CLIFFORD

CHANCE

# ALTERNATIVE INVESTMENT FUNDS
## THE LUXEMBOURG TOOLBOX

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“The Luxembourg toolbox for alternative investment funds offers tailored solutions for fund managers and investors, allowing a combination of features from different jurisdictions. Notably thanks to its limited partnership regime, the needs of clients from both common law and civil law jurisdictions can be accommodated.”

# WHY LUXEMBOURG?

1. Luxembourg, your gateway to Europe and beyond
2. Steady growth in alternative investment sectors
3. A unique and innovative toolkit of investment products
4. Flexible structuring options for operating AIFMs
5. A stable and trusted jurisdiction
6. An established experience in servicing alternative assets
7. An international and multilingual environment
8. A pragmatic legal and supervisory framework
9. A favourable and predictable tax environment `
10. A forward-looking and innovative global player

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# LUXEMBOURG'S FUND INDUSTRY

In recent years, Luxembourg has become an overachiever when it comes to the alternative investment fund industry. At December 2019, the net assets under management in Luxembourg funds amounted to EUR 4,718.9 billion, growing by an impressive 16.10% year-on-year. Knowing that this only captures regulated funds – while most alternative funds in Luxembourg are unregulated, this is a remarkable success.

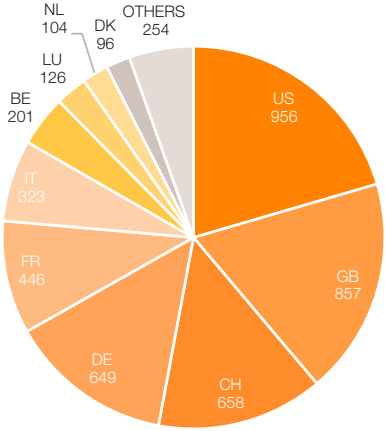
This puts the Grand Duchy of Luxembourg in the top league, qualifying as the second largest fund center worldwide, following the United States.

The Luxembourg market is enticing to a wide number of fund initiators stemming from various jurisdictions. The top three (in terms of assets under managements) as at 31 December 2019 were the United States, the United Kingdom and Germany.

Luxembourg has been a first mover in the implementation of European fund regulation since 1988, including the European Union's Alternative Investment Fund Managers Directive (AIFMD). The country has played a pivotal role in opening-up markets for international fund distribution due to its long history of creating products that enable firms to develop their businesses.

Luxembourg is characterised by a highly flexible regulatory framework and has constantly adapted its legislation to the needs of the market. This particularly innovative legal framework gives a real advantage in the development of new products and investment vehicles.

**Origin of sponsors of Luxembourg funds**




**NUMBER 1 INVESTMENT FUND CENTER IN EUROPE**

**NUMBER 1 IN CROSS-BORDER FUND DISTRIBUTION**

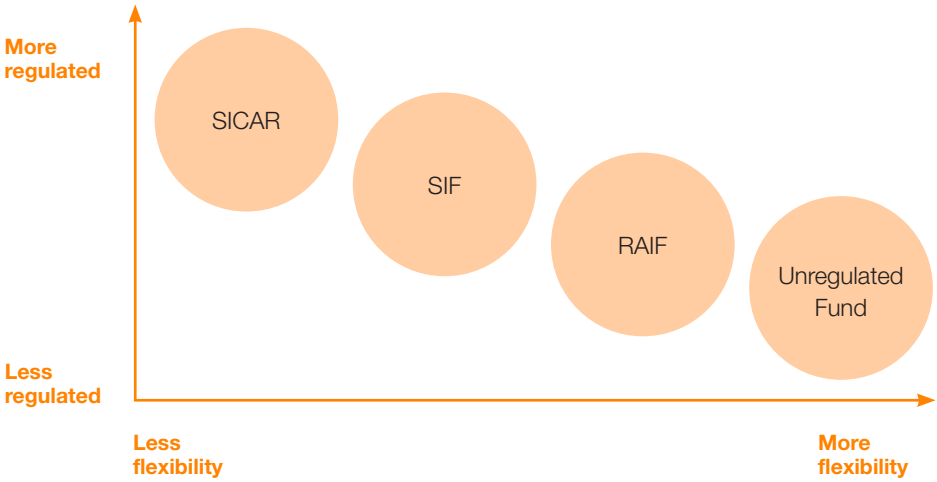
# AIFMD

The AIFMD, implemented in Luxembourg in 2013, has created the first regulated environment for alternative investment funds worldwide – and has considerably transformed the way the global alternatives industry operates.

The Luxembourg legislator and its supervisory authority (*Commission de Surveillance et du Secteur Financier* or CSSF) has developed extensive expertise in alternative investment funds (AIFs) and alternative strategies, in a strong competitive position, contributing to strengthening its role as a global platform for alternative investments whose regulatory quality is internationally recognized.

The Directive aims to create a harmonised and stringent regulatory and supervisory framework for the activities of all alternative investment fund managers (AIFMs) within the European Union (EU). For the first time, AIFMs were allowed to benefit from a "passport" to provide management services to AIFs in order to market them to professional investors in the EU on the basis of one single authorisation.

This brochure intends to provide an overview of the AIFs available for fund managers in Luxembourg, without addressing all level and tax aspects in detail.



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# UNREGULATED FUNDS

## Overview

Unregulated investment vehicles are mainly governed by the law of 10 August 1915 on commercial companies (the Company Law). Various types of vehicles are available, with the limited partnership regimes being the most popular.

An unregulated vehicle qualifies as an AIF if its activities fall within the scope of the AIFM Law and if no exemption is available.

Unregulated vehicles are useful for private equity, venture capital, infrastructure and real estate investment structuring, as well as for a holding and financing activity.

## Key Features

### Legal form

An unregulated fund is typically organised in the form of a special or common limited partnership (SCS or SCSp). It can be open or closed-ended but cannot be set-up as an umbrella fund.

### Capital

No minimum capital requirement for SCS and SCSp.

### Supervision

An unregulated fund is not subject to the approval of the CSSF.

### Investment restrictions

An unregulated fund may invest in any asset class and any investment policy or strategy.

## Marketing

AIFMs may market an unregulated company to investors within the EU through a regulator-to-regulator notification regime, if the unregulated fund qualifies as an AIF.

## Key Restrictions

### AIFM

Unregulated funds qualifying as AIFs and not benefitting from an exemption contained in the AIFM Law must appoint an AIFM.

### Eligible investors

There are no restrictions in relation to the eligible investors.

## Taxation

Tax treatment depending on the legal form of the vehicle.

# RAIF

## Overview

The reserved alternative investment fund (RAIF) was introduced by the law of 23 July 2016 (the RAIF Law). The RAIF regime was introduced to allow fund sponsors to structure a type of alternative investment fund that combines the legal and tax features of the well-known SIF and SICAR regimes but one that remains unregulated.

The RAIF regime aims to minimize the planning uncertainty that may arise during fund launches, by eliminating the need for prior authorization and the ongoing direct prudential oversight by the CSSF.

## Key Features

### Legal form

The RAIF may be constituted as an FCP or as a SICAV or SICAF.

RAIFs can be open or closed-ended and may be set up as a stand-alone fund or as an umbrella structure consisting of multiple sub-funds or compartments.

### Capital

The RAIF's net assets must reach EUR 1.25 million within 12 months following its launch.

### Supervision

The RAIF is not subject to approval by the CSSF. Instead, it must be managed by an authorised external AIFM, the CSSF is informed about the RAIF's activities via its manager.

### Investment restrictions

The RAIF may invest in any asset class and any investment policy or strategy, except when opting for the SICAR's tax regime, in which case it is restricted to investing in risk capital.

### Disclosure requirements

A RAIF must prepare a prospectus, a PRIIP Key Information Document (KID) if open to retail-type investors and an annual report. There is no obligation to prepare a semi-annual report.

### Specific aspects: EuVECA and EuSEF

RAIFs that qualify as EuVECA or EuSEF funds have the option of being subject to the EuVECA and EuSEF regulation, respectively.

## Key Restrictions

### AIFM

RAIFs are required to appoint an authorised external AIFM. The AIFM can be established in Luxembourg, in another EU Member State or in a third country.

### Risk diversification

RAIFs are subject to mandatory risk spreading, meaning that:

1. A RAIF may not invest more than 30% of its assets or commitments in securities of the same kind issued by the same issuer.
2. Short sales may not result in a RAIF holding a short position in securities of the same kind issued by the same body, which represents more than 30% of the assets.
3. Where financial derivative instruments are invested in, a RAIF must ensure a comparable spread of risk by an appropriate diversification of the underlying assets. With the same objective, the counterparty risk in an OTC transaction must be limited depending on the quality and the qualification of the counterparty.

The risk diversification rules do, however, not apply to any RAIF that has opted for the SICAR's tax regime and is therefore restricted to investing in risk capital.

### Eligible investors

RAIFs are limited to "well-informed" investors that are able to adequately assess the risks associated with an investment in such a vehicle.

## Marketing

RAIFs can be marketed to professional investors within the EU through a regulator-to-regulator notification regime.

### Specific aspects: EuVECA and EuSEF

Both regimes provide a passport that permits the marketing of the fund to EU-based eligible investors.

## Taxation

RAIFs are limited to "well-informed" investors that are able to adequately assess the risks associated with an investment in such a vehicle.

# SIF

## Overview

The exclusive object of Luxembourg specialised investment funds (SIF) governed by the Luxembourg law of 13 February 2007 (the SIF Law) is the collective investment in assets to facilitate the spreading of investment risks and to provide investors with the benefit resulting from the management of their assets. The concept of "management" refers to an activity comprising at least the service of portfolio management. This aims at expressly excluding from the SIF definition passive investment vehicles, the activity of which is limited to holding participations.

## Key Features

### Legal form

The SIF may be constituted as contractual-type mutual funds (FCP) or as investment companies with variable capital (SICAV) or fixed capital (SICAF).

SIFs can be open or closed-ended and may be set up as a stand-alone fund or as an umbrella structure consisting of multiple sub-funds or compartments.

### Capital

The SIF's net assets must reach EUR 1.25 million within 12 months following the CSSF's approval.

### Investment restrictions

Other than the risk diversification requirement, the SIF Law does not impose particular investment restrictions or borrowing limits, which allows for significant flexibility with regard to the assets in which SIFs may invest.

### Disclosure requirements

A SIF must prepare a prospectus, a PRIIP Key Information Document (KID) if open to retail-type investors and an annual report. There is no obligation to prepare a semi-annual report.

### Specific aspects: EuVECA and EuSEF

SIFs that qualify as EuVECA or EuSEF funds have the option of being subject to the EuVECA and EuSEF regulation, respectively.

## Marketing

SIFs qualifying as AIFs and managed by an authorised EU AIFM benefit from a passport allowing AIFMs to market the SIF's shares or partnership interests to professional investors within the EU through a regulator-to-regulator notification regime.

### Specific aspects: EuVECA and EuSEF

Both regimes provide a passport that permits the marketing of the fund to EU-based eligible investors.

## Key Restrictions

### Supervision

Prior to commencing its activities, the SIF must be authorised by the CSSF. Mandatory ongoing supervision comes at the price of a small annual fee.

### AIFM

SIFs that qualify as AIFs and do not benefit from an exemption contained in the AIFM Law are required to appoint an AIFM.

### Risk diversification

SIFs are subject to mandatory risk spreading, meaning that:

1. A SIF may not invest more than 30% of its assets or commitments in securities of the same kind issued by the same issuer.
2. Short sales may not result in a SIF holding a short position in securities of the same kind issued by the same body, which represents more than 30% of the assets.
3. Where financial derivative instruments are invested, a SIF must ensure a comparable spread of risk by an appropriate diversification of the underlying assets. With the same objective, the counterparty risk in an OTC transaction must be limited depending on the quality and the qualification of the counterparty

### Eligible investors

SIFs are limited to "well-informed" investors that are able to adequately assess the risks associated with an investment in such a vehicle.

## Taxation

SIFs have a tax-exempt status and only limited entitlement to double tax treaties, if established as an investment company.

# SICAR

## Overview

The Luxembourg investment company in risk capital (SICAR) was specifically designed for investments in private equity and venture capital. The regime is to promote raising funds from investors that accept the increased risks associated with investments in risk capital (i.e. lower liquidity, higher price volatility and lower credit quality) in expectation of a better return.

The SICAR is governed by the law of 15 June 2004 (SICAR Law) and is divided into two parts: (i) general provisions applicable to all SICARs and (ii) specific provisions applicable to SICARs qualifying as AIFs and which must therefore be managed by an AIFM.

## Key Features

### Legal form

A SICAR must always be constituted as corporate entity with fixed or variable share capital. The SICAR may be set up as a stand-alone fund or as an umbrella structure with multiple compartments.

### Capital

The share capital (including share premiums, if any) must reach EUR 1 million within 12 months following the CSSF's approval.

### Investment restrictions

Other than the requirement to invest in risk capital only, the SICAR Law does not contain investment rules or restrictions and does not impose borrowing limits. Furthermore, a SICAR is not required to comply with the principle of risk diversification.

### Disclosure requirements

A SICAR must prepare a prospectus, a PRIIP Key Information Document (KID) if open to retail-type investors and an annual report. There is no obligation to prepare a semi-annual report.

Specific aspects: EuVECA and EuSEF

SICARs that qualify as European Venture Capital (EuVECA) or European Social Entrepreneurship Funds (EuSEF) have the option of being subject to the EuVECA and EuSEF regulation, respectively.

## Marketing

SICARs qualifying as AIFs and managed by an authorised EU AIFM benefit from a passport allowing AIFMs to market the SICAR's shares or partnership interests to professional investors within the EU through a regulator-to-regulator notification regime.

### Specific aspects: EuVECA and EuSEF

Both regimes provide a passport that permits the marketing of the fund to EU-based eligible investors.

## Key Restrictions

### Supervision

Prior to commencing its activities, the SICAR must be authorised by the CSSF. Mandatory ongoing supervision comes at the price of a small annual fee.

### AIFM

SICARs that qualify as AIFs and do not benefit from an exemption contained in the AIFM Law are required to appoint an AIFM.

### Eligible assets

SICARs must invest in risk capital.

The notion of risk capital is characterised by the following elements:

- a high risk associated with the relevant assets;
- an intention to develop target entities; and
- an exit strategy.

SICARs may also marginally hold financial derivative instruments on an exceptional basis.

### Eligible Investors

SICARs are limited to "well-informed" investors that are able to adequately assess the risks associated with an investment in such a vehicle.

## Taxation

SICARs are fully taxable entities if established as a company but exempt of income tax and capital gains tax derived from risk capital securities and are entitled to double tax treaty benefits.

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# WHY CLIFFORD CHANCE?

Our Luxembourg team offers a full legal, regulatory and tax service based on specialist knowledge of the local and international dynamics of this unique location.

Our 45+ investment fund specialists excel in cross-border fund structuring and work seamlessly across jurisdictions and continents. They work on a daily basis with clients and colleagues in all major financial centres of the world, giving our investment funds practice an unrivalled geographical footprint.

Fund managers benefit from our corporate, regulatory and tax expertise needed throughout the fund lifecycle, including fund structuring, establishment, marketing and capital raising, as well as on ongoing operational issues, fund financing and restructuring mandates.

We also advise retail and institutional investors on the full range of Luxembourg funds investing in all asset classes. Our knowledge of local markets means we can tailor transactions effectively from both a tax and marketing position.

Clifford Chance is often involved in regulatory discussions concerning Luxembourg investment funds with the CSSF and maintains a strong professional relationship with regulatory authorities.

**“Enjoys an outstanding track record advising UCITS, SICARs and Specialised Investment Funds.”**

Chambers Europe 2019 : Investment Funds Luxembourg

**“One of the firm’s advantages is the assistance from its network, which is very helpful when there are international matters.”**

Chambers Europe 2019 : Investment Funds Luxembourg

1 BAND

**“Investment Funds Luxembourg”**

Chambers Europe & Global 2020

**“Tier 1: Investment Funds Luxembourg”**

Legal 500 Emea 2019

**“Band 1: Investment Funds Luxembourg”**

IFLR 1000 2019

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# LUXEMBOURG AIF COMPARISON TABLE

| | Regulated Investment Vehicles | | Unregulated Investment Vehicles | |
|---|---|---|---|---|
| | **SIF** | **SICAR** | **RAIF** | **Unregulated Fund** |
| **Applicable Legislation** | SIF Law | SICAR Law | RAIF Law | Company Law |
| **CSSF Prior Authorisation and Supervision** | Yes | Yes | No | No |
| **Full Scope AIFMD Vehicle** | Yes, unless specific exemption under AIFMD | Yes, unless specific exemption under AIFMD | Yes | Yes, unless specific exemption under AIFMD |
| **Eligible Investors** | Well-informed investors only, i.e. institutional investors, professional investors as well as any other sophisticated retail or private investor that:<br>a) has declared in writing his status as a well-informed investor; and<br>b) invests a minimum of 125,000€ in the SIF/SICAR/RAIF; or<br>– has obtained an assessment from a credit institution, a MiFID investment firm or a UCITS management company certifying his expertise, his experience and his knowledge in appraising in an appropriate manner an investment in a SIF/SICAR/RAIF | | | Unrestricted |
| **Eligible Assets** | Unrestricted, but prior approval of investment objective and strategy by CSSF | Risk capital only and prior approval of investment objective and strategy by CSSF | Unrestricted, unless for RAIFs opting for special tax regime (investment in risk capital only like SICAR) | Unrestricted |
| **Risk Diversification** | 30% investment limit of its net assets in securities of the same type issued by the same issuer | Not required | Same risk diversification rules as SIFs, unless for RAIFs opting for special tax regime (no risk diversification like SICAR) | Not required |
| **Legal Form** | FCP<br>SICAV/SICAF (SA, SCA, Sàrl, SCSA, SCS, SCSp) | SA, SCA, Sàrl, SCSA, SCS, SCSp (fixed or variable capital) | FCP (unless for RAIFs opting for special tax regime)<br>SICAV/SICAF (SA, SCA, Sàrl, SCSA, SCS, SCSp) | Most commonly SCS and SCSp but other legal forms are available |

# LUXEMBOURG AIF COMPARISON TABLE (CONTINUED)

| | Regulated Investment Vehicles | | Unregulated Investment Vehicles | |
|---|---|---|---|---|
| | **SIF** | **SICAR** | **RAIF** | **Unregulated Fund** |
| **Open or Closed-Ended** | Open or closed-ended | | | |
| **Multiple Sub-Funds** | Yes | Yes | Yes | No |
| **Cross Sub-Fund Investments** | Yes | No | Yes | N/A |
| **Multiple Share Classes** | Yes | | | |
| **Minimum Capital Requirements** | EUR 1,250,000to be reached within 12 months from CSSF authorisation | EUR 1,000,000to be reached within 12 months from CSSF authorisation | EUR 1,250,000to be reached within 12 months from launch | No minimum capital requirement for SCS and SCSp |
| **Required Service Providers** | Luxembourg management company in case of FCP | N/A | Luxembourg management company in case of FCP | N/A |
| | Depositary (Luxembourg credit institution or Luxembourg branch of EU credit institution, Luxembourg MiFID investment firm or Luxembourg branch of a EU MiFID investment firm (subject to specific requirements) or Luxembourg professional depositary of assets other than financial instruments if the SIF/SICAR/RAIF (i) is closed-ended for a period of 5 years from the date of its initial investments and (ii) does generally not invest in assets to be held in custody or generally seeks to acquire the control over the issuers or non-listed companies) | | | Depositary (being one of the entities also eligible to act as depositary of SIF/ SICAR/RAIF) if qualifying as AIF |
| | Central administration in Luxembourg | | | No central administration required |
| | Luxembourg approved statutory auditor (réviseur d'entreprise agréé) | | | Luxembourg approved statutory auditor if qualifying as AIF |
| **EU Marketing Passport** | If Full Scope AIF: AIFMD passport for marketing to professional investors in the EU | | | |

| | Regulated Investment Vehicles | | Unregulated Investment Vehicles | |
|---|---|---|---|---|
| | **SIF** | **SICAR** | **RAIF** | **Unregulated Fund** |
| **Taxation** | No income tax | Subject to income tax except if incorporated as SCS/SCSp (tax transparent), but income from securities held by the SICAR are exempt | Same tax regime as SIF, unless for RAIFs opting for special tax regime that are subject to SICAR tax regime | Tax treatment depending on the legal form of the company |
| | No wealth tax | No wealth tax | | |
| | Subscription tax at a rate of 0.01% of the NAV, but SIFs investing in other funds already subject to the subscription tax, money market SIFs, SIFs set up as a pension pool vehicle for a group and microfinance SIFs are exempted under certain conditions | No subscription tax | | |
| | No withholding tax on dividends/capital gains | | | |
| | VAT exemption on management services | | | |

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Clifford Chance, société en commandite simple admitted to the Luxembourg Bar.

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