Jersey: The Trends, Opportunities and Challenges for its evolving Alternative Funds Ecosystem

The COVID-19 pandemic has caused such a devastating impact on human life and health, and the global economy. As a consequence, the funds industry has faced unprecedented challenges, as it continues to navigate through unchartered waters.

Before the pandemic, many institutional investors and pension funds had increased their allocations to alternative investment funds sector. Due to the extreme market volatility, low asset valuations and lack of liquidity caused by the pandemic, many businesses are managing liquidity crises and the markets remain uncertain for foreseeable future. Whilst market volatility and low valuations present opportunities for some investors, more cautious investors are considering more passive investing in these times, which should stimulate further growth in alternative investment funds sector.

The Jersey funds industry has remained resilient with net assets under administration up 5.7% year on year standing at £361.7 billion, with alternative investment funds representing 87%. Noticeably, private equity was up 19% year on year and managers using Jersey to market funds into the EU increased by 9% year on year.

With over a 50-year proven track record, Jersey is internationally recognised as a first-class and well-regulated domicile for funds and managers. Although close in proximity to the UK and EU, Jersey is independent, which provides political, economic and fiscal stability, as well as offering tax neutrality with substance, and a flexible regulatory regime. As a jurisdiction, Jersey cooperates with global authorities and meets all international standards. It also has wide choice of flexible and innovative entities and fund products with fast-track procedures, supported by a world-class infrastructure with high-quality professionals, service providers and non-executive directors.

This platform forms the basis of an essential ecosystem providing a perfect environment for Jersey's alternative investments funds to evolve, grow and thrive, whilst meeting the needs of managers and investors.

Q What are the key trends currently driving growth and development within the Jersey funds industry?

Despite the challenges and impact of COVID-19, the Jersey funds industry has seen continued growth and development in new funds and investment structures. This year, many funds were opportunistic in nature, taking advantage of the volatile markets, the lower valuations and distressed assets. Across the asset classes, private equity and venture capital funds were the most prominent, particularly those focused on technology, Fintech, health and financial services, as these sectors continued to thrive in the current climate. With many businesses struggling with liquidity issues due to the prolonged pandemic, distressed asset funds and credit funds have also been on the rise. Many hedge funds have taken advantage of the market volatility, reporting strong performances. Other than infrastructure funds, the real estate sector has been slow this year, however, some funds have raised capital ready for when the market picks up again.

Jersey has proven to be popular for acquisition and alternative investment vehicles, taking into account their unregulated status and no audit, custody or valuation requirements. Many co-investment, joint venture, managed account or single asset investment structures formed were opportunistic in nature, as managers wanted to take advantage of good investment opportunities. Other vehicles had defensive objectives, such as side pocket arrangements to hold underperforming or hard to sell or value assets.

Due to the proximity to the UK and Europe and offering stability, governance and substance, Jersey continues attract new managers, which are either hosted by a local service provider or a 'full presence' manager, with promoters ranging from the institutional or well-known and established players to the start-up managers.

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How has the jurisdiction fared over the course of the pandemic?

As an island, Jersey responded and adapted well to mitigate the impact of the pandemic. The States of Jersey introduced emergency laws addressing public health concerns, imposing non-essential travel restrictions, physical distancing and lockdown measures. When borders re-opened, a free testing system was implemented with contact tracing, permitting travel.

The Jersey Financial Services Commission ("JFSC") and the Jersey Comptroller of Revenue ("Comptroller") recognised the challenges faced by Jersey's funds industry and they took a pragmatic and flexible approach, introducing measures and relaxing certain procedures to help the industry maintain 'business as usual'. The JFSC extended regulatory filing deadlines for funds and managers, and accepted electronic signatures on application forms submitted using its online portal, which greatly helped with fund and entity formations. It also allowed electronic identification for client due diligence, instead of original 'wet-ink' documents, to facilitate client and investor take-on. The Comptroller relaxed the economic substance requirements, so that Jersey companies would not fail to meet the substance test, where it had to make temporary adjustments to its normal operating practices to mitigate the effects of COVID-19, which allowed directors, who were unable to travel, to attend fund or manager board meetings by telephone.

The Jersey funds industry was robust and also adapted well to challenges faced. Service providers' businesses and working practices completely changed overnight with businesses transitioning to remote working operations. This led to an increased use of technology, in particular video conferencing for meetings to maintain contact and conduct day-to-day business, and online portals and secure file sharing for managers' and investors' access to information.

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How are these trends impacting your organisation's objectives?

Although previous recessions and market crashes have been experienced before, the pandemic presented new challenges and we found that our clients needed more timely support and guidance

on a wide range of legal and regulatory issues. With our global network of 18 offices worldwide, we have the benefit of a deep bench of expertise and know-how globally and this has ensured that we can continue to provide the most innovative and efficient solutions for our clients at all times.
Whilst new fund and manager workflows have helped us achieve our financial objective, we have to ensure that our teams are appropriately resourced with the most effective systems and back office support, to enable us to meet our client-focused service objective.

With more reliance on technology this year, our continued investment in our technology and infrastructure platforms has ensured that we have efficient, secure and fail-safe systems in place, particularly using secure file sharing sites and online portals for our clients.

Q Jersey is looking to appeal to US managers, particularly in light of Brexit. What has your experience been in this regard and how do you see this initiative developing going forward?

Jersey provides a stable, flexible and cost-effective solution for Jersey-based managers and as a result, there has been an increase in the number of Jersey-based managers recently. Having advised our US manager clients who focus on Europe, we continue to see a growing interest in this area. Jersey has worked hard to raise its profile in the US, and this is supported by industry and Jersey Finance who, having opened their New York office last year, are proactively promoting the jurisdiction. With the ability for non-domiciled funds to be managed in Jersey, combined with the introduction of the procedure for the migration of limited partnerships into Jersey this year and the US-style LLCs next year, Jersey should appeal to US managers.

Being closely situated to the UK and Europe and outside of the EU, Jersey funds and managers have access to the EU/EEA market through the national private placement regime ("NPPR"). As most funds only target a select number of EU/EEA markets, Jersey provides sufficient access on a lighter-touch regulatory basis. As ESMA approved, Jersey is also ready if the third country EU passporting is 'switched on' in the future.

With the end of the Brexit transition period fast approaching on 31 December 2020, if no agreement is reached before that date, the UK will become a third country and lose its EU passporting right. UK funds and managers will only be able to market in the EU through the NPPR. As the EU still wants non-EU funds and manager to have access to the EU, it is unlikely to close the NPPR. As the UK and Jersey will be in the same position, Brexit should bring them closer together. This should potentially present more manager opportunities, as Jersey has the advantage of tax neutrality, a lighter regulatory touch or, an exemption if managing a Jersey private fund, faster authorisation process and lower costs.

Q Can you outline the primary challenges your clients in Jersey are facing at the moment and how your services are helping them overcome these difficulties?

Clients experienced unprecedented challenges this year, with the impact continuing as the 'second wave' is combatted. As with our Corporate and Finance practice clients, fund managers have also had to deal with crisis management, being forced to implement business continuity plans to protect their staff and businesses, transition to remote working operations, and adapt to conducting business virtually. With an increased reliance on technology and IT, data and cybersecurity risks had to be monitored.

For funds managing to launch, new challenges were encountered with fund raising and investor take-on. Face-to-face investor meetings were replaced by virtual meetings, and online portals and secure file sharing sites were used for sharing and exchanging fund, due diligence and know your client documentation.

Completing cross-border fund closings and investment transactions, came with their own complications. In light of travel restrictions and social distancing measures, boards had to consider new protocols for meetings to ensure continued compliance with corporate governance and tax requirements. For document signing, most parties accepted electronic signatures, but in some cases 'wet-ink' signatures were still required, for instance, and witnessing signatures was also difficult.

Many funds and portfolio companies have experienced valuation difficulties and liquidity issues, particularly those exposed to the hospitality and retail sectors, requiring emergency funding as revenues fell, potentially resulting in loan covenant breaches. Some open-ended funds had to carefully manage redemptions or seek short-term funding, once reserves exhausted. Against this background, whilst managing these liquidity crises, fund and managers still have had to ensure that accounting standards and valuation principles are followed, and regulatory and tax filings are met.

In addition to the pandemic, UK and EU managers and funds have also had to assess the implications of the UK losing its EU passporting right and the impact on existing cross-border delegation arrangements, requiring the possible restructure of those arrangements.

Leveraging the broad capabilities within the Maples Group's global network, we have been able to guide our clients through these difficult times, providing timely advice to help them resolve or manage their issues or crises. The pragmatic and flexible approach taken by JFSC and the Comptroller has greatly helped us to facilitate transactions, form new entities and appropriately advise our clients. Our global IT team and systems have enabled us to use secure file sharing sites for investor take-on, due diligence and transactions.

Q What changes have you observed in client needs in Jersey? Which have been the most significant and how have you responded to these new demands?

Clients have had to contend with a multitude of issues, as well as navigating the complex corporate governance, tax and regulatory requirements. Most significantly, our clients have needed more support and guidance, and in cases of emergency, urgent, practical and clear advice, covering many complex areas. We quickly identified and contacted clients who we thought may require our support, just to let them know we could help, if required. We have had be responsive, flexible and innovative, as well as offer practical options and solutions.

Q What are the most significant developments you expect within the Jersey funds industry over the coming year?

A significant development will be the launch of the Jersey LLC, which is based on US LLC, as a flexible vehicle for a fund, manager or SPV, which should increase Jersey's appeal to US managers. We will closely monitor AIFMD II, which should have minimal impact on Jersey. OECD BEPS and the Pillar One and Pillar Two blueprints will also be monitored to track if there will be a workable carve-out for fund vehicles.

Another hot topic is environmental, social and governance ("ESG"), as managers are now more aware of their responsibilities to the environment and are looking to factor ESG into their operations and investment processes. Jersey has actively encouraged sustainable finance. The JFSC is committed to maintaining ESG international standards, where applicable and proportionate to Jersey. Depending on the outcome of the JFSC's consultation paper concerning ESG, the regulatory codes of practice applying to Jersey funds and managers are likely to be revised to include certain ESG requirements, covering disclosure and 'greenwashing'.

Q What are the key objectives over the coming year to ensure the Jersey financial industry remains a competitive global jurisdiction?

In order to remain competitive, a key objective is to enhance Jersey's excellent reputation as a well-regulated, stable, flexible and cost-effective domicile for funds and managers, and for its exceptionally high standards of service and governance. To achieve this, Jersey will need to continue to cooperate with the EU and other global authorities, particularly in relation to ESG, OECD/BEPS and AIFMD II; continue to strengthen its relationship with the UK following the transaction period; continued promotion of the jurisdiction to the Americas, Asia and the Middle East; and enhance its vehicle and fund product range, in particular, promoting LLCs to attract US managers.

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