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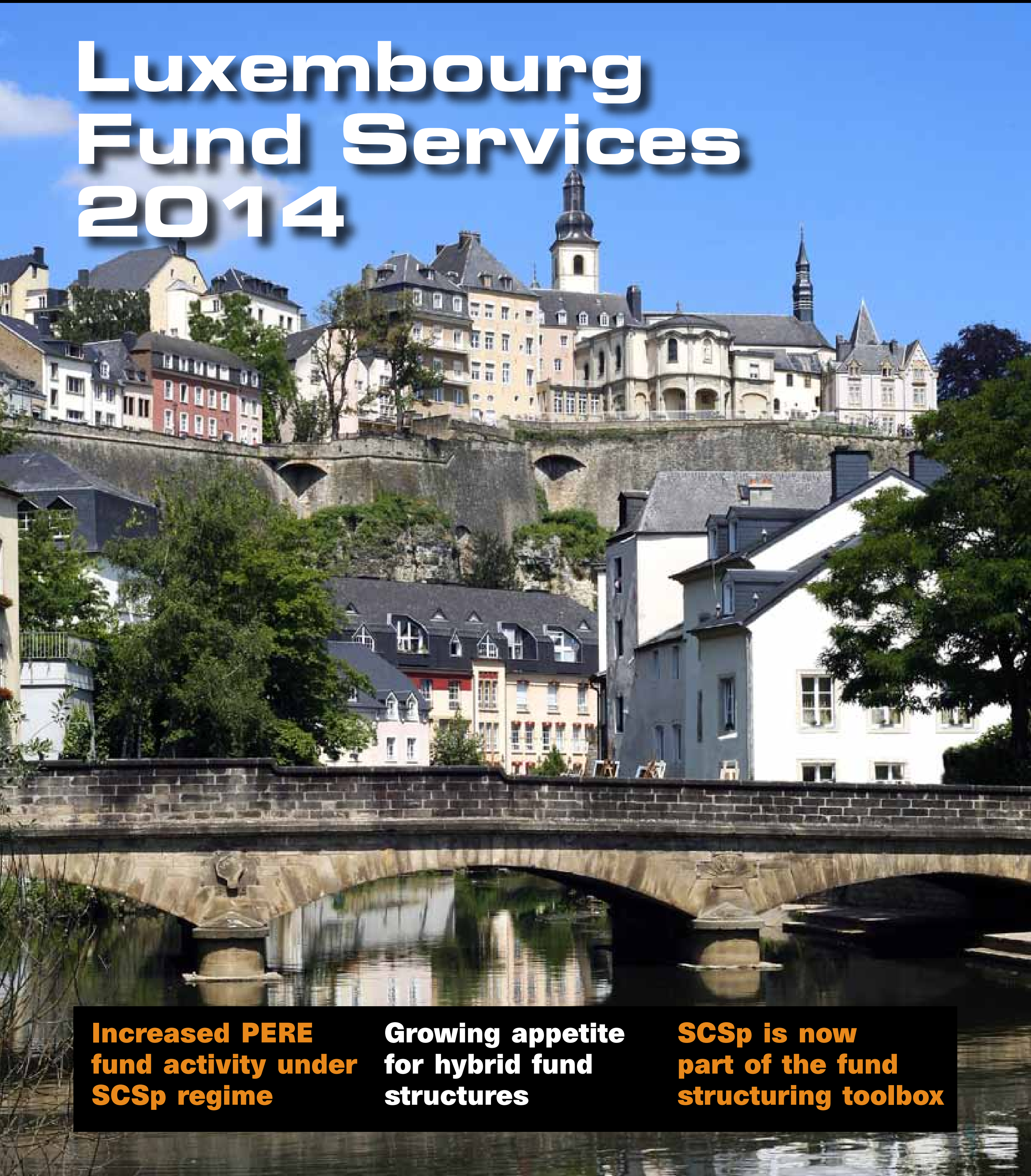

Increased PERE fund activity under SCSp regime

Growing appetite for hybrid fund structures

SCSp is now part of the fund structuring toolbox

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Luxembourg braces itself for increased PERE fund activity

By James Williams

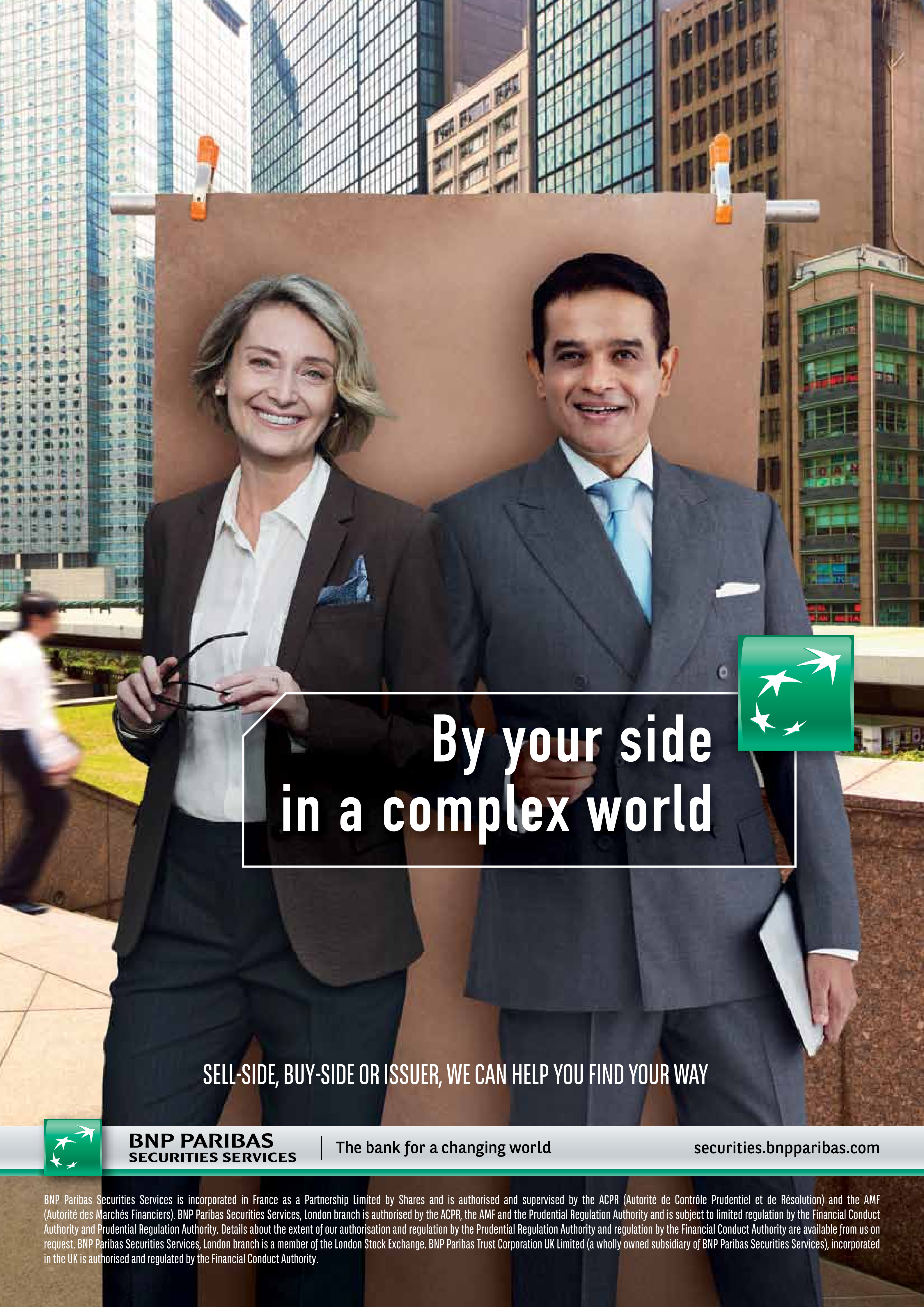
According to figures released by ALFI at the end of July 2014, there were 3,891 funds with total assets of EUR2.90trn. By comparison, at the end of 2013 the size of Luxembourg's fund industry was EUR2.61trn with 3,902 funds. During 2013 the number of sub-funds increased by 265 and there were 279 SICARs established. Between end-2012 and end-2013, the number of Specialised Investment Funds (SIFs) – Luxembourg's most popular regulated fund vehicle – increased from 1,485 to 1,562.

Much emphasis has been placed by the Luxembourg authorities on ensuring that financial market regulation is closely monitored. As the fund numbers listed above show, the Grand Duchy remains Europe's leading onshore fund domicile. Far from being hesitant over the potential impact of the AIFMD, Luxembourg used its experience of building out a successful UCITS fund market to embrace the Directive to likewise grow its alternative funds market.

"Very early on the Luxembourg authorities were involved in discussions to lobby and influence regulation coming out, and was one of the first EU countries to transpose the AIFMD. Like UCITS, it wanted to have a first mover advantage," says Jean-Daniel Zandona, Director, Financial Institutions/Asset Managers at Credit Suisse (Luxembourg).

"In addition to the AIFMD, the authorities revamped and strengthened the country's legal arsenal. The SCSp, Luxembourg's new LP regime, is a clear move by Luxembourg to introduce more flexibility. Accommodating the new AIFMD regulations is important; bringing a flexible investment manager structure under the SCSp is also important. This was a good move by the authorities and it has translated into inflows into new funds, into new managers coming into Luxembourg and leveraging the cross-border expertise of the domicile as a hub for fund distribution under AIFMD," he adds.

To be sure, the new SCSp (Special Limited Partnership) introduced last year has the potential to take Luxembourg onto a new level altogether as global private equity and real estate managers begin to sit up and take notice. Even though Luxembourg has close to ▶ 7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Coping with the demands of risk transparency

Interview with Hugh Stevens

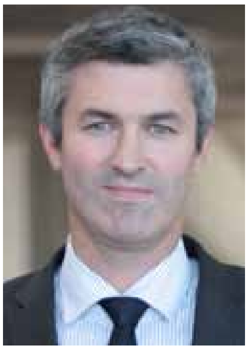
Today's prevailing narrative is quite simple: heightened demands for a transparent view of investment risks are putting considerable pressure on private equity and real estate fund managers, and their service providers.

In short, risk transparency is becoming a key requirement which managers need to address. This is not that easy when one considers the complex structure of private equity and real estate funds and the illiquid non-tradeable nature of the underlying assets. The complexity of data needed to meet various global reporting regimes is a challenge. Indeed, the much talked about Solvency II regime in Europe is merely one cog of the risk transparency wheel now turning.

"One must also consider Annex IV reporting under the AIFMD in Europe. Another market we know well is Australia," comments Hugh Stevens, head of Private Equity and Real Estate Services at BNP Paribas Securities Services. "There, the 'Stronger Super' regime aims for systemic transparency by making full disclosure of the underlying assets. Australian superannuation funds are big investors in private market assets – real estate, private equity and infrastructure – throughout the world, so this will directly impact the Luxembourg fund market."

The reason for the Australian government's plans to roll out the Stronger Super reforms is to make its superannuation system more robust and efficient and to help superannuants maximise their retirement income. The plan includes paying particular focus to self-managed superannuation funds and to beef up the disclosure and reporting requirements.

"An Australian superannuation fund might invest in international infrastructure through a Luxembourg vehicle and what the Australian regulators are saying is that superannuation funds have to satisfy themselves that they've got to the bottom of the economic targets in the funds. Regardless of the domicile of the fund, APRA (Australian Prudential Regulation Authority) just wants to know what's in the fund. ASIC (Australian Securities and Investments Commission), the other regulator of these funds, has announced even deeper look-through reporting requirements for these investors and, in addition, the data would be made available to the public," explains Stevens.



Hugh Stevens, head of Private Equity and Real Estate Services at BNP Paribas Securities Services

If ASIC's proposals go through, the Stronger Super regime will therefore have an extra-territorial impact on private equity and real estate fund managers.

Greg Tanzer, Commissioner of ASIC, gave a speech on 3rd September 2014 where he talked about portfolio disclosure, governance and risk management expectations. Tanzer referred to the Superannuation System Review – which is driving the Stronger Super reforms – by noting that "systemic transparency is currently lacking in the Australian superannuation system".

Tanzer went on to say that the obligation to publish portfolio holdings disclosure information would help create an information platform that would promote better analysis of superannuation funds. The level of illiquid assets in portfolios would be more observable and this would bring Australia into line with global practice.

"There is a crossover between regimes. In Australia, a market utility is emerging which is becoming the primary data collector. This would be responsible for collecting and then collating information from all private equity and real estate funds, alongside all other asset classes.

"This is an interesting development and our view is that a similar model will be needed in Europe for Luxembourg funds," comments Stevens.

In the UK, the Walker report laid

out guidelines on how to bring better transparency to the private equity market back in 2007. The guidelines, prepared by Sir David Walker, were formulated at the request of the British Private Equity and Venture Capital Association ('BVCA'). In their view, concerns about a lack of transparency in the industry were deflecting attention from the positive role of private equity in generating growth and contributing to the real economy.

"We have therefore seen a voluntary transparency push with the formulation of guidelines in the UK and a regulatory initiative in Australia.

"Meanwhile, in Europe, under Solvency II, there are added commercial and economic reasons for transparency and look-through. If managers can prove what's in their funds' portfolios by providing look-through reporting, then investors – in particular insurance companies – can optimise their use of capital.

"So we see voluntary regimes, regulatory-driven regimes and commercial-driven imperatives, all of which are driving this need for risk transparency and reporting," comments Stevens.

Stevens confirms that BNP Paribas Securities Services is already working with clients on numerous transparency reports and notes that insurers are getting ready ahead of Solvency II in a bid to "align to the new regulatory environment".

Referring back to Australia for comparison, pension funds and their trustees now have both civil and criminal liability hanging over their heads if they get things wrong.

"If they are negligent in their look-through reporting they could actually face criminal charges. If trustees are awarding a mandate to invest in a target fund, transparency and risk considerations are now top of mind. We see investment committees refusing to make investments not on the basis of economics but purely on the basis that the fund is not able to produce the data required for APRA reporting.

"I would estimate that it will be the same under Solvency II. Underlying GPs who are not able to produce the required depth and complexity of reporting will find themselves at risk with large institutional investors," opines Stevens.

Connor Sloman, Head of Asset Management Solutions, EMEA for Morningstar was quoted in April 2014 as saying that Morningstar was seeing "first-hand how asset managers are taking an active interest in providing additional insight into how their funds' asset allocations may drive Solvency II capital charges."

As Stevens points out, whilst there are different regimes for managers to deal with, once you scratch below the surface they share a lot of similarities.

In Australia currently APRA is requiring superannuation funds to look through to the first non-controlled entity. As a next step, ASIC is proposing that from next year superannuation funds will be required to report on a look-through basis right down to the underlying investments.

This move to deepen look-through reporting is encouraged under Solvency II and has also been reflected by the obligations on depositaries under AIFMD. "So there is a degree of consistency between different regimes but some important differences as well."

Not all service providers are going to be well equipped to provide an industrial-strength risk transparency reporting solution. Given that under AIFMD managers will also be required to appoint an independent depositary, many will look to leverage off a single counterparty to reduce costs.

BNP Paribas Securities Services is all too aware of this. Last July it completed the acquisition of Commerzbank's "Depobank" business. The firm now has USD125bn of PERE assets under custody giving it significant weight in the European market.

"There are now synergies available for managers to engage with the same counterparty to use our data expertise and record keeping to perform the depositary function and some of the regulatory reporting tasks. The benefit to this is that the data is already collected. It becomes a marginal cost to the manager to deal with different risk regimes and reporting obligations like Annex IV. I think there is going to be a degree of consolidation in the industry once Europe decides on the best model. Some of the more bespoke solutions that currently exist may fall by the wayside."

With risk transparency on everyone's agenda, getting the right solution in place is going to be paramount for global PERE managers. ■

3 ▶ EUR3trn in regulated AuM alone, it still felt the need to innovate and offer more potential to US, UK and Asia managers. The SCSp is an important step towards achieving this.

"Typically these managers have chosen UK, Delaware or Cayman partnership structures. That's what Luxembourg wanted to tap into with the introduction of the SCSp.

"I really think that Luxembourg has a complete toolbox for fund structuring. Of course there were already plenty of options in the past – maybe somewhat less familiar to Anglo-Saxon managers – but the SCSp is a very good addition and completes the picture," says Paul Van den Abeele, Partner at Clifford Chance (Luxembourg).

It certainly strengthens Luxembourg's position. PERE managers have a lot more choice, depending on the make-up of their investors, as to whether to structure the partnership without legal personality – as is now the case with the SCSp – or with legal personality under the existing Common Limited Partnership (SCS).

"Both can be set up as regulated entities, in this case SIFs, SICAVs or Part II funds. The promoter can also set up the partnership as an unregulated entity. The partnership set up as an unregulated or a regulated product may be an AIF. In such case it may fall under the AIFMD and have to be managed by an AIFM," explains Christine Casanova, a director in the Alternative Group at PwC (Luxembourg). "If the partnership is unregulated it is only subject to Company Law. It is not subject to the regulations of the CSSF."

For non-EU managers, Van den Abeele believes the SCSp could potentially become an important part of their global distribution strategy, especially given the preference that continental European institutions have for regulated fund structures.

"The SCSp is a good solution that combines the LP structure that managers are used to with the tax efficiency they require. At the same time, they are able to tap into the EU investor market and benefit fully from the passport," says Van den Abeele, who notes that currently more managers are choosing to go down the regulated SCSp route and get licensed as an AIFM.

"Nevertheless, some clients are structuring joint ventures which means they can remain

out of scope. A lot of insurance companies will have their own funds and look to leverage group exemption. There are different cases; it's not a one-size-fits-all approach but a typical PERE manager is now seriously considering the benefits of the passport under the AIFMD."

There is a palpable sense that under the Directive, and with the SCSp now in place, Luxembourg's PERE funds sector could really start to ramp up. Maitland, a leading legal, fiduciary and funds services group with over USD200bn in AuA, has been active in Luxembourg since 1976. In May 2014 it acquired a Management Company license allowing it to act as a third party AIFM. In addition to the ManCo (MS Management Services S.A.) the firm also established the MS SICAV SIF, a platform allowing managers to set up their own sub-funds to market across Europe.

Kavitha Ramachandran, Director of MS Management Services S.A. says that Maitland is expanding into the real estate funds area to provide AIFM services.

"We are looking to extend our AIFM license to these asset categories. We see the demand. We are currently speaking to the CSSF with a view to expanding our services in the PERE space," comments Ramachandran.

Every year, PwC (Luxembourg) runs an emerging trends survey. Current market perception is improving for pan-European real estate funds and in the opinion of Alexandre Jaumotte, partner and Real Estate and Infrastructure Tax Leader at PwC, Luxembourg is in a prime position to benefit. ▶ 11

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SCSp is now part of the fund structuring toolbox

Interview with Paul Van den Abeele

"The Special Limited Partnership (SCSp) has been successfully introduced into Luxembourg law. It is set to benefit from onshore fund activity following the AIFMD and is of particular interest to Anglo-Saxon managers and investors given their familiarity with limited partnership structures," explains Paul Van den Abeele, Partner at Clifford Chance (Luxembourg).

In essence, what Luxembourg's lawmakers have done is modernise what was quite an antiquated limited partnership regime in the SCS (société en commandite simple) based on the 1915 company law.

Alternative fund managers – in particular private equity and real estate managers – can now choose to either avail of the SCS regime, which is invested with legal personality, or use the SCSp, which is invested with no legal personality.

"The existing SCS was not extensively covered in Luxembourg company law; given the legal uncertainty, there was less use of this legal structure. Now, with the AIFMD implementation, Luxembourg has seized the opportunity to introduce an efficiency package. What this involved was revamping the SCS and creating the SCSp, a counterpart that has no legal personality. The driver was essentially to offer a competitive answer to the UK, Delaware and Cayman limited partnership structures," comments Van den Abeele.

Previously, the unregulated market was dominated by so-called SOPARFIs (société de participations financières) – private holding companies that limit themselves to small groups of investors and remained outside the scope of supervision of Luxembourg's regulator, the CSSF. The SCSp now adds to Luxembourg's toolbox and is available to both unregulated structures and regulated funds.

Paul Van den Abeele, Partner at Clifford Chance (Luxembourg)

From a Luxembourg perspective, the SCS and SCSp have a fairly similar tax and corporate treatment. "The SCSp's lack of legal personality is more important for other jurisdictions where it is considered equivalent to domestic partnership structures, such as the UK LP and the German KG. This means that investors can obtain a similar tax treatment as the SCSp is considered by tax authorities to be equivalent to the local structure," adds Van den Abeele.

The Luxembourg SCSp has a number of distinguishing features. Unlike partnership structures in other jurisdictions such as the UK LP, the GP is not required to disclose the identity of every limited partner in the partnership. In addition, there is substantial flexibility within the limited partnership agreement, including with regard to voting rights and distribution of the economic benefits of the partnership. Also, there is now more clarity around LPs engaging in the management activities of the SCSp in terms of the risk of losing their limited liability status.

"We are working more and more with global clients on real estate, debt funds and private equity structures, some of which would, in the past, probably have adopted UK LP structures but are now choosing the Luxembourg SCSp. It's very important that we don't have legal personality from a tax perspective, particularly in markets like the UK. It's a big advantage," explains Van den Abeele.

It is a strong message for managers – especially those outside Europe, particularly in the US and Asia – to be able to say to investors that they now have a fund structure that is more to their liking. For EU managers that tap into the European market to raise capital, the AIFMD has become a given, something that has to be, or has been, dealt with. However, not all institutional investors are looking for additional regulation (e.g. UK pension funds). Therefore, where managers used to choose offshore locations to structure funds, they can now come to potential investors with a similar vehicle that is subject to regulation and onshore, which makes for a more compelling proposition.

Van den Abeele says that there is already clear evidence of managers beginning to use the SCSp structure, in and out of scope of the AIFMD, especially as debt funds and other alternative funds are en vogue right now. UK and US managers are choosing to go with the SCSp "almost without exception" confirms Van den Abeele, whereas German managers, for example, are favouring the updated SCS.

"Germany made changes to its investment and tax laws. The revamped SCS structure has become interesting to German insurance companies and other investors as an alternative to the mutual fund structure (FCP) used in the past. As a result, they have tended to launch Luxembourg funds (debt, infrastructure, real estate) using this structure.

"Post-AIFMD, our fund structuring work for German clients has been heavily weighted towards regulated SCS vehicles, particularly in structuring real estate and private equity funds for German insurance companies, which form an important part of the client base of our Luxembourg and Frankfurt offices," explains Van den Abeele.

Managers now have a full complement of options both for the legal structure of the manager and the fund itself. More specifically, on the funds side, managers have the option to run regulated or unregulated funds and either can adopt the legal form of an SCS or an SCSp. With respect to Luxembourg's regulated fund suite, the two main options are to run a SICAR (société d'investissement en capital à risque) or the more popular specialised investment fund (SIF).

If in scope of the AIFMD, the manager can remain subject to the so-called small manager regime if its assets under management remain below the EUR100m (leveraged) or EUR500m (unleveraged and closed-ended) thresholds, even though the manager will need to be registered as an AIFM. The point here is that they would not need to comply with the full extent of the AIFMD, thus giving managers the opportunity to gradually build interest in the fund, without immediately incurring the full burden of regulation as a fully in-scope AIFM or through a regulated fund product.

"The advantage to having an in-scope AIF is that it makes it easier to market due to the marketing passport available to investors. Some investors on top require the fund to be regulated because of their own regulations. That generally results in a SIF structure, which is exempt from most taxes. There's only one tax that is levelled at the fund and that is an annual subscription tax (taxe d'abonnement), which equates to one basis point applied to the fund's net assets," says Van den Abeele.

Moreover, regulated funds allow the benefit of the VAT exemption on management services.

"The SICAR fund structure really focuses on risk capital: private equity and venture capital investments. The main difference between this and a SIF is that there is no diversification requirement. With a SIF, it is not possible to hold more than 30 per cent of the fund's assets in a single investment, which does not apply to the SICAR. Otherwise there aren't that many differences between the two structures other than the risk capital nature of the SICAR.

"A lot of private equity vehicles have been structured as SIFs but the SICAR is still available and is something that works well for particular markets. For example, in Spain it is used quite often because from a structuring and tax perspective it can be used quite effectively," says Van den Abeele, also confirming that this year, one clear trend that has emerged has been for managers to obtain authorisation as AIFMs and launch unregulated vehicles.

In conclusion, Van den Abeele encourages non-EU managers to consider the SCSp as part of their European fund strategy.

"It is a good solution that combines the LP structure that they are familiar with the tax efficiency they require. At the same time, managers will have the ability to tap into the EU investor market and benefit fully from the AIFMD marketing passport." ■

7 "Since the launch of the SIF, real estate fund numbers have grown steadily. Case in point: there are now around 380 regulated real estate funds in Luxembourg. For unregulated vehicles there are no official statistics. Big institutional investors from Asia, the Middle East and the US who were originally passively investing in commingled pan-European real estate funds are these days more willing to invest into segregated accounts where they can get access to much more information and could take a more active role. They can sit on the investment committee or even the Board of Directors of the fund. This is keeping us busy at the moment," comments Jaumotte.

Investors are becoming much more selective in the underlying assets they invest in. They want to be much more involved in the management of the structure and have the assets available to insist on doing so.

"Instead of allocating to a large commingled European fund they prefer to have a segregated account with one of the big name managers and of course, these segregated account structures are often unregulated. I cannot say we see more segregated account structures than regulated pan-European funds, per se, but we are certainly seeing more of these unregulated structures than we did in the past," observes Jaumotte.

Hugh Stevens is head of Private Equity and Real Estate Services at BNP Paribas Securities Services. He notes that a continuing trend among the top 20 real estate managers is that more and more are global alternative managers and mainstream managers. "These are starting to make it on to the top 20 list. Pure play real estate managers are now facing much more competition."

Zandona says that by adapting Luxembourg's regulations to bring it more in line with the traditional Anglo-Saxon LP model brings greater comfort not just to managers, but investors as well.

"Typically, the largest investors are sovereign wealth funds, UK and Nordic pension plans, US pension plans and endowments. As such, they need to invest into structures that are well known to them and robust. That's why the SCSp has been such a good introduction; managers have to spend less time explaining the legal structure and can focus more time on explaining performance objectives.

"Investors are now more aware of the SCSp and this is helping the PERE fund sector," says Zandona.

One of the biggest adjustments that PERE managers are facing, not just under European but global regulatory regimes, is the need to up the ante when it comes to risk transparency. Typically, people will always refer to Solvency II as if it was the only piece of regulation to impact managers. This is not the case.

Take Australia for example. Under proposed Stronger Super reforms, its much vaunted superannuation system – in particular self-managed superannuation funds – will need to provide much greater disclosure and reporting details on the economic interests within their portfolios. The Australian Securities & Investments Commission (ASIC) will not concern themselves with the fund's domicile meaning Luxembourg-based funds will fall under its net just as much as Cayman funds.

"For any one of these regulatory regimes, the ability to offer look-through capabilities provides the answer. If the investor or underlying manager is only reporting on the immediate asset(s) in the portfolio then there are maybe 40 or 50 asset lines in the portfolio. If the manager must look through these lines to the 40 or 50 portfolio companies or other investments underneath, that is an exponential growth in the volume of information that you'd need to track and report on," says Stevens. This appetite for 14

Growing appetite for hybrid fund structures

Interview with Jesper Steiness & Roger Woolman

"There has been a lot of fund activity in Luxembourg this year focused on private equity and real estate. It's an area of growing investor demand. They are looking for different options now and ways for investing that go beyond hedge funds," observes Jesper Steiness, director of business development EMEA at Advent (Luxembourg).

This is encouraging news for the jurisdiction and suggests the early signs of greater private equity fund formation are favourable. But as Steiness's colleague Roger Woolman, senior solutions consultant at Advent notes, the firm is also working more with hybrid fund structures on a global basis.

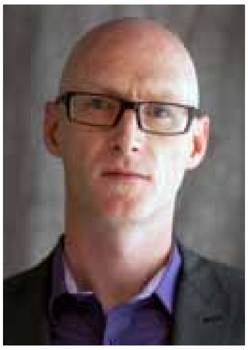
"What I mean by hybrid structures is bank loan funds, real estate debt funds. The hybrid functionality that we have in Geneva has been designed to support these funds that have a private equity-style flow of capital. In addition to hybrid structures we've responded to increased investment activity among the private equity management community by adding native transaction capabilities into Geneva," confirms Woolman.

"We've added functionality around closed-ended funds for fund-of-private-equity-fund investors," says Woolman. "In recent weeks we've had a number of enquiries from firms making direct investments into real estate who want to track the attributions of a building: who is the manager? What is the square footage of the building? What's the rental income?"

Debt products have become an important diversifier for institutional investors. Their proliferation coincides at a time when European banks are removing non-performing loans off their balance sheets in response to Basel III.

Regardless of whether they are portfolios of real assets (companies, properties) or loans, this hasn't put any undue pressure on Advent. As Woolman comments:

Jesper Steiness, director of business development EMEA at Advent (Luxembourg)



Roger Woolman, senior solutions consultant at Advent

"Geneva uses an object-based approach to say 'How does this asset behave?' Some will behave more like fixed income assets, others will behave more like private equity or real estate: real illiquid assets. That's an area where we've really built out functionality over the last two or three years.

"If you put hedge funds in the middle, on the one side you've got private equity and on the other side you've got liquid alternative funds. We get pushed in all directions from managers and service providers. Their client base is not only requesting hedge fund structures but asking managers to do things in private equity and real estate, even asking them to launch long-only funds," adds Steiness. "Today's alternative manager is increasingly doing everything under the sun."

The advantage of using Advent Geneva is that it doesn't matter what the regulation is because of the way the system architecture has been designed – data is derived as and when needed. That's a big advantage, especially to fund administrators who need greater automation to support private equity and hybrid funds.

"We don't need to create new tables or batches; we simply derive what we need in real time. We store very basic information: what are people buying, what are they selling and how does that particular instrument behave?

"From those attributes of a particular instrument we derive things like accruals, cash flows and so on. This places us at an advantage in being able to provide new views, more transparency and different ways to slice and dice data. Providing the relevant information required for the various regulatory requirements is not a problem for Advent Geneva," concludes Woolman. ■

11 ▶ more data will continue to increase, not just to meet regulatory requirements but satiate investors' thirst.

"The costs for providing that information are starting to decrease on a marginal basis. The big service providers are developing smart tools and for us as a firm that's been a key development; to be able to respond to the data needs of our clients by collecting, transforming and reporting it for them. We are building more and more sophisticated and industrial tools to manipulate and present data the way managers want. That is very difficult for small boutique players to do.

"This discussion on risk transparency is moving from an intellectual debate into reality. Managers of Luxembourg funds need to be engaging specialists in smart data who are equipped to provide this service on a variable cost basis," stresses Stevens.

Luxembourg service providers are all too well aware of the pressure that all alternative fund managers are under as they adapt to global regulations. The operational burden it puts on the middle and back office teams is getting heavier each year. Managers don't want to be consumed by reporting and compliance obligations which is why the third party management company solution is becoming an essential solution.

Take, for example, a US hedge fund manager who wishes to expand his investor base in Europe. Do they go to Luxembourg or Ireland? Regulated or unregulated? Where is the best jurisdiction from a tax perspective? Then the manager has to think about their fund strategy. Where are they looking to attract investors? What is their distribution strategy? It quickly becomes very complicated.

"They realise that if they don't raise EUR100-200m within six to 12 months, there's really no point setting up a regulated fund. There aren't too many banks offering full value chain services ranging from platform and ManCo services down to administration services, financing services, asset management services etc. That for us is a clear advantage. We cover financing, cash management, brokerage services, middle office services. We can cover it all," explains Credit Suisse's Zandona.

The point Zandona makes is that asset servicing is a given for financial institutions like Credit Suisse. What is now more important for managers is finding the right solution, the right distribution strategy and how best to cope with regulation for different fund structures. Only after, does the discussion turn to fund services.

"Increasingly, managers are looking for a partner that can support all of their needs and make their lives easier. You don't make life easier just by settling trades faster than everybody else.

"You need to adapt your business proposition to cope with the challenges managers face today and offer support across the entire value chain," adds Zandona.

Maitland too offers a ManCo solution as well as a full SIF platform solution – MS SICAV SIF – for managers who want help setting up new funds to distribute in the EU.

"It was key for us to build a position to support alternative regulated alternative funds, making sure our operational procedures and technology capabilities were up to the task. We have had a lot of enquiries with regard to our platform and ManCo solution. We also see an increase in requests for the Special Limited Partnership. We are talking to some US managers whereas before it would have more continental European managers so we are seeing a shift," confirms Ramachandran.

The great advantage to third party AIFMs and platforms is that it raises the portcullis and stops non-EU managers viewing Europe as a fortress that frankly isn't worth the hassle, or cost, of trying to penetrate.

"The third party ManCo is already popular in Luxembourg under its UCITS regime. There are a lot of these companies operating in Luxembourg. Applying the same model to AIFs under the AIFMD is a good development and makes complete sense," says Ramachandran who, when asked about distribution opportunities under this arrangement.

He concludes: "Typically as the AIFM we would delegate the distribution function where the manager is then free to choose their own sub-distributors. What we help with is registering the fund(s) in different countries. For example, we have assisted with fund registrations for clients in the UK, Spain, Italy, France. Eventually, we will look to offer our own distribution network; we see that as a real opportunity." ■

Full service menu to handle European regulations

Interview with Jean-Daniel Zandona

It is fair to say that alternative fund managers are feeling a degree of regulatory fatigue. Every month, it seems, there are updates, developments and areas of additional compliance. But whilst on the surface this can appear overwhelming, digging a little deeper reveals that service providers are positioning themselves to offer a more complete set of value-added solutions.

As a leading European domicile, Luxembourg is seeing this develop first hand. One firm, Credit Suisse Fund Services, has moved quickly to bring a menu of options to help managers address today's fund management issues.

"Focusing purely on security services, asset servicing is not the main issue; The initial discussion with a client is more about finding the right domicile, fund structure, the right distribution strategy and how to cope with regulation for different fund structures… then comes the discussion about asset servicing. Today, managers are looking more for a banking partner that can support all of their needs and make their lives easier. You don't make life easier just by settling trades faster than anybody else," says Jean-Daniel Zandona, Director, Financial Institution / Asset Managers at Credit Suisse Luxembourg.

As fund managers needs are moving up the value chain, Credit Suisse offers a large range of services ranging from fully-fledged labelled fund platforms and management company services through to administration services, financing services, asset management services, etc. "Offering a wider range of services is for us a clear advantage. At Credit Suisse, we recognise the specific needs of the Assets Managers segment and have designed end-to-end solutions for them." adds Zandona.

Jean-Daniel Zandona, Director, Financial Institution / Asset Managers at Credit Suisse Luxembourg

This is important as it is allowing institutions like Credit Suisse to benefit from this new era of regulation under AIFMD to bring its fund manager clients more deeply into the bank as regulation increases the costs of doing business.

"Being one of the first licensed AIFMs in Luxembourg clearly helped us anticipate the market and better understand the specific needs of in-scope fund managers, being ourselves one of the largest fund managers of Luxembourg funds. We leveraged this experience to also reinforce the management company that we offer for rent to both UCITS and AIFMD-compliant managers, which in turn significantly increased its 3rd party AuM over the last 12 months," says Zandona.

Indeed, under AIFMD, the ability to act as the AIFM on behalf of both EU and non-EU managers is proving to be a real fillip for global banking institutions. Straight away, it takes the regulatory burden off the investment manager's shoulders, leaving them free to focus on running the strategy and raising assets.

Whilst the Management Company for rent is clearly useful, some non-EU managers without a EU footprint need something more complete: that is, a turnkey solution for both the manager and the fund.

"We are seeing non-EU managers coming to Europe to replicate a fund strategy they've been running successfully in their home market to widen their investor base. The AIFMD and UCITS regulation is still a bit unclear to them. We don't realise just how complex and fragmented things can still look from a non-European perspective, despite the recent EU-wide harmonisation efforts deployed. That's the feedback we've been getting from non-EU managers".

"What we realise is that these managers don't want to take too much risk penetrating into Europe. That's why we see more turnkey solutions where firms are coming from outside the EU and renting a cell on a fully-fledged platform," explains Zandona.

By providing a white labelled SICAV fund platform, Credit Suisse is meeting the speed to market and cost challenges that non-EU managers face head-on.

It is, in many ways, a win-win situation. Using a fund platform to test a new product, without having to incur all the set-up costs of a standalone fund, gives the manager a longer runway for raising assets. If successful, they can choose to revert out of the platform and go solo. If it fails, they can terminate the contract with 90 days notice. It basically takes the pressure off launching a regulated fund and trying to raise EUR100-200m within six to 12 months to break even.

"Clients who don't need to use our labelled fund umbrella can create their own fund and rent our management company services. We provide the substance; i.e. the technical infrastructure, operational means, governance and people that need to operate, amongst other duties, risk management, compliance, corporate services and reporting locally to ensure that the fund fully complies with these substance requirements, which really matters from a cross-border distribution and tax perspective." says Zandona.

He adds: "A mid-sized private equity manager might want to focus exclusively on sourcing and executing deals. They may not want the administrative burden imposed by the AIFMD and prefer talking to a single counterparty doing the heavy lifting."

"The global coverage of the bank, both in terms of geographies and products, is a clear advantage when it comes to proposing integrated solutions encompassing various needs along the lifecycle of an investment, from investment structuring, distribution, execution and administration".

"We continue to see strong demand for these 'alternative' fund services in addition to the more traditional asset servicing capabilities that we provide at Credit Suisse"

That Credit Suisse also has a strong credit rating and a fortress balance sheet are key points for managers to consider at the initial discussion phase. An independent

management company or custodian might only have the minimal capital reserves. "When institutional investors perform their due diligence on the fund manager, teaming up with a bank or a management company offering sound financials is key," says Zandona.

It is precisely because of the fact that large bank-owned institutions can bring scale and a comprehensive menu of services that Credit Suisse also offers depositary services under AIFMD. The operational responsibilities are not new, per se, as the firm has been providing custody services for a significant time, given the depth of Luxembourg's UCITS market.

"Depositary services is a low margin business. By offering a widened suite of services including brokerage, custody, management company services and administration, it allows you to leverage off connectivity between each business division across the value chain. You might not be making huge revenues from custody on a stand-alone basis but you are able to achieve greater cost efficiencies by offering a one-stop shop," comments Zandona.

Most managers view regulation as a necessary evil. Yet because many target a relatively limited number of institutional investors, they could have lived with private placement, observes Zandona.

"Fund registration for distribution in foreign countries is becoming an increasingly important topic, where some grey zones subsist. AIFMD is bringing more harmony on paper. As industry practitioners, we are all trying now to make it work practically," concludes Zandona. ■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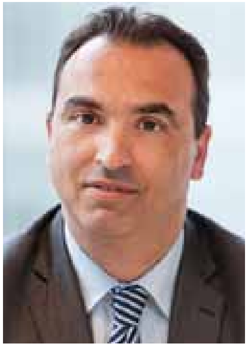
Annex IV reporting: the challenges of a moving target

Interview with Mario Mantrisi

There is no experience as the one gained in the front lines. The fund industry struggles with changing regulation, and those companies whose business model is based on providing reporting services know best that the devil lies in the detail. The following are a number of observations after 12 months of report production and filing of the Annex IV Transparency Reports of AIFMD.



Mario Mantrisi, Senior Advisor to the CEO and Member of the Executive Board at KNEIP

During the preparation phase, KNEIP, one of the industry's long-standing legal and regulatory report providers, has learned a number of lessons that it is applying to ensure that the filing process becomes as hassle-free for managers as possible; in particular non-EU AIFMs who continue to rely on private placement.

"The first point is the number of data sources that are required. It was not a surprise to us that clients didn't have all the data available in one place. It is all over the place and in different systems at the administrator, the prime broker, the custodian, in risk systems etc. This required us to build an interface to our clients to collect all this different data," says Mario Mantrisi, Senior Advisor to the CEO and Member of the Executive Board at KNEIP.

A second challenge relates to the nature of the data. Certain fields required by the Annex IV reports were not easy to interpret. In recent weeks, however, ESMA has provided additional clarification, with some surprises.

"As was known, non-European AIFMs will have to report country by country depending on where they privately place their fund(s). A US manager targeting the UK and the Netherlands, for example, will have to report to both regulators. The surprise is that ESMA has said that to determine the frequency of reporting–which depends on the AuM of the manager – a consolidated AuM position must be taken. That US manager might have EUR500m in the UK and EUR500m in the Netherlands, which ordinarily would equate to two Annex IV reports a year. However, an aggregate AuM of EUR1bn means that the frequency of reporting becomes quarterly rather than semi-annually," explains Mantrisi.

Also, all data on positions in the fund will need to be in notional value. This already applied to derivatives but it will now include traditional securities. "Often the market value and notional value of those securities is the same however there are some instruments where these values differ; e.g. convertible bonds. Another challenging issue is that ESMA is asking for Value at Risk (VaR) numbers to be reported. I understand that some managers do not use this parameter so they will need to start using it for the Annex IV report. This adds another layer of complexity to the data for some managers. This becomes not a data collection issue but a data management issue."

Another challenge that KNEIP is helping clients overcome is that the Annex IV reporting XML standard is not the same for every European regulator. The UK is a case in point. Its regulator, the FCA, insists on the very first version of Annex IV–issued in 2013–and that it has to be used, even though an updated version was released earlier this year. This is an added burden for those managers who are filing in different jurisdictions including the UK as it means they need to manage more than one version of the report.

"Also, the delivery mechanism of how to deliver the report varies from country to country. Some regulators have their own proprietary system, such as the UK with Gabriel, others, such as Luxembourg impose their secured encrypted channels. Many countries, however, still rely on the use of an FTP (File Transfer Protocol) server. Considering the different varieties of transmission mode, this is another real challenge to overcome.

"We suspect that ESMA will come up with additional amendments to Annex IV so managers have to be prepared to understand that this is a moving target," adds Mantrisi.

Over the last 12 months KNEIP has built up a dedicated team to produce and file Annex IV reports on behalf of its clients as newly registered AIFMs come to grips with transparency reporting under AIFMD. It is the first firm to handle both aspects of the process: production and filing. The company is currently working with around 40 clients as they prepare their first filings at the end of October, and many more for the upcoming January filing, according to Mantrisi. "Our teams are very flexible and work hard to ensure all the data is coherent and accurate; and that requires close liaison with managers. It's a comprehensive solution."

The company has a team of 15 staff dedicated to its Annex IV solution and 10 people in IT making sure that all the data interfaces are in place.

Whilst the information contained in Annex IV reports is not made public, managers should also be aware of investor disclosure requirements under AIFMD. The Directive specifies that a certain amount of information must be given to investors before they invest on areas such as investment guidelines, leverage, past performance etc. However, what the Directive does not mention is how to disclose this information.

One of the options is that managers produce a KIID-equivalent document similar to that used for UCITS funds. The KIID is a pre-contractual document so it has to be up-to-date at the moment an investor enters the fund. With respect to this investor disclosure information within AIFMD, not only must it be updated, but in addition the manager has to mention in their annual report the material changes made to this information.

"Therefore, there's an on-going maintenance aspect to the annual report that is not the case under the UCITS regime", confirms Mantrisi. This is something that a lot of managers overlook at the moment.

As Mantrisi concludes: "Managers should be careful not to underestimate the nature of this investor disclosure information and how to maintain it. Although transparency reporting under Annex IV is clearly important, they shouldn't overlook the investor disclosure requirements." ■

Luxembourg develops the right ecosystem to support PERE managers

By James Williams

A true sign of how well a fund jurisdiction is doing is the level of growth, not just in new fund formations, but asset growth within administration firms. The onset of the AIFMD has opened up a new range of services for administrators, in particular by providing a Depo Lite solution to managers running non-EU funds.

Ipes is one of the world's leading private equity fund administrators. According to Justin Partington, Commercial Director at Ipes, "clients are continually asking us about Management Company solutions and providing substance in Luxembourg. There are significant hurdles to set up a ManCo because we think it's a bit conflicting with the administration role."

What Ipes has done, however, is establish a depositary service in the UK. The reason for this was because a lot of managers operating funds out of Luxembourg needed to have a depositary in place from day one. "Also, we work closely with a number of custodial banks so we didn't see the switch play (that is, managers rotating out of existing depositary agreements) as an obvious place to start. We do get some clients asking us to do depositary services in Luxembourg on new funds," adds Partington.

Over the last 12 months, Ipes has seen its client numbers grow from 103 clients to 117 clients. The firm's AuA has similarly grown from USD43bn to USD62bn. On the depositary side, despite only operating since July 2013 it already has 26 clients. On 1 Aug 2014, the FCA listed 17 PE AIFMs, of which Ipes can count 10 of them as clients. The fact that another four of these also use independent depositaries gives a clear insight into how PE managers are approaching the Directive. They want specialist providers, not necessarily bank-owned depositaries.

Bob Brimeyer is Group Head of Fund Services at Alter Domus in Luxembourg. In his view, the introduction of the SCSp was perfect timing. Fund managers have been highly motivated by their investors to consider onshore jurisdictions and as Brimeyer says: "For Luxembourg it was an intelligent initiative to offer a broader suite of products including, regulated vehicles, less regulated vehicles and non-regulated vehicles.

"Having the SCSp is a key success factor, as we are now able to tell global PERE managers who historically have preferred Cayman or UK LP structures, 'Now we can provide the same thing here'. It has certainly helped to remove some of the hurdles that we have faced in the past."

Brimeyer remarks that some competitors have decided to centralise their operations in one jurisdiction, in effect using Luxembourg only for client fronting. However, many of these outsourcing projects do not seem to deliver the expected quality and Alter Domus has been able to win a substantial amount of business as a result: "Our strategy is to service the vehicle out of the jurisdiction where the vehicle is based but using a vertically integrated global platform; all of our offices use the same technology and the same processes, but we deliver the service locally where our clients need us to be."

Simon Henin is the Managing Director of Ipes (Luxembourg). He has no doubt that the SCSp will raise interest from the global PE community, especially for those who chose to go down the non-regulated route. That said, Henin does not yet see any clear push to set up new funds. "Whilst we don't see any clear trends of fund redomiciliation we certainly see more new fund manager startups expressing interest in the SCSp structure. Luxembourg is increasingly being placed on the list of jurisdictions for managers thinking about their next fund," says Henin.

"There are significant hurdles to set up a ManCo because we think it's a bit conflicting with the administration role."

Justin Partington, Ipes

Partington re-emphasises the point by adding: "A lot of US managers have holding companies in Luxembourg. Indeed, most PE managers do if they have Continental European assets. The overwhelming trend that we see is that fund managers aren't changing their fund structure. There have been a couple of notable exceptions (e.g. Swedish PE manager EQT Partners) but in general, people are sticking with the same fund structures for now."

Brimeyer says that there is a move towards onshore funds, initiated in part by the fact that the AIFMD has created more of a level playing field. Brimeyer sees this as a real benefit to Alter Domus going forward.

"There has always been a requirement to appoint a depositary in Luxembourg. We can therefore inform clients, that if they want to set up an AIFMD-compliant fund, Luxembourg is ready with depositaries that have been up and running for the past 15 years. Everyone understands what needs to be done," explains Brimeyer. Since 2008, Alter Domus has serviced PERE funds as well as the holding companies.

This is why these specialist administrators are enjoying a period of growth in Europe. Brimeyer estimates that 80 per cent of new clients opt for a more complete integrated solution, using Alter Domus for both administration and depositary lite services. Of its existing client base, that number is more like 30 to 40 per cent.

"In Luxembourg a new regulatory category of service providers has been introduced specifically to act as the depositary for AIFMD-compliant funds. We decided it was definitely something we should be offering as not many of the custodian banks here are specialised in handling PERE assets. We were the first non-banking financial institutions to acquire a depositary license from the CSSF in Luxembourg," says Brimeyer.

He continues: "Many banks have been ▶ 25

Luxembourg leads in AIFMD stakes

By Kavitha Ramachandran

As the alternative investment market matures, investors are increasingly demanding far more information and transparency from fund managers in return for their capital. Transparency is the new name of the game. In this regard, the Alternative Investment Fund Managers Directive (AIFMD) may be viewed as a single piece of regulation, but its ultimate aims are more or less in line with other regulatory changes such as MiFID II/MiFIR and PRIPS. There will come a point where the reporting and transparency requirements demanded under the AIFMD will become the minimum accepted standard needed to attract investors.

It is within this context that we welcome Luxembourg's status as an AIFMD-friendly jurisdiction and an ideal place in which service providers can set up compliant structures to support their clients' growth into the significant EU alternative investment market. There is no doubt that Luxembourg has become the premier jurisdiction for domiciling alternative investment funds. It sets exacting requirements and demands high standards of skills and experience, substance and reporting transparency.

Maitland has operated in Luxembourg for nearly 40 years, ever since the company was founded in the Grand Duchy in 1976. We are a part of the Luxembourg professional landscape and it was a logical decision therefore for us to choose this jurisdiction to set up our AIFMD compliant solution.

Being an independent third party fund administration business we are able to provide both fund managers and investors with the necessary transparency, independent oversight, controls and segregation of functions, as well as the benefit of our technological platform for reporting requirements, all of which are required under the AIFMD.

Kavitha Ramachandran, Senior Manager, Client Services at Maitland Luxembourg

In May 2014 MS Management Services SA, a Luxembourg-based subsidiary of the Maitland group, was authorised by the CSSF to act as a third-party Alternative Investment Fund Manager (AIFM) for alternative investment funds as well as to the new Maitland Alternative Investment Fund (AIF) platform, MS SICAV SIF.

Fund clients can focus on their core activity of portfolio management but outsource to MS Management Services all the duties envisaged in the AIFMD including risk management, compliance monitoring, regulatory reporting and investor due diligence.

Maitland has also established its own comprehensive AIFMD compliant SIF (Specialised Investment Fund) platform, MS SICAV SIF, for product construction and innovation in the EU. This is a Luxembourg domiciled alternative investment umbrella fund with multiple sub-funds each with flexible investment strategies allowing managers to invest in a range of alternative asset classes and have their "own brand". The SIF has appointed a depositary and auditor that are well established and regulated in Luxembourg with a global presence. Both are independent of Maitland.

Many alternative funds and their managers are currently weighing up the options in terms of the AIFMD. It may seem overwhelming to some to implement the changes needed to attract investors in the EU and they may decide against this but before they do so, we would strongly encourage them to remember that the AIFMD is likely before long to become the minimum accepted standard.

So if the costs are too high to go it alone initially, managers should consider partnering with a service provider as a way of testing the waters before developing a full-fledged AIFM presence later. ■

22 ▶ reluctant to service the different holding companies below a PERE fund. Alter Domus was incorporated in Luxembourg 11 years ago and we have always specialised in handling PERE holding vehicles. We have full control over the holding structure so that makes our lives as a depositary quite straightforward as we know exactly what happens in the structure. It isn't difficult for us to supervise."

Previously, if a PERE manager chose to launch a fund out of Luxembourg they needed to appoint a depositary with a bank license. Now they are free to choose from a wider selection of non-banking service providers.

The big shift for PERE managers under the AIFMD is having to prepare for regulatory reporting – namely Annex IV. The complexity of fund structures and multi-line items in portfolios makes it more of a challenge for the GP to deliver the same kind of transparency that regulators are asking for than say a hedge fund manager. A move into more of a risk transparent environment will take a period of adjustment but software providers like Advent Software are well prepared, not only for PERE managers, but increasingly hedge fund managers who are choosing to launch bank loan and hybrid fund strategies.

"We've always had good coverage within Geneva for credit-type instruments, whether they be bank loans, structured products, asset-backed securities. It's really just a case of taking the business that someone has and understanding how that business behaves. In terms of accounting, our approach is to have all the necessary parameters in place for managers that generate cash flows, P&L flows from whatever kind of instruments; it's all parameter-driven," confirms Roger Woolman, senior solutions consultant at Advent.

Transparency is available for managers throughout Advent, not just in solutions like Geneva World Investor, a piece of Geneva that supports LP-type onshore structures and offshore unit-type structures.

"It depends on where you need to look from and to. Ultimately, for investor look-through capabilities it could be Geneva World Investor or it could be the core Geneva platform; it depends on the type of investor," adds Woolman.

"For Luxembourg it was an intelligent initiative to offer a broader suite of products including regulated vehicles, less regulated vehicles and non-regulated vehicles."

Bob Brimeyer, Alter Domus

Partington says that middle office services to provide LPs with more granular reports are not yet high on the agenda simply because GPs see that as their job. He does however note that LPs are doing increased due diligence on third party administrators and other service providers although "it's still a tiny fraction of the ODD that hedge fund investors conduct".

Henin adds: "Reporting on capital accounts for LPs is new to a lot of Luxembourg service providers under the SCSp but we've been doing this for Anglo-Saxon LP structures for the past 16 years. Our people and systems are fully focused on private equity."

One area of asset class growth that Luxembourg seems to be benefiting from is that of real estate debt funds. It is, says Aexandre Jaumotte, partner and Real Estate and Infrastructure Tax Leader at PwC, Luxembourg, "an area where we are seeing good trends. We now have a specialised team dedicated to supporting these debt funds."

The same is true at Alter Domus which now has a team of 20 people focusing on this asset class.

According to Amaury Evrard, partner, Real Estate Leader at PwC Luxembourg, the rise of real estate debt funds is a combination of managers capitalising on the opportunity to fill the funding gap as banks strengthen their balance sheets and a response to Solvency II.

"It wasn't always straightforward for investors to know in which bucket these real estate debt funds should sit so it took a bit of time to define what type of product it was. It's not completely real estate, it's not completely like other debt or bond funds in the market so it took a bit of time; it's effectively a mixture of the two."

▶ 29

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SCSp gives real estate fund managers greater choice

Interview with Alexandre Jaumotte & Christine Casanova

PwC Luxembourg is the leading professional services firm in the country with around 2,400 people. Similarly, its Real Estate and Infrastructure team is the largest multidisciplinary team of specialists in the Grand Duchy with more than 250 experts supporting global real estate managers; these range from tax advisers and engineers to auditors and fund accountants.

"We service a large segment of the Luxembourg and international real estate market and this allows our team to deliver tailor-made specialised services to our clients," explains Amaury Evrard, Partner and Real Estate Leader at PwC Luxembourg. "We can make the most of our global tax structuring team for managers who choose to operate through Luxembourg RE funds. Our network is very well recognised by the Luxembourg and international real estate community."

Since Luxembourg introduced the Specialised Investment Fund (SIF) in 2007 the number of real estate funds has grown substantially – although precise consolidated figures are not known given that not all funds are regulated. Nevertheless, with the AIFMD in full swing and a new legal structure – the Special Limited Partnership (SCSp) – for managers to use, Luxembourg is well placed to build the same level of success with alternative funds as it did 20 years ago with UCITS funds.

PwC Luxembourg's real estate and infrastructure business is a centre of excellence, working with numerous professional organisations such as, for example, INREV, ALFI (Association of the Luxembourg Fund Industry) and the country's financial regulator, the CSSF. "We sit on numerous committees where alternative fund structures and products are discussed both from a regulatory, a tax and an operational perspective. This helps keep clients up to speed with developments, which in turn benefits their investors," adds Evrard.

Alexandre Jaumotte, partner, Luxembourg Real Estate and Infrastructure Tax Leader, PwC Luxembourg

Christine Casanova, a director in the Alternative Group, PwC Luxembourg

One important group initiated by the Luxembourg Government – the Alternative Investment Group – a few years ago began discussions amongst the market players, the Luxembourg regulator and tax authorities to develop a new and more flexible, legal structure for global managers to avail of. What resulted was the Special Limited Partnership.

"Before the AIFMD came into force, if a real estate or private equity fund promoter wanted a regulated vehicle they would have put Luxembourg products at the top of the list. Conversely, if they wanted something unregulated and more flexible, the UK was often at the top of their short list primarily because of the UK Limited Partnership," explains Alexandre Jaumotte, partner, Luxembourg Real Estate and Infrastructure Tax Leader.

Jaumotte continues: "Then AIFMD arrived and the mindset of real estate managers changed slightly and we started getting approached by a number of private equity and real estate houses to establish regulated products. In the past they would stuck with the UK LP but given that the obligations that the Directive places on the Manager are very similar to those that apply to Luxembourg regulated vehicles, the rationale became: 'Well, if the Manager (the AIFM) has to be regulated anyway it's probably better if the fund is too'.

"Indeed, this helps marketing of the fund without simple duplication of costs and administrative burden. For private equity players, this new partnership form is a new onshore alternative of fund structuring, regulated or not regulated as a product, linked to an EU-based AIFM to access the AIFMD distribution passport to EU investors.

"We quickly realised that what Luxembourg needed was a more flexible legal regime from a corporate governance perspective, that could meet the wishes of fund promoters and which could be either regulated or unregulated. This is where the idea was born to create the Luxembourgish Special Limited Partnership.

"The SCSp has been created through close collaboration between the authorities and the market players."

Christine Casanova, a director in the Alternative Group, explains that alongside the updated SCS regime, managers now have greater choice over whether to establish a structure with (SCS) or without legal personality (SCSp). There will obviously be tax transparency considerations depending on how the partnership is structured.

As Casanova explains: "Investors in some jurisdictions may want to have a partnership without legal personality and this is where the new SCSp is helpful in terms of providing tax transparency. Other investors in other jurisdictions may prefer to invest in a vehicle having legal personality.

"With SCSp, full tax and legal transparency from an investor's perspective may allow them to claim direct treaty benefits with the investment country."

The revamped common limited partnership and the new special limited partnership are both, if properly set up, fully transparent for Luxembourg tax purposes also. No income tax leakage may be expected. There is no withholding tax on payments made by the partnership to the limited partners and the general partner.

This applies whether the partnerships are set up as regulated or unregulated vehicles.

Relying on the full transparency of the partnership for an investor perspective, works well if the GP/LP arrangement consists of a limited number of investors. However, where there are multiple (potentially global) investors involved, Casanova says the partnership might best be structured with a platform underneath to reduce the burden of individual tax filings.

"Here, investors would not rely on tax transparency but would have an entity claiming the treaty benefits on their behalf," adds Casanova.

It is critical for any manager that they work through how best to structure the partnership. They need to decide whether the legal framework has legal personality or not, whether it needs full tax transparency or not, and whether the fund they launch (e.g. a SIF, a SICAR or a Part II fund) will be regulated or not.

Jaumotte says that the two main questions PwC asks its clients are the following:

- #1 – Who are your investors? Are you targeting institutional investors? If yes, are they coming from Europe, the US, Asia? Or are you targeting HNW individuals or corporations?

  "This is a key question because the answer will drive the choice of vehicle," says Jaumotte. "It will help the Manager decide whether they need a regulated or unregulated vehicle. If the Manager is targeting European institutional investors that cannot invest into an unregulated structure then clearly they will go down the regulated fund path. So that's the first question: who are your targeted investors?"
- #2 – Where are your investments located? If, for instance, the Managers invest across Europe in a pan-European fund and they want access to treaty protection and avoid double, even sometimes triple, taxation, then Jaumotte says it may be better to consider a vehicle without the "legal personality than a vehicle with legal personality or to consider the setting-up of an investment platform underneath the fund".

"Depending on what the answers are to these 2 key questions, we can guide the client on whether it's best to have legal personality or not; to have a regulated product or not. Once that is established, one needs to consider whether the fund will be open-ended or closed-ended and what is the distribution policy of the fund because that will also guide the choice and the regulatory regime of the vehicle.

"And of course, there is a taxation consideration. If, for instance, the Manager is targeting tax-exempt institutional investors they will need to invest a fund with no tax on distribution otherwise investors may be hit with different levels of taxation."

The Luxembourg common limited partnership and special limited partnership may be used as funds vehicles but also as e.g. feeder funds or vehicles, as joint venture or co-investment vehicles, a pooling vehicle for management, a carry vehicle in the private equity industry or a property-owning entity in the real estate industry.

As Casanova concludes: "The only limit is imagination." ■

25 ▶ Hugh Stevens is head of Private Equity and Real Estate Services at BNP Paribas Securities Services. Stevens says that some of the world's leading asset managers are taking more of a portfolio approach to structuring real estate. Some refer to the approach as the "four quadrants of real estate": namely public versus private assets, and equity versus debt.

As Stevens explains: "If an investor wants to invest in Emerging Market real estate, for example, a manager will first look at the fundamental economics and decide which countries to target. The next decision is how to structure the product. That will depend on the investor; where they are domiciled and what regulations they are exposed to and what capital charges might apply.

"If the best option for the investor is to structure something in public equity then a Reit might be chosen. If the option taken is private equity, then a private real estate fund might be the best option as a closed-ended fund structure. Or the investor may prefer to go down the private debt route, in which case a real estate loan fund might be an option. Finally, if they decide on public debt a listed debt fund or a CMBS vehicle might be used."

East Capital is a Swedish frontier and emerging markets asset manager with a well-established UCITS business as well as an alternatives business. According to Magnus Lekander, General Counsel at East Capital, the AIFMD "has been a catalyst for consolidation of our business and has brought us efficiency gains. When you look at PERE managers, they have struggled more than hedge funds because they've never had to come under supervision and have had to make more changes to their businesses to accommodate these new rules.

"We have all the necessary processes in place because we've been running UCITS funds for 17 years. We run real estate and private equity funds as a separate silo to our main business. By establishing one management company – East Capital Asset Management SA – last year, we've been able to consolidate our business. Our Luxembourg management company manages both our UCITS and SIF platforms," explains Lekander.

East Capital has been running daily traded retail funds out of Luxembourg since 2005 under a SICAV structure. Back in 2009, the firm recognised that the AIFMD was coming and started to explore which domiciles it thought would best cope the new regulations. In that sense, Luxembourg was an easy choice. What resulted was a gradual migration of its offshore Cayman funds onto an AIFMD-compliant SIF platform.

"The AIFMD has been a catalyst for consolidation of our business and has brought us efficiency gains."

Magnus Lekander, East Capital

"We currently have six strategies on our SIF platform: one real estate fund, a special situations fund, a China A Shares fund, a Russia domestic growth fund, a deep value fund and the East Capital New Markets fund. The last two funds were Cayman funds that we moved onshore as part of our adaption to AIFMD. Originally these two Cayman funds were four separate strategies which we decided to re-model. We could see the operational benefits of plugging these offshore strategies into our SIF platform," states Lekander.

The most recent fund launch was the East Capital China A-shares fund last December. The fund is long-only but sits on the SIF platform as China's QFII regime does not lend itself favourably to UCITS limitations. Despite only being available to Swedish investors, based on the Memorandum of Understanding between Sweden and China to avail of the QFII quota, the fund is already closed with USD125mn in AuM.

"Our current QFII license goes through Sweden but the special treatment that Luxembourg has received is definitely something we'll explore further. We can see a niche in this market. We want to establish ourselves as a leading player offering this limited access to China's market," says Lekander. With real estate debt funds on the rise, a potential Reit product on the horizon and an RQFII programme to tap in to, global managers suddenly have a number of compelling reasons to use Luxembourg as their springboard. ■