

## “WINTER IS COMING” – HOW TO OBTAIN LITIGATION FUNDING FOR CRYPTOCURRENCY DISPUTES

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In 2022, the value of popular cryptocurrencies plummeted precipitously on account of a perfect storm of events, namely, the failure of the TerraUSD/Luna “stablecoin” and its contagion effect on Three Arrows Capital, Voyager Digital and Celsius Network, as well as FTX’s collapse which also brought crypto lender BlockFi down with it. The term “crypto winter” was coined, with the resulting loss to investors estimated at USD 42 billion (or more).

With recent revelations pointing to possible fraud and mismanagement at these crypto businesses, it is unsurprising that a spate of lawsuits and arbitrations are on the broil in multiple jurisdictions. Disgruntled investors, having lost significant amounts of money, are turning to litigation funders to provide funding to pursue these claims and recover their losses. This article is intended to be a high-level primer for parties seeking to obtain litigation funding, by looking at some of the criteria that funders apply when considering whether or not to fund a crypto dispute.

### Will winter turn to summer? Recoverability and collection

A fundamental consideration when it comes to funding any dispute is whether a defendant can, or will, satisfy an award or a judgement. Crypto disputes present a unique challenge because of the inherent volatility of cryptocurrency itself: if the capital adequacy of a defendant is tied to the value and quantity of cryptocurrency held by it, there may be uncertainty around whether it can satisfy an award for damages. This may be compounded in fraud or mis-selling claims, where there is a risk of dissipation of assets into dormant or cold wallets to thwart a successful litigant.

From a funder’s perspective, a claim becomes more viable if the defendant has cash reserves, or at least fiat-backed stablecoins that are pegged to the US dollar, to hedge against the risk of non-payment on account of a market downturn. Indeed, even better if a claimant (or a class of claimants) is able to obtain interim freezing injunctions to prevent the disposal of assets, or an order compelling payment into court.



Understandably, such measures cost money which impecunious litigants and retail investors are unlikely to have. If a funder is convinced that these interim measures will succeed (and that the overall merits of the claim are also good), preliminary funding can be provided as part of a larger facility to enable a claimant or group of claimants to obtain such relief and improve the overall prospects of success of the case.

### Picking the “right” case

Crypto disputes tend to fall within three broad categories:

- (a) Claims based on misrepresentation as to the stability and safety of certain crypto currency, such as the representative action in the Singapore High Court brought by retail investors against the founders of Terra/Luna.
- (b) Disputes relating to corporate transactions or abortive M&As, which are essentially contractual in nature.
- (c) Claims arising out of the insolvency or bankruptcy of crypto businesses.

A funder will undertake a fulsome assessment of the legal merits of a claim, including a detailed examination of the evidence available. There is a strong preference for clear documentary evidence to prove a claim, as opposed to one that is heavily reliant upon witness testimony.

Other considerations include forum, dispute resolution method (arbitration or litigation) and governing law as these inform the legal elements that need to be satisfied for a claim to be made out, the admissibility of certain types of evidence, and the availability of certain remedies (both interim and final).

For example, in certain jurisdictions like Canada, there is securities legislation available that makes the bringing of statutory claims in misrepresentation less arduous than under the common law by virtue of dispensing with the requirement to prove reliance.

Therefore, it is crucial for claimants to obtain a legal opinion on the merits of their claim when making an application for funding. A funder will also require a comprehensive budget from the lawyers acting for the claimants, which should be proportionate to the quantum of the claim envisaged. In this regard, funders appreciate lawyers who are prepared to undertake such work as part of a broader conditional fee arrangement with their clients, as that signals an alignment of interest and the sharing of risk with both clients and the funder.

### **Funder's return**

A key feature of litigation funding is that it is generally provided on a non-recourse basis (i.e. if the case is unsuccessful, the funder loses its investment and has no right of recourse against the funded party). The funder's return is derived from the proceeds of the dispute only. A typical return structure that funders employ is the combination of a reimbursement of invested capital (or "funded costs") and a "higher of" of a multiple of funded costs or a percentage of the recoveries, which progressively increases with the effluxion of time. The multiples and percentages charged by a funder are reflective of the overall risk associated with the case.

It is also important to note that the reimbursement of funded costs and the return are paid in priority to the funder from any recoveries before the net proceeds are distributed to the funded party. Each funding agreement is bespoke to meet the requirements of a claimant. For example, a funder may be prepared to cover historic legal spend or advance working capital as against the claim or consider funding a portfolio of multiple claims.

Parties who have put their claims on ice would thus be wise to consider litigation funding as fuel to light a fire to survive, or even thrive, in this long and dark crypto winter.



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