

# PRIVATE EQUITY

MOOK edition (magazine + book) / Winter 2014

## Say hello to improved reporting

- **What's hot**  
SICAR infographic: our annual SICAR 2013 survey in a nutshell
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Director in KPMG's global PE team
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Squeezing more out of valuation
- **Best Practice**  
Focus on PE investor reporting
- **Spotlight on**  
Environment Social and Governance  
agenda by Jane Wilkinson



cutting through complexity



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# Say hello to improved reporting

2014 is the year that PE reporting comes of age. While regulators may have previously approached reporting with a 'light touch', especially when compared with other industries, times are now changing. A number of factors come into play this year which will push PE houses to rethink reporting and overhaul practices.

One driving force behind change is PE investors, who increasingly desire more detailed and timely information to facilitate decision-making on investments. In a market where the balance has tipped in investors' favor, we expect PE houses to grant their clients' wish and put increased efforts into upgrading their investor reporting. David Nordlund, our reporting expert, provides insight on this topic, as well as a detailed analysis of how changes to IFRS will also be altering the way companies disclose information.

A further catalyst for reporting change is the AIFM Directive and its much publicized reporting requirements. Kian Navid and Mickael Tabart present the ESMA and the CSSF's most recent guidelines on reporting obligations and discuss next steps in the AIFMD saga for both the EU and for companies.

David, Kian and Mickael are just three amongst a whole team of experts from our Private Equity Team at KPMG Luxembourg. Thanks to the lineup below and many other PE professionals working behind the scenes for another year crammed with hard work and fun. A happy New Year to all from the KPMG team: 2014 is here.



**Thierry Ravasio**

Partner, Head of Private Equity

KPMG Luxembourg



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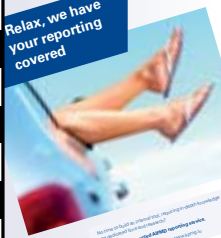
**Jane Wilkinson**



**This is just one half of the MOOK:  
if you like the magazine  
why not try the book:  
SICAR Illustrative Annual  
Report in accordance with  
Luxembourg GAAP**

# START

Relax, we have your reporting covered



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## Preface

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In this exclusive Interview, James answers our six questions on the current and future state of the PE industry. Will 2014 be a better year for Private Equity? Read this article and find out.

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## PE on Social Media

Private Equity has gone social and KPMG Luxembourg is now active on Twitter, LinkedIn and the KPMG Luxembourg blog. Don't miss our PE insights and follow us on our social media accounts or subscribe to our news letter on [blog.kpmg.lu](http://blog.kpmg.lu).

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## Jane Wilkinson talks about the ESG agenda

While Private Equity and Investment Funds are both close to Jane Wilkinson's heart, she chose this interview to focus on a topic important for both industries: sustainability. Jane explains how ignoring the ESG agenda could have disastrous effects on both your company's reputation and consequently its performance.

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In this wrap up of our Winter Mook, we take our favourite quotes from feature articles to give you the key takeaways from this edition on one single page.

Simple!

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Have a little time to spare while on the annual skiing trip? Why not catch up with some essential reading, courtesy of KPMG. Here you'll find a range of Luxembourg and Global publications made just for Private Equity professionals.

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## Interest for Limited Partnerships ignited in the States

Ilka Hesebeck and Julien Bieber went stateside to see how Luxembourg fits into the PE industry's world view in the US. The new Luxembourg Limited Partnership (LP) was met with enthusiasm by clients and colleagues in the US. Could the LP be the next success story for Luxembourg?

# Finish

## Infographic

# Our SICAR survey in a nutshell

## Introduction

The SICAR is dedicated to vehicles investing in risk capital. It is designed for private equity and venture capital funds and vehicles investing in alternative assets, including timber, ships, infrastructure, wine. The SICAR is a relatively flexible, regulated structure with the following key legal and regulatory requirements :

- invest in assets representing risk capital,
- have a registered office and a central administration based in Luxembourg,
- the assets of the SICAR must be valued at fair value in the financial statements
- the minimum subscribed share capital of a SICAR amounts to € 1 million which may include share premium.

Furthermore, the SICAR Law does not impose any diversification rules.

A SICAR may thus invest in a single portfolio company, provided the risk capital criteria is met.

## Our approach

Beginning of autumn 2013, KPMG Luxembourg's private equity practice performed an analysis of the SICAR landscape based on annual reports filed with the Registre de Commerce et des Sociétés (RCS), the official list of SICAR published by the Commission de Surveillance du Secteur Financier (CSSF) and other related data.

For some SICARs listed on the official CSSF list, none or incomplete information was available and, therefore, these SICAR were not included in our analysis.

nutshell

Statements  
Partnership  
Limited  
innovative  
Private  
Illustration  
INFO

# Geographical SICAR Equity survey disclosure Financial KPMG glance Luxembourg SCSp

The fund landscape in Luxembourg has emerged almost unchanged since last year. UCITS continue to dominate the sector and variations in the breakdown of other fund types are negligible. The increase in the proportion of non-UCITS funds, which was expected in light of the introduction of the AIFMD and new Limited Partnership, has yet to materialise.

The number of SICAR remained stable with 24 newly authorised structures and 24 SICAR being withdrawn from the official list, mainly due to liquidations.

Private Equity global players continued to use Luxembourg for their deal structuring at the investment portfolio level and less for fund raising through SICAR or other alternative vehicles, such as SIF or preferring offshore fund structures, which in their turn usually use Luxembourg's SPV for acquisitions of investments. This partly explains why SICAR represents only a tiny fraction of the total funds landscape, even among other alternative vehicles in Luxembourg. It remains to be seen how AIFMD will impact this trend.

The partnership limited by shares (SCA) remains by far the most popular legal structure as it stems from the company law, but gives the possibility to General Partners (GP) to retain control of the fund management and limits investors in their right to dismiss the GP. The predecessor of the new special limited partnership form (SCSp), namely simple limited partnership (SCS) failed to attract private equity players looking for a counterpart of anglo-saxon limited partnership (LP) as it had unclear legal features and failed to provide full tax transparency, although it met the contractual freedom principle. We expect to see a slight shift to the newly introduced SCSp in the next year analytics.



Find out [more](#) about the Luxembourg Limited Partnership

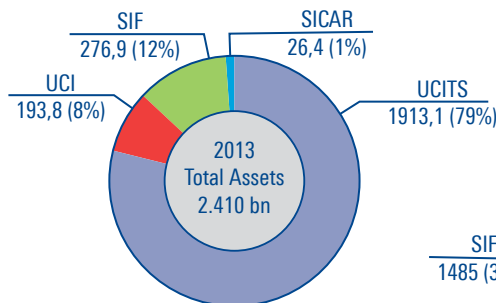
The use of umbrella structures increased by 5% compared to previous year. It appears that the advantages of umbrella structures - including the distinct allocation of costs and the possibility to meet the various needs of several investor groups in the same SICAR - are much appreciated by fund managers.

There is still a clear trend for using multiple share classes in SICAR to accommodate various shareholder classes and related contract terms.

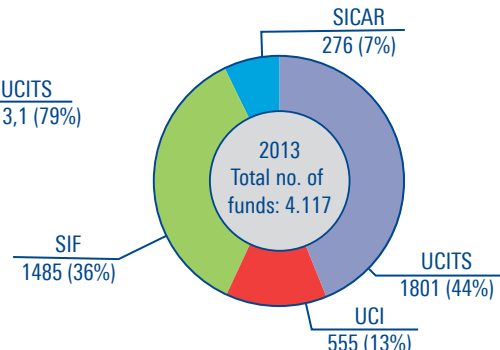


## The Fund Landscape

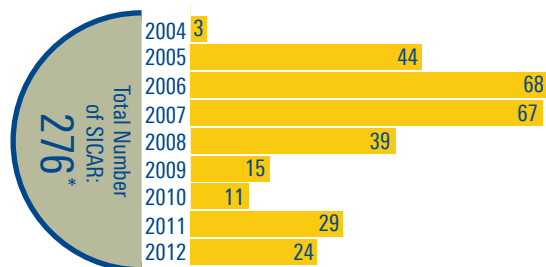
### Total assets in bn EUR



### Number of funds



### Number of SICAR incorporated



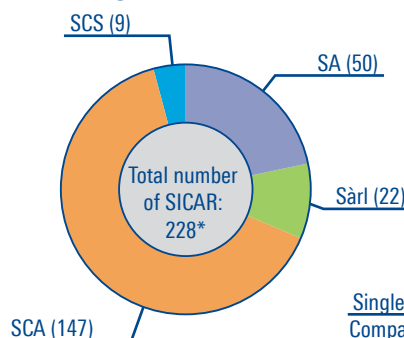
\*According to CSSF data (SICAR's regulator)

## SICAR at a Glance

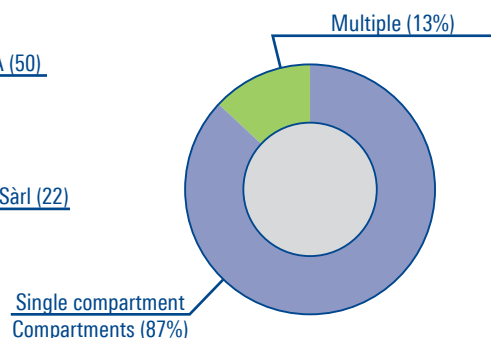
SICAR are quite diverse in terms of legal structures and are mainly dominated by the top 10 players which represent 39% of total assets (PY: 52%).



### Legal Structures

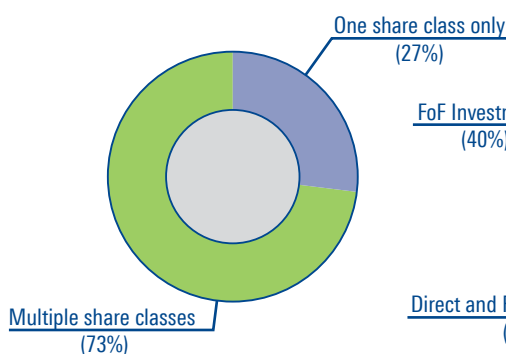


### Umbrella Structures

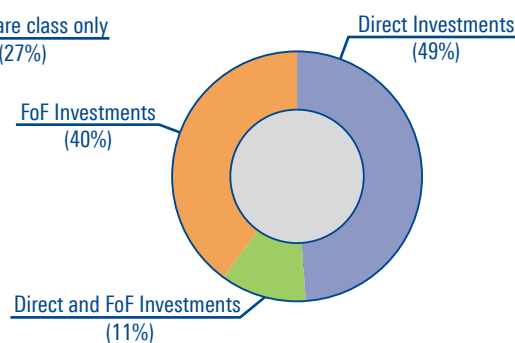


\*For the remaining SICAR, there was no data available in analysed Financial Statements.

### Number of share classes



### Direct portfolio vs. fund investments



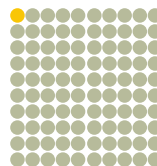


## The Financial Statements

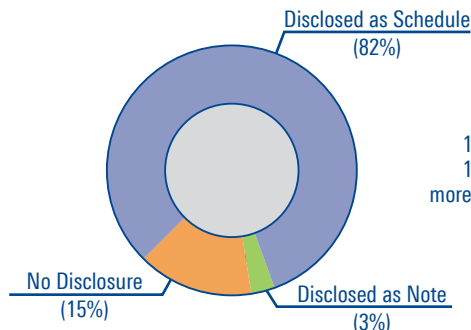
Compared to prior year, the number of SICAR preparing their financial statements under IFRS declined even further from 4 to 2 funds. Lux GAAP prevails as the preferred accounting principles.

The onerous disclosure requirements and complexity linked to IFRS reporting when compared to the Lux GAAP do not facilitate the transition to IFRS reporting in Luxembourg. And this despite the fact that IFRS becomes increasingly popular in Europe due to the globalisation of business and finance and introduction of consolidation relief for investment funds.

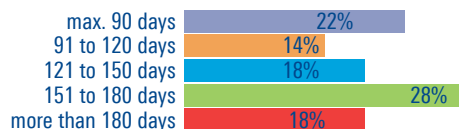
### GAAP



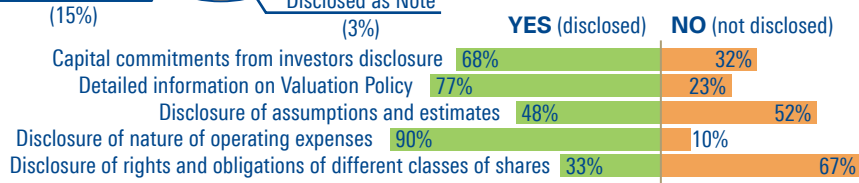
### Investments Disclosure



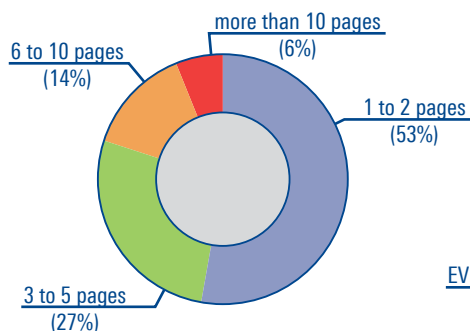
### Time period to issue the annual report



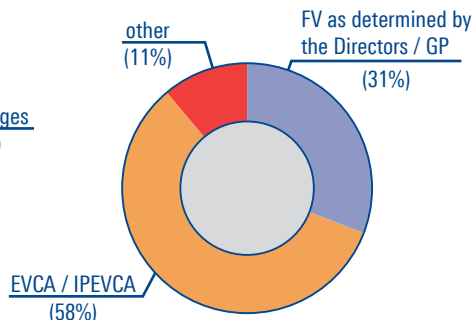
The average time period to issue a report for SICAR improved slightly from 145 to 142 days.



### Size of activity report



### Valuation policy applied



## The market players

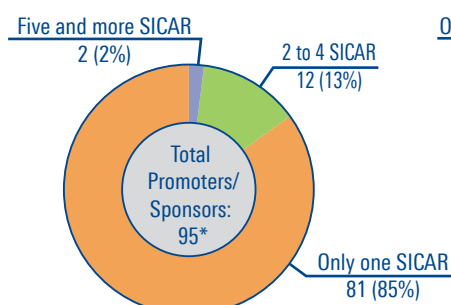
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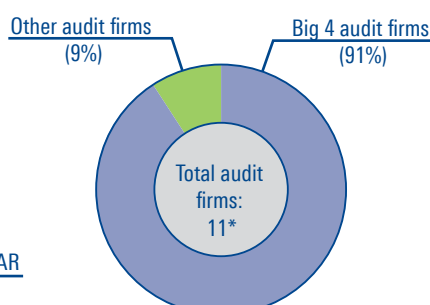
### Disclosure about management and service providers in SICAR FS



### Number of SICAR managed by Promoters / Sponsors



### Audit firms in the SICAR market



\*According to information disclosed in the financial statements of the SICAR analysed.

We noted a positive trend towards a higher level of transparency in annual reports. The most significant improvement was observed with regards to disclosures of investments. The vast majority of annual reports - a whopping 82 percent - depict their SICAR investments in the form of a schedule, allowing readers to follow the development of investments over time. For many other disclosures, an overall improvement was also observed. This includes capital commitments from investors and the disclosures regarding assumptions and estimates.

The time taken to issue annual reports showed no improvement compared to last year. Although the SICAR law requires companies to issue the report within a period of six months - with CSSF fines in place for non-filing and late-filing - the percentage of SICAR filing their reports late remained high.

The length of the activity report did not change significantly compared to previous year. The majority of activity reports was kept very short with 1 to 2 pages, whereas a minority of 6 percent of the reports provided extensive information on more than 10 pages.

No significant changes were reported with regards to applied accounting policy. Whereas around one third of SICAR still report their assets at fair value as determined by Directors or General Partners, the same proportion of SICAR apply the European Private Equity and Venture Capital Association (EVCA) valuation policy.

Compared to last year, there has been a slightly rise to 27 percent in the number of SICAR using a more precise valuation model found in the guidelines issued by the International Private Equity and Venture Capital (IPEV) Board. Only a very small minority apply other valuation policies. A positive development could, however, be noted in the fact that more detailed information is now provided on valuation of the financial statements.

Around two-thirds of SICAR provided such information and, in addition to stating the valuation guidelines they follow, they also included their approach to valuing different asset classes.

Only 40 percent of SICAR investing in funds and not only in direct investments disclosed further information regarding the underlying assets of their investments.



Compare with previous year analysis

# Private Equity: A better new year?

James White, Director in KPMG's Private Equity Global Team shared insights with KPMG Luxembourg's Private Equity team and talks about global PE trends.



**Natacha Oskian «**

» A good place to start is fundraising.  
After years of poor fundraising in a market full of “dry powder” and where exits are rare, is there any positive news on the horizon?

Overall, the PE industry is not yet quite back to full strength following the crisis, but there is more and more evidence that it is bouncing back strongly. 2013 has indeed been the strongest year for fundraising since the financial meltdown and this upward trend seems to be gathering momentum. According to Preqin, fundraising was up substantially in 2013. Over the last six months, there has also been very encouraging fundraising news from big PE Houses such as CVC, Advent and BC Partners all of whom comfortably exceeded their targets in relatively short timescales.

Investor appetite remains strong and levels of dry powder have been falling. An increase in the volume of exits and refinancing has resulted in increasing levels of funds being returned to investors which should allow Limited Partners to recycle allocations, which we expect to translate into higher levels of fundraising. Rising public markets also helped investors make new commitments as fewer became constrained by asset allocation boundaries.

Some PE funds will continue to struggle to raise funds but we expect the fallout to be relatively modest and significantly lower than many had predicted. In fact, very few PE funds are going out of business.





**Marko Körner «**

## » Moving on to deals: what can you say about the recovery of deal activity levels? Do you see any major disparities between different countries or regions?

Deal volumes have picked up considerably, although some markets remain a challenge due to macroeconomic factors. The UK, Northern Europe and Scandinavia in particular are doing pretty well, whereas the recovery in Southern Europe and emerging Europe is a lot patchier due to the challenging local conditions, recession and a decline in bank lending. Generally speaking, levels of dry powder are still substantial, leverage is available and hence deal activity certainly won't be threatened by a shortage of capital. Volumes in fact are more likely to be constrained by deal supply issues.

I think an interesting contrast is the US where absent the Euro zone macroeconomic issues recovery in deal volumes has been stronger than in Europe, with activity levels now approaching pre-crisis levels at least in terms of numbers of deals rather than capital deployed. This should give people confidence that the PE model as a whole is not broken and has proved more resilient than some doubters predicted.

There are other positive signs out there: we are seeing the debt markets come back strongly, Collateralised Debt Obligation (CDO) funds are being raised and even the European high-yield market, which never really took off before the crisis, is now a substantial provider of funds particularly in the upper mid market and large buyout sectors. I feel the sentiment within the PE market generally is pretty bullish overall.

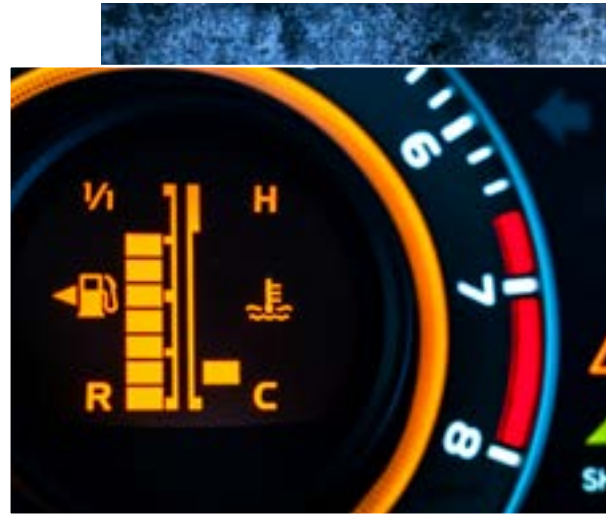
**Natacha Oskian «**

## » What can you say about exits and performance?

Exits have picked up very strongly, with 2013 having the highest level of exits since the global financial crisis and the funds returned from these exits are now being recycled into new fundraising. Strong current refinancing activity is also allowing further returns of capital to investors via dividend recapitalizations

Another factor driving healthy exit levels was generally improved corporate valuations: for the past 12 months or so, there has no longer been such a mismatch in price expectation between sellers and buyers as was arguable the case during the difficult years post 2008.

In addition we are seeing many exits structured as secondary buyouts, thus providing GPs with further investment opportunities.





**Marko Körner «**

**>> Talking about valuation and performance, a lot of NAVs were quite severely written down during the crisis. How did this affect market and investor confidence?**

A good illustration to answer your question would be discounts we have seen in the secondary PE market to NAV - i.e. the trading of existing fund commitments and positions. These were quite substantial during and after the financial crisis, as sellers had a variety of problems which forced them to exit into a market with very little demand. This clearly affected confidence in the LP community and consequently made fundraising very difficult. However, we now see that the secondary market has very substantially recovered and now discounts are at a very low level.

Over the last financial year, PE NAV valuations have recovered well, as evidenced in earnings reports and stock prices from the large US listed PE houses (KKR, Blackstone, Carlyle) and similarly those in the UK (SVG, 3i).

It should also be borne in mind that NAVs are 'paper' valuations and that at the fund level GPs are rarely forced sellers. Hence while in the short term PE may underperform compared to other markets based on these valuations, it has a proven track record of out-performing over longer periods and through economic cycles as ultimately PE performance is measured on a cash invested versus cash realized basis. All this, I think, is actually helping to renew investor confidence in this asset class going forward.

**Natacha Oskian «**

**>> Let's talk about what is happening in emerging markets and "the next place to be" in terms of new markets for private equity?**

If we look back 10 years or so, we saw quite low levels of funds being channelled into emerging markets. This allocation level is now approaching 20% and emerging markets have become a fairly important area for global private equity players. We have not only seen renewed interest from international funds, but also rapid development of domestic funds.

New markets have also attracted attention, notably Africa, which mainly appeals to PE houses that already invest in other emerging markets. This shift is partially driven by growing caution about some more established emerging markets. China and India in particular pose problems. Some GPs and LPs believe they may have put too many eggs in these baskets, as problems in exiting minority positions due to market conditions making IPO's difficult, have left investors with too many unrealized positions.



**Marko Körner «**

## » How is the PE operating model now evolving, particularly in terms of investments in OECD economies?

Generally, the OECD economies have got debt and liquidity issues and most economists are predicting a period of relatively low growth rates. Given the lower macro economic growth, PE will have to adapt its operating model to likely lower (if any) arbitrage returns. This suggests that there will be a greater focus on adding value through increasing earnings in underlying portfolio companies and therefore greater levels of intervention in the portfolio will be needed.

PE will likely need to rebalance its skill set to take best advantage of these new circumstances calling on people who are familiar with running companies and have operational and change management experience. Many GPs have already been doing just this as we are seeing more 'special advisers', 'portfolio managers' and 'industrial partners'.



Natacha Oskian

Private Equity, Marketing, Innovation and Communication



Marko Körner

Private Equity, Audit

# IFRS 13 – Valuation

By David Nordlund



Private equity managers generally claim to be in the best position to value their investments, due to the access they have to private information about portfolio companies. Now, however, those reporting under IFRS will have to assess how others would value their investments too.

Fair value under IFRS 13 is defined as “the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date”. From the perspective of a private equity fund, this is the price at which the fund could exit its investment or transfer its liability.

Exit price

Orderly transaction

Market participants

Measurement date

**Exit price** While exit price is easy enough to define when there has been an actual transaction, private equity funds will generally have to apply a valuation technique.

**Orderly transaction** Circumstances that may indicate that a transaction is not orderly can be the following:

- The seller is in distress;
- The seller is forced to sell to meet legal or regulatory requirements;
- The seller marketed the asset to a single market participant or there was otherwise inadequate exposure to the market to allow usual and customary marketing activities.

**Valuation techniques** IFRS 13 does not prescribe a specific valuation technique to arrive at fair value unless there is a quoted price in an active market for an identical asset or liability. The standard does, however, refer to valuation approaches such as market approach and income approach which can be applied separately or in combination.

Some of the principal characteristics of a valuation technique are:

- It is commonly used by market participants;
- It is consistent with accepted economic methodologies and techniques;
- It uses input that market participants would usually take into consideration; and
- It maximizes the use of observable data.

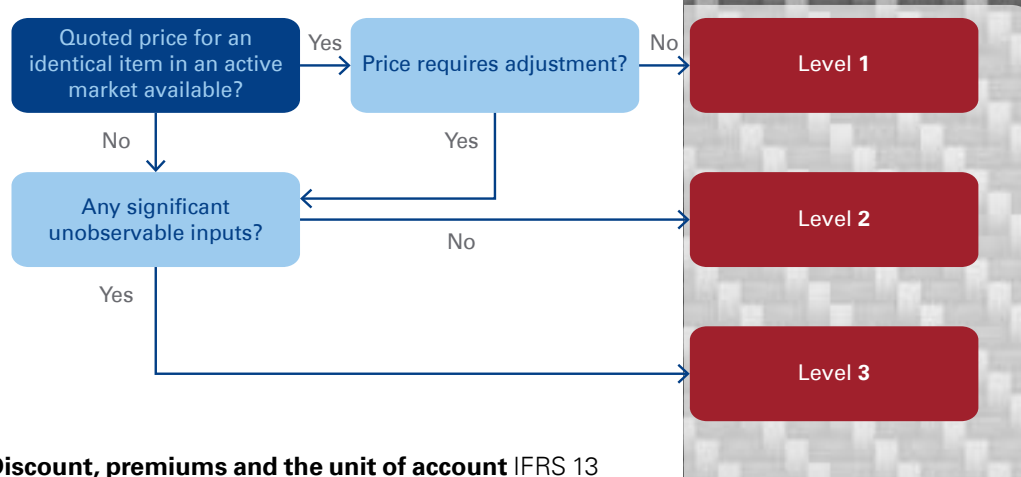
Two of the most common techniques for valuing private equity investments are referencing to comparable companies and discounted cash flows, which are clear examples of market and income approaches, respectively. Other frequently used valuation techniques include comparable transactions, which in the world of private equity often turns out to be a refinancing round or co-investor dealing for strategic purposes. Under these circumstances, it is not clear whether the transaction price represents fair value under IFRS 13, for several reasons:



- the transaction may not have been orderly because the seller sold to a related party acting on strategic considerations with regards to existing investments.
- the asset sold may have been offered only to a limited number of market participants who already have an interest in the investment.
- the comparable transaction price may no longer reflect fair value at measurement date, even if it did so at the transaction date.

Many private equity managers would apply a number of valuation techniques which would produce different outcomes for their valuation. While it is best practice to cross check the outcome between different valuation techniques, it cannot be assumed that the fair value is the arithmetical average of the outcomes. Judgment should be applied.

#### Fair value hierarchies



**Discount, premiums and the unit of account** IFRS 13 defines unit of account as “the level at which an asset or liability is aggregated or disaggregated in an IFRS for recognition purposes”. This means that the unit of account will determine what is measured and not the other way round. As a comparison, the unit of account for an equity investment in a listed and actively traded company would typically be one share, as this is the unit in which the investment is traded and valued by market participants.

In private equity, however, single shares are rarely tradable or considered to be a meaningful unit for valuing an investment. This matters because, under IFRS 13, discounts and premiums that reflect characteristics of the holding - such as size and controlling stakes, rather than characteristics of the asset or liability itself - are not permitted in a fair value measurement. Now some argue that the unit of account for certain private equity investments is the entire holding as it is considered unlikely that any market participant would ever consider buying a fraction of it. From this argument it follows that if the unit of account is the entire holding characteristics of that holding are also characteristics of the asset or liability in its unit of account. This question is currently under debate and the last word has surely not been said yet.



You can follow some of the developments on the IASB's website:

<http://www.ifrs.org/Current-Projects/IASB-Projects/FVM-unit-of-account/Pages/FVM-unit-of-account.aspx>

Please visit KPMG Luxembourg's IFRS institute for further reading and to subscribe to our newsletter:

<http://www.kpmg.com/lu/en/topics/luxembourgifrsinsights/pages/default.aspx>

# Squeezing more out of valuation

By Yves Courtois



Up until now, PE houses have handled their portfolio valuations with some degree of discretion, navigating in the grey zone between quoted comparables and sometimes longer term approaches to value. The vast majority opted for a customized approach, with models that they carefully crafted over time to suit their business and the needs of stakeholders. The AIFM Directive has somewhat changed this by introducing stricter rules on reporting, including stringent requirements on the underlying valuation process.

As a result, PE houses are finding themselves pondering the same question: how can one segregate the valuation function from portfolio management without seeing costs spiral upwards?

## Out with outsourcing

Outsourcing valuation has long been unthinkable for the industry, since valuation lies at the core of performance reporting and GPs want to keep their grip on this process. With their in-depth knowledge of portfolio companies and custom of using bespoke calculations, PE managers have – quite justifiably – eschewed this option, as well as the cookie cutter approach offered by software vendors. Although a shift in mindset will be needed for the new regulatory era, there are alternatives out there which can be considered by those wishing to avoid costly options such as outsourcing. The name of the game will be making sufficient efficiency improvements to find a healthy balance between the old way and the new rules.

## Putting the GP first



Increasingly, we're being asked to cast an independent eye on the valuation process of companies who are struggling to bring greater operational efficiency without sacrificing quality. In close collaboration with PE managers, we've had to develop new ways of achieving their goals. Our collaboration is bearing fruit in the form of a solution that automates valuation using Visual Basic Excel programming as well as external financial data sources which can plug into it.

The beauty of this approach is that the model can be tailored according to the existing cash flow streams that each GP receives. Every manager is different, so we work with them to understand, in terms of output, what type of value drivers they want to use and what type of information they want to release. Whereas in a traditional approach to value, 80% of time may be spent on data collection,

formatting the results and the rest being spent on analysis; our re-engineering of the valuation process using technology leads to the reverse being true.

While the GP lies at the heart of this approach, the end goal is achieving efficiency. It's important to be consistent across the entire portfolio and standardize the approach implemented. By taking a holistic view, costs are pushed down and efficiency achieved without jeopardizing the quality of the output. Even when we perform valuation reviews, this re-engineered approach to value leads to significant efficiencies.



# PE on the blog & Social Media



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## The nitty-gritty of valuation and risk management under AIFMD

By Sven Mueller-Brock on 15. 01. 2014

Finding an innovative, comprehensive and coherent risk management approach is far from easy under AIFMD. A risk model that can be applied across all asset classes – from PE to RE to Hedge funds and MF funds – is very difficult to hit upon. As AIFs get busy implementing their Risk Management and Valuation processes in line with the AIFMD requirements, we have put together our very own KPMG overview of these two key areas of the directive to help them on their way.

## AIFMD applications – breaking news

By Natalie Orlan on 29. 11. 2013

Since writing about how to approach the AIFMD application last week, we have held our annual fund conference for German speakers which a representative of the CSSF attended as speaker. The CSSF gave an update on where Luxembourg stands with regards to AIFMD applications. Here's a quick round-up of the main statistics:

## Are you filling in your AIFMD application file? Read this

By Klem Navard on 20. 11. 2013

Way back in March, we received a first request to put together an AIFMD application file. There was no implementation law in Luxembourg, no application form, no FAQs – it was a little like trying to put up IKEA furniture without the instructions. Fortunately, things today is a whole lot easier.

## At last, lobbying

By Thierry Ravasio on 15. 10. 2013

On 1 October, ESMA obligations and the Pr collective sigh of relief.





39 Kennedy Avenue

About this blog

KPMG's leadership blog brings you insight, opinion and debate from our business and industry experts. We'll be discussing the issues that matter to your business and the trends that could shape your future decision making.

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# Investor Reporting

By David Nordlund and Laurence Vivarie



## Overview of Monitoring process

**Due diligence process**



**Monitoring process**

**Exit strategy**

## Investor Reporting – what is it for?

Most private equity funds issue audited financial statements once a year; some also produce semi-annual financial statements. This is naturally an important source of information for investors, however most of them would not consider the information detailed or frequent enough to effectively monitor their investments. Having invested substantial amounts, investors expect to receive information allowing them to assess the investments' performance and also build their expectations for the future.

Importantly for private equity houses, investors are likely to use the reporting they receive to judge the managers' performance and decide whether to invest – or not- in later vintages raised by the manager.

## Content of reporting

In order to monitor both the performance of their investments as well as the performance of the manager to whom they have confided their money, investors will need to know both what is happening to the investment and what control the manager has over the investment. Both

the International Private Equity and Venture Capital Association ("IPEV") [www.privateequityvaluation.com](http://www.privateequityvaluation.com) and the Institutional Limited Partners Association ("ILPA") [www.ilpa.org](http://www.ilpa.org) have issued comprehensive guidelines and best practices in the field of investor reporting. The main financial indicators therein will surprise no one. Both organizations, in one form or another, include cash flow statements, net IRR, portfolio company updates and investor capital account statements in the information that investors should expect to receive at least quarterly.



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## How to know if reporting is reliable?

Professional private equity investors will generally have defined monitoring activities which will include tracking missing data but may also include back testing of earlier provisions or estimates received. Over time, some investors will also benchmark their different investments against each other or against an index or other market data. This serves the dual purpose of identifying outliers, which could indicate that the data is not completely comparable, and as a means to spot over and under performance among the managers available. But numbers are not everything. The view gained by analyzing figures should be confronted with the information the investor collects from interacting with the manager. Signals that all is not well can be when there is an un-announced exit from an investment or unexplained changes to the assumptions on which the valuation had previously been based.

## Purpose of investor reporting monitoring

### **Compliance with the overall investment strategy:**

- Check any development in terms of return, risk profile and liquidity needs
- Is that in line with due diligence expectations and deal promises?

### **Fair valuation tracking:**

- Compliance with EVCA fair valuation guidelines
- Detection of potential impairment in due time

### **Board seats:**

- Demonstrate you know what happens when it is time to decide.

## Risk management monitoring

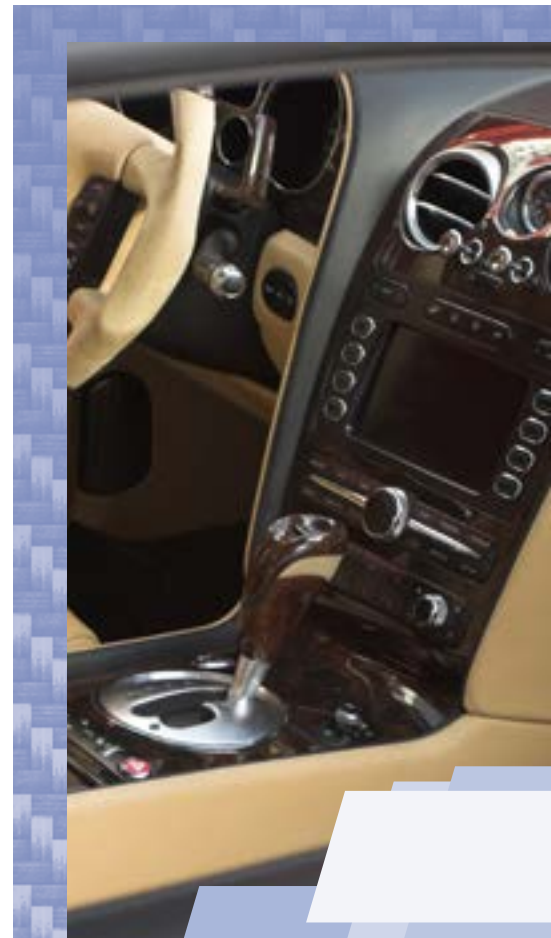
Analyzing investor reporting may be perceived as an administrative burden once the deal is done, the due diligence process being often the key exciting step and the exit, the final one.

This is indeed time-consuming work and requires staff experienced in equity business and its specific risks.

In practice, receiving reports on a quarterly basis and analyzing them are part of the regular risk management monitoring activities.

It's true this could become a challenge depending on the size of the overall investment portfolio. It means in a few words at least:

- Anticipate information reporting you want to receive (content, frequency and deadlines of reporting) during due diligence and fix it in the final agreement;
- Deploy a monitoring policy and procedure supporting a strong control environment from data collection to control archiving and data conservation;
- Collect data & track missing reporting;
- Inspect data on a timely basis;
- Identify key events/adverse events among available information, relevant to the investor;
- Corroborate understanding thanks to coordination with front managers / Board attendance, direct contacts to investment managers/general partner of underlying funds;
- Evaluate any significant financial impact and adapt your investment decision.



## Optimizing review & think “risk-based approach” for a timely action

The monitoring process should remain efficient whatever the size of the overall portfolio otherwise it will become useless.

The monitoring does not need to be systematic for each investment. It would need to be systematic if any material issue affecting some investments could

significantly impact the overall portfolio considering risk mitigating tools used at investor level - for instance diversification (country, sector, vintage).

It requires a strong understanding of the overall portfolio & related risks. It may be then more appropriate to determine a watch list of the most risky investments for which the investment monitoring would be enhanced and overall results available at a glance and stored.

You may also consider the investment period of the investment and adapt the frequency of monitoring accordingly: the risk profile is usually more important during the investment period of the underlying investment.

It should be remembered that the use of investor reporting is one component of the monitoring process: regular visits to fund managers as well as attendance of BoD/AGM are key to correctly interpret or corroborate the analysis made based on investor reporting.

## Q3 reporting is key but tracking events is a continuous process

From an accounting perspective, year-end process often relies on Q3 reporting (adjusted for Q4 cash flows) since Q4 reporting is usually not yet available at the time the accounting records are booked and the final audit ends.

Any Q3 subsequent event that could impact the financial position and performance of the funds should be identified quickly and reported to auditors as part of their subsequent events procedures.

Anticipation is required to instruct underlying fund managers/target investments that any material events should be reported in a shorter timeframe compared to the usual reporting.

Some private equity houses require their team to get in touch with those who report to capture proactively the latest news. The others mainly focus on strong back testing procedure. Following the outcome, they will adapt their monitoring approach for the following year.

## Information analysis

Basic monitoring usually pertains to NAV tracking. However other material events being either adverse signals or indicators of good performance should be further analyzed.





Here are examples of areas of focus:



To ensure the capture of any key indicators, investor reporting should be tailored accordingly following investor specific instructions.

The impact of detected events should be assessed at overall portfolio level.

In addition the analysis of the investor reporting should be made on time to ensure a prompt reactivity, noting that the investor reporting is usually made available 2 months after the period end.

The objective of the overall monitoring process should be first to quickly get relevant and treatable data in order to spend more time in analyzing the potential impact on the overall portfolio. Private equity houses are now developing tools to make this possible.

### What next?

While the demand for more frequent, more detailed, more recent and higher quality investor reporting is unlikely to ebb out, it is likely that this will increase the adoption of standards and guidelines. Not always because they may improve quality but because it reduces the re-working of data communicated to investors – and that both on the manager and investor side of things.

One recent initiative to reduce manual data checking is [Altexchange](#) which is a data validation platform. It neither stores nor distributes data but allows fund managers to submit files to a validation engine which checks for data completeness and, if successful, will emit a validation certificate.

Furthing reading on investor reporting:

[Altexchange](#)

[ILPA Best Practices](#)

[ILPA Standardized Reporting Templates](#)



# ESMA issues guidelines on reporting obligations under AIFMD

By Kian Navid and Mickael Tabart



On 1 October 2013, ESMA published its final guidelines on reporting obligations under AIFMD. Since this date, recent communications from the CSSF – namely circular 14/581 and newly released updates to the AIFMD FAQs, 10 January 2014 – have shed light on reporting obligations providing much needed clarity for those embarking on the reporting journey.

Reporting requirements are expected to be one of the main cost drivers for AIFMs as the Directive requires fund managers to report extensive amounts of information to the regulators.

## Next big step for Alternative Investment Fund Managers

The comprehensive data analysis requires AIFMs to fill in data fields which are the sum of hundreds of other different data fields. Most of the fields require dynamic data which is likely to change for each reporting period, such as the net asset value or risk measures. With the recently published [CSSF update](#), even additional fields – such as the VaR, the Vega exposure and the portfolio's sensitivity to a change in FX rates or commodity prices – will be required when relevant, in line with proposals from ESMA's opinion on this topic.

But the complexity will come in knowing exactly what data to collect as AIFMs will have to look outside the traditional fund accounting system if they are to amass all the data necessary for report production. Broker, collateral and risk management figures are just three of many possible examples of data requirements. Further layers of complexity sum up when it comes to compiling this information: Where is the data located? In-house or with external parties? Is there data missing? Who will be responsible for sourcing it?

In a recent survey conducted by KPMG on the use of Data and Analytics - [Going Beyond the Data – Achieving actionable insights from data & analytics](#) - it was noted that many organizations are still struggling with key components of becoming a data and insight-driven organization.

## First reporting date to National Competent Authorities

Following strong criticism from the industry, ESMA has taken a more flexible approach to the phasing in of AIFMD reporting than it its previous communication on this topic. ESMA now suggests that when determining the timing of their reporting obligations, AIFMs should take into account certain factors, such as their authorisation status.

In recent updates to its [FAQs](#), the CSSF chose to adopt ESMA's guidelines on this subject. This means that an AIFM authorized on 15 February of a given year with a quarterly reporting obligation has to submit its first reporting covering the period of 1 April to 30 June on 31 July of that given year at latest, then the AIFMs will have to prepare the reports for each AIFs in either quarterly, half-yearly or annually depending on factors such as the assets under management or value of the AIFM



and submit it to the NCA no longer than 30 calendar days (45 days for fund of funds) after the end of the reporting period.

### Insourcing or outsourcing?

Reporting is more complex than simple data collection and mapping. AIFMs must either develop (costly) internal data control processes to verify the completeness, consistency and accuracy of the data or outsource this task to specialized service providers.

As not all AIFMs business models are the same, an AIFMD reporting solution will require developing a high level of expertise in linking data from different databases and building complex data models. This all requires a deep understanding of the requirements combined with significant IT intelligence.

With extensive experience now under our belt insourcing the entire reporting process for KPMG clients, KPMG Luxembourg has built a full AIFMD reporting solution that could be tailored to AIFMs' size and volume of reporting required.

### AIFMD reporting, the first step towards fully integrated data reporting?

This could also be an opportunity for many organizations to move to a fully embedded Data and Analytics strategy. This can be done by using the data gathered for regulatory reporting to create internal reporting for management and also for investor reporting purposes, thus creating value for the industry.

To stay up to date with the latest AIFMD developments, visit <http://blog.kpmg.lu/tag/aif/>





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# Spotlight on Jane Wilkinson and the ESG agenda for PE

By Sarah Brook

Jane Wilkinson is an audit partner in our private equity team, but she is also passionate about sustainability and why it is good for private equity.

## » What is it that you like about Private Equity?

Looking into target investment development is a really interesting side to working in PE. Our clients bring so much to their investments and, as a result, these companies develop over time and we're able to follow their progression. In this development process lies an opportunity for PE houses to effect a positive influence on their target companies, by encouraging them to implement the Environment, Social and Governance (ESG) agenda. Those who position themselves ahead of the game by looking at subtle non-financial risks and opportunities have the potential to create real added value for both portfolio companies and their limited partners.

## » Why is it important for PE houses to address non-financial risks? How can this add value to the investment?

By ignoring factors with a less obvious direct financial impact on the target company – areas such as long term raw materials supply, corruption risk, human rights violations - unexplored risks can evolve into potentially significant risks with an impact on both value and reputation. On the flipside, many businesses are now seeing opportunities through in-depth ESG analyses, boosting value creation.

## » How far have businesses come in terms of integrating ESG into their operating model?

For most businesses, this process begins with taking a look at internal practices and policies: making donations to charity, CO2 emissions in the office, recycling, switching off lights. This is nice, however it is not the real issue. A large proportion could use their influence by imposing appropriate responsible business practices on target and portfolio companies.

## » Do any tools exist for PE houses looking to implement ESG?

For those wishing to evolve, guidance can be found in documents like the UN Principles of Responsible Investing. The second principle "We will be active owners and incorporate ESG issues into our ownership policies and practices" relates to encouraging others where you have an influence: this is what I see as the main role and challenge for PE houses. Up until now, the best PE dealmakers don't necessarily have the same level of experience with certain ESG issues as





they do with everyday business. They need to surround themselves with the best people, ensuring the right experts are at hand.

## »» Is there a future for the ESG agenda in PE?

We have come a long way so far with sustainability, but I am still rather disappointed that ESG isn't an integral part of the very fabric of what we do. Nonetheless, there has been increased recognition by PE houses of the vital role it should play. This recognition, in fact, can also be observed in the wider fund industry. If the upward trend continues, I'm confident that our goal of seeing ESG integrated across the board will one day be realised. I just hope that this day will come sooner rather than later!

## »» What do you enjoy the most about working at KPMG?

As you may have guessed, sustainability is a favourite topic of mine. I'm also responsible for CSR and being able to work for a firm which takes its responsibilities towards society seriously and gives opportunities for staff to contribute is really rewarding. I'm particularly proud of our work with our staff selected charity Alupse, a local organization which works with families affected by child abuse. My advisory colleagues have been working to refine and reinforce Alupse's strategy to ensure the long-term growth of the association. It's nice to see a team of staff paint a children's home, however it's even more gratifying when we can put our real professional expertise to work where it matters.

## »» If you were able to change one thing about Luxembourg, what would it be?

I'm a true English girl at heart and there is nothing like fish and chips. When will we get a real fish and chip shop here in Luxembourg?

**Future of corporate reporting**  
Wednesday, 26 February 2014  
at 4.30pm  
Chamber of Commerce  
7, rue Alcide de Gasperi  
Luxembourg-Kirchberg  
[REGISTER NOW >>](#)

### **The next step**

We'll be holding an event on 26 February 2014 with Mark Vaessen – member of the European Financial Reporting Advisory Group Supervisory Board and global IFRS leader at KPMG – to look at why Integrated Reporting is here to last.

We have reserved a limited number of places at the event for our Mook readers. To be in with a chance of filling a seat, register your interest in attending by emailing [events@kpmg.lu](mailto:events@kpmg.lu). The lucky few will be notified by email.



# Interest for Limited Partnerships ignited in the States

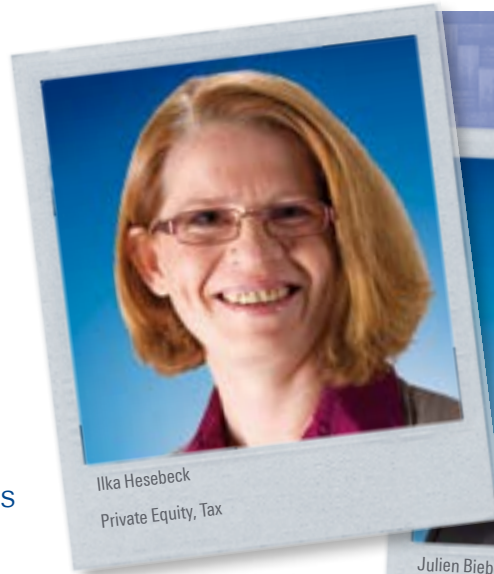
By Ilka Hesebeck & Julien Bieber

Private Equity in Luxembourg and Europe has seen some significant changes over the past year and this hasn't gone unnoticed across the Atlantic. AIFMD is still making waves with US PE houses as they struggle to grasp who's in and who's out, however, there's a new contender for America's attention.

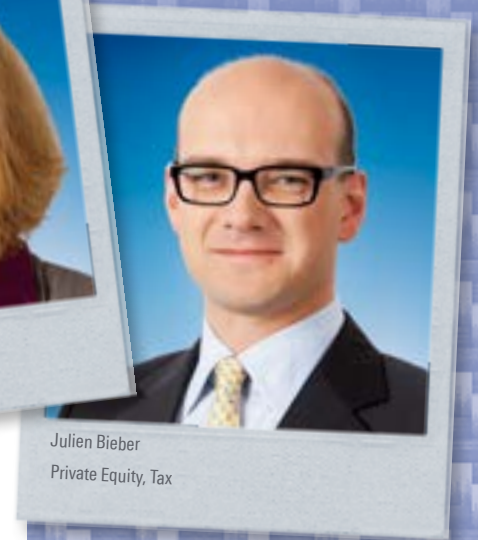
At a recent KPMG roadshow, it was the new Luxembourg Limited Partnership which caused a splash with PE managers stateside.

To capitalise on the new developments, a KPMG Luxembourg delegation led by Ilka Hesebeck and Julien Bieber set out to the US to conduct a roadshow on what Luxembourg has to offer for the US PE industry. The roadshow was addressed to a wide audience, including those who have yet to discover Luxembourg's assets, as well as existing clients and our tax network in the US. Although the agenda was full, the Luxembourg Limited Partnership took centre stage, drawing the attention of Private Equity houses and advisors seduced by this new vehicle for fundraising, acquisition and financing. For many, the LP brings with it the possibility to strengthen the economic substance that many Private Equity houses have built up in Luxembourg over the years.

The new Luxembourg Limited Partnership was also deemed to be attractive in the context of another growing trend; the on-shoring of the industry following the entry into force of the European Alternative Investment Fund Managers Directive. US PE houses who plan to raise funds from European investors may choose Luxembourg as the best suited gateway to domicile funds thanks to the opportunities offered by the LP. 2015 will be another key milestone for US Managers as they will have to choose a country of reference. So, why not Luxembourg?



Ilka Hesebeck  
Private Equity, Tax



Julien Bieber  
Private Equity, Tax



Ilka in the park in New York between two meetings



Julien admiring the skyscrapers in Chicago between presentations



# Must read in the Alps

## Relevant KPMG publications



Made in Luxembourg:  
Limited Partnership



MOOK edition  
Spring/Summer 2013



AIFMD  
Re-shaping for the future



AIFMD  
Beware the tax impacts



AIFMD  
e\*Book



Illustrative Annual Report  
for SICAR (Lux GAAP)



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AIFMD applications  
Breaking news  
(Natacha Oskian)



Are you filling in your  
AIFMD application file?  
Read this  
(Kian Navid)



The global megatrend  
for 2030 that is a reality  
for Luxembourg in 2014  
(Patrick Wies)

# Providing a simpler answer to complex training requirements

Global PE Houses face an increasingly complex accounting environment. Operations across the world and Mergers & Acquisition opportunities in new markets bring regulatory and implementation risks that span multiple jurisdictions. As global accounting standards evolve and operations grow, organizations need to develop the knowledge and skills to succeed—now and in the future.

The KPMG Luxembourg Private Equity team (KPMG) addresses this new and more complicated environment. KPMG's training programs help put organizations and their professionals in a position to understand, adapt, and even benefit from global accounting and regulatory changes on both global and local scales.

## The topics that matter most to you

Our suite of course offerings helps prepare PE companies for major changes that could have significant accounting and reporting implications. Below are a sample of the types of courses that KPMG can offer your organization and its people:

### PE fundamentals

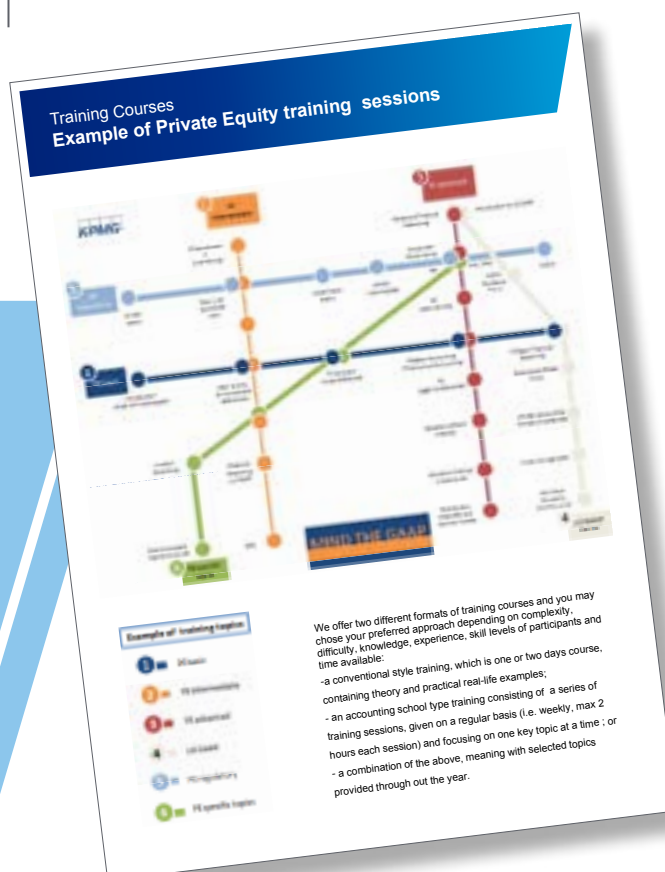
- PE lifecycle & terminology
- Roles & Responsibilities (GP, LP, ...)
- Processes & Controls

### PE in Luxembourg

- Luxembourg investment vehicles
- Reference laws & regulations
- Tax environment & Tax optimization

### Accounting and reporting

- Complex transactions and various or new accounting rules and principles
- Comparison of Lux GAAP, IFRS and US GAAP for PE
- Valuation of investments



## Customized Training

- Instructional designers will consult on training goals to develop customized language, examples, exercises, and activities
- KPMG will work with you to design an approach that blends instructional methods that can deliver the results you are seeking in your business culture
- Webcasts and Web-based self-studies can be combined with a traditional classroom approach using on-the-job tools.

### For more information

For more information on how KPMG's Training Solutions offerings can help your organization meet its global and local training needs including course content, customized training, or general inquiries, please contact [lu-fmtraining@kpmg.lu](mailto:lu-fmtraining@kpmg.lu).

## KPMG Training — an industry-wide reputation

The accounting profession's high regard for KPMG's training curriculum is a constant amid a rapidly changing business and regulatory environment. KPMG has been providing high quality, effective executive training and continuing education for more than 20 years.

At KPMG all professionals working on PE have received this dedicated PE training to ensure you receive high quality service from our tax, audit and advisory PE team.

# Sound bites

**"2013 has indeed been the strongest year for fundraising since the financial meltdown and this upward trend seems to be gathering momentum"**

James White

**Private Equity: A better new year?**



**"PE houses are finding themselves pondering the same question: how to segregate the valuation function from portfolio management without seeing costs spiral upwards?"**

Yves Courtois

**Squeezing more out of valuation**



**"Those who position themselves ahead of the game by also looking at non-financial risks have the potential to generate real added value"**

Jane Wilkinson

**Spotlight on Jane Wilkinson**



**"The LP brings with it the possibility to strengthen the economic substance that many Private Equity houses have built up in Luxembourg over the years."**

David Nordlund

**PE Investor Reporting**



**"A number of factors come into play this year which will push PE houses to rethink reporting and overhaul practices."**

Thierry Ravasio

**Say hello to improved reporting**







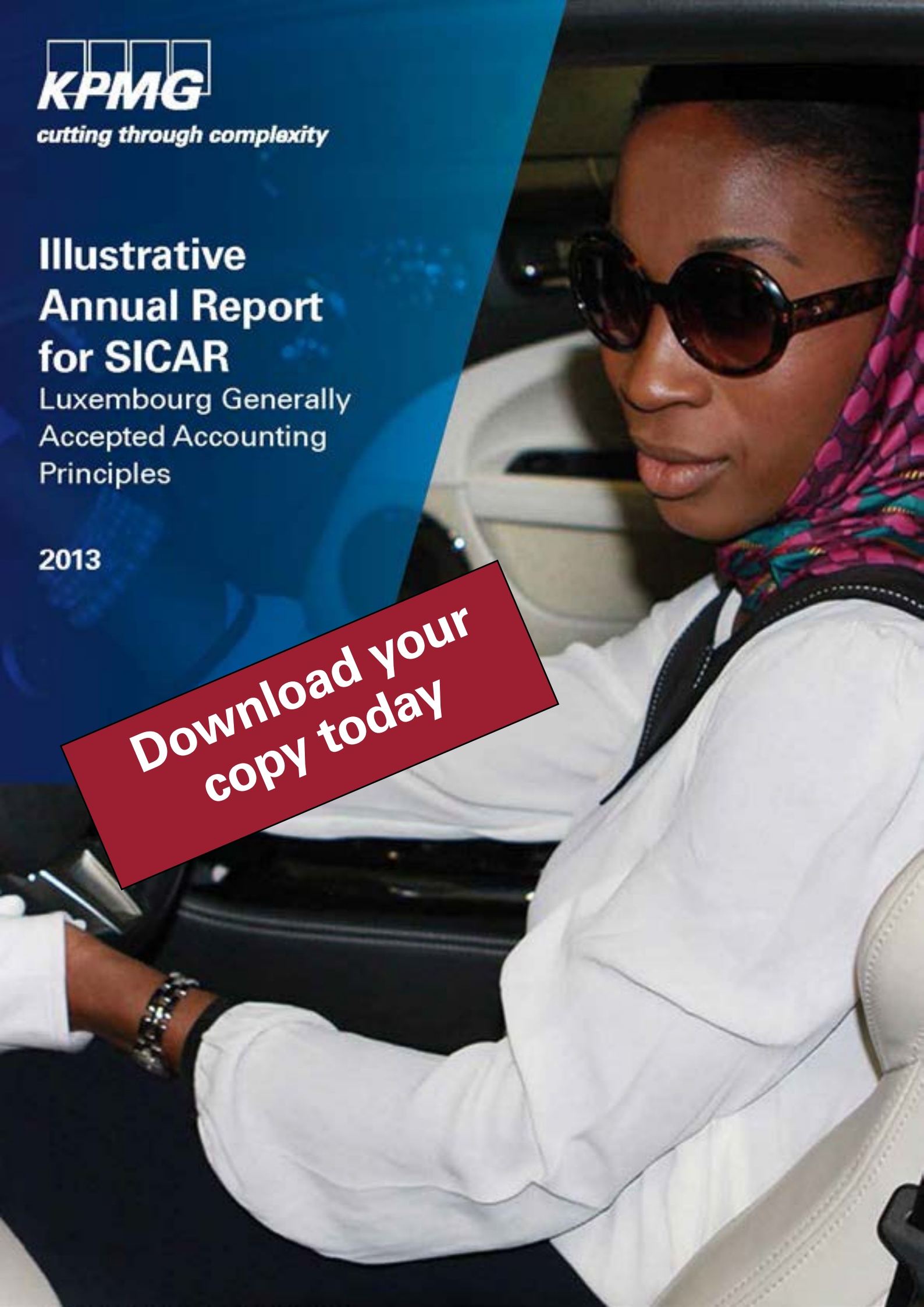
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