

Close-Ended Investment Companies in the Isle of Man



The Isle of Man's low tax status, political and economic stability and proximity to the key markets of Europe make it a compelling and cost-effective alternative for the domicile of investment funds. With a wide range of service providers and a sophisticated professional and banking infrastructure, the Island offers a solution for all promoters of investment funds. The Island prides itself on its "can-do" business environment and the close co-operation between public and private sectors has resulted in a flexible regime that meets the expectations of promoters and the concerns of key investors. This briefing note sets out the Island's proposition for closed-ended investment companies.

Constitutional Position

The Isle of Man is a self-governing dependency of the British Crown. It does not form part of the United Kingdom. By long-established constitutional convention, the Isle of Man has complete autonomy in relation to domestic affairs, including taxation and business law.

The Island is not a member state of the European Union. Under Protocol 3 to the Act of Accession, whereby the United Kingdom became a member state, EU rules only apply to the Isle of Man in relation to a limited range of matters. Accordingly, EU directives on tax harmonisation, company law and financial services do not apply in the Isle of Man.

Tynwald, the Island's parliament, has been in existence for over 1,000 years and is the world's oldest continuously functioning parliament. The

Island also has an independent Court system, including a High Court and a locally-based appellate court; the final court of appeal for the Isle of Man is the UK Privy Council.

The Island is a common law jurisdiction and its legal traditions draw heavily on those of England; English case law is of high persuasive authority in the Isle of Man. This legal stability gives the jurisdiction the commercial legal certainty long associated with the English legal system, combined with the flexibility of an international finance centre.

Regulatory Environment

The Isle of Man has a well-founded reputation as a premier jurisdiction in terms of regulation, achieving a balance between, on the one hand, providing a business friendly environment and, on the other hand, meeting international standards of financial supervision. A number of independent assessments of the Island's regulatory framework have been conducted which verify the Island's status. The most comprehensive of these was the assessment carried out by the IMF which was completed in November 2003, but they have also included the positive assessment by the Financial Stability Forum of May 2000 identifying the Island as a 'category 1' jurisdiction, and confirmation as a co-operative jurisdiction from the FATF in 2000. The IMF is due to publish a further report following an inspection visit to the Island in September 2008. It has been reported that the draft copy of the IMF report praises the Island's financial regulation, financial stability and anti-money laundering legislation.

The Review of the British offshore financial centres commissioned by the Chancellor Alistair Darling and undertaken by Michael Foot is currently taking place. The focus of the review is working with the financial centres to analyse their assessment of the risks flowing from the current and forecast macro-economic environment. The visits and discussions undertaken so far have been fact finding. The review continues and Mr Foot is expected to deliver his final report in the last quarter of 2009. The Island's Chief Minister, Tony Brown, recently stated that no specific concerns about the Isle of Man have been identified so far. The Island was able to provide the review with information about its internationally recognised standards on regulation and tax as well as an overview as to how its diverse economy is performing during the global downturn. The Island's progress on signing 14 tax information exchange agreements, placing it firmly on the OECD's 'white list' of jurisdictions that have substantially implemented internationally agreed tax standards, was welcomed by the review.

The Isle of Man has worked hard to ensure that it is not regarded as a tax haven with harmful tax practices and its inclusion on the most recent OECD white list in April 2009 is recognition of its efforts. It also demonstrates that the Isle of Man is a co-operative and transparent international financial services centre which takes its international responsibilities very seriously.

By being pro-active and entering into tax information exchange agreement with other jurisdictions, the Island is currently ahead of the game and a number of its competitors.

Regulation of fund managers and administrators, and of collective investment schemes, is undertaken in the Isle of Man by the Financial Supervision Commission or "FSC". As well as a framework for the regulation and supervision of financial services providers, the Island has adopted extensive regulatory measures to prevent money laundering and the financing of terrorism.

Regulation of closed ended investment companies

Isle of Man law draws a fundamental distinction between "open-ended investment companies" and

"closed-ended investment companies". An open-ended investment company is a corporate vehicle that provides for investment risk spreading **and** provides investors with a right of exit (e.g. by a redemption of their shares).

An open-ended investment company is regarded as a "collective investment scheme" for the purposes of Isle of Man law. Collective investment schemes, or funds, are subject to varying degrees of regulation in the Isle of Man depending on the category into which they fall. If an Isle of Man corporate vehicle does not provide its investors with a right of exit as described above then, even if it is an investment vehicle aimed at spreading investment risk, it will not be an open-ended investment company and therefore will not be subject to "fund" regulation in the Isle of Man. Such a closed-ended investment company is treated in the same way as any other company for regulatory purposes.

As a result of this approach there are a number of important advantages to using an Isle of Man closed-ended investment company:

- no regulatory pre-approval requirements for launch in the Isle of Man
- no regulatory fees in the Isle of Man
- no requirement for a licensed fund manager or administrator to be appointed
- no prescriptive requirements as regards board composition
- no requirement for a separate custodian
- no restrictions on asset classes, investment strategy or leverage
- no prescriptive rules about permitted investors or minimum subscription requirements

Companies – Traditional and Modern

The Island's Companies Act 2006 means that promoters wishing to use an Isle of Man company may choose between using a vehicle incorporated under the new legislation or a traditional company established under the Companies Act 1931.

Companies Act 2006

This Act created a new stand-alone corporate vehicle, which represents the gold-standard for international special purpose vehicles. Minimal

administrative requirements, flexible capital structure and limited disclosure requirements are counter-balanced by the Island's well-respected regime for the regulation and supervision of registered agents. Companies incorporated under this Act are not subject to prescriptive prospectus requirements.

Companies Act 1931

For those whose tastes are more conservative, the Island's long-established conventional companies incorporated under the Companies Act 1931 draw heavily on English legislative traditions, but without the more prescriptive requirements associated with companies incorporated in metropolitan jurisdictions. This Act does contain prospectus requirements but these are not prescriptive and are also subject to a wide range of exemptions in relation to private placements and restricted institutional offerings.

AIM Market`

A listing or admission to a trading facility is often a driving force behind the establishment of a closed-ended investment company. Isle of Man companies are suitable for listing on many recognised investment exchanges. In recent years the AIM Market has proved popular with both investors and promoters and Isle of Man companies have been the vehicles of choice for quality international AIM offerings. In 2007 the Isle of Man has 15 of the top 100 AIM companies – more than any other jurisdiction outside the UK.

Administration Requirements

Although there is no requirement for a closed-ended investment company to appoint a regulated fund administrator, the use of an Isle of Man corporate vehicle will require an Isle of Man corporate services provider to provide formation and ongoing compliance services. These are regulated activities in the Isle of Man and there are a wide range of service providers available.

Taxation

The Isle of Man offers a tax neutral environment for hedge fund operations. There are no capital or inheritance taxes in the Isle of Man and stamp duty does not apply. In 2006 the Isle of Man introduced a

zero rate of corporate tax for most taxpayers. This means that a closed-ended investment company will benefit from a zero rate of income tax. It follows that the Island no longer has a "tax exemption" regime and therefore investment vehicles need not go through the process for applying for exemption on an annual basis; nor are such vehicles subject to the risks associated with inadvertently ceasing to qualify for exempt status and the adverse taxation consequences that follow.

Some fees levied by functionaries based in the Isle of Man in respect of services to exempt schemes are subject to value added tax in the Isle of Man.

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