

Patterson Belknap Partners Discuss FTX Task Force

By Emma Cueto

Law360 (December 9, 2022, 3:33 PM EST) -- In the wake of the meltdown of cryptocurrency exchange FTX and its associated entities in November, Patterson Belknap Webb & Tyler LLP formed a task force to represent those affected, with the firm saying it is seeing interest from potential clients around the world with FTX in bankruptcy.

The Bahamas-based FTX, once the third-largest cryptocurrency exchange by volume, was led by Sam Bankman-Fried and closely linked to other businesses owned by Bankman-Fried, especially trading firm Alameda Research, which was allegedly propped up with FTX customer money. The exchange collapsed in early November and filed for bankruptcy on Nov. 11, saying its creditors could number as high as 1 million.

The FTX task force at Patterson Belknap seeks to represent those affected by the collapse and brings together attorneys from many of the firm's practice groups.

Partners Daniel Lowenthal, Daniel Ruzumna and Jason Vitullo, who are members of the firm's business reorganization and creditors rights practice, white collar defense practice, and litigation department, respectively, spoke to Law360 Pulse about the firm's decision to launch a task force, the potential long-term impacts of the collapse, and the challenges in trying to advise clients in the midst of uncertainty.

This interview has been edited for clarity and length.

In the wake of the FTX collapse, what prompted you to decide that it made sense to create a formal task force?

Ruzumna: A number of us at the firm had been focusing on the crypto space for some time and closely monitoring the developments in the crypto space. Earlier this year, there was the collapse of two coins, Terra Luna and **Celsius**, and we realized that was likely to be followed by further shakeups. When we then read about the FTX collapse, we recognized that more was likely to shake out.

I am a white collar lawyer and received calls from clients and potential clients about what this meant. The same is true of our other practices. Essentially we recognized after the FTX collapse and the calls we were getting that a more coordinated approach probably made sense, so that we could share expertise, use the information and experience we were getting to help out clients on all fronts. So we decided to create a task force so that we could hopefully address all clients' needs.

Dan and Jason, was that also your experience, that you were getting a lot of calls after the collapse?

Lowenthal: I chair our creditors rights and bankruptcy practice and do a lot of cross-border work. And when FTX filed in both Delaware and the Southern District of New York, I got calls from around the world — I was recently talking to a company in Singapore.

There are a lot of questions. Typical creditor questions about when people will be able to collect, but also: What will be bankruptcy estate property? What will be customer property? What's going to be the fallout from this, the ripple effect? Will there be clawback actions? Will customers be subject to that? What about the money that Sam Bankman-Fried donated to charity? Will that be subject to clawbacks?

And in addition to that, there's this big cross-border component, because more than 100 entities filed in Delaware, and then the Bahamian regulators had their liquidators file in New York. And now everything's in Delaware, but it was apparent to me that this case could have a lot of tendrils. And so pulling together a group of us to start working through all of this just made complete sense.

Vitullo: Building off of what Dan said, I think we recognized right away this was a significant event, and we had some experience in a somewhat similar context in the financial crisis. Our firm was an early pioneer in recognizing the structured finance and residential mortgage-backed securities issues, and we formed a group in 2007, right at the start of seeing those issues in the RMBS and structured finance arena.

And similarly now, we have an interdisciplinary group. These issues are not going to be confined to one particular practice group, and we want to draw on the expertise and experience and learning across all these different areas and come together, share insight, and be able to be right at the forefront, just like we were in 2007-2008. We've been litigating those claims for the past decade and have recovered billions for our clients.

When you have an event like this that affects potentially millions of investors and entities, what are the challenges associated with trying to get a handle on the situation in order to advise your clients?

Ruzumna: I think one issue we see, particularly in the crypto space, is that everything is just so new. There are a lot of open issues with crypto: Is it a security? Is it not a security? There are jurisdictional issues in this case, because it is a Bahamian entity.

There are also issues from a practical standpoint, including conflicts of interest. One of the reasons we thought we were well positioned to create a task force is that Patterson is a single-office firm. We tend to be pretty aware of our clientele, we don't have the same types of institutional clients some of the larger firms have, and we're very nimble in terms of clients. But that's a very real concern.

Lowenthal: I'll add from my practice area that the word uncertainty is very on point. In talking to potential clients, what I say to them is, "We always want to add value." You don't want to take on someone and just bill for time. But with this situation, someone could be owed millions of dollars and we don't know how it will unfold. It could turn out that you have a million creditors and that this money isn't theirs, and they're going to lose their life savings.

There is so much uncertainty, and we need to work through it.

Vitullo: And I think that's also part of the motivation of the task force. This is a new area, and it's evolving and changing. There's going to be new precedent that's set. There seems to be clamoring for new regulation, and we're trying to advise our clients on how that might impact them. So bringing together people from different areas who can monitor and report back to the group is important.

What is your sense of this even in terms of the scale of it or the long-term fallout? You were comparing it to 2008; is that the sort of event people should have in their minds when trying to conceptualize it?

Vitullo: I don't think this is at the scale of 2008; certainly it doesn't seem to have the same effect as the RMBS issues on the larger economy. But we're certainly seeing ripple effects in the crypto space. We're already seeing that. I think there's going to continue to be a domino effect that continues in the crypto space, though whether it goes beyond that remains to be seen.

But I think we also believe that something will emerge from this. In the dot-com bubble of the early 2000s, out of that turmoil emerged some more stable, long-term companies. So while we're monitoring this initial turmoil and collapse of FTX and advising clients, it's also about looking to the future.

Ruzumna: One thing that I think is very, very clear at this point is that one result of this situation with FTX is going to be a clamoring for more legislation and regulation. Both houses of Congress are set to hold hearings on what happened with FTX next week. We can expect that there will be further congressional investigation into this, further regulation proposed. We're going to see further developments in this area.

And the players in the crypto space will likely need advice on how to follow that regulation and what it means for them.

Since the FTX collapse and since launching the task force, have you been getting a lot of interest from people who are affected or potentially affected?

Ruzumna: We do have clients in this area now, and we're keeping busy — on certain fronts more than others. It's mostly advisory at this point as we wait to see which shoe is going to drop. We've had meetings with clients, and I know our corporate partners have as well.

Lowenthal: I've been getting various inquiries from folks who have exposure: When can we file a claim? When can I get paid? What can I do? And some of them have millions at stake. I've been telling them that there's no date yet for people to file any claims, so let's see how it goes.

We've thought about trying to get a group together to spread the cost, because there's a lot of the same issues. We're just figuring out what might make sense.

And for people who are affected by this and don't know where to start in terms of figuring out what they should be doing right now, what is your advice?

Lowenthal: Well, they should be talking to Dan and to Jason and to me!

But all kidding aside, there are a lot of people here with a lot of exposure, and it all needs to be analyzed. The big question here is going to be what property here is property of the estate and what is

customer property. That needs to be sorted out because that is going to drive so much of the analysis of what customers can get back, what can get clawed back.

So if I were an investor, all kidding aside, I would definitely talk to a professional.

--Editing by Robert Rudinger.