MALTA – THE ONE TO WATCH
MamoTCV Advocates is a tier-one law firm in Malta with a strong international practice and actively involved in all areas of commercial law, with a particular focus on financial services.

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.
Overview

Seen as a good place for start-up hedge funds, Malta is looking attractive to larger managers keen to have an EU presence in a low-cost, friendly and accessible jurisdiction.

Interview: Finance minister

Finance minister Tonio Fenech outlines Malta’s plans to grow financial services. Alternative fund development is a key part of the growth strategy.

Legal services: overview

As the financial services sector develops in Malta, the legal profession is keeping pace. Teams are expanding and lawyers are increasing their skills and knowledge.

Legal services: securitisation

New tax rules on the treatment of structured finance transactions confirm Malta’s tax neutrality and maximise the efficiency of securitisation transactions.

Fund administration

Fund administrators continue to see strong growth with more mid-sized funds now considering the jurisdiction as a good domicile.

Custody

Malta still finds a lack of choice of custodian a drawback in its plans to develop as a major fund domicile in Europe.

Accounting

As Malta’s funds sector and financial services industry grows, accountancy firms are finding it difficult to find staff and are using global networks for expertise and experience.

What they say about Malta

Malta at a glance

All reports written by Margie Lindsay.
Seen as a good place for start-up hedge funds, Malta is looking attractive to larger managers keen to have an EU presence in a low-cost, friendly and accessible jurisdiction.

Growth in challenging times

Malta may be the European Union’s smallest member but it punches above its weight in the hedge fund industry. While many believe it has still not reached critical mass, Malta’s fund sector growth is impressive, even coming from a low base.

What has been most remarkable is its continued growth, despite a challenging economic environment. Not immune from the woes of the eurozone (Malta joined in 2008), the country nevertheless is in a good position, with little external debt. However, this does not seem to have impacted the hedge fund sector. In fact, the woes of some of its fellow eurozone members may be making the tiny island state an even more attractive jurisdiction.

Over the last few years Malta has gained a reputation as a jurisdiction favoured by start-ups. This was due not just to its relatively low costs but also to an approachable regulator in the form of the Malta financial services authority (MFSA). Joseph Bannister, chairman and president of the MFSA, is widely praised for his openness and flexibility when talking with funds about strategies. However, he is also keen to protect Malta’s reputation and believes thorough vetting of every fund application is not just necessary but a prerequisite for the jurisdiction. The MFSA overall has an open-door policy, encouraging managers to discuss their strategies before applying for registration. This helps both sides speed up the process and quickly establishes if Malta is the place for the fund or management company.

Malta’s fund sector has seen substantial growth in 2011 with more funds and sub-funds licensed between January and September than in all of 2010, according to Bannister. He attributes this increase to the rise in Ucits-compliant funds as well as the continued popularity of the professional investor funds (PIFs), the structure of choice for hedge funds. Bannister says the MFSA’s open-door policy, which encourages managers and companies to discuss plans and how strategies and ideas fit into regulations, is helping attract more hedge funds to Malta.

Elsewhere in the EU regulators in Ireland and Luxembourg are widely reported to be difficult to approach, particularly for new funds. Ireland’s continuing economic problems coupled with a regulator that appears to be concentrating more (understandably) on banking and internal measures rather than development of the funds sector, is not usually seen as the first choice by many new funds. Luxembourg is costly and short of space.

Approachable regulator

What Malta’s fund industry hopes is that the natural choice for managers will be their island. “I think operators are increasingly finding it more easy to operate here. It’s not a question of lighter regulations because here we are bound by the EU directives. But I think the fact that we still manage, and I hope that we will continue to manage, to have meetings with operators, discuss their plans, see how these fit in within the regulations, make necessary suggestions, and engage in the whole thing, makes us attractive,” says Bannister.

He is clear that engagement is one of the key reasons more fund managers are looking at Malta. For London-based managers he thinks it is particularly attractive; just an overnight stop or even a day trip to hold board meetings or discuss issues with service providers, including the MFSA.

“We’re finding more people here than in all of 2010, according to Banister. He attributes this increase to the rise in Ucits-compliant funds as well as the continued popularity of the professional investor funds (PIFs), the structure of choice for hedge funds. Bannister says the MFSA’s open-door policy, which encourages managers and companies to discuss plans and how strategies and ideas fit into regulations, is helping attract more hedge funds to Malta.

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just the lower costs in Malta but of also of the proliferation of platforms where funds can ‘plug and play’ for a relatively low fee. “I think Malta has a key advantage when it comes to costs and therefore we’re still seeing an increased level of business here,” he says. “I still think [Malta’s] a niche for the alternative funds looking to set up new funds, hoping to grow very quickly with a low total expense ratio. TER is significant in the fund sector, particularly with start-ups.”

He says the country is continuing to attract a lot of start-ups but at the same time larger funds are beginning to look at the jurisdiction. In particular Swiss fund management companies, looking for a presence in the EU, are giving Malta more than a quick glance, finding Luxembourg crowded and unresponsive and Ireland too far away and less familiar.

**Friendly tax regime**

Another factor encouraging migration of fund managers and fund vehicles to the island is the friendly tax regime. Bannister at the MFSA is keen to attract qualified persons throughout the financial services sector, including insurance, banking and investments. Personal income tax is capped at 15% for a period of five years. “They can have their bonuses also taxed here but obviously they have to be resident here,” notes Bannister.

The generous tax limit is helping to attract much-needed expertise to the island. The idea is that the expatriates needed to build the financial services sector, including funds, will gradually train local staff.

Aside from local initiatives aimed at making the jurisdiction more attractive, Malta like all EU members is facing the introduction of the alternative investment fund managers (AIFM) directive. Bannister is positive about the new rules. He believes managers needed more regulation. “What we needed were some basic rules in each jurisdiction,” he says. With AIFM, managers will at least have the general principles the same in all the jurisdictions. As with other EU fund jurisdictions, Malta is keen to have the directive in place. According to law firm Ganado & Associates, Malta should have no problems implementing the directive, although some of the requirements may be a challenge for the jurisdiction. For example, the AIFM directive will require the prime brokers appointed by the PIFs to be based in Malta. The objective of the directive, believes Ganado, is to retain the flexibility of the PIF regime and the challenge is how the fund manager will structure the PIF under the directive.

**Investment services**

<table>
<thead>
<tr>
<th>Category</th>
<th>New licences</th>
<th>Surrendered licences</th>
<th>Total licences as at end 2010</th>
<th>New licences (Jan-Sept)</th>
<th>Surrendered licences (Jan-Sept)</th>
<th>Total licences as at end Sept 2011</th>
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<tbody>
<tr>
<td>Category 1a</td>
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<td>0</td>
<td>5</td>
<td>0</td>
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<tr>
<td>Category 3&amp;4</td>
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<td>0</td>
<td>2</td>
<td>0</td>
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<td>2</td>
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<td>Category 4</td>
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<td>0</td>
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<td>1</td>
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<tr>
<td><strong>Total</strong></td>
<td><strong>22</strong></td>
<td><strong>8</strong></td>
<td><strong>102</strong></td>
<td><strong>14</strong></td>
<td><strong>5</strong></td>
<td><strong>111</strong></td>
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</table>

* a One licence was upgraded from Cat 1a to Cat 2.
* b One licence was upgraded from Cat 1a to Cat 2 and another licence was upgraded from Cat 2 to Cat 3.
* c One licence was upgraded from Cat 2 to Cat 3. Source: Malta Financial Services Authority.

**Recognised fund administrators**

<table>
<thead>
<tr>
<th>Recognised fund administrators</th>
<th>New licences</th>
<th>Surrendered licences</th>
<th>Total licences as at end 2010</th>
<th>New licences (Jan-Sept)</th>
<th>Surrendered licences (Jan-Sept)</th>
<th>Total licences as at end Sept 2011</th>
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</thead>
<tbody>
<tr>
<td>Recognised fund administrators</td>
<td>5</td>
<td>0</td>
<td>18</td>
<td>6</td>
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<td>24</td>
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</table>

Source: Malta Financial Services Authority.

**Collective investment schemes**

<table>
<thead>
<tr>
<th>Schemes</th>
<th>New licences</th>
<th>2010 Total licences</th>
<th>Total licences as at end 2010</th>
<th>New licences (Jan-Sept)</th>
<th>Surrendered licences (Jan-Sept)</th>
<th>Total licences as at end Sept 2011</th>
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</thead>
<tbody>
<tr>
<td>Pifs</td>
<td>Qualifying investor</td>
<td>95</td>
<td>73</td>
<td>251</td>
<td>115</td>
<td>18</td>
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<td></td>
<td>Extraordinary investor</td>
<td>1</td>
<td>3</td>
<td>15</td>
<td>13</td>
<td>0</td>
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<tr>
<td></td>
<td>Experienced investors</td>
<td>6</td>
<td>5</td>
<td>40</td>
<td>4</td>
<td>1</td>
</tr>
<tr>
<td>Total</td>
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<td>102</td>
<td>81</td>
<td>306</td>
<td>132</td>
<td>19</td>
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<tr>
<td>Ucits</td>
<td>Schemes</td>
<td>4</td>
<td>0</td>
<td>8</td>
<td>2</td>
<td>10</td>
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<tr>
<td></td>
<td>Schemes (including sub-funds)</td>
<td>5</td>
<td>0</td>
<td>50</td>
<td>14</td>
<td>5</td>
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<tr>
<td>Non-Ucits</td>
<td>Schemes</td>
<td>0</td>
<td>1</td>
<td>11</td>
<td>1</td>
<td>0</td>
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<tr>
<td></td>
<td>Schemes (including sub-funds)</td>
<td>0</td>
<td>6</td>
<td>30</td>
<td>2</td>
<td>1</td>
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<td>Foreign</td>
<td>Schemes</td>
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<td>1</td>
<td>5</td>
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<td>0</td>
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<td>Schemes (including sub-funds)</td>
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<td>22</td>
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<td>Recognised private CIS</td>
<td>Schemes</td>
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<td>2</td>
<td>2</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td></td>
<td>Schemes (including sub-funds)</td>
<td>1</td>
<td>2</td>
<td>2</td>
<td>0</td>
<td>0</td>
</tr>
</tbody>
</table>

Source: Malta Financial Services Authority.
He says the MFSA is already looking at the AIFM directive and will decide by the end of the year on how to implement it. He believes 90% of the directive’s strictures will be able to be addressed through Malta’s ‘rule book’ or guidelines issued by the MFSA which have the force of law.

A new type of manager?
Bannister also confirmed the MFSA is looking at a new category of hedge fund manager. “We will be looking at a category of hedge fund managers which will be different to Ucits and non-Ucits and unlike any other jurisdiction,” he reveals.

He believes Malta’s ideas could give it a competitive advantage vis-à-vis Luxembourg and Ireland. Others say the regulator could be looking at how to accommodate managers from outside the EU.

Looking ahead, he is keen to continue growing the financial services sector overall and in particular the fund side. Regulatory oversight of fund service providers will be increased. Bannister is keen that the regulator retains a good relationship with all areas of fund management and servicing. He wants to strength the onsite visits of the regulator as well as increasing oversight of the corporate governance side of fund managers, particularly ensuring board meetings are taking place and numbers of outside experts coming in to help develop new skills and teach locals.

The MFSA is also keen to attract more custodians and could also be looking, with one eye on the AIFM directive, at attracting more prime brokerage services to the island.

Although the global macro economic outlook may be grim, Malta’s fund sector is confident of continued growth, even in the face of a global recession. Most on the island believe the jurisdiction’s attractions, including not only cost benefits but also a stable economic and political outlook, will be positives for larger fund managers in future too.

Malta’s professional investor funds (PIFs)

<table>
<thead>
<tr>
<th>Regulatory requirements</th>
<th>PIFs sold to experienced investors</th>
<th>PIFs sold to qualifying investors</th>
<th>PIFs sold to extraordinary investors</th>
</tr>
</thead>
<tbody>
<tr>
<td>Licensing requirements in terms of the ISA</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Target investors</td>
<td>Experienced</td>
<td>Qualifying</td>
<td>Extraordinary</td>
</tr>
<tr>
<td>Custodian/prime broker requirement</td>
<td>Yes</td>
<td>No (1)</td>
<td>No (1)</td>
</tr>
<tr>
<td>Self-managed option</td>
<td>Yes (2)</td>
<td>Yes (2)</td>
<td>Yes (2)</td>
</tr>
<tr>
<td>Minimum investment</td>
<td>€10,000</td>
<td>€75,000</td>
<td>€750,000</td>
</tr>
<tr>
<td>Investment/borrowing restrictions</td>
<td>Leverage for investment purposes up to 100%; use of derivatives for efficient portfolio management unlimited (other restrictions apply)</td>
<td>None</td>
<td>None</td>
</tr>
<tr>
<td>Fit and proper test: service providers and directors</td>
<td>Compulsory</td>
<td></td>
<td></td>
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<tr>
<td>Reporting</td>
<td>Interim (if applicable) and annual</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Legal form of the PIF</td>
<td>Investment company with fixed or variable share capital company; limited partnership; unit trust; mutual fund; incorporated cell companies</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Review of application documents</td>
<td>Within seven working days response (3)</td>
<td>Within seven working days response (3)</td>
<td>Within three working days response (3)</td>
</tr>
</tbody>
</table>

1 Provided there are appropriate safekeeping arrangements in place. 2 subject to a number of local presence requirements. 3 if external parties are all established in recognised jurisdictions. Source: PricewaterhouseCoopers

Malta’s financial services legislation

Primary legislation
Banking Act
Financial Institutions Act
Insurance Business Act
Insurance Intermediaries Act
Investment Services Act
Special Funds Act (Retirement Pensions Act)
Trustees and Trusts Act
Malta Financial Services Authority Act
Central Bank of Malta Act

Supporting legislation
Companies (includes limited partnerships) Act
Netting upon Insolvency Act
Securitisation Act
Prevention of Financial Market Abuse Act
Professional Secrecy Act
Prevention of Money Laundering Act
Companies Act. Continuation of Companies Regulations 2002

Malta’s credit rating

<table>
<thead>
<tr>
<th>Moody’s rating</th>
<th>Moody’s outlook</th>
<th>Fitch rating</th>
<th>Fitch outlook</th>
<th>S &amp; P rating</th>
<th>S &amp; P outlook</th>
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</thead>
<tbody>
<tr>
<td>A2</td>
<td>Negative</td>
<td>A+</td>
<td>Stable</td>
<td>A</td>
<td>Negative watch</td>
</tr>
</tbody>
</table>

What Moody’s Investors Service says
Malta’s foreign and local currency government bond ratings are A2 with a negative outlook, reflecting medium economic strength, high institutional strength, medium government financial strength and low susceptibility to event risk. Malta’s medium economic strength reflects its small and open economy, which displays moderately favourable long-term economic prospects, while a relatively high GDP per capita denotes a high level of economic development. Other key factors supporting Moody’s assessment include a rather well-educated labour force with relatively low wages and an attractive tourism infrastructure that caters to core European markets. Income convergence to EU levels over the past decade has advanced at a vigorous pace, benefiting from sizable foreign direct investment (FDI) inflows linked to EU accession. FDI has helped to finance Malta’s recurrent external deficits, which are common to island economies.
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Finance minister Tonio Fenech outlines Malta’s plans to grow financial services. Alternative fund development is a key part of the growth strategy.

Steady growth, confident outlook

While the sovereign debt crisis in Europe has dominated headlines and European Union meeting agendas, Malta has quietly continued to build on its reputation as a reputable and growing hedge fund jurisdiction.

Despite the sovereign crisis in Europe, the financial services sector in Malta will bring in double-digit growth of over 30% in 2011. This puts the industry firmly on target to hit its overall growth target for 2015 of accounting for 25% of gross domestic product (GDP) in Malta.

“Despite the turmoil that has shaken the world’s financial market over the past three years, Malta’s financial services industry has continued to grow at a rapid pace,” declares finance minister Tonio Fenech. A main driver of financial services growth has come from the funds sector.

Although the fund industry is a vital part of the financial services sector, the 25% target includes the extended industrial cluster that is built around financial services, including legal service, office space industry, property and other services that benefit from growth in this sector.

Malta’s ambition to become an international financial centre in the Mediterranean is not new. In the late 1980s the government started planning this development. What the government at the time could not have predicted, however, was the attraction the island would hold for the hedge fund industry.

“Malta has really and truly experienced strong international growth over these last five years,” notes Fenech. “This was primarily driven by Malta’s membership in the EU which I believe was the catalyst that led to this paradigm shift of the industry from being one led by insular business to becoming a truly international sector.”

While the financial crisis of 2008 and the subsequent eurozone predicament in 2011 have impacted Malta, Fenech believes the challenges thrown up by these twin blows to the economy were “well managed”.

“The financial sector has continued to register year-on-year strong growth numbers. Our legislative and regulatory framework has been continuously updated to ensure that Malta remains competitive,” he says.

Malta has seen a surge in the level of local service provision to all types of funds. The number of domiciled funds that are managed in Malta in 2010 increased from 22% to 44% while the number of Maltese funds administered locally increased from 47% to 78%. “Clearly this is in itself a testament of Malta’s increased competitiveness in the funds servicing sector with Malta-based administrators today administering funds also domiciled in the Cayman Islands, British Virgin Islands and the Channel Islands among others,” says Fenech.

The minister is also keen for Malta to take advantage of the increasing popularity of Ucits hedge funds. “With more funds seeking EU onshore domiciles, fund promoters previously focused on the private placement market are becoming increasingly interested in the distribution opportunities presented by Ucits,” states Fenech.

The introduction of Ucits IV is expected to bring a “lot of opportunities to Malta that could continue to drive the Maltese fund sector forward”.

But Ucits is not the only factor driving growth in the funds area. Overall, there has been a 100% increase in the number of funds licensed in 2011 and a surge in new fund services operations. “Not only has the industry understood the importance of having all the legislation in place from day one but it has also recognised the importance of opening up new channels by strengthening regulatory ties with counterparts in China, Singapore and Latin America,” adds Fenech.

The minister emphasises the regulator, the Malta Financial Services Authority (MFA), “is conscious of the fact that international regulatory co-operation and exchange of information is essential if the market is to develop”.

Ucits driving growth

Again, the popularity of Ucits products is helping to drive growth. “This is particularly true of the Latin American market where Ucits are considered the foreign investment opportunity of choice for local pension funds in a growing number of South American countries,” he adds.

In other parts of the world, such
as Asia, UCITS is also seen as the ideal vehicle to channel wealth into investment opportunities in emerging economies such as those of Brazil and neighbouring countries. The MFSA has signed some 40 bilateral or multi-lateral memoranda of understanding and protocols with other regulators worldwide to help boost sales of UCITS products. Such deals are giving Malta another plus point, particularly for investors looking to structure tax-efficient vehicles.

Malta came late to the UCITS scene and at first was keen on promoting the brand. As more hedge fund managers began to use UCITS wrappers and the market grew, the MFSA became more enthusiastic. The implementation of UCITS IV on July 1, 2011 was another catalyst for the regulator. According to Fenech, UCITS IV “fits in perfectly with Malta’s long-declared, open architecture policies and opens up new possibilities in the management and structuring of funds under the UCITS stamp”.

The key investor information document (KIID), the master-feeder framework and cross-border merger regime all introduced under the latest version of the directive, bring greater transparency and more flexibility in the structuring of funds. “There are strong indications that the new UCITS IV will place Malta’s growth as a fund domicile and servicing centre at a higher level,” claims Fenech. “With more funds seeking EU onshore locations, fund promoters who have hitherto focused on the private placement market have also become increasingly interested in the distribution opportunities presented by UCITS. Some have taken the redomiciliation route to Malta specifically with this in mind.”

However, one shortcoming of Malta’s expansion in the UCITS marketplace is a lack of choice of custody services available in Malta. Although it has already improved compared with what it was a couple of years ago, more providers are needed. Fenech says the MFSA is in discussions with at least two European banks that are actively interested in entering the Maltese hedge fund sector. International banks already on the ground offering custody include HSBC and recent newcomer Deutsche Bank. Austria’s Sparkasse offers custody services for smaller players and Bank of Valletta has formed a joint venture with JP Morgan to provide global custody services.

The growth of Malta’s fund industry has so far been driven by alternative investment funds, but lately the increased demand for UCITS fund structures has overshadowed the hedge fund growth. Although this trend is expected to continue, the government believes hedge funds will be more dominant than UCITS products in Malta.

Aside from UCITS there are opportunities for distributing European-based funds on a private placement or institutional basis in some South American countries, notes Fenech. Closer to home, Fenech admits the future of the European funds industry will be dominated by the introduction of the alternative investment fund managers (AIFM) directive and decisions taken by the European Securities and Markets Authority (ESMA) as well as the European Commission on the law’s implementation.

“The MFSA understands the importance of this process to the future of the alternative funds industry in Europe and is fully engaged in the discussions surrounding its implementation,” says Fenech. “Beyond that, the primary aim is to transpose the AIFM directive into Maltese legislation in as clear and seamless a manner as possible. This entails extensive consultation both with other European supervisory authorities as well as with industry.”

Positive regulation

Fenech is positive about the overall impact EU fund regulation will have on Malta. “It is clearly evident that many fund managers that established funds offshore will have a rethink on their strategy going forward. In effect we have already witnessed and experienced the redomiciliation of schemes from offshore jurisdictions to Malta. However, the biggest impact will in my view be the registration of new funds as I believe that a new trend will emerge with these being domiciled in onshore Europe.”

Although one of the smallest EU members, Malta is known to punch above its weight, particularly on issues affecting the hedge fund industry. Fenech confirms the MFSA “is a very active member” of ESMA and is involved in its work not only on the board of supervisors but at every other level through various committees and working groups. “Through this participation in the formal work of ESMA as well as the informal sharing of ideas with its peers, the MFSA seeks not only to enhance its experience and expertise but also to encourage balanced development of regulation in the interest of the stability and the future development of the European hedge fund industry,” says Fenech.

While EU regulation dominates the headlines, at the same time the MFSA is conscious it needs to maintain what Fenech calls an “ongoing regulatory development effort” in order to continue development of the funds sector in the country. Various initiatives are currently underway to review legislation that has a bearing on the funds industry. This includes securitisation and trust legislation as well as the introduction of new concepts such as the incorporated cell company (ICC). Other areas under review reflect the growth in exchange traded funds (ETFs) and high-frequency trading. There are also potential developments at EU regulatory level in some of these areas.

The MFSA and government are also currently working on a number of legislative initiatives that will provide further scope for the setting-up of alternative and other types of funds in Malta, according to the minister.

Recently attention has been given to making Malta even more attractive to investment services operators by further improving the tax environment for high net worth individuals and to encourage top-end international finance executives to move into the Maltese financial services industry. Fenech says the government is also addressing “a number of other structural issues in Maltese tax legislation” as evidenced by recent changes in tax
provisions related to securitisation operations and foundations.

“There are a number of initiatives that have already been undertaken by the government of Malta and various other stakeholders to ensure that the industry’s growth is sustained,” declares Fenech. “These include the timely introduction of EU directives, the introduction of the highly qualified persons rules as well as initiatives to strengthen female participation in the workforce.”

For Fenech another issue that needs to be addressed in order to boost financial services concerns employment. Retraining programmes and attracting more service providers to Malta is high on the agenda.

Although the island state is already home to more than 500 funds, 21 fund administrators and more than 10 investment services licence holders, the government believes even more businesses will consider Malta as a base in future.

The strong growth of financial services in recent years has highlighted the “significant” need for additional highly qualified workers. “The need is being felt for the importation of knowledge, particularly in those areas of the financial services sector where local expertise is lacking,” admits Fenech.

“The objective of Legal Notice 106 Highly Qualified Persons Rules 2011 is the creation of a scheme to attract highly qualified persons to occupy ‘eligible office’ with companies licensed and/or recognised by the MFSA. Clearly, this scheme addresses Malta’s highly evident realities and is aimed to ensure that the growth of the industry is sustained through the continued availability of skilled resources. This strategy is but just one of the initiatives that government has undertaken to strengthen the resource base of the industry,” he adds.

Fenech says the government is “investing heavily” in local training and educational institutions, including financial services courses at the University of Malta, training programs by MCAST, Malta’s vocational training institution, and through specific programmes being organised by the MFSA.

The private sector is also playing an important role in supporting training and development. “We are confident of building on this success in 2012,” says Fenech.

Tax matters
Another reason Malta has been successful in promoting its funds industry is the country’s extensive network of tax treaties. Although it is a small jurisdiction, it has 57 comprehensive double-taxation agreements in force. Malta has also signed double-tax agreements which are all waiting to be ratified with Bahrain, Israel, Switzerland, Turkey and Uruguay. Agreements with Bosnia and Herzegovina, Guernsey, Hong Kong, Mexico, Oman, Russia, Saudi Arabia and Ukraine have been successfully negotiated but are also waiting to be signed and ratified before they enter into force. Negotiations with Azerbaijan are also advanced but not yet concluded.

While Malta has been developing as an onshore domicile and is recognised “as a highly functional, cost-competitive, well-regulated jurisdiction with the underlying theme being availability of skilled and experienced personnel,” says Fenech, the government has ambitious plans for the future.

“My view is that Malta’s position as a servicing hub will continue to be driven by regional business, as is being evidenced in other economic sectors. There is strong interest in Malta being used to service international business,” says Fenech.

He says Malta is “uniquely positioned” in the Mediterranean and could become an “excellent EU regional hub”. Its geographic position is also, he believes, helping the country become more attractive as an international hub for financial services, particularly with the political developments in North Africa and the Middle East.

Fenech believes Malta can leverage its physical location as well as its close ties with the Middle East and North Africa to promote Islamic finance, too. “We have seen the use of various special purpose vehicles (SPVs) as part of international Islamic finance transactions. The main attraction so far has been that Malta structures put Islamic finance on a level playing field with conventional finance. This has been possible through the use of certain legislative instruments such as the Trusts and Trustees Act combined with the income tax legislation, which provide for an excellent platform for Islamic finance transactions.”

Malta’s geopolitical and geo-strategic position combined with EU membership has been of significant importance, believes Fenech. “Malta is developing as an important centre for SPVs for Islamic finance transactions. With respect to the funds industry there is a clear interest from various organisations as well as the takaful [Islamic insurance] and banking industries,” he continues.

Fenech points to the presence of senior figures from Islamic finance institutions in Malta. The formation of the World Islamic Finance Institute in Malta, he believes, is another indication of the “trust that international organisations such as Al Baraka Banking Group, Kuveyt Turk Participation Bank and Ernst & Young (Bahrain) have in Malta”.

According to Fenech, local banks have also been exploring the idea of linking with Islamic banks to provide financing or to offer Islamic finance investment products. “We are positive that particularly the funds industry will start reaping the benefits of the efforts made.”

The fact that the Chartered Institute of Management Accountants (Cima) qualification in Islamic finance is being offered in Malta is another clear indication of where the industry wants Malta, declares Fenech. The publication of a book by the Malta Institute of Management on Units IV and Islamic funds is “further confirmation”, he says.

Fenech believes “the knowledge and expertise gained in the Islamic finance sector and through local alliances with international organisations, combined with the knowledge in creating a robust regulatory framework, will allow Malta to take a leading role in the development of Islamic finance in the Mediterranean, particularly in the North Africa region but also in southern Europe such as Italy.”
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As the financial services sector develops in Malta, the legal profession is keeping pace. Teams are expanding and lawyers are increasing their skills and knowledge.

Challenging structures

If the quality of legal services is an indication of Malta’s standing in the hedge fund world, then the island state is well on the way to being a major jurisdiction. Although only local law firms are present in any significant number on the islands, a good number have embraced the opportunities and challenges offered by the growing financial services industry and the hedge fund sector in particular.

All are reporting increased business and more in the pipeline, although the volume varies from firm to firm and the type of work is also different between legal firms.

According to David Griscti, a partner at David Griscti & Associates, his firm saw a lot of new work in the first half of the year. A volatile summer for hedge funds slowed the pace but he says “over September we’ve seen a surge of new scheme applications coming through with a variety of strategies”. While he says the majority of the work is in traditional strategies, some of the more exotic funds are looking at Malta as a domicile of choice.

“Definitely one of the reasons is the willingness of the regulator to listen to a manager explain his strategy. The other reason is also cost. Very often these types of new strategies would not be in a position to raise significant amounts of start-up subscriptions. So obviously it is then prohibitive to set them up in jurisdictions such as Luxembourg and even Ireland to a certain extent,” he says. “Malta is more accommodating. We’ve seen for example the setting-up of an art fund. We’re also seeing funds being set up, for example, with strategies in the alternative energy sector with an interesting mix of real and market driven assets in that sector. We see tremendous scope there for new entrants into the market,” he says.

At Fenech & Fenech, Joseph Ghio agrees. He, too, is seeing more esoteric strategies finding a home in Malta. “It’s pushing the envelope not only for the practitioner such as ourselves but also for the MFSA [Malta Financial Services Authority], particularly with these type of specialist funds. So we have to be creative in how to structure the fund within the terms of our regulative framework.” This is particularly tricky when the fund goes to appoint an independent director. “The MFSA has to be sure, keeping in mind how important our reputation is, and take a view as to whether a particular person has the expertise in dealing or choosing, for example, fine wine,” explains Ghio.

“The regulator is not only concerned with the rules but how to apply a particular fund situation within those rules. In these cases, of course, it’s understandable that the time to market can be slightly longer,” he adds.

Swiss attraction

Another trend Griscti sees is interest in the jurisdiction from Swiss-based managers. The reason is that the vast majority of Swiss managers are self-regulated. The Swiss regulator, however, is changing the rules. So, rather than contend with stringent criteria at home, many are looking at basing themselves in Malta, with the added benefit of being in a European Union jurisdiction.

He confirms that some managers, with funds in the $100-$300 million range have decided the best option would be to move completely to Malta. Griscti thinks the addition of Swiss managers will be welcome. “It is an interesting opportunity for the jurisdiction in terms of attracting quality, in terms of creating quality employment in the sector.”

He continues: “We’re still very, very small but definitely if you look at certain surveys that have come out recently, Malta is getting a decent amount of business.”

For Griscti, the basis of Malta’s success is commonsense. “This is so important at this stage, that we don’t go over the top. It’s important that the regulator does not become inflexible because that is an absolute driver for Malta.”

Like others in the legal profession, he is wondering what the MFSA will look like when Joseph Bannister, current chairman, finishes his term of office in a couple of years. “Bannister has been a fantastic ambassador for Malta and financial services but I think financial services has grown to such an extent where it’s not a one-man thing. There are certainly capable people out there who could succeed him.”

Certainly Ghio at Fenech & Fenech is equally positive about the future and believes Malta will continue to boom. He says the funds industry has grown substantially and believes overall the island has reached critical mass and is on the map as far as European fund jurisdictions go.

“If we look at the development of the funds industry in Malta, perhaps to use Churchill’s words, this is the end of the beginning. We’re very bullish looking at our prospects in the years to come, not as a developing jurisdiction but as a developed jurisdiction which is firmly on the map alongside Dublin and Luxembourg,” notes Ghio.

Nevertheless Ghio is not complacent. “Although we have had a lot of traction and continue to have a lot of traction, we need to continue working harder on our visibility. Word of mouth will always remain our best marketing tool but I think we have to be more creative in the way not only within Europe but also an international context. We have to increase our profile,” he states.

One new element that has come to Malta since 2010 is the fund platform. “Our practice has been active in the adding up of new sub-funds to existing fund platforms which are promoted..."
generally by administrators. “The platforms make launching in Malta not only easier but also cost effective. “Coupled with that, we have also seen quite some work with a new type of fund set up that can be licensed in Malta which is in the form of incorporated cell companies. It’s still early days but we have seen quite some interest there as well,” continues Ghio.

He also says the firm has seen increased interest from US promoters – something that was lacking in the past. One attraction may be the use of English as one of the two official languages for legislation. “Just in the same way as Luxembourg particularly.”

He and others in his firm and elsewhere in the legal services area believe the island has a solid future in the funds sector. All agree that the introduction of more specialisations with financial services will be even more attractive to fund managers, looking for a stable jurisdiction within the EU in which to base their funds. -

One of the largest law firms in terms of fund business, Ganado & Associates, also has seen increased activity and believes as others it is due to attractive regulation and wider recognition of Malta as a jurisdiction for funds.

“Effectively this year was a little of a frenzy, as last year [2010] was a manager’s year because we set up a large number of fund management companies in Malta,” says Joe Farrugia, a partner at the firm.

In 2011 the trend was mixed. The firm saw a record number of funds establishing, with it estimating it handled at least half of all the hedge funds set up in Malta. “The increase has been substantial and has been very encouraging,” he says.

In the second and third quarters of 2011, the mood slightly changed. “The bulk of the work was still on the professional investor fund (PIF) side. The PIF work is steady and we have about 17 fund structures being set up.” But the proportion of Ucits versus PIF has changed. Before there was an absolute majority of PIF. “Now we are seeing Ucits gaining ground and the proportions seem to be about 65%/35% with 35% being Ucits and 65% being PIFs.”

Partner Max Ganado is enthusiastic about the future. He points to the Securitisation Act as a major piece of legislation. “Not in the old form of securitisation, because now the whole landscape has changed. In securitisation we’re going forward and there will still be a need for securitisations,” he says. “Grouping assets and converting them into securities for purposes of easier and more liquid investment, that’s a good tool.”

He believes this shows that Malta is not a one-trick pony. “Now people are using Malta generally for many things. You start having crossover. You find people interested in suing Malta companies,” notes Ganado.

He and others in his firm and elsewhere in the legal services area believe the island has a solid future in the funds sector. All agree that the introduction of more specialisations with financial services will be even more attractive to fund managers, looking for a stable jurisdiction within the EU in which to base their funds. -

Malta’s tax regime

Collective investment schemes
- Maltese-licensed collective investment schemes may be set up in various forms: corporate, unit trust, partnership.
- Maltese-licensed funds investing outside Malta are tax-exempt.
- No tax is charged on distribution of profits to non-residents share/unitholders.
- Gains on share/unit transfers by non-residents normally exempt.
- No capital/stamp duty on issues/units and exemption available on transfers of shares/units in licensed funds.
- No net asset value tax or other taxes on fund assets.

Tax relevance to asset management companies
- Maltese companies are resident and domiciled in Malta (for example, taxed on their worldwide profits); other bodies of persons (such as general/limited partnerships) are resident where management and control is located.
- Companies incorporated outside Malta but managed and controlled in Malta are resident but not domiciled in Malta (for example, taxed on a remittance basis).
- Standard corporate tax rate is 35%; unlimited loss carry-forward.
- Participation exemption for dividends/gains derived from qualifying participations (minimum 10% holding or lower holding with investment of €1.164 million-plus or with entitlement to appoint a director on subsidiary’s board), subject to satisfaction of a rather straightforward anti-abuse provision.
- Participants of dividends paid out of profits taxed in Malta may be entitled to a full or partial refund of the tax paid by the distributing company.
- Dividends do not actually need to be paid (for example, profits can be capitalised by way of a bonus share issue and/or merely credited to shareholders).
- Refunds reduce Maltese tax leakage to between 0% and 10% in most cases.
- Size of refund depends upon nature of the profits being distributed and if double tax relief was claimed in Malta thereon.
- Such tax refunds are the fundamental basis of international tax structuring using Malta.
- Tax refund mechanism under Maltese tax law was amended in 2007 to reflect discussions with EU and state aid Code of Conduct. However, the refund concept has been there since 1994.
- Tax refunds payable by Revenue typically within around two weeks from tax payment by distributing company.
- No thin capitalisation /interest-capping rules, very flexible transfer pricing.
- No withholding tax on dividends; interest and royalties paid to non-residents.
- No capital gains tax on most transfers of shares in Maltese companies by non-residents.
- Possibility of advance rulings on international tax issues.

Expatriates working for asset management companies
- Expatriates working for the Maltese (licensed) asset management company may be entitled to certain tax benefits.
- Two systems are in place in this respect: a) tax exemption on a number of fringe benefits for a 10-year period (accommodation, provision of car, medical expenses, school fees for children), or b) flat rate of 15% (Maltese tax rates for individuals go up to 35%) on income from qualifying employment (specified senior positions may qualify).
- The above systems are subject to some statutory conditions but if they apply in the particular circumstances, they may result in substantial tax savings for such expatriates.

Source: PricewaterhouseCoopers
New tax rules on the treatment of structured finance transactions confirm Malta’s tax neutrality and maximise the efficiency of securitisation transactions.

Last piece in finance legal puzzle

While tax matters may sometimes make eyes glaze over, Malta’s new securitisation tax rules covering the treatment of structured finance transactions confirm the principle of tax neutrality applying to Maltese securitisation vehicles, says Richard Ambery, a partner at Ganado & Associates. “In our view the effect of the new rules maximises the efficiency of securitisation transactions undertaken in and through Malta by eliminating tax leakage in vehicles established there.”

In general Malta’s securitisation laws are good news for hedge funds. The laws should help establish Malta as a ‘domicile of choice’ for the structuring of securitisation transactions, according to Ambery, who specialises in practice areas, investment services, investment funds capital markets and derivatives banking. The Securitisation Act protects securitisation creditors’ supremacy if there is an insolvency.

Other European Union fund jurisdictions are not making it simple for hedge funds. “One of the restrictions in Ireland,” says Ambery, “is that you need to establish your vehicle under section 110 of the tax code.” Section 110 companies are restricted to buying financial assets in limited categories.

The Malta Financial Services Authority (MFSA) does not require vehicles aimed at qualified investors to be pre-approved. A fund is not required to get a pre-ruling by the MFSA if it does not offer the securities to the public and only to certain classes of investors.

“We believe the effect of the new rules on securitisation transactions, coupled with the flexible regime offered by the Securitisation Act, underlines Malta’s competitiveness in the field of structured finance,” says Ambery.

The Securitisation Act, which came into force in 2006, provides what Ambery says is a comprehensive statutory framework for a wide variety of securitisation, including asset, synthetic and life settlements securitisation as well as insurance risk and whole business securitisation. The act was designed to facilitate domestic and cross-border securitisation transactions. Previously a number of provisions in Malta’s Civil Code had created barriers to creating efficient securitisations, particularly compared with other jurisdictions.

The act also applies a special statutory regime for bankruptcy remote- ness, true sale, creditor protection and debtor notification in securitisation transactions to remove most, if not all, of the uncertainties that have doffed structured financings in many other jurisdictions, according to Ambery. He also thinks the rules represent the “final piece in Malta’s legislative jigsaw” for structured finance. A ‘securitisation asset’ is defined as ‘any asset, whether existing or future, whether movable or immovable, and whether tangible or intangible, and where the context so allows includes risks’.

Keeping it simple

There are only two principal aspects of regulation: the constitutive documents of the securitisation vehicle must include a statement that it is established subject to the provisions of the act; and the MFSA must be notified if a securitisation vehicle is going to be used in one or more transactions in or from Malta.

The act enables securitisation vehicles to be established either as a company, including an investment company, a commercial partnership, a trust (created via a written instrument) or any other legal structure the MFSA considers appropriate. The most logical form of securitisation vehicle to use in Malta is probably a private limited company owned by a purpose founded.

Malta wanted to avoid as far as possible the legal uncertainty inherent in common-law jurisdictions surrounding the treatment of a sale of receivables into a securitisation on a subsequent insolvency of the originator.

A provision of the act provides that no insolvency proceedings attributable to an originator are capable of impinging on the securitisation assets transferred to the securitisation vehicle. Any action taken to consolidate the assets of one of the vehicle’s affiliates with those of the securitisation vehicle itself is specifically excluded by the act.

Legal reform also extended to transfers of financial assets. The act allows for a number of possibilities; novation, sale, assignment or a declaration of trust.

The rules also make securitisation vehicles tax efficient. Under rule four a securitisation vehicle can deduct other expenses, according to Ambery. These consist of sums payable by the securitisation vehicle to the originator or assignor of the securitised risk or assets, premium, interest or discounts in relation to the financial instruments issued or funds borrowed by the securitisation vehicle as well as any expenditure insured by the vehicle for its operations and collection of receivables. The fees of third-party service providers, including the originator, are also deductible.

If any income remains after the expenses are deducted the vehicle can opt to deduct the resulting profit, if this is brought into account by the originator. Using this option is subject to the irrevocable written consent of the originator or assignor in terms that are satisfactory to the Malta Inland Revenue.

The cost of acquisition of the securitisation assets or the cost of the assumption of risk and any optional additional deduction for income are also considered as income. The rule provides that the originator’s income, if arising in Malta, can be considered as profit and will be subject to the usual tax rules, unless the management and control of the business of the originator is not in Malta.”

“In our view the effect of the new rules maximises the efficiency of securitisation transactions undertaken in and through Malta by eliminating tax leakage in vehicles established there.”

Richard Ambery
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Fund administrators continue to see strong growth with more mid-sized funds now considering the jurisdiction as a good domicile.

Growing in stages

Fund administration is not a new business for Malta. But the growth has been fast and impressive. Only a couple of years ago, less than a quarter of all funds administered in Malta were domiciled in the jurisdiction. That has now risen to over 50%. The number of fund administrators has also grown, with more than 20 now based on the island.

The reasons for the growth are varied. Malta offers a good talent pool of human resources with one of the highest university graduate percentages in the European Union. Although there are concerns about the numbers needed to continue growth, few are too concerned as the burgeoning financial services industry offers different career paths and should mean more young people look at the financial services sector for employment while the attractions of the island – sunshine, a Mediterranean lifestyle, safety, good education and a friendly population – are tempting many from outside Malta to move to the jurisdiction.

Added to this are some other attractions. One is the proliferation of small platforms, offering start-up hedge fund managers a plug-and-play model that is not just easy to access but cost-efficient, particularly when compared with Ireland and Luxembourg.

Many of the fund administrators have started their own platforms or are providing services for a variety of these structures.

In addition Malta’s regulator has wholeheartedly embraced UCITS funds and administrators are expecting a significant increase in business from this sector as well, although few expect it to equal the numbers seen in Luxembourg or even Ireland.

“We’ve seen more and more requests for UCITS, definitely, although that has slowed down a bit. In the beginning, after the first crisis, I would say UCITS was flavour of the month,” says Els Serracino Inglott, general manager at TMF Fund Administrators (Malta).

“There are some managers who are actually want to do UCITS, mainly for the name. Then when they look at the portfolio restrictions that come with it, they say, ‘Well no, actually it’s not really what we’re looking for so we will just go for a professional investor fund anyway.’ There’s definitely been more requests about UCITS,” she confirms, adding that TMF has not really seen a big shift into the structure.

At Valletta Fund Services, Kenneth Farrugia, general manager, confirms he also administers some UCITS through platform structures but says the majority of the funds are hedge funds. “We have all sorts,” he says, noting that strategies are wide and varied. They range from funds with 1,500 trades a day to ones that are fairly inactive in that sense.

“The nature of the business that we are servicing is very much reflective of the business that has come to Malta. If you look at the business, there’s quite a lot of funds that have been authorised by the MFSA [Malta Financial Services Authority]. I think some 75% of them are hedge funds. We have around 75% of our funds which are hedge funds,” adds Farrugia.

Increased popularity as domicile
Although local legislation does not make it a requirement to use a Maltese fund administrator, all service providers are reporting more business coming from funds domiciled in Malta. Farrugia believes it is important, at least in the short term, to keep this flexibility and allow funds to retain existing relationships.

He points to the tier one administrators such as Custom House, Apex and HSBC (as well as Valletta Fund Services) operating on the island as proof that the sector is healthy and has the expertise and reach needed by the larger funds now considering Malta.

While TMF, Custom House, Apex and HSBC have a global presence, Valletta Fund Services is firmly rooted in Malta. Farrugia does not think that has seriously affected his ability to pitch for business. “More fund managers will be interested in the Malta proposition and they will come here and then we’ll compete. It’s a level playing field. I think there will be instances where we will lose and there will be instances where we will win. I’m more inclined to think of the latter rather than the former. But I think it’s healthy.”

Nick Mahy, managing director at Praxis Fund Services (Malta), is equally enthusiastic about prospects. He thinks a lot of business is coming by word of mouth as well as through other local services, such as legal and accounting, suggesting locally based administrators.

“You can see the natural increase in the industry here. It’s happening quite quickly. Getting our fair share of that seems quite easy to do. It’s how much of the cake do you want? You’ve got to look at some of the business that’s coming to Malta. Some of it is coming from small and emerging managers. It isn’t as sophisticated as you’d necessarily want,” he says.

Categories of regulated funds

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<th>Retail UCITS funds</th>
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Nevertheless, Praxis is growing in terms of staff size and the number of funds under administration out of Malta. Because small and emerging managers are fee-conscious, many administrators are being aggressive in the way they are pricing services. Praxis, like many others, is more “relationship driven than pure fee driven. Because we can see how it will map out. You can see which ones are going to work well and which ones are going to be hard work.”

So while administrators in Malta are open to funds with a few hundred million as start-ups, they are clearly trying to pick the ones that should be winners and grow assets under management (AUM). Mahy also says the market is widening with a few $300 million-plus funds also coming and at least one new launch with a start-up AUM of $300 million has chosen Malta.

Global reflection
While Malta's growth has been impressive, Mahy believes it is to some extent reflecting what is happening globally as more funds spin out of investment banks and established, larger funds.

One administrator usually known for its ability to cater for smaller funds is Apex Fund Services. Anthony O’Driscoll, who set up the Malta operation, confirms he is still seeing a lot of smaller managers but has also seen an increase in hedge fund UCits as well as retail UCits, without the majority still in the traditional UCits camp.

He believes there are a number of managers in Europe looking at redomiciling or moving their investment management companies to Malta “where regulation is a bit more pragmatic than where they’re currently located. That helps. There are advantages to joining a jurisdiction where they’re going to be more than just a number. They’re not making up thousands of funds. They’re making up a very small community. Hopefully they should get a better service.”

He confirms although the number of funds administered has been growing, AUM has remained quite similar to 2010. “The fund launches we’ve seen so far have been quite small still all year. UCits will obviously increase our assets but you need more assets to make a viable UCits product, so that should have a large impact on our asset size,” he notes. He confirms the average launch size Apex is seeing is around €10-€15 million with most managers based in London or Switzerland.

For Serracino Inglott at TMF, the story is a bit different. “I think the hedge fund industry itself is rapidly changing. The situation now is completely different than it was even 12 months ago, even six months ago. It’s a completely different world for hedge funds. If you compare it to three years ago, it’s a completely new world.”

This actually seems to be seen as an advantage for Malta. Promotion of the jurisdiction has been effective and the island is now on the list of domiciles to be considered. Its reputation for sound regulation and its position as an EU member countries are plus points Serracino Inglott also believes are important.

She says funds are coming to Malta because with the alternative investment fund managers (AIFM) directive looming, managers want to be in an EU jurisdiction. They are also keen on a domicile where the regulator is responsive. Serracino Inglott confirms the funds making the move are not huge, as other jurisdictions like Ireland and Luxembourg feel the strain of numbers. He notes the MFSA is not quite as quick in approving funds as it was but it is not slow. “There was a lot of work this year to get a lot of people in the door trained and qualified.”

SGGG Fexo has seen a strong increase in new business since January 2010, and is presently working on a number of new fund launches, including UCits, with clients from the UK, North America, Switzerland and the Middle East. The company is also assisting a number of fund managers with the redomiciliation of funds from the Caribbean islands to Malta.

A recent development has been a number of requests from fund managers with offshore funds, to move the fund servicing of these funds to Malta from a number of different Caribbean islands, very often at a saving to the fund.

Whatever the future may hold for the hedge fund industry, Malta's fund administrators are confident they are well placed to increase their own market share. Although smaller funds may have fuelled the early stage of Malta's development – and may continue to do so for the foreseeable future – the jurisdiction is also beginning to attract mid-sized hedge funds. This in turn should help increase the visibility of the jurisdiction and, eventually, also help boost assets under administration.

For 2012 administrators are keeping one eye on the global economic environment but betting that Malta continues to ride out the financial crisis in relatively good shape. That in turn should give the administration business confidence of continuing growth.

Brendan Conlon, business development director at SGGG Fexo Fund Services (Malta), has also seen a lot of new start-ups and thinks that is likely to continue. However, he agrees some of the bigger named funds are giving Malta more than just a glance. Fund managers and fund management companies are attracted by low corporate tax. “There’s a lot of tax structuring going on in Malta. I think it will be very positive,” he predicts.

Like TMF, Conlon is concerned that the MFSA keeps its edge, particularly as other jurisdictions like Ireland and Luxembourg feel the strain of numbers. He notes the MFSA is not quite as quick in approving funds as it was but it is not slow. “There was a lot of work this year to get a lot of people in the door trained and qualified.”

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Malta still finds a lack of choice of custodian a drawback in its plans to develop as a major fund domicile in Europe.

More competition needed

The Maltese regulator is actively encouraging more custodians to set up in the jurisdiction. The Malta Financial Services Authority (MFSA) believes not only is there a market for Malta-based UCits products but believes the alternative investment fund managers (AIFM) directive will drive demand. HSBC and Deutsche Bank are the main global custodians, while Austrian bank Sparkasse tends to concentrate on the smaller end of the scale. Bank of Valletta is in partnership with JP Morgan and acts as a sub-custodian for the bank.

For Joseph Bannister, chairman and president of the MFSA, the need is simple. When Malta first began developing its fund sector, it was more focused on developing other local services. Now with the popularity of UCits wrappers for hedge funds as well as the requirement within the AIFM directive for a local custodian, Malta appears to be playing catch-up to the other major European fund jurisdictions.

He predicts that over the coming few years, Malta will see a gradual increase in the volume of custodial business. “Most custodians tend to work on volume and I think they will find the volume attractive for them to establish here. Some take the plunge and they say: ‘Well, here is a jurisdiction which is developing and we need to be here.’ That’s one of the reasons why Deutsche Bank came and it’s now developing its scale prime brokerage;”

“Malta is developing through the legislation and regulation procedures.”

Concerns about delays
Sparkasse’s Paul Mifsud is concerned about any attempt by the MFSA to delay implementation of the custodial parts of the AIFM directive. He says it is likely that hedge funds in particular will wait until the last minute to decide about choosing a custodian under the directive. If Malta delays for any reason, it could seriously harm its ability to attract business to the island.

Despite these concerns Mifsud is positive about the legislation as it affects custodians. “I still believe Malta is a very good base for having your fund. We have the infrastructure. As long as the investment manager is willing to move down and operate here or through a UCits fund structure remain in his country of origin and passport his services, Malta should continue to develop. I see it developing primarily through these benefits: through the legislation and regulation procedures.”

At Bank of Valletta, head of custody operations Lino Calleja is relatively optimistic about prospects. JP Morgan has granted the bank a full custody licence and, says Calleja, “they’re still not very active in the market as yet”. He does not think there is the critical mass in Malta to lure the big international custodians. “It’s always the same thing. Which is first: the chicken or the egg. Who’s going to come first?”

The big player at present on the market is HSBC. Although Deutsche Bank has committed to the jurisdiction with a small office, HSBC dwarfs it as well as the other local competition.

“HSBC’s response to the challenge and opportunity offered by increased custodial work coming to Malta has undertaken a significant reorganisation, including technology improvements aimed at ensuring the local facilities are linked into the global network of HSBC. The local operation has had a 34% growth in its funds business in 2011. At the same time the bank has upgraded its transfer agency platform, establishing a new team known as the trustee, depository and fiduciary unit. This links into HSBC’s ‘centre of excellence’ in Edinburgh, which covers its entire fund services across Europe.

HSBC is trying to strike a balance between substance with actual presence on the ground in Malta and its connection to the international network. The bank has its eye not only on expanding fund services and custody but also prime services. While it is unlikely that full-scale prime brokerage would be offered from Malta in the short term, it is clear the bank is looking at how to accommodate and service the growing investment community in Malta.

So far demand for this service is limited. The hope is that as the jurisdiction grows and when the AIFM directive comes into force, demand will grow. Being the first on the ground to offer the service, believes HSBC, will give the bank first-mover advantage.

Whatever the future of Malta’s custody service, however, it is clear the driving force behind the growing popularity of the jurisdiction is its good reputation as a domicile concerned with sound regulation but with a regulator that is approachable as well as fast to react. The increasing amount of regulation for Europe’s alternative fund managers should continue to boost the jurisdiction. When and how many international banks and custodians will find it useful to establish a presence in the jurisdiction in the interim, however, remains an open question.
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REVIEW

the voice of the alternative investment industry.
As Malta’s funds sector and financial services industry grows, accountancy firms are finding it difficult to find staff and are using global networks for expertise and experience.

Strong growth continues

“Growth generally within financial services is still strong,” comments a pleased Joseph Camilleri, a partner and asset management leader at PricewaterhouseCoopers (PwC). He confirms the funds team, which also includes assurance, tax and advisory, is growing.

Like the other Big Four accountants, PwC is seeing growth across the alternatives, which includes hedge funds, private equity funds and others, such as real estate funds. “The challenge that companies like us face is that in the alternative sector, say, with private equity, there’s a lot of tax involvement in terms of tax restructuring, using Malta as a fund domicile. In other areas where you have sophisticated valuations or methodologies, the advisory department gets involved. Our team is growing larger. We’re still recruiting heavily and training,” says Camilleri.

For all the accountancy firms training is a priority. PwC says in 2011 it sent 25 of its Malta staff to the US, with over half of them working in the alternative funds team in New York. “They came back with loads of experience,” Camilleri admits this expertise may not be needed just yet, as Malta is far from reaching the sophistication of the US and UK fund management scene. Nevertheless, across the board firms are looking to bring in experts, training staff and preparing for what all believe will be an increasingly complex and expanding funds sector.

Ronald Attard, partner in transaction advisory services at Ernst & Young, agrees. Numbers at his firm have been growing as a reflection of more funds being registered in Malta and more managers locating in the jurisdiction. He says the firm is “experiencing challenges with recruitment”. Although the majority of people at the firm are still Maltese there is a good representation from Ireland, the UK, Eastern Europe and the Far East. “We’re seeing huge mobility coming into our industry. I think it’s healthy, and I think it will become more multi-cultural and more multi-country,” he says.

All of the Big Four use Malta’s university as a hunting ground for new recruits. “We are investing heavily in trying to recruit the best people from universities at an early stage,” says Attard.

At Deloitte, partner Stephen Paris says the story is similar. “I think the knowledge pool isn’t coping with the demand,” he says. It is not only accountants within financial services but also other areas of financial services. “The department has I’d say probably 10 different nationalities. There are some with financial service industry experience who’ve come from Cayman or wherever. But it’s to serve the general shortcoming.”

He believes Malta has no shortfall of talent but lacks experience. As growth has been steady and controlled, the industry has not been overwhelmed.

Momentum in 2011

“This year has been a continuation of 2010 in that the interest and momentum, as expected, has continued at a more accelerated rate.”

Stephen Paris

“This is an area where we’re seeing increased interest and I think the UCITS market is the most difficult one for Malta to penetrate,” he says. With Luxembourg established as the main centre, he believes it will be tough for Malta to be considered but has high hopes.

PwC’s Camilleri confirms that most growth in the funds sector comes from the professional investor funds (PIFs) rather than UCITS and predicts this will continue, although both types will increase in numbers.

With the introduction of the alternative investment fund managers (AIFM) directive, Camilleri thinks UCITS may revert back to being a purely retail structure and hedge funds will lose interest in the wrapper. He sees AIFM giving much more flexibility to hedge funds than through a UCITS structure.

“I still think we’re attracting a lot of the start-up businesses,” he confirms, but believes prime brokers and others, especially in London, are advising clients to look at Malta. “A lot of prime brokers are keen in this sector. They help clients come up with innovative structures and products. They are advising clients to look at Malta, at least as an alternative jurisdiction. So I still think we have a niche area with respect to the alternative sector and start-ups.”

For 2012 and beyond few see any reason for a slowdown in the growth picture. Camilleri says one of the new elements has been a widening and deepening of the financial services sector overall. “There’s also been growth in the investment services licences provided to service the fund growth. We’ve had fund growth. Now, because of the number of funds being registered in Malta, you’d expect that the service providers would have increased as well. In 2011 this has started to increase."

He is confident of further expansion. “I think it will continue growing. I think Malta before was being seen as an alternative jurisdiction. But now it’s probably being seen as another jurisdiction, not necessarily as an alternative. In the sense that we’ve moved on from there. It is a financial services location where we have banks, captive insurance companies, insurance brokers, funds and their administrators and their managers.”
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**MALTA: WHAT THEY SAY**

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### What they say about Malta

**Chris Bond, head of global banking and markets, HSBC Bank Malta**

As Malta's financial services sector widens and deepens, Bond believes the “trend is your friend”. He expects the majority of funds domiciled in Malta to continue to be professional investor funds (PIMs) as well as more UCits products. “The reason for that is that I think the UCits brand is becoming better and better recognised throughout the world.” Although Luxembourg has the lion's share of UCits business, he believes cost and capacity constraints will mean that Malta will be able to attract more business. “This leaves Malta with an important role to play – not just looking at the tiniest of funds. We work very closely with our Luxembourg colleagues and I think the bar for minimum criteria, net asset value and size of fund is getting higher and higher. From my point of view, I don’t want to focus solely on the small funds and the very small start-ups. I think Malta’s growth will come from attracting some of the larger funds. That’s where our recognition will come from which will then stimulate further growth. Given that Luxembourg is setting the bar very high now, it gives Malta an important space to play in.” While realistically he does not think Malta is a direct competitor to Luxembourg for the very large branded funds, he does see a rosy future for the island in developing this business.

For Bond, the attractions of Malta come from a combination of things. “I don’t think we focus enough on some of the softer credentials we have here. The quality of life, not just for busy executives but also for their whole families, is really important,” he says, adding that Malta is also pragmatic and realistic about its prospects. “We keep our feet on the ground, recognising the small size of our economy and our fund industry but being involved in a growth story is very, very exciting.”

**Joseph Camilleri, partner, PricewaterhouseCoopers**

Malta has wanted to develop its financial services sector for many years, says Camilleri. He reflects that the government decided “many, many years ago” to move away from manufacturing, high labour-intensive industries. “We have the right attributes: the English language, a high level of professionalism in terms of lawyers, accountants, bankers; part of the Commonwealth; business mentality.” He points to the fact Malta’s Companies Act dates back to 1967. “We have mandated audits for a very long time. We introduced, for example, IFRSs, which are accounting standards, 10 years before the rest of Europe. They were enacted in 1995 in Malta, one year after the financial services legislation.”

He believes Malta’s membership of the European Union (EU) has been a catalyst for growth and change. In addition, the financial services crisis has also helped Malta accelerate in terms of clients looking to locate funds in a more transparent jurisdiction but within the EU. “The fact is that a lot of the service providers in Malta were really knowledgeable about this particular sector, so we’ve had fund managers and fund administrators that have been set up in Malta since 1994 and 1995.”

For him, Malta was in the right place at the right time to take advantage of the turmoil in the financial sector because there was no doubt there was a seismic shift in terms of fund locations, when the alternative investment fund managers (AIFM) directive was being introduced and Malta was, therefore, seen as an alternative jurisdiction.

Because the whole infrastructure needed for the development of the fund industry was in place well before the financial crisis, Malta was positioned for growth.

“There’s no short-term view in this. Malta takes, I think, a long-term view in this sector and this is why I think [Malta’s] careful with the sort of clients that it wants to be associated with. Financial services, in its broadest sense, not funds, is key. I think, to Malta’s development.”

**Patrick Mangion, senior manager, financial services industry, Deloitte Audit**

“Whichever sphere you look at you look at, we are in a situation where we have started off with various service providers – with the administrators we just had a couple and we now have about over 22. If you look at the custodians, we just had one. If you look at the lawyers, we just had one or two law firms, which were interested in [the fund industry]. Now we have all the major law firms in Malta interested in the industry. We’re also hearing that there’s some international names which might be joining the market,” says Mangion. “Wherever you look, even at the Big Four, before we had the presence here but now we’re seeing specialisation in financial services.”

Mangion believes Malta’s financial services sector is continuing to expand and the fund industry is part of the development impetus. “I think everybody’s aware of the interesting opportunities,” he notes. “If you look at our associations, you’ve got Malta Finance which has been formed, you’ve got the Institute of Financial Services Practitioners, which has specialised committees which are tackling financial services issues. We have people and committees in the industry, which are meeting with government. We’ve got bigger names coming here that will create a certain amount of awareness.”

**Anthony O’Driscoll, managing director, Apex Fund Services**

Only a short time ago Malta’s authorities were worried there were not enough service providers based in
the country to help service what they hoped was a growing fund industry. Apex took an early decision to open an office in Malta and this foresight has been rewarded. Now O’Driscoll says there are a sufficient number of fund administrators in Malta.

“There’s always room for more to come but I think the key to continuing the success in Malta is looking at where those weaknesses, and definitely we need more competition and possibly [office] space.”

He believes Malta still offers a cost advantage both to service providers and to the industry in general. “Of course it’s eroding but I think it will remain for a number of years to come yet.”

He points to the fact that a start-up fund can not only launch quickly in Malta but is looking at a relatively low price tag. “The minimums are around €75,000 for a qualifying investor fund, which is a good subscription minimum,” he notes. “There’s no requirements for local custodians. [Malta] gives flexibility in the model.”

He continues: “I think Malta will always stand on its own. It has a place in the market. The challenge for Malta is to build its reputation from a service point of view, being capable to increase its brand name and visibility. They are the challenges while holding our cost advantage. I think there’s a place for Malta on the market. At the moment it is doing all the right things: attracting the management companies and the managers.”

Kenneth Farrugia, general manager, Valletta Fund Services and chairman of FinanceMalta

“More fund managers will be interested in the Malta proposition and they will come here,” says a confident Farrugia. “You look at some of the names that have come to Malta, and maybe wearing my Finance Malta hat, I think today Malta can really carry the stamp that it’s a tried and tested jurisdiction.”

He points to the variety of funds, including UCits products, setting up in the jurisdiction. There is a “significant variety of hedge funds” he notes as well as a number of private equity and other specialist funds. “I think that’s testimony to an industry which has developed a cluster to start with. Because you get clusters on the asset management administration and fund side in an industry that’s constantly growing. Despite the constant vacillations of the market, the industry has continued to grow very, very strongly.”

Farrugia continues: “I think clients are very surprised when they come here, when they meet up with the regulator, when they meet up with the various practitioners and the service providers, to find the calibre of employees and skills depth present in Malta.”

Although Malta is the smallest member of the EU, Farrugia says the country is ranked first by the union for its efficiency of transposing directives directly into law. “I think maintaining that efficiency is critical.” He also thinks the Malta Financial Services Authority (MFSA) is doing “an excellent job”. “They’re growing and they’re adapting themselves as well. Recently, they’ve set up and split the divisions in terms of the authorisations unit and the supervisory unit. They’re evolving with the way that the industry’s shaping itself and looking as well to what’s happening outside our shores. That’s the first critical success factor: our legal regulatory framework and the efficiency of the regulator as well.”

When Farrugia speaks of the MFSA, he also emphasises its responsiveness and accessibility. “This is a two-pronged approach. On the one hand the fact that the regulator has maintained the regulatory framework at par with the key developments taking place in Europe and at the same time been innovative, with the introduction of assurance, the protected cell company [PCC] legislation for example, which is a first for Europe.”

Nick Mahy, managing director, Praxis Fund Services (Malta)

For Mahy, Malta may still be an emerging jurisdiction but it is also now established itself as a credible hedge fund jurisdiction. “It’s making good noises for itself,” he says. He believes that one of the unique characteristics of Malta is its straightforward and direct networking. Compared with other jurisdictions, where business usually comes through an intermediary, clients are coming directly to him. “It’s a one-to-one relationship, which I find is quite interesting from a business perspective and a marketing perspective especially.”

Like Farrugia, he thinks Malta’s legislation and regulations are attractive as well as the country’s EU membership.

The filtering system for start up funds begins with the simple question of which jurisdiction to select. “I think you could say that FinanceMalta has done a pretty good job on getting Malta’s name out and about, in the general and internationally.”

Brendan Conlon, business development director, SGG Fexco Fund Services (Malta)

Conlon sees a positive future for Malta as a hedge fund jurisdiction and overall for the expansion of financial services. He believes many are looking at the jurisdiction as a cost-effective alternative to Ireland. The accessibility of the MFSA is, he thinks, another advantage as regulators in the other EU jurisdictions tend to be harder to see or distracted by other concerns.

Although the regulator was under considerably more pressure in 2010, it is now fully staff and prepared for expansion in the funds sector. Although approvals slowed and were not as quick as usual, the MFSA quickly addressed the problem and is now prepared for growth. He says the MFSA response times are still excellent compared with other jurisdictions, and that the regulator is proactively finding and training qualified staff in preparation for further expansion of the fund sector.

One concern he points to is rising legal fees. Although overall these are still competitive, he believes Malta’s legal services need to be aware that there is a danger to the sector if their fees continue to rise.
Gross domestic product
Gross domestic product (GDP) in real terms between 2009 and 2010 expanded by 3.2%. In nominal terms GDP grew by 6.2%. Within the European Union (EU) 27, GDP in 2010 expanded by 1.8% in real terms and 4.2% in nominal terms. GDP per capita for Malta in nominal terms for 2010 stood at €14,982 as against €14,181 in 2009. Within the EU 27, GDP per capita stood at €24,500 in 2010 as against €23,500 in 2009.

Gross value added – 2009 compared with 2010
Total gross value added (GVA) increased 6.7% between 2009 and 2010. The financial intermediation sector contributed 5.5% to total GVA in 2009 and 7.5% to total GVA in 2010. Between 2009 and 2010, GVA for financial intermediation grew by 45%, to €402 million in 2010.

When reviewing data for the first quarter of the year, total GVA increased by 6.2% between 2009 and 2010, and 5.7% between 2010 and 2011. Through the same quarter, GVA for financial intermediation grew by €45 million between 2009 and 2010, and increased by €2,000 between 2010 and 2011, reaching €98 million in Q1 2011. Financial intermediation contribution to total GVA during Q1 2009 stood at 4%; 8% in 2010 and 7% in 2011.

Employment
The total employment rate reached 56% in 2010, an increase of 2% between 2009 and 2010. Within the EU 27 the total employment rate stood at 64.6% in 2009 and 64.2% in 2010. Full-time employment within Malta’s financial services sector in January 2011 totalled 6,323, representing a 0.4% increase from the previous year. Employment within the financial services sector reflects 4% of total employment in Malta.

Hourly labour costs in Malta increased 0.3% between fourth quarter of 2009 and 2010 and increased by 2% within the same period in the EU 27. Consequently, between first quarter of 2010 and 2011, hourly labour costs in Malta increased by 2.4% and by 2.7% within the EU 27.

Inflation
Inflation, based on the harmonised index of consumer prices (HICP), was volatile over the last two years. During 2009 inflation rate fell drastically consequently turning negative for the first time since the introduction of the euro in 2008. Inflation rates stood at 3.1% in January and fell to minus 0.4% in December. The inflation rate picked up during 2010 mainly due to higher energy prices closing the year at 4%.

The annual average inflation rate for 2009 stood at 1.8% and 2% in 2010. In comparison with the euro area (EA17), the annual average inflation rate stood at 0.3% in 2009 and 1.6% in 2010. Malta’s inflation rate during the first and second quarter of 2011 took a downward trend. In the beginning of the year, the inflation rate stood at 3.3%, 2.1 percentage points higher than in January 2010. During 2011 the inflation rate fell 1.1 percentage points with inflation reaching 2.2% in July.

The annual average inflation rate within EA17 stands at around 2.7%.
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