

Cyprus

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1 Regulatory Framework

1.1 What legislation governs the establishment and operation of Alternative Investment Funds?

The legislation that governs the establishment and operation of Alternative Investment Funds in Cyprus is the Alternative Investment Funds Law of 2014 (the “AIF Law”) and the Alternative Investment Fund Managers Law of 2013 (the “AIFM Law”). Alternative Investment Funds are authorised and regulated by the Cyprus Securities and Exchange Commission (“CYSEC”).

In addition, the adoption of the EU Alternative Investment Fund Managers Directive (“AIFMD”) has led to the modernisation of the legal framework governing investment funds in Cyprus.

1.2 Are managers or advisers to Alternative Investment Funds required to be licensed, authorised or regulated by a regulatory body?

Fund Manager

As per Section 6 of the AIF Law, an AIF may be either:

- (a) self-managed, where it does not appoint an external manager, if it is established as an investment company and one of the following applies:
 - (i) the assets of the portfolio of the AIF, including any assets acquired through use of leverage, do not exceed a threshold of EUR 100,000,000 in total;
 - (ii) the assets of the portfolio of the AIF, where the AIF does not employ leverage and its unitholders have no redemption rights exercisable during a period of five years following the date of initial investments in each AIF, do not exceed a threshold of EUR 500,000,000; and
 - (iii) the persons that sign the instruments of incorporation of the investment company under incorporation or the members of the board of directors, in case of an incorporated company, decide not to appoint an external manager, but to exercise internal management according to the provisions of the AIFM Law, either obligatory in the case that the assets of the portfolio of the investment company exceed the thresholds of points (i) or (ii) above, respectively, or by choice, because they choose to opt into the AIFM Law, then the investment company is considered as an AIFM and falls within the scope of the AIFM Law; or
- (b) externally managed, where it appoints an external portfolio manager who:

- (i) is an AIFM authorised in accordance with the AIFM Law;
- (ii) where subparagraph (i) does not apply, may operate as a management company authorised in accordance with the Open-ended Undertakings for Collective Investments Law; or
- (iii) operates as an Investment Firm authorised in accordance with the Investment Services and Activities and Regulated Markets Law, as amended.

Each self-managed AIF and each external manager of an AIF, where they are not authorised AIFMs, are subject to registration in accordance with the provisions of section 4(3) of the AIFM Law, in the Special Register of sub-threshold AIFMs which is maintained by CYSEC.

A Variable Capital Company and a Fixed Capital Company can be self-managed or externally managed; however, a Limited Partnership and Common Fund should always appoint an external manager.

In case an AIF is self-managed, the application to CYSEC shall also be accompanied by its programme of activities, which shall include, *inter alia*, the organisational structure of the AIF.

Administrator

Does not require a licence to act as an outsourced administrator of a fund. The administrator is responsible for keeping the fund’s books and records, accounting, reporting filing, share issue and other services.

Depository

As per the provisions of the AIF Law, the assets of the AIF shall be entrusted for safe-keeping to a depository which (a) has its registered office in Cyprus or in another Member State of the EU or in a third country, provided that CYSEC has signed a Memorandum of Understanding and Exchange of Information with the competent authorities of the third country, and (b) is either a credit institution or investment firm or another category of institution which is subject to prudential regulation and ongoing supervision and which falls within the categories of institution which have been defined by their home state as eligible to be a depository.

1.3 Are Alternative Investment Funds themselves required to be licensed, authorised or regulated by a regulatory body?

As per section 12 of the AIF Law, the commencement of operations of an AIF requires the prior authorisation and communication of the authorisation by CYSEC, in accordance with the provisions of the AIF Law.

1.4 Does the regulatory regime distinguish between open-ended and closed-ended Alternative Investment Funds (or otherwise differentiate between different types of funds) and if so how?

Section 7 of the AIF Law provides that an AIF can be established as:

- (a) an open-ended Alternative Investment Fund, where its unitholders have the right to redeem or repurchase their units upon request (i) at any time, or (ii) at regular intervals which do not exceed one year and are defined in the fund rules or the instruments of incorporation of the AIF; or
- (b) a closed-ended Alternative Investment Fund, where its unitholders have the right to redeem or repurchase their units upon request: (i) at regular intervals that exceed one year but shall not extend to more than five years and are defined in the rules or instruments of incorporation of the AIF (however, in the case of an AIF that is constituted as a venture capital fund in accordance with Regulation (EU) No. 345/2013, the initial period of redemptions may be extended up to 10 years from the date of its incorporation); or (ii) at a specific time that is defined in the fund rules or the instruments of incorporation of the AIF.

1.5 What does the authorisation process involve?

CYSEC shall grant authorisation to the AIF once it is satisfied that the application – including the information on the fund manager, or board of directors in the case that there is no external manager of the fund, the custodian, the prospectus and all necessary incorporation documentation – has been submitted as per the requirements of the AIF Law. CYSEC shall inform the external manager of the AIF, or the AIF itself in the case that it is self-managed, within three months of the submission of the filing of the complete application, in accordance with section 12 of the AIF Law, whether or not the authorisation has been granted.

In the case that CYSEC refuses to grant the authorisation, the reasons for such a decision must be justified.

1.6 Are there local residence or other local qualification requirements?

An AIFM of the Republic of Cyprus (the “Republic”) must have its registered office and central management in Cyprus; an AIF licensed by CYSEC must also have its registered office in Cyprus.

The depositary shall have its registered office in the Republic or in another Member State of the EU or in a third country, provided that CYSEC has signed a Memorandum of Understanding and Exchange of Information with the competent authorities of the third country.

1.7 What service providers are required?

The service providers appointed by an AIF managed by an external manager will include the external manager and a depositary, as per section 20 of the AIF Law.

The service providers appointed by a self-managed AIF will include the directors responsible for the management of the AIF, the administrator, the depositary (subject to the depositary not being appointed in accordance with section 23(2) of the AIF Law). The self-managed AIF shall also appoint a Compliance Officer, an Internal Auditor, an External Auditor and a Risk Manager.

1.8 What co-operation or information sharing agreements have been entered into with other governments or regulators?

The AIF Law and AIFM Law, through a number of directives, have adopted EU and ECD standards in respect of the supervision and prevention of money laundering and insider dealing.

Under Regulation 1287/06, the Competent Authorities have the obligation to protect market integrity, report transactions to the European Securities and Markets Authority (“ESMA”), maintain records and collaborate with other Member States.

In addition, as per Directive 2011/61, if units are to be marketed in a third country, that country must: (i) not be listed as non-cooperative FATF; (ii) have signed an agreement of understanding with the Member State; and (iii) if non-EU units are to be marketed in the home Member State of the AIFM, a notification to the home Member State must be made. The competent authority of the home Member State will inform ESMA.

2 Fund Structures

2.1 What are the principal legal structures used for Alternative Investment Funds?

An AIF can be set up under the following legal structures:

- (a) as a mutual fund;
- (b) as an investment company in the form of a variable capital investment company or/and a fixed capital investment company; or
- (c) as a limited liability partnership.

2.2 Please describe the limited liability of investors.

The liability of investors of an AIF should be examined with respect to the legal structures of the AIF.

In the case of a limited liability partnership, the liability of a limited liability partner is limited to the amount that the partner undertakes to contribute or is committed to contribute in the capital of the partnership and, without prejudice to the cases provided for by the AIF Law, is not liable for the debts or the obligations of the limited liability partnership beyond the amount that the partner contributed or is committed to contribute.

In the case of a common fund, the unitholders are co-owners of each of the assets that comprise the portfolio of the common fund, and are liable only up to the amount of their contribution, which is expressed in units of the common fund.

The investment company has the legal form of a limited liability company with shares, whose liability is limited to the amount, if any, unpaid on its shares.

2.3 What are the principal legal structures used for managers and advisers of Alternative Investment Funds?

Managers and advisers are generally set up as private limited liability companies.

2.4 Are there any limits on the manager's ability to restrict redemptions in open-ended funds or transfers in open-ended or closed-ended funds?

The subscriptions and redemptions of units shall take place in accordance with the conditions included in the instruments of incorporation and the prospectus of the AIF.

In addition, in an open-ended fund, the unitholders have the right to redeem or repurchase their units upon request (i) at any time, or (ii) at regular intervals which do not exceed one year and are defined in the fund rules or the instruments of incorporation of the AIF.

In closed-ended funds, the unitholders have the right to redeem or repurchase their units upon request: (i) at regular intervals which exceed one year but shall not extend to more than five years and are defined in the rules or instruments of incorporation of the AIF; or (ii) at a specific time that is defined in the fund rules or the instruments of incorporation of the AIF.

2.5 Are there any legislative restrictions on transfers of investors' interests in Alternative Investment Funds?

In its incorporation documents, an AIF with a limited number of persons shall: (a) specify that the relevant fund is only addressed to professional and/or well-informed investors as per the provisions of the law; (b) limit the number of its unitholders, including the co-holders, to a maximum of 75 persons; and (c) not allow the issue of bearer shares.

In addition, restrictions on the transfer of shares may also be included in the partnership agreement of the limited liability partnership or the incorporation documentation of the AIF.

3 Marketing

3.1 What legislation governs the production and offering of marketing materials?

The production and offering of marketing materials are governed by the following:

- The Alternative Investment Fund Managers Law of 2013 (the "AIFM Law").
- The Alternative Investment Funds Law of 2014 (the "AIF Law").
- The Prospectus Law 114(I)/2005 as amended.

3.2 What are the key content requirements for marketing materials, whether due to legal requirements or customary practice?

Section 30 of the AIFM Law provides the information that the AIFM should disclose to the investors of the AIFs that they market. This information includes, among others: information on the investment strategy; ways in which the investment strategy may change; the identity of the AIFM, the AIF's depository, auditor and any other service providers; and a description of their duties and the investors' rights. It should also include a description of the AIF's valuation procedure and the pricing methodology for valuing assets, a description of how the AIFM ensures the fair treatment of investors, etc.

The main purpose of giving this information to investors is to provide them with sufficient information as to their investment in

the fund, therefore the AIF Law provides that all announcements from an AIF to investors shall be precise, clear and not misleading.

In addition, section 77 of the AIF Law provides that the prospectus of an AIF shall include, at least, the information referred to in section 30(1) of the Alternative Investment Fund Managers Law. The prospectus shall also include a statement in a distinct section on its first page, to the effect that the AIF is targeted at professional and/or well-informed investors or retail investors, accordingly.

3.3 Do the marketing or legal documents need to be registered with or approved by the local regulator?

AIFs should have a prospectus, which has to be submitted to CYSEC for prior approval; any changes made to the prospectus should also be sent to CYSEC for prior approval.

3.4 What restrictions are there on marketing Alternative Investment Funds?

An AIFM of the Republic, authorised by CYSEC, may market units of any EU AIF to professional investors across the EU, subject to the requirements of the AIFM Law. The AIFM which intends to market units of an EU AIF shall submit a notification to CYSEC in respect of the relevant AIF, as well as the necessary documentation as per the provisions of the AIFM Law. CYSEC shall, within 20 days from receipt of the notification, inform the AIFM whether it may start marketing the AIF identified in the notification.

3.5 Can Alternative Investment Funds be marketed to retail investors?

The AIF Law provides that an AIF, which is either self-managed or externally managed by an AIFM, may market its units to retail investors in the Republic in accordance with section 67 of the AIFM Law. This is subject to CYSEC's authorisation, which may impose obligations on the AIFM or the AIF in addition to those requirements applicable to AIFs marketed to professional investors in the Republic.

3.6 What qualification requirements must be carried out in relation to prospective investors?

The AIF Law and AIFM Law distinguish between the following categories of investor:

A well-informed investor is defined as an investor who is not a professional investor and fulfils the following conditions:

- (a) the investor confirms in writing that he is a well-informed investor and that he is aware of the risks related to the proposed investment; and
- (b) either his investment in the AIF amounts to at least EUR 125,000, or he is assessed as a well-informed investor, either by a credit institution that falls within the scope of the Banking Laws as amended, or by an Investment Firm, or by a UCITS management company, and the above-mentioned assessment shows that he has the necessary experience and knowledge to be able to evaluate the appropriateness of the investment in the AIF.

A professional investor is an investor who possesses the experience, knowledge and expertise to make its own investment decisions and properly assess the risks that it incurs, and who complies with the criteria of Law 144(1)/2007 on the provision of investment services, the exercise of investment activities, the operation of regulated markets and other related matters.

A retail investor is defined as an investor who does not meet the conditions required in order to be included in the “professional investor” or “well-informed investor” category.

3.7 Are there additional restrictions on marketing to public bodies such as government pension funds?

There are no additional restrictions.

3.8 Are there any restrictions on the use of intermediaries to assist in the fundraising process?

No, there are no such restrictions, except if the services that they provide fall within the scope of regulated services, which will require a licence.

3.9 Are there any restrictions on the participation by financial institutions in Alternative Investments Funds (whether as sponsors or investors) arising from the 2008 financial crisis?

No, there are no such restrictions.

4 Investments

4.1 Are there any restrictions on the types of activities that can be performed by Alternative Investment Funds?

The AIF can perform only the activities listed in the incorporation documentation of the AIF, and should not be engaged in other activities, since CYSEC has granted the licence for the operation of the AIF on the basis of the activities listed in the incorporation document of the same.

There are also some additional restrictions imposed on self-managed AIFs as per section 6 (2) of AIF Law, which states that an AIF can be considered self-managed when it does not appoint an external manager, if it is established as an investment company and one of the following applies: (i) the assets of the portfolio of the AIF, including any assets acquired through the use of leverage, do not exceed a threshold of EUR 100,000,000 in total; and (ii) the assets of the portfolio of the AIF, where the AIF does not employ leverage and its unitholders have no redemption rights exercisable during a period of five years following the date of initial investment in each AIF, do not exceed a threshold of EUR 500,000,000.

4.2 Are there any limitations on the types of investments that can be included in an Alternative Investment Fund's portfolio whether for diversification reasons or otherwise?

CYSEC may specify by directive any investment restrictions regarding AIFs according to the nature of the assets in which they invest and the investors to which they are addressed.

4.3 Are there any restrictions on borrowing by the Alternative Investment Fund?

There are no restrictions on borrowing; however, the AIFM has to demonstrate that the leverage limits set for each AIF are reasonable and that the AIF complies with these limits at all times. CYSEC may impose limitations on the use of leverage if necessary.

5 Disclosure of Information

5.1 What public disclosure must the Alternative Investment Fund make?

There is no public disclosure that the AIF must make, except in cases where the AIF is listed on the stock exchange or other regulated markets.

Please see question 3.2 above with regard to the disclosure obligations on investors of AIFs as per section 30 of the AIFM Law.

5.2 What are the reporting requirements in relation to Alternative Investment Funds?

The reporting requirements of an AIF as per section 74 of the AIF Law, are that the external manager of the AIF or the self-managed investment company shall prepare and submit to the Securities and Exchange Commission: (a) the prospectus of the AIF and any amendments thereto; (b) the annual report of the AIF for each fiscal year; and (c) the half-yearly report of the AIF for the first six months of the fiscal year.

The annual and half-yearly report of the AIF shall be communicated to CYSEC and made available to the investors at the points of distribution of its units within the following deadlines: (a) six months from the end of the fiscal year, in the case of the annual report; and (b) two months from the end of the first six-month period, in the case of the half-yearly report.

5.3 Is the use of side letters restricted?

There are no restrictions on the use of side letters.

6 Taxation

6.1 What is the tax treatment of the principal forms of Alternative Investment Funds?

In general, there are no specific provisions regarding the taxation of AIFs under the Cyprus tax laws. AIFs that are formed as private limited liability companies and are managed and controlled from Cyprus, are taxed like any other Cyprus tax-resident company.

Cyprus-resident companies are subject to a flat Income Tax rate of 12.5% on their taxable profit.

The tax treatment on the main source of income of AIFs is detailed below:

■ Dividend

Dividend income will be taxed under Income Tax in Cyprus only if the payment of the dividend is a tax-deductible expense for the company paying the dividend under the laws of the country in which it is resident. Such dividends will be taxed as normal business income subject to Income Tax and will be exempt from the Special Contribution for Defence (“SCD”).

Dividend income will be exempt from SCD when it is derived from trading activities (directly or indirectly) or the underlying tax rate is significantly greater than the tax rate in Cyprus.

■ Interest

Interest earned during the ordinary course of business is taxable under the Income Tax Law at 12.5% and is exempt from SCD.

■ Capital Gains Tax

Profits from the disposal of shares and other financial instruments are exempt from tax.

There is no withholding tax on interest and dividend payments made to non-Cyprus tax residents as a result of Cyprus law and the double tax treaties which Cyprus has entered into.

AIFs are exempt from the provisions of the Stamp Duty Law.

6.2 What is the tax treatment of the principal forms of investment manager/adviser?

Investment managers and advisers are liable to tax at the rate of 12.5%, provided they are Cyprus tax-resident entities. There are no special provisions under Cyprus tax law regarding the aforementioned.

6.3 Are there any establishment or transfer taxes levied in connection with an investor's participation in an Alternative Investment Fund or the transfer of the investor's interest?

No establishment or transfer taxes are levied in Cyprus in connection with an investor's participation in an AIF or the transfer of the investor's interest.

6.4 What is the tax treatment of (a) resident, and (b) non-resident investors in Alternative Investment Funds?

The tax treatment of a resident investor is different from that of a non-resident investor.

A non-resident investor is not subject to any tax in Cyprus unless the profit or gain arises from a direct or indirect interest in immovable property located in Cyprus. In such case, the profit or gain will be subject to Cyprus Capital Gains Tax.

A Cyprus tax resident (company or individual) will be liable to tax in Cyprus on the whole income generated. Profits from the disposal of shares will be exempt from any tax. Dividends distributed to Cyprus tax residents are subject to the Social Defence Contribution at 3% (as opposed to 17%, which normally applies).

6.5 Is it necessary or advisable to obtain a tax ruling from the tax or regulatory authorities prior to establishing an Alternative Investment Fund?

There is no requirement to obtain a tax ruling in Cyprus before the establishment of an AIF, but it is common practice to do so.

6.6 What steps have been or are being taken to implement the US Foreign Account and Tax Compliance Act 2010 (FATCA) and other similar information reporting regimes?

Cyprus and the US signed an Intergovernmental Agreement ("IGA") (Model 1) on 2 December 2014 in order to implement the US Foreign Account Tax Compliance Act ("FATCA") in Cyprus.

Under the IGA, Cypriot Financial Institutions having a reporting obligation are required to collect and disclose details of their US-reportable accounts to the Cypriot Competent Authority (the Ministry of Finance). The Cypriot Competent Authority will then forward this information to the US Competent Authority (the Internal Revenue Service – "IRS").

The IGA provides that Cypriot Financial Institutions must collect certain information relating to depository and custodial accounts held by US persons, certain interests in investment entities held by US persons, and certain insurance policies or annuities that have "cash value" and are held by US persons.

6.7 Are there any other material tax issues?

There are no other material tax issues that need to be taken into consideration.

6.8 What steps are being taken to implement the OECD's Action Plan on Base Erosion and Profit-Shifting (BEPS), in particular Actions 6 and 7?

Various Actions of the BEPS report will be adopted by the EU, as on 28 January 2016 the European Commission presented its anti-tax-avoidance package. One of the core pillars of the Commission's agenda is an anti-tax-avoidance directive, also known as the EU BEPS Directive. As Cyprus is a member of the EU, upon approval of the proposed rules, the proposed changes will need to be implemented by Cyprus in its national legislation.

Cyprus has already announced its intention to amend its regime further, in order to comply with Action 5.

In addition, Cyprus has recently announced its intention to further amend its regime to comply with Action 13. Cyprus does not have any detailed transfer pricing rules in its national legislation. Consequently, detailed transfer pricing rules, including transfer pricing documentation, are expected to be introduced in Cyprus' national legislation in 2016.

Actions 6 and 7 will be adopted through Action 15 (a multilateral instrument to modify bilateral tax treaties). Cyprus has already set up a committee that will look at the issue and identify the actions needed to be taken once the multilateral instrument process is completed. It is anticipated that the effects of the multilateral instrument will be felt in 2018 or 2019, depending on when Cyprus adopts this instrument.

7 Reforms

7.1 What reforms (if any) are proposed?

Please refer to question 6.8 above.

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Advocate

Mrs. Christina Sofocleous was born in Moscow Russia in 1990. She graduated in Law with Honours from the University of Kent and she obtained her LL.M. with Merit at University College London. She then completed the Russian language course at Peoples' Friendship University of Moscow. Mrs. Sofocleous was admitted to the Cyprus Bar in 2014. In March 2015, she obtained the advanced Cyprus Securities and Exchange Commission Certification and registered in the Public Register of Certified Persons.

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Mrs. Antigoni Hadjiyianni was born in Nicosia, Cyprus in 1983. She graduated from York University in Toronto, Canada with a degree in Administrative Studies with Specialized Honours in Accounting in 2006. She then worked for four years in KPMG Limassol, Cyprus where she also qualified as a Chartered Accountant in 2009. After working for two years as a financial controller in a small company, Mrs. Hadjiyianni joined Andreas M. Sofocleous & Co LLC in 2012 as a Tax Manager. She has experience in the provision of tax advice, tax compliance and international tax planning.

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Andreas M Sofocleous & Co LLC is one of the most successful Corporate and Commercial law firms in Cyprus. Headquartered in Limassol, and with offices in Eastern Europe and the UK, the firm provides legal services for individuals and companies at both the national and multinational level across a wide range of industries, dealing with mergers and acquisitions, cross-border transactions, joint ventures and intellectual property licensing, as well as company formation and management and other business arrangements.

Since 1995 our firm has been working successfully in the market of legal and consulting services. The skills and experience of our partners and staff, along with the use of modern technology, enable us to deliver high quality and rapid results for the benefit of our clientele, which include multinational corporations, public companies, small and medium-sized enterprises, as well as individuals.