PRIVATE EQUITY
INSIGHT/OUT

MICHAEL JACKSON THE MIGHTY CRYPTO

Case Study: Governance tips by HLD Europe

Private Equity: to reinvent or disappear

LëtzLIVE in Luxembourg

Issue 1, 2018

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DEAR READER

The new "Private Equity Insight/Out" replaces the former "Capital V" magazine, which has been published by the LPEA since 2013. As Private Equity and Venture Capital enjoy significant growth in Luxembourg, we take this opportunity to rebrand our publication as a fresh way to communicate with private equity professionals in Luxembourg and abroad. We trust you will appreciate the new approach.

Our cover article in this edition focuses on the "mighty" crypto assets which are already rippling through the venture capital sector. Despite the popularity and volatility of crypto currencies, crypto assets – and notably initial coin offerings (ICOs) – are deemed to stay and have a greater impact on the financing process. In publishing a report on ICOs and tokenisation, Mangrove's Michael Jackson questions the entire VC industry.

In this edition we also take the opportunity to interview the Luxembourg team of HLD Europe, a French group building an international investment platform from Luxembourg – its operating model allows for a governance takeaway.

Enjoy reading!

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THE MAGAZINE OF THE LUXEMBOURG PRIVATE EQUITY & VENTURE CAPITAL ASSOCIATION
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BREXIT UPDATE

Brexit is proving to be a major external force, challenging the status quo of the private equity houses which have exposure to the UK and Europe business environment, but recent regulatory and market developments (eg BEPS, ATAD, CRS, MiFID II) have also put great pressure on the private equity agenda, forcing players to react rapidly by implementing severe changes varying from reviewing the existing corporate structure, operating model and internal controls.

Of all the challenges posed by Brexit, investors are probably the ones offering the hardest push to the private equity firms – under periods of uncertainty being cautious is the sole mantra.

Some investors are demanding private equity houses to cap their exposure to UK assets at a reasonable level. Business continuity is another point of concern, and a good number of private equity houses have already responded by either increasing their substance through an existing European entity or establishing a new entity in the EU.

Due to its consistent reputation as the second-largest fund centre in the world, associated to its economic and political stability, Luxembourg has been attracting the interest of several number of private equity houses, asset managers and insurance companies. To date 23 institutions have decided that their EU entity should be located in Luxembourg, meaning that a full investment management ecosystem is emerging in the Grand Duchy. ●

By **Jefferson L. M. Oliveira**
Financial Services Director
& Brexit Counsel, PwC

SUPPORTING THE FUTURE CHAMPIONS OF CLIMATE FINANCE

Spurred by the tremendous impact potential of climate finance fund projects, as well as the high-level backing through recent international commitments, the interest from public and private investors in climate finance has been growing relentlessly over the last few years. In order to limit the global temperature rise to well below 2°C, there is a strong need for professional intermediation to bring investable projects to the investor community.

In this context, 11 public and private partners have come together to launch the International Climate Finance Accelerator Luxembourg (ICFA Luxembourg), a one-stop shop for fund managers dedicated to providing early-stage support for projects with a high-climate-related impact potential. By leveraging first-mover advantage, the platform will attract and support a number of promising players at an early stage to bring their visions to life and build significant scale.

ICFA Luxembourg's first call for applications opened in January and is followed by a four-month selection process. Once on track, the accelerated fund projects will receive comprehensive support via access to tailor-made support services, financing operating capital, personalised coaching by climate finance experts, training and workshops, as well as support in fundraising before and after the launch of the fund.

As such, ICFA Luxembourg aims to enhance the international climate finance ecosystem through its attractive partner network and by creating an enabling environment for future champions of climate finance. To apply visit **www.icfa.lu.**

LUXEMBOURG'S #INDUTECH AT WORK

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In 2016, engineering and steel-making company Paul Wurth launched an incubator and co-working space in the heart of Luxembourg City, next to its headquarters. Called Paul Wurth InCub, this space caters specifically for start-ups working in the industrial technology sector ("#InduTech"), which includes cleantech, energytech, smart safety, smart construction, artificial intelligence, smart engineering applications, advanced manufacturing and logistics, sustainable mobility and Industry 4.0.

The idea was to create an #InduTech community where entrepreneurs in these fields could go to work and exchange ideas alongside experts, potential clients, investors, partners and suppliers from Paul Wurth's network to explore new opportunities together and grow their businesses.

"What I like in Paul Wurth InCub is that we can have quick connections to major corporate leaders. It is essential for us as a start-up to have support and feedback with our product development", explains DataThings, one of the #InduTech Start-ups Made in Luxembourg.

Connecting entrepreneurs with suppliers, partners and large corporates is key to the development of new products in an agile manner in an ever-evolving market. This experience is beneficial both for the entrepreneurs and for innovative companies; it provides additional networks internally and with external suppliers and partners.

InCub's motto, "Together we create industrial value", perfectly reflects that philosophy.

"WAT ASS PRIVATE EQUITY?"

LPEA conducted the "Wat ass Private Equity" (What is Private Equity) campaign in the last quarter of 2017 to raise awareness of private equity and venture capital among the population of Luxembourg. Through a series of articles published in the national newspaper Wort and a video shared on YouTube and social media, experts from the Luxembourg private equity sector have tried to clarify the concepts behind investing in non-listed assets and explain its importance and impact on the national economy.

This initiative, conducted by LPEA with the support of its recently established Young Leaders in Private Equity group, was a wonderful opportunity to showcase some of the local players that invest in Luxembourg-based firms, such as François Tesch (Luxempart), Eckart Vogler (Investindustrial), Hans-Jürgen Schmitz (Mangrove Capital Partners) and Jérôme Wittamer (Expon Capital), while at the same time demystifying this fast-growing segment of the Luxembourg financial sector.

For more information about this initiative visit **www.lpea.lu/wat-ass-private-equity** or scan the QR code.

SGG GROUP AND FIRST NAMES GROUP JOIN FORCES

Luxembourg-headquartered SGG Group acquired First Names Group from AnaCap Financial Partners (AnaCap) to create a world leader in investor services, providing trust, corporate and fund services through the combined entities. First Names Group is a rapidly growing provider of private client, corporate and fund services headquartered in Jersey and is present in 14 jurisdictions.

The acquisition from AnaCap – Europe's largest specialist private equity investor in the financial services sector – strengthens SGG Group's reach and capabilities in key markets such as Jersey, Guernsey, the Isle of Man, Switzerland and Cyprus. The transaction (which is subject to regulatory approval) means that SGG Group will become, by revenue, the world's fourth-largest provider of trust, corporate and fund services. The combined group will employ over 1,500 people with a presence in 23 jurisdictions.

NEW HOUSE OF START-UPS

The House of Start-ups is set to open its doors in April 2018. It will reunite three different start-up initiatives: the Nyuko accelerator, the Luxembourg House of Fintech (LHoFT) and the Luxembourg City Incubator – all under the patronage of the Luxembourg City and of the Chamber of Commerce. The incubators will share four floors of a total of 5,000 square metres in the "Dôme" building in Luxembourg-Bonnevoie, thus considerably increasing the capacity to host start-ups. The goal is to create a real start-up ecosystem in the heart of Luxembourg City. All stages and types of start-ups will be welcome to join the House of Start-ups – from merely people wanting to pursue a business idea to mature and late-stage ventures in a variety of fields.

SANNE GROUP ACQUIRES LUXEMBOURG INVESTMENT SOLUTIONS

Pierre Weimerskirch

Thomas Goergen

Daniel Kranz

Sanne Group plc, a leading provider of alternative asset and corporate administration services, acquired Luxembourg Investment Solutions S.A. (LIS), the country's leading third-party AIFM with activities well beyond Luxembourg's borders. Since its foundation in 2011 by Pierre Weimerskirch, Thomas Goergen and Daniel Kranz, LIS has been playing an ever-increasing role in the Luxembourg AIFM market. As the first third-party AIFM authorised in Luxembourg and a pioneer in that market, it has grown from a team of four to a group that employs almost 80 people.

Despite the acquisition, LIS will continue to operate as a standalone divisional business within Sanne's EMEA Alternative Segment.


Private Equity.
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build for tomorrow?
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MARLIN EQUITY PARTNERS ACQUIRES MAJORITY STAKE IN TALKWALKER

Talkwalker, a leading global listening and analytics company created in Luxembourg in 2010, announced in January that a majority stake in the company has been acquired by Los Angeles-based Marlin Equity Partners. The acquisition allows the software company to leverage Marlin's operational resources and expertise in growing technology businesses. Talkwalker's founders and management team will continue to lead the company during this exciting new stage of growth, with a focus on accelerating product innovation and international expansion – and with an expected increase of the current 180 to 500 team members in the mid-term. Used by over 1,000 clients, Talkwalker's state-of-the-art multi-tenant cloud platform uses AI-powered technology to analyse images and text in 187 languages across social, online and traditional media.

AIVA RAISES €650K TO CREATE MUSIC BY WAY OF ARTIFICIAL INTELLIGENCE

AIVA, short for Artificial Intelligence Virtual Artist, uses artificial intelligence to compose emotional soundtracks for films, games, trailers, and other entertainment content. The concept and technology have attracted several business angels as well as Kima Ventures, the investment fund of French billionaire Xavier Niel, securing a total of €650,000 for AIVA. In order to train the AI's understanding and interpretation of music, the team behind AIVA starts by feeding the algorithm with more than 15,000 scores of symphonic music. Using deep neural networks, AIVA looks for patterns and rules in the scores to understand the basic style of the music and predicts what should come next on the track. Once it gets good at these predictions, it creates a set of mathematical rules, allowing AIVA to compose totally unique scores.

MERGER OF DOCTENA WITH BOOKMYDOC

The N.1 platform of online medical appointments in Europe, Doctena has taken over its competitor Bookmydoctor. Both platforms were founded in Luxembourg and, through their consolidation, 20% of all medical doctors in Luxembourg now display their agenda on Doctena.lu. This is only the latest expansion in a series of acquisitions by Doctena. With the support of business angels, Doctena previously took over its German competitors Doxter and Terminland, the Austrian Mednanny as well as the Belgian Docbook and Sanmax. The group also operates in the Netherlands and Switzerland. In 2018 Doctena expects to grow the number of its subscribed doctors from 10,000 to 100,000.

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LUXEMBOURG FUTURE FUND AND EXPON CAPITAL INVEST IN SPACE COMPANY SPIRE

Spire Global has announced that it is continuing its global expansion with a closing of its Series C and the opening of new European headquarters in Luxembourg. The Luxembourg Future Fund (LFF) and Expon Capital have committed to becoming shareholders in Spire, participating in its €57.2 million funding round. According to the company's CFO Bryan LeBlanc, "Spire has a once-in-a-lifetime combination of next generation space technology and software analytics that can address a massive market opportunity in logistics, weather, and the IoT".

Luxembourg has a long history of space innovation, open borders, and a highly talented workforce. It also has an unparalleled commitment to growth in the New Space industry and a vibrant ecosystem of new and old space companies, including SES and some start-ups with visionary ambitions for exploration and use of space resources. "We've been deeply impressed with the support, commitment, and expertise of Luxembourg when it comes to New Space. Their robust yet supportive regulatory environment for New Space companies, coupled with incredible open access to international talent and targeted investment vehicles, made Luxembourg an obvious choice for our expansion", noted Peter Platzer, CEO of Spire. ●

MICHAEL JACKSON ON THE FUTURE OF FUNDRASING, TOKENISATION AND THE RISE OF NEW ASSET CLASSES

INTERVIEW by Natacha Oskian
Co-head of the FinTech team of Allen & Overy

MICHAEL JACKSON IS A PARTNER AT MANGROVE CAPITAL PARTNERS AND WAS PREVIOUSLY COO AT SKYPE, WHERE HE WAS RESPONSIBLE FOR RAPIDLY GROWING AN IDEA INTO A WELL-MANAGED, HIGH MARGIN, MULTI-MILLION DOLLAR BUSINESS. BEFORE JOINING SKYPE, MICHAEL LAUNCHED NINE MOBILE OPERATIONS AND TWO ISPS ACROSS EUROPE WITH TELE2. MICHAEL IS ALSO ON THE BOARD OF BLOCKCHAIN AND IS A CONTRIBUTOR TO THE BLOCKCHAIN POLICY INITIATIVE. HE GRADUATED WITH HONOURS FROM UNIVERSITY COLLEGE LONDON WITH A DEGREE IN COMMUNICATIONS ENGINEERING AND IS A GUEST LECTURER IN THEIR MBA PROGRAMME: THE BUSINESS OF TELECOMS.

Some people say that cryptocurrencies and Initial Coin Offerings (ICOs) have formed a bubble which is about to burst. What can we expect in 2018?
Regarding cryptocurrency, the market has been driven heavily by expectation and desire. It's an irrational market just now, but does that mean it's going to burst? I don't know. Cryptocurrency as such won't stop. The question is whether the price of some of the currencies is irrational, and it certainly is. I think we'll see some corrections in the market but, because it's irrational and driven by sentiment, it's very difficult to give any real prediction.
Next up are ICOs. Will we see many of these? Yes we will, and we'll see a significant number because it represents

Mangrove Capital Partner's team : Mark Tluszcz, Hans-Jürgen Schmitz, David Waroquier and Michael Jackson.

a very efficient way for businesses to collect funds – it's more time efficient than using venture capital if you have the right projects with the right people.

Crowdsourcing and ICOs emerged as alternative ways to raise money. How will these new forms of fundraising impact the Venture Capital (VC) industry?

I think it will impact the industry a lot. Indeed, it's already impacting it. ICOs give people a much more open market; they're able to reach a wider range of people, address their products more openly and solicit funding. At the moment the VC world is very opaque. In reality, there are very few venture capital funds, and finding them and getting a deal through with them is not straightforward. This is often a four-to-six month process involving many investment rounds, even in the early stages. In the ICO world however this can happen much more quickly and founders have more control. At the same time, ICOs attract investors that are somewhat immature when it comes to understanding the terms for investment and this is why we are going to see so many scams.

Do you think that ICOs are about to replace equity crowdfunding?

No, I think there is a big future for crowdfunding platforms and I think we have an antiquated fundraising world today where only one per cent of rich people can invest in growth projects and put their money into projects they love. And I look upon it in a broader context: some people say that the VC industry is being disrupted but VC constitutes a very small part of the fundraising environment for small businesses. The banking environment is much larger and of course, a lot of businesses get their funding through an overdraft facility. To be honest, I think the banks are going to be much more side-lined by crowdfunding and ICOs than VC.

> ICOS GIVE PEOPLE A MUCH MORE OPEN MARKET; THEY'RE ABLE TO REACH A WIDER RANGE OF PEOPLE, ADDRESS THEIR PRODUCTS MORE OPENLY AND SOLICIT FUNDING.
>
> Michael Jackson

An effective crowdfunding environment allows a company to raise money from customers, employees, supporters, family, etc. Today it is very difficult for a company to fundraise, and I would like to see the European ecosystem developing and facilitating crowdfunding platforms like Kickstarter and Crowdcube to make sure small businesses can raise money in a much more diverse world.

An ICO is a very geeky thing to do just now and building a token-based company is also very complex. I get ICO requests all the time and one of the checks I always make is to ask: "Can you do this project without a token; what does the token give you? What does it give to your customers? Is it really necessary or are you just jumping on the bandwagon?" And in many cases you don't need a token or blockchain. ICO costs are high and if you fail, it's going to be really difficult to get VC fundraising at a later stage.

Do you see a way of regulating ICOs, particularly offers to retail investors, without lowering any of the existing investor protection standards?

In general, as you know, there's a good framework around "high net worth" or "well informed" investors that already exists in AIFMD and MiFID. I can imagine that regulators may continue to apply these principles for ICOs. There will be, however, a huge number of operational difficulties in

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I THINK WE HAVE A VC SYSTEM WHICH HAS NOT FUNDAMENTALLY CHANGED SINCE IT STARTED IN AMERICA IN THE EARLY 70S.

Michael Jackson

handling payments received from these ICOs in cryptocurrencies. It's not like you can just call your bank and put the money in your account. It is impossible at the moment, but it will happen. Custodians for cryptocurrencies will naturally appear as a lot of people have cryptocurrency and they do not want to keep it under mattress.

Do you know of any custodian who is accepting cryptocurrencies in Luxembourg?

No, not yet. There should be one; there's no reason why there shouldn't be one. They will need a different concept for security on a multi-level. Something needs to happen around the regulatory framework.

The challenge is coming because most companies and ICOs are advertising on the Internet and Facebook, tapping into the retail world. But we know that selling financial products to retail investors is not allowed or at least it is very tightly regulated. I haven't seen a need for new regulation to stop people doing bad things in ICOs as long as it can be stopped now under the existing laws. People ask me why this isn't happening, why isn't the SEC enforcing this? My view is quite simple: there's no hurry for regulators. I think a lot of the early investors and entrepreneurs I meet look at securities law as they do the Highway Code; if the police don't catch you speeding then you pretty much get away with it and don't need to worry. But this isn't the case with securities law and other regulations. I think the advantage we have in Europe is that the regulator can come up with circulars very quickly, which means that the schemes people are cooking up with Switzerland, Singapore, and the Cayman Islands can be stopped very quickly in Europe with a CSSF circular, for example.

There is another school of thought about regulators wanting to stop cryptocurrency because it may undermine the Euro. I think that's complete nonsense. Regulators, at least in Europe, don't exist to stop you doing things. They exist to protect investors, so they are not going to stop it, but what they will do is clamp down hard on retail. What they need to do, in my opinion (and I think that this is something we can work on), is establish a retail investment framework that is acceptable for smaller issuances and doesn't require a full MiFID implementation for an offering. When it comes to the prospectus directive, we need to be able to think about mini prospectuses for small cap offerings rather than maxi prospectuses. We need to think about what kind of organisations can make the issuances. The bottom line is that we don't have a facility in Europe for smaller fundraisings, and yet we have tremendous amounts of money tied up in zero interest bank accounts from people who have a few thousand Euros and who like to invest some of it into the venture of someone they know and trust.

Another trend from the last ten years is the greater transparency of businesses. It used to be impossible to get an idea of how a business was doing. Now we can read about it on the internet, see it on their website, their forums, in their customers' responses. We can also check their audited annual accounts in the Registre de Commerce of Luxembourg and in most of Europe.

I would like to reset our expectations in terms of regulation and see a new mini IPO environment emerging for ICO-like smaller listings, accessible for retail investors. I think we've maybe gone too far in terms of regulation and MiFID II is a good example of this. The goal of the European financial system should be to get more capital at work powering businesses and business growth in a responsible and protected manner. The law just needs to be adjusted to help promote growth in the European economy.

Your recent report "Tokenisation: implication for the venture capital industry" acts as something of a wake-up call to all VCs to take the competition seriously. Why did you choose to go down this route?

Because I'm annoyed about the process. I see the fundraising process as inefficient for VC companies and for the entrepreneur who has to spend a lot of time going through a somewhat random and unstructured process. In the end it depends a lot on whether an entrepreneur is reaching the right person at the right time and who is in the right mood to listen, and that doesn't feel right to me. I think we have a VC system which has not fundamentally changed since it started in America in the early 70s or just beforehand, and three decades later in Europe. I think it is the right way to look at it, and at Mangrove Capital Partners we are certainly not afraid to question our own existence. Indeed we ask our entrepreneurs to question their own existence, to be disruptive, to think, to move forward, and move with the times, and, of course, we can't sit in our fancy offices in Luxembourg earning 2% management fee and 20% carry without continually demonstrating our value.

Do you consider tokens and cryptocurrencies as an asset class? What kind of triggers could make it available for a wider range of investors?

Yes, I think they are an asset class with proper characteristics, uncorrelated to other asset classes and to the Stock Exchange or the real world or anything at the moment. It's rather sentiment-based.

In terms of a trigger, it needs to come through structured products and should be available through trading platforms like E-trade, where you can already buy Bitcoin,

or through banks. In terms of the structured products, I could imagine funds-based products with baskets of cryptocurrencies and derivatives.

Do you see any interest among VC firms in the potential for using digital currencies and ICOs?

Yes. I was recently involved in an experiment with a Berlin-based company where equity was tokenised, so that one token was equal to one share. One of the aims of this was to manage the employee stock option plan, which is very complicated and involves managing, granting, vesting, cancelling and exercising of stock options for a large number of employees. And it's a nightmare. To do this, we created a smart contract which is a self-executing contract, connected with the employee payroll database, so it could automatically manage the share structure or the share cap online. Entrepreneurs and other players have been looking at tokenisation because it gives them access to the crypto world and I think there are going to be some crypto-funds in the future. We are looking at it at Mangrove as well, trying to find out when it would really make sense. Everybody says it's going to give you liquidity in the fund because your shares or units are going to be tradable. But if you are going to have tradable units then you almost become a mutual fund, so what's the point for VC firms?

Can you invest in a company today using ETH (Ether) instead of using Euros, for example?

There's nothing that really stops us from doing that today. Our limited partnership (LP) agreement, however, stops us at the moment because we disclose the currencies we invest in, amongst other things. But if we said to our limited partners that we want to invest in a company with the underlying asset being an equity priced in Ethereum or other distributed ledger, that would be okay. For the majority of the funds, our fund structures oblige us to invest in equity. To invest in tokens, a change to the LP agreement would be required, meaning that LPs would need to be comfortable with that. And that's a stretch when it comes to the institutional world, typically represented by large insurance companies or pension funds, for example. When they talk about alternative assets or alternative lending they are talking about household mortgages as alternative lending or securitised assets. It's going to be a long, long way to cryptoassets.

As a VC have you considered using an ICO as an exit strategy for your portfolio companies?

Yes, absolutely.

In which type of companies would you use it? Only in tech companies?

Like IPO, it would be the kind of company that can do a successful ICO and engage with a lot of customers. It's a good exit strategy. We haven't done it yet but it could happen.

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THE LAW JUST NEEDS TO BE ADJUSTED TO HELP PROMOTE GROWTH IN THE EUROPEAN ECONOMY.

Michael Jackson

Is it in the pipeline, maybe?

No, not really, but only because we don't have an obvious target in our portfolio.

Should Luxembourg aim to become the global financial centre for cryptocurrency funds (as it did for mutual and alternative funds), and if so, what steps need to be undertaken to achieve this?

The answer is a resounding yes. First of all, why would we not do that? We have a good fund environment. We obviously need people who are willing to set up the infrastructure around that, as we said, the custodian, the accounting, all of this needs to be there. I think the risk management framework is fine. We have tier-one data centres and good ideas.
Secondly, I believe we can establish a mini-listing concept as we have a fairly well-functioning stock exchange. And we are nimble enough to do it, as we have a good regulator and the Luxembourg economy is pretty strong. We just need to come up with the right framework.

As we come to the last question... have you invested your own funds in virtual currencies or tokens?

Yes, I have. ●

FUND STRUCTURING – ISSUING TOKENS IN A FUND

By Yannick Arbaut
Counsel, Allen & Overy
Luxembourg

INITIAL COIN OFFERINGS ("ICOS") HAVE MADE RECENT HEADLINES IN THE NEWS, SOME SUCCESSFUL ICOS RAISING MILLIONS IN RECORD TIMES. THIS HAS SPARKED AN OBVIOUS INTEREST IN THE VENTURE CAPITAL AND STARTUP SECTORS, BUT ALSO WITH FUND MANAGERS. STRUCTURING A LUXEMBOURG INVESTMENT FUND RAISING MONEY THROUGH TOKEN SALES IS A TEMPTING NEW OPPORTUNITY; THERE ARE HOWEVER A NUMBER OF CONSIDERATIONS TO BE TAKEN INTO ACCOUNT AND STILL SOME UNCERTAINTIES.

All about securities

The principle here is for a fund to issue tokens or coins in consideration for fiat currencies (or potentially virtual currencies). "Are these tokens securities or not?" is the first question that comes to mind. When tokens are issued in the context of a fund, they will likely and should qualify as securities and should, from a legal perspective, be treated as any other security. Tokens will be a more advanced form of dematerialised securities, presumably even offering greater transparency and security. The offering is not a typical ICO but rather a token sale, to the extent that the tokens will be asset-backed and the consideration paid in exchange for the tokens will be used to make investments in accordance with the fund's investment strategy. The resulting questions are then similar to those which other types of funds face, but with the added complexity of the distributed ledger technology and its resulting legal uncertainties (for example, regarding the register of "securities").

What about fund rules and restrictions?

Luxembourg alternative investment funds, whether subject to regulatory supervision or not, are subject to a number of rules that apply in other sectors as well such as AML/KYC requirements, eligible investor or marketing restrictions, to name only a few. Structuring a fund issuing tokens means that some of these requirements will need to be complied with in the blockchain world. How do you identify token holders? Permissioned blockchains limiting and identifying the parties who can transact may be a solution. Cooperation between the fund's service providers and selected regulated exchanges (who perform AML/KYC) may be another. Only pre-identified and eligible investors are granted access and can then freely acquire or sell their tokens. Regulators could even be granted full access to the blockchain resulting in greater transparency. Permissioned blockchains do not solve all issues, but the issue of anonymity can be solved to a certain extent.

Why?

Tokens may be tradable 24/7, offer security, traceability and greater transparency than typical securities. Exchanges may offer liquidity to the tokens, even for funds with rather illiquid underlying assets. A number of uncertainties remain though for which there are no clear cut solutions. Some will be solved by first movers, and others will require legal or regulatory clarifications, although EU regulators seem to have adopted a rather passive approach with messages to caution firms and investors. ●

THE CHALLENGE OF CRYPTOASSETS VALUATION FOR INVESTMENT FUNDS

By **Marie-Line Ricard**
Partner and Blockchain Leader,
PwC France and French-speaking Africa

and **Grégory Weber**
Head of Research and FinTech Leader,
PwC Luxembourg

Cryptoassets are mushrooming, with over 1,400 different cryptoassets and the market capitalisation exploding from approximately EUR15 billion at the end of 2016 to over EUR600 billion today. But not all cryptoassets are created equal, and defining the value characteristics of cryptoassets can be difficult. As such, valuation remains a work in progress.

Ample due diligence is needed to determine what the cryptoasset represents and its utility value based on the balance of supply and demand. A mark-to-market approach can be used for the main cryptoassets that are traded on exchanges, however, price differences between exchanges are still noticeable. In the absence of a market price and sufficient liquidity (e.g. new cryptoassets issued through an Initial Coin Offering), investors and fund managers should agree on a valuation approach that could be based on various qualitative aspects, including how the asset relates to others, issuance model and supply schedule, developer quality, community adoption, and so on.

Asset valuation is complex and should be discussed with authorities to understand the regulatory and tax implications. The approach should be clearly described in the fund prospectus and include details such as the policy related to events such as forks (which are most often protocol upgrades). Applicable accounting norms could depend on the asset's legal qualification, formalised either as financial or non-financial assets. Currently, while there are arguments in favour of a formal legal qualification as financial assets, uncertainties remain and will need to be addressed before formalisation. ●

"CRYPTOASSETS ARE LIKELY TO BECOME PART OF THE FUND LANDSCAPE"

LPEA ASKED DR. PINAR EMIRDAG, SENIOR VICE PRESIDENT AND HEAD OF DIGITAL PRODUCT DEVELOPMENT AND INNOVATION AT STATE STREET, HER VIEW ON THE OPENING OF BANKS TO CRYPTOCURRENCIES.

By **Pinar Emirdag**
Head of Digital Product Development and Innovation, State Street

From your perspective, what is the current appetite for developing new services in relation to cryptocurrency in your bank?

Institutional interest in cryptocurrencies and related digital assets increased over the course of 2017, and continues today. In line with market demand, we are considering all appropriate service offerings that may be developed around the emerging cryptoasset class. This includes:

- fund administration services and the challenge of creating Net Asset Value for these alternative assets;
- custody services for cryptoassets that may require sub-custodian relationships or self-custody models; and
- the creation of indicators and other data services that provide insights and intelligence regarding cryptoasset movements and correlation to evolving regulatory frameworks.

As the markets develop to cater for the needs of institutional investors, our areas of exploration are likely to broaden.

What would be the biggest challenges in implementing these new facilities, such as depositary services, for cryptoassets?

There are many challenges in implementing new services for cryptoassets, from regulatory landscape to security, lack of a developed market structure to tools, and needing to deal with the intricacies of the instruments themselves. Many of these challenges are not uncommon when building new services for new asset classes. The regulatory opinions vary vastly from jurisdiction to jurisdiction, and are mostly still in development, with a lot of inconsistencies. Similarly, on/off ramps to cryptoassets are in development, catering for OTC platforms.

Alongside the nature of the instrument itself, the lack of a well-connected market structure contributes to the volatility of the assets. An equally daunting challenge exists around the implementation of appropriate security principals for these cryptoassets that, by-design (for the most part), operate on a network of anonymous participants. While there are implementations that have evolved providing certain levels of KYC/AML capabilities, these will require thorough analysis to ensure fraudulent individuals can be identified and appropriately controlled.

Many of the markets we serve today started in similar ways, some dating back hundreds of years while others over the last decade or two.

How can a jurisdiction such as Luxembourg become a global financial centre for cryptocurrency funds?

As cryptoassets and their market structures develop, they are likely to become part of the fund landscape and it will be difficult to make a distinction. This is in line with alternative funds that are already looking into these instruments. Similarly, managers from well-established funds have been moving to this space and setting up new funds. The above points will need to be tackled in order for any jurisdiction to appropriately support this evolving space. ●

LUXEMBOURG IN THE CENTER OF HLD GROUP'S EUROPEAN AMBITIONS

HLD GROUP IS A FRENCH INVESTMENT FIRM FOUNDED IN 2010 PROVIDING LONG-TERM FINANCING TO FRENCH AND EUROPEAN COMPANIES AND MANAGING TODAY IN EXCESS OF EUR700 MILLION. WITH AN ATYPICAL INVESTOR BASE AS WELL AS INVESTMENT HORIZON, HLD MADE THE DECISION, EARLY IN ITS HISTORY, TO TURN TO LUXEMBOURG TO SUPPORT ITS EUROPEAN AMBITIONS. LET'S COME BACK ON THE WHY AND HOW WITH HLD GROUP'S CFO ANNE CANEL AND TWO ICONIC LUXEMBOURG ENTREPRENEURS ACTING AS INDEPENDENT DIRECTORS IN HLD'S INVESTMENT VEHICLE, ROBERT DENNEWALD AND XAVIER BUCK.

By **Arnaud Bon**
Director – Strategy, Regulatory & Corporate Finance, Deloitte

Given that HLD Associés is a relatively young French investment firm with a very strong footprint in France but limited presence or activities in other countries, what drove you to open an office in Luxembourg a few years ago?

Anne Canel (AC): HLD Group was founded in 2010, with wealthy French entrepreneurs as anchor investors and partners but also a main investment focus in France. We quickly perceived that growth meant we needed a hub that would be less French-centric and more open to the international world, both to penetrate new investment markets and for fundraising purposes. This was the main driver for opening our Luxembourg operations in June 2015.

We raised €70 million the following year through a bond issuance on the Luxembourg stock exchange. We would likely not have been as successful in France, as our main fundraising efforts in Luxembourg focused on the private banking and wealth management sectors. For HLD, this has been a real chance to diversify its source of funding from a handful of French industrial families, such as DentresSangle, Bébéar or Decaux. Further to the bond issuance, we also admitted the Italian De Agostini as equity investors in our vehicle.

We not only used Luxembourg as a fundraising hub but also an investment platform outside of France. In September 2017, we completed our first investment in M-Cube, an Italian technology company, to help it expand internationally. HLD's management believes that Luxembourg is an ideal location from which potential acquisitions can be sourced, structured, and managed.

Besides Luxembourg, were other countries and cities considered to give this international touch to HLD?

AC: At the time, London and Brussels were also considered. Luxembourg was eventually chosen for its geographic

location as well as for the recognition it receives internationally as a hub for Private Equity investments.
In Luxembourg, we have found a developed Private Equity environment with a rich investment vehicle toolbox as well as a mature ecosystem composed of fund managers and service providers. We understand that Luxembourg has made Private Equity development one of its priorities, which is comforting when operating an evergreen investment vehicle for which we need long-term legal, regulatory, and tax stability.

I understand one of HLD's trademarks is the fact that the fund you structured is evergreen, with a stable investor base composed of private investors. How does it make HLD different from other PE investment firms?

AC: We can afford the luxury of time. Our investment time horizon is not constrained by the term of the fund. HLD invests in companies with a sound development project and we can take the time we need to achieve that objective.
This allows us to have a real industrial approach. HLD efficiently combines an industrial approach with a financial approach, inherent to all investment activity, where time remains the best ally to create value at the portfolio level.

Robert, Xavier, you are both, in your respective fields, captains of the industry. Is this the reason you decided to join HLD as independent directors?

Robert Dennewald (RD): I come from the industry, and more particularly, a company that has been operating for over a century. Aligning long-term investment and target development strategy is key to success. In my world, when considering investment options, the time horizon rarely counts in anything else then decades. HLD's approach of accompanying its portfolio companies until maturity—meaning when a sale makes sense for the target rather than the investor—is an important differentiator from other Private Equity players I have seen operate.
In addition, having different business exposures than HLD's management and team, I can contribute to deal sourcing in my activity sectors.

Xavier Buck (XB): Another interesting differentiator lies in HLD's approach with respect to sectors. We have invested in targets as different as Kiloutou, signed in December 2017, Gekko, an online hotel-booking platform sold to AccorHotels in October 2017, and Filorga, acquired in 2010 and now a worldwide success with an annual growth of over 40 percent.
With each of those acquisitions comes a dedicated team of specialists. After all, management and investment are first about people. It is consequently important for a firm to invest in what its professionals understand. Giving all the merit to the investment team based in Paris, at our level, Robert and myself bring our industry and sector expertise and experience.

HLD has an office in Luxembourg—Anne you act as the Group's CFO. I would consequently assume that you did not decide to appoint Robert and Xavier as independent directors for what is usually referred to as "substance reasons"...

AC: This is correct. We have all the "substance" we should have in Luxembourg but wanted to make sure we also had the adequate governance at the level of our investment vehicle. We are of the opinion that proper governance is a key success factor for any enterprise, be it in the investment management industry or else. This is a source of comfort for our investors, as Xavier and Robert are truly independent and can bring divergent opinions, views, and experience in the discussion.
We also wanted to compose a board well-balanced in term of competences and personalities.

How does this governance work in practice?

RD: HLD Europe replicated the French management model, with a board of directors and a supervisory board. This two-headed organization creates safeguards at the top management level.
The board would typically meet on a monthly basis by default, with a standard agenda covering Luxembourg operations as well as, most importantly, investment activity reviews, such as

A Case in Action

Governance tips

- Double-headed management structure with a board of directors and a supervisory board
- Balanced composition in the board
- Monthly board meetings with a standard agenda covering all relevant dimensions of the investment vehicles
- Board pack shared sufficiently in advance to allow a proper review and preparation by board members
- Sufficient board meeting duration
- Mutual professional respect between members to accept "no" as an answer or dare say "no"

HLD Board: Robert Dennewald, Anne Canel, Jean-Bernard Lafonta, Jean-Philippe Hecketsweiler and Xavier Buck.

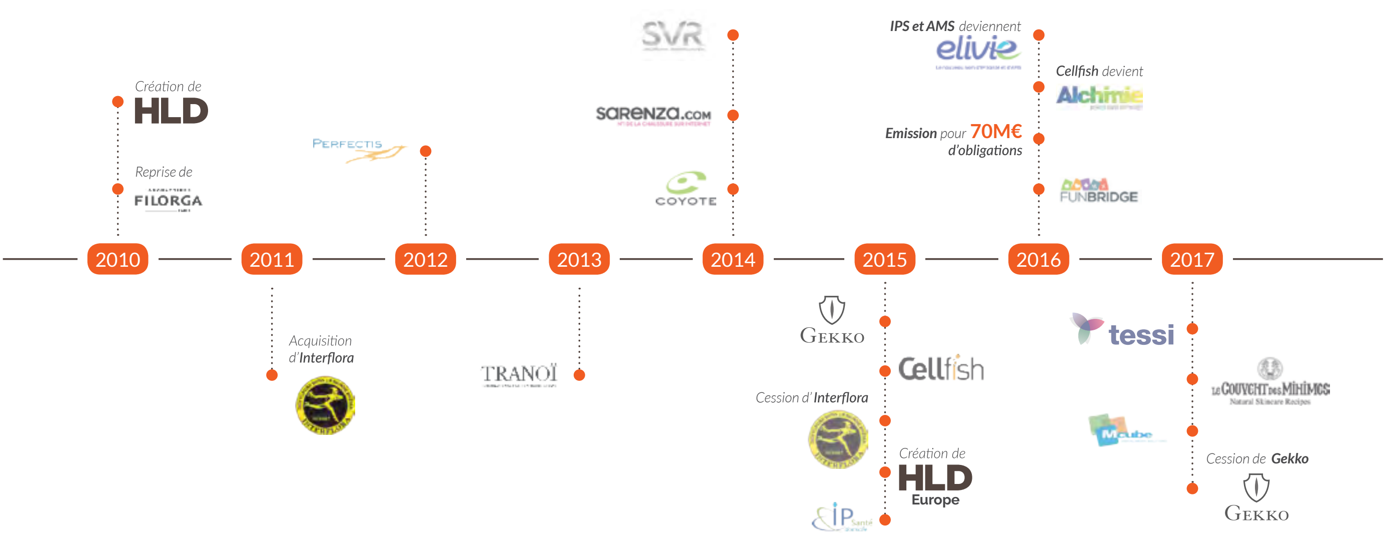
deal flow, investment monitoring, and discussions on potential exits.
XB: In addition to discipline in the board meeting's organization, the quality of the exchanges between board members is paramount to their success. I feel, as an independent board member, that no topic or opinion is taboo, and I have not been proven wrong so far! All decisions of the board are systematically made unanimously, meaning that should divergent opinions arise, we all work together toward a decision respectful of these opinions.
AC: Sufficient preparation before the discussion is also essential. Because each board member is provided with all relevant documents at least a week in advance, when someone opposes a proposed decision, we all understand that there might be serious reasons for this position. It takes mutual professional respect both to prepare a board discussion of the meeting and to accept all opinions around the table.

I would assume it also takes time to properly prepare.

RD: It does indeed. In this way, the policy of the CSSF is to limit the number of mandates a person can hold as a director. One cannot contribute to a board to his or her full capacity when substantial time has not been invested ahead of the meetings.
It also takes time to discuss; our agendas are generally so rich that we had to extend the standard duration of the meetings to three hours.

What could we do to further reinforce or help the industry develop in Luxembourg?

AC: Luxembourg, in general, has done a great job attracting Private Equity fund managers. It is now mainly up to each player to reach a market level playing field consistent with the quality expected from professionals in this sector. Where LPEA could further help would be to offer specific programs to PE board members on relevant topics. ●



THE PRIVATE EQUITY INDUSTRY: TIME TO REINVENT ITSELF OR TO DISAPPEAR...

SINCE ITS BEGINNINGS IN THE 1960'S, THE PRIVATE EQUITY INDUSTRY ("PE") HAS GROWN ENORMOUSLY TO BECOME A SECTOR WORTH MORE THAN USD 4 TRILLION IN ASSETS UNDER MANAGEMENT. IN THE SAME PERIOD, THE PE WORLD HAS CHANGED, AND PAST GROWTH ALONE DOES NOT GUARANTEE THE INDUSTRY'S FUTURE SUCCESS. TODAY, THE PE INDUSTRY STANDS CLEARLY AT A CROSSROADS AND NEEDS TO ENGAGE IN AN IN-DEPTH TRANSFORMATION PROCESS TO CONTINUE BRINGING REAL ADDED VALUE TO ITS CUSTOMERS.


By **José Aubourg**
Director, Private Equity,
EY Luxembourg


and **Olivier Coekelbergs**
Private Equity Leader,
EY Luxembourg

Alongside the industry's strong growth, the competition among players in the race for the best deals has intensified and become fiercer. In addition to the exponential increase of new PE funds and major industrial groups comes the entry of new players such as sovereign wealth funds or some large pension funds, more and more often in direct competition for acquisitions with traditional PE houses. Furthermore, borders between PE houses, investment banks and asset managers have become more and more blurred and open. Nowadays, PE houses represent only 30% of total alternative assets under management.

Competition for deals remains fierce

In a low interest rate environment and with a growing appetite for high returns on investment, the hunt for assets is constantly disputed, with the result being a significant and sustainable growth of valuations and the increasing difficulty of fulfilling a promise of investment profitability. PE houses have no other choice but to either overpay for assets to be able to deploy considerable amounts of "dry

THE DAYS WHERE THE LEVERAGE EFFECT AND "COST-CUTTING" ALLOWED FOR THE GENERATION OF ENOUGH VALUE ON PORTFOLIO COMPANIES ARE DEFINITELY OVER.

Olivier Coekelbergs

powder" that they have accumulated over recent years (USD541 billion in April 2017 against USD473 billion in 2015 and USD470 billion on average for the period 2006 to 2007)* or target lower quality assets.

Nowadays, competition for capital and for investors is also intensifying. In 2017, a record number of 1,865 funds have been attempting to raise approximately USD624 billion[1]. At the same time, we observe a trend of large traditional investors now being much more selective in their choice of management companies or eager to restrict their relationships to a few carefully selected houses.

Value creation at stake

The Private Equity industry is clearly at a crossroads, and should rethink its model as well as engage in an in-depth transformation process to reinvent itself and continue bringing real added value to its customers. The days where the leverage effect and "cost-cutting" allowed for the generation of enough value on their portfolio companies are definitely over. PE houses will need to be more innovative to continue creating value for their investors.

Search for the best talents

The first challenge to take on is to attract talent and to gain a competitive advantage on transactions in developing real expertise, while simultaneously developing in sectoral, geographical and technological areas which can really make a difference in identifying the best targets. This is particularly true for funds with a focus on technology or for Venture Capital funds.

Digital transformation

The second challenge, which is probably the most important, is to be able to create value in portfolio companies. Indeed, using conventional financial engineering techniques, as in the past, is no longer sufficient; one must now be able to support companies in their strategy, as well as in their "business model" and "process" transformation processes in order to improve income and net income. This inevitably implies being able to develop new digital and technological solutions, as well as the ability to attract new entrepreneur profiles capable of achieving the digital transformation of portfolio companies.

The risk of digital gap is to be found first in the PE houses themselves which will have to go through a revolution in their own processes. Curiously enough, PE companies with a strong focus on transactions and the management of portfolio companies have often not really assessed the risk of digital gap within their own organisations and have not yet truly integrated this dimension in their strategies. Most PE houses have not yet appointed someone in charge of their digital development, which would not only allow them to implement a digital transformation strategy in the portfolio companies but would also enable them to transform their own organisations, reduce their costs and optimise their data usage.

The next generation of PE leaders

Finally, the third biggest challenge to take up is the implementation of a real transition plan to allow for the handover to a new generation of partners. The largest PE houses are indeed closely organised around their founders and many of them will be prompted to cease their activities in the coming years. Achieving a smooth transition between old and new leaders is a mutual interest, and there must be the implementation of an attractive scheme for new partners which will likely bring about changes without betraying the root values which will prove to be absolutely critical in the years to come.

The Private Equity industry, though flourishing, should recognise the nature of all the challenges threatening its business model and not push its arrogance to the point of thinking that it could do without an in-depth transformation to embrace the emerging technological revolution. Only the players who will make this shift early enough will be able to survive and continue to thrive. ●

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THE IMPACT OF THE PRINCIPAL PURPOSE TEST ON THE PRIVATE EQUITY SECTOR

LUXEMBOURG SIGNED THE MULTILATERAL CONVENTION TO IMPLEMENT TAX TREATY RELATED MEASURES TO PREVENT BASE EROSION AND PROFIT SHIFTING ("MLI") ON 7 JUNE 2017 AND INDICATED ITS INTENTION TO APPLY IT TO ALL ITS DOUBLE TAX AGREEMENTS ("DTA"), PROVIDED THE OTHER PARTY IS ALSO A SIGNATORY OF THE MLI AND HAS OPTED TO APPLY THE PRINCIPAL PURPOSE TEST ("PPT").

By **Audrey Legrand**
Tax Director (specialising in M&A), Deloitte

Purpose of the PPT

Article 7 of the MLI and Paragraph 9 of Article 29 of the 2017 OECD model convention set out the principles according to which, the benefits of a tax convention should not be available where one of the principal purposes of certain transactions or arrangements is to secure a benefit under a DTA, and obtaining that benefit in these circumstances would be contrary to the object and purpose of the relevant provisions of the DTA.

What are the benefits that can be denied?

A benefit, as targeted by Paragraph 9 of Article 29, includes all limitations on taxation imposed on the State of source (e.g. a tax reduction, exemption, deferral or refund) or the relief of double taxation, such as, for example, limitations on the taxing rights of a State in respect of dividends, interest or royalties arising in that State and paid to the resident of the other State or over a capital gain realised by the alienation of movable property located in that State by a resident of the other State.

Example of PPT application in the private equity sector

The OECD gave illustrations of how the local tax authorities could assess situations to determine whether the benefit of the DTA should be granted or denied in light of Paragraph 9 of Article 29. According to the OECD, such examples shall not be construed as being more than mere illustrations. Nevertheless, aligning an organisation's business operating model to resemble the examples given by the OECD cannot per se be detrimental.

The example that appears to be the most relevant to the private equity sector concerns a "regional investment platform". In this example, a company resident of State R ("RCo") is a wholly owned subsidiary of an institutional investor, an investment fund established in State T and subject to State T's regulation (the "Fund"). The example details that RCo operates exclusively to generate an investment return as the regional investment platform, through the acquisition and management of a diversified portfolio of private market investments located in countries in a regional grouping that includes State R. The example further clarifies that the decision for establishing the regional investment platform in State R was driven by (i) the availability of directors with knowledge of regional business practices and regulations, (ii) the existence of a skilled multilingual workforce, (iii) the State R's

WHILE THE OECD FURTHER ELABORATES THAT THE INTENTION OF DTAS IS TO ENCOURAGE CROSS-BORDER INVESTMENTS, IT ALSO OUTLINES THE NECESSITY OF CONSIDERING THE CONTEXT IN WHICH THE INVESTMENT WAS MADE.

Audrey Legrand

membership of a regional grouping, and (iv) the extensive DTA network of State R, including its DTA with State S, which provides for low withholding tax rates.

In terms of substance, the OECD notes that: (i) RCo employs an experienced local management team to review the Fund's investment recommendations and performs various other functions; depending on the case, the other functions may include approving and monitoring investments, carrying out treasury functions, maintaining RCo's books and records, and ensuring compliance with regulatory requirements in States where it invests; and (ii) RCo's board of directors, appointed by the Fund, comprises a majority of State R resident directors with expertise in investment management, as well as members of the Fund's global management team. RCo pays tax and files tax returns in State R.

While the OECD further elaborates that the intention of DTAs is to encourage cross-border investments, it also outlines the necessity of considering the context in which the investment was made. The context can include the reasons for establishing RCo in State R, the investment functions, as well as the other activities carried out in State R. The OECD concludes that, on these facts, it would not be reasonable to deny RCo the benefit of the State R-State S DTA in the absence of other facts or circumstances, showing that RCo's investment is part of an arrangement or relates to another transaction undertaken for the principal purpose of obtaining the benefit of the DTA.

This illustration tends to support the investment scheme having the following core elements located in one single jurisdiction: (i) the regional investment platform whose shares would be held by the institutional investor, (ii) the SPVs holding the investments, and (iii) the service company in which the substance could be pooled and the core commercial activities be conducted and sub-delegated to the SPVs, rather than the old investment scheme where each local investment would be held by a local SPV whose shares would be held by the institutional investor.

The choice of the jurisdiction in which the platform would be established would then be based on multiple factors such as political stability, the legal framework adapted to business needs, the possibility of hiring qualified personnel, as well as, of course, a robust DTA network. At Deloitte, we believe that Luxembourg offers all of this and that, in the future, Luxembourg will increasingly become the preferred location for funds and investment platforms, and it seems that our clients, the major private equity players, are of the same opinion as we accompany them in the different aspects of their move toward an organisational substance similar to that described above. ●

THE IMPACT OF THE MULTILATERAL INSTRUMENT ON PRIVATE EQUITY STRUCTURES IN LUXEMBOURG

ON 7 JUNE 2017, LUXEMBOURG SIGNED THE MULTILATERAL INSTRUMENT (MLI) WHICH WAS DEVELOPED BY THE OECD TO INTEGRATE BEPS MEASURES INTO DOUBLE TAX TREATIES. THIS ARTICLE PROVIDES AN OVERVIEW OF THE MLI'S IMPACT ON LUXEMBOURG INVESTMENT STRUCTURES, WITH SPECIFIC FOCUS ON THE APPLICATION OF THE PRINCIPAL PURPOSE TEST (PPT).

By **Giuliano Bidoli**
Partner, M&A,
KPMG Luxembourg

and **Sophie Richard**
Senior Tax Manager,
KPMG Luxembourg

The MLI: an overview

The MLI will update an existing network of more than 1,100 bilateral tax treaties, putting in place measures to prevent treaty abuse (BEPS Action 6), changes to the definition of permanent establishment (BEPS Action 7), changes to the residence tie-break for companies (BEPS Action 2), and mutual agreement procedures and mandatory binding arbitration (BEPS Action 14). The changes in the MLI will apply only if both parties to a double tax treaty have designated it as a covered tax agreement (CTA). Certain measures are BEPS minimum standards, whereas others are non-minimum standards.

As part of the minimum standards, the anti-abuse PPT has been adopted by all current signatories. The objective of the rule is to refuse treaty benefits if it is reasonable to conclude, taking all facts and circumstances into consideration, that obtaining such benefits was one of the principal purposes of an arrangement or transaction, unless it is in accordance with the object and purpose of the relevant provisions of the tax treaty. This rule can be supplemented by a provision that requires the competent authorities applying the PPT to consult with each other, upon request from the taxpayer, before denying treaty benefits. Some countries also intend to supplement the PPT with a limitation on benefits (LOB) clause, or through subsequent bilateral negotiation with treaty partners.

Luxembourg's choices

Luxembourg has chosen to include all its tax treaties that are in force in the MLI; however, out of these 81 tax treaties, only 55 are currently CTAs based on the choices made by other States, as of 22 September 2017[1]. Currently, Luxembourg has not made many choices in the provisions of the MLI that will be incorporated into its double tax treaties, and the changes it has opted for are effective and pragmatic. In a nutshell, Luxembourg respects the minimum standards and does not go much further.

Luxembourg has decided to insert the PPT rule into its CTAs, as an anti-treaty abuse provision, as well as the rule providing for the consultation process

THE APPLICATION OF THE PPT RULE BY LOCAL TAX AUTHORITIES WILL GENERALLY REQUIRE TAXPAYERS TO DEMONSTRATE THAT THEY HAVE AN ADEQUATE LEVEL OF SUBSTANCE IN LUXEMBOURG AND VALID COMMERCIAL REASONS FOR SECURING TREATY ACCESS.

Giuliano Bidoli

prior to the denial of the treaty benefits based on the application of the PPT rule. With reference to the current choices made by Luxembourg's treaty partners, the simplified LOB rule should not apply to Luxembourg's CTAs; however, the application of a detailed LOB might still be possible based on the upcoming bilateral negotiations with countries that have expressed the willingness to insert such a clause into their treaties (for instance Canada and Poland).

Impact on Luxembourg investment structures

The application of the PPT rule by local tax authorities will generally require taxpayers to demonstrate that they have an adequate level of substance in Luxembourg and valid commercial reasons for securing treaty access. The comments on the PPT clause contained in the OECD Model Convention provide further guidance on the application of the rule and should be considered a key source in this respect.

In particular, the examples on non-CIVs[2] give useful information. One of these examples[3] depicts the situation of the acquisition by Company A, which acts as a regional platform, of Company B, which is located in another jurisdiction. The PPT should be met and, accordingly, Company B could benefit from treaty benefits in cases where the decision to establish the subsidiary in that jurisdiction was driven by the availability of directors with knowledge of regional business practices and regulation, the existence of a skilled multilingual workforce, the existence of an extensive network of tax conventions and the company's employing an experienced local management team to review and perform various functions which may inter alia include approving and monitoring investments.

On this basis, one might conclude that a Luxembourg company that is owned by a foreign or domestic fund, has appropriate substance, and whose main management and administrative decisions are taken in Luxembourg by a board of directors with strong industry knowledge, should be considered the beneficial owner of the income received from its investment, meet the PPT and, accordingly, benefit from the tax treaty provisions.

The next steps

The exact impact of the PPT clause on investment structures nevertheless remains dependent on the application of this rule by local tax administrations. Taxpayers with Luxembourg structures that rely on tax treaty benefits and for which the tax treaty is a CTA will, therefore, need to closely monitor any local tax developments in this respect.

The date of application of the new rules is not yet known, and will depend on the MLI ratification process in Luxembourg and in the other contracting States. It is nevertheless not expected that they would apply before 2019 or 2020 at the earliest. ●

1. Situation as of 22 September 2017. For the Americas: Mexico, Uruguay, Canada; for Europe/Eurasia: Andorra, Armenia, Austria, Belgium, Bulgaria, Croatia, Czech Rep., Denmark, Finland, France, Georgia, Germany, Greece, Guernsey, Hungary, Iceland, Ireland, Isle of Man, Italy, Jersey, Latvia, Liechtenstein, Lithuania, Malta, Monaco, Netherlands, Norway, Poland, Portugal, Romania, Russia, San Marino, Serbia, Slovak R., Slovenia, Spain, Sweden, Switzerland, Turkey, UK; for ASPAC: China, Hong Kong, India, Indonesia, Japan, Korea, Mauritius, Singapore; for Africa/Middle East: Israel, Seychelles, Senegal (not yet in force), South Africa.

2. Initially included in BEPS Action 6 Discussion draft on non-CIV example dated 6 January 2017.

3. 2017 draft OECD commentaries on paragraph 9 of Article 29, example K.

MARKET UPDATE

A GROWING PREFERENCE FOR PRIVATE EQUITY

By Dariush Yazdani
Market Research Centre,
PwC Luxembourg

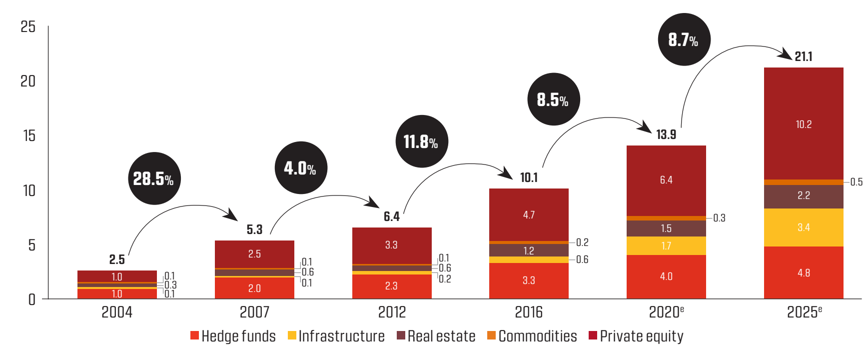
Following the global financial crisis, as investors search for yield and diversification, alternative asset classes have seen a remarked upsurge in investment. PwC expects alternatives to continue their rise and will reach USD13.9 trillion in 2020 and USD21.1 trillion in 2025. This growth is expected on the back of multi-asset, outcome-driven solutions rising in prominence, booming infrastructure, and the sustained strong growth of private equity.

Investor appetite for private equity has grown in recent years. Low correlation with traditional asset classes in the post-crisis period increased its attractiveness, while a low interest rate environment made money cheaper for leveraged funds. Institutional investors' preference for long-term investments has benefitted illiquidity premiums and, at the same time, the rise of emerging markets have driven up growth rates and led to private equity maintaining its position as the most dominant alternative asset class. Between 2007 and 2016, its AuM almost doubled, to reach USD4.7 trillion. Locally, Luxembourg's regulated private equity market experienced even greater growth as AuM quintupled over the same period reaching USD108 billion. Regulated private equity funds are vastly popular in Luxembourg, best illustrated by SIF AuM growing from EUR2 billion in 2007 to EUR63.2 billion in 2016. This is largely due to their greater flexibility, in terms of available fund vehicles and applicable investment rules. SICAR funds also showed notable growth as sustained increases since 2013 saw AuM reach EUR41.6 billion. Despite this, unregulated funds, SCSps in particular, are still the most adopted legal framework (80% of private equity funds) due to their universally understood fund structure.

Regarding firms, new opportunities in the market are being considered as the total volume of "dry powder" reached USD942 billion in September 2017. Pressure, however, is being applied to firms as competition and costs rise, as well as increasing investor demand for greater transparency surrounding fee structures. Looking ahead, the current resurgence of mega funds offers a potential source of funding to boost AuM.

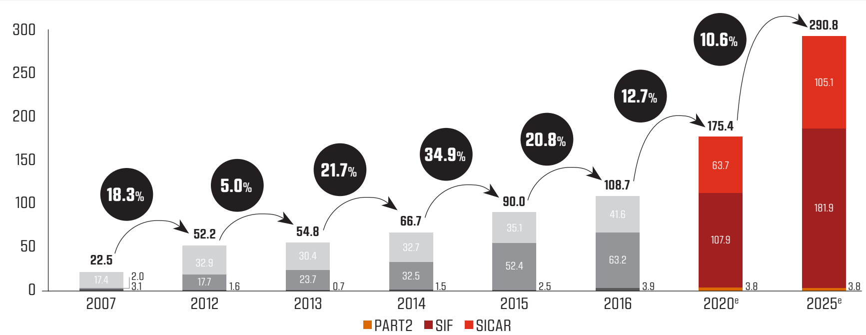
Private Equity is experiencing strong growth both globally and within Luxembourg, despite increasing pressures. Current trends point to greater positives for the industry as expected market conditions favour private equity among other asset classes. Favourable conditions and a well regulated market will likely draw funds to Luxembourg in the future. ●

Global Alternative AuM Growth (USD trillion)



Source: PwC Market Research Centre analysis. Past data based on Preqin, Lipper, and Hedge Fund Research.

Global Alternative AuM Growth (USD trillion)



Source: PwC Market Research Centre analysis. Past data based on CSSF and Monterey Insight 2017.

EASTERN EUROPE AND TURKEY FROM A VENTURE CAPITAL POINT OF VIEW

By **Roland Manger**
Co-Founder and Partner
Earlybird Venture Capital

The partner team behind Earlybird's Digital East Fund (DEF) for CEE and Turkey came together from different backgrounds: one partner had engaged in opportunistic investments in the East from previous funds, another one had covered the region for a U.S. corporate investor and two had built a reputation as successful angel investors. Through research and personal experience, we came to the conclusion that the region provided a medium- to long-term buyers' market for earlier stage technology investments, and the resulting economic advantages were outweighing the specific risks of our area.

The Venture Capital (VC) business model

While most Private Equity funds invest in good companies to help them become better, grow faster or generate more profit, VC funds look for groups of people that can either create large new markets or turn existing ones on their head. The risk inherent on an individual investment might be high; however, research into VC returns, and their volatility, has shown the total portfolio risk of well-managed funds to be relatively low.

Supply and demand factors in the region

As in any market and for any business, the economic upside of VC investing depends on supply and demand for some key factors. More specifically, VCs rely on having access to the best possible human resources, eg entrepreneurs, engineers, commercial specialists, who are able to create or disrupt major markets against tremendous headwind from large incumbents and significant resistance to change from potential customers and users.

We believe that raw entrepreneurial talent can be found anywhere in the world. As technology investors, we also realise that the standard of technology and engineering education in our region is quite high.

Unlike China, India, the U.S. or parts of Western Europe, Eastern Europe and Turkey have not been the global hot spots of VC investing, with hardly any experienced fund managers looking at opportunities in an area where the population is not much smaller than that of the U.S. Few VC teams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on the ground means much less capital-chasing available opportunities, and an environment in which founders have realistic valuation expectations. In this type of buyers' market for start-up equity, entrepreneurs know how to do more with less. Both factors, lower entry prices and higher capital efficiency, have a direct and positive impact on investment returns.

Opportunities pursued by Earlybird´s Digital East Fund (DEF)

Based on this favourable supply and demand situation, DEF is pursuing a two-pronged strategy:

1. We look at large local markets that are ripe for digital disruption, such as intercity transport, real estate, and property management. Segments within these markets that are undergoing offline-to-online conversion, or those that are facing software-driven transformation, are particularly interesting. We can usually avoid technology and business model risk as often there have been similar winners in other, more advanced, markets.

Following the example of Wayfair, the U.S. leader in online furniture retail, Vivense has become number one in the Turkish online furniture market. When the company started in 2013, only 3% of all sales were online compared to 8% in the U.S.[1]. By 2017, its turnover (GMV) reached USD30 million. We expect the online share of furniture sales to increase to 9% by 2023 while Vivense will be growing its own market share even further.

For this first strategy, presence in large local markets is critical.

2. Our second investment strategy, however, does not rely on the location of the team. We look for world-class founders hailing from CEE and Turkey that are driving innovation in enterprise technologies, addressing the global market from the outset.

When we first met UiPath in Bucharest in 2015, the company had less than USD1 million in revenues. Its Robotic Process Automation software, however, had already caught the attention of some enterprise early adopters and leading-edge tech analysts. By the end of 2017, the company recorded mid-double-digit million dollar Annual Recurring Revenues (ARR), moved its headquarters to the U.S., and is continuing its meteoric rise.

Specific risks and mitigation

Part of our region is not within the Euro Zone, so we are aware of currency risk; however, a large share of our portfolio companies, the ones that sell to enterprises around the world, draw most or all of their revenues in hard currency. Those that address local markets, specifically in Turkey, are subject to currency risk but their expenses are also mostly in local currency and their growth rates on a U.S. Dollar basis are still quite high.

There are political and regulatory risks. Not all of which can be mitigated, although we set up holding structures in Western Europe or the U.S. to take advantage of superior governance standards. We also strive to avoid heavily regulated industries.

Whatever risks remain in our region we attempt to balance or even outweigh them by taking advantage of favourable supply and demand conditions, and the resulting proprietary deal flow. ●

1. Source: Euromonitor

LETZLIVE

INTRODUCING NEW MEMBERS

INTERMEDIATE CAPITAL GROUP (ICG)

First name Paul

Last name King

Job title Director and Conducting Officer

City and Country of origin Melbourne, Australia

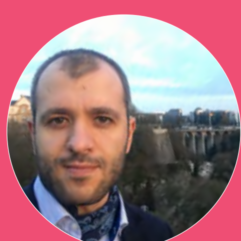
In Luxembourg since 2007

Three reasons to live in Luxembourg
1. Location. Very centrally located, and great for weekend trips to anywhere in Europe.
2. Beautiful city, villages and countryside like the Mullerthal region, which are a pleasure to walk around. 3. A very multicultural population, which brings a variety of languages, food and creativity.

Best tourist attraction Luxembourg City itself, with its fantastic old city walls, buildings and remnants of its medieval past. It offers amazing walks and views of the surrounding city from the lookouts.

Surprising Luxembourg... Luxembourg has produced a pair of Nobel Prize winners (Jules A. Hoffmann and Gabriel Lippmann). That puts it third on the list of prize winners per capita, just ahead of Sweden – well done Luxembourg!

CREON CAPITAL S.À.R.L.



First name Ruslan

Last name Zaidan

Job title Member of the Board of Directors

City and country of origin Moscow, Russia

In Luxembourg since December 2016

Three reasons to live in Luxembourg It is in the centre of Western Europe. It is a well-interconnected business community, very multicultural and diverse.

Best tourist attraction Vianden Castle

Surprising Luxembourg... The world is too small!

JOGGING IN LUXE

1. You may actually begin anywhere but starting in the Vallée de la Pétrusse will allow you to warm up for a few kilometres on a level part of the course surrounded by beautiful scenery.
2. Short but unusual run over the old wall before the first climb.
3. Plateau du Rham: take a break and look around – the old city on one side and the former barracks (now retirement home) on the other.
4. Run along the Alzette and take a look at Les Rives de Clausen on your right – entertainment guaranteed.
5. Cross the very old bridge and take the steep climb up, but don't forget to take a downward look at Neumünster Abbey.
6. Run below the old drawbridge at Sigfried's castle.
7. While running up towards the Kirchberg, do not miss the Tour Malakoff, hidden in the woods a few metres away from the bustling city.
8. Cross the Place de l'Europe with its impressive buildings while running towards the MUDAM.
9. Stop for a few minutes to take a look at one of the most beautiful panoramic views of the old city.
10. Take a break and use the brand new panoramic elevator to reach the old city and the city park, occupying the grounds of the former city walls.
11. Admire the beautifully renovated Villa Vauban.
12. Finally, cross the new hanging bridge below the Pont Adolphe (the "New Bridge") before returning to the starting point.

MBOURG CITY

By Pierre Beissel
Partner, Arendt & Medernach

Whether you live in Luxembourg or visit it regularly, you have the chance to see many of the city's landmarks, try different viewpoints and enjoy the details of your favourite places. However, if by any chance you are able to jog around Luxembourg City, your experience is considerably enhanced. Not only do you get to know in detail if your path is sloping up or down, you also notice other details that would otherwise skip the distracted eye.

We asked Pierre Beissel, sportsman and a partner at Arendt & Medernach, to help us appreciate the city by way of following his preferred city track. This is his recommended route:

HOTELS

Which are your three preferred hotels to host clients in Luxembourg?

Recommended by Nigel Williams, Chairman of Royalton Partners
Given the location of our offices, right in the city centre, our preference is for:

- Le Place d'Armes
- Le Royal
- Sofitel Luxembourg Le Grand Ducal

Junior analysts stay at Grand Hôtel Cravat, which remains very central but is more affordable.

RESTAURANTS

Which are your three preferred restaurants to have lunch with your clients in Luxembourg?

Recommended by Claus Mansfeldt, Chairman and Managing Director, SwanCap Investment Management S.A.

- Mosconi
- Um Plateau
- Owstellgleis (Hostert) – a short drive from the office

PHOTO GALLERY

Mickael Fischer (RBC) and Jakub jasica (Varde Partners) - New Year's Event 29/01

Paul Junck (LPEA), Jérôme Wittamer (LPEA/ Expon Capital) - New Year's Event 29/01

Stephanie Apicella and Benoit Dheur (BGL BNP Paribas) - New Year's Event 29/01

Hana Balajkova (Aztec) and Karl Heinz Horrer (EQT) - New Year's Event 29/01

Nathalie Chemtob (Pomery Capital) and Anne Canel (HLD Europe) - LPEA Roadshow in Paris 20/09/2017

Jean-Christian Six (Allen & Overy), Oliver Pritchard (17 Capital), Andreas Fuchs (Quilvest Private Equity) and Jérôme Wittamer (Expon Capital) - LPEA Roadshow in London 26/10/2017

LUXTRAM INCREASES COMMUTING OPTIONS

© Henri Goergen

The much-awaited tramway has finally started operating in Luxembourg. Since December 2017 passengers can use the Luxtram in Kirchberg, from the stop in Luxexpo to the stop at the Red Bridge. Construction continues: in 2019, the tram will connect the Kirchberg quarter with the city centre and the central train station. In 2021, the tram will connect the airport, Kirchberg, the city centre, the central train station and Gasperich/Cloche d'Or. The intention is to operate a multi-modal line – passengers will be able to combine various means of transport: parking the car in a Park&Ride, taking the bus or tram, arriving by plane, hopping on the tram and taking the train. The increased connectivity is hoped to decrease rush-hour traffic for a growing population.

UPCOMING EVENTS

PRIVATE EQUITY

PRE-INSIGHTS: ICOS
Luxembourg
19 February

LPEA BREAKFAST CONFERENCE
Munich
8 March

PRE-INSIGHTS: IMPACT INVESTMENT
Luxembourg
21 March

LUXEMBOURG PRIVATE EQUITY PANEL
In the context of ALFI's London Cocktail and Conference
London
2-3 May

LPEA AGM
Luxembourg
7 May

US ROADSHOW
New York and Boston
16-17 May

0100 CONFERENCES
Luxembourg
27 June

LPEA INSIGHTS 2018
Luxembourg
25 April

Luxembourg will welcome the second edition of the LPEA Insights, Luxembourg's leading private equity and venture capital conference. This half-day event will focus on the contribution of private equity to the economy and will bring on stage case studies that demonstrate the sector's impact in the overall society. With an agenda composed of GPs, LPs and entrepreneurs, one can expect first-hand testimonials and compelling perspectives that extend further beyond Luxembourg.
With 330 participants in 2017, the majority coming from the asset management community, LPEA Insights is the best setting to meet fellow GPs and LPs, as well as other asset managers exploring their way into the asset class.
On top of the main conference, LPEA will host two "pre-Insights" lunch meetings focusing on Initial Coin Offerings (ICOs) and Impact Investment.

OTHER EVENTS IN LUXEMBOURG

Luxembourg City Film Festival
22 February – 4 March

Le Lac des Cygnes
3 March
Rockhal

Sir Simon Rattle & London Symphony Orchestra
23-24 April
Philharmonie

ING Night Marathon
12 May
Luxembourg City

Manhattan: the American Dream
18 May
Philharmonie

Shakira - El Dorado World Tour
19 June
Rockhal

Bryan Adams
24 June
Rockhal

Siren's Call – Music & Culture Festival
30 June
Luxembourg City

Medieval Festival
28 July
Vianden Castle

e-Lake Festival
10-12 August
Echternach Lake

Elevate your Private Equity operational excellence

Luxembourg is the preferred destination for Private Equity fund managers to set up their fund structure, due to its **unique** and **flexible** fund structuring environment. However, have you considered the operational strategy in the face of steady growth, changing regulatory and tax environment?

Our experts at PwC Luxembourg can help you understand and navigate through the complex issues and challenges that fund managers face on a daily basis. We help identifying the right **tailored solutions** to your pressing needs, so that you may achieve the desired operational excellence.

With over 250 experts that make up the multilingual Private Equity team, unmatched market share and size, and an integrated global network of 157 countries, we offer you **unique insights**, **industry leading practices** and **informed perspectives**.

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ABOUT LPEA

The Luxembourg Private Equity and Venture Capital Association (LPEA) is the representative body of private equity and venture capital professionals in Luxembourg.
With over 160 members, LPEA plays a leading role in the discussion and development of the investment framework and actively promotes the industry beyond the country's borders.
Luxembourg disposes of a stable tax regime and is today at the forefront of international PE regulation providing a flexible, secure, predictable and multi-lingual jurisdiction to operate in.
LPEA provides a dynamic and interactive platform for its members to discuss and exchange information and organises working meetings and networking opportunities on a regular basis.
If Luxembourg is your location of choice for private equity, LPEA is where you actually join the industry!

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Luís Galveias Marketing & Communication Manager
Dušan Gladović Legal & Regulatory Manager
Kheira Mahmoudi Executive Assistant to the Managing Director

ALLEN & OVERY

crypto challenge

In partnership with

the LHoFT
Luxembourg House of Financial Technology

SILICON LUXEMBOURG
The Startup Magazine

Cryptocurrencies, tokens and distributed ledgers...
Do these terms seem increasingly familiar to you, but you haven't quite managed to get your head around them yet?

Are you a young mind working in the legal profession or financial sector, a techy start up leader or an entrepreneur? Then stay tuned for the first Crypto Challenge!

#SaveTheDate #13March2018 #Luxembourg
@AllenOvery_LU @LHoFT @SiliconLux #crptchllng

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