

Isle of Man Exempt Schemes



The Isle of Man has a full suite of fund options, but the exempt scheme is a flexible and low cost vehicle that is wholly outside the scope of fund regulation in the Isle of Man and is suitable for use in relation to start up private funds. This briefing note describes the key features of the exempt scheme.

Flexibility of Legal Form

The Isle of Man offers a full range of vehicles for use as fund structures. **Corporate vehicles** can be established either as traditional companies or under the Island's new Companies Act 2006, which offers a stand-alone vehicle with minimal administrative requirements, flexible capital structure and limited disclosure requirements.

Both types of company can be established as **protected cell companies**. PCCs are ideal for use both in multi-class/single manager structures and in multi-manager offerings.

Isle of Man **limited partnerships** offer tax transparency and a flexible legal framework. A limited partnership may return capital prior to the winding up of the partnership and, in order to provide comfort to investors, the statute sets out a "white-list" of activities that will not result in limited partners being regarded as involved in the management of the partnership thereby prejudicing their limited liability status.

The Isle of Man follows England in its trust law. As a fund vehicle, the **unit trust** arrangement offers huge flexibility and the security of knowing that the arrangements are not a matter of public record.

Regulatory Status

Funds in the Isle of Man are generally subject to regulation commensurate with the category into which they fall. Regulatory requirements may include the need to appoint appropriately licensed functionaries (such as an administrator, custodian and/or auditor), requirements as regards the preparation and content of an offering document, investor certification obligations, minimum subscription levels etc.

Exempt schemes are an exception to these requirements. If the criteria for exempt scheme status are met, then the Isle of Man Financial Supervision Commission or "FSC" regards the arrangements as being wholly outside the scope of fund regulation.

Criteria for Exemption

The criteria for exempt scheme status are two in number. The first relates to the means of distribution; the second relates to the diversity of the investor base. In detail, the criteria are as follows:

- interests in the exempt scheme may not be offered (either by or on behalf of the fund or any investor) to the public or any section of it (i.e. the fund may only be offered on a private "friends and family" basis) and a prohibition to this effect must be included in the constitutional documents of the fund; and
- the exempt scheme must have fewer than 50 investors. This is a question of fact and

represents an ongoing requirement.

As an exempt scheme grows there may be good reasons why it would become necessary or appropriate to make arrangements for public offerings or to exceed the investor limit. In these circumstances it is a straightforward process to convert an exempt scheme into a higher category of scheme such as a Specialist Investment Fund or “SIF” or a Qualifying Investor Fund or “QIF”.

Administration Requirements

Although there is no requirement for an exempt scheme to appoint a regulated fund administrator, the use of an Isle of Man fund vehicle will require an Isle of Man fiduciary 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.

If the use of a regulated fund administrator is regarded as necessary or appropriate, there are also a number of experienced fund administration outfits based on the Isle of Man, from the global names to boutique providers. Overseas administrators may also be used in relation to an exempt scheme.

Asset Management

As an unregulated vehicle, there are no restrictions on asset classes, trading strategies or leverage for an exempt scheme. Accordingly, the exempt scheme is suitable for any type of investment fund from traditional, long-only equity funds to hedge fund strategies and from private equity to property investment.

An exempt scheme can obtain investment advice from any source.

The Isle of Man is unique among international finance centres in continuing to have the capacity to attract and accommodate real business operations. The FSC has announced certain new investment business licence categories and refinements to its licensing policy designed to attract hedge fund management and related operations to the Island.

Governance and Board Position

There are no prescriptive requirements regarding the composition of the board of directors of an exempt scheme.

No Regulatory pre-approvals

There is no requirement for any pre-approval to be sought from the FSC or any other body to launch an exempt scheme.

Fees

No application fee is payable for the establishment of an exempt scheme. However, an annual fee of £500 is payable to the FSC. In addition, a modest annual corporate charge is payable in relation to the use of an Isle of Man corporate vehicle.

Investors

Interests in an exempt scheme may not be offered to the public. Therefore investment may only be accepted on a private basis from “friends and family”. As explained above, an exempt scheme is also subject to a limit on investor numbers. The fund cannot accept more than 49 investors and artificial arrangements for evading this limit are not effective.

No Minimum Subscription

As an unregulated vehicle, there is a no prescribed regulatory minimum initial investment requirement for an exempt scheme.

Taxation

The Isle of Man offers a tax neutral environment for fund management operations. There are no capital taxes and the Island has a zero rate of corporate tax for most taxpayers. This means that a corporate fund vehicle will benefit from a zero rate of income tax, as will any fund management or administration business based in the Isle of Man. 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.

Placing Documents

As an unregulated, private vehicle, there are no mandatory requirements relating to the preparation of a prospectus or offering document for an exempt scheme.

Clearly though, even in the context of a private placement, it is prudent to ensure that there is a clear statement of the terms and statements upon which investors may base their decision to invest.

Accordingly, the preparation of a fairly detailed private placement memorandum is common.

Flexible Custody Arrangements

There are no prescriptive requirements for the appointment of a custodian in relation to an exempt scheme. The fund is free to implement whatever arrangements are appropriate for holding its assets, whether through the use of a third party, direct ownership or special purpose vehicles.

No Mandatory Audit

There are no mandatory requirements relating to the audit of the financial statements of an exempt scheme, although the Isle of Man does host offices of all the major accountancy and audit practices should an audit be regarded as appropriate.

Should you have any questions or requests for further information please contact:

Simon Harding

Partner

sharding@applebyglobal.com

Gill Crennell

Senior Associate

gcrenell@applebyglobal.com

Bahrain

Bermuda

British Virgin Islands

Cayman Islands

Hong Kong

Isle of Man

Jersey

London

Mauritius

Seychelles

Zurich