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Trends and Developments

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Pitfalls of Securing Cryptocurrencies under Swiss Law

Introduction

Initially only traded by a niche community, cryptocurrencies such as Bitcoin, Ether, Ripple, and Litecoin, to name a few, are growing in acceptance. Developments such as leading banks planning to offer their clients access to crypto investments, Tesla's recent US billion-dollar investment in Bitcoin and accepting it as payment for their cars, as well as Coinbase's recent IPO, mean the relevance of cryptocurrencies will also inevitably increase in asset-recovery proceedings.

Determining the available means to secure cryptocurrencies in Switzerland hinges on the legal qualification of the same under Swiss law which, in the absence of any case law, remains controversial among legal practitioners in Switzerland. While certain jurisdictions consider cryptocurrency as property, the situation is less clear under Swiss law, where a minority would like to qualify cryptocurrency as a chattel according to the Swiss Civil Code. The majority view, however, qualifies cryptocurrencies as a new asset category (assets sui generis). The prevailing qualification is similar under Swiss criminal law.

This article provides an overview of the most frequent practical pitfalls when attempting to recover cryptocurrencies by way of attachment in civil and/or criminal proceedings, which are among the most common recovery instruments.

Attachment in civil proceedings

The majority view considers cryptocurrencies as assets sui generis, and it is generally acknowledged that cryptocurrencies can be secured by way of civil attachment under the Swiss Debt Enforcement and Bankruptcy Law (DEBA).

According to Article 271 seq DEBA, a Swiss court grants a civil attachment if the applicant can provide prima facie evidence that:

- it has an unsecured and due claim against the debtor;
- there is a statutory ground for attachment; and
- the debtor has assets located in Switzerland.

The first two prerequisites usually do not raise any issues. From practical experience, however, a creditor frequently faces difficulties in providing the required prima facie evidence that the debtor indeed holds attachable assets in Switzerland. This is even more difficult with cryptocurrencies. On the one hand, a debtor is not obliged to disclose their assets to the creditor or court in attachment proceedings. Also, a court dealing with an attachment request will not undertake an investigation, but only rely on evidence provided by the applicant. An additional hurdle for an applicant is that the courts will, in principle, only admit documentary evidence in attachment proceedings. For traditional commercial transactions, a creditor is typically more likely to succeed by submitting correspondence referring to a debtor's bank account in Switzerland. For cryptocurrencies, the situation is inherently more difficult and, in practice, most applicants may therefore already fail at the level of demonstrating that the debtor holds cryptocurrencies. Firstly, commercial transactions are not (yet) ordinarily settled by cryptocurrencies. Secondly, even if the creditor finds an alphanumeric address, this will be of little help to identify the location of

cryptocurrencies, which, as assets sui generis, are not considered chattels and therefore cannot be physically located. Indeed, by virtue of the distributed ledger technology, cryptocurrencies are "located" on the blockchain and are therefore ubiquitous.

Swiss legal doctrine primarily focuses on the private key when determining where cryptocurrencies are located. In the case of cold storage, ie, storing the cryptocurrencies' private keys in an offline environment, eg, on a private storage device such as a USB stick (hardware wallet) or a piece of paper (paper wallet), cryptocurrencies are arguably located at the physical location of the private key. In that case, the private key is technically a movable object, but the cryptocurrency itself is not. If located in Switzerland, the private key may be attached according to the Swiss DEBA and taken into custody by the competent Swiss debt collection office, however, this does not amount to an attachment of the cryptocurrencies themselves.

In the case of hot storage, ie, online, the debtor is either using the services of a third-party provider (online wallet) or installing software on their computer (desktop wallet) to manage access to their cryptocurrencies. Whereas in the case of a desktop wallet, the private key is saved locally on a hard disk, which can be attached if located in Switzerland and taken into custody, in the case of an online wallet, the private key is saved on the server of a third-party provider. Taking the private key into custody may only be possible in this case if the server is located in Switzerland. Again, attaching the private key does not amount to an attachment of the cryptocurrencies themselves. Attaching the private key is therefore only half of the equation.

In general, a wallet is also password-protected. If a debtor does not provide the password voluntarily, the means available to a Swiss debt collection office to force a debtor to release the password are limited. Although a debtor refusing to provide a password may become criminally liable for fraud against seizure under Article 163 of the Swiss Criminal Code, this may only be the case after unsuccessful debt collection proceedings against the debtor, which can take years.

Without actual access to the private key by the debt collection office and preservation of the cryptocurrencies by moving them to another public address under the control of the Swiss debt collection office, the attachment of the private key may be a moot point if the debtor can still dispose of the assets (eg, by keeping a spare copy of the private key).

A debtor may not always hold a private key to its cryptocurrencies, but may have them managed by specialised third-party providers (vault providers). In such a case, a holder of cryptocurrencies merely has a claim against the provider for delivery of its virtual currency units. If such a claim is known to a creditor, and they are able to produce corresponding prima facie evidence, the virtual currency units can be attached like any other claim against a debtor, either at the debtor's Swiss domicile, or outside such domicile, at the Swiss seat of the vault provider.

Attachment in criminal proceedings

In criminal proceedings, cryptocurrencies arguably also qualify as assets sui generis. As such, they cannot be confiscated as chattels, which might be possible in the case of a private key in the form of a USB stick or a piece of paper. However, according to Swiss doctrine, cryptocurrencies may qualify as assets according to the definition in Article 70 of the Swiss Criminal Code. As such, under Article 263(1)(d) of the Swiss Criminal Procedure Code, in conjunction with Article 70 of the Swiss Criminal Code, they can be (provisionally) confiscated if they have been acquired through the commission of an offence

or are intended to be used in the commission of an offence or as payment for an offence. By way of (provisional) confiscation, the criminal authority prevents the accused from disposing of an asset.

The Swiss criminal authority will, however, face the same practical problems as the debt collection office. Firstly, it must discern the existence of the cryptocurrencies. In practice, a public prosecutor usually does so as a result of a house search, or the analysis of further (documentary) evidence, eg, (email) correspondence, records from WhatsApp, or phone conversations. However, even if the criminal authority has established the existence of the cryptocurrencies, the location of the private key will still remain unknown. As explained above, even confiscating a private key does not ensure access to the cryptocurrencies if the wallet is password-protected. The accused will (again) be of little help as they are not obliged to disclose any holdings in cryptocurrencies, the private key or its location, nor the password to the wallet.

In practice, if the cryptocurrencies presumably originate from a felony or aggravated tax crime, the interesting question comes up as to whether a recalcitrant cryptocurrency holder could then be considered as frustrating the identification of the origin or the tracing or the forfeiture of these assets, which they know or should know originate from a felony or aggravated tax crime. Such behaviour may qualify as money laundering under Article 305bis of the Swiss Criminal Code and the cryptocurrency holder may be prosecuted.

In order to fulfil Article 305bis of the Criminal Code under Swiss law, the paper trail and thus the tracking of asset history must be interrupted, which is arguably the case if an accused refuses to release a password. As a consequence, pressing charges for money laundering may provide an alternative avenue of prosecution, should an accused resist confiscation of cryptocurrencies, or refuse to provide the password to the wallet. However, this has never been tested in court.

The situation is slightly different from a criminal perspective, where an accused makes use of a specialised vault provider as outlined above under the heading, **Attachment in civil proceedings**. In such a case, the specialised vault provider may be under an obligation to disclose information at the request of the criminal authority and perhaps even to transfer cryptocurrencies to them.

LALIVE is an international law firm, renowned for its expertise in international legal matters, with offices in Geneva, Zurich and London. Core areas of practice include asset recovery, litigation, white-collar crime and compliance, commercial and investment arbitration, art and cultural property law, corporate and commercial law, real estate and construction. The firm's litigation team of ten partners and 32 counsel and associates has an established practice in complex, multi-jurisdictional, cross-border matters, including in the tracing and recovery of assets, misappropriated or otherwise. It also represents clients before the Swiss courts for the purpose of obtaining interim measures of protection, and in criminal and mutual legal assistance matters. LALIVE has a strong banking litigation practice and is unique in Switzerland in that it is conflict-free to act against banks and financial institutions. Recent work includes representing a Latin American state in a large-scale investigation and the tracing and recovery of illicit assets totalling over USD1 billion; a UHNWI in the recovery of assets in relation to artwork transactions exceeding USD1 billion in multiple jurisdictions; and a telecommunications company in a matter involving over USD500 million in claims of criminal mismanagement and fraud.

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