

HedgeLine

ON-LINE NEWS FOR HEDGE FUNDS AND COMPLIANCE SPECIALISTS

WELCOME to the latest edition of **HEDGELINE** - a publication by FSI dedicated exclusively to hedge fund regulation. Each month we will provide a summary of the major legal and regulatory developments in hedge fund regulation, both in Europe and key offshore jurisdictions. For those who want to read in more depth, we have also provided links to all relevant materials currently available.



LOOK CLOSER

THIS MONTH'S UPDATES ARE:

- FSA gives hedge fund manager £52,500 fine and one-year ban for insider dealing
- Swiss financial taskforce approves new measures to attract hedge funds
- AIMA welcomes HM Treasury's tax proposals for offshore funds

ABOUT YOUR PUBLISHER, FSI:

FSI is a well known law firm with specialist expertise in relation to enquiries and investigations instigated by the FSA and overseas regulators, including AMF in France and the SEC in the US. Often working in conjunction with compliance specialists and other professional advisers, the team will attend interviews at the FSA, advise on all correspondence with the FSA and represent their clients before the Regulatory Decisions Committee and the Financial Services Markets Tribunal. For further information on how we might be able to help you, please contact head of team:

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FSA GIVES HEDGE FUND MANAGER £52,500 FINE AND ONE-YEAR BAN FOR INSIDER DEALING

IN BRIEF:

- Lengthy ban for hedge fund manager for failing to recognise inside information; sanctioned despite not profiting personally from insider dealing
- FSA warns managers entrusted with inside information not to misuse it

The FSA has issued a £52,500 fine and one-year ban on trading against hedge fund manager, Steven Harrison, for insider dealing. Harrison was a portfolio manager at Moore Europe Capital Management in London.

Although not a large fine - in 2006 the former GLG trader, Philip Jabre, was fined £750,000 by the FSA - the decision is significant because of the lengthy ban imposed. It is also notable because Harrison did not profit personally from trading in inside information. The FSA also acknowledged that Harrison did not deliberately commit market abuse but rather had failed to recognise that he had been given inside information.

In September 2006, Harrison was contacted by Credit Suisse regarding the refinancing of Rhodia, a French chemicals firm. Credit Suisse contacted Harrison with the aim of establishing correct pricing for the tender of some of Rhodia's bonds. Harrison, who was asked by Credit Suisse if he wanted to receive restricted information, was subsequently told the size of the refinancing, the timing of the announcement, the likely type of structure and the expected pricing - all of which was deemed inside information.

Shortly after his conversation with Credit Suisse, Harrison told a colleague to buy up to 10 million bonds in Rhodia, knowing that the next day Rhodia would be repurchasing the bonds at a market premium. (In the event, only two million bonds were purchased by the Moore Credit Fund.) As a result of the difference between the market price of the bonds and the premium paid by Rhodia, the Moore Credit Fund made a profit of €44,000.

Harrison would have received a fine for £75,000 if he had not agreed to settle at an early stage of the investigation and qualify for a 30% discount, under the FSA executive settlement procedures. According to the FSA, the level of the penalty also reflected the "very significant impact" that the ban would have on his career. The FSA did not make any criticism of Credit Suisse or Moore Europe Capital Management Limited itself.

Announcing the sanction, the FSA Director of Enforcement, Margaret Cole, stressed that "hedge fund managers and people in similar roles are often legitimately provided with inside information....the FSA expects people entrusted with such responsibility to observe high standards of conduct and not to take advantage of their privileged access to information."

Inside information is defined in section 118 of the Financial Services and Markets Act 2000 as information that is "of a precise nature", "not generally available" and "would, if generally available, be likely to have a significant effect on the price of a qualifying investment."

For more background, see the [FSA Final Notice](#).

SWISS FINANCIAL TASKFORCE APPROVES NEW MEASURES TO ATTRACT HEDGE FUNDS

IN BRIEF:

- Tax rules on hedge fund performance fees and carried interest to be clarified
- Authorisation process for managers of offshore funds to be made easier
- Swiss cantons target U.K. hedge fund managers

A joint taskforce for the Swiss financial services industry has approved several new measures aimed at attracting more hedge fund managers to Switzerland. The measures form part of a financial sector "Master Plan" launched last year by the Swiss Funds Association, Swiss Bankers Association, Swiss Insurance Association and SIX group to regain the country's status as one of the world's top three financial centres.

The first measure announced by the Swiss Financial Centre Dialogue Steering Committee is a clarification of the tax regime for hedge funds, specifically in relation to performance fees and carried interest. The tax position in Switzerland is complex because of different tax rates levied at federal, canton and local levels - according to a [report by KPMG](#), the effective tax rate for hedge funds in Switzerland can vary from 16% to 27%. The new regime, which will be implemented "rapidly" by the Swiss Federal Tax Administration, will simplify the system to ensure a more "competitive fiscal environment."

The second measure announced by the committee is a simplification of the authorisation process required by the Swiss Regulator (the Swiss Federal Banking Commission) for hedge fund managers, particularly those who manage offshore funds. In a recent report, the SFBC noted the "limited opportunity" for managers of foreign hedge funds to be licensed by the SFBC, something it said that could deter institutional investors from investing in Swiss hedge funds.

A number of Swiss cantons have been [aggressively targeting hedge fund managers](#) since the change in the UK non-domicile tax regime announced by Alistair Darling earlier this year, which previously made London an attractive location for non-UK managers. Earlier this month, UK hedge fund Krom River announced it would be moving to the canton of [Zug](#), one of the cantons that has successfully targeted the financial services industry.

Currently, Switzerland holds a 31% share of the global fund of hedge funds industry, with approximately CHF 280 billion (£225 billion) under management, but has relatively few single hedge funds.

For more information on the new measures, go to: [Background Information on the Swiss Financial Centre Dialogue Steering Committee's Report to the Strategy Committee](#).

For a recent assessment of the Swiss Hedge Fund Industry, go to: [Swiss Fund Association, Alternative Investments Committee, Review of First Half of 2008](#).

ALTERNATIVE INVESTMENT MANAGEMENT ASSOCIATION (AIMA) WELCOMES HM TREASURY'S TAX PROPOSALS FOR OFFSHORE FUNDS



IN BRIEF:

- New proposals will help to simplify tax regime and provide greater certainty, according to AIMA
- New definition of offshore fund to be included in 2009 budget
- Draft regulations to be published by end of 2008; New regime in place by spring 2009

The AIMA has given a lukewarm welcome to the Treasury's proposals for a new offshore funds tax regime. First announced in the 2007 Budget, the new regime has several objectives including simplification of the regime, to provide greater certainty for UK investors and funds, to give investors in offshore funds economic parity with investors in onshore ("authorised") funds, and to strengthen anti-avoidance rules so that UK investors make investment decisions on commercial grounds rather than to obtain tax advantages.

In a statement, AIMA said the proposals would go "some way towards simplifying the existing tax regime and providing more certainty to UK investors and funds."

Under the current regime, most hedge funds are classified as non-distributing funds. UK investors in non-distributing funds are subject to tax only when they dispose of their investment; however any profit is treated as income rather than capital gain (known as "offshore income gain") so investors do not benefit from capital gains tax exemptions. The Treasury is proposing to retain this arrangement.

UK investors in distributing funds, which must distribute all their income each year, are taxed differently being liable for both income tax on the annual income distribution and capital gains tax on eventual disposal. The Treasury is proposing to make it easier for funds to apply for distributing fund status by abolishing a 5% investment test, which limited a fund to investing no more than 5% of its assets in another offshore fund at any time during the tax period.

AIMA has endorsed the abolition of the 5% investment test as well as the greater flexibility for funds that inadvertently breach their distributing fund status. The proposals suggest three breaches will be permitted within 10 years.

However, AIMA still believes that the proposals will not reduce the administrative complexity of the existing regime and could also increase costs for hedge fund managers and investors.

As part of the new regime, the Treasury also intends to amend the definition of offshore fund from a regulatory-based definition to a characteristics-based definition. Its aim is to counter unfair tax advantages being obtained "where an offshore tax arrangement is technically outside the current definition of an offshore fund but the arrangement are technically the same." However, most respondents to the Treasury's discussion paper argued the list of proposed characteristics did not go far enough and could lead to greater uncertainty.

The draft regulations are expected to be published by the end of 2008, with implementation planned for Spring 2009.

For more information, see the Treasury's consultation paper, click here: [Offshore Funds: A Discussion Paper](#).

To view the consultation responses, click here: [Offshore Funds: Next Steps](#).