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**European Investment
Fund**

AGENDA

- Introduction
- Key considerations in structuring a fund
- Some examples (UK vs Luxembourg)
- Alternative Investment Fund Manager Directive
- Q&As

KEY CONSIDERATIONS IN STRUCTURING A FUND

- Tax Efficiency (for all parties involved)
 - Avoid double taxation (i.e. fund and investors)
 - Low tax rates or *ad hoc* exemptions
 - VAT on management fee
 - Carried interest
- Suitability for Investors
 - Familiarity of structure
 - Certainty re legal and regulatory
 - Limited liability
 - "Control"
- Ease of Operation
 - Corporate governance
 - Regulatory Authorities
 - Need for service providers – proven system
- Costs
- Marketing

UNITED KINGDOM (Limited Partnership)

- Tax efficiency
 - Typically avoids double taxation
 - No VAT on management fee – priority share of profits
 - Carried interest typically taxed as capital gain (not income)
 - No tax for non-resident investors
- Suitability for Investors
 - Most familiar structure for institutional investors
 - Offers certainty re legal and regulatory status
 - Limited liability for Investors
 - Legal documentation (LPA) is well standardised and tested and offers flexibility
- Ease of Operation
 - Light corporate governance
 - No need for third party service providers
- Costs: generally limited
- Marketing: OK to institutional investors (no to the general public)

LUXEMBOURG (SICAR, SIF, FCP)

- Tax efficient
 - Depending on the form, tax opaque/transparent - Typically avoids double taxation
 - If taxable entity is chosen – extended tax exemption regime
 - No VAT on management fee
 - No tax for non resident investors
 - Carried Interest - depending on the structure, efficient options available
- Suitability for Investors
 - Recognised by most institutional investors (OECD white list)
 - Legal (flexible – continental Europe) and regulatory (CSSF supervision)
 - Limited liability for Investors
 - Legal documentation typically more cumbersome as a result of corporate structure, regulatory constraints and need to for service providers
- Ease of Operation
 - Corporate Governance – Typical of corporate/continental European structures
 - Service providers needed: Custodian and Depository (acting independently in the interest of Investors)
- Costs: higher– but to be balanced against the comfort re independent scrutiny
- Marketing: OK to institutional investors (no to the general public)

Country (Structure)	Tax transparent for domestic investors?	No permanent establishment for international investors	Ability to incorporate a capital investment/incentive for fund managers	No VAT on management charges	No VAT on carried interest	Freedom from restrictions on investments
Austria (MFAG)	✓ ¹	✓	✓	✓ ²	✓ ³	✓ ⁴
Belgium (limited company or privak)	✗	N/A	✓	✗ ⁵	✓	✓ ⁶
Czech Republic	✗	✓	✗	✓	✓	✓ ⁷
Denmark	✓	✓	✓	✗	✓	✓
Finland (limited partnership)	✓	✓	✗	✓	✓	✓
France (FCPR)	✓	✓	✓	✗ ⁸	✓	✗
Germany (limited partnership)	✓	✓	✓ ¹⁰	✗	✓	✓
Hungary (Private Equity Fund or Investment Fund)	✓ ¹¹	✓	✓ ¹²	✓ ¹³	✓ ¹⁰	✓
Ireland	✓	✓	✓	✓	✓ ¹⁴	✓
Italy (<i>fondo chiuso</i>)	✗ ¹⁵	✓	✓	✓	✓	✓
Luxembourg (SICAR, SIF)	✓ ¹⁶	✓ ¹⁷	✓	✓	✓	✓
Netherlands (limited partnership)	✓	✗ ¹⁸	✓	✓	✓	✓
Poland	✓	✓	✓	✓	✓	✓
Portugal (VCC (SCR) - CRF (FCR))	✗	N/A	✓	✓	✗	✗
Slovak Republic	✗	✓	✓	✗ ¹⁹	✓	✓ ⁷
Spain (SCF-FCR)	✗	N/A ²⁰	✓ ²¹	✓ ²²	✗ ²³	✗
Sweden (limited partnership)	✗	✗	✓	✓	✓	✓
Switzerland ²⁴ (investment company)	✗ ²⁵	✓	✗ ²⁶	✗ ²⁶	✗ ²⁶	✓
United Kingdom (limited partnership)	✓	✓	✓	✓	✓	✓

Alternative Investment Fund Manager Directive (AIFM)

- Background – response to financial crisis: fund managers should register and disclose activities to increase transparency, improve investors protections and minimise threats to the stability of financial system
- Aims at establishing common requirements for fund managers and provide an harmonised and stringent regulatory framework for the activities of fund managers operating across the EU
- Timing
- To apply also to managers established in the EU when managing a fund established outside the EU
- To apply also to managers established outside the EU when marketing a fund in the EU

Alternative Investment Fund Manager Directive (cont'd)

- Basic issues:
 - Manager to be authorised
 - Conduct of business/conflict of interest/risk management
 - Systems and controls
- More serious issues:
 - Reporting/valuations
 - Disclosure
 - Remuneration policy
 - Regulatory capital
 - Depository
 - Marketing (pre notification + restrictions)
 - Not yet clear: marketing of non EU funds; investors access to non-EU funds; non-EU investors access to EU funds

CONCLUSIONS

Questions?

OVERVIEW OF PRINCIPAL TYPES OF FUND STRUCTURES IN EU

Suitable tax/legal structures

Country	Local Investors	Foreign Investors
Austria	Mittelstandfinanzierungsaktiengesellschaft or AG	Mittelstandfinanzierungsaktiengesellschaft or AG/Foreign structures
Belgium	NV (Participation Privilege) and foreign structures	Foreign structures preferable, possibly NV subject to tax treaty
Czech Rep.	s.r.o. (similar to private company)	Foreign structures preferable
Denmark	Local company possible: no tax on gain if investment held for 3 years	Foreign structures preferable
Finland	Limited Partnership	Limited Partnership for investors from tax treaty countries Foreign structures preferable for investors from non-treaty countries
France	FCPR, FCPI, FIP or SCR	FCPR or FCPI or foreign structures
Germany	GmbH, GmbH & Co KG or UBG	Foreign structures or passive investment partnerships
Hungary	Private Equity Fund Investment Fund	Foreign structures preferable

Country	Local Investors	Foreign Investors
Ireland	Limited Partnership	Limited Partnership
Italy	closed-end structure or foreign structures	Foreign structures preferable
Luxembourg	SICAR, SICAV (SIF) or FCP (SIF)	SICAR, SICAV (SIF) or FCP (SIF)
Netherlands	BV or NV (Participation Privilege) & CV (Partnership)	BV or NV (Participation Privilege) & CV (Partnership)
Poland	Limited liability company	Limited liability company
Portugal	Local corporate structure, but very restrictive	Only foreign structures
Spain	Local corporate structure, but very restrictive	Foreign structures
Slovak Rep	s.r.o. (similar to private company)	Foreign structures preferable
Sweden	Limited Partnership, Qualified Investment Company and Consortium	Foreign structures preferable
Switzerland	Foreign limited partnership structures preferable for tax reasons	Foreign limited partnership structures preferable for tax reasons
UK	Limited partnership, Investment Trust, Venture Capital Trust & other structures	Limited partnership & other countries

Notes:

- ¹ Tax exemption.
- ² Depending on structure/clarification with fiscal authorities recommended.
- ³ Depending on structure.
- ⁴ For tax benefits, restrictions have to be considered; can be avoided by using another – less tax advantageous – structure.
- ⁵ Under certain conditions, option is granted to avoid VAT on management charges (provided falling within the scope of Director power as stated in the by-laws). Moreover, it is possible to « reduce » the VAT cost by assuring that certain services can benefit from specific VAT exemptions (e.g. transaction in shares). Finally, a particular exemption provision applicable to management of investment funds could be applied provided certain conditions are met.
- ⁶ It should be noted that a Privak is subject to restrictions on the type of investment which can be made.
- ⁷ There are some restrictions relating to investments into specific sectors such as the defence sector.
- ⁸ The management company can choose not to charge VAT, but in that case it cannot itself deduct VAT and has to pay a tax on the wages it pays out, so that ultimately it needs to raise the amount of management fee it asks from the investors.
- ⁹ From a tax point of view and in order to avoid a permanent establishment for foreign investors, certain investments such as in trading partnerships should be avoided. The non-trading status of certain partnerships may change in the future.
- ¹⁰ The carried interest treatment may change in the future.
- ¹¹ Hungarian fund vehicles regulated by domestic law (Private Equity Fund and Investment Fund) are tax transparent for domestic investors although in practice these are hardly used. Non-Hungarian investors usually prefer to use non-Hungarian fund vehicles. The tax treatment of non-Hungarian vehicles will vary but if treated as tax transparent in their home jurisdictions, then Hungary should in principle accept this approach.
- ¹² Usually these are non-Hungarian based.
- ¹³ This results in the non-deductibility of the input VAT.
- ¹⁴ Yes, if structured in a way that these retain the same character as the distribution that gave rise to them (e.g. capital gains, dividends, etc).
- ¹⁵ Despite the fact that the *Fondo Chiuso* is not tax transparent, non-business investors and all international investors from Treaty Countries benefit from specific exemptions which in substance give the same results of tax transparency.
- ¹⁶ The Luxembourg SICAR may be established under the form for fiscally transparent (SCS) or fiscally opaque (SARL, SA, SCA, and SCSSA) undertakings.

Note: In each case the most appropriate structure available in each country has been taken (cont').

- 17 Not an issue in case of a fiscally opaque SICAR. May well be an issue in case of a transparent SICAR. See footnote 16.
- 18 Each foreign investor will be considered to be engaged in the conduct of a business through a Dutch permanent establishment to which the shares in the portfolio companies must be allocated. In computing the taxable profit of the permanent establishment, however, the benefits (gain and dividend) derived from the portfolio companies should generally be exempt under the participation exemption.
- 19 It should be noted that it is possible to « reduce » the VAT cost by localising certain services outside the EU (e.g. administrative services) or by assuring that certain services can benefit from specific VAT exemptions (e.g. transaction regarding shares).
- 20 The mere fact of investing through an SCR/FCR would not give rise « per se » to a permanent establishment in Spain. Investing through an SCR/FCR could give rise to a permanent establishment in Spain depending on several circumstances, but there are ways for an international investor investing in Spain through and SCR/FCR to avoid a permanent establishment in Spain.
- 21 The SCR/FCR current regulations do not allow to structure easily a tax efficient carried interest for the promoters. Thus, carried interest structures are complicated.
- 22 These management changes are usually VAT exempt in Spain. However, advisory fees charged to the Manager bear VAT, which is usually a cost for the manager.
- 23 The SCR/FCR current regulations do not allow to structure easily a tax efficient carried interest for the promoters. Thus, carried interest structures are complicated. Additionally, where carried interest is possible, it would normally be structured as rendering of services and consequently VAT would not be avoided.
- 24 In Switzerland, regulatory reasons prevent the use of Swiss investment funds (contractual structure) for typical private equity structures. The only local structure available for private equity funds is the investment company. Because of the many disadvantages of the investment company (including absence of tax transparency), offshore structures (e.g. limited partnerships) are the most common vehicles.
- 25 There might be further developments on this issue with the complete overhaul of the Swiss legal framework applicable to investment funds, which will be replaced by a new « Collective Investment Schemes Act » the draft of which is currently pending before Swiss parliament.
- 26 There is no tax efficient option to structure a carried interest payable to the fund managers other than as a « performance fee » which is subject to Swiss VAT (not recoverable by the fund) and to income tax at the level of the fund manager.