International
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Legal Guides

Public Investment Funds 2020

A practical cross-border insight into public investment funds

Third Edition

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1 Registration

1.1 Are funds that are offered to the public required to be registered under the securities laws of your jurisdiction? If so, what are the factors and criteria that determine whether a fund is required to be registered?

Undertakings for collective investment in transferable securities ("UCITS") are the most common category of Irish fund that are offered to the public. UCITS are EU-based regulated investment funds that are available for public participation. For an Irish UCITS to be offered to the public it must firstly be authorised by Ireland's regulatory authority, the Central Bank of Ireland (the "CBI"). Once a UCITS has been authorised by the CBI it is automatically registered in Ireland and can be marketed to the Irish public.

In order for the UCITS to be marketed in other jurisdictions, such as Member States of the EU ("Member States"), it must submit a passporting notification to the CBI in respect of the relevant Member State with supporting documentation including, *inter alia*, the relevant key investor documents ("KIIDs"), annual financial statements and the formal passporting notification. Once the passporting notification has been reviewed and there are no comments from the CBI or the local regulator of the EU Member State(s) that the UCITS is proposed to be marketed in, the UCITS fund can be offered in that EU Member State(s). UCITS funds benefit from this passporting notification process for EU Member States on the basis of the marketing passport under the UCITS Directive which allows UCITS authorised in one EU Member State to be sold cross-border in another EU Member State without any additional authorisation processes to be completed.

There is another type of retail fund that may be offered to the public and registered in Ireland known as a retail investor alternative investment fund ("RIAIF") which is a sub-category of alternative investment fund ("AIF"). In essence, an AIF is any fund that is not a UCITS. However, as RIAIFs are not as commonly authorised or widely marketed as UCITS, the focus of this section is on UCITS.

1.2 What does the fund registration process involve, e.g., what documents are required to be filed?

The CBI has a prescribed authorisation process that all UCITS applicants must comply with. As part of the UCITS authorisation process, there are a number of documents that are required to be filed with the CBI either for review or as confirmation of the UCITS' compliance with applicable regulatory requirements.

The central document in the application is the prospectus. This document is submitted for prior review and comment by the CBI. Any comments raised during the application must be addressed to the CBI's satisfaction before the UCITS can be authorised. In addition, should the UCITS propose to invest in certain asset types or instruments such as contracts for difference, binary options or contingent convertible bonds, then the CBI will require supplementary materials to be provided as part of the application, such as model portfolio information, due diligence on the underlying portfolio and evidence to support the view that the proposed investment portfolio is suitable, taking into account the CBI's requirements. The review process with the CBI, once the documents have been drafted, can take two to four months depending on the complexity of the strategy of the proposed UCITS.

As part of the authorisation process, there are other documents that are submitted to the CBI in a final executed format. Such documents are not subject to prior review and include, *inter alia*, the management agreement (where a management company is appointed), depositary agreement, investment management agreement, administration and distribution agreements, KIIDs, risk management process (where the UCITS proposes to use financial derivative instruments ("FDIs")) and various confirmations that the relevant documentation meets the CBI's requirements.

As mentioned above, a management agreement may be put in place where a management company is appointed to a UCITS. It is not a requirement for a UCITS to appoint a management company in Ireland. Where a UCITS does not appoint a management company it is referred to as a self-managed investment company ("SMICs"). Where a UCITS is a SMIC, it is required to prepare a detailed corporate governance and oversight document known as a business plan that is filed with the CBI for prior review and commentary before the UCITS is authorised. In light of the additional corporate governance, oversight and time commitment obligations that the CBI imposes on UCITS, for new UCITS, the externally managed model has become a predominant model within the industry in Ireland as it allows the UCITS to relinquish compliance with many of these requirements and have them sit with the Management Company.

1.3 What are the consequences for failing to register a fund that is required to be registered in your jurisdiction?

If a fund is not registered as a UCITS it cannot hold itself out as this type of regulated entity. From a commercial perspective the fund then does not benefit from the UCITS marketing passport and will not be able to avail of the global recognition that UCITS funds enjoy as the gold standard investment fund within the EU financial services community. If a fund holds itself out as a UCITS and it is not authorised as such, then a number of authorities, in particular the CBI, have a range of prohibitory powers such as enforcement, sanctions and fines that can be applied to the fund.

1.4 Are there local residency or other local qualification requirements that a fund must meet in order to register in your jurisdiction? Or are foreign funds permitted to register in your jurisdiction?

As mentioned in question 1.2 above, Irish domiciled UCITS must go through an authorisation process with the CBI. For UCITS domiciled in other EU Member States, as set out in question 1.1 above, these UCITS must make a passporting notification to their home state regulator who liaises with the CBI. Once there are no outstanding comments from the relevant regulatory authorities, the UCITS can be offered to the public in Ireland.

2 Regulatory Framework

2.1 What are the main regulatory restrictions and requirements that a public fund must comply with in the following areas, if any? Are there other main areas of regulation that are imposed on public funds?

i. Governance

UCITS that are legally structured as ICAVs or Plcs are required to have a board of directors with at least three directors, two of which must be Irish resident directors. There is a voluntary Irish corporate governance code (the "Code") which is an industry rather than a regulatory obligation, but the vast majority of UCITS adopt the Code on a comply or explain basis with any instances of partial or non-compliance disclosed in their financial statements. The Code sets out recommendations on board composition including, *inter alia*, that boards comprise a majority of non-executive directors, at least one independent director who would not be an employee, partner, significant shareholder or director of a service provider to the UCITS and that at least one director be an employee, partner or director of the UCITS' investment manager or management company.

Further, the CBI requires for UCITS SMICs that: (i) two directors are resident in Ireland; (ii) half of the UCITS SMIC's directors are resident in the EEA or such other country as determined by the CBI; and (iii) half of the UCITS SMIC's managerial functions are performed by at least two designated persons resident in the EEA or such other country as determined by the CBI. As set out in question 1.2 above, UCITS SMICs are required to prepare and maintain a detailed business plan. The business plan will indicate designated persons, either directors and/or external individuals responsible for six managerial functions that relate to regulatory compliance, fund and operational risk, financial management, distribution and investment management. These individuals, who are known as designated persons, along with the directors, are required to be fit and proper in the eyes of the CBI; i.e., they must be competent and capable, honest, ethical, act with integrity and they must be financially sound. The designated persons and the directors must also specify a minimum time commitment to the UCITS which indicates the minimum amount of time they require to carry out their roles, responsibilities, duties and obligations. The CBI requires that letters of engagement are to be put in place in respect of designated persons as well as directors of a UCITS.

ii. Selection of investment adviser, and review and approval of investment advisory agreement

In Ireland there are two categories of entities that can be involved in the portfolio management of a UCITS; namely, investment managers who have discretionary authority over the assets of the UCITS and investment advisers who do not have discretionary authority over the assets of the UCITS. For an entity to be appointed as an investment adviser to a UCITS, no prior engagement with the CBI is required, and an executed investment advisory agreement is submitted as part of the UCITS authorisation process along with a confirmation letter that the investment adviser will act in an advisory capacity only and will have no discretionary powers over any of the assets of the UCITS.

For an investment manager to be appointed to a UCITS, the CBI has a fast-track application process for EU-based investment managers whereby a simple notification is made to the CBI prior to the investment manager's appointment, setting out the name and registered address of the investment manager, details of the investment manager's regulatory status (typically relating to Directive 2009/65/EC as amended ("UCITS Directive"), Directive 2004/39/EC ("MiFID"), Directive 2014/65/EU ("MiFID") or Directive 2011/61/EU ("AIFMD")), its home state regulator and contact details of the relevant contact within the home state regulator.

Non-EU-based investment managers must go through a once-off full review process with the CBI prior to their appointment which involves a detailed application being made to the CBI with supporting documents evidencing expertise, integrity and adequacy of financial resources which will include background details and experience of senior staff, organisational structure of the investment manager to include details of shareholders, assets under management and latest audited financial statements. This process can take approximately one month but it will vary depending on the jurisdiction of the investment manager, as the CBI will also be seeking to ascertain if the investment manager is appropriately regulated in its home state and that the investment manager is from a jurisdiction that the CBI recognises as being equivalent from a prudential supervision perspective. Once this process is complete, the non-EU investment manager will be deemed cleared and can be appointed to any other UCITS or AIF and, provided it does not let the clearance lapse, need not go through the clearance process again. The CBI does not typically review investment management agreements.

iii. Capital structure

As set out above in question 1.2, a UCITS can be a SMIC or it can appoint a management company. UCITS that appoint a management company do not themselves have any capital requirements imposed on them. In such instances, the capital requirements are imposed on the UCITS' management company. However, a UCITS that is a SMIC must retain a minimum capital amount of €300,000 in order to be authorised by the CBI. Typically, this €300,000 is usually provided by way of cash injection from the UCITS' promoter or sponsor and it must be evidenced in writing at the authorisation phase. However, once subscriptions have been received that exceed this minimum, the sponsor/promoter may withdraw its €300,000 it had initially provided and investor funds will meet the minimum capital amount.

iv. Limits on portfolio investments

UCITS can invest in a number of asset classes such as: transferable securities (including debt and equities) and money market instruments, units of UCITS and units of non-UCITS collective investment schemes, deposits with credit institutions and financial derivative instruments that meet certain criteria. However, there are a number of investment and borrowing restrictions placed on UCITS through the UCITS legislative framework with the primary focus of such restrictions relating to portfolio diversification and liquidity. A UCITS cannot invest in real estate nor can it invest directly in commodities (however, it can gain exposure to commodities indirectly through FDI or exchange traded notes).

v. Conflicts of interest

The CBI set out requirements for the management and disclosure of conflicts of interests which primarily involves disclosing in the prospectus how potential conflicts of interests between the UCITS and its service providers will be dealt with, e.g.: (i) transactions are executed on best terms on an organised investment exchange in accordance with the rules of such exchange; and (ii) a person approved by the depositary certifies the value of the transaction, or, where the transaction involves the depositary, a person approved by the UCITS, or its management company; or (iii) where (i) and (ii) are not possible where the depositary (or UCITS/management) is satisfied that the transaction is conducted at arm's length and is in the best interests of shareholders.

vi. Reporting and recordkeeping

UCITS have reporting and recordkeeping requirements as set out under the UCITS Directive and must have policies in place to ensure compliance with those requirements. However, there are additional periodic reporting requirements imposed by the CBI that relate to, for example, filing of returns in relation to annual and semi-annual financial statements, the fitness and probity of the directors of the UCITS, updating of the KIIDs and the profile of a sub-fund of the UCITS as at the financial year end.

vii. Other

There are listing requirements where a UCITS is listed on a stock exchange e.g. notices to shareholders, material changes to the prospectus, financial statements, etc. Further obligations may be imposed for UCITS that are structured as ETFs (as set out in question 2.5 below) and money market funds.

2.2 Are investment advisers that advise public funds required to be registered and/or regulated in your jurisdiction? If so, what does the registration process involve?

This is set out in question 2.1(ii) above.

2.3 In addition to the requirements above, are there additional regulatory restrictions and requirements imposed on investment advisers that advise public funds?

The primary requirements are set out above in question 2.1(ii), however, once an investment manager is cleared to act for a UCITS, it should inform the CBI in advance of any upcoming changes to its regulatory status, name or registered address.

2.4 Are there any requirements or restrictions in your jurisdiction for public funds investing in digital currencies?

As set out in question 2.1 (iv) above, there are a number of eligible asset classes that a UCITS can invest in. Currently, digital currencies are not a permissible asset class that a UCITS can directly invest in. However, a UCITS may be able to get indirect exposure to digital currencies through, for example, financial indices or the equities of related companies.

2.5 Are there additional requirements in your jurisdiction for exchange-traded funds?

The CBI requires UCITS structured as exchange-traded funds ("ETFs") to include in its name "UCITS ETF". UCITS that are ETFs generally function as index tracking funds and as a result are subject to additional CBI disclosure requirements in the prospectus such as descriptions of the relevant index being tracked, how it will be tracked, the tracking error, factors that affect the ability of the UCITS to track the index, leverage at the level of the index, etc. Where a UCITS ETF is actively managed, it must make clear that the UCITS does not track an index and that it is actively managed by the investment manager. ETF UCITS are required to be listed on an exchange and, as a result, are required to comply with the relevant listing obligations. In order for investors to deal in the UCITS ETF, one or more market makers will be appointed by a UCITS ETF to: (i) subscribe for and redeem UCITS ETF shares directly from the UCITS ETF but usually only in large blocks called creation units; and (ii) make a market in the UCITS ETF shares in the secondary market.

3 Marketing of Public Funds

3.1 What regulatory frameworks apply to the marketing of public funds?

Marketing of a UCITS throughout the EU is primarily governed by the UCITS Directive. However, if a UCITS is marketed by a distributor that is subject to MiFID then the UCITS may be indirectly impacted by certain aspects of MiFID by virtue of that appointment. Marketing of the UCITS outside of the EU will be subject to the requirements of the relevant jurisdiction in which the UCITS is being marketed as well as the rules to which the distributor is subject.

3.2 Is licensure with a regulatory authority required of persons (whether entities or natural persons) engaged in marketing activities? If so: (i) are there commonly available exceptions that may be relied on?; and (ii) describe the level of substantive regulation applied to licensed persons.

Entities that propose to market a UCITS within the EU must be authorised under an appropriate regulatory regime, such as the UCITS Directive, AIFMD, or MiFID. Non-EU distributors or local distributors in non-EU jurisdictions must be authorised to sell the UCITS in the relevant jurisdiction. In all cases, the relevant UCITS itself must also comply with the applicable local requirements.

3.3 What are the main regulatory restrictions and requirements in the following areas, if any, that must be complied with by entities that are involved in marketing public funds?

i. Distribution fees or other charges

Where fees or other charges of entities responsible for distribution are payable out of the assets of the UCITS, this is required to be disclosed in the prospectus. As a result, the main requirement centres around prospectus disclosure. The disclosure will cover the maximum fee payable to the distributor or in the case of a sub-distributor, confirmation that the fees and expenses are at normal commercial rates. Distributors governed by, for example, MiFID, are not permitted in certain circumstances to accept fees, commissions or any monetary or non-monetary benefits. As a result, these distributors may require the share classes they are marketing to be in compliance with this prohibition on inducements under MiFID and these are commonly known as "clean share classes". In this regard, some prospectuses will disclose which share classes are suitable for MiFID distributors and disclosure regarding MiFID compliance will typically be included. As set out in question 3.1 above, this is not a direct requirement on the UCITS, but rather the indirect effect of appointing a MiFID distributor.

ii. Advertising

The CBI requires UCITS to comply with its applicable statutory advertising standards. The overarching principle of these requirements is that the design and presentation of an advertisement must be clear, fair, accurate and not misleading. Notwithstanding that a UCITS may be marketed solely to institutional investors, the CBI views UCITS as a retail product and, as such, advertisements must be consistent with the offering documents and pitched at such a level that the marketing material can be understood easily and clearly by a retail investor.

iii. Investor suitability

The CBI requires a UCITS to identify and disclose the profile of the typical investor for whom the UCITS is designed. Distributors such as those authorised under MIFID may be subject to their own obligation regarding target market assessment.

iv. Custody of investor funds or securities

All Irish regulated collective investment schemes, including a UCITS, must appoint an independent depositary located in Ireland. The majority of the duties and responsibilities of the depositary are prescribed directly by the UCITS Directive including the rules for delegation of safe-keeping and the standard of liability to which the depositary is subject. As part of its duties, the depositary monitors all cash flows, provides reconciliations and verifications, due diligence and risk assessments, segregation arrangements, sub-custody oversight and reporting of breaches to the CBI.

3.4 Are there restrictions on to whom public funds may be marketed or sold?

As set out in question 3.3 (iii) above, a UCITS at its core is a collective investment scheme that can be offered to retail investors. Notwithstanding this, there is no restriction on who can invest in a UCITS. However, the entity who is supporting the establishment of the UCITS, commonly known as the "promoter" may seek to self-impose restrictions on who can invest in the UCITS and thus who the UCITS can be marketed to. These self-imposed restrictions can relate to minimum subscription amounts and minimum holding amounts. The higher these thresholds are set, the more likely that the promoter is seeking to target institutional investors. Please see the response to question 1.1 above in respect of the notification process to market a UCITS. Each share class of a UCITS must be available for public participation. While a UCITS might establish a share class which restricts investment to a specific group of potential investors, any restriction must not be so narrow that the share class does not provide for public participation.

Where a UCITS offers a share class which is not open to the public or a sector sufficiently broad enough to constitute the public, it is not complying with the sole object requirement in Regulation 4(3) of the UCITS Regulations.

If a UCITS seeks to establish share classes with a restriction on participation, the CBI will require a confirmation that, notwithstanding the proposed restriction, the share class provides for public participation. This applies to each share class and, in the context of an umbrella UCITS, to each share class within each sub-fund.

3.5 Are there other main areas of regulation that are imposed with respect to the marketing of public funds?

No, the responses above cover the main areas that relate to the marketing of a UCITS in Ireland.

4 Tax Treatment

4.1 What are the types of entities that can be public funds in your jurisdiction?

The types of entities that can be public funds (i.e. UCITS funds) are: Irish collective asset-management vehicles ("ICAVs"); public limited companies ("Plcs")/variable capital companies; trusts; and common contractual funds ("CCFs").

4.2 What is the tax treatment of each such entity (both entity-level tax and taxation of investors in respect of allocations of income or distributions, as the case may be)?

Assuming an Irish UCITS (other than a CCF) is Irish tax resident, then it will be exempt from Irish tax on its income and gains, except for certain limited cases where the UCITS (known under Irish tax law as an IREF) holds Irish real estate assets or certain assets deriving their value or the greater part of their value from Irish real estate.

Investors (in an Irish UCITS which is not an IREF and not a CCF) who are not tax resident (or ordinarily resident) in Ireland, will not be subject to Irish withholding tax in respect of a "chargeable event" (which includes distributions, redemptions, disposals and a deemed chargeable event arising on the eighth anniversary of the relevant investment made by the investor) provided an appropriate declaration is completed by such investors. With respect to Irish resident investors, an Irish UCITS will be obliged to withhold Irish tax (at a rate of either 25% or 41%) on the happening of a chargeable event, although there are certain exceptions to that withholding tax requirement for pension schemes, charities, etc. and where the percentage (by value) of Irish resident investors is below 10% of the UCITS and an election is made.

CCFs are considered to be Irish tax transparent and therefore investors (both Irish residents and non-Irish residents) are taxed as if the income and gains of the CCF had arisen directly to them.

For non-Irish resident investors in a UCITS, certain exemptions from Irish gift and inheritance taxes apply.

No stamp duty is payable in Ireland on the issue, transfer, repurchase or redemption of an investor's interest in an Irish UCITS (although in certain cases stamp duty will apply for UCITS which are an IREF).

4.3 If a public fund, or a type of entity that may be a public fund, qualifies for a special tax regime, what are the requirements necessary to permit the entity to qualify for this special tax regime?

The UCITS (other than a CCF) must be regulated in Ireland and Irish tax resident. If a CCF, it must be Irish regulated.

Emmet Quish is a partner in the Financial Services Department and he is a specialist adviser to asset managers, investment funds, management companies and their service providers on a wide range of legal, regulatory and compliance matters. His expertise includes the structuring, establishment and operation of all types of investment funds, including UCITS and alternative investment funds. He also advises on the establishment and operation of UCITS management companies and alternative investment fund managers ("AIFMs").
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