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GLOBAL GUIDE 2017

INVESTMENT FUNDS

in British Virgin Islands, Cayman Islands, Guernsey and Jersey

The law in key jurisdictions worldwide

- Essential legal questions answered
- Analysis of critical legal issues

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Investment funds in British Virgin Islands: regulatory overview

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RETAIL FUNDS

1. What is the structure of the retail funds market? What have been the main trends over the last year?

Open-ended retail funds

The majority of investment funds established in the British Virgin Islands (BVI) are non-retail funds. In the BVI, the laws governing investment funds are mainly geared towards attracting sophisticated investors. Investment funds that give investors a right to redeem their interests in the investment fund are defined as mutual funds under the Securities and Investment Business Act 2010 (SIBA). Mutual funds are regulated by the BVI Financial Services Commission (FSC) subject to limited exceptions. There are currently two types of mutual funds that are open to investors regardless of the amount invested, private funds and public funds.

A private fund is restricted either in:

- Marketing its interests to the public.
- The number of investors it can have.

Private funds are therefore not typical retail fund products.

Public funds may be used as retail funds as such funds can market their interests to any member of the public in or from within the BVI. Public funds must be registered with the FSC. The public funds market is relatively small with currently around 90 public funds registered with the FSC. There have not been any specific changes related to public funds in the last year.

Closed-ended retail funds

Closed-ended funds (that is funds whose interests cannot be redeemed at the option of the investor), whether retail or not, are currently not regulated by the FSC. In the author's experience it is difficult for closed-ended funds to comply with retail market restrictions in other jurisdictions and the number of closed-ended funds admitting retail investors is statistically not significant. Therefore, *Questions 2 to 15* focus on open-ended retail funds registered as public funds under SIBA.

Regulatory framework and bodies

2. What are the key statutes, regulations and rules that govern retail funds? Which regulatory bodies regulate retail funds?

Open-ended retail funds

Regulatory framework. Public funds are regulated by the Securities and Investment Business Act 2010 (SIBA). The Mutual Funds Regulation 2010 (MF Regs) and the Public Funds Code 2010 (PF Code) are secondary legislation issued under SIBA.

Regulatory bodies. The Financial Services Commission (FSC) is the regulatory body for open-ended funds, including public funds.

Closed-ended retail funds

Regulatory framework. There is no regulatory framework for closed-ended retail funds in the BVI (*see Question 1, Closed-ended retail funds*).

Regulatory bodies. There is no regulatory framework for closed-ended retail funds in the BVI (*see Question 1, Closed-ended retail funds*).

3. Do retail funds themselves have to be authorised or licensed?

Open-ended retail funds

BVI fund. A public fund can be established as a company or unit trust but not as a limited partnership. A public fund carrying on business in or from within the BVI must be registered under the Securities and Investment Business Act 2010 (SIBA). A company or unit trust is deemed to carry on business from within the BVI even if it carries on business outside the BVI, if either:

- It is incorporated in the BVI (in the case of a company) or governed by BVI laws (in the case of a unit trust).
- It solicits an individual within the BVI to subscribe for or purchase its fund interests. However, a fund does not solicit an individual where the subscription or purchase is a result of an approach made by the individual to the fund without any solicitation being made by or on behalf of the fund.

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INVESTMENT FUNDS

A foreign fund (that is, a fund incorporated outside of the BVI in the case of a company or governed by a non-BVI law in the case of a unit trust) does not carry on business in the BVI solely by reason of the fact that it is managed or administered in or from within the BVI, or otherwise appoints a BVI functionary.

A public fund must appoint an investment manager, administrator (*see Question 6, Open-ended retail funds*), custodian (*see Question 7, Open-ended retail funds*) and auditor, all of which must satisfy the Financial Services Commission's (FSC's) fit and proper criteria. The FSC also assesses the directors (in the case of a company) or the trustee (in the case of a unit trust) against the FSC's criteria to determine whether they are fit and proper persons to fulfil the contemplated roles (the fit and property criteria).

In addition, to qualify to invite any member of the public to subscribe for fund interests, the invitation must be made in a prospectus registered by the FSC. The prospectus must:

- Be approved by the board (or the trustee).
- Provide a full and accurate disclosure of all information that investors would reasonably require and expect to find for the purposes of making an informed investment decision.
- Comply with the requirements for a prospectus set out in the Mutual Funds Regulation 2010 (MF Regs) and the Public Funds Code 2010 (PF Code).

Section 12 of the MF Regs contains brief requirements for the contents of a prospectus, while the PF Code contains a schedule of more prescriptive contents.

The fund must submit a written application to the FSC for registration as a public fund using the FSC's omnibus application form. An application is typically made at the same time as the application for registration of the fund's first prospectus. The application must be accompanied by a completed Form A for each of the directors of the fund (unless such persons have previously been approved by the FSC's Approved Person's Unit). The prospectus and copies of each of the agreements between the fund and its functionaries must also be submitted. An application fee of US\$1,000 is payable for the registration of the fund. An additional application fee for the registration of the prospectus of US\$250 is payable. Upon registration of the fund and the prospectus further fees of US\$1,500 and US\$500 respectively are payable. The annual registration fee for the fund is US\$1,500. The FSC's Performance Accountability Policy and Supervisory Service Standards state that a completed application for registration of a public fund should be completed in no more than two weeks.

Non-BVI fund. A non-BVI fund (that is, a fund domiciled outside of the BVI) can seek registration as a public fund or recognition as a recognised foreign fund. It generally only needs to do this if it either:

- Wishes to solicit an individual within the BVI to subscribe for or purchase its fund interests.
- Is otherwise carrying on business in or from within the BVI. However, appointing a manager or administrator located in the BVI is expressly excluded from the meaning of carrying on business in or from within the BVI.

A non-BVI fund may be recognised as a recognised foreign fund under SIBA if all of the following apply:

- It is subject to an authorisation and supervisory regime in the jurisdiction in which it is constituted, which, in the FSC's opinion, provides BVI investors with protection at least equivalent to the protection provided under SIBA for investors in public funds.
- Adequate arrangements exist for co-operation between the authorities in the home jurisdiction of the fund and the FSC.
- The fund is being operated and managed in compliance with the authorisation and supervisory regime to which it is subject.

An application must be made to the FSC for recognition as a foreign fund using the omnibus application form. A full explanation must be provided as to how the criteria for recognition are satisfied. An application fee of US\$700 is payable and the annual recognition fee is US\$1,000.

Closed-ended retail funds

See Question 1, Closed-ended retail funds.

Marketing

4. Who can market retail funds?

Open-ended retail funds

A fund cannot be promoted in or from within the BVI unless the fund is registered or recognised as a mutual fund or a foreign fund (*see Question 3, Open-ended retail funds*). The person carrying on the promotion may need to be licensed under the Securities and Investment Business Act 2010 (SIBA) to promote the fund. For example, subject to limited exceptions (such as acting for a company within the same group, or providing business to a company for which you act as a director without receiving remuneration), a licence is required under SIBA to:

- Carry on business as an investment adviser (promotion of a mutual fund by a third party in or from within the BVI may, depending on the circumstances, amount to regulated investment business as set out in SIBA).
- Arrange transactions in mutual fund interests.

Closed-ended retail funds

See Question 1, Closed-ended retail funds.

5. To whom can retail funds be marketed?

Open-ended retail funds

Public funds can be marketed to any member of the public both in and outside of the BVI (subject to foreign regulations). However, the offer must be made by way of a registered prospectus (*see Question 3*).

A recognised foreign fund is permitted to market its interests in the BVI in accordance with the authorisation and supervisory regime of its home jurisdiction.

Closed-ended retail funds

See Question 1, Closed-ended retail funds.

Managers and operators

6. What are the key requirements that apply to managers or operators of retail funds?

Open-ended retail funds

A public fund must have at all times appointed an investment manager and an administrator, which must satisfy the Financial Services Commission's (FSC's) fit and proper criteria (see *Question 3, Open-ended retail funds*). There is no requirement for either the investment manager or the administrator to be located in the BVI. An investment manager or administrator generally satisfies the FSC's fit and proper criteria if it both:

- Carries on business in a recognised jurisdiction (the FSC has issued a list of recognised jurisdictions, comprising 41 of the most widely used financial services centres).
- Meets the local requirements to carry on the business including, where applicable, holding any licence (however, if there is no local requirement to hold a licence, this does not prevent the functionary from satisfying the FSC's fit and proper criteria).

An investment manager or administrator requires a licence under the Securities and Investment Business Act 2010 (SIBA) if it is a BVI entity or has a physical presence in the BVI.

Closed-ended retail funds

Carrying on business as a closed-ended fund is currently not regulated (see *Question 1*). However, a BVI investment manager or adviser of a closed-ended fund requires a licence under SIBA or the Investment Business (Approved Managers) Regulations 2012 (Approved Manager Regulations). An administrator requires a licence under SIBA to provide certain activities for closed-ended funds. A non-BVI company acting as investment manager, adviser or administrator to a BVI closed-ended fund does not generally require a licence, unless it carries on business through a physical presence in the BVI.

Assets portfolio

7. Who holds the portfolio of assets? What regulations are in place for its protection?

Open-ended retail funds

A public fund is required to appoint a custodian in the BVI or a recognised jurisdiction. The custodian must be functionally independent from the investment manager and the administrator and meet the Financial Services Commission's fit and proper criteria (see *Question 6, Open-ended retail funds*).

Closed-ended retail funds

See *Question 1, Closed-ended retail funds*.

Legal fund vehicles

8. What are the main legal vehicles used to set up a retail fund and what are the key advantages and disadvantages of using these structures?

Open-ended retail funds

Legal vehicles. A public fund can be formed as a company or a unit trust.

Advantages. A company limited by shares registered under the BVI Business Companies Act (BCA) is by far the most common type of legal vehicle used. Investors are issued with shares in the company. The BCA is widely admired for its flexible and comprehensive company regime.

Disadvantages. A unit trust formed under BVI laws is also flexible (like a company), but it does not benefit from the backing of company legislation. Unit trusts issue units.

Closed-ended retail funds

Legal vehicles. See *Question 1, Closed-ended retail funds*.

Advantages. See *Question 1, Closed-ended retail funds*.

Disadvantages. See *Question 1, Closed-ended retail funds*.

Investment and borrowing restrictions

9. What are the investment and borrowing restrictions on retail funds?

Open-ended retail funds

There are no statutory investment or borrowing restrictions on open-ended funds, including public funds.

Closed-ended retail funds

The position is the same for closed-ended funds (see *above, Open-ended retail funds*).

10. Can the manager or operator place any restrictions on the issue and redemption of interests in retail funds?

Open-ended retail funds

Open-ended funds can agree any restrictions on the issue and redemption of interests with their investors at the time they subscribe for such interests. In addition, the Public Funds Code 2010 (PF Code) requires a public fund to adopt policies and procedures for the issue and redemption of fund interests. The policies must be appropriate for the nature, size, complexity, structure and diversity of the fund and the fund property. They must also meet prescribed minimum criteria set out in the PF Code including the timing of dealing and redemption of fund interests. The introduction of additional restrictions in respect of an investor's existing interest can only be achieved in accordance with the consent mechanisms contained in the fund's constitutional documents.

Closed-ended retail funds

See *Question 1, Closed-ended retail funds*.

11. Are there any restrictions on the rights of participants in retail funds to transfer or assign their interests to third parties?

Open-ended retail funds

There are no statutory restrictions on the ability of investors in open-ended funds to transfer their interests to third parties, although the constitutional documents of the fund will normally contain restrictions.

ONLINE RESOURCES

BVI Financial Services CommissionW www.bvifsc.vg

Description. The BVI Financial Services Commission is the Territory's single financial services regulator. The BVI FSC website contains links to all relevant financial legislation, policy guidelines, guidance notes and statistics.

BVI Official GazetteW www.bvigazette.org

Description. The *Official Gazette* is the official publication of the Government of the Virgin Islands. It is printed by the Gazette Unit, a unit of the Cabinet Office. It is free to register and access legislation online that has been published since 2007. BVI Financial Services Commission.

Closed-ended retail funds

The position is the same for closed-ended funds (*see above, Open-ended retail funds*).

Reporting requirements**12. What are the general periodic reporting requirements for retail funds?****Open-ended retail funds**

Investors. The audited financial statements must be made available to investors with the registered prospectus within six months of the year end.

Regulators. A public fund's audited financial statements must be filed with the Financial Services Commission (FSC) within six months of the year end. A fund must submit an annual return to the FSC by 30 June each year, in relation to the position of the fund as at 31 December of the previous year.

Closed-ended retail funds

Closed-ended funds have no statutory reporting requirements.

Tax treatment**13. What is the tax treatment for retail funds?****Open-ended retail funds**

Funds. A fund registered under the Securities and Investment Business Act 2010 is exempt from all provisions of the Income Tax Act. It will not be liable to BVI payroll tax unless it has employees in the BVI. Customary fees paid to directors are generally outside the scope of the payroll tax.

Resident investors. The following are exempt from income tax (*Income Tax Act*):

- All dividends and amounts that a fund formed as a BVI company pays to investors (including redemption proceeds).
- Capital gains realised by investors in relation to fund interests of a fund formed as a BVI company.

There are no estate, inheritance, succession or gift taxes payable in the BVI in relation to shares in a fund. Technically, income tax may apply to income and capital gains arising from interests in funds. However, as the income tax rate is currently zero, and not expected to change, this is academic.

However, as the income tax rate is currently zero (and is not expected to change), this is academic.

Non-resident investors. The following are exempt from payment of income tax (*Income Tax Act*):

- All dividends and amounts paid by a fund to non-resident investors (including redemption proceeds).
- Capital gains realised by non-resident investors from fund interests.

There are no estate, inheritance, succession or gift taxes payable in the BVI in relation to shares in funds.

Closed-ended retail funds

Funds. A closed-ended fund established as a company is exempt from all provisions of the Income Tax Act. The same rules apply as for open-ended retail funds (*see above, Open-ended retail funds: Funds*).

Resident investors. The same rules apply as for open-ended retail funds (*see above, Open-ended retail funds: Resident investors*).

Non-resident investors. The same rules apply as for open-ended retail funds (*see above, Open-ended retail funds: Non-resident investors*).

Quasi-retail funds**14. Is there a market for quasi-retail funds in your jurisdiction?**

The author is not aware of any significant market for quasi-retail funds.

Reform**15. What proposals (if any) are there for the reform of retail fund regulation?**

The author is not aware of any proposal to reform retail fund regulation.

HEDGE FUNDS**16. What is the structure of the hedge funds market? What have been the main trends over the last year?**

The regulatory regime applicable to investment funds in the BVI differentiates between open-ended and closed-ended funds. Most hedge funds are open-ended funds, regulated under the Securities and Investment Business Act 2010 (SIBA). Open-ended hedge funds are either regulated by the Financial Services Commission as private funds, professional funds or public funds. As at 31 December 2014, there were just under 2,200 funds recognised or registered under SIBA. The majority of these are recognised as professional funds (1,511), followed by private funds (539) and public funds (87). Professional funds require an initial investment of at least US\$100,000 subject to certain exemptions. These figures indicate that BVI funds are mostly used as non-retail funds.

Regulatory framework and bodies**17. What are the key statutes and regulations that govern hedge funds in your jurisdiction? Which regulatory bodies regulate hedge funds?****Regulatory framework**

Open-ended hedge funds are governed by the Securities and Investment Business Act 2010 and the Mutual Funds Regulation 2010. The Financial Services Commission is the regulator for open-ended hedge funds.

Private funds

A private fund is restricted to either:

- Having no more than 50 investors.
- Only making an invitation to subscribe for or purchase fund interests on a private basis.

See also *Question 20, Private funds*.

Professional funds

In relation to a professional fund:

- Fund interests can only be issued to professional investors (see below).
- The initial investment for all investors (other exempt investors) cannot be less than US\$100,000 or the foreign currency equivalent.

A professional investor is a person:

- Whose ordinary business involves, whether for his own account or the account of others, the acquisition or disposal of property of the same kind as:
 - the fund property; or
 - a substantial part of the fund property.
- Who has signed a declaration that he both:
 - whether individually or jointly with his spouse, has net worth in excess of US\$1 million or its foreign currency equivalent; and
 - consents to being treated as a professional investor.

Exempt investors comprise:

- The manager, administrator, promoter or underwriter of the fund.
- Any employee of the manager or promoter of the fund.

Regulatory bodies

The regulator is the FSC (see *Question 2*).

18. How are hedge funds regulated (if at all) to ensure compliance with general international standards of good practice?

All regulated funds must have their annual financial statements audited (if not exempted by the Financial Services Commission (FSC)). The audited financial statements must be submitted to the FSC within six months of the financial year end of the fund.

Public funds must adopt detailed pricing and valuation policies. Details of the policies must be made available to investors in public funds.

The BVI has a strict anti-money laundering and anti-terrorist financing regime in place. The BVI government, the FSC and other statutory bodies liaise with regulators in other jurisdictions to ensure compliance with international standards of good practice. All hedge funds are subject to:

- Anti-money Laundering Regulations 2008.
- Anti-money Laundering and Terrorist Financing Code of Practice 2008.

This legislation provides a BVI hedge fund with the option to outsource client verification requirements to its non-BVI based administrator if the administrator is based in a recognised jurisdiction (see *Question 6, Open-ended retail funds*).

19. Who can market hedge funds?

The position is the same as for retail funds (see *Question 4*).

20. To whom can hedge funds be marketed?

The position is essentially the same as for retail funds (see *Question 5*). However, a private fund may either have a maximum of 50 investors or offer interests in the fund on a private basis only.

Investment restrictions**21. Are there any restrictions on local investors investing in a hedge fund?**

The position is the same as for retail funds (see *Question 5*).

Assets portfolio**22. Who holds the portfolio of assets? What regulations are in place for its protection?**

A private or professional fund must, subject to limited exceptions, at all times have a custodian appointed (see also *Question 7*). According to guidance from the Financial Services Commission, an exemption from the custodian requirement will normally be available in the following circumstances:

- Funds who have appointed prime brokers that perform the same function.
- Feeder funds in master/feeder structures.
- Funds operating as fund of funds.
- Funds in the process of winding down.
- Funds that invest in esoteric assets.

Requirements**23. What are the key disclosure or filing requirements (if any) that must be completed by the hedge fund?**

A private or a professional fund must file any offering document with the Financial Services Commission (FSC) within 14 days of the date of its issue to any investor. Amendments to the offering documents previously provided to the FSC must be notified to the FSC within 14 days.

All regulated funds must submit an annual return for statistical and reporting purposes setting out summary financial information as at 31 December.

24. What are the key requirements that apply to managers or operators of hedge funds?

The same rules for retail funds apply (*see Question 4*).

Any person carrying on business in or from within the BVI as an investment manager, adviser or administrator of a fund must hold a licence issued by the Financial Services Commission.

Legal fund vehicles and structures**25. What are the main legal vehicles used to set up a hedge fund and what are the key advantages and disadvantages of using these structures?**

BVI funds are established as:

- Companies limited by shares (including as segregated portfolio companies) under the Business Companies Act 2010 (BCA).
- International limited partnerships under the Partnership Act 1996.
- Unit trusts governed by the laws of the BVI.

The vast majority of BVI hedge funds are established as companies under the BCA. The BCA is widely regarded as cutting edge corporate legislation and provides a modern and flexible regime suitable for use for hedge fund vehicles.

Tax treatment**26. What is the tax treatment for hedge funds?****Funds**

See *Question 13*.

Resident investors

See *Question 13*.

Non-resident investors

See *Question 13*.

Restrictions**27. Can participants redeem their interest? Are there any restrictions on the right of participants to transfer their interests to third parties?**

The position is the same as for retail funds (*see Questions 10 and 11*).

Reform**28. What (if any) proposals are there for the reform of hedge fund regulation?**

In December 2014, a consultation paper was filed with the Financial Services Commission (FSC) setting out a proposal for the following two new fund products that are designed for start-up and emerging markets and family and friends funds:

- BVI Incubator Fund.
- BVI Approved Fund.

In June 2015 new legislation, the Securities and Investment Business (Incubator and Approved Funds) Regulations 2015 (Regulations), created both the incubator fund and the approved fund.

The incubator fund may operate for two years (three years with FSC permission) with no administrator, custodian or manager. Certain thresholds apply, including a maximum of 20 investors; a minimal initial investment from each investor of US\$20,000 and an overall cap on the value of the fund's net assets of US\$20 million. At the end of its term as an incubator fund (or on exceeding any of the above thresholds), the fund must either apply for recognition as a private or professional fund, or apply for approval as an approved fund, or it must wind-up.

The approved fund regime is geared towards funds of a longer term and with a private investor offering. Its thresholds are a maximum of 20 investors and a cap of US\$100 million on the value of the net assets of the fund. The approved fund is not required to appoint an auditor, manager or custodian. It must have an administrator. There is no time limit on the life span of the approved fund.

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Recent transactions

- Advising on the launch of two multi-billion US dollar hedge funds.
- Advising a US pension fund manager on investment in a BVI private equity fund.
- Advising a sovereign fund on investment in a BVI company operating in various Latin American countries in the telecommunications sector.

Languages. English

Professional associations/memberships. Member of the British Virgin Islands Bar Association.

Publications. *Private equity in British Virgin Islands: market and regulatory overview Private Equity Global Guide 2015/16 (co-author).*

Investment funds in Cayman Islands: regulatory overview

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RETAIL FUNDS

1. What is the structure of the retail funds market? What have been the main trends over the last year?

Open-ended retail funds

The Cayman Islands are not primarily known as a retail fund jurisdiction. Its laws and regulations applicable to investment funds are geared mainly towards attracting institutional investors.

Open-ended funds established in or marketed to the public in the Cayman Islands (that is, funds where investors can voluntarily redeem their interests) are considered "mutual funds" under the Mutual Funds Law (2015 Revision) (MF Law) and therefore must be regulated by the Cayman Islands Monetary Authority (CIMA), unless they fall within a limited exception.

Three types of CIMA-regulated funds (Regulated Funds) can admit retail investors (that is, investors who invest less than US\$100,000):

- Funds licensed under section 4(1)(a) of the MF Law (Licensed Funds).
- Funds licensed under section 4(1)(b) of the MF Law (Administered Funds), that is, funds for which a CIMA-licensed mutual fund administrator provides the principal office and has delegated regulatory responsibilities.
- Funds registered under section 4(3) of the MF Law (Registered Funds) by virtue of being listed on an approved stock exchange.

In theory, retail investors can also invest in unregulated mutual funds (Unregulated MFs). These are funds exempted from registration with CIMA under section 4(4) of the MF Law due to having 15 or fewer investors, a majority of whom can appoint and remove the operator of the fund (the directors, general partner or trustee, as applicable). It is impossible to be certain, but it can be inferred that being limited to 15 investors makes them generally unsuitable for marketing to retail investors and therefore statistically insignificant as retail funds.

Although investment fund regulation in the Cayman Islands is generally geared towards institutional investors, there is one exception to this. The Retail Mutual Funds (Japan) Regulations (2007 Revision), as amended (Retail Japan Regulations) provide a compliance framework for Licensed Funds that will market to retail investors in Japan, enabling them to automatically comply with the applicable Japanese securities laws. However, these funds are merely a sub-set of Licensed Funds, which themselves only comprise 1% of Regulated Funds.

According to CIMA's latest statistical digest (for 2013) only 8% of Regulated Funds have a minimum required investment of less than US\$50,000 and only 5% require a minimum investment between US\$50,000 and US\$100,000.

Between 31 December 2014 and 31 December 2015, the number of Licensed Funds declined by three (from 104 to 101) and the number of Administered Funds also declined by six (from 386 to 380).

Closed-ended retail funds

Closed-ended funds (that is, funds whose equity interests cannot be redeemed at the option of the investor), whether retail or non-retail, are currently not regulated by CIMA under the MF Law.

As unregulated vehicles, it is difficult to know how many closed-ended funds exist, and harder still to guess the number admitting retail investors. However, based on the author's experience and the fact that, as unregulated funds, they would presumably find it even more difficult to comply with retail marketing restrictions in other jurisdictions, the author believes the number of closed-ended funds admitting retail investors is statistically insignificant.

Regulatory framework and bodies

2. What are the key statutes, regulations and rules that govern retail funds? Which regulatory bodies regulate retail funds?

Open-ended retail funds

Regulatory framework. Open-ended funds are regulated by the Mutual Funds Law (MF Law) (*see Question 1*). The Retail Japan Regulations also apply to Licensed Funds that market to retail investors in Japan (*see Question 1*).

Directors of corporate Regulated Funds are regulated by The Directors Registration and Licensing Law 2014 (Director Licensing Law) as supplemented by The Directors Registration and Licensing (Registration and Licensing) Regulations 2014.

The Securities Investment Business Law (2015 Revision) (SIB Law) provides that the Cayman Islands Monetary Authority (CIMA) is responsible for the licensing and control of persons carrying on "securities investment business" in or from within the Cayman Islands (*see Question 4*).

Regulatory bodies. CIMA is the regulatory body for open-ended retail funds (*see Question 1*).

Closed-ended retail funds

Regulatory framework. There is no regulatory framework for closed-ended retail funds in the Cayman Islands (*see Question 1*).

Regulatory bodies. There is no regulatory body for closed-ended retail funds in the Cayman Islands (*see Question 1*).

3. Do retail funds themselves have to be authorised or licensed?

Open-ended retail funds

There following types of open-ended fund can admit retail investors (*see Question 1*):

- Licensed Funds.
- Administered Funds.
- Registered Funds listed on an approved stock exchange.
- Unregulated Mutual Funds (MFs).

Of the four types, only Unregulated MFs are not required to be regulated by CIMA. The licensing and registration requirements for Regulated Funds are set out below.

Any proposed director of a corporate fund regulated by CIMA must register with CIMA (via CIMA's online registration portal) before he can be appointed.

Licensed Funds. A Licensed Fund must have either:

- For companies or limited partnerships: a registered office in the Cayman Islands.
- For unit trusts: a trustee that is a trust company licensed under the Banks and Trust Companies Law (2013 Revision) (BTC Law).

To apply to be licensed as a Licensed Fund, the following must be submitted to CIMA:

- An offering document (or the latest draft) describing the offered interests in all material respects and containing any other information necessary for an investor to make an informed investment decision (CIMA prescribes certain information that must be included).
- A completed application (Form MF3).
- A certified copy of the certificate of incorporation or registration.
- Completed personal questionnaires, three references and police clearance certificates (or affidavit of no convictions for certain individuals) for:
 - directors of the fund (for a company);
 - directors of the fund's trustee (for a unit trust); or
 - the fund's general partner or the general partner's directors, as applicable (for a limited partnership).
- Background details on the fund's service providers, if not included in the offering document.
- For an existing fund, a copy of the most recent annual audited accounts.
- A consent letter from an approved local auditor.

- A consent letter from an administrator.
- The prescribed licence fee (US\$4,268.29) and application fee (US\$365.85).
- Details of who will be responsible for dealing with queries from CIMA and the payment of fees (such as the registered office provider or local administrator).

CIMA must be satisfied that:

- Each promoter of the fund is of sound reputation (a promoter is any person responsible for preparation and distribution of the fund's offering document other than its professional advisers).
- The fund's administration will be undertaken by persons:
 - with sufficient expertise;
 - of sound reputation; and
 - who are fit and proper to be in their respective positions.
- The fund's business and any offering of its interests will be carried out in a proper way.

CIMA may grant a licence subject to any conditions that it considers appropriate.

Administered Funds. An Administered Fund must have a principal office in the Cayman Islands provided by a CIMA-licensed mutual fund administrator.

To register as an Administered Fund, the following must be submitted to CIMA:

- An offering document (or the latest draft) describing the offered interests in all material respects and containing any other information necessary for an investor to make an informed investment decision.
- Completed application (Forms MF2 and MF2A).
- A certified copy of the certificate of incorporation (or equivalent).
- A consent letter from an approved local auditor.
- The prescribed registration fee (US\$4,268.29) and application fee (US\$365.85).

The administrator providing the fund's principal office must be satisfied that:

- Each promoter of the fund is of sound reputation.
- The fund's administration will be undertaken by persons with sufficient expertise and who are of sound reputation.
- The fund's business and any offering of its interests will be carried out in a proper way.

Registered Funds. To admit retail investors, a Registered Fund must be listed on an approved stock exchange.

To register as a Registered Fund, the following must be submitted to CIMA:

- An offering document (or the latest draft) describing the offered interests in all material respects and containing any other information necessary for an investor to make an informed investment decision.

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- A completed application Form MF1.
- A certified copy of the certificate of incorporation or registration.
- A consent letter from an approved local auditor.
- A consent letter from an administrator.
- The prescribed registration fee (US\$4,268.29) and application fee (US\$365.85).
- Details of who will be responsible for dealing with queries from CIMA and the payment of fees (such as the registered office provider or local administrator).

Closed-ended retail funds

There are no regulatory requirements for closed-ended funds (*see Question 1, Closed-ended retail funds*).

Marketing

4. Who can market retail funds?

Open-ended retail funds

The Securities Investment Business Law (SIB Law) provides for the licensing and control of persons carrying on "securities investment business" in or from within the Cayman Islands by the Cayman Islands Monetary Authority (CIMA). Securities investment business includes dealing in, arranging deals in and advising on securities. Accordingly, the marketing of interests in funds will generally constitute securities investment business.

With limited exceptions for public authorities and so on, the SIB Law applies to:

- Any entity formed or registered in the Cayman Islands carrying on securities investment business.
- Any person that establishes a place of business in the Cayman Islands from which securities investment business is carried out.

Any of the foregoing will require a licence under the SIB Law to carry on securities investment business, unless the entity or person:

- Qualifies as an "excluded person".
- Files the relevant annual declaration and fee (US\$6,097.56) with CIMA before commencing securities investment business (and by 31 January each year thereafter).

An entity or person will qualify as an excluded person if it only carries on securities investment business with:

- Group companies (that is, other companies within the same group of companies).
- Sophisticated persons, meaning persons who:
 - are regulated by CIMA;
 - are regulated by a recognised overseas regulatory authority;
 - have securities listed on a recognised security exchange; or
 - have the knowledge and experience and are capable of evaluating the merits of a proposed transaction with a value of at least US\$100,000.
- High net worth persons, meaning individuals with a net worth of at least US\$1 million or any person with total assets of at least US\$5 million.

- Entities in which the investors are all sophisticated or high net worth persons.
- Persons regulated in relation to securities investment business by a recognised overseas regulatory authority.

Closed-ended retail funds

The position is the same as for open-ended retail funds (*see above, Open-ended retail funds*).

5. To whom can retail funds be marketed?

Open-ended retail funds

If incorporated as an exempted company, a fund's securities cannot be offered to the public in the Cayman Islands unless listed on the Cayman Islands Stock Exchange.

Any other type of Regulated Fund or an Unregulated MF can market its interests to the public in the Cayman Islands through a person appropriately licensed under the Securities Investment Business Law (SIB Law).

Overseas open-ended funds that do not register with the Cayman Islands Monetary Authority (CIMA) as a Regulated Fund, can only market their interests to the public in the Cayman Islands through a person appropriately licensed under the SIB Law, and provided that either:

- The interests are listed on a stock exchange approved by CIMA.
- The fund is regulated in a category and by an overseas regulator approved by CIMA.

However, for this purpose, "public in the Cayman Islands" does not include the following categories of person (meaning an overseas fund will not be restricted in marketing to them from outside the Cayman Islands):

- Sophisticated persons (as defined in the SIB Law) (*see Question 4*).
- High net worth persons (as defined in the SIB Law) (*see Question 4*).
- Entities in which all the investors are sophisticated or high net worth persons.
- Exempted or ordinary non-resident Cayman Islands companies, or any director or officer of the same acting in such capacity.
- Overseas companies registered as foreign companies in the Cayman Islands, or any director or officer of the same acting in such capacity.
- Any Cayman Islands exempted, ordinary non-resident or foreign company acting as general partner of a Cayman Islands exempted limited partnership, or any director or officer of the same acting in such capacity.
- The trustee of any Cayman Islands exempted trust.

Closed-ended retail funds

Closed-ended funds can market their interests to the public in the Cayman Islands through a person appropriately licensed under the SIB Law.

Overseas closed-ended funds can freely market their interests to the public in the Cayman Islands provided they do so from outside the Cayman Islands, and not from a place of business in the Cayman Islands.

Managers and operators

6. What are the key requirements that apply to managers or operators of retail funds?

Open-ended retail funds

The following key requirements apply to managers and operators of open-ended funds:

- A corporate Regulated Fund or the corporate general partner of a limited partnership Regulated Fund must have at least two directors.
- All the directors of a corporate Regulated Fund must be registered with the Cayman Islands Monetary Authority (CIMA) under the Directors Licensing Law.
- The trustee of a Licensed Fund must be licensed under the Banks and Trust Company Law (BTC Law).
- Investment managers incorporated or registered in the Cayman Islands must generally be regulated under the Securities Investment Business Law (SIB Law) (see Question 4).
- Any director, manager or officer of a fund regulated by CIMA must be a "fit and proper person", as determined by reference to this person's:
 - honesty, integrity and reputation;
 - competence and capability; and
 - financial soundness.

Closed-ended retail funds

Investment managers of closed-ended funds, if incorporated or registered in the Cayman Islands, will generally be carrying on securities investment business and require regulation under the SIB Law, unless the fund does not invest in "securities" (as defined in the SIB Law).

Assets portfolio

7. Who holds the portfolio of assets? What regulations are in place for its protection?

Open-ended retail funds

Licensed Funds to which the Retail Japan Regulations apply must appoint a custodian in an approved jurisdiction.

Apart from this exception, there are currently no rules requiring the appointment of a custodian or broker to hold a fund's portfolio assets.

Closed-ended retail funds

There are no restrictions applicable to closed-ended funds.

Legal fund vehicles

8. What are the main legal vehicles used to set up a retail fund and what are the key advantages and disadvantages of using these structures?

Open-ended retail funds

Legal vehicles. Open-ended funds can be formed as:

- **Companies.** The exempted company limited by shares is the most commonly used vehicle for regulated open-ended funds (accounting for 78% of Regulated Funds, based on the Cayman Islands Monetary Authority's (CIMA's) statistical digest for 2013). Most of these are standard exempted companies, but about 16% of such companies are segregated portfolio companies (in which separate portfolios can be created with assets and liabilities that are legally ring-fenced).

Exempted companies and their shares are widely understood and in addition to a body of Cayman Islands jurisprudence, the Cayman Islands courts can draw on a long tradition of relevant case law from England and the rest of the Commonwealth. A company has legal personality separate from its shareholders and can issue shares in different classes and series. A shareholder's liability for the company's debts is limited by statute to the amount unpaid on its shares (which in an investment fund will usually be issued fully paid).

- **Limited partnerships.** These are registered under the Exempted Limited Partnership Law 2014. Cayman Islands exempted limited partnerships are underpinned by English partnership law, but are modified by statute to make them more suitable for use as investment funds. For example, exempted limited partnerships, while not having separate legal personality, can sue and be sued in their own name.
- **Unit trusts.** These are governed by the Trusts Law (2011 Revision). Unit trusts are underpinned by English trust law, but are modified by statute to make them more suitable for use as investment funds. For example, STAR trusts (Special Trusts - Alternative Regime) are not subject to any perpetuity period and can have purposes as their objects.

Advantages/disadvantages. The key advantages and disadvantages of the different types of vehicle are:

- **Flexibility.** Companies are generally governed by more rigid rules than those applicable to limited partnerships and unit trusts (for example, in relation to provisions regarding maintenance of capital, the method of changing their constitutional documents and so on).
- **Legal personality.** Companies have separate legal personality, while limited partnerships must operate through their general partner, and unit trusts through their trustee.
- **Additional vehicles.** Exempted limited partnerships require at least one general partner that is established or registered in the Cayman Islands and unit trusts require a trustee, who will usually insert a controlled subsidiary for liability protection.
- **Regulatory requirements.** A Licensed Fund that is a unit trust requires a trustee licensed under the Banks and Trust Company Law (BTC Law).

- **Overseas requirements.** The choice of vehicle will often depend on whether it can qualify for specific tax or regulatory treatment in an overseas jurisdiction (for example, unit trusts are generally used for the Japanese market and limited partnerships for the Israeli market).

Closed-ended retail funds

The position is the same as for open-ended funds (*see above, Open-ended retail funds*).

Investment and borrowing restrictions

9. What are the investment and borrowing restrictions on retail funds?

Open-ended retail funds

There are no statutory investment or borrowing restrictions on open-ended funds.

Closed-ended retail funds

The position is the same as for open-ended funds (*see above, Open-ended retail funds*).

10. Can the manager or operator place any restrictions on the issue and redemption of interests in retail funds?

Open-ended retail funds

Open-ended funds can agree any restrictions on the issue and redemption of interests with their investors at the time they subscribe for such interests. The introduction of additional restrictions in respect of an investor's existing interests can only be achieved in accordance with the consent mechanisms contained in the fund's constitutional documents.

Closed-ended retail funds

The position for closed-ended retail funds is the same as for open-ended funds (*see above, Open-ended retail funds*).

11. Are there any restrictions on the rights of participants in retail funds to transfer or assign their interests to third parties?

Open-ended retail funds

There are no statutory restrictions on the ability of participants in open-ended funds to transfer or assign their interests to third parties. However, the constitutional documents of such funds usually contain restrictions, except where the interests are listed on a stock exchange.

Closed-ended retail funds

The position for closed-ended retail funds is the same as for open-ended funds (*see above, Open-ended retail funds*).

Reporting requirements

12. What are the general periodic reporting requirements for retail funds?

Open-ended retail funds

If the fund is regulated by the Cayman Islands Monetary Authority (CIMA), it must file the following with CIMA within six months of the end of each financial year:

- Audited financial statements (audited by an approved local auditor).
- Fund Annual Return.

Closed-ended retail funds

Closed-ended funds have no statutory reporting requirements.

Tax treatment

13. What is the tax treatment for retail funds?

Open-ended retail funds

There is no Cayman Islands tax applicable to payments made to or from an open-ended fund.

Closed-ended retail funds

There is no Cayman Islands tax applicable to payments made to or from a closed-ended fund.

Quasi-retail funds

14. Is there a market for quasi-retail funds in your jurisdiction?

The author is not aware of any significant market for quasi-retail funds.

Reform

15. What proposals (if any) are there for the reform of retail fund regulation?

The author is not aware of any proposals to reform retail fund regulation.

HEDGE FUNDS

16. What is the structure of the hedge funds market? What have been the main trends over the last year?

The regulatory regime in the Mutual Funds Law (MF Law) distinguishes between open-ended funds (which are mostly hedge funds) and closed-ended funds (which are generally not hedge funds).

Open-ended hedge funds will either be regulated by the Cayman Islands Monetary Authority (CIMA) as Licensed Funds, Administered Funds or Registered Fund, or will be Unregulated MFs and therefore not subject to regulation by CIMA (*see Question 1*).

ONLINE RESOURCES**Cayman Islands Monetary Authority (CIMA)**W www.cimoney.com.ky

Description. This is the CIMA website. It provides useful information and has a feature that allows users to search for regulated entities.

As at 31 December 2015, the total number of Regulated Funds was 10,940 (down from 11,010 a year earlier). The vast majority of these (96%) are Registered Funds (10,459, down from 10,520 a year earlier). Approximately 87% (about 9,500) of these Regulated Funds require an investment of at least US\$100,000 (*see Question 1*).

These figures reveal the predominance of the non-retail, institutional market. To register as a Registered Fund (rather than obtain a licence as a Licensed Fund or register as an Administered Fund), a fund must satisfy one of the following criteria:

- Require a minimum initial investment of at least US\$100,000.
- Have its interests listed on an approved stock exchange.
- Be a "master fund" (*see below*) that satisfies one of the two conditions above.

Based on the figures above, Registered Funds listed on an approved stock exchange generally still require an investment of at least US\$100,000 and are therefore listed for reasons other than the ability to admit retail investors.

The slight decrease in the number of Regulated Funds reflects a mature and relatively stable market. Numbers decreased in the first quarter of 2015 due to year end de-registrations, but increased in each subsequent quarter.

A master fund must register with CIMA under the MF Law if it is an open-ended Cayman Islands vehicle trading in investments that has one or more "regulated feeder funds" (that is, a fund that is itself a Regulated Fund, and conducts more than 51% of its investing through the master fund).

Master funds will generally qualify for registration as Registered Funds under section 4(3) of the MF Law and require the:

- Filing of a Form MF4.
- Payment of the annual fee (US\$3,048.78) and application fee (US\$365.85).

Importantly, master funds can no longer rely on the Unregulated MF exemption in section 4(4) of the MF Law (*see Question 1*).

Regulatory framework and bodies**17. What are the key statutes and regulations that govern hedge funds in your jurisdiction? Which regulatory bodies regulate hedge funds?**

Open-ended hedge funds are regulated by the Mutual Funds Law (MF Law) (*see Question 16*).

18. How are hedge funds regulated (if at all) to ensure compliance with general international standards of good practice?

The offering document of a Regulated Fund must:

- Describe the equity interests being offered in all material respects.
- Contain the information necessary to enable a prospective investor to make an informed decision whether or not to subscribe for or purchase the interests (the Cayman Islands Monetary Authority (CIMA) prescribes some information that must be included in the offering documents of Licensed Funds, and will generally expect to see such information in the offering documents of all Regulated Funds).

All Regulated Funds must have their financial statements audited annually by an approved local auditor. The audited statements must be submitted to CIMA, together with a Fund Annual Return, within six months of the fund's financial year end.

CIMA has issued guidance on corporate governance that is applicable to all Regulated Funds, and takes non-compliance into account when determining if the fund is being managed in a fit and proper manner. CIMA can impose significant sanctions on funds and their operators if it determines that a regulated fund is not being managed in a fit and proper manner or is otherwise in breach of the Mutual Funds Law (MF Law).

The Cayman Islands operates a strong anti-money laundering and anti-terrorist financing regime. The Cayman Islands government and CIMA actively engage with regulators in other jurisdictions to ensure compliance with international standards of good practice. All hedge funds are subject to the:

- Proceeds of Crime Law (2014 Revision).
- Misuse of Drugs Law (2014 Revision).
- Terrorism Law (2015 Revision).

In addition, all Regulated Funds must comply with the detailed anti-money laundering compliance regime contained in the:

- Money Laundering Regulations (2015 Revision).
- Guidance Notes on those regulations issued by CIMA.

Marketing**19. Who can market hedge funds?**

The position is the same as for retail funds (*see Question 4*).

20. To whom can hedge funds be marketed?

The position is the same as for retail funds (*see Question 5*).

Investment restrictions**21. Are there any restrictions on local investors investing in a hedge fund?**

The position is the same as for retail funds (*see Question 5*).

Assets portfolio**22. Who holds the portfolio of assets? What regulations are in place for its protection?**

The position is the same as for retail funds (see *Question 7*).

Requirements**23. What are the key disclosure or filing requirements (if any) that must be completed by the hedge fund?**

For the filing requirements to register with the Cayman Islands Monetary Authority (CIMA) as a regulated fund, see *Question 3*.

For the filing requirements for Regulated Funds that are master funds, see *Question 16*.

For annual account filings requirements applicable to Regulated Funds, see *Question 18*.

Regulated Funds must also comply with the following ongoing requirements:

- If the fund is offering its interests to investors on an ongoing basis and becomes aware that something in its offering document is materially affected by any change, it must file an updated offering document with CIMA within 21 days (which can take the form of a supplement).
- Any additional director of a corporate fund must be registered with CIMA before he can be appointed.
- Annual fees must be paid to CIMA by 15 January each year.

24. What are the key requirements that apply to managers or operators of hedge funds?

The position is the same as for retail funds (see *Question 6*).

Legal fund vehicles and structures**25. What are the main legal vehicles used to set up a hedge fund and what are the key advantages and disadvantages of using these structures?**

These are the same as for retail funds (see *Question 8*).

Tax treatment**26. What is the tax treatment for hedge funds?**

There is no Cayman Islands tax applicable to payments made to or from a Cayman Islands fund.

Restrictions**27. Can participants redeem their interest? Are there any restrictions on the right of participants to transfer their interests to third parties?**

The position is the same as for retail funds (see *Questions 10 and 11*).

Reform**28. What (if any) proposals are there for the reform of hedge fund regulation?**

In September 2015, the Mutual Funds Law and the Securities Investment Business Law were amended to introduce an "opt in" regulatory framework for purposes of the EU's Alternative Investment Fund Managers Directive (AIFMD). Subject to obtaining European Securities and Markets Authority (ESMA) approval, this regulatory regime is designed to enable Cayman Islands investment funds and managers to market in the EU under the AIFMD passport system. Full details of the regime are to be contained in regulations that are expected to be issued during 2016.

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Professional qualifications. England and Wales, Solicitor, 2000 (non-practising); Cayman Islands, Attorney-at-law, 2004

Areas of practice. Corporate and commercial; investment funds and private equity; mergers and acquisitions.

Recent transactions

- Advising a leading Canadian fund manager on the launch of a Can\$600 million alternative credit fund.
- Advising on an innovative investment fund structure to syndicate participation in an aircraft financing transaction.
- Advising a US private equity fund on the structuring of its acquisition vehicles in connection with the US\$130m acquisition of a UK online travel agency.
- Advising an Israeli fund manager on the launch of a US\$400m private equity fund.
- Advising on multiple fund financings secured against capital calls.
- Advising on multiple open-ended and closed-ended fund launches for existing and new manager clients.
- Advising leading Israeli and Chinese fund managers on the establishment of a jointly-managed venture capital fund to invest in Israeli and Israeli-related companies operating in China.

Investment funds in Guernsey: regulatory overview

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RETAIL FUNDS

1. What is the structure of the retail funds market? What have been the main trends over the last year?

Open-ended retail funds

A significant number of open-ended funds are established in Guernsey and the island continues to attract non-Guernsey open-ended funds due to its ability to provide high quality administration, management and custody services. Such vehicles are often designed to be promoted to institutional or professional investors, rather than retail investors, but they can also be used as retail funds. The funds regime in Guernsey is highly flexible and most types of funds can be used in a number of different markets, including the retail markets.

As at end of September 2015, the Guernsey Financial Services Commission (GFSC) announced that the total net asset value of funds under management and administration for Guernsey domiciled open-ended funds was GB£39.4 billion. Non-Guernsey open-ended funds that are administered or managed in Guernsey provided a total net asset value of GB£47 billion.

Closed-ended retail funds

The funds sector (and in particular the closed-ended fund sector) is one of the main pillars of the finance industry in Guernsey, with the net asset value of all funds under management or administration in Guernsey being GB£224.8 billion at the end of September 2015. The majority of funds established in Guernsey are designed to be promoted to institutional or professional investors, rather than retail investors. However, Guernsey has a significant number of listed funds, whose shares can be acquired by the public on the secondary market. Guernsey continues to be the global leader for non-UK London Stock Exchange listings, with 129 Guernsey entities listed on the Main Market, AIM or the SFM as at the end of December 2015. Guernsey funds are also listed on many other exchanges such as the CISE, Euronext, ISE, ASX and TSX.

In the past year, the Guernsey closed-ended funds sector has experienced increases in aggregate asset value as well as significant new launches and sizeable fund-raising by established funds. There is a continued move away from remunerating managers through performance fees. Debt funds have remained popular for new fund launches in the past year as investors seek yield during this period of low interest rates. Other dominant themes have been infrastructure and real estate. The Guernsey closed-ended funds sector is valued at GB£138.4 billion as at end of September 2015.

AIFM Directive

Guernsey is a "third-country" non-EU jurisdiction under the Directive 2011/61/EU on alternative investment fund managers (AIFM Directive), which provides Guernsey based managers and funds with a number of potential advantages.

There has been a strong trend towards establishing funds with a Guernsey based AIFM (whether this is the fund itself or a separate Guernsey based manager) so that the fund and the manager are free from the requirements and costs associated with the AIFM Directive, but can make use of national private placement regimes if they wish to market the fund in specific EEA jurisdictions. As a result, Guernsey is particularly attractive for promoters based in the EU or for promoters in the US and Asia who may otherwise be discouraged by the complexities of raising capital in the EU.

A significant proportion of Guernsey funds fall outside the scope of the AIFM Directive, and it is expected that promoters will continue to use Guernsey as a base for such products, taking advantage of the non-EU status.

Regulatory framework and bodies

2. What are the key statutes, regulations and rules that govern retail funds? Which regulatory bodies regulate retail funds?

Open-ended retail funds

Regulatory framework. The types of open-ended funds are as follows:

- **Authorised funds.** Funds that are authorised by the Guernsey Financial Services Commission (GFSC) and subject to permanent and continuing supervision by the GFSC. These funds fall into three classes:
 - **Class A.** These are true retail funds that are equivalent to Undertakings for Collective Investment in Transferable Securities (UCITS) in the EU. The rules applicable to Class A funds are the Collective Investment Schemes (Class A) Rules 2002 (Class A Rules) (although these are due to be replaced by the Authorised Collective Investment Schemes (Class A) Rules 2008 at a date which has not yet been specified). These rules are prescriptive as to the form and content of the fund documents, and place limits on the investment and borrowing powers of the fund. Class A funds benefit from an investor compensation scheme under the Collective Investment Schemes (Compensation of Investors) Rules 1988. Class A funds can be registered for sale in numerous countries and promoted or distributed to the public in the UK in the same way as UK-authorised funds (subject to complying with certain notification requirements).

- **Class B.** These can be structured as retail products marketed to the public, or established as strictly private or institutional funds. The rules applicable to Class B funds are the Collective Investment Schemes (Class B) Rules 2013 (Class B Rules). These rules are less prescriptive than for Class A funds, and allow Class B funds greater latitude in their investment and borrowing powers, provided that there is full disclosure in the fund documents.
- **Class Q.** These are not retail funds as they can only be beneficially owned by qualifying professional investors (essentially, government bodies or high net worth individuals or entities). The rules applicable to Class Q funds are the Collective Investment Schemes (Qualifying Professional Investor Funds) (Class Q) Rules 1998 (Class Q Rules).
- **Registered funds.** These are funds that are registered with the GFSC and are regulated, but not authorised, by the GFSC. The rules applicable to registered open-ended funds are the Registered Collective Investment Scheme Rules 2015. The fund documents must contain the disclosures required by the Prospectus Rules 2008. These rules are not prescriptive concerning the features of the fund (for instance, in relation to investment powers) but require full disclosure of all material matters and ongoing notification of specific events. There are no restrictions on who can invest in a registered fund. They are unlikely to be used as retail funds.

Regulatory bodies. The GFSC regulates all funds in Guernsey and its powers are derived from the Protection of Investors (Bailiwick of Guernsey) Law 1987, as amended (POI Law). The GFSC issues the rules and regulations regulating funds under powers derived from the POI Law.

Closed-ended retail funds

Regulatory framework. The types of closed-ended funds are as follows:

- **Authorised closed-ended funds.** These are funds that are authorised by the GFSC and are subject to its permanent and continuing supervision. The rules which apply to authorised closed-ended funds are the Authorised Closed-ended Investment Schemes Rules 2008. These rules are not prescriptive concerning the features of the fund (for example, in relation to investment powers) but require full disclosure of all material matters and ongoing notification of specific events.
- **Registered closed-ended funds.** See above, *Open-ended retail funds: Registered funds*.

Regulatory bodies. The GFSC rules governing closed-ended funds are issued under powers derived from the POI Law.

AIFM Directive

Guernsey is a "third-country" non-EU jurisdiction under the EU Directive 2011/61/EU on alternative investment fund managers (AIFM Directive) and has established a dual regime which provides a flexible regulatory framework and allows fund managers to comply with the AIFM Directive without being required to do so when compliance is not absolutely necessary.

The first part of the dual regime ensures that Guernsey funds can be marketed in the EEA using national private placement regimes, with the GFSC acting as a local regulator that co-operates with the relevant EEA securities regulator. Such funds can also be marketed to non-EU investors without being concerned with compliance with the AIFM Directive.

The second part of the dual regime allows managers and depositaries, before the introduction of the pan-European passport, to opt in to a regime which is fully compliant with the AIFM Directive, if this is required.

The European Securities and Markets Authority (ESMA) has assessed Guernsey and concluded that no obstacles exist to the extension of a "third country" passport to Guernsey. However, at present it is uncertain when the passport regime will be introduced for third countries and so Guernsey funds with non-EU AIFMs continue to make use of national private placement regimes in the EU.

3. Do retail funds themselves have to be authorised or licensed?

Open-ended retail funds

Open-ended funds must be either authorised or registered (*see Question 2, Open-ended retail funds*), but do not require licensing. Special rules apply to foreign funds (*see below, Foreign funds*).

Authorised funds. There are two separate procedures that apply for authorisation of an authorised open-ended fund:

- **Traditional three-stage application process.** This procedure applies to Class A, Class B and Class Q funds. It involves the following stages:
 - **Preliminary (new promoter's introductory checklist).** Before starting the three-stage application process, it is necessary to identify the promoter of the fund (the person ultimately responsible for the success of the fund, usually the investment manager). If the promoter is not previously known to the Guernsey Financial Services Commission (GFSC), the promoter should review the checklist and provide the information outlined in that form. The GFSC requires a demonstrable track record in the establishment and/or management of investment funds. The GFSC will then indicate whether or not it will consider a formal application from the promoter. New promoters should allow up to three months for this process;
 - **Stage one (outline authorisation).** A Form GFA is submitted setting out the basic details of the proposed fund; the fund's objectives; the parties involved; the fees to be charged and any unusual features.

The designated manager (a locally based administrator) and the designated custodian must sign this form. A prospectus is not required at this stage. If the parties meet the GFSC's selection criteria and the proposals are acceptable, the GFSC then issues an outline authorisation. Applicants should allow between six to eight weeks from the submission of the stage one application to the formal authorisation (assuming that no issues arise);
 - **Stage two (interim authorisation).** The following are submitted a nearly final draft of the fund's prospectus (or equivalent document); the investor's application form and the appropriate form for the proposed class of the fund (forms APA, APB and APQ respectively);

These forms act as a checklist and ensure that the required disclosures are included in the fund documents. Derogations can be sought in respect of the Class B and Class Q rules, but no derogations are allowed from the Class A rules. The GFSC aims to issue the interim authorisation within ten working days of the receipt of the application;

- Stage three (formal authorisation). This is granted when all issues have been resolved and all conditions have been satisfied, including the GFSC receiving a certified copy of the prospectus and certified copies of all final constitutive documents and key agreements (for example, articles of incorporation, management agreement, custodian agreement, and so on).
- **Fast track application (Qualifying Investor Funds) (QIFs).** A fast track application process is also available, under which the proposed designated manager of the fund carries out the assessment that the GFSC otherwise carries out at stage three of the traditional process (see above). The designated manager submits the QIF application (Form QIF) once all:
 - due diligence on both the parties and the fund structure is complete; and
 - fund documents are in final (or near final) form.

Form QIF includes warranties from the designated manager to the GFSC concerning the suitability of the fund and the parties involved. The GFSC then undertakes to issue the formal authorisation of the fund within three working days of the receipt of a complete application.

The disadvantage to this fast track process is that investment in the fund must be restricted to qualified investors, which are defined as professional investors, experienced investors or knowledgeable employees.

Registered funds. The process for applying for the registration of a registered open-ended fund is the same as for the QIF application (see above), except that the applicable form is Form REG. The time period of three working days also applies. The type of investor who can invest in the fund is not restricted.

Foreign funds. Certain categories of funds that are authorised in the UK, Jersey, Isle of Man or Republic of Ireland can be promoted in Guernsey on completion of a Form EX and the payment of a fee, but without being authorised or registered in Guernsey (*The Investor Protection (Designated Countries and Territories) Regulations 1989* and *The Investor Protection (Designated Countries and Territories) (Republic of Ireland) Regulations 1992*).

In addition, an EU AIFs (within the meaning of the AIFM Directive) may be promoted in Guernsey on completion of a Form EX and the payment of a fee, but without being authorised or registered in Guernsey (*The Investor Protection (Designated Countries and Territories) (Amendment) (AIFMD) Regulations 2015*).

A Guernsey licensee providing management, administration or custody services to open-ended foreign funds must comply with the Licensees (Conduct of Business and Notification) (Non-Guernsey Schemes) Rules 1994.

Under these rules, the licensee must notify, and obtain the approval of, the GFSC before providing these services. This approval will usually only be granted if the fund would broadly meet the criteria for authorisation as an authorised fund in Guernsey (if this authorisation was necessary).

Closed-ended retail funds

Closed-ended funds must be either authorised or registered (see Question 2, *Closed-ended retail funds*) but do not need to be licensed.

Authorised funds. There are two separate processes for applying for authorisation of an authorised closed-ended fund:

- **Traditional three-stage application process.** This process is the same as for authorised open-ended funds (see above, *Open-ended retail funds*), except as follows:
 - **Stage one (outline authorisation).** As there is no requirement for closed-ended funds to appoint a custodian or trustee, there is no requirement for the custodian or trustee to sign the Form GFA;
 - **Stage two (interim authorisation).** The A, B and Q Classes do not apply to closed-ended funds, and so there is only one type of application form (Form APC). Derogations from the Authorised Closed-ended Investment Schemes Rules 2008 can be sought if either compliance with a particular rule is not appropriate in the circumstances or compliance would require a fund to alter its proposed operations or practices.
- The GFSC must be satisfied that investors will not be adversely affected before granting derogations. **Fast track application (QIFs).** The fast track application process is available for authorised closed-ended funds and is the same as for authorised open-ended funds (see above, *Open-ended retail funds*).

Registered funds. The process for applying for the registration of a registered closed-ended fund is the same as for a registered open-ended fund (see above, *Open-ended retail funds*).

Foreign funds. Closed-ended funds that are constituted outside Guernsey must be authorised or registered in Guernsey if the functions of administration and custody of the fund are carried out within Guernsey. This does not apply if only the administration of the fund is carried out in Guernsey.

Marketing

4. Who can market retail funds?

Open-ended retail funds

Any person marketing a fund, receiving subscriptions or registering investors in (or from within) Guernsey must be licensed by the Guernsey Financial Services Commission (GFSC) (*POI Law*). An exemption applies to nationals of the UK, Jersey, Isle of Man or the Republic of Ireland who would be permitted to market the relevant fund in their home country. In addition, investment products, including foreign funds, can be marketed in Guernsey without a licence provided that the promotion is only directed at persons or entities who are licensed by the GFSC.

Closed-ended retail funds

See above, *Open-ended retail funds*.

Foreign funds

See above, *Open-ended retail funds*.

In addition, certain categories of funds that are authorised in the UK, Jersey, Isle of Man or Republic of Ireland or which are EU AIFs within the meaning of the AIFM Directive can be promoted in Guernsey without being authorised or registered in Guernsey, and without the promoter being licensed in Guernsey, on both completion of a Form EX and payment of a fee (*The Investor Protection (Designated Countries and Territories) Regulations 1989*, *The Investor Protection (Designated Countries and Territories) (Republic of Ireland) Regulations 1992* and *The Investor Protection (Designated Countries and Territories) (Amendment) (AIFMD) Regulations 2015*).

5. To whom can retail funds be marketed?

Open-ended retail funds

The following restrictions apply:

- **Class A funds.** There are no restrictions.
- **Class B funds.** There are no restrictions.
- **Class Q funds.** These non-retail funds can only be marketed to qualifying professional investors (*see Question 2, Open-ended retail funds*).
- **Funds authorised using the fast-track QIF application process.** These funds can only be marketed to qualified investors (*see Question 3, Open-ended retail funds*).
- **Registered open-ended funds.** There are no restrictions on the type of investor. These funds can be offered to regulated entities in Guernsey, or to the public in Guernsey by entities licensed by the Guernsey Financial Services Commission (GFSC).

Closed-ended retail funds

The following restrictions apply:

- Authorised closed-ended funds: there are no restrictions.
- Funds authorised using the fast-track QIF application process: qualified investors only.
- Registered closed-ended funds: there are no restrictions on the type of investor, but these funds cannot be marketed directly to the public in Guernsey. These funds can be offered to regulated entities in Guernsey, or to the public in Guernsey by entities licensed by the GFSC.

Foreign funds

Certain funds authorised in the UK, Jersey, Isle of Man or Republic of Ireland can be promoted in Guernsey without being authorised or registered in Guernsey (*see Question 4, Foreign funds*). Guernsey regulations do not restrict the persons to whom such funds can be marketed.

Managers and operators

6. What are the key requirements that apply to managers or operators of retail funds?

Open-ended retail funds

There are two key roles in a Guernsey fund:

- **Promoter.** The term promoter is not specifically defined but is generally considered as the party ultimately responsible for the fund's success. It is usually, but not always, the investment manager. The identity, standing and track record of the fund's promoter are of vital importance to the Guernsey Financial Services Commission (GFSC) when determining whether (or not) to authorise a fund. The GFSC's selection policy requires applicants to be able to demonstrate a favourable track record in an established jurisdiction, involving a business which is:
 - equivalent to the new proposal; and
 - financially successful.

The following are also taken into consideration:

- whether the promoter is authorised or licensed by another regulatory body is a positive indicator (although the GFSC will make its own assessment);
- the promoter's ownership, financial resources and reputation;
- the experience of the principals behind the promoter.

In the case of QIFs and registered funds, the proposed designated manager of the fund carries out the assessment. However, it involves the same considerations and the same criteria as if the GFSC was conducting the review.

- **Designated manager/designated administrator.** All funds authorised or registered in Guernsey must appoint a local designated manager (also referred to as the designated administrator) which must be licensed by the GFSC. Guernsey has a well-developed fund administration industry, and a local firm usually carries out the functions of the designated manager. However, these functions can be outsourced to a third party (whether local or foreign). In those cases, the local designated manager remains primarily responsible to the GFSC, and must comply with the GFSC's guidance on outsourcing when considering and monitoring those appointments. Designated managers must comply with:
 - The Licensees (Conduct of Business) Rules 2014 (COB Rules);
 - The Licensees (Capital Adequacy) Rules 2010 (CA Rules).

The COB Rules include provisions dealing with the following:

- compliance arrangements, including monitoring and employee training;
- record keeping;
- categorising clients;
- suitability of transactions for clients and disclosure of information to clients;
- timely execution and best execution;
- dealing with client assets;
- the timing and content of contract notes relating to transactions;
- conflicts of interest;
- events to be notified to the GFSC.

The CA Rules specify the level of financial resources, liquidity and insurance that a licensee must maintain, as determined by reference to their business type, historical turnover and risk profile.

It is common for a foreign manager to perform the investment management role, and a local designated manager to perform the administration role.

Foreign funds. A Guernsey licensee providing management, administration or custody services to open-ended foreign funds must comply with the Licensees (Conduct of Business and Notification) (Non-Guernsey Schemes) Rules 1994 (*see Question 3, Open-ended retail funds*).

Closed-ended retail funds

See above, *Open-ended retail funds*.

Assets portfolio

7. Who holds the portfolio of assets? What regulations are in place for its protection?

Open-ended retail funds

All open-ended funds authorised or registered in Guernsey must appoint a local designated custodian or trustee, who must be licensed by the Guernsey Financial Services Commission (GFSC). Irrespective of the type of fund, the custodian or trustee must be:

- Independent of the designated manager and investment manager.
- Where the fund is a company, independent of the company and its directors.

Designated custodians/trustees must comply with the Licensees (Conduct of Business) Rules 2014 and the Licensees (Capital Adequacy) Rules 2010.

Closed-ended retail funds

Closed-ended funds are not required to appoint a designated custodian or trustee. However, the GFSC must be satisfied that the assets of the fund are adequately safeguarded. This can involve the appointment of a local custodian or trustee (or a foreign custodian or trustee), or it can involve some other form of safeguarding arrangement. The designated manager can provide safekeeping facilities.

Legal fund vehicles

8. What are the main legal vehicles used to set up a retail fund and what are the key advantages and disadvantages of using these structures?

Open-ended retail funds

Legal vehicles. The vehicles most often used for open-ended retail funds are corporate vehicles or unit trusts. Limited partnerships and limited liability partnerships (LLPs) are unlikely to be used for retail funds (see Question 25, *Legal vehicles: Limited partnership and Limited liability partnership (LLP)*).

Corporate vehicles. Guernsey company law allows for a number of different forms of company (*The Companies (Guernsey) Law 2008, as amended*). The following types can be used for retail funds:

- **Non-cellular company.** This is a traditional company with limited liability and issuing shares of one or more classes.
- **Protected cell company (PCC).** The PCC takes the form of one company that can form any number of cells, with the assets and liabilities of each cell segregated from the other cells. Shares issued by the PCC are attributed to a cell, so that a shareholder's rights relate only to that cell.
- **Incorporated cell company (ICC).** The same rules apply as for a PCC (see above), except each cell has its own legal personality.

The non-cellular company structure is most frequently used for open-ended retail funds; PCCs and ICCs are more commonly used for hedge funds (see Question 25, *Legal vehicles: Corporate vehicle*).

Unit trust. A unit trust is not a legal person in its own right. It is a trust arrangement, under which a trustee holds the assets on trust for the benefit of unitholders, according to the terms of a trust instrument. Investors hold units in the trust, with each unit representing an undivided fractional interest in the trust property. The Trusts (Guernsey) Law 2007 regulates unit trusts.

Compared to companies, unit trusts have greater flexibility in regulating their own affairs as they see fit, within the confines of the applicable fund rules. Unit trusts are familiar to UK investors in the authorised retail funds market. However, most investors are typically more familiar with corporate entities, and there is a greater body of established learning and practice in relation to the operation and management of companies.

Guernsey company law permits the use of open-ended companies in all circumstances and this therefore removes one of the original advantages of using unit trusts.

Advantages. Unit trusts offer greater flexibility as regards internal governance.

Disadvantages. Investors (particularly non-UK investors) may be more comfortable with corporate structures than they would be with unit trusts.

Closed-ended retail funds

Legal vehicles. The vehicles always used for closed-ended retail funds are corporate vehicles (see above, *Open-ended retail funds: Corporate vehicles*). Private equity funds are typically structured as closed-ended limited partnerships but such vehicles are not appropriate for retail funds.

Advantages. Only corporate vehicles are used, and so the advantages are not relevant.

Disadvantages. Only corporate vehicles are used, and so the disadvantages are not relevant.

Investment and borrowing restrictions

9. What are the investment and borrowing restrictions on retail funds?

Open-ended retail funds

Guernsey law only sets out restrictions on investment and borrowing powers for Class A authorised open-ended funds. The Class A Rules contain restrictions that apply to all Class A funds, such as:

- Requirements designed to ensure efficient portfolio management.
- Rules regulating the use of stocklending.
- Restrictions on the circumstances in which the fund can hold cash.
- A requirement that borrowing is on a temporary basis and does not exceed 10% of the value of the fund's property.

In addition, the Class A Rules include specific restrictions which apply to each of the following categories of Class A fund:

- Securities funds.
- Money market funds.
- Futures and options funds.
- Geared futures and options funds.
- Property funds.
- Warrant funds.
- Feeder funds.
- Funds of funds.
- Umbrella funds.

The investment restrictions vary, depending on the type of fund and the nature of the investment. All other forms of open-ended retail fund must disclose the investment and borrowing limits that apply, but no specific restrictions are prescribed.

Closed-ended retail funds

All forms of closed-ended fund must disclose the investment and borrowing limits that apply, but no specific restrictions are prescribed.

10. Can the manager or operator place any restrictions on the issue and redemption of interests in retail funds?

Open-ended retail funds

For Class A funds, the issue or redemption of interests can only be suspended by the manager if the custodian or trustee considers that "due to exceptional circumstances there is good and sufficient reason to do so, having regard to the interests of holders" (*Rule 13.01, Class A Rules*). The fund documents can specify a minimum number, or value, of interests that can be redeemed, and can specify a minimum holding. If a redemption request does not comply with those minimums, the request can be refused.

For all other types of fund, managers are free to impose restrictions on the issue and redemption of interests, but the circumstances in which these arise must be clearly disclosed in the fund documents. New restrictions for redemptions cannot generally be imposed (and existing restrictions cannot be increased) without giving existing holders an opportunity to exit on the old terms.

Closed-ended retail funds

The manager or operator can impose restrictions on the issue of shares. Holders of interests in closed-ended retail funds have no right of redemption in any event.

11. Are there any restrictions on the rights of participants in retail funds to transfer or assign their interests to third parties?

Open-ended retail funds

Restrictions on the transfer of interests would normally be imposed for both open-ended and closed-ended funds to ensure that interests are not transferred to any investor whose circumstances would cause the fund to breach any securities laws or to suffer any adverse tax consequences, or if the transfer would result in any investor holding less than the specified minimum holding for the fund.

Units or shares in Class A funds and Class B funds must be freely transferrable. For all other types of fund, restrictions can be imposed. Interests in Class Q funds and QIFs cannot be transferred to persons who are not eligible to invest in such funds (see *Question 5, Open-ended retail funds*). The manager, the fund and its directors must take all reasonable steps to ensure that interests in Class Q funds are not owned by ineligible investors. The designated manager of a QIF must be satisfied that effective procedures are in place to ensure that interests in the QIF are not owned by ineligible investors.

Closed-ended retail funds

Restrictions can be imposed. Interests in QIFs cannot be transferred to persons who are not eligible to invest in a QIF. The designated manager of a QIF must be satisfied that effective procedures are in place to ensure that interests in the QIF are not owned by ineligible investors.

Reporting requirements

12. What are the general periodic reporting requirements for retail funds?

Open-ended retail funds

Investors. The managers of open-ended funds must prepare the following periodic reports:

- **Class A fund: annual and half-yearly reports.** The annual reports must contain audited accounts and a report by the custodian or trustee. The annual reports must be published within four months of the year end, and half-yearly reports must be published within two months of the end of the half-year period.
- **Class B fund: annual reports.** The reports must contain audited accounts and a report by the custodian or trustee. The annual reports must be published within six months of the year end, and if interim reports are prepared, they must be on a basis consistent with the annual reports.
- **Registered open-ended fund: no periodic reporting requirements.** However, the annual report that must be given to the Guernsey Financial Services Commission (GFSC) is usually also given to investors. Every Guernsey company is legally required to lay its accounts before its shareholders at its annual general meeting.

Regulators. The reporting requirements depend on the type of fund:

- **Class A fund.** The manager must provide to the GFSC:
 - reports issued to investors;
 - either an annual notification of any changes to the information contained in the application form, or a confirmation that there are no changes.
- **Class B fund.** The manager must provide to the GFSC:
 - reports issued to investors;
 - either an annual notification of any changes to the information contained in the application form, or a confirmation that there are no changes.
- **Registered open-ended fund.** The manager must provide to the GFSC:
 - either an annual notification of any changes to the information contained in the application form, or a confirmation that there are no changes;

- audited annual report and accounts within six months of the year end;
- a quarterly statistical return;
- annual notification of any material amendments to the fund's principal documents or agreements.

Closed-ended retail funds

Investors. The same rules apply as for registered open-ended funds (see above, *Open-ended retail funds: Investors*).

Regulators. The same rules apply as for registered open-ended funds (see above, *Open-ended retail funds: Regulators*).

Tax treatment

13. What is the tax treatment for retail funds?

Open-ended retail funds

Funds. Funds are eligible for tax exempt status (for Guernsey tax purposes), on payment of an annual fee of GB£1200. Funds with exempt status are not regarded as being tax resident in Guernsey.

Resident investors. The fund must provide the Guernsey director of income tax with details of distributions made to investors resident in Guernsey, or who carry out business in Guernsey through a permanent establishment. In all other respects, the tax treatment is the same as for non-resident investors (see below).

Non-resident investors. The fund does not deduct income tax from any dividends, distributions or interest payable by the fund to investors. There are no death duties, capital inheritance, capital gains, gifts, sales or turnover taxes levied in Guernsey in connection with the acquisition, holding or disposal of interests in funds. No Guernsey stamp duty or stamp duty reserve tax is payable on the issue, transfer, conversion or redemption of interests in funds.

Closed-ended retail funds

- **Funds.** See above, *Open-ended retail funds*.
- **Resident investors.** See above, *Open-ended retail funds*.
- **Non-resident investors.** See above, *Open-ended retail funds*.

Quasi-retail funds

14. Is there a market for quasi-retail funds in your jurisdiction?

The majority of funds established in Guernsey are designed to be promoted to institutional or professional investors, rather than retail investors. However, Guernsey has a significant number of listed funds, whose shares can be acquired by the public on the secondary market.

Reform

15. What proposals (if any) are there for the reform of retail fund regulation?

The Guernsey Financial Services Commission (GFSC) has conducted a consultation on a major revision of the regulatory laws, including the Protection of Investors (Bailiwick of Guernsey) Law 1987, as amended (POI Law). It is anticipated that the change will result in a rationalisation and consolidation of laws, rather than result in substantial changes in the nature of regulation applicable to funds.

The Class Q Rules are due to be revised (following the recent revision of the Class B Rules), although wholesale changes are not expected.

The Limited Partnerships (Guernsey) Law 1995, as amended, is due to be revised and updated to enable further flexibility in the use of limited partnerships.

HEDGE FUNDS

16. What is the structure of the hedge funds market? What have been the main trends over the last year?

Guernsey is a long established jurisdiction for the establishment of hedge funds and funds of hedge funds, and such funds form a significant part of the island's fund industry. Established promoters of hedge funds in Guernsey include Dexion, BBBSA, Man, FRM, Fauchier and Credit Suisse. The net asset value of hedge funds and funds of hedge funds currently stands at approximately GB£27 billion.

Alternative investments are at the core of Guernsey's funds industry, in particular private equity and funds of hedge funds. Private equity funds account for more than half of the closed-ended funds in Guernsey, by number and value, with a current net asset value of over GB£85 billion.

Regulatory framework and bodies

17. What are the key statutes and regulations that govern hedge funds in your jurisdiction? Which regulatory bodies regulate hedge funds?

Regulatory framework

The position is virtually the same as that for open-ended retail funds (see Question 2, *Open-ended retail funds*). Class A funds are not suitable for use as hedge funds, but the other types of fund are all suitable.

The Guernsey Financial Services Commission (GFSC) can also grant certain derogations to different types of hedge funds (which are not available to other types of fund), as follows:

- Institutional or expert investor hedge funds can be permitted to appoint a foreign prime broker rather than a local custodian or trustee.
- Retail or less sophisticated investor hedge funds can be permitted to appoint a foreign prime broker to take control of the fund's property, but will normally be expected to appoint a local custodian or trustee to oversee the prime broker.
- Hedge funds can be permitted to accept subscription monies or effect redemptions on the basis of estimated valuations.
- Hedge funds can be permitted to apply client money in certain circumstances, in which other funds would be required to segregate such money in a client account.

Regulatory bodies

See above, *Regulatory framework*.

ONLINE RESOURCES

Guernsey Financial Services Commission (GFSC)W www.gfsc.gg

Description. The official website of the GFSC. This website contains relevant legislation, rules, guidance and application forms. The website also provides access to the public register of regulated entities.

Royal Court of GuernseyW www.guernseylegalresources.gg

Description. An official website maintained by the Royal Court of Guernsey and containing copies of legislation, both in its official original form and in unofficial consolidated form.

18. How are hedge funds regulated (if at all) to ensure compliance with general international standards of good practice?**Risk**

The applicable fund rules require clear disclosure of all material risks to the fund and investors, in order to enable the investor to make an informed judgment as to whether or not to invest.

Valuation and pricing

The applicable fund rules do not prescribe a method of valuation or pricing. However, fund documentation must disclose the methods and bases to be used.

Systems and controls

All Guernsey funds must be administered by a local licensee, which must comply with the COB. These rules also apply to custodians and trustees in relation to the provision of custody services.

Insider dealing and market abuse

Insider trading is prohibited (*The Companies Securities (Insider Dealing) (Bailiwick of Guernsey) Law 1996*). The POI Law prohibits market abuse.

Transparency

There are no transparency requirements requiring reporting to investors or the disclosure of significant holdings, aside from periodic reporting requirements (see Question 12, *Open-ended retail funds*).

Money laundering

Funds and their Guernsey service providers must comply with the various laws and regulations concerning the prevention of both money laundering and terrorist financing. The local designated manager of the fund must ensure compliance with these laws. The Guernsey Financial Services Commission (GFSC) endorses the international standards of the Financial Action Task Force (FATF) in relation to combating money laundering and the financing of terrorism.

Short selling

There are no applicable regulations.

Marketing**19. Who can market hedge funds?**

See Question 4, *Open-ended retail funds*.

20. To whom can hedge funds be marketed?

See Question 5, *Open-ended retail funds*.

Investment restrictions**21. Are there any restrictions on local investors investing in a hedge fund?**

There are no restrictions on local investors investing in a hedge fund.

Assets portfolio**22. Who holds the portfolio of assets? What regulations are in place for its protection?**

See Question 7, *Open-ended retail funds*.

Requirements**23. What are the key disclosure or filing requirements (if any) that must be completed by the hedge fund?**

The fund must file copies of the following with the GFSC:

- All constitutional and offering documents.
- The principal agreements relating to the fund, for example, the:
 - administration agreement;
 - custodian agreement; and
 - investment management agreement.

Side letters which are personal to a particular investor do not need to be filed.

24. What are the key requirements that apply to managers or operators of hedge funds?

See Question 6, *Open-ended retail funds*.

Legal fund vehicles and structures**25. What are the main legal vehicles used to set up a hedge fund and what are the key advantages and disadvantages of using these structures?****Legal vehicles**

The vehicles most often used for hedge funds are corporate vehicles, although it is also possible to use limited partnerships:

- **Corporate vehicle.** Guernsey company law allows for a number of different forms of company (*The Companies (Guernsey) Law, 2008, as amended*). PCCs and ICCs are commonly used for hedge funds (see *Question 8, Open-ended retail funds*) and are particularly useful for managers wishing to establish a number of sub-funds that share many similar features. In this way, the cells can each have different investment objectives, invest in different asset classes, or be hedged against different currencies. The statutory basis for the segregation between cells provides comfort to investors that each cell is properly ring-fenced.
- **Limited partnership.** Funds established as Guernsey limited partnerships have the following features:
 - a specific general partner company is usually incorporated. It manages the affairs of the limited partnership and has unlimited liability in respect of those affairs. It must be licensed or receive an exemption from licence if incorporated or operating in Guernsey;
 - each of the investors is a limited partner, holding a partnership interest, with no liability beyond its investment commitment, provided that it does not do anything that would constitute conduct or management of the partnership's business. The law provides that certain investor actions do not constitute management (*The Limited Partnerships (Guernsey) Law, 1995, as amended*), including acting as a director or shareholders of a corporate general partner; being an employee of the limited partnership or of a general partner and consulting with and advising the general partner;
 - a partnership is typically treated as tax transparent in many jurisdictions (that is, tax is levied at the level of the individual investor rather than the partnership itself);
 - there are no restrictions on returning capital to limited partners, provided that the limited partnership is solvent. If the partnership becomes insolvent within six months of the payment, the return of capital can be clawed back within one year of the payment;
 - the limited partnership agreement remains a private document (but must be provided to the Guernsey Financial Services Commission (GFSC));
 - limited partnerships can elect to have a separate legal personality and to be a body corporate. However, this does not affect its transparency for tax purposes.
- **Limited liability partnership (LLP).** LLPs were introduced in Guernsey in 2014. LLPs are rarely used as fund vehicles but may be used as part of the wider structure for funds that are established as limited partnerships. LLPs have the following features:
 - an LLP is an incorporated legal entity;
 - members have limited liability for the liabilities of the LLP;
 - an LLP is typically treated as tax transparent in many jurisdictions (that is, tax is levied at the level of the individual investor rather than the LLP itself).

The most important difference between the corporate and partnership structures (whether limited partnerships or LLPs) is the partnership's tax transparency. Whether this is an advantage or a disadvantage depends on the position of the prospective investors. With corporate funds it is usual for investors to subscribe for the full amount of their commitment at the outset, whereas with a limited partnership structure the investors' commitments are often drawn down in stages as and when required.

Advantages. The advantages of each legal vehicle in relation to each proposed structure will depend on what the parties wish to achieve when establishing the fund. For example, a corporate vehicle has greater certainty as to its rules of governance as many rights of shareholders are enshrined in law or are considered to be standard practice. Limited partnerships are more flexible in terms of their governance and the rights of partners depend, to a greater extent, on the terms of the individual agreements. This may be an advantage or disadvantage depending on the view of the promoter and the investors.

Disadvantages. The disadvantages of each legal vehicle in relation to each proposed structure will depend on what the parties wish to achieve when establishing the fund.

Tax treatment

26. What is the tax treatment for hedge funds?

Funds

See *Question 13, Open-ended retail funds*.

Resident investors

See *Question 13, Open-ended retail funds*.

Non-resident investors

See *Question 13, Open-ended retail funds*.

Restrictions

27. Can participants redeem their interest? Are there any restrictions on the right of participants to transfer their interests to third parties?

Redemption of interest

Participants of open-ended hedge funds can redeem their interests under the terms specified by that fund. Interests in closed-ended funds are not redeemable at the option of the participant.

Transfer to third parties

It is common to include restrictions to prevent persons acquiring interests if that acquisition would bring the fund within the scope of US Employee Retirement Income Security Act 1974 (*Pub. L. 93-406, 88 Stat. 829*) (ERISA) legislation. This is generally undesirable as the ERISA legislation can impose strict fiduciary standards on the management of the fund assets.

The rules concerning restrictions on participants' rights to transfer their interests are the same as for retail funds (see *Question 11, Open-ended retail funds*).

Reform

28. What (if any) proposals are there for the reform of hedge fund regulation?

See *Question 15*.

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Areas of practice. Corporate; commercial; investment funds.

Recent transactions

- Advised Alchemy Partners on the launch of Alchemy Special Opportunities Fund III.
- Advised Ashmore on the launch of an Emerging Market Distressed Debt Fund and a Russian Debt Fund.
- Advised Permira on the launch of Permira V and Permira Credit Solutions II.
- Advised Roundshield on the launch of Roundshield Fund I.



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Professional qualifications. England and Wales, Solicitor, 1998; admitted as an advocate of the Royal Court of Guernsey, 2010

Areas of practice. M&A; investment funds; public equity transactions.

Recent transactions

- Advising Apax Global Alpha on its establishment (including its acquisition of an existing private investment structure), IPO and listing on the Main Market of the LSE.
- Advising Fair Oaks Income Fund on its establishment (including an underlying limited partnership master fund), IPO and listing on the Specialist Fund Market of the LSE.
- Advising Better Capital PCC, a closed-ended private equity fund listed on the LSE, in relation to its conversion to a PCC, the launch of its second fund and subsequent transactions.
- Advising The Glanmore Property Fund on an ongoing basis in relation to all regulatory matters, a reorganisation and a scheme of arrangement.

Investment funds in Jersey: regulatory overview

Robert Milner, James Mulholland and Daniel O'Connor
Carey Olsen

global.practicallaw.com/5-501-4947

RETAIL FUNDS

1. What is the structure of the retail funds market? What have been the main trends over the last year?

Open-ended retail funds

Jersey is a leading global centre for the establishment of funds covering many investment disciplines and themes.

Jersey offers a range of open-ended funds:

- **Public funds.** All funds that can be offered to more than 50 people and which are not recognised funds (*see below, Recognised funds*) are considered public funds. There is no limit to the number of investors. Open-ended public funds can be established as:
 - **open-ended collective investment funds (OCIFs).** These can be offered to the general public;
 - **expert funds.** These are semi-retail or non-retail funds available to ten categories of "expert investor" (for example, those investing at least US\$100,000) with no investment restrictions;
 - **regulated Jersey eligible investor funds (JEIFs).** JEIFs must be alternative investment funds for the purposes of the Directive 2011/61/EU on alternative investment fund managers (AIFM Directive) and are available to 11 categories of "eligible investors";
 - **eligible investor funds.** These are funds with no regulatory supervision and no investment or borrowing restrictions, which are available to 11 categories of "eligible investors". These are not retail funds and can be used for hedge funds.
- **Private funds (PFs).** The Commission has recently established a new private funds regime so that PFs can benefit from a light touch fast-track regulatory process under the new private funds guide (PFG). Up to 50 offers can be made to investors who qualify as professional investors or subscribe for interests with a value of more than J£250,000. The fund (and frequently its service providers) is entirely unregulated, other than the need to obtain consent under the Control of Borrowing (Jersey) Order 1958 (COBO) upon the establishment of the fund vehicle.
- **Recognised funds.** These are very public funds that must meet highly prescribed standards in relation to most aspects of the fund's structure, operation and prospectus content. These funds can:
 - seek authorisation under the UK's Financial Services and Markets Act 2000 to market directly to the general public in the UK;

- be marketed freely in certain other jurisdictions once they have registered with the relevant authority.

Jersey has a large number of open-ended funds that are retail or semi-retail in nature and these represent a significant part of Jersey's funds under management and funds under administration.

Closed-ended retail funds

For Jersey regulatory purposes, a closed-ended fund is a fund that is not open for redemptions at the option of holders of securities. Some of the same regulatory categories apply to open-ended and closed-ended funds, and the regulatory landscape of each is therefore sometimes similar. Funds that fall within the listed fund category must be closed-ended.

Jersey offers the following closed-ended funds:

- **Public funds.** In the retail closed-ended fund context these include:
 - closed-ended collective investment funds (CCIFs). These can be offered to the general public;
 - listed funds. These are funds with a listing on a recognised exchange (such as LSE/AIM and The International Stock Exchange (TISE) (formerly known as the CISE) with no investment or borrowing restrictions; no minimum subscription; no restrictions on the type of investor and a three-day approval process;
 - expert funds. *See above, Open-ended retail funds;*
 - JEIFs. *See above, Open-ended retail funds;*
 - unregulated eligible investor funds. *See above, Open-ended retail funds.*
- **Private funds (PFs).** *See above, Open-ended retail funds.*

For many years Jersey has collected a wide range of statistics in relation to the finance industry. The pattern is of steady, sustainable growth. Statistics are available from Jersey Finance Limited (www.jerseyfinance.je), with the latest figures (as of the end of September 2016) showing:

- Bank deposits of J£111.5 billion.
- Net asset value of funds under administration increased by J£14.1 billion to J£237.3 billion during Q3 2016.
- 1,125 regulated funds with a total number of 1,863 separate investment pools and 120 active unregulated funds.
- J£19.7 billion total funds under investment management.

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In terms of new funds, the main focus of activity has been the following European and global sectors:

- Private equity.
- Real estate.
- Distressed debt.
- Infrastructure.

There has also been a returning trend of listed funds (on TISE or LSE's main board, SFM or AIM). Unregulated funds have also remained a popular structure due to the flexibility of that regime. Given the global economic climate, fund and manager restructuring activity levels have remained consistently high.

An increasingly common trend is the migration of manager teams to Jersey. An increasing number of fund managers have relocated to or established a presence in Jersey and the tax and regulatory authorities have been sympathetic to these new businesses.

As EU member states implement the AIFM Directive, as a "third country" non-EU jurisdiction, Jersey has been working hard to ensure it can continue to offer professionals a blend of stability and flexibility.

Jersey's strategy in relation to the AIFM Directive is to have the right frameworks in place to continue to provide fund establishment, management and administration services on a "business as usual" basis. This has been achieved by placing an AIFM Directive "overlay" on existing regulatory frameworks such that a Jersey fund need only comply with the AIFM Directive to the extent it is absolutely necessary.

Jersey is committed to:

- Continuing to facilitate funds business within the EU through national private placement regimes until at least 2018.
- Introducing the option of a fully AIFM Directive-compliant regime and obtaining an EU-wide passport as soon as practicable.

As a non-EU jurisdiction, Jersey can offer investors the choice of maintaining a separate regime that lies outside the scope of the AIFM Directive, for managers who do not wish to access EU capital or operate in the EU.

Combined, this range of options means that Jersey continues to operate its existing fund regime whilst at the same time offering an option that is fully compliant with the AIFM Directive, providing managers with the flexibility to market to investors both inside and outside the EU.

Jersey already regulates and authorises alternative fund managers in accordance with the International Organization of Securities Commissions (IOSCO) standards, and tax information exchange agreements (TIEAs) are (or will be) in place with each member state where alternative funds are to be marketed, including TIEAs or double taxation agreements (DTAs) with 13 EU member states.

In addition, Jersey is able to comply with all required international reporting and transparency requirements, and is more compliant with Financial Action Task Force (FATF) recommendations than many onshore asset management jurisdictions. Jersey is therefore confident that it will be able to satisfy the criteria needed to comply with the AIFM Directive.

Regulatory framework and bodies

2. What are the key statutes, regulations and rules that govern retail funds? Which regulatory bodies regulate retail funds?

Open-ended retail funds

Regulatory framework. The following legislation applies:

- The Collective Investment Funds (Jersey) Law 1988, as amended (CIF Law), which regulates public funds and recognised funds.
- The Control of Borrowing (Jersey) Order 1958 (COBO), which regulates private funds (PFs) and controls, among others, the creation and issue of:
 - shares;
 - securities;
 - units in a unit trust scheme; and
 - limited partnership interests.
- The Collective Investment Funds (Certified Funds - Prospectuses) (Jersey) Order 2012 (CFPO), which regulates the contents of prospectuses for certified funds.
- The Financial Services (Jersey) Law 1998 (FSJ Law), which regulates fund service providers operating or incorporated in Jersey.
- Alternative Investment Funds (Jersey) Regulations 2012, which overlays the AIFM Directive requirements where applicable.

The following legislation applies to recognised funds:

- The Collective Investment Funds (Recognized Funds) (Rules) (Jersey) Order 2003 (RF Order).
- The Collective Investment Funds (Recognized Funds) (Permit Conditions for Functionaries) (Jersey) Order 1988 (RF Functionary Permit Order).
- The Collective Investment Funds (Recognized Funds) (Compensation for Investors) (Jersey) Regulations 1988.
- The Collective Investment Funds (Recognized Funds) (Actions for Damages) (Jersey) Regulations 2008.

The legislation that applies to unregulated eligible investor funds is the Collective Investment Funds (Unregulated Funds) (Jersey) Order 2008 (UF Order), which exempts them from regulation under the CIF Law if specified conditions are satisfied. Jersey's internationally compliant regime to assist in the detection and prevention of money-laundering and terrorism still applies to these funds (*see Question 18*).

Regulatory bodies. The Commission authorises and supervises regulated investment funds as the principal regulatory authority in Jersey. In addition to its statutory regulation of the financial services sector, the Commission also publishes guidelines and codes of practice for the different industry sectors. These guidelines and codes of practice are produced after consultation with the relevant industry sectors. Funds and their Jersey service providers must comply with the following legislation, which applies international standards:

- Proceeds of Crime (Jersey) Law 1999, as amended.
- Money Laundering (Jersey) Order 2008, as amended.

- Terrorism (Jersey) Law 2002, as amended.
- Proceeds of Crime (Supervisory Bodies) (Jersey) Law 2008.
- Drug Trafficking Offences (Jersey) Law 1988, as amended.
- Criminal Justice (International Co-operation) (Jersey) Law 2001, as amended.

They must also comply with any related legislation, and the Commission's Handbook for the prevention and detection of money laundering and the financing of terrorism.

Guidelines and codes of practice. The Commission has published the following codes and guidelines which are often as important as the primary legislation:

- Guide to open-ended unclassified collective investment funds offered to the general public (OCIF Guide). This is also applied (by analogy) to CCIFs (*see below, Closed-ended retail funds*).
- Promoters of Public and Private Collective Investment Funds (Promoter Policy).
- Licensing Policy in respect of those activities that require registration under the FSJ Law (Licensing Policy).
- Codes of Practice for Fund Services Business (FSJ Codes of Practice).
- Establishing a Collective Investment Fund Operation in Jersey.
- Securities Issues under the Control of Borrowing Legislation.
- The Codes of Practice for Certified Funds (including Expert Fund, JEIF and Listed Fund guides), which applies to funds domiciled and regulated in Jersey holding a certificate under the CIF Law (that is, Expert Funds, JEIFs, Listed Funds, OCIFs and CCIFs).
- The Codes of Practice for Alternative Investment Funds and AIF Services Business (the AIF Codes), which apply where funds and/or fund services businesses are required to comply with provisions of the AIFM Directive.
- The PFG.

The Commission also issues letters to industry participants from time to time covering fund and manager related issues as a way of highlighting to practitioners and fund professionals the Commission's approach on a particular policy area.

Closed-ended retail funds

Regulatory framework. The key statutes are the same as for open-ended funds, and the Commission is the regulator (*see above, Open-ended retail funds*).

In addition:

- Listed funds must comply with the Jersey Listed Fund Guide (LF Guide).
- The OCIF Guide is applied to CCIFs as a licensing starting point (by analogy only and with more flexibility). *See above, Open-ended retail funds.*

Regulatory bodies. *See above, Closed-ended retail funds: Regulatory framework.*

3. Do retail funds themselves have to be authorised or licensed?

Open-ended retail funds

All Jersey public funds must apply to the Commission to be issued with a fund certificate under the CIF Law, save for eligible investor funds which comply with the terms of the UF Order. Personal questionnaires for the directors of a certified public fund vehicle should be submitted electronically to the Commission as early as practicable.

Service providers to public funds must be registered under the FSJ Law and regulated by the Commission (unless an exemption applies) if carrying on business (or incorporated) in Jersey. Once a service provider is regulated, there is no requirement to obtain any further consent to act in the same capacity for other public funds (including non-Jersey funds). A tailored regime applies for the establishment of fund service providers as special purpose vehicles (SPVs) such as general partner or investment management companies. These applications are dealt with together in the fund application.

PFs are largely unregulated (although additional regulation for the fund and/or its manager is generally needed where a PF is classified as an AIF for the purposes of the AIFM Directive) and are relatively quick and easy to establish (*see Question 1, Open-ended retail funds*).

All other OCIFs, CCIFs and recognised funds must, after any informal discussions with the Commission, follow a two-stage approval procedure:

- **Initial review.** A short checklist is submitted to the Commission. The review takes up to ten working days.
- **Documentary review.** The following are submitted to the Commission:
 - an application;
 - a documentary checklist; and
 - all material fund documents.

In relation to expert funds, the Commission does not need to review the structure, documentation or the promoter. Instead the fund administrator certifies to the Commission that the fund complies with the Expert Fund (EF) Guide. The Commission aims to issue its approval within three working days of the submission of a completed application. The EF Guide is flexible. However, where any unusual derogations are sought from its terms, it is usual to seek these in advance while the documents are being prepared to avoid potential delay in the approval process.

Similarly, in relation to JEIFs, the fund administrator certifies to the Commission that the JEIF complies with the relevant guide and aims to issue its approval within three working days of the submission of a completed application (assuming that no derogations are needed).

Recognised funds are structured to ensure investor protection that is at least equivalent to that afforded to investors in the UK. Recognised funds issued with a recognised fund certificate can apply to the UK Financial Conduct Authority (FCA) to market directly to the public in the UK and can also be marketed to the public (subject to any local requirements) in a number of other territories including Australia, Belgium, Hong Kong, The Netherlands and South Africa. Functionaries of recognised funds are regulated under the CIF Law.

Closed-ended retail funds

In relation to service providers to closed-ended public funds see above, *Open-ended retail funds*.

In relation to listed funds, the Commission operates an expedited approval procedure. This is based on the expert fund model where the Commission:

- Relies on a certification by the fund administrator.
- Aims to issue its approval within three working days from the submission of a completed application.

Where any unusual derogations are sought from the terms of the LF Guide, it is usual to seek these in advance while the documents are being prepared. This avoids potential delays in the approval process.

In relation to CCIFs, the procedure set out for OCIFs applies (*see above, Open-ended retail funds*).

Marketing**4. Who can market retail funds?****Open-ended retail funds**

Jersey law does not prescribe who can market retail funds. However, a fund distributor which carries on business (or is incorporated) in Jersey must be registered with the Commission under the FSJ Law.

Closed-ended retail funds

See above, *Open-ended retail funds*.

5. To whom can retail funds be marketed?**Open-ended retail funds**

There are no applicable restrictions for marketing to non-Jersey retail investors. Investor qualification rules apply to expert funds, JEIFs, eligible investor funds and PFs (*see Question 1, Open-ended retail funds: Public funds*). A Jersey distributor may be needed to market non-domiciled funds to Jersey investors, unless a non-Jersey distributor which falls within an appropriate exemption to the FSJ Law has been appointed.

Closed-ended retail funds

See above, *Open-ended retail funds*.

Managers and operators**6. What are the key requirements that apply to managers or operators of retail funds?****Open-ended retail funds**

The identity of the promoter and other entities involved in a fund (whether based in Jersey or not) is an important factor for the Commission in deciding whether to grant regulatory approval.

The Promoter Policy is applied to promoters of OCIFs and CCIFs. It does not apply to:

- Expert funds.
- Jersey eligible investor funds (JEIFs).

- Listed funds.
- Eligible investor funds.
- PFs.

The promoter is described as the driving force behind the scheme. The criteria for approval are (*Promoter Policy*):

- The promoting group's:
 - track record and relevant experience;
 - reputation;
 - financial resources; and
 - spread of ultimate ownership.
- The type of investor to whom the fund will be offered.

The OCIF Guide requires that a manager must:

- Be engaged primarily in the business of fund management.
- Be independent of any trustee or custodian of the fund.
- Have sufficient financial resources for it to conduct its business effectively and meet its liabilities.
- Be a company incorporated and resident in Jersey (unless a Jersey administrator is appointed).
- Be registered under the FSJ Law for the conduct of fund services business and therefore comply with the FSJ Codes of Practice.

In relation to expert funds, there is no requirement for the investment manager or adviser to be incorporated or carry on business in Jersey, and the Promoter Policy does not apply. However, the investment manager or adviser should confirm in writing to the Commission whether it satisfies certain "good standing" requirements (including as to its experience and solvency) set out in the EF Guide, which the administrator, manager or trustee (as applicable) must countersign having undertaken appropriate due diligence. If an investment manager or adviser does not meet the criteria listed in the EF Guide, it can approach the Commission on a case-by-case basis. This also applies to JEIFs. The distributor of the expert fund or JEIF (if different from the investment manager/adviser) must also satisfy these requirements if it is not the investment manager/adviser or one of its associates. A distributor is either:

- The driving force behind the fund (that is, if the distributor were to withdraw from the proposal, the fund would not go ahead).
- The entity responsible (either directly or through its agents) for putting the majority of investors into the fund.

Expert funds and JEIFs must appoint an administrator or a manager with at least two Jersey resident directors with appropriate experience, together with staff and a physical presence in Jersey.

Service providers to public funds that carry on business in or are incorporated in Jersey must (unless an exemption applies) be registered under the FSJ Law and comply with the FSJ Codes of Practice, including the codes relating to:

- Managers.
- Investment managers.
- Investment advisers.
- Administrators.

The manager of a recognised fund must obtain a functionary permit under the CIF Law and comply with the provisions set out in the RF Functionary Permit Order.

Where the AIFM Directive applies to a manager, it must comply with the relevant sections of the AIF Codes of Practice.

Closed-ended retail funds

The Promoter Policy applies to CCIFs. The OCIF Guide also applies, although by analogy only, with more flexibility being permitted for closed-ended funds.

The Promoter Policy does not apply to listed funds. Listed funds must appoint an administrator or a manager which has at least two Jersey-resident directors with appropriate experience, together with staff and a physical presence in Jersey. The investment manager or adviser to a listed fund should confirm in writing to the Commission whether it satisfies certain "good standing" requirements (including as to its experience and solvency) set out in the LF Guide, which the administrator or manager (as applicable) must counter-sign having undertaken appropriate due diligence. If an investment manager or adviser does not meet the criteria listed in the LF Guide, it can approach the Commission on a case-by-case basis. The distributor of the listed fund must also satisfy these requirements if it is not the investment manager/adviser or one of its associates (*see above, Open-ended retail funds*).

At least two Jersey-resident directors must sit on the board of the entity responsible for supervising the fund. A private placement memorandum must also be produced.

The same FSJ Law or AIF Codes requirements in relation to registration apply to service providers to closed-ended public funds (*see above, Open-ended retail funds*).

Assets portfolio

7. Who holds the portfolio of assets? What regulations are in place for its protection?

Open-ended retail funds

The OCIF Guide generally requires a trustee or custodian to be appointed to hold the assets of the fund. It must be:

- A company that is a member of a major banking or insurance group of companies, or any other institution which is acceptable to the Commission.
- A company incorporated and with an established place of business in Jersey, or the Jersey branch of a non-Jersey bank.
- Independently audited and have:
 - an issued and paid-up capital and non-distributable capital reserves of at least JE£250,000; and
 - net shareholders funds of at least JE£250,000.
- Independent of the manager.

Expert funds and Jersey eligible investor funds (JEIFs) must have adequate arrangements for the safe custody of their assets (including, if applicable, prime brokerage arrangements), which must be disclosed in their offer document. The EF Guide and the JEIF Guide both require a trustee or custodian to be appointed to hold the fund's assets if it is open-ended. There are no specific requirements for PFs.

A public fund's trustee or custodian that carries on business in, or is incorporated in, Jersey must be registered under the FSJ Law and is subject to the FSJ Codes of Practice.

The manager of a recognised fund must obtain a functionary permit under the CIF Law and comply with the provisions set out in the RF Functionary Permit Order. For recognised funds, there are also requirements for the protection of assets under the recognised funds legislation (*see Question 2, Open-ended retail funds: Regulatory framework*).

In cases where the AIFM Directive applies and a Jersey depositary is required, both the "depositary lite" and the "depositary super-lite" regimes are available under the AIF Codes. There is no Jersey requirement to appoint a depositary for these purposes.

Closed-ended retail funds

Listed funds, expert funds and JEIFs must have adequate arrangements for the safe custody of their assets (including, if applicable, prime brokerage arrangements), which must be disclosed in their offer document.

In relation to CCIFs, the requirements for OCIFs apply (by analogy and with more flexibility) (*see above, Open-ended retail funds*). An independent trustee or custodian is often not required.

The FSJ Law and the AIFM Directive requirements for registration of service providers to public funds apply (*see Question 3, Open-ended retail funds*).

Legal fund vehicles

8. What are the main legal vehicles used to set up a retail fund and what are the key advantages and disadvantages of using these structures?

Open-ended retail funds

Funds in Jersey are typically established as:

- Companies (single class, multi-class, umbrella or protected cell or incorporated cell).
- Limited partnerships (including incorporated limited partnerships (ILPs) and separate limited partnerships (SLPs)).
- Unit trusts.

Hedge funds usually prefer a corporate structure, except where another vehicle is used to achieve tax transparency from the perspective of one or more onshore jurisdictions (*see Question 25*).

A fund of any legal structure can be open-ended or closed-ended.

Recognised funds must be structured as companies or unit trusts.

Companies. In recent years, the Companies (Jersey) Law 1991 has been modified to accommodate improvements for the funds industry (particularly companies with a fluctuating membership), such as:

- Introducing no par value companies (that is, companies the shares of which do not have a nominal value).
- Allowing companies to hold treasury shares.
- Simplifying the making of income and capital distributions, generally permitting them from any source, subject to the company's solvency.

ONLINE RESOURCES

Jersey Financial Services Commission

W www.jerseyfsc.org

Description. This is the website for the Jersey Financial Services Commission. It contains the relevant guidance notes and application forms.

- The use of corporate directors.
- The abolition of financial assistance restrictions.
- Permitting the merger of companies and the migration of companies to Jersey from other jurisdictions.

Investors' interests can be represented by shares (which can be traded uncertificated) or by depository receipts or certificates.

Cell companies are companies which can create cells separate from themselves, each of which can hold separate assets (and liabilities):

- **Protected cell companies (PCCs).** The PCC has a number of features, for example, a PCC cell can invest in another cell within the same PCC structure.
- **Incorporated cell companies (ICCs).** The ICC is very similar to a PCC except that individual cells have separate legal personality.

The ICC and the PCC have found favour as fund vehicles. Statute clearly provides for the segregated nature of the cellular structure, giving legal certainty. Over 400 protected cells and 250 incorporated cells have now been registered. PCCs and ICCs are particularly suited to repeat transactions, where:

- A fund manager can seek to establish a number of funds.
- The same infrastructure is used but with different investment objectives, investor profiles or fee structures.

Given their ring-fenced structure, PCCs and ICCs are particularly suitable as hedge fund vehicles.

Limited partnerships. Limited partnerships are established under the Limited Partnerships (Jersey) Law 1994 (LP Law). The liability of limited partners for the debts of the partnership cannot extend beyond their agreed capital contributions, provided their activity does not constitute management under the LP Law. The LP Law provides a safe harbour for certain activities that would otherwise constitute management and permits the limited partner a greater degree of involvement in the management of a limited partnership than some other jurisdictions.

Other advantages of a Jersey limited partnership include that:

- There is no upper limit on the number of limited partners.
- Confidentiality is preserved, as the only document to be publicly filed is a short declaration of limited partnership that does not disclose the:
 - identity of the limited partners;
 - business of the partnership; and
 - partnership contributions.

Both ILPs and SLPs (introduced in Jersey in 2011 by the Incorporated Limited Partnerships (Jersey) Law 2011 and the Separate Limited Partnerships (Jersey) Law 2011 respectively) have separate legal personalities (allowing each form of limited partnership, for example, to own assets, and sue and be sued in its own name). An ILP is also a body corporate (SLPs do not have this status). These entities provide greater flexibility for fund managers in structuring their fund's general partner and carried interest vehicle, particularly where the fund is an English limited partnership.

Unit trusts. A unit trust is not a separate legal entity but a trust arrangement under which the legal ownership of the scheme's assets is vested in a trustee who holds those assets on trust for the benefit of unitholders. A unit trust is constituted by an instrument of trust (in the case of an open-ended structure, the parties to the instrument are usually a manager and a trustee), which regulates:

- The appointment and retirement of the trustee and manager.
- Their respective duties.
- The distribution or accumulation of trust income.
- Investment powers.
- Dealing.
- Valuation.

The applicable trusts legislation in Jersey is the Trusts (Jersey) Law 1984. In addition to preserving confidentiality, and the relative flexibility of trusts, there can be significant tax advantages where a unit trust structure is used.

Closed-ended retail funds

See above, *Open-ended retail funds*.

Investment and borrowing restrictions

9. What are the investment and borrowing restrictions on retail funds?

Open-ended retail funds

In relation to expert funds, no investment or borrowing restrictions are prescribed for funds under the EF Guide. However, the fund's approach to both must be clearly disclosed in its marketing document. This also applies to Jersey eligible investor funds (JEIFs). There are no relevant restrictions for PFs.

The OCIF Guide provides guideline investment and borrowing restrictions depending on the nature of the unclassified fund. Borrowing restrictions (where they apply) are usually restricted to 10% of NAV in the case of (among others) feeder funds and funds of funds. Derogations from these restrictions (and the setting of restrictions for other types of fund) can be agreed with the Commission. The restrictions must be fully disclosed in the fund's prospectus.

Detailed investment and borrowing restrictions apply to recognised funds, depending on the nature of the fund.

Closed-ended retail funds

For the position in relation to expert funds and JEIFs, see above, *Open-ended retail funds*.

In relation to listed funds, there are no investment or borrowing restrictions for funds under the LF Guide, but the fund's approach to both must be clearly disclosed in its marketing document.

No investment or borrowing restrictions are prescribed for CCIFs. However, the Commission will, for a retail fund:

- Refer to the OCIF Guide as a benchmark.
- Require, as a condition to the certificate granted to the fund, that any change in investment or borrowing restrictions receive prior consent from the Commission.

In relation to CCIFs, the requirements for OCIFs apply (by analogy and generally with some flexibility) (*see above, Open-ended retail funds*).

10. Can the manager or operator place any restrictions on the issue and redemption of interests in retail funds?

Open-ended retail funds

There are no limits on the restrictions which can be imposed on issues or redemptions for expert funds, Jersey eligible investor funds (JEIFs) or PFs.

The OCIF Guide imposes various compulsory:

- Redemption requirements, for example, concerning:
 - non-cash redemption;
 - period until payment; and
 - compulsory redemption.
- Issue requirements (for example, regarding non-cash consideration).

Suspension of dealings can be provided for in exceptional circumstances and having regard to the interests of holders.

For a recognised fund, the manner, process and pricing of the issue and redemption of interests is prescribed by the RF Order. The manager is not permitted to alter these prescribed terms.

Closed-ended retail funds

See above, *Open-ended retail funds*.

There are no limits on these restrictions for expert funds or listed funds.

In relation to CCIFs, the requirements for OCIFs apply (by analogy and with more flexibility).

11. Are there any restrictions on the rights of participants in retail funds to transfer or assign their interests to third parties?

Open-ended retail funds

No restrictions are imposed on public funds, except that the fund documents for expert funds, Jersey eligible investor funds (JEIFs), unregulated eligible investor funds and PFs must make provision to prevent non-expert investors or non-eligible investors (as the case may be) acquiring interests in the fund. Public funds often have transfer restrictions for onshore tax and/or regulatory reasons (subject to any applicable stock exchange rules on free transferability).

Recognised funds can only restrict transfers in limited circumstances.

Closed-ended retail funds

See above, *Open-ended retail funds*.

Reporting requirements

12. What are the general periodic reporting requirements for retail funds?

Open-ended retail funds

Investors. Under the OCIF Guide:

- At least two reports must be published and distributed to holders in relation to each financial year, with the annual statements audited. Holders must be notified of any changes to the offering or constitutive documents (unless there is no prejudice to the holders' interests).
- The latest selling and redemption prices and NAV must be available to all holders.

For recognised funds, the annual and half-yearly audited financial statements and portfolio statements and reports prescribed by the RF Order must be made available to investors and sent out within:

- Four months of the relevant period's end in the case of an annual report.
- Two months of the period's end in the case of a semi-annual report.

Regulators. Copies of the same reports distributed to the holders must be filed with the Commission (*see above, Investors*). In relation to expert funds, Jersey eligible investor funds (JEIFs) and listed funds, see *Question 23*.

Where the AIFM Directive is applicable, the disclosure and transparency requirements under the AIF Codes will also apply to all funds which have not appointed a sub-threshold manager (regardless of their regulatory classification).

Closed-ended retail funds

Investors. There are no requirements, other than for companies to file annual audited financial statements under the Companies (Jersey) Law 1991. The requirements for OCIFs apply to CCIFs (by analogy only and with more flexibility).

Regulators. See above, *Open-ended retail funds: Regulators*.

The same AIF Codes considerations apply as for open-ended funds.

Tax treatment

13. What is the tax treatment for retail funds?

Open-ended retail funds

Funds. A fund, whether established as a company, unit trust or limited partnership, is not generally subject to any local Jersey tax. In particular, there is no capital gains, capital transfer, wealth or inheritance tax payable in relation to the issue or realisation of investments in a Jersey investment fund (unless the fund invests in Jersey property or buildings). In addition, no corporation tax, profits tax or stamp duty is payable. Funds structured as unit trusts and limited partnerships are fully exempt from tax; fund companies are subject to a 0% rate but can become fully exempt (*see Question 14*).

Jersey resident administrators and custodians are generally liable to Jersey income tax at the rate of 10%. However, Jersey-administered entities, such as general partners and managers that provide services to a fund, are taxed at 0%.

Resident investors. Jersey-resident investors must pay tax at up to 20% on income received from a fund. There is no capital gains tax in Jersey (*see above, Open-ended retail funds: Funds*).

Non-resident investors. Non-resident investors are generally not subject to Jersey tax.

Closed-ended retail funds

Funds. The same tax rules for open-ended retail funds apply (*see above, Open-ended retail funds*).

Resident investors. The same tax rules for open-ended retail funds apply (*see above, Open-ended retail funds*).

Non-resident investors. The same tax rules for open-ended retail funds apply (*see above, Open-ended retail funds*).

Quasi-retail funds

14. Is there a market for quasi-retail funds in your jurisdiction?

There is no specific market for quasi-retail funds in Jersey. See *Question 7* for more details on the expert fund route in this context.

Reform

15. What proposals (if any) are there for the reform of retail fund regulation?

A comprehensive review of Jersey funds legislation is underway. A new, user-friendly regime should be implemented in the foreseeable future.

The Commission has a large and pro-active enforcement team. Recently, the Commission has increased its investigatory profile and has published critical findings (with public censure) against a prominent Jersey fund administration and custody business.

Contributor Profiles



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Professional qualifications. Advocate of the Royal Court of Jersey, 2003

Areas of practice. Innovative Jersey fund structures, with a particular focus on property and hedge funds.

Recent transactions

- Advising Gravis Capital Partners on the launch of a new fund and the restructuring of their existing Jersey-funds.
- Advising Ahli United Bank (UK) PLC on the restructuring of AUB Central London Office Fund.
- Advising Alpha Real Capital LLP on their restructuring of an existing Irish fund into a new Jersey vehicle.
- Advising Brevan Howard Capital Management LP on internal restructurings.
- Advising Morgan Stanley & Co International plc. on the establishment of a new Jersey expert fund and new sub-funds.
- Advised SG Hambros on the launch of new sub-funds for SGH Collectives PCC.
- Advising Bluecrest on their migration to Jersey.
- Advising Systematica on their established regulation in Jersey.
- Advising Altis Partners on a new fund launch.



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Areas of practice. International funds and corporate work with a particular emphasis on private equity.

Recent transactions

- Carey Olsen advised Blackstone/GSO Loan Financing Limited ("the fund") in respect of the listing of shares of the fund on the Channel Islands Securities Exchange Limited and continues to advise the fund in respect of its future growth opportunities. The fund is listed on the Specialist Funds Market of the London Stock Exchange and the Channel Islands Securities Exchange.
- Advising Kennedy Europe Real Estate Plc in relation to the successful close of its GB£300 million debt senior unsecured bond and GB£2 billion Euro Medium Term Note Programme, under which a further EUR300 million notes were issued.
- Advising Global Advisors on the launch of the world's first ever regulated Bitcoin investment Fund.
- Advising on the establishment of Kennedy Wilson Europe Real Estate plc and unprecedented capital raise of up to GB£1 billion through its initial public offering (IPO) on the LSE.
- Advised on the Jersey law aspects of one of last year's most competitive real estate acquisition and financing mandates: the GB£430 million purchase of three UK business parks in a joint venture between funds managed by Oaktree Capital Management, LP and Patrizia Immobilien AG.
- Advising Hastings Insurance Group on investment by Goldman Sachs private equity funds valuing the business at GB£700 million.
- Advised property company Kennedy Wilson Europe Real Estate plc (KWERE) on its acquisition of a corporate vehicle that owns the building which houses the Telegraph Media Group's London headquarters.



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Areas of practice. Investment funds (including structuring and formation of investment funds and offshore funds).

Recent transactions

- Acting for PW Real Assets LLP (formerly Perella Weinberg Real Estate UK LLP) in relation to their substantial Jersey-domiciled fund portfolio focused on real estate and real estate related opportunities in Europe Advising on the establishment of the Falko Regional Aircraft Opportunities Fund L.P, which raised US\$415 million in capital to fund the purchase and leasing of aircraft primarily based in developed markets across Europe, Australia and the US.
- Advising Nordic Capital in respect of their extensive £GB billion Jersey-domiciled private equity fund portfolio, including in relation to the launch of the firm's eighth fund, Nordic VIII, which closed with investor commitments of EUR3.5 billion.

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