



## Cyprus Alternative Investment Fund

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## Introduction: Alternative Investment Funds Law 2014

The new AIF Law has passed by the House of Representatives on the 10th of July 2014 and seeks to improve the regulatory conditions for Cyprus AIF's. Under the new law CySEC will become the sole Regulatory Authority for AIF's.

The new law was designed to make Cyprus a more competitive EU investment fund jurisdiction along with other EU member states. In particular it initiates the option to set up AIF's marketed to retail investors and AIF's with multiple investment compartments as well.

In addition the new law initiates the option to set up an AIF taking the contractual form of a Common Fund, which is a type of fund developed in Ireland and provides low administrative costs and tax efficiency. Finally, the new law brings up the option to set up an AIF marketed to Well Informed investors with unlimited number of Investors.

## Definition of an AIF

The new legislation defines an AIF as a collective investment scheme, including its investment compartments which:

- raises capital from a number of investors with a view to investing it in accordance with a defined investment policy for the benefit of those investors;
- has the exclusive purpose of the collective investment of its available capital in assets to ensure for the investors the benefit of the results of the management of their assets;
- it is not a UCIT authorized under the UCITS IV Directive (2009/65/EC).

## Types of AIFs

An AIF can be:

- Alternative Investment Fund with **Unlimited Number of Persons** which:
  - may be marketed either to well-informed or retail investors
  - have investor shares which are freely transferable
  - may be listed on a Stock Exchange, and in the case of a Variable Capital Company or Fixed Capital Company marketed to Retail investors, may be traded
  - are subject to minimum capital requirements equal to €125.000 or €300.000 in the case of self-managed AIF/AIFM.
  - are subject to certain investment restrictions for the purpose of risk spreading and ensuring liquidity
- Alternative Investment Fund with **Limited Number of Persons** which:
  - may not exceed the total number of 75 investors
  - may be marketed to professional or/and well-informed investors
  - may take one of the two following legal forms:
    - Variable/Fixed capital company ( 'VCC/FCC' )
    - Limited Partnership ( 'LP' )
  - In the legal form of a company the AIF can be either externally or self managed. In the legal form of a 'LP' the AIF must always have an external manager.
  - have investor shares which are freely transferable only if their transfer does not result in the AIF having more than 75 investors

All types of AIF's can be open ended or close ended Funds

## Investor Classification

There are two classifications of investors:

- Well-informed Investor
  - A Professional Client, as such term is defined in the MiFID; OR
  - One that meets the following two requirements:
  - Confirms in writing that he/she is a qualified investor and that he/she is aware of the risks involved with an investment in the relevant AIF; and
    - (1) investment made in AIF is at least €125.000 OR
    - (2) expertise, experience and knowledge in evaluating an investment opportunity properly, have been certified by a licensed bank/credit institution, an authorised investment firm or an authorised Management Company
- Retail Investor
  - An investor, other than well-informed, i.e. who does not meet the requirements above

## Legal Forms of AIFs

An AIF can take the following legal forms:

- Fixed Capital Company ('FCC')
- Variable Capital Company ('VCC')
- Limited Partnership ('LP'), and
- Common Fund ('CF')

All four types of AIFs may be established with limited or unlimited duration.

## Investment Manager

In the case of an AIF with Unlimited Number of Persons, a VCC and FCC can be managed either internally (self-managed) or externally (appoint an external manager). However it is mandatory for a CF to have an external manager. An LP's external manager is the General Partner.

An external manager must fulfill the following licensing requirements:

- if coming from an EU Member State, he/she will need to be one of the following:
  - Alternative Investment Fund Manager; or
  - UCITS Management Company; or
  - Investment Firm; or
- if coming from a third country, he/she will need to comply with the AIFMD rules on third country undertakings.

In the case of an **AIF with Limited Number of Persons**, a VCC and FCC can be managed either internally (self-managed) or externally (appoint an external manager). However it is mandatory for an LP to have an external manager.

The licensing requirements for an external manager depend on the investment objectives:

- if the AIF will invest in financial instruments, then:

- if established in an EU Member State, he/she will need to be one of the following:
  - UCITS Management Company; or
  - Investment Firm; or
  - if established in a third country, he/she will need to grant permission for managing the specific AIF and have adequate regulation and supervision in its home state;
- if the AIF will invest exclusively in other types of assets (eg. real estate, shipping, energy, etc.), the externally appointed manager may be a company incorporated solely for the purpose of managing the specific AIF whose suitability is deemed by the CySEC.

In the case of an AIF being self – managed (can be applied only for VCC & FCC) one of the following requirements must be met:

- ④ Assets of AIF's portfolio including those obtained with leverage do not exceed €100mil
- ④ Assets of AIF's portfolio do not exceed €500mil euro for AIFs with no leverage and for which shareholders cannot acquire their share for the first 5 years since the original investment
- ④ If the managers of AIF decide not to appoint an external administrator, then in case that the assets of the fund exceed the above amounts then the AIF it takes the form of an AIF/AIFM

## Custodian/Depository

AIF's must appoint a Custodian for safekeeping and cash monitoring functions. It must be based in the Republic or other EU member State or third country provided that CySEC and the competent authorities of the third country have signed a Memorandum of cooperation and information exchange.

The custodian can be a credit institution or an investment company or any other entity determined by the member states as eligible for custodian based in EU or in the case of AIF's outside the EU in the country of origin.

Its duties include:

- ④ Ensuring the appropriate monitoring of the AIF's cash flow
- ④ Custody of the AIF's assets
- ④ Monitoring the observance of the current legislation

AIF with limited number of persons is allowed not to designate a Custodian in case:

- ④ its total assets do not exceed the amount of €5mil (or equivalent in another currency)
- ④ its total assets are not indicated for safekeeping
- ④ the memorandum or the articles of association limit the number of shareholders to 5 (in case of AIF with limited number of persons with multiple investment compartments the total number of shareholders of all compartments is taken into account)



## Fund Administrator

The Fund's Administrator renders services with regards to book-keeping and accounting, compliance, reporting, filing, share issue, transfer and redemption and other relevant services.

The Administrator must be approved by CySEC and our expectation at present is that CySEC will require the administrator to be based in Cyprus.

## Auditors

A qualified professional Cyprus auditor must be appointed upon formation of the AIF and will attend to the annual audit.

## Legal Advisors

The AIF's lawyers draft various documentation such as the Memorandum and Articles of Association in the case of VCC or partnership agreement in a case of LP and attend to the legal formation, licensing and regulatory compliance of the AIF both upon formation and afterwards.

## AIF with Multiple Investment Compartments (Sub – Funds)

A significant development provided in the new AIF Law is the ability to set up an AIF with multiple investment compartments, each constituting a separate pool of assets. Such an AIF constitutes a single legal entity. Each investment compartment shall issue units corresponding solely to its assets. Correspondingly, the value of the assets per investment compartment may differ. Unit holders of a specific compartment shall only have rights arising from the assets of such compartment, while each compartment shall be liable for the obligations arising solely from its constitution, operation or dissolution.

A compartment of an AIF may invest in another compartment of the same AIF, if such possibility is provided for in its constitutional documentation, under the condition of certain defined investment restrictions.

## Benefits of an AIF

Cyprus offers a range of legal, regulatory and tax solutions to address and meet the needs of AIF promoters and investors alike. Services such as set up and acquisition structuring, fund administration, legal, custody and audit are provided in a wide and customized range, and at competitive costs in comparison to other reputable funds jurisdictions. It further has in place rigorous anti-money laundering regulations, in line with EU and international standards.

There are no specific provisions or special modes of taxation in Cyprus tax law regarding AIFs. Therefore, provided an AIF is structured in the form of a private limited liability company, and its management and control is exercised in Cyprus, it is taxed in the same way as a Cyprus tax resident company. All of the advantages afforded by the Cyprus tax regime will fully apply to the AIF regime.

The following are the main tax advantages enjoyed by an AIF:

- Exemption from tax on profits from disposal of shares and other financial instruments;
- Exemption from tax on foreign dividends received (with some conditions);
- No withholding tax on interest and dividend payments made to non-residents;

- No stamp duties on the subscription, redemption, repurchase or transfer of units;
- Dividends distributed or deemed to be distributed by an AIF to Cyprus tax residents are subject to 3% SDC (compared to 17% that applies to dividends from normal limited liability companies to Cyprus tax residents);
- No withholding tax on redemption of units;
- Can obtain a Tax Residency Certificate;
- Enhanced image and creation of substance. Unlike private companies, an AIF is subject to regulation and monitoring, all Directors are deemed to be “fit and proper”, investment strategy is documented within a Private Offering Memorandum, and a custodian/depositary and investment manager are typically appointed.
- A wide network of Double Tax Treaties is in place with more than 45 countries worldwide, securing tax incentives and encouraging the channeling of funds in other countries with nil or low withholding tax rates;
- In practice most AIFs generate only exempt forms of income, hence are not subject to Cyprus tax.

## Application procedure and requirements

A comprehensive application must be submitted to CySEC in order to an AIF license. The application must include the following:

- Private Offering Memorandum, listing among other things the strategy of the fund, expected return for investors, risk management and identification of all providers.
- Details of all proposed Directors, with each providing the following:
  - Copy of passport and recent utility bill evidencing residential address
  - CV with details covering a minimum period of 10 years
  - Reference letters from all employers in last 10 years
  - Copy of all college/university/diploma or professional designation. If not in English, official translation is required by a sworn translator of the local Ministry of Justice
  - Clean criminal record certificate, translated by a sworn translator of the local Ministry of Justice
  - Duly completed CySEC questionnaire form

It should be noted that all Directors must be “fit and proper”, meaning that must have adequate financial and fund management experience and academic credentials. In addition in practice CySEC requires a minimum of two Executive Directors

- Details of the following providers:
  - Investment manager
  - Custodian
  - Administrator
  - Auditor
  - Legal advisors

CySEC will require anywhere from 4 to 12 weeks for review and approval of the application (provided there are no deficiencies in the application)



## Services provided by LLPO Law Firm

We can assist the company with the application process, as described below:

- Preparation and submission of an application package to CySEC to obtain a license, including advice on the best way to set up the fund as regards staffing, organisational structure, costs, etc.
- Preparation and reviewing of any requested documentation and/or agreements and/or contracts for the application or during the activation of the fund.
- Recommendation and appointment of service providers
- Provision of administrative services including directors, secretary and registered office address

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