to provide information relating to the promotion, formation, business, dealings, affairs, property, rights, obligations or liabilities of the company in liquidation. The legislation also made the breach of this duty a criminal offence. The liquidators successfully obtained an order, within the Singapore recognition order, extending this duty of cooperation to the liquidators. However,

the breach of this duty of cooperation would not lead to criminal penalties. Instead, the liquidators were given the power to apply for an injunction compelling third parties to cooperate. If the third parties disobeyed the injunction, they could be liable to contempt of court.

In addition, the Singapore insolvency legislation empowered liquidators to apply to court for orders to summon officers of company or any person known or suspected to have in his or her possession any property of the company (among others) to be examined on oath, to provide an affidavit and/or to produce any books, papers or other records in the person's possession or under the person's control relating to the company's affairs. The liquidators successfully obtained an order, within the Singapore recognition order, empowering them to bring such an application in the same way that the liquidator of a Singapore liquidation could.

The liquidators relied on these powers to successfully obtain information disclosure orders against various parties. One issue that the liquidators faced was obtaining information from the founders of 3AC, whose locations were for the most part unknown; and there was the associated difficulty of obtaining orders against parties that may not be physically within the jurisdiction. However, a related company that had acted as the investment manager (and sole shareholder) of 3AC was a Singapore company, and the founders were its only two directors. Accordingly, the liquidators managed to obtain information disclosure orders against the related company, but also against the founders personally in their capacity as the only directors of the related company. When the founders disregarded and breached the information disclosure orders, and the liquidators commenced proceedings to commit the founders for contempt of court.

In a prime demonstration of the no-nonsense enforcement regime in Singapore, the court sentenced the founders to four months' prison. One of the founders was arrested at Singapore's international airport while attempting to travel out of the country and was sent to prison, though the other founder's whereabouts were unknown.

Critically, since one of the founders was now undoubtedly within the jurisdiction as he served his imprisonment term, the liquidators brought a further application to examine him in court, which was granted, and the liquidators' counsel conducted a 2-day examination of this founder to obtain information regarding the affairs, business and property of 3AC.

Asset preservation injunctions against "persons unknown"

In two landmark cases, the Singapore courts granted injunctions prohibiting the disposal of cryptocurrency assets against persons whose identities were unknown, and disclosure orders to facilitate asset tracing efforts.

In the first case, *CLM v CLN* [2022] 5 SLR 273 ("***CLM***"), the plaintiff had substantial amounts of Bitcoin and Ethereum stolen from him. The stolen assets were funnelled through a series of digital wallets which had negligible transactions and appeared to have been created solely for the purpose of frustrating tracing and recovery efforts.

Even though the plaintiff did not know the identify or location of the wrongdoers, it sufficed for him to provide a description of the wrongdoers for the purposes of naming the defendant for the suit. The defendant(s) in *CLM* were described as "*any person or entity who carried out, participated in or assisted in the theft of the Plaintiff's Cryptocurrency Assets on or around 8 January 2021, save for the provision of cryptocurrency hosting or trading facilities*". The court considered this description sufficiently certain in its scope.

A freezing injunction and interim proprietary injunction were granted by the court against this category of persons to prohibit the dissipation of the stolen cryptocurrency assets.

Crucially, the plaintiff was also able to trace a portion of the misappropriated assets digital wallets that were controlled by cryptocurrency exchanges with operations in Singapore. The plaintiff did not bring substantive claims against

the exchanges, believing them to be innocent third parties, but sought disclosure of information and documents collected by the exchanges in relation to the accounts which received the stolen Bitcoin and Ethereum and details of transactions involving these accounts. The disclosure orders were granted to facilitate the identification of the defendants or any persons that may have assisted or acted in concert with them.

As a result of investigations and disclosure by the exchanges, the plaintiff identified two foreign nationals associated with the accounts that received the stolen assets and sought to join them as defendants in the proceedings. The court held that it was impractical to require the plaintiff to effect personal service of the court papers on them, as their physical whereabouts were unknown and they had used virtual private network services to obscure their physical locations. Instead, the court permitted the use of substituted service by email to email addresses tied to their crypto accounts with the exchanges.

In the second case, *Janesh s/o Rajkumar v Unknown Person ("CHEFPIERRE")* [2023] 3 SLR 1191, the claimant was the owner of a Bored Ape non-fungible token ("**NFT**") that he put up as collateral for a loan he obtained from the defendant on a cryptocurrency lending marketplace. When the loan was nearing the maturity date, the claimant and defendant agreed to enter a refinancing loan. However, the defendant subsequently changed his mind, foreclosed on the collateral, and transferred the Bored Ape NFT out of the marketplace escrow account into his cryptocurrency wallet.

Similar to *CLM*, the claimant commenced the claim against the defendant, even though he did not know the identity of the defendant. The claimant was only known through his handle "chefpierre.eth", which the court found to be a sufficiently certain description for the purpose of naming the defendant for the action. Given the practical impossibility of effecting personal service on an unknown person, the court permitted substituted service on the defendant through the defendant's Twitter and Discord accounts, and through the messaging function of the defendant's cryptocurrency wallet address. The court granted an interim proprietary injunction prohibiting the disposal of the NFT.

Restructuring toolkit

The spate of crypto restructurings in 2023 has also spawned the use of innovative deal structures and elements which will have much broader application beyond the crypto space.

Substantive consolidation

In *Re Babel Holding Ltd* [2023] SGHC 329 ("***Babel***") (see also *Re Babel Holding Ltd* [2023] SGHC 98), the court confirmed that a Singapore scheme of arrangement can pool the assets and liabilities among different entities within a corporate group to effect a global restructuring of the group. The pooling of assets and liabilities is referred to as "substantive consolidation".

Substantive consolidation is not permissible in every situation, but would be appropriate only where the affairs of the group companies are hopelessly intertwined, the legitimate interests of creditors are not unfairly overridden and the restructuring demonstrably benefits the affected creditors.

The court in *Babel* was satisfied on the evidence of the debtor's financial advisors that the affairs of the group were so hopelessly intertwined that a pooling of their assets was the only sensible way to proceed. The financial advisors opined that they were unable to distinguish what remaining cash and crypto assets belong to which entities within the group. It was also said that vast expenditure and time would be needed to identify which entity in the group owns the money and cryptocurrency, which the group could not afford.

The lack of clarity on asset ownership and segregation is not peculiar to Babel, or crypto cases for that matter. Corporate groups may sometimes end up in tangled webs of intercompany transactions over the course of its regular dealings. The availability of substantive

consolidation enhances the utility of the Singapore regime in restructuring corporate groups. It also represents a further step on the path laid in *Re DSG Asia Holdings Pte Ltd* [2022] 3 SLR 1250 which approved the use of deed poll structures to restructure a corporate group's debts under a single scheme of arrangement.

Administrative convenience class

In *Re Zipmex Pte Ltd and other matters* [2023] SGHC 88 ("***Zipmex***"), the court approved the creation of an "administrative convenience" class of creditors which would not have to vote on the proposed scheme, but could opt in to vote if they wished. The practical significance of creating an administrative convenience class is that it enables greater execution certainty in restructuring deals where the vast majority of debt is controlled by a small number of creditors.

The Zipmex group sought to restructure through a "pre-packaged" scheme of arrangement. A pre-packaged scheme of arrangement is an expedited procedure for implementing a scheme of arrangement, which avoids the need for convening a creditors' meeting to vote on the proposed scheme, provided the scheme proponent can lock-up sufficient consents to cross the required approval thresholds (75% in value and majority in number).

The difficulty faced by the Zipmex Group was that a significant portion of their creditor base comprised customers with relatively small claims. There were approximately 67,000 customers whose withheld assets were below US$5,000 in value. Though the supermajority in value of debt was held by a relatively small number of creditors, the headcount requirement (i.e. a majority in number of creditors) would have been entirely determined by Zipmex's customer-creditors.

Given the practical impossibility of locking up the votes of 67,000 customers, Zipmex proposed the creation of an administrative convenience class comprising the customers, who would be excluded from the voting exercise unless they opted in. The customer creditors would receive full access to their withheld assets after a liquidity injection into Zipmex Asia by a white-knight investor.

To facilitate the creation of the administrative convenience class, the court dispensed with the headcount requirement using its discretion under section 210(3AB) of the Companies Act 1967. With the dispensation of the headcount requirement, it was not necessary for the Zipmex Group to demonstrate that a majority in number of the customers would have voted for the scheme, and hence the pre-packaged scheme could be approved on the back of the supermajority-in-value creditors' approval of the scheme.

Conclusion

The developments and demonstration of the tools available in Singapore borne out of the 2022 crypto winter have charted a path for the next down-cycle, be it crypto or otherwise. Insolvency office-holders and debtor companies overseas and in Singapore can leverage these strategies and tools under Singapore law with a view to maximising value for creditors. The Singapore courts have displayed a willingness to facilitate the global tracing, preservation and recovery of misappropriated cryptocurrency assets, and where appropriate, employing novel features in schemes of arrangement to promote effective restructuring outcomes.

Authors:

Manoj Sandrasegara, Partner
Tel: +65 64168106
Email: manoj.sandra@wongpartnership.com

Lionel Leo, Partner
Tel: +65 6517 3758
Email: lionel.leo@wongpartnership.com

Daniel Liu, Partner
Tel: +65 6416 2470
Email: zhaoxiang.liu@wongpartnership.com

Clayton Chong, Partner
Tel: +65 6416 2472
Email: clayton.chong@wongpartnership.com

Adnaan Noor, Partner
Tel: +65 6416 2477
Email: adnaan.noor@wongpartnership.com

Eden Li, Partner
Tel: +65 6517 3766
Email: eden.li@wongpartnership.com

Muhammed Ismail Noordin, Partner
Tel: +65 6517 3760
Email: muhammedismail.konoordin@wongpartnership.com

WongPartnership LLP
12 Marina Boulevard Level 28
Marina Bay Financial Centre Tower 3
Singapore 018982
Tel: +65 6416 8000
Web: www.wongpartnership.com