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Luxembourg
Private Equity Investment Vehicles

September 2007

Preface

This brochure has been prepared jointly by the *Luxembourg Bankers' Association (ABBL) and the Association of the Luxembourg Fund Industry (ALFI)* in order to provide general background information on the legal and tax aspects of regulated and unregulated private equity vehicles domiciled in the Grand Duchy of Luxembourg.

> Luxembourg offers today a whole platform of services and opportunities to the private equity industry. Products include competitive structures for setting-up private equity funds, such as the SICAR or the SIF, and structures for pan-European private equity acquisitions. Luxembourg based service providers have specialised in servicing the private equity industry and offer today a wide range of customised services in private equity fund and acquisition structuring, transaction advisory, fund administration, custody and audit services.

This publication is intended to provide private equity houses with comprehensive information on Luxembourg's state-of-the-art fund vehicle for private equity, the SICAR, as well as a summary of the key characteristics of other Luxembourg solutions for private equity.

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Private equity industry in Luxembourg

The context

Luxembourg

Benefiting from a flexible tax and legal environment Luxembourg has been recognised for many years as a pre-eminent jurisdiction for structuring private equity funds and private equity deals.

The launch in June 2004 of the SICAR (société d'investissement en capital à risque) as an investment vehicle dedicated to private equity and venture capital is the latest illustration of Luxembourg's commitment to the industry.

Financial centre & investment fund centre

With more than 10,000 fund units and assets under management in excess of EUR 2 trillion at the end of June 2007, Luxembourg is the second most important investment fund domicile in the world after the US. The Luxembourg fund centre is the prime location for the pan-European and global distribution of investment funds.

Alternative investments sector

At the same time Luxembourg has developed a strong track record in alternative investment products and bespoke investment structures such as hedge funds and funds of hedge funds, private equity vehicles, real estate funds, securitisation vehicles and pension pooling.

Private equity

The last years have seen record M&A transactions with massive volume of European deals backed by private equity firms, essentially leveraged buy-outs (LBOs), many of them being structured through Luxembourg investment vehicles. In this respect, Luxembourg may be proud to have joined an important market share of the total funds raised by private equity and venture capital funds.

Traditionally, private equity firms have been adverse to submitting their funds to any specific regulatory framework. This was driven by many legitimate factors such as a need for maximum flexibility to accommodate specific investor requests and a need for privacy over certain aspects of the fund's operation. As such, most of the private equity funds are incorporated in the form of private limited partnerships in jurisdictions such as the United Kingdom, the Channel Islands, Cayman, Bermuda or the State of Delaware in the USA.

Besides the lightly regulated Luxembourg fund structures such as the SICAR and the SIF, SOPARFIs are often used as Luxembourg-domiciled unregulated private equity vehicles. This is because they offer a flexible and efficient tax regime. Even if SOPARFIs are subject to taxes, these vehicles make it possible to manage a private equity investment without significant income and exit tax charges. The tailor-made structuring that can be put into place with SOPARFIs allows private equity partners to have the flexibility of a mere partnership in a corporate body. These vehicles thus provide a combination of flexibility and an efficient tax regime.

There is also an increasing demand from certain types of investors to commit their monies through regulated on-shore private equity funds.

In that respect, Luxembourg offers a choice of both regulated and non-regulated structures that meet the different requirements of a fund sponsor.

Many large private equity houses now have substantial presence in Luxembourg (offices, personnel, accounting, etc) and SOPARFIs are used in many private equity deals such as LBO refinancing or other types of transaction. Luxembourg's efficient vehicles such as the SOPARFI and dedicated vehicles such as the SICAR, combined with the willingness of the Government to promote the private equity business, explain the growing importance gained by Luxembourg year after year in this specific area.

Overview of available structures

The below table provides an overview of the Luxembourg structures which are available for private equity and venture capital investments. While the SICAR is the premier private equity/venture capital vehicle *per se*, other structures analysed herein may also be used as fund vehicles to host private equity investments, under certain conditions. The SOPARFI is further often used in combination with other structures, as an acquisition vehicle.

	SICAR	SIF	Part II fund
Applicable legislation	SICAR Act (2004)	SIF Act (2007)	Investment Funds Act, Part II (2002)
Prospectus Directive	Applicable (i.e., a PD Prospectus must be issued where an "offer to the public" within the meaning of the Prospectus Directive is made unless the offer is made under an exemption of the Prospectus Directive). SICARs which make an offer under an exemption of the Prospectus Directive must issue a prospectus compliant with the SICAR Act. This prospectus must be updated each time new securities are issued.	Only applicable if the SIF is closed-ended (i.e., does not offer any redemption opportunities to investors). Open-ended SIFs may make a public offer in Luxembourg on the basis of their issue document compliant with the SIF Act. This issue document must be updated each time new securities are issued to new investors.	Only applicable if the fund is closed-ended (i.e., does not offer any redemption opportunities to investors). Open-ended funds may make a public offer in Luxembourg on the basis of their prospectus compliant with the Investment Funds Act. This prospectus must be updated on an on-going basis.
Supervision by the CSSF	Yes (light supervision)	Yes (light supervision)	Yes

SPF	Securitisation vehicle	SOPARFI [1]
SPF Act (2007)	Securitisation Act (2004)	Companies Act (1915)
Not applicable as the number of investors is limited and shares of a SPF may neither be offered to the public nor listed.	Applicable (i.e., a PD Prospectus must be issued where an "offer to the public" within the meaning of the Prospectus Directive is made unless the offer is made under an exemption of the Prospectus Directive).	Applicable (i.e., a PD Prospectus must be issued where an "offer to the public" within the meaning of the Prospectus Directive is made unless the offer is made under an exemption of the Prospectus Directive).
No	No, unless issue of securities to the public more than 3 times a year (offers to institutional investors and private placements do not constitute "public offers")	No

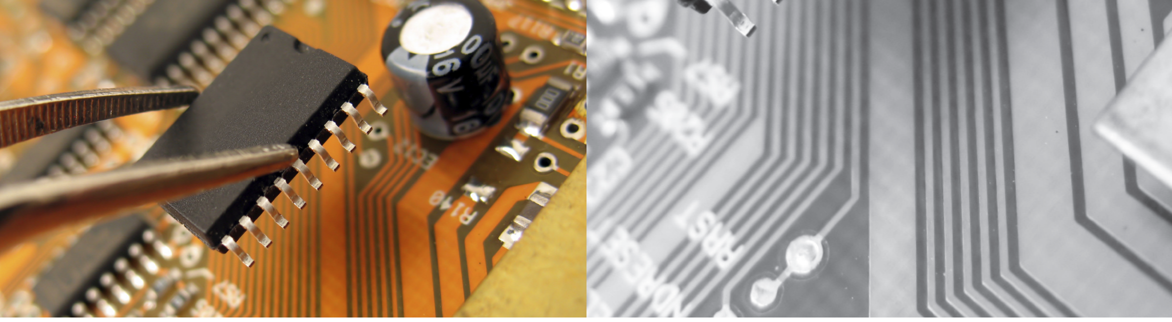
[1] This table only refers to SOPARFIs established under the form of an SA, an SCA or an Sàrl.

	SICAR	SIF	Part II fund
Eligible investors	Institutional investors Professional investors Well-informed investors	Institutional investors Professional investors Well-informed investors	Unrestricted
Eligible assets / strategies	All types of private equity / venture capital investments (including real estate private equity) Temporary investments in other assets pending investments in private equity / venture capital	Unrestricted	Unrestricted (subject to CSSF prior approval)
Risk diversification requirement		Yes (no detailed investment restrictions; spreading of the investments over a few targets should be sufficient)	Yes (in principle, investment in any target company may not exceed 20% of the NAV)
Entity type	Corporate entity (SA, SCA, Sàrl, SCoSA, SCS)	SICAV/F (SA, SCA, Sàrl, SCoSA) FCP Other (e.g., fiduciary structure)	SICAV (SA) SICAF (SA, SCA, Sàrl) FCP
Segregated sub-funds	No. (SICAR Act should be amended shortly to authorise segregated sub-funds; tracking stock schemes have been authorised by the CSSF).	Yes	Yes
Substance in Luxembourg / nationality or residency requirements	Head office in Luxembourg No nationality / residency requirements for directors / managers	Head office of SIF-SICAV/F (or of management company of SIF-FCP) in Luxembourg No nationality / residency requirements for directors / managers	Head office of SICAV/F (or of management company of FCP) in Luxembourg No nationality / residency requirements for directors / managers
Required service providers in Luxembourg	Depositary (credit institution) Administrative agent (PFS or unregulated company) [1] Independent auditors	Depositary (credit institution) Administrative agent (PFS) [1] Independent auditors	Depositary (credit institution) Administrative agent (PFS) [1] Independent auditors

[1] The administrative agent is not required if the administration duties are performed by the securitisation company, the SICAR, the SICAV/F or the management company itself in Luxembourg.

SPF	Securitisation vehicle	SOPARFI
Individual investors Private estate management entities Intermediaries acting on behalf of the above-referred investors	Unrestricted	Unrestricted
Financial assets only (no controlling activity over investments)	Securitisation of risks linked to any types of assets No active management of the assets	Unrestricted
No	No	No
Corporate entity (SA, SCA, Sàrl, SCoSA)	Securitisation company (SA, SCA, Sàrl, SCoSA) Securitisation fund (organised under the contractual form or on a fiduciary (trust) basis)	Any corporate type of entity
No	Yes	No
Head office in Luxembourg No nationality / residency requirements for directors / managers	Head office of securitisation company (or of management company of securitisation fund) in Luxembourg No nationality / residency requirements for directors / managers	Head office in Luxembourg No nationality / residency requirements for directors / managers
Usually none	No depositary required, unless securitisation vehicle is subject to supervision of the CSSF Administrative agent (PFS or unregulated company) [1] Independent auditors	Independent auditors may be required depending on size of company and/or number of employees (if any)

	SICAR	SIF	Part II fund
Approval process by the CSSF	Launching of a SICAR is subject to prior approval by the CSSF of: • Articles, prospectus and agreements with main service providers; • directors / managers (must be experienced and reputable); • choice of depositary and auditor. The CSSF generally does not carry out an in-depth review of documents and mainly checks eligibility of investment strategy. No offer of securities may be made before CSSF approval.	An application for approval of the fund will need to be submitted to the CSSF within one month of the offer of securities. Although it is anticipated that the CSSF will not carry out an in-depth review of all materials, the CSSF will approve: • Articles or management regulations, prospectus and agreements with main service providers; • directors / managers (must be experienced and reputable); • choice of depositary and auditor. In practice, it may be advisable to seek CSSF prior approval if the SIF displays unusual features.	Launching of a fund is subject to prior approval by the CSSF of: • Articles or management regulations, prospectus and agreements with main service providers; • directors / managers (must be experienced and reputable); • investment manager(s) (if any) (must be experienced and reputable); • eligibility of promoter (financial institution with sufficient financial means); • choice of depositary and auditor. No offer of securities may be made before CSSF approval.
Capital (fixed / variable)	Fixed or variable capital	Fixed or variable capital	Fixed or variable capital
Minimum capital / net assets requirements	Upon incorporation: SA/SCA: EUR 31,000 Sàrl: EUR 12,500 Subscribed share capital must reach EUR 1 mio within 12 months of authorisation.	**For FCPs** Net assets must reach EUR 1.25 mio within 12 months from authorisation. **For SICAV/Fs** Upon incorporation: SA/SCA: EUR 31,000 Sàrl: EUR 12,500 Subscribed share capital and share premium must reach EUR 1.25 mio within 12 months of authorisation.	**For FCPs** Net assets must reach EUR 1.25 mio within 6 months from authorisation. **For SICAV/Fs** Upon incorporation: SA/SCA: EUR 31,000 Sàrl: EUR 12,500 Share capital must reach EUR 1.25 mio within 6 months of authorisation.



SPF	Securitisation vehicle	SOPARFI
Not applicable	Not applicable for unregulated securitisation vehicles	Not applicable
Fixed capital	Fixed capital for securitisation companies	Fixed capital
Upon incorporation: SA/SCA: EUR 31,000 Sàrl: EUR 12,500 SCoSA: no requirement	For securitisation companies (upon incorporation): SA/SCA: EUR 31,000 Sàrl: EUR 12,500 No requirement for securitisation funds	Upon incorporation: SA/SCA: EUR 31,000 Sàrl: EUR 12,500 SCoSA: no requirement

	SICAR	SIF	Part II fund
Structuring of capital calls and issue of shares / units	Capital calls may be organised either by way of capital commitments or through the issue of partly paid shares (to be paid up to 5% at least). Existing shareholders have no pre-emptive right of subscription, unless otherwise provided for in the Articles. Issues of shares of SICAR with a variable capital do not require an amendment of the Articles before a public notary. Issue price may be freely determined in accordance with the principles laid down in the Articles.	Capital calls may be organised either by way of capital commitments or through the issue of partly paid shares (to be paid up to 5% at least) or units. Issues of shares of a SICAV do not require an amendment of the Articles before a public notary. Issue price may be freely determined in accordance with the principles laid down in the Articles or management regulations. For SICAVs, existing shareholders have no pre-emptive right of subscription, unless otherwise provided for in the Articles.	**For FCPs** Capital calls may be organised either by way of capital commitments or through the issue of partly paid units. Existing unitholders do not have a pre-emptive right of subscription in case of issue of units, unless otherwise provided for in the management regulations. Units must be issued at a price based on the NAV (plus costs and actualisation interests, if appropriate). **For SICAFs** Capital calls in an SA/SCA may be organised either by way of capital commitments or through the issue of partly paid shares (to be paid up to 25% at least). An Sàrl cannot issue partly paid shares. Existing shareholders of an SA/SCA have a pre-emptive right of subscription in case of increase of capital by way of cash contribution (except if waived by shareholders' meeting). Issues of shares require an amendment of the Articles before a public notary. Issue price is determined in accordance with the principles laid down in the Articles. **For SICAVs** Capital calls must be organised by way of capital commitments (shares must be fully paid-up). Existing shareholders do not have a pre-emptive right of subscription in case of issue of shares, except if otherwise provided for in the Articles. Issues of shares do not require an amendment of the Articles before a public notary. Shares must be issued at a price based on the NAV (plus costs and actualisation interests, if appropriate).

SPF	Securitisation vehicle	SOPARFI
Capital calls may be organised either by way of capital commitments (i.e., contractual undertaking of an investor to subscribe shares of the company upon request) or through the issue of partly paid shares (to be paid up to 25%). Sàrl and SCoSA cannot issue partly paid shares.	**For securitisation funds**	Capital calls may be organised either by way of capital commitments (i.e., contractual undertaking of an investor to subscribe shares of the company upon request) or through the issue of partly paid shares (to be paid up to 25%). Sàrl and SCoSA cannot issue partly paid shares.
	Capital calls may be organised either by way of capital commitments or through the issue of partly paid units.	
Existing shareholders of an SA/SCA/Sàrl have a pre-emptive right of subscription in case of increase of capital by way of cash contribution (except if waived by shareholders meeting).	Existing unitholders do not have a pre-emptive right of subscription in case of issue of units, unless otherwise provided for in the management regulations.	Existing shareholders of an SA/SCA/Sàrl have a pre-emptive right of subscription in case of increase of capital by way of cash contribution (except if waived by shareholders' meeting).
Issues of shares require an amendment of the Articles before a public notary.	Issue price may be freely determined in accordance with the principles laid down in the management regulations.	Issues of shares require an amendment of the Articles before a public notary.
No legal constraints on issue price.	**For securitisation companies**	No legal constraints on issue price.
	Capital calls in an SA/SCA may be organised either by way of capital commitments or through the issue of partly paid shares (to be paid up to 25% at least). Sàrl and SCoSA cannot issue partly paid shares.	
	Existing shareholders of an SA/SCA/Sàrl have a pre-emptive right of subscription in case of increase of capital by way of cash contribution (except if waived by shareholders' meeting).	
	Issue price may be freely determined in accordance with the principles laid down in the Articles.	
	Issues of shares require an amendment of the Articles before a public notary.	

	SICAR	SIF	Part II fund
Distribution of dividends	There are no statutory restrictions on payments of (interim) dividends (except for compliance with minimum capital requirement).	**For SIF-FCPs and SIF-SICAVs** There are no statutory restrictions on payments of (interim) dividends (except for compliance with minimum net assets / capital requirement). **For SICAFs** Distributions may not reduce the SICAF's assets, as reported in the last annual reports, to an amount less than one-and-a-half times the total amount of the SICAF's liabilities to its creditors. Interim dividends are subject to statutory conditions.	**For FCPs and SICAVs** There are no statutory restrictions on payments of (interim) dividends (except for compliance with minimum net assets / capital requirement). **For SICAFs** Distributions may not reduce the SICAF's assets, as reported in the last annual reports, to an amount less than one-and-a-half times the total amount of the SICAF's liabilities to its creditors. Interim dividends are subject to statutory conditions.
Calculation of NAV	The NAV must be determined at least once a year. Assets are to be valued at fair value.	The NAV must be determined in accordance with the rules laid down in the Articles or management regulations. Assets are to be valued at fair value.	The NAV must be determined at least once a year on the basis of the realisation value estimated in good faith.
Financial reports / consolidation	Audited annual report (within 6 months from end of relevant period) Explicit exemption from consolidation requirements	Audited annual report (within 6 months from end of relevant period) Explicit exemption from consolidation requirements	Audited annual report (within 4 months from end of relevant period). An audited long form report is required to be issued along with the annual reports. Semi-annual report (within 2 months from end of relevant period)

SPF	Securitisation vehicle	SOPARFI
Distributions may not reduce the net assets of the SPF to less than the amount of the subscribed capital plus non-distributable reserves. Interim dividends are subject to statutory conditions. SCoSA: profits are distributed proportionally to investors each year, except if provided otherwise in the Articles.	**For securitisation funds** There are no statutory restrictions on payments of (interim) dividends. **For securitisation companies** Distributions may not reduce the net assets of the company to less than the amount of the subscribed capital plus non-distributable reserves. Interim dividends are subject to statutory conditions.	Distributions may not reduce the net assets of the SOPARFI to less than the amount of the subscribed capital plus non-distributable reserves. Interim dividends are subject to statutory conditions. SCoSA: profits are distributed proportionally to investors each year, except if provided otherwise in the Articles.
Not applicable	Not applicable	Not applicable
Not applicable	Audited annual report	Audited annual report may be required if company exceeds a certain size in terms of turnover, total assets and number of employees.

	SICAR	SIF	Part II fund
Tax regime	Fiscally opaque SICARs (i.e. all SICARs except those established under the form of an SCS) are fully taxable. However, they can generally avoid any substantial tax in Luxembourg as they are authorised to exempt from their tax base all income and capital gains deriving from: i) investments in transferable securities [1] and ii) temporary cash investments pending investments in risk capital for a maximum period of twelve months. Fiscally opaque SICARs may in principle claim treaty protection and benefit from the parent-subsidiary directive. However, the eligibility of SICARs must be reviewed on a case-by-case basis depending on the jurisdiction of the target company. SICARs established as an SCS are tax transparent and the profit share of foreign investors investing in these SICARs is not subject to any tax in Luxembourg. A fixed capital duty of EUR 1,250 is payable upon incorporation of the SICAR.	SIFs are subject to an annual subscription tax (taxe d'abonnement) of 0.01% p.a. of their NAV. Unlike SIF-FCPs, SIF-SICAV/Fs should benefit from certain double tax treaties. Investments may be made through fully taxable subsidiaries benefiting from double tax treaties and the EU parent-subsidiary directive. A fixed capital duty of EUR 1,250 is payable upon incorporation of SICAV/Fs.	Part II funds are subject to an annual subscription tax (taxe d'abonnement) of 0.05% p.a. of their NAV. Classes of shares which are reserved for Institutional investors are subject to a subscription tax at a reduced rate of 0.01%. Unlike FCPs, SICAV/Fs benefit from certain double tax treaties. Investments may be made through fully taxable subsidiaries benefiting from double tax treaties and the EU parent-subsidiary directive. A fixed capital duty of EUR 1,250 is payable upon incorporation of SICAV/Fs.

[1] Tax authorities have accepted in certain cases that loans may be assimilated to securities for the purpose of the tax exemption, as long as the loan agreement includes a clause providing for the possibility to transfer the loan to a third party.

SPF

SPFs are subject to an annual subscription tax (taxe d'abonnement) of 0.25% p.a. of their share capital, share premium and debt exceeding eight times the share capital plus share premium, with a maximum of EUR 25,000 per annum.

The SPF is exempt from corporate income tax, municipal business tax and net worth tax.

This tax regime is not applicable if for a given year, at least 5% of total dividends come from non-resident and non-listed companies that are not subject to an income tax similar to Luxembourg corporate income tax. In that case, the SPF will be fully taxable for that given relevant year.

SPFs do not benefit from double tax treaties and the EU parent-subsidiary directive.

Capital contributions to SPFs are subject to a 1% capital duty (droit d'apport) (likely to be abolished in the future).

Securitisation vehicle

Securitisation funds are considered to be investment funds. They are subject neither to corporation taxes nor to the annual subscription tax (taxe d'abonnement).

Securitisation companies are fully taxable. They may however deduct from their taxable profit payments made to investors. Basically, investors in a securitisation company may hold either equity or debt securities. The Securitisation Act expressly states that for tax purposes payments made by the company are always interest, even if under the Companies Act they take the form of dividends. Thus, securitisation companies may deduct any payments to investors.

A fixed capital duty of EUR 1,250 is payable upon incorporation of securitisation companies.

SOPARFI

SOPARFIs are fully taxable companies, subject to an aggregate corporation tax burden which currently amounts to 29.63% for companies located in Luxembourg City.

However, SOPARFIs benefit from exemptions to corporation tax for dividends received from share-holdings, capital gains made on the sale of share-holdings and gains made on liquidation of companies in which shares are held.

Exemption is granted on the following conditions:

- Dividend and liquidation gains exemption on share-holdings of at least 10% or the acquisition cost of at least EUR 1.2 million provided such qualifying share-holding is held for at least 12 months;
- Capital gains exemption of share-holdings of at least 10% or an acquisition cost of at least EUR 6 million provided such qualifying share-holding is held for at least 12 months.

A 15% withholding tax will be applied on the gross amounts of dividends paid by the SOPARFI (subject to tax treaties and EU parent-subsidiary directive). No withholding tax is levied on liquidation payments.

There is no formal legal rule concerning thin capitalisation. The Luxembourg tax authorities usually consider that an acceptable debt/equity ratio is 85:15. If this ratio is not complied with and the SOPARFI is over-indebted, interest paid on the excess debt on a loan received from its shareholder or to a bank, when the loan of the bank is guaranteed by the shareholder, can be considered as a hidden profit distribution subject to dividend withholding tax at a rate of 15% and such interest is then not deductible.

Capital contributions to a SOPARFI are subject to a 1% capital duty (droit d'apport) (likely to be abolished in the future).

The investment company in risk capital (SICAR)

The *Société d'Investissement en Capital à Risque*, SICAR, was created by the law dated June 15, 2004 on the investment company in risk capital (the SICAR Act).

General partner access

In order to carry out its activities, the SICAR must be authorised by the CSSF.

The authorisation regime of the SICAR is relatively light as it is limited to the approval by the CSSF of its constitutive documents, its directors, the choice of the depository, the auditor and the place of central administration.

The directors[1] of the SICAR and the depository must be of sufficiently good repute and have sufficient experience in the performance of their functions in the private equity field and consistent with the investment policy of the SICAR. To that end, their identity must be notified to the CSSF. This does not concern the initiator and the investment manager/ investment advisor of the SICAR as they are not subject to authorisation by the CSSF, although their experience may be cross-checked.

The CSSF will approve the articles of incorporation of the SICAR, its prospectus, ancillary agreements with services providers and any modifications made thereof.

The authorisation is subject to demonstrating that the custodian and the central administration of the SICAR are situated in Luxembourg, as further detailed under section 3.8.

Once authorised, the SICAR is put on an official list by the CSSF. This registration is tantamount to the authorisation by the CSSF but should not be considered to be an endorsement by the CSSF of the quality of the SICAR.

Investors

Due to the high risk associated to the investments made by a SICAR, Luxembourg law restricts the access to the SICAR to investors who fully acknowledge the risk borne (referred to as "well-informed investors","eligible investors" or "qualified investors").

In accordance with the SICAR Act, the following investors may be regarded as well-informed:

- institutional investors, which under current guidance would include notably banks, insurance companies, pension funds, commercial companies, investment funds and certain holding companies[2];
- professional investors defined as "a client who possesses the experience, knowledge and expertise to make its own investment decisions and properly assess the risks that it incurs";
- any other investor who cumulatively a) has confirmed in writing that he adheres to the status of well-informed investor, and b) invests a minimum of EUR 125,000 in the company.

The latter minimum investment condition (b) may be waived if the investor can evidence his expertise, experience and knowledge in adequately appraising an investment in risk capital. This is done through the deliverance of a written certification by a credit institution, another professional of the financial sector[3] or by a management company.

Investments

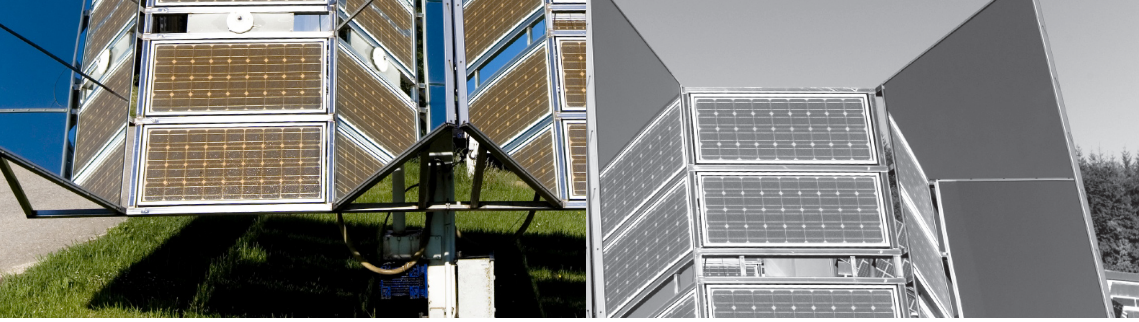
Investment scope: risk capital

The SICAR is a vehicle reserved for investments in risk capital. As per the SICAR Act, the object of a SICAR is to "invest its assets in securities representing risk capital in order to provide its investors with the benefit of the result of the management of its assets in consideration for the risk which

[1] The directors who formally represent the SICAR are: the general partner of the partnerships limited by shares and limited partnerships, the board members of public limited companies and cooperative companies set up as public limited companies and the managers of private limited companies.

[2] Definition provided by Appendix II of the EU Directive 2004/39/EEC (JOCE L 145, 30/04/2004 P.0001 – 0044). Even if parliamentary documents refer to the definition included in CSSF circular 2000/15 referring to the FESCO recommendations, the definition given in the directive will certainly prevail. For a complete definition, please refer to the directive.

[3] Professional of the financial sector as defined within the meaning of the EU Directive 1993/22/EEC of 10 May 1993 on investment services in the securities field.



they incur", where risk capital "is to be understood as the direct or indirect contribution of assets to entities in view of their launch, their development or their listing on a stock exchange".

The SICAR must fulfil the criteria of i) "high risk" and ii) the "intention to develop" the investee companies.

The "high risk" element can be demonstrated through various characteristics of the investment, such as the lack of liquidity due to the fact that the investments are not listed. The expected return should be in line with the amount of risk taken.

The "intention to develop" can take a large variety of forms and materialise in the value creation at the level of the investee companies.

Value can be added for example via the restructuration, modernisation or development of new products and markets as well as any measures aiming at a better allocation of resources. This often entails the intervention of the general partner in the management of the target investment companies, such as through an active representation at board level of the target company. While the active management is mandatory from a regulatory standpoint for a SICAR investing in one single target company, this may not necessarily be required where the SICAR invests in several targets, as long as other criteria sufficiently establish the risk capital criterion.

It is important to note that traditional holding companies that make acquisitions with a view to holding on to the assets cannot be set up as a SICAR.

In practice, traditional investments into venture capital and private equity always fulfil these criteria as it is for this industry that the SICAR Act was created.

The following are examples of underlying assets of SICARs that have been set up:

- Buy-out
- Venture capital
- Mezzanine
- Opportunistic real estate
- Infrastructure
- Renewable energy
- Microfinance
- Others.

No diversification rules

The SICAR Act does not impose any diversification rules. A SICAR can consequently invest in one single company, provided the above criteria are met.

Fund of funds and master-feeder structure

In addition to investing directly in investee companies, a SICAR can be set up as a fund of funds (such as a fund of private equity funds), provided that the underlying funds also fulfil the criteria of "high risk" and "intention to develop".

A SICAR can also be set up as a feeder fund investing exclusively in a local or foreign master fund, provided that the master fund's investment policy is in compliance with the SICAR Act's criterion of risk capital.

Type of investment instruments

All equity and debt instruments are eligible for investment purposes, including shares, bonds, notes, mezzanine loans, convertible loans or straight loans.[1]

Financing

The SICAR can issue equity, debt instruments and loans. The SICAR Act does not impose any leverage restrictions.

[1] The tax consequences for interest derived from loans to target companies are however to be considered (refer to Section 3.4.)

Exit

The SICAR Act does not restrict in any way the exit mechanism, such as through a trade sale or initial public offering.

The ultimate objective is to exit the investment company at a profit. This differentiates the SICAR from holding companies whose objective is to "hold" on to its investments. The type of financing used by the SICAR is left entirely at the discretion of the partners of the SICAR.

The special case of real estate investments

Real estate funds can be set-up as SICARs if they fulfil the criteria of "high risk" and "intention to develop". In practice, this category of real estate funds mainly includes opportunistic real estate funds. In addition to "high risk" criterion (e.g. such as political risk of the countries of investment or high risk concentration of the investments), the clear objective of developing the real estate is essential. This value creation process can take several forms, such as construction, renovation and leasehold improvements, portfolio restructuring, etc.

It is important to note, however, that SICARs cannot hold real estate items directly on their balance sheet but must invest via legal entities which hold the real estate assets.

Non-eligible investments

SICARs are not allowed to invest in hedge funds.

Although a SICAR may use derivatives for hedging purposes, the investment in derivatives cannot be the objective of the investment policy.

Investment in listed securities

Investments in listed securities are generally not eligible. Exceptions include investments with the intention of taking the investee company private, investments in listed securities that do not meet the requirements applicable to regulated markets and the temporary investment of available cash pending investment in risk capital assets.

Further detailed information on the concept of risk capital and the scope of the SICAR Act in terms of eligible investments can be found in the CSSF Circular 06/241 as of April 5, 2006.

Tax regime

The income tax treatment of the SICAR depends upon the legal form under which it has been incorporated. The SICAR will be considered as a transparent entity, for tax purposes, if it is incorporated under the form of a limited partnership (SCS) and as a non-transparent entity (i.e. liable to tax) if it takes the legal form of a partnership limited by shares (SCA), a cooperative company organised as a public limited company (SCoSA), a private limited company (Sàrl) or a public limited company (SA).[1]

Transparent entity

Under the legal form of a limited partnership (SCS), the SICAR should be considered to be a transparent entity for tax purposes whose income is deemed to be taxed at the level of its investors. It is however necessary to analyse the tax treaties signed with source countries. The consequences will be as follows:

At the level of the target company

Withholding tax, if any, on income distributed by the target company to the SICAR should be reduced in accordance with the double tax treaty between the country of residence of each investor in the SICAR and the country of residence of the target company from which the income is derived.

In principle, EU investors investing in a EU target through the SICAR may benefit from the exemption of withholding tax in the target country, in cases where the conditions of the participation exemption provided by the domestic legislation of the target country are met.

[1] For more detailed information on the legal structures available, please refer to §3.5.

At the level of the transparent SICAR

The SICAR is not subject to corporate income tax (impôt sur les revenus des collectivités). Moreover, the SICAR is never considered to be carrying out a commercial activity in Luxembourg. As a result, it is not subject to municipal business tax (impôt commercial communal).

There is no Luxembourg withholding tax on distributions made by the SICAR.

At the level of the investors

Income received by the SICAR will in principle be taxed directly in the hands of each investor in proportion to his participation in the SICAR and in accordance with the tax regime of his country of residence which may treat the SICAR either as a transparent or as an opaque vehicle.

Double taxation of the income generated by the SICAR will generally be avoided at the level of the investor by application of the double tax treaty between his country of residence and the country of residence of the target company from which the income is derived.

Foreign investors are not subject to Luxembourg tax on any capital gain realised upon the sale of an interest in the SICAR.

Non-transparent entity

If the SICAR is established as a corporation, it will be considered a non-transparent entity for tax purposes whose income is in principle subject to tax in Luxembourg at the standard rate (i.e. 29.63% in Luxembourg City). The SICAR Act provides however for some specific exemptions that render the tax regime of the SICAR very attractive. This tax regime is as follows:

At the level of the target company

Corporate SICARs are in principle entitled to benefit from double tax treaties concluded by Luxembourg. Therefore, withholding tax, if any, on income generated by the target company should be reduced in accordance with the double tax treaty between Luxembourg and the country of residence of the target company from which the income is derived. However, the eligibility of SICARs must be reviewed on a case-by-case basis depending on the jurisdiction of the target company.

In principle, based on the Parent-Subsidiary Directive and provided the local conditions are met, no withholding tax should be levied on dividends distributed by EU target companies to the SICAR.

At the level of the non-transparent SICAR

The SICAR is subject to corporate income tax (impôt sur les revenus des collectivités) at the rate of 22.88% and to municipal business tax (impôt commercial communal) at the rate of 6.75% (Luxembourg City). This leads to a total effective tax rate of 29.63%.

The SICAR benefits from an exemption from corporate income tax on income resulting from transferable securities (valeurs mobilières) as well as on income resulting from the sale, contribution or liquidation of these assets. This mainly includes dividends, interest and capital gains. In addition, the exemption is extended to income arising from funds held for a period of twelve months pending their investment in risk capital. For this purpose, it must be proven that the funds have effectively been invested in risk capital.

There is no Luxembourg withholding tax on dividends and liquidation proceeds distributed by the SICAR.

The SICAR cannot apply for tax consolidation with another Luxembourg company.

At the level of the investors

Double taxation on the income generated by the SICAR will be avoided at the level of the investor by application of the double tax treaty between his country of residence and Luxembourg.

In principle, as the SICAR is subject to Luxembourg corporate income tax, EU investors may be in the position to benefit from the participation exemption on dividends distributed by the SICAR.

Foreign investors are not subject to Luxembourg tax on any capital gains realised upon the sale of the shares of the SICAR.

VAT

The Luxembourg law on the SICAR amended the Luxembourg VAT Act. The new VAT provisions stipulate that the management of UCIs, subject to the supervision of the CSSF including SICARs, is exempt.

A key element to the application of this exemption is the term "management". The commentaries to the VAT Act indicate that the objective of the modified VAT provision is to ensure that the exemption applies in a similar way to the management of a SICAR and to the management of other UCIs.

The administrative VAT practice applicable to the management of UCIs should therefore be relevant for determining the VAT treatment of supplies made to SICARs. The day-to-day management of a SICAR should notably be exempt. Special attention should however be given to sub-contracted management services which can only be exempt if certain conditions are met.

Other taxes

The following rules apply to both transparent and non-transparent SICARs:

Contributions made to a SICAR at the time of its incorporation or further to any capital increase are subject to capital duty (droit d'apport) at a fixed maximum amount of EUR 1,250.

The SICAR is exempt of net worth tax (impôt sur la fortune).

The SICAR is not subject to any subscription tax (taxe d'abonnement).

A fixed annual fee of EUR 1,500 is due by the SICAR to the CSSF. Moreover, the application for authorisation to the CSSF is subject to a registration fee of EUR 1,500.

Legal structures

The SICAR Act offers the choice between 5 legal structures. For all matters that are not expressly provided by the SICAR Act, the law dated 10 August 1915 concerning commercial companies, as amended from time to time, is applicable.

In Luxembourg, five corporate forms are available to incorporate a SICAR:

- Partnership limited by shares (*Société en commandite par actions*, SCA);
- Private limited company (*Société à responsabilité limitée*, Sàrl);
- Public limited company (*Société anonyme*, SA);
- Limited partnership (*Société en commandite simple*, SCS);
- Cooperative company organised as a public limited company (*Société cooperative organisée comme une société anonyme, SCoSA*).

Each of these five corporate vehicles constitutes a legal entity, distinct from its investors as from incorporation. They exist under a firm name which is followed by "SICAR". Of the five forms available, most SICARs incorporated so far opted for the SCA, the SA and the Sàrl. SCA and SA may seek admission of their securities to the Luxembourg or a foreign stock exchange.

Partnership limited by shares (SCA)

Partnerships limited by shares are comparable to foreign structures common in private equity transactions such as UK-type limited partnerships. Such partnerships require a minimum of two partners as from incorporation. Partners in an SCA must be categorised into two groups: those with unlimited liability and those with liability limited to the amount of their contribution.

The name of the company shall include the name of one or more unlimited partners.

The management of the company shall be assumed by one or several unlimited partners. A limited partner who became involved in the management would loose the limitation of his liability.

The unlimited partner in charge of the management is entrusted with broad powers and thus controls the company. Unless otherwise provided for in such documentation, no amendment to the constitutional documents of the company may be adopted without his agreement. Where the unlimited partner is appointed as manager in the articles of incorporation, he benefits from a stability of position.

Where the unlimited partner managing the company is a corporate entity, such corporate entity must appoint an individual as its permanent representative. The permanent representative bears the same liability as if he had been appointed in his own name, without prejudice to the joint liability of the legal entity he represents.

Apart from provisions specific to the organisation of powers and duties of limited and unlimited partners, most rules applicable to SAs are applicable to SCAs.

Shares held by limited partners are freely transferable to third parties as long as they qualify as eligible investors according to the SICAR Act.

Private limited company (Sàrl)

Where the number of investors is to remain limited (less than forty), an Sàrl offers some flexibility in both organisation and functionality. The management of the company may be entrusted either to a single manager or to several managers. If there are less than 25 shareholders in an Sàrl, shareholders' meetings may be held by written resolution. Shares in an Sàrl are not freely transferable. An Sàrl may not distribute its shares to the public or have them listed on a stock exchange.

Public limited company (SA)

A Luxembourg public limited company, or SA, may be incorporated with only one shareholder and there are no limitations to the number of shareholders.

Shares in an SA are freely transferable unless otherwise agreed between the shareholders by specific provisions in either the articles of incorporation, or in a shareholder's agreement.

An SA is managed by a board of directors of at least 3 directors (except in the case that there exists only one single shareholder where only one director is required).

Recently, the law of 10 August 1915 concerning commercial companies has been amended in order to offer the option of organising the management of an SA with either the traditional board of directors or with a two-tier structure where powers are balanced between a management board and a supervisory board. The management board has the power to take any action necessary or useful to realise the corporate object of the company, with the exception of the powers explicitly attributed to the supervisory board or the general meeting of shareholders. The management board performs its duties under the control of the supervisory board. Members of the management boards are appointed and may be revoked by the supervisory board (or the shareholders meeting if the articles of incorporation so provide). The management board has to report in writing to the supervisory board at least every 3 months. Members of either board may only serve on one board at a time.

Other corporate forms

Although less frequently used, the limited partnership (SCS) and the cooperative company organised as a public limited company (SCoSA) may present opportunities to address specific needs of promoters.

Capital structure and distributions

Provisions relating to the capital structure and distributions to investors are for the large part drawn from the legislation applicable to investment funds and even go beyond in order to increase efficiency for private equity and venture capital investments. For such investments, it is usual that, in a first period, the investment vehicle collects commitments from investors to invest a certain amount of funds. The funds are not immediately needed but they will be at a later stage during the investment period. The investment vehicle will then address capital calls to the investors and draw down funds in order to match the rhythm of investments to be made.

Capital structure

Minimum capital

The minimum capital for the launch of a SICAR, as required by the SICAR Act, is EUR 1 million (or the equivalent in a foreign currency). A period of 12 months is granted, as from the authorisation of the SICAR by the CSSF, to reach the minimum capital.

At the time of incorporation of the corporate structure, the required share capital for the various structures varies:

• SCS	no minimum
• Sàrl	EUR 12,500
• SA/SCA	EUR 31,000

Contributions can be made in cash or in kind. The valuation of the assets contributed in kind to an SA or an SCA must be supported by an auditor's report.

The minimum capital requirement applies to the subscribed capital. Only 5% must be paid-up immediately. This provision allows a SICAR to be launched with a minimum of funds at incorporation. The outstanding capital will be paid-up, in one or several payments, when funds are drawn down by the SICAR as investments opportunities are identified.

The shares may have a nominal value, with a minimum set at EUR 1, or alternatively be without mention of a nominal value.

Variable capital

SICARs – with the exception of SICARs incorporated as SCSs – have the option of adopting a fixed or a variable share capital. Where a SICAR has a variable capital, it is at all times equal to the net asset value of the SICAR.

This provision provides flexibility as the variations in the capital are thus effected *ipso jure* without having to comply with the requirements that are applicable to unregulated commercial companies with respect to modifications of the share capital.

Issuance of securities

A SICAR may issue different kinds of securities such as shares, bonds, founders shares or other financial instruments (with some restrictions for S.à.r l. due to their private features, i.e. limitation to forty shareholders and no issuance to the public).

New securities are issued in accordance with the conditions and procedures set forth in the articles of incorporation without further constraints imposed by the SICAR Act. Notably, it is not required by law that the new securities be issued at the net asset value per share at the time of issuance.

Distributions

Distributions are for the most part left to the contractual agreement of the shareholders expressed in the articles of incorporation. Hence, there are no legal restrictions on repayment of capital or distribution of dividends to investors, subject to those set forth in the articles of incorporation. In particular, provisions organising distribution of interim dividends in SA and SCA are not applicable to SICAR.

This flexibility is completed by the absence of obligation for the SICAR to maintain a legal reserve.

Valuation, accounting and reporting

Valuation

Legal requirement: fair value

The SICAR law requires the SICAR assets to be "valued at their foreseeable realisation value estimated in good faith" (Article 5 (3)). The concept of "foreseeable realisation value" is to be understood as the "fair value"[1] and a current draft SICAR Act amendment bill replaces the notion of "foreseeable realisation value" by "fair value" so as to avoid any confusion. According to the SICAR Act, the Articles of the SICAR must describe the fund's fair valuation methodology, introducing an expectation that such methodology would be in line with the valuation principles established by professional associations, such as the EVCA.[2]

Practice

Whilst the SICAR Act introduces flexibility on the methodology to adopt for determining the market value of investments it is a clear requirement that investments need to be fair valued.

In practice, general partners opt to comply with all or part of the International Private Equity and Venture Capital Valuation Guidelines issued by the EVCA, the BVCA[3] and the AFIC[4] in March 2005 or with another recognised set of valuation guidelines. It is also acceptable to use a robust internal valuation methodology that responds to the unique nature of the Fund's investments.

Accounting

LuxGAAP

The SICAR reports under Luxembourg Generally Accepted Accounting Principles (LuxGAAP) as per the law on the annual accounts of companies as of December 19, 2002 (the 2002 law on annual accounts). The SICAR Act however introduces a number of differing treatments to LuxGAAP, the main one being (i) the reporting of assets at fair value and (ii) the exemption from consolidation.

Consolidation exemption

The SICAR benefits from an explicit exemption from consolidation requirements. Consequently a SICAR that holds controlling interests is not required to produce consolidated accounts. This constitutes a major advantage in the private equity industry.

Optional application of IFRS

The SICAR can be granted the approval by the CSSF to adopt IFRS[5] as its accounting framework instead of LuxGAAP. It has to be noted that if a SICAR holds controlling interests, IFRS will require the production of consolidated accounts.

Reporting

Format and content of the annual accounts

The SICAR Act does not prescribe a specific format or content for the preparation of the annual accounts, so that the general framework of the 2002 law on annual accounts regulates

[1] As per the definition of the International Accounting Standards' Board (IASB), the fair value is "the value for which an asset could be exchanged, or a liability settled, between knowledgeable willing parties at an arm's length transaction".

[2] European Private Equity and Venture Capital Association

[3] British Venture Capital Association

[4] Association Française des Investisseurs en Capital

[5] Intrenational Financial Reporting Standards

the format and content of the SICAR accounts (except in case of adoption of IFRS in which case IFRS accounting rules are to be followed).

The annual accounts also include an activity report detailing any information of significance to the investors of the SICAR so that they are able to make an informed judgment on the development and the results of the SICAR.

This framework consequently offers general partners a sufficient degree of flexibility with regard to the nature and detail of disclosures to be done in the annual accounts.

Filing deadline

The SICAR must establish its annual accounts within six months of the end of the financial year. The annual accounts must be filed at the Luxembourg companies and trade register (Registre de Commerce et des Sociétés).

The SICAR is not required to produce semi-annual accounts.

Net asset value (NAV)

The NAV of the SICAR must be computed at least once a year. Upon request by the limited partners, the SICAR must inform the investors of the NAV of the SICAR on a semi-annual basis: the current draft SICAR Act amendment bill eliminates this requirement.

Reporting to the CSSF

Regulatory reporting to the CSSF corresponds to the concept of light supervision as it is condensed and should not result in any significant administrative burden. The SICAR needs to report the following information to the CSSF on a semi-annual basis:

- a balance sheet or statement of net assets and liabilities,
- a statement of capital subscribed, drawn down and committed,
- a schedule of investments,
- information about the type of investors in the SICAR,
- information about debt financing used by the SICAR, where applicable.

The custodian, the administrative agent and the auditor

The custodian

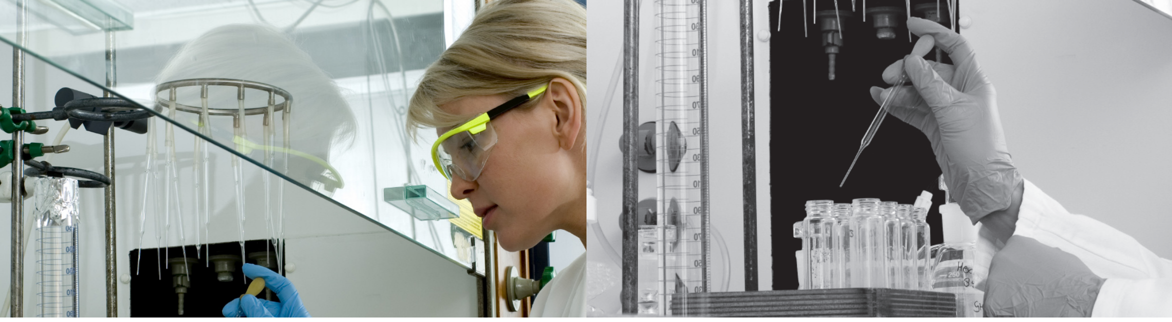
The SICAR must appoint a custodian located in Luxembourg per article 8 of the SICAR Act. The custodian must be a credit institution as per the Law of April 5, 1993 relating to the financial sector and needs to be approved by the CSSF.

The custodian acts exclusively in the interest of the investors of the SICAR and is liable to both the SICAR and its investors for any losses suffered through the non-execution or fautive execution of the custodian functions. While the custodian can sub-delegate some of its functions to third parties, it nevertheless remains fully liable to the SICAR and its investors.

The custodian's key function is the safekeeping of the assets of the SICAR. This function entails certain monitoring functions such as the verification that the capital calls or subscription price for the shares of the SICAR are received within the time limits specified in the SICAR's articles of incorporation or that the income generated at the level of the SICAR is allocated to the investors (general and limited partners) in accordance with the SICAR's articles of incorporation. In practice, the custodian's services may include a range of other value-added services, targeted to the needs of a private equity fund.

The administrative agent

The SICAR must appoint a Luxembourg-based administrative agent fulfilling the role of central administration as per articles 1(3) and 12(5) of the SICAR Act.



No special licence or status as a PSF is required to fulfil the role of administrative agent. The CSSF will approve the choice of the administrative agent based on the latter's level of expertise as well as sufficient technical and human resources to administer private equity funds. Also, GPs are free either to appoint a third party administrative agent or to fulfill themselves all or part of the functions of the central administration.

In practice, the administrative agent's functions include services such as the accounting function of the SICAR, the computation of the NAV or the production of the legal and investor reporting. As for the custodian, professional administrative agents in Luxembourg offer a complete range of customised services such EVCA-compliant and multiple GAAP reporting or capital account services.

As the SICAR is obliged to have its registered office in Luxembourg, full range domiciliary services are of course also available.

The auditor

The SICAR has to appoint an independent auditor (Réviseur d'Entreprises) in Luxembourg. This appointment requires the approval of the CSSF so as to ensure that the independent auditor has sufficient professional expertise in the area of private equity.

The main role of the independent auditor is to audit the annual accounts of the SICAR.

The specialised investment funds (SIFs)

General legal and regulatory framework

The SIF Act introduces a new type of UCI which is clearly differentiated from the ones governed by the Investment Funds Act.

The first purpose of the SIF Act was to replace the Institutional Funds Act due to the numerous cross references in the Institutional Funds Act to the law of 30 March 1988 on UCIs which expired on 13 February 2007.

The SIF Act was also an opportunity to create a self-contained body of law, independent of the Investment Funds Act, to be the perfect tool for the creation in a European context of specialised UCIs subject to regulatory supervision and consequently to strengthen the competitiveness of Luxembourg as a financial centre.

It was important to secure the competitiveness of Luxembourg in the specific area of UCIs dedicated to sophisticated investors. This industry is thriving, witness the development of such UCIs in Luxembourg. At the time the new legislation was passed, there were 207 UCIs under the 1991 law holding EUR 78.4 billion in net assets (source: CSSF monthly report, December 2006). However, the 1991 law regime was considered too restrictive, in particular with respect to real estate and private equity funds. In particular, the concept of "institutional investor" was too limited and excluded a large pool of potential investors, the high net worth individual and/or "well-informed investor". In addition, the requirement to have an official promoter approved by the CSSF for specific types of UCIs was an obvious obstacle to many projects.

Although procuring more flexibility as regards the different elements described below, the SIF Act offers a vehicle subject to regulatory supervision, guaranteeing thereby an appropriate level of investor protection.

The SIF can be a particularly appropriate vehicle for private equity investment when the pure private equity or risk capital component of the fund is not so obvious and thus rules out the creation of a SICAR, in compliance with CSSF Circular 06/241 of April 5, 2006 on the concept of risk capital under the SICAR Act.

Key characteristics and advantages

The main features of the SIF Act may be summarised as follows:

Eligible investors

Only well-informed investors are allowed to invest in SIFs. The definition of a well-informed investor is the same as the one comprised in the SICAR Act i.e. institutional investors, professional investors as defined in Directive 2004/39/EC of the European Parliament and the Council of April 21, 2004 in financial instruments and other investors (i) who adhere in writing to the status of well-informed investor and (ii) who invest at least EUR 125,000 in a particular SIF or who have been subject to an assessment made by a credit institution, an investment firm or a management company certifying their expertise, experience and knowledge in adequately appraising an investment in this SIF.

The SIF Act represents an important broadening of the range of investors permitted to invest in such types of UCI compared to the Institutional Funds Act. Well-informed investors now have an appropriate and specific legal framework suitable to their particular interests and needs.

Organisational flexibility

Legal structure

Large flexibility is granted as to the legal form adopted by a SIF. In contrast to the SICAR Act, the SIF Act permits the creation of UCIs of the contractual type (FCP).

SIFs may also be created in a corporate form (investment companies) with fixed (SICAF) or variable (SICAV) capital. Whereas the Institutional Funds Act only authorised the creation of SICAVs under the form of a public limited company (SA), the law on SIFs also allows such vehicles to be established under the legal forms of a private limited company (Sàrl), a partnership limited by shares (SCA) or a cooperative company organised as a public limited company (SCoSA).[1]

Furthermore, the Law of February 13, 2007 permits the creation of umbrella SIFs. A SIF consequently enables promoters to create a single structure with several sub-funds, each having a different investment policy.

Classes of shares may also be created within subfunds.

Central management & administration

A SIF does not need a promoter with significant financial resources requiring the approval of the CSSF. Indeed, Article 42, paragraph 3 of the SIF Act provides that only the formal "directors" of the SIF are subject to CSSF approval and not the "persons who effectively determine the conduct of the activities of the Undertaking for Collective Investment" as provided in the 2002 Investment Funds Act. It results from this provision that the investment manager of a SIF will also no longer be subject to CSSF approval.

A SIF created as a FCP must be managed by a management company submitted to chapter 13 or 14 of the Investment Funds Act.

The central administration of the SIF must be located in Luxembourg.

Custodian

The custodian's role is restricted to the safekeeping and general supervisory functions. Additional monitoring functions as applicable under the Institutional Funds Act are no longer be applicable. This also differentiates the SIF from the SICAR, for which more responsibilities are entrusted to the custodian.

Capital structure and distributions

The SIF Act provides several advantages with regard to capital requirements. The share capital structure can be very flexible in the sense that while the minimum capital required for a SIF still amounts to EUR 1,250,000, this amount, if the SIF is incorporated as a SICAV or SICAF, will be examined in respect of the subscribed capital and issue premiums instead of the net paid-up assets. This amount must be reached within twelve months of receiving approval from the CSSF. SIFs of the corporate type must have their capital entirely subscribed, but only five percent of each share must be paid-up. In addition, it will be possible for SIFs of the corporate type to issue partly paid shares.

SIFs are allowed to issue not only shares or units, but also other types of instrument, such as notes, for example.

Authorisation

A SIF may start its activities before approval by the CSSF, provided that within a period of one month following the creation of the SIF an application for approval is filed with the CSSF.

Information requirements

The "Issuing Document", i.e. the prospectus, does not require any minimum content and needs to be updated only in the case of new issuance of shares or units to new investors.
The SIF Act does not provide a list of information to be included in the Issuing Document.

[1] Please refer to §3.5. for advantages/disadvantages of the different available types of companies.

In addition, SIFs will not be required to publish semi-annual reports, notwithstanding the obligation to publish an annual report.

Valuation, accounting and reporting

The terms and conditions applicable to the subscription and/or redemption of shares or units of a SIF will be the ones described in its Issuing Document, implying a softening of the regulation and supervision by the CSSF relating thereto. In particular, the price applied to the issue or the redemption of units or shares of a SIF may be different from the net asset value.

As regards the valuation of the assets of a SIF, the SIF Act requires that this valuation be made in accordance with the accounting principle of "fair value". The precise valuation methodology of this "fair value" must be set out in the constitutional documents or by reference to valuation methods recommended by professional associations of the industry or business concerned.

There is, in addition, no requirement as to the frequency of the net asset value calculation which can be limited to one NAV per year, at least for reporting purposes.

Investments

Compared to the Investment Funds Act and even to the SICAR Act, the SIF Act grants increased flexibility in terms of eligible assets. A SIF may invest in transferable securities, money market instruments, real estate, hedge funds, funds of funds, private equity, commodities, financial derivative instruments, debt instruments, microfinance, etc. However, contrary to SICARs for which there are no diversification requirements, SIFs will remain subject to the principle of risk spreading.

Tax regime

General

The tax regime of a SIF is similar to the one which used to be applicable to UCIs subject to the Institutional Funds Act.

At the level of the SIF

SIFs will be subject to a subscription tax at a rate of 0.01% of the fund's net assets; however, the portion invested in other Luxembourg undertakings for collective investment subject to the subscription tax, certain institutional cash funds and pension pooling funds will be exempt from the subscription tax.

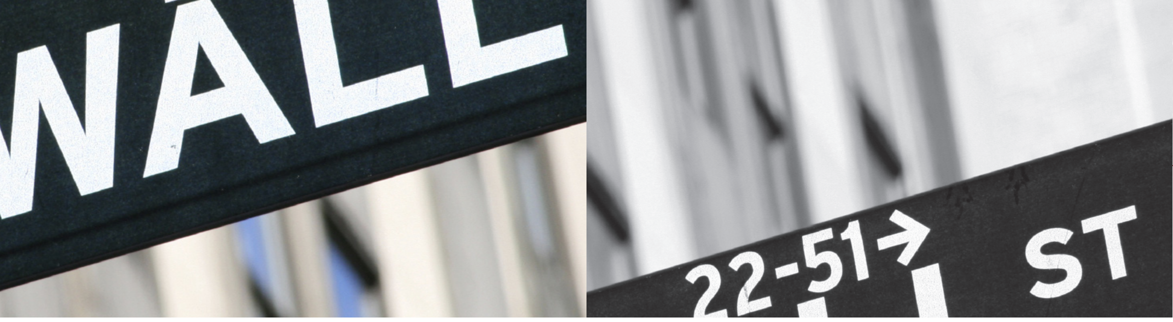
The SIF Act, unlike the Investment Funds Act, does however not require that the participating pension funds be of the same group and permits that individual sub-funds or individual classes reserved to pension schemes also benefit from the exemption.

SIFs of the corporate type

SIFs of the corporate type benefit from an exemption which relates to ordinary corporate taxes on both income and capital. In other words, all their current income - from domestic or external sources - as well as capital gains (whether realised or not) are tax exempt (article 66 of the SIF Act).

SIFs of the contractual type

SIFs of the contractual type are transparent for taxation purposes. Income of such SIFs is attributed proportionally to its investors, and any investor resident in a State having a treaty with Luxembourg may therefore, to the extent practicable, be able to take advantage of treaty benefits, for example by offsetting his tax liability in his own jurisdiction against the withholding taxes incurred by the SIF in territories where the SIF has made its investments.



At the level of the investors

Shareholders are not subject to any capital gains, income or withholding tax in Luxembourg, except for:

- those domiciled, residing or having a permanent establishment in Luxembourg, or
- non-residents of Luxembourg who hold more than 10 per cent of the shares of a fund of the corporate type and who dispose of all or part of their holdings within six months from the date of acquisition, or
- in some limited cases, some former residents of Luxembourg who hold more than 10 per cent of the shares of such corporate-type fund.

In addition, any dividends, other distributions of income made by some SIFs (with the FCP form) or payments of the proceeds of sale and/or redemption of shares in such SIFs, might be subject to the withholding tax and/or information providing regime imposed by Directive 2003/48/EC of 3 June 2003 (the Savings Directive), where payment is made to a shareholder who is an individual resident in a Member State for the purpose of the Savings Directive (or a "residual entity" established in a Member State) by a paying agent resident in another Member State.

Former 1991 funds

Undertakings for collective investment the securities of which are not intended to be placed with the public created according to the Law of 19 July, 1991 have *ipso jure* become subject to the SIF law on 13 February 2007.

The fully regulated funds (UCIs Part II)

General legal and regulatory framework

Apart from the possibility of gaining exposure to listed private equity companies in the context of UCITS compliant funds subject to Part I of the Investment Funds Act, private equity investors wishing to set up a fully regulated investment vehicle under the Investment Funds Act can do so by submitting their fund to Part II of the Investment Funds Act governing UCIs which do not qualify as UCITS. Such regulated UCIs are nevertheless subject to authorisation and ongoing supervision by the CSSF and a promoter must be presented to the CSSF for each project.

A collective investment scheme can qualify as a UCI under Part II if 1) it is of the closed end type 2) it raises capital without promoting the sale of its shares or units to the public within the European Union 3) it reserves in its constitutional documents the sale of its units or shares to the public in non-EU countries or 4) it pursues investment policies for which the investment restrictions of UCITS funds are inappropriate (which would typically be the case for private equity vehicles).

The CSSF has issued several circulars in relation to UCIs that pursue non-UCITS compatible investment strategies, most notably in relation to venture capital funds, futures and options funds, real estate funds and UCIs pursuing alternative investment strategies (hedge funds and funds of hedge funds). [1] The regime of circular 91/75/IML on venture capital funds can be summarised as follows:

- With regard to their professional qualification the directors of the management bodies and the investment advisers must establish that they have sufficient experience in the field of venture capital investments.
- Even though the traditional investment restrictions do not apply to venture capital funds, the UCI must ensure a minimum risk spreading (i.e. not invest more than 20% of its net assets in any one company).
- Securities issued to participants must at the moment of issue have a value of at least EUR 12,500 but there are no further eligibility criteria for investors.
- The prospectus must clearly identify whether the (potentially higher) investment management fees are also due on the portion of the assets not yet or not invested in venture capital. The financial reports of the UCI must contain information on the development of the companies in which investments were made. In the case of sale of securities, the UCI must publish separately the profit or loss amount for each investment. In addition, the financial statements must mention whether there is a potential conflict of interest between the interest of a director of the management bodies and the UCI.
- In addition, the circular clarifies that the prospectus must contain a detailed description of the investment risks inherent to the investment policy of the UCI and the type of conflict of interest which may arise between the interests of a director of the management bodies and the interests of the UCI.
- Finally, the prospectus must include statements indicating relevant risk factors and the fact that the UCI is only suitable for the persons who can afford to take such risk.

Other key characteristics

Available legal forms

UCIs can be created in contractual or in corporate form.

Under both legal forms umbrella funds offering segregated sub-funds can be created.

[1] Circular 91/75/IML of 21 January 1991 on revision and recasting of rules governing Luxembourg undertakings covered by the law of 30 March 1988 on undertakings for collective investment and Circular 02/80/CSSF of 5 December 2002 on specific rules applicable to Luxembourg undertakings for collective investment (UCIs) pursuing alternative investment strategies.

Contractual form

The unincorporated form is that of the "fonds commun de placement" or "FCP", being an unincorporated co-ownership of assets managed by a management company in accordance with management regulations established by such management company and signed by the custodian. Investment management functions can be delegated to professionals authorised by the CSSF (which may be located abroad).

Authorisation for a management company to manage FCPs is delivered separately by the CSSF in compliance with the requirements of chapter 14 of the Investment Funds Act. Alternatively, such Part II FCP can also be managed by a UCITS III compliant management company created under chapter 13 of the Investment Funds Act.

Corporate form

UCIs are usually created as SICAVs or SICAFs. The SICAV (société d'investissement à capital variable - investment company with variable capital) can only be incorporated as a public limited company (SA) while the SICAF (société d'investissement à capital fixe - investment company with fixed capital) can be incorporated as a public limited company (SA), as a partnership limited by shares (SCA) or as a private limited company (Sàrl).

An SA or Sàrl will be managed by its own board of directors/managers in charge as a collegiate body for all material decisions affecting the company. The designation of a management company is not required but investment management functions can be delegated to professionals authorised by the CSSF (which may be located abroad).

The SCA is managed by a manager appointed in the Articles and is similar to a partnership limited by shares issuing two classes of shares: the management shares issued to the manager entailing an unlimited liability towards third parties and the participating shares where the holders' liability is limited to the amount paid in on the shares.

Custodian bank

For all UCIs, the depositary bank must be a Luxembourg based bank. The depositary bank will have been authorised by the competent governmental authorities in the context of its establishment but the CSSF requires confirmation that such bank is properly equipped to fulfil its duties under the Investment Funds Act. The depositary bank has, in the case of an FCP, certain specified functions in order to ensure the protection of the unitholders of the scheme.

Central administration and auditor

The central administration has to be located in Luxembourg and a Luxembourg auditor (Réviseur d'Entreprises) must be appointed to exercise the supervision functions provided by the Investment Funds Act.

Summary table

	SICAV	SICAF	FCP
Supervision by CSSF	Yes	Yes	Yes
CSSF approval process	Articles of incorporation Prospectus Directors Investment manager (if any) Eligibility of promoter Choice of custodian	Articles of incorporation Prospectus Directors/managers Investment manager (if any) Eligibility of promoter Choice of custodian	Management regulations Prospectus Directors of management company Investment manager (if any) Eligibility of promoter Choice of custodian
Legal entity	SA	SA, SCA	/
Management	By board of directors or appointed manager	By board of directors or appointed manager	Management company or appointed manager
Type of fund	Open-ended or closed ended	Closed-ended or open-ended	Open-ended or closed-ended
Minimum capital	EUR 31,000 EUR 1.25 mio (to be attained within 6 months)	Upon incorporation: SA/SCA: EUR 31,000 EUR 1.25 mio (to be attained within 6 months)	EUR 1.25 mio (to be attained within 6 months)
Capital (fixed/variable)	Variable	Fixed	/
Financial reporting	Audited annual report within 4 months of end of relevant period Semi-annual report within 2 months of end of relevant period	Audited annual report within 4 months of end of relevant period Semi-annual report within 2 months of end of relevant period	Audited annual report within 4 months of end of relevant period Semi-annual report within 2 months of end of relevant period
NAV calculation	Normally once a month but derogation possible	Normally once a month but derogation possible	Normally once a month but derogation possible
Required service providers in Luxembourg	Central custodian Administrative agent Auditor	Central custodian Administrative agent Auditor	Central custodian Administrative agent Auditor
Eligible investors	Unrestricted	Unrestricted	Unrestricted
Diversification requirements	Yes	Yes	Yes

Tax regime

There is no Luxembourg tax payable on income received and capital gains realized by a UCI.

Schemes of the corporate type have to pay a capital duty which has been fixed as a lump sum of EUR 1,250.

UCIs investing in private equity are subject in Luxembourg to an annual subscription tax (taxe d'abonnement) amounting to:

- 0.05% p.a. of the net assets, such tax to be levied quarterly on the basis of the net assets at the end of each calendar quarter;
- 0.01% p.a. of the net assets of undertakings or of sub-funds or classes within a sub-fund of collective investment schemes regulated by the Investment Funds Act which are restricted to institutional investors;

If investments are made by a collective investment scheme in other Luxembourg UCIs no subscription tax will be payable.

Shareholders are not subject to any capital gains, income or withholding tax in Luxembourg, except for:

- those domiciled, residing or having a permanent establishment in Luxembourg, or
- non-residents of Luxembourg who hold more than 10 per cent of the shares of a fund of the corporate type and who dispose of all or part of their holdings within six months from the date of acquisition, or
- in some limited cases, some former residents of Luxembourg who hold more than 10 per cent of the shares of such corporate-type fund.

In addition, any dividends, other distributions of income made by some UCIs (with the FCP form) or payments of the proceeds of sale and/or redemption of shares in such UCIs, might be subject to the withholding tax and/or information providing regime imposed by the Savings Directive, where payment is made to a shareholder who is an individual resident in a Member State for the purposes of the Savings Directive (or a "residual entity" established in a Member State) by a paying agent resident in another Member State.

The SOPARFI (société de participations financières)

In Luxembourg, the most common non-regulated private equity vehicle is known as the SOPARFI. This type of vehicle, which may carry on holding and financing activities, benefits from an efficient tax regime: it has access to Luxembourg's treaty network (which comprises over 60 countries) and to the EU Parent-Subsidiary Directive. These are all key factors in selecting a private equity investment vehicle.

Nowadays, it is common practice for private equity funds, irrespective of their country of incorporation, to use Luxembourg SOPARFIs as investment vehicles into target companies.

Legal framework

The Companies Act constitutes the general legal framework applicable to Luxembourg companies. A SOPARFI is a Luxembourg commercial corporate entity, which can be incorporated as a public limited company (SA), a private limited company (Sàrl) or a partnership limited by shares (SCA).

The management of those types of companies may be organised in ways that are specific to private equity investments. In this respect, the choice between an SA, an Sàrl and an SCA may sometimes be crucial. However, this choice can be reversed during the life of the company without any adverse tax consequences if properly managed.

Regulatory framework

SOPARFIs are not specifically regulated by any supervisory authority.

Tax regime

A Luxembourg SOPARFI is subject to the general corporate tax regime. The company is thus subject to corporate income tax and municipal business tax at an aggregate rate of 29.63% for companies located in Luxembourg City. It is also subject to net worth tax (at the rate of 0.5% of the unitary value of the company, computed on the basis of the balance sheet as of 31 December of the preceding year). Lastly, it is subject to a capital duty amounting to 1% of the subscribed capital (upon incorporation of the company and at the occasion of any subsequent share capital increase).

However, this general tax regime includes a participation exemption regime, which results for a SOPARFI, as for any Luxembourg company, in a tax exemption on all income (dividends and capital gains) derived from its holdings (dividends, capital gains and liquidation bonuses) provided that provisions set forth by the law are met (i.e. essentially conditions regarding the target company, the participation itself and the duration of the holding).

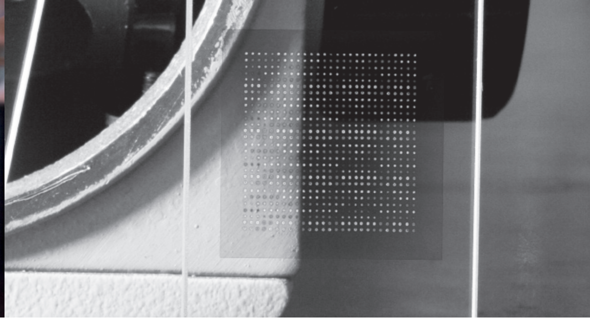
Moreover, holdings benefiting from the participation exemption regime are excluded from the taxable base for the purpose of the computation of the net worth tax. Lastly, under certain conditions, a SOPARFI may be exempted from the registration duty (e.g. in case of a contribution of a participation).

As SOPARFIs benefit from EU directives and double tax treaties signed by Luxembourg, they are generally able to distribute dividends without any significant Luxembourg withholding tax cost. In instances where this is not possible, dedicated financial instruments may reach a similar exemption goal.

Tax substance

One growing issue in international taxation is the requirement by foreign tax administrations of real substance for private equity vehicles (and more generally in international tax structures as well) in order to benefit from a desired tax status (e.g., tax treaty eligibility, application of Parent-Subsidiary Directive, avoidance of CFC rules, etc.). The lack of substance may thus lead a foreign tax administration to conclude that a specific entity is purely artificial and should be disregarded from a tax standpoint.

The requirements for substance for these entities are determined primarily by the tax rules of the country where entities directly own the assets, rather than the

territory where the entity is established or based. These requirements vary from country to country and will therefore need to be considered on a case by case basis.

The entities must be provided with sufficient "business substance" in terms of purpose of the business, and sufficient "material substance", i.e., office premises, equipment, staff, etc.

It is important to point out that these requirements impact not only Luxembourg, but all locations playing a role in the private equity sector, as well as in the international tax structuring area.

In this respect it should be stressed that Luxembourg service providers have been accustomed to providing such a level of substance for a long time. The human resources potential existing in Luxembourg and in the neighbouring countries also makes it easier for Luxembourg than for some other jurisdictions to accommodate the substance requirement of e.g. staffing.

Market outlook

Many large private equity houses now have substantial presence in Luxembourg (offices, personnel, accounting, etc) and SOPARFIs are used in many private equity deals such as primary or secondary Buy-Outs, refinancings or other types of transactions. Luxembourg's efficient acquisition vehicles like SOPARFIs or dedicated fund vehicles like the SICAR and the SIF, combined with the willingness of the government to promote the private equity business, explain the growing importance of Luxembourg year after year in this industry.

The SPF
(société de gestion de patrimoine familial)

The Law of 11 May 2007 creates a new vehicle for the management of individuals' family wealth. The family wealth management company (société de gestion de patrimoine familial, SPF) is designed as an investment company intended solely for individuals managing their private wealth. Just as an individual may directly invest his/her savings or private liquid assets in shares, bonds, bank balances, undertakings for collective investment, etc., that person may wish to create one or more corporate structures to manage all or part of his/her private liquid assets, which is the aim of the SPF. The latter is, therefore, empowered to acquire, hold, manage and sell any financial asset insofar as this is possible within the framework of private wealth management for individuals, irrespective of the level of the person's wealth or sophistication.

The private character of the SPF enables those individuals involved to have the assets of the SPF managed in the way they wish and, if so desired, to waive the risk-spreading requirement imposed on undertakings for collective investment.

General and legal framework

Legal form

The SPF should adopt the form of a corporate entity. It may then choose between the form of a private limited company (Sàrl), a public limited company (SA), a partnership limited by shares (SCA) or a cooperative company organised as a public limited company (SCoSA).

Corporate name

The company articles of incorporation should clearly indicate that the company is a family wealth management company (SPF).

Agreement

SPFs require no agreement, unlike other vehicles, such as specialised investment funds (SIFs), for example or investment companies in risk capital (SICARs).

Shareholders

Given the specific tax regime of the company, restrictions apply with respect to the qualification of the shareholders.

Eligible investors comprise, first and foremost, any individual acting within the framework of the management of his/her private wealth.

Secondly, the SPF is open to wealth management entities acting exclusively in the interest of the private wealth of individuals. This includes entities – whether or not they have the status of legal person – such as trusts, private foundations or similar entities, the object or purpose of which is to manage all or part of the private wealth of individuals, to the exclusion of any commercial undertaking. It should be added that any legal person, resident or not, is included in this notion, provided that it does not exercise any commercial activity. A pure holding company exercising no economic activity under EU law could, then, be a shareholder of an SPF, provided that it is itself owned by investors eligible under the terms of the Law, to the exclusion of any commercial undertaking.

Finally, intermediaries acting on a fiduciary basis or in a similar capacity, on behalf of investors who are themselves eligible may also hold shares in a SPF.

Supervision of the company

Fiscal control over SPFs is attributed to the Administration de l'enregistrement et des domaines.

Capital structure and distributions

Minimum capital upon incorporation

- EUR 31,000 for an SA or SCA,
- EUR 12,500 for an Sàrl.
- No requirement for a SCoSA

Distributions

Distributions may not reduce the net assets of the SPF to less than the amount of the subscribed capital plus non-distributable reserves.

Interim dividends are subject to statutory conditions.

For a SCoSA, profits are distributed proportionally to investors each year, except if provided otherwise in the articles of incorporation.

Fiscal framework

The Law introduces a subjective or personal exemption regime for most direct taxes. This subjective exemption is justified by the fact that the SPF does not have a commercial activity.

At the level of the SPF

The SPF is personally exempt from income tax and municipal business tax on profits and capital gains. It is also exempt from net worth tax.

This exemption will not be applicable for a given year, if during this financial year, the SPF has received at least 5% of total dividends from shareholdings in non-resident and non-listed companies which are not subject to taxation comparable to the Luxembourg corporate income tax. In that case, the SPF will lose the benefit of its favourable tax regime for the financial year in question and will have to pay income tax and municipal business tax (i.e. a maximum combined rate of 29.63% in 2007 in Luxembourg City) as well as a net worth tax of 0,5% on its net assets as determined on 1 January of that year.

The SPF does not benefit from double tax treaties and from the provisions of the EU parent-subsidiary directive.

The SPF is subject to a capital duty of 1% on incorporation and on further contributions (cash or in kind).

The SPF is subject to a 0.25% subscription tax. The Law, however, provides for minimum annual taxation of EUR 100 and maximum annual taxation of EUR 125,000. The taxable base of the subscription tax is composed of the paid-up share capital plus, if applicable (i) the share premium and (ii) the part of the debt, in whatever form, which exceeds eight times the paid-up share capital and the share premium on 1 January or, for the year of its incorporation, existing at the date of incorporation.

Finally, the SPF is not subject to VAT obligations.

At the level of the investors

Capital gains from sales of their shareholding in the SPF or from liquidation proceeds of the SPF received by non-residents are exempt from any taxation in Luxembourg.

Dividend distributions by an SPF are not subject to withholding tax. However, resident individuals to whom dividends are paid are taxed at the progressive rate since the subjective exemption of the SPF excludes the application of the half-dividend system provided for in article 115 (15a) of the Luxembourg income tax law (exemption up to 50% of the dividends paid by fully-taxable companies).

Interests paid by an SPF are not subject to withholding tax except in cases where the EU Savings Directive or Luxembourg domestic withholding tax apply.

Glossary

Articles	Articles of incorporation of a Luxembourg company.
Companies Act	The act dated 10 August 1915 on commercial companies, as amended.
CSSF	Commission de surveillance du secteur financier, the Luxembourg financial supervisory authority.
FCP	Fonds commun de placement, an unincorporated co-ownership of assets managed by a management company.
GP	General partner.
Institutional Funds Act	The act dated 19 July 1991 concerning undertakings for collective investment the securities of which are not intended to be placed with the public.
Institutional investor	Undertakings and organisations that manage an important amount of funds and assets. This concept covers inter alia credit institutions and other financial sector professionals, insurance and re-insurance undertakings, welfare institutions and pension funds, industrial and financial groups and structures put in place by these entities to manage an important amount of funds and assets.
Investment Funds Act	The act dated 20 December 2002 concerning undertakings for collective investment, as amended.
NAV	Net asset value.
Professional investor	Any professional investor within the meaning of Annex II to the Directive 2004/39 on markets in financial instruments.
PD Prospectus	Prospectus compliant with the Prospectus Directive.
Prospectus Directive	Directive 2003/71/EC on the prospectus to be published when securities are offered to the public or admitted to trading and amending Directive 2001/34/EC.
PFS	Luxembourg professional of the financial sector.
SA	Société anonyme (public limited company).
Sàrl	Société à responsabilité limitée (private limited company).
SCA	Société en commandite par actions (partnership limited by shares).

SCoSA	Société coopérative organisée comme une société anonyme (cooperative company organised as a public limited company).
SCS	Société en commandite simple (limited partnership).
Securitisation Act	The act dated 22 March 2004 on securitisation, as amended.
SICAR	Société d'investissement en capital à risque (investment company in risk capital).
SICAR Act	The act dated 15 June 2004 on the investment company in risk capital, as amended.
SICAF	Société d'investissement à capital fixe (investment company with fixed capital).
SICAV	Société d'investissement à capital variable (investment company with variable capital).
SIF	Specialised investment fund.
SIF Act	The act dated 13 February 2007 on specialised investment funds.
SOPARFI	Société de participations financières.
SPF	Société de gestion de patrimoine familial
UCI	Undertaking for collective investment.
UCITS	Undertaking for collective investment in transferable securities.
VAT	Value-added tax.
Well-informed investor	Any investor who has adhered in writing to the status of well-informed investor and complies with one of the following conditions: (i) he/she/it invests at least EUR 125,000 in the special fund; (ii) or his/her/its expertise is confirmed by a Luxembourg professional of the financial sector or management company; or (iii) he/she/it has carried out a certain minimum number of significant transactions on the relevant market over the previous year.

Statistical information

The following information is as of 31 July 2007, except where indicated:

• SICARs:	(17 August 2007)	152
• SIFs:		302
of which SIFs created under the new regime		85
• Part II UCIs:		
• Part II SICAVs:		374
• Part II FCPs:		203
• Part II others:		9
• SOPARFIs:	approximately	25,000

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