

E-Reporting for Cayman Islands Monetary Authority Regulated Funds

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Background

Which country was discovered by Christopher Columbus, has a political party led by Mr. Bush and is in the top five largest financial centers in the world? A more obvious question: Which country is the domicile of choice for approximately 80 percent of the world's hedge funds? In both cases, the answer is the Cayman Islands, a growing center for a number of fund types.

The number of regulated funds domiciled in the Cayman Islands has shown explosive growth over the last few years, growing from under 2,000 at the start of 1999 to more than 8,000 by the end of 2006. The challenge of regulating these funds has fallen to the Cayman Islands Monetary Authority (“CIMA,” or “the Authority”).

In order to enable it to regulate this large and growing number of funds, CIMA recently required electronic reporting (“E-Reporting”) for all of its regulated mutual funds.

“The Authority believes that E-Reporting will provide both reliable aggregate statistics relating to the Cayman fund industry (which, to date, has not been possible), and permit the Authority to conduct its supervisory and cooperative responsibilities more efficiently and cost-effectively.” (CIMA—Consultation on Electronic Reporting Initiative for Investment and Securities Division letter—January 20, 2006)

History and Development

In early 2006, CIMA proposed E-Reporting in a consultation document which explained why such a system was required:

- (i) **Managing the Exponential Growth in New Funds**—Technology enables CIMA to cost-effectively manage the large and growing number of funds.
- (ii) **Better Understanding of the Fund Industry**—The hedge fund industry and supranational bodies increasingly seek aggregate statistics and trends. Aggregated, automated collection and analysis of data makes it possible to provide this information.
- (iii) **Timely and Accurate Filings**—Regulated funds must file audited financial statements with CIMA within six months of the end of the financial year and also keep CIMA up to date with any material changes to fund operations. Electronic submission helps to ensure that CIMA receives timely information.
- (iv) **Business Continuity**—Receiving and maintaining information electronically assists CIMA's business continuity plans.

The consultation document was followed by a press release in August 2006 and a letter to operators of all CIMA-regulated funds in October 2006. These documents provided an update to the industry on the implementation and the “who, what, when, why and how” of E-Reporting. In the meantime, CIMA worked with the major financial centers and other stakeholders to ensure transparency of the E-Reporting process and to address any concerns. The initiative also was featured in CIMA's quarterly newsletters.

The “Mutual Funds (Annual Returns) Regulations, 2006,” officially announced by CIMA in late 2006, requires a regulated mutual fund's operator (e.g., a director if the fund is a company; the trustee if it is a trust; or the general partner if it is a partnership) to submit to CIMA an accurate and complete Fund Annual Return (“FAR,” previously referred to as the “Key Data Elements Form” in the October 2006 letter to fund operators) within six months after the end of the relevant financial year. The FAR is to be submitted in electronic format through the fund's Cayman Islands auditor. Notably, the legislation emphasizes that “... such auditor shall not be liable for the accuracy or completeness of any returns submitted by him ...”

In addition to the FAR, each fund is required to submit its audited financial statements electronically as an Adobe Acrobat PDF through its Cayman Islands auditor. The E-Reporting submission must include both the FAR and the financial statements and will not be accepted by CIMA unless both are submitted.

Fund Annual Return

The FAR is a Microsoft Excel-based document, featuring several drop-down choice boxes. It is separated into standing data (which probably will not change

significantly from year to year) and financial data (which can be extracted easily from the fund's financial statements). The standing data is further broken down into four sections:

- (i) **Identification of the fund**—Fund name, certificate number and information about operating structure.
- (ii) **General information**—Fund details (investment strategy, any stock exchange listing, GAAP, GAAS, minimum subscription, etc.), details about the fund's operators, the investment manager, the fund administrator, the registered office, the Cayman Islands legal counsel and the auditor.
- (iii) **Operating information**—Has there been any suspension of trading, regulatory investigations, changes in offering documents or imminent termination in activities?
- (iv) **Operator responsible for filing**—Name, position, e-mail address and completion date.

The financial data include information relating to the change in net assets of the fund during the reporting period as well as a high-level reporting of the fund's investment portfolio and details of four common fees (management, performance, administration and professional fees). This information normally would be readily available from the fund's financial statements. There also are certain macros contained in the document to ensure that completion of the FAR is as straightforward as possible.

CIMA has issued guidance notes (the "notes") and directions for completing the FAR. They clarify that, although the fund's operator has legal responsibility for the completion and accuracy of the FAR, it may delegate completion to a service provider. E-Reporting is required of all funds with a year-end on or after December 27, 2006.

Comments or questions concerning the FAR can be made by e-mail (ereporting@cimoney.com.ky) or by calling the CIMA analyst responsible for the fund.

Umbrella Structures

In instances where the fund is an "umbrella-type" structure and presents its subfunds within one set of financial statements, the fund may file one FAR for all the subfunds if the nonfinancial data (i.e., standing data) are substantively similar for each subfund. If financial data for each subfund is not aggregated in the fund's financial statements, the fund's operator will have to aggregate the relevant financial information for each of the subfunds in order to complete the FAR.

If stand-alone separate financial statements for each subfund in an umbrella structure are prepared, then a FAR is required to be submitted

for each subfund, along with the PDF financial statements for each subfund.

Auditor Interface

The Cayman Islands firm of PricewaterhouseCoopers ("PwC-Cayman") has designed a system whereby a fund's operator or its designee can send the completed FAR and PDF of the financial statements to a dedicated PwC-Cayman e-mail address (efiling@ky.pwc.com). PwC-Cayman will acknowledge receipt of the documents and file the FAR and the financial statements on behalf of the fund. CIMA's system will generate an acknowledgement e-mail once PwC-Cayman has filed the documents. If CIMA has any follow-up questions, it will contact the operator based on the information provided in the FAR.

In order to keep the incremental fee for PricewaterhouseCoopers' involvement in the E-Reporting process as low as possible, the Firm has decided that it is not necessary for other PricewaterhouseCoopers network firms to be involved.

Conclusion

CIMA is cognizant of the Cayman Islands' preeminent position in the funds industry and, after careful consideration, decided that the improvement in the informational system was necessary and will provide significant benefits that outweigh any increased regulatory burden and cost to industry. In the words of Gary Linford, CIMA's former Head of Investments and Securities, "Many of the investment managers and service providers with whom we have had dialogue are relieved to hear that meaningful statistics on the industry will soon be available from a credible source."

Copies of all the above-referenced documents and information are available at www.cimoney.com.ky. ■

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