THE RAIF LEAVES NO ALTERNATIVE

LUXEMBOURG LAUNCHED THE RESERVED ALTERNATIVE INVESTMENT FUND (RAIF) IN JULY, A GAME-CHANGING INNOVATION IN THE TOOLBOX THAT HAS ALREADY BECOME A FIRM FAVOURITE WITH INTERNATIONAL INVESTORS. THIS IMMEDIATE SUCCESS HAS SHOWN THAT THE RAIF LEAVES ASSET MANAGEMENT GROUPS NO ALTERNATIVE BUT TO CONSIDER LUXEMBOURG WHEN FULLY DEVELOPING THEIR FUND SERVICE PLATFORMS.

FIVE MONTHS ON, WE TAKE A LOOK AT WHAT MAKES THE RAIF SO DIFFERENT FROM OTHER FUNDS.

THE ORIGINS OF RAIF

Traditionally, Luxembourg's fund management industry was modelled on product regulation, meaning that all of the country's investment funds were subject to the authorisation and on-going supervision of Luxembourg's financial regulator, the CSSF.

However, with the introduction of the Alternative Investment Fund Managers Directive (AIFMD), this is no longer the case with regulation now focusing on fund managers rather than their products. This has led to the development of the RAIF, which is regulated by the asset manager and can be passported across the EU.

"The RAIF was created following discussions among practitioners," says Jacques Elvinger, Partner and Head of Investment Funds at Elvinger, Hoss & Prussen. *"In the aftermath of the financial crisis, we realised that the AIFMD would bring important change in Europe and the regulation of the managers on top of the fund product would lead to double-layer regulation, which is not always required."*

"Although the RAIF is not supervised by the CSSF, it is very much regulated via the AIFMD and RAIF laws," he adds. *"Also the fund manager, depository, administrator, domiciliary agents are all subject to supervision. They need to make sure that the fund is fully in line with the law."*

Because the RAIF was created in Luxembourg and is subject to local regulations, the central administration and registered offices of the funds must be based in the country, explains Freddy Brausch, Partner in the Investment group at Linklaters.

"One must be mindful of the overall Luxembourg legal environment to properly deal with the RAIF, especially when the structure is set up from abroad," he adds.

THE NEED FOR SPEED

One of the major attractions of the RAIF is the speed in which new funds can be launched, says Alain Kinsch, Country Managing Partner at EY Luxembourg.

"The RAIF is a game-changer because certain structuring features such as segregated compartments are available."

ALAIN KINSCH

> "Don't fall into the trap of putting a Ferrari in the hands of a newly licensed driver that might crash in the first curve."
>
> FREDDY BRAUSCH

"As soon as the manager has a license, the RAIF can be launched without having to go through the CSSF process every time," he adds. *"Especially private equity, real estate and hedge fund managers often have small structures and the fact that they don't have to invest extra time and resources on regulatory processes at the level of the fund is of course a significant advantage. The RAIF helps them to gain time and save costs. As soon as they are approved and have obtained their license, they can proceed very quickly with each product launch."*

Also Mr Elvinger says that the RAIF provides asset managers with the visibility they need to market the funds effectively and inform investors when they will go live.

"Especially in areas like private equity, asset managers prepare documents that need to be approved by the investors," he adds. *"Very often these investors will suggest changes to the documents. In the case of a Specialised Investment Fund (SIF), the fund manager would need to go back to the CSSF, return to the investors, and again to the CSSF with further amendments, which can take a lot of time. The RAIF is much more time efficient. Once the structure exists and you make sub-funds, you don't need to go back each time to the CSSF."*

CANNIBALISATION?

RAIF benefits from the same structural flexibility and tax regime as the SIF and Investment company in Risk Capital (SICAR), yet it is not supervised by the CSSF.

"The RAIF is a game-changer because certain structuring features such as segregated compartments are available," says Mr Kinsch. *"It allows us to reach out to clients that would otherwise not have come to Luxembourg."*

"The RAIF is the perfect vehicle for doing segregated managed accounts, which are currently very much in demand. For instance, pension funds often want their own product, instead of investing in a fund with other investors. They want the asset manager to create a separate product according to their specific criteria. In case of a traditional fund, it would not make sense to do this for one investor only."

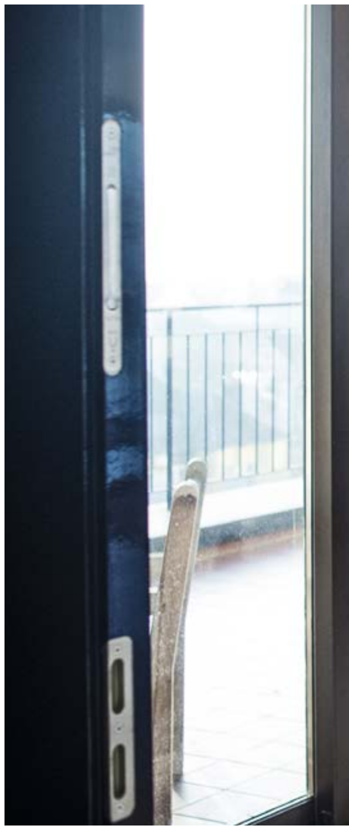
But does this spell the end of the SIF regime? Mr Brausch does not think so and believes that institutions such as sovereign wealth funds and insurers may still want the additional security the older fund models bring.

"If you are a sovereign wealth fund, you do not have a 'legal' obligation but rather a 'moral' obligation to invest in a regulated product. This allows the manager to show that all necessary precautions were taken and to minimise their own responsibility," he explains.

FULL PLATFORM

Luxembourg has always been able to strike the right balance between offering a solid structuring framework and keeping innovation at a steady pace.

"Recently, we have noticed that asset management groups are developing a full platform in Luxembourg," says Mr Elvinger. *"A lot of investors were used to invest in offshore structures such as Cayman but in the last years there is a clear preference to invest in a European vehicle."*



FREDDY BRAUSCH,
PARTNER IN THE INVESTMENT GROUP,
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JACQUES ELVINGER,
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Mr Brausch adds: *"Luxembourg offers a number of structuring features that are not necessarily available elsewhere and that can be used for the RAIF, such as share classes, umbrella structures, compartments, etc."*

Mr Kinsch agrees. *"Compared to other jurisdictions, Luxembourg has taken a more holistic approach. The RAIF is a piece that makes the puzzle complete. Given the high demand for the RAIF, we are currently looking into the compilation of statistics."*

BEWARE INEXPERIENCED DRIVERS

The RAIF can be useful for wealth managers and family offices because it allows them to make flexible transactions.

However, Mr Brausch warns that the client needs to be well advised. He says the RAIF should never be used without doing the necessary checks and stresses that it is always the client who will ultimately bear the risk.

"Yes, the RAIF has possible uses in complex structuring, but not in all cases. For the client's best interest, the provider has to do his job properly. Don't fall into the trap of putting a Ferrari in the hands of a newly licensed driver who might crash in the first curve," he concludes.

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FOR MORE INFORMATION CHECK OUT THE LUXEMBOURG FOR FINANCE WEBSITE:

- FACTSHEET: HOW TO SET UP A RAIF
- BROCHURE: WEALTH MANAGEMENT