

Regulatory Update Q2



Welcome to Athena's quarterly industry update!

It is our pleasure to present this summary of the latest legal and regulatory developments in the Cayman Islands affecting the alternative investment industry. The environment is changing more rapidly than ever in these extraordinary times and, whilst there are many specific updates available, we wanted to let you have an outline of the key changes to ensure that you are aware of the major developments during Q2.

As background to many of the legislative developments this past quarter, you will be reminded of Cayman's ongoing efforts to bolster its regulatory framework and respond to various recommendations of the Caribbean Financial Action Task Force (CFATF) and the Financial Action Task Force (FATF) on anti-money laundering, countering the financing of terrorism and countering proliferation financing (AML/CFT/CPF), virtual assets, private funds and more. In conjunction with these efforts, the Cayman Islands government remains in close contact with the EU Commission and is making progress towards proposals, which the government believes, will result in the removal of the Cayman Islands from the list of non-cooperative jurisdictions at the next available opportunity, which is expected to be as early as October.

Cayman COVID-19 Update: The Cayman Islands government continued its successful efforts with the phased reopening of the Cayman Islands local economy. With the daily number of positive COVID-19 cases being between zero and the low single digits the country continues to ease local restrictions and is currently operating under a suppression level 2. It is anticipated that further lifting of restrictions will continue, however the Cayman Islands borders remain closed at this time.

Disclaimer: The information provided does not, and is not intended to, constitute legal advice, instead, the information herein is for general informational purposes only. Please contact your usual Cayman counsel for specific legal advice on any of the matters outlined below.

PRIVATE FUNDS (AMENDMENT) LAW 2020

The Private Funds Law, 2020 (PF Law) was recently amended to clarify the position for certain entity types and to broaden the definition of "private fund" to extend to additional entities.

The PF Law was passed earlier this year to enhance the oversight of investment funds in response to the evolution of global regulations and recommendations and drive towards tax neutrality and to fulfill the Cayman Islands' commitments regarding the EU's list of non-cooperative jurisdictions in tax matters.

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The PF Law came into force on 7 February 2020 with the effect of bringing in certain closed-ended entities, including most private equity, infrastructure and real estate fund structures within the scope of a regulatory regime in the Cayman Islands for the first time. Private funds have 6 months (7 August 2020) to register with CIMA and comply with the new Law.

The Ministry of Finance (Ministry) recently published an industry advisory summarizing the key changes to the definition of a “private fund” under the PF Law and the rationale behind the changes:

- **Amendment of the element of "offering and issuing" of investment interests to refer instead to vehicles that "offer or issue" investment interests.** Because a narrow interpretation of the term "offering" may result in some fund vehicles that are not engaging in a sales process that amounts to the offering of investment interests falling outside the definition of a private fund, the definition has been amended to include a vehicle that offers or issues investment interests.
- **Amendment of the issuing element to bring in scope entities that have "issued" investment interests (in the past), as well as those that "issue" investment interests.** The PF Law is intended to capture all private funds, including those existing funds that have in the past issued investment interests but no longer do so. The definition has been amended to remove any ambiguity in this regard.
- **Deletion of the "principal business" element.** The definition has been amended to delete the "principal business" aspect of the definition. Removing this element removes the need for private fund operators to take a view on what the current principal business of the vehicle e.g. is the principal business of the vehicle issuing interests or making investments or managing assets. This deletion also aligns with the addition of the past tense "has issued" language. The Schedule of Non-Fund Arrangements carves out arrangements not operated "by way of business" from the definition, so the Ministry does not consider that this amendment risks bringing non-commercial activities in scope of the PF Law.
- **Deletion of the "spreading investment risks" element.** The Ministry understands that there has been uncertainty whether a fund falls outside the scope of the definition where it invests only in one asset, or even one type of asset, as this could be said not to constitute the "spreading" of investment risks. The definition has been amended to delete this element to prevent these kinds of vehicles from automatically falling outside the scope of the PF Law (though some of them may, of course, then be exempted by virtue of the Schedule of Non-Fund Arrangements).

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- **Deletion of the element that investments are managed "for reward based on the assets, profits or gains of the company, unit trust or partnership".** The Ministry understands that this language is creating uncertainty as to whether all vehicles in a multi-fund investment structure are required to register, where manager fees are generally charged only at one level. The argument made is that investments at the other level are therefore not managed "for reward". Indirect reward, where the payment is made at the other fund level, should in the Ministry's view have been caught under the existing definition, but the Ministry believes the amendment should put the matter beyond doubt.

If your Cayman entities have been previously considered for registration, and have been deemed out of scope, it may be necessary for your entities to be reconsidered by your usual Cayman legal counsel as a result of the new amendment. The deadline for all private funds to be registered with the Cayman Islands Monetary Authority (CIMA) is 7 August 2020.

CIMA's previously published FAQ on the PF Law can be found [here](#).

CIMA PUBLISHES DISCLOSURE RULES FOR OFFERING DOCUMENTS AND MARKETING MATERIALS

CIMA has published new rules in relation to the marketing materials of registered private funds and the contents of offering documents for regulated mutual funds. Regulated Mutual Funds and Private Funds with new or ongoing offerings are required to comply with the new disclosure rules.

The rules can be accessed on CIMA's website [here](#).

- **RULE - Contents of Offering Document – Regulated Mutual Funds:** This rule applies to funds regulated under the Mutual Funds Law (Revised) and provides a list of fund information that should be included in a funds offering document. The list generally follows current market practice on the disclosure of fund information, however the rule includes new mandatory disclosure statements on the funds power to enter into side letters, a statement if the fund is registered/licensed outside the Cayman Islands and a standard statement concerning CIMA's liability.
- **RULE - Contents of Marketing Materials – Registered Private Funds:** This rule applies to private funds registered under the PF Law which intend on preparing marketing materials (other than

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AIVs). The rule does not put an obligation on private funds to prepare marketing materials, but where such materials are prepared or already existing, such materials must include the list of fund information disclosures, including new mandatory disclosure statements.

MONETARY AUTHORITY (ADMINISTRATIVE FINES) (AMENDMENT) REGULATIONS 2020

On 26 June 2020, the Monetary Authority (Administrative Fines) (Amendment) Regulations 2020 were passed, amending the Monetary Authority (Administrative Fines) Regulations 2019 (Administrative Fine Regulations). The amendment extends the application of the fines administered by CIMA from the anti-money laundering regime to all regulatory laws and regulations, and any rules issued by CIMA pursuant to those laws and regulations.

As a reminder CIMA has the power to impose administrative fines for breaches committed by individuals and entities, under various laws (and associated regulations and rules), including, but not limited to, the Anti-Money Laundering Regulations (2020 revision), the Directors Registration and Licensing law, 2014 (as revised), the Mutual Funds Law (2020 Revision) and the Private Funds law, 2020 (as revised).

The Administrative Fine Regulations set out both the criteria and procedure for administering such fines, which can range from (approx.) US\$6,098 up to (approx.) US\$1,219,512 depending on the seriousness of the breach and whether such breach was committed by an individual or an entity.

EXEMPTED LIMITED PARTNERSHIP (AMENDMENT) REGULATIONS, 2020

The Exempted Limited Partnership (Amendment) Regulations 2020 came into effect on 22 May 2020 as part of the Cayman Islands governments efforts to boost the regulatory framework for financial services in the Cayman Islands. Under the regulations, the fees payable by exempted limited partnerships (ELPs) registered with the Registrar of ELPs that are formed for the purpose of being regulated by CIMA are reduced.

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DEPARTMENT FOR INTERNATIONAL TAX COOPERATION (DITC)

- **FATCA and CRS Reporting Deadline Extension:** The FATCA and CRS reporting deadline for the 2019 reporting period has been extended to 16 November 2020.
- **Tax Information Authority (International Tax Compliance) (Common Reporting Standard) (Amendment) Regulations, 2020 and Tax Information Authority (International Tax Compliance) (United States of America) (Amendment) Regulations, 2020:** The annual reporting deadline for FATCA and CRS reporting has been changed from 31 May to 31 July and the requirement for the 'Authorising Person' and 'Principal Point of Contact' to be an individual has been removed, now allowing for institutional users to appoint an entity to these roles.
- **CRC Compliance Form (new):** DITC released its new CRC Compliance Form (which must be completed annually by all Reporting Financial Institutions). It should be noted that the 2020 deadline for submission of the new form is 31 December 2020. The DITC has also published Notes for Users on the DITC website which explain the purpose of the form and provide a high-level overview of the requirements. It should be further noted that the CRS Compliance Form is a critical component in the Cayman Islands assessment by the Global Forum's AEOI Peer Reviews, which are currently under way, to ensure data collection, analysis, and effective implementation of the CRS.
- **AEOI Portal/new DITC Portal:** The Cayman Islands Automatic Exchange of Information (AEOI) portal is currently offline, pending the development of a new portal, called the DITC Portal for registration (notification) and reporting purposes and which will eventually serve as the registration and reporting portal for all legislative frameworks (including economic substance and other reporting).

BENEFICIAL OWNERSHIP UPDATES

- **Reminder: Change in Definition of Beneficial Owner came into effect on 15 May:** The definition of beneficial owner under the Companies Law (2020 Revision) and the Limited Liability Companies Law (2020 Revision) has been widened from "more than 25% of the shares

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or voting rights in a company” to “twenty-five per cent or more” of the shares or voting rights in a company.

- **Updated Beneficial Ownership Filing System:** On 19 May 2020, the first phase of the updated on-line beneficial ownership filing system came into effect. Phase 1 entailed the release of the updated CSV file and guidance notes. Phase 2 consisted of in-house training and a pilot test. Industry training on the bulk upload of beneficial ownership (BO) information to the updated BO system is set to commence as phase 3 of the implementation of the on-line beneficial ownership filing system continues.

The Ministry of Financial Services has reassured the industry that the submission of BO information via the Corporate Administration Platform (CAP) onto the BO system, which is not internet-facing, is secure. The CAP is used only as the upload interface and not as a storage facility. The uploaded data is not viewable without strict authorization. All BO data is encrypted in transit and at rest, the data, upon storage, is then obfuscated.

The Ministry reminded industry that the use of the CAP and the shift away from manual filings is intended to increase efficiency and security while adding convenience for both corporate service providers and the competent authority for BO. In addition, the enhancements to the framework will allow the authority to quickly monitor and analyze gaps in the submission of BO details, thereby aiding the competent authority with its compliance efforts.

THE COMPANIES (AMENDMENT) (NO.2) LAW AND THE LIMITED LIABILITY COMPANIES (AMENDMENT) (NO.2) LAW – PROPOSED CHANGES TO CORRESPONDING REGULATIONS

The Companies (Amendment) (No.2) Law, 2020 and the **Limited Liability Companies (Amendment) (No.2) Law, 2020** (the Laws) which were passed in May and which introduced follow-on amendments following changes made earlier this year to the beneficial ownership regime were given assent by the Governor and came into effect on 29 June 2020.

In summary (as a re-cap), the amendments introduced more dissuasive penalties on entities to increase compliance with the beneficial ownership legislation. The amendments provide additional powers to corporate service providers where entities they are providing registered office services fail to provide

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them with the required information. These powers come in the form of a restriction notice that can be issued by the corporate services provider to the company where the company is not providing the information needed by the corporate services provider for its submission to the Registry. The amendments also create an administrative fines framework allowing the Registrar to issue financial penalties on those failing to comply with their legal obligations.

As a result of the foregoing amendments the Ministry of Finance published 2 bills for consultation in connection with the recent changes, namely, ***The Beneficial Ownership (Companies) (Amendment) Regulations, 2020***; and ***The Beneficial Ownership (Limited Liability Companies) (Amendment) Regulations, 2020***. The proposed amendments to the Regulations reflect two key changes to the aforementioned Laws – changes to the issuance of restrictions notices and the introduction of the administrative fines framework. The consultation period closed on 17 June 2020.

ECONOMIC SUBSTANCE

Update on Economic Substance Forms: Updated economic substance forms were released on 15 May 2020, namely the Form for Outsource Service Providers and Form for Entity Tax Resident in Another Jurisdiction. It should be noted that economic substance reporting functionality is expected to be added to the Department for International Tax Cooperation's (DITC) on-line portal later this year. The 2020 deadline for submission of Form for Entity Tax Resident in Another Jurisdiction is 31 December 2020. The DITC have also published notes for users for both forms on the DITC website [here](#).

VIRTUAL ASSET (SERVICE PROVIDER) REGULATORY FRAMEWORK

Further to the recent changes to the AML / CFT regime to include virtual asset services as "relevant financial business", the Cayman Islands has now passed the **Virtual Assets (Service Providers) Law, 2020** (VASP Law) which introduces a number of measures relating to the supervision and regulation of virtual asset services taking place within the Cayman Islands and originating from the Islands. Among other measures, the VASP Law introduces a registration requirement, a Virtual Asset Service Licence, and a Sandbox Licence for virtual asset service providers. The VASP Law will come into force upon the issuance of a commencement order.

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The regulatory framework is essentially based on anti-money laundering and counter terrorist financing (AML/CFT) recommendations adopted in 2019 by the Financial Action Task Force (FATF). As a member of the Caribbean Financial Action Task Force (CFATF), a body comprising Member States in the Caribbean with associate FATF status, Cayman is fully implementing the FATF's standards for virtual asset services.

The VASP Law applies to any person providing virtual asset services as a business or in the course of business for Cayman-based customers or for overseas clients and will need to be officially recognised as a virtual asset service provider. This means that persons are required to apply for a virtual asset licence, or seek registration, or obtain a waiver before they can provide any virtual asset services.

The VASP Law includes the following elements:

- A **virtual asset** means a digital representation of value that can be electronically traded or transferred and can be used for payment or investment purposes. However, a virtual asset does not include digital fiat currencies, such as the electronic representation of US dollars or any other currency. Examples of virtual assets include Bitcoin, Ethereum and others that are commonly called "crypto assets", "digital assets" or "cryptocurrencies".
- A **virtual asset service** means the business of providing one or more of the five activities outlined in the VASP Law for or on behalf of a third party. The activities include the exchange, transfer, issuance, and safekeeping of virtual assets.
- A **virtual asset service provider** is a person who is registered, licensed or the holder of a waiver under the VASP Law in order to provide virtual asset services as a business or in the course of business, to clients within or outside of the jurisdiction.
- Virtual assets themselves will not be regulated; virtual assets are in and of themselves only a potential means to transfer or store value. Rather, the new framework regulates the persons engaged in relevant financial business which use virtual assets.
- Requirements will only apply to persons who exert a certain level of custody or control of the virtual assets, or the ability to actively facilitate the financial activity on behalf of a third party. A person engaged in virtual assets strictly for his or her own purposes (not a business) is not in scope of the new framework.

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