European Fund Structures

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Simmons & Simmons Bloomberg

Introduction

- **Why use an “onshore” structure?**
- **UCITS**
- **Irish QIAIF**
- **Luxembourg RAIF**
- **Impact of Brexit**

Why use an “onshore” structure?

- Investor preference
- Passporting/access to capital
- Tax treaty network
- Populism / press / PR
- Main options: Ireland and Luxembourg

UCITS

UCITS: What is a UCITS and why set it up?

- A harmonised European regulated fund product
- Can be “passported” on a cross-border basis within the EEA
- Designed to be capable of retail sale; diversification of investor base
- Strong focus on investor protection – liquidity, transparency, security
- Robust governance and risk framework
- Has evolved into “gold” standard regulated fund
- Alternative strategies accommodated
- Recognised for sale by regulators in Asia, South America, Middle East, South Africa

UCITS: Principal requirements

- Sole object must be collective investment in transferable securities or in other liquid financial assets of capital raised from the public
- Must operate on the principle of risk spreading
- Must be open-ended
- Must be authorised by home regulator
- May invest only in eligible assets, with restrictions on spread, leverage and exposure
- Assets must be entrusted to an independent depositary

UCITS: Alternative strategies

- Product opportunities continue to evolve
- Many hedge strategies can be replicated using the right mix of derivatives, leverage and hedging
- Likely to be adjustments required to accommodate liquidity, eligible asset, diversification, leverage and counterparty limits and requirements
- Physical shorting not permitted but can gain short exposure through use of derivatives
- Financial indices can be used

UCITS: Common UCITS strategies

- Equity long/short
- Market neutral
- Convertible bond arbitrage
- Emerging markets
- Global macro
- Managed futures
- Event driven
- Fund of funds

Irish Fund Structures

Regulatory Category	UCITS	QIAIFs
Legal Structures	ICAV VCC Unit Trust CCF	ICAV VCC Unit Trust CCF ILP
Main Characteristics	Suitable for retail sale Must be open ended No minimum investment Eligible asset requirements Strict investment restrictions No borrowing UCITS Passport	Only for Qualifying Investors Can be closed ended Minimum investment of €100,000 No eligible asset requirements Very few investment restrictions No risk spreading requirements Unlimited borrowing/leverage AIFMD passport

Irish ICAV QIAIF

Irish ICAV QIAIF: Irish alternative fund structure

- **ICAV – Irish Collective Asset-management Vehicle – ie the fund <u>structure</u>**
- **Advantages**
  - corporate vehicle operating outside of Companies Acts
  - not registered with Companies Registration Office
  - can dispense with AGM
  - no shareholder approval required for amendments to IoI
  - no risk diversification requirement
  - can produce audited accounts on a per sub-fund basis
  - can elect to “check-the-box” for US tax purposes

Irish ICAV QIAIF: Irish alternative fund structure

- **QIAIF – Qualifying Investor Alternative Investment Fund – ie the <u>regulatory status</u> of the fund**
- **Advantages**
  - Ireland's flagship AIF
  - designed for sophisticated investors
  - flexible investment strategies – hedge, PE, RE, feeder, FoF, loan origination
  - can be single asset
  - no borrowing/leverage restrictions
  - speed to market – 24-hour approval by the Central Bank
  - can avail of AIFMD passport

Irish Funds: Conclusion

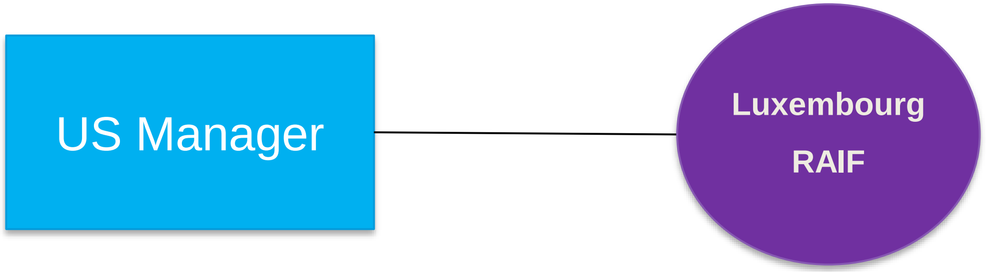
- **Onshore, regulated, EU & OECD member state**
- **Focus on investor protection**
- **Access to EU market through UCITS & AIFMD passports**
- **No Irish tax at fund level or on non-Irish resident investors, if no Irish assets**
- **QIAIF speed to market**
- **Re-domiciliations accommodated**
- **45 administrators, 18 depositaries**

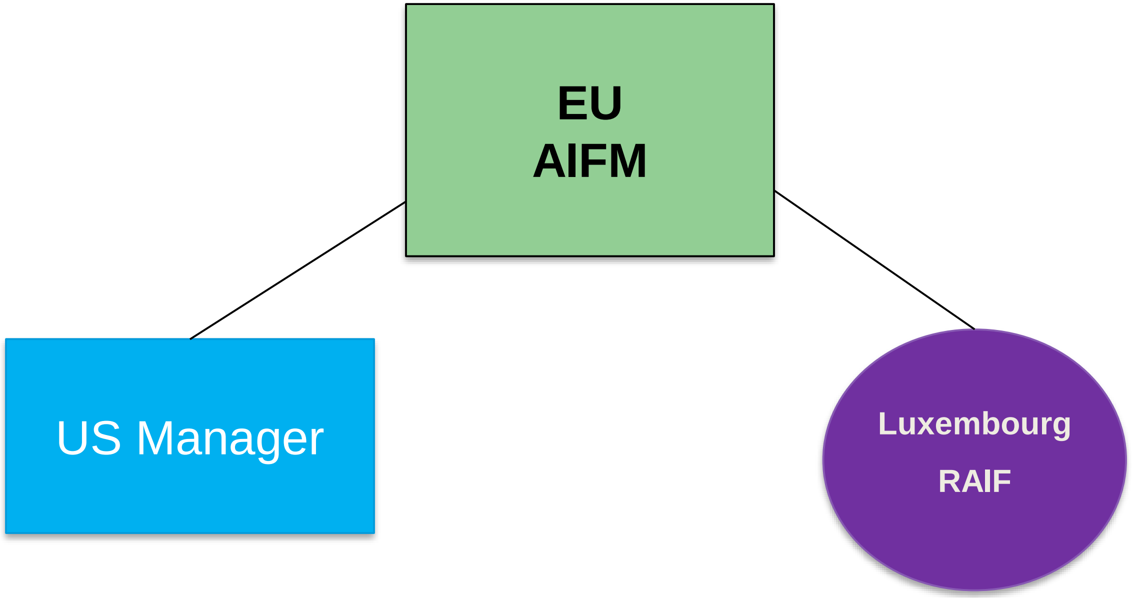
Luxembourg RAIF

Luxembourg RAIF: Key features

- Previous "onshore" Luxembourg hedge fund structure (Luxembourg SIF) required CSSF approval/regulation
- New Luxembourg RAIF is <u>not</u> regulated by CSSF
- RAIF must appoint a European alternative investment fund manager ("<u>AIFM</u>")
- RAIF therefore under "indirect" supervision by CSSF
- What does this mean for US managers wanting to set up a RAIF?

Luxembourg RAIF: How can a US firm manage such a fund?





Either: (1) US Manager sets up its own EU entity; or
(2) US Manager uses third party EU AIFM "manco"

Not allowed

Allowed

Luxembourg RAIF: Key features

Who can invest in a RAIF?

RAIFs only available to "well-informed" investors

- Institutional investors
- Professional investors
- Investors who
  - have declared in writing that they adhere to the status of a "well informed"; and either
  - have invested at least EUR125,000 into the fund; or
  - assessed by an EU credit institution or a UCITS management company as being "sufficiently expert"

What investment restrictions are there for a RAIF?

- RAIFs following an open-ended strategy are subject to risk spreading requirements possible (generally <30% in any one asset)
- RAIF is allowed a "ramp up" period to achieve risk spreading (up to 1 year for open-ended structure)

Luxembourg RAIF: Key features

Structure and documentation

- Master-feeder possible – choose the correct master fund structure to “check the box”
- Offering memorandum; constitutional documentation; subscription forms
- Offering memorandum required for Luxembourg master fund

Service Providers

- AIFM – RAIF must appoint an EU AIFM (but this can be a non-Lux AIFM)
- Depositary – RAIF must have a “full” Luxembourg depositary
- Auditor – Usually a Luxembourg auditor
- Administrator – Luxembourg administrator required
- Fund directors – No residency requirements (unlike Ireland)

Luxembourg RAIF: The story so far…

- **To date, the investors that have shown interest in the RAIF are**
  - Institutional clients
  - Pension funds
  - Insurance companies
  - HNWIs
  - Family offices

  …except those that need a regulated vehicle (for whom a Luxembourg SIF might be more appropriate)

- **Over 500 umbrella RAIFs launched since 2015**

European alternative funds compared with a Cayman fund

	RAIF	QIAIF/ ICAV	Cayman
Investment restrictions?	General risk spreading requirement	Limited regulatory restrictions	None
EU AIFM required?	Yes	Yes	No
Authorised / regulated product?	No	Yes – CBI authorised	Yes - CIMA regulated
Master-feeder possible?	Yes	Yes	Yes
Master fund prospectus required?	Yes	Yes	No
Local directors required?	No	Yes	No
Access to AIFMD marketing passport?	Yes	Yes	Not at present
Access to AIFMD NPPRs?	N/A	Only if non-EU AIFM	Yes
Umbrella structure possible?	Yes	Yes	Yes
Management passport?	Must have EU AIFM but can be non-Lux ie AIFM with EU passport	Only if EU AIFM	No

European funds: Impact of Brexit

- **For a US manager with no European presence, little impact**
- **Until EU-UK financial services deal is agreed, UK not a suitable EU fund “manco” location and US managers setting up a new EU fund should:**
  - establish a management entity in EU 27; or
  - set up an arrangement with a third party UCITS or AIFM “manco” (most likely in Ireland or Luxembourg)
- **US managers with an existing UK management entity and EU funds may need to reconfigure existing arrangements**
- **Delegation from EU27 manco to UK management entity likely to be permitted (even if only on a bilateral basis)**

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