



Jersey  
blockchain and  
cryptocurrency  
regulation 2019,  
first edition

**CAREY OLSEN**

## 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.

*Originally published in conjunction with Global Legal Insights.*

*Contributing editor Josias Dewey.*

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## 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 Jersey LLP  
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

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