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Arendt Financial Law Forum Asia 2018

Hong Kong, 21 November 2018

Agenda

- Opening Speech
- Session I: Structuring Alternative Investment Funds in the EU
- Session II: Distribution of Alternative Investment Funds in the EU
- Session III: UCITS and AIFMD Legal & Regulatory Updates
- Questions & Answers

Session I

Structuring Alternative Investment Funds in the EU

- Latest Trends in the Global and European Fund Industry
- Luxembourg and its Funds' Industry
- European Regulatory Framework
- Luxembourg AIFs vs offshore AIF Vehicles
- Luxembourg Vehicles
- Tax Structuring Aspects
- Alternative Investment Funds Structuring

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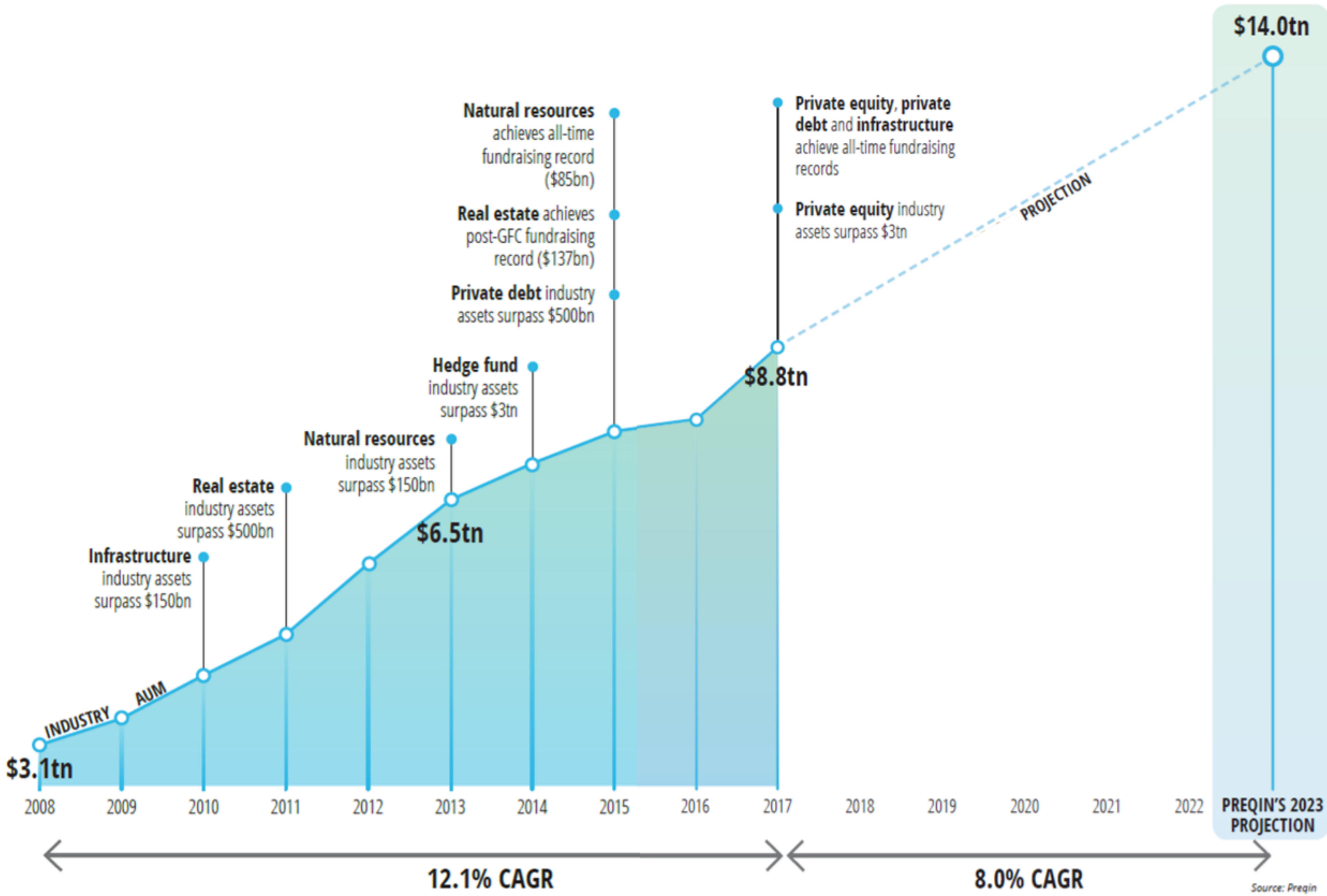
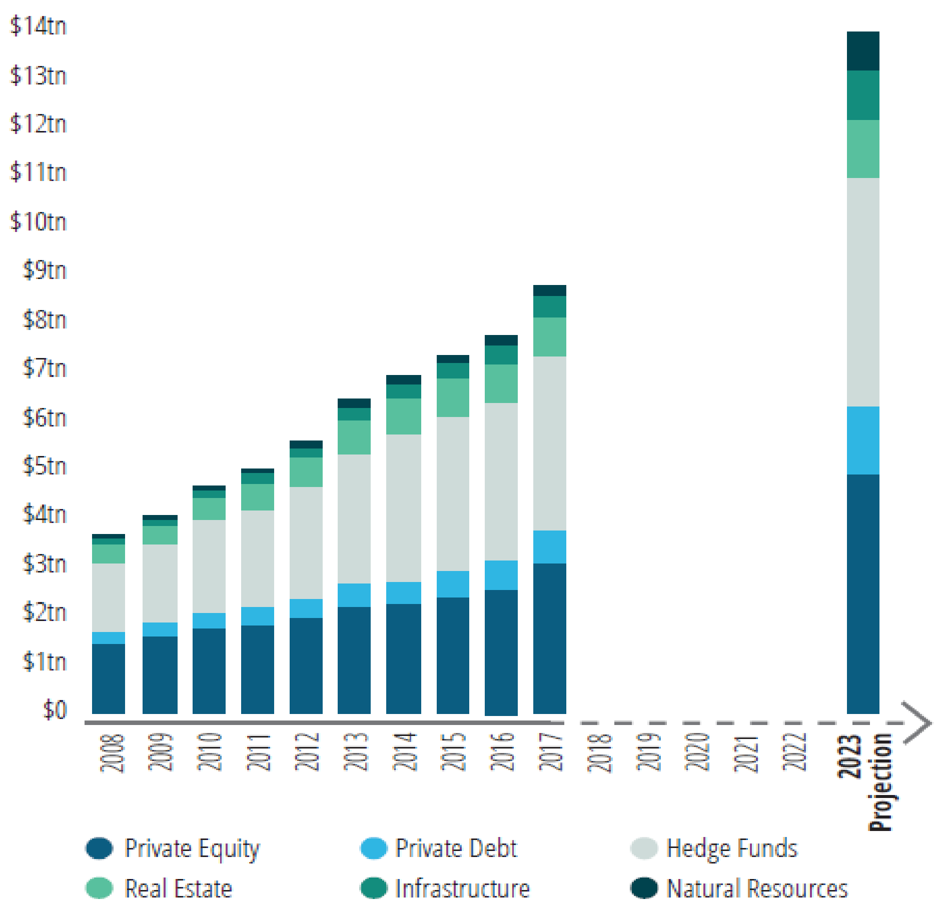
Global Alternative Investments Market Timeline



Global Alternative Investments Market
Main Trends

Assets under Management by Asset Class



- **Private equity** and **hedge fund** industries represent 75% of the alternative assets industry and are expected to contribute the **majority of the growth** in dollar terms **over the next five years**
- The **private debt** market is predicted to **double in size**, reaching $1.4tn in 2023 and **overtake the real estate** market to become the **third** largest alternatives industry
- Driven by **natural resources**, real assets are expected to represent **13% of the alternatives industry** by 2023
- Emerging markets: the **Chinese venture capital** industry already matches that of the US in size with an **increasing penetration of alternative assets**

Global Alternative Investments Market
Europe & Chinese FDI

TRENDS IN EUROPE

+40%

Private equity and venture capital fundraising in Europe for the **first six months of 2018** hit €45.6 billion ($52.9 billion), **up 40% vs. the second half of 2017**

+20bn

Private debt capital targeted by Europe-focused funds has **climbed by $20bn** since the middle of 2017 to Q3 2018

33,8%

33,8% of total global **real estate assets** were **invested in Europe** last year (€837 billion ($946 billion)

35,5%

Europe is the region with **the largest allocation within real estate portfolios** at 35.5%, followed by the US at 29.3% and Asia Pacific at 14.1%

EUROPE: 2nd largest region

for global alternative investments

CHINESE FOREIGN DIRECT INVESTMENT (FDI) 2018

EUROPE

$20 Bn

In the first six months of the year, newly announced **Chinese M&A into Europe** was $20 billion compared to $2.5 billion in North America.

NORTH AMERICA

$2 Bn

Chinese outbound **FDI into North America has dropped by a whopping 92 percent** in the last year from $24 billion to $2 billion

Trump effect

Chinese investing **nine times more in Europe than North America** as policies force divergence

Sources: Forbes 2018, Preqin Q2 2018, Invest Europe 2018, INREV 2018

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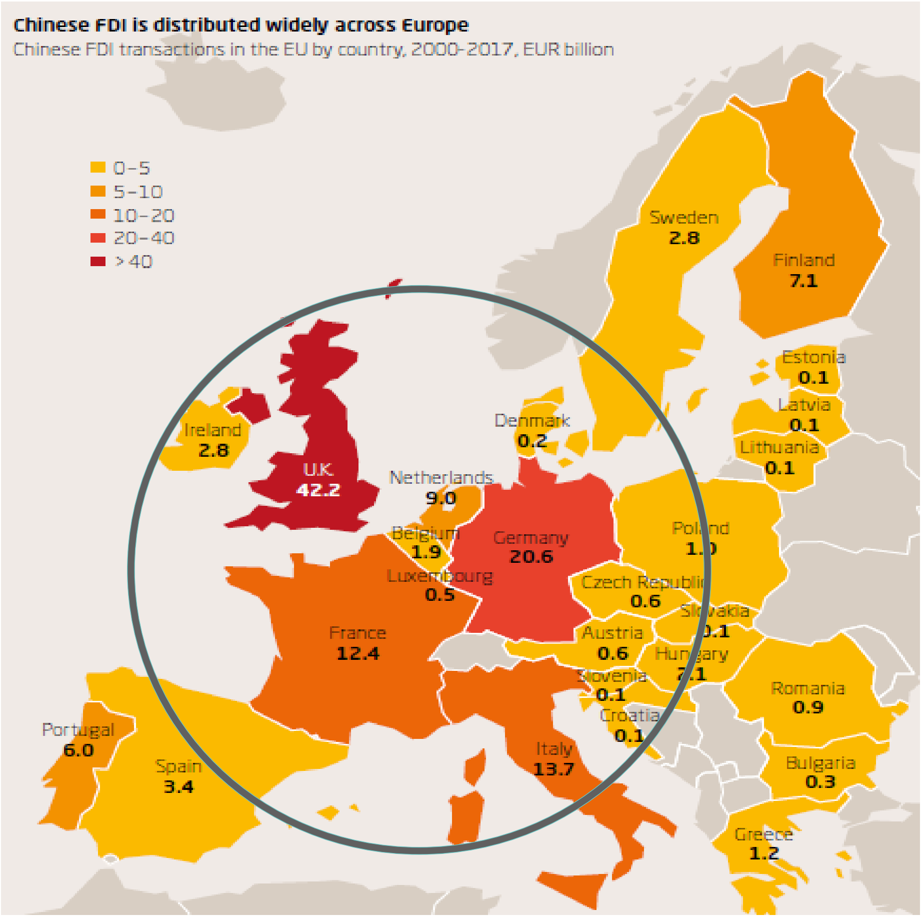
Luxembourg, the chinese gateway to the EU
The landscape of Chinese FDI in Europe

From $840 million invested in 2008, China's annual **FDI in Europe grew to $42 billion in 2017**.

Total Chinese investments in Europe, including both mergers and acquisitions (M&A) and greenfield investments, amount to **$318 billion**, **45 percent more than Chinese investment in the U.S.** between 2008 and 2017.

China's investments are also **broadly spread geographically:**

- United Kingdom ($70 billion)
- Italy ($31 billion),
- Germany ($20 billion)
- France ($13 billion)



Sources: Carnegie 2018, Bloomberg 2018.

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Grand Duchy of Luxembourg

PUBLIC FINANCES

Sovereign debt:
23,0%
Maastricht criteria: < 60%

Budget deficit/Surplus:
1,7%
Maastricht criteria: > -3%

RATING

AAA

Standard & Poor's
Moody's
Fitch

PRODUCTIVITY (GDP /hour)

Second highest in the world (second to Norway)

590.667

48%
foreigners

MACRO-ECONOMIC DATA

Real growth of GDP:
3,9%

Employment growth rate:
3%

Unemployment rate:
6,1%

Sources: Luxembourg for Finance, ALFI 2017 & 2018

Grand Duchy of Luxembourg (continued)

Investment funds

FUNDS, FUND UNITS AND NET ASSETS

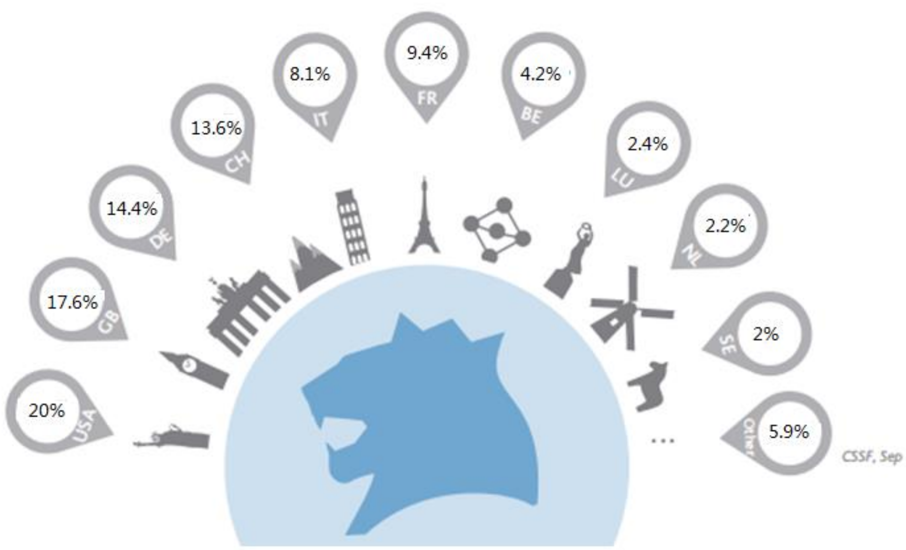
Number of funds	Number of Units	Net assets
4.044	**14.728**	**4.160 *Billion Euro***

ALFI/CSSF 2018

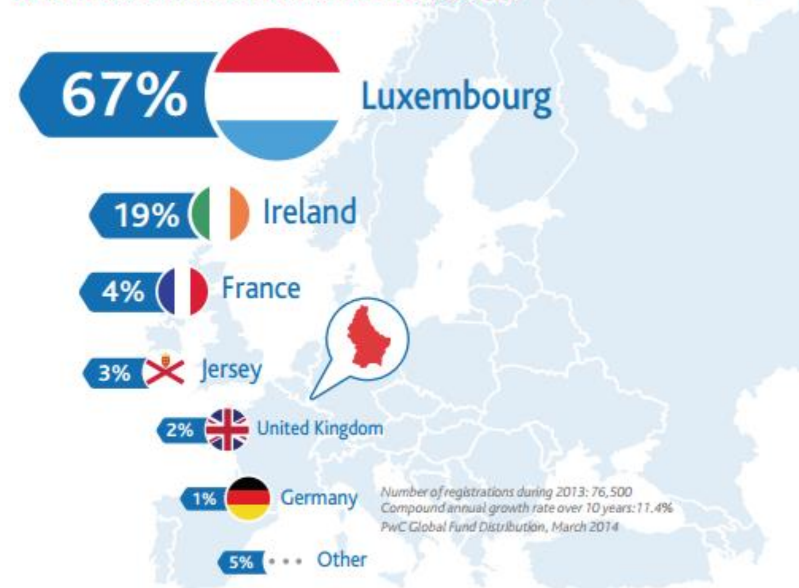
FIRST IN CROSS-BORDER FUND DISTRIBUTION

SECOND LARGEST INVESTMENT FUND CENTRE IN THE WORLD AFTER THE US

PROMOTERS OF LUXEMBOURG DOMICILED FUNDS BY COUNTRY OF ORIGIN



MARKET SHARES IN CROSS-BORDER FUND DISTRIBUTIONS

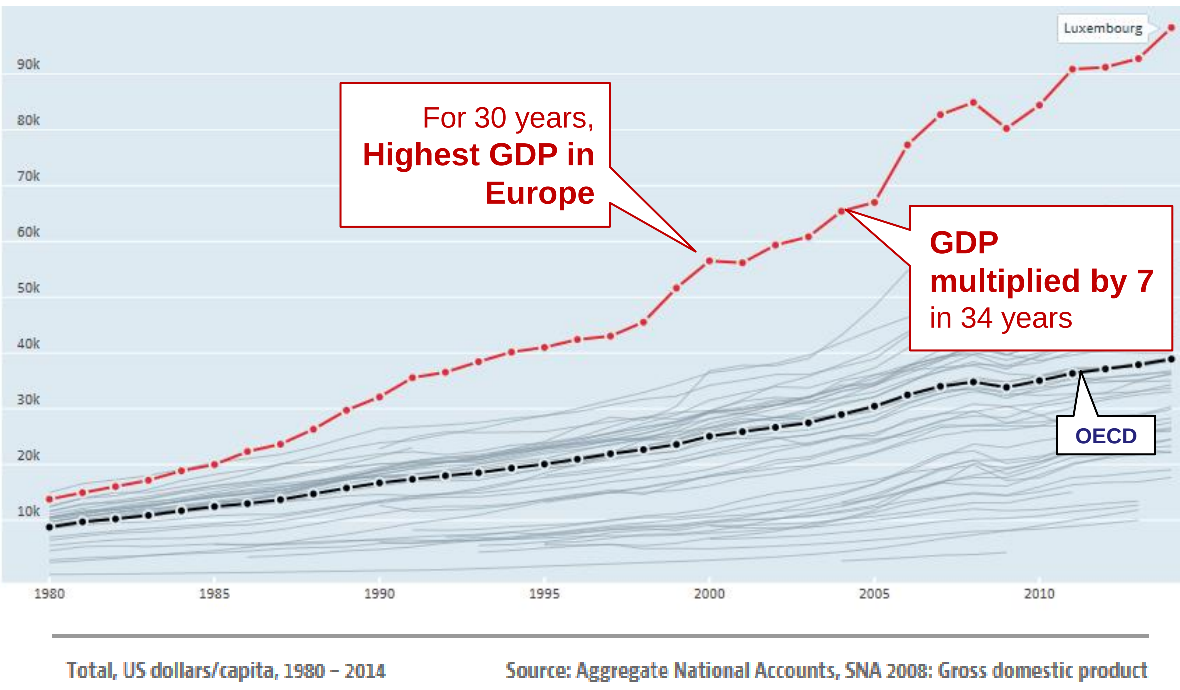


Sources: Luxembourg for Finance, ALFI Sep 2018

The advantages of Luxembourg

A constantly evolving business location

Gross domestic product (GDP)



The advantages of Luxembourg

A stable & business friendly environment

For more than 20 years, **Luxembourg is rated AAA***

*Fitch's, Moody's and Standard & Poor's rating

Business-oriented government which attracts international companies

Lowest standard VAT rate in European Union (17%)

A constitutional monarchy with a **stable political environment**

Efficient logistics network due to the clusters

Lowest government debt in Europe

= fiscal stability

Luxembourg fund industry
UCITS & AIF

UCITS	▪ **3,987** UCIs ▪ **14,796** fund units* ▪ EUR **4,237** billion of AUM in Luxembourg funds
AIF	▪ **330** fund units* invested in real estate with **EUR 69,842 million** net AUM ▪ **640** fund units* invested in Private Equity and Venture Capital with **EUR 88,527 million** net AUM ▪ **248** fully authorised AIFMs (PE/VC, real estate) in Luxembourg ▪ **575** registered (below-threshold) AIFM managers (PE/VC, real estate) in Luxembourg ▪ **533** reserved alternative investment funds (RAIFs) ▪ **469** special limited partnerships (with appointed AIFM) (*) Number of single funds plus number of sub-funds of umbrella structures

Source: CSSF September 2018

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AIFMD: Background & scope of application

- Objectives
  - Extend appropriate regulation and oversight to all alternative actors
  - Create a European market for alternative investment managers via passports for management and marketing activities

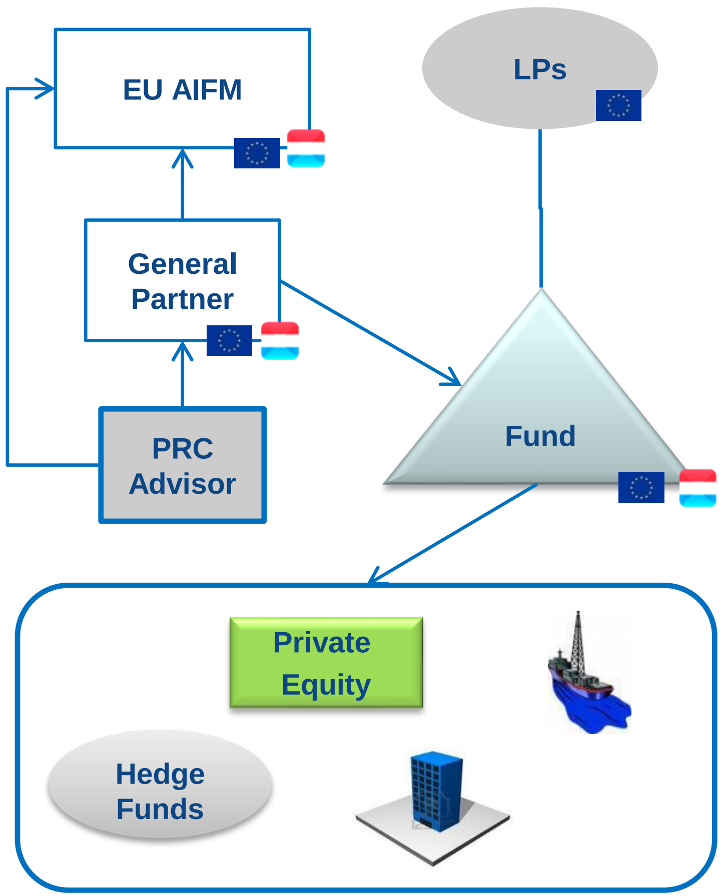
The AIFMD applies to

- EU AIFM which manage one or more AIF (EU or Non-EU)
- Non-EU AIFM which manage one or more EU AIF
- Non-EU AIFM which market one or more AIF (EU and Non-EU) in the EU

- Sources
  - Level 1: Directive 2011/61/EU ("AIFMD")
  - Level 2: Delegated regulation of the European Commission
  - ESMA: Several guidelines, discussion papers etc.
  - Luxemburg: Law of 12 July 2013 ("AIFM Law") and CSSF Q & A
  - EU Commission Q & A 25.03.2013
  - Circular CSSF 18/698 concerning approval process & organisation of management companies

Structuring a European Fund

Option 1: The Fund as a European limited partnership with appointment of a fully authorised AIFM



The Fund may be set up as a European limited partnership (or other type of fund) appointing a fully authorised AIFM. Full AIFMD compliance is mandatory if:

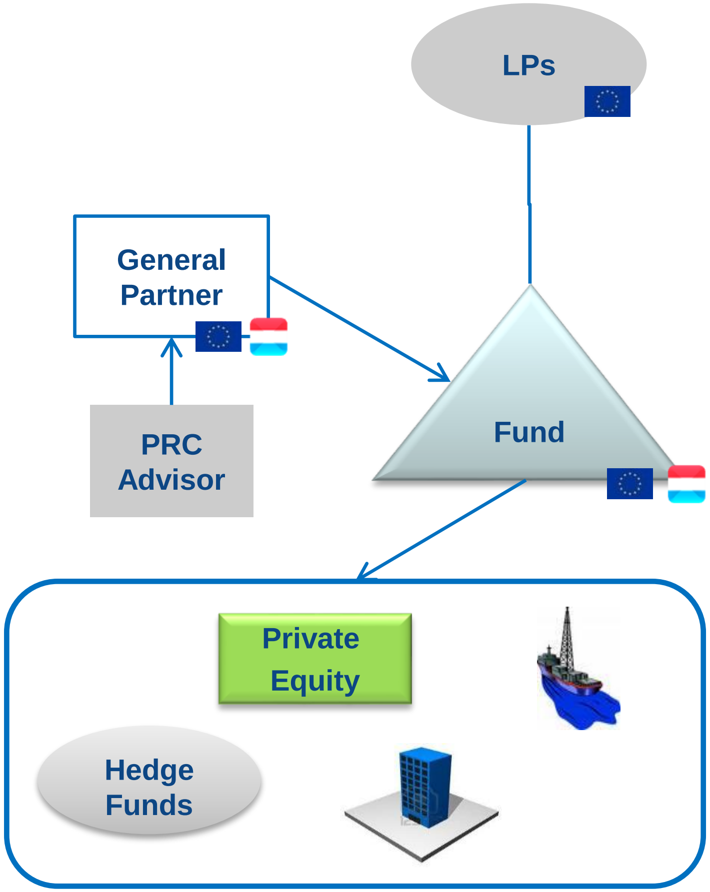
- The AuM of the European AIFM exceed EUR 500M for closed-ended, unleveraged funds;
- The AuM of the European AIFM exceed EUR 100M in all other cases.

The key features are:

- fund will be fully AIFMD compliant;
- no direct authorization or prudential supervision by a regulator unless required by local law;
- marketing passport to distribute the Fund to professional investors in Europe (single autorisation);
- fund may be marketed outside of Europe;
- fund may be advised by non-EU (e.g. PRC) advisor or fund management may be delegated outside of EU;
- fund may be eligible for preferential quotas under Solvency II.

Structuring a European Fund

Option 2: The Fund as a European limited partnership with appointment of a registered (i.e. not fully authorised) AIFM



The Fund may be set up as a European limited partnership (or other type of fund) with a registered (i.e. not fully authorised) AIFM if:

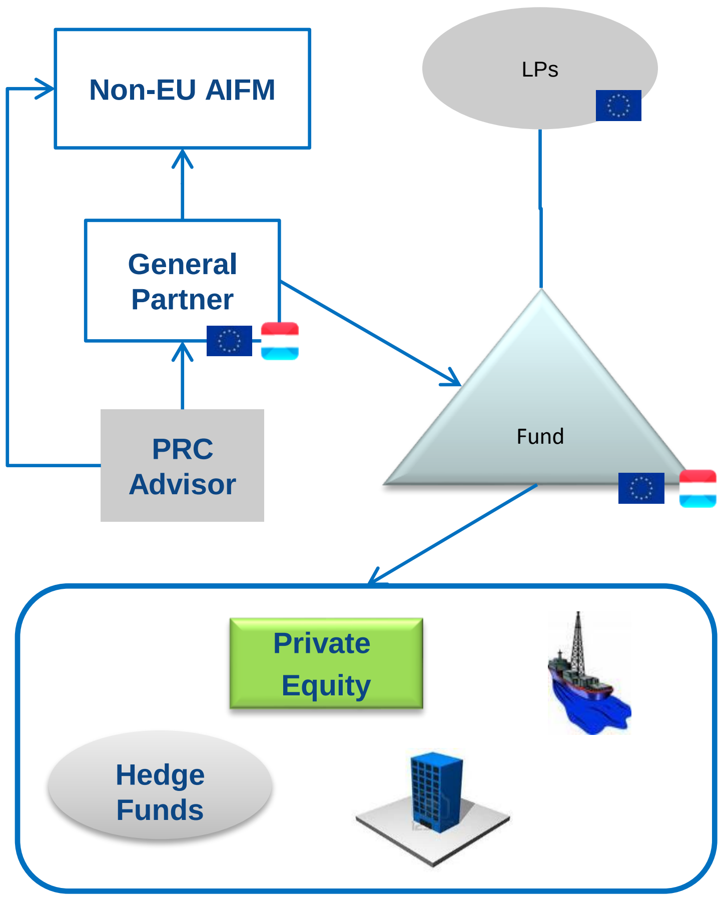
- The AuM of the European AIFM do not exceed EUR 500M for closed-ended, unleveraged funds;
- The AuM of the European AIFM do not exceed EUR 100M in all other cases.

The key features are:

- fund shall be registered with a European regulator;
- will be subject to limited reporting requirements;
- no direct authorization or prudential supervision by a regulator unless required by local law;
- no marketing passport to distribute the Fund, but may be distributed under NPPRs within Europe;
- fund may be marketed outside of Europe;
- fund may be advised by non-EU (e.g. PRC) advisor or fund management may be delegated outside of EU;
- Light touch regime which may be suitable for non-EU investors

Structuring a European Fund

Option 3: The Fund as a European limited partnership with appointment of a non-EU AIFM (article 42 AIFMD)



The Fund may be set up as a European limited partnership (or other type of fund) appointing a non-EU AIFM:

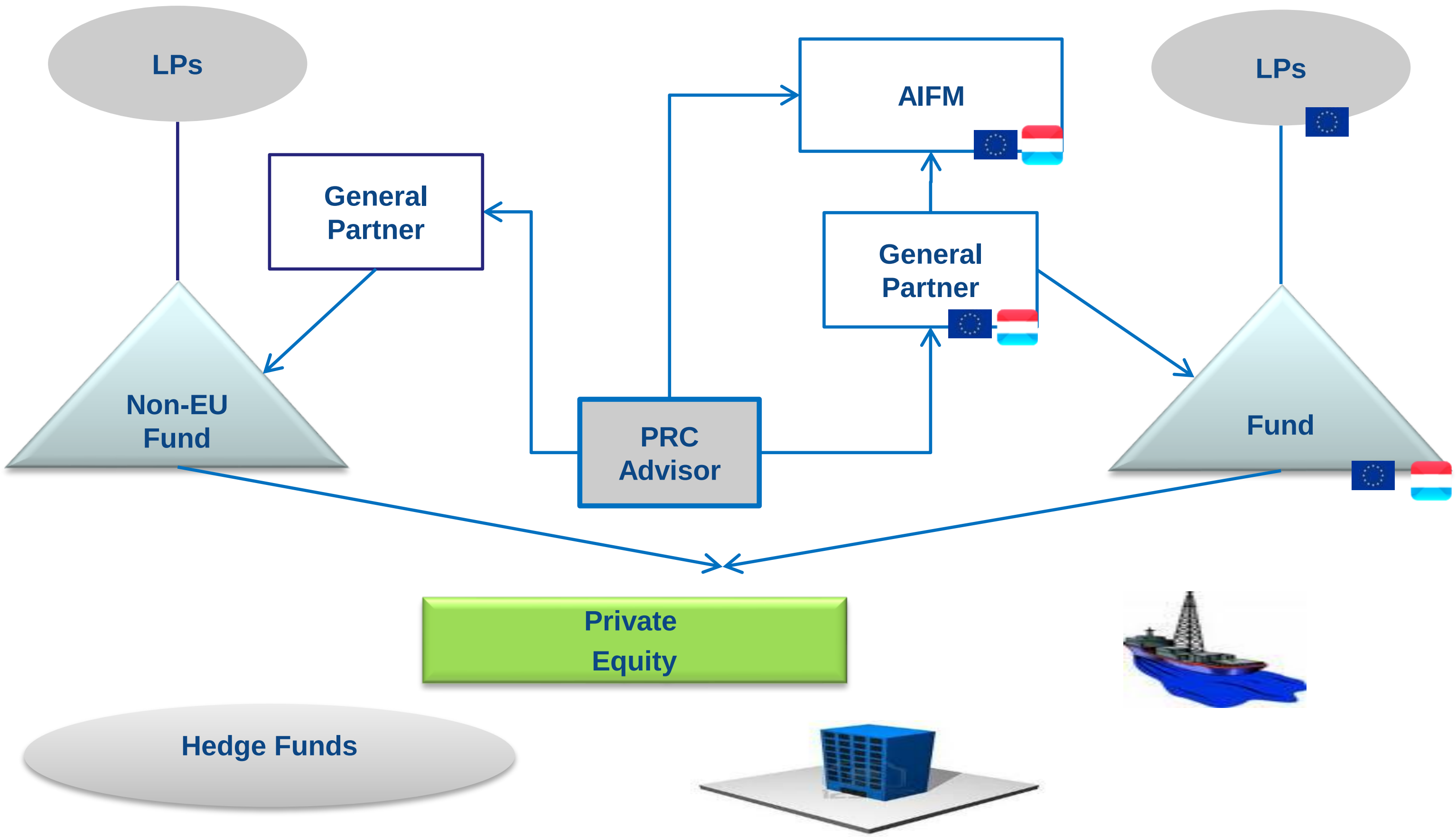
- If the fund is marketed to EU investors, compliance with art. 22 (annual report), 23 (disclosure) and 24 (reporting) and art. 26-30 of the AIFMD is mandatory;
- If the fund is not marketed to EU investors, it will be outside the scope of the AIFMD.

The key features are:

- no or limited AIFMD compliance;
- no authorization or prudential supervision;
- no EU marketing passport;
- fund may be marketed outside of Europe.

Structuring a European Fund

Option 4: Parallel Fund Structure



Structuring a European Fund

Option 4: Parallel Fund Structure

The European Fund may be set up as a fully AIFMD compliant parallel fund of a non-EU fund structure, allowing marketing with a passport into the EU.

The key features are:

- fund will run alongside a non-EU fund;
- fund cannot be set up as a feeder fund for a non-EU master fund;
- portfolio management can be performed by the same manager, be it the AIFM or the non-EU manager receiving a portfolio management delegation (provided there is an MoU in place between the EU and the manager’s jurisdiction);
- alternatively, the funds can be advised by the same advisor;
- funds may invest in common through a single aggregator vehicle;
- funds may have an investment agreement in place for the purposes of coordinating the voting procedure and sharing costs.

The advantages are:

- non-EU investors may remain in the non-EU vehicle which they have been used to;
- fund will operate as a fully AIFMD compliant fund with all advantages, including in particular the marketing passport;
- costs for AIFMD compliance may be confined to the European fund.

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Distribution under the AIFMD

Passport vs NPPRs

Marketing and distribution of AIFs in the EU

EU Marketing Passport (AIFMD)

- Authorised EU AIFM
- Managing EU AIF
- Sold to professional investors only
- Through a direct / indirect offering or placement
- At the initiative (or on behalf) of the AIFM

Distribution without passport (NPPRs)

- Non-EU AIFMs (Art 42) Non-EU AIFs (Art 36)

Potential Passport Extension ?

- AIFs distributed to retail investors (Art 43 AIFMD)
- EU Registered AIFM (Sub-thresholds)

AIFM Marketing Statistics *

- Around 190 Luxembourg AIFMs have passported 1,472 AIFs as follows:

Germany	11,6%	Sweden	6,7%
UK	10,1%	Denmark	6,5%
Italy	8,4%	Finland	6,2%
France	8,4%	Austria	5,7%
Netherlands	8,3%	Ireland	3,9%
Belgium	7,9%	Others	9,6%
Spain	6,8%	TOTAL	100%

- 293 non-EU AIFMs have notified 755 AIFs for sale in Luxembourg (under article 42 of the AIFMD)

- 19 EU AIFMs have notified 64 non-EU AIFs for sale in Luxembourg (under article 36 of the AIFMD)

Source: CSSF, as of November 2018

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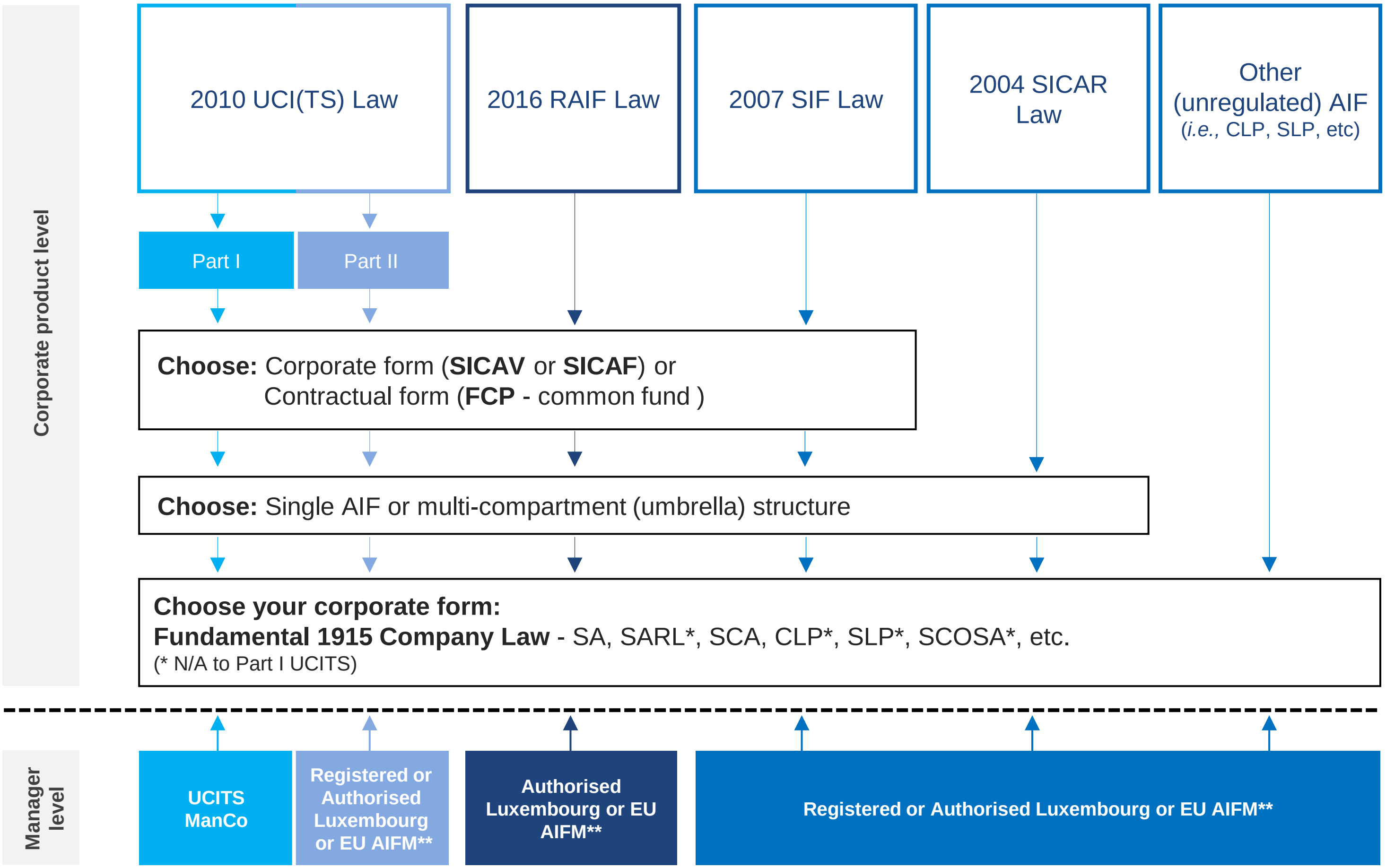
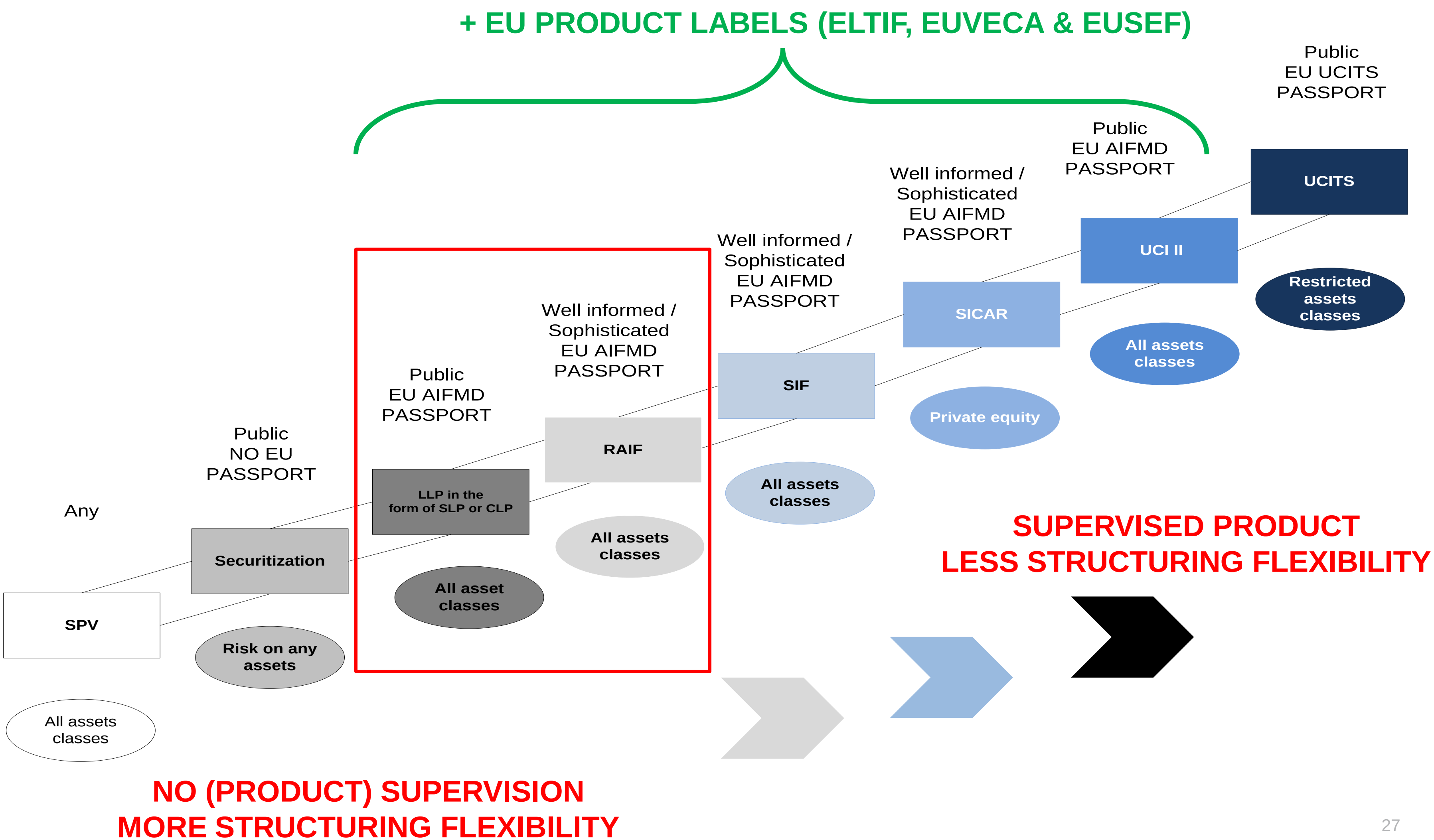
The Luxembourg toolbox
Overview



*** Third country when passport available*

The Luxembourg toolbox

From non-regulated to highly regulated



Luxembourg fund industry
Key features

1855 UCITS with more than EUR 3.486 billion of assets under management

as of February 2018

Regulated vehicle

Savings invested on a collective basis

Savings collected from the public

High diversification rules – principle of risk spreading

Invests in TS and other liquid financial assets

Taxe d'abonnement applicable under certain circumstances

UCITS

PRO's:

- Regulated vehicle under the supervision of the Luxembourg regulator, the *Commission de Surveillance du Secteur Financier* (CSSF)
- Umbrella form/stand-alone, variable or fixed share capital
- The shares/units are promoted to the public in the EU and the EEA
- Benefits from the EU passport and is open to the public of the EEA
- Share capital not less than EUR 31.000 at incorporation for public limited companies per share but EUR 1,25 million to be reached within 6 months

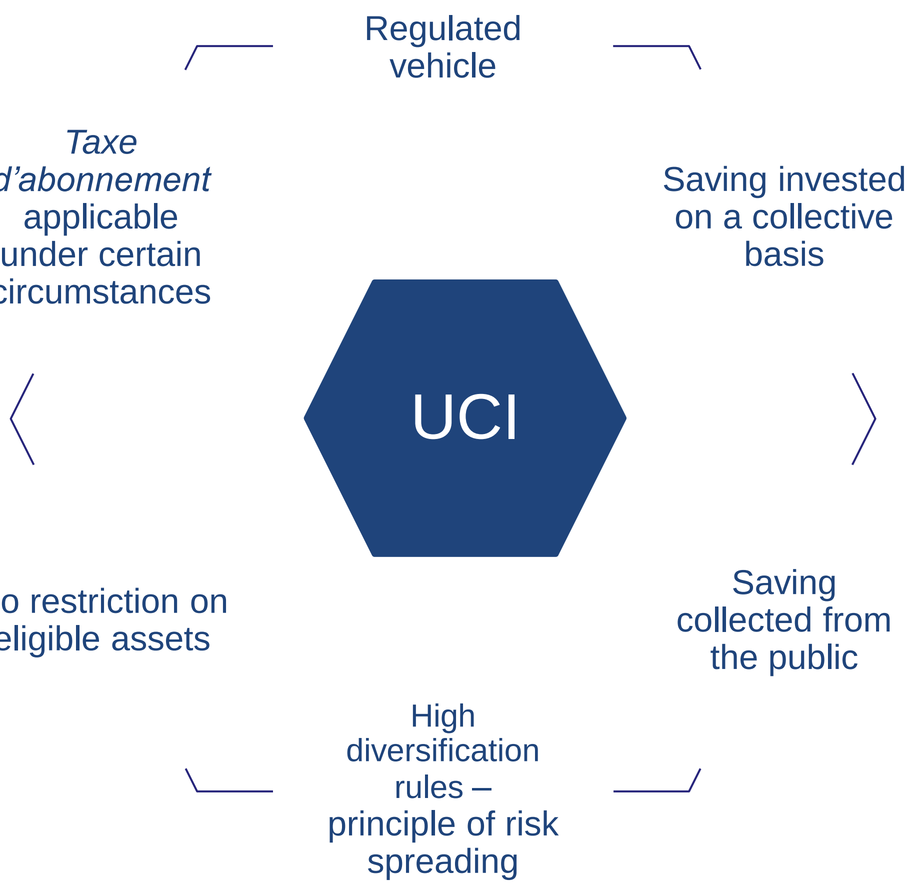
CON's:

- Time to market due to prior CSSF approval
- Must redeem at least twice per month its units/shares at the request of the investors = **open-ended**
- Investment restrictions very strict and no borrowing allowed

Luxembourg fund industry
Key features

320 UCI with more than EUR 154 billion of assets under management

as of February 2018



PRO’s:

- Regulated vehicle under the supervision of the Luxembourg regulator, the *Commission de Surveillance du Secteur Financier* (CSSF)
- Umbrella form/stand-alone, variable or fixed share capital
- The shares/units may be sold to retail investors in Luxembourg
- Share capital not less than EUR 30.000 at incorporation for public limited companies per share but EUR 1,25 million to be reached within 6 months

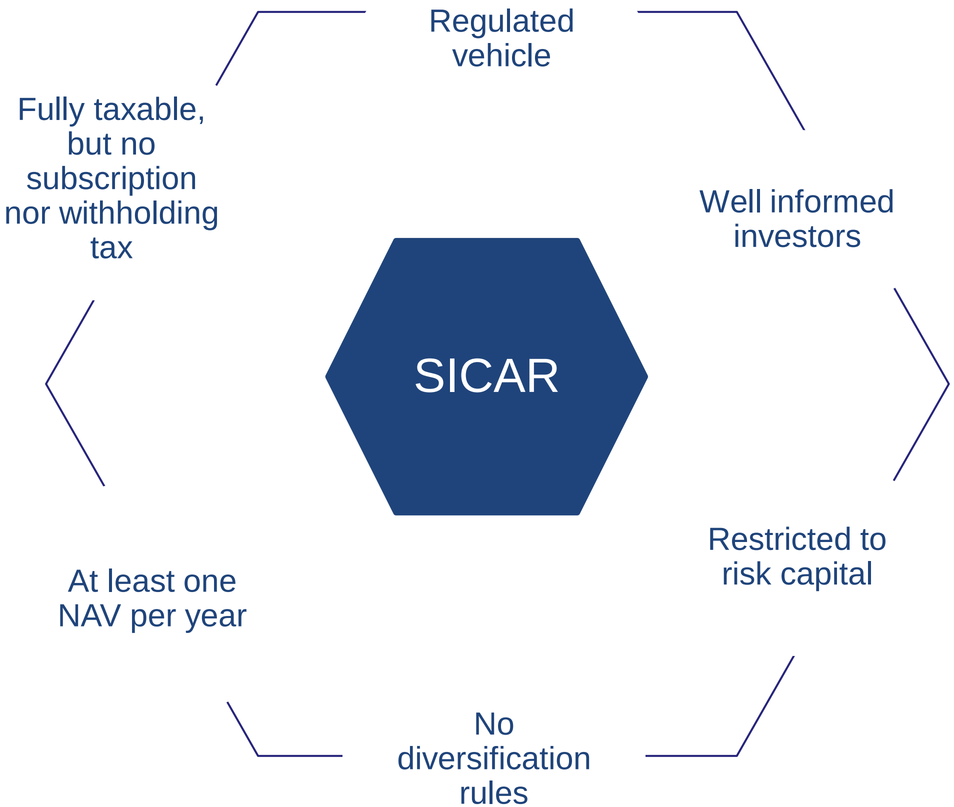
CON’s:

- Time to market due to prior CSSF approval

Luxembourg fund industry
Key features

284 SICARs with more than EUR 45 billion of assets under management

as of February 2018



PRO's:

- Regulated vehicle under the supervision of the Luxembourg regulator, the *Commission de Surveillance du Secteur Financier* (CSSF)
- Institutional and professional investors, including High Net Wealth Individual (HNWI), managed account solutions
- Umbrella form/stand-alone, variable or fixed share capital
- Fully taxable (26.01% for 2018) but exemption on (i) the returns derived from securities, whether in the form of interest income, dividends or capital gains and on (ii) income arising from funds awaiting to be invested by the SICAR (transit funds)
- Share capital and share premium not less than EUR 31.000 at incorporation for public limited companies per share but EUR 1,25 million to be reached within 12 months

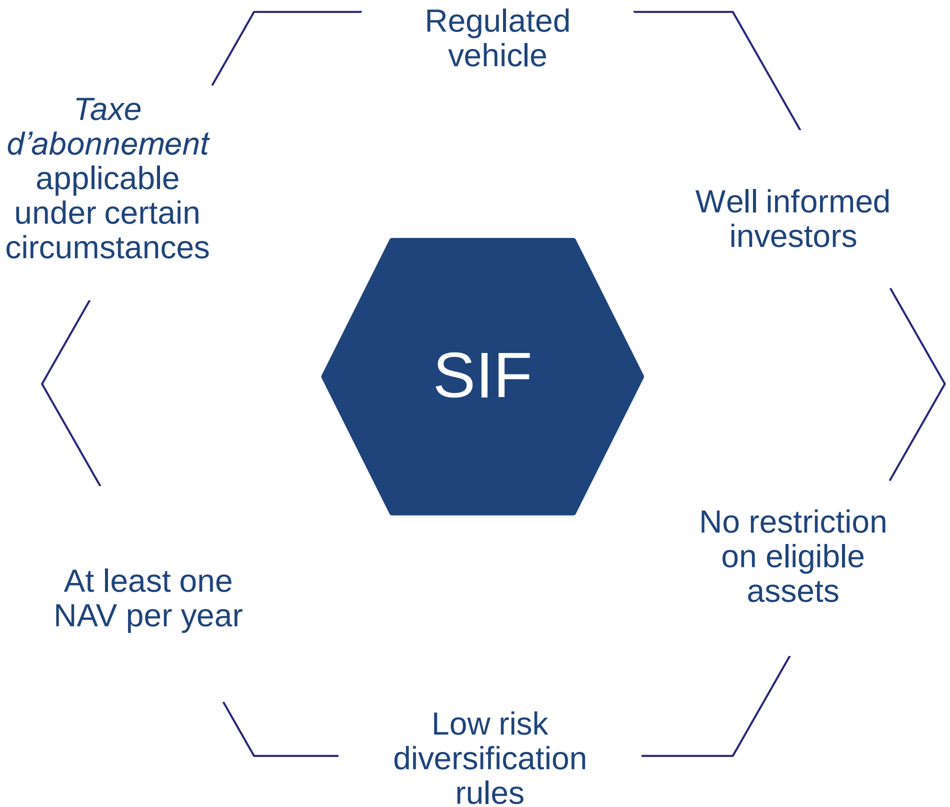
CON's:

- Time to market due to prior CSSF approval
- AIFMD impacts

Luxembourg fund industry
Key features

1571 SIFs with more than EUR 472 billion of assets under management

as of February 2018



PRO’s:

- Regulated vehicle under the supervision of the Luxembourg regulator, the *Commission de Surveillance du Secteur Financier* (CSSF)
- Institutional and professional investors, including High Net Wealth Individual (HNWI), managed account solutions
- Umbrella form/stand-alone, variable or fixed share capital
- Tax exempt status (subject only to an annual subscription tax of 0.01% payable on the net asset value (“NAV”) unless an exemption applies) and entitlement to several double tax treaties if established as a company
- Share capital and share premium not less than EUR 31.000 at incorporation for public limited companies per share but EUR 1,25 million to be reached within 12 months

CON’s:

- Time to market due to prior CSSF approval
- AIFMD impacts

Luxembourg fund industry
Key features

362 RAIFs

as of February 2018

Unregulated vehicle

Well informed investors

No restriction on eligible assets

Low risk diversification rules

Lightened accounting requirements

Taxe d'abonnement applicable under certain circumstances

RAIF

PRO's:

- Time to market, no prior approval of the Luxembourg regulator, the *Commission de Surveillance du Secteur Financier* (CSSF)
- Institutional and professional investors, including High Net Wealth Individual (HNWI)
- Umbrella form/stand-alone, variable or fixed share capital with lightened requirements
- Tax exempt status (subject only to an annual subscription tax of 0.01% payable on the net asset value ("NAV") unless an exemption applies) and entitlement to several double tax treaties if established as a company

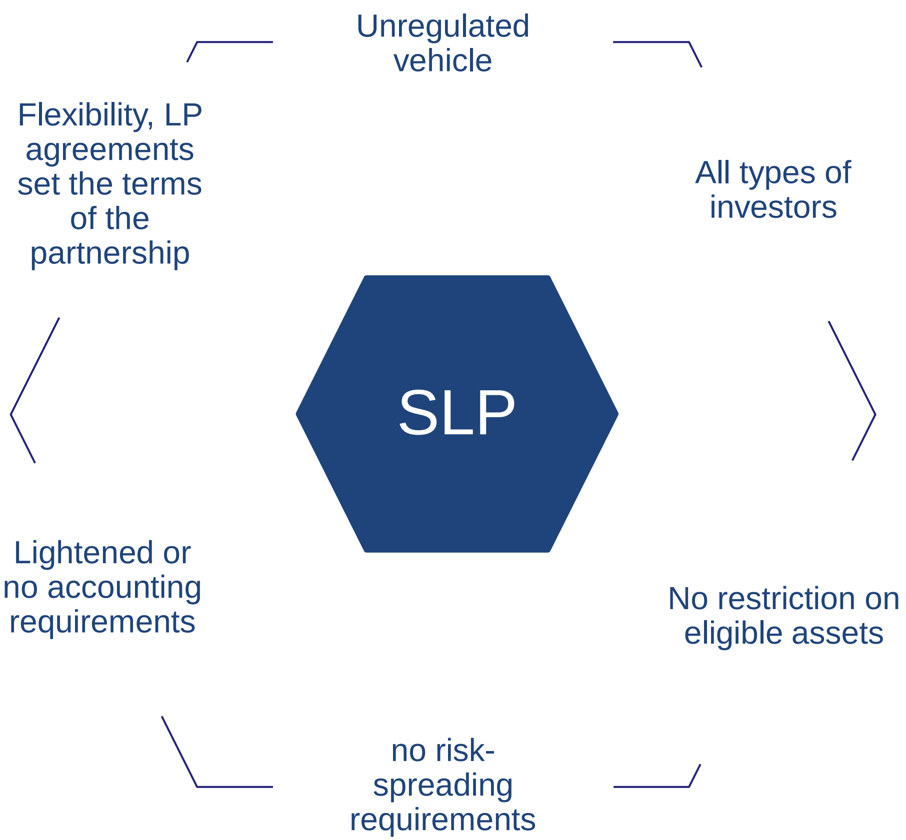
CON's:

- Fully fledged EU AIFM to be appointed
- Compared to unregulated AIFs in the form of SCS or SCSp ONLY advantage if (a) umbrella structure and (b) marketing to well-informed investors in Luxembourg

Luxembourg fund industry
Key features

469 SLPs*

as of February 2018



<u>PRO's:</u>

- Time to market, no prior approval of the Luxembourg regulator, the *Commission de Surveillance du Secteur Financier* (CSSF)
- All types of investors, including High Net Wealth Individual (HNWI)
- Tax transparent status
- no minimum capital requirements;
- no investor eligibility requirements (unless subject to AIFMD);
- no authorization or prudential supervision by the CSSF;
- capital accounts or unitised models available;
- only the general partner has unlimited liability.

<u>CON's:</u>

- No umbrella form possible
- Fully fledged EU AIFM to be appointed if AuM are above EUR 500 mio (with leverage) or EUR 100mio (without leverage)

*this number does not show the total number of LPs in Luxembourg, it only shows the ones with an authorised AIFM

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Luxembourg investment structuring

A neutral tax environment

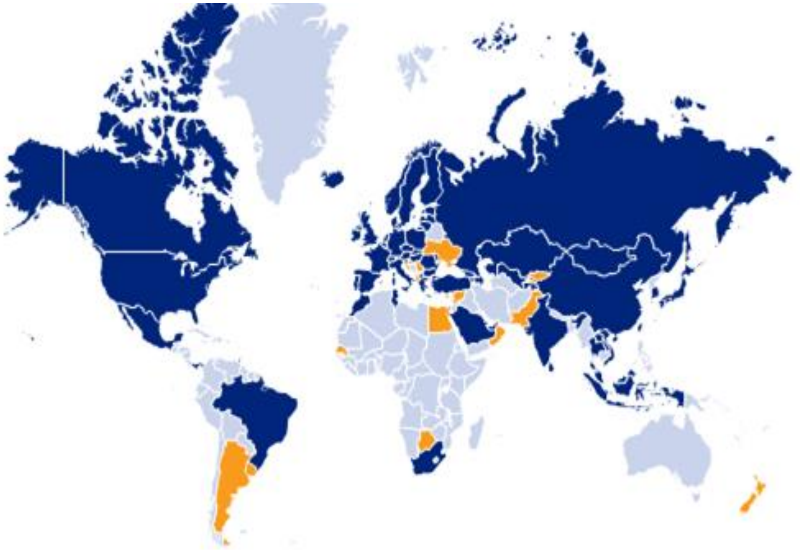
- Low effective tax rate
- Low or zero ‘exit’ taxes (withholding taxes)
- 100% participation exemption for dividends and capital gains on shares with very flexible / favorable conditions
- Access to EU Directives
- Extensive network of double tax treaties
- No CFC legislation
- No capital / stamp duty

Luxembourg investment structuring

Our double tax treaty network

Tax Treaties in force
Tax Treaties pending

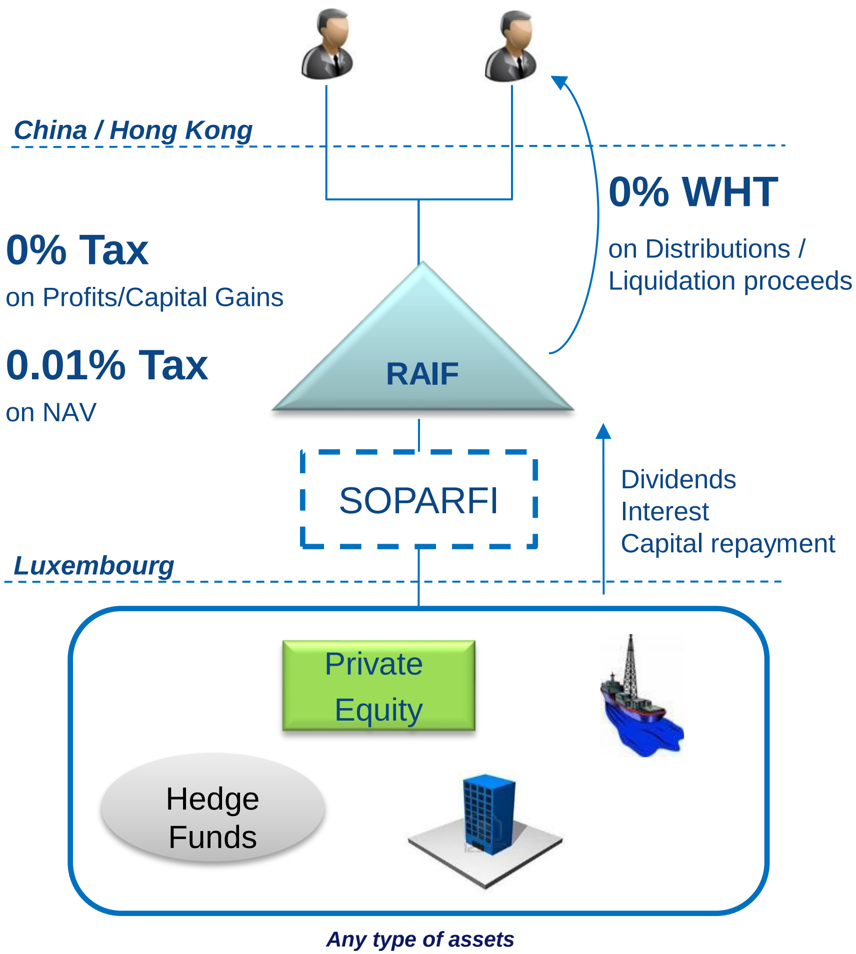
1. Armenia
2. Austria
3. Azerbaijan
4. Bahrain
5. Barbados
6. Belgium
7. Brazil
8. Bulgaria
9. Canada
10. China
11. Czech Republic
12. Denmark
13. Estonia
14. Finland
15. France
16. Georgia
17. Germany
18. Greece
19. Guernsey
20. Hong Kong
21. Hungary
22. Iceland
23. India
24. Indonesia
25. Ireland
26. Isle of Man
27. Israel
28. Italy
29. Japan
30. Jersey
31. Kazakhstan
32. Laos
33. Latvia
34. Liechtenstein
35. Lithuania
36. Macedonia
37. Malaysia
38. Malta
39. Mauritius
40. Mexico
41. Moldova
42. Monaco
43. Mongolia*
44. Morocco
45. Netherlands
46. Norway
47. Panama
48. Poland
49. Portugal
50. Qatar
51. Romania
52. Russia
53. San Marino
54. Saudi Arabia
55. Seychelles
56. Singapore
57. Slovakia
58. Slovenia
59. South Africa
60. South Korea
61. Spain
62. Sri Lanka
63. Sweden
64. Switzerland
65. Taiwan
66. Tajikistan
67. Thailand
68. Trinidad & Tobago
69. Tunisia
70. Turkey
71. United Kingdom
72. United Arab Emirates
73. USA
74. Uzbekistan
75. Vietnam
76. **Albania**
77. **Andorra**
78. **Argentina**
79. **Botswana**
80. **Brunei**
81. **Croatia**
82. **Cyprus**
83. **Egypt**
84. **Kyrgyzstan**
85. **Kuwait**
86. **Lebanon**
87. **New Zealand**
88. **Oman**
89. **Pakistan**
90. **Senegal**
91. **Serbia**
92. **Syria**
93. **Ukraine**
94. **Uruguay**



***terminated as from 2014**

Source: Luxembourg Tax Authority – January 2015

Reserved Alternative Investment Fund (RAIF)



Tax advantages

- No taxes on capital gains, profits or income
- The RAIF is only subject to an annual subscription tax of 0.01% payable on the net asset value ("NAV")
- No withholding tax ("WHT") on distributions, whether in the form of dividends or interest payments or other, paid by the RAIF to the Asian investors
- No tax on capital gains realised by the Asian investors upon the sale of the RAIF's shares/units
- No tax on the profits of liquidation earned by and repatriated to the Asian investors
- No stamp duty or other tax upon the issue of the RAIF's units/shares
- No inheritance tax on the transfer of the RAIF's units/shares upon death of an Asian investor

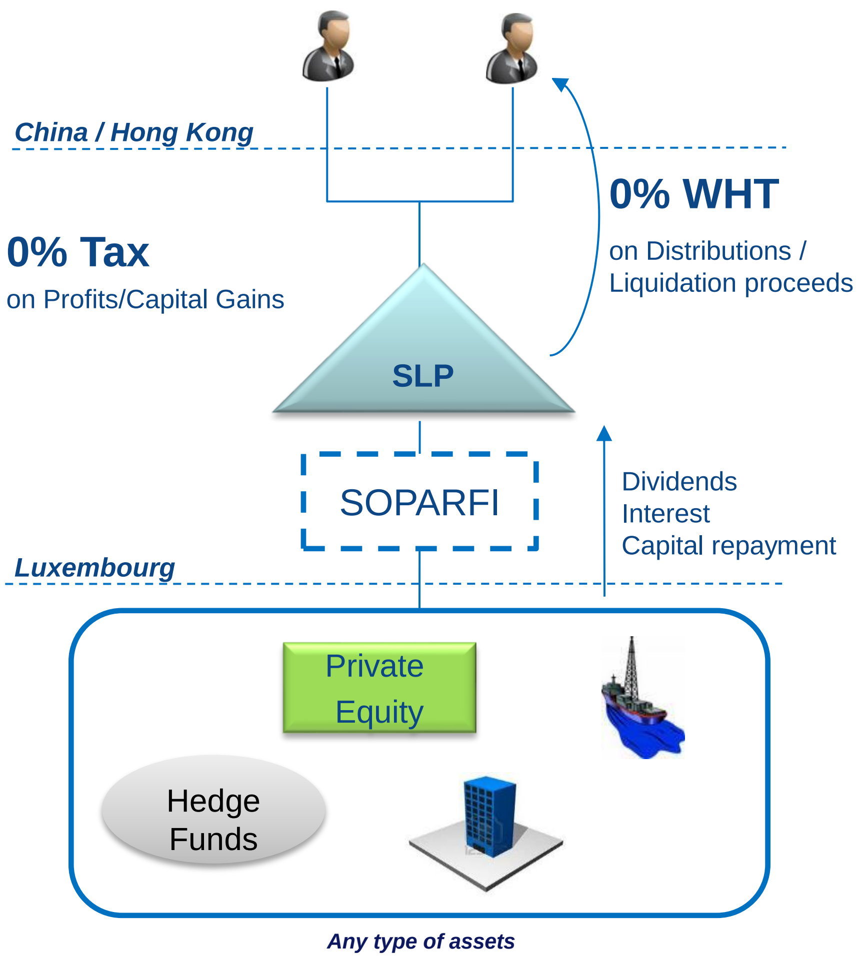
Eligible investments

- Any type of assets

Point of attention

- Access to double tax treaties (DTTs) to be checked on a case-by-case basis - Possible SOPARFI interposition

Special Limited Partnership (SLP)



Tax advantages

- Tax transparent, no taxes on capital gains, profits or income at the level of the SLP
- No withholding tax ("WHT") on distributions, whether in the form of dividends or interest payments or other, paid by the SLP to the Asian investors
- No tax on capital gains realised by the Asian investors upon the sale of the SLP's units
- No tax on the profits of liquidation earned by and repatriated to the Asian investors
- No stamp duty or other tax upon the issue of the SLP's units
- No inheritance tax on the transfer of the SLP's units upon death of an Asian investor

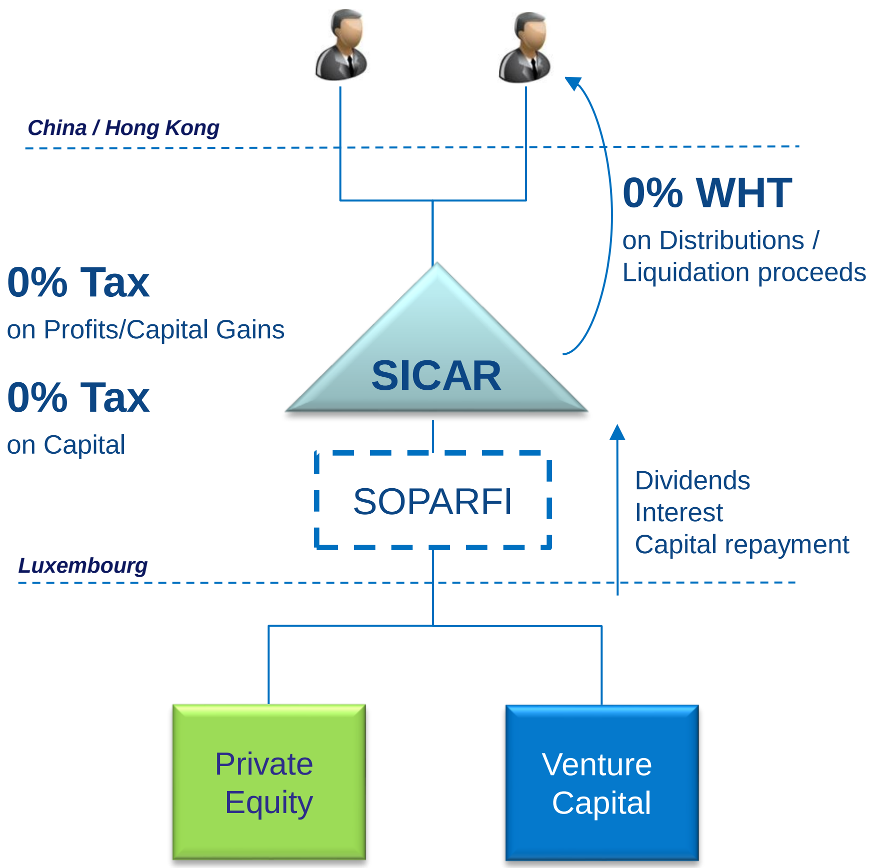
Eligible investments

- Any type of assets

Point of attention

- Access to double tax treaties (DTTs) to be checked on a case-by-case basis - Possible SOPARFI interposition

Investment Company in Risk Capital (SICAR)



Tax advantages

- Fully taxable (29.22% for 2016, 27.08 % for 2017, 26.01% for 2018) but exemption on (i) the return derived from securities, whether in the form of interest income, dividends or capital gains and on (ii) income arising from funds awaiting to be invested by the SICAR (transit funds)
- No subscription tax, but subject to a minimum net wealth tax
- No withholding tax (”WHT”) on distributions, whether in the form of dividends or interest payments or other, paid by the SICAR to the Asian investors
- No tax on capital gains realised by the Asian investors upon the sale of the SICAR’s shares/units
- No tax on the profits of liquidation earned by and repatriated to the Asian investors

Eligible investments

- Appropriate for risk capital investments

Points of attention

- Access to DTTs and EU Directives (in principle) for avoidance of withholding tax on source country income
- Possible SOPARFI interposition

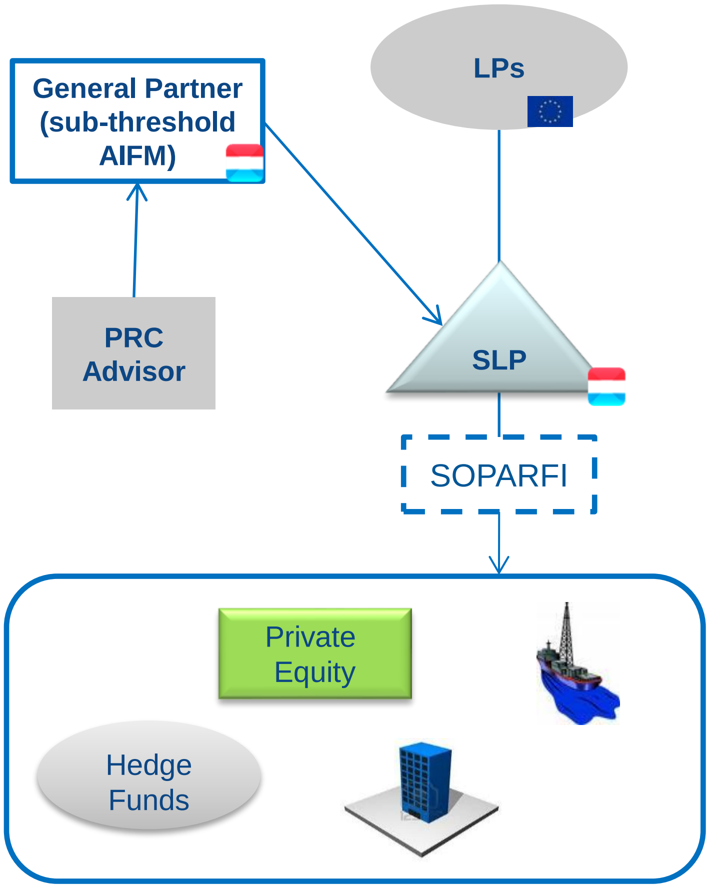
Session I

Structuring Alternative Investment Funds in the EU

- Latest Trends in the Global and European Fund Industry
- Luxembourg and its Funds' Industry
- European Regulatory Framework
- Luxembourg AIFs vs offshore AIF Vehicles
- Luxembourg Vehicles
- Tax Structuring Aspects
- Alternative Investment Funds Structuring

Example of structure

Option 1: The Fund as a Special Limited Partnership with a “sub-threshold AIFM”



Any type of assets

In this set-up, the GP would act as “sub-threshold” AIFM of the partnership. The SLP is suitable for structuring joint-ventures, special purpose vehicle as well as open-ended or closed-ended funds. In addition, SLPs are particularly convenient for private equity transactions where (i) tax transparency is required at the level of the partnership and (ii) fund initiators want to retain total control over the management.

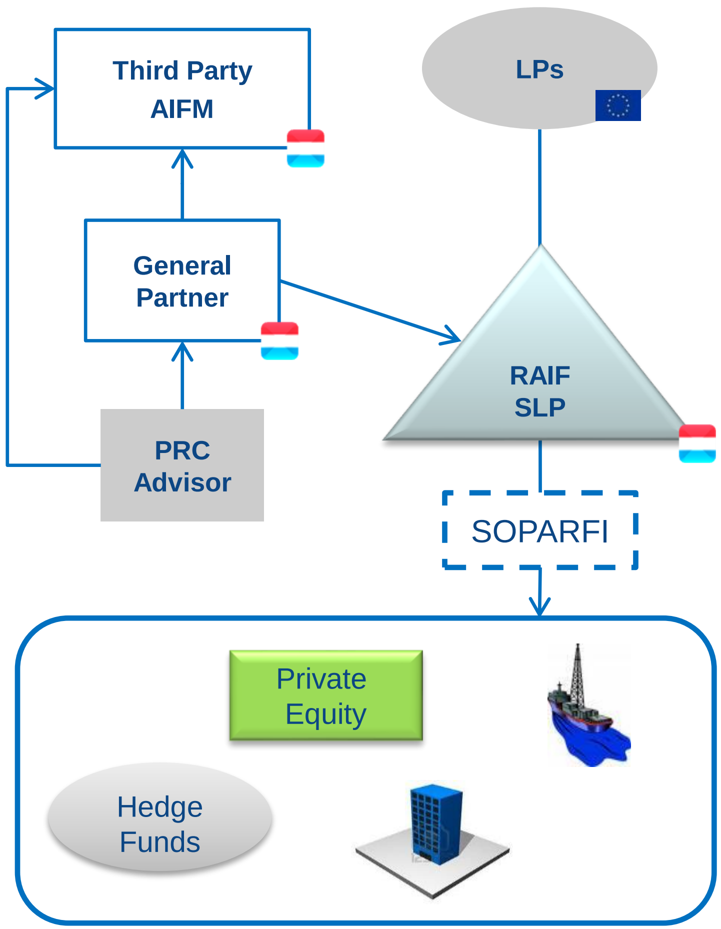
The key features are:

- flexibility, limited partnership agreements set the terms of the partnership;
- no minimum capital requirements;
- no investment restriction or limitations;
- no risk-spreading requirements;
- no authorization or prudential supervision by the CSSF;
- capital accounts or unitized models available;
- simplified accounting obligations;
- only the general partner has unlimited liability.

The Fund may be converted into a RAIF at a later stage if necessary.

Example of structure

Option 2: The Fund as a multi-compartment RAIF in the form of a SLP with appointment of a third party AIFM



Any type of assets

The Fund may be set up as a multi-compartment RAIF (with at least one compartment upon launching) in the form of a SLP with a Luxembourg GP and a third party AIFM.

The key features are:

- no investment restrictions or limitations;
- risk-spreading requirements ;
- no authorization or prudential supervision by the Luxembourg regulator (CSSF);
- simplified accounting obligations;
- only the GP has unlimited liability;
- marketing passport to distribute the Fund to professional investors in Europe (single autorisation);
- all obligations and duties foreseen by the AIFMD would be performed by the service provider;
- no further substance requirements would apply;
- no time consuming authorisation procedure with the CSSF would be necessary.

Session II

Distribution of Alternative Investment Funds in the EU

- Description of the European and Asian fund products distribution
- NPPRs vs AIFM passport, legal & regulatory landscape of main markets, reporting requirements
- Own AIFM vs third-party AIFM

Session II

Distribution of Alternative Investment Funds in the EU

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Distribution under the AIFMD: key terms

National private placement regime (“**NPPR”**) regulate the marketing by AIFMs of AIFs that are not allowed to be marketed under the AIFMD passporting regime. This relates to the marketing of non-EU AIFs and AIFs managed by non-EU AIFMs, sub-threshold AIFMs and to non-professional investors.

Private placement

Authorised EU AIFMs benefit from a passport to market EU AIFs to professional investors in the EU

AIFMD marketing passport

“**Reverse solicitation**” or “passive marketing” is the marketing which is at the own initiative of the investor.

Reverse solicitation

AIF distribution - principles

Capital raising under AIFMD

Marketing

“**Marketing”** means a direct or indirect offering or placement at the initiative of the AIFM or on behalf of the AIFM of units or shares of an AIF it manages to or with investors domiciled or with a registered office in the EU.

Distribution

“Distribution” corresponds to all the methods used to market AIFs authorised for sale in the EU.

Marketing Trends

- Steady growth in Alternative Investment Sectors over the last years
- Investors dedicated products market
- Emergence of Specialised Placement Agents
- Increased presence of Asian Asset Managers
- EU AIFs more and more used for EU and non EU distribution countries

Session II

Distribution of Alternative Investment Funds in the EU

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Raising money in the EU by non-EU managers

Raising money in the EU by non-EU managers

Marketing Matrix

AIF concerned	Marketing regime	Sold to	How?
EU AIF + **Authorized** EU AIFM	Passport	Professionals	Home State Notification
▪ Non-EU AIF + Authorized EU AIFM ▪ AIF + Registered EU AIFM ▪ AIF + Non EU-AIFM ▪ EU AIF + Authorized AIFM targeting EU retail	National Private Placement Regime (NPPR)	Professionals Retail investors	Registration / authorization

Raising money in the EU by non-EU managers

Marketing vs. pre-marketing

- What is "marketing"?

AIFMD defines "marketing" as a direct or indirect offering or placement at the initiative of the AIFM or on behalf of the AIFM of units or shares of an AIF it manages to or with investors domiciled or with a registered office in the EU. **Marketing in the EU triggers application of the AIFMD even to non-EU managers.**

- What is "pre-marketing" (i.e. activities not yet triggering filing or registration requirements)?

Pre-marketing (i.e. testing an investment idea or strategy with potential investors) would be admissible and hence not require any information of regulators , but definition, if any ,differs in each MS. For example, UK, Lux and Germany: draft PPM can be used, making clear that no subscription is possible! Some MS are stricter! Subscriptions by investors after such pre-marketing activities are considered as being the result of marketing, and hence necessary prior authorizations must have been obtained.

Circulation of Draft documents = Marketing ?	
Austria	yes
Belgium	no
Denmark	no
Finland	yes *
France	no **
Germany	no
Ireland	yes ***
Italy	yes
Luxembourg	no
Norway	yes
Spain	yes
Sweden	no
The Netherlands	no
United Kingdom	no

* But Roadshows OK

** But towards 50 investors only

*** But Promotional doc ok if not related to a specific product

Raising money in the EU by non-EU managers

- What is reverse solicitation within the EU ?

“ Reverse solicitation […] involves providing information regarding an AIF […] and making units of the AIF available for purchase [to] a potential investor upon the initiative of such investor […] in the absence of any solicitation by the AIFM […] ”

- There is currently no common EU-wide guidance on reverse solicitation and positions vary across the EU
- Reverse solicitation is only possible for professional investors
- When relying on reverse solicitation, the AIFM has the burden of proof as regards to the investor’s initiative (a written confirmation)
- Reverse solicitation is possible with a specific AIF, not ‘any product’: → specific fund name must be mentioned!
- Reverse solicitation should not be used to circumvent the AIFMD: → Reverse solicitation is not a marketing strategy!
- Complex to administer (record keeping, monitoring for each transaction,…)
- Unlikely to work for smaller or “start-up” managers, and not in line with marketing campaigns of larger asset managers

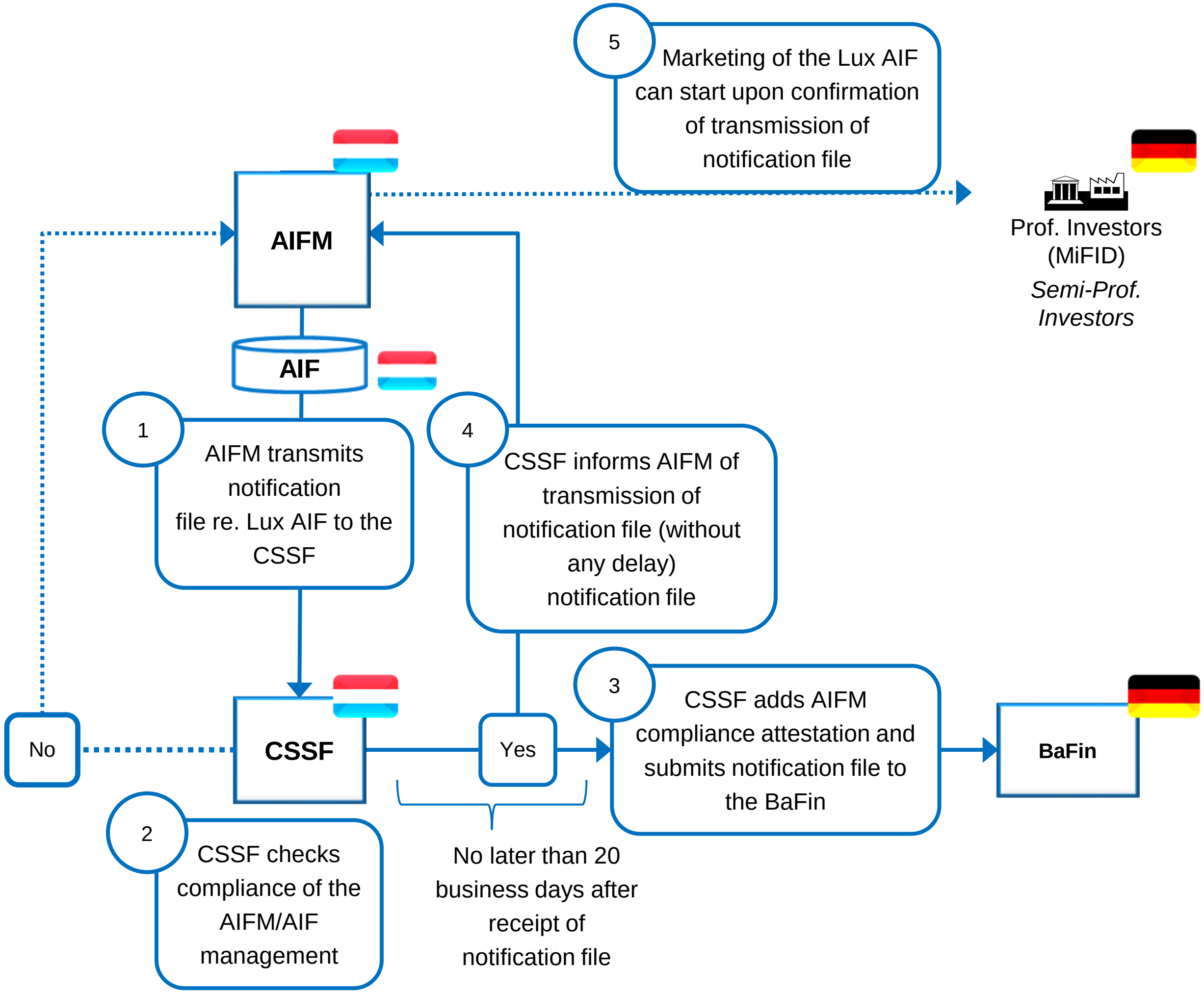
Reverse solicitation regulators’ definition	
Austria	😐
Belgium	😐
Denmark	😊
Finland	😊
France	😊
Germany	😐
Ireland	☹
Italy	☹
Luxembourg	😊
Portugal	😐
Spain	☹
Sweden	😐
The Netherlands	😐
United Kingdom	😊

😊 = Possible with clear definition by regulator

😐 = Possible but informal (no clear definition by regulator)

☹ = No guidance from regulator; to be used very carefully

EU AIFM Marketing Passport - Art. 32 AIFMD Notification process



- Process and content of the notification not as standardised as in the UCITS world
- Notification to be filed with the home country regulator of the AIFM (not of the AIF)
- Notification file per AIF
- Annex IV AIFMD incl. Art. 23(1)
- Procedures to set up with distributor(s) to avoid sale to non-professionals

NPPRs- Marketing under article 42 of the AIFMD (non EU AIFM)

Minimum conditions for marketing in the EU without passport:

- Cooperation agreements in place between the AIF, the AIFM country of domicile and the targeted country of distribution
- AIFM compliance with AIFMD transparency requirements (Art. 22 Annual report, Art. 23 reporting to investors, Art. 24 reporting to the regulators) and chapter XIII of the ESMA guidelines on remuneration policies
- AIFM notification of the acquisition of major holdings and control of non-listed companies (Art. 26 and 27 AIFMD)
- The AIFM and the AIF are not established in a country listed as a Non-Cooperative Country and Territory by FATF

Performance of an authorization/notification procedure

Maintenance of registration with payment of regulators' fees

NPPRs- Marketing under article 42 of the AIFMD (non EU AIFM)

Art. 42 - national requirements

Updated as of September 2018

Member State	Approval / Notification	Regulator timeframe applicable to process the application	Start of marketing	Regulator fees	
				Registration fee	Maintenance fee
Austria	Authorization procedure (FMA)	Up to 4 months	After approval is granted	EUR 4,500 per AIF and EUR 1,100 per add. sub-fund	EUR 2,500 per AIF and EUR 600 per add. sub-fund
Belgium	Authorization procedure (FSMA)	No time period (in practice about 5 weeks)	After approval is granted	None	None
Denmark	Authorization procedure (Danish FSA)	Up to 3 months	After approval is granted	None	DKK 3,770 per AIF
Finland	Authorization procedure (Finnish FSA)	No time period	After approval is granted	EUR 2,600 per AIF	None
France	Authorization procedure (AMF)	Up to 2 months	After approval is granted	EUR 2,000 per AIF/sub-fund	EUR 2,000 per AIF/ per sub-fund
Germany	Authorization procedure (BaFin)	From 2 to 4 months	After approval is granted	EUR 1, 545 per AIF / sub-fund	EUR 1,270 per AIF/ sub-fund
Ireland	Notification procedure (CBI)	Not applicable	Upon notification	None	None
Italy	Not possible (waiting for passport extension)	Not applicable	Not applicable	Not applicable	Not applicable
Luxembourg	Notification procedure (CSSF)	Not applicable	Upon notification	EUR 2,650 per AIF or EUR 5,000 in case of an umbrella structure	EUR 2,650 per AIF or EUR 5,000 in case of an umbrella structure
Netherlands	Notification procedure (AFM)	Not applicable	Upon notification	None	None
Norway	Authorization procedure (Norwegian FSA)	No official time period	After approval is granted	None	None
Portugal	Authorization procedure (CMMV)	Up to 30 days	After approval is granted	None	None
Spain	Authorization procedure (CNMV)	No official time period	After approval is granted	EUR 2,500 per AIF/sub-fund	EUR 3,000 per AIF/sub-fund
Sweden	Authorization procedure (Swedish FSA)	Up to 3 months (3 weeks in practice)	After approval is granted	SEK 22,000 per AIF/sub-fund	None
UK	Notification procedure (FCA)	Not applicable	Upon notification	GBP 250 per AIF	GBP 345 per AIF

NPPRs- Marketing under article 42 of the AIFMD (non EU AIFM) – Zoom on some countries specific requirements

Austria:

- Confirmation from home state authority of compliance with Austrian law + AIFMD
- Appointment of legal representative
- Depositary must fulfill all requirements of the AIFMD
- Regulator fees: 4 500 euros + 1 100 euros per sub-fund (one-off fee) and 2 500 euros + 600 euros per sub-fund (maintenance fees)

France:

- Depositary must fulfill all requirements of the AIFMD
- Regulator fees: 2 000 euros per AIF + 2 000 euros per additional sub-fund (one-off fee) and 2 000 euros per AIF + 2 000 per additional sub-fund (maintenance fees)

Germany:

- Depositary must fulfill all requirements of the AIFMD, but only in case where semi-professional investors are targeted
- “Lite” depositary requirements applicable in case professional investors only are targeted
- Regulator fees: 1.545 euros per AIF / sub-fund (one-off fee) and 1.270 euros per AIF / sub-fund (maintenance fees)

Regulator fees and time to market
– Article 32 (Passport) vs Article 42 (NPPR)

EEA Member State	EEA Member State Regulator	Art 32 AIFMD / Marketing Passport		Art 42 AIFMD / NDPR		Marketing approval
		Registration fees	Annual Maintenance Fees	Registration fees	Annual Maintenance fees	Non EEA Authorised AIFM (Art 32)
Austria	FMA	EUR 1100+ EUR 220 per subfund (from 2nd)	EUR 600 + EUR 200 per sub-fund (from 2nd)	EUR 4500 + EUR 1100 per sub-fund (from 2nd)	EUR 2500 + EUR 600 per sub-fund (from 2nd)	Max 4 months (but difficult to obtain)
Belgium	FSMA	None	None	None	None	About 5 weeks
Denmark	Danish FSA	None	DKK 4980 per AIF/ compartiment	None	DKK 3770 per AIF	Max 3 months
Finland	Finnish FSA	EUR 1600 per AIF	None	EUR 2600 per AIF	None	About 1-2 months
France	AMF	EUR 2000 per sub-fund	EUR 2000 per sub-fund	EUR 2000 per AIF/ sub-fund	EUR 2000 per AIF/ sub-fund (from 2nd)	Max 2 months (but difficult to obtain)
Germany	BaFin	EUR 435 per fund/sub-fund	EUR 290 per fund/sub-fund	EUR 1545	EUR 1270	About 2 to 4 months
Ireland	CBI	None	None	None	None	About 5 business days
Italy	Consob	None	EUR 4000 + EUR 1820 per sub-fund	Not applicable	Not applicable	Not applicable
Luxembourg	CSSF	EUR 2650 per single fund/ EUR 5000 per umbrella fund	EUR 2600 per sungle fund/ EUR 5000 per umbrella fund	EUR 2650 per AIF / EUR 5000 per umbrella fund	EUR 2650 per AIF / EUR 5000 per umbrella fund	Upon filing
Netherlands	AFM	None	None	None	None	Upon filing
Norway	Norwegian FSA	None	None	None	None	About 1-2 months
Portugal	CMVM	EUR 5000 per AIF	EUR 1500 per year (monthly payment)	None	None	Max 30 days
Spain	CNMV	EUR 2500 per AIF/sub-fund	EUR 3000 per AIF/ sub-fund	EUR 2500 per AIF/ sub-fund	EUR 3000 per AIF/ sub-fund	No specific time frame
Sweden	Swedish FSA	None	None	SEK 22000 per AIF/ sub-fund	None	Max 3 months
United Kingdom	FCA	None	None	GBP 250 per AIF	GBP 345 per AIF	Upon Filing

WHO ARE ELIGIBLE EU INVESTORS?

Who are eligible EU investors?

Two categories of professional investors are foreseen by **Annex II of the MiFID:**
"per se" professionals and professionals "on request" ➔ Eligible EU investors !

Per se professional investors are:

- A firm that is authorized by a European supervisory authority to operate in the financial markets, including banks, investment firms, funds and their managers, pension funds and their managers, insurance companies, commodity and commodity derivatives dealers;
- An institutional investor that does not fall within category (a), the main activity of which is to invest in financial instruments, including special purpose vehicles used in securitizations or other financing transactions;
- A national or regional government or a public body that manages public debt at national or regional level; or
- Large undertakings fulfilling at least two out of three criteria of scale (balance sheet total: EUR 20 million, net turnover: EUR 40 million; own funds: EUR 2 million

What falls under « professional » will again depend on local interpretation:

- In Luxembourg, a bank acting as a discretionary portfolio manager for a retail client will be considered as the « professional » investor, in Germany this will not be the case
- Foundations, churches, family offices, NGOs, UHNWI… are not professionals per se

Who are eligible EU investors?

Professionals « on request » are other investors that ask to be treated as professionals. This is acceptable under strict conditions only:

Request from investor to “opt-in” to professional status

Assessment made by the manager of the investor’s capacity of making its own investment decisions and understanding the risks involved with regard to the transactions or services envisaged.

The investor needs to fulfill at minimum two out of three quantitative criteria

- an average of 10 transactions per quarter over the last 4 quarters;
- a financial instrument portfolio of more than EUR 500,000;
- work in the financial sector in a professional position for at least one year requiring knowledge of the services or transactions envisaged

Who are eligible EU investors?

All other investors are considered « retail » investors

Certain countries have introduced the concept of « well- informed », « qualified », « semi-professional » etc… investors and allow that AIFs be sold to them (sometimes even via passport), but in many other a registration according to art 43 AIFMD would be required (if possible in the targeted country);

In any case **Regulation** on **Packaged Retail** and **Insurance-based Investment Products (PRIIPS)** entered into force last January 2018 will apply (as soon as a PRIIP is sold to a retail investor within the territory of the EU).

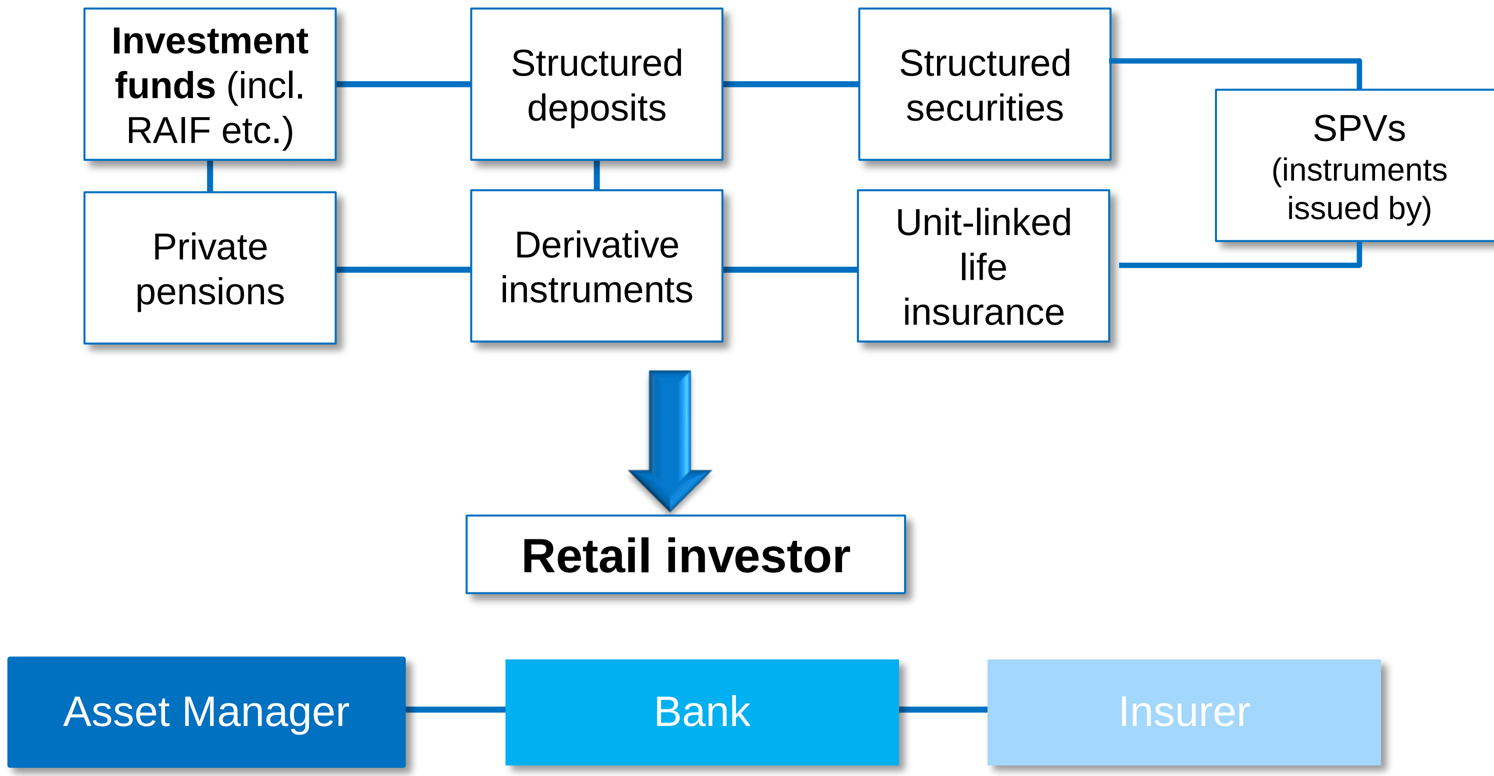
Who are eligible EU investors? Focus on PRIIPS

Scope?

Any packaged product, such as (non-exhaustive):

Sold to:

By any type of:



REPORTING OBLIGATIONS

Focus on AIFMD reporting requirements

Marketing passport or NPPRs entails the obligation for periodic reporting to the regulator of the marketing country according to Art. 24 (1) (2) and (4) of the AIFMD

What information to report?

- defined in the Annex IV of the AIFM Regulation No. 231/2013
- depending on the complexity of the non EU-AIFM structure, AuM and type of AIFs marketed
- information concerning the general profile description of both the non-EU AIFM and AIFs marketed
- in-depth portfolio data (markets exposures, type of instruments, risk metrics, borrowings, liquidity, etc.)

When to start the reporting and how often?

- Start of reporting period: determined by the regulator of each marketing country (e.g. the date of the Art. 42 filing form as provided to CSSF in Luxembourg, i.e. the first day of the following quarter)
- Reporting frequency: annual, semi-annual or quarterly, depending on total AuM and use of leverage, and type of AIFs in scope for reporting.
- Reporting period always aligned with the last business day of March, June, September and December of each year
- Reports must be filed under XML format with the regulator no later than one month after the end of the reporting period (15 days later for fund of funds)

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Focus on AIFMD reporting requirements - How to report

Case of a EU AIFM

EU AIFM *reports* Home Member State

Case of a non-EU AIFM

Non-EU AIFM *reports*

Country 1

Country 2

…

Country n

Depending on the target country, the filing must be made under XML and sent through secured FTP, web portal with manual upload, web portal with XML upload, simple email, split per articles or as a whole, zipped with encryption (or not) which requires local electronic certificates

Session II

Distribution of Alternative Investment Funds in the EU

- Description of the European and Asian fund products distribution
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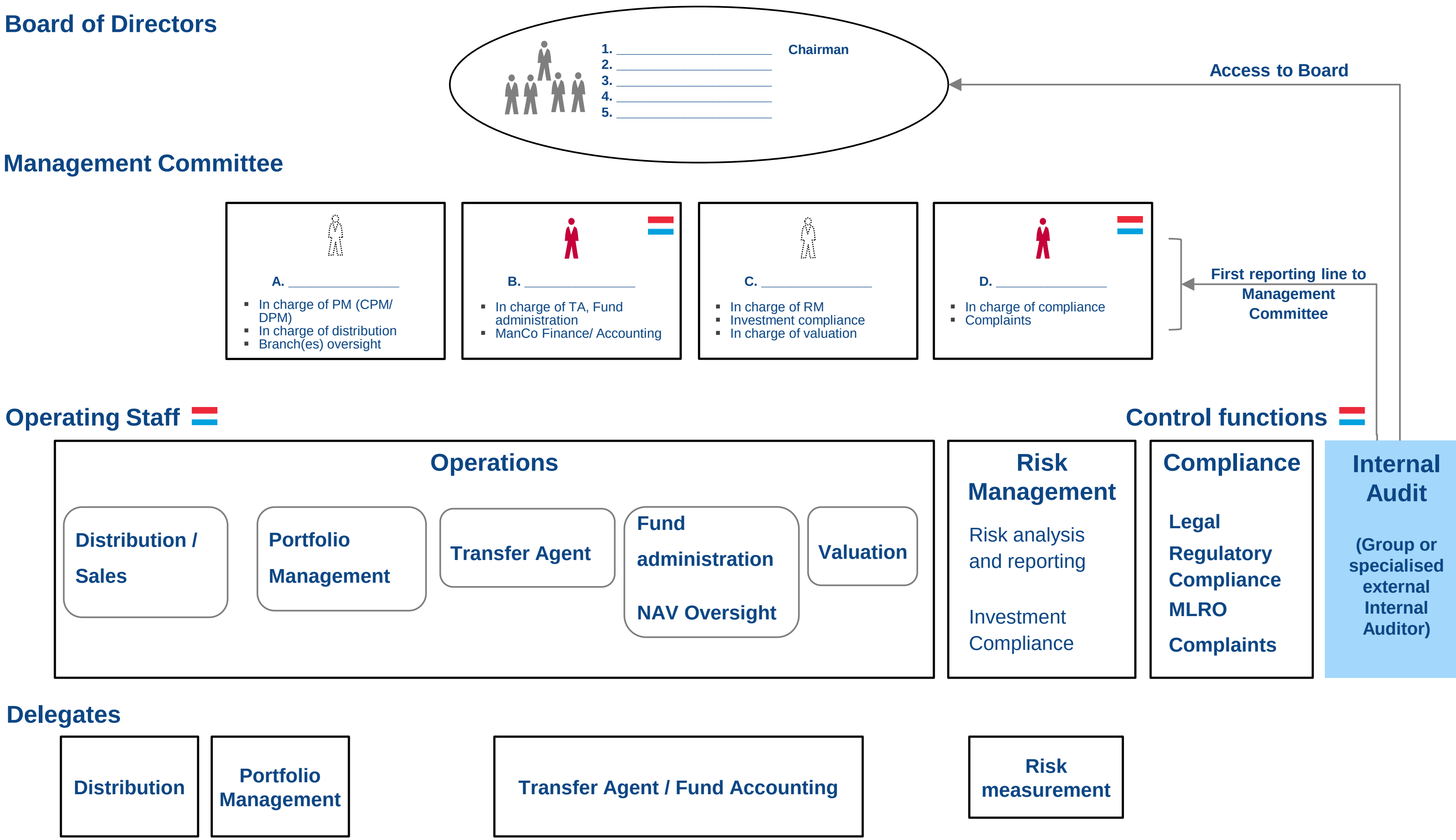
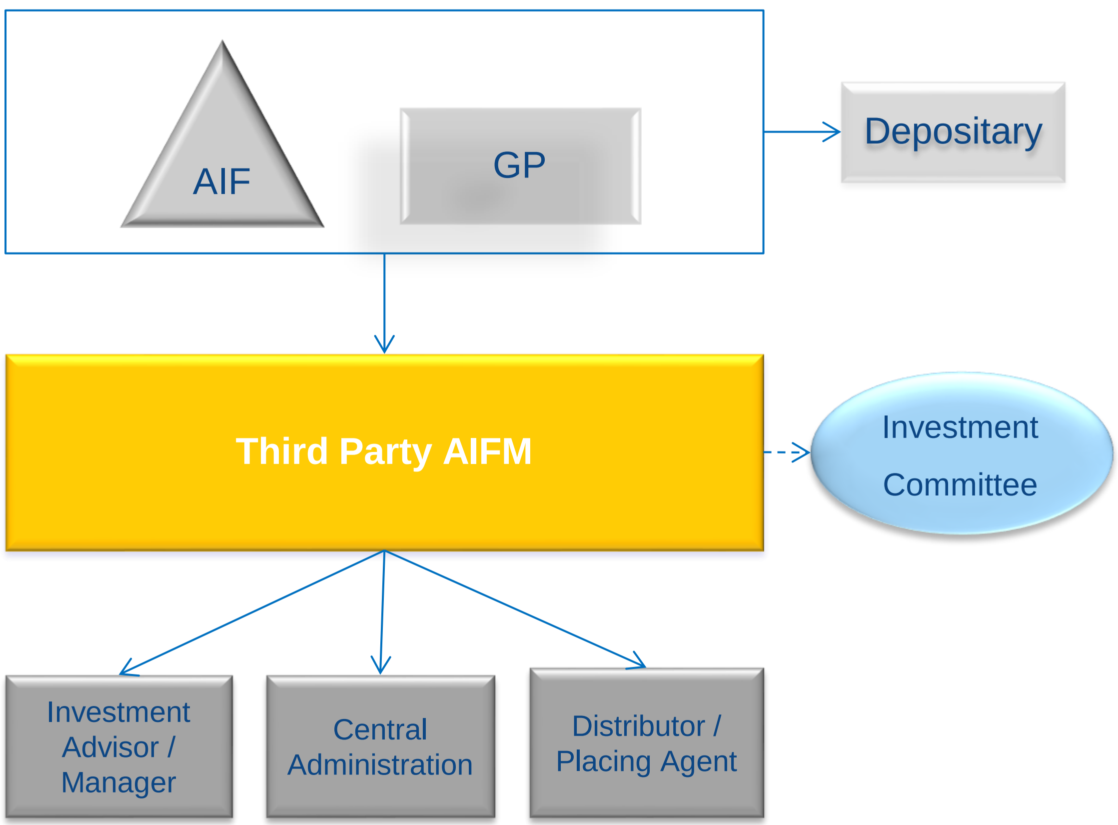
Setting-up of own AIFM



Appointment of a third-party AIFM



+ **Time to market**
+ Established **processes**
+ No **substance** issue
+ No **staff** to recruit

- **Cost** of an additional service provider
- Third party AIFM to be included in the **investment process**
- Involvement of the AIFM in the **distribution/sales**

Session III

UCITS and AIFMD Legal & Regulatory Updates

- Luxembourg Compliance Requirement
- Brexit
- UCITS & AIFMD, China Access Channels and Strategies

Session III

UCITS and AIFMD Legal & Regulatory Updates

- Luxembourg Compliance Requirement
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Compliance required

- GDPR
- MiFID II
- PRIIPs
- Benchmarks Regulation
- Luxembourg substance requirements

General Data Protection Regulation

- **General Data Protection Regulation (GDPR)**
  - ✓ Compliance by 25 May 2018
  - ✓ Directly applicable by EU Member States

- **Objective**
  - ✓ Protection of EU citizens' personal data

- **Impact**
  - ✓ UCITS, AIFs, UCITS management companies and AIFMs
  - ✓ Data processing agreements
  - ✓ Client consent
  - ✓ Record keeping

MiFID II

- **Directive on Markets in Financial Instruments**
  - ✓ Compliance by 1 Jan 2018
  - ✓ Implementation by Member States required

- **Objective**
  - ✓ Amending existing provisions on authorisation, conduct of business and organisational requirements for providers of investment services

- **Impact**
  - ✓ UCITS management companies and AIFMs authorised to perform MiFID activities
  - ✓ Indirect impact for investment funds, UCITS management companies and AIFMs regarding target market, inducements and research costs

PRIIPs

- **Regulation on key information documents for packaged retail and insurance-based investment products (PRIIPs)**
  - ✓ Compliance by 1 Jan 2018
  - ✓ Directly applicable by EU Member States

- **Objective**
  - ✓ Introduction of a new, pre-contractual disclosure document (key information document or KID) for retail consumers, considering buying investment products referred to as PRIIPs

- **Impact**
  - ✓ AIFs sold to retail investors as defined in MiFID II
  - ✓ UCITS (eventually as per 1 Jan 2020)

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Benchmarks Regulation

- **Benchmarks Regulation (BMR)**
  - ✓ Compliance by 1 Jan 2018
  - ✓ Directly applicable by EU Member States

- **Objective**
  - ✓ Ensuring that benchmarks are calculated in a fair and transparent way and are immune to manipulation

- **Impact**
  - ✓ UCITS and UCITS management companies (i) tracking the return of an index (or indices), or (ii) defining the asset allocation of a portfolio by reference to an index (or indices), or (iii) calculating the performance fees base on an index (or indices)

Luxembourg substance requirements

- **CSSF Circular 18/698 on substance requirements of fund management companies in Luxembourg**
  - ✓ Published on 23 August 2018
  - ✓ Entering into force with immediate effect
  - ✓ Repealing and replacing CSSF Circular 12/546 on substance requirements for Chapter 15 ManCos

- **Objective**
  - ✓ To set out in one single document all substance related aspects concerning both UCITS management companies and AIFMs

- **Impact**
  - ✓ Investment fund managers governed by Luxembourg law (Chapter 15 ManCos, Chapter 16 ManCos, AIFMs, self-managed investment funds)

Session III

UCITS and AIFMD Legal & Regulatory Updates

- Luxembourg Compliance Requirement
- Brexit
- UCITS & AIFMD China Access Channels and Strategies

Brexit

- **Revised version of the draft Withdrawal Agreement and Political Declaration**
  - ✓ 585 pages-long Withdrawal Agreement to be approved by EU Summit on 25 November 2018, then by the UK Parliament by the end of the year

- **Memorandum of Understanding between EU and UK**
  - ✓ ESMA seeking authority from the EU Commission to negotiate MoU on behalf of the EU Member States
  - ✓ Contingency planning in case ESMA initiative fails

- **Impact**
  - ✓ All market players with UK ties relying on EU passports
  - ✓ Fund distribution and delegation to UK manager

Session III

UCITS and AIFMD Legal & Regulatory Updates

- Luxembourg Compliance Requirement
- Brexit
- UCITS & AIFMD China Access Channels and Strategies

Luxembourg UCITS funds

Chinese strategies in UCITS

→ 73% of European funds investing in PRC onshore assets are domiciled in Luxembourg

- Possibility to invest in / take exposure to a wide range of asset securities listed in Hong Kong, Singapore or securities traded on other regulated markets (such as **Dim Sum bonds** issued in Hong Kong or elsewhere), **A-Shares, A-Shares financial indices, RMB fixed income securities**, etc
- Possibility to use a **UCITS** with **QFII** license/quotas
- Possibility to use a **UCITS** structure with **R-QFII** license/quotas. Allocation of R-QFII quotas by managers based in **Hong Kong**, but also in the **UK, France, Germany, South-Korea, Taiwan, Singapore, Switzerland, Qatar, Australia, Canada, Malaysia, the UAE, Chile, Thailand, Hungary**, **Ireland**, the **United States** and **Luxembourg**
- Investments in **A-Shares** and listed **RMB bonds** on the **Shanghai Stock Exchange** and **Shenzhen Stock Exchanges** but also in **RMB fixed income** securities dealt with on the China **Interbank Bond Market (CIBM)**
- Possibility to use **Stock Connect** in a UCITS
- Possibility to use **CIBM Direct Access** in a UCITS
- Possibility to use **Bond Connect** in a UCITS

Luxembourg UCITS funds

Chinese strategies in UCITS

Three types of China Access Channels

- **License** and **quota** based CACs, **QFII** and **R-QFII**
- **Connect** based CACs, **Stock Connect** and **Bond Connect**
- **Authorization** based CAC, **CIBM Direct**

- **Common features** (non-fungible securities, closed-ended circuit, CNH-CNY Fx)
- **Preference for connect schemes** by mainstream asset managers

Luxembourg UCITS funds

Chinese strategies in UCITS

QFII and UCITS

- **Before 2012**, indirect investments in the PRC via p-Notes or other derivative instruments with China A-Shares or other PRC assets as underlying assets. Direct investments in the PRC were very limited
- Concerns over the liquidity of the China A Shares market and foreign exchange controls
- Reason of such limited access: QFII rules **not fully compatible with UCITS** rules since
  - (i) lock-up period of 1 year
  - (ii) monthly repatriations
  - (iii) regulatory approvals required prior to repatriations
  - (iv) other limitations

→ **Limitation to the exposure to PRC onshore assets to 35% of the NAV of the UCITS**

Luxembourg UCITS funds

Chinese strategies in UCITS

QFII and UCITS

- End of **December 2012**, new QFII rules Provisions on Foreign-Exchange Administration of Domestic Securities Investment by Qualified Foreign Institutional Investors

- Creation of the concept of Open-ended China funds, i.e. "open-ended securities investment funds that are established abroad in public offerings, with over 70 percent of the funds invested in China"

  (i) lock-up period of 3 months but possible specific arrangements

  (ii) weekly repatriations

  (iii) overall limit of 20% of the quota per month

→ **Requirement for 70% investment in the PRC capital markets removed**

→ **No limit in principle on exposure to PRC onshore assets for UCITS qualifying as QFII open-ended China funds**

Luxembourg UCITS funds

Chinese strategies in UCITS

QFII and UCITS

- In **February 2016**, a number of QFII rules were amended to improve the accessibility to the PRC capital account and promote cross-border investment
  - (i) USD200 million to USD5 billion quota awarded based on AUM
  - (ii) investment requirement within 6 months of quota approval
  - (iii) daily redemption of open-ended funds
- In **June 2018**, new QFII rules cancelled the 20% limits on outward remittance, removed lock-up period on principle repatriation and allowed the use of onshore FX derivative instruments.

→ **Greater convergence between QFII and R-QFII**

→ **Greater compatibility of QFII with UCITS**

→ **Merger QFII and R-QFII (?)**

Luxembourg UCITS funds

Chinese strategies in UCITS

R-QFII and UCITS

- R-QFII open ended funds (i) are not subject to a lock-up period, (ii) can proceed to daily repatriations and convert freely from RMB into any other currencies, and vice-versa within the limits of the R-QFII quota and (iii) are not subject to maximum repatriation amounts per month
- The compatibility with UCITS was not an issue, however, the possibility to delegate the portfolio management function and allow sub-managers to use their R-QFII quotas with a foreign fund structure was not clear until end of 2013
- R-QFII sub-management (delegation of portfolio management function to an R-QFII manager) model widely accepted
- Extension of the R-QFII regime to jurisdictions other than Hong Kong (including Luxembourg) and use of those R-QFII quotas with their UCITS and Luxembourg R-QFII quota used with Luxembourg UCITS and management companies

→ **Most UCITS managers willing to take an exposure to PRC onshore assets with their UCITS have been using R-QFII**

Luxembourg UCITS funds

Chinese strategies in UCITS

CIBM Direct Access and UCITS

- Available to fund managers since the Summer of 2016
- Delay in availability of application material and forms from the PBoC
- Regulator raised similar questions as for QFII/RQFII
- Specificities of the CIBM Direct Access (approval process, account opening structure, role of the PBoC, restrictions to repatriations) to cover in the application
- Approved in UCITS since end 2016

→ **UCITS managers have not embraced the CIBM Direct Access and preferred other available CACs such as QFII and R-QFII for their RMB fixed income allocations**

Luxembourg UCITS funds

Chinese strategies in UCITS

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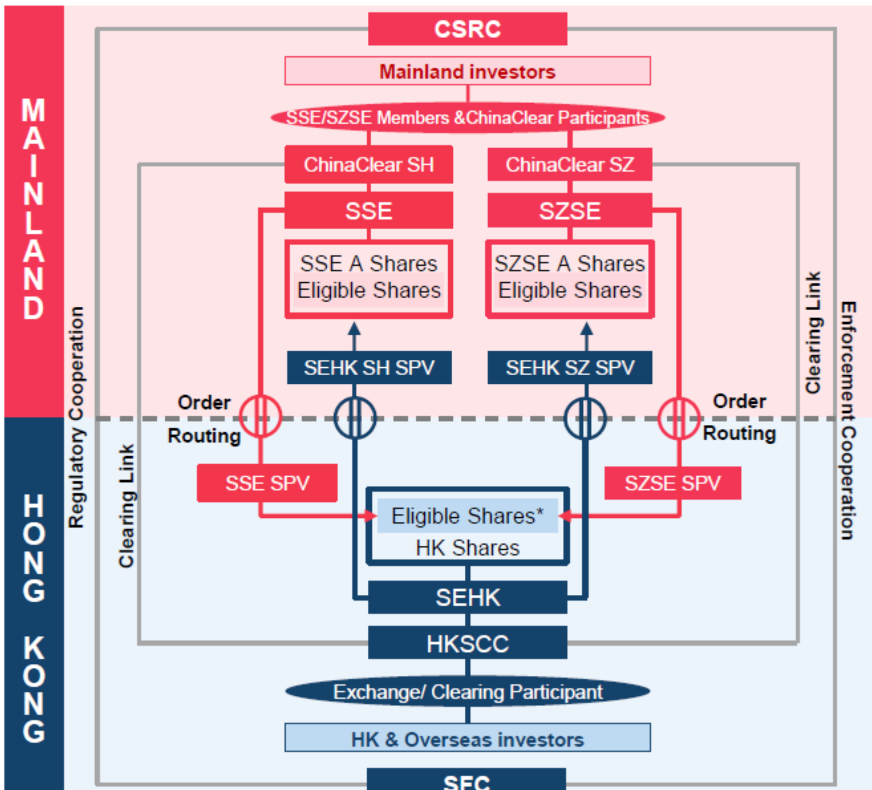
Stock Connect and UCITS

Stock Connect between the Hong Kong Stock Exchange and the Shanghai Stock Exchange launched in November 2014 and extended to Shenzhen Stock Exchange in December 2016



Source: HKEx Group

Innovative scheme involving the connection between the HKEx and the SSE and SZSE, through a platform operated by the HKEx and the HKSCC, connecting into their PRC counterparts.

Main discussion points from a regulatory point of view were on (i) the **beneficial ownership** of China A-Shares held through the HKSCC, (ii) the **segregation** of the assets held through the HKSCC, (iii) **risks over the counterparty** (i.e. the broker) during the settlement cycle, (iv) **recourse** of the involved parties in case of default of a market participant in HK or the PRC, (v) **pre-trade requirements** and other risks associated with the Stock Connect system and (vi) **disclosure** requirements.

Luxembourg UCITS funds

Chinese strategies in UCITS

Stock Connect and UCITS

→ **Questions of the regulator on beneficial ownership and segregations were addressed and although not a UCITS requirement as such, "Synthetic DvP" mechanisms developed by market players permitted to avoid the counterparty risk for the UCITS**

- Luxembourg UCITS were authorized to make use of Stock Connect as from **December 2014**, subject to certain conditions (i) stock Connect qualifies as regulated market for UCITS, (ii) proper segregation of assets throughout the custody chain, (iii) mitigated counterparty risk over the broker (no "free of payment"), (iv) proper disclosures in the prospectus and the KIID.

- According to the ALFI press release of **December 2016**, the Luxembourg UCITS, its management company (if any) and the depositary bank appointed by the fund must give due consideration to a number of factors and ensure that their risk management procedures adequately covering them. These factors include:

  (i) accounts opened by the depositary bank of the UCITS with a sub-custodian in Hong Kong are segregated

  (ii) the broker model involving Delivery Versus Payment settlement must be chosen in order to limit counterparty risk;

  (iii) the prospectus, and most particularly the KIID, will contain a specific disclosure to inform investors of the specific legal risks linked to compulsory requirements of the local CSDs, HKSCC and ChinaClear for custody of securities on a cross-border basis.

Luxembourg UCITS funds

Chinese strategies in UCITS

Stock Connect and UCITS

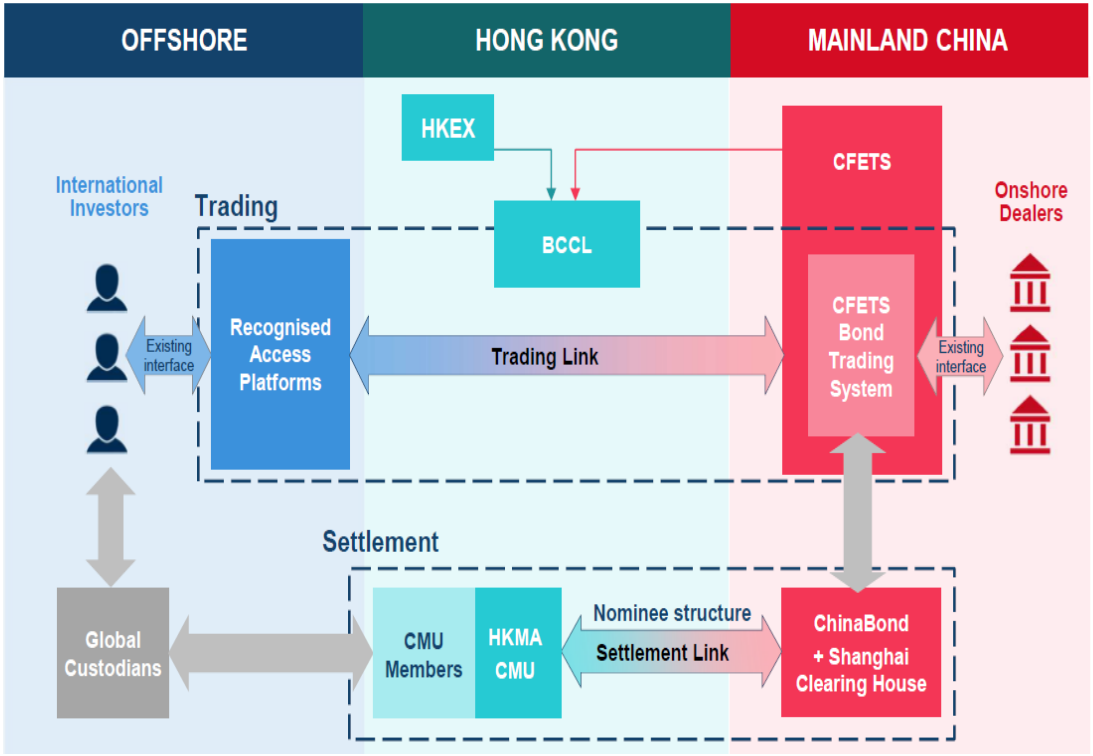
- Various brokers and sub-custody models available since 2014
- **Integrated (or TC) models** in 2014, synthetic DvP, one broker (limited volumes, best execution)
- SPSA introduced in 2015, **SPSA+** or other enhanced models available (still limited number of brokers)
- **SPSA with R-DvP** introducted in November 2017, full SPSA (up to 20 brokers)

Luxembourg UCITS funds

Chinese strategies in UCITS

Bond Connect and UCITS

Bond Connect was launched in July 2017 as an access platform organized by the Hong Kong Monetary Authority ("**HKMA**") and allowing participating institutions in Hong Kong to trade RMB fixed income securities dealt on the China Interbank Bond Market ("**CIBM**") directly from Hong Kong.



Source: BCCL

The architecture of Bond Connect is similar from legal perspective and involving the **connection between the HKMA CMU and the CIBM** through a platform operated by the HKMA and the BCCL, connecting into their PRC counterparts (CCDC and SCH).

BCCL playing a similar role as the HKSCC for Stock Connect.

R-DvP was expected on day one in Bond Connect.

No Pre-trade delivery and SPSA-type of segregation possible with the registration of the UCITS with the CFETS (and issuance of a CFETS ID).

Luxembourg UCITS funds

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Bond Connect and UCITS

- However, **R-DvP was not available** for bonds cleared through the CCDC, which triggered questions on the potential risk for a UCITS fund buying securities on Bond Connect (similar to Stock Connect when selling securities)
- Questions of the regulator were inspired from Stock Connect Main discussion points from a regulatory point of view were on (i) the **beneficial ownership** of the RMB Bonds held through the CMU, (ii) the **segregation** of the assets held through the CMU, (iii) **risks over the counterparty** (i.e. the broker) during the settlement cycle, (iv) **recourse** of the involved parties in case of default of a market participant in HK or the PRC, and (v**) disclosure requirements**.
- From 2017, the regulator approved UCITS willing to include Bond Connect in their prospectus provided that an Integrated Model be put in place or that Bond Connect is not used before the R-DvP be fully implemented, subject to additional conditions
- In **August 2018**, the full implementation of R-DvP has been announced and R-DvP is therefore available for Bond Connect dealings cleared through the CCDC and the SCH

Luxembourg UCITS funds

Chinese strategies in UCITS

Bond Connect and UCITS

- Possible to use Bond Connect in UCITS subject to disclosure in the prospectus and the KIID.
- Outstanding question resulting from the China State Council announcing a three-year exemption from withholding tax and VAT on interest payment for RMB bonds purchased through Bond Connect.
- Question as to whether the UCITS manager should provision any amounts for the payment of the tax should the exemption not be prolonged and the tax apply on RMB the duration/maturity of which would exceed the period of three years

Q&A

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Pierre Beissel

Partner, Arendt & Medernach S.A.
Private equity & Real estate
Tel : +352 40 78 78 262
Pierre.beissel@arendt.com

Catherine Rasseneur

Partner, Arendt Regulatory & Consulting
Tel : +352 40 78 78 7742
Catherine.rasseneur@arendt.com

Stephane Karolczuk

Partner, Arendt & Medernach S.A.
Investment Management
Tel : +852 2901 5808
Stephane.karolczuk@arendt.com

Gaëlle Schneider

Principal, Arendt
Tel : +352 40 78 78 294
Gaelle.schneider@arendt.com

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