

The SICAR



CORPORATE FLEXIBILITY

The “*Société d’investissement en capital à risque*” (“**SICAR**”) has been implemented by a law dated 15 June 2004 (the “**SICAR Law**”) in order to offer a new regulated vehicle for investment in private equity to well-informed investors¹ (the “**Investors**”) in addition to the other investment vehicles already at their disposal. These other vehicles include the Undertakings for Collective Investment type vehicles (the “**UCI**”) and the SOPARFI type companies (non-regulated commercial companies) investing in private equity. It offers the advantages of a considerably flexible corporate structure for the sole purpose of investing in risk capital while simultaneously offering the benefits of the supervision of the Commission de Surveillance du Secteur Financier (the “**CSSF**”) as well as a neutral tax regime.

In the event that the option to use the SICAR structure to invest in risk capital be chosen, it shall be expressly stated by the Investor(s) in the articles of association of the SICAR, which shall be incorporated under the form of one of the following Luxembourg commercial companies: (i) *société en commandite simple* (limited partnership), (ii) *société en commandite par actions* (partnership limited by shares), (iii) *société coopérative organisée sous forme de société anonyme* (cooperative in the form of a public limited company), (iv) *société à responsabilité limitée* (limited company) or (v) *société anonyme* (public limited company).

The general corporate law of 10 August 1915, which applies to the above corporate structure, is applicable to the SICAR, however the derogations permissible are significantly wide and the SICAR has substantial leeway in deciphering what rules will be included in its articles of association. This places its obligations on a more contractual level than a mandatory one.

The share capital of the SICAR must be at least EUR 1 million, which has to be subscribed for within one year of incorporation². The SICAR Law provides for the possibility to opt for a variable capital³ (in such a case the capital shall at all times be equal to the net asset value of the SICAR)⁴. SICAR Law does not require the creation of a legal reserve.

The issuance of new shares by the SICAR and the payment and distribution of dividends shall also be regulated by the rules outlined in the articles of association of the SICAR; these derogations allow the SICAR to exercise a considerable amount of flexibility in this regard.

Moreover, the valuation of the assets of the SICAR shall be based on a good faith estimation, which estimation shall be guided by the procedure expressed in the articles of association of the SICAR⁵.

The central administration⁶ and registered office of the SICAR must be located in Luxembourg.

¹ i.e. (1) institutional investor, (2) professional investor or (3) any other investor who meets the following conditions: confirmation in writing that they adhere to the status of a “well informed investor”, and (i) investment of a minimum of EUR 125,000 or (ii) certification of another professional of the financial sector, verifying his/her experience and knowledge in risk investment.

² The share capital of a (i) *société en commandite par actions*, (ii) *société coopérative organisée sous forme de société anonyme*, (iii) *société à responsabilité limitée* or (iv) *société anonyme* must be fully subscribed for and paid up at least up to an amount of 5% of the capital.

³ Apart from the *société en commandite simple*.

⁴ The amendments to the share capital can therefore occur automatically without formalities. This significant flexibility means that an authorised share capital could be provided for in a SICAR incorporated under the form of a *société à responsabilité limitée*.

⁵ For instance, the guidelines of EVCA (European Venture Capital Association) may be followed.

⁶ This notion is more flexible than for an UCI, the entity entrusted with the central administration does not need to be a professional of the financial sector in the meaning of the law of 5 April 1993 on the financial sector as amended. The CSSF, on a case by case basis, may allow such central administration to delegate specific tasks to some entities located in foreign countries.

NOTION OF RISK CAPITAL

It is important to note that the diversification of investments, as is the case for instance for the UCI, is not a requisite for SICAR. In addition it is foreseen that a parliamentary bill will soon be introduced to allow the possibility for the SICAR to compartmentalize its risks⁷, which is not possible currently.

Article 1(2) of SICAR Law defines the investment in risk capital as “*the direct or indirect contribution of assets to entities in view of their launch, their development or their listing on the stock exchange*” (the “**Risk Capital**”).

In order to clarify the meaning of Risk Capital for the purposes of satisfying the CSSF, the latter has issued a circular on 5 April 2006 (the “**Circular**”).

The Circular states that Risk Capital can be characterized as the simultaneous combination of two principal elements, which are the existence of (i) a high-risk business and (ii) a desire to develop it, i.e. creation of wealth at the level of the target companies. These two elements are notably present in venture capital type investments⁸.

The “development” element may be characterized as including for instance (i) the initial injection of capital in order to launch the business of the target company or to aid its listing on a stock exchange and/or (ii) the intervention⁹ of the SICAR in the management of the targeted companies with the aim of allocating the resources in a more efficient manner.

This element also requires that the investment(s) be made for a certain period of time¹⁰ as well as there being an intention of selling it down the line in order to make a profit¹¹. This can be contrasted with a holding company, which acquires shares with the intention of holding them for an indefinite period.

The element of “high risk investment” denotes the aim of obtaining a high return upon sale of an investment, which is not liquid per se. The Circular also states that high risk involves the appraisal of a number of factors including the number and nature of the target companies, their degree of maturity, etc.

In principle the types of financing available to the SICAR are open ended. It can range from contribution to the share capital, to bridge finance, to mezzanine loans, to convertible loans or essentially any form that relates to risk capital¹².

Although the law on SICAR does not permit the direct investment in real estate property, it can do so indirectly where such investment fulfils the criteria as is required for all the investments of the SICAR, i.e. (i) an aim to develop¹³, (ii) a particular risk¹⁴ and (iii) an aim to purchase in order to resell with a capital gain.

⁷ It is possible for the UCI.

⁸ Such as start up and early stage investments.

⁹ e.g. advising or presence in the management of the target companies; this criteria is important in the case of an investment in one target company.

¹⁰ The duration of the investment is an important criteria for the CSSF. The SICAR are therefore generally closed ended funds.

¹¹ How the SICAR disinvests is not specified in the SICAR law; this is left at the discretion of the SICAR management.

¹² The circular also states that the law permits notably (i) indirect investment (e.g. through UCI, real estate funds) in shares that represent risk capital without imposing the SICAR type restrictions on these intermediary companies and (ii) investments in quoted securities fulfilling some conditions characterizing both a “high risk” and “development”.

¹³ This can be achieved by some changes in the existing conditions e.g. renovation, change of tenants, etc.

¹⁴ Demonstration of a risk superior to the normal risk linked to a defined real estate market. The fact that the real estate property be located in a country with a certain political risk is not in itself sufficient to characterize the high risk.

SUPERVISION OF THE SICAR

The SICAR offers the assurance for its Investors of the supervision of the CSSF, which supervision is at the same time lighter than for other regulated investment funds because of the qualification of the SICAR Investors. In their supervisory role, the CSSF shall approve (i) the persons composing the management organs of the SICAR¹⁵, whom must evidence a strong experience in private equity, (ii) the incorporation documents (e.g. prospectus¹⁶ and articles of incorporation) in order to ensure notably that they comply with the risk capital requirements and (iii) the custodian with which the assets of the SICAR shall be deposited¹⁷.

The SICAR Law through the obligation to prepare and publish annual accounts also provides for regular monitoring¹⁸ and requires that the prospectus be updated when the SICAR issues additional shares. An independent auditor shall be appointed notably to audit these annual accounts and to report to the CSSF any contraventions of the SICAR Law, should the case arise.

As previously stated, in addition to the corporate flexibility of the SICAR and the benefits of the supervision of the CSSF, one of the prime advantages of the SICAR is its neutral tax status.

NEUTRAL TAX STATUS

At the level of the SICAR, the status of tax payable depends on the legal form chosen.

In the case of *société en commandite simple*, the principle is transparency and therefore the taxation fundamentally rests at the level of the Investor¹⁹. Double tax treaties are applicable in both the country of the Investor and the country of the target company, essentially allowing the avoidance of double taxation at the level of the Investor.

Other SICAR companies, which are non-transparent, are therefore fully taxable (29,63%) and should in principle benefit from tax treaties (Luxembourg treaties) and EU participation exemption directives. In principle, the following are income exempted at the level of the SICAR: (i) capital gains resulting from transferable securities, (ii) income gains deriving from transferable securities and (iii) income arising from funds held pending their investment in risk capital subject to certain conditions²⁰.

For all types of SICAR, the capital duty is fixed at EUR 1,250²¹. There is a fixed annual fee of EUR 1,500 payable to the CSSF and a registration fee of EUR 1,500. SICAR are not liable for wealth tax or subscription tax. SICAR cannot apply for tax consolidation with other European subsidiaries.

In principle, there is no taxation in Luxembourg on the disposal of an interest in SICAR by non-resident Investors. Withholding tax on distributions does not apply for SICAR²².

¹⁵ Contrary to what is required for the UCI, the promoter of the SICAR does not need to be approved by the CSSF.

¹⁶ In the event that a SICAR may wish to make a "public" offer, as defined in the law of 10 July 2005 with respect to the prospectus for securities, the prospectus shall comply with the provisions of this law unless it qualifies for any stated exemptions.

¹⁷ The custodian shall have its registered office in Luxembourg or at least shall be established in Luxembourg if its registered office is elsewhere. This custodian must be a recognized credit institution in accordance with the meaning of the law of 5 April 1993 on the supervision of the financial sector, as amended. Its duties include notably the holding of assets and monitoring the receipt of the subscription price and the consideration paid for assets etc.

¹⁸ SICAR is not obliged to prepare consolidated accounts however it is obliged to provide the Investors with the annual accounts at least twice a year upon their request.

¹⁹ As a consequence, there is also no corporation or municipal business tax in Luxembourg.

²⁰ Only applies to the period of twelve months before the investment in risk capital and the investment must be such as to satisfy the definition of risk capital under the law.

²¹ There is no other subscription tax.

²² Without prejudice to the taxation of such income in the country of the Investor as the case may be.

This tax status is currently subject to some debate over whether this system could be qualified as “state aid” and hence potentially in breach of European Law but the Luxembourg government has firmly denied any such contentions.

OVERVIEW OF THE EXISTING SICARS

FORM OF LEGAL ENTITY*	NUMBER
Société en Commandite Simple [Limited Partnership]	1
Société en Commandite par Actions [Partnership Limited by Shares]	30
Société Coopérative Organisée sous forme de Société Anonyme [Cooperative in the form of a Public Limited Company]	0
Société à Responsabilité Limitée [Limited Company]	16
Société Anonyme [Public Limited Company]	23
TOTAL	70
TYPE OF INVESTMENT POLICY**	
Private Equity	18
Venture Capital	12
Private Equity + Venture Capital	16
Private Equity + Venture Capital + Mezzanine	1
TOTAL	47
TYPE OF INVESTMENT STRATEGY**	
Buy, Build and Sell (B.B.S)	29
Buyout Instruments	9
Mezzanine Instruments	6
Risk Capital Funds (RCF)	4
TOTAL	48
SECTOR OF INVESTMENT**	
Every Sector	22
Energy	3
IT / Communication	7
Sciences	1
Microfinance	1
Real Estate	10
Financial Sector	3
TOTAL	47
COUNTRY OF INVESTOR**	
United States	11
France	6
Great-Britain	6
Switzerland	6
Luxembourg	5
Italy	3
Belgium	2
Egypt	2
Others	6
TOTAL	47

* As of 7 July 2006

** As of 31 December 2005

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