Changing global environment highlights Malta's appeal

By Simon Gray

One of the most striking developments in the European fund industry over the past five years has been the emergence of Malta as a credible and respected fund domicile and servicing centre. While the industry as a whole has been afflicted by liquidity issues, economic and market turbulence and investor skittishness, keeping both fund numbers and asset growth constrained, the Mediterranean island has steadily expanded its business volume along with its range of providers and skills.

Members of Malta's fund industry attribute its rapid development to a combination of factors – a low cost base compared with rival jurisdictions, an open-door attitude (plus tax incentives) encouraging firms to bring in highly-qualified expatriates to complement a well-educated and skilled local workforce, a regulatory approach that combines rigorous oversight with flexibility in legislative drafting and innovation in product design, and an entrepreneurial attitude that has helped Malta to seize opportunities even in a seemingly unfavourable economic environment.

The country's membership of the EU and of the eurozone has placed it at the heart of a vast and sophisticated market in financial services, yet it has been spared the financial turbulence of its southern European neighbours. Despite its mid-Mediterranean geographical location it enjoys plentiful and rapid air connections to other European centres. Its IT and telecommunications infrastructure has developed rapidly in recent years, and the Maltese people themselves have an outward-looking perspective characterised by their ease with languages.

The island's development as a financial services hub has started to become a self-sustaining process, with the broad network of law firms and fund administrators increasingly attracting fund business, asset management activities and complementary service providers. A good example is EXANTE, a brokerage with offices in St. Julians that sees growing opportunities in the burgeoning fund management sector.

"We chose Malta as the most suitable headquarters domicile for our business after a selection process that took us about a year," says managing partner Gatis Eglitis. "We evaluated more than 20 financial centres including London, Luxembourg, Zurich and Cyprus, but only Malta ticked all our check boxes. Today, now that we are fully operational, we are glad that this was our choice."

Eglitis says the firm's location in Malta enhances its competitiveness in various ways, including convenient transport connections to most destinations where customers are located. At the same time, labour costs, living expenses and operational overheads are favourable compared with other European countries.

The banking sector is solid and considered one of the safest within the euro zone, the regulatory environment meets all EU standards, and the country enjoys political consensus on the importance of providing an attractive environment for financial services. In addition, he says, Malta offers the continent's most competitive effective tax rate and most convenient financial business passport policy.

"Malta's benefits have attracted many other players, creating a rapidly growing financial centre and offering an unprecedented opportunity to a brokerage firm like ours," Eglitis says. "More than

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120 investment firms, 120 trusts and 70 fund managers have joined the financial community in just the past five years, and 24 per cent year-on-year growth in the number of established funds, which currently number more than 440, tells its own story."

He hopes that EXANTE's presence provides a further argument in Malta's favour for offshore funds and managers considering relocation. "We fill a gap in the country's investment community by offering a cutting-edge electronic platform for trading financial instruments," Eglitis says. "As an agency prime broker, we provide full global market coverage to enable futures, stocks, options, currencies, metals, fixed income and funds to be traded on a single account."

The firm's co-location infrastructure enables Malta-based funds to access global markets with state-of-the-art direct market access technology. Membership of the EXANTE Financial Marketplace allows clients to benefit from the firm's Infrastructure Sharing Programme and to list on exchanges, accessing a global institutional liquidity pool. Eglitis says: "As a one-stop shop prime broker, EXANTE is contributing significantly to Malta's financial services infrastructure and making the domicile more attractive. We are pleased to see this trend and be a part of it."

The influx of managers started in earnest three or four years ago, according to Dr Andre Zerafa, a partner with law firm Ganado & Associates. "There has been a significant influx of fund managers, some of them redomiciling from the Cayman Islands or other offshore centres, as well as firms starting afresh with a Maltese operation," he says. "The busiest year for setting up fund management companies was 2010, and while 2011 saw a slowdown, numbers picked up strongly again in 2012."

An important driver over the past couple

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Chris Bond, HSBC Bank Malta

of years has been uncertainty on the part of groups carrying out fund management from non-EU jurisdictions about the future impact of the union's Alternative Investment Fund Managers Directive, Zerafa says. But just as important are tax rules introduced in 2011 benefitting expatriates with in-demand skills that move to Malta for up to five years.

"The government has established a lower tax rate of 15 per cent for expatriates working in the financial sector, subject to a number of conditions," he says. "It basically covers income arising in Malta for expatriates occupying a position of seniority within a fund management or other financial services firm. That has not only encouraged expats to move to Malta with their families but has a positive effect on local employment in the sector, because typically the incomers will spend a couple of years or so building and training a team of local employees."

Chris Bond, head of global banking and markets at HSBC Bank Malta, says the range of specialist financial services providers establishing operations on the island extends well beyond the fund industry. He points to the fact that Malta is developing a strong reputation as a hub for insurance, with global corporates not only domiciling their captive insurance companies in the jurisdiction but putting people on the ground.

"Malta's protected cell company legislation offers a capital-efficient way of running an insurance business, especially in its early stages," Bond says. "Insurance managers follow the insurance companies, and we now have several of the global leaders in the sector including Aon, Willis and Marsh. That creates substance and critical mass on the island, making it even more attractive for new business."

He notes that other sub-sectors of the financial services industry are developing in Malta, including treasury centres and corporate pension schemes, and the banking sector has been boosted in recent years by the launch of several new institutions.

"More and more companies are being incentivised to put substance on the ground in Malta," Bond says. "In addition to being encouraged by the government and the Malta Financial Services Authority, the 15 per cent tax rate available to highly-qualified expatriates for a five-year period helps us to raise the bar in terms of specialist skills."

Bond sees the substance built up in Malta's financial industry as a critical factor distinguishing it from the offshore jurisdictions that have traditionally served the alternative fund industry. "This is not just a brass nameplate domicile but one that is attracting both service providers and fund managers themselves," he says. "As a banker, it is much easier to develop a relationship with people on the ground than with a legal entity managed by people on the other side of the world. This enables us to act as a trusted advisor and offer a full range of personal and corporate banking facilities.

"The presence in Malta of expatriate experts also underpins local recruitment and better training of local staff, which answers any questions about the breadth and depth of the skill set and the size of the local talent pool. As part of a global group, it is easy for HSBC Bank Malta to bring in talent from centres such as New York and London to fill key roles and help the development of our local resources."

The next target for the authorities is to boost the number of custodian banks offering services to Maltese-domiciled funds. Although HSBC is itself a leading global custodian, Bond says the bank is extremely keen to see other international players set up custody operations in Malta, which will make the jurisdiction more attractive when the AIFM Directive takes effect in July this year.

Alternative funds run by managers authorised under the directive must normally use a depositary – a bank in the case of assets that can be kept in custody – in the fund's domicile jurisdiction, although Malta can if it chooses obtain a derogation from this rule until 2017. However, there is confidence that more global custodian will soon set up operations on the island,

which will also increase its appeal for the establishment and servicing of UCITS funds.

Already the range of options for managers has been boosted by the presence of Mediterranean Bank, which was established in 2005 and acquired by UK private equity firm Anacap Financial Partners four years later. Today the bank's balance sheet has grown to USD1.5bn and it has positioned itself to serve managers of small and start-up funds that are seeking custody services tailored to their particular requirements.

"We're active in capital markets and support both retail and institutional clients looking to access these markets," says head of credit and investments Ximo Vincent. "We can leverage the infrastructure we have set up to benefit ourselves to offer it to smaller funds." Addressing the segregation of assets issues raised by the Lehman Brothers and MF Global bankruptcies, the firm offers non-commingled segregated accounts with Clearstream to clients with, in some cases, as little as EUR2m in assets under management.

Mediterranean Bank sees a gap in the market for provision of execution and other prime brokerage services in Malta as its fund management sector continues to grow. The AIFM Directive is bringing extensive change to the alternative fund industry, Vincent notes, placing new burdens on custodians and consigning to history much of the traditional prime brokerage model based on rehypothecation of clients assets.

"All these additional regulatory burdens will add costs to the service providers,

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Laragh Cassar, Camilleri Preziosi

so there is a need to re-think business models," he says. "That is our advantage in approaching this with a fresh perspective and no legacy issues."

Another recent arrival in Malta is Castlegate Fund Services, which set up an operation in the island in 2011 after an existing client of its British Virgin Islands office decided to restructure its offshore fund as a UCITS. According to general manager Roger Buckley, the firm provides administration services both to offshore-domiciled funds and Malta-based UCITS and Professional Investor Funds.

He notes that an important source of growth in Malta has been the revamp of Switzerland's Collective Investment Schemes Act, which imposes an extensive compliance burden on managers of non-Swiss funds that up to now have not been regulated. A significant number of Swiss managers have already begun moving operations to Malta or are considering doing so.

In addition, the AIFMD rules on marketing of alternative funds offer an incentive for managers based outside Europe to consider a domicile within the EU in order to gain immediate and guaranteed access to the directive's 'passport' for distribution to sophisticated investors throughout the 27-member union. Buckley emphasises the advantages offered by Malta both in its location and its suitability for managers starting out with resource constraints.

Pointing out that Castlegate recently appointed a business development officer in the Middle East, he adds: "Malta benefits from its proximity to the Middle East and North Africa, and has begun marketing itself as a centre for Shariah-compliant funds, a sector we are positioning ourselves to service in the future. It is a good fit for smaller managers; the regulator is very flexible and readily available to discuss a firm's proposed strategy or any other issue regarding establishing itself or a fund in Malta."

Laragh Cassar, a partner at law firm Camilleri Preziosi, says a combination of factors make the jurisdiction a competitive option for establishment of a fund management company. "Malta is very well placed to attract these firms, including the regulatory side and structuring options," she says. "There is also an advantage because of the way the double taxation treaties concluded by Malta work, as well as the country's tax system as a whole. All these factors make it attractive for managers to move their business here."

Joseph Ghio, a partner with Fenech & Fenech Advocates, one of the oldest and largest law firms on the island, says Malta has repeatedly demonstrated its understanding of the industry's requirements and priorities, for example in responding to the need for urgency in the licensing of new funds geared to specific opportunities in a volatile market.

That reputation is serving the island well in persuading businesses to move to Malta,

"Relocation is growing thanks to an attractive fiscal regime, a wide tax treaty network, and a pragmatic regulator."

Joseph Ghio, Fenech & Fenech Advocates

he says: "The number of managers deciding to relocate is growing thanks to an attractive fiscal regime and wide network of double tax treaties, timely licensing by the regulator, and its pragmatic approach, not to mention our warm, sunny climate and English-speaking workforce."

Adam de Domenico, founder and managing director of Zodiac Advisory Services, says the firm has a pipeline of managers looking to set up operations in Malta. In the past demand has come largely from the UK, he says, but legislative changes in other jurisdictions are prompting a significant increase in interest from managers there. "For example, Swiss managers that now face a lot of regulation without enjoying the passport benefits of the AIFMD are looking toward Malta," he says.

ZAS provides services to asset managers including regulatory compliance, accounting, non-executive directorships, investment committee membership and risk oversight. De Domenico notes that incoming firms enjoy a six-month window to organise their operations, something not available in other jurisdictions.

However, he says the MFSA monitors closely aspects such as the credibility of outsourcing providers and is rigorous in expecting firms to deliver on promises made during the approval process, such as an undertaking to base one or more portfolio managers in Malta within a certain timeframe.

Another priority for new firms, he says, is ensuring that they adhere to capital requirements on an ongoing basis. Managers need minimum capital of EUR125,000 plus 2 basis points on assets under management above EUR250m. "We can advise managers or help them to discuss such issues with the MFSA before they get into difficulties, which is always better," de Domenico says. "The regulator is accessible, but has rules and sticks by them." ■

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Adam de Domenico, Zodiac Advisory Services