Preventing a ‘Rug Pull’: Ontario Superior Court on Risk of Crypto-Asset Flight and Freezing NFTs

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In a recent decision of the Ontario Superior Court of Justice, **McRae-Yu v. Profitly Incorporated et al.**, Hooper J. granted and then upheld a Mareva injunction in the context of an allegedly fraudulent non-fungible token (“NFT”) collection called “Boneheads.” The judgment offers an important illustration of how courts may approach NFTs, “minting,” and the potential dissipation of crypto-assets in fraud-based litigation. (*McRae-Yu v Profitly Inc. et al.*, 2024 ONSC 1593)

Early in the Reasons for Decision, the Court describes NFTs as “cryptocurrency-based assets” that “can be developed within a collection wherein the developers create numerous NFTs to be offered to the public at the same time” (para. 5). This “offering of a collection for public sale” is referred to by Hooper J. as the “minting” of the NFTs (para. 5). The Court also explains that an NFT sale is governed by a “smart contract— a self-executing contract formed when certain conditions are fulfilled,” whose terms “are transparent” (para. 6). Each NFT “is given a unique identification number which allows it to be distinguishable from all other NFTs” (para. 6), meaning its ownership and transactional history can be tracked on a blockchain.

The Court situates the case within the broader backdrop of NFTs, acknowledging that “NFTs can be anything digitally tokenized on a blockchain” and that “one popular form of NFT is a piece of digital art” (para. 7). Citing the “excitement and anticipation surrounding an NFT collection,” Hooper J. points out that, although the NFT market has become volatile, certain collections can draw in consumers with “a roadmap of benefits and privileges” to spur confidence in the value of the tokens (para. 7-9). According to the Court, when the Boneheads project minted in 2021, NFTs were “seen to be a potentially valuable investment” (para. 8).

Minting and the Alleged Fraud

The Plaintiff in this action claimed that the Boneheads development team had promised substantial post-mint benefits for NFT owners, as well as promotional giveaways—namely “one lucky randomized token holder would get a monetary mystery box valued at a quarter million dollars, ‘revealed instantly at the end of the mint’” (para. 12). Almost immediately after the sale, investors began to suspect “a rug pull,” which Hooper J. defines as “a scam in which an NFT developer props up the product with fake promises, mints the collection, and then takes the proceeds of the mint and disappears” (para. 15). Although the team remained sporadically present, the Plaintiff characterized the situation as a “slow rug pull,” which the Court describes as “a modified scam where the NFT developer continues to make false promises to pacify disappointed consumers with false hope, never intending to fulfill those promises” (para. 15).

Crucially, the Boneheads project had garnered approximately “950.5 ETH,” which was worth around “$4,005,047.38 CAD” at the time of mint (para. 13). These digital assets were then distributed into three crypto wallets. In reviewing the trajectory of these wallet transfers, the Plaintiff and other investors accused the Defendants of fraud and, fearing dissipation of the NFTs’ proceeds, successfully moved for a Mareva injunction that froze the Defendants’ bank accounts and crypto wallets.

Crypto-Assets and the Risk of Dissipation

The Court's analysis of whether to continue the Mareva injunction centered on the fact that NFTs and cryptocurrencies can be "instantly and anonymously" moved (para. 37). Hooper J. stresses that a Mareva injunction is an "extraordinary remedy" (para. 22) because it effectively amounts to "pre-judgment execution against the defendant's assets" (para. 22). Yet in cases of alleged fraud, the Court indicated that "the courts have found it can be appropriate for the initial motion to be brought without notice," precisely because "if any further assets are dissipated, that dissipation can be remedied through the contempt powers of the court" (para. 23).

Acknowledging that cryptocurrency's very nature facilitates swift asset flight, the Court cites and applies the principle that "it is not necessary to show that the defendant has bought an air ticket to Switzerland, has sold his house and has cleared out his bank accounts" (para. 39, quoting from another authority). Rather, "it should be sufficient to show that all the circumstances, including the circumstances of the fraud itself, demonstrate a serious risk that the defendant will attempt to dissipate assets or put them beyond the reach of the plaintiff" (para. 39). Hooper J. then observes that the Defendants offered "extremely vague" evidence as to how the minted funds had been used, thus adding to the Court's inference of a "real risk of dissipation of assets" (para. 41).

In language emphasizing the particular ease of moving crypto-assets, Hooper J. comments: "I find that the plaintiff is not required to adduce direct evidence showing the defendants are actively dissipating their assets. A serious risk of dissipation is sufficient and may be inferred from the surrounding circumstances. As I have already found there exists a strong prima facie case of fraudulent misrepresentation, I find that the defendants are very likely to attempt to dissipate the remaining assets or remove them from this jurisdiction" (para. 41).

Court's Willingness To Enjoin Access to Crypto Wallets

From a procedural standpoint, the Court initially granted a broad freeze of both conventional and crypto accounts, later modifying it by consent to allow the Defendants some living expenses. However, the Defendants were still "denied access to their cryptocurrency wallets and cryptocurrency assets under this modified order" (para. 3). In deciding to continue that freeze until trial or further order, the Court found that the stringent requirements for a Mareva injunction had been met, including "a strong prima facie case" of fraud, a serious risk of dissipation, and a balance of convenience favoring the Plaintiff class (para. 30-47).

Hooper J. highlights that crypto-assets' ease of secretive transfer (and the alleged fraud) weighed heavily in favor of maintaining the injunction. As stated: "Given the fraudulent nature of the launch and the Boneheads' continued misrepresentations of the benefits attached to this NFT collection, the real risk of dissipation of assets can be proven by inference" (para. 39). Although the Defendants argued legitimate uses of funds, the Court found these explanations insufficiently detailed: "There is insufficient evidence from the defendants to explain how the $3.5 million was used or what ongoing expenses require access to the frozen funds" (para. 45).

Conclusion and Significance

The judgment underscores the Court's acknowledgment of NFTs and cryptocurrency as novel yet susceptible vehicles for fraud, where "the nature of cryptocurrency makes it easy to instantly and anonymously dissipate" (para. 37). Hooper J. expressly recognized that, while that ease alone does not automatically justify a Mareva injunction, evidence or inference of misrepresentation and potential fraud can shift the balance decisively in favor of freezing the assets. This approach demonstrates the Court’s readiness to adapt conventional equitable remedies to the digital realm.

By continuing the injunction against most of the Defendants’ crypto wallets, while allowing further hearings to assess legitimate needs such as “payment of legal fees,” the judgment confirms the Court’s willingness to intervene in order to “ensure that actual and potential wrongdoers do not ignore their obligations” (para. 29, quoting the Supreme Court of Canada). As Hooper J. put it, “if there is a finding of fraud, there is virtually no chance that the defendants, as perpetrators of this fraud will be held accountable without this injunction” (para. 43). This case, therefore, serves as a meaningful precedent for plaintiffs seeking to preserve crypto-assets in disputes where fraud or other misconduct is alleged.

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