

HFEM

HEDGE FUND MANAGER

SPECIAL REPORT

GUERNSEY 2007

A photograph of a lighthouse on a stone pier in the ocean. The lighthouse is white with a stone base and a lantern room on top. The pier is made of large stone blocks. The ocean is blue and the sky is clear.

A leading light

Guernsey's alternative investment
fund levels reach record highs

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Peter Niven, chief executive of GuernseyFinance, charts the success of the funds industry on the Channel Island

The cutting edge

Guernsey's investment fund industry is booming. The substantial growth that was a feature of 2005 continued throughout 2006, pushing levels of business to record highs. It was largely driven by a surge in alternative asset classes, including hedge funds.

The island has become well known as an administrative centre. But the depth of expertise, strong corporate governance, convenient location and fast-track consent process for funds targeting experienced investors have made Guernsey increasingly popular with promoters and managers seeking a base for their funds – in particular, alternatives.

Notwithstanding these huge flows of business, work is ongoing to enhance Guernsey's funds environment. In February, the island introduced a new streamlined consent process for registered closed-ended funds that will be particularly attractive to promoters and sponsors looking for a hedge fund domicile. Guernsey is by no means resting on its laurels.

Booming funds industry

Figures from the island's regulator, the Guernsey Financial Services Commission (GFSC), show that the value of funds under management and administration in Guernsey last year increased by 30.2% to a record level of £130.2bn. A breakdown reveals:

- Guernsey-domiciled open-ended funds grew by 17.5% to finish 2006 at £56.6bn;
- Guernsey-domiciled closed-ended funds rose by 55.8% during 2006 to reach £48.5bn;
- The combined total of £105.1bn was the first time it has exceeded the £100bn mark; and
- Non-Guernsey schemes, for which some aspect of management or administration is carried out on the island, rose in value by 21.2% to £25.1bn.

Fund approvals also ran at record levels during 2006:

- There were 48 new open-ended funds and 127 closed-ended ones. The total of 175 was 62 more than in the previous year.
- Of these, 51 were qualifying investor funds (QIFs). These are the fast-track consent pro-

cess for funds targeting experienced investors that were introduced early in 2005, and through which 27 funds were established that year.

Market conditions have undoubtedly played a part, but it primarily indicates how Guernsey is being viewed as a jurisdiction of choice for alternatives. Indeed, while traditional funds remain well represented in these increased business flows, it is the popularity of alternatives such as hedge funds, private equity, property and more esoteric asset classes such as timber, wine and fine art that have played a major part in this growth.

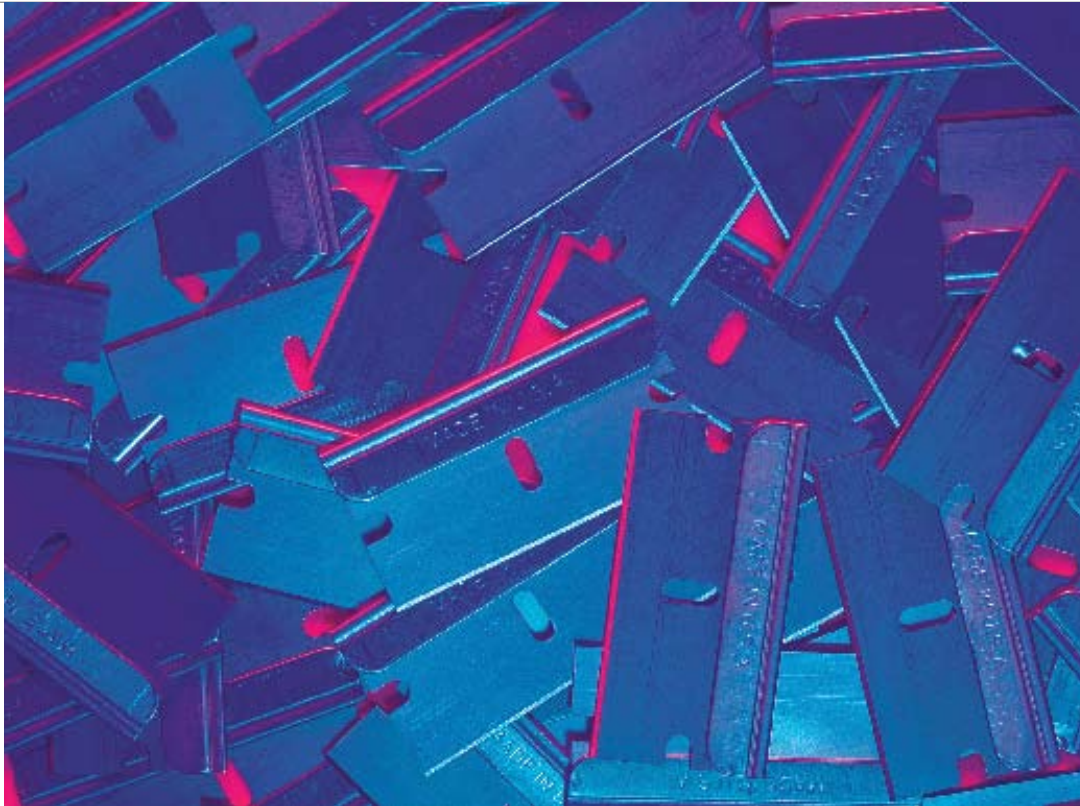
Hedge fund-friendly environment

Guernsey's funds industry has nearly four decades of experience in providing investment products and services. This has helped establish a sector with a substantial depth of expertise, making the island a particularly attractive location for the administration of funds – especially alternatives such as hedge funds. This expertise is also making the jurisdiction increasingly popular for the domiciling of alternatives.

Today, there are more than 45 administrators on the island, with a significant number specialising in alternative funds. Most funds that they service are Guernsey open- and closed-ended funds, which are now promoted and sponsored by leading institutions in 45 countries. These funds can be established through a range of flexible investment vehicles such as unit trusts, PCCs, ICCs and limited partnerships, which the administrators are skilled at using.

Guernsey's administrative heritage is increasingly being complemented not just by the availability of custody services, but also fund managers, and in particular those specialising in hedge funds, ranging from larger organisations such as Financial Risk Management to more boutique operators such as BBBSA Strategic Management.

The island's broad-based financial services industry means that there are on-island banking, fiduciary and insurance providers, legal advisers, auditing and tax advisers and stockbrokers, as well as the Channel Islands Stock Exchange (CISX).



Peter Niven is the Chief Executive of GuernseyFinance

Guernsey also boasts a large pool of experienced and qualified non-executive directors. There are no direct rules on the make-up of the board for funds domiciled in the island, but it makes practical sense that the majority of directors would be located locally. Taking this approach also helps provide clear delineation between the onshore investment management and the offshore overall management and control of the company. Finding the required personnel is made easy in Guernsey, which as a result has rightly acquired a reputation for strong corporate governance.

Domiciling (and, for that matter, administering) a fund in Guernsey, particularly for investment managers in the UK, is also made easier by the island's location. Situated between the UK and the Continent, it is in a time zone that allows business to be conducted with the US and the Far East during the same day. There are good air and sea links to the island, with flights from London taking less than an hour. In addition, a high volume of business can be carried out face-to-face in a short period of time

because of the proximity of Guernsey's institutions and businesses.

Avoiding complacency

Guernsey cemented its position at the forefront of the international fund and, in particular, alternatives industry when it introduced QIFs early in 2005. This self-certification regime, which enables short authorisation times for funds targeting experienced investors, has become increasingly popular.

With a thriving funds industry, it might be easy for the island to become complacent. However, the industry, regulator and government established a working party led by leading Guernsey advocate Peter Harwood to undertake a root-and-branch review of investment funds sector legislation and regulation. The Harwood Report, as it was christened, made several recommendations, including the creation of a 'registered funds route' where the focus of regulation would be on the licensed Guernsey administrator, rather than the individual investment funds as products.

A registered regime was introduced for closed-ended funds on 1 February, 2007.

Taking this avenue means that the GFSC will grant the required fund consent within three working days if the Guernsey licensed administrator can show that it has carried out sufficient due diligence to be satisfied that the promoter and associated parties are fit and proper. This is a development of the approach taken by the Commission in respect of QIFs. The rest of the Harwood Report's proposals will be implemented when legislation is enacted later this year.

Flourishing market

Guernsey's fund industry is flourishing, with alternative asset classes such as hedge funds playing a significant part. Renowned as an administrative centre, the island's substantial depth of expertise, strong corporate governance, convenient location and fast-track consent process for funds targeting experienced investors have made it increasingly popular for the domiciling of alternatives such as hedge funds. Guernsey's progressive attitude also ensures that developments such as the registered funds regime keep it at the cutting edge of the international fund industry.

Stuart Mauger of Royal Bank of Canada highlights the net added value that an administrator can bring to permanent capital

Fitting the pieces together

The value of Guernsey closed-ended funds under administration increased by 55.8% in 2006 to a new high of £48.5bn. Part of this spectacular increase is related to the trend among investment managers ('promoters') to raise permanent capital on the LSE, AIM and Euronext. Guernsey has become the jurisdiction of choice for fund promoters/sponsors when considering listings across a broad product spectrum of hedge funds, funds of hedge funds, private equity, syndicated loans, real estate and property. According to ABN Amro research, at the end of last year, £5.9bn was listed in hedge funds and individual managers – a 70% rise on the previous year. This constitutes 37 funds of hedge funds and three individual hedge funds.

For fund of hedge fund managers, stepping into public listing enables them and the fund promoters to take a longer-term view with respect to investment returns. Additionally, there is far greater transparency of the underlying portfolio to shareholders, competitors and market makers. Another facet of closed-ended listed funds is the broader corporate governance requirements. For example, a company listing on the LSE would establish a framework to comply with the requirements of the Combined Code on Corporate Governance (June) 2006 issued by the UK Listing Authority, where appropriate.

The Guernsey Financial Services Commission (GFSC) recently introduced a regime relating to the approval for 'registered' funds, whereby closed-ended funds will no longer be required to complete the present consent application process, which can take weeks. Instead, consent may be obtained within three days of the administrator filing the appropriate documents with the GFSC. The administrator has to provide certification that the promoter is fit

and proper, and that the administrator is satisfied with the promoter's integrity, solvency and competency. Historically, while the UK and Guernsey legal teams, together with the lead sponsor, expertly guided the promoter through the launch of a fund, the appointment of an administrator was generally one of the last aspects to be decided. This led to the perception that the administrator's timeframes for conducting due diligence on the promoter, and documenting and transitioning the fund were delaying the launch. In effect, the new regime partners the promoter and administrator from the onset.

Valuing teamwork

This collaborative approach between service provider and promoter is welcomed by Royal Bank of Canada (RBC), whose vision is to "earn the right to be the client's service provider of choice". RBC adopts a team-based approach to prospective fund launches, placing the business professionals in banking credit, trustee, fund accounting/valuations and custody services and their support teams in front of promoters from the first meeting. This ensures the client has an acute understanding and is comfortable with respect to the strength of the RBC team from the onset of discussions. Working in a consultative capacity, RBC's team can understand a client's business needs upfront and add value to a true partnership. Such meetings raise important questions and answers, which RBC is happy to provide guidance on, in particular:

- The roles and responsibilities of a corporate secretary, including the weekly estimate preparation and timeline and agreement of templates for RNS reporting;
- Treatment of currency hedging valuation and cost across share classes;



Since joining RBC in 2001, Stuart Mauger has occupied a number of client-focused roles and has recently moved to become head of sales and business development in the British Isles. This role focuses on the provision of custody and fund administration services.

- Arrangement of inaugural and subsequent board meetings;
- Co-ordination of D&O insurance;
- Preparation of financial reporting procedures board memorandum;
- Review of annual expense budget and working capital memorandum;
- Processing of share conversion programmes and trailer payments; and
- Changes in financial reporting – for example, with the EU transparency directive.

No question is deemed insignificant and RBC encourages follow-up site meetings to deepen each other's understanding.

The manager of transitions acts as the promoter's first point of call for meetings, discussions review and feedback on project plans, prospectus, and service provider agreements with the respective legal teams.

Overseeing this process, the relationship manager will create service standards to ensure mutual expectations among the service provider and promoter are tabled and met, and that the launch is successful.

Trust is important

Promoters appreciate the importance of a 'trusted' relationship manager, who understands their business but is sophisticated enough to know that it would be difficult for one person to have all the necessary skills and experience to deal with specialist areas such as hedge funds and fund of hedge funds. For that reason, promoters highly value the ongoing accessibility to the wider team.

Currently, RBC also acts as 'custodian' to about US\$22bn in hedge funds and can provide ancillary services to promoters, such as currency hedging and timing and settlement financing to the fund. Passive hedging is critical to the performance of fund share class prices and, where a fund is closed-ended, the availability of a credit facility helps the promoter to purchase investments against future redemptions or invoke the discount provisions clause.

Processing about 450 trades a month, the custodian's proprietary 'Utmost' hedge fund deal-

"Promoters appreciate the importance of a trusted relationship manager, who understands their business and knows it would be difficult for one person to have all the necessary skills and experience"



ing system is capable of providing promoters with a full trade status report, from DHL number to acknowledgement to expected contract note date.

Possibly RBC's greatest value to promoters, through its global network, is its commitment to capability, continuity and sustainability in the burgeoning Guernsey funds business.

Its Corporate & Institutional Business operation has 150 staff in the Caribbean, Hong Kong, Guernsey, Jersey, London and Edinburgh, providing global custody and fund administration services to both 'alternative investment' and 'traditional asset' investment managers.

RBC is proud to have been appointed as custodian and fund administrator to the largest LSE-listed fund of hedge funds offering to date, and as custodian to Alternative Investment Strategies, the first closed-ended fund to be listed on the LSE.

Neale Jehan of KPMG asks whether institutionalisation of the funds industry is good or bad for offshore business

Better technique

Institutionalisation has been a growing phenomenon in the hedge fund community for a number of years. As asset allocations continue to swing to the sector, there are few managers whose businesses look like they did ten years ago. As hedge funds utilised as an investment technique become more mainstream, so do their managers.

The phenomenon

Institutionalisation is evident through a number of factors: the establishment of in-house boutiques; the trend for listing funds; the greater demands for transparency and reporting and the pressure on the two-and-twenty fee structure borne out of poor performance in some quarters.

Established investment businesses of the larger insurers, banks or traditional asset managers are creating in-house boutiques which give their investment professionals the flexibility to replicate hedge fund returns but with the established back-office infrastructure. It is early days still for these boutiques but inevitably they may have a distinct advantage over independent managers for institutional money, or at least have less to do to clear the due diligence hurdle.

There is an increasing trend for managers to admit their funds to trading and Guernsey has been a key jurisdiction facilitating this trend, not just with the London Stock Exchange but increasingly Euronext. These funds are key to the institutional phenomena as they enable investors to deal in hedge funds through a traditional analyst route without the detail of the due diligence approach that had previously been the norm.

A very recent but fascinating aside to this is that institutional investors are now becoming more activist in their holdings of these listed hedge funds when faced with bad performance, showing how hedge fund strategies have come full circle and are now mainstream.

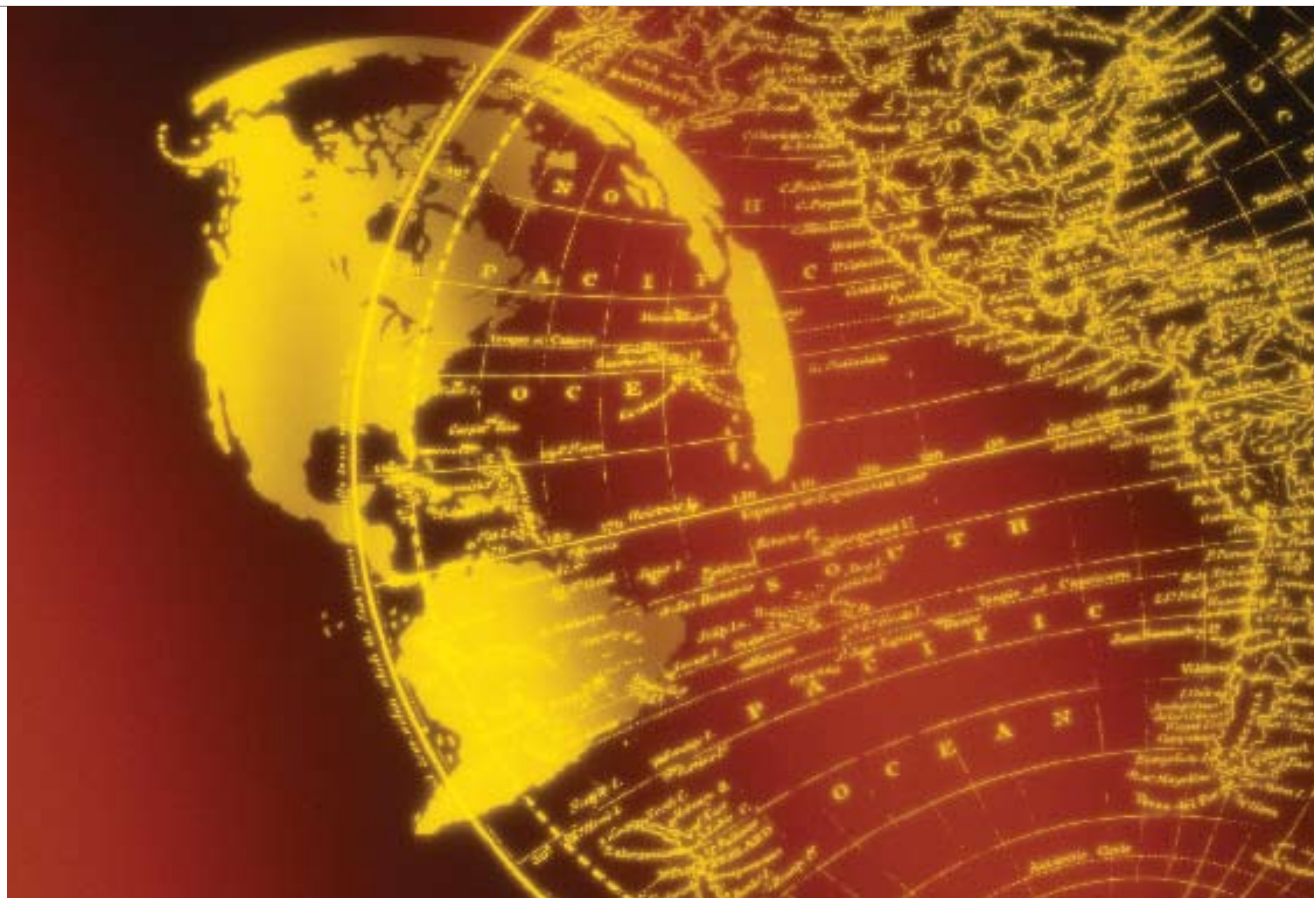
The impact

The operational practices of hedge fund managers are not immune from institutionalisation. Investor demands for continued improvement in governance and risk management bring new pressures to businesses that have typically been front-office focused.

But how does this trend impact the offshore jurisdictions? Well, actually as much, if not more, than it does the managers. From lawyers and accountants servicing listings and administrators and bankers providing the back office infrastructure the demands of institutionalisation feed all the way through the delivery chain.

The island's administrators are the hardest hit as their role is key. The demands of investors lead to a need to produce more information, more quickly and more robustly than before. Institutional investors expect complete transparency in their portfolios which is not something that the industry has been used to providing to date. The systems and personnel implications of these demands cannot be underestimated and a variety of strategies are emerging such as investment in new technology or the increased use of outsourcing.

So does institutionalisation in itself pose a threat to the island? Guernsey does not have an administration



presence from the largest specialist global players in this industry who might be seen more naturally as the home for key institutional administration, either through scale or preferred supplier arrangements. This is not necessarily a realistic threat, however, as the kind of business administered in Guernsey has traditionally been in the fund of hedge funds sector or in esoteric areas where a specialist service is required. The kind of business run by the global players is largely outsourced off-island.

Institutionalisation may also prove an opportunity. As some of our largest administrators are establishing themselves on a global scale and others are growing rapidly there is space in the market for new entrants, subject to the necessary infrastructure of course.

There is also the growing trend for managers to set up a presence in the island. There are many reasons behind this trend, but the challenge of institutionalisation is certainly one of the factors. The ability to monitor the activities

of the local administrator real time and move some of the middle office investor reporting activities to the island can only assist with the improved standards of risk management and governance demanded by investors.

One other factor is divergence of the definition of what constitutes a hedge fund. As the industry appears to subsume everything which once could be described as alternative, its diversity will leave many independent managers with many differing strategies in demand by investors. A maturing industry always has new entrants and new ideas to drive it forwards.

Guernsey has always been a dynamic and responsive jurisdiction at the cutting edge of new developments. Institutionalisation will not significantly change this. There will always be a place in the industry for the island, whether it is dealing with high-profile listed funds or with a smaller body of independent managers promoting funds with emerging alternative strategies.



Neale Jehan leads KPMG's services to the alternative investment sector in the Channel Islands and is a member of KPMG's Global Alternative Investments Leadership Team. KPMG is the leading auditor of funds in Guernsey per the Fitzrovia survey and the European Practice recently won The Hedge Fund Journal Award for the Best Provider of Transactional/ Advisory Services to the hedge fund sector.

Paul Christopher of Ozannes assesses prospects for Guernsey's investment business sector

Sector is keeping its eye on the ball

In early 2005, a committee reviewing the investment sector of the finance industry in Guernsey (one of several review committees) was established with advocate Peter Harwood as chairman. Importantly, Peter Moffatt, the director of the Investment Business Division of the Guernsey Financial Services Commission (GFSC), was also appointed to the committee. This recognised that the industry and regulator would need to co-operate and understand each other to create the appropriate environment for a modern offshore centre.

The terms of reference for the committee were "to consider the investment industry in the bailiwick of Guernsey and the conditions required for its continued prosperity". The review would consider the legal and regulatory framework, as well as aspects of public policy relating to the industry.

Proposals

The committee produced a report in March 2006, which recognised that Guernsey's investment business sector had two sub-sectors:

- The fund-specific sector (investment funds, for example) and related fund-specific services such as custodians, fund managers and administrators; and
- A significantly smaller fund-specific sector, such as traditional investment advisers/stockbrokers, discretionary investment managers, execution-only broking activity, boutique investment houses and wealth management.

Perhaps the most important matter dealt with was the issue of time taken in the licensing and regulatory approval processes in the fund sector. The report suggested that the regulatory approach be altered so that regulation be concentrated less on the regulation of individual investment funds, with more attention given to the regulation of those licensees who provide services to investment funds. To this end, there were detailed proposals to:

- Repeal the Control of Borrowing ordinances and replace them with a generic 'prospectus' law, applicable to all Guernsey entities, setting out minimum disclosure criteria for offering documents;
- Take the funds' provisions from the existing Protection of Investors Law and modify them to become a generic 'funds law' applying to both the open- and closed-ended sectors;
- Establish two categories of fund – regulated and registered – and remove the current requirement for principal managers. All funds, whether regulated or registered, would have to appoint a locally licensed administrator. Registered fund prospectuses would have to make it clear that the fund was not regulated by the commission; and
- Allow Guernsey service providers to offer services to non-Guernsey vehicles, subject only to a notification requirement to the commission.

The report reached several other significant conclusions. In particular, it was found that the fund-specific sector had been responsible for creating and sustaining a significant volume of employment on the island and contributing to Guernsey's profile in the international investment community. Consequently, it was understood that it was important to encourage and sustain the fund-specific sector.

It recognised the possibility of an "overheating" economy and noted that there needed to be a careful balance between the amount of administration to be undertaken in Guernsey and the level of administration that was permitted to be outsourced.

One key difference between the proposed Guernsey model and the model used in, for example, the Cayman Islands is that a Guernsey-licensed entity must retain responsibility for the conduct of the administration of each Guernsey fund. The Cayman model, which, if adopted, would have allowed



Paul Christopher specialises in investment, finance and corporate work. He regularly advises on the establishment of offshore investment funds and on the regulatory and commercial issues relating to them. Paul has an established trust practice and acts for several of the island's leading trust institutions. He joined Ozannes in 1999.

greater administration of Guernsey-domiciled funds to be undertaken outside the island, was rejected because of the impact it would have on:

- The economic benefit retained within Guernsey;
- The continued sustainability of Guernsey as an administration centre; and
- The reputation of the island where Guernsey-domiciled funds were administered by persons over whom the commission had no authority.

The good news is that moves are already taking place to alter regulatory policy to allow for these changes, and other amendments to the regulatory laws are anticipated shortly to implement the proposals. In February 2007, the registered fund regime in respect of closed-ended funds was implemented, and the policy requirement for there to be a principal manager incorporated and licensed in Guernsey for open-ended funds was reversed.

The report was keen to encourage growth in both the fund-specific and non-fund-specific sectors. In particular, the report considered it was important that the island attracted intellectual capital to move there and to establish ownership in Guernsey.

New-found confidence

Even before the implementation of the report, the influx of new funds – chiefly hedge funds, private equity and property funds, as well as traditional vehicles – to the island has been substantial. This is not only a reflection of global markets, but also the new-found confidence the sector has, as a result of the Harwood proposals.

For example, in 2006, the value of funds under administration and management increased 30.2% to £130.2bn. There is also a new trend in the establishment of businesses such as asset managers, stockbrokers and private wealth managers, driven by various factors. Again, the significance of the investment sector's regained sense of purpose should not be underestimated.

The streamlining of the authorisation and licens-



ing processes for the investment business sector will produce faster responses and enable the industry to react more quickly to the pace of the global commercial environment. The focus of attention by the regulator will move towards more frequent monitoring and review of the licensed service providers. This shift of emphasis will present its own challenges with service providers themselves being required to take an enhanced responsibility for the business they conduct to protect the reputation of the island (and their peers on the island).

As one service provider said recently: "It will be the case that, if one of us drops the ball, we all do." There will need to be a greater degree of dialogue between the industry – as a whole and as individual businesses – and the regulator, as there will be a shared responsibility.

To a large extent this is already starting to happen. These may be challenging times, but the future is very bright.

Stuart Dyer of Close Fund Services, suggests what clients should look for – and avoid – in their service providers

Serious about business

‘Excellent service at a competitive price.’
‘Sure, that’s what they all say!’ I can hear the sarcasm from here, and possibly warranted, given your own experience.

‘Providers of administrative service are a necessary evil in the value chain.’ Not, I hasten to add, a direct quote from a disgruntled client, but more a flavour of the perception that operations is the poor relation compared to the glamorous world of money management and marketing.

The one thing that we would all agree on is that failure in operational performance has significant impacts right through the value chain and material or continued underperformance gives rise to loss of reputation and loss of clients. Choosing the wrong provider is an expensive mistake, and can be seriously detrimental. So what should service providers, such as Close, be doing to enrich and fulfil your business?

The first thing to say is that being satisfied with the status quo is dangerous, both to the service provider and the hedge fund manager/promoter. Out there in the real world, clients are experiencing the entire spectrum of service quality, but some of it will be truly outstanding and, life being unfair, that is the standard against which many will be judged. Therefore, what may seem fine to a service provider may be irritating the life out of the underlying client.

The second key issue is the problem of success. General industry growth can reduce the amount of available talent as intellectual capital is spread thinly across providers. Hence isn’t there a chance that the available labour pool in the jurisdiction in which your fund is managed may suffer from restraints of access to genuine quality people?

So how does Close deal with this?

There is the standard operational stuff that every business does, but if there is no focus on the following points in addition, you need to ask some questions:

- Don’t simply measure everything that moves in the service relationship. Rather, focus on key performance indicators that really matter and

pursue their progressive improvement with a passion. The concept of service debits and credits may work wonders in this regard – never underestimate the power of greed.

- Continuous investment in technology. I have never been involved in an operational business that can survive without feeding this particularly voracious beast. New instruments emerge, trading processes evolve and, in general, the world conspires against zero development. In this regard, the demon Excel spreadsheet or the yellow sticky label is not really a viable alternative – watch out for these during your next supplier audit. If you do spot them, check the liability clauses in the administration agreement very quickly.

- Evidence of training and development programmes and excellence in staff is critical given the evolving industry.

Close Fund Services is committed to the long term growth and development of our specialist fund administration business. We are also committed to maintaining a powerful presence in our Guernsey location, an attractive place to do business from the twin viewpoints of its regulatory/legislative framework and skill base.

Local labour pool

However, the jurisdiction is proving so attractive that skilled resource is being spread quite thinly and, in our view, total reliance on the local labour pool to support growth is risky. Close is the only fund service provider in Guernsey to address this issue.

Faced with the competing forces of the growth imperative, a stretched local resource pool and the fundamental requirement to progressively improve service, a strategic decision was made to move elements of our investment accounting function outside Guernsey. Careful consideration was given to the factors that would be vital in achieving a successful outcome, and in retaining my job. We chose Cape Town, South Africa as the venue, for the following reasons:

- The availability of a highly skilled, competent



Stuart Dyer is the senior director of Close Fund Services and the executive chairman responsible for the Fiduciary Division of Close Private Bank Group of Companies.



and experienced labour pool. We are specialists in the more esoteric end of the investment administration spectrum and Cape Town, as a centre of investment management in South Africa, provides exactly the sort of individual that we seek, apart from the fact that they all appear to be at least seven feet tall. Further, Cape Town and the Eastern Cape provide a massive graduate population, a significant proportion of which have obtained the relevant degrees.

- Employment costs are attractive. Very much a secondary consideration, but nonetheless vital in the equation of progressively improving service at a competitive price.
- Good communications, both electronic and logistical.
- Compatible time zone.
- No language difficulties (well, almost none!)
- A 'developed world' economic model.

It goes without saying that South Africa grapples with a whole range of political and social issues. However, we were impressed with the way that major international businesses lived with and

managed these issues successfully, developing thriving businesses into the bargain. Our experience has been overwhelmingly positive and our assumptions, particularly around labour quality have proved right in practise.

The Guernsey Financial Services Commission publishes clear guidelines regarding the control of outsourced functions, including the requirement to maintain sufficient expertise in the island to ensure effective oversight.

Overall responsibility for the performance of the entire service remains with the local service provider in Guernsey. The guidelines make absolute common sense and, frankly, represent sound business practise.

Graduate training

So, what is the big deal and what's in it for our clients, both current and prospective? The answer is – plenty!

We are absolutely confident that we can support our growth plans while seeing additional benefits to service quality. The available skilled labour pool is significant and our graduate training programme will enable us to 'grow our own'

over time. Employment costs are such that our strategic imperative to drive up service quality over time will not come with increased fees. Rather, we are seeking to share the benefit with our clients, good news for both of us.

The one thing that we all know is, at some point, market conditions will change and life will get tougher; income will fall, there will be increased pressure on costs, holding onto clients will become even more important, service has to continue improving and there is much less cake to go round.

It is at times like this that you need a strong, long-term player as an administrative service partner. We believe our infrastructure and skills base put us in the position to truly deliver 'excellent service at a competitive price' and means we have a sustainable advantage over other fund service providers in Guernsey. We have positioned our business to provide the right service in good and bad times. Make sure that your service provider can demonstrate the same. If not, I can tell you right now that we are best placed to service your business, now and in the future.

Wayne Bulpitt of Active Group explains why establishing an investment management company in Guernsey has never been easier

Providing that helping hand

Guernsey has long been respected for providing high-quality financial services to a global customer base. This reputation, underpinned by a continual competitive updating of legislation, such as the recent Harwood review of investment sector legislation, has led to several hundred financial services businesses setting up on the island. These institutions have been attracted by Guernsey's many attributes, including its stability and security.

It is recognised that it is an increasing commercial necessity to ensure that where offshore centres are utilised, businesses must put in place an appropriate decision-making and support mechanism. The 24-square-mile island, which has a population of 60,000 and is situated 25 miles from France and 60 from England, has several advantages over other offshore centres:

- A business-friendly environment with no restrictions on the number of employees and no requirement to discriminate in favour of local staff;
- Legislative and physical independence;
- A British crown dependency, it is English speaking, uses Sterling, is in the same time zone as the UK and has good air links to London;
- A special relationship with the EU;
- Excellent infrastructure and professional support services;
- A high standard of living; and
- An open market for housing (or licensing opportunities for the local housing market).

A recent development in Guernsey has been the provision of practical and professional support services for companies in the financial sector. One such improvement is the 'incubator service', which has removed many of the traditional hurdles to the establishment, by a new business, of a physical presence in an offshore jurisdiction. This has been well received and Guernsey has witnessed a lot of progress in this area. These services provide a ready-made solution for those wishing to establish a financial services company on the island. The incubator service provides established support services including the provision of premises employing staff from senior managers to administration and secretaries, enabling a company to become quickly established.

Paving the way

Louise Hall, a partner at AO Hall Advocates, says: "The ability to move directly into a managed office equipped and staffed to a high standard eases the establishment of any new venture and adds to the attraction of Guernsey, not only as a centre where quality and efficiency come as standard, but also as a place where costs can be streamlined, because of the incubator service."

Serviced businesses can enter the 'incubator' with a longer-term strategy to evolve and establish their own independent location. In such instances, the incubator service provider continues to offer support once this has occurred.

Indeed, it is able to advise on and encourage such strategies to prepare serviced businesses to become independent to whatever degree they require.

Edward Moore, managing director of Aztec Financial Services (Guernsey), says: "Knowing that a specialised service provider is there, not only to handle our present needs to the same high standard with which they assisted with our establishment, but also to advise and assist us with our growing independence, is key to our long-term strategy."

Guernsey has never been more attractive to hedge fund managers who wish to establish a physical presence on the island. The investment sector legislation is being revamped, with the intention of building on several specific provisions made by the Guernsey Financial Services Commission (GFSC), thus ensuring it is able to support Guernsey's rapidly growing hedge fund industry. In June 2006, Guernsey agreed to a package, the main strands of which come into effect on 1 January 2008, that include, as standard, a zero rate of corporate tax.

In addition, Guernsey resident shareholders will be taxed on only distributed company profits. In terms of personal taxation, Guernsey residents will continue to be levied at 20% on assessable income but this will be limited to a maximum contribution of £250,000. There has also been a commitment not to introduce wealth taxes such as inheritance or capital gains tax.

The agreement to this package highlights the government's continued commitment to enterprise, and the finance industry in particular.

Furthermore, Guernsey's continuing development of the GFSC's rules and regulations has offered increasingly efficient and helpful guidance to the establishment of new funds. A streamlined and commercial approach to regulation has allowed the creation of self-certification-style fund set-ups, which offer a quick application turnaround for new fund business. Whether dealing with the management of locally authorised schemes, or the administration from within Guernsey of schemes outside of the island, business continues to develop. In all cases, the establishment of an 'incubated' serviced investment manager allows an efficient structure to be put in place to facilitate the obligations of the legislation and fund rules.

John Mills, of Dalton Capital (Guernsey), says: "A combination of legal advice and specialist compliance consultants on site and on hand to assist our business with its ongoing obligations and regulatory issues gives us the comfort that we remain compliant. Equally, we can equally utilise their expertise to plan strategies for our future business, including the requirements and expected timeframes of establishing new ventures."

The GFSC has implemented the high standards expected of the promoters behind new funds and management companies. Structures are required to be set up with a 'four-eyes management approach' and to implement policies and procedures governing anti-money laundering; compliance with fund rules; handling of complaints; gifts and hospitality procedures; disaster-recovery plans; and meeting legislative requirements on insider trading and data protection. Investment managers are expected to have agreements in place with local service providers and documentation evidencing their policies and procedures, as outlined above. The 'incubator service provider' not only handles the collation of information and production of documentation for an application to the regulator, but will advise on the practical aspects



throughout the application process, from informal approaches to the regulators to the submission of application forms and liaison with legal advisers.

GFSC approval

The GFSC recognises the merits of the incubator service. Service providers work closely with the regulators in a transparent and open environment in which creativity is important in the focus to develop a support industry which itself is not regulated, but in turn services the requirements of licensed businesses to the standard expected. This development has allowed a new wave of licensed entities to establish themselves in Guernsey, producing economic benefits for the island.

Incubator service providers employ compliance and administration specialists whose experience is key in the regulatory application process for companies to be licensed to conduct controlled activities and for funds, whether they are open-ended or closed-ended vehicles. Such specialist knowledge provides an efficiency welcomed by all sides and at all stages, from planning 'off the

wall' ventures to establishing traditional managers and products or meeting the obligations of regulators or the Stock Exchange.

Combined with the above, Guernsey's validation as a co-operative jurisdiction by respected international bodies including IMF, FATF and the OECD, and its co-operative approach to the adapting of international standards, make it the obvious location to base management companies and key staff.

The island's business-friendly environment and the availability of specialist support services make it the ideal location to incubate a presence.



Wayne Bulpitt established Active Management Services in 2001 to provide management and consultancy services to investment companies and funds. He was previously head of offshore investment services for

Canadian Imperial Bank of Commerce. Active Group provides professional and practical support services, including compliance, management, administration and consultancy to all sectors of offshore finance.

New registered funds regime

Peter Franks, head of audit for Guernsey and head of Ernst & Young's Channel Islands' Asset Management Practice, explains how the registered fund regime is making Guernsey more competitive

The Harwood report, which was published just over a year ago, saw members of the funds industry in Guernsey plus the regulator and the government sitting down with a blank sheet of paper to work out what legal and regulatory improvements were required in Guernsey to enable the continual growth of its investment funds industry.

The report came up with quite a few ideas as to how this could be achieved, one being the concept of registered funds. The registered funds regime reflects what can be done in other jurisdictions, where the due diligence on the promoter, the manager and the fund itself is performed by the service provider in that location. The service provider then submits the documentation to the regulator and within three working days the Guernsey Financial Services Commission (GFSC) will come back and give its consent to the launch of the fund.

The investment funds industry in Guernsey has faced a challenge in terms of the timing of the regulatory approval process where, in some cases, approval could take a few weeks. In the past, people were reluctant to build that amount of time into their launch schedule when they could go to other jurisdictions and maybe get it approved in a shorter time. Guernsey has now eliminated that particular disadvantage of doing business in the domicile.

It should be noted that this development does not represent an enormous leap in service provision for Guernsey. Historically, when managers have needed funds to be processed urgently, we have benefited from a co-operative regulator who has been agreeable to speeding certain documents through. The new registered funds regime applies only to closed-ended funds. The regulatory approval processes for open-ended funds will stay the same.

The approval process

The role of the designated administrator in this process is to liaise with the manager to ensure that the relevant documentation that's required for admission to the GFSC is obtained. The administrator must then review it to ensure the documentation is up to appropriate standards. A further responsibility exists to ensure the fund's manager meets the existing criteria for appropriate individuals and organisations entitled to come to Guernsey. The administrator will have to assess the qualifications and abilities of the individuals that are going to be sitting on the fund's board as well as managing the investment to ensure that Guernsey's reputation is protected.

In short, the administrator needs to be satisfied that the promoter is 'fit and proper'; that they have the integrity, solvency and competence for running the fund.



Peter Franks is head of audit for Guernsey and head of Ernst & Young's Channel Islands' Asset Management Practice. He is also the Channel Islands' representative on Ernst & Young's European Asset Management Network, Global Hedge Fund Executive Committee, Global Hedge Fund IFRS Committee and Global Asset Management IFRS Policy Committee.



Whereas it appears that administrators are taking on a responsibility for establishing the above burden of proof, it should be said that Guernsey administrators have, in the past, usually done a good job of ensuring appropriate documentation is compiled before the client submits to the GFSC for consent to establish a closed-ended fund.

A faster process

The lead time involved in establishing this burden of proof will depend on the background research that is required of the administrator and the availability of this background information. In addition, they will be dependent on the relevant documentation being supplied in a timely manner.

It is important, going forward, that managers who are thinking of launching a new Guernsey fund are in contact with the administrator upfront. This is necessary to reach an agreement on what the documentation and reporting requirements are with the administrator and to ensure that everyone is clear as to the timetable of compiling the relevant documentation and materials.

We will probably see a shorter process for some organisations, compared to the work being carried out by the regulator, simply because there are probably more resources resting with the administrators than reside in the GFSC.

In addition, administrators will have more flexibility in resourcing, which means they will be able to ensure that they are prioritised in the appropriate manner.

Registered funds have already engendered a lot of interest and a few funds are going through the regulatory consent process already. There is a lot of interest in the wider funds community and many new funds in the pipeline. Given that the regime only became effective on the 1 February, the promotion of registered funds has been moving out into the investment funds world quite quickly and will be one of the main areas of growth for Guernsey over the next 12 months.

The role of the CISX

Whereas these funds can be listed on the CISX, wider listing depends on the requirements of the individual exchanges. It is our understanding that registered funds will not be able to be listed, for example, on Euronext, which has been one of the key listing locations for Guernsey vehicles over the past 12 months. This is due to the fact that these funds are not subject to a full regulatory review process before they are launched.

The key issue with the CISX is its speed in enabling organisations to get listings and its pragmatic approach to the documentation you are required to submit. The flexibility in the accounting standards organisations are allowed to employ in Guernsey, as well on the CISX, means that some people have taken the opportunity to use US GAAP – an option that may not be available to a group wanting to list on an EU-regulated exchange.

It is also very cost-effective to have a CISX listing. For example, to list on

the London Stock Exchange (LSE) you need to engage a reporting accountant to review the working capital report, you need to do a review of the financial reporting procedures of the group and you may need to look at the tax disclosures within the prospectus. There is also a potential need, if it's a company that's been operating for a while, to produce what is called a 'long-form' report. These documentation requirements of the LSE don't actually exist under the CISX listing process; therefore you save time and a lot of money not having to engage many different service providers.

Growth areas: listed funds

The phenomenal growth of listed funds in Guernsey over the past 12 months has been boosted in particular by the size of some of the new funds coming in: KKR, raising US\$5bn; Apollo Investment Management, with a Euronext listing, raising US\$1.5bn and several others, including Marshall Wace, which is also raising billions of dollars' worth of new capital. These permanent capital vehicles are proving very popular in Guernsey at this point in time.

This trend is reflective, from the Euronext perspective, of the GFSC having engaged in a memorandum of understanding with the Dutch regulator going back several years. Guernsey was able to use that memorandum to get approval from the Dutch listing authority, the AFM, that the island has a well-regulated jurisdiction and that therefore a Guernsey-regulated product could be listed on the Dutch Euronext.

This means that we have in Guernsey an EU-listed product using an offshore vehicle, which has proved popular with US promoters and managers of funds. We've even seen limited partnerships being listed on the Euronext exchange, which is not necessarily available on other exchanges in Europe.

We are also seeing in Guernsey the next evolution of funds. Many funds are now going for London Stock Exchange listings, using the secondary listing options under the Chapter 14 rule. There continues to be a lot of interest in the Guernsey product, but linking it into an EU listing.

Chris Gambrell of Praxis Fund Services says that Guernsey continues to attract new fund managers in a wide variety of shapes and sizes

Taking the bait

With the background of a well-regulated, established jurisdiction that is close to the European financial centres and that enables fund managers to exercise off-shore management and control, Guernsey offers an attractive package to new fund business.

As well as a well-established infrastructure, in terms of administrators, custodians, lawyers, bankers and accountants, the jurisdiction has implemented some enterprising regulatory enhancements to attract new fund managers. The qualifying investor fund (QIF), that was introduced two years ago, there registered funds regime that is already applicable for closed-ended funds, and the new proposed regulated funds regime all indicate a proactive quality in Guernsey's approach.

Looking back even further, the island was the first jurisdiction to have PCC legislation. And, of course, the Channel Islands Stock Exchange is also based in Guernsey.

Fast track fund application

The registered fund, although currently only applicable to closed ended funds, resembles the QIF, which can still be applied to open ended funds. It enables us to submit a new fund application to the Guernsey Financial Services Commission (GFSC) and to receive approval within three working days. This is achievable through the certification of the parties involved being undertaken by the administrator.

The administrator is separately reviewed by the GFSC to see that their controls and procedures in adopting these application methods on behalf of their clients are reliable. The relative novelty of the closed-ended fund

regime means that, despite the streamlined authorisation process, the number of funds registered has not yet reached a significant level.

Having worked on a substantial number of QIFs in the past, for which the application processes are virtually identical, we have previously experienced impressive turnaround times, with some funds even being granted regulatory approval within a day. Praxis Fund Services is working on our first registered fund.

The self-certification regime for QIFs has also proved very successful in attracting hedge fund business to Guernsey, as well as being used extensively for property and closed-ended funds. One of Praxis' largest clients is a fund of hedge fund manager who was specifically attracted to the domicile by the fast track qualifying investor fund regime.

Tax benefits

The tax structure is always a part of the package for offshore domiciles, so long as it can be demonstrated that the fund is controlled and managed from Guernsey.

This typically involves: careful structuring at the fund launch stage; a majority of offshore resident directors constituting the board; frequent and properly minuted board meetings evidencing the decision-making process taking place in Guernsey; and perhaps an offshore domiciled fund management entity enabling certain marketing, compliance and accounting activities of the manager to be performed.

From an investor perspective, Guernsey is attractive as, unless an investor is resident in Guernsey, then they too, like the fund, will suffer no Guernsey tax.

Channel Islands Stock Exchange

Another draw for new fund managers is the Channel Islands Stock Exchange (CISX). The exchange is a proactive and go-ahead organisation offering competitive listing fees.

The application process is extremely efficient, which gives certainty to clients looking to list on the exchange. You only have to look at the statistics for the stock exchange's growth – 2007 is looking like another record year – to see that it has a continual upwards chart.

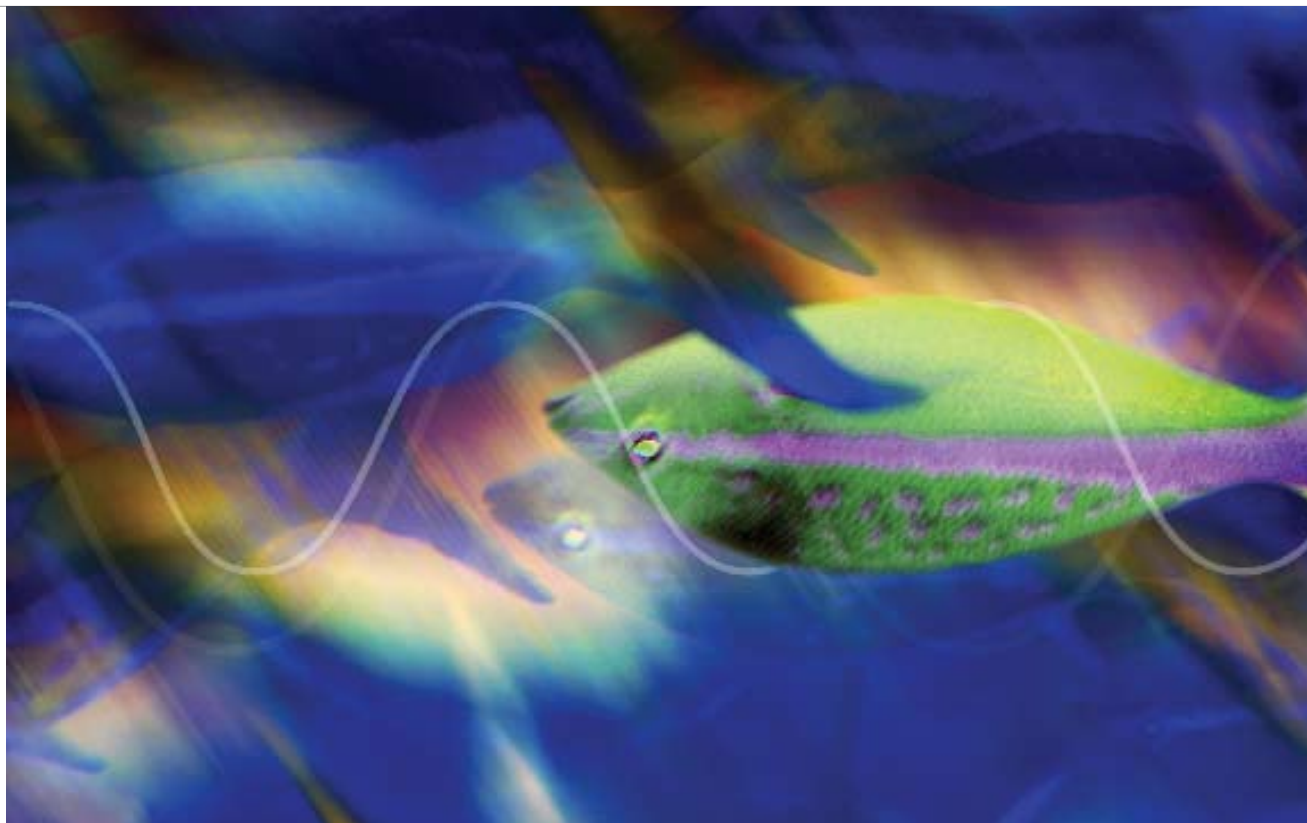
It is a good 'one-stop-shop' selling-point to hedge fund managers to say that in Guernsey, we have got the administration, the lawyers, accountants and other service providers – and we've got the CISX.

The CISX is more of a technical listing than a trading listing, of course. Accordingly, funds may decide to dual list between the CISX and AIM.

The trade-off in Guernsey's favour is that AIM is not a recognised stock exchange for Inland Revenue purposes, whereas the CISX is recognised by not only the Inland Revenue but also notably the FSA and SEC, among others. Hopefully, we will see other market participants make more of a market with the CISX.

London-listed Guernsey funds

With Guernsey's long track record of dealing with London-listed funds, one of the trends that we have seen in recent months is the attraction of several fund managers whose hedge strategy may involve slightly illiquid assets. In an open-ended arena, this makes liquidity management quite difficult because of the possibility of redemptions – and the knock-on effect those redemptions have on the illiquid assets.



We are seeing a significant number of funds coming to Guernsey and creating a closed-ended fund which then lists on the London Stock Exchange or even AIM. Being closed-ended aids that liquidity management because there are not going to be any redemptions. Because it is a London-listed fund, it also helps the profile of the manager. This is proving attractive for both fund of hedge fund managers and certain hedge fund managers as well as other illiquid asset class fund managers.

Outsourcing of services

The outsourcing of services is undeniably something that is happening from Guernsey. There are various pros and cons in this debate, but Guernsey needs to look to outsourcing simply because the demand for fund product is very high.

The crucial issue with outsourcing is making sure you retain total control over the outsourcing – be it a segment of your own organisation that you have established in another jurisdiction or some form of third party. From the clients' point of view, you have to make this relationship and process seamless. The client will want to telephone someone in Guernsey to ask questions and seek advice – they will not want to phone someone in another part of the world.

We must also ensure that responsibility for Guernsey funds, regardless of where certain administrative tasks are undertaken, remains in Guernsey. In this way we can best protect the reputation that Guernsey has developed as well as ensuring that there is a seamless service for the fund manager.

Praxis Fund Services Limited

When you first knock on the door of prospective clients, there are factors that distinguish Praxis. One is that the business is owner-managed. Most boutique-type investment management companies are also owner-managed, so they can appreciate what that concept involves.

They can also understand our very short 'decision tree'. If you are a smaller organisation, you do not have to go through various other offices within the group simply to make a decision about doing the business.

We are more of a niche personal-based organisation and that is often synonymous with how some of our clients run their business, as well. There is a commonality of approach to how we do our respective bits of the job.

Consequently, we can react to a client's issues that much faster, not only at inception, but throughout the life of the fund.



Chris Gambrell is the Managing Director of Praxis Fund Services Limited. He has been involved in the Guernsey offshore fund industry for over 15 years and has recently worked on the establishment of property, hedge and private equity funds. Chris is a chartered accountant.

William Simpson of Ogier explains the three paths to consent for closed-ended funds

Full speed ahead

Consent for the establishment of a closed-ended investment fund in Guernsey is obtained under the Control of Borrowing (bailiwick of Guernsey) Ordinances (COBO). On 1 February 2007, a new fast-track procedure was introduced for closed-ended investment funds. This procedure has been adopted in response to a recent report which reviewed legislation and regulation of Guernsey's investment business sector. Consequently, there are now three procedures that may be followed to obtain COBO consent for a closed-ended fund:

- The 'normal' procedure, which involves outline, interim and final consent;
- A 'fast-track' procedure for qualifying investor funds (QIFs); and
- A new 'fast-track' procedure for 'registered' closed-ended investment funds ('registered funds').

QIFs and registered funds are fast-track procedures in the sense that it cuts the time spent by the Guernsey Financial Services Commission (GFSC) in reviewing the fund and its promoters. Following submission to the GFSC of all necessary documentation, and subject to compliance with requisite matters, COBO consent should be given in about three working days. This is in contrast to the 'normal' procedure, which can take weeks.

Qualifying investor funds

A QIF is identified as such by virtue of restrictions placed on the type of investor permitted to invest in the relevant fund. They can be either a closed-ended or open-ended investment fund, but only qualified investors are permitted to invest in them. Essentially, a 'qualified investor' is someone who is deemed able to evaluate the risks and strategy of investing in a QIF, and to bear the economic consequences (including the possibility of any loss arising) of such an investment. A qualified investor is either a professional investor – an individual who makes an initial investment of at least US\$100,000, or its equivalent – or an experienced investor, who is a knowledgeable employee of a qualified investor.

Warranties must be obtained from prospective investors in a QIF to the effect that they meet the

requirements of a 'qualified investor', to ensure that the restrictions are met. At the time of application for COBO consent for a closed-ended fund, the relevant administrator of that proposed fund must warrant to the GFSC that, among other things, effective procedures are in place to restrict investment in that fund to qualified investors.

Registered funds

A closed-ended investment fund that is not offered direct to the public in Guernsey can apply to become a 'registered fund'. The administrator of the proposed fund is required to give a warranty to the GFSC that effective procedures are in place to ensure such an offer is not made in Guernsey.

Importantly, a registered fund is not required to impose restrictions on the type of investors permitted to invest in the relevant fund. This difference from a QIF may be relevant if the fund is considering listing. A listing authority may not allow an entity to be included on its official list where that entity has restrictions on potential investors. This is a potentially limiting factor for a QIF.

Promotion of registered funds

The administrator of a registered fund must certify that it will not be offered direct to the public in Guernsey. In this regard, the GFSC has previously provided detailed guidance on what it considers is permissible promotion in Guernsey. Broadly speaking, the GFSC allows passive promotion, but not active. In this respect, a registered fund:

- Can be listed;
- Has no minimum subscription limit;
- Can be promoted to any entity or person licensed under the Banking Law, Protection of Investors Law, Insurance Laws or Fiduciaries Law in Guernsey;
- Is not permitted to directly advertise in the Guernsey press; and
- Can respond to requests for information by any individual or entity in Guernsey.

Administrator's role

Where the normal COBO consent procedure is followed, the GFSC will undertake due diligence



William Simpson is a partner and head of Ogier's Guernsey office. He specialises in investment funds, structured finance, banking, corporate and commercial work, and trusts. Simpson, who is a qualified barrister, has been on the island since 1991. He joined Ogier in 2002 and featured in the 2006 edition of *Who's Who Legal* for private funds.



and determine whether the promoters are 'fit and proper', as set out in GFSC guidelines. However, where either the QIF procedure or the registered fund procedure is used, the administrator undertakes due diligence of the promoters and, once satisfied, it warrants to the GFSC that the promoters and associated partners are fit and proper.

The QIF or the registered fund regime might be preferred to the normal closed-ended procedure if the promoters of the fund are known to the administrator. Even if they are not, the administrator may be able to undertake those checks more quickly than the GFSC.

The background checks on a promoter that an administrator must carry out are similar for a QIF and registered fund. The normal closed-ended procedure places with the GFSC the responsibility for due diligence in relation to the promoters of the fund.

The GFSC places great reliance on the certification of the fund by the administrator. Should an administrator not provide satisfactory certification, it is likely that the administrator will not be permitted to participate in the QIF or registered fund regime.

As the onus is on the administrator under both of the fast-track procedures, its fees will reflect this work.

Licensing of fund's service providers

Irrespective of which COBO consent procedure is adopted for a closed-ended fund, a fundamental issue to be taken into consideration for the launch timetable is whether any of the fund's service providers require a regulatory licence.

For example, in the context of a limited partnership, a new general partner must obtain a licence under the Protection of Investors (bailiwick of Guernsey) Law 1987 (the POI Law). If a general partner does not already hold a POI

licence, it must obtain one prior to seeking COBO consent for the fund itself.

The time required to obtain a POI licence will depend on whether the beneficial owners of the prospective licensee are already known to the GFSC. If they are not, then the GFSC will undertake due diligence. Enquiries should be made, on a case by case basis, to get an idea about the time it is likely to take to obtain a licence.

Over time, it is expected that registered funds will replace QIFs as the preferred 'fast-track' procedure for Guernsey closed-ended funds. This is primarily because a registered fund is not required to impose restrictions on the type of investors permitted to invest in them. However, the QIF procedure will remain the only 'fast-track' one for the authorisation of Guernsey open-ended investment funds, and it is in this context that it will remain an important process to expedite applications.

Patrick Firth of Butterfield Fund Services (Guernsey) says recent self-certification schemes for funds have naturally led to a rise in business on the island

Take a flexible approach

Guernsey's proximity to European markets, particularly the UK, continues to attract new fund managers to domicile on the island. The ability to list on the London Stock Exchange, AIM and the Channel Island Stock Exchange, which is increasingly being used as an alternative to Dublin, is an added inducement for new and existing funds business to use Guernsey as a base of operations.

Certainty to approval process

Guernsey's standard of regulation is high, but the regulator here is still seen to be approachable and flexible in its working practices. The launch of the qualifying investor fund (QIF) regime and, more recently, the registered closed-ended fund regime, which happened in pretty short order, have also helped to boost Guernsey's reputation.

In particular, the self-certification schemes in place for both the registered funds and QIFs have helped to add certainty to the approval process. Fund managers who are ready to take a fund to market do not want to be kept waiting if they have got investors already lined up. When managers are out marketing to prospective investors they need to be able to say to the day when the fund will be ready, rather than hoping it will be ready in two or three weeks, depending on the regulator.

Now managers and administrators

know that it's going to be turned around in three days, from submission of the application. This may not necessarily speed up the overall process significantly, but the measure of certainty is key. It is important at that stage in the launch for all parties to have a defined completion date. This still allows for a certain amount of time for the self-certification – for the administrator to perform all the due diligence and for all parties to get the product into the required shape. Previously, that process used to occur at the same time as the Guernsey Financial Services Commission's authorisation. It is better for all parties and for the jurisdiction as a whole that we now have this certainty.

The number of QIFs being set up is increasing all the time. When the regime was first introduced there was no minimum investment requirement but the subsequent introduction of a US\$100,000 limit has been a necessary part of the self-certification process.

Provision for outsourcing

Previously, applicants for this type of fund would have been required to meet a number of criteria to prove that contributors to the fund were qualifying investors. Now, so long as investors are investing more than this amount then you can rightfully assume that they are deemed to have done so.

With the significant increase in the number of funds coming into Guernsey



Patrick Firth is managing director of Butterfield Fund Services (Guernsey) Limited. He qualified as a chartered accountant in 1990 and is a member of the Securities Institute. Prior to joining Butterfield Fund Services Limited in 2002 he was managing director of a large fund services company in Guernsey administering both offshore and onshore (FSA regulated) funds.

it is inevitable that some degree of outsourcing will have to take place. Provisions for outsourcing have been in place for quite some time, with the rules governing the practices originally being introduced at the end of the 1990s and revised a couple of years ago. The framework of regulatory oversight of outsourcing is there for administrators who wish to take advantage of it.

As a company, we look at outsourcing on a case by case basis – we do not generally outsource, but we will in certain cases. If we have a significant client who already has a tried and tested outsourcing structure in place then we are quite comfortable working with that. There are certain things that we would not outsource, however – our corporate secretarial work, for instance, is all done in Guernsey, for reasons of control.

Aimed at hedge funds

Providing corporate secretarial services to hedge funds is an area in which Butterfield specialises and is one that has gained in importance as hedge funds move towards the mainstream. Such services are aimed specifically at boards of funds for which we provide other aspects of administration not as a stand-alone service. Butterfield offer full facilities for board meetings at our St Peter Port offices, with a member of our corporate secretarial team in attendance. The service includes the preparation of board packs, preparation of reports for board meetings and any associated work. This aspect of our work is necessarily proactive.

Butterfield also provide services for the audit committees for listed funds and have the ability to support board facilities in other areas of the world where fund sponsors are located. Our corporate secretarial team are ready to attend the hedge fund board meetings wherever they take place.

These services to the board are becoming more in demand as the corporate governance requirements are becoming increasingly important. The board's level of control has to become more clearly documented and evidenced. As corporate governance becomes more important, the corporate



secretarial department supporting that will consequently grow.

The rise in the numbers of boutique administrators in Guernsey is, in our view, a natural progression – partly as a result of the significant increase in business coming to the island. The island has a substantial quantity of very skilled and knowledgeable people within the island, who have been working in the industry for quite some time.

Innovative new products

Guernsey has always been innovative, especially in bringing out new products, and boutique administration is just one of those innovations. Over the years we have had the Guernsey limited partnerships for private equity; open-ended investment companies were set up in Guernsey some time before other jurisdictions and PCCs were set up here first as well. As these products are rolled out then naturally all the administrators will provide niche services.

Butterfield are a large enough player to provide all the benefits that concept brings with it. We are in Guernsey, Bermuda, Cayman and Bahamas. As an overall group we have the critical mass.

We put a lot of emphasis on working with advisers and sponsors in setting up funds and we work with our clients to provide more of a tailored solution. We administer a breadth of funds and that gives us a corresponding breadth of experience.

As part of a larger organisation, with the support of the bank offering foreign exchange, lending/banking services and also custody, we can also offer a better solution, working with our sister companies, to provide an offering to customers. On the other hand, we do not insist on doing that, so if clients wish to use other providers for the other services then they can do so.

Butterfield's flexibility, from running a wide range of different types of fund, means that we are in a good position to accommodate the increase in closed-ended business coming into the island, in line with the general trend. There is more private equity business coming in as well, and we have become involved with that.

Finally, we do a lot of work providing services for family offices – a number of the funds being introduced to us are coming from that route.

Sean Cheong of Collas Day examines registered closed-ended investment funds

Still competitive

In recognition of the need to remain competitive in the international market, Guernsey recently introduced the concept of registered funds. This is essentially a fast-track process of authorisation, with a three working-day turnaround time, for certain closed-ended investment funds. This new process has been in place since the start of February, and so far, four registered funds have been established.

Structuring a closed-ended fund

As with any investment fund, the usual ways of structuring it – through corporate vehicles, limited partnerships and unit trusts – are compatible with the registered funds regime. In relation to corporate vehicles, Guernsey can also offer structuring possibilities to potential promoters, which involves the use of protected and incorporated cell companies.

It should be noted that registered funds may not be offered directly by the issuer to the public within Guernsey, but may be listed, for example, on the Channel Islands Stock Exchange. The registered funds process may not be suitable in the case of funds seeking listing in a jurisdiction where a greater degree of regulation is required from the home regulator, in this case, the Guernsey Financial Services Commission (GFSC).

The process

This new regime is a simplification of the current procedure. The GFSC will require an appropriately licensed Guernsey service provider to be appointed to act as administrator of the fund. The administrator must certify to the GFSC that:

- It has performed sufficient due diligence to be satisfied that the promoter and associated parties are fit and proper;

Everything you need to know about PCCs and ICCs

What is a protected cell company (PCC)?

The most notable feature of a PCC is that it remains a single legal entity, but with separate and distinct cells.

The assets and liabilities of one cell are kept separate and protected from the assets and liabilities of the other cells, as well as from the PCC's non-cellular assets and liabilities. Consequently, the assets of a single cell are available only to the creditors who are creditors in respect of that specific cell.

Importantly, the PCC is a legal framework by which recourse is limited by law, not simply by documentation. Although a PCC may create one or more cells, the PCC remains a single legal entity and the creation by a PCC of a cell does not create in respect of that cell, a legal entity or person separate from the PCC itself.

What is an incorporated cell company (ICC)?

An ICC is a company which houses within it incorporated cells (each an 'IC') that are companies within their own right. Unlike a protected cell company, which has separate and distinct cells whereby the assets and liabilities of a cell are legally segregated from those of other cells, each IC is ring-fenced by virtue of its separate legal existence, apart from other ICs and the ICC itself.

Other than certain regulated businesses, there are no restrictions as to the type of companies which can be established as, or converted into, ICC or ICs.

- Effective procedures are in place to ensure that the fund is not offered directly by the issuer to any person not regulated under any of Guernsey's financial services regulatory laws within the bailiwick of Guernsey; and

- The status of the registered fund is specifically referred to in the offering document such that neither the GFSC nor the States of Guernsey Policy Council has reviewed the offering document and that neither the GFSC nor the States of Guernsey Policy Council takes any responsibility for the financial soundness of the fund or for the correctness of any of the statements made or opinions expressed with regard to it.

Registered funds will have to comply with the minimum prospectus disclosure requirements required by a

proposed generic 'prospectus' law. Until this legislation is implemented, it is proposed to utilise the existing disclosure requirements for closed-ended investment funds seeking consent under the Control of Borrowing (bailiwick of Guernsey) Ordinance, 1959 (as amended).

Registered funds will be required, through their administrator, to make an initial filing with the GFSC and to submit notifications in respect of changes to the fund, together with annual financial statements and quarterly statistical information. The administrator would be required to certify that it has undertaken due diligence on the fund's promoter.

There should be a standard rubric to be incorporated on any offer document issued by a registered fund and also in its annual report and accounts to the



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effect that the fund is registered and that the GFSC has relied upon specific warranties provided by the administrator when issuing the relevant consent under the Control of Borrowing Ordinance.

Promoter and/or investment manager

The promoter and/or investment manager of a proposed registered fund must be an institution which is in good standing. In other words, neither the institution itself, nor its directors, controllers or senior management, has been the subject of a material disciplinary action, or conviction, in the previous five years.

The administrator must certify that they have performed sufficient due diligence on the promoter and/or investment manager so as to be satisfied that they have the necessary integrity, solvency and competency, as set out in GFSC guidelines. The administrator must also document their findings.

Applications on behalf of new promoters and/or investment managers will also be considered.

In such cases, the administrator will need to consider the track record, experience and employment history of the controllers, directors and management of these entities, and show that it is relevant in relation to managing investors' funds, using similar investment strategies to those that will be adopted by the registered fund.

Once a fund has been registered, the GFSC assesses the due diligence that an administrator has gathered on a post-facto basis, and insists that such due diligence must be updated regularly.

With the introduction of this new regime, applications for approval of closed-ended investment funds may now be made in one of three ways:

- The registered funds regime briefly described above;
- The three-stage consent process by which the GFSC assesses the application in detail – the more traditional application and considerably more time-consuming process, which, in time, may become less popular as pro-

motors are able to target more defined classes of investors;

- The qualifying investor funds regime, which is restricted to investment funds aimed at professional, experienced and knowledgeable investors, as defined by the relevant rules.

Application to hedge funds

The new registered fund regime will be of considerable assistance to promoters wishing to set up a fund quickly. This will enable hedge funds and private equity funds to establish new vehicles with the benefit of Guernsey's excellent infrastructure and experienced service providers.

| Comparison of ICCs versus PCCs | | |
|---|--|--|
| | ICC | PCC |
| Single legal entity | Yes | No |
| Segregation | By law | By separate legal entity |
| Setting up new cell | Board resolution only | Special resolution of members |
| Registration of new cell at Companies Registry | Not required | Registration required |
| Memorandum and Articles | Only one set required for whole PCC | Separate Memorandum and Articles required for each ICC cell |
| Contracting between cells | Cells can make 'arrangements' with other cells akin to contracts | Cells can contract with other cells |
| Can cell spin off to stand-alone company? | No | Yes |
| Consolidation of accounts | Cell accounts and consolidated PCC accounts required | Can have separate cell accounts and ICC or consolidated accounts |

Martin Tolcher of Legis Fund Services looks at the implementation of new regulations for Guernsey funds from an administrator's perspective

It's all change

The working party chaired by advocate Peter Harwood, which published its report in June 2006, made several recommendations pertaining to the simplification of fund registration. In January 2007, the Guernsey Financial Services Commission (the Commission) confirmed that, with effect from 1 February, 2007, new regimes would be put into place for:

- Registered closed-ended investment funds; and
- Principal managers.

This article considers the practical consequences and positive benefits of these changes, particularly from a Guernsey administrator's perspective.

Closed-ended investment funds

To date, closed-ended, as well as open-ended, investment funds in Guernsey have been subject to regulation (and regulatory consent) by the Guernsey Financial Services Commission (the Commission). The new regime in respect of the registration of closed-ended funds makes several fundamental changes that accelerate the consent process.

■ Responsibility

Under the new regulatory regime, rather than the Commission being responsible for the approval of the promoter, investment manager and prospectus or offering document of the fund, the onus falls upon the Guernsey administrator.

Thus, before submitting the relevant documentation to the Commission, the administrator must undertake sufficient due-diligence enquiries and checks on the parties referred to above, in accordance with the Guidance Note, dated February 2007, in respect of registered closed-ended investment funds issued by the Commission.

As administrators, we consider it of paramount importance for the introducers of new business to Guernsey (for example, fund managers) and/or their advisers to look to appoint, and involve, the Guernsey administrator early in the establishment process, rather than considering and determining the appointment just prior to making a submission to the Commission. In this way, the administrator, with the valued assistance of the Guernsey lawyers, can begin its due-diligence processes so that it is positioned to make the application to the Commission when required.

It is also incumbent upon the administrator to ensure that the fund will not be offered direct to the public within the bailiwick of Guernsey. Further, it needs to satisfy itself that the prospectus or offering document contains adequate disclosures.

■ Streamlined approach

Once the administrator is comfortable that it can report positively with respect to all of the above aspects, it can then submit duly completed documentation to the Commission. In effect, the same documentation needs to be included with this submission that would have been completed and dealt with historically by the Guernsey lawyers when seeking approval for a regulated fund, namely:

- i) Forms GFA and APC;
- ii) Form PQ for all relevant individuals; and
- iii) Certified final copies of the prospectus or offering document, application or subscription form, constitutive documents and all material agreements.

Additionally, the administrator must make three declarations, formally

confirming that it has done the tasks referred to in the paragraphs above.

■ Certainty

Perhaps the change of most immediate interest to the introducers of fund business to Guernsey is how long it takes the Commission to give the necessary consent. This remains up to six weeks for regulated funds. For registered funds, the Commission will issue the necessary consent under the Control of Borrowing Ordinance within three working days of receipt of the Form REG and accompanying documentation.

In the short time since the process has been introduced, reaction has been positive. This was illustrated at a seminar in London in March hosted by GuernseyFinance and the Guernsey Investment Fund Association, which was well attended by fund industry practitioners.

In summary, the features and benefits of this regime for registered closed-ended investment funds are:

- Responsibility – now placed upon the administrator to review;
- Streamlined application – a one-stage process, rather than the previous three-step one; and
- Certainty – once documentation has been submitted, consent is given within three working days.

Principal manager

Historically, it has been necessary for open-ended funds domiciled in Guernsey to have a locally based principal manager, traditionally 'run' by the Guernsey administrator, ensuring that the decisions (or recommendations) of the onshore investment manager/adviser are replicated within Guernsey.

The removal by the Commission of the requirement to have a principal



manager enhances the ability of the structures to have greater flexibility, as well, of course, of reducing the overall fees and costs of running such an entity.

However, it is interesting to note that there remains a trend among fund managers to establish a Guernsey principal manager, with a physical presence on the island. This may be considered to be driven, at least in part, by the need to demonstrate that mind, management and control are being exercised offshore from a UK, or other jurisdictional, tax perspective. This gives rise for further opportunities for Guernsey administrators to assist in this regard.

Specifically, not only can the Guernsey administrator provide all aspects of administration to the principal manager, but also dedicated office space, communications and employee resources. Increasingly, enquiries are being made to determine what appears to be perceived as a cost-effective way of beginning to establish a full physical presence of the fund manager in

Guernsey, with the ultimate aim of moving the successful individuals responsible for the investment management decision-making process to Guernsey, establish an office and employ staff for that company.

Conclusion

The above changes illustrate the continued importance of the role of the administrator for funds to be serviced from Guernsey. It is needed not only after a fund has been launched to provide ongoing administration services, but also at the outset, thus enabling the Guernsey funds and linked management companies to be established and authorised in the most efficient manner.

These two new regimes further demonstrate the desire of the fund industry in Guernsey to move forward in enhancing its share in an increasingly competitive marketplace. Allied to this is the responsive, pragmatic and flexible approach of the Guernsey Financial Services Commission, thus enabling the

necessary changes to be implemented in a timely and efficient manner.

Guernsey remains a jurisdiction in which there is a high skill base among the specialist administration providers that continues to engender confidence among the introducers of new business. These changes enable such introducers of funds business to see why Guernsey should remain high on their list of jurisdictional locations where their funds can be domiciled and managed in one central location.



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Cayman and the British Virgin Islands, from its offices in Guernsey. He is a member of the Securities Institute and has been involved in the fund administration industry in Guernsey for 20 years.

Kevin Gilligan of Louvre Fund Management explains how boutique fund administrators have begun to make their mark

Boutiques want to hold your hand

Ever-changing, forward-thinking legislation and increasingly straightforward regulations are making it easier to establish new funds in Guernsey. The introduction of the protected cell company (PCC) concept, the success of the qualifying investor funds (QIFs) and the Harwood Report provide adequate illustrations of this in recent years.

The rationale of the Guernsey Financial Services Commission (GFSC) is obvious – make it quick and easy, and more fund business will be attracted to Guernsey. The manner in which it has been achieved has also been important because the Commission has done it through close dialogue with the fund industry, ensuring that everyone is inside.

The figures speak for themselves: the GFSC reported funds under management and administration for 2006 of £130.2bn. This represented a year-end high and a 30.2% increase over the year. Also of interest is that non-Guernsey schemes for which some aspect of Guernsey administration or management was provided increased in value by 21.2% to a new high of £25.1bn.

These figures reflect an important, and perhaps unexpected, spin-off from the continual and dynamic changes – they have encouraged the evolution of the boutique fund administrator.

Boutiques have always been around, but the intense and rapid changes to the regulatory environment in recent years, together with the high costs of compliance and corporate governance, priced them out of the market. Arguably, there was a period of consolidation in the market that saw the boutiques swallowed by the larger corporations, while the industry took stock of the impact of the legislative and regulatory changes.

However, several years on, the constructive manner in which the regulatory authorities have

managed to relax the rules, while maintaining their robustness and efficacy, has encouraged the re-emergence of the boutique administrator, as the industry's entrepreneurs seize the opportunity.

So, what does the boutique fund administrator offer that large institutions do not? Primarily, a boutique such as Louvre Fund Management offers a friendly, hand-holding service. We do not provide custody, banking or legal work. Instead, the boutique offers a closer relationship and a single point of contact with a specialist administrator. They, in turn, will work with the manager and advisers to the fund or recommend appropriate service providers in Guernsey. In doing this, they offer choice and take on a crucial co-ordination role.

The boutique is also an advantage to smaller, perhaps less experienced, fund managers. Larger, more experienced institutions go straight to the large Guernsey institutions because they require the full suite of services. They will be looking for custodial, legal, banking and accounting services as a one-stop, often fee-negotiable, package.

However, the smaller manager may require an initial consultancy process during which the more personal boutique, such as Louvre, can guide the manager through the options available for their needs. Maybe they need a cell in a PCC, to follow the QIF route or to establish a limited partnership. Whatever the requirement, boutiques such as Louvre co-ordinate, advise and follow the process through to the establishment of the fund.

What follows from the boutique is the provision of a bespoke and personal administration service meeting the precise needs of the manager – whether a specialist fund manager or one who has all of the other services on tap already and simply needs administration of the fund to be demonstrably in Guernsey.



Kevin Gilligan is an associate director of Louvre Fund Management, with responsibility for the day-to-day operation of the company and its clients. He joined five years ago, bringing with him asset management expertise. Gilligan has been instrumental in the establishment and development of the fund administration business.



The importance of this last point cannot be over-emphasised, particularly for many UK and European fund managers who have suffered increased scrutiny from their regulators in recent years. The principal reason for this is the taxation perspective.

The UK revenue has included the offshore funds sector as part of their 'special arrangements' initiative and investigations, and their focus is on identifying the 'true' jurisdiction of management and control. Clearly, they hope to show that the fund is UK resident and therefore liable to tax there.

Using a boutique that can offer qualified and knowledgeable non-executive directors to the board and, importantly, hold regular and frequent board meetings to demonstrate administrative knowledge and control, is crucial. They will also be closer to the manager and have a greater depth of understanding of the underlying business. In short, they will be more involved.

It is also worth highlighting Guernsey's proximity to the UK and Continent, which allows directors based elsewhere to attend regular board meetings.

The rise in Guernsey of the small specialist boutique administrator and manager reflects the success of the island's fund industry. They are a response to the needs of the growing number of alternative fund managers and they reflect the depth of experience and expertise that is available on the island, as well as the maturity of the industry as a whole.

Louvre Group

Established in Guernsey in 1976, the Louvre Group has grown into a successful, privately owned international operation offering confidential, personal and professional offshore and onshore services to private and corporate clients. The company has developed into a strong, multi-disciplinary professional business with offices in Guernsey, the UK, Switzerland and Liechtenstein. It is shortly to establish a presence in Dubai and Hong Kong, and has associate offices in the British Virgin Islands, as well as affiliates in many other countries as a result of its association with UHY International.

The Louvre Group provides clients with a diverse range of services with tailored solutions for their wealth and business management needs using structured financial arrangements and products, and the use of both onshore and offshore entities. Its wide-ranging client base has assets of more than £1.4bn.

The Louvre Fiduciary Group, the principal holding company of Louvre Group, is located in the financial heart of Guernsey's capital, St Peter Port. It is registered as a fiduciary company, under a full licence issued by the Guernsey Financial Services Commission. The island is internationally recognised as an ideal location for fiduciary business as a result of its stable economic and political environment, and its independent government supported by a low tax base and a first-class legal infrastructure.