

Legislative and Regulatory Recommendations of Isle of Man Funds Review Group

By-lined by Paul Branford, Senior Associate, Commercial Department, Dickinson Cruickshank

The Isle of Man funds industry has been the subject of a recent high level review to identify how the Island can continue to expand the size and increase the quality of the business. The Funds Review Group, as it is known, is comprised of senior figures from both the public and private sectors in the Island. The Group delivered its initial recommendations in February 2007; from a legal perspective it proposed significant changes to two principal aspects of the Island's funds regime. The first is for significant alterations to the policy by which investment business licences are granted by the Isle of Man Government Financial Supervision Commission ("FSC") to investment managers and advisers. The second recommends the introduction of a new type of fund, provisionally named the "specialist fund", and for the phasing out of the experienced investor and professional investor fund classifications.

The Isle of Man has a substantive and rigorous licensing regime for those carrying on investment business in or from the Island. As the law presently stands, an applicant for an investment business licence must have a real presence in the Island with staff, premises and a proven track record in the category of business for which the application is being made. The Group has recommended a streamlined approach to licensing for fund managers and advisers forming part of a group, other members of which are already licensed in the Isle of Man or elsewhere to provide the same services.

Any company licensed in this manner would only be able to provide services to funds in the new specialist fund category (or to equivalent funds in other jurisdictions). It would need to be managed and controlled in the Island, but it would be sufficient for the company to be administered by a local fund administrator or fiduciary service provider, without the need for dedicated staff and premises in the Island.

It is proposed that the focus for licensing should in these cases be on the fitness and propriety of the licence applicant, criteria which are already applied by the FSC as part of its general licensing policy. Any successful licence applicant would not be obliged to meet any minimum capital or professional indemnity ("PI") insurance thresholds, but would be subject to an annual audit and a duty to make regulatory returns to the FSC.

In addition, it is proposed by the Group that fund managers and advisers who only provide services to specialist funds (or their overseas equivalents), but who do not form part of a group which is licensed to undertake this business, are nonetheless to be capable of applying for a licence if they can demonstrate to the FSC that they are fit and proper and have the relevant experience. Successful applicants would have to maintain staff and premises for their operations in the Island, comply with minimum capital and PI insurance thresholds and meet the other criteria outlined above.

The specialist fund, to which these providers' services would be limited under the Group's recommendations, is to be targeted at professional investors and high net worth individuals who have sufficient experience to understand the risks of investing in the fund and who must each invest a minimum of US\$100,000. All material

information about the fund would need to be set out in an offering document, and the documents constituting the fund are to be subject to Isle of Man law.

A departure from current practice is the absence of any requirement for the fund to appoint a custodian, nor must the fund administrator be located in the Island if it is authorised in another acceptable jurisdiction to provide its services to similar funds. This approach will allow promoters of offshore funds to use the flexible vehicles available in the Isle of Man and to source administration and custody services from those providers offering the best quality and value services, irrespective of the jurisdiction in which they operate. Where there is no administrator in the Island, a local agent must be appointed whose role is to ensure that certain administrative requirements for the fund are fulfilled. For added investor protection the Group also recommends that the accounts of specialist funds should be audited by an independent auditor holding PI insurance of at least £20 million and distributed to investors no later than six months after the fund's financial year end, and that the FSC should be granted additional supervisory and enforcement powers for all types of funds.

Managers and administrators of specialist funds in the Isle of Man would not be obliged to charge VAT on their fees, in line with an existing exemption for most other fund categories in the Island.

The specialist fund is intended by the Group to be the successor to the experienced investor and professional investor fund classifications. Existing funds of these types should be permitted to convert to specialist funds or to a new category of international scheme with a regulated administrator, custodian and promoter.

The Group's recommendations are innovative, and, if implemented, will considerably increase the Island's appeal in the competitive offshore fund market.

Notes to editor: Paul Branford is a senior associate in the Commercial Department and deals with a broad range of corporate, financial services and regulatory issues, with an emphasis on funds and investment vehicles. Prior to joining Dickinson Cruickshank, Paul gained extensive experience in the commercial department of Mann & Partners in the Isle of Man where he worked for approximately nine years.