

# Exchange Traded Notes ('ETNs')

Since Barclays Bank issued the first ETN in June 2006, marketed as iPath Exchange Traded Notes, the ETN market has boomed in a relatively short space of time, reaching around \$7.5 billion in July 2008. Although ETNs, like many structured finance products, have taken a fall in the last year, commentators suggest that the ETN market will recover and remain a popular choice of investment.

Jersey remains a popular jurisdiction for the creation of ETN issuance vehicles and this briefing outlines some of the benefits of using Jersey and Ogier for ETN structures.

## What are Exchange Traded Notes?

ETNs may be senior, unsecured debt securities of an issuer like a bank designed to track a specified index or commodity but may also be asset-backed securities issued as secured limited recourse securities for a special purpose entity issuer. They can also be referred to as exchange traded securities. The return on an ETN is based on the performance of an underlying index or strategy, less fees. Although they are traded on an exchange, unlike equities or index funds (Exchange Traded Funds) they do not own anything they are tracking but instead typically use derivatives to track the underlying index. ETNs can be tax efficient and provide investors with a liquid product with access to new markets and strategies.

## Advantages of Jersey as a jurisdiction generally

Jersey has proven to be popular as a jurisdiction for the incorporation of issuing entities for many structured product transactions, including ETN structures. It is in the same time zone as London and there are close links between the major financial centres of Europe and Jersey. Such features and those set out below enable Jersey entities to be structured to meet a wide variety of business purposes.

Advantages of Jersey include the following:

- **Tax neutrality.** An SPV will be established as a 0% rated company for income tax purposes and, it will, therefore, not be liable to pay any Jersey income tax, and any notes and/or any equity issued by it will not be subject to withholding tax.
- **No stamp duty on transaction documents or notes.** Unlike a number of other jurisdictions, Jersey has no stamp duty except in respect of Jersey real property. This removes a complication that can otherwise impact on the closing of a transaction and the execution of relevant documents.

- **Established commercial legal framework** based in the main, upon established English law principles. The Companies (Jersey) Law 1991 (the "Companies Law") has been updated in recent years and draws on many of the provisions of the equivalent UK and other common law jurisdictions' statutes. As a consequence, the principles that apply in Jersey will be familiar to many practitioners and arrangers based in London. The Companies Law imposes no requirements relating to thin capitalisation or moratorium on insolvency.
- **Corporate advantages.** The benefits of using a Jersey company in terms of company law provisions are extremely wide, and generally include separate legal identity, limited liability for shareholders and ease of transfer of ownership. The Companies Law enables capital to be denominated in any currency and share capital of either par value or no par value shares to be issued in various classes, including redeemable shares. It also allows for the incorporation of guarantee companies, unlimited companies and cell companies (the latter providing particular flexibility).
- **Speed of the regulatory authorities** in issuing the relevant consents to securities issuing vehicles. The Jersey Financial Services Commission's (the "JFSC") published response time in dealing with applications for consents under the Control of Borrowing (Jersey) Order 1958 and the Companies (General Provisions) (Jersey) Order 2002 is five business days. The approach taken is that of a "gatekeeper", where the entry requirements are checked carefully but there is no annual review process; the JFSC will be concerned to ensure that complex debt instruments are not being offered to ineligible investors, that the promoters are organisations that are recognised in the marketplace and that the proposed activities of the SPV are not likely to detract from Jersey's reputation.
- It is a **member of the OECD and on its White List of Offshore Finance Centres.** Some investors will be subject to investment restrictions requiring that the SPV is located in an OECD member country.
- Well established as being **acceptable to the rating agencies.**
- **Political stability**
- **Speed of incorporation.** A Jersey SPV can usually be established within 24 hours.
- **Quality of financial services providers.** Jersey has had a thriving financial services sector for over thirty years, and there is a strong body of law firms,

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administrative services providers and accountants on the Island.

- **Competitive costs** of legal, accounting and administrative services.

## Suitability of Jersey for derivative transactions common to ETN structures

Jersey is a 'netting friendly' jurisdiction and Ogier currently are ISDA appointed counsel in Jersey. The Bankruptcy (Netting, Contractual Subordination and Non-Petition Provisions) (Jersey) Law 2005 (the "**Netting Law**") enshrines the enforceability of contractual netting and set-off arrangements as part of Jersey's statutory laws.

The Netting Law provides that, despite any enactment or rule of law to the contrary, a close-out netting or a set-off provision (both such terms being defined broadly) contained in an agreement is enforceable in accordance with its terms. This is the case despite the bankruptcy of a party to the agreement or of any other person, or the lack of any mutuality of obligation between a party to the agreement and any other person.

## How are ETN issuers treated in Jersey for regulatory purposes?

Regulatory treatment in Jersey will primarily turn on whether the structure is regarded as a collective investment fund or not.

English law analysis usually points to an ETN as being outside UK "collective investment scheme" scope and it can be possible for a similar conclusion to be reached in Jersey

The Collective Investment Funds (Restriction of Scope) Jersey Order 2000 carves out from the funds regime any scheme established for the principal purpose of 'securitisations' or 'repackaging assets' and involving the issuance of securities. If this exemption can be relied on the issuer will essentially be treated as a debt issuing SPV and benefit from what is a "light-touch" regulatory regime which is highly developed as a result of Jersey's track record in securitisation and structured finance over many years.

Even if the conclusion is that the structure is to be regulated as a fund for Jersey purposes, Jersey now offers a number of choices of regulatory regime for investment funds which make the path to the launch of an exchange traded fund a simple one.

## Would ETNs fall foul of any anti-gambling legislation in Jersey?

No, unlike many jurisdictions, Jersey's gambling legislation does not restrict the use of ETNs. Article 12(2) of the Gambling (Amendment No. 3) (Jersey) Law 1995 provides for a carve out for 'dealings in investments' from

the general prohibition against all forms of gambling. As ETNs fall within the definition of 'investment' as set out in the gambling law, they have the benefit of this carve out.

## Why Ogier?

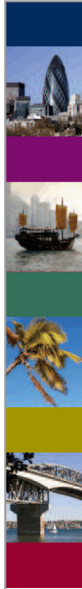
- Ogier has worked on a number of exchange traded fund structures established in Jersey including one of the market leaders. We have also been active in structured product issues (debt form) and have worked on index-linked and similar securities for many years. Details of our track record in this area are available on request.
- **One stop shop** - Ogier can provide legal and administrative services seamlessly, an area in which Ogier has international recognition.
- Ogier is **ISDA Counsel for Jersey**. The Ogier Derivatives Team is recognised internationally as a leading offshore practice.
- We can form ETN SPVs within 24 hours, administer them and provide legal services in relation to the most **complex transactions**. (We can usually obtain regulatory consents within 4-5 working days.)
- Legal Services - Ogier was named "**International Law firm of the Year, 2009**" at the annual City Wealth Magic Circle Awards and is consistently rated a top offshore law firm by the leading legal directories.

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## About Ogier

Ogier is an award winning offshore legal and fiduciary services provider. The Group advises on all aspects of BVI, Cayman, Guernsey and Jersey law and associated fiduciary services through a global network of offices covering all time zones and key financial markets.

Ogier continues to be recognised as a leading law firm by the principal legal directories, including Legal 500 and Chambers.



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