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Introduction

This document is intended to provide a brief overview of some of the legal and regulatory considerations to be taken into account when establishing a new open-ended fund (a "Fund") in Guernsey.

Type of funds

A new Fund can be established using any one of a range of vehicles including traditional limited liability companies, protected cell companies, incorporated cell companies, unit trusts and limited partnerships. The introduction of "Foundations" is also currently being considered by the States of Guernsey.

The choice of vehicle for a new Fund will usually be driven by a number of considerations including the nature of the underlying assets, taxation, market practise and investor requirements. More detailed information can be provided on the range of vehicles available and their respective characteristics.

New promoter

When launching a new Fund it is necessary to identify a promoter (the "Promoter"). In some cases the identity of the Promoter is clear. In other instances the identity of the Promoter is not so clear. As a general rule, the Promoter is usually the person, or persons, establishing the Fund and ultimately responsible for ensuring its success. In the case of a failed launch the Promoter is usually the person, or persons, responsible for paying the abort costs.

The Commission requires each Promoter to be "fit and proper" and to have, and be able to demonstrate, an identifiable track record in the management of third party assets. For these reasons the Guernsey Financial Services Commission (the "Commission") has produced a checklist of information (the "New Promoter Checklist") that must be completed by each new Promoter. The New Promoter Checklist will need to be prepared in respect of each new Promoter along with a bundle of supporting documents. The bundle will need to contain information relating to operating history, group structure and financial status. The ultimate beneficial owners of the Promoter will also need to be disclosed. Individuals holding more than 15 per cent of the Promoter's voting capital, along with the

Promoter's directors, will need to complete a personal questionnaire in the form of a form PQ.

Once a Promoter has been cleared, it will not be necessary to undertake the same due diligence exercise for future fund launches sponsored by that Promoter although it may, from time to time, be necessary to update the information.

Establishing the funds vehicle

Recent reforms in Guernsey have introduced a new companies law, a new companies registry and a new company formation procedure. Under this new regime it is possible to establish a Guernsey company using an on-line facility. It is no longer necessary to seek the approval of the Commission prior to incorporation and fund vehicles can therefore be incorporated in advance of launch. Incorporation can be achieved within 24 hours, two hours or even 15 minutes, depending on the option adopted and the fees paid. The new process has greatly improved the efficiency of company formations in Guernsey.

Limited partnerships and unit trusts can also be established very quickly, although they still require the consent of the Commission. However, whilst a new limited partnership or company requires registration with the Company Registry, unit trusts can be established through the simple execution of a trust instrument.

Pre-marketing

Guernsey regulations do not prevent the issue of "red herring" or "pathfinder" offering documents prior to the grant of authorisation or the registration of a Fund providing appropriate language describing the status of the document is included on the cover sheet. Having said this, no monies may be raised until authorisation has been granted or the Fund has been registered, as the case may be.

We would discourage circulation of any marketing materials referring to Guernsey as the jurisdiction in which a new Fund will be established until, in the case of an application made in respect of an Authorised Fund, the Commission has at least granted outline consent. In the case of a Registered Fund, the Administrator should be consulted in respect

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of any early marketing materials to ensure that there are no issues that would prevent it, in due course, from giving the necessary warranties to the Commission and thus delaying or preventing the launch of the Fund in Guernsey.

Taxation

Exempt Status

The States of Guernsey abolished exempt status for the majority of companies with effect from 1 January 2008 and introduced a zero rate of tax for companies carrying on all but a few specified types of banking, utilities and/or property development business. However, the Administrator of Income Tax continues to allow collective investment schemes to apply for exempt status and, consequently, to be treated as non-resident for tax purposes. An annual fee of £600 is payable for the privilege of exempt status. Alternatively, if the Fund chooses not to apply, it will be treated as resident in Guernsey for tax purposes and its income will be taxable, albeit at the rate of 0%.

Payments of dividends by a Fund with exempt status are regarded by the Administrator as having their source outside Guernsey and are therefore payable without deduction of tax in Guernsey. A non-Guernsey resident shareholder will not be liable to Guernsey income tax unless he is carrying on business from a permanent establishment situated in Guernsey (in which case, distributions would only be taxable if they formed part of the profits of the business in question).

EU Savings Directive

Guernsey has introduced measures that are equivalent to the EU Savings Tax Directive (the "Directive"). However, the States of Guernsey has issued guidance stating that only Class A open-ended funds established in Guernsey are within the scope of the Directive. Closed-ended funds and other types of open-ended funds therefore currently fall outside of the scope of the Directive and paying agents are not required to operate the measures on distributions made to shareholders of such funds.

Other Taxes

The Guernsey authorities do not levy capital gains taxes (other than a dwellings profit tax

on real estate), inheritance taxes, gift taxes or estate duties (other than small probate charges), nor is there any value added tax on the provision of goods or services. No stamp duty is payable in Guernsey on the issue or transfer of shares, units or interests in a Fund.

Authorised, Registered and QIF Funds

Following recent changes made to the Protection of Investors (Bailiwick of Guernsey) Law 1987 an open ended collective investment scheme may now be established as a registered fund (subject to no/very little ongoing supervision by the Commission) or as an authorised fund (subject to ongoing supervision by the Commission). The principal differences between the two types of fund are outlined below.

The disclosure requirements for a registered open-ended scheme are contained in the Prospectus Rules. Although there are some similarities, there are certain additional requirements under the Prospectus Rules and some differences in comparison with those required for Authorised Class B schemes under the Class B Rules.

The issues to be considered when deciding whether or not a scheme should be authorised or registered include the following:

- **Rules:** Authorised schemes are governed by the applicable rules (Class A, Class B, Class Q). A registered open ended scheme is governed by the Registered Collective Investment Scheme Rules 2008 and the Prospectus Rules 2008.
- **Disclosure:** The differences between the disclosure requirements for registered schemes as set out in the Prospectus Rules and those for authorised schemes (contained in the relevant Class rules/ Commission forms) should be noted. In particular, the Prospectus Rules contain certain prescribed statements which must be made in a registered fund prospectus (subject to any derogation which may be granted in any particular case by the Commission).
- **Application process:** An authorised scheme may choose between the traditional three stage application process or the Qualifying Investor Fund ("QIF") fast track (72 hour) process. A registered

scheme has a fast track process similar to that for a QIF except that there is no qualifying investor restriction.

- **Supervision:** An authorised scheme must file all amendments to scheme particulars and principal documents and is required to notify and obtain prior Commission written approval for certain changes. Prior written approval for a registered fund is required only for the addition of new classes, sub-funds etc. A registered scheme is required only to notify the Commission of certain material changes and an annual notification regime applies in respect of all other changes.
- **Offering Restrictions:** A registered fund may not be offered directly to the public in Guernsey. However, a registered fund may be offered to regulated entities in Guernsey, or to the public, via a person licensed to carry out promotion under the relevant regulatory law. There are no restrictions contained in the class B Rules in respect of offers in the Bailiwick of authorised funds.
- **Service Providers:** Both types of scheme are required to have a Guernsey incorporated and licensed administrator ("designated" manager) and a Guernsey incorporated and licensed designated trustee/custodian. There is no relaxation of this requirement for registered schemes. 'Conflicts of interest' and 'arms length' requirements also apply to both regimes.
- **General:** Whilst neither regime is overly prescriptive in that there are no specified detailed investment parameters or limitations, the rules applicable to authorised schemes arguably impose a greater administrative burden on the scheme and the scheme service providers. The Class B Rules, for example, include provisions governing the administration of the scheme by the parties, dealings in shares, the register, distribution of income, reports to holders, content of reports, meetings of holders, termination of the scheme and service of notices. Investors must be given sufficient notice to enable them to deal in shares of the scheme prior to

any change of investment, borrowing or hedging powers becoming effective and 90 days' notice is required of any increase in the manager's maximum periodic charge. In addition, authorised open ended schemes are usually subject to the Commission's Designated Person Rules, including provisions relating to client money and contract notes.

- **Marketing and Suitability:** A registered open ended scheme may be perceived by many to be "unsupervised". Consequently, consideration must be given to the effect that will have on investor perception and the marketability of such a fund and also whether an "unsupervised" fund is suitable for the target investor base.

Establishing a new Principal Manager

Although the Commission only strictly requires the appointment of a designated manager (ie a local administrator) for a new open-ended fund, most new open-ended funds are established with a locally-licensed principal management vehicle. Most local administrators are uncomfortable with the level of investment responsibility they are expected to carry if a Commission-licensed principal manager is not established.

In addition to the fund vehicle it is therefore often necessary to establish a second Guernsey company (the "Manager"). The Manager will normally require a licence from the Commission under the Protection of Investors (Bailiwick of Guernsey) Law 1987. This is a relatively straightforward process and can be run as part of the overall fund set up procedure. Details of the Commission's requirements in relation to the license application are set out below. A period of approximately six to eight weeks should be allowed for making the relevant application and obtaining the licence (unless the Fund in question is established as a Qualifying Investor Fund or a registered fund in which case a fast track licensing power can apply).

As part of the license application for a Manager it will be necessary to submit, amongst other things, the following:

- A financial business plan for the Manager including a simple budgeted profit and loss account for the next 12 months and

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an estimated balance sheet as at the end of that 12 month period.

- A three year business plan would be required in the event that the Manager intends to maintain a physical presence in Guernsey. Otherwise this requirement will usually be satisfied by confirmation in the accompanying cover letter that the Manager's three year business plan is to act as manager to the new Fund.
- An explanation of how the Manager will be run, staffed and managed and the support systems that will be put in place. Normally the administrator's support systems will suffice in the case of an entity with no physical presence in Guernsey.
- A structure chart showing where within a group the new entity will sit.
- A copy of the insurance policy that will provide professional indemnity insurance in respect of the Manager along with a clear statement in the Form RA/1 as to the exact level of cover such policy provides.
- A copy of the administration agreement between the Manager and the chosen Guernsey administrator.
- Confirmation from the Directors of the Manager that it has sufficient paid up share capital and appropriate professional indemnity cover to withstand the risks it may face.
- The Manager will also be subject to certain regulatory capital requirements. In the case of a Manager with no physical presence, the Manager is usually just required to have gross capital and professional indemnity insurance sufficient to meet its commitments and to withstand the risks to which the business is likely to be subject. Normally, a paid up capital of £10,000 will suffice.

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