Tracing

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Following, tracing and claiming

Tracing is the process of identifying the asset into which the claimant's original asset has been converted. Following is the process of identifying the same asset as it moves from hand to hand. Claiming is the assertion of a right against the asset identified.[1] Blockchain analysis is in substance a following and tracing exercise conducted on a public ledger. Each transaction is visible, so the analyst can follow a specific unspent output in a UTXO chain such as Bitcoin or trace value through an account-based chain such as Ethereum where balances are fungible. Mixing, chain-hopping through bridges and conversion on exchanges are the points where following ends and tracing begins.

Common law and equity

Common-law tracing is defeated by mixing. Equitable tracing is not, but it has traditionally required a fiduciary relationship or an equitable proprietary interest at the start of the chain.[2] The constructive trust that arises on theft or fraud supplies that interest, so a crypto fraud victim can trace in equity. The rules for mixed funds then apply. Where the wrongdoer mixes stolen assets with his own, the claimant may elect the most favourable attribution, treating the wrongdoer as having spent his own assets first or as having preserved the claimant's in whatever remains.[3] Where the wrongdoer mixes the assets of several victims, the courts apply a pari passu or rolling-charge distribution in preference to the first-in-first-out rule where that rule would produce arbitrary results.[4]

Blockchain analytics firms apply their own attribution conventions, often first-in-first-out, last-in-first-out or a "haircut" that treats each output as tainted in proportion to the tainted inputs. A court is not bound by the analyst's convention. In litigation the analyst's report should state the convention used and the result under the alternatives, so that counsel can argue for the attribution most favourable to the client. Singapore courts have accepted such reports as evidence supporting interim relief without requiring the analyst to give oral evidence at that stage, but a contested trial would require expert evidence meeting the usual standards.[5]

Where tracing stops

Tracing stops at a bona fide purchaser for value without notice, at a mixer whose output cannot be attributed and at a cash withdrawal. In practice it also stops at an exchange that will not co-operate and that has no presence in a jurisdiction whose courts will compel it. The practitioner's task in the

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first days is to get a freezing order to the exchange before the assets are withdrawn, which is why speed matters more than the perfection of the pleading.

Checklist

In the first seventy-two hours after a client reports a crypto theft or fraud, the following steps should run in parallel. Part Q, Chapter II contains the extended version. - Secure the client's remaining assets by moving them to new keys generated on a clean device. - Preserve evidence: screenshots, transaction hashes, communications with the fraudster, device logs. - Commission a blockchain analysis identifying the destination addresses and any exchange deposit addresses. - Send notice letters with the analysis to every exchange identified, requesting a voluntary freeze and preservation of records. - File a police report in Singapore and in any other jurisdiction with a connection, because exchanges respond faster to law enforcement requests. - Prepare an ex parte application for a proprietary injunction, a worldwide freezing injunction, disclosure orders against the exchanges and substituted service, supported by an affidavit exhibiting the analysis. - Consider parallel relief in Switzerland or elsewhere if the exchange or the fraudster has assets there (Part H, Chapter V).

Notes

1. *Foskett v McKeown* [2001] 1 AC 102 at 127–128 (Lord Millett). The distinction has been adopted in Singapore, for example in *Caltong (Australia) Pty Ltd v Tong Tien See Construction Pte Ltd* [2002] SGCA 28.
2. *Re Diplock* [1948] Ch 465 (CA). The requirement of a fiduciary relationship for equitable tracing has been criticised but remains the orthodox position in Singapore.
3. *Re Hallett's Estate* (1880) 13 Ch D 696. *Re Oatway* [1903] 2 Ch 356.
4. *Barlow Clowes International Ltd v Vaughan* [1992] 4 All ER 22 (CA).
5. *CLM v CLN* [2022] SGHC 46 at [21] and [61]–[63], accepting the plaintiff's tracing evidence as the basis for joinder of further defendants.

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