

Cayman Islands Hedge Fund Services 2018



Regulatory updates maintain robust growth in funds

Focus on creating innovative fintech framework

Go-to jurisdiction for budding crypto currency funds

Cryptocurrency and blockchain technology in the Cayman Islands

By Chris Humphries

Blockchain technology offers an exciting, unprecedented and innovative opportunity for the Cayman Islands investment funds industry. Whilst cryptocurrencies (such as Bitcoin) have been around for a number of years, we are now seeing a surge of activity in this area. Funds are being established in the Cayman Islands which will focus entirely on blockchain and cryptocurrency strategies. In addition, funds are seeking to innovate by accepting cryptocurrencies as a payment mechanism for subscription proceeds.

We expect smart contracts (discussed below) to become more mainstream in connection with subscriptions into and redemption out of funds. Such technology would enable investors to set parameters for those transactions without needing to take specific additional action each time they requested such a transaction to take place.

Cayman Islands vehicles are also used to execute initial coin/token offerings (ICOs). Where an ICO is structured through the Cayman Islands, the vehicle of choice seems to be a Cayman Islands exempted company. However, following the enactment of the new foundation company regime in the Cayman Islands, we expect to see these structures being increasingly used too.

It is, of course, an ever-changing and fast-paced market and we expect funds to continue to adopt smart contracts and cryptocurrencies in order for the funds to remain competitive and attractive to potential investors.

Smart contracts

Aside from the obvious potential for value creation, perhaps the most interesting application of blockchain technology for the



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legal market is the ability to generate "smart contracts". In the context of cryptocurrencies and blockchain, smart contracts are self-executing software programmes running on blockchain databases that enable transactions to be executed based on specific rules or triggers.

Once encoded onto the blockchain, a smart contract can then be definitive in the sense that, if one party performs their end of the bargain, the other contracting party's performance is automatic and guaranteed. The lack of human interaction required in executing the terms of the smart contract therefore limits the ability for error or disputes to arise. However, this automation also means that ensuring the contractual terms are accurate in the first instance is of vital importance.

Transparency

Blockchain technology is a decentralised digital ledger in which transactions made in Bitcoin or another cryptocurrency are recorded chronologically and publicly.

The blockchain operates in a similar way to a spreadsheet and is a shared and continually reconciled database. When a transaction occurs and is verified by the network, the ledger records one fixed and highly secure copy of the transaction that all users are able to see at the same time.

The funds industry is now looking at blockchain technology as a way to provide a fast, streamlined method of communicating with investors or recording and transferring shares or other securities.

Blockchain technology could offer a higher level of transparency because the distributed ledger reflects the real-time ownership and



movement of a company's shares or other securities. The blockchain system could therefore be used to quickly distribute a share dividend and to correct the Register of Members of a fund contemporaneously with the underlying transactions.

Is hacking a real concern?

If someone wanted to hack into a particular block in a blockchain, a hacker would not only need to hack into that specific block, but all of the proceeding blocks going back the entire history of that blockchain. In addition, the hacker would need to make the same change on every ledger in the network (numbering in the millions) simultaneously. Blockchain technology is therefore far less susceptible to hacking attacks than existing, centralised databases such as those used by intermediaries and banks.

Cayman's involvement in cryptocurrencies

Cayman's existing legal framework provides the flexibility to allow technologies like blockchain to flourish. As the leading offshore jurisdiction for the establishment of

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Blockchain raises a wide range of legal issues including data protection, document retention, changes to participants and service providers once a blockchain is launched and verification of source of funds. Legal advice will also be critical to the process of development and launch of blockchain products, including smart contracts. ■

Stuarts Walker Hersant Humphries has an Investment Funds Team focusing on investments using cryptocurrencies. Our team is a market leader in advising managers on the set-up and establishment of a broad range of investment funds in the Cayman Islands.

World class responsiveness in offshore legal advice



We provide timely, exceptional legal advice and representation to our clients in connection with their commercial transactions, structures, liabilities and obligations in the Cayman Islands.



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