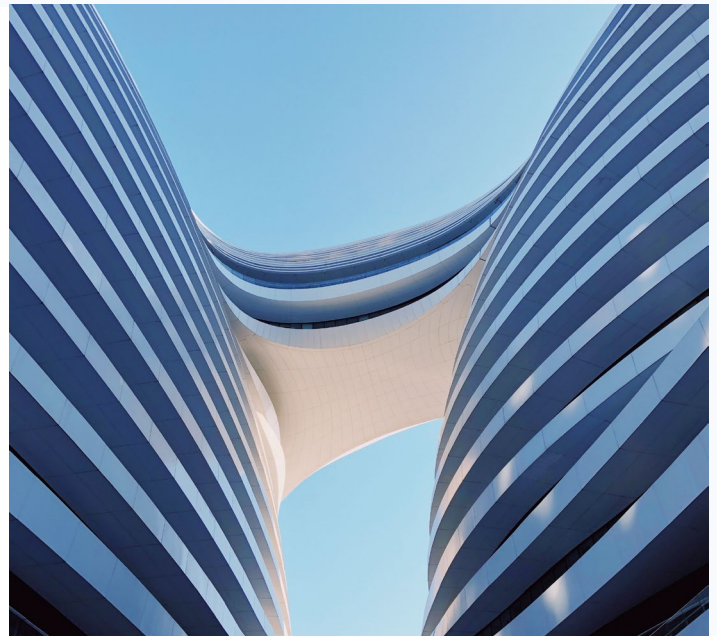


A new model of trust for crypto fund administration and custody

In this article, Vauban and Trustology explore managing the evolving landscape of crypto funds and assets and how institutional investment funds can benefit from new partnerships emerging.



A view on where we are today

In recent years, many institutional investment funds looking to place a portion of their portfolio in the uncorrelated cryptocurrency markets have been delayed in doing so due to risks from regulatory uncertainty and the technical challenges of handling a digital bearer asset. The lack of insurance, certified custodians, and the difficulty of allowing for liquidity while retaining security of the private keys has made it difficult and often illegal for them to invest their funds into cryptoassets. Added to those risks are compliance and security costs for knowing both the customer and the transaction. Compliance alone can add 5% in cost to coin acquisition, as demonstrated by the OTC markets pricing of “virgin” non-transacted coins at a premium when the miners liquidate their newly minted coins.

These costs are incurred due to regulations requiring the acquisition and protection of the individual's identifying documents, as well as paying specialists to do transaction chain analysis. The KYC documentation and the transaction history record-keeping requirements both demand strengthened cyber-security defenses, new partnerships, and new skill sets.

The responsibilities for funds to address can be categorized into either administrative or custodial concerns.

Segregation of the risks incurred by these responsibilities can be accomplished by:

- Outsourcing cryptoasset custody to an insured 3rd party that maintains control, but not “ownership” of the keys.
- Separating and outsourcing administrative and management duties to separate parties in order to segregate the governance responsibilities of the fund. For fund administrators that means addressing exactly:
 - **Who** the fund manager is
 - **What** transactions are they authorised to do
 - **What** assets will they be managing
 - **Where** the business entity is to be domiciled and using which entities for what purpose,
 - **Where** the assets are to be kept and
 - **Who** will custody those assets

Hong Kong, having chosen to make itself a leader in the crypto industry, has issued rules for crypto asset administrators, managers, and custodians, providing some of the much needed clarity that institutional crypto funds require.

The securities regulator published a 37-page document titled “Proforma Terms and Conditions for Licensed Corporations which Manage Portfolios that Invest in Virtual Assets” on October 4, 2019.

It provided detailed guidance for entities managing portfolios that invest in “virtual assets,” its term for cryptocurrencies.

In order to ensure the safety of fund assets, the SFC requires the cryptocurrency fund managers to entrust these assets to custodians that are functionally independent of said fund managers and to ensure their fund assets are segregated from their own assets.

The SFC also requires that fund administrators must securely integrate communications between themselves and their clients’ selected trading platforms and do so in a timely fashion with a verifiable audit trail. Attempting to accomplish all this by leveraging existing banking relationships has been slow, expensive, and ineffective.

A growing landscape and the challenges of existing solutions today

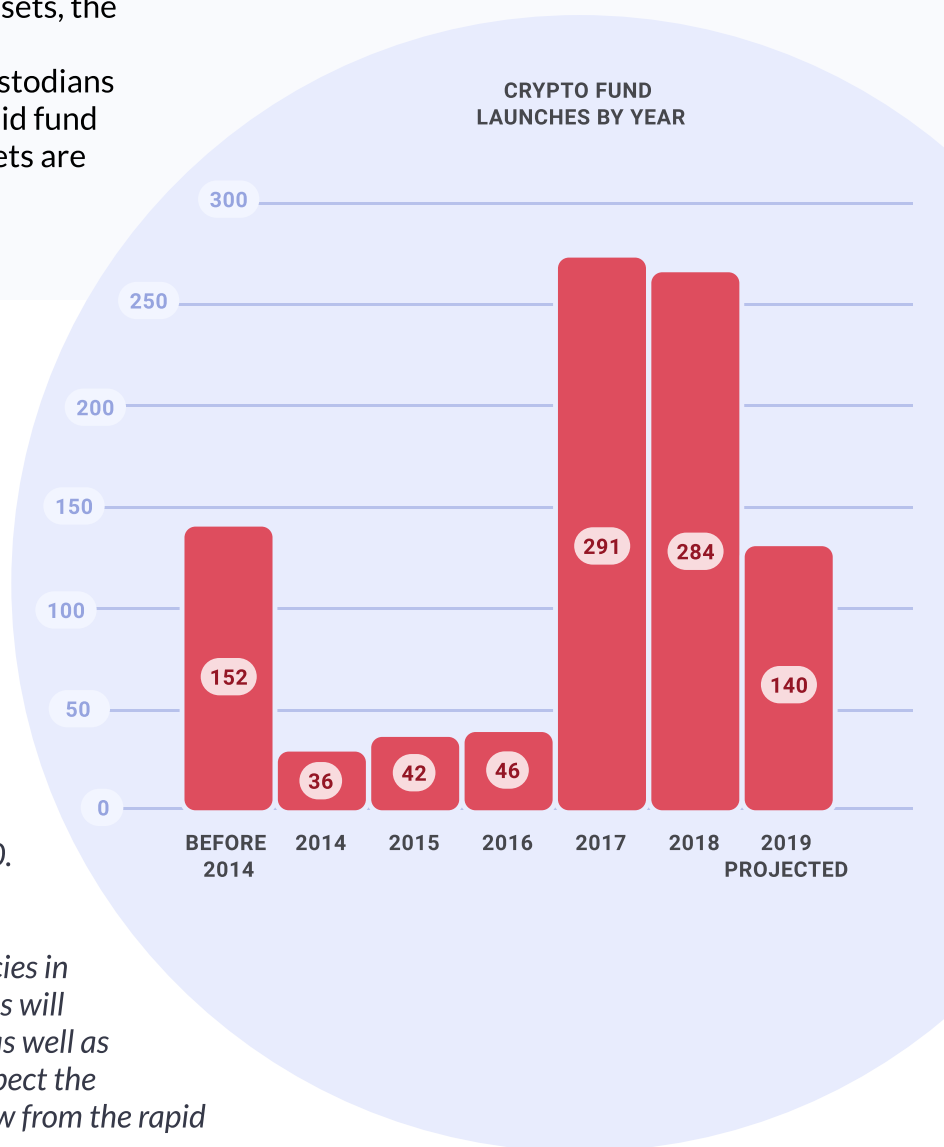
“ 2017 was a record year for the launch of new cryptocurrency funds with over 290 new funds including hedge funds and venture capital. This was more than triple the number of funds launched in 2016. 2018 sustained the high pace of new crypto funds launches seen in 2017 in terms of crypto fund launches with more than 230. In addition to the launch of new VC and crypto hedge funds, we expect existing hedge funds to incorporate cryptocurrencies in their portfolios. Likewise, existing VC firms will continue to add blockchain investments as well as launch separate blockchain funds. We expect the number of funds launched in 2019 to slow from the rapid pace in 2017 and 2018.”

Crypto Fund Research

Securing and managing cryptoassets

There are an increasing number of competing custodial models available to institutional fund managers, but securing digital bearer assets is challenging and complex. Generally, convenience and security are inversely proportional.

Acquiring fast, flexible, and easy transaction capability brings with it decreased security as accomplishing this usually requires trust in a 3rd-party, adding exposure to security sinkholes. Almost always, secure solutions are slower, more rigid in their protocols, and



more complex to use safely. Solutions that offer both are rare, and if located, are generally expensive to implement and transact with frequently.

Compromising on security in order to enable convenience has likely led to many of the recent hacks and scams experienced by several exchanges. According to Forbes, over \$4 Billion USD worth of cryptocurrency has already been stolen in 2019 alone. Hackers, malware, and exit scams are ever-present threats that few are prepared to tackle and fewer still to successfully manage. Add in market manipulation, regulatory attacks and extreme volatility, (in 2019 alone, BTC spiked over 400% from \$3,200 to \$14K & then dropped down another 50% to \$7K), along with the many competitors vying for Bitcoin's position as the preferred international reserve currency in the digital asset marketplace,

and cryptoasset fund managers and administrators have their hands full.

Strategically aligning with strong partners in the market that have the appropriate background and skill sets is essential to their survival against these types of threats.

Pricing

Crypto market prices move quickly and delays of even minutes can create opportunity costs for fund managers. Competitive fund managers must learn to take advantage of market inefficiencies and implement strategies such as cross-exchange arbitrage, integrating with exchange APIs, as well as both hedging and speculating with leverage on futures contracts or risk being left behind. Doing so with their virtual assets kept liquid, yet secure and insured remains a challenge still today.

Balancing the scales - supporting increasing institutional participation through effective partnership models

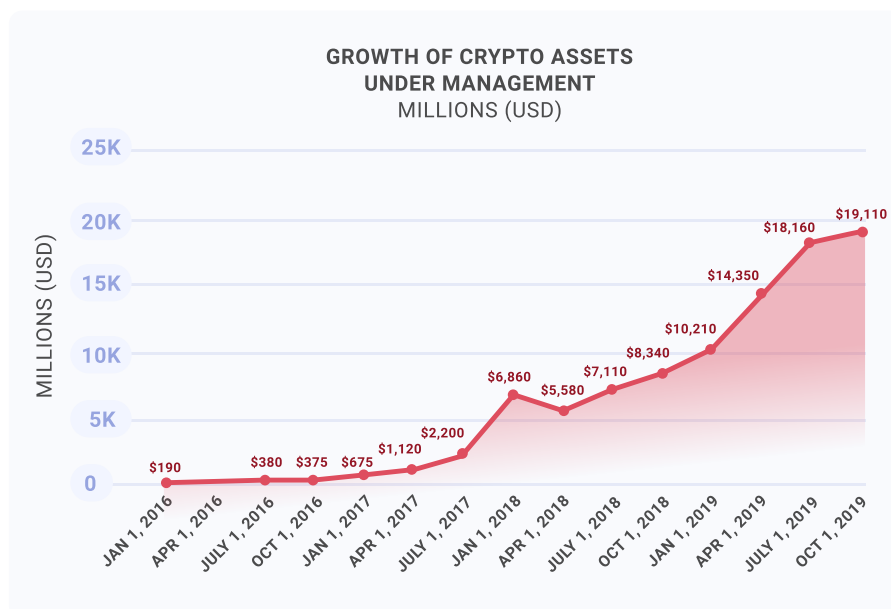
As institutional level players have entered the crypto realm, they often choose business structures that are regulated and registered, all generally requiring regular audits by independent parties. The custodial solutions they choose must have capabilities in place for confirming the location(s) of assets and its transactional history. The strategic alliance formed between Vauban and Trustology creates closed-loop coordination between cryptoasset fund administrators, Vauban, and its custodians. The tight relationship formed by this alliance increases the likelihood that acceptable audit trails will be produced, pleasing both the auditors and the regulators.

Trustology has crafted a solution that addresses a regulated institutional fund's needs for account segregation, advanced access and authorization controls, and scalability that enables arbitrage plays, high-frequency trading, and hedging / speculating with leverage, that all require fast response times, high security, and access flexibility. Trustology's solution allows for easily coordinating with developer APIs to

enable convenience and flexibility while enabling access to new tools brought by decentralised finance (DeFi) technology - the DeFi tools that are providing new solutions for borrowing, lending, and stabilizing of capital through smart contracts.

Vauban offers complex fund structuring services that can be implemented quickly - with legal documentation done in a day - and delivering standalone fund structures within 4-6 weeks. They have expertise in integrating fund accounts with derivative exchange accounts to enable access to futures markets. They were the first Fund Administrator to establish full connectivity with Crypto Facilities, now Kraken Futures. Vauban is a crypto-native fund administrator that allows for funds to implement a range of strategies, i.e. cross-exchange arbitrage, high-frequency trading, leveraged futures speculation, and more. With Vauban now supporting 110 exchanges and OTC desks, an alliance with Trustology's secure, insured, and flexible custodial wallet solution makes a seamless integration between the crypto fund administrator and custodian possible.

“The overall crypto fund industry has been growing rapidly. Changes in assets are a result of three primary factors: the launching of new crypto funds, net inflows to existing funds, and changes in the value of portfolio assets. The latter factor was particularly prevalent in the last half of 2017 when Bitcoin, for example, increased in value nearly fourfold. Prices for leading cryptocurrencies fell sharply in 2018. Despite this, the growth of new funds and fund inflows contributed to rising AUM for the crypto fund industry as a whole.”



Crypto Fund Research

Concluding thoughts

Crypto fund managers can be confident that, through this partnership, they can comply with all applicable regulations while also utilising streamlined services that scale providing flexibility in day-to-day operations that is essential in a quickly evolving marketplace. Through a dedicated custodian such as Trustology, there is separation and segregation at the execution level for better governance and ensuring less risk.

Equally, leveraging Vauban's fund services platform provides the ability to both setup and administer a fund with ease.

This strategic alliance between these crypto powerhouses is still in development. Any and all that would like to see this coordinated solution brought to the crypto marketplace should reach out directly to both platforms via the contact details below.



Contact Us: hello@vauban.io

The Vauban platform gives our users the chance to set up and administer a range of funds and investment vehicles entirely online - saving time, effort and money.



Trustology

Contact us: info@trustology.io

Trustology's vision is to create the most compelling cryptoassets company of the 21st century. Our first focus has been securing and managing cryptoassets with our TrustVault platform technology.

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