

Luxembourg Publishes Bill of Law on Reserved Alternative Investment Funds

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The Luxembourg Council of Government approved on 27 November 2015 the bill of law (“**Bill**”) on reserved alternative investment funds (“**RAIF**”), a new form of Luxembourg alternative investment fund (“**AIF**”). The Bill was deposited with the Luxembourg parliament on 14 December 2015 and was published under number 6929 today.

In the post-AIFMDⁱ environment – where regulation is focused on the alternative investment fund manager (“**AIFM**”) of the AIF and only indirectly imposes certain requirements upon the AIF itself – the Luxembourg Government is creating a fund vehicle with the advantages of specialized investment funds (*fonds d’investissement spécialisé* or “**SIF**”) or investment companies in risk capital (*sociétés d’investissement d’investissement en capital à risque* or “**SICAR**”) in terms of structuring (e.g., ability to adopt a variable capital structure and to establish sub-funds) without being required to seek prior authorization by the Luxembourg supervisory authority, the *Commission de Surveillance du Secteur Financier* (“**CSSF**”). The Bill is largely inspired by the Luxembourg SIF Lawⁱⁱ and the Luxembourg SICAR Lawⁱⁱⁱ.

Main features and conditions to be fulfilled by the RAIF

Obligation of an external AIFM

The RAIF is an undertaking for collective investment that always qualifies as an AIF^{iv}. Unlike the SIF or the SICAR, the RAIF cannot be structured as a non-AIF^v.

The RAIF must always be managed by an external AIFM that does not seek exemption from the AIFMD under the sub-threshold regime of article 3(2) of the AIFMD^{vi}.

Although the RAIF will not be authorized by the CSSF, the AIFM must ensure that the AIF complies with the conditions set under the AIFMD. The RAIF is therefore indirectly regulated, as it is managed by an external AIFM that in turn must be authorized.

An AIFM must notify its supervisory authority once it starts to manage a RAIF.

Eligible investments – risk spreading – concept of risk capital

The RAIF can invest in any type of assets and follow any type of investment strategy.

The portfolio of the RAIF must be managed under the principle of risk spreading, unless the RAIF invests exclusively in risk capital.

The Bill simply refers to the requirement of risk spreading (as is the case in the SIF Law), but does not provide further guidance. The concept of risk capital in the Bill is taken from the SICAR Law, and provides that investment in risk capital means the direct or indirect contribution of assets to entities in expectation of their launch, development or listing on a stock exchange.

The governing body of the RAIF has the responsibility to assess the level of risk spreading deemed appropriate for the RAIF’s portfolio, or, where applicable, whether the investments of the RAIF may qualify as risk capital. As a starting point, references might be made to the current guidelines on risk spreading applicable to SIFs^{vii} and on the concept of risk capital applicable for SICARs^{viii}.

The question may be raised whether the RAIF may have as main object lending activities without falling into the scope of article 28-4^{ix} of the Luxembourg law of 5 April 1993 on the financial sector, as amended (“**Financial Sector Law**”) as the Bill does not contemplate to amend the Financial Sector Law to explicitly exclude the RAIF from the scope of the Financial Sector Law as it is the case for the SIF or the SICAR.

Management and administration of the RAIF

Any authorized AIFM established in Luxembourg or another EU Member State can manage the RAIF. A non-EU AIFM will be permitted to manage a RAIF when the non-EU AIFM is authorized under the passport regime to manage and/or market an AIF in the EU^x.

The safe-keeping of the assets of the RAIF must be entrusted to a Luxembourg depositary, which can either be a Luxembourg credit institution or the Luxembourg branch of a credit institution established in another EU Member State. If the RAIF invests mainly in non-financial instruments, is not leveraged and does not grant any redemption rights to its investors during a period of five years after the first investment has been made, the depositary can also be a depositary of assets other than financial instruments, under article 26-1 of the Financial Sector Law.

The administration of the RAIF must be conducted in Luxembourg. As an undertaking for collective investment, the administration and register-keeping of a RAIF can only be entrusted to an administrative agent^{xi} and registrar^{xii} authorized by the CSSF under the Financial Sector Law.

The RAIF must establish an annual report, which is made available to the investors within six months after the closing of the accounting year. The annual report must be reviewed by a Luxembourg statutory auditor (*réviseur d'entreprises agréé*). Separate annual reports may be established on a sub-fund basis, provided consolidated information on all sub-funds is also contained in these annual reports.

Structures available to the RAIF

The RAIF can be structured as: (i) a common fund (*fonds commun de placement* or “**FCP**”), which is a contractual co-ownership scheme without legal personality; (ii) an investment company with variable capital (*société d'investissement à capital variable* or “**SICAV**”) whose capital is automatically adjusted to its net asset value (“**NAV**”); or (iii) in a form other than FCP or SICAV in which case the capital of the RAIF is generally fixed.

The RAIF in the form of an FCP must always be managed by a Luxembourg management company. This management company can be a Luxembourg AIFM^{xiii}. If the Luxembourg management company^{xiv} is not authorized as a Luxembourg AIFM, it must appoint an AIFM either in Luxembourg or in another EU Member State.

In the case of a SICAV, the RAIF can be formed as a public limited liability company (*société anonyme* or “**SA**”), private limited liability company (*société à responsabilité limitée* or “**Sàrl**”), corporate partnership limited by shares (*société en commandite par actions* or “**SCA**”), common limited partnership (*société en commandite simple* or “**SCS**”), special limited partnership (*société en commandite spéciale* or “**SCSp**”) or cooperative company formed as a public limited liability company (*société cooperative sous forme de société anonyme* or “**SCoSA**”).

The RAIF can be structured as an umbrella fund with one or more sub-funds, where the assets and liabilities of each sub-fund are segregated from the assets and liabilities of other sub-funds, unless otherwise stated in the constitutive documents of the RAIF. The Bill also permits cross-investment between sub-funds.

Creation of the RAIF

Based on the Bill, the creation of the RAIF must be acknowledged by notarial deed. Within ten days of its creation, a confirmation (which must contain the identity of the AIFM of the RAIF) will be deposited with the Luxembourg trade and companies' register and published in the Luxembourg official gazette.

RAIFs must be registered on a publicly available list maintained by the Luxembourg trade and companies' register.

Eligible investors – marketing of the RAIF

Only well-informed investors will be admitted to the RAIF. The definition of well-informed investor is taken from the SIF Law and the SICAR Law, which distinguish among three types of investors: (i) institutional investors (as defined by the administrative practice of the CSSF); (ii) Professional Investors^{xv}; and (iii) well-informed investors – this category refers to any investor who is neither an institutional investor nor a Professional Investor, and who invests or commits to invest at least EUR 125,000 in the RAIF and confirms in writing to maintain the status of a well-informed investor. In instances where an investor who is neither an institutional investor nor a Professional Investor wishes to invest less than EUR 125,000 in the RAIF, such investor's experience and knowledge to adequately appraise the investment in the RAIF must be certified pursuant to an assessment by: a credit institution (within the meaning of Directive 2006/48/EC); an investment firm (within the meaning of Directive 2004/39/EC); or a management company (within the meaning of Directive 2009/65/EC).

As a RAIF is required to appoint an authorized AIFM, the RAIF can be marketed to Professional Investors in the various EU Member States under the passport regime, in accordance with the notification process established under the AIFMD.

A RAIF must establish an issuing document that contains all information necessary for investors to assess their participation in the RAIF. To avoid any confusion with a SIF or a SICAR (whose issuing documents are filed with the CSSF), the cover page of the RAIF's issuing document must clearly indicate that the RAIF is not subject to the supervision of the CSSF. Important information in the issuing document must be kept up-to-date before new investors are admitted to the RAIF. Separate issuing documents may be established on a sub-fund by sub-fund level, provided that the issuing document of a relevant sub-fund discloses that there are other sub-funds.

Although marketing under the passport regime of the AIFMD is limited to Professional Investors, well-informed investors who do not qualify as Professional Investors are permitted under the Bill to invest in the RAIF.

Tax regimes

As with the SIF, the RAIF is subject to an annual subscription tax (*taxe d'abonnement*) of 0.01% unless it invests exclusively in risk capital. The RAIF is exempted from the subscription tax on, among other items, investments in other Luxembourg undertakings for collective investment subject to the subscription tax. A RAIF whose investment objective is to invest in money market instruments and bank deposits or microfinance, or whose units or interests are held by institutions for occupational retirement or by similar institutions, is also exempted from the subscription tax.

Where the constitutive documents of a RAIF exclusively limit investment in risk capital, income generated from securities or capital gains is exempted. In such a case, the tax regime of the RAIF is thus comparable to that of the SICAR.

The applicable tax regime must be determined for the RAIF as a whole – the Bill does not enable that a relevant sub-fund is subject to the subscription tax whilst another sub-fund is subject to a tax regime comparable to SICARs.

Comparison of the RAIF to other Luxembourg regulated and unregulated AIFs

	Luxembourg ordinary company	Part II UCI ^{xvi}	SIF	SICAR	RAIF
Qualification under the AIFMD – Supervision – Regulation					
Qualification as an AIF	Generally, an ordinary company is a non-AIF unless its activities fall within the scope of article 1(39) of the AIFM Law.	Always an AIF.	In principle, an AIF unless the SIF does not raise capital from investors.	In principle, an AIF unless the SICAR does not raise capital from investors.	Always an AIF.
Exemption from the AIFMD under the Lighter Regime	Possible.	Possible.	Possible.	Possible.	Not possible.
Appointment of an external authorized AIFM	Required if the company is an AIF that is not internally managed and whose assets under management (“AUM”) are above the threshold of the Lighter Regime.	Required if the Part II UCI is not internally managed and its AUM are above the threshold of the Lighter Regime.	Required if the SIF is an AIF that is not internally managed and whose AUM are above the threshold of the Lighter Regime.	Required if the SIF is an AIF that is not internally managed and whose AUM are above the threshold of the Lighter Regime.	Always required.
Authorization and supervision by the CSSF	No.	Yes.	Yes.	Yes.	No.
Risk spreading requirement	No.	Yes.	Yes.	No.	Yes, unless investments are made in risk capital only.

Registered Office – Administration – Depositary – Audit					
Registered office and administration	Registered office must be in Luxembourg; administration is generally in Luxembourg.	Registered office and administration must be in Luxembourg; administration can only be delegated to a service provider authorized by the CSSF under the Financial Sector Law.	Registered office and administration must be in Luxembourg; administration can only be delegated to a service provider authorized by the CSSF under the Financial Sector Law.	Registered office and administration must be in Luxembourg; administration can only be delegated to a service provider authorized to provide administration services.	Registered office and administration must be in Luxembourg; administration can only be delegated to a provider authorized by the CSSF under the Financial Sector Law.
Appointment of a depositary	Luxembourg depositary under article 19 of the AIFM Law ^{xvii} is required if the company is an AIF either managed by an external AIFM whose AUM are above the threshold of the Lighter Regime or if the company is an internally managed AIF with AUM above this threshold. Otherwise, there is no obligation to appoint a depositary.	Luxembourg depositary under article 19 of the AIFM is required if AUM of the external AIFM are above the threshold of the Lighter Regime or if the AUM of the internally managed Part II UCI are above this threshold. Otherwise a Luxembourg depositary fulfilling the requirements and the obligations under part II of the UCI Law ^{xviii} must be appointed.	Luxembourg depositary under article 19 of the AIFM is required if the SIF is an AIF and AUM of the external AIFM are above the threshold of the Lighter Regime or if the AUM of the internally managed SIF are above this threshold. Otherwise a Luxembourg depositary fulfilling the requirements and the obligations under part I of the SIF Law must be appointed.	Luxembourg depositary under article 19 of the AIFM is required if the SICAR is an AIF and AUM of the external AIFM are above the threshold of the Lighter Regime or if the AUM of the internally managed SICAR are above this threshold. Otherwise a Luxembourg depositary fulfilling the requirements and the obligations under part I of the SICAR Law must be appointed.	Luxembourg depositary under article 19 is always required.
Appointment of an auditor	Required, unless the company is not an AIF managed by an AIFM with AUM above the threshold of the Lighter Regime and two of the	Required.	Required.	Required.	Required.

	following three criteria are fulfilled: (i) balance sheet below EUR 4.4 million; (ii) net turnover below EUR 8.8 million; and (iii) average number of employees below 50.				
Structuring Options – Tax					
Possibility to adopt variable capital structure	Joint stock companies cannot be structured with variable capital.	Yes.	Yes.	Yes.	Yes.
Possibility to be structured as a common fund	No.	Yes.	Yes.	No.	Yes.
Possibility to create sub-funds	No.	Yes.	Yes.	Yes.	Yes.
Subject to ordinary tax regime on profit and wealth	Yes, unless the company is an AIF adopting the form of an SCS or SCSp which are tax transparent and considered as not carrying out a business activity under circular LIR 14/4 of the Luxembourg tax authorities, provided the general partner formed as a joint stock company does not hold more than 5% of the interests of the AIF.	No.	No.	In principle, a taxable person whose income and capital gains from securities qualifying as risk capital are exempted. Exempted from wealth tax.	No.

Subscription tax	No.	Annual subscription tax of 0.05% on NAV (with possibilities to partially reduce the rate to 0.01% or to be exempted).	Annual subscription tax of 0.01% on NAV (with possibilities to be exempted).	No.	Annual subscription tax of 0.01% on NAV (with possibilities to be exempted), unless the AIF is joint stock company exclusively investing in risk capital (in which case, income and capital gains generated from securities qualifying as risk capital are exempted).

Conversion of an existing Luxembourg entity into a RAIF

A SIF or SICAR can be converted into a RAIF in accordance with applicable laws and the provisions governing its constitutive documents. The conversion is subject to the prior approval of the CSSF with respect to the amendments of the entity's constitutive documents.

A non-regulated Luxembourg entity can also be converted into a RAIF. In addition to applicable laws and the provisions governing the constitutive documents of the relevant entity, the Bill imposes that the conversion is approved with a majority of at least two third of the shareholders/partners of the relevant entity. The Bill does not require a minimum quorum for the conversion.

Next steps

The Bill will now be under review by the Parliament. The Luxembourg State Council (*Conseil d'Etat*) and the Chamber of Commerce (*Chambre de Commerce*) are requested to provide their comments. It is generally expected that the Bill will be adopted by the Parliament in the course of the second quarter of 2016.

ⁱ Directive 2001/61/EU on Alternative Investment Fund Managers.

ⁱⁱ Law of 13 February 2007 on SIFs, as amended.

ⁱⁱⁱ Law of 15 June 2004 on SICARs, as amended.

^{iv} AIFs are collective investment undertakings, including any sub-funds thereof, that: (a) raise capital from a number of investors, with a view to investment in accordance with a defined investment policy for the benefit of those investors; and (b) do not require authorization pursuant to article 5 of Directive 2009/65/EC on undertakings for collective investment funds in transferable securities.

^v SIFs or SICARs who do not raise any capital from investors do not fall within the scope of the definition of an AIF under article 1(39) of the law of 12 July 2013 on alternative investment fund managers ("**AIFM Law**"). Illustrations of such SIFs or SICARs are entities whose access is limited to a predefined group of investors or which have only one investor within the meaning of the final report on guidelines on key concept of the AIFMD 2013/600 of ESMA.

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- vi The sub-threshold exemption applies to AIFMs managing assets below EUR 100 million, or below EUR 500 million provided no redemption rights are granted to investors during a minimum period of five years after the first investment was made and no leverage is undertaken. AIFMs qualifying for this exemption must only register with their home supervisory authority for the purpose of reporting.
 - vii CSSF circular 07/309 on risk spreading.
 - viii CSSF 06/241 on the concept of risk capital.
 - ix Professionals performing lending operations under article 28-4 of the Financial Sector Law are professionals engaging in the business of granting loans to the public for their own account. These professionals shall be authorized by the Minister of Finance.
 - x Article 66(3) of the AIFMD.
 - xi Article 29-2 of the Financial Sector Law.
 - xii Article 25 of the Financial Sector Law.
 - xiii The management company is authorized as an AIFM under article 125(2) of the UCI Law.
 - xiv The management company which is not an AIFM is subject to article 125(1) of the UCI Law.
 - xv Professional Investor as defined under Directive 2015/65/EU on markets for financial instruments.
 - xvi A Part II UCI is an undertaking for collective investment under part II of the law of 17 December 2010 on undertakings for collective investment, as amended. Units of a Part II UCI can be distributed to retail investors in Luxembourg and abroad, provided local rules on marketing permit the distribution to retail investors.
 - xvii The depositary under article 19 of the AIFM Law must fulfill the requirements and the obligations set under the AIFMD.
 - xviii Luxembourg law of 17 December 2010 on undertakings for collective investment, as amended.

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