

Cyprus Investment Funds: Everything you need to know



By CX Financia, January 2023

An investment fund, also known as a **collective investment undertaking (UCI)**, is a financial organisation that collects savings from several investors. It is a flexible structure that makes it easier to invest in various initiatives, including those that aim to generate returns above the market, buy shares in early-stage start-ups, and projects that address climate change. As a result, it is a crucial component of the worldwide flow of capital and obtaining an investment fund license is a big step towards realising a particular investment strategy.

A typical fund structure will have a Fund Manager assigned to enforce the fund's investment strategy and manage the distribution of funds capital between the invested assets of the fund. There are two broad categories of funds, Undertakings for Collective Investment in Transferable Securities (UCITs) and **Alternative Investment Funds (AIFs)**.

What is the difference between a UCIT and AIF Fund?

UCITs, as the name denotes, mainly invest in "safe" liquid assets like bonds, shares, debt etc., making them more suitable for retail investors. On the other hand, AIFs can invest in various assets, limited only by their investment strategy, making them ideal for professional or well-informed investors. Only under certain conditions are allowed to accept retail investors. In general, UCITs invest in low-risk, low yield investments, whereas AIFs prefer high-risk, high-yield investments.

What is an AIF Fund?

An AIF in a Collective Investment Undertaking:

- Which raises capital from a number of investors intending to invest it following a defined investment policy for the benefit of those investors;
- Which does not require authorisation as UCITS.

What are the Types of AIFs structures in Cyprus?

There are three types of Alternative Investment Funds that can be set up in Cyprus.

1. the Alternative Investment Fund of an unlimited number of investors (AIF)
2. the Alternative Investment Fund of Limited Number of Investors (AIFLNP), and
3. the Registered Alternative Investment Fund (RAIF).

Overview of AIFs structures

It is important to note for AIFLNP, investors may not exceed the total number of 50, whereas for AIFs and RAIFs number of Investors can be unlimited.

AIFs or RAIF follow similar legal and regulatory principles whereby they are both considered a Fund with its shares redeemed or repurchased directly or indirectly by its assets following an application of its shareholders as defined in the Fund's Prospectus.

Its capital is increased by the issue of new shares, whereas its capital is decreased by the redemption or the repurchase of the old ones. Hence it adopts the Variable Capital Investment Company statutes. The value of its shares is reflected by the net asset value (NAV) of its assets.

AIF's are marketable to qualified, professional or institutional investors internationally and within the EU member States (full pass-porting rights within the EU).

Highlights of AIF structures

Let's see the characteristics of each AIF (Alternative Investment Fund)

Alternative Investment Fund with Unlimited Number of Persons (AIF)

- May be marketed to "retail", "well-informed", and/or "professional investors."
- Freely transferable investor shares
- Must appoint a Depositary
- It can be listed on a recognised stock exchange, and AIFs marketed to retail investors can be traded.
- Subject to minimum capital requirements of €125,000 or €300,000 if a self-managed fund
- Depending on the investor type and overall investment policy, it may be subject to certain investment restrictions.



Alternative Investment Fund with Limited Number of Persons(AIFLNP)

- May be marketed only to "well-informed" and/or "professional investors."
- Cannot exceed the total number of 50 investors/unitholders
- Freely transferable investor shares, with the condition that their transfer does not result in the AIF having more than 50 investors
- In some cases, it may not be required to appoint a licensed manager or a custodian
- Assets under management do not exceed the AIFMD thresholds of €100 million (including leverage) or €500 million (5-year lock-up period without leverage)

Registered Alternative Investment Funds (RAIFs)

- A RAIF is similar to AIF; however, it is registered and regulated under the responsibility of the AIFM hosting it, whereby all operational and marketing efforts are conducted under the liability of the AIFM as a European fully passported Fund Management Structure.
- RAIFs are registered within one month from submission of the relevant notification package to CySEC to confirm the RAIF's registration and allow capital raising.

What Is an Umbrella Fund?

An **umbrella fund** is an investment fund that contains multiple sub-funds.

An umbrella AIF is a **single legal entity** and no separate fund rules or instruments of incorporation are drawn up, nevertheless, the rights of unitholders and the claims of creditors or the liabilities arising in connection to the establishment, operation, liquidation and dissolution of the investment compartment are limited to the assets of that investment compartment.

It is crucial to emphasise that each compartment or sub-fund is wholly isolated from the Umbrella Fund and the other Sub-Funds and is ring-fenced. Each compartment may have a different approach to investing. Investor rights in each case are limited to the assets of the respective compartment, and each compartment may be liquidated independently. It is also crucial to note that each compartment's setup and maintenance costs are lower than those of individual funds.

If funds intend to employ various investment techniques, they might be set up as umbrella funds. An umbrella fund can lower investment risk by segmenting its asset pool into different compartments and applying other investing techniques in each compartment. Investors have some flexibility to change their strategies thanks to umbrella funds.



So, what does capital raising mean in simple terms?

It's the process a business goes through in order to raise money, so the business can get off the ground, expand, or transform in some way.

In other words, it is the commercial activity of taking direct or indirect steps by an undertaking, or a person, or entity, acting on its behalf (typically, the AIFM) to procure the transfer or commitment of capital by one or more investors to the undertaking, to invest, following a defined investment policy.

It is important to note here, when capital is invested in an undertaking by a member of a pre-existing group, for the investment of whose private wealth the undertaking has been exclusively established, this is likely to be outside the scope of raising capital.

The fact that a pre-existing group member invests alongside investors who are not members of a pre-existing group should not mean that the condition for "raising capital" is not met. All investors should have complete access to AIFMD rights whenever a situation like this does occur.

Is there a minimum number of Investors required to raise capital in a fund?

An undertaking that is not prevented by its national law, the rules or instrument of incorporation, or any other provision or arrangement of binding legal effect, from raising capital from more than one investor should be regarded as an undertaking that raises capital from several investors. This should be the case even if it has, in fact, only one investor.

An undertaking that is prevented by its national law, the rules or instrument of incorporation, or any other provision or arrangement of binding legal effect, from raising capital from more than one investor should be regarded as an undertaking that raises capital from several investors if the sole investor:

1. Invests capital which is has raised from more than one natural or legal person with a view to investing it for the benefit of those persons; and
2. Consists of an arrangement or structure which, in total, has more than one investor for the purpose of the AIFMD.



Who can invest in the Fund-Eligible Investors?

- **AIF:** Unlimited Investors, Retail, Professional or Well-informed – unless established as a private company.
- **AFILNP:** Up to 50 Investors, Professional or Well-informed only
- **RAIF:** Unlimited Investors, Professional or Well-informed only – unless established as a private company.

AIF's under the Alternative Investment Funds Law



What are the categories of Investors?

- **Professional Investor:** An investor is considered a professional client with the experience and expertise to make his/her own investment decisions and assess the risks involved. To be considered a professional client, the investor must comply with the criteria prescribed in the Markets in Financial Instruments Directive (MiFID).
- **Well-informed Investor:** An investor which is not a professional investor and fulfils the following conditions is considered as Well-informed Investor:
 - (i) must confirm in writing that they are a qualified investor aware of the risks involved with an investment in the relevant AIF and
 - (ii)(ii) makes an investment of a minimum of €125,000 or has been evaluated by a licensed bank/credit institution, an authorised investment firm or an authorised Management Company that they have the expertise, experience and knowledge in evaluating the suitability of an investment opportunity.
- **Retail Investor:** An investor who does not meet the requirements listed above.

How CX Financia can help you

The CX Financia team comprises professionals with specialist knowledge in setting up, structuring and promoting licencing Investment Funds and Fund Managers with the Regulators. We provide services to our clients and business partners, including licencing for investment funds, administration of funds, internal audit, risk management, compliance, and regulatory reporting services.

We assist you in selecting the best form and structure for establishing a new fund by considering your needs, the company structure, and the regulations. We quickly create the relevant paperwork for the Investment Fund's incorporation and offer assistance when dealing with CySEC's pre- and post-authorisation processes.

We will be happy to answer your questions and work with you. For additional information, please send us an email at info@cxfinancia.com.

