



January 5, 2017

VIA EMAIL

Wilbur Welcome
Ministry of Financial Services
Government Administration Building
133 Elgin Avenue, Box 126
Grand Cayman KY1-9000

Re: Response to the Public Consultation on Legislative Amendments to Enable the Creation of a Centralised Platform of Beneficial Ownership Information

Dear Mr. Welcome:

Managed Funds Association (“MFA”)¹ represents the global alternative investment industry and its investors by advocating for sound industry practices and public policies that foster efficient, transparent, and fair capital markets. MFA takes a keen interest in all policy issues that may affect hedge fund and managed futures firms in the alternative investment industry. Accordingly, in light of the considerable stake that our members have in the Cayman Islands investment funds industry, we welcome this opportunity to submit comments to the Ministry of Financial Services on the proposed legislative amendments to enable the creation of a centralised platform of beneficial ownership information.²

We fully recognize the international context, including the Exchange of Notes with the UK, in which these legislative amendments are being proposed. Our approach is therefore primarily intended to suggest specific areas where the proposals could be rendered more workable. As a general comment, we believe that it is in the interests of all stakeholders for the legislation to allow

¹ The Managed Funds Association (MFA) represents the global alternative investment industry and its investors by advocating for sound industry practices and public policies that foster efficient, transparent, and fair capital markets. MFA, based in Washington, DC, is an advocacy, education, and communications organization established to enable hedge fund and managed futures firms in the alternative investment industry to participate in public policy discourse, share best practices and learn from peers, and communicate the industry’s contributions to the global economy. MFA members help pension plans, university endowments, charitable organizations, qualified individuals and other institutional investors to diversify their investments, manage risk, and generate attractive returns. MFA has cultivated a global membership and actively engages with regulators and policy makers in Asia, Europe, North and South America, and many other regions where MFA members are market participants.

² MFA previously submitted comments in response to the open public consultation on the beneficial ownership of Cayman Islands registered companies, available at: <https://www.managedfunds.org/wp-content/uploads/2014/01/MFA-Comments-on-Cayman-Islands-Consultation-on-Beneficial-Ownership.pdf>.

maximum flexibility in drafting the Regulations. References to sections are references to sections of the draft Companies (Amendment) Bill,³ 2017 unless otherwise stated.

Reasonable Steps

Sections 247 and 248 respectively require a company to take “reasonable steps” to identify any individual who is a beneficial owner of the company and all relevant legal entities that exist in relation to the company. We note that guidance for UK companies on what will constitute “reasonable steps” in the context of the corresponding UK legislation⁴ is provided in section 2.3 of the UK Department for Business Innovation and Skills Guidance on the Register of People with Significant Control. We would welcome confirmation from the Government that it will provide similar guidance for Cayman Islands companies in due course.

Deadlines

Section 249 requires a company to give notice⁵ to beneficial owners, relevant legal entities, registered shareholders and certain other persons, requiring them to provide information within one month of the date of receipt of the notice.⁶ Section 250 also requires beneficial owners and relevant legal entities to proactively supply information in certain circumstances in the absence of a notice under section 249, where such circumstances have continued for a period of at least one month.⁷ In each case, we would recommend extending the deadline to 60 days or, preferably, 90 days in order to take into account the fact that recipients may often not only be located overseas but may also be frequent travelers. Indeed, if the law contemplates that the postal service is permissible as a means of providing notice, the one-month period could be difficult to comply with in practice in any case.

Scope of Corporate Services Providers’ Duties

³ Supplement No. 8 published with Extraordinary Gazette No. 100 dated 16th December, 2016. A Bill for a Law to amend the Companies Law (2016 Revision) in order to require companies incorporated in the Islands to establish and maintain beneficial ownership registers which may be searched by the competent authority; and for incidental and connected matters.

⁴ Namely the UK Small Business, Enterprise and Employment Act 2015.

⁵ The notice shall require persons to whom it is addressed to state whether or not they are registrable persons and, if so, to conform or correct any particulars in the notice and supply any required information missing from the notice.

⁶ Pursuant to section 255 the company is required to provide the information to a corporate services provider or Registrar, as the case may be in order that the corporate services provider or Registrar, as the case may be, may enter the information in the company's beneficial ownership register.

⁷ The circumstances, which are set out in section 250, are as follows:

- (a) the person is a beneficial owner of a company to which this Part applies or is a relevant legal entity in relation to such a company;
- (b) the person knows the facts referred to in paragraph (a);
- (c) the person has no reason to believe that the person’s required particulars are stated in the company’s beneficial ownership register;
- (d) the person has not received a notice from the company under section 249; and
- (e) the circumstances described in paragraphs (a), (b), (c) and (d) have continued for a period of at least one month.

We agree that the duty to identify beneficial owners and relevant legal entities pursuant to section 247 and 248 is that of the company, not of its corporate services provider. We also agree that pursuant to section 255, it is the duty of the company to provide required particulars of its registrable persons to its corporate service provider, once the company has confirmed those particulars. However, pursuant to section 258, if a company's corporate service provider is of the opinion that a company has made a statement which is false, deceptive or misleading in respect of a material particular, the corporate services provider is required to give notice of its opinion to the company.

We would welcome clarification from the Government to the effect that under section 258, a corporate services provider is not required to verify or question the information provided to it by a company, unless the corporate services provider considers that it has reason to do so. We suggest inserting the following or similar wording at the end of section 258: "*Notwithstanding the above, a company's corporate services provider is not required to verify or question the information provided to it by the company unless the corporate services provider considers that it has reason to do so.*"

Security Concerns

We note that the Cayman Islands Government is extremely aware of the risk of cyberattacks and the potential for illegal disclosure of confidential information, and that the design and technical specifications of the centralised platform and the beneficial ownership registers will be designed to mitigate these risks.

However, a number of companies will have beneficial owners with objectively valid and serious security concerns of their beneficial ownership information. We note that under section 256, the required particulars of an individual include his or her residential address. We would recommend that a business address may be provided as an alternative to a residential address to help allay concerns about security.

We also note that pursuant to section 280 the competent authority may exempt an individual or legal entity from complying with specified requirements, and that the competent authority shall exercise such exemption powers in accordance with criteria to be specified in regulations. We would welcome an indication that the Ministry will include security considerations, among the criteria that it considers on a case by case basis.

Criminal Liability

We note that the proposed legislation introduces a number of offences for which a person will be liable on conviction to a fine or, in some cases, by imprisonment.⁸ We agree that unlawful search or disclosure of beneficial ownership information should be criminalized as set out in section 278. However, we believe that other offences should be administrative, rather than criminal, in nature. We would also suggest that all references to fines be amended to read "*up to a maximum of \$...*" rather than "*a fine of \$...*" to retain flexibility.

⁸ Sections 269 (breach of restrictions), 270 (company issuing shares in breach of restriction), 275 (failure of company to establish or maintain beneficial ownership register), 276 (failure to comply with notices), 277 (failure to provide information), 278 (unlawful search or disclosure of beneficial ownership information) and 279 (offences by officers and directors of legal entities).

Reporting Threshold

We note that while currently the Cayman Islands requires that corporate services providers verify information at a level of 10%, under the Exchange of Notes with the UK, the requirement is to exchange beneficial ownership information only on persons with a level of ownership or control that is greater than 25%. The difference in the reporting threshold (10% v 25%) would therefore require a corporate services provider to comply with two sets of requirements.

Although we see merit in requiring a reporting threshold of 10% rather than 25%, primarily because the 10% threshold is consistent with corporate services providers' existing responsibilities, we support the existing proposed legislative amendments for beneficial ownership information requiring a reporting threshold of 25%. We note that a 10% reporting threshold would go further than other jurisdictions and potentially prejudice the Cayman Islands as a jurisdiction.

Length of Time for Maintaining Beneficial Ownership Information for Persons that Are No Longer Registerable

We support the proposed amendment which reflects that a company may remove a person from a beneficial ownership register on the expiration of 5 years from the date on which he/she ceased to be registerable. We would not support the suggestion that this period be increased to 20 years. First, this change would represent a significant increase in compliance cost for companies. Compliance is representing increasingly significant costs for companies and, in some cases, may be a barrier to entry. Second, there would be little or no benefit given that the average life span of a Cayman Islands entity is well under 20 years. Third, the retention of information necessarily creates a data security risk, in that the longer information is retained, the greater the risk. As such, we see a significant downside and little or no upside in increasing the period beyond 5 years.

Technical Clarifications

We note that the proposed draft legislation is based on the UK's Small Business, Enterprise and Employment Act 2015, albeit amended for the Cayman Islands. However, we would suggest certain technical changes as follows to ensure that companies are able to clearly understand and comply with the requirements.

1. We agree with the exceptions to the application of Part XVIIIA (Beneficial Ownership Registers) pursuant to section 245(1), but would suggest deleting certain wording in section 245(1)(c) as superfluous and not conforming to any defined terms found elsewhere as follows:

(c) managed, arranged, administered or promoted by a person regulated in, or listed on a stock exchange in the Islands or a jurisdiction listed in Schedule 3 of the Money Laundering Regulations (2015 Revision) that is—

(i) a special purpose company;

(ii) a private equity or collective investment scheme; or

(iii) an investment fund (or if such fund is an exempted limited partnership, its general partner);

2. The definition of 'relevant interest' and subsections 247(1), 252(10) and 253(3) refer to 'shares or voting rights' in the company, whereas subsection 245(2) refers to 'shares or the voting shares' in the company. We would suggest that all references are conformed to the former description as, in many instances, shareholder votes in a Cayman Islands company are not

determined solely on the basis of number of shares held, but may be weighted on the basis of net asset value per share or an equivalent concept.

3. We note that pursuant to subsection 247(2) an individual must meet one or more conditions in order to be a “beneficial owner”. As currently drafted, condition (d) is that “*X has the absolute and unconditional right to exercise, or actually exercises, significant influence or control over company Y through the ownership structure described in (a), (b) or (c) through the ownership structure described in (a), (b) or (c)*”. We believe that any “significant influence or control” type condition along the lines of condition (d) should be applied only if conditions (a), (b) and (c) have not identified an individual beneficial owner.

Our view is consistent with the approach taken in the UK, as set out in the Department for Business Innovation and Skills Guidance on the Register of People with Significant Control at section 2.3 (Table 1: Summary of PSC conditions), which states that a company will only need to refer to condition (iv) if they do not meet one or more of conditions (i) to (iii). It is also consistent with the approach taken by the Financial Action Task Force (FATF) in relation to the identification of beneficial owners of legal entities in the FATF Recommendations for International Standards on Combating Money Laundering and the Financing or Terrorism & Proliferation at Interpretive Note to Recommendation 10 (Customer Due Diligence), which makes it clear that measures it recommends are not alternative options, but are cascading measures, with each to be used where the previous measure has been applied and has not identified a beneficial owner.

The intent of the addition of the words “*through the ownership structure described in (a), (b) or (c)*”, which did not appear in the previous draft, is not entirely clear. As currently worded, it appears that condition (d) can only be met if one or more of conditions (a), (b) or (c) is met, so we assume condition (d) may be intended to apply to a situation where an individual “X(d)” somehow has significant influence or control over company Y through an individual meeting condition (a), (b) or (c), but it is difficult to understand how this is intended to apply in practice.

4. We note that the term “firm” is used within the proposed draft legislation within the definition of a “legal entity” as referring to a legal person. However, it is also used within the definition of a “beneficial owner” pursuant to section 247(2) as referring to an entity which does not have legal personality. We would suggest deleting and replacing the term “firm” as suggested below in order to avoid confusion.

“legal entity” means a body corporate, firm or other body that is a legal person under the law by which it is governed;

247(2) At least one of the following conditions must be met by an individual (“X”) in relation to ~~is a beneficial owner of a company (“company Y”)~~ if in order for the individual to be a “beneficial owner” meets one or more of the following conditions in relation to the of company Y-

- (a) X ~~must~~ holds, directly or indirectly, more than 25% of the shares in company Y;*
- (b) X ~~must~~ holds, directly or indirectly, more than 25% of the voting rights in company Y;*
- (c) X ~~must~~ holds the right, directly or indirectly, to appoint or remove a majority of the board of directors of company Y;*
- (d) X has the absolute and unconditional right to exercise, or actually exercises, significant influence or control over company Y through the ownership structure described in (a), (b) or (c);*

(e) (i) *X has the absolute and unconditional right to exercise, or actually exercises, significant influence or control over the activities of a trust, partnership or firm ~~other entity~~ described in subparagraph (ii), other than in a professional advisory capacity, and*
(ii) *the trustees of the trust or the members of the ~~firm~~ partnership or other entity that, under the law by which it is governed is not a legal person, meet any of conditions (a), (b), (c) or (d) (in their capacity as such) in relation to company Y, or would do so if they were individuals*

5. We note that under subsection 248(2) of the draft legislation a “relevant legal entity” is defined as follows:

A “relevant legal entity” in relation to a company is a legal entity –

- (a) that would be a beneficial owner of the company if it were an individual; or*
- (b) meets a prescribed description.*

Our understanding, taking into account the corresponding definition in section 790C(6) of the UK Small Business, Enterprise and Employment Act 2015 and paragraph 2.2 in the UK's Guidance on the Register of People with Significant Control, is that for Cayman Islands purposes an entity is a “relevant legal entity” in relation to a company if that legal entity is required to keep its own beneficial ownership register, and that it will be a “registrable person” if it is the first registrable legal entity in the company's ownership chain.

It would be helpful to have this understanding confirmed or corrected, as the case may be, as a number of provisions in the draft legislation hinge on the meaning of “relevant legal entity”. If our understanding is correct, limbs (a) and (b) of section 248(2) would need to be cumulative, rather than alternative, for example as follows:

248. (2) A “relevant legal entity” in relation to a company is a legal entity –

- (a) that would be a beneficial owner of the company if it were an individual; and ~~or~~*
- (b) is subject to its own disclosure requirements under this Law that meets a prescribed description.*

6. We would suggest deleting certain wording in section 249(1) as superfluous and not conforming to any defined terms found elsewhere as follows:

249. (1) ~~Subject to subsection (5), a company to which this Part applies shall give notice to beneficial owners and relevant legal entities identified under sections 247 and 248 and to any person that it knows or has reasonable cause to believe is a registrable person in relation to it.~~

7. Section 255 (Role of corporate services provider and Registrar) requires a company to “provide in writing to a corporate services provider or to the Registrar, as the case may be, the required particulars of registrable persons in respect of that company, once those particulars have been confirmed” and provides that the “company shall instruct the corporate services provider or the Registrar, as the case may be, to enter the required particulars of registrable persons in the company's beneficial ownership register in the prescribed form and manner, or if no registrable persons are identified to enter a nil return”.

Section 257 (Duty of company to keep register up to date) requires a company which has become aware of a relevant change with respect to a registrable person to “record the details of the change and instruct the corporate services provider or the Registrar, as the case may be, to enter in the company's beneficial ownership register in the prescribed form and manner”.

We interpret these sections and understand the intention of the legislation to be that the corporate service provider, not the company, should be able to access and maintain the beneficial ownership register.

8. We note that section 262 (Duty of competent authority to establish search platform) requires the competent authority to “*establish a search platform by means of which access may be provided to all beneficial ownership registers maintained on behalf of companies subject to this Part by corporate services providers or the Registrar*”.

However, section 263 (Duties of Registrar and corporate services providers) provides as follows:

263. A company services provider engaged by a company pursuant to section 254, or the Registrar if so engaged, shall provide the company with an information technology solution, either directly or through another corporate services provider, that -
(a) enables the company to establish and maintain its beneficial ownership register; and
(b) connects that register with the search platform.

As currently worded, section 263 seems to suggest that a corporate service provider shall provide a company with an information technology solution that enables the company to maintain its beneficial ownership register itself, rather than instructing the corporate services provider to do so on the company's behalf. We do not believe this to have been the intention and do not, in any case, believe this would be desirable or workable in practice. We would therefore suggest amending the wording along the following lines:

263. A company services provider engaged by a company pursuant to section 254, or the Registrar if so engaged, shall provide ~~the company with~~ an information technology solution, either directly or through another corporate services provider, that -
(a) enables the corporate services provider or Registrar, as the case may be ~~company~~ to establish and maintain the company's ~~its~~ beneficial ownership register on its behalf; and
(b) connects that register with the search platform.

Conclusion

MFA appreciates the opportunity to provide comments on the proposals and we would welcome the opportunity to discuss further the relevant issues. If you have any questions, please do not hesitate to contact Matthew Newell, Associate General Counsel, or the undersigned at (202) 730-2600.

Respectfully submitted,

/s/ Stuart J. Kaswell

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