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Offshore Funds  
The Tax Advisor's Role and Recent Case Studies

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# Scope of Lecture

- An update on the current state of the market
- Focus on offshore funds
- Structuring issues
- Tax considerations
- Case studies
- Q&A

# Update

- Investment funds have taken a hit - like the rest of us
  - High risk investments and high management fee structures have had a negative impact
  - Lack of capital
  - Lack of liquidity in the markets
  - Possible green shoots? Perhaps...
- 
- Clear business and investment strategy vital
  - Route to market
  - Distribution
  - Believable returns
  - KISS tax structure

# The Monkey Test

## *"Sorting the wheat from the chaff"*

Does the promoter have any of the following:

- Track record?
- Business plan?
- Exit strategy?
- Cornerstone investor?
- Seed capital?
- Fee awareness?

If not.....they have failed the 'Monkey Test'.

# Alternative Asset Classes

- Real estate (commercial / residential / development)
- Private equity
- Finance / Mezzanine finance
- Film finance
- Art / Emotional assets

# Tax Planning Objectives

- No taxation of the fund entity
- Minimise taxation on asset class / source
  - DTTs
  - EU Directives
  - Finance
  - Hybrids
- Minimise tax leakage on profit distributions to the fund
- Ensure no additional taxation to investors
- Management structure
- Performance fee / carried interest

# Fund Entity

- Choice of entity can be crucial to the success of the fund
- Various entities can be used as the fund vehicle:
  - Unit trusts
  - Limited partnerships
  - Limited companies
  - Protected cell companies
  - Incorporated cell companies
- KISS - is a cell company too complex?
- Key objectives are:
  - Administrative ease
  - Investor acceptance

# Fund Jurisdiction

- A Pandora's Box:
  - Channel Islands
  - Isle of Man
  - Cayman
  - Ireland
  - Luxembourg
  - Malta
- Differentiating factors include:
  - EU Status
  - 'Light touch' regulation
  - Time zone

# Key Tax Considerations

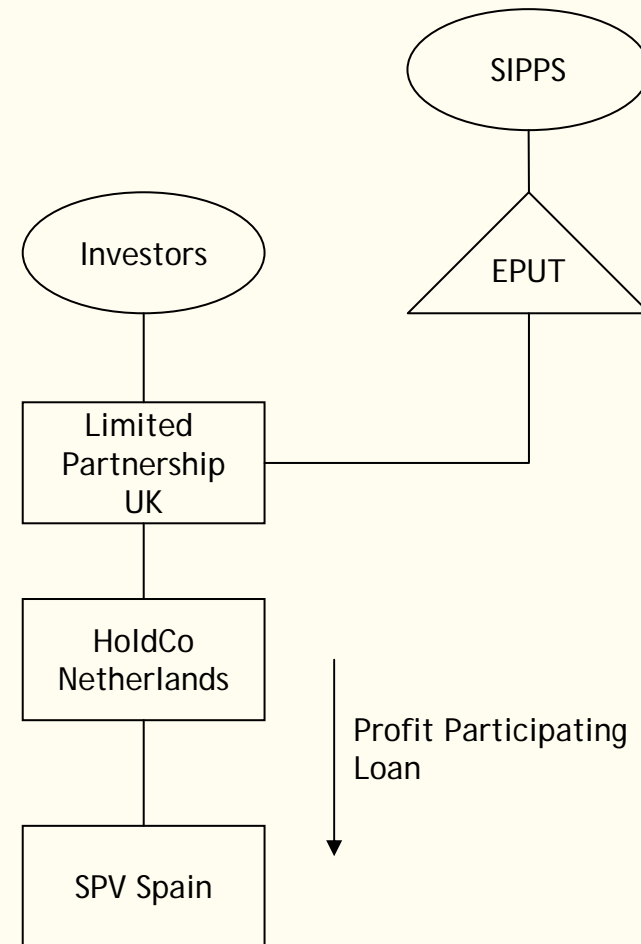
- Internal rate of return vital to fund success
- Tax leakage and management is the key
- Detailed planning is essential
- What is the asset that is being invested in?
- What is the return: income, capital gains, interest, royalties?
- Long term yields or capital growth?
- Exit strategy - sale of company or assets?
- Financing techniques and internal debt very useful
- Hedging arrangements - currency risks often overlooked

## The “Achilles Heel”

- Management and control
- Residency of the board
- Experience of the board
- Regular formal meetings take place in relevant jurisdiction
- Investment advisors should advise and not manage
- Bank account operated abroad
- Intermediary and SPV companies should be properly managed and controlled
- Documents should reflect the above

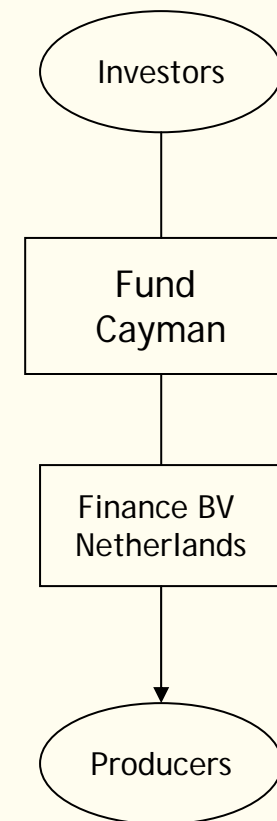
# Spanish Real Estate

- Investors invest via a tax transparent UK LP
- SIPP investors invest via an EPUT feeder
- Netherlands used for NL/SP DTT
- Exit at:
  - Spanish property level; or
  - HoldCo level
- Dutch participation exemption used for share sale exit
- Profit participating loan (PPL) to reduce tax base in Spain if property sold
- PPL allows classic double dip
- Transfer pricing an issue as are Spanish thin cap rules
- Beware Art 17,3 of Dutch Tax Code
- Beware new UK 'Offshore Fund' Rules



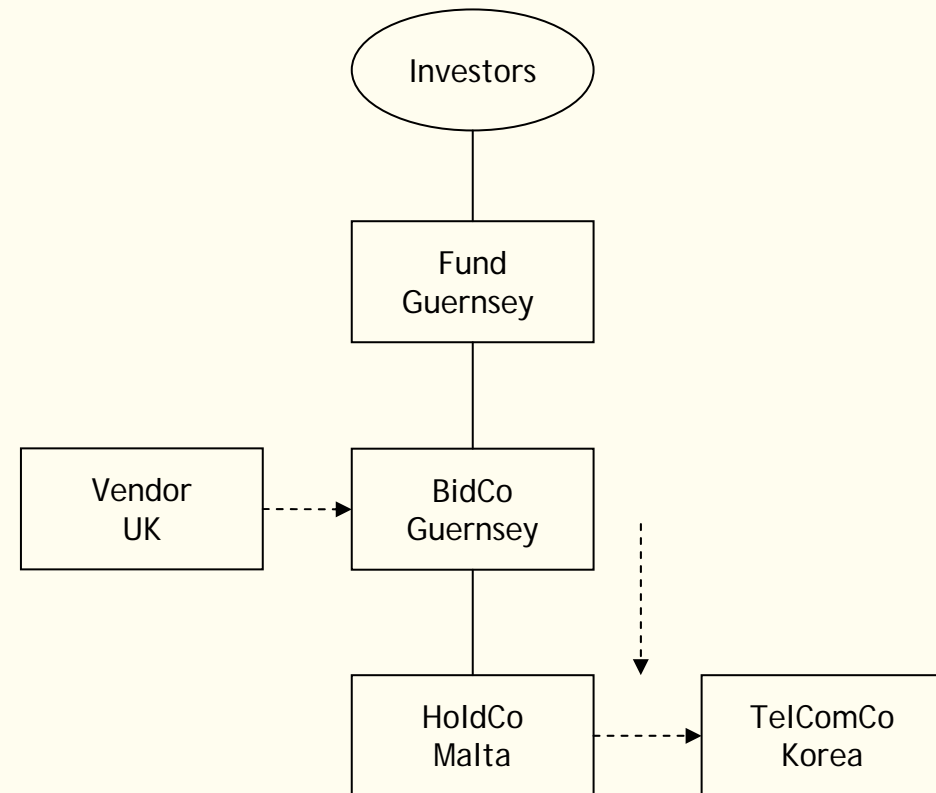
# Film Gap-Finance Fund

- Cayman SPC established to provide high-interest, short term loans to film producers in Europe and US
- But: cash repatriation to Cayman can create additional tax costs
- Dutch Finance BV was chosen because:
  - Excellent DTA network
  - Nominal effective rate on spread earned in BV
  - No withholding tax on outbound payments to Cayman
  - Availability of advance tax rulings
- Mitigate application of specific Dutch anti-avoidance rules
- *Indofood* case - conduit companies and treaty benefits
- US portfolio interest exemption



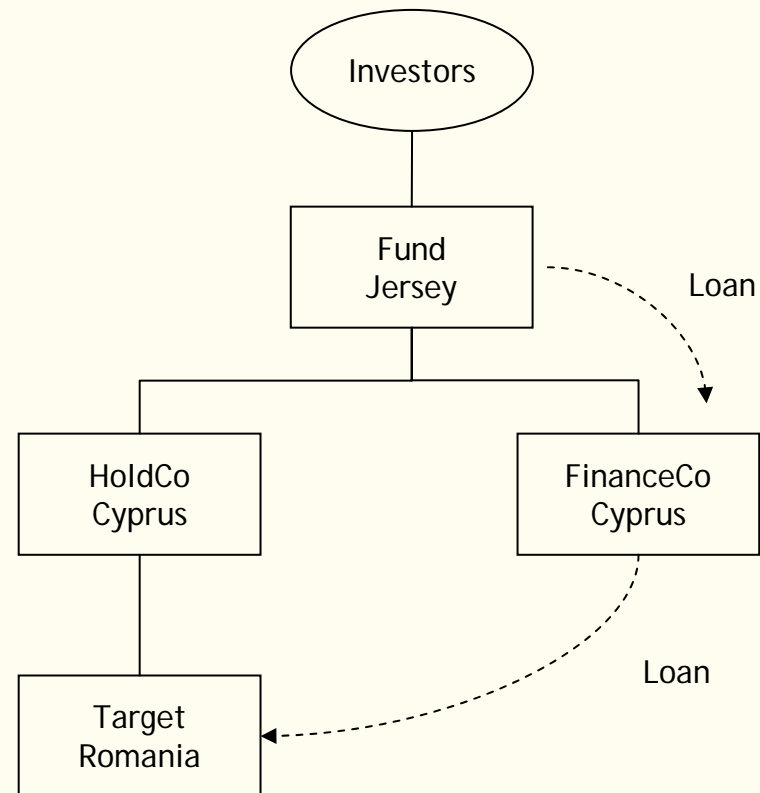
# Private Equity / Patent Acquisition

- Acquisition of a business and IPRs (patents) from UK Vendor by BidCo Guernsey
- BidCo hives down certain valuable patents to HoldCo in Malta crystallising a dry gain in Guernsey using inter-company loan
- Malta on-sells these assets to TelComCo realising a gain subject to 35% CIT
- Payment from Korea is classified as a royalty even though it is an outright acquisition
- Malta/Korea reduces WHT from 20% to nil
- Application of 6/7 reduction gives ERT of 5%
- No withholding tax from Malta to BidCo



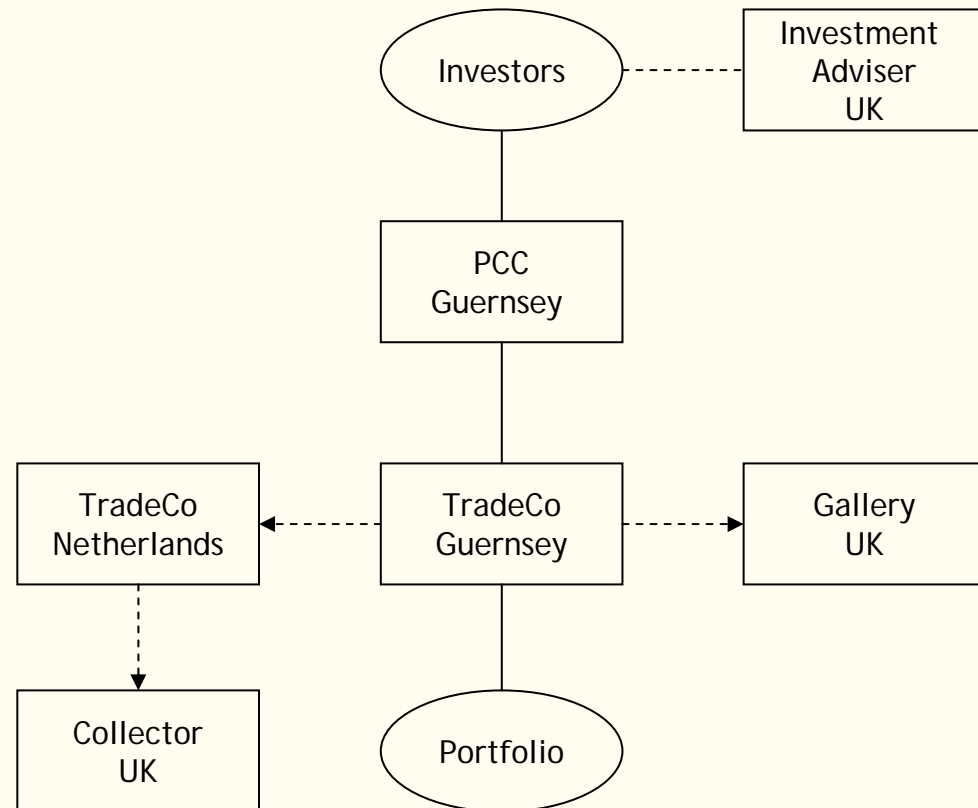
# Romanian Acquisition

- Cyprus used because:
- DTA with Romania
- Tax free sale of target shares
- EU Directive allows repatriation
- Minimal margins permitted
- Effective tax rate on spread (0.035 - 0.05%)
- Two companies used to ensure full deductibility at Cyprus level
- Equity contribution not deductible



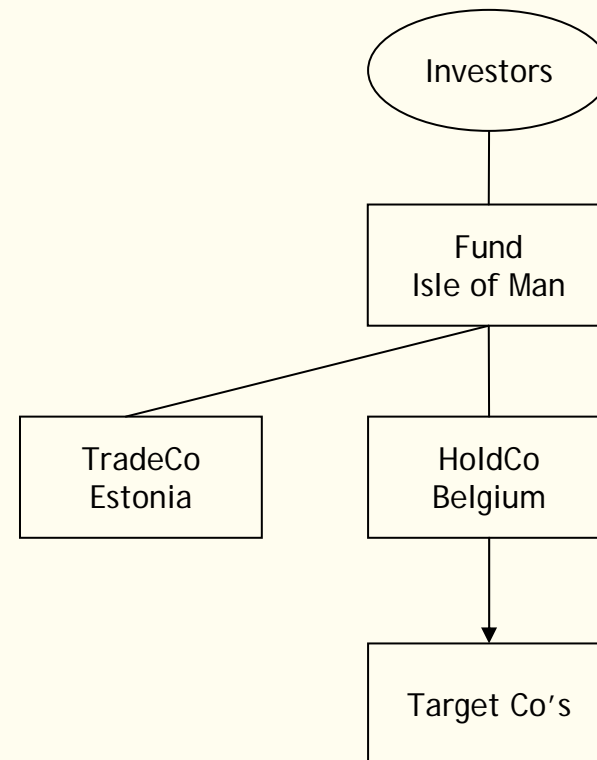
# Art Fund

- Protected cell company used to allow future diversification into other genres
- TradeCo Guernsey used to avail of UK DTA to prevent p.e. at UK galleries
- TradeCo Netherlands used to avoid 'effectively connected income' on consignment to the US



## The Isle of Man / Belgium Connection

- IoM now has OECD DTT with Belgium
- Zero WHT on:
  - Dividends
  - Interest
  - Royalties
- Belgian participation exemption and DTT network make an ideal 'fit' with IoM



# Thank You

- Any questions - please ask!