



Blockchain and  
cryptocurrency  
regulation 2019,  
first edition

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## **BIGGER PICTURE**



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# Bermuda

## Government attitude and definition

The current Bermuda government was elected in 2017 having undertaken to create new economic pillars in Bermuda, identify new opportunities for economic diversification, and seek local and overseas investment to develop new local industry and thereby create jobs in Bermuda. Since its election, it has enthusiastically embraced the financial technology (“fintech”) sector and the potential it offers, and has repeatedly expressed its intention for Bermuda to be a significant centre for this industry.

In furtherance of this goal, the government is in the process of implementing a comprehensive regulatory regime aimed at providing legal certainty to industry participants and ensuring that business in the sector conducted in or from Bermuda is done in a properly regulated matter, in accordance with the highest international standards. This regulatory regime is described in more detail below, but, in summary:

- a new Digital Asset Business Act has been passed by the Bermuda Parliament and is awaiting royal assent. When passed, this will comprise a regulatory framework for fintech businesses; and
- although not covered by the Digital Asset Business Act, initial coin offerings will be regulated under a separate regime.

The government has also announced that fintech businesses wishing to set up in Bermuda are to benefit from a relaxed work permit policy, and has signed a number of memoranda of understanding with fintech businesses, under which these businesses have committed to establishing operations and creating jobs in Bermuda.

Although digital asset offerings and businesses will be regulated in the manner described in this article, there is no legislation or other provision of Bermuda law affording official or legal recognition of any cryptocurrency or any other digital asset, or conferring equivalent status with any fiat currency. Nor has the government or the Bermuda Monetary Authority (the “BMA”), the territory’s financial regulator and issuer of its national currency, backed any cryptocurrency itself, and the Bermuda dollar remains the territory’s legal tender.

In advance of the publication of such review and any steps to implement the same, however, this chapter sets out the current legal position in the Cayman Islands.

## Cryptocurrency regulation

While both the Bermuda government and the BMA are on record as being keen to embrace the potential offered by fintech, both recognise that the industry presents tremendous risk, requiring prudent regulation.

The Financial Action Task Force (the “FATF”) recommended in its June 2014 report on virtual currencies<sup>1</sup> that regulators, for the time being, focus their efforts on convertible virtual currencies (i.e. those which can be converted into and out of fiat currencies), on the basis that these currencies presented the highest money-laundering risk. This guidance has heavily influenced the BMA in shaping Bermuda’s proposed regulatory regime for digital assets.

## Digital Asset Business Act

In April 2018, the BMA published a consultation paper on the regulation of digital asset business. This consultation exercise has resulted in the enactment of a new Digital Asset Business Act (the “DABA”), which, at the time of writing, had been passed by the Bermuda Parliament and was awaiting royal assent. Once in force, the DABA will be supplemented by rules, regulations, codes of practice, statements of principles and guidance promulgated by the BMA, and so will operate in a similar manner to the regulatory frameworks in place for other financial services regulated by the BMA.

In summary, the DABA will specify the digital asset-related activities to which it applies, impose a licensing requirement on any person carrying on any of those activities, lay out the criteria a person must meet before it can obtain a licence, impose (and permit the BMA to impose) certain continuing obligations on any holder of a licence, and grant to the BMA supervisory and enforcement powers over regulated digital asset businesses.

## Scope of the DABA

The DABA will apply to any entity incorporated or formed in Bermuda and carrying on digital asset business (irrespective of the location from which the activity is carried out) and to any entity incorporated or formed outside of Bermuda and carrying on digital asset business in or from within Bermuda. The term “digital asset” in the legislation is defined widely enough to capture cryptocurrencies, representations of debt or equity in the promoter, representations of other rights associated with such assets, and other representations of value that are intended to provide access to an application or service or product by means of distributed ledger technology. “Digital asset business”, for the purposes of the DABA, will be the provision of the following activities to the general public as a business:

- **Issuing, selling or redeeming virtual coins, tokens or any other form of digital asset**

This is intended to regulate any business providing these services to other businesses or to individuals. It will not include initial coin offerings (“ICOs”) to fund the issuer’s or promoter’s own business or project. Instead, ICOs will be regulated under a separate regime, on which see below.



- **Operating as a payment service provider business utilising digital assets, which includes the provision of services for the transfer of funds**

The term “payment service provider” is used globally in anti-money laundering and anti-terrorist financing (“AML/ATF”) laws, regulations and guidance, and is defined in Bermuda’s Proceeds of Crime (Anti-Money Laundering and Anti-Terrorist Financing) Amendment Regulations 2010 as “a person whose business includes the provision of services for the transfer of funds”. The aim here is to ensure that businesses involved in the transfer of digital assets fall within the DABA’s ambit.

- **Operating as an electronic exchange**

This category will capture online exchanges allowing customers to buy and sell digital assets, whether payments are made in fiat currency, bank credit or in another form of digital asset. Exchanges facilitating the offer of new coins or tokens through ICOs will also be caught.

- **Providing custodial wallet services**

This will cover any business whose services include storing or maintaining digital assets or a virtual wallet on behalf of a client.

- **Operating as a digital asset services vendor**

This category will regulate a person that, under an agreement as part of its business, can undertake a digital asset transaction on behalf of another person or has power of attorney over another person’s digital asset, or a person who operates as a market-maker for digital assets. It is intended to capture any other business providing specific digital asset-related services to the public, such as operating as a custodian of digital assets.

In addition to the above categories, the DABA will include an option for the Minister of Finance, after consultation with the BMA, to be able to add new categories or to amend, suspend or delete any of the categories listed above by order.

The DABA specifically provides that the following activities will not constitute digital asset business:

- contributing connectivity software or computing power to a decentralised digital asset, or to a protocol governing transfer of the digital representation of value (this category will exempt mining from the DABA’s scope);
- providing data storage or security services for a digital asset business, so long as the enterprise is not otherwise engaged in digital asset business activity on behalf of other persons; and
- the provision of any digital asset business activity by an undertaking solely for the purposed of its business operations or the business operations of any of its subsidiaries.

## Licensing requirement

The DABA will require persons carrying on digital asset business to obtain a licence before doing so, unless that person is subject to an exemption order issued by the Minister of Finance. At the time of writing, the Minister had not announced any proposed exemption orders.

Two classes of licence will be available for applicants:

- The Class M licence will be a restricted form of licence, with modified requirements and certain restrictions, and will be valid for a specified period, the duration of which will be determined by the BMA on a case-by-case basis. Following the expiry of this specified period, it is generally expected that the licensee will either have to apply for a Class F Licence (as described in further detail below) or cease carrying on business, although the BMA will have discretion to extend the specified period.
- The Class F licence will be a full licence not subject to any specified period, although it may still be subject to restrictions the BMA may deem appropriate in any given case.

The intention behind this tiered licensing regime is to allow start-ups engaging in digital asset business to do so in a properly supervised regulatory environment, and to engage in proof of concept and develop some sort of track record before obtaining a full licence. The restrictions to which a licensee will be subject will depend on the business model of the prospective licensee (and the risks associated with it), but will almost invariably include an obligation to disclose to prospective customers the fact that the licensee holds a Class M licence and certain limitations on the volume of business the licensee is permitted to conduct, along with other restrictions as the BMA may deem necessary or appropriate on a case-by-case basis.

A prospective licensee may not necessarily receive the licence for which it applies: an applicant for a Class F licence may receive a Class M licence if the BMA decides that a Class M licence would be more appropriate in the circumstances. It is also anticipated that the licence will specify the category (or categories) of digital asset business in which the licensee is permitted to engage.

Carrying on digital asset business without a licence will be a criminal offence punishable by a fine of up to US\$250,000, imprisonment for a term of up to five years, or both.

### Criteria to be met by licensees

The DABA will provide that the BMA may not issue any licence unless it is satisfied that the applicant fulfils certain minimum criteria addressing the fitness and propriety of directors and officers, ensuring business is conducted in a prudent manner, the integrity and skill of the business's management and standards of corporate governance observed by the (prospective) licensee. This is consistent with the position under other regulatory laws applicable to other sectors and is intended to ensure the BMA maintains high standards for the conduct of regulated business. The BMA has also announced an intention to publish a code of practice detailing requirements as to governance and risk management proportionate to the size, complexity and risk profile of a licensee.

The DABA will require licensees to notify the BMA upon changes in directors or officers, and the BMA will have powers to, inter alia, object to and prevent new or increased ownership of shareholder controllers and the power to remove controllers, directors and officers who are no longer fit and proper to carry on their role.

### Continuing obligations of licence holders

Persons holding a licence issued under the DABA will be subject to several ongoing obligations.

**Dissemination of key information to customers:** in order to mitigate the high degree of risk for consumers owing to the highly speculative and volatile nature of digital assets, the BMA has announced it will use powers conferred to it under the DABA to require licensees, before entering into any business relationship with a customer, to disclose to that customer: the class of licence it holds; a schedule of its fees; whether it has insurance against loss of customer assets arising from theft (including cybertheft); the extent to which a transfer or exchange of digital assets is irrevocable and any exceptions; and the extent to which it will be liable for an unauthorised, mistaken or accidental transfer or exchange. Draft rules published by the BMA for this purpose also oblige licensees to confirm certain information regarding transactions with clients at the conclusion of each such transaction.

**Crisis management programme:** the BMA announced in its consultation plans that licensees will be required to develop and implement a comprehensive crisis management, including cybersecurity, programme commensurate to the licensee's nature, size, complexity and risk profile. This programme must be sufficient to enable the licensee to:

- identify internal and external risks;
- protect the licensee's electronic systems and the information stored on them;
- detect systems intrusions and breaches;

- respond to a detected event in order to mitigate negative effects; and
- recover from operational disruption to the normal course of the licensee's business.

Although licensees will be permitted to engage the services of specialist third parties in order to enhance and supplement the strength of their own cybersecurity systems, ultimate responsibility for compliance with these requirements will rest with the licensee.

**Custody and protection of consumer assets:** licensees will be required to have in place and maintain a surety bond, trust account or indemnity insurance for the benefit of their customers. Any such trust account must be maintained with a "qualified custodian", which the DABA will define as a licensed Bermuda bank or trust company or any other person recognised by the BMA for this purpose. A licensee will, in addition, be required to maintain books of account and other records sufficient to ensure that customer assets are kept segregated from those of the licensee and can be identified at any time. All customer funds must be held in a dedicated separate account and clearly identified as such.

**Senior representative:** the DABA will impose an obligation on licensees to appoint a senior representative, to be approved by the BMA, who must be resident in Bermuda and who is sufficiently knowledgeable about both the licensee itself and the industry in general. This senior representative will himself be under a duty to report to the BMA certain significant matters, including: a likelihood of the licensee becoming insolvent; breaches by the licensee of any conditions imposed by the BMA; involvement of the licensee in criminal proceedings, whether in Bermuda or elsewhere; and other material developments.

**Head office:** the DABA also requires licensees to maintain a head office in Bermuda and to direct and manage their digital asset business from Bermuda. The relevant section goes on to list a number of factors the BMA shall consider in determining whether a licensee satisfies this requirement, together with a number of additional factors to which the BMA may (but need not) have regard.

**Annual prudential return:** a licensee will be obliged to file with the BMA an annual prudential return, with the BMA being granted the power to require more frequent filings or additions to a filing if required in the interest of consumer protection. The standard annual prudential return will include information relating to business strategy and risk appetite, products and services, number of customer accounts and geographical profile of accounts, information on risk and cybersecurity (including a risk self-assessment and policies in these areas), audited financial statements and details on any outsourcing to third parties.

## BMA's supervision and enforcement powers

The DABA will grant the BMA wide-ranging powers of supervision and enforcement.

It will have the power to compel production of information and documents (with criminal sanctions for making false or misleading statements), the power to issue such directions as appear to be desirable to it for safeguarding the interests of a business's customers or potential customers, and the power to impose conditions and restrictions on licences. For example, the BMA may:

- require a person or entity to take certain steps or to refrain from adopting or pursuing a particular course of action, or to restrict the scope of its business activities in a particular way;
- impose limitations on the acceptance of business;
- prohibit a person or entity from soliciting business, either generally or from prospective customers;
- prohibit a person or entity from entering into any other transactions or class of transactions; and
- require the removal of any officer or controller.

In more extreme cases, the BMA may revoke a licence altogether and, if it so elects, subsequently petition the court for the entity whose licence it has revoked, to be wound up.

In the event a licensee fails to comply with a condition, restriction or direction imposed by the BMA or with certain requirements of the DABA, the BMA will have the power to impose fines of up to US\$10,000,000. Alternatively, it may issue a public censure ("naming and shaming"), issue a prohibition order banning a person from performing certain functions for a Bermuda regulated entity, or obtain an injunction from the court. It is expected that the BMA will issue guidance in the form of a statement of principles setting out how it proposes to use these enforcement powers shortly after the DABA is passed.

## ICO regulation

As noted above, the DABA will not apply to any ICO intended to finance the issuer's or promoter's own business. Instead, the Companies and Limited Liability Company (Initial Coin Offering) Amendment Act, 2018 (the "ICO Act") will effect amendments to the Companies Act 1981 and the Limited Liability Company Act 2016 which will form a regulatory framework for ICOs. At the time of writing, the ICO Act had been passed by both houses of the Bermuda Parliament and was awaiting royal assent.

The ICO Act will define an ICO as an offer by a company or a limited liability company (a "LLC") to the public to purchase or otherwise acquire digital assets and designate any ICO as a "restricted business activity", requiring consent from the Minister of Finance before any ICO may be made to the public. Private sales and offers of further coins or tokens to existing holders of coins or tokens of the same class will be exempted, as will issuances where the offer is made to a limited number of persons (the actual limit depends on the type of company or LLC the issuer is, and will be 35 in most cases).

The application for consent from the Minister will be required to include specific details regarding:

- the persons managing the issuer and the underlying digital asset(s) offered for sale;
- the development and implementation of any product, service or other project related to the ICO, including timelines for completion;
- the target amount to be raised through the ICO;
- rights, features, functionality and intended transferability of the digital asset(s) offered for sale;
- the technology to be used and confirmation of the ability of the technical platform to enable the collection, confirmation and storage of purchaser identity information; and
- compliance and auditing of ICO transactions.

In addition to obtaining consent from the Minister of Finance, a prospective ICO issuer will also have to publish, in electronic form, an offering document and file this with the Bermuda Registrar of Companies. The offering document must contain:

- details regarding any promoter, including its registered or principal office and details of its officers;
- the business or proposed business of the issuer company or LLC;
- a description of the project to be funded by the ICO and the proposed timeline for the project, including any proposed project phases and milestones;
- the amount of money that the ICO is intended to raise;
- disclosure as to the allocation of the amounts intended to be raised amongst the classes of any issuance (pre-sale, post-ICO etc.);
- any rights or restrictions on the digital assets that are being offered;
- the date and time of the opening and closing of the ICO offer period;
- a statement as to how personal information will be used; and

- a general ICO risk warning containing:
  - information regarding any substantial risks to the project which are known or reasonably foreseeable;
  - information as to a person's rights or options if the project which is the subject of the ICO in question does not go forward;
  - a description of the rights (if any) in relation to the digital assets that are being offered; and
  - information regarding any disclaimer in respect of guarantees or warranties in relation to the project to be developed or any other asset related to the ICO.

If an ICO issuer offers digital assets to the public over a period and any of the particulars in its offering document cease to be accurate in a material respect, the issuer must publish supplementary particulars disclosing the material changes and file these with the Registrar.

The promoter must provide an electronic platform to facilitate communication with prospective investors, and the legislation will also grant investors a cooling-off period during which they will be permitted to withdraw an application to purchase the digital assets offered.

Any person who makes or authorises the making of a false statement in an ICO offering document will be guilty of an offence punishable by a fine of up to US\$250,000, imprisonment for a term of up to five years, or both, unless the person proves either that the statement was immaterial or that at the time he made the statement he had reasonable grounds to believe it was true. Officers of the issuer and promoters of the ICO will also incur civil liability to any person who suffers loss as a result of false statements in the offering document, subject to certain defences.

## Sales regulation

Issuing, selling or redeeming cryptocurrencies will be regulated under the DABA if carried on as a business, and ICOs will be regulated under the ICO Act, in each case in the manner described more particularly above.

## Taxation

There are no income, capital gains, withholding or other taxes imposed in Bermuda on digital assets or on any transactions involving them (the potential application of Bermuda's foreign currency purchase tax is discussed below, under "Border restrictions and declaration"). Moreover, exempted companies or LLCs carrying on digital asset business, including ICO issuers, may apply for, and are likely to receive, an undertaking from the Minister of Finance to the effect that, in the event of there being enacted in Bermuda any legislation imposing tax computed on profits or income or computed on any capital asset, gain or appreciation, then the imposition of any such tax shall not be applicable to such company or to any of its operations.

## Money transmission laws and anti-money laundering requirements

Operating a payment service business utilising cryptocurrency or other digital assets (including the provision of services for the transfer of funds) or operating a digital exchange will constitute a regulated activity for the purposes of the DABA (on which see above).

Bermuda has a long-established and well-earned reputation as an international financial centre, and a crucial aspect of this is its robust AML/ATF regime. Bermuda is also due to undergo its fourth round mutual evaluation by the FATF in 2018.

As part of its consultation exercise on the DABA, the BMA announced that activities falling within the scope of the DABA will be subject to AML/ATF regulation. Consequently, the DABA contains provisions amending certain provisions of Bermuda's existing AML/ATF laws and regulations in order to ensure that the carrying on of digital asset business is expressly captured. However, the BMA also recognises the need for new AML/ATF guidelines relating specifically to the conduct of digital asset business, and at the time of writing the BMA is engaged in the drafting of these guidelines in collaboration with the National Anti-Money Laundering Committee and the Bermuda government. These draft guidelines will be presented, along with a new consultation paper addressing the AML/ATF aspects of digital asset business, for industry feedback in due course.

A detailed discussion of the requirements imposed by Bermuda's AML/ATF regime is beyond the scope of this chapter, but in short, digital asset businesses will be required to establish policies and procedures to prevent money laundering and terrorist financing. These policies and procedures must cover customer due diligence, ongoing monitoring, reporting of suspicious transactions, record-keeping, internal controls, risk assessment and management, and the monitoring and management of compliance with, and internal communication of, these policies and procedures.

## Promotion and testing

As noted at the beginning of this chapter, the Bermuda government is very enthusiastic about the potential offered by fintech for the territory's economy and has launched, or is in the process of developing, a number of initiatives aimed at promoting investment by fintech businesses in Bermuda.

One aspect of this is a new immigration policy for fintech businesses, announced by the Minister of Home Affairs to the Bermuda Parliament in early May 2018. This allows a company operating in the fintech space and which is new to Bermuda to receive immediate approval of up to five work permits for non-Bermudian staff within the first six months of obtaining its business permit. In order to benefit from this, a business must present a plan for the hiring, training and development of Bermudians in entry-level or trainee positions.



A business may not, however, apply for a work permit under this policy in respect of any job categories which are closed (i.e. reserved exclusively for Bermudians, their spouses and permanent resident cardholders only) or restricted (in respect of which a permit may only be obtained for one year) under Bermuda's employment legislation, or which are entry-level, graduate or trainee positions.

Throughout 2018, the government has also been busy entering into a series of memoranda of understandings with various digital asset businesses. Under these memoranda:

- Binance Holdings Limited, the parent company of the Binance Group, the world's largest digital exchange, has committed to develop its global compliance base in Bermuda, creating at least 40 jobs, and to develop a digital asset exchange in Bermuda. It has also undertaken to sponsor university scholarships for Bermudians in blockchain technology development and regulatory compliance, and to make capital available for investment in new Bermuda-based blockchain companies.
- Medici Ventures LLC, a subsidiary of overstock.com (the world's first major enterprise to accept Bitcoin), will create at least 30 jobs in Bermuda over three years, develop a security token trading platform in Bermuda, support the training of Bermudians in software development, and collaborate with government, the BMA and other stakeholders in developing and improving Bermuda's legal and regulatory framework applicable to digital asset businesses.
- Shyft, a blockchain AML/ATF and identity startup, will invest up to US\$10 million over the next three years into Bermuda's economy, support the training of Bermudians in blockchain technology and software development, and collaborate in the development and improvement of Bermuda's digital asset legal and regulatory framework. Shyft has also signed a separate MOU with Trunomi, a Bermuda-based consent and data rights platform, which aims to leverage Shyft's blockchain technology with Trunomi's expertise in consumer consent frameworks to support Bermuda in the implementation of an electronic ID scheme.
- Omega One, an agency brokerage for cryptocurrencies, will open an office in Bermuda, hire at least 20 Bermudians over the next three years, and donate 10% of a planned token sale to philanthropic causes (with 10% of the amount donated going to sports and community clubs in Bermuda).
- Arbitrade, a coin and cryptocurrency exchange, is to move its global headquarters to Bermuda.

## Ownership and licensing requirements

Under current Bermuda law, and under the ICO Act and the DABA, no licensing requirements are (or will be) imposed on any person merely by virtue of that person holding any form of digital asset, unless that person does so in the course of its business and on behalf of another, in which case that person will likely be regarded as a digital asset services vendor and thus subject to regulation under the DABA.

An investment fund incorporated or formed in Bermuda which proposes to deal in digital assets as part of its investment strategy or programme may fall within the ambit of the Investment Funds Act 2006. This requires open-ended funds, subject to certain exceptions, to apply to the BMA for authorisation prior to commencing business, and subjects such funds to the ongoing supervision of the BMA. It does not apply to closed-ended funds, such as private equity funds.

## Mining

Mining is specifically exempted from the scope of the DABA, as currently drafted. It will therefore remain an unregulated activity.

Although mining is not prohibited by any Bermuda law of which we are aware and will not be subject to regulation under the DABA, Bermuda's high energy costs will, it is anticipated, operate as a practical deterrent to the establishment of any mining operations in Bermuda.

## Border restrictions and declaration

Bermuda imposes a foreign currency purchase tax of 1% whenever a Bermuda resident purchases a foreign currency from a Bermuda-based bank. This tax will not apply to most (if not all) purchases of cryptocurrency or other digital assets, on the grounds that these are purchased almost exclusively from digital exchanges, whereas the foreign currency purchase tax applies only to purchases from banks in Bermuda. This renders immaterial the question of whether "foreign currency" in this context would include a cryptocurrency (the BMA has not, to date, expressed a view).

There are no other border restrictions on cryptocurrencies or other digital assets; the only obligation to make a customs declaration in respect of any form of money arises in respect of cash or negotiable instruments in excess of US\$10,000.

## Reporting requirements

Digital asset businesses and their senior representatives will be subject to certain reporting obligations under the regulatory regime to be imposed by the DABA, as described in more detail above. The DABA will not impose any reporting requirements in respect of individual digital asset payments, irrespective of their value.

## Estate planning and testamentary succession

There is no particular regime of Bermuda law which deals specifically with the treatment of cryptocurrencies or other digital assets upon the death of an individual holding them. This means that, in principle, digital assets will be treated in the same way as any other asset and may be bequeathed to beneficiaries in a will, or, if a person dies intestate, will fall to be dealt with under the Succession Act 1974.

The main potential difficulty that may arise is practical and is by no means unique to Bermuda; namely that anyone inheriting any kind of digital asset will, on the face of it, only be able to access that digital asset if the beneficiary has, or can obtain or access, the private key to the wallet in which it is stored. Most exchanges have policies in place to transfer digital assets to next of kin but these policies, and the transfer requirements, will vary between the exchanges.



## Authors



**Michael Hanson**  
Managing Partner

D +1 441 542 4501  
E [michael.hanson@careyolsen.com](mailto:michael.hanson@careyolsen.com)

Michael Hanson is the managing partner of Carey Olsen Bermuda. His core practice is centred on human capital and regulatory law where he advises the largest insurance and reinsurance, banks and professional services businesses on the island.

Michael has particular and significant expertise in corporate, employment and regulatory investigations, complex executive disputes, multijurisdictional crisis management and executive benefit and incentive programs.

Michael is ranked as a leading lawyer by Chambers Global and The Legal 500 describing him as “highly rated”, “very knowledgeable”, and that “his responsiveness is unbelievable!”.



**Adam Bathgate**  
Counsel

D +1 441 542 4511  
E [adam.bathgate@careyolsen.com](mailto:adam.bathgate@careyolsen.com)

Adam is counsel in the Bermuda office and advises on all aspects of Bermuda corporate law. His particular specialisms lie in debt finance transactions, the formation and maintenance of investment funds, and the fintech sector.

Adam has considerable expertise in the areas of fund finance, leveraged and acquisition finance and general lending, whether secured or unsecured. He has also worked on asset finance and structured finance transactions.

In the funds sphere, Adam’s practice is largely focused on the formation and maintenance of private equity, infrastructure and real estate funds, including related downstream deal work, although he also has experience in hedge funds and hybrid funds.

Adam is ranked as a “rising star” in IFLR1000.

## Endnotes

1. Virtual Currencies: Key Definitions and Potential AML/CFT Risks, FATF, June 2014.

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*‘Carey Olsen Bermuda’ is the trading name for Michael Hanson, a barrister and attorney, carrying on Bermuda legal services. The use of the title ‘Partner’ is merely to denote seniority. Services are provided on the basis of our current terms of business, which can be viewed at <http://www.careyolsen.com/sites/default/files/TermsOfBusiness.pdf>*

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# British Virgin Islands

## Government attitude and definition

The British Virgin Islands (“BVI”) regulator, the Financial Services Commission (“FSC”), recognises Bitcoin- and Ether-focused funds. This has resulted in leading fintech companies such as Bitfinex, Finamatrix and Football Coin being incorporated in the BVI. The primary focus of the service providers in the jurisdiction relates to initial coin offerings (“ICOs”) and initial token offerings (“ITOs”). The challenge for the BVI, along with all other jurisdictions, is how to regulate the fundraising for such offerings. Most ICOs and ITOs established in the BVI use the structure of a business company incorporated under the BVI Business Companies Act 2004 (the “BCA”). This provides corporate flexibility, relative free-flow of funds, and low comparative establishment costs associated with a BVI company.

At the present time neither the FSC nor the BVI Government have given any form of regulatory advice or guidance in respect of ICOs or ITOs, nor have they issued any guidance for cryptocurrencies, blockchain or financial technology more generally. The BVI Government has indicated its intention to establish a legal framework that is supportive of the cryptocurrency and financial technology sectors in the BVI, but no draft legislation or consultations have been announced. In the meantime, the consensus view is that the BVI are following a ‘wait and see’ approach to the development of how ICOs and ITOs will be regulated.

Some ICOs and ITOs have been promoted as an unregulated form of investment, relying on the argument that tokens do not constitute a security for the purposes of the different investor protection laws around the world. As a result, some token issuers have used ICOs and ITOs as a means of avoiding regulation. However, depending on the nature of an investor’s rights that attach to a token, it is possible that a token may represent a form of security, particularly if those rights entitle the investor to a share of the profits of the token issuer and the investor is not involved in the day-to-day management and control of the token issuer. Tokens that give investors other rights, such as licences to products and services, could fall outside the scope of being classed as a security. However, token issuers and investors still need to proceed with caution because it is possible that those types of tokens could be classed as a security, depending on the facts and circumstances of each case and the investor protection laws that apply to the tokens. Further, how the gains on tokens are taxed in different countries may also influence how they are recognised for regulatory purposes.

While the consensus is that ICOs and ITOs will not be subject to securities legislation in the BVI, whether or not the legislation applies will be fact-specific and driven by the nature of the underlying assets of the respective offering. In particular, if a company wishes to: (a) collect and pool investor funds for the purpose of collective investment; and (b) issue fund interests that entitle the holder to receive, on demand or within a specified period after demand, an amount calculated by reference to the value of a proportionate interest in the whole or in a part of the net assets of the company, then it will be deemed open-ended and need to be licensed. There are a number of fund options in the BVI, including public funds, professional funds, private funds, approved funds and incubator funds.

With regard to cryptocurrencies, these are not treated as money in the BVI and do not enjoy equal dignity with domestic or foreign fiat currencies. Pursuant to the Legal Tender (Adoption of the United States Currency) Act 1959 and the Coinage and Legal Tender Act 1973, the US dollar is the legal tender of the BVI. BVI legislation is silent regarding the definition of what is money and currency and the existing regulatory framework does not contemplate cryptocurrencies.

There are no government-backed cryptocurrencies and the BVI’s constitutional and currency system means it does not have a central bank.

## Cryptocurrency regulation

As discussed above, there is no current regulatory framework for cryptocurrencies in the BVI; similarly there is no express prohibition. The government has indicated a willingness to establish a supportive legal framework, but the industry is still in its early stages in the BVI. The regulation of cryptocurrencies, ICOs and ITOs will be determined by how the framework for such transactions fits into the existing regulatory framework in the BVI which, as noted, above was drafted without contemplating cryptocurrencies.

## Sales regulation

The Securities and Investment Business Act 2010 (“SIBA”) regulates, amongst others, the provision of investment services from within the BVI. SIBA provides that any person carrying on, or presenting themselves as carrying on, investment business of any kind in or from within the BVI must do so through an entity regulated and licensed by the FSC (subject to the safe harbours in SIBA). Investment business is widely defined and covers: (i) dealing in investments; (ii) arranging deals in investments; (iii) investment management; (iv) investment advice; (v) custody of investments; (vi) administration of investments; and (vii) operating an investment exchange.

“Investments” is also widely defined and may include: (i) shares, interests in a partnership or fund interests; (ii) debentures; (iii) instruments giving entitlements to shares interests or debentures; (iv) certificates representing investments; (v) options; (vi) futures; (vii) contracts for difference; and (viii) long-term insurance contracts.

Cryptocurrencies in general, and tokens under an ICO or ITO, do not fall immediately within any of the above criteria and therefore do not fall under the SIBA regime. Where they may fall under the SIBA regime is where the token that is subject to the ICO or ITO is viewed as security or derivative. This will be fact-specific to the relevant ICO or ITO that is being undertaken and would require a level of detailed analysis in each case.

## Anti-money laundering

BVI AML legislation must be carefully considered with respect to an ICO or ITO. AML legislation primarily focuses on regulated entities in the BVI and requires certain policies and procedures to be established by “relevant persons” conducting “relevant business”. Both the terms “relevant persons” and “relevant business” are strictly defined terms. The requirements seek generally to provide for regulatory rules to minimise and eliminate any form of money laundering or terrorist financing through the BVI. If the company is deemed to carry out “relevant business” (e.g. it is a fund, provides money transmission services, advises on money brokering, etc.) then it has to obtain and maintain client KYC and have internal systems and controls and provide the FSC with a copy of such internal policies for approval.

ICOs of standard utility tokens would not be caught within the definition of “relevant business”, and therefore the company is unlikely to be a “relevant person”. However, the company and its directors should nevertheless be aware of the BVI AML obligations as a way of future-proofing the business.

## Taxation

There are no specific taxes levied against cryptocurrencies in the BVI. The BVI is a tax-neutral jurisdiction and does not have any withholding tax, capital gains taxes, income tax or corporate taxes at the time of writing. In the unlikely event that a BVI entity owns BVI situate land, the entity may be responsible for stamp duties.

Where there is an ICO or ITO, the exchange operators will need to be cognisant of the impact of the Foreign Account Tax Compliance Act (“FATCA”) and Common Reporting Standards, which will be relevant to determining the ultimate beneficial ownership of the BVI entity issuing the ICO or ITO. While these pieces of legislation will not be immediately relevant at the launch of the ICO or ITO, they will need to be considered as the BVI business company acting as the issuer starts to conduct business more generally.

## Money transmission laws and anti-money laundering requirements

The relevant money transmittal law in the BVI is the Financing and Money Services Act, 2009 (“FMSA”) which regulates money services business. FMSA defines money services as including:

- money transmission services;
- cheque exchange services;
- currency exchange services; and
- the issuance, sale or redemption of money orders or travelers’ cheques or other such services.

The regime under FMSA is broadly equivalent to the Payment Services Directive. As set out above, the consensus is that for the purposes of BVI legislation, “money” and “currency” refer to fiat currencies rather than cryptocurrencies. It is therefore unlikely that ICO or ITO transactions solely involving cryptocurrency or digital tokens would be viewed as falling within the definition of money services and the FMSA regime. Where a cryptocurrency transaction is used to facilitate currency exchange services, then this may be viewed as the provision of money services and therefore fall within the remit of FMSA.

## Promotion and testing

There are no “sandbox” or other programmes intended to promote research and investment in cryptocurrency in the jurisdiction at present.

## Ownership and licensing requirements

As discussed above, there are no specific regulatory requirements in respect of cryptocurrencies; set out below is the framework for the approved financial manager regime under BVI law.

For persons wishing to act as an investment manager or investment advisor in the BVI, regulatory approval from the FSC may be obtained under: (1) SIBA; or (2) the Investment Business (Approved Managers) Regulations, 2012 (the “Approved Manager Regulations”). The Approved Manager Regulations were implemented in 2012 with a view to offering a significantly simplified approval process and a lighter regulatory framework than that provided under SIBA.

An Approved Manager’s licence authorises you to act as manager or advisor to: (1) BVI incubator funds; (2) BVI approved funds; (3) BVI private funds; (4) BVI professional funds; (5) funds domiciled in certain recognised jurisdictions; and (6) closed-ended funds domiciled in the BVI or in certain recognised jurisdictions, if they have the key characteristics of a private or professional fund. However, an Approved Manager cannot offer services to public funds.



The Approved Manager can be set up as a BVI company or a BVI partnership. The Approved Manager licence is fairly easy to obtain, provided that the directors of the Approved Manager can demonstrate expertise and experience in the area of investment business. The main restriction is that an Approved Manager must not manage assets exceeding US\$400m if managing regulated investment funds (such as professional and private funds) or US\$1bn if managing unregulated funds. The Approved Manager licence can also be used for the provision of asset management to individuals. The limit on assets under management for the provision of asset-management services depends on the type of asset management to be provided, but will not be below US\$400m.

There are no capital requirements for the Approved Manager and there is no need to appoint a compliance officer. In contrast, a holder of a licence under SIBA will have to submit audited financial statements, appoint a compliance officer, provide employees with compliance training, etc. That said, the advantage of having a licence under SIBA is that there is no limitation on the value of assets under management. For eligible investment managers or investment advisors, the advantage of becoming licensed as an Approved Manager, as opposed to becoming licensed under SIBA, is that the ongoing obligations owed by an Approved Manager are less onerous than those owed by an investment business licensee under SIBA, namely:

An Approved Manager must:

- at all times have at least two directors, one of which must be an individual. However, directors can be resident in any jurisdiction;
- have an authorised representative appointed;
- submit financial statements annually, which need not be audited; and
- submit an annual return which has to contain certain prescribed information such as that the directors continue to be fit and proper, details of the persons to whom the manager provides service, complaints received, etc.

## Mining

Mining Bitcoin in the BVI is permitted and there are no current regulations in respect of mining activity.

## Border restrictions and declaration

Further to the earlier distinction between cryptocurrency holdings and fiat currency, there are no border restrictions or obligations currently in place in the BVI in respect of cryptocurrencies.

## Reporting requirements

There are no reporting requirements or thresholds for payments made by cryptocurrency currently in place in the BVI. The Beneficial Ownership Secure Search System Act 2017 (“BOSS”) requires BVI companies and their registered agents to record information about the beneficial ownership of a BVI company on a central government-controlled, but confidential, database. Beneficial ownership is determined by reference to control tests, i.e. share ownership, voting rights, the right to remove a majority of the board of directors, and the exercise of significant influence and control over a company.

## Estate planning and testamentary succession

Cryptocurrencies have not been widely used for the purposes of estate planning and testamentary succession under BVI law. If, in the unlikely event that the cryptocurrency is regarded as an asset actually situated in the BVI, then a deceased’s cryptocurrency could not be validly transmitted to his/her heirs or beneficiaries until an application is made to the BVI High Court Probate Registry (the “Registry”). To deal with the deceased’s cryptocurrency, a person would need to be appointed as legal personal representative of the deceased, by obtaining the appropriate grant from the BVI Probate Registry. There are two types of grant that may be obtained: (1) Grant of Probate (where the deceased left a will which expressly deals with the BVI cryptocurrency); and (2) Grant of Letters of Administration (where the deceased did not leave a will expressly covering the BVI cryptocurrency). In respect of the latter, the deceased would be deemed to have died “intestate” in relation to the BVI cryptocurrency – even if they had a valid will covering assets in other jurisdictions.



## Authors



### Clinton Hempel

Managing Partner, BVI

D +27 76 412 6091

E [clinton.hempel@careyolsen.com](mailto:clinton.hempel@careyolsen.com)

Clinton is the managing partner of Carey Olsen's British Virgin Islands practice group.

Clinton has practised law for over 20 years and has significant experience in advising financial institutions, public and private businesses, high-net-worth individuals and their onshore advisers on the laws of the British Virgin Islands.

He advises on a wide range of corporate and commercial transactions, financings and investment structures, including takeovers, joint ventures, mergers and acquisitions and public and private equity transactions. Clinton also advises on all aspects of BVI regulatory compliance and risk management.



### Mark Harbison

Associate

D +1 284 394 4034

E [mark.harbison@careyolsen.com](mailto:mark.harbison@careyolsen.com)

Mark is an associate in Carey Olsen's British Virgin Islands office. Mark focuses on a broad range of corporate, commercial and finance transactions.

Mark has acted for a wide variety of clients in respect of mergers and acquisitions, cross-border debt finance, corporate restructurings and voluntary liquidations. Mark has also worked on a number of BVI regulatory compliance projects.

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*Please note that this guide is only intended to provide a very general overview of the matters to which it relates. It is not intended as legal advice and should not be relied on as such. © Carey Olsen 2018*

Cayman Islands  
blockchain and  
cryptocurrency  
regulation 2019,  
first edition



# Cayman Islands

## Government attitude and definition

The Cayman Islands is a leading global financial centre and has, over the course of several decades, developed a reputation as one of the world's most innovative and business-friendly places to operate. The jurisdiction offers a stable society and political system, judicial and legislative links to the United Kingdom, tax neutrality, many sophisticated service providers, and a proportionate regulatory regime that focuses closely on the financial services industry, and in particular those catering to sophisticated and institutional investors based elsewhere.

It is this reputation and these attributes that have helped the jurisdiction become an obvious choice for many of those proposing to establish fintech-related structures, whether it be in the form of a fund vehicle investing into Digital Assets,<sup>1</sup> an exchange for the same, an initial coin offering ("ICO"), or otherwise.

Each of the Cayman Islands Government, the Cayman Islands Monetary Authority ("CIMA"), and industry bodies such as Cayman Finance, acknowledge the importance of continuing to attract fintech business to the jurisdiction and ensuring the further growth of the sector. They are also aware, however, of the need to balance this approach with maintaining the Cayman Islands' commitment to the highest standards of financial probity and transparency and the specific considerations that can accompany Digital Assets.

Consequently, there has been no precipitous introduction of new regulation of the Digital Asset space, but rather a more judicious review of the sector and existing regulatory framework. Currently, the Cayman Islands Government is in the process of considering the proposals of an industry working group convened by CIMA regarding the adoption of any additional regulatory measures or governance standards for the marketing or trading of Digital Assets within and from the Cayman Islands. It is anticipated that the conclusion of this review will be made public shortly, but our expectation is that the results of the process are unlikely to lead to a wholesale or dramatic change of the current regulatory burdens, and will instead maintain the existing pro-industry approach while providing welcome clarification on certain areas of potential ambiguity.

In advance of the publication of such review and any steps to implement the same, however, this chapter sets out the current legal position in the Cayman Islands.

## Cryptocurrency regulation

Save for certain aspects of the Cayman Islands anti-money laundering regime (as further detailed below), the Cayman Islands has not enacted any law or imposed any regulation that specifically targets Digital Assets.

As such, whether any activity involving a Digital Asset is subject to regulation will largely be determined in accordance with: (a) the nature of the activity being conducted; and (b) how the relevant Digital Asset would best be classified within the existing legislative framework.

Although a detailed analysis of each is outside the scope of this chapter, a summary of the statutory regimes that are most likely to be of relevance are as follows:

### The Mutual Funds Law

Pursuant to the Mutual Funds Law of the Cayman Islands, an entity formed or registered in the Cayman Islands that issues equity interests and pools the proceeds thereof, with the aim of spreading investment risks and enabling investors to receive profits or gains from the acquisition, holding, management or disposal of investments, may come within the ambit of that statute and be required to obtain a registration or licence from CIMA.<sup>2</sup> The particular nature or classification of the Digital Assets will not generally be of relevance, provided they are being held as an investment.

As such, any pooling vehicle that is investing into the Digital Asset space or accepting Digital Assets by way of subscription and then investing into more traditional asset classes, would be advised to seek Cayman Islands legal advice on the point.

### The Securities Investment Business Law

Pursuant to the Securities Investment Business Law of the Cayman Islands, an entity formed or registered in or that is operating from the Cayman Islands which engages in dealing, arranging, managing or advising on the acquisition or disposal of Digital Assets, may come within the ambit of the Securities Investment Business Law and be required to obtain a registration or license from CIMA. This will, however, only apply to the extent that such Digital Assets constitute "securities" for the purposes thereof. The statute contains a detailed list of assets that are considered securities thereunder. Although such list does not currently make specific reference to any Digital Asset, in our view, certain types of Digital Asset are likely to constitute securities. Consequently, consideration will need to be given on a case-by-case basis as to whether the Digital Asset in question falls within one of the existing categories; for example, instruments creating or acknowledging indebtedness, options or futures. Equally, however, it seems clear that certain Digital Assets are likely to fall outside the definition, and thus outside the scope of the law (for instance, pure utility tokens and some cryptocurrencies).

### The Money Services Law

Please see below for further details.

### Anti-money laundering regulations

Please see below for further details.

## Sales regulation

There are no securities or commodities laws in force in the Cayman Islands that apply specifically to Digital Assets (although please see the requirements of the Securities Investment Business Law as detailed above), whether in relation to their marketing and issuance by a Cayman Islands entity (e.g. pursuant to an ICO), or their sale by an existing holder.

In relation to the offering of securities or interests more broadly, where issuances or sales are targeted at investors based outside of the Cayman Islands, Cayman Islands law does not generally impose any prohibition or regulatory burden; it will instead look to the local authorities where such investors are based, to restrict or regulate the same as they see fit. With that said, this is one area in which the Cayman Islands Government's review may lead to further regulation; specifically, in circumstances where structures are established in order to offer Digital Assets to retail investors based elsewhere. Whether or not this is seen as a suitable step will, however, likely depend in part on the speed with which the major on-shore jurisdictions clarify their approach to Digital Assets under their own securities law regimes.

In relation to the offering, sale, or issuance of interests within the Cayman Islands, however, certain regulatory provisions should be borne in mind. For example, the Companies Law prohibits any exempted company formed in the Cayman Islands and not listed on the Cayman Islands Stock Exchange from offering its securities to the Cayman Islands public. The Limited Liability Companies Law includes a similar prohibition in relation to LLCs. Even persons based, formed or registered outside the Cayman Islands should be careful not to undertake any activities in relation to a sale or issuance of Digital Assets that would constitute "carrying on a business" in the Cayman Islands. To do so may entail various registration and licensing requirements and financial and criminal penalties for those who do not comply. There is no explicit definition of what will amount to "carrying on a business" for these purposes, and consequently, persons who propose to undertake concerted marketing to the Cayman Islands public, particularly if it involves engaging in any physical activity in the Cayman Islands, are encouraged to seek specific legal advice on the point.

In practice, however, these restrictions do not generally pose much of a practical concern for issuers given that:

- the "public" in this instance is taken to exclude other exempted companies, exempted limited partnerships, and LLCs (which together comprise the majority of Cayman Islands entities); and
- issuers' target investors tend not to include other persons physically based in the Cayman Islands themselves.

For completeness, and as detailed further above, Cayman Islands persons, or those operating from within the Cayman Islands, arranging for the sale or issuance of Digital Assets by another, may come within the ambit of the Securities Investment Business Law regardless of where the activity takes place, or the ultimate investors are based.

## Taxation

There are no income, inheritance, gift, capital gains, corporate, withholding or other such taxes imposed by the Cayman Islands government, including with respect to the issuance, holding, or transfer of Digital Assets.

Stamp duty may apply to original documents that are executed in the Cayman Islands (or are brought into the Cayman Islands following execution). However, the sums levied are generally of a nominal amount.

Entities formed or registered in the Cayman Islands may also apply for and, upon the payment of a fee of approximately US\$1,830, receive a tax exemption certificate confirming that no law enacted in the Cayman Islands after the date thereof imposing any tax to be levied on profits, income, gains or appreciations shall apply to such entity or its operations. Such certificates will generally apply for a period of between 20 and 50 years (depending on the type of entity).

## Money transmission laws and anti-money laundering requirements

### Money transmission laws

Pursuant to the Money Services Law, any person carrying on a "money services business" in or from the Cayman Islands must first obtain a licence from CIMA. Any breach of this requirement will constitute a criminal offence.

For the purposes of the foregoing, a "money services business" means the business of providing (as a principal business), among other things, money transmission or currency exchange services.

Although there is no clear authority on the extent to which the foregoing would be seen to include such transactions in cryptocurrency or other Digital Assets, a cautious and substantive reading of the statute may, in some cases, warrant it. In particular, if the Digital Assets in question are primarily used to facilitate the transfer of fiat currency from one party to another, or the conversion between fiat currencies, the legislation may well apply. Consequently, persons wishing to establish such businesses are encouraged to consider closely the application of the Money Services Law and consult appropriate advisors.

Although a consideration of the requirements of the licensing application and approval process under the Money Services Law is beyond the scope of this chapter, it will generally require:

- the maintenance of specified capital levels;
- the appointment of approved auditors;
- the provision of audited financials to CIMA;
- the maintenance of proper records; and
- the payment of an annual fee.

### Anti-money laundering requirements

The very nature and, in some cases, the intended features of Digital Assets can present heightened compliance risks and, moreover, practical hurdles to addressing the same. Such features may include the lack of a trusted central counterparty, increased anonymity, and ease of cross-border transfer without any gating or restriction.

Consequently, the Cayman Islands authorities have maintained a keen focus on balancing the jurisdiction's long track record of innovation and the promotion of a business-friendly environment with its commitment to the prevention of crime and maintaining robust standards of transparency. To date, this has been done, not by establishing an entirely separate regime for Digital Assets, but by applying the purposive approach enshrined within the existing framework which focuses on the specific activity and the nature of the assets in question so as to properly quantify the risk that the same may be used to facilitate illegal activity. With that said, we anticipate that the Cayman Islands authorities will continue to provide clarifying guidance and updates to address any ambiguities or uncertainties that arise in relation to the current regime.

Pursuant to the provisions of the Proceeds of Crime Law, the Anti-Money Laundering Regulations, and the guidance notes thereon (together the "AML Laws"), any persons formed, registered or based in the Cayman Islands conducting "relevant financial business" are subject to various obligations aimed at preventing, identifying, and reporting money laundering and terrorist financing.

"Relevant financial business" is defined in the Proceeds of Crime Law, and encompasses a broad variety of activity, including the following which may be of particular relevance in the context of Digital Assets:

- money or value-transfer services;
- issuing and managing means of payment (specifically including electronic money);
- trading in transferable securities;
- money broking;
- securities investment business; and
- investing or administering funds or money on behalf of others.

As such, the relevant requirements may depend on the type of Digital Asset in question; for instance, whether it can best be classed as a currency or money substitute, a security, a utility token or something else. We would thus generally expect businesses that engage in the operation of cryptocurrency exchanges, cryptocurrency issuances, brokering transactions in cryptocurrency, the trading and management of Digital Assets that are properly classed as securities, and the investment of funds (whether in the form of fiat currency or cryptocurrency) on behalf of others into Digital Assets, to come within the scope of the AML Laws. Notably, Digital Assets that are purely in the nature of utility tokens may fall outside of the ambit of the regime. However, specific legal advice on such distinctions is vital to ensure proper compliance and readers are encouraged to generally adopt conservative approach.

Although a detailed consideration of the specific requirements of the AML Laws falls outside of the scope of this chapter, any person subject to the regime will generally need, among other things, to do the following:

- appoint a named individual as anti-money laundering compliance officer to oversee its adherence to the AML Laws and to liaise with the supervisory authorities;
- appoint named individuals as the money laundering reporting officer and a deputy for the same to act as a reporting line within the business; and
- implement procedures to ensure that counterparties are properly identified, risk-based monitoring is carried out (with specific regard to the nature of the counterparties, the geographic region of operation, and any risks specifically associated with new technologies such as Digital Assets), proper records are kept, and employees are properly trained.

As above, particular practical concerns will often arise in relation to Digital Assets, specifically with regard to the identification of counterparties and the monitoring of source and use of funds. Most, in our experience, will be best advised to consult specialist third party providers to assist with this process.

### Promotion and testing

There are currently no 'sandbox' or other similar programmes in place in the Cayman Islands. However, the Cayman Islands Government has been vocal in promoting the Special Economic Zone ("SEZ") to those wishing to develop fintech-related products from the jurisdiction.

The SEZ offers businesses focused on the fintech industry the opportunity to establish physical operations within the Cayman Islands in a more streamlined manner. It provides several benefits, including a simpler, more rapid, and cost-effective work permit process, concessions with respect to local trade licences and ownership requirements, the ability to be operational within four to six weeks, and allocated office space.



When coupled with the other benefits of the jurisdiction and its recently updated intellectual property laws, the SEZ has proven highly popular with the fintech industry. To date, over 50 blockchain-focused companies have been established within it and this is expected to continue to grow. The SEZ also hosts a number of industry-focused events and conferences.

### Ownership and licensing requirements

The Cayman Islands does not impose any restrictions or licensing requirements that are specifically targeted at the holding, management or trading of Digital Assets, whether by those doing so for their own account, or those doing so as a manager, trustee or advisor for the account of others.

As such, whether or not any such licensing or regulatory requirement is applicable to a particular activity will fall to be determined in accordance with the existing regulatory regimes, such as the Mutual Funds Law or the Securities Investment Business Law (each as further detailed above).

As also outlined further above, investment funds and managers that operate in the Digital Assets space are likely to need to comply with the requirements set out in the AML Laws.

### Mining

The mining of Digital Assets is not regulated or prohibited in the Cayman Islands. We would note, however, that the import duties applicable to computing equipment and the high cost of electricity production in the Cayman Islands are likely to present practical deterrents to the establishment of any material mining operations within the jurisdiction. It is possible that the increased availability of renewable energy options, and the falling price of the same, may mitigate this somewhat in the future.

### Border restrictions and declarations

The Cayman Islands does not impose any general border restrictions on the ownership or importation of Digital Assets.

As part of the Cayman Islands' commitment to combating money laundering and terrorist financing, the Customs (Money Declarations and Disclosures) Regulations mandate that individuals transporting money amounting to CI\$15,000 (approximately US\$18,292) or more into the Cayman Islands must make a declaration in writing to customs officers at the time of entry. However, the Customs Law defines "money" as being confined to cash (i.e. bank notes or coins that are legal tender in any country) and bearer-negotiable instruments (i.e. travellers cheques, cheques, promissory notes, money orders). As such, we would not expect such a requirement to apply to Digital Assets. Further, given the nature of Digital Assets, particularly those based or recorded on a distributed ledger, there is also the conceptual question of what would amount to the importation or transportation of the same.

### Reporting requirements

There are no reporting requirements in the Cayman Islands specifically targeted at payments of, or transfers in, Digital Assets.

As above, to the extent that such a payment or transfer is made in the context of the conduct of "relevant financial business" for the purposes of the AML Laws, there may of course be an obligation to make certain filings or reports in the event that there is a suspicion of money laundering or other criminal activity.

### Estate planning and testamentary succession

There is no particular regime under Cayman Islands law which deals specifically with the treatment of cryptocurrencies or other Digital Assets upon the death of an individual holding them. This means that, in principle, and assuming Cayman law governs succession to the deceased's estate, Digital Assets will be treated in the same way as any other asset and may be bequeathed to beneficiaries in a will, or, if a person dies intestate, will fall to be dealt with under the intestacy rules in the Cayman Islands Succession Law.

Although, as is the case in many jurisdictions beyond the Cayman Islands, there is likely to be some uncertainty as to where the situs of a Digital Asset is located (or indeed whether or not a situs can be determined at all), to the extent that the asset can be analysed under traditional conflict-of-laws rules as sited in the Cayman Islands, then a grant of representation would be required from the Cayman Islands court to preclude the risk of intermeddling claims in dealing with the asset in the Cayman Islands.

The main potential difficulty that may arise is practical; namely that anyone inheriting a Digital Asset will, on the face of it, often only be able to access that Digital Asset if the personal representative of the deceased or the beneficiary (as the case may be) has or can obtain the information needed in order to gain access and control over that Digital Asset (e.g. a private key to the wallet in which it is stored). Most exchanges have policies in place to transfer Digital Assets to next of kin but these policies, and the transfer requirements, will vary between the exchanges.



## Authors



### Alistair Russell

Partner

D +1 345 749 2013

E [alistair.russell@careyolsen.com](mailto:alistair.russell@careyolsen.com)

Alistair is a partner in the corporate and finance group of Carey Olsen in the Cayman Islands and advises on all aspects of finance, fintech, corporate, investment funds and commercial law.

He has advised clients on a broad range of transactions including financing, fintech, ICOs, private equity, joint ventures, mergers and acquisitions and capital markets, and is described by clients in IFLR1000 as “the best Cayman lawyer we’ve ever worked with”.

Alistair was formerly with Skadden, Arps, Slate Meagher & Flom and Cleary, Gottlieb, Steen & Hamilton, each in London.

Alistair obtained a Bachelor of Civil Law with distinction from ChristChurch, Oxford University, and an LL.B. with first class Honours from King’s College London.



### Dylan Wiltermuth

Counsel

D +1 345 749 2010

E [dylan.wiltermuth@careyolsen.com](mailto:dylan.wiltermuth@careyolsen.com)

Dylan is a counsel in the corporate and finance group of Carey Olsen in the Cayman Islands and advises on all aspects of on securities, corporate and structured finance and public and private M&A.

He has spent many years advising clients on complex cross-border transactions across a wide range of jurisdictions and has a demonstrable track record of success in mitigating risk and delivering results.

Dylan was formerly with Kirkland & Ellis in London and Freshfields Bruckhaus Deringer in London and New York.

Dylan obtained an LL.B. with first class Honours from Bond University.

## Endnotes

1. For the purposes of this chapter, “Digital Assets” shall be used to include all forms of blockchain-based units, whether in the form of securities-like tokens, utility tokens, cryptocurrencies or otherwise.
2. Notably, if the entity itself is “closed-ended” in nature, it will generally fall outside the scope of the law.

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Guernsey  
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# Guernsey

## Government attitude and definition

The Bailiwick of Guernsey (“Guernsey”), as one of the world’s leading financial centres, has always been an early adopter of financial innovation and has a reputation for expertise and stability. The first ever commercial deployment of blockchain technology for the private equity market in early 2017, which was pioneered in Guernsey by Northern Trust and IBM, demonstrates that Guernsey is very much open to new innovation and development.

The Guernsey Financial Services Commission (the “Commission”) is the body responsible for the regulation of the finance sector. One of the founding objectives of the Commission is to protect the public, and to protect and enhance the reputation of Guernsey as a financial services centre, and one of the ways that the Commission seeks to fulfil this objective is to adhere the highest international standards of compliance and transparency and to adopt a policy of encouraging promoters of only the highest calibre. Accordingly, the Commission has issued advice calling for caution in the field of digital, virtual or cryptocurrencies (“Virtual Currencies”) and initial coin offerings (“ICOs”). The Commission has indicated that whilst it has a broad policy of encouraging innovation, and is keen to liaise with firms or individuals to discuss potential applications, it believes that there are potential risks in the use of Virtual Currencies especially for retail customers. The Commission has indicated that it would be cautious about approving applications for ICOs which could then be traded on a secondary market, or the establishment of a digital currency exchange within Guernsey, due to the significant risk of fraud and/or money laundering, and has generally issued advice to investors that when investing in Virtual Currencies they should act with extreme caution – and be prepared to lose the entire value of their investment.

At present, there are no cryptocurrencies backed by Guernsey’s government, the States of Guernsey, and Guernsey does not have a central bank. There have been no pronouncements from the States of Guernsey or the Commission which would indicate that Virtual Currencies are given any form of equal status as domestic currency, although it should be noted that there have similarly been no pronouncements that would indicate that Virtual Currencies will not be treated as a currency or foreign currency.

In general, funds seeking to invest in Virtual Currencies should be aware that whilst the Commission is generally cautious about the regulatory approach which should be taken in relation to Virtual Currencies and ICOs, Guernsey as a jurisdiction is keen to encourage financial innovation, and provided that an applicant can satisfy the Commission that key controls are in place for the protection of investors, there should be no reason why a responsible fund should not be regulated in Guernsey by the Commission.

## Cryptocurrency regulation

Guernsey does not at present have any specific regulatory laws or guidance relating to any form of Virtual Currencies or ICOs, but the nature of Guernsey’s existing regulatory laws is such that Virtual Currencies and ICOs could be capable of regulation in a number of ways. The Commission has indicated that it will assess any application for regulation by the same criteria that it uses for any other asset types or structure, and look to ensure that key controls around custody, liquidity, valuation of assets and investor information are in place.

A fund based on Virtual Currencies or the making of an ICO, if required to be regulated, is likely to fall under one of two regulatory regimes; that of the Protection of Investors (Bailiwick of Guernsey) Law, 1987 (as amended) (the “POI Law”) or the Registration of Non-Regulated Financial Services Businesses (Bailiwick of Guernsey) Law, 2008 (the “NRFSB Law”).

### Regulatory position under the POI Law

Every “collective investment scheme” (a “fund”) domiciled in Guernsey is subject to the provisions of Guernsey’s principal funds legislation – the Protection of Investors (Bailiwick of Guernsey) Law, 1987, as amended (the “POI Law”) – and regulated by the Commission.

Broadly speaking:

- Every fund domiciled in Guernsey (a “Guernsey fund”) must be administered by a Guernsey company which holds an appropriate licence under the POI Law (a “POI Licence”).<sup>1</sup> The administrator is responsible for ensuring that the fund is managed and administered in accordance with the fund documentation.
- Every open-ended Guernsey fund must also appoint a Guernsey company which holds a POI Licence to act as custodian (or trustee, where the Guernsey fund is structured as a unit trust). The trustee/custodian is (with limited exceptions) responsible for safeguarding the assets of the fund and, in some of the rules, to oversee the management and administration of the fund by the administrator.

The POI Law makes it a criminal offence, subject to certain exceptions, for any person to carry on or hold himself out as carrying on any controlled investment business in or from within the Bailiwick of Guernsey without a POI Licence. Additionally, it is an offence for a Bailiwick body to carry on or hold itself out as carrying on any controlled investment business in or from within a territory outside the Bailiwick of Guernsey unless that body is licensed to carry on that business in the Bailiwick and the business would be lawfully carried on if it were carried on in the Bailiwick.



Guernsey funds regulation only applies to “collective investment schemes” – arrangements relating to property of any description which involve:

- the pooling of contributions by investors;
- third party management of the assets; and
- a spread of risk.

Thus arrangements with a single investor or a single asset would not usually be classified as a fund.

The POI Law divides Guernsey funds into two categories:

- “registered funds”, which are registered with the Commission; and
- “authorised funds”, which are authorised by the Commission.

The difference between authorised funds and registered funds is essentially that authorised funds receive their authorisation following a substantive review of their suitability by the Commission, whereas registered funds receive their registration following a representation of suitability from a Guernsey body holding a POI Licence (the administrator, who scrutinises the fund and its promoter in lieu of the Commission and takes on the ongoing responsibility for monitoring the fund).

The POI Law grants the Commission the power to develop different classes of authorised and registered funds and determine the rules applicable to such classes.

Funds seeking authorisation or registration must therefore satisfy the requirements of the POI Law and (where applicable) the applicable rules specified by the Commission.

The rules governing the different classes of Guernsey funds state whether funds in each class may be open-ended or closed-ended (or whether they may choose from either).

A Guernsey fund is open-ended if the investors are entitled to have their units redeemed or repurchased by the fund at a price related to the value of the property to which they relate (i.e. the net asset value).

There is no prescribed period within which the redemption must occur or the moneys be paid.

Fund types in Guernsey include, but are not limited to:

- Registered Collective Investment Schemes (a registered open- or closed-ended fund governed by the Registered Collective Investment Schemes Rules 2015 and the Prospectus Rules 2008).
- Private Investment Funds (a registered open- or closed-ended fund governed by the Private Investment Fund Rules 2016).

- Class A Funds (an authorised open-ended fund governed by the Authorised Collective Investment Schemes (Class A) Rules 2008). Class A Funds are primarily designed for offering to retail investors.
- Class B Funds (an authorised open-ended fund governed by the Authorised Collective Investment Schemes (Class B) Rules 2013). Class B Funds are the most popular form of fund and are suitable for retail and institutional investors alike.
- Class Q Funds (an authorised open-ended fund governed by the Authorised Collective Investment Schemes (Qualifying Professional Investor Funds) (Class Q) Rules 1998). Class Q Funds benefit from a lighter regulatory regime and are therefore limited to Qualifying (sophisticated) Investors.
- Authorised closed-ended funds (an authorised closed-ended fund governed by the Authorised Closed-Ended Investment Schemes Rules 2008).

### Regulatory position under the NRFSB Law

The NRFSB Law provides that if an entity carries out certain “financial services businesses” in or from within the Bailiwick by way of business then it must, subject to certain exceptions (see below), register with the Commission. A financial services business which is not registered is guilty of an offence.

The NRFSB Law provides that a business holds itself out as carrying on business in or from within the Bailiwick if:

- by way of business, it occupies premises in the Bailiwick or makes it known by an advertisement or by an insertion in a directory or by means of letterheads that it may be contacted at a particular address in the Bailiwick;
- it invites a person in the Bailiwick, by issuing an advertisement or otherwise, to enter into or to offer to enter into a contract or otherwise to undertake business; or
- it is otherwise seen to be carrying on business in or from within the Bailiwick.

### Financial services business

The NRFSB Law only applies to businesses specified in Schedule 1 of the NRFSB Law, the relevant parts of which are summarised as follows:

- Facilitating or transmitting money or value through an informal money or value-transfer system or network.
- Issuing, redeeming, managing or administering means of payment, including, without limitation, credit, charge and debit cards, cheques, travellers’ cheques, money orders and bankers’ drafts and electronic money.

For the purposes of the NRFSB Law, the activities listed will only constitute “financial services businesses” when carried on: (i) by way of business; and (ii) for or on behalf of a customer”. “By way of business” is interpreted to mean charging some form of fee for the service provided.

A business will not constitute a “financial services business” for the purposes of the NRFSB Law if it is a “regulated business”, meaning business carried on in accordance with a licence granted under: the Banking Supervision (Bailiwick of Guernsey) Law, 1994, as amended; the POI Law; the Insurance Business (Bailiwick of Guernsey) Law, 2002, as amended; or the Insurance Managers and Insurance Intermediaries (Bailiwick of Guernsey) Law, 2002, as amended.

### Exceptions

Businesses undertaking “financial services business” on an incidental or occasional basis may not be required to register with the Commission. To be excluded, the business must meet all of the criteria below:

- the total turnover of that business, plus that of any other financial services business carried on by the same person, does not exceed £50,000 per annum;
- no occasional transactions are carried out in the course of such business, that is to say, any transaction involving more than £10,000, where no business relationship has been proposed or established, including such transactions carried out in a single operation or two or more operations that appear to be linked;
- the turnover of such business does not exceed 5% of the total turnover of the person carrying on such business;
- the business is ancillary, and directly related, to the main activity of the person carrying on the business;
- in the course of such business, money or value is not transmitted or such transmission is not facilitated by any means;
- the main activity of the person carrying on the business is not that of a financial services business;
- the business is provided only to customers of the main activity of the person carrying on the business and is not offered to the public; and
- the business is not carried on by a person who also carries on a business falling within Paragraphs 20 to 23A of Part I of Schedule 1 to the NRFSB Law.

In addition, activities that are merely “incidental and other activities”, as listed in Part III of Schedule I of the NRFSB Law, do not constitute “financial services businesses”. In short, these relate to activities carried out in the course of carrying on the professions of a lawyer, accountant or actuary.

### Requirement to register

This is still an evolving regulatory area in Guernsey, and there is some uncertainty as to whether cryptocurrency falls within the terms set out in B) above (and Schedule 1 of the NRFSB Law), but as these are not exhaustive, the cautious approach would be to assume that this section is wide enough to capture cryptocurrency. Further, A) also refers to transfer of money or value, which is wide enough to capture cryptocurrency.

### Application to virtual currencies

A person is treated as carrying on controlled investment business if he engages by way of business in any of the “restricted activities” specified in Schedule 2 of the POI Law in connection with any “controlled investment” identified and described in Schedule 1 of the POI Law. The scope of this chapter does not permit a detailed look at either of these concepts, but generally “restricted activities” include the promotion of funds, dealings with investments (including buying, selling, subscribing for, borrowing, lending or underwriting an investment) or making arrangements for another person to do the same, or operating an investment exchange, each in connection with a controlled investment, which can include either open- or closed-ended collective investment schemes, or general securities and derivatives.

Whether a POI Licence is necessary in relation to an ICO or a fund engaged in any way with a Virtual Currency will largely turn on whether such a Virtual Currency can legitimately be defined as a security. This is likely to be tested on a case-by-case basis in practice, but consideration may be given to whether a Virtual Currency is asset-based or whether it is a more “pure” cryptocurrency.

Given the uncertainty surrounding the nature of Virtual Currencies in Guernsey, it would be prudent to assume that where an endeavour in Guernsey is not subject to regulation under the POI Law, it will be registrable under the NRFSB Law.

### Sales regulation

At present, there are no securities laws or commodities laws in Guernsey regulating the sale of Bitcoin or tokens. The POI Law makes it a general offence to operate an investment exchange in relation to a controlled investment without an appropriate POI Licence, but it is generally unclear if any specific Virtual Currency would constitute a “security” for the purpose of the POI Law, and whilst the Commission have not yet adopted an official position on the matter, it would likely find guidance issued by the prominent financial regulators (the U.S. Securities Exchange Commission, the UK Financial Conduct Authority, etc.) persuasive. Given the general uncertainty in this area, it would be prudent for any individual or firm contemplating engaging in the business of running an investment exchange in relation to any Virtual Currency to consult with the Commission at the early stages.

## Taxation

There are no specific laws in Guernsey regulating the taxation of Virtual Currencies, and it is therefore likely that they will be taxed in accordance with general Guernsey taxation principles and provisions.

Guernsey does not have a concept of value added, goods and services or consumption tax, capital gains tax, net wealth/net worth tax or inheritance tax (although there are registration fees and ad valorem duty for a Guernsey Grant of Representation where required). Similarly, apart from transfers of Guernsey real property or transfers of interest in certain unlisted entities (other than collective investment schemes) that have a direct or indirect interest in Guernsey real property, which may (subject to exemption) attract a document duty, no stamp or transfer taxes are applicable. Withholding taxes are payable at a rate of 20% solely in relation to the payment of dividends by a Guernsey company to a Guernsey resident individual (unless the company has exempt status), but are not payable in relation to the payment of dividends to non-residents, or on interest, royalties or service fees.

It would therefore be prudent to assume that any income arising from a Virtual Currency (whether in the form of a Virtual Currency or otherwise), or any income arising in the form of a Virtual Currency, will be taxable in line with Guernsey income tax provisions and valued at the appropriate spot rate on the date that the income arises, although the Guernsey Income Tax Office has not made a formal statement on the matter and may determine that another valuation method should be used.

### Corporate Income Tax

Companies incorporated in Guernsey are treated as tax-resident in Guernsey. Companies resident in Guernsey are subject to income tax on their worldwide income (although certain reliefs are available to prevent double taxation). Most companies that are tax-resident in Guernsey are taxed at a standard rate of 0%, but income arising from certain activities is taxed at 10% or 20%. This includes (but is not limited to) income arising from fund administration, investment management (except in relation to funds) and fiduciary business (each of which are taxed at the 10% rate), and income arising from regulated trading activities such as telecommunications or the importation and/or supply of gas and hydrocarbon oil in Guernsey (which are taxed at the 20% rate).

Unit trusts are treated as companies for Guernsey income tax purposes and limited partnerships and limited liability partnerships are considered tax-transparent, and so are not taxable entities in Guernsey.

There is an exemption regime available for collective investment schemes, entities beneficially owned by collective investment schemes, and entities established for the purpose of certain specified activities relating to a specific collective investment scheme. Applications for this exemption must be made annually and attract a payment of an annual fee currently fixed at £1,200. Where an exemption is granted, the entity is treated as not being resident in Guernsey for tax purposes and is not liable for Guernsey tax on non-Guernsey source income (including Guernsey bank deposit interest).

### Personal income tax

Individuals in Guernsey pay income tax at a flat rate of 20%. The personal income tax year is based on the calendar year, and income tax returns must be filed by 30 November of the year following the relevant tax year (which filing can be made electronically or on paper).

There are different classes of residence which may affect an individual's tax treatment. Individuals may be:

- "principally resident" – they are in Guernsey for 182 days or more in a tax year, or are in Guernsey for 91 days or more in a tax year and have spent 730 days or more in Guernsey over the four prior tax years;
- "solely resident" – they are in Guernsey for 91 days or more in a tax year, or are in Guernsey for 35 days or more in a tax year and have spent 365 days or more in Guernsey over the four prior tax years, and in either case have not spent 91 days or more in any other jurisdiction in the tax year; or
- "resident only" – they would be treated as solely resident in a tax year, but they have spent 91 days or more in another jurisdiction for that tax year.

Individuals who fall within the scope of any of the above will pay Guernsey tax on their worldwide income, although foreign tax relief is available. Individuals who are "resident only" can elect to pay a standard charge of £30,000, which has the effect of exempting them from Guernsey income tax on their worldwide income (they will still have to pay tax on any Guernsey-source income).

A personal allowance is available for individuals of £10,500 (although earners of more than £142,896 have their allowance reduced by £1 for every £3 exceeding this limit. Certain reliefs are available for pension contributions and mortgage interest which are beyond the scope of this chapter. A Guernsey resident individual can elect for a cap on their income tax liability in relation to their worldwide income (but not in relation to income arising on Guernsey real property).



## FATCA and CRS

Guernsey is party to an intergovernmental agreement with the United States regarding the Foreign Account Tax Compliance Act of 2009 (“FATCA”) and implemented FATCA due diligence and reporting obligations in June 2014. Under FATCA legislation in Guernsey, Guernsey “financial institutions” are obliged to carry out due diligence on account holders and report on accounts held by persons who are, or are entities that are controlled by, one or more natural persons who are, residents or citizens of the United States, unless a relevant exemption applies.

Guernsey is also a party to an intergovernmental agreement with the United Kingdom in relation to the United Kingdom’s own version of FATCA, which it also implemented in June 2014. However, the United Kingdom’s version of FATCA has now been superseded by the adoption by Guernsey (alongside numerous jurisdictions) of the much broader global Common Reporting Standard (“CRS”).

Guernsey is a party to the OECD’s Multilateral Competent Authority Agreement regarding the CRS and implemented the CRS into its domestic legislation with effect from 1 January 2016. Under CRS legislation in Guernsey, Guernsey “financial institutions” are obliged to carry out due diligence on account holders and report on accounts held by persons who are, or are entities that are controlled by, one or more natural persons who are residents of jurisdictions that have adopted the CRS, unless a relevant exemption applies.

Guernsey has implemented measures equivalent to the EU Savings Directive (“EUSD”), although these are in the process of being phased out following the repeal of the EUSD in order to make way for the CRS.

It is unclear at this stage what, if any, reporting should take place in relation to Virtual Currencies under FATCA or CRS, and much will turn on whether individual Virtual Currencies are “securities” for FATCA and CRS purposes. Until this point has been settled, it would be prudent to adopt a conservative approach.

## Money transmission laws and anti-money laundering requirements

All Guernsey individuals and firms are subject to the Drug Trafficking (Bailiwick of Guernsey) Law, 2000 (as amended), the Terrorism and Crime (Bailiwick of Guernsey) Law, 2002 (as amended) and the Disclosure (Bailiwick of Guernsey) Law, 2007. These laws contain various offences which arise should a financial service business, a non-financial service business or a nominated officer in a financial service business fail to make a disclosure to Guernsey’s Financial Intelligence Unit, the Financial Intelligence Service where they have knowledge or suspicion (or reasonable grounds for knowledge or suspicion) of money laundering or terrorist financing. It is also an offence to disclose information or any other matter which is likely to prejudice an investigation by law enforcement.

In addition, regulated entities in Guernsey are bound by various rules and regulations – in particular, Guernsey’s anti-money laundering and counter-terrorist financing legislation, including the Criminal Justice (Proceeds of Crime) (Financial Services Businesses) (Bailiwick of Guernsey) Regulations, 2008 and the Handbook for Financial Services Businesses on Countering Financial Crime and Terrorist Financing (current edition June 2017) published by the Commission (the “Handbook”).

The full scope of Guernsey’s anti-money laundering regime, counter-terrorist financing legislation and of all of the applicable laws, rules and regulations applicable to an entity regulated under the POI Law or the NRFBS Law is beyond the scope of this chapter but the key points to consider are as follows:

- a regulated entity should appoint a money laundering reporting officer (“MLRO”) resident in Guernsey;
- the board or equivalent of the entity will have effective responsibility for compliance with Guernsey’s anti-money laundering regime and counter-terrorist financing legislation and must take responsibility for the policy on reviewing compliance, consider the appropriateness and effectiveness of compliance and the review of compliance at appropriate intervals, and take appropriate measures to keep abreast of and guard against the use of technological developments and new methodologies in money laundering and terrorist financing schemes. The board may delegate some or all of its duties but must retain responsibility for the review of overall compliance with Guernsey’s anti-money laundering and counter-terrorist financing legislation requirements;
- the entity will require appropriate customer take-on policies; procedures and controls will need to be adopted to sufficiently identify and verify identity (to a depth appropriate to the assessed risk of the business relationship and occasional transaction) of all of its existing and new customers;
- all transactions and activity will need to be monitored on an ongoing basis to include all business relationships (on a risk-based approach), with high-risk relationships being subjected to an appropriate frequency of scrutiny, which must be greater than may be appropriate for low-risk relationships;
- appropriate and effective policies, procedures and controls must be established in order to facilitate compliance with the reporting requirements of the regulations; and
- appropriate employee screening and training policies will need to be in place.

The Handbook permits the use of technology for customer due diligence, and indeed as referenced above, Guernsey was one of the earliest adopters of blockchain technology in the private equity market for administration purposes. Other administrators have since adopted technologically backed systems for undertaking customer due diligence, and in particular, private equity fund administrator Ipes has set up the ID Register, an online platform for connected due diligence, FATCA and investor reporting.

### Promotion and testing

The Commission has introduced the free “Innovation SoundBox” to serve as a hub for enquiries regarding innovative financial products and services, and encourages firms or individuals to use this facility to discuss potential applications in the field of Virtual Currencies at an early stage. No fees are charged for engaging with the Innovation SoundBox.

### Ownership and licensing requirements

There are no specific restrictions in Guernsey on investment managers holding cryptocurrencies for investment purposes, and as the regulatory position is unclear, individuals should approach the Commission on a case-by-case basis to determine whether they are required to obtain a POI Licence in order to hold cryptocurrency as an investment advisor or fund manager. The above section, headed “Cryptocurrency regulation”, provides more detail on when an individual or entity is required to be licensed under the POI Law, and the section headed “Money transmission laws and anti-money laundering requirements” provides further detail about applicable anti-money laundering and counter-terrorist financing requirements.

### Mining

There are no specific restrictions on the mining of Virtual Currencies in Guernsey.

### Border restrictions and declaration

There are no specific border restrictions or declarations which must be made on the ownership of Virtual Currencies in Guernsey. However, the Cash Controls (Bailiwick of Guernsey) Law, 2007 (as amended) (the “Cash Controls Law”) does set out requirements for any person who is entering or leaving Guernsey who is carrying cash in any currency to the equivalent value of €10,000 or more to make a declaration to a Guernsey Border Agency Officer. The definition of “cash” under the Cash Controls Law is broad, including banknotes, bullion, ingots and coins (whether or not in circulation as a medium of exchange) and it is not clear whether Virtual Currencies would be caught under such a provision. Despite this, it is likely that the Cash Controls Law will not apply to the movement of Virtual Currencies, as to be caught under the Cash Controls Law the cash must be carried in baggage or on one’s person and, given the purely digital nature of many Virtual Currencies, it is unclear whether it would be conceptually possible for it to be “carried”.

### Reporting requirements

There are no specific Guernsey reporting requirements for cryptocurrency payments made in excess of a certain value. However, any transactions should be monitored to ensure that they are compliant with anti-money laundering and countering the financing of terrorism procedures.

### Estate planning and testamentary succession

At present, Virtual Currencies in Guernsey are not treated differently than any other asset on the death of the holder. In principle, therefore, if an estate is subject to Guernsey succession laws, Virtual Currencies would be treated in the same way as any other asset and distributed in accordance with the will or intestacy of the holder under Guernsey law. There may, however, be practical difficulties with both locating and distributing any Virtual Currencies which may be stored in virtual wallets or protected by other forms of security, and the means for transferring Virtual Currencies to a successor in title may largely depend on the relevant issuer or exchange.



## Authors



### David Crosland

Partner

D +44 (0)1481 741556

E [david.crosland@careyolsen.com](mailto:david.crosland@careyolsen.com)

David undertakes a wide range of corporate transactions with a particular experience in the launch of investment funds.

He is regularly instructed by fund managers, UK and international law firms and other financial services firms on the launch, administration, restructuring and listing of both closed and open-ended investment funds. David was listed in the International Who's Who of Private Funds Lawyers 2018.

In addition to fund formation, David frequently advises on corporate real estate and general corporate matters, including those with a heavy regulatory content.

David trained at Clifford Chance in London, qualifying as an English solicitor in the Private Funds Group in 2004. While there, he specialised in the establishment of institutional closed-ended investment funds particularly private equity, real estate and infrastructure funds. In 2006, he spent nine months on secondment at ABN AMRO advising on the structuring and launch of institutional fund-linked investment products, before joining Carey Olsen in May 2007. David became a partner in 2013.



### Felicity White

Associate

Admitted in England & Wales

D +44 (0)1481 741538

E [felicity.white@careyolsen.com](mailto:felicity.white@careyolsen.com)

Felicity is an associate in Carey Olsen's Guernsey corporate team. She assists on a range of corporate, commercial, banking and finance matters.

Felicity joined Carey Olsen in 2016, having trained and qualified as a solicitor in the UK. Having initially read Modern History at Merton College, Oxford, she obtained her GDL (Commendation) at City Law School, London, before completing her LPC at the University of Law in Guildford (Distinction), where she was awarded prizes in Commercial Litigation and Commercial Dispute Resolution.

Felicity is a member of the Law Society of England and Wales.

## Endnotes

1. Under the POI Law, such an administrator is referred to as a "designated manager", but in the rules governing the various classes of funds in Guernsey, such an administrator is sometimes described as a "designated administrator". For the sake of convenience, we will refer to them as an "administrator" throughout this chapter.

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*Please note that this guide is only intended to provide a very general overview of the matters to which it relates. It is not intended as legal advice and should not be relied on as such. © Carey Olsen (Guernsey) LLP 2018*

Jersey  
blockchain and  
cryptocurrency  
regulation 2019,  
first edition



# Jersey

## Introduction

Jersey's legal and regulatory framework in relation to blockchain and cryptocurrencies can be divided up into the following areas:

- investment funds;
- the regulation of managers;
- Initial Coin Offerings ("ICOs"); and
- Virtual Currency Exchanges ("VCEs").

This guide provides an overview of the regulatory framework for each of these areas.

## Investment Funds

Promoters of cryptocurrency funds can take advantage of Jersey's well established funds regulatory regime. Indeed, Jersey stole a march on its competitor jurisdictions as a crypto-friendly jurisdiction when the Island's regulator, the Jersey Financial Services Commission (the "JFSC"), approved the launch of the world's first regulated Bitcoin investment fund, GABI Plc. At the time, Bitcoin was far less well known and was regarded by the mainstream as a fringe asset class. GABI Plc's regulatory approval was regarded by many industry commentators as a statement of intent from the Island.

Cryptocurrency fund promoters typically make use of one of the following regulatory regimes to establish their investment funds:

- the Jersey Private Fund (up to 50 investors); or
- the Jersey Expert Fund (unlimited number of investors) – GABI Plc was approved as an Expert Fund.

A brief summary of each regime is set out below:

### Jersey Private Fund – key features

- Maximum of 50 investors at any time and a maximum of 50 initial offers, and must not be listed on a stock exchange.
- May be open or closed for redemptions by investors.
- Investors must qualify as "professional" investors and/or subscribe for interests with a value of at least £250,000, and sign a simple investment warning (usually included in the subscription document).
- No investment or borrowing restrictions.
- A Jersey regulated administrator must be appointed as the fund's designated service provider ("DSP") to ensure that the necessary criteria and applicable anti-money laundering legislation are complied with, to carry out due diligence on the promoter and to file an annual compliance statement.
- A non-Jersey administrator can be appointed to administer the fund (but not to act as the DSP).

- Jersey "special purpose" vehicles established to act as service providers (such as a general partner, trustee or investment manager/adviser) are generally not required to be regulated.

Due to requirements imposed on Jersey as conditions to its EU/EEA market access, additional requirements apply if the fund is actively "marketed" into the EU/EEA (as defined in the AIFMD):

### Not actively marketed into the EU/EEA

Where the fund will not be marketed into the EU/EEA:

- There is no need to prepare an offering memorandum.
- There is no need for Jersey directors or service-providers, and no audit requirement.
- The fund is not regulated by the JFSC on an ongoing basis.

### Marketed into the EU/EEA (AIFM is sub-threshold)

Funds which are to be actively "marketed" into the EU/EEA in accordance with the AIFMD and which have appointed a sub-threshold AIFM:

- For a Jersey AIFM, a simple JFSC consent is required (there is no ongoing regulation).
- Minimal requirements will apply under the Code of Practice for Alternative Investment Funds and AIF Services Business published by the JFSC.

### Marketed into the EU/EEA (AIFM is not sub-threshold)

Funds which are to be actively "marketed" into the EU/EEA in accordance with the AIFMD through national private placement regimes (or when available, through passporting):

- JFSC consent obtained in 48 hours (draft PPM to be filed with the JFSC).
- An "AIF Certificate" is needed to permit EU/EEA marketing. For the ongoing JFSC, regulation is limited to compliance with the limited applicable AIFMD provisions.
- The JFSC assesses the suitability of the fund's promoter, having regard to its track record and relevant experience, reputation, financial resources and spread of ultimate ownership, in light of the level of sophistication of the target investor group.
- Where the AIFM is a Jersey entity (such as a general partner or trustee or an external manager), it must be regulated by the JFSC, in accordance with the AIFMD.

### Jersey Expert Fund – key features

Expert Funds are attractive for non-retail schemes aimed at "Expert Investors". Expert Funds can be established quickly and cost-effectively and must comply with the Jersey Expert Fund Guide (the "EF Guide").

## JFSC approval process

The JFSC does not need to review the fund structure, documentation or the promoter. Instead the fund administrator certifies to the JFSC that the fund complies with the EF Guide and, once the certification and the fund's offer document are filed, the JFSC aims for a three-day turnaround on the application for approval. The EF Guide provides fund promoters with certainty, efficiency and cost-effectiveness in the establishment of a new fund.

## What is an Expert Fund?

The definition of "Expert Investor" is crucial. An investor must fall within any one of the 10 categories, which include a person or entity: in the business of buying or selling investments; with a net worth of more than US \$1m, excluding principal place of residence; with at least US \$1m available for investment; connected with the fund or a fund service provider (there is a flexible approach to carried-interest arrangements); or (the simplest category) making an investment or commitment of US \$100,000 or more (or currency equivalent).

The investment manager/adviser must be established in an OECD member or any other state or jurisdiction with which the JFSC has entered into a Memorandum of Understanding or equivalent; regulated in its home jurisdiction (or, if not required to be, approved by the JFSC, which usually occurs on an expedited basis); without convictions or disciplinary sanctions; solvent; and experienced in using similar investment strategies to those adopted by the Expert Fund. If the investment manager/adviser does not meet these requirements, it may approach the JFSC on a case-by-case basis. Of course, if permission is granted then, absent any material change, the investment manager/adviser will not need specific approval to establish further Expert Funds. An investment manager/adviser is not required for certain self-managed funds, such as direct real estate or feeder funds.

A small number of additional requirements are imposed on Expert Funds:

- Two Jersey-resident directors with appropriate experience must be appointed to the board of the general partner/trustee/fund company.
- A licensed Jersey administrator or manager (which may be a special purpose vehicle) must be appointed (save in the case of a unit trust, where a trustee is often the only required Jersey service provider).
- A Jersey custodian or (in the case of hedge funds) an international prime broker must be appointed for funds which are open for redemption at the option of investors.
- The offer document must set out all material information in respect of the fund.
- Investors must sign a prescribed form of investment warning (usually contained in the subscription document).
- The fund must be audited.

## Flexibility

There are no investment or borrowing restrictions imposed on the fund, nor is there any limitation on the number of investors such a fund may have.

The EF Guide aims to provide a "safe harbour" available to the majority of non-retail funds. On occasion, where derogations from the EF Guide are required, these are considered on an expedited basis.

## Ongoing requirements

Ongoing requirements are limited. Future changes to the fund generally do not require regulatory approval unless they are contrary to the EF Guide or there is a change to the fund's directors or service providers.

## AIFMD

Expert Funds are eligible to be marketed into the EU/EEA in accordance with the AIFMD through national private placement regimes (and, when available, third country passporting).

## Jersey fund managers

Subject to the requirements applicable to the fund's regulatory category, a manager/investment manager of a Jersey fund can be: (i) an entity with proper physical presence in Jersey; or (ii) a "special purpose" Jersey vehicle.

## AIFMD

Jersey entities which act as the manager of a fund (the "AIFM" as defined in the AIFMD) are subject to regulation by the JFSC.

- Managers which are already regulated (such as those acting for Expert Funds) need only comply with the applicable requirements of the AIFMD.
- For other managers (such as Jersey "special purpose" companies established to act for Jersey Private Funds):
  - a "light touch" approach applies where the AIFM will qualify as a "sub-threshold" manager (by reference to value of the funds under management);
  - otherwise, the usual 10-day application process applies, including prior submission of personal questionnaires (see paragraph headed, "Establishing a special purpose vehicle manager").

## Manager of a Jersey Private Fund

Subject to any AIFMD related requirements (see "AIFMD" in this section, above), managers which are special purpose companies established in Jersey are usually exempt from regulation using an applicable exemption, for example:

- for services between "connected companies";
- an exemption for trustees and general partners; or

- where the fund is a “professional investor regulated scheme”, which requires only that the investor sign a simple specified form of investment warning and either: (i) qualify as a “professional investor” (which includes “a person whose ordinary activities involve the person in acquiring, holding, managing or disposing of investments (as principal or agent) for the purposes of the person’s business or who it is reasonable to expect will acquire, hold, arrange or dispose of investments (as principal or agent) for the purposes of that business”); or (ii) make a minimum investment of £250,000 or currency equivalent.

Please note that a regulated “designated service provider”(i.e. Jersey administrator) will also be needed.

### Establishing a special purpose vehicle manager

Where a special purpose Jersey entity needs to be regulated as described above (for example, where acting for an Expert Fund or acting as an AIFM which is not “sub-threshold”), a simplified licensing regime applies:

- The entity is administered by a regulated Jersey administrator, which assumes responsibility for ongoing regulatory compliance and often provides one or more directors.
- Minimum capital requirement is usually £25,000 (or £10,000 where acting only for one or more related Expert Funds, other than for AIFMs where £125,000 is required (increasing where assets under management exceed £250,000)).
- Each director of the entity (and each of its beneficial owners with a 10% or greater interest) is required to be approved by the JFSC. As international regulatory checks often take three weeks or more to complete for individuals who have not already been approved by the JFSC, these should be completed and submitted as early as possible.
- The JFSC licensing process for a manager to an Expert Fund under the Financial Services law typically takes two weeks.

### Initial Coin Offerings

There has been an explosion in the number of ICOs in the last year. Founded principally on the Ethereum blockchain, the use of the “smart contract” allows an ICO promoter to mint his own coin or token in exchange for Ether subscriptions. Tokens can be “utility” in nature, allowing the holder access to new software or to a particular platform, or they may give the holder certain economic rights. In essence, ICOs are cryptographic crowdfunding, and regulators are understandably nervous because they do not conform to traditional ways of raising capital, around which the word’s capital markets and securities regulations have been crafted.

All jurisdictions have scrambled to get up to speed with ICOs, with varying degrees of risk appetite. While some regulators have prohibited ICOs entirely and others have given carte blanche to almost any ICO promoter, the JFSC has sensibly recognised that there is a middle ground; ICOs are here to stay and those ICOs with proper substance, and which are backed by a credible promoter, should be nurtured.

Against this backdrop, Carey Olsen advised on launch of Jersey’s first ICO in December 2017, ARC Reserve Currency. ARC is an asset-backed “stablecoin” crypto-currency which is designed to act like a currency without the volatility spikes one sees in other cryptocurrencies such as Bitcoin. Against a very tight timeline, and with other competitor coins about to be launched, Carey Olsen worked closely with the JFSC to ensure that the ARC coin launched ahead of time and with a degree of regulatory scrutiny which should give prospective purchasers a degree of comfort that is not available in other jurisdictions. Very recently, Carey Olsen built on its ICO expertise by advising on AX1 token, an ICO designed to raise capital for investment in a crypto-currency mining operation based in the UK.

In both instances, the JFSC adopted a purposive and pragmatic approach to approving the ICOs, focusing on consumer protection and anti-money laundering and having regard to the fact that ICO promoters want to use a Jersey-incorporated issuer because of Jersey’s reputation as a well-regulated and reputable jurisdiction.

In order to give prospective ICO investors a degree of disclosure and comfort that may not be available in many other jurisdictions – and being mindful of the guiding principle pursuant to which the JFSC discharges its functions as the Island’s financial services regulator – the JFSC sets out certain requirements on an ICO issuer.

### JFSC requirements on a Jersey ICO issuer

The ICO issuer is required to:

- be a Jersey company;
- receive consent from the JFSC before it undertakes any form of activity (see “Application process”, below);
- comply with the JFSC’s Sound Business Practice Policy (see below);
- apply relevant AML/CFT requirements to either purchase tokens from or sell tokens back to the issuer;
- appoint a Jersey-licensed administrator;
- appoint and maintain a Jersey-resident director on the board;
- be subject to an ongoing annual audit requirement;

- have procedures and processes in place to (i) mitigate and manage the risk of retail investors investing inappropriately in the ICO, and (ii) ensure retail investors understand the risks involved;
- prepare an information memorandum which complies with certain content requirements required under Jersey company law; and
- ensure that any marketing material is clear, fair and not misleading, and include in any such materials certain prescribed consumer warnings.

### Security vs. non-security tokens

Before the issuer can undertake any activity, it requires a consent from the JFSC under the Island's statutory instrument governing the raising of capital, the Control of Borrowing (Jersey) Order 1958 ("COBO"). The type of COBO consent granted by the JFSC will depend on whether the token is categorised as a "security" under COBO.

While there is no precise definition of what constitutes a "security" under COBO, the Guidance Note stipulates that a token which has one or more of the following characteristics will be regarded by the JFSC as a "security":

- a right to participate in the profits/earnings of the issuer or a related entity;
- a claim on the issuer or a related party's assets;
- a general commitment from the issuer to redeem tokens in the future;
- a right to participate in the operation or management of the issuer or a related party; and
- an expectation of a return on the amount paid for the tokens.

Importantly and helpfully, there is an express statement in the Guidance Note that the JFSC will not treat a utility token (i.e. a token conferring a usage right and with no economic or voting rights) as a security token solely by reason of the fact that it might be traded in the secondary market (e.g. listed on the cryptocurrency exchange).

Whether or not a token is a "security" under COBO makes no difference as to the requirements imposed on an issuer by the JFSC.

### Application process

Application for the issuer's COBO consent is to be accompanied by analysis prepared by the issuer's legal advisers outlining:

- the proposed activity including relevant timelines;
- details of the issuer and the ICO;

- rationale for the ICO, amount to be raised and use of proceeds;
- a summary of the features of the tokens;
- a summary of the token purchase and redemption processes;
- the service providers to the issuer;
- the relationship between issuer and holder of tokens;
- the management of underlying assets and security rights over such assets (if any) for holders of the tokens;
- how the activity will be wound up/dissolved and assets (if any) distributed to the holders of the tokens; and
- a Jersey legal and regulatory analysis, including consideration of relevant legislation or other regulatory laws (for example, whether the ICO is a "collective investment fund" under Jersey law).

Following grant of the COBO consent, the issuer must seek the prior consent of the JFSC to any material change to the matters contained in the application.

### JFSC's Sound Business Practice Policy

The Guidance Note makes clear that an ICO is 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, such as 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.

### Ongoing requirements imposed on the issuer

- The JFSC's prior consent is required for any change of Jersey administrator or Jersey-resident director.
- The board of the issuer is required to advise the JFSC promptly if the issuer defaults on any token issued.
- The directors of the issuer are required to make an annual confirmation to the JFSC (at the same time as the normal company annual return) that, to the best of their knowledge and belief, there have been no breaches of the conditions set out on the issuer's COBO consent.





## Virtual Currency Exchanges

At a very early stage, the JFSC saw that the volume and value of trading in crypto-currencies was increasing hugely, as people sought to convert their crypto into real-world 'fiat' currency and vice versa. Recognising that there was a regulatory gap, the JFSC brought those enterprises that provide so-called VCE services under Jersey's regulatory umbrella way back in 2016, requiring VCEs to comply with Jersey law and regulation aimed at preventing and detecting money laundering and terrorist financing.

The Proceeds of Crime (Miscellaneous Amendments) (Jersey) Regulations 2016 (the "Regulations") require VCEs to comply with the Island's laws, regulations, policies and procedures aimed at preventing and detecting money laundering and terrorist financing.

The Regulations also make virtual currency exchange a supervised business and require VCEs to register with and be subject to the supervision of the JFSC.

At the same time, the JFSC recognised that many promoters of VCEs need time to road-test their product without being burdened by the full weight of regulatory compliance. The JFSC therefore allowed VCEs with turnover of less than £150,000 per calendar year to test VCE delivery mechanisms in a live environment without the normal registration requirements and associated costs.

As such, Jersey's VCE regulation balances the need to provide robust regulation with a desire to foster the development of the Island's burgeoning crypto-credentials.

## Author



### Christopher Griffin

Partner

D +44 (0)1534 822256

E [christopher.griffin@careyolsen.com](mailto:christopher.griffin@careyolsen.com)

Christopher has broad experience of both general international corporate and funds work with particular expertise in private equity and hedge funds, having spent ten years in the City at Ashurst, RAB Capital plc and most recently at S J Berwin.

Christopher spearheads Carey Olsen's crypto practice, advising on the launch in 2017 of Coinshares Fund I (a venture cap fund investing in crypto assets) and ARC Reserve Currency, Jersey's first initial coin offering or "ICO". Christopher also advises on all aspects of fund and corporate transactions, including the legal and regulatory aspects of fund launches, and joint ventures. He also has considerable experience in dealing with the Jersey Financial Services Commission in navigating investment vehicles through the Jersey regulatory approval process.

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*Please note that this guide is only intended to provide a very general overview of the matters to which it relates. It is not intended as legal advice and should not be relied on as such. © Carey Olsen 2018*



## Our offices

### Jurisdictions

#### Bermuda

Carey Olsen Bermuda  
2nd Floor  
Atlantic House  
11 Par-la-Ville Road  
Hamilton HM11  
Bermuda

T +1 441 542 4500  
E [bermuda@careyolsen.com](mailto:bermuda@careyolsen.com)

#### British Virgin Islands

Carey Olsen  
Rodus Building  
PO Box 3093  
Road Town  
Tortola VG1110  
British Virgin Islands

T +1 284 394 4030  
E [bvi@careyolsen.com](mailto:bvi@careyolsen.com)

#### Cayman Islands

Carey Olsen  
PO Box 10008  
Willow House  
Cricket Square  
Grand Cayman KY1-1001  
Cayman Islands

T +1 345 749 2000  
E [cayman@careyolsen.com](mailto:cayman@careyolsen.com)

#### Guernsey

Carey Olsen (Guernsey) LLP  
PO Box 98  
Carey House  
Les Banques  
St Peter Port  
Guernsey GY1 4BZ  
Channel Islands

T +44 (0)1481 727272  
E [guernsey@careyolsen.com](mailto:guernsey@careyolsen.com)

#### Jersey

Carey Olsen  
47 Esplanade  
St Helier  
Jersey JE1 0BD  
Channel Islands

T +44 (0)1534 888900  
E [jerseyco@careyolsen.com](mailto:jerseyco@careyolsen.com)

### International offices

#### Cape Town

Carey Olsen  
Protea Place  
40 Dreyer Street  
Claremont  
Cape Town 7708  
South Africa

T +27 21 286 0026  
E [capetown@careyolsen.com](mailto:capetown@careyolsen.com)

#### Hong Kong

Carey Olsen (Hong Kong) LLP  
Suite 4120  
Jardine House  
1 Connaught Place  
Hong Kong

T +852 3628 9000  
E [hongkong@careyolsen.com](mailto:hongkong@careyolsen.com)

#### London

Carey Olsen LLP  
8-10 Throgmorton Avenue  
London EC2N 2DL  
United Kingdom

T +44 (0)20 7614 5610  
E [londonco@careyolsen.com](mailto:londonco@careyolsen.com)

#### Singapore

Carey Olsen Singapore LLP  
10 Collyer Quay #24-08  
Ocean Financial Centre  
Singapore 049315

T +65 6911 8310  
E [singapore@careyolsen.com](mailto:singapore@careyolsen.com)

OFFSHORE LAW SPECIALISTS

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BERMUDA BRITISH VIRGIN ISLANDS CAYMAN ISLANDS GUERNSEY JERSEY  
CAPE TOWN HONG KONG LONDON SINGAPORE

[careyolsen.com](https://www.careyolsen.com)