

Changes to the Guernsey Class B Rules

Insights - 20/02/2014

As a result of the changes, Class B scheme service providers will need to take action. In particular, it should be noted that the transitional provisions require that:

- scheme particulars must be updated in compliance with the Class B Rules by no later than 1 January 2015; and
- principal documents will need to be reviewed and amended as necessary to comply with the Class B Rules by no later than 1 January 2016.

There are no specific transitional provisions to deal with differences under the new regime, for example, stating that the previous regime under the 1990 Rules in respect of particular matters will continue until such time as the fund documents are updated as described above. As a result, the new position in respect of double charging should be noted in particular (see further below) and further advice may need to be taken, as appropriate.

Further, in accordance with Class B FAQs published by the Guernsey Financial Services Commission (**the Commission**), any derogations granted under the 1990 Rules which continue to be required must be re-applied for by no later than 2 January 2015, otherwise they will lapse as from that date.

As a result of clarifications made in relation to service provider roles and duties under the Class B Rules (see below), service providers may also wish to carry out a review of the contractual arrangements under which they have been appointed.

The changes made to the Class B Rules include the following:

Applications

New classes and cells of a Class B authorised scheme will now be declared approved by the Commission and declarations of authorisation will now be issued. However, any such declaration will be subject to a time frame of one year. If the relevant new class is inactive after that time, the declaration is liable to be revoked.

As part of an application for a Class B declaration of authorisation, the required statement confirming compliance by the principal documents and scheme particulars with the contents of the Class B Rules may now be signed either by the manager or an approved law firm (previously it was just an approved law firm).

Regulatory approvals and notifications

It is still necessary to notify the Commission in advance of any proposed material alteration to a scheme's investment, borrowing and hedging powers. It is also necessary to give sufficient notice to investors to enable them to redeem their shares before the amendment takes effect. However, there is no longer any need to obtain prior written approval from the Commission for any such change. Further, the required certificate to confirm continued compliance of the principal documents or scheme particulars following such a change may now be issued either by the manager or an approved law firm.

There is also no longer any need to request prior approval from the Commission in respect of expenses, fees and charges to be paid out of scheme property when they are not already authorised for payment under the principal document or disclosed in the scheme particulars. That particular requirement has been replaced by a requirement to notify the trustee and to give notice to investors.

There is a new requirement which means that it is likely to be necessary to obtain the Commission's prior approval (and the approval of investors) in the case of a reconstruction which involves the transfer of property to or by an authorised scheme. This requirement may be dispensed with but only if the trustee or directors can be satisfied that the inclusion of the property concerned is not likely to result in material prejudice to interests of investors, is consistent with the scheme's objectives and may be effected without breach of the Class B Rules.

A proposed change of designated administrator or trustee continues to require prior notification and the Commission's prior approval in practice, because the Commission will need to formally vary the relevant Class B declaration of authorisation accordingly.

Other prior notifications required are in respect of any proposed change of principal manager or investment adviser.

There are also new immediate written notification requirements for changes of directors, the registrar, and the auditor and of a proposal to terminate a class or cell.

If dealings are suspended, there is now a specific requirement for the designated administrator to notify the Commission "forthwith", stating the reason for the suspension.

Service provider roles and duties

There is a new definition of "**designated administrator**". This is the designated manager for the purposes of the Protection of Investors (Bailiwick of Guernsey) Law, 1987 (as amended), that is, the person named as the designated manager in the relevant scheme's declaration of authorisation.

The definition of "principal manager" now makes it clear that this term in the Class B Rules refers to the Guernsey-based principal manager (if any), who would normally delegate some or all of its administration functions to the designated administrator.

The Class B Rules further clarify, including by way of added guidance, that the Commission normally expects the duties of a designated administrator to be limited to administering the scheme and monitoring the constituents of the scheme property. Responsibility for investment decisions is expected to be that of the principal manager (or, in the case of a company scheme, the company).

As regards the trustee, its principal duties remain those of safe custody of scheme property and oversight over the designated administrator and the principal manager (if any). Instead of the duty under the 1990 Rules to take all the scheme property "into its custody or under its control and hold it in trust", the trustee now has responsibility "for the safe custody of all the scheme property"; and it will be liable to the relevant authorised scheme "in the event that the loss of any scheme property occurs as a result of the trustee's unjustifiable failure to perform its obligations or its improper performance of them".

The Class B Rules now recognise that the function of registrar will often be carried out by a service provider other than the trustee, normally the designated manager. That appointment may now be made direct, subject to provision being made for the trustee's oversight role (whereas previously this was typically delegated out of the trustee).

Roles and responsibilities have been clarified in certain places throughout the Class B Rules for example in relation to preparation of scheme particulars (which the Commission now recognise would not normally be the responsibility of a trustee, except in the case of a unit trust, where there was no principal manager). Certain responsibilities which would previously have fallen to the "manager" (meaning either the designated manager or the principal manager or both) are now clarified, for example, as being those of a principal manager only (or, in the case of a company scheme, the company). By way of example, in the case of Rule 7.01(1), the reference to "manager"

has been replaced with "principal manager". This means that the designated administrator would not now have any entitlement under the Class B Rules to convene a meeting of holders.

In its guidance in Part 2 of the Class B Rules, the Commission notes that whoever is ultimately responsible will be a matter of contractual arrangement. The Commission further indicates that, in assessing compliance with the Class B Rules, it will take into account those contractual arrangements. If they have not already done so, service providers may wish to review those arrangements immediately and not wait until the principal documents and scheme particulars are to be updated under the transitional arrangements described above.

Fees and expenses, including double charging

Where a Class B scheme invests in other schemes managed by the same manager or investment adviser or persons in the same group, double charging of any charge payable by a target scheme is prohibited. The GFSC has now confirmed by means of its Class B FAQs that "any charge" in fact means management or investment advisory charges. This is still stricter than the position under the 1990 Rules, where double charging of the preliminary charge or any redemption charge was prohibited. However, double charging in feeder fund structures is not prohibited, provided that the relevant fee structure is fully disclosed.

As noted above, the requirement for the prior approval of the Commission for payment out of scheme property of previously unauthorised or undisclosed expenses, fees or charges, has been replaced with a requirement to notify the trustee and to give notice to investors.

There is also no longer any need for 90 days' notice to be given to investors of any increase in the manager's periodic charge. Instead, the Class B Rules provide that sufficient notice must be given such that an investor may redeem his shares prior to the increase coming into effect. Note, however, that there is now a requirement to disclose in the scheme particulars the amount of notice to be given to investors to increase the principal manager's and the investment adviser's charges.

Meetings of holders

The minimum period of notice fixed by the Class B Rules for a meeting of holders is reduced from 14 days to 10 days, subject to any longer period specified in the principal documents or by applicable law.

The provisions of the Companies (Guernsey) Law, 2008 relating to the deemed service of notices and documents will apply regardless of the constitution of the scheme in question. For some Class B schemes, this may extend the period that is normally allowed for deemed service and the position may need to be checked and advice taken, as appropriate.

In relation to the powers of a meeting of investors, a resolution for this purpose now requires only a simple majority of the holders or class of holders in order to be passed; an extraordinary resolution is no longer required.

Other changes

In addition to the changes set out above (and in no particular order):

- the Commission may object to undesirable or misleading names in relation to a scheme or class
- the conflicts of interest section has been expanded upon to set out the best execution, independent valuation or arm's length requirements to be applied
- the definition of "principal documents" in the case of a unit trust, now includes the management agreement (which is also likely to include the administration agreement)
- there is no longer a specific requirement to make available principal documents and scheme particulars at a stated address for inspection and they may also be made available on a relevant website
- there is no longer a specific requirement to issue certificates within 21 days
- there is no longer a requirement to file the interim report and accounts for a Class B Scheme with the Commission
- whilst minimum disclosure requirements for scheme particulars are reduced, there are several new requirements, including disclosure of accounting standards, directors' interests, material conflicts of interest, arrangements for the removal of service providers and the notice required to be given to increase principal manager or investment adviser charges
- in respect of directors, details of any other directorships that are held and have been held in the past five years are to be made available to any potential investor at the registered office of the authorised scheme
- there are new provisions to enable a sub-fund of an umbrella fund to be wound up

This note is a summary only. Specific legal advice should be sought in relation to any particular set of facts.

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