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association of the
luxembourg fund industry

London, 10 May 2010

Workshop:

UCITS & NON UCITS Alternative Investment Strategies

Moderator: Claude Niedner, Partner, Arendt & Medernach
Nathalie Dogniez, Partner, KPMG

Alain Guérard, Executive Director, JPMorgan Bank Luxembourg SA

Claude Noesen, Managing Director, Prime Fund Solutions



Agenda

1. Key features of UCITS, UCI and SIF
2. Alternative investment strategies in UCI and SIF
3. Alternative investment strategies in UCITS
4. Regulatory developments at EU level: the AIFMD

1. Key features of UCITS, UCI and SIF

1.1 Large choice of available structures for implementing alternative strategies

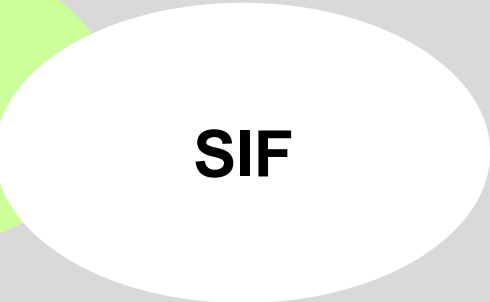
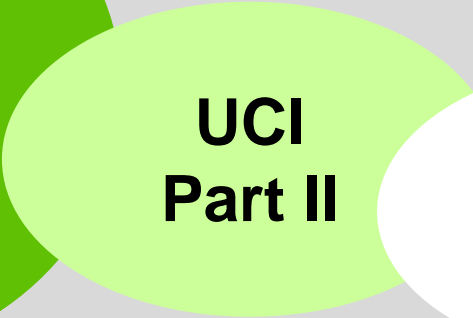
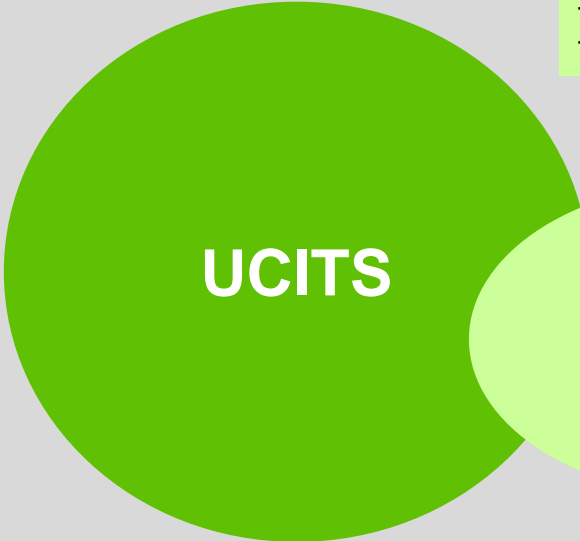


Regulation

- public distribution (retail + institutional investors)
- eligible asset classes only
- high level of regulation

- public distribution (retail + institutional investors) – no EU passport
- all asset classes
- medium level regulation

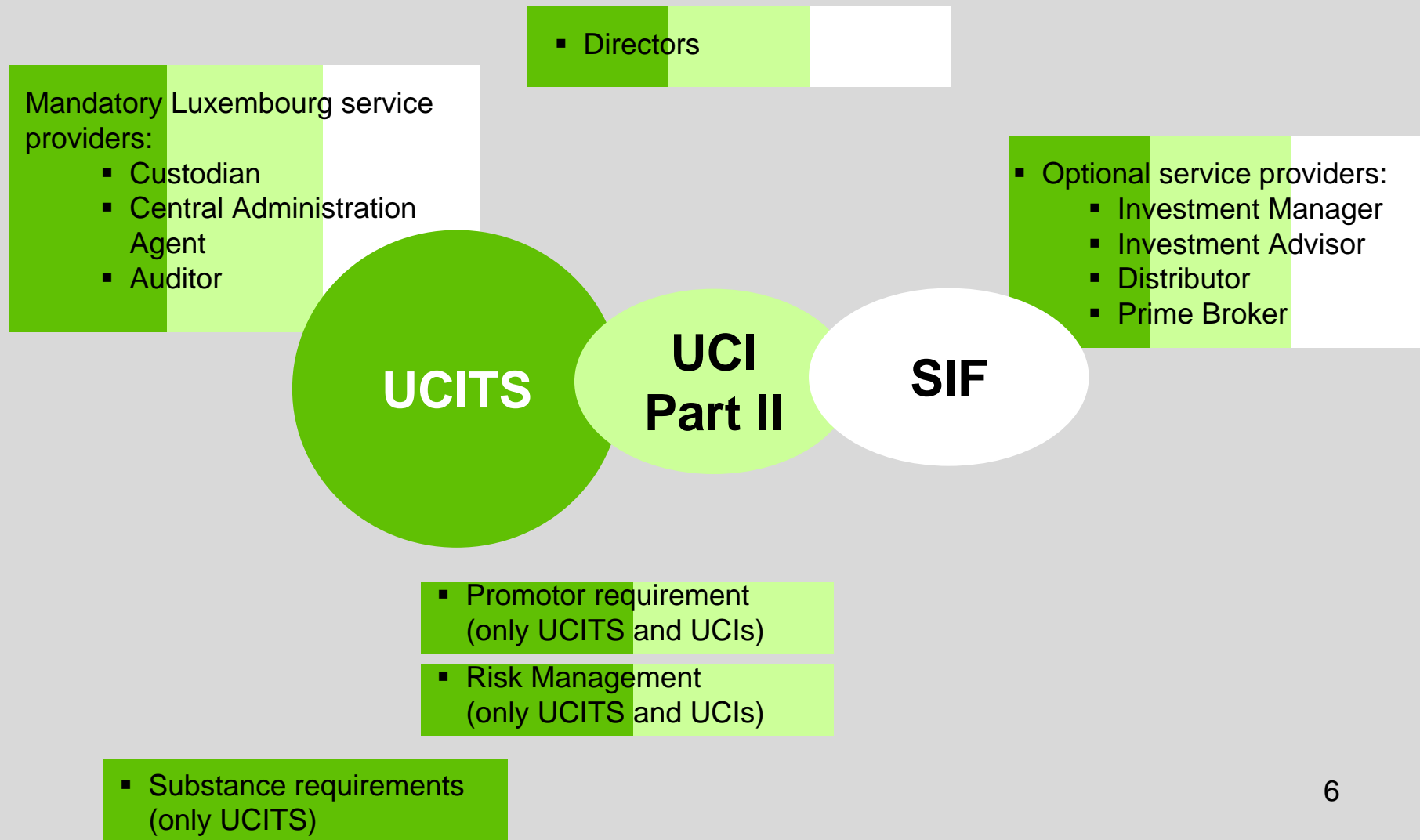
- qualifying investors only (institutional, professional, well-informed)
- all asset classes
- low / medium level regulation



Structuring - flexibility ⁵



1.2 Requirements for setting-up a UCITS, UCI or SIF



1.3 Governance

1. Substance aspects

- ManCo requirement (chapter 13) for FCP
- SICAV/SICAF may be self-managed or may appoint a ManCo
- Head office of SICAV/SICAF or ManCo in Luxembourg
- One of the two conducting persons of the ManCo or of the SICAV/SICAF must be in Luxembourg

2. Directors

- Directors subject to CSSF approval
- Directors must justify their repute + professional experience
- No residency requirement for directors

3. Investment Manager (IM)

- UCITS:
 - IM must be authorised or registered for the purpose of asset management
 - IM must be subject in its home country to prudential supervision
 - if located in a third country, cooperation agreement between CSSF and relevant supervisory authority
- UCI:
 - IM must be authorised or registered for the purpose of asset management
 - IM must be subject in its home country to equivalent prudential supervision or be part of a group subject to equivalent prudential supervision
- SIF - IM may be located abroad
 - in principle, IM not subject to regulatory approval or supervision in Luxembourg



1.4 Main requirements regarding Promotor

- Concept not defined by law, but used as an administrative practice
- Promotor = reputable professional who commits its name and reputation to the proper functioning of the fund to be created
- Promoter must:
 - have sufficient financial resources (otherwise co-promoter requirement)
 - be of sufficiently good repute
 - have sufficient experience in relation to the type of fund concerned
- Appointment of representatives of Promoter at board level



1.5 Main requirements regarding the relationship Custodian / Prime Broker

- Prime Broker appointment
 - Tripartite agreement Fund-Custodian-Prime Broker
 - Bipartite agreement Fund- Prime Broker + side-letter Custodian
 - Possibility to use UK or US Prime Brokerage contracting entities

- Relationship between the Custodian and Prime Broker
 - PB safekeeps assets of the Fund under the supervision of Custodian
 - PB executes transactions and compensation operations for the Fund
 - Intervention PB in margin deposits
 - PB sets credit lines in order to finance any deficit
 - Intervention PB in lending, borrowings or pensioning securities
 - PB effects day-to-day administration of FCPs



1.5 Main requirements regarding the relationship Custodian / Prime Broker

▪ Role of the Custodian

- Operational due diligence necessary (initiation and ongoing)
- Organisation: access on-line + ongoing communication PB/Custodian
- Oversight activities:
 - Supervision of the assets
 - Daily review of the portfolio (including rehypothecation level)
 - Control of cash flow out of PB trading A/C
 - Review of risk report

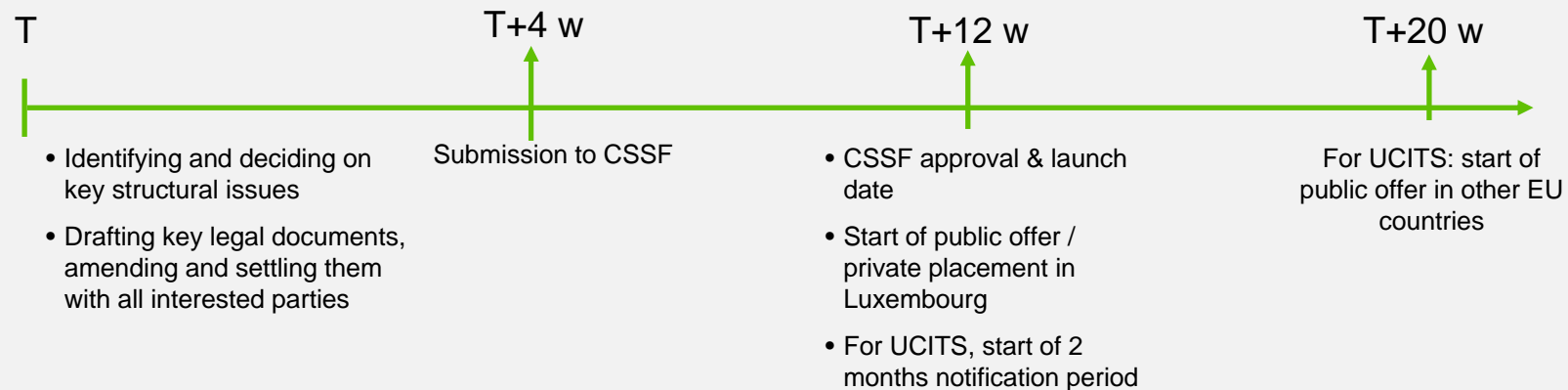
▪ Prime Brokerage Agreement

- Detailed description in the Prospectus
- PBA submitted to CSSF: typically no comments
- Description information flows with the custodian for CSSF
- Limitation of the counterparty risk (+ margin deposit)

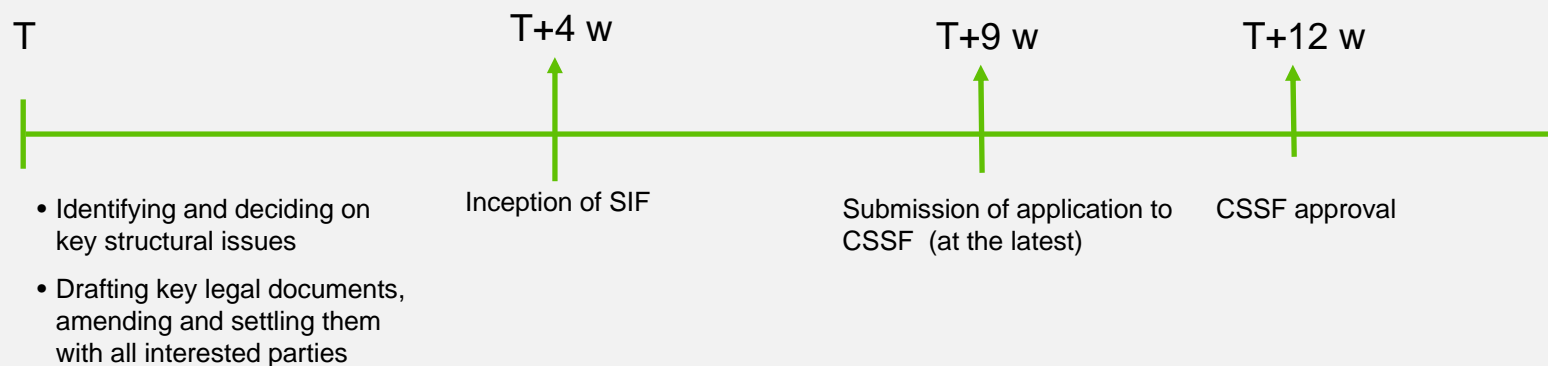


1.6 Regulatory approval process

UCITS and UCI



SIF



Although a SIF may be launched prior to CSSF approval, it is usually recommended to submit the term sheet to the CSSF before launch to determine whether the CSSF has any substantial issues.

1.7 Investment strategies and restrictions

UCITS	UCI	SIF
<ul style="list-style-type: none"> ▪ Art. 41 and following of 2002 Law ▪ CESR Guidelines ▪ Grand-Ducal Regulation of 8 February 2008 ▪ Eligible assets: <ul style="list-style-type: none"> ▪ Transferable securities and structured financial instruments ▪ Money market instruments ▪ Units of UCITS and other eligible UCIs ▪ Deposits with credit institutions ▪ Financial derivative instruments based on eligible underlying assets 	<ul style="list-style-type: none"> ▪ No limitation regarding eligible assets and investment strategies 	<ul style="list-style-type: none"> ▪ No limitation regarding eligible assets and investment strategies

2. Alternative investment strategies in UCI and SIF



2.1 UCI and SIF in numbers: General figures

	Number of funds	Net assets (Eur bn)
Part II (2002 Law)	649	220.250
SIF	989	163.425

Source: ALFI/CSSF (figures as of January 2010)

2.2 UCI and SIF in numbers: Hedge Funds and Fund of Hedge Funds



Number of hedge funds by legal status

		<i>Domiciled & Administered</i>	
		Funds	%
GLOBAL		120	100
of which :	<i>Part II (law 2002)</i>	73	60,8
	<i>SIF</i>	47	39,2

Number of funds of hedge funds by legal status

		<i>Domiciled & Administered</i>	
		Funds	%
GLOBAL		242	100
of which :	<i>Part II (law 2002)</i>	157	64,9
	<i>SIF</i>	85	35,1

(ALFI Survey 06/09)

2.3 Flexible structuring possibilities in a SIF

Large choice of legal forms

- Examples of corporate forms:
 - Partnership limited by shares (SCA) – control over management
 - Public limited company (SA) – flexible corporate governance rules
 - Private limited company (Sàrl) – for partners with a significant personal link
- Contractual form:
 - FCP – no legal personality; managed by a ManCo; control over management

Light reporting requirements

- No legally defined content of issue document;
- Annual report within 6 months after financial year end
- No semi-annual report
- No publication of NAV

Rules of operation

- Issues and redemptions according to constitutive documents
- Valuation on the basis of “fair value”
- Minimum capital to be reached within 12 months

2.4 UCI and SIF: Possible investment strategies

- Large variety of investment strategies
 - Hedge Fund
 - Fund of Hedge Funds
 - Real Estate
 - Venture capital/Private Equity
 - Exotic funds (e.g. art, wine, luxury goods)
 - Socially responsible fund
 - Microfinance
 - Natural resources, Energy

2.5 UCI and SIF: Investment restrictions

UCI	SIF
<ul style="list-style-type: none"> ▪ Risk diversification rules (10% rules) ▪ Rules relating to Funds of Funds: in principle, no more than 20% in the same target UCI, except if : <ul style="list-style-type: none"> ▪ target UCI is open-ended UCI with risk spreading rules similar to those existing for Part II UCI and ▪ target UCI is subject to regulatory supervision 	<ul style="list-style-type: none"> ▪ Principle based risk diversification rules (CSSF Circular 07/309): <ul style="list-style-type: none"> ▪ No more than 30% in securities of the same kind issued by the same issuer ▪ Exception for investments in securities e.g. issued or guaranteed by OECD Member State ▪ Exception for investment in other UCI with similar risk spreading requirements ▪ Rules relating to Funds of Funds: in principle, 30% rule applies

2.6 UCI and SIF: Master Feeder structures

UCI	SIF
<ul style="list-style-type: none"> ▪ Master-Feeder: traditionally, master and feeder must be established in Luxembourg ▪ On a case by case basis: Luxembourg feeder may invest in foreign regulated master, if: <ul style="list-style-type: none"> ▪ foreign master subject to risk diversification requirements at least equivalent to the risk diversification requirements to which Luxembourg retail funds are subject and ▪ custodian of the Luxembourg feeder is granted access to the systems of the custodian of the foreign master fund 	<ul style="list-style-type: none"> ▪ Luxembourg feeder may invest in foreign master (even unregulated), if: <ul style="list-style-type: none"> ▪ foreign master subject to risk diversification requirements at least equivalent to the risk diversification requirements to which Luxembourg SIF are subject (30% rule)



2.7 Examples of alternative investment strategies in a SIF

- Investment in diverse alpha sources with low or negative correlations with each other
- mix of alpha sources rebalanced periodically / mix may change over time
- alpha sources include:
 - market neutral equity strategies
 - market neutral fixed income strategies
 - currency overlay
 - active asset allocation overlay
 - long-only equity strategies
 - short equity index future positions
 - swap positions
- risk diversification:
 - exposure to at least 4 alpha streams
 - cash exposure to any single alpha stream < 30% of the market value of portfolio
 - notional exposure of a single alpha stream may > 30% of the market value of portfolio
- leverage:
 - gross market exposure may > 100% of the value of the portfolio (through use of derivatives + short positions)
 - net exposure is market neutral over the long term

3. Alternative investment strategies in UCITS

3.1 Alternative investment strategies in UCITS – why?

Press releases



Ucits hedge vehicles to flood sector

News analysis
Providers intend to launch despite higher costs and lower returns, says Steve Johnson

A wave of investment vehicles targeting the new breed of "onshore hedge funds" is set to be launched in 2010 – despite even their sponsors believing they will have lower returns and higher costs than funds already on the market. Some 80 per cent of established fund of hedge fund providers intend to launch similar collective vehicles investing in a basket of "UCITS-compliant hedge fund" products in the next 12 months, according to a survey by London-based K&K Asset Management.

The move comes after a host of leading hedge fund houses, such as Man Group, Brevan Howard, GLG Partners and Marshall Wace, have created onshore, regulated UCITS funds, dubbed "Newcits", in response to investor demands for greater protection and regulation.

However, more than 90 per cent of fund of funds believe these Newcits vehicles will have lower returns

than their equivalent offshore versions, according to the K&K survey, with a quarter expecting the shortfall to be greater than 3 percentage points a year.

This shortfall is expected because UCITS hedge funds face restrictions on levels of leverage, are prohibited from making direct investments in commodities or physically shorting stock and must provide fortnightly liquidity, restricting their ability to invest in illiquid assets.

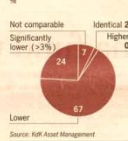
Further, almost 80 per cent of the respondents said the cost of investing in the underlying UCITS hedge funds – as expressed by the total expense ratio, the broadest measure of cost – was likely to be higher than that of investing in traditional offshore funds. These charges are passed on to fund of funds investors.

K&K said most of the Newcits launched to date had retained the "2 and 20" fee structure, comprising a 2 per cent annual fee and 20 per cent performance levy, commonplace in the offshore world, while administration and custody costs were likely to be higher for onshore funds.

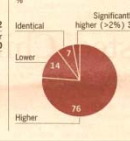
Most of the respondents consider that the performance of the UCITS hedge funds is likely to be lower than the offshore funds and



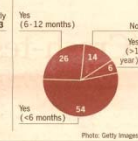
How will the performance of a UCITS hedge fund compare to its sister offshore fund?



How will the total expense ratio of a UCITS HF compare to its offshore equivalent?



Do you plan to launch a fund of UCITS hedge funds?



that their TER is likely to be higher," said Henrik de Rooy, co-founder of K&K. "They are probably going to be less attractive or have a worse risk/return ratio than a traditional fund of fund. But UCITS has lots of advantages in terms of distribution."

The fund of funds industry believes the biggest selling points for these UCITS vehicles will be access to retail investors, who are generally wary of offshore funds, and better liquidity terms, which stop managers

of the underlying funds from limiting redemptions by imposing suspensions, gates and sidepockets, a scourge that has afflicted the hedge fund industry in the past two years.

Managers also laud the improved regulatory oversight, transparency and risk management of the UCITS world.

Three-quarters of fund of funds houses said they had had demand from both retail networks and fund platforms or distributors for UCITS vehicles. Around two-

thirds had demand from family offices and wealthy individuals and almost half from institutional investors and insurance companies.

HSBC, Collins Stewart and the Fund Management, Switzerland's SA, Parnal Group, and Kairos Partners of Milan have launched funds of Newcits in recent months.

More than half of the houses surveyed by K&K said they intended to follow suit within six months, and a further quarter within a year.

Questions linger over Ucits hedge offerings

Talking head
NOEL AMENC and SAMUEL SENDER

Many hedge fund strategies will soon be offered via regulated funds structured as European UCITS. Changes in UCITS regulation have made this possible. A muddled political agenda and an unfinished directive on alternative investment fund managers (AIFM) will encourage hedge funds to take advantage of this leeway.

As part of a recent study, supported by Caevis, Edhec-Risk canvassed managers of UCITS and alternative assets, their service providers, external observers such as regulators and trade bodies, as well as buyers of funds, for their views on the structuring of hedge fund strategies as UCITS.

professionals, representing assets under management of around €13,000bn (£11,300bn, \$15,270bn), responded to the survey.

The managers of alternative funds report that the uncertainties in the AIFM directive make any investment in compliance risky and are an argument for structuring their strategies as UCITS. An offshore hedge fund that relocates to Europe to benefit from the passport directive will find itself in a bind: the directive is never passed.

Professional investors say they will push for UCITS structuring because they are hamstrung by quantitative restrictions that prevent them from investing freely in alternative funds but allow investment in UCITS funds. UCITS are though

funds in each strategy already meet the risk requirements for UCITS, as measured by value at risk (VaR – the risk of loss on a specific portfolio).

Although the recent crisis has cast doubt on the reliability of VaR numbers, they were once a useful selection criterion:

Respondents to the survey fear that strategies into UCITS will lower returns

in crises before 2008, high-VaR hedge funds were more likely to implode. In 2008, the crisis hit high- and low-VaR hedge funds indiscriminately.

illiquid securities as well as any non-financial assets; they will need to diversify their assets and limit counterparty risk arising from derivatives instruments.

In addition, because UCITS funds cannot borrow more than 10 per cent of the value of their assets and are forbidden from engaging in naked short sales, they will use derivatives instruments to short securities. Where alternative funds only face the cost of borrowing securities, UCITS funds will use a product whose cost includes a margin on top of the cost of borrowing securities faced by the broker.

Respondents to the survey fear that turning hedge funds into UCITS

premium cannot be fully accessed by UCITS. Funds will also be required to take on a depositary whose due diligence requirements will increase the cost of services provided to UCITS.

In addition to the normal cost of using derivatives, the more hedge funds structured as UCITS there are, the more expensive shorting may become.

Last, heavily regulated UCITS are attractive, as they may enable professional investors to reduce the risk of operational losses caused by the likes of Madoff or Lehman. Operational risks from hedge fund strategies, however, are transferred either to depositaries or to asset managers.

longer do a deep analysis of the risks of investing in hedge funds, a false sense of security; adverse selection and moral hazard are thus more likely. This foisting off of risk and responsibility will also come with a cost to the asset management industry. Clear contracts can help define responsibilities for operational risks and assign responsibilities properly. But for the liability for non-financial risks to be shared effectively, asset management companies, depositaries and other actors in the investment industry's value chain must be efficient and not yet

Plan for Ucits with hedge fund strategies

Trends
Schroders new range is evidence of a convergence between traditional and alternative management, writes Heather Dale

Schroders is teaming up with hedge fund managers to launch a new range of UCITS funds for sophisticated investors.

The company, which wants to make hedge fund strategies more transparent and liquid by manufacturing funds in the UCITS III wrapper, is expected to launch an equity long/short product first.

Gavin Ralston, chairman of IEMFA and global head of products at Schroders, says the product development team is working hard to create products that reflect the advantages between traditional and alternative investment.

"For this particular fund, we are looking to partner with third-party hedge fund firms," says Ralston.

"We will provide management selection, due diligence and

distribution, and the hedge fund manager will provide the investment skills. It is unclear which hedge fund will manage the equity long/short fund, but other strategies are expected to follow in the UCITS III wrapper.

Mr Ralston says, "You can replicate virtually 100 per cent of the strategies that a hedge fund manager uses in a UCITS-compliant format."

That is not the case in strategies that depend on high levels of leverage, he adds.

Schroders, which has €113.2bn (€108n, \$160bn) in UCITS equity long/short products, is expected to launch a similar product later this month or October. It will be available to retail investors across Europe.

"Our model is to offer our products as broadly as possible. Typically, funds are domiciled in our Luxembourg fund range so they can be registered for sale in Europe but also in Asia and Latin America," says Mr Ralston.

These types of funds have been criticised for being too complicated for retail investors. In a recent Ignite survey, almost one fifth (19 per cent) of asset management professionals said it was unattractive to offer retail investors hedge-fund-like products.

Mark Damper, head of research at Hargreaves Lansdown, says, "It means the intermediary needs to do a lot more time-consuming research. Such explanations are complicated and are not all the same."

The absolute return sector is in a mess because there are lots of different types of funds with lots of different risk profiles.

Mr Ralston says the firm will not be actively promoting the funds to retail investors, but selling them through private banks and smaller institutions.

However, the UCITS format will mean, in theory, they could be available to retail investors. "As with all our products, we will have different levels of minimum investment reflecting the nature of the investment."

"We typically have A, C and I shares. A shares are

particularly clear who is going to win," says Mr Ralston.

"We think the combination of our skills and those of the hedge fund manager is a particularly compelling package."

It is not only traditional fund managers launching these types of products; more and more hedge fund managers have been moving into the UCITS III space as the result of stricter regulation and lost revenues due to high watermarks.

For example, Man Group, the world's largest hedge fund firm, attracted \$8.4bn in new money from retail investors in the first quarter of this year.

Schroders also recently announced plans to launch a number of multi-asset funds for European retail investors later this year.

The firm plans to launch two types of multi-asset fund.

The first will be broadly diversified, with a mix of equities, bonds and alternatives. The house is also working on a number of long-term pension solution products.

Heather Dale is a reporter on Ignite Europe, a Financial Times publication, where this article first appeared



Schroders to launch long/short product soon



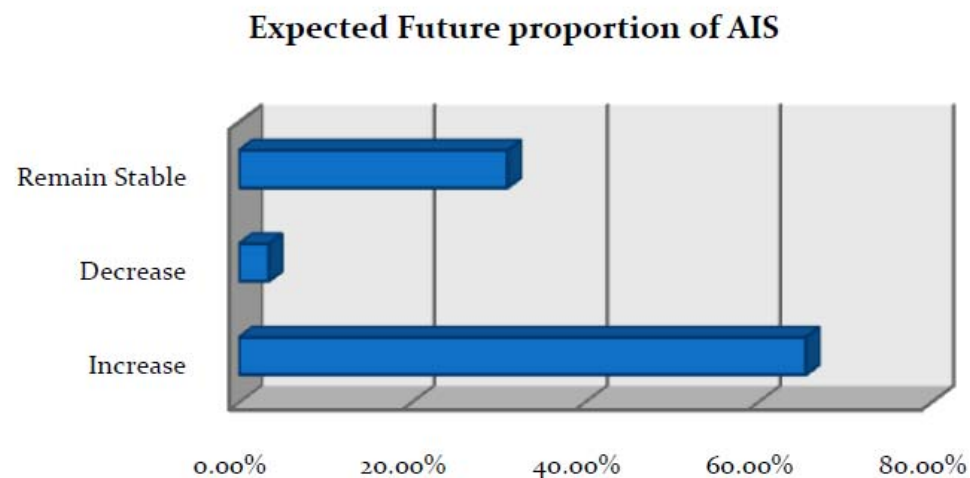
3.1 Alternative investment strategies in UCITS – why?

Press releases

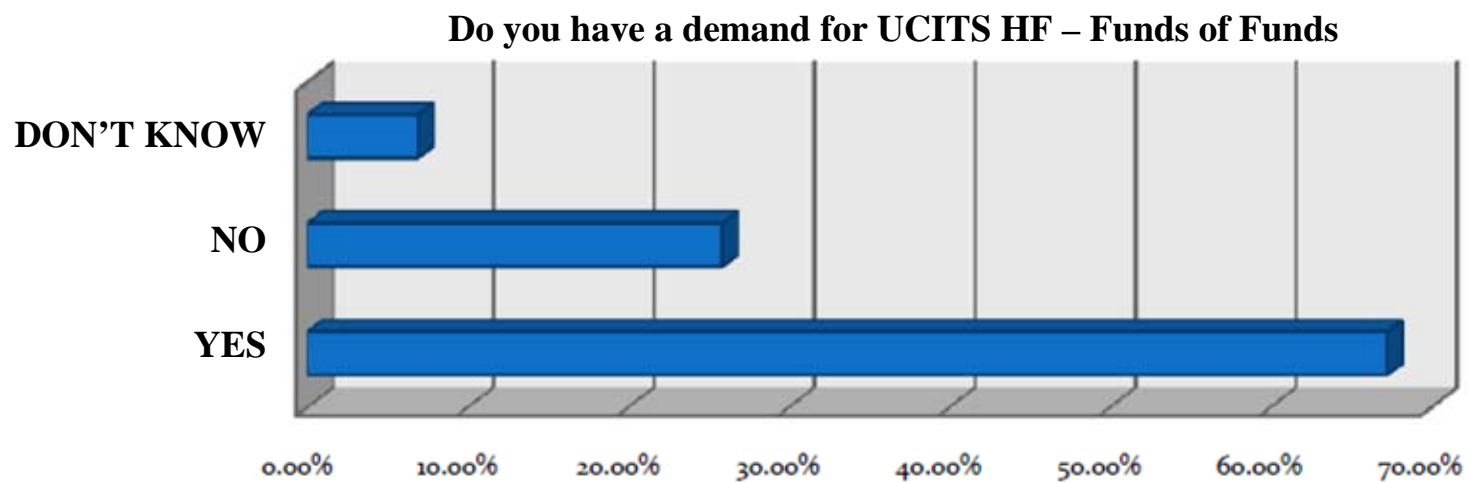
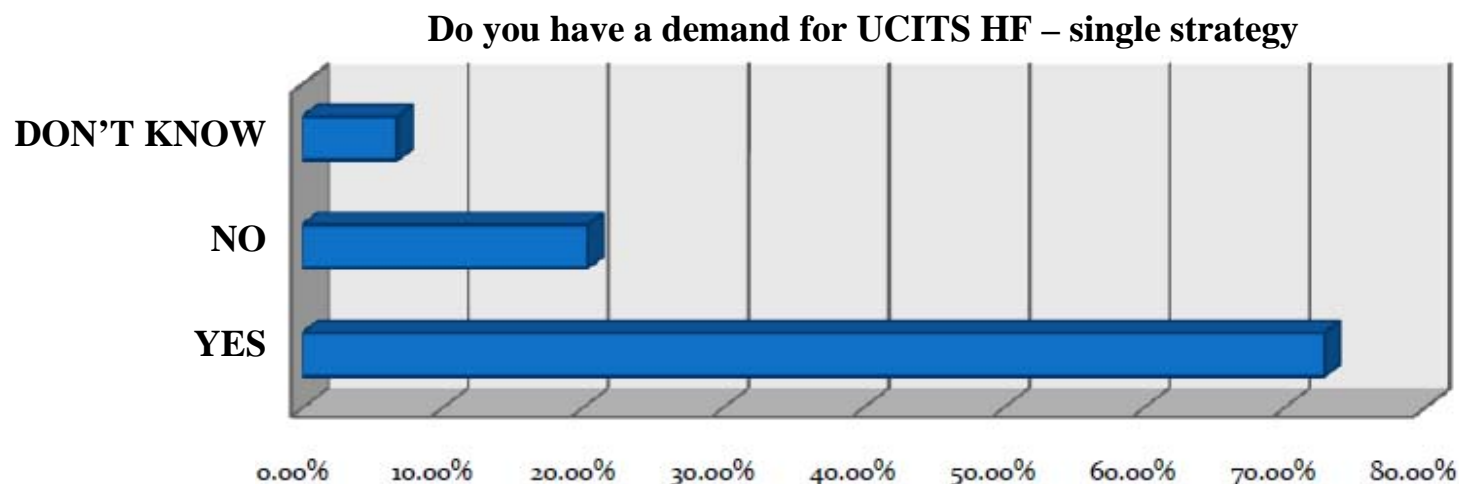
- ➔ “There is a substantial demand, in particular from HNWI, for regulated fund of hedge funds profiles”
- ➔ “Since the crisis of 2008, the “need” for more liquidity and tighter regulation certainly brought UCITS firmly into the spotlight. Following the wake of gates, suspensions, losses, regulators and investors started to look towards regulation.”
- ➔ “Most of the largest Fund of Hedge Funds managers intend to enter the UCITS space over the next year”
- ➔ “Ambition to gather more assets from sources that are not or no longer accessible through offshore funds or managed accounts”

3.1 Alternative investment strategies in UCITS – why?

- ➔ Survey conducted among 59 fund distributors (largest private banking networks + small UCITS / Hedge Fund distribution boutiques):
annual distribution of funds = 50 - 100 billion EUR
- ➔ Findings with regard to expectations of future business development:



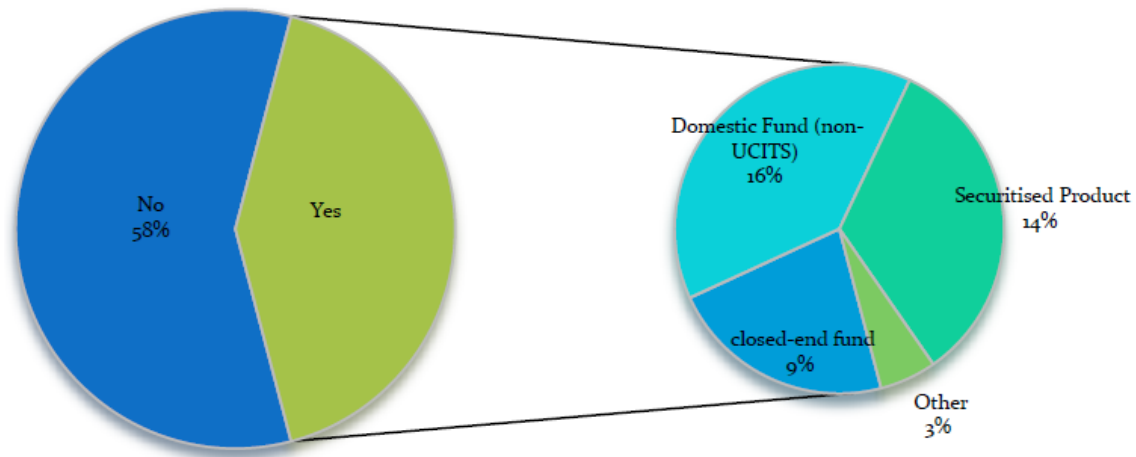
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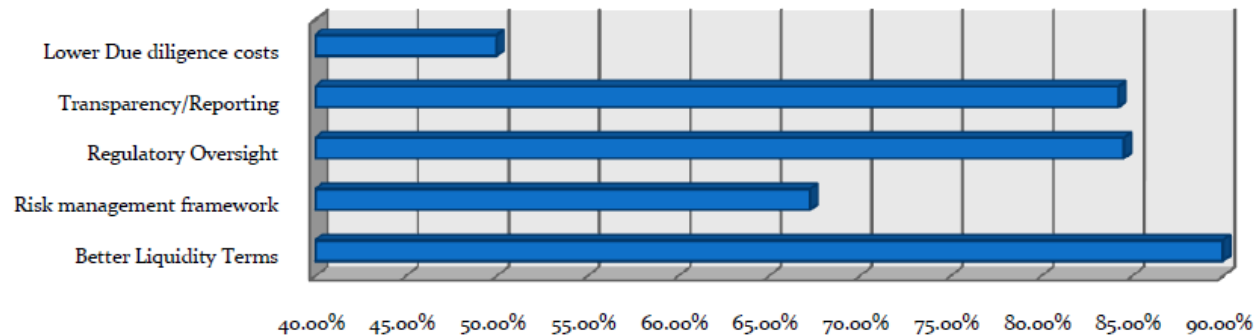
Source: KdK UCITS FoHF Distributors Survey – Q1 2010

3.1 Alternative investment strategies in UCITS – why?

Can such demand be satisfied with other Investment Vehicles

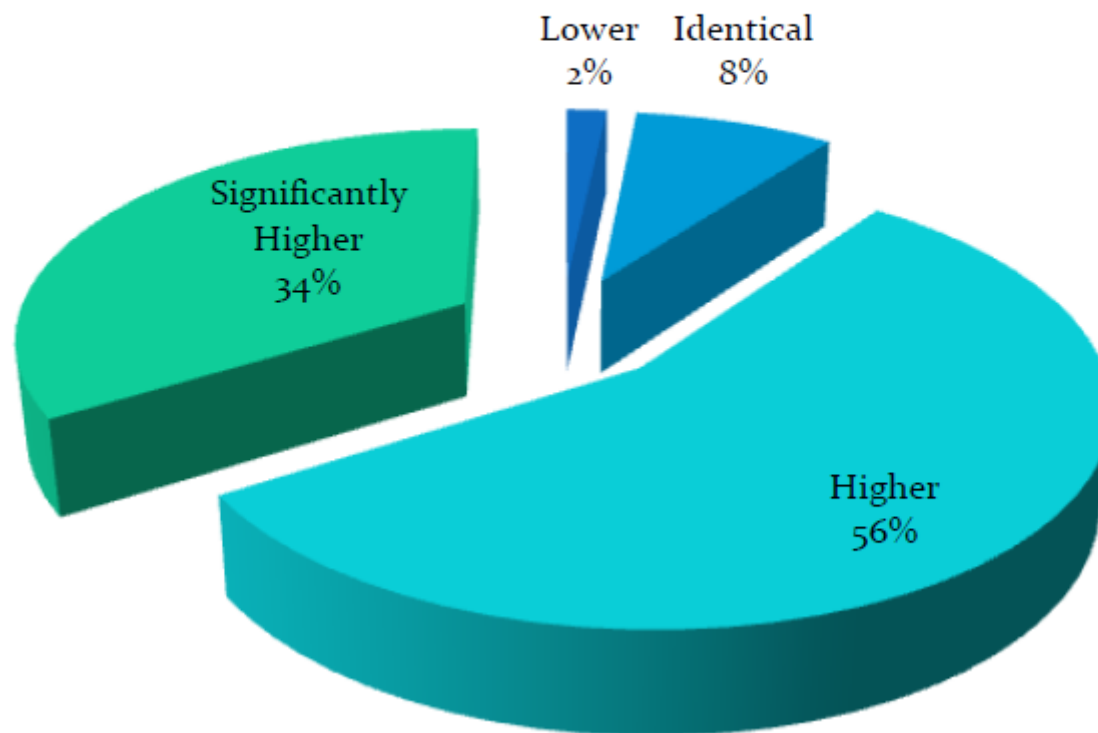


Value Added of UCITS as compared to Offshore Funds



3.1 Alternative investment strategies in UCITS – why?

Distribution potential for UCITS HF as compared to offshore HF



3.2 Alternative investment strategies in UCITS – which assets?

1. Alternative assets in UCITS

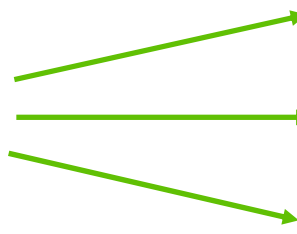
a. “Index” funds

→ UCITS using derivatives (swaps, etc) on

- hedge fund
- Commodity



indices

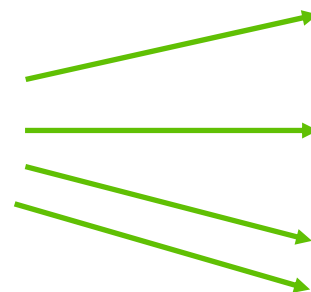


diversification

benchmark

publication

HF indices



- predetermined rules and objective criteria for selection and rebalancing of components
- no payments from index components
- backfilling
- due diligence on the index

3.2 Alternative investment strategies in UCITS – which assets?

b. UCITS Fund of Funds

→ UCITS of UCITS + other eligible assets

smaller investment universe than “offshore” universe?

→ UCITS of closed-ended hedge/commodity funds

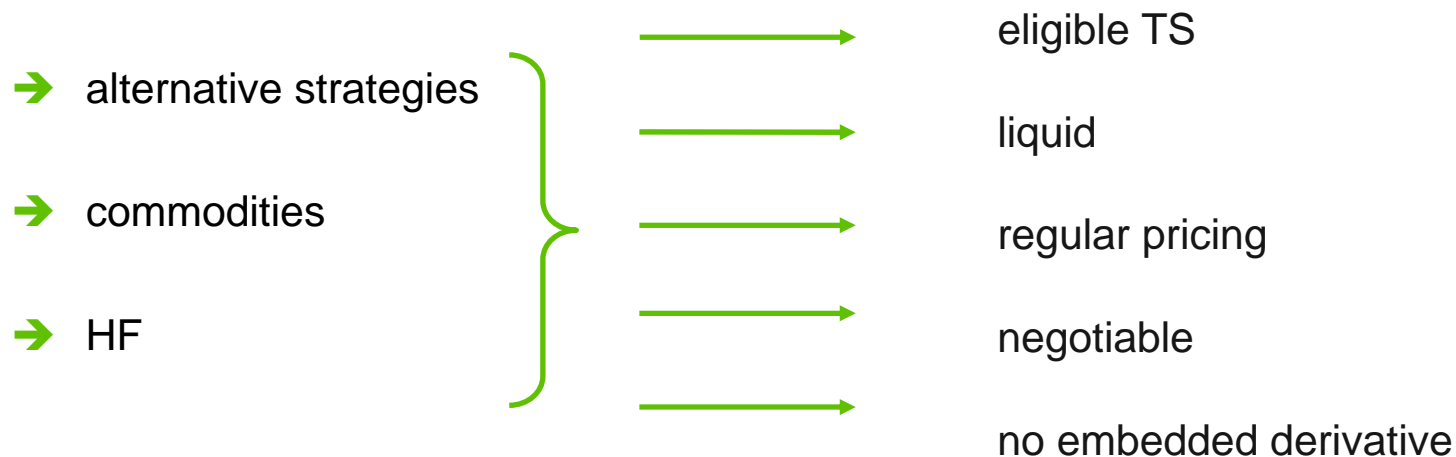
- eligible TS
- corporate governance
- supervision of manager

→ UCITS of open-ended regulated non-UCITS hedge/commodity funds
under the 30% or 10% ratios

- supervised
- cooperation between authorities

3.2 Alternative investment strategies in UCITS – which assets?

c. UCITS investing in delta-one notes on



d. UCITS using derivatives (structured swaps) to obtain an indirect exposure to a portfolio of offshore hedge funds

3.2 Alternative investment strategies in UCITS – which assets?

- e. 130/30 UCITS
 - synthetic short selling

- f. UCITS investing in managed accounts
 - comprised of eligible assets

- g. UCITS investing in CDSs on loans
 - no physical delivery

or a combination of different approaches for an improved diversification

BUT no free lunch



3.2 Alternative investment strategies in UCITS – which assets?

CORE PORTFOLIO

certificates on commodities reflecting the performance of an underlying commodity 1:1	10% per issuer
derivatives on diversified commodity indices or on diversified indices of commodity futures	counterparty risk limited to 5-10%
derivatives on non sufficiently diversified indices (if no high exposure to the index)	maximum 10 % to a given index (application of 5-10-40% rule)
listed closed-end funds (including SIFs)	10% per issuer
securities of companies whose principal income derives from a given commodity	10% per issuer

TRASH

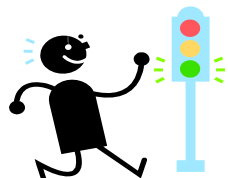
unlisted closed-end funds	10% (together with total unlisted holdings and open-ended funds)
open-end alternative funds (if supervised and supervisory cooperation)	10% together with other unlisted investments
open-end SIFs	10% together with other unlisted investments

} Trash ratio:
maximum 10%

However :

no commodities, no commodity derivatives, no derivatives on commodity futures

3.2 Alternative investment strategies in UCITS – which assets?



- Short positions through derivatives
- Closed end listed alternative funds
- Regulated open end alternative funds within trash ratio
- Derivatives on commodity indices
- Certificates on uneligible assets if no embedded derivatives
- CDS on loans with cash settlement
- 100% leverage through derivatives
- Liquid portfolio



- Direct short sales
- Open end alternative funds



- Direct investment in commodities
- Derivatives on commodities
- Certificate embedding derivatives on uneligible assets
- CDS resulting in kind settlement
- Leverage from borrowing
- Illiquid portfolio



3.2 Alternative investment strategies in UCITS – which assets?

2. Combination of “traditional” eligible assets and “traditional” financial derivative instruments actively managed

- Fixed income or equity securities

- MMI

- Derivatives (futures, forwards, options, swaps) on
 - interest rates
 - foreign currencies
 - fixed income securities
 - equity securities

- Synthetic short selling

- Cash



3.2 Alternative investment strategies in UCITS – which assets?

- To pursue different absolute return/macro-equity objectives:
- at different risk levels
 - through different exposures to underlying securities
 - through long and short positions in cash settled derivatives
 - through either very high or rather low exposure to derivatives within the limits of CSSF Circular 07/308
 - using the flexibilities of the CSSF Circular 07/308 in particular in terms of (i) netting, (ii) calculation of the market risk, counterparty risk and global risk exposure

3.3 Examples of alternative investment strategies in UCITS



1. Hedge Fund Index

Investment strategy:

- Investment in a **total return swap** linked to a Hedge Fund Index
- Hedge Fund Index sufficiently **diversified**
(Index composed of a diversified portfolio of 15 hedge funds, average weighting: +/- 7%)
- Hedge Fund Index = adequate **benchmark** for the market:
 - linked to the performance of a diversified portfolio of hedge funds with recognized investment strategies (i.e. equity long/short, event driven, tactical trading, multi strategy etc.)
 - rebalanced on a monthly basis
 - sufficiently liquid

3.3 Examples of alternative investment strategies in UCITS



- Index is **published** in an appropriate manner:
 - components NAV's published at least on a monthly basis
 - information published on the website of the Index provider

- Construction methodology: **rebalancing** on the basis of predetermined objective criteria

- No retrospective changes to previously published index values ("**backfilling**")

- Adequate **due diligence** prior to investment and continuous **monitoring** (methodology, availability of information, index components, calculation etc.)



3.3 Examples of alternative investment strategies in UCITS

2. Total Return Fund

- Achievement of a total rate of return in excess of cash indices
- Investment in instruments with low volatility: fixed or variable interest transferable securities or investment grade money market instruments, financial derivative instruments on interest rates + currencies; entering into short positions
- Gross average exposure: 2000%
- Net average exposure: 400%
- Low level of absolute VaR (4%)



3.4 Risk Management regulations at EU level in the context of UCITS IV

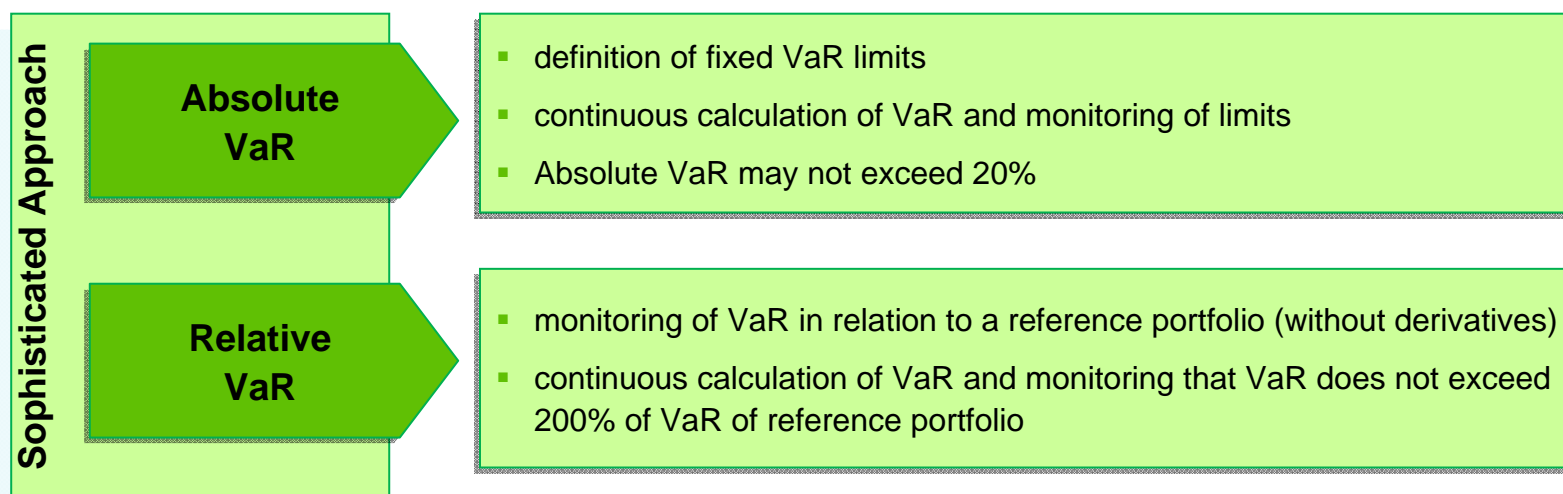
- UCITS IV Directive (2009/65/EC)
- CESR's technical advice to the European Commission regarding Level 2 measures related to the Management Company Passport (28 October 2009)
- CESR Consultation Paper of 19 April 2010 on Risk Measurement and the calculation of global exposure and counterparty risk for UCITS (level 3 guidelines)
- Level 2 measures and Level 3 guidelines to be adopted as a single package by July 2010

3.5 Risk Management regulations at national level

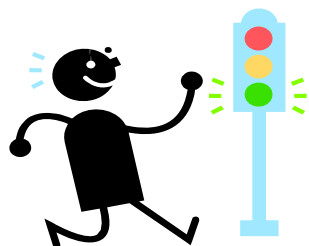
Applicable provisions	<ul style="list-style-type: none"> • Art. 42 (1) of the 2002 Law • CSSF Circular 07/308 on risk management
Organisational requirements	<ul style="list-style-type: none"> • Self-assessment: sophisticated / non-sophisticated UCITS • Change of risk classification -> information of the CSSF • Risk Management: independent unit
Reasons for implementing a Risk Management	<ul style="list-style-type: none"> • Measurement + monitoring of market risk • Measurement + monitoring of counterparty risk • Measurement + monitoring of concentration risk • Measurement + control of valuation of OTC derivatives • Risk reporting, communication to CSSF
Limitations on risk	<ul style="list-style-type: none"> • Concentration risk • Counterparty risk • Market risk : <ul style="list-style-type: none"> • non-sophisticated UCITS = commitment approach • sophisticated UCITS = relative / absolute VAR (sophisticated approach)
Valuation	<ul style="list-style-type: none"> • Fair and on an independent basis • based on current market value; if not available, valuation according to appropriate + recognized methodology

3.6 Risk Management: Calculation of global exposure

- Risk profile of UCITS determines calculation of global exposure
 - non-sophisticated UCITS: “Commitment Approach”
 - sophisticated UCITS: “VaR” (daily valuation)
 - absolute VaR (no definition of a reference portfolio)
 - relative VaR (definition of a reference portfolio)



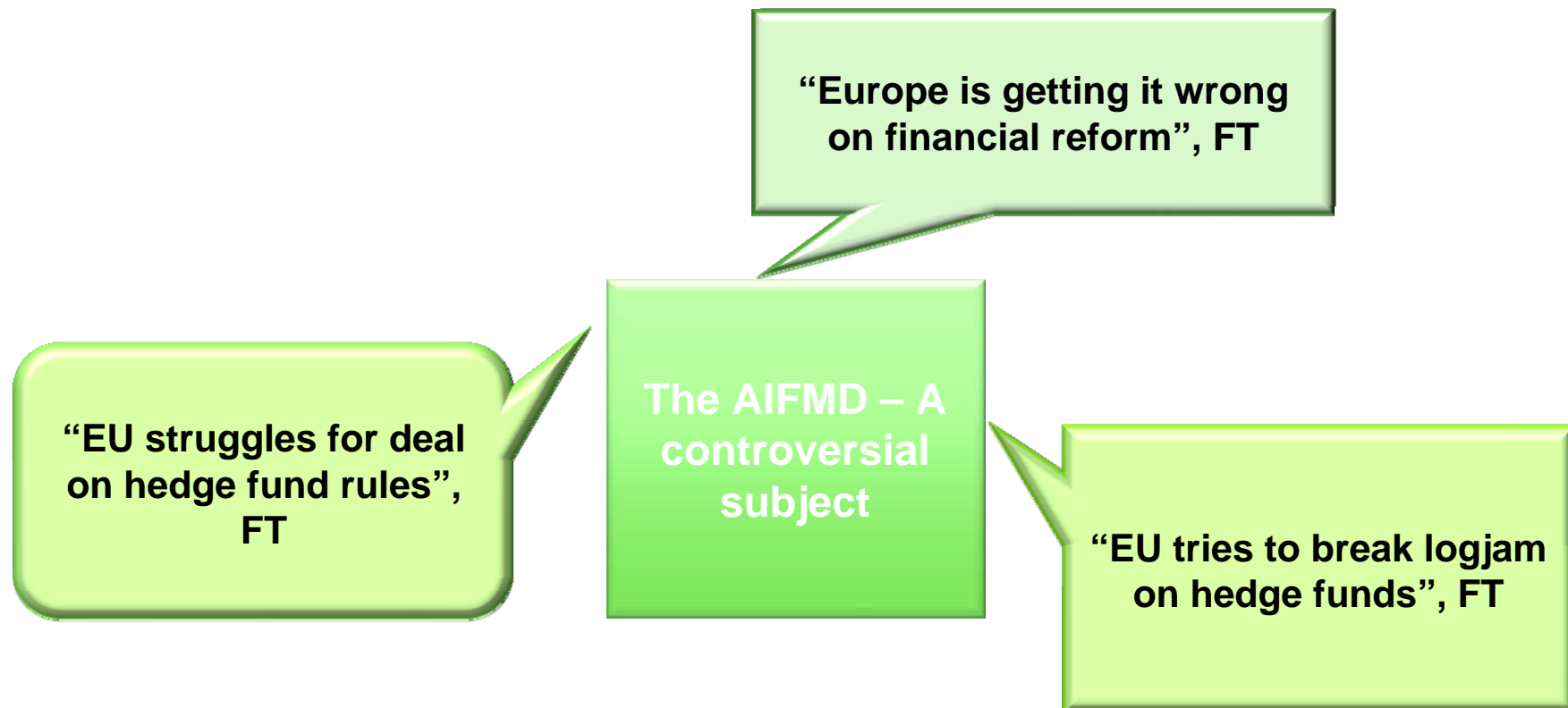
3.7 Impact of CESR Consultation of 19 April 2010



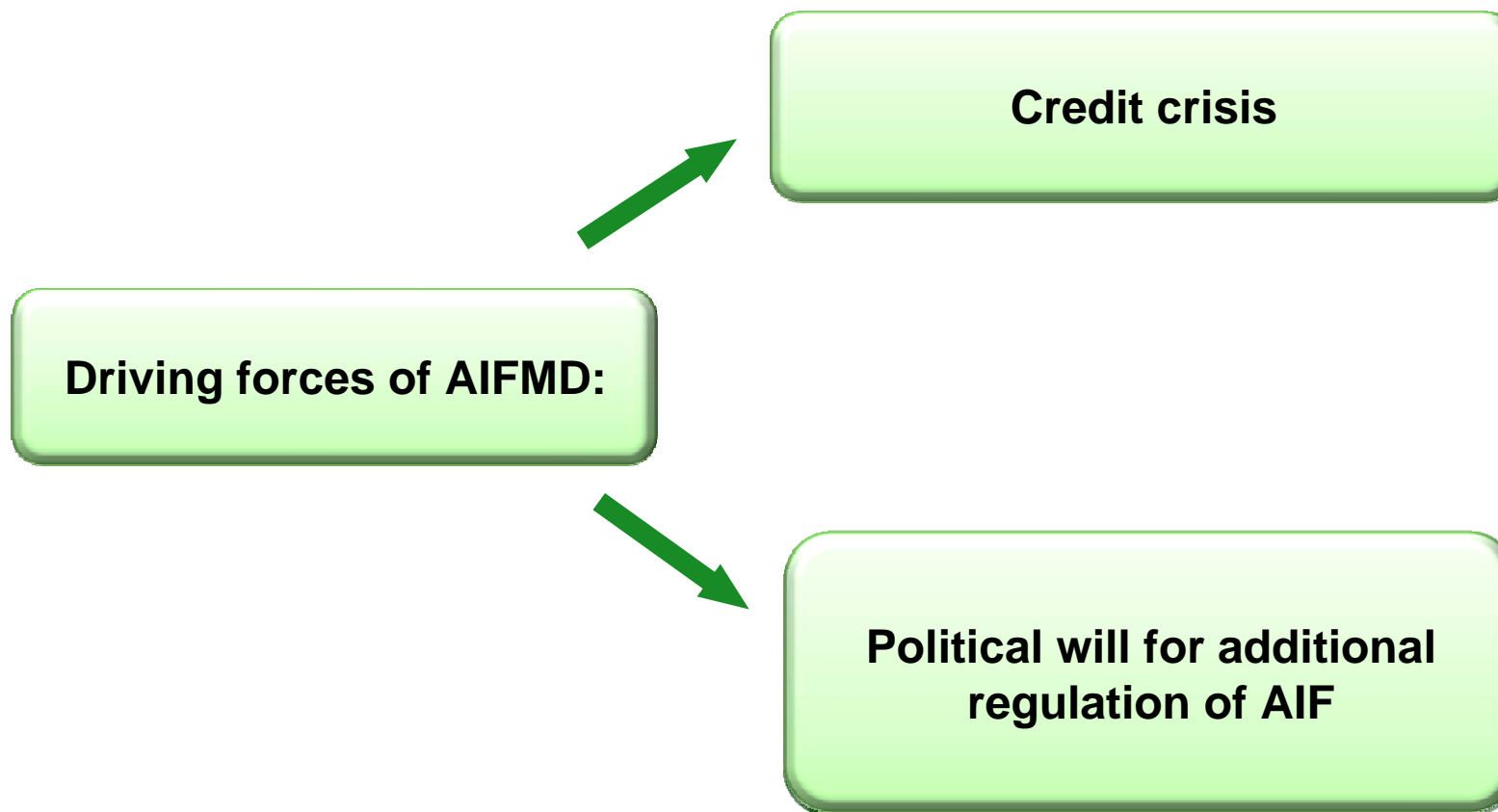
- **No major change in approach compared to current requirements**
- Sophisticated terminology not used anymore
- Main points of development:
 - Conversion methodologies for standard / embedded and exotic derivatives
 - Netting and Hedging
 - Sensitivity Approach
 - Stress testing

4. Regulatory developments at EU level: the AIFMD

4.1 Regulatory developments at EU level: the AIFMD



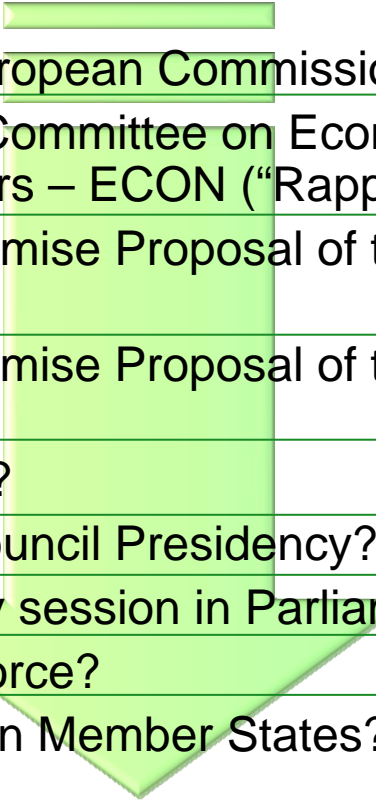
4.2 Driving forces of the AIFMD



- ➔ Establish common requirements governing the authorisation and supervision of AIFM in order to provide a coherent approach to the related risks and their impact on investors and markets in the EU

4.3 The AIFMD: Timeline

Timeline

- 
- A large, light green arrow graphic pointing downwards, centered behind the timeline text. It starts as a horizontal bar at the top and tapers to a point at the bottom.
- 30 April 2009 Draft of the European Commission
 - 23 November 2009 Report of the Committee on Economic and Monetary Affairs – ECON (“Rapport Gauzès”)
 - 15 December 2009 Latest Compromise Proposal of the Swedish Presidency
 - 11 March 2010 Latest Compromise Proposal of the Spanish Presidency
 - 10 May 2010 Vote in ECON?
 - 18 May 2010 Vote by the Council Presidency?
 - July 2010 Vote in plenary session in Parliament?
 - 2011 Entering into force?
 - 2013 Transposition in Member States?



4.4 Main issues of the AIFMD

1. Scope

- One-size-fits-all approach: all AIFM managing AIFs, i.e. all EU non-UCITS (private equity funds, real estate funds, hedge funds)
- General exemptions (e.g. UCITS, credit institutions, industrial holding companies)
- Specific or partial exemptions

2. Valuation

- Legal/functional independence between valuator and AIFM
- Liability of depository in valuation process
- Optional valuation for certain types of funds (private equity/real estate)

4.4 Main issues of the AIFMD

3. Depository bank

- Eligible entity
- Passport of depository bank
- Liability of depository bank / compatibility with UCITS regime

4. Third countries

- Level playing field EU funds/non-EU funds
- Equivalency EU AIFM/non-EU AIFM
- EU private placement regime
- Transitional period

4.5 The impact of the AIFMD

- Creation of a European market for alternative investments
 - AIFM Passport
 - AIF Passport

- Standardisation of:
 - Custody
 - Valuation
 - Risk Management
 - Reporting



4.6 Luxembourg: the European hub for alternative investments

- Leading European fund jurisdiction
- Fastest growing centre for alternative investments
- In depth knowledge for administration, custody and risk management processes
- Recognised and highly professional regulator
- Global hub for fund distribution

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