

Scaling alternatives with tokenised fund structures

Tokenisation has moved from pilots to production for investment funds. Leading commentators are predicting that tokenisation of real world assets will quickly scale to a multi-trillion market by 2030. Asset managers now issue and service funds on distributed ledger technology (DLT), shortening settlement, opening new distribution, and delivering real-time transparency and automation. Money market funds lead, with tokenised share classes and on-chain wrappers live across Europe, the US, and Asia. We are also seeing rising interest in the tokenised ETF space, with industry players actively exploring the area. It is clear that tokenising ETFs will be game-changing for the funds industry. The next wave – alternatives – will use tokenisation to lower minimums, streamline capital flows, enable controlled secondary liquidity, and encode any required access and transfer restrictions. As legal frameworks and standards mature, the priority is safe scale, near-term value, strong governance, custody, and interoperability.

Opportunities: Efficiency, liquidity and new market access

Tokenised funds create a single, secure ownership ledger, cutting reconciliation, operational risk, and duplicative infrastructure. Smart contracts automate corporate actions, distributions, and eligibility controls to improve accuracy and reduce costs.

Liquidity and access are enhanced through intraday settlement that reduces counterparty risk and releases trapped collateral and treasury capital, and through fractionalisation and 24/7 transfer that broaden distribution while permissioned networks preserve investor protections. For alternative investment funds, fractionalisation widens the investor base.

Tokenised funds are more than digital wrappers and can become connective tissue across modernised market rails. These can be used as collateral, composed with tokenised treasuries and deposits, and reconciled in real time by regulators and service providers. Institutions that align issuance, custody and settlement across digital and traditional rails are already reporting measurable operational gains.

Challenges: Interoperability, liquidity formation and operating risk

Growth is constrained by fragmented platforms, thin liquidity, and poor interoperability. Most systems operate in silos without standards for cross chain settlement, wallet portability, or common data formats. Secondary trading is rising but remains sparse outside permissioned networks, limiting, to some extent, scalability and optimum liquidity for digitally native regulated funds. Ensuring that current anti-money laundering and countering the financing of



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terrorism (AML) and sanctions rules which impose 'know your client' (KYC) requirements on funds and managers, can be met on permissionless networks is a distinct challenge. The task will be to reconcile onboarding, verification and approvals with the open infrastructure of a truly permissionless DLT.

From an operational perspective, operational resilience and security considerations differ for a fully on-chain model. For example, institutions will need to have the infrastructure to ensure enterprise grade wallet security, key management, smart contract governance, and cyber resilience. Dual running on and off chain books requires rigorous three way reconciliation. DORA style expectations, outsourcing oversight, and code audits demand disciplined governance. On-chain AML is viable, but identity and data subject rights must remain compliant with GDPR and the principles of data minimisation especially considering the use of immutable ledgers, which are unchangeable once recorded.

Alternatives add complexity; valuing hard to price assets; encoding side letters and transfer rights; managing capital calls, defaults, and cross fund set offs; tax across feeder/parallel structures; and custody/control of assets and digital LP records. Liquidity for fund tokens should favour controlled venues and periodic windows over continuous trading. For products that maintain a bucket of liquid assets to provide liquidity, redemptions should be from that bucket.

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Legal and regulatory considerations in key funds jurisdictions

Some of the same key issues and priorities emerge across jurisdictions and regulators. For example, it is important to ensure legal certainty for on-chain ownership, transfers, settlement finality, collateral perfection, and to have certainty around rights and outcomes in an insolvency event. Aligning permissioned public, private, and institutional networks with applicable prudential and conduct requirements will also be key to prevent fragmentation, especially for settlement and custody. Another area of discussion has been whether an industry standard will emerge for smart contracts to allow for optimal interoperability and efficiency for full transactions, and how data protection and privacy requirements will be integrated into the DLT. Clear rules on tokenised LP interests, transfer restrictions, recognition of on-chain registers, and enforceability of digital waterfalls and side letters will also be important. Finally, with the advent of DLT, it is essential that the technology used fully facilitates compliance with AML requirements. Given the increased cybersecurity risk inherent to tokenisation, this consideration must be heavily scrutinised.

- **The European Union.** Across the EU, tokenised fund shares that qualify as financial instruments generally fall within the MiFID, UCITS, or AIFMD frameworks. The EU recognises DLT-based issuance, account-keeping, and settlement through pilot regimes, and several Member States have updated securities laws to accommodate DLT registries and dematerialised issuance. The European Commission is actively preparing for tokenisation, and it is expected that their upcoming proposals for the Savings and Investment Union will include elements on tokenisation, while also supporting initiatives like the EU Blockchain Sandbox to foster innovation. In Ireland, tokenisation models are being mapped to existing fund legal requirements, to allow for on-chain registers, intraday transfers,

and record location rules. In Luxembourg, successive “Blockchain laws” have provided a specific legal framework to issue, distribute, hold, and manage native tokenised funds, including introducing a new control-agent concept to add an additional layer of security and oversight to Luxembourg tokenised funds.

- Cayman Islands.** The Cayman Islands’ Virtual Asset (Service Providers) Act (2024 Revision) (the “VASP Act”) establishes a registration and licensing regime for virtual asset service providers, with the licensing phase for custodians and trading platforms effective from 1 April 2025. Under the VASP Act, activities such as exchange, transfer, custody and participation in, or provision of, financial services related to a virtual asset issuance are regulated. Whether tokenised funds fall within the VASP perimeter is fact specific: Cayman Islands private funds and mutual funds continue to be regulated primarily under the Private Funds Act and Mutual Funds Act, with tokenisation typically addressed through constitutional/documentary updates and operational controls. However, where a fund (or its service providers) conducts a “virtual asset service” (for example, issuing freely transferable tokens to the public, operating a transfer function akin to an exchange, or providing custody of investors’ tokens), VASP registration or licensing and CIMA engagement will be required. Issuers must also consider the Securities Investment Business Act for any dealing/arranging activities involving security tokens. For alternatives, common structures (exempted companies and exempted limited partnerships) support tokenised feeders and closed ended vehicles, but sponsors should calibrate transfer restrictions, secondary windows and AML/KYC checks to align with the terms of offering documents and Cayman Islands AML rules. In August this year, the Ministry of Financial Services and Commerce released a Consultation Paper setting out various proposed amendments specifically for tokenised funds. For example, under the proposals, tokenised funds would be required to keep clear, complete records of how their digital equity or investment tokens are created, sold, transferred and owned; be able to show these records to CIMA on request within 24 hours; have appropriate skills, knowledge and experience to operate the fund properly; maintain enough capital and have strong cybersecurity measures in place; and comply with certain audit requirements. The industry is awaiting the outcome of the consultation process.
- British Virgin Islands.** The British Virgin Islands Virtual Assets Service Providers Act, 2022 (as amended) requires VASPs carrying on business in or from within the British Virgin Islands to be registered with the FSC for activities including exchange, transfer, safekeeping/custody and administration of virtual assets, and participation in or provision of financial services related to an issuer’s offer or sale of a virtual asset. Tokenised funds are generally structured within existing British Virgin Islands fund regimes under the Securities and Investment Business Act and Mutual Funds Regulations (e.g., approved, incubator, professional or private funds), with the tokenisation layer addressed in the fund documents and transfer agency operations. VASP registration may be triggered where the fund, manager or an affiliate provides a regulated virtual asset service (for example, operating an issuance portal, on-chain transfer function, or custody). As in the Cayman Islands, analysis is case by case. Alternatives sponsors should ensure side letter mechanics, transfer restrictions and investor eligibility are enforceable at the token level, and that British Virgin Islands AML, Travel Rule and data handling requirements are embedded in onboarding and wallet controls.
- Jersey.** Jersey became the first jurisdiction to approve a regulated Bitcoin investment fund in 2014. Since then, the Jersey Financial Services Commission published guidance in 2024 that provides clear, proportionate pathways for asset tokenisation. Requirements generally include having a Jersey-incorporated issuer (company or LLC), appointing appropriate corporate services providers and custodians, having a Jersey-resident director, applying AML controls, issuing risk warnings and transparency and investor disclosure requirements, requirements for underlying assets to be verified by a qualified third party and for smart contract audits, with related reporting obligations.

Emerging best practices

A resilient model brings together a permissioned token on institutional-grade infrastructure, an approved list of investors matched to a verified register, and programmable transfer rules aligned with the fund's prospectus and target market. Transfer agency can be operated in parallel with existing systems or built natively on-chain, with an immutable audit trail for transparency.

Custody arrangements for investors should accommodate investors who wish to self-custody in their existing wallet, or alternatively, institutional custody arranged for the investor, supported by a robust oversight infrastructure. The cash leg of transactions is often raised as an issue to the scalability and interoperability of tokenised funds with the broader / traditional financial system so the cash leg of subscriptions and redemption will need to evolve to digital cash—such as stablecoins or tokenised bank deposits—to enable atomic delivery-versus-payment. Governance should include rigorous code audits, formal change controls, clear incident-response processes and human-in-the-loop safeguards for exceptions.

For alternatives, “good” also means tokenised capital call notices and payment rails; encoded distribution waterfalls with testable models and off-chain oversight; side letter terms reflected in token permissions; periodic transfer windows and price discovery mechanisms on regulated venues; and audit-ready connections between underlying asset data—such as loan tapes and leases—and NAV and oracle inputs.