FEATURE:
THE DEMAND FOR NEXT-LEVEL ASSET SERVICING

PRIVATE EQUITY:
RIDING A WAVE OF REGULATORY CHANGE

REAL ESTATE
LIGHTENING THE LOAD FOR REAL ESTATE DEBT MANAGERS
Dear readers,

As we venture into this new decade, I would first of all like to wish you all the very best for 2020. As the new CEO of Alter Domus, my expectations for our organisation are set very high. Based on recent conversations with our clients, I’m coming to find that the same is true for them as well, as we’ve highlighted in this edition of Sensus.

Stepping into this new era brings with it its own unique set of challenges, new ways of thinking, and an increasingly important and technologically advanced role for service providers. Some of you are wondering if technology will eventually replace the customer-client relationship. Others are concerned with keeping up with globalisation in the modern world.

In this edition, we shed some light on our research findings on alternative asset managers’ appetite for outsourcing in the US and the Asia Pacific region. We explore ESG trends in private equity and the continuing allure of private debt in both the US and across Europe. We also review the succession crisis in Japan and its impact on M&A activity in the greater region.

As always, we welcome your feedback and encourage you to share any content ideas or contact us if you would like to collaborate on a future article.

Wishing you all a prosperous 2020.

Doug Hart,
Chief Executive Officer, Alter Domus
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Against a background where demand is driving private equity to peak valuation levels, change is sweeping through the industry and it is a wave of change that fund administrators will need to ride.

Increased professionalism is bringing both challenges and opportunities to third-party service providers. George Rologis, Chief Corporate Development Officer at Alter Domus, says fund administrators will need to up their game for the benefit of the market.

As demand rises for private equity and alternative asset products, in addition to big names pushing for an increased carry structure of 30 percent, demand for our services rises in parallel. In order to provide GPs with the best possible support in a challenging market, our focus is on automation that will enhance the GPs’ ability to report to LPs. Advancing data management systems, recruiting top-flight professionals and developing our relationship with chief financial officers will help enable us to stay on top of a growing and dynamic market.

There is no doubt that the traditional role of a fund administrator is evolving and being shaped not only by additional requirements from LPs and regulators, but also from increasing competition in our industry. We see ourselves more as partners to fund managers with an active, middle-office role to play that allows GPs more time to focus on their value-added skills and portfolio transactions.

The ability to be flexible and to work with clients to deliver a specific solution for a specific situation is a central component of our high-quality service levels. This flexibility includes building a more diverse team with a mix of skills and experiences, providing our clients with extra resources through ‘loaning’ our professionals and offering additional support wherever needed.

**ADAPTING TO THE AIFMD ERA**

Contrary to feelings at the time AIFMD I was introduced, the new legislation, while it did make operational activity more cumbersome, did not result in a slowdown of business. One clear outcome of AIFMD is that our business has become significantly more process-driven with automated data management and reporting facilities smoothing the transition. While demand for both ourselves and our clients did not decrease, AIFMD does appear to have segmented the market, with larger funds better placed to meet the challenges of evolving regulatory demands. And it is possible that AIFMD II will see smaller funds pushed further out of the market leaving predominately mid-sized and larger funds operating in an increasingly regulated investment space.

“Today’s dynamic market suggests that AIFMD has minimal, if any, impact on holding back investor demand. If AIFMD II were to come in at a time when the industry was struggling, then it may drive investors to something else, but I doubt the additional requirements as currently suggested will serve to dampen demand.”

George Rologis, Chief Corporate Development Officer

Transparent is only going in one direction: up. Regardless of what is happening on the regulatory scene, investors have been increasingly focused on this subject in recent years. It does put pressure on fund administrators and it can seem daunting to small and mid-sized investment firms. Yet the servicing industry must find a solution that enables any size of asset manager to operate within the rules. Technology provides solutions and service providers must be prepared to invest in the latest automation and data management systems. We may also see a reshuffling of the cards in what might be called a third phase for the industry. A decade ago, the major players were not necessarily the same names as they are now, and we have seen some big brands fall by the wayside.
As Environmental, Social and Governance investing continues to gain traction, growing public support and a new generation of investors who see ESG as a priority are set to redefine how fund administrators and funds operate in the future. Already, sizeable ESG-related funds are being raised and it increasingly plays a significant role in LPs’ due diligence. It matters to investors, so GPs must show that they take ESG concerns seriously.
SEEKING DEFINITION IN SUBSCRIPTION CREDIT FACILITIES

Subscription credit facilities remain a hotly debated subject with the industry still to offer clear guidelines about how long the facility should be applied. With competing groups of opinions each defending their corner, Tim Ruxton, Managing Director, examines this sometimes contentious issue.

If we start at the beginning and look at the actual purpose of this credit facility, it was designed to bridge a gap to a capital call. By its very nature, this would seem to suggest a short-term loan with a typical term of 90 days, but we’re increasingly seeing terms of six months and beyond with the industry seemingly pulling in two different directions. So, what is going on?

In private equity, there is a clear move towards longer duration credit facilities. However many managers continue to pay off as soon as called capital comes in. We’re even seeing developments where some of the more well-established managers are using credit facilities to fund working capital, expenses and even acquisitions. In these cases, repayment periods can start upwards of 12 months and last a number of years. Private equity houses are using credit facilities for different purposes, which in turn sees them seeking different repayment frameworks. On the other hand, pension funds are keen to maintain short-term repayment credit lines in order to avoid the risk of generating a tax liability or a tax loss they would be unable to claim back. Other fund types favour a credit facility line that lasts throughout the fundraising period. So, competing interests and outlooks, different fund types and the diversity of investors are all making it difficult to find a consensus view.

THE IMPACT ON PERFORMANCE REPORTING

Even with more transparency and understanding, the proper use of subscription credit facilities remains unclear. How long is too long? In an audience poll conducted at Private Equity International’s CFOs and COOs Forum at the start of 2019, 42 percent said the average length of loans drawn on their credit line was around three
months, and a quarter said they were averaging more than six months. In a separate poll, 31 percent replied they had “generally extended” the duration of the loans over the course of the last year.

One emerging development around the credit facilities question is that investors are starting to request performance reporting both with, and without, a line of credit. It is possible we may even see these types of request appearing in due diligence questionnaires and when raising capital for a new fund. This itself brings additional complications as reporting will be based on a number of assumptions. For example, what is the estimated cost to the GP of holding LP cash before a transaction rather than bridging the capital call? What impact would closing a deal faster using a credit line have on an asset price? There are many unknowns to be addressed.

“Transparency is very important for investors, and they are demanding disclosure of the use of a credit facility. Regarding the disclosure of levered versus unlevered returns, that topic rests with the LP community and their ongoing conversations with PE sponsors.”

Tim Ruxton, Managing Director

A CHANGING PICTURE

Generally speaking, first-time managers may find that obtaining a subscription line is much more difficult than for funds that have been established for longer periods of time. But typically, newcomers starting with a smaller initial fund quickly raise a second, often larger, vehicle, allowing them to obtain a line with mid-market providers. As their fund size grows with the third and fourth generations, they can borrow from the large banks. We are also seeing a move towards uncommitted subscription lines of credit with managers knowing that capital is available, but they will not be charged fees as banks do not have to reserve the capital. A hybrid solution of committed and uncommitted is growing in popularity. With investors and GPs mindful of a market downturn and the potential for interest rate hikes, it remains to be seen how GPs’ use of subscription lines of credit will play out.
Private debt remains an attractive investment option throughout Europe with particular interest in the real estate private debt space. Drawn by speedy returns, real estate assets are highly popular in the EU and the UK with investors favouring property development projects. As the private debt arena continues to gather pace, increasingly sophisticated real estate and infrastructure debt lenders are arriving on the scene along with a more diverse range of investors. With a mature market and buoyant demand, what does the future for European fund managers look like? Spencer Wells, Country Executive United Kingdom and Patrick McCullagh, Head of Sales EMEA take a look.

While the barriers to entry may be rising, new debt managers are continuing to enter the European market, bringing investors more choice about their debt strategies. Recently there has been growing activity from global debt fund managers. However, as investment options open up, investors are looking for those managers with an established record of creating and efficiently managing a broad portfolio of loans. Europe’s substantial reporting requirements, along with the administration of complex real estate and private debt structures, remain a challenge to both fund managers and administrators. It requires a significant investment in teams and technology, an investment that not everyone is prepared to make. To understand the private debt market, it is important to recognise that debt-focused tools are not enough on their own. Experienced teams can see the nuances of this specialist asset class and are able to leverage the technology to meet the complex needs of managers, investors and regulators. These teams with experience evaluating loan agreements, together with dedicated technology, provide invaluable support to new debt managers finding their footing.

OPPORTUNITIES ON BOTH SIDES OF THE ATLANTIC

With Europe’s appetite for investing in private debt probably at its highest to date, US managers, large European banks and multi-class asset managers see clear opportunities and healthy returns in the European private debt market. While it offers their investors an attractive diversification option, tapping into the right advice and putting the right infrastructure in place in order to capitalise on these opportunities can be a challenge. In an unfamiliar environment, it is important to make it as easy as possible for investors to enter the market by supporting them every step of the way.
“It’s certainly an exciting sector to work in and one where continued investment in human expertise, technology and operational scale are vital for keeping pace with the growing sophistication and needs of debt fund managers, investors and borrowers.”

Patrick McCullagh, Head of Sales EMEA

In addition to operational support, funds must also be financially attractive to US investors who typically adhere to a tight total expense ratio. Clear cost controls, a solid fund administration and reporting platform and sharp technology can be critical deciding factors for US managers looking to Europe. But this is not a one-way journey; US managers are setting up parallel funds as they hope to attract European investors across the Atlantic. And while special structures and strategies are required to protect a fund from triggering domestic taxable income, managers and administrators working in cooperation with appropriate tax and legal advisers can smooth the path through complex structuring.

THE IMPACT ON PERFORMANCE MEASUREMENT

Due to the increase in volume and complexity of the private debt market, specialist teams play an important role in the aggregation and presentation of performance data at both portfolio and loan level. With increasingly sophisticated investors demanding transparent reporting, managers must be able to demonstrate their position and their strategy in all market conditions for all portfolio assets. This stringent approach to performance measurement will quickly expose any lack of expertise from a manager or administrator.

“Both banks and private lenders have continued to meet borrower needs and respond to growing demand. The industry is maturing with both private debt managers and investors boasting teams of specialists familiar with the assets, resulting in a higher frequency of deals coming through. The challenge for managers has shifted away from finding investors and more towards finding good debt to fund or acquire.”

Spencer Wells, Country Executive United Kingdom
PATIENCE AND PERSISTENCE IN ASIA-PACIFIC

Johnson Har, Head of Hong Kong, Kevin Williams, Head of Operations for Asia-Pacific, and Jayesh Peswani, Relationship Manager for Asia-Pacific, share their perspective on the challenges and opportunities facing special situations and distressed debt markets in the Asia-Pacific region.

Recent developments in the trade war between US and China are getting a lot of media coverage with news stories suggesting that the economic impact is going to hit some companies soon. Analysts believe that when that impact arrives, investors will become more active, either investing directly or waiting in the wings as transactions pick up the pace. But it is hard to paint a truly accurate picture as often distressed debt managers operate stealthily, approaching potential targets and sealing the deal before anyone finds out. Kevin explains, “In years past we had not seen high volumes of transactions in China. The main issue has been lack of supply, but that could be changing. In 2019, prices dropped to more attractive levels as more inexperienced players took a step back. Then in early 2020, the US-China trade deal included surprising clauses allowing foreign investors more direct access to the China NPL market, which our clients are strongly considering.” As the debt market in Asia-Pacific has more depth and breadth than Europe, investors are growing in confidence and debt is no longer seen as a niche product. First-time debt funds and established debt fund managers are seeking to develop their fixed income strategies into the distressed debt scene with real estate proving an attractive option. Johnson adds, “Whether it’s NPLs or special situations, Chinese real estate developers need more flexible sources of capital, be they domestic or international in origin.”

OVERCOMING OPERATIONAL CHALLENGES

According to Kevin, it is important that participants in the debt and special situations space must be better at coordinating their people on the ground and building more efficient platforms because without the right structure and processes in place, it is not possible to develop a consolidated view across their portfolio. He says, “Often the fund managers have front-office capabilities and they know what they are doing in underwriting credit, but they don’t have the type of operational platform we see with banks. The software available to manage this is often not tailored to alternative investment managers.” One of the main constraints we are hearing is that sourcing deals in the Asia-Pacific region is difficult. While demand for exposure in these markets exists and capital can be raised, the supply is limited. And even when an opportunity is identified, there is unlikely to be a fully operational, comprehensive platform to enable the funds to be administered in-house. Additionally, as the opportunity is most likely to be unique, the paperwork burden and extensive workflow processes across teams is a real challenge, particularly for those managing portfolios from a distance. Kevin adds, “It’s tough to run the whole operation in Excel. In many cases, when firms buy those portfolios in different geographies, they must be local to capitalise and convert those NPLs into cash.” Often there is a scramble operationally to catch up with investment activity to ensure the portfolio is being monitored and reported on correctly.
LOOKING BEYOND CHINA

The market may currently be dominated by activity and opportunities in a maturing Chinese market, but if successful it could drive interest across the region. Increasingly India is being seen as an attractive investment destination with new and clearer rules in place concerning the collection of NPLs. Slowly investors are overcoming their reservations and becoming more comfortable with India. While sharper rules make a difference to investor confidence, the central driver for investment opportunities is how the economy is performing at a fundamental level. India is making progress but still has a way to go. Jayesh explains, “If you take a look at South-East Asia there is a lot of nuance with each of the markets, so it’s very difficult to say what level of opportunity there is. You have activity going through Hong Kong and Singapore, and a lot of it is directed at these markets. Nevertheless, I would say that South-East Asia is still lagging a little bit behind.”

“In Hong Kong we are seeing more direct special situations investment activity. Historically this has been conducted by locally based fund managers focusing on that specific strategy, but we are now witnessing a change in the type of market participants.”

Johnson Har,
Head of Hong Kong
Real estate debt as an asset class is booming and has grown to become investors’ number one alternative investment option. Doug Hart, Chief Executive Officer at Alter Domus, and Maximilien Dambax, Head of Fund Services North America, examine the trends and the technology shaping the outsourcing debate.

Real estate debt has always been complex, but it has now hit a new level of complexity bringing with it an array of cost implications. Regulatory changes post-2008 have seen mainstream banks adopt a more conservative, cautionary approach to lending. In the space left vacant by traditional lenders, we are seeing the growth of debt fund managers, sophisticated new structures and an increasing need for tailored solutions from third party service providers. With investors demanding greater levels of transparency in response to increased complexity, the outsourcing model is an attractive option. However, what is emerging is not a ‘one size fits all’ model, but a more flexible approach to outsourcing, offering truly tailored solutions. In some cases, large, established investment managers are opting to ‘lift out’ a component of their operations team, or sometimes their full team. Co-sourcing, where managers are happy to have some or all of their system in-house but do not have the capacity to service a component of their operational activity, is increasingly seen as a viable option as well.

What is clear is that there are a number of different outsourcing arrangements emerging, with investment managers able to precisely define the operational relationship that works best for them. This applies not only to new investment managers, but to large, established players as well. Staying ahead of emerging technology and on top of the complexities needs highly trained, and in some cases retrained staff, with ongoing cost implications. While cost is a key element in the decision-making process, the cost implications and variables of outsourcing go beyond staff and systems – efficient outsourcing can fill a knowledge gap. Experienced teams of specialists supporting new funds or fund structures can be an invaluable resource, delivering a streamlined service and hitting the ground running in terms of operational needs.

TECHNOLOGY, SETTING HIGHER STANDARDS FOR CASH FLOW

Real estate debt is unique in that it has payments coming through every day with different yield maintenance-type calculations and paydowns. Thankfully, the days of unreliable spreadsheets are increasingly a thing of the past replaced by specialist systems with integrated loan administration and fund accounting functions. Automated daily reconciliation offers managers clearer risk management analyses and an ongoing underlining of their investment strategy. Direct access to detailed data showing portfolio cash flows and returns across industries, rating, size and type allows managers to monitor, report and transact based on solid data points.
“The operations team supporting the front end has to be a servicer – an advanced reporting agent – and then you’re providing a professional accounting overlay on top. All of that working together makes real estate debt unique when compared with the other sectors.”

Doug Hart,
Chief Executive Officer

A SEAMLESS TRANSITION FROM DEBT TO EQUITY

A particular strength within the administrator space is having the platforms in place to support both real estate equity and real estate debt, where transactions are supported at both the holding company and asset level. By building out the collateral for the loan in addition to the loan itself and leveraging administrators’ loan servicing and property-level accounting services, reporting is consistent through transition. As complexity increases and cost pressure continues, it is the role of third-party service providers to create a unique infrastructure around the operations team that does not exist in-house. ★
As growth in the private markets investment space continues to gather pace, a new era is emerging, bringing with it new challenges, new thinking and an increasingly important and technologically advanced role for service providers. We examine the ever-growing demands facing asset managers in the alternative investment sphere and take a look at how the current trends in private markets are shaping investment opportunities in APAC and driving mergers and acquisitions activity for service providers across the board.

In a world of persistently low interest rates, investors seeking healthy returns, or simply diversification, are increasingly turning their attention to alternative investments. This demand is driving rapid growth in the global asset management industry led in particular by private markets, a position which seems likely only to accelerate. Globally, private markets are forecast to grow at a compound annual growth rate of 9.4 percent from 2018 to 2025. While private equity remains the largest asset class, infrastructure looks set to grow fastest of them all at a staggering rate of 22.5 percent from 2018 to 2025. However, despite its exceptional growth forecast, private equity and real estate remain asset managers’ top focus with infrastructure thought to be the most important asset class by just 12 percent of those surveyed*. This discrepancy may reflect the fact that only a small number of the largest asset managers have enough scale to manage infrastructure strategies.

BRINGING CLARITY TO A COMPLEX ENVIRONMENT

Against this backdrop of rapid private markets expansion and the growing awareness of infrastructure as an asset class with clear potential, the role of service providers is set to become increasingly vital. With investors allocating more assets to private markets, they require more information available 24/7, customised reporting and a smarter, sharper service. In addition to the ever-increasing demands of institutional investors, US regulators continue to add to the maze of legislation with the country’s new tax system, the Tax Cuts and Jobs Act,
which will impact private equity and other asset classes. Taken together, investor demands and regulatory requirements are making asset managers’ operations more complex, putting them at risk of becoming less efficient and less cost effective. It is the responsibility of service providers to make the complex simple by providing cutting-edge data management and new technologies that asset managers will need. Those service providers who have not only the capability to manage high volumes of complex data but also the ability to maximise this data, will set themselves apart. Such scope leads to better pricing models, clearer settlements, faster reporting on complex transactions, as well as better risk analytics across multi-asset portfolios.

“If asset servicers are to square the circle between service quality and cost, new technology and enhanced data management are essential. Those providers with high levels of automation are ideally placed to deliver the higher levels of service and reporting that are demanded. It’s time for asset servicers to shift to a ‘data as a service’ model that delivers automated and insightful information.”

Bruno Bagnouls,
Head of Products,
Head of Relationship Management

HARNESSING THE POTENTIAL OF TRANSFORMATIVE TECHNOLOGY

Data is at the core of performance metrics. And service providers investing in the latest technological tools can excel at data management and differentiate themselves with superior service levels and integrated, seamless processes. Artificial intelligence, robotic process automation, blockchain, cloud computing and the latest web portals offer invaluable efficiencies in time, cost and management. Asset managers have clear expectations for their service providers and a strategic technological solution will address all four focus areas.

TOP EXPECTATIONS FOR SERVICE PROVIDERS

1. Improved workflow
2. Solving accounting discrepancies between fund and SPV
3. Providing investment models and analytics
4. Providing market insights
ASIA PACIFIC GEARS UP FOR CHANGE

Change is afoot in APAC’s fast-growing private markets. Global and regional asset managers are positioning themselves for the opportunities presented by the increase in the region’s private markets activity. PwC’s forecast that global private markets will grow from USD 8.7 trillion in 2018 to USD 16.3 trillion in 2025 is reflected in investor activity in the APAC region. Institutional investors are turning to private markets in Australia and Japan, the east Asian countries of Korea and Taiwan, and Hong Kong, Malaysia and Singapore. Just as in the rest of the world, this growth is led by private equity, with infrastructure and real estate likely to experience rapid growth over the coming five years. As APAC’s private markets asset managers expand, service providers must provide centralised, scalable, multi-asset platforms and local knowledge to meet the specific needs of this diverse region. It seems clear that the complexity of administering private markets’ assets will mount as the growth of APAC’s private markets accelerates.

“Asset managers are looking to service providers to make sense of such complexity. Service providers must invest in the expertise and technology to make operating in multiple asset classes across the region both effective and efficient. As private markets asset managers grow in APAC, they are likely to outsource complexity to centralised platforms that meet clients’ information and reporting requirements.”

Alexander Traub, Regional Executive Asia Pacific and Chief Commercial Officer

NEW FUND STRUCTURES FUELLING GROWTH

The launch of the Asian Regional Fund Passporting Scheme in early 2019 and the arrival of new fund structures such as the Singapore VCC and Hong Kong’s OFC structure seem likely to trigger greater centralisation. As opportunities across the region continue to open up with increased standardisation and innovative investment vehicles, a single, centralised service provider will be an invaluable resource. Most APAC private markets managers use just one service provider, reflecting the need for specialist expertise. Managing asset classes ranging from private equity and venture capital to real estate and infrastructure across several Asian countries is challenging. Simply mastering the wide range of regulations in the region is a highly complex task requiring in-depth local knowledge. Not surprisingly, regulatory expertise is one of the key criteria for selecting a service provider.
When selecting a service provider, asset managers in APAC value high quality service above all else, followed closely by asset class expertise and competitive costs. The solution to delivering a first class service at a competitive price lies with technology – automation, data analysis, transparency. In such a geographically diverse region, there is a natural appetite for the benefits and efficiencies that cutting edge financial technology brings. It seems clear that leading APAC service providers will be investing in relevant technology platforms as well as increasing their investment in self-service and mobile applications. While the region may be diverse, one thing that APAC asset managers share in common is that they all value service providers’ competence with technology and data.

**PRIVATE MARKET EXPERTISE DRIVING M&A ACTIVITY**

Service providers are following in asset managers’ footsteps as they too expand through acquisition activity, offering access to new investment opportunities and investors. Specialist asset servicing businesses in both the US and Europe, particularly niche service providers with expertise in private markets, are likely to attract interest from larger, generalist rivals. Additionally, acquiring companies may be looking to gain scale and access to new technology. As the pace of technology continues to advance, M&As may become an increasingly important approach, especially considering the high cost of in-house development in specialist areas.

**OPPORTUNITIES ARISING FROM SERVICE PROVIDER M&A**

- Increasing scale and capabilities with new clients, new emerging product types and access to new market offerings
- Increased access to innovation, differentiated technology and IP in existing platforms
- Opportunity to migrate away from slow growth cycles and lower margin business models

**ALL EYES ON EUROPE**

For US-based service providers, Europe is an important and highly attractive market, making it a likely M&A destination. Almost half (45 percent) of survey respondents reported that European jurisdictions are important for their investors. Tax and tax compliance rank highly as required services in Europe, followed by legal and compliance. Fund administration, data analytics and reporting, and valuation are also regarded as important. Luxembourg is regarded as the most important fund domicile over a 12-24-month horizon, as it is already well established. US-based service providers aiming to expand into Europe may conclude that an acquisition is their best option. Depending on the acquisition target, the advantages are an existing client base, a pool of specialist knowledge, a distribution network and existing technology.

**A CHANGING INVESTMENT LANDSCAPE**

While growth in private markets is making an impact on the investment landscape, service providers must ensure that their offering provides the sophisticated, speedy solutions needed to support asset managers in their increasingly intricate business activity. Typically asset managers outsource routine processes such as fund administration and tax and also anti-money laundering requirements. In addition, those service providers who can manage and maximise the potential of large, complex data sets are ideally placed to deliver investment models and clear analytics at the push of a button – invaluable information from a customised service.

“Service providers can help their clients meet investors’ expectations for real time data transparency. Those with strong technological capabilities who can successfully bridge the gap between data and their knowledge base will be in high demand.”

Doug Hart, Chief Executive Officer

* All findings are derived from Alter Domus’ 2019 APAC Alternative Asset Servicing Survey and 2020 US Alternative Asset Servicing Survey unless otherwise stated.
As the alternative investment industry is slowly but surely embracing new and better technology, Anita Lyse, Head of Real Estate, examines how fund administrators are growing in status and how technology affects the relationship between administrators and their clients.

Anita Lyse sees one trend in particular emerging in the fund administration business as third party service providers continue to develop their role and relationship with fund managers. There are both push and pull dynamics in the market that lead the way for administrators to move further into fund managers’ middle office. The need for additional data and reporting in the industry seems to be never ending and many fund managers are looking at which outsourced solutions are available to respond to these challenges in the most robust and efficient manner. They are typically all keen to ensure their own back and middle office are as streamlined as possible to keep their strategic focus where it needs to be; on investment and asset management activities.

At the same time, administrators have been broadening their services to offer more comprehensive support and now play an increasingly important role in supporting investment managers’ business activities and goals. They also have large amounts of data already available as a result of the back office function they have carried out for years, so enhanced data analytics and reporting capabilities are natural add-ons in the service offering.

Administrators’ success in stepping into managers’ middle offices has until now to a large extent been based on their ability to demonstrate a real understanding and knowledge of their clients’ environment and needs and to establish a true partnership with their clients, but going forward technology will become increasingly important as a key success factor.

She says, “we look at ways in which we can be smarter about certain types of reporting, data aggregation and analytics to produce meaningful reports that will help our clients make informed asset management decisions.” Sharper, smarter reporting and deeper data analysis are indeed helping to build closer relationships between administrators and their clients, as the value add for managers is immediate.

**STANDARDISATION SMOOTHS THE WAY**

It is true that the alternative investment industry has been slow to standardise operational processes and investor reporting among other things, and falls behind more traditional investment vehicles. This often comes down to the very nature of private equity real estate, which comes with highly complex transactions, making standardisation so much more difficult to achieve. Yet the desire to harness the full potential of technology solutions, bringing improved efficiencies and automated processes,
is driving the alternatives industry slowly towards greater standardisation. Anita believes there is room to push standardisation a lot further in many different areas, such as for example the definition of a fund’s NAV and investor reporting requirements, which is illustrated also by initiatives carried out by both global and regional industry bodies. However, she is clear that increased standardisation in some areas does not mean there is no need for further customisation in other areas.

Tapping into technology and building greater standardisation is an ongoing process; its main drivers are to deliver a highly efficient service allowing the providers’ staff to focus on their value-added tasks, maximising their skills and competencies, and ultimately to support the fund managers in the most efficient way possible.

**DEMAND IS DRIVING NEW TECHNOLOGIES**

The demand for more sophisticated technology solutions also arises from the call for new products such as look-through capabilities and data analytics. One of the key challenges for large real estate fund structures is data aggregation because these funds will hold assets across several continents and jurisdictions. Many of these will have their own standards, so ensuring a like for like comparison between countries is sometimes easier said than done. The challenge is to find a way to collate data and consolidate it into meaningful data and analytics.

With well-developed client portals, we are now witnessing a move towards a self-service model, where fund managers and investors alike can not only easily retrieve static information and documents online, but also – and more importantly – build and extract various types of reports themselves based on their own needs.

The prerequisite for this to be possible is of course the availability of both financial and non-financial data within the portal, which needs to be as live as possible. This creates a completely different dynamic in the service offered by administrators.

Anita believes that we are still a long way from a ‘one size fits all’ solution, but a global and integrated technology platform seems indispensable as a starting point to solve the reporting complexities facing the alternative investment industry. “Technology investment never stops. At Alter Domus, technology is not simply about how we can automate repetitive and sometime low value tasks, but how we can provide a best-in-class service to our clients, constantly evolving to meet their changing needs.”

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“I think in tomorrow’s world, technology will continue to play an increasingly important role in the delivery of our services. Technology will never replace the human relationship between the provider and the client, however it will help improve it as it continuously reduces risks of human error, increases speed of execution, and facilitates communication and access to live information.”

**Anita Lyse,**

**Head of Real Estate**
Maximilien Dambax, Head of Fund Services North America at Alter Domus, and Antonis Anastasiou, Managing Director of Alter Domus Management Company, discuss how alternative investment funds are being structured and the challenges in operating a global fund platform in an AIFMD world that is about to see significant changes.

To support large capital-raising exercises involving a wide range of institutional investors, US managers are increasingly establishing global fund platforms either through parallel fund structures or with feeder fund structures that may include US, offshore and European sleeves. European sleeves and parallel funds are designed to be compliant with the European Union’s Alternative Investment Fund Managers Directive (AIFMD), often in association with a combination of Delaware and Cayman vehicles to complement the fund platform. These structures cover a diverse range of institutional investors by catering to their particular legal, tax and operational requirements.

WHAT OPTIONS ARE AVAILABLE FOR ATTRACTING EUROPEAN INSTITUTIONAL INVESTORS?

The alternative fund distribution and marketing landscape has changed dramatically in recent years, particularly in Europe with the implementation of the AIFMD in 2013, and further evolution lies ahead in the form of EU legislation amending the alternative fund framework. The AIFMD seeks to regulate the management of Alternative Investment Funds (AIFs), with Alternative Investment Fund Managers (AIFMs) required to meet key conditions regarding authorisation, general business conduct and marketing of the fund.

Accessing the European investor community is typically done via one of two marketing routes: national private placement regimes (NPPR) in certain jurisdictions where they are still in place, and AIFMD compliance. With NPPRs the manager must register with each national regulator to offer its funds in that market, but each market entails different levels of complexity, access to and availability of the regulator, as well as costs. The AIFMD option is more streamlined - by adhering to a single set of rules, alternative asset managers can passport their fund to all countries within the European Economic Area. It is also ideal if seeking access to institutional investors such as insurance companies that are often required to invest through fully AIFMD-compliant vehicles or fund structures.
### OPTIONS FOR AN EU AND NON-EU AIF

#### Parallel EU Fund Structure
- **EU AIFMD Compliant Sleeve for Marketing to EU Investors**
  - **EU Investors**
  - **EU Marketing Passport**
- **EU Parallel AIF**
- **EU AIFM**
- **Delegation of PM or appointment of Advisor**
- **Non-EU Manager**
- **Portfolio**
- **Non-EU Based Master for Marketing to Non-EU Investors**
- **Non-EU Investors**

#### EU Feeder Fund Structure
- **EU AIFMD Compliant Sleeve for Marketing to EU Investors**
  - **EU Investors**
  - **EU Marketing Passport**
- **EU Parallel AIF**
- **EU AIFM**
- **Delegation of PM or appointment of Advisor**
- **Non-EU Manager**
- **Non-EU Fund**
- **Non-EU Based Master for Marketing to Non-EU Investors**
  - **Non-EU Investors**

### POINTS FOR CONSIDERATION:
- Under AIFM definition of master/feeder: Over 85 percent of feeder must invest into master
- Marketing of the EU feeder is only eligible if the master is an EU master managed by an EU AIFM
- Non-EU managers looking to set up an EU feeder for marketing to EU investors should ensure they do not fall within the definition of master/feeder under AIFMD
American Flag

HOW ARE ALTERNATIVE FUNDS MARKETED TO EU INVESTORS?

AIFMD-compliant alternative investment funds are marketed within the EU via the single market passport. A manager that is an authorised AIFM or has appointed a third-party AIFM can market its AIF in all EU states using a simpler regulator-to-regulator notification mechanism.

In July, legislation was finalised covering the pre-marketing of alternative investment funds within the European Economic Area, which is widely used by non-EU managers to exchange information about AIFs with investors. The new rules introduce a notification requirement for pre-marketing to professional investors in the EU and will have implications for reverse solicitation.

EU AIFMs that have taken advantage of pre-marketing will no longer be able to accept investments from any institutional investors through reverse solicitation for 18 months from the start of pre-marketing activity, and no investors contacted during the pre-marketing phase can invest via reverse solicitation. Instead they can only invest once the AIF is authorised for marketing in the relevant EU member state under the full AIFMD requirements. The legislation came into force in August and the new rules will be fully enforced from August 2021.

Under the new regime, only investment firms, banks, UCITS management companies or AIFMs will be authorised to conduct pre-marketing and marketing activities. This provision underlines the need for the appointment of an EU-domiciled AIFM for alternative investment funds raising capital within the EU by a non-EU based manager.

Regarding NPPRs, it’s important to note that in July 2018, guidelines were issued to EU member states regarding the abolition of private placement marketing of AIFs. Some large member states including France, Germany and Italy have already either restricted the marketing of alternative funds for certain types of investors or abolished their NPPR regimes altogether.

ARE THERE ANY SPECIAL CONSIDERATIONS REGARDING GLOBAL FUND STRUCTURES?

When setting up and operating a global fund platform, either involving a parallel fund or a feeder format, various operational factors should be considered.

Income and expenses: The deduction of costs cannot be conducted pro-rata from the overall structure, as AIFMD-related costs should be borne solely by the EU vehicle. The same is true for currency variants and hedging strategies through feeders or special purpose vehicles, as foreign exchange and hedging costs are attributed to and impact only the entities and investments they relate to.

Rebalancing: Rebalancing mechanisms may be required to rebalance pools of assets across the different funds, due to varying progress of fundraising, operational constraints or capital availability. External bridge financing is one way to remedy this, but it entails additional direct costs. Master-feeder structures do not require a balancing mechanism for holdings, but they involve analytics requirements and capabilities to extract investment performance on an investment-by-investment basis.

Portfolio and risk management: The core functions of an AIFM are portfolio management and risk management of the AIF. One of these activities, but not both, can be delegated to a third-party AIFM if the delegate is an authorised and regulated asset manager in the country where they are established, and if a memorandum of understanding is in place between the domicile country of the AIF and that of the asset manager.

Control: Where the manager of the vehicle is not considered a regulated asset manager in their country of domicile, the AIFM retains the role of portfolio manager and, in theory, has full control of investment in and divestment of assets by the AIF. Solid procedures should be followed in the onboarding phase to provide the necessary assurance to the asset manager that there should be no concern regarding the approval of the assets they recommend.
WHAT PITFALLS OR CHALLENGES MAY ARISE IN IMPLEMENTING AND RUNNING A GLOBAL PLATFORM?

While these structures offer flexibility for both investors and managers, they require a great deal more coordination and collaboration between the parts of the fund structure or parallel vehicles. This makes a vertically integrated approach across structures from fund to asset level critical. Partnering with a fund administrator with management company capabilities helps ensure that compliance, internal controls, regulator and investor reporting and performance evaluation are streamlined across the board.

Vertical integration also simplifies the generation of data required for investment and risk management. End-users often require access to more than just live portfolio data, and may expect data and analytics at the fund, intermediate holding and portfolio company levels. This is best achieved through interactive portals that provide access to all pertinent data through drill-down and slice-and-dice functionality.

When conducting fundraising rounds, asset managers must identify robust partners that can provide a full suite of services across multiple jurisdictions with a high level of expertise along with specialist local insight. Running an EU parallel fund or an EU-specific entity represents an additional cost for US and other non-EU asset managers, and the efforts undertaken by some groups to develop these capabilities in-house or use multiple service providers to lower costs are often unsuccessful – managing multiple service providers across various jurisdictions can add to asset managers’ administrative burdens.

Selecting a single provider that can not only service AIFs and SPVs in all jurisdictions required but deliver management company services with interactive access to the structure’s data leaves asset managers better equipped to manage complex inter-connected fund structures – and frees them to focus on fundraising and investment strategy for their EU institutional investor base.
Singapore is a well-established and well-regarded financial centre. Renowned for its stability and commitment to a level playing field, recent years have seen the Singaporean government take steps to shore up its leading position while opening doors to new investment structures. Assets under management have grown and the country remains an attractive regional base, one which is increasingly seen as the preferred destination for asset managers in Asia.

Singapore offers US and European fund managers an attractive package when looking for a regional base to invest in Southeast Asia, India or even Australia and New Zealand. Alongside a robust regulatory framework and stringent licensing requirements, Singapore offers a large network of double tax treaties and tax incentives for fund managers. The Monetary Authority of Singapore (MAS), the country’s central bank and regulator, enjoys a strong reputation and is widely respected around the world with investors regarding MAS licensing as a real positive. With the government playing an active role in supporting the financial services sector, stability and reliability are important elements of the country’s offering. Against this background, the MAS recently introduced a Venture Capital Fund Managers license in addition to passing the Variable Capital Company Act in 2018. Aiming to attract venture capital fund managers with a display of tax incentives for funds, along with extensive double taxation treaties with some 90 countries, Singapore is keen to expand its alternative investment market, often acting as a co-investor.

A SOLID FINANCIAL ECOSYSTEM

In 2017, the Intellectual Property Office of Singapore, in collaboration with local private equity firm Makara Capital, launched a USD $1 billion Makara Innovation Fund. Additionally, in November 2018 the MAS announced a USD $5 billion pool to invest in start-ups and entrepreneurs. With government funding such as this, a domino effect running from the private sector to the public sector has enabled Singapore to build a comprehensive financial ecosystem. However, despite the nature of Singapore’s investment regime, specific regulatory structure and logistical aspects, it can still seem difficult to navigate for new players in the market.
ON THE GROUND EXPERTISE

While the process to establish a regional HQ in Singapore is fairly straightforward, it can be a challenge for finance professionals in Asia to find exit opportunities for their investments. Despite the dynamic regional economies of Vietnam, Indonesia and the Philippines, fund managers can face problems realising the gains from their investments. However, a fund administrator who understands the variations and individualities of the markets in Southeast Asia proves invaluable to clients operating across the region’s different jurisdictions and regulatory regimes.

Alter Domus has had a presence in Singapore for more than a decade and has built up extensive regional knowledge and developed professional relationships and in-depth expertise. This solid foundation allows the team to support fund managers in all areas including incorporation of vehicles and providing a registered office and directorships services. By assessing clients’ needs, their business and their long-term growth strategy, an approach can be developed that allows both to grow together over the long term. By taking care of all aspects of setting up and running a fund, an established administrator can free up investment managers to focus on generating higher returns for their clients.

While many overseas fund managers attempt to enter the market on their own, a large proportion find the task daunting as even seasoned investment professionals often lack experience in the specific regulatory and logistical aspects of administering a fund, especially in a new market.

“It’s important for fund managers to work with specialist service providers with the flexibility to develop bespoke solutions for clients – unlike the rigid offerings provided by many larger banks. Additionally, the provider must also have the scale to handle clients with more substantial needs.”

Tze Sheng Sum,
Country Executive Singapore
SUBSTANCE REQUIREMENTS: THE CAYMAN ISLANDS TIGHTEN UP

Traditionally the Cayman Islands have offered fairly flexible, indeed loose, substance requirements. Last year, however, saw a tightening of the rules, ushering in new operational requirements. Alexander Traub, Regional Executive Asia Pacific and Chief Commercial Officer, Ming Bi, Head of China, and Jayesh Peswani, Relationship Manager for Asia-Pacific, take a look at how fund managers are responding to the regulatory changes.

The International Tax Co-operation (Economic Substance) Law was introduced in December of 2018 to fall in line with global efforts to match revenue and gains with operational substance. Cayman’s new economic substance law aims to ensure that companies engaged in banking, distribution and service centres, financing and leasing, fund management, headquarters, holding companies, insurance, intellectual property or shipping businesses have actual operations in the island nation. So, what does it mean for Cayman’s long-established and popular funds domicile?

Ming Bi explains, “The introduction of both the Economic Substance Law as well as the new Securities Investment Business Law which introduces new requirements for registration and exemption of securities investments, have brought an array of changes to the Cayman Islands. Many private equity managers have begun to make organisational changes to their funds to ensure compliance with both new regulations.”

A MOVING TARGET

As the actual requirements of the new law remain a moving target, some organisations are choosing to take minimal action for the time being – preferring to wait until the law takes on a more final form before taking more decisive efforts. However, requests for Cayman onshore directorships are rising while Cayman directors are taking a more active role in their respective funds, with increasing requests for information.

“It’s important to understand this is an evolving requirement,” notes Jayesh. “The changes reflect ongoing negotiations between Cayman and the OECD, where the OECD is pushing Cayman (as well as other offshore jurisdictions) to regulate the fact that entities domiciled there actually have operations there. Tighter regulations negate the ease of setting up and doing business in Cayman when compared with onshore jurisdictions. At present, both parties are trying to find a balance between these two factors.”

Although Cayman’s economic substance law will definitely affect its future as a financial centre, the specifics remain fluid as negotiations continue. According to experts at Alter Domus, in some 99 percent of cases, fund managers domiciled in Cayman would not have to make any significant changes to their current operations. For the 1 percent that are affected, they will have to demonstrate a certain level of operations in Cayman, such as holding on-shore board meetings or maintaining some level of portfolio management on-shore. There are, however, others seeking to re-domicile their managers to where they have their operations. If funds are focused on Asia, they may be looking at Hong Kong or Singapore, while Luxembourg is a natural choice for European funds.

Aside from the majority of managers that are choosing to wait and see what happens, we’ve also seen some of our clients setting up non-Cayman investment managers to mitigate some of the risk, rather than asking Cayman directors to take on more roles.”

Ming Bi,
Head of China
“It’s important to work with a partner with a global presence and ability to structure the best possible solution based on individual needs, operations and financial requirements. Once clients have decided where to domicile and have substance, they’ll need support for not only their funds and holding companies, but their management entities as well.”

Alexander Traub,
Regional Executive Asia Pacific and Chief Commercial Officer
AS JAPAN’S BUSINESS OWNERS MOVE ON, COULD PRIVATE EQUITY MOVE IN?

The Japanese market is unique in that SMEs represent 99 percent of all businesses, and the segment employs 70 percent of the workforce. And at the moment, nearly 2.5 million Japanese SMEs are facing succession issues. Tokyo-based Scott Reynolds, Country Executive Japan for Alter Domus explains, “In light of a substantial 55 percent inheritance tax, many business owners approaching retirement age are choosing to look for potential buyers instead of handing over the reins to the next generation. This presents a clear opportunity for the private equity market.”

Looking to stimulate the market, Japanese lawmakers are considering new tax perks to increase cross-border M&A deal activity – which set a fifth consecutive record of 777 transactions in 2018.

STRENGTH IN STABILITY

As one of the most mature economies in the region, Japan offers a stable platform for investors with relatively low risk. Scott explains, “Right now, it’s an interesting place to invest, and PE is definitely ahead of the curve in identifying opportunities. Building on robust due diligence, PE firms are seeing the value in the market – which is characterised by more conservative returns offset by relatively lower risk. Recently, almost two-thirds of primary transactions have been linked to succession issues.”

For many Japanese firms, PE investment not only offers a financially rewarding exit opportunity, but also a chance to keep the business alive when an appropriate heir is unavailable or unwilling to take over. Private equity investment can breathe new life into 28 SENSUS ISSUE 2

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For many Japanese firms, PE investment not only offers a financially rewarding exit opportunity, but also a chance to keep the business alive when an appropriate heir is unavailable or unwilling to take over. Private equity investment can breathe new life into
traditionally-run Japanese companies through corporate reorganisation and productivity enhancements – as well as improvements in transparency, governance, management and strategic planning.

According to Scott, “Another trend we are seeing is large conglomerates selling off non-core assets and divisions. In many of these cases, the companies are solid, but could easily benefit from cost cutting or additional investment in IT infrastructure. Leveraging their business networks, PE investors can also quickly expand distribution by providing access to new domestic and international markets.”

Although some wariness remains amongst older generations of business owners, younger founders and CEOs are proving receptive to the idea of foreign investment, seeing it as an opportunity to grow the business. “In this aspect, global PE firms with strong brand recognition and due diligence teams have a comparative advantage – not just in terms of financial strength, but also in the receptiveness of Japanese companies,” comments Scott.

With well-established roots in the market, Alter Domus is noting strong investor interest in the large-cap health care and health-related technology sectors, as well as manufacturing support companies – such as those feeding into the country’s mature automotive industry. However the country’s recent succession issues have been unearthing attractive opportunities across all major sectors, and PE firms would be well advised to keep an open mind when evaluating potential investments in Japan.

“Alter Domus has the global and regional footprint, as well as the deep local knowledge to serve clients across the world’s key financial centres. With 2,400 professionals located around the world, we are initially serving a proportionately higher ratio of foreign clients through our Tokyo office – clients who appreciate our consistent service, stringent internal controls and transparent reporting, as well as our emphasis on cyber security,” Scott added.

He concluded, “Japan offers a balance of stable returns and relatively low risk. As the succession issue paves the way towards increased foreign investment, Alter Domus has the experience, knowledge and expertise to guide private equity investors as they seek the most attractive and potentially rewarding opportunities.”

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Luxembourg authorities update the Standard Chart of Accounts in an effort to streamline and simplify the accounting process. A development welcomed by the country’s administrators.

On 23 September 2019, the Grand-Ducal Decree of 12 September 2019, which determines the new Luxembourg Standard Chart of Accounts (“SCA”), was published in the Luxembourg Official Journal. The new SCA brings with it a number of innovations and clarifications to the accounting doctrine.

While not considered to be a complete transformation of the standard chart of accounts, this new SCA draws upon lessons from the original Grand Ducal Regulation of 10 June 2009. It intends to address many of the main concerns users expressed during the public consultation made by the Accounting Standards Commission in 2014.

OBJECTIVES OF THE NEW SCA
This timely modernisation is part of the regulator’s efforts to progressively reshape the Accounting Standards environment in Luxembourg.

As a whole, the modernisation of the SCA was designed to better meet the needs of companies and public users. It aims to improve the traceability of accounting information, to harmonise the practice, and to simplify the process of preparing annual accounts.

The new SCA will apply to financial years beginning on or after 1 January 2020 and is relevant for nearly all commercial companies which are obliged to keep accounting books and draw up and deposit annual accounts.

DIFFERENCES BETWEEN THE OLD AND NEW SCA
With a focus on simplifying administrative formalities and enhancing the technological aspect to reduce the risk of error, the new SCA is made with both accounting professionals’ and Luxembourg’s administrators’ interests in mind.

The Grand Ducal Regulation introduces the use of a mandatory mapping table for filling in the balance sheets and profit and loss accounts. The mapping table is customisable and can be made to fit the needs of individual companies.

Under the new regulation, additional consistency checks will automatically be performed when the standard chart of accounts and financial statements are filed.

When compared to its previous version, some accounts in the new SCA have been added, merged or split. Specifically, in order to eliminate unused accounts and any discrepancies between the SCA and the financial statements, some accounts in the SCA have been completely deleted. As such, it’s paramount that accounting professionals involved in preparing these documents have received adequate training on this new standard.

PREPARING FOR LUXEMBOURG’S NEW SCA
Companies will have to adapt their current chart of accounts to this new one. Mastering the practical and technical aspects of this new regulation is crucial for all accounting practitioners. It’s also important to ensure that accounting software can support the new SCA in order to ease the transition. Companies or their service providers will need to anticipate the timing and transitional steps necessary in order to move from the previous SCA to the new one.
“This move by the Luxembourgish authorities to modernise the Standard Chart of Accounts is yet another example of the local regulator adapting to the evolving needs of financial professionals in the country. Streamlining and updating the SCA certainly requires a great deal of coordination and effort on the part of service providers initially, but the outcome will ultimately be more straightforward and streamlined once fully adopted.”

Sandra Legrand, Regional Executive Europe