HARNEYS

Duties and obligations of a director of a Cayman Islands fund

This guide provides an overview of the powers, duties and obligations of a director of an exempted company incorporated under the Companies Act of the Cayman Islands (***Companies Act***) which is registered with the Cayman Islands Monetary Authority (***CIMA***) as a fund (***Fund***).

Overview

This guide is limited to those Funds registered with CIMA under section 4(3) or 4(4)(a) of the Mutual Funds Act (a ***Regulated Fund***) and those Funds registered with CIMA under the Private Funds Act (a ***Private Fund***) as well as the law and practice of the Cayman Islands. Other duties, obligations and potential liabilities may also arise under the laws of other jurisdictions.

Who are the directors of a Fund?

There is no precise definition of a 'director' under Cayman Islands law. The directors of a Fund may be individuals or corporate bodies and they are the persons with ultimate responsibility for the management and conduct of the Fund's affairs.

The first directors of a Fund (whether described as 'executive' or 'non-executive') are typically appointed by the initial subscribers to the Fund or otherwise in accordance with the articles of association of the Fund (***Articles***). The register of directors maintained by the Fund will be prima facie evidence of the identity of the directors from time to time.

A person undertaking the activities of a director without being formally appointed may be found to be acting as a 'de facto director'. Also, if the duly appointed directors of a Fund are found to be acting in accordance with the directions or instructions of another person then that person may be found to be acting as a 'shadow director'. A person is not deemed to be a shadow director however by reason only that the directors act on advice given by him in a professional capacity, so that an investment manager of a Fund making recommendations as to the purchase or sale of investments should not usually constitute a shadow director.

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Executive directors, non-executive directors, shadow directors and de facto directors are all subject to the duties and obligations set out in this guide.

Should I agree to act as a director of a Fund?

When deciding whether or not to act as a director of a Fund, the following points should be considered:

- who will be the other directors of the Fund? Will your fellow directors have the ability to work with you to properly co-ordinate the proper oversight and management of the Fund?

- any other interests you may have in the overall structure of the Fund and its advisers or service providers. If you are a connected person (for example, a principal of the Fund's investment manager) you may want to consider either not sitting on the board of the Fund or making sure that you are in a minority position. These measures will reduce the potential for conflicts of interest to arise which could increase the risk of your actions later being challenged by the investors of the Fund as not being in accordance with your duties to the Fund

- the expectations of the Fund's key investors. They may be comfortable with a board of directors comprised of connected persons or may require the Fund to have one or more directors independent of the Fund's investment manager. This is something that you may wish to discuss further with the Fund and the Fund's current or proposed key investors before agreeing to accept any appointment as a director

- you need to have sufficient and relevant knowledge and experience to discharge your duties as a director. It is up to you to acquire and maintain sufficient knowledge to enable you to carry out your role. You should use the Fund's professional advisers to provide advice on any areas or transactions of which you are unsure. In particular, you should ensure that you are able to properly read and understand the financial information relating to the Fund, including its financial statements. If there is anything that you do not understand, then you should promptly obtain professional advice

- whether the Fund has in place, or will be obtaining, any directors and officers insurance policy that would provide appropriate coverage to you

- you need to have sufficient time to carry out your duties and this should be reflected in your remuneration

- even if you are also an employee or principal of the investment manager or any other connected party, your duties as a director of the Fund remain the same as an independent director. You should ensure that you are wearing the right 'hat' when turning your mind to the affairs of the Fund and be aware of actual and potential conflicts of interest. Any actual and potential conflicts of interest should then be disclosed in any prospectus, offering document or private placement memorandum issued by the Fund (***Offering Document***).

Please note that it is not mandatory under either the Mutual Funds Act or the Private Funds Act for a section 4(4)(a) Fund or a Private Fund to issue an Offering Document, and references in this guide to an Offering Document are only applicable to a section 4(4)(a) Fund or a Private Fund if it has issued a prospectus, offering document or private placement memorandum.

What are the powers and authority of the directors of a Fund?

The powers and authority of a director are derived from, and constrained by, the Fund's memorandum of association (***Memorandum***) and the Articles. The Memorandum sets out the capacity and powers of the Fund and the Articles set out the manner in which the Fund is to be operated.

The directors will need to ensure that the Fund is operated in accordance with the terms of any Offering Document issued by the Fund to its investors from time to time. Whilst the terms of the Offering Document do not fetter the powers of the directors of the Fund, the Offering Document forms a collateral contract between the Fund and its shareholders and so the directors should ensure that they regularly review, and are familiar with, the contents of the Offering Document.

In practice, the Articles will almost certainly allow the directors to delegate their powers to service providers. The directors of a Regulated Fund must appoint an auditor and will typically appoint an investment manager, an administrator and a custodian/prime broker, amongst other service providers. The directors of a Private Fund must appoint an auditor and a custodian (unless exempt) and may also appoint an independent third party or administrator to perform certain functions set out in the Private Funds Act.

In deciding to appoint a service provider the directors will need to be diligent and careful in their selection, forming the reasonable opinion that the service provider is competent to carry out the relevant function(s) on behalf of the Fund.

Once service providers have been appointed, the directors are entitled to trust (to a reasonable extent) the competence and integrity of the service provider in discharging its functions. The directors remain subject, however, to a continuing duty to supervise and monitor the activities of the service provider on a high-level basis. If a director is found to be in breach of this duty, they may be found guilty of wilful neglect or default, thereby potentially voiding the indemnity provisions in the Articles and also the terms of any directors and officers insurance policy that the director may have in place – meaning that the director could potentially become personally liable for the breach.

What are a Fund director's duties?

The duties of a director of a Fund arise as a consequence of the fiduciary relationship between the director and the Fund and are based on a combination of English and Commonwealth common law, as applied in the courts of the Cayman Islands, statute and regulatory guidance. There is, however, no statutory codification in the Cayman Islands of the general directors' duties, obligations and liabilities (although, see below on regulatory guidance under the section CIMA Statement of Guidance for Regulated Mutual Funds with respect to Regulated Funds).

Directors' duties will ordinarily be owed to the Fund but can, in particular circumstances, be owed to creditors or individual shareholders.

In the ordinary course of business, the interests of the Fund mean acting in the best interests of the Fund's shareholders as a whole. However, if the Fund becomes insolvent or 'doubtfully' solvent directors must take account of the Fund's creditors when discharging their duties.

Directors are also obliged to comply with various statutory obligations regarding the management and operation of the Fund. The principal obligations applicable to the Fund and to the directors arise under the Companies Act, the Mutual Funds Act (for Regulated Funds), the Private Funds Act (for Private Funds) and the Proceeds of Crime Act.

Directors' key duties can be summarised as follows:

Fiduciary duties

- to act bona fide in what the director considers to be the best interests of the Fund
- to exercise their powers under the Articles for the purposes for which they are conferred
- to avoid conflict between the interests of the Fund and the director's personal interests and duties or (where such conflicts are permitted by the Articles, as is common) making sure that any such conflicts are properly disclosed
- to exercise the director's powers as a director independently, without subordinating their powers to the will of others (except to the extent that such powers have been properly delegated)
- not to make secret profits from acting as a director of the Fund

Duties of skill and care

- to acquire and maintain a sufficient knowledge of the business of the Fund on a continuing basis; and
- to supervise the discharge of functions which have been delegated to advisers and service providers (see What are the powers and authority of the directors of a Fund? above).

Directors are obliged to undertake these duties with care, diligence and skill. Directors are subject to a minimum objective standard as a director of the Fund, but the expected standard will be raised if a particular director has more knowledge, skill or experience than would ordinarily be expected of a director in their position. Directors will also have the relevant contractual duties and obligations set out under any service agreements that they may enter into with the Fund.

Statutory obligations

Directors of a Fund are obliged under Cayman Islands legislation:

- to maintain the Fund's register of members, the register of directors and officers and the register of mortgages and charges
- Funds are likely to be exempt from having to maintain a register of beneficial ownership but when an exemption applies, the Fund must file written confirmation of the exemption with its registered office provider, with instructions to file the written confirmation with the competent authority in the Cayman Islands. Please see our Guide to the Cayman Islands beneficial ownership regime for more details on beneficial ownership registers and exemptions that can apply
- to maintain proper books of account for the Fund
- to maintain a registered office in the Cayman Islands for the Fund
- to comply with the Anti-Money Laundering Regulations (***AML Regulations***) issued under the Proceeds of Crime Act
- to ensure that the Offering Document issued by the Fund describes the shares in all material respects, and contains such other information as is necessary to enable a prospective investor in the Fund to make an informed decision whether or not to invest;

- to update the Offering Document to take account of any material changes
- file any material changes to the information previously filed with CIMA, including an amended Offering Document, within 21 days of the change
- to ensure that the Fund is audited on an annual basis
- to comply with reporting obligations including, without limitation, notifying the Registrar of Companies (***Registrar***) of any changes in the directors, officers or registered office of the Fund, arranging for the filing of the Fund's annual return and exempted company declaration with the Registrar and filing the Offering Document and annual audited financial statements with CIMA
- to comply with the requirements of the Director Registration and Licensing Act (see Directors registration and licensing below)

Offering document obligations

CIMA has issued a Rule for the Content of Offering Documents for Regulated Funds and a Rule for the Content of Marketing Materials for private funds, which set out the specific content to be included in Offering Documents for each type of fund.

Where one is prepared or is required, as well as the requirements set out in the applicable Rule, CIMA expects a market standard Offering Document which properly and adequately describes the main features of the Fund (including investment structure and strategy, role and functions of service providers, disclosure of interests, risk factors, fee information) and provides all of the information that would reasonably be considered material to investors to make an informed investment decision.

Automatic Exchange of Information and AML obligations

A Fund also has reporting obligations under Cayman Islands legislation which implements the US Foreign Account Tax Compliance Act (***FATCA***) and the OECD's Common Reporting Standard (***CRS***, and together with FATCA, ***AEOI Legislation***).

Full details of the ongoing reporting obligations of a Fund can be found in our Guide to Continuing Obligations of Mutual Funds.

In practice, the maintenance of statutory registers, the establishment of policies and procedures in accordance with the AML Regulations, reporting under AEOI Legislation and compliance with statutory filing obligations will be delegated by the directors to the registered office provider and/or administrator or another service provider of the Fund. However, whilst the directors may be entitled to delegate these functions, the directors are still obliged to supervise the appointed service providers' discharge of them.

Segregated portfolio company funds

If the Fund is a segregated portfolio company (***SPC***), the directors will also have additional duties under the Companies Act. These include:

- the duty to establish and maintain the segregation of the assets and liabilities attributable to each segregated portfolio from the assets and liabilities attributable to each other segregated portfolio and the general assets and liabilities of the Fund
- the duty to ensure that the Fund states the capacity in which it is contracting (ie which portfolio it is acting for) when entering into contractual documentation

In particular, proper oversight by a director of the proper maintenance of the segregation of assets and liabilities between the segregated portfolios in an SPC is important to demonstrate the proper discharge of the director's duties in respect of that SPC under the Companies Act. Such oversight should minimise the prospect of any potential cross-contamination of liabilities within the segregated portfolios of the SPC. Please see our Guide to Cayman Segregated Portfolio Companies for further details.

CIMA statement of guidance for Regulated Funds

Following the 2011 first instance decision of the Grand Court of the Cayman Islands in *Weavering Macro Fixed Income Fund (In Liquidation) v Peterson and Ekstrom (2011)* (***Weavering***), CIMA published a Statement of Guidance (***SoG***) in 2014 which applies to Regulated Funds. The SoG sets out best practices and establishes certain minimum corporate governance standards for governing bodies of Funds and whilst only applicable to Regulated Funds at this stage, it provides helpful guidance for all Funds.

The SoG does not impose a strict or all-encompassing code of conduct on governing bodies or operators of Regulated Funds but expects the oversight, direction and management of a Regulated Fund to be conducted in a fit and proper manner. At a concise eight pages, the SoG establishes an overall framework for good corporate governance within which Regulated Funds should operate. The SoG does not contain specific restrictions on investments, risks or strategies, nor does it attempt to direct, prescribe or constrain the management or business activities of Regulated Funds.

The SoG includes the following:

Structure

Directors should make sure that the governance structure of the fund is appropriate and suitable for effective oversight of the fund, looking at the fund's size, nature and complexity, including the level of assets under management, number of investors and nature of its investment strategy. Directors should make sure that the fund's constitutional documents and Offering Document comply with Cayman Islands law.

Oversight and compliance function

The directors of a fund are ultimately responsible for overseeing and supervising the activities of the fund. They should regularly monitor and take steps to ensure that the fund and its service providers are conducting the affairs of the fund in compliance with the fund's defined investment criteria, investment strategy and restrictions as well as with all applicable laws, regulations and other rules. Directors should receive regular reporting from the investment manager, administrator and other service providers to ensure they are able to make informed decisions and to adequately oversee and supervise the fund.

The directors should regularly ask for confirmation from the service providers that they are acting in accordance with the fund's constitutional documents and Offering Document, including regularly monitoring whether the investment manager is acting in accordance with the fund's investment criteria, strategy and restrictions. What constitutes 'regular' in this context will very much come down to the nature of the particular fund structure, strategy and service provider relationships and therefore must be looked at on a case by case basis. As part of this function, directors should also be mindful of CIMA's Outsourcing SoG as described below.

The directors should act in a transparent and honest manner with CIMA, always disclosing any matter which would materially and adversely affect the fund's financial soundness and any non-compliance with applicable laws. If in doubt, professional legal advice should be obtained prior to making any disclosure to CIMA.

This is particularly important for Private Funds that have engaged service providers to undertake the core requirements of valuation, custody and cash monitoring set out in the Private Funds Act.

Conflicts of interest and risk

Directors of funds must ensure that the fund's Offering Document adequately and accurately discloses conflicts of interest and ensure that the fund has adequate measures in place to identify, disclose, monitor and manage any conflicts of interest. Directors should ensure that they provide suitable risk management oversight and that risks are appropriately managed and mitigated.

This is particularly important for Private Funds where valuation, title verification or cash monitoring is being performed by a related party.

Meetings

The board of directors of a fund should meet at least twice a year, in person or by telephone or video conference call, and more often depending upon the circumstances or size, nature and complexity of the fund. Service providers should also

attend and provide reports to board meetings. Full, accurate and clear written records must be kept of such meetings and all resolutions passed at such meetings, including agenda items, circulated documents, a list of attendees and if they were present physically or by telephone or video conference, all matters considered and decisions made and information requested from and provided by service providers and advisors.

Duties

Directors of funds**:**

- are responsible for the appointment, removal, monitoring and supervision as well as the contractual terms of service providers including notifying investors and CIMA of any changes to the fund's service providers and making appropriate updates to the fund's Offering Document
- should communicate adequate information to the fund's investors, including where enhanced disclosure to investors is appropriate, making relevant enquiries when issues are raised and be satisfied that appropriate action is being taken
- must have sufficient capacity to apply their minds to overseeing and supervising each fund in accordance with relevant laws, regulations, rules, statements of principles and the provisions of the SoG and other relevant SoGs issued by CIMA. No specific limits are set on the number of directorships that can be accepted by an individual or corporate director, although under the Directors Registration and Licensing Act if the number of directorships exceeds 20 or more Covered Entities (as defined below), then the professional director licensing requirement will apply, see Directors registration and licensing below
- should ensure that the Offering Document contains such information as is necessary to enable a prospective investor to make an informed investment decision, including clear descriptions of the investment strategy and conflicts of interest policy
- should exercise independent judgment, act in the best interests of the fund, take into account the interests of investors as a whole, and should operate with due skill, care and diligence and act honestly and in good faith at all times, making sure they have sufficient and relevant knowledge and experience to carry out their duties
- must exercise the care, skill and diligence of a reasonably diligent person with such general knowledge, skill and experience
- should at all times be fully aware of the fund's investment activities, performance and financial position and review and approve the fund's financial statements
- should also regularly monitor the fund's net asset valuation policy and that the fund's net asset value is being calculated in accordance with the policy at the relevant intervals.

Outsourcing arrangements

In terms of outsourcing arrangements to service providers, directors should also be mindful of CIMA's policy in its Statement of Guidance on Outsourcing issued in 2015 (the Outsourcing SoG) that provides guidance to regulated entities on the establishment of outsourcing arrangements (including sub-outsourcing) and the outsourcing of material functions or activities. The Outsourcing SoG is not intended to be prescriptive or exhaustive, rather it sets out CIMA's minimum expectations on the outsourcing of material functions or activities and outsourcing arrangements.

The Outsourcing SoG provides guidance to regulated entities (including sub-contractors where applicable) on the following matters:

- appropriate due diligence of service providers
- contents of outsourcing agreements
- materiality assessments of outsourcing arrangements (ie impact of outsourcing arrangements on the entity and its finances, reputation and operations)
- confidentiality and disclosure of information

- what boards of directors of regulated entities are expected to do with respect to the outsourcing of material functions or activities
- termination and exit strategies
- expectations with respect to a regulated entity's relations with CIMA regarding the outsourcing of material functions or activities.

The Guidance Notes on the Prevention and Detection of Money Laundering and Terrorist Financing issued by CIMA also detail how funds may outsource / delegate AML compliance, provided the Fund has designated natural persons as their AML compliance officer, money laundering reporting officer and deputy money laundering reporting officer.

Directors registration and licensing

The Directors Registration and Licensing Act (***DRL Act***) imposes obligations on directors of Regulated Funds and certain securities investment businesses (***Covered Entities***) to register with CIMA prior to being appointed as a director of a Covered Entity.

Directors of Private Funds are not subject to the DRL ACT.

The definition of "director" also includes managers of Covered Entities which are formed as limited liability companies in the Cayman Islands under the Limited Liability Companies Act. The registration fee is currently US$854 per director which is a natural person who acts as a director for less than 20 Covered Entities. Licences are required for 'Professional Directors', being natural persons appointed to the boards of 20 or more Covered Entities and for corporate directors of Covered Entities. Licence fees for Professional and corporate directors are currently US$3,658 and US$9,756, respectively. Annual fees of the same amount are also payable to CIMA by 15 January each calendar year to maintain registration / licensing.

Please see our Guide to the Cayman Islands Directors Registration and Licensing Act for further details.

What practical considerations should be taken into account during the life of a Fund?

The Grand Court of the Cayman Islands provided a detailed analysis of the scope of an independent director's duties toward an offshore fund in its first instance decision in Weavering. Although that decision with respect to liability was over-turned by the Cayman Islands Court of Appeal in 2015, the first instance judge's division of the life of a fund into three distinct phases provides helpful commentary when considering the performance of the directors: (1) establishment, (2) ordinary course of business and (3) crisis management. Much of the commentary from the first instance decision in the Weavering case was subsequently reflected in the SoG by CIMA.

Establishment

Before the launch of a Fund the directors will need to make sure that they review and approve the Fund's documents, in particular the Offering Document. This will include being satisfied that the overall structure of the Fund and service providers is reasonable and consistent with industry standards, confirming the investment strategy and restrictions, confirming the valuation, custody and cash monitoring functions of a Private Fund are being satisfactorily handled, making sure that statements can be verified, risk factors are appropriate and conflicts of interest are fully disclosed, in particular where the valuation, custody and cash monitoring functions of a Private Fund are being performed by a related party.

As a practical matter, if a director's role is limited to that of an independent director then the director will not be expected to be involved in detailed negotiations with service providers. However, when taking on a role as independent director it is sensible to ask that before any agreements are signed, the investment manager or whoever is negotiating them lets the counterparties know that the directors will want to review them and approve them and that they may have comments or questions following their review.

Launch board minutes or resolutions of the Fund should also include approval of delegation of agreed functions to the various service providers and the directors should make sure that the appointments actually happen on terms that are consistent with industry practice, among other launch matters. At the establishment stage, directors should be thinking about potential investors when considering their duties to act in the best interests of the Fund.

Ordinary course of business

After launch of a Fund, CIMA expects the oversight, direction and management of a Regulated Fund to be conducted in a fit and proper manner, in line with the principles set out in the SoG, as described above. During the ordinary course of business of a Fund, the directors should properly minute board meetings, maintain records of board resolutions and keep evidence of enquiries made to service providers, such as emails or records of telephone conversations that take place outside of board meetings. As a Fund has six months from its financial year end to finalise its audited financial statements and to file them with CIMA, directors should ensure that they are provided with the draft financial statements in plenty of time to review them and ask any relevant questions. For a fund of funds, for example, this is particularly important because it might not be possible to finalise the audit until very late in the six month period.

If there are changes to arrangements with service providers, then the approval of these changes should be properly minuted, with directors reviewing and approving any relevant amendments to contractual documentation with existing service providers or new contractual documentation with new service providers.

If the Fund is a party to side letters undertaking to carry out certain actions, the directors should review them and be comfortable with their commercial terms. For example, if the side letter imposes extra investment restrictions, can these be carried out, and does agreeing to these impact on the rest of the Fund's strategy as reported to investors? It is not enough simply to know that legally they can be entered into by the Fund. If the investment manager has been given delegated authority to negotiate and execute side letters on behalf of the Fund, this should form part of the regular reporting to the board and the scope of such authority should be agreed – including ensuring that the investment manager obtains prior board approval if necessary. Other common provisions in side letters include additional information rights, statements of general intent as to exercise of powers, the ability to transfer shares, the ability to disclose information received from the Fund (whether to satisfy public disclosure or other legal requirements or to upstream investors in a fund of funds), and provisions that relate to the tax, legal or regulatory status of an investor. We would generally recommend that professional legal advice be obtained prior to entering into any side letter arrangements as they are a potential liability minefield for directors and as they can increase the prospect of an inadvertent breach of a director's duty. Any side letter provisions that would seek to impose an obligation upon a Fund to treat an individual investor preferentially and which would adversely affect the other investors (such as changes in cost sharing or indemnity arrangements) would usually be unacceptable.

Ongoing monitoring and crisis management

Throughout the life of a Fund, directors should be pro-active in ensuring that the investment manager is required to provide information on an ad hoc basis which might require urgent action by the board. In addition to standard regular reporting requirements, directors should be asking the investment manager and any other relevant service providers whether there is anything that should be brought to the attention of the board. A non-exhaustive list of the issues that would fall under this heading are:

- is there any actual, pending or threatened litigation against the Fund?
- are there any disputes with investors or counterparties that will fall short of actual litigation?
- will outstanding redemption requests have a significant impact on NAV at the next dealing day; if so, could such redemptions de-stabilise the Fund or adversely affect the liquidity of the Fund?
- will accepting subscriptions in respect of ERISA/pension assets have an impact on existing investors?
- are market or other conditions having or likely to have a material impact on the trading strategies of the Fund?
- is there any significant counterparty risk for 'over the counter' transactions to which the Fund is a party?
- has there been any change to or movement away from the investment strategy, policy or restrictions set out in the Offering Document?
- has there been any reduction in the investment manager's holding in the Fund?
- have there been or are there likely to be any material changes of staff at the investment manager (for example, triggering 'key-man' events) or at any other service provider?

- has the valuation function been suitably performed in accordance with the Fund's policies and the law?
- are there any issues with title verification or cash monitoring in a Private Fund?

If the Fund does find itself in difficulties, directors cannot sit back and assume that other service providers, and in particular the investment manager, will rescue the Fund without significant oversight from the directors of the Fund.

The directors are entitled to rely on the advice of suitably qualified third-parties and, in respect of areas where they do not have expertise, may be considered negligent if they make a decision without obtaining expert advice on behalf of the Fund.

It is essential that directors seek advice from the Fund's legal advisers as soon as they become aware of any circumstances that could have a material adverse effect on the management and operations of the Fund or the interests of the Fund's investors.

What are the consequences of a director not discharging its duties?

Breach of statutory obligations

The Companies Act, the Mutual Funds Act, the Private Funds Act and the Proceeds of Crime Act (among others) impose certain obligations on directors of a Fund. Some of these obligations are sanctioned by criminal penalties and, on conviction, are punishable by a potentially substantial fine and (in relation to certain offences) a custodial sentence. It is also important to note that if a Fund is in breach of a statutory obligation, the relevant legislation may also impose penalties on any 'operator' or 'officer' of the Fund (which includes a director) who is 'in default'. For these purposes, directors will be 'in default' if they knowingly and willingly authorise or permit the default, refusal or contravention that constitutes the breach.

CIMA also has the power under the Monetary Authority Act to impose significant administrative fines of up to CI$1 million (US$1.2 million) for each breach of certain provisions of the AML Regulations and other Cayman regulatory laws and regulations, including the Mutual Funds Act, the Private Funds Act, Securities Investment Business Act and the DRL ACT. The level of an administrative fine will depend on various factors including whether the breach is committed by an individual or a body corporate and if the breach is classified as minor, serious or very serious.

Breach of fiduciary duty

If directors breach their fiduciary duties to the Fund they may be found personally liable to the Fund in damages.

Negligent mis-statement

In circumstances where a director has been negligent in making a statement, for example in the Offering Document, such director may be liable for a claim in damages brought by a person who has suffered loss in reliance on that statement.

Deceit

If a director is fraudulent in misrepresenting facts by making a statement in the knowledge that it is false, or by being reckless as to whether or not the statement is true or false, for example in the Offering Document, the director could be found liable in damages to an investor or purchaser who is deceived by the statement.

The Penal Code

If a director publishes (or concurs in publishing) a written statement or account which to its knowledge is or may be misleading, false or deceptive in any material particular with intent to deceive shareholders or creditors of the Fund then the director will be guilty of an offence, punishable on conviction by up to seven years imprisonment.

Recent changes to the Penal Code also now require reporting of suspicion of overseas tax evasion as part of the AML framework in the Cayman Islands. This offence, together with obligations under the Mutual Funds Act, the Private Funds Act, and the liabilities described at paragraphs Negligent mis-statements and Deceit above, are of particular relevance to statements made in the Offering Document.

Contempt of court

If a director is aware that the Fund has been ordered by any court of competent jurisdiction either to do or refrain from doing something, or that the Fund has given an undertaking to the court to do or refrain from doing something, then the director is under a duty to take reasonable steps to ensure that the order or undertaking is complied with. If a director wilfully fails to do so, with the result that the order or undertaking is breached, the director can be punished for contempt of court. Turning a 'blind eye' to the breach may still result in liability for contempt, even if the director does not actively participate in the breach.

Fraud on, or prior to, winding-up

The Companies Act provides for a range of statutory offences relating to the actions of the directors prior to, or in connection with, a winding-up of the Fund.

Ultra vires

The Memorandum sets out the capacity and powers of the Fund and the Articles prescribe the manner in which the Fund is to be operated.

If the directors of the Fund purport to enter into any transaction that is outside the objects set out in the Memorandum, the transaction will be ultra vires and the Fund will be without capacity to enter into the transaction. Similarly, if the directors enter into a transaction on behalf of the Fund that is ultra vires their powers under the Articles, the directors are without capacity to bind the Fund.

In either circumstance, the Companies Act steps in to ensure that any such transaction with a third party is not invalid by such lack of capacity. The Fund may however bring a claim against the directors for any loss caused or damage suffered as a consequence of the ultra vires act.

Note that actions taken by the directors that are ultra vires their powers under the Articles may be capable of ratification by the shareholders. Actions taken by the directors that are ultra vires the objects in the Memorandum are not capable of ratification however. This is often not an issue in practice as funds typically have very broad general objects clauses in the Memorandum.

Indemnification

The Articles may provide for the indemnification of a director or an officer for breach of duty, save in limited circumstances such as where the director has been fraudulent or dishonest or where there has been wilful neglect or wilful default in the fulfilment of fiduciary duties. *Re City Equitable Fire Insurance [1925] Ch 407* defined what is meant by wilful neglect or default as:

> *an act, or an omission to do an act, is wilful where the person of whom we are speaking knows what he is doing and intends to do what he is doing. But if that act or omission amounts to a breach of his duty, and therefore to negligence, is the person guilty of wilful negligence? In my opinion that question must be answered in the negative unless he knows that he is committing, and intends to commit, a breach of his duty, or is recklessly careless in the sense of not caring whether his act or omission is or is not a breach of duty.*

The Cayman Islands Court of Appeal reiterated that the *Re City Equitable* definition applies under Cayman Islands law in its 2015 *Weavering* decision. Whether a director is guilty of wilful neglect or default, so that they would be unable to rely on an indemnification provision in the Articles, depends on the facts and evidence in any specific case.

Funds will also obtain directors and officers insurance.