

GREAT FUND INSIGHTS

Why more private capital fund managers are domiciling in Asia

Pragmatic fund structures and attractive tax and setup incentives are convincing an increasing number of private capital fund managers to domicile in Hong Kong and Singapore.

Asia is rapidly maturing as a market for alternative asset management by offering exposure to some of the world's highest-growth, most innovative and most diverse economies. While the Cayman Islands and British Virgin Islands (BVI) are still the locations most fund managers choose to domicile their funds, many Asia-based managers are turning their attention closer to home.

The phenomenal growth we've seen in Asia-Pacific alternatives is only tipped to increase. Preqin forecasts Asia-Pacific private capital AUM to rise from USD1.7 trillion in 2020 to USD6.1tn by 2025, as the region quickly makes ground on the world's largest alternatives market, North America.

New structures modelled on international best practice

Eager to tap into this growth Hong Kong and Singapore have introduced appealing new fund structures and tax incentives. These structures have been modelled on international best practice and are designed to attract private capital to their jurisdictions and enhance their positions as leading wealth and fund management centres.

Hong Kong's Limited Partnership Fund (LPF) regime was introduced in 2020 and targets private equity funds, venture capital funds, real estate funds, buy-out funds and infrastructure

funds. It offers no restriction on investment scope and is flexible in terms of capital contribution and profit distribution.

Managers of offshore funds planning to establish a Hong Kong LPF find that it is similar to other limited partnerships in common law jurisdictions. There are few surprises in terms of how it operates and what the documents look like. It is, therefore, relatively easy to convert documents they may have used previously.

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The LPF is also as flexible as other partnership vehicles used for funds in this space. It can be used as a fund vehicle and as an investment structuring vehicle, in the same way offshore partnership vehicles have been used in the past.

At the same time, investors have also found it more acceptable to invest in a new structure which closely resembles structures they are familiar with.

Impressively, more than 300 LPFs have been registered since August 2020.

In addition, Hong Kong has introduced a 0% tax rate on eligible carried interest, which exempts qualifying carried interest from profits tax and salaries. In practice, payments of carried interest become tax neutral in Hong Kong. Any fund, wherever it is established, can qualify for the ‘0% carry’.

Singapore, meanwhile, introduced a limited partnership regime in 2009, also modelled on global best practices. This regime has now gained solid traction with sponsors and investors, and was recently joined by the Singapore Variable Capital Company (VCC) structure in January 2020.

The future of private capital in Asia

In our experience working with fund managers to set up new structures – LPFs in Hong Kong and Singapore in particular – we have found the process to be efficient, simple and easily transferrable from the traditional Cayman Islands and BVI models.

We see the trend of onshoring funds and investment platforms in Asia will continue to gain traction, especially as the new regimes in Hong Kong and Singapore provide for a very competitive funds framework.

Both jurisdictions have succeeded in setting up this framework in a short timeframe, with attractive incentives.

Private capital fund managers can set up a VCC as a corporate structure for a stand-alone fund or for an umbrella fund with multiple sub-funds. A VCC can also be established for both traditional and alternative strategies (open-ended and closed-ended).

Along with the usual tax incentives, the Singapore Government has enhanced the structure’s attractiveness by paying a SGD150,000 grant to any fund manager that sets up a VCC within the first 18 months of a fund’s launch.

As with Hong Kong’s LPF, it has proved popular, with more than 250 VCCs established by March 2021.

But can Hong Kong and Singapore challenge the Caribbean’s dominance?

Against the backdrop of a significant growth in alternative assets in Asia – including an increase in the number and size of Asia-based fund managers – we believe the two Asian centres are well positioned to enjoy a growing share of the private capital pie.

The structures and incentives are appealing, and operating within local time zones is a bonus. Fund managers are also aware of the continuing trend of international tax authorities increasing their scrutiny of investment holding company substance in jurisdictions such as the Cayman Islands.

The Cayman Islands and BVI may be not under imminent threat as the world’s leading funds destinations. However, as familiarity with the new structures in Asia grows, more Asia-based funds will use them rather than their Caribbean counterparts.

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