

Luxembourg Private Funds Organized as Companies: How to Make Them Fit for Purpose?

By Frank van KUIJK, Andy LI, Veronique SWAY & Daryna IVANIUTA, Loyens & Loeff

The typical legal form for a private fund is a limited partnership. This is unsurprising as private fund management originated in the United States, and this required a vehicle that supports their operating model, ultimately settling on the Delaware limited partnership. Since then, investors and sponsors all over the world have become familiar with limited partnerships.

For any jurisdiction seeking to attract private funds, offering a limited partnership that resembles the Delaware model is therefore essential. As the industry knows, Luxembourg achieved this through its special limited partnership (SCSp), which is now firmly established in the market. Having such a tool available is very valuable, but certain sponsors, especially specific EU sponsors, may still have compelling reasons to use a corporate entity in the form of a Luxembourg partnership limited by shares (SCA) as their fund vehicle instead.

Below, we focus on why the SCA should be on the radar of private fund managers, how it compares to the SCSp, and which fund managers, investment strategies and investors may find it appealing. We also consider, more holistically, how to ensure that an SCA can in practice function as a genuine investment fund: tax-neutral, with workable distribution mechanics, and offering investor confidentiality.

First, why is an SCSp such a great fit for organizing a Luxembourg fund?

An SCSp offers ample contractual freedom regarding governance, commercial arrangements with investors and the allocation and distribution of income. The general partner (GP) retains virtually full control over the partnership's management. An SCSp does not publicly disclose its investors and fund terms, and its financial statements are not publicly accessible.

Subject to rare exceptions, an SCSp is "looked through" for Luxembourg tax purposes and is tax neutral if it acts as a private fund. This "look-through" approach also applies under the tax laws of many foreign countries, including investor jurisdictions (which then regard the investors as the direct owners of the SCSp's assets) and investee jurisdictions (which then regard the investors rather than the SCSp itself as the tax owners of the SCSp's assets). Such look-through status may give rise to tax efficiencies, depending on the investor and investee jurisdictions.

If an SCSp is so great, what may prompt the use of a Luxembourg corporate fund vehicle (SCA) instead?

Fund sponsors that focus on commitments from EU family offices and EU high-net-worth individuals (HNWI) often



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use SCAs as investor-facing vehicles. This is largely driven by familiarity: these types of investors are usually more familiar with corporate vehicles with share-based participation rather than partnership-style interests. EU family offices and HNWI often gravitate, more than other investors, towards secondary strategies, which avoid the J-curve and fund-of-funds strategies, which offer strong diversification despite smaller commitments. It is therefore no coincidence that such strategies are overrepresented among funds relying on the SCA as legal form. Also, open-ended private fund strategies usually opt for a corporate vehicle to accommodate unitization through shares.

The drivers for using SCAs are not limited to familiarity. Certain fund sponsors prefer to organize their Luxembourg fund as a corporate vehicle because such corporate form may come with tax efficiencies and/or tax compliance benefits depending on the investor or investee jurisdictions. An SCA is the go-to Luxembourg vehicle for such cases. These tax benefits are usually a consequence of the fact that the SCA is generally not "looked through" for foreign tax purposes. In fact, the SCA is typically seen as the owner of the assets from both the investor and investee tax perspective.

As an example, an SCA as an access point to a wider fund complex paves the way for more efficient tax treatment for investors that are onboarded through e.g. Dutch or Belgian private wealth pooling vehicles, depending on the specifics of the case. As explained above, EU family offices and HNWI in particular demonstrate appetite for secondary and fund-of-funds strategies, and as such parties often come in private wealth pooling vehicles, managers of such strategies often consider the use of SCAs.

These SCA usually subject themselves to the RAIF regime, why is that?

As explained above, an SCA may secure tax and tax compliance benefits at investee and/or investor level, but it is a full-fledged Luxembourg taxpayer and could therefore cause a substantial Luxembourg tax drag on portfolio performance, which is a showstopper for organizing a fund as an

SCA. In addition, an SCA is subject to corporate law-driven contribution and distribution restrictions including notarial involvement and interim accounts for instance, which would undermine its usefulness as a fund vehicle. However, the Luxembourg reserved alternative investment fund (RAIF) regime, which can be adopted by an SCA, provides a solution for those tax and corporate law-driven concerns.

How adoption of the RAIF wrapper fixes the SCA's key legal and tax drawbacks as a fund vehicle

If an SCA subjects itself to the RAIF regime (commonly referred to as "adopting the RAIF wrapper"), Luxembourg taxes are *de facto* switched off. The RAIF can either (i) opt for a regime to switch off all Luxembourg taxes except for a subscription tax of 1bps on its AUM per year (**Regular Exemption**) or (ii) opt for a regime to be subject to Luxembourg corporate income tax, but with an exemption for income and gains from securities representing risk capital (**Risk Capital Exemption**). If the SCA-RAIF holds only assets qualifying as securities representing risk capital within the meaning of the RAIF law, the latter option effectively entails full tax neutrality.

Selecting the appropriate Luxembourg tax regime for an SCA-RAIF requires careful consideration. While the Regular Exemption is more commonly used, the Risk Capital Exemption may be preferred by certain investors to accommodate their specific tax position. The downside of the Risk Capital Exemption is that the RAIF's assets must be annually screened against the risk capital criteria, which requires auditor involvement. In certain cases, the screening is done on a deal-by-deal basis to avoid surprises at year end, which could potentially invalidate the Risk Capital Exemption. Screening can be particularly challenging for fund-of-funds strategies, as it may entail a look-through analysis down to the portfolio funds' assets.

The choice for the type of tax exemption must be made in the SCA's articles of association (**Articles**) and is in practice challenging (but not impossible) to change once investors have been onboarded. Any amendments to the Articles must be passed before a notary and

come with a shareholder quorum of at least 50% and approval by two-thirds of the votes cast. Changes are sometimes prompted by investor demand, especially where such investors participate through private wealth pooling vehicles which are better off tax-wise if the SCA applies the Risk Capital Exemption rather than the Regular Exemption.

The RAIF regime not only switches off the general tax rules at the SCA level but also allows it to opt for a variable share capital model. Under such model, the above-mentioned corporate law-driven contribution and distribution restrictions, as well as related formalities, no longer apply to an SCA-style fund. An SCA-RAIF then functions as a so-called SICAV, where "V" stands for variable capital. In terms of its capital position, an SCA-SICAV-RAIF only needs to monitor the RAIF law's minimum capital requirement of EUR 1.25 million (subject to a 24-month ramp-up period) and no other corporate share capital variation formalities are applicable.

Hence the RAIF status is a tax and legal necessity for an SCA, and also comes with the option to structure separate compartments, each of which can function as a separate fund within the same legal shell. The tax exemptions referred to above apply at the RAIF level and cannot differ between compartments. Provided the fund documents allow for it, launching such compartments typically requires a mere GP decision (without notarial involvement).

RAIF status is a must-have for a private fund type of SCA, does it also come with downsides?

The RAIF regime does not impose a meaningful incremental compliance burden, although an SCA-RAIF relying on the Regular Exemption is subject to risk-spreading rules. As a matter of regulatory practice, exposure to a single asset is generally capped at 50%, with a 70% threshold for infrastructure assets. These diversification rules are usually not problematic as they are much lighter than what is typically commercially acceptable in a private fund.

However, when the goal is to accommodate a single co-investment, the diversification rules would render the use of a RAIF with the Regular Exemption impossible while a RAIF with Risk Capital Exemption remains a possibility if the underlying asset qualifies as risk capital. A RAIF must have its financial statements audited, but this should not be viewed as an incremental burden, as audits are standard practice for private funds.

To adopt the RAIF regime, an EU authorized alternative investment fund manager (AIFM) must be appointed. In practice, this is usually not a material constraint: sponsors may hire a third-party AIFM or rely on an in-house EU AIFM. If the AIFM is not Luxembourg based care should be taken that the non-Luxembourg, but EU AIFM does not create taxable footprint for the SCA-RAIF outside Luxembourg. The RAIF regime also re-

quires investors to qualify as "well-informed investors" for onboarding purposes. Much can be said about that definition, but, in essence, any investor investing at least EUR 100,000 can qualify.

How to manage public disclosure concerns if a SCA is used as a private fund?

A potential concern that comes with the use of an SCA is the public disclosure of the key fund terms through the SCA's Articles. To solve this concern, the Articles usually contain only generic corporate governance provisions, while the core confidential fund terms are set out in a private offering memorandum. The offering memorandum provides for its own amendment mechanics, which largely resemble those commonly seen in an SCSp, meaning that the GP can unilaterally make changes that do not materially impact investors, while investor consent, by majority or super majority, is only needed for material changes.

Such mechanics eliminate the need for Luxembourg notarial involvement to alter most of the commercial terms, since changes made in an offering memorandum do not require such involvement, whereas amendments to the SCA's articles do. To ensure that the core terms in the offering memorandum are binding on the investors and the GP, the subscription documents of an SCA provide that the investors subject themselves to the fund terms contained in the offering memorandum by submitting their executed subscription documents.

From a confidentiality perspective, it is worth noting that, unlike an SCSp, an SCA must file financial statements with the Luxembourg company register, where they become publicly accessible. In practice, this aspect is, however, not seen as a drawback that creates strong momentum in favor of the SCSp. An SCA-RAIF requires an annual report, including financial statements prepared in a prescribed format, to be prepared and made available to investors upon request. The statutory filing and the annual report may be drawn up under either IFRS or Lux GAAP, with optional fair value principles. To avoid duplication of work, the same accounting principles are usually applied to both the filing and reporting process. Like the limited partnership register of an SCSp, the SCA's shareholders register is not publicly available.

Conclusion

While the SCSp remains the default choice for Luxembourg private funds, an SCA can be a very compelling alternative where a corporate, share-based vehicle better fits the investor base, distribution strategy or tax structuring objectives. When the SCA adopts the RAIF wrapper, the RAIF regime's tax neutrality and variable capital rules, further supported by confidentiality-focused drafting, means that the SCA meets all key requirements and preferences that fund sponsors expect from a private fund vehicle.

La Chine renforce sa présence à la Bourse de Luxembourg

Le 26 juin, le ministère des Finances de la République populaire de Chine a annoncé l'émission d'un nouvel emprunt souverain libellé en euros de cinq milliards d'euros, destiné à être coté sur le marché Euro MTF de la Bourse de Luxembourg (LuxSE).

L'opération a été célébrée lors d'une cérémonie « Ring the Bell » organisée à Luxembourg, en présence de responsables chinois et luxembourgeois ainsi que de représentants du secteur bancaire.

Cette nouvelle émission intervient sept mois après une précédente opération de quatre milliards d'euros, également cotée à la Bourse de Luxembourg. Elle confirme le recours régulier de la Chine à la place fi-



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nancière luxembourgeoise pour ses émissions obligataires internationales et la solidité des relations financières entre les deux pays, engagées depuis 1994 avec la première cotation internationale d'un emprunt souverain chinois à Luxembourg.

Depuis, les liens entre les deux marchés se sont renforcés, avec une présence croissante d'émetteurs chinois sur la place luxembourgeoise. À l'occasion de cette émission, les autorités chinoises ont réaffirmé leur volonté d'approfondir la coopération financière avec le Luxembourg et l'Europe.

La Bourse de Luxembourg confirme ainsi son positionnement comme place de référence pour les émissions souveraines internationales. L'emprunt a été arrangé par un consortium bancaire composé notam-

ment de Bank of China, Bank of Communications et Crédit Agricole CIB.

Les participants ont souligné le rôle du Luxembourg comme passerelle entre les marchés financiers européens et asiatiques, offrant aux émetteurs souverains un accès élargi aux investisseurs internationaux. Cette transaction s'inscrit dans la stratégie de la Chine visant à diversifier ses sources de financement.

Elle traduit la volonté de maintenir un accès durable aux investisseurs européens tout en confortant la position de Luxembourg comme hub international de référence pour les marchés obligataires. Les intervenants ont enfin rappelé l'importance de cette coopération pour le développement des marchés de capitaux, notamment dans la finance durable.