Passport to the U.S.: Finding the Right Strategies for International Fund Managers

By Barbara Nelligan and Ryan Dargis

In an effort to tap into fresh sources of capital, non-U.S. fund managers are looking increasingly to the U.S. to distribute investment strategies. This raises a number of issues, chief among them are the right vehicles for the job, the regulatory considerations involved, and more.

Looking at the U.S. market today, there are roughly $20T[1] in assets managed in pooled vehicles. The largest and most familiar market is the registered mutual fund market which dominates with $14.5T. Today, however, over $3T is managed in bank maintained funds and $3T in unregistered vehicles such as group trusts, LP/LLCs, Statutory Business Trusts and the like. How does an adviser decide the best course of action to meet the end objective of growing assets while maintaining a budget?

As each market entry strategy has its own unique set of challenges, it is crucial that advisers take the time to properly match the product with the purpose. For instance, a European adviser looking to distribute its strategy on a broad basis with the most flexibility would likely consider a U.S. Registered Mutual Fund. This type of fund would not be entirely unfamiliar if the adviser was currently managing a UCITS vehicle. Both vehicles are highly regulated and generally governed (with some exception) by independent bodies; the management company in the case of UCITS and the Board of directors in the case of the mutual fund. Both also have the ability to offer multiple series and multiple share classes. These can be utilized to target specific investor groups while managing one portfolio.

Registered mutual funds are very familiar to the majority of U.S. investors and the regulatory framework provides a large degree of comfort and security for those investors. This comfort, however, comes at a cost. Launching registered mutual fund product is expensive and the adviser needs to be prepared as a substantial amount of assets will likely be required to ensure the fund can be priced competitively yet be profitable to the firm.


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One solution to this cost problem is the Series Trust or Umbrella Trust. Series Trusts are maintained by many service providers and offer an existing regulatory framework under which an adviser may launch its own individual fund (series). The Series Trust solution provides an efficient, cost effective solution to the adviser and access to expertise on fund governance.

That said, what if the adviser's business plan is more targeted? What if the adviser is considering solely the U.S. retirement market? A Collective Fund may be a good choice. These funds operate similarly to mutual funds and are well suited for the Defined Contribution market. They are exempt from SEC registration and, therefore, carry lower overall cost structures. Collective Funds can only be sponsored by banks willing to deploy the governance structure needed to oversee the investment firm as the sub-advisor. Yet, there is increasing acceptance of this vehicle within its eligible investor base and it is a strong viable option.

Finally, there are a host of unregistered vehicles that may be suitable options for an international adviser. Targeted to larger institutional and high net worth investors, Group Trusts, LPs and Business Statutory Trusts are exempt from registration with the SEC, are usually valued less frequently than daily and tend to carry lower cost structures. However, the exemptions under which these vehicles operate include investor head count limits and specific standards of investor sophistication level. These vehicles may be suitable when the adviser has targeted investors and is looking to "test the waters" before investing in a more widely distributed vehicle.

Regardless of the strategy, penetrating the U.S. market has been an ongoing challenge for non-U.S. asset managers and could become even more so in light of various regulatory mandates in the making. Dodd-Frank, the SEC's Form PF and the CFTC's CPO-PQR are compelling investment managers to devote more time and energy to the process of registration and reporting than ever before. As a result, the overall cost structure for advisers targeting U.S. investors is increasing.

It is now even more important for advisers to consider their distribution strategies and do the work upfront within the U.S. distribution channels to ensure that their strategies are received. While U.S. mutual funds require a distributor, similar to the fund promoter of UCITS, the distributor is more regulatory in nature. The real legwork of active distribution still normally resides with the adviser. This will require patience; U.S. distribution channels, including consultants and retirement plan sponsors demand a 3-5 year track record before considering a strategy. Faced with these regulatory and distribution challenges, investment managers are finding it helpful to team with strategic partners who have the scale to support a large middle and back office operation, as well as the jurisdictional expertise needed to monitor ongoing regulatory developments and maintain operational processes.

Outsourced platforms offered by an experienced service provider can address many of the issues associated with new fund distribution, reducing start-up costs while streamlining the launch process. In addition to easing the administrative burden, these platforms allow the investment manager to leverage the provider's existing governance and risk-management infrastructure.

1. EFAMA, September 2012

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