



IN THE GRAND COURT OF THE CAYMAN ISLANDS
FINANCIAL SERVICES DIVISION

CAUSE NO. FSD OF 2023 ()

IN THE MATTER OF THE VIRTUAL ASSET (SERVICE PROVIDERS) ACT (2022 REVISION)

NEXO CAPITAL INC.

APPLICANT

THE CAYMAN ISLANDS MONETARY AUTHORITY

RESPONDENT

NOTICE OF ORIGINATING MOTION

TAKE NOTICE that the Court at the Law Courts, George Town, Grand Cayman will be moved on the day of 2023, at o'clock, or as soon thereafter as counsel can be heard, by counsel on behalf of Nexo Capital Inc. (the "**Applicant**") for:

- 1 An order under section 30(7) Virtual Asset (Service Providers) Act, 2020 (the "**Act**") that the decision made by the Cayman Islands Monetary Authority (the "**Authority**") rejecting the Applicant's application for registration as a virtual asset service provider ("**VASP**") for the purposes of the Act (the "**Refusal Decision**") be reversed.

- 2 A declaration that the Applicant is suitable to be registered under section 6(3) of the Act and an order requiring the Authority to register the Applicant as a VASP.

- 3 In the alternative, an order under section 30(7) of the Act that the Refusal Decision be reversed and remitted to the Authority for re-consideration with the opinion of the Court as to how the Authority's decision making powers should be exercised, namely that the Applicant is suitable to be registered under section 6(3) of the Act and should be so registered.

- 4 The Applicant's costs of and incidental to this application be paid by the Authority.

Background

1 The Applicant is an exempted limited company incorporated in the Cayman Islands on 2 February 2018, with registration number 332370. Its registered office is situated at Ogier Global (Cayman) Limited, 89 Nexus Way, Camana Bay.

2 The Applicant is a non-bank financial institution and one of the world's largest lending companies for overcollateralized digital asset-based credit products and provides high-yield 'Earn Interest' products which allows its customers to up certain digital assets in interest-yielding accounts. The Applicant also offers in-house, over-the-counter (OTC) desk and supplementary B2B services to its customers. The Applicant therefore provides a "virtual asset service" within the meaning defined at section 2 of Act.

3 VASP has the meaning given to it under section 3 of the Act and includes a company incorporated in the Cayman Islands who provides virtual asset service as a business, or in the course of business, in or from the Islands and *is registered or licenced in accordance with the Act*.

4 Pursuant to section 4(1) of the Act, a person shall not carry on, or purport to carry on, virtual asset service in or from the Islands unless that persons is, *inter alia*, a registered person in accordance with the Act. As such, in order act as a VASP, the Applicant was required to be registered as such in accordance with the Act.

5 The process for applying to become a registered person is set out in section 6 of the Act:

"(1) Subject to subsection (3), a person, not being an existing licensee, who — (a) at the commencement of this Act is carrying on virtual asset service for which a licence is not required under this Act; or (b) wishes to carry on virtual asset service for which a licence is not required under this Act, shall apply in the prescribed form to be a registered person under this Act and submit the application along with the prescribed assessment fee to the Authority"

(2) The Authority in determining whether to approve the application from a person in subsection (1), shall consider — (a) the matters set out in section 22...

(3) The Authority shall, further to its determination under subsection 2 that the applicant is suitable to be registered, register the applicant upon payment of the application fee

or reject the application for registration if the applicant is found to be unsuitable. (emphasis added).

- 6 On 28 January 2021 the Applicant applied to the Authority pursuant to section 6(1) of the Act. In making that application, it lodged the prescribed form as required by section 6(1) of the Act being a APP-101-84 form for registration as a VASP. In addition, it also lodged the linked AIR-157-84 AML Inherent Risk form (together, with the APP-101-84 form, the "**Application**"). The Application was lodged on the Authority's Regulatory Enhanced Electronic Forms Submission (REEFS) online platform.
- 7 On 4 February 2021, the Authority requested additional information and raised queries with respect to the information submitted by the Applicant in the Application and in the documents annexed to the Application. The Applicant promptly provided all information requested by the Authority. Furthermore, it took significant and meaningful steps to address all queries raised by the Authority, including by appointing a third party service provider to perform the role of AML officer to ensure independence from the management of the Applicant.
- 8 On 18 November 2021, the Authority requested further information and documentation with respect to the senior officers of the Applicant and requested a comprehensive business plan and transaction flowchart.
- 9 On 22 February 2022, the Authority published a notice which advised that Part XA of the Anti-Money Laundering (Amendment) (No. 2) Regulations will commence effective 1 July 2022 setting out the identification and record-keeping requirements relating to the transfer of virtual assets (the "**Notice**"). The Notice noted that Financial Action Task Force ("**FATF**") Recommendation 16 prescribes that originating virtual asset VASPs must obtain and hold required and accurate originator information along with the required beneficiary information on virtual asset transfers. The FATF Recommendation 16 also included certain requirements concerning wire transfer in the virtual asset context; such requirements being known as the "Travel Rule".
- 10 The Notice concluded by noting that "*given that Part XA of the [Anti-Money Laundering Regulations] will be effective from 1 July 2022, all VASPs registered or in the process of registering with the Authority are required to advise the Authority on how they will comply with the Travel Rule related provisions as outlined in the [Anti-Money Laundering Regulations], by submitting details of their compliance arrangements, including the relevant policies and procedures and the use of resources (including technological tools) via email to vaspinfo@cima.ky by 31 March 2022*".

- 11 The Authority consequently wrote to the Applicant on 17 March 2022 attaching a copy of the Notice and requesting the information sought therein by the specified deadline.
- 12 On 24 March 2022, the Applicant provided the Authority with the information and documents it requested on 18 November 2021.
- 13 On 8 April 2022, the Applicant also sent the Authority a copy of its Travel Rule policy; an extension of time for providing the same having previously been granted by the Authority.
- 14 Further information was subsequently sought from the Applicant by the Authority in July and August 2022 with respect to the Application and the Applicant's Travel Rule policy more specifically. This additional information was promptly provided by the Applicant.
- 15 The last request for information was made by the Authority on 18 August 2022 and was responded to by the Applicant on 24 August 2022.
- 16 Between 24 August 2022 and 4 October 2022, the Applicant received no communication from the Authority with respect to the Application.
- 17 On 4 October 2022, the Applicant wrote to the Authority requesting an update with respect to the determination of the Application.
- 18 On 14 October 2022, the Authority sent a letter (dated 13 October) to the Applicant which stated, *inter alia*:

"Further to a review of the application, the Authority became aware of certain legal and regulatory matters as noted in the news media, relating to the Applicant and other related entities, which have not been disclosed to the Authority. These matters relate to a judgement brought in 2021 relating to ownership of bitcoins and the cease-and-desist orders issued in 2022 by several US states.

In light of this, to determine the suitability of the application for registration under the VASP Act, the Authority would require further details. As such, the Authority is requiring an explanation, together with any actions the Applicant may have already taken or proposed to take. The Authority requires a response within 14 days of the date of this letter".

(the "14 October Letter")

- 19 A response to the 14 October Letter was provided by the Applicant by letter dated 25 October 2022 (sent on 26 October) which addressed the specific queries raised by the Authority in its 14 October Letter, namely an explanation of "*legal and regulatory matters*" referred to therein as well as an explanation of the actions the Application had already taken or those which it proposed to take in relation to those matters.
- 20 By letter dated 20 December 2022 (but sent to the Applicant on 23 December 2022), the Authority made the Refusal Decision and rejected the Application.
- 21 The explanation for the Refusal Decision was contained in the Authority's 20 December 2022 letter and was limited to the following:
- "...the Authority determined that the Applicant's proposed business model upon which the Application is based does not meet the required risk profile for the purposes of registration under the Act for reasons including those set out below:*
- 1. the size, scope and complexity of the Applicant's proposed business model;*
 - 2. the risk the Applicant poses to market confidence, consumer protection and the reputation of the Islands as a financial centre; deficiencies in the AML, CFT, CPF and sanctions policies and procedures relating to insufficient documentation on customer risk assessment and enterprise risk assessment to ensure adequate compliance with the said requirements;*
 - 3. failure by the directors and ultimate shareholders to disclose to the Authority the potential regulatory enforcement matters in various states in the United States and proceedings in the High Court of Justice of England & Wales; and*
 - 4. the impact the proposed product offering may have and risks it may pose to existing clients, further clients, other licensees or to the financial system of the Islands as a whole".*
- 22 The Applicant considers that the Refusal Decision is amenable to appeal and accordingly wishes to appeal the Refusal Decision to this Honourable Court pursuant to section 30(1) of the Act.

AND FURTHER TAKE NOTICE that the general grounds of this application are:

Insufficient reasons

- 1 The Authority breached its constitutional and statutory duty to provide comprehensible, satisfactory and sufficiently detailed reasons for its Refusal Decision. In particular, the Authority has acted in breach of:
 - (a) Section 6(4) of the Act which states that "*where an application for registration has not been approved, the Authority shall notify the applicant of its decision and the reasons therefor*";
 - (b) Article 19(2) of the Bill of Rights scheduled to the Cayman Constitution Order 2009 (the "**Constitution**") which states that:

"(2) Every person whose interests have been adversely affected by such a decision or act has the right to request and be given written reasons for that decision or act".

- 2 The Applicant relies on the following matters:
 - (a) The Authority has failed to notify the Applicant of the entirety of the reasons for the Refusal Decision as:
 - (i) the Refusal Decision states that, upon the Authority taking into consideration the matters set out in section 22 of the Act when reaching its decision, it has determined that the Applicant's proposed business model does not meet the required risk profile for the purposes of the Act for "*reasons including those set out below*" (emphasis added);
 - (ii) without prejudice to the Applicant's contention that certain of the matters referred to by the Authority are not properly categorised as "reasons", the clear effect of the wording utilised by the Authority in the Refusal Decision acknowledges that the Authority has only provided the Applicant with a non-exhaustive list of reasons; such that
 - (iii) the Applicant is unaware of the full reasons for the Refusal Decision but only a limited sub-set of the same;

- (b) In any event, certain of the matters referred to by the Authority in the Refusal Decision are not "reasons". Instead, they are a simple recitation of the factors prescribed by section 22 of the Act by which the Authority was required to assess the Application without any explanation of the way in which these factors have impacted the Authority's decision making. In this connection, the Applicant notes:
- (i) Reason 1 recites the factor identified at section 22(a) of the Act without more;
 - (ii) Reason 2 recites, in part, the factor identified at section 22(f) of the Act without more;
 - (iii) Reason 4 recites the factor identified at section 22(f) of the Act without more;
- (c) Further, and without prejudice to the Applicant's contention that certain of the matters referred to by the Authority are not properly categorised as "reasons", to the extent that the Refusal Decision does in fact to provide "reasons", the explanations provided are not sufficiently detailed to discharge the Authority's constitutional and/or statutory duties. In that connection, the Applicant notes:
- (i) with respect to Reason 1, the Refusal Decision does not provide an explanation of how the size, scope and complexity of the Applicant's proposed business model did not meet the Authority's criteria for registration;
 - (ii) with respect to Reason 2, the Refusal Decision fails to provide an explanation of:
 - (A) what risks it says the Applicant poses to market confidence, consumer protection and the reputation of the Islands (if any);
 - (B) what deficiencies in the AML/CFT/CPF and sanctions policies and procedures it has identified, including what was considered to be insufficient documentation on customer risk assessment and enterprise risk assessment to ensure adequate compliance with sanctions policies and procedures; and

- (C) the reasons why the extensive documentation submitted by the Applicant on risk assessment and compliance was insufficient;
 - (iii) with respect to Reason 3, the Refusal Decision fails to provide an explanation of:
 - (A) why the alleged failure of the directors and ultimate shareholders to disclose to the Authority the potential regulatory enforcement matters in the United States and proceedings in the High Court of England & Wales led to the Refusal Decision; and
 - (B) whether, and if so, why the referred to regulatory enforcement matters and proceedings were material to the Authority's decision in light of the explanations provided by the Applicant as to their nature and progress;
 - (iv) with respect to Reason 4, the Refusal Decision fails to provide an explanation of:
 - (A) what it considers the impact of the Applicant's proposed product offering to be existing clients, further clients, other licensees or the financial system of the islands as a whole; or
 - (B) what risks such an offering is said to have on existing clients, further clients, other licensees or the financial system of the islands as a whole.
- 3 In circumstances where the Applicant is adversely affected by the decision of the Authority, the Authority was obligated, having regard to its duties set out in paragraph 1 above, to not only give reasons for its findings, but sufficiently detailed and full reasons so as to allow the Applicant to properly exercise its right of appeal under section 30(1) of the Act.
- 4 In failing to do so, the Authority has breached its constitutional and statutory duties.
- 5 As a consequence, the Applicant has been prejudiced in its ability to properly plead these general grounds of appeal. As such, the Applicant reserves the right to amend its grounds of appeal pursuant to section 30(6) of the Act, Order 55, rule 6 of the Grand Court Rules or otherwise.

The Refusal Decision was irrational

- 6 The Authority had a constitutional duty, provided for by section 19(1) of the Constitution, which requires its decisions to be "*lawful, rational, proportionate and procedurally fair*".
- 7 In making the Refusal Decision, the Authority has acted in breach of both the Act and section 19(1) of the Constitution in that the Authority erred by taking into account matters which it ought not to have taken into account and/or failed to take into account matters which it ought to have.

The Authority's reliance upon the failure to disclose the potential regulatory enforcement proceedings and the proceedings in the United Kingdom is irrational

- 8 As noted above, one of only 4 matters relied upon by the Authority in refusing the Application is the omission of the Applicant to disclose various proceedings in which it was involved. However, for the reasons set out below, the Authority's reliance upon this omission was irrational.
- 9 In that connection, the relevant facts are as follows:
 - (a) Section 8(3) of the Act states:

"An application under this section shall include such information as may be prescribed and any additional information as may be specified by the Authority that enables it to make a determination and the application shall be accompanied by the prescribed assessment fee";
 - (b) Rule 4 of the Virtual Asset (Service Providers) Regulation, 2020 (the "**Regulations**") states that "*an application for registration under section 6(1) of the Law shall be made to the Authority in the form set out in Schedule 1*";
 - (c) Schedule 1 sets out a pro-forma application for registration and notes that "*All parts of this form are to be completed by applicants and shall be submitted, along with any additional information that is required, to the Authority*". Paragraph A.12 of the Regulations requires the Applicant to "*state any penalties that have been imposed or enforcement actions taken in another jurisdiction*" (emphasis);

- (d) No penalties were imposed on or enforcement actions taken against the Applicant at the time it lodged the Application and for most of the intervening period during which the Application was being determined by the Authority;
 - (e) Neither the Act nor the Regulations require the Applicant to disclose "potential regulatory enforcement matters" which the Authority refers to in the Refusal Decision; and
 - (f) Similarly, none of the Act nor the Regulations require the Applicant to disclose litigation in which it is engaged.
- 10 In circumstances where the Applicant was not under any obligation to provide the Authority with information related to, *inter alia*, the proceedings commenced against it in the High Court of England & Wales (the "**English Proceedings**"), by taking into account the alleged omission to do so, the Authority acted irrationally.

The Authority failed to take into account the materiality of the omission

- 11 Further, and without prejudice to the foregoing, in the event there was an omission, the Authority erred in failing to take into account the materiality of any such alleged omission. The purpose of any requirement to provide the Authority with the required information is to ensure that it is in possession of all information which it considers to be relevant to the Application at the time of exercising its decision making authority.
- 12 In this connection, the Authority ought to have taken into account:
- (a) When the Authority requested information regarding the various US regulatory matters and the English Proceedings in the 14 October Letter, that information was promptly provided to the Authority by the Applicant in compliance with the Regulations and section 8(3) of the Act;
 - (b) The Applicant provided a fulsome and detailed explanation of the regulatory matters and the English Proceedings upon request and the Authority has not suggested that the information provided by the Applicant in this regard was insufficient or inaccurate in any way;
 - (c) That it had the knowledge of the allegedly omitted matters, and the Applicant's explanation of them, in good time prior to the making of the Refusal Decision such that the purpose of any such requirement was satisfied; and

- (d) That the length of time of time between the issuance of the various orders in the regulatory enforcement matters (in or around 23 and 26 September 2022) and the explanation being provided by the Applicant (on 25 October 2022), was immaterial only being a matter of weeks.
- 13 Accordingly, the Authority erred by taking into account and/or placing too much weight upon the alleged omission of the Applicant in this regard.
- 14 Further, or in the alternative, the Authority erred by placing too much weight upon the existence of the regulatory enforcement matters and/or English Proceedings as the matters in question do not impact the Applicant's suitability for registration. In this regard, the following matters are noted:
- (a) The English Proceedings were commenced by HDR Global Trading Limited (trading as BitMex) against the Applicant and one of its disgruntled former employees to determine the rightful owner of an account held with BitMex. No allegations of wrong-doing were made against the Applicant in those proceedings and BitMex did not ultimately participate in the hearing before the English court;
- (b) The Applicant had been successful in the English Proceedings by a judgment handed down by Justice Henshaw on 1 July 2022 which was explained to the Authority in the Applicant's letter of 25 October 2022;
- (c) It is common for regulatory issues to arise in the context of the digital asset industry and the Applicant had assured the Authority that it has taken all necessary steps to conduct business in full compliance with the regulatory framework in every jurisdiction in which it operates;
- (d) The Applicant had diligently cooperated with all US states and federal regulatory inquiries and has been proactive in maintaining dialogue with the respective regulators;
- (e) There have been some regulatory ambiguities with respect to the laws and regulations applicable to digital assets in the US such that the fact of the regulatory enforcement itself does not connote any improper behaviour; and

- (f) The Applicant has complied with all its filings to the Financial Reporting Authority of the Cayman Islands and has engaged cooperatively with all public authorities in the Islands.

The Refusal Decision failed to take into account the statutorily required factors

- 15 The Authority has acted unlawfully and/or irrationally in that it breached section 22 of the Act by failing to take into consideration the following factors:
 - (a) The procedures that the Applicant has in place to combat money laundering, terrorist financing and proliferation financing (in breach of section 22(c) of the Act);
 - (b) The internal safeguards and data protection systems being utilised by the applicant (in breach of section 22(d) of the Act); and
 - (c) The Applicant's ability to comply with this Act and the relevant requirements of the Anti-Money Laundering Regulations (2020 Revision) (in breach of section 22(k) of the Act.

- 16 The above can be inferred from the Refusal Decision which refers to "*deficiencies in the AML, CFT, CPF and sanctions policies and procedures relating to insufficient documentation on customer risk assessment and enterprise risk assessment to ensure adequate compliance with the said requirements*" notwithstanding that the Applicant had provided extensive information with respect to the issue of compliance in support of its Application. In particular:
 - (a) The Application contained a comprehensive risk assessment, dealing in particular with capital risk, insurance risk, cybersecurity and which outlined four key pillars with respect to its AML/CTF risk mitigation;
 - (b) The Applicant provided extensive supporting documentation which was either attached to the Application or was subsequently sent to the Authority on request; and
 - (c) The Applicant addressed all issues raised in correspondence by the Authority with respect to its compliance with AML requirements, including by appointing independent AML officers in accordance with the Authority's guidance and by appointing a professional AML service provider to ensure the Applicant's compliance with the Travel Rule requirement introduced with respect to VASPs.

- 17 In addition, it is also inferred from its failure to advert to them in the Refusal Decision that the Authority failed to take into consideration the relevant matters as follows:
- (a) The knowledge, expertise and experience of the Applicant (in breach of section 22(b) of the Act);
 - (b) The net worth, capital reserves and financial stability of the Applicant (in breach of section 22(h) of the Act);
 - (c) The impact that the Applicant's virtual asset service may have on financial services in the Islands (in breach of section 22(i) of the Act);
 - (d) The likelihood that the service will promote innovation, competition and benefits to consumers (in breach of section 22(j) of the Act);
 - (e) The Applicant's senior officers and trustees are fit and proper persons to hold the respective positions (in breach of section 22(l) of the Act);
 - (f) The Applicant's beneficial owners are fit and proper persons to have such ownership or control (in breach of section 22(m) of the Act);
 - (g) The skill, knowledge and experience of the Applicant's personnel (in breach of section 8(4) of the Act);
 - (h) The extent and satisfactory nature of the Applicant's facilities, books, records and accounting systems (in breach of section 8(4) of the Act); and
 - (i) That the Applicant's capital and cybersecurity measures were in fact adequate (in breach of section 8(4) of the Act).
- 18 The Authority's failure to take into consideration the matters referred to in paragraph 17 can be inferred from the Authority's failure to refer to those matters in its Refusal Decision, particularly when having regard to the Applicant's financial position and its status as a world leading and trusted lending institution in the digital finance industry which manages assets across 200 jurisdictions worldwide.
- 19 Had the Authority taken into account all relevant factors and/or discounted all irrelevant factors, it would not have exercised its decision making powers in that manner that it did and instead would have acceded to the Application.

The Refusal Decision was procedurally unfair

- 20 The Authority acted in a procedurally improper manner and/or in breach of the principles of natural justice in that:
- (a) The Authority adopted improper delegation in the determination of the Application. In particular, the Application passed between multiple analysts since it was lodged by the Applicant in January 2021 before it finally being reassigned in an apparent portfolio re-assignment in July 2022, after most of the information requested by the Authority with respect to the Application had been provided by the Applicant and approximately 18 months after the Application had been lodged;
 - (b) This inconsistency has created prejudice to the Applicant as it prevented the Application being reviewed in a comprehensive and holistic way such that it was impossible for the Authority to fairly review the Application;
 - (c) The Refusal Decision refers to "*the size, scope and complexity of the Applicant's proposed business model*" but a "comprehensive business plan" was requested by the Authority on 18 November 2021 and provided by the Applicant on 24 March 2022. Accordingly, and without prejudice to the insufficient reasons ground referred to above, it is manifestly unfair for the Authority to have made a decision on the basis of the size, scope and complexity of a business model in circumstances where the detailed nature of the business plan provided was at the Authority's request;
 - (d) Without prejudice to the Applicant's position that there was no such omission, the Authority erred in relying upon the omission of the Applicant to refer to the potential regulatory enforcement matters in the United States and the English Proceedings (the "**Legal Matters**") as:
 - (i) the Legal Matters were first raised by the Authority in its 14 October Letter following correspondence sent by the Applicant requesting an update on the status of its Application;
 - (ii) the 14 October 2022 Letter refers to "*a judgement brought in 2021 relating to ownership of bitcoins and the cease-and-desist orders issued in 2022 by several US states*" and which simply noted that "*the Authority would require further details*" and requested "*an explanation, together*

with any actions the Applicant may have already taken or proposed to take";

- (iii) moreover, and notwithstanding the above, the Applicant provided a detailed response to the Authority on 25 October 2022. The Applicant did not subsequently receive any response from the Authority until the Refusal Decision was issued in December 2022 nor was it given any opportunity to address any concerns which remained with the Authority; and
- (iv) the Authority did not request an explanation regarding why the Legal Issues were not disclosed to the Authority in the Application and thereby deprived the Applicant of the opportunity to provide that explanation.

The Refusal Decision was unreasonable and/or disproportionate

- 21 Given the matters addressed above, the Refusal Decision was not proportionate and was not one which any reasonable authority would have reached.

Relief

- 22 It is the Applicant's case that, had the Authority acted in a manner consistent with its statutory and/or constitutional duties, it would not have refused the Application.
- 23 In the circumstances, the Applicant seeks:
- (a) An order under section 30(7) of the Act that the Refusal Decision be reversed.
 - (b) A declaration that the Applicant is suitable to be registered under section 6(3) of the Act and an order requiring the Authority to register the Applicant as a VASP.
 - (c) In the alternative, an order under section 30(7) of the Act that the Refusal Decision be reversed and remitted to the Authority for re-consideration with the opinion of the Court as to how the Authority's decision making powers should be exercised, namely that the Applicant is suitable to be registered under section 6(3) of the Act and should be so registered.
 - (d) The Applicant's costs of and incidental to this application be paid by the Authority.

24 For the avoidance of doubt, the Applicant reserves the right to amend its grounds of appeal pursuant to section 30(6) of the Act, Order 55, rule 6 of the Grand Court Rules or otherwise.

DATED this 12th day of January 2023



Ogier (Cayman) LLP

TO: The Clerk of the Court

AND TO: The Cayman Islands Monetary Authority