



Loeb Smith

British Virgin Islands | Cayman Islands | Hong Kong

Legal Insights

Cryptoasset trading in Cayman Islands

Fiat currency transactions

What rules and restrictions govern the exchange of fiat currency and cryptoassets?

Assuming the subject cryptoassets fall within the definition of virtual assets under the Virtual Asset (Service Providers) Act (As Revised) (VASP Act), the exchange of fiat currency and cryptoassets will likely constitute a virtual asset service under the VASP Act and hence any person providing the service of exchange of fiat currency and cryptoassets in the course of their business will be a virtual asset service provider regulated by the VASP Act.

Furthermore, if the exchange of fiat currency and cryptoassets falls within one of the relevant financial businesses under the Proceeds of Crime Act, the relevant service provider will be required to comply with the AML and KYC requirements under the AML Regulations, which include, among other things, implementing client identification and verification, record-keeping, and internal reporting and control procedures.

Exchanges and secondary markets

Where are investors allowed to trade cryptoassets? How are exchanges, alternative trading systems and secondary markets for cryptoassets regulated?

There are generally no legal requirements or restrictions on where investors are allowed to trade cryptoassets in the Cayman Islands, so investors are usually free to trade cryptoassets wherever they desire.

Assuming the subject cryptoassets that are traded on the exchanges, alternative trading systems and secondary markets qualify as virtual assets under the VASP Act, such exchanges, alternative trading systems and secondary markets will have to apply for a licence with the Cayman Islands Monetary Authority (CIMA) if either of them qualifies as a virtual asset trading platform under the VASP Act, which is defined as: *a centralised or decentralised digital platform — (a) 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 (b) which — (i) holds custody of or controls virtual assets on behalf of its clients to facilitate an exchange; or (ii) 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.*

If the exchanges, alternative trading systems or secondary markets are licensed with CIMA as virtual asset trading platforms, each of them would be subject to various restrictions and obligations stipulated, among other things, under section 11 of the VASP Act, such as being restricted from providing financing to its clients for the purchase of virtual assets unless disclosures are made to clients regarding the terms of, and the risk of, the financing, and being obligated to carry out reasonable due diligence procedures on virtual assets and their issuers that are listed on the platform.

Alternatively, the exchanges, alternative trading systems and secondary markets for cryptoassets may otherwise have to be registered or licensed with CIMA if its business activity constitutes any virtual asset service under the VASP Act.

At the same time, the exchanges, alternative trading systems and secondary markets for cryptoassets may be regulated by the Securities Investment Business Act (SIBA) if the subject cryptoassets fall within the definition of securities under the SIBA, and if they are engaged in certain securities investment business, which would mandate the registration or licensing with CIMA.

Furthermore, if the business of exchanges, alternative trading systems and secondary markets for cryptoassets falls within one of the relevant financial businesses under the Proceeds of Crime Act, they will be required to comply with the AML and KYC requirements under the AML Regulations, which include, among other things, implementing client identification and verification, record-keeping, and internal reporting and control procedures.

Custody

How are cryptoasset custodians regulated?

Assuming the cryptoassets that are the subject of the custody service of the relevant cryptoasset custodians qualify as virtual assets under the VASP Act, such custodians will have to apply for a licence with CIMA if either of them provides virtual asset custody service under the VASP Act, which is defined as ‘the business of safekeeping or administration of virtual assets or the instruments that enable the holder to exercise control over virtual assets’. If the custodians are licensed with CIMA to provide virtual asset custody service, each of them would be subject to various restrictions and obligations stipulated, inter alia, under section 10 of the VASP Act, such as being obligated to:

- maintain best technology practices relating to virtual assets held in custody;
- not encumber or cause any virtual asset to be encumbered, unless specifically agreed to by the beneficial owners of the virtual assets;
- ensure that all proceeds relating to virtual assets held in custody shall accrue for the benefit of the owner, unless otherwise agreed in writing;
- take such steps as may be necessary to safeguard the virtual assets held;
- have adequate safeguards against theft and loss; and
- enter into a custodial arrangement with the owner of a virtual asset, which includes the prescribed details set out in the VASP Act.

Furthermore, if the business of such cryptoasset custodians falls within one of the ‘relevant financial businesses’ under the Proceeds of Crime Act, they will be required to comply with the AML and KYC requirements under the AML Regulations, which include, among other things, implementing client identification and verification, record-keeping and internal reporting and control procedures.

Broker-dealers

How are cryptoasset broker-dealers regulated?

Assuming the broker-dealer business of the relevant cryptoasset broker-dealers involves cryptoassets that qualify as virtual assets under the VASP Act, it is likely that such broker-dealers will have to be registered with CIMA and be regulated accordingly because such broker-dealer business typically involves either one or a combination of the following virtual asset services: transfer of virtual assets, virtual asset custody service, or participation in and provision of financial services related to a virtual asset issuance or the sale of a virtual asset.

At the same time, the cryptoasset broker-dealers may be regulated by the SIBA if the subject cryptoassets fall within the definition of securities under the SIBA, and if they are engaged in certain securities investment business (which would be likely in terms of dealing in securities and/or arranging deals in securities), which would mandate the registration or licensing with CIMA.

Furthermore, if the business of such cryptoasset broker-dealers falls within one of the relevant financial businesses under the Proceeds of Crime Act, they will be required to comply with the AML and KYC requirements under the AML Regulations, which include, among other things, implementing client identification and verification, record-keeping and internal reporting and control procedures.

Decentralised exchanges

What is the legal status of decentralised cryptoasset exchanges?

Since the definition of 'virtual asset trading platform' under the VASP Act also covers those trading platforms with a decentralised nature, certain pieces of legislation and regulations, such as the VASP Act, the SIBA and the AML Regulations, may similarly apply to decentralised cryptoasset exchanges so long as the subject cryptoasset and business activities fall within the corresponding scopes.

Peer-to-peer exchanges

What is the legal status of peer-to-peer (person-to-person) transfers of cryptoassets?

Assuming the cryptoassets that are the subject of the peer-to-peer transfers qualify as virtual assets under the VASP Act, if such peer-to-peer transfers are conducted in the course of the relevant party's business, such peer-to-peer transfers may constitute a virtual asset service with respect to transfer of virtual assets under the VASP Act, which renders the need to be registered with CIMA.

Similarly, a party of peer-to-peer transfers of cryptoassets may be regulated by the SIBA if the subject cryptoassets fall within the definition of securities under the SIBA, and if that party is engaged in certain 'securities investment business' (which would be likely in terms of dealing in securities), which would mandate the registration or licensing with CIMA.

Furthermore, if such peer-to-peer transfers fall within one of the relevant financial businesses under the Proceeds of Crime Act, the relevant party will be required to comply with the AML and KYC requirements under the AML Regulations, which include, among other things, implementing client identification and verification, record-keeping, and internal reporting and control procedures.

Trading with anonymous parties

Does the law permit trading cryptoassets with anonymous parties?

In general, there are no legal restrictions on trading cryptoassets with anonymous parties, unless such trades are considered to be conducted in the course of business of the relevant party and the relevant party is considered to be providing the services of transfer of virtual asset under the VASP Act, and/or carrying out the relevant financial business under the AML Regulations, in which the relevant party will then be subject to certain due diligence requirements of the transaction parties and/or customers, hence making it difficult for a party to keep itself anonymous.

Foreign exchanges

Are foreign cryptocurrency exchanges subject to your jurisdiction's laws and regulations governing cryptoasset exchanges?

In general, the location of domicile of a foreign cryptocurrency exchange does not affect whether Cayman Islands' laws and regulations may govern such exchange.

For the VASP Act, what matters is whether any virtual asset service is provided in or from within the Cayman Islands in the course of business, the affirmation of which will render the foreign cryptocurrency exchange to register or be licensed with CIMA.

In addition, the SIBA also does not differentiate between the treatment for varying locations of domicile of a foreign cryptocurrency, and what matters is the actual business activity conducted by the relevant exchanges and whether it is being conducted in or from within the Cayman Islands.

Under what circumstances may a citizen of your jurisdiction lawfully exchange cryptoassets on a foreign exchange?

From the perspective of Cayman Islands laws, there is generally no legal restriction or requirement on how a citizen of the Cayman Islands is required to exchange cryptoassets on a foreign exchange.

Do any tax liabilities arise in the exchange of cryptoassets (for both other cryptoassets and fiat currencies)?

There is generally no Cayman Islands tax liability for the exchange of cryptoassets.

This publication is not intended to be a substitute for specific legal advice or a legal opinion. For specific legal advice on the subject matter of this Briefing, please contact your usual Loeb Smith attorney or any of the following:

E: gary.smith@loebsmith.com

E: robert.farrell@loebsmith.com

E: elizabeth.kenny@loebsmith.com

E: vanisha.harjani@loebsmith.com

E: kate.sun@loebsmith.com

E: vivian.huang@loebsmith.com

E: faye.huang@loebsmith.com

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Loeb Smith is a leading offshore corporate law firm, with offices in the British Virgin Islands, the Cayman Islands, and Hong Kong, whose Attorneys have an outstanding record of advising on the Cayman Islands' law aspects and BVI law aspects of international corporate, investment, and finance transactions. Our team delivers high quality Partner-led professional legal services at competitive rates and has an excellent track record of advising investment fund managers, in-house counsels, financial institutions, onshore counsels, banks, companies, and private clients to find successful outcomes and solutions to their day-to-day issues and complex, strategic matters



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