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CIMA Consultation on Corporate Governance Statement of Guidance for Mutual Funds

Background

Following receipt of feedback on its January 2013 consultation on corporate governance for the financial services industry, the Cayman Islands Monetary Authority (“CIMA”) has proposed a Statement of Guidance on Corporate Governance specifically for Mutual Funds (“SOG-MF”). The SOG-MF provides for the first time in the Cayman Islands bespoke guidance on corporate governance standards specifically for the mutual funds industry. The SOG-MF will extend not only to licenced funds, but also to Cayman registered and administered funds (“Funds”).

The proposed SOG-MF was issued to industry for consultation which closed on August 16th 2013 and a finalised version is expected from CIMA in due course. Set out below are the principal features of the proposed SOG-MF in its current form.

Proposed SOG-MF

Once finalised, the SOG-MF will provide high-level guidance on the corporate governance standards expected in the oversight of Cayman Islands-registered Funds, including detail on the primary duties applicable to the directors, general partner or trustee of a Cayman Islands-registered Fund (each an “Operator”).

The SOG-MF will set out to provide clarity on what the primary Operator’s duties are (including those imposed by common law and recently discussed in the Cayman Courts in the Weaving judgement), as well as to guide Operators and service providers on

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corporate governance standards. The SOG-MF is not a codification of and does not amend the existing law of the Cayman Islands.

The objectives of the SOG-MF are as follows:

- ❑ To promote and enhance market confidence by confirming and clarifying the corporate governance standards required from Operators;
- ❑ To review international developments on corporate governance to ascertain what is relevant to adopt in the Cayman Islands to allow Cayman to maintain its position as a leading international financial centre;
- ❑ To protect the reputation of the financial services industry of the Cayman Islands by confirming corporate governance standards and guiding the sector to continuously adopt internationally-accepted standards; and
- ❑ To act in the best economic interests of the jurisdiction.

Highlights of the proposed SOG-MF

- ❑ The SOG-MF applies to administered and registered mutual funds in the Cayman Islands. A licenced fund will continue to be guided by the Statement of Guidance – Corporate Governance for licensees of CIMA, but may look to the SOG-MF for additional guidance.
- ❑ The SOG-MF is not intended as a prescriptive or exhaustive guide to CIMA's governance expectations.
- ❑ The governance structure of a Fund must be appropriate and suitable to ensure the effective oversight of the Fund. The size, nature and complexity of the Fund are fundamental factors in determining the adequacy and suitability of its governance framework.
- ❑ Where the governance of a Fund does not meet the governance standards endorsed by the proposed SOG-MF it is open to CIMA to cancel any Fund licence or registration, impose conditions on any licence held by a Fund (or to amend or revoke those conditions), to require the substitution of any promoter Operator of the Fund, appoint a person to advise the Fund on the proper conduct of its affairs and appoint a person to controls the affairs of the Fund.
- ❑ It is the view of CIMA that the Operators are the directing will and mind of a Fund.

Oversight by Operators under the SOG-MF Proposal

- ❑ Operators are responsible for ensuring the Fund conducts its affairs in accordance with all applicable laws, regulations, rules and standards.
- ❑ Operators should monitor compliance with the laws, regulations, rules and standards, including anti-money laundering and terrorist financing requirements. Operators should request appropriate information to enable on-going and effective monitoring of compliance with these laws rules and standards.
- ❑ Operators must ensure that they put in place a conflicts of interests policy and adhere to this.
- ❑ Operators must enquire into the affairs of the Fund, requesting information from service providers for Operator meetings, together with their presence at Operator meetings where necessary.
- ❑ The Operator should require regular reporting from the Funds' investment manger and other service providers to enable it to make informed decisions and to adequately oversee and supervise the Fund.
- ❑ Operator meetings should be held regularly at intervals sufficient to enable the Operator to carry out its role effectively, requesting the presence of a service provider where necessary.
- ❑ Operator meetings should be held at least twice a year and more often where the circumstances or the size, nature and complexity of the Fund necessitate it.

Duties of Operators under the SOG-MF Proposal

- ❑ The Operator must exercise independent judgement and act in the best interests of the Fund, taking into consideration the interests of the Fund's investors as a whole.
- ❑ The Operator must operate with due skill, care and diligence.
- ❑ The Operator must communicate openly with Fund investors and act honestly and in good faith at all times.
- ❑ The Operator must ensure he has sufficient time to complete his responsibilities as an Operator of each Fund he is appointed to.
- ❑ The Operator is responsible on a continuing basis for ensuring that the constitutional and offering documents of the Fund comply with Cayman Islands law (including ensuring that the investment strategy is clearly described in the offering documents) and, for licenced funds, CIMA's Rule of Contents of Offering Documents. The Operator should continuously verify that the Fund is acting in accordance with its constitutional documents and any other documents directing the supervision and operation of the Fund and/or its advisors or Service Providers.

- The Operator retains responsibility for delegated functions and must monitor and supervise delegated functions appropriately, and on a continuing basis, including monitoring whether the investment manager is performing in accordance with the defined investment criteria and restrictions.
- The Operator is responsible for approving the appointment and removal of, and continuously assessing the suitability and capability of, the Fund's service providers;
- The Operator is responsible for ensuring that the role and responsibilities of the Fund's service providers are clearly set out and defined. The Operator must satisfy himself that the service provider contracts ensure a proper division of responsibilities and such service providers are performing their functions in accordance with the terms of their contracts.
- The Operator should continuously inform himself of the Fund's investment activities and financial position and review the Fund's financial results at their Board meetings.
- The Operator should monitor the Fund's compliance with its investment strategy, criteria and restrictions and well as its net asset valuation policy and the calculation of its net asset value.
- The Operator must ensure that all potential or actual conflicts of interests are managed and controlled.
- The Operator must exercise care, skill and diligence that would be exercised by a reasonably diligent person with the general knowledge skill and experience that may reasonably be expected of an Operator and the general knowledge, skill and experience that the Operator has.

Documentation under the proposed SOG-MF

- The Operator must fully, accurately and clearly record the Operator meetings and any material decisions and/or considerations.
- Records should include agenda items, circulated documents, matters considered, decisions made, and information requested from and provided by service providers.

Relations with CIMA

The Operator must conduct its affairs with CIMA in a transparent and honest manner, always disclosing to CIMA any matter affecting the financial soundness of the Fund and any non-compliance with the laws, regulations, rules and standards applicable, including those of the Cayman Islands and CIMA. Where the Board is uncertain about whether to communicate certain information to CIMA it should be prudent and diligent and report such information to CIMA.

Risk Management

The Board Operator should ensure it provides suitable oversight of risk management and maintain a sound system of risk measurement and control.

How Dillon Eustace Can Help

To assist in compliance with the SOG-MF when it is finalised, an Board Operator should ensure that Directors are it is aware of the relevant policies and procedures that apply to their Fund and can avail of adequate and sufficient training to enable them to discharge their duties.

In advising clients in relation to complying with the SOG-MF and its various requirements, Dillon Eustace has identified a number of key areas in which boards Operators might consider formal training in relation to their commitments under the SOG-MF and, more generally good corporate governance for their Board.

Dillon Eustace can tailor a training programme to suit the needs of your board and deliver it in a confidential interactive setting in which directors will have an opportunity to raise issues that are of concern to them. These training sessions can be arranged to tie in with your Bboard Mmeetings either in here in our Cayman Islands offices, or can be delivered at any other convenient location. Some of the topics in which Dillon Eustace can provide training include:

-  Understanding the Board's Role
-  Creating and Maintaining an Effective Board
-  Operating an Effective Board
-  Monitoring Risk

In addition to training, Dillon Eustace can provide and tailor support documentation for directors, including Board Operating Procedures, Board Policies and relevant compliance manuals, each reflective of client requirements as well as the requirements of the finalised SOG-MF.

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