Industry Professionals serving as non-executive directors to Alternative Funds

This edition of IPAF's newsletter comes from Brian O'Callaghan, resident in Malta. Brian has previously worked as both a CEO and COO of alternative funds and specialises in operations, risk and regulation. He asks you to consider whether Malta can be Robin to London's Batman…

If London is Batman, can Malta be Robin?

London remains the undisputed hub of the European investment management sector, but every Batman can use a Robin, and in recent years, Malta has been making an ever stronger case to be London's "Robin". As an EU fund domicile, Malta has been in the picture for most of the past decade and it is increasingly being considered as a jurisdiction for fund managers, or at least a part of the fund management structure. Transfer pricing requirements of the UK's HMRC and the implementation of AIFMD have made Malta's value proposition for this role ever more compelling.

Malta offers opportunity to put genuine presence in the AIFM domicile

Few jurisdictions can compete with London's talent pool, its abundance of capital allocators (whether by permanent or frequent presence), and the flow of ideas and market colour that swirl on a continuous basis. This all comes at a price of course, and London's is exacted through a high cost base and relatively high taxation (and the weather, some might argue). Where fund group structures have sought to mitigate their tax exposure, a Cayman based management company that retains some fees has traditionally been the solution of choice. To be sure, Cayman is a first rate jurisdiction, but fund managers are increasingly mindful of the challenges of establishing genuine presence from a transfer pricing perspective, as well as the need to maximise the potential to market funds across the EU with an AIFMD facilitated passport. Taxation considerations, the need for local substance, the cost and convenience of that substance, and the AIFMD positioning of the group are all critical considerations. It is within this context that Malta shines as an attractive potential solution for fund management groups.

Lower cost base but a strong pool of English speaking, skilled workforce

An AIFM in Malta can market its funds across the EU under the passporting rules, while benefiting from Malta's advantageous dividend taxation policy. Establishing a fund management company in Malta naturally requires local substance but this can be viewed more as an opportunity than a challenge, given Malta's low cost base relative to London. Malta has a well-educated and English-speaking workforce, a strong IT infrastructure and, although only an hour's time difference and a reasonably short flight from London, a Mediterranean climate that boasts 300 days of sunshine per year. Most importantly, in the MFSA, it has a regulator that has gained a well-deserved reputation for being rigorous, yet highly accessible.

Risk management out of the Maltese Batcave

The MFSA will consider approving AIFMs where either portfolio management or risk management has been delegated in its entirety (though liability remains with the AIFM). It will also consider cases where both have been partially delegated. With London's undisputed pre-eminence in portfolio management, a compelling solution is for the Malta based AIFM to delegate portfolio management to the London investment advisor (sub-manager), while retaining the risk management function and possibly other operational support functions.

No 'look through' when implementing the ESMA's remuneration policy

There is an additional benefit to utilising a structure with a Malta domiciled AIFM and a London based advisor, which is perhaps less well known. The AIFMD remuneration provisions are well-intentioned and may represent a positive long-term development; however, for some investment managers, the rules might be too prescriptive and rigid for the manager's particular circumstances. In this regard, the MFSA has implemented ESMA's guidelines on the remuneration policies but has decided against imposing these on a look-through basis. As explained in its June 2013 newsletter, "The approach adopted by the MFSA does not require that entities to which portfolio management or risk management activities may have been delegated be subject to similar remuneration requirements as the AIFM." Consequently, a business structured in this way retains a high degree of flexibility in structuring its compensation policies and the risk management professionals in Malta are less likely to be affected by the most restrictive provisions.

Holy Hedgies Batman, what do we do now?

Each fund manager has its own needs and every jurisdiction has its own advantages, so it would be wrong to suggest that there is an optimal solution that will suit everyone. A Malta domiciled AIFM does, however, offer a solution that enables fund management groups to preserve access to London's key advantages in the portfolio management sphere, while enhancing the overall economics and flexibility of the business. To the batcave...?

About Brian O'Callaghan

Brian O'Callaghan has served as CEO and COO of investment firms in the alternative funds industry, specialising in hedge and private equity funds. After graduating from Harvard with a BA in Economics, he worked in strategy consulting with SJH & Co and then became a CDS broker in Hong Kong and London for Tullett & Tokyo. In 2002, Brian co-founded Holte Capital, a European special situations hedge fund. Brian managed the start-up of the business and was COO for five years. Most recently, his positions have been in frontier markets, firstly as CEO of Renaissance Investment Management UK Ltd, where his experience included open and closed-ended funds, as well as a private equity infrastructure fund. Additionally, he oversaw the establishment and later sale of a Dubai subsidiary office and fund. In 2010 Brian was appointed CEO of Compass Asset Management in Almaty, Kazakhstan, where the investment focus was on Central Asia, through both public markets and private equity. He left in 2012 to focus on international independent non-executive directorships.

About IPAF

IPAF provides Industry Professionals – independent, knowledgeable and experienced people - as non-executive directors to Alternative Funds. IPAF is run from London with a panel of 16 directors across 9 jurisdictions: Cayman, Luxembourg, Ireland, Switzerland, the Channel Islands, Malta, Bermuda, Barbados and the UK. All the IPAF directors are independent of each other and no additional fee is charged by IPAF to a fund that selects a member of its panel: the fund only pays the director's fees. For more information please telephone 020 7340 6316 or email info@ipafgroup.com.