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Luxembourg is now home to nearly 250 alternative investment fund managers and 600 registered managers, making it one of the largest private equity fund domiciles in the world. Vistra's Joost Knabben reflects on how the jurisdiction's fund offer has evolved and what the future holds for the Grand Duchy.

Luxembourg was originally best-known for its UCITS regime but has done a huge amount of work to build up its investment fund structures. What does Luxembourg offer GPs now and how has it evolved to meet their needs?

Luxembourg has always been a jurisdiction with a strong UCITS brand. With the implementation of AIFMD, Luxembourg tried and succeeded to achieve a similar result in the alternative investment space.

Indeed, Luxembourg now has a very complete toolkit available for alternative investment funds.

The process started with the introduction in 2004 of Investment Company in Risk Capital (SICAR), and the Specialised Investment Fund (SIF) in 2007.

Managers want a fund regime that is flexible and responsive. Luxembourg has worked hard to deliver that by creating (for example) the Special Limited Partnership (SLP) which was developed in 2013 to provide partnership structures that these managers were familiar with.

Following the introduction of the SLP, there was a significant increase in interest in Luxembourg from managers across the alternative assets space – including real estate, private equity and infrastructure.

The more recent introduction of the Reserved Alternative Investment Fund (RAIF) has added to Luxembourg's suite of resources in providing an additional supervised vehicle -requiring the appointment of an AIFM- with quick time to market capacity and more flexibility in corporate forms.

One of the advantages of the RAIF is that it regulates the alternative investment fund manager (AIFM) rather than the fund. Are fund managers (as opposed to AIFMs) happy to set themselves up as AIFMs to speed up the time to market for their funds?

It all depends on the size of the assets under management that the fund manager has. A manager running multiple funds would potentially set up its own AIFM subject to a cost analysis and its existing set-up, resources and outsourcing policy. The system is flexible and no particular requirement applies. There are third-party AIFMs which perform risk and portfolio management tasks for AIFs delegating investment advice back to the fund managers.

At Vistra, for example, we are authorised to act as AIFM to private equity, real estate, infrastructure and private debt AIFs. This is a solution that can work for a fund manager that is focused on any market and wants to distribute to professional investors throughout the EEA. This could also apply to small fund managers that do not have the resources to go through the AIFM registration process. By appointing a third party AIFM, one can benefit from AIFM compliant expertise, already set processes, track record and infrastructure to reach EEA professional investors quickly.

The Grand Duchy's fund regime has evolved rapidly. Looking back, what do you think were the reasons for this and why do you think Luxembourg has been able to move so quickly?

Luxembourg is a small jurisdiction and the financial sector is very important to its economy. The regulator takes the time to meet with GPs and advisers and listens to what they have to say and what they need. The regulator and the Luxembourg Government benefit from the expertise of practitioners leveraging concrete feedback from the industry.

The development of the investment fund offering was sparked by the acknowledgement of advisers, the regulator and the Government that Luxembourg had a great potential to further strengthen its funds industry.

This led to a speedy implementation of AIFMD into Luxembourg law and the creation of the toolkit that was mentioned above.

Aside from the introduction of the SLP and RAIF, have there been any other drivers behind the growth of the investment funds industry in Luxembourg?

Brexit has been a big driver. For any UK manager looking at an alternative to their current arrangements post-Brexit, Luxembourg is the obvious jurisdiction to consider. The OECD's Base Erosion and Profit Shifting (BEPS) initiative has also been a factor. We have observed fund managers having existing investment structures in scattered jurisdictions consolidating in Luxembourg to aggregate their investments in one domicile of choice. In this context we have seen managers structuring their affairs in Luxembourg, with an AIFM and a fund above an existing investment structure allowing them to show a clear business rationale, mitigate risk and create adequate substance complying with BEPS requirements.

Finally, I would also point out that the private equity industry as a whole has gone through an incredible period of growth. There are more managers in the market and more funds to be administered. That has obviously also contributed to the growth of the funds business in Luxembourg.

On the Brexit point, how are managers reacting? Have GPs already moved their investment management teams across to Luxembourg or are they taking a wait-and-see approach?

We have seen some managers make the move. As I mentioned earlier, I think there are managers who looked at Brexit and BEPS and decided to relocate or first build up their back office team to Luxembourg and are now looking at moving their deal teams because it enabled them to remove any Brexit uncertainty and deal with BEPS at the same time.

Of course, there are a number of managers who did not want to be first movers and decided to wait and see what comes out of Brexit before making a decision. What we hear more is UK managers putting contingency plans in place, where they can push the button and make the move if they need to in case of a hard Brexit. There are a number of new office buildings going up in Luxembourg where some fund managers have reserved space.

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