

Client Update



Cayman Islands Funds - Expanded Master Fund Registration Regime

15 January 2013

Executive summary

The Cayman Islands has recently introduced amendments to the Mutual Funds Law (the "Law") which require the registration of certain trading subsidiaries of registered funds as "master funds".

Closed ended funds are unaffected by these changes and remain outside of the Law.

Recent amendments also increase the fees applicable to registered mutual funds, other than master funds.

Timeline

The amendments to the Law came into force on 10 January 2013 with fee regulations issued on 15 January 2013. Pursuant to a recent governmental advisory, existing master funds affected by the amendments to the Law have a grace period until 1 March 2013 in which to comply.

Summary of the Law

Under the Law, pooled funds that are formed (or carry on business) in the Cayman Islands which offer equity interests redeemable at the option of an investor are classified as "mutual funds". This definition captures collective investment schemes whether formed as companies, partnerships or trusts.

Mutual funds are required to register with the Cayman Islands Monetary Authority ("CIMA") unless an exemption applies. A fund that is registered with CIMA is referred to as a "regulated mutual fund". Historically an exemption from registration was applicable 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**"). However now certain "master funds" may not rely upon the 15 Investors Exemption and must register under the Law.

By this amendment, the definition of a "master fund" has been expanded to include certain trading subsidiaries of regulated mutual funds.

Identification of master funds

In summary, the new Law defines a "master fund" to be a company, partnership or trust that is held by a "regulated feeder fund". A "regulated feeder fund" is

a regulated mutual fund that "conducts more than 51% of its investing in a master fund or through an intermediary entity". In addition the master fund must:

- be formed in the Cayman Islands;
- offer equity interests redeemable at the option of the holder;
- hold investments and conduct trading for the principal purpose of implementing the overall investment strategy of a regulated feeder fund; and
- have one or more regulated feeder funds directly or through an intermediary entity established to invest in the master fund.

Application to typical structures

The main structural outcomes are as follows:

- where a regulated mutual fund conducts its investment business through a single open ended subsidiary trading 51% or more of its assets then that subsidiary should register as a master fund.
- where a feeder fund is not registered with CIMA, for example on the basis there is no pooling or in reliance upon the 15 Investors Exemption, then the master fund registration requirements will not apply to its subsidiaries.
- where one or more feeder funds have less than 51% of their assets invested in a subsidiary that subsidiary is not a master fund and is not required to be registered.

We would note:

- for a regulated mutual fund with two or more wholly owned trading subsidiaries, the subsidiaries will normally fall outside the regime (as no one subsidiary will implement the "overall investment strategy" of the parent fund).
- the definition focuses upon the ultimate master fund where the trading of investments occurs, as opposed to any intermediate vehicles.
- the requirements for a "principal purpose" and an arrangement "established to invest",

mean that inadvertent or short term structures are not caught.

- there is no clarification as to when or how the 51% test is applied, for example in the cases of a fund with fluctuating allocations or an umbrella fund.

Registration requirements for master funds

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

- payment of the initial and annual fees of US\$3,049;
- filing of letters of consent from the administrator and the Cayman Islands auditor;
- initial filing of a copy of the certificate of incorporation or registration for the fund;
- annual filing of locally audited accounts (and 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. A separate offering memorandum is not required for the master fund. Master funds are subject to the full provisions of the

Law, including the supervisory powers of CIMA and the whistle blowing obligation upon the fund's auditors.

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

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

- closed ended funds, i.e. funds which do not offer investors a right to redeem;
- funds for a single investor (unless they are the sole trading subsidiary of a regulated feeder fund); and
- master feeder fund structures where both the master fund and the feeder fund rely on the 15 Investors Exemption.

New fees under the Law

The initial and annual registration fees for all regulated mutual funds, other than master funds, have increased to US\$4,268. In addition, an initial filing fee and, shortly, an annual audit filing fee of US\$366 shall apply to all regulated funds including master funds.

Next steps

Operators and managers of Cayman Islands funds should contact their legal advisers to assess the legal and business impact of the amendments to the Law on them. A number of funds will now require registration or restructuring with consequent amendment to their offering and constitutional documentation.

This Client Update 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 Travers Thorp Alberga at any time if you have any specific questions or would like more detail on any of the points made in this memorandum.

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