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SPECIAL REPORT

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REGULATION

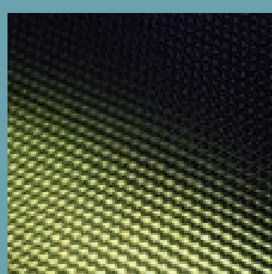
Confidence grows as the implementation of the AIFMD looms

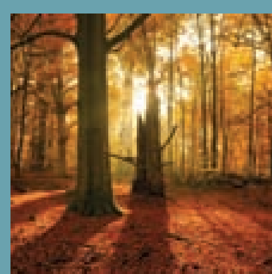
KEY PRODUCTS

The Irish perspective on Ucits, Newcits, QIFs and ETFs

NEW MARKETS

Ireland does business with Asia, the Middle East and Latin America





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ALTERNATIVES: NOW AND THE FUTURE

SHAY LYDON OF **MATHESON ORMSBY PRENTICE** TALKS TO *HFMWEEK* ABOUT HOW IRELAND IS MAINTAINING ITS LEAD AS THE DOMICILE OF CHOICE FOR ALTERNATIVE FUNDS

Shay Lydon is a partner in the Asset Management and Investment Funds Group at Matheson Ormsby Prentice. He advises many of the world's leading financial institutions, investment banks, asset management companies and service providers carrying on business in Ireland or through Irish vehicles and is a member of the Trustee Committee of the Irish Funds Industry Association.

Ireland's popularity as a fund domicile is no surprise, given its robust regulatory and highly developed fund-services environments. Its attractive tax regime, under which Ucits and other alternative funds remain entirely tax free, also offers it a key advantage over its competitors. These unique attributes combine to make Ireland the domicile to watch in 2011, not only in terms of its booming QIF sector, but in regards to the much sought after Newcits funds, explains Shay Lydon of Matheson Ormsby Prentice.

HFMWeek (HFM): What is Ireland's track record in domiciling and servicing alternative investment funds?
Shay Lydon (SL): Ireland was the first regulated jurisdiction to provide a regulatory framework specifically for the alternative investment funds industry. It is an established global leader in the alternatives space, building since the 1990s to become the European domicile of choice and home to 63% of all European hedge funds today.

Ireland is the world's largest hedge fund administration centre, servicing 43% of global hedge funds. The proportion of the world's hedge funds domiciled in Ireland doubled to 7.4% from the end of 2009 to the end of the third quarter of 2010. With alternative investment strategies also in demand in a Ucits format, the sophistication of the Irish regulator and the unrivalled expertise of the service industry in complex financial instruments have been critical to the success of investment managers launching innovative Ucits products in response to market appetite for Newcits.

"A TOTAL OF 388 FUND PROMOTERS FROM OVER 50 COUNTRIES HAVE CHOSEN IRELAND FOR THEIR FUNDS"

HFM: Ireland has a reputation for sophisticated and robust regulation. To what extent would you say this is justified?
SL: The regulatory authorities and advisory firms in Ireland have exceptional experience in applying the protections typically associated with regulated investment funds to alternatives. As far back as the mid-1990s, the Central Bank looked at the issues arising from the use of prime brokerage arrangements from the perspective of investor protection and fund exposure to prime brokers. The subsequent substantial increase in the numbers of hedge funds and funds of hedge funds being established in Ireland has given the regulatory authorities and service providers an advantage in understanding alternative strategies, and also the instruments and contracts on which such strategies are based.

The Central Bank anticipated by some years the increasing focus on issues such as depositary liability now apparent in initiatives such as AIFMD and Ucits V, while at the same time adopting a flexible attitude to investment strategies, so that alternative managers were enabled to offer investors the full range of their strategies, provided that the operational arrangements that supported those strategies satisfied the key requirements of the Central Bank.

HFM: What is the scale of Ireland's status as a distribution hub?
SL: Irish funds are sold in 70 countries across Europe, the Americas, Asia and the Pacific, the Middle East and Africa. A total of 388 fund promoters from over 50 countries have chosen Ireland as a domicile for their investment funds. When including non-Irish domiciled funds administered in Ireland, there are over 852 fund promoters who have chosen Ireland to domicile and/or service their funds.

HFM: What are Ireland's advantages as the domicile of choice for Newcits? Do you see the Newcits trend continuing into 2011 and beyond?
SL: Ireland's strong history and experience in both alternative investment funds (AIFs) and Ucits, mean that it is very well placed to benefit from the merging of these concepts in the form of absolute return style Ucits or 'Newcits'. Ireland's extensive community of administration, custody, legal and advisory firms with experience in such products give it a significant competitive advantage over other onshore jurisdictions in attracting Newcits and this has resulted in a substantial number of Newcits platforms being launched in Ireland.

In addition many alternative managers have opted to create their own standalone Newcits. Apart from the depth of experience of service providers in relation to such products in Ireland, the most significant advantage Ireland has is its efficient and accessible regulator, which has developed a reputation for sensible, prudent regulation, with approval timeframes that meet the expectations of the alternative investment community. As a jurisdiction that does not impose any direct taxes on Ucits, Ireland also enjoys a significant competitive advantage over its nearest rival, Luxembourg.

We would expect the current strong trend onshore and towards Newcits to continue, as more and more managers are keen to fit their strategies into this product to access the wider distribution opportunities it can provide within the EU and globally. Continued interest from investors in greater regulatory protections, liquidity and transparency for their chosen investment products will also continue to drive the Newcits trend in 2011.

HFM: What other key trends do you anticipate will emerge in the Irish alternatives space in 2011?

SL: We expect that focus from alternative managers will definitely remain on the movement of funds onshore to regulated domiciles, as we believe investor demand, particularly from Europe, will continue to support this. The long-term implications of the AIFMD also make this a sensible long term structuring solution for managers.

We also expect there will be a growing focus by managers on consolidation when it comes to fund domiciles, so that managers will, increasingly, look to locate all of their Ucits and non-Ucits funds in the same jurisdiction.

HFM: What recent regulatory developments have been enacted to support alternative providers and alternative funds domiciled in Ireland?

SL: Ireland continues to innovate and respond on the regulatory front. Alternative fund products established as Qualifying Investor Funds (QIFs) benefit from a fast-track authorisation process leading to regulatory authorisation in 24 hours.

Further enhancements in 2010 broadened the category of permitted investors for QIF products and reduced the minimum initial subscription threshold for those investors to €100,000. This has added to the attractiveness of the QIF product for promoters of proposed and existing Irish QIF structures. In particular, it is anticipated that these amendments will be of significant interest to fund promoters who are considering the redomiciliation of previously unregulated funds to Ireland under the recently enacted Irish redomiciliation provisions. These new provisions facilitate a straightforward migration process to Ireland by way of a 'continuation' for corporate investment funds from the Cayman Islands, British Virgin Islands, Jersey, Guernsey, Bermuda and the Isle of Man. Similar principles are applied to migrating unit trust structures.

Other recent regulatory initiatives include permitting the establishment of share classes with exposure to different derivative contracts within retail funds, including Ucits.

HFM: Overall, what are the primary opportunities and threats facing Irish domiciled and serviced alternative investment funds?

SL: There are significant opportunities for AIFs. In times of increasing market volatility, there is a considerable appetite for strategies that offer diversification from and protection against traditional long only approaches to equity and debt markets.

The considerable problems faced by markets in recent years have also made such strategies more familiar and attractive to retail investors. This, in turn, has led managers to establish retail products, including Ucits, that will enable them to offer such strategies to retail investors. The challenge in bringing these strategies to retail markets is to ensure that the increased regulatory scrutiny to which retail products are subject will not result in a dilution of the strategy to the extent that it will fail to provide such investors with the optimum benefits that the strategies can offer. In Ireland, the unique experience of having the same regulator and advisors interacting on both traditional regulated products and alternatives over many years should reduce the risk that alternative strategies are not modified unnecessarily as they are adapted for a different and wider market.

HFM: The AIFMD looms on the horizon for alternatives providers – how well equipped is Ireland to deal with its implementation?

SL: As noted above, Ireland is the world's largest centre for servicing AIFs, with 43% of the global hedge fund market; €193bn of those assets are in Irish-domiciled non-Ucits funds, principally QIFs.

The QIF is the leading regulated AIF vehicle and Ireland as a jurisdiction is very well placed to become the leading jurisdiction for AIF domicile post-AIFMD. The Irish Central Bank has a long history of regulating AIFs, Irish administrators have the necessary expertise to perform independent valuations, Irish custodians have extensive experience providing custody and oversight services to AIFs and Irish professional service firms have a proven track record of excellence and innovation. ■

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