

Guernsey

Regulation

HEDGE FUNDS 2009

Hedge fund managers/advisors

Regulation

Authorization requirements and process

Prior to commencing operations as a hedge fund manager/advisor in Guernsey a license is required under the Protection of Investors (Bailiwick of Guernsey) Law, 1987, as amended (the POI Law) from the Guernsey Financial Services Commission (the GFSC). Schedule 2 of the POI Law sets out the activities which constitute restricted activities in connection with controlled investment business. The restricted activities include promotion, subscription, registration, dealing, management, administration, advising, custody, and operating an investment exchange.

Prior to making an application for a license an informal approach may be made to the GFSC, which often includes a preliminary meeting with the potential licensee. Completion of the New Promoter's Introductory Checklist, which is available from the GFSC Web site, will assist this process. Once enquiries are complete the GFSC notifies the applicant as to whether it would be willing to consider a formal application. The formal application comprises of:

- a fully completed Form RA/1, which is available from the GFSC Web site; and
- all supporting documents requested on Form RA/1 and a non-refundable application fee, currently GBP 1,450.

Once submitted, the application is processed by the GFSC. It is important for forms to be fully completed as the GFSC will follow up any question left unanswered and this will inevitably delay an application. Once all matters are satisfactorily resolved and the application approved a license is issued by form of a letter, setting out the categories of investment business the new licensee may deal with and the restricted activities it may undertake in connection with that business.

Typical timescale to receive approval

If the applicant, its parent or principals is already known to the GSFC, or has received a positive response after submitting a New Promoter's Introductory Checklist, the amount of documentary evidence required in support of Form RA/1 (and the time taken for this form to be processed) should be considerably reduced. Normally, the application should be processed should be within approximately six to eight weeks. In 2008, the GFSC introduced a fast track process for consideration of a POI license application for any company domiciled in Guernsey which acts as a fund manager to a registered fund or QIF. Where the fund structure includes a Guernsey fund manager or the fund is structured as a limited partnership and has a Guernsey general partner, the Commission will process the application for the license of such an entity (with reliance on the certification of the administrator) under the fast track licensee application process and put it before the GFSC's Licensing Committee within ten business days of receipt.

Regulatory capital requirements

The regulatory capital requirements for a hedge fund manager/advisor are detailed in The Licensees (Financial Resources, Notification, Conduct of Business and Compliance) Rules 1998 Part 2 Section 2.01.

The requirements are gross capital (total assets less total liabilities after adjustments) of GBP 25,000 or gross capital equal to the expenditure based requirement (a figure equal to 25 percent of the licensee's annual audited expenditure, which is an estimate of budgeted expenditure for the first 12 months in the case of a licensee which has not yet commenced its controlled investment business; or the annual gross revenue less profit before appropriations of a licensee and in the case where a loss before appropriations occurs the amount of the loss shall be added to the annual gross revenue calculated on the basis of the audited annual financial statements), whichever is the greater and minimum professional indemnity insurance cover of GBP 250,000, (or three times annual gross revenue (total revenue shown by the audited annual financial statements for the immediately preceding accounting period plus any dealing profit (or less any dealing loss) less a deduction to eliminate commissions and fees payable which are attributable directly to commissions and fees receivable which are included in annual gross revenue), whichever is greater), the excess of which must not exceed 20 percent of the total insured.

Significant restrictions on marketing to investors

Promotion is a restricted activity under the POI Law; hence, the licensee must have authorization from the GFSC prior to conducting any promotional activities. The POI Law Part III Section 18 sets out the rules regarding promotion. There are no significant restrictions within the POI Law relating specifically to the marketing of hedge funds to investors in Guernsey.

Hedge fund structures

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Authorization requirements

All Guernsey hedge funds must be licensed by the GFSC under the POI Law. There are three different types of schemes that can be utilized, namely: Class B, Class Q, or qualifying investor fund. The type of scheme used will depend on the target investor base of the promoter. Such funds can now be authorized or registered under the POI law. The time scale for the establishment of hedge funds is detailed below.

The manager is required to be domiciled in Guernsey and appropriately licensed under the POI Law. However, the manager can delegate duties to a sub-manager in another jurisdiction providing a sufficient level of oversight/monitoring is undertaken by the manager.

It is also worth noting that in the case of institutional and expert investor hedge funds the GFSC are prepared to waive the requirement for a locally licensed custodian and will be prepared to designate as custodian a prime broker, regulated in an acceptable jurisdiction and having substantial net worth. Formal oversight duties of the prime broker on the manager would not be required. In addition, the prime broker would not be required to offer physical segregation of fund assets from its own assets, even where fund assets held by the broker exceed credit extended by the broker. If these rule waivers are exercised the prospectus would have to make clear and prominent disclosures of the risks inherent in these arrangements.

Restrictions on types of investments, concentration levels, and the manner in which hedge funds can invest and/or strategies

The GFSC will review the fund's prospectus during the application process and will consider whether there is an adequate spread of risk, comprehensive risk warnings, the investor profile is consistent with the fund's objectives and minimum subscription levels and that all material facts are fully disclosed. Once a license has been granted the licensee would have to operate within the investment restrictions as defined within the prospectus.

Rules regarding the publishing of the accounts and prospectuses

Other than the requirements for any Class B, Class Q, qualifying investor fund, or listed fund, there are no rules specific to hedge funds regarding the publishing of the accounts and prospectuses. Class B, Class Q, and qualifying investor funds must file their accounts with the GFSC within six months of the accounting reference date.

Time-scale of establishment of a hedge fund

Time-scale regarding applications for authorized funds such as Class B and Class Q schemes are still subject to the lengthier, traditional approval process as detailed above and may not take advantage of the three day fast-track approval process which applies to registered funds. However, it has been known to be quicker than the six to eight weeks indicated above depending on the manager and the standard of documentation.

The GFSC undertakes to grant the required fund approval for qualifying investors funds, registered closed ended and open ended schemes within three working days provided that an appropriately licensed Guernsey applicant has certified that:

- the fund will be restricted to professional, experienced, and knowledgeable investors; and
- the applicant has conducted due diligence on the promoter and associated parties and has found them to be fit and proper and the applicant is satisfied as to the fund's economic rationale and the disclosure of any risks associated with the investment vehicle.

Investors

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Restrictions on which type of investors can invest in a hedge fund and/or the minimum/maximum number of investors in a hedge fund

The type of scheme utilized (Class B, Class Q, or qualifying investor fund) will determine the type of investor. Hence, the promoter needs to establish the target investor base prior to applying for a license. There are no restrictions on the minimum/maximum number of investors. However, a qualifying investor fund requires that an individual investor makes an initial investment of not less than USD 100,000. There may also be minimum subscription level requirement in the fund's prospectus.

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The information contained herein is of a general nature and is not intended to address the circumstances of any particular individual or entity. Although we endeavor to provide accurate and timely information, there can be no guarantee that such information is accurate as of the date it is received or that it will continue to be accurate in the future. No one should act upon such information without appropriate professional advice after a thorough examination of the particular situation.