

## Obligation to Pay Cryptocurrency May Count As Debts in Determining Insolvency, Singapore High Court Rules

In *Loh Cheng Lee Aaron and another v Hodlnaut Pte Ltd (Zhu Juntao and others, non-parties)* [2023] SGHC 323, the General Division of the High Court of Singapore (**High Court**) clarified that a company's obligation to pay cryptocurrency to its creditors may, for the purposes of determining whether the company is insolvent, count as "*debts*" within the meaning of section 125(1)(e) read with section 125(2)(c) (**Section 125(2)(c)**) of the Insolvency, Restructuring and Dissolution Act 2018.

This update takes a look at the High Court's decision.

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### Background

The dispute arose from an application to wind up the defendant, Hodlnaut Pte Ltd (**Company**). The Company had operated a platform where users (**Users**) could deposit cryptocurrencies and earn interest on them. Accordingly, a substantial portion of its assets comprised cryptocurrencies and it correspondingly owed the Users substantial obligations to repay cryptocurrencies.

It was in this context that the High Court had to determine the novel issue of whether cryptocurrencies owed by the Company to its creditors were to be treated as debts in assessing whether the Company was unable to pay its debts such that it should be wound up. The High Court answered the question in the affirmative.

The claimants, who were the interim judicial managers of the Company (**Claimants**), argued that the Company was cash flow insolvent when its current assets (including its cryptocurrency holdings) were measured against its current liabilities (including its liabilities to repay cryptocurrencies). The Claimants also argued that the Company should be wound up as the restructuring proposal that had been belatedly put forth by the directors of the Company (**Directors**) was doomed to fail as it did not have the support of the Company's major creditors.

The Directors contended that the cryptocurrencies owed by the Company to its creditors were not "*debts*" within the meaning of Section 125(2)(c) because, among other things, "*debts*" refers only to liabilities denominated in fiat or actual money. They submitted that the Company was not insolvent as it could pay its debts denominated in fiat. Further, the Directors argued that the liability to repay the Users their cryptocurrencies had not yet arisen because the Company had imposed a halt on withdrawals by the Users, which was permitted under the user terms entered into between the Company and the Users.

The Directors also contended that the court should exercise its discretion not to wind up the Company to allow their proposed restructuring to be attempted. Finally, they argued that, if the Company was wound up, the Claimants should not be appointed as the Company's liquidators.

## The High Court's Decision

The High Court ruled in favour of the Claimants on all the issues.

First, the High Court agreed with the Claimants that obligations to repay cryptocurrencies counted as debts owed by the Company and were relevant in determining whether the Company was insolvent. The High Court observed that the test of cash flow insolvency as set out in the Court of Appeal's decision in *Sun Electric Power Pte Ltd v RCMA Asia Pte Ltd (formerly known as Tong Teik Pte Ltd)* [2021] 2 SLR 478 is a broad one. Not only does the court consider whether a company's current assets exceed its current liabilities such that all debts can be met as and when they fall due within a 12-month timeframe, to avoid absurd outcomes, it must also have regard to the holistic position of the company and consider not just liquidated claims but also those that might be made on the non-monetary assets of the company, though which may ultimately be payable in money.

The High Court noted that while *Algorand Foundation Ltd v Three Arrows Capital Pte Ltd* (HC/CWU 246/2022) (30 March 2023) (General Division of the High Court, Singapore) (**Algorand v 3AC**) had held that a debt denominated in cryptocurrencies was not a money debt capable of forming the subject matter of a statutory demand under Section 125(2)(a), that case did not stand for the proposition that pursuing and obtaining a judgment to obtain liquidated damages is necessary before an assessment is made of cash flow insolvency. Section 125(2)(a) involves "indebtedness" measured by reference to a specific amount of money on a specific claim, which stands in contrast to the more holistic approach under Section 125(2)(c).

The High Court highlighted that the fact that a debt might be defined in money or money's worth does not mean that the debt arises only when actual quantification of assets in monetary terms is determined through court proceedings. Holdings of various kinds of assets – such as wine, commodities or even cryptocurrency – can be assessed by the court in a winding up application. Whether the court accepts the applicant's valuation of the assets in question turns on the evidence presented to the court.

Second, the High Court agreed with the Claimants that the halt on withdrawal neither extinguishes liability nor necessarily postpones the accruing of liability for the purposes of cash flow insolvency. All it does is prevent the withdrawal of the asset. The High Court noted that it may well be that appropriately drafted clauses could effectively bar anyone holding an account subject to a withdrawal halt from pursuing a winding up of a company on the basis of an unsatisfied demand under Section 125(2)(a), or even preclude him from establishing cash flow insolvency under Section 125(2)(c), but found that the withdrawal halt provisions in the user terms in this case did not have any such effect.

Third, the High Court accepted the Claimants' arguments that the likelihood of success of the Directors' proposed restructuring was very low as the major creditors did not support it. The High Court therefore declined to exercise its discretion against winding up.

Fourth, the High Court disagreed with the Directors' objections to the appointment of the Claimants as liquidators of the Company, holding that it did not find any reason to doubt the ability or suitability of the Claimants to function as liquidators. The High Court noted that, if anything, the Claimants' familiarity with the Company and its business would aid in liquidation being more efficient, and therefore appointed the Claimants as liquidators of the Company.

## Concluding Observations

This decision is significant as it clarifies that, in assessing whether a company is insolvent, liabilities to repay cryptocurrencies are to be taken into account.

This is particularly important given that the effect of the High Court's earlier decision in *Algorand v 3AC* is that a creditor who is owed cryptocurrencies would have to first obtain a court judgment for a liquidated sum of money denominated in fiat currency, before seeking to commence insolvency proceedings against the debtor under Section 125(2)(a).

This decision now clarifies that such creditors can, under Section 125(2)(c), commence insolvency proceedings without first obtaining a court judgment for a liquidated sum of money denominated in fiat currency, by proving that the company is unable to pay all its debts (including its liabilities denominated in cryptocurrencies) as they fall due.

Further, this decision clarifies that the question whether the court should exercise its discretion against winding up to allow restructuring to be pursued would depend on requirements based on similar considerations to those for an initial moratorium extension but, in addition, given that the discretion is sought to be invoked in the face of a winding up application, the level of persuasiveness has to be ratcheted up significantly. This signifies that the court will not generally adjourn a winding up application to entertain last-ditch restructuring proposals unless a feasible restructuring proposal is put forward, and an important consideration would be whether there is support from major creditors.

If you would like information and/or assistance on the above or any other area of law, you may wish to contact the Partner at WongPartnership whom you normally work with or any of the following Partners:



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