

Non-retail offshore funds - where to next?

The change in the offshore landscape due to the financial crisis and tightening regulations is driving fund managers to move funds onshore. Vanessa Molloy, investment funds partner looks into the issues facing fund managers when deciding whether or not to re-domicile their funds onshore and what can attract or disappoint a fund manager in their choice of onshore jurisdiction.

Introduction

It is undeniable that the offshore landscape has changed forever. This is due to a number of reasons, including the change in government in the US, the Madoff scandal, the near collapse of the banking sector, and to top it all off, the proposed Alternative Investment Fund Managers Directive.

It is understandable that professional and institutional investors are more nervous and vigilant when investing than was the case 18 months ago. This has in turn put pressure on fund managers to review their existing offshore structures and consider the commerciality of continuing as before.

What are the options?

One of the issues on the table for consideration by most offshore managers is the domicile of their funds. Do they sit it out offshore and see how things develop in the next year with the possibility of launching future funds onshore.

Alternatively do they move their existing offshore fund structures onshore either by going all the way and offering investors the maximum protection by opting for a UCITS III compliant fund structure (where the investment strategy is compatible with the UCITS requirements). Alternatively, choosing an onshore non-retail structure subject to lighter regulation than a UCITS fund.

Another option is the re-domiciliation of funds i.e. where the fund continues to exist in a different jurisdiction to that of its original incorporation, which is often a neat solution. Usually, the re-domiciliation does not trigger a capital realisation event for investors and allows the manager to keep its track record intact.

What are the issues at stake in the case of a re-domiciliation?

There are a number of issues that fund managers and directors need to consider when deciding if a re-domiciliation onshore is appropriate. Among these considerations are

1. does the existing jurisdiction allow for an outwards migration, and does the new jurisdiction allow for an inwards migration;
2. is the fund vehicle in a corporate form (limited liability partnerships are not eligible for migration);
3. shareholder consent issues and the increased regulatory costs of running the fund onshore;
4. the need to appoint local services providers, and what to do when existing investors do not meet the minimum investment requirement that may be higher in the new jurisdiction than the typical USD 100,000 required in the Cayman Islands and the British Virgin Islands or other onshore investor eligibility requirements.


A decision on whether to move onshore will primarily depend on whether the fund manager or the promoter thinks that the onshore profile will help to retain and attract additional capital and whether the proposed changes to the regulatory environment will make it unsustainable to remain offshore. Ultimately, many professional investors are familiar with offshore fund jurisdictions and take the jurisdiction of the fund into account together with a number of other facts (e.g. the performance of the manager etc) when deciding to make an investment.

Which onshore jurisdictions are the most popular?

The onshore hedge fund jurisdictions most favoured and known in the market are Luxembourg, Ireland and Malta.

The aim of the table on the next page is to set out the salient features of the most common Maltese, Luxembourg and Irish non-retail fund structures thereby providing fund managers with a starting point in considering which of the jurisdictions may be more suitable.

A comparative table can only go so far in comparing the jurisdictions and does not always illustrate advantages which may be difficult to quantify.

To view the comparative table please click on the tag 

Conclusion

The migration of a fund is a genuine cross border transaction. The jurisdictions involved impose their own procedures, which often do not correlate at first sight. This is particularly the case when common law and civil law jurisdictions are involved. Cross-border expertise and advice is therefore essential to provide for a smooth migration, allowing the fund to continue with its business during the migration with the minimum interruption.

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