

Summary of Jersey Funds Updater (16 January 2020)

UPDATE

Update prepared by, Ben Robins (Partner), Sarah Huelin (Counsel), Tim Morgan (Partner) and Mathew Cook (Counsel)

JFSC Commissioner Mark Hoban, previously the Financial Secretary to the UK Treasury and currently a non-executive director of London Stock Exchange plc and chairman of the International Regulatory Strategy Group, joined us as a guest speaker to provide his assessment of the regulatory direction of travel post-Brexit, for both Jersey and the UK. Mark was joined by speakers from our own team who reviewed global and Jersey funds market performance and emerging trends in 2019 and looking forward into 2020. They also provided insightful analysis of the latest legal, regulatory and tax developments impacting Jersey funds industry as we head into 2020.

Overview of Global Private Capital Performance in 2019 – Ben Robins, Partner

Ben Robins provided an overview of the performance of the global private capital industry in 2019 by reference to recently published Preqin data. The data highlight **mixed fortunes across the principal asset classes**: – although most assets classes had a successful fundraising year, capital raised fell behind records set in 2017-2018, and deal-making proved more challenging, with almost all asset classes seeing a decline relative to 2018 levels. Against a backdrop of market downturn fears, these results are perhaps unsurprising, but investor sentiment appears to remain positive as we head into 2020.

Private equity and venture capital – for the fourth year in a row PE fundraising exceeded half a trillion dollars at \$595bn, with 1,316 funds raised but, relative to 2018, the number of funds closed and the amount raised saw modest declines. PE deal-making was strong in 2019 (\$393bn of buyout deals and \$224bn of venture capital deals announced), but also lower than 2018. Preqin remarked that the impact of high deal valuations on future performance has weighed heavily on fund managers, with many slowing the pace of their deal-making to avoid overpaying for investments, but with investor sentiment remaining broadly positive, capital will likely continue to flow into these funds in 2020. With 3,524 PE funds in the market fundraising in January 2020 (compared with 3,465 in January 2018 and 2,257 in January 2017), those investors will be facing an ever more crowded market.

Real estate - in 2019 global RE fundraising reached \$151bn, the highest amount ever recorded. However the number of RE funds closed (295) declined relative to 2018 which indicates that, like PE funds in recent years, RE funds are getting larger, with capital more unevenly distributed between managers and the concentration among the largest RE fund managers greater than ever. RE deal activity in 2019 did not match the records set in 2018 but remains substantial, with manager's still successfully deploying capital. The number of RE funds in the market is at an all-time high.

Infrastructure – continuing its steady growth pattern since 2015, the infrastructure fund market was particularly buoyant in 2019, with 88 infrastructure funds closed, raising a total of \$98bn. This included two \$20bn+ funds, including Global Infrastructure Partners' \$22bn fund, the largest infrastructure fund ever closed. That record fundraising has pushed infrastructure dry powder to \$212bn, twice the figure at the end of 2015, and there are currently 253 funds in the market, targeting \$203bn, suggesting investor appetite for this asset class remains strong. In contrast to the positive fundraising market, numbers of infrastructure

deals have been declining in recent years, having peaked in 2017, but the value of deals ticked-up in 2019 to a second-highest annual total of \$485bn, surpassed only by 2016 (\$523bn).

Private debt funds – have had the most difficult 2019 of all of these asset classes, following a lengthy period of steady growth. More than 200 private funds closed in each year between 2015 and 2018 but in 2019 fundraising fell back: just 152 private debt funds reached their final close. Collectively, those funds secured \$107bn, the lowest annual fundraising total since 2015, and dry powder has fallen back to \$261bn (from \$291bn last year). Deal-making also declined from 2018 levels but, in spite of these downturns, 436 private debt funds currently crowd the marketplace, seeking to raise a total of \$192bn, up from the 399 funds seeking \$168bn at the start of 2019: unless fundraising rebounds significantly in 2020, it is likely many of these funds will face a long haul to raise capital.

Key trends in Jersey in 2019

In 2019 our Jersey funds team has noted:

- **Steady demand for Jersey fund structures.** Although the competition from EU centres for new fund business remains intense where a large proportion of the targeted investors are in the EU, existing managers and GPs using Jersey continue to launch their (usually larger) successor funds in Jersey
- The **enthusiasm with which managers and GPs have adopted the Jersey Private Fund (JPF) model** for their funds, particularly in niche areas such as tech, venture capital and impact investing. Since the inception of the JPF regime in April 2017, **almost 350 JPFs have now been launched**
- A modest decline in regulated collective investment fund (CIF) numbers. **Although the aggregate NAV of regulated funds under management or administration in Jersey reached a high of approximately £341bn** in Q3 2019, the maturity of Jersey's funds market means that historic closed ended CIFs are now coming to the end of their life and more new funds are being launched as JPFs
- **Co-investment and fund finance activity is buoyant**
- **A resurgence in the use of Jersey property unit trusts and increased interest in Jersey structures for UK REITs**

Opportunities for Jersey in 2020

Ben also highlighted some of the key areas of opportunity for Jersey as we enter into 2020:

- **continuing to leverage the success of the JPF product:** the numbers created to date (see above) highlight the appeal of this regime - as a highly cost-effective and swift (48 hour) regulatory route to market for new and existing managers and GPs, and its popularity underlines Jersey's pedigree as an appropriately regulated fund domicile offering genuine speed of execution
- **a levelling of the playing field with Cayman:** the Cayman fund product is a truly global success story and, other than open ended funds with more than 15 investors, it has been largely unregulated to date. A new Private Funds law and an amended Mutual Funds law will shortly extend CIMA registration and a measure of regulation of Cayman funds to cover closed ended funds and all open ended funds. Funds AML, economic substance and GDPR requirements are also landing in Cayman at the same time. This may bolster the relative appeal of Jersey's JPF and Unregulated Fund regimes in a global market context, in terms of relative product stability and cost effectiveness
- **hitting our marks on Economic Substance:** the new economic substance requirements for fund managers in Jersey represent an evolution, not revolution, so whereas the new onshore EU regulatory substance model is putting pressure on the hiring and retention of senior human resources, and the new offshore substance model may prove harder for some other offshore IFCs to adopt, Jersey has an opportunity to present something close to business as usual
- **leveraging our real estate and infrastructure fund capabilities:** three factors point to a potentially strong year for Jersey real estate funds and structures in 2020: (i) the Preqin statistics (above) confirming record fund-raising and substantive deal activity in the global RE and infrastructure fund sectors in 2019; (ii) the likelihood of a post-UK election uplift in UK FDI as Brexit uncertainties reduce; and (iii) the continued availability of tax transparency for qualifying Jersey real estate funds and unit trusts following the recent changes to UK Non Resident CGT

A clear pathway for using the 3 Tier Test – Sarah Huelin, Counsel

Fund managers and fund service businesses use the 3 Tier Test regularly but we know that its application to complex structures raises queries. The Test determines who are the beneficial owners and controllers of an entity and is used to complete client due diligence (CDD) and to choose the correct individuals for inclusion on the Registry's central register of beneficial owners and controllers.

It is helpful to remember that the Test originates in guidance from the Financial Action Task Force and the requirement to identify beneficial owners and controllers for CDD and transparency purposes is an international standard. Using the Test puts Jersey on a level playing field with others who follow these standards.

In summary, the Test is used to identify: (1) any person with control through ownership interests; and (2) any person with control through other means; and, if necessary (3) any person with control through positions held. There are some useful rules to keep in mind when applying the Test. For example, owners of a company are only of interest if their ownership gives them control and tier 3 of the Test should only be applied if no individual has been identified by applying tier 1 and tier 2.

Our experience is that using a clear pathway and set of rules to apply the Test, helps to ensure that it consistently reaches the right outcome, even in relation to the most complex structures. For example, if the Test is applied correctly to a Jersey company that is the general partner of a Jersey limited partnership and to the limited partnership itself, the individuals who are the beneficial owners and controllers of each entity will not necessarily be the same.

If we can help by guiding you through our pathway to applying the Test, do get in touch.

Sound Business Practice Policy Update

The JFSC updated its Sound Business Practice Policy in November 2019 by adding two new activities that are to be regarded as sensitive and posing reputational risk to Jersey. The two new activities are:

- (a) where an activity is regulated in Jersey but not in the 'target market'; and
- (b) the cultivation, production and supply of cannabis (even where the activity is lawful in the place where it is being carried out).

The detail of the updated policy should be considered in any case where a Jersey entity is planning to carry on one of these activities or to invest in other entities carrying on one of these activities. In some cases it won't be possible to use the Jersey entity and in others, it might be necessary to agree some mitigating factors with the JFSC, in order to obtain a COBO Consent.

Regulated businesses should remember that they are obliged to have regard to the Sound Business Practice Policy. This would apply, for example, if any client entity is already doing these new sensitive activities and if any client entity plans to change its activities to include sensitive activities.

Economic Substance update – Tim Morgan, Partner

Following the updates to the economic substance guidance notes at the end of 2019, we reviewed key economic substance issues applying to Jersey fund managers, including issues around classification, dealing with multijurisdictional fund structures, best practice around governance including the directed and managed test, and a focus on definitions of CIGA for fund management. We are working closely with Revenue Jersey on developing best practice around the governance and the documenting of management structures and decision-making across different asset classes. We are also assessing further detail in relation to the treatment of certain self-managed funds.

Jersey Funds Association, Member Survey Results

We considered key feedback from the Q4 2019 Jersey Funds Association member's survey. Particular focus was placed on Brexit/political confidence issues, the impact of economic substance on growing the Jersey governance model, likely industry engagement with the JFSC going forward and the increasing focus on outsourcing and technology as the industry develops. These are all areas that we anticipate to be relevant as workflows in 2020 develop, and as Jersey's funds industry positions itself increasingly strongly in the current economic, political and regulatory environment, as touched on the market developments section.

We also considered the valuable role in being able to articulate the strengths of Jersey's funds ecosystem in a fast-evolving environment.

Data Protection Registration Regulations – Mathew Cook, Counsel

The Data Protection (Registration and Charges) (Amendment) (Jersey) Regulations 2019 came into force on 1 January 2020, and amends the model for registration charges for data controllers and processors. In light of existing demands on data protection compliance, the fees are inevitably increasing for many entities, particularly in the financial services industry. The new model does give rise to some issues, in particular:

- The applicable fee under the new model is determined based on revenue, employee numbers, type of business and whether special category data is processed. That may be straight-forward for a business made up of one company which employs all the staff and receives all the revenue, but is clearly more complicated for a group structure, and may not be ascertainable for the relevant period by the time the relevant details need to be submitted; and
- More fundamentally, there is the question of companies administered by a trust company business or fund services business. There is now an exception whereby those administered companies do not need to register individually, but register through the TCB or FSB. That is helpful, but it does raise the question of what is intended to be caught as an administered company. Previously, companies processing very little personal data may have been able to rely on either an exemption or by an accepted position on the part of the Office of the Information Commissioner. However, it appears that that no longer applies, and rather the expectation is that all Jersey companies need to be registered. In addition to the burden of paying the standard £50 fee for administered company, there is the additional burden of full compliance with the Data Protection (Jersey) Law 2018 including, for example, having a privacy notice. Arguably, that creates an unnecessary administrative burden on companies processing a very small amount of data on their own directors and shareholders only.

We are liaising with the Office of the Information Commissioner to try and get clarity on these points and a further briefing will follow.

Contacts

To find out more about any of the topics mentioned above, please get in touch with your usual Mourant contact, or, alternatively, contact one of the specific contacts named below:



Ben Robins
Partner, Mourant Ozannes
Jersey
+44 1534 676 475
ben.robins@mourant.com



Felicia de Laet
Partner, Mourant LP
Jersey
+44 1534 676 137
felicia.delaat@mourant.com



Tim Morgan
Partner, Mourant Ozannes
Jersey
+44 1534 676 817
tim.morgan@mourant.com



Mathew Cook
Counsel
Jersey
+44 1534 676 688
mathew.cook@mourant.com



Sarah Huelin
Counsel
Jersey
+44 1534 676 540
sarah.hueln@mourant.com

This update is only intended to give a summary and general overview of the subject matter. It is not intended to be comprehensive and does not constitute, and should not be taken to be, legal advice. If you would like legal advice or further information on any issue raised by this update, please get in touch with one of your usual contacts. © 2020 MOURANT OZANNES ALL RIGHTS RESERVED