The Gulf-Rock Crypto Fund Solution

Gibraltar's innovative and flexible crypto hedge funds regime must be a top level consideration for Dubai based managers and entrepreneurs when establishing a crypto fund.

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Gibraltar's innovative and flexible crypto hedge funds regime needs to be considered by Dubai based managers and entrepreneurs when establishing a crypto fund.

In April 2022, I had the privilege of participating on a crypto funds panel in Dubai with Dr Marwan Alzarouni, CEO of the Dubai Blockchain Centre. As a representative of the Gibraltar Blockchain ecosystem, I was asked by our very able and provocative moderator *"which is the best jurisdiction for crypto funds?"* I answered that it really depends on what you want to achieve. The various regimes for ICOs, Token Sales and VASPs in Dubai are indeed dynamic. In some cases, they are more fit for purpose than in other jurisdictions which would require full KYC for even a $15 acquisition of a gaming token. On the other hand, I continued, I understood that the ecosystem for crypto funds in the UAE is not yet developed to its full potential; the various regimes being still too restrictive to be effectively usable for many crypto strategies. I suggested that establishing a Dubai-based crypto fund in Gibraltar might indeed be a more effective solution. I received gracious support from my co-panelists, and it was there that the seed was planted of what we have been working on for the last two years: The Gulf-Rock Crypto Fund Solution.

1. The Experienced Investor Fund Regime

Gibraltar has excelled as a crypto funds jurisdiction. The PwC Crypto Hedge Funds Report lists Gibraltar as the top Crypto Funds jurisdiction east of the Atlantic. Why is this the case and how has this come about?
Let me first describe the Financial Services (Experienced Investor Funds) Regulations 2020 (the EIF Regime). The EIF is the flagship hedge fund product in Gibraltar. Geared for investors who are experienced or at least who have access to professional advice, the regime can be much more flexible than most of the "onshore" regimes.

Speed to Market: It is the only regime in the Eastern Hemisphere that allows for the preauthorization launch of a fund without having to engage a costly and cumbersome AIFM manager. A fund can be established with its necessary documentation and service providers and then launched on the basis of a legal opinion from a senior Gibraltar based lawyer which is countersigned by a licensed fund administrator.

Regulatory Certainty: The fund is entitled to launch, accept subscriptions and even trading immediately so long as within ten business days, the documentation is sent to the Gibraltar Financial Services Commission (fsc.gi). This means that one is certain to be able to launch at a specific time without fear of regulatory delay.

UAE Management: This degree of flexibility is possible because EIFs require the engagement of two directors on its board (or on the board of it's GP) who are authorized by the GFSC to act as fund directors. There may be any number of other directors but the two "EIF directors" must always be there. Their purpose is to ensure compliance with regulations and to promote corporate governance. An EIF can be managed by a manager, in any jurisdiction provided that the manager is entitled under its home legislation to manage a fund. This means that there is no Impediment, from a Gibraltar perspective, for a UAE based manager to manage an EIF.

Flexible Administration: An EIF must appoint a fund administrator either from Gibraltar from a jurisdiction that has equivalent fund administration legislation (such as the UAE) and that has been approved by the GFSC and by the Minister of Financial Services to service Gibraltar funds. This is to ensure that the administrator is of a certain size and that it is in good standing with its home regulator. It must appoint a representative to accept service of documents and there is no other substance requirement in Gibraltar.

No Need for Licensed Investment Manager: Many Gibraltar funds are self-managed meaning that they are managed by their

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board of directors rather by a third party investment manager. It is quite common, therefore, for a corporate director, particularly in a low tax jurisdiction such as the UAE, to manage an EIF in its capacity as a director. This means that it is possible in many cases to establish a crypto fund without having to also establish a separate investment manager. A manager, as opposed to an EIF often requires a full regulatory approval before commencing business. This is costly and can delay a fund launch significantly.

Audit: An EIF must submit Financial Statements to the GFSC within six, or in some cases nine months of its financial year end. These must be audited by a Gibraltar registered auditor and they serve to provide investor confidence and robust governance.

No Investment Restrictions: There are no inherent investment restrictions or restrictions on leverage save that one must specify in the fund's private placement memorandum what one's policies are in this regard.

The EIF is therefore a very flexible funds regime that may be used for any asset class if it is promoted only to experienced investors.

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2. Blockchain in Gibraltar

Gibraltar is small and therefore able to be entrepreneurially and regulatorily nimble. In 2018, the Financial Services Distributed Ledger Technology Regulations were published establishing a substantive framework for firms to "store or transmit value for third parties on the blockchain." This ensured that there would be a rich ecosystem of service providers that were ready and able to service blockchain based businesses. This includes directors, administrators, regulators, auditors and even banks that are willing to service blockchain based firms. A couple of years later, the VASP regime came out for businesses wishing to sell digital assets or to provide services to digital firms. Interestingly, the EIF regime was so flexible that it did not require any specific legislation in order for it to be allowed to be used for investment into crypto assets.

Nevertheless, the GFSC issued a statement on 17 October 2018 saying that it had no objection to EIF's being used to establish crypto funds.

On the other hand, the Gibraltar Funds and Investments Association (GFIA.gi), in consultation with the regulator, felt that there were issues specific to crypto funds which were understandably not addressed in the general EIF regulations. Therefore, they produced the world's first Code of Conduct for Crypto Funds which is now in its second edition, and which identifies the elements of crypto funds that directors and managers should be aware of for good governance. The Code is based on an a "comply or explain" basis which means that while it is not necessary to follow the recommendations in the Code, it is nevertheless necessary to document how a specific fund will achieved those regulatory outcomes even if in a manner different to that suggested. Gibraltar was drawn out of the European Union along with the United Kingdom because of Brexit. This meant that it was no longer under a statutory obligation to comply with EU legislation such as the Alternative Investment Fund Manager's Directive which makes it indeed exceedingly difficult to establish a crypto fund. The industry along with the Government and the Regulator produced the Gibraltar Funds Dual Regime added an exemption to AIFMD for funds that notify the GFSC that they have opted out of the operative provisions of the directive. This was perfectly logical since the AIFIM marketing passport was no longer available to Gibraltar funds. Furthermore, compliance with AIFMD would prove almost impossible for crypto funds. It is no wonder therefore Gibraltar became a top crypto funds jurisdiction.

Development in Gibraltar

3. Cooperation

I listened to a fascinating podcast by a crypto funds luminary Henri Arslanian who was proud of having launched a VARA regulated crypto fund but said that it was "*that is had been the most difficult regulatory experience he had ever encountered.*" I believe the regulatory authorization of the fund took over a year. As I mentioned at the outset, different people are good at doing different things and this holds true for regulatory regimes and jurisdictions as well. My discussions with colleagues and even some regulators have shown that the regulatory environment for crypto funds in the UAE is still not as developed as where many would like it to be. The UAE has excelled in so very many areas, even in crypto, that it is not easonable for it to have the best regime for everything. This is why the Gulf-Rock Crypto Solution has been created – to facilitate fund formation for UAE crypto entrepreneurs. The premise is that they can manage Gibraltar EIFs from within the UAE. The symbiosis is clear, the existence of crypto entrepreneurs on the one side, a robust regulatory regime for crypto managers in the UAE (in its different forms with the different regulators) and a robust but flexible regulatory regime for crypto funds based in Gibraltar. This allows both parties to find a solution that was not necessarily available to them before.

It is true that there are other crypto fund options, but we live in a world of the OEDC's Base Erosion and Profit Shifting initiative (BEPS) which requires more that one justify the location of establishment of ones' business, most often by demonstrating substance in that jurisdiction. Looking at a map, it is infinitely more likely that a Dubai based entrepreneur attend a board meeting in Gibraltar than across the Atlantic in the Caribbean.

The UAE is an incredibly dynamic and can-do jurisdiction, as is Gibraltar. The Gibraltar EIF regime offers a highly compelling and effective solution for UAE based crypto managers to set up their fund in a matter of weeks. I believe that the Gulf-Rock Solution could be the beginning of a beautiful friendship.

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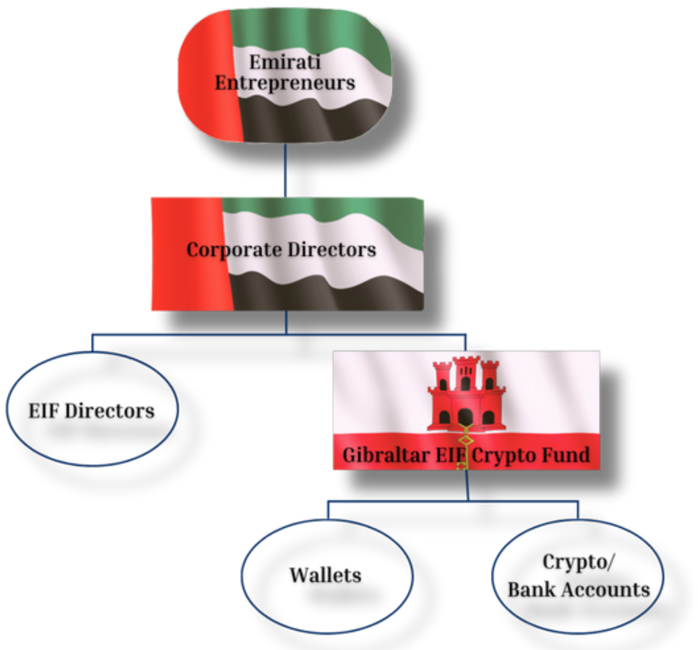

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