

PRIVATE EQUITY AND VENTURE CAPITAL

FINANCE MALTA:
9th ANNUAL CONFERENCE

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PE/VC - Alternative Investments

- We speak of alternative investments because of the move we have seen in the financial markets from both the demand and supply sides for different asset classes and investment strategies as well as different sources of funding.
- Traditional Investments:
 - asset classes: debt or equity instruments and cash;
 - diversification: limited;
 - risk structure: inefficient dispersion;
 - return: highly dependent on beta, relative returns;
 - fees: typically flat fee structure.

The European Dimension

- On a European level, collective investment undertakings can be structured as UCITS or AIFs. All collective investment undertakings which do not qualify as UCITS schemes are deemed to be alternative investment funds, unless a particular exemption applies.
- UCITS funds are not usually considered to be ideal vehicles for alternative investment strategies, given the restrictions imposed by the UCITS Directive on the instruments that constitute eligible assets as well as the limits on investments.
- Managers wanting to invest in alternative assets and market the fund on a European level should consider setting up an alternative investment fund.

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- As the name implies, alternative investment funds are meant to implement alternative investment strategies mainly targeting professional investors, although, subject to adherence to local regulatory requirements, may also be made available to retail investors.
- The clear advantages:
 - no investment restrictions;
 - possible marketing in all of Europe.

What is an Alternative Investment Fund?

Defined as a collective investment undertaking, including investment compartments, which:

- raises capital from a number of investors, with a view to investing it in accordance with a defined policy, for the benefit of those investors; and
- do not require authorization in terms of the UCITS Directive.

Unless the AIF is internally managed, its status as an AIF depends on the status of the investment manager.

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The AIMFD does not apply to those managers which, directly or indirectly (through a company with which the AIFM is linked by commend management or control, or by a substantive direct or indirect holding) manage portfolio of AIFs whose AUM in total does not exceed:

- a threshold of EUR 100 million; or
- a threshold of EUR 500 million, when the portfolios of AIFs consist of AIFs that are unleveraged and have no redemption rights exercisable during a period of 5 years following the date of initial investment.

EuVECA

- The EuVECA offers Small Managers of Qualifying Venture Capital Funds an alternative route to a European marketing passport without the need to apply the provisions of AIFMD.
- Only available to AIFMs managing AIFs having a combined AUM of less than EUR 500 million, which are unleveraged and have a lock in period of 5 years.
- Smaller Managers may register such funds under the EuVECA Regulation, comply with the requirement imposed by such Regulation and benefit from a European passport without having to comply with the AIFMD requirements.

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- Not of mandatory application. Small Managers must apply to their home state regulator in order to benefit from registration in its terms, such registration valid through the EU.
- The manager may market the EU VECA across the EU under the EuVECA branding, subject to the appropriate notification being submitted to the home state regulator.

Requirements for qualification for EuVECA

- The Small Manager must be subject to registration in its home Member State;
- The fund must be established in the EU;
- The funds managed by the Small Manager must not exceed the threshold AUM of 500 million, be unleveraged and have a lock-in period of 5 years;
- The funds managed by the Small Manager must qualify as “qualifying venture capital funds”.

Qualifying Venture Capital Funds

Defined as a collective investment undertaking that:

- Intends to invest at least 70% of its aggregate capital contributions and uncalled committed capital in qualifying investments;
- Up to 30% of its aggregate capital contributions and uncalled committed capital in assets other than qualifying investments.

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Qualifying investments are defined as:

- equity or quasi-equity instruments that are issued by:
 - a qualifying portfolio undertaking and acquired directly by the qualifying venture capital fund from the qualifying portfolio undertaking,
 - a qualifying portfolio undertaking in exchange for an equity security issued by the qualifying portfolio undertaking, or
 - an undertaking of which the qualifying portfolio undertaking is a majority-owned subsidiary and which is acquired by the qualifying venture capital fund in exchange for an equity instrument issued by the qualifying portfolio undertaking;

Private Equity

- Nature
- No investment restrictions in the AIFMD
- Some investment requirements incumbent on the AIFM
- No restrictions and no investment requirements if the fund is a PIF
- Typical strategy which lends itself to self-managed structures
- Limited partnership vs SICAV