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Research Report

RAIF – Reserved Alternative Investment Fund – The impact on the Luxembourg Fund Market and the Alternative Investment Fund landscape

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EIKV-Schriftenreihe zum
Wissens- und Wertemanagement

RAIF – Reserved Alternative Investment Fund – The
impact on the Luxembourg Fund Market and the
Alternative Investment Fund landscape

Patrick Matthias Sprenger

IMPRESSUM

EIKV-Schriftenreihe zum Wissens- und Wertemanagement

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Table of contents

Table of contents	II
List of figures	IV
List of tables.....	IV
List of abbreviations.....	V
Abstract.....	IX
1. Preface	1
1.1. Motivation.....	3
1.2. Objective	4
1.3. Structure	5
1.4. Methodology	6
1.5. Disclaimer	9
2. The Luxembourg Investment Fund Market.....	10
2.1. Market potential	15
2.2. Investment funds and their regimes.....	21
2.2.1. Legal forms and organizational structures.....	24
2.2.2. UCITS	32
2.2.3. AIF – Alternative Investment Funds.....	33
2.2.4. AIFMD.....	37
3. RAIF – Reserved Alternative Investment Fund	41
3.1. RAIF – introduction and setup	42
3.2. RAIF & AIF/M regulation absence of CSSF supervision	51
3.3. Benefits of the RAIF compared to other Luxembourg AIF vehicles	55
3.3.1. SIF – Specialized Investment Fund.....	56
3.3.2. SICAR – Investment Company in Risk Capital.....	60
3.3.3. UCI – Part II Law Fund	63
3.3.4. Non-regulated vehicles	64

3.4.	Comparison of European Fund Markets.....	67
3.5.	Interim result	70
4.	Strategic direction of the Luxembourg AIF Market	72
4.1.	Strengths and weaknesses of the Luxembourg AIF Market.....	73
4.2.	Opportunities and threats of the Luxembourg AIF Market.....	75
5.	Empirical analysis	77
5.1.	Interview development.....	77
5.2.	Interview partners	79
5.2.1.	Summary of the interview I	80
5.2.2.	Summary of the interview II	83
5.2.3.	Summary of the interview III	85
5.2.4.	Summary of the interview IV.....	87
5.2.5.	Summary of the interview V.....	90
5.3.	Interim result of the empirical analysis.....	92
6.	Conclusion	94
	ANNEX	X
	Interview I – Hermann Kranz (UBS Europe SE, Luxembourg Branch).....	X
	Interview II – Christopher Dortschy (Allen & Overy, Luxembourg)	XVII
	Interview III – Jendrik Fuhrmann (Hauck & Aufhäuser, Luxembourg)	XXII
	Interview IV – Susanne Weismüller (ALFI, Luxembourg)	XXVI
	Interview V – Kai Braun (Ernst & Young, Luxembourg).....	XXXIV
	VI Potential catalogue of questions for the interviews	XXXVII
	Bibliography	XXXVIII
	Internet Sources	XLI

List of figures

Figure 1: Key questions of this thesis.....	4
Figure 2: The research wheel.....	7
Figure 3: Assets under management in the European investment fund industry....	13
Figure 4: Legal status of Luxembourg domiciled investment funds	14
Figure 5: Government debt to GDP ratio, 2016 Q2 in percentage.....	19
Figure 6: Importance of the financial sector	20
Figure 7: Actors and functions of an investment fund	22
Figure 8: Net Asset Value - NAV	23
Figure 9: Corporate forms available in Luxembourg	26
Figure 10: Alternative and traditional investments	34
Figure 11: Luxembourg entities considered as AIFs.....	36
Figure 12: Potential AIFM entities	38
Figure 13: The EU AIFMD framework.....	39
Figure 14: AIFMD Luxembourg transposition.....	40
Figure 15: RAIF - common fund (FCP).....	44
Figure 16: RAIF - Investment company that appt. a ManCo.....	45
Figure 17: Taxation RAIF - standard and related to Risk Capital.....	50
Figure 18: The Luxembourg fund structuring toolbox.....	55
Figure 19: Net Assets under management in Europe	67
Figure 20: RAIF - comparison with similar EU Regimes	68
Figure 21: SWOT-analysis of Luxembourg related to the Fund Business	72

List of tables

Table 1: Interview structure continuum.....	8
Table 2: Worldwide numbers & total net assets of regulated open-end funds.....	11
Table 3: Comparison of the most popular corporate forms in Luxembourg	29

List of abbreviations

ABBL	Luxembourg Bankers' Association
AIF	Alternative Investment Funds
AIFM	Alternative Investment Funds Manager
AIFMD	Alternative Investment Funds Manager Directive
Appt.	Appointed
AuM	Assets under Management
BaFin	Federal Financial Supervisory Authority (Bundesanstalt für Finanzdienstleistungsaufsicht)
BEPS	Base Erosion and Profit Shifting
CIS	Contrats à impact social
CSSF	Luxembourg supervisory authority of the financial sector (Commission de Surveillance du Secteur Financier)
DTT	Double Taxation Treaty
EC	European Commission
EEA	European Economic Area
EFAMA	European Fund Asset Management Association
ELTIF	European Long-Term Investment Fund
EMEA	Europe, the Middle East and Africa
ESM	European Stability Mechanism
EuSEF	European social entrepreneurship funds
EuVECA	European Venture Capital Fund
EU	European Union
FCP	Contractual Funds (fonds commun de placement)

FCPR	Retail Private Equity Investment Fund
FGR	Fund for Joint Account (fonds voor gemene rekening)
FinTec	Financial Technology
FPS	Fonds professionnels spécialisés
GDP	Gross domestic product
HCPF	High Committee for the Financial Centre (Haut comité de la place financière)
IFCS	Ireland's International Financial Services Centre
IML	Institut Monétaire Luxembourgeois
IPO	Initial public offering
KAGB	Kapitalanlagegesetzbuch
LP	Limited Partnership
ManCo	Management Company
NATO	North Atlantic Treaty Organization
NAV	Net Asset Value
NON-UCITS	All funds not subject to UCITS
PIF	Professional investor fund
QIAIF	Qualifying Investor Alternative Investment Fund
QIF	Irish Qualifying Investor Fund
RAIF	Reserved Alternative Investment Fund
RIAIF	Retail Investor Alternative Investment Fund
RSCL	Company Register (Registre de Commerce et des Sociétés)
SA	Public Limited Company (Société Anonyme)
SARL	Limited Liability Company (Société à responsabilité limitée)

SCA	Partnership Limited By Shares (Société en commandite par actions)
SCoSA	Cooperative Company organised as a Public Limited Company (Société cooperative organisée sous forme de société anonyme)
SCS	Limited Partnership (Sociétés en commandite simple)
SCSp	Special Limited Partnership (Société en commandite spéciale)
SE	Societas Europaea
SICAF	Investment company with fixed capital (Société d'investissement à capital fixe)
SICAR	Investment Company in Risk Capital
SICAV	Investment company with variable capital (Société d'investissement à capital variable)
SIF	Specialized Investment Funds
SOPARFI	Societe de Participations Financieres
SPF	Private Asset Management Company (Société de gestion de patrimoine familial)
SPV	Special Purpose Vehicle
SV	Securitization Vehicle
SWOT	Strengths, Weaknesses Opportunities, Threats
Tn	Trillion
UCI	Undertakings for Collective Investment (Part II of law of 17 December 2010 as amended relating to undertakings for collective investment)
UCITS	Undertakings for Collective Investment in Transferable Securities (Part I of law of 17 December 2010 relating to undertakings for collective investment)

UK United Kingdom

US United States of America

Abstract

Master Thesis of Mr. Patrick Matthias Sprenker, Master of Business Administration, European University for Economics and Management, eufom.

Within the theme “RAIF – Reserved Alternative Investment Fund – The impact on the Luxembourg Fund Market and the Alternative Investment Fund landscape” this thesis will present the possible effects related to the introduction of the Reserved Alternative Investment Fund (RAIF) and its impact on the Luxembourg Alternative Investment Fund Industry.

Especially Luxembourg’s ability to diversify its product range and to extend its product offers by creating new and innovative fund structures attracts potential investors and initiators. These unique circumstances have an impact on the Alternative Investment Fund Industry.

The aim of this thesis is to provide a detailed and comprehensive overview of the relevant fund business and its related regulations in order to access the RAIF within the current market environment and to investigate if such a product can positively influence the growth of the local Alternative Investment Fund Market.

The current role of the Luxembourg Alternative Investment Fund Industry and its potential as well as the outcomes, derived from the analysis of the RAIF in relation to other available fund products, will be presented and evaluated based on a SWOT analysis.

The gained theoretical insights will be compared with the practical and current market view of the product derived from five expert interviews, each conducted with a specialist in the specific field of the Alternative Investment Fund Industry in Luxembourg.

In a final conclusion the findings and results, gained from the theoretical and practical part of this thesis, will be presented. The RAIF has a significant potential to become a well-established fund structure in the Luxembourg market. It reflects the level of creativity, flexibility and diversity of a market and its players within in a fast changing environment.

1. Preface

The time of the RAIF – Reserved Alternative Investment Fund – another revolution in Luxembourg and its Alternative Investment Fund landscape.

In the current media different headlines like “The RAIF: A game changer for Luxembourg”¹, “Ready for the RAIFolution”², “RAIF: Ein neues Fondsvehikel aus Luxemburg”³, “Luxembourg looking to repeat its UCITS success with AIFs”⁴ signalize a change in the Luxembourg Alternative Investment Fund (AIF) landscape.

Reason for these articles is the new law on Reserved Alternative Investment Funds (RAIF) that was adopted by the Luxembourg Parliament on July 14th, 2016.⁵

“Luxembourg is the leading jurisdiction in Europe for the structuring and setup of investment fund structures and is recognized as a center of excellence in the investment fund industry. The country has become the global leader for cross-border distribution of regulated investment vehicles and is the jurisdiction of choice for the structuring of alternative investment funds.”⁶

This innovation in the field of AIF industry strengthens the role of Luxembourg as global center of excellence for AIFs.

The RAIF is a completely new Luxembourg based AIF, only managed by an authorized Alternative Investment Fund Manager (AIFM). With this vehicle Luxembourg aims to revolutionize the international AIF sector by extending the existing range of structuring solutions for Private Equity, Real Estate, Hedge Funds and other AIF strategies. Important is, that the RAIF has the legal obligation to be managed by an authorized AIFM it will have the benefit of the marketing to professional investors in the European Union (EU). The innovation is that the RAIF is no longer subject to the supervision of the Luxembourg supervising authority, the ‘Commission de Surveillance du Secteur Financier’ (CSSF). The CSSF will not be involved in the approval of the fund documentation and will not be in charge of the ongoing supervision of the fund anymore. This aims at accelerating the setup of a

¹ (Williams, Hedgeweek, 2016 (II)), p.1.

² (Williams, Hedgeweek, 2016 (I)), p.1.

³ (von Kymmell, 2016), p.1.

⁴ (Global Investor ISF, 2016), p.1.

⁵ Cf. (Elvinger Hoss Prussen, 2016 (I)), para.1.

⁶ (Luxembourg Fund Partners, 2016 (I)), para.2.

RAIF in a shorter timeframe. The RAIF is said to be the new vehicle of choice for managers and investors who are looking for an investment vehicle which combines contractual flexibility, efficiency in a regulated framework governed by the Alternative Investment Fund Manager Directive (AIFMD) and which simultaneously benefits from the European Passport enabling marketing to professional investors within the EU.⁷

Another aspect is related to the fact that some of the RAIF's characteristics can be changed during the life of the fund without going through the regulatory approval, which means faster reactivity and increased flexibility. The RAIF has similarities with the already existing Specialized Investment Fund (SIF) and can also take several different legal forms, thus allowing for a number of tax structures as well as various management options. This has been eagerly awaited, not only by private equity players but also in terms of asset-based products. Institutional and high net worth investors, along with their asset managers, were longing for a faster time-to-market vehicle offering similar characteristics as the already existing SIF. The RAIF offers similar advantages while giving its managers enough flexibility in the choice of the investment strategies and eligible assets. This seems to be a very promising product with a very bright future.⁸

In summary: the RAIF will not be supervised by the CSSF. It offers more structuring flexibility than the SIF. Due to the exclusive distribution to well-informed, qualified investors the RAIF benefits from less restrictive investment requirements. However, the RAIF will need to comply with all valuation, risk and portfolio management requirements set out in the AIFMD.⁹

In order to provide an understandable view to this new vehicle and its related environment, this thesis aims at introducing the relevant fund business and its regulations in order to compare the RAIF with the available fund structures in its current environment and to investigate if such a product can positively influence the local market structure. The detailed description of the approach will be illustrated in the next chapters.

⁷ Cf. (ALFI - Association of the Luxembourg Fund Industry, 2016 (I)), p.1.

⁸ Cf. (Lentschat, 2015), video, an expert's view on the RAIF.

⁹ Cf. (Luxembourg Fund Partners, 2016 (I)), p.2.

1.1. Motivation

Having witnessed the ongoing developments of investment fund products in the Luxembourg Fund Market in regards to new products in today's fund economy, I was motivated to analyze the current state of the AIF Industry and its key drivers. In order to understand in detail the creation of a new product, I focused on the RAIF, and how this product impacts the fund market. In particular, how it fulfills the required needs professional investors have been demanding for quite a while.

Being working and studying in Luxembourg during the last years, my interest of investigating the strategy of Luxembourg's investment fund business grew. The creation of a new fund vehicle for professional investors is an elementary topic in regards to the marketing and creates added value to the economic landscape of the Luxembourg Fund Industry.

Another reason why this area has been chosen in particular, is related to my professional work field. Having worked for more than six years in the financial industry within the fields of investment fund taxation, the taxation of private investors and today in the business management area of a Luxembourg bank, has led to an increasing interest on how the RAIF can revolutionize the AIF Market as a new innovative vehicle.

Due to the fact that the environment of the AIF business is not really a common subject for non-professionals this thesis aims to provide a general understanding of the RAIF for the reader in order to understand its purpose and to point out the interactions and benefits for the Luxembourg AIF Sector. Furthermore, it is analyzed how a RAIF is structured, what are its features and what are the advantages and disadvantages for initializing such a vehicle in a European context.

This thesis should serve as a guide for interested readers, professionals and non-professionals, in order to gain a broad overview about this new AIF vehicle and to understand its meaning within the AIF Market in Luxembourg and in the European context as well as to get a first indication about how this instrument is adopted in practice.

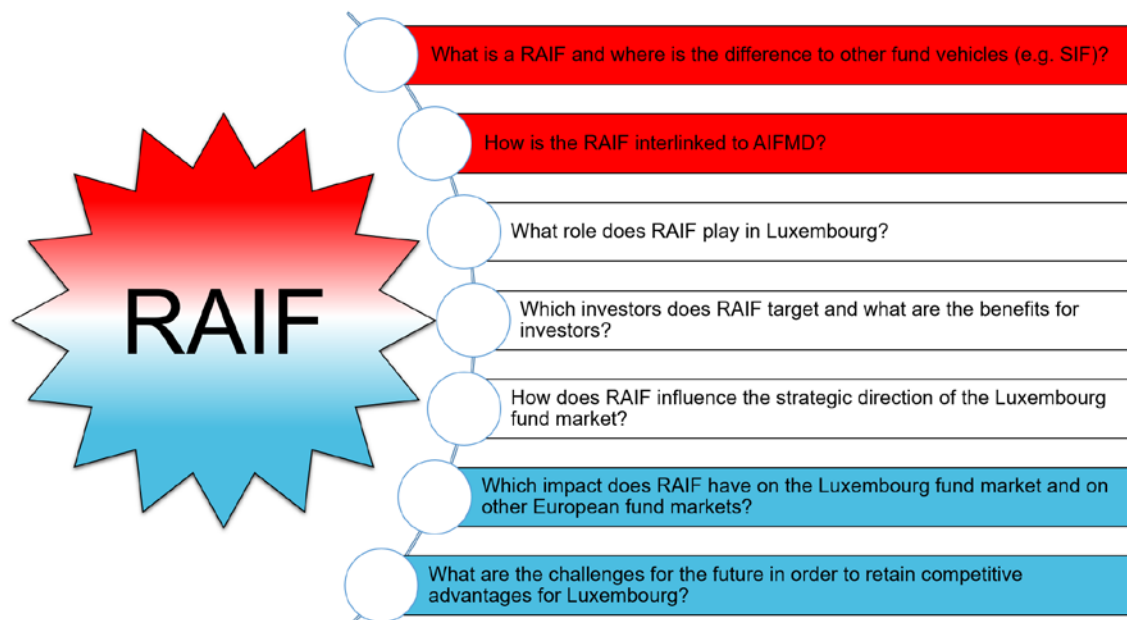
1.2. Objective

The main objective of this thesis is to point out the opportunities that the RAIF provides for the development of the AIF Market in Luxembourg. Due to the importance of regulations and supervision in this area, the relevant regulations and laws have to be considered and will be presented on the basis of the most important key elements.

The potential that Luxembourg offers in terms of AIFs, innovation and attraction for potential investors will be explained. Therefore, the classification of the RAIF within the AIFMD as well as the comparison to other existing AIF vehicles is pointed out.

Based on the above, the thesis illustrates how the RAIF can be used and how it inspires the players around the AIF Market to ensure competitive advantages for Luxembourg's future development. In this context it is essential to consider the needs of the different market players and to describe how the RAIF can potentially influence other markets in Europe. In summary the thesis aims to answer the key questions pointed out in below Figure 1: Key questions of this thesis:

Figure 1: Key questions of this thesis



Source: Own elaboration of the relevant key questions of this thesis.

1.3. Structure

Firstly the thesis provides a general overview of the Luxembourg Fund Landscape as well as its potentials focusing on the current regimes. In a first step Luxembourg's Investment Fund Market will be introduced and its market potential will be presented. Subsequently, the Investment Fund itself will be defined and the most important regimes of Undertakings for Collective Investment in Transferable Securities (UCITS) and AIFMD will be briefly presented, to enable the basic understanding for the functionality of the RAIF.

Following the above the RAIF itself will be introduced in more detail, presenting its features and how the RAIF is interlinked with the AIFM governed by AIFMD. In this regard the interdependencies to the AIF as well as the AIFM related to AIFMD will be explained.

Further, Luxembourg's most important AIF structures will be briefly introduced and it will be pointed out how these vehicles differentiate from the RAIF in terms of possible investments and advantages the structures provide for the initiators and potential investors. Furthermore, the RAIF will be compared to other European fund structures with similar setup to identify the potential of this new vehicle.

In chapter four the focus is set on the strategic direction of the Luxembourg Fund Market. Especially the current role of the Luxembourg Alternative Investment Fund Industry and its potential as well as the outcome of the analysis performed during the thesis which is evaluated based on a SWOT analysis. This illustrates the results in a clear and structured manner.

In the fifth chapter the empirical analysis of five expert interviews conducted, is presented. This is done in order to gain practical insights and expert knowledge directly from the source of the specific fields of the Alternative Investment Fund Industry in Luxembourg.

In the conclusion, the outcomes and results gained from the theoretical and practical part of this thesis, will be combined to a final statement.

1.4. Methodology

For the handling of the topic “RAIF – Reserved Alternative Investment Fund – The impact on the Luxembourg Fund Market and the Alternative Investment Fund landscape” a specialized knowledge and profound expertise is required. In order to obtain this knowledge it is essential to deal with the latest state of the current laws in Luxembourg as well as with technical terms that relate to the chosen topic. Due to the novelty of this topic a detailed online and literature research is necessary.

Most currently available literature deals with the regulatory requirements of AIFMD and the regimes that are already existing in Luxembourg. At the moment, no academic research or work has been concluded that includes RAIF structures in Luxembourg.

Due to the lack of data sources it is essential to gather primary data in order to discover results for the topic. To generate the necessary information, established empirical methods can assist for the research in order to gain profound knowledge to determine specificities in the research field.

In common literature three different empirical methods are known as source to generate this information and knowledge: direct observations, guided interviews or surveys and/or experiments. Practical data-collection is necessary to confirm or reject a hypothesis. In the case of confirmation, theories or models can be developed or transcended and other recommendations for action can be derived from the actors from practice.¹⁰

In addition a qualitative research approach will be used in order to provide a better understanding of the strategic direction of the Luxembourg Alternative Fund Market. The strategy tool SWOT analysis (strengths, weaknesses, opportunities, threats) is used to connect the results of the analysis of the external and internal environment.¹¹

The results of the analysis will feed the tool in order to provide a profound conclusion for the strategic positioning of the Luxembourg Fund Market.

¹⁰ Cf. (Burchert & Sohr, 2008), p.20.

¹¹ Cf. (Paul, Cadle, & Yeates, 2014), p.49.

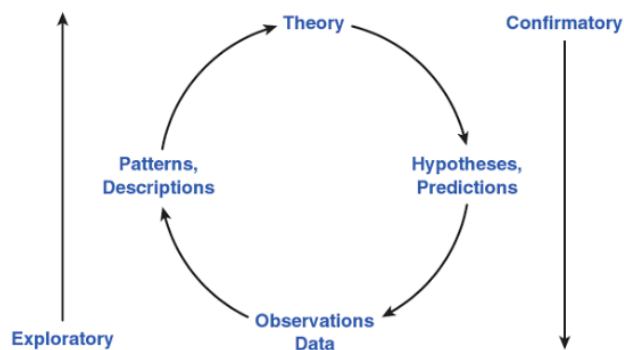
Furthermore, this thesis will focus on interviews as selected empirical method.

“Interviewing has obvious advantages as a methodology. The researcher feels in control, in the sense of having the research participants in front of him or her, at the end of the phone or, virtually, online. He or she can set the agenda, ask questions, observe and/or listen to or read responses. It is a relatively efficient, effective and versatile methodology.”¹²

This research aims at explaining and pointing out how the RAIF is interlinked in its market environment and which are its special features. Furthermore, its attractiveness for the Luxembourg Fund Market should be described and compared to other available fund vehicles in Luxembourg and Europe. In addition personal impressions on how the market for RAIF in Luxembourg will develop shall be determined by questioning about any potential threats and challenges. These questions imply that only professional interview partners can be considered for this purpose.

This leads consequently to the fact that a qualitative interview fits the needs of this research task. Quantitative research focuses on testing theories and hypotheses using quantitative data, e.g. standardized tests just focus on seeing if they are confirmed or not, whereas qualitative research focuses on exploration, description and the generation and construction of theories using qualitative data, e.g. open-ended interviews that provide data and information based on the participant’s perspective and their actual words.¹³

Figure 2: The research wheel



Source: Cf. (Johnson & Christensen, 2012), p.18.

¹² (Keegan, 2009), p.73.

¹³ Cf. (Johnson & Christensen, 2012), p.18.

Figure 2: The research wheel, illustrates very vividly the difference between quantitative and qualitative research. While quantitative research accentuates movement from theory to hypotheses to data and to conclusions (confirmation), qualitative research emphasizes movement directly from observations and data to descriptions and patterns or even theory generation (exploration).¹⁴

In the last step the type and structure of qualified interviews has to be specified. In Table 1: Interview structure continuum, an overview of three types of interviews is presented. The types of highly structured/standardized interviews, semi structured interviews and unstructured/informal interviews vary in relation to the amount of structure inherent in the interview.¹⁵

Table 1: Interview structure continuum

Highly Structured/Standardized	Semistructured	Unstructured/Informal
Wording of questions is predetermined	Interview guide includes a mix of more and less structured interview questions	Open-ended questions
Order of questions is predetermined	All questions used flexibly	Flexible, exploratory
Interview is oral form of a written survey	Usually specific data required from all respondents	More like a conversation
In qualitative studies, usually used to obtain demographic data (age, gender, ethnicity, education, and so on)	Largest part of interview guided by list of questions or issues to be explored	Used when researcher does not know enough about phenomenon to ask relevant questions
Examples: U.S. Census Bureau survey, marketing surveys	No predetermined wording or order	Goal is learning from this interview to formulate questions for later interviews
		Used primarily in ethnography, participant observation, and case study

Source: Cf. (Merriam, 2009), p.89.

The more structured an interview is, the more difficult it becomes to access the participants' perspectives and understanding of the topic. The main benefit of a highly structured format in qualitative research is to collect, e.g. common sociodemographic data from respondents. On the opposite side unstructured or informal interviews are

¹⁴ Cf. *ibid.*

¹⁵ Cf. (Merriam, 2009), p.89.

used to explore a new phenomenon and aim to gather information about an unknown topic. One of the goals of the unstructured interview is to learn about a new situation in order to formulate specified questions for subsequent interviews. Insights and understanding can be obtained in this approach, while at the same time an interviewer may feel lost from divergent points of view and seemingly incoherent information.¹⁶ Both formats are not very suitable for achieving the objective since the potential questions are already known.

Semi structured interviews are in the middle between structured and unstructured interviews. This less structured but guided way of interviewing "...assumes that individual respondents define the world in unique ways."¹⁷ This more flexible way of interviewing allows a more open-ended way of interviewing while at the same time predefined questions can be taken into consideration and may be varied during the interview. This allows the researcher to react to the prevailing situation and at the same time to respond to the emerging worldview of the interviewee and collect new ideas on the subject.¹⁸ For the reasons described, the semi structured interview is conducted to achieve the objective of this work.

1.5. Disclaimer

It is also essential to note that the content of this thesis has been compiled with utmost care by the author. However, no guarantee can be given for the correctness, completeness and timeliness of the content provided. The regulatory and legal content is not intended to be comprehensive nor does it constitute any tax or legal advice. The sections of directives and laws presented were specially selected by the author and are aimed to introduce and to compare the most important features regarding the regular framework of this thesis. A complete presentation of all legal, fiscal and regulatory aspects would not be feasible in the course of this work.

¹⁶ Cf. *ibid*, p.90f.

¹⁷ *Ibid*, p.90.

¹⁸ Cf. *ibid*.

2. The Luxembourg Investment Fund Market

This chapter provides an overview of the current situation of the fund business in general and of Luxembourg's position within the EU.

In a first step the current global conditions and the importance of the investment fund business in the financial sector will be presented. Followed by the present situation of the fund business in Europe. In a second step the situation of the Luxembourg Fund Market will be explained and the market potential will be presented. Therefore, the distribution of the market shares, the number of different types of investment funds as well as the amount of their assets will be illustrated. In a last step the available legal forms are introduced and the current market regimes are explained.

In general the fund industry is a growth sector.¹⁹ Globally more than 119'000²⁰ funds with total fund assets of EUR 38 trillion²¹ are competing for investors. The structure of the European Fund Market is significantly different from the US market. The European market has many more public funds than the American one, but the average fund size is smaller in Europe. The smaller scale tends to generate higher administrative costs.²² Table 2: Worldwide numbers & total net assets of regulated open-end funds, illustrates the development for the years 2008-2015.

¹⁹ Cf. (International Bank for Reconstruction and Development / The World Bank, 2015), p.118.

²⁰ Cf. (EFAMA - European Fund and Asset Management Association, 2016), p.7.

²¹ Cf. *ibid*, p.1.

²² Cf. (Smith, Walter, & DeLong, 2012), p.208ff.

Table 2: Worldwide numbers & total net assets of regulated open-end funds

	2008	2008	2009	2009	2010	2010	2011	2011	2012	2012	2013	2013	2014	2014	2015	2015
World	76.519	\$20.631.003	75.293	\$25.088.939	77.836	\$27.374.359	81.429	\$26.578.593	82.410	\$30.213.561	88.747	\$34.462.543	98.832	\$37.072.351	100.494	\$37.190.528
Americas	17.205	11.130.264	17.732	13.355.373	18.916	14.591.545	20.884	14.583.246	22.291	16.488.566	23.322	18.864.164	24.378	20.009.504	25.230	19.557.328
Argentina	253	3.867	252	4.470	254	5.179	281	6.808	291	9.185	297	11.179	302	15.630	346	16.435
Brazil	4.169	479.321	4.744	783.970	5.618	980.448	6.513	1.008.928	7.468	1.070.998	8.072	1.018.641	8.560	989.542	8.783	743.530
Canada	2.015	416.031	2.075	565.156	2.117	636.947	2.655	753.606	2.866	856.504	2.963	940.580	3.164	981.804	3.283	889.610
Chile	1.484	17.587	1.691	34.227	1.912	38.243	2.150	33.425	2.286	37.900	2.385	39.291	2.418	44.166	2.500	39.898
Costa Rica	85	1.098	64	1.309	68	1.470	83	1.266	66	1.484	66	1.933	66	2.092	65	2.533
Mexico	431	60.435	407	70.659	434	98.094	464	92.743	488	112.201	487	120.518	486	119.504	499	105.940
Trinidad and Tobago	N/A	N/A	36	5.832	35	5.812	36	5.989	42	6.505	43	6.586	43	7.121	44	6.983
United States	8.768	10.151.925	8.463	11.889.750	8.478	12.825.352	8.722	12.680.481	8.784	14.393.789	9.009	16.725.436	9.339	17.849.645	9.710	17.752.399
Europe	43.521	7.393.787	41.862	8.912.070	42.712	9.573.876	43.400	8.949.093	42.449	10.257.646	43.092	11.715.462	49.335	12.858.573	47.427	12.772.328
Austria	1.765	155.555	1.717	176.008	1.762	173.908	1.760	157.510	1.776	172.950	1.805	181.694	1.629	165.084	1.596	151.199
Belgium	1.828	105.057	1.845	106.721	1.797	96.288	1.723	81.505	1.529	81.651	1.432	91.528	1.231	100.790	1.164	92.115
Bulgaria	81	226	85	256	90	302	92	291	95	324	98	504	104	496	104	440
Croatia	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	1.975
Czech Republic	76	5.260	78	5.436	80	5.508	80	4.445	80	5.001	85	5.131	108	5.746	128	7.812
Denmark	489	65.182	483	83.024	490	89.800	500	84.891	495	103.506	510	118.702	526	120.844	556	116.696
Finland	389	48.750	377	66.131	366	71.210	368	62.193	375	73.985	369	88.462	383	86.397	371	88.351
France	8.301	1.591.082	7.982	1.805.641	7.791	1.617.176	7.744	1.382.068	7.392	1.473.085	7.154	1.531.500	11.273	1.940.490	11.122	1.832.073
Germany	5.633	1.130.972	5.967	1.342.275	5.923	1.389.306	5.813	1.356.446	5.868	1.587.390	5.905	1.824.429	5.509	1.847.268	5.604	1.799.574
Greece	239	12.189	210	12.434	213	8.627	196	5.213	177	6.011	166	6.742	143	5.256	139	4.292
Hungary	302	10.234	301	13.127	325	14.672	200	8.417	214	4.944	216	12.870	307	15.980	316	14.825
Ireland	3.097	720.486	2.721	860.515	2.899	1.242.321	3.085	1.324.482	3.167	1.581.361	3.345	1.811.933	5.833	2.020.134	3.864	2.067.251
Italy	977	288.354	880	297.839	823	248.838	822	191.479	733	189.937	777	223.403	687	217.363	713	207.867
Liechtenstein	335	20.489	348	30.329	536	38.981	596	36.412	717	36.585	875	40.940	946	45.792	1.184	44.938
Luxembourg	11.166	2.042.317	11.136	2.538.921	11.860	2.799.021	12.258	2.587.137	12.458	3.007.396	12.760	3.453.934	11.838	3.518.566	12.074	3.565.757
Malta	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	54	3.033	69	3.160	110	4.223	130	3.808
Netherlands	458	77.379	N/A	95.512	N/A	85.924	495	69.156	497	76.145	501	85.304	561	74.922	N/A	N/A
Norway	530	41.157	487	71.170	507	84.505	507	79.999	406	98.723	573	109.325	619	112.223	700	102.526
Poland	210	17.782	208	23.025	214	25.595	226	18.463	259	25.883	264	27.858	398	34.177	391	32.286
Portugal	184	13.572	171	15.808	171	11.004	173	7.321	157	7.509	153	9.625	184	15.786	396	21.628
Romania	52	326	51	1.134	56	1.713	105	2.388	62	2.613	64	4.000	72	4.932	74	5.038
Russia	528	2.026	480	3.182	462	3.917	472	3.072	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Slovakia	57	3.873	55	4.257	59	4.381	65	3.222	62	2.997	58	3.347	87	6.514	88	6.202
Slovenia	125	2.067	125	2.610	130	2.663	137	2.279	131	2.370	114	2.506	110	2.550	109	2.448
Spain	2.944	270.983	2.588	269.611	2.486	216.915	2.474	195.220	2.349	191.284	2.267	248.234	2.235	274.072	2.238	274.715
Sweden	508	113.331	506	170.277	504	205.449	508	179.707	456	205.733	484	252.878	522	283.683	471	279.977
Switzerland	572	135.052	509	168.260	653	261.893	664	273.061	667	310.686	765	397.080	843	436.431	860	457.162
Turkey	304	15.404	286	19.426	311	19.545	337	14.048	351	16.478	373	14.078	398	15.288	377	12.833
United Kingdom	2.371	504.681	2.266	729.141	2.204	854.413	1.941	816.537	1.922	985.517	1.910	1.166.834	2.597	1.501.308	2.573	1.578.360
Asia and Pacific	14.909	2.037.535	14.795	2.715.235	15.265	3.067.323	16.198	2.921.278	16.703	3.322.199	21.271	3.740.049	23.948	4.057.800	26.510	4.738.804
Australia	N/A	841.133	N/A	1.198.838	N/A	1.455.850	N/A	1.440.128	N/A	1.667.128	N/A	1.624.081	N/A	1.601.078	N/A	1.521.313
China	429	276.303	547	381.207	660	364.985	831	339.038	1.065	437.449	1.415	460.332	1.763	708.884	2.558	1.263.130
India	551	62.805	590	130.284	658	111.421	680	87.519	692	114.489	699	107.895	768	136.834	804	168.186
Japan	3.333	575.327	3.656	660.666	3.905	785.504	4.196	745.383	4.384	738.488	7.818	1.157.972	8.761	1.171.974	9.804	1.328.634
Korea, Rep. of	9.384	221.991	8.703	264.574	8.687	266.495	9.064	226.717	9.121	267.583	9.876	285.172	11.235	330.168	11.918	343.293
New Zealand	643	10.612	702	17.657	700	19.562	709	23.709	700	31.145	694	34.185	632	41.559	609	41.908
Pakistan	83	1.985	96	2.224	125	2.290	137	2.984	139	3.159	152	3.464	159	4.156	162	4.164
Philippines	43	1.263	41	1.488	43	2.184	47	2.363	48	3.566	47	4.662	53	5.098	55	5.029
Taiwan	443	46.116	460	58.297	487	59.032	534	53.437	554	59.192	570	62.286	577	58.049	602	63.147
Africa	884	69.417	904	106.261	943	141.615	947	124.976	967	145.150	1.062	142.868	1.171	146.474	1.327	122.068
South Africa	884	69.417	904	106.261	943	141.615	947	124.976	967	145.150	1.062	142.868	1.171	146.474	1.327	122.068

*Year-end data are not available. Data are as of September.

NA = not

Note: Regulated open-end funds include mutual funds, exchange-traded funds (ETFs), and institutional funds. New Zealand and Trinidad and Tobago include home- and foreign-domiciled funds. Croatia, France, Ireland, Netherlands, Norway, and N/A = not available

Note: Components may not add to the total because of rounding. Regulated open-end funds include mutual funds, exchange-traded funds (ETFs), and institutional funds. New Zealand and Trinidad and Tobago include home- and foreign-domiciled funds. Croatia, France, Ireland, Netherlands, Norway, and Slovakia include funds of funds. Prior to 2014, Finland, Germany, Italy, Luxembourg, Romania, Spain and Switzerland include funds of funds. After 2013, Japan includes funds of funds. Prior to 2014, ETFs and other non-UCITS are not included in European data. Prior to 2013, institutional funds are not included in data for Japan.

Source: Own elaboration based on (ICI - Investment Company Institute, 2016 (I)) and (ICI - Investment Company Institute, 2016 (II)).

Table 2: Worldwide numbers & total net assets of regulated open-end funds, also provides a rough overview of the current situation of the European Fund Industry with its core markets. Europe is the second-largest region following the United States with nearly one-third of the world's assets. Investment funds are the most attractive segment in the European investment market. In recent years the national European Fund Markets have attracted a growing investor's interest and therefore consequently achieved high growth rates. With around 30% of the European assets, Luxembourg is the largest European Fund Market.²³

²³ Cf. (Pozen, Hamacher, & Philipps, 2015), p.452ff.

Several reasons exist for making this segment very attractive for investors. Typically investment funds are being recognized as savings products. In several countries certain funds have been ranked alongside life and pension insurance products and legal and tax changes have been made to allow funds to be used as part of such insurance vehicles.²⁴

Throughout history investment funds achieved high returns in the 1990s, increasing the appeal for investors.²⁵ Another reason for the impressive size of fund assets are findings from scientific studies of the financial markets, which have also been made public to a broader audience. These results verify that it is possible to pursue a successful and systematic investment strategy by using funds. This applies to mutual funds as well as to any other fund investment.²⁶

In 1990, Professors H. Markowitz, W. Sharpe and M. Miller were awarded a Nobel Prize for their work in the sphere of quantitative financial market research and company valuation. Their findings regarding the avoidance of the unsystematic (= security specific) risk in relation to securities and consideration of the question of how much diversification contributes to the risk management of a portfolio were of particular relevance for investment funds.²⁷

Nowadays stepped-up sales strategies on the part of fund providers promote the business. The big European and US-providers of investment funds cover all the major European Fund Markets today. While every big bank used to offer its clients exclusively in-house funds, the fund market is moving towards open architecture. In other words, banks also sell clients funds from other fund providers. This is leading to fierce competition among this group.²⁸

As a result banks are promoting investment funds because they are attractive for both, clients and for the banks themselves. With a low level of risk, clients receive returns in line with the market, while the banks secure an attractive income in commissions.²⁹

²⁴ Cf. (Haan de, Oosterloo, & Schoenmaker, 2012), p.251ff.

²⁵ Cf. (Jones, 2010), p.71.

²⁶ Cf. *ibid*, p.51ff.

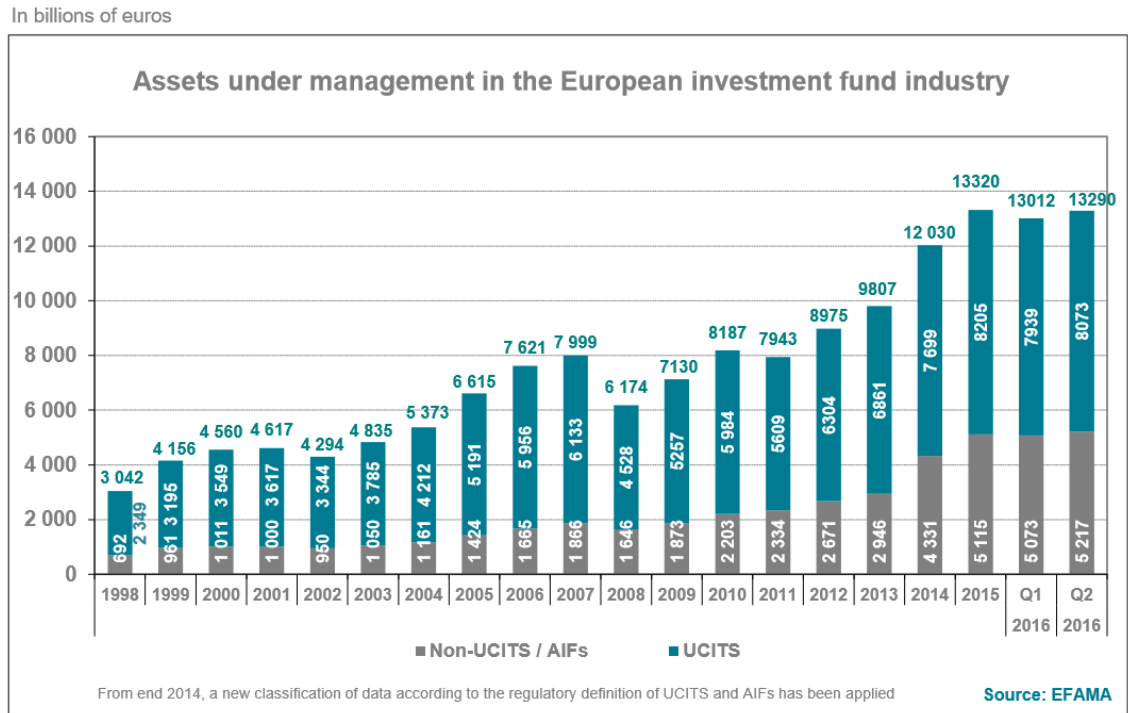
²⁷ Cf. (Mathonet & Meyer, 2007), p.317f.

²⁸ Cf. (Fasnacht, 2009), p.98f.

²⁹ Cf. (Gitman, Joehnk, & Billingslex, 2011), p.436ff.

Below stated Figure 3: Assets under management in the European investment fund industry, provides an understanding of the most important developments within the European Fund Sector and indicates the latest available figures on the market segment:

Figure 3: Assets under management in the European investment fund industry

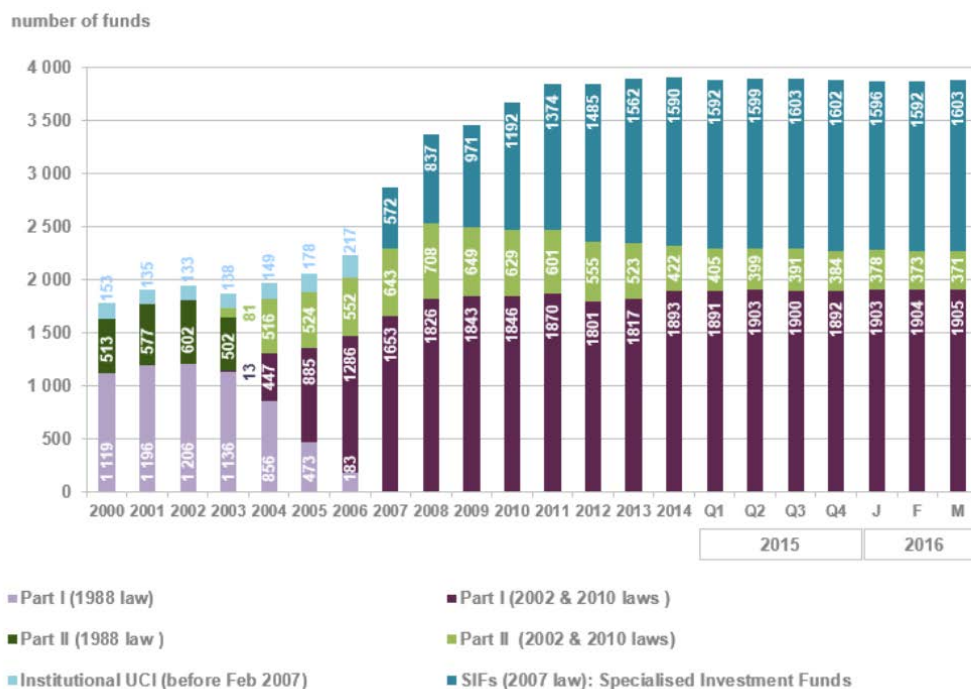


Source: Cf. (ALFI - Association of the Luxembourg Fund Industry, 2016 (II)).

Figure 3: Assets under management in the European investment fund industry, indicates that an increasing interest in non-UCITS/AIFs is predominant. This growing interest should be analyzed with a focus on Luxembourg. The difference between UCITS and Non-UCITS/AIFs regarding the regulatory requirements as presented needs to be mentioned as it will play a role in the following chapters.

In Figure 4: Legal status of Luxembourg domiciled investment funds, an overview of the most common used legal status and their development between the years 2000 and 2016 is presented:

Figure 4: Legal status of Luxembourg domiciled investment funds



Source: Cf. (ALFI - Association of the Luxembourg Fund Industry, 2016 (III)), para. 8.

It is important to point out that the development of the SIF since the introduction of this legal form in 2007. Since then nearly 60% of all new funds were created as SIFs. This seems to be a confirmation of the success of this vehicle in Luxembourg and confirms the raising demand for new structures. At the end of the first quarter 2016 SIFs accounted for 41.3% of the Luxembourg market. The most popular legal structures since 2012 were the 'Société d'Investissement en Capital Variable' (SICAV) representing 55.8% of funds while the 'Fonds Commun de Placement' (FCP) only represents 43.1% of the current market share.³⁰

This short overview of the current situation on the investment fund market is followed by the explanation of the Luxembourg Fund Market potential and a differentiation between the different legal regimes in Luxembourg. Therefore the next chapters provide an insight in the history of the Luxembourg Fund Market and its potential as well as an introduction of investment funds as specific investment instruments and their legal forms and legal structures.

³⁰ Cf. (ALFI - Association of the Luxembourg Fund Industry, 2016 (III)), para.8.

2.1. Market potential

This chapter shall provide an overview of Luxembourg market potential on order to provide a basic understanding of its position as the key player in Europe and the reasons for its focus on the fund industry.

Located in the heart of Europe, one of the most successful financial centers in Western Europe, between France and Germany, Luxembourg was founded in 963. The country with an area of only 2586 square kilometers³¹ shares borders with Germany to the east, Belgium to the west and France to the south. Being part of the Benelux group, along with Belgium and Netherlands, Luxembourg has had a fully integrated monetary and economic union with its larger neighbor Belgium. 1948 Luxembourg entered into the Benelux Customs Union and became a chart member of the North Atlantic Treaty Organization (NATO) in 1949. Luxembourg was one of the six founding countries of the European Economic Community in 1957, which later become the EU introducing the Euro currency area. Even if Luxembourg has been performing banking activities internationally since the end of the 19th century, Luxembourg was not a financial center until about 32 years ago.³²

This rapid development brings advantages today: Located in the heart of Europe it brings from a business and customer base view the advantage that "...within driving distance all major European business centers"³³ it can be reached. "Around 40% of the European Union's wealth is concentrated in a 500km area around Luxembourg, extended to 700km, this figure rises around 70%".³⁴

Luxembourg is the largest fund domicile in Europe by far and its investment fund industry is the second largest in the world after the US.³⁵ In August 2016 a new all-time record has been reached. The total the amount of EUR 3,6tn of net assets under management in Luxembourg has been exceeded.³⁶ Spoken in figures, actually more than 3,900 funds with more than 14,000 sub-funds³⁷ are distributed in more than 70 countries worldwide with a particular focus on Europe, Asia, the Middle East and the

³¹ Cf. (Le Gouvernement du Grand-Duché de Luxembourg, 2016 (I)), para.1.

³² Cf. (Crouch, Nolan, & Sola, 2010), p.157ff.

³³ (PWC - Luxembourg, 2015 (I)), p.10.

³⁴ Ibid.

³⁵ Cf. (Luxembourg for Finance, 2016 (I)), para. 1f.

³⁶ Cf. (ALFI - Association of the Luxembourg Fund Industry, 2016 (IV)), para. 1.

³⁷ Cf. (Ernst & Young S.A., Luxembourg, 2016 (I)), p. 6.

Americas. Related to the fund initiators, the main countries of origin are US, United Kingdom, Switzerland and France.³⁸

With regards to fund regulation and financial authorities Luxembourg has shown important characteristics that are unique. The responsible authority before January 1st, 1999 “for supervision and control of the financial sector in Luxembourg is the IML – Institut Monétaire Luxembourgeois – a creation of the 1983 law³⁹ to regulate Undertakings for Collective Investment, which first appeared in 1959.”⁴⁰

By the Law of 30 March 1988⁴¹ Luxembourg was the first EU Member State that transposed the 1985 UCITS – Undertakings for Collective Investments in Transferable Securities - directive into national law and legislation and positioned it to take advantage of the cross-border marketing opportunities available to complying funds. This directive refers to the European Directive EC 85/611/EEC⁴² from December 1985 which aimed at offering more effective protection to the investors and to facilitate cross-border offerings on investment funds to retail investors within the EU. This transition was one of the keys for securing its status as key player within Europe. Furthermore this directive provided the cornerstone for all amendments of regulations onwards.⁴³

“The law has been updated by IML Circular of 29 January 1991 and extended by further legislation – Law of 19 July 1991 – relating to UCIs for institutional investors and the Law of 8 June 1999 concerning pension funds.”⁴⁴

The novelty of implementing the the 1988 Law where several regulatory rules and controlling procedures within the EU for investing into open-ended funds. Furthermore the law permits funds to be established as either common investment funds FCP or as investment companies (SICAV or SICAF).⁴⁵

³⁸ Cf. (PWC - Luxembourg, 2015 (I)), p.9.

³⁹ Cf. Law of 19th July 1983 (Fiduciary Assets).

⁴⁰ (Russell, 2007), p.59.

⁴¹ Law of 30th March 1988 (Undertakings for Collective Investment in Transferable Assets).

⁴² Cf. Council Directive 85/611/EEC of 20 December 1985 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS).

⁴³ Cf. (International Business Publications, USA, 2013), p.129.

⁴⁴ Cf. (Russell, 2007), p.59f.

⁴⁵ Cf. *ibid*, p.60.

Since January 1st, 1999 authorizations and routine approvals and supervision are in the responsibility of the CSSF. Prior to the CSSF and after the IML, the Luxembourg Central Bank has also been responsible between June 01st 1998 and December 31st 1998. Together with other centers, Luxembourg has meanwhile updated its laws to align with the EU UCITS Directive III⁴⁶ by the Luxembourg Law of 20 December 2002 and EU UCITS Directive IV⁴⁷ by the Luxembourg Law of 17 December 2010.⁴⁸

The latest update was the EU directive 2014/91/EU commonly known as UCTIS V transposed by the Luxembourg Law of 10 May 2016 and modifying EU directive 2009/65/EC.⁴⁹

“Like Ireland, Luxembourg is primarily an administrative center for funds that are targeted at investors elsewhere in Europe, but having been the first to capitalize on the UCITS Directive, Luxembourg has three to four times the value of funds under management than Dublin’s IFSC and has currently pulled ahead of France for leadership of the European league table.”⁵⁰

The competence of Luxembourg combined with its flexible and accessible financial and legislative authorities and improvements is constantly attracting new developments.

More than 32 years of experience in the fields of adaption and development to the newest directives combined with a strong legislation is continuing to attract investors, initiators and institutions for new products and services. The result is market

⁴⁶ Cf. Directive 2001/108/EC of the European Parliament and of the Council of 21 January 2002 amending Council Directive 85/611/EEC on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS), with regard to investments of UCITS and Directive 2001/107/EC of the European Parliament and of the Council of 21 January 2002 amending Council Directive 85/611/EEC on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) with a view to regulating management companies and simplified prospectuses.

⁴⁷ Cf. 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).

⁴⁸ Cf. (Turner, 2004), p.210 and (Russell, 2007), p.60.

⁴⁹ Law of 10 May 2016, - transposing Directive 2014/91/EU of the European Parliament and of the Council of 23 July 2014 amending Directive 2009/65/EC on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) as regards depositary functions, remuneration policies and sanctions; amending: the Law of 17 December 2010 relating to undertakings for collective investment, as amended; the Law of 12 July 2013 on alternative investment fund managers, as amended.

⁵⁰ (Russell, 2007), p.60.

leadership in Europe with a variety of regulated and unregulated instruments that are available to all investors and meets their expected requirements.

This demonstrates very well the diversified areas of expertise that developed within Luxembourg. These, to name only the most important in regards of this thesis, are Asset Management, Investment Funds, Wealth Management, Structured Finance, Corporate Banking, Insurances & Reinsurances and a growing business related to Asia - the Renminbi Business.⁵¹

Further advantages of Luxembourg to be mentioned are the financial and fiscal stability as well as the stable political and economic situation.⁵² “Luxembourg is a highly stable EU member State with sound public finances, relatively low government debt and low public deficits, which are the best guarantee for fiscal stability.”⁵³

Ensured by a strong macro-economic growth consistently above the EU average growths rate Luxembourg reports the world’s lowest debt-to-GDP ratio, also contributing to fiscal stability.⁵⁴

In relation to EU member states: “The highest ratios of government debt to GDP at the end of the second quarter of 2016 were recorded in Greece (179.2%), Italy (135.5%) and Portugal (131.7%), and the lowest in Estonia (9.7%), Luxembourg (22.0%) and Bulgaria (29.4%).”⁵⁵ Figure 5: Government debt to GDP ratio, 2016 Q2 in percentage, illustrates these data.

⁵¹ Cf. (Luxembourg for Finance, 2015 (I)).

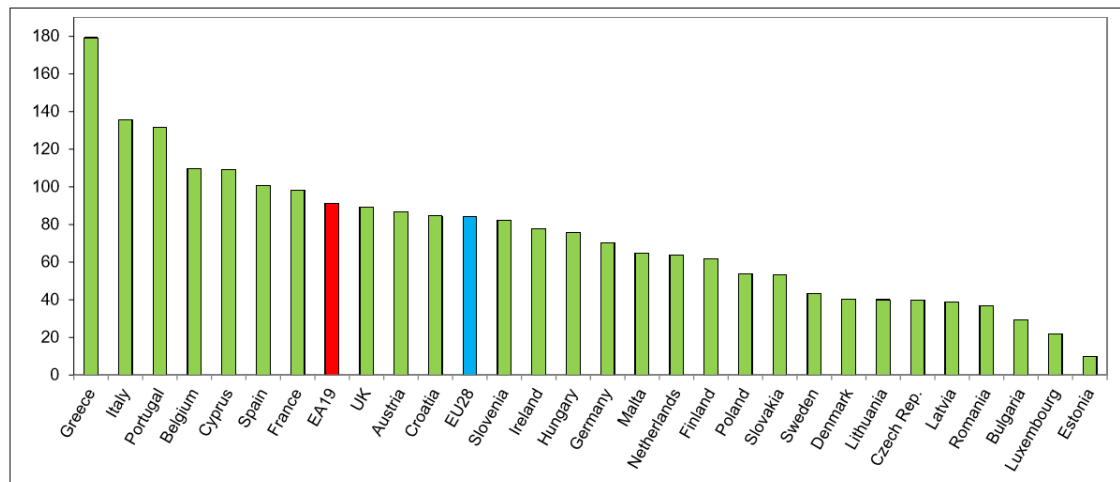
⁵² Cf. (ALFI - Association of the Luxembourg Fund Industry, 2013 (I)), p.4f.

⁵³ (ALFI - Association of the Luxembourg Fund Industry, 2010 (I)), p.8.

⁵⁴ Cf. (Luxembourg for Business & Innovation, 2016 (II)), para.1.

⁵⁵ Cf. (European Commission - Eurostat, 2016 (I)), para.2.

Figure 5: Government debt to GDP ratio, 2016 Q2 in percentage



Source: Cf. (European Commission - Eurostat, 2016 (I)), para.2.

In terms of the EU Luxembourg is a founding member, an EU capital and a parliamentary representative where, e.g. the European Investment bank, the ESM European Stability Mechanism, the European Court of Justice, the European Court of Auditors, the European Parliament Secretariat are settled.⁵⁶

This is also a sign why Luxembourg is still one of the few European countries which received an AAA rating confirmed by Standard & Poor's, Moody's and Fitch. Its stable banking sector combined with the stable political, social and economic environment verify this rating.⁵⁷

Luxembourg profits from a unique concentration of highly experienced investment fund experts, fund lawyers, audit firms and tax advisors in terms of cross-border registrations for both UCITS and non-UCITS funds. Luxembourg can profit in all relevant aspects of product innovation and development, administration and distribution from this experience.⁵⁸

Another important aspect is the workforce Luxembourg can profit from. At the moment Luxembourg has 576,000 inhabitants, whereof 46.7% are foreigners of more than 170 nationalities.⁵⁹ Each day around 166,000 cross-border employees commute to Luxembourg in order to perform their jobs within Luxembourg whereof

⁵⁶ Cf. (Le Gouvernement du Grand-Duché de Luxembourg, 2016 (II)).

⁵⁷ Cf. (Feld, 2016 (I)), p.4.

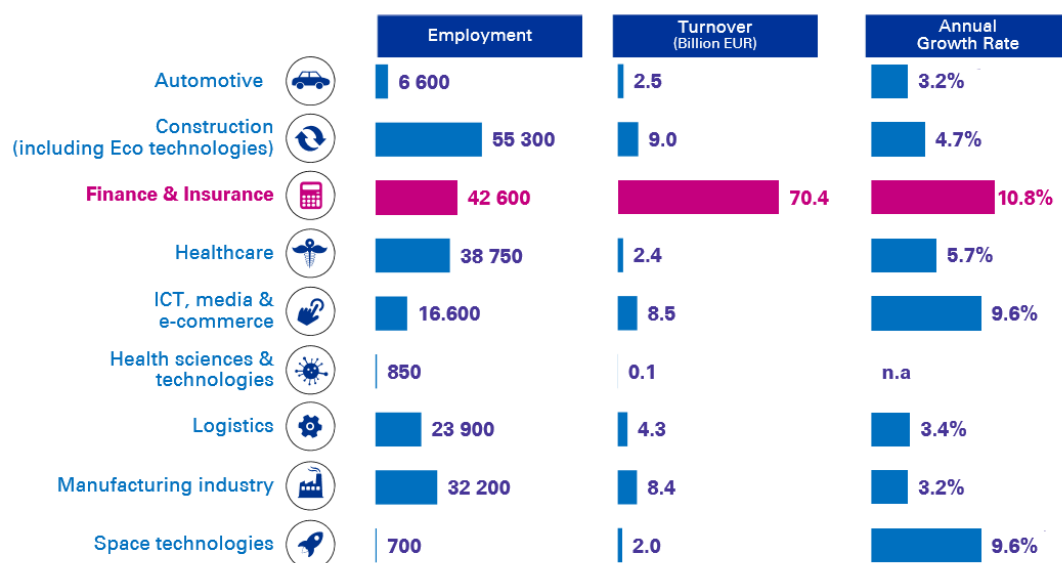
⁵⁸ Cf. (ALFI - Association of the Luxembourg Fund Industry, 2013 (I)), p.5.

⁵⁹ Cf. (Le Gouvernement du Grand-Duché de Luxembourg, 2016 (III)), para.1.

17% of all employees work in the financial sector. A high quality of life attracts high-skilled multicultural and multilingual professionals from around the world. The multilingual setup is another characteristic that helps integrating these foreigners because Luxembourgish, German and French are considered as official languages and more than 75% of Luxembourgers are able to speak English. The combination of living quality, social security coverage, public infrastructure, rewarding packages and the gateway to European careers have attracted highly skilled profiles.⁶⁰ Additionally, Luxembourg was ranked by Education First as 8th best worldwide for English proficiency allowing with the prevailing languages a best possible multilingual communication with authorities and legislations as well as foreigners and business partners worldwide.⁶¹

Figure 6: Importance of the financial sector, indicates that the finance and insurance sector are major contributors to the Luxembourg economy. In this area more than 42'600 professionals being employed, generating a turnover of EUR 70.4 bn.

Figure 6: Importance of the financial sector



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Source: Cf. (Feld, 2016 (I)), p.10.

⁶⁰ Cf. (PWC - Luxembourg, 2015 (I)), p.12.

⁶¹ Cf. (Feld, 2016 (I)), p.4.

In summary, Luxembourg has lots of potential for its fund industry. In order to examine this in more detail, the different fund regimes will be presented in the following sections. This aims at providing the basic understanding of the current situation and prepares the route for the introduction of the RAIF.

2.2. Investment funds and their regimes

Before diving into the detailed illustration of the different fund regimes currently present in Luxembourg a brief overview of the functionality of an investment fund is given. Therefore, in order to understand the purpose of an investment fund the meaning of investment needs to be defined, at first.

Investment is assessed on the basis of the following three criteria, which can compete with one another in some instances. These three criteria are income (less costs), security and liquidity. None of the three investment goals income, security and liquidity can be maximized without affecting the other two. Unfortunately, there is no such thing as an investment that is capable of realizing sizeable profits and income at the same time, whilst offering absolute security and a high level of liquidity.⁶²

In this regard investment funds offer an optimum solution to the conflict between the investor's goals. Regarding the income investment funds provide the investor with income in line with the market. Security means hereby the broad diversification of investments and professional fund management providing investors with risk diversification in the investment category that they have opted for. Liquidity in hereby the possibility to return the fund's units to the management company at almost any time, mostly free of charge and receive the equivalent cash in return.⁶³

An investment fund is a vehicle with the purpose to collect money from investors. The raised money is used for a special investment purpose defined in the fund's distribution document or its prospectus. Funds allowing retail or institutional investors to participate in the security markets by pooling smaller amounts of money into larger amounts for investments or investment strategies that would otherwise not be

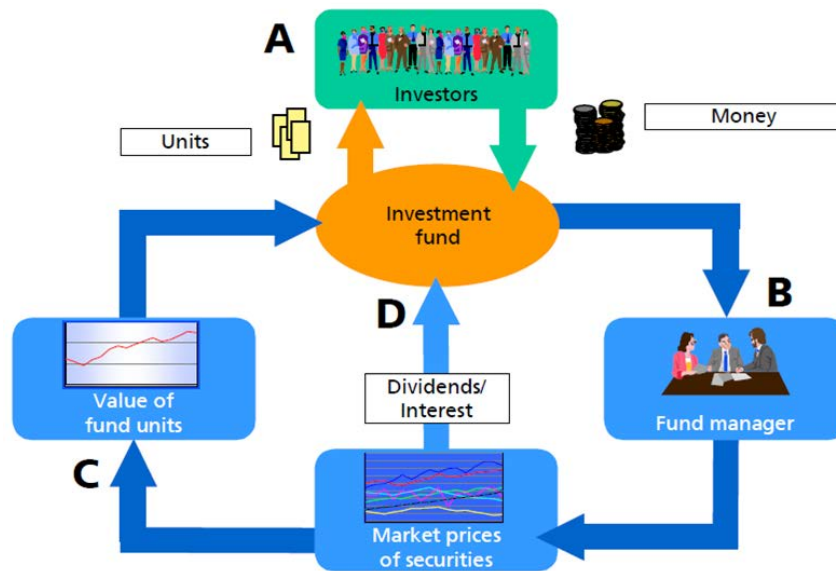
⁶² Cf. (Heckmair, 2009), p.25f.

⁶³ Cf. (Foitzik, 2003), p.169ff.

feasible. Summarized, an investment fund combines the investments of many investors with the same investment objective in one portfolio. The entire money raised constitutes the fund's assets.⁶⁴

In order to provide a basic understanding of the operational principles of an investment fund the following Figure 7: Actors and functions of an investment fund, displays the actors and functions:⁶⁵

Figure 7: Actors and functions of an investment fund



Source: Own elaboration based on Mark St. Giles, Ekaterina Alexeeva and Sally Buxton: "Managing Collective Investment Funds" (Chichester, West Sussex, UK: John Wiley & Sons Ltd., 2003), p. 30.

Step A illustrates the collection of monies from the different investors. In return the investors receive shares or units from the fund according to their proportion of the fund's total assets and become a shareholder of the structure. The fund assets are also referred to as the fund portfolio. Because fund units are often available in small denominations, clients can use investment funds to participate in a large number of different investments even by only contributing a small sum.⁶⁶

Step B involves the professional fund managers who decide in which assets to invest according to the investment policy of the fund. They monitor the development of the

⁶⁴ Cf. (Gremillion, 2005), ch.1.

⁶⁵ Cf. (St. Giles, Alexeeva, & Buxton, 2003), p.28ff.

⁶⁶ Cf. (Dampier, 2015), ch.3.

portfolio and reallocate the assets if necessary. The investment policy stipulates which investment universe to invest in in.⁶⁷

Step C: The fund assets are valued on a regular basis defined in the prospect using the latest available prices of the assets. They are composed of securities bank balances and other assets. From the total sum of assets the fund's liabilities are deducted accounting for the net fund assets. Dividing the net fund assets of each fund by the number of units issued values the current price per fund unit also known as net asset value (NAV). The fund prices which are published in the print and electronic media usually represent the NAV per unit. The NAV is the intrinsic value of the fund. It is not based on the supply of and demand for specific fund units, but on the stock market price of the securities held in the fund.⁶⁸

The NAV calculation is undertaken by the fund accounting company using the following formula shown in Figure 8: Net Asset Value - NAV:

Figure 8: Net Asset Value - NAV

	Securities
+	Bank balances
+	Other assets
	TOTAL FUND ASSETS
-	Liabilities
	NET FUND ASSETS
:	Number of units
=	NET ASSET VALUE PER UNIT (NAV)

Source: Own elaboration based on G. Timothy Haight, Stephen O. Morrell and Glenn E. Ross: "How to Select Investment Managers & Evaluate Performance" (Hoboken, New Jersey, USA: John Wiley & Sons Inc., 2007), p.208.

Step D: Dividends and interest paid by the individual securities or received from bank balances are collected by the fund and added to the fund's assets on an ongoing basis. These earnings are either distributed to the investors on a defined basis or remain in the fund increasing the NAV. On the one hand, the income of the fund is made up of interest and dividends or in the case of real estate funds, primarily of

⁶⁷ Cf. (Drake & Fabozzi, 2010), p.7.

⁶⁸ Cf. (Little, 2007), p.243ff.

rental income. On the other hand, funds realize capital gains and losses as a result of the price difference between the purchase and selling price of investments within the fund.⁶⁹

Funds can take various legal forms in different countries and have a wide range of purposes. In this assignment the focus is set on the Luxembourg Fund Industry. After illustrating the general functionality of an investment fund the next chapter introduces the set up options of a fund structure.

2.2.1. Legal forms and organizational structures

For the setup of an investment fund it is important to make the right decisions regarding the following three structural questions which consider the choice of legal setup, the operating structure and the management structure.⁷⁰

There is a legal and regulatory distinction between funds that are set up on a contractual basis and those that are corporations with their own legal identity. On the one hand an investment fund can be setup as FCP (contractual fund/fonds commun de placement), but the FCP itself is not a legal entity and based on a contract between the fund manager or the Management Company (ManCo) and the Investors named investment or fund contract.⁷¹ Because the FCP is no legal entity, it must be managed by a ManCo.⁷²

In the contract the fund management is bound to allow investors to participate in the fund in proportion to the units they own. The fund management manages the fund's assets independently and in its own name, according to the stipulations of the fund contract. The contract sets down the rights and duties of the investor, the fund

⁶⁹ Cf. (Jacobs, 2012), p.140f.

⁷⁰ Cf. (Gremillion, 2005), ch.1 and (St. Giles, Alexeeva, & Buxton, 2003), p.27.

⁷¹ Cf. (ALFI - Association of the Luxembourg Fund Industry, 2017 (I)), para. 3.

⁷² Cf. Law of 17 December 2010 transposing 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); amending: the law of 20 December 2002 relating to undertakings for collective investment, as amended; the law of 13 February 2007 relating to specialised investment funds, as amended; Article 156 of the law of 4 December 1967 on income tax.

management company and the custodian bank. The fund contract has to be approved by the supervisory authorities.⁷³

As already mentioned above, an FCP has no legal personality and must be managed by a ManCo incorporated in Luxembourg, subject to chapter 15 or chapter 16 of the 2010 Law.⁷⁴ The ManCo can delegate parts of its functions to investment managers located in Luxembourg or abroad. Unitholders of the FCP, who have their liability limited to the amounts contributed by them to the FCP, are not, in principle, entitled to rights akin to shareholder rights in a company.⁷⁵

The ManCo can “[...] be incorporated as a public limited company, a private limited company, a cooperative company, a cooperative company set up as a public limited company or a corporate limited partnership”.⁷⁶

On the other hand, an investment fund can be established in form of an investment company that is a legal entity. Available company forms are the SICAV (Investment Company with variable capital/Société d’investissement à capital variable) and the SICAF (Investment Company with fixed capital/Société d’investissement à capital fixe).⁷⁷ The SICAV or SICAF may be self-managed or appoint a ManCo.⁷⁸

For the choice of a corporate structure there are restrictions for the setup as FCP, SICAV or SICAF, depending if the fund will be established under UCITS or in form of an alternative investment fund. “The SICAV is formed as a Public Limited Company (PLC., Corp./SA). In contrast, the SICAF can be formed as a corporation in Luxembourg in the form of the Public Limited Company (PLC., Corp./SA), Limited Liability Company (LLC., Ltd./SARL), Partnership Limited by Shares (SCA) or Co-operative in the form of the Public Limited Company (SCOSA).”⁷⁹

Another aspect is that not all investors are qualified to invest in all available structures. In Luxembourg restrictions related to alternative fund investments for investors may also apply. For all unregulated or lightly regulated products the investment is limited to well-informed investors who are able to understand the given

⁷³ Cf. (ALFI - Association of the Luxembourg Fund Industry, 2017 (I)), para.3.

⁷⁴ Cf. (ALFI - Association of the Luxembourg Fund Industry, 2015 (I)), p.10.

⁷⁵ (ALFI - Association of the Luxembourg Fund Industry, 2015 (I)), p.10.

⁷⁶ (CSSF - Commission de Surveillance du Secteur Financier, 2010), art.101.

⁷⁷ Cf. *ibid.*

⁷⁸ Cf. (Luxembourg for Finance, 2016 (III)), para.4.

⁷⁹ (LCG International AG, 2013), p.4.

risks with an investment in such fund structures.⁸⁰ Well-Informed Investors are defined as:⁸¹

- an institutional investor
- a professional investor investing within the meaning of Annex II to the MiFID
- an investor who has adhered in writing to the status of a well-informed investor and complies with one of the following conditions:
 - investment of at least EUR 125,000 in the fund
 - his expertise is confirmed by a banking institution, by an investment firm as defined in the MiFID or by a management company as defined in the UCITS IV Directive”

Figure 9: Corporate forms available in Luxembourg, delivers an illustrative comparison of the corporate forms and their restrictions under the respective regimes.

Figure 9: Corporate forms available in Luxembourg

Regulated		
UCITS (“Part I Fund”)	Part II Fund with registered AIFM	Part II Fund with authorised AIFM
SICAV (SA) SICAF (SA, SCA)	SICAV (SA) SICAF (SA, SCA, Sàrl, SCS, SCSp)	SICAV (SA) SICAF (SA, SCA, Sàrl, SCS, SCSp)
FCP	FCP	FCP
All three must be open-ended.	Structures may be open or closed-ended.	Structures may be open or closed-ended.

Lightly regulated	
SIF with registered AIFM	SIF with authorised AIFM
SICAV / SICAF (SA, SCA, Sàrl, SCoSA, SCS, SCSp)	SICAV / SICAF (SA, SCA, Sàrl, SCoSA, SCS, SCSp)
FCP	FCP
Structures may be open or closed-ended.	Structures may be open or closed-ended.

SICAR with registered AIFM	SICAR with authorised AIFM
Corporate entity with fixed or variable share capital (SA, SCA, Sàrl, SCoSA, SCS, SCSp)	Corporate entity with fixed or variable share capital (SA, SCA, Sàrl, SCoSA, SCS, SCSp)
Structures may be open or closed-ended.	Structures may be open or closed-ended.

RAIF only with authorised AIFM
SICAV / SICAF (SA, SCA, Sàrl, SCoSA, SCS, SCSp)
FCP
Structures may be open or closed-ended.

Unregulated		
SOPARFI	SPF	SV
(SA, SCA, Sàrl, SCoSA, SCS, SCSp)	(SA, SCA, Sàrl, SCoSA, SCS, SCSp)	(SA, SCA, Sàrl, SCoSA, SCS, SCSp) or securitisation fund

Source: Own elaboration based on (KPMG - Luxembourg, 2016 (I)), p.6; and (Bonn Steichen & Partners, 2014), p.22ff.

⁸⁰ Cf. (Peter & Whelan, 2013), p.105.

⁸¹ (Bonn Steichen & Partners, 2012), p.37.

With the implementation of the AIFMD⁸², a number of amendments to the 1915 Law⁸³ have been introduced in order to modernize the Luxembourg limited partnership regime.

Under the new regime, two forms of Luxembourg LPs are available:⁸⁴

“In Luxembourg, the management supervision introduced by the AIFMD has come as an additional layer of supervision on top of the existing Luxembourg product supervision. In certain circumstances, the double layer of supervision may seem excessive, in particular for funds targeting sophisticated investors. The risk of Luxembourg appearing as an overly protective fund domicile has been identified in the early days of the implementation of the AIFMD. In order to mitigate that risk, the Luxembourg limited partnership (LP) regime has been modernised in the context of the implementation of the AIFMD. This modernisation process involved a complete revamping of the rules applicable to the common limited partnership (société en commandite simple, SCS) and the creation of a new form of LP without legal personality: the special limited partnership (société en commandite spéciale, SCSp). SCSs and SCSpS are used for the structuring of regulated (SIFs and SICARs) as well as unregulated investment vehicles. The fact that an SCS/SCSp may avoid product regulation/supervision does not necessarily mean that it falls outside the supervision of regulators. Unless it benefits from an AIFMD exemption, an unregulated SCS/SCSp that is an AIF must be managed by an authorised AIFM, and is therefore indirectly subject to regulatory oversight through its AIFM.”

In summary, the SCS and the SCSp are limited partnership forms. The SCSp is comparable to a UK Limited Partnership (LP) without a legal personality, while the SCS is similar to a Scottish LP having a legal personality. Both are corporate forms, rather than regulatory statuses. In essence SCS/SCSp can be used for the structuring of regulated vehicles, e.g. a regulated SCS/SCSp can be subject to either the SIF Law, the SICAR Law, the RAIF Law or Part II of the 2010 Law or be an unregulated investment vehicles on its own.

⁸² Cf. Chapter 2.2.3.

⁸³ Cf. Loi du 10 août 1915 concernant les sociétés commerciales.

⁸⁴ Cf. (Allen & Overy, 2015), p.2.

This provides the following advantages:⁸⁵

“Confidentiality of the identity of limited partners is ensured.

•Management of the limited partnership is entrusted to one or more managers, who may or may not be unlimited partners.

•A limited partner does not lose the benefit of its limited liability if it takes actions which are internal to the limited partnership.

•Partnership interests may be represented by securities or partnership accounts.

•No statutory restrictions on the following topics (which may be freely organised in the partnership agreement):

-Issue and reimbursement of partnership interests;

-Entitlement of partners to the profits and losses of the limited partnership;

-Distributions to partners, whether under the form of a distribution of profits or a reimbursement of partnership interests;

-Voting rights;

-Transfer of partnership interests.”

Table 3: Comparison of the most popular corporate forms in Luxembourg, provides an overview about the most popular corporate forms for investment funds available in Luxembourg and their advantages in comparison.

⁸⁵ Cf. (ALFI - Association of the Luxembourg Fund Industry, 2015 (I)), p.13.

Table 3: Comparison of the most popular corporate forms in Luxembourg

	Public limited company (SA)	Private limited company (Sàrl)	Corporate partnership limited by shares (SCA)	Common/special Limited partnership (SCS/SCSp)
Incorporation	Notarial deed required	Notarial deed required	Notarial deed required	Notarial deed required
Minimum capitalisation (at incorporation/launching)	EUR 31,000	EUR 12,500	EUR 31,000	No capital required
Shareholders/ Partners	≥1	1 to 40	Limited partners: ≥ 1 Unlimited partners: ≥ 1	Limited partners: ≥ 1 Unlimited partners: ≥ 1
Liabilities	Shareholders' liability is limited to the amount of their participation	Shareholders' liability is limited to the amount of their participation	Limited partners' liabilities: Limited to the amount of their participation	Limited partners' liabilities: Limited to the amount of their participation
Liabilities			Managing general partner(s)' liability: Unlimited	Managing general partner(s)' liability: Unlimited
Management	One-tier management structure with a board of ≥3 directors (if there is more than one shareholder) or two-tier management structure with a management board and a supervisory board	≥1 manage	≥1 manager which does not have to be an unlimited partner	≥1 manager which does not have to be an unlimited partner

Source: Own elaboration based on (ALFI - Association of the Luxembourg Fund Industry, 2015 (I)), p.17ff.

With regard to the operating structure 'open-ended' or 'closed-ended' the fund's legal structure needs to be chosen. With open-end funds, investors may continuously subscribe new units and may also return units to the ManCo. The number of outstanding units open-end fund variable and the fund assets are accordingly open for the issuance of new units and for redemptions of distributed units,⁸⁶ based on the known NAV⁸⁷. Closed-end funds, on the other hand, comprise a precisely determined number of units. The fund is issued for subscription in one single offering.⁸⁸

A further aspect is related to the umbrella structure: "Many Luxembourg investment funds are so-called umbrella funds, which consist of multiple sub-funds that in effect function as separate investment funds but form a single legal entity. This enables

⁸⁶ Cf. (International Monetary Fund, 2014), p.70.

⁸⁷ Cf. (Lovicsek & Anderson, 2004), p.58.

⁸⁸ Cf. *ibid*, p.58ff.

funds with different strategies or that are designed for different types of investor to be established within the same legal structure, which can reduce the funds' costs.”⁸⁹

Any number of sub funds within the same category (e.g. the various Luxembourg Money Market Funds) may, e.g. be managed in Luxembourg or in Switzerland under a common “umbrella”. These sub funds are also referred to as compartments, or segments. New compartments may be established as required at little cost. This makes things easier for the fund ManCo.⁹⁰

In order to guarantee the best capital investment a good management structure is important. In order to understand and manage the current economic developments, stock exchange prices must be continuously monitored and the composition of the fund assets needs to be constantly adjusted to match current market circumstances. In addition to specialist knowledge, this takes a lot of time. With investment funds, trained professionals take care of all analytical and administrative tasks, for example:⁹¹

- Observation and analysis of companies, security prices and exchange rates, as well as of the financial markets
- Analysis of the current composition of the fund assets
- Making decisions to buy or sell and placing and monitoring instructions to buy and sell
- Custody of the securities within the fund
- Redemption of coupons on the securities within the fund
- Keeping accounts in relation to the money and securities making up the fund assets

Choosing the right management strategy is another important point. There is a difference between actively and passively managed funds. Some investment funds have active management whereas others adopt a passive approach. The term management strategy is often being used to express this distinction. With active

⁸⁹ (ALFI - Association of the Luxembourg Fund Industry, 2012), para.4.

⁹⁰ Ibid.

⁹¹ Cf. (Szylar, 2012), ch.5.1.1.

management, the fund manager tries to outperform the prescribed comparative index (bench-mark) while deliberately deviating from the reference index in his stock selection. The additional effort requires to obtain information and is reflected in additional charges. However, with a passively managed portfolio or one managed based on an index, the aim is to mirror the index's risk/return profile exactly. The portfolio management is consequently cost-effective and delivers the index yield fairly precisely.⁹²

In a last step it is important to define the distribution respectively the reinvestment policy of the investment funds. A distinction has to be made in respect of how fund income is dealt with:⁹³

- Distributing funds
- Reinvesting funds
- Distributing funds with automatic, commission-free reinvestment.

Distributing funds offer the advantage that the investor has access to the income from the fund at least once a year. Distributions from funds take place at the ex-date, and are payable at the value date. The reason why for example under Swiss law, reinvesting funds are not practical is due to the withholding tax. This tax has to be deducted from the income. If units were redeemed, the custodian bank would have to retrospectively charge interest in arrears for the entire holding period. Since reinvesting funds retain all income, the unit value increases in accordance with the income retained. As in the case of a savings account, there is a compound interest effect over the years.⁹⁴

Regarding the regulatory requirements there is a difference between the regimes of UCITS and Non-UCITS or so called Alternative Investment Funds. This differentiation is based on provisions concerning the minimum risk distribution in the corresponding investment funds. These rules differ from country to country. "In 2004 and 2007 Luxembourg created the Investment Company in Risk Capital (SICAR) and

⁹² Cf. (Little, 2007), p.246f.

⁹³ Cf. (ALFI - Association of the Luxembourg Fund Industry, 2012), para.6.

⁹⁴ Cf. (ALFI - Association of the Luxembourg Fund Industry, 2012), para. 3, see also (Dembowski, 2011), p.29ff.

the Specialised Investment Fund (SIF) in anticipation of a changing regulatory environment for AIFs.

An Undertaking for Collective Investment (UCI) established under Part II of the Law of 2010 is an investment fund that does not invest in transferable securities. An additional – complementary – alternative investment fund regime which is similar to both the SIF and SICAR regimes was recently introduced by the so called Reserved Alternative Investment Fund (RAIF).⁹⁵

2.2.2. UCITS

As already mentioned in chapter 2.1 the EU has created a certain degree of standardization by implementing several so called UCITS-directives. In Luxembourg the UCITS IV directive was transposed into national law by the Part I of the Law of 17 December 2010 relating to undertakings for collective investment.⁹⁶

This law was modified last in 2016 by the EU UCITS V directive being transposed into local Luxembourg Law of 10 May 2016.⁹⁷

UCITS V imposes further duties and liabilities on the depositary of a UCITS fund. It also brings in line a UCITS managers' remuneration with the requirements of the AIFMD. The level 1 directive had to be implemented into national law by the member states by March 18th, 2016. The level 2 requirements and ESMA remuneration guidelines were published shortly after in March 2016. The background relates to the Madoff fraud case as well as the default of Lehman Brothers. These two incidents brought forward the weaknesses and the lack of harmonization of the depositary duties and liabilities across different EU countries. In fact, the depositary rules have

⁹⁵ (ALFI - Association of the Luxembourg Fund Industry, 2017 (II)), see also para.1. Law of 17 December 2010 relating to undertakings for collective investment: transposing 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) (recast); amending: the Law of 20 December 2002 relating to undertakings for collective investment, as amended; the Law of 13 February 2007 relating to specialised investment funds, as amended; Article 156 of the Law of 4 December 1967 on income tax.

⁹⁶ Cf. (ALFI - Association of the Luxembourg Fund Industry, 2017 (I)), para. 1.

⁹⁷ Directive 2014/91/EU of the European Parliament and of the Council of 23 July 2014 amending Directive 2009/65/EC on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) as regards depositary functions, remuneration policies and sanctions; amending: the Law of 17 December 2010 relating to undertakings for collective investment, as amended; the Law of 12 July 2013 on alternative investment fund managers, as amended.

remained unchanged since the original UCITS Directive was introduced in 1985, although the framework had been revised several times over the years.⁹⁸

The choice of the regime largely depends on the investment strategy selected and the target investor base. UCITS are especially designed, but not limited to the broad mass of retail investors, providing the highest investor protection possible. UCITS are subject to more stringent regulations. The implementation of any investment strategies within the UCITS framework must be in strict compliance with guidelines of the Committee of European Securities Regulators.⁹⁹

For this thesis in particular the Non-UCITS funds under Part II of the 2010 Law as well as the other AIFs under their relevant product laws are important. The reason for mentioning UCITS was the success of the fund regime here in Luxembourg. Therefore, the UCITS development is regarded as role model for making Luxembourg successful in the AIF sector as well.

2.2.3. AIF – Alternative Investment Funds

This chapter introduces the term AIF and will highlight which structures are part of this regime. It is done by defining the scope of the AIFMD and by analyzing the relevant structures which are presented afterwards.

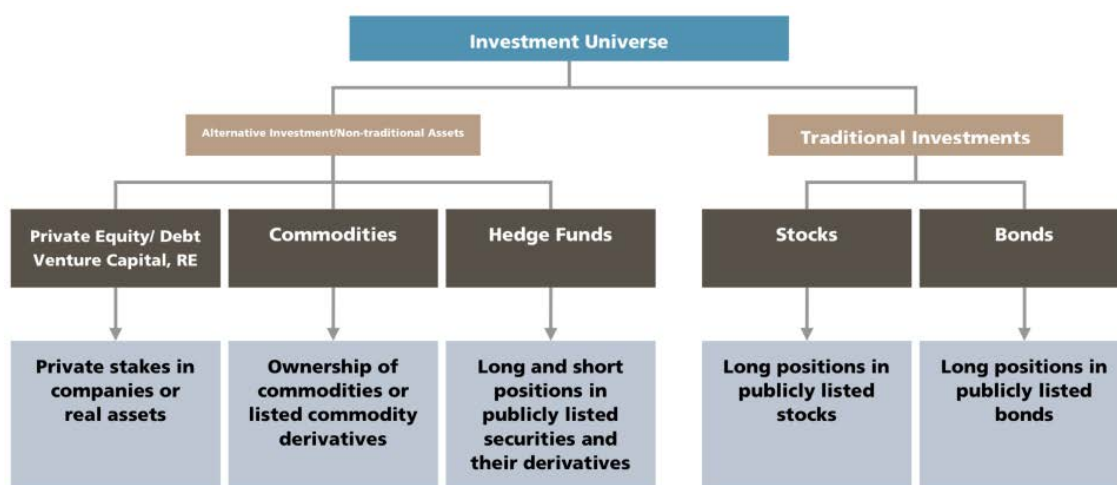
Being mentioned in chapters 2.2.1 and 2.2.2 the term UCI includes all investment funds that raise capital from investors and investing it with a defined investment policy. Not all investment funds are covered by Part I of the Law of 17 December 2010 as amended. This includes, e.g. hedge funds, funds of hedge funds, venture capital and private equity funds as well as real estate funds and under the regimes of e.g. UCI, SIF, SICAR and RAIF.¹⁰⁰

⁹⁸ Cf. (Kleyr / Grasso, 2016), para.1ff.

⁹⁹ Cf. (Ball, 2011), p.227f.

¹⁰⁰ Cf. (ALFI - Association of the Luxembourg Fund Industry, 2017 (II)), para.1.

Figure 10: Alternative and traditional investments



Source: Own elaboration based on (Maginn, Tuttle, Pinto, & McLeavey, 2007).

A comparison between the traditional investment assets and assets considered as alternative ones is provided in Figure 10: Alternative and traditional investments. Compared to traditional investments, which account for the majority of UCITS assets, the alternative investments are assets which are linked to a higher risk. These investments are referred to as non-traditional assets.

The legal definition of an AIF was established in the Luxembourg by the transposition of the AIFMD which will be presented in the next chapter 2.2.4. The main innovation of the AIFMD is the qualification of a UCI as an AIF governed by the Luxembourg Law of 12 July 2013¹⁰¹ on alternative investment fund managers (AIFM-Law):¹⁰²

“As one of the first European countries, the Luxembourg Parliament adopted the law transposing the Alternative Investment Fund Manager Directive (AIFMD) into Luxembourg law on 10 July 2013. The law relating to investment managers of alternative investment funds was published in the Memorial A N° 119 on 15 July 2013. This presents an opportunity for Luxembourg to create a brand in the alternative investment market, similar to the global brand it has created with UCITS. The AIFMD involves the introduction of a European

¹⁰¹ Cf. Law of 12 July 2013 on alternative investment fund managers – transposing Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010.

¹⁰² (Luxembourg for Finance, 2016 (IV)), para.2.

passport for alternative investment fund managers who wish to access the entire European market. Through the AIFMD, the European Union is creating the first regulated environment for alternative investment funds worldwide.”

In regards to legal restrictions for AIF investments the advantage to UCITS funds under Part I Law is an almost complete freedom in choice of assets. Because “[...] the investment policy must be approved by the financial sector regulator, the CSSF. The regulator has established requirements regarding risk diversification, but these are less strict than for UCITS.”¹⁰³ Nevertheless, all “[...] these funds are subject to the ongoing supervision of the Luxembourg supervisory authority (the Commission de surveillance du secteur financier, CSSF)”.¹⁰⁴

For the setup of an AIF the already mentioned legal structures and forms introduced in chapter 2.2.1 can be used. Additionally the AIF might be governed by additional product laws providing further legal structures namely the SIF, SICAR and the new RAIF to set up an AIF governed by the AIFMD. This will be illustrated in detail as part of chapter 3.3.

The official legal definition of AIF under Art 1(39) Luxembourg AIFM Law is the following:¹⁰⁵

“Alternative Investment Funds (AIFs)”: collective investment undertakings, including investment compartments thereof, which:

(a) raise capital from a number of investors, with a view to investing it in accordance with a defined investment policy for the benefit of those investors; and

(b) do not require authorisation pursuant to Article 5 of Directive 2009/65/EC;”

Per definition the AIF is a collective investment undertaking, including investment compartments that raises capital from a number of investors.

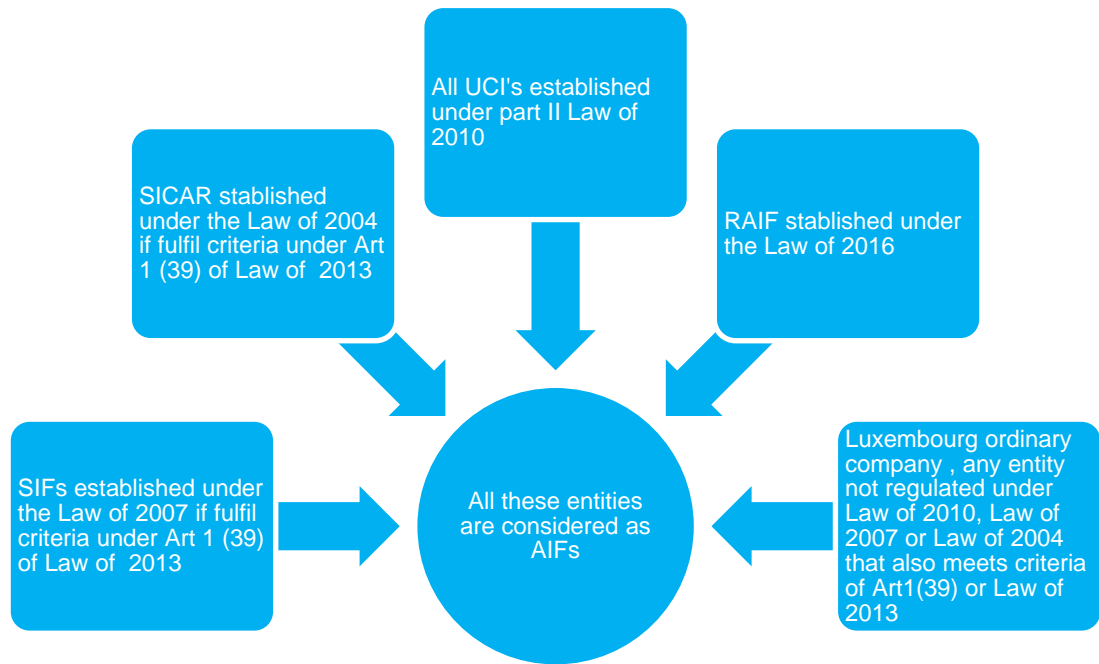
¹⁰³ (Luxembourg for Finance, 2016 (IV)), para.4.

¹⁰⁴ (Allen & Overy, 2015), p.2.

¹⁰⁵ Art. 1 (39) of the Law of 12 July 2013 on alternative investment fund managers – transposing Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010.

As stated below in Figure 11: Luxembourg entities considered as AIFs, AIFs include all forms under Part II UCI as well as SIF, SICAR and other forms meeting the conditions of the AIF definition provided by AIFMD.

Figure 11: Luxembourg entities considered as AIFs



Source: Own elaboration based on ALFI - Association of the Luxembourg Fund Industry - Alternative Investment Funds: "Luxembourg: The Clear Alternative.", published on July 14th, 2014, viewed on June 19th, 2015 - (<http://www.alfi.lu/setting-luxembourg/alternative-investment-funds-0>), see also (Wildgen - Partners in Law, 2016), p.4f.

After the definition of AIF in general the next chapter will introduce the AIFMD and will specify the main regulatory requirements for AIF managers in Luxembourg.

2.2.4. AIFMD

This chapter describes the differences between UCITS and non-UCITS (AIFs) in regards to the AIFMD. The aim is to provide a general overview of the main changes and the impacts of this directive.

The AIFMD effective since July 22nd, 2013,¹⁰⁶ regulates¹⁰⁷

- fund managers that manage AIFs,
- fund managers that manage AIFs established in the EU, and
- fund managers that market the units or shares of an AIF in the EU.

AIFMD introduced harmonized requirements for entities involved in distributing AIFs to professional investors in the European Economic Area (EEA). Important is that AIFMD does not harmonize the distribution of AIFs to retail investors. This is subject to national rules.¹⁰⁸

Funds that do not qualify as UCITS and their AIFMs are not subject to the same rules to protect their investors than funds governed by UCITS. In general, the lack of financial regulation was seen as one reason contributing to the severity of the global financial crisis. AIFMD aimed to redress this perceived regulatory gap. It fits into the broader context of investor protection related efforts pursued by many politicians and policy makers.¹⁰⁹

AIFMD regulates the AIFM rather than the AIF itself. The AIFM represents the legal person whose regular business is managing one or more AIFs. The official legal definition of AIFM under Art 1(46) Luxembourg AIFM Law is the following:¹¹⁰

"Alternative Investment Fund Managers (AIFMs)": legal persons whose regular business is managing one or more AIFs;"

¹⁰⁶ Cf. DIRECTIVE 2011/61/EU OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL of 8 June 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010.

¹⁰⁷ Cf. (Loader, 2016), p.32ff.

¹⁰⁸ Cf. (Loader, 2016), p.33f.

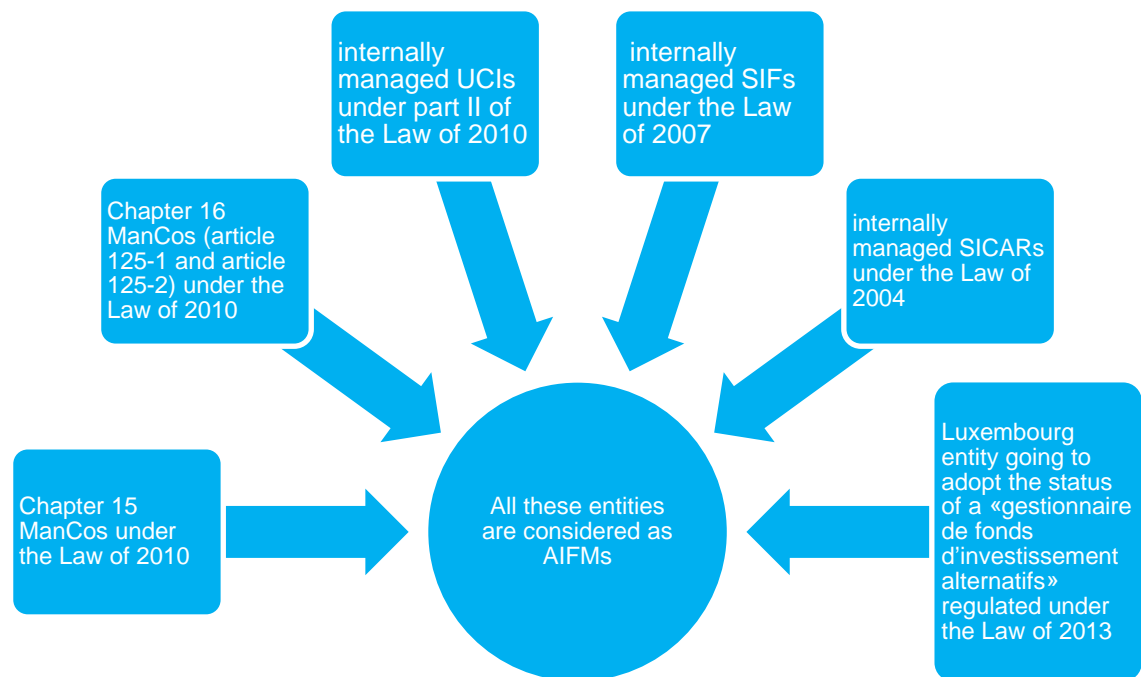
¹⁰⁹ Cf. (de Lavenère Lussan, 2012), p.207ff.

¹¹⁰ Art. 1 (46) of the Law of 12 July 2013 on alternative investment fund managers – transposing Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010.

Herby, the AIF is the AIFM in case the AIF is managed internally, if relevant to its legal structure, for example in Luxembourg FCP, SICAVs, SICAFs etc.¹¹¹

AIFMD sets out rules for authorization, ongoing operation and transparency of AIFMs. It aims to create a harmonized and comprehensive legal framework within the EU and tries to regulate the acting fields of the AIFMs of funds. These rules requiring major changes to the structure, strategies and operations of fund managers and funds in the AIF Sectors.¹¹² The possible legal entities qualifying as an AIFM are stipulated in Art. 1(49) Luxembourg AIFM Law and illustrated in the below stated Figure 12: Potential AIFM entities.¹¹³

Figure 12: Potential AIFM entities



Source: Own elaboration based on Art. 1 (46) of the Law of 12 July 2013 on alternative investment fund managers – transposing Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010.

¹¹¹ Cf. (PWC - Luxembourg, 2013), p.3.

¹¹² Cf. (Muller & Ruttiens, 2013), p.41f.

¹¹³ Art. 1 (49) of the Law of 12 July 2013 on alternative investment fund managers – transposing Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010.

Like the regulatory principle of UCITS IV+V, AIFMD should regulate the alternative investment fund industry EU wide. AIFMD starts with setting out organizational requirements for the AIFM. Once authorized as an AIFM, the fund manager is entitled, upon notification, to manage or market funds to professional investors throughout the EU. This is similar to the EU-Passport for UCITS to market their shares in the EU.¹¹⁴

Figure 13: The EU AIFMD framework, indicates the directive and the most important regulations as basis for the transposition into local law.

Figure 13: The EU AIFMD framework

EU AIFM framework	
•AIFM Directive (cf“Level1”)	08.06.2011: Directive 2011/61/EU on Alternative Investment Fund Managers
•AIFM Regulations (cf“Level 2”)	<ul style="list-style-type: none"> •19.12.2012: Commission Delegated Regulation (EU) No 231/2013 on exemptions, general operating conditions, depositaries, leverage, transparency and supervision •15.03.2013: Commission Delegated Regulation (EU) No 447/2013 on the procedure for AIFMs that fulfill the conditions set out in Article 3(2) of the AIFMD which choose to opt in under Directive 2011/61/EU •15.03.2013: Commission Delegated Regulation (EU) No 448/2013 on a procedure to determine the Member State of reference of an AIFM established in a third country pursuant to the second subparagraph of Article 37(4) of the AIFMD •17.12.2013: Commission Delegated Regulation (EU) No 694/2014 on the rules set out by the AIFMD with regulatory technical standards determining types of AIFMs. This regulation distinguishes whether an AIFM is managing AIFs of the open-ended or closed-ended type or both in order to apply correctly the rules on liquidity management and the valuation procedures of the AIFMD to AIFMs
•ESMA’s main publications (cf“Level3”)	<ul style="list-style-type: none"> •19.07.2016: ESMA Q&A on application of the AIFMD •01.10.2013: ESMA/2013/1340 effective monitoring of risk •15.11.2013: ESMA/2013/1339 Guidelines on reporting obligations under Articles 3(3)(d) and 24(1), (2) and (4) of the AIFMD (revised) – final report •13.08.2013: ESMA/2013/611 Guidelines on key concepts of the AIFMD-Guidelines and recommendations •11.02.2013: ESMA/2013/232 Guidelines on sound remuneration policies under the AIFMD-Guidelines and recommendations

Source: Own elaboration based on (CSSF - Commission de Surveillance du Secteur Financier, 2017 (I)).

¹¹⁴ Cf. (Rodriguez, Vandervelde, & Lebrecht, 2015), p.25.

Figure 14: AIFMD Luxembourg transposition

<p>•Luxembourg Law</p> <p>12.07.2013: The Law of 12 July 2013 (This law transposes the AIFMD and amends directives 2003/41/EC and 2009/65/EC and the regulations (EC) No 1060/2009 and (EU) No 1095/2010) on alternative investment fund managers amending:</p> <ul style="list-style-type: none"> •Part II of law of 2010 on undertakings for Collective Investment (UCI), •The Specialised Investment Fund (SIF) law of 13 February 2007 and the •Investment Companies in Risk Capital (SICAR) law of 15 June 2004 <p>10.05.20116: The Law of 10 May 2016 transposing Directive 2014/91/EU of the European Parliament and of the Council of 23 July 2014 amending Directive 2009/65/EC on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) as regards depositary functions, remuneration policies and sanctions; amending:</p> <ul style="list-style-type: none"> •the Law of 17 December 2010 relating to undertakings for collective investment, as amended; •the Law of 12 July 2013 on alternative investment fund managers, as amended. <p>Grand-ducal Regulation of 28 October 2013 relating to the fees to be levied by the CSSF</p> <ul style="list-style-type: none"> • CSSF Regulation: <ul style="list-style-type: none"> • 02.12.2015: CSSF Regulation N° 15-03 laying down detailed rules for the application of Article 46 of the Law of 12 July 2013 on alternative investment fund managers on the marketing of foreign alternative investment funds to retail investors in Luxembourg • 26.10.2016: CSSF Regulation N° 16-07 relating to out-of-court complaint resolution 	<p>•CSSF Circulars:</p> <ul style="list-style-type: none"> •01.02.2010: CSSF 10/437 - Guidelines concerning the remuneration policies in the financial sector •26.03.2010: CSSF 10/446 - Change regarding the communication of circulars issued by the CSSF for the entities under its supervision •05.05.2010: CSSF 10/456 - Cooperation between the professionals of the financial sector and the judicial authorities •11.03.2011: CSSF 11/504 - Frauds and incidents due to external computer attacks •13.01.2014: CSSF 14/581 - New reporting obligations for Alternative Investment Fund Managers •25.02.2014: CSSF 14/585 - Transposition of the European Securities Markets Authority's (ESMA) guidelines on remuneration policies and practices (MiFID) - Addition of Annexe V to Circular CSSF 07/307 •27.06.2014: CSSF 14/589 - Details concerning Regulation CSSF N° 13-02 of 15 October 2013 relating to the out-of-court resolution of complaints •27.03.2015: CSSF 15/609 - Developments in automatic exchange of tax information and anti-money laundering in tax matters •16.04.2015: CSSF 15/611 - Managing the risks related to the outsourcing of systems that allow the compilation, distribution and consultation of management board/strategic documents •05.05.2015: CSSF 15/612 - Information to be submitted to the CSSF in relation to unregulated alternative investment funds (established in Luxembourg, in another EU Member State or in a third country) and/or regulated alternative investment funds established in a third country •10.12.2015: CSSF 15/629 (as amended by Circular CSSF 16/641) - Supplementary supervision to be applied to financial conglomerates and definition of structure coefficients to be observed by the regulated entities belonging to these financial conglomerates pursuant to Article 56 of the law of 5 April 1993 on the financial sector, as amended •28.12.2015: CSSF 15/631 - Dormant or inactive accounts •29.12.2015: CSSF 15/633 - Financial information to be provided by investment fund managers and their branches on a quarterly basis •05.08.2016: CSSF 16/641 - Update of Circular CSSF 15/629 relating to supplementary supervision to be applied to financial conglomerates and definition of structure coefficients to be observed by the regulated entities belonging to these financial conglomerates pursuant to Article 56 of the law of 5 April 1993 on the financial sector, as amended •18.10.2016: CSSF-CPDI 16/02 - Scope of the deposit guarantee and the investor compensation •18.10.2016: CSSF-CPDI 16/03 - Survey on covered claims in connection with investment business <p>•CSSF FAQ</p> <p>FAQ concerning the Luxembourg Law of 12 July 2013 on alternative investment fund managers as well as the Commission Delegated Regulation (EU) No 231/2013 of 19 December 2012 supplementing Directive 2011/61/EU of the European Parliament and of the Council with regard to exemptions, general operating conditions, depositaries, leverage transparency and supervision (10th update version 09.06.2016)</p>
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Source: Own elaboration based on (CSSF - Commission de Surveillance du Secteur Financier, 2017 (II)).

The AIFMD authorizes AIFMs to benefit from a passport, enabling them to offer their management services and market their AIFs throughout the EU, and helps to regulate the markets and to offer more attractive investment solutions for institutional investors with less risks.

It is worth mentioning is that a new regulation related to European long-term investment fund (ELTIF) has been laid down by the EU on December 9th, 2015 which directly applies in all EU member states without national transposition. The idea of this vehicle is to channel capital pan-European towards “long-term investments in the real economy, in line with the European Union (EU) objective of smart, sustainable and inclusive growth[.]”¹¹⁵. The AIFM of this structure is also governed by the AIFMD. Every Luxembourg AIF can apply for this ELTIF label. This label offers, e.g. marketing to professional and retail investors subject to additional restrictions.¹¹⁶

After the introduction of the Luxembourg Investment Fund Market and its available regimes and structures for investment funds the next chapter aims to introduce the new AIF, the Reserved Alternative Investment Fund, commonly referred to as RAIF.

3. RAIF – Reserved Alternative Investment Fund

In order to understand its evolution and its advantages, it is important to introduce the structure itself and its main features as an AIF.

For this purpose an overview of the relevant innovations related to the setup is given. Furthermore, the requirements for the AIF and AIFM are provided, e.g. in regards to the CSSF regulation the innovation is the non-existing supervision of the Luxembourg supervising authority for the fund itself. Afterwards, these facts are compared to the most important already existing AIF structures in Luxembourg and a comparison with fund structures from other countries will be performed.

¹¹⁵ (ALFI - Association of the Luxembourg Fund Industry, 2015 (II)), p.3.

¹¹⁶ Cf. *ibid.*

3.1. RAIF – introduction and setup

With the adoption of the RAIF-Law of 23 July 2016¹¹⁷ by the Luxembourg Parliament on 14 July 2016, Luxembourg introduced the RAIF a completely new AIF product that is only managed and authorized by an AIFM. The aim of this newly introduced AIF product is to revolutionize the existing range of structuring solutions for AIFs in terms of Private Equity, Real Estate, Hedge Funds and other alternative investment strategies.¹¹⁸

The introduction of the RAIF responded to the growing needs for more efficient contractual flexibility and a faster time-to-market perspective, in the context of the AIFMD legal framework, benefitting from the European passport to ensure marketing to professional investors.¹¹⁹

The RAIF is only available to well-informed investors, parallel to existing Luxembourg regulated AIFs. This category includes institutional investors, professional investors and investors investing a minimum amount of EUR 125,000 and providing a certification which proves that they understand the risks involved in the investment from a credit institution, a ManCo or a fund manager.¹²⁰

In relation to the setup of a RAIF the already known structures¹²¹ can be recognized.¹²²The structuring of an RAIF is therefore identical to already existent AIF products¹²³ in Luxembourg:

“A RAIF in the form of an FCP must always be managed by a Luxembourg management company. This management company can be a Luxembourg AIFM. If the Luxembourg management company is not authorized as a Luxembourg AIFM, it must appoint an AIFM either in Luxembourg or in another EU Member State. In the case of a SICAV, the RAIF can be formed

¹¹⁷ Cf. Mémorial A n° 140 de 2016 - Loi du 23 juillet 2016 relative aux fonds d'investissement alternatifs réservés et portant modification de: 1. la loi modifiée du 16 octobre 1934 concernant l'impôt sur la fortune; 2. la loi modifiée du 1er décembre 1936 concernant l'impôt commercial communal; 3. la loi modifiée du 4 décembre 1967 concernant l'impôt sur le revenu; 4. la loi modifiée du 5 avril 1993 relative au secteur financier; 5. la loi modifiée du 13 février 2007 relative aux fonds d'investissement spécialisés; et de 6. la loi modifiée du 17 décembre 2010 concernant les organismes de placement collectif.

¹¹⁸ Cf. (Luxembourg Fund Partners, 2016 (I)), para.1.

¹¹⁹ Cf. (Luxembourg for Finance, 2016 (V)), p.5 f.

¹²⁰ Cf. (ALFI - Association of the Luxembourg Fund Industry, 2017 (III)), p.1.

¹²¹ Cf. chapter 2.2.1.

¹²² Cf. (ALFI - Association of the Luxembourg Fund Industry, 2016 (V)), p.2.

¹²³ Cf. Chapter 2.2.1.

as a public limited liability company (société anonyme or “SA”), private limited liability company (société à responsabilité limitée or “Sàrl”), corporate partnership limited by shares (société en commandite par actions or “SCA”), common limited partnership (société en commandite simple or “SCS”), special limited partnership (société en commandite spéciale or “SCSp”), or cooperative company formed as a public limited liability company (société coopérative sous forme de société anonyme or “SCoSA”).”¹²⁴

However, structuring as an investment company could indeed pose a potential risk related to the supervision of the AIFM. Existing AIFs can be managed internally. In the case of a RAIF, the company would authorize and supervise itself. In order to avoid such a dilemma, the RAIF Law still has introduced an additional requirement for its structuring:

“For the avoidance of doubt, the RAIF regime is thus not be available to:

- (i) AIFs using the benefit of an exemption or derogation under the AIFMD, such as the so called de minimis or group exemption, and*
- (ii) internally-managed AIFs.*

The sole possibility for a RAIF not to be obliged to appoint an external AIFM is when the RAIF is managed

- (i) by a supranational institution (such as ECB, EIB, EIF) or by another similar international institution acting in the public interest, or*
- (ii) by the Central Bank of Luxembourg or another national central bank.”¹²⁵*

The ‘de minimis’ rule derives from an exemption of the AIFM Law related to investments below specific thresholds. The UCI may be exempt from the AIFMD and can choose for an application to the EuVECA or EuSEF regulations in relation to the marketing of qualifying venture capital/social entrepreneurship funds in the European Union.

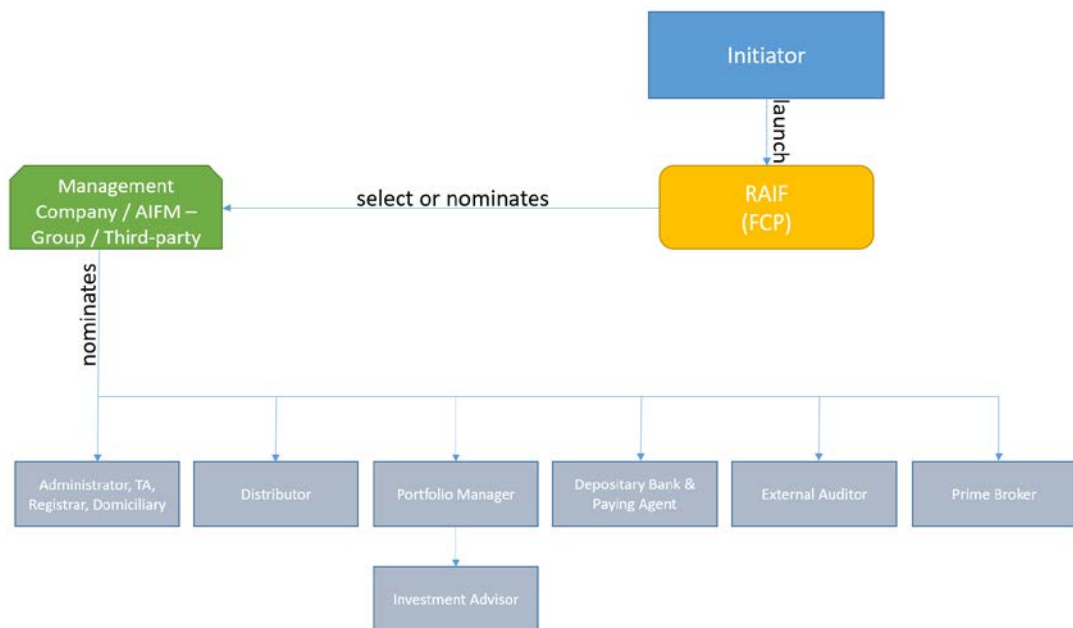
¹²⁴ (Seimetz, Astleford, Frognet, Goebel, & Terblanche, 2016), p.3f.

¹²⁵ (ALFI - Association of the Luxembourg Fund Industry, 2016 (VI)), p.1.

“For these types of managers, the European Union acknowledged the need to overcome the existence of multiple fragmented national regimes by introducing a separate marketing passport regime under the Regulation on European venture capital funds (EuVECA) and the Regulation on European social entrepreneurship funds (EuSEF) respectively.”¹²⁶ This is applicable for Part II UCI, SIF and SICAR vehicles. The RAIF is excluded from this regulation.¹²⁷ “Managers wishing to be subject to one of the two regimes have to inform their competent authorities. They will be not authorised but registered and can market eligible funds to professional investors in the EU.”¹²⁸

In order to visualize the available structures, Figure 15: RAIF - common fund (FCP) and Figure 16: RAIF - Investment company that appt. a ManCo, illustrate these possibilities related to the structuring of the organization.

Figure 15: RAIF - common fund (FCP)



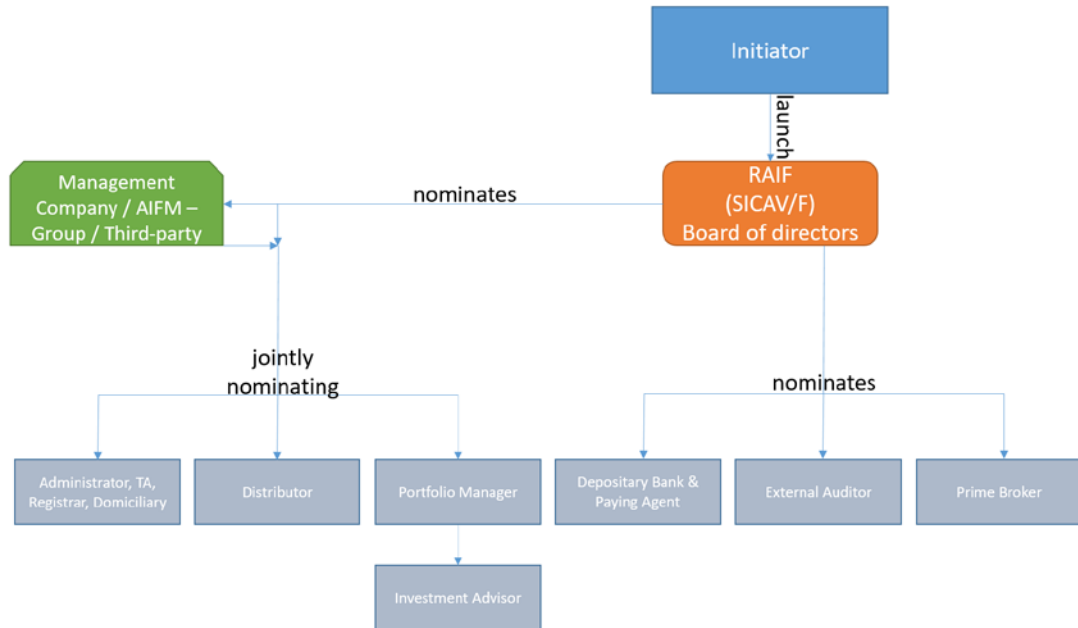
Source: Own elaboration based on (Ernst & Young S.A., Luxembourg, 2016 (I)), p.18.

¹²⁶ (ALFI - Association of the Luxembourg Fund Industry, 2017(VI)), p.1.

¹²⁷ Cf. *ibid.*

¹²⁸ *Ibid.*

Figure 16: RAIF - Investment company that appt. a ManCo



Source: Own elaboration based on (Ernst & Young S.A., Luxembourg, 2016 (I)), p.18.

The above illustrated figures demonstrate very easily the differences of the different organizational setups. In case of the setup as an investment company (SICAV/F) the appointment of the depository, the auditor and the prime broker can be determined by the investment company itself. Whereas, the appointment of the administrator, the distributor and the portfolio manager can be jointly decided by the ManCo and the investment company. For the setup as FCP the appointed ManCo is fully responsible for the appointment of the service providers. “In order to comply with AIFMD, the RAIF will be subject to a Luxemburg-based depository and central administration requirement, and will need to appoint an auditor, all providing comfort to investors, as envisaged by the directive.”¹²⁹

The RAIF is set up through a founder, whereas the management body in form of an investment company or an investment fund, depending on the chosen legal form and the terms of the constitutive documents must be indicated. The roles of the administrator are, e.g. the legal and fund management accounting services, maintenance of units-/ shareholder or partnership register, issue and redemption of units/shares or partnership interests, regulatory compliance monitoring (e.g. Anti-

¹²⁹ (Cutolo, 2016), p.5.

Money-Laundering, Counter Terrorist Financing rules), NAV-calculation, pricing and tax returns just to mention a few. In terms of distributors the distribution channels and the appointment of the distributor are to be mentioned. The portfolio manager or delegated investment advisor needs to be appointed in order to fulfil the duties of portfolio management as well as risk management, monitoring of investments, knowledge and understanding of investments and related areas. In regard of the depositary, the custody of the assets of any RAIF must be assigned to a depositary having its registered office in Luxembourg or having a Luxembourg branch or entity in case its registered office is in another member state of the EU. The depositary must be sufficiently experienced in order to fulfil its tasks such as ensuring that the RAIF's cash-flows are properly monitored, the holding in custody is fulfilled and that diverse oversight duties, as well as safekeeping duties are observed.¹³⁰

At last an approved statutory auditor must be appointed: "The accounting information contained in the annual report of a RAIF must be audited by an approved statutory auditor (réviseur d'entreprise agréé), which is appointed by the RAIF (i.e. by the management company of the FCP-RAIF or by the general meeting of shareholders/partners of the SICAV/SICAF-RAIF) and remunerated by the RAIF."¹³¹

Optionally, a prime broker "which acts as counterparty to a RAIF is allowed to act as a depositary from the RAIF only if it has functionally and hierarchically separate the performance of its depositary functions as a prime broker."¹³²

From a practical point of view, the RAIF is set up in the form of an investment fund, which differs from the setup of traditional unregulated investment vehicles. Compared to, e.g. existing Limited Partnerships (LP) the RAIF can profit from the available umbrella structure with multiple sub-fund options. A fund with one or more compartments or sub-funds, where the assets and liabilities of each sub-fund can be segregated from the assets and liabilities of other sub-funds. The RAIF-Law also permits cross-investment between sub-funds.¹³³

In relation to the diversification of its investments a RAIF will have nearly no limits and may invest in any kind of assets. Related to its investment strategy the RAIF is allowed to invest without restrictions but subject to diversification rules in order to

¹³⁰ Cf. (Clifford Chance, Luxembourg, 2016), p.10ff.

¹³¹ (Clifford Chance, Luxembourg, 2016), p.13.

¹³² (Elvinger Hoss Prussen, 2016 (II)), p.10.

¹³³ Cf. (Loyens & Loeff Luxembourg S.à r.l., 2016), p.6.

spread the investment risk. Although the RAIF Law itself does not set specific rules, it refers to the SIF regimes and the Circular CSSF 07/309¹³⁴ related to risk-spreading for SIFs, allowing it not to invest more than 30% of its assets in assets from the same issuer.¹³⁵

The RAIF offers another interesting opportunity related to risk investments: If it opts, what needs to be declared in the incorporation documents, for exclusively investments in risk capital linked to the current SICAR regime and similar to the risk investment a SIACAR invests in, the diversification rules of risk-spreading do not apply. Then a RAIF can invest up to 100% in one asset from just one issuer as declaratively applicable.¹³⁶ When opting for SICAR like investments and being setup in form of a FCP the structure cannot be recognized for the SICAR taxation anymore.¹³⁷ This refers to SICAR regime in the sense of Circular CSSF 06/241¹³⁸ related to the concept of risk capital applicable to SICARs.¹³⁹

In essence, the RAIF has nearly no limits in terms of eligible assets, and although its incorporation documents state that it is, e.g. investing in venture capital, it will be able to deviate from its investment strategy. This was eagerly awaited not just by private equity players but also for more asset-based products and from institutional and high net worth investors, along with their asset managers. In addition the expectation for a faster time-to-market vehicle offering similar advantages, like the existing SIFs or SICARs, has been fulfilled. The RAIF offers similar advantages while giving its managers enough flexibility in the choice of the investment strategies and eligible assets.¹⁴⁰

Another feature is related to the fact that some of the RAIF's characteristics can be changed during the life of the fund without going through a regulatory approval. Subsequently this leads to a faster reactivity and increased flexibility. "Existing SIFs, SICARs and unregulated AIFs may elect for the RAIF regime subject to securing the relevant approvals from investors and, where applicable, the CSSF. Under the same conditions, the RAIF could be used in a phased approach to organize a first closing rapidly with investors that do not require direct product supervision, with a transition

¹³⁴ Cf. (CSSF - Commission de Surveillance du Secteur Financier, 2007), p.1.

¹³⁵ Cf. (Arendt & Medernach, 2016), p.8.

¹³⁶ Cf. (Ruddy, 2016), p.1.

¹³⁷ Cf. (Loyens & Loeff Luxembourg S.à r.l., 2016), p.6.

¹³⁸ Cf. (CSSF - Commission de Surveillance du Secteur Financier, 2006), p.1ff.

¹³⁹ Cf. (Allen & Overy, 2015), p.8.

¹⁴⁰ Cf. (Lentschat, 2015), p.1.

into another regime, such as the SIF, to follow at a later stage to permit other investors that prefer or are limited to investing in directly supervised products.”¹⁴¹

This is an interesting method for setting up a structure in a short time or due to an urgent request and to convert it in a second stage into an AIF for such as a Part II UCI, a SIF or a SICAR.¹⁴²

Related to the conversion of already existing structures (Part II UCI, SIF or SICAR) into the RAIF, these are subject to the additional requirement of a prior CSSF approval and related amendments of the constitutive documents of the fund. Furthermore, the prospectus as well as the issue document of the fund need to be adapted accordingly to the conversion into a RAIF. Related to unregulated LP's an amendment of the LP agreement will be necessary. Also entities that are non-Luxembourg entities may apply for a conversion into a RAIF, subject to the condition that the relevant entity is at the time of the conversion compliant with AIFMD, meaning that appointment of a fully and duly authorized external AIFM took part.¹⁴³

An additional special feature of the RAIF is related to its tax regimes. Basically, the RAIF will have similar characteristics as the already existing SIF and may also take several different legal forms, thus allowing for a number of tax structures as well as various governance options.

“The tax regime of the RAIF is equal to that of a SIF. It is exempt from income and net wealth taxes and its distributions are exempt from withholding tax. It is subject to an annual subscription tax of 0.01% (certain exemptions exist). A RAIF can, however, opt for being taxed as a SICAR where its sole object is to invest in risk capital assets. A RAIF that takes a corporate legal form (like the S.A., S.à r.l. or S.C.A.) will be a normally taxable entity for income tax purposes, but with an exemption from its taxable basis for any profits and gains derived from securities representing risk capital. It will further be exempt from net wealth and subscription taxes.”¹⁴⁴

If the RAIF is subject to the SIF tax regime it will be exempt from corporate income tax and further taxes in Luxembourg. The subscription tax, nevertheless will be

¹⁴¹ (Bourke & Lasserre, 2016), p.60.

¹⁴² Cf. (Ernst & Young S.A., Luxembourg, 2016 (II)), p.2.

¹⁴³ Cf. (Ernst & Young S.A., Luxembourg, 2016 (II)), p.2.

¹⁴⁴ (Luxembourg for Finance, 2016 (VI)), p.2.

applied, but is subject to certain exemptions. It will be applied on its net assets at a rate, as stipulated above, of 0.01%. This tax will also apply to a RAIF established as an SCS or a SCSp unless it opts for the special tax regime and exclusively invests in risk capital, linked to the current SICAR regime. Under this circumstances the above mentioned differentiation takes place, but allows RAIFs incorporated under the form of an SA, an SCA or an S.à.r.l the access to the Luxembourg double taxation treaties (DTT). Organized as limited partnership (SCS or SCSp) opting to be taxed as a SICAR it is not liable to income, net wealth, or subscription taxes in Luxembourg.¹⁴⁵

“To avail of this optional regime, the constitutive documents of the RAIF will need to disclose that (i) its object is to exclusively invest in risk capital and (ii) it is subject to the provisions of the specific article of the RAIF Law which provides for this alternative tax regime. RAIFs investing in "risk capital" (which, with respect to the SICAR, the CSSF has interpreted to mean the direct or indirect contribution of assets to entities in view of their launch, development or listing on a stock exchange) would therefore (where their legal forms permit) be subject to general corporation taxes in Luxembourg, including corporate income tax, municipal business tax and a solidarity surcharge. However, any income derived from securities held by the RAIF or funds drawn for investment (within 12 months) as well as any income from the sale, contribution or liquidation thereof will be fully exempt. Such RAIFs should also generally benefit from the network of double tax treaties entered into by Luxembourg.”¹⁴⁶

Figure 17: Taxation RAIF - standard and related to Risk Capital, represents these fields of tax application schematically.

¹⁴⁵ Cf. (Allen & Overy, 2015), p.7.

¹⁴⁶ (Baker & McKenzie Luxembourg, 2016), para.3.11.

Figure 17: Taxation RAIF - standard and related to Risk Capital

	SIF & RAIF not qualifying for SICAR-like taxation	SICAR & RAIF investing in Risk Capital	
		SA, SARL, SCA	CLP, SLP
Corporate income tax (CIT)	N/A: tax exempt	<ul style="list-style-type: none"> ■ Maximum 21%, plus a solidarity surcharge of 7% which leads to an effective CIT of 22.47% ■ However 100% exemption for profits derived from (i) risk capital securities and (ii) funds to be invested within 12 months in risk capital securities 	N/A: tax transparent
Municipal business tax (MBT)	N/A: tax exempt	<ul style="list-style-type: none"> ■ 6.75% (in Luxembourg-city) ■ However 100% exemption for profits derived from (i) risk capital securities and (ii) funds to be invested within 12 months in risk capital securities 	N/A: tax transparent
Withholding Tax		<ul style="list-style-type: none"> > On dividends: N/A³ > On interests: N/A⁴ 	
Net worth tax	N/A: tax exempt	Only subject to minimum tax of EUR 3,210	

Source: (Arendt & Medernach, 2016), p.12.

Due to the reform of the taxation system on January 01st, 2017 the corporate income tax was adapted to a maximum of 20.33%:

“On 26 July 2016, a law proposal on tax reforms, effective as from 2017, was submitted to the Luxembourg Parliament. In this proposal, it is proposed to lower the corporate income tax (CIT) rate from 21% to 19% in 2017 and to further reduce it to 18% in 2018 (not including the 7% surcharge which is a contribution to the Luxembourg unemployment fund). The combined proposed CIT rates would then be 20.33% for 2017 and 19.23% for 2018 (as opposed to the current rate of 22.47% in 2016). Assuming the municipal business tax (MBT) does not undergo any changes, then for Luxembourg City, the combined rate to be levied on corporations is 27.08% in 2017 and 26.01% in 2018 (with Luxembourg City having an MBT rate of 6.75%).”¹⁴⁷

¹⁴⁷ (Baumgartner, et al., 2016), p.31.

The next chapter aims at explaining the differences in regulatory requirements of the RAIF being subject to AIFM regulations as an AIF, in the absence of the CSSF products supervision.

3.2. RAIF & AIF/M regulation absence of CSSF supervision

In summary with the aforementioned definition in chapter 2.2.4 related to the AIFMD any authorized AIFM established in Luxembourg or another EEA Member State can manage a RAIF. In order to profit from the RAIF regimes, the RAIF must be an AIF managed by an AIFM. Both the AIF and the AIFM are regulated through the AIFMD. As already introduced in chapter 2.2.3 AIF – Alternative Investment Funds, the RAIF regime will only be entitled to AIF in the meaning of the Luxembourg law of 12 July 2013 that transposed the AIFMD into the Luxembourg Law.

This is an important factor because at this stage the sole management of the RAIF through the AIFM begins. As already stated in chapter 3.1 the RAIF cannot take the form of an internally-managed AIF.¹⁴⁸

The RAIF regimes allows founders to set up an AIF, which combines the legal and tax features of the SIF and SICAR product laws but without the supervision of the CSSF.¹⁴⁹

In general Luxembourg's financial sector and especially the fund market is regulated by the supervisory authority of the CSSF that was firstly established in 1999.¹⁵⁰ The CSSF controls and authorizes investment vehicles for compliance with the current applicable laws and regulations applicable in Luxembourg. The particular focus goes on the track record of fund managers, e.g. the investment strategy a fund opted and the objectives and the origin of money related to money laundering prevention in line with the anti-money laundering legislation. This results in various reporting obligations on a monthly, semi-annual and annual basis in order to transmit the fund's information to the CSSF. The authorization is not required for unregulated vehicles which are not acting in the terms of AIFMD.¹⁵¹ Furthermore

¹⁴⁸ Cf. (ALFI - Association of the Luxembourg Fund Industry, 2017 (III)), p.3.

¹⁴⁹ Cf. (Luxembourg Fund Partners, 2016 (II)), p.5.

¹⁵⁰ Cf. Chapter 2.1, p.17.

¹⁵¹ Cf. (PWC - Luxembourg, 2015 (I)), p.54.

“the access to the activity of a Management Company or an AIFM is also subject to prior authorization of the CSSF. The authorization given to a Management Company or AIFM and the maintaining of its authorization also depends on the respect by this company of a set of conditions described in the 2010 Law (Chapters 15 and 16) for a Management Company and respectively in the AIFM Law for an AIFM. The CSSF indeed checks that the Management Company or the AIFM complies with the requirements to which the company is subject to, notably via the use of information reported by this company.”¹⁵²

Exactly at this point the RAIF Law established the new special feature of non-CSSF regulation for the fund/product itself. Before the recent implementation of the RAIF Law, each AIF was regulated and supervised at two levels. On the one hand the AIF itself through product regulations and on the other hand the AIFM through the management regulations and requirements provided by the AIFMD. This constituted a doubled supervision system related to the AIF itself and the AIFM through AIFMD.¹⁵³

“The entry into force of AIFMD in Europe has resulted in a double layer of regulation, as we now have regulation and supervision at the level of the product (regulated investment funds) and supervision at the level of the manager (AIFM)”¹⁵⁴, but actually “this double system of approval and supervision is not required by the AIFMD. It entails increased protection, which is not necessarily deemed justified by a series of professional and sophisticated investors performing their own review of the AIF’s structure and documentation.”¹⁵⁵

These needs are reflected within the RAIF Law. The new and innovative idea is that the RAIF itself is an AIF no longer subject to the product supervision of the CSSF, meaning that the CSSF will not be involved in the product approval process of the fund documentation and will not be in charge of the ongoing supervision of the fund. This ensures avoiding the double layer of regulation and sets the focus on the management supervision instead of the product supervision, in line with the new regulatory focus of the Luxembourg Fund Regime. In parallel, this synchronizes the

¹⁵² Ibid.

¹⁵³ Cf. (Elvinger Hoss Prussen, 2016 (II)), p.2.

¹⁵⁴ (Seimetz, Astleford, Frognet, Goebel, & Terblanche, 2016), p.2.

¹⁵⁵ Ibid.

Luxembourg Fund Regime with the new regulatory focus, which has moved to management supervision.¹⁵⁶ “This offers greater flexibility on the product side by avoiding this double layer of regulation. The RAIF product will be regulated only through its manager, which will also significantly reduce the time to market in Luxembourg.”¹⁵⁷

This is obviously the most welcomed feature of the introduced RAIF Law and has been requested since a long time from investment fund managers and initiators that are ensuring the process of new product launched in Luxembourg.¹⁵⁸

*“With the introduction of the manager regulation via the AIFM Directive, the Luxembourg legislator identified an opportunity to revise its long standing strategy: continue the strong and recognised regulatory framework applicable to the Luxembourg fund product and the Luxembourg service providers surrounding it but replacing the authorization and prudential supervision of the CSSF by the authorisation and supervision of the product through the authorised AIFM. The outcome will be absolute planning certainty thus resolving the single most important issue of the Luxembourg alternative funds centre.”*¹⁵⁹

Following to this the RAIF must comply with the requirements for management and administration. In agreement with the AIFMD the AIFM may be established either in Luxembourg, or in a member state of the EU. Also an AIFM that is not residing in the EEA will be permitted to manage a RAIF if the entity complies with the provisions set out in the AIFM Directive respectively the AIFM Law.¹⁶⁰

In line with this the creation of a RAIF must be witnessed and acknowledged by notarial deed in public. Within 10 days thereafter, a confirmation (which must name the AIFM of the RAIF) must be deposited with the electronic gazette RESA (Recueil Electronique des Sociétés et Associations) because a RAIF needs to be registered on a publicly available list maintained by the Luxembourg trade and company register.¹⁶¹

¹⁵⁶ Cf. (Allen & Overy, 2015), p.3.

¹⁵⁷ Ibid.

¹⁵⁸ Cf. (Dusemon, Niedner, & Hoffmann, 2016 (VII)), p.34.

¹⁵⁹ Ibid.

¹⁶⁰ Cf. (Luxembourg Fund Partners, 2016 (III)), p.6.

¹⁶¹ Cf. (Seimetz, Astleford, Frognet, Goebel, & Terblanche, 2016), p.4.

In summary the new features of the RAIF Law enable an attractive and fast time-to-market in addition to the great flexibility related to the offered possibilities of risk diversification rules and the option to create compartments or umbrella vehicles in form of sub-funds. Furthermore, the applicability of the fund taxation except related to risk capital offers opportunities in the tax related structuring. Managed by an AIFM only restricted in the choice of directors, depository and auditors the RAIF can profit from marketing through the EU because it benefits from an EU marketing passport.¹⁶²

“the AIFMD quality seal (transparency, risk management and independent valuation) and a fund structure with many of the same characteristics and structuring flexibility as the SIF and the SICAR are undoubtedly the main qualities that attract the interest of many players. Indeed, the RAIF, unlike the SIF and the SICAR, will not benefit from investors protection afforded by the CSSF. Moreover, there are some costs linked to the appointment to an AIFMD and to the fund set up (mainly lawyer fees). Certain promoters will continue to favor establishing a regulated product, often to respond to investors’ preferences, because of CSSF supervisions and control, the SIF label and the recognition in other countries.”¹⁶³

In order to display these differences to the SIF and the SICAR in further detail, the next chapter will broadly introduce the most important AIF structures available in Luxembourg.

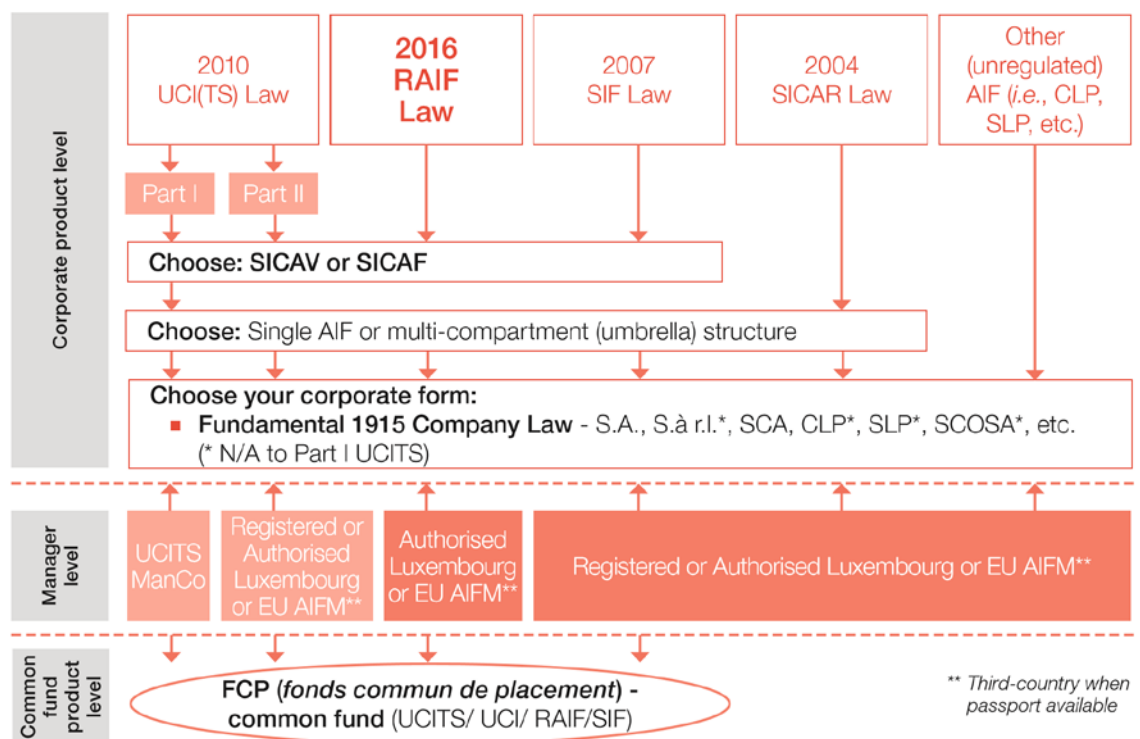
¹⁶² Cf. (Cutolo, 2016), p.6.

¹⁶³ (Cutolo, 2016), p.6.

3.3. Benefits of the RAIF compared to other Luxembourg AIF vehicles

Luxembourg offers a wide range of AIFs, this includes in addition to the already presented RAIF, further vehicles like SIFs, SICARs and Part II funds. The construct of a SOPARFI or a LP under common law might be interesting for the shareholders of the funds and will only be mentioned in the end to complete the picture of the Luxembourg Fund Market.

Figure 18: The Luxembourg fund structuring toolbox



Source: (Arendt & Medernach, 2016), p.6.

The above illustrated Figure 18: The Luxembourg fund structuring toolbox, shows a comparison of the whole range of investment fund vehicles and their respective laws available in Luxembourg compared to the introduced RAIF Law. In addition to the RAIF Law, there are other vehicles available that can classify, under their respective law, as AIF for the marketing in the EU under the AIFMD. These are the SIF (SIF Law), the SICAR (SICAR Law), any UCI under Part II Law (Part II law) and other

unregulated forms, e.g. the SOPARFI or the LP in form of a SLP or CLP regime which can fall under or apply for a treatment under AIFMD.¹⁶⁴

In order to complete the comparison of the RAIF with the currently available AIF vehicles in Luxembourg, a brief overview of these vehicles will be given in the next subchapters.

3.3.1. SIF – Specialized Investment Fund

The Luxembourg Specialized Investment Fund (SIF) refers to a very successful Luxembourg alternative investment fund vehicle, which is adapted to invest into nearly any type of assets. Legally, this structure is based on the Law of 13 February 2007¹⁶⁵ as amended, related to the Specialized Investment Fund. This structure is a lightly regulated, operationally flexible and fiscally efficient vehicle which can classify as an AIF. Once classified and managed by an AIFM it is accessible to an international qualified investor base and is an AIFMD compliant product.

“The specialised investment fund was introduced by the Luxembourg Law of 13 February 2007. The SIF regime was amended by the Law of 12 July 2013 on alternative investment fund managers (AIFM Law). As a result, the SIF Law is now divided into two parts: (i) general provisions applicable to all SIFs, and (ii) specific provisions applicable to SIFs which qualify as Alternative Investment Funds (AIFs) and which are required to be managed by an authorised Alternative Investment Fund Manager (AIFM). Due to the broad definition of SIF AIFs, most SIFs qualify as SIF AIFs.”¹⁶⁶

The principle characteristics of the SIF are reduced restrictions on the type of assets in which it can invest in and a lighter supervisory regime. Therefore the restrictions regarding investment policy are mitigated and a limited risk diversification offers a wide possibilities for investing.¹⁶⁷ This offers also the opportunity to invest in any type of assets like Hedge funds, Real Estate and Infrastructure Funds, Private Equity and

¹⁶⁴ Cf. (Arendt & Medernach, 2015), p.7ff.

¹⁶⁵ Cf. Law of 13 February 2007 relating to specialised investment funds and - amending the law of 20 December 2002 relating to undertakings for collective investment, as amended; - amending the law of 12 February 1979 on value added tax, as amended.

¹⁶⁶ (ALFI - Association of the Luxembourg Fund Industry, 2017 (IV)), p.1.

¹⁶⁷ Cp. (Loyens & Loeff Luxembourg S.à r.l., 2012), p.2.

Venture Capital Funds, exotic assets such as art objects, jewelry, wine, etc. and intangible assets such as patents and other intellectual property rights.¹⁶⁸

Related to its legal setup, like the RAIF that is not investing into risk capital, the SIF has the possibility to opt for a number of legal structures and can be established either as FCP or as SICAV or SICAF. The SIF is product regulated and subject to the prior authorization of the CSSF. The SIF can rely on the same legal forms as the RAIF and can be either set up as a single fund or as an umbrella structure in form of multiple sub funds.¹⁶⁹

Like the RAIF it is important to be mentioned that due to the lower level of investor protection offered, this structure is not designed for the general public. It is designed and foreseen for sophisticated investors, which are looking for a maximum of flexibility in order to give scope to their expertise and their specific needs. The SIF must respect the principal of risk diversification.¹⁷⁰ The main regulatory requirements are the following:

- Accessible to informed investors defined as (i) Institutional investors; (ii) Professional investors and (iii) any private investor investing EUR 125,000 or received an appraisal from a financial institution confirming appropriate expertise and knowledge;*
- Minimum capital structure of EUR 1,250,000 to be reached within twelve months of approval by the CSSF;*
- There are no minimum and maximum number of shareholders;*
- Light risk diversification requirements prohibiting a SIF to invest in more than 30% of its assets or commitment to subscribe securities of the same type issued by the same issuer – for some type of assets to be reached up to 4 years.*
- A risk management policy at the SIF's level is required;*
- Required investors reporting consists in (i) the offering document (prospectus) as well as (ii) annual financial statements and report;*

¹⁶⁸ Cf. (Atdomco, 2013), p.2.

¹⁶⁹ Cf. (ALFI - Association of the Luxembourg Fund Industry, 2017 (IV)), p.3.

¹⁷⁰ Cf. (Luxembourg for Finance, 2015(II)), p.1.

- *Required service providers are (i) Central administration, registrar and transfer agent, (ii) Depository, (iii) External auditor;*
- *Net asset value (NAV) computation is required at least annually for reporting purpose.*¹⁷¹

Accordingly, the SIF shows many similarities to the RAIF, which is based on the orientation of the RAIF Law on the SIF-Law. This is related to the fact that the RAIF Law combines both regimes and “wraps them into one single legislative text”.¹⁷²

Compared to the RAIF it is subject to a product regulation through the CSSF and if the SIF qualifies as AIF, subject to the supervision of the AIFM for marketing purposes and in order to guarantee more assurance for investors due to the product and management supervision unless it is small in size. It must appoint a depository as well.¹⁷³

At this point it is important to mention that a draft law related to the SIF has been deposited before the Luxembourg Parliament on January 18th, 2016¹⁷⁴ amending as well the SICAR Law, the Part II Law and the AIFM Law:

“On January 18, 2016 the draft law amending (i) the law of June 15, 2004 (“SICAR Law”) relating to investment companies in risk capital (the “SICAR”), (ii) the law of February 13, 2007 (“SIF Law”) relating to specialised investment funds (the “SIF”), (iii) the law of December 17, 2010 (“UCI Law”) concerning undertakings for collective investment (“UCI”) and (iv) the law of July 12, 2013 (“AIFM Law”) relating to alternative investment fund managers (“AIFM”), has been deposited before the Parliament (the “Draft Law”).”¹⁷⁵

This draft law aims to revise the scope of the SIF Law in terms of the scope of investments, the limitation of investors as well as a review of the eligible assets

¹⁷¹ (Atdomco, 2013), p.2f.

¹⁷² (Arendt & Medernach, 2016), p.6.

¹⁷³ Cf. (Gutiérrez & Dukmedjian, 2016), p.17ff.

¹⁷⁴ Cf. Chambre des Deputes N° 6936; PROJET DE LOI portant modification de: – la loi modifiée du 15 juin 2004 relative à la société d’investissement en capital à risque (SICAR); – la loi modifiée du 13 février 2007 relative aux fonds d’investissement spécialisés; – la loi modifiée du 17 décembre 2010 concernant les organismes de placement collectif; – la loi modifiée du 12 juillet 2013 relative aux gestionnaires de fonds d’investissement alternatifs (Dépôt: le 18.1.2016).

¹⁷⁵ (Bonn & Schmitt, 2016 (I)), p.1.

related to atypical assets, and to set these investments more into the area of the RAIF Law which was specially created for these types of assets:

“The main purpose of the Draft Law is to revise the scope of the SIF Law in order to clarify the scope of investment and include a limitation depending on the type of investors. Indeed, SIF reserved to professional investors (as defined in Annex II of Directive 2014/65/EU of the European Parliament and of the Council of May 15, 2014 on markets in financial instruments (“MiFID II”)) (“Professional Investor”) can invest in all type of assets, including atypical assets such as wine, diamonds, insurance contracts, rights of economic football players, artworks or animals. For SIFs that are accessible to investors other than Professional Investors, the Commission de Surveillance du Secteur Financier (the “CSSF”) will determine, by way of regulation, the types of eligible assets.

For SIFs that are accessible to investors other than Professional Investors, the Commission de Surveillance du Secteur Financier (the “CSSF”) will determine, by way of regulation, the types of eligible assets.

A reserved alternative investment fund (“RAIF”), which is not subject to approval or supervision of the CSSF, will also be able to invest in atypical assets.”¹⁷⁶

Following the introduction of the SIF the SICAR will be introduced in the next chapter.

¹⁷⁶ Cf. (Bonn & Schmitt, 2016 (I)), p.1.

3.3.2. SICAR – Investment Company in Risk Capital

The Investment Company in Risk Capital (SICAR) refers to an alternative investment fund vehicle with the purpose to provide investments in securities representing risk capital. This structure is legally governed by the Luxembourg Law of 15 June 2004¹⁷⁷ as amended. It is, comparable to the SIF, also a product regulated, operationally flexible and a fiscally efficient vehicle that can classify as an AIF. It is accessible to an international qualified investor base and an AIFMD compliant product.¹⁷⁸

In terms of eligible assets, the SICAR may only invest in risk capital that is defined, e.g. “as direct or indirect investment in entities with a view to their set up, development or IPO”¹⁷⁹. This includes private equity, venture capital and indirect investments via subsidiaries, like e.g. a SOPARFI in opportunistic real estate.¹⁸⁰ In this case the “CSSF policy applies two criteria when assessing the eligibility of an applicant’s proposed investment policy, namely (a) high risk and (b) an intention to develop the portfolio entities”.¹⁸¹

As legal setup it can opt for an establishment as Investment Company and can be structured either as investment company with fixed or variable capital. The SICAR is product regulated and subject to the prior authorization of the CSSF. The vehicle can rely on the same legal forms as the RAIF and can also be incorporated as single fund or an umbrella structure in form of multiple sub funds.¹⁸²

The main regulatory requirements of a SICAR are the following:

“Due to the high risk associated with the investments made by a SICAR, the SICAR is only available to well informed investors defined by the law as institutional investors; professional investors, investors investing a minimum of EUR 125.000,- or any other investors for which a credit institution or other

¹⁷⁷ Cf. Law of 15 June 2004 relating to the Investment company in risk capital (“SICAR”) and amending - the law of 4 December 1967 on income tax, as amended - the law of 16 October 1934 on wealth tax, as amended - the law of 1 December 1936 on business tax, as amended - the law of 12 February 1979 on value added tax, as amended - the law of 20 December 2002 relating to undertakings for collective investment (Mém. A 2004, No. 95).

¹⁷⁸ Cf. (ALFI - Association of the Luxembourg Fund Industry, 2017(V)), p.1.

¹⁷⁹ (Richards, 2013), p.6

¹⁸⁰ Cf. (ALFI - Association of the Luxembourg Fund Industry, 2017(VI)), p.1.

¹⁸¹ (Richards, 2013), p.6.

¹⁸² Cf. *ibid.*

professional of the financial sector has certified that they are aware of the risk they have undertaken.

- The minimum subscribed capital of a SICAR is fixed at EUR 1.000.000,- and must be fully subscribed within 12 months after the SICAR has been approved by the local banking supervisory authorities, the CSSF.*

- The SICAR is subject to control by the CSSF and must be authorized by it in order to carry out its activities.*

- SICARs are not subject to investment restrictions and limitations.*

- The custody of the assets of a SICAR must be entrusted to a depository accepted by the CSSF.*

- A SICAR must publish accounts on a yearly basis and must publish an offering memorandum (“prospectus”). This prospectus must include the information necessary for investors to be able to make an informed judgment on the investments proposed to them and the risks attached thereto. The SICAR is obliged to provide those investors who request the information details of the net asset value of their shares at least every six months.*

- The valuation rules must be defined in the articles of incorporation. The only condition required by law is that the assets should be valued on the basis of the foreseeable sales price estimated in good faith.*

- The SICAR must appoint an independent auditor who will audit the annual accounts. The auditor has to be approved by the CSSF.*

- The same eligibility criteria apply to investors in SICAR as to investors in SIF. There are no minimum or maximum requirements as to investor numbers.”¹⁸³*

Compared to the SIF there is no requirement for investment diversification. Aligned to the aforementioned features, the SICAR is the vehicle for investors who intend to invest in risk capital within a stronger regulated environment.

Compared to the RAIF, as structure that can opt for sole investment into risk capital, the SICAR is subject to a product regulation through the CSSF and if the SICAR qualifies as AIF also subject to the supervision of the AIFM for marketing purposes.

¹⁸³ (Halsey Group SARL, 2015), p.1.

This is in order to guarantee more assurance for investors due to the product and management supervision.

Related to the above mentioned draft law, the SICAR will be subject to further supervisory requirements and the draft law sets further conditions that the SIF vehicle is already subject to:

“According to the Draft Law, the powers of the CSSF are expended and aligned with those defined in the SIF Law, in particular: (i) the appointment of the directors of the SICAR and/or of every successor will be subject to the approval of the CSSF, (ii) the identity of the portfolio management of the SICAR will be subject to communication to the CSSF, (iii) redemptions of units and/or shares of the SICAR could be suspended by the CSSF in the best interests of the investors. The amount of fine will be increased and the list of the persons concerned by the fine will be extended to the depositary and to the service providers.

The requirement of procedures and constraints of the SICAR are also aligned on the SIF.

The contributions into SICAR other than in cash will be subject to the auditor report and the SICAR must implement appropriate systems of risk management to detect, measure, manage and monitor appropriately the risk associated with the overall risk of the portfolio profile. The Draft law introduces also the conditions under which the SICAR will be able to delegate its functions.

Existing SICARs will have an additional deadline to comply with the new provisions (systems of risk management and delegation of functions) until December 31, 2016, if applicable.”¹⁸⁴

To complete the overview of the AIF landscape in addition to the RAIF, SIF and SICAR the Part II UCI fund will be introduced in the next chapter.

¹⁸⁴ (Bonn & Schmitt, 2016 (I)), p.1.

3.3.3. UCI – Part II Law Fund

The Law of 2010 was already introduced in chapter 2.2.2 UCITS, referring to its first part. The second part of the Law refers to UCI Part II funds which may fall under the landscape of the AIF regime. This chapter aims to provide a simple overview of the advantages provided by an UCI under the Part II Law.

The Part II UCI is based on the Part II of the Law of 2010¹⁸⁵ as amended. Compared to the introduced structures this vehicle is not subject to a specific named product law like the RAIF/SIF or SICAR. Depending on the setup it might not be subject to investor restrictions and can be therefore also eligible to retail investors. The legal structures and legal forms available are stated in Figure 9: Corporate forms available in Luxembourg.¹⁸⁶ Based on this the Part II Fund are more limited, compared to the RAIF/SIF or SICAR. It can opt for all legal structures, but as a SICAV it can only apply for the legal form of an SA and as a SICAF it cannot use the SCoSA.¹⁸⁷

Concerning eligible investors and investment restrictions the UCI is much more comparable to an UCITS. While there is no restriction on the type of investors the applicable risk diversification are more specific and stricter compared to the SIF/RAIF. For the UCI, these are defined by IML Circular n° 91/75. Further specific restrictions concerning funds adopting an alternative investment strategy are contained in CSSF Circular n° 02/80. If the UCI Part II fund qualifies as AIF, it must be managed by an authorized AIFM, unless it is small in size.¹⁸⁸ Furthermore, the relevant service providers involved in the operations of the fund have to be approved by the CSSF.

These funds are typically used when it is the aim to target retail investors. Due to very strict approval process and a much stricter supervision through the CSSF, the

¹⁸⁵ Cf. Law of 17 December 2010 relating to undertakings for collective investment: – transposing 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) (recast); – amending: – the Law of 20 December 2002 relating to undertakings for collective investment, as amended; – the Law of 13 February 2007 relating to specialised investment funds, as amended; – Article 156 of the Law of 4 December 1967 on income tax. (Mém. A 2010, No 239).

¹⁸⁶ Cf. Chapter 2.2.1. Legal forms and organizational structures.

¹⁸⁷ Cf. (KPMG - Luxembourg, 2016 (I)), p.6-7.

¹⁸⁸ Cf. (ALFI - Association of the Luxembourg Fund Industry, 2017 (VIII)), p.1f.

usage of an UCI might be very difficult and is very costly/expensive if only institutional investors should be targeted.¹⁸⁹

In a last step some forms of unregulated vehicles will be presented, but in respect of the topic of this thesis, only to complete the view of holding and securitization structures available to bundle special assets in an unregulated form subject to commercial law.

3.3.4. Non-regulated vehicles

In addition to the regulated instruments in Luxembourg further unregulated vehicles in the forms of the SOPARFI, Partnerships in form of, e.g. a SCS or a ScSp, the Securitization Vehicle (SV) and the Société de Gestion de Patrimoine Familial (SPF) are available.¹⁹⁰

The 'Société de Participations Financières' (SOPARFI) is not a special type of company but a conventional commercial entity governed by the 1915 Law on commercial companies. The legal setup of a SOPARFI can be selected from the forms listed in Figure 9: Corporate forms available in Luxembourg. A SOPARFI is typically designed for holding and financing private equity and venture capital investments. It may serve as a special purpose vehicle, a joint venture vehicle or as a private equity 'fund-like' vehicle. Due to these features, SOPARFIs can be used as stand-alone companies for acquiring private equity and venture capital, holding or financing vehicles or in combination with SIFs, SICARs and UCIs. The SOPARFI is attractive to be included in the setup of a SIF/SICAR or RAIF because of the exemption to certain taxation under specified circumstances. Profiting from the various Luxembourg DTTs it is especially attractive when investing in markets for which the DTTs apply.¹⁹¹

SOPARFIs are not limited to investor eligibility, investment and diversification restrictions and can be managed by a general partner, a sole manager or a

¹⁸⁹ Cf. (PWC - Luxembourg, 2016 (I)), p.12.

¹⁹⁰ Cf. (B.A. Trust Group, 2016), p.1.

¹⁹¹ Cf. (ALFI - Association of the Luxembourg Fund Industry, 2013 (II)), p.32f.

management body. Fully taxable, a SOPARFI can have access to the DTTs and can profit from exemptions on dividends, capital gains.¹⁹²

The Partnerships in form of SCS and SCSp, introduced in chapter 2.2.1, can be used solely or combined with an AIFMD compliant investment strategy, managed by an authorized AIFM and will therefore benefit from the European marketing passport. Used in the unregulated form it is governed by the 1915 Law on commercial companies and it benefits, like the SOPARFI, from a unlimited investor eligibility, the absence of investment and diversification restrictions and can be managed by a general partner.¹⁹³

Due to the fact that partnerships are highly flexible in the setting of terms of partnership and not supervised by the CSSF, investors are treated as owners for tax purposes.¹⁹⁴

The Luxembourg SVs introduced by the Luxembourg Law of 22 March 2004 as amended, SVs allowing the securitization of all types of risks and make it accessible to all types of investors. By pooling any type and form of assets the SV can acquire and issue securities for financing. This law provides lots of structuring possibilities and methods for transferring the risks to the vehicle. The securitization vehicle is flexible¹⁹⁵, “tax neutral and usually not subject to supervision by the Luxembourg financial regulator (if not issuing to the public on a continuous basis)”.¹⁹⁶

The legal setup of a SV can be selected from the forms available according to Figure 9: Corporate forms available in Luxembourg. Its main features are no investor eligibility requirements, limitation to securitization transactions, no diversification requirements, financing through the issue of equity/debt instruments, management by a sole manager, a management body or a general partner, segregation of assets via multiple compartments, tax neutrality, no supervision by the Luxembourg financial regulator (under conditions) while an independent auditor is required.¹⁹⁷

The Private Asset Management Company (SPF) or in French ‘Société de Gestion de Patrimoine Familial’ exists in Luxembourg since 2007 and a successor of the

¹⁹² Cf. (LCG International AG, 2013 (II)), p.3ff.

¹⁹³ Cf. (RSM International Association, 2015), p.2f.

¹⁹⁴ Cf. (Felten & Associates, 2016), p.4.

¹⁹⁵ Cf. (Bonn Steichen & Partners, 2014), p.16.

¹⁹⁶ (Felten & Associates, 2016), p.5.

¹⁹⁷ Cf. *ibid.*

Luxembourg Holding 1929. The SPF can be set up in the forms available according to Figure 9: Corporate forms available in Luxembourg law but it cannot be set up in the form of a transparent entity. Therefore, the purpose of the SPF is limited to the acquisition, holding and management of financial assets excluding any business activity.¹⁹⁸

Due to this limitation the SPF is a passive investment vehicle without commercial activity (including the management of a company where the SPF has a majority stake), and is reserved for private shareholders managing their wealth. The SPF regime benefits from tax neutrality and an exemption from corporate income tax, communal business tax and net wealth tax. Due to these exemptions, an SPF cannot take advantage of the available DTTs in Luxembourg and is exempt from the information exchange provision of the relevant DTT. Only the indirect tax authorities 'Administration de l'Enregistrement et des domaines' has to confirm that the setup conditions are eligible to those of a SPF. Due to the fact that the SPF is not limited in terms of eligible assets it offers various investment opportunities for private investors and can be considered as an alternative for private wealth and asset management purposes.¹⁹⁹

In summary, the unregulated vehicles offer additional opportunities to structure assets in alternative investment products and thus provide a wider prospect for investors who prefer non-regulated products.

After the introduction of the RAIF, its setup and the illustration of its available features and benefits compared to the other available AIFs and unregulated structures in Luxembourg, it can be stated that the product range in Luxembourg offers numerous structuring possibilities for potential initiators and investors.

In order to assess the impact of the RAIF structure on the Luxembourg AIF Market the next chapter introduces the leading European Fund Markets in terms of AIF, followed by an analysis if similar products already existing in those markets.

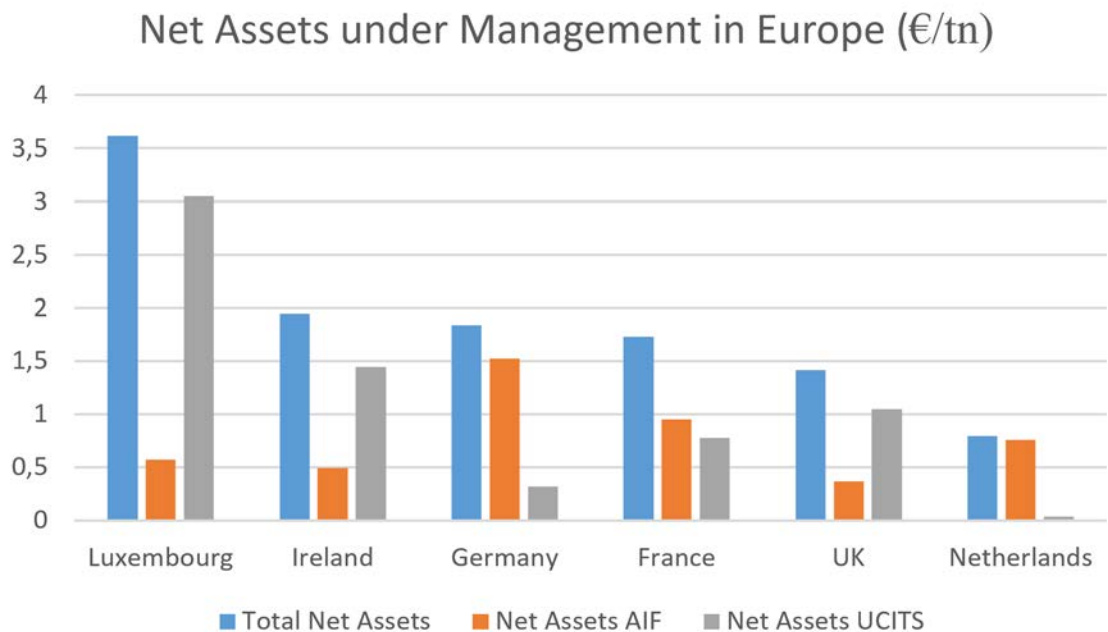
¹⁹⁸ Cf. (Bonn Steichen & Partners, 2014), p.17.

¹⁹⁹ Cf. (Bontemps, et al., 2015), p.1f, see also (Bonn Steichen & Partners, 2014), p.17.

3.4. Comparison of European Fund Markets

For this comparison, first of all, the most important fund markets have to be determined. For this purpose, the current available net assets of the different European countries will be compared and then analyzed with regards to the allocation of AIF and UCITS. The European Fund Asset Management Association (EFAMA) is a reliable source and data provider for this information.

Figure 19: Net Assets under management in Europe



Source: Own elaboration based on (EFAMA - European Fund and Asset Management Association, 2016 (II)), p.6 table 5, p.11 table 11, p.13 table 12.

As stated in Figure 19: Net Assets under management in Europe, and mentioned in Chapter 2.1. Market potential, Luxembourg is by far the largest market for investment funds within the Europe. The Luxembourg market is also a dominant pioneer in terms of net assets within UCITS. However, if the focus is set on the AIF markets, it is clearly visible that Luxembourg is not the market leader and is in fourth place behind Germany, France and the Netherlands.

The following table provides an overview of already existing structures from other jurisdictions comparable to the Luxembourg RAIF structure:

Figure 20: RAIF - comparison with similar EU Regimes

RAIF – Comparison with Similar EU Regimes

	Luxembourg RAIF	Irish QIAIF	French FPI	German Spezial AIF
AIF approval required?	No	Yes (24 hours)	No, AMF notification only	No, BAFIN notification only
Authorized EU AIFM	Yes	AIFM, sub-threshold AIFM (to upgrade within 2 yrs) or self-managed	Yes	AIFM or sub-threshold AIFM
AIF type/form	SA, Sàrl, SCA, SCS, SCSp, ScoSA, FCP	ICAV, PLC, Unit Trust, CCF, ILP	SA, SAS, SCS, FCP	Contractual or Corporate (investment restrictions apply)
Depository	Local	Local	Local	Local
AIF strategy	All	All	All	Restrictions: structure/form driven
Local board	No	2 Irish residents required	No	No

Source: (Seimetz, Astleford, Frognet, Goebel, & Terblanche, 2016), p.8.

In Germany, the ‘Spezial-AIF’ is the equivalent to the RAIF. Compared to the RAIF the Spezial-AIF is limited to well informed and professional investors. The German Special AIF is considerably more limited than the RAIF under design aspects. The German Kapitalanlagegesetzbuch (KAGB) does not envisage the possibility of an unregulated AIF. The same applies to an unregulated AIF umbrella structure. Conversely, there is nothing to prevent the administration of a Luxembourg RAIF set up in company form on the basis of the European passport by a German AIFM. Even under time-to-market conditions, the RAIF appears to be favorably placed against the German ‘Spezial Fund’ whose investment requirements and their significant changes have to be submitted to BaFin before the issue of shares.²⁰⁰

²⁰⁰ Cf. (Munchen, Babel, & Walry, 2017), p.2.

The Irish equivalent, “the QIAIF is also very flexible when it comes to eligible assets. It is regulated by the Central Bank of Ireland and is very quick to market (with a turnaround time of just 24 hours after a single filing of documentation with the Central Bank of Ireland)”.²⁰¹ Like for the RAIF the Central Bank of Ireland does not apply investment restrictions or requirements related to diversification, making the QIAIF available for nearly all investment strategies.²⁰²

Ireland as well as Luxembourg are well developed AIF jurisdictions. Meanwhile, lots of AIF products have already been set up by a growing number of asset managers governed by AIFMD and consequently received the EU passport. Currently, a majority of institutional investors within the EU is familiar with Irish QIAIF²⁰³ structures and Luxembourg SIFs as hedge fund/alternative investment vehicles. Compared to the Luxembourg Part II Fund Ireland offers a RIAFI solution, an AIF for retail investors comparable with the diversification rules and eligibility of assets.²⁰⁴ The RAIF may have potential to also achieve this level of recognition. Both are countries offering a wide range of investment funds and are also aiming to re-domicile offshore structures.²⁰⁵

In France the ‘fonds professionnels spécialisés’ (FPS) called, Professional Specialised Investment Funds including the former contractual CIS and contractual retail private equity investment funds (FCPR) are created for professional investors with a vehicle regulated under French law and a similar flexibility as to its eligible assets as the RAIF. This vehicle is reserved for eligible investors. Like the RAIF, it is not subject to authorization but must be declared to the French authority, the AMF, within one month after incorporation.²⁰⁶

In addition, in the Netherlands the Fonds voor Gemene Rakening (FGR), which is comparable with the Luxembourg FCP, is the commonly used vehicle for this kind of investments. The FGR is a contractual arrangement between the fund manager, the fund custodian and the investors. It has become market practice to use this vehicle

²⁰¹ (Carne Global Financial Services Limited, 2016), p.11f.

²⁰² Cf. (Fox & Rooney, 2015), p.4f.

²⁰³ Cf. (FundRock Management Company S.A., 2016), p.1f.

²⁰⁴ Cf. (Alexander & O’Callaghan, 2015), p.11ff; see also (Carne Global Financial Services Limited, 2016), p.11.

²⁰⁵ Cf. (ALFI - Association of the Luxembourg Fund Industry, 2016 (VII)), p.2; see also (Fox & Rooney, 2015), p.19.

²⁰⁶ Cf. (Autorité des Marchés Financiers, 2015), p.1f.

especially for Dutch and foreign pension funds.²⁰⁷ “The FGR terms and conditions are flexible and can be tailored for each specific case. For regulatory purposes, the FGR is either subject to regulation (UCITS or AIFM, as from 1 July 2013), or exempt from it depending on the purpose of the vehicle.”²⁰⁸ Compared to the RAIF, the FGR’s advantages are a very quick set up at a very cost efficient level and a wide contractual flexibility.²⁰⁹

In the UK especially LPs are the most favored structures of AIFs for investments into Private Equity and Real Asset Funds. Basically, the LPs are not regulated themselves, but with the appointment of an AIFM the regulatory status of the AIF will be governed by the AIFMD.²¹⁰

In summary, it has been demonstrated that different structures, which are comparable to the Luxembourg RAIF, are also available in other European countries. Apart from the main arguments, such as flexible structuring possibilities, less regulation and faster time-to-market, the RAIF is the only vehicle not being supervised by an authority, only by the AIFM. This is a clear and outstanding feature of the RAIF.

3.5. Interim result

It can be concluded that the RAIF, being the most recent vehicle added to the Luxembourg range of AIFs, has the major advantage of not being regulated or approved by the CSSF. It ensures a sufficient level of investor protection and is reserved to be managed by an authorized external AIFM.

The RAIF offers contractual flexibility and a faster time-to-market perspective in the context of a regulated framework that benefits from the European passport in order to ensure marketing to professional investors. Whereas, as the vehicle must comply with the requirements for management and administration, it has to appoint a depository which adheres to the duties and responsibilities provided by the AIFMD.

²⁰⁷ Cf. (Muntinga & Mulder, 2013), p.1ff.

²⁰⁸ (Muntinga & Mulder, 2013), p.1.

²⁰⁹ Cf. (Circle Partners, n.d.), p.2.

²¹⁰ Cf. (Carne Global Financial Services Limited, 2016), p.12.

As demonstrated, the RAIF is very much aligned to the SIF/SICAR regime, with the main difference that the RAIF does not have to be approved by the CSSF. Related to its investment strategy the RAIF is allowed to invest without restrictions but subject to diversification rules in order to spread the investment risk aligned to SIF/SICAR.

As the characteristics of the RAIF can be changed during the life of the fund without approval of the regulator, this offers fast reactivity and increased flexibility.

“The RAIF hasn’t been designed by Luxembourg to blindly add another string to its bow. During the past year a think tank composed of well-regarded industry players and members of the government have regularly met to assess the current needs and requirements of the market. Much research and studies have been compiled by the Luxembourg based alternative industry, largely through its industry bodies, to carefully interview local and international PE & RE houses, gather and analyse their input and formulate an appropriate action plan. This new vehicle has therefore not been rashly or hastily designed but has been well thought through, carefully considered and very much designed to meet the requirements of the most demanding industry players.”²¹¹

As a result, the positioning of Luxembourg with the RAIF offers significant opportunities related to the future setup of the Luxembourg AIF Market. The RAIF has potential to be an alternative to already known AIF vehicles and offers also special features for other investors within Europe and also globally for structures in Cayman Islands, the British Virgin Islands or even to Delaware structures. The compatibility with EU regulations will be total and the marketing reach truly global.²¹² This could attract investors who prefer security and regulation in form of the AIFM, in particular.

In a last step the following chapter will dive into the strategic direction of the Luxembourg AIF Market and will point out how the RAIF, in line with the whole range of AIFs, that Luxembourg offers, can attract potential investors in order to ensure innovation and attraction and generate competitive advantages in the future.

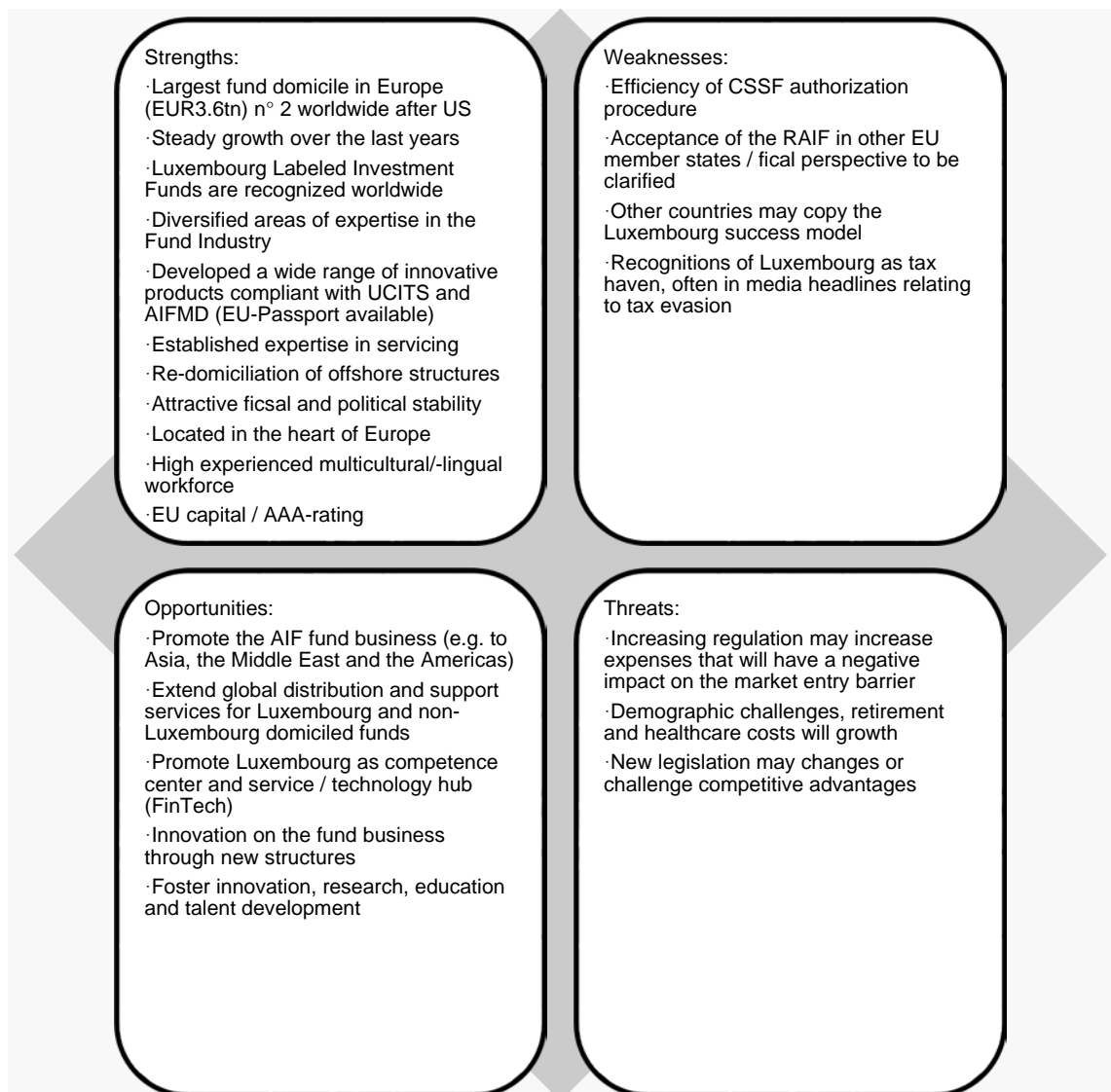
²¹¹ (Dundon & Despret, 2015), p.1.

²¹² Cf. (Arendt & Medernach, 2016), p.5.

4. Strategic direction of the Luxembourg AIF Market

In order to reiterate all of the aspects outlined in this thesis, this chapter provides a comparative overview, concerning the market potential of Luxembourg, the potentials of the AIF segment and the impact through the creation of the RAIF. The current strengths and weaknesses, as well as the opportunities and threats derived from this topic in form of a SWOT analysis are illustrated. In order to point out the most relevant elements considering this topic the Figure 21: SWOT-analysis of Luxembourg related to the Fund Business summarizes the results of this analysis, which is further detailed in the following pages.

Figure 21: SWOT-analysis of Luxembourg related to the Fund Business



Source: Own elaboration based on the reproduction of this thesis.

4.1. Strengths and weaknesses of the Luxembourg AIF Market

A. Strengths:

Luxembourg is by far the largest fund domicile in Europe and the second largest in the world after the United States of America.²¹³ With a new all-time-record reached in August 2016 Luxembourg benefits from EUR 3.6tn of Net Assets under Management.²¹⁴ Based on these results Luxembourg profits from a steady growth rate within its fund business, especially the alternative investment sector has been identified being a main growth driver.

Luxembourg funds are recognized worldwide as brand/label, e.g. Luxembourg UCITS Label or the SIF Label, and are distributed actually in more than 70 countries worldwide with a particular focus on Europe, Asia, the Middle East and the Americas. Related to the fund initiators, the main countries of origin are US, United Kingdom, Switzerland and France.²¹⁵

The current EU regulations, e.g. UCITS and AIFMD have been adapted in Luxembourg. Consequently, Luxembourg offers a wide range of innovative vehicles under UCITS and AIFMD, e.g. UCITS, RAIF, SIF, SICAR and the UCI, in line with the EU passport for marketing within the EU. Luxembourg has been identified as one of the leading fund industry centers especially for private equity, venture capital, real estate, hedge funds and funds of hedge funds, covering all the needs of investors and initiators.²¹⁶

In Luxembourg well developed and diversified areas of long standing expertise have evolved, e.g. Asset Management, Asset Servicing, Service Providers, Legal Advice, Auditors, Management Companies, Wealth Management, Structured Finance, Corporate Banking, Insurances & Reinsurances and a growing business related to Asia the Renminbi Business.²¹⁷ Furthermore, Luxembourg offers re-domiciliation of offshore structures.²¹⁸

²¹³ Cf. Table 2: Worldwide numbers & total net assets of regulated open-end funds.

²¹⁴ Cf. chapter 2.1. Market potential.

²¹⁵ Cf. *ibid.*

²¹⁶ Cf. chapters 2.2.2. UCITS, 2.2.3. AIF – Alternative Investment Funds and 3. RAIF – Reserved Alternative Investment Fund.

²¹⁷ Cf. chapter 2.1. Market potential.

²¹⁸ Cf. 3.4 Comparison of European Fund Markets.

Luxembourg evolved an encouraging taxation environment, profits from a broad DTT network with over 77 countries and the CSSF is a satisfying regulator within the fund business and the financial area.²¹⁹

Located in the center of Europe, positioning Luxembourg as a natural center for diversification in a stable economic and political environment, strong macro-economic growth, consistently above the EU average growths rates, Luxembourg reports the world's lowest debt-to-GDP ratio that institutes the best indicator for fiscal stability. With a skilled and multilingual as well as a multicultural workforce, Luxembourg profits from a unique concentration of highly experienced investment fund experts, fund lawyers, audit firms and tax advisors in terms of cross-border registrations of both UCITS and non-UCITS funds. Luxembourg can profit in all relevant aspects of product innovation and development, administration and distribution from this experience.²²⁰

Luxembourg is a founding member of the EU, a EU capital and the home of several EU institutions e.g. the European Investment bank, the ESM European Stability Mechanism, the European Court of Justice, the European Court of Auditors, the European Parliament Secretariat.²²¹

In summary, these are reasons why Luxembourg is still one of the few European countries which received an AAA rating confirmed by Standard & Poor's, Moody's and Fitch. Its stable banking sector combined with the stable political, social and economic environment verify this rating.²²²

Weaknesses:

The weaknesses are, e.g. a long authorization procedure of the regulator CSSF to approve the growing requests for fund approvals. Needs for more efficient authorization processes and more contractual flexibility for a faster time-to-market have been expressed by the market participants.²²³

Other countries may copy the Luxembourg success model.²²⁴

²¹⁹ Cf. chapter 3.2 RAIF & AIF/M regulation absence of CSSF supervision.

²²⁰ Cf. *ibid.*

²²¹ Cf. *ibid.*

²²² Cf. *ibid.*

²²³ Cf. chapter 3.1 RAIF – introduction and setup.

²²⁴ Own suggestion.

It remains to be seen if the RAIF will be accepted in other EU member states from a fiscal perspective that may be subject to the acceptance by the relevant countries. The SIF had different problems in the beginning and access to the DTT is still not entirely solved.²²⁵

Luxembourg is still referred to as a tax haven in the media, although all EU regulatory requirements have been implemented. As a result, Luxembourg is often mentioned in tax evasion processes in relation to court trials. “If people have heard of Luxembourg at all, the words “tax haven” will tend to jump into their minds. But if a recent report is to be believed, it is unfair to single out the Grand Duchy for offering uniquely advantageous tax conditions to international firms.”²²⁶

4.2. Opportunities and threats of the Luxembourg AIF Market

Opportunities

Luxembourg’s opportunities are the big potential for AIF business in Asia and promoting the AIF business in the Middle East and the Americas.²²⁷ Currently ALFI and Luxembourg for Finance are promoting the Luxembourg Fund Industries, performing roadshows in the countries in the above mentioned regions and launching working groups to strengthen cooperation. ALFI has set itself five equally important key objectives:

- “Promote practices that align the interests of investors and industry
- Articulate the essential role of investment funds for the global economy
- Connect investors with worldwide market opportunities
- Ensure Luxembourg remains the fund centre of choice for asset managers
- Stimulate innovation, research, education and talent development”²²⁸

Another opportunity identified is to promote Luxembourg as the competence center and service/technology hub (FinTec) in terms of expertise to support global

²²⁵ Cf. (Deloitte Luxembourg, 2015 (I)), p.1f.

²²⁶ (Evans, 2016), p.1.

²²⁷ Cf. chapter 2.1 Market potential.

²²⁸ (ALFI - Association of the Luxembourg Fund Industry, 2015 (III)), p.1, see also (ALFI - Association of the Luxembourg Fund Industry, 2015 (IV)), p.1f.

distribution of funds and asset servicing combined with the presence of all major global players in fund administration of alternative assets.²²⁹

Furthermore, innovation of the fund business, the development and adaption of fund vehicles and new structures is an important opportunity to remain competitive. Because the asset industry seeks new business opportunities in a fast changing world, innovative ideas and creation of new models become essential for staying successful.²³⁰

“Thanks to its international openness, Luxembourg is ideally positioned to source innovation and best practices worldwide. It also constitutes a living lab, with a multi-cultural population and workforce encapsulating global trends and investor expectations on an ideal scale for market research. Once innovation and research is underway, management needs to deploy it rapidly throughout its organisation. International education and talent development become key concerns, and Luxembourg needs to improve its support to the industry in these areas. Developing talent in international risk management and compliance will be a primary area of focus.”²³¹

Threats:

Threats are mainly related to an increasing regulation. Expenses increase due to more regulatory changes and this will lead to a negative impact on the market entry barrier, which is mostly cost depended.²³²

Demographic challenges are the growing cost and commitments to retirement and healthcare schemes. “As the baby boomer generation approaches retirement and life expectancy continues to improve, public sector pension liabilities will grow. This will lead to a drawdown of assets, but also reinforce the need for greater personal savings and retirement income. Once investors see the implications, demand for capital preservation and income yielding strategies will increase, creating opportunities for new products and services.”²³³

²²⁹ Cf. (ALFI - Association of the Luxembourg Fund Industry, 2016 (VIII)), p.2.

²³⁰ Cf. (ALFI - Association of the Luxembourg Fund Industry, 2015 (III)), p. 5f.

²³¹ (ALFI - Association of the Luxembourg Fund Industry, 2015 (III)), p.6.

²³² Cf. (American Chamber of Commerce in Luxembourg, 2013), p.1ff.

²³³ (ALFI - Association of the Luxembourg Fund Industry, 2015 (III)), p.1f.

5. Empirical analysis

This chapter aims to enrich the gained theoretical aspects of the Luxembourg RAIF, the AIFs and its related regulation and business in Luxembourg with practical insights from market players. The purpose of this qualitative research is to gather information and practical insights from professionals of the AIF industry related to the initially introduced research questions:²³⁴

- What is a RAIF and where is the difference to other fund vehicles (e.g. SIF)?
- How is the RAIF interlinked to AIFMD?
- What role does RAIF play in Luxembourg?
- Which investors does RAIF target and what are the benefits for investors?
- How does RAIF influence the strategic direction of the Luxembourg Fund Market?
- Which impact does RAIF have on the Luxembourg Fund Market and on other European Fund Markets?
- What are the challenges for the future in order to retain competitive advantages for Luxembourg?

Based on the above questions, five semi structured expert interviews have been conducted to retrieve insights and opinions. The following chapters introduce how the interview and the potential question catalogue were developed and how the interview partners have been selected. Afterwards, a summary of the interviews results is presented.

5.1. Interview development

In order to obtain these practical insights, in addition to the derived theoretical knowledge that is also the basis for the practical use, potential questions for the interviews were to be developed. The interviews shall introduce the practical aspect of the RAIF, its usage in and outside of as well as for Luxembourg, taking into consideration the specific features of the available range of Luxembourg AIF products. Advantages and disadvantages for the Luxembourg AIF Market shall be

²³⁴ Cf. chapter 1.2 Objective.

derived from a practical insight and it should be determined which structures are used in practice and what the impact of the RAIF is. Therefore, the qualitative research method of a semi-structured²³⁵ expert interview was used.

The aim during the development of the interview was to formulate questions that are flexible, easy to handle and related to the specified area of research. Especially in the interview itself, the interviewer must be able to respond to issues that emerge during the interview process. Meaning, a fixed interview catalogue like it is used in quantitative research would not be the right choice for this research task.²³⁶

Taking the above into consideration, a potential catalogue of questions has been prepared in order to gather practical insights and information that have an impact on the related field of research. The developed question catalogue is stated in Annex VI and consists of 13 questions based on the research questions.

This developed question catalogue²³⁷ was used as “[...] ‘interview guide’ that outlines the main topics the researcher would like to cover, but is flexible regarding the phrasing of questions and the order in which they are asked, and allows the participant to lead the interaction in unanticipated directions.”²³⁸

The potential questionnaire was made available to the interview partners in advance. Afterwards, the respective appointments for the survey were agreed. It was the goal to conduct all interviews personally with each interview partner. In order to fully concentrate on the interviews, the sessions have been recorded to put down the interview results in writing. This method has been chosen to capture every detail and cover all aspects in the analysis of the interviews.²³⁹ This allowed the interviewees to check their statements and to officially release the content for the further use in this thesis, also under the aspect of a potential publication.

²³⁵ Cf. chapter 1.4 Methodology.

²³⁶ Cf. (King & Horrocks, 2010), p.35.

²³⁷ Cf. Annex VI.

²³⁸ (King & Horrocks, 2010), p.35.

²³⁹ Cf. (King & Horrocks, 2010), p.45f.

5.2. Interview partners

In order to gain insights into different fields of expertise surrounding AIF products, interview partners from those professional fields have been contacted. The selection of these persons had to be in accordance with the characteristics of the chosen qualitative research method; the expert interview.

The term 'expert interview' is reserved for interviews with informants who have expertise on a certain subject.²⁴⁰ This led to the question of which group of people would be considered as experts.

In general, the term 'expert' is related to a person with a special knowledge of a field of research.²⁴¹

“An expert has technical, process and interpretative knowledge that refers to a specific field of action, by virtue of the fact that the expert acts in a relevant way (for example, in a particular organizational field of the expert’s own professional area). In this respect, expert knowledge consists not only of systematized, reflexively accessible knowledge relating to a specialised subject or field, but also has to a considerable extent the character of practical or action knowledge, which incorporates a range of quite disparate maxims for action, individual rules of decision, collective orientations, and patterns of social interpretation.[...] In other words, the possibility exists that the expert may be able to get his/her orientations enforced (at least in part). As the expert’s knowledge has an effect on practice, it structures the conditions of other actors in the expert’s field in a relevant way.”²⁴²

Based on the facts presented, the interview partners should have an experienced view on the research topics. Ideally, this includes professionals in Luxembourg that are working in the professional field of AIF's in Luxembourg and have been involved in the setup or in projects conserving the RAIF. Furthermore, these professionals of the Luxembourg AIF Industry, should have looked at this development from different angles, meaning they should be selected from different areas of involved parties around the AIF Industry who are in contact with the RAIF.

²⁴⁰ Cf. (Boeije, 2010), p.63.

²⁴¹ Cf. (Bogner, Littig, & Menz, 2009), p.100.

²⁴² Ibid, p.54f.

Subsequently, five interview partners with an expert status within the industry field, have been selected. Two partners being experts in the Asset Servicing/Management related to the Fund/Banking Industry, one being a Legal Advisor in a law firm, one operating in the Alternative Fund Sector as Advisor as part of the consultants and one from the ALFI, being the representative body of the complete range of service providers acting in the Luxembourg Fund Industry and including: “custodian banks, fund managers and administrators, transfer agents, fund distributors, law firms, consultants and tax advisors, auditors and accounting firms, IT services companies, etc.”.²⁴³

5.2.1. Summary of the interview I

The first interview²⁴⁴ was conducted on January 20th, 2017 with Hermann Kranz from UBS Europe SE, Luxembourg Branch in his role as Head of Asset Servicing EMEA for the Asset Servicing Business in Luxembourg. Nine questions from the questionnaire were addressed during the interview and aimed to derive information related to H. Kranz’ experience in the financial industry including the fund industry, concerning the setup of AIFs especially the RAIF, the advantage of the absence of product supervision through the CSSF as well as its advantages and potential threats related to the marketing in Europe. Furthermore, questions related to the cross-border aspects as well as the typical investments were addressed. In the end H. Kranz provided an overview of the allocations about AuM within Europe with a special focus on Germany. Additionally, a personal opinion on the added value of the RAIF for investors outside of Luxembourg as well as for Luxembourg as domicile for RAIFs. However, in part, the wording of the questions has been matched to the progress of the interview and new questions arose during the interview aligned to the information provided.

H. Kranz has 23 years of experience in the financial sector and gained a special knowledge in the Asset Servicing sector, with a focus on the setup of UCITS, SIFs and now also the RAIF. Heading the Asset Servicing department of UBS Europe SE, Luxembourg branch and having reached impressive growth rates in recent years, H. Kranz aims to derive further remarkable growth. This should be achieved in alignment with the Luxembourg Fund Market growth plan for the future. UBS will

²⁴³ Cf. (ALFI - Association of the Luxembourg Fund Industry, 2015 (V)), p.1.

²⁴⁴ Cf. Annex, Interview I.

especially serve clients from the segments such as Ultra High Net Worth, Global Family Office, Financial Intermediary, Third Party Institutional as well as UBS' own Funds. A special focus is set on launching SIFs and now also the RAIF structures, in addition to the well-integrated flagship product UCITS. Furthermore, the trend of setting up regulated onshore products instead of structures in offshore locations and converting existing ones back into regulated onshore structures was mentioned in this regard.

Associated with the CSSF approval processes H. Kranz pointed out that the growing number of fund launches in Luxembourg led to a slowdown of the approval processes. The Luxembourg Fund Industry is dependent on fast fund launches in order to be competitive with other European markets like, e.g. Ireland with a process duration of about 4 weeks, compared to Luxembourg with a current duration of up to 3-4 months. Although an accelerated approval procedure with the CSSF, the straight-through process, has been agreed, the RAIF is now also being considered as new approach to mitigate the long lasting approval processes. H. Kranz' experience showed that both possibilities shorten the time-to-market to about four weeks, even if the RAIF might have the potential for three days. The first experience to launch a RAIF took four weeks to establish the structure. It was acknowledged that there might be potential to accelerate the process.

Related to the RAIF's advantages and the acceptance of other European countries H. Kranz compared the RAIF with the SIF and the SICAR vehicles. It was derived that the RAIF can mirror 1:1 both structures in terms of possible investments, an advantage that many investors have been asking for. Furthermore, H. Kranz noted that here might be countries questioning the tax status of the RAIF from a fiscal perspective, similar to the issues in the introducing phase of the SIF. In order to profit from fiscal acceptance comparable with a UCITS or a SIF, this may take some years. Feedback will be provided once the first customers close their financial year and received feedback from their tax advisor respectively their local tax authority. For the time being, it is expected that the RAIF will be accepted from a fiscal point of view. While the fiscal handling in Luxembourg is well known, other countries may also consider 'gold-plating' the RAIF from a fiscal view by implementing new regulations.

In terms of typical investments by the RAIF, H. Kranz mentioned the wide degree of investments possibilities in line with the SIF or SICAR law, depending of the investment choice, the RAIF can opt for. It was pointed out that especially succession

rules are considered as reasons for setting up SIFs and RAIFs. The aim is to bundle, e.g. company participations as assets in the fund and then allocate the fund units to the next generation. This simplifies the succession and can even be attractive in terms of taxation and controlling the risks taken by the manager.

These facts were compared to Irish RIAIF, QIF and PIF AIF structures, comparable with a Luxembourg RAIF or SIF. The RIAIF was introduced in Ireland with the aim to gain back market shares from Luxembourg. The RIAIF is also based on the QIF and PIF offers equal aspects like the SIF. Having a decreased demand in comparison to the Luxembourg RAIF, H. Kranz pointed out that Luxembourg is still ahead due to its more robust environment and by the number of DTTs that have to be taken into account. In addition, European customers tend towards Luxembourg structures.

During the interview a special focus was set on the allocation of AuM especially considering to the market leadership of Germany in AIF structures. H. Kranz attributed this fact to Germany being the biggest European domestic market. This also led to the conclusion that in particular Luxembourg funds are marketed cross-border, whereas German funds are not typically subject to cross-border distribution. Nevertheless, raising marketing activities for Luxembourg vehicles could increase this business. A growth potential for the RAIF is expected in line with the one of the Luxembourg AIF Market. In the past, a notable disadvantage was particularly related to the preference of US hedge fund managers for the Irish or the UK environment, due to the language compatibility and the closer time zone to the US markets. All in all, the target groups are now Middle East, Asia and Latin America because these groups have no preference where their assets are booked, but this group is attracted by the advantages of the Luxembourg Fund/Banking sector. Nowhere else in Europe is the concentration of consultants, tax specialists, tax lawyers, administrators and custodians so high.

Analyzing the answers, the main features of the RAIF structure H. Kranz foresees are a raising potential for wealthy families, especially the billionaires. Billionaires leaving offshore structures and targeting into regulated tax transparent onshore structures. Taking into consideration that Luxembourg for Finance, the ABBL and the ALFI carry out marketing activities and communication for Luxembourg products all over the world, Luxembourg investment vehicles become better known in the focused areas. It was also pointed out that UBS is actively communicating the AIF products like the RAIF, in particular in Asia, as a potential and attractive regulated

alternative to the predominant Cayman Funds structures. Therefore, the RAIF is not only an answer to enhance the slow approval process but also an opportunity for the AIF Industry. Whereas the UCITS will still play the most important role in Luxembourg.

5.2.2. Summary of the interview II

The second interview²⁴⁵ was conducted on January 23rd, 2017 with Christopher Dortschy from Allen & Overy in Luxembourg in his role as counsel in the Investment Funds Department. Eight questions from the questionnaire were addressed during the interview and aimed to derive information related to C. Dortschy's experience in Funds' Law practice in the fund industry. The questions have been selected according to C. Dortschy's involvement and aiming to address the following: the structuring possibilities of RAIFs, most favorable AIF structures and the RAIF's impact on EU investors, tax/fiscal aspects, marketing and an future outlook of the RAIF for the strategic orientation of the Luxembourg AIF Market within the EU and potentially even global.

C. Dortschy has 10 years of experience practicing Investment Fund Law and the structuring of Luxembourg AIFs. C. Dortschy deals primarily with the structuring of Luxembourg Fund Vehicles including UCITS, AIF and also UCIs as well as unregulated fund structures not governed by UCITS or AIF in the meaning of AIFMD. Furthermore, C. Dortschy is experienced in advising AIFMs and ManCos, e.g. for the process of licensing as well as for policy reviews.

Having not yet been involved in an entire RAIF incorporation process, C. Dortschy compared the part of incorporation with those of the most popular unregulated structures, the SCS and the SCSp qualifying as AIF, with a full scope AIFM. The RAIF is similar in the setup because a notary confirmation is needed but in addition the confirmation of the RSCL is required before money of investors can be raised and accepted. C. Dortschy pointed out that this might be a drafting error based on the proposal of the SIF Law, minor legal subtleties that may occur in the beginning. With a focus on the potentials provided by the RAIF compared to the features of

²⁴⁵ Cf. Annex, Interview II.

already existing fund structures in the Luxembourg AIF Market, C. Dortschy named the possibility of opting for an umbrella structure. In the view of C. Dortschy not really a convincing argument because also unregulated structures may synthetically create such a benefit. Particularly, with regard to distribution across the borders, there is no obligation in terms of acceptance from other countries for the RAIF related to the umbrella structure.

What is rather decisive, is the fact that the RAIF can opt for being set up in the corporate structure form of a SA, a SARL and an SCA - so called "tax blockers". Normally these are not being used for unregulated AIF vehicles under the current tax legislation, but now combine the SIF, SICAR taxation under the RAIF regime. A great success for investors preferring transparent solutions. Furthermore, structuring as an SCA allows direct access to the Luxembourg DTTs, an innovation that is not possible for the unregulated forms of SCS/SCSp. Especially with the introduction of BEPS, where obscure tax structures will be topic to deeper investigation, the RAIF has huge potential to become successful also from a substance view.

With the view on the SICAR and its unattractiveness due to long lasting approval and authorization procedures by the CSSF, C. Dortschy expects changes for the RAIF opting for risk capital investments: "Having a fully taxable entity which receives a special tax treatment because of its very specific investment strategy and therefore permitted to deduct its entire investment income from its taxable base. In the form of a RAIF, incorporated as an SCA for instance, it might be that this is really going to be a successful vehicle."²⁴⁶ Particularly the absence of product regulation by the CSSF, long lasting approval processes might be a subject of the past. Nevertheless, with regard on the cross-border marketing the RAIF must have an AIFM that applies for the passport by submitting the relevant information and documentation to the CSSF. The CSSF issues the V-number to the AIFM in order to progress with the RAIF.

From a tax perspective, C. Dortschy guessed that the RAIF will be accepted in other countries identical to the SIF /SICAR, according to the investment/tax regime it opts for, but this is largely dependent on the regulators and tax authorities of the foreign countries.

²⁴⁶ Cf. Annex, Interview II.

Related to the possibilities of the RAIF and its impact on the Luxembourg AIF Market especially to the strategic orientation, C. Dortschy highlights the possibility of the RAIF to be seen as an established brand in several years, once sophisticated investors in Europe or even globally have understood the functionalities of the RAIF. To come to this stage, marketing activities and communication for the RAIF need to be undertaken in order to make investors and potential initiators responsive to the RAIF. Once established, C. Dortschy sees a success potential for the RAIF similar to the SIF story. For the time being, a lot of advisory and explanation is needed to convince, e.g. institutional investors, like pension funds or professional provision schemes with internal committees, for the RAIF. The RAIF is not yet part of structures within their procedures and policies foreseen for their investments. Once this changes, C. Dortschy predicts a new selling proposition for funds Luxembourg.

5.2.3. Summary of the interview III

The third interview²⁴⁷ was conducted on January 24th, 2017 with Jendrik Fuhrmann from Hauck & Aufhäuser Alternative Investment Services S.A. in Luxembourg. Eight questions from the questionnaire were addressed during the interview and aimed to derive information related to J. Fuhrmann's experience in the structuring of AIF vehicles in the AIF Industry. The questions have been selected according to J. Fuhrmann involvement and aimed to address: the structuring possibilities of RAIFs, potentials and advantages for the investors in Luxembourg and in the EU, threats in the distribution, RAIF compared to LP, potential for the strategic direction of Luxembourg AIF Market and a future outlook.

J. Fuhrmann is an expert for structuring AIF in all forms. This includes SIFs, SICARs, RAIFs as well as corporate structures like, e.g. LPs (SCS, SCSp) and Securitization Vehicles. For the time being the most favored investment structure in the client base of J. Fuhrmann's working environment is still the SIF setup in the corporate form of a SCS. This structure is widely recognized and a well-known instrument.

The team of J. Fuhrmann is currently structuring two RAIFs. Actually many potential clients have already been asking for the RAIF. The interest in this product is growing

²⁴⁷ Cf. Annex, Interview III.

but most clients are not yet familiar with the structuring possibilities, therefore opting for the already known SIF product. J. Fuhrmann believes that the RAIF could cause problems for investors because the vehicle is not very well known. In addition it requires a different due diligence process. Once the structure is understood by the clients, there might be more requests to set up RAIFs.

With a focus on the potential provided by the RAIF for investors and typical investments J. Fuhrmann pointed out the time-to-market advantage and the setup without the CSSF. According to J. Fuhrmann this provides more flexibility and offers cost saving potentials because no fees have to be paid to the CSSF. J. Fuhrmann added that a first glance it seems the RAIF has less regulation, but the RAIF Law implemented strong regulatory standard requirements that are close to those ones of the SIF. For typical investments J. Fuhrmann stated that the RAIF, depending to the chosen investment strategy, can invest in nearly any type of assets implicitly to the investments of the SIF/SICAR Law on the alignment to risk spreading or exclusively risk capital investments.

In reference to added value, J. Fuhrmann identified potential especially for non-EU managers targeting European investors by structuring products. For the distribution of the RAIF in Europe or even globally, J. Fuhrmann did not expect threats or problems. Linked to the notification passport the RAIF should benefit from a cross border distribution without difficulty at least in the EU/EEA.

For the potential to expand the AIF business in Luxembourg and having an impact on the strategic direction of the Luxembourg AIF Market, J. Fuhrmann compared the introduction on the RAIF with the early days of the SIF in 2007. Though the number of launched RAIFs has not reached the numbers of the SIFs in their beginning, J. Fuhrmann predicted the RAIF to become a commonly used product in the long-term, depending on the regulatory development in the coming years. The RAIF might not be the number one choice of clients because distributing an AIF, not subject to regulatory approval, within the EU or even globally is today not common standard.

From a professional point of view out of the fund structuring field J. Fuhrmann expects that within Hauck & Aufhäuser a shift from non-regulated companies towards the RAIF will be seen, as these structures were only very rarely used in the past. In addition, the wider choice of legal entities within the RAIF offers more flexibility.

J. Fuhrmann added that the RAIF is generally a good beginning of setting the regulatory focus on the manager and not on the product anymore and avoiding a double regulation. The RAIF is therefore a good addition to the toolbox Luxembourg offers, although J. Fuhrmann doubts that the RAIF will have the potential of a predominant structure in the future. Experiences showed that the primary market Germany is not really attracted at the moment, mostly based on clients questioning the absence of product regulation. Therefore, J. Fuhrmann predicts an unchanged trend to the SIF complemented by RAIF products.

5.2.4. Summary of the interview IV

The fourth interview²⁴⁸ was conducted on February 2nd, 2017 with Susanne Weismüller from the ALFI, in her role as Senior Legal Advisor. The whole range of questions were addressed during the interview and aimed to derive information related to S. Weismüller's experience as coordinator of the association's regulation advisory board and alternative investments committee. Also, two more specific questions have been raised during the interview process, aiming to obtain insights on the identified double layer of supervision and the topic of gold plating.

S. Weismüller presented the number of registered RAIFs as of January 23rd, 2017. In total 55 RAIFs in form of a single funds and umbrella funds have been registered, not considering the number of compartments in case of an umbrella structure. S. Weismüller was involved in the process of introducing the RAIF, because ALFI is being represented in the High Committee for the Financial Centre (Haut Comité de la place financière HCPF) and its subgroup responsible for AIFs, the first discussions about the idea of the RAIF occurred in these committees.

With a focus on the most favorable structures in Luxembourg, and how the RAIF is interacting with other AIFs, it was asked if the RAIF would fight against the other AIFs or if it would be a parallel world. S. Weismüller pointed out that intention of introducing the RAIF was not to cause a fight against or between the other AIF vehicles. Rather more, this was linked to the different needs and demands of AIFMs that have to be considered. Based on this, S. Weismüller pointed out the different features of the

²⁴⁸ Cf. Annex, Interview IV.

SIF, the SICAR, and UCI covered by Part II of the Law of 2010. The SIF offers a flexible legal framework, a lighter prudential regime appropriate for sophisticated (well-informed) investors, whereas the SICAR was specifically designed for private equity investments. UCI part II funds are open to professional and retail investors. S. Weismüller highlighted that the success of the SIF will continue because it profits from the product stamp from the CSSF, an important feature of additional assurance for certain investors. All three vehicles can classify as AIF and have to be managed by an authorized AIFM, unless they are small in size and must appoint a depositary. Considering the potential investments of the fund structures, S. Weismüller differentiated the possibilities for the three products. For the SIF traditional and exotic investments are permitted but capped at a maximum of 30% in securities of the same issuer subject to certain exceptions. Whereas the SICAR is a specific company for private equity investing in risk capital not bound to a diversification requirement. The Part II funds have no restriction in terms of eligible assets, but its investment objective as well as its strategy are subject to prior CSSF approval. The risk diversification requirements are laid out by several circulars.

As potential impact on the SIF Law as well as on the SICAR Law, S. Weismüller named a current draft law adoption of these laws by revising the scope. Funds investing in certain exotic investments, which are difficult to value (e.g. luxury goods like watches or horses), should in the future rather be set up as RAIFs. Furthermore, the draft law aligns the SICAR regime to the SIF regime.

For the newest structure, the RAIF, S. Weismüller explained that its main advantage is not being subject to the CSSF approval, although investor protection is ensured by its obligation to appoint an authorized external AIFM and a depositary subject to responsibilities provided by AIFMD. S. Weismüller stated, that the RAIF is aligned to the SIF regime but profits, due to the absence of product regulation by the CSSF, from a much faster setup time being a gain for the AIFM. S. Weismüller predicted that it might need more time in the beginning in order to find the right partners for the managers and in order to set up the contracts. But, having solved these steps a setup of the structure can be finalized within 1-2 weeks.

In order to complete the overview of the AIF product range S. Weismüller added the European Fund vehicles ELTIF (long term assets investments), EuVECA (funds collect venture and growth capital) and EuSEF (funds are dedicated to social businesses). Taking this offering into consideration, Luxembourg offers a wide

ranged toolbox of fund vehicles and investment solutions with the ability to meet all interests requested from initiators and investors, being a really important fact for everyone, S. Weissmüller highlighted.

As special features of the RAIF, S. Weismüller expressed most notably the benefits of time-to-market, less costs because of the absence of CSSF approval, a setup as SICAV that is not possible for unregulated vehicles, the setup in form of an umbrella structure and especially the marketing aspect governed by the AIFMD passport. The following typical investments possibilities were furthermore outlined by S. Weismüller. In general the RAIF is not subject to investment restriction and allows traditional and exotic assets such as private equity, real estate, hedge funds, infrastructure, debt acquisition, loan origination, listed securities and any types of real or tangible assets. Furthermore, the RAIF may opt, as a derogation to this rule, for investing only in risk capital not subject to the risk diversification rules and applicable to the SICAR taxation.

Based on this, S. Weismüller indicated the added value to investors and pointed out that due to the broad investment possibilities the RAIF can be marketed in and outside of Luxembourg to well-informed investors. Therefore the RAIF is a perfect combined tool for AIFMs to offer unlimited possibilities of investments for investors in several countries with different backgrounds. Fund investors and initiators can choose the vehicle that meets their needs. If opting for a higher level of supervision by the regulator, the SIF or SICAR suits best. In case indirect supervision is sufficient the RAIF would suit better.

In terms of cross-border investment and marketing, S. Weismüller confirmed a good establishment of the RAIF because it is governed by the AIFMD therefore its shares or units can be marketed within the EEA on a cross-border basis by only notifying regulators. Furthermore, it is expected that investors from abroad acknowledge the level of investor protection. The roadshows that ALFI performs on a regular basis, in order to communicate innovations and changes to potential fund initiators and investors worldwide, shall also contribute to the acceptance. S. Weismüller pointed out that the acceptance of Luxembourg products by managers and investors domiciled in other countries is really impressive.

S. Weismüller further noted that it is up to the managers, as well as the investors, to opt for their favored level of regulation and protection also in terms of unregulated

products, like the LP whose success contributed to the fast implementation of the RAIF Law. With a focus on the further development, S. Weismüller predicts a positive development and compared the potential of the RAIF with the development of the LPs raising numbers. Furthermore, the gained positive feedback and the rising interest in the RAIF during the roadshows worldwide undermines this prediction. In terms of threats, S. Weismüller referenced the EU Law and outlined that the RAIF is compliant with AIFMD therefore and, after similar experiences gained from the SIF and SICAR acceptance, no threats are expected.

Luxembourg as domicile for the RAIF, S. Weismüller distinguished that especially this leading fund center is the place of choice for offering AIF structures and referred to the related advantages Luxembourg offers as fund domicile. In terms of acceptance in other countries and the gold plating problem, S: Weismüller outlined that due to AIFMD other EU countries do not have the possibility to refuse the RAIF. The issue of gold plating a review of AIFMD shall address this issue, for the RAIF no specific feature should cause this problematic.

5.2.5. Summary of the interview V

The fifth interview²⁴⁹ was conducted on February 08th, 2017 with Kai Braun from Ernst & Young in Luxembourg in his role as Advisory Partner. Six questions from the questionnaire were addressed during the interview and aimed to derive information related to K. Braun's experience in advising AIF providers related to alternative investments. The questions have been selected according to K. Braun's professional expertise and aiming to address the following: potentials of the RAIF in the AIF Market compared to other vehicles, the cross-border contribution and marketing, the impact of the new draft Law related to SIF/SICAR and its meaning for the RAIF as well as its expected acceptance of other EU countries from a tax/fiscal perspective.

K. Braun is well experienced as Advisory Partner with special focus on advising the related service providers such as Fund Managers, Depositories, Administrators, and Distributors. He has further experience in the setup of AIFMs and embedding

²⁴⁹ Cf. Annex, Interview V.

depositories into the AIFMD. Not involved in the direct legal part of a RAIF setup, K. Braun is helping AIFMs including RAIFs in new and current structures.

In terms of the Luxembourg AIF Market and the potentials for Luxembourg investors, K. Braun compared the situation to two worlds. On the one hand the regulated world, on the other hand the unregulated world. K. Braun pointed out, the SIF being a regulated product which is very well-known by institutional investors and the SICAR being a special vehicle that needs a specific purpose of private equity or types of venture capital investment related to risk capital. For both products investors do not need to perform a regulatory Due Diligence to invest in. The RAIF as vehicle falls into the unregulated world, but other than that is a simple copy of the SIF. K. Braun highlighted that its advantage is clearly the time-to-market aspect and the absence of product regulation. In K. Braun's view there will be a number of especially German investors that will still prefer the direct supervision to the indirect regulation through the AIFM. Nevertheless, according to an informal statistic of K. Braun, around 30% of all RAIFs that have been setup are originated in Germany. A very positive feedback especially because the German market was identified as critical for the RAIF.

In terms of cross border distribution and marketing K. Braun explained that a feedback is not yet possible because the RAIF product is still too new. The fact that a product must be known in the relevant markets and by investors, being also the main aspect for a good cross-border product, was highlighted by K. Braun. In the case of the RAIF, which is still very new, it is hard to predict if it is going to be a success or not, but so far the number of RAIFs that have already been setup show that it is a good product and has been adopted quickly by the market.

The next step, according to K. Braun, would be to put the RAIF on a global display because it is already well adopted in Europe, whereas on a global level, especially in Asia, there is still a need to raise awareness to the RAIF structure through marketing campaigns. In K. Braun's opinion, the RAIF is a very good vehicle to supplement the Luxembourg fund tool-box.

Taking the draft Law related to the SIF/SICAR that has been deposited before the Parliament on January 18th, 2016 into consideration and assuming that the RAIF will be further used as type of fund for especially exotic investments, K. Braun pointed out, that the RAIF will be much more scrutinized by all the players involved in the

setup of a RAIF. Especially, the third party AIFM will have to check what is stated in the prospectus because there is no second regulatory layer and the AIFM knows that the CSSF is not looking into it.

K. Braun predicted that the RAIF might have potential to reduce the time-to market by a third, from three months to one month. Compared to the one week that was initially mentioned for the RAIF, being still a longer timeframe as expected, due to that fact that a Due Diligence will not be finished within one week, this is still an acceptable timeframe. The Due Diligence will also include a review of the investments with special regards to exotic assets.

With the focus on the acceptance in other European countries, K. Braun added that in parallel to the RAIF is introduction a number of countries planned to do similar things. The concept of having an unregulated vehicle underneath an AIFM is according to K. Braun a valid and good concept that has been discussed as well in Malta and Ireland. In terms of taxation K. Braun believes in the Luxembourg model and added that the RAIF is compliant with BEPS and the European tax regimes. In this aspect K. Braun did not expect any issues from other countries rather believed that other countries will try to have similar vehicles as well.

5.3. Interim result of the empirical analysis

The aim of the empirical analysis was to gather aspects and practical insights related to the experience of the different interview partners with connection to the AIF Industry. With regards to the research questions different statements have been collected and were introduced in the interview summaries.

As a conclusion, it can be stated that all interview partners were well chosen because they already gained expertise in the setup of or in the dealing with the new structure. Therefore, different aspects and views on the RAIF occurred that have been already pointed out in the theoretical part of this thesis, other new aspects rose up during the interviews and completing the picture of the RAIF.

The interviews summaries show several similarities as well as differences that need to be worked out. In general, the view on the gains of the RAIF compared to other AIF vehicles in Luxembourg were presented consistently. It was pointed out from

nearly all interview partners that the benefits are a faster time-to-market, the absence of the CSSF regulation and approval processes, aligned with costs saving aspects and the fact that the RAIF can opt for an umbrella structure. Furthermore the RAIF can be set up in forms that are normally not accessible for unregulated vehicles like the SICAV in entity form of SA, SARL or SCA, which have an impact on the taxation and the access to the Luxembourg DTTs.

Compared to the other AIFs available in Luxembourg the SIF, the SICAR, and UCI covered by Part II of the Law of 2010, the RAIF can be seen as required supplement to complete a broad offering that fulfills all requirements of initiators, managers and well-informed investors.

Interlinked with AIFMD the advantage of the RAIF is not being subject to the CSSF approval, although investor protection is ensured by its obligation to appoint an authorized external AIFM and a depositary subject to responsibilities. The AIFM ensures the cross-border marketing and the access to the AIFMD passport.

For Luxembourg the RAIF offers a new potential to be regarded as competence center of choice offering a new vehicle covering needs and having potential to be a new recognized brand compared to the SIF. The condition for success is that well-informed investors in Europe as well as globally have been informed about the functionalities of the RAIF.

The RAIF can be set up to meet investor's needs and it offers unlimited investment possibilities. Meaning, the RAIF represents a perfect tool for managers to offer a broad choice investors from different backgrounds and countries. This may especially be an advantage for wealthy families or the billionaires of the world. Also in terms of re-domiciliation the RAIF offers similar structuring flexibility in an onshore location as an offshore structure, but in addition provides investor protection and a minimum of regulation.

In terms of strategic orientation of the Luxembourg market the RAIF might also have potential to enlarge the focus on the AIF strategy aspect. During the interviews many aspects showed potential for growth once the RAIF is commonly known. Taking this offering into consideration, Luxembourg offers a wide ranged toolbox of fund vehicles and investment solutions with the ability to meet all interests requested from initiators and investors.

With the focus on other European markets the RAIF may be subject to scrutiny by other countries of its tax status, currently no issues were detected and it is expected that the RAIF will be accepted by all European countries, based on its compliance with the EU Law. Furthermore, Luxembourg offers great competitive advantages by several aspects of the fund industry. In order to ensure these, further communication and marketing activities for the RAIF especially in the targeted markets, like Asia, have to be performed. Especially the possibility of non-EU managers to structure products for European investors needs to be pointed out.

Particular challenges have to be addressed. These are: marketing activities, a better penetration of the US market and related hedge fund managers, and driving forward the advertising campaigns performed by Luxembourg for Finance, the ABBL and the ALFI. There is still need for further activities to establish the RAIF in Europe. For the time being, a lot of advisory and explanation is needed to convince investors of a setup in form of a RAIF.

6. Conclusion

The overall objective of this thesis is to point out the opportunities that the RAIF provides for the AIF Market in Luxembourg in line with the topic “RAIF – Reserved Alternative Investment Fund – The impact on the Luxembourg Fund Market and the Alternative Investment Fund landscape” and the research questions aligned to this research task.

Considering the theoretical part, the SWOT analysis of the strategical direction of the Luxembourg AIF Market and the practical insights derived from the empirical analysis it can be concluded that the introduction of the RAIF is a brilliant innovation for the AIF Market in order to foster further the growth of the AIF Industry.

The RAIF is perfectly integrated in the EU regulation and the Luxembourg Laws and therefore offers flexibility and potential that have been requested from several groups’ being part of the AIF Industry. Linked to AIFMD and managed by an AIFM the RAIF can avoid the double layer of regulation and therefore profit from a faster approval process, lower regulation requirements and offers cost efficiencies. In parallel, this unregulated structure must be linked with an authorized AIFM, to ensure

the compliance with the regulatory requirements of the AIFMD, e.g. the appointment of a depository, in order to guarantee investor protection.

Based on the above the RAIF is an innovative expansion of the AIF product range and offers by its new features new dimensions for eligible investors and initiators worldwide. Linked to its domicile in Luxembourg the RAIF can profit from several aspects that Luxembourg offers in line with the introduced market advantages in chapter 4 Strategic direction of the Luxembourg AIF Market.

Furthermore, these advantages have an impact on the market attractiveness of the AIF Industry which also profits from these demographic as well as geographic aspects. In line with the above, the AIF Market is in a good position to further boost up the AIF Industry and enlarge the potential of the AIFs comparable to the UCITS flagship in Luxembourg.

The development of the RAIF is a clear statement for Luxembourg being an innovative, research focused and highly educated industry with lots of potential. This is clearly a sign for future development and the possibility to attract further investors and initiators for setting up in Luxembourg domiciled investment solutions.

Added together, the outcome of this research showed a possible impact to further turn the strategic direction of the Luxembourg Fund Market in the direction of AIFs. An aim that is still attractive not achievable without overcoming some obstructions.

Especially, markets like Asia and the Middle East have been identified as attractive target markets, not only by the ALFI. To reach those investors and potential initiators communication and enlightenment has to be undertaken, in order to make aware of the new structure available in Luxembourg. Currently, there have been several activities identified in the related countries and this demonstrates a good development. Yet, in comparison to the interview results, it was mentioned that there are still lots of potential investors and initiators, also in the EU, that are not yet aware of the RAIF. This is still an obstacle that needs to be considered by the market players.

Furthermore, in order to ensure its advanced position as a center of choice for initiators, managers and investors, Luxembourg needs to further develop and strengthen areas of innovation, research and talent development as basis for the future setup of new innovative structures and ideas in relation to the AIF Market and

its industry. The RAIF is an example showing the good collaboration of different players from the fund industry fostering a joint aim by combining the efforts.

In my opinion all the necessary actions have already been triggered or are currently addressed in order to solve the existing, above mentioned, issues. But, the scope of such activities needs time and therefore I expect that the RAIF has potential to further increase the AuM in the AIF Industry and also opens other aspects to invest in alternative strategies within the next couple of years.

For Luxembourg it is especially important to achieve a fast growth of AuM administrated by RAIF structures and to increase the number of incorporations. Once the RAIF is well known, it can act as the next brand of the Luxembourg AIF sector. Other countries offering already similar products and there is a high demand for this products. Therefore, Luxembourg needs to act fast ensuring its competitiveness against outer countries.

Another important aspect is the aim to foster the distribution of the RAIFs in all European markets and to be compliant with regulations, laws and to regulatory processes in order to rise market attractiveness as well as to lower the risks currently associated with the RAIF. All regulations put in place are part of a greater European, if not worldwide regulatory system to avoid the next finical crisis caused by unregulated and uncontrollable finance and investment instrument and markets. What also needs to be considered is the raising demand for alternative investment. A need that has to be covered by suitable investment opportunities. Consequently, more and more financial products/assets have to be offered/developed to meet the growing demand. This is a similar situation that has led to a serious failure known as the financial crisis. With the effects caused by this crisis, Europe is still struggling with.

It needs to be considered that within Europe a lot of capital is already allocated into financial instruments. To encourage investors/initiators to opt for a new product is difficult. Therefore, it is hard to convince them for a change in investment products. This is another reason to ensure the fast awareness for the RAIF in order to convince the reallocation of assets to Europe and/or to absorb the raising investments from fast growing regions like Asia.

ANNEX

Interview I – Hermann Kranz (UBS Europe SE, Luxembourg Branch)

The interview was conducted on January 20th, 2017 between Mr. Hermann Kranz from UBS Europe SE, Luxembourg Branch as Head of Asset Servicing EMEA for the Asset Servicing Business in Luxembourg and the interviewer Mr. Patrick Sprenger for his MBA-Thesis. The interviewer thanks Mr. Kranz for the possibility to perform this interview.

**Interviewer: “Please describe yourself and your role within your company.”
(Q1)**

Mr. Kranz: “I have been working for UBS for more than 23 years, of which I spent 23 in Luxembourg. I started as a system programmer in IT, then led the IT and I took over the role of coordinator of the strategic project portfolio in CMU. After that, I went to the Netherlands and built up the UBS subsidiary together with my Dutch colleagues. Returning to Luxembourg I took the role of the CAO, which was a combination of branch oversight manager and the CFO for the banks that we were operating. In 2010 it turned out that the head of the Ultra High Net Worth (UHNW) clients decided to leave the Bank. I took over this department because I partly knew the customers from there. We realized very quickly, that this part could be split up or should be divided up due to the specializations in regards to Real Ultra and Beneficial Owner Business and the Structure Business. At that time Hugues Delcourt, who is now the CEO of BIL, joined UBS in Luxembourg. We split up the business and I took over the fund structuring and he took over the end clients. Today, the classical Ultra Business is managed by Ariste Chiabotti, while I drive forward the Asset Servicing department. Asset Servicing is operating globally, together with colleagues from Switzerland, Hong Kong and Singapore, with different activities in the home countries. In Luxembourg the main focus of Asset Servicing is set on the Undertakings for Collective Investments in Transferable Securities (UCITS) funds, Specialized Investment funds (SIFs) and now new so-called RAIFs, while in Switzerland Global Custody and Risk Analytics is the key business. In Asia the main focus is on Securities Lending from UBS Investment Bank and the sale of risk reporting. The target for 2010 was to generate EURm 40 more in revenues and to acquire Net New Assets, or Net New Money (NNM) worth EURbn 10. We reached

the target on the NNM after 18 months of a 5-year plan and the expected additional revenues were reached within only 3.5 years. Nevertheless, we purposefully continued to proceed working on our revenues and in 2016 a surplus on the business plan of 14-15% was achieved. Taking these different factors into consideration, we received the instruction to develop a strategy to double the profit before tax within 5 years. We plan to exceed expectations year on year with the ambition to grow 15% per year. This can only be achieved if the product range of the Luxembourg fund market is covered as far as possible. Luxembourg has also set up a growth plan which is similar aggressive and the last 2 years have shown that this plan can be exceeded and that we only have to grow with the market speed to reach our growth target.”

Interviewer: “Have you been involved in any projects regarding RAIF structures or any similar like SIF, SICAR, UCI, etc.)?” (Q2)

Mr. Kranz: “At this end, we are preparing to serve customers from different segments such as Ultra High Net Worth (UHNW), Financial Intermediary (FIM), Global Family Office (GFO), Third Party Funds and UBS funds in order to serve them with Alternative Investment Funds, i.e. the classical SIF structuring and from now on the new RAIF structure in addition to the wide range of UCITS and other undertakings for collective investment (UCI) - in the meaning of Part II funds. The UCIs still exist but play only a subordinated smaller role for AS in Luxembourg. There are very few UCIs under custody of UBS in Luxembourg which make up less than 4% of the overall AS asset volume which is more than CHFbn 160. What has been seen in the past is that in 2010 we still had many structures in offshore locations that we gradually took back to Luxembourg. We see a very clear trend, among investors as well as promoters of funds, that they take out funds of the offshore structures and transfer them to regulated onshore structures in Luxembourg. They can be distributed because there is hardly no more demand for an offshore structure in Europe unless it has a very special investment purpose. But in principle we see that the large families tend to be more inclined to the regulated structures.”

Interviewer: “Do you think it is an advantage to have less supervision through the CSSF compared to a SIF or other well-known fund structures in Luxembourg? (Q3)

Mr. Kranz: “This growth in the number of funds has led to a slowdown of the approval process. The industry needs a much faster approval process, especially with the focus on Ireland where a regulatory process enables launches of funds within 4 weeks, while in Luxembourg as of now 3-4 months have to be taken into consideration. There are two approaches existing that can solve this issue and we pursue both. One is the straight-through process with the CSSF. We have agreed with the CSSF that we are creating standard documents, being already the approach today in Spain, Germany and in Switzerland. Only a few paragraphs, such as the Investment Guidelines, the Fund Name and the Initiator or Promoter are to be changed. The rest of the prospectus, the CBA (Custodian Bank Agreement) and the CAA (Central Admin Agreement) remain unchanged. This means that the administrator at the CSSF has only to evaluate 4-5 pages to make the decision on the fund’s approval. This is one way for increasing the efficiency and shortening the approval process to about 4 weeks for a SIF or a UCITS. The second approach to solve this time issue is the RAIF. The CSSF has delegated the approval processes to the Management Company (ManCo), which of course adds more responsibility to the ManCo. The ManCo must ensure as an AIFM that all providers are compliant with AIFMD, but it allows – quoting a consultant: “that the setup of a RAIF should be possible in the best case in 3 days, if everything runs smoothly.” Our experience showed that we probably need about 4 weeks. We launched our first RAIF a few days ago. This was the showcase, but we believe and we are quite comfortable to get the RAIF through the approval processes in the bank and also through the registration in four weeks.”

Interviewer: “What are the advantages of the new structure RAIF? Do you see any threats for RAIFs and do you think that other European countries will accept this structure? (Q4)

Mr. Kranz: “The question I asked myself on the first day when the RAIF was introduced, which probably many have asked themselves, was if the RAIF is really comparable to the SIF in regards to investment restriction. Depending on the way, it can mirror 1:1 a SIF, or even a SICAR if incorporated in the legal form of a SICAR.

In addition, the RAIF makes it possible to hold less investments and thus allows less portfolio lines which one cannot create with the normal SIF. This is a degree of freedom that certain investors want to take and have always asked for. The next question, thus also being a main issue: certain countries may question the tax status of the RAIF. This could also not be predicted at the beginning of the SIF structure. About the UCITS, being a relatively old or in financial terms ancient product, we know how the single tax authorities in different countries treat that product. There are by example small differences, e.g. between the handling of a Luxembourg Fund in Luxembourg or e.g. in Spain. As an example I need to mention the number of investors to invest to make a switch tax free or the number of investors needed to change the portfolio allocation without creating a liquidity event. In one case we are talking about 100 investors, while in the other 512 are required. After that it took a while and the SIF was introduced to the market. Then there were countries which have not accepted the SIF, e.g. Spain. The SIF is still not accepted there today with regard to its taxation handling compared to a UCITS, it also took a long time to know whether the Italians accept it from that perspective. In Germany it has been accepted and the same we expect for the RAIF. In the different countries we may see a non-acceptance from a fiscal view. We do not know yet because there are still no showcases available. I think we will learn in the course of the next 2 years, when the first customers had their annual closing and have tried to get the RAIF through a tax audit. At this point, we will receive feedback how the tax auditor will react. We are currently in discussion with 2 of the Big-Four's and we all share the opinion that it should work from a fiscal point of view. The main point of concern is that each country can make a “gold-plating” when implementing new regulations and how to classify a RAIF and how to recognize it. While it is clear for Luxembourg: When I live in Luxembourg and invest in a RAIF, then I know exactly how this vehicle is handled from a tax perspective, exactly like a SIF today. From the AIFMD legal framework perspective, which the RAIF is subject to, it is 1:1 comparable with the SIF and the obligations of any party are also identical.”

Interviewer: “Is the RAIF a good cross-border investment vehicle and well placed from a marketing perspective?” (Q5)

Mr. Kranz: “The legal distribution possibilities are the same, so you can easily register the RAIF with the Luxembourg EU Passport in other countries for distribution and distribute it there. But one will have to see whether the tax deductibility then works.”

Interviewer: “How do typical investments of RAIFs look like?” (Q6)

Mr. Kranz: “There are several reasons why clients, in addition to the fiscal aspects, are investing into such a fund structure, e.g. succession rules. Families that have arrived in the 2nd generation have to manage the assets of their parents or grandparents, which can be relatively complex. If they want to allocate the parents' assets e.g. to the 3rd generation, it is very difficult to divide the company's participations into small pieces. This is why they have the tendency to place them into a SIF or RAIF and then simply allocate the units of the structure. This is a usage where you do not just look at the tax efficiency, it is one criteria, but not the main decision criteria. The main decision criteria are that you have a robust platform where you can invest these assets. By using different managers you are able to control risks taken by the manager and the performance he generates. It is then relatively easy to exchange the assets between the family members by returning or buying units. In this regard the RAIF should be 1:1 equivalent to the UCITS or the SIF to strict investment of rules, degree of freedom offered by the RAIF in terms of investments, compared to the SIF, especially in the field of cluster risk formation. In Ireland, nearly in parallel, the new fund structure RIAIF was introduced, clearly with the idea to gain back market share from Luxembourg. Now also from customers who came to Luxembourg because we have the RAIF. This is caused by the development of the QIF and the PIF, being the counterpart of the SIF, which have decreased in demand in comparison to the RAIF. I believe, however, that Luxembourg is still ahead, since we have the more robust environment and because the Assets under Management (AuM) are tremendously bigger in size compared to the Irish ones. We should not be afraid that Ireland is trying to catch up. But also the number of Double Tax Treaties (DTT) has to be taken into consideration. Another question is if the European clients, all of sudden, prefer the Irish funds to all the other European ones. This has not been the case in the past. In the past it was fact that each country had its own fund structures within Europe which has always stayed the same, Luxembourg have lead always the biggest stake. Luxembourg is the second largest fund market in the world and by far the biggest one in Europe.

Interviewer: “Regarding the allocation of Assets under Management of AIFs: Especially Germany has a bigger market share than Luxembourg. How can Luxembourg position itself even better in the AIF Market or how is the outlook for Luxembourg in the AIF Market especially in regards to an European perspective and the competition in the EU or even globally when regarding the Cayman Fund structures. Maybe there is also room for the RAIF?” (Q7)

Mr. Kranz: “The German AuM are currently higher because Germany has the biggest European domestic market. I only know a very few cases, or hardly any at all, where a person not living in Germany has a German investment fund in his portfolio. Usually, these are Luxembourg Funds or funds incorporated in the home country of the investors. I think that Luxembourg has to increase the marketing activity. Germany is the biggest economy in the EU, which provides a location advantage not related to the funds. I think that if Luxembourg grows further, the RAIF will grow along with the market or the alternative investments. In the past one disadvantage, being the reason for Ireland doing so well, was that many Hedge-Fund Managers invested in AIFs. These are usually U.S. based and prefer the Irish or the UK environment due to the language compatibility and the time zone which is closer to US time as Luxembourg time. These were the reasons named that we have lost cases. There is an affinity from US Hedge Funds Managers to invest into a SIF and they tend to UK or Ireland based providers or structures because they can be distributed similarly in Europe as a Luxembourg structure. What we have achieved in the last couple of years is that we have added clients from Latin America, Asia and the Middle-East as target groups and even in the meanwhile onboard more and more of these clients. These client groups do not care or pay attention if their assets are booked and administrated in Luxembourg or Ireland. In this case the attractiveness of the Luxembourg Banking Sector as a location advantage plays a great role. There is nowhere else in Europe this concentration of consultants, Tax Specialists, Tax Lawyers, Administrators and Custodians.

Interviewer: “Do you think that RAIF structures can bring added value to the investors in and outside of Luxembourg?” (Q8)

Mr. Kranz: “With regard to the global rollout, I have already answered that question partially. We have observed that a lot of big and wealthy families, the billionaires of this world, leave the offshore structures and invest in regulated tax transparent

onshore structures. What we have to achieve, and Luxembourg is already fostering this with visits in those countries, from Luxembourg for Finance and from the ABBL and the ALFI, that the Luxembourg products are becoming better known there. We have observed when we visited Asia, that e.g. the Lawyer Community in Hong Kong is mainly and still focusing on Cayman Structures. We had to convince our people to also accept other structures than Cayman Structures. We learnt that some more educational work on the Luxembourg Investment Structures has to be done there. Once the differences were understood it was acknowledged that there was the readiness to invest into Luxembourg Funds, for accumulating their assets, even though they are more expensive than Cayman Funds.”

**Interviewer: “What do you think about Luxembourg as domicile for RAIFs?”
(Q9)**

Mr. Kranz: “Absolutely, the RAIF is the answer to the extremely slowed down approval process. In my opinion the RAIF will catch up with the speed of setting up AIFMs within the next two years. The UCITS will stay flagships of the Luxembourg fund sector. At the moment the asset allocation is 70/30 in favor of the classical UCITS in our client population and the booked assets.

Interviewer: “Thank you very much for the Interview.”

Mr. Kranz: “You are welcome.”

Interview II – Christopher Dortschy (Allen & Overy, Luxembourg)

The interview was conducted on January 23rd, 2017 between Mr. Christopher Dortschy from Allen & Overy in Luxembourg and the interviewer Mr. Patrick Sprenger for his MBA-Thesis. The interviewer thanks Mr. Dortschy for the possibility to perform this interview.

Interviewer: “Please describe yourself and your role within your company Allen & Overy” (Q1)

Mr. Dortschy: “My name is Christopher Dortschy. I am a German national living in Luxembourg for almost ten years and practicing Investment Fund Law since 2010. I am currently a counsel in the Investment Funds Department here at Allen & Overy primarily dealing with the structuring of Luxembourg Investment Vehicles. When I say investment vehicles I would say that in the broader sense. Everything that works like a fund – be it commitment/drawdown approach or similar aspects of funds that are advised by us. That does not necessarily mean that it must qualify as an Undertaking for Collective Investments in Transferable Securities (UCITS) or it must qualify as an Alternative Investment Fund (AIF), but it should qualify as a fund in a broader sense. The investment funds practice in general is of course busy with the setup of UCITS and AIFs. AIFs in the meaning of regulated AIFs and unregulated funds. Also, we are advising Alternative Investment Fund Managers (AIFM) and Management Companies (ManCo) on specific aspects such as granting or obtaining their licenses or the extension of their licenses as well as the review of their policies and procedures. We also advise Limited Partners (LP) and other investors of Luxembourg fund structures and carry out the due diligences, to name just some examples. All this is frameworked by the corporate aspect and we advise our clients on that as well.”

Interviewer: “Have you already been involved in structuring or the setup of a RAIF and compared to that what was the advantage especially regarded this structure?” (Q2)

Mr. Dortschy: “Yes, but I must admit, I have not gone through a whole project yet. I haven’t come to that “brilliant” part of the incorporation which is generally comparable to the incorporation of the most popular structure of the last years, being unregulated Limited Partnership (SCS) or a Special Limited Partnership (SCSp) qualifying as an

AIF, and then probably with a full scope manager. But, the process for a RAIF is bit more complicated. You need, even if you are constituting under private seal, a notary confirmation. Furthermore, there is this strange provision in the law – I do not know if you have seen that already – that only permits you to collect money from investors as of the moment the letter confirming the incorporation of the RAIF has been sent to the Registre de Commerce et des Sociétés (RSCL). This is as I believe a drafting error, a copy/paste from the SIF Law which does not really make sense in the RAIF context. Well, I think that these are just elements which we have to go through in the beginning. We have to get used to them and then afterwards we can implement these steps in our internal checklists. Then we go through these and things will not be that difficult anymore. But, there were certain uncertainties in the beginning of the very first RAIFs which still need to be handled in a proper way.”

Interviewer: “In regards to favorable structures here in Luxembourg for the Alternative Investment Fund market do you see a potential that RAIFs provide better possibilities for the investors within Luxembourg or within the EU?” (Q3)

Mr. Dortschy: “There are certainly strong arguments for a RAIF. But, I am not sure if I am that thrilled about it, or so convinced that we are actually needed it, to be honest. The first point that nearly everybody points out when being asked what makes a RAIF more attractive in comparison to an SCS or a SCSp is of course the Umbrella Structure. In my view there are already certain ways that exist to artificially or synthetically create an Umbrella Structure, e.g. take one general partner and you could create several SCS or SCSp, all managed by the same general partner. In my view you have exactly the same result as an Umbrella Structure or maybe even better because you actually have your assets in different partnerships. Who knows if an Umbrella Structure is recognized all over the world, it has never been tested so far. I think that the Umbrella Structure argument is maybe a bit more a window dressing argument and might be also more cost efficient on the service provider side. Potential initiators are maybe more familiar with the treatment of an Umbrella Structure but maybe not be so used to treat a general partners platform with several SCS/SCSp and see them actually as compartments of an Umbrella Structure. I think – as I said, I am not that entirely convinced about that – an Umbrella Structure is really a big win for the RAIF – at least from a selling point of view. What in my personal view is a much more important point is a more the technical detail: It is the ability of now being able to use so called “tax blockers” like the Public Limited Company (SA), the Limited

liability company (SARL) or the Partnership limited by shares (SCA). These corporate structures, until now rarely used to structure unregulated AIFs, can now be effectively put into the tax framework of either the SIF or SICAR via the RAIF route. I think that is probably the most important point of the whole new RAIF legislation, because you will have structures where certain investors would prefer tax opaque investment vehicles, whereas others prefer a transparent solution. SCS or SCSp are not appropriate for each and every type of structure or investor. If you, as the initiator, or your investors like the idea of having a limited partnership they can from now on also opt for an SCA if it better serves the purpose. This legal structure has also been reformed, there have been some weaknesses in the Law before 2013, now it is more similar in the way it functions to the SCS/SCSp. Structuring a RAIF as an SCA might give you direct access to certain Double Tax Treaties (DTT). This is something which was not possible for AIFs in the form of an SCS/SCSp.”

Interviewer: “You mean On the SICAV side?” (Q4)

Mr. Dortschy: “Yes, I am referring to a RAIF-SICAV in the form of an SCA, whereas a SCS or a SCSp – I am not a tax lawyer – but in my view they will never have access. If they want to have access to DTTs they will always need put an entity with access rights (SA/SARL/SCA) underneath. These are the so called “investment holding companies” or “Master HoldCos”. From a substance perspective this is not ideal. Prior to the enactment of the RAIF law, I received a comment from my Italian tax colleagues in a specific case that they preferred an SCA structure over an SCS/SCSp structure – fully acknowledging that as an unregulated structure the SCA would be much more cumbersome and difficult to handle (fixed capital, unitized shares, stricter corporate governance). But the point was that this SCA will have direct access to the Luxembourg-Italian DTT and would be the entity being looked at from an Italian substance perspective, meaning you would be able to concentrate all substance at the level of the general partner of the SCA and there would be no need for an additional investment holding company having its own directors and other substance. From my personal view this is probably the core aspect for the RAIF to become successful; especially with BEPS, where tax structures will be under specific scrutiny.

Another important point is – but that is maybe more in theory – that the RAIF regime might result in a renaissance for the SICAR. The SICAR has been – un-technically

spoken – “killed” by the CSSF over the last years with a very cumbersome authorization procedure, whereas the basic idea of the SICAR from a tax point of view is quite interesting: Having a fully taxable entity which receives a special tax treatment because of its very specific investment strategy and therefore permitted to deduct its entire investment income from its taxable base. In the form of a RAIF, incorporated as an SCA for instance, it might be that this is really going to be a successful vehicle.”

Interviewer: “...a perfect structured combination you can say?” (Q5)

Mr. Dortschy: “Yes, without the CSSF procedure you do not have to discuss any longer problems which you – as the initiator – consider to be minor. Please bear in mind however, that an auditor statement will be required confirming that the RAIF qualifies for the SICAR treatment.”

Interviewer: “Related to the cross-border distribution of the RAIF, is there ideally something which is already known or if – maybe – other countries will accept the forms of a RAIF from a tax/fiscal perspective and how it will be treated?” (Q6)

Mr. Dortschy: “Related to the passport-process itself, it is the same as we have for every AIF. It is in fact very similar to the process of unregulated AIFs in the form of an SCS/SCSp. The AIFM of the RAIF has to announce to the CSSF that it is the manager of the RAIF. It transmits certain information to the CSSF which includes inter alia the issue document or PPM as well as the limited partnership agreement/articles of incorporation of the RAIF. The CSSF then issues a V-number to the AIFM with which it can start passporting the RAIF. From the perspective of the other Member States, i.e. the Member States into which the RAIF is passported, I think it is a bit too early to say how it is going to be perceived by the regulator and how it is going to be perceived by foreign tax authorities. In terms of the latter, my guess is that it will probably be seen as either, a SIF or a SICAR, depending on which tax regime it opts for – but that’s just a guess of course. Our tax team is currently assessing the access rights of RAIFs to the DTTs. The last circular related to DTTs in this respect has been issued before the Law was enacted and mentioned e.g. SIFs and SICAV-SIFs but it does not mention of course SICAV-RAIFs. But in my opinion it would not be very logical if they would be treated in a different way.”

Interviewer: “If we look into the future, were do you see potentials for the RAIF in regards to the AIF Market here in Luxembourg, especially from a perspective of strategic orientation within Europe and maybe even global –is there a difference on marketing Luxembourg AIFs and to really expand the Luxembourg AIF Business? (Q7)

Mr. Dortschy: “Related to the advantages and what I didn’t mentioned before is the brand. I think it is a very soft factor but I think we cannot underestimate how much it will be worth in a couple of years when sophisticated investors in Europe or even worldwide will understand what a RAIF actually stands for, compared to the SIF or maybe even in a more smaller scale for the SICAR. My main issue in advising clients nowadays is to introduce them to the whole Luxembourg structuring toolbox and to point out the differences in the different regulations, structures and legal forms as well as the Laws applicable. Only to explain to a client what an SCS/SCSp qualifying as an AIF with a full scope manager is and why there might be dependencies of appointing a depository, an auditor, the marketing related to the EU passport and EU access, to mention just a piece of the whole structuring discussions, is very difficult to understand for the client and time consuming for myself. My expectation and my hopes are that in a couple of years, whenever I mention the RAIF to a client or an investor, he or she will have a general idea and see it in a positive way, comparable to what the SIF stands for today - even if it will probably not mean that the client will have fully understood all detailed aspects. If you now go to smaller pension Funds like the German “Versorgungswerke”, they still want a SIF because they know what it is. Probably they would be interested in a RAIF structure but, depending on their governance and approval procedures for the time being they do not have approved these structures internally. As they have to go through their committees and a SIF is already well known an unregulated SCSp or a RAIF will be difficult to introduce. Once all these slower moving investors have adapted their internal procedures and the RAIF is better known, I think then it will be a selling argument for Luxembourg.”

Interviewer: “So all in all it can be said that the RAIF is an advantage for Luxembourg and for promoting the Alternative Investment Fund market here within Europe and perhaps also globally?” (Q8)

Mr. Dortschy: “Yes, probably.”

Interviewer: “Many thanks for the interview, these were very detailed insights.”

Mr. Dortschy: “You are welcome.”

Interview III – Jendrik Fuhrmann (Hauck & Aufhäuser, Luxembourg)

The interview was conducted on January 24th, 2017 between Mr. Jendrik Fuhrmann from Hauck & Aufhäuser Alternative Investment Services S.A. in Luxembourg and Mr. Patrick Sprenger as the interviewer for his MBA-Thesis. The interviewer thanks Mr. Fuhrmann for the possibility to perform this interview.

Interviewer: “Please describe yourself and your role within your company Hauck & Aufhäuser Alternative Investment Services S.A.” (Q1)

Mr. Fuhrmann: “My name is Jendrik Fuhrmann from Hauck & Aufhäuser in Luxembourg. Our company is acting in the field of investment funds, focusing on Undertakings for Collective Investments in Transferable Securities (UCITS) as well as Alternative Investment Funds (AIF). In addition we setup and administrate Securitization Vehicles within the meaning of the Law of 2004. In 2008 we setup a separate corporate entity, only dealing with AIFs. In total, most of our assets under administration are from AIFs at the moment. My task within the company is the structuring of AIFs in all forms, e.g. Specialized Investment Funds (SIF), Investment Companies in Risk Capital (SICAR), Reserved Alternative Investment Funds (RAIF) as well as any corporate structure, e.g. the Limited Partnerships (SCS), Special Limited Partnerships (SCSp), Public Limited Companies (SA) and the structuring of Securitization Vehicles.”

Interviewer: “Have you already been involved, within your projects of structuring, in the setup of a RAIF and do you have on the AIF-side favorable structures like the mentioned structures SIF, SICAR or comparable?” (Q2)

Mr. Fuhrmann: “Yes, today our favorite structure is definitely the SIF setup in the corporate form of a SCS. That is the main structure in the up to now and we recognize very often that the SIF is such a well-known instrument for our clients. It is very easy to provide them with information about the product and the investors also know this product already, so it is easy to distribute. We have to see what comes with the RAIF.

At the moment we are structuring two RAIFs. They have not been setup yet completely. We have a lot of requests for the RAIF - from new clients as well as from clients we are already administrating – in the pipeline. They are interested in the new product but partly they are also overstrained when it comes to the structuring and opting for an already known SIF product. The RAIF may cause problems for the investors, as the vehicle is not very well known and requires a separate due diligence. That is one of the reasons we still setup a lot of SIFs but we hope, once the structure is better known with the clients, there might be more requests for the setup of a RAIF.”

Interviewer: “And where do you see potential advantages especially for the investors, or in your case institutional investors and what do you think could be a typical investments of a RAIF?” (Q3)

Mr. Fuhrmann: “I think there are two main advantages: One is time-to-market because you can setup these structures very fast and without the CSSF approval process. Furthermore changes to the structure can be implemented without prior approval of the CSSF, giving more flexibility to the clients. The second one is that a RAIF does not have to bear the initial as well as yearly fees from the CSSF. These two aspects are – from my perspective – the most important ones. Additionally you might have less regulatory aspects than under the SIF Law, but – to be honest – the RAIF Law has also implemented some regulatory standard requirements that are not less than the once of the SIF Law Time to market and costs are the most important aspects. With regards to typical investments the RAIF can invest in any type of assets depending on its investment strategy. Related to the structure the RAIF can opt for investments compared to the SIF Law or to the SICAR Law, depending on the alignment to risk spreading or exclusively risk capital investments.”

Interviewer: “Do you believe the RAIF provides added value to the investors outside of Luxembourg or outside of the EU, as well?” (Q4)

Mr. Fuhrmann: “Last year we had one client who is a US-Real Estate Debt Manager. They were setting up an unregulated AIF structure with an AIFM. They already have a parallel Fund in the US and wanted to setup a similar product in the EU for European investors. The RAIF might have been interesting for them as they did not know the SIF structure very well and though did not have any preferences regarding the vehicle. This can be an advantage to promote the RAIF to non-EU managers.”

Interviewer: “Do you see potential threats for distributing the RAIF structure in Europe or even global, e.g. in Asia for Asian investors?” (Q5)

Mr. Fuhrmann: “From a global perspective, I do not know because we have only few investors that are not from Europe. We do have clients that are not from the EU but want to setup an EU product for European investors. We only have few EU products for foreign investors. Distributing the RAIF in the EU – at least at the moment – is possible and I do not see any problems currently as long as we can make use of the notification passport. At the moment no reasons exist opposing the procedure of using the notification passport and notifying the product. So for EU/EEA distribution it is good in use.”

Interviewer: “Related to the potential of the RAIF for the strategic direction of Luxembourg’s Alternative Investment Fund market: Do you see it as a potential to expand the AIF Business here in Luxembourg?” (Q6)

Mr. Fuhrmann: “There is definitely potential, but I am not sure where we are standing in two or three years. When I look back to the year 2007 when the SIF Law came into effect– and you just have to look at the specific year 2007 –an extreme number of SIFs had been setup for different reasons. We do not see this with the RAIFs at the moment. I think in the long-term it will be a commonly used product but probably not the N°1 product of choice for clients. Additionally I am not sure how the regulatory development will look like in five to ten years because the CSSF – when the AIFMD came into effect and the Law of 2013 was setup – probably did not have in mind that it would be possible to setup AIFs without product regulation of the authority. I think that was a new aspect for the CSSF. Legally this is absolutely fine but I think the CSSF did not have in mind that AIFs can be distributed in the whole EU without having approved that product before.”

Interviewer: “As initially mentioned, you are working in the structuring area. Do you see any potentials compared to Limited Partnerships setup or what do you think is the biggest advantage compared to the LP setup which is not regulated?” (Q7)

Mr. Fuhrmann: “I am not sure if we at Hauck & Aufhäuser will setup “unregulated” AIFs in the future anymore. Probably these products will fall within the scope of the RAIF Law. At least when we have an AIF managed by an external AIFM we will

probably always choose the RAIF structure. We have already seen in the past that unregulated AIFs, at least for our company, are very rarely used. With regards to corporate structures you have a wide flexibility of choosing your legal form, e.g. SA, SCS or SCSp. The corporate structure does not depend on the product chosen.”

Interviewer: “And what is your personal opinion for this new structure?” (Q8)

Mr. Fuhrmann: “I think we have a good starting point: why should you regulate in two ways, the structure itself as the product and the AIFM? It is a good question and it makes really sense to concentrate on regulating only AIFM. I think the RAIF is a good product in the toolbox of Luxembourg, but I have some doubts that it will be the new predominant structure as promoted by some market participants. At least for our primary market in the German speaking countries we cannot see a heavy trend in the moment. Some clients have doubts regarding the RAIF because the product itself has not been approved by the CSSF. Sometimes it is difficult for the clients to understand, that the AIFM is regulated, however the product is not. That is why I think we will still setup a large number of SIF vehicles complemented by some RAIF products.”

Interviewer: “I would like to thank you for the interview, and the quite impressive insights provided.”

Mr. Fuhrmann: “You are welcome, thank you very much.”

Interview IV – Susanne Weismüller (ALFI, Luxembourg)

The interview was conducted on February 2nd, 2017 between Ms. Susanne Weismüller from the ALFI (the Association of the Luxembourg Fund Industry) and Mr. Patrick Sprenger as the interviewer for his MBA-Thesis. The interviewer thanks Ms. Weismüller for the possibility to perform this interview.

**Interviewer: “Please describe yourself and your role within your company.”
(Q1)**

Ms. Weismüller: “My name is Susanne Weismüller and I work as a senior legal adviser at the Association of the Luxembourg Fund Industry (ALFI). I hold a degree in law with a specialization in European Law and Public International Law from the University of Trier, Germany. Before joining ALFI in 2008, I started work with a German law firm in Luxembourg specialized in business and tax law. At ALFI, I coordinate among other things the association’s regulation advisory board and alternative investments committee.”

Interviewer: “Do you know how many RAIF structures have already been set up in Luxembourg?”(Q2)

Ms. Weismüller: “As at 23 January 2017, 55 RAIFs (single funds or umbrella funds) have been registered with the Luxembourg Registre de Commerce et des Sociétés. From the feedback we have heard so far we can say that the Luxembourg fund industry is confident about a positive development.”

Interviewer: “Have you been involved in any projects regarding RAIF structures or any similar? (Q3)

Ms. Weismüller: “Yes, the idea of introducing a RAIF had been discussed in the alternative investment fund group of the Haut Comité de la Place Financière (HCPF), and in the HCPF itself. ALFI is represented in both committees among other market players. After its adoption, ALFI published a flyer on the RAIF. Now, it is up to the industry to make use of the RAIF structure.”

Interviewer: “What is the most favorable structure in Luxembourg and do you think that there is a potential for the RAIF or does it ‘fight’ against other AIFs (SIF, SICAR, UCI) or is it more a parallel combined world? (Q4)

Ms. Weismüller: “For me there was and is really no intention to cause a fight between the different vehicles, because it depends on many different aspects which structure you choose. But this question is difficult if not impossible to answer, because the needs/demands of alternative investment fund managers (AIFMs) and their investors are different. Accordingly, different structures are set up.

The SIF offers a flexible legal framework and lighter prudential regime appropriate for sophisticated (well-informed) investors. The SIF will continue to be successful as it gets the ‘stamp’ from the CSSF and for certain investors this is important for marketing purposes. It provides more assurance to the related investors, because it is directly supervised by the CSSF. Furthermore, traditional and exotic investments are allowed whereas only a maximum of 30% can be invested in securities of the same issuer, which can be subject to exceptions. If the SIF qualifies as alternative investment fund (AIF), it must be managed by an authorized AIFM, unless it is small in size and it must appoint a depositary. At this stage, it is worth noting that a current draft law, further to the adoption of the RAIF Law, aims at revising the scope of application of the SIF Law. Funds investing in certain exotic investments, which are difficult to value (e.g. luxury goods like watches or horses), should in the future rather be set up as RAIFs.

Then you can compare the RAIF to the SICAR which was specifically designed for private equity investments and is, like the SIF, only open to well-informed investors. As it is a specific company for private equity it invests in risk capital, and there is no particular diversification requirement. It typically offers a direct or indirect contribution to smaller entities in view of their launch (start-ups), development or listing on a stock exchange. If the SICAR qualifies as alternative investment fund (AIF), it must be managed by an authorized AIFM, unless it is small in size. SICARs must appoint a depositary. It is worth noting that a current draft law aims to further align the SICAR regime to the SIF regime.

Furthermore, non-UCITS that are not subject to a specific product law (like the SIF and SICAR Law) are considered Undertakings for Collective Investment (UCIs) established under Part II of the Law of 2010. UCI part II funds are open to

professional and retail investors. They are and will still be used because they can be marketed to retail investors, too. There is no restriction in terms of eligible assets. However, the investment objective and strategy is subject to prior approval by the CSSF. Risk diversification requirements are defined by IML Circular n° 91/75 and specific restrictions concerning funds adopting an alternative investment strategy are contained in CSSF Circular n° 02/80. If the UCI part II fund qualifies as alternative investment fund (AIF), it must be managed by an authorized AIFM, unless it is small in size.

The RAIF is the newest vehicle which has been created and certainly its major advantage is, that it does not have to be approved by the CSSF. It ensures a sufficient level of investor protection and it must be managed by an authorized external AIFM, in other words it is reserved to them. A depository which has exactly the same duties and responsibilities as provided for under the AIFMD must also be appointed. The RAIF is very much aligned to the SIF regime, with the main difference that the RAIF does not have to be approved by the Luxembourg regulator. An authorized AIFM that wants to set up a RAIF can do so quite quickly. In the beginning, it takes time for interested managers to find the right partners and to sign the contracts with the depository and the auditor, but once they have solved this task, the setting up of the RAIF structure itself can be done within 1 to 2 weeks.

During the past few years, the EU introduced new European fund vehicles (or labels), which can be chosen by alternative investment funds. ELTIFs invest in long-term assets, EuVECA funds collect venture and growth capital, and EuSEF funds are dedicated to social businesses.

All in all, Luxembourg always wants to offer a broad toolbox of fund vehicles and investment solutions; this way, it can meet the interests of both fund initiators and investors, which is really important for everyone.”

Interviewer: “What are the advantages of the new structure RAIF? (Q5)

Ms. Weismüller: “In particular, managers can benefit from a reduced time-to-market and face less cost, because the fund itself does not have to be approved by the CSSF. RAIFs can be managed and marketed on a cross-border basis and once the AIFMD passport is granted to third countries also by non-EU managers. Compared to existing non-regulated vehicles, which are governed by Luxembourg company

law, the RAIF can have a variable capital (if it takes the form of a SICAV) and be set up as an umbrella fund, with distinct share classes.”

Interviewer: “How do typical investments of RAIFs look like? (Q6)

Ms. Weismüller: “There is as such no investment restriction for the RAIF, both traditional and exotic investments are allowed. The RAIF can for example invest in private equity, real estate, hedge, infrastructure, debt acquisition and loan origination, as well as listed securities of any type or in real/tangible assets. In the absence of any detailed rules in the RAIF Law itself, the principle of risk-spreading and its interpretation in relation to SIFs should be taken into account (notably CSSF circular 2007/309). By derogation to this rule, RAIFs investing only in risk capital are not subject to the risk-spreading principle. The SICAR tax regime is in this case applicable.”

Interviewer: “Do you think that RAIF structures can bring added value to the investors in and outside of Luxembourg? (Q7)

Ms. Weismüller: “Yes, absolutely. As I said the RAIF is a flexible vehicle which can be used for traditional and exotic investments. As any other Luxembourg AIF a RAIF can be marketed to investors domiciled in and outside of Luxembourg. The investor must be a well-informed one, which means he can be an institutional investor, a professional investor or any other investor who has stated in writing that he adheres to the status of well-informed investors and:

- he invests a minimum of 125'000 euros in the RAIF; or
- he has been the subject of an assessment made by a credit institution, by an investment firm or by a management company or by an authorized AIFM, certifying his expertise, his experience and his knowledge to adequately appraise an investment in the RAIF.

Considering that fund structures are usually set up to meet investor’s needs and that the RAIF offers almost unlimited investment possibilities, the RAIF represents a perfect tool for managers to offer investors from different backgrounds and countries a broad choice.

A sufficiently high level of investor protection is ensured by the fact that RAIFs must be managed by authorized external AIFMs. The latter are obliged to fulfil their

reporting obligations towards national regulators on a regular basis, which includes reporting on RAIFs managed by such AIFMs. This means that the RAIF is still supervised, not directly but indirectly. The depositary which is appointed by the RAIF is also subject to the strict requirements set out in the AIFMD, which ensures a high level of investor protection.”

Interviewer: “You already mentioned the external AIFM: Luxembourg already identified the double layer of regulation and supervision, on the one hand for the fund/product itself and on the other hand through the AIFM the manager. Do you think it is an advantage for the RAIF compared to the SIF or the SICAR for example, that there is less supervision performed by the CSSF and for the RAIF only the AIFM is now responsible for such an instrument?” (Q7a)

Ms. Weismüller: “Fund investors and initiators should be able to choose the vehicle that meets their needs. If they would like to have a higher level of supervision by the regulator to be sure that everything is checked upfront, then they should choose the SIF or SICAR, provided these investors are sophisticated ones. Initiators which think that indirect supervision is sufficient (because reporting on funds is anyway done by the AIFM) should choose the RAIF. The second option became available following the introduction of the AIFMD, because now in the alternative space the focus is primarily on the manager and not on the vehicle. As you mentioned at the beginning, fund regulation in Europe was based for a long time only on the UCITS framework which is a product directive, and, as a consequence, all regulated fund vehicles that have been created before AIFMD were focused on fund approval. Now, we have the option to introduce alternative fund vehicles that are only indirect supervised, and which benefit from a shorter time-to-market.”

Interviewer: “Is the RAIF a good cross-border investment vehicle and well placed from a marketing perspective? (Q8)

Ms. Weismüller: “Yes. As RAIFs are reserved to authorized AIFMs, their shares or units can be marketed within the EEA on a cross-border basis, i.e. it is sufficient to notify regulators but not required to launch separate registration processes. The same would apply in case the AIFMD passport is extended at a later stage to selected third countries like e.g. Switzerland or Canada. Being a fully compliant AIFMD vehicle, it is expected that investors from abroad acknowledge the level of investor protection. Compared to non-regulated vehicles they will appreciate the

typical fund features such as the possibility to invest in different sub-funds. This is also a reason for the roadshows that we are performing on a regular basis to communicate innovations and changes to potential fund initiators and investors worldwide. The acceptance of Luxembourg products by managers and investors domiciled in other countries is really impressive.”

Interviewer: “Do you think it is an advantage to have less supervision through the CSSF compared to a SIF or other well-known fund structures in Luxembourg? (Q9)

Ms. Weismüller: “Managers and sophisticated investors should be able to choose which level of regulation and protection is sufficient. While the SICAR and SIF regimes enjoy and will continue to enjoy a widespread use amongst international investors and managers alike, it is the unparalleled success of the Luxembourg limited partnership regimes since 2013 which actually triggered the design and swift enactment of the RAIF Law.

RAIFs are indirectly supervised via their AIFMs, which have to meet regular reporting requirements. If a manager prefers for marketing purposes to get fund approval, he is free to set up a SIF, SICAR or UCI Part II fund. On the other hand, an authorized manager should be able to set up a RAIF within a short time period if he meets all the formal requirements set by the AIFMD.”

Interviewer: “How do you think will the RAIF develop within the next years (short and long-term)? (Q10)

Ms. Weismüller: “At the beginning, it takes a bit more time to negotiate contracts, but we believe that many RAIF structures will be created in the coming years. We think there will be a positive development, comparable to the one we have seen for the limited partnership regime in Luxembourg which was modified along the implementation of the AIFMD. In particular, the numbers of the new special limited partnership are very good. We think the RAIF will also be successful because it is a sufficiently well-regulated vehicle with the advantage of having a shorter time-to-market. ALFI is doing during the year numerous roadshows all over the world and we can say there is positive feedback and a lot of interest from other places in Luxembourg’s structures.”

Interviewer: “Do you see any threats for RAIFs? If yes, could you please describe them? (Q11)

Ms. Weismüller: “There are no threats for RAIFs. The vehicle being fully compliant with the AIFMD is in conformity with EU law and similar to the SIF/SICAR regime, which are well accepted. It is worth noting that the accounting information given in the annual report must be audited by an auditor. If a RAIF invests exclusively – in line with its constitutional documents – in risk capital, it is subject to the SICAR tax regime and the auditor must confirm the investment in risk capital. This also gives confirmation that the structure is in line with the law and regulations in Luxembourg.”

Interviewer: “What do you think about Luxembourg as domicile for RAIFs? (Q12)

Ms. Weismüller: “Luxembourg being Europe’s leading fund centre is the best place to offer another competitive alternative fund structure. It is a perfect domicile for setting up funds and to use it as platform for cross-border distribution, which is one of our biggest strengths. ALFI has published a brochure with the title ‘Why Luxembourg?’ which summarizes the advantages of Luxembourg as fund domicile as follows:

- Strategic location: at the heart of Europe;
- Founding member of the EU, member of all principle international organisations;
- Traditional openness towards cross-border integration, international orientation, leader in the cross-border distribution of investment funds;
- Country AAA rating;
- Sound public finances and political stability;
- High quality of living, cultural events;
- Unique concentration of investment fund experts specialised in all aspects of product development, administration and distribution;
- International and multilingual workforce;

- Highly experienced and responsive regulator, high standard of investor protection;

Luxembourg's legal and regulatory framework for investment funds is state-of-the-art, umbrella funds with several compartments and different asset classes offer tailor-made solutions. All these arguments are also applicable to the RAIF."

Interviewer: "Do you think that other European countries will accept this structure? (Q13)

Ms. Weismüller: "Qualifying as AIFs within the meaning of the AIFMD, other European countries do not have the possibility to reject RAIFs. The authorized external AIFM must ensure that the provisions of the AIFMD, as implemented into national law, are complied with. Marketing without passport (private placement) to third countries is still subject to national rules, but considering that the RAIF regime is similar to the one of SIFs and sits within the AIFMD framework, it is not expected that RAIFs are criticized by foreign regulators. We should not be in a situation where national regulators have the possibility to reject this vehicle, because it complies with the European standard as defined by the EU legislator. I do not expect any problems."

Interviewer: "For the SIF and for the SICAR there raised problems related to the fiscal acceptance in different countries related to 'gold-plating'?" (Q14)

Ms. Weismüller: "We have the issue of gold-plating still with regard to numerous aspects of the AIFMD, e.g. as far as national requirements for reporting under the AIFMD are concerned. This year's review of the AIFMD may help to overcome certain issues. But there is no specific feature in the RAIF Law which should cause issues from the perspective of foreign regulators."

Interviewer: "I would like to thank you for the interview and the interesting insights provided."

Ms. Weismüller: "You are welcome."

Interview V – Kai Braun (Ernst & Young, Luxembourg)

The interview was conducted on February 08th, 2017 between Mr. Kai Braun from Ernst & Young in Luxembourg and the interviewer Mr. Patrick Sprenger for his MBA-Thesis. The interviewer thanks Mr. Braun for the possibility to perform this interview.

Interviewer: “Please describe yourself and your role within your company Ernst & Young Luxembourg.” (Q1)

Mr. Braun: “My name is Kai Braun, I am an Advisory Partner at Ernst & Young taking care of everything that is related to Alternative Investments, meaning I am working with all sorts of Alternative Investment providers like Managers, Depositories, Administrators, Distributors, etc. With the focus on the regulatory perspective I have set up many AIFMs and I have helped many Depositories embracing the AIFMD also from an operational and IT perspective.”

Interviewer: “You mentioned that you have already set up AIFMs, have you already been involved in structuring or the setup of a RAIF structure?” (Q2)

Mr. Braun: “I am not really involved in the direct legal part of it, but I am obviously helping a number of AIFMs embracing a RAIF and to see where it suites best and how it could be set up, yes.”

Interviewer: “In regards to favorable structures here in Luxembourg for the Alternative Investment Fund market do you see a potential that RAIFs provide better possibilities for the investors within Luxembourg?” (Q3)

Mr. Braun: “If you look at the two worlds and compare the unregulated with the regulated: the regulated with the SIF or the SICAR for example, personally I think the SICAR is always a special vehicle that needs a specific purpose of Private Equity or types of Venture Capital investment related to risk capital. The SIF is broader and it is a product which is very well known by the Institutional Investors. These investors do not need to perform a regulatory Due Diligence to invest into a SIF. Now, there is the RAIF, which is an unregulated vehicle, but other than that, an exact copy-paste of the SIF Law. That sounds good in a first place. The advantage clearly lies in the time to market, since it does not need to go through the CSSF approval process and it is not supervised by the CCSF. However, there is a number of German investors who still prefer to use the regulated product, not just indirectly regulated through the

AIFM. For those, I still see the option to start off with a RAIF and convert into a SIF later on, which is obviously a smooth option. If my source of ‘informal’ statistics is correct, there are about 30% of all RAIFs that are set up, originated for German investors. That speaks to me a very positive language for this country. Especially because the German market was seen as critical for the interest in setting up vehicles in the form of a RAIF. ”

Interviewer: “This leads directly to the question of cross border contribution. Is the RAIF a good possibility for the cross border business, especially from a marketing perspective?” (Q4)

Mr. Braun: “It is difficult to say as of today, because it is still too new. What makes a good cross border product really excellent is the fact that it is known in the related markets by the typical investors, like e.g. the German Pension Funds, the UK Insurance Companies and the Swiss Insurance Companies. The RAIF is not long enough on the market in order to really say if it is going to be a success story or not. But everything that we have seen so far and the number of RAIFs that have already been set up shows that is a good product and has been really quickly adopted by the market. The next step, I think, is to put it on a global display. In Europe the RAIF is already well adopted, but on a global level, especially in Asia, there is the need to raise awareness to the RAIF structure. Additional marketing campaigns, to explain the RAIF as a product are mandatory. But in my opinion it is a very good vehicle to supplement the Luxembourg fund tool-box.”

Interviewer: “If we look into the future, perhaps you have heard about the new draft Law related to the SIF/SICAR that has been deposited before the Parliament on January 18th, 2016 with the aim to revise these laws, do you think the RAIF will be further used as type of fund for especially exotic investments?” (Q5)

Mr. Braun: “I doubt that. To be honest, if I interpret your statement in negative way, we would say that the RAIF gets all the ‘trash’ and the regulated products keep all the high value assets, because they have to go through an authorization process by the CSSF. I do not believe in such a situation, because - and that is maybe a bit controversial to the short time to market - the RAIF will be much more scrutinized by all the players surrounding the RAIF. Especially the third party AIFM will have to check what is stated in the prospectus, because there is not a second regulatory

layer and they know that the CSSF is not looking into it. Sometimes people say, that the RAIF brings the time to market from 3 months, comparable with the CSSF and the SIF, to one week. I do not believe in the one week. Because it is not possible to reduce the Due Diligence processes to a week, but it probably reduces the launch time by a third, from three months to one month. Since it is being scrutinized by, nevertheless all the players around the AIFM but also the Depositories, the Administrator and possibly the Distributor, that means that you can't do just anything with it either, so all these - I called them 'trash'-assets - with which we had sometimes issues in the past, I do not think we will see them in a RAIF going forward because the market has learned sufficiently that these things are not being done, no matter if in a SIF, SICAR or RAIF."

Interviewer: "Perhaps one last question: What do you think about the acceptance in other European countries? Is there already something known if other countries will accept the RAIF structure from a tax/fiscal perspective?"
(Q6)

Mr. Braun: "You saw when the RAIF came out, a number of countries planned to do similar things. For example Malta was talking about it, the Irish were talking about it, that is why I think the concept of having an unregulated vehicle underneath an AIFM is a valid and good concept. In terms of taxation, I very much believe in the Luxembourg model which says, that we have a certain tax rate but at the same time things are modular and can be discussed or amended. We are fully compliant with things like BEPS, the European tax regimes etc., so I do not see any issues from other countries. I rather believe that other countries will jump on the same train and try to have similar vehicles as well."

Interviewer: "Many thanks for the interview, very interesting insights."

Mr. Braun: "Thank you. Good luck with your thesis!"

Interviewer: "Thank you, too."

VI Potential catalogue of questions for the interviews

- 1) Please describe yourself and your role within your company.
- 2) Do you know how many RAIF structures have already been set up in Luxembourg?
- 3) Have you been involved in any projects regarding RAIF structures or any similar?
- 4) What is the most favorable structure of AIFs? (SIF, SICAR, RAIF, UCI, etc.)
- 5) What are the advantages of the new structure RAIF?
- 6) How do typical investments of RAIFs look like?
- 7) Do you think that RAIF structures can bring added value to the investors in and outside of Luxembourg?
- 8) Is the RAIF a good cross-border investment vehicle and well placed from a marketing perspective?
- 9) Do you think it is an advantage to have less supervision through the CSSF compared to a SIF or other well-known fund structures in Luxembourg?
- 10) How do you think will the RAIF develop within the next years (short and long-term)?
- 11) Do you see any threats for RAIFs? If yes, could you please describe them?
- 12) What do you think about Luxembourg as domicile for RAIFs?
- 13) Do you think that other European countries will accept this structure?

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