

**SPV regime in AIFC**

# Dealing on own account is an “investment activity” under MiFID II

Article 2(1)(d) of MiFID II **exempts** persons **dealing on own account** in financial instruments from the requirement **to be authorised** as a MiFID investment firm.

'**Dealing on own account**' takes place when a firm puts its own books at risk (ESMA Consultation Paper Guidelines).

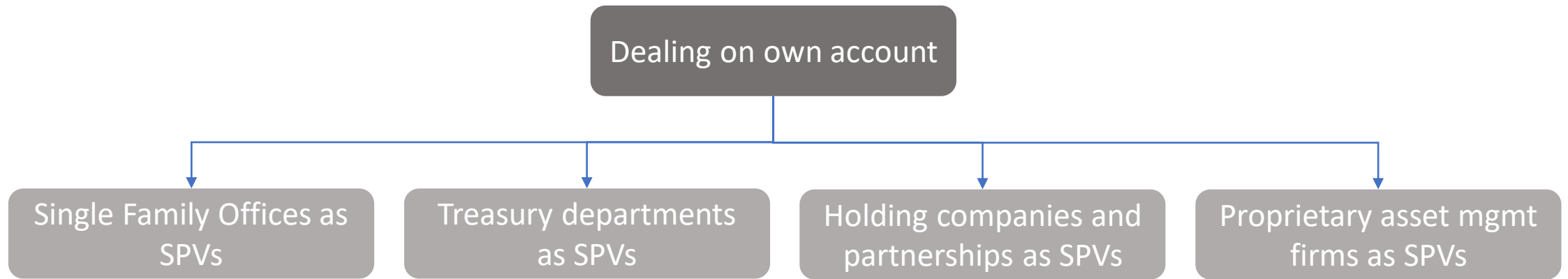
Persons using dealing on own account exemption are not allowed to provide any other investment services and/or perform any other investment activities in financial instruments.

## SECTION A Annex I MiFID II

### Investment services and activities

1. Reception and transmission of orders in relation to one or more financial instruments;
2. Execution of orders on behalf of clients;
- 3. Dealing on own account;**
4. Portfolio management;
5. Investment advice;
6. Underwriting of financial instruments and/or placing of financial instruments on a firm commitment basis;
7. Placing of financial instruments without a firm commitment basis;
8. Operation of an MTF;
9. Operation of an OTF.

# Dealing on own account in regard to AIFC



Dealing in own account also related to family or privately held business, especially single family offices, holding companies and partnerships, proprietary asset management that can be structured in form of SPVs.

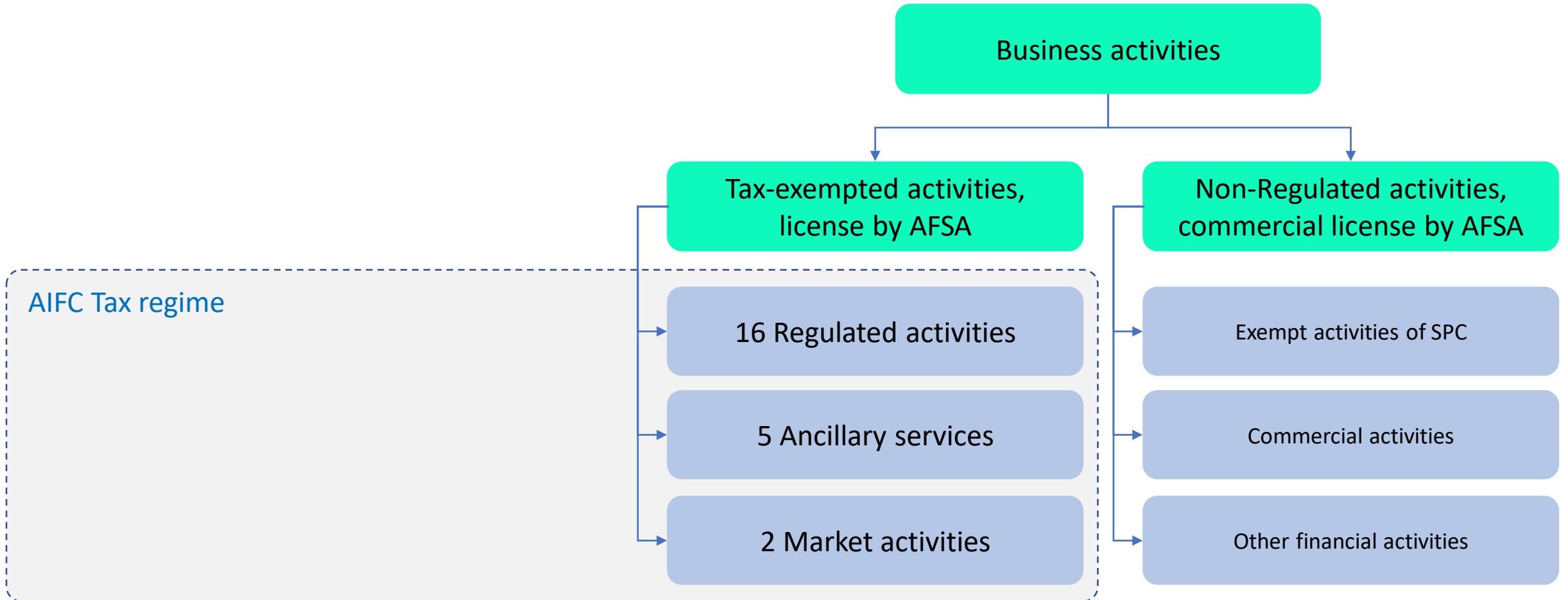
In recent times, family offices have become highly significant on the global economic landscape. According to the Global Entrepreneurs Council, about 70% of all companies in the world are family businesses.

In this respect, CIS is not an exception: large part of the private sector activity is run by family groups.

Particularly, in Kazakhstan the vast majority of companies are family businesses where the family members are trusted more than anyone else.

AIFC plans to develop a private wealth market and it is very important to address the needs of family run entities and create conditions to set up their legal structures in AIFC.

# Current AIFC Tax Regime





# Problem #1

## Taxes on SPV activities in AIFC

Current situation in financial activities in AIFC

### Exempt activities of SPC in AIFC:

Acquisition

Holding and the disposal of any asset

Obtaining of any type of financing

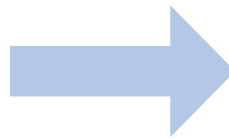
Granting of any type of security interest over its assets

Providing of any indemnity or similar support

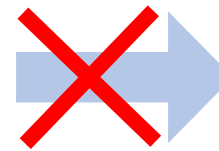
Entering into any type of hedging arrangements

Financing of the Initiator or another SPC

Acting as trustee or agent for any participant in the Transaction



Not financial activity under AIFC GEN Rules



No tax exemption for SPVs of:

Single Family Offices

Treasury departments

Holding companies and partnerships

Proprietary asset management firms



# Proposal #1

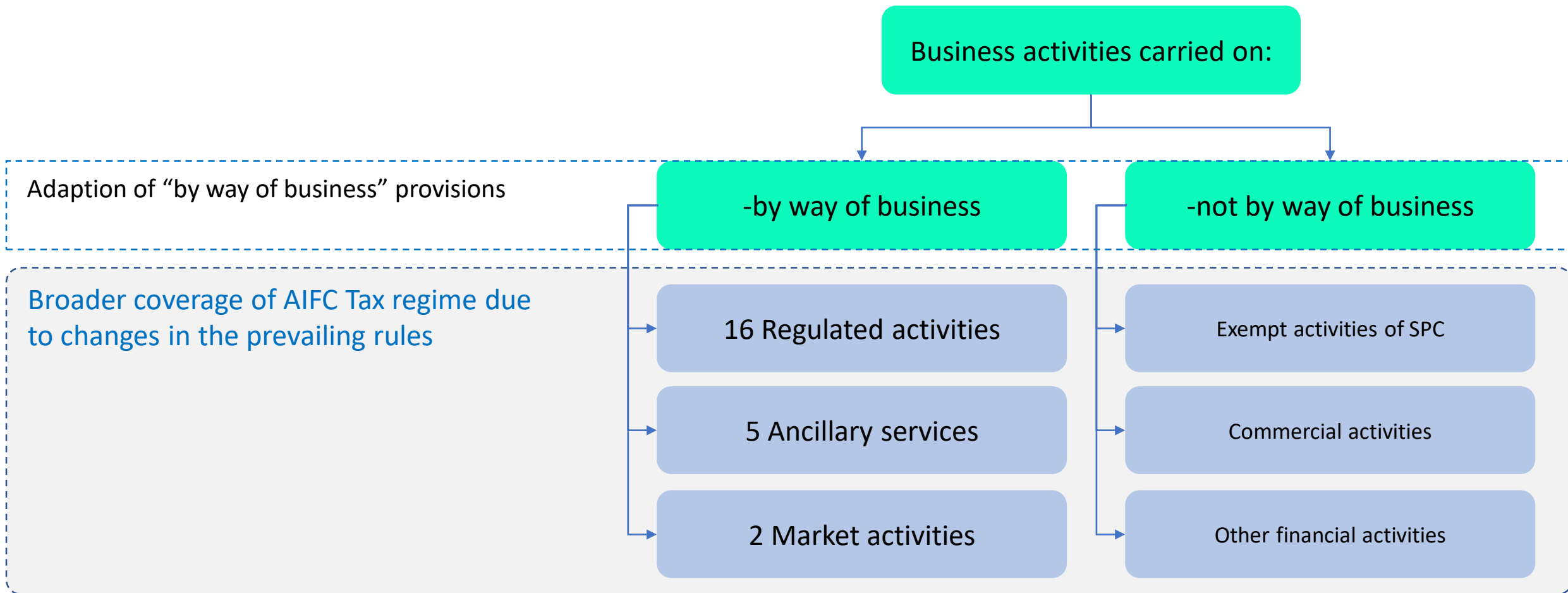
**In order to develop AIFC SPV regime:**

**We need to adapt the “by way of business” test provisions (ADGM model) where:**

One or several of the Single Family Office, SPV, proprietary asset management, intercompany operations and other related activities declared in the application can be considered as a financial service carried on not by way of business and thus the applicant (the following should be exactly prescribed in AIFC rules):

- 1) can claim for a tax exemption;
- 2) can apply for a typical commercial license and thus doesn't have to comply with higher reporting and capital requirements of Regulated activities.

# Proposed AIFC Tax Regime



# “By way of business” compliance with AIFC Tax regime

Are there any tax exemption on activities carried on NOT by way of business in AIFC?

Financial activities carried on NOT by way of business comply with the Constitutional statute on the AIFC. It is not specified, whether a single family office or a proprietary investment firm may carry on prescribed financial activities in AIFC by way of business or not by way of business:

## Article 1. Definitions used in this Constitutional Statute

5) AIFC Participants means legal entities registered under the Acting Law of the AIFC and legal entities recognized by the AIFC;

It does not specify whether the legal entity is Authorised Firm or not

## Article 6. Tax regime in the AIFC

3. Until 1 January 2066, AIFC Participants are exempt from corporate income tax on income received from providing the following financial services in the AIFC:

It does not specify whether the activity is Regulated or not

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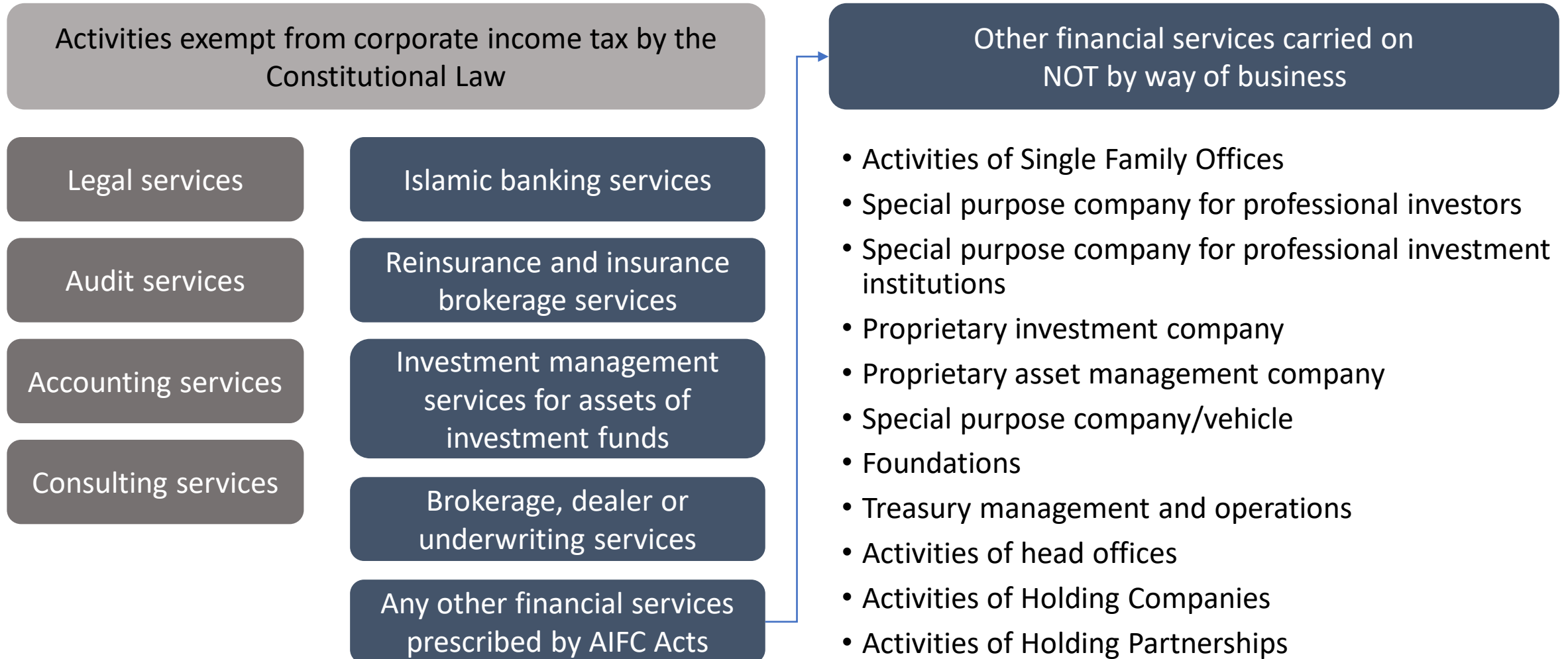
5) any other financial services prescribed by AIFC Acts.

Thus we can add other financial services that can be carried on NOT by way of business



# “By way of business” compliance with AIFC Tax regime (cont.)

According AIFC Act No. 38 of 2017 “Financial services exempt from corporate income tax” other financial services carried on NOT by way of business can be added to AIFC General Rules Schedule 1.



**“By way of business” test in ADGM**

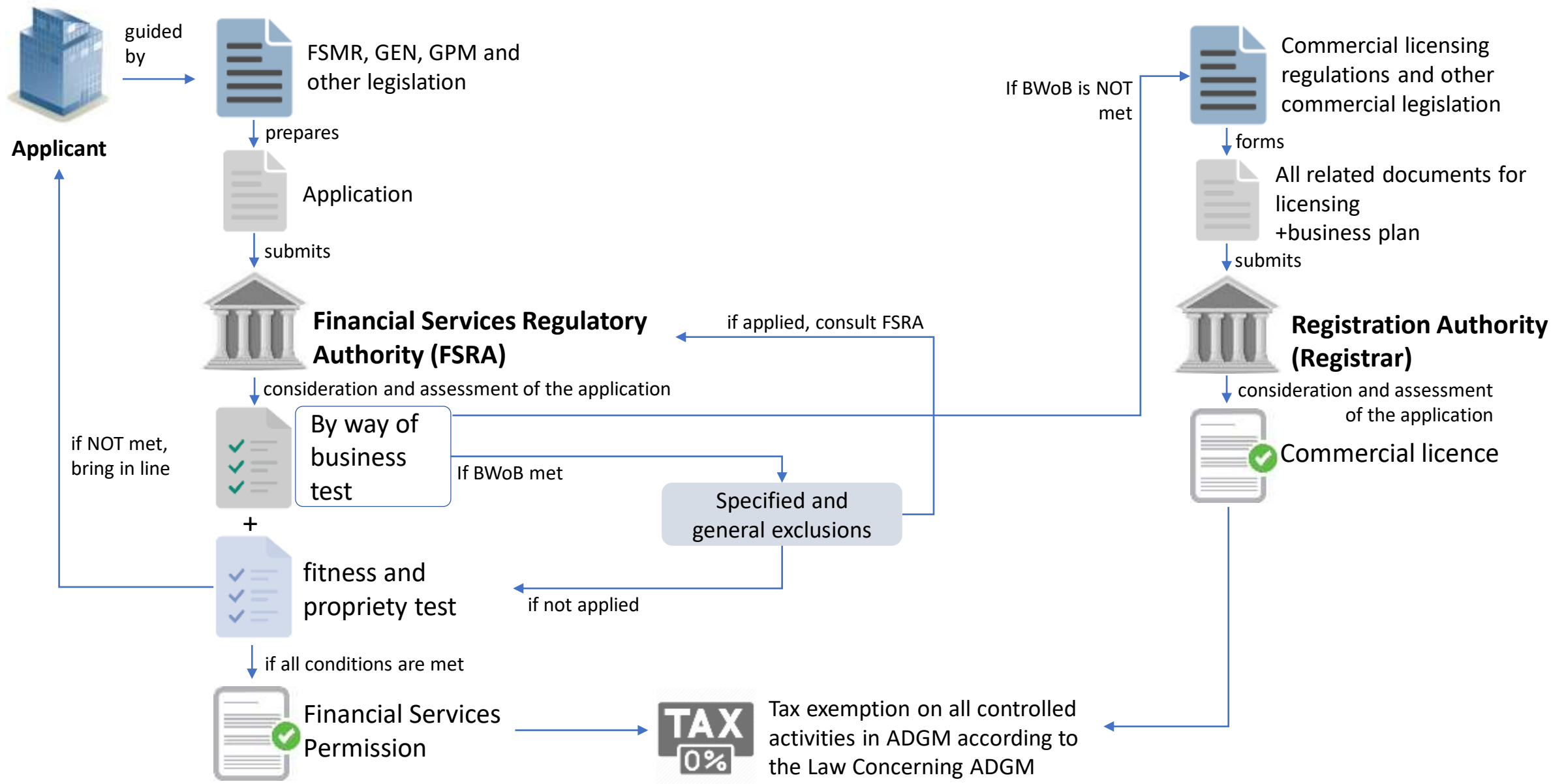
# ADGM FSRA's "By way of business" test

## From FSRA's Guidance & Policies Manual (GPM):

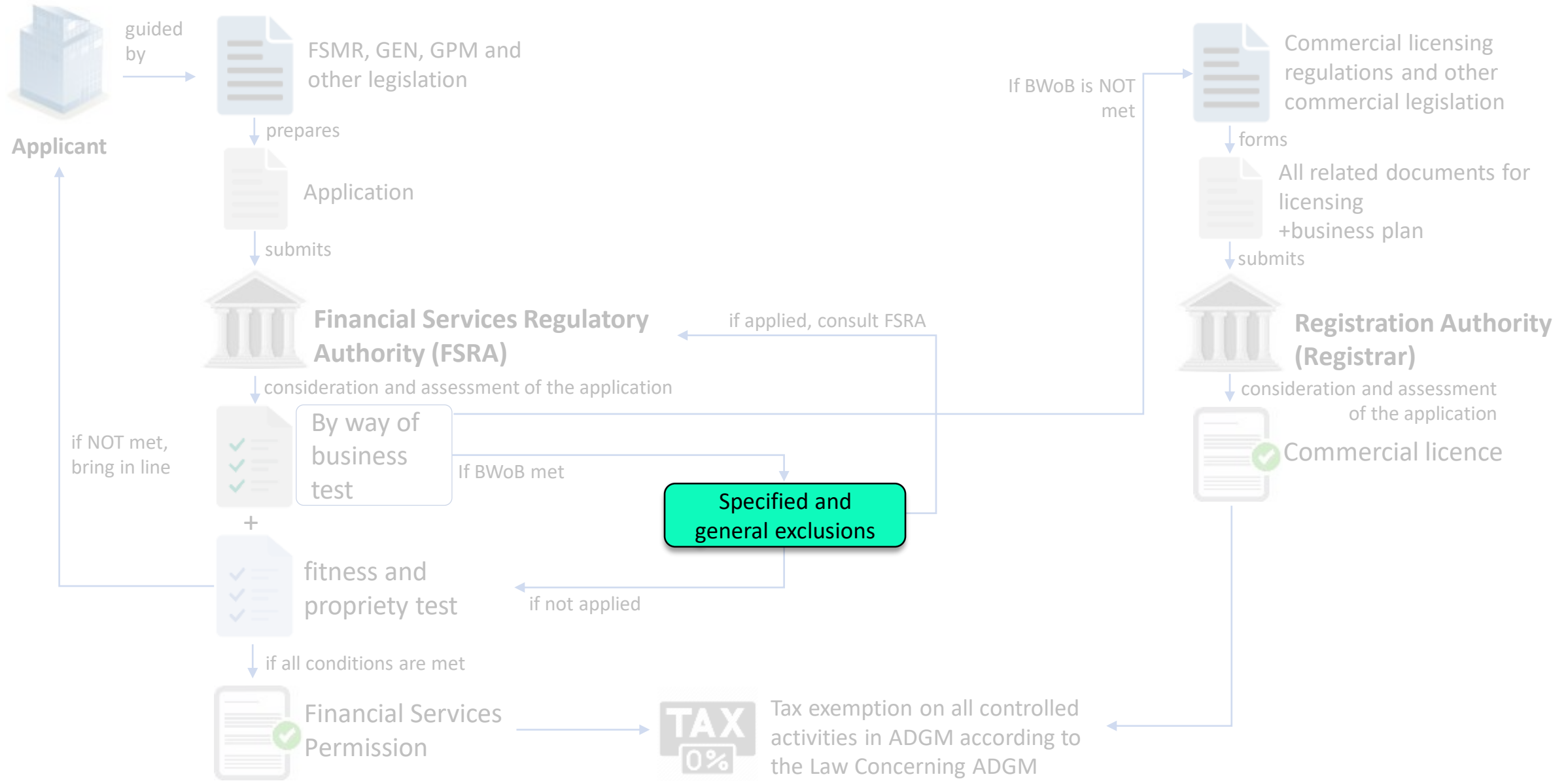
Considering application of the incorporated firm for an authorisation the Financial Services Regulatory Authority (FSRA) concludes whether or not an activity will be carried on **by way of business** where it takes into account **several factors**:

- the degree to which the activity is conducted with continuity, regularity and systemically;
- the existence of a commercial element;
- the scale proportion and impact which the activity bears to other activities carried on by the same Person but which are not regulated; and
- the nature, context and circumstances of the particular activity that is carried on.

# Specified and general exclusions for Regulated activities in ADGM



# Specified and general exclusions for Regulated activities in ADGM



# FSMR. Specified exclusions applying to several Regulated activities

## 4. Dealing in Investments as Principal

- 12. Dealing in Investments as Agent
- 16. Arranging Deals in Investments
- 28. Advising on Investments or Credit
- 31. Effecting Contracts of Insurance
- 32. Carrying Out Contracts of Insurance as Principal
- 33. Insurance Intermediation
- 36. Insurance Management
- 38. Accepting Deposits
- 43. Providing Custody
- 46. Arranging Custody
- 48. Providing Credit
- 50. Arranging Credit
- 52. Providing Money Services
- 54. Operating a Multilateral Trading Facility or Organised Trading Facility

## 56. Managing Assets

- 59. Managing a Collective Investment Fund
- 60. Acting as the Administrator of a Collective Investment Fund
- 61. Acting as the Trustee of an Investment Trust
- 64. Managing a Profit Sharing Investment Account
- 65. Operating a Credit Rating Agency
- 67. Operating a Representative Office
- 68. Specified Benchmarks
- 70. Agreeing to Carry On Specified Kinds of Activity
- 72. Providing Trust Services

## Dealing in Investments as Principal

**A Person does not carry on an activity of the kind specified by paragraph 4 if he:**

1. Do not hold himself out as willing and able to engage in that activity and do not regularly solicit other persons to engage with him in transactions constituting that activity.
2. Deals with or through Authorised Persons or Exempt Persons or through foreign licensed persons.
3. Accepts the instruments creating or acknowledging indebtedness
4. Issues or buys his own shares etc.
5. Deals with options, futures and CFDs in purposes of risk management

**A person does not carry on an activity of the kind specified by paragraph 56 if:**

- a) he is a person appointed to manage the assets in question under a power of attorney; and
- b) all routine or day-to-day decisions, so far as relating to investments of a kind mentioned in paragraph 56, are taken on behalf of that person by:
  - i. an Authorised Person with permission to carry on activities of the kind specified by paragraph 56;
  - ii. a person who is an Exempt Person in relation to activities of that kind; or
  - iii. a Non-Abu Dhabi Global Market Person.

# FSMR. General exclusions applying to several Regulated activities

## 4. Dealing in Investments as Principal

- 12. Dealing in Investments as Agent
- 16. Arranging Deals in Investments
- 28. Advising on Investments or Credit
- 31. Effecting Contracts of Insurance
- 32. Carrying Out Contracts of Insurance as Principal
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## Groups and Joint Enterprises

**There is excluded from paragraph 4 any transaction into which a person enters as principal with another person if that other person is also acting as principal and—**

- a) they are members of the same Group; or
- b) they are, or propose to become, participators in a Joint Enterprise and the transaction is entered into for the purposes of or in connection with that enterprise.

**There is excluded from paragraph 56 any activity carried on by a person if—**

- a) he is a member of a Group and the assets in question belong to another member of the same Group; or
- b) he is or proposes to become a participator in a Joint Enterprise with the person to whom the assets belong, and the assets are managed for the purposes of or in connection with that enterprise.

# ADGM Tax regime

## From the Law No. 4 of 2013 Concerning Abu Dhabi Global Market:

### Tax Exemptions

The Global Market and the **Global Market Establishments** and Authorities and their workers shall be subject to zero taxation, including income tax relating to their operation within the Global Market.

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Global Market: The Financial Free Zone pursuant to the aforesaid Federal Decree No. (15) of 2013.

Global Market's Authorities: The "Global Market's Registration Bureau", the "Financial Services Regulation Bureau" and the "Global Market's Courts".

**Global Market Establishments**: Company, Any branch, representative office, institution entity, or project registered or licensed to operate or conduct any activity within the Global market by any of the Global market Authorities according to the provisions of this law or the Global market regulations or the executive resolutions including the licensed financial Global market Establishments.

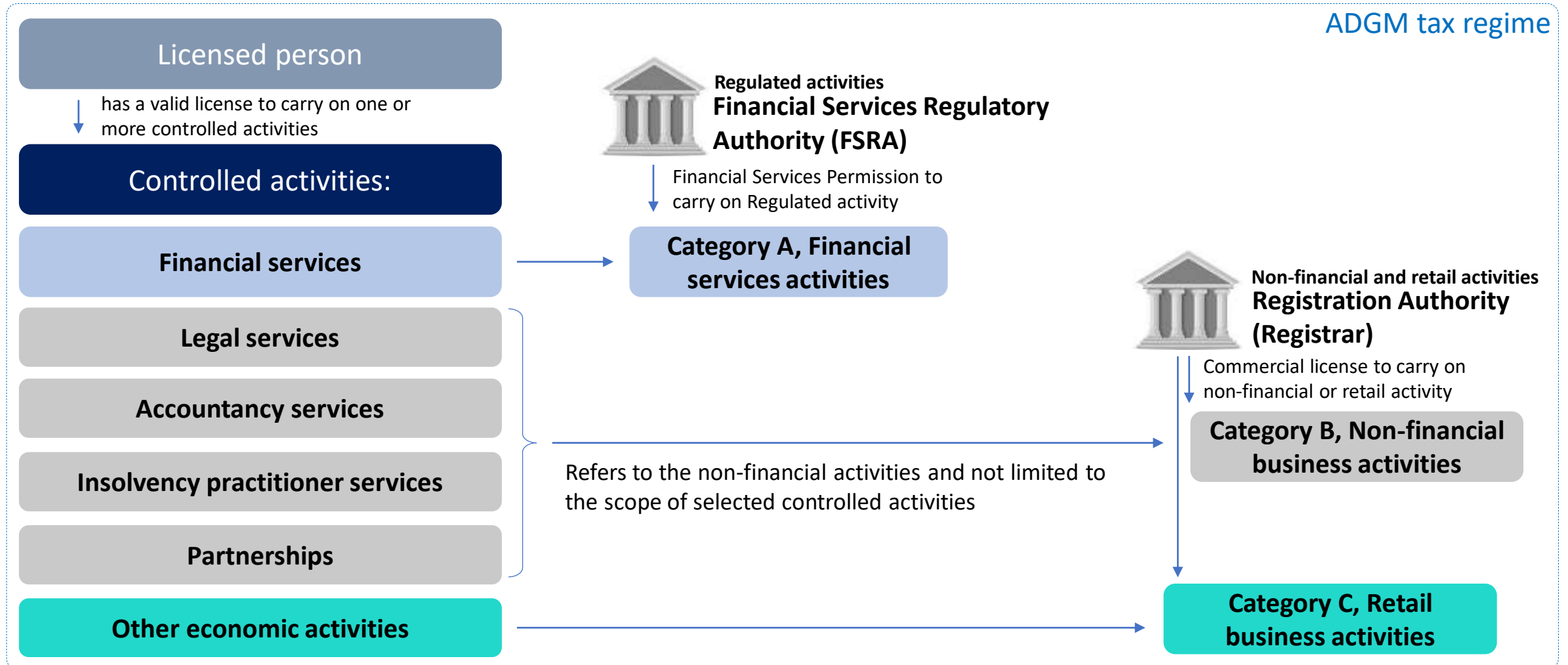
## From ADGM Commercial Licensing Regulations 2015:

A "Licensed Person" is a person who has a valid license (Licensed Service Providers) to carry on one or more **controlled activities**.



# ADGM. All licensed activities are tax-exempt.

According to the **Law No. 4 of 2013 Concerning ADGM** the Global Market and the Global Market Establishments and Authorities and their workers shall be subject to zero taxation, including income tax relating to their operation within the Global Market.



# Single family offices, proprietary investment entities, management offices and SPVs fall under licensed activity in ADGM and have zero taxation

When an applicant applies for a license to carry on a controlled activity, the application shall be regarded as including all business activities falling within the scope of the controlled activity carried on by way of business.

Controlled activity of financial services

## Category A, Financial services activities

Regulated activities:

- Arranging deals or dealing in investment as principal
- Advising on investments or credit
- Dealing in investments as agent
- Accepting deposits
- Providing custody
- Providing or arranging credit
- Money services, managing assets or collective investment funds
- Operating a Multi-lateral Trading Facility, Organised Trading Facility, Credit Rating Agency or Representative office
- Administering or providing information re. a specified benchmark
- Shari-a compliant regulated activities
- Effecting contracts of insurance
- Insurance management
- Agreeing to carrying on regulated activities

Controlled activity of other than financial services

## Category B, Non-financial business activities

- Professional service providers, such as legal and tax consultancy, audit, accounting and bookkeeping services firms, insolvency practitioner, liquidator firms, business training providers, IT and HR/search firms
- Corporate headquarters, management offices and treasury functions
- Single family offices and proprietary investment entities
- Holding companies and **special purpose vehicles**
- Industry and professional associations
- Real estate activities
- Open Ended/ Close Ended investment activities
- Accommodation and food service activities
- Administrative and support service activities
- Other non-financial service activities

Controlled activity of other economic activities

## Category C, Retail business activities

- Manufacture of food products, textiles, apparels, chemical products, furniture, jewellery
- Wholesale and retail trade
- Postal and courier activities
- Food and Beverage service activities
- Motion picture, video and television program activity
- Photographic activities
- Rental and leasing of motor vehicles, personal and household goods, machinery, equipment
- Travel agency, tour operator, reservation service and related activities
- Arts, entertainment and recreation
- Other retail service activities

# Example: ADGM FSRA's "By way of business" test (cont.)

1

## Application

**Applicant** wants to deal with the following **operations** in ADGM:

- Investments of individual professionals and professional investment institutions
- Securitising assets and project financing
- Managing, holding and investing of own assets
- Private wealth management
- Company portfolio management and treasury operations

These activities can be treated as as dealing on clients' accounts or as dealing in own account.

2

## By way of business test

**FSRA** considers the applicant's business plan and concludes whether or not a financial activity will be carried on **by way of business**.

3

## Authorisation

If activity is considered to be carried on **by way of business** the applicant may apply for an **Authorisation** from FSRA to carry on **Regulated activities**:

- Dealing in Investments as Principal
- Managing Assets

## Commercial license

If activity is considered to be carried on **not by way of business** the applicant may apply for a **commercial license** from the Registration Authority to carry on **non-financial business activities**:

- Activities of Single Family Offices
- Special purpose company for professional investors
- Special purpose company for professional investment institutions
- Special purpose company/vehicle
- Proprietary investment company
- Proprietary asset management company
- Activities of Foundations
- Activities of Holding Companies and Partnerships
- Treasury management



**The “by way of business” test applied by ADGM’s FSRA gives tax-exemption for activities carried not by way of business on already tax free regime on regulated and non-regulated activities. What other advantages the “by way of business” test gives to the applicants?**

Besides tax exemption, carrying on activities not by way of business will face obvious less stringent:

1. Reporting requirements
2. Capital requirements

# Reporting requirements for authorisation vs. commercial license in ADGM

Companies that carry on financial activities not by way of business and have commercial license in non-financial Category B in ADGM face less stringent reporting requirements and have to fulfill requirements of the Registrar only (not of FSRA) :

## **Reporting requirements from FSRA:**

to all authorised persons:

- Annual returns
- Client Money Auditor's Report
- Safe Custody Auditor's Report
- Remuneration Structure and Strategies
- Annual report on Controllers
- Financial Statement Auditor's Report
- Regulatory Returns Auditor's Report

to authorised persons related to specific prudential categories:

- Public Listed Company Auditor's Report
- Professional Indemnity Insurance cover
- IRAP assessment
- ICAAP assessment
- Capital adequacy summary report
- Leverage ratio report
- Details of PII arrangements and evidence of cover
- Fund Auditor's Report

## **Reporting requirements from the Registrar:**

to all registered companies:

- a copy of the company's annual balance sheet
- a copy of the company's annual profit and loss account
- copy of the auditor's report on those accounts
- a copy of the directors' report

# Capital requirements for Regulated activities in ADGM

Base capital requirements that would otherwise be applicable are waived for activities carried out by **NOT** by way of business:

Prudential Category	Regulated Activities	Capital Requirements	Base Capital Requirement	Risk Capital Requirement	Expenditure Based Capital Minimum	Capital Conservation Buffer*
Category 2	Dealing in investments as principal (not as a matched principal)	Higher of applicable Base Capital Requirement (PRU 3.6), Risk Capital Requirement (PRU 3.8) or Expenditure Based Capital Minimum (PRU 3.7)	US \$2 million	√	√	√
Category 3C	Managing assets	Higher of applicable Base Capital Requirement (PRU 3.6) or Expenditure Based Capital Minimum (PRU 3.7). Must also maintain liquid assets which exceed its Expenditure Based Capital Minimum.	US \$250,000	-	√	-

## **Proposal #1: Provide “by way of business” provisions in AIFC FSFR**

✓ **The AIFC FSFR must contain the AFSA specific rule making power regarding:**

### **Chapter 1. Licensing of Authorised Firms**

#### **By way of business test:**

Whether or not an activity is carried on by way of business is a question of fact that takes account of several factors. These include:

- (a) the degree to which the activity is conducted with continuity, regularity and systemically;
- (b) the existence of a commercial element;
- (c) the scale proportion and impact which the activity bears to other activities carried on by the same Person but which are not regulated; and
- (d) the nature, context and circumstances of the particular activity that is carried on.

## **Proposal #1: Provide “by way of business” provisions in AIFC FSFR (cont.)**

- ✓ **The AIFC FSFR must contain the AFSA specific rule making power regarding:**

### **8. AFSA power to make Rules**

#### **Carrying on Regulated Activity by way of business**

The Regulator may make Rules which make provision—

- as to the circumstances in which a person who would otherwise not be regarded as carrying on a Regulated Activity by way of business is to be regarded as doing so;
- as to the circumstances in which a person who would otherwise be regarded as carrying on a Regulated Activity by way of business is to be regarded as not doing so.

- ✓ **In AIFC FSFR, the General Prohibition must include the “by way of business” provision:**

### **24. The General Prohibition**

A Centre Participant must not carry on a Regulated Activity by way of business unless it is licensed to do so by the AFSA.



## **Proposal #1: Provide “by way of business” provisions in AIFC FSFR (cont.)**

- ✓ **In AIFC GEN, the Definition of Regulated Activities must include the “by way of business” provision:**

### **1.1.1. Definition of Regulated Activities**

The Regulated Activities that may be carried on **by way of business** by an Authorised Firm, subject to the terms of its Licence, are specified in Schedule 1.

- ✓ **In AIFC FSFR, the Authorised Firms must include the “by way of business” criteria:**

### **34. Criteria for the grant of a Licence to carry on Regulated Activities**

#### **By way of business:**

A person carries on an activity by way of business if the person:

- a) engages in the activity in a manner which in itself constitutes the carrying on of a business
- b) holds himself out as willing and able to engage in that activity or
- c) regularly solicits other persons to engage with him in transactions constituting that activity.



## **Problem #2**

# **Not flexible SPV regime in AIFC**

### **Current SPV regulatory regime in ADGM and DIFC, compared to AIFC**

1. Current AIFC SPC Rules are very similar to old DIFC SPC Regulations (restrictions on the number of shareholders, mandatory CSP services), whereas DIFC implemented a new Intermediate SPV regime in 2016.
2. SPV framework in ADGM looks more flexible, compared to DIFC and AIFC. The amount of registered SPVs in ADGM has reached from 0 in June 2016 to 560 today.  
  
ADGM implemented a Restricted Scope Company (type of a Private Company Limited by shares that can be structured as SPV), which gives limited public disclosure option for private companies and family offices.



# Proposal #2

**In order to develop AIFC SPV regime we need:**

1. Bring the AIFC SPC regime close to or in line with ADGM SPV regime
2. Adapt RSC in AIFC Companies Regulations

# Uses of SPVs (for reference)

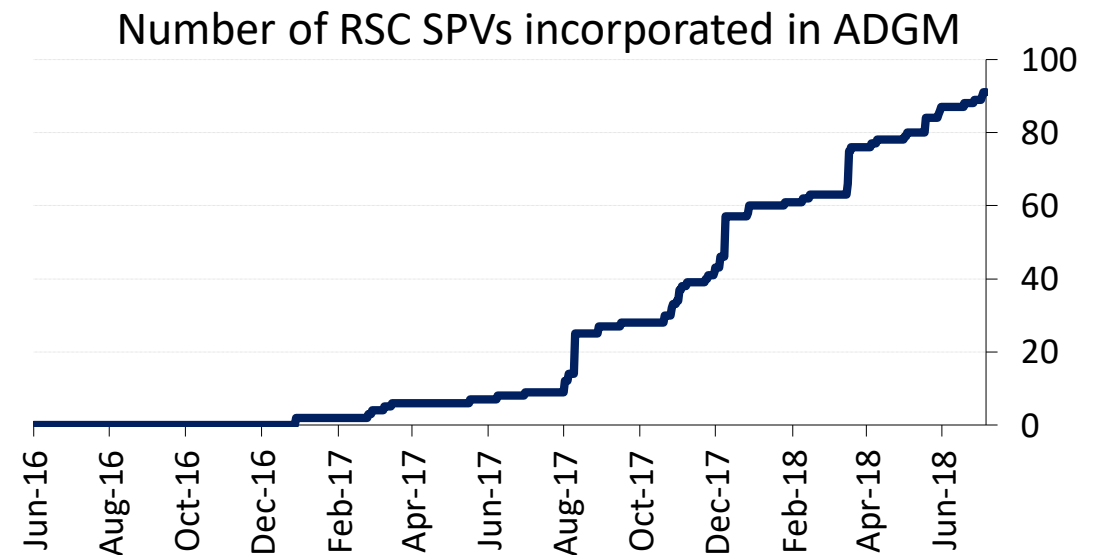
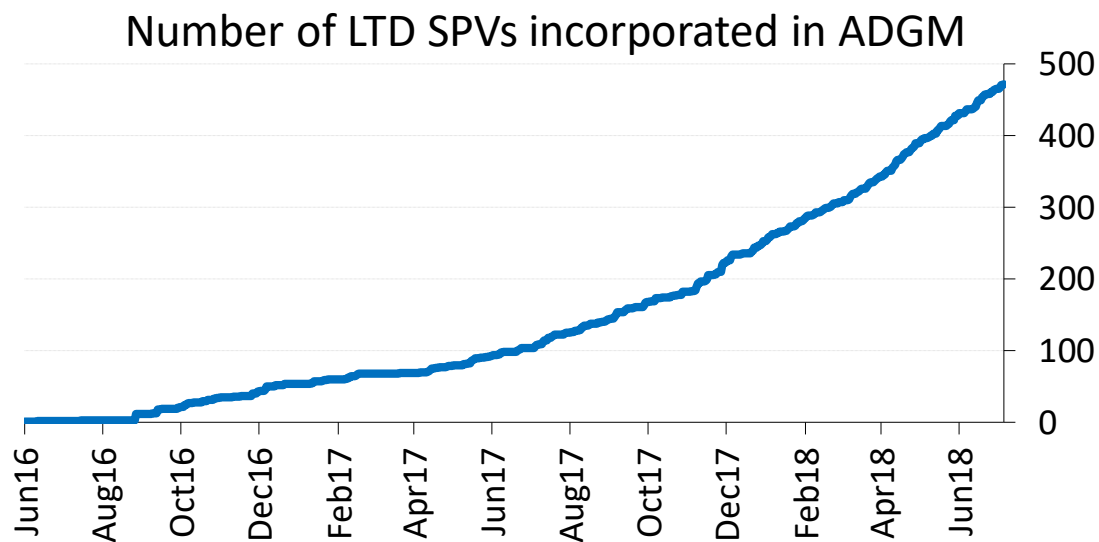
Intellectual property	To help ring-fence intellectual property (IP), for example, when IP is used as security to raise finance and to isolate it from other business risks such as insolvency.
Ring-fence assets	An SPV can own assets to reduce the complexity of asset ownership in large companies. By holding assets in an SPV, any asset can be sold in an isolated vehicle instead of lengthy contract, license and permit processes.
Securitisation	An SPV can be used to finance the purchase of assets by raising capital bonds, asset securitisation utilising an SPV structure could be a desirable way for a company to raise cash.
Risk sharing	An SPV can be used to mitigate risk through the setup of an SPV to hold assets or liabilities, particularly where the parent company/sponsor may be subject to other volatile markets.
Succession planning	For single family offices the set-up of an SPV can help in succession planning, through developing a new governance structure, managing a specific business continuity plan and ring-fencing assets

# SPV activities definitions compared (for reference)

DIFC, AIFC SPC exempt activities, described in SPC Rules	ADGM SPV activities described in Category B, Non-Financial Permitted Business Activities specified by the Registrar
<p>Exempt Activity, in relation to a Special Purpose Company, means any of the following activities, whether undertaken in an Islamic or conventional way:</p> <ul style="list-style-type: none"><li>• Acquisition (by way of leasing, title transfer, risk transfer or otherwise)</li><li>• Holding and the disposal of any asset (tangible or intangible, including but not limited to receivables and shares)</li><li>• Obtaining of any type of financing (banking or capital markets)</li><li>• Granting of any type of security interest over its assets</li><li>• Providing of any indemnity or similar support for the benefit of its Shareholder(s) or any of its subsidiaries</li><li>• Entering into any type of hedging arrangements</li><li>• Financing of the Initiator or another Special Purpose Company</li><li>• Acting as trustee or agent for any participant in the Transaction</li><li>• Any other activity approved in writing by the Registrar</li><li>• Any activity ancillary to an activity mentioned above.</li></ul>	<p>A Body Corporate whose sole purpose, either generally or when acting in a:</p> <ul style="list-style-type: none"><li>• particular capacity, is to carry out one or more of the following functions:</li><li>• Issuing Investments</li><li>• Redeeming or terminating or repurchasing, whether with a view to re issue or to cancellation, an issue, in whole or part, of Investments or</li><li>• Entering into transactions or terminating transactions involving Investments in connection with the issue, redemption, termination or re purchase of Investments</li></ul> <p>And has been explicitly established for the purpose of:</p> <ul style="list-style-type: none"><li>• Securitising assets</li><li>• Investing in Real Property.</li></ul>

# Strong interests in ADGM's SPVs

- High demand for ADGM SPVs from asset management, family wealth, aviation, shipping, and technology/intellectual property development.
- Over 200 SPVs were incorporated in the first 12 months of SPV regime operations (Dec 2017)
- \$302m Natixis-Etihad aircraft lease finance structured through SPVs in ADGM
- 560 registered SPVs (471 private companies and 89 restricted private companies, Jul 2018)



# ADGM SPV regime: key features

- Fully digital registration process
- Flexible ownership structure
- Shelf SPVs permitted
- Operate under Companies Regulations rather than separate SPV regulations
- Limited public disclosure option
- Perpetual existence
- “By way of business” test
- No restrictions on nationality of ownership
- No restrictions on the number of shareholders

# Requirements for SPV incorporation

Requirements	ADGM SPVs	DIFC, AIFC SPCs
No requirement to take physical office space (but must maintain a registered office address in Centre's territory)	Yes	Yes
Limited liability status equal to the share capital	Yes	Yes
Corporate body directors are permitted	Yes	No
Restrictions on the number of Directors	$\geq 1$	$\geq 2$
Restrictions on the number of Shareholders	$\geq 1$	$\leq 3$
Regulated Commercial license holding requirement	Yes	No
Majority of the Directors of SPC must be employees of its Corporate Service Provider (CSP)	N/A	Yes
Secretary must be a CSP or a subsidiary of CSP	N/A	Yes
No requirement to maintain, file or audit accounts	Yes	Yes
No requirement to hold an annual general meeting	N/A	Yes
Minimum share capital	No min	\$100
No requirement for shareholders to be based in the Centre	N/A	Yes

**ADGM requirements for SPV incorporation are more flexible and less burdensome.**



# ADGM SPV incorporation forms

The following types of private companies can be registered as SPVs in ADGM:

Type	Uses
<b>Private Company Limited by shares, LTD</b>	<ol style="list-style-type: none"><li>1. Standard private limited company</li><li>2. Passive holding company</li></ol>
<b>Restricted Scope Company (RSC), restricted LTD</b>	<ol style="list-style-type: none"><li>1. A subsidiary of a group which publicly files consolidated accounts</li><li>2. A subsidiary of a company formed by Emiri decree</li><li>3. A Single Family Office</li></ol>

# ADGM. Public disclosure.

## The ADGM offers limited public disclosure for Private Companies

- Restricted Scope Companies (RSC) can avail of this advantage. It is desirable for family offices that want to manage their assets discreetly, as well as for multinational corporate groups that require passive entities.
- This is very similar to Private Company Limited by Shares except to the fact that it has less disclosure on public register and lighter compliance requirements.
- The limited public disclosure applies to an RSC's records of Directors, Shareholders, financial statements, beneficial ownerships, and filing of accounts.

Requirements	Private Company Limited by Shares, LTD	Private Company Limited by Shares (RSC), restricted LTD
Full disclosure to Registrar	Yes	Yes
Publicly accessible records of Directors	Yes	No
Publicly accessible records of Shareholders	Yes	No
Publicly accessible financial statements	Yes	No
Filing of accounts	Yes	No
Audit requirement	No	No
Annual return requirement	Yes	Yes
Minimum natural person director requirement	1	1
Beneficial ownership publicly disclosed	No	No

# Requirements for public disclosure

Requirements	ADGM SPV		DIFC old SPC	AIFC SPC
Legal forms	Private Company Limited by Shares, LTD	Private Company Limited by Shares (RSC), restricted LTD	LTD, LLC	Private Company Limited by Shares, LTD
Full disclosure to Registrar	Yes	Yes	Yes	Yes
Publicly accessible records of Directors	Yes	No	N/A	N/A
Publicly accessible records of Shareholders	Yes	No	N/A	N/A
Publicly accessible financial statements	Yes	No	N/A	N/A
Beneficial ownership publicly disclosed	No	No	N/A	N/A
Annual return requirement	Yes	Yes	No	No
Minimum natural person director requirement	1	1	2	2
Filing of accounts	Yes	No	No	No
Audit requirement	No	No	No	No

**ADGM RSC public disclosure requirements are much lower than at AIFC or DIFC.**

## **Proposal #2.1: Bring the AIFC SPC regime in line with ADGM regime**

- ✓ Corporate body directors must be permitted
- ✓ Min number of Directors must be 1
- ✓ Min number of Shareholders must be 1 with no upper limit
- ✓ Regulated Commercial license holding requirement must be met
- ✓ Requirement for the majority of the Directors of SPC to be employees of its Corporate Service Provider must be removed
- ✓ Requirement of the Secretary to be a CSP or a subsidiary of CSP must be removed
- ✓ Shelf SPVs must be permitted
- ✓ Provide limited public disclosure regime by RSC

## **Proposal #2.2: Adapt RSC in AIFC Companies Regulations**

- ✓ Application of incorporation and Certificate of incorporation for private companies must include RSC type option.
- ✓ Restricted Scope Company (RSC) as a type of private company and its formation criteria must be added to the Types of companies.
- ✓ Provision of no public disclosure requirement for annual returns of RSC must be added.
- ✓ Name of the RCS must be followed by the word “restricted”, e.g. “restricted Ltd.”.
- ✓ Function of re-registration of RSC as non-RSC with certain criteria must be added.
- ✓ Exception of any inspections to Register of Shareholders, Register of Debt security holders of RSC and ability of RSC to decline such inspection requests must be added.