

## Revolutionising the "creator" economy: are non-fungible tokens "virtual assets" in Cayman?

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There has been an explosion of interest around non-fungible tokens (**NFTs**) (otherwise known as "niftys" and "crypto-collectibles") in the past year and even greater growth in the sector is expected for 2022. According to [Jeffries](#), the NFT market is forecast to be valued at more than US\$35 billion for 2022 and to over US\$80 billion for 2025.

We have seen headline grabbing news from digital artists such as Mike Winkelmann (more famously known as the digital artist "Beeple") [who auctioned his collage, 'Everydays: The First 5000 Days', for US\\$69 million](#) and the renowned and prestigious auction house, Christie's, [auctioning five unique NFTs of digital works created by Andy Warhol](#) in the mid-1980s. Mega-brands are also moving in on the metaverse and positioning themselves at the forefront of NFTs, as can be seen by [Nike's acquisition of NFT studio, RTFKT](#), and [Adidas collaborating with the Bored Ape Yacht Club](#).

It is an exciting time for artists, developers, celebrities, athletes, and other "creators" as a new world of value and revenue creation can be made through NFTs by the tokenisation of real world assets and virtual assets. However, regulatory uncertainty could result in a missed opportunity for many. Or worse, it could result in legal action for an unknowing breach of law. Therefore, participants in the market should navigate this new and complex area with a degree of caution.

In this article, we will dive into the regulatory landscape of virtual assets from a Cayman Islands perspective and explain the impact of the Cayman Islands Virtual Asset (Service Providers) Act (Revised) (**VASP Act**) on NFTs.

### What are NFTs

For those who are experts, you can skip this section, but for those who are new to the topic, a little background could help.

NFTs are digital assets based on computer code "which can be used to create a tokenised proof of title to a unique digital version of an underlying digital asset (such as images, videos or other digital content) or physical asset (such as paintings, sculptures or other tangible assets)". [1] One can therefore compare NFTs to, say, a digital certificate or deed of title, and be used to prove ownership and authenticity of an asset as evidenced by an immutable, cryptographically-secured record on a blockchain such as Ethereum or other distributed ledger technology. They also have the key characteristics of being "non-fungible" and "non-interchangeable" and are generally freely tradeable.

As a result, NFTs could open new revenue streams and earning potential for brands, celebrities, athletes, artists, bands, songwriters, authors, and many others in the "creator" economy. Through the use of inbuilt smart contracts, these "creators" can receive royalty payments upon onward sales and, due to their transferability, provide access to a much wider, fairer and more inclusive global market with no geographical or economic boundaries. NFTs will also aid in the fight against fraud and theft by proving authenticity and ownership throughout the lifetime of an NFT, which will ultimately benefit the "creator".

## **Virtual Assets in Cayman**

The definition of "virtual asset" is set out in Section 2 of the VASP Act, which generally tracks the language of "virtual asset" provided by the Financial Action Task Force in its Glossary. The VASP Act defines "virtual assets" 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".

The VASP Act was introduced into the Cayman Islands as a means of regulating virtual asset issuances, as well as the exchange, transfer and custody of, and provision of financial services relating to, virtual assets. Under the VASP Act, the Cayman Islands Monetary Authority (**CIMA**) is the regulator tasked with oversight of virtual assets in the Cayman Islands and therefore, possibly, NFTs.

## **So, are NFTs categorised as "virtual assets" in Cayman?**

The FATF in its most recent Guidance has very helpfully provided that NFTs "are generally not considered to be [Virtual Assets] under the FATF definition" (which as noted above, in Cayman, the definition generally tracks the FATF version). Given that the regulation of virtual assets is relatively new, regulators, such as CIMA, typically look towards the FATF and their recommendations. Accordingly, this FATF guidance is a positive step forward in providing direction as to the regulation of virtual assets and NFTs.

We see two important aspects in the definition of "virtual asset" that supports the proposition

that NFTs should not be generally categorised as virtual assets for the purposes of the VASP Act; namely, that NFTs cannot typically be used for:

1. "payment" purposes, or
2. "investment" purposes

We will now explore these specific points in further detail.

### **NFTs typically cannot be used for "payment" purposes**

While the word "payment" may cover a multitude of ways of discharging obligations, "payment in the legal sense means a gift or loan of **money** or any act offered and accepted in performance of a **money** obligation" and, it is said, "[m]oney must therefore feature in some way" per Goode and McKendrick on Commercial Law (which is an authoritative text that many common law students know well).

So then, one must next ask whether NFTs are "money"? We believe this is not the case. On a general level, the common view under English law is that, per Goode and McKendrick, "virtual currencies are not presently regarded as money", a view that has also been supported by the Bank of England.

To be defined as "money", NFTs would need certain key "essential legal characteristics" to be present. However, NFTs generally do not possess such features. For example, in Cayman:

1. there is currently no "backing" of NFTs by the Cayman Islands Government, as "money"
2. there is no "recognition" by the Cayman Islands Government that NFTs are "money"
3. NFTs are said not to be a store of value and are not a generally accepted medium of exchange as they are too volatile to be used as a means of payment
4. given NFTs are not stores of value and are an inefficient and an unreliable media of exchange, they could not be used as units of account

Accordingly, as NFTs lack the requisite characteristics of money, NFTs cannot, and should not, be treated as being capable of being used for "payment" purposes.

### **NFTs typically cannot be used for "investment" purposes**

In addition to the inability to use NFTs for payment purposes as explained above, we are also of the view that they cannot be used for "investment" purposes. English law provides welcome direction as to the determination as to what constitutes a traditional "investment", which is "to apply money in the purchase of some property from which interest or profit is expected and which property is purchased in order to be held for the sake of the income which it will yield" and where property is purchased for "some other purpose than the receipt of income [...] it is

not [...] an investment" (Re Power).

Purchasing and holding NFTs would not be expected to provide a "yield", nor an "expectation of profit" for the holder (such as, for example, a dividend, interest or repayment of principal or capital at the end of a defined period). Yes, there may be capital appreciation and profit when one sells, but it is not necessarily "expected" and not the sole purpose of the purchase. Rather, NFTs are typically held for some "other purpose" (such as representing a unique piece of artwork or one off fashion piece). Therefore, NFTs should not be considered "investments" and so cannot be held for "investment purposes" within the meaning of "virtual asset" under the VASP Act.

## **Ready to mint?**

We welcome FATF's Guidance on NFTs and look forward to confirmation from regulators, including CIMA, that NFTs are not virtual assets.

Whether you are planning on issuing, minting or trading your own NFTs or developing a platform that will involve NFTs, our global team of experienced lawyers at Ogier are on hand to assist.

NFTs and virtual assets generally are an evolving asset class and their regulatory situation remains uncertain. The considerations and suggestions above do not constitute legal advice and developers, issuers and market participants should obtain their own unique legal advice before undertaking any NFT-related project in, or from within, the Cayman Islands.

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[1] Read more [here](#).

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