Lending, rehypothecation and the end of custody

Dr Alexander Ressos, TEP
Attorney-at-Law (Switzerland and Germany),
Solicitor (England & Wales and Hong Kong)
Of Counsel, KGP Legal LLC
alexander.ressos@kgplegal.com.sg
www.ressos.com.sg

Custody ends where lending begins. A custodian that may use client tokens for its own account, lend them to third parties or pledge them, holds a debt to the client and not the client's asset. This is the lesson of Celsius, Voyager and, in Singapore, Hodlnaut and Vauld, whose customers discovered in 2022 that "earn" accounts were unsecured loans to a failing company. Part J, Chapter V and Part N, Chapter IV analyse the Singapore proceedings. The technical point for this chapter is simple. If the terms permit the custodian to move the tokens for its own purposes, no key-management architecture restores the client's position. The chain will show the tokens leaving the custodian's address, and insolvency law will treat the client as a creditor.

Swiss law states this directly. Art. 242a DEBA protects only assets the custodian has undertaken to hold "at all times" for the client. A right of use destroys the protection and converts the arrangement into a deposit, which requires a banking or fintech licence under Art. 1 or 1b BankA.[1] Singapore reaches a similar result through contract and trust law. A term permitting use is inconsistent with a trust and leaves the customer with a contractual claim.

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Notes

1. Banking Act, SR 952.0, Art. 1b para. 1 (acceptance of public deposits up to CHF 100 million without interest or investment); Banking Ordinance, SR 952.02, Art. 5a (crypto-based assets as deposits where the custodian may dispose of them). Part E, Chapter II. ↩

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Author contact: Dr Alexander Ressos, TEP · contact@ressos.com