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Cyprus, an emerging fund destination – key facts for setting up an alternative investment fund

By Nicoletta Kouvara Pantelides

As an EU member state and Eurozone member, Cyprus is emerging as the new destination in the international fund industry. It is geared as an attractive and cost-effective jurisdiction for the set up and operation of alternative investment funds and alternative investment fund managers, capitalising also on the high-level professional services and resources.

By the transposition of the European Union Directive 2011/61/EU on Alternative Investment Fund Managers (AIFMD) and the update of its legal framework relating to the formation of various types of alternative investment funds, Cyprus has seen a rapid increase in the set up and licensing of various types of alternative investment funds (AIF) and of alternative investment fund managers (AIFM). In 2018, the assets under management by funds set up in Cyprus reached €4.86bn and there were 170 registered funds and management companies. Currently, there are more than 60 managers and funds pending registration.

Fund managers and investors benefit from the local regulatory regime which harmonises all EU financial services regulations in relation to UCITS V, AIFMD and MIFID II, permitting use of the European passport for the cross-border distribution of units and providing a high level of protection to investors.

Legal forms of AIFs

- AIFs can be established using one of the following legal forms (depending on the type of AIF being set up):
- Common funds;
- Investment companies (fixed or variable capital);
- Partnerships, with or without legal personality.

The types of AIFs that can be set up and licensed/registered in Cyprus are AIFs with unlimited number of investors, AIFs with limited number of persons (AIFLNP) and Registered Alternative Investment Funds (RAIFs). AIFs can include hedge funds, private equity funds and venture capital funds.

Key features of various types of AIFs

1. AIF with unlimited number of investors

An AIF must be licensed and supervised by the Cyprus Securities and Exchange Commission (CySEC). There is the flexibility of setting up the AIF under any of the prescribed legal forms, either as open ended or closed ended and it can be marketed to retail and/or well informed and professional investors.

It can be externally managed (falling under AIFMD) or self-managed subject to certain conditions, including, not falling within the AIFMD thresholds, that is, (i) assets of the portfolio of AIF not exceeding €100 million if leverage is used or (ii) €500m if no leverage is used and there is no redemption for five years.

A self-managed AIF, not being an AIFM which is an internally managed AIF, must have an initial capital of at least €125,000. It must invest a minimum of €500k, which must be realised within the first year.

A depositary must be appointed and can either be a local or EU licensed credit institution/ investment firm or a third country firm (subject to certain conditions).



A RAIF must appoint a depositary, which is either a local or an EU licensed credit institution/investment firm or a third country firm (subject to certain conditions).

2. AIF with limited number of persons (AIFLNP)

An AIFLNP must also be licensed and supervised by CySEC and must be set up in the form of an investment company or limited liability partnership (with or without legal personality). This form of AIF may only be marketed to a maximum of 50 well-informed and professional investors.

It should not exceed the thresholds of the AIFMD, described under the AIF section above. If these are exceeded, the AIFLNP must convert into an AIF of unlimited number of persons.

It can be either self-managed or externally managed by Cyprus UCITS Manager/ Cyprus investment firm or third country firm (subject to conditions), and not by an AIFM. An externally managed AIFLNP does not need to meet initial capital requirements, however, a self-managed AIFLNP requires an initial capital of €50k. It has an obligation to invest a minimum of €250k, which must be realised within the first year.

A depositary must be appointed which is either a local or an EU licensed credit institution/ investment firm or a third country firm (subject to certain conditions). If, however, the total assets under management are less than €5m or the AIFLNP has less than five investors or its assets are not subject to custody, it is exempted from the requirement to appoint a depositary.

3. Registered Alternative Investment Fund (RAIF)

In 2018, the RAIF was introduced as a new fast and cost-effective fund option. Unlike the other licensed AIFs, the RAIF must be registered with CySEC (not licensed) and is subject to supervision by its external manager. It can be set up in the form of a closed or open-ended common fund, an investment company or a limited partnership (with or without legal personality) and can be marketed to an unlimited number of well-informed and professional investors.

It must be externally managed by a licensed AIFM being responsible for its supervision. If the RAIF is set up as a closed-ended partnership and it invests as a minimum 70% of its funds in illiquid assets (real estate property, ships, planes, etc.), it may be managed by local or EU licensed UCITS manager or investment firm.

There are no initial capital requirements, but when a RAIF is externally managed by an AIFM, there is an obligation to invest a minimum of €500k which must be realised within the first year. There are no investment restrictions except that they cannot be set up as Funds of Funds, Money Market Funds or Loan Origination Funds.

A RAIF must appoint a depositary, which is either a local or an EU licensed credit institution/investment firm or a third country firm (subject to certain conditions).



Incoming dividends are exempt from tax, subject to certain conditions. Income arising from trading in securities, such as shares, shares options, units in AIFs are exempt from tax in Cyprus.

Tax Benefits

There is a plethora of tax benefits applicable to AIFs. Significantly, the corporate tax rate is currently set at 12.5% on income accrued from AIF operations, following the deduction of expenses incurred exclusively in the production of income, including but not limited, to office costs, payroll and outsourcing costs.

Interestingly, as from the 2015 tax year onwards, a notional interest deduction (NID) for new equity can reduce the taxable base for interest received by up to 80% (for investment company type funds). This reduces the effective tax on interest to 2.5%.

Incoming dividends are exempt from tax, subject to certain conditions. Income arising from trading in securities, such as shares, shares options, units in AIFs are exempt from tax in Cyprus. There is no taxation of capital gains (unless they arise from disposal of real estate in Cyprus or shares of companies holding real estate in Cyprus). Fund management services are exempt from VAT, subject to certain conditions. For foreign investors, there is no withholding tax on dividends, no taxation on redemption of units and no deemed distribution restrictions.

There are also tax incentives for high-earning managers and high net worth individuals relocating to Cyprus. Subject to certain conditions, high earning executives may opt to be taxed at the flat rate of eight per cent on amounts constituting carried interest, with a minimum tax payable of €10k per year, for a total period of 10 years.

Additionally, an extensive double tax treaty network covering over 60 countries, offers a competitive advantage for cross border investment.

Cyprus evidently has all the prerequisites to rival other EU jurisdictions in fund formation and asset management, due to the sound regulatory regime, the lower set-up and on-going operation service costs, the multiple tax benefits, its developed infrastructure and highly skilled workforce. Asset managers seeking the above should have a closer look into this emerging fund destination.

Nicoletta Kouvara Pantelides is a Partner at Chrysostomides, specialising in corporate and commercial law, banking and financial services, funds, M&A transactions, secured financing, and capital markets.

Chrysostomides counts over 35 years' experience and commitment to client service and is one of Cyprus' leading and largest law firms. Its experienced Funds team advises on and assists clients with the setting-up, licensing, passporting of services, and regulatory compliance of Investment Firms, UCITS, AIFs, as well as the managers of these funds. The firm also advises on related services, including the re-domiciliation of the funds and their managers, listing of the funds on regulated and unregulated markets, as well as, assisting with tax related matters.

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