

UK investment funds overview

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Introduction

In this practice note, [Neil Simmonds](#), a partner in the Financial Services group at Simmons & Simmons LLP and [Martin Shah](#), a partner in the firm's Corporate Tax group, provide an overview of the permissible structures for UK investment funds. This includes discussion of collective investment schemes (CIS), authorised and unauthorised unit trusts, open-ended investment companies (OEICs), investment companies with variable capital (ICVCs), investment trusts, limited partnerships (including private fund limited partnerships (PFLPs)), authorised contractual schemes (ACS), and the various categories of FCA-regulated schemes, namely UCITS schemes, non-UCITS retail schemes (NURS), qualified investor schemes (QIS), and European long-term investment funds (ELTIFs).

This practice note was originally published by Practical Law Company, who have agreed to Simmons & Simmons making it available on [simmons-simmons.com](https://www.simmons-simmons.com).



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Introduction to UK investment funds

Investment funds benefit both those that manage them and (hopefully) those that invest in them.

From an investor's point of view, the principal advantage of investing through a fund is the collective nature of the vehicle: the ability to pool its investment in a fund that is professionally managed. This gives an investor the opportunity to benefit from diversification and economies of scale that it would usually not be able to achieve individually. The investor also benefits from the manager's experience, expertise and access to research.

From a manager's point of view, of course, funds are an attractive way in which a manager can package up its expertise and services in return for a fee.

The basic fund structures commonly adopted in the UK are:

- Unit trusts (see [UK authorised and unauthorised unit trusts](#) below)
- Open-ended investment companies (OEICs) (see [UK authorised ICVCs](#) below)
- Authorised contractual schemes (ACS) (also referred to as tax transparent funds (TTFs)) (see [UK authorised contractual schemes \(ACS\)](#) below)
- Investment trusts (see [UK investment trusts](#) below)
- Limited partnerships (see [English \(unauthorised\) limited partnerships](#) below).

Other than investment trusts, each of these structures is capable of constituting a [collective investment scheme](#) (see [What is a collective investment scheme?](#) below) and all are discussed further in the sections below.

Assets normally held by a fund include shares or bonds issued by companies and, although less common, other asset classes such as real property, commodities (for example, precious metals) and, increasingly, derivatives (for example, futures, options and contracts for differences (CFDs)).

The role of a fund's investment manager is to take investment decisions for the fund, that is, deciding which assets to buy and sell and when to do so. The role of a fund's trustee, custodian or depositary (the various names given to the party fulfilling an asset safekeeping function) is to hold legal ownership of the fund's assets and to safeguard the interests of the fund's unitholders or shareholders.

The only fund structures capable of being authorised for promotion to retail customers in the UK, and that are regulated by the FCA, are:

- Authorised unit trusts (AUTs) (see [What is an authorised unit trust?](#) below).
- Investment companies with variable capital (ICVCs, often referred to as OEICs) (see [UK authorised ICVCs](#) below)
- European long-term investment funds (ELTIFs) (see [What is an ELTIF?](#) below)
- ACS (see [UK authorised contractual schemes \(ACS\)](#) below), although these are subject to a minimum investment of £1 million

The proposed manager and trustee of an AUT, the proposed authorised corporate director (ACD) and depositary of an authorised OEIC, the proposed manager and depositary of a co-ownership ACS, the proposed manager of an ELTIF as well as the ELTIF itself or the proposed general partner and depositary of a limited partnership ACS must apply to the FCA for permission to establish such a fund.

For details of the procedure for authorisation of unit trusts, OEICs, ELTIFs, and ACS, see [What is an authorised unit trust?](#), UK authorised ICVCs, [What is an ELTIF?](#) and [UK authorised contractual schemes \(ACS\)](#) below.

What is a collective investment scheme?

Definition

Section 235(1) of the Financial Services and Markets Act 2000

A [collective investment scheme](#) (CIS) is defined in [section 235\(1\)](#) of the Financial Services and Markets Act 2000 (FSMA) as

"any arrangements with respect to property of any description, including money, the purpose or effect of which is to enable persons taking part in the arrangements (whether by becoming owners of the property or any part of it or otherwise) to participate in or receive profits or income arising from the acquisition, holding, management or disposal of the property or sums paid out of such profits or income".

There is no restriction on the type of underlying property and arrangements that may constitute a CIS even if the underlying property would not itself be an investment regulated by FSMA (for example, real property).

Arrangements

The arrangements may involve a contract, a partnership, a trust or a company and may even include an understanding or a course of conduct. However, [section 235\(2\)](#) of FSMA requires that the arrangements must be such that the participants "do not have day-to-day control over the management of the property, whether or not they have the right to be consulted or to give directions". This was considered in the November 2005 Court of Appeal decision of [Financial Services Authority v Fradley and Woodward \[2005\] EWCA Civ 1183](#) (see [Legal update, Court of Appeal considers the construction of section 235 of the Financial Services and Markets Act 2000](#)).

The arrangements must also have either or both of the following characteristics, set out in section 235(3) of FSMA:

- The participants' contributions and the profits or income out of which payments are to be made to them must be pooled.
- The property must be managed as a whole by, or on behalf of, the operator of the scheme.

Pooling

[FSMA](#) does not define the term "pooled". This term may cover the blending or co-mingling of assets, or collective beneficial ownership of assets, for example, if the contributions are kept in a common account, and the profits or income from the contributions are paid into a common account before distribution.

Operator

[Section 237\(2\)](#) of FSMA defines an "operator" only in relation to unit trust schemes, OEICs and ACS. The term OEIC is used generically in section 237 rather than referring specifically to an ICVC formed under UK law (which, as mentioned above, is also sometimes referred to as an OEIC, but, in this practice note is referred to as an ICVC). Operator means:

- In the case of a unit trust with a separate trustee, the manager.
- In the case of an ICVC, the ICVC itself, or, if applicable, the ACD (it is suggested that, as all ICVCs must have an ACD, it will be applicable).
- In the case of any other form of OEIC (that is, a UCITS that has appointed a UCITS manager) the manager.
- In the case of an ACS in the form of a co-ownership scheme, the person appointed under the terms of the contractual scheme.
- In the case of an ACS in the form of a limited partnership, the general partner.

The FCA Glossary also defines "[operator](#)" in relation to various other fund types.

Bodies corporate

[Paragraph 21](#) of Schedule 1 to the Financial Services and Markets Act 2000 (Collective Investment Schemes) Order 2001 (SI 2001/1062) (CIS Order) states that no body corporate, other than an OEIC as defined by [section 236](#) of FSMA, or a limited liability partnership (LLP), can constitute a CIS. Therefore, no company may be a CIS unless it is an OEIC.

Participant

A participant (as defined in [section 235\(2\)](#) of FSMA) is a person who takes part in the arrangements described in section 235(1) of FSMA. The participants need not own any of the property but must all participate in, or receive profits or income arising from, the arrangements.

Unit

A unit is defined in [section 237\(2\)](#) of FSMA as "the rights or interests (however described) of the participants". Examples include shares in an OEIC, units in a unit trust, or a partnership interest in a limited partnership.

Exclusions from the definition of a CIS

Although the definition of a CIS in section 235(1) of FSMA is very wide, section 235(5) of FSMA and the CIS Order contain a number of exclusions from it.

Paragraph 1 of Schedule 1 to the CIS Order (the Schedule) excludes arrangements where investors retain ownership in their portfolios but all use the services of the same investment manager. The investments to which this exclusion applies are shares, debentures, government and public securities, warrants, certificates representing securities, units in an AUT, OEIC, ACS or recognised CIS and rights under long-term insurance contracts. Arrangements for the discretionary management of options and futures may, therefore, constitute a CIS if they have all the other necessary characteristics in section 235 of FSMA.

The paragraph 1 exclusion only applies if the participants own a part of the property that they may withdraw at any time. This may be evidenced in the accounts of a nominee holding title to the investments and in periodic statements to the individual investors stating their beneficial entitlement to particular investments. Furthermore, there must be no pooling of either contributions, or profits or income, and the management function must be limited to the buying and selling of investments in bulk on behalf of the various participants.

The CIS Order contains a further 20 specific exclusions from the definition of a CIS, some of the most commonly encountered being:

- Enterprise initiative schemes (EIS) (paragraph 2 of the Schedule)
- Pure deposit based schemes (paragraph 3 of the Schedule)
- Schemes not operated by way of business (paragraph 4 of the Schedule)
- Debt issues (paragraph 5 of the Schedule)
- Schemes entered into for commercial purposes related to existing business (paragraph 9 of the Schedule).
- Group schemes (paragraph 10 of the Schedule)
- Bodies corporate (paragraph 21 of the Schedule)

Special purpose vehicles and the definition of a CIS

Under the [CIS Order](#), certain arrangements that would otherwise constitute a "collective investment scheme" for the purposes of [section 235](#) of FSMA can benefit from a number of available exemptions. [Paragraph 9](#) of the Schedule to the CIS Order is intended to exempt arrangements carried out in the course of an existing business constituting a CIS, where that business is not a specified regulated activity. In its original form, the paragraph 9 exemption was not available for arrangements where a special purpose vehicle (SPV) is set up for the purposes of a transaction, because SPVs cannot be said to have an "existing business". However, following consultation by HM Treasury, the [Financial Services and Markets Act 2000 \(Collective Investment Schemes\) \(Amendment\) Order 2008 \(SI 2008/1641\)](#) (2008 Order) amended the terms of the paragraph 9 exemption, to allow those setting up arrangements greater freedom to use SPVs by reducing the number of such arrangements that will constitute a CIS, provided certain conditions are met.

Examples of CIS

Examples of CIS include:

- A unit trust scheme where the property is held on trust for the participants (regardless of whether it is open-ended or closed-ended) (see [UK authorised and unauthorised unit trusts](#) below).
- An OEIC, whether established in the UK or not, where the property belongs to the company and investors' rights are represented by shares, which they are entitled to have redeemed or repurchased. (Note that closed-ended investment companies, such as UK investment trusts (see [UK investment trusts](#) below), are not CIS.)
- An English limited partnership (which does not constitute a body corporate), regardless of whether it is open-ended or closed-ended (see [English \(unauthorised\) limited partnerships](#) below). This includes the recently created private fund limited partnership (PFLP) structure.
- A Delaware limited partnership (which does constitute a body corporate), if it is open-ended. (Note that a Delaware limited partnership that is closed-ended will not constitute a CIS by virtue of [paragraph 21](#) of the Schedule to the CIS Order since it will be a body corporate other than an OEIC.)

What are the principal consequences of being a CIS?

If arrangements constitute a CIS the following consequences arise:

- Units in a CIS are classified as "investments" within [article 81](#) of the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (SI 2001/544) (RAO) and are, therefore, investments regulated under [FSMA](#). For example, the provisions of FSMA relating to financial promotion ([section 21](#), FSMA) will apply in respect of units in a CIS. Note that units in a CIS are **not** investments within [article 76](#) of the RAO (shares etc), even though they may be shares in a company, since the two categories are mutually exclusive for the purposes of the RAO.
- Under [article 51ZE](#) of the RAO, establishing, operating or winding up a CIS is an activity constituting investment business and is, therefore, a regulated activity under [section 19](#) of FSMA. For example, acting as trustee of an authorised or unauthorised unit trust (see [UK authorised and unauthorised unit trusts](#) below), as depositary or sole director of a UK authorised ICVC (see [Directors and depositary](#) below) or as depositary of an ACS constitutes "operating" a CIS. For more information, see [Practice note, Regulated activities: establishing, operating or winding up a collective investment scheme](#).
- The other categories of activities constituting investment business under the RAO (dealing, arranging deals, custody, managing, advising and so on) can also apply in respect of units in a CIS.
- [Section 238](#) of FSMA severely restricts the ability of persons authorised under FSMA to promote unregulated CIS, such as unauthorised unit trust schemes and unauthorised offshore OEICs (for example, hedge funds). However, UK AUT schemes, UK authorised ICVCs, ACS and recognised schemes under [sections 264](#) or [272](#) of FSMA are not subject to the section 238 restriction.
- The [Offshore Funds \(Tax\) Regulations 2009 \(SI 2009/3001\)](#) apply to most CIS established outside the UK. Broadly speaking, the effect of these provisions is that any gain accruing to a UK tax resident investor on the disposal of its units or shares in an offshore fund will be taxed as income and not as a capital gain. This is the case unless, throughout the period during which the investor held the interest, the fund (or a relevant subfund or share class therein) was recognised by HMRC as a reporting fund. If such recognition is obtained, then any gain will continue to be taxed as a capital gain and not as income. To be recognised as a reporting fund, the fund must satisfy certain income reporting requirements. If such a fund has not obtained reporting status, certain categories of UK resident investors may, depending on their circumstances and particularly with the current divergence of the rates of UK taxation on capital gains and income, find the taxation of gains as income unattractive.
- Units in an open-ended CIS are exempt from the general prohibition on offering transferable securities to the public without an approved prospectus by virtue of [section 85](#) and [paragraph 1](#) of Schedule 11A of FSMA (Schedule 11A having been inserted in FSMA by regulation 2(2) and Schedule 2 of the [Prospectus Regulations 2005 \(SI 2005/1433\)](#)).

FCA regulated funds

Four types of fund structure may currently be formed in the UK, which may be authorised and regulated by the FCA for sale to retail customers:

- ICVCs established and authorised by the FCA under the [Open-Ended Investment Companies Regulations 2001 \(SI 2001/1228\)](#). For more detail, see [UK authorised ICVCs](#) below.

- AUTs established under trust law and authorised by the FCA under [section 243](#) of FSMA. For more detail, see [What is an authorised unit trust?](#) below.
- ELTIFs, established under the [Regulation on European long-term investment funds](#) ((EU) 2015/760) (ELTIF Regulation) and authorised under the [Alternative Investment Fund Managers Directive](#) (2011/61/EU) (AIFMD). For more detail, see [What is an ELTIF?](#) below.
- ACS (whether in the form of a co-ownership scheme or a limited partnership scheme) established under the [Collective Investment in Transferable Securities \(Contractual Scheme\) Regulations 2013 \(SI 2013/1388\)](#) and authorised by the FCA under [section 261C](#) of FSMA. For more details, see [UK authorised contractual schemes \(ACS\)](#) below.

In addition, two other categories of authorised fund may be established that have separate treatment under the FCA's Collective Investment Schemes sourcebook ([COLL](#)) for certain purposes, but which are not strictly separate categories of fund. These are:

- Charity authorised investment funds (CAIFs). Authorised funds registered as a charity under Part 4 of the [Charities Act 2011](#) and subject to the provisions of Chapter 14 of COLL ([COLL 14](#)).
- Funds of alternative investment funds (FAIFs). Authorised funds that allow investment in certain types of unregulated CIS and that may be established as either a non-UCITS retail scheme (NURS) or a qualified investor scheme (QIS). A FAIF that is established as a NURS is subject to the investment and borrowing powers in [COLL 5.7](#) and one established as a QIS is subject to those in [COLL 8.4](#).

Separately, the term "property authorised investment fund" (PAIF) is used for authorised ICVCs to which Part 4A of the [Authorised Investment Funds \(Tax\) Regulations 2006 \(SI 2006/964\)](#) applies and which are used for investment in real estate.

UCITS schemes

The acronym "UCITS" stands for "undertakings for collective investments in transferable securities", which are governed by the [UCITS Directive](#) (2009/65/EC) as amended. UCITS schemes must comply with the requirements set out in the [UCITS Directive](#). For more detail on UCITS and the UCITS Directive, see [UCITS Schemes](#) below, and [Practice notes, The UCITS IV Directive: EU legislative route and adoption](#) and [UCITS regime](#).

Non-UCITS schemes

Not all UK authorised schemes are UCITS schemes. It is also possible to establish an AUT, an ICVC or an ACS that is a NURS or a QIS. For more details on these types of scheme, see [Non-UCITS retail schemes](#) and [Qualified investor schemes \(QIS\)](#) below.

(Note that although UK ELTIFs are non-UCITS schemes that are required to be authorised by the FCA, their authorisation does not stem from [FSMA](#), so they will not generally fall within the definition of "authorised fund" set out in the FCA Glossary.)

What does "open-ended" and "closed-ended" mean?

In common parlance, an "open-ended" fund is one in respect of which the participants have a right to redeem or sell their interest in the fund at a price related to the net value of the assets held by the fund. When considering whether a fund that is an alternative investment fund (AIF) is an open-ended or a closed-ended AIF for the purposes of the [AIFMD](#), the [European Commission's Delegated Regulation determining types of AIFMs](#) (Regulation 694/2014) provides further guidance on these terms. For more information, see [Practice note, Hot topics: AIFMD: Regulation determining types of AIFMs](#).

UK AUTs (see [What is an authorised unit trust?](#) below), UK authorised ICVCs (see [UK authorised ICVCs](#) below) and ACS (see [UK authorised contractual schemes \(ACS\)](#) below) are all open-ended funds, as they are required to confer on unitholders or shareholders the right to redeem their units or shares. This means that they have variable capital and no fixed number of units or shares in issue. New units or shares in the unit trust, ICVC or ACS are offered to the public, and any unitholder or shareholder has the right to sell the units or shares back to the fund at a price determined by reference to the net asset value (NAV) of the fund's underlying portfolio. The aggregate capital may increase or decrease depending on:

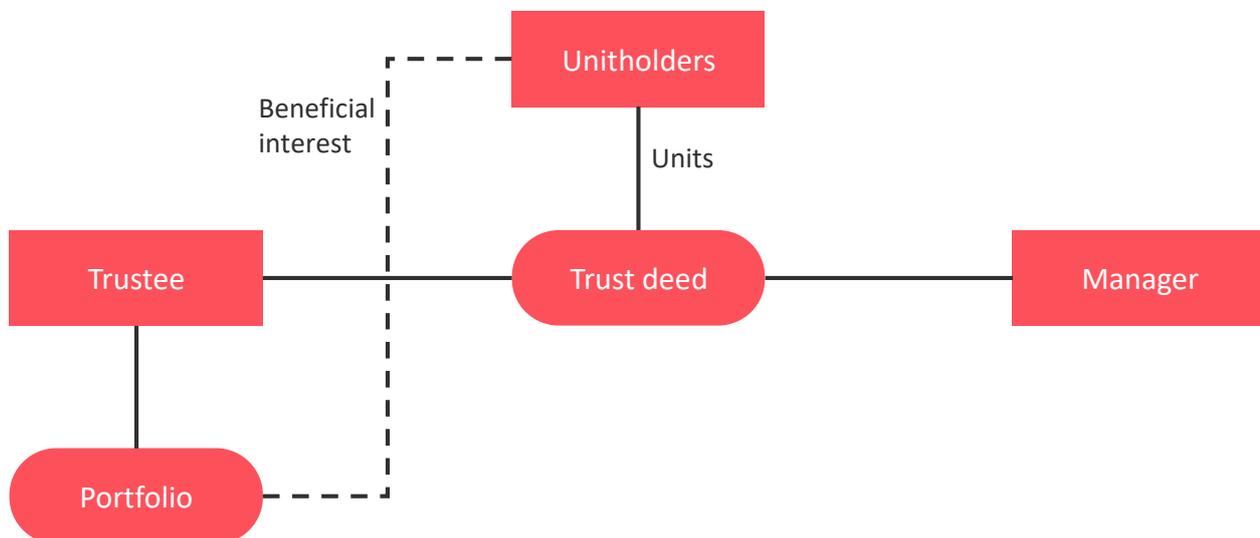
- The performance of the assets of the fund
- The volume of new investors putting money into the fund
- The volume of existing investors selling units or shares

The term "closed-ended fund" is, broadly, a reference to any fund that is not an open-ended fund. Closed-ended funds have a fixed number of units or shares that may be issued subject to company law or other constraints in the fund's constitution. Once issued, unitholders or shareholders are not entitled to have their units or shares redeemed on demand and the units or shares are usually only traded in the secondary market or redeemed on the winding up of the fund. UK investment trusts (which, confusingly, are not trusts) are public companies formed for the purpose of investing in the equity of other companies, and are examples of closed-ended funds (see [UK investment trusts](#) below).

[Section 236](#) of FSMA defines an open-ended investment company, or OEIC, but not any other open-ended kind of investment fund (for example, an open-ended unit trust or limited partnership).

A unit trust, limited partnership or other non-corporate vehicle must, therefore, be analysed against the definition of a CIS (see [Definition](#) above). A corporate body, however, by virtue of [paragraph 21](#) of the Schedule to the CIS Order can only constitute a CIS if it is either an OEIC (wherever incorporated) or a UK LLP.

UK authorised and unauthorised unit trusts



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[Section 237\(1\)](#) of FSMA defines a unit trust scheme as a CIS under which the property in question is held on trust for the participants and which is not an ACS.

The unit trust is a trust in the same way that a will or marriage settlement is a trust. In the case of a unit trust, three parties are involved:

- The management company, which operates as a distinct entity from the trust it conducts.
- The trustee, which is usually a well-known bank.
- The unitholders, who occupy the position of beneficiaries under the trust deed.

The essential principle of the unit trust is the entrusting of a portfolio of property to a trustee and the sale to participants of units of interests in this portfolio. The management company, with the co-operation and supervision of the trustee, is responsible for the selection of investments and the administration of the fund, but not its safekeeping, which is the responsibility of the trustee.

A unit trust is constituted by a trust deed made between a manager and a trustee. Interests in a unit trust are usually known as "units". A unitholder has a beneficial interest in an undivided proportion of the assets, liabilities and cash comprised in the trust fund equal to the proportion which the number of units held by him bears to the total number of units in existence.

What is an authorised unit trust?

This is a unit trust which has been approved by the FCA as being suitable for general promotion and sale to the public in the UK under [section 243](#) of FSMA.

The manager and the trustee (which must be separate entities) apply to the FCA for an authorisation order in accordance with [section 242](#) of FSMA. The application must contain such information as is reasonably required for the purpose of determining the application and additional information may be required after the application has been made.

Authorisation may be granted if:

- A satisfactory application has been made in accordance with section 242 of FSMA.
- The scheme complies with the trust scheme rules and scheme particulars rules made under [sections 247 and 248](#) of FSMA (that is, the rules in [COLL](#)).
- A copy of the scheme particulars and the trust deed has been sent to the FCA accompanied by a solicitor's certificate stating that the trust deed complies with regulations as to its contents (section 243(1), FSMA).

The scheme must also meet certain other requirements which are set out in [section 243](#) of FSMA.

If authorisation is granted, the FCA may issue a certificate stating that the scheme complies with relevant conditions. In the case of a "standard" unit trust, authorisation generally takes place four to six weeks after the application is made to the FCA.

Once authorised, any proposed alteration to the scheme and any proposal to replace the trustee must be notified in writing by the manager to the FCA ([section 251\(1\)](#), FSMA).

In addition, AUTs (as well as ICVCs and ACS) are governed by [COLL](#), compliance with the provisions of which has been mandatory since 13 February 2007. COLL specifies that the unit trust scheme does not qualify to be authorised under FSMA unless the scheme is constituted by a deed made between the manager and trustee, which conforms with COLL requirements.

For more information about the procedure for authorisation of an AUT, see [Practice note, Procedure for authorisation of an AUT](#).

Consequences of authorisation

- An AUT scheme is subject to [COLL](#) on an ongoing basis and to [sections 242 to 261](#) of FSMA.
- An AUT scheme may be promoted and sold to the public in the UK ([section 238](#), FSMA) subject to compliance with COLL and the FCA's Conduct of Business sourcebook ([COBS](#)) (to which the manager will usually be subject)
- An AUT is taxed within the special direct tax regime for authorised investment funds in the [Authorised Investment Funds \(Tax\) Regulations 2006 \(SI 2006/964\)](#) (the Authorised Investment Fund Regulations). This regime also governs the tax treatment of ICVCs. For more information, see [Tax treatment of AUTs and ICVCs/OEICs](#) below

What is an unauthorised unit trust?

This is a UK unit trust that has not been approved by the FCA as being suitable for general promotion and sale to the public in the UK.

Apart from that, the main differences between a UK AUT and a UK unauthorised unit trust are:

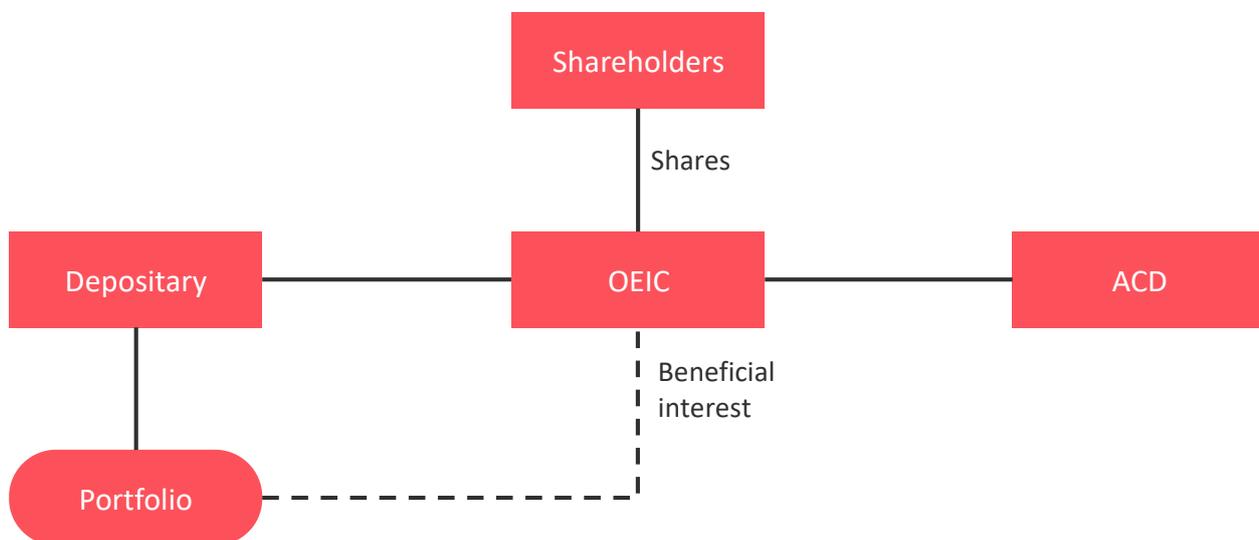
- [COLL](#) does not apply to an unauthorised unit trust. As a result, the trust deed of an unauthorised unit trust tends to be much more detailed because, unlike an AUT, there are no specified rules on, for example, pricing, valuations, dealings and investment restrictions.

- Unlike an AUT, an unauthorised unit trust has no exemption from UK capital gains tax. As a result, unauthorised unit trusts are only attractive to UK tax exempt investors such as UK pension funds and charities that do not pay capital gains tax.

Principal documentation required

- A trust deed made between the manager and the trustee.
- Prospectus, which, in the case of an AUT, must comply with the detailed content requirements set out in [COLL](#).
- A solicitor's certificate stating that the trust deed complies with such provisions of [section 243](#) of FSMA and COLL as relate to its contents (not required for an unauthorised unit trust).
- If the AUT is also authorised as a UCITS scheme, a key investor information document (KII or KIID). For more information, see [Practice note, Key investor information document \(KIID\)](#).
- Key features document (KFD) for a NURS, which is a mandatory disclosure document required by [COBS 13](#) unless the operator of the NURS has: (i) elected instead to provide a simplified prospectus; or (ii) has obtained a dispensation from the FCA in the form of a waiver to permit the use instead of a KIID (see above). The KFD (unlike the KIID) need only be given to investors who are retail clients at the time of sale or very shortly thereafter, and must contain certain details (for example, risk factors and the effect of charges and expenses on the value of their investment). In practice, this is not required for an unauthorised unit trust as the investors are usually professional clients.

UK authorised ICVCs



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Definition

Since January 1997, it has been possible to establish an authorised OEIC in the UK (that is, an ICVC) under a corporate code that is almost entirely separate from the [Companies Act 2006](#) and for that OEIC to be promoted and sold to the general public in the UK. It is still not possible to establish an unauthorised OEIC in the UK.

The corporate code for ICVCs consists of two self standing sets of regulations, HM Treasury's [Open-Ended Investment Companies Regulations 2001 \(SI 2001/1228\)](#) (OEIC Regulations) and the rules in the FCA's [COLL](#).

The OEIC Regulations provide the legal framework for ICVCs in a similar way that [FSMA](#) does for AUTs and ACS, while COLL provides the detailed rules for ICVCs as an investment product.

Application for authorisation is made to the FCA under [regulation 12](#) of the OEIC Regulations by submitting an application form, together with a fee, and drafts of the various required documents. The FCA will review the application and revert to the applicant if it has any comments. If the FCA has no comments and is satisfied with the application, it will issue a certificate of incorporation and, at that point, the ICVC comes into existence.

In common with UK AUTs and ACS, an ICVC is a CIS for the purposes of FSMA, and shareholders in an ICVC must be entitled to have their shares redeemed at a price relating to the NAV of the property to which the shares relate (see [What does "open-ended" and "closed-ended" mean?](#) above).

For more information about the procedure for authorisation of an OEIC, see [Practice note, Procedure for authorisation of an OEIC](#).

Corporate structure

Unlike AUTs and ACS, ICVCs are bodies corporate and have a separate legal personality. The ICVC, therefore, owns its portfolio of investments - shareholders in an ICVC have no beneficial interest in the underlying portfolio but, instead, simply own shares in a company, which give them certain legal and economic rights and benefits as against the company.

As a body corporate, an ICVC is capable of taking legal proceedings and of being sued. An ICVC is also capable of entering into contracts and will do so (for example) with its ACD and depositary (see [Principal documentation required](#) below).

Directors and depositary

The [OEIC Regulations](#) require an ICVC to have at least one (corporate) director but additional directors are permitted. One of the directors (and almost always the only one) will have special responsibilities as the ACD, who must be an authorised person under [FSMA](#) or otherwise authorised by its home state regulator in the case of a UCITS management company or AIFM of a UK AIF passporting into the UK under the provisions of the [UCITS Directive](#) or the [AIFMD](#).

In essence, the ACD runs the day-to-day operations of the ICVC. The OEIC Regulations require that, where an ICVC has only one director, that director must manage the business of the ICVC. As mentioned, almost all ICVCs have only one director, which is the ACD. Effectively, this means that the ACD of an ICVC will almost invariably also be the manager.

The other key party in an ICVC is the depositary. The OEIC Regulations require an ICVC to entrust its assets to a depositary for safe keeping. The depositary must be an authorised person under FSMA and must be independent of the ICVC and of its director(s), including the ACD.

Note that it is the ICVC itself that receives authorisation from the FCA through the issue of an authorisation order, further to an application made under [regulation 12](#) of the OEIC Regulations.

The legal ownership of an ICVC's portfolio will be vested in the depositary or its nominee. However, as mentioned above, unlike AUTs and ACS, the beneficial interest in the portfolio will be vested in the ICVC itself and not in the ICVC's shareholders.

Consequences of authorisation

- An ICVC is subject to the [OEIC Regulations](#) and [COLL](#) on an ongoing basis
- An ICVC may be promoted and sold to the general public in the UK ([section 238](#), FSMA) subject to compliance with COLL and [COBS](#) (to which the ACD will also be subject)
- An ICVC, like an AUT, is subject to the direct tax regime provided for in the Authorised Investment Fund Regulations. See [Tax treatment of AUTs and ICVCs/OEICs](#) below

Principal documentation required

- An instrument of incorporation. This is the founding document for an ICVC, as the trust deed is for a unit trust, and broadly fulfils the same function as the memorandum and articles of association of an ordinary UK public or private company. It must comply with the content requirements set out in [the OEIC Regulations](#). The [Companies Act 2006](#) generally does not apply. A model instrument of incorporation has been drafted by the Investment Association and it is customary to provide the FCA with a comparison document showing changes to the model instrument when submitting papers for authorisation of a new ICVC.
- A prospectus. This is primarily an information document and is very similar to the prospectus for an AUT. It must comply with the content requirements set out in [COLL](#).
- A solicitor's certificate stating that the instrument of incorporation complies with the OEIC Regulations as to its contents.
- Contracts between the ICVC and its ACD, and the ICVC and its depository. Unlike a unit trust, an ICVC is capable of entering into contracts.
- A KFD which is a mandatory disclosure document for a NURS required by [COBS 14](#). This must be given to investors who are retail clients at the time of sale or very shortly thereafter and must contain certain details (for example, risk factors and the effect of charges and expenses).
- If the ICVC is authorised as a UCITS scheme, a KIID. For more information, see [Practice note, Key investor information document \(KIID\)](#).

Tax treatment of AUTs and ICVCs/OEICs

Tax at the level of the authorised investment fund

The tax treatment for ICVCs is the same as that for AUTs and both are authorised investment funds under [regulation 3](#) of the Authorised Investment Fund Regulations.

The principal tax features of these authorised investment funds are:

- An AUT is generally treated for tax purposes as if it was a company resident in the UK and as if the rights of the unitholders were shares in that company
- The authorised investment fund's chargeable gains are exempt from UK tax
- The authorised investment fund's income is subject to UK corporation tax at 20%. Income includes offshore income gains realised on a disposal of interests in certain non-reporting offshore funds (NROFs) and proceeds of disposal of assets bought and sold as trading transactions. Property income distributions from a real estate investment trust (REIT) or property authorised investment fund (PAIF) are subject to corporation tax (again currently at 20%) without the ability to seek a deduction against such distributions where the authorised investment fund pays out amounts by way of interest distribution (see below)
- Certain categories of receipt are, however, not taxable income: such as income from most dividends and capital profits, gains and losses from derivative contracts, options and creditor loan relationships, provided the authorised investment fund accounts for such income in the appropriate way. In addition, gains realised on the disposal of interests of certain NROFs may not be taxed as income, but instead give rise to exempt capital gains, where various conditions are met, in particular that the authorised investment fund has sufficient information to compute what would have been its share of the offshore fund's reportable income had that fund been a reporting fund, with any excess of this amount over the authorised investment fund's share of distributions actually made by the offshore fund in question being included in the authorised investment fund's amount available for income allocation. Typically this will only be possible for "in house" funds, where the necessary information is readily available

- The authorised investment fund may be entitled to a tax deduction for certain amounts distributed or deemed to be distributed. The total amount shown in the authorised investment fund's distribution account as being available for distribution to investors must be shown as being available for distribution either as yearly interest or dividends. The authorised investment fund is deemed to distribute all such amounts whether or not it actually makes any distributions. The authorised investment fund is generally able to deduct all amounts of yearly interest distributed or deemed to be distributed when calculating its tax liability on income provided such amounts relate to income that was taxable for the authorised investment fund. Hence, with a full deduction the authorised investment fund will avoid the (current) 20% tax charge (save to the extent it receives property income distributions from a REIT or PAIF). Dividends distributed or deemed to be distributed by the authorised investment fund are not, however, deductible. The authorised investment fund may also be entitled to deduct other amounts, such as management charges, when computing its liability to corporation tax.
- The total amount shown in the authorised investment fund's distribution account as being available for distribution to investors may only be shown as being available for distribution as yearly interest if 60% or more (by market value) of the authorised investment fund's investments are "qualifying investments" (money placed at interest, securities, shares in a building society, qualifying units in another investment fund, certain derivative contracts and CFDs, and alternative finance arrangements) throughout the distribution period.
- The above summarises the basic rules applying to authorised investment funds. There are a number of add-on special regimes, for example, the PAIF regime, tax electing fund regime (TEF), funds investing in non-reporting offshore funds regime (FINROF), and the "white list" that can apply where the genuine diversity of ownership test and/or other conditions are met. The "white list" provides certainty that specified transactions will not be treated as trading activities (and is separately also used to determine the types of investment transactions that may qualify for the investment manager exemption). It is currently set out in the [Investment Transactions \(Tax\) Regulations 2014 \(SI 2014/685\)](#).
- Authorised investment funds are not required to pay VAT on the fees that they pay for management services. The VAT exemption for the management of special investment funds in Item 9 of Group 5 of [Schedule 9](#) to the Value Added Tax Act 1994 also covers the services provided by a third party manager in respect of the administrative management of funds as well as asset management, provided the administrative services form a "distinct package" of services

Tax at the level of the additional (that is, top) rate individual UK resident and UK domiciled investor

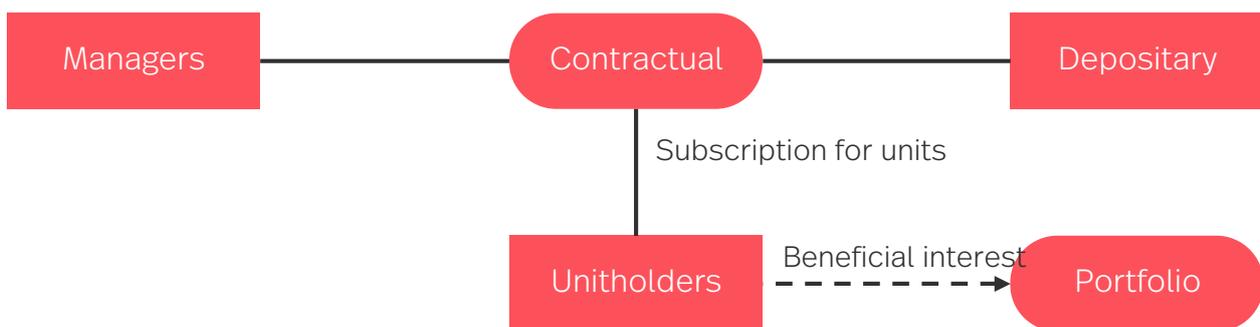
The key features are as follows:

- Yearly interest received or deemed to be received is subject to income tax at 45%. Before 6 April 2017, 20% tax was withheld by the authorised investment fund and paid over to HMRC and a further 25% was payable by the investor under self-assessment. Additional rate taxpayers are not entitled to the personal savings allowance. Authorised investment funds are not required to withhold tax on interest distributions made on or after 6 April 2017 so the full amount of any income tax due is instead collected under self-assessment.
- Dividends received or deemed to be received are subject to income tax at the dividend rate, which is 38.1% for additional rate taxpayers where dividends received exceed the annual tax free dividend allowance. This allowance is £2,000 with effect from the tax year that started on 6 April 2018.
- Investors are, therefore, subject to tax on income (actually distributed or deemed to be distributed), that is not exempt at the level of the authorised investment fund, at an effective rate of 50.48%, assuming the authorised investment fund (i) distributes amounts as dividends and hence suffers a 20% corporation tax charge on its income and (ii) is not a FINROF and ignoring the tax free dividend allowance
- A gain realised on a disposal of the interest in the authorised investment fund where it is not a FINROF is subject to capital gains tax at 20% in the hands of the investor

- Typically, investors will be issued either distribution units/shares or accumulation units/shares. An investor holding accumulation units/shares will not receive distributions but will be deemed to do so for UK tax purposes. When the investor disposes of its interest in the authorised investment fund and realises any chargeable gains, any deemed distributions previously received are included in the investor's base cost for capital gains purposes. An investor holding distribution units/shares will receive distributions and hence there is no double tax charge for that investor as amounts distributed are not reflected in the redemption NAV.
- [Schedule 19](#) of the Finance Act 1999 previously imposed a stamp duty reserve tax (SDRT) charge on surrenders of shares in an ICVC or units in an AUT to the manager (including transfers to the manager's box). However, the Schedule 19 charge was abolished with retrospective effect from 30 March 2014 by the [Finance Act 2014](#). A principal SDRT charge may still arise for investors in respect of certain non-pro rata in specie redemptions.

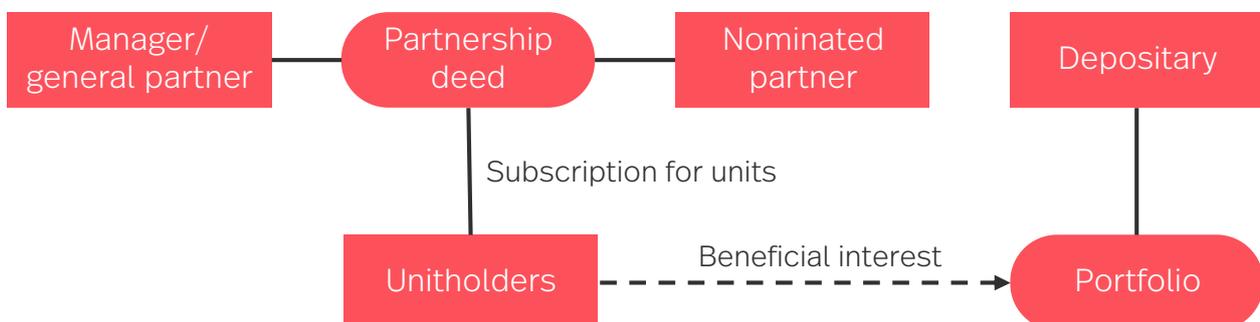
UK authorised contractual schemes (ACS)

ACS: co-ownership scheme



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ACS: limited partnership scheme



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What is an ACS?

Established under the [Collective Investment in Transferable Securities \(Contractual Scheme\) Regulations 2013 \(SI 2013/1388\)](#) (the ACS Regulations), ACS are intended (in the words of HM Treasury) to offer a tax transparent vehicle that can compete to win an appropriate share of European pooled funds as UK domiciled funds and consolidate the UK's position as the largest asset management centre in Europe.

The ACS Regulations, which came into force on 6 June 2013 provided, among other things, for a new Chapter 3A of Part XVII (Collective Investment Schemes) of [FSMA](#). In addition, the FCA amended [COLL](#) in order to implement the changes brought about by the ACS Regulations.

Additional ACS guidance from HMRC has now been published in the [Investment Funds Manual](#) at IFM08000.

The [Finance Act 2016](#) introduced a seeding relief for co-ownership ACSs into the [Finance Act 2003](#) (see [Practice note, Authorised contractual schemes: tax: Stamp duty land tax](#)). The [Finance \(No. 2\) Act 2017](#) contains legislation concerning the availability of capital allowances to investors in co-ownership ACSs. The Finance (No. 2) Act 2017 also contains legislation introducing powers for regulations to be made relating to the provision of information by ACSs to investors and HMRC, and to the tax treatment of participants in co-ownership ACSs investing in offshore funds. These regulations (the [Co-ownership Authorised Contractual Schemes \(Tax\) Regulations 2017 \(SI 2017/1209\)](#)) were made on 5 December 2017 and came into force on 27 December 2017. In addition, regulations (the [Collective Investment Schemes and Offshore Funds \(Amendment of the Taxation of Chargeable Gains Act 1992\) Regulations 2017 \(SI 2017/1204\)](#)) were made on 4 December 2017 and came into force on 1 January 2018 clarifying the capital gains treatment of a disposal of units in a transparent fund, including a co-ownership ACS.

Structure

An ACS may take one of two forms, namely a co-ownership scheme or a limited partnership scheme, and may be established as a UCITS, a NURS or a QIS.

In the case of a co-ownership scheme, a deed between the authorised fund manager, on behalf of the participants, and a depositary must meet the requirements of [COLL](#). Investors automatically and by operation of law acquire rights and liabilities by subscribing for units in the scheme rather than by entering into the deed. The scheme itself has no legal personality; the scheme's property is beneficially owned by its unitholders as tenants in common (common property in Scotland), while the depositary holds legal title.

Assets are managed by the authorised fund manager, who may acquire, manage and dispose of property for the purposes of the scheme. Co-ownership schemes (though not limited partnership schemes) may be in the form of an umbrella fund as well as a standalone vehicle.

A unitholder's liability is limited to the price of his or her units. Property subject to a sub-fund of an umbrella fund may only be used to discharge the liabilities of the participants in that sub-fund.

In the case of a limited partnership ACS, the scheme will again be formed by deed, entered into by the general partner as authorised fund manager (although it may delegate management functions to another person) and a nominated partner, which will be the only limited partner of (but not a participant in) the scheme on its formation. The contents of the deed must meet the requirements of [COLL](#). The investors in the scheme will be limited partners and legal title will, as in a co-ownership scheme, be held by a depositary. The form of a limited partnership ACS follows closely that of a limited partnership made under the [Limited Partnership Act 1907](#) (see [English \(unauthorised\) limited partnerships](#) below for a fuller description of such vehicles), although the [ACS Regulations](#) make three amendments to the 1907 Act specific to ACS, in order to provide sufficient flexibility for such schemes to operate successfully.

These are that:

- Limited partners will be able to withdraw their contributions without this requiring the dissolution of the partnership as a whole, provided that at least one limited partner remains
- In the absence of wrongdoing on its part, the general partner will not be liable for the debts of the limited partnership
- Partnership changes need not be published in the Official Gazette.

Liability of a limited partnership scheme is restricted to the amount of partnership property available to the general partner to meet debts and obligations.

Authorised fund manager and depositary

In the case of each type of ACS, the [ACS Regulations](#) and [COLL](#) contain a number of provisions relating to the authorised fund manager and depositary. In particular:

- The authorised fund manager and depositary must be independent persons.
- Each must be a body corporate, incorporated in the UK or in another EEA state.
- The depositary must have a place of business in the UK.
- The authorised fund manager must have a place of business in either the UK or in another EEA state (and, if in an EEA state, the scheme must not be a Recognised Overseas Scheme under [section 264](#) of FSMA).
- Both the authorised fund manager and depositary must be authorised persons with the appropriate permission to act as an authorised fund manager or depositary respectively.
- The authorised fund manager must pass the FCA's fitness and propriety test.

Consequences of authorisation

Application for authorisation as an ACS is made by the scheme's authorised fund manager and depositary pursuant to [section 261C](#) of FSMA (as introduced by the [ACS Regulations](#)). In addition to the specific provisions relating to the authorised fund manager and depositary outlined above, the scheme's name must be neither undesirable nor misleading, and the purposes of the scheme must be "reasonably capable of being successfully carried into effect".

The application must be determined by the FCA within six months of receipt (or two months where the ACS is a UCITS).

Given the complex reporting obligations to which an ACS is subject, units may only be issued to:

- A professional ACS investor (defined as being a person who falls within Section 1(1) to (4) of Annex II (Professional clients for the purpose of this directive) to the [MiFID II Directive](#) (2014/65/EU))
- A large ACS investor (that is, one who makes a payment of, or contributes property with a value of not less than £1 million)
- An existing ACS investor

In addition, where the ACS is a QIS, units may only be issued to a person to whom they may be promoted under [COBS 4.12.4R](#) and who also meets the criteria in [COLL 8 Annex 2R](#).

While units in an ACS may be transferred (subject to any restrictions contained within the terms of the scheme's deed), they may not be transferred to a person who does not fall within one of the categories of eligible investor above (and, in the case of an ACS that is a QIS, a person to whom they may be promoted under [COBS 4.12.4R](#) and who also meets the criteria in [COLL 8 Annex 2R](#)).

Principal documentation required

Where the ACS is a co-ownership scheme:

- Form 261C.
- Contractual scheme deed.
- A solicitor's certificate stating that the scheme's proposed contractual scheme deed complies with [section 261H](#) of FSMA and with any requirements of [COLL](#) that relate to its contents
- Prospectus. This must comply with the content requirements set out in COLL
- A model portfolio

- If the ACS is also authorised as a UCITS scheme, a KIID that is a mandatory disclosure document for UCITS schemes (see [UCITS schemes](#) below) required pursuant to the [UCITS Directive](#) by [COBS 14](#). This must be provided to all investors in good time before they invest
- KFD for a NURS, which is a mandatory disclosure document required by [COBS 13](#) unless the operator of the NURS has elected to provide instead a simplified prospectus or KIID, or the information appears with due prominence in another document. The KFD (unlike the KIID) need only be given to investors who are retail clients at the time of sale or very shortly thereafter, and must contain certain details (for example, risk factors and the effect of charges and expenses on the value of their investment). In practice, this will not be required in the case of an ACS whose investors are all professional ACS investors

Where the ACS is a limited partnership scheme:

- Form 261C
- Partnership Deed
- A solicitor's certificate stating that the scheme's proposed partnership deed complies with section 261H of FSMA and with any requirements of COLL which relate to its contents.
- The Certificate of Registration (or a copy) of the scheme as a limited partnership
- Prospectus. This must comply with the content requirements set out in COLL
- A model portfolio
- If the ACS is also authorised as a UCITS scheme, a KIID that is a mandatory disclosure document for UCITS schemes (see [UCITS schemes](#) below) required pursuant to the [UCITS Directive](#) by [COBS 14](#). This must be provided to all investors in good time before they invest. For more information, see [Practice note, Key investor information document \(KIID\)](#)
- KFD for a NURS, which is a mandatory disclosure document required by [COBS 13](#) unless the operator of the NURS has elected to provide instead a simplified prospectus or KIID, or the information appears with due prominence in another document. The KFD (unlike the KIID) need only be given to investors who are retail clients at the time of sale or very shortly thereafter, and must contain certain details (for example, risk factors and the effect of charges and expenses on the value of their investment). In practice, this will not be required in the case of an ACS whose investors are all professional ACS investors

Tax treatment of ACS

Tax at fund level

The ACS is not a taxable entity for UK direct tax purposes and suffers no such UK tax directly. For direct tax purposes, investors will be treated as if they had invested directly in the underlying assets (apart from gains arising on the disposal of assets of a co-ownership scheme – see Tax at UK investor level below). The ACS is not, therefore, subject to UK corporation tax, income tax or capital gains tax. The treatment of an ACS for non-UK purposes, and in particular whether it is regarded as tax transparent, is a matter for local advice.

Tax at UK investor level

The key features are:

- Income arising to both co-ownership schemes and partnership schemes is treated as arising directly to the investors for UK tax purposes. For tax exempt investors, it should therefore be exempt from UK tax. For UK taxable investors, income will be taxable as it arises. This means that the investor will require detailed information about the source and timing of amounts comprising its share of the income to meet its UK income or corporation tax obligations. This is addressed in Part 2 of the [Co-ownership Authorised Contractual Schemes \(Tax\) Regulations 2017](#) for co-ownership schemes, whereas partnership schemes will be obliged to prepare a partnership tax return and partnership statement that will be shared with investors.
- The co-ownership scheme, while transparent for income tax purposes, is effectively opaque for UK capital gains tax and corporation tax on chargeable gains tax purposes. For such purposes, therefore, the asset

held by a UK investor is treated as being the interest in the co-ownership scheme itself, and not the investor's share of the underlying assets. The investor will realise a chargeable gain or loss, therefore, only upon a disposal (including a redemption) of that interest. The Collective Investment Schemes and Offshore Funds (Amendment of the Taxation of Chargeable Gains Act 1992) Regulations 2017 (SI 2017/1204) set out specific rules dealing with the computation of any such gain or loss, which generally will apply to disposals arising on or after 1 January 2018

- The partnership scheme by contrast is fully transparent and so investors may realise chargeable gains and losses when a disposal is made by the scheme. This is consistent with the current treatment of unauthorised English limited partnerships (see Tax treatment of unauthorised English limited partnerships below). Partnership schemes are expected to be more suitable for exempt investors, since taxable investors in a partnership scheme will need to report all income and gains as they arise unless they invest via an opaque feeder
- As mentioned above, [Schedule 19](#) was abolished with effect from 30 March 2014 onwards. ACS have always been, however, outside the Schedule 19 charge to SDRT entirely
- Transfers to third parties and agreements to transfer to third parties of units/partnership interests in an ACS are not subject to UK stamp duty/SDRT charge, provided the transfer or agreement to transfer does not form part of arrangements of which the main purpose, or one of the main purposes, is the avoidance of a stamp duty or SDRT charge
- Relief from stamp duty and SDRT is available in certain circumstances, such as on transfers of units/partnership interests in the ACS between sub-schemes of an umbrella co-ownership scheme, subject to an anti-abuse rule
- The supply of management services to ACS is exempt from VAT

Charity authorised investment funds

What is a CAIF?

The introduction by the FCA of [COLL 14](#) on 1 October 2016 established a new type of authorised fund, the charity authorised investment fund (CAIF).

A charity fund is a CIS or another type of vehicle in which only charities are allowed to invest. The fund is eligible for registration as a charity in its own right and enjoys the same tax-exempt status as charities.

Prior to the introduction of the CAIF regime, investment funds established for charitable purposes pursuant to [section 96](#) of the Charities Act 2011 (usually structured as common investment funds or CIFs) were regulated by the Charity Commission and fell outside the scope of FSMA. As an authorised fund, a CAIF is supervised and regulated by the FCA with the same regulatory oversight and protections as any other authorised investment fund. A CAIF is also, however, eligible (and required to be) registered as a charity in its own right under Part 4 of the [Charities Act 2011](#) and regulated as such by the Charities Commission.

COLL 14 sets out specific rules and guidance applicable to authorised fund managers (AFMs) and depositaries of CAIFs (see [Requirements under COLL 14](#) below). In addition, since a CAIF may be a UCITS, a NURS or a QIS and may be structured as an AUT, ICVC or an ACS, those sections of the FCA Handbook relevant to such types and structures of authorised investment funds will also apply to a CAIF.

The manager, trustee and depositary of a CAIF must have the necessary permission under Part 4A of [FSMA](#).

For more information about CAIFs, see [Practice note, How to set up a charity authorised investment fund \(CAIF\)](#).

Structure

In practice, a CAIF is most likely to take the form of an AUT, as this most closely reflects existing charity structures. As mentioned above, though, it is possible for a CAIF to be formed using a different structure, such as an authorised OEIC (ICVC) or ACS, provided the Charity Commission is satisfied that the chosen structure can be a charity.

The Investment Association (IA), Charity Investors Group (CIG) and Charity Law Association (CLA) have produced a basic [guide](#), which includes assistance on completing the charity registration process.

Requirements under COLL 14

The AFM and the depositary of a CAIF must notify the FCA, without undue delay, of both the registration of the CAIF with the Charity Commission and when that registration is cancelled.

CAIFs may be established with an advisory committee (akin to a board of charity trustees, as some existing charities have) which performs a consultative role only, with no right to take decisions on matters which are the responsibility of the AFM and/or the depositary. The committee could, though, be given certain rights to receive information and to be explicitly consulted on issues affecting investors' rights and the continued charitable status of the CAIF.

In a number of areas, [COLL 14](#) provides CAIFs with a similar degree of flexibility as available to CIFs. In particular, provided the CAIF's constitution and prospectus allow it, the AFM and depositary of a CAIF are permitted to:

- Smooth income payments by holding back some of the income available for distribution, then paying it out later, thereby creating a stable income stream
- Adopt a total return approach, which allows capital growth to be treated as income for the purpose of meeting a pre-determined target

Converting a CIF to a CAIF

CIFs in existence when the CAIF regime came into force may continue under their existing rules, although their managers or sponsoring charities may choose to wind them up and replace them with CAIFs in due course. No mechanism has been introduced to "convert" an existing charity fund into a CAIF or to streamline the transition of assets from a CIF to a CAIF so it seems likely that, where a promoter of a CIF wishes to bring the assets of an existing charitable fund into the CAIF structure, the CAIF would need to enter into a form of arrangement pursuant to which the CAIF would receive property by way of subscription in kind. The precise form of these arrangements will depend to an extent on the terms of the scheme governing the CIF in question.

The principal documentation required is:

- **A trust deed.** This is the founding constitutional document for a CAIF formed as an AUT and is binding on the manager, trustee and unit holders. Content requirements are set out in [COLL](#) though, as mentioned above, those relevant to a given CAIF will vary depending on whether the CAIF is structured as a UCITS, NURS or QIS. The trust deed should, though, contain an exclusively charitable objective
- **A solicitor's certificate.** This confirms that the trust deed meets the requirements set out in [COLL](#) and must be submitted to the FCA as part of an application for authorisation
- **Prospectus.** This sets out information to investors and potential investors in the CAIF as set out in [COLL](#) and, if relevant, the Investment Funds sourcebook ([FUND](#)). The content requirements of the prospectus will vary depending on the exact structure of the CAIF
- **A checklist.** This confirms to the FCA where each content requirement in [COLL](#) has been addressed within the CAIF's prospectus
- **A KIID.** Where the CAIF is to be authorised as a UCITS (or a NURS-KIID, where it is to be authorised as a NURS but the manager has elected to provide KIID rather than a KFD)

Tax treatment of a CAIF

For direct and stamp tax purposes, a CAIF will benefit from tax-exempt status as a registered charity, provided it has been recognised as a charity by HMRC.

In addition, the management of a CAIF (covering both portfolio and administrative management) should fall within the VAT exemption for management of special investment funds as the CAIF will fall within the UK domestic law definition of those funds that are "special investment funds", being an AUT, ICVC or ACS.

FCA categories of regulated schemes

There are three categories of schemes (as opposed to fund types or legal structures - see [FCA regulated funds](#) above) that can be authorised by the FCA in the UK:

- UCITS schemes that comply with the [UCITS Directive](#) (see [UCITS schemes](#) below)
- NURS, which will be AIFs for the purposes of the [AIFMD](#) (see [Non-UCITS retail schemes](#) below)
- QISs, which will be AIFs for the purposes of the [AIFMD](#) (see [Qualified investor schemes \(QIS\)](#) below)

UCITS schemes

What are UCITS schemes?

UCITS are open-ended collective investment vehicles (in the UK, AUTs, ICVCs, ACS or CAIFs) that comply with the requirements of the [UCITS Directive](#) as amended. The purpose of the UCITS Directive is to co-ordinate

the laws regulating UCITS in EU member states in order to achieve similar competitive environments and investor protection mechanisms. To this end, the UCITS Directive, as amended, establishes common basic rules for the authorisation, supervision, structure and activities of UCITS schemes in the EU. It is based on the principle of "home-country control".

A UCITS scheme must be authorised by the member state in which it is established. It may then be promoted in every other member state, provided it complies with the local marketing regulations, without the need for re-authorisation.

The UK gives effect to the [UCITS Directive](#) in Chapter 3 of Part XVII of [FSMA](#) (which applies to CIS) and [COLL](#) and, also in relation to ICVCs, in the [OEIC Regulations](#) and [COLL](#).

The UCITS regime was amended with effect from 18 March 2016 following the adoption of the [UCITS V Directive](#) (2014/91/EU), which introduced changes in relation to remuneration policies, depositaries, and sanctions. For more information, see [Practice note, UCITS V: overview](#).

Conditions

In order to qualify as a UCITS scheme, a fund must meet several conditions:

- The sole object of the fund must be to invest capital collected from the public in transferable securities based on the principle of risk spreading
- Units or shares issued by the fund must be directly or indirectly redeemable out of the fund's assets on the request of the unitholders. Thus the [UCITS Directive](#) only applies to open-ended funds (see [What does "open-ended" and "closed-ended" mean?](#) above)
- The head office of the fund must be situated in the same member state as the registered office

Exclusions

The UCITS Directive does not allow for the following types of funds:

- Closed-ended funds (for example, a UK investment trust)
- Funds not directly available to the general public
- Funds sold only in non-member states
- Funds investing in physical assets such as property or commodities

Investment restrictions

The UCITS Directive imposes several restrictions on the investment policies of a UCITS scheme, including:

- In general, it may invest no more than 10% of its assets in transferable securities or approved money-market instruments that are issued by any single body and all holdings in excess of 5% of its assets may not, in aggregate, exceed 40% of the assets
- No more than 20% of scheme property may be in transferable securities or approved money-market instruments issued by entities in the same group
- No more than 20% of assets may be invested in any one single CIS (UCITS and non-UCITS only), with a general restriction of a maximum of 30% of assets invested in non-UCITS schemes
- Maximum over-the-counter (OTC) counterparty exposure is limited to 5% (10% in the case of approved banks)
- No more than 20% of assets may generally be invested in a combination of transferable securities and approved money-market instruments issued by, and deposits or OTC derivative transactions made with, a single body. Note, however, that the European Securities and Markets Authority's (ESMA) [guidelines](#) on ETFs and other UCITS issues, published on 1 August 2014, allow a UCITS to be fully collateralised in different transferable securities and money market instruments issued or guaranteed by a member state or by certain other specified bodies (including local authorities and public international bodies), provided that, where a UCITS intends to be fully collateralised in securities issued or guaranteed by a member

state, this fact is disclosed in the prospectus. The UCITS should also identify the member states, local authorities, or public international bodies issuing or guaranteeing securities that they are able to accept as collateral for more than 20% of their NAV

- No more than 35% of assets may be invested in the government or public securities of a single body (subject to the point below)
- Over 35% of scheme property may be invested in a single government or public securities body, but there is a restriction that no more than 30% of the scheme property may consist of securities of any single issue and a requirement that the securities must come from at least six different issues

Since 21 December 2014, an authorised fund manager of a UCITS scheme must not rely, for the purposes of its risk management process, "solely or mechanically" on credit ratings issued by credit rating agencies (CRAs) when assessing the creditworthiness of the UCITS's assets (as specified in [CRA III](#) (Regulation 462/2013)).

Non-UCITS retail schemes

It is possible to have a retail scheme that is an AUT, an ICVC, an ACS or a CAIF, but that does not fall within the UCITS regime. This is referred to as a non-UCITS retail scheme, or NURS. A NURS will constitute an AIF for the purposes of the AIFMD.

The FCA has allowed NURS greater investment flexibility than UCITS schemes and accordingly, [COLL](#) makes allowance for NURS to invest in the following assets:

- Those investments that are permitted for UCITS schemes (though in some cases subject to different limits, see [Investment limits and risk spread](#) below)
- Unregulated schemes
- Gold
- Real property

Where a scheme is an umbrella scheme, the rules on investment powers and limitations apply to each sub-fund separately. It should also be noted that a sub-fund is prohibited from investing in another sub-fund under the same umbrella. It should also be noted that, under COLL 1.2.1AG, while an ACS set up as a co-ownership scheme may be structured as an umbrella scheme (as is the case for the other types of authorised funds), one which is in the form of a limited partnership may not.

Investment limits and risk spread

A NURS is subject to a number of limitations in relation to the amount of scheme value that it is allowed to invest and limited in its ability to invest in different assets. The most important of these are:

- Up to 35% in any one target fund (compared with 20% for a UCITS scheme)
- Up to 20% in deposits with a single body
- Up to 10% in transferable securities or money market instruments issued by a single body (other than in respect of index trackers). The 10% limit is raised to 25% in the case of covered bonds
- Maximum OTC counterparty exposure is limited to 10% of the value of the scheme

Investment in collective investment schemes

A NURS is allowed to invest in:

- UCITS schemes
- Other NURS
- Recognised schemes
- Non-UK constituted schemes whose investment and borrowing powers are equivalent to, or more restricted than, those of NURS
- Other unregulated schemes (including hedge funds), provided that (other than in the case of funds of alternative investment funds (FAIFs), see [Funds of alternative investment funds \(FAIFs\)](#)) the combined value of unapproved securities and unregulated schemes does not exceed 20% of the NURS's value

In addition, any target fund in which a NURS invests must:

- Be prohibited from having more than 15% of its value invested in other CIS. Note the reference here to "prohibited". Most hedge funds do not adopt an express investment restriction regarding investment in other funds although it is believed that a statement of policy adopted by the fund's directors, which is binding on the hedge fund manager, would suffice, as would a side letter covering the same matter
- Operate in accordance with the principle of risk
- Entitle its participants (investors) to redeem their units at a price related to NAV

Funds of alternative investment funds (FAIFs)

Funds of alternative investment funds (FAIFs) are authorised CIS that can invest up to 100% of their assets in unregulated CIS, such as hedge funds or unauthorised property funds, and that can be marketed and distributed to retail investors. The FAIF regime came into effect on 6 March 2010. Although a FAIF can be launched as a QIS, this note assumes that a FAIF is a NURS operating as a FAIF. The investment powers and restrictions of a FAIF under [COLL 5.7](#) follow closely those of a NURS under [COLL 5.6](#) (see [Non-UCITS retail schemes](#)) save that the limitation of a holding of more than 20% in unregulated schemes (in combination with unapproved securities) does not apply to a FAIF with the result that a FAIF may invest up to 100% of its assets in such schemes (including, of course, hedge funds, private equity and property funds).

As with a NURS that is not operated as a FAIF, the schemes in which a FAIF invests must meet certain criteria. They must:

- Operate on the principle of the prudent spread of risk
- Be prohibited from investing more than 15% in value of the property of the scheme in other CIS
- Entitle their participants (investors) to redeem their units at a price related to NAV

FAIFs may be formed as standalone funds or as feeder funds investing at least 85% of their assets in the units of a master fund which may or may not be a UK scheme authorised by the FCA. A master scheme for a FAIF (and, where the master is itself a feeder in a master/feeder arrangement, the schemes in which the master invests) must operate in a way that is consistent with the rules in [COLL 5.7](#). It is, therefore, possible to organise a FAIF as a feeder fund for an offshore unregulated fund of hedge funds, but the rules in [COLL 5.7](#) must be applied effectively as if the offshore fund of hedge funds was itself a FAIF.

In addition, there is a requirement on the authorised fund manager to carry out appropriate due diligence on the underlying funds on an ongoing basis and:

- To be satisfied, on reasonable grounds, that each underlying fund complies with relevant legal and regulatory requirements
- To take reasonable care to determine that:
 - the property of the underlying funds in question is held in safekeeping by a third party (for example, a custodian) that is subject to prudential regulation
 - the functions of calculating the NAV of the underlying funds and the maintenance of their accounting records are segregated from the investment management function
 - each underlying fund is regularly audited by an independent auditor in accordance with international auditing standards.

[COLL 5.7.11G](#) sets out extensive guidance on the extent and nature of this due diligence exercise.

It should be noted, however, that the success of an onshore fund of offshore funds will depend to a large extent on their tax treatment (for further details, see [Practice note, Offshore funds: tax](#)).

Investment in derivatives

Derivative exposure must not exceed the spread limits set out in [Investment limits and risk spread](#) above.

A derivative transaction entered into by a NURS must be either:

- In an approved derivative
- A transaction in an OTC derivative and subject to the restrictions set out below

The definition of "approved derivative" includes not only options, futures and CFDs based on assets in which the scheme itself could invest directly (such as transferable securities, money market instruments, deposits or units in other CIS) but also financial indices, interest rates, forex rates and currencies.

OTC counterparty exposure is limited to 10% of the scheme value with any one counterparty (as mentioned above) where the counterparty is an eligible counterparty.

A NURS may enter into a derivative or forward transaction only where the fund's maximum exposure is covered at a global level, that is, the scheme property has adequate cover to meet total exposure taking into account the value of the underlying assets, any reasonably foreseeable market movement, counterparty risk and the time available to close-out any positions.

Cash

A NURS may not hold cash or near cash except to the extent it is reasonable to regard it as necessary for the pursuit of its objectives, to meet redemptions, for efficient management in accordance with its objectives, or other "ancillary purposes".

Borrowing powers

A NURS can borrow money repayable by the fund from a bank or "eligible institution" although there is no requirement (as there is for UCITS) that such borrowings must be of a temporary nature. A limit of 10% of the scheme value which may be in borrowings "on any day" does, however, apply.

Stock lending

Stock lending by a NURS is permitted under the rules in [COLL](#) provided it is reasonably seen as appropriate in order to generate additional income and may be done with an acceptable degree of risk.

The counterparty must be authorised either by the FCA or, where it is an entity established in a different EEA member state, by the regulator in that member state and the agreement must be in terms that are both:

- Acceptable to the depositary or trustee.
- In accordance with good market practice.

The collateral obtained under the stock lending agreement must be acceptable to the depositary, adequate and "sufficiently immediate" (that is, either transferred to the depositary by or at the time that the depositary transfers the securities being loaned or transferred at the latest by close of business on the day of the transfer out).

In order to be "adequate", the collateral should be in the form of either cash, government and public securities, a certificate of deposit, letter of credit or a readily realisable security, which is at least equal in value to the securities transferred out of the scheme property.

Investment in property

The prospectus of a NURS which invests in an immovable (that is, land or a building) must identify the country in which the immovable is located.

Where the immovable is located:

- In England and Wales or Northern Ireland, it must be in a freehold or a leasehold interest
- In Scotland, it must be an interest or estate in or over land or heritable right (including a long lease)
- In any other jurisdiction, it must be in interests analogous to those permissible for UK-situated immovables

The ACD must take reasonable care to determine that the title to the land or building is a good and marketable title.

A report must be obtained from an "appropriate valuer" (that is, an independent valuer with knowledge and expertise in the valuation of immovables of the particular kind, in the particular area) containing a valuation of the immovable and stating that in the valuer's opinion it would, if acquired, be capable of being disposed of "reasonably quickly" at that valuation. The land or building must be bought (or an enforceable contract to buy entered into) within six months of receipt of the valuer's report.

An immovable cannot be bought either:

- If the ACD becomes aware that the valuer's report can no longer be relied on.
- At more than 105% of the valuation contained in the required report.

Strict limits apply to the permissible level of investment in land and buildings by a NURS. These limits include:

- Not more than 50% of scheme property can consist of immovables that are unoccupied, non-income producing or in the course of substantial development, redevelopment or refurbishment
- Not more than 15% in value of the scheme property may consist of any one immovable. (This may increase to 25% once the immovable has been included in the scheme property, provided it fell within the 15% limit when obtained)
- Not more than 20% in value of the scheme property is to consist of mortgaged immovables
- The scheme cannot enter into a mortgage that secures more than 100% of the valuation given in the valuer's report
- An immovable can only be mortgaged up to 100% of its value if the combined value of immovables, borrowings of the NURS and unapproved securities is not greater than 20% of the scheme's value

A NURS may only grant a third party an option to buy any of its immovables if the value of the immovable in question, taken together with any investments in unregulated CIS and any transferable securities, which are not approved securities, does not exceed 20% of the value of the scheme property.

Funds investing in inherently illiquid assets (FIIA)

In the light of a variety of drivers (including the temporary suspension of a number of property funds following the UK's Brexit referendum result in 2016), the FCA initiated work on whether the use of liquidity management tools in NURS was working as well as it should. This work resulted, in September 2019, with the FCA's [policy statement](#), (PS19/24) setting out feedback to its October 2018 [consultation paper](#) (CP18/27), focusing on NURS that invest in immovable assets, such as commercial property.

PS19/24 also contains new rules and guidance, effective from 30 September 2020, including the introduction of a new category of fund, that is a "fund investing in inherently illiquid assets" (FIIA).

A FIIA is a NURS in respect of which:

- At least 50% of the value of the scheme property is either:
 - stated, in the fund's investment objective and policy and prospectus, to be intended to be invested in inherently illiquid assets; or
 - has been invested in such assets for at least three "continuous" (that is, consecutive) months in the last twelve months

- The fund's constitutional documents and prospectus do not provide for limited redemption arrangements that reflect the time typically needed to sell, liquidate or close out the inherently illiquid assets in which the NURS invests
- The NURS is not in the process of winding up or termination

The FCA's new rules will require all NURS that hold property and other immovables to suspend dealing (as soon as possible and in any event within two business days) when the standing independent valuer (SIV) determines there is material uncertainty regarding the value of more than 20% of the fund's assets or the fund invests more than 20% of its scheme property in another authorised fund that has temporarily suspended dealings. A fund manager will, though, still be allowed to deal where it has a reasonable basis for determining that it is not in the best interests of investors to suspend and the fund's depository has agreed.

The FCA's new rules will also place additional obligations on a manager of a FIIA to maintain plans to manage liquidity risk, including:

- Increased disclosure of how liquidity is managed.
- Standard risk warnings in financial promotions to retail clients.
- Enhanced depository oversight.
- A requirement to produce liquidity risk contingency plans.

As mentioned above, the new rules will not apply to a NURS that provides for limited redemption arrangements designed to reflect the time needed to sell the assets in which it invests, as the FCA regards such funds as having mitigated the liquidity mismatch and so have addressed the purpose of the new rules.

Patient capital

In December 2018, as part of its response to the patient capital review launched by HM Treasury and the Department for Business, Energy and Industrial Strategy (BEIS), the FCA opened a discussion with stakeholders (in [DP18/10](#)) on the question of how, and to what extent, authorised funds should be able to invest in so-called patient capital, while ensuring that investment risks are managed appropriately and that investors are able to redeem investments in a timely manner when they want to withdraw from the fund. In this context, the term "patient capital" refers to a broad range of alternative investment assets, for example, infrastructure or real estate, which are intended to deliver long-term returns but that are typically illiquid and often require an investor to be willing to tie up its capital and forgo an immediate return on their investment.

The consultation period under DP18/10 closed in February 2019. The FCA has noted that it intends to publish a feedback statement and set out its next steps later in 2019, with any proposals for change being the subject of a further consultation in due course.

Qualified investor schemes (QIS)

The QIS was introduced by the FCA's predecessor, the FSA, in April 2004 under [COLL](#). A QIS can only be promoted to persons in the UK who fall within the gateways in [COBS 4.12.1](#) (for example, eligible counterparties or professional clients). A QIS will constitute an AIF for the purposes of the [AIFMD](#).

[COLL 8.1.3R](#) also requires the ACD or manager of the QIS to take reasonable care to ensure that the fund is only invested in by persons to whom units in the fund may be promoted under [COBS 4.12.4R](#) (reliance can be placed on information provided by another person, for example, an IFA, for this purpose to the extent that the ACD or manager can show that it was reasonable to do so).

Investment and borrowing powers

There is a basic requirement for a spread of risk consistent with the investment objective and policy but there are no specific spread or concentration limits, except in relation to property.

The following are permitted investments for a QIS:

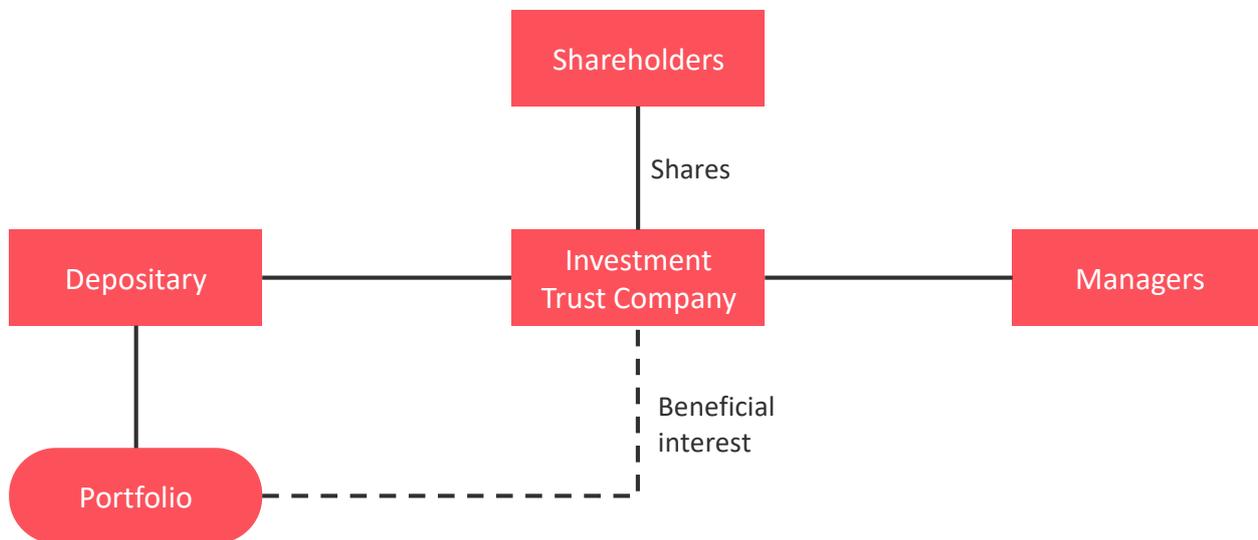
- Shares
- Debt instruments
- Deposits
- CIS
- Derivatives
- Contracts of insurance
- Government and public securities
- Property
- Precious metals (gold, silver and platinum)
- Commodity contracts

Collective investment schemes

A QIS can also invest without limit in unregulated CIS (for example, hedge funds and property funds established in the Cayman Islands, BVI or the Channel Islands) provided that each underlying fund:

- Is the subject of an independent annual audit conducted in accordance with international accounting standards
- Has its value verified by a person independent from its operator on each dealing day. Note that this condition may prohibit investment in certain US hedge funds where the NAV is calculated by the investment manager, rather than an independent administrator (as is usual for European hedge funds).
- Permits its unitholders to redeem their units within a reasonable time. Note that the term "reasonable time" is undefined. While it would permit investment to be made in an underlying hedge fund with, say, monthly, quarterly or six monthly dealing days, the treatment of lock-up periods is unclear
- Is prohibited from having more than 15% of its value invested in other CIS. Note the reference here to "prohibited" and contrast this with the equivalent provision for UK investment trusts which refers to "stated investment policy". Most hedge funds do not adopt an express investment restriction regarding investment in other funds, although it is believed that a statement of policy adopted by the fund's directors, which is binding on the hedge fund manager would suffice as would a side letter covering the same point
- Operates in accordance with the principle of risk spreading

UK Investment trusts



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Definition

Despite its name, an investment trust is a company, not a trust. In common parlance, an investment trust is simply a company formed for the purpose of investing in other companies or investment assets. In legal terms, an investment trust is typically a UK public company that meets the eligibility conditions in [section 1158](#) of the Corporation Tax Act 2010 (CTA 2010), that satisfies certain other requirements on an ongoing basis, and that has been approved as an investment trust by HMRC. It is possible for a non-UK incorporated company (for example, a Guernsey or Jersey company) to qualify as an investment trust for UK tax purposes, but these companies are relatively uncommon. The vast majority are UK public companies, and all investment trusts are likely to be AIFs for the purposes of the AIFMD.

Investment trusts are closed-ended funds and do not constitute CIS – the restriction on promotion of CIS set out in [section 238](#) of FSMA does not, therefore, apply. A share in an investment trust is an investment within [article 76](#) of the RAO and accordingly, Part VI of [FSMA](#) (official listing of securities) the [Prospectus Rules](#) and the [Prospectus Regulations 2012 \(SI 2012/1538\)](#) are applicable. (For more information see [Practice note, When is a prospectus required?](#))

A company that obtains HMRC approval as an investment trust is exempt from UK tax on any chargeable gains realised from its portfolio of investments ([see section 100\(1\)](#), Taxation of Chargeable Gains Act 1992). HMRC approval must be obtained for a company to qualify as an investment trust. The application must specify, among other things, the first day of the accounting period in respect of which approval is sought. Once a company becomes an approved investment trust in respect of a particular accounting period then it continues to be treated as approved for all subsequent accounting periods until one or more certain events occur, for example a serious breach of the [Investment Trust \(Approved Company\) \(Tax\) Regulations \(SI 2011/2999\)](#) (as amended) or where the company no longer meets one or more of the eligibility conditions. Approval will only be granted if the company meets certain eligibility conditions and other ongoing requirements. Prior to the 2012 changes to the rules, a company was required to satisfy seven conditions. Under the regime introduced on 1 January 2012, an investment trust must now satisfy three eligibility conditions. The requirements are that:

- All, or substantially all, of the business of the company consists of investing its funds in shares, land or other assets with the aim of spreading investment risk and giving members of the company the benefit of the results of the management of its funds

- The shares making up the company's ordinary share capital (or, if there are such shares of more than one class, those of each class) are admitted to trading on a regulated market
- The company is not a venture capital trust within the meaning of Part 6 of the [Income Tax Act 2007](#) or a company UK REIT within the meaning of Part 12 of the [CTA 2010](#)

The ongoing requirements for investment trust status may be summarised as:

- The company must not be a close company (as defined in [section 439](#) of the CTA 2010)
- The company must not retain in respect of any accounting period an amount that is (generally) greater than 15% of its income for the period.
- The company must notify HMRC if it revises its investment policy
- The company must give notice to HMRC of relevant breaches of the regime

Investment trusts themselves do not need to be authorised persons under FSMA because although they carry out investment activities falling within [article 14](#) of the RAO (that is, dealing in investments), they do so as principals for their own account and qualify for the exemption in [article 15](#) of the RAO. Moreover, no authorisation or approval is required from the FCA to establish an investment trust (although the management of funds and investments is regulated).

Management

Ultimate responsibility for management rests with the board of directors although this is usually delegated to an investment management company that will be regulated by the FCA. The investment manager is usually also responsible for the administrative and company secretarial functions.

Most, if not all, investment trust boards are comprised of non-executive directors and often include representatives of the investment manager. However, the UK Listing Rules require the board of directors of an investment trust to be able to demonstrate that it will act independently of any investment manager and a majority in number of the board must not be directors or employees of, or professional advisers to, the investment manager or any company in the same group as the investment manager.

Custody

The legal ownership of the investment trust's assets will usually be vested in the custodian or its nominee. Unlike an AUT or ICVC, the custodian need not be independent of the manager and a single entity can, in theory, act as both manager and custodian (though this is rare in practice). The beneficial interest in the assets will be vested in the investment trust itself and not in the investment trust's shareholders.

Principal documentation required

- A prospectus complying with the UK Listing Rules
- Memorandum and Articles of Association, which must comply with the requirements of the [Companies Act 2006](#), the UK Listing Rules and [section 842](#) of the Income and Corporation Taxes Act 1988 (ICTA)
- Agreements between the investment trust and its investment manager and any separate administrator or custodian. The investment trust will be a customer of the investment manager and the custodian for FCA purposes

Tax treatment of UK investment trusts

Tax at the level of the investment trust

Investment trusts are treated like any other company within the charge to UK corporation tax except, as mentioned above, that they are exempt from tax on chargeable gains. These include gains arising from investment transactions listed on the "white list".

Investment trusts may elect effectively to remove the corporation tax charge on otherwise taxable income by paying such amounts out as an interest, not a dividend, distribution to investors.

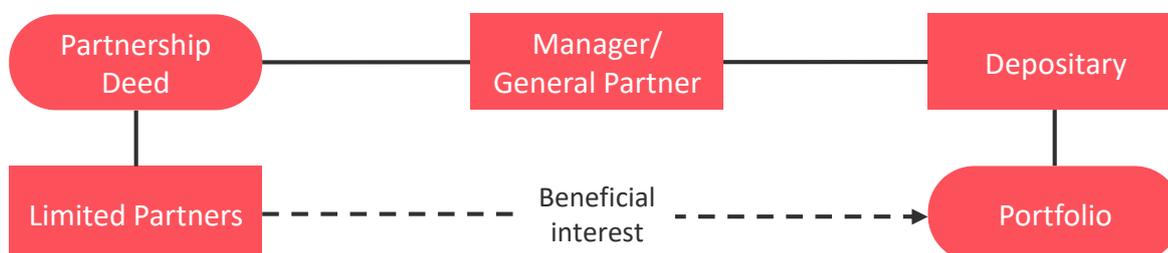
Investment trusts are generally subject to the loan relationships rules in Part 5 of the [Corporation Tax Act 2009 \(CTA 2009\)](#) and the derivative contracts regime in Part 7 of the CTA 2009, subject to special rules for creditor relationships held.

The VAT exemption in Item 10 of Group 5, [Schedule 9](#) to the VATA 1994 effectively exempts from VAT the management of UK investment trusts.

Tax at the level of UK resident UK domiciled investors

Individual investors in an investment trust hold shares in a company. They are therefore generally subject to tax on dividend distributions from their shares or on capital gains realised on the disposal of their shares just as if they held shares in any other company. Dividend distributions are subject to tax at the dividend rates while interest distributions, if the investment trust opts to pay such distributions, are taxed as yearly interest and, as mentioned above, effectively enable the investment trust to move the tax point on relevant income to the investors.

English (unauthorised) limited partnerships



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Definition

A partnership is defined in section 1(1) of the [Partnership Act 1890](#) (the 1890 Act) as "the relation which subsists between persons carrying on a business in common with a view of profit". An English limited partnership is a partnership that is registered as such with the Registrar of Companies under the [Limited Partnerships Act 1907](#) (LPA). It is subject to the specific provisions of the LPA and is governed by the general law affecting partnerships, including both the common law and the 1890 Act. An English limited partnership is not a separate legal entity, although partnerships established in certain foreign jurisdictions may be recognised as such. All English limited partnerships that are operated as investment vehicles are potentially AIFs for the purposes of the [AIFMD](#).

A limited partnership must have at least one general partner with unlimited liability. The remainder of the partners are limited partners who enjoy limited liability so long as they do not participate in the management of the partnership's business.

A limited partnership is a common vehicle for venture capital funds established in the UK because of its tax transparency and its relatively flexible structure, given that it is not subject to the complications of company law or FCA rules. It acquires and manages investments that are owned collectively by the partners as partnership assets. The general partner usually acts as the investment manager, but this function is sometimes delegated by the general partner to a third party.

UK limited partnerships are potentially CIS whether they are open-ended or closed-ended. [Section 235](#) of FSMA is wide enough to include limited partnerships formed under the LPA (unlike straightforward

partnerships) since the limited partners do not maintain day-to-day control over the management of the partnership property. If the general partner of a limited partnership manages the investments in the UK, the general partner must be an authorised person under FSMA.

Registration

The registration of a limited partnership involves sending a statement to the Registrar of Companies in the part of the UK in which the principal place of business of the limited partnership is to be situated. The statement, which is signed by the partners, must be sent before the partnership commences business or incurs any liabilities and must contain certain particulars.

The Registrar of Companies maintains a register of limited partnerships and all of the statements registered in relation to them. On receiving any statement, the Registrar of Companies files and posts a certificate of registration to the firm from which it was received. Filed statements are available for public inspection.

In order to be registered, the principal requirements that must be satisfied are that:

- There are one or more persons who are liable for all the debts and obligations of the firm (usually a single general partner).
- The principal place of business of the partnership must be in the UK.

Principal documentation required

- A limited partnership deed between the limited partners and the general partner
- An application to the Registrar of Companies ([Form LP5](#)) to register a limited partnership
- An offering memorandum/subscription agreement between the limited and general partners

Private fund limited partnerships

On 6 April 2017, the [Legislative Reform \(Private Fund Limited Partnerships\) Order 2017 \(SI 2017/514\)](#) (the Order) came into force, amending the LPA and creating the private fund limited partnership (PFLP) as an alternative to the existing limited partnership.

The PFLP is designed for private investment funds and is intended to offer a more flexible vehicle for fund managers by reducing certain administrative and financial burdens associated with the existing limited partnership vehicle (although the existing vehicle will continue to be available).

In consequence, the PFLP is less burdensome administratively, so reducing the number and content of public filings that are required; it offers investors greater clarity as to what actions LPs can undertake without risking their limited liability; and it removes the capital rules requiring LPs to contribute capital to the partnership upon their admission as well as those that restrict repayment of the capital contribution before the end of the fund's life.

For more information, see [Practice note, Private fund limited partnerships \(PFLPs\)](#).

Designation as a PFLP

In order for a new or existing limited partnership to be designated as a PFLP, the partnership must be constituted by an agreement in writing, and must be a CIS as defined in [section 235](#) of FSMA.

Provided these conditions are met, the general partner may make an application for designation of the fund as a PFLP either at the time of registration of the limited partnership or at any time thereafter. However, it would appear that, if a fund is designated as a PFLP, it cannot subsequently be converted back to a limited partnership.

A new fund seeking designation as a PFLP must complete Form LP7, providing:

- The name and signature of each general partner
- The name and signature of each limited partner
- The address of the principal place of business of the PFLP

An existing fund seeking designation as a PFLP must use Form LP8, providing:

- The registered number of the fund
- The date of registration of the fund

- The name and signature of each general partner
- The address of the fund's principal place of business

Key changes made to the LPA

- **Public filings.** PFLPs are exempt from the requirement to advertise transfers of limited partnership interests in the Gazette in order for such transfers to take effect. Equally, Form LP6, used to notify Companies House of certain changes to the limited partnership, has been amended so that PFLPs no longer need to make a filing either to reflect a change in the PFLP's term or character, to reflect a change in the nature of the PFLP's business, or to specify an increase in capital contributions made (or by whom).
- **Capital contributions.** In order to be admitted as a limited partner under the LPA, a capital contribution must be made to the partnership and this cannot be withdrawn before the end of the fund's life. As a result, limited partnerships have traditionally been structured with only a nominal capital contribution (usually around 0.01% of the commitment) together with a much larger loan commitment.

For a PFLP registered on or after 6 April 2017, the requirement for limited partners to make a capital contribution has been removed, as has the rule that restricts withdrawal of capital contributions before the end of the fund's life. Limited partners will simply be able to make capital contributions to the PFLP over time, as is already the case with limited partnerships in many other jurisdictions.

However, an existing limited partnership registered before 6 April 2017, but which has subsequently been designated as a PFLP, is treated slightly differently. Capital contributions made before the fund was designated as a PFLP are subject to the old rules under the original LPA and cannot therefore be returned during the life of the fund, while those made subsequent to the fund's designation as a PFLP are subject to the amended rules. In principle, then, those contributions can be returned to the limited partners before the end of the fund's life albeit subject to the terms of the fund's limited partnership agreement.

- **Limited liability.** A key concern of many limited partners has been the extent to which they can be involved in the affairs of the partnership without being seen as participating in the "management of the limited partnership's business" and thereby losing their limited liability. In respect of PFLPs (but not other limited partnerships), the Order introduces a "white list" of activities which will not, by themselves, constitute participating in management.

The white list is broad - a limited partner will, for example, be able to take part in a decision approving an action to be taken by a general partner, manager or adviser, including for the acquisitions and disposals of investments or act as an advisory board member or as a director, member, employee, officer, agent, shareholder or partner of or in a general partner, manager or adviser of the PFLP (provided, in both cases, that that person is not taking part in management of the partnership business).

Tax treatment of unauthorised English limited partnerships

The following applies to English limited partnerships that are not ACS, including PFLPs. For a discussion on English limited partnerships that are ACS, see [ACS: limited partnership scheme](#) above.

English limited partnerships are treated as transparent for UK tax purposes in respect of both income and capital/chargeable gains and are not, therefore, separate taxable entities for such purposes.

All activities carried on by the limited partnership are, therefore, for UK income and capital gains tax purposes treated as being carried on by the partners, not the limited partnership.

HMRC, therefore, looks through the limited partnership for UK income, capital gains and corporation tax purposes and treats the limited partners as if they were directly holding the underlying assets in proportion to their respective interests in the partnership. This means that there is no UK income, capital gains or corporation tax at the level of the limited partnership itself and the tax treatment of UK resident UK domiciled individual investors in the limited partnership is the same as if they held the relevant underlying property directly. Schedule 1 to the Finance Act 2019 extends the charge to capital gains tax and corporation tax on gains made by non-UK residents on disposals of all UK immovable property from 6 April 2019. Consequently, non-UK resident partners will be liable to UK tax on their share of any gain realised on a disposal of UK immovable property by the limited partnership (see [Practice note, Disposals of UK immovable property by non-UK residents from 6 April 2019](#)).

Special rules apply in relation to changes in limited partnership interests.

Since unauthorised English limited partnerships are not special investment funds for the purposes of Items 9 or 10 of Group 5 in [Schedule 9](#) of VATA 1994, management services received by the limited partnership are not within the exemption from UK VAT in such items.

European long-term investment funds (ELTIFs)

What is an ELTIF?

ELTIFs were introduced by the [ELTIF Regulation](#), the aim of which was to create a cross-border framework for long-term investments in order to stimulate demand from institutional and/or retail investors for assets requiring "patient capital". To this end, the ELTIF Regulation establishes rules and restrictions on the authorisation, investment policies, and operating conditions of EU AIFs that may be marketed as ELTIFs. The ELTIF Regulation came into effect on 9 December 2015.

ELTIFs operate within the regime introduced under the [AIFMD](#). The manager of a UK ELTIF must be authorised by the FCA as a full-scope UK AIFM, while the ELTIF itself must also be authorised as a fund, again by the FCA.

The ELTIF Regulation enables EU-authorised AIFMs to market EU AIFs that they manage as ELTIFs to both professional investors (as defined under the [MiFID II Directive](#)) and, subject to certain additional requirements, to retail investors across the EU. Suitably authorised managers are able to make use of an EU-wide passport, subject to a notification procedure established under the AIFMD.

Although, as an EU regulation (rather than a directive), the ELTIF Regulation's provisions apply directly without the need to be transposed into each member state's law, adaptations to the UK's regulatory framework were necessary for the ELTIF Regulation to function properly in the UK. These changes were brought about through the [European Long-term Investment Funds Regulations 2015 \(SI 2015/1882\)](#) and the introduction of a new section of the FCA Handbook, FUND 4.2.

For more information, see [Practice notes, ELTIF Regulation: overview](#).

Eligible investments

ELTIFs may only invest in:

- "Eligible investment" assets (see [Investment restrictions](#) below)
- Assets permitted under Article 50(1) of the [UCITS Directive](#) (UCITS assets)

At least 70% of the ELTIF's capital must be invested in eligible investment assets.

In addition, ELTIFs:

- Cannot engage in short selling.
- Must observe strict limitations on their use of borrowing, leverage and derivatives.

Investment restrictions

"Eligible investment assets", as defined in article 10 of the [ELTIF Regulation](#), include (but are not limited to):

- Equity or quasi-equity instruments issued by a qualifying portfolio undertaking (see below) and acquired directly from the qualifying portfolio undertaking by the ELTIF or via the secondary market
- Debt instruments issued by a qualifying portfolio undertaking
- Loans granted by the ELTIF to a qualifying portfolio undertaking with a maturity no longer than the life of the ELTIF
- Direct or indirect holdings via a qualifying portfolio undertaking of individual real assets with a value of at least EUR 10 million

A "qualifying portfolio undertaking" is an undertaking that:

- Is not a "financial undertaking" (that is, it is not a credit institution, a MiFID investment firm, an insurance undertaking, a financial holding company, a mixed-activity holding company as defined in the [Capital Requirements Regulation](#) (Regulation 575/2013) (CRR), a UCITS management company or an AIFM)
- Either:
 - is not admitted to trading on a regulated market or multilateral trading facility (MTF) as defined in MiFID/[Markets in Financial Instruments Regulation](#) (Regulation 600/2014) (MiFIR); or
 - is admitted to a regulated market or MTF and has a market capitalisation of no more than EUR 500 million
- Is established in an EU member state or in a third country that:
 - is not a Financial Action Task Force (FATF) high risk and non co-operative jurisdiction
 - has signed an agreement with the ELTIF manager's home member state and with each other member state in which the ELTIF is intended to be marketed to ensure that the third country fully complies with the standards set out in Article 26 of the OECD Model Tax Convention on Income and Capital and ensures an effective exchange of information in tax matters

An ELTIF cannot invest more than:

- 10% of its capital in instruments issued by, or loans granted to, any single qualifying portfolio undertaking
- 10% of its capital directly or indirectly in a single real asset
- 10% of its capital in units or shares of any single ELTIF, European venture capital fund (EuVECA) or European social entrepreneurship fund (EuSEF)
- 5% of its capital in UCITS assets where those assets have been issued by a single body

Where the ELTIF breaches the above diversification requirements and the contravention is beyond the control of the ELTIF manager, the manager must rectify the position, "in an appropriate time period", taking due account of the interests of the ELTIF's investors.

Borrowing restrictions

The ELTIF manager must specify in the ELTIF's prospectus whether or not it intends to borrow cash as part of its investment strategy.

An ELTIF may not borrow more than 30% of its own capital and borrowings must, in general, be used to invest in eligible investment assets where the ELTIF's own cash or cash equivalent holdings are insufficient to acquire the assets.

Redemption

Investors in an ELTIF will not ordinarily be able to redeem their units or shares before the "end of life" of the fund, although redemptions may be made earlier than this if a number of conditions (set out in Article 18(2) of the [ELTIF Regulation](#)) are met. These include the manager of the ELTIF setting out a defined policy that clearly indicates the periods of time during which investors may request redemptions.

The "end of life" of an ELTIF is a specific date, which must be clearly disclosed to investors and indicated in the ELTIF's rules or instruments of incorporation. The life of an ELTIF must be consistent with its long-term nature and must be sufficiently long to cover the life-cycle of each of the fund's individual assets.

Redemption to investors must commence on the day following the end of the ELTIF's life and investors must always have the option to be repaid in cash.

The ELTIF must adopt an itemised schedule for the orderly disposal of its assets to redeem investors at its life's end. The details that such a schedule must contain are set out in [Commission Delegated Regulation](#) (EU) 2018/480 supplementing the ELTIF Regulation. The schedule must be disclosed to the relevant regulator at least one year before the ELTIF's end of life.

As a result of the redemption provisions, it is unlikely in practice (though not impossible) that a UK ELTIF would be set up as an ICVC. However, an ELTIF could amount to a CIS for the purposes of [section 235](#) of FSMA if it meets the requirements set out in that section (see [What is a collective investment scheme?](#) above).

Marketing

To market a UK ELTIF to professional and retail investors in the UK, the ELTIF manager must notify the FCA in accordance with Article 31 of [AIFMD](#).

The ELTIF Regulation also contains a passport regime, under which the manager of an ELTIF can market a fund to professional and retail investors in member states other than the ELTIF's home member state upon notification to its home regulator in accordance with Article 32 of [AIFMD](#).

As well as any documentation and information required under Articles 31 or 32 of the AIFMD, the manager must provide the regulator with:

- The ELTIF's prospectus
- The partnership agreement (where relevant)
- Its KID (where it is marketing to retail investors)
- Information on facilities that the ELTIF's manager must put in place (see below)

The manager must inform the regulator whether or not it intends to market the ELTIF to retail investors.

Additional provisions applicable where the ELTIF is to be marketed to retail investors

- Where the ELTIF is to be marketed to retail investors, the manager must:
- Have in place, in each member state in which it intends to market the ELTIF, facilities for making subscriptions, making payments to investors, repurchasing or redeeming units or shares and making available the information that the ELTIF and/or the manager must provide. (Level 2 measures to specify the characteristics of such facilities are set out in [Commission Delegated Regulation](#) (EU) 2018/480.)
- When [Directive \(EU\) 2019/1160](#) on the cross-border distribution of funds comes into effect on 2 August 2021, member states will no longer be able to require that an ELTIF provides these facilities by means of a physical presence in the member state.
- Establish a process for assessing whether the ELTIF is suitable for distribution to retail investors, taking into account the lifecycle of the ELTIF and its intended investment strategy.
- Where the ELTIF is being distributed directly, obtain information necessary to ensure that the ELTIF is suitable for the retail investor. This will include information on the investor's knowledge and experience in the investment field relevant to the ELTIF, their financial situation (including their ability to bear losses) and their investment objectives including their time horizon.
- Where the ELTIF has a lifecycle of ten years or more, issue a clear written alert that the product may not be suitable for retail investors unable to sustain such a long term and illiquid commitment.
- Provide retail investors with "appropriate investment advice".
- Establish appropriate complaint procedures that allow retail investors to file complaints in the official language of their own member state.

Where the manager has performed the suitability test referred to above and has provided appropriate investment advice, but the potential retail investor's portfolio does not exceed EUR 500,000, the manager must also ensure that the investor does not invest more than 10% of its portfolio in ELTIFs, provided that the initial minimum amount invested in one or more ELTIFs is EUR 10,000.

Disclosure of costs

Article 25 of the ELTIF Regulation requires the development of Level 2 measures to determine the costs disclosure requirements applicable to ELTIFs. ESMA set out its original proposals in a [consultation paper](#)

(ESMA/2015/1239) published in July 2015. However, since the ELTIF Regulation also specified that this work should take into account the equivalent Level 2 measures under the PRIIPs Regulation, it was determined that the PRIIPs measures should be finalised before ESMA's work to develop those under the ELTIF Regulation could continue.

The corresponding PRIIPs Delegated Regulation was published in April 2017 but is in the process of being revised by the European Supervisory Authorities (the EBA, EIOPA and ESMA).

In March 2019, ESMA, therefore, published a second ([consultation paper](#) ESMA34-46-89) putting forward amended proposals. Following the closing of the consultation period in June 2019, ESMA will consider responses and submit final draft measures to the Commission for endorsement and subsequent publication.

AIFM and depositary

The [ELTIF Regulation](#) requires the appointment of a manager and depositary, in line with the [AIFMD](#), and the manager and depositary must comply with both AIFMD and the ELTIF Regulation.

In the UK, a full-scope UK AIFM wishing to manage an ELTIF must obtain Part 4A permission from the FCA to manage an authorised AIF, while the depositary will require Part 4A permission to act as a depositary of an authorised AIF.

Additional requirements apply in respect of the depositary where the ELTIF is marketed to retail investors. In this situation, the depositary:

- Must be a type of entity permitted to be a depositary under the [UCITS Directive](#) (as amended by [UCITS V](#))
- Cannot exclude liability or limit it by agreement; any agreement that contravenes this provision will be void
- Cannot discharge itself of liability in the event of a loss of financial instruments held in custody by a third party
- Must comply with restrictions on the re-use of the assets held in custody.

Consequences of authorisation

In order to avoid all the requirements for an authorised AIF applying to an ELTIF's manager or depositary, the FCA's definition of an "authorised fund" has only limited application to a UK ELTIF.

So, while ELTIFs are funds that will be authorised by the FCA, the UK regulator does not regard them (for most purposes) as being "authorised funds" (that is, as defined under [FSMA](#)) since they are created under, and are subject to, the [ELTIF Regulation](#) rather than FSMA. (An authorised fund, as defined in the FCA's Glossary, is an open-ended collective investment scheme authorised by the FCA in accordance with Part XVII of [FSMA](#).) As a result, although a UK ELTIF could be established as a unit trust, as a co-ownership scheme or, perhaps most likely in the UK, as an English Limited Partnership, it is unlikely to be an AUT or an ACS for FCA purposes. As mentioned above, because of the redemption provisions in the ELTIF Regulation, it is unlikely in practice (though, it would appear, technically not impossible) that a UK ELTIF would be set up as an ICVC.

Principal documentation required

- An instrument of incorporation or, where the ELTIF is a company, a memorandum and articles of association
- A prospectus
- Where the ELTIF is marketed to retail investors, a KID
- Contracts between the ELTIF and its manager and its depositary

Tax treatment of ELTIFs

The [ELTIF Regulation](#) is silent on the tax treatment that should apply to an ELTIF and its investors. Accordingly, it will be a matter for member states to determine how ELTIFs should be taxed. Although the UK tax authorities have not made any announcement concerning the treatment of UK ELTIFs, one might expect that the starting position would depend on the legal form adopted by the ELTIF, for example, if it is established as a limited partnership, one might expect it to be treated as a tax transparent entity for UK tax purposes.

A comparison of different UK funds

Feature	AUT	Authorised OEIC	ACS	Investment trust	English limited partnership	ELTIF
Legal structure	Trust	Company	Contractual scheme (in the form of either a co-ownership scheme or a limited partnership scheme)	Company	Partnership	Any form permitted Partnership or ACS most likely
Separate legal personality	No	Yes	No	Yes	No	Not necessarily
Open/closed ended	Open-ended	Open-ended	Open-ended	Closed-ended	Either	Closed-ended
Investor's holding	Units	Shares	Units	Shares	Interests	Units or shares
Pricing system	Dual or single price	Dual or single price	Dual or single priced	Dual price	Dual or single price	Dual or single price
Stock Exchange listing?	Not listed in practice	Not listed in practice	Not listed in practice	Must be London listed	No	Not likely to be listed
CIS?	Yes	Yes	Yes	No	Yes	Yes
Management	Authorised Fund Manager	Authorised Fund Manager (usually an ACD as the sole director that is responsible for day-to-day management)	Authorised Contractual Scheme Manager	Board of directors Usually delegated to investment fund manager	Usually a manager is appointed by the general partner	Alternative investment fund manager (UK or passported)
Who holds portfolio	Trustee/Depository on behalf of unitholders	Depository on behalf of the OEIC	Depository on behalf of participants (in the case of a co-ownership scheme) or on behalf of the limited partners (in the case of a limited partnership scheme)	Custodian/Depository on behalf of the investment trust	Custodian/Depository on behalf of the limited partners	Depository on behalf of unitholders
Is the fund / manager / trustee / depository regulated?	Manager, trustee and fund	ACD, depository and fund	Manager, general partner (in the case of a limited partnership scheme), fund and depository	Manager and custodian, fund (Companies Act, Listing Rules and HMRC approval)	General Partner/Custodian/Manager	Manager, depository and fund
How is the fund constituted?	Trust deed	Instrument of Incorporation	Contractual scheme deed (in the case of a co-ownership scheme) or partnership deed (in the case of a limited partnership scheme)	Memorandum and Articles of Association	Partnership agreement	Depends on legal structure chosen
How is price determined?	NAV	NAV	NAV	Market forces	Valuation principles	Valuation principles
UK tax treatment at fund level	Exempt from tax on chargeable gains; may be subject to corporation tax at 20% on income	Exempt from tax on chargeable gains; may be subject to corporation tax at 20% on income	Co-ownership scheme: not taxable on capital/chargeable gains, transparent for income and corporation tax on income. Partnership scheme: transparent for capital/chargeable gains and income and corporation tax on income	Exempt from tax on chargeable gains; may be subject to corporation tax on income	Transparent; not taxable	Will depend upon legal form of ELTIF and any specific legislation

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