

FICTION and FACT

The Financial Times and Cayman Islands Hedge Fund Transparency

12th February 2013

The Financial Times	Fact
<p>1. "The Cayman Islands thanks to a light touch some would say no touch-tax and regulation regime".</p> <p>2. "The Caymanian plan to increase transparency in corporate governance rules will help investors verify that the directors ostensibly representing them have the ability and indeed time to discharge that duty".</p> <p>3. "Why anyone would entrust their money to funds whose directors they know nothing about is a puzzle".</p>	<p>1. 60% of Cayman Islands assets under management are invested through fund managers in the US, 20% in the United Kingdom and 20% in Asia and elsewhere. The investment of these assets is regulated by the SEC, CFTC, FSA and others under the laws of those jurisdictions. No additional prudential regulation is required in the Cayman Islands. Taxes are paid on profits made in accordance with the laws of those jurisdictions. The Cayman Islands does not impose an additional layer of taxation.</p> <p>2. The Cayman Islands Mutual Funds Law requires an offering document with full disclosure of the identity and background of all directors of a Cayman Islands hedge fund which document is reviewed and accepted by a prospective investor. This provision in 1993 codified the common law and has thus been a requirement of Cayman Islands law from inception. CIMA proposals effect no change to this disclosure requirement. Any investor may under existing law and regulation make due enquiry of a director as to the number of directorships held. All directors of a Cayman Islands company are subject to fiduciary duties and duties of care and skill substantially similar to those laid down under English authority.</p> <p>3. But not as big a puzzle as to why the editor of the Financial Times in the light of the foregoing point should suggest this supposition should possibly be of application to a Cayman Islands hedge or mutual fund.</p>

<p>4. "Transparent corporate governance is one thing; transparent company accounts is another".</p> <p>5. "The diminutive tax haven's minimal disclosure requirements and tough corporate privacy laws".</p> <p>6. "They even featured in rancorous debates over the tax affairs of US Presidential candidate, Mitt Romney".</p> <p>7. "Many of the world's largest pension funds have until now had no way of verifying details of Cayman Islands funds they invest with or their directors".</p> <p>8. ""We have been screaming for more transparency for some time now" said Vincent Vandenbroucke, head of operational due diligence at Hermes BPK".</p> <p>9. "Beyond such numbers however, little information has been historically available making the Islands an easy locale in which to secrete money and assets away from prying eyes".</p> <p>10. "For investors, one of the most critical elements has become understanding who their fund's Caymanian directors are".</p>	<p>4. All Cayman Islands hedge funds are required by the Mutual Funds Law to have audited accounts prepared by recognized and major audit firms and signed off by their Cayman Islands affiliate firms. The Madoff scheme could not have occurred in the Cayman Islands.</p> <p>5. Nothing could be further from the truth. The Cayman Islands has complete transparency in relation to tax matters with over 30 G20 and other countries including the USA and the UK and full automatic disclosure reporting in relation to bank account information with all European Union Treasuries. There are all encompassing all crimes anti-money laundering provisions with the USA and the highest level of domestic anti-money laundering legislation far exceeding that in effect in the United States of America, notably Delaware.</p> <p>6. It appeared from those debates that Mr Romney's affairs were perfectly legitimately structured in the Cayman Islands and that all due taxation was paid by him in relation to his affairs under United States tax law.</p> <p>7. This is only correct if we assume that the investors were incapable of reading the required offering memorandum and of undertaking any due diligence in relation to it.</p> <p>8. See above at 7.</p> <p>9. In addition to the tax transparency treaties above mentioned, the Cayman Islands Monetary Authority has full IOSCO membership and therefore full regulator to regulator disclosure in relation to all regulated entities including hedge and mutual funds. The Financial Times statement is correct only in that journalists and others in the private sector who are not investors may not enquire directly as to fund operations as the Cayman Islands provide legitimate confidentiality.</p> <p>10. This information is all fully disclosed in the offering memorandum which forms the basis of the contract on which the investor invests.</p>
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<p>11. "Indeed, Cayman fund boards staffed by directors are the only protection investors have against unscrupulous managers who may try to fiddle performance numbers or worse, steal assets".</p> <p>12. "Under the current long standing regime, information on who fund directors are has been thin on the ground. Due diligence is more a matter of detective work than fact checking".</p> <p>13. "There have been horror stories".</p>	<p>11. The role of the directors in relation to most hedge funds is supervisory only. The administrator, the prime broker, and the auditors and now under the EUAIFM, the distributor, all have direct responsibility for safe guarding assets.</p> <p>12. It is a matter of reading the offering memorandum and applying appropriate due diligence prior to, or at any time after, investment.</p> <p>13. Notably, consequent on the financial crisis, only one major case came to court in the Cayman Islands, <u>Weaving (now reversed on Appeal)</u>, in which delinquent directors who failed to perform their duties were found liable. During the crisis, hedge funds, as did many financial institutions, suffered liquidity issues which triggered gating provisions in their constitutional documents which operated as they were intended. All such provisions would have been duly disclosed in the offering documentation and therefore, constituted legitimate and accepted investment risk.</p>
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