



Opalesque Round Table Series '11

CAYMAN

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Editor's Note

Dear Reader,

Onshore and offshore jurisdictions are facing similar battles on the regulatory front like the enactment of the Dodd-Frank Act, FATCA and Fin 48, and the AIFM Directive in Europe. By far and large, **FATCA will pose the most immediate and significant challenge for global hedge fund managers and their service providers in 2012.** Gathering and reporting the large amounts of information required in order to be compliant will be a massive undertaking.

Will hedge fund administrators raise fees?

From the fund's perspective, the main entity responsible for liaising with investors in order to comply with new regulations will be the administrator. Administrators will bear the greatest burden, and funds will need to ensure that this service is covered by the admin agreement. It will be interesting to see whether administrators will look for additional fees to provide this service or perhaps greater limitations on their liability. We may well see some tension around those issues.

Getting value for money: Hedge funds re-evaluate and re-negotiate service provider agreements

Investors now require managers to demonstrate they have actually gone through a thorough process when selecting the right service provider. Just because a manager's former firm used a set of service providers that may have perfectly reputable names does not necessarily mean they are the right provider for every fund.

Therefore, many of the larger and more established hedge funds have started to look across their whole spectrum of service providers and analyze them - everything from administration to audit and legal and prime brokers, making sure they are getting value for money.

Implications of the Weaving Case

In August 2011, the Grand Court of Cayman fined two Directors of the Weaving macro hedge fund \$111m each for willful negligence or default. There is not a lot of case law out there where the Directors of a hedge fund have been held accountable for a fund failure. The fact is that you cannot hedge away the risk of poor corporate governance, and investment managers should understand that investors are no longer prepared to accept this risk. **What guidance did the Judge provide in the Weaving judgment?**

This Roundtable further includes details on:

- **How many funds can a Director really serve as an Independent Director?**
- **Cayman hedge funds rebound better as expected, visible uptick in new fund formations and demand from South America and Asia**
- **What drives Cayman's continued success as the dominant offshore hedge fund jurisdiction?**
- **What is the dynamic between offshore fund formations and UCITS in onshore jurisdictions?**
- **How does Cayman avoid falling into the infrastructure trap which can affect places like Zug or Geneva?**

The Roundtable was sponsored by law firm Walkers and The Harbour Trust and took place on Sept. 26th 2011 at Walker's Georgetown office with:

- **Ingrid Pierce, Partner, Walkers**
- **Andrew Stepaniuk, Head of Alternative Investment Practice (Cayman), KPMG**
- **Greg Bennett, Director, The Harbour Trust Co. Ltd.**

Matthias Knab
Director Opalesque Ltd.
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Participant Profiles



(LEFT TO RIGHT)

Andrew Stepaniuk, Ingrid Pierce, Greg Bennett, Matthias Knab



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Introduction

Ingrid Pierce

Walkers

My name is Ingrid Pierce. I am a partner at Walkers in the Global Investment Funds Group. The Walkers Group comprises the law firm and Walkers Management Services, which specialises in corporate and fiduciary services. On the law firm side we focus principally on corporate and international finance with an emphasis on investment funds, private equity, capital markets and structured finance. Walkers also has a significant focus on the legal, regulatory and commercial environment in the key international financial centres, with offices in the Cayman Islands, Singapore, Hong Kong, Jersey, London, Ireland, Dubai and the British Virgin Islands. We have over 450 staff across 9 offices.

Andrew Stepaniuk

KPMG's Alternative Investment
Practice

My name is Andy Stepaniuk, I am head of KPMG's Alternative Investment Practice here in the Cayman Islands, where we have 12 resident partners and 240 staff that deal primarily in financial services, with particular focus on the alternative investment industry. We are part of KPMG's global network and work closely with our network offices, including those in New York, London, Dublin, Luxembourg, Hong Kong, Toronto and Brazil.

Greg Bennett

Harbour Trust Co. Ltd.

My name is Greg Bennett. I am a Director of The Harbour Trust Co. Ltd. Harbour is a leading specialist provider of Directorship and fiduciary services to hedge funds. Founded in 1982, Harbour is a wholly owned subsidiary of the Cayman Islands office of Rawlinson & Hunter, which is a member of an international grouping of professional firms specializing in financial advisory services, whose network of offices includes Australia, Bermuda, BVI, the Cayman Islands, Guernsey, Jersey, New Zealand, Switzerland, and the United Kingdom.

Ingrid Pierce

In the last year, there has been a definite uptick in new fund formations. I think it is fair to say that the industry has rebounded better than expected. Last year numbers were somewhat flat and 2011 has certainly been more active than the last couple of years.

Most of the new managers we have seen have come from established hedge funds and others have spun out from banks. As you are aware, managers who want to set up a fund today require substantial capital to get going. The formula of setting up with \$10 million or \$20 million AUM from friends and family is not quite as popular as it used to be. You need a certain amount of capital to survive. We are actually finding that managers are getting significant amounts of seed capital now.

Another trend is the growth in funds launched by managers in South America. Walkers has established a global Latin American group focused specifically in this region, particularly in Brazil but also other areas such as Chile, and we expect to see a lot more activity going forward.

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**Ingrid Pierce****Ingrid Pierce**

Yes, our Asian offices and particularly Singapore have been very active. Asian based clients have traditionally invested through Cayman structures and BVI. Although the market can be cyclical, we haven't seen any slowdown from our Japanese clients. For example, we also act for many of the larger institutional banks for whom we set-up unit trust structures, and that segment of the market has never really slowed down.

Greg Bennett

We have also seen an uptick in new fund launches over the last year or two.

This trend began initially with existing managers who successfully navigated through the 2008 financial crisis – i.e. those who had decent performance and did not unfairly lock up investors or surprise them with gates. They were able to attract the money that initially flowed back into the industry, and in some cases this resulted in the creation of new fund products. Recently we have

started to see more start up managers launching products, which is a result of increased investor interest in funding start-ups, as was noted by Ingrid, as well as the availability of talented traders and managers, including those that have been leaving bank proprietary trading desks as a result of the so called Volcker rule, which proposes to ban banks from short term trading on their own accounts.

Matthias Knab

Where is that seed money coming from?

Greg Bennett

The last decade saw a notable shift in hedge fund investors from high net worth individuals to institutional investors. Pension plans, endowments and sovereign wealth funds have all become major allocators in the hedge fund space. One of the drivers of this is the fact that many pension plans have large funding gaps as a result of the ultra low interest rate environment. As such, they are allocating more money to alternative investments in order to help make up this shortfall.

Matthias Knab

Let us go in to this in more detail. There is a difference between allocating to alternatives and actually seeding them. We at Opalesque, through our Roundtables and Opalesque.TV have reported on the impressive growth of the seeding industry.

As Ingrid said, people try to launch with more money than the traditional \$10 million or 25 million. A seeder at our recent Connecticut Roundtable said the future will even be more \$100 million deals instead of two deals of \$50 million each. These are big tickets. From your perspective, what more background can you share with us?

Ingrid Pierce

We have definitely seen seed capital in the \$100 million plus range, and this has been a relatively recent trend. For managers who have the benefit of significant seed capital, the launch period is accelerated rather than elongated. Some institutions are quite active in this space and pension plans are seeding more frequently. Start-up managers with smaller amounts of capital tend to harbor ambitions of closing funds very quickly, but the launch process tends take longer than they might expect, partly because they need a bit more guidance and hand holding.

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Ingrid Pierce

Matthias Knab

Correct, some of the pension funds have even set up dedicated seeding firms for that. Andrew, what do you see from your perspective, what news or insights do you have to share?

Andrew Stepaniuk

At KPMG we've seen the same uptick in market activity post credit crisis, Beginning in, for the most part, 2010. Not surprisingly, there has been a great deal of interest in managed accounts which institutional investors are using as a controlled entry into the hedge fund universe.

We are seeing a large variety of managed account platforms that cater to a growing number of investors wish to establish greater control of their risks by selecting their own flavor of managers

on a particular platform. Investors can pick and choose their risk rating and define their liquidity constraints and exposure to different managers. That element of additional customization has been a valuable commodity and a huge growth area over the last year. Many of the larger existing managers have been the primary beneficiaries of capital allocations as a result of this trend as many institutional investors are looking for managers with longer established track records.

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The other area in which we have seen a lot of recent activity is that many of the larger and more established hedge funds have started to look across their whole spectrum of service providers and analyze them - everything from administration to audit and legal and prime brokers. More and more managers are taking a close look at their constituents and making sure they are getting value for money. This has been a very recent trend over the last year which I think will continue, and as a result I believe all service providers in the alternative investment industry will see a lot more RFPs in the coming year.

Andrew Stepaniuk



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Matthias Knab

That is interesting. Is this just about fees or is this also Trying rank their service providers according to reputation? What is behind that?

Andrew Stepaniuk

Certainly the starter is likely to be fees as people analyze and strive to understand their value proposition and control costs. When markets are tighter and returns are harder to achieve, managers are looking across their entire structure to see where they can provide better value for money to their investors. This renewed interest in controlling costs has a knock-on effect to all the other players in the industry, including ourselves, the custodians and prime brokers, administrators and the law firms – no one is immune.

After costs though, the focus is definitely on quality of service and technology. Whoever can provide the best quality service with cutting edge technology will certainly benefit in this market environment.

Matthias Knab

The key question is how is Cayman positioned to deal with that cost cutting pressure? Is this possibly an opportunity for Cayman?

Andrew Stepaniuk

Cayman Islands has always credited itself with a lot of knowledge and innovation, and I believe rightly so. This focus will continue to serve us well in bringing competitive offerings and knowledge

to the marketplace. I think Cayman is very well placed to continue building on those values. The previous Opalesque Cayman Roundtables offered good insights into Cayman's history and why Cayman finds itself in this position as the leading offshore marketplace. This experience and excellence that has always been present in Cayman will serve us well to compete globally.

Greg Bennett

Andy raises some excellent points. I agree that key considerations when looking at service providers go well beyond cost. We already mentioned the growing influence of institutional investors in the hedge fund space and these investors are very much focused on high quality corporate governance and ensuring that funds have the appropriate infrastructure and service providers.

These investors demand much more than good returns and the ability of a manager to generate Alpha. They are as concerned about the operational infrastructure and the quality of a fund's service providers, and making sure that the responsibilities delegated to them are appropriately met in order to safeguard their assets.

I believe that we in Cayman are extremely well placed to deal with these issues, because the Cayman regulatory model is based on full and fair disclosure, and information and transparency is really what institutional investors are demanding.

Andrew Stepaniuk

Since the credit crisis there is a renewed interest in the alternative marketplace, including everything that makes it tick. And with that came fundamental changes in the procedures involved. If you allow me, I think that pre-crisis there was at times a sort of lenience among the investors - I would not say laissez faire, but as we know at that time the market was going up, investments were doing well, and there were not a lot of questions asked. Post credit crisis, everybody is re-analyzing and questioning how things work, why they work this way, and can they be done better? That goes all the way up from the due diligence of investors on managers and to how managers run their organizations.

Ingrid Pierce

I think these are great opportunities for Cayman based firms. It is true that investors now require managers to demonstrate they have actually gone through a thorough process when selecting the right service provider. Just because a manager's former firm used a set of service providers that may have a perfectly reputable name does not necessarily mean they are the right provider for every fund. As part of this process managers will typically request input from two or three different providers to demonstrate they have actually done their due diligence.

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We have not only excellent lawyers, audit firms, administrators, independent Directors and other management service providers in Cayman, but we can actually provide those services directly to the fund. In the past, there was a tendency to come offshore for an audit sign-off, but for some time now there has been some pressure for funds that are domiciled in offshore jurisdictions to demonstrate that more mind and management takes place in the relevant offshore jurisdiction.

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That has led to a huge growth in the independent Director business and as you know it is now market standard for funds to have at least some members of the Board who are independent and those Directors are usually based in the offshore jurisdiction. As I said, funds are increasingly using administrators, auditors, and other management service providers who are actually domiciled in the relevant offshore jurisdiction.

Again, this is where Cayman can really excel, because we have the quality and depth of personnel that can provide the highest levels of service that are needed and demanded by investors and managers onshore.

By way of example, it has always been quite important for Canadian managers to be able to demonstrate that the mind and management of their offshore funds is really offshore. In addition to having the majority of Directors offshore, they usually set up a STAR Trust or a charitable trust to hold voting shares of the fund so that the manager has no control over the structure. There are reputable and reliable licensed Cayman trustees who can provide this service.

Greg Bennett

The fact is that you cannot hedge away the risk of poor corporate governance, and investment managers should understand that investors are no longer prepared to accept this risk. Funds need to have a corporate governance model that includes high quality independent Directors with responsibility for supervising the various service providers to the structure.

Harbour strongly encourages investment managers to go through a robust process for selecting service providers. These are critically important decisions that require extensive thought, in particular as there is no single service provider that is a best fit for every fund.

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Greg Bennett



Male Speaker

Let us move to the Weaving case and let us examine some of the legal aspects and consequences of that ruling for the industry.

Ingrid Pierce

As a starting point it is important to note that there is not really anything new in the core principles mentioned in the Weaving Judgment. The case reiterates the fundamental principle that a Director must have the requisite skill and care to discharge his or her duties.

This judgment highlights and brings to the fore an issue that professional Director services providers in Cayman have known and have practiced for a very long time, namely, that you cannot simply lend your name to a fund when you are required to act in a fiduciary capacity and expect to be let off the hook if you do not actually pay any attention to what is going on.

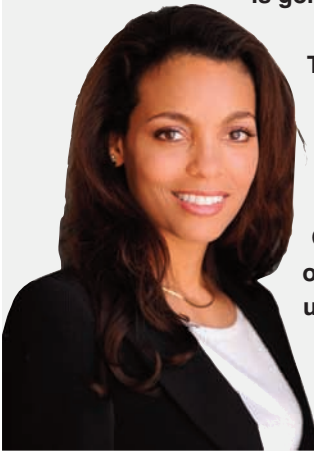
The decision made clear that a Director who not only fails actively to supervise the fund's service providers, but also fails to make any proper enquiries of the manager and other service providers when the facts self-evidently call for an enquiry, will have breached the minimum standard of skill and care expected of an independent Director.

Of course, the actual facts of that case are far removed from the way in which the vast majority of offshore funds are overseen by independent Directors. I think we all agree it is extremely unlikely that

a professional Director services firm in Cayman would ever sign minutes of Board meetings that did not take place! All those facts need to be considered when discussing this case.

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Ingrid Pierce

Part of a wider discussion at the moment is whether or not the obiter comments of the Judge in the case mean that Directors have to change any of the practical aspects of the way in which they work. Directors should consider whether they have sufficiently robust procedures in place especially at the stage of the fund set up, when reviewing the offering memorandum, contractual agreements with service providers and so forth.

Greg Bennett

It is interesting that this case received such widespread attention, although I think part of the reason for this is the fact that the behavior of the Directors was so egregious. These individuals simply did not do any of the things that a Director is required to do and they were also not actually independent of the Investment manager. It is also important to keep in mind that the judgment did not speak to other important aspects of the failure of this fund, namely the responsibilities of the other service providers.

That said, there is not a lot of case law out there where the Directors of a hedge fund have been held accountable for a fund failure. So, from that perspective, and to Ingrid's point, the guidance the Judge provided about what the Directors should have been doing is very useful and important for everyone involved in the industry, and in particular to those that serve as a Director on funds, whether as a member of the investment manager or as an independent non-executive.

The key points to highlight are that Directors are expected to have appropriate skills and act in a professional and diligent manner. While they do not need to be an expert in investment management, they do have to apply their mind to the business of the fund, and do so in a thoughtful manner. They also do have an obligation to supervise the fund and fund's service providers. Also, where meetings and minutes are used to document how they discharged these supervisory responsibilities, they actually need to have proper meetings, including speaking with the various service providers, reviewing relevant financial information, reaching conclusions, and documenting the basis for decisions taken.

At Harbour we have taken onboard the relevant guidance provided by the judgment, as we do with all industry best practices as well as guidance and requirements issued by relevant regulatory and standard setting bodies.

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Greg Bennett



Matthias Knab

Each of the two Directors was sentenced US \$111 million n. That also caught some attention. What do you think will happen to those US \$222 million, will they get the money?

Greg Bennett

No, my understanding is the Directors don't have near this amount of net worth. As well, I believe the judgment may be appealed.

Andrew Stepaniuk

It is likely to be appealed; and as a result could go on for a few years.

From our perspective as auditors, we welcome the focus this case brings on corporate governance. I totally agree with Ingrid and Greg that this case is by itself on the edge of absurdity in terms of the relationships that existed and on the level of oversight conducted, and I would echo the fact that certain lessons can be learned from the introspection of the Judge in that case. The judgment helps bring focus to best practices and in the long term will strengthen corporate governance in the offshore world.

Matthias Knab

Let us examine how the relationship between onshore and offshore finance and funds have been developing, and how the European AIFM Directive may influence Cayman?

Ingrid Pierce

One thing I would like to point out is that the onshore and offshore jurisdictions are facing similar battles at the moment, particularly on the regulatory front. We have had the enactment of the Dodd-Frank Act in the U.S., the AIFM Directive in Europe and regulation at national and local level in both onshore and offshore jurisdictions. There are many overlapping principles. For everyone involved in our industry it would be helpful to see some sort of global harmonization of these regulations, but we are a long way away from that.

What this means is that industry stakeholders have to be aware of what is going on in all the major jurisdictions, as each one has some impact on the other. Here at Walkers we have become much more focused on onshore regulation in order to better understand the challenges facing our clients. To give an example, U.S. managers that we represent and the funds they manage will be impacted by SEC registration or other provisions of Dodd-Frank, FATCA and also FIN 48.

Non-European managers have also realized that they need to understand the impact of the AIFMD if

they have any interest in marketing to European investors or setting up funds in Europe. The good thing is that now there is a bit more synergy and coordination between offshore and onshore jurisdictions.

When the terms of the AIFM Directive were finally settled, most industry bodies who had spent a lot of time commenting on the proposals or lobbying for specific changes felt that they could live with the final results. We certainly believe that Cayman will be able to meet the relevant thresholds and requirements; for example Cayman already has a sufficient number of Tax Information Exchange Agreements (TIEA's) in place and agreements continue to be put in place.

The European Securities Markets Authority (ESMA) has set up a task force to look at implementation of the Directive, and their work will continue to be the subject of some discussion. There is some concern that ESMA reverted to some of the restrictions on market access that had been rejected earlier. Another concern is whether in the long term non-EU managers are actually going to be prohibited or in some way restricted from accessing EU funds and we still do not have a complete answer to that question. In the meantime the reverse solicitation process remains intact for non-EU managers.

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Ingrid Pierce

Greg Bennett

When you look at the purpose of the AIFM Directive, it is driven by a desire to protect European investors, which is understandable. I am also convinced that so long as there is a level playing field, Cayman will be able to meet the standards ultimately established.

However, even under a worst case scenario, which would involve the establishment of an extremely protectionist regime, the ultimate losers would be European investors and their plan beneficiaries, as they might not be able to allocate capital to the full universe of hedge fund managers, which would negatively affect their investment performance. Even in that case however, the option of reverse solicitation would be available, which would allow European investors wanting to get access to non-European hedge fund managers, to make initial contact with them and gain access that way.

Andrew Stepaniuk

All market participants understand the global focus on regulation and why the different regulators and governments have taken certain steps to implement measures like FATCA, Dodd-Frank, or AIFMD. Any feedback from market constituents that I have seen is mostly focused on finding a practical, understandable solution to implementation that has the least impact on costs. However at times there can still be a huge gap or mismatch between what regulators are trying to achieve and what is practical from a market perspective, which is part of the reason why initial drafts of regulations can differ greatly from the final outcome.

This is the part of the process AIFMD is presently going through, where market constituents not only within Europe but outside of Europe want to understand the final implications of the regulations. In many respects, what people are looking for is more clear criteria or guidance rather than a generic equivalency mandate that is subject to interpretation at a later stage. As soon as market participants understand what they need to do, everyone, including Cayman, can get there.

Matthias Knab

Ingrid, you mentioned the growth in demand from Brazil. Brazil has a strong onshore regulatory regime, onshore hedge funds there are regulated in the same way as money market or mutual funds – it is one set of legislation for all, which has created the base for a very strong independent hedge fund community there. I am now interested to learn more about the offshore developments there.

Ingrid Pierce

Yes, that is the case: Brazilian managers will often set up offshore funds to facilitate the investment of private wealth of ultra-high net worth families or for institutional investors. These are not retail funds, so this fits well with Cayman's market which is predominately directed at servicing institutional and high net worth investors. The funds have been set up in order to take advantage of the structuring benefits of using a Cayman fund and are run by Brazilian managers and investment advisors so the capital ultimately flows back into the international markets.

In general, Brazil is continuing its growth story and has not been greatly impacted by the crisis, although there have been some issues with the Real currency. These however have not affected the country as a whole.

Matthias Knab

We already touched about AIFMD, Dodd-Frank, FATCA, FIN 48 – what are some of the main aspects managers and investors need to know about these initiatives?

Andrew Stepaniuk

Of the regulatory initiatives you mention, by far and large, FATCA will pose the most immediate and significant challenge for global hedge fund managers and their service providers in 2012. Gathering and reporting the large amounts of information required in order to be compliant will be a massive undertaking. From the perspective of industry participants, no one will be immune from its requirements - from investment managers and custodians, to administrators and Directors, all are going to have to understand the corporate reporting requirements that the legislation is bearing upon them.

KPMG recently surveyed the leading fund promoters in 12 countries, who indicated only 10% have already conducted a FATCA impact analysis. FATCA takes effect on January 1, 2013. The survey results indicate there is a whole lot of work firms need to do to ensure compliance with the legislation

within the next 12 to 15 months. Planning for implementation will need to start as soon as possible, but only once firms have thought through what their fundamental objectives and strategies are.

Because the operational changes required by FATCA are so far reaching, senior executives must fully consider the fundamental strategic issues facing their organizations. All companies and funds are different, each with their own particular circumstances, business models, objectives and key stake holders. The last thing you want to do is start implementing costly changes to your operational structure only to later determine the results do not match your longer term strategic initiatives. There is no 'one size fits all' solution that is practical or possible – each analysis and implementation plan will be unique.

The legislation requires additional information reporting and withholding requirements for all 'foreign financial institutions' (FFI's). All non-U.S. entities, including non-U.S. domiciled investment funds will be deemed FFI's. Neither the Cayman Islands, nor any other non-U.S. jurisdiction is immune. This is a global issue. Essentially, if an FFI fails to comply by entering into an agreement with the IRS (an FFI Agreement), significant withholdings on all U.S. source income and/or gross proceeds on the disposition of U.S. securities will apply. Non-compliance will be very economically punitive, so much so that non-compliance will not be an option.

There is indeed, still a lot of work to do.

Of the regulatory initiatives you mention, by far and large, FATCA will pose the most immediate and significant challenge for global hedge fund managers and their service providers in 2012. Gathering and reporting the large amounts of information required in order to be compliant will be a massive undertaking. From the perspective of industry participants, no one will be immune from its requirements - from investment managers and custodians, to administrators and Directors, all are going to have to understand the corporate reporting requirements that the legislation is bearing upon them.

KPMG recently surveyed the leading fund promoters in 12 countries, who indicated only 10% have already conducted a FATCA impact analysis. FATCA takes effect on January 1, 2013. The survey results indicate there is a whole lot of work firms need to do to ensure compliance with the legislation within the next 12 to 15 months. Planning for implementation will need to start as soon as possible, but only once firms have thought through what their fundamental objectives and strategies are.

Because the operational changes required by FATCA are so far reaching, senior executives must fully consider the fundamental strategic issues facing their organizations. All companies and funds are different, each with their own particular circumstances, business models, objectives and key stake holders. The last thing you want to do is start implementing costly changes to your operational structure only to later determine the results do not match your longer term strategic initiatives. There is no 'one size fits all' solution that is practical or possible – each analysis and implementation plan will be unique.

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Andrew Stepaniuk



Ingrid Pierce

From the fund's perspective, the main person responsible for liaising with the investors in relation to this issue will be the administrator. I suspect administrators will bear the greatest burden, and funds will need to ensure that this service is covered by the admin agreement. It will be interesting to see

whether administrators will look for additional fees to provide this service or perhaps greater limitations on their liability. We may well see some tension around those issues.



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Ingrid Pierce

To pick up on Andy's points, I also believe that the liaison between the Directors and the audit firms will become even closer. Directors will need to be satisfied that they have a really good audit firm in place who is well versed in all the new regulations, because ultimately the Directors will have to sign off on the fact that all the appropriate agreements are in place between the foreign financial institution and the IRS.

Greg Bennett

Andy and Ingrid are spot on. This is definitely on our radar and we have already had discussions with investment managers, administrators, lawyers and auditors on this issue. Further, Andy and his professional audit colleagues have been holding information sessions on this matter for some time, helping the various industry participants better understand the implications.

Andrew Stepaniuk

Just to be clear, if you are an FFI dealing with U.S. securities and you do not comply with the FATCA reporting requirements, the penalty could be as high as 30% withholdings on U.S. sourced income, or proceeds from sales of U.S. securities irrespective of whether there are any gains, which would be extremely punitive to any non-U.S. fund. This provides a lot of motivation to get industry participants started and focused on preparing their FATCA implementation plans over the coming year.

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Andrew Stepaniuk

Matthias Knab

Each time I am on Cayman I am impressed by the broad and deep range of financial service providers you can offer from here, and more how the different firms and sectors are forming in fact highly efficient and cooperative clusters which makes them very competitive on a global measure. Greg's reference just now to how Andy's group is educating the Directors is a perfect example for that. Can you give us more insights and examples how you all work together through the different formal and informal gatherings and industry groups here on Cayman?

Ingrid Pierce

It is true that the industry in Cayman is quite close knit and there is a strong network across service providers and also within each sector – i.e. the law firms communicate with each other on key issues and we speak to the independent Directors, the administrators, the audit firms and so on.

There are multiple forums that facilitate these dialogues and exchanges. For example, the Cayman Chapter of AIMA hosts educational sessions for the local industry and they are very well attended. Walkers has its own Know-How training sessions and is represented on AIMA and on the Financial Services Legislative Committee of the Cayman Islands. Whenever there is any new piece of legislation or regulation in the works, either from onshore or offshore with the potential to affect our clients, all of us engage in a broad range of discussions and try to have legislation enacted which is helpful to the sector.



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Ingrid Pierce

We also participate in webinars and other educational forums. Walkers is a member of the Managed Funds Association in the U.S. We also speak on regulatory changes at events produced by the Regulatory Compliance Association. So, all of us here in Cayman are very engaged and tuned into what is going on globally, and we share that information quite readily through white papers and reports.

Greg Bennett

It is also important to note that industry engagement is not simply local, we reach out to and engage with constituents across the global industry, including investors, investment managers, and onshore council and auditors.

Andrew Stepaniuk

From the auditors' side it is the same, for example any firm with an international network like KPMG that deals with Cayman funds globally is constantly engaged in an ongoing collaboration and education between countries. All of us are engaged not only at a local level, on Cayman issues, but at an international level there is a high level of collaboration and exchange of information. If an auditor works on part of the books and records in Hong Kong for a Cayman domiciled fund, there will be a fair amount of discussion and collaboration going back and forth between their teams and our teams on both Cayman and Hong Kong related regulatory matters as applicable.

Matthias Knab

Are there any new developments from the regulatory side here on Cayman?

Ingrid Pierce

There is a proposed amendment to the Mutual Funds Law which includes the regulation of master funds in Cayman. We are in the consultation period at the moment; the private sector has been in discussions with the government and CIMA about how this might operate in practice.

Andrew Stepaniuk

The background of this is that various international bodies have provided commentaries post financial crisis on a number of different issues related to regulation, and while many global regulatory bodies have been quite positive on Cayman as of late, an area of potential improvement was to increase the regulatory status of master funds to address a small gap. Between the where the trading assets reside and the regulated feeder funds.

That is, CIMA presently regulates the feeder funds where investors come into a fund, but if all the proceeds are passed onto and all the trading assets actually reside at a master fund level, there is presently no mandatory CIMA oversight. This a possible way for CIMA to tie in the actual trading assets in a typical master feeder structure to the Cayman Islands existing regulatory regime.

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Andrew Stepaniuk



Matthias Knab

How is this particular initiative viewed by the industry here?

Ingrid Pierce

Regulation for the sake of regulation is never a great idea, but if it contributes to a better regulatory regime and offers some additional protection for investors there could be some benefits.

Ultimately we don't believe this will have a massive impact on the industry or on existing fund managers but we can't make an informed comment until we see the drafting.

Greg Bennett

CIMA has also publicly stated that they are looking at the Director regime in Cayman post Weaving and that they may do something to improve the standard of corporate governance. That said, I believe what is being considered revolves around increased transparency, which has general support. In addition, there is an allocators' working group made up of some of the largest hedge fund investors globally, and they have also been pushing for increased transparency in relation to independent Directors. Ultimately what these investors would like to see is more disclosure in relation to a fund's Directors, including having Directors disclose what they believe their obligations are, how they discharge these obligations as well as detail their client acceptance policies and procedures.

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The allocators group also seeks full disclosure of conflicts of interest, including any relationships the Directors may have to the investment manager or to any of the other service providers to the fund. The group would also like information on the structure of the Directorship business, including the model (i.e. professional services firm model versus a standalone provider), how many Directors and support staff does the firm have, and of course, the big question, how many Directorships does each Director hold.

Greg Bennett

From Harbour's perspective, we support this initiative as we believe investors should be able to obtain information necessary for them to make appropriate investment decisions. We are also not seeking clients that are considering independent Directors just as part of a due diligence check the box exercise. Investment managers should understand that independent Directors perform a significant and critical function and that having a robust corporate governance framework is important and beneficial to all parties.

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Matthias Knab

The investor or allocator group that you mention, is that a formal association or more an informal group?

Greg Bennett

It is an informal group of 20 or 25 large allocators that represent about \$300 billion of invested money..

Matthias Knab

Greg, you already hinted at that one – the million dollar question is obviously how many funds can a Director really serve as an Independent Director. What is your take on that?

Greg Bennett

Correct, how many funds can a Director really serve as an Independent Director for is the key question being asked by investors and considered by independent Directorship providers. The reason that it generates such consideration is that there really is no simple answer on the issue. There are a number of reasons for this, including that the time and effort required to discharge one's obligation varies by structure. For example, a Segregated Portfolio Company can have numerous trading portfolios that are effectively each a separate fund, however this would count as a single position if you just counted legal entities. Similarly, someone might be the Director on say 20 funds serviced by a single investment manager - in which case there are many synergies that arise from having a single set of operational controls, service providers and trading strategies. As such, these funds can be reviewed and considered as a group. On the other hand, if those 20 funds were separate unrelated standalone funds, each one would have a different operating environment and operational structure, and you would have to consider and evaluate each individually.

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As such it seems that most interested parties are starting to look at the number of underlying manager relationships as opposed to strictly counting the number of funds.

I also think that careful thought should be given to whether or not having professional support infrastructure allows for a higher number of Directorships. The fact is, and as was noted in the Weaving judgment, industry wide events like the 2008 financial crisis can demand the care and attention of the Director (and not his or her designates or support staff) for every fund they service around the same time, and at the end of the day this needs to be considered and incorporated into any analysis of numbers.

Greg Bennett



As such it seems that most interested parties are starting to look at the number of underlying manager relationships as opposed to strictly counting the number of funds. Of course as with anything, numbers can be deceptive and investors that are considering the matter will ultimately need to talk to the Directors in order to gain a meaningful understanding of what the number means in terms of their ability to effectively discharge their obligations.

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Matthias Knab

What is the current situation with the immigration law that sets limits for expatriates, which is also known as the rollover policy? I understand this rollover policy was initiated to prevent the majority of foreigners from remaining in the Cayman Islands 10 years or more consecutively and thus earning the right of security of tenure.

Andrew Stepaniuk

Correct, the Cayman Islands government has introduced a temporary suspension of the rollover regime which has been in place for a numbers of years. We have a substantial number of expatriate workers that will reach their term limit in the next couple of years, and at the same time the government has recognized it has become more and more difficult to attract the top international talent. Therefore, the government is looking for a more workable solution to keep talent in Cayman longer.

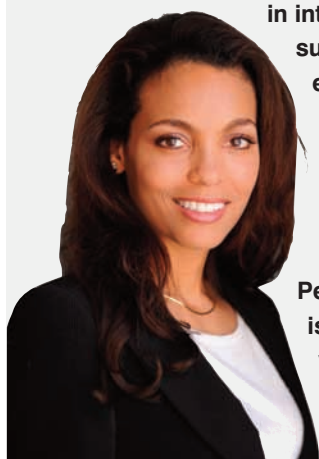
Greg Bennett

The government is very supportive of attracting new businesses and there is all kinds of assistance available for those that are interested in coming to Cayman to start a business, particularly in the financial sector. So, this is definitely a very real option for investment managers for example who want to re-domicile and establish their business here in Cayman.

Ingrid Pierce

Cayman has an extremely capable talent pool for such a small jurisdiction. Inevitably when you compete in international markets you have to have the best in every sector. Thus far, Cayman has been successful in bringing top international talent to the Island to complement the existing local expertise, and this is evident from the overall service levels in the Cayman market. Those capabilities were potentially threatened or at least hampered by having a term limit, which caused the government to reevaluate whether the immigration rules were really working efficiently. The government has therefore proposed some changes which should have a positive impact on the financial services industry.

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Ingrid Pierce

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Matthias Knab

So apparently you are not running into the same trap as for example some places in Switzerland like Zug or Geneva that try to attract international hedge funds but then their staff trying to relocate there has issues getting appropriate housing and putting their kids into the international schools?

Ingrid Pierce

There is certainly no difficulty in finding suitable and high quality accommodation.

Greg Bennett

There are also no restrictions on purchasing real estate, we have a number of first rate international schools, excellent infrastructure and there are a number of daily flights to the U.S., including daily service to Miami, which is only 60 minutes away by air. As a result, we have all of the things an investment manager, or any business owner, would be focused on when considering relocating.

Matthias Knab

Correct, I have seen that also some fund management companies have their full operation here on Cayman.

Ingrid Pierce

We have always had professional services firms, insurance groups or other blue-chip organizations operating here in Cayman. As in all jurisdictions, during the financial crisis some businesses departed, but a fair number of international businesses have recently established here, many of them investing large amount of capital and resources, all of which is very positive.

Matthias Knab

The European UCITS funds have become a global success. There are about 1000 UCITS funds out there, and managers from all parts of the world keep issuing them. With an UCITS fund, managers can diversify their investor base and offer absolute return strategies to investors that otherwise may not be able to invest in offshore funds. How does the global success of UCITS affect Cayman?

Ingrid Pierce

The regimes are in fact complementary and managers who look for diversification through a UCITS fund structure will frequently maintain their Cayman structure.

We found that this has become the operating model for the majority of managers, i.e. to utilize both products. In general they have not re-domiciled any funds or assets away from Cayman. If they have the right product and investor base, in time they might also look at establishing a UCITS fund as well. Our Irish funds lawyers are doing this for a number of our larger clients.

Andrew Stepaniuk

KPMG and RBC Dexia published a study recently that looked at any movement in fund products between the offshore and onshore jurisdictions involving UCITS. In almost all instances UCITS products were identified as complementary structures to existing offshore fund products employed by various managers. Basically, UCITS funds have allowed investment managers the ability to access a different investor base that was not, for various reasons, investing in their existing offshore products.

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