

# Cayman Funds Quarterly Legal and Regulatory Update Q3

Insights - 28/11/2017

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## 1. The Anti-Money Laundering Regulations, 2017

1.1 The third quarter of 2017 has seen a further strengthening of the Cayman Islands' regulatory framework to maintain the jurisdiction's adherence to international standards and the recommendations of the Financial Action Task Force (**FATF**). The FATF sets the global standard for legal, regulatory and operational measures against money laundering, terrorist financing and the proliferation of weapons of mass destruction - collectively and commonly referred to as **AML/CFT**. The Cayman Islands will undergo a FATF evaluation in December 2017.

1.2 The Anti-Money Laundering Regulations, 2017 (**AML Regulations**) came into force on 2 October 2017 repealing The Money Laundering Regulations (2015 Revision). The AML Regulations have expanded the scope of the previous regulations in line with the FATF recommendations. Specifically and significantly the definition of activities covered by the AML Regulations, being 'relevant financial business' now includes (i) otherwise investing, administering or managing funds or money on behalf of other persons' and (ii) underwriting and placement of life insurance and other investment related insurance". This means that both regulated and unregulated investment entities, insurance entities and finance vehicles now will be subject to the AML Regulations and the mandatory procedure obligations. Insurance entities, finance vehicles and unregulated investment entities not previously subject to the AML/CFT regime have until 31 May 2018 to implement

appropriate procedures (or delegation arrangements) to comply. The AML Regulations have introduced expanded provisions on risk-based approach and enhanced due diligence. In particular the mandatory AML/CFT procedures have been expanded with the addition of specific procedures for (i) adopting a risk-based approach in relation to the customer, its business and transactions, (ii) employee screening procedures and (ii) conducting sanction and FATF non-compliant territory checks. A requirement for enhanced due diligence has been introduced where the risk assessment procedures determine that certain client relationships are higher risk for example for 'politically exposed persons' and their family member and close associates. Where an applicant for business is a legal person or arrangement, the identification and verification procedures will be applied to the beneficial owners or controllers. The AML Regulations adopt similar definitions for such concepts to those adopted under the FATF recommendations.

1.3 The list of jurisdictions previously approved by CIMA as having equivalent AML/CFT regimes to the Cayman Islands (commonly referred to as Schedule 3 countries) has been removed and is now maintained by the Anti-Money Laundering Steering Group, a body created under the Proceeds of Crime Law (Revised) (PCL), to enable more agile updates of the list. The current published list removes Mexico, Panama and Turkey as jurisdictions with equivalent regimes.

1.4 The AML Regulations significantly increase the penalties for breach to summary conviction with a fine of up to US\$500,000 or and indictable conviction with an unlimited fine and imprisonment of two years.

1.5 Further guidance relating to the applicability and interpretation of the AML Regulations is provided in the Guidance Notes on the Prevention and Detection of Money Laundering and Terrorist Financing (**Guidance Notes**). These are of significant importance to clarify and interpret the AML Regulations, particularly as the AML Regulations recognise that a court or supervisory body shall take into account any relevant and applicable supervisory or regulatory guidance notes for determining compliance with the AML Regulations. Draft Guidance Notes have been circulated by the Cayman Islands Monetary Authority (CIMA) for industry consultation and are expected to be published in the coming weeks.

1.6 For a further summary of the AML Regulations please see our client briefing - [Cayman Islands - The Anti-Money Laundering Regulations 2017](#).

## **2. Beneficial Ownership**

Clarifications to the Cayman Islands beneficial ownership regime which came into force on 1 July 2017 are to be made. Notably, the scope of the regime is to be extended such that legal entities or subsidiaries of legal entities that are registered as an excluded person under section 5(4) of the Securities Investment Business Law (2015 Revision) shall be in-scope entities for the purposes of the regime. Legal entities or subsidiaries of one or more legal entities regulated in one of the approved jurisdictions published from time to time by the Anti-Money Laundering Steering Group, shall not be in-scope.

In addition, corporate services providers in the Cayman Islands will be required to record in a company's beneficial ownership register details of all out-of-scope entities and the reasons for their exemption.

### **3 Digital, Blockchain and Fintech offerings in the Cayman Islands**

3.1 Cayman has seen a flurry of interest and a pipeline of pending projects in the blockchain and initial coin offering (ICO) market - see our client briefing [Building blocks for ICOs in the Cayman Islands](#). Ogier has established a dedicated Digital, Blockchain and Fintech team lead by a global team of partners specifically to assist clients operating or investing in businesses in the Fintech space. We have seen a great deal of interest in the new asset classes emerging in the investment funds sector such as cryptocurrencies and other blockchain-based currencies and digital assets and we are able to advise on all offshore legal and regulatory aspects of these evolving structures.

3.2 For further details of our Digital, Blockchain and Fintech team please see our dedicated webpage on [Ogier.com](http://Ogier.com) [here](#).

### **4. Foundation Companies**

4.1 The Cayman Islands Foundation Companies Law, 2017 (**Foundation Law**) has now come into force.

4.2 By enacting the Foundation Law, the Cayman Islands has introduced a novel form of vehicle into its legal system. A Foundation Company has features and flexibility that have been designed to allow a company, retaining separate legal personality and limited liability, to function like a civil law foundation or common law trust.

4.3 When looking at other jurisdictions, the approach taken by the Foundation Law is unique and it is hoped that the creative solution will appeal to many clients. It is expected that its uses may include operating as a holding vehicle for shares in a private trust company, as a protector or enforcer of a trust, as a special purpose vehicle in finance or commercial transactions, including in crypto-currency and other technology offerings, as well as a traditional succession planning vehicle.

4.4 It is possible to use Foundation Companies to act as "ownerless" vehicles that will make them, simple solutions in the context of private trust companies, management shares of investment funds, or in wider commercial transactions.

4.5 For further information on Foundation Companies please see our client briefing [A Guide to new legislation on Foundation Companies in the Cayman Islands](#).

### **5. Ocean Rig - Schemes of Arrangement**

5.1 In the largest ever Cayman Islands restructuring, Ocean Rig UDW Inc (**UDW**), a leading international contractor of offshore deep-water drilling services, and three of its subsidiaries have been successful in their application for the sanction of four schemes of arrangement by the Grand Court of the Cayman Islands, and recognition and enforcement of the schemes under Chapter 15 in the United States of America.

5.2 The schemes restructured the Scheme Companies' core financial indebtedness of approximately US\$3.7 billion (plus accrued interest), and sanction was given recently by the Grand Court of the Cayman Islands.

5.3 The four scheme companies were all originally incorporated in the Republic of the Marshall Islands. The parent company, UDW, transferred to the Cayman Islands by way of continuation as an exempted company in April 2016, in advance of the restructuring. Each of the subsidiary Scheme Companies were registered as foreign companies in the Cayman Islands in October 2016. As a result of the transfer (in the case of UDW) and the registrations (in the case of the subsidiaries), the four companies were able to benefit from the Cayman Islands' scheme of arrangement regime - of which there is no equivalent in the Marshall Islands - and also the well-established statutory framework and highly regarded Court system in the Cayman Islands. This represents the first ever 'light touch' provisional liquidation of foreign registered companies in the Cayman Islands. For further information please see our client briefing [Ocean Rig - Schemes of Arrangement in the Cayman Islands](#).

## **6. Carlyle Litigation**

6.1 The Carlyle Group, Carlyle Investment Management and TCGH, represented by Ogier's Global Head of Dispute Resolution Simon Davies, has won a civil case which was the largest in Guernsey's history successfully defending claims including that its management of a Guernsey fund, was in breach of duties alleged to be owed, that led to a total of investment capital in the 2008 financial crash.

6.2 A judgment handed down by Guernsey's Royal Court early in September has cleared the US investment firm, its investment manager and any holding company in the Carlyle Group together with the directors of Carlyle Capital Corporation (**CCC**) of liability over the collapse of CCC, a Guernsey investment fund that went into insolvency in the wake of the 2008 crash.

6.3 The case - valued at well over USD\$1 billion - is the largest in Guernsey's history by financial value, duration, the number of witnesses and number of documents filed. In all, more than 187 claims were pursued by CCC and its liquidators against its seven executive and non-executive directors, its investment manager (the Carlyle Group) as promotor of the fund and TCGH, a holding company in the Carlyle Group. The Royal Court's judgment comprehensively dismissed all claims considered at trial against each of the Defendants.

6.4 The court concluded "In a nutshell, CCC's original business model was reasonable...CCC's

directors ... made judgements to enable CCC to try to regain health and strength which were reasonable at the time. CCC failed because the depth of the weaknesses in the financial markets was so great that those weaknesses came to threaten ... their very viability, and hence to cause a systemic withdrawal of what had previously been a very normal, stable and reliable form of finance. ... To suggest that there was anything that they, or CIM, clearly ought to have done significantly differently from July 2007 until CCC's eventual collapse in March 2008 is, in my judgment, being entirely wise with hindsight.”

6.5 Obviously a decision of the Guernsey Royal Court, its discussion in the judgment on types of directors, fiduciary duties, duty of care and conflicts and disclosures will be of interest to offshore funds and their directors as such authority is likely to be persuasive in the Cayman Islands. It will also be of interest to the courts of other offshore jurisdictions and provides guidance on the scope of their duties. Ogier will be publishing a series of client briefings reviewing the decision.

If you require further information, please speak to your usual Ogier contact or a member of our team listed here.

## About Ogier

Ogier is a professional services firm with the knowledge and expertise to handle the most demanding and complex transactions and provide expert, efficient and cost-effective services to all our clients. We regularly win awards for the quality of our client service, our work and our people.

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