

# Guidance Note

## Cayman Structures for Web 3.0 Entities

### Introduction

Despite most legislation relevant to the financial services in the Cayman Islands being written before the Blockchain revolution began, the Cayman Islands has made a number of legal and regulatory advancements to make it a jurisdiction in which such innovation can thrive.

This article examines the common structures used for Web 3.0 entities seen in the current marketplace including: Token Offerings, Platform Controlling Entities, DAO's, Special Economic Zone Companies, DeFi's, IP Holding Companies, and Exchanges; and refers to the Virtual Asset (Service Providers) Act (as Revised) (the "VASP Act") and to the Economic Substance regime established by the International Tax Co-operation (Economic Substance) Act (as Revised) (the "ES Act"). For more detailed information on the VASP Act and the ES Act, the following additional articles can be viewed: [VASP Registration and Continuing Obligations](#), [Registration of Virtual Asset Service Providers](#), and [Updated Guidelines on Economic Substance](#).

### Token Offerings

A token issuer can be set up as a standalone entity to issue tokens or NFT's (the "Token Issuer") or more commonly as a subsidiary of a second entity that develops the platform or protocol (the "Developer") and in this way much of the regulatory liability of the Token Issuer is separated from the value built up in the Developer entity. Many Web 3.0 businesses choose an exempted limited company as the tax neutral vehicle to be the Token Issuer but for the Developer there are a number of choices:

- An exempted limited company can be used for the Developer;
- A Cayman Islands [Special Economic Zone \(SEZ\) company \("SEZC"\)](#) can be used, being a form of exempted limited company established within the Cayman Islands Special Economic Zone (SEZ) and which enjoy several special benefits due to that status;
- A Cayman Islands **foundation company** can be used for the Developer (please see the section titled "Decentralised Autonomous Organisations" for further information); and
- If the Developer or platform entity has already been formed in a jurisdiction outside the Cayman Islands then that company may be used.

Where a dual-entity structure is used, careful consideration should be given to the documentation of the commercial relationship between the entities. Licensing agreements, development agreements, service agreements or other commercial agreements are crucial as they ensure that it is clear – to investors, regulators, and other interested parties – what role each entity is undertaking within the structure.

For example, under the VASP Act a "virtual asset" is defined as a digital representation of value that can be digitally traded or transferred and used for payment or investment purposes but does not include digital representations of fiat currencies. The Token Issuer will be required to register with the Cayman Islands Monetary Authority ("CIMA") under the VASP Act, but would not require a phase 2 license, careful agreements need to be drafted to ensure that the Developer is not also caught by the registration requirements of the VASP Act.



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## Platform Controlling Entities

An entity that controls a platform that only provides a forum where sellers and buyers may post bids and offers or, a forum where the parties trade in a separate platform or in a peer-to-peer manner will be exempted from the requirement to obtain a license from the CIMA under the VASP Act. This kind of platform controlling entity could be formed using any one of the previously described legal forms, but most commonly would use an exempted limited company.

## Decentralised Autonomous Organisations (“DAO”)

Combining the limited liability protections of a corporate entity with the flexibility of a trust, the **Cayman foundation company** provides Web 3.0 DAO projects with a very user-friendly option. Foundation companies, unlike trusts or partnerships, have separate legal personality, can hold assets, assume obligations, sue, and be sued. However, a key distinction of a foundation company is that it can be structured without shareholders, and so does not have a clear “owner”. In place of shareholders, the foundation company can be supervised by a supervisor (or even multiple supervisors if desired). A supervisor has no ownership or economic entitlement in the foundation company but simply acts as a steward, ensuring that the directors of the foundation company observe their obligations to the DAO pursuant to the foundation company's governing documents. Therefore, with no shareholders, all the officers of a foundation company simply have the objectives of the DAO as their priority – similar to trustees and enforcers carrying out the objectives of a trust.

For Web 3.0 projects looking to issue virtual assets privately, the foundation company is also able to represent the DAO. The VASP Act only regulates the sale of virtual assets to the public. Private sales which are not advertised, and made available to a limited number of persons who are each selected prior to the sale by way of a private agreement, may well fall outside of scope. Furthermore, as the definition is limited to sales for consideration, airdrops and bonus issues should also be excluded.

Where the DAO wishes to carry on VASP activities, one alternative is to create a wholly owned subsidiary of the foundation company in a virtual asset-friendly jurisdiction. The Cayman foundation company will then procure the subsidiary to carry on whichever activities it cannot perform from the Cayman Islands. Whilst this structure is more complex it allows projects to take full advantage of the benefits of the foundation company vehicle in a way that ensures compliance with the VASP Act.

A foundation company limited by guarantee is specifically excluded from the ES Act and from the economic substance regime of the Cayman Islands and therefore a DAO need not move staff, nodes or resources to the Cayman Islands to prove that it has substance here.

## Special Economic Zone (SEZ)

The creation of Cayman Tech City, also known as Technology City Cayman Islands in the SEZ allows a tax neutral environment for technology companies looking to expand in the Cayman Islands. Using Cayman Tech City and the benefits of the SEZ, companies can quickly and cost-effectively establish a genuine physical presence offshore with staffed offices within the special economic zone. See here for more information on [Cayman Special Economic Zone Companies](#).



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## Decentralised Finance (DeFi)

The Cayman Islands has long been a jurisdiction of choice for a variety of financial products and its flexible regulatory environment makes it ideal to use the exempted company or foundations to accommodate the latest shift towards a variety of DeFi products. For DeFi projects the **foundation company** can provide a legal 'wrapper' with corporate personality. In this role the foundation company can undertake many of the real-world activities required by the DeFi project.

For example, the foundation company can act as a service provider for DeFi projects by signing documents and engaging developers or consultants on behalf of the project. It can also act as a fundraising vehicle for early stage and VC private funding (something expressly provided for by the VASP Act) or it can hold a DeFi project's treasury assets to pay for services that are needed on an ongoing basis. The foundation can also act as the entity that opens and operates a bank account for fiat currency if this is required.

This can also provide a vehicle for airdrops, which can be an effective way to promote decentralisation, and grants to support those interested in helping a project. The company can also provide marketing and development services for NFTs, P2E games and metaverse projects.

A foundation company also provides a corporate parent or holding entity for subsidiaries, potentially formed in other jurisdictions, to be formed. These subsidiaries can then carry out functional activities for the project if they better suited to the particular circumstance of that activity. DeFi products are subject to compliance with the VASP Act.

## Intellectual Property Holding Companies

In addition to either the token and coin offering structures and sometimes as a complementary entity to a DAO, some clients wish to incorporate a separate entity to separate IP holding companies or separate software operators in addition to the above. This choice is often driven by the preferences of each business, its risk appetite and its tax considerations.

The preferred vehicle for an entity established to hold Web 3.0 intellectual property is an exempted limited company. Any vehicle established for the sole purpose of holding, exploiting or receiving income from intellectual property assets will not be required to register with CIMA under the VASP Act, but it will be required to satisfy an extended economic substance test under the ES Act. If the satisfaction of the extended economic substance test under the ES Act would be too onerous or cause problems, then it may be more beneficial to use a foundation company for this purpose, as foundation companies are specifically excluded from the ES Act.

## Exchanges

The Cayman Islands exempted limited company allows a Web 3.0 business that conducts its economic activity outside of the Cayman Islands to register as a Cayman Islands domiciled company. The exempted limited company has a more traditional form as it has shareholders and directors. This is therefore a very familiar style of entity that investors and third parties around the world will easily understand. An exchange, in whatever legal form it is created, will inevitably and eventually become subject to phase 2 of the VASP Act. This will require it to register with the CIMA and to obtain a virtual asset service license from the CIMA for the operation of the exchange.



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## Duties of Directors

All the legal entities described above require at least one director. In each case this person or entity acting as the director will be subject to the standard duties and liabilities of a director under Cayman Islands law. For more information on this please see our guidance note on [Duties of a Director under the Law of the Cayman Islands](#).



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