

Tiptoeing through the tulips

Could software developers be held accountable in cryptocurrency hacking cases? Lauren Pardoe considers the definition of 'fiduciary' in a fast-developing area of the law



IN BRIEF

- ▶ A recent jurisdiction challenge has raised the question of whether cryptocurrency network developers are accountable as fiduciaries.
- ▶ The Court of Appeal concluded it is possible for developers to meet the fiduciary definition.
- ▶ This may have implications for victims of cryptocurrency fraud.

Cryptocurrency is a new and fast-developing area, in which there has to date been little in the way of judicial intervention, and in which there is little regulation. The argument lies in whether the developers of cryptocurrency networks, working on behalf of bitcoin owners, are accountable as fiduciaries if such networks are hacked, as seen in *Tulip Trading Ltd (a Seychelles company) v Van Der Laan and others* [2023] EWCA Civ 83, [2023] All ER (D) 27 (Feb).

Case summary

This claim was brought by a Seychelles-registered company, Tulip Trading Ltd, which is the owner of some bitcoin (valued at approximately \$4bn as of April 2021), held across four cryptocurrency networks. The claim was brought against a number of software developers whom Tulip alleges had sufficient control over the cryptocurrency networks that they owed fiduciary duties to Tulip.

The claim arose when the owner and director of Tulip became aware in February 2020 that at some point prior to that date, the private cryptocurrency keys held by Tulip, which gave Tulip access to its bitcoin in the various cryptocurrency networks, had been hacked by persons unknown. Tulip had as a result lost its ability to access its cryptocurrency assets, which Tulip believes are still held within the networks, or move them out of reach of the hackers.

Tulip's case is that the developers control and run the networks in which the bitcoin is held. As such, they should be able to create

some form of software patch which would secure Tulip's assets, eg by moving the bitcoin to different locations within the network and providing Tulip with access. The developers argue that:

- (1) they have no such duty to Tulip; and
- (2) the solution sought by Tulip would be completely unworkable in practice.

Jurisdiction at first instance

The developers are based across a large number of jurisdictions, and so Tulip made an application to the court for service out of the jurisdiction, which was granted in May 2021. The developers disputed jurisdiction and the matter went to a hearing before Lady Justice Falk in March 2022.

“Whether the developers were in fact fiduciaries was a serious issue to be tried”

Falk LJ found that, for the purposes of the jurisdiction challenge, Tulip was resident in England and the damage arising from the alleged losses would be suffered in England. This was on the basis that, although it is registered in the Seychelles, Tulip's controlling mind and director was at all relevant times in England, and access to the assets was possible from England.

However, Falk LJ found that there was no serious issue to be tried because there was no realistic prospect of establishing that the facts pleaded amounted to a breach of fiduciary or tortious duty owed by the defendants to Tulip. The order allowing service out of the jurisdiction and the service of the claim form were therefore set aside.

Appeal

Tulip appealed the decision of the High Court, and the matter went to a hearing before the Court of Appeal on 7-8 December 2022. The developers did not contest Falk LJ's findings regarding the residence of Tulip within the jurisdiction, and so the only matter on appeal was whether there was a serious issue to be tried—namely whether there was a good arguable case that the developers could be held to have fiduciary duties.

In a judgment delivered by Lord Justice Birss and handed down on 3 February 2023, the Court of Appeal reversed Falk LJ's judgment, finding that there was a serious issue to be tried.

Birss LJ referred to the judgment in *AK Investment CJSC v Kyrgyz Mobil Tel Ltd and others and other appeals* [2011] UKPC 7, [2011] All ER (D) 144 (Mar) and the warning therein that it is not normally appropriate in a summary procedure to decide a controversial question in law in a developing area. Birss LJ agreed with Tulip that Falk LJ had erred in accepting the developers' arguments as to the networks' 'decentralisation', which should properly be a matter for evidence at trial.

The Court of Appeal then considered the standard definition of a fiduciary as set out in *Bristol and West Building Society v Mothew (t/a Stapley & Co)* [1998] Ch 1 at p18:

'A fiduciary is someone who has undertaken to act for or on behalf of another in a particular matter in circumstances which give rise to a relationship of trust and confidence. The distinguishing obligation of a fiduciary is the obligation of loyalty. The principal is entitled to the single-minded loyalty of his fiduciary. This core liability has several facets. A fiduciary must act in good faith; he must not make a profit out of his trust; he must not place himself in a position

where his duty and his interest may conflict; he may not act for his own benefit or the benefit of a third person without the informed consent of his principal. This is not intended to be an exhaustive list, but it is sufficient to indicate the nature of fiduciary obligations. They are the defining characteristics of the fiduciary.'

It was, however, noted that 'the facts of this case (whichever party is right about the details) are new and quite a long way from factual circumstances which the courts have had to examine before in the context of fiduciary duties'.

On the facts of Tulip's case, should they be made out at trial, the developers were found to have met the definition of fiduciaries because:

- ▶ they had a unique level of control over the cryptocurrency networks;
- ▶ they had a duty as controllers to put the interests of the bitcoin owners ahead of their own self-interest;
- ▶ they were the only parties with the ability to alter the software and fix any 'bugs'; and
- ▶ the bitcoin owners had a legitimate expectation that the developers would act in good faith.

It was noted that the categories of fiduciaries are not closed, and 'the common law often works incrementally and by analogy with existing cases, and rightly so; but if the facts change in a way which is more than incremental I do not believe the right response of the common law is simply to stop and say that incremental development cannot reach that far'.

The court's conclusion

Birss LJ concluded that: 'I recognise that for Tulip's case to succeed would involve a significant development of the common law on fiduciary duties. I do not pretend that every step along the way is simple or easy. However, there is, it seems to me, a realistic argument... [that if the facts of the case are found in Tulip's favour] the developers therefore are fiduciaries...'

The content of the duties... also involves a duty to act in positive ways in certain circumstances. It may also, realistically, include a duty to act to introduce code so that an owner's bitcoin can be transferred to safety in the circumstances alleged by Tulip.'

The Court of Appeal therefore concluded it was indeed possible under common law for the developers to meet the definition

of fiduciaries. The issue of whether the developers were in fact fiduciaries was a matter for evidence at trial, and was a serious issue to be tried.

Commentary

It is notable that this was a jurisdiction challenge only, and the matter of whether or not the developers are fiduciaries on the facts is yet to be tried. However, followers of cryptocurrency developments will be interested to see that the English courts are open to accepting jurisdiction for these claims (subject to the facts of the case) and to considering how fundamental legal principles can be applied and indeed extended in an ever-changing and ever more quickly developing world.

If it is found that the developers are fiduciaries, victims of cryptocurrency fraud, who currently have little opportunity to seek redress, may find themselves able to claim against developers or others for restitution of their assets. No doubt developers and cryptocurrency owners will be watching with interest.

NLJ

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