

Tracing Crypto Assets

There is no doubt about it: crypto assets are gaining acceptance in the mainstream in the United States. Congress has passed the GENIUS Act, calling for a comprehensive regulatory framework for stablecoins. And the Securities and Exchange Commission has proposed rulemaking to regulate the market of cryptocurrencies and other crypto assets.

As more and more transactions involve crypto assets, creditors should familiarize themselves with the nuances of recovering crypto assets from defaulting debtors. Like the recovery of traditional assets, such as cash, real estate, and securities, asset tracing is an important tool for recovering crypto assets.

Asset Tracing Scenarios

“Asset Tracing” generally refers to the process of identifying an asset and locating and identifying each transfer of that asset to identify its current location. Creditors ordinarily perform tracing to assist in the collection of a liability or enforce a judgment. The typical scenario involves a creditor who seeks to recover a legal obligation from a debtor. The creditor obtains historical information about the debtor’s assets, which may include, for example, bank account statements, stock transfer records, or real property transfer records. The creditor uses these records to identify each transfer to locate the current location of the asset so that it can be attached and seized by the creditor.

Crypto assets may be traced, but also present new and unique scenarios. Despite some misconceptions, crypto transactions are *not* confidential. Due to the public key cryptographic principles underlying blockchain technology,[\[1\]](#) every transaction on a blockchain is public (with certain exceptions). Each transfer of an asset on the blockchain is hard-coded with the addresses of the wallet from which the asset was transferred and the wallet(s) to which the asset is sent.

Although tracing crypto assets using wallet addresses is possible, it may not be simple and may not necessarily result in easy recoveries. Recalcitrant debtors can use various techniques to hide their crypto assets from creditors. For example, a crypto debtor may use a “mixing service” or “tumbler” to obscure the destination of a crypto transfer. A tumbler divides a single crypto transfer into a larger number of

smaller transfers and routes these smaller transfers to various wallets, often in combination with unrelated transactions. The large number and “mixing” of transfers increases the difficulty in determining the final destinations of specific crypto assets.

Tornado Cash is a well-known mixing service that has been used by nefarious actors to hide the ultimate destination of crypto assets. Tornado Cash was blacklisted by the United States Department of the Treasury in August 2022, and Roman Storm, one of its founders, was recently found guilty by a United States jury of knowingly operating a money transmitting business. Nonetheless, Tornado Cash and several other mixing services remain available on the internet.

Crypto debtors may also hide their assets by converting their crypto assets from one type of asset to another, which may be a different type of crypto (i.e., from Bitcoin to Ethereum) or another type of asset altogether. Sometimes a crypto asset might be converted into a traditional asset, such as cash or securities.

Sophisticated debtors may conduct multiple conversions involving many types of assets. For example, a debtor may exchange Ethereum for gold and later convert the gold into Bitcoin. The conversion process introduces another hurdle to the location and recovery of the asset.

Recovery of Crypto Assets

The use of offshore jurisdictions by recalcitrant crypto debtors mirrors traditional techniques used by debtors to hide assets. For example, a crypto debtor may transfer an asset from a domestic wallet to a wallet controlled by an offshore entity or person. Even if the creditor knows the address of the offshore wallet, they may still need to initiate legal proceedings in the relevant offshore jurisdiction to take action against the wallet.

Another technique used by crypto debtors is to use a straw man to present a transfer as a legitimate transaction. The straw man may present as a legitimate vendor or service provider who requests payment in crypto for goods delivered or services rendered. In reality, the straw man provided no goods or services and has conspired with the debtor to transfer the crypto asset. In this circumstance, the creditor may need to demonstrate the legal fiction of the transaction before obtaining a court order against the wallet that received the crypto.

These techniques may delay the recovery of crypto assets, but they do not prevent it. Creditors have several tools available to assist in the recovery of crypto assets.

Blockchain analysis, where a creditor uses the publicly distributed ledger to trace transactions involving specific crypto assets, is a powerful tool that creditors can use to map out transfers of crypto assets. Once an action has been commenced, a creditor may use subpoenas to depose witnesses and obtain other records to fill in the gaps. Finally, a creditor can use traditional enforcement tools, such as orders of attachment and levies, to recover the crypto assets.

Although crypto technology introduces new issues to address in recovery, the technology also provides new opportunities to obtain successful recoveries. Creditors should not shy away from enforcement merely because crypto assets are involved.

[\[1\]](#) Blockchains are publicly distributed ledgers encrypted with cryptographic hashes. Each address (or “wallet”) on the blockchain is encrypted using a public key. Transactions relating to the address require a private key. Because the blockchain itself is publicly distributed and the public key identifies a specific wallet, all transactions involving a wallet are public.