

The European Venture Capital Fund Regulations

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Introduction

Amidst all of the discussions, publications and anxieties regarding EU Directive 2011/61/EU on Alternative Investment Fund Managers (“**AIFMD**”) and its implications for both EU and Non-EU AIFMs, it can sometimes be overlooked that, on the same date that AIFMD goes live, July 22, 2013, a somewhat related EU regime for EU venture capital funds also comes into force under EU Regulation 345/2013 on European Venture Capital Funds (the “**EuVECA Regulation**”).

The EU Commission wants to strengthen venture capital financing in order to fully realise the commercial potential of European Small and Medium Enterprises (“**SMEs**”). The introduction of a uniform EU framework for European Venture Capital Funds (“**EuVECAs**”) is designed to provide an additional financing tool for SMEs, a sector that is key to Europe’s future economic success.

This regime is of note because it allows EU registered AIFMs manage certain types of qualifying venture capital funds domiciled in the EU, known as EuVECAs, and to market those EuVECAs to professional (and certain other) investors throughout the European Union.

This represents, in effect, a relaxation of the AIFMD rule that a registered AIFM cannot benefit from any of the rights under AIFMD (e.g. right to manage or market cross-border).

As a result a registered AIFM can manage an EuVECA domiciled anywhere in the EU and can market it anywhere in the EU to professional (and certain other) investors. The Regulation does not extend to Non-EU AIFMs nor to Non-EU funds.

The EuVECA Regulation will be directly applicable from July 22, 2013.

Asset Management and Investment Funds Group

Dillon Eustace

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Who does the EuVECA Regulation apply to?

In summary, they apply to sub-threshold (i.e. registered) AIFM who meet the following criteria:

- (i) manage portfolios of EuVECAs;
- (ii) are established in the EU;
- (iii) whose assets under management in total do not exceed the threshold referred to in point (b) of Article 3(2) of AIFMD (i.e. a total AUM of less than EUR 500million comprised of closed ended and unleveraged funds); and
- (iv) are registered with the competent authorities of their home Member State in accordance with point (a) of Article 3(3) of AIFMD.;

For more information AIFMD, please refer to Dillon Eustace's "Guide to AIFMD", which can be found [here](#).

When does the EuVECA Regulation apply?

The Regulations come into force on July 22, 2013.

Key Concepts

What is an EuVECA?

An EuVECA is a fund that:

- (i) is a collective investment undertaking;
- (ii) intends to invest at least 70% of its aggregate capital contributions and uncalled committed capital in assets that are qualifying investments;
- (iii) does not use more than 30% of its aggregate capital contributions and uncalled committed capital to acquire non-qualifying investments; and

- (iv) is established in the European Union;

A "*collective investment undertaking*" means an AIF as defined in point (a) of Article 4(1) of AIFMD i.e. a fund which (i) raises capital from a number of investors, with a view to investing it in accordance with a defined investment policy for the benefit of those investors; and (ii) does not require authorisation under the UCITS Directive;

"*Qualifying investments*" are equity, or quasi-equity instruments; secured or unsecured loans granted by the qualifying venture capital fund to a qualifying portfolio undertaking; shares of a qualifying portfolio undertaking; and units or shares in other qualifying venture capital funds, provided (in each case) that certain tests are met; and

"*Qualifying portfolio undertaking*" means an undertaking that:

- (i) is not admitted to trading on a regulated market or multilateral trading facility;
- (ii) employs less than 250 people;
- (iii) has an annual turnover not exceeding €50 million, or an annual balance sheet total not exceeding €43 million;
- (iv) is not a collective investment undertaking, a credit institution, an investment firm or an insurer, and
- (v) is established within the territory of a Member State, or in a third country provided that the third country:
 - is not listed as a Non-Cooperative Country and Territory by the Financial Action Task Force on Anti-Money Laundering and Terrorist Financing,
 - has signed an agreement with the home Member State of the manager of a qualifying venture capital fund and with each other Member State in which the units or shares of the qualifying venture capital fund are intended to be marketed to ensure that the third country fully complies with the standards laid down in Article 26 of the OECD Model Tax Convention on Income and on Capital and ensures an effective exchange of information in tax matters, including any multilateral tax agreements;

Who is or can be the manager of an EuVECA?

The Regulations provide that the manager can manage portfolios of EuVECAs whose assets under management, in total do not exceed the threshold referred to in point (b) of Article 3(2) of AIFMD (i.e. a total AUM of less than EUR 500million comprised of closed ended and unleveraged funds)

Registered managers of EuVECAs are subject to a lighter regulatory regime than AIFM with a full authorisation under AIFMD. Once they comply with the AIFMD requirements in relation to organisational requirements, liquidity management, valuation, certain of the transparency obligations and certain of the requirements set out in the European Commission's Delegated Regulation (EU) 231/2013 (the "**Level 2 Regulation**"), they will be able to benefit from the marketing passport offered by the EuVECA Regulation.

For more information on the requirements applicable to registered managers, please refer to Dillon Eustace's "Guide to AIFMD", which can be found [here](#).

The EuVECA Regulation provides that the manager shall be either:

- an external manager, which is the legal person appointed by the EuVECA or on behalf of the EuVECA and which, through this appointment, is responsible for managing the EuVECA (external AIFM); or
- the EuVECA itself, which shall then be registered as manager, where the legal form of the EuVECA permits an internal management and where the AIF's governing body chooses not to appoint an external manager.

An internally managed EuVECA cannot be appointed as the external manager or another EuVECA.

Who can invest?

EuVECAs may only be marketed to investors who have the experience, knowledge and expertise to make their own investment decisions and properly assess the risks associated with such investments.

Therefore EuVECAs may only be sold to investors who:

- (i) are **or elect to be treated as** professional clients;

- (ii) are willing to invest at least €100,000: and
- (iii) have confirmed in writing that they are aware of the risks associated with their investment;

These restrictions do not apply to investments made by executives, directors or employees involved in the management of a manager of an EuVECA when they are investing in an EuVECA that they manage.

A “professional investor” is any investor which is considered to be a professional client or may be treated as a professional client on request within the meaning of Annex II of Directive 2004/39/EC. A list of investors categorised as professional investors can be found in Dillon Eustace’s “Guide to AIFMD”, which can be found [here](#).

Limited use of Leverage

In order to ensure that EuVECA do not contribute to the development of systemic risks, and that such funds concentrate, in their investment activities, on supporting qualifying portfolio undertakings, the use of leverage at the level of the fund is limited.

Managers of EuVECA may not:

- (i) leverage the EuVECA using any method by which the exposure of the fund will be increased beyond the level of its committed capital, whether through borrowing of cash or securities, the engagement into derivative positions or by any other means.
- (ii) borrow, issue debt obligations or provide guarantees at the level of EuVECA where such borrowings, debt obligations or guarantees are covered by uncalled commitments.

Conduct of business rules

Managers of EuVECA must meet the following criteria in relation to the conduct of business and the relationship of those managers with their investors. They must:

- (i) act honestly, fairly and with due skill, care and diligence;

- (ii) have appropriate systems and controls in place to prevent malpractice that can reasonably be expected to affect the interests of investors;
- (iii) conduct their business activities in a way that promotes the best interests of the funds they manage, their investors and the integrity of the market;
- (iv) have adequate knowledge and understanding of the undertakings in which they invest;
- (v) treat their investors fairly;
- (vi) ensure that no investor obtains preferential treatment, unless that treatment is disclosed in the rules or instruments of incorporation of the fund;
- (vii) not delegate functions to third parties to such an extent that it becomes a mere "letter-box" entity;
- (viii) identify and, wherever possible, avoid conflicts of interest. Where this is not possible, the manager must manage, monitor and disclose conflicts of interest appropriately to prevent them adversely affecting the fund and investors' interests;
- (ix) have sufficient own funds, and use adequate and appropriate technical and human resources as necessary for the proper management of the funds it manages; and
- (x) give their regulators and investors prescribed information at regular intervals.

Is registration obligatory and what are the benefits of registration as manager of an EuVECA?

If a manager and its funds are registered the manager will be entitled to use the 'EuVECA' label for its EuVECAs. This label will entitle the manager to sell such funds across the EU by way of a marketing passport, thereby avoiding the 'patchwork of uncertainty' of private placement regimes across the EU.

Registration as manager of an EuVECA is an entitlement but is not an obligation. If you are a sub-threshold manager, marketing your funds in the EU and the investment policy of your funds is compatible with the requirements of the EuVECA Regulation then you will be missing out on an opportunity to greatly simplify the distribution of your funds while also

remaining subject to the registration criteria under AIFMD. For more information on registration and AIFMD, please refer to Dillon Eustace's "Guide to AIFMD", which can be found [here](#).

Overall assessment of the practicalities of registration as manager of an EuVECA?

If a manager manages funds that invest in qualifying portfolio undertakings (as defined in the EuVECA Regulation) and meets the requirement of Article 3(2) of AIFMD (i.e. a total AUM of less than EUR 500million comprised of closed ended and unleveraged funds), then the opportunity to avail of a marketing passport will be very attractive as it will not add appreciably to the light touch regulatory burden already imposed on that manager, who would in any case, be a registered manager under AIFMD.

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