

Payment of
Dividends out of
Capital

DILLON  EUSTACE

DUBLIN HONG KONG NEW YORK TOKYO



Contents

Heading

Payment of Dividends out of Capital

Page 1

Background

Page 1

Updated Requirements

Page 1

Conclusion

Page 2

Contact us

Page 4

PAYMENT OF DIVIDENDS OUT OF CAPITAL

Following a submission from both Dillon Eustace and subsequently the Irish Funds Industry Association, the Central Bank of Ireland (the “Central Bank”) has issued a policy update revising its position in respect of the payment by retail collective investment schemes (including UCITS) of dividends out of capital. All Irish authorised retail collective investment schemes including UCITS are now permitted to pay dividends out of capital subject to complying with a number of disclosure requirements which are outlined below.

Background

The Central Bank’s previous policy of not permitting retail funds (including UCITS) to pay dividends out of capital was borne out of a desire to protect retail investors. This prohibition was in place because of concerns for investor protection based on two key factors, namely (1) a retail investor may not be aware of the potential for capital erosion over the life of his or her investment and (2) there is a danger that returns which include distributions out of capital are potentially misleading.

There has been a recent increase in investor demand globally (and in particular in Asian markets) for investment products that can provide a consistent income with a certain tolerance for a stable or declining net asset value. These products are often referred to as “target dividend income funds”. In response to these trends, many fund promoters are likely to explore launching such funds.

The Central Bank is now satisfied that the concerns highlighted at (1) and (2) above can be addressed by means of enhanced disclosure rather than an outright prohibition. This change in the Central Bank’s policy will facilitate promoters of Irish retail funds (including UCITS) to establish such investment products. As outlined above, the demand for target dividend income funds is particularly significant in Asian markets which are key growth markets for the Irish funds industry. There are currently 61 promoters from Asia with funds either domiciled or serviced from Ireland and a total of 1143 Irish domiciled funds are currently registered for sale in the Asia Pacific region.

Updated Requirements

The Central Bank’s revised requirements are as follows:

Constitutional document

Appropriate provision to allow distributions out of capital must be contained in the relevant constitutional document.

Prospectus

The rationale for distributions out of the capital of the fund must be clearly outlined.

The prospectus must include a prominent risk warning, at the front of the document which describes the effects of making distributions from capital namely that:

- ▣ capital will be eroded;
- ▣ the distribution is achieved by forgoing the potential for future capital growth; and
- ▣ this cycle may continue until all capital is depleted.

A similar risk warning must be contained in any subscription form or marketing material.

The prospectus must highlight that distributions out of capital may have different tax implications to distributions of income and recommend investors to seek advice in this regard.

Income Statements / Distribution Vouchers

Documentation issued to unit holders in conjunction with a distribution should indicate if the distribution has been paid out of capital.

▣ Conclusion

As investor appetite for new types of product continues to grow, Ireland, with its favourable regulatory approach, range of fund structures and relevant experience and expertise, continues to be an attractive jurisdiction for the establishment of funds. In particular, UCITS products have proved appealing to promoters seeking to take advantage of the strong distribution opportunities and globally recognised brand name that authorisation under the UCITS regime provides.

This policy update indicates the Central Bank's willingness to adopt a pragmatic and evolving approach to regulation in seeking a balance between investor demand with investor protection. Existing promoters wishing to avail of this change in policy should review their fund's documentation (prospectus, constitutional documents, subscription application forms, dividend policies) to assess the impact of this policy change on your fund and determine what steps are necessary should you decide to implement such changes. Your usual Dillon Eustace contact will be able to advise and assist you in this regard.

CONTACT US

Dublin

33 Sir John Rogerson's Quay,
Dublin 2,
Ireland.
Tel: +353 1 667 0022
Fax: +353 1 667 0042

Hong Kong

Room 604
6/F, Printing House
6 Duddell Street
Central
Hong Kong
Tel: +852 35210352

New York

245 Park Avenue
39th Floor
New York, NY 10167
United States
Tel: +1 212 792 4166
Fax: +1 212 792 4167

Tokyo

12th Floor,
Yurakucho Itocia Building
2-7-1 Yurakucho, Chiyoda-ku
Tokyo 100-0006, Japan
Tel: +813 6860 4885
Fax: +813 6860 4501

e-mail: enquiries@dilloneustace.ie

website: www.dilloneustace.ie

Contact Points

Date: 14 February 2012

For more details on how we can help you, to request copies of most recent newsletters, briefings or articles, or simply to be included on our mailing list going forward, please contact the below contacts or your usual Dillon Eustace contacts.

Brian Higgins

e-mail: brian.higgins@dilloneustace.ie
Tel : +353 1 667 0022
Fax: + 353 1 667 0042

Emmet Quish

e-mail: emmet.quisht@dilloneustace.ie
Tel : +353 1 667 0022
Fax: + 353 1 667 0042

DISCLAIMER:

This document is for information purposes only and does not purport to represent legal advice. If you have any queries or would like further information relating to any of the above matters, please refer to the contacts above or your usual contact in Dillon Eustace.

Copyright Notice:

© 2012 Dillon Eustace. All rights reserved.

DILLON  EUSTACE

DUBLIN HONG KONG NEW YORK TOKYO

33 Sir John Rogerson's Quay, Dublin 2, Ireland.
www.dilloneustace.ie

In alliance with Arendt & Medernach