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VARIABLE CAPITAL COMPANY

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The Variable Capital Companies ("**VCC**" or "**SVCC**") framework was officially launched by the Monetary Authority of Singapore ("**MAS**") and the Accounting and Corporate Regulatory Authority (**ACRA**) on 15 January 2020. A total of 20 investment funds were either newly incorporated or re-domiciled as VCCs in Singapore. As the legal adviser to one of the 18 fund managers selected by the MAS to be part of its VCC pilot programme, this article provides an overview of the VCC framework as well as details some of our current thoughts on the VCC framework.

INTRODUCTION

The VCC is a new Singapore corporate structure that can be utilised for all types of collective investment schemes in Singapore, be it closed-end funds (typically venture capital funds and private equity funds) or open-ended funds (typically mutual funds and hedge funds), and a VCC can be structured either as a single standalone fund or an umbrella fund. A VCC can also have a single shareholder and therefore be utilised in master-feeder structures or a single family office managed by a licensed or registered fund manager or exempted financial institution.

Structurally similar variants of the VCC exist in other jurisdictions, such as open-ended investment companies in the United Kingdom, société d'investissement à capital variable in Luxembourg, segregated portfolio companies in the Cayman Islands and the British Virgin Islands, open-ended fund companies in Hong Kong and cell companies in Guernsey and Jersey.

SALIENT FEATURES OF THE VCC

The VCC has the following salient features:

(a) Each sub-fund of an umbrella VCC operates as a cell in which its assets and liabilities are segregated and ring-fenced from those of the other sub-funds.

(b) An umbrella VCC and its sub-funds are a single legal entity. As such, unlike a fund setup that utilises special purpose vehicles, the board of directors, administrative, accounting, compliance and other functions of a VCC can be centralised at the umbrella fund level, which provides for greater economies of scale and cost savings. For example, an umbrella VCC is only required to submit a single income tax return to ACRA, regardless of the number of sub-funds that it has[1].

(c) VCCs may issue shares and redeem fully-paid (and not unpaid) shares without the need for shareholders' approval and no solvency tests are required[2]. This lowers administrative costs, facilitates seamless movement of capital and enhances the efficiency of an investment fund structured as a VCC.

(d) VCCs can pay dividends out of capital[3]. In this connection, it is provided in the Variable Capital Companies Act 2018 (No. 44 of 2018) (the "**VCC Act**") that the value of the paid-up capital of a VCC is at all times deemed to be equal to the net asset value of the VCC.

(e) The register of members, constitution and financial statements of a VCC are not required to be made available for public inspection, thus offering privacy to investors.

(f) Financial statements can be prepared using a range of accounting standards, instead of only the Singapore Financial Reporting Standards. See the section titled "*Accounting*" for further details.

THE VCC ACT

VCCs are regulated under the VCC Act. The VCC Act is administered by ACRA and the approval of the MAS is not required to be sought before the incorporation of a VCC, although existing requirements under the Securities and Futures Act (Chapter 290 of Singapore) (the "**SFA**") which are applicable to offers of units in a collective investment scheme to persons in Singapore will apply to VCCs.

Some of the key provisions of the VCC Act (and its subsidiary regulations, some of which are still in the process of being finalised as at the date of this article) that fund managers should take note of are as follows:

(a) A VCC must have a registered office in Singapore

(b) A VCC must have at least one (1) Singapore-resident[4] director and at least one (1) director (who may be the same person as the Singapore-resident director) who is either a "qualified representative"[5] or a director of the VCC's fund manager, and all directors must be "fit and proper" persons. Inability by ACRA to contact the local director after reasonable efforts to do so have been taken by ACRA may be deemed by ACRA as a reasonable ground to believe that the VCC is not carrying on business, which may result in a court winding-up of the VCC.

(c) At least one (1) secretary must be appointed within six (6) months of incorporation.

(d) An auditor must be appointed within three (3) months of incorporation.

(e) Annual general meetings ("**AGMs**") must be held within six (6) months of the end of the financial year. However, AGMs can be dispensed with if (i) the directors[6] of the VCC give written notice to the VCC's members, at least 60 days before the last date on which a VCC must hold an AGM, that an AGM for the relevant financial year will not be held, or (ii) the VCC has sent a copy of the its financial statements to all persons entitled to receive notice of general meetings of the VCC not later than five (5) months after the

[1] However, goods and services tax returns are filed at the sub-fund level. See the section titled "*Tax Treatment and Tax Incentives*" for further details.
[2] Contrast this with companies, which are required to comply with procedures for the notification of creditors and the making of solvency declarations by directors in order to undertake a share capital reduction.
[3] Contrast this with companies, which can only pay dividends out of profits.
[4] Singapore citizens, permanent residents or holders of EntrePass/Employment Pass (subject to the Ministry of Manpower's letter of consent) with a Singapore residential address may qualify as a Singapore-resident director.
[5] As defined in the VCC Act and the SFA.
[6] Contrast this with company AGMs, which can only be dispensed with if all members of the company pass a resolution at general meeting approving such dispensation.

end of the financial year to which the financial statements relate. Notwithstanding the foregoing, any one (1) or more members holding at least 10.0% of the total voting rights in the VCC may by notice to the VCC require the AGM to be held.

(f) Annual returns must be filed after the AGM and within seven (7) months after the end of the financial year. The failure to file annual returns may be deemed by ACRA as a reasonable ground to believe that the VCC is not carrying on business, which may result in a court winding-up of the VCC.

(g) Any sub-funds that are established under the umbrella fund will have to be registered within seven (7) days[7].

(h) An umbrella VCC is required to disclose to contractual counterparties (whether written or oral) in respect of any sub-fund the fact that the assets and liabilities of the relevant sub-fund are segregated.

(i) The assets of a sub-fund must not be used to discharge any liability of the umbrella VCC or any other sub-fund, and any liability of a sub-fund must be discharged solely out of the assets of that sub-fund.

(j) Despite not being a legal person separate from the umbrella VCC, a sub-fund of an umbrella fund may be wound up separately as if it were a legal person. An umbrella VCC may also sue or be sued in respect of a sub-fund and may exercise rights of set-off (if any) as between its sub-funds as if each sub-fund were a legal person.

(k) A member is entitled to inspect the register of members of the VCC, but only the part of the register that relates to that member.

(l) If a VCC acquires any property which is subject to a change of any kind that is registrable in Singapore, it has a duty to register the charge with ACRA within 30 days of the date of acquisition.

(m) A VCC may be wound up by the court if it does not commence business within one (1) year from the date of incorporation or if it suspends its business for an entire year.

(n) A VCC may be wound up by the court if it is used for a purpose other than to be one (1) or more collective investment schemes.

(o) A VCC may be wound up by the court if it does not have or ceases to have a duly licensed, registered or exempted fund manager for more than three (3) months.

[7] The MAS' approval is not required prior to the establishment of a sub-fund.

(p) A VCC may be wound up by the court if it breaches any anti-money laundering ("**AML**") and/or Countering the Financing of Terrorism ("**CFT**") laws, regulations and/or obligations.

In addition to the foregoing, the MAS has clarified that a fund manager may delegate fund management activity and operational duties to a third party (such as a sub-manager), provided that (a) such third party is regulated as a fund manager in another jurisdiction(s) and (b) the fund manager retains overall responsibility for the fund management duties and mitigates any conflict of interests that may arise.

Separately, the SFA provides that a custodian approved under Section 289 of the SFA must be appointed to supervise custody of the assets of a VCC which is an authorised collective investment scheme. A custodian is also required for a VCC that is a restricted collective investment scheme, but such VCCs have the option of maintaining their assets in trust or custody accounts with a prescribed entity[8]. Private equity and venture capital funds structured as VCCs are not required to appoint a custodian if the fact that a custodian has not been appointed is disclosed to their investors and acknowledgement of this fact has been obtained from such investors.

The new Section 286(2A) of the SFA also requires an approved VCC to have at least three (3) directors, one (1) of whom must be an independent director.

Fund managers should also note that MAS Notice VCC-N01 (Prevention of Money Laundering and Countering the Financing of Terrorism – Variable Capital Companies) ("**MAS AML/CFT Notice**") requires VCCs to maintain a register of beneficial owners of VCC (which is akin to the concept of controllers for companies).

ACCOUNTING

Each VCC must have audited financial statements for each financial period/year which gives a true and fair view of the financial performance of the standalone VCC, or in the case of an umbrella VCC, for each sub-fund.

[8] Prescribed entities include: (a) a bank licensed under the Banking Act (Chapter 19 of Singapore); (b) a merchant bank approved as a financial institution under the MAS Act (Chapter 186 of Singapore); (c) a finance company licensed under the Finance Companies Act (Chapter 108 of Singapore); (d) a depository agent within the meaning of Section 81SF of the SFA for the custody of securities listed for quotation or quoted on Singapore Exchange Securities Trading Limited or deposited with Central Depository (Pte) Ltd; (e) an Approved Trustee (as defined in the SFA); (f) any person licensed under SFA to provide custodial services for securities; and (g) a foreign custodian that is licensed, registered or authorised to conduct banking business or to act as a custodian in the country or territory where the account is maintained.

The first financial year of a newly-incorporated VCC must not be longer than 18 months, unless otherwise approved by the Registrar of VCCs.

An umbrella VCC must keep separate accounting and other records for each sub-fund that sufficiently explain the transactions and financial position of the sub-fund and that will enable true and fair financial statements, and any document required to be attached to those records, to be prepared from time to time. It must also devise and maintain a system of internal accounting controls sufficient to provide a reasonable assurance that the assets of each sub-fund are safeguarded against loss from unauthorised use or disposition and transactions of each sub-fund are properly authorised and that they are recorded as necessary to permit the preparation of true and fair financial statements of the umbrella VCC and to maintain accountability of assets. There is no statutory restriction on investment cycles, but all sub-funds of an umbrella fund must have the same accounting period.

The flexibility of VCCs is extended to accounting standards in that VCCs have the option of preparing their financial statements using international standards such as the International Financial Reporting Standards and U.S. Generally Accepted Accounting Principles, although for an umbrella VCC, the accounts of each sub-fund must be prepared using the same accounting standards as those used to prepare the financial statements of the umbrella VCC. Compared to other Singapore fund structures that are required to prepare financial statements which generally comply with the Singapore Financial Reporting Standards, such as unit trusts and real estate investment trusts, the VCC's flexibility allows it to better serve the needs of global investors and enhances the attractiveness of Singapore as a fund domiciliation destination.

REGULATED FUND MANAGER REQUIREMENT

VCCs are required to appoint a regulated fund manager (namely, a holder of a capital markets services ("**CMS**") licence for fund management issued by the MAS (a licensed fund manager), a registered fund management company issued by the MAS (a registered fund manager) or certain classes of persons exempt from the requirement to hold a licence but still subject to MAS-oversight, such as a licensed bank (an exempt fund manager)). As such, certain fund managers which rely on any of the licensing exemptions, such as single family offices, may not be able avail themselves of the VCC.

RE-DOMICILIATION

A key feature of the VCC Act which has most certainly had a positive impact on adoption of the VCC so far is its inward re-domiciliation mechanism. This mechanism enables existing foreign-domiciled funds with similar structures to the VCC to re-domicile in Singapore as VCCs by submitting an application for transfer to ACRA and notifying the foreign authorities of the de-registration.

Based on the draft version of the Variable Capital Companies (Transfer of Registration) Regulations 2019, which are expected to be finalised soon, the key minimum requirement for re-domiciliation is that the fund seeking re-domiciliation is solvent. There are currently no other prescribed minimum requirements, although ACRA will not approve the application of a proposed VCC which satisfies all of the prescribed requirements where:

(a) the person named as manager of the proposed VCC does not satisfy the regulated fund manager requirement and/or is not a "qualified representative";

(b) none of the directors of the proposed VCC is a "qualified representative" of the manager;

(c) the proposed VCC is likely to be used for an unlawful purpose or for purposes prejudicial to public peace, welfare or good order in Singapore; or

(d) it would be contrary to national security or the national interest for the proposed VCC to be registered.

AML/CFT

The MAS AML/CFT Notice sets out the AML/CFT requirements and obligations that are applicable to all VCCs. In general, the policy outcomes and AML/CFT requirements and obligations applicable to VCCs are similar to those required of existing MAS-regulated entities.

VCCs are allowed to delegate their AML/CFT obligations[9] to the fund manager or to not more than one (1) eligible financial institution (such as a licensed bank in Singapore or a licensed finance company). Any outsourcing arrangements that a VCC enters into will also have to comply with the Guidelines on Outsourcing. In an earlier consultation paper on the VCC framework, the MAS suggested that the eligible financial institution may in turn sub-delegate the AML/CFT obligations that have been outsourced to it to another service provider that may not be regulated by the MAS for AML/CFT purposes, such as a fund administrator. However, the MAS AML/CFT Notice provides that an eligible financial institution may only delegate such obligations to another eligible financial institution or a financial institution which is subject to and supervised by a foreign authority for compliance with

[9] Save for the requirements set out in paragraphs 3, 4 and 10 of the MAS AML/CFT Notice.

AML/CFT requirements consistent with standards set the Financial Action Task Force. Accordingly, it does not seem that an eligible financial institution will be able to sub-delegate the AML/CFT obligations applicable to a VCC to a fund administrator which does not fall within the list of eligible financial institutions set out in the MAS AML/CFT Notice, even though it is common market practice for funds to outsource the AML/CFT functions of the fund to fund administrators or other service providers such as compliance firm. It is hoped that this will be clarified in the Guidelines to the MAS AML/CFT Notice.

It is also important to note that MAS has clarified that the VCC will remain ultimately responsible for fulfilling its AML/CFT obligations, regardless of whether it has delegated such obligations to a third party. Accordingly, it would be prudent for fund managers to negotiate an indemnity clause in the services agreement as a risk allocation mechanism for any financial penalty that may be levied upon the VCC by the MAS for the third party's failure to perform the outsourced AML/CFT obligations, although it remains to be seen how amenable third-party service providers would be to assuming such risks.

VCC GRANT SCHEME

The MAS has launched a grant scheme to encourage industry-wide adoption of the VCC framework in Singapore. The grant scheme, which will run for three (3) years initially, has been established with the purpose of helping fund managers defray costs associated with incorporating or registering a VCC by co-funding up to 70.0% of eligible expenses paid to Singapore-based service providers, such as legal counsels and tax advisors, with a cap of S$150,000 per application and a maximum of three (3) VCCs per fund manager. This means that a fund manager will have to frontload approximately S$214,286 per VCC to get a reimbursement of S$150,000 through the grant scheme.

VCC set-up costs can be included in the calculation of the annual S$200,000 business expenditure requirement for both Sections 13R and 13X of the Income Tax Act ("**ITA**").

TAX TREATMENT AND TAX INCENTIVES

Tax Treatment

Notwithstanding the classification of a VCC in the VCC Act as a "body corporate" (as opposed to a "company"), a new Section 107 has been introduced in the ITA to clarify the applicability of the ITA to VCCs. Accordingly, the VCC will be treated as a company and a single entity for the purpose of Singapore tax liabilities. In the case of an umbrella VCC, tax residence is determined at the umbrella level. Tax deductions and allowances are applied at the sub-fund level, and the resulting chargeable income of each sub-fund is aggregated to comprise the total chargeable income of the VCC.

Goods and Services Tax

In respect of goods and services tax ("**GST"**), each sub-fund is required to assess its respective GST registration liability based on the value of taxable supplies made, and GST-registered sub-funds are required to file separate GST returns. While GST registration, accounting and reporting are performed by the umbrella VCC on behalf of its sub-funds, the collection and enforcement of GST will be administered at the sub-fund level based on the GST returns filed by the respective GST-registered sub-funds.

"Check-the-Box" Election for U.S. Investors

For funds that have U.S. investors, a key benefit of the VCC is its eligibility for the U.S. "check-the-box" election, which allows a fund to be treated as transparent for the purposes of U.S. federal income tax. This means that any U.S. investor is placed in the same tax position as if they had invested directly in the underlying investments of the VCC. Where a VCC intends to make the "check-the-box" election in respect of a sub-fund for U.S. tax purposes, a suitable U.S. tax adviser will need to review the proposed VCC structure to ensure that the relevant sub-fund is suitable for the "check-the-box" election and also to consider if there is any risk of adverse tax consequences for non-U.S. investors in the sub-fund with such an election.

Other Tax Considerations for Investors

Given the relative ease with which shares of a VCC may be redeemed, it is not inconceivable that redemptions may be a preferred way for some investors to realise investment gains as well as a way to access short-term liquidity, particularly where the relevant fund does not charge a redemption and/or subscription fee. While capital gains are not taxed in Singapore, any gains from redemptions which could be construed as "gains or profits of an income nature" will be taxable. The frequency of subscriptions and redemptions would presumably be a persuasive factor for the purposes of such construction. An investor that intends to subscribe for and redeem shares in a VCC periodically, whether to manage cash flow or as part of its investment strategy, should be mindful of this capital-revenue dichotomy.

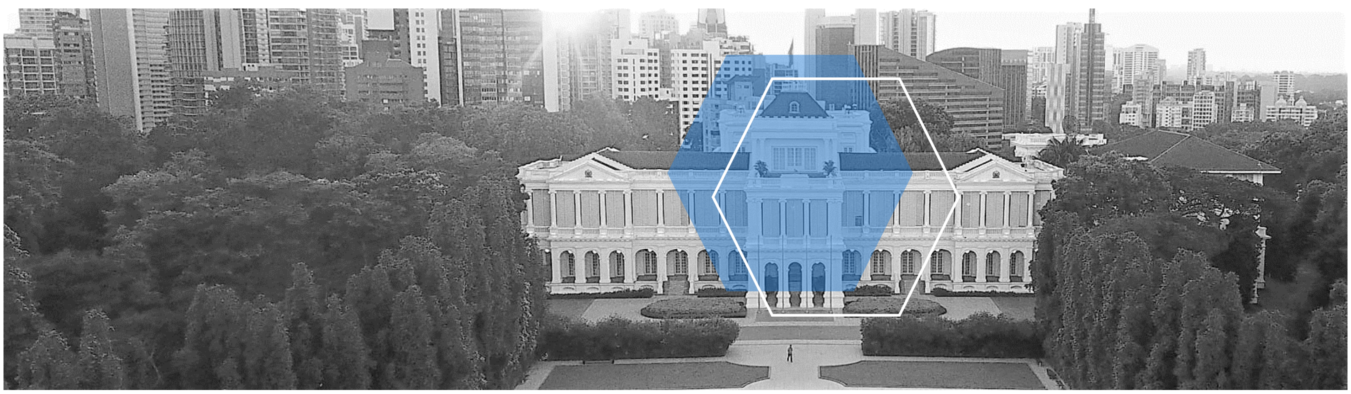
Sections 13X and 13R of the ITA

Sections 13R and 13X of the ITA (respectively, the "**13R Scheme**" and "**13X Scheme**") provide tax exemptions on specified income from designated investments derived by funds managed by a Singapore-based fund manager. The tax incentives under the 13R Scheme and the 13X Scheme have been extended to VCCs. Accordingly, VCCs approved under the 13R Scheme or 13X Scheme will qualify for withholding tax exemptions on interest and other qualifying payments currently available to funds approved under the 13R Scheme or 13X Scheme. The 13R Scheme requires, among other things, the applicant fund to have annual business expenses of at least S$200,000 (local or otherwise), while the 13X Scheme requires the applicant fund to have annual local business expenses of at least S$200,000 and a minimum fund size of S$50.0 million at the time of application.

In the case of umbrella VCCs, the tax incentives under the 13R Scheme and the 13X Scheme are granted at the umbrella level. Practically, this means that the requirements for these tax incentive schemes, including the requirements pertaining to assets under management (in the case of Section 13X) and annual business expenditure (in both cases), can be aggregated across all of the sub-funds under the umbrella VCC. Thus, a fund manager managing four (4) funds who would previously have had to use four (4) Singapore companies with a fund size of at least S$50.0 million each and have annual local business expenses totalling US$800,000 across the four (4) funds in order to qualify for the 13X Scheme would now be able to utilise an umbrella VCC with four (4) sub-funds and enjoy the tax incentives provided under the 13X Scheme across all four (4) sub-funds while satisfying only a quarter of the quantitative requirements.

Under the 13R Scheme, a financial penalty is levied on a Singapore non-individual investor who either alone or together with its associates beneficially owns more than a prescribed percentage (typically 30.0%) of the total value of all issued securities of the approved fund. For the purposes of the said penalty, the percentage ownership of the Singapore non-individual investor and its associates in an umbrella VCC is similarly calculated across all sub-funds of the VCC (i.e. at the umbrella level). As such, this would potentially enable a Singapore non-individual investor and its associates to hold participating shares that exceeds the prescribed percentage at the sub-fund level while still falling below the prescribed percentage at the umbrella fund level.

A key thing for fund managers to note in respect of the 13R Scheme and 13X Scheme is that the requirement that a fund that has been approved under either of the schemes cannot change the investment objective of the fund (other than in certain situations and subject to approval of the authorities) must be satisfied at the VCC level, which means, practically, that a breach of the investment objective condition by a sub-fund will adversely impact the umbrella VCC and the other sub-funds. Thus, before a new sub-fund with a different investment objective than what was previously approved under either scheme can be established, the VCC will need to obtain approval from the Inland Revenue Authority of Singapore.



Tax Exemption Scheme for New Start-Up Companies

The Tax Exemption Scheme for New Start-Up Companies (the "**SUTES**") has also been extended to VCCs. Under the SUTES, a VCC will be exempted from any tax on 75.0% the first S$100,000 of chargeable income and 50.0% of the next S$100,000 of chargeable income for the first three (3) years of assessment, determined from the date of the incorporation of the VCC. The SUTES will be applied once at the umbrella level, regardless of the number of sub-funds that the VCC may have.

GST Remission

The GST remission for Singapore domiciled funds will be extended to VCCs approved under the 13R Scheme or 13X Scheme. Accordingly, a VCC that is approved under the 13R Scheme or 13X Scheme will be able to recover GST charged by Singapore-registered goods and services suppliers at the fixed rate set annually by the MAS, even if it is not itself GST-registered.

Financial Sector Initiative – Fund Management Scheme for Fund Managers

For fund managers, the concessionary corporate income tax rate of 10.0% (instead of 17.0%) under the Financial Sector Initiative – Fund Management scheme will apply to management or advisory fees paid by VCCs which have been approved under the 13R Scheme or 13X Scheme, provided that the prescribed requirements (relating to, among other things, minimum assets under management) are satisfied.

STRUCTURAL ADVANTAGES IN MASTER-FEEDER FUNDS

Prior to the VCC, Singapore-based alternative investment funds are sometimes set up with a Singapore-incorporated master fund and a limited partnership feeder fund (that may or may not be established in Singapore) to take advantage of Singapore's network of Avoidance of Double Taxation Agreements ("**DTAs**"), which is currently only available to Singapore-resident companies. With the introduction of the VCC and the MAS confirming that VCCs will be able to benefit from Singapore's DTA network, it is now possible to merge the master and feeder entities into the same entity (and, therefore, the same jurisdiction) while achieving segregation of assets and liabilities within the same corporate entity. This is in line with an emerging trend towards consolidation of multi-jurisdictional fund structures into fewer jurisdictions or even a single jurisdiction.

To the extent that the feeder fund under the typical master-feeder structure is established in a jurisdiction other than Singapore, the ability to situate both the fund and the fund manager in the same jurisdiction would conceivably increase administrative convenience and operational efficiency, and reduce overlapping or duplicative regulatory and other requirements, which may otherwise be imposed separately on the fund and the fund manager. For example, there is no longer a need to comply with foreign directorship requirements, thereby translating into lower operating costs.

To the extent that the feeder fund under the typical master-feeder structure is established in Singapore, merging the master and feeder entities into the same entity could potentially eliminate the problem of the domestic laws of certain jurisdictions, in particular civil law jurisdictions, not recognising the concept of a trust for the purposes of determining beneficial ownership and therefore denying DTA benefits to the feeder entity on that basis. With confirmation from the MAS that VCCs which are Singapore tax residents can apply for a certificate of residence[10] from the Inland Revenue of Singapore, the VCC potentially provides a convenient solution to the risk of a limited partnership being double taxed on income sourced from certain jurisdictions.

[10] The certificate of residence will be issued in the name of the VCC and will detail the names of all sub-funds receiving the same income from the same source jurisdiction.

The master-feeder convergence solution offered by the VCC also provides more robust protection against the challenges posed by the principal purpose test under the Multilateral Instrument, pursuant to which a source jurisdiction may deny treaty benefits if the principal purpose of a transaction or arrangement is to obtain such benefits. An example of a jurisdiction where this might be of particular relevance is India, where, in addition to the ratification of the Multilateral Instrument, the Income Tax Act, 1961 of India, allows Indian tax officials to deny tax benefits if a deal is found without any commercial purpose other than tax avoidance pursuant to the General Anti-Avoidance Rule.

The structural efficiencies of the VCC is also significant in the light of economic substance requirements that several jurisdictions such as the Cayman Islands, the British Virgin Islands, the Isle of Man, Jersey and Guernsey have put in place in response to the European Union's blacklisting of these jurisdictions for not cooperating with economic substance requirements. The requirements under the VCC Act, *viz*, the requirement to have at least one (1) Singapore-resident director, a Singapore-resident company secretary and auditor and a registered office in Singapore, and the requirement that the day-to-day fund management and operations be carried out or overseen by a MAS-regulated fund manager, makes the case for establishing the economic substance necessary to benefit from Singapore's network of DTAs a lot stronger.

The VCC also allows for highly convoluted and customised fund structures to be simplified and made more cost- and administratively effective. For example, multiple VCCs could be utilised in a master-feeder structure, where both the feeder and the master entities are VCCs. In such a setup, the feeder fund can be easily customised to cater to a variety of investor profiles and appetites by using multiple sub-funds, such as to cater to an institutional investor which may want to have its own dedicated feeder or to separate U.S. and non-U.S. investors where the "check-the-box" election is available to the sub-fund through which the U.S. investors are investing, and there is a risk of adverse tax consequences for non-U.S. investors with such election.

CONSTITUTION

Two (2) model VCC constitutions, neither of which are endorsed by ACRA or the MAS, have been promulgated by the Singapore Academy of Law, one for open-ended funds and another for closed-end funds. The model constitutions have been drafted in a fairly general manner with sufficient details to comply with the baseline requirements prescribed in the VCC Act for the constitution of a VCC. In practice, the detailed terms of a VCC and its sub-funds (if any) will more often than not be documented primarily in the offering document (where there is one) and any supplement thereto (the "**Offering Documents**"), such that the Offering Documents form the core constitutional documents of the VCC and the constitution is kept relatively broad and generic. This is the more sensible approach as it facilitates speed to market, which is one of the key reasons for utilising an umbrella VCC structure.

DRAWBACKS OF THE VCC

Confidentiality

As alluded to above, umbrella VCCs are required to prepare financials statements containing separate accounts for each sub-fund, and the financial statements of the VCC must be sent to all persons entitled to receive notice of general meetings of the VCC not less than 14 days before the date of the meeting if the VCC is not exempted from the requirement to hold general meetings. For better or for worse, this means that the investors of a sub-fund under an umbrella VCC will have access to the financial statements of other sub-funds, even if it is not an investor of the other sub-funds. Conceivably, this may be less than ideal for fund managers and investors.

Recognition of the Concept of Segregation

Although the VCC allows for assets and liabilities of each sub-fund to be ring-fenced, this concept of segregation of assets and liabilities has yet to be judicially tested. Thus, to the extent that a VCC operates or has assets held on its behalf or be subject to claims in other jurisdictions, it is not certain that such jurisdictions will necessarily recognise such segregation under their relevant laws. However, this is a potential issue that is inherent in every structurally similar variant of the VCC in other jurisdictions, and a standard risk factor is typically provided in the offering document to cater for such risks. On a related note, retail fund managers should note that under the proposed amendments to the Code on Collective Investment Schemes, an authorised VCC or an authorised sub-fund may only invest in assets located in jurisdictions that do not have a structurally similar variant(s) of the VCC after taking reasonable measures to mitigate cross-cell contagion risk, such as ensuring that the agreements that the VCC enters into on behalf of the relevant sub-fund and which govern the relevant sub-fund's overseas assets are governed by the laws of jurisdictions that recognise cellular structures and uphold the segregation of assets and liabilities across sub-funds.

Carried Interest

Because carried interest is ordinarily considered as income for the purposes of taxation in Singapore, it is not uncommon for Singapore-based fund managers to structure carried interest offshore, whether as foreign-sourced income or otherwise, to optimise its tax treatment. With the strong Singapore nexus of the VCC framework, it would arguably be a lot harder for a VCC fund manager to justify having only the carried interest component parked offshore while everything else is in Singapore.

LOOKING AHEAD

We share some of our current thoughts on the road ahead for the VCC framework below:

Availability of the VCC to Foreign Fund Managers and Fund Managers Exempted Under the SFA

Currently only MAS-regulated fund managers are eligible to be fund managers of VCCs, fund managers licensed in other jurisdictions are not. This is not expected to change any time soon, given how it seems that the MAS has decided to take the approach of keeping the VCC as flexible as possible and exercising regulatory control through the CMS licensing regime. However, the VCC is conceivably a very appealing vehicle for large families with multiple stakeholders to pool resources for inter-generational legacy planning purposes, and with the recent addition of family offices as one of the options available under the Global Investor Programme, the Singapore Government has clearly demonstrated its intent to attract and anchor wealthy business families in Singapore through active management of their respective family offices. It is therefore not hard to imagine the VCC being made available to exempt single family offices in the future.

Conversion of Other Existing Singapore Fund Structures into VCCs and Other Regulations

Although the current version of the VCC Act only allows existing foreign-domiciled funds with similar structures to the VCC to re-domicile in Singapore as VCCs, we expect future iterations of the VCC Act to contain mechanisms that facilitate the conversion of other existing Singapore fund structures directly into VCCs. More robust corporate governance requirements are also likely to be introduced progressively, which will likely see more regulations imposed on fund administrators and also independent director requirements for non-retail VCCs being introduced, conceivably through a soft regulation medium such as a corporate governance code, at least initially.

Adoption

From the perspective of accessing the Asian investor base, the VCC makes a lot of sense, and its introduction could not have been more timely. With the MAS being widely recognised as the gold standard for Asian financial regulators coupled with the geopolitical situation of Hong Kong, Singapore's closest competitor in the region for the asset management space, Singapore is being viewed increasingly as a relatively less risky hinterland for investing in the region and managing the wealth of global investors. Also, as alluded to above, the introduction of economic substance requirements in some of the popular offshore jurisdictions for funds domiciliation has resulted in these jurisdictions losing some of their lustre and the proposition of onshoring becoming a lot more attractive and perhaps even operationally necessary. The re-domiciliation mechanism into the VCC Act offers a low-hanging fruit for fund managers seeking to consolidate their multi-jurisdictional fund structures and is likely to be the main driver of adoption in the near future.

In terms of funds with a large proportion of U.S. investors, investor education is probably the key to adoption, given the relative familiarity of U.S. investors with the limited partnership structure, at least insofar as private equity funds are concerned. Ultimately, adoption boils down to investor appetite, and investor education and familiarity go a long way towards that.

Boosting the Fund-Platform-as-a-Service Industry

Third-party platforms are generally umbrella fund structures established by fund managers or promoters, including distributors, which enable other previously unaffiliated (sub-)fund managers to essentially plug-and-play by "leasing" the platform's existing fund infrastructure to quickly establish its own separately managed sub-fund. Through the concept of aggregation, such platforms centralise certain functions and costs that fund managers utilising the platform outsource to them, such as fund formation, compliance, licensing, regulatory filings and fund administration, thereby achieving economies of scale across all of the sub-funds under the umbrella fund. With the introduction of the structurally superior VCC, the sharing economy becoming increasingly mainstream and the increasing preference of fund managers wishing to access new markets for distribution to utilise more regulated onshore products instead of traditionally preferred offshore routes, this sector is expected to grow rapidly in Singapore.

WMH Law Corporation is an award-winning medium sized boutique law firm founded by a group of enterprising next-generation lawyers who were previously practising at a Big 4 law firm in Singapore with the goal of delivering big firm quality legal work in a cost-effective manner. WMH Law Corporation's corporate law practice advises on a range of specialised and general corporate law matters, with a particular focus on asset management, start-ups, fintech and financial services regulatory compliance and corporate finance. Owing to their differentiated backgrounds, the strength of WMH Law Corporation's corporate law advisers lies in their ability to combine solid legal know-how with business acumen to help clients navigate the regulatory landscape while also achieving their commercial goals.