COLLAS CRILL

Private Funds Bill 2020

JANUARY 2020

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On 8 January 2020 the Cayman Islands published draft legislation named the Private Funds Bill (the '**Bill**'). The Bill sets out requirements for the registration of closed ended funds with the Cayman Islands Monetary Authority ('**CIMA**'), bringing closed ended funds within the scope of a regulatory regime for the first time in this jurisdiction.

The publication of the Bill stems from the Cayman Islands' commitment to strengthen investor confidence, ensure jurisdictional dominance for fund formation and to comply with the EU's recommendations on the oversight of investment funds.

The Bill will be considered by the Cayman Islands Legislative Assembly on 30 January 2020 and, thereafter, drafted into law. The requirements set out in the Bill will be implemented by way of additional regulations and guidance.

We set out below the key features of the Bill. As the Bill has not yet become law, the information set out here is subject to change.

Which Funds come under the scope of the Bill?

The majority of closed-ended funds with more than one investor are likely to come within the scope of the bill. Specifically, the Bill applies to 'private funds'. A fund is a 'private fund' if:

- it has been structured as a Cayman Islands company, unit trust or partnership;
- its principal business is offering and issuing investment interests, the purpose or effect of which is the pooling of investor funds with the aim of spreading investment risk and enabling investors to receive profits or gains from the fund's acquisition, holding, management or disposal of investments;
- its investment interests are not redeemable at the option of the investor;
- its investors do not have day to day control over the acquisition, holding, management or disposal of the fund's investments;
- its investments are managed as a whole by or on behalf of its operator, directly or indirectly, for reward based on the assets, profits or gains of the fund.

Non Cayman Islands 'private funds' are also captured by the Bill, if they invite the public in the Cayman Islands to subscribe for investment interests.

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Carve Outs

The Bill helpfully excludes several 'non fund' arrangements from its scope. An example of some of the 'non fund' arrangements which are specifically excluded from the Bill are:

- securitization special purpose vehicles;
- joint ventures;
- proprietary vehicles;
- holding vehicles;
- individual investment management arrangements;
- debt issuing vehicles;
- structured finance vehicles;
- employee incentive schemes (or similar);
- sovereign wealth funds; and
- single family offices.

A full list of the 'non fund' arrangements is set out in the schedule to the Bill, which can be found here.

Registration with CIMA

Under the Bill, newly established private funds will be required to submit an application to register with CIMA within 21 days after it accepts capital commitments from investors.

The Bill does not give an indication of the time frame by which existing private funds will need to register with CIMA. It is expected that additional regulations and guidance will provide existing private funds with a transitional period, during which they will be required to register with CIMA, and comply with any other relevant requirements.

A private fund may not accept capital contributions from investors until it is registered by CIMA.

However, quite helpfully, a private fund may engage in oral or written communications and enter into agreements with potential investors who are high net worth persons or sophisticated persons prior to the submission of its registration application to CIMA.

In order to apply to be registered with CIMA, a private fund will need to submit specific information and documentation. Exactly what each fund is required to submit will be confirmed by CIMA in due course.

Once CIMA receives a complete application from a fund, it will consider the application and register the fund once satisfied. The Bill sets out that CIMA will communicate its decision to register a fund as soon as reasonably practicable after its review of the application.

Ongoing Obligations

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A summary of the ongoing obligations of a registered private fund are set out below:

- Valuations: private funds must have appropriate and consistent procedures for the proper valuation of its assets. Valuations must be carried out at least once a year. Valuations must be carried out by an independent third party, an administrator or the manager or operator of the fund provided the valuation function is independent of the management function or that potential conflicts of interest are properly identified, managed, monitored and disclosed to investors.
- Safekeeping: private funds must appoint a custodian to hold the custodial fund assets. The custodian must verify that the fund holds title to any other fund assets and maintain a record of those assets. A fund may notify CIMA that it is neither practical nor proportionate to appoint a custodian having regard to the nature of the assets which it holds. In this case, the fund must appoint an independent third party or the manager or operator of the fund to carry out the title verification function. If this function is carried out by the manager or operator, it must be independent from the portfolio management function and potential conflicts of interest must be properly identified, managed, monitored and disclosed to investors.
- Cash Monitoring: private funds must appoint a person to monitor its cash flow, ensure all cash has been booked in cash accounts opened in the name, or for the account of, the private fund and ensure that all payments made by investors have been received. An independent third party may be appointed to perform this role. The manager or operator of the fund may also be appointed provided this function is independent of the management function or that potential conflicts of interest are properly identified, managed, monitored and disclosed to investors.
- Identification of Securities: private funds which regularly trade securities or hold them on a consistent basis must maintain a record of the identification codes of the securities it trades and holds. This information must be made available to CIMA upon request.
- Annual Fee: an annual fee must be paid to CIMA by 15 January of each year. The exact fee amount has not yet been confirmed;
- Annual Return: a private fund will need to submit an annual return to CIMA in respect of each financial year.
- Inform CIMA of Changes: details of any changes to the fund which materially effect the information submitted upon the fund's initial registration must be submitted to CIMA within 21 days; and
- Accounts and Audit: private funds will need to prepare accounts in accordance with the International Financial Reporting Standards or generally accepted accounting principles of the United States of America, Japan, Switzerland or a non-high risk jurisdiction and an audited set of accounts must be filed with CIMA within six months of the fund's year end. The audit will need to be undertaken by a Cayman Islands auditor approved by CIMA.

Pre-existing Ongoing Obligations

In addition to the new obligations proposed by the Private Funds Bill, operators of closed ended funds should be aware of the pre-existing continuing obligations that closed ended funds are subject to

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- Anti-money laundering: closed ended funds are subject to the requirements of the Anti-money Laundering Regulations (as amended) and will usually either delegate anti-money laundering functions to a service provider or rely on the manager or administrator to perform the functions. Closed-ended funds are also required to appoint natural persons to the roles of Anti-money Laundering Compliance Officer, Money Laundering Reporting Officer (MLRO) and Deputy MLRO.
- Automatic Exchange of Information: all closed ended funds should already be complying with their reporting obligations under the Foreign account Tax Compliance Act ('**FATCA**') and the Common Reporting Standards ('**CRS**') which require the collection and reporting of financial account information in relation to investors.
- Data Protection: closed ended funds and their functionaries and service providers are data controllers or data processors under the Data Protection Law ('**DPL**') and must ensure that they are handling personal data in relation to investors and employees in accordance with the DPL.

Supervision and Enforcement

The Bill provides CIMA with new supervisory and enforcement powers to ensure the requirements of the Bill are complied with. For example, if CIMA deems it necessary to comply with its functions under the Bill, it may request additional information from a fund, carry out on site inspections, impose additional conditions or apply to Court for an order to take any action it deems necessary to protect the interests of the investors. Failure to comply with the provisions of the Bill may result in the imposition of fines on a fund and / or its operators.

Contact

We will make sure to keep you informed of any updates relating to the implementation of the Bill.

If you would like any additional information, your usual Collas Crill contact, or any of the contacts listed here, would be happy to speak with you.

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