

Guidance Note

Private Funds Bill, 2020 & Mutual Funds
(Amendment) Bill, 2020

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Introduction

On 8 January 2020, the Government of the Cayman Islands published a draft Private Funds Bill, 2020 (the “**Private Funds Bill**”) and simultaneously a draft Mutual Funds (Amendment) Bill, 2020 (the “**Mutual Funds Bill**”) and together with the Private Funds Bill the “**Bills**”).

The Bills act together to provide for the registration of closed-ended and exempted funds with the Cayman Islands Monetary Authority (the “**Authority**”) and to impose extended administrative and operational requirements upon previously exempted funds. The Bills are published as a response to EU and other international recommendations and are drafted on a similar basis as several other jurisdictions.

The Private Funds Bill 2020

A “*private fund*” is defined as a company, unit trust or partnership whose principal business is the offering and issuing of its investment interests, the purpose or effect of which is the pooling of investor funds with the aim of spreading investment risks and enabling investors to receive profits or gains from such entity’s acquisition, holding, management or disposal of investments, where:

- a) the investors do not have day-to-day control over the acquisition, holding, management or disposal of the investments; and
- b) the investments are managed as a whole by or on behalf of the operator of the private fund, directly or indirectly, for reward based on the assets, profits or gains of the vehicle.

REGISTRATION PROCESS

The Private Funds Bill sets out a registration process for private funds which involves the filing of prescribed details with the Authority and payment of an annual fee. The Private Funds Bill does not require the filing of a full offering memorandum (or similar) in relation to a private fund or impose any requirements on the contents of a private fund’s offering materials (if any). Where a private fund (a) makes any changes, or becomes aware of any changes, that materially affects any information submitted to the Authority under the provisions of the Private Funds Bill; or (b) changes its registered office or the location of its principal office, the private fund shall within twenty-one days after making the change or becoming aware of the change, as the case may be, file with the Authority the details of the changes.

The Private Funds Bill also includes provisions relating to a private fund being able to elect to be registered as a ‘restricted scope private fund’, although no further details on this are set out in the Private Funds Bill.

TIMING FOR THE REGISTRATION OF NEW PRIVATE FUNDS

A new private fund which is covered by the Private Funds Bill must submit its registration application to the Authority within 21 days after its acceptance of capital commitments from investors for the purposes of investments and be registered by the Authority before it accepts capital contributions from investors in respect of investments.

Oral or written communications and agreements can be entered into with potential investors who are high net worth persons or sophisticated persons prior to the new private fund's registration application being filed with the Authority.

The Private Funds Bill does not set out the timing for the registration of existing private funds but we expect they will be given a longer period of time to comply with the registration process.

OPERATING CONDITIONS FOR PRIVATE FUNDS

The Private Funds Bill requires a private fund to ensure it has certain ongoing operating provisions in place relating to annual audits, annual returns, retention of records, valuation of assets, safekeeping of fund assets, cash monitoring and identification of securities which can be summarised as follows:

Annual Audit of Private Fund

A private fund shall have its accounts audited annually by an auditor approved by the Authority. Accounts will need to be prepared in accordance with International Financial Reporting Standards or the generally accepted accounting principles of the United States of America, Japan or Switzerland or any non-high-risk jurisdiction. The Private Funds Bill is not clear as to whether accounts for past financial years will require audit.

Annual Return

A private fund will, in respect of each financial year of the private fund, be required to submit an annual return in the prescribed form. This form is yet to be published.

Retention of Records

A private fund shall maintain its records in an accessible manner and in accordance with rules, statements of principle and guidance issued by the Authority under section 34 of the Monetary Authority Law (2018 Revision). This requirement includes an obligation to maintain a record of the identification codes of any securities that are regularly traded or held on a consistent basis.

Valuation

A private fund shall have appropriate and consistent procedures for the purposes of proper valuations of its assets, which shall ensure that valuations are conducted in accordance with the requirements in the Private Funds Bill. Valuations of the assets of a private fund shall be carried out at a frequency that is appropriate to the assets held by the private fund and, in any case, on at least an annual basis.

Valuations of the assets of a private fund shall be performed by (a) an independent third party that is appropriately professionally qualified to conduct valuations in a non-high-risk jurisdiction or (b) the manager or operator of the private fund, or a person who has a "control relationship" with the manager of the private fund. If the valuation is undertaken by the latter of these options then it must be independent from the portfolio management function and potential conflicts of interest must be properly identified, managed and disclosed to investors. Alternatively, the valuation function could be undertaken by an administrator not falling under option (a) who is appointed by the private fund.



Private Funds & Mutual Funds (Amendment) Bill, 2020

Safekeeping of Fund Assets

A private fund shall appoint a custodian to hold in custody, in segregated accounts opened in the name, or for the account, of the private fund, the custodial fund assets and verify, that the private fund holds title to any other fund assets and maintain a record of those other fund assets.

A private fund is not required to appoint a custodian if it notifies the Authority that it is neither practical nor proportionate to do so, having regard to the nature of the private fund and the type of assets it holds.

In this scenario the private fund shall appoint either an administrator or another independent third party or the manager or operator, or a person with a control relationship with the manager of the private fund, provided that the verification function is kept separate and conflicts of interest are identified and managed in the same way that the valuation function is administered as set out above.

Cash Monitoring

The Private Funds Bill requires that monitoring of cash flows and checking of cash accounts and receipt of investor payments be carried out by any of the manager or operator of the private fund (subject to functional independence or conflicts management requirements), an independent administrator, independent custodian or other independent third party.

The Private Funds Bill will continue to be reviewed and the details in the Private Funds Bill remain subject to change.

The Mutual Funds (Amendment) Bill, 2020

The Mutual Funds Bill amends the Mutual Funds Law (2019 Revision). The primary effect of the changes is to bring within the scope of regulation, funds with 15 or fewer investors who have the ability to appoint or remove the operator of the fund; these funds are currently referred to as "exempted funds" or "section 4(4) funds".

The Mutual Funds Bill will impose upon section 4(4) funds many of the same requirements that the Private Funds Bill will impose upon private funds. Section 4(4) funds will be required to register with the Authority in the prescribed form, pay an annual registration fee, submit annual audited accounts audited by a Cayman Islands based auditor (and prepared in the same manner as those required under the Private Funds Bill) and annual returns, inform the Authority of material changes to the information submitted as part of its registration application and retain appropriate accessible records.

A certified copy of an extract of the relevant fund's constitutional documents will need to be filed with the Authority showing that a majority in number of its investors are capable of appointing or removing the operator of the fund.

Existing section 4(4) funds will need to complete the registration, and comply with the new requirements, set out in the Mutual Funds Bill within six months of the date on which the Mutual Funds Bill becomes law. We expect to see further guidance on both Bills, including as to any exemptions that may become available.



Private Funds & Mutual Funds (Amendment) Bill, 2020

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This publication is for general guidance and is not intended to be a substitute for specific legal advice. Specialist advice should be sought about specific circumstances. If you would like further information, please contact:

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