Channel Islands Funds Quarterly Update: Q2 2020

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1 Developments in the Channel Islands

1.1 Mandatory Disclosure Rules

As reported in a previous briefing (Channel Islands Funds Quarterly Update: Q4 2019), the Government of Jersey has been consulting with stakeholders on the introduction of Mandatory Disclosure Rules (**MDR**). Draft regulations (the Taxation (Implementation) (International Tax Compliance) (Mandatory Disclosure Rules for CRS Avoidance Arrangements and Opaque Offshore Structures) (Jersey) Regulations 202-) were lodged au Greffe on 31 December 2019 and were approved at a first reading by the States on 16 June 2020. The draft regulations closely follow the MDR regime published by the OECD, which is the international standard for MDR. The intention is that these draft regulations will be supplemented by guidance to be published by the Comptroller of Revenue, which will assist industry in making the important "reasonable to conclude" decision when considering whether or not to report specific arrangements or structures.

Under the MDR regime, Jersey promoters and service providers will be required to provide the Comptroller of Revenue with information on avoidance arrangements and opaque offshore structures.

We are anticipating that the new MDR legislation will come into force by the end of the year and industry will need time to make changes to their systems in order to be ready for the new reporting obligation.

The Income Tax (Approved International Agreements) (Implementation) (Mandatory Disclosure Rules) Regulations, 2020 (the **Guernsey Regulations**) were passed by the States of Guernsey on 11 March 2020, with a commencement date yet to be announced. The Guernsey Regulations require Guernsey based "intermediaries" and in certain cases those considered to be reportable taxpayers using opaque offshore structures and/or Common Reporting Standards avoidance arrangements, to report certain information about those structures and arrangements to the Guernsey Revenue Services. The Guernsey Revenue Services will then exchange information relating to users of such reportable arrangements resident in another jurisdiction to the tax authority of that jurisdiction.

With the EU adopting DAC6 and Jersey and Guernsey adopting MDR, the result for Channel Islands structures is that they may be in scope for both regimes.

2 Jersey developments

2.1 Deadline for submission of JPF annual compliance return extended

Mindful of the challenges businesses have faced during the Covid-19 pandemic and the potential challenges in meeting regulatory deadlines, the Jersey Financial Services Commission (**JFSC**) has extended the deadline for submitting a Jersey Private Fund (**JPF**) annual compliance return by one month, from 31 July to 31 August.

The JFSC has also published guidance on completing the return based on its experiences over the past two years. Designated service providers (**DSPs**) need to demonstrate a clear understanding of their responsibilities to JPFs under the JPF Guide.

Key points are:

- Only investors who have confirmed receipt and accepted the disclosure statement and investment warning are eligible to invest in a JPF. Equally, if the JPF is also structured as a professional investor regulated scheme, there are additional requirements that relevant warnings are received and acknowledged in writing by investors – all of whom have to be professional investors as determined by the Financial Services (Investment Business (Restricted Investment Business - Exemption)) (Jersey) Order 2001 and/or the Financial Services (Trust Company Business (Exemptions No.5)) (Jersey) Order 2001.
- Material issues need to be notified to the JFSC within 28 calendar days. DSPs should not wait until the annual return to make a notification of a material issue, such as the winding up of a JPF.
- The JFSC expects DSPs to confirm they are performing their due diligence and AML duties in line with the requirements of the JPF Guide and the Money Laundering (Jersey) Order 2008. If a DSP is unable to confirm compliance with these requirements due to ongoing remediation, this needs to be notified to a DSP's JFSC supervisor before submitting the compliance return.

The extension notification and guidance can be found here:

Deadline extended for JPF Annual Compliance Returns

2.2 Outsourcing Notifications to be submitted online

As from Monday 29 June, the JFSC will only accept Outsourcing Notifications online via myJFSC portal. Paper submissions will no longer be accepted. If you need to set up a portal user, you can send your request to the JFSC Regulatory Maintenance team: RegulatoryMaintenance@jerseyfsc.org. Note that the user of the portal needs to have the appropriate seniority to submit the notification and the JFSC expect this would usually be a Key or Principal Person.

The JFSC update can be found here:

Move to digital outsourcing notifications from 29 June

2.3 JFSC consultation on changes to fund fee rates

On 22 May 2020, the JFSC issued a consultation paper which sets out proposals for fund fee rate changes. Although the period to provide comments closed on 22 June 2020, industry should be aware that the JFSC is proposing to increase FSB, AIF and CIF, CoBO and QSMA fees by 12.5% (with 2.7% being the most recent Jersey RPI). The main driver of this above-inflation increase is the JFSC's aim to significantly enhance its supervisory and compliance function and to provide some additional capital for investment in technology.

Further detail is in the consultation paper and the feedback paper, which can be found here:

Fund fee rates from 1 July

2.4 JFSC Annual Report 2019 published

For the JFSC, 2019 was a year of prioritising and planning, which is reflected in its annual report and financial statements. The report documents the regulator's performance during the year and its comprehensive review of its activities in order to plan its strategy for the next four years.

Key achievements for 2019 include:

- working with the Government of Jersey on the Island's National Risk Assessment, securing access to UK markets ahead of Brexit;
- setting up a dedicated team for fighting financial crime;
- implementing a comprehensive risk framework; and
- launching a new website.

While the JFSC made a surplus in 2019, for the next four years the regulator is embarking on its largest capital programme to date. Its primary aims are to remain ahead of the financial crime threat and become an even more effective regulator.

Access the Annual Report here:

JFSC Annual Report 2019

2.5 Migration of foreign limited partnerships into Jersey

It will shortly be possible to migrate (continue) foreign limited partnerships into Jersey using the statutory migration process set out in new regulations, the Limited Partnerships (Continuance) (Jersey) Regulations 202- (the **Regulations**) which will be debated by the States of Jersey on 14 July 2020.

Read our briefing here:

Migration of foreign limited partnerships into Jersey

2.6 JFSC consultation on Environmental, Sustainable and Socially Responsible Investing for Funds

In response to international reforms in relation to ESG, the JFSC has issued a consultation on proposals to enhance disclosure and governance requirements for investment funds committing to sustainable investments. The proposed changes will potentially impact Jersey funds and fund service providers.

Read our briefing here:

JFSC consults on environmental sustainable and socially responsible investing for funds

We are happy to collate responses from clients and other contacts wishing to engage in this process. The consultation period closes on 30 September 2020.

2.7 Jersey LLC law paves the way for new offering

It is anticipated that limited liability companies will be available for use in Jersey by the end of the year. The Limited Liability Companies (Jersey) Law 2018 will, once in force, create a new structure in Jersey which is similar to the Delaware LLC model. This will offer a new structuring option that is tax transparent and which offers the limited liability protection of a company and the flexibility of a partnership in one vehicle.

Read our briefing here:

Jersey LLC law will build on Island's offer to US clients

2.8 Asset freeze designations will now be published on the Jersey Gazette

Notices of changes to asset freeze designations will now be published on the Jersey Gazette. In order to receive alerts when new notices are published, you can register to receive notification by email.

Notices will be published when:

- individuals or entities have been designated for the purpose of an asset-freeze;
- the details of existing asset-freeze designations (e.g. identifying information) have been changed; and
- individuals or entities are no longer subject to an asset-freeze.

The Notices will include identifying information on the asset-freeze designations and what relevant financial institutions must do, as well as legislative details and other relevant information. Detailed guidance on financial sanctions can also be found on the JFSC website.

2.9 Guidance on wrongful trading

The guidance issued by the Law Society of Jersey (in conjunction with the Government of Jersey and the Viscount) for directors of Jersey companies can be found here:

Wrongful trading under Jersey law practice statement

The guidance concludes that directors of a Jersey company should not be penalised under the Jersey wrongful trading provisions if they take reasonable steps to minimise the potential loss to creditors.

2.10 JFSC consults on revisions to the AML/CFT Handbooks

On 28 May 2020, the JFSC issued a consultation paper asking for feedback on proposed revisions to the AML / CFT handbooks. The deadline for comments is 31 July 2020. The revisions are required in order to implement the 2012 FATF Recommendations, specifically in relation to:

- business risk assessments;
- customer due diligence;
- reliance;
- equivalent countries and territories; and
- merging the AML/CFT Handbooks.

2.11 Case confirms JFSC's extraterritorial power

In a recent case heard by the Royal Court in Jersey (Guardian Global Capital (Suisse) SA v JFSC 29-Apr-2020), it was held that that on a proper construction, the JFSC had power under Article 32(2) of the Financial Services (Jersey) Law 1998 to compel a foreign entity to produce documents held in Jersey through one of its officers in Jersey in connection with an investigation as to whether the foreign entity was carrying on unauthorised trust company business in Jersey.

The court also found that legislation does not have extraterritorial effect unless that intention appears; rather it is a question of construction.

3 Guernsey developments

3.1 GFSC Support for Financial Services Industry

The Guernsey Financial Services Commission (the **GFSC**) is maintaining its efforts to monitor financial stability issues across Guernsey's financial services sector as result of the COVID-19 pandemic. As part of this, the GFSC considers it essential that firms continue to make accurate regulatory returns in a timely manner. The GFSC appreciates that some firms may encounter challenges in their interactions with some third parties in preparing their regulatory returns and in such instances, the GFSC is willing to receive requests for third party sign off to be delayed.

The GFSC also expects firms to manage their financial and operational resilience including actively managing their liquidity. Firms should report to the GFSC immediately if they believe they will be in difficulty rather than delaying speaking to the GFSC. For example, the GFSC expects firms to be monitoring their financial resources requirement and having early conversations with them as soon as they are aware that they might breach such requirement at a foreseeable date in the future.

3.2 Updated deadlines for Key Financial Returns

The GFSC has confirmed that firms have an additional month to submit the relevant returns due to be submitted at the end of May, June, July, August and September 2020. After 1 October 2020, all new returns will revert to the normal submission schedule. It should be noted that only the submission dates of such returns have been extended by one month, the information reporting dates for quarterly returns remains unchanged.

In addition, the GFSC has temporarily relaxed the requirement for audited financial statements to be submitted until 1 October 2020.

3.3 GFSC warns licensees of increased risk of fraud arising from COVID-19

Licensees and registered business have been requested by the GFSC to stay attuned to the heightened risk of fraud facing their business, as the sophistication of fraud schemes is likely to evolve as a result of COVID-19. Such imminent threats include:

- third party impersonation fraud, i.e. the risk that a third party may impersonate an individual or business to extract payment;
- first party application fraud, i.e. the risk that an applicant may misrepresent their circumstances to qualify for a payment or loan; and
- increased risks of phishing and other cybercrimes.

The GFSC recognises that firms may have to amend their processes and procedures to accommodate customer and client circumstances and, while these changes are necessary, firms should ensure that potential weaknesses in amended processes are fully assessed, addressed and documented and that all relevant staff are made aware of the increased risks.

It is expected that licensees continue to apply effective fraud controls, which could include, although are not limited to:

- undertaking or updating the licensee's fraud risk assessment;
- ongoing scanning for new threats and risks, including through the increased use of remote working;
- integrated fraud control as part of the licensee's policies and procedures, including continuing efforts to prevent cybercrime;
- continuing upfront controls to identify and verify individuals and businesses, including the beneficiary's account details as a means to prevent fraud taking place; and
- using upfront fraud prevention clauses in application forms and processes (including call scripts) to make applicants aware of how their data will be used and their legal obligations.

3.4 Cannabis Funds

The GFSC has been approached by a number of organisations regarding its appetite to register or authorise collective investment schemes (**CIS**) which would make cannabis related investments under section 8 of the Protection of Investors (Bailiwick of Guernsey) Law, 1987.

The GFSC would never countenance an authorised or registered CIS investing in something which would be illegal either in the jurisdiction of the asset or in the Bailiwick of Guernsey. Further, the GFSC expects the directors of such funds, the administrator and the promoter to give careful consideration to, and obtain legal advice on, both the legality of the investment in the jurisdiction where the investment is made and, in particular issues relating to the Criminal Justice (Proceeds of Crime) (Bailiwick of Guernsey) Law, 1999 and the Misuse of Drugs (Bailiwick of Guernsey) Law, 1974.

Subject to the GFSC's normal requirements and processes in relation to the authorisation or registration of CIS, the GFSC would be willing to consider applications for registration or authorisation of a CIS which invested in the following classes of cannabis related investments:

- synthetic or biosynthetic production of cannabinoids;
- pharmaceutical research, development and sales;
- medical research, development and sales;
- production solely for the purposes of medical, pharmaceutical or wellness sectors;
- wellness CBD products.

The GFSC would not consider CIS where one of the investment classes was the production, sale or marketing of recreational cannabis products.

For further information, please refer to our briefing:

Investment by Guernsey vehicles into cannabis and other drug related assets

3.5 Resumptions of onsite inspections

The GFSC announced on 8 June 2020 that its Financial Crime Division would be recommencing its routine financial crime inspections of firms with immediate effect. The routine inspections were suspended on 19 March 2020 to enable firms to deal with the immediate operational impact of COVID-19, but are now resuming as the financial sector has demonstrated its resilience and firms have generally adapted to new methods of working.

3.6 GFSC Annual Report 2019 published

The GFSC Annual Report and Accounts for 2019 (the **Report**) was published on 12 May 2020 and provides a comprehensive overview of the activities the GFSC has undertaken over the year, together with a detailed analysis of the income it received, the expenditure it incurred and its overall financial position moving into 2020.

Since the Report was prepared, the world's circumstances have changed fundamentally with the arrival of COVID-19. The extraordinary measures taken by governments worldwide in response to COVID-19, have significantly altered any forward-looking statements. As such, the GFSC has had to remove many of the forward-looking statements drafted back in January from the Report, as they were no longer appropriate.

Read the GFSC Annual Reports here:

GFSC Annual Reports

3.7 New Fast-Track Application Regime for Managers of Overseas Collective Investment Schemes

The GFSC has launched a new fast-track application regime for managers of overseas CIS. The intention is to make the process as simple as possible for such managers looking to apply for a Guernsey licence. The regime caters for fast-track applications for managers migrating to Guernsey, as well as those managers looking to establish a new Guernsey entity.

Applications under the fast-track regime are subject to a 10 day review period. For managers looking to migrate to Guernsey, the Commission has helpfully combined its consent to migrate along with the licensing process.

Read our full briefing here:

Guernsey introduces new fast-track licensing regime for managers of overseas collective investment schemes

For related information from our Guernsey relocations team:

At A Glance Guide to Guernsey's Relocations Team for HNWIs

3.8 Handbook on Countering Financial Crime and Terrorist Financing

On 19 June 2020, the GFSC issued, in final form, the revised Handbook on Countering Financial Crime and Terrorist Financing (the **Handbook**).

The GFSC has made various amendments to the Handbook in order to take into account the Bailiwick of Guernsey's National Risk Assessment on money laundering (**ML**) and the financing of terrorising (**FT**), which was published earlier this year. It is intended that the changes will assist firms in identifying high risk countries and territories for both ML and FT purposes. In particular, the GFSC has created two new appendices:

- Appendix H, which lists those countries and territories which the Financial Action Task Force (**FATF**) has identified with significant strategic deficiencies in their regime to counter ML, FT and financing of proliferation for which it has called for the application of countermeasures; and

- Appendix I, which lists a number of countries and territories that are identified by the UK and US governments, intergovernmental and supranational organisations such as the FATF as presenting certain ML and FT risks. Information reflecting assessments of a country or territory by non-governmental organisations and think-tanks is also provided which firms may find useful when they are determining the level of country risk presented by a business relationship or occasional transaction.

The FATF usually updates its lists three times per year, and the GFSC will amend Appendices H and I shortly after each FATF update.

3.9 Data Protection Registration

The Office of the Data Protection Authority in Guernsey (**ODPA**) has announced that anyone who is currently exempt from the legal requirement to register with the ODPA will now continue to be exempt until January 2021, extending the deadline for registration from 31 December 2019.

Every controller and processor of data is required to work and comply with the Data Protection (Bailiwick of Guernsey) Law, 2017 (the **DP Law**), however, certain exemptions mean that currently there is no need for some data controllers or processors to register with the ODPA.

In broad terms, these exemptions apply to the following three groups:

- those that only process data that is for accounts and record-keeping for core business purposes for staff administration and to market their own goods and services;
- those who only process data under the instruction given by another entity; and
- those who have charity or not-for-profit status.

As from 1 January 2021, all exemptions to registering with the ODPA under the DP Law will end and all previously exempt local entities that are processing or controlling personal data will be legally obliged to register with the ODPA and pay a small annual fee that will contribute to the ODPA's operational activity. While the ODPA has not confirmed what the annual fee will be, they have indicated that it will be between £25 to £50 per year, per entity.

For more information, read our full briefing here:

Guernsey data protection authority announce extension to exemption registration

4 Other News

4.1 ESMA to undertake supervisory exercise in respect of investment funds in light of COVID-19

The Securities and Markets Authority (ESMA) is to take on a specific role to:

- coordinate with national competent authorities to undertake a supervisory exercise with investment funds that have significant exposures to corporate debt and real estate assets to assess their preparedness for potential future adverse shocks; and
- report to the European Systemic Risk Board (ESRB) on its analysis and conclusion.

The recommendation from the ESRB on liquidity risks in investment funds

4.2 European Commission report on AIFMD

On 10 June 2020 the European Commission published a report assessing the application and scope of the AIFMD. The report follows a comprehensive study by KPMG. It summarises the impact on AIFs, AIFMs and investors and the monitoring and assessment of systemic risk and touches on the problems with gold-plating and the differences in national rules and the different approaches taken by national supervisors. The report also acknowledges the barriers faced by small AIFMs in accessing capital in member states. In the absence of a third country passport, NPPRs are acknowledged to play an important role in the market, allowing those member states with such regimes to access global markets for financial services and diversify their investment allocations.

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