

SINGAPORE VARIABLE CAPITAL COMPANIES – WIDENING THE ARRAY OF SINGAPORE FUND STRUCTURES

On 14 January 2020, the Monetary Authority of Singapore (MAS) and Accounting and Corporate Regulatory Authority (ACRA) launched the Variable Capital Companies (VCC) framework following the passing of the Variable Capital Companies Act 2018 (Act) on 31 October 2018, which was amended by the Variable Capital Companies (Miscellaneous Amendments) Act 2019.

This briefing discusses several key features of the VCC and how the VCC strengthens the array of fund structuring options that are available to Singapore fund managers:

"Onshoring" of fund structures

Historically, investment funds have been established in "offshore" jurisdictions (principally the Cayman Islands and other tax-neutral jurisdictions), but the past decade has seen a trend of funds being established in "onshore" jurisdictions (typically tax-advantageous jurisdictions with a network of double taxation treaties (DTTs) where the fund manager is located). With the launch of the VCC adding to the fund structuring options available in Singapore, the investment funds industry in Singapore is well-placed to benefit from this onshoring trend.

At the launch of the VCC framework, MAS and ACRA announced that a group of 18 fund managers participated in a VCC Pilot Programme pursuant to which 20 investment funds across a range of strategies (hedge funds, private equity and venture capital to name a few) were either incorporated or re-domiciled as VCCs. As part of this process, a Working Group formed under the Singapore Academy of Law prepared VCC model constitutions to reduce the time to incorporate a VCC, a project led by Clifford Chance.¹

In addition to the VCC, fund managers have also for several years had the option of establishing funds in Singapore as limited partnerships. The Singapore Limited Partnerships Act was launched in 2009, and based on the latest ACRA annual report, as of 31 March 2019, there are already 400 limited partnerships active in Singapore.

Key updates

- Framework for new corporate fund structure is now operational.
- VCCs may have several sub-funds, each with segregated assets and liabilities, with cross sub-fund investment permitted, and are free from the restrictions on redemptions of shares that are imposed on Singapore companies.
- The VCC complements the existing vehicle options in Singapore.
- ACRA will administer the VCC Act, while MAS will administer the AML/CFT obligations of VCCs.

¹ The VCC model constitutions can be downloaded here: <https://www.singaporelawwatch.sg/About-Singapore-Law/VCC-Model-Constitutions>

Generally speaking, from the perspective of global investor familiarity, the limited partnership is the preferred vehicle option for closed-ended funds, while corporate structures are preferred for open-ended funds.

Current Structuring Options

With access to both VCCs and limited partnerships, Singapore fund managers (or in the case of the VCC, only those regulated by the MAS) have a wealth of fund structuring options.

A Singapore fund manager may establish a fund in Singapore consisting of a single VCC or limited partnership or with a VCC as a master holding company beneath and with parallel funds in Singapore or elsewhere. It is also possible to establish a master-feeder structure with single or multiple feeder funds, both in Singapore and elsewhere. For investor familiarity and tax-related reasons, one structuring option for closed-ended funds may be to establish the fund as a limited partnership with a master holding company established as a VCC.

At present, a VCC must appoint a fund manager that is licensed or regulated by the MAS (a Permissible Fund Manager). Although this prevents managers who are not regulated by MAS from acting as the primary fund manager of a VCC in their own right, this does present opportunities for fund managers regulated by MAS. MAS-regulated managers may be engaged by fund managers not regulated by MAS (either foreign fund managers or managers relying on a licensing exemption) to establish VCCs and delegate certain portfolio management duties in respect of the VCC to fund managers not regulated by MAS.

Taxation

A number of features make the VCC structure a compelling fund structuring option from a tax perspective:

- (a) existing tax exemptions under sections 13R and 13X of the Income Tax Act (Cap. 134) of Singapore will be extended to VCCs. These incentives will be granted at the umbrella level for umbrella VCCs;
- (b) a VCC will be treated as a company and a single entity for tax purposes, and only one set of income tax returns will be required to be filed with the Inland Revenue Authority of Singapore even if the VCC is an umbrella VCC with multiple sub-funds;
- (c) deductions and allowances will be applied at the sub-fund level for determining the sub-fund's chargeable or exempt income;
- (d) the 10% concessionary tax rate under the Financial Sector Incentive – Fund Management scheme will be extended to Permissible Fund Managers managing incentivised VCCs;
- (e) as a corporation with its own legal personality, a VCC will be able to access Singapore's network of DTTs more easily as compared with other fund structures, potentially making VCCs attractive to investors accessing investments across Asia and beyond; and
- (f) a VCC may make an election under the US "check the box" rules to be treated as a "pass-through" entity for US federal income tax purposes, further enhancing the attractiveness of investing in VCCs for US taxable investors.

Other key features of the VCC are:

Shares and Share Capital

The Act provides that the requirement for shares in a VCC to be issued or redeemed at a price equal to the proportion of the NAV of the VCC represented by each share will be implied in the constitution of every VCC. In addition, VCCs will be able to issue different classes of shares with different rights and dividend payment policies, although the rights attaching to each share must be set out in the VCC's constitution. The Act appears to permit the approach of providing the rights of holders of shares in broad terms in the VCC's constitution, with more detailed provisions for such rights incorporated by reference (for example, by reference to the VCC's offering document), which is consistent with international best practice.

Redemption

Unlike shares in companies incorporated under the Companies Act (Chapter 50) of Singapore (the CA), shares in VCCs may be freely redeemable subject to the terms of redemption of shares set out in the constitution of the VCC, which enables VCCs to be used as open-ended funds. An umbrella VCC may also have the flexibility to use liquidity management tools, provided that any rights or limits to redemption are clearly set out in the VCC's constitution.

Cellular Structure

An umbrella VCC will be a single legal entity with sub-funds that have segregated assets and liabilities, but each sub-fund will not have its own separate legal personality. The Act provides for certain disclosure requirements for umbrella VCCs, allows for cross sub-fund investment, and for each sub-fund to be wound up as if it were a separate legal person.

Confidentiality

A VCC must maintain an up-to-date register of members at its registered office or at the office of a service provider whose office is in Singapore and must disclose this information to the necessary regulatory and law enforcement authorities upon request, although neither this, nor the constitution of the VCC, need to be made available to the public. Also, information on share allotments and redemptions will not be required to be lodged with the Registrar.

However, an umbrella VCC is required to send consolidated financial statements (in respect of each sub-fund of the VCC) to all members of the VCC entitled to receive notice of general meetings of the VCC (which would ordinarily include members of the VCC who hold shares in only some but not all of the sub-funds of the VCC).

Corporate Governance

A VCC must appoint a Singapore-based fund manager that is regulated by MAS – either licensed or registered – to retain overall responsibility for the fund management duties and to mitigate any conflicts of interests. At least one director of a VCC must be a representative or director of the Permissible Fund Manager. However, MAS has noted that it may reconsider this requirement in the future.

Directors of VCCs must be fit and proper persons, and the board of directors of Authorised VCCs must have at least three directors, including one independent director. VCCs must have at all times at least one director who is ordinarily resident in Singapore.

Custodial Arrangements

Authorised VCCs are required to appoint a custodian that is a trustee approved by MAS (an Approved Trustee). Such custodian will not have a general obligation to safeguard the rights and interests of the VCC's members, which will instead be imposed on the board of directors of the VCC.

However, restricted schemes structured as VCCs will instead only be required to maintain their assets in trust or custody accounts with a prescribed entity that does not need to be an Approved Trustee (e.g., licensed/approved banks, custodians or financial institutions, etc). Further, the requirement to appoint a custodian will not apply to restricted schemes that are private equity or venture capital funds, provided that investors have both been informed of the absence of custodial arrangements and their acknowledgement has been obtained.

Financial Statements

All sub-funds in an umbrella VCC will also be required to prepare financial statements using the same accounting standards as the umbrella VCC, which must be audited annually.

Winding-up of VCCs

VCCs may be wound up voluntarily by a members' resolution, similar to companies incorporated under the CA. The Court may also wind up a VCC: on the same grounds on which CA-incorporated companies may be wound up; where the VCC has conducted business outside its permitted use as a vehicle for a collective investment scheme only; where the VCC does not have a Permissible Fund Manager for a continuous period of 3 months; or where the VCC breaches its AML obligations.

Re-domiciliation and Restructuring

The Act enables foreign corporate entities compose of one or more collective investment schemes to be redomiciled in Singapore as VCCs under a regime adopted from the re-domiciliation regime under the CA. There is no minimum timeframe that a foreign corporate entity has to be in operation in a foreign jurisdiction before it can re-domicile to Singapore as a VCC. Also, MAS has clarified that a foreign umbrella fund may re-domicile to Singapore as an umbrella VCC, and that a foreign non-umbrella fund may re-domicile to Singapore as a non-umbrella VCC. However, multiple foreign non-umbrella funds may not re-domicile together to Singapore as a single umbrella VCC.

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