

Client Update

Cayman Islands Master Funds – New Registration Requirements

22 December 2011

Executive summary

On 22 December 2011, the Cayman Islands introduced legislation to widen the range of master funds that are required to register with the Cayman Islands Monetary Authority (“CIMA”). The affected funds that are now required to register are open-ended funds which have a CIMA regulated fund as an investor, where the regulated fund conducts 51% or more of its investing through another fund.

The new legislation does not impact closed-ended funds or funds for a single investor.

Timeline

The amendments to the Cayman Islands Mutual Funds Law came into force on 22 December 2011. Any new affected fund will need to comply with the amended law immediately. Existing funds will have a 90 day grace period (which is subject to possible extension by government regulation).

The change to the earlier law

Under the Mutual Funds Law, unless an exemption applies, funds that are formed (or make a public offer) in the Cayman Islands which offer equity interests redeemable at the option of an investor are required to register with CIMA.

Prior to the amendment of the Mutual Funds Law, an exemption from registration applied to any fund with fifteen or fewer investors where those investors have certain powers of control over the operation of the fund (the “**15 Investors Exemption**”). The amendment to the law has effectively narrowed the 15 Investors Exemption with the result that many funds that operate as a master fund within a typical “master-feeder” fund structure will now be required to register with CIMA.

Identification of affected master funds

In summary, the Mutual Funds Law defines the affected master funds that are now required to register with CIMA to be funds that:

- are formed in the Cayman Islands;

- offer equity interests redeemable at the option of the investors;
- have one or more “regulated feeder funds” as investors; and
- have (or intend to have) more than one investor.

A “regulated feeder fund” is a fund regulated by CIMA that “conducts more than 51% of its investing through another mutual fund”.

Application to typical structures

In the case of a typical “master-feeder” fund structure, there are two principal outcomes:

- where the feeder fund is registered with CIMA, the master fund will now be required to register with CIMA; and
- where the feeder fund is not registered with CIMA (e.g. in reliance upon the 15 Investors Exemption), then the master fund may rely on the 15 Investors Exemption and thus also avoid registration with CIMA.

It should be noted that under the new provisions:

- there is no requirement that the master fund and feeder fund are under common or affiliated management;
- there is no clarification of when or how the 51% test is applied, for example in the case of a fund with fluctuating allocations or in the case of an umbrella fund;
- the legislation does not expressly link a feeder fund to a single master fund (and accordingly a feeder fund could conceivably “trigger” several investee master funds into a registration requirement); and
- a regulated fund could conceivably be considered a regulated feeder fund if it invests more than 51% of its assets in a foreign mutual fund.

Accordingly, careful analysis will be required for any case of potential doubt.

Registration requirements for affected master funds

Affected master funds will need to register with CIMA. Assuming the minimum investment level for each investor in the fund exceeds US\$100,000, the procedure will be similar to most fund registrations, though with some streamlining where there is an overlap with the filings made in respect of the feeder fund. The principal requirements will be:

- payment of the initial and annual fees;
- initial filing of letters of consent from the auditor (who must be a Cayman Islands auditor) and the administrator of the fund;
- initial filing of a copy of the certificate of incorporation or registration for the fund;
- annual filing of locally audited accounts (and related annual review information); and
- initial filing and ongoing maintenance with CIMA of limited registered particulars concerning the master fund and, if one has been prepared, any offering document for the master fund.

An application for registration will not entail a substantive review of the fund's terms by CIMA, and registration should be automatic upon submission of a completed application. It is envisaged by the legislation that CIMA will not require a master fund to produce a separate offering memorandum.

Registered master funds will be subject to the full provisions of the Mutual Funds Law, including the supervisory powers of CIMA and the whistle blowing obligation upon the fund's auditors.

The initial and annual fee for a registered master fund is US\$3,048 (which is less than the rate of US\$3,658 applicable to other kinds of registered fund). Given the slightly reduced fees, we expect master funds that have previously registered under the Mutual Funds Law (for example where

the 15 Investors Exemption was not available) may choose to re-register under the new regime.

If an affected master fund cannot observe the minimum investment level of US\$100,000 for each investor (for example, due to having existing small investments into the fund), then alternative compliance with the Mutual Funds Law may be required, such as direct substantive licensing from CIMA or by appointing a local administrator that assumes specified supervisory responsibilities.

No impact on closed ended funds, single investor funds or wholly unregistered "master-feeder" fund structures

The following exceptions from registration under the Mutual Funds Law continue to apply:

- closed ended funds (i.e. funds which do not offer investors a right to redeem their interests) are not required to register;
- funds for a single investor are not required to register; and
- "master-feeder" fund structures where both the master fund and the feeder fund rely on the 15 Investors Exemption are not required to register.

Next steps

Operators of Cayman Islands funds should contact their legal advisers to assess the legal and business impact of the amendments to the Mutual Funds Law on them. A number of master funds will now require registration or restructuring with consequent amendment to their offering and constitutional documentation. Operators of unregistered Cayman Islands funds may need to review their investor bases and consider procedures to monitor (and, as necessary, assess powers to exclude) investment by Cayman Islands registered feeder funds.

This memorandum is intended to provide only general information for the clients and professional contacts of Travers Thorp Alberga. It does not purport to be comprehensive or to render legal advice. Please do not hesitate to contact us at any time if you have any specific questions or would like more detail on any of the points made in this memorandum. Our contact details are set out below.

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