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The International Comparative Legal Guide to:

Public Investment Funds 2019

2nd Edition

A practical cross-border insight into public investment funds

Published by Global Legal Group, with contributions from:

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GLG Cover Design
F&F Studio Design

GLG Cover Image Source
iStockphoto

Printed by
Ashford Colour Press Ltd
April 2019

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ISBN 978-1-912509-66-9
ISSN 2516-4821

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This publication is intended to give an indication of legal issues upon which you may need advice. Full legal advice should be taken from a qualified professional when dealing with specific situations.

EDITORIAL

Welcome to the second edition of *The International Comparative Legal Guide to: Public Investment Funds*.

This guide provides corporate counsel and international practitioners with a comprehensive worldwide legal analysis of the laws and regulations of public investment funds.

It is divided into two main sections:

Four general chapters. These chapters are designed to provide readers with an overview of key issues affecting public investment funds, particularly from the perspective of a multi-jurisdictional transaction.

Country question and answer chapters. These provide a broad overview of common issues in public investment funds laws and regulations in 17 jurisdictions. All chapters are written by leading public investment funds lawyers and industry specialists and we are extremely grateful for their excellent contributions.

Special thanks are reserved for the contributing editors Gregory S. Rowland and Sarah E. Kim of Davis Polk & Wardwell LLP for their invaluable assistance.

Global Legal Group hopes that you find this guide practical and interesting.

The *International Comparative Legal Guide* series is also available online at www.iclg.com.

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PREFACE

Davis Polk & Wardwell LLP is honoured to serve as Contributing Editor for the second edition of *The International Comparative Legal Guide to: Public Investment Funds*, and it is my pleasure to have been invited to write this preface.

Publicly offered investment funds are subject to regulatory frameworks that, depending on the jurisdiction, impose comprehensive restrictions on how a fund is operated. The regulatory framework in the U.S., for example, imposes strict requirements on, among other things, a public investment fund's corporate governance, capital structure, portfolio investments, affiliated transactions, reporting and recordkeeping. The degree of regulation and the specifics of the requirements in each jurisdiction vary significantly, which is why a guide such as this is essential.

The second edition provides broad overviews of the general regulatory framework for public investment funds in 17 jurisdictions, as well as four general chapters on topics of particular interest.

As the regulations in the financial services industry continue to evolve in response to new developments and obstacles in financial systems globally, it will be important for legal professionals and industry participants to have up-to-date resources such as this guide for practical insight relating to different jurisdictions.

We hope that you find this guide useful in your practice, and we look forward to future editions of the guide going forward.

Gregory S. Rowland

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1 Registration

1.1 Are funds that are offered to the public required to be registered under the securities laws of your jurisdiction? If so, what are the factors and criteria that determine whether a fund is required to be registered?

There are two primary types of regulated investment fund in Ireland that can be sold to the public; namely undertakings for collective investment in transferable securities ("UCITS") and alternative investment funds ("AIFs" which, in essence, covers all non-UCITS funds). There is a sub-category of retail AIFs available to the public at large (other sub-categories are restricted) but it is not frequently used and the overwhelming majority of funds sold to the public are UCITS. As such, this section focuses on UCITS.

UCITS are collective investment schemes established and authorised under a harmonised EU legal framework. UCITS benefit from a marketing passport, which means that a UCITS authorised in one EU Member State can be sold cross-border into other EU Member States without the requirement for additional authorisation. UCITS authorised in Ireland go through an authorisation process with the Central Bank of Ireland and, by default, may be sold in Ireland. UCITS authorised elsewhere in the EU go through an authorisation process with their local regulator, which then sends a simple regulator-to-regulator notification for the UCITS to be registered for sale in Ireland.

1.2 What does the fund registration process involve, e.g., what documents are required to be filed?

In order for an Irish UCITS to be authorised by the Central Bank, various documents need to be put in place. The Central Bank imposes minimum standards for the majority of these documents and, in the case of the offering document (prospectus), it reviews the document in advance and provides comments which must be addressed. Other fund documents (such as the depositary, investment management, distribution and administration agreements, the risk management process and the Key Investor Information Document) are not reviewed by the Central Bank but executed/final versions of the agreements are filed with the Central Bank, along with a confirmation that they meet the minimum requirements. Once the draft prospectus is filed with the Central Bank for review, a non-complex UCITS is typically approved by the Central Bank within six to eight weeks (during which period the other, non-review documents are finalised).

It is worth noting that every UCITS must either: (1) appoint a UCITS management company; or (2) be a self-managed UCITS. The former category is becoming far more common that the latter but, in the event that a given UCITS decides to be self-managed, then it must obtain a particular authorisation as a self-managed UCITS. This process involves different documents (including a business plan) and the appointment of designated persons (individuals, some of whom must be based in the EEA and potentially Ireland, who oversee the UCITS on a day-to-day basis). The authorisation process for a self-managed UCITS can take several months, whereas the appointment of a UCITS management company does not add any time to the six- to eight-week period mentioned above.

1.3 What are the consequences for failing to register a fund that is required to be registered in your jurisdiction?

There are various supervision and enforcement laws that will apply in circumstances where an Irish fund is held out as authorised when it is not or where a foreign fund is sold in Ireland when it is not suitably registered for sale. These laws provide the appropriate authorities with a range of sanction powers, including fines.

1.4 Are there local residency or other local qualification requirements that a fund must meet in order to register in your jurisdiction? Or are foreign funds permitted to register in your jurisdiction?

As noted in the answer to question 1.1, UCITS established in EU Member States other than Ireland can be sold in Ireland once a simple regulator-to-regulator notification process is completed.

2 Regulatory Framework

2.1 What are the main regulatory restrictions and requirements that a public fund must comply with in the following areas, if any? Are there other main areas of regulation that are imposed on public funds?

i. Governance

A UCITS established as a corporate vehicle (e.g., an ICAV or plc) is required to have a minimum of two Irish-resident directors appointed to its board and the board must comprise at least three directors in total. The corporate governance code (which applies on a comply-or-explain rather than mandatory basis) recommends at

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least one director from the promoter. The size of a board of the fund generally depends on the requirements of the promoter – boards would typically comprise four or more directors, a majority of whom are interested directors (i.e., are employees of the promoter).

The Central Bank must be satisfied that all directors are fit and proper in terms of: (i) competence and capability; (ii) honesty, integrity, fairness and ethical behaviour; and (iii) financial soundness. Letters of appointment must be put in place with each director setting out the terms of their engagement. The Central Bank must also be notified of all resignations from a board of directors.

ii. Selection of investment adviser, and review and approval of investment advisory agreement

A UCITS must have one or more discretionary investment managers/advisors who manage the portfolio of investments. Each discretionary manager/advisor must be cleared to act as such by the Central Bank. Essentially, the Central Bank must be satisfied that it is authorised by an appropriate regulatory authority and is subject to ongoing supervision in its home jurisdiction (the jurisdiction itself must also be considered appropriate by the Central Bank). Where the given entity is regulated in Europe under a pan-European framework such as MiFID, this process is a simple notification. Where the entity is not regulated in Europe (e.g., it is an SEC registered manager), there is a more formal process which involves an application setting out information regarding the entity's history, performance record, AUM, details of senior staff and their experience, financial resources and regulatory status. This process typically takes four to five weeks. The process need only be completed once – thereafter, the entity is cleared to act for any Irish fund (whether UCITS or AIF). The only ongoing obligation owed to the Central Bank is to notify it of any change in regulatory status, name or registered address

iii. Capital structure

A UCITS is not itself subject to any capital requirements. As noted above in question 1.2, every UCITS must either (1) appoint a UCITS management company, or (2) be a self-managed UCITS. In the former case, the UCITS management company is subject to a minimum capital requirement of €125,000 or one-quarter of its preceding year's fixed overheads, whichever is the greater. In addition, the management company must maintain additional capital of 0.02% of the value of the assets under management in excess of €250 million, subject to a maximum level of capital of €10 million. In the case of a self-managed UCITS, it is subject to a minimum capital requirement of €300,000, which can be withdrawn once and for so long as the UCITS has received subscriptions from investors of at least €300,000.

iv. Limits on portfolio investments

A UCITS can invest in a diverse range of investments such as transferable securities, bank deposits, money market instruments, financial derivatives and units of other funds, either as a fund of funds or a feeder fund. A UCITS cannot invest in real estate or invest directly in commodities (but can obtain exposure to commodities using derivatives). The UCITS legislative framework imposes a number of investment restrictions, including concentration limits, exposure limits, counterparty requirements, use of FDI, etc.

v. Conflicts of interest

The Central Bank of Ireland UCITS Regulations contain requirements regarding management of conflicts of interest. The primary obligations in this regard are disclosure related; the prospectus of the relevant UCITS must include a description of the potential conflicts of interest and details of how they will be managed. In addition, the annual reports must contain details of soft commission arrangements and any amounts paid to the investment manager for directed brokerage services. Furthermore, where an investment manager negotiates the recapture of a portion of the commissions charged by brokers or dealers in connection with the purchase and/or sale of securities for a UCITS, the rebated commission must be paid to the UCITS.

vi. Reporting and recordkeeping

The Central Bank of Ireland UCITS Regulations contain requirements regarding reporting and recordkeeping, including the requirement for annual and semi-annual reports to investors and monthly and quarterly returns and other necessary reports to the Central Bank.

vii. Other

In circumstances where a UCITS is listed, there may be stock exchange rules to be followed, including in relation to notices, reports and material changes. In addition, where a UCITS obtains a secondary authorisation (e.g., as an ETF or a money market fund), further obligations are imposed.

2.2 Are investment advisers that advise public funds required to be registered and/or regulated in your jurisdiction? If so, what does the registration process involve?

As noted in question 2.1 (ii), advisers or managers with discretionary portfolio management powers must be cleared to act as such by the Central Bank. Essentially, the Central Bank must be satisfied that the adviser/manager is authorised by an appropriate regulatory authority and is subject to ongoing supervision in its home jurisdiction (the jurisdiction itself must also be considered appropriate by the Central Bank). Where the given entity is regulated in Europe under a pan-European framework such as MiFID, this process is a simple notification. Where the entity is not regulated in Europe (e.g., it is an SEC registered manager), there is a more formal process which involves an application setting out information regarding the entity's history, performance record, AUM, details of senior staff and their experience, financial resources and regulatory status. This process typically takes four to five weeks. The process need only be completed once – thereafter, the entity is cleared to act for any Irish fund (whether UCITS or AIF). The only ongoing obligation owed to the Central Bank is to notify it of any change in regulatory status, name or registered address.

2.3 In addition to the requirements above, are there additional regulatory restrictions and requirements imposed on investment advisers that advise public funds?

The above sets out the primary requirements that apply.

2.4 Are there any requirements or restrictions in your jurisdiction for public funds investing in digital currencies?

As noted in question 2.1 (iv), a UCITS can invest in transferable securities, bank deposits, money market instruments, financial derivatives and units of other funds. The Central Bank (and equivalent European regulatory authorities) have not yet satisfied themselves that digital currencies fall into one of those categories. As such, and until that changes, a UCITS cannot invest directly in digital currencies. It may be able to invest in such currencies (and other ineligible assets) indirectly, e.g, through indices.

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3 Marketing of Public Funds

3.1 What regulatory frameworks apply to the marketing of public funds?

Marketing of UCITS funds in Ireland is subject to the UCITS regime but may also be subject to other regimes (e.g., MiFID), depending on the entity undertaking the marketing.

3.2 Is licensure with a regulatory authority required of persons (whether entities or natural persons) engaged in marketing activities? If so: (i) are there commonly available exceptions that may be relied on?; and (ii) describe the level of substantive regulation applied to licensed persons.

Yes, entities marketing UCITS must be suitably authorised for the same under a relevant regime (generally MiFID, UCITS or AIFMD). There are no commonly available exemptions (e.g., private placement).

3.3 What are the main regulatory restrictions and requirements in the following areas, if any, that must be complied with by entities that are involved in marketing public funds?

i. Distribution fees or other charges

The primary obligations in this regard are disclosure based. The UCITS must provide disclosures in relation to fees, including the mechanism for altering fees and restrictions regarding paying fees out of capital. Depending on the other entities involved, further obligations may be relevant, e.g., a MiFID distribution may be subject to restrictions against certain commissions or fees being paid in respect of distribution of a UCITS.

ii. Advertising

The Central Bank imposes certain obligations as regards advertising, including the overriding requirement that advertising must be clear, fair, accurate and not misleading, and that the advertisement can be understood easily and clearly. In addition: (a) the name of a UCITS and its regulatory status shall be shown clearly in any advertisement relating to that UCITS; (b) any advertisement relating to a UCITS shall not contain information which is false or misleading or presented in a manner that is deceptive; (c) any advertisement relating to a UCITS shall refer to the key investor information document and the prospectus; and (d) no advertisement relating to a UCITS shall be inconsistent with any relevant provision of the key investor information document or of the prospectus.

iii. Investor suitability

There is a UCITS obligation to identify a typical investor and disclose the profile of that investor in the prospectus. In addition, distributors may be subject to their own regulatory requirements. As regards distributors operating in Ireland, these requirements are likely to be MiFID requirements, including, in particular, the product governance rules and the obligation to carry out a target market assessment.

iv. Custody of investor funds or securities

Each UCITS must appoint an Irish depositary, which is responsible for safekeeping the assets, ensuring that the cash flows are properly monitored and carrying out oversight in relation to the management of the UCITS, amongst other things.

3.4 Are there restrictions on to whom public funds may be marketed or sold?

UCITS are designed to be suitable for broad distribution to the public. Promoters of UCITS themselves may effectively restrict the sale of certain fund types to more institutional investor types through setting high minimum investment amounts or other means and a UCITS has the ability to reject a given subscription request for any or no reason. Where a UCITS is sold in an EU Member State other than Ireland, the simple notification procedure described in question 1.1 must be completed.

3.5 Are there other main areas of regulation that are imposed with respect to the marketing of public funds?

No, the above sets out the main areas of regulation with regard to the marketing of public funds in Ireland.

4 Tax Treatment

4.1 What are the types of entities that can be public funds in your jurisdiction?

ICAVs, unit trusts, Common Contractual Funds (CCFs) and variable or fixed capital companies can be public funds.

4.2 What is the tax treatment of each such entity (both entity-level tax and taxation of investors in respect of allocations of income or distributions, as the case may be)?

At the entity level and assuming that a UCITS conducts its affairs so that it is Irish tax-resident, an Irish UCITS qualifies as an "investment undertaking" for Irish tax purposes and, consequently, is exempt from Irish corporation tax on its income and gains, save for certain limited cases where the UCITS holds Irish real estate or Irish equity assets.

At the investor level, where an investor is not resident (or ordinarily resident) in Ireland for Irish tax purposes, an Irish UCITS will not deduct any Irish tax in respect of the investor's shares once a declaration has been received by the UCITS confirming the investor's non-resident status. With respect to Irish resident investors, an Irish UCITS will be obliged to account for Irish income tax to the Irish Revenue Commissioners if shares are held by Irish resident investors, unless they fall into an exemption category (for example, pension schemes, charities, etc.). For non-exempt Irish resident investors, the UCITS will deduct Irish tax on distributions, redemptions and transfers and, additionally, on "eighth anniversary" events (being the eighth anniversary of the acquisition of shares, where they are not disposed previously). Depending on the nature of the Irish resident investor, Irish tax is levied at either 25% or 41% of the distribution/gain in value.

No Irish stamp duty (or other Irish transfer tax) applies to the issue, transfer or redemption of shares.

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4.3 If a public fund, or a type of entity that may be a public fund, qualifies for a special tax regime, what are the requirements necessary to permit the entity to qualify for this special tax regime?

As described in question 4.2, for a UCITS to qualify as an "investment undertaking" for Irish tax purposes it must conduct its affairs so that it is Irish tax-resident. This would include, for example, holding board meetings in Ireland.

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Barry O'Connor is a partner in the Asset Management and Investment Funds Group at Matheson. He practises financial services law and advises many of the world's leading financial institutions, investment banks, asset management companies, broker-dealers and corporations carrying on business through Irish domiciled investment funds (ICAVs, investment companies, unit trusts, CCFs and ILPs) and Irish-domiciled management companies (UCITS and AIFMs).

Barry has extensive experience advising on the launch of UCITS and AIFs (stand-alone funds, umbrellas and third-party manager platforms) across the full range of strategies, including plain vanilla strategies, hedge fund strategies, structured UCITS, fund of funds, money market funds, ETFs and master-feeders, and on their ongoing servicing (including the launch and termination of sub-funds, a change of service providers and listing on the Irish Stock Exchange). He is also experienced in more complex issues arising in the course of the life of a UCITS or AIF, including obtaining Central Bank approval for innovative fund mechanics and structures.

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Matheson

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