Alternative Investment Funds (AIFs) and Managers (AIFMs)

Following the introduction of the EU’s Alternative Investment Fund Management Directive (AIFMD) that regulates both alternative fund managers and the promotion of alternative funds within the EU, Malta’s fund industry is entering a new phase in its development.

The AIFMD will act as a catalyst for further expansion in the coming years, attracting non-EU managers to set up shop in Malta. In addition to the newly introduced Alternative Investment Fund (AIF) regime that allows managers to launch funds under the AIFMD, the island’s successful Professional Investor Fund (PIF) regime was retained offering fund promoters diverse structuring opportunities.

What is the AIFMD?
The Alternative Investment Fund Managers Directive is a 2011 EU Directive regulating the marketing or the management of funds (other than UCITS) within the EU. The AIFMD and its implementing regulation, subjects fund managers within scope to an authorisation or registration requirement as well as a number of ongoing obligations including in relation to investor disclosure, regulatory reporting, appointment of a depositary and limits on remuneration. The AIFMD came into effect in all EU Member States in 2013. The AIFMD creates a passport for EU AIFMs authorised under the directive to market units or shares in their EU AIFs to professional investors in all EU Member States without needing to comply with any further local requirements. The directive could potentially introduce a passport for non-EU AIFMs/AIFs as early as 2015.

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The remit of the AIFMD is particularly wide due to its all-encompassing definition of AIFs, as it covers all legal forms of AIF, whether open or closed-ended and applies whatever the asset class invested in.

AIFs are collective investment undertakings which:
• raise capital from a number of investors with a view to investing it in accordance with a defined investment strategy
• do not require authorisation under the UCITS Directive2.

Therefore, hedge funds, private equity funds, real estate funds, venture capital funds and others all fall within the scope of the AIFMD.

Authorisation: All AIFMs and AIFs (if self-managed) which do not fall out of scope or under any exemptions as set out in the directive, must be authorised by their home EU member state (where they have their registered office).

Initial Capital Requirements and Own Funds:
• Self-managed AIFs €300,000
• Self-managed PIFs €125,000
• AIFM €125,000 but if the portfolio value of the AIFMs managed by the AIFM exceeds €250 million, an 0.02 per cent of the amount exceeding €250 million is required. However, this amount shall not exceed €10 million and either 0.01 per cent of the portfolio value of the AIF or professional indemnity insurance cover.

Required Information on each AIF:
• Information on the AIF’s investment strategies
• Information on where the master AIF is established if the AIF is a feeder AIF
• The rules or instruments of incorporation of the AIF
• Information on the arrangements made for the appointment of the custodian
• Additional information in relation to information to be disclosed to investors

Passporting: The AIFMD provides a harmonised framework for the cross-border management and marketing of AIFs within the EU via an AIFM passport.

The Custodian: An AIF managed by an AIFM is required to appoint a single independent custodian for each AIF under management. Under certain conditions the MFSA may allow the appointment of a Category 4b custodian licensed under a lighter version of the custody framework open to fund administrators and other licensed service providers. AIFMs and prime brokers are specifically prohibited from acting as custodians. However, the prohibition is lifted in the case of prime brokers where measures have been taken to functionally and hierarchically separate the two functions and where no potential conflicts of interest arise. Until July 2017, the entity appointed as Custodian of an AIF need not be a Maltese entity but may be a credit institution established in any other EU Member State.

Eligible Custodians:
• a Maltese credit institution
• a branch established in Malta of a credit institution authorised in an EU or EEA Member State
• a branch in Malta of an overseas credit institution which is subject to prudential requirements at least equivalent to the requirements applicable to Maltese credit institutions
• a Maltese company which is wholly owned by a credit institution (provided that the liabilities of such company are guaranteed either by a Maltese credit institution or by an overseas credit institution which is subject to prudential requirements at least equivalent to the requirements applicable to Maltese credit institutions)
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- a Maltese company which is wholly owned by a Maltese or foreign institution or company which the MFSA deems to provide unit-holders with protection equivalent to that provided by the entities fulfilling the requirements listed above (provided that the liabilities of such company are guaranteed by the holding institution/company and provided that the holding institution/company has paid-up share capital of €5m or its equivalent in foreign currency
- an investment firm in Malta or a branch of an investment firm established in another Member State or EEA State subject to capital adequacy requirements in accordance with the Capital Adequacy Directive and authorised under MiFID and which also provides the ancillary service of safekeeping and administration of financial instruments for the account of clients in accordance with MiFID

At the end of 2013, Malta had seven MFSA-licenced custodians. However, by the end of 2014 regulator MFSA reported it was seeing an increase in applications from both new international custodians as well as existing Malta-based entities looking to expand their activities.

Tax Benefits for a Malta-domiciled AIF:
- an exemption from income tax and capital gains tax at both the fund level and at a non-resident investor level as long as more than 85% of the value of its assets is situated outside Malta
- investment income received by the Fund is not subject to any withholding tax

The De Minimis Regime
The AIFMD framework provides for a lighter or de minimis regime for small AIFMs.
De minimis AIFMs are managers which, whether directly or indirectly, manage portfolios of AIFs whose assets under management collectively do not exceed the following amounts:
- €100m or
- €500m for AIFMs managing only unleveraged AIFs with no redemption rights exercisable within 5 years from the date of initial investment in each AIF

While AIFMD allows Member States to choose merely to register rather than authorise de minimis AIFMs, the MFSA’s policy in the interest of investors is to require authorisation as de minimis Category 2 Licence Holders.

Once authorised, a de minimis AIFM will be exempt from complying with the provisions of the AIFMD with the exception of certain reporting requirements towards the MFSA such as:
- the investment strategies of the AIFs under management
- the main instruments in which the AIFs under management are trading
- the principal exposures and most important concentrations of the AIFs under management.

Any AIFM whose assets under management fall below the above thresholds may choose to opt in to the AIFMD framework. This would render it subject to all the obligations applicable to full-scope AIFMs, but would also enable it to make use of the EU passporting rights deriving from the AIFMD.

Key Benefit for AIFMs:
Approval by any EU financial services regulator will be sufficient for all other EU regulators to allow a fund to trade across the EU. Only fully compliant managers will get regulatory approval and have open access to all of Europe’s 400 million consumers.

AIFM Management Functions:
- Portfolio and risk management
- Administration duties, such as legal and fund management accounting services, customer inquiries, valuations and pricing including tax returns, regulatory compliance monitoring, maintenance of unit/share register, distribution of income, unit/share issues and redemptions, contract settlements including certificate dispatch and record-keeping
- Marketing
- Activities related to the assets of AIFs, such as services necessary to meet the fiduciary duties of the AIFM, facilities management, real estate administration activities, advice to undertakings on capital structure, strategy, services relating to mergers and the purchase of undertakings and other services connected to the management of the AIF and the companies and other assets in which it has invested in

License Timeframe:
Three months. Successful applicants will also be entered in a central register kept by the European Securities and Markets Authority (ESMA), with authorisation valid in all EU Member States.

Remuneration:
The MFSA has announced that although it has implemented ESMA’s guidelines on remuneration policies, it has decided not to transpose ESMA’s guideline that AIFMs should be required to impose equivalent remuneration policies and restrictions on its sub-managers and other delegates.

Alternative Investment Fund Managers (AIFMs)
The AIFMD requires all EU AIFMs to be authorised by the regulatory authority of the Member State in which they are incorporated and, subsequently to authorisation, to comply with a number of on-going obligations. In Malta, the relevant regulatory and supervisory body is the MFSA.

Required Information on AIFMs
- Information on the qualifying shareholders and on the amount of their holdings
- The organisational structure of the AIFM
- Information on the AIFM’s remuneration policies
- Information on any arrangements made on delegation and sub-delegation

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