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New Zealand court rules on cryptocurrency

Scott Barker and Brooke Marriner report on the recent case in New Zealand regarding cryptocurrency



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The New Zealand High Court in *Ruscoe v Cryptopia Ltd (in liq)* [2020] NZHC 728, [2020] 2 NZLR 809 found that cryptocurrencies are a form of property capable of being held on trust.¹ The judgment is understood to have been the first in a common law jurisdiction to consider the categorisation of cryptocurrency after a fully contested hearing.

Legal arguments were presented on behalf of the liquidators of the cryptocurrency exchange, and court appointed senior counsel representing account holders and unsecured creditors respectively. The judgment also addressed the distinction between mere information and property – a useful framework in today's digital age.

Background

From 2014, Cryptopia operated as a cryptocurrency trading exchange. In January 2019, its servers were hacked and approximately USD30 million in cryptocurrency was stolen. It was placed into liquidation in May 2019. Aside from the digital assets held for accountholders,

Cryptopia's assets totalled approximately NZD5.4 million, and liabilities totalled approximately NZD12.7 million.

The liquidators asked the Court to determine:

- whether the cryptocurrencies held by the liquidators constituted "property" capable of forming the subject matter of a trust; and
- if it is, what are the terms and consequences of that finding?

Cryptocurrency is property capable of being held on trust

First, the definition of "property" in New Zealand's Companies Act 1993 (governing the liquidation process) is wide, encompassing "*rights, interests and claims of every kind in relation to property however they arise*".

Second, Gendall J considered recent case law from several jurisdictions where proprietary rights had been asserted over cryptocurrency.

Finally, Gendall J considered whether cryptocurrencies satisfied the four criteria of "property" set out by Lord Wilberforce in *National Provincial Bank Ltd v Ainsworth* [1965] AC 1175 (HL). He considered that they did:

cryptocurrency is definable, identifiable by third parties, capable in nature of assumption by third parties, and has some degree of permanence or stability. In particular, "*They obtain their definition as a result of the public key recording the unit of currency. The control and stability necessary to ownership and for creating a market in the coins are provided by the other two features — the private key attached to the corresponding public key and the generation of a fresh private key upon a transfer of the relevant coin.*"

An assertion that cryptocurrencies were "mere information" was too simplistic an analysis: their entire purpose is to create an item of tradeable value, not simply to record or impart knowledge. Relevantly, currencies stored in wallets were protected by a private key, every transaction used a unique code, and a crypto asset could only be assigned once.

All coins were held on express trust

Gendall J considered the three elements required for a trust:

- 1) **Certainty of subject matter.** Cryptopia kept and stored the private keys

associated with the wallets of each cryptocurrency – accountholders did not know the private key associated with any wallet. The subject matter of the various trusts was clearly recorded in Cryptopia's databases.

- 2) **Certainty of objects.** The beneficiaries were those with positive coin balances for each currency (relevantly, evidential uncertainty does not defeat a trust).
- 3) **Certainty of intention.** Cryptopia's terms provided that *“each user's entry in the general ledger of ownership of coins is held by us, on trust, for that user.”* Cryptopia manifested its intent by creating the exchange without providing to accountholders the details of the public and private keys for the coins it held for them. Its databases showed that the company was custodian and trustee of the assets and Cryptopia did not

intend to (and nor did it) trade those assets in their own right. Relevantly, Gendall J concluded that it was not necessary for all terms of the trust to be expressly recorded – the law would fill the gaps by implication.

Terms and consequences of trust

A trust came into existence for each cryptocurrency as soon as Cryptopia came to hold a new coin on behalf of its accountholders. Cryptopia's duties were that of a bare trustee: to hold the relevant pools of currency on behalf of the accountholders, to follow their instructions, and to allow accountholders then to increase or reduce their beneficial interest in accordance with the system Cryptopia had created for that purpose.

If the liquidators are unable to ascertain the identity of an accountholder, the coins

associated with that account would fall to be dealt with under s 76 of the Trustee Act 1956. They would not become available to Cryptopia's creditors.

Whether something is “property” has important ramifications in insolvency law, succession law, trust law and the availability of proprietary remedies (which are absolute). The decision is a welcome one for those investing in digital assets, but also for data protection more broadly. ■

Footnotes:

- 1 The New Zealand Court of Appeal implicitly endorsed the finding that cryptocurrency was property, when later in 2020, it permitted a cryptocurrency to be provided to the court as security for an undertaking in damages in support of a freezing order. See *MB Technology Ltd v Ecomi Technology Pte Ltd* [2020] NZCA 363.

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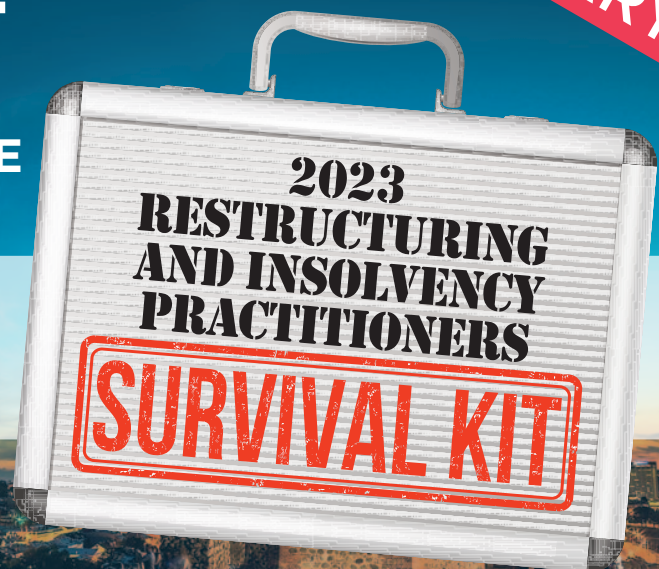
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