alfi
association of the
luxembourg fund industry

LUXEMBOURG PRIVATE EQUITY

Why Luxembourg ?

- Political, legal and fiscal stability
- State-of-the-art legal and regulatory environment
- High regulatory and investor protection standards
- Solid financial sector supervision
- Rapid and innovative responses to new trends
- Highly international, in terms of origin of financial institutions and fund promoters, clients, population and workforce
- Diversified offer of financial products and services
- Europe's number one investment fund centre
- Unique concentration of investment fund industry experts in all aspects of product development, administration and distribution
- Unrivalled know-how in cross-border investment funds business
- Top-notch market infrastructure for securities trading, clearing and settlement

Foreword

This brochure purports to provide general background information on the legal and tax aspects of regulated and unregulated private equity and venture capital vehicles set-up in the Grand Duchy of Luxembourg.

Luxembourg today offers a large variety of services and structuring opportunities to the private equity industry. Products include competitive structures for setting-up private equity and venture capital funds, such as the investment company in risk capital (SICAR), the specialised investment fund (SIF) or the reserved alternative investment fund (RAIF), as well as structures for pan-European private equity and venture capital acquisitions.

Luxembourg based service providers have teams specialised in servicing the private equity and venture capital industry and today offer a wide range of customised services in fund and acquisition structuring, transaction advisory, fund administration, custody and audit services.

ALFI cannot be held responsible for any errors or omissions or for the results obtained from the use of the information contained in this brochure. Interested parties should seek the advice of qualified professionals before making any decision as to the most appropriate Luxembourg private equity structure.

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1. Luxembourg – a conducive environment for private equity

Choosing the right location for the set-up of Private Equity operations means having to take into consideration many different factors. The following features are Luxembourg's strengths – the combination of these strengths makes Luxembourg attractive to Private Equity.

Political & economic stability

The political stability of Luxembourg is marked by a political culture of consensus where the traditional parties coexist within the context of broad agreement on key issues.
In this context, a group of key ministers have been allowed to remain in government for a significant period of time providing continuity in important policy initiatives under successive coalition governments, with an emphasis on economic policies. The business-friendly political environment is conducive to welcoming decision-makers and entrepreneurs. Attracting international players is considered paramount in building an efficient business framework and economic growth, and has enabled Luxembourg to establish a permanent and innovative business community.
An illustration is the recent special tax regime for highly skilled workers aimed at attracting a specialised workforce in areas such as Private Equity.

A stable and rewarding tax environment

The tax framework is considered among the most stable and rewarding in Europe for companies, their shareholders and their employees. This is a key component of Luxembourg's development. The tax authorities lead a constructive dialogue with taxpayers, have a business friendly attitude and the quick and pragmatic approach to the requirements of international investors.
Luxembourg is not a tax haven but it offers one of the most flexible and attractive tax regimes within the EU.

The strength of the Luxembourg financial services industry

Luxembourg is the largest financial centre for investments funds in Europe and the second largest worldwide. Initiators from 69 countries distribute their Luxembourg funds around the world through more than 59,000 distribution agreements: 65 out of 100 authorisations for distribution granted to worldwide funds are allocated to Luxembourg funds.
Luxembourg has been able to turn retail EU funds, the UCITS, into a brand that stands on its own, not only within Europe but worldwide.
More than 45,000 people are employed in the financial services industry which creates one third of the Grand Duchy's gross domestic product. Therefore, it is easily understandable why the financial industry and government are working closely and smoothly together to ensure continued efficiency. Luxembourg today hosts more than 500 companies servicing funds, such as central administrators, domiciliary agents, law firms, auditors, consultants, depositaries, management companies and alternative investment fund managers (AIFM) and many more; an industry that continues to develop dynamically.

Business-friendly environment

Luxembourg has a unique system of social dialogue that involves regular meetings between the government, employers' representatives and unions, which is key to avoiding social conflicts and to reaching consensus on important decisions regarding economic and social affairs.

Luxembourg was further one of the pioneers to implement the AIFMD and has largely leveraged on its long-standing and recognised UCITS experience to adapt the private equity industry to the new regulatory standards and marketing or placement regimes.

Although the initial objective of the G20 and the EU Commission was principally aimed at regulating the alternative investment industry in order to control and avoid systemic risk, the AIFMD indeed also entails a European marketing passport for AIFM. Once authorised in a EU Member country, these AIFMs can market the AIFs they manage to professional investors in all other EU Member countries. In the context of UCITS, Luxembourg has taken advantage of the opportunities given by the passport regime and has, on that basis, become the leading jurisdiction in the world for retail cross-border distribution. Luxembourg is therefore currently building on this positive experience and offer the possibility for both AIFM and AIF to use Luxembourg as their hub for marketing AIFs to professional investors in the EU and, potentially, as is currently the case for UCITS, beyond the EU.

A considerable number of Luxembourg UCITS management companies have also obtained approval to act as AIFM, allowing them to manage both UCITS and AIF. These AIFMs, as well as stand-alone AIFMs without UCITS licenses, offer private equity sponsors a cost-efficient solution, benefitting from the marketing passport.

Players on the Luxembourg Private Equity scene

- **GPs/Private Equity houses or their subsidiaries**

Whilst historically local presence was limited mostly to smaller and/or emerging General Partners (GPs), many large international houses have set up and conduct business out of Luxembourg since the middle of the last decade with a considerable and growing local substance.

- **Private Equity administrators**

These service providers offer domiciliary, accounting, trust services and, since the introduction of AIFMD in 2013, depositary services for closed-ended funds investing in Private Equity and Venture Capital. They provide offices to conduct business from, as well as a range of additional services to Private Equity houses that are conducting business out of Luxembourg. Luxembourg is home to both administrators specialised in Private Equity as well as many more generalist administrators that are often part of larger financial services groups. Governance standards of Private Equity structures set up in Luxembourg have undergone a significant evolution with enhanced governance having been made a priority by the supervisory authority and industry stakeholders themselves. Today, there is a high number of skilled independent directors available to serve Private Equity structures.

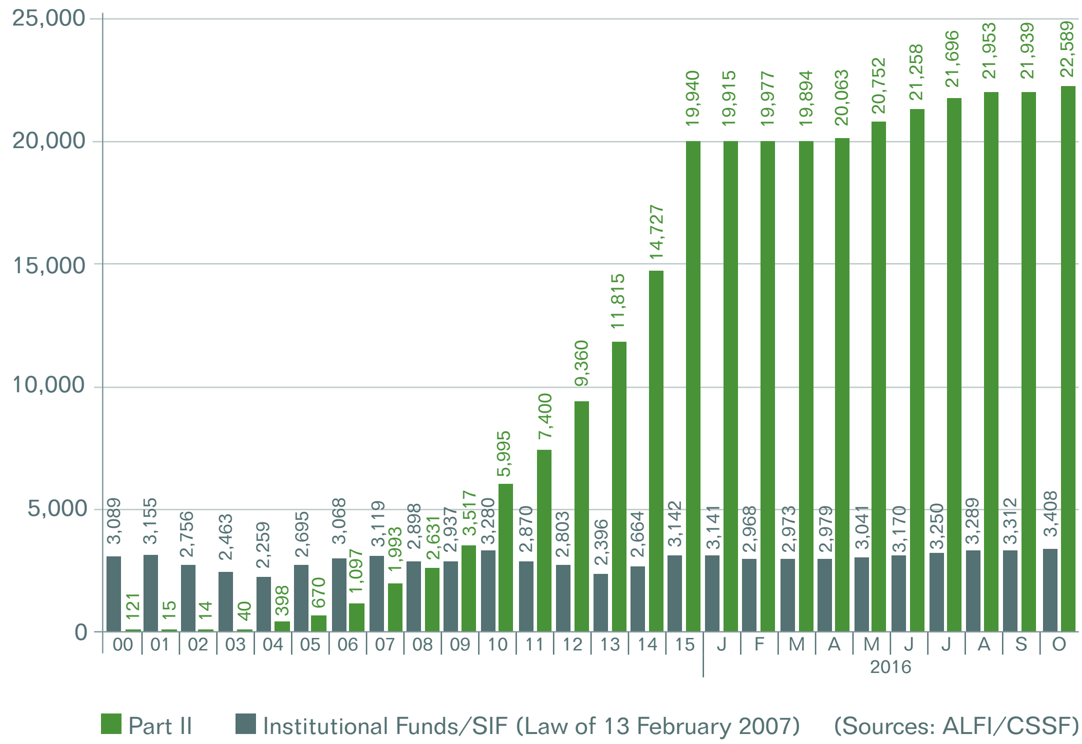
Luxembourg today offers a platform of services and structuring opportunities to the private equity industry. Products include competitive structures for setting-up private equity and venture capital funds, such as the investment company in risk capital (SICAR) or the specialised investment fund (SIF), and structures for pan-European private equity and venture capital acquisitions. Luxembourg has thus emerged as a prime jurisdiction for the structuring of private equity acquisitions and financings.

Besides the SIF and the SICAR, Luxembourg has built up its market share in private equity and venture capital funds thanks to its non-regulated special purpose companies (such as the SOPARFI - financial participation company) which are used for private equity acquisitions and financings alike. A SOPARFI is typically used for holding and financing private equity and venture capital investments. It may thus equally serve as a special purpose vehicle, a joint venture vehicle or more rarely a private equity fund vehicle.

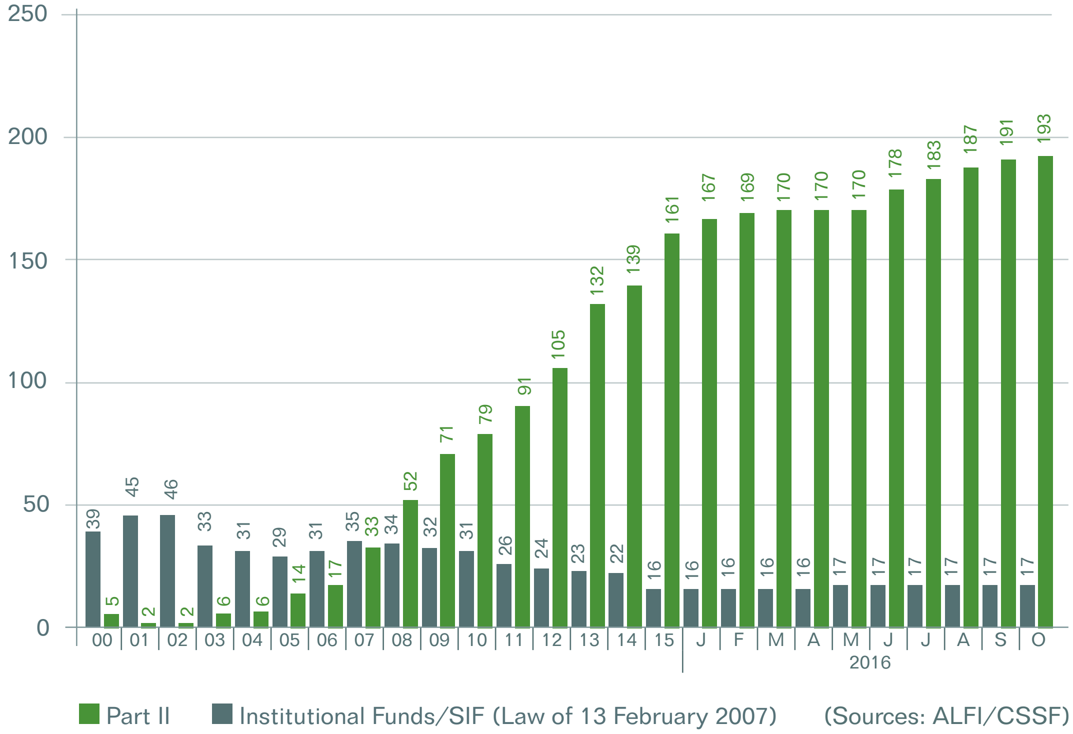
The RAIF (Reserved Alternative Investment Fund) structure allows private equity and venture capital fund initiators to set up Luxembourg-domiciled funds that are not subject to regulatory approval by the Luxembourg supervisory authority. This option permits the achievement of a significantly enhanced time-to-market for new fund launches.

Assets under management in Luxembourg Private Equity funds

EUR millions

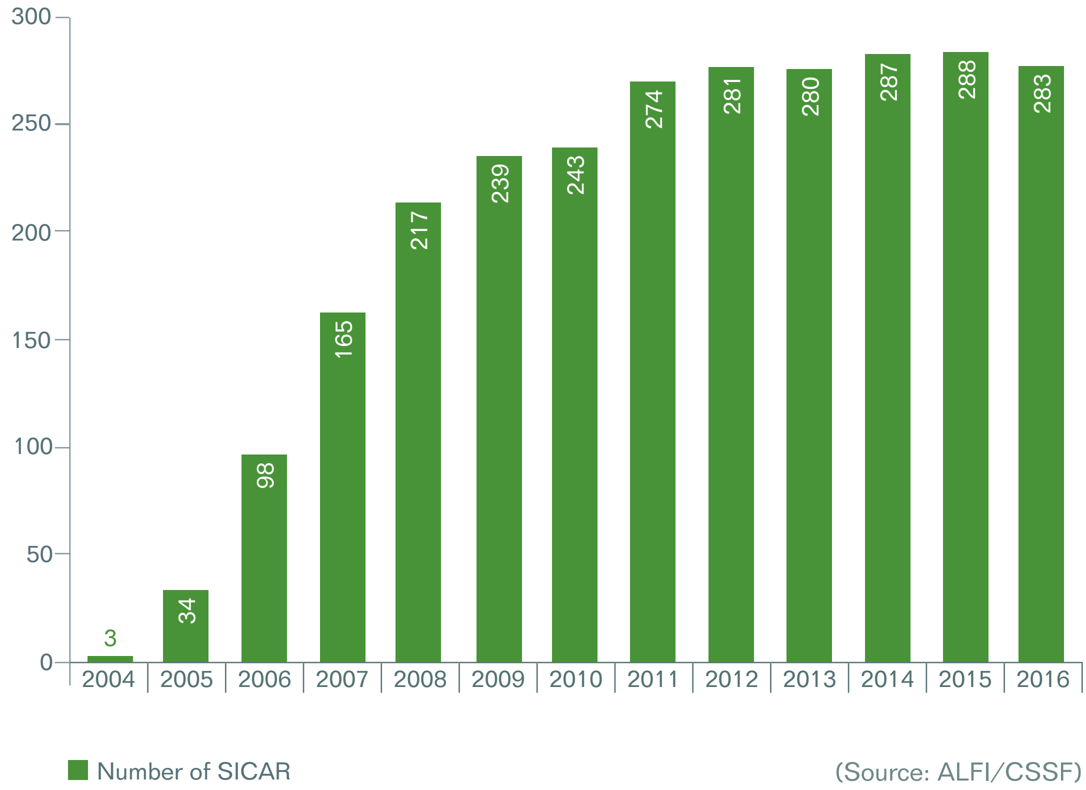


Number of Luxembourg Private Equity units



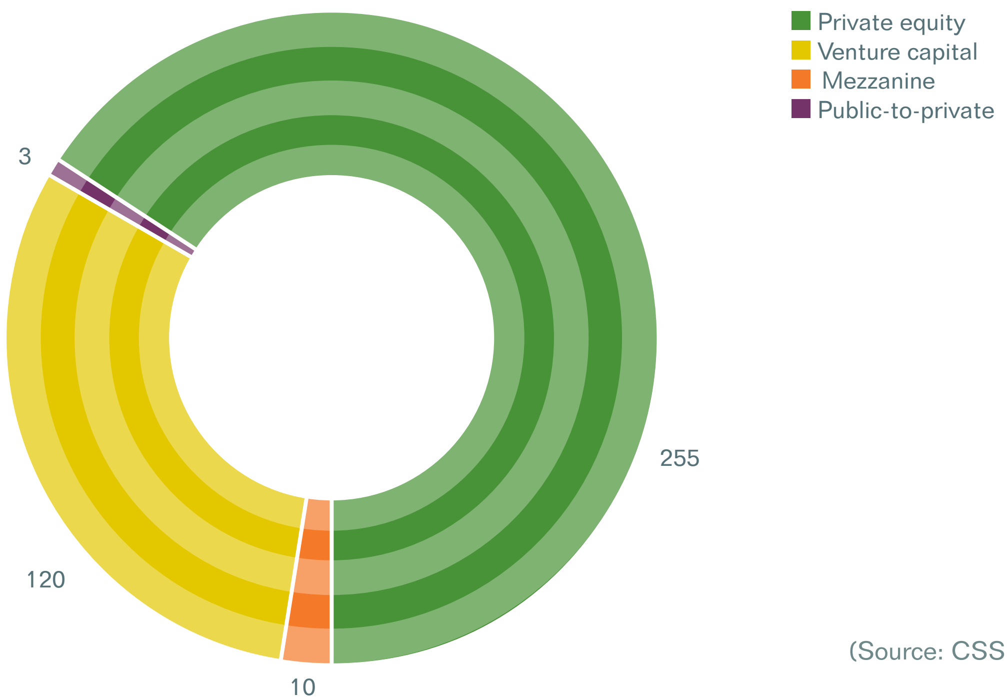
For the regulated SICAR and SIF, which will be described in further detail in section 4.1., the following figures have been published by the Luxembourg supervisory authority of the financial sector, the CSSF (*Commission de Surveillance du Secteur Financier*).

SICAR



(Source: ALFI/CSSF)

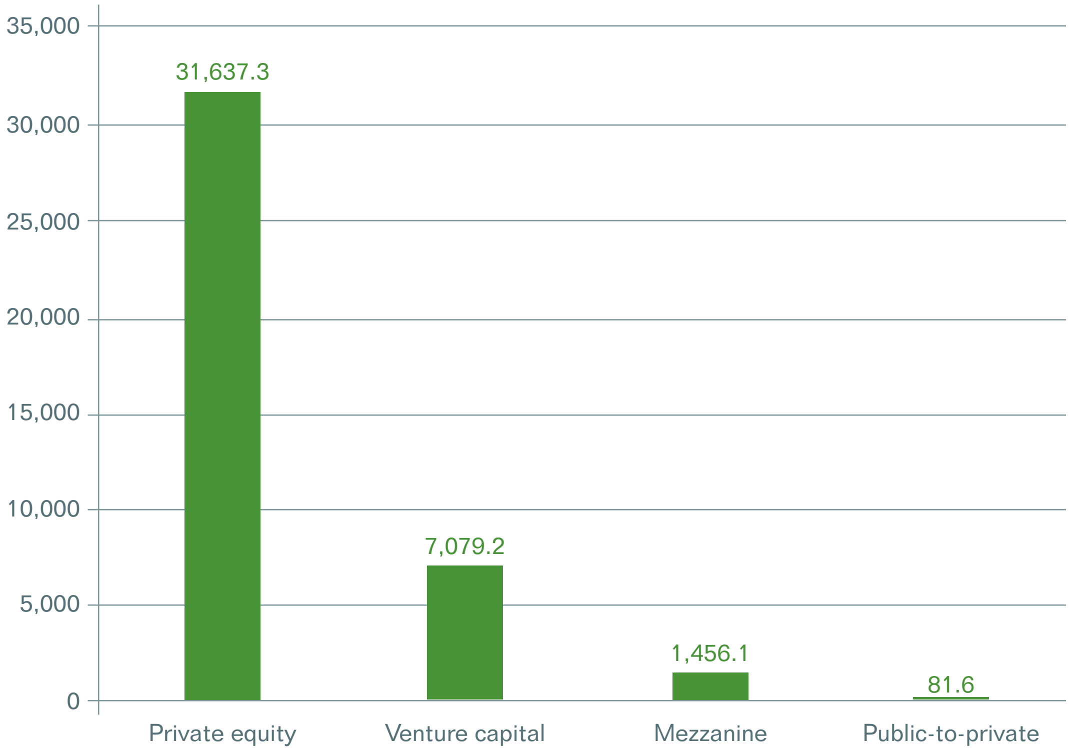
Investment policy of Luxembourg SICAR units in 2016
(by number of SICAR units)



(Source: CSSF)

Breakdown of SICAR net assets by investment policy

(*in million EUR*)



(Source: CSSF)

Geographical origin of SICAR initiators

Country/region	As % of total
France	26.1%
Switzerland	16.5%
United States	15.6%
Rest of the world	15.1%
Luxembourg	6.5%
Belgium	4.8%
Germany	3.9%
Other countries in Europe	2.8%
Other countries of the euro area	2.7%
Italy	2.5%
Spain	2.0%
United Kingdom	1.2%
BRICS	0.3%
Total	100%

(Source: CSSF)

2.1. Typical Luxembourg Private Equity structures

SICARs, RAIFs, SIFs and SOPARFIs can take a large variety of legal forms available under Luxembourg law and thus accommodate any set of tax and governance requirements – both from the investors' as well as the initiators' perspective – that typically arise in the context of setting up private equity vehicle as well as in special situations (e.g. master-feeder structures, acquisition structures etc.).

The table below compares the four most commonly used available structures on key criteria when choosing the right form for a Private Equity vehicle.

Besides the existing S.C.S., the AIFMD Law introduced a new legal form, the Special Limited Partnership (SLP or in French the *Société en Commandite Spéciale* S.C.Sp.) a limited partnership without legal personality. This legal form is comparable to the common English law limited partnership and can also be set up under a specific regulatory wrapper regime such as the SICAR or SIF regimes, or now also under the RAIF regime.

Since August 2016, the Simplified limited company (in French the *Société par Actions Simplifiée*, S.A.S.) offers an alternative vehicle that can be used for SICARs, RAIFs, SIFs and SOPARFIs.

Flexibility	Diversification
▪ SIFs and RAIFs are eligible for all asset classes ▪ SICARs are exclusively eligible for risk capital investments ▪ SOPARFIs benefit from flexible provisions of Luxembourg corporate law and offer flexibility in structuring of debt and equity	▪ SIFs and RAIFs must invest in a diversified asset portfolio ▪ SICARs are not subject to diversification requirements ▪ SOPARFIs have no constraints in terms of investment policy
Structuring	**Regulation**
▪ SICARs, SIFs, RAIFs and SOPARFIs are suitable for a large variety of institutional and professional investors ▪ SICARs, SIFs, RAIFs may in principle be organised in a fiscally neutral manner (to the extent they qualify as fiscally transparent) ▪ SIFs, RAIFs, SICARs and SOPARFIs may in principle benefit from all or part of Luxembourg's double tax treaty network (to the extent they are not fiscally transparent) ▪ SIFs, RAIFs, SICARs and SOPARFIs may be organised using different corporate forms (private limited liability company (S.à r.l.), public limited liability company (SA), corporate partnership limited by shares(SCA), limited partnership (SCS) simplified limited partnership (SCSp) etc.)	▪ SICARs and SIFs are subject to prudential authorisation and ongoing prudential supervision ▪ RAIFs are not subject to prudential authorisation but remain subject to indirect supervision via their AIFM ▪ SICARs, SIFs and RAIFs are subject to certain minimum disclosure obligations ▪ SOPARFIs are not subject to regulation (though may qualify as an AIF)

2.2. General Partners/ Management

When setting-up a corporate partnership limited by shares (*Société en Commandite par Actions* or S.C.A.), a common limited partnership (*Société en Commandite Simple* or *S.C.S.* or CLP) or a Special Limited Partnership (*Société en Commandite Spéciale* or S.C.Sp. or SLP), the general partner is typically set-up as a Luxembourg limited liability company. The management of the S.C.A., S.C.S. or S.C.Sp. can solely be entrusted to a general partner, managed by a single manager or a board of managers. Limited partners may also be entrusted with limited management functions.

The general partner will always be personally liable for the partnership's debts and obligations which cannot be satisfied out of the partnership's assets. In order to limit this joint and several liability, the general partner will typically (though not always) be organised as a private limited liability company (S.à.r.l.) or a public limited liability company (S.A.).

The general partner may delegate some of its powers to agents that it may in principle freely determine. For example, the general partner may or may have to nominate an AIF Manager, an investment advisor as well as all service providers in Luxembourg (e.g. central administration and depositary). It may furthermore organise various forums or committees to assist it in various functions. All such delegations and functions need to be organised in such a manner so as to limit the joint and several liability with the general partner only.

SICARs, SIFs and RAIFs may also be set up in the form of an S.A. or S.à r.l., either with a one-tier management structure, consisting of a board of directors or a two-tier management structure comprised of a management board and a supervisory board.

2.3. Substance and supporting industry

The growing presence of Private Equity business has prompted both general partners and the services industry to develop middle office activities locally. A significant number of Private Equity houses have created considerable proprietary infrastructure in Luxembourg.

Middle office services are focused on compliance, risk management and corporate governance and are used to dealing with highly complex structures, financial instruments and the active participation in the ultimate investee companies held by the entities organised and operated in Luxembourg.

The RAIF law provides that every RAIF must be managed by an authorised AIFM, which may be established in Luxembourg or in another EEA country.

The AIFMD and its implementing Regulations (Level 2) impose requirements on managers of (or self-managed) SIFs, RAIFs, SICARs and unregulated vehicles captured by the AIFMD on the necessity inter alia to retain eligible conducting officers, the enhancement of the central administration and substance of the PE structure, the necessity to introduce rules or policies on risk management, compliance, internal audit, transparency, remuneration and conflict of interest situations. The AIFMD Law, the Level 2 measures and CSSF Circular Letters detail the level of functions that may be outsourced and if so, to which degree.

2.4. Administration

The Luxembourg Private Equity fund administration sector basically falls into two categories: large international administrators servicing all fund ranges, including Private Equity funds, as well as independent local and international specialist administrators.

Today, the vast majority of Private Equity administrators offer the full range of central administration services, including domiciliation, administration, accounting, tax filing and company secretarial services to AIF including their controlled special purpose vehicles located in Luxembourg or abroad.

2.4.1. Depositary services

Depositary services for regulated Private Equity structures comprise the following two specific components: the safekeeping and the monitoring of the structure's assets.

The depositary services for regulated vehicles are only performed by credit institutions or investment firms. The AIFMD Law permits certain closed-ended AIFs to appoint as depositary non-banking institutions provided the relevant AIF and assimilated structures generally do not invest in assets that must be held in custody (i.e. financial instruments). This depositary function is only open to qualifying PSFs serving as professional depositary of assets other than financial instruments.

2.4.1.1. Monitoring function

As Private Equity fund assets are usually not physically safeguarded by the depositary itself, the depositary will have to focus on its oversight duties. In such case the scope of the supervision and oversight function of the depositary implies:

- Handling of the legal documentation related to the transactions carried out;
- Compliance monitoring of the cash and securities flows linked to transactions;
- Control of any single transaction including settlement;
- Implementation of an internal verification check list and escalation procedure;
- Monitoring of subscriptions and redemptions;
- Valuation duties.

2.4.1.2. Safekeeping of assets

Luxembourg based depositaries are today very well positioned to perform these legal duties under the AIFMD. The know-how of Luxembourg-based depositary institutions in providing a full range of customised services for Private Equity structures is nowadays widely recognised.

The services cover all investment and divestment processes, such as:

- Follow-up of board approval process as well as collection of underlying agreements and documentation related to the transactions;
- Supervision and monitoring of investments and divestments;
- Asset registration in the name of the vehicle under the supervision of the depositary;
- Compliance checks with the investment policy as described in the private placement memorandum/offering memorandum.

In addition, the depositary, in its role as paying agent or in cooperation with the transfer agent, may also offer among others, the following services:

- Processing of payments linked to the underlying investments;
- Collection of interest income and dividends from underlying investments;
- Processing of corporate events on underlying investments;
- Liaison with local correspondents, lawyers, notaries and others service providers;
- Recording of documentation and data back-up;
- Collateral management services;
- Tax reclaim management services (withholding tax treaty);
- Collection of subscription proceeds;
- Payment of redemption amounts;
- Execution of dividend payments to investors.

2.4.2. Banking services

Luxembourg banks offer cash management services, treasury, foreign exchange management, bridge financing and management of escrow accounts to their Private Equity clients.

2.4.3. Legal, tax and audit services

Luxembourg avails itself of significant expertise in legal and tax matters through numerous local and international law firms, tax advisors and audit firms experienced in Private Equity structuring and servicing.

3. Luxembourg tax environment

One of the key factors in favour of Private Equity operations in Luxembourg remains its favourable tax environment. A stable tax framework, a highly competitive social security system (for companies, employers and employees) and the lowest VAT rate in Europe greatly contribute to making Luxembourg one of Europe's most attractive jurisdictions for Private Equity operations and investments. Of key importance remains, however, the double tax treaty network that Luxembourg has built up over many years.

Taxation of Luxembourg PE vehicles

The Luxembourg tax environment is extremely beneficial for Private Equity structures, both regulated and unregulated.

■ The SOPARFI

As a regular company subject to normal corporate taxation and not subject to a specific regulatory regime, the SOPARFI benefits from Luxembourg's extensive network of double-taxation treaties and from the EU Parent-Subsidiary Directives. Despite being a fully taxable company, the SOPARFI allows for tailor-made structuring providing, under certain conditions, for a full exemption for dividends and capital gains upon exit.

■ The SICAR

SICARs can be created using different corporate forms.

- SICARs in the form of a limited partnership (S.C.S.)
  The SICAR, organised in the form of an S.C.S., is tax transparent and thus not subject to corporate, municipal business and net wealth tax. Income and gains received or realised are thus not subject to tax in the hands of the SICAR. Income and gains may furthermore be paid to investors without any Luxembourg source taxation.

- SICARs in the form of a corporate partnership limited by shares (S.C.A.)
  The SICAR, organised as an S.C.A., is a fully taxable company. The income from transferable securities is however exempt under specific conditions. The SICAR in the form of an S.C.A. will equally not be subject to net wealth tax. Dividend distributions are also not subject to any Luxembourg taxation at source.

■ The SIF

SIFs whether organised as a limited partnership or a corporate partnership limited by shares are not subject to any Luxembourg taxes on capital gains or income. The sole tax due is a subscription tax of 0.01% based on the quarterly net asset value. Certain exemptions are available. SIFs in corporate form can moreover claim access to certain double tax treaties.

■ The RAIF

In principle, RAIFs will be subject to the same tax regime as SIFs (see above). However, optionally, RAIFs investing in risk capital can opt for the SICAR regime (see above).

Luxembourg's Double Tax Treaty Network

Luxembourg has bilateral tax treaties in force with all EU Member States (except Cyprus) and with a number of other countries (including almost all OECD Member States). This network of tax treaties is constantly being expanded.

SICARs and SOPARFIs as Luxembourg taxable companies, are, from a Luxembourg perspective, entitled to treaty benefits and therefore benefit from double tax treaties concluded between Luxembourg and third countries. The application of tax treaties to SIFs and RAIFs taking the corporate form is to be assessed on a case-by-case basis depending on the wording of the treaty provisions and their interpretation by the relevant foreign authorities.

Fiscally transparent SIFs and RAIFs themselves may generally not benefit from treaty provisions due to their tax transparency.

Highlights of Luxembourg Tax Framework for Private Equity

- Effective carried interest structuring
- Extensive double tax treaty network
- Lowest VAT rate in the EU (17% currently), VAT exemption on management services rendered to RAIFs, SIFs and SICARs and free trade zone for valuable goods
- Competitive effective tax rates and low social security charges for individuals

3.1. Direct taxation of corporations

Luxembourg companies are subject to the following taxes:

- Income taxes at a combined rate of 29.22% in Luxembourg city in 2016, including municipal business tax;
- Annual net worth tax levied at a rate of 0.5% on the company's worldwide net worth on 1st January up to a value of EUR 500 million, and 0.05% on any amount in excess, subject to certain adjustments (eg. qualifying shareholdings). A minimum flat net worth tax of EUR 4,815 applies to most holding and financing companies which have a low or negative net worth.

Corporate income tax

Taxation for Luxembourg entities:
Corporate income tax applies to all tax resident corporations and to Luxembourg permanent establishments of foreign corporations.

Partnerships, other than those limited by shares, are regarded as tax transparent for Luxembourg tax purposes and are therefore not subject to corporate income tax and net worth tax at their own level. Income distributed by such entities will be considered, from a Luxembourg tax point of view, as flowing through the entity and are thus allocated directly to investors.

Resident taxpayers are liable to tax on their world-wide income, unless income is exempt under the provisions of applicable tax treaties or specific domestic tax law. There is a possibility of obtaining tax credits for foreign taxes paid.

Non-resident taxpayers are liable to tax on their Luxembourg-sourced income only, e.g. income realised by and allocable to a Luxembourg permanent establishment.

Thin capitalisation rules generally require a debt to equity ratio of 85:15 in the context of financing of participations or real estate. Following the example of other European countries, the Luxembourg direct tax authorities have clarified the tax treatment of Luxembourg group financing companies. Besides appropriate operational infrastructure, the relevant guidance provides that the equity of the financing company should be sufficient for the functions it performs, the assets used and the risks it assumes. No CFC rules exist in Luxembourg.

Capital gains taxation for non-residents

If a non-resident shareholder is resident (for tax purposes) in a country that has a double tax treaty with Luxembourg, the treaty will generally allocate the right to tax to the country of residence of the relevant shareholder. In the event that no such double tax treaty exists or can be applied, capital gains on the sale of shares in a Luxembourg company are subject to tax in Luxembourg only if the non-resident shareholder has held a substantial interest in the Luxembourg company and the transfer occurs within 6 months of the acquisition or in the event of a transfer after 6 months, the non-resident individual shareholder has been a Luxembourg resident taxpayer for more than 15 years and has become a non-Luxembourg taxpayer less than 5 years before the disposal takes place.

For this purpose, a substantial interest exists if a shareholder, either alone or together with certain close relatives, has held a shareholding of more than 10% in a Luxembourg company at any time during the five year period preceding the transfer.

Municipal business tax

Municipal business tax varies from 6% to 12% (levied on income of businesses operating in Luxembourg), depending on the municipality where companies have their registered office. For companies operating in the city of Luxembourg, the rate is 6.75%. A deduction of EUR 17,500 applies to the municipal business tax base for entities liable to corporate income tax (EUR 40,000 for other businesses). Municipal business tax is cumulative with corporate tax and is non-deductible.

Net wealth tax

Net wealth tax is levied at a rate of 0.5% (or 0.05% when the net worth exceeds EUR 500 million) on the company's worldwide net worth on 1 January of each year. Qualifying shareholdings under the participation exemption regime net of allocable debt (allocable debt that exceeds the value of the shareholding is deductible against other assets) are excluded from the taxable base. Luxembourg corporate income tax is creditable to the net worth tax provided certain conditions are met.

Withholding taxes

A withholding tax of 15% is levied on dividend payments (17.65% if the dividend tax is not charged to the shareholder) unless an applicable tax treaty provides for a lower rate or the Luxembourg participation exemption regime reduces withholding tax to 0%. Liquidation proceeds are not subject to withholding tax. Arm's length fixed or floating rate interest payments are generally not subject to withholding tax. Interest paid on certain profit sharing bonds and profit sharing interest paid on loans is subject to 15% withholding tax unless a lower tax treaty rate applies. Royalty payments are not subject to withholding tax provided they are not connected with non-resident artists' performances and sportsmen's activities in Luxembourg.

Automatic Exchange of information

On 28 March 2014, Luxembourg entered into an intergovernmental agreement ("Luxembourg IGA") with the United States of America with respect to the US Foreign Account Tax Compliance Act ("FATCA"), which was implemented into Luxembourg law by the law of 24 July 2015 ("FATCA Law"). Under the Luxembourg IGA and FATCA Law, Luxembourg financial institutions (including in certain cases SICARs, SIFs, RAIFs or SOPARFIs) are required to provide certain information about their US account holders to the Luxembourg tax authorities, which will share that information with the Internal Revenue Service ("IRS") on an annual basis. Luxembourg financial institutions that do not comply with their FATCA obligations risk being subject to a 30% US withholding tax on their US source income in addition to local penalties.

Largely inspired by FATCA, the OECD has developed a global standard for the automatic exchange of financial account information, the Common Reporting Standard ("CRS"). The CRS has been implemented at European Union level through the Directive on Administrative Cooperation (Directive 2014/107/UE), transposed into Luxembourg law by the law of 18 December 2015 ("CRS Law"). Under the CRS Law, Luxembourg financial institutions (including in certain cases SICARs, SIFs, RAIFs or SOPARFIs) are required to collect certain information about their account holders that are fiscally resident in a EU Member State or in a country with which Luxembourg has a tax information sharing agreement, and to report this information to the Luxembourg tax authorities: The Luxembourg tax authorities will thereafter automatically exchange the information with the foreign tax authorities on an annual basis. Luxembourg financial institutions that do not comply with their CRS obligations may be subject to local penalties (no withholding tax penalty system).

Value Added Tax (VAT)

The Luxembourg VAT standard rate of 17% is the lowest in the EU, compared with an average of 21% in the other EU Member states. The Luxembourg VAT regime furthermore exempts from VAT management services provided to investments funds. Since July 2013, the exemption has been available for all alternative investment funds covered by the law of 12 July 2013 transposing the AIFMD, including unregulated funds. This exemption is applicable on portfolio management, advisory services and administrative services. Due to this exemption and the low VAT rate, the VAT burden of SICAR, SIF and other alternative investment funds is very limited. This exemption is however not available to SOPARFIs unless they qualify as an AIF.

Assuming their activity is limited to the ownership of shares, SOPARFIs are not obliged to register for VAT except in the unlikely case they acquire goods from abroad. They cannot recover the VAT incurred on their costs.

Luxembourg has no “use and enjoyment” rule obliging, as in some Member States, holding companies, which are not VAT taxable persons, to self-assess the local VAT on services received from non EU service providers without allowing the deduction of this VAT.

A Freeport, operational since September 2014, in the vicinity of the Luxembourg airport, benefits from the VAT-free zone regime on transactions in valuable goods, including their storage. Certain types of investment funds (i.e. passion funds, investing into art and other collectibles) may take advantage of the Freeport.

Registration duty and transfer taxes

A fixed registration duty of EUR 75 is due upon incorporation and modification of the articles of association of a Luxembourg company or upon transfer of the statutory seat or place of central administration of a company to Luxembourg.

Transfer taxes on the sale of local real estate amount to 7% or 10%.

Tax treatment of carried interest

In the law transposing the AIFM directive, a regime for the taxation of carried interest from AIFs was also introduced.

The share of profits derived from an AIF and paid to AIFM employees is treated as ordinary income and is thus subject to the highest marginal rate of tax for the recipient (44.10% for 2016) on global income. However, if the employee satisfies certain conditions, the carried interest would be taxable at one quarter of the global tax rate.

The conditions to be fulfilled are:
- The recipient was neither resident in Luxembourg nor subject to Luxembourg tax on his/her professional income during the 5 preceding years;
- The recipient becomes Luxembourg tax resident;
- No advance payments were received by the recipient;
- The entitlement to carried interest is conditional on the investors having priority in recovering their initial investment.

The individual can benefit from this tax treatment for up to 10 years after having started his/her professional activity in Luxembourg.

The beneficial tax rates do not apply to capital gains realised on the sale of interests in the AIF, which are subject to standard capital gains rules.

Implications of OECD BEPS project

In February 2013, the Organization for Economic Development (OECD) issued a report entitled “Addressing Base Erosion and Profit Shifting” (BEPS), followed by an action plan with 15 actions in July 2013 (Action Plan). The BEPS project is supported by the G20 and is not limited to OECD member countries only, but also includes a number of developing countries. The Action Plan is intended to prevent taxpayers operating internationally from shifting profits to low- or no-tax jurisdictions and thereby reducing their tax base. While BEPS was not aimed at the fund sector, many of the actions and recommendations will likely have an impact on private equity and venture capital funds and/or their portfolio companies. The recommendations include rules to deal with hybrid instruments and entities, a review of harmful tax practices of Member States and associated countries, a framework for mandatory spontaneous information exchange on tax rulings covering certain regimes, rules against treaty abuse as well as an update of transfer pricing rules for intangible assets. In addition, groups would be required to draw up a "country-by-country-report" that is to be made available to tax authorities and should allow tax authorities to get a more global view on a group's worldwide operations, also functioning as a risk-assessment tool.

Many countries have started to consider or are already implementing some of the solutions suggested by the OECD. Many of the recommendations are primarily targeted at multinationals seeking to minimise their tax burden, rather than through-bound investment and financing structures typically used by Private Equity. There may be an effect on the businesses into which Private Equity Funds invest, however the primary areas, for example deduction of interest expense and transfer pricing, had already been the subject of focus by many of the key larger economies. It will therefore be important to regularly review existing structures to ensure they are not adversely affected by tax law changes implemented as a result of the BEPS project.

3.2. Miscellaneous charges and fees

Chamber of Commerce Fee

All Luxembourg commercial companies are subject to an annual contribution (cotisation) ranging from 0.02% to 0.025% based on the relevant taxpayer's profit generated in the penultimate fiscal year before the relevant contribution generating year. This contribution is capped at EUR 3,000 for SOPARFIs, however the company in question must be coded with the correct NACE code in order to benefit from this cap.

CSSF Fees

Prudential oversight comes at a cost to the entities supervised:

Authorisation: EUR 3,500 for single-compartment structures and EUR 7,000 for multi-compartment structures Annual fee: for single-compartment structures EUR 3,000. In case of SIFs, for multi-compartment structures the charge varies according to the number of compartments:

- 1-5 compartments: EUR 6,000
- 6-20 compartments: EUR 12,000
- 21-50 compartments: EUR 20,000
- More than 50 compartments: EUR 30,000

The annual fee for SICARs is fixed at
- EUR 3,000 (single-compartment) and
- EUR 6,000 (multi-compartment).

3.3. Personal taxation

Luxembourg is one of the EU Member States with the lowest effective taxes and social security charges for individuals.

Social security

Social security contributions are computed on the annual gross remuneration capped at EUR 115,374. Self-employed persons are subject to a 23.56% rate on their gross professional income capped at also EUR 115,374.

In addition, employees and self-employed persons are subject to a 1.4% dependency contribution (*assurance dépendance*) assessed on their annual gross professional income (uncapped). This dependency contribution applies to all income (and not only to employment or self-employed income) in the hands of taxpayers who are subject to the Luxembourg mandatory State social security regime.

Income tax

Resident taxpayers are subject to income tax on their worldwide income. Non-resident taxpayers are only subject to income tax on Luxembourg-sourced income. Taxable income is assessed on the basis of total income less exemptions, deductible expenses and allowances. The law provides for many exemptions and deductions especially for families with children. Income tax is progressive with rates between 0% and a maximum 42% and is assessed on the basis of the taxpayers' family status. This tax rate is itself increased by an employment fund contribution of 7% or 9% (depending on the family status and level of income) resulting in a top marginal rate of 45.60%.

In principle personal tax is assessed on the basis of an annual tax return that must be lodged by taxpayers. A withholding tax is levied on employment income (progressive withholding tax scale) and director's fees (20% flat withholding under conditions). Withholding taxes on employment income and director's fees are creditable against the taxpayer's final income tax liability.

A special regime for highly skilled workers ("HSWs"), who are seconded to a Luxembourg undertaking belonging to an international group or are recruited from abroad by a Luxembourg undertaking, has been applicable since 1 January 2011. This special regime consists - subject to certain conditions – of an exemption from Luxembourg personal income tax on certain expenses and allowances paid to or on behalf of HSWs due to their expatriation. However these expenses and allowances remain tax deductible costs for the Luxembourg undertaking.

Net wealth tax

There is no net wealth tax for individuals.

Inheritance/Gift tax
Inheritance tax is due on the value of all property inherited from a Luxembourg resident whereas transfer tax is due on the value of real property located in Luxembourg that is inherited from a non-resident.

Where the heir is a direct descendant or a spouse with children, there is in principle no inheritance tax liability.
Gift tax rates vary according to the degree of kinship between the donor and the donee, ranging from 1.8% to 14.4%.

Summary of tax-related features:
- Attractive effective tax rates;
- Broad participation exemption regime;
- Significant exemptions from withholding tax on dividends;
- No withholding tax on interest, royalties and liquidation proceeds;
- No capital/stamp duties on the sale of shares in a Luxembourg company;
- Use of international exchange of information standards;
- Extensive double tax treaty network;
- Transfer pricing and thin capitalization adhering to international standards;
- Advance tax clearance system;
- Specific tax regimes for investment funds, securitisation activities, risk capital and reinsurance;
- Competitive personal income tax regime and low social security contributions for employers and employees.

Private Equity vehicles in Luxembourg are either non-regulated companies or structures that are supervised by the Luxembourg *Commission de Surveillance du Secteur Financier* (CSSF).

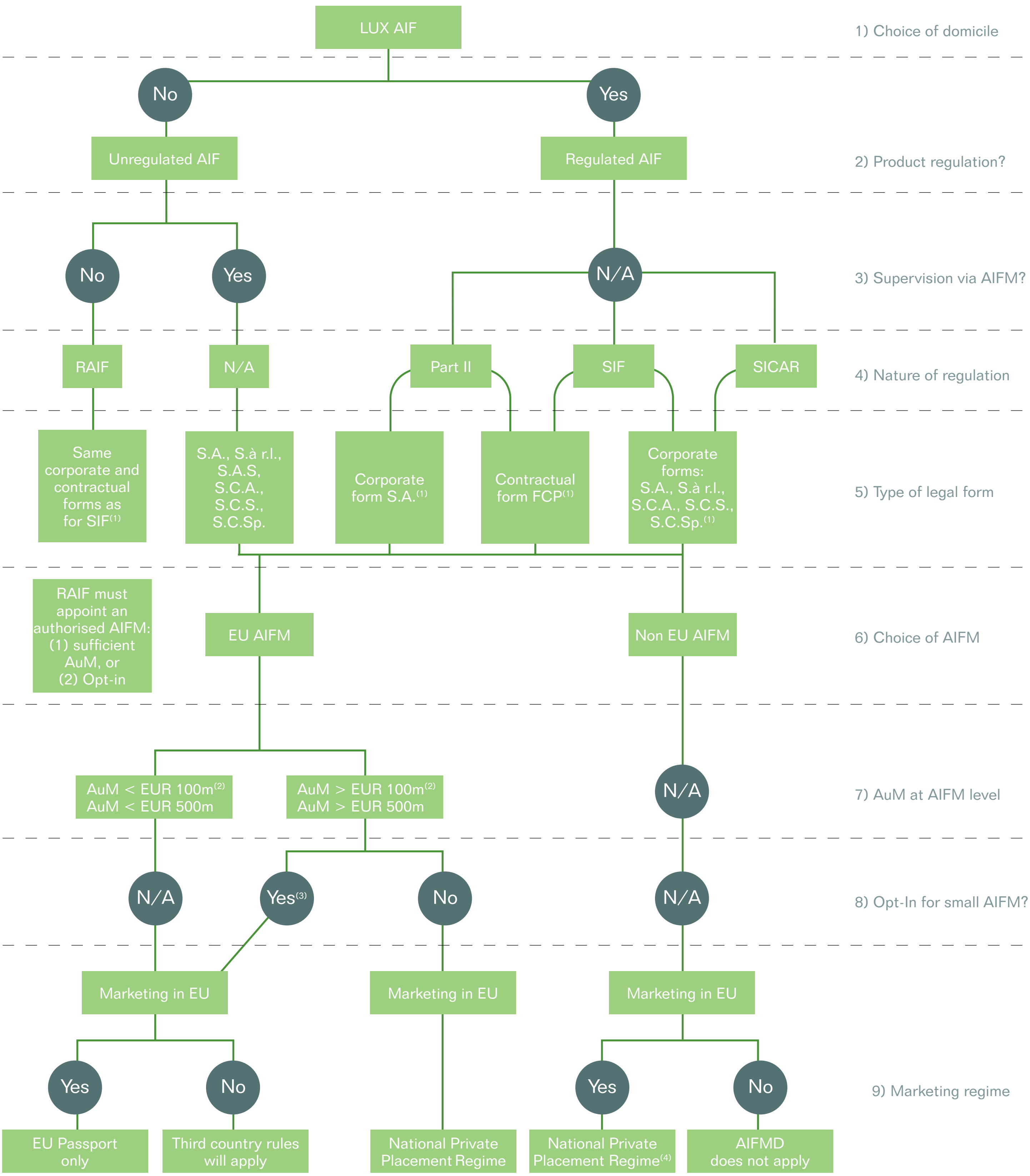
The CSSF regulates SICARs and SIFs. SIFs are regulated under the provisions of the law dated 13 February 2007 on the specialised investment funds (the SIF Law) while SICARs are regulated under the provisions of the amended law of 15 June 2004 (the SICAR Law). Both SICARs and SIFs are registered on official lists maintained by the CSSF.

The CSSF also regulates accessory services, among which:

- Registrar agents;
- Depositaries;
- Professionals providing fund transfer services;
- Company domiciliation agents;
- Client communication agents;
- Administrative agents of the financial services industry;
- IT systems operators of the financial services industry;
- Professionals providing company management services;
- Auditors.

As of 13 January 2015, 315 entities with Professional of the Financial Services (PSF) status were registered with the CSSF employing 14,750 persons.

4.1. Schematic representation of principal choices to be operated when implementing a Private Equity structure



(1) *Other legal forms may be envisaged (for available legal forms, please refer to Appendix 1).*
(2) *Article 3 (2) of the AIFM Law.*
(3) *Article 3 (4) of the AIFM Law.*

(4) *2015-2018: Dual Marketing regime.*
- *NPPR + AIFMD on transparency, reporting and controlling entities and partial 3rd country requirements*
- *EU Passport: accessible upon fulfillement of all AIFMD conditions.*

4.2. Luxembourg Private Equity unregulated and regulated structures

Private Equity vehicles in Luxembourg may (i) either be any normal commercial companies (as further detailed under 5.1 below), ie non-regulated structures or (ii) investment structures that are supervised by the Luxembourg *Commission de surveillance du secteur financier* ("CSSF") and therefore regulated structures (as further detailed under 5.2).

The specific (legal) features of all of these structures (non-regulated and regulated alike) are further explained in 5.3 below.

The aforementioned structures may qualify as an alternative investment fund ("AIF") under the Luxembourg implementation of the AIFMD, ie the Luxembourg law on alternative investment fund managers ("AIFM")[1] of 12 July 2013, as amended (the "AIFM Law"). They would then potentially need to appoint an AIFM for the performance of the respective AIF's portfolio and risk management services within the meaning of the AIFM Law.

4.2.1. Non-regulated (standard commercial) companies

Any standard commercial company under the Luxembourg law of 10 August 1915 on commercial companies (the "1915 Law") can be used as a Private Equity structuring vehicle in Luxembourg. These vehicles may either be intermediate holding vehicles for an entity located abroad (typically a non-European Private Equity fund) or be themselves the investment vehicle for the end investors/ beneficial owners of the structure.

To the extent that the corporate object of that vehicle is limited to the holding of participations in other (asset holding) companies (be it in Luxembourg or abroad) the most common non-regulated Private Equity structure in Luxembourg is the SOPARFI. SOPARFIs are ordinary commercial companies (in principle able to take any corporate form available under the 1915 Law, while in practice this often will be a private limited company, i.e. a *société à responsabilité limitée*, S.à r.l. or a simplified limited company, i.e. a *société par actions simplifiée*, S.A.S.) governed by the 1915 Law.

As an ordinary company, the SOPARFI is not subject to any risk-spreading requirements and may in principle invest in any asset class. SOPARFIs are used to invest and manage financial participations in Luxembourg or foreign companies. SOPARFIs can also undertake commercial activities which are directly or indirectly connected to the management of their holdings including the debt servicing of their acquisitions.

The Luxembourg law which implemented the AIFMD, revamped and updated the legal framework for limited partnerships under the 1915 Law, ie the *société en commandite simple* (SCS). In addition, the law implementing the AIFMD also added another form of limited partnership under Luxembourg law, ie *the société en commandite spéciale* (SCSp), which, unlike the SCS, does not have legal personality itself. Both vehicles have increasingly been used for structuring private equity investments. Records of the Luxembourg trade register show that by June 2016, 1165 SCS or SCSp have been set up since its introduction in July 2013, seemingly substituting the former vehicle of choice, the S.à r.l.. While the principal reasons for choosing the legal form of a Luxembourg private equity structuring vehicle may often be driven by considerations of applicable foreign (tax) law, the increased structuring flexibility of the SCS or the SCSp. The limited partnership agreement will fix their operating rules and its tax-transparent status (under Luxembourg tax law and subject to appropriate structuring under applicable foreign tax law, to the extent applicable) has added to its increased popularity.

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[1] *According to article 1 (39) of the AIFM law, an AIF is any collective investment undertaking, including investment compartments thereof, which: (a) raise capital from a number of investors, with a view to investing it in accordance with a defined investment policy for the benefit of those investors; and (b) do not require authorisation pursuant to Article 5 of Directive 2009/65/EC;*

Reserved alternative investment fund - RAIF

On 14 July 2016, bill of law n°6929 on reserved alternative investment funds ("RAIFs") was adopted by the Luxembourg Parliament. Its purpose is to introduce a new type of Luxembourg investment vehicle that is reserved to Luxembourg alternative investment funds ("AIFs") managed by an authorised external alternative investment fund manager ("AIFM") within the meaning of Directive 2011/61/EU of 8 June 2011 on alternative investment fund managers (the "AIFMD").

To a large extent, the RAIF vehicle offers similar structuring flexibilities as Luxembourg specialised investment funds ("SIFs"). However, in contrast to SIFs, RAIFs are not subject to supervision of the Luxembourg supervisory authority of the financial sector (the "CSSF").

RAIFs are Luxembourg AIFs governed by the Luxembourg law of 23 July 2016 on RAIFs (the "RAIF Law").

In addition, RAIFs adopting a corporate form are, unless it is derogated therefrom by the RAIF Law, subject to the general provisions of the 1915 Law.

Moreover, as RAIFs qualify as AIFs managed by a duly authorised AIFM subject to the full AIFMD requirements, RAIFs will be subject to the so-called "AIFMD Product Rules" applicable to them. These AIFMD Product Rules include, among others, specific AIFMD requirements in terms of (i) appointment of the RAIF's depositary, (ii) appointment of the RAIF's approved statutory auditor, (iii) minimum content of the RAIF's annual report, (iv) valuation of the RAIF's assets, and (v) investment and leverage rules regarding certain type of assets. However, in exchange for complying with all the conditions laid down in the AIFMD and provided that their AIFM is fully licensed, RAIFs may benefit from the AIFMD passport under certain conditions in order to be marketed to professional investors (and retail investors if permitted by the relevant Member States) in the EU.

4.2.2. Directly regulated or indirectly supervised structures

The CSSF regulates SICARs and SIFs. SIFs are regulated under the provisions of the law of 13 February 2007 on specialised investment funds (the "SIF Law") while SICARs are regulated under the provisions of the amended law of 15 June 2004 (the "SICAR Law") on investment companies for risk capital investment. Both SICARs and SIFs are registered on official lists maintained by and accessible on the website of the CSSF. SIFs and SICARs would typically also qualify as AIFs under the AIFM Law.

Amidst an international regulatory environment seeking to increase transparency and oversight the SICAR and the SIF are tried-and-tested regulated Private Equity frameworks. The legal framework applicable to SICARs and SIFs offers a combination of a flexible and accessible regulatory infrastructure with strong investor protection features. They can only be subscribed to by "well-informed" investors (see the Glossary for a more detailed definition).

As of 31 December 2016 the number of 384 SICARs comprising in total a volume of EUR 40.2 billion and the number of 1,639 SIFs comprising a total amount of EUR 424.4 billion were registered with the CSSF.

SICAR

SICARs are investment vehicles designed specifically to suit the needs of Private Equity and Venture Capital. SICARs allow direct or indirect contributions of assets to be made to entities in view of their launch, development or listing on a stock exchange.

SIF

SIFs were created to replace a predecessor regime which was no longer suitable. In particular, with Luxembourg starting to position itself as an alternative funds domicile, the time was ripe for a complete overhaul of the then existing legal and regulatory framework. The SIF regime was thus created in 2007 in order to clearly establish Luxembourg as an AIF domicile further accommodating all alternative asset classes and hedge funds, real estate funds and private equity funds in particular.

The unregulated SCS and SCSp can be converted into a regulated SIF or SICAR at any time. Advantages of starting off with an unregulated fund are:

- Quick set-up as no CSSF approval needed;
- No depositary needed (cost savings);
- Contractual relationship means that parties have freedom to negotiate contractual contents, no regulation prescribes any rules. Note, however, that the costs for setting up legal documents is slightly higher than for an SCS/SCSp in the form of a SIF or SICAR as all details have to be defined individually and negotiated with the signees.
- When the unregulated SCS or SCSp has reached a certain volume and/or more external fundraising is foreseen, it may be interesting to (i) convert the SCS/SCSp into a regulated SIF or SICAR (regulation on fund level) and (ii) nominate an alternative investment fund manager (AIFM) under the AIFMD regime (regulation on the manager level) to benefit from the distribution freedom in the EU under the AIFMD regime.

4.3. Features of Luxembourg Private Equity vehicles

<table>
<tr><th>SIF (CSSF regulated)</th><th>SICAR (CSSF regulated)</th><th>SOPARFI (unregulated)</th><th>RAIF (indirectly supervised by its AIFM)</th></tr>
<tr><td colspan="2">■ In principle always qualifies as an alternative investment fund (AIF) under the AIFM Law (unless single investor)
■ De minimis AIF possible
■ Internal management under the AIFM Law possible</td><td>■ May qualify as an alternative investment fund (AIF) under the AIFM Law
■ De minimis AIF possible
■ Internal management under the AIFM Law possible</td><td>■ Alternative investment fund (AIF) qualification under the AIFM Law mandatory
■ Not admitted for de minimis AIF
■ Not admitted for internal management under the AIFM Law</td></tr>
<tr><td>Choice of legal form:
Corporate vehicles
■ Public limited company (S.A.)
■ Simplified limited company (S.A.S.)
■ Private limited company (S.à r.l.)
■ Corporate partnership limited by shares (S.C.A.)
■ Common limited partnership (S.C.S.)
■ Special limited partnership (S.C.Sp.)

The aforementioned corporate vehicles will all qualify as investment companies with variable capital (société à capital variable, SICAV), ie their capital will be allowed to increase or decrease freely without the need to convene a shareholders' meeting to that effect.</td><td colspan="3">Choice of legal form:
Corporate vehicles
■ Public limited company (S.A.)
■ Simplified limited company (S.A.S.)
■ Private limited company (S.à r.l.)
■ Corporate partnership limited by shares (S.C.A.)
■ Common limited partnership (S.C.S.)
■ Special limited partnership (S.C.Sp.)</td></tr>
<tr><td>Choice of legal form:
Contractual form
common fund (FCP-SIF)</td><td colspan="2">N/A</td><td>Choice of legal form:
Contractual form
common fund (FCP-RAIF)</td></tr>
<tr><td>Tax Treatment
Transparent:
■ Common fund (FCP-SIF)
■ Common limited partnership (S.C.S.)
■ Special limited partnership (S.C.Sp.)

Not transparent (all vehicles in principle taxable in Luxembourg):
All corporate forms (see above)

For all vehicles mentioned in this box, the SIF regime applies as set out below (other than that there is no other direct taxation in Luxembourg).</td><td colspan="2">Tax Treatment
Transparent:
■ Common limited partnership (S.C.S.)
■ Special limited partnership (S.C.Sp.)

Not transparent (taxable vehicle in Luxembourg):
All corporate vehicles (see above). All these corporate vehicles are otherwise fully taxable in Luxembourg.</td><td>Tax Treatment
Transparent:
■ Common fund (FCP-RAIF)
■ Common limited partnership (S.C.S.)
■ Special limited partnership (S.C.Sp.)

Not transparent (taxable vehicle in Luxembourg):
All corporate vehicles (see above). All these corporate vehicles are otherwise fully taxable in Luxembourg (except if they opt for the special tax status outlined in the next box below similar to the SIF and SICAR regimes only available to RAIFs).</td></tr>
</table>

<table>
<tr><th>SIF (CSSF regulated)</th><th>SICAR (CSSF regulated)</th><th>SOPARFI (unregulated)</th><th>RAIF (indirectly supervised by its AIFM)</th></tr>
<tr><td>SIF regime, i.e. vehicles respecting the principle of risk spreading (CSSF Circular 07/309):
■ Annual subscription tax (taxe d'abonnement) at a rate of 0.01%
■ Some SIFs are exempted from the subscription tax
■ SIFs are not subject to any Luxembourg taxes on capital gains or income
■ The corporate vehicles may in principle benefit from certain double tax treaties</td><td colspan="2"></td><td>SIF regime for RAIF respecting the principle of risk spreading (mutatis mutandis CSSF Circular 07/309):
■ Annual subscription tax (taxe d'abonnement) at a rate of 0.01%
■ Some SIF-RAIFs are exempted from the subscription tax
■ SIF-RAIFs are not subject to any Luxembourg taxes on capital gains or income
■ The vehicle should in principle benefit from certain double tax treaties</td></tr>
<tr><td></td><td colspan="2">SICAR regime for funds investing in risk capital (CSSF Circular 06/241):
■ Subject to income tax in Luxembourg, but any income arising from securities held by the SICAR does not constitute taxable income
■ May benefit from certain double tax treaties
■ Capital gains realised by non-Luxembourg residents are not subject to tax in Luxembourg
Dividend and interest payments paid are exempt from withholding tax</td><td>SICAR regime for RAIF investing in risk capital (mutatis mutandis CSSF Circular 06/241):
■ Subject to income tax in Luxembourg, but any income arising from securities held by the SICAR does not constitute taxable income
■ May benefit from certain double tax treaties
■ Capital gains realised by non-Luxembourg residents are not subject to tax in Luxembourg
■ Dividend and interest payments paid are exempt from withholding tax</td></tr>
<tr><td colspan="4">Duration
Unlimited or limited period of time</td></tr>
<tr><td colspan="4">Form of securities
■ (Registered) shares or units (FCP-FIS/SIF or FCP-FIAR/RAIF): ordinary, preference, beneficiary (the latter not for SIF)*
■ Partnership interests (for S.C.S and S.C.Sp.)
■ Redeemable
■ Voting and non-voting (only voting for SIF)
■ Bonds and/or notes

* issuance of registered shares of any vehicle recommended in order to ensure proper management of eligible investors (i.e. professional investors to the extent vehicle qualifies as an AIF)</td></tr>
<tr><td colspan="4">Listing
Possible (only for S.A., S.C.A., FCP-SIF and FCP-RAIF)</td></tr>
<tr><td colspan="4">Redemption
Possible though unlikely in a PE/VC context</td></tr>
</table>

<table>
<tr><th>SIF (CSSF regulated)</th><th>SICAR (CSSF regulated)</th><th>SOPARFI (unregulated)</th><th>RAIF (indirectly supervised by its AIFM)</th></tr>
<tr><td colspan="2">Capital calls/Distributions
Capital calls and distributions to investors are subject solely to the rules provided for in the constitutive documents

Flexibility on issue price (except where NAV calculation in specific cases)
Preferential rights may be limited or cancelled</td><td colspan="2">Capital calls/Distributions
Capital calls and distributions to investors are subject to the rules provided in the constitutive documents

Flexibility on issue price
Preferential rights may be limited or cancelled</td></tr>
<tr><td>Permissible asset classes
asset classes as set out in SIF law (as amended by RAIF law)</td><td>Restricted asset classes
Investment in risk capital (according to definition of “risk capital” in CSSF Circular 06/241)</td><td colspan="2">Permissible asset classes
Any kind of asset class</td></tr>
<tr><td>Risk spreading
Risk diversification requirement (as contained in CSSF Circular 07/309)</td><td colspan="3">Risk spreading
No risk diversification requirement

i.e. as long as an SCS/SCSp remains unregulated, no need for risk diversification.
If the SCS/SCSp is converted into a SIF, diversification is required, if converted into a SICAR, also no need for risk diversification.</td></tr>
<tr><td colspan="2">Compartments/Sub-funds
Possible</td><td>Compartments
Not possible</td><td>Compartments/Sub-funds
Possible</td></tr>
<tr><td>Capital
■ Fixed or variable EUR or foreign currency equivalent
■ Minimum of EUR 1,250,000 (including share premium), to be reached within 12 months of authorisation provided at incorporation
■ Minimum of EUR 12,000 for S.à r.l. and EUR 30,000 for S.A./S.C.A.
■ Partly paid shares must be paid up to at least 5%
■ No restriction for S.C.S./S.C.Sp.
■ Contribution in kind and/or in cash permissible
■ Commitment or subscription based model.</td><td>Capital
■ Fixed or variable EUR or foreign currency equivalent
■ Minimum of EUR 1,000,000 (including share premium) to be reached within 12 months of authorisation, provided at incorporation
■ Minimum of EUR 12,000 for S.à r.l. and EUR 30,000 for S.A./S.C.A.
■ Shares must be paid up to at least 5%
■ No restriction for S.C.S. or S.C.Sp.
■ Contribution in kind and/or in cash permissible
■ Commitment or subscription based model.</td><td colspan="2">Capital
■ Fixed or variable EUR or foreign currency equivalent
■ Minimum of EUR 12,500 for S.à r.l. and EUR 31,000 for S.A./S.C.A. at incorporation only
■ Shares must be paid up to 25% for S.A./S.C.A. and 100% for an S.à r.l. No restriction for S.C.S. or S.C.Sp.
■ Contribution in kind and/or in cash permissible
■ Commitment or subscription based model

Note: no share capital for SCS/SCSp</td></tr>
<tr><td colspan="2">Management bodies
■ Board of directors, manager(s) or managing general partner – dependent on corporate form
■ Approval of board members by the CSSF.</td><td colspan="2">Management bodies
■ Board of directors, manager(s) or managing general partner – dependent on corporate form
■ No approval requirements for board members by the CSSF.</td></tr>
<tr><td>Supervisory reporting
■ Monthly reporting
■ Annual audited report due 6 months after year end.</td><td>Supervisory reporting
■ Semi-annual reporting
■ Annual audited report due 6 months after year end.</td><td>Supervisory reporting
■ Not applicable (as long as the SCS/SCSp does not nominate an AIFM who needs to report on each fund it manages).</td><td>Supervisory reporting
AIFM supervised by responsible authority to report on RAIFs it externally manages.</td></tr>
</table>

SIF (CSSF regulated)	SICAR (CSSF regulated)	SOPARFI (unregulated)	RAIF (indirectly supervised by its AIFM)
Filing requirements with trade register Within 7 months after year end, audited annual accounts and appendix have to be filed.	**Filing requirements with trade register** Within 7 months after year end, audited annual accounts have to be filed.	**Filing requirements with trade register** Within 7 months after year end, annual accounts have to be filed.	**Filing requirements with trade register** Within 7 months after year end, annual accounts have to be filed. **RAIF List** RAIF will have to be registered on RAIF list kept by RCS
Depositary Luxembourg depositary required (regardless of AIF qualification)		**Depositary** Not required unless the relevant entity qualifies as an AIF, which is not a de minimis AIF	**Depositary** Luxembourg depositary required for RAIF
Administrator Administrator to be appointed unless own infrastructure		**Administrator** Administrator unless own Luxembourg infrastructure	**Administrator** Administrator to be appointed unless own infrastructure
Auditor Independent approved Luxembourg auditor required		**Auditor** Independent Luxembourg auditor in certain circumstances only (i.e. there is no audit requirement for an unregulated SCS/SCSp as long as not submitted to the AIFMD regime by appointing an AIFM)	**Auditor** Independent approved Luxembourg auditor required

4.4. Structuring by means of Luxembourg vehicles

The following examples illustrate how PE investments could be structured via of a variety of Luxembourg vehicles, including options to locate PE funds themselves in Luxembourg.

Luxembourg structures typically consist of either a SOPARFI, an unregulated S.C.S./ S.C.Sp, a SICAR or SIF or of a combination of the latter two with one or more SOPARFIs.

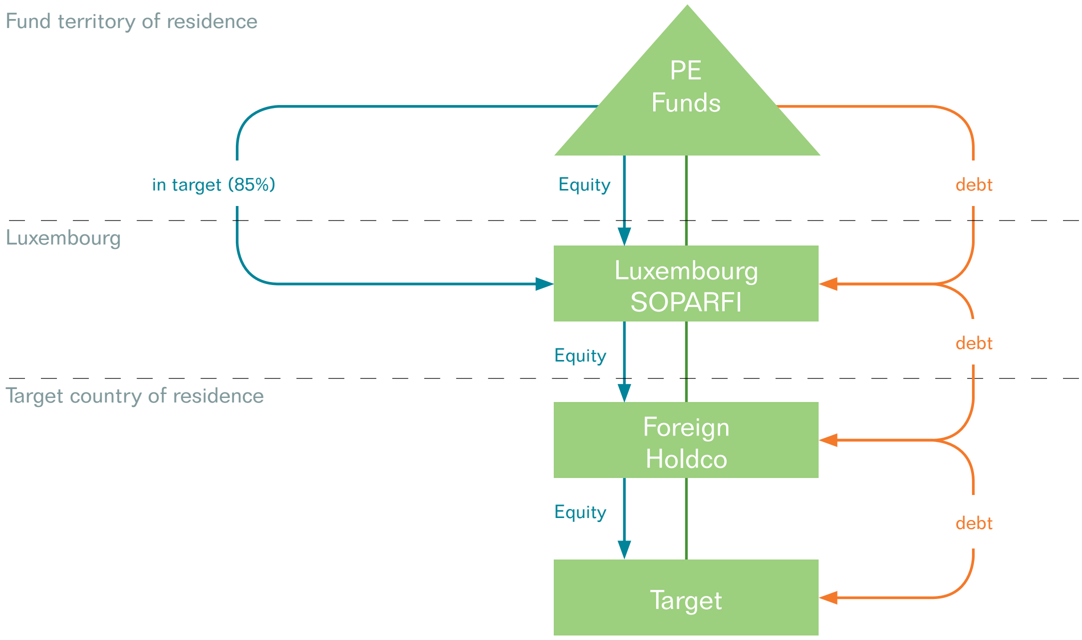
In the case of an FCP (SIF or RAIF), S.C.S. and S.C.Sp. qualifying as a tax transparent structure the use of intermediate companies is usually recommended to benefit from double tax treaties and EU directives that only companies can benefit from, unlike an FCP.

Investors can invest either directly into the Luxembourg vehicle or indirectly via an additional Luxembourg-based or non-Luxembourg-based feeder vehicle.

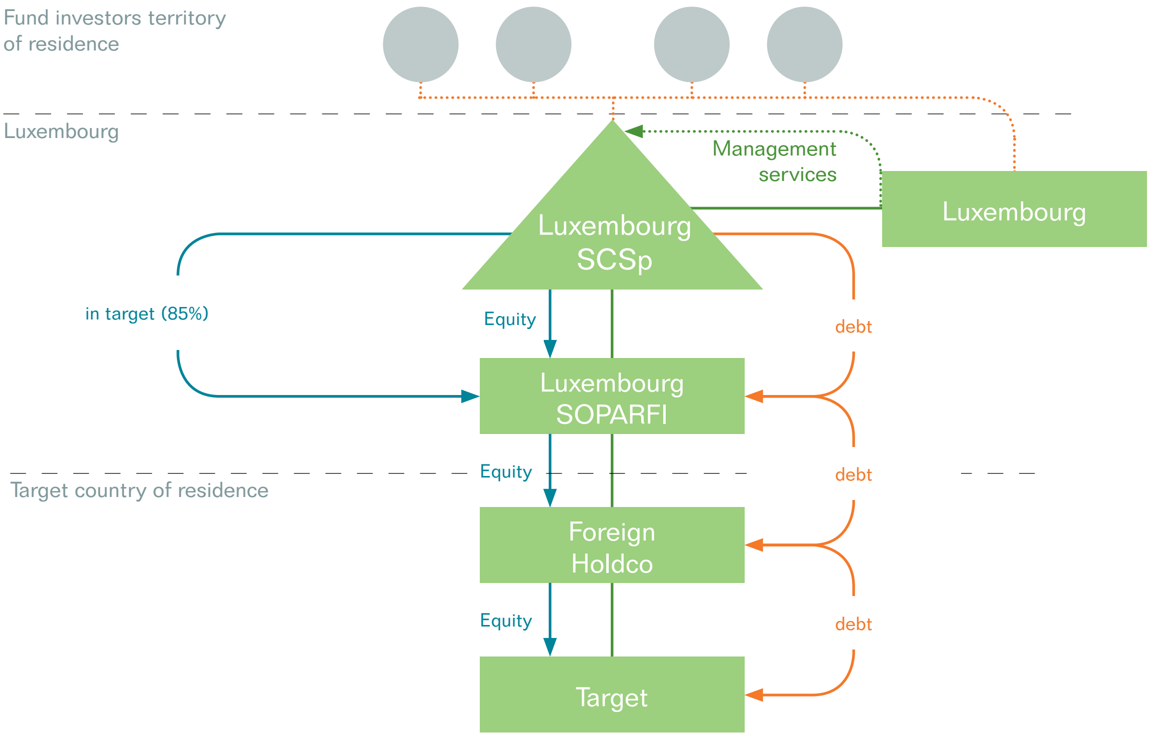
The following charts are examples of typical Luxembourg Private Equity structures:

Direct investment or via a Luxembourg or non-Luxembourg based feeder vehicle into a Luxembourg SOPARFI: the SOPARFI, possibly via a second SOPARFI, invests into a local target company.

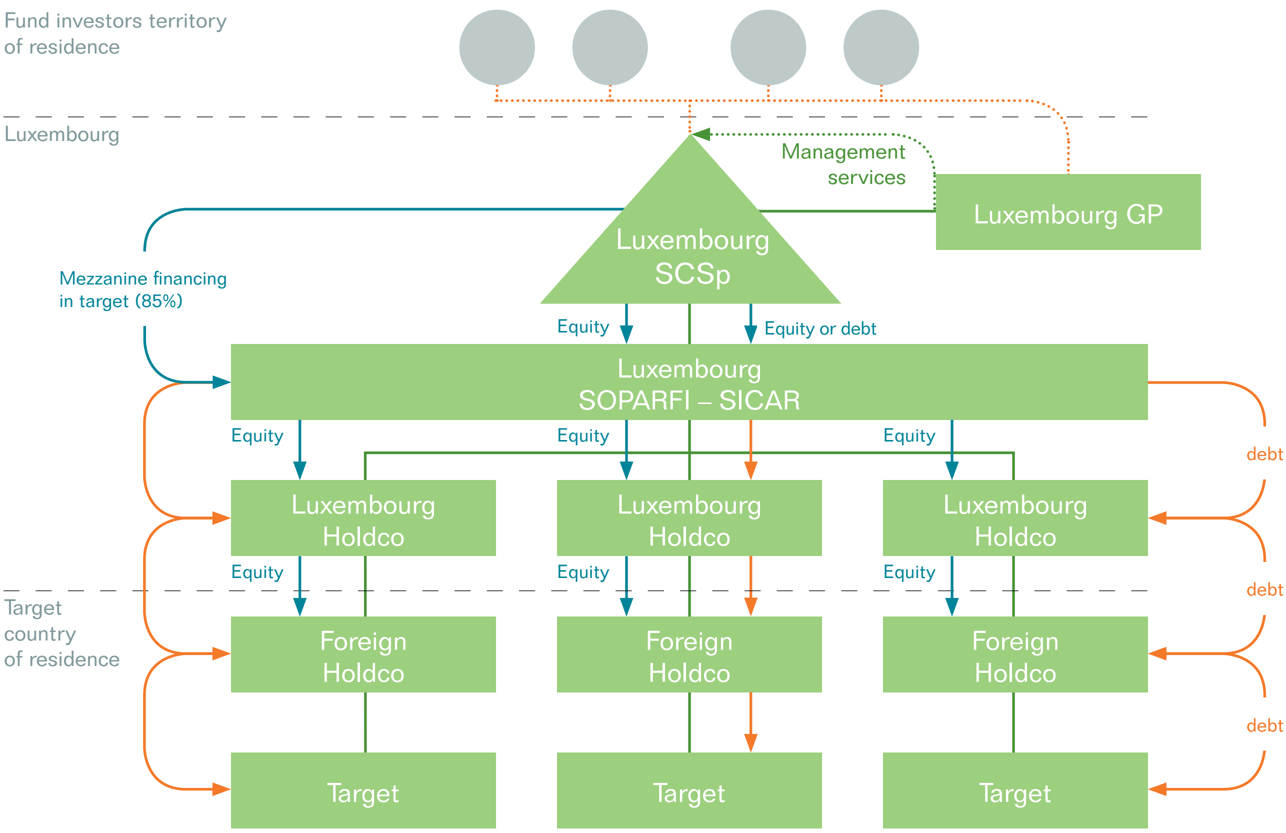
Example 1: traditional investment via a Luxembourg SOPARFI



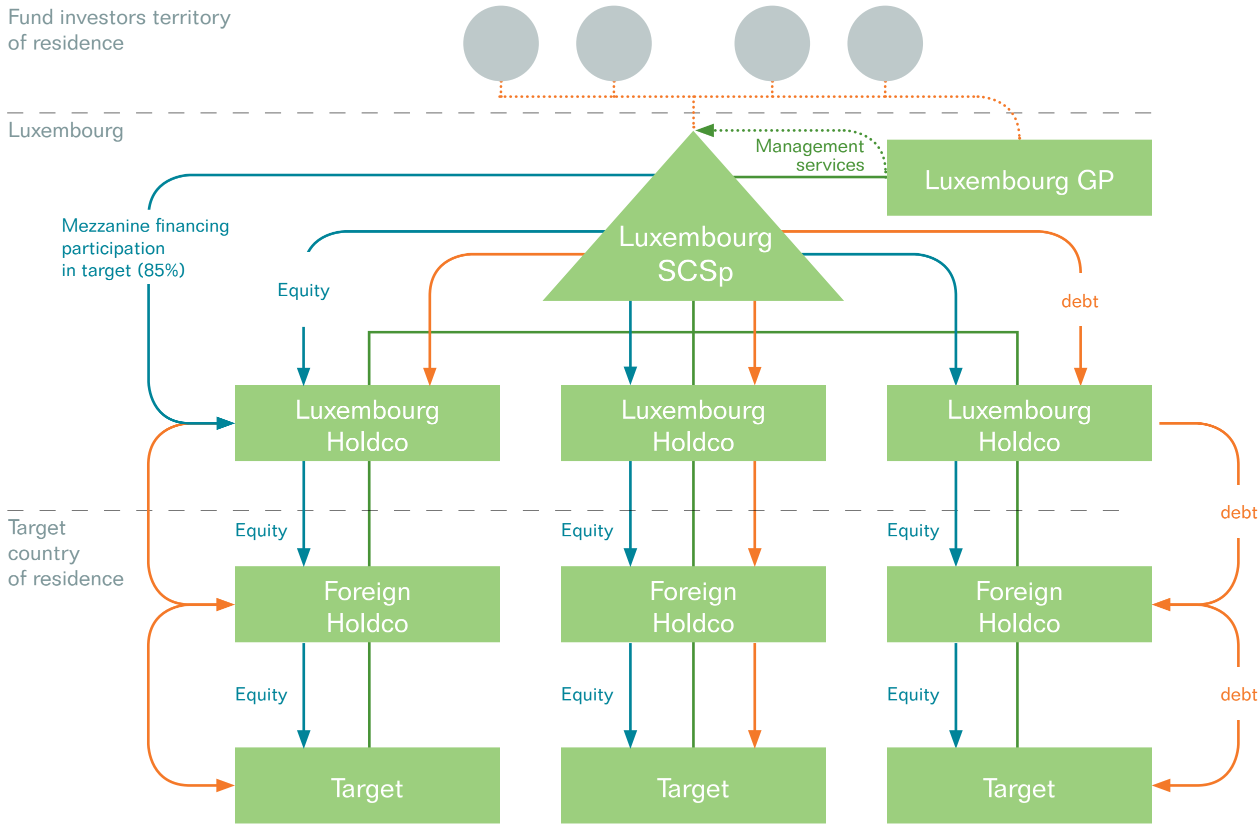
Example 2: investment via Luxembourg an S.C.Sp. and a SOPARFI



Example 3: investment via Luxembourg S.C.Sp. and a SOPARFI, SICAR or SIF with a Luxembourg General Partner



Example 4: investment via foreign feeder entities into Luxembourg S.C.Sp. and several Luxembourg SOPARFI



5. Accounting framework for Luxembourg private equity vehicles

5.1. Accounting Standards and audit requirements

With the exceptions of the Contractual Joint Venture (“S.N.C.”), the Partnership limited by Shares (whose annual turnover does not exceed EUR 100,000 ex-VAT and whose partners with unlimited liability are not all limited liability companies) as well as the Special Limited Partnership, companies can elect any accounting framework. All Luxembourg vehicles may choose to adopt Luxembourg Generally Accepted Accounting Principles (“Lux GAAP”) or International Financial Reporting Standards (“IFRS”) as adopted by the EU. In addition, with the specific approval from the local Accounting Standards Board a company may use any alternative internationally accepted accounting framework such as US GAAP. In practice, the standalone annual accounts of Luxembourg Private Equity vehicles are very frequently prepared under Lux GAAP whereas consolidated annual accounts (whether legally required – see below – or contractually required – for example through the raising of external financing) are frequently prepared under IFRS as adopted by the EU. Through its international exposure, Luxembourg service providers have in most cases significant experience in the application of IFRS.

Note that while most companies are required to prepare annual accounts there are specific size thresholds that will determine if an audit by an approved statutory auditor under International Standards on Auditing (“ISA”) is required by law.

5.2. Valuation Rules

As a general rule, Luxembourg accounting rules have always been a primarily prudence-focused framework permitting the booking of investments at cost less durable impairment with the recognition only of unrealised losses and not of unrealised gains in the profit and loss accounts of a company. In recent years, with the creation of vehicles such as the SICAR and the SIF and with the harmonisation derived from recent EU accounting directives, the possibility of using fair value in the financial statements of Luxembourg companies has been introduced. Depending upon the corporate structure and nature of a private equity vehicle different valuation principles are thus allowed.

Companies adopting IFRS as an accounting framework have to apply valuation policies depending on the type of instruments being valued. Under Lux GAAP there is a certain level of additional flexibility and possible choices as outlined in the table below:

Type of vehicle/ Regulatory framework	Valuation under Lux GAAP
Unregulated S.C.S. and S.C.Sp.	The valuation rules to follow can be freely determined in the partnership agreement. In practice, these rules will follow internationally recognised principles for determining fair value (see below).
Other unregulated vehicle	Valuation rules are governed by the Law of 19 December 2002, as amended. **There are two valuation options:** a) Acquisition cost/principal less any durable impairment b) Fair Value. The choice of which method to use rests with the management of the company. As a general rule, companies tend to adopt option a).
SICAR, SIF	SICARs are obliged to account for their investments at fair value. SIFs are also required to account for investments at fair value unless their constitutional documents specify otherwise. Generally the prospectus, Private Placement Memorandum (“PPM”) or the Offering Memorandum (“OM”) will contain more detailed explanations with regard to the valuation methodologies adopted.

The International Private Equity and Venture Capital ("IPEVC") guidelines are typically used as a reference basis for calculating the fair value of private equity type investments.

5.3. Consolidation

5.3.1. Unregulated Vehicles

Principles: Luxembourg law requires that limited liability companies, as well as the S.N.C. and the S.C.S. whose partners with unlimited liability are all limited liability companies that control another company prepare and publish consolidated financial statements. S.C.Sp. are not required to produce consolidated financial statements. If consolidated annual accounts are required, most companies ensure today that their preparation is actually done in Luxembourg, either internally or through specialised service providers.

Consolidation exemptions are foreseen in the following cases:

■ **Exemptions**

1. **Sub-group exemption:** any parent company which is also a subsidiary undertaking of a parent undertaking may be exempted from the obligation to draw up consolidated accounts and a consolidated annual report under certain conditions. The parent undertaking might be governed by the law of a Member State of the EU or not, but different conditions apply. This exemption is not applicable if the Luxembourg parent company has its securities (shares and/or bonds) listed on an EU regulated market.
2. **Threshold exemption:** consolidation is not required for consolidated groups which do not exceed the following metrics: balance sheet total: EUR 17.5m / total turnover: EUR 35m / total employees: 250. However, the "threshold exemption" is not applicable in case the relevant company has its securities (shares and/or bonds) listed on an EU regulated market.
3. **Financial Holding exemption:** no consolidation is required if the parent company has not intervened in the management of the subsidiary, has not exercised its voting rights in respect of the appointment of the management within the current and the last 5 years, has not granted loans to the subsidiary and, if the conditions were met, has received an exemption granted by the Luxembourg authorities. This exemption is quite rare in practice.

■ **Exclusions**

Specific investments may be excluded from the consolidation requirement if they meet one of five possible exclusions as set out by the 1915 Law. These are: immateriality, severe restrictions or disproportionate costs on obtaining financial information, subsequent resale or diverging activities.

However, in these cases, the consolidated accounts will still have to be published in Luxembourg according to the local requirements and the notes to the annual accounts of the excluded company must disclose the name and registered office of the parent undertaking and the exemption from the obligation to draw up consolidated accounts and a consolidated annual report.

Specific application of the "subsequent resale" exclusion for private equity holding vehicles: In December 2009, the Luxembourg Ministry of Justice, through the Accounting Standards Board, issued a recommendation relating to the "subsequent resale" exclusion that allows private equity companies (for which all their subsidiaries are held for subsequent resale) not to present consolidated financial statements in case six conditions are fulfilled:

- The company is subject to the 1915 Law and is held by one or more well-informed investor(s);
- The company's exclusive corporate object is to invest in risk capital, which is defined as direct or indirect contribution of funds to one or several entities in view of their launch, development and their listing on a stock exchange. These investments are held with the intention to sell them at a profit;
- An ex-ante exit strategy has been formally defined and documented in writing,

communicated to investors, and it is part of the investment policy, implying the intention to divest on a mid-term basis (generally 3 to 8 years);
- The company's objective is to provide its investors with the benefit of the results of the management of its investments in return for the risk which they incur;
- If the investments are not carried at fair value on the face of the balance sheet, the fair value is disclosed in the notes to the financial statements;
- Any event, guarantee or uncertainty that might have a significant impact on the entity's ability to continue as a going concern, on its cash-flow situation, on its available liquidities or on its solvency has to be disclosed adequately in the notes to the annual accounts.

■ **IFRS Exemption from Consolidation**
Under IFRS 10, an entity is exempted from consolidating its subsidiaries if it qualifies as an "investment entity".

An investment entity is defined as an entity that:

- Obtains funds from one or more investors for the purpose of providing those investor(s) with investment management services;
- Commits to its investor(s) that its business purpose is to invest funds solely for returns from capital appreciation, investment income or both and;
- Measures and evaluates the performance of substantially all of its investments on a fair value basis.

An investment entity is however obliged required to account for its investments at fair value through profit or loss.

It is important to note that the determination as to whether a company is in scope of the investment entity exemption under IFRS 10 is a significant judgement and will be impacted by the way the Private Equity investment(s) is (are) managed from Luxembourg.

5.3.2. Regulated Vehicles (SICARs and SIFs)

The SICAR and the SIF are specifically exempted by law from the consolidation requirement.

5.4. Profit Repatriation

Through the use of appropriate financial instruments and an adequate regulated or non-regulated structure, the tax charge levied on profit repatriation can be minimised both at investment level and investor level.

(RAIF)-SIF (regulated)	SICAR (regulated)	SOPARFI (unregulated)
Distribution of dividends(*) Not subject to specific restrictions except compliance with minimal capital requirements and limitations provided for in the articles of incorporation/ management regulations.	**Distribution of dividends(*)** Not subject to specific restrictions except compliance with minimal capital requirements and limitations provided for in the articles of incorporation.	**Distribution of dividends** For S.A., S.A.S., S.C.A. and S.à r.l. subject to the requirements of the 1915 Law.
Withholding tax on distributions Distributions, whether paid to resident or non-resident investors, are not subject to withholding tax in Luxembourg.	**Withholding tax on distributions** Distributions, whether paid to resident or non-resident investors, are not subject to withholding tax in Luxembourg.	**Withholding tax on distributions** Except for specific situations, no withholding tax should apply to liquidation proceeds or interest payments. Dividend payments are subject to 15% withholding tax (exemptions are available under certain conditions).
Non resident capital gains taxation Non-residents are not subject to capital gains tax in Luxembourg.		

(*) For vehicles with variable capital, the Luxembourg manager should pay attention to the qualification of distributions between return of capital and income. This analysis should take into account the specific tax situation of the investors in the various countries in which they are tax residents.

Appendix I – comparative table of legal structures

The following tables provide a comparison of the main features of the most popular corporate forms:

	Public limited company (SA)	Simplified limited company (S.A.S)	Private limited company (Sàrl)	Corporate partnership limited by shares (SCA)	Common/special Limited partnership (SCS/SCSp)
Incorporation	Notarial deed required	Notarial deed required	Notarial deed required	Notarial deed required	Notarial deed not required
Minimum capitalisation (at incorporation/ launching) (EUR or equivalent in another currency)	EUR 30,000	EUR 30,000	EUR 12,000	EUR 30,000	No capital required
Shares/interests/ beneficiary units/capital accounts	Dematerialised, registered or bearer, voting or non-voting shares, beneficiary units (with or without voting rights)	Dematerialised, registered or bearer, voting or non-voting shares, beneficiary units (with or without voting rights)	Registered shares only, beneficiary units (with or without voting rights)	Dematerialised, registered or bearer, voting or non-voting shares, beneficiary units (with or without voting rights)	Registered partnership interests only or capital accounts
"Tracking shares"	Yes	Yes	Yes	Yes	Yes (subject to terms of the partnership agreement)
Share Classes	Yes	Yes	Yes	Yes	Yes
Shareholders	≥1	≥1	1 to 100	Limited partners: ≥ 1 Unlimited partners: ≥ 1	Limited partners: ≥ 1 Unlimited partners: ≥ 1
Transfer of shares/ interests	Free, subject to restrictions set out in articles of incorporation	Free, subject to restrictions set out in articles of incorporation	Subject to certain conditions being shareholders' prior consent	Shares of limited partners freely transferable – shares of unlimited partners transferable subject to certain conditions	Freely determined by the partnership agreement
Liabilities	Shareholders' liability is limited to the amount of their participation	Shareholders' liability is limited to the amount of their participation	Shareholders' liability is limited to the amount of their participation	Limited partners' liabilities: Limited to the amount of their participation Managing general partner(s)' liability: Unlimited	Limited partners' liabilities: Limited to the amount of their participation Managing general partner(s)' liability: Unlimited
Listing of shares	Yes	No	No	Yes	No

	Public limited company (SA)	Simplified limited company (S.A.S)	Private limited company (Sàrl)	Corporate partnership limited by shares (SCA)	Common/special Limited partnership (SCS/SCSp)
General meeting	1 annual general meeting required	Modalities freely set in the articles of incorporation	1 annual general meeting required if the number of members/ partners is ≥60	1 annual general meeting required	Modalities freely set in the partnership agreement
Management	One-tier management structure with a board of ≥3 directors (if there is more than one shareholder) or two-tier management structure with a management board and a supervisory board Possibility to put in place an executive committee or a chief executive, a daily manager, ad hoc committee	Managed by a chairman (president) possibility to delegate the chairman's powers to one or more officers (directors)	≥1 manager If several managers, may be structured as a board, possibility to put in place a daily manager, ad hoc committee	≥1 manager which does not have to be an unlimited partner	≥1 manager which does not have to be an unlimited partner
Amendments to constitutive documents	By a quorum representing at least 1/2 of the share capital at first call and a 2/3 majority of shareholders	Quorum and majority freely set in the articles of incorporation	By a majority of the shareholders representing at least 3/4 of the share capital	Same as the S.A., but the unlimited partner has a veto right (unless contrary provision in the articles of incorporation)	By all the partners, unless otherwise provided in the partnership agreement
Accounts	Annual	Annual	Annual	Annual	Limited accounting obligation
Statutory auditor	Required	Required	Required only if the number of partners is ≥60	Required only for large companies	Required only for large companies
Independent auditor's report	Required if certain size thresholds are exceeded	Required if certain size thresholds are exceeded	Required if certain size thresholds are exceeded	Required if certain size thresholds are exceeded	Required if certain size thresholds are exceeded

AIF	Alternative Investment Fund as defined in the AIFMD Law
AIFMD	Directive 2011/61/EU of the European Parliament and of the Council of 8 June 20111 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010
AIFMD Law	The Law of 12 July 2013 implementing Directive 2011/61/EU into Luxembourg law, as amended
Capital Call	Written notice to Limited Partners requesting them to make a capital contribution to the fund vehicle (within the limits of their subscription commitment) in order to permit the fund vehicle to pay for its investments or to pay expenses
Carried Interest	Carried interest or carry is a share of the profits of the fund vehicle that is paid to the general partner and/or the investment manager/advisor in excess of the amount that the general partner/manager/advisor contributes to the fund vehicle. In order to receive carried interest, the fund vehicle must first return all capital contributed by the investors, and, in certain cases, the fund must also return a previously agreed-upon rate of return (the “hurdle rate” or “preferred return”) to investors
CSSF	*Commission de Surveillance du Secteur Financier*, the Luxembourg supervisory authority of the financial services sector
FCP	*Fonds Commun de Placement*, an undivided co-ownership of assets or proprietorship managed by a management company
GP	The general partner of either a corporate partnership limited by shares (S.C.A.), a common limited partnership (S.C.S.) or a special limited partnership (S.C.Sp.). The managing general partner is normally jointly and severally liable with the partnership for any liabilities which may not be satisfied out of partnership assets
IFRS	International Financial Reporting Standards
1915 Law	Law of 10 August 1915 on commercial companies, as amended
LP	The limited partner, typically an investor or limited shareholder in a fund vehicle; limited partners enjoy limited liability (i.e., up to the amount invested or committed for investment)
LPEA	Luxembourg Private Equity & Venture Capital Association
Lux GAAP	Luxembourg Generally Accepted Accounting Principles Most frequently used accounting framework in Luxembourg for PE vehicles
PSF	*Professionnel du Secteur Financier*, a professional of the financial services sector; each PSF is subject to the prior authorisation and ongoing prudential supervision by the CSSF
RAIF	Reserved Alternative Investment Fund, a collective investment scheme governed by the law of 28 July 2016 on reserved alternative investment funds
RCS	*Registre de Commerce et des Sociétés*, the Luxembourg register of commerce and companies
S.A.	*Société Anonyme*; Public limited liability company
S.à r.l.	*Société à Responsabilité Limité* ; private limited liability company
S.A.S.	*Société par Actions Simplifiée*; simplified limited company
S.C.A.	*Société en Commandite par Actions*; corporate partnership limited by shares

S.C.S.	*Société en Commandite Simple*; common limited partnership
S.C.Sp.	*Société en Commandite Spéciale*, special limited partnership without legal personality introduced into Luxembourg law by the AIFMD Law
SICAR	*Société d'Investissement en Capital à Risque*, investment company investing in risk capital only
SICAV	*Société d'Investissement à Capital Variable*; investment company with variable capital
SIF	Specialized Investment Fund, a collective investment scheme governed by the law of 13 February 2007 on specialised investment funds, as amended
SOPARFI	*Société de Participation Financière*, a mere marketing acronym used to designate an ordinary commercial company governed by the 1915 Law and which is used as a vehicle for holding participations in Luxembourg or foreign companies or other instruments
Subscription Tax	Also: *Taxe d'Abonnement*; a tax of 1 basis point assessed on the net asset value and payable by certain collective investment schemes only
UCI	Undertakings for Collective Investments; collective investment schemes governed by the law of 17 December 2010 relating to undertakings for collective investment, as amended
UCITS	Undertaking for Collective Investments in Transferable Securities; collective investment schemes organized in accordance with Directive 2009/65/EC of the European Parliament and Council of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS)
VAT	Value Added Tax
Well-informed Investor	**For SICAR and SIF:** Institutional investor, professional investor or any other investor who meets the following conditions: a) investor has confirmed in writing that he adheres to the status of well-informed investor, and b) (i) investor invests a minimum of EUR 125,000 in the SIF, or (ii) investor has been the subject of an assessment made by a credit institution within the meaning of Directive 2006/48/EC, by an investment firm within the meaning of Directive 2004/39/EC or by a management company within the meaning of Directive 2009/65/EC certifying investor's expertise, experience and knowledge in adequately appraising an investment in the SIF. **For RAIF:** Institutional investor, professional investor or any other investor who meets the following conditions: a) investor has confirmed in writing that he adheres to the status of well-informed investor, and b) (i) investor invests a minimum of EUR 125,000 in the RAIF, or (ii) investor has been the subject of an assessment made by a credit institution within the meaning of Regulation (EU) No. 575/2013, by an investment firm within the meaning of Directive 2004/39/EC, by a management company within the meaning of Directive 2009/65/EC or by an authorised alternative investment fund manager within the meaning of Directive 2011/61/EU certifying investor's expertise, experience and knowledge in adequately appraising an investment in the RAIF.

About ALFI

The Association of the Luxembourg Fund Industry (ALFI), the representative body for the Luxembourg investment fund community, was founded in 1988. Today it represents more than 1 500 Luxembourg-domiciled investment funds, asset management companies and a wide variety of service providers including depositary banks, fund administrators, transfer agents, distributors, law firms, consultants, tax advisers, auditors and accountants, specialist IT providers and communications agencies.

Luxembourg is the largest fund domicile in Europe and its investment fund industry is a worldwide leader in cross-border fund distribution. Luxembourg-domiciled investment structures are distributed in more than 70 countries around the globe, with a particular focus on Europe, Asia, Latin America and the Middle East.

ALFI defines its mission as to "Lead industry efforts to make Luxembourg the most attractive international centre".

Its main objectives are to:

Help members capitalise on industry trends

ALFI's many technical committees and working groups constantly review and analyse developments worldwide, as well as legal and regulatory changes in Luxembourg, the EU and beyond, to identify threats and opportunities for the Luxembourg fund industry.

Shape regulation

An up-to-date, innovative legal and fiscal environment is critical to defend and improve Luxembourg's competitive position as a centre for the domiciliation, administration and distribution of investment funds. Strong relationships with regulatory authorities, the government and the legislative body enable ALFI to make an effective contribution to decision-making through relevant input for changes to the regulatory framework, implementation of European directives and regulation of new products or services.

Foster dedication to professional standards, integrity and quality

Investor trust is essential for success in collective investment services and ALFI thus does all it can to promote high professional standards, quality products and services, and integrity. Action in this area includes organising training at all levels, defining codes of conduct, transparency and good corporate governance, and supporting initiatives to combat money laundering.

Promote the Luxembourg investment fund industry

ALFI actively promotes the Luxembourg investment fund industry, its products and its services. It represents the sector in financial and in economic missions organised by the Luxembourg government around the world and takes an active part in meetings of the global fund industry.

ALFI is an active member of the European Fund and Asset Management Association, of the European Federation for Retirement and of the International Investment Funds Association.

To keep up to date with all the news from the association and the fund industry in Luxembourg, join us on LinkedIn (The Luxembourg Fund Industry Group by ALFI), Twitter (@ALFIfunds), Youtube, Vimeo or visit our website at www.alfi.lu.

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Luxembourg private equity