

Asset Management: Luxembourg, your location of choice

*Seizing opportunities
in Luxembourg*



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Challenges and issues



Didier Prime
Luxembourg Asset
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Harmonising the retail fund world to create a level-playing field between EU countries and to better protect their investors is a constant effort... The UCITS framework was created over 25 years ago with the objective of creating a single market for investment funds across the EU.

Back in 1985, when the first UCITS directive was introduced, the European fund management industry was still considered infancy.

In 2001, the UCITS directive was amended by two directives (together the “UCITS III Directives”). Together, they aimed to provide new operating conditions for management companies and to introduce simplified fund prospectuses (i.e. the management company directive) as well as a wider range of investment powers (i.e. the product directive).

Even if UCITS III had a profound impact on the fund landscape in Europe, this initiative was however felt as falling short on certain key expectations of the industry: reduce administrative burden, increase market efficiency, but not at the expense of investor protection. On 13 July 2009, the EU adopted a new directive¹, commonly known as UCITS IV, to fix the

identified shortfalls. The UCITS IV world is the one we will be living in for a little while... but the ink will not yet be dry on all national transposition laws that they will need to be adapted again. UCITS V, a European initiative addressing the issue of EU depositaries following the Madoff scandal and more generally the financial crisis, is already expected for 2012.

UCITS VI is probably not far down the line, if the pace of changing the UCITS legislation, between 1985 and today, keeps on growing!²

No one knows yet if the non-retail fund world will follow the same route. The Alternative Investment Fund Manager Directive (“AIFMD”), adopted in its final form on 27 May 2011, is a major piece of legislation with overwhelming effects on the alternative fund world. Also a response to the financial crisis, and a result of many political compromises, it is yet unclear whether it will reach the goals that were set initially (i.e. the avoidance of systemic risks) or whether it will require another quick “lifting” once in place.

There have never been times like the current ones, where so many uncertainties linger around a business that needs stability to be trustworthy.

The asset management world is, indeed, in the middle of a regulatory storm. The production and selling of products “the old way” are constantly being challenged. Investor protection is one of the cornerstones of the current MiFID³ review by the EU Commission and the heart of its initiative on PRIps, two developments that will give rise again to new regulation and impose a serious rethinking of current models.

It is a time of change and challenges, of balancing the needs for better and fairer regulation and those of doing business in an efficient manner.

It is a complex time, for institutions and for service providers, for supervisory authorities and for investors.



Didier Prime
Luxembourg Asset Management Leader

¹ Directive 2009/65/EC of the European Parliament and of the Council of 13 July 2009, on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS). This directive has been complemented by two “Level 2” directives (Commission Directive 2010/43/EU of 1 July 2010 implementing Directive 2009/65/EC of the EP and of the Council as regards organisational requirements, conflicts of interest, conduct of business rules, risk management and content of the agreement between a depositary and a management company; as well as Commission Directive 2010/42/EU of 1 July 2010 implementing Directive 2009/65/EC of the EP and of the Council as regards certain provisions concerning fund mergers, master feeder structures and notification procedure) and one EU Regulation (N. 583/2010 implementing Directive 2009/65/EC of the EP and of the Council as regards key investor information and conditions to be met when providing key investor information or the prospectus in a durable medium other than paper or by means of a website), all of 1 July 2010.

² 16 years between the original 1985 UCITS directive and that of 2001, 8 years between 2001 and 2009, 3 years between 2009 and 2012, expected date for UCITS V...

³ “MiFID” stands for Markets in Financial Instruments Directive, a directive applied since November 2007, the main objective of which is to create a single market for investment services and activities and to ensure a high degree of protection for investors in financial instruments.

Where does Luxembourg stand?

End of 2010, Luxembourg had over EUR 2,199 trillion in net assets in over 12,900 sub-funds (3,667 legal entities), easily placing Luxembourg as the second largest fund centre after the United States.

Luxembourg's position as a key domicile for internationally distributed funds began in 1988 when the first UCITS Directive was implemented into local law. Since this date, Luxembourg has enjoyed significant and consistent growth in both assets and fund numbers with a notable surge since the turn of the century reflecting the increasing attractiveness of Luxembourg as a hub for global fund products in both mainstream and alternative asset classes.

Historically, Luxembourg's success has been fuelled by its ability to offer an attractive platform for firstly European and more recently globally distributed retail funds. In addition to the importance of the mainstream, Luxembourg is a major centre for each of the primary alternative asset classes. Real Estate funds have been a particular success story with Luxembourg now recognised within this market segment as the leading domicile for structured real estate products targeting international investment and distribution. Private Equity funds are emerging as the third significant alternative asset class with Luxembourg building on its dominance as a location for structuring transactions to become a leading centre for establishing the fund-level vehicles themselves. Finally, Luxembourg's long-standing focus on Hedge funds and fund of Hedge funds products has enjoyed rapid growth in recent years as a result of regulatory and market developments. The consequences of the financial crisis have obviously been felt in Luxembourg: domestic Hedge funds and fund of Hedge funds have greatly suffered from the liquidity crisis, with a drop of assets between end of 2007 and early 2009. However, promoters have continued to create products (over 1886 (sub) funds up and running mid-2010, representing over 141 bio EUR in assets) and the trend remains a very positive one.

The reasons for this success story are intimately linked to Luxembourg's recent history, to its geographic location and to the support the government has consistently provided over the years to the fund industry.

A founding member of the EU, located in the heart of Europe and with geographical borders to Germany, France and Belgium, the Grand Duchy of Luxembourg can count on a multicultural and multilingual workforce, with the commuters from neighbouring countries and the high number of other European nationals living in the country (Italian, Spanish, Portuguese, British). Grand Duchy employers, including the significant financial sector, can tap into a readily available population of 5 Mio qualified workers and service employees.

This international nature of Luxembourg, a country with three official languages (Luxembourgish, French and German), as well as English in the financial sector, is one reason why international promoters choose Luxembourg as their centre for international fund business.

Being a small country in size and having had to rethink its traditional steel-based economy to make it a centre for international banks and funds, the Luxembourg government has always had an open and friendly ear for the financial community. The authorities, and particularly the financial regulator (Commission de Surveillance du Secteur Financier "CSSF"), are accessible and flexible; officials are welcoming, easy to contact and open to dialogue.

This close working relationship between government and the business community will allow Luxembourg to continue to strengthen its position as the most attractive international fund centre.

The fund industry also has its representative body, the ALFI (Association Luxembourgeoise des Fonds d'Investissement), created in 1988 to promote the industry's development. ALFI plays a proactive role in leading industry efforts to maintain Luxembourg as the most attractive centre for establishing investment funds and as the predominant gateway to the European and global fund markets.

As an active member of EFAMA (European Fund and Asset Management Association), the European trade association for investment funds, the ALFI participates to all discussions at EU level on the future of the industry in Europe and beyond. As an organiser of "road shows" throughout the world, ALFI raises the awareness of foreign promoters, distributors and regulators alike to the opportunities offered by Luxembourg.

Last but not least, the development of the Grand Duchy as a centre of financial and fund services has led to an exceptional concentration of highly specialised service providers, in custody, fund administration and transfer agency, business and tax consultants, audit firms, international and local law firms, providers of fund data to the global media, etc.

Luxembourg's success has been and continues to be predicated on a combination of the depth and breath of the supporting infrastructure – service providers and professionals, systems and technology geared toward supporting the diverse and complex vehicles we see in the funds world today – in addition to a stable and business friendly regulatory and tax environment which effectively supports international fund providers.

However, Luxembourg does not live in isolation – and the great regulatory overhaul mentioned before hits it hard. Other fund domiciles see the coming changes as a unique occasion to get their share of the "asset pie". And yes, there is a strong domestic servicing industry in Luxembourg that stands much to lose from the flexibilities of UCITS IV!

At PwC Luxembourg, we are confident that the expertise of the fund community in Luxembourg, together with the business minded environment and the long standing tradition of being a safe fund centre will allow the Grand Duchy to weather the regulatory storm as it did, mostly, with the financial crisis. We are pleased to provide this summary of the Luxembourg business and regulatory environment for your information and stand ready to provide support whatever your needs may be.



Regulation and supervision of funds

Funds for all types of investors

In line with its reputation as a major fund centre, Luxembourg has created a legislation allowing the offering of regulated fund products to all types of investors.

The retail regime

Since its inception as a fund centre, in the early 1970's, Luxembourg has turned out to be a platform for funds meant for the "public", this latter term including virtually all conceivable types of investors. This strong tradition is enshrined in its primary fund legislation, the law of 22 December 2002 on undertakings for collective investment (the "2002 Law"), soon to be fully replaced by an entirely new set of legislation implementing the UCITS IV Directive of 2009 and modernising certain aspects of the 2002 Law: the law of 17 December 2010 on undertakings for collective investment (the "Fund Law") and two CSSF Regulations of the same date⁴. While the 2002 Law remains into force until 1 July 2012 to allow for certain aspects of the transition of existing fund structures, new structures will be ruled, at the latest as from 1 July 2011, by the Fund Law.

The rules described in this guide are based on the Fund Law.

This essential piece of legislation remains, true to the original Luxembourg UCITS law of 1988, divided in several "parts".

The first part of the Fund Law regulates funds which are UCITS compliant, that is that they are open-ended and comply with the requirements set by the EU legislator in terms of asset eligibility, risk spreading requirements, prohibition of leveraging and short selling, existence of a strong risk management process, all under the control and responsibility of a highly regulated and supervised management company, in Luxembourg or elsewhere in the EU. These UCITS funds, sold to the public and to institutions all over Europe and in many jurisdictions beyond, are still known in Luxembourg as "Part I Funds".

A second part of the Fund Law deals with those funds (known as "Part II funds") which are excluded from the UCITS regime for reasons which are diverse. Usually, this means that either their investment policy or their risk spreading is not compliant with that foreseen by UCITS; or they use leverage to an extent not permitted by UCITS rules; or they do not actively market their shares to the public in the EU; or finally they are not opened for redemptions as often as the UCITS regime would require.

The well-informed investor regime

Next to the retail regime of the Fund Law exists a fund regime tailored to fit the need of institutional investors. Created by the law of 13 February 2007 on Specialised Investment Funds ("SIF"), this regime ("the SIF Law") allows a rapid time-to-market of funds investing into all types of existing assets, with flexible restrictions in terms of risk diversification.

Because of these features, SIFs are by law reserved to "well-informed investors", i.e. either institutional, large corporate or other investors (including individuals) who are ready to testify that they adhere to the status of well-informed investors and who invest a minimum of EUR 125,000 in the SIF or, alternatively, obtain an assessment from a regulated entity certifying their experience and knowledge in assessing the risk of their investment.

In line with its reputation as a major fund centre, Luxembourg has created a legislation allowing the offering of regulated fund products to all types of investors.

⁴ CSSF Regulation N. 10-4 transposing Commission Directive 2010/43/UE of 1 July 2010 implementing Directive 2009/65/EC of the European Parliament and of the Council as regards organisational requirements, conflicts of interest, conduct of business, risk management and content of the agreement between a depositary and a management company ("Regulation 10-4").
CSSF Regulation N. 10-5 transposing Commission Directive 2010/444/UE of 1 July 2010 implementing Directive 2009/65/EC of the European Parliament and of the Council as regards certain provisions concerning fund mergers, master feeder structures and notification procedure ("Regulation 10-5").

Funds covering the whole investment universe

Luxembourg has not only created fund products targeted to the specific needs of all types of investors, but also a legal and business infrastructure which is able to support almost any investment strategy. While UCITS are, by definition, restricted in terms of asset eligibility to transferable securities, funds, derivatives, cash and money market investment, the other funds, be they Part II funds or SIFs, have an extremely broad (indeed, almost unlimited) scope of eligible assets.

Next to the “traditional alternative” funds that are the Real Estate, Private Equity and Hedge funds, we also observe more specialist mandates like art, infrastructure, containers, wine, woods and agriculture, pollution rights and many others. There is no limitation in terms of asset class and no limitation in terms of geography – the only limit being the possibility to value the investment and to have it safeguarded by a Luxembourg depositary.

Private Equity and venture capital funds

Specific to this asset class, Luxembourg has introduced legislation designed to meet the needs of the Private Equity and venture capital community. This law of 15 June 2004 relating to an investment company in risk capital (“SICAR”) creates a very favourable regulatory and tax regime for vehicles which technically are not investment funds, but resemble their functioning closely. The SICARs, which are also exclusively reserved for well-informed investors, are, next to the SIFs, the prime vehicles for investing into Private Equity and venture capital.

Legal structures

Luxembourg investment funds, whether subject to the Fund Law or the SIF Law, are either created under a contractual or a corporate form (including the form of a partnership).

The contractual form: the Fonds Commun de Placement (“FCP”)

The FCP, which closely resembles the German or Swiss “Sondervermögen” and the UK Unit Trust, is an undivided collection of assets, managed by a management company on behalf of joint owners (the “unit holders”). Legally speaking, it is established by a contract between the management company and the depositary bank, which create “management regulations”. Investors, in the form of unit holders, buy units issued by the management company which represent a portion of the FCP managed, and by doing so become a party to the contract. The units acquired represent their right in the undivided collection of assets. Their liability is limited to the amount contributed by them.

This fund structure, which is available for funds under the Fund Law or the SIF Law, always requires a management company, which must, for the time being, be situated in Luxembourg as regards Part II funds and SIF.

The management company may be situated in Luxembourg or in another EU Member State, when it acts for UCITS funds (a “UCITS management company”). Wherever its location, a UCITS management company will have to obey strict conditions imposed by the UCITS directives and fulfil requirements in terms of capital, human, organisational and technical resources.



The corporate form: Investment Company with Variable Capital (“SICAV”)

SICAVs are corporate vehicles whose articles of incorporation provide that the amount of capital is at all times equal to the Net Asset Value (“NAV”) of the vehicle. The capital increases or decreases automatically as a result of subscriptions or redemptions, without any of the formalities generally imposed under company law regarding issuance or reduction of capital. Although called “unit holders” in the Fund Law, SICAV investors are legally-speaking, shareholders and as such have a right to vote in shareholders’ meetings in addition to their economic rights.

A SICAV created as a UCITS fund may either designate a UCITS management company (as for the FCP above) or may be a so-called Self-Managed SICAV, whereby the necessary processes and infrastructure are technically part of the fund itself.

For Part II funds and SIFs, no legal requirement exists for appointing a management company although other reasons (e.g. fiscal, governance structure, etc.) may make use of such a management company valuable.

SICAVs may take different legal forms, depending on the law to which they are subject. The Fund Law limits SICAVs to being public limited companies (S.A.) while the SIF Law allows them to also take the form of e.g. limited partnerships (S.C.A.) or private limited companies (S.à.r.l.). This flexibility in the choice of legal form has many advantages, from a tax and corporate law point of view.

Finally, in addition to the SICAV, a fund may also be structured as a SICAF, being a corporate vehicle with fixed capital. Available for all types of funds, its limited flexibility means it is rarely used.

Main actors in the fund world

Management companies

All Luxembourg FCPs must, and SICAVs, if they so desire, may, be managed by a management company.

UCITS management companies

One of the major novelties of UCITS IV is the ability for management companies to set up and run funds in another EU State than their own. In order to qualify as an admissible UCITS management company and hence be able to “remotely” manage foreign funds, entities in Luxembourg must fulfil strict conditions, described in Chapter 15 of the Fund Law as well as in CSSF Regulation n.10-4, in terms of activity scope, organisation and functioning.

The activities of UCITS management companies are the “collective portfolio management” (“CPM”) of UCITS funds, this function encompassing asset management, administration and marketing. They may however also manage other types of Luxembourg UCIs, like Part II funds and SIFs. Management companies may also manage individual portfolios on a discretionary basis for private clients or pension funds. If they do so, they can also provide investment advice and perform safekeeping of UCI shares or units. This extended scope of activity will trigger the application of certain organisational and conflicts of interest rules taken from the financial legislation as modified by MiFID. In addition, the capitalisation requirements will change, compared to a management company limiting itself to CPM, if it performs the investment service of individual portfolio management.

Unlike before, where only UCITS management companies with an extended scope of activity had to function in accordance with MiFID standards, current rules impose that the highest standards in terms of organisation and procedures, conflict of interest rules, compliance with rules of conduct and risk management apply to all UCITS management companies.

In order to be authorised in Luxembourg, a UCITS management company must hence show to the CSSF that it is organised and that it functions in line with the Fund Law and Regulation 10-4, namely:

- That it has a capital of EUR 125,000, plus additional own funds if the assets it manages are in excess of EUR 250 Mio. These additional own funds equal 2 bp of the amount of AUM in excess of EUR 250 Mio, with a cap of EUR 10 Mio. Half of these own funds may be provided through a bank or insurance guarantee;
- That it has sufficient technical and human means necessary for the proper performance of its duties. In particular, that at least two individuals (“the managers”), of relevant experience and reputation also in relation to the type of UCITS or UCIs concerned, must be designated to conduct the activities of the management company (“4-eyes principle”);
- That it is audited by an external auditor approved by the CSSF.

The management company must further show:

- That it has sound organisational, administrative, accounting and internal control procedures, sufficient resources and procedures regarding customers' complaints;
- That it has put in place permanent functions like compliance, internal audit and risk management;
- That it complies with the requirements regarding identification and management of conflicts of interest;
- That it respects its rules of conducts, including the duty to act in the best interest of the UCITS and their unit holders, the duty of best execution and the rules regarding payment and receipt of inducements in the context of asset management or administration of the UCITS;
- That it has in place a sound risk management process so that all risks pertaining to the funds managed can be identified, monitored and managed at all times. This risk management process must be duly described in a policy, kept up-to-date and operational at all times;
- That investment compliance monitoring procedures are in place and function at all times.

Further, management companies must take the utmost care in the selection and the supervision of delegates, i.e. the service providers of the fund who contract directly with the management company. Any of the functions delegated to third parties must indeed be properly monitored and supervised, with the possibility for the managers to intervene directly with the delegate and even revoke its mandate.

UCITS IV has not changed the previous rules on delegation of the asset management functions: they can still only be performed by duly regulated and supervised entities, approved for the business of asset management. They can never be performed by the depositary bank, which is also prevented from performing risk management functions for the funds, this tasks being too closely related to asset management.

Management companies can outsource performance of some or all of their functions, so long as they do not become a "letter box entity".

Luxembourg UCITS management companies using their passport

With UCITS IV, the possibility is now open for Luxembourg UCITS management companies to perform their CPM activities cross-border and even to set-up and manage funds located in a different Member State. They may do so either by establishing a branch in that other Member State, or by using what is known as the Freedom to provide Services ("FPS") route, i.e. acting on foreign territory without having a permanent physical presence abroad.

Both routes require a prior authorisation of the CSSF, which will closely liaise with its fellow supervisory authority of the Member State in which the management company will operate and/or create/ manage a UCITS fund.

The procedure for obtaining such authorisation is fairly straightforward: The Luxembourg management company must inform the CSSF of the activities it wants to perform in a given Member State, if relevant, give a description of the branch it intends to establish for performing these activities, describe the procedures in place for investor complaints handling and, last but not least, describe the risk management process put in place. This information is then transmitted (within two months in case of a branch, one month in case of FPS) by the CSSF to the supervisory authority of the relevant State, along with an attestation regarding the management company's scope of authorisation in Luxembourg and an indication as to the restrictions, if any, on the types of UCITS it is allowed to manage in Luxembourg. The foreign regulator has then up to two months from receipt of this information to organise its supervision over the branch and inform the management company of its start of activities. When the FPS route is chosen, the management company can start its activities immediately once the CSSF has transmitted to file to the foreign regulator.

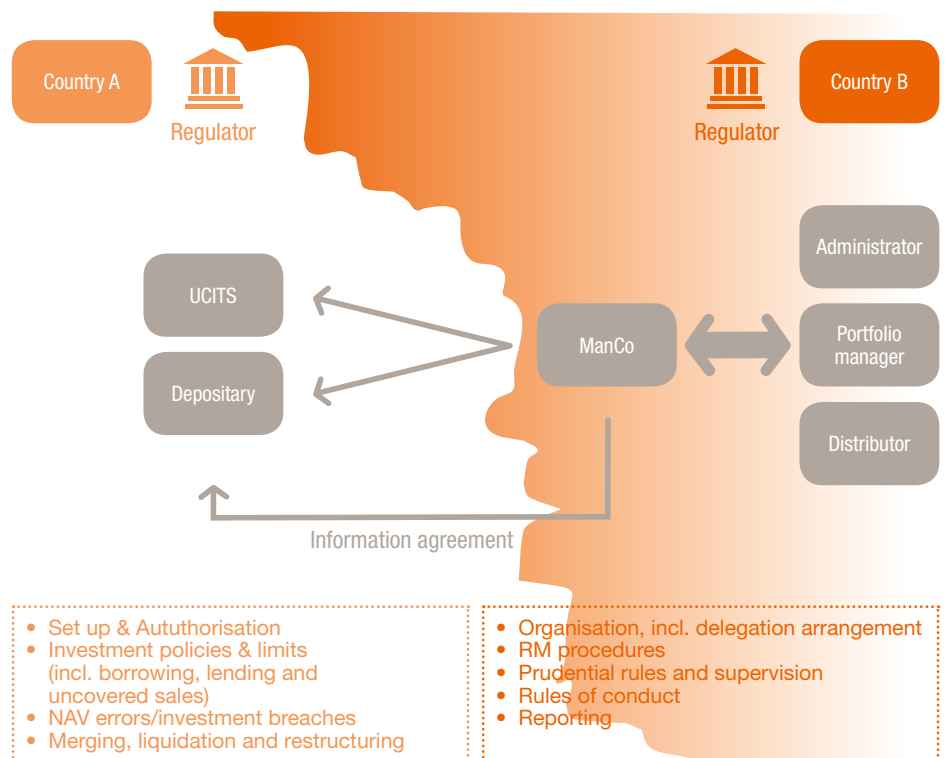
The interaction between the management company's approval to act abroad using its passport and the setting up of a fund abroad is interesting from a legal point of view and raises the question of the rules applicable to the various business fields involved in running a fund.

The Fund Law clearly states that the Luxembourg management company exercising its functions cross-border via a branch or the FPS route must apply Luxembourg law to its organisation, notably the delegation rules, risk management procedures, prudential rules and supervision, rules of conduct and reporting. The CSSF is responsible for supervising the adequacy of the arrangements and organisation of the management company so that the latter is in a position to comply with its obligations and rules relating to the constitution and functioning of all the UCITS it manages.

However, the law of the fund's Member State will rule the creation and functioning of the fund, i.e. its set-up and authorisation, investment policies and limits (incl. borrowing, lending and uncovered sales), NAV errors and investment breaches, merging, liquidation and restructuring. The foreign authority supervises the fund and obtains relevant information from the management company (agreement with the depository, delegation arrangements taken) allowing it to perform its supervision.

The following diagram illustrates this split:

Applicable law and allocation of responsibilities



Various rules are foreseen to make the management company passport, the communication flow between management companies and authorities and between the authorities themselves, function properly. Future will tell if and to what extent management companies will make avail of the pass-porting possibility, notably in view of the potential tax issues⁵ not foreseen nor addressed by the UCITS IV Directive.

The rules applicable to foreign management companies wanting to act in Luxembourg e.g. by establishing or managing a Luxembourg UCITS obviously mirror exactly those described above, in terms of authorisation, applicable law and split of responsibility between regulators (supervision of the management company's activities by the foreign regulator, supervision of the fund by the CSSF).

⁵ For example, that tax authorities of the domicile of the management company want to treat the foreign fund as if it were a domestic one from a tax point of view.

Other management companies of Luxembourg funds (“Non-UCITS or Chapter 16 management companies”)

While the onerous requirements above-listed and the corresponding passport only apply to UCITS management companies, there is a number of management companies in Luxembourg which manage Part II funds or SIFs, generally because these funds are created as FCPs. These management companies, ruled by Chapter 16 of the Fund Law, are also regulated entities in Luxembourg and hence need to be authorised by the CSSF. This authorisation will be given if the management company can show:

- A minimum capital of EUR 125,000 and sufficient financial resources at its disposal to enable it to conduct its business effectively and meet its liabilities;
- An activity limited to the management of UCIs, the administration of its own assets being only ancillary;
- High repute and experience of its conducting persons (i.e. directors);
- There is no specific requirement as to “managers”, like in a UCITS management company, but the CSSF takes under scrutiny the identity of the shareholders of the management company and wants to be fully informed of its organisational structure.

A new feature introduced by the Fund Law for non-UCITS management companies, which confirms recent administrative practice of the CSSF, is the limited freedom in the choice of third parties to which delegate tasks and the requirement of controlling closely such delegation. As for UCITS management companies, any of the functions delegated to third parties must indeed be properly monitored and supervised. Whereas previously a non-UCITS management company was more or less free to pick its investment managers, even if they were not subject of supervision by an authority, this freedom disappears now. Asset management functions can only be performed by entities which are duly authorised in their country for the purposes of asset management and duly supervised by an authority with which the CSSF can cooperate. Finally, the management company may not delegate the core function of asset management to the depositary of the Part II fund or SIF.

By introducing these requirements directly inspired from the UCITS Directive, the Luxembourg legislator has also taken a few steps towards the future introduction of AIFMD. Indeed, management companies of Part II funds and of SIFs will most probably be considered as AIFM for the purposes of the AIFMD, which will entail for them a series of requirements in terms of organisation, risk management and valuation process to put in place, conduct of business rules and limitations as regards delegations and sub-delegations. While AIFMD will hit the Luxembourg market only by 2013 at the earliest, its consequences on the non-UCITS world, including Chapter 16 management companies as AIFM, will be tremendous.

As for the UCITS management companies, the accounts of a Chapter 16 management company must be audited and certified by a Luxembourg authorised auditor, duly approved by the CSSF.

The management companies ruled by Chapter 16 of the Fund Law are also regulated entities in Luxembourg and hence need to be authorised by the CSSF.

The self-managed SICAV (“SIAG”)

One of the particularities of the regime introduced by the UCITS III directives is that it has allowed the corporate UCITS funds to choose to be “self-managed”, i.e. they decided not to appoint a UCITS management company. They are known as SIAG (“Sociétés d’investissement auto-gérées”) and have proven to be a popular structure for UCITS.

The SIAG remains a “product” as such, the units of which are to be sold to investors around the globe: it cannot perform any services to a fund or other client, and the management of its assets is its sole function. However, if they are UCITS SIAG, they must fulfil many of the requirements described before for UCITS management companies, i.e. having:

- At least two managers conducting their affairs, supervising and monitoring its delegates, ensuring a sound risk management process, etc.;
- A permanent risk management function;
- Rules and policies in place to deal with conflicts of interest, apply rules of conduct destined a.o. to ensure the SIAG acts in the best interest of investors. A list of rules applicable to SIAGs (as compared to UCITS management companies) can be found in the Quick Reference Guide of this brochure;
- An important difference (next to the purpose and scope of activities) lies in the capitalisation rules: there are no additional “own funds” for a SIAG, just a minimum capital of EUR 300,000 at the time of the SIAG approval. The governance framework is obviously very different in a SIAG, compared to a fund with a management company. In this instance, the designated managers will act directly with the Board of Directors of the SIAG.

SIAGs are a relatively popular form of UCITS. End of 2010, out of the 685 UCITS SICAVs registered with the CSSF, 196 were self-managed ones.

The self-managed form is standard for Part II SICAVs and for SIFs organised as SICAVs. While they have traditionally not had to comply with substance requirements in terms of managers, resources, delegation control, etc., the Fund Law now imposes to non-UCITS SICAVs to comply with its rules on delegation of asset management, i.e. to regulated entities only and not to the depositary bank.

The depositary bank

A depositary bank (also called “custodian bank”) must be appointed to hold the fund’s assets and exercise other control functions, the extent of which depends on the fund’s status (Part I or Part II of the Fund Law, SIF). It must be a credit institution within the meaning of Luxembourg law, either having a registered office in Luxembourg or be a branch of an EU-based credit institution (for UCITS and SIF). The depositary is always in the same domicile as the fund.

The recent Madoff scandal and its European ramifications, in which assets of UCITS funds deposited with EU custodians had vanished due to fraudulent sub-custodians, has raised the question of the exact roles and responsibilities of a UCITS depositary. It has also shown that not all EU Member States have the same approach and interpretation of the UCITS directive’s rules on depositaries.

In Luxembourg, the duties of a depositary are the safekeeping of the funds’ assets. The task of safe-keeping of the assets means that the depositary has a duty of supervision implying that the depositary must have knowledge at any time of how the assets of the fund have been invested and how the assets are available.

In addition to his safekeeping function, the depositary has various monitoring and supervisory functions, the scope of which depends on the type of fund concerned. For the funds of the Fund Law, the depositary must ensure that the activities of the fund are being performed by the relevant service providers in a proper manner, notably regarding investment activity and settlement of subscription and redemption flows.

As it will now be possible for a Luxembourg UCITS to be operated by a foreign UCITS management company, the depositary in Luxembourg must take necessary measures with that management company to obtain all relevant information allowing it to perform its supervision and control duties.

Financial crisis, Lehmann insolvency and Madoff fraud have shown that to protect investors who entrust their monies to regulated funds, a greater onus should be put on the depositary’s role and responsibility, notably in terms of supervision of its sub-custodian network and obligation of returning the assets to the funds. The recent AIFMD has, to some extent, clarified the depositary’s functions and liability for “alternative” funds (i.e. in Luxembourg, all Part II and SIF funds). UCITS being even more tightly regulated, it appears that European rules need to be passed to have a harmonised approach towards the custody function. This is the object of the current initiative, at EU level, known as “UCITS V”, which purports to clarify the duties of the UCITS depositary in terms of selection, due diligence and supervision of sub-custodian networks and imposes a more strict liability regime.

Central administration

Before UCITS IV and the possibility for a UCITS fund to be run by a management company located outside of Luxembourg, the Luxembourg regulation provided that a fund's "central administration" had to be located in the Grand-Duchy. An old circular of 1991 clarified that the term central administration encompassed essentially those administrative and accounting functions that need to be controlled and supervised by CSSF, auditors and the depositary⁶. This did not prevent from receiving support from entities located outside of Luxembourg.

This requirement did impose, for all funds created under Luxembourg law, to have the administrative agent and the registrar and transfer agent, in Luxembourg. This will probably no longer be mandatory in the future, at least for those UCITS funds that are managed by a foreign management company.

The administrative agent

Officially recognised by a law of 2003 creating new categories of regulated financial professionals active in the fund sector, the basic function of the administrative agent consists for all types of funds, in calculating the fund's Net Asset Value (NAV) and maintaining the fund's accounting records.

From a relatively basic (yet labor intensive) activity, this function has evolved in line with the sophistication of the funds and the instruments they invest in and consequently, the administrative agent will often demonstrate nowadays specific skills like:

- The ability to deal with complex instruments like OTC derivatives, complex swap structures, various types of structured notes involving embedded derivatives;
- The ability to provide the fund with prices for all kinds of investments supporting the investment strategy;
- The ability to understand market practices and legal requirements;
- The knowledge of specific Risk Management tools for alternative UCITS funds;
- Experienced staff used to work in alternative investments;
- The ability to deal with any kind of performance fee calculation (including equalisation);
- The understanding of specific compliance issues;
- The understanding of IT infrastructure enabling effective interface with other service providers;
- The ability to implement pooling techniques;
- The ability to calculate certain tax figures.

The registrar and transfer agent

Also a regulated profession in Luxembourg and subject to specific banking secrecy rules, registrar and transfer agents execute subscription and redemption requests, maintain the fund's share/unit holders register and, in general, correspond with shareholders. Since they are the primary service provider in Luxembourg dealing with the underlying clients, AML/KYC procedures, as well as market timing/late trading monitoring and declarations, are also primary responsibilities of this party.

While the requirement of having these providers performing their services from Luxembourg (often with the help of platforms abroad) will probably remain, at least in the near future, for Part II funds and SIFs, it is unlikely that it will survive UCITS IV, at least for those entities or promoters choosing to have their Luxembourg UCITS run by a management company abroad. It will in that context be interesting to see how other domiciles will tackle the complex issues handled for years by Luxembourg service providers, who had to adapt to the increasing sophistication of Luxembourg products.

The auditors

Any investment fund in Luxembourg, even those run by a management company located abroad, must appoint an auditor, authorised by the CSSF, to certify the accounting information provided in its annual report and, for certain types of funds, provide the management body and the CSSF with information on the operations of the fund and its service providers (through the Long Form Report). The auditors' main functions and obligations are described under the section Audit and reporting (see page 17).

⁶ A description of these functions can be found in Chapter D of the IML Circular 91/75.

Obtaining approval

The CSSF, the Luxembourg regulator, is in charge of the approval, oversight and control of investment funds in Luxembourg. It acts exclusively in the public interest.

All funds domiciled in Luxembourg must be duly authorised by the CSSF, that will also approve the service providers involved in the operations of the fund.

Sponsor of the fund

The Luxembourg supervisory authority has always been very demanding regarding the sponsor of a fund, the entity that decides to launch or distribute a product. Traditionally, any fund subject to the 2002 Law needed to have what is known as a “promoter”, an entity that would ultimately bear a financial responsibility for the fund. The CSSF’s administrative practice in that respect has consistently been to require such promoter to be (i) a regulated entity, with (ii) a significant capital base (at least EUR 7.5 Mio in equity), these conditions being assessed in the course of the fund’s application file. The CSSF also required that a majority of the Board of the fund be composed of promoter’s representatives, so as to ensure its full involvement in the fund it initiates.

For entities which were either too small or otherwise failed to comply with the CSSF requirements, Luxembourg banks often offered a “co-promotership” service, whereby they assumed, against consideration, the roles and responsibilities of the promoter vis-à-vis the CSSF.

The introduction of UCITS IV in Luxembourg and the fact that foreign UCITS management companies approved on their territory may now set-up and run Luxembourg UCITS obviously questions the possibility for CSSF to impose a promoter requirement, as described above.

Luxembourg wants to protect its reputation and remain immune from problems resulting from initiators lacking the necessary seriousness and standing for launching products. Whatever form it will take, there is no doubt that the CSSF will keep a close scrutiny on the entities “behind” the funds, as it has done in the past and does more and more for SIFs, structures which are currently exempt from the promoter’s approval requirement.

Funds approval

In order for a fund to be approved, the CSSF must review and agree to the following constitutive documentation:

- articles of incorporation (if SICAV/SICAF) or management regulations (if FCP);
- prospectus and, for UCITS funds, Key Investor Information Document (“KIID”);
- custodian agreement;
- agreements with the principal service providers: management company (for a UCITS), investment manager, administrative agent, transfer agent, potential distributors, etc.;
- information on the fund’s sponsor.

If the fund is to be launched by a foreign management company, the CSSF will also decide on the application of that entity, which will need to provide information on its delegation arrangements regarding asset management and administration as well as the agreement with the depositary organising the flow of information cross-border.

The directors of the fund (if in corporate form) or of the management company (if in Luxembourg) must be authorised by the CSSF, in view of their experience and reputation: hence, CVs and documentation certifying such reputation must also be filed with the CSSF.

Depending on the type of fund to be approved (Fund Law or SIF), some of the service providers must themselves be subject to supervision by a regulatory authority to be approved by the CSSF. This is, for example, the case for the investment manager who, if acting for a fund ruled by the Fund Law, must be a regulated firm licensed for asset management services and, if located outside the EU, must be in a country whose supervisory authority cooperates with the CSSF. To avoid any conflicts of interests, the investment manager of such fund can never be its depositary bank.

The requirements relating to the quality of the investment managers are not yet foreseen in the current SIF Law. This may, however, change soon in anticipation of AIFMD.

The Key Investor Information document (“KIID”)

In the course of the approval process of a new fund, and even though it will not “visa” the document, the CSSF will want to see the KIID, which is the investor information document replacing the old and far too long “simplified prospectus”. The KIID is the response brought by UCITS IV to the investors’ demand of having simple, understandable, transparent and comparable information on their proposed investment.

A two-page⁷ document, harmonised in form and content, the KIID purports to give the investors essential information on a fund’s policy, its risk and reward profile, past performance, charges borne by fund and investor and a series of practical information.

This KIID, to be revised on a periodic basis to always be as current as possible, will be the main information document for investors, in all countries of distribution and an essential communication tool for asset managers.

Existing Luxembourg funds dispose of a grace period until 1 July 2012 to replace the many thousands of existing simplified prospectuses of UCITS by as many KIIDs. The complexity of cross-border distribution of funds and the requirements which may be imposed by regulators outside of the EU should not be underestimated when preparing for this transition to the KIID.

⁷ Three pages for structured UCITS.



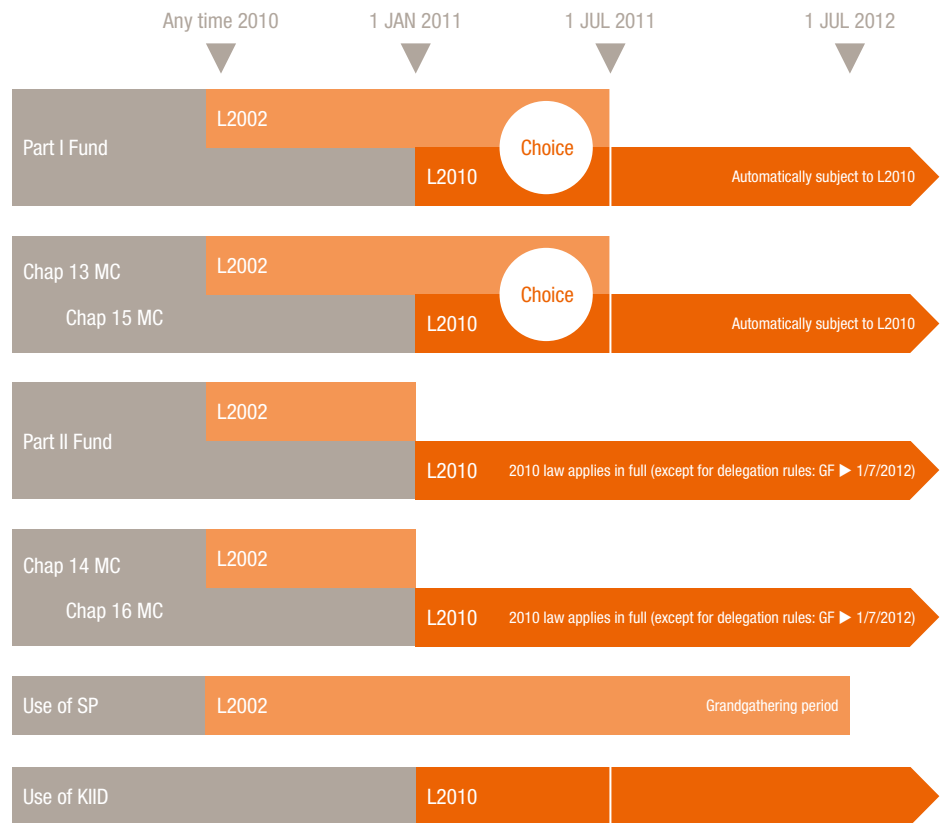
Transitory rules

While the Fund Law has entered into force on 1 January 2011, some of its rules⁸ as regards cross-border activities will only be applicable as from 1 July 2011, which is the latest date for the transposition into the national legislation of Member States.

Part I funds which were created under the 2002 Law will all automatically become subject to the Fund Law in July 2011. They will however need to adapt their prospectuses if they want to benefit from the new flexibilities. A “fast-track” procedure at the CSSF will allow promoters to amend their prospectuses swiftly before the end of 2011, in order notably to insert mandatory new wording on risk management measurement. Management Companies will also be automatically subject to the Fund Law as from 1 July 2011 and will need to be compliant with the new constraints in their organisation and functioning by that date⁹.

All provisions of the Fund Law are already applicable to Part II funds (except for those relating to the delegation of functions, where the funds have until 1 July 2012 to adapt their situation). Non-UCITS management companies are also already subject to the Fund Law, with the same grace period to adapt to the new delegation constraints.

The following diagram illustrates the main transitory provisions:



⁸ Cross-border master-feeders, cross-border mergers, management company passport, cross-border notification.

⁹ A CSSF Circular 11/508 dated 15 April 2011 imposes Luxembourg management companies to update their application file in that respect.

Audit and reporting

Financial statements and the audit report

For funds submitted to the Fund Law, an audited annual report and unaudited semi-annual report are to be made available free of charge to share/unit-holders and sent to the supervisory authority within four months and two months, respectively, of the financial period-end. For SIFs, this period is extended to six months for the audited annual report and there is no requirement to produce semi-annual accounts.

The annual report should include at least the following:

- a management report;
- a statement of assets and liabilities;
- a detailed income and expenditure account;
- a report on the activities of the past fiscal year;
- the portfolio of the investments;
- a statement of changes in net assets;
- the number of shares/units in circulation and the value of Net Asset Value per unit/share;
- statistical information with regards to total Net Asset Value and Net Asset Value per unit/share over the last three fiscal years.

The semi-annual report includes the same information with the exception of the detailed income and expenditure account, the statement of changes in net assets, the statistical information over a three-year period and the management report which may be omitted. As indicated above, the semi-annual report is not mandatory for SIFs.

- Financial information is prepared under Generally Accepted Accounting Principles applicable to investment funds in Luxembourg (“Luxembourg GAAP”). Derogation to use different GAAP like IFRS can be obtained;
- The accounting information included in the annual report of a Luxembourg fund has to be audited by a Luxembourg authorised auditor (“réviseur d’entreprises”), approved by the CSSF. The auditor’s report must certify that the financial statements give a true and fair view of the financial position of the UCI and of the results of its operations and changes in its net assets for the period, in accordance with Luxembourg legal and regulatory requirements relating to the preparation of the financial statements.

The auditor also has a legal obligation to inform the CSSF if the accounting information does not present a true and fair view of the UCI’s financial position.

In addition, he is also bound by such reporting obligation if he becomes aware that the assets of the UCI are not or have not been invested in accordance with the respective legal requirements or the provisions of the prospectus.

What’s more, the Luxembourg investment funds must provide to the CSSF a monthly set of figures. This is generally performed by the central administration in Luxembourg.

The Long Form and the auditor reporting

In addition, the auditor must produce the so-called Long Form Report describing and testing the UCI's activities. This Long Form Report is solely for the attention of the Board of Directors of the SICAV or of the management company and the CSSF. It covers defined areas including, among others, an evaluation of key internal control procedures existing at the central administration and depositary bank, Anti-Money Laundering provisions, valuation methods, description of the Risk Management system, etc. SIFs are not subject to a Long Form Report.

The auditor should also prepare a specific report in case of material net asset calculation error and/or investment breaches that lead to a compensation of the UCI and/or its investors in accordance with the principles detailed in the CSSF circular 2002/77.

In addition to these tasks foreseen by law or regulation, the CSSF also often requests the auditor to issue specific certificates or attestations concerning e.g.:

- the pricing of OTC derivatives, where the auditor will have to confirm the pricing model and list of parameters;
- the calculation methodology of performance fee;
- the validity of an outsourcing model and its conformity with local regulation.

Management companies

Both UCITS and non-UCITS management companies, as regulated entities, must be audited by a Luxembourg authorised auditor, who can demonstrate an adequate professional experience. The CSSF may define the scope of the auditor's mandate and the contents of the audit report of the annual accounting documents of a management company. In any event, the auditor has a general obligation to report to CSSF if, during the audit of the accounts, it becomes aware of any fact or decision which is likely to constitute a material breach of the law, impairs the continuous functioning of the management company or may lead the auditor to refuse to certify the accounts or to express reservations.

CSSF, using the auditor as its watchdog, may request it to perform controls on particular aspects of the activities and operations of a management company, at the expense of the management company.



Supervisory Cooperation between Member States

Many of the new measures introduced by UCITS IV, like the management company passport, cross-border mergers and master-feeder structures will require an increased exchange of information between the national supervisory authorities of the Member States in which asset managers will be active. In this context, UCITS IV provides for a minimum degree of harmonisation of supervisory powers designed to improve cooperation mechanisms between national supervisory authorities.

While the existing UCITS framework already imposed a general obligation on national supervisory authorities to co-operate with one another, UCITS IV takes this cooperation one step further by imposing a detailed framework for information exchange. One national supervisory authority will now have the possibility to request the cooperation of another authority for on-the-spot verifications or an investigation on the territory of the latter.

In particular, where a Luxembourg UCITS is managed by a non-Luxembourg management company, the supervision is split between the CSSF for the UCITS, on the one hand and the other authority for the management company, on the other hand. These authorities will now have to establish mechanisms for the exchange of information concerning any problems arising or any decisions that need to be taken against an entity. The Fund Law, in line with the UCITS IV Directive, contains provisions on the investigations or on-the-spot verification of any entity in Luxembourg, as may be demanded by the supervisory authorities of any given Member State.

Hence, if CSSF receives on-the-spot verification or investigation requests from the supervisory authority of another Member State, the CSSF may carry out the verification or investigation itself, allow auditors or experts to carry out the verification or investigation, even allow the requesting competent authorities to carry out itself the investigation subject however to the overall control of the CSSF. The CSSF may in limited cases refuse to exchange information or to act on a request for cooperation in carrying out investigation or on-the-spot verification in certain situations.

The European Securities Market Authority (“ESMA”), successor of the Committee of European Securities Regulators (“CESR”), will now have an increased role at the level of colleges of supervisors, including a mediation process to try to resolve possible “disputes” between national supervisory authorities and conduct peer review analysis.

In addition to its previous duties as CESR, ESMA is aimed at contributing to the stability of the financial system of the EU by ensuring integrity, transparency, efficiency and orderly functioning of the financial markets while enhancing protection to investors. In the light of these new competencies and in contrast to CESR, ESMA is entrusted with the possibility to elaborate directly applicable binding technical standards. Among others, ESMA will now have new powers in the field of consumer protection and arrangement of centrally accessible data base of registered financial institutions.

Supervisory and Investigatory Powers

The CSSF, in the light of its supervisory and investigatory powers, has at its disposal specific measures and penalties to ensure that the UCITS, the management company and depositary comply with the high quality framework that the UCITS regime imposes.

These powers include, inter alia, the access to any document in any form and the right to receive a copy; to require any person including management companies or depositaries, to provide information and if necessary to summon and question a person with view to obtaining information; to require the cessation of any practice that is contrary to the UCITS regime; to request temporary prohibition of professional activity as well as full withdraw of the authorisation granted to the UCITS, management company or a depositary; to impose the suspension of the issue, repurchase or redemption of unit/shares in the interest of unit or shareholders or the public, to impose fines.

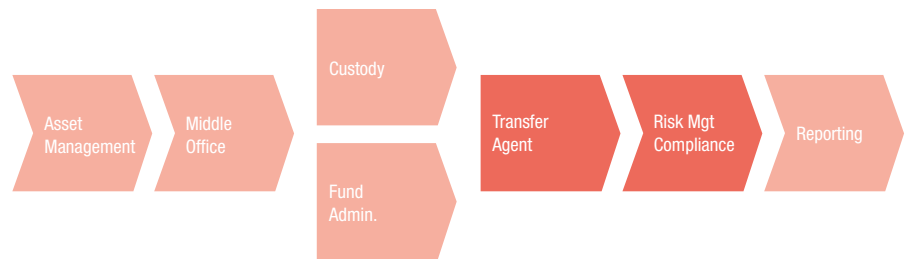
Product and operational flexibility in Luxembourg

Luxembourg is globally known for its dominant position in domiciliation and administration of UCITS funds. Since the implementation of the first UCITS Directive in 1988, it has established itself as the leader in UCITS fund administration and fund custody. The early embracement of the UCITS scheme has contributed to the creation of a pan-European and international distribution hub as 75% of worldwide mutual fund registrations were domiciled in Luxembourg.

The positioning of Luxembourg has led to the establishment of significant depth and expertise within the service provider community to support the complexities of internationally invested and distributed funds.

Within the generic value chain of the asset management industry, Luxembourg is positioned with a strong focus on back-office tasks. However, the substance and governance requirements introduced by the UCITS III regulation have broadened the competencies of the Luxembourg service providers and management companies (e.g. Risk Management, distribution reporting, etc.). With UCITS IV and the new structures it allows, this well established sophistication in back-office tasks comes as a true competitive advantage as compared to other domiciles.

Some of the more common features of complex fund administration support/structuring that are readily seen in Luxembourg are summarised below. These solutions have evolved over time and are constantly being expanded to meet the needs of today's fund providers.



Innovative services in fund administration

The administration of investment funds is largely considered a commodity. However, Luxembourg has developed over the past years a number of very distinctive administrative services that support fund promoters, asset managers or distributors in their activities.

The dilemma of the fund promoters has never been as intense as today: they have to cope with an increasing pressure on margins due to disintermediation and competitive products (e.g. ETFs, certificates) in a context of higher need for more tailored fund products due to an intensified competition over investor money. Luxembourg service providers are world leaders in providing solutions to this dilemma:

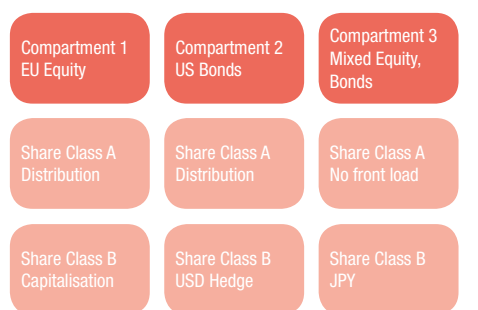
Umbrella ABC



Umbrella funds

The same legal entity can contain an unlimited number of “compartments”. These compartments are allowed to have distinct investment policies and, although part of the same legal entity, rights and obligations of the investors are segregated. Umbrella funds contribute thus to a limitation of the number of legal entities and by such to a reduction of the time-to-market as well the costs involved for the launch and maintenance of an investment vehicle.

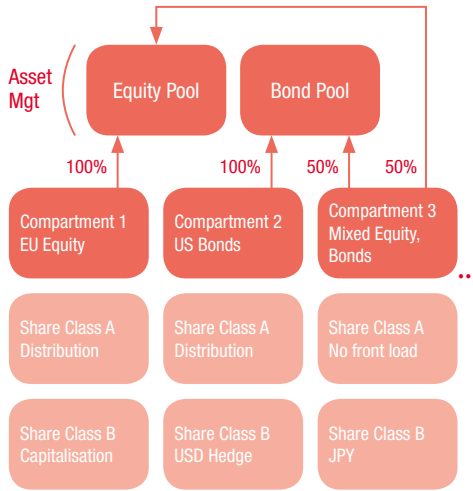
Umbrella ABC



Multiple share classes

The flexibility of the umbrella principle is further enhanced by the possibility to create an unlimited number of share classes in fund/compartments. Each share class can be tailored to needs of the investors to whom the fund is distributed. Common share class characteristics are different dividend policies, base currencies, investor types, fee levels. In addition, class specific hedging techniques are more and more being observed.

Umbrella ABC



Intra/extra-fund pooling

The concept of pooling is an administration service directly supporting asset managers. In essence, pooling allows consolidating on an accounting level the assets of multiple compartments of single fund (i.e. intra-pooling) or of multiple legal entities (i.e. extra-pooling or cloning).

The pooling of assets thus allows creation of common pools of assets assigned to asset managers without restricting the fund profiles distributed to investors. In addition, pooling enables asset specialisation and economies of scale in terms of portfolio management and transaction costs.

Umbrella ABC



Multi-manager portfolios

This concept is similar to asset pooling, the difference being that each fund/compartment has multiple managers. As such, the Asset Management specialisation effects are still maintained, however, the economics of scale are rather limited due to multiplication of investment “pockets” per funds/compartment.



The above services are considered standard services in Luxembourg and provided by most large service providers. This has made Luxembourg a unique environment allowing competitive pricing of back-office services combined with a sophistication of service level well above most other fund domiciles in the world.

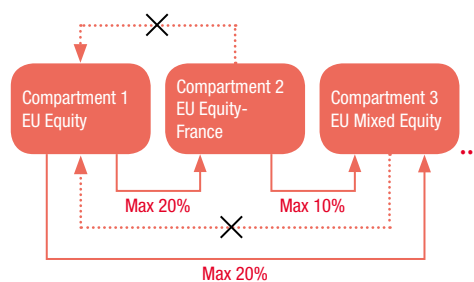
The Fund Law has added to this operational arsenal a few novelties that will push even further the boundaries of asset pooling.



Cross sub-fund investment

With the possibility of “cross sub-fund investments”, it becomes now possible for any compartment created within a fund to invest into one or more other compartments of that same structure.

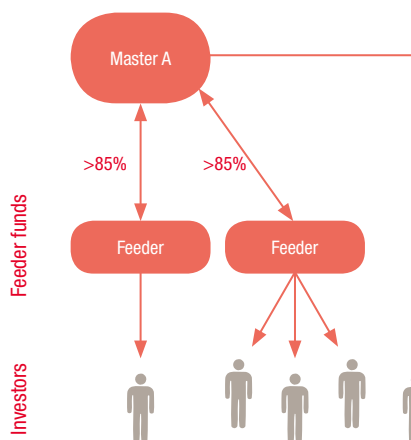
Umbrella ABC



While there are some limitations as to the maximum percentage of the NAV of a given sub-fund invested into another one (20% max) and to the number of shares of target sub-funds held by the investing sub-fund, this structure allows, within the same UCI, the use of fund of funds investment policies, without the need for two separate legal entities. It may also allow efficient cash management, by having all sub-funds of a given UCI investing their ancillary cash in a specially allocated sub-fund.

Master-feeders

The implementation of UCITS IV in the Fund Law will allow the creation of UCITS-compliant master-feeder structures. Although not a novelty under Luxembourg law, where they were already admissible between two local funds, master-feeders will now permit the cross-border pooling of assets.

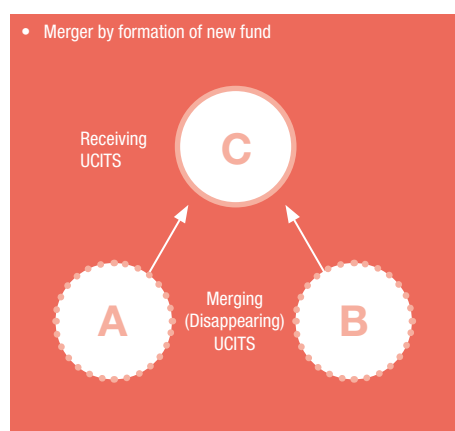


In a master-feeder construct, one or several feeder funds, established in any Member State of the EU, invest a minimum of 85% of their assets in a master fund, which may be located in another Member State.

There are several conditions to be fulfilled to create those structures, pertaining to the master and to the feeder(s). This UCITS-compliant structure will be a powerful distribution tool, permitting to adapt to the “local” taste of investors, while permitting the pooling of assets and hence enhanced efficiency. There are, however still a few tax uncertainties to be clarified, failing which the success of master-feeders will be in jeopardy.

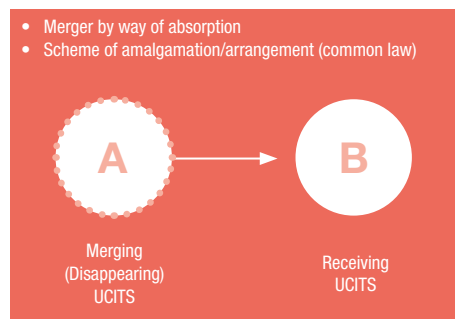
Fund Restructuring

Strictly-speaking not an operational flexibility, the possibility opened by the UCITS IV directive to merge funds even on a cross-border basis will allow to rationalise fund ranges while increasing asset pools, hence contributing to economies of scale.



Three mergers schemes are recognised by the UCITS IV Directive, as depicted here. Detailed rules regarding merger approval, third party controls and investors rights will make a cross-border merger a complex procedure.

Many questions relating to the actual migration of the assets, the impact on the distribution of the fund and, last but not least, the tax neutrality (or absence thereof) of the merger for investors are yet to be cleared.



These issues should not, however, hide the fantastic advantage of having at last a legal tool permitting market consolidation and rationalisation of UCITS fund structures.

Distribution support

The administration and custody activities in the UCITS fund value chain have traditionally been concentrated in Luxembourg. Yet, in a more and more active manner, Luxembourg is also focusing on global distribution support activities. In this area, trailer fee administration hubs or distribution agreement negotiation are service models making use of the concentration of cross-border fund distribution in Luxembourg, especially towards the new distribution markets in Asia and Latin America. Linked to this is the ability of administrators in Luxembourg to support the complex and varied needs of investors tax reporting for various domiciles like Germany, Austria and the UK.

Risk Management

Risk Management is among the basic principles of the UCITS framework, largely assigning the control and monitoring of risks inherent to the product and its service providers to the management company of the UCITS funds. By doing so, Risk Management becomes a key differentiation factor for the UCITS brand overall, as well as for each promoter individually. In the distribution filing with non-EU supervisory authorities, the sound expertise in Risk Management is a key selling argument for granting the market access and acceptance of UCITS products. By such, the competence of the Luxembourg management companies of monitoring risk measurement and consolidating the scattered contributions of the promoter's organisation is essential to cover the full spectrum of risks inherent to an investment fund (i.e. market risk, credit risk, liquidity risk, distribution risk, reputation risk, operational risk) and ensure distribution success in Europe and abroad.

Under the risk principles and global exposure guidance published by ESMA (i.e. CESR 09-178 and 10-788), UCITS funds may now use derivatives to replicate strategies that, until recently, were the domain of the Hedge fund managers. Strategies like market neutral/absolute return, long/short equity, fixed-income or commodity trading are now common in the Luxembourg market within the so-called “Alternative UCITS” funds. To benefit from this increased scope of products, the UCITS guidelines impose the establishment of a robust Risk Management framework as noted above. The success in Luxembourg of providing such solutions, linked to the abilities of Luxembourg-based administrators to effectively deal with the back-office requirements of highly complex daily priced products has meant that the Grand Duchy has become a centre for many of the more complex UCITS products seen on the market place today.

In addition, UCITS IV foresees additional disclosures relative to the risk exposure (i.e. VaR levels) and leverage used within the portfolio management strategy. These disclosures are to be made within the prospectus (ex-ante estimates) or within the financial statements (ex-post computations).

Alternative funds (Hedge funds, Real Estate funds, Private Equity funds)

Each large asset management company is grappling with the blurring of the distinction between traditional long-only investment and alternative strategies. In Luxembourg, this is evidenced both by the strong growth in pure alternative funds and also the rapid emergence of alternative strategies embedded within the UCITS funds – the above-mentioned “Alternative UCITS”. The innovation in the regulatory framework (e.g. SICAR, SIF) has fostered a dominant position in closed or open-ended Real Estate funds, some of them distributed on a cross-border basis. In addition, Luxembourg has well established administration expertise for Private Equity and fund of Hedge fund structures. The general shift towards non-traditional asset classes has forced the majority of the traditional fund administrators to broaden their service proposal and invest in dedicated resources and systems. Most of the Luxembourg providers are now able to perform high quality accounting of alternative funds with the specific aspects of consolidation and IFRS reporting. What’s more, distribution aspects like shareholder monitoring (e.g. hot issues, capital calls and side pockets) and performance fee management (e.g. computation, shareholder equalisation and crystallisation) are part of the standard services offered. Thus, the one-stop-shopping of traditional and alternative fund servicing can be achieved, at least on a domicile level, by relying on dedicated resources and technically mature infrastructures.

Sourcing

Luxembourg is appreciated because of its deep expertise in fund administration, its multi-cultural pool of qualified resources and flexible service approach. The increase in volumes and number of mandates over the past years has challenged the availability of skilled resource. As such, to avoid limiting the business growth as well as the quality of services delivered, the Luxembourg regulator has adopted a business-minded approach regarding sourcing and “rightshoring”. Various models exist in the market place making use of competencies/resources existing in other parts of the service provider’s organisation (e.g. centralised risk measurement department) or offshoring of parts of the administration tasks (e.g. trade input, reconciliations and pricing). The sourcing models are embedded in the existing regulatory environment, essentially focusing on the controlling/monitoring of the outsourced tasks to be performed in Luxembourg.

Conclusion

Innovation and service quality are required and driven by competition. Luxembourg must remain innovative to continue to succeed and it will continue to be so, setting a very high market standard compared to other domiciles.

Taxation of investment funds

Luxembourg funds are essentially tax-exempt vehicles (with the exception of the asset based tax, the subscription tax or “taxe d’abonnement”). They may be formed either as a corporate type or contractual type vehicle, thus enabling the vehicle to be either opaque or look-through according to the fund provider/investor needs. Key aspects of taxation may be summarised as follows.

Taxation of income/capital gains

Luxembourg investment funds (UCITS and non-UCITS) are not subject to income/capital gains taxes in Luxembourg. Capital gains realised on non-Luxembourg assets could be potentially subject to taxation locally depending upon the country of investment and the application of double tax treaties.

Withholding taxes on income received

Withholding taxes levied at source on income received by a Luxembourg fund are normally not refundable (unless a relevant tax treaty applies) nor creditable. While UCIs formed as investment companies (SICAV, SICAF) may benefit from certain double taxation treaties¹⁰, FCPs will generally not.

However, the unitholders of an FCP should be in theory able to claim the reduced rate under the double taxation treaty between the country of source and the country of residence of the investors. This possibility usually applies as long as the FCP is simultaneously recognised as tax transparent by the source country and by the investor country.

There are currently 36 double taxation treaties potentially applicable to a Luxembourg SICAV/SICAF. When there is no tax treaty application to a Luxembourg SICAV/SICAF for a particular country, there are however several possibilities to mitigate or even avoid the withholding tax costs.

Tax on distributions

Distributions by investment funds, whether paid to resident or non resident investors, are not subject to any Luxembourg withholding tax (see however comments hereafter regarding the EUSD). The tax position of the investor depends on the legislation applicable in his/her country of residence.



¹⁰ Corporate funds are not subject to any corporate income tax in Luxembourg; this is why access to double taxation treaties is sometimes restricted.

Other taxes

Value Added Tax (VAT)

The management of investment funds (UCITS and non-UCITS) subject to the supervision of the CSSF is exempt from VAT in Luxembourg. The same applies to the management of foreign investment funds, which are subject to a “prudential supervision” in their country. The VAT exemption applies among others to the investment management and administrative functions, including investment advice, transfer and registrar agent functions, etc.

Management services outsourced to third-party managers also benefit from the VAT exemption under certain conditions. They must form a distinct whole and are specific to and essential for the management of the fund. In this regard, the outsourcing of only one “isolated” type of service may not benefit from this VAT exemption.

The distribution of investment funds is also exempt from VAT.

Other services like legal and audit services rendered to investment funds cannot benefit from a VAT exemption and are subject to the 15% standard VAT rate.

The depositary services are partly exempt from VAT. The part related to the control and supervision functions of the depositary is subject to VAT at 12%.

Investment funds with corporate form are VAT taxable persons and may be required to register for Luxembourg VAT purposes when they receive goods or services from abroad for which they are liable to account for Luxembourg VAT on a reverse charge basis. Contractual funds (FCP) are considered to be the same legal person as their management company and have the same VAT number.

Registration Duty

A registration duty of EUR 75 is due upon incorporation of the legal entity.

Subscription tax (“Taxe d’abonnement”)

An annual subscription tax of 0.05% of net assets is payable and calculated quarterly, based on a UCI’s Net Asset Value at the end of each quarter.

The rate is reduced to 0.01 % p.a. for UCIs invested solely in money market instruments and bank deposits.

This reduced tax of 0.01 % p.a. is also levied on the total net assets of UCIs which are governed by the SIF Law and of institutional sub-funds and classes of shares even if offered, as the law allows, within a fund subject to the Fund Law.

The proportion of a UCI’s assets invested in other Luxembourg UCIs, which have already been subject to subscription tax, are exempt for the purposes of computing the tax.

There are also several other exemptions available: for money market SIF, and SIF reserved for institutions for occupational retirement provision, or similar investment vehicles, set up on one or several employers’ initiative for the benefit of their employees and companies of one or several employers investing the funds they own, in order to provide their employees with retirement benefits. In addition, the Fund Law foresees an exemption from subscription tax for funds (or sub-funds) investing mainly in microfinance institutions as well as for Exchange Traded Funds (“ETFs”). Finally, funds dedicated to multi-employer pension vehicles or to several employers providing pension benefits to their employees are also exempt.



Taxation of share/unit-holders

Luxembourg resident investors

The taxation of investors residing in Luxembourg depends upon whether they are corporations or individuals.

(a) Corporate investors

Dividends and capital gains

Dividends and realised capital gains are subject to tax (at a rate of 28,80% for 2011 for a corporation established in Luxembourg city) in Luxembourg as they are deemed to be part of the commercial profit of the investor.

(b) Individual investors

Distributions by investment funds

Individual investors must declare any distributions received and will be taxed at their own progressive tax rates (maximum 41.34%). In addition, a 1.4% dependency contribution and a 0.8% crisis contribution have to be calculated.

A total lump-sum deduction of EUR 1,500 (doubled for married taxpayers taxable jointly) applies on total distributions (dividend and interest income subject to final taxation) received during the tax year.

UCIs may neither reclaim foreign withholding taxes on behalf of their investors nor transfer foreign tax credits to them, although these may in theory be available through double tax treaties.

In principle, FCPs should be considered as transparent from a Luxembourg tax point of view so that any income received by an FCP should be immediately taxable at the investor level according to its nature. Again, practical application of the tax transparency of the FCP is quite rare.

Capital gains

Capital gains may either:

- be taxed as speculative profit or as sale profit, or
- be exempt from taxation.

Resident investors

Disposition within six months

A Luxembourg resident investor is deemed to make a speculative profit when he/she sells or exchanges his/her shares/units within a six-month period following the acquisition. To the extent that the annual global amount of speculative profit exceeds EUR 500, the said profit is taxed at progressive tax rates (maximum 41.34%). In addition, a 1.4% dependency contribution and a 0.8% crisis contribution have to be calculated.

Disposition after six months

A Luxembourg resident investor is deemed to make a sale profit when he/she sells an important shareholding interest over the above-mentioned six-month period. Generally speaking, a shareholding interest is deemed to be important when the seller holds, or held at any time during the five previous years, alone or together with the spouse and his/her minor children, directly or indirectly, more than 10%¹¹ of the capital (or of social assets if there is no capital). The said sale profit is taxed at maximum 20.67%. In addition, a 1.4% dependency contribution and a 0.8% crisis contribution have to be calculated.

Gains derived from the sale of shares/units, which have been held for more than six months and that do not qualify as important shareholding interest of at least 10% are tax exempt.

Non-resident investors

Under Luxembourg law, income paid to non-resident investors holding shares/units in Luxembourg UCIs is tax-exempt. As from 1 January 2011, non-resident investors are no longer subject to Luxembourg capital gains tax on the disposal of shares in a Luxembourg SICAV.

¹¹ This threshold is increased to 25% when the shareholding interest has been acquired before 1 January 2002 and has not been further increased as from that date.

European Savings Directive

The Luxembourg Law of 21 June 2005 implemented the EU Council Directive 2003/48/EC on taxation of savings income in form of interest payments.

The Directive's goal was to prevent European investors from escaping their personal tax obligations regarding their savings income.

Following this agreement, all EU Member States – with the exception of Austria and Luxembourg only (Belgium has decided to discontinue applying the transitional withholding tax as of 1 January 2010 and exchanging information as of that date) – certain associated and dependent territories, as well as some third countries, are now automatically exchanging information on cross-border EU interest payments originating in their territories. Depending on their legal form and regulatory classification, distribution made by some funds (UCITs according to the Directive 85/611/CEE or entities who opt to be treated as such), or capital gains realised on these funds, could be caught by this Directive when their investments in debt claims exceed certain threshold.

Austria and Luxembourg as well as some of the associated or dependent territories/ third countries are allowed to levy a withholding tax on such payments instead of exchanging information. (Exchange of information remains possible for these countries however upon express election by investors). The rate of withholding tax has been increased to 20% (since July 2008) and will rise to 35% as from 1 July 2011.

When structuring a Luxembourg-based fund, it is essential to take into account the impact of this tax requirement, as the location of service providers (like the paying agent for example), is even more important than the fund's domicile. The choice of legal form and investment strategy is also a key factor for determining whether the fund may be in the scope or not of the EUSD.

Revision of the EU Savings Directive

It should be noted that the European Commission issued a draft proposal in order to amend the EU Savings Directive (amended version dated 25 November 2009). Possible (future) EU Savings implications should thus be monitored on a continuing basis. The amendments will notably concern: the notion of beneficial owner, the definition of paying agent and an extension of the EUSD products' scope (will notably be considered in scope all investment funds or schemes independently of their legal form and located either into an EU Member State or into the European Economic Area).

Taxation of management companies/advisory companies of Luxembourg funds

The management company of a SICAV, commonly set up in the legal form of an S.A. or an S.à r.l., is a fully taxable company being subject to municipal business tax and corporate tax (aggregate tax rate of 28.80% in Luxembourg City) with its worldwide income, as well as annual net wealth tax of 0.5%.

Management company passport and residency conflicts

According to UCITS IV, management companies could carry out collective portfolio management activities in other Member States for which they have been authorised in their country of origin, either through the free provision of services or by establishing a local branch.

From a tax perspective, this opportunity could generate some tax residency issues for funds managed by a management company established in a different jurisdiction. As a consequence, and depending upon particular facts and circumstances, a foreign fund could potentially be taxed in the country where the management company is resident.

The Fund Law brings a legal certainty by expressly stating that, where a foreign UCI is managed by a Luxembourg-based management company (or where the UCI's place of effective management is located in Luxembourg), the UCI will not be deemed to be domiciled in Luxembourg and will therefore not be subject to any tax in Luxembourg.

Distribution of investment funds

Cross-border distribution of Luxembourg funds

Almost without exception, Luxembourg funds are established to sell on a cross-border basis in markets all around the world and thus distribution and the gathering of assets is the most important aspect in the life of a Luxembourg fund.

For more than 20 years Luxembourg has remained the number one hub for cross-border funds and the leading product for global distribution, especially for UCITS. Today, more than 40 of the top 50 leading cross-border fund management groups use Luxembourg-based UCITS platforms for their global distribution strategies. In fact the Luxembourg brand has become so strong that it is now synonymous with global fund distribution. Distributors, investors and regulatory authorities around the world known, accept and respect the Luxembourg UCITS brand.

Within the EU, Luxembourg UCITS funds benefit from the pass-porting arrangements available under the UCITS Directives and are thus able to be freely publicly marketed within all Member States, subject to the “notification” process in each State.

Whilst the notification procedures to follow in each Member State are harmonised and, since UCITS IV, dramatically simplified as compared to the previous situation¹², there are differences surrounding the local marketing arrangements that need to be complied with, together with various tax reporting requirements in some jurisdictions. Often your Luxembourg UCITS will also be required to appoint a financial institution to act as a local paying and information agent towards local investors.

Outside the EU, Luxembourg UCITS funds must satisfy local regulations governing public distribution of foreign funds. This will of course vary from country to country. However, such is the acceptance of the Luxembourg UCITS brand that many jurisdictions UCITS funds have a “lighter” authorisation process than is the case for non-UCITS equivalent investment funds.

Over the past seven years or so Luxembourg UCITS have been marketed strongly across the Asian region. In fact in many of the key Asian markets, Luxembourg UCITS are clearly the most dominate investment fund sold locally. The Asian region has recently been supplying approximately 35% of all net sales into UCITS. Moreover, Luxembourg UCITS are increasingly sold into the Middle East, especially Bahrain and Latin America, especially Peru and Chile to the large and growing pension fund market.

The following map illustrates this trend: **Hot spots for distribution**



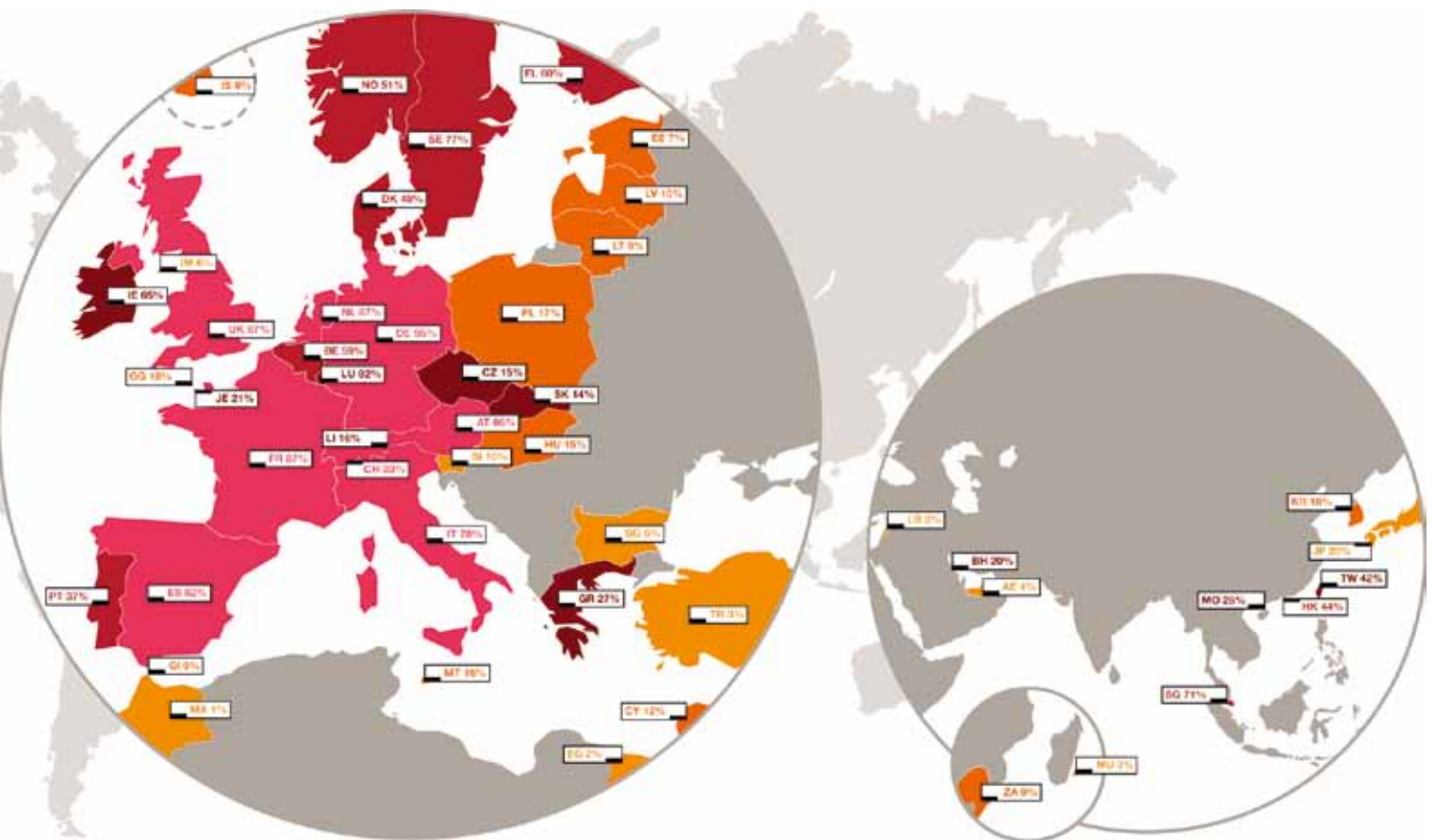
¹² Please refer to the Quick Reference Guide “UCITS IV - Cross-border notification of UCITS” for additional information on this simplified process.

Explanation The heat map indicates the total number of registrations at the end of 2010 (see table “Target Markets”) while the percentage shows the number of Top 100 cross-border management groups distributing in each market.

Total number of cross-border registrations as at 31 December 2010:

- Over 3,000
- Between 1,000 and 2,999
- Between 500 and 999
- Between 100 and 499
- Less than 100

x% Percentage of Top 100 management groups distributing cross-border funds in each market



Distribution of Luxembourg non-UCITS funds in other jurisdictions

Although less common, it is possible to publicly distribute Luxembourg non-UCITS funds in a number of EU and non-EU jurisdictions. However, the authorisation process is very time consuming, expensive and often complex, as each jurisdiction will tend to require the Luxembourg fund to satisfy local regulatory requirements regarding public distribution.

These requirements can often lead to features of the fund needing to be constantly altered to comply with local requirements in multiple jurisdictions, most of which are not similar or even compatible.

The result of this complexity is that it is simply not practical to publicly distribute certain types of non-UCITS funds in a large number of jurisdictions. Moreover, some jurisdictions do not even allow the possibility of authorisation of non-UCITS funds for public distribution if they operate a certain investment policy, for example, a Hedge fund or a Private Equity strategy. The alternative is to distribute these non-UCITS via private placement arrangements to certain restricted investor types and segments.

Alternative distribution methods for investment funds

Private placement

An alternative to public distribution is distribution by way of private placement. Typically this means seeking local investors without entering into public marketing arrangements or processes, as they may be defined under the domestic regulatory framework of the host jurisdiction.

For many years private placement has been a common method of distribution for Luxembourg based non-UCITS funds both in and outside the EU. Invariably, the target investors of non-UCITS funds have tended to be large institutional or sophisticated or professional investors rather than mass retail or high net wealth individuals.

Because of the intended market segment, private placement has been a viable distribution strategy for many funds mainly because the regulations of many jurisdictions allow for certain investors to subscribe for shares or units with the foreign fund, which do not require the authorisation, notification and supervision of the host country supervisory authority.

It is possible to distribute both domestic and foreign investment funds in Luxembourg on a private placement basis notwithstanding that there are no specific rules regarding private placement but, rather certain marketing activities that would not be considered to be public in nature.

Distributing Luxembourg domiciled UCITS and non-UCITS funds into selective jurisdictions via private placement is becoming increasingly common, especially for funds targeting a very narrow category of institutional type investors. However, as above-mentioned, there are no harmonised rules within the EU surrounding private placement and thus, fund promoters must contend with the specific local regulations governing private placement (or lack of), in every jurisdiction of intended distribution.

Whilst this form of distribution provides quick market entry there are drawbacks in the sense that the scope of available investors is quite limited and the rules or market practices are often widely interpreted and subject to change, meaning increased risks of non-compliance with local regulations.

Fund wrappers

Investment funds may also be offered through life insurance wrappers provided that certain investment restrictions and eligible assets criteria are respected and satisfied. Sold via firms benefiting from the Insurance Mediation Directive, they may, in this manner, be offered throughout Europe.

They may finally be wrapped in structured products, securitised or otherwise included in a distinct mantle than the fund one, thereby even potentially taking advantage from other EU Directives conferring a passport, like the 2003 Prospectus Directive.

Listing funds on the Luxembourg Stock Exchange

The Luxembourg Stock Exchange offers broad listing opportunities for UCIs via its two markets, the “Bourse de Luxembourg” market, operated since 1929 and the Euro MTF, which is a Multilateral Trading Facility, in operation since 2005. The “Bourse de Luxembourg” market is a European regulated market and hence issuers on that market are subject to the requirements of the Prospectus and Transparency Directives, contrary to the Euro MTF.

There are no restrictions on the type of securities (shares, fund units and bonds) which can be listed on both markets, as long as they comply with the Rules and Regulations of the Luxembourg Stock Exchange. Issuers need to comply with the specific requirements of the market they have chosen, both prior to and after admission to trading in terms of disclosure obligations.

UCIs can thus, under certain conditions, be listed either on the “Bourse de Luxembourg” market or on the Euro MTF. At the end of 2009, 7,285 UCI shares and units were listed on the Luxembourg Stock Exchange. What’s more, between 1996 and 2009, the number of shares and units of UCIs has increased from 2,766 to 7,285. Domestic Hedge funds and Real Estate funds as well as foreign offshore funds are among the vehicles the units/shares of which are listed in Luxembourg.

Listing a UCI triggers some constraints, but mostly brings the following advantages:

- Increases a fund’s potential investor base;
- Makes it eligible for other investment funds;
- Provides daily liquidity and mark-to-market: investors can trade the fund’s shares without getting involved in time consuming subscription and redemption procedures;
- Investors pay only usual brokerage and not redemption fees;
- Provides publicly available information for investors;
- Increases the image and profile of a fund and provides enhanced market visibility, which can be a valuable marketing tool;
- Provides liquidity to enclosed-ended funds.

Further information on the listing process, in particular conditions for listing, content of the application file and continuing obligations of listed UCIs are available on the Luxembourg Stock Exchange website (www.bourse.lu).



Glossary

ALFI: Association Luxembourgeoise des Fonds d'Investissement (the association representing the Luxembourg fund industry)

AML: Anti-Money Laundering

AUM: Assets Under Management

CESR: Committee of European Securities Regulators

CSSF: Commission de Surveillance du Secteur Financier (the Luxembourg supervisory authority)

EFAMA: European Fund and Asset Management Association

ESMA: European Securities Market Authority

EUSD: European Union Savings Directive

FCP: Fonds Commun de Placement (contractual funds)

GAAP: Generally Accepted Accounting Principles

IML: Institut Monétaire Luxembourgeois (former denomination of the CSSF)

IFRS: International Financial Reporting Standards

KYC: Know Your Customer

MiFID: Market in Financial Instruments Directive

NAV: Net Asset Value

MTF: Multilateral Trading Facility

OECD: Organisation for Economic Co-operation and Development

Part I funds: UCITS governed by Part I of the Law of 17 December 2010

Part II funds: UCIs funds governed by Part II of the Law of 17 December 2010

SIAG: Société d'Investissement Autogérée (self-managed investment company)

SICAF: Société d'Investissement à Capital Fixe (investment company with fixed capital)

SICAR: Société d'Investissement en Capital à Risque (investment company in risk capital)

SICAV: Société d'Investissement à Capital Variable (investment company with variable capital)

SIF: Specialised Investment Fund

UCI: Undertakings for Collective Investment

UCITS: Undertakings for Collective Investment in Transferable Securities

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UCITS

Applicable legal framework

As from 1 July 2011, Luxembourg UCITS funds are subject to the following main laws and regulations:

- Part I and Part V of the law of 17 December 2010 on Undertakings for Collective Investment implementing the UCITS IV Directive (the “Fund Law”);
- IML Circular 91/75 of 21 January 1991 clarifying certain aspects of the UCI legislative framework;
- IML Circular 97/136 of 13 June 1997 on financial information to be provided by public funds;
- CSSF Circular 02/77 of 27 November 2002 on the protection of investors in case of NAV calculation error or breach of investment rules;
- CSSF Circular 07/308 of 2 August 2007 on the use of derivatives and management of financial risks (will apply only until 1 July 2011);
- Grand Ducal Decree of 8 February 2008 transposing Directive 2007/16/EC which clarifies certain definitions in the UCITS III Directive;
- CSSF Circular 08/356 of 4 June 2008 on the use of securities lending, “réméré” and repo transactions;
- CSSF Circular 08/371 of 5 September 2008 regarding electronic transmission of prospectuses and financial reports of UCIs and SIFs to the CSSF;
- CSSF Circular 08/380 of 26 November 2008 regarding guidelines of the Committee of European Securities Regulators (CESR) concerning eligible assets for investments by UCITS;
- CSSF Regulation N° 10-04 on organisational requirements, conflicts of interest, conduct of business, risk management and content of agreement between a depositary and a management company;
- CSSF Regulation N° 10-05 of 22 December 2010 on fund mergers, master-feeder structures and notification procedures;
- CSSF Circular 11/498 of 10 January 2011 on entry into force of the Fund Law;
- CSSF Circular 11/508 of 15 April 2011 on the new provisions applicable to Luxembourg management companies subject to Chapter 15 of the Fund Law and to self-managed SICAVs;
- CSSF Circular 11/509 of 15 April 2011 on the new notification procedure to apply by a Luxembourg UCITS wanting to sell its shares in a different Member State and by a foreign UCITS wanting to sell its shares in Luxembourg;
- CSSF Circular 11/512 of 30 May 2011 presenting the main changes to the risk management regulation following publication of CSSF regulation 10-4 and the precisions brought by ESMA; providing some additional CSSF guidance on risk management rules; and defining format and contents of the RMP to communicate to CSSF;
- CESR Guidelines on a common definition of European money market funds of 19 May 2010 (CESR/10-049);
- CESR Guidelines on risk measurement and the calculation of global exposure and counterparty risk for UCITS dated 28 July 2010 (CESR/10-788);
- ESMA Guidelines on risk measurement and the calculation of global exposure for certain types of structured UCITS dated 14 April 2011 (ESMA 2011/112).

Quick Reference Guide

Investors

There is no limitation as to the type of investors in a UCITS fund. Originally created as a true retail product, UCITS funds are sold to the public but also to corporates and institutions. As UCITS funds may be easily marketed across the EU and beyond, investors originate from many parts of the world.

Eligible investments and investment restrictions

An overview of the eligible investments (and associated investment restrictions) is given below (all percentages are % of net assets, unless otherwise stated).

Global limits by type of assets

Type of assets	Article of Fund Law	Limits to be checked at sub-fund level
Transferable securities	Article 41 (1) a) to d)	100%
Money market instruments	Articles 41 (1) a) to d) and 41 (1) h)	100%
Bank deposits	Article 41 (1) f)	100%
UCITS	Article 41 (1) e)	100%
Other UCIs	Article 41 (1) e)	30%
Financial derivative instruments	Article 41 (1) g)	100%
Ancillary liquid assets	Article 41 (2)	49%

Individual limits by type of assets: diversification, counterparty and concentration limits

a. Individual and combined investment limits per security (article 43 of the Fund Law)

Type of instruments	Limits to be checked at sub-fund level		
Transferable securities	10% ¹	25%	35%(100%)
Money market instruments	10%	10%	35%(100%)
Bank deposits	20%	20%	/
OTC financial derivative instruments	5% / 10%	10%	/
Combined total exposure per issuer	Max 20% ²	Max 35%(100%) ²	Max 35%(100%)

¹ This limit of 10% per issuer may be of a maximum of 20% in the case of index funds i.e. UCITS that replicate passively the performance of a financial index.

² Limit to be checked at group level.

b. Individual and combined investment limits per security (article 46 of the Law)

Type of instruments	Limits to be checked at sub-fund level
Units of UCITS*	20%
Units of other UCI	20%

*Under article 181 (8) of the Fund Law, a sub-fund of a UCITS may hold units of other sub-funds of the same UCITS provided it meets the following requirements:

- The target sub-fund should not in turn invest its assets in the sub-fund which intends to hold its units;
- The target sub-fund should not hold, as per its prospectus or constitutive documents, more than 10% in aggregate of its assets in units of the target sub-funds of the same UCITS;
- Any potential voting rights attached to the units of the target sub-fund should be suspended during the holding period;
- For as long as the units are held by the UCI, their value will not be taken into consideration for the calculation of the net assets of the UCI for the purpose of verifying the minimum threshold of the net assets;
- No double taking of subscription/redemption fees or management fees at the level of the UCITS which intends to hold units of a target sub-fund of the same umbrella fund.

c. Permitted holding as a percentage of the securities in issue (article 48 of the Fund Law)

Type of instruments	Article of the Fund Law	Limits to be checked at sub-fund level
No-voting shares of the same issuer	Article 48 (2)	10%
Debt instruments of the same issuer		10%
Units/shares of the same UCITS/ other UCI		25%
Money market instruments of the same issuer		10%

Article 40 of the Fund Law foresees that each sub-fund of a UCITS with multiple sub-funds is considered as a distinct UCITS for the purpose of checking the investment restrictions of Chapter 5. As a result, in contrary to what was done under the previous regime, these concentration limits have to be checked at the level of each sub-fund and not at the level of the UCITS as a whole.

d. Other key limits

Other limits	Article of the Fund Law
UCITS are not allowed to grant loans or act as guarantor for third parties	Article 51 (1)
UCITS may borrow the equivalent of up to 10% of their assets provided that the borrowing is on a temporary basis	Article 50 (1)
UCITS may not acquire either precious metals or certificates representing them	Article 41 (2) c)

Master-feeder UCITS

The Fund Law allows master-feeder structures, where the master and the feeder may be established in the same Member State or in two different ones. These structures may be used for distribution purposes and to gain efficiencies through the pooling of assets.

Investment limits applicable to master feeder structures:

Limits/conditions	Article of the Fund Law
A feeder fund should invest at least 85% of its assets in units of a master fund	Article 77 (1)
A feeder fund should invest up to a maximum of 15% of its assets in: <ul style="list-style-type: none"> Ancillary liquid assets Financial derivative instruments used for hedging purposes Movable and immovable property which is essential for the direct pursuit of its business if the feeder fund is an investment company 	Article 77 (2)
The master fund should: <ul style="list-style-type: none"> Not be itself considered as a feeder fund Not hold units of a feeder fund Have at least one feeder fund among its unit holders 	Article 77 (3)
Articles 41, 43, 46 and 48 (2) third bullet do not apply to feeder funds	Article 77 (1)

Money Market Funds

CESR's "Guidelines on a common definition of European money market funds (CESR/10-049)" aim at improving investors' protection, who usually expect to preserve the principal of their investment while at retaining the ability to withdraw their capital on a daily basis. In this document, CESR makes a distinction between Short-Term Money Market Funds and Money Market Funds.

These guidelines will apply amongst others to any UCITS subject to Part I of Fund Law which label or market themselves as "money market funds". Money market funds that existed before 1 July 2011 are allowed a six month grand-fathering period to comply with these guidelines, in respect of all investment acquired prior to that date.

A money market fund must indicate in its prospectus and in its Key Investor Information Document ("KIID"), whether it is a Short-Term Money Market Fund or a Money Market Fund.

Short-Term Money Market Funds

To be considered as a Short-Term Money Market Fund, a UCITS must comply with the following criteria:

<i>Criteria</i>	<i>Short-term money market funds</i>
<i>Primary investment objective</i>	To maintain the principal of the fund and to provide a return in line with the money market rates
<i>Type of investments</i>	Money market instruments complying with the criteria defined in the Directive 2009/65/EC or deposits with credit institutions
<i>Quality of investments</i>	High quality securities (factors to be taken into account: credit quality, nature of the asset class, the operational and counterparty risk linked to structured financial instruments, liquidity profile)
<i>Securities with a residual maturity until redemption date</i>	Of less than or equal to 397 days (ABS with a residual maturity until the legal date of redemption of 5 years but with an expected maturity of 8 months would not be eligible anymore for Short-term money market funds)
<i>NAV and price calculation frequency</i>	Daily NAV and price calculation, daily subscription and redemption of units
<i>Weighted average maturity</i>	60 days
<i>Weighted average life</i>	120 days
<i>Direct and indirect exposure (via derivatives) to equities and commodities</i>	No
<i>Currency exposure</i>	Should be hedged
<i>Currency derivatives</i>	Only for hedging purposes
<i>Valuation approach</i>	Constant or stable NAV (amortised cost) and fluctuating or variable NAV (market value)
<i>Investment in other UCIs</i>	Permitted but only in short-term money market funds

Money Market Funds

To be considered as a Money Market Fund, a UCITS must comply with the following criteria:

<i>Criteria</i>	<i>Money market funds</i>
<i>Primary investment objective</i>	To maintain the principal of the fund and to provide a return in line with the money market rates
<i>Type of investments</i>	Money market instruments complying with the criteria defined in the Directive 2009/65/EC, deposits with credit institutions and sovereign issuance of at least investment grade quality
<i>Quality of investments</i>	High quality securities (factors to be taken into account: credit quality, nature of the asset class, the operational and counterparty risk linked to structured financial instruments, liquidity profile)
<i>Securities with a residual maturity until redemption date</i>	Of less than or equal to two years provided that the time remaining until the next interest rate reset date is less than or equal to 397 days
<i>NAV and price calculation frequency</i>	Daily NAV and price calculation, daily subscription and redemption of units
<i>Weighted average maturity</i>	Six months
<i>Weighted average life</i>	12 months
<i>Direct and indirect exposure (via derivatives) to equities and commodities</i>	No
<i>Currency exposure</i>	Should be hedged
<i>Currency derivatives</i>	Only for hedging purposes
<i>Valuation approach</i>	Fluctuating NAV
<i>Investment in other UCIs</i>	Permitted but only in short-term money market funds and money market funds

Luxembourg UCITS funds may, as from 1 July 2011, be set-up and managed by a UCITS management company located in a different EU Member State than the Grand Duchy. The description below regarding risk management, organisation requirements and procedures, etc. applies only to UCITS management companies and SIAGs located in Luxembourg.

Risk management

The Fund Law, the UCITS IV Directive and CESR's level 3 Guidelines on Risk Measurement of 28 July 2010 (CESR/10-788) harmonise the interpretation of the rules introduced under the old UCITS III regime. In addition, they impose a few new requirements in terms of reporting, disclosure and monitoring of risks such as the liquidity risk, operational risks, etc.

The major changes compared to the UCITS III framework are listed below:

- The “sophisticated funds” versus “non sophisticated funds” classification, which in the past determined the risk management approach, is now abandoned. Instead, the selection of the methodology used to calculate the global exposure is based on the risk profile of the UCITS, resulting from the complexity of the investment strategies or the use of exotic financial derivative instruments;
- The daily monitoring of the calculation of the global exposure is extended to UCITS using the commitment approach. It is even envisaged to carry out intra-day monitoring in particular conditions;
- CESR recommends an initial validation of the Value at Risk model (“VaR”) by a unit either internal or external to the UCITS;

- Reporting of back testing to the senior management should be done at least on a quarterly basis if the number of overshootings over the last year (250 business days) exceeds four. A similar reporting should be sent to the CSSF on a semi-annual basis when relevant;
- The calculation of the counterparty exposure of a UCITS is simplified. The positive mark-to-market value of over-the-counter financial derivatives is used to assess the UCITS' counterparty risk instead of using the 3 steps method.
- The UCITS should disclose in the prospectus the method used to calculate the global exposure, the expected level of leverage and the possibility of higher leverage levels. The expected level of leverage should be calculated as the sum of the notional of the financial derivative instruments used. For UCITS using a relative VaR, the reference portfolio should also be disclosed in the prospectus;
- The UCITS should disclose in the annual financial statements the reference benchmark, the level of leverage, the lowest, highest and average VaR utilisation of the year under review.

The recent CSSF Circular 11/512 of 30 May 2011 provides a detailed framework in which the risk management procedure has to be communicated to the CSSF and clarifies its format and content. It also details the CSSF approach towards certain rules relating to risk management.

Organisational requirements

Organisational requirements applicable to management companies have been detailed in CSSF Regulation n°10-4. UCITS IV management companies in Luxembourg are required to have sound administrative and accounting procedures, control and safeguard arrangements for electronic data processing and adequate internal control mechanisms. Management companies must also have the necessary and sufficient human and technical infrastructure in order to conduct its activities and to supervise the activities that can be delegated to third party service providers.

Senior management responsibility

People managing the management company must have the relevant experience for their duty and must be approved by the CSSF. Board members will take the ultimate responsibility for the entire activity. At least two conducting officers will control and take in charge the conduct of the day-to-day activity.

Internal control functions

Management companies must have permanent and independent internal control functions:

- Compliance function with one designated physical compliance officer;
- Risk management function;
- Internal audit.

The internal functions have to report to senior management at least annually and on an ad hoc basis if necessary.

These control functions can be externalised to qualified third parties according to the proportionality principle, i.e. when such derogation is appropriate and proportionate in view of the nature, scale and complexity of the management company's business.

Internal administrative procedures

Management companies are required to have a manual of procedures validated by the senior management. These procedures cover the following areas: remuneration policy, compliance, internal audit, personal dealings, record keeping and archiving, accounting procedures, business continuity plan, IT and security policy, recording of portfolio transactions, recording and processing of subscription and redemption orders, complaints handling, conflicts of interests management, exercise of voting rights, due diligence (inv. compliance) of investment portfolio, best execution, handling of orders, policies and procedures for preventing malpractices that might reasonably be expected to affect the stability and integrity of the market (market timing, churning), inducements.

Of course, depending on the size of the organisation, management companies in practice establish additional policies and procedures like for example for the creation, the update/ dissemination of internal procedures, human resources policy, outsourcing policy, monitoring of capital adequacy, governance policy including board functioning and composition rules, decision making and signature power guidance, etc.

Conduct of business rules

Management companies also have to take the necessary arrangements to act in the best interest of UCITS and investors (e.g. accurate asset valuation, market timing and late trading prevention, transparency and duty to prevent undue cost for investors, etc.).

Management companies have to ensure that client's orders will be properly handled and that adequate reporting on subscriptions and redemptions will be provided to investors. They must also ensure that the UCITS is provided with the best possible result for portfolio transactions e.g. best price, cheapest transaction cost, speed of execution, etc. (Best execution).

Financial resources

Management companies must have a minimum capital of EUR 125,000 plus additional own funds calculated as a percentage of the assets under management "AUM" (0.02% calculated on AUM over 250 Mio) with a cap at EUR 10 Mio. Management companies are authorised not to provide up to 50% of the additional amount of own funds referred to above if they benefit from a guarantee of the same amount given by a credit institution or an insurance undertaking.

Self-managed SICAV

SICAV which have not designated a management company have to comply with the same rules as management companies with some exceptions:

- Some administrative procedures are not required (as not really relevant);
- Self-managed SICAV do not have to have an internal compliance function and an internal auditor;
- Minimum capital requirements is EUR 300,000.

The proportionality principle can also be invoked by the SIAG. It is subject to the CSSF approval upon receipt of a duly motivated request.

UCITS main features at a glance

<i>Legal forms available for UCITS</i>	<ul style="list-style-type: none"> • Investment company with variable capital (SICAV) to be incorporated as a public limited company (S.A.); • Investment company with fixed capital (SICAF); • Contractual fund (FCP).
<i>Eligible investors</i>	<ul style="list-style-type: none"> • No restriction on the type of investors authorised to invest in a UCITS.
<i>Licensing requirements</i>	<p>A UCITS fund must receive the CSSF's prior authorisation before it can start its activities. The CSSF will pay particular attention to:</p> <ul style="list-style-type: none"> • The UCITS fund's draft constitutional documents (incl. its prospectus and, for new UCITS, its KIID); • The identity and quality of the sponsor of the UCITS funds; • The quality of the UCITS management company, if there is one; • The identity of the investment manager of the UCITS funds who must be duly licensed for that function in its country of domicile; • The identity of any other delegates or sub-delegates; • The identity of the managers in charge of conducting the business of the UCITS funds, who must show good reputation and adequate experience for acting in such capacity; • The identity of the central administration, of the Luxembourg depositary and of the Luxembourg external auditors; • The risk management put in place which has to cover all the UCITS managed by the management company and all the risks including liquidity and operational risks pertaining to these UCITS.
<i>Compulsory service providers in Luxembourg</i>	<ul style="list-style-type: none"> • Depositary – responsible for safekeeping of the UCITS assets and other supervisory duties – which must be a Luxembourg bank or a Luxembourg branch of a EU bank; • External auditors.
<i>Valuation principle</i>	<ul style="list-style-type: none"> • Valuation is made for officially listed securities on the basis of the last known stock exchange quotation. If it is not representative or for other securities, valuation is made based on the realisable value of the assets, estimated in good faith (unless differently provided for in the constitutional documents of UCITS).
<i>Minimum NAV frequency</i>	<ul style="list-style-type: none"> • Twice a month.
<i>Subscription/Redemption</i>	<ul style="list-style-type: none"> • Subscription at NAV plus subscription fees. A UCITS fund can be closed to subscriptions; • Redemption at NAV minus redemption fees. A UCITS fund must offer the ability to redeem to investors at least twice a month.
<i>Minimum capital requirement in the UCITS</i>	<ul style="list-style-type: none"> • EUR 1.25 Mio to be reached within six months following approval.
<i>Documents to be established according to laws and regulations</i>	<ul style="list-style-type: none"> • Prospectus; • Key Investor Information Document ("KIID"); • Articles of association (in case of a SICAV or SICAF); • Management regulations (in case of an FCP); • Agreements with the service providers; • Annual audited financial statements (annually within four months of period end); • Semi-annual non-audited financial statements (annually within two months of period end); • Long Form Report describing the organisation of the UCITS funds (annually within four months of period end); • Risk management process in accordance with the CSSF Circular 11/512 of 30 May 2011.

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Non-UCITS

Applicable legal framework

Luxembourg non-UCITS funds (“Part II” funds) are subject to the following main laws and regulations:

- Part II of the Law of 17 December 2010 on Undertakings for Collective Investment (“the Fund Law”);
- IML Circular 91/75 of 21 January 1991 clarifying certain aspects of the UCI legal framework;
- IML Circular 97/136 of 13 June 1997 on financial information to be provided by public funds;
- CSSF Circular 02/77 of 27 November 2002 on the protection of investors in case of NAV calculation error or breach of investment rules;
- CSSF Circular 02/80 of 5 December 2002 on the specific rules applicable to Luxembourg Part II funds pursuing alternative investment strategies;
- CSSF Circular 08/371 of 5 September 2008 regarding the electronic transmission of prospectuses and financial reports of UCIs and SIFs to the CSSF;
- CSSF Circular 11/498 of 10 January 2011 regarding the entry into force of the Law of 17 December 2010 relating to undertakings for collective investment.

Investors

Part II funds are open to the retail public in Luxembourg as well as to corporates or institutions. There is no limitation as to the type of investors. However, unlike UCITS, they do not have a European passport and hence cannot be freely marketed throughout the EU, once the CSSF has approved them. They are required to meet the specific conditions laid down by the regulatory authorities of the host countries in which they wish to market their shares or units.

Quick Reference Guide



Eligible investments and investment restrictions

Part II funds are required to invest their assets according to the principle of risk-spreading but are not restricted as to the type of assets they can acquire. The applicable risk-spreading requirements applicable to the funds are defined per investment strategy in various circulars:

<i>CSSF Circular 91/75 Chapter G</i>	Part II funds investing in transferable securities
<i>IML Circular 91/75 Chapter I.I.</i>	Part II funds investing in venture capital (*)
<i>IML Circular 91/75 Chapter I.II.</i>	Part II funds investing in futures contracts and options
<i>IML Circular 91/75 Chapter I.III.</i>	Part II funds investing in real estate (*)
<i>CSSF Circular 02/80</i>	Part II funds investing in alternative strategies (*)

The CSSF may grant exemptions from requirements in these circulars upon proper justification from the fund promoter.

The risk-spreading requirements applicable to the funds marked with a (*) are each detailed in a specific Quick Reference Guide. The risk-spreading requirements applicable to Part II funds investing in "traditional" transferable securities as well as to Part II funds of funds are detailed below.

Investment in transferable securities

<i>a) Investments in unlisted securities</i>	max. 10% of net assets
<i>b) Investments in securities of the same issuer</i>	max. 10% of net assets
<i>c) Acquisition of securities of the same kind of the same issuer</i>	max. 10% of the securities issued by the same issuer
<i>d) Borrowings</i>	max. 25% of net assets

Restrictions a), b) and c) are not applicable to securities issued or guaranteed by the OECD Member States, their local authorities or public international bodies with EU, regional or worldwide scope.

The 10% ceilings mentioned above can be increased up to 20% upon proper justification to the CSSF.

Investment in funds (Part II fund of funds)

<i>Investments in closed-ended funds</i>	Units of closed-ended funds are treated in the same way as other transferable securities and are therefore subject to the general rules applicable to transferable securities as mentioned above.
<i>Investments in open-ended funds</i>	Max. 20% of net assets unless the target open ended funds are subject to risk diversification requirements comparable to those applicable to a Part II fund, in which case the 20% restriction may not apply (case-by-case negotiation with the CSSF; master-feeder structures are even acceptable in certain cases). For the purpose of the application of this 20% ceiling, each compartment of a target fund is to be considered as a distinct fund provided that the principle of segregation of the commitments of the different compartments vis-à-vis third parties is ensured.
<i>Investments in securities issued by one or more compartments of the same fund</i>	Subject to the provisions of the management regulations, the constitutive documents and the prospectus, the target compartment may not invest more than 10% of its assets in units of other compartment of the same UCI, there is no duplication of the management/subscription or redemption fees and the value of the securities of the target compartment held by the UCI will not be taken into account for the calculation of the net assets of the UCI.

A Part II fund which principally invests in other funds must make sure that its portfolio of target funds presents liquidity features in line with the redemption provisions of the prospectus.

Organisational requirements

Part II funds are not required to have a substance and an organisation comparable to that of UCITS funds, nor is there any explicit requirement in the Law to have in place specific risk management processes. As the UCITS IV directive does not affect Part II funds, the CSSF may continue to require, for such vehicles, a promoter complying with certain financial surface and reputation requirements.

A Part II fund can only use asset managers which are duly regulated, supervised, with relevant experience, human and technical means to exercise their functions. The Fund Law provides that the depositary bank of a Part II fund cannot perform the function of asset management. Existing Part II funds have until 30 June 2012 to adapt their functioning to this new requirement.

If the Part II fund is set up as an FCP, it requires a management company, which can be subject to Chapter 16 of the Fund Law. It may also be set up by a UCITS Management Company situated in Luxembourg.

Part II funds main features at a glance

<i>Legal forms available</i>	<ul style="list-style-type: none">• Investment company with variable capital (SICAV) to be incorporated as a public limited company (S.A.);• Investment company with fixed capital (SICAF);• Contractual fund (FCP).
<i>Eligible investors</i>	No restrictions.
<i>Licensing requirements</i>	<p>A Part II UCI must receive CSSF's prior authorisation to start its activities. CSSF will pay particular attention to:</p> <ul style="list-style-type: none">• the Part II UCI's draft constitutional documents, notably the prospectus;• the identity of the promoter and of the persons in charge of conducting the business of the Part II UCI; they must show good reputation and adequate experience for acting in such capacity. The promoter must show good reputation, be a professional in the financial sector, be supervised in its country of residence and have sufficient financial resources;• the identity of the directors;• the identity of the investment manager of the Part II UCI, which must be authorised or registered for the purpose of asset management and subject to the prudential supervision of a regulatory authority;• the identity of the Luxembourg central administration, the Luxembourg depositary and the Luxembourg external auditors.
<i>Compulsory service providers in Luxembourg</i>	<ul style="list-style-type: none">• Depositary – responsible for safekeeping of the UCIs assets and certain other supervisory duties – which must be a Luxembourg bank or a Luxembourg branch of a foreign bank;• Central administration – responsible for accounting, NAV calculation, keeping of the register of the shareholders/unitholders, handling subscriptions and redemptions, communication with investors and preparation of financial statements – which must be a Luxembourg bank or a branch of a foreign bank or a professional of the financial sector with a proper license;• A Chapter 16 Management Company if the Part II fund is set up as an FCP;• External auditors.
<i>Minimum frequency of NAV calculation</i>	Monthly (in principle).

Part II funds main features at a glance (continued)

<i>Valuation principle</i>	Valuation is made for officially listed securities on the basis of the last known stock exchange quotation. If it is not representative or for other securities, valuation is made based on the realisable value of the assets, estimated in good faith (unless differently provided for in the constitutional documents of the fund).
<i>Subscription/ Redemption</i>	<ul style="list-style-type: none">• Subscription at NAV plus subscription fees. A Part II fund can be closed to subscriptions;• Redemption price must in practice be made at NAV minus redemption fees. A Part II fund can be closed to redemptions.
<i>Minimum capital requirement in the fund</i>	EUR 1,25 Mio to be reached within six months following approval.
<i>Documents to be established according to laws and regulations</i>	<ul style="list-style-type: none">• Prospectus;• Articles of association (in case of a SICAV or SICAF);• Management regulations (in case of an FCP);• Agreements with the service providers;• Annual audited financial statements (annually within four months of period end);• Semi-annual non audited financial statements (annually within two months of period end);• Long Form Report describing the organisation of the fund (annually within four months of period end).

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Specialised Investment Funds

Applicable legal framework

Luxembourg Specialised Investment Funds (SIFs) are subject to the following main laws of regulation:

- Law of 13 February 2007 on Specialised Investment Funds (“SIF Law”);
- CSSF Circular 07/283 of 28 February 2007 regarding entry into force of the law of 13 February 2007 relating to SIFs;
- CSSF Circular 07/309 of 3 August 2007 concerning risk diversification requirements applicable to SIFs;
- CSSF Circular 07/310 of 3 August 2007 regarding financial information to be provided by SIFs;
- CSSF Circular 08/371 of 5 September 2008 regarding the electronic transmission of prospectuses and financial reports of UCIs and SIFs to the CSSF;
- CSSF Circular 08/372 of 5 September 2008 regarding the guidelines for depositaries of SIFs adopting alternative investment strategies, where those funds use the services of a prime broker.

Investors

Only well-informed investors are authorised to invest in SIF. Well-informed investors are (i) institutional investors, i.e. regulated institutions active in the management of assets for their clients or themselves, (ii) professional investors within the meaning of Annex II to Directive 2004/39 on markets in financial instruments including notably large corporates, even unregulated ones and (iii) any other investor who meets the following conditions:

- He/she has confirmed in writing that he/she adheres to the status of well-informed investor, and;
- He/she invests a minimum of EUR 125,000 or has been the subject of an assessment by a credit institution, an investment firm or a UCITS management company certifying his expertise, experience and knowledge in adequately appraising an investment in the SIF.

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Eligible investments and investment restrictions

The range of eligible assets is unlimited: Private Equity, alternative strategies, Real Estate and commodities are just a few examples.

However, as for all kinds of UCIs, the risk diversification requirement applies. The SIF Law itself does not define any detailed investment limits or leverage rules. The CSSF has published general guidelines for the risk diversification requirements applicable for SIFs in the Circular CSSF 07/309:

- In principle, a SIF may not invest more than 30% of its assets or commitments to subscribe securities of the same type issued by the same issuer. However, this restriction does not apply to (i) investments in securities issued or guaranteed by an OECD Member State or its regional or local authorities or by EU, regional or global supranational institutions and bodies and to (ii) investments in target UCIs that are subject to risk-spreading requirements at least comparable to those applicable to SIFs;
- Short sales may not in principle result in a SIF holding a short position in securities of the same type, issued by the same issuer and representing more than 30% of its assets.
- When using financial derivative instruments, a SIF must ensure, via appropriate diversification of the underlying assets, a similar level of risk-spreading. Similarly, the counterparty risk in an OTC transaction must, when applicable, be limited having regard to the quality and qualification of the counterparty.

The CSSF states expressly in its circular that it may grant exemptions upon appropriate justification. Moreover, in case of specific investment policies, additional investment restrictions may be required.

Launch process of a SIF

Unlike funds submitted to the Fund Law, where prior approval by the CSSF is always required, SIFs may start their activities without such prior approval. The application for approval must however be filed with the CSSF within a month following the creation of the SIF, in order to then be posted on the official list of approved funds in Luxembourg. Thus, time-to-market for SIFs may be significantly reduced compared to traditional funds.

Organisational and administrative requirements

The directors of a SIF need to be authorised by the CSSF. They must be of high repute and have sufficient experience in relation to the type of SIF being created.

The custody of the SIF assets must be entrusted to a Luxembourg depositary bank, i.e. a credit institution which has its registered office in Luxembourg or which is the Luxembourg branch of a bank with registered office in another EU member state. The depositary bank has a lightened role compared to depositaries of Luxembourg public distributed funds. It is not legally required to perform supervisory and control functions e.g. regarding the NAV calculation, the issue, repurchase, cancellation of units, the timely remittance of consideration regarding the fund's assets, the compliance with investment restrictions, etc.

While making use of derivatives or adopting alternative investment strategies, a SIF may also use the services of a prime broker in accordance with market practice. According to CSSF Circular 08/372, the depositary of a SIF must approve the prime broker chosen by the SIF and must be in a position to obtain information from the prime broker on the composition and value of the SIF assets entrusted to it. If the depositary deems the prime broker to no longer be able to fulfil its supervisory tasks in relation with the SIF's assets, the depositary has the right to intervene in the relationship.

The central administration of a SIF must be situated in Luxembourg, but, it can obviously use external service providers. Finally, the SIF needs to appoint a Luxembourg-based authorised external auditor.

Legislative developments – the future of SIF

Since its entry into force in 2007 the SIF Law has clearly demonstrated that it enables tailored solutions responding to the industry's needs. There was a demand for a vehicle which is regulated but at the same time flexible, open to a wide, clearly defined range of investors. The increase in respect of numbers of SIFs and their assets under management demonstrates the high acceptance by the market players.

To ensure its future success, the Luxembourg regulator is currently analysing the options to readjust some provisions of the SIF Law, taking into consideration the economic and legislative developments and practical experiences of the last years. An as of yet unofficial draft law is currently under discussion: the amendments it will introduce to the SIF Law concern mainly the licensing process of a SIF (with a prior, yet swift, approval by the CSSF), the quality of its delegates (notably the portfolio manager), the introduction of a risk management process. These changes to the current regime purport essentially to give the CSSF the necessary tools to perform its supervisory role over the SIFs, while preserving their flexibility.

Moreover, the SIF framework will be heavily affected by the Alternative Fund Managers Directive (“AIFMD”), a European directive adopted in 2011 and to be transposed into national law within two years of entering into force. It aims at regulating and harmonising the European investment fund sector currently not covered by UCITS. Luxembourg SIFs will be clearly in scope of this new European regulation. Even if it is too early to analyse in detail the future amendments of the SIF Law, it seems clear that this new regulation will have a massive impact not only on the SIF Law but also on the functioning of SIF and the currently used business models.

SIF main features at a glance

<i>Legal forms available for SIFs</i>	<ul style="list-style-type: none"> Investment company with variable capital (SICAV), to be incorporated as a public limited company (S.A.), a private limited company (S.à r.l.), a cooperative company organised as a public limited company (SCoopSA) or as a corporate partnership limited by shares (SCA); Investment company with fixed capital (SICAF); Contractual fund (FCP).
<i>Eligible investors</i>	Well-informed investors only.
<i>Type of securities that a SIF may issue to investors, for financing purposes</i>	<ul style="list-style-type: none"> Shares/Units; “Parts bénéficiaires”; Debt.
<i>Licensing requirements</i>	<p>A SIF may start operations without receiving CSSF’s prior clearance, but must file an application for approval within one month following its creation. The CSSF will pay particular attention to:</p> <ul style="list-style-type: none"> the SIF draft constitutional documents (incl. offering document); the identity of the persons in charge of conducting the business of the SIF. They must show good reputation and adequate experience for acting in such capacity; the identity of the Luxembourg central administration, the Luxembourg depositary and the Luxembourg external auditors.
<i>Compulsory service providers in Luxembourg</i>	<ul style="list-style-type: none"> Depositary – responsible for safekeeping of the SIF assets – which must be a Luxembourg bank or a Luxembourg branch of a EU bank; Central administration – responsible for accounting, NAV calculation, keeping of the register of the shareholders/unitholders, handling with subscriptions and redemptions, communication with investors and preparation of financial statements – which must be a Luxembourg bank or a branch of a foreign bank or a professional of the financial sector with a proper license;
	<ul style="list-style-type: none"> A Chapter 16 Management Company if the SIF is set up as an FCP;
	<ul style="list-style-type: none"> External auditors.
<i>Minimum NAV frequency</i>	<ul style="list-style-type: none"> Yearly.
<i>Valuation of assets</i>	<ul style="list-style-type: none"> Fair value unless otherwise stated in the SIF documentation.
<i>Subscription/Redemption</i>	<ul style="list-style-type: none"> Subscriptions and redemptions must be carried out in accordance with the rules laid down in the SIF constitutional documents (i.e. not necessarily linked to the NAV); Partly paid-up shares may be issued.
<i>Minimum capital requirement in the SIF</i>	EUR 1.25 Mio to be reached within 12 months following the authorisation.
<i>Documents to be established according to laws and regulations</i>	<ul style="list-style-type: none"> Offering document; Articles of association (in case of a SICAV or SICAF); Management regulations (in case of an FCP); Agreements with the service providers; Annual audited financial statements (annually within six months of period end).

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Hedge funds

Applicable legal framework

Hedge funds may be created either as Part II funds, SIFs or even as Part I funds (“Alternative UCITS”).

Public funds : UCITS (“Part I” funds) and non-UCITS (“Part II” funds):

- Law of 17 December, 2010 on Undertaking for Collective Investment (the “Fund Law”);
- IML Circular 91/75 of 21 January 1991 clarifying certain aspects of the UCI legal framework;
- IML Circular 97/136 of 13 June 1997 on financial information to be provided by public funds;
- CSSF Circular 02/77 of 27 November 2002 on the protection of investors in case of NAV calculation error or breach of investment rules;
- CSSF Circular 02/80 of 5 December 2002 which details specific rules applicable to Luxembourg Part II funds pursuing alternative investment strategies (applies to Part II funds only);
- CSSF Circular 07/308 of 2 August 2007 on the use of derivatives and management of financial risks (applies to Part I funds only and only until 1 July 2011);
- Grand Ducal decree of 8 February 2008 transposing Directive 2007/16/EC which clarifies certain definitions in the UCITS III Directive (applies to Part I funds only);
- CSSF Circular 08/356 of 4 June 2008 on the use of securities lending, “réméré” and repo transactions (applies to Part I funds only);
- CSSF Circular 08/371 of 5 September 2008 on the electronic transmission of prospectuses and financial reports of UCIs and SIFs to the CSSF;

- CSSF Circular 08/380 of 26 November 2008 on the guidelines of the Committee of European Securities Regulators (CESR) concerning eligible assets for investment by UCITS (applies to Part I funds only);
- CSSF Regulation N° 10-04 of 22 December 2010 on organisational requirements, conflicts of interest, conduct of business, risk management and content of agreement between a depositary and a management company (applies to Part I funds only);
- CSSF Regulation N° 10-05 of 22 December 2010 on fund mergers, master-feeder structures and notification procedures (applies to Part I funds only);
- CSSF Circular 11/498 of 10 January 2011 on entry into force of the Fund Law;
- CSSF Circular 11/508 of 15 April 2011 on the new provisions applicable to Luxembourg management companies subject to Chapter 15 of the Fund Law and to self-managed SICAVs (applies to Part I funds only);
- CSSF Circular 11/509 of 15 April 2011 on the new notification procedure to apply by a Luxembourg UCITS wanting to sell its shares in a different Member State and by a foreign UCITS wanting to sell its shares in Luxembourg (applies to Part I funds only);
- CSSF Circular 11/512 of 30 May 2011 presenting the main changes to the risk management regulation following publication of CSSF regulation 10-4 and the precisions brought by ESMA; providing some additional CSSF guidance on risk management rules; and defining format and contents of the RMP to communicate to CSSF (applies to Part I funds only, as from 1 July 2011);
- CESR Guidelines on a common definition of European money market funds of 19 May 2010 (CESR/10-049) (applies to Part I funds only);
- CESR Guidelines on risk measurement and the calculation of global exposure and counterparty risk for UCITS dated 28 July 2010 (CESR/10-788) (applies to Part I funds only);
- ESMA Guidelines on risk measurement and the calculation of global exposure for certain types of structured UCITS dated 14 April 2011 (ESMA 2011/112) (applies to Part I funds only).

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Funds dedicated to well-informed investors (“SIFs”):

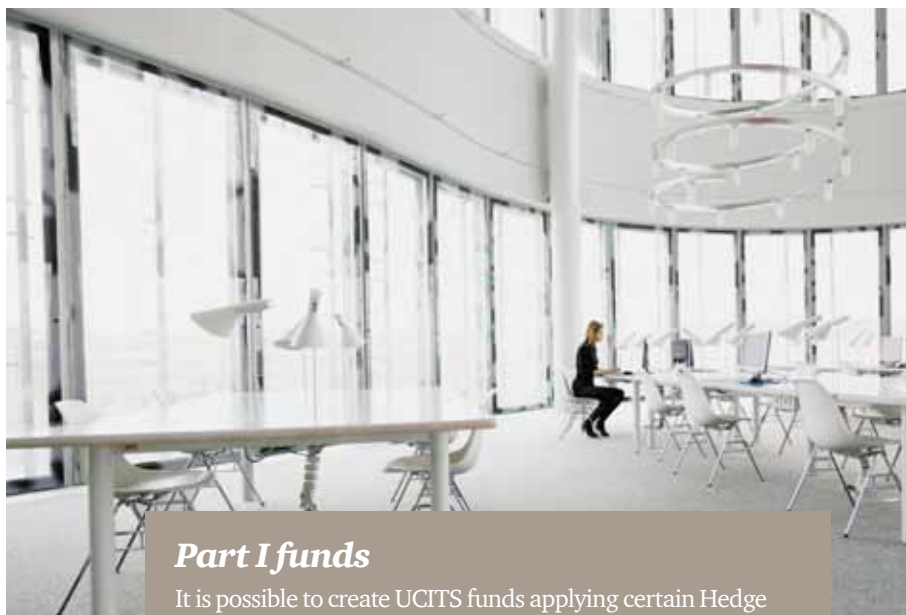
- Law of 13 February 2007 on Specialised Investment Funds (SIFs);
- CSSF Circular 07/283 of 28 February 2007 regarding entry into force of the law of 13 February 2007 relating to SIFs;
- CSSF Circular 07/309 of 3 August 2007 concerning risk diversification requirements applicable to SIFs;
- CSSF Circular 07/310 of 3 August 2007 regarding financial information to be provided by SIFs;
- CSSF Circular 08/371 of 5 September 2008 on the electronic transmission of prospectuses and financial reports of UCIs and SIFs to the CSSF;
- CSSF Circular 08/372 of 5 September 2008 on the guidelines for depositaries of SIFs adopting alternative investment strategies, where those funds use the services of a prime broker.

Eligible investments, investment restrictions and valuation requirements

Investors

If the Hedge fund is created under the provisions of the Fund Law, there is no restriction as to the type of investors.

If however, the fund is a SIF, only well-informed investors will be allowed to invest in it. For further details on the “well-informed investors” definition, please refer to the SIF Quick Reference Guide of this brochure.



Part I funds

It is possible to create UCITS funds applying certain Hedge fund techniques. Through derivatives such as futures, Contracts for Difference (“CFD”) or swaps on indices, managers can invest in asset classes otherwise not eligible within UCITS, and pursue strategies such as arbitrage, macro, CTA strategies with complex drivers of risk and reward.

Part II funds

The range of investments eligible for Part II funds is not limited: all types of alternative strategies are, from an eligibility of assets point of view, acceptable. Circular 02/80 has defined the investment restrictions applicable to Part II funds pursuing alternative strategies; they are summarised in the table below. The Circular is flexible enough to allow investment managers to achieve their investment objectives through the use of borrowings and short selling or with derivatives or a combination of both.

Within the Part II framework, all known Hedge fund strategies can, and have been, deployed.

SIFs

Similar to Part II funds, the range of investments eligible for SIFs are not limited: all types of alternative strategies are, from an eligibility of assets point of view, acceptable. There is no circular defining the limits specifically applying to SIFs pursuing Hedge fund techniques; the restrictions in the CSSF Circular 07/309 are generic (which leaves greater room for agreeing specific restriction features with the CSSF) and, clearly, provide for even more flexibility than in a Part II fund as shown in the table in the opposite table.

Eligible investments, investment restrictions and valuation requirements

	<i>Part I funds</i>	<i>Part II funds</i>	<i>SIF</i>
<i>Restrictions on long positions in securities</i>	Max. 10% of the fund's net assets in one issuer.	Max. 20% of the fund's gross assets in one issuer.	Max. 30% of the fund's gross assets in one issuer.
	A fund cannot buy more than 10% of the securities issued by any one issuer.	A fund cannot buy more than 10% of the securities issued by any one issuer.	No limitation in this respect indicated in the Circular 07/309.
	Max. 10% of the fund's net assets in unquoted securities.	Max. 10% of the fund's gross assets in unquoted securities.	No limitation in this respect.
<i>Restrictions on short selling of securities</i>	Short selling is prohibited (but the use of derivatives may allow equivalent economic results. For example, contracts for differences (CFD) may be shorted).	<ul style="list-style-type: none"> • Sales proceeds from short selling applicable to any issuer cannot exceed max. 10% of the fund's gross assets; • Stop loss limit when short sale results in an unrealised loss representing 5% of the fund's gross assets (does not apply for market neutral or relative value strategies). 	Max. 30% of the fund's gross assets exposed to one issuer.
		A fund cannot sell more than 10% of the securities issued by any one issuer.	No limitation in this respect indicated in the Circular 07/309.
<i>Restrictions on borrowings</i>	Borrowing for investment purposes is prohibited (but the use of derivatives may allow equivalent economic results).	<ul style="list-style-type: none"> • Max. 200% of the fund's net assets (for directional strategies); • Max. 400% of the fund's net assets (for market neutral or relative value strategies for which short positions are covered by long positions); • The CSSF has always been opened to discussions if additional borrowing is needed. 	No limitation in this respect indicated in the Circular 07/309.
<i>Derivatives</i>	<ul style="list-style-type: none"> • Global exposure (incl. embedded derivatives) cannot exceed 100% of the fund's net assets; • Counterparty risk (by counterparty) on OTC derivatives of max. 5% or 10% (according to quality of the counterparty) of the fund's net assets; • The fund may not combine investments in transferable securities (incl. indirect exposure), money market instruments, deposits and OTC derivatives with a single body in excess of 20% of the fund's net assets. 	<ul style="list-style-type: none"> • For derivatives admitted to trading on a regulated market, margin deposits on any one position cannot exceed 5% of the fund's gross assets; • For OTC derivatives, any unrealised loss on any position cannot exceed 5% of the fund's gross assets; • Total margin deposits and/or total unrealised loss for OTC derivatives cannot exceed 50% of the fund's gross assets; • Premiums paid on options are taken into account in the 5% and the 50% limits above-described. 	<ul style="list-style-type: none"> • Diversification level similar to the restrictions on long positions in securities; • Such limit may also apply to the counterparty of the OTC derivative depending on the quality and qualification of the counterparty.
<i>Broker</i>	N/A.	The value of the assets transferred to the prime broker cannot exceed the debt of the fund to the prime broker by 20% of the fund's gross assets.	No limitation in this respect indicated in the Circular 07/309; limitation applied by the CSSF will probably depend upon the quality and qualification of the prime broker.

Note that, because these investment restrictions are, as regards to Part II funds and SIFs, laid down in CSSF circulars, they may in certain cases be derogated upon proper justification vis-à-vis the CSSF.

Hedge funds main features at a glance

Provided below are the main characteristics of Alternative UCITS, Part II funds and SIFs.

	Part I funds	Part II funds	SIF
Legal forms available	<ul style="list-style-type: none"> Investment company with variable capital (SICAV) to be incorporated as a public limited company (S.A.); Investment company with fixed capital (SICAF); Contractual fund (FCP). 	<ul style="list-style-type: none"> Investment company with variable capital (SICAV) to be incorporated as a public limited company (S.A.); Investment company with fixed capital (SICAF); Contractual fund (FCP). 	<ul style="list-style-type: none"> Investment company with variable capital, to be incorporated as a public limited company (S.A.), a private limited company (S.à r.l.), a cooperative company organised as a public limited company (SCoopSA) or as a corporate partnership limited by shares (SCA); Investment company with fixed capital (SICAF); Contractual fund (FCP).
Eligible investors	No restriction on the type of investors authorised to invest in a UCITS.	No restriction.	Well-informed investors only, i.e. institutional investors, professional investors and other investors provided that they formally declare themselves as well-informed investors and either invest a minimum of EUR 125,000 or obtain a certificate from a regulated entity confirming their understanding of the risks associated to the investment in a SIF.
Licensing requirements	<p>A UCITS fund must receive the CSSF's prior authorisation before it can start its activities. The CSSF will pay particular attention to:</p> <ul style="list-style-type: none"> The UCITS fund's draft constitutional documents (incl. its prospectus and for new UCITS, its KIID); The identity and quality of the sponsor of the UCITS fund; The quality of the UCITS management company, if there is one; The identity of the investment manager of the UCITS fund who must be duly licensed for that function in its country of domicile; The identity of any other delegates or sub-delegates; The identity of the managers in charge of conducting the business of the UCITS fund. They must show good reputation and adequate experience for acting in such capacity; The identity of the central administration, of the Luxembourg depository and of the Luxembourg external auditors; The risk management put in place, which has to cover all the UCITS managed by the management and all the risks incl. liquidity and operational risks pertaining to these UCITS. 	<p>A Part II UCI must receive CSSF's prior authorisation to start its activities. The CSSF will pay particular attention to:</p> <ul style="list-style-type: none"> The Part II UCI's draft constitutional documents, notably the prospectus; The identity of the sponsor and of the persons in charge of conducting the business of the Part II UCI; they must show good reputation, and adequate experience for acting in such capacity; The identity of the directors; The identity of the investment manager of the Part II UCI, which must be authorised or registered for the purpose of asset management and subject to the prudential supervision of a regulatory authority; The identity of the Luxembourg central administration, the Luxembourg depository and the Luxembourg external auditors. 	<p>A SIF may start operations without receiving the CSSF's prior clearance but must file an application for approval within one month following its creation. The CSSF will pay particular attention to:</p> <ul style="list-style-type: none"> The SIF draft constitutional documents (incl. offering document); The identity of the persons in charge of conducting the business of the SIF. They must show good reputation and adequate experience for acting in such capacity; The identity of the Luxembourg central administration, the Luxembourg depository and the Luxembourg external auditors. <p>Under the current regime, SIFs do not require a promoter identified as such to the CSSF nor are they required to use a duly regulated investment manager.</p>

Hedge funds main features at a glance (continued)

	<i>Part I funds</i>	<i>Part II funds</i>	<i>SIF</i>
<i>Compulsory service providers in Luxembourg</i>	<ul style="list-style-type: none"> • Depositary – responsible for safekeeping of the UCITS assets and other supervisory duties – which must be a Luxembourg bank or a Luxembourg branch of a EU bank; • External auditors. 	<ul style="list-style-type: none"> • Depositary – responsible for safekeeping of the UCIs assets and certain other supervisory duties – which must be a Luxembourg bank or a Luxembourg branch of a foreign bank; • Central administration – responsible for accounting, NAV calculation, keeping of the register of the shareholders/unitholders, handling subscriptions and redemptions, communication with investors and preparation of financial statements – which must be a Luxembourg bank or a branch of a foreign bank or a professional of the financial sector with a proper license; • A Chapter 16 Management Company if the Part II fund is set up as an FCP; • External auditors. 	<ul style="list-style-type: none"> • Depositary – responsible for safekeeping of the SIF assets – which must be a Luxembourg bank or a Luxembourg branch of a EU bank; • Central administration – responsible for accounting, NAV calculation, keeping of the register of the shareholders/unitholders, handling with subscriptions and redemptions, communication with investors and preparation of financial statements – which must be a Luxembourg bank or a branch of a foreign bank or a professional of the financial sector with a proper license; • A Chapter 16 Management Company if the SIF is set up as an FCP; • External auditors.
<i>Minimum frequency of NAV calculation</i>	Twice a month.	Monthly (in principle).	Yearly.
<i>Valuation principle</i>	Valuation is made for officially listed securities on the basis of the last known stock exchange quotation. If it is not representative or for other securities, valuation is made based on the realisable value of the assets, estimated in good faith (unless differently provided for in the constitutional documents of the UCITS).	Valuation is made for officially listed securities on the basis of the last known stock exchange quotation. If it is not representative or for other securities, valuation is made based on the realisable value of the assets, estimated in good faith (unless differently provided for in the constitutional documents of the fund).	Fair value, unless otherwise stated in the SIF documentation.
<i>Subscription/Redemption</i>	<ul style="list-style-type: none"> • Subscription at NAV plus subscription fees. A UCITS fund can be closed to subscriptions; • Redemption at NAV minus redemption fees. A UCITS fund must offer the ability to redeem to investors at least twice a month. 	<ul style="list-style-type: none"> • Subscription at NAV plus subscription fees. A Part II fund can be closed to subscriptions; • Redemption price must in practice be made at NAV minus redemption fees. A Part II fund can be closed to redemptions. 	<ul style="list-style-type: none"> • Subscriptions and redemptions must be carried out in accordance with the rules laid down in the SIF constitutional documents (i.e. not necessarily linked to the NAV); • Partly paid-up shares may be issued.
<i>Minimum capital requirement in the fund</i>	EUR 1.25 Mio to be reached within six months following approval.	EUR 1,25 Mio to be reached within six months following approval.	EUR 1.25 Mio to be reached within 12 months following the authorisation.
<i>Documents to be established according to laws and regulations</i>	<ul style="list-style-type: none"> • Prospectus; • Key Investor Information Document (“KIID”); • Articles of association (in case of a SICAV or SICAF); • Management regulations (in case of an FCP); • Agreements with the service providers; • Annual audited financial statements (annually within four months of period end); • Semi-annual non-audited financial statements (annually within two months of period end); • Long Form Report describing the organisation of the UCITS funds (annually within four months of period end); • Risk management process in accordance with the CSSF Circular 11/512 of 30 May 2011. 	<ul style="list-style-type: none"> • Prospectus; • Articles of association (in case of a SICAV or SICAF); • Management regulations (in case of an FCP); • Agreements with the service providers; • Annual audited financial statements (annually within four months of period end); • Semi-annual non audited financial statements (annually within two months of period end); • Long Form Report describing the organisation of the fund (annually within four months of period end). 	<ul style="list-style-type: none"> • Offering document; • Articles of association (in case of a SICAV or SICAF); • Management regulations (in case of an FCP); • Agreements with the service providers; • Annual audited financial statements (annually within six months of period end).



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Real Estate funds

Applicable legal framework

Real Estate funds¹ must be created either as a Part II fund of the Fund Law or as a SIF. The choice of one or the other depends on the type of investor targeted as well as the flexibility sought in terms of diversification and running of the fund.

Public funds: Non-UCITS (“Part II” funds)

- Part II of the Law of 17 December 2010 on Undertakings for Collective Investment (“the Fund Law”);
- IML Circular 91/75 of 21 January 1991 clarifying certain aspects of the UCI legislative framework (Chapter I lays down specific rules applying to Part II funds investing in Real Estate assets);
- IML Circular 97/1 36 of 13 June 1997 on financial information to be provided by public funds;
- CSSF Circular 02/77 of 27 November 2002 on the protection of investors in case of NAV calculation error or breach of investments rules;
- CSSF Circular 08/371 of 5 September 2008 regarding the electronic transmission of prospectuses and financial reports of UCIs and SIFs to the CSSF;
- CSSF Circular 11/498 of 10 January 2011 on entry into force of the Fund Law.

Investors

If the Real Estate fund is created under the provisions of Part II of the Fund Law, there is no restriction as to the type of investors. If however, the fund is a SIF, only well-informed investors will be allowed to invest in it. For further details on the “well-informed investors” definition, please refer to the SIF Quick Reference Guide of this brochure.

Funds dedicated to well-informed investors (“SIFs”):

- Law of 13 February 2007 on Specialised Investment Funds (SIFs);
- CSSF Circular 07/283 of 28 February 2007 regarding entry into force of the law of 13 February 2007 relating to SIFs;
- CSSF Circular 07/309 of 3 August 2007 concerning risk diversification requirements applicable to SIFs;
- CSSF Circular 07/310 of 3 August 2007 regarding financial information to be provided by SIFs;
- CSSF Circular 08/371 of 5 September 2008 on the electronic transmission of prospectuses and financial reports of UCIs and SIFs to the CSSF.

¹ REITS funds or funds investing in Real Estate assets that are securitised may be created as UCITS.

Eligible investments, investment restrictions and valuation requirements

The range of investments eligible for Part II funds and SIFs is not limited: all types of Real Estate assets and Real Estate related assets are eligible.

The investment restrictions, depending on whether one considers Part II funds or SIFs investing in Real Estate assets, can be summarised as follows:

	<i>Part II funds</i>	<i>SIF</i>
<i>Maximum investment in one property²</i>	20% of fund/sub-fund's net assets.	30% of the fund/sub-fund's gross assets.
<i>Maximum leverage</i>	Borrowings may not exceed 50% of the valuation of all properties in the fund.	No maximum foreseen by regulation but the CSSF checks that the maximum leverage indicated in the prospectus is acceptable.
<i>Minimum liquid assets in the fund</i>	No minimum foreseen by regulation but the fund's liquidity features must be in line with sections dealing with investors' ability to redeem in the prospectus.	No minimum foreseen by regulation but the fund's liquidity features must be in line with sections dealing with investors' ability to redeem in the prospectus.

Because these investment restrictions are laid down in the CSSF circulars, they may in certain cases be derogated subject to proper justification vis-à-vis the Commission.

Part II funds and SIFs have to comply with the following valuation requirements:

	<i>Part II funds</i>	<i>SIF</i>
<i>Minimum frequency of NAV calculation</i>	Once a year and each time shares or units are issued to, or redeemed from, investors.	Once a year.
<i>Valuation principles</i>	Valuation is made based on the realisable value of the Real Estate assets, estimated in good faith (unless differently provided for in the constitutional documents of the fund).	Fair value unless derogated in the fund constitutional documents (prospectus).
<i>Requirement for independent valuation of the properties</i>	Yes, at least annually and each time properties are bought or sold. Valuation to be performed by recognised professionals in the Real Estate sector.	No.

² As per Chapter I of Circular 91/75 of 21 January 1991 applicable to Part II funds, this restriction (i) is not applicable during the start up phase of the fund, which may not extend beyond a four-year period following the closing date of the initial offer period and (ii) is to be considered at the date of acquisition of the real estate property. Regulations on SIFs are silent on these matters; this must consequently be agreed with the CSSF on a case-by-case basis.

Real Estate funds main features at a glance

	Part II funds	SIF
Legal forms available	<ul style="list-style-type: none"> Investment company with variable capital (SICAV) to be incorporated as a public limited company (S.A.); Investment company with fixed capital (SICAF); Contractual fund (FCP). 	<ul style="list-style-type: none"> Investment company with variable capital, to be incorporated as a public limited company (S.A.), a private limited company (S.à r.l.), a cooperative company organised as a public limited company (SCoopSA) or as a corporate partnership limited by shares (SCA); Investment company with fixed capital (SICAF); Contractual fund (FCP).
Eligible investors	No restriction on the type of investors authorised to invest in a Part II fund.	Well-informed investors only, i.e. institutional investors, professional investors and other investors provided that they formally declare themselves as well-informed investors and either invest a minimum of EUR 125,000 or obtain a certificate from a regulated entity confirming their understanding of the risks associated to the investment in a SIF.
Licensing requirements	<p>Part II funds must receive the CSSF's prior authorisation before it can start its activities. The CSSF will pay particular attention to:</p> <ul style="list-style-type: none"> The fund's draft constitutional documents, notably the prospectus; The identity of the promoter of the fund, which must be a professional in the financial sector and must have sufficient financial surface; The identity of the investment manager of the fund which must be duly licensed for that function in its country of domicile; The identity of the persons in charge of conducting the business of the fund; they must show good reputation and adequate experience for acting in such capacity; The identity of the Luxembourg central administration, the Luxembourg depositary and the Luxembourg external auditors. 	
	<p>A SIF may start operations without receiving the CSSF's prior clearance but must file an application for approval within one month following its creation. SIFs do not require a promoter identified to the CSSF nor do they need a duly regulated investment manager.</p>	
Compulsory service providers in Luxembourg	<ul style="list-style-type: none"> Depositary: responsible for safekeeping of the UCI assets and certain other supervisory duties – must be a Luxembourg bank or Luxembourg branch of a foreign bank. 	<ul style="list-style-type: none"> Depositary: responsible for safekeeping of the SIF assets – must be a Luxembourg bank or the Luxembourg branch of a EU bank.
	<ul style="list-style-type: none"> Central administration – responsible for accounting, NAV calculation, keeping of the register of the shareholders/unitholders, handling with subscriptions and redemptions, communication with investors and preparation of financial statements – which must be a Luxembourg bank or a branch of a foreign bank or a professional of the financial sector with a proper license; 	
	<ul style="list-style-type: none"> A Chapter 16 Management Company if the Part II or the SIF is set up as an FCP; 	
	<ul style="list-style-type: none"> External auditors. 	

Real Estate funds main features at a glance (continued)

	Part II funds	SIF
Subscription/ Redemption	<ul style="list-style-type: none"> • Subscription at NAV plus subscription fees. A Part II fund can be closed to subscriptions; • Redemption price must in practice be made at NAV minus redemption fees. A Part II fund can be closed to redemptions. 	<ul style="list-style-type: none"> • Subscription price can be freely determined in the offering document. A SIF can be closed to subscriptions; • Redemption price can be freely determined in the offering document. A SIF can be closed to redemptions.
Minimum capital requirement	EUR 1.25 Mio to be reached within six months following approval.	EUR 1.25 Mio to be reached within 12 months following approval.
Documents to be established according to laws and regulations	<ul style="list-style-type: none"> • Prospectus; • Articles of association (in case of a SICAV or SICAF); • Management regulations (in case of an FCP); • Agreements with the service providers; • Annual audited financial statements (annually within four months of period end); • Semi-annual non audited financial statements (annually within two months of period end); • Long Form Report describing the organisation of the fund (annually within four months of period end). 	<ul style="list-style-type: none"> • Offering document; • Articles of association (in case of a SICAV or SICAF); • Management regulations (in case of an FCP); • Agreements with the service providers; • Annual audited financial statements (annually within six months of period end).

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Private Equity funds

Quick Reference Guide



Applicable legal framework

Private Equity funds may be created either as SIFs, SICARs or Part II funds of the Fund Law. The choice of the appropriate vehicle depends on the type of investor targeted, the type of investment as well as the flexibility sought in terms of diversification and operation of the fund.

Funds dedicated to well-informed investors (“SIF”)

- Law of 13 February 2007 on Specialised Investment Funds (“SIF Law”);
- CSSF Circular 07/283 of 28 February 2007 regarding entry into force of the law of 13 February 2007 relating to SIFs;
- CSSF Circular 07/309 of 3 August 2007 concerning risk diversification requirements applicable to SIFs;
- CSSF Circular 07/310 of 3 August 2007 regarding financial information to be provided by SIFs;
- CSSF Circular 08/371 of 5 September 2008 regarding the electronic transmission of prospectuses and financial reports of UCIs and SIFs to the CSSF.

Investment Company in Risk Capital (“SICAR”)

- Law of 15 June 2004 on SICARs, as amended;
- CSSF Circular 06/241 of 5 April 2006 on the concept of risk capital in SICARs;
- CSSF Circular 06/272 of 21 December 2006 on technical specifications regarding the communication to the CSSF, under the law on prospectuses for securities, of documents for approval or for filing and of notices for offers to the public of securities issued by SICARs and admissions of securities issued by SICARs to trading on a regulated market;
- CSSF Circular 08/376 of 23 October 2008 regarding financial information to be submitted to the CSSF by SICARs.

SICARs, since they are not subject to the principle of risk diversification, are technically **not** investment funds.

Public funds: Non-UCITS (“Part II” funds)

- Part II of the Law of 17 December 2010 on Undertakings for Collective Investment (“the Fund Law”);
- IML Circular 91/75 of 21 January 1991 clarifying certain aspects of the UCI legislative framework (Chapter I lays down specific rules applying to Part II funds investing in Private Equity and venture capital);
- IML Circular 97/136 of 13 June 1997 on financial information to be provided by public funds;

- CSSF Circular 02/77 of 27 November 2002 on the protection of investors in case of NAV calculation error or breach of investment rules;
- CSSF Circular 08/371 of 5 September 2008 regarding the electronic transmission of prospectuses and financial reports of UCIs and SIFs to the CSSF;
- CSSF Circular 11/498 of 10 January 2011 regarding the entry into force of the law of 17 December 2010 on UCIs.

Investors

If the Private Equity fund is created under the provisions of Part II of the Fund Law, there is no restriction as to the type of investors. If the fund is a SIF or a SICAR, only well-informed investors will be allowed to invest in it. For further details on the “well-informed investors” definition, please refer to the SIF Quick Reference Guide of this brochure.

Eligible investments, investment restrictions and valuation requirements

Unlike SICARs, which are only permitted to invest in risk capital, the range of investments eligible for Part II funds and SIFs is not limited: all types of Private Equity assets are eligible.

The investment restrictions, depending on whether one considers SIFs, SICARs or Part II funds investing in Private Equity assets, can be summarised as follows:

	SICAR	SIF	Part II funds
Maximum investment in one target	SICARs are not submitted to risk spreading obligations. SICAR may invest in only one or several targets.	30% of the fund/sub-fund’s gross assets.	20% of fund/sub-fund’s net assets in any one company.
Maximum leverage	No maximum cap foreseen by regulation but the CSSF checks that the maximum leverage indicated in the prospectus is acceptable.		
Minimum liquid assets in the fund	No minimum cap foreseen by regulation but the fund’s liquidity features must be in line with sections dealing with investors’ ability to redeem in the prospectus.		

Note that, because these investment restrictions are laid down in CSSF circulars, they may in certain cases be derogated upon proper justification vis-à-vis the Commission.

SIFs, SICARs, Part II funds must also comply with the following valuation requirements:

	SICAR	SIF	Part II funds
Minimum frequency of NAV calculation	Once a year.	Once a year.	Once a month (but derogation may be obtained).
Valuation principle	Fair value.	Fair value unless derogated in the fund constitutional documents.	Valuation is made for officially listed securities on the basis of the last known stock exchange quotation. If it is not representative or for other securities, valuation is made based on the realisable value of the assets, estimated in good faith (unless differently provided for in the constitutional documents).
Requirement for independent valuation of the assets	No.	No.	No.

Private Equity funds main features at a glance

	SIF and SICAR	Part II funds
Eligible Investors	Well-informed investors only, i.e. institutional investors, professional investors and other investors provided that they formally declare themselves as well-informed investors and either invest a minimum of EUR 125,000 or obtain a certificate from a regulated entity confirming their understanding of the risks associated to the investment in a SIF/SICAR.	No restriction on the type of investor authorised to invest in a Part II fund. (Min. subscription amount of EUR 12,500.)
Licensing requirements	<p>Part II funds and SICARs must receive the CSSF's prior authorisation before they can start their activities. The CSSF will pay particular attention to:</p> <ul style="list-style-type: none"> • The fund draft constitutional documents, notably the prospectus; • The identity of the promoter of the fund, which must be a professional in the financial sector and must have sufficient financial surface; • The identity of the investment manager of the fund which must be duly licensed for that function in its country of domicile; • The identity of the persons in charge of conducting the business of the fund; they must show good reputation and adequate experience for acting in such capacity; • The identity of the Luxembourg central administration, the Luxembourg depositary and the Luxembourg external auditors. <p>In addition, for SICARs, CSSF requires a business plan with a risk analysis as well as a description of the governance structure.</p> <p>A SIF may start operations without receiving the CSSF prior clearance but must file an application for approval within one month following its creation. SIFs do not require a promoter identified to the CSSF nor do they need a duly regulated investment manager.</p>	
Compulsory service providers in Luxembourg	<ul style="list-style-type: none"> • Depositary: responsible for safekeeping of the SIF and SICAR assets – must be a Luxembourg bank or the Luxembourg branch of a EU bank. 	<ul style="list-style-type: none"> • Depositary: responsible for safekeeping of the fund assets and certain other supervisory duties – must be a Luxembourg bank or the Luxembourg branch of a foreign bank.
	<ul style="list-style-type: none"> • Central administration – responsible for accounting, NAV calculation, keeping of the register of the shareholders/unitholders, handling with subscriptions and redemptions, communication with investors and preparation of financial statements – which must be a Luxembourg bank or a branch of a foreign bank or a professional of the financial sector with a proper license. 	
	<ul style="list-style-type: none"> • A Chapter 16 Management Company if the Part II fund or the SIF is set up as an FCP. SICARs cannot be set up as FCPs. 	
	<ul style="list-style-type: none"> • External auditors. 	
Subscription/Redemption	<ul style="list-style-type: none"> • Subscription price can be freely determined in the offering documents. A SIF or SICAR can be closed to subscriptions; • Redemption price can be freely determined in the offering documents. A SIF or SICAR can be closed to redemptions. 	<ul style="list-style-type: none"> • Subscription at NAV plus subscription fees. A Part II fund can be closed to subscriptions; • Redemption price must in practice be made at NAV minus redemption fees. A Part II fund can be closed to redemptions.

Private Equity funds main features at a glance (continued)

	SIF and SICAR	Part II funds
Minimum capital requirement	EUR 1.25 Mio for SIF and 1 Mio for SICAR to be reached within 12 months following approval.	EUR 1.25 Mio to be reached within six months following approval.
Documents to be established according to laws and regulations	<ul style="list-style-type: none">• Offering document;• Articles of association (in case of a SICAV or SICAF);• Management regulations (in case of an FCP) – a SICAR can only take a corporate form;• Agreements with the service providers;• Annual audited financial statements (annually within six months of period end);• Filing of financial statements with trade Registry within seven months of period end (for SICAR only).	<ul style="list-style-type: none">• Prospectus;• Articles of association (in case of a SICAV or SICAF);• Management regulations (in case of an FCP);• Agreements with the service providers;• Annual audited financial statements (annually within four months of period end);• Semi-annual non-audited financial statements (annually within two months);• Long Form Report describing the organisation of the fund (annually within four months of period end).

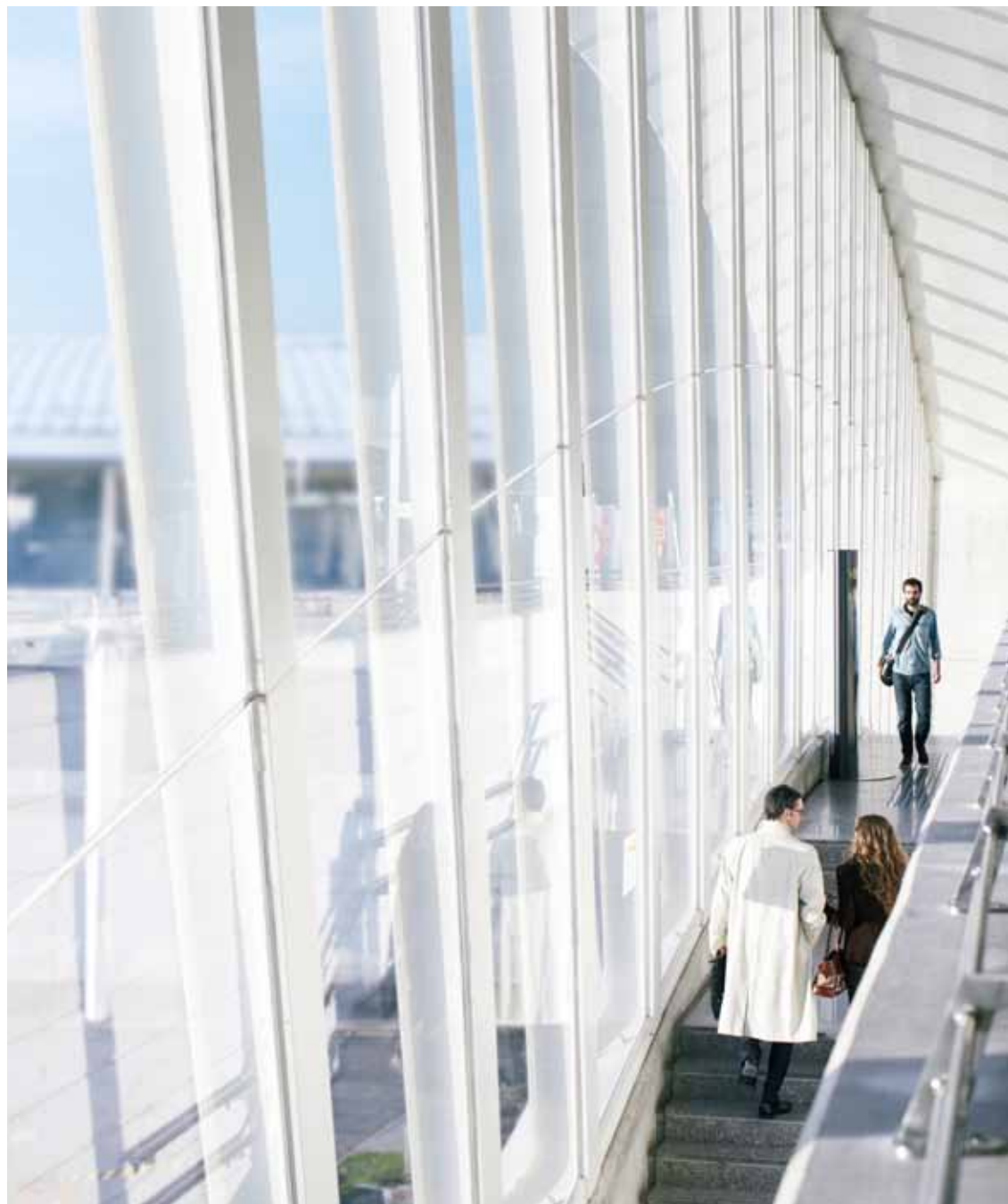
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UCITS IV - Management Company regulation

Quick Reference Guide



CSSF Regulation n° 10.4 of 20 December 2010 transposing implementing Directive 2010/43/EU regarding management companies

CSSF Circular 11/508 of 15 April 2011 on new provisions applicable to UCITS management companies and self-managed SICAVs

<i>Chapter I & II - Organisation, administrative procedures and control mechanisms</i>	<i>Article Reg 10-4</i>	<i>Appl. to SIAG?</i>
Subject matter, scope and definitions	1, 2, 3	✓
General requirements on procedures and organization	5	- *
Resources	6	-
Complaints handling	7	✓**
Electronic data processing	8	-
Accounting procedures	9	-
Control by senior management and supervisory function (oversight on delegated activity)	10	-
Permanent compliance, internal audit and risk management functions	11, 12, 13	✓ (RM)
Personal transactions	14	-
Recording of portfolio transactions	15	-
Recording of subscription and redemption orders	16	-
Recordkeeping requirements	17	-
<i>Chapter III - Conflict of interests</i>		
Criteria for the identification of conflicts of interest	19	✓
Conflicts of interest policy	20	✓
Independence in conflicts management	21	✓
Management of activities giving rise to detrimental conflict of interest	22	✓
Strategies for the exercise of voting rights	23	✓
<i>Chapter IV - Rules of conduct</i>		
Duty to act in the best interests of UCITS and their unit-holders	25	✓
Due diligence requirements	26	✓
Reporting obligations in respect of execution of subscription and redemption orders	27	✓
Execution of decisions to deal on behalf of the managed UCITS	28	✓
Placing orders to deal on behalf of UCITS with other entities for execution	29	✓
Handling of orders - General principles	30	✓
Aggregation and allocation of trading orders	31	✓
Safeguarding the best interests of UCITS (Inducements)	33	✓
<i>Chapter V - The standard agreement between a depositary and a management company</i>		
Elements related to the procedures to be followed by the parties to the agreement	34	-
Elements related to the exchange of information and to obligations on confidentiality and money-laundering	35	-
Elements related to the appointment of third parties	36	-
Elements related to potential amendments and the termination of the agreement	37	-
Applicable law	38	-
Electronic transmission of information	39	-
Scope of the agreement	40	-
Service level agreement	41	-
<i>Chapter VI - Risk management</i>		
Risk management policy (incl. connections with KIID)	43	✓
Assessment, monitoring and review of risk management policy	44	✓
Measurement and management of risk	45	✓
Calculation of global exposure	46	✓
Commitment approach	47	✓
Counterparty risk and issuer concentration	48	✓
Procedures for the assessment of the value of OTC derivatives	49	✓
Reports on derivative instruments	50	✓

* CSSF Regulation n° 10.4 has not transposed the recital of Directive 2010/43/EU and notably recital 5 : "[...] administrative procedures and internal control mechanism should, as a matter of good practice, apply both to management companies and investment companies that have not designated a management company, taking into account the principle of proportionality."

** Even if not mentioned in CSSF Regulation n° 10-4, CSSF Circular 11/508 of 15 April 2011 imposes SIAGs to have in place a complaints handling procedure and to designate a person responsible for such handling.

UCITS IV - Key Investor Information Document (“KIID”)

The UCITS IV Directive provides for the replacement of the simplified prospectus by the KIID. This change is probably one of the most important challenges for the cross-border UCITS industry over the last decade. While UCITS funds existing in Luxembourg as at 30 June 2011 benefit from a grandfathering period of one year to switch from simplified prospectus to KIID, new UCITS structures created on or after 1 July 2011 need to create their KIID right away.

Quick Reference Guide

Background

The Simplified Prospectus failed to bring into the UCITS world increased comparability and transparency regarding the core characteristics of investment funds. It is seen as a much too technical document, varying in length and content from promoter to promoter. The regulators’ response was therefore to replace the Simplified Prospectus with a simpler and hopefully more engaging document, easier to understand and digest by the common retail investor.

As the European Commission’s intention is to enforce tighter rules regarding investor protection for the whole spectrum of the investment products, the KIID might also be used as a first standard for all future retail investor communication regarding Packaged Retail Investment Products (“PRIIPs”).



Scope of the KIID

The KIID is designed as a concise document delivering critical information about the fund. It must be drafted in plain language and be easily understood by investors.

The Management Company of the fund is responsible for the production of the KIID and for making it readily available “upon request” at the point of sale, while the distributors or the investment advisers will have the obligation to deliver the KIID prior to any sale – it is in essence a pre-contractual document. All parties over the fund distribution value chain will have to identify the most pragmatic way to ensure KIID updates are properly provided to the entities responsible to deliver it. Web technologies and documentation management tools will probably be used and developed to absorb the huge increase of fund documents to be disseminated (130 000 KIIDs just for Luxembourg).

Core requirements

The KIID has to provide information at share-class level. However, some asset managers have decided to combine several share-classes in one KIID or to opt for one share-class KIID that represents fairly the other share-classes. The strategy here depends on the number of share-classes, their characteristics or asset manager’s distribution needs.

The document must be delivered to the investors either in a paper format or via a “durable” medium, easily replicable on paper. Although investors may choose another format than paper (electronic) or specifically consent to receive KIID via a website, they have the right to ask for a paper copy. KIIDs have to be delivered to EU Member States resident investors in their language and translation into local language is binding vis-à-vis the investors. Both the original and translated versions must be in “plain language”.

Regulated two pages format

The format and length of the KIID will be highly standardised. It will not be more than two pages long (except for structured funds, where three pages are acceptable) and the capacity of promoters to bring their personal touch will be limited to the narrative sections and perhaps a small, unobtrusive company logo.

The KIID will therefore be comparable across a wide range of funds.

CESR's template for the Key Investor Information Document (CESR/10-1321 of 20 December 2010):

1. Objectives and investment policy

2. Synthetic Risk and Reward Profile

Key Investor Information

This document provides you with key investor information about this fund. It is not marketing material. The information is required by law to help you understand the nature and the risks of investing in this fund. You are advised to read it so you can make an informed decision about whether to invest.

123 Fund, a sub-fund of ABC Fund SICAV (ISIN: 4321)
The fund is managed by ABC Fund Managers Ltd, part of the XYZ group of companies

Objectives and Investment Policy

Joint description of the objectives and policy of the UCITS in plain language (it is suggested not to copy-out the prospectus)

Essential features of the product which a typical investor should know:

- main categories of eligible financial instruments that are the object of investment
- a statement that the investor may redeem units on demand, and how frequently units are dealt in
- whether the UCITS has a particular target in relation to any industrial, geographic or other market sectors or specific classes of assets
- whether discretionary choices regarding particular investments are allowed, and whether the fund refers to a benchmark and if so which one
- a statement of whether any income arising from the fund is distributed or reinvested

Other information if relevant, such as:

- what type of debt securities the UCITS invests in
- information regarding any pre-determined pay off and the factors expected to determine performance
- if choice of assets is guided by growth, value or high dividends
- how use of hedging / arbitrage / leverage techniques may determine the fund's performance
- that portfolio transaction costs will have a material impact on performance
- minimum recommended holding term

Risk and Reward Profile

Lower risk
Tends to lower rewards

Higher risk
Tends to higher rewards

1 2 3 4 5 6 7

Narrative explanation of the indicator and its main limitations:

- Historical data may not be a reliable indication for the future
- Risk category shown is not guaranteed and may shift over time
- The lowest category does not mean “risk free”
- Why the fund is in its specific category
- Details of nature, timing and extent of any capital guarantee or protection

Narrative presentation of risks materially relevant to the fund which are not adequately captured by the indicator:

- Credit risk, where a significant level of investment is made in debt securities
- Liquidity risk, where a significant level of investment is made in financial instruments that are likely to have a low level of liquidity in some circumstances
- Counterparty risk, where a fund is backed by a guarantee from, or has material investment exposure through contracts with, a third party
- Operational risks including safekeeping of assets
- Impact of any techniques such as derivative contracts

Charges for this Fund

The charges you pay are used to pay the costs of running the fund, including the costs of marketing and distributing it. These charges reduce the potential growth of your investment.

One-off charges taken before or after you invest

Entry charge [2%]

Exit charge [0%]

This is the maximum that might be taken out of your money (before it is invested/before the proceeds of your investment are paid out)

Charges taken from the fund over a year

Ongoing charges [0%]

Charges taken from the fund under certain specific conditions

Performance [1% a year of any returns the fund achieves above the benchmark for these fees. (insert name of benchmark)]

The entry and exit charges shown are maximum figures. In some cases you might pay less - you can find this out from your financial adviser.

The ongoing charges figure is based on expenses for the year ending []. This figure may vary from year to year. It excludes:

- Performance fees
- Portfolio transaction costs, except in the case of an entry/exit charge paid by the UCITS when buying or selling units in another collective investment undertaking.

For more information about charges, please [see pages x to x / section x] of the fund's prospectus, which is available at www.abcfundprospectus

Past Performance

The chart will be supplemented with prominent statements which:

- warn about its limited value as a guide to future performance
- indicate briefly which charges have been included or excluded
- state the year when the fund started to issue units
- indicate the currency in which past performance has been calculated.

10%	
7.5%	
5%	
2.5%	
0%	
-2.5%	
-5%	
-7.5%	
-10%	

2001 2002 2003 2004 2005 2006 2007 2008 2009 2010

Practical Information

- Name of the depository
- Where and how to obtain further information about the UCITS (prospectus, reports & accounts)
- Where and how to obtain other practical information (e.g. where to find latest unit prices)
- A statement that tax legislation of the fund's Home State may have an impact on the personal tax position of the investor
- A statement that (Name of management company) may be held liable solely on the basis of any statement contained in this document that is misleading, inaccurate or inconsistent with the relevant parts of the prospectus for the fund
- Specific information relating to umbrella funds (e.g. any switching rights between sub-funds)
- Information about other share classes, if applicable (N) may be based on a representative class

This fund is authorised in [name of Member State] and regulated by [identity of competent authority].
[Name of management company] is authorised in [name of Member state] and regulated by [identity of competent authority].

This key investor information is accurate as at [the date of publication].

3. Charges

4. Past performance

5. Practical information

The KIID will be divided into five sections, each of them with specific requirements:

1. Objectives and investment policy

- Space limited description of objectives and the investment policy;
- Main targeted investments, benchmark, dividends distribution, holding period;
- Plain language, no technical jargon;
- Consistency with prospectus.

2. Synthetic Risk and Reward Profile

- Synthetic risk and reward indicator – SRRRI (calculation methodology based on fund classification – principally based on fund historical volatility);
- Disclaimers on SRRRI limitations;
- Other relevant risks not captured by SRRRI.

3. Charges

- Entry/exit fees;
- Ongoing charges (replaces Total Expense Ratio (TER)) - ex-post calculation based on a standardised methodology provided by CESR;
- Performance fee.

4. Past performance

- Calendar year past performance;
- Bar chart showing ten or five years;
- Benchmark comparison.

5. Practical information

- Depositary bank, law applicable to the fund, where to find additional information, etc.;
- No country specific information.

Main operational and business implications

Content accuracy and consistency with prospectus

Avoiding inconsistencies with the prospectus (which might generate civil liability) will be challenging for UCITS funds using complex hedging or arbitrage strategies, which cannot be easily explained in a few non-technical words. New processes should be put in place to facilitate the calculation and monitoring of the SRRRI and the ongoing charges figure.

Revision of the KIID

The KIID must be updated as frequently as needed in order to preserve its accuracy. The KIID must be updated as the SRRRI and the charges change during the year and annual figures have to be updated 35 business days after the end of the calendar year. Therefore, the integration of KIID update process with current investor information maintenance (prospectus, investors' notices, regulator approval) is likely to create an important coordination challenge.

Impact on product range

Since the KIID should facilitate comparison between products, there may be an increased need to monitor competition. This would allow both the product range and costs to be adapted to market levels.

Impact on distribution

Promoters have to look into how the KIID is going to disrupt distribution settings and if this will require an overhaul of fee arrangements and remuneration schemes. Promoters will have to find effective ways to streamline their distribution flow and ensure that distributors have easy access to the documents and that they are knowledgeable about their responsibilities towards investors.



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UCITS IV - Cross-border notification of UCITS

From July 2011 the recast UCITS Directive (“UCITS IV”) introduces a new notification procedure for UCITS intending to market cross-border into other EU Member States.

Quick Reference Guide



Background

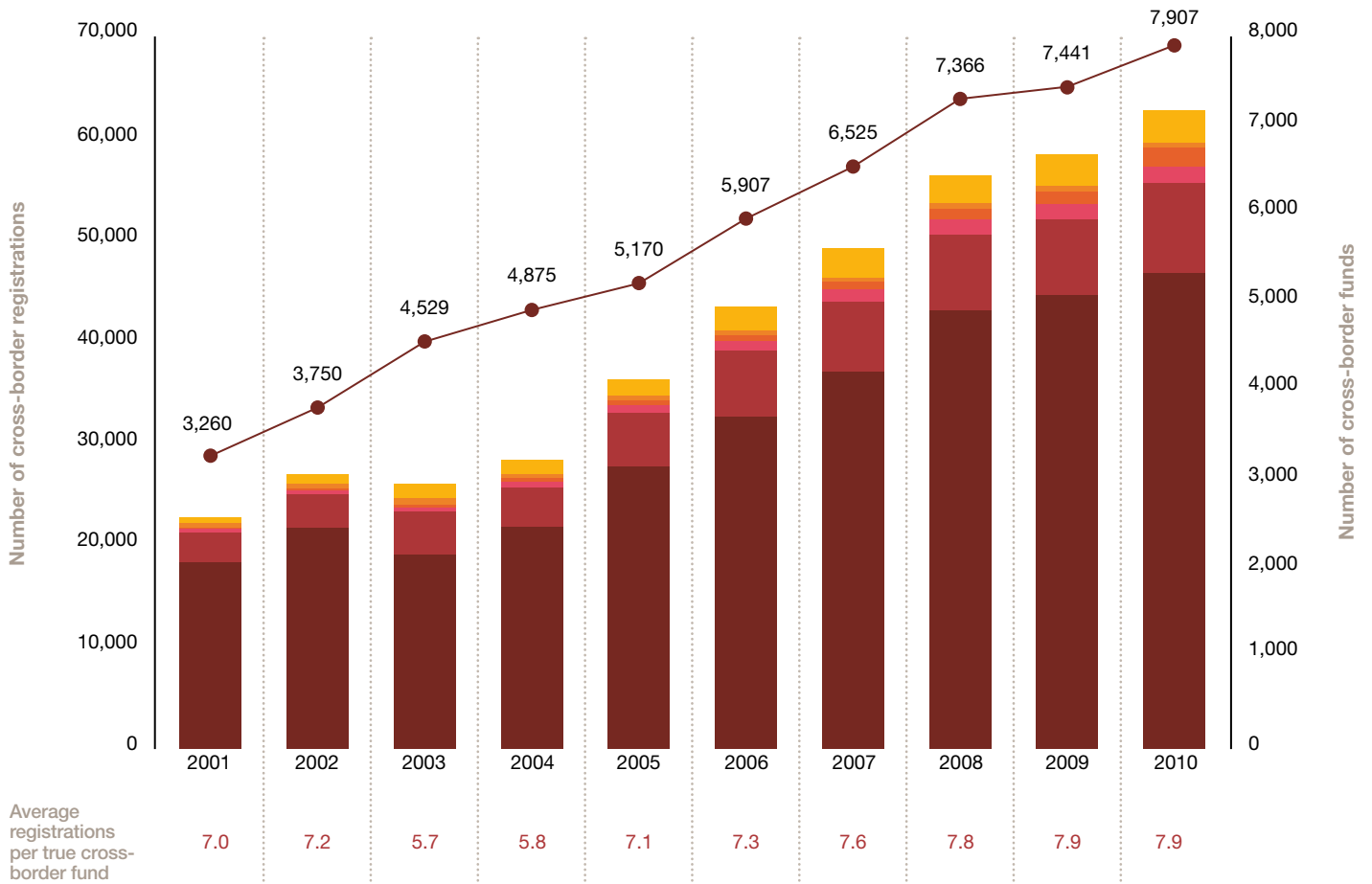
The last few years have seen a heavy focus on cross-border UCITS activities as an increasing number of asset managers have broadened their distribution strategies outside of their domestic environment. This trend has been assisted by the previous UCITS Directive (“UCITS III Directive”), together with the 2006 CESR notification guidelines, as demonstrated in the table below.

UCITS IV introduces standardised rules to follow by firms which intend to market their UCITS on a cross-border basis within the EU and will hence provide quicker market access than what is currently the case.

Underpinning the new notification procedure is the electronic transfer of standardised documentation between authorities in a short period of time before marketing can start.

The new procedure significantly shifts the ability of host EU country authorities to review documents or information pertaining to local marketing arrangements by the foreign UCITS after the beginning of marketing rather than before.

Number of cross-border funds and registrations



Average registrations per true cross-border fund

Source: Lipper Hindsight and PwC analysis, 31 December 2010

Note: Only true cross-border funds were taken into account - i.e. funds distributed in at least 3 countries including their domicile.

Funds Domicile:

- Luxembourg
- Ireland
- United Kingdom
- France
- Germany
- Other
- Number of cross-border funds

New notification procedures

The new notification (or registration as it is often referred to) procedure which permits cross-border marketing will involve a UCITS-to-home-regulator communication rather than UCITS-to-host-regulator. The home regulator will then transmit, within ten working days, a standardised notification file prepared by the UCITS, or its representative, to the host regulator. Normally, the host regulator has five working days to confirm the file is

complete. The home regulator transmission and confirmation thereof to the UCITS will trigger the right to start marketing in that host EU country without review by the host regulator. However, it is important to note that host regulators can review local marketing information after distribution has started.

Moreover, the new notification process is not as efficient or as harmonised as expected. The UCITS must continue to provide, where required, bespoke information concerning its local marketing arrangements in each EU Member State.

Indeed, once marketing begins, the process by which notification documentation must be kept up to date (including arrangements for local marketing) reverts to a UCITS-to-host-regulator, as is currently the case. So while speed to market will be improved, the overall level of simplification and reduction in administrative burden will be more modest.

Information and communication

Unfortunately, UCITS IV does not regulate the marketing activities of foreign UCITS in host Member States. As a compromise, host Member States must publish, presumably in English, details of their regulations and administrative provisions specifically related to the marketing arrangements of foreign UCITS in their jurisdiction. How much detail they will provide and the benefit this will be to market participants remains an open question.

Moreover, host Member States must be provided access to a website containing the documents required in the initial notification as well as any subsequent update of these documents. As under the current rule, it will remain the responsibility of the UCITS to keep this documentation up-to-date and provide the host regulators with details of any update by electronic means.

Translations

Under UCITS IV, only the Key Investor Information Document (“KIID”) is required to be translated into a language approved by the host Member State regulator. Other fund documents may be provided in English. However, commercial considerations will override this and we predict that many, maybe even the majority, of cross-border UCITS (especially those sold to retail investors in key markets) will continue to also translate the main prospectus and financial statements.

Contents of the notification letter

The form and to some extent, content of the notification letter to be submitted together with the UCITS attestation for cross-border notification has been standardised. Part A of the letter contains specific UCITS related information. Part B, which has been expanded, covers the various non-harmonised marketing requirements specific to each host Member State. At this stage we expect all of these local marketing rules to remain as UCITS IV starts.

Electronic transmission of notification files

Member State regulators must accept transmission and filing of notification documents by email. Upon sending of the notification email including the UCITS documentation, the home regulator must inform the UCITS of such transmissions. The host regulator is then required to confirm receipt/completeness of the notification file within five working days. The home regulator must ensure that the transmission of the complete documentation to the host regulator has taken place before it notifies the UCITS about its transmission.

Main operational and business implications

While the new notification procedure will improve speed to market, it does not go far enough and fails to fully harmonise the process within the EU. The notification process will remain overtly complex and cumbersome. There is no harmonisation of local marketing rules on cross-border UCITS, the new rules contain differing processes (involving different stakeholders), depending on what is trying to be achieved by the UCITS and, finally, host regulators will continue to review certain fund related information after marketing starts and subscriptions taken, meaning commercial risks remain.

Moreover, a myriad of other business implications and issues to consider and/or resolve remain, and some include:

- Can you rely on the information made publicly available by the Member States and what if the information provided is not fully up-to-date nor clear and precise?
- Your fund will remain responsible to ensure the notification file is complete before sending it to the home Member State regulator;
- A UCITS must ensure its marketing documents are in line with all host Member State local marketing requirements before finalising the notification file and sending it to the home regulator - how will you ensure this is the case?
- A UCITS must use the standard notification letter and ensure that Part B (non-harmonised requirements) are in line with host Member States requirements. Since information included in Part B will be different depending on each host Member State's requirements, there will be one specific file per country where the UCITS intends to be registered for distribution to the public;
- The new notification process will reduce time to market to ten days but should your marketing start before the five-day period in which host regulators confirm that the notification file is complete – is this extra delay an appropriate trade-off to obtain additional comfort?
- The new translation requirements will reduce the costs for UCITS, unless the commercial imperatives (including local distributors) continue to prefer translated versions to investors;
- UCITS will need to ensure they comply with local marketing laws, regulations and provisions applicable in host Member States to avoid ex-post sanctions by host regulators and regulation issues;
- What level of ex-post control will Member States actually impose and will local marketing rules be further expanded and made more complex?
- How will the marketing of UCITS in a host Member State be impacted in cases where the ex-post controls discover the UCITS is not in compliance with local requirements, especially in circumstances where subscriptions have been accepted?

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UCITS IV - Master-feeder structures

Master-feeder structures enable strategies in view of pooling funds' assets and achieving economies of scales. The use of such structures in Luxembourg was always possible for Part II funds or SIFs, but was prohibited for UCITS funds. This changes with UCITS IV and the introduction of rules regarding master-feeder structures into the UCITS framework.

Quick Reference Guide

Master-feeder in a nutshell

In a master-feeder structure, the feeder is the “collection fund” in the target distribution country in which retail and/or institutional investors may be allowed to invest. The feeder invests the cash received from its own investors in the master, becoming its unitholder.

UCITS IV master-feeder structures

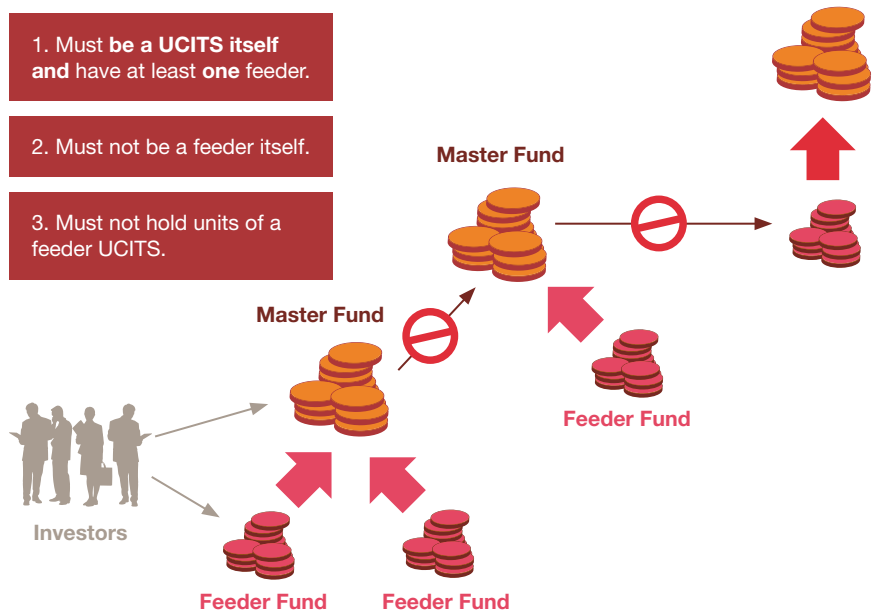
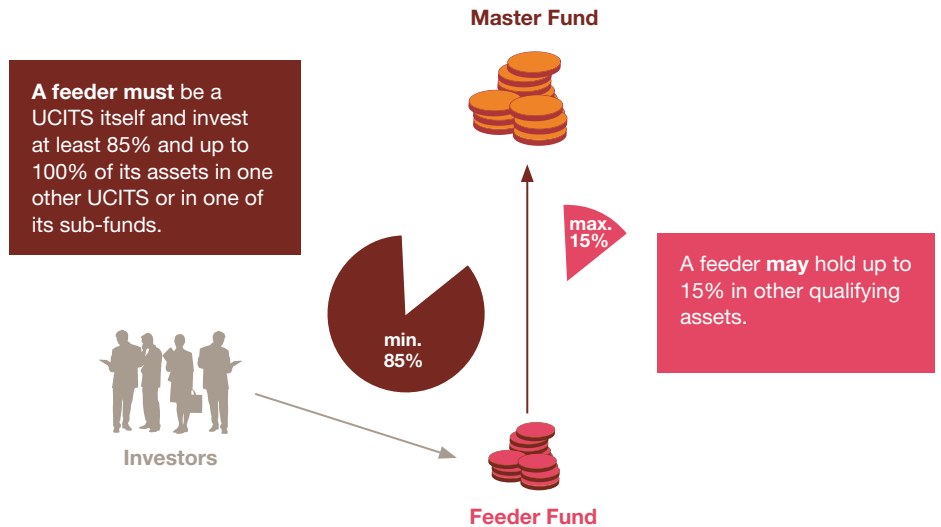
Any UCITS (FCP or SICAV/SICAF) or any investment compartment thereof is permitted to adopt a master-feeder investment policy. A feeder UCITS derogates, by law, from the usual UCITS diversification limits in order to be allowed to invest up to 100% of its assets in only one target UCITS. However, UCITS master-feeder structures are only allowed between European-domiciled coordinated UCITS, meaning that both the feeder and the master must be subject to the European UCITS Directive. At the level of the master UCITS, besides the feeder's investment, other investors could be present: institutional or retail investors, other funds of funds and even other feeders.



Core requirements of UCITS IV

Investment restrictions

- A feeder UCITS has to invest at least 85% of its assets in the master UCITS and the 15% remaining assets being invested in ancillary liquid assets, derivatives for hedging purposes and movable and immovable property essential for the direct pursuit of the business (for investment companies only).
- The master UCITS is subject to the classic diversification limits as set forth in the UCITS Directive as implemented in part I of the Luxembourg Law of 2010. To avoid the creation of opaque structures, the master UCITS is not allowed to invest in another feeder or be itself a feeder.



Competent regulators

- The UCITS master-feeder structure is subject to the authorisation of the feeder's home regulator, i.e. in case of a Luxembourg UCITS feeder the CSSF.
- If the feeder and the master are domiciled in two different jurisdictions, the home regulator of the master UCITS is solely involved to officially confirm in writing that the master complies with the investment restrictions (the "Master UCITS Regulator's Attestation").

Approval of master-feeder structures

- For its creation, a Luxembourg feeder UCITS has to provide the CSSF with a set of documents, including its own prospectus and KIID, but also information related to the master UCITS (prospectus, KIID, the Master UCITS Regulator's Attestation (where applicable), the information sharing agreements put in place between master and feeder, and also between their respective auditors and depositaries).
- All documents must be transmitted to the CSSF in one of the official languages (i.e. French, German or Luxembourgish) or English.
- Approval should be granted within 15 working days following the submission of a complete file.
- In case of conversion of an existing UCITS into a feeder UCITS, the same principles apply, being however understood that the feeder has to (i) prior inform its existing unitholders who will have the right to request within 30 days the repurchase or conversion of their units without charges other than disinvestment costs and (ii) notify accordingly each regulator of the feeder host Member States in case of cross-border distribution.

Monitoring of the Master UCITS

- The feeder UCITS has to monitor the activity of the master UCITS. For that purpose, an information sharing agreement between the feeder and the master is compulsory (except in the case where both master and feeder are managed by the same company) to ensure adequate information flows are in place.
- The depositary of the master UCITS is responsible for immediately informing both its own and the feeder's regulator, the feeder UCITS itself, but also the feeder's depositary and management company (if applicable) about any irregularities detected with regard to the master.

Content of marketing information:

- The prospectus of the feeder UCITS shall contain:
 - a declaration that the feeder is a feeder of a particular master UCITS and as such permanently invests 85% or more of its assets in that master;
 - the investment objective and policy, the risk profile and the performances of the feeder and the master are identical, or to what extent and for which reasons they differ, including a description of investments made in the feeder's 15% pocket (if any);
 - a brief description of the master (organisation, investment objective and policy, risk profile, how the prospectus of the master may be obtained, etc);
 - a summary of the information sharing agreement established between the feeder and the master;
 - how the unitholders may obtain further information on the master and the information sharing agreement between feeder and master;

- a description of all charges payable by the feeder by virtue of its investment in the master and aggregate charges of the feeder and master;
- a description of the tax implications of the investment into the master for the feeder.
- The KIID of the feeder UCITS shall describe:
 - the proportion of the feeder's assets invested in the master;
 - the master's objectives and investment policy;
 - the investment returns of the feeder and master and explanations related to potential differences;
 - the SRRI of the feeder and master differ and explanations related to potential differences;
 - the combination of costs of both in the ongoing charge figure.
- A statement on the aggregate charges of the feeder UCITS and the master UCITS must be included in the annual report of the feeder as well as how the annual and the half-yearly report of the master can be obtained (also in the semi-annual report).

Main operational and business implications

- Information flows and monitoring requirements are quite heavy in particular for master-feeder structures using services providers not belonging to the same group;
- New value chain and related fee arrangements will probably need to be put in place, implying management decisions but also regulatory, tax, operational and marketing analyses;
- Potential accounting, central administration and KIID production issues should not be under-estimated, in particular in case of cross-border master-feeder structure;
- Potential tax impact and regulatory reporting requirements must be closely analysed before any restructuring decision;
- Fund promoters will lastly have to make sure that the savings envisaged by a master feeder structure will exceed the costs incurred, including marketing risks.





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UCITS IV - Mergers

The Luxembourg law of 17 December 2010 (the “Fund Law”) offers new opportunities for market consolidation and rationalisation of UCITS structures through the possibility of merging UCITS both on a domestic and cross-border basis.

Quick Reference Guide



Scope of the UCITS IV merger provisions

UCITS only!

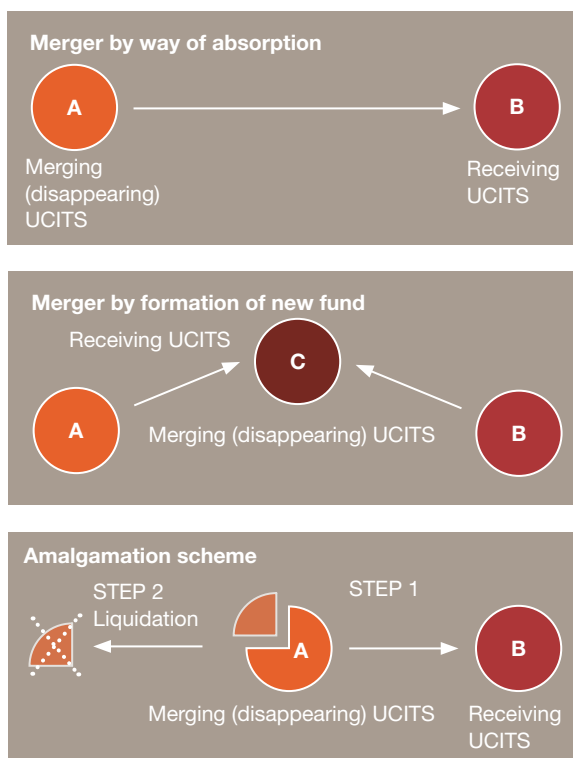
Any type of UCITS funds – SICAV or FCP – are allowed to merge. In case of a cross-border merger, it does not matter if the same legal form for UCITS does not exist in the country where a merger target resides. In addition, promoters can choose to merge entire umbrella structures or a selection of their investment compartments.

Luxembourg non-UCITS are however not allowed to merge across borders using the UCITS IV merger facilities, as they are not covered by the UCITS IV Directive.

Types of merger

In Luxembourg, three merger schemes are recognised :

- Where a UCITS (or one or several of its investment compartments), transfers all its assets and liabilities to another existing UCITS without going into liquidation;
- Where at least two UCITS (or one or several of their investment compartments) transfer all their assets and liabilities to a new UCITS which they form, without going into liquidation;
- Where one or more UCITS (or investment compartments thereof) - which continue to exist until the liabilities have been discharged - transfer their net assets to another compartment of the same UCITS, to a UCITS which they form, or to another existing UCITS (or investment compartment thereof).



Core requirements

Competent regulators

The home regulator of the “merging” UCITS (the UCITS which is being absorbed partially or in full) will authorise the merger. The role of the home regulator of the “receiving” UCITS is to safeguard the interests of investors in that UCITS, working closely with the home regulator of the merging UCITS.

Third party control

The depositary(ies) of both the merging and the receiving UCITS have to confirm, separately in a written statement, that the draft terms of the merger (describing in particular the type of the merger, the merger date and the transfer of assets) comply with the Luxembourg Law provisions as well as the UCITS legal documentation.

An independent external auditor (in this situation, the external auditor of both the merging and the receiving UCITS are considered independent), appointed by the merging UCITS will also have to validate the methodology used to calculate the exchange ratio, the actual exchange ratio and any cash payment per unit.

Lastly, for any Luxembourg merging UCITS which ceases to exist, the effective date of the merger must be recorded by notarial deed.

Merger regulatory approval process

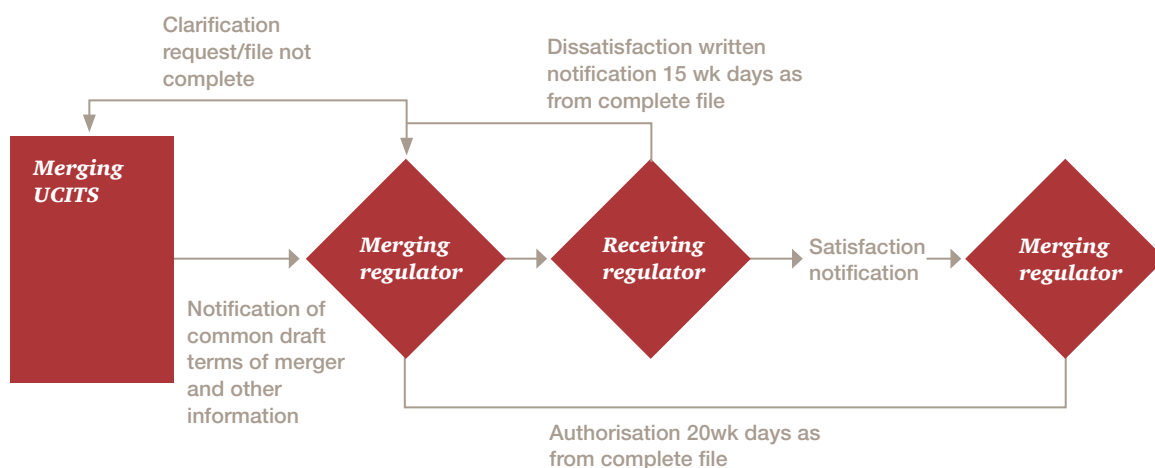
A regulator-to-regulator approach is key to the approval process.

The merging UCITS must file a standardised, prescribed set of documents with its home regulator (the “Merging Regulator”). This includes the draft terms of the merger, an up-to-date prospectus and Key Investor Information Document (“KIID”), both depositaries’ statements and any translated information intended for either the receiving or merging UCITS investors.

The Merging Regulator has to check the file for completeness, requesting any additional information within ten working days of initially receiving it.

Once complete, the Merging Regulator immediately has to send the file to the receiving UCITS regulator (the “Receiving Regulator”). Authorisation then follows within 20 working days.

The following diagram illustrates this approval process:



Investors' rights

Investors obviously need to be properly informed. They need to receive information on the background of, and rationale for, the merger, possible impacts on investors, description of investors' rights, the merger process, the date of the merger and the KIID of the receiving UCITS.

The implications for the investors in the receiving UCITS will differ from those for the investors in the merging UCITS. So, logically, both sets of investors do not need to receive the same information.

The Merging Regulator has to assess the appropriateness and accuracy of the information provided to the merging and receiving investors in close cooperation with the Receiving Regulator, and approves its issuance.

Before the merger, investors of both the merging and receiving UCITS should have at least 30 calendar days to request the repurchase (or, where possible, conversion) of their units free of charge (except for related divestment costs). Consequently, investors have to receive the approved information at least 30 days before the cut-off date for repurchases. The cut-off date is set five working days before the date for calculating the exchange ratio.

Concerning the decision-making process, Luxembourg UCITS are free to foresee in their legal constitutive documents which forum (investors' meeting or, alternatively Board meeting (for SICAV), or Board meeting (for the management company of a FCP)) is competent to decide on the merger. In the case where the merger decision would be subject to the vote of the investors, such decision will not be subject to a majority of more than 75% of the investors present and represented. However, for any merger where the merging UCITS is an investment company which ceases to exist, the effective date of the merger must be decided by a meeting of the unitholders of the merging UCITS.

Main operational and business implications

Focus on the preparatory work/tasks

Before deciding on a merger, a promoter should undertake an in-depth review to analyse the major implications and identify the key factors to be taken into account, including distribution, tax and regulatory issues. It is worth noting that tax is often the most important consideration, as a merger has generally significant tax implications for investors.

The promoter needs to analyse the different merger schemes to choose the most appropriate one. A clear plan for managing the merger will ensure it goes smoothly, without regulatory or operational difficulties on transfer. Particular attention needs to be paid to the completeness and accuracy of the merger file.

The KIID of the receiving UCITS must be updated (including empty shelves if necessary) and communicated to investors prior to deciding on the merger.

The promoter will have to make sure that the investment policies of the merging and receiving UCITS are aligned, as well as each of the portfolios, to avoid possible investment breaches.

Focus on the transfer

The rules described above will be applicable for cross-border and domestic mergers, including the contribution of one investment compartment to another. Given that EU rules will apply to domestic mergers of UCITS, national practices (including the Luxembourg one) will probably become less flexible (as the depositary and the auditor will have to intervene, investors in both investment compartments will be able to request the redemption of their units, etc.).

A merger implies potential migration issues that must be considered prior to the merger.

In case of merger between two UCITS being incorporated under the form of a company, the existing agreements may remain in force (i.e., no re-negotiation will be required).

Performance track record may be kept, subject to certain conditions, at least from a marketing perspective.

Focus on the investors

The rules relating to the merger decision and the way in which information is provided to investors will still be subject to national laws (no harmonisation), and potentially, be different from one UCITS to another: the promoter will then have to comply with specific local/vehicle requirements and manage possibly divergent rules.

In the case where the merger decision is subject to a vote by investors, such a decision may not be subject to a majority of more than 75% of the present and represented shareholders. The merger decision will bind the investors not being in favour of the merger and not having requested the repurchase of their units during the 30 days period of time.

The rules described above will be applicable for cross-border and domestic mergers, including the contribution of one investment compartment to another.

The preparatory work based on distribution footprint will be key.

Focus on the tax issues

Mergers may have tax consequences for the investors in their home country when no tax relief or deferral is available. So, before moving ahead with a merger, it is advisable to undertake a detailed analysis of the nature of the investors and tax implications in their country of residence.

It will also be key to consider the impact of the EU Savings Directive (including tax and reporting duties) as the Directive normally triggers a reportable/taxable event where it is applicable.

Exit taxation and/or registration/stamp duties in underlying investments' countries should also be closely analysed.

In some circumstances, a merger may qualify as a transfer of going concern and, therefore, be out of the scope of the VAT requirements. This should be confirmed at a national level, as conditions can vary between EU Member States.

In addition, reorganisations can create additional and often irrecoverable VAT costs. Considering the VAT implications in the context of the reorganisation plan may enable the promoter to take advantage of any opportunities, while mitigating VAT costs.

Focus on the distribution footprint

The preparatory work based on distribution footprint will be key. Relevant notifications (within the EU) and prior registrations (outside the EU) must be approved before merging. Potential registration issues outside the EU must be considered prior to merger.

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