CHAPTER IV

SUPERVISORY FRAMEWORK FOR SICARS

1. Legal framework
2. Prudential supervisory practice

SUPERVISORY FRAMEWORK FOR SICARS

As at 31 December 2004, three SICARs are registered on the CSSF's official list of investment companies in risk capital, namely:

- Naxos Capital Partners S.C.A.
- Amber Trust II S.C.A.
- MediaWin I S.C.A..

Ten application files were being processed at the end of 2004.

1. LEGAL FRAMEWORK

The coming into force of the law relating to investment companies in risk capital (SICARs) on 15 June 2004 provided the Luxembourg financial centre with an investment vehicle complementary to undertakings for collective investment.

Consistent with the communication of the European Commission published in 1998 and the conclusions drawn by the European Council of Lisbon in March 2000, the Luxembourg government has indeed decided to set up a legal framework for a new type of investment firm specialised in risk capital whose securities are reserved to well-informed investors.

The purpose of the law relating to the investment company in risk capital is to promote the pooling within a specialised vehicle of what is known as "Venture Capital" or "Private Equity". "Venture Capital" generally refers to the capital provided to start-ups or business sectors with high development potential. "Private Equity" is widely defined as any investment in a private non-listed company.

The elements that these types of investments have in common are to knowingly engage in a risk transaction, the expectation of sizeable yield, the lack of liquidity of the subscribed securities and a relatively long maturity before payment of the first dividends or redemptions.

The law lays down a flexible framework allowing well-informed investors wishing to invest in risk capital to opt for a prudential supervisory regime which is less strict than that applicable to UCIs. This product is therefore restricted to investors who are informed and aware of the risks inherent in the investments. The illiquid character of investments in a SICAR is often accompanied by the fact that the investor is unable to request the redemption of his shares.

Under article 2 of the law of 15 June 2004, a "well-informed investor" refers to any institutional investor, professional investor or other investor who confirmed in writing his status as a well-informed investor, and who either invests a minimum of EUR 125,000 in the company, or has obtained certification from a credit institution, another professional of the financial sector subject to rules of conduct under Article II of Directive 93/22/EEC, or from a management company under Directive 2001/107/EC, certifying his expertise, experience and knowledge allowing him to adequately assess an investment in risk capital.

To perform their activities, SICARs must dispose of a prior licence from the CSSF. The administrative procedure to authorise a SICAR is very much in line with that applicable to undertakings for collective investment and pension funds.

Like UCIs and pension funds, SICARs are subject to the "visa" procedure at the time of authorisation, and subsequently in case of amendments. This procedure is not only intended for internal CSSF identification purposes, but also purports to facilitate the admission of the SICAR's shares to trading on a stock exchange or on a regulated market, in accordance with article 13(3) of the law of 15 June 2004.

The CSSF carries out a “light” prudential supervision of SICARs. Indeed, it does not authorise the promoters and asset managers of SICARs, nor does it impose requirements regarding the latters’ financial standing or status. The CSSF solely assesses the acceptability of the depositary bank, the central administration, the managers, as well as the compliance of the SICAR’s constitutive documents with the legal provisions.

2. PRUDENTIAL SUPERVISORY PRACTICE

Article 1 of the law of 15 June 2004 on the investment company in risk capital specifies that investment in **risk capital** refers to the capital provided directly or indirectly to entities in view of their launch, development or listing on a stock exchange. As the law does not precisely define the term “risk capital”, compliance of planned investments with the spirit of the law of 15 June 2004 will be verified on a case-by-case basis. The CSSF adopts a flexible approach in this context in accordance with the spirit of the law.

Several decisions have been made as regards eligible investments for a SICAR in particular cases submitted to the CSSF.

Professionals perceive the investment company in risk capital as an efficient means to invest in certain segments of the **real estate sector**. The CSSF accepts such investments for a SICAR on the condition that they are considered as risk capital and are indirectly made through real estate companies. Whether the capital qualifies as risk capital depends on the type of investment and its expected yield. So-called opportunistic investment strategies are acceptable in principle, while core-plus investments will be analysed on a case-by-case basis. Core investments are not eligible in principle.

The CSSF allows a SICAR to invest in units or shares of other **undertakings for collective investment** as long as the latter have themselves adopted a venture capital/private equity investment strategy.

A SICAR is allowed to invest in **listed securities** if such an investment pursues a defined project aiming to generate added value within a target company, i.e. via the development of its activities. A SICAR is allowed to invest in listed securities that do not represent risk capital and hold liquid assets and other similar investments only on a temporary basis, while waiting to invest in risk capital.

As far as the conditions applying to the **directors of a SICAR** are concerned, article 12(3) of the law of 15 June 2004 specifies that the directors of the SICAR and of the depositary must be of sufficiently good repute and have sufficient experience to perform their duties. To that end, their identity must be notified to the CSSF. “Directors” shall mean, in the case of limited partnerships, the general partners and in the case of public limited companies and limited companies, the members of the board of directors and the manager(s), respectively. As regards partnerships limited by shares, “directors” shall mean the general partner. Thus, the members of the board of directors of the general partner are considered as directors of the SICAR. Where the general partner does not have a board of directors, these conditions must be fulfilled by the manager in charge of administrating the general partner. Where the manager is a legal person having the status of professional of the financial sector subject to a supervisory authority that performs an equivalent prudential supervision, the CSSF could accept this person as director of a SICAR.