

Sweden

Niclas Rockborn, Nils Unckel and Caroline Walderfors
Gernandt & Danielsson

www.practicallaw.com/4-501-3364

RETAIL FUNDS

1. Please give a brief overview of the retail funds market in your jurisdiction. (How developed is the market? Has it been active in the past year?)

Swedish investment fund savings plans date back to the 1950s. The Swedish retail funds market has since become home to a wide range of investment funds, offering various investment possibilities, risk levels and fees. It consists of two main categories of product:

- **Undertakings for collective investments in transferable securities (UCITS).** These funds are established under the regulations implementing Directive 85/611/EEC on undertakings for collective investment in transferable securities (UCITS Directive). The Directive has been implemented in Sweden through the Investment Funds Act (*Jagen (2004:46) om investeringsfonder*).
- **Special funds (non-UCITS).** These are subject to domestic laws, including the applicable provisions of the Investment Funds Act. A hedge fund is normally categorised as a non-UCITS.

Investment fund is a collective term for both UCITS and non-UCITS. Funds that are not classified as investment funds under Swedish rules and regulations are referred to as “fund-similar products” and can be considered as a third category of product. They are not subject to the same provisions as UCITS and non-UCITS and are not covered in this chapter.

98% of the Swedish population (aged 18 to 74) currently save through various investment funds. If premium pension savings are excluded, 74% of the population own shares in an investment fund. 67% of all children also have fund savings. The percentage that save in funds has increased dramatically over time: in the mid-1990s, the figure was only about 50%.

Competition in the Swedish investment fund market has increased since 2000, with the number of funds increasing from about 1,500 to over 4,000. Net fund assets are now equivalent to nearly SEK1,200 billion (about EUR115 billion). Many foreign fund management companies have established a presence in Sweden and the local banks' dominance of the fund market has declined. Over the last few years, independent players, and banks and fund management companies have launched fund marketplaces where they offer a wide range of their own funds and external funds.

One of the main principles of the Swedish fund legislation is that investment funds should be open for subscription to the public and

that unitholders shall have the right to redeem their units in the fund at any time (open-ended funds). However, a non-UCITS may be partly closed for subscriptions and redemptions but open at least once a year, subject to the permission of the Swedish Financial Supervisory Authority (SFSA). The rules for such non-UCITS are similar to the rules for UCITS or non-UCITS without such permission.

2. What are the key statutes, regulations and rules that govern retail funds in your jurisdiction? What regulatory bodies are involved in regulating retail funds?

Regulatory requirements

The key statutes and regulations are the:

- Investment Funds Act. Swedish investment fund legislation is primarily based on the UCITS Directive (*see Question 1*). The Investment Funds Act implements the Directive, and also contains national legislation applicable to non-UCITS.
- SFSA's Regulations Governing Investment Funds (*Finansinspektionens föreskrifter (FFFS 2008:11) om investeringsfonder*).
- Swedish Marketing Act (*marknadsföringslagen (2008:486)*), which provides that marketing measures must be compatible with good marketing by fund managers practice and must not be misleading.
- Swedish Investment Fund Association's (*Fondbolagens Förening*) (SIFA) guidelines. The guidelines cover several areas, including financial advice and marketing of investment funds. Therefore, they must be considered when marketing investment funds in Sweden.

SIFA is a trade organisation whose purpose is to protect the collective interests of fund management companies and investors in all dealings with the public authorities and the legislature.

Further legal requirements may apply in relation to fund management companies, for example under the Money Laundering and Terrorist Financing (Prevention) Act (*Jagen (2009:62) om åtgärder mot penningtvätt och finansiering av terrorism*) and the Capital Adequacy and Large Exposures Act (*Jagen (2006:1371) om kapitaltäckning och stora exponeringar*).

Regulatory bodies

The SFSA supervises financial institutions in Sweden. The SFSA issues regulations regarding, among other things, the following:

- Governance structures.
- Risk control.

- Capital adequacy under the Basel 2 rules.
- Accounting.
- Procedures for the prevention of money laundering and financing of terrorism.

The SFSA has a range of tools to facilitate its supervision, including the right to interview the employees of an institution under its supervision. If the SFSA considers that the institution's operations are unsound or that the institution is breaching the laws or regulations, it can impose the following sanctions:

- Disciplinary reprimands.
- Warnings.
- Fines.
- Revocation of the operating licence.

3. Do the retail funds themselves have to be authorised or licensed? If so, what are the main steps involved?

Domestic fund management companies

A fund management company must be authorised by the SFSA to conduct fund operations. Only a Swedish limited liability company can be authorised for that purpose. In addition, the fund management company can be authorised to:

- Manage the discretionary portfolio of financial instruments.
- Accept units in collective investment undertakings for custody.
- Accept assets subject to a reporting obligation.
- Provide investment advice in respect of certain financial instruments.
- Perform certain services or functions for a:
 - Swedish fund management company;
 - foreign fund management company;
 - foreign investment fund.

The application for authorisation must, among other things, include:

- A plan for the contemplated operations (business plan) containing a summary description of the fund management company's organisation. A business plan must contain, among other things, the following documents:
 - the company's activities;
 - the ownership list;
 - the group description and organisation;
 - the management list;
 - a description of the economic situation;
 - any outsourcing agreements;
 - a description of the information system and any security issues;

- instructions for handling conflicts of interest;
- a description of compliance;
- a description of risk management;
- instructions for the internal audit;
- instructions for handling events of material significance;
- instructions for the management of ethical issues;
- instructions for the management of complaints;
- measures taken to prevent money laundering and financing of terrorism.

The SPSA must make a decision regarding the application to conduct fund operations within five months.

- Fund rules must be registered for all investment funds. The fund rules must contain, among other things:
 - a general summary of the fund's nature regarding its:
 - holdings;
 - aims;
 - strategies.
 - a detailed description of the fund's investment objectives to enable investors to assess the risks associated with the fund.

The SFSA approves the fund rules, if the provisions are reasonable for the holders of the investment fund's units. The SFSA must make a decision within:

- 30 days for UCITS;
- 60 days for non-UCITS.

Foreign fund management companies

The following applies to foreign fund management companies wishing to conduct business in Sweden:

- A fund, domiciled in the European Economic Area (EEA), which complies with the UCITS Directive, can notify the SFSA by using the model notification letter of the Committee of European Security Regulators (CESR). The SFSA's practice of notification of UCITS in Sweden is based on the CESR's guidelines to simplify the notification procedure of UCITS (CESR/06-120b).
- A fund, domiciled outside the EEA or that does not comply with the UCITS Directive, must obtain the SFSA's authorisation.
- A foreign fund management company domiciled within the EEA can, under certain conditions:
 - conduct operations from its Swedish branches;
 - conduct operations in Sweden by offering and providing services in Sweden from its home state.

4. Who can market retail funds?

Pure marketing of investment funds such as UCITS and non-UCITS does not require the SFSA's authorisation. The SFSA considers that the term marketing does not cover selling or re-

deeming fund units. Merely providing application forms should not trigger any approval or notification requirements, as long as the subscribers fill in and send the forms themselves.

However, the SFSA's authorisation is necessary to conduct fund operations such as the sale of fund units in Sweden. In addition, investment firms licensed to execute orders under the Securities Markets Act (*lagen (2007:528) om värdepappersmarknaden*) can sell investment fund units to investors.

5. To whom can retail funds be marketed?

UCITS and non-UCITS can be marketed to any investor (including retail and professional investors) in Sweden.

6. What are the key requirements that apply to managers/operators of retail funds?

A Swedish limited liability company can only be authorised to conduct fund operations if it meets the following criteria:

- The company's head office is located in Sweden.
- It can be reasonably assumed that the planned operations will be conducted in accordance with the provisions of the Investment Funds Act and other legislation regulating the company's operations.

In addition, the following requirements apply:

- **Business plan.** This must be attached to the application for authorisation (see *Question 3*).
- **Capital requirements.** On the grant of authorisation, a fund management company's initial capital must be equivalent to at least EUR125,000 (about US\$186,500). Once operations begin, the fund management company's own funds cannot be less than the minimum initial capital. Depending on the managed assets, the fund management company's own funds (including the initial capital) must be up to the equivalent of EUR10 million (about US\$14.7 million). This requirement applies to fund management companies that manage fund assets with a value exceeding EUR250 million (about US\$360 million).
- **Requirement of sound business operations.** A fund management company must conduct its operations in a manner that ensures that:
 - the public's confidence in the fund market is maintained;
 - the individuals' capital investments are not unduly jeopardised;
 - the operations are considered sound.
- **Damages.** A fund management company must compensate a unitholder who incurs a loss as a result of the company's breach of the:
 - Investment Funds Act; or
 - fund rules (see *Question 3*).

7. Who holds the portfolio of assets? What regulations are in place for its protection?

A depositary holds the portfolio of the investment fund's assets (*förvaringsinstitut*). The name of the depositary must be stated in the fund rules which must be approved by the SFSA (see *Question 3*). A depositary must maintain its registered office in Sweden or, where a depositary is a Swedish branch of a foreign fund management company, in another state within the EEA.

The following institutions can act as depositaries:

- Supervised banks as defined in the Banking and Financing Business Act (*lagen (2004:297) om bank- och finansieringsrörelse*).
- Other credit institutions as defined in the Banking and Financing Business Act.
- Securities companies licensed to conduct specific ancillary operations under the Securities Market Act.

The depositary must conduct business:

- Independently of the fund management company.
- Exclusively in the unitholders' interests.

However, the depositary can be a company within the same group as the fund management company, provided that the companies are two separate legal entities.

8. What are the main legal vehicles used to set up a retail fund and what are the key advantages and disadvantages of using these structures? What are the participants' interests in the fund called (for example, share or unit)?

The Swedish fund system is formed on a contractual basis and regulated funds cannot have any other legal form. A retail fund can be described as a multilateral contract between the:

- Unitholders.
- Fund management company.
- Depositary.

The parties' respective obligations are:

- **Unitholders:** to contribute the capital to the investment fund. Investors, in the form of unitholders, subscribe units issued by the fund management company which represent a portion of the fund and their rights in the fund's undivided assets. The liability of unitholders is limited to the amount they have contributed.
- **Fund management company:** to manage the assets and represent the unitholders in respect of all issues concerning the investment fund.
- **Depositary:** to take receipt of, and hold in custody, the investment fund's assets.

Funds that are not regulated (for example, non-regulated investment companies) may be structured differently.

9. Describe the investment and borrowing restrictions to which retail funds are subject.

Permitted investments

UCITS and non-UCITS must maintain a suitable diversification of investments, taking into consideration the spreading of risk associated with the fund's investment focus as stated in the fund rules (see *Question 3*). UCITS and non-UCITS can, subject to the limitations under the Investment Funds Act, invest in:

- Transferable securities and money market instruments. The value of transferable securities and money market instruments issued by any single issuer cannot exceed 5% of the fund's value. The limit may be higher in certain cases, for example, when investing in government bills.
 - Derivative instruments. An investment fund can invest in derivative instruments provided that:
 - they are traded on a regulated market;
 - the underlying assets constitute or relate to:
 - money market instruments;
 - interest rates;
 - exchange rates or foreign currency.
 - the underlying assets can be included in the fund according to the fund rules.
- An investment fund can also invest in derivative instruments that are traded directly between the parties (OTC) if:
- the counterparty is supervised and belongs to the categories of undertakings approved as counter parties by the SFSA;
 - the derivative instrument is subject to reliable and verifiable valuation on a daily basis;
 - the derivative instrument is capable at any time (and for fair market value) of, on the initiative of the fund management company, being:
 - sold;
 - redeemed;
 - closed by an offsetting transaction.
 - Units in a collective investment undertaking. An investment fund can invest in:
 - units in other investment funds;
 - units in special funds and foreign collective investment undertakings which fulfil certain conditions in the Investment Funds Act. However, this is provided that those funds and foreign collective investment undertakings cannot invest more than 10% of their assets in units of other funds or foreign collective investment undertakings under their fund rules or the articles of association.
 - Deposits with credit institutions. Assets of an investment fund can be deposited with:
 - Swedish credit institutions;
 - foreign credit institutions with registered offices within the EEA; and

- other foreign credit institutions if they are subject to prudential rules equivalent to those under EC law.

The deposits' maturity must not exceed 12 months. In addition, the terms and conditions of the account must make it possible, through notice of termination, to make the assets available to the fund immediately.

- Liquid assets necessary for the investment fund's management.

In its investment operations, a fund management company cannot:

- Raise or grant cash loans.
- Act as a guarantor.
- Sell:
 - transferable securities;
 - money market instruments;
 - derivative instruments;
 - units in collective investment undertakings that are not part of the fund.

A fund management company can raise short-term loans that, collectively, do not exceed 10% its value.

An investment fund cannot lend financial instruments (securities loans) that amount to more than 20% of its net asset value (NAV).

Exemption

The SFSA can authorise non-UCITS (organised under the Investment Funds Act) to diverge from the above investment restrictions. Generally, non-UCITS must maintain:

- An adequate spread of investments.
- Diversification limits that are substantially similar to those of a UCITS (unless specific exemptions have been approved by the SFSA).

10. Can the manager/operator place any restrictions on the issue and redemption of interests in retail funds?

Investment funds must (*Investment Funds Act*):

- Be constituted by capital contributions from the public.
- Be open to all investors.
- Not place any restrictions on the issue and redemption of interests in the fund.

Non-UCITS

Non-UCITS, including foreign non-UCITS, that are licensed to market and sell fund units in Sweden under the Investment Funds Act, can, subject to the SFSA's approval:

- Limit the scope of investors who can acquire units in collective investment undertakings in their fund rules to a specially identified and limited group of investors.
- Set a minimum initial investment amount per investor.

A non-UCITS must permit redemption of units at least once a year.

UCITS and non-UCITS

The fund management company can refuse subscription if either:

- An issue of units to the investor would breach Swedish or foreign law.
- Acceptance of the investor would require the fund management company to effect any registration or similar action in a foreign jurisdiction.

11. Describe any restrictions on the rights of participants in retail funds to transfer or assign their interests to third parties.

The investment fund's rules often regulate the unitholders' rights to transfer or assign their units to third parties. Normally, a unitholder can transfer its units to a third party on fulfilment of certain requirements. A notice must be given to the fund management company on transfer.

Units can also normally be pledged. The fund management company must be notified in writing about the pledge.

12. Describe the periodic reporting requirements to:

- Investors.
 - Regulators.
-

Investors. In relation to unitholders, a fund management company must regularly, and at least once a week, publish the value of the units of the relevant UCITS or non-UCITS.

A fund management company must provide:

- An annual report within four months of the expiry of the financial year. (A fund management company may have a split financial year.)
- A half-yearly report on the first six months of the financial year within two months following the expiry of the half-year.

The annual and half-yearly report must contain all information necessary to assess the investment fund's development and financial position.

Regulators. A fund management company must:

- Be able to present a list of each investment fund's asset holdings (as stated in the Investment Funds Act) at any time.
- Submit certain information to the SFSA regarding its activities and each individual investment fund at the end of every quarter.

In relation to UCITS, a fund management company must prepare a list of each UCITS' holding of financial instruments on the final banking day of each quarter.

In relation to non-UCITS, the fund management company must:

- Prepare a list of each holding of financial instruments, as and when the SFSA instructs.
- Calculate and report to the SFSA the risk level in relation to:
 - standard deviation;
 - performance of the past month; and
 - concentration risk.

13. Describe the tax treatment for:

- Funds.
 - Resident investors.
 - Non-resident investors.
-

Funds. An investment fund is taxed in Sweden on its income. However, an investment fund can make deductions for dividends to unitholders. To avoid taxation, investment funds normally distribute dividends to unitholders.

Unitholders (resident physical persons). Dividends from units in an investment fund are subject to capital income tax. Preliminary tax is charged at a rate of 30% of the dividend. A preliminary tax deduction is made irrespective of whether the dividend is reinvested or distributed. Redemption of units is considered a sale and subject to capital income tax.

Special tax provisions apply if the investment fund is associated with a:

- A unit-linked insurance.
- An individual pension saving (IPS).
- A premium pension.

The tax rate may also be affected by individual circumstances.

Non-resident investors. In relation to dividends, paid to physical persons with limited tax liability in Sweden (resident abroad), a fund management company is normally required to withhold Swedish coupon tax in accordance with applicable legislation and double taxation treaties.

14. Please summarise any proposals for the reform of retail fund regulation in your jurisdiction.

Sweden is expected to implement EC Directive 85/611/EEC on the co-ordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS IV Directive) by July 2011. The following changes are expected as a result:

- The introduction of the management company passport (MCP), which will allow an authorised management company to provide services in other member states without having to form a local fund management company. This development will centralise the control of funds.
- Changes in relation to co-operation between supervisory authorities in different countries within the EU.

- The Key Investor Information (KII) will replace the simplified prospectus. KII will:
 - be shorter and simpler;
 - disclose information in a clear and understandable manner;
 - have a standardised content.
- Mergers between UCITS will be allowed both domestically and cross-border, following a harmonised regime of disclosure to the affected investors.
- The use of master-feeder structures will be allowed so that a fund (feeder) will be allowed to fully invest its assets into another fund (master).

In addition, the Swedish government has recently proposed changes to the Swedish taxation rules for investment funds and unitholders. The proposal means that investment funds will not be obliged to pay income tax. Instead, unitholders must each year declare 0.4% of the volume of the units in an investment fund (domestic or foreign) as income of capital. The purpose of the proposal is to avoid tax differences between investing in domestic or foreign investment funds. The new tax rules are proposed to enter into force on 1 January 2011.

HEDGE FUNDS

15. Please give a brief overview of the hedge funds market in your jurisdiction. (How developed is the market? Has it been active in the past year?)

Sweden's first hedge fund was launched in the mid 1990s and the interest in hedge funds has increased since 2000. Swedish investors can often invest small amounts in hedge funds (unlike in many other countries). In 2008, hedge funds' assets comprised 5% of net fund assets in Sweden. In August 2009 there were 62 onshore Swedish hedge funds, many of which are managed by independent fund management companies.

16. What are the key statutes and regulations that govern hedge funds in your jurisdiction? What regulatory bodies are involved in regulating hedge funds?

There are no regulations in Sweden that specifically regulate hedge funds but specific rules for different categories of investment funds exist (that is, for UCITS and non-UCITS). Further, there is no legal definition of hedge funds and they are often categorised as non-UCITS since the investment restrictions applicable to UCITS are too strict (see *Question 9, Exemption*).

The key statutes and regulations are the:

- Investment Funds Act.
- SFS Regulations Governing Investment Funds (*FFFS 2008:11*).
- Swedish Marketing Act.
- SIFA's guidelines.

These are also applicable to retail funds (see *Question 2*).

17. How are the following areas regulated (if at all) in relation to hedge funds:

- **Risk.**
- **Valuation and pricing.**
- **Systems and controls.**
- **Insider dealing and market abuse.**
- **Transparency.**
- **Money laundering.**
- **Short selling**

Since hedge funds in Sweden are regulated as non-UCITS pursuant to the Investment Funds Act, the regulations regarding risk, valuation and pricing, systems and controls, and so on, are basically the same for hedge funds categorised as non-UCITS as for UCITS.

Risk. A fund management company must:

- Identify, measure, control, internally report, and verify the risks associated with its business. A fund management company must specifically ensure that its credit risks, market risks, operating risks and other risks do not, on aggregate, jeopardise its ability to fulfil its obligations to the investors, counterparties and so on. To fulfil this requirement, the fund management company must:
 - have mechanisms in place that enable continuous evaluation and maintenance of capital, which, in terms of amount, type, and distribution, is sufficient to cover the nature and level of the risks to which the fund management company is or can be exposed;
 - regularly evaluate these mechanisms to ensure that they provide full coverage.

The senior management is responsible for ensuring that the management and monitoring of risks in the activities is satisfactory.

- Have satisfactory internal controls. A fund management company must maintain an independently operating risk management function.

For activities outside of fund management, the fund management company is not subject to the independence requirement, if it can demonstrate that both:

- this requirement is not proportionate when considering the nature, scale and complexity of the business;
- the fund management company's risk management function is still functioning efficiently.

The fund management company's business plan must state:

- How the company intends to identify, measure, manage, internally report and maintain control over the risks associated with its activities.
- The company's routines and instructions concerning risk management.

Valuation and pricing. The value of an investment fund is the fund's value divided by the number of units in it. The fund's value is calculated by the fund management company in accordance with the principles stated in the fund rules. The investment fund's holdings must be valued on the basis of the applicable market value. Where investments are made in OTC-derivatives the fund rules must state specifically how these assets are to be evaluated and what valuation principles will be used.

Further, the SIFA provides guidelines for determining month-end values for performance measurement that must be considered in this respect.

Systems and controls. The fund management company is subject to various organisational requirements, including the following:

- Current and appropriate internal control mechanisms that must ensure compliance with decisions and procedures at all levels of the fund management company.
- Internal reporting and communication of information that is current and effective.
- Current and documented decision-making procedures that clearly specify reporting lines, and an organisational structure that clearly allocates functions and areas of responsibility.
- Permanent and effective compliance, risk management and internal audit functions.
- Systems and procedures for safeguarding the security, integrity and confidentiality of its information.

Insider dealing and market abuse. The fund management company must maintain current and adequate procedures to prevent, among other things, relevant persons from entering certain personal transactions (*see below*), where that relevant person either:

- Is involved in activities that can give rise to a conflict of interest.
- Has access to:
 - inside information within the meaning of the Financial Instruments Trading (Market Abuse Penalties) Act (*lagen (2005:377) om straff för marknadsmissbruk vid handel med finansiella instrument*); or
 - other confidential information relating to the fund management company's clients.

A relevant person includes:

- a member of the senior management, a partner or a manager of the fund management company;
- an employee of the fund management company and any other natural person who either performs services for the company, is under the control of the company or who is involved on behalf of the company in conducting fund activities; and
- a natural person who, under an outsourcing agreement, is directly involved in conducting parts of the fund activities on behalf of the company.

The prohibited personal transactions are personal transactions that would:

- Violate the Financial Instruments Trading (Market Abuse Penalties) Act.
- Entail the misuse or improper disclosure of confidential information or a conflict of interest.
- Be likely to conflict with the fund management company's obligations under the Investment Funds Act.

A personal transaction is defined as a trade, of a financial instrument, which is conducted by a relevant person or on a relevant person's behalf, where either:

- The relevant person is acting outside of the scope of the activities he or she carries out in his or her capacity as a relevant person.
- The transaction is carried out on behalf of any of the following persons:
 - the relevant person himself;
 - any other person with whom the relevant person has a family relationship, or with whom the relevant person has a close relationship;
 - a person whose relationship with the relevant person is such that he or she has direct or indirect material interest in the outcome of the transaction, other than a fee or commission for the execution of the transaction.

A fund management must ensure, among other things, that:

- All relevant persons are aware of the restrictions that exist regarding personal transactions and the measures established by the company regulating personal transactions and their disclosure.
- The company knows promptly of all personal transactions entered into by a relevant person, either by notification or other procedures enabling the company to identify such transactions.
- A record is kept of the personal transactions notified to, or identified by, the company.

Transparency. Subject to certain conditions, a fund management company must report in writing any change in the investment funds' holdings to the SFSA.

A fund management company must:

- Be able, at any given time, to present a list of each investment fund's holdings of all assets listed in the Investment Funds Act.
- Prepare a list of each UCITS' holdings of financial instruments on the final banking day of each quarter.
- Prepare a list of each non-UCITS' holdings of financial instruments on a date instructed by the SFSA.
- Calculate and report to the SFSA, on the last calendar day of every month, the non-UCITS' risk level in accordance with the "standard deviation" (that is, performance of the fund), performance during the past month and the "concentration risk" (that is, assets of the fund).

An application for authorisation to acquire shares requires an ownership assessment if the application concerns authorisation

to acquire a qualifying holding of shares in a fund management company. Ownership assessment applies to all of the following:

- The buyer of shares as a legal or natural person.
- If a legal person, the buyer's members, alternate board members, managing directors and deputy managing directors.

Generally a fund management company must also conduct its operations in a manner that ensures that:

- The public's confidence in the fund market is maintained.
- The individuals' capital investments are not unduly jeopardised.
- The operations are otherwise deemed to be sound.

Money laundering. Money laundering is regulated by the Money Laundering and Terrorist Financing (Prevention) Act (*lagen (2009:62) om åtgärder mot penningtvätt och finansiering av terrorism*), which implemented Directive 2005/60/EC on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing. The Act complies with other relevant EC Directives.

A fund management company must, in its fund operations, comply with the anti-money laundering provisions in the Money Laundering and Terrorist Financing (Prevention) Act and apply the relevant customer due diligence requirements to identify their clients and ascertain relevant information.

Short selling. A management company can use techniques and instruments relating to transferable securities, including securities borrowing, and money market instruments for the purpose of efficient portfolio management.

The fund management company can sell securities that are held by the investment fund (for example, borrowed securities) (that is, engage in short selling). However, a management company cannot sell securities which are not held by the fund. Therefore, naked short selling (that is, selling a financial instrument short without first borrowing the security or ensuring that the security can be borrowed, as is done in a conventional short sale) is not possible, unless a special exemption applies to a non-UCITS.

18. Who can market hedge funds?

Pure marketing of investment funds such as UCITS and non-UCITS does not require authorisation from the SFSA. However, conducting fund operations (for example, selling fund units) requires authorisation (*see Question 4*).

19. To whom can hedge funds be marketed?

Domestic hedge funds (organised under the Investment Funds Act as non-UCITS) can be offered to the public in the same way as UCITS.

20. Who holds the portfolio of assets? What regulations are in place for its protection?

The portfolio of assets is held by a depository. (For more information, see *Question 7*.)

21. Describe the key disclosure or filing requirements (if any) that must be done by the fund (for example, in relation to the prospectus or offering memorandum and side letters).

The fund management company must maintain the following documents for both UCITS and non-UCITS:

- **Fund rules.** The fund management company must prepare fund rules for each investment fund. The fund rules must regulate, among other things:
 - the principles underlying the focus of the fund's investments and the investment of the fund's assets;
 - whether dividends will be paid;
 - the calculation of the value of the fund and its units;
 - the calculation of the sale and redemption price of the units in collective investment undertakings, and when and where the sale and redemption price for the units in fund must be published;
 - the fund management company's fees; and
 - the fund's management.

In respect of a non-UCITS, information must be provided as to whether the fund is intended for the public or a limited group of investors. The group of investors must be identified. The fund rules must also contain information regarding the extent to which the non-UCITS deviates from provisions applicable to UCITS, the risk level, and the manner in which risks are evaluated.

- **Full and simplified prospectuses.** A full prospectus (*informationsbroschyr*) and a simplified prospectus (*faktablad*) must be maintained in respect of each investment fund. A full prospectus must contain, among other things:
 - the fund rules (*see above*);
 - any additional information required to assess the investment fund and the risks associated with investing in it;
 - a clear and readily understandable explanation of the investment fund's risk profile;
 - the information regarding the services and functions that may be delegated to a third party by the fund management company;
 - where the fund manager is entitled to a performance-based management fee:
 - an easily comprehensible calculation of the fee model;
 - an explanation of how the fee model works;
 - a description of any effects which the fee model may entail for the unitholder.

The simplified prospectus must, in a readily understandable and concise manner, contain basic information required to assess:

- the investment fund;
- the risks associated with investing in the investment fund.

The simplified prospectus may be attached to the full prospectus as a detachable part.

22. What are the key requirements that apply to managers/operators of hedge funds?

See *Question 6*.

23. What are the main legal vehicles used to set up a hedge fund and what are the key advantages and disadvantages of using these structures? What are the participants' interests in the fund called (for example, share or unit)?

A Swedish hedge fund is typically classified as a non-UCITS and set up as a Swedish registered non-UCITS (see *Question 16*). A fund management company can establish a Swedish non-UCITS. In addition, a foreign non-UCITS established in another EEA country can apply for a licence in Sweden, provided it has a Swedish investment manager.

For example, it has become more common for Luxembourg registered non-UCITS to be marketed and sold in Sweden and for the investment management of the non-UCITS to be outsourced from the Luxembourg fund management company to a Swedish investment manager. Such a foreign non-UCITS could be structured as either:

- A contractual fund (where the participants' interests are called units).
- An investment company with variable capital (where the participants' interests are called shares).

However, for a Swedish investment manager to act as investment manager for a foreign non-UCITS, the investment manager must be licensed as an investment firm that provides discretionary management pursuant to the Swedish Securities Markets Act.

One of the advantages of a foreign non-UCITS structure is that the Swedish investment manager only needs to be licensed as an investment firm, rather than a fund management company. A disadvantage is that the licensing process in relation to the foreign non-UCITS is almost as extensive as for a Swedish non-UCITS.

24. What are the advantages and disadvantages of using onshore and offshore structures?

Onshore

The main advantages of an onshore fund are its:

- Fairly straightforward structure.

- Ability to be marketed and sold to any investor. Certain investors such as Swedish insurance companies and pension funds can be limited to invest primarily in onshore funds.

Offshore

An offshore fund offers a number of advantages over an onshore fund. It:

- Is cheaper to establish.
- Is less regulated.
- Offers tax benefits for investors.
- Is subject to fewer investment restrictions.

However, a main disadvantage of an offshore fund is that it may not in all cases be marketed and sold to the public in Sweden.

25. Describe the tax treatment for:

- Funds.
- Resident investors.
- Non-resident investors.

See *Question 11*.

26. Can participants redeem their interest? Are there any restrictions on the right of participants to transfer their interests to third parties?

See *Question 11*.

27. Please summarise any proposals for the reform of hedge fund regulation in your jurisdiction.

On 30 April 2009, the European Commission published a draft Directive on Alternative Investment Fund Managers (AIFM Directive). The European Commission intends the AIFM Directive to establish a common regulatory and supervisory framework for all investment managers of funds promoted to investors in the EU that are not currently subject to regulation at European level. Swedish rules and regulations regarding hedge funds will probably be affected by the AIFM Directive. However, since the Directive is still being negotiated, it is too early to assess its effect on the Swedish rules and regulations regarding hedge funds.

CONTRIBUTOR DETAILS

**Niclas Rockborn, Nils Unckel and Caroline Walderfors
Germandt & Danielsson**
T +46 8 670 66 00
F +46 8 662 61 01
E niclas.rockborn@gda.se
nils.unckel@gda.se
caroline.walderfors@gda.se
W www.gda.se

G&D

– one of the leading business law firms in Sweden

Gernandt & Danielsson is one of the foremost and highest ranked business law firms in Sweden.

In the area of investment funds we have a particularly deep knowledge of fund establishments, asset management services and cross border issues. Also, we have a unique competence in the field of alternative investment products, including hedge funds.

Gernandt & Danielsson's practice areas include banking and finance, financial regulation, restructurings, dispute resolution, mergers and acquisitions, capital markets, real estate, competition, employment and benefits and TIME.

Gernandt & Danielsson

Hamngatan 2, Box 5747
SE-114 87 Stockholm

Tel +46 8 670 66 00

Fax +46 8 662 61 01

www.gda.se