

IFC Review

The definitive guide to the world's leading international financial centres

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Gibraltar Funds

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THE TREMENDOUS SUCCESS of new and developing finance centres as a part of the global asset management industry is now a commonly reported feature. However, equally well-reported has been the issue of 'capacity' within these often small jurisdictions. The global expansion in funds has unquestionably placed considerable pressure on the established fund centres of Dublin, Luxembourg and the Caribbean, where spare capacity to deal with smaller-sized funds is becoming increasingly rare. This has led, not only to far greater selectivity by fund administrators, but also to a natural increase in fees and set-up costs.

Gibraltar, through the introduction of its Experienced Investor Funds legislation, and the necessary legislative changes made to accommodate the rapidly changing requirements of the global fund market, is ready and well-placed to offer itself as a serious alternative fund jurisdiction and finance centre.

Although Gibraltar is not unique in allowing administrators to work within a European time zone, its position is quite unique in that the jurisdiction offers a favourable tax regime while at the same time existing within the EU by virtue of its relationship with the UK. All relevant EU banking, insurance, and investment services directives have been transposed into Gibraltar law, allowing for the financial services sector to work within an integrated, structured financial services system implemented by the EU. Financial 'passporting' has also been in effect since July 2003, thus allowing financial services firms and certain funds to offer their products and services throughout Europe on the basis of their Gibraltar licence. The value of the European passport cannot be under-estimated, with 27 member states, a strong euro, and a population of 494 million, all offering a wealth of marketing opportunity.

Gibraltar's Unique Position

Gibraltar's success as an international finance centre will always depend somewhat on its ability to create simple and tax-efficient structures. Historically, the Gibraltar tax-exempt company (launched in 1967) formed very much the backbone of the finance centre. However, the legality of the exempt status regime in Gibraltar was challenged in July 2001 by the EU Commission under EU State Aid Rules. Initially, the government of Gibraltar successfully defended this challenge in the European Courts, with the ruling eventually determining that by attacking the whole of the exempt company regime as "new aid", as opposed to treating the original 1967 legislation for the establishment of the exempt company as "existing aid", the Commission had breached the rules on State Aid procedure. The Commission then issued a challenge of the exempt company regime under the existing aid procedure, with the result that on 18 February, 2005, a positive agreement was reached with the European Commission for Gibraltar's exempt company to be phased out of existence by 31 December, 2010. No new exempt company certificates have or may be issued as of 30 June, 2006.

New proposals regarding a tax reform to replace the tax-exempt company legislation have been made by the Gibraltar government with the unconditional support of the UK government, but the Commission has challenged these proposals on the basis of regional or material selectivity. The view of the Gibraltar government has always been that this is an unsustainable position, and that this will be challenged successfully in the European Courts on the basis that Gibraltar is not a region of the UK, and is also politically, constitutionally, and economically separate from the UK, making a recognised low-cost tax regime (rather than a 'no tax' regime) a realistic

goal of the Gibraltar government.

However, the immediate effect of the phasing out of the exempt company has had a far more positive effect than could have been envisaged, and it is altogether surprising to reflect that Gibraltar's place as a jurisdiction of choice for funds has actually been in part due to the phasing out of the Gibraltar tax exempt company. The phasing out of the exempt company has allowed Gibraltar companies access in some jurisdictions to the benefits of the European Parent Subsidiary Directive. As part of the solution for the phasing out of the tax-exempt company in Gibraltar, the European Commission notified member states that the Parent Subsidiary Directive should be applied to Gibraltar tax-resident companies in the same way that it is applied to companies that are resident in any other member state.

This Directive is an extremely important piece of EU legislation, designed to eliminate tax obstacles in the area of profit distributions between groups of companies in the EU by effectively abolishing withholding taxes on payments of dividends between these associated companies, even when they are domiciled in different member states. To illustrate, if a Gibraltar company is properly tax-resident in Gibraltar and has a relevant participation in a Luxembourg company, the tax authorities will not tax dividends that are paid from that Luxembourg company to the Gibraltar parent. To take this a step further, the result is that the fund may invest in a wholly-owned French company, and allow the French company, after it has paid any French taxes on its income, to pay its dividends to the Luxembourg parent without paying French withholding tax. The structure would then allow for those profits to be sent as dividends to the Luxembourg corporation's Gibraltar parent, without suffering Luxembourg withholding tax. In Gibraltar, the dividends would not



attract any tax on the basis that they are from the proceeds of the parent subsidiary relationship, and there would be no capital gains tax, wealth, or estate duty tax, since these taxes do not exist in Gibraltar. Furthermore, there is no withholding tax on dividends paid to non-Gibraltarian shareholders of a Gibraltar company (unlike, for example in Luxembourg), so the profits of the French investment have essentially been repatriated to the investors of the fund without tax leakage. It becomes easy to see the potential that the Gibraltar domiciled fund has been able to offer to real estate and private equity funds, asset managers, and private investors.

In terms of the products available in Gibraltar, there have also been new and exciting developments recently, and these have not gone unnoticed within the fund industry. The Capita Group has recently established itself on "the rock" (as Gibraltar is known), and executive director, Robert Coyle, believes that Gibraltar "is on the cusp of taking off and already has a good infrastructure of lawyers and accountants". Locally, the Fiduciary Group, a long-established company and trust administrator in Gibraltar and Spain, also recently identified the funds industry as the primary area of growth, and set up Fiduciary Fund Administration Limited, which provides independent third party fund administration services. In short, everybody wants a piece of the action, and competition has led to competitive pricing within Gibraltar, which is already economical compared to other jurisdictions.

Fund Types

The current legislation in Gibraltar, namely the Financial Services Act, 1989, Financial Services Act (Collective Investment Schemes) Regulations, 1991, Financial Services (Collective Investment Schemes) Act, 2005, the Financial Services (Collective Investment Schemes) Regulations, 2006, and the Financial Services (Experienced Investor Funds) Regulations, 2005 can be said to divide the types of licensing requirements for Gibraltar funds into four categories: Private funds, Experienced Investor funds, non-UCITS retail funds, and UCITS funds.

Without question, the most exciting of these, and also the most commonly used vehicle for funds, is the Experienced Investor fund (EIF), a highly versatile and lightly-regulated instrument which allows for the possibility of setting up

funds for experienced investors. This style of fund has pioneered a rapid growth in the funds industry worldwide, but the Gibraltar EIF is unlike many competitive products in that it also enjoys a light level of regulation, providing a layer of comfort to its investors.

To establish the EIF, the fund administrator needs to notify the regulator within 14 days of establishment, and provide the fund's offering documents along with an opinion from counsel that the fund complies with the relevant provisions. The EIF is designed for professional, high net worth, or experienced investors, so investors in this fund must have a net worth of €1 million, or invest a minimum of €100,000. It is also a requirement that the EIF have two Gibraltar resident directors who are licensed by the Financial Services Commission (FSC - see www.fsc.gi) to act as EIF directors, a custodian or broker to hold its assets, and a Gibraltar-based licensed administrator. They must also produce annual audited accounts. In this way, the EIFs are 'fast-tracked' through the regulatory process, and do not have to go through the procedure for regulatory approval and licensing, which allows them to set up extremely quickly. At the same time, they are structured to ensure that there is adequate investor protection through the regulation of the counterparties to the fund, namely the administrator, directors and custodian. This, along with the opinion from counsel and the auditing requirement, lessens the need for regulation of the actual fund. When compared to private funds, where the disadvantage is the restriction on marketing, and retail funds, which can take months to launch, the EIFs provide an attractive, regulated solution that can be set up by fund promoters very quickly.

Furthermore, EIFs are exempt from income tax in Gibraltar upon receipt of the relevant certificate from the Commissioner of Income Tax, thus providing a favourable tax environment for the fund, investment manager and investors. The introduction of the Protected Cell Companies Act, 2001 also allows a Gibraltar fund to operate separate ring-fenced 'cells' under the single corporate body of the structure with one prospectus and a single board of directors.

Investor Perception

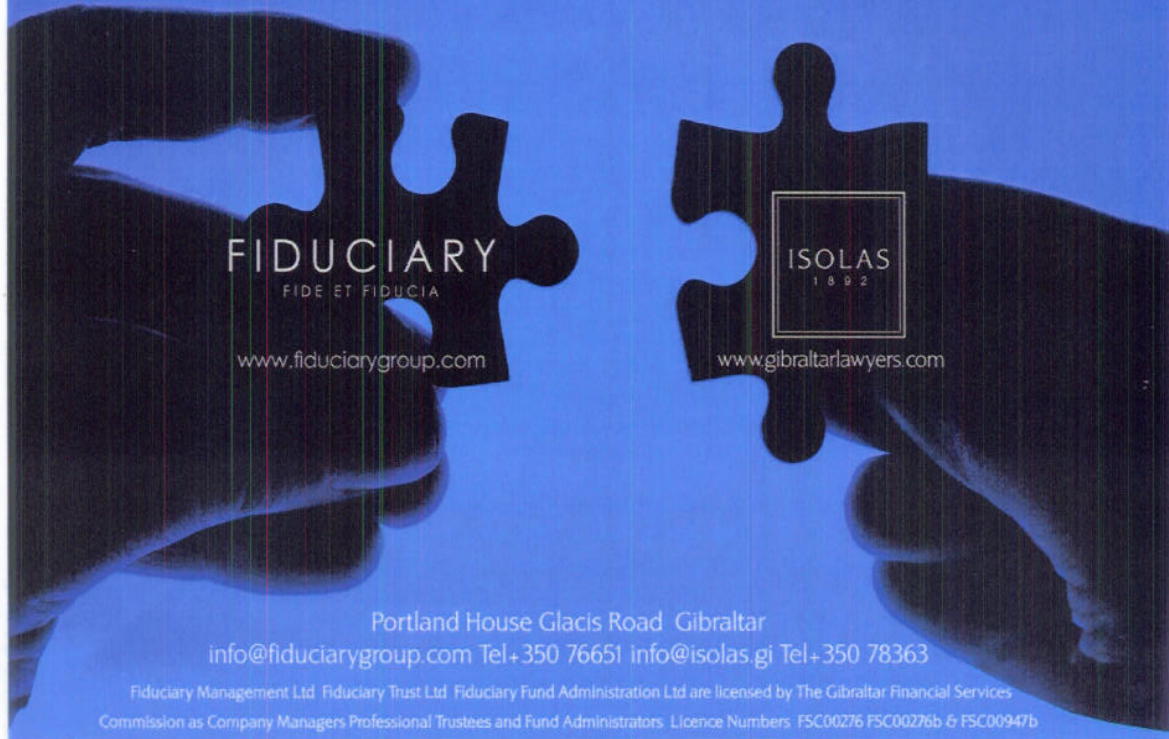
There has been a sea change in Gibraltar, reflected in the rapid growth of the

finance centre in Gibraltar. The regulator in Gibraltar, the Financial Services Commission was the first to pioneer this change, proving to the International Monetary Fund that it takes a strong stand against money laundering with a sound regulatory body. This was fundamental in Gibraltar's adaptation of the competitive requirements of the sector, and the advances that have been reflected recently in the IMF evaluation on Gibraltar's supervision of banking, insurance and anti-money laundering measures on 2 May, 2007, which further endorsed Gibraltar's robust regulatory environment. The assessment was conducted against recently revised and strengthened international standards, and Gibraltar was still found to be ahead of many other onshore and much larger financial centres.

In September 2006, CNBC European Business published a Country Report on Gibraltar, recognising it as a serious financial centre that could become even bigger if London and Madrid agreed on a development plan to open the border and expand the airport. Soon after this article was published, the Cordoba Accord was signed by the UK, the Kingdom of Spain, and Gibraltar, thereby ending all discriminatory restrictions on civilian flights to Gibraltar Airport, including the prohibition of flights over Spanish soil. The practical result of the Agreement is that Gibraltar will now benefit from full EU aviation measures, allowing civilian flights from all nations into Gibraltar Airport. Currently, there are direct flights to London and Madrid, with plans for a new air terminal that will assist in the development project of Gibraltar as an alternative funds jurisdiction within Europe, easily accessible and in the same time zone.

Overall, with an impressive location, legislative framework, regulatory regime, developed infrastructure and high calibre of advisors enhancing the perception of Gibraltar, Gibraltar has now evolved into a competitive option for a fund domicile with the capability and capacity to service clients on a personal and relationship-driven level. A further boost to the industry is likely to be the new Gibraltar stock exchange, provisionally named 'Gibex'. The exchange is a natural progression for Gibraltar, and it is hoped that it will create various opportunities for Gibraltar funds, and even Gibraltar-based companies who could opt for a secondary listing locally in the future. Indeed, the future looks bright. ■

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