Real estate niche workshop

The beginning of a new cycle

24 October 2013
## Agenda

<table>
<thead>
<tr>
<th>Time</th>
<th>Session</th>
<th>Details</th>
</tr>
</thead>
<tbody>
<tr>
<td>9:00 a.m.</td>
<td><strong>Introduction</strong></td>
<td>Michael Hornsby, Partner, EMEIA Real Estate Funds Leader, AIF Club Chairman, EY</td>
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<tr>
<td>9:30 a.m.</td>
<td><strong>Panel 1: Market trends</strong></td>
<td><strong>Guests:</strong> Simon Nelson, Senior Vice President, Fund Management, ProLogis, Christian Schulz-Wulkow, Partner TAS, EY Berlin</td>
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<td><strong>Moderator:</strong> Bruno Di Bartoloméo, Partner, Real Estate, EY</td>
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<td>10:30 a.m.</td>
<td><strong>Coffee break</strong></td>
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<tr>
<td>11:00 a.m.</td>
<td><strong>Keynote speech on EY’s global real estate funds report “Trends in Real Estate Private Equity”</strong></td>
<td>Michael Hornsby</td>
</tr>
</tbody>
</table>
Agenda (cont’d)

11:30 a.m.  Panel 2: Drive for efficiency and outsourcing
Guests:
► Brian McMahon, Managing Director Business Development, BNY Mellon Alternative Investment Services
► Mark Houston, Director - Investment Management, Hines Luxembourg S.à r.l.
► Sascha Calisan, Vice President, Global Product and Strategy, Northern Trust
► Renaud Breyer, Executive Director, Financial Reporting Advisory Services, EY
Moderator:
► Michael Hornsby

12:30 p.m.  Networking lunch

1.30 p.m.  Panel 3: Fund distribution and capital raising
Guests:
► Marnix Arickx, Managing Director and Senior Project Manager Global Fund Solutions, BNP Paribas Investment Partners Belgium N.V. / S.A.
► Rudolf Koemen, Conducting Officer and Board Member, Crédit Suisse Fund Management S.A.
► Kerry Baronet, Head of Product Development, M&G Real Estate
Moderator:
► Rafael Aguilera, Executive Director, Advisory Services, EY
Agenda (cont’d)

2.30 p.m.  Panel 4: Tax substance vs. regulatory substance
Guests:
► Sven Rein, Managing Director, BNP Paribas Real Estate Management Luxembourg S.A.
► Raj Gill, National Director - Tax, LaSalle Investment Management
► Ian MacMahon, Vice President, Morgan Stanley

Moderators:
► Dietmar Klos, Partner, Head of Financial Services Tax, EY
► Axelle Ferey, Executive Director, AIFM Directive subject matter expert, EY

3.30 p.m.  Closing statements
► Michael Hornsby

3.45 p.m.  Cocktail reception
Panelists

Guests:
► Christian Schulz-Wulkow, Partner TAS, EY Berlin
► Simon Nelson, Senior Vice President, Fund Management, ProLogis

Moderator:
Bruno Di Bartoloméo, Partner, Real Estate, EY
Do you expect RE transaction market to be impacted by expected increase in interest rates?

1. Yes
2. No
Polling question 2

Is the current US political instability going to negatively impact the transaction market for RE?

1. Yes
2. No
Polling question 3

What is the main issue RE Funds will face in their investment strategy in the current market?

1. Lack of investors’ appetite to further invest in RE
2. Lack of bank financing available
3. Lack of available products at reasonable prices
4. Lack of flexibility in investment strategy
5. Other
Polling question 4

What are in your view the more attractive locations to invest in the near future?

1. Specific single EU country
2. All over EU
3. Asia
4. US and Latin America
5. All of the above
In 2011 EY carried out a survey to determine the impact of operating platform and different dimensions on the operating costs of the real estate funds domiciled in Luxembourg.
Luxembourg real estate funds cost survey – key findings of 2011 survey

Property specific costs represent the major portion of costs out of the total operating costs incurred by the funds followed by the management fees.

Management fee charged by the funds range from 0.31% to 1.27% of GAV. The average management fee is 0.78%.

The running costs for an opportunistic fund are significantly higher than those of a core and value added fund.

Operating costs of funds investing in core Europe and beyond Europe are considerably higher than of those investing within Emerging Europe.
Luxembourg real estate funds cost survey – key findings of 2011 survey

The TER and REER of funds which are carrying out their functions internally, or have a “predominantly insourced” operating platform, are lower than average.

Funds investing only in the industrial sector have much lower REER and funds investing only in residential, retail or multi-sector have higher property specific costs than average.

Only 18% of fund managers are doing detailed analysis of cost based ratios.
Luxembourg real estate funds cost survey – 2013 survey

2013 SURVEY

Benefits of survey:
- It will assist asset managers in improved decision making by providing correlation amongst cost ratios;
- It will help benchmark fund’s cost drivers and ratios with industry peers;
- It will help establish or refine a cost reduction plan;
- It will assist in setting KPIs by knowing the benchmark cost/cost matrix of industry peers operating in a similar dimension.
Luxembourg real estate funds cost survey – 2013 survey

Confidentiality

All data collected and details of the participants will remain strictly confidential and anonymous. The survey will contain only averaged market data and trends and no participant-specific data will be revealed at any stage.

How to participate

We invited in May 2013 all real estate funds domiciled in Luxembourg to participate in the survey. We have received feedback from funds representing 42% of the net assets under management in Luxembourg real estate funds and we count to receive even more before publishing the results of our survey in December 2013.
EY’s global real estate funds report “Trends in Real Estate Private Equity”

Slides are not available as underlying report has not yet been published. Survey will be available mid-November and will be posted on the AIF Club website and circulated to AIF Club members when available.
Panel 2: Drive for efficiency and outsourcing
Panelists

Guests:
► Sascha Calisan, *Vice President, Global Product and Strategy, Northern Trust*
► Brian McMahon, *Managing Director, Business Development, BNY Mellon Alternative Investment Services*
► Mark Houston, *Director - Investment Management, Hines Luxembourg S.à r.l.*

Moderators:
► Michael Hornsby, *Partner, EMEIA Real Estate Funds Leader, EY*
► Renaud Breyer, *Executive Director, Financial Reporting Advisory Services, EY*
Drivers of platform operating model

- Focus on core activities
- Business opportunities
- Service offering
- Investors’ expectations
- Expense ratios
- Efficiency and synergy opportunities
- Review of platform operating model
- AIFMD
Summary of activities

**AIF level operations**
- AIFM appointment/monitoring
- Valuer appointment/monitoring
- Modeling
- Financial framework
- Fund NAV computation
- Tax returns
- Legal
- Domiciliation
- Corporate governance
- Depository appointment

**Depository**
- Accounting
- Performance measurement
- Policies and procedures
- AIF on-boarding
- Ownership verification
- Cash flows review
- Valuation/NAV monitoring

**Distribution**
- Product marketing
- Customer relations
- Investor transactions
- Network management

**AIFM level functions**
- Accounting
- Risk/liquidity management
- Internal audit
- Regulatory reporting
- Legal
- HR
- Portfolio management
- Compliance
- Systems and workflows
- Tax
- IT
- Treasury

Real estate niche workshop
Overall approach

Key questions to be addressed:
• What is the fund manager’s core business?
• Where is my highest added value?
• Would outsourcing be profitable?

<table>
<thead>
<tr>
<th>Process complexity and dynamics</th>
<th>Strategic importance</th>
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<tbody>
<tr>
<td>Complex and dynamic processes but not part of fund manager’s core competencies: hard to automate, so outsource</td>
<td>Complex, dynamic, high value processes which generate a competitive advantage: careful monitoring, keep in-house</td>
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<td>Simple, commodity-like processes: automate with off-the-shell systems or outsource</td>
<td>Simple but important. Automate to improve efficiency</td>
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Case study (cont’d)

Process complexity and dynamics

<table>
<thead>
<tr>
<th>Strategic importance</th>
<th>1</th>
<th>2</th>
<th>3</th>
<th>4</th>
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<tbody>
<tr>
<td>Hard to automate, so outsource:</td>
<td>Legal</td>
<td>Careful monitoring, keep in-house</td>
<td>Automate with off-the-shell systems or outsource:</td>
<td>Try to automate to improve efficiency:</td>
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<tr>
<td>Legal</td>
<td>Tax</td>
<td>Risk and liquidity management</td>
<td>Accounting</td>
<td>Treasury monitoring (liquidity management)</td>
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<td>HR</td>
<td>Portfolio management</td>
<td>Regulatory reporting</td>
<td>Fund NAV computation monitoring</td>
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<td>Internal audit</td>
<td>Performance measurement</td>
<td>Domiciliation (to the extent no office in Luxembourg)</td>
<td>Financial framework</td>
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<td>Systems and workflows</td>
<td>Outsourced activities monitoring</td>
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<td>Cash payments and day-to-day treasury</td>
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<td>Modeling</td>
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<td>Depository/valuer appointment</td>
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Panel 3: Fund distribution and capital raising
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► Rudolf Koemen, Conducting Officer and Board Member, Crédit Suisse Fund Management S.A.

► Kerry Baronet, Head of Product Development, M&G Real Estate

Moderator:

Rafael Aguilera, Executive Director, Advisory Services
Key concepts

Private Placement → Distribution

Marketing → Reverse solicitation
Being an AIFM

► Opportunity or must be

► Passport

  ► Is regulation clear

  ► Impact on distribution and marketing model

  ► Impact on product development
Panel 4: Tax substance vs. regulatory substance
Introduction

- Base Erosion and Profit Shifting (BEPS)
- Alternative Investment Fund Manager Directive (AIFMD) implementation in Luxembourg
Base Erosion and Profit Shifting Report

- Overview on BEPS
- Key elements of BEPS report
- Next steps and action plan
- Potential impact on alternative fund products
BEPS: the Actions

- Action 1: Address the challenges of the digital economy
- Action 2: Neutralizing the effects of hybrid mis-match arrangements
- Action 3: Strengthening controlled foreign company (CFC) rules
- Action 4: Limit base erosion via interest deductions and other financial payments
- Action 5: Harmful practices
- Action 6: Prevent treaty abuse
- Action 7: Status of the permanent establishment (PE) rules
- Actions 8, 9 and 10: Aligning transfer pricing outcomes with value creation
- Action 11: Establish methodologies to collect and analyze data on BEPs
- Action 12: Require taxpayers to disclose their aggressive tax planning arrangements
- Action 13: Disclosure of supply chain information to tax authorities
- Action 14: Make dispute resolution mechanisms more effective
- Action 15: Develop a multilateral instrument
Potential impact on alternative fund products

OECD is not able to force the member states to implement its initiative. However, the following tax risk areas may be identified:

**Increase of the effective tax rate at the Target’s level:**

1. Amendments of Double Tax Treaties (e.g. LOB type of rules)
2. Rules for interest deductibility (limitation for debt-push-down),
3. More common application of PE concept,
4. New/stricter transfer pricing rules,
5. Broader jurisdiction to tax – CFC rules
6. Question of tax residency etc.

**Tax leakage on distributions:**

1. Amendments of Double Tax Treaties (e.g. less favorable methods of elimination of double taxation)
2. Anti-hybrid rules (limited usage of hybrid instruments),
3. Question of tax residency
4. Additional withholding taxation on distribution etc.
AIFMD - key considerations

**Business and operations considerations**

- Position regarding AIFMD?
  - AIFM passport
  - AIF passport
  - Branding
- Product strategy going forward?
- Distribution strategy going forward?
- Expectations of existing/target investors?
- Current structure of platform functions (insource/outsource)
- Main place of business?
- Alternatives
  - Reorganization of core IM functions
  - Migration of AIF/AIFM
  - Duplication of structures for EU/non-EU investors

**Regulatory and tax considerations**

- Identification of in-scope AIF
  - Location of investors
  - Grandfathering provisions
- Current AIFMD compliance level?
- Which regulator do I want to deal with?
- Tax implications of reorganization of core IM functions
  - For AIFM
  - For AIF
  - For AIF investors

Trade-off
Case study 1: Luxembourg

► Key facts

► Pan-European private equity manager
► 15 AIFs (EU AIFs) – 2 bn AuM
► GPs dedicated to each fund
► Portfolio management function relying on key competencies of investment advisors located worldwide
► Headcount in Luxembourg: 7
► Tax rulings in place for legacy structure
Case study 1: Luxembourg
Setting the scene
Case study 1: Luxembourg
Target model – Role of tax considerations

Investment Management

Mother company A.
(Luxco)

GP1 (Luxco)
GP2 (Luxco)
GP3 (Luxco)
GP 4 (Luxco)
GP 5 Sàrl (Luxco)

Sub adv France
Sub adv USA
Sub adv UK
Sub adv Singapore
Sub adv Middle East

Company A S.A.
(Luxco)

Company A Services
(Luxco)

Sub advisors

Investment advice

Investment
management

Unchanged

AIF level

SCA
SICAR
(Luxco)

Compartment 1

Compartment 2

Compartment 3

Mandates
Panel discussion
Panel 4: Tax substance vs. regulatory substance
Panelists

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► Raj Gill, National Director - Tax, LaSalle Investment Management
► Ian MacMahon, Vice President, Morgan Stanley

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► Axelle Ferey, Executive Director, AIFM Directive subject matter expert, EY
Polling question 5

In structuring your AIFM, how do you position the tax criteria?

1. First position
2. One amongst a set of key drivers
3. Not a key driver

![Graph showing poll results: 56% for option 1, 28% for option 2, and 16% for option 3.]
Polling question 6

In how many countries will you register as an AIFMD complaint manager?

1. 0
2. 1
3. 2
4. 3
5. More than 3
6. I do not know
Polling question 7

Will you register as an AIFMD manager in Luxembourg?

1. Yes
2. No
3. Not decided yet

69% 19% 12%
Polling question 8

Do you think that you will need more people and substance in Luxembourg as a result of BEPS?

1. Yes
2. No
3. I do not know

1 2 3
39% 39% 22%
Polling question 9

How do you evaluate the pressure from tax authorities regarding substance and PE issues compared to 3 years ago?

1. Same
2. Increased
3. Reduced
Thank you.
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