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Editor’s Note

Cayman regulator turns the spotlight on Corporate Governance

In January 2014, CIMA, the Cayman Islands financial regulator, issued a “Statement of Guidance” on corporate governance which is discussed in depth in this Roundtable.

The recent developments have to be seen in context with a groundbreaking report in the Financial Times from 2011 exposing what are called 'jumbo directors' - companies that provide directorships for hundreds of Cayman funds. These relationships were only found out through investigative journalism, which subsequently drew the attention of regulators. Since then, Cayman has offered investors access to a database that shows the directors relationships in an effort to let them make up their own minds during the due diligence process. Critics have called for even more transparency, although industry insiders say limiting the number of director roles is unrealistic. Participants of this Roundtable commented on how they see the issue from inside Cayman, as CIMA works through how to handle directorships. The situation will be difficult for the regulator as jumbo directors are a virtual cottage industry in Cayman, and relationships within the alternatives space are intertwined.

Will U.S. managers have to form more advisory committees?

Another industry development is the increasing use of Limited Partnership structures for a master fund, whether via a Delaware LP or a Cayman LP. This has increased from 5% to 10% of launches to 30% to 40% of recent launches as the partnership structure is more suitable for U.S. investors for tax reasons. This creates an interesting situation from a corporate governance standpoint as traditionally the independent director would sit on the boards of the Cayman feeder and the Cayman master. Once that becomes a Delaware master or a Cayman LP master, then the directors will typically have no responsibility, especially for U.S. managers who usually are the General Partner to the LP master: directors on such a feeder board will have no insight or control over what is happening at the master level where the portfolio is. In order to address this situation, managers are encouraged to form an advisory committee which then has certain powers with respect to the master fund such as liquidity, suspensions, etc.

This Opalesque Roundtable took place in February 2014 in Georgetown, Cayman Islands, with:

1. Ashley Gunning, Partner, Walkers
2. Darren Stainrod, Principal, HighWater Limited
3. James George, Partner, BDO
4. Kobi Dorenbush, CEO, Caledonian Global Financial Services

The group also discussed the following trends and topics:

- Mega funds versus Boutique: How have the emergence of major hedge fund complexes with assets in the order of $50-100bn AUM changed the industry?
- Why do large hedge funds tend to underperform?
- Why may the last six months of 2013 have made a difference to a startup manager and help them to survive 2014?
- Increased spin outs from existing fund management groups and mergers of both funds and of fund management groups
- Increase in special situations funds, real estate based private equity funds, and activity on managed account platforms
- Should investors be wary of irregularities regarding the proper allocation of expenses and compliance between managed accounts and funds?
- How do U.S. based managers deal with AIFMD?
- What are the prevalent fee structures now?
- How does the future for Cayman and other IFC jurisdictions look like?

Enjoy!

Matthias Knab
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Cover Photo: Evening on Seven Mile Beach, © Matthias Knab

Participant Profiles

(LEFT TO RIGHT)

Matthias Knab, Darren Stainrod, James George, Ashley Gunning, Kobi Dorenbush.

Introduction

James George
BDO

My name is James George, I am a partner with BDO in the Cayman Islands. I have more than 15 years of experience in the financial services sector auditing a variety of investment structures including hedge funds and private equity funds. BDO is the world's fifth largest accounting network with offices in 138 countries and employing almost 55,000 people worldwide. The Cayman Islands office was established in 2002 and is the 5th largest firm in the islands. We provide audit, US tax and corporate recovery and insolvency services primarily to financial services related entities.

Ashley Gunning
Walkers

My name is Ashley Gunning. I am a partner in the investment funds group at Walkers and am based in the Cayman Islands office which is the headquarters for our law firm. Originally an English qualified solicitor, I joined Walkers in 2004 and worked in our offices in the British Virgin Islands and the Cayman Islands until 2009 when I founded our Singapore office and remained there until returning to the Cayman Islands in 2012.

As well as investment funds, Walkers also has practices in corporate, finance, insolvency and corporate recovery, trusts and general litigation.

In total we have eight offices around the globe and practise the laws of the Cayman Islands, the British Virgin Islands, Jersey and Ireland.

Walkers represents the majority of the top 50 hedge fund managers and private equity fund managers worldwide. Our Global Investment Funds practice is one of the largest specialist offshore teams with over 60 lawyers engaged in investments funds work. We provide legal advice upon fund formation and issues occurring throughout the life of funds, structural issues, regulatory matters, distressed funds, re-domiciliation, termination and on-going general advice to investment funds and managers. Our team has extensive first-hand experience in the market with in-depth knowledge of the practical, legal and commercial issues which arise.

Darren Stainrod
HighWater Limited

My name is Darren Stainrod, I am a Principal at HighWater Limited, a premium provider of professional directors and related services to the alternative investment industry. HighWater was established in January 2007 and is currently licensed by the Cayman Islands Monetary Authority to carry on the business of company management. Prior to joining HighWater in 2013, I spent 17 years with UBS where I was responsible for their global alternative fund services business and and prior to that I was an auditor in the financial industry.

Kobi Dorenbush
Caledonian Global Financial Services

I am Kobi Dorenbush, CEO of Caledonian Global Financial Services, a privately owned financial services provider based in the Cayman Islands. I am a Canadian lawyer by trade. I previously acted as legal counsel to one of the largest offshore fund administrators. At Caledonian, we are focused mainly on international banking, brokerage and custody, from our headquarters in the Cayman Islands

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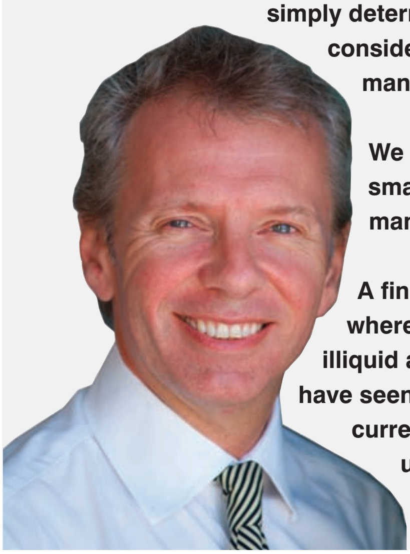
Matthias Knab Each year the world of hedge funds and alternative investments is changing. What has been happening recently on the Cayman Islands, and what developments do you see for this year?

Ashley Gunning: In 2014 we expect to see more of the same and a continuation of the trends experienced in 2013.

The market is dominated by the institutional groups who continue to go from strength to strength. They raise capital quite easily, are able to manage the regulatory hurdles well and continue to launch new funds.

Conversely, new start-ups – although, we have seen a slight uptick in the last six or eight months – still find it difficult to raise sufficient cash and are very much bogged down by regulatory issues and the costs associated with them.

There has been a noticeable trend towards spin outs from existing fund management groups. Often, larger firms and the professionals working there, realize their business has reached a certain maturation, or, in some cases, they have simply determined to stop trading and managers that have worked with those funds, often for considerable periods of time, are leaving and starting their own new funds. Such new managers often find it relatively easy to attract seed capital.



We have also seen mergers of both funds and of fund management groups – either where small standalone funds become subsumed by other funds, or, where an entire management group is taken over by another.

A final trend which I would expect to continue is the increase in special situations funds where specialist managers are buying shares from existing shareholders in funds that hold illiquid assets and which in many cases have now been static for three or four years. What we have seen is some special situations funds and activist investors buying those assets from the current holder at a discount, and then actively pressuring the manager to sell the underlying assets so that even at a forced sale price the new owner will profit.

Kobi Dorenbush: One of the things we are seeing on our side is the increase in activity from real estate based private equity funds. There has been a lot of change in that sector, particularly in United States. The U.S real estate market has really started to pick up, particularly outside of the core areas where real estate values seem to have started to rebound.

We have also noticed increasing activity on managed account platforms. Essentially, investors are looking for greater control, particularly when they tend to invest with younger or smaller managers.

Darren Stainrod: From our perspective we see a continued increase of flows into alternative investments, particularly hedge funds in the U.S. and private equity globally.

However, the general shift of institutional money away from co-mingled fund of funds to direct investment in managed accounts and funds of one (with the fund of fund manager often providing varying degrees of support or advice sometimes up to a full discretionary mandate) continues.

Some of these launches in the U.S. are from the last of the talent coming out of the prop desks of the banks that need to comply with the Volcker rule, however most are now formed by seasoned managers breaking away from the larger shops to start their own funds (often seeded or with other support from the mother-ship who see the bigger picture of retaining the talent in that sub-strategy over breaking ties with former colleagues). These new launches have helped create opportunities within the professional director services industry in Cayman, which continues to be the domicile of choice for hedge fund managers, despite growing competition.

Most U.S. managers are initially marketing their funds within the U.S. as they wait for the confusion of rules relating to marketing in Europe to clarify with implementation of the AIFM Directive. In any case the capital flows are largely coming from the U.S., and so there is no need for them to navigate the European minefield or take long flights to Asia.

In Europe itself managers are too distracted by rules and regulations to concentrate on innovation and product development. AIFMD, EMIR reporting, SEC and CFTC registration, FATCA and a change in UK partnership tax law has them bogged down until at least the second half of 2014. In Asia there continues to be a steady trickle of launches but few of any significant size.

Globally the barriers to entry continue to rise as fee pressure from seed and other investors put pressure at one end, while the ever-increasing costs of set up squeezes them from the other. An increasing army of compliance consulting firms as well as middle and back office service providers can provide lower cost solutions at the start. Notwithstanding, a fund starting with $20m to $30m of friends and family money will have to grow quickly, even if they can generate reasonable returns.

In terms of strategies the launches have been predominantly equity long/short, often with sector specializations and a best ideas portfolio or allocation. Obviously the fundamental managers struggled with their short positions during 2013. There were a few credit and global macro launches as well but managers in the once hot emerging markets and commodity strategies hunkered down to ride out the storm.

Finally, as Ashley just indicated, the increased activities of the larger institutional investors are pushing trends in the industry. From our perspective, focusing on the corporate governance angle, we do see them continually pressing for higher standards, culminating in the Statement of Guidance being issued by CIMA in January 2014. There is an ever-growing trend away from larger volume players that offer directorship services on a platform basis towards the boutique firms with a smaller number of experienced directors and smaller, more focused client portfolios. The trend is also away from Corporate Governance provided by firms affiliated to the offshore law firms, although this situation is resolving itself as the law firms continue to sell off these businesses in order to help manage and fund the generational change of the old guard.

Kobi Dorenbush: I would say first of all I completely agree with Darren's observations about the direction that the directorship industry is taking right now and governance in general. As a result of a number of legal decisions and investors wanting greater risk control, you are seeing a real trend away from what you could call "volume players". Investors and fund sponsors are looking for directors who can provide real oversight, who are able to dedicate a significant amount of time and proper attention to the responsibilities of their directorship. There is a real emphasis on quality over quantity in terms of the number of directorships that a professional director has.

The second point that I mention affects existing funds as well, but particularly start-up funds again. In a year like 2013 where various stock markets returned 30% on their respective index, some alternative investment managers struggled to outperform that, notwithstanding the past few days in January where you saw some temporary and minor corrections.

Coming up with say 15% or even 20% returns in a year like 2013 can really present a challenge, particularly for startup managers who are working to build their credibility and reputation. That kind of competition coming from the market benchmarks just represents another challenge for them.

Darren Stainrod: You are right. Markets like 2013 present a significant challenge for hedge fund managers in reaching their target benchmark indices. Trying to demonstrate that they are actually generating alpha rather than riding a beta wave can be difficult, although the performance fees for those without benchmark hurdles may help them survive in the short term even if they are underperforming their target returns.

While I do take your point that raising additional capital in this environment can be a challenge when they are not beating an index, most managers are now above high water and have collected at least some incentive fees to help pay the bills. From that perspective, strangely enough, the last six months of 2013 may actually make a difference to a start-up manager and help them to survive 2014.

James George: I agree and want to reinforce our observation that the smaller managers are really struggling and the institutionally backed funds are continuing to expand.

One activity we have also noted is that some firms have decided to "clean up" their existing fund structures in an effort to reduce costs, especially given all the regulatory changes and pressures that still keep coming down the pipeline. This includes getting rid of unnecessary share classes, trying to deal with side pockets and unwanted illiquid positions, or they may be closing down some funds that aren't overly successful or under-subscribed.

Ashley Gunning: The big institutional funds certainly tend to be more risk averse. So, while some of the mega funds performed quite well last year, given the buoyant markets, the fact is that many of them rather unperformed. This is a concern, because to some extent a number of those funds have started to look a bit like the S&P 500 and are not really doing what they set out to do in the first place and produce above average returns. One knock-on effect of this, especially with professional investors in these lesser performing funds, is that there is some pressure on fees.

We currently see quite a lot of pressure on management fees and to a lesser degree also on performance fees. I read a review quite recently stating that management fees were now closer to 1.4% in certain seeded funds and 1.7% in others rather than the customary 2%.

I fully agree with the observations made regarding corporate governance. The decision not to use or appoint potentially conflicted parties is important to the industry and is clearly the direction in which we are headed. As the industry strives for increased credibility, then those businesses providing important services to investment funds have to be free from any influence or material relationship. The one concern that investors tend to raise as a result is that robust corporate governance and the provision of independent directors creates an extra cost burden, and there is a further concern that certain service providers may price their offerings at high levels as demand for their services increase.

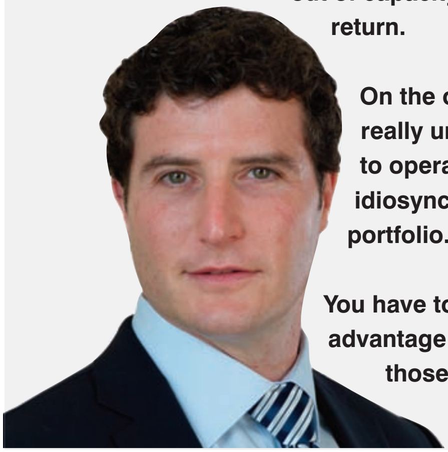
Matthias Knab We mentioned the growth of the large funds or hedge fund firms - I remember a participant at our first Connecticut Roundtable in 2009 making the prediction that with the continued institutionalization, we could even witness the emergence of some major hedge fund complexes with assets in the order of $50-100bn AUM. If you think about Bridgewater and a few others, we are already in that region or will soon be there. How do you see this growth and asset concentration changing or affecting the industry?

Ashley Gunning: There are certainly institutional businesses that have well in excess of that amount of money under management at the moment, but often the assets are divided up into a number of different management groups or structures within those institutions and managed accordingly. The drawback for smaller management firms is that the cost of operating the business is becoming prohibitive. Not just in terms of the daily cost of managing money or dealing with regulatory issues, but all the additional costs of hiring staff and different service providers in order to professionally run an investment management company.

Nevertheless, I don’t think that just being big for the sake of economies of scale will be the only future model. I think there is room for everybody and given the trend I mentioned earlier about the performance of some larger funds getting weaker, then for obvious reasons, I would expect that a good deal of the smart money will follow the more entrepreneurial manager who is bound to be more nimble. But as Darren said, the manager with $20 to $25m simply won't be able to cope if he stays at that level. The minimum size required to deal with operational costs and the increased regulatory oversight is probably in the region of $100m.

Kobi Dorenbush: Let me bring up a question here. With the large funds getting larger and in a way building pressure and challenges for the smaller funds, are the large firms in this environment now recruiting new managers who otherwise would have started out their own small funds?

But if the larger funds bring on would-be managers on a grand scale, you have to wonder at what point they will run out of capacity because they can't deploy capital in an effective manner to generate enough return.



On the other side, it's often the smaller managers who are able take advantage of many really unique opportunities – if they are able to get to that critical mass which allows them to operate and stay in business. Many of these opportunities are limited and very idiosyncratic – they may be too small for a large manager to make any difference to their portfolio.

You have to ask if it will be the smaller, more nimble managers that will be able to take advantage of inconsistencies and opportunities in the market. But, you also have to ask if those smaller managers will be able to reach the necessary critical mass to stay in business.

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Darren Stainrod: While some of the large hedge funds do seem to keep getting bigger and more institutionalized, if you are looking at them as a percentage of total active hedge funds, they are very much in the minority. There are probably only about 10 hedge funds out there that are $25bn+, and maybe only 100 that are over $10bn, while about 80% of all hedge funds registered with CIMA are under $200m. The giants are still the exception to the rule, and many surveys point to these smaller managers being able to generate better returns as they are often more focused, hungry and nimble in the early years.

As for the point made relating to consolidation of funds, while we have seen some examples of smaller funds being consumed by bigger hedge funds, there are many more examples of the larger funds spawning offspring as fund managers break away to start their own funds, as I said sometimes with the support of the larger hedge funds who see the value of supporting them and seeding them, rather than losing them altogether.

This industry is by its nature innovative, and despite all the major barriers to entry, with the ever-growing compliance and regulatory reporting requirements etc., there are very good providers that this can be outsourced to which allow the manager to focus on what he is good at, rather than distracted by building infrastructure. A small start up manager can leverage these options to begin with and still be able to attract institutional money. So there are ways the industry enables managers to survive a little bit longer with a smaller asset base, but still, as I said earlier, at the end of the day a firm won't survive forever with just $20m AUM, but will ultimately have to attract institutional money.

As managers grow and ticket sizes get larger, some investors will request a managed account or a fund of one in order to gain more transparency, better liquidity and control over the assets. When this happens we are interested, from a corporate governance view point, on how expenses are allocated to the various portfolios, and in case of a carve out, that the existing funds does not give up performance as a result of any positions transferred to the new portfolios.

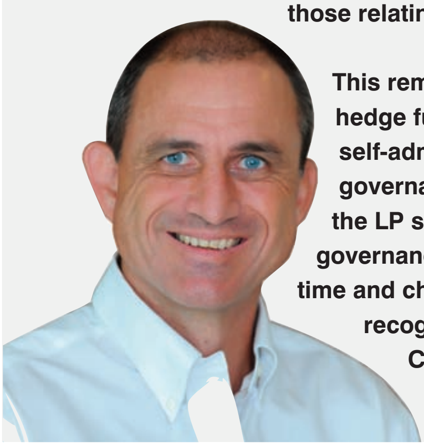
We would also be interested in the trade allocation policy on a go forward basis to ensure that they are equitable and any filtering is done post-allocation. This can often be complex because we are not actually sitting on the boards of all of the products that the manager runs (some might not even have a legal structure).

Matthias Knab So do you come across irregularities regarding the proper allocation of expenses and compliance between managed accounts and funds?

Darren Stainrod: Yes absolutely, these things do happen. It may not be necessarily done in a malicious or even intentional way. Sometimes people just start a managed account and don't think about the implications to the existing fund of expanding the number of portfolios for the strategy by adding managed accounts and funds of one alongside it. For those expenses allocated to the fund, we must be assured that the new managed account is being billed appropriately for its fair share of the costs. Of course we are not concerned with any expenses that are borne by the manager anyway.

Another industry development is the increasing use of Limited Partnership structures for the master fund, whether via a Delaware LP or a Cayman LP. This has increased from 5% to 10% of launches to 30% to 40% of recent launches as the partnership structure is more suitable for U.S. investors for tax reasons. This creates an interesting situation from a corporate governance standpoint as traditionally we would sit on the boards of the Cayman feeder and the Cayman master. Once that becomes a Delaware master or a Cayman LP master, then we typically have no responsibility, especially for U.S. managers who usually are the General Partner to the LP master.

This creates a situation where we will be sitting on a feeder board but without insight or control over what is happening at the master level where the portfolio is. In order to address this situation we encourage the manager to form an advisory committee which then has certain powers with respect to the master fund such as liquidity, suspensions, etc. – but this is an evolving area. The advisory committee does not have full fiduciary responsibility in the same way that a board of directors has, but it will have certain agreed powers that are important to investors. These range from no advisory committee being appointed to giving the advisory committee all powers other than those relating to investment decisions.



This reminds me a bit of the situation before the global financial crisis where very few U.S. hedge funds had third-party administrators, while today it is uncommon to find one that is self-administered. In the same way, almost no U.S. funds at the moment have any corporate governance. Establishing an advisory committee is a first step because the typical set up is the LP structure, and then if the manager is the GP to that structure, obviously the corporate governance that is in place is conflicted. I am positive that this is a trend that will evolve over time and change in the hedge fund industry. On this note, Cayman as a jurisdiction has recognized this trend of using more LPs, and there are some changes to the existing Cayman LP law as well as a new LLC product in the pipeline that may be attractive to hedge funds.

James George: We are also seeing more use of the LPs in master feeder structures.

In terms of the corporate governance of investment funds, there have been some developments particularly surrounding the CIMA Corporate Governance Paper that was recently published. Given the short period of time since its release, I haven't had a chance to see if there has been any impact yet, but obviously from an auditor's perspective we welcome any improvements to corporate governance. Notwithstanding the issues with the U.S.-based entities, there are in fact a number of Cayman funds that have no Cayman directors which can sometimes lead to issues if directors are unfamiliar with new requirements; they may also be less diligent in terms of the general documentation of fund matters, policy changes, etc. This can make our job as auditor a little more difficult and result in unnecessary delays, audit adjustments, missed deadlines or, in extreme cases, a notification to the regulator.

Ashley Gunning: There has been some limited criticism of the growth of the Cayman independent director model – mainly on cost grounds or on spreading themselves too thin - but also because when assets are generally held and controlled at a master fund level and that entity is controlled by an LLC, then the feeder fund directors are often considered toothless.

There is talk of a trend that funds are setting up committees at the master fund level and given reasonable powers to control the master fund to some degree as in a private equity fund structure, but whether it's in fact a trend or just something being talked about at the moment is a little unclear. We certainly don't see it happening with particular regularity despite often being talked about at the various conferences and in structuring meetings.

Darren Stainrod: James mentioned the Statement of Guidance on Corporate Governance that CIMA published on 13th of January 2014. I would say it received a mixed response from the allocators that had been pushing for more stringent corporate governance standards. Some of them felt that it didn't go far enough as it wasn't a prescriptive set of requirements, whereas others we have spoken to are happy that at least there is now a defined minimum criteria to which they can request directors to confirm that they are in compliance with. It is a step in the right direction and something that can be built on, as standards are continually pushed forward.

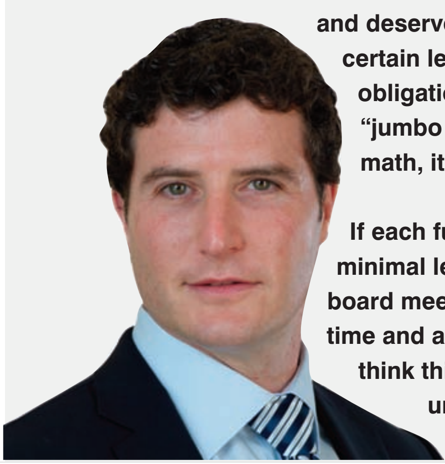
The Statement of Guidance was the first of three initiatives that resulted from the Consultation on Corporate Governance that CIMA circulated widely within the industry at the beginning of 2013. The second initiative is the regulation of professional directors (defined as directors with over a certain number of funds or relationships, yet to be determined) as well as the registration of all fund directors so that data on current names and contact numbers are maintained. This is not an issue for Cayman fund directors as most are already regulated under a Company Managers License.

Finally, the much discussed public database showing details of offshore directors' workloads is likely to go ahead as the third initiative, albeit probably not in 2014. The exact format, contents and whether it will be searchable is not yet finalized, and there is an industry working group looking at these questions. HighWater is one of the few professional director service firms that supported this initiative – although we understand that the funds are private funds and that investors can, in any case, request the directors to disclose the number of funds they service before they decide to invest, there is value to Cayman in being transparent and putting the issue to bed.

Other potential initiatives discussed in the consultation such as the mandatory requirement for a Cayman director did not get implemented as this was felt to be protectionist and an unnecessary step.

Another issue discussed in the consultation was the use of corporate directors and whether this practice should be allowed. It was felt that although their use was not widespread, corporate directors had some merits in specific circumstances and that the investors should be left to make their own informed decisions on this.

Another question was whether to put a cap on the number of directorships a director could have. It was decided that this was too subjective due to the different complexity of various funds structures and strategies and the capacity of directors to devote time to them. While there were good arguments in favor of putting a limit on the number, the decision was made to retain the open framework and leave it to the due diligence of the institutional investors to judge if the directors they were appointing had enough capacity to devote sufficient time to the fund that they were looking to invest in.



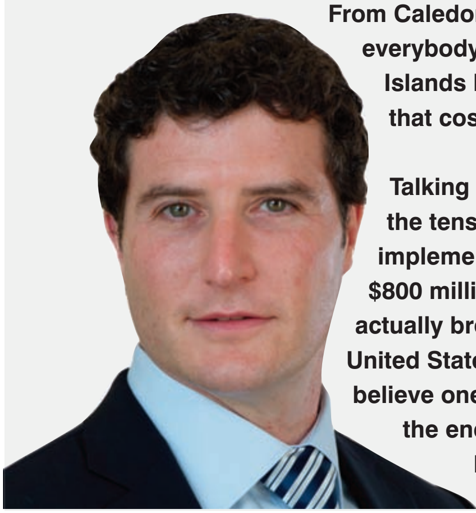
Kobi Dorenbush: There is a lot of debate on issue of what some people call the "jumbo directors", and deservedly so. Serving as an independent director is an important function and requires a certain level of time and attention on the part of that independent director to meet their obligations and provide real value. But in many cases, when you look at some of these "jumbo directors" who, in some cases, serve on thousands of boards, and start doing the math, it just doesn't add up.

If each fund has at least one board meeting a year – and we are talking here about the minimal level of involvement for a director, that means on average you'll have one or more board meetings on every single business day. At some point you have to question how much time and attention some of those "jumbo directors" have to devote to each directorship. I think this is the stage that the industry is at right now and it will be interesting to see how it unfolds in the near future.

Ashley Gunning: Like many industry participants, Walkers has provided input into the CIMA process for their corporate governance paper. In our view, one of the critical points – that of limiting the number of directorships that can be held – was unlikely to occur. Obviously, different firms approach the provision of directorships in different ways, and having different options works well for the varied industry in which funds and fund managers operate. I don't think that a fixed limit of 50 or 60 relationships or whatever is feasible when considering the large number of funds registered in the Cayman Islands. Rather, in my view the route that CIMA elected to take which is to provide the database and related disclosures so that parties can research and then make up their own minds is a perfectly natural way to deal with this issue..

Matthias Knab Let's take a look at global regulatory and legal developments and how Cayman is affected by them – things like AIFMD, FATCA, onshore funds versus offshore funds, etc.

Kobi Dorenbush: Capital is fluid and is always looking for opportunities and a home that provides it with the least barriers and the greatest opportunities. So from one perspective, the more the onshore markets increase regulation and increase barriers for capital, the more that capital will find its way to a home like the Cayman Islands, where we don't place significant barriers on capital. I think it is really important to distinguish clearly between barriers that limit capital and the performance capital can achieve – the investment performance – versus demands for increased transparency.



From Caledonian's perspective, we have no issue at all with transparency and I think everybody in the room would and in fact all top-end service providers from the Cayman Islands have no issue with transparency. It will unfortunately add a layer of cost, and that cost will ultimately be borne by the investor or the client.

Talking about cost, the latest statistics I am reading are basically saying that for all of the tens of billions of dollars that for example FATCA is going to cost in terms of implementation in the public and private sector, it is only expected to generate about $800 million per year in additional revenue to the U.S. government. Worse, when you actually break that number down to the six million U.S. citizens who live outside of the United States, you are talking about $135 per year per U.S. citizen living outside of the U.S. I believe one really has to question the effectiveness of a very costly regime like that, but at the end of the day, what can you do but comply. I don't think it really changes our business; we just adapt.

James George: The point of view of most managers seems to be that they just have to accept the reality of the situation. They realize things like FACTA are not unique to Cayman. Cayman has to comply and implement it order to stay competitive in the marketplace, just like everyone else.

A lot of managers seem to have adopted a wait and see attitude regarding AIFMD. Some managers that were heavily focused on Europe will have adopted straightaway, but a good number are waiting.

Many North American managers don't really have a lot of direct involvement in Europe, so they are either out of scope or they are looking to restructure in order to be out of scope of AIFMD. It seems to me that by and large the funds will continue to operate as normal under the private placement regimes for the time being.

Ashley Gunning: From a reputational point of view, and for the sake of enhancing Corporate Governance, we welcome most of the regulation that has been produced, we just wish it hadn't all come at the same time. This has created a huge amount of fatigue in the industry, and there is no doubt that managers have been prioritizing one piece of regulation over another, and AIFMD is the one that has been shunted to the back of the queue at the moment, and it has not helped that some of the European regulators have been slow to react and have not done enough to eradicate the confusion amongst industry professionals.

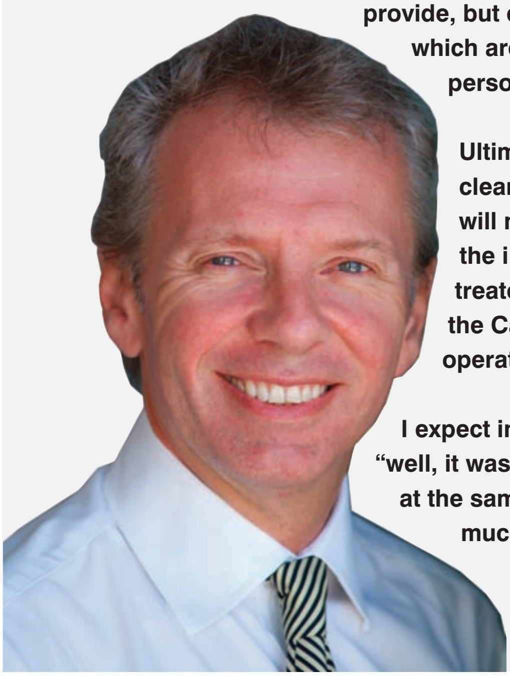
Participants are rightly concerned about the volume and the resultant cost of it all, and certainly, as Kobi indicated, are making their own conclusions about what the overall benefit might eventually be. However, if legislation helps create transparency and makes the relevant governments, regulators and industry participants look favorably upon the Cayman Islands and other offshore jurisdictions and helps them to appreciate what has been achieved and that our business is legitimate and credible, then I believe we are very happy to comply.

With respect to the national implementation of the AIFMD, the U.K., as you might expect, has made life easier with respect to the private placement regime, whereas some of the other European jurisdictions have favored other European locales and thus have made the life of managers based in third countries rather more difficult.

Regarding FATCA, we have to wait for the enacting legislation to be produced by the Cayman Islands government, but we have done everything else that's necessary. The Cayman Islands has signed all the required cooperation agreements for AIFMD, are not on any FATF blacklist, and are raring to go.

Finally, we are presently faced with the consultation exercise upon the register of beneficial ownership of corporate (and potentially other) entities and the decision as to whether to implement that concept and, if so, whether it should be made publicly available. The Cayman Islands is already fully compliant with international standards required by the OECD and FATF, and our robust AML regime means service providers in the Cayman Islands have now been collecting beneficial ownership information for 10 years or so.

There are many advantages for leaving the system as is and many disadvantages involved in producing a central register, and I fully expect the consultation to result in resistance to the central register concept. As to the suggestion of making this public, as opposed to what must surely be the primary purpose of permitting regulatory and taxation authorities and governmental bodies access to the information, then I fail to see what possible benefit that could provide, but could readily provide a long list of problems and disadvantages, not least of which are cost, security and a simple right to confidentiality in one's business and personal dealings.



Ultimately, the Cayman Islands will provide a measured response and make it clear that whilst there are strong and justifiable objections, the Cayman Islands will nevertheless adhere to what the international community demands and what the international community enacts – on the condition that all jurisdictions are treated the same and can meet the same high standards of a jurisdiction such as the Cayman Islands. The entire concept will be dependent upon all participants operating on a level playing.

I expect in one or two years' time we will look back at the events of this period and say, "well, it was an expensive exercise, it was probably overkill and a shame it all happened at the same time, but we are out the other end and the industry is carrying on pretty much as before, and perhaps with a cleaner bill of health..."

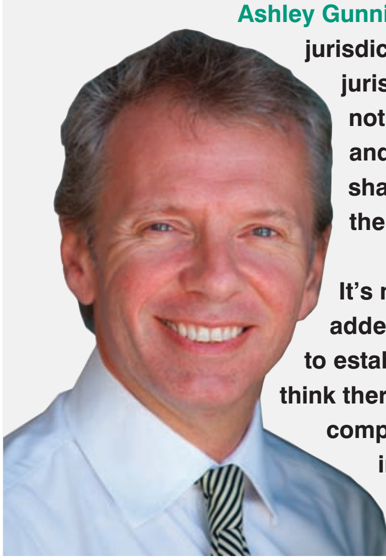
Darren Stainrod: I think that Cayman has done a good job in preparing itself by negotiating Tax Information Exchange Agreements with a large number of countries and demonstrating to Europe that it is in a position to be accepted as a third country in 2015. When AIFMD was first announced, some parties said this was the end of the Cayman funds industry and that a significant amount of funds would re-domicile to Europe. We haven't seen that happening. Clearly we can't substantiate how many new funds have launched in Europe instead of using a Cayman structure, but what we can say is that there is a healthy flow of new funds in Cayman, that the hedge fund industry is thriving in Cayman, and there is no expectation this will change as a result of the AIFMD directive.

There are even discussions as to whether or not AIFMD creates an opportunity for Cayman assuming that it is accepted as a third country. This includes oversight functions of the custodian ("depo-light" opportunities) and the potential for establishing management companies in Cayman.

In terms of the flood of regulation affecting the hedge fund industry in Cayman I think that the jurisdiction has reacted positively and swiftly to the challenges (Cayman was one of the first countries to successfully negotiate a Type 1 IGA with the IRS) which has positioned us well verses the competition. The real challenge may actually be the number of competing offshore jurisdictions coming up with similar products or a change in US legislation that makes Cayman less attractive to US non taxable investors.

One thing I would like to mention at this Roundtable relates to the cost of Cayman funds that now have reached a level where at least the smaller funds might start to feel the effect. I know that the government is aware that they cannot keep on increasing fees, and they have indicated that there will be no further increases in the near future. On the positive side Cayman has worked hard to rebalance the budget in the past year. A combination of targeted austerity measures coupled with increased revenues from the buoyant tourism industry as well as the opening of the new medical tourism as a third pillar in the economy should all ease the pressure off of the financial industry.

The new government has representation by a number of leaders that previously held senior positions in the financial industry in Cayman and there is an expectation that this will further help support the industry. Touching wood, I dare say that the future is pretty rosy for the Cayman economy. Most of the signs, which of course come on the back of a resurgence of the economy in the U.S., seem to be fairly positive at the moment.

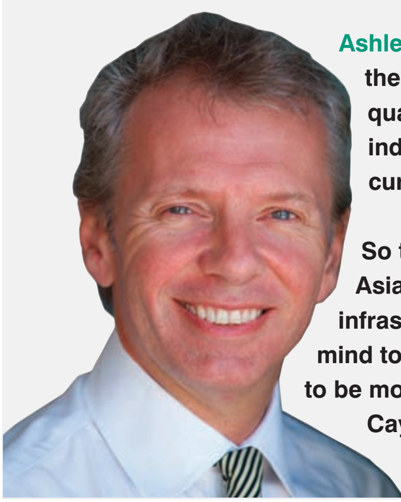


Ashley Gunning: I agree with Darren - Cayman should be aware of the fact that there are other jurisdictions competing for the same business. As a law firm we work in several different jurisdictions and can benefit either way, but purely from a Cayman perspective it is worth noting that there are some sleeping giants that are stirring and looking at the fund industry and enacting legislation which either mimics the Cayman Islands model with a view to sharing in the benefits, or considering new legislation to attempt to position themselves as the fund jurisdiction of choice.

It's not difficult for a competing jurisdiction to be less expensive than Cayman. We have added a lot of cost to the fund establishment process over the years and the myriad of fees to establish a hedge fund are actually fairly complicated now and this is confusing to people. I think there are probably better ways of doing it, and in considering change we must be aware of competition from other jurisdictions and examine their approach. We do have a far better infrastructure and a far better service provider base than our traditional competitors, so I think we are well ahead of the game, but we have got to keep our eye on the ball.

Kobi Dorenbush There are many other jurisdictions that are trying to enter or increase their market share. All statistics still show that Cayman is by a wide margin the leading fund jurisdiction, and in fact one of the largest financial centers in the world. But the market isn't growing at the same rate as it did in previous years during more robust economic cycles. In response, governments in all jurisdictions are looking for new ways to increase revenues and that certainly includes attempts to take market share away from the incumbents like the Cayman Islands. But Cayman continues to offer a compelling product in terms of the quality of its service providers, strength of its governing institutions and comprehensive legal system. But this doesn't mean that the Cayman Islands can rest on this. We have to continue to provide world class service and be innovative.

James George: I do want to mention one thing in relation to the quality of service providers available in Cayman, which I consider one of Cayman's strengths. The Cayman Islands Society of Professional Accountants (CISPA), the regulator of auditors in the Cayman Islands, was recently admitted as a member to the International Federation of Accountants (IFAC), the global standard setter for the accounting profession. As part of CISPA's obligations to IFAC, a quality review system has now been established and all audit firms in the Cayman Islands are subject to a quality assurance review. CISPA did not have to join IFAC but did so to further support the credibility of the profession in Cayman and demonstrate that audit service providers here are committed to meeting internationally recognized standards. In addition, the Cayman Islands Auditor Oversight Authority, the Cayman PCAOB equivalent, is now established and will review Cayman-based audit firms that audit EU market traded companies. So even the auditing profession isn't immune to increased oversight and regulation.



Ashley Gunning: If you compare the Cayman Islands to the other small IFC jurisdictions, there is no doubt that we are the clear market leader for the hedge fund industry. The quality of service providers on island is unparalleled and includes highly professional independent directorship firms, auditors, administrators, and law firms which are currently ahead of the competition.

So the real threat has to come from the onshore jurisdictions in Europe and particularly in Asia, where all of those same quality service providers are also available and where infrastructure is already in place. If, or when, governments in those jurisdictions turn their mind to competing with the Cayman Islands, then we should be wary. We are smaller and able to be more nimble and to react faster, but we have to stay focused, flexible and innovative if the Cayman Islands are to remain competitive.

Darren Stainrod: As Ashley mentioned, the quality of Cayman's local service providers is well recognized. However, one of the strengths of Cayman is the fact it has an open architecture which allows all but the audit sign off of a fund to be performed by service providers located outside of Cayman. That is a real strength of the Cayman product but also means that not all parts of the value chain of the funds registered and domiciled in Cayman are retained here.

I saw the downside of that in my prior role in fund administration where most of the processes migrated away from Cayman to less expensive countries or nearer to the manager. Part of that was due to regulatory changes with the lifting of the Ten Commandments, but the real driver was probably the growth in technology which allowed administration to be performed anywhere in the world, leveraging time zone arbitrage and less expensive workforces. In reality as the hedge fund industry boomed in the mid 2000's the ten thousand plus people in the industry could not all have squeezed onto the island in any case.

Many law firms that started here have become major global powerhouses. For example, Maples and Walkers each probably have over or close to ten offices in other jurisdictions servicing Cayman funds.

I believe that in addition to keeping Cayman as an attractive domicile to managers, finding ways to retain as much of that value chain that it creates in Cayman is probably just as important to the Cayman economy.

It helps that Cayman is able to attract and keep talent. A warm climate, low taxes, stunning beaches and great diving all help in this regard. In addition, immigration policies which have been problematic in the past are being revisited and made easier, if not cheaper.

Finally some audit firms are offering lower fees for hedge funds than in New York which is seeing some audits migrating back to Cayman. There has also been some small growth in the administration industry here in recent months (although a full return of the industry to Cayman is unlikely, not least because all of the past fund admin heads are now in the directorship industry...).