

New partnership

A new limited partnership for private equity and hedge funds

A special form of limited partnership, designed for collective investments in the alternative investment area, has been introduced into Swiss law. The revised Act on Collective Investment Schemes (the CISA) came into force on January 1.

The limited partnership already existed under ordinary company law, the Swiss Code of Obligations. But the ordinary LP (in German *Kommanditgesellschaft* and in French *société en commandites*) could not have a company with limited liability as its general partner. And the ordinary LP lacked the fiscal transparency that is typically present in most limited partnership jurisdictions.

The CISA has now removed these two obstacles, but for a price and with a clearly defined scope. The price is regulation by the Swiss Banking Commission. And the scope of the new limited partnership is limited to collective investments by qualified investors in alternative investments, that is, private equity, hedge funds and real estate projects, including fund-of-funds structures for these investment categories.

Fiscal transparency is a big step forward for investors and the industry. Managers and promoters might view regulation as a disadvantage, but many investors, both institutional and private, welcome the transparency and accountability resulting from the regulation.

The Swiss Private Equity & Corporate Finance Association (SECA) is drafting the model documentation and reconciling it with the Swiss Banking Commission to ensure a smooth application procedure.

Features

The new limited partnership is largely based on the ordinary Swiss limited partnership. The CISA modifies the Swiss Code of Obligations to create a special type of limited partnership: the collective investment limited partnership (the CILP).

As in most jurisdictions, the CILP is not a legal entity but, formed on the basis of an agreement, is a limited partnership agreement. The general partner has unlimited liability for the obligations of the partnership and is responsible for the management. But contrary to the ordinary (Swiss) limited partnership, the general

partner must be a corporation (the GP company) with a minimal capital of SFr100,000 (\$82,250).

The limited partners (in this context the investors) have a clearly established limited liability (registered for each CILP in the Register of Commerce) and do not have the right or the duty to manage the partnership. Only qualified investors may be limited partners. The term comprises institutional investors and high-net-worth individuals.

Regulation

The CILP is subject to regulation and continuous supervision by the Swiss Banking Commission (the SBC). In the admission process, the SBC examines the partnership agreement and the prospectus for compliance with the minimum requirements laid down in the CSIA and its implementing Ordinance. The SBC may dispense with the prospectus requirement. The GP company must prove that it is "fit and proper" to manage the CILP: the reputation and the skills of the managers, the directors and (to some degree) the important shareholders of the GP company need to meet the minimum standards laid down in the Act and the Ordinance. The GP company must also have an adequate organization.

The GP company is subject to a strict duty of loyalty and continuous information to investors and the SBC. The CILP's auditor must be approved by the SBC.

The need for regulation and supervision varies greatly according to the partnership in question. The SBC acknowledges that a small closed-end venture fund with 30 qualified investors and 10 portfolio companies requires less scrutiny than a big fund of funds with several hundred investors and certain open-end features (above all, redemption rights). As mentioned above, the SECA is, together with the Swiss Funds Association, drafting model documentation that is intended to win the approval of the SBC and so simplify and accelerate the admission procedure.

Admission with the SBC (which has signalled repeatedly its flexibility and support regarding the CILP) is expected to take about two months. The admission and legal fees are moderate. The auditor fees depend on the business volume and size of operations.

Tax

For Swiss income tax purposes, the CILP is a transparent non-taxable entity. (If the CILP holds a direct investment in real estate, some modified tax treatment might apply.) Capital, income and gains derived from the LP are taxed directly with the investors, so there is no tax on the distribution of capital gains by the CILP to Swiss individual investors. To ensure this tax treatment, the CILP must observe certain accounting and reporting requirements. Dividend and interest income is taxable but typically of little importance, if any, in a private equity context. Non-resident investors in a CILP are not subject to income, profit, capital or net-wealth tax in Switzerland (unless they hold their investment as part of a fixed business or a permanent establishment in Switzerland).

The issuance of LP interests is exempt from Swiss securities issuance tax and securities transfer tax. The repayment of invested capital is tax exempt anyway.

The GP company's profit is, in principle, subject to the ordinary profit tax (about 18% in the low-tax cantons). Under the existing regime the tax burden may already be considerably reduced depending on the structure. There is strong pressure from various areas of the political spectrum to alleviate the tax burden further not only for the GP company, but also for its managers and owner individuals.

The tax treatment of the CILP will be regulated in more detail in the guidelines of the Federal Tax Administration and the cantonal tax authorities.

The CILP is an attractive option for traditional offshore limited partnerships. It is flexible, has attractive tax features and removes the need to resort to complicated and expensive offshore structures. If the promoter and its team are based in Europe, the new Swiss CILP offers obvious advantages.

The prudential regulation and supervision by the SBC is at first sight a cost and inconvenience factor for the promoter. But so far it has proved a strong selling argument with investors, above all institutional investors, who appreciate that the partnership is based in Switzerland and so is accountable to the SBC and subject to the jurisdiction of the Swiss courts.

The CILP should prove popular with the Swiss and foreign alternative investment industry, above all the many fund-of-funds structures in the private equity and hedge fund areas. Further, the CILP is well positioned to accommodate local Swiss direct private equity and hedge funds.

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