

Cayman Islands Virtual Assets Framework

The Cayman Islands Government has announced that the Virtual Asset (Service Providers) Law, 2020 (the “**VASP Law**”) will come into force in two phases.

Phase one, commencing on 31 October 2020, will focus on anti-money laundering (AML) and countering the financing of terrorism (CFT) compliance, supervision and enforcement.

Phase two, which will include licensing requirements and prudential supervision, is expected to come into force in June 2021.

Phase One

Entities engaged in or wishing to engage in virtual asset services (“**VASPs**”) must now register with the Cayman Islands Monetary Authority (“**CIMA**”) under the VASP Law. VASPs that are currently subject to CIMA’s supervision under another regulatory law must notify CIMA (in the case of licensees) or register with CIMA (in the case of registrants) under the VASP Law.

Provisions of the VASP Law which relate to enforcement, penalties and offences will commence on 31 January 2021. Entities engaging in virtual asset services that have not registered with or notified CIMA by the applicable deadline (set out below) will be subject to penalties and other enforcement measures.

An application for registration or a notification being made under phase one will need to be submitted via CIMA’s Regulatory Enhanced Electronic Forms Submission (“**REEFS**”) online platform using the ‘VASP Application Form’ (together with a non-refundable assessment fee of CI\$1,000 (US\$1,220)). The ‘VASP Application Form’ requests, amongst other things, details of the nature of the entity’s virtual asset service(s), the entity’s Anti-Money Laundering Compliance Officer, Money Laundering Reporting Officer and Deputy Money Laundering Reporting Officer, the entity’s revenue for the prior 12 months (or if unavailable, projected revenue for the 12 months following the application), the entity’s AML/CFT/CPF procedures and the entity’s internal safeguards and data protection systems to protect the assets and data of clients.

As part of the registration or notification process, entities will also be required to complete an ‘AML/CFT Form’ which will need to be submitted through CIMA’s REEFS online portal.

If an application for registration is successful, the applicant will be required to pay an application fee of between CI\$1,000 (US\$1,220) and CI\$15,000 (US\$18,293) (the fee amount will depend on various prescribed factors).

An annual renewal fee equal to the relevant application fee will also be payable.

Phase Two

Phase two will bring into force the remaining provisions of the VASP Law, including the licensing requirement for virtual asset custodians and trading platform operators, and the sandbox licensing regime.

Entities engaged in virtual asset custodial services, or the operation of virtual asset trading platforms, are required to register in phase one. These entities will then need to apply for a licence once phase two commences.

Timing

If an entity provided virtual asset services prior to 31 October 2020, and continues to provide such services, it is permitted to do so provided it registers with or notifies CIMA (as applicable) pursuant to the VASP Law by 31 January 2021. CIMA has advised that, in order to ensure registrations are completed on or before 31 January 2021, applicants are encouraged to apply by 12 December 2020.

An entity planning to start providing virtual asset services after 31 October 2020 must register with or notify CIMA (as applicable) before it starts providing such services.

Future Developments

CIMA will issue a Statement of Principles for entities providing virtual asset services in due course, in order to provide a broad framework and guidance for the conduct of virtual asset activities in or from the Cayman Islands.

CIMA has also indicated that it proposes to issue rules, procedures and guidance tailored to each VASP entity type in the future.

Overview of the VASP Law

The VASP Law incorporates relevant anti-money laundering, countering the financing of terrorism and counter proliferation financing recommendations adopted in 2019 by the Financial Action Task Force and provides for the registration or licensing (as applicable) of businesses providing virtual asset services.

A high-level summary of some of the key provisions in the VASP Law is set out below.

Virtual Assets and Virtual Asset Service Providers

A virtual asset is defined as a digital representation of value that can be digitally traded or transferred and can be used for payment or investment purposes but does not include a digital representation of fiat currencies.

A VASP is (a) an entity that issues virtual assets; or (b) an entity that provides as a business or in the course of business in or from within the Cayman Islands one or more of the following services or operations for or on behalf of a natural or legal person or legal arrangement:

1. the exchange between virtual assets and fiat currencies;
2. the exchange between one or more other forms of convertible virtual assets;
3. the transfer of virtual assets;
4. the virtual assets custodian services;
5. the participation in and the provision of financial services related to the issuance or the sale of a virtual asset.

A virtual service token is not deemed to be a virtual asset for the purposes of the VASP law and accordingly an entity that provides services that involve virtual service tokens only is not required to be licensed or registered under the VASP Law. A virtual service token is a digital representation of value which is not transferrable or exchangeable with a third party at any time and includes digital tokens whose sole function is to provide access to an application or service or to provide a service or function directly to its owner.

Issuance of Virtual Assets

The “issuance of virtual assets” means the sale of newly created virtual assets to the public in or from within the Cayman Islands in exchange for fiat currency, other virtual assets or other consideration but does not include the sale of virtual service tokens. An entity that wishes to issue virtual assets in or from within the Cayman Islands must register with CIMA before conducting such issuance. The entity must also submit to CIMA a request (containing such information as may be specified by CIMA) seeking the approval of CIMA in advance of the proposed virtual asset issuance.

Should an entity wish to issue virtual assets to the public in excess of the prescribed threshold, it must engage one or more licensed virtual asset trading platforms to undertake the issuance. Before undertaking such an issuance, the issuer must also obtain CIMA’s prior approval.

Virtual Asset Custody Services

A “virtual asset custodian” is a licensee who provides virtual asset custody services in or from within the Cayman Islands.

A “virtual asset custody service” is the business of safekeeping or administration of virtual assets or the instruments that enable the holder to exercise control over virtual assets.

Entities providing virtual asset custody services are required to register with CIMA in phase one and must apply for a licence when phase two commences.

Virtual Asset Trading Platforms

A “virtual asset trading platform” means a centralised or decentralised digital platform:

1. which facilitates the exchange of virtual assets for fiat currency or other virtual assets on behalf of third parties for a fee, commission, spread or other benefit; and
2. which:

- holds custody of or controls virtual assets on behalf of its clients to facilitate an exchange; or
- purchases virtual assets from a seller when transactions or bids and offers are matched in order to sell them to a buyer,

and includes its owner or operator, but does not include a platform that only provides a forum where sellers and buyers may post bids and offers, and a forum where the parties trade in a separate platform or in a peer-to-peer manner.

Entities engaged in the operation of virtual asset trading platforms are required to register with CIMA in phase one and must apply for a licence when phase two commences.

Sandbox Licensees

The VASP Law creates a new regulatory sandbox in the Cayman Islands. A sandbox licence is a temporary licence granted for a period of up to one year to businesses which CIMA determines utilise innovative technologies or an innovative method of delivery. Where CIMA grants a sandbox licence it may, amongst other things, impose any restrictions that it considers necessary to effectively supervise, monitor and assess the relevant virtual asset service or fintech service, exempt the sandbox licensee from requirements that are applicable to VASPs or modify any such requirement in such manner as CIMA considers appropriate.

The introduction of the new regulatory sandbox is expected to form part of phase two.

Key Ongoing Requirements

A VASP is required, amongst other things, to:

- prepare accounts annually and make the accounts available for inspection upon request by CIMA;
- comply with the Anti-Money Laundering Regulations (as revised) (the “**AML Regulations**”) and other Cayman Islands laws relating to the combating of money laundering, terrorist financing and proliferation financing;
- put in place anti-money laundering systems and procedures for the purpose of complying with the AML Regulations;
- designate an employee as the officer with responsibility for the procedures for combating money laundering, terrorist financing and proliferation financing;
- obtain the prior approval of CIMA in respect of the appointment of any senior officer or trustee or an anti-money laundering compliance officer;
- ensure that its senior officers and trustees are fit and proper persons to hold the respective positions;
- ensure that its beneficial owners are fit and proper persons to have such control or ownership;
- obtain the prior approval of CIMA in respect of the issue or transfer of shares or interests (as applicable) totalling 10% or more of a company or partnership (as applicable) that is a VASP;
- take the necessary steps to protect and secure the personal data and virtual assets of its clients;
- ensure all communications relating to the virtual assets service are accurate; and

- have a registered office in the Cayman Islands.

CIMA may, at the VASP's expense, require a virtual asset service provider to provide an auditor's report, prepared by an independent auditor, on the anti-money laundering systems and procedures for compliance with the AML Regulations.

Additional requirements will apply to a licensee that provides virtual asset custody services or operates a virtual asset trading platform when the relevant sections of the VASP Law come into effect as part of phase two.



Richard Spencer

Partner

+1 345 914 5835

rspencer@campbellslegal.com



Aoife Tuohy

Associate

+1 345 914 5821

atuohy@campbellslegal.com