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MALTA: A NEW VISION OF FINANCIAL SERVICES

Malta's competitive edge
Borza ta Malta upgrades connectivity
A gathering of new funds
Custody providers find new business growth
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The Financial Services Department within the firm is committed to providing bespoke legal solutions to credit and financial institutions, investment firms, family offices and other stakeholders in the financial services industry. Our mission is to deliver high-quality services in structuring and implementing investment proposals, operations and products in a pro-active, efficient and timely fashion. To this end, we continue to foster and develop our local and international network with a view to offering comprehensive and integrated services to clients.
<table>
<thead>
<tr>
<th>FEATURES</th>
<th>CONTENTS</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>TOWARDS A NEW VISION OF FINANCIAL SERVICES</strong></td>
<td>Page 2</td>
</tr>
<tr>
<td>The story of the financial sector in Malta over the last ten years is one of growth. Growth is evident in the number and size of organisations locating in the jurisdiction and the services that have sprung up in support of the financial industry. Ruth Hughes Liley headlines a report on the Maltese financial services sector.</td>
<td></td>
</tr>
<tr>
<td><strong>AN INTERCONNECTED FUTURE</strong></td>
<td>Page 5</td>
</tr>
<tr>
<td>Borza ta Malta (MSE), the Maltese stock exchange, is steeped in cultural heritage on the outside, yet on the inside, it is pure 21st century. Among the Maltese glass, chrome and polished timber of the Grade I listed Garrison Chapel, a quiet revolution is taking place, not least the replacement of the exchange’s current trading platform by Deutsche Börse’s Xetra platform in June 2012 after just seven months preparation.</td>
<td></td>
</tr>
<tr>
<td><strong>FUND PROFILE: HSBC AM – A BALANCED APPROACH</strong></td>
<td>Page 8</td>
</tr>
<tr>
<td>Developing a diversified and balanced investment approach is <em>de rigueur</em> for asset managers working in Malta, to optimise returns for investors and to minimise risk. Ruth Hughes Liley profiles HSBC Global Asset Management (Malta).</td>
<td></td>
</tr>
<tr>
<td><strong>Q&amp;A: ASSET MANAGEMENT EVOLUTION IN MALTA</strong></td>
<td>Page 9</td>
</tr>
<tr>
<td>The principal elements contributing to the growth of Malta’s financial services industry have been the shift in status from an offshore jurisdiction to an onshore jurisdiction, and Malta’s entry into the European Union in 2004. In a special Q&amp;A Daniele Cop, partner and Dr Nicolé Ann Saliba, associate, at Mamo TCV Advocates explain the dynamics.</td>
<td></td>
</tr>
<tr>
<td><strong>A READY GUIDE TO SETTING UP PIFs</strong></td>
<td>Page 14</td>
</tr>
<tr>
<td>Over the past seven or so years of its existence, the Maltese Professional Investor Fund (PIF) regime has proven to be a success story with over 400 PIFs licensed in Malta to date. As the scramble for AIFMD friendly jurisdictions for hedge funds heats up, the PIF regime looks set to continue from strength to strength. In this brief guide, Ganado &amp; Associates outlines some of the salient features of the PIF regime in Malta.</td>
<td></td>
</tr>
<tr>
<td><strong>DEMAND FOR CUSTODY SERVICES GROWS IN MALTA</strong></td>
<td>Page 16</td>
</tr>
<tr>
<td>In 2004 there were just eight locally-based professional investor funds (PIFs) licenced in Malta. By December 2006 this had grown to 91 funds worth €3bn. Today 700 licences have been issued for all types of collective investment schemes, of which 566 funds, including sub-funds, are actively operating, with a net asset value of €8.3bn. How far can the island deepen its securities services segment?</td>
<td></td>
</tr>
<tr>
<td><strong>DIRECTORY</strong></td>
<td></td>
</tr>
<tr>
<td><strong>MALTA SECURITIES SERVICES &amp; BUSINESS DIRECTORY</strong></td>
<td>Page 20</td>
</tr>
</tbody>
</table>
The story of the financial sector in Malta in the last ten years has been one of growth. Growth is evident in the number and size of organisations locating there, growth in the type of support services which have sprung up, and growth in the numbers of people working in financial and related firms. Ruth Hughes Liley reports.

A NEW VISION OF FINANCIAL SERVICES

"WE HAVE SEEN the financial services sector grow from very humble beginnings," says Kenneth Farrugia, chairman of FinanceMalta, a non-profit public-private partnership tasked with promoting Malta to the world's financial community. Indeed the sector is starting to play a vital role in the Maltese economy. The independent National Statistical Office of Malta estimates that its direct and indirect contribution to the economy in 2001 was over €1bn, representing over 12% of total GDP.

Still short of the 25% contribution spelt out in the Maltese government's Vision 2015, it has some way to go. The ten-year plan named financial services as one of seven through which the government wanted to develop the country.

With this in mind, the government set up FinanceMalta in 2007 to drive forward development of the financial services sector once it became clear that Malta Financial Services Authority (MFSA), the investment market regulator, could not both promote and regulate at the same time. Funded partly by the state and partly through subscriptions and sponsorships, its eight-strong board includes representatives from across the financial sector including the head of the Malta Financial Services Authority, Joe Bannister, a government representative, Alan Caruana and chief executive officer of HSBC Malta Bank, Mark Watkinson.

Bruno L'ecuyer, head of business development at Finance Malta, sees the promotion agency as a bridge between the government and industry and points out: "Because we are small it helps. We have more governors than staff and the board is very active and involved in opening doors for the industry."

It is a vital role in a country where the financial services sector seeks to become a significant employer: out of Malta’s active labour force of 170,000, around 7,000 people are employed directly in the sector with a further 1,900 as lawyers, accountants and other supporting personnel. In total, it accounts for 5% of the workforce.

There is still some way to go. Farrugia understands that it is a slow process and explains that: "Malta was never positioned as a financial region, but the MFSA did a very good job of preparing us for EU membership. We shed our offshore status to become onshore in the 1990s and aligned our laws with Europe so by the time we joined the EU in 2004, we didn’t have to overhaul our systems because we had been using them for nearly ten years already. It was a seamless transition."

FinanceMalta organises its promotional activities across five sectors: funds, insurance, trusts, banking and wealth management, which was added last year, and has produced in-depth guides to each sector. In May it will hold its fifth annual conference, providing a forum for those in Malta and internationally to discuss regulatory and economic issues and industry trends.

In a sense, promotion of Malta as an EU base is not difficult. On an island no bigger than 30 miles by 10 miles including the satellite island of Gozo, access to high speed broadband and ICT infrastructure is a given, English is an official language, and it has a highly educated workforce, low cost of living (salaries are 25% to 30% lower than in Luxembourg), an efficient tax framework and an enviable climate. On top of this, office space is one third to half the cost of other European jurisdictions, according to the latest Ernst & Young Malta Attractiveness Survey.

Farrugia is also tasked with looking beyond the financial sector."We don’t want to be dependent on one sector and we need to induce firms and institutions to encourage people to come here to work," he says.

Large organisations are beginning to set up shop in the country. Toy manufacturer Playmobil makes all its toy figurines in Malta and pharmaceutical specialist Baxter is moving its global research and development to Malta later this year. The usual quota of global brands is also visible in the economy; accountancy firm PwC employs 400 people and HSBC, one of the larger financial groups operating in the country employs more than 500.

One of the concerns for the financial industry is that not enough adequately qualified people are available. The jobs page of the FinanceMalta website has around 46 vacancies.
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INTRODUCTION

To try to attract the more senior and experienced employees, the government has created inducements including the ‘highly qualified persons’ rule, which offers a tax rate of 15% on income for anyone living in Malta and working for a qualifying institution at senior level.

That said, Erik Nelson, a hedge fund director who resides in Malta says: “There’s an oversupply of accountants coming out of university and there’s definitely a lack of more senior level risk management and portfolio management personnel. However, you do see Maltese leave, go to London and get their experience and then come back. People are waiting for good opportunities to arise [in the jurisdiction] and get the equivalent salary [for their experience]. Now that is becoming a reality.”

Farrugia agrees: “You don’t have employees with 20 years’ experience in, say, investment analysis. We need to ensure we have a good supply of workers to service the industry.” Nonetheless, he explains that Malta invests heavily in the country’s educational system (around €250m a year) and that this will pay dividends going forward.

While its business networking activities are a given, FinanceMalta also aims to dig deeper promoting business where it will aid the development of the financial industry. To this end it also works closely with Malta Enterprise, the economic development agency tasked with promoting business. In April, for example, Malta Enterprise organised a business delegation to the Middle East, which FinanceMalta helped to promote. In March, they collaborated with the Malta High Commission in the UK and government agencies in ‘Malta Month’ in the Harrods department store in London showcasing key sectors within the Vision 2015 economic programme.

Another sign of the country’s growing confidence in the financial sector is the news in February that for the first time in Malta’s shipping history, Malta has surpassed Greece and Cyprus as keeper of the largest ship register in Europe at 45.6m tonnes, according to figures from law firm Ganado & Associates.

Promoting Malta overseas is one of the key planks of FinanceMalta’s strategic vision, staying focused on Europe in 2012 with a gradual expansion around the world over the next two to three years. L’ecuyer says: “Malta’s Minister of finance, the economy and investment has a vision for a diversified financial sector so we are starting to look beyond Europe and to promote to the Middle East, Africa, Asia, North America and South America in the next two years. Our core focus is Europe, but we follow the double tax agreements in place, which are modelled on the OECD.”

Malta has in place 59 double tax agreements with other countries. A further eight are signed but not yet ratified and another ten are up for further negotiation. Around 30 memoranda of understanding (MOUs), including ones with China and South Africa in 2009, cover different aspects of financial services and provide clearer channels for co-operation, exchange of regulatory and technical information and investigative assistance between the financial services regulators.

As Malta becomes a more viable alternative to Luxembourg or Dublin, FinanceMalta’s role will not recede, says L’ecuyer: “We will still be needed to push the boundaries. We established a good reputation in Europe and are happy with the flows of business and need to further that and go to new markets where our members have not classically been going to.”

One of Malta’s selling points is its banking system—the 12th soundest in the world, according to the latest World Economic Forum’s Global Competitiveness Report 2011-2012. Indeed, Malta contributed €30m to the European bailout fund, the European Financial Stability Fund during the sovereign debt crisis.

A founding organisation of FinanceMalta was the Malta Bankers’ Association and Farrugia says: “In the crisis, banks in Malta proved to be very resilient because actually, they are ‘boring’ banks. So you do not find collateralised loan obligations, for example and banks have always adopted prudent policies. They fared relatively well under the EU stress tests. Also, government debt is 70% domestically funded and that has kept us afloat as a country.”

Nonetheless, one of the challenges it has had to overcome is that of the legacy of the 1980s when Malta was seen as an offshore tax-saving jurisdiction with easy tax laws, although Farrugia dismisses this: “I don’t think that any serious institution seeking to move to any domicile is driven solely by tax. You look at the regulatory regime; you look at the regulatory body and how it issues licences and supervises the sector; you look at the other structures and supporting institutions.”

Farrugia believes it is important to convey Malta as a domicile with a good reputation: “Trust has become a very important word in the vocabulary of financial services. Investors have become more sensitive to the products that are being provided. There’s a lot of emphasis placed on due diligence and Know Your Domicile! I don’t believe there should be an offshore/onshore interplay because they address different needs.”
Borza ta Malta (MSE), the Maltese stock exchange, is steeped in cultural heritage on the outside, yet on the inside, it is pure 21st century. Among the Maltese glass, chrome and polished timber of the Grade I listed Garrison Chapel, a quiet revolution is taking place, not least the replacement of the exchange’s current trading platform by Deutsche Börse’s Xetra platform in June 2012 after just seven months preparation. Ruth Hughes Liley reports.

MALTA STOCK EXCHANGE


AN INTERCONNECTED FUTURE

“IT IS ALL about connectivity. It is all about transparency,” holds Borza ta Malta’s chief executive officer Eileen Muscat. “It is a strategic decision and not just about the technology. Today it is all about being able to connect to large venues of liquidity and we believe the new platform will be an effective enabler to access such liquidity.”

Xetra with its €1,492bn trading volume is a monster compared with Malta’s current platform, which handled a modest €37m in 2011. The German platform was chosen because it “ticked all the boxes” according to Muscat. “We considered other platforms, but Xetra appeared to be the most appropriate to our present and future needs.” It follows implementation in April 2011 of another element from the Deutsche Börse stable, its post-trade capability, Clearstream. One year on, Clearstream, which allows cross-border settlement of Maltese listed securities, has shown the potential to increase cross-border trades of both Maltese as well as international securities and enable MSE’s 72,000 investors to participate in international markets. With Clearstream’s network stretching to a further 51 markets, this has opened up Malta significantly. The exchange will also implement new registration software in advance of the pan-European settlement system, Target2-Securities (T2S), to be implemented in 2015. “Clearstream has opened a lot of doors for us. We went into Clearstream with one objective in mind but having opened the door we found we have access to other opportunities. This connectivity is vital for expansion of the secondary and primary market,” acknowledges Muscat.

She has wasted no time since her appointment as chief executive in June 2010. Indeed, the last few years have gradually seen all the necessary elements put in place to set the Malta Stock Exchange up as an international player: a fast multi-asset platform, an international clearing and settlement system, a growing depositary business and a finance-friendly government and regulator. Among the other opportunities she mentions, the MSE is planning to launch an exchange traded funds market that could operate on the main market or as a multi-lateral trading facility (MTF).

“When we launch the ETF platform, this will probably be through the main market listing process since this will make them tax efficient. However, there is nothing to say that once we have an MTF platform, this could not be used for a variety of vehicles,” she explains.

As part of the contract with Deutsche Börse, the German exchange is including reference to Malta’s exchange as a listing venue in its marketing materials and roadshows. While no listing took place on the MSE during 2011 due to the financial climate, Muscat is anticipating a number of new listings to be submitted by companies shortly. The exchange has noted interest from overseas companies looking at potentially using Malta as a listing venue. “It is more boutique and personal and you can meet people you need to see easily. For example, one company we recently saw was able to speak directly to the head of the regulatory body—that wouldn’t happen anywhere else,” explains Muscat.

The exchange wants to develop its custody services [the MSE has offered custody since 2007 following a change in the law]. There are currently six global custodians on Malta, including Bank of Valletta, HSBC, Mediterranean Bank, Sparkasse Bank Malta and Custom House. The latest addition to this list is Deutsche Bank. While it is a discrete and competitive market, the potential is rising. For instance, the number of investment funds on the island has ballooned in
recent months from 419 in September 2011 to 566 by April 2012, bringing with it a greater demand for custody. "There is a cultural tradition preferring global custodians, but it depends on [the] client," says Muscat. "We are seeing a growth in the local custody business in Malta. It is an expensive business because of the risk issues involved but we are moving into this area and seeing a lot of interest coming in, as people like the one-stop-shop idea. It is important to position ourselves as a specific provider and we think now is the right time with a lot of re-domiciling of funds going on."

The stock exchange has two licences: one to operate a regulated market and the other to operate a central securities depositary. The depositary services currently provided by the exchange includes new issue registration services, securities administration, and clearing and settlement, all accounting for around 50% of business. In future however, as trading at the exchange moves on to the new Xetra platform, Muscat is expecting the trading arm of the exchange to develop further as a result of international networking opportunities.

Right now, the exchange has 12 member firms including HSBC (Malta) plc, Bank of Valletta plc and local stockbrokers. Twenty equities are listed, 45 corporate bonds, 52 Government bonds and 28 treasury bills. With an equities market capitalisation of €2.6bn as at end 2011, the Maltese market is small. Its 12 member firms compare with the Irish Stock Exchange’s 39 international members, for example. However, after the Xetra implementation, international members already linked to Xetra will also be able to apply for membership of the Malta Stock Exchange.

The exchange is aiming to encourage clients to trade on its main board instead of opting to trade in similar products elsewhere. It’s a tough job, particularly as the exchange has still to build trading volume in depth across its band of listed firm and the exchange will have to diversify its listings if it is to succeed. Trading in shares of the two largest listed companies—HSBC and Bank of Valletta—contributed 55% of annual turnover in equities at €20bn in 2010. Muscat says: "Ideally, we would like to see products that will entice investors to the market in order to increase liquidity, since the local culture is such that investors, who are more retail than institutional, tend to keep their investments in the case of bonds to maturity or in the case of equities in perpetuity."

**Reviewing fee structures**

As part of the exchange’s expansion, it is in the process of reviewing its fee structure, which was based on a system set up when the exchange first started operations 20 years ago. "We are looking to restructure fees and charges where the services are ‘being given,’" Muscat points out. "We have tended to look at the exchange and depositary as a whole package, with registration, trading and settlement as one complete value chain, but we are now focusing on the trading and the central securities depositary separately and marketing them separately."

The exchange is also building links with the Irish Stock Exchange in Dublin, which also operates on the Xetra platform. In February 2012, the two exchanges jointly launched a new pan-European market for wholesale fixed-income debt securities, the European Wholesale Securities Market (EWSM). The ISE owns 80% of the market and provides primary market infrastructure while the Maltese exchange owns 20% is the market operator and provides secondary market services. "Dublin provided assistance 20 years ago when we were setting up the exchange in particular with regards to our compliance department. With the EWSM we have consolidated our long-standing collaboration. The two exchanges are natural partners working relatively similar legislative, regulatory and operational frameworks and sharing a common language," adds Muscat.

Regulated by the Malta Financial Services Authority, the new market is targeting the wholesale or professional investor market for passportable listed securities, and represents a new international market for wholesale funds. It is a move away from the exchange’s traditional investor base: some 30% of government paper and 80% of corporate bonds are held by retail investors, for example.

The political parties share the same view as to the importance of the financial services sector, and of the strategic role of the exchange. Talk of privatisation has been going on since 2008, when finance minister Tonio Fenech announced in a budget speech he was looking for a strategic partner for the stock exchange.

Like all other stock exchanges right now, an important question for Malta’s bourse is whether to continue life as a discrete independent, or to become part of a larger whole. Muscat demurs and points out that: “We are still wholly owned by the government so the first step would be to privatise. So far the government has not declared a definite time line for this. However, privatisation could create synergies with the right shareholder that may lead to huge value-creating opportunities. But like any small market, there is always the notion of national identity. Whatever way we have to find the right solution, though as a target it could be a very attractive proposition.”

However, it has been an issue for discussion for some time now; with no immediate resolution in sight. In the 2010 annual report, for instance, the chairman of the stock exchange Arthur Galea Salomone explained that: “Though Government, as shareholder, has no immediate plans for the privatisation of the exchange, it is increasingly evident that the exchange cannot rely exclusively on the local market for sustained growth. Developing a niche for the exchange is therefore increasingly important if meaningful internationalisation is to be achieved, an objective which to date remains challenging.”

“We are so small that it is important that in the event of a strategic partnership taking place, we retain our national identity whilst reaping any benefits that this may create,” Muscat adds. For the time being however, reality bites: “At the moment our resources are focused on major technological projects, not least, the Xetra project, and investing resources to market our services locally and more importantly, internationally,” she concludes.
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Aiming for a balanced approach to investing

HSBC Global Asset Management (Malta) manages several retail funds and twelve discretionary mandates, and distributes over 40 HSBC funds managed internationally. Managing director of HSBC Global Asset Management Malta, Reuben Fenech, took up his role in October 2009, and restructured the business. The exercise resulted in changes to the fund management team and a new business strategy. The transition was to a balanced approach between manufacturing and distribution and between retail and discretionary. Ruth Hughes Liley reports.

Reuben Fenech, Managing Director of HSBC Global Asset Management Malta, explains that over the last two years “we have gone through a consolidation of the product range to focus on funds managed here. We now have a smaller range which allows us to have more focus and add value for our investors, but it’s wide enough to satisfy the main needs of our client base.” The firm’s locally managed retail funds are at least partially invested in local assets and securities. Among them and one of the oldest funds, the €100m Malta Government Bond Fund holds 85% Maltese bonds and 15% global bonds. Others such as the €50m Maltese Assets Fund invests mainly in the local stock exchange. In the alternative space, the HSBC Property Investment Fund is a fund of property funds invested largely outside Malta, while the Maltese Money Market Fund is in liquidity, government Treasury bills and deposits.

Maltese law distinguishes between prescribed and non-prescribed funds; with prescribed funds having to have at least 85% of assets invested in Malta. These funds “can benefit from better tax treatment,” says Fenech. “The non-prescribed funds have between 10% and 20% invested in Malta by choice. We vary it according to the local market demand and the opportunities in the local equity and bond market.”

The firm divides into three business lines: retail, discretionary and advisory. The retail business represents around half of the business and holds over €540m. The discretionary business for institutions and family offices holds €500m, while the advisory business which relates to mainly internal services to HSBC’s wealth management and insurance business covers over €250m.

Nonetheless, it is the firm’s discretionary portfolio management business that Fenech believes is set to grow. The number of mandates under the discretionary business has grown from four to 12 in the past two years and Fenech is expecting more still, with insurance companies, trusts, family offices, and small private institutions with portfolios of more than $5m which are the main client base. In particular, Fenech has seen a change in the strategy of his discretionary clients: “Insurance companies have become more conservative in their approach to investing due to heightened volatility in equity and credit markets and as a result on the significant changes in regulatory capital requirements lying ahead. While various insurance companies used to run investments in house, I think the game has become more sophisticated as they evaluate the combination of investments that will attract the least requirement for capital.”

“The challenge for them is to have an investment strategy that minimizes the potential for loss based on the volatility exhibited by those assets in the past. So there is a whole process to go through in identifying the portfolio with best risk-return trade-off for any given level of risk stipulated by the investor. It has become a more sophisticated exercise and many companies are outsourcing this,” he says.

According to Fenech, “We are working to grow while keeping up with the changing investors’ preference to diversify their portfolios outside Malta and out of the limited local markets.” One example is in the performance of two new global locally-managed funds. The International Bond Fund which invests in corporate, high yield and sovereign bonds has grown from €16m to €27m over 12 months. Similarly the Equity Growth Fund, a global equity fund, has increased from €8m to €23m in the same period after amalgamating with a separate all-European equities fund in 2010.

Nonetheless, Fenech believes that the 2008/2009 crisis left a lasting impression on investors and forced many not only to diversify globally, but also to switch into fixed income and away from the more volatile equities. “The local market has been paying high dividends for a few years and the correlation with local markets and foreign markets has been low, so this has been a nice cushion in volatile times. People feel more secure when they are tied into assets they can touch and see. It gives them a sense of comfort when the companies they are investing in are familiar names,” he explains.

Meantime the firm is dealing with increasing competition in the funds industry, not least from the emergence of exchange traded funds (ETFs). “Passive strategies provided by ETFs have gained support because of their flexibility and their costs and fees are considerably lower than that for actively managed funds. ETFs also became more popular as investors at times felt that active fund managers are not always worth their fees,” he says.
MamoTCV Advocates is one of Malta’s tier-one law firms with a strong international practice and is actively involved in all areas of commercial law, with a particular focus on corporate law, banking and finance and financial services. The firm has a dedicated financial services department which has been involved in the setting up of professional investor funds since 2006, and which has been earned the firm a solid reputation in the local financial services scene, not only for the structuring and setting up of funds, but also for its work in other areas, such as fund management, fund administration and custody. We spoke with two of its specialists about the steady growth of Malta’s financial services industry in recent years.

FITSE GLOBAL MARKETS (FTSEGM): What are the principal advantages of the financial services regime which have buoyed its prospects over the near term?

DANIELE COP, PARTNER FINANCIAL SERVICES DEPARTMENT AND DR NICOLÉ ANN SALIBA, ASSOCIATE, FINANCIAL SERVICES DEPARTMENT, MAMO TCV ADVOCATES (DC/NAS): The principal elements contributing to the growth of Malta’s financial services industry have been the shift in status from an offshore jurisdiction to an onshore jurisdiction, and Malta’s entry into the European Union in 2004. The local regulator, the Malta Financial Services Authority (MFSA) has also played a vital role in developing a robust yet flexible legal and regulatory framework. It has done this by aligning regulation with EU Law, and in designing domestic rules governing—for instance—professional investor funds, which have proved essential in attracting business to the country. While Malta has managed to establish itself a place on the map of domiciles of choice for alternative investment funds, because of the Professional Investor Fund (PIF) regime, we have, over the past years, also seen significant growth in other areas; in particular in the fund servicing industry. Furthermore, an increasing number of operators inside and outside the EEA are setting up, for example, UCITS management companies, investment firms, payment institutions and even banks in Malta, and effectively using Malta as a base for their operations to service clients throughout the EEA, by exercising their passport rights under harmonised EU law on financial services.

FTSEGM: Do you think something more has to be added to the mix?

DC/NAS: Over the last three years, there have been a number of other pertinent factors which have contributed to Malta’s continued success in financial services, notwithstanding the international climate of financial distress and economic uncertainty. These mainly consist of (though are not strictly limited to): the relatively low cost of setting-up and conducting business in or from Malta; a highly beneficial tax regime applicable both for funds as well as fund services providers and other interested parties; an extensive double tax treaty network; a skilled and knowledgeable workforce; and an approachable regulator. The fact that Malta is a well-regulated jurisdiction is frequently mentioned by fund promoters as one of the key factors influencing their choice of Malta as a domicile, especially in view of investors’ demands for increased transparency and oversight.

FTSEGM: Can you outline some of the immediate opportunities?

DC/NAS: Seeing the number and variety of enquiries and
projects in the pipeline this year, we are optimistic that Malta will continue to grow and develop, not only in the funds industry but also in the area of investment services, asset management, financial services and banking. Although there is still uncertainty about the nature and consequences of the Directive on Alternative Investment Fund Managers (AIFMD) and other major regulatory changes that are imminent (not only within the EU, but also in third countries such as Switzerland) it is clear that these changes will cause a transformation in the way the alternative investment funds industry currently operates. We expect that this may present Malta with opportunities to further assert its place as a domicile for funds targeting the European market as well as for fund management companies and other service providers. At the same time, the MFSA and local practitioners continue to apply their efforts to refining the existing domestic rules, so as to tap into new potential niche markets—structured finance and private equity come to mind here.

FTSEGM: How exhaustive is the financial regulatory regime: what more (in your view) needs to take place for the jurisdiction to build on its successes?

DC/NAS: Malta boasts a comprehensive legal and regulatory framework for the financial services industry at large. As an EU Member State, the country is obliged to implement and apply the various pieces of EU law, regarding, e.g. credit institutions, payment institutions, investment firms, UCITS and UCITS management companies and financial collateral. The approach so far has always been to afford maximum flexibility through the exercise of available options and derogations, thus ensuring a level playing field with other EU jurisdictions such as Luxembourg and Ireland. Malta has also put in place various pieces of domestic legislation to accommodate the various segments of the financial services industry, drawing from experience in other countries; by way of example: the Seccuritisation Act, which creates the framework for securitisation and lays down special rules for securitisation vehicles; rules on re-domiciliation which have been successfully tried and tested as an easy, fast and effective procedure since it came into force in 2002; rules on control of assets and specific types of security interests; a dedicated framework for pension funds and pension schemes (retirement schemes established in Malta and regulated by the MFSA may be recognised by Her Majesty’s Revenue and Customs (HMRC) in the UK as Qualifying Recognised Overseas Pension Schemes (QROPS).

Admittedly, there is always room for improvement, and but as local law is tried and tested over time, the MFSA regularly reviews and fine-tunes the existing rules. The MFSA is also an important driver in new initiatives to further enhance the financial regulatory regime. Since most rules applicable to local licence holders are set out in rules issued by the MFSA, which is authorised to do so under primary or subsidiary legislation, changes of a technical or regulatory nature can usually be adopted swiftly by the MFSA.

FTSEGM: What is the outlook for the local capital markets? What role can the stock exchange play in this regard?

DC/NAS: For a long time the Malta Stock Exchange ran the only regulated market in Malta. Issuers of securities listed on the Malta Stock Exchange’s official list are predominantly local companies, and the market is not particularly liquid at the moment. However, in the past years, efforts have been made to attract and accommodate foreign issuers, in particular by improving the local infrastructure; for instance, the Malta Stock Exchange is expected to start using Xetra, Deutsche Börse Group’s fully electronic trading system, in the near future. In February 2012, the Irish Stock Exchange and the Malta Stock Exchange announced a joint venture to launch the European Wholesale Securities Market (EWSM), a new regulated market in terms of MiFID, authorised and supervised by the MFSA. The eligible securities for admission to trading on the EWSM are asset backed securities, debt securities and derivative securities, with a denomination per unit of at least fifty thousand euro. The EWSM is intended to provide issuers and arrangers of such securities access to an EU regulated market with the support of a dedicated listing agency service. While the ISE acts as the market promoter providing primary market infrastructure as well as other corporate services to the EWSM, the MSE acts as the market operator providing secondary market services to the EWSM.

FTSEGM: How flexible is the government in making modifications to the financial regulatory regime to leverage Malta’s interests in developing as a financial/investment markets hub?

DC/NAS: Essentially, the Maltese financial regulatory regime is composed of three layers: the primary basis are the acts of law which set out the main legal framework and
confer powers to the Minister responsible for finance to adopt subsidiary legislation in the form of regulations, and to the MFSA, to issue (among others) rules for the detailed implementation of provisions of the said acts and regulations. Since the bulk of the provisions governing the setting up and conduct of financial services business are in the form of rules issued by the MFSA, it is relatively easy to make changes to such rules when the MFSA deems this necessary—be it for the purpose of implementing EU law, or in order to clarify or modify certain rules in order to fine-tune the regime. The MFSA tends to make such amendments in consultation with local practitioners, through frequent consultation.

One of the challenges with which the Maltese government is often faced is remaining up to speed with all legislative, administrative and regulatory changes being enacted at the supra-national level, in particular by the EU institutions (especially now with the avalanche of new measures being adopted and existing Directives such as MiFID being reviewed and changed). Nevertheless, Malta has an excellent track record in timely implementation of EU Directives regarding financial services—as far as possible this is done via regulations drafted and rules issued by the MFSA, in order to avoid the more cumbersome legislative process of changing acts of parliaments for this purpose. It must also be said that the MFSA is generally quite receptive for suggestions from local practitioners and their respective associations on improvements to the local regime, as long as it is satisfied that these are to promote high standards of conduct and investor protection.

FTSEGM: Are there any new regulations in train which might act as a transformational engine of change in the jurisdiction?

DC/NAS: As previously mentioned, there is a lot going on at EU level, but one specific piece of legislation which is expected to bring about a paradigm shift is the AIFMD. Local practitioners are eagerly awaiting the promulgation of the implementing measures for this Directive, and MFSA’s proposals for transposition (expected to be issued in the summer of this year 2012), in order to assess the full impact of the AIFMD regime on Malta as a fund domicile.

Malta already regulates fund management activities and collective investment schemes, as well as the provision of custody services to collective investment schemes. Nevertheless, for the implementation of AIFMD we are expecting an overhaul of local rules, and obviously, we will need to revisit our existing fund structures and revise the offering documents and contracts in place, and probably also the fund’s constitutional documents. However, there are still a lot of loose ends and uncertainties, as we are waiting for the Level II measures to be published by the European Commission. We do not know yet which approach the MFSA intends to take for the implementation of the AIFMD, but we understand that the MFSA is currently working on a consultation document in which it will set out its views on this. Generally, Malta tends to exercise the available options and derogations when implementing EU directives on financial services, and we expect that this will also be the case for AIFMD. For instance, it is an option for Member States to allow certain funds with a five-year lock up period, typically private equity funds, venture capital funds or real estate fund, to appoint a notary, lawyer, a registrar or another entity to carry out depositary functions, subject to certain conditions—our guess is that Malta will probably allow this. Another example is that there is a transitional provision regarding the location of the depositary of alternative investment funds managed by management companies captured by AIFMD, which is optional too: in this case, the option is granted specifically to the competent authorities of home Member State of the fund, or if the fund is not regulated, the competent authorities of home Member State of the manager, and offers those Member States the possibility to allow credit institutions established in another Member State to be appointed as a depositary until July 22nd 2017 (by way of exception to the general rule, that the depositary of an EU alternative investment fund would need to be established in the home Member State of the fund). Malta will certainly exercise this option.

What we are curious about is to know whether there will be a complete overhaul of the current regime, in the sense of a one-size-fits-all regime or if Malta will put in place a two-tier regime, whereby a distinction is made between funds whose managers are caught by the AIFMD and those that are not. Funds in Malta tend to be relatively small, so it is very well possible that certain managers who have alternative investment funds in Malta would not be fully subject to the directive, as long as they fall below certain thresholds. For those cases, it may be worth considering affording more flexibility, for example when it comes to the requirement to appointment a single custodian and the location of the custodian.
INVESTMENT MANAGERS ARE being faced with an array of legislative changes which have the potential to fundamentally affect how they continue to run their business and reach their clients. These changes include the latest development of the Alternative Investment Fund Managers Directive (AIFMD), UCITS brand and MIFID II in Europe and the Dodd-Frank Act and Foreign Tax Compliance Act (FATCA) in the US. Investment Managers will face increased cost and time pressures due to new compliance and administrative obligations resulting from.

In addition many of the actions necessitated by regulation and changing client behavior are likely to require investment by managers in their systems, personnel, communications and compliance infrastructure. For many, this will highlight the need to make use of efficiencies, and economies of scale in order to reduce costs and increase effectiveness in the face of a more demanding regulatory and client environment.

Some investment managers have the potential to make adjustments that could reshape their business models by looking to streamline costs. In doing so they should consider what alternative jurisdictions, other than their current setup, can provide and what services they can outsource to gain further efficiencies.

As investment managers look at the way they do business, Apex Malta is seeing an increasing number of managers looking more closely at what Malta has to offer and taking the necessary steps set up in Malta.

There are a number of key advantages Investment Managers are finding when assessing Malta as a location for establishing a Management Company:

The Financial Services Regulator
The Malta Financial Services Authority (MFSA) is the single regulator for the financial services industry and is staffed by a team which is highly technical. The regulator has been instrumental in ensuring that Malta develops as a reputable financial centre by applying the highest standards and also by ensuring that legislation, directives and policies are in line with EU law, with the latest market developments and the needs of the industry. This technical yet entrepreneurial attitude has been a major part of the success in the substantial growth of the industry. The MFSA is open to understanding business needs and actively works with industry players and professionals to seek effective solutions.

Regulatory Framework
Malta’s regulatory framework is geared to ensure the highest standards of probity and transparency while allowing operators the freedom to compete and innovate.

The Investment Services Act provides the statutory framework for the licensing and supervision of investment services and collective investment schemes (CISs). The legislative framework is flexible enough to adapt to different business models within parameters set by both Maltese and EU legislation.

The MFSA distinguishes between Retail Collective Investment Schemes and Professional Investor Funds. Retail Collective Investment Schemes include both UCITS and non-UCITS Schemes. These types of schemes are based on the UCITS Directive which is fully transposed into the Maltese regulatory framework.
A Professional Investor Fund (PIF) is a non-retail fund which is not subject to investment restrictions and is not regulated to the same degree as other collective investment schemes, and accordingly may only be promoted to specified categories of investors. Given the characteristics of a PIF, the objective of this regime is to create a “fast track” for regulatory approval for this type of investment vehicle and a reduced level of ongoing regulation and supervision.

A PIF may only be promoted to specified categories of investors and the licensing and ongoing regulatory obligations of the PIF depend on the category of target investor (Experienced, Qualifying or Extraordinary investors).

The regulatory framework for Investment Managers is based primarily on the EU Markets in Financial Instruments Directive and the Capital Requirements Directive. Managers establishing operations in Malta would need to apply for a Category 2 license under the Investment Services Act.

Low Taxation
Malta is one of the few countries whose income tax regime is based on the full imputation system. The mechanisms of the Malta tax system ensure a low effective corporate tax rate, that is; companies that are both resident and incorporated in Malta are chargeable to tax in Malta, on a worldwide basis. The overall Malta effective tax rate applicable to the taxable income of companies once distributed is in general approximately 5%. This is based on the opportunity for shareholders to claim, upon a dividend distribution in their favour, a refund of a portion of the Malta tax paid by the Company on the distributed profits. The 5% effective corporate tax rate is the lowest rate applicable to active trading profits within the EU.

In 2011 the Maltese Government introduced specific tax rules targeted at highly qualified persons performing particular functions within entities licensed by the MFSA. In terms of the Highly Qualified Persons Rules (HQP), a 15% flat rate of tax would be chargeable on employment income derived by duly qualified personnel. This favourable tax rate applies in respect of such income up to a maximum of €5,000,000 per annum. Any income in excess of the €5,000,000 threshold is exempt from Maltese tax.

The following functions are examples of the positions that would qualify the person as HQP: Chief Executive Officer, Chief Financial Officer, Chief Investment Officer, Chief Operating Officer, Head of Marketing, Portfolio Manager, Senior Analyst and Senior Trader.

To be eligible for the HQP flat tax rate, an individual must derive employment income of at least €75,000, be employed by company licensed by the MFSA and satisfy the MFSA that he holds a qualifying position with the licensed Company.

Malta has more than 50 double taxation agreements.

Low Set-up and Operational Costs
The costs of obtaining an investment management license in Malta, setting up of the corresponding corporate vehicle as well as the running expenses of the Company are reasonable and relatively lower than the same costs in other financial centres in Europe.

Location
The country’s location in the Mediterranean provides a time zone the same as mainland Europe with regular flights from all over Europe. Within three hours you can be in the international hubs of London or Frankfurt. Malta is also within two hours of Munich and just an hour from Rome, if you want to escape Island life.

Human Resources
Diligent, highly educated, enthusiastic and quick to learn, the Maltese workforce is the Island’s greatest strength and most valuable asset.

Lifestyle
Malta provides the perfect work/life balance with its Mediterranean lifestyle. English is not only widely spoken and used in business and education, but is the language used for general day to day living. The pleasant weather; over 300 days of sunshine, the warm Mediterranean sea, the culture and history, the cuisine, the outdoor living, short commute to work, the easy getaways to mainland Europe, make Malta the ideal place where one can not only do business, but also enjoy a relaxed lifestyle.

Professional Services
Malta has wide range of experienced support services providers giving the ability to outsource certain back office functions. At Apex, we continually have an eye on providing services that produce efficiencies for our clients. For example the recently launched Apex Financial Outsourcing Solutions service (AFOS), frees up investment managers’ time by outsourcing their middle office functionality to a specially designated Apex team. This can generate cost savings, reduces the time spent by investment managers on trade support, reconciliation, and report creation. Apex also provides a full range of accounting, compliance and support services necessary for the maintenance of a company’s accounting records which creates efficiencies and economies of scale for investment managers setting up in Malta.
Over the past seven or so years of its existence, the Maltese Professional Investor Fund (PIF) regime has proven to be a success story with over 400 PIFs licensed in Malta to date. As the scramble for AIFMD friendly jurisdictions for hedge funds heats up, the PIF regime looks set to continue from strength to strength. In this brief guide, Ganado & Associates outlines some of the salient features of the PIF regime in Malta.

A ready guide to establishing a Maltese Professional Investor Fund

In terms of the Investment Services Act (ISA), no collective investment scheme (CIS) is permitted to issue, or create, any units, or carry on any activity, in or from within Malta unless it is licensed by the Malta Financial Services Authority (MFSA). In terms of the Act, an investment fund is bound to satisfy the following criteria to qualify as a CIS. It must, for instance, have the objective, or one of its objectives must be, the collective investment of capital acquired through an offer of units for subscription, sale or exchange and operate according to the principle of risk spreading. It also has to involve the pooling of investments; or that unit-holders are able to request the fund for redemption of their units; or that units will be issued continuously or in blocks at short intervals.

CIS can be established as companies (so called SICAVs or INVCOs), unit trusts, limited partnerships or in contractual form (mutual funds). CIS can be open-ended or closed-ended. By far the most popular choice, the investment company with variable share capital (or SICAV) may be established as a single fund with multiple shares classes (multi-class), an umbrella fund with or without legal segregation between sub-funds (multi-fund), an incorporated cell company (ICC) with incorporated cells and now as a recognised incorporated cell company (RICC).

CIS licenses in Malta come in three main types: Retail CIS (including Maltese UCITS), Non-Retail CIS (the PIF Regime) and Private CIS, the latter being subject to a recognition requirement rather than a formal licence or authorisation. This represents the first major choice for a fund promoter looking to establish a CIS in Malta which will be decided according to the type of investor being targeted, investment strategy proposed to be pursued and distribution methods envisaged. There are also three categories of PIFs, those targeting Experienced Investors, those for Qualifying Investors and those for Extraordinary Investors.

Experienced Investors have the expertise and knowledge to make their own investment decisions and understand the risks involved. The minimum investment threshold is €10,000, $10,000 or equivalent and may not fall below this threshold unless this is due to a fall in the NAV of the PIF. Qualifying Investors include individuals, trusts, associations or corporate entities whose net assets exceed €750,000, with reasonable experience of PIFs and investments. They might be employees and directors of service providers to the PIF, or relations and close friends of the promoters (limited to a total of 10 persons per PIF). The minimum investment is €75,000 or $75,000 or equivalent.

Extraordinary Investors are the highest qualifying individuals or entities, defined by a net worth of over €7.5m or $7.5m. The minimum initial investment in this case is of €750,000 or equivalent. PIFs available to Qualifying or Extraordinary Investors are not subject to any restrictions on their investment or borrowing powers except for those imposed by the PIF’s own marketing and offering documentation. Restrictions remain only in the case of Experienced Investor Funds wherein gearing or leverage is limitedly allowed and the PIF is subject to certain investment limits.

Service providers

Another advantage of Malta’s PIF regime is that none of the PIF’s service providers (such as its manager, investment advisor, prime broker, administrator or custodian) have to be based or licensed in Malta as long as they are based in recognised countries which are subject to a standard of regulation equivalent to Malta’s regulatory regime.

The MFSA would carry out limited due diligence on service providers licensed in recognised countries or in countries that are full signatories to IOSCO’s multi-lateral memorandum of understanding on regulatory cooperation. If a particular PIF has no physical presence in Malta, it is expected to appoint a local representative who will accept directions from the MFSA and provide it with any information requested. Local representation, which can be local law firms, audit firms or investment services providers, is required to comply with certain record-keeping requirements for possible inspection by the regulator.

A PIF which is made available to Qualifying or Extraordinary Investors is not required to appoint a custodian or a prime broker although the PIF directors have to inform the MFSA of the alternative arrangements for the safe-
keeping of assets. Promoters with one eye on AIFMD may wish to identify a custodian willing to act as custodian for the whole PIF in line with the AIFMD's single depositary requirement. In this regard, since Malta intends exercising its derogation under AIFMD until 2017, a custodian in Malta or any other EU member state may be selected.

Self-Managed PIFs
PIF Rules permit structures where discretion on the PIF’s investments is retained solely and directly by the PIF Board of Directors rather than delegated to an external discretionary investment manager. These are Self-Managed PIFs.

Typically, a Self-Managed PIF would set up an investment committee of the board of directors, with one or more portfolio managers, whether appointed from within the board of directors or consisting of such other competent persons approved by the MFSA for that role. However, as part of the application process, there are additional requirements to be fulfilled, such as an initial capitalisation of €125,000 and an Investment Committee that is composed of individuals who satisfy the MFSA’s competence assessment in addition to being “fit and proper”.

The Application
While the MFSA is flexible and ready to discuss issues arising in the application process, promoters should not expect an offshore regulatory approach. The MFSA applies thorough due diligence on the PIF’s directors, promoters and service providers before issuing a licence.

The MFSA ordinarily requires a number of supporting documents depending on the structure of the PIF and the service providers involved. Documentation is normally submitted in draft form and, once feedback is provided by MFSA, these are finalised. A typical application pack includes: an application form; a non-refundable application fee consisting of €1,500 per fund and €1,000 per sub-fund (if any). A supervisory fee of €1,000 per scheme and €500 per sub-fund (if any) is subsequently due and first payable in advance on the day of issuance of the license and on each subsequent anniversary thereafter; the Offering Documentation or Prospectus; a copy of the minutes of the first meeting of the PIF’s Board of Directors; the PIF Memorandum and Articles of Association; the MFSA Personal Questionnaires of each proposed director and qualifying shareholder holding more than 10% of the PIF’s voting shares, whether such are corporate entities or individuals; other information required by the MFSA, proposed local representation (if applicable); and the PIF’s Compliance Officer & MLRO (where applicable).

Licensing and Post-Licensing Supervision
The MFSA will reply to licence applications within seven working days after the submission of a full set of complete and final documentation and the process typically takes eight to ten weeks from first submission to issue. Documents are thoroughly reviewed by the MFSA’s Authorisations Unit and a two-way dialogue commences. Once the MFSA is satisfied, its Supervisory Council issues an approval letter setting out any pre-licensing, post-licensing and post-commencement of business stage conditions. Pre-licensing conditions typically include submission of signed application documentation and incorporation of the legal entity.

Once the PIF has been licensed and has commenced operations, it is vital that the appointed Compliance Officer maintains accurate records and scrutiny of the PIF’s ongoing obligations. PIFs set up as investment companies are also required to submit an annual return to the Registry of Companies in Malta indicating the PIF’s Directors and shares in issue and file the annual audited accounts and financial statements to both the Registry of Companies and the MFSA. Changes to the Offering Documentation and the PIF’s constitutional documents have to be approved by the MFSA in advance. Advance notice must also be given to MFSA before changing the PIF’s Investment Manager or any other service provider.

Taxation of PIFs
The tax treatment of the income derived by a CIS and any income derived by individual investors in the form of capital gains or dividend depends on whether the CIS qualifies as a prescribed or non-prescribed fund. Essentially, a CIS is classified as a prescribed fund if it satisfies two conditions cumulatively, namely, that the fund is resident and based in Malta and that the value of the assets situated in Malta amount to at least 85% of the fund’s total assets. By default, other funds are classified as non-prescribed fund and as a general rule; non-prescribed funds are exempt from payment of tax in Malta on any income received or gains made.

As soon as a fund is licensed by the MFSA, it is subject to tax but then exempt from tax if it qualifies as a non-prescribed fund irrespective of legal form.

On the other hand, prescribed funds are tax exempt in Malta on their income and capital gains except from a 15% final withholding tax on bank interest payable by banks licensed under the Maltese Banking Act and a 10% final withholding tax on other investment income (interest, discounts or premiums). Subject to certain filings with local tax authorities, no stamp duty is payable by investors in a Maltese PIF on a transfer of their shareholding or participation. Maltese funds can also benefit from Malta’s extensive double taxation treaty network, however, this needs to be determined by the tax authorities of countries where the Maltese fund has its assets and where such fund is invoking double taxation treaty benefits.

Listing of PIFs
CIS licensed in Malta can seek a listing on the Malta Stock Exchange. A CIS (including PIFs) which is licensed in Malta is also permitted to list on an investment exchange overseas. The promoters of the fund would have to go through a listing application process with the MFSA (also the Listing Authority) which process is typically neither extensive nor costly.
Demand for custody services grows in Malta

In 2004 there were just eight locally-based professional investor funds (PIFs) licenced in Malta. By December 2006 this had grown to 91 funds worth €3bn. Today 700 licences have been issued for all types of collective investment schemes, of which 566 funds, including sub-funds, are actively operating, with a net asset value of €8.3bn. Three-quarters of these are professional investor funds, although there are a small number of UCITS funds (59 as of December 2011). Ruth Hughes Liley looks at the emergence of the Maltese fund industry and the opportunity as well as the current limitations therein.

When Daniel Gladiš set up a hedge fund worth $7m in Malta in 2004, the year Malta joined the EU, he recalls: “We didn’t know at the time whether we were one of the first of many or whether we were doing something really stupid.” Vltava Fund, of which Gladiš is director, was only the sixth fund to be licensed in the jurisdiction as a PIF. He had considered Ireland and Luxembourg, but he heard Malta was trying to develop its hedge funds sector. Even then there were problems: Vltava was looking for a prime broker: “We visited lots but almost no-one—only two—were ready to deal with Maltese funds.” Eight years later, the fund has grown to $55m.

The fund industry in Malta was designated one of seven target growth areas in a ten year strategy outlined in Vision 2015, the government official growth plan. Financial services were expected to contribute up to 25% of the country’s GDP by 2015; though it looks some way off plan right now; in real terms it makes up 12%, including supporting services. However, say local professionals, the trend is directional. Bill Scrimgeour, global head of regulatory and industry affairs, at HSBC Securities Services believes Malta is at a crossroads: “There are more than 500 funds with approaching €10bn assets under management. That’s small compared with the European alternative fund base of €2.1trn, but it is somewhat of a threshold to get noticed from a global industry point of view.

Stephen Pandolfino, deputy head of Global Banking and Markets, HSBC Bank Malta, explains: “The growth from this sector has been exponential in the span of a few years and this has gone hand in hand with an increasing contribution to GDP. Malta has focused on foreign direct investment, so initiatives have been created around attracting and encouraging international fund managers to transfer their activities to [the island]. The country is reaching out and offering a base where regulation is firm but flexible and where the providers are focused on building relationships and service through local expertise that satisfy the administrative, accounting, legal, custody and banking needs of international clients.”

Head of the Malta Financial Services Authority (MFSA) Professor Joe Bannister can take much of the credit for the development of the hedge fund industry on Malta. A former
professor of bio-chemistry at Oxford University and then at Cranfield Institute of Technology, UK, he began to cross-paths with a few of his former students who had taken jobs in the City of London and were setting up hedge funds. “Talking to them, I thought this was an area I needed to get involved in,” he recalls and later when he developed a regulatory structure for Malta at the MFSA, the hedge fund space was the first thing he looked at.

The MFSA has established three classes of hedge funds with different minimum investment levels: €10,000 for funds promoted to ‘experienced investors’; €75,000 for funds promoted to ‘qualifying investors’; and €750,000 minimum investment for funds marketed to ‘extraordinary investors’. This last category is mainly used by private equity firms. Other restrictions also apply; for instance, a fund manager cannot invest more than 30% of an experienced investor fund in a single instrument.

While most hedge funds operate as PIFs, a few have chosen to operate under the UCITS wrapper as Anthony Farrell of Temple Asset Management explains: “It is cheaper to set up a PIF but I personally think the investor definitions in the three forms of hedge fund allowed under the term are a little too vague for our purposes: you are relying on the client to self-certify that they are an ‘experienced’ investor and this could cause problems down the road, particularly when the fund is marketed cross border, for example. We would prefer to have retail funds, even though the compliance is more rigorous, so that these issues don’t arise.”

A boost to the funds industry

The funds industry was given a boost in 2009 when the MFSA issued new guidelines to offshore funds regarding redomiciliation to Malta. It is not a free-for-all. Funds have to show that they have operated for 12 months successfully in their existing domicile before being given a licence. Any fund wishing to redomicile has to go through a strict process. This starts with an application to the MFSA for a licence, and notifying the Registrar of Companies. The MFSA conducts due diligence on the fund, vets the draft documentation and in the first instance, issues an agreement ‘in principle’.

While funds registered in Malta are not required to appoint a local administrator, the funds administration business has grown substantially. The MFSA issued six new Recognised Fund Administrator licences in 2011 alone, bringing the total number of fund administrators on the island to 24. On the other hand, one of the challenges for the hedge funds industry has been a shortage of custodians and prime brokers. Deutsche Bank became only the sixth custodian on the island when it received a licence (in 2011). It has joined Bank of Valletta, HSBC, Mediterranean Bank, Sparkasse Bank Malta and Custom House as a custodian provider.

Manufacturers of UCITS retail funds and PIFs targeting ‘experienced investors’ are obliged to appoint a custodian or prime broker, those funds targeting the higher-level ‘qualifying’ or ‘extraordinary’ investors are not obliged to have one, although the MFSA recommends it. FMG Funds, which has eight funds domiciled in Malta, uses Credit Suisse as its custodian/prime broker, while all local corporate banking is handled by HSBC Malta.

FMG’s General Manager, Erik Nelson, says: “There is still a limited supply of custodian services in Malta. Because of the lack of competition for custody, custodial fees can be relatively costly. It’s a chicken and egg thing: it is hard for the banks to come here before the funds set up and hard for the funds to set up without the banks. [However,] because the MFSA has done such a good job, this has been improving.”

In the two years Nelson has lived in Malta, he has seen the banks holding conferences and seminars and says “it is just a question of time” as to when the prime brokerage and custody sector expands. “We are definitely waiting to see banks come down here. The prime broking and custody industry is one of the last common denominators we are missing. In the next 12-18 months we will definitely see changes in one form or another.”

Indeed, the MFSA is already in negotiation with two more global custodians and Bannister believes that this will help start to solve the bottleneck. “It is being driven by clients and so the issue is solving itself,” says Nelson.

It is also being driven the plethora of regulation sweeping through most of the G20 economies. New regulations, the Alternative Fund Managers’ Directive and UCITS 4, which allows funds to be marketed cross-border within the EU, have created a level playing field for fund managers wanting to distribute funds into several different countries. Malta is one of three international distribution centres. Their raison d’etre is to service funds out of other people’s markets and ♦♦
this gives Malta a wonderful opportunity to take advantage and create a third choice. It can’t catch up or compete with Luxembourg, but it can set itself a focus to win new business,” thinks HSBC’s Scrimgeour.

Kenneth Farrugia, chief officer of Valletta Fund Services, a fully-owned subsidiary of Bank of Valletta, Malta’s largest banking group, says “There is clearly a cluster shaping the industry in fund administration although this is not yet the case on the custody side. Moreover, as is the case with the other EU fund service providers, keeping up with the pipeline of new regulations is taking its toll on operational costs to ensure full adherence to these new regulations; this not to mention the operational challenges that these new regulations bring about.”

Dermot Butler, chairman, Custom House Global Fund Services, a licensed custodian in Malta, believes insurance premiums could rise 20% as a result of changes needed to comply with new regulations coming out of EU and US. “It is not difficult to believe that many regulators think they cannot adequately police this. The service offering from administrators will have to grow. It makes it even more difficult the smaller funds who cannot afford the whole suite of services. I think the requirement for administrators to up their game is important. All this is going to add to cost. Whereas it used to be two or three meetings a year, they are going to have to do a lot more work.”

The fund industry has grown also because it is cheaper to set up a fund in Malta; up to 40% cheaper than Dublin and up to 60% cheaper than Luxembourg according to Chris Bond, head of Global Banking & Markets for HSBC Bank Malta. But other elements are also in play. Bond says: “In a very short space of time, anyone doing due diligence on Malta can meet with the regulator, who adopts an open door policy, with all major service providers and even with the government. Time to market is of critical importance.”

The opportunity presented by sub funds
Farrell is planning to expand Temple Asset Management, for example, by offering sub-funds.

Custom House is also using sub-fund capability in offering a ‘Nascent’ fund, a ‘Maltese umbrella’ with segregated cells that allows an aspiring fund manager to use a template structure at much less cost than it would otherwise.

Butler explains the process: “The cost of setting up a fund is very expensive—around €35,000 to establish it going up to €150,000, and that is crippling for a small fund. Then operating costs mount up and are rarely less than €100,000. So we lease out a sub-fund. You manage the money and you have to use our boiler-plate structure which includes using a Maltese auditor. We charge €2,000 a month administration fees and 20bp overall organisational charge on the net asset value of the fund. If after two years you have lost money, you should probably go back to the sun, but if you have made money and have reached an appropriate size you should probably set up your own fund and you are obliged to use Custom House for the next three years. Setting up has become incredibly difficult to do and finding seed capital for start-up investors is very difficult so we thought this was an idea for them to get their toes wet quite inexpensively.”

Trading conditions are also improving the environment. Upcoming enhancements to the Malta Stock Exchange platform will also help. Furthermore, the creation of the European Wholesale Securities Market, a joint venture between the Malta and Irish stock exchanges, in which secondary listed products will be traded on Deutsche Börse’s Xetra platform, is the first time that international securities will be using the Malta Stock exchange to list products and is the first move away from a solely domestic market.

A challenging marketplace
As with other jurisdictions, the impact of the cold hand of recession in Europe has also dampened Malta’s immediate prospects. Nonetheless, funds are still choosing to redomicile in Malta to ensure a European base. When FMG’s eight Maltese funds redomiciled there from Bermuda in 2008 they were domiciled both in Bermuda and Malta through a master-feeder fund structure. The main funds were kept in Bermuda due to the large number of clients invested in them, while the newly launched Malta funds were feeding into the Bermuda funds. This was the ideal set-up while the Malta fund structure was settling down. Two years later, in 2010 FMG switched the feeder fund structure around to work the other way, so the Malta funds became the main funds with Bermuda funds feeding into them.
“A lot of different companies have had to do this,” explains Nelson, “because there has been a lot of migration of funds and getting into the EU is the gold standard. In our case we wanted to keep the clients in Bermuda, while giving new investors the ability to invest in our funds onshore, with greater regulation, transparency and liquidity.”

Farrugia is confident the hedge funds market will continue to grow: “Despite the challenges still being faced by the international hedge fund industry and the state of flux of the world’s capital markets, investors’ investment appetite has improved over the past few months. Within this context, the fund industry in Malta is expected to remain highly buoyant as is evidenced by the healthy pipeline of new business.”

Funds have even moved to Malta from Luxembourg and Ireland, says Nelson: “It is a popular new place to be. It’s a charming island, safe and everyone speaks English; there’s a high standard of living, a great climate and business is great. There are definitely tax benefits to being here, so it makes sense. We are expanding here in Malta. This is where we are seeing the most growth. We’re here for the long term.”

Bank of Valletta Group is the most heavily traded stock on the Malta Stock Exchange with a market capitalisation of €2.5m. In line with other Maltese banks, Bank of Valetta has endured muted demand for credit and investment related business as a consequence of the continuing euro crisis. The bank has taken the opportunity to reduce the proportion of non-performing accounts to total loans and advances, through this period of subdued demand for credit; notably in the construction, property and retail segments.

“We believe that we are able to maintain an effective balance between a conservative risk appetite and innovation, which means a prudent approach on behalf of our shareholders coupled with the latest technological solutions, such as mobile banking, which we were the first to offer in Malta,” says a bank spokesman.

At the end of April presentation of its first quarter numbers Bank of Valletta chairman Roderick Chalmers claimed that the bank has come in with “a decent set of numbers” for the six months to March 31st, registering a pre-tax profit of €49.1m, up 9% on the €45.2m for the same period last year. The bank had also accessed “a small amount” from the long-term refinancing operation facility (LTRO) from the European Central Bank (ECB) for three years at 1% per year. “In times of financial uncertainty, liquidity is key,” noted the presentation. However, he added that LTRO monies made available to European institutions from the ECB were “a shot of morphine, not a permanent cure”, and fiscal and structural reforms were required, some of which would be painful.

The bank’s interim net operating profit before fair value movements is flat on last year’s at €47m, noted Chalmers. The bank’s loan book rose by €87m to total €3.69bn, while the bank’s non-performing loans ratio improved to 4.1% from 5.1% in the previous quarter. Customer deposits rose €94m to €5.62bn, with “modest” growth seen in retail and institutional sectors despite high levels of government bond issues and competition for deposits in the Maltese market.

Chalmers points to the oversubscription of the bank’s recent €40m medium term note programme, which carried interest of 4.25%, lengthening the duration of the bank’s liabilities in anticipation of more demanding liquidity regulations. Even so, he pointed out that liquidity at the bank remains robust at 49% while the loans-to-deposit ratio was largely unchanged at 68.7%, while core Tier I capital is at 10.8%, up from 10.5% at the end of last year.

In light of current developments the bank is keen to leverage opportunities elsewhere and has not been slow to invest overseas. The bank was among the first foreign financial institutions to open a representative office in Libya in 2002 with a view to promoting business development between the two neighbouring countries. “We will clearly look into the scale and scope of our operations as the political situation stabilises,” says the spokesman. Bank of Valletta is already receiving new business requests from customers operating in the Libyan market. The bank is also in process of opening a representative office in Brussels.
MALTA – SECURITIES SERVICES & BUSINESS DIRECTORY

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Legal Experts

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Camilleri Preziosi is a leading Maltese law firm with a commitment to deliver an efficient service to clients by combining technical excellence with a solution driven approach to the practice of law.

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Ganado & Associates, Advocates is one of the protagonists in local legal practice and has contributed specifically to Malta’s internationally recognised reputation as a centre for financial services and maritime law.

It is currently the largest legal firm in Malta and specialises mainly in financial services and shipping. It has departments in other practice areas such as general litigation, general corporate, corporate secretarial and governance, taxation and labour law. New areas of development are environmental, energy and aviation law.

Ganado & Associates, Advocates enjoys an excellent reputation at national and international level and has relationships with many major firms in Europe and worldwide.
Legal Experts

Mamo TCV Advocates is a Maltese tier-one law firm with a strong international practice and actively involved in all practice areas of commercial law, with a particular focus on corporate and financial services. The firm is committed to providing bespoke legal solutions to a number of companies and groups, firms, family offices and other entities and individuals in the relevant sectors and industries.

Our mission is to deliver high-quality services in structuring and implementing business and investment proposals in a pro-active, efficient and timely fashion, and to foster our local and international network to offer comprehensive and integrated services to clients.

Malta Business Development & Investment Promotion

FinanceMalta, a non-profit public-private initiative, was set up to promote Malta's international business and financial centre, both within, as well as outside Malta. It brings together, and harnesses, the resources of the industry and government, to ensure Malta maintains a modern and effective legal, regulatory and fiscal framework in which the financial services sector can continue to grow and prosper.

The Board of Governors, together with the founding associations: The Malta Fund Industry Association, the College of Stockbrokers, the Malta Bankers Association, the Malta Insurance Association, the Association of Insurance Brokers, the Institute of Financial Services Practitioners, and the Malta Insurance Managers Association (which is also affiliated); its members and staff are committed to promote Malta as a centre of excellence in financial services and international business.

Regulator – Financial Services

The Malta Financial Services Authority (MFSA) is the single licensing and supervisory authority for all financial services activity. The Authority is an autonomous public institution set up by law. The sector overseen by NFSA includes banks, investment firms, insurance companies and financial intermediaries, which together provide a wide range of products and services for the domestic and international markets. The regulation of the Malta Stock Exchange also falls under the responsibility of the MFSA.

The MFSA is also responsible for consumer education and consumer protection in the financial services sector. Moreover, it manages Malta's Registry of Companies.
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15th position in financial market development

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Internal Market Scoreboard 2010

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