

UPDATE

Summary of Jersey Funds Updater

Update prepared by Carla Benest (Partner, Jersey), Alistair Horn (Partner, Jersey), Joel Hernandez (Partner, Jersey) Mark Chambers (Partner, Jersey) and Leanne Wallser (Counsel, Jersey)

Overview

With just three weeks until its implementation (on 25 May 2018), newly appointed Mourant Ozannes partner, Carla Benest, provided an expert update on the impact of GDPR from a funds perspective.

Partner Ben Robins then moderated a panel session, involving Jersey partners Alistair Horn, Joel Hernandez, Mark Chambers and Jersey counsel Leanne Wallser, exploring a wide variety of market-driven, legal, tax and regulatory developments impacting on our funds industry, including uses of the buoyant JPF regime, tech fund trends, hopefully early signs from UK property CGT working groups and a full round-up of progress with local legal and regulatory initiatives.

GDPR

Carla Benest provided insights on the impact of the General Data Protection Regulation (GDPR) and its equivalent Jersey legislation on the Jersey funds industry.

She discussed the entities which are likely to be identified as a "data controller" in fund structures and the responsibilities that a controller has. In complying with the data protection principles contained in the legislation, data controllers must understand their reasons for processing data and identify the particular legal ground(s) for processing data on which they are relying. In line with the GDPR's greater focus on transparency, the grounds relied upon need to be explained to investors and other relevant data subjects, by way of a privacy notice, so those individuals understand exactly what data is held about them, why it is held and how it is used. As a consequence, existing fund documentation as well as new prospectuses and subscription documents should be reviewed and updated to ensure compliance.

Carla stressed the importance of fund boards ensuring that they are well versed in the obligations pertaining to data controllers, in particular regarding data protection breaches to ensure that such breaches are reported to the supervisory authority within the necessary timeframe. It will be important that the fund engages with its administrator (and other service providers where relevant) in supporting these matters. In particular, the fund data controller must review its relationships with third party providers and, where such provider is acting as a "data processor", ensure any contractual arrangements regarding the processing of personal data are updated to meet new requirements. For most fund structures, this will require a review and update of the agreement with the administrator as a minimum.

Panel Session – a summary of the questions asked and responses given

Question 1: Mark, the latest JFSC statistics on the use of JPF's seems to show that market as buoyant. Is that what you are seeing, who's been using this approach and why?

Yes – we understand around 120 JPFs have been launched to date. Why has it been so successful? It's a very versatile product. We have seen it used for:

- numerous private equity, venture capital, real estate, infrastructure, credit and technology funds for well-established promoters raising capital for successor funds; but also
- first-time funds for new fund promoter teams, bringing their collective past experience to bear in setting up their first-fund platform in a cost-effective environment; and
- narrowly-held co-investment structures.

Conclusion: it's a very efficient and cost-effective route to launching a wide variety of private fund structures in Jersey.

Question 2: What do you think marks the differentiation from prior regulatory frameworks? In other words, what's so "special" about JPF's?

Several features:

- Streamlined authorisation procedure (48 hour turn-around)
- No application of JFSC promoter policy
- Offering document flexibility
- Open architecture
- Type and number of investors (up to 50 professional/sophisticated investors)
- Flexibility for structuring (different types of fund vehicle permitted, whether Jersey or non-Jersey)
- Regulatory advantages (licensing exemptions) for the establishment of Jersey-based managers/advisors
- Ease of interaction with EU marketing requirements

Question 3: Do you think this enables Jersey to further challenge Luxembourg as a funds domicile?

Yes, on a number of fronts:

- (1) regulatory timing: 48 hour JFSC turnaround, far less time than in Lux, which can take weeks or months
- (2) no need for regulated manager/AIFM (unless above-threshold for AIFMD) because local licensing exemptions usually apply
- (3) lower costs generally, whether legal fees, regulatory fees, audit fees (no need to have one), service provider fees and costs (since less need for highly regulated service providers with detailed regulatory roles) – and no VAT!
- (4) far fewer "rules" for the manager and fund compared to either AIFMD/Lux on the one hand (or FSB/CIF Codes in Jersey on the other)
- (5) lack of offering document requirement/ prescription (unless "above-threshold" and actively AIFMD marketing)
- (6) no depositary requirement (unless "above-threshold" and actively AIFMD marketing to Germany/Denmark)

Question 4: Leanne, looking at recent EU developments, what are we seeing around a possible "AIFMD II"?

The European Commission issued a press release and draft "Omnibus Regulation" in March 2018, off the back of its Capital Markets Union (CMU) initiative to enhance the free flow of capital around the EU. The draft regulation is proposed to amend both the AIFMD and UCITS directives, with a desire to reduce the costs for cross-border distribution in the EU and make it simpler, quicker and cheaper.

- the papers admit that currently 70% of the total assets under management under the directives are held by investment funds authorised or registered for distribution only in their domestic market. And only 37% of UCITS, and about 3% of alternative investment funds (AIFs) are

registered for distribution in more than 3 Member States. This really underlines the limited practical value of EU passporting under AIFMD in most cases!

- the proposals include provisions intended to improve transparency, by aligning national marketing requirements, and reduce regulatory fees (at the moment there is broad EU national variance)
- the papers also propose harmonising the conditions under which investment funds may exit a national EU market if they wish to cease marketing there; and add of a new definition of acceptable "pre-marketing" activity – this latter element requires careful consideration and an industry lobbying response as the proposed "pre-marketing" definition doesn't sit comfortably with current processes for the pre-marketing of AIFs (eg by including the circulation of draft constitutional documents (such as LPAs) within the definition) – it is likely that Member States will also apply the same definitions to NPPR marketing arrangements
- there is no specific mention of changes to the 3rd country NPPRs in these proposals but, in their recent visit to Jersey, Invest Europe suggested that 3rd country NPPRs may be revisited in AIFMD II after BREXIT has been concluded (perhaps in 2/3 years' time).

Question 5: Joel, a lot has been made of the proposed CGT changes impacting on foreign owners of UK property - could you provide a brief summary of what HRMC announced in November 2017?

This relates to HRMC's November 2017 consultation paper to extend capital gains tax (CGT) to non-resident investors disposing of UK commercial property. Key features of the proposal include a rationale to increase tax revenue, the creation of the single regime for the taxation of UK commercial property and the application of CGT to direct and indirect disposals of UK commercial property by non-resident investors from April 2019.

Question 6: It seems that the industry responses to the consultation have been extensive. Can you take us through some of the issues that have been raised and some of the anecdotal feedback you've received on the consultation?

Industry feedback on consultation had been significant. A number of common issues had emerged from industry feedback. This included: (a) the need to avoid an adverse impact on those investors who would otherwise be exempt from CGT (eg. pension funds, charities, sovereign funds) who may indirectly suffer tax where they are investing through foreign entities (such as JPUTs); and (b) the need to address the disadvantages that would be faced by offshore collective investment vehicles when compared to the special tax regimes that apply to UK collective investment vehicles (eg. REITs, PAIF, and CoAC regimes), which have structural and practical limitations relative to offshore equivalents.

Question 7: What's next following the consultation?

Industry consultation with HMRC and HM Treasury has continued and has proved constructive with the need to address some of the key concerns raised during the feedback, including those raised in Question 6 above, being recognised. Draft legislation is expected to be released in late summer 2018.

Question 8: Alistair, you have been actively involved in the areas related to Fintech. How is this relevant to Jersey Funds?

Our Jersey team has long had exposure to funds which invest in a wide range of technology-related companies, including anything associated with the research, development and use of computers, software, apps, electronic communications, the Internet, semiconductors or any other segment of technology.

Although there are exceptions, most technology funds tend to invest in larger, more established technology companies that have strong cash flow and substantial market share or companies that have developed new ideas or patents that analysts believe will provide significant potential for growth.

Promoters of these funds have been able to use the regulatory regimes on offer in Jersey to raise significant amounts of money.

Question 9: Can you tell us about virtual currencies and Jersey funds? Is this [an area] relevant to Jersey? And what is driving this?

Yes, there is no doubt the media attention around bitcoin and other digital currencies means that interest in investing in digital currencies is growing. The astronomical (although fragile) profitability of investments

in cryptocurrencies and ICO tokens has also drawn the attention of newcomer investors. Most of them do not fully understand the technical and financial features of the crypto market but well-run crypto funds can provide them with a relatively secure investment method.

In short, the number of crypto funds is growing by the day, and the amount of funds under management already exceeds 4 billion dollars. This means there are potential opportunities for Jersey in the fund formation area through reputable promoters.

Question 10: Can you give a give a quick overview of the crypto fund landscape?

Crypto funds are generally similar to conventional funds in their structuring. They borrow investment strategies from conventional funds to some extent and adapt them to the crypto market. Operationally, however, there is plenty that's novel to consider in terms of the way the crypto currencies function; for example:

- if a manager is taking in crypto-assets as "in kind" subscriptions, then it becomes very difficult for the MLRO at a fund administrator to check the source of that subscription, so this may not be allowed
- accounting best practice is a work in progress
- custody: how can crypto assets safely and legally store their tokens or digital assets?

Question 11: You mentioned ICOs briefly before. What's the update on this?

The JFSC has issued a couple of releases warned potential investors of the risks involved in investing in an ICO and industry is currently working with the Government, JFSC and relevant stakeholders to formalise a policy regarding the licencing of Jersey based ICO Issuers and the service providers in relation to ICOs.

Question 12: Leanne, what's next/on the regulatory and legal horizon for Jersey funds?

JRAIFS

- having streamlined the private funds arena with JPFs, it is likely Jersey will be looking towards doing the same for public funds in Jersey with introduction of the JRAIF regime
- again, the focus will be on simplifying the application and regulatory processes, with the main difference being an emphasis on the regulation of the JRAIF's manager, not the fund
- the JFSC is currently working on a draft JRAIF Guide, to be reviewed by Government prior to inviting comments from industry in the coming weeks.

LLP Law amendments

Debate is scheduled for 26 June 2018 with the amended LLP Law to come into force from 1 July 2018. Government is confident that this timeframe is achievable.

COBO Amendments/Registry Law

Government and JFSC are developing a new Registry Law and proposing amendments to COBO in tandem. This has been assigned a high priority. The intention is to plug gaps in the supervisory and enforcement powers of the JFSC, to formalise the provisions on the central beneficial ownership register and to include the new central register of Jersey company directors. We understand that this could also substantially change the authorisation process for SPVs and fund vehicles.

The targeted implementation date for both sets of changes is June 2019 and they warrant prompt and close inspection by industry.

Company Demerger Amendments

These regulations were lodged on 27 February for debate at the end of June 2018.

The message from industry is that the sooner we can bring the demerger regulations into force the better. This is in part because of the upcoming UK CGT changes which may necessitate a measure of restructuring of real estate holding structures. Having the ability to de-merge certain structures may avoid the need for some clients to re-domicile the whole structure and therefore some of the structure could remain in Jersey. Government are aiming for the demerger regime to come into effect on 1 September 2018.

MIFID II

- A Consultation Paper on implementing certain MIFID II measures in the Island is due out in out in the coming weeks.

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