

Statement of Guidance
**Guidance for the provision of virtual
asset services -Virtual Asset Custodians
and Virtual Asset Trading Platforms**

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List of Acronyms

IT	Information Technology
MAA	Monetary Authority Act
VASP	Virtual Asset Service Provider



Guidance – Virtual Asset Custodians and Virtual Asset Trading Platforms

1. Introduction

- 1.1. This document establishes the Cayman Islands Monetary Authority’s (the “Authority”) Guidance on the provision of virtual asset services by virtual asset custodians and virtual asset trading platforms (“the Guidance”) regulated under the Virtual Asset (Service Providers) Act (as amended) (the “Act”).

2. Statement of Objectives

- 2.1. To provide guidance to virtual asset custodians and virtual asset trading platforms in relation to the provision of virtual asset services, pursuant to the Monetary Authority Act (“MAA”).
- 2.2. This Guidance is not intended to be prescriptive, exhaustive or a comprehensive approach to managing VASP related risks and operations; rather this Guidance sets out the Authority’s minimum expectations in relation to the management of risks and operations by custodians or trading platforms.

3. Statutory Authority

- 3.1. Section 34(1)(a) of the MAA provides that:

After private-sector consultation and consultation with the Minister charged with responsibility for Financial Services, the Authority may -

issue or amend rules or statements of principle or guidance concerning the conduct of licensees and their officers and employees, and any other persons to whom and to the extent that the regulatory laws may apply;

- 3.2. This Guidance should be read in conjunction, where applicable, with all the laws and regulatory measures addressing anti-money laundering, the conduct of virtual asset services, ownership and control, fitness and propriety, internal controls, cybersecurity, business continuity management, corporate governance, outsourcing, nature, accessibility and retention of records, securities investment business, banks and trusts and any other relevant laws and regulatory instruments issued by the Authority from time to time.
- 3.3. In this document, references to any act or regulation shall be construed as references to those provisions as commenced, amended, modified, re-enacted or replaced from time to time.

4. Scope of Application

- 4.1. This Guidance applies to virtual asset custodians and virtual asset trading platforms that are regulated by the Authority under the Act.



5. Definitions

5.1. The following definitions are provided for the purpose of this Statement of Guidance:

“bank” means a person carrying on banking business, as defined under the Banks and Trust Companies Act;

“client” means a legal or natural person, to whom virtual asset services are provided;

“governing body” of a regulated entity¹ means the Board of Directors where the entity is a corporation, the General Partner where the entity is a partnership, the manager (or equivalent) where the entity is a Limited Liability Company, and the Board of Trustees where the entity is a trust business;

“independent third party” means a party who, to the best of the governing body’s knowledge, information and belief having made all reasonable enquiries, are independent of, and not connected with, the regulated entity or any of its connected persons;

“senior officer” has the same meaning as defined in the Act;

“virtual asset custodian”, hereafter referred to as **“custodian”**, has the same meaning as defined in the Act;

“virtual asset custody service” has the same meaning as defined in the Act;

“virtual asset trading platform” hereafter referred to as **“trading platform”**, has the same meaning as defined in the Act;

“SOC 1” means a Service Organisation Control 1 audit report which documents the audit of an entity’s internal controls relevant to the processing and securing of financial data; and

“SOC 2” means a Service Organization Control 2 audit report which documents the audit of an entity’s internal IT controls relevant to the security, availability, processing integrity; confidentiality and/or privacy.

6. Governance

6.1. The governing body should have the appropriate balance of skills, experience, independence, and knowledge of the industry to enable them to discharge their respective duties and responsibilities.

¹A regulated entity refers to any natural or legal person(s) or arrangement(s) that has been licensed or registered under the Act.

- 6.2. Directors should review their commitments to ensure they have sufficient availability and resources to be able to carry out their role on the governing body effectively.
- 6.3. The governing body should undertake a formal review by an independent third party, on an annual basis, that ensures that the policies and procedures of the custodian or trading platform are effective in meeting the obligations set out in the Act and accompanying rules and guidance.

7. Conduct of Business

Conflicts of interest

- 7.1. The policies and procedures implemented by custodians or trading platforms for the identification and management of conflicts of interest should consider:
 - a) conflicts of interest between custodians or trading platforms and their beneficial owners, directors, senior officers, employees and clients;
 - b) any personal conflicts of interest of any employee tasked with decision-making;
 - c) keeping and maintaining a register of potential and existing conflicts of interests, along with the mitigating measures in place; and
 - d) avoiding assignment of conflicting duties to one individual. Certain duties within a custodian or trading platform should be split, to the extent possible, among various individuals to reduce the risk of manipulation of financial data or misappropriation of assets.

Treating clients fairly

- 7.2. A custodian or trading platform should have policies and procedures for the fair treatment of clients that promote the following outcomes:
 - a) developing, marketing, and selling products or services in a way that pays due regard to the interests and needs of clients;
 - b) providing clients with information before, during and after the transaction that is accurate, clear, and not misleading;
 - c) minimising the risk of providing products or services which are not appropriate to clients' interests and needs;
 - d) dealing with client complaints in a fair and timely manner;
 - e) protecting the privacy of information obtained from clients; and
 - f) where relevant, protecting any virtual assets or fiat funds held on behalf of clients.



- 7.3. A custodian or trading platform may demonstrate that it has acted ethically and with integrity if, at all times, the custodian or trading platform:
- a) observes high standards of integrity and fair dealing in the conduct of its business;
 - b) acts within its powers;
 - c) uses information obtained in confidence by their customers for the benefit only of their customers and for the purpose for which it was obtained;
 - d) acts professionally and execute its responsibilities properly; and
 - e) does not behave in a way that is dishonest, reckless, or misleading.

The list set out above is non-exhaustive.

Client communications and full disclosure

- 7.4. A conflict of interest is considered to exist if the conflict may damage the interests of a client.
- 7.5. A conflict of interest or potential conflict of interest may occur between:
- a) the custodian or trading platform and their beneficial owners, directors, senior officers, employees and clients;
 - b) one client and another; or
 - c) business of another subsidiary or entity within the group.
- 7.6. The types of conflict of interest that may arise in the course of a custodian or trading platform providing services and which should be disclosed may include, but is not limited to, cases where the custodian or trading platform:
- a) is likely to make a financial gain, or avoid a financial loss, at the expense of the client;
 - b) has an interest in the outcome of the service provided to the client or of a transaction carried out on behalf of the client, which is distinct from the client’s interest in that outcome;
 - c) has a financial or other incentive to favour the interest of another client or group of clients over the interests of the client; and
 - d) receives or will receive from a person other than the client an inducement in relation to a service provided to the client, in the form of monies, goods or services, other than the standard commission or fee for their service.



- 7.7. A custodian or trading platform should maintain and operate effective organisational and administrative arrangements with a view to taking all reasonable steps to prevent conflicts of interest from adversely affecting the interests of its clients.
- 7.8. In ensuring that information provided to clients is fair, clear, and not misleading, the custodian or trading platform should consider the ways of conveying information, the content of the communication is intended to convey and the type and experience of the client.
- 7.9. Communication with clients, whether verbal or written, would be considered 'clear' if it:
- a) uses plain language;
 - b) is logically ordered and easy to follow;
 - c) highlights important information; and
 - d) explains complex information in plain language and provides a clear explanation or definition of any necessary jargon.
- 7.10. The custodian or trading platform should ensure that all information provided to clients:
- a) includes the name of the custodian or trading platform together with its applicable CIMA authorised number;
 - b) is accurate and always gives a fair and prominent indication of any relevant risks in relation to the provision of virtual asset services;
 - c) is sufficient for and presented in a way that is likely to be understood by the average client in the group of clients to whom it is directed, or by whom it is likely to be received;
 - d) does not disguise, diminish, or obscure important items, statements, or risk warnings;
 - e) uses a font size in the indication of relevant risks that is at least equal to the predominant font size used throughout the information provided, as well as a layout that ensures that such indication is prominent;
 - f) is consistently presented in the same language throughout all forms of information and marketing materials that are provided to each client, unless the client has agreed to receive information in more than one language; and
 - g) is up-to-date and relevant to the means of communication used that the client has agreed to.



- 7.11. When communicating information to clients, the custodian or trading platform should consider whether an omission of relevant facts would result in the information being unfair, unclear, or misleading.
- 7.12. When making disclosures to clients regarding the capacity they are acting in (in relation to a relevant transaction), this could be detailed in a terms and conditions document or an alternative and should be made available to clients prior to any transaction or client agreement being made.
- 7.13. The custodian or trading platform should inform clients of the regulated activity they perform and the Authority responsible for regulating such activity.
- 7.14. If a custodian or trading platform has partnered with a third-party provider (i.e. a bank to hold fiat funds), it should make it clear to clients' which party they are transacting with.
- 7.15. When a custodian or trading platform is part of a larger group structure, clients must be made aware of which group entity they are transacting with at all times, including the regulatory status of that entity, and the level of protection afforded to the client.
- 7.16. A custodian or trading platform should disclose to its client any conflict of interest or potential conflict of interest.
- 7.17. A custodian or trading platform should inform clients of the typical timeframes for the processing of account withdrawals or account closure, including where, as a result of safeguarding controls (such as virtual assets being stored in offline wallets), virtual asset withdrawals would take longer to process. A custodian or trading platform should inform clients of any withdrawal limits and related timeframes for specific thresholds.
- 7.18. Disclosures to clients should be made when any material changes have been made to the service(s) provided by the custodian or trading platform that may impact clients. This includes sale of the custodian or trading platform or ceasing of operations.

Risk warnings

- 7.19. When providing an indication of the risks relating to the product or service being offered, the custodian or trading platform should provide clients with sufficient information to allow them to make well-informed decisions. Client risk warnings should include the following:
 - a) a disclosure, where necessary, that the virtual asset has a particularly volatile trading history;
 - b) where applicable, insurance and safeguarding measures in place;
 - c) where the client wishes to deposit or withdraw virtual assets to or from a wallet address controlled by the custodian or trading platform the risks relating to the transfer and storage of virtual assets; and



- d) a disclosure that the client’s invested capital is at risk.
- 7.20. Particularly with regards to higher risk and more complex products, virtual asset trading platforms should include, where appropriate, risk warnings to clients relating to:
- a) the percentage of clients that lose money when trading a particular product with the virtual asset trading platform; and
 - b) the risks of trading derivatives, with leverage or other similar products, including the enhanced risk of loss and the risks relating to margin calls and position liquidations.
- 7.21. The custodian or trading platform should ensure that clients understand and acknowledge the risk warnings provided.

Complaints handling

- 7.22. A custodian or trading platform should establish effective internal complaints handling systems and procedures. These should include:
- a) making available details of the custodian’s or trading platform’s complaints handling policy that can be easily accessed by clients;
 - b) establishing a standardised template or simple method for clients to be able to make complaints;
 - c) acknowledging receipt of client complaints in writing within 7 days;
 - d) maintaining a record of complaints received and the remediation measures or actions taken;
 - e) investigating all complaints in a manner which is timely, fair, and consistent;
 - f) providing the complainant with timely updates as to the status, proposed resolution, or outcome of their complaint;
 - g) informing complainants of their options if a complaint is not resolved in a manner that they are satisfied with; and
 - h) ensuring that the governing body is provided with regular reports on complaints handling, including analysis of all ongoing complaints, outcomes, complaints handling data, and any potential systemic issues.
- 7.23. The governing body should ensure that complaints data are sufficiently analysed and that any necessary improvements are made to the service provided to clients.
- 7.24. Clients should be able to file complaints with a custodian or trading platform free of charge.



Marketing & promotions

- 7.25. A custodian or trading platform should ensure that any marketing communications of their products or services do not include any misleading statements or promises regarding the scale of the custodian or trading platform activities or any statements that the custodian or trading platform does not believe to be true.
- 7.26. A custodian or trading platform should not include in their marketing communications any statements detailing historic market performances of virtual assets unless:
- a) the basis on which such performance is measured is clearly stated and the presentation is not misleading;
 - b) it is accompanied by a risk warning that past performance is not necessarily a guide to future performance; and
 - c) the past performance detailed is relevant to the service or product offered by the custodian or trading platform.
- 7.27. A custodian or trading platform should ensure that marketing communications do not compare their products or services to other forms of investment or trading unless the reason for the comparison is clearly stated, justified and appropriate.
- 7.28. A custodian or trading platform should ensure that the marketing of higher risk products, such as derivatives or leveraged trading, includes a warning of the risks involved. These may include:
- a) the enhanced risk of losing invested capital through margin calls or liquidations;
 - b) the impact of small fluctuations in the price of virtual assets;
 - c) the risk of imperfect correlation between a derivative and the underlying asset and the resultant hedging risk; and
 - d) statistics and statements on the percentage of clients that lose money when trading with the custodian or trading platform.
- 7.29. A custodian or trading platform should maintain a record of any marketing communications or promotional campaign. This should be made available to the Authority if necessary.

Client protection

- 7.30. A custodian or trading platform should:
- a) assess the risks and complexity of its products and services;



- b) assess the level of understanding, experience, and vulnerability of its clients; and
 - c) develop controls which are proportionate to the level of risk and the experience and vulnerability of clients and client assets.
- 7.31. Although not an exhaustive list, examples of the measures that a custodian or trading platform may take in this regard include:
- a) carrying out robust testing of new products and services and the effectiveness of controls before they are offered to clients;
 - b) considering the extent to which client assets are at risk as a result of the product or service offered;
 - c) assessing the volatility of a virtual asset, product or service and the extent to which a product or service is suitable and appropriate for a client. This may include taking into consideration the nature of the client (whether it is a retail or corporate client), the client's risk appetite and the client's financial position; and
 - d) assessing the level of understanding by the client of the features and risks of the products and services offered or previous experience in dealing with virtual assets or similar products and services.

Client agreement

- 7.32. A custodian or trading platform should, when structuring a client agreement, look to include the following:
- a) a description of all group entities and other parties including any relevant third-party service providers carrying out outsourced functions, in connection with the services being provided;
 - b) the nature of the products and description of services being provided, and the name of the legal entity being contracted to provide those services;
 - c) the basis and method of calculation of fees payable by the client as well as the frequency and method of payment, whether by bill or deduction of capital;
 - d) any commission received by the custodian or trading platform or associated parties in connection with the client transaction;
 - e) the jurisdiction and Authority that is responsible for regulating a custodian or trading platform and where relevant, the jurisdiction and Authority responsible for regulating any relevant third-party service provider;
 - f) the way instructions may be given by the client in any transaction;



- g) the arrangements for handling client virtual assets, including any details in relation to the payment of interest;
 - h) in respect of any contractual right of the custodian or trading platform to realise client virtual assets:
 - i) the circumstances in which and the action it may take to do so; and
 - ii) the specific virtual assets over which it may do so; and
 - i) the arrangements for bringing the agreement to an end.
- 7.33. When providing written confirmation to a client, on or before the completion of a transaction, a custodian or trading platform should include the following details in a clear and concise manner:
- a) an order identification number that the client is able to communicate to the custodian or trading platform in the event of any discrepancies or operational issues;
 - b) the virtual asset being transacted along with the price, quantity, and total cost;
 - c) the date and time that the transaction was placed;
 - d) any commissions or fees charged as a result of the transaction; and
 - e) if applicable, the direction of the transaction i.e. a buy or sell order.

8. Prudential

Regulatory capital

- 8.1. A custodian or trading platform should always hold adequate regulatory capital, being the higher of:
- a) the risk-based capital as determined pursuant to sections 8.2 and 8.3 below; or
 - b) the amount equal to six months fixed overheads of the custodian or trading platform as determined pursuant to section 8.4 and 8.5 below; or
 - c) such amount as determined by the Authority.

Risk Based Capital

- 8.2. A custodian or trading platform should conduct periodic risk assessments and stress tests on their business strategy and operations and consider the impact on their regulatory capital.

- 8.3. The risk-based capital should cover potential financial losses which are proportionate to the type and level of risks the custodian or trading platform is exposed to. Consideration should be given when identifying significant sources of risk which could impact the ability of the custodian or trading platform to meet its liabilities, including analysis and monitoring of the following risk areas which should assist in the calculation of the risk-based capital:
- a) credit risk;
 - b) market risk (including virtual assets and fiat funds);
 - c) operational risk;
 - d) liquidity risk;
 - e) insurance risk;
 - f) interest rate risk;
 - g) concentration risk;
 - h) IT and cybersecurity risk;
 - i) settlement risk; and
 - j) legal and compliance risk.

Working Capital for Fixed Overheads

- 8.4. A custodian or trading platform should hold sufficient working capital to cover fixed overheads amounting to at least six months of the preceding year or projected fixed overheads in the case of the custodian or trading platform not having completed a full year of business.
- 8.5. The working capital for fixed overheads should be reviewed annually and calculated by subtracting the following items from the total expenses after distributions of profits to shareholders:
- a) employee bonuses and other types of remuneration which are subject to net profits of the services provided;
 - b) any shares in profits; and
 - c) variable expenses from non-ordinary activities.
- 8.6. A custodian or trading platform may consider the use of virtual assets as part of its regulatory capital. Should this approach be taken, the Authority will require, as a minimum, for custodian or trading platform to hold additional capital and apply stress tests and risk assessments on the exposure of each virtual asset. Consideration should also be given to the security and storage

controls in place to manage the virtual assets, and the ongoing monitoring of the capital position with the use of suitable triggers and margin calls.

- 8.6.1 If a custodian or trading platform decides to use virtual assets as part of its regulatory capital, the Authority will consider the particulars of each circumstance (including security and storage controls) and work with the custodians or trading platforms to ensure that it is in a position to be able to meet its prudential obligations on an on-going basis.
- 8.7. If a custodian or trading platform decides to hold regulatory capital in a foreign currency, the custodian or trading platform should consider the need to have an adequate capital buffer to mitigate risks such as exchange rate fluctuations.
- 8.8. The custodian or trading platform should hold sufficient working capital to allow for the day-to-day operations of the business and to ensure that adequate regulatory capital is maintained.
- 8.9. The custodian or trading platform should inform the Authority of any breaches to regulatory capital requirements or of any material changes to business or operational controls that may cause financial losses and affect the adequacy of the total regulatory capital.

Recovery plan

- 8.10. A recovery plan should set out options to restore financial strength and viability when the custodian or trading platform comes under severe stress. The recovery plan should be designed to respond to different types of stress.
- 8.11. The recovery plan should include an analysis of the vulnerabilities associated with the size, nature, and complexity of the custodian's or trading platform's operations, risk profile, and business model.
- 8.12. Consideration should also be given to identifying when an event has occurred. Such triggers could be either financial or non-financial. Financial triggers could include:
- a) revenue reports;
 - b) account withdrawals and closures; and
 - c) regulatory financial penalties.
- Non-financial triggers could include:
- a) unexpected loss of senior officers;
 - b) adverse court rulings;
 - c) cyber incidents; and
 - d) negative press and significant reputational damage.

- 8.13. A custodian or trading platform should consider credible options to cope with a range of scenarios including both specific and market wide stress. The feasibility of each of these options and the factors that may affect implementation should also be considered. Recovery options may include:
- a) the custodian or trading platform capital raising ability;
 - b) asset sales;
 - c) access to wholesale funding;
 - d) cost saving;
 - e) risk reduction;
 - f) earnings retention; and
 - g) liability management.

Stress testing

- 8.14. A custodian or trading platform should use an appropriate number of market-wide and specific stress scenarios to assess the robustness of their recovery plans, balance sheet capital, and material lines of business.
- 8.15. Stress testing should be severe enough to be useful in establishing triggers, estimating impacts of adverse situations, and establishing responses to remediating situations. They should also acknowledge that the price of any virtual asset sales or disposals will be lower than the market rate if, as a result of market distress, competitors are taking similar action at the same time.
- 8.16. A custodian or trading platform should identify, test, and at least annually, update scenarios that are most likely to cause a custodian or trading platform to become non-viable or to fail. Typical scenarios could include:
- a) how a cyber-attack resulting in the loss of access and value of client's online wallets will affect the custodian or trading platform in relation to both reputational damage and immediate financial impact; and
 - b) the sudden drop in market value of a particular virtual asset that is held by the custodian or trading platform on its balance sheet as regulatory capital.
- 8.17. A custodian or trading platform should also undertake a worst-case scenario assessment in which multiple risks materialise simultaneously, including documenting the impact and likelihood of such a scenario occurring.

Insurance

- 8.18. The level of insurance cover that a custodian or trading platform hold should be based on their products and services they offer, and their scale of operations. Consideration should be given to the following risks:

- a) loss or theft of virtual assets belonging to clients;
- b) loss of documents;
- c) misrepresentations or misleading statements made;
- d) acts, errors, or omissions resulting in a breach of:
 - i) legal and regulatory obligations;
 - ii) the duty to act honestly, fairly, and professionally towards clients; and
 - iii) confidentiality obligations; and
- e) failure to establish, implement and maintain appropriate procedures to prevent conflicts of interest.

8.19. Where a custodian or trading platform are unable to obtain insurance cover, the Authority may expect them to justify how the risks that would otherwise have been covered by insurance will be mitigated. This could include holding additional risk-based capital or through self-insurance subject to approval from the Authority. A custodian or trading platform should be required to perform a review of self-insurance cover on at least an annual basis, considering the number of clients and volume of business to ensure that sufficient coverage is in place.

Audit requirements

8.20. A custodian or trading platform should undertake an annual assessment of the need to conduct, through an independent third party, an audit of their AML/CFT internal controls and procedures. The Authority may, at the custodian's or trading platform's expense, request a report by the independent third party on the audit of the custodian's or trading platform's AML/CFT procedures and their compliance with the Anti-Money Laundering Regulations.

8.21. A custodian or trading platform should also undertake audits of their financial statements, technology and cybersecurity, among others, in accordance with applicable acts and regulatory measures issued by the Authority from time to time.

9. Risk Management

9.1. A custodian or trading platform should adopt a culture that encourages good risk behaviours, with the governing body setting the tone from the top.

9.2. A custodian or trading platform should implement a business-wide risk management framework that outlines how they will identify, evaluate, and manage risks to their objectives, clients, and the reputation of the Cayman Islands.

- 9.3. The risk management framework should set out:
- a) clearly defined roles, responsibilities and accountability for the governing body, senior officers, and employees in relation to the management of risk;
 - b) the custodian's or trading platform's risk appetite and tolerance, defining the custodian's or trading platform's position and strategy in relation to the risks that it faces;
 - c) the process for the identification, evaluation, management and reporting of risk;
 - d) the process and method by which identified risks will be recorded and reported to the governing body to ensure that well informed, timely, risk-based decisions are made; and
 - e) policies setting out the minimum standard to be applied to the management of key risks, such as risks to client assets, money laundering, terrorist financing, proliferation financing and cybersecurity.
- 9.4. Risk management frameworks should be approved by the custodian's or trading platform's governing body. A review to ensure that the risk management framework continues to be fit for purpose should be carried out at least annually or as required by the Authority and in the event of any material changes to the custodian's or trading platform's external or internal environment.
- 9.5. A custodian or trading platform should establish a risk register consisting of at least the following information:
- a) a description of all risks identified;
 - b) the individual(s) responsible for monitoring each specified risk;
 - c) the inherent risk profile, including an impact and probability of occurrence rating;
 - d) the controls in place to mitigate each risk;
 - e) the residual risk profile and overall rating taking into account the controls in place and their effectiveness; and
 - f) any management actions to be taken or further controls to be implemented should the residual risk fall outside the risk appetite of the custodian or trading platform.
- 9.6. Risk registers should be reviewed and updated at least annually.



Internal controls

- 9.7. A custodian or trading platform should have in place internal control mechanisms that help manage and control their business effectively and minimise their risk exposure.
- 9.8. Internal controls should be relevant to specific business processes or areas and the custodian or trading platform should have a system in place to record controls.
- 9.9. A custodian or trading platform should at least annually and independently assess the effectiveness of their internal controls. Any failings or deficiencies identified in relation to an internal control should be remediated in a timely manner.
- 9.10. All findings of the annual assessment should be reported to the governing body at least annually unless there is an internal control failure which should be reported immediately.

10. IT and Cybersecurity

Technology risk management and IT vulnerabilities

- 10.1. A custodian or trading platform should ensure the following is performed over any material outsourcing including IT third-party service provider, including those carrying out any related outsourced functions:
 - a) due diligence reviews;
 - b) review of contractual terms and conditions;
 - c) review of cyber security policies, procedures and controls in place at the service provider;
 - d) review of the incident recovery strategy of the service provider;
 - e) review of the disaster recovery plan of the service provider;
 - f) review of the financial stability of the service provider; and
 - g) insurance cover of the service provider.
- 10.2. A custodian or trading platform should monitor and review the IT service provider on a regular basis.
- 10.3. A custodian or trading platform should ensure that there is an exit strategy in place in the event of termination of the relationship with an IT service provider.
- 10.4. A custodian or trading platform should put in place procedures to monitor technology risks and IT vulnerabilities including risks specific to virtual assets such as smart contract vulnerabilities and hacks.

- 10.5. Technology risk and IT vulnerabilities should be assessed on an annual basis and included in a risk register detailing how risks were mitigated or accepted.

Independent assessments and tests

- 10.6. A custodian or trading platform should arrange for external penetration tests by an independent third party to be performed annually and should disclose the results of such tests to the Authority.
- 10.7. A custodian or trading platform should arrange for tests of internal controls to be performed once every 12 months from the date on which the custodian or trading platform has been authorised by the Authority.
- 10.8. Tests of internal controls by an independent third party may take the form of external tests which may include, but are not limited to:
- a) SOC1 audit reports when testing the internal controls relating to financial data;
 - b) SOC2 audit reports when testing the internal IT controls;
 - c) Penetration testing, vulnerability assessments and other cybersecurity related testing;
 - d) any other controls or audit reports prepared under International Standards which are equivalent to SOC1 or SOC2 reports; or
 - e) any other controls or audit reports which the Authority may deem appropriate.

11. Virtual Asset Custody Service

- 11.1. When ensuring that virtual assets and fiat funds belonging to clients are protected from third party creditors, custodians or trading platforms should:
- a) implement an appropriate contractual relationship with its customers that is adequately reflective of its arrangements;
 - b) not stake its client’s virtual assets unless the client has provided consent in writing; and
 - c) ensure that, if the client has consented to their virtual assets being staked, appropriate safeguards are put in place to protect the client’s virtual assets.
- 11.2. A custodian or trading platform that provides virtual asset custody services should implement appropriate policies and procedures to ensure the safekeeping and control of client assets, as well as the means of access to such virtual assets. These policies and procedures should mitigate the risk of loss of client’s virtual assets, or the rights related to those virtual assets through fraud, cyber threats, or negligence. Policies, procedures and controls to ensure safekeeping should include the following:



- a) providing for adequate segregation of virtual assets and fiat funds belonging to clients from those belonging to the custodian or trading platform or to other clients of the group;
 - b) ensuring frequent reconciliation of client balances;
 - c) providing regular and timely information to the client detailing the client's position in relation to all virtual assets and fiat funds in their name. This should include the client's balance and value in each as well as all transfers and other transactions made during that period;
 - d) providing clients with any information relating to operations on virtual assets that would require a client response without delay;
 - e) management of private keys or any other method by which virtual assets are held by the custodian or trading platform;
 - f) multi-factor authentication; and
 - g) recurring testing of IT security and access management.
- 11.3. A custodian or trading platform that outsources custody of virtual assets and fiat funds to a third-party custodian should be satisfied that the assets and funds are held in trust and that the custodian is not entitled to combine the amounts with any others or to exercise any right of set-off or counterclaim against such assets or funds in respect of any debt owed to the custodian by the Custodian or trading platform.
- 11.4. A custodian or trading platform that provides virtual asset custody services should have an appropriate framework in place when it comes to determining the use of online and offline wallets, including the mechanisms and parameters used for transfer between such wallets. The framework should:
- a) consider and determine the parameters and balance kept in online and offline wallets, taking into account:
 - i) the nature of its products and services, including the speed and frequency with which transactions are effected and settled;
 - ii) the liquidity needs of the business and its clients; and
 - iii) past performance and demands;
 - b) carry out a risk assessment and analysis on the chosen mechanisms for the use of online and offline wallets, and the balance between each type. This should include security measures, how the mechanisms and parameters will be monitored, and how risks will be mitigated, particularly the risk of potential financial losses for clients; and
 - c) test, record, and conduct audits on the storage and transfer between offline and online wallets, by an independent third party.



- 11.5. A custodian or trading platform that provides virtual asset custody services should always ensure they are adhering to the latest industry standards on the use of online and offline wallets, such as having adequate and regular backup systems, multi-signature controls, wallet software updates, and robust cybersecurity controls and measures in place.

Reconciliation

- 11.6. A custodian or trading platform that provides virtual asset custody services should:
- a) reconcile the account balances of its own assets and of virtual assets and fiat funds belonging to clients at a minimum on a daily basis;
 - b) ensure that virtual assets belonging to clients are applied to the correct addresses in good time;
 - c) develop and maintain a reconciliation process which compares virtual asset balances on its internal account balances with those recorded on the relevant distributed ledger;
 - d) maintain adequate records of any discrepancies and take the necessary measures to remedy any differences and fully reconcile account balances;
 - e) cover any unresolved discrepancies in clients' account balances as part of the reconciliation process; and
 - f) have an automated reconciliation process.

Management of private keys

- 11.7. The custodian or trading platform that provides virtual asset custody services should have documented policies, procedures and controls in place around:
- a) Key/seed creation;
 - b) Key storage;
 - c) Key usage; and
 - d) Key compromise protocols

These policies should detail the procedures followed and controls in place to ensure the safe creation, storage and usage of private keys.

- 11.8. The custodian or trading platform that provides virtual asset custody services should carry out robust due diligence at least annually on individuals who operate and hold private keys.
- 11.9. Security audits should be performed in line with industry standards such as the Crypto Currency Security Standard ("CCSS") or other recognised standards.

Remediation actions should be put in place for any findings identified during the audit.

12. Virtual Asset Trading Platforms

Market integrity

- 12.1. Virtual asset trading platforms should establish and maintain efficient arrangements, systems, and procedures to detect and report suspicious orders and transactions, which are effective and appropriate to the size and nature of the business.
- 12.2. Virtual asset trading platforms should adopt a surveillance system to detect market abuse. The type of system, whether it is manual or automated, will be driven by the size, scale, and complexity of the virtual asset trading platforms. Consideration should be given to:
 - a) the number of transactions that will need to be monitored;
 - b) the type of virtual asset being traded by the client;
 - c) the frequency and volume of orders and transactions; and
 - d) the risk profile and nature of the virtual asset trading platforms.
- 12.3. Virtual asset trading platforms should implement appropriate surveillance arrangements that apply to all virtual asset product offerings and should at least annually reconcile the coverage of such arrangements against its risk assessment.
- 12.4. Virtual asset trading platforms should have policies and procedures in place that allow for the analysis, individually and comparatively, of each transaction executed and order placed, modified, cancelled, or rejected in their systems.

Clearing and settlement

- 12.5. Virtual asset trading platforms should have the operational capability and capacity to facilitate prompt and accurate clearance and settlement for all transactions. This should include:
 - a) the development of a system of internal accounting specifically for the safeguarding of client assets, and the reliability and security of related records;
 - b) the ability to detect any material failure, error, or defect in the operation or function of its clearing and settlement data systems;
 - c) setting out the expected settlement dates or times of transactions, which should be clearly communicated to clients;
 - d) verifying the clearing and settlement of transactions by confirming settlement details;



- e) the development and maintenance of trading systems that record key transaction details, including settlement timings and all trades concluded during the trading period;
- f) root cause analysis of failures in transactions such as incomplete settlement details for execution or insufficient account balances;
- g) the implementation of a framework ensuring delivery versus payment; and
- h) providing clients with sufficient information regarding risks and costs associated with the clearing and settlement process.

Provision of financing to purchase virtual assets (leveraged trading)

- 12.6. Virtual asset trading platforms that offer leveraged trading should have controls in place to ensure clients do not lose more than their investment and collateral held with the trading platform (negative balance protection).
- 12.7. Leveraged limits offered by virtual asset trading platforms should be prudent and correspond with the client’s experience and ability to bear losses. Excessive levels of leveraging should not be made available to clients.
- 12.8. Virtual asset trading platforms should ensure that an initial margin is maintained on the capital leveraged and that appropriate controls are established to monitor and maintain this margin as well as notifying clients of any related changes.
- 12.9. Virtual asset trading platforms should adapt limits and parameters such as stop loss orders commensurate to the products and services offered.
- 12.10. Virtual asset trading platforms should have in place a leveraged trading agreement with clients, which should include the following:
 - a) an explanation of leveraged trading and acknowledgement by the client confirming they understand the related risks and exposure;
 - b) details of the required margin;
 - c) expenses incurred by the client as part of this activity and account;
 - d) process and timings in relation to margin calls on client positions;
 - e) percentage of capital paid by the client for leveraged trading; and
 - f) any rights to recover, dispose of, or exchange virtual assets or fiat balances from client accounts.
- 12.11. A custodian or trading platform should not allow a client to have more than one leveraged trading account, or sub account.



12.12. A custodian or trading platform should conduct enhanced due diligence before allowing any client to carry out leveraged trading. This should include the following:

- a) client knowledge and experience of virtual assets and leveraged trading;
- b) client risk appetite and risk tolerance; and
- c) client financial position.

12.13. A custodian or trading platform should only accept the following as eligible collateral for leveraged trading:

- a) virtual assets; and
- b) fiat currencies.

Pricing

12.14. Virtual asset trading platforms should develop price discovery mechanisms to prevent price manipulation and any unfair trading practices. This should include a breakdown of pricing components, such as interchange rates and fees for each product and service provided. Price discovery mechanisms should include pre-trade and post-trade transparency in relation to bid and offer prices, the depth of trading interests at prices advertised on trading platforms, and volume and transaction times.

12.15. Virtual asset trading platforms should ensure effective controls are implemented to reject transactions that would exceed internal volume and price thresholds.

Listing Rules

12.16. Virtual asset trading platforms should develop procedures to list and delist virtual assets on their platforms.

12.17. Virtual asset trading platforms should consider establishing a listing committee, subject to the nature and complexity of its business. A listing committee should comprise appropriately skilled and experienced individuals, ultimately responsible for listing and delisting decisions. If the virtual asset trading platform elects not to establish a listing committee, this responsibility will remain with the governing body. The listing or delisting process should include:

- a) submission of a listing proposal or delisting request by the issuer;
- b) consideration of the listing proposal or delisting request by the listing committee or governing body. This should explore the costs, opportunities, and risks of listing the virtual asset or the consequences of any decision to delist;
- c) consideration of technical resources and capacity involved in listing the virtual asset; and

- d) the ongoing monitoring of the virtual asset once listed.

12.18. Virtual asset trading platforms should consider the following when reviewing a listing proposal or delisting request;

- a) risks relating to the listing of the virtual asset, which may include technical, operational, legal, regulatory, AML/CFT and reputational risks;
- b) other legal and regulatory obligations;
- c) details provided on the virtual asset in the form of a whitepaper or equivalent, the issuer's track record, and strategy;
- d) background information on the issuer of the virtual asset and the outcome of due diligence conducted;
- e) technical aspects of the virtual asset, including the source code, code audits, and safe storage and any relevant network security aspects; and
- f) information on the expected or current demand for the virtual asset, including details on the marketing strategy once listed.

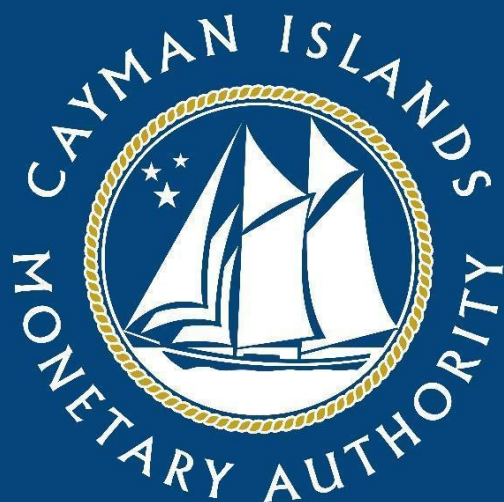
12.19. The listing committee or governing body should make a decision on the acceptance or rejection of a listing proposal or delisting request in line with specified timeframes.

12.20. Virtual asset trading platforms should make public the decision to accept a listing proposal or delisting request.

12.21. Virtual asset trading platforms should monitor listed virtual assets to ensure the listing remains compliant with regulatory obligations. This should include consideration of any significant changes to the approved listings such as adverse information or increased risk exposures.

12.22. When considering the nature and features of a virtual asset to determine whether it should be listed, a virtual asset trading platform may consider the following non-exhaustive factors:

- a) whether the technological features of the virtual asset can offer enhanced anonymity and adds hurdles to the usual customer due diligence;
- b) whether the issuer has a good reputation and whether it is well established;
- c) the liquidity of the virtual asset; and
- d) information on the technical aspects of the virtual asset such as source code and code audits, the openness and transparency of the underlying technology and network security.



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