

Jersey blockchain and cryptocurrency regulation 2022

Briefing Summary: Christopher Griffin and Holly Brown have authored the Jersey chapter of Global Legal Insight's fourth edition guide to blockchain and cryptocurrency regulation. The chapter covers the Jersey legal requirements relating to cryptocurrency and blockchain, including government attitude and definition, taxation, money transmission laws and AML requirements, mining and licensing requirements.

Service Area: Banking and Finance, Banking Regulation, Corporate, Corporate Regulation and Compliance, Dispute Resolution and Litigation, Corporate Disputes, Investment Funds, Fund Regulation and Compliance, Funds Strategies and Asset Classes, Listing Services, Regulatory, Banking Regulation, Corporate Regulation and Compliance, Fund Regulation and Compliance, Trusts and Private Wealth, Estate Planning

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Government attitude and definition

Jersey continues to welcome fintech including cryptocurrencies, blockchain and distributed ledger technology ("DLT") more widely as a pioneer in fintech regulation. Jersey enjoys a sophisticated legal, regulatory and technological infrastructure, supporting development and innovation in fintech including:

- payment services and online payment solutions;
- electronic identification ("**E-ID**");
- virtual currency exchanges ("**VCEs**") (cryptocurrency exchanges);
- security token and non-security token issuances and initial coin offering security token offerings ("**ICOs**" / "**STOs**");¹
- custody services and arrangements for holding digital assets; and
- fintech funds and other vehicles.²

Jersey is fast becoming an established market for fintechs and professional investment firms being home to a number of token issuers, global payment platforms and fintech-focused investment funds. In the past few months alone, Jersey has seen multimillion pound investments and capital raises structured using Jersey vehicles and advisers. Jersey clients include tech giants, cryptocurrency exchanges, payment platforms and emerging blockchain developer talent.

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Jersey recognised cryptocurrencies as a separate asset class long before the “ICO Craze” of 2017, when the island’s regulator, the Jersey Financial Services Commission (the “**JFSC**”), licensed the world’s first Bitcoin-focused, regulated fund (GABI Plc). From that point onwards, the island has seen a surge in exchange vehicles, token issuers and fintech funds choosing Jersey, including the world’s largest investment fund (the SoftBank “Vision Fund”, which raised USD 97 billion over two years). Both GABI and SoftBank were advised by Carey Olsen.

The JFSC is a member of the Global Financial Innovation Network and participates in the cross-border testing pilot.

Jersey has an exceptional pool of blockchain expertise, developed from the JFSC’s forward thinking attitude combined with Jersey’s flexible range of corporate vehicles and favourable tax regime.

Examples of structures that have recently used Jersey (advised in each case by Carey Olsen) include:

- CoinShares (Europe’s largest digital asset investment firm with USD 3 billion in assets under management (“AUM”)) recently used Jersey for the establishment of its new institutional-grade cryptocurrency-backed exchange-traded product (“**ETP**”). CoinShares Physical Bitcoin (Ticker: BITC) launched on 19 January 2021 with USD 200 million in AUM, and is the first CoinShares product to be listed on the SIX Swiss Exchange. The ETP programme’s physically backed structure provides institutions that are experienced in trading similar commodity-based investment securities with a familiar structure for cryptocurrency investments.
- CoinShares previously used Jersey for the launch of its ETH denominated investment fund (2017), which provided investors with exposure to the liquid digital asset ecosystem, and the 2014 launch of the first ever regulator-approved Bitcoin investment fund.
- Radix, a decentralised finance platform, used Jersey for the launch of its utility token. The platform allows users to transact with each other over a fast, secure blockchain-based platform without the need for intermediaries. Tokenholders are able to use the tokens to pay transaction fees and/or to participate in the platform’s “proof of stake” consensus mechanism to validate transactions.
- Global payment solutions provider Checkout.com, which undertook a USD 450 million Series C fundraising round. The transaction gave the company a post-money valuation of USD 15 billion, making Checkout.com the fourth-largest fintech globally and the EMEA’s most valuable venture-backed business.
- Token issuer PIP Limited used Jersey for the launch of its Vow token ecosystem, a solution for distributing debt-free liquidity into local communities through a customer loyalty mechanic.

Jersey distinguishes between traditional fiat currency and cryptocurrencies and does not treat cryptocurrencies on an equal footing to fiat currencies. For example, regulations around holding client monies focus only on fiat. Within cryptocurrencies, Jersey distinguishes between utility tokens and security tokens, as set out in the ICO guidance published by the JFSC.

There are no cryptocurrencies backed by the Government of Jersey and Jersey does not have a central bank. Jersey uses British pound sterling, although the States of Jersey Treasury issues its own bank notes separate to those in the UK.

In terms of trends, we are seeing an increased use of, and enquiries relating to, funds rolling out crypto-backed products, primarily but not limited to Bitcoin- and Ethereum-backed products, online payment solutions and E-ID and a continued interest in the establishment of cryptocurrency and security token exchanges. More recently, as a result of COVID-19, we are seeing a sharp increase in the uptake of technology and new entrants to the market. Whilst not fintech as such, this includes a widespread use and adoption of electronic signatures (including witnessing) and a general shift towards digitisation and automation of manual procedures consistent with a widespread move to remote working. We are therefore expecting this trend to continue in the coming months and welcome the opportunities that this may present in terms of increased usage of blockchain and smart contracts and automation and AI in Jersey.

In terms of innovation generally, Jersey is striving to promote fintech development by supporting local fintech talent and innovation. Digital Jersey, a Government-backed economic development agency and industry association dedicated to the growth of the digital sector, aims to do this. Further, the JFSC is a member of the Global Financial Innovation Network and participates in the cross-border testing pilot. COVID-19 has also brought about pragmatic developments in Jersey's legal practice and has given rise to recent guidance from The Law Society of Jersey in relation to the signing of certain powers of attorney by electronic signature, which demonstrates Jersey's willingness to adopt technological developments.

Blockchain and cryptocurrency/digital asset regulation

To date, Jersey has not sought to introduce any fintech specific legislation. The JFSC has sought to cater for fintech businesses within the existing regulatory framework until such time as there is a global consensus on how to regulate aspects of the fintech ecosystem; for example, if the fintech service involves the provision of a financial service, it will fall to be regulated within Jersey's financial services regime under the Financial Services (Jersey) Law 1998 (the "FSJL") unless an applicable exemption is available. The FSJL defines "financial services business" as investment business, trust company business, general insurance mediation, money services business, fund services business or alternative investment fund services business.

The main types of fintech activities that are currently active in Jersey and require some level of regulatory oversight are:

- Payment services – depending on the payment services being offered these may be required to be regulated under the FSJL to undertake "money services business", trust company business (as outlined above to the extent the services include an e-wallet relating to digital assets) or under the Banking Business (Jersey) Law 1991 for "deposit-taking" business. There are a number of exemptions that may apply and early advice should be sought.

- VCEs – these exchanges must maintain a registration under the Proceeds of Crime (Jersey) Law 1999 (the “**POCJL**”) as a “supervised business”. The POCJL requires VCEs to comply with Jersey’s laws, regulations, policies and procedures aimed at preventing and detecting money laundering and terrorist financing
- Security token exchanges – these exchanges are currently required to be regulated under the FSJL to undertake “investment business” (an “**IB Licence**”). A standard application for an IB Licence will take approximately eight weeks. An application for a digital assets-related matter may take a little longer. A full regulatory application to the JFSC will be required and will include the following documents:
 - a regulatory application form;
 - a business plan; and
 - a business risk assessment.

In terms of regulatory capital requirements, the main requirement to be aware of is that an exchange platform will be required to maintain at all times:

- a net liquid assets position of 130% of its projected quarterly expenditure;
- a minimum of GBP 25,000 paid-up share capital; and
- a minimum net assets position of GBP 25,000.

In addition, a Jersey security token exchange must be audited and the composition of the board must comply with the Jersey regulatory and economic substance requirements, being:

- there must be a minimum of two Jersey resident directors;
- the board must meet with adequate frequency having regard to the amount of decision making being undertaken;
- at meetings there must be a quorum of directors physically present in Jersey; and
- the directors of the company must have the necessary knowledge and expertise to discharge their duties (this is assessed on a whole-board basis).

Once an IB Licence has been obtained, the holder will need to observe the provisions of the JFSC’s Code of Practice for Investment Business:

- There are locally regulated administrators in Jersey who can assist by providing “incubation” services to entities and groups that are new to Jersey.
- There is no requirement to have electronic clearing and settlement or for clearing of security tokens to be carried out by a clearing house or central depository.
- The increase in uptake of exchange-related investment business in Jersey has resulted in the JFSC consulting on proposed amendments to the class of investment business to include a specific new category of exchange business. We await the outcome of the Consultation.
- Custody services and arrangements for holding digital assets – there are two models: (i) custody services provided by the exchange itself (or a related entity) to investors and exchange users; and (ii) custody services outsourced to a third-party custody provider to be provided to investors and exchange users.

- In both models, where digital assets will be stored offline or where the investor or exchange user is not provided with the keys to access the digital asset, the investor/exchange user will no longer have control over the digital assets they have invested in. In this way, it is likely that the relevant custodian entity will be providing trustee services and will need to be regulated for “trust company business” under the FSJL. However, where the storage of digital assets is incidental or ancillary to the main purpose of the entity and where there was no separate remuneration, an exemption may apply. Early advice should be sought on this point, and this is something Carey Olsen has experience of advising on.
- Business relating to digital assets and cryptocurrency – the JFSC will treat involvement by Jersey structures with digital assets and cryptocurrencies as a “sensitive activity” under the JFSC’s Sound Business Practice Policy. The practical consequence of this is that certain anti-money laundering/countering the financing of terrorism (“**AML/CFT**”) obligations are imposed on the Jersey structure. For instance, a token-issuing company is required to carry out checks on: (i) the purchasers of the tokens who purchase coins directly from the issuer; and (ii) the holders of tokens issued by the issuer in the event they are sold back to the issuer. In such circumstances, the issuer will be required to obtain information to: (a) establish and obtain evidence to verify identity; and (b) establish and, depending on the level of risk, obtain evidence to verify the source of funds and source of wealth.

Sales regulation

In Jersey, the sale of Bitcoin or other crypto or digital tokens per se is not regulated by a specific securities law or commodities law. As noted above, transactions relating to digital assets and cryptocurrencies are treated as a “sensitive activity” under the JFSC’s Sound Business Practice Policy. In addition, there are requirements under Jersey’s existing regulatory framework for sale transactions that arise in the following circumstances:

- token issuers (whether utility tokens or security tokens) who issue or offer tokens for sale;
- companies operating VCEs – these exchange fiat monies to cryptocurrencies and vice versa; and
- companies operating security token exchanges – these exchange fiat monies to security tokens and vice versa.

The sale of cryptocurrencies in the secondary market (such as on an exchange) in return for payment in cryptocurrencies (i.e. crypto-to-crypto transactions) does not fall within the VCE or security token exchange regime although would still be considered a “sensitive activity” as outlined above.

Taxation

Jersey provides a stable, tax-neutral environment. Many Jersey companies (apart from locally regulated financial services companies and utilities) can be zero-rated for income tax and are not subject to capital gains tax within the jurisdiction. Jersey has no capital transfer or similar taxes and does not levy any withholding tax on dividends. There is also no stamp duty on Jersey share transfers. Companies can also be incorporated in Jersey but can be resident for tax purposes in another jurisdiction if certain criteria are met.

There are currently no specific laws regulating the taxation of cryptocurrencies or digital assets, although Jersey's Comptroller of Taxes has issued guidance on cryptocurrency tax treatment regarding both Jersey income tax and Jersey goods and services tax. The guidance provides that such assets will be taxed in accordance with general Jersey taxation principles and provisions.

Money transmission laws and anti-money laundering requirements

In terms of money transmission, as noted above, depending on the services in question, payment services business and money transmission services may be required to be regulated under the FSJL in order to undertake "money services business", trust company business (as outlined above to the extent the services include an e-wallet relating to digital assets) or under the Banking Business (Jersey) Law 1991 for "deposit-taking" business. There are a number of exemptions that may apply and early advice should be sought.

In terms of AML, as noted above, the JFSC will treat transactions with digital assets and cryptocurrencies as a "sensitive activity" under the JFSC's Sound Business Practice Policy. The practical consequence of this is that certain AML/CFT obligations are imposed on the issuer from Jersey's AML regime. This includes the issuer being obliged to carry out checks on: (i) the purchasers of the tokens who purchase coins directly from the issuer; and (ii) the holders of tokens issued by the issuer in the event they are sold back to the issuer. In such circumstances, the issuer will be required to obtain information to: (a) establish and obtain evidence to verify identity; and (b) establish and, depending on the level of risk, obtain evidence to verify the source of funds and source of wealth.

In addition, Jersey also has an industry working group focused on managing Virtual Assets Risk in relation to Virtual Assets and Virtual Assets Service Providers ("**VASPs**"). This working group involves Carey Olsen representatives, the Government of Jersey representatives, JFSC representatives and other interest groups on the Island. The working group is reviewing the Island's AML requirements in relation to Virtual Assets and VASPs.

Promotion and testing

Jersey promotes and tests fintech firms products and services in a number of ways. In terms of testing products and services, the JFSC has proven itself to be a proactive and forward-thinking regulator in becoming a member of the Global Financial Innovation Network (a group of international regulators and observers committed to supporting innovative products and services) and participating in the cross-border testing pilot that launched in January 2019, offering firms the opportunity to test their products and services in multiple jurisdictions.³

Jersey also operates a sandbox run through Digital Jersey, supporting local fintech firms and fintech firms seeking to relocate to Jersey.⁴

In terms of promoting fintech and thought-leading in Jersey, the Digital Assets Working Group (the “**DAWG**”) works hard to raise awareness and interest in Jersey. Combining representatives of the States of Jersey, representatives of the JFSC and other interest groups on the Island, the DAWG is a group of individuals knowledgeable in the fintech space promoting digital assets and blockchain technologies in Jersey. Carey Olsen is a founder member of the DAWG and is an active participant and contributor.

Ownership and licensing requirements

There are no specific additional restrictions or licensing requirements on investment managers owning cryptocurrencies for investment purposes or holding cryptocurrency as an investment advisor or fund manager. We are seeing many fund structures starting to invest in cryptocurrencies and offering crypto-related products. The usual rules applicable to investment managers continue to apply in terms of both the general regulations applicable to them to undertake investment business and in relation to the investment policies described in their offer documentation.

However, as noted above, cryptocurrency-related transactions do constitute “sensitive activities” and we would expect to see additional business risk assessments, policies and procedures relating to that specific asset class. This includes a level of diligence on the providence of the cryptoasset in question to detect any prior illicit activity relating to the asset. There are various service providers such as Chainalysis and Merkle Science that carry out crypto threat detection (i.e. previous transaction screening) and related services that can be used to mitigate the potential risk of acquiring tainted assets.

We do advise fund managers and investment managers looking to enter this space to make contact with us so that we can advise as appropriate. In some instances, it may be appropriate to address new policies with the JFSC.

Mining

Mining cryptocurrencies is not covered by any specific piece of legislation or regulation in Jersey. However, depending on the manner in which mining activities are conducted, it may fall within the existing regulatory framework for funds (mentioned above).

>Border and declaration

At present, there are no border restrictions in place on declaring cryptocurrency holdings.

Reporting restrictions

Equally, there are currently no specific reporting requirements triggered for cryptocurrency payments.

Estate planning and testamentary succession

Cryptocurrencies are treated as intangible movable property. If the owner of the cryptocurrency is a natural person, then the cryptocurrency falls to be dealt with within the movable estate of the owner on his/her death. Although there is no decided case on the point, it is generally assumed that the Jersey Courts would determine the situs of any cryptocurrency by reference to Jersey's private international law rules, which broadly follow and adopt English private international law principles.

Additional considerations need to be given to the practicalities of accessing the digital assets and ensuring that the testator shares access to all private keys, hot and cold wallets and any other form of password-protected account with the administrator or executor of his/her estate to ensure that the digital assets are capable of being accessed and transferred in accordance with the testator's will in the event of his/her demise.

The future of DLT in Jersey

As a nascent technology, international industry practices around blockchain and DLT are still evolving and their applications and use cases (including outside the finance industry) being asserted. To maintain its place as a respected, well-regulated international finance centre, Jersey is cognisant, and encouraging, of the advantages blockchain and DLT bring to Jersey's finance industry.⁵

As a long-established, well-regulated international finance centre, Jersey boasts a host of industry experience and local expertise,⁶ making it an ideal jurisdiction to launch new blockchain and DLT initiatives.

Leveraging this existing expertise and the low-tax environment, we expect to see Jersey and Jersey vehicles continue to be used in both established areas of finance as they embrace blockchain solutions (such as climatech, proptech, online settlement solutions, E-ID and regtech, etc.) and new areas of finance and other sectors as blockchain and DLT use cases are established.

The JFSC's considered and measured approach to fintech regulation to date should equip Jersey to be a leading blockchain and DLT jurisdiction of the future by ensuring that regulation in Jersey remains appropriate and commensurate to the product or service in question.

We would be happy to discuss any blockchain or DLT initiatives backed by persons of substance.

If you have any questions relating to blockchain and cryptocurrency regulation or about our services in this sector, please contact one of the lawyers listed or visit our crypto and blockchain service page.

The full GLI guide to blockchain and cryptocurrency regulation 2022 covers 29 jurisdictions and includes 17 general chapters.

1. In the fintech space, the ICO terminology has now largely been superseded by reference to security and non-security tokens, a reflection of the evolving regulatory backdrop. We retain reference to ICOs in this chapter because we, Carey Olsen, have advised in relation to a number of ICOs and that was the terminology used at that time. The settled approach now is to determine whether a coin or token or other digital asset issued constitutes a security or not and therefore whether it is a "security token" or not. We have addressed STOs and non-security token issuances separately.

2. There is JFSC guidance available: It has been confirmed that this JFSC guidance has a wider application and can be used to inform how digital assets and cryptocurrencies more generally will be treated.

3. The window for applications to participate in the January 2019 pilot has now closed.

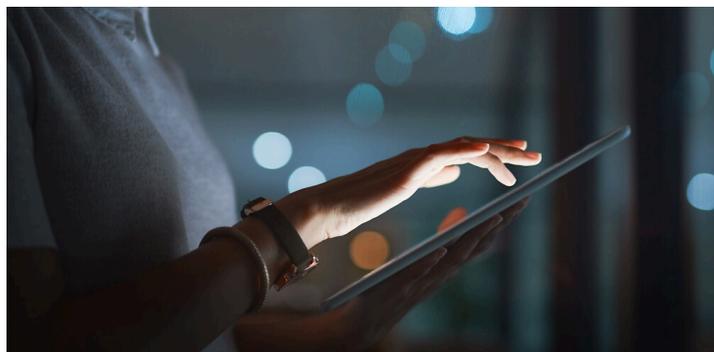
4. See: <https://www.digital.je>.

5. Such as: (i) real-time settlement; and (ii) greater transparency as to origination or provenance of the asset in question. For example, as Jersey currently has no restrictions or requirements around financial settlement, Jersey is an ideal jurisdiction from which to launch securities and cryptocurrency exchanges.

6. Including in banking, international payments, compliance, funds, capital markets, real estate and company administration.

Carey Olsen Jersey LLP is registered as a limited liability partnership in Jersey with registered number 80.

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