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"European Private Equity-Fund for Entrepreneurs and the Impact on Market Growth within the Boundaries of the European Union."

Autor:
Ralf Mauer

Directores:
Prof. Dr. Mª Dolores García Pérez
Prof. Dr. Roland Wolf

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Prof. Dr. Mª Dolores García Pérez and Prof. Dr. Roland Wolf as Directors of the Doctoral Thesis "European Private Equity Fund for Entrepreneurs and the Impact on Market Growth within the Boundaries of the European Union" by Mr. Ralf Mauer in the Departamento de Ciencias Sociales, Jurídicas y de la Empresa, **authorizes for submission since it has the conditions necessary for his defense.**

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Prof. Dr. Mª Dolores García Pérez

Prof. Dr. Roland Wolf

Tercer Ciclo. Vicerrectorado de Investigación
Campus de Los Jerónimos. 30107 Guadalupe (Murcia)
Tel. (+34) 968 27 88 22 • Fax (+34) 968 27 85 78 - C. e.: tercerciclo@pdi.ucam.edu

PREFACE

“"Most of the creations of the intellect or fancy pass away for good after a time that varies between an after-dinner hour and a generation. Some, however, do not. […] These we may well call the great ones. […].”

(Joseph A. Schumpeter, 1883 – 1950)

When considering the above quote, one can ask onself, what is being done to promote these unique and great things? As an honorary business start-up consultant for the Bochum start-up competition (now business promotion) in Germany, I have found that there are enough great innovative ideas and good business plans for potential entrepreneurs. The most striking problem, however, remains the lack of financial support (equity) for entrepreneurs. What must be done to ensure that more equity providers are engaged? It is the main goal of this dissertation to find the answers to this very important question. To do this, the dissertation looks to the industry that provides equity - the private equity industry - and considers its current fiscal framework. The basic assumption is that if the conditions for the supporters are better, they will be more committed. The return benefits in turn ultimately benefit the entrepreneurs. The idea to write this dissertation was created by the progressive need to help business founders to implement their projects. In addition, as a lecturer at the FOM College of Economics & Management in Germany, I have gained access to many helpful discussions. My thanks for that.

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ACRONYMS AND ABBREVIATIONS

AIF	Alternative Investment Fund
AIFM	Alternative Investment Fund Manager
AIFMD	Alternative Investment Fund Manager Directive
AO	Abgabenordnung (German) = General Tax Code
AStG	Außensteuergesetz (German) = Foreign Tax Act
AVCO	Austrian Private Equity and Venture Capital Organisation
BaFin	Bundesanstalt für Finanzen (German) = Federal Financial Supervisory
BAO	Bundesabgabenordnung (German) = Federal Tax Code
BFH	Bundesfinanzhof (German) = Federal Fiscal Court
BVK	Bundesverband Deutscher Kapitalbeteiligungsgesellschaften (German) = Federal Association of German Venture Capital firms
CPI	Consumer Price Index
CRO	Chief Restructuring Officer
CSSF	Commission de Surveilance du Secteur Financier (French) = Financial Sector Supervisory Commission
DAX	Deutscher Aktien Index (German) = German Stock Market Index
DCF	Discounted Cash Flow
DD	Due Diligence
DTA	Double Taxation Agreement
EAGF	European Agricultural Guarantee Fund
EARFRD	European Agricultural Fund for Rural Development
EBITDA	Earings before Interests Taxes Depreciation and Amortisation
ECB	European Central Bank
EEA	European Economic Area
EFF	European Fischers Fund

EFSI	European Fund for Strategic Investments
e.g.	Exempli gratia (Latin) = for example
ESF	European Social Fund
ERDF	European Regional Development Fund
ESMA	European Securities and Markets Authority
EStG	Einkommensteuergesetz (German) = Income Tax Act
et al.	Et alii (Latin) = and others
et seqq.	Et sequential (Latin) = and those which follow
EU	European Union
€	Euro, Euros (currency)
EVCA	European Private Equity & Venture Capital Association
FCP	Fonds Commun de Placement (French) = Mutual Fund
FMA	Financial Market Authoritiy
GDP	Gross Domestic Product
GmbH & Co. KG	Gesellschaft mit beschränkter Haftung und Compagnie Kommanditgesellschaft (German) = Private Limited Partnership
G20	Acronym for Group of twenty major industrialized and emerging countries
GewStG	Gewerbesteuergesetz (German) = Trade Tax Act
HGB	Handelsgesetzbuch (German) = Commercial Code
HICP	Harmonized Index of Consumer Prices
H_0	Null hypothesis
I	Interests
i.e.	Id est (Latin) = that is
InvG	Investmentgesetz (Investment Law)
InvMARisk	Minimum Requirements for Risk Management
InvStG	Investmentsteuergesetz (German) = Investment Tax Act
IPO	Initial Public Offer

IPR	Intellectual Property
IRR	Internal Rate of Return
JASPERS	Joint Assistance in Supporting Projects in European Regions
JEREMIE	Joint European Resources for Micro to Medium Enterprises
JASMINE	Joint Action to Support Micro-finance Instistutions in Europe
JESSICA	Joint European Support for Sustainable Investment in City Areas
KAG	Kapitalanlagegesellschaft (German) = Investment Trust
KAGB	Kapitalanlagegesetzbuch (German = Investment Code
KapESt	Kapitalertragsteuer (German) = Gains Tax
KG	Kommanditgesellschaft (German) = Limited Partnership
km^2	Quadratkilometer (German) = square kilometer
KSt	Körperschaftsteuer (German) = Corporation Tax
KStG	Körperschaftsteuergesetz (German) = Corporate Tax Act
KVG	Kapitalverwaltungsgesellschaft (German) = Financial Investment Management Company
LBO	Levereged Buyout
LP	Limited Partnership
MFG	Mittelstandsfinanzierungsgesellschaft (German) = SME Financing Corporation
MiFiG	Mittelstandsfinanzierungsaktiengesellschaft (German) = SME financing joint-stock company
M-IRR	Modified Internal Rate of Return
MBI	Management Buy-in
MBO	Management Buyout
NA	National Accounting
NOI	Net Operating Income
NDP	Net Domestic Product
NPV	Net Present Value

OECD	Organization for Economic Co-Operation and Development
OTC	over-the-counter
PPS	Purchasing Power Standard
ROA	Return on Asset
ROE	Return on Equity
SA	Société Anonyme (French) = Stock Corporation
SARL	Société à responsabilité limiteé (French) = Limited Liability Company
SCA	Société en commandite par actions (French) = Partnership Limited by shares
SCOSA	Société cooperative d´actions (French) = Cooperative in the legal form of a stock coporation
SCSp	Société en commandite spéciale (French) = Special Limited Partnership
SECS	Société en commandite simple (French) = Limited Partnership
SICAR	Société d'investissement en capital à risqué (French) = Risk Capital investment Company
SICAV	Société d´Investissement de Capital à risqué (French) = Risk Capital Investment Corporation
SIF	Specialized Investment Fund
SOPARFI	Société de Participations Financieres (French) = Associated Company
SPE	Special Purpose Entitiy
SPD	Sozialdemokratische Partei Deutschlands (German) = Social Democratic Party of Germany
SPV	Special Purpose Vehicle
StAnpG	Steueranpassungsgesetz (German) = Tax Adaption Act
STOXX	Alternative to stocks
TFEU	Treaty on the Functioning of the European Union
UCI	Undertakings for Collective Investment

UCITS	Undertakings for Collective Investment in Transferable Securities
UK	United Kingdom
UmsG	Umsetzungsgesetz (German) = Implementation Act
UntStRefG	Unternehmenssteuerreformgesetz (German) = Corporate Tax Reform Act
USA	United States of Amerika
UStG	Umsatzsteuergesetz (German) = Value Added Tax Act
VAT	Value-Added Tax
WACC	Weighted Average Cost of Capital
%	Percent(age)

1 INTRODUCTION

1.1 PREAMBLE

1.1.1 **Emotional Situation in Europe**

"Whoever does not believe in Europe, who doubts Europe, whoever despairs of Europe, should visit the military cemeteries in Europe."

(Jean-Claude Juncker, President of the European Commission)[1]

Not least because of the problems of some countries within the European Union (EU), it is necessary to obtain stability within the European Economic Area. Some countries such as France and Italy (Broyer, Renner, Schneider, & Utermöhl, 2014, pp. 11-18) have already wanted to deviate from the stipulated budget deficit limit of 3 percent. The economic downturn in Europe is increasingly impeding the adherence to the self-imposed goal to carry out an austerity plan for the consolidation of markets. Countermeasures, such as the ones taken by Mario Draghi, president of the European Central Bank (ECB) since November 1, 2011, who has prompted the reduction of the key interest rate[2] by the ECB from 0.05 percent (Fischer & Hennersdorf, 2014, p. 18) to now 0.00 percent (Wirtschaftswoche, 2016) or the promotion of a further coalescence of the markets, are supposed to help the sluggish economy throughout the Eurozone back up on its feet. A functional European Single Market (Neumair, Schlesinger, & Haas, 2012, p. 460) is mainly dependent on the free movement of goods, free movement of persons, the free transaction

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[1] Speech on 16.11.2008 from Jean-Claude Juncker in Congress on Rememberance Day 2008. At the time he was still Prime Minister of Luxembourg.

[2] Also central rate. The key interest or central rate is fixed by the European Central Bank for the countries of the euro zone. The key interest rate is the interest rate for which banks can borrow money from the central bank itself. Thus the key interest rate determines how expensive a loan from the European Central Bank for the credit institutions is (Wildmann, 2015, p. 158 et seqq.).

of capital and the free exchange of services. Most of these areas encounter quite extensive problems. As there is indeed a price convergence in goods, the price differences for services – or exemplary in the electricity market (Hitzeroth, 2012, p. 11) – are still blatant. There are still significant opportunities for improvement in regards to the infrastructure as well. Plans of the European Commission to launch initiatives and invest billions of Euros in transport, energy and information technologies (Corner, 2014, p. 203) could not be complied (Lucke, 2014, p. 142) with because the heads of state reduced the multi-year financial framework of the Connecting-Europe-Facility. These general obstacles need to be eliminated. Already in 2009, the former president of the European Commission, José Manuel Barroso[3] had cited the deepening of the internal market as being one of the main priorities for the future of the European economy. However, this project is also influenced by the still not fully overcome debt crisis, which was caused by the turmoil throughout the international financial market and had reached its peak during fall of 2008 with the collapse (De Haas & Van Horen, 2013, p. 244) of the investment bank, Lehman Brothers (Soros, 2009, p. 25).

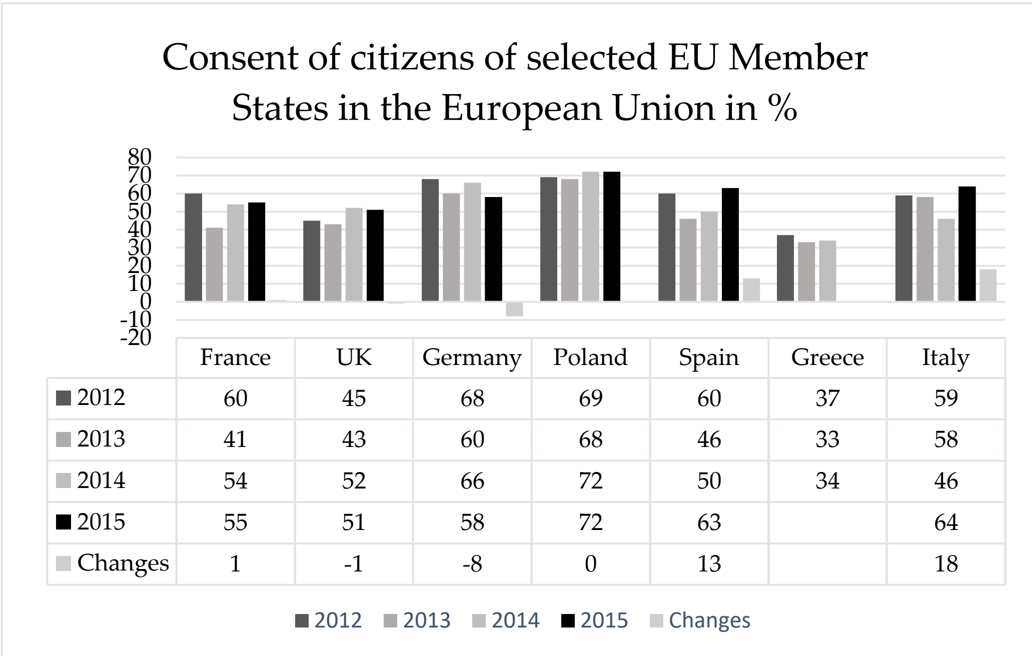
These disruptions developed into the most important and most fatal global economic and financial crisis since the Great Depression with its "Black Thursday" – or "Black Friday" due to the time difference in Europe – on October 24, 1929, hitting also and in particular the European Union.

Europe was a place that enticed high hopes for almost one decade. Limitless freedom (Gebhardt, Glaser, & Lentz, 2013, pp. 2-25) to travel and the prospect of undisturbed trade was terrific. Meanwhile, many do have concerns regarding the future success of the European Union. The trust in the European Union (EU) is only slowly gaining momentum again. Merely the Euro seems stable in its popularity. While the approval rate for the EU had stood at 60 percent in 2012, according to a study (PewResearch, 2014, p. 3) of the Pew Research Center, a polling institute

[3] As from November 2014, Jean-Claude Juncker from Luxembourg is the new president of the European Commission (Friedrichs, 2015, p. 63). This marks an historic situation, since he is the first president of the European Commission, more or less having been elected by the people, which illustrates the expansion of the significance of the European Union (europarl, 2014).

with a neutral position towards the European Union and based in Washington D.C., this value took a nose-dive by 2013 with only 46 percent of the EU – with Greece – and 52 percent without Greece - citizen polled showing a positive attitude towards the EU. A survey, also conducted by the Pew Research Center from March 17 through April 9, 2014, suggested a slight improvement of the situation within the EU. Out of the 7.022 persons surveyed in seven member states - France, Germany, Greece, Italy, Poland, Spain and the United Kingdom, now 52 percent - with Greece – and 53 percent without Greece - of the respondents were in favor of the EU and stated that the integration of their own countries into a European economy is good. In figure 1, the sensitivities, respectively the consent of the citizens of these member states from 2012 to 2015 are displayed.

Figure 1: Consent of Citizens of selected EU Member States in the EU in %



	France	UK	Germany	Poland	Spain	Greece	Italy
2012	60	45	68	69	60	37	59
2013	41	43	60	68	46	33	58
2014	54	52	66	72	50	34	46
2015	55	51	58	72	63		64
Changes	1	-1	-8	0	13		18

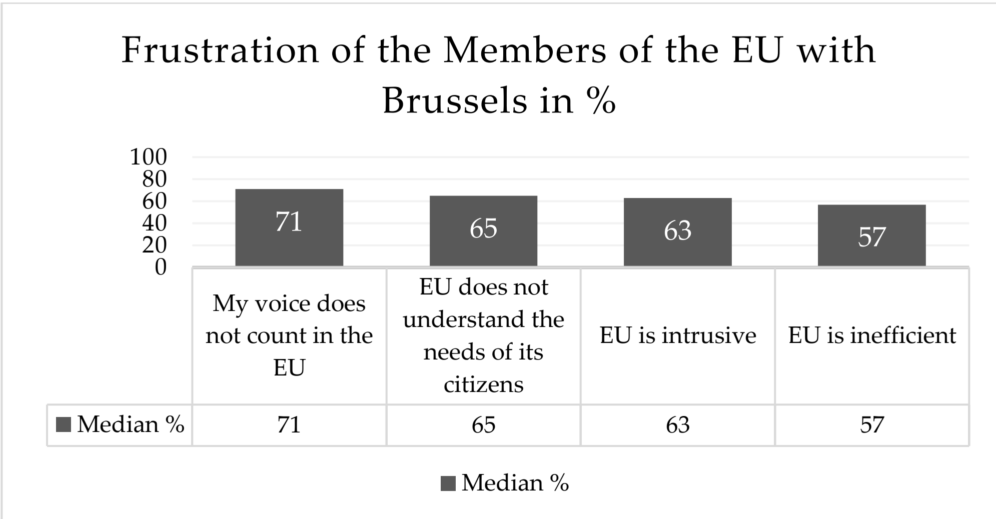
Source: Own representation based on PewResearch, 2014 and 2015.

In 2015, a new study (Stokes & Oates, 2015, pp. 1-36) of PewResearch Center was conducted (April 7, 2015 to May 13, 2015) with a total of 6.028 citizens. They were interviewed by phone or in Poland and Italy face to face. The study found (Stokes

& Oates, 2015, pp. 1-36) that Italy and Spain now believe more in the European Union (Stokes & Oates, 2015, pp. 1-36), while the consent of United Kingdom and especially in Germany subsides (integrated in figure 1) so that the so-called Brexit of the United Kingdom from the European Union (EU) after the referendum of June 23, 2016 was not very surprising (Stokes & Oates, 2015, pp. 1-36), although 55% of respondents had chosen to remain in the EU since 2015 (Stokes & Oates, 2015, pp. 1-36). Greece has made no predictions for this new study.

Even though consent seems to slightly recover, skepticism in states such as Greece is still particularly high. Primarily the Greeks, which have been hit especially hard by the crisis, are extremely skeptical in regards to the European idea. In its biggest crisis, Europe is tattered.

Figure 2: Frustration of the Members of the with Brussels in %



Source: Own representation based on PewResearch, 2014 and 2015.

Overall, the citizen in detail, even if he appreciates the economic integration in a more positive aspect again (Koppelberg & Schlotmann, 2014, p. 30), is hardly of the opinion that his interests are being protected adequately. This is being illustrated in figure 2.

The difficulties in solving the debt and economic crisis, leaves the Europeans anxious. The impression has arisen that the divide between the citizens and politicians throughout the European politics has become larger (Herrmann, 2014, p. 123). It has been repeatedly suggested that reducing this gap is taking a high priority on the agenda in order to prevent the development respectively the extension of elites (Kirt, 2016, p. 1).

Almost grotesque, yet understandable in this context is the awarding of the Nobel Peace Prize to the European Union (Dittrich, 2016, p. 1) for over six decades of contributing to the development of peace and reconciliation, democracy and human rights, which should possibly appease the citizens (Ruf, 2014, p. 52).

Regardless of such surveys concerning the mood, it can be agreed that under the deepening of the internal market as defined by Barroso, not only the clarification of questions of detail regarding the facilitation of trade relations are to be understood, but also and foremost the growth of the European market, long to be identified as independent.

That the growth, of which the Chancellor of the Federal Republic of Germany, Dr. Angela Merkel spoke (Merkel, 2003, p. 13), must be responsible especially for the future Wealth of Nations, already prophesied by Adam Smith (List, 2012, p. 205), is beyond dispute, an infinite growth, on the other hand, surely at least arguable. A key driver for the growth of an economy are new foundations and further development of businesses, which not only create jobs (bmwi, 2014), but are also responsible for transfer payments such as taxes and interest and provide impetus for other companies such as suppliers. The support of these companies, e.g. in the sense of providing equity and improved framework needs to be a central task in the future of the EU, if she is to rationally oppose the recession of the economic growth.

1.1.2 Motivation, Private Equity Cycle and Research Situation

"We need increased willingness to be independent, better fiscal conditions, and more innovation-friendly banks."

(Roman Herzog, Federal President of Germany from 1994 – 1997)[4]

Motivation

Becoming self-employed is part of the growing process. Every market and thus every economic space lives and thrives on growth (Aaker, 1989, p. 188; Schmidt R. , 2015, p. 33; Vries, 2013, p. 461). It is undisputed that entrepeneurs in sense of business founders can contribute significantly to this growth through their activities (Barth, 1995, p. 4; Pohl, 2014, p. 62; Leineweber, 2003, p. 79). They – as mentioned above – create jobs, pay taxes and in some cases even help suppliers to get orders (Lahn, 2015, p. 13; Hölzle, Puteanus-Birkenbach, & Wagner, 2014, p. 40). Unfortunately, it is not always easy for entrepreneurs.

The present work pursues an approach to facilitate access to funds for entrepreneurs who are often unable to finance their ideas. Access to funds from banks is sometimes not possible or incredibly difficult. Banks want collaterals that many founders often do not have (Möckel, 2005, p. 158 et seqq.; Brettel, Rudolf, & Witt, 2005, p. 193; Schneider S. , 2015, p. 24). Regrettably, banks do not provide current low interest rates to start-ups (Soisses, 2014, p. 56; Schmale, 2015, p. 1). Companies that provide private equity - so-called private equity or venture capital companies - can help in these cases (Nathusius, 2001, p. 145; Kollmann T. , 2016, p. 83 et seqq.). However, unclear and, above all, inconsistent tax regulations provide for the partial restraint on this market. The proposed tax harmonization is not yet sufficient (Biebinger, 2015, p. 148; Pressrelease, 2014). For this reason, tax-related parameters are determined in this work, which are optimized (unified) for such companies and

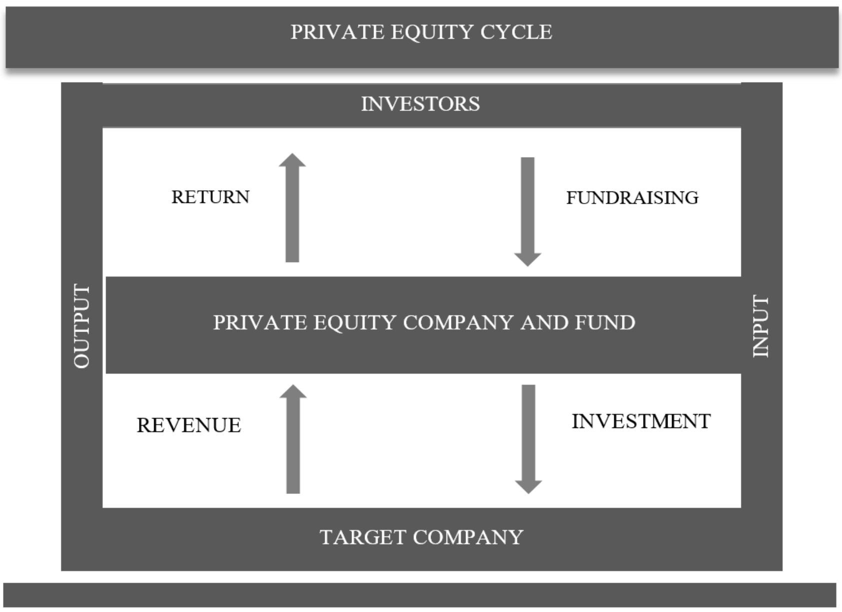
[4] Own translation – original quote (German): „Wir brauchen mehr Bereitschaft zur Selbständigkeit, bessere steuerliche Rahmenbedingungen dafür und etwas innovationsfreundlichere Banken." Address by Federal President Roman Herzog on the occasion of the opening of the Hanover Fair '96, Herzog (1996).

their funds (funds are designated for certain purposes – in this case the provision of equity capital) and thus create a completely new type of fund. By unifying the taxation of private equity companies, this restraint could cease. The increased involvement of such companies would benefit entrepreneurs, because more of these companies would result in more money, which can flow as equity in business start-ups. This again creates growth.

Private Equity Cycle

Basically, three groups of stakeholders are involved in the Private Equity market (Bayaz, 2013, p. 46; Grethe, 2010, p. 65; Hehn, 2011, p. 50): the investors as equity holders, the Private Equity firms and the target company - including portfolio companies (Bandulet, 2005, p. 40) - as equity buyers (Bandulet, 2005, p. 40; Bayaz, 2013, p. 46, Grethe, 2010, p. 65).

Figure 3: Private Equity Cycle



Source: Own model based on Gebhardt, G., 2009, pp. 71-90.

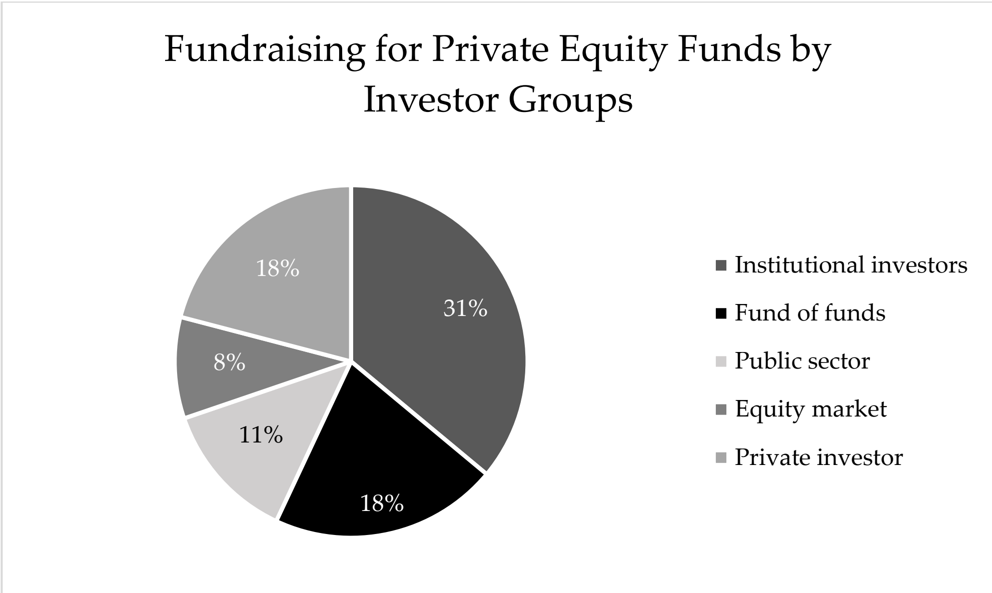
With an investment of debt as part of a total corporate acquisition (Geidner, 2009, p. 30), banks are further participants (Kraft, 2001, p. 34) within this business model (Bandulet, 2005, p. 40; Geidner, 2009, p. 30; Kraft, 2001, p. 34). Such a cycle (Gompers, Kovner, Lerner, & Scharfstein, 2008, pp. 1-23) might look like figure 3 on page 7 (Gebhardt G., 2009, pp. 71-90; Grethe, 2010, p. 65; Mauer, 2015, pp. 140-143).

Consultants and management companies complete this model (Gebhardt G. , 2009, pp. 71-90). In order to obtain a cycle in the sense of the graphic chart in figure 3, this model needs to be supplemented by an input – in this case the fundraising and investment – and an output – here the revenues and returns.

At the beginning of a Private Equity (Caselli, 2010, p. 36) investment, there is the soliciting of funds and the fundraising (Metrick & Yasuda, 2011, pp. 619-654), which will be explained in more detail below. To do so, a Private Equity firm launches a fund to pool capital for participation in a company (Hannich, 2012, p. 7). This fund collects the monies (Balz & Arlinghaus, 2007, p. 419) from banks, insurance companies, pension funds, corporations and private investors (Balz & Arlinghaus, 2007, p. 419; Grethe, 2010, p. 67; Vogt, 2007, p. 40). In the consideration of Private Equity investments, the individual investment areas are being identified according to the life cycle phases, respectively the activities of the funded target companies as described in detail in 2.1.2.2. Revenues arising from the investment in the target company from the sale of shares or the returns (Marquez, Nanda, & Yavuz, 2015, pp. 1783-1823) from, for instance, a silent participation are then adjusted for the amounts (Bernhardt, 2010, p. 89) deriving from expense allowances withheld by the Private Equity Company, returned to the investors (Hehn, 2011, p. 53), which in turn satisfy their customers with the corresponding expected returns (Bernhardt, 2010, p. 89; Hehn, 2011, p. 53; Marquez, Nanda, & Yavuz, 2015, pp. 1783-1823).

The way to the emergence of a Private Equity transaction (Koester, 2011, p. 261) is initially paved by the investors (Grethe, 2010, p. 67; Koester, 2011, p. 261; Pankotsch, 2005, p. 2). Its success depends on their readiness to invest in such a quite risky undertaking. Because of the generally very high minimum investment amounts required (Brettel, Kauffmann, Kühn, & Sobczak, 2008, p. 16), it may well be assumed that the investors in the asset class Private Equity (Pankotsch, 2005, p. 2) display a high level of professionalism (Bayaz, 2013, pp. 46-47; Pankotsch, 2005, p. 2; Brettel, Kauffmann, Kühn, & Sobczak, 2008, p. 16). The most important investors, by volume, who are providing Private Equity firms with means in fundraising, are first and foremost – as mentioned above – institutional investors such as insurance companies, banks or pension funds (Bayaz, 2013, p. 46; Thum, Timmreck, & Keul, 2008, p. 16). The allocation of fundraising, which has been rather constant for some time on the different investor groups, is shown in figure 4 (Thum, Timmreck, & Keul, 2008, p. 16).

Figure 4: Fundraising for Private Equity Funds by Investor Groups



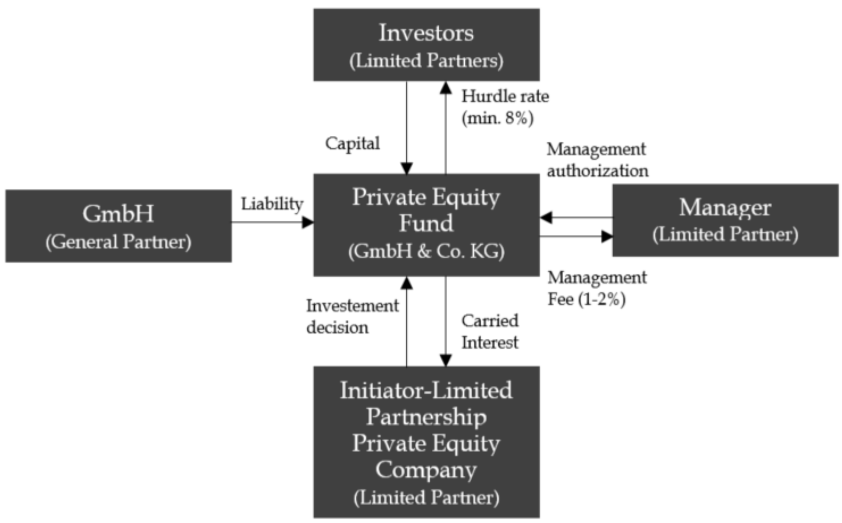
Source: Own representation. Data from Thum, Timmreck, & Keul, 2008, p.

However, funds are provided by private investors, the public sector or are collected on the capital market as well (Thum, Timmreck, & Keul, 2008, p. 16). The motive for investors to place their money in such a form of investment lays naturally in achieving a high return on their invested capital (Bayaz, 2013, p. 46; Fueglistaller, Müller, & Volery, 2008, p. 137).

Many institutional investors are approaching Private Equity via so-called Fund of Funds (Brettel, Kauffmann, Kühn, & Sobczak, 2008, pp. 24-27; Gresch & Wyss, 2011, pp. 43-58; Jugel, 2003, p. 101). In the first instance, Fund of Funds (Gresch & Wyss, 2011, pp. 43-58) are to be understood as a Mutual Fund that invests the money of the shareholders in shares of Mutual Funds (Wolf E. , 2011, p. 3). For Private Equity, this means that these funds in turn invest in Private Equity (Scharfman, 2012, p. 309). Fund of Funds are a possible and reasonable investment option also for less experienced investors (Natter, 2003, pp. 201-203) who do not want to invest in expensive research on their own, because the operator of Fund of Funds (Cumming, 2010, p. 58) is taking over the search for suitable cost objects in the class of investments of Private Equity – as far as it is to be considered as such – and is spreading the risks by distributing his monies into several Private Equity funds (Cumming, 2010, p. 58; Natter, 2003, pp. 201-203). Nearly every risk-return profile can be depicted with this particular form of a fund (Peterreins, 2008, p. 103). This construct has an unmistakable character. One positive aspect for the investor is probably that the portfolio can be broadly diversified and is actively managed (Peterreins, 2008, p. 103). In this context it should be noted that for the effective operation of the diversification, the independence of the Fund of Funds management needs to be ensured in order to prevent an increased consideration of funds of a certain house (Götzenberger, 2008, pp. 105-107). The major advantage (Born, 2009, p. 30) of the active participation in this event is being slightly clouded by the high costs such a vehicle entails (Born, 2009, p. 30; Peterreins, 2008, p. 103). The additional management level – the very Fund of Funds manager – who appears alongside the management of the target fund, naturally adds to the costs (Born, 2009, p. 30; Peterreins, 2008, p. 103).

The demeanor of Private Equity companies has a certain similarity (Reichmann, 2011, p. 210) with the exchange construct (Bayaz, 2013, p. 47; Reichmann, 2011, p. 210). On the one hand, capital is being supplied, and on the other hand, capital is being demanded (Bayaz, 2013, p. 47). The difference is just that this is preferably not done in a public place (Reimers, 2004, p. 5), but mostly over the counter (Bayaz, 2013, p. 47; Reimers, 2004, p. 5; Trübestein, 2012, p. 369). Just as the stock exchange acts as an intermediary, it is the Private Equity firm that acts as an intermediary (Witt, 2012, p. 457) between the investor and the target company (Bayaz, 2013, 47-48; Hehn, 2011, 46; Prym, 2011, p. 27; Witt, 2012, p. 457). Very often, the Private Equity companies (Cumming & Johan, 2014, p. 145) present themselves as Limited Partnerships (Bayaz, 2013, p. 48; Tcherveniachki, 2007, p. 26) or in Germany as limited partnership with a limited liability company as general partner (Gmbh & Co. KG). However, more or less rare exceptions can be found here as well. Thus, public companies, as well as other forms of corporations present themselves so in this industry (Jugel, 2003, 224; Tcherveniachki, 2007, p. 175). The Limited Partnership (Schauer, 2016, p. 51) is by its very nature, the combination of at least two shareholders (Schauer, 2016, p. 51; Scherbaum, 2015, p. 87). Here, at least one partner is completely and indefinitely liable (Müssig, 2010, p. 421 et seqq.), and at least one partner exclusively (Mühlhaus & Wenzel, 2014, pp. 87-92) with the deposit provided by him (Mühlhaus & Wenzel, 2014, pp. 87-92; Müssig, 2010, p. 421 et seqq.; Schauer, 2016, p. 51).

Figure 5: Private Equity Fund Structure



Source: Own representation.

Figure 5 is a construct of a private equity fund. For this graphic, the German GmbH & Co. KG has been simulated, since the task of the general partner is somewhat more evident in this structure than in a limited partnership which otherwise works in the same way.

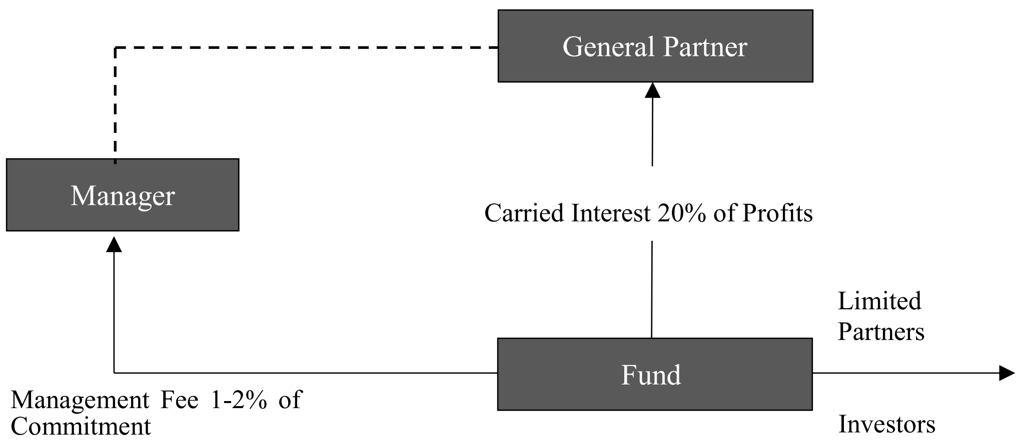
In principle, Private Equity companies do not have any interest in providing target companies with equity deriving from their own money (Bayaz, 2013, p. 48). Rather, these companies float a fund during the fundraising already indicated (Bayaz, 2013, p. 48; Daniels, 2004, 21; Prym, 2011, p. 21). In the process, the so-called General Partners (Bayaz, 2013, p. 48; Weißflog, 2014, p. 47) – thus, the partner of a partnership or, like above, the limited liability company with a limited partnership company being completely and indefinitely liable – provide 1% of the fund's capital, while 99% comes from the Limited Partners (Smith, Smith, & Bliss, 2011, p. 90). The Limited Partners are only liable (Grunewald, 2008, p. 128 et seqq.) to the amount of their capital contributed (Schauer, 2016, p. 51). The General Partners (or a management company representing the General Partners) take over the operational fund management, the investors as Limited Partners have – again based on the stock market and similar to shareholders – only controlling rights. The General Partners are being compensated with a management fee in the amount of 1-2% per annum on the capital stock and the profit share (Bayaz, 2013, p. 48) the carried interest, of approximately 20% on capital gains of the fund (Müller K. , 2007, p. 18). However, this fund remuneration is only calculated after the repayment of the capital contributions to the other limited partners plus an average minimum interest rate of 8% (the so-called hurdle rate).

In addition to their capital employed, the capital gain less the management fee and the carried interest remains with the Limited Partners (Bayaz, 2013, p. 49; Tcherveniachki, 2007, p. 26). Within the industry, the Private Equity companies are to be diversely subdivided. On the one hand, they can be subdivided according to their geographical, industrial and functional specialization, and on the other hand they can be differentiated in globally acting, more opportunistically construed financial investors (Bayaz, 2013, p. 49) – see also the empirical study on the participation types for clarification of correlations of participation motivations, for example, of companies, that purchase businesses or stocks of businesses for strategic and and financial reasons – and the active industry specialists.

It is possible and even common (Renz, 2015, pp. 26-27) for the management of a fund to be taken over by a management company.

Figure 6 is intended to illustrate the position of the manager or the management company within a private equity structure.

Figure 6: Management as General Partner in a Private Equity Investment



Source: Own model.

This structure is typically (Jugel, 2003, p. 62) designed as part of a business management contract. Therein, the management company takes over the position (Landau, 2010, pp. 27-29) of the General Partner.

Normally, a management company operates, according to their management capacity, several fund companies, which are established one after the other within a certain time (Grethe, 2010, p. 65) interval.

In general, the main motivation for target companies to turn to a Private Equity investor is the strengthening of its equity ratio (Stadler, 2013, p. 194) and to gain access to means for growth (Quelle & Woikowsky, 2011, p. 28), respectively investments (Bayaz, 2013, p. 52; Quelle & Woikowsky, 2011, p. 28; Stadler, 2013, p. 194). There are manifold reasons for wishing to strengthen the equity base. These are described in detail in the chapter regarding the reasons for Private Equity financing. Especially young, capital-intensive businesses that are in the start-up or growth phase (Kollmann & Kuckertz, 2003, p. 32), often experience difficulties in financing (Reichle, 2010, p. 1) themselves through banks or the public capital market (Bayaz, 2013, p. 52; Kollmann & Kuckertz, 2003, p. 32; Reichle, 2010, p. 1). For this reason, a large part of the capital derives from Venture Capital (Börner & Grichnik, 2005, p. 97) firms, from which the companies also expect management support (Bayaz, 2013, p. 52; Börner & Grichnik, 2005, p. 97). The alternative financing Private Equity has long extended to the circle (Bayaz, 2013, p. 53) of medium-sized (Matejun, 2008, p. 12) and family businesses (Aronoff & Ward, 2011, p. 1). Especially medium-sized companies (Wiedmann & Heckemüller, 2003, p. 73) often show a permanent lack of equity to execute investments (Bayaz, 2013, p. 53; Wiedmann & Heckemüller, 2003, p. 73). This weak equity base has fatal consequences for the company (Bayaz, 2013, p. 53). The debt ratio, which results from this strategy – or rather negative strategy – leads to a poor credit rating (Hess, 2007, p. 29), which in turn impedes the borrowing of additional debt (Bayaz, 2013, p. 53; Hess, 2007, p. 29). Meanwhile, family businesses are increasingly requesting Private Equity or considering such alternative financing in order to – another essential reason for Private Equity financing – find a succession plan in the sense of selling to an existing management or selling to a management (Bayaz, 2013, p. 53; Renner, 2016, p. 62)[5] from the outside.

Research Situation

Investments in new businesses – and this goes undisputed – is essential (Europäische Kommission, 2016) to the future of Europe. There are a number of funds, which at first sight, promise relief for regions, structures or industries (Europäische Kommision, 2014). This was started in Europe early on. The European Agricultural

[5] In contrast, there are those who say, that there are problems in the financing of family business (Schraml, 2010, p. 247) with private equity (Simon, 2012, p. 348). So there is a tension between the long-term horizon of family businesses and the relatively short-term private equity exposures (Simon, 2012, p. 348).

Guidance and Guarantee Fund for Agriculture (Hofreither, 2012, pp. 8-12), established in 1962 (Kienle, 2009, p. 1) probably counted as one of the first financial aids designated in their entirety as a structural fund. This fund was also once a very extensive fund and at last – until 2006 it was in charge of the financing (Beichelt, 2006, pp. 162-163) of the common agricultural policy of the EU – accounted for approximately half the budget of the European Union (Koerber, Männle, & Leitzmann, 2012, p. 173). Today, the funds for the development of structures and industries are the

- European Social Fund (ESF),
- the European Regional Development Fund (ERDF),
- the Cohesion Fund,
- the Solidarity Fund of the European Union,
- the European Agricultural Fund for Rural Development (EARFRD),
- the European Agricultural Guarantee Fund (EAGF),
- the European Fisheries Fund (EFF) and

other entities wishing to supportively engage (Europäische Kommission, 2015). Thus, in this context, the JASPERS (Joint Assistance in Supporting Projects in European Regions), JEREMIE (Joint European Resources for Micro to Medium Enterprises), JESSICA (Joint European Support for Sustainable Investment in City Areas) or as well JASMINE (Joint Action to Support Micro-finance Institutions in Europe) are to be mentioned (European Commission, 2015). Not quite uniformly yet in general, the ESF and the EFRE are henceforth being subsumed under structural funds (Europäische Union, 2013).

They work on the concept of co-financing (Steinrücken, 2016, p. 47), which means nothing more than the projects funded by the Structural Funds must always be supported by the public fund of the country concerned as well. The European Social Fund is also designed to be permanent, as well as the European Regional Development Fund (Rein & Schuler, 2012, p. 257 et seqq.).

It is the most important employment policy instrument of the EU (Rein & Schuler, 2012, p. 258). It was created with the formation of the European Economic Community (Heise, 2014, p. 6) in 1957 and launched in 1958, at which the production and strengthening of regional competitiveness was issued as the goal (Becker S. , 2003, p. 183 et seqq.) of this fund (Rein & Schuler, 2012, p. 257 et seqq.; Becker S., 2003, p. 183 et seqq.). It is used to promote growth and employment in the regions least developed (Rein & Schuler, 2012, p. 257 et seqq.; Becker S., 2003, p. 183 et seqq.). It aims to improve employment opportunities in these regions and to help people through education and training (Rein & Schuler, 2012, p. 257 et seqq.; Becker S., 2003, p. 183 et seqq.). Furthermore, it is set to contribute to the reduction of inequities, disadvantages and discriminations in the labor market (Rein & Schuler, 2012, p. 257 et seqq.; Becker S., 2003, p. 183 et seqq.). So should – by volition of the European Union – all people receive a professional perspective (Rein & Schuler, 2012, p. 257 et seqq.; Becker S., 2003, p. 183 et seqq.). In the process, each region, respectively each Member State shall develop its own strategy in the context of an operational program (Rein & Schuler, 2012, p. 257 et seqq.; Becker S., 2003, p. 183 et seqq.). The funds from the European Social Fund can be requested, for example, by public authorities or charities that are active in the field of employment and social inclusion (Saarland, 2016, p. 1). The European Regional Development Fund is targeted into a similar direction. It is the most important instrument of regional development of the European Union, supporting regions which are showing development deficits and structural problems. Under article 176 (Brandenburg, 2014, p. 41) of the TFEU (Treaty on the Functioning of the European Union (AEUV – Vertrag über die Arbeitsweise der Europäischen Union)) the purpose of this fund is to:

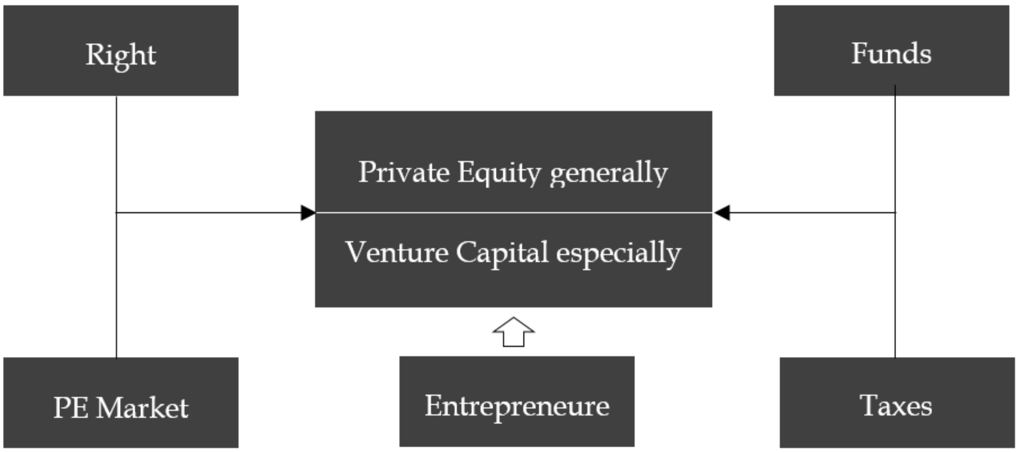
„…., help to redress the most significant regional imbalances in the Union by participating in the development and structural adjustment of underdeveloped areas and the restructuring of industrial regions with regressive development." (Anikor, 2014)

The European Regional Development Fund primarily finances investments to strengthen business competitiveness and job creation in small and medium-sized enterprises (Kirchhof & Kreuter-Kirchhof, 2012, p. 82). However, a promotion of measures is possible, which are relevant to the environment, such as the development of technologies that are conducive to energy efficiency. It goes without saying that the Structural Funds as well as the other provided funds are very helpful.

This work is essentially not about intervening in the structure of funding or to even provide an additional fund that could be accessed in particular by entrepreneurs or managers of Private Equity funds. Instead, it is about the fact that a well-known phenomenon, or rather an industry and its dependents could be granted better options as it has been the case thus far. The participation of companies in and with other companies through the provision of Equity Capital (Private Equity) is of paramount importance for the European Union. The economic relevance of Private Equity, which provides equity and detaches the supported enterprises from the banks (Heyke & Stahl, 2010, p. 28), shows itself significantly in an economically uncertain environment and the associated reluctance in the lending policy of banks. Relatively independent from economic activities, Private Equity companies can invest in sustainable and promising companies, using the funds launched by them for that very purpose. Therewith, they support the creation of new jobs and the preservation of the innovative capacity of a nation. Private equity is a major contributor to the development of high-tech industries, information, communications, biotechnology and medical technology, and should actually go above that. It is well known, that – compared to other companies - Private Equity firms performed much better (Gottschalg & Schramm, 2013) in the past as well, thus showing considerably stronger growth rates, creating more jobs and investing higher volumes in research and development (Cerqua & Pellegrini, 2014, pp. 115-126). However, due to the differing views of the Member States concerning the treatment of Private Equity funds, a not only imaginary bolt has been placed before more extensive activities so far.

The private equity business therefore plays an important role in the global financial economy (Lucks & Meckl, 2015, p. 36; Schüle, 2015, p. 18 et seqq.). The fact that a private equity investment brings the expected profit to the investor is not least due to the particular tax conditions in the country in which the company's stake was acquired (Groh, 2004, p. 29 et s; Jesch, 2004, p. 157 et seqq.). The taxation of profits from the sale of company interests is of particular relevance (Jesch, 2004, p. 157 et seqq.). Overall, private equity (PE) is influenced by a variety of things. In addition to taxation, these are the legal framework conditions which later lead to fiscal treatment, the private equity market in general, the fund structures of the individual member countries of the European Union and, in particular, financing in the early stages of a company (Venture capital) the entrepreneurs addressed here. Figure 7 is intended to illustrate this.

Figure 7: Influencing Variables on Private Equity (PE)



Source: Own representation.

When speaking of private equity, there are two main stocks. Some speak of the opportunities and the others of the risks of private equity. Thus, discussed is, on the one hand, the economic importance, while on the other hand, the risks in the sense of company purchases which are charged to the acquired company. For example, Bayaz (2014, p. 39) and Achleitner, Schramel and Tappeiner (2011, p. 9) argue that the private equity market has gained in importance. On the legal side, too, a lot has been done in recent years to make private equity and venture capital more interesting in Europe.

The AIFM Directive 2011/61 / EU (Alternative Investment Fund Manager Directive), which had to be implemented in the Member States of the European Union (EU) on 22 July 2013, initially set strong regulation in response to the financial crisis (Postler, 2015, p. 5 et seqq.; Sixt, 2014, p. 175 et seqq.). However, this should also create a clear structure (Postler, 2015, p. 5 et seqq.; Sixt, 2014, p. 175 et seqq.). The EuVECA Regulation (European Regulation on European Risk Capital Funds) of 17 April 2013 goes further (Hoffmann-Riem, 2014, p. 413 et seqq.; Gogarn, 2015, p. 4 et seqq.). This regulation is intended to ensure that the obstacles to cross-border fundraising and the creation of a Europe-wide level-playing field for venture capital funds are eliminated (Hoffmann-Riem, 2014, p. 413 et seqq.; Gogarn, 2015, p. 4 et seqq.). This European venture capital fund will facilitate access to start-ups for financing (Hoffmann-Riem, 2014, p. 413 et seqq.; Gogarn, 2015, p. 4 et seqq.). Through the uniform regulation of this fund, the EU hopes that investor-backed investors will have more confidence (Hoffmann-Riem, 2014, p. 413 et seqq.; Gogarn, 2015, p. 4 et seqq.). This regulation has not yet had any success (Schwarz & Hillebrand, 2016, p. 60). A further consideration is the European Investment Fund, which was established in 1994 and is based in Luxembourg (Europäische Union, 2016). Its main shareholders are the European Investment Bank, the European Commission and various European banks and financial institutions (Europäische Union, 2016). The task of risk capital financing in favor of small and medium-sized enterprises provides that the financing is not directed to companies, but rather to private banks.

Also the private equity market, which has organized itself in associations in the respective national states (eg BVK as the German Association of German Equity Companies for Germany, AVCO as Austrian Private Equity and Venture Capital Organization for Austria, LPEA as Luxembourg Private Equity & Venture Capital Association for Luxembourg), as well as the umbrella organization EVCA (now Invest Europe) as European Venture Capital and Private Equity Association, are working to improve the framework for private equity. In this way, the associations demand that the taxation of management fees be abolished and the tax conditions be made more transparent. BVK (see above) calls for a list of measures, specifically the amendment of the Income Tax Act, the Corporate Income Tax Act, the Trade

Tax Act and the Value Added Tax Act. The Investment Tax Act is also to be amended. The measures to be taken are: transfer of profits for the promotion of participation in small and medium-sized companies and special depreciation for the promotion of participation in small and medium-sized enterprises. That is, e.g. profits realized on the sale of shares may be carried forward over the next four financial years, or, for example, that purchase costs for shares may be claimed for five equal annual amounts (Richters, 2015). For knowledge on the taxation of such funds, specific literature is needed, some of which do not originate from the academic sector. Specialists such as the foundation "Deutsches Venture Capital Institut", which is operated by Pöllath & Partner, an economic legal and tax consulting firm, are dealt with in more detail. With the income tax treatment of venture capital and private equity funds. In particular, it is a question of whether a fund is asset management or commercial. This segment shows that the market is developing very little. There is no longer a general solution. In contrast, this work attempts a new approach - the approach of a tax-optimized model - which facilitates the work of all European venture capital funds and thus indirectly helps entrepreneurs. The novelty of this approach is, therefore, that work is being done mainly on the regulations, but not on a fiscal solution.

In order to know who is involved in this work, the protagonists will be explained in the next sections. In this work, the end result is that the entrepreneurs are helped - so that these companies are promoted. Therefore, these are defined in the following sub-chapter. Chapter 1 continues with the research questions and ends with the presentation of the investigation procedures.

1.1.3 **Entrepreneurs in the Common Market**

The entrepreneur – and that applies in particular to the European Union – cannot place his possibly brilliant reflections on the market without further ado. Entrepreneurs must and will play a crucial role in the European Union in the future (Hotz-Hart & Rohner, 2014, p. 11). In accordance with a not quite uniform definition, he is at first a founder of a new business and has to take some determining considerations into account. Despite or because of his partially brilliant ideas – exemplary is and always will be Ray Kroc, who with his innovative business model, to spread existing business modules further under a franchise system (Kierdorf, 2011, p. 223), helped McDonalds (Schögel, 2012, p. 310) to attain global success – there is a risk that foundation-specific aspects in particular are being overlooked. Other than the foundation of a company itself, the establishment of a tax structure (This does not, of course, address the taxes that are examined in this work for private equity funds) plays an essential role (Kußmaul & Beckmann, 2002, pp. 40-51). In total, corporate taxes are a factor rightly receiving much attention in the course of corporate planning and corporate management. All taxes relevant for a business and the owner-manager – and therefore also for the entrepreneur – are in part subject to an impetuous change. The list of amendatory and continuously newly edited statutes, executive orders, statutory notices and guidelines seems ad infinitum, their constant modifications are vexing.

Hardly less extensive and therewith confusing for the entrepreneur is the range of literary aides. Generally literary support hardly exists. It would be helpful to provide the founders with a general framework. However, this remains the responsibility of the several Member States of the European Union. The key problem that entrepreneurs face is that they sometimes encounter difficulties in financing their ideas. In general, and according to the prevailing opinion of the parties concerned, entrepreneurs do not feel sufficiently appreciated (Faber, Siems, Riedel, & Pohl, 2014, p. 43) and supported in Europe.

Entrepreneur

In this context, an entrepreneur (Wolk & Zerres, 2009, p. 7) is to be understood as an individual (Horngeber, 2012, p. 3), who – with the help of predictive talent and creativity – is able to enforce products, services or production methods on the market, where others might possibly fail. He distinguishes himself in that, due to his efforts, he is being provided with the necessary resources for his project (Fueglistaller U. , Müller, Müller, & Volery, 2012, p. 21) and he is consistently pursuing his business idea.

Entrepreneurship

Thus entrepreneurship (Stokes, Wilson, & Mador, 2010, p. 8) can indicate a process, which is being initiated and conducted by those very individuals, having the purpose to recognize the entrepreneurial opportunities offered with this talent, creativity, risk-taking and enthusiasm (Volkmann & Tokarski, 2006, p. 2) and utilize it accordingly. Despite all the apparent specificity of an entrepreneur, he as well is challenged with first having to implement and realize a business idea. Therefore, entrepreneurship can be understood as a classical foundation (Kollmann, 2004, p. 1) of an enterprise, assuming that the founder is equipped with a certain degree of dynamics and motivation. There are good reasons (Berning & Novak, 2010, p. 129) for starting a business (Tanski, Schreier, & Thoma, 2013, p. 6), such as the threat of losing the place of work (Heyse & Erpenbeck, 1994, p. 130), as well as the pursuit of free allocation of working hours and work load (Thomas, 2011, p. 37). Also, an excellent business idea could account (Wassmuth, 2004, p. 168) for withdrawal from a supposedly secure existence. A good business idea is the basic requirement for a successful foundation of an enterprise (Langholz, 2011, p. 74). However, it is a condition precedent for success that there is a consumer demand for the product or service.

> *„There is no point in having a business idea if no one wants to buy it. To set up a company and make money you need a product that people want"*
> *(Russo, Gleich, & Straschneg, 2008, p. 19).*

Summary

The entrepreneur (Kunze & Offermanns, 2016, pp. 177-196) is being distinguished in that he also provides – aside from this idea – talent, perseverance, joy in self-employed working and most of all the will to actualize himself within his own company. In doing so, it does not matter whether he acts within a familiar industry or tries a completely new business idea (Hoffmann T. M., 2015, p. 21) to conquer the market. Once such consideration is completed and usually placed under a competitive situation, he needs to be aware of the status of competitors and customers before finalizing his decision to start a business, but also of how he wants to finance his company in the initial phase and beyond (Ahr, Schwenk, & Matros, 2011, p. 16). How much more difficult must such a decision be with the increasingly converging markets within Europe, but as well as in global aspects?

The problems and uncertainties with which an entrepreneur is being confronted during the beginning of his activities could certainly not be sufficiently and satisfactorily solved on a European level at present, since the regional, respectively the domestic occurrences, for instance in regards to the above-mentioned tax and establishing aspects, as well as the financing aspects, are too deeply embedded within the structures of the individual Member States and their traditions. Nevertheless, the European Union could intervene, by providing entrepreneurs with a fund that has general validity in itself throughout the European Union for all who are eager to start a business. Thus, this model would overcome language barriers, borders of interest and countries and institutionally is subject to only the feasibility of the project of the entrepreneur. Structures could be designed, which at first do not help the entrepreneur directly but rather indirectly by providing this fund, respectively the fund company that oversees these funds with general fiscal conditions in order to reduce the barriers for the operation and operators of such funds. Consequently, standardized provisions and improved structures for Private Equity funds could result in providing more funds and facilitating access to Private Equity for entrepreneurs.

1.2 RESEARCH ISSUES: OBJECT OF OBSERVATION PRIVATE EQUITY

This work intends to discuss the possibility of changed conditions, particularly in regards to fiscal but also regulatory treatment of Private Equity funds from a theoretical point of view. This study would also draw a little attention to the regulatory overkill. The background to this is the creation of better opportunities for entrepreneurs in the European Union via improved, modified and new structures for the development of Private Equity. In the context of the consideration of the actors in a Private Equity transaction, the regulatory requirements of private funds, and the modified parameters for such structures, the possibility of a different approach shall be analyzed and presented using the description and empirical data. In a rough outline, this work shall

1. *present the approach on Private Equity transactions and consider the protagonists in such participation constellations, as well as to establish a relationship to the European Union,*
2. *study, compare and discuss the fiscal and corporate parameters for Private Equity funds in selected Member States of the European Union,*
3. *and modify the above-mentioned fiscal parameters in such a way that compared to current realities new opportunities can be identified.*

These three research approaches, considered as starting points, are in recourse once again responsible for the development of the research questions. They follow a logical chain analysis to pursue a forecast, design and respectively a utopian approach.

The first research question is addressed to the Private Equity industry, in order to select and analyze which information is required to later correctly classify the importance of Private Equity. Necessarily, Private Equity is being presented in great detail and the economic benefit examined. This includes theoretical knowledge, which may also have a generally valid character for e.g. the company evaluation. Furthermore, empirical data are collected to identify areas of activity.

What role do Private Equity firms and their funds play in addition to the other players in an investment transaction and what economic importance has Private Equity for the EU?

The second research question addresses the constitutional conventions, rules and regulations of the Member States to be examined, resorting to basic theoretical knowledge of fiscal and regulatory concepts of these states. The selection of countries has changed several times during the data acquisition phase and processing phase of this work. Reasons are the changed conditions – explained in chapter 3 - from the previously selected states.

How do fiscal and regulatory provisions influence the Private Equity industry?

The third research question is addressed to option of future design opportunities for the treatment of Private Equity funds, resorting on a theoretical basis on previous data, which are then modified appropriately. Furthermore, already conducted comparative data are being consulted in order to determine the inter-related effects between the current approach and the changed conditions. This third central research question can be described as superior. Answering this questions is aimed at entrepreneurs. This means that Venture Capital is considered at the end.

Which countries within the European Union and beyond are measurably successful in regards to Private Equity, respectively Venture Capital investments, and have such similarities among each other that their conditions for optimized fiscal conditions may be taken under consideration? Which parameters requires a tax-optimized Private Equity fund?

Naturally, all measures to facilitate start-ups to finance their ideas and projects also have strong growth and interconnection effects for the European Union and the EU-market.

Figure 8 represents a cycle, in which the goal of growing the market is achieved by optimized Private Equity Financing of entrepeneurs.

Figure 8: Effects of Optimizing

Source: Own representation.

These research questions shall provide an overview of the research program, which is carried out in this work. The development of other, more specific questions will result from a fundamental discussion of the aspects surrounding Private Equity in the respective preliminary remarks of chapters 2, 3 and 4.

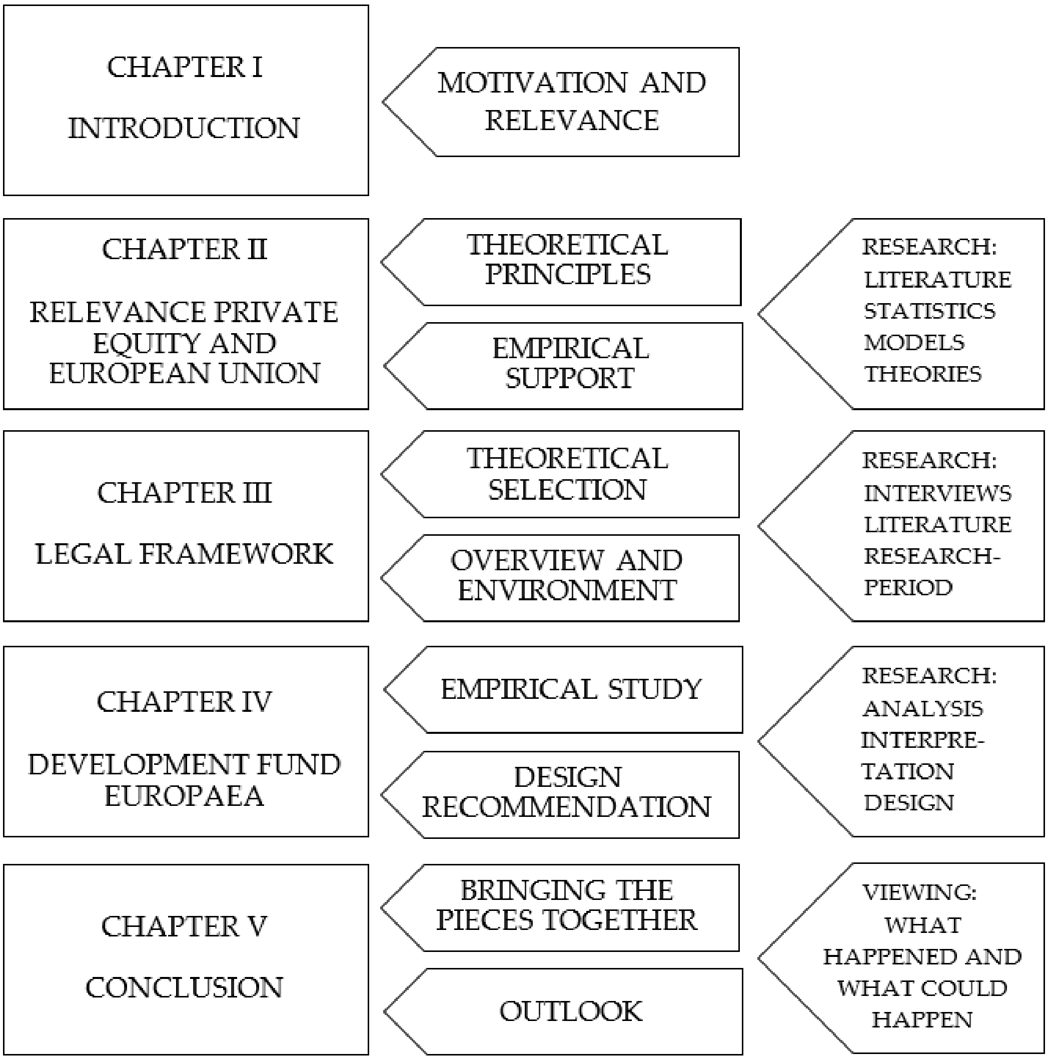
1.3 COURSE OF INVESTIGATION

If it is possible for the market within the European Union to achieve such a structure as mentioned above, the necessary transparency of these framework conditions would probably provide the non-market equity, for example the private equity companies, with an increased commitment from companies, which in turn would benefit the entrepreneurs.

It has already been established that entrepreneurs have difficulties financing their projects – which is the reason for the pursuit of a solution to this issue – and because the provision of equity by appropriate companies can be helpful in solving these difficulties, in a small digression in the mood of European citizens (EU) the great idea of a European internal market and its dependence on market growth has been discussed. The mood is important because a low interest rate, which is currently available, should actually increase the investment and therefore a better atmosphere is to be expected. The convergence of markets into a single single market is an essential part of the EU's efforts. Its growth could be a building block in order to increase the sentiment among the inhabitants of the EU. Now back to the entrepreneurs. A strong entrepreneurial scene could revive the market, which is why it is important to be involved in this segment. The provision of equity is therefore an approach. These entrepreneurs and therefore entrepreneurship as a whole was subsequently defined. In order to get an overview of the industry, which is intended to help these entrepreneurs generate equity capital, the participants were introduced beforehand to such a project (investors, private equity companies, target companies) with the help of a corresponding graphic. Chapter 1 examines the relevance for the European Union and also addresses the research situation. This passage ends with the aforementioned research questions. The main focus here is on the framework conditions for the provision of equity (private equity) and the tax-related framework conditions still to be developed in order to provide indirect access to equity for entrepreneurs. To this point, private equity has been spoken of only to a certain extent. In the next chapter (chapter 2) the procedure for such a private equity transaction (provision of equity in the life phases of a company) is explained in detail. The question is therefore answered as to the reason for using such equity and in this part of a company's life. To this end, the company is being further expanded (right up to internal and external financing) in order to be able to precisely classify what is known as private equity. After the defining private equity comes a decisive step: the distinction between private equity and venture capital. Private equity can be understood as an umbrella term for the provision of equity; while venture capital is more likely to support companies "only" in the early stages of their existence (for example, entrepreneurs). The provision of equity leads to the provider (private equity company) acquiring a stake in the subsidized company. For this reason, the following section examines the type of participation (majority or minority participation) that occurs most frequently. This is particularly important for entrepreneurs, so they know who to turn to. The economic significance of private equity in the European Union, which is also the total investment in participations in the European Union, is large, and this chapter is inclusive of the capital of the European Union and growth behind it. The point is that entrepreneurs from all over the European Union will have easier access to equity. This can be achieved if the owners of capital are uniformly taxed and are therefore more committed, while no individual state has its own structures. Therefore, the European Union is considered a system. Some data, such as the number of inhabitants, are also collected in order to be able to classify later that the total income of a country is not essential for the willingness to invest in entrepreneurs, but rather the per capita income. In addition, this section also mentions for the first time the key figure of the Gross Domestic Product (in essence, the total value of all goods and services produced within a given economy over the course of one year). The derivation of this figure is then made clear in the following chapter on national accounts. Since this indicator is an indicator of the growth of an economy, the growth theories according to Keynes and Neoklassik are still indicated. Thus, the demand function as stated by Keynes, according to the literature, is identical with the formula for the Gross Domestic Product. After considering the entrpreneurs in the sense of business founders, the overview of the provision of equity as an alternative financing of a company (private equity), the short insight into the European Union (EU), an overview of the investment volume in participations and the development of the essential indicator of growth (GDP), the tax parameters (capital gains tax, withholding tax, company tax, value added tax) are now determined in Chapter 3, which are later important for the investigation. The legal framework for private equity is examined intensively. The analysis of the legal and fiscal frameworks of selected EU countries is intended to exemplify the differences and thus the lack of consistency of the conditions. For the investigation in Chapter 4, all the necessary components are now known. This is the Gross Domestic Product (divided by the population of one country it is the Gross Domestic Product per capita), the Purchasing Power Standard (PPS - Purchasing Power Standard), the investments in participations and the different taxes. Through a series of cluster analyzes, Chapter 4 examines which countries within the European Union have the greatest similarities taking into account these parameters. In the end, only those investments in participations that are made in the early stages of a company (the above-mentioned venture capital) are taken into account. From the countries determined, the taxes which are important for venture capital (as for private equity) are now extracted at the company level and the fund level, which have contributed to the obvious success of these countries with regard to venture capital. These taxes and / or their tax rates are now summarized. This is used to calculate average tax rates, which in turn are used to calculate an optimized "European" Gross Domestic Product. Chapter 5 summarizes the investigation and provides an outlook for the tasks that need to be done to make such an optimized fund a reality. For example, at the highest level the legal framework such as custody, accessibility and administration of such funds must be clarified.

1.4 GRAPHICAL STRUCTURE OF THE INVESTIGATION

Figure 9: Structure of the Dissertation



Source: Own representation.

2 RELEVANCE OF PRIVATE EQUITY IN THE EUROPEAN UNION

2.1 PRIVATE EQUITY AS FINANCING ALTERNATIVE

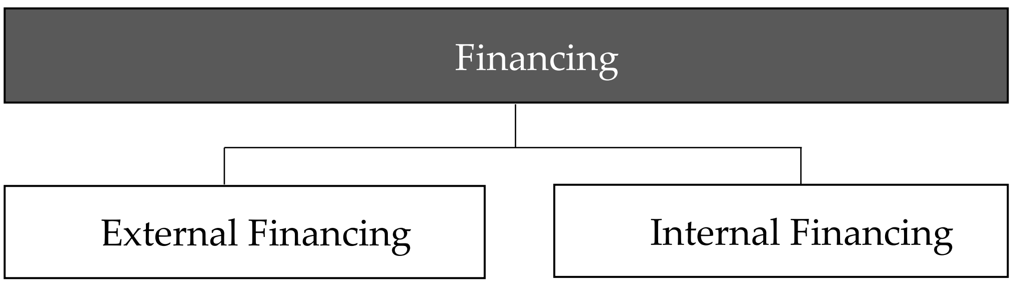
2.1.1 Preliminary Remarks

The development of economies increasingly depends on the start-up activities and the growth of young companies (Lüken, 2016, p. 54), as initially discussed (Zeuner, 2014, p. 30). Regardless of the doubtlessly strongly to be observed above mentioned problems of the founders, the difficult financial situation of such a project needs to be especially considered (Strauß, 2012, p. 3). These difficulties extend from covering the external capital requirements (Brecht, 2005, p. 116) with financial means of external investors, to the troubles of diverse capital and financing environments of the founding companies (Schöning, 2006, p. 273). These differ already regionally and even more so compared to the other countries (Wolf B. , 2006, p. 1), for instance within the European Union. For example, it is possible to obtain funding at a given point in time, but not in separate country or at a later date. When determining the financing environment (Wolf, 2006, p.3) a distinction has to be made according to the existence of different types (Lerch, 2011, p. 13) of financing options (Fueglistaller et al, pp. 344-347) and the extent of available (Alt, 2015, p. 36) resources (Linz, 2001, p. 27). This refers to the distinction of quality of the environment and quantity of the environment (Wolf & Nathusius, 2007, p. 149). These are being influenced (Wolf, 2006, p. 3). by the parameters (Wolf, 2006, p. 3) socio-culture (Fischer, Picot, Reichwald, & Franck, 2004, p. 41) and legal (Busack & Kaiser, 2006, p. 116) framework (Friedrichsen, Grüblbauer, & Haric, 2015, p. 57), of the financing system (Cumming D. , 2010, pp. 359-393). Despite the regional and international differences, these influential factors of the qualitative and quantitative development of the financing environment are, in general, to be considered similar everywhere and include the following factors listed, which are not sorted by relevance nor are they to be understood as being conclusive (Hackethal & Schmidt, 2000, pp. 53-102): the preferential structure of investors and intermediaries (Schultz C. , 2011, p. 122), the power of the financial market (Wiegert, 2003, p. 101), the government funding (Breloh, 2000, p. 159), the tax legislation (Sellien, 1964, p. 113), the regulatory law (Wolf, 2006, p. 3), the economic activity (Dupriez, 1963, p. 314), the investment alternatives (Kessel, Gawlitta, Hilbig, & Walther, 2015, p. 515), the competition between investors and (Wolf & Nathusius, 2007, p. 52) the needs for capital. The past has shown, that fiscal (Potthof, 1998, p. 187) and company laws (Schmoll, 2015, p. 817), respectively the regulatory framework (Matz, 2002, p. 33) and the funding instruments are significantly influential on the financial services offered (Müller, Gramigna, & Linder, 2008). Thus, the fiscal law can already prefer or exclude certain forms of capital. The following explanations show which options the entrepreneur has within the financing system, and where private equity is classified. In order for the delineation and arrangement to be carried out successfully, the foundations are described in detail. Inclusion of private equity in the forms of financing

Inclusion of private equity in the forms of financing

Characteristically, the entrepreneur is initially looking at the usual financing transactions and types of financing (Bobka, 2014, p. 28). In principle, a distinction is being made between internal and external financing (Becker H.-P. , 2013, p. 240), whereas these terms of financing (figure 10) are each being subdivided, as presented in the figures 11 and 12 (Perridon, Steiner & Rathgeber, 2012, p. 358).

Figure 10: Types of Financing

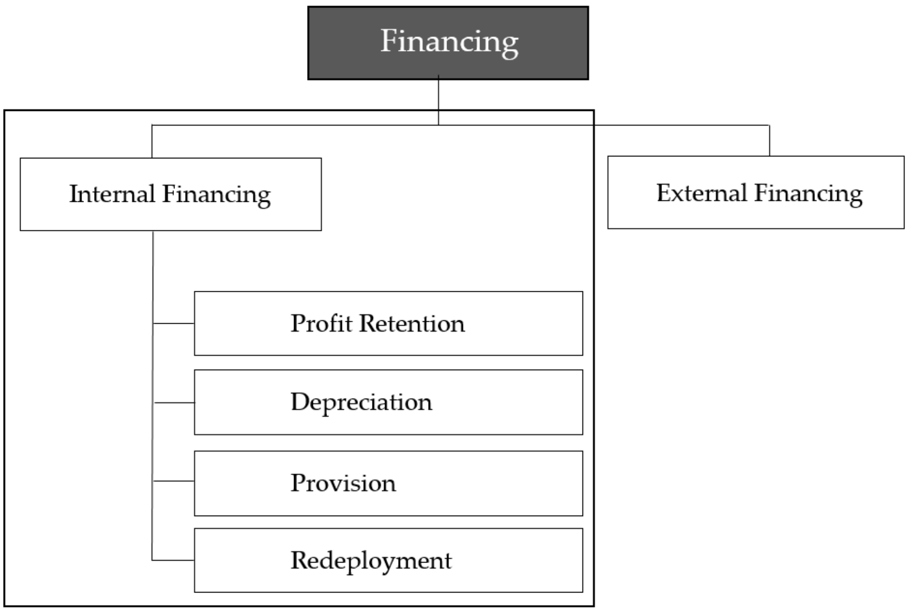


Source: Own representation based on Perridon, Steiner & Rathgeber.

An internal financing is then provided when the funds are raised internally, that is to say by the enterprise itself. Accordingly, self-financing from retained earnings and other internal financing such as depreciation and provisions are included.

With internal financing (Vernimmen, 2011, p. 727), the funds are released (Härdler, 2015, p. 363) within the company and no injection of cash is obtained (Olfert & Reichel, 2005, p. 33) from the outside. Among internal financing are, as can be seen in figure 11, the retention of earnings, the financing of depreciation, financing from provisions (Becker, 2016, p. 245) and the financing from the redeployment of capital (König, 2014, p. 7). Due to the profits partially or completely remaining in the company, the company finances itself. While internal financing may take the form of retained earnings by waiving a dividend or a distribution, with concomitant increase in capital (Becker H. P., 2016, p. 246), the financing through depreciation is done over a settlement of profits against the depreciation expenses (Losbichler, 2015, p. 248).

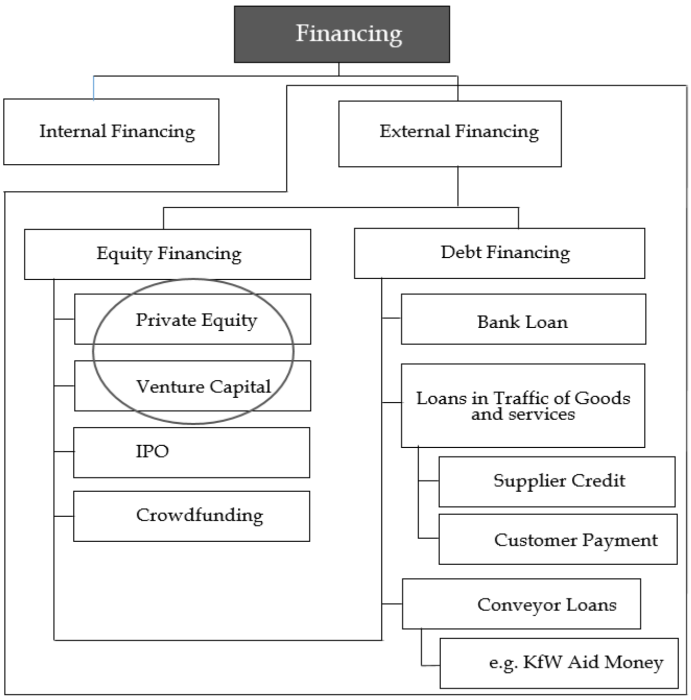
Figure 11: Internal Financing



Source: Own representation based on Perridon, Steiner & Rathgeber.

With financing from provisions (Röhrenbacher, 2008, p. 233), balance positions for contingent liabilities, warranties and anticipated losses from pending transactions are recognized (Hermanns, 2006, p. 235). The previously formed provisions are initially recorded as expenses decreasing the profit (Röhrenbacher, 2008, p. 233; Hermanns, 2006, p. 235). With the occurrence of the event, the provisions must be resolved (Binger, 2009, p. 112), just as the creation (Paul J. , 2015, pp. 430-432) of provision has been recorded as income (Binger, 2009, p. 112; Paul J., 2015, pp. 430-432). The profit resulting from the reversal of the provision (Tanski J. S., 2014, p. 6) earnings increases the tax burden and therefore has an opposing effect (Daum, Petzold, & Pletke, 2016, p. 155).

Figure 12: External Financing



Source: Own representation based on Perridon, Steiner & Rathgeber, 2012, p. 358.[6]

[6] The KfW aid money is from the Development Loan Corporation in Germany and only an example.

Financing through redeployment of assets (Ganzer, 2015, p. 29) procures liquidity (Wöltje, 2013, p. 381), for example, by selling no longer needed assets, such as non-operating buildings (Ganzer, 2015, p. 29; Wöltje, 2013, p. 381).

External financing includes all financial transactions in which resources from the outside are introduced into the company (Brauchle & Pifko, 2011, p. 139 et seqq.). As can be seen in figure 12 at page 34, all inflows of external financing occur via equity financing or debt financing (Schulte, 2009, p. 56).

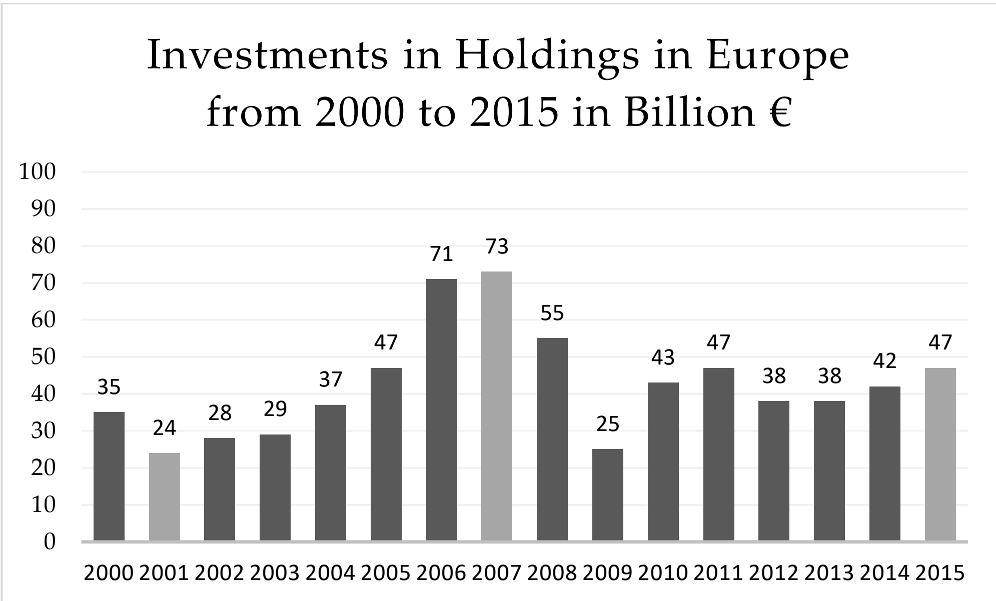
The equity financing includes (Schmidt & Terberger, 1996, pp. 230-231) participation in the opportunities and risks associated with the company (Reuter, 2008, p. 20). With credit financing however (Neugebauer, 2014, p. 36), the investor obtains creditors 'rights such as the right to repayment and interest payment (Grundmann, 2013, p. 16), which may be distinguished from a time of one to less than four years and long-term loans (Ermschel, Möbius, & Wengert, 2011, p. 111) with a term of four years and more (Neugebauer, 2014, 2014, p. 36; Grundmann, 2013, p. 16). The interest rate of a bank loan (Geyer, Hanke, Littich, & Nettekoven, 2015, p. 151) can be agreed upon for the entire term (Jacob, Klein, & Nick, 1994, p. 164). In addition to a fixed rate agreement (Buck, 2016, p. 36), the contracting parties may conclude an agreement of a variable (Kuttner, 1995, p. 36) interest rate (Buck, 2016, p. 36; Kuttner, 1995, p. 36). With this interest rate agreement, the debit interest is adjusted at regular intervals according to the development of the money market (Bitz & Stark, 2015, p. 57). The delivery of goods in which the payment target is in the future considered a supplier credit, which – just like the premature customer payment – counts among the credit financing (Hering, 2015, p. 24). Likewise, the credit financing includes development loans, which are often used for their beneficial conditions and favorable contractual arrangements when a company is founded (Plenker, 2016, p. 239). Figure 12 shows the instruments of equity financing. The crowdfunding belongs to the equity financing as well as the IPO (Initial Public Offering). In crowdfunding, equity or equity-related mediums are provided by the crowd, mostly by internet users, ie the crowdfunders. In return for the provision of minimum sums, the crowdfunder receives rights, benefits or idle values. The communication between the borrower and the crowdfunder takes place as part of a crowdfunding platform (website). The donor provides e.g. a video with its idea on this platform and the crowdfunder donates money or participates in this idea. An IPO is discussed when shares of a company are offered for sale to interested investors. This is also referred to as a "first public offer". Through an IPO, a company acquires risk capital from the outside by using the shares as a financing instrument.

As figure 12 illustrates, equity financing includes Private Equity (Tcherveniachki, 2007, p. 204), which seeks to offer a financing option (Hoffmann D. , 2014, p. 77) for such companies whose credit is already exhausted or that no longer receive loans (Bieg, Kußmaul, & Waschbusch, 2015, p. 130) due to lack of collaterals (Tchervenichki, 2007, p. 204; Bieg, Kußmaul, & Waschbusch, 2015, p. 130). A Private Equity firm acquires company shares, through which the firm participates in the odds and the risks of loss (Bieg, Kußmaul, & Waschbusch, 2015, p. 130). The participation on corporate earnings allows for a possible return through dividend payments or a profitable selling of the company´s shares (Renz M. , 2015, pp. 25-28). Venture Capital as part of Private Equity typically pursues yield-oriented goals (Schüle, 2015, p. 20). The difference to Private Equity is the entry point (Bernhardt, 2010, p. 84). While Venture Capital invests in very young companies to reveal the possible present high growth potential, Private Equity investors invest at a later phase of the company (Bernhard, 2010, p. 84).

In addition, mezzanine financing should be mentioned (Völker, 2014, p. 36), which is a hybrid form of financing (Nohtse, 2012, pp. 19-20), i.e. a mixture of equity and debt (Brezki, Böge, Lübbehüsen, Rohde, & Tomat, 2006, p. 23), and – as a theoretical consideration regarding the capital structure – the Irrelevance Theorem of Modigliani and Miller (Harris & Raviv, 1991, p. 297), who assume in opposition to the traditional hypothesis of an optimal capital structure (Uhrig-Homburg, 2001, p. 187) that it does not affect the asset position of the shareholders (Modigliani & Miller, 1959) in what ratio a company resorts to equity and debt. Mezzanine financing is then used when a company with sufficient and stable cash flow has to meet the demands of investors and all credit lines are exhausted (Hockenbrink, 2015, pp. 64-65). Thus the gap between the maximum available borrowing and the financing needs of the company is closed (Bienert, 2005, p. 410). The traditional core application area (Fersadi, 2015) for mezzanine financing (Lühn, 2013, pp. 37-38) can be found in management buyouts (Lühn, 2013, p. 37; Fersadi, 2015). For small and medium-sized companies mezzanine financing (Abrahamczik, 2012, pp. 269-270) is used to finance growth strategies (Lehmann-Tolkmitt, Knöll, & Elmers, 2010, p. 14), for project financing (Lühn, 2013, p. 35) or for the initial public offering (Wirtz & Salzer, 2001, p. 10) financing (Reichling, Beinert, & Henne, 2005) .

Basically, equity financing means the provision of capital by the owner of the company (Tursch, 2009, pp. 5-7). This type of financing, paradoxically identified as self-financing, already indicates Private Equity (Cooke, 2011, p. 21). Namely, if the provider of equity is not the original owner of the company, but an outside player, this already is - assuming that the company to be financed is generally not market-listed – Private Equity in its original mold (Widmann, 2014, p. 3).

Figure 13: Investments in Holdings in Europe in bn. Euro



Source: Own representation based on Invest Europe, 2015, p. 1-76.

Meanwhile, Private Equity has established itself on the international markets as a form of financing and investment (Grethe, 2010, p. 4). Although, the financial crisis took a sharp decline in the positive development of the Private Equity industry starting in 2007 – and before then in 2005, triggered by the locust debate initiated by the SPD politician Franz Müntefering (Frommann, 2014, p. 24), which showed its effects not only in Germany – those circumstances could not prevent a revival of the Private Equity engagement back to an average level due to its undisputable advantages as is being illustrated in the graph of the investments in holdings in Europe (figure 13). More than 1.200 European Private Equity firms have been analyzed in the process (Invest Europe, 2015, pp. 1-76).

As seen in figure 13 on the previous page after the sharp decline between 2007 and 2009, the upward development initially made good progress again and has consolidated in the meantime (Meyer T. , 2009, pp. 1-16). This convalescence was mainly driven by the fact that this form of financing companies is interesting for investors (Speck, 2014, pp. 24-25) and it is certainly being discussed that the Private Equity market did not plummet as strongly during the financial crisis in comparison to other investment forms (Meyer T., 2009, pp. 1-16). The most important reason as a young entrepreneur, founder and growth company to consider Private Equity as a form of financing is and will remain - first and foremost – the difficulty for these companies to finance themselves (Lutz, 2011, p. 194) via "normal" bank loans (Möckel, 2005, p. 158). The regulations in Basel II and Basel III (Schröder, 2014, p. 30) have not necessarily encouraged the access to capital, specifically the willingness of banks (Neuthinger, 2014, pp. 38-41) to take a certain risk in financing (Schröder, 2014, p. 30; Neuthinger, 2014, pp. 38-41).

2.1.2 Terms and Approach of Private Equity

2.1.2.1 Derivation of the Term Private Equity

Private Equity is actually a financing concept (Becker, 2013, p. 233) and not a financial instrument (Philipp, 2012, p. 3). In addition to the financing function (Bernhardt, 2010, p. 102) in general (Müller F. , 2010, p. 70), Private Equity supports the target company (Weißflog, 2015, p. 254), also called the portfolio company, in solving many problems an enterprise will encounter during the course of development (Wöhe, Bilstein, Ernst, & Häcker, 2013, p. 193). According to Invest Europe, formerly known as EVCA (European Private Equity & Venture Capital Association), now Invest Europe, Private Equity is defined (Schoon, 2011, p. 69) as follows (EVCA, 2013, pp. 1-16; Mauer, 2015, pp. 140-143):

> *„Private Equity provides equity capital to enterprises not quoted on a stock market. Private Equity can be used to develop new products and technologies, to expand working capital, to make acquisitions, or to strengthen a company´s balance sheet. It can also resolve ownership and management issues – a succession in family-owned companies, or the Buyout or buy-in of a business by experienced managers may be achieved using Private Equity." (EVCA, 2013, p. 1-16; Sauermann, 2010, p. 7)*

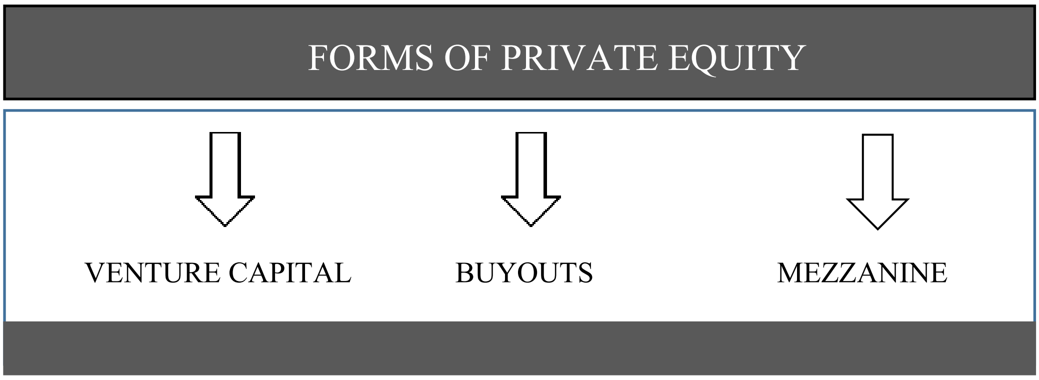
This definition points to an important requirement, namely that most or almost all target companies of Private Equity (Reimers, 2004, p. 4) are not publicly listed (Zipser, 2008, p. 1). This means, that the companies are not yet listed (Gaedke, Nöstlthaller-Kropf, Pinter, Rhomberg, & Weigl, 2012, p. 205) on the stock exchange (Barkalov, 2015, p. 120). Anyhow, it must be pointed out, that this definition is not yet a unified description of Private Equity (Kartashova, 2014, p. 3300). The current scientific literature lists a variety of definitions. The term component *Private* is often misunderstood (Henreich, 2012, p. 1) as private funding from individuals. However, it represents the fact, that the own funds are not public funds (Meyer, 2010, p. 181), but over the counter, as explained above. The term *Equity* (Schröer, 2009, p. 8) refers to the provision (Niederdrenk & Müller, 2012, p. 29) of capital as liable and risk-bearing equity or quasi-equity (Humphery-Jenner, 2013, pp. 1-50). As opposed to debt capital (Pohlhausen & Röder, 2013, p. 724), where the interest rate over (Grunow & Figgener, 2006, p. 188) a certain period of time is generally determined prior to the approval of the loan, there is generally no previously fixed return (Timm, 1976, p. 27) and no repayment (Hagenmüller, 1959, p. 241) or exit-date with equity investments (Bayaz, 2013, p. 39). Compared to lenders of debt capital (Vormbaum, 1990, p. 46), equity investors acquire (Bösch, 2009, p. 67) a greater risk since (Perridon, Steiner & Rathgeber, 2012, p. 358) the company's losses (Wöltje, 2016, p. 343) are first offset against equity (Behringer, 2014, p. 98). At the same time as well, however (Kreuzer, 2013, p. 46), the equity investor benefits from a business success, (Schneeberger & Peyerl, 2011, p. 46) much more than the lenders of debt capital (Schneeberger & Peyerl, 2011, p. 327). This *equity* participates in both the positive as well as the negative (Philipp, 2012, p. 3) corporate development (Hehn, 2011, p. 78).

Therefore, the goal (Kaplan & Schoar, 2005) of Private Equity (Siegel, Wright, & Filatotchev, 2011) and its accompanying services can be defined as the achievement of profit through the performance of the company (Sust, 2009, p. 86) within the investment period (Fahrenschon, Kirchhoff, & Simmert, 2015, p. 343). With the support (Achleitner, Schraml, & Tappeiner, 2011, p. 27) of Private Equity, (Pfeifer, et al., 2009, p. 37) the value of the investment increases, whereby the expected return can be achieved (Hehn, 2011, p. 42). The investment period (Weimerskirch, 2000, p. 10) of the equity capital in the target company is limited (Hahn, 2014, p. 61). In most cases this is five to ten years (Lerch, 2011, p. 5), which corresponds to a medium or long-term (Moritz G. , 2004, p. 400) Private Equity investment (Groh, 2004, p. 26). During the investment period, the investor is a shareholder of the company (Becker L. , 2006, p. 227). Subsequently, the company can resort to the additional equity as well as (Söding, 2012, p. 17) to the expertise of the investor (Engelbrechtsmüller & Losbichler, 2010, p. 123), if necessary (Philipp, 2012, p. 3). In addition, the investor acquires certain rights (Müller, 2010, p. 79), and obligations to the company (Vogt, 2007, p. 35), such as in terms (Schenck, Balda, Dorbert, Hogh, & Zieske, 2015, pp. 1-37) of strategic decisions (Dworezkij, 2010, p. 4) and operational activities (Schneider, 2011, p. 57).

It is also referred to as *private* because it is a private corporate financing (Eilenberger & Haghani, 2008, p. 11) as opposed to a public (Bassi & Grant, 2006, p. 123) company. But for all that, this does not imply (Bayaz, 2013, p. 40) that Private Equity companies (Friedrich, 2005, p. 11) only engage (Landau, 2011, p. 1) in companies (Bruhn & Hadwich, 2011, p. 154) that are not (North & Caes, 2012, pp. 6-8) quoted (Vogt, 2007, p. 4) on the stock exchange (Scherbaum, 2015, p. 6), rather they are unlisted (Bayaz, 2013, p. 40), because after the acquisition of the shares through a publicly available market, the company would be taken off the exchange (Bayaz, 2013, p. 40). A public company would turn (Stamp, 2001, p. 11) into a private company (Bayaz, 2013, p. 40) and public equity would turn (Brettel, Kauffmann, Kühn & Sobczak, 2008, p. 111; Bayaz, 2013, p. 40) into Private Equity (Brettel, Kauffmann, Kühn & Sobczak, 2008, p. 111).

Thum, Timmreck & Keul (2008, pp. 13 f) define Private Equity as a temporary (Bayaz, 2013, p. 40) - seven to ten years (Bayaz, 2013, p. 40) - majority shareholding - usually over 40% (Bayaz, 2013, p. 40) - in the equity of non-listed companies with the target to increase the value through restructuring (Bayaz, 2013, p. 40). In contrast Boué, Kehlbeck & Leonhartsberger-Heilig (2012, p. 84) distinguishes between evergreen funds and funds with a fixed maturity. The evergreen funds (Bascha, 2001, pp. 153-187) have an indefinite term and the term of the fixed fund is about 8 to 10 years. Others like Willert (Willert, 2006, pp. 35-36) are of the opinion that the term is not regulated and therefore must be determined individually. Despite numerous discussions, and public debates (Bayaz, 2013, p. 40), the term (Auel, 2014, p. 11) Private Equity (Sewing, 2008, p. 10) is not yet clearly defined (Bayaz, 2013, p. 40). On one hand, it applies in a broader sense (Bayaz, 2013, p. 40) to the entire market of private corporate financing, (Manchot, 2009, p. 20), following the example in figure 14, whereby, in my view, under Venture Capital in the early stages of financing up until the later stage are meant.

Figure 14: Forms of Private Equity



Source: Own representation based on Bayaz, 2013, p. 40.

In part, Secondary Purchase (Cateora & Richardson, 1967, p. 323) and Tertiary Purchase (Friedlander, 2004, pp. 10-11) are also being considered (Fraser-Sampson, 2010, p. 189) Private Equity (Renz M. , 2015, p. 25) in general (Siegel, Wright, & Filatotchev, 2011). Overall, it can be agreed that in fact, depending on the chronological use, Venture Capital (Gompers, Kovner, & Lerner, 2009), Buyouts (Bratton & McCahery, 2015, p. 491) – Management Buy Out (MBO - take over of the company or company shares by the existing management), Management Buy In (MBI – takeover of the company or company shares by external management) und Leveraged Buy Out (LBO – take over of the company by an external group of investors) can all be subsumed under Buyouts - and Mezzanine Capital (Willis & Clark, 2005) (Gladstone & Gladstone, 2002, pp. 5-8) under Private Equity (Manchot, 2009, p. 20; Bayaz, 2013, p. 40). On the other hand, terms (Manchot, 2009, p. 20; Bayaz, 2013, p. 40) such as equity, Venture Capital, and risk capital (Lohfert, 2003, p. 2) are used interchangeably (Bayaz, 2013, p. 40).

Short Demarcation Venture Capital

Venture Capital usually provides equity at an early stage (Middelberg, 2013, p. 9) of a company. This financing is therefore associated with a high risk (Ramsinghani, 2014, p. 6). Buyouts rather represent majority shareholding (Dänzer, 2010, p. 25) up to the acquisition of a company, (Schwenkedel, 1991, pp. 4-19) and Mezzanine Capital (Hager, 2007, p. 1) is a hybrid form of equity and debt capital (Slee, 2011, p. 347). On the other hand, and to come back to the attempt to uniformly define the term of Private Equity, it is to be understood in a narrower sense as the commitment in the late life cycle stages (Sacher, 2013, p. 10) of a company.

Origin

The origins of the term Private Equity are to be found in the United States and it derives from the term Venture Capital (Lessambo, 2013, pp. 186-187). Already during the 50s, companies of the technology sector were supported by Venture Capital firms (Manger, 2003, p. 154) during their Start-up Phase by providing equity (Tcherveniachki, 2007, p. 16). This special form of long-term but temporary business and innovation financing with risk-bearing equity or equity-like capital

(Gaughan, 2011, pp. 363-364), coupled with active business consulting and support of the company to be financed without affecting and influencing the ongoing daily business is nearly unchanged to this day. The recipients of Venture Capital are mainly small or medium-sized, mostly highly innovative and often technology-oriented companies with a high growth potential that are not issuable and cannot generate enough capital from its own resources (Kraus, 2008, p. 150).

2.1.2.2 Venture Capital as Risk Capital

The classification of Venture Capital is, above all else, incredibly important for this study. While the phases of a Private Equity Investment are explained chronologically and are thus unambiguous, the distinction to Venture Capital is neither clear in the literature nor according to its character (Schüler, 2016, p. 43 et seqq.; Brettel, Rudolf & Witt, 2005, p. 79 et seqq.; Hockenbrink, 2015, p. 46 et seqq.; König, 2014, p. 16 et seqq.). In chapter 2.1.2.1, Venture Capital was described as an early-stage of financing, which is at a high risk (Schüler, 2016, p. 43 et seqq.; Brettel, Rudolf & Witt, 2005, p. 79 et seqq.; Hockenbrink, 2015, p. 46 et seqq.; König, 2014, p. 16 et seqq.). Thus, if Venture Capital is risk capital (Schüler, 2016, p. 43 et seqq.; Brettel, Rudolf & Witt, 2005, p. 79 et seqq.; Hockenbrink, 2015, p. 46 et seqq.; König, 2014, p. 16 et seqq.), the question arises when the risk is particularly high. Certainly, financing is a risk in the early stages of a company. However, the financing of a Turnaround is dangerous as well. Per definition, financing the Turnaround would be a Venture Capital funding. In practice it is quite common for Venture Capital companies to completely finance a company - from the foundation to the expansion, to the exit through the financing (Schüler, 2016, p. 43 et seqq.; Brettel, Rudolf & Witt, 2005, p. 79 et seqq.; Hockenbrink, 2015, p. 46 et seqq.; König, 2014, p. 16 et seqq.). This, in turn, would qualify as a total private equity financing. While in principle the work has the financing of entrepreneurs in mind, the later analyses will often refer to venture capital.

As a result, a uniform definition is necessary. Under Venture Capital, the seed, start-up and expansion financing (expansion not in the sense of growth financing to open up new markets or restructure operations) is included in the investigation

(Schüler, 2016, p. 43 et seqq.; Brettel, Rudolf & Witt, 2005, p. 79 et seqq.; Hockenbrink, 2015, p. 46 et seqq.; König, 2014, p. 16 et seqq.). This risk of Venture Capital is usually required as a capital support in order to develop products or to finance initial growth in sales (Schüler, 2016, p. 43 et seqq.; Brettel, Rudolf & Witt, 2005, p. 79 et seqq.; Hockenbrink, 2015, p. 46 et seqq.; König, 2014, p. 16 et seqq.). Seed financings are investments in companies, which are in a very early phase, sometimes also in the pre-founding phase (Schüler, 2016, p. 43 et seqq.; Brettel, Rudolf & Witt, 2005, p. 79 et seqq.; Hockenbrink, 2015, p. 46 et seqq.; König, 2014, p. 16 et seqq.). The risk of entrepreneurial failure is still high, as it is unclear whether the company and the planned products will be able to penetrate the market. The financing of a start-up is incredibly important in a young company (Schüler, 2016, p. 43 et seqq.; Brettel, Rudolf & Witt, 2005, p. 79 et seqq.; Hockenbrink, 2015, p. 46 et seqq.; König, 2014, p. 16 et seqq.). The products often have to be developed or brought to market maturity. Even at this stage, the risk of entrepreneurial failure is high (Schüler, 2016, p. 43 et seqq.; Brettel, Rudolf & Witt, 2005, p. 79 et seqq.; Hockenbrink, 2015, p. 46 et seqq.; König, 2014, p. 16 et seqq.). Expansion financing focuses on companies whose products are already developed and which have a customer base. However, further expansion is needed to expand, with the risk of failure at this stage already declining. This view is also in line with that of EVCA, today's Invest Europe (investeurope.eu, 2016).

2.1.2.3 Motives, Phases and Leveraged Risk of Private Equity Financing

A series of considerations prompts companies to address financing outside the classic financing methods (May, 2006, p. 71). Most certainly, the succession plan (Müller F. , 2010, p. 154) is one of the more often mentioned reasons especially for small to medium-sized companies. Hence, motives for Private Equity financing could be (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 53; Müller F., 2010, pp. 65-67):

- Succession planning (Klein & Vossius, 2013, p. 7).
- Growth (Croce & Martí, 2016, pp. 657-683).

- Bridge Financing (Hockenbrink, 2015, p. 69; Bayaz, 2013, p. 41).
- Going Private (Schneider & Valenti, 2010, pp. 75-106).
- Spin-Off (Austin & Gottlieb, 2003, pp. 2-7).
- Private Placement (Tuli & Shukla, 2015, pp. 165-190; Shiu & Wei, 2013, pp. 875-877).
- Turn Around (Lymbersky, 2013, pp. 53-56).
- Buy and Build (Hoffman, 2005, p. 39).

Succession Plan

Often, a generation change within a company is not possible (Herzog, 2014, p. 1), either because of the lack of a successor or because an adequate member of the family for example is not available (Eddleston, Kellermanns, Floyd, Crittenden, & Crittenden, 2013, p. 1177).

However, in order to maintain the company, a less restrictive regulation must be found (Wegmann & Wiesehahn, 2015, p. 201). One scheme of this kind could be the MBO (Kluth, 2011, p. 41) or MBI (Jesch, 2013, p. 79) as explained in the previous chapter. Prevalently, MBO is the only possible succession plan (Kluth, 2011, p. 41). It entails an extensive financial restructuring, since it requires the overtaking management to move large volumes of money. Consequently, a large part of the funding needs to be provided by financial investors. The advantage of Management Buyout is (Kappeller & Mittenhuber, 2009, p. 245), that the former owner hands over his business to people he has known for many years (Hohenlohe, 2006, p. 83). Discussions and decisions are simplified by the fact, that the former owner has confidence in his former employees – mostly executives – and is able to assess their skills well (Habbel, 2001, p. 19). This environment of trust includes that confidential and critical business documents, possibly bearing the signature of the former owner in collaboration with the ex-managers, do not fall into the hands of potential external buyers. However, an advantage and at the same time, disadvantage of the acquisition by the former management is the information advantage of the former employees being able to precisely assess the situation of the company, if necessary

(Fueglistaller, Müller, & Volery, 2008, p. 141). When negotiating the price of the company, this could cause an imbalance between the proceeds expected by the previous owner (Kreis, 1998, p. 362) and that of the well-informed transferee (Holstein, 2015, p. 143).

Growths

Growth financing (Portisch, 2016, p. 647) is used to finance expansion projects. These expansions include the expansion of production capacity (Werner T. , 2009, p. 186) and additional working capital, whereas in this case, working capital is to be understood as an accounting ratio which determines the difference between the current assets and current liabilities of the company (Rao & Rao, 2014, pp. 1-14). The expansion of market shares or a change in the product range as well could stimulate demand for financial resources (Hoffmann W. , 2011, p. 49). Acquisitions that cannot be financed through debt capital are part of the expansion capital (Portisch, 2016, 319). Usually, Private Equity companies are financing the growth of companies (see also 2.1.2.5) through minority shareholdings (Hahn, 2014, p. 203). In contrast to the early-stage financing, this is mainly because the former owners would like to limit the influence of the Private Equity company. In addition, the minority shareholding is often sufficient for realizing the financing of these expansion projects (Seggewiss, 2015).

Bridge Financing

Bridge Financing (Hockenbrink, 2015, p. 69; Bayaz, 2013, p. 41) is used for the preparation of an IPO (Brokamp, Ernst, Hollasch, Lehmann, & Weigel, 2012, p. 41). Private Equity financing is an essential prerequisite for small to medium-sized companies (Hess, 2007, p. 20) in obtaining the ability to go public (Brüse, 2011, p. 37) and to finance the IPO (Hess, 2007, p. 20; Brüse, 2011, p. 37). Here, additional equity is being provided to bridge the time period until the introduction of the company on the stock exchange is available (Dürr, 2007, p. 40). Also in the Venture Capital sector, Bridge Financing arrangements can be witnessed (Huchzermeier, 2006, p.

203) in the form of interim financing (Bayaz, 2013, p. 41) for the IPO of young technology companies immediately after the expiration of the Venture Capital commitment (Huchzermeier, 2006, p. 203; Bayaz, 2013, p. 41). The IPO (Hohla, 2001, p. 60) usually requires a long-term preparation (Staroßom, 2013, p. 360) to meet both the legal requirements and those required by the legislation governing stock exchange transactions (Deloitte, 2009, p. 13), as well as the expectations of potential private and institutional investors (Deloitte, 2009, p. 13; Hohla, 2001, p. 60; Staroßom, 2013, p. 360). The preparation phase for an IPO (Natter, 2003, p. 164), in which a Private Equity firm accompanies an enterprise, may take one to two years to complete (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 52), even with larger medium-sized companies (Deloitte, 2009, p. 13) already established on the market (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 52; Deloitte, 2009, p. 13; Natter, 2003, p. 164). In that, the Private Equity capital improves (Arnold, Englert, & Eube, 2013, p. 171) the equity adequacy (Burkhardt, 2008, p. 59) to accomplish the preparation time for the IPO (Arnold, Englert, & Eube, 2013, p. 171; Burkhardt, 2008, p. 59; Deloitte, 2009, p. 13). In addition, many companies need capital in preparation of the IPO in order to deliver a compelling equity story – meaning the possible course of the investment (Kirchhoff, 2006, p. 217) – to the potential investors (Deloitte, 2009, p. 13; Kirchhoff, 2006, p. 217). Part of these efforts at persuasion is that it needs to be clearly explained to the investors why, for example, the acquisition of a certain company (Bernhardt, 2010, p. 97) and the capital required might be necessary (Bernhardt, 2010, p. 97; Deloitte, 2009, p. 13). Through the additional capital, the perfect time for the IPO can be arranged without exposing the company to financial pressure by having to perform an IPO under circumstances based on a bad market environment (Deloitte, 2009, p. 13). This flexibility, brought forth by Bridge Financing can be declared as the essential advantage (Deloitte, 2009, p. 13).

Going Private

As already suggested in 2.1.2.1, Going Private (Müller F., 2010, p. 67) indicates the conversion of a publicly listed company – thus Public Company (Deloitte, 2009, p. 13) – to a private company whose shares are no longer traded on the stock markets

(Borden & Yunis, 2006, p. 6) – thus Private Company (Borden & Yunis, 2006, p. 6; Deloitte, 2009, p. 13; Müller F., 2010, p. 67). Private Equity is an essential prerequisite (Eisele, 2006, p. 5) for the transition of medium-sized companies from the stock exchange (Bloss, Ernst, Häcker, & Eil, 2009, p. 194), which allows medium-sized enterprises a greater flexibility regarding the use of and dependence on capital markets (Bloss, Ernst, Häcker, & Eil, 2009, p. 194; Deloitte, 2009, p. 14). For the classification of a transaction as Going Private (Abrams, 2004, pp. 14-15), a complete delisting of the company (Vernimmen, 2011, p. 777) is carried out and the company will be transferred to a shareholder level (Abrams, 2004, p. 14-15; Deloitte, 2009, p. 14; Vernimmen, 2011, p. 777). In this context, delisting (Jansen, 2016, p. 146) is to be understood as the discontinuation of the trading of shares on all stock markets, all the while maintaining investor protection (Picot C. M., 2009, p. 6). The transferees of a corporation, which is to be taken from the stock market (Deloitte, 2009, p. 14), seek to obtain full control over a listed company in order to accompany it after the conversion in a non-listed company and at best, continue further development (Deloitte, 2009, p. 14).

Spin-Off

In a Spin-Off, a part of an existing company is spun off (Deloitte, 2009, p. 14) as an independent company (Festel & Rittershaus, 2014, pp. 5-10). These divestitures or spin-offs do not receive their own legal independence (Deloitte, 2009, p 14). Often, the motive for a Spin-Off (Austin & Gottlieb, 2003, pp. 2-7) is a change in the strategic orientation of the parent company (Deloitte, 2009, p. 14), which no longer considers the tasks of this department or component of the company as being an element of the priority tasks for the entire company (Anand, 1994, p. 581). Of course, it is also possible that newly developed products are being considered for a Spin-Off (Herzog, 2014, p. 20), which the corporate group does not wish to integrate after their maturity (Deloitte, 2009, p. 14; Herzog, 2014, p. 20) has been reached.

Private Placement

Private Placement (Tuli & Shukla, 2015, pp. 165-190) refers to the placement of securities (Deloitte, 2009, p. 15), which are not publicly sold (Rudolph, 2006, p. 294) and traded (Cao, Xia, & Wang, 2013, pp. 91-93). After their sale, they usually remain in the charge of the first investor (Deloitte, 2009, p. 15). Private Placement includes (Deloitte, 2009, p. 15) not only the OTC (over-the-counter) issue (Shiu & Wei, 2013, pp. 875-877) of shares of other participatory instruments in which investment capital from private investors is placed as a non-voting, diversified investor capital (Werner H. , 2006, p. 42); the scope of investment opportunities within the scope of private emissions (Deloitte, 2009, p. 15) is much broader and more interesting than a securities issue on the stock exchange and covers the entire range of mezzanine financial instruments (Geisel, 2004, p. 17). Given the equity capital requirements under Basel II and Basel III, more and more companies realize the benefits (Deloitte, 2009, p. 15) of Private Placements (Gündel & Katzorke, 2014). Basel II has the goal to ensure capital adequacy of financial institutions and to create standardized competitive conditions both for lending and loan trading; also, it aligns regulatory capital requirements (Rossi, 2011, p. 17) with actual risk and hence approaches the capital requirement, internally determined by those institutions (Herfurth, 2010, pp. 20-22), whereby the so-called regulatory arbitrage is to be reduced (Duthel, 2013, p. 76), thus making the allocation of risky and possibly non-performing loans on a larger scale unlikely in the entirety of its regulations (Kelm, 2007, pp. 4-11). On the other hand Basel III, refers to the regulations regarding the increase of quality (Zirkler, Hofmann, & Schmolz, 2014, pp. 1-4), consistency and transparency of equity capital, the improvement of risk coverage (Breidenbach, 2011, pp. 7-15), the introduction of a debt limit – the leverage ratio (Hofmann & Schmolz, 2014, p. 31) – the reduction of pro-cyclicality and the strengthening of counter-cyclical buffers (Walter, 2012, pp. 29-44), as well as the liquidity and the general reluctance of banks to grant loans as a result of the changing of the lending business of banks.

Turn Around

A Turn Around (Gietl, 2009, p. 33) financing is forced by external circumstances. If a company's structure is outdated and no longer competitive (Walters-Malcolm, 2007, pp. 19-22), Turn Around capital must be applied in order to keep the company alive (Schneider, 2011, p. 11). Accordingly, Turn Around capital is dedicated to logging off or respectively averting insolvencies; this happens, in extreme cases, if the company has already gone bankrupt (Lymbersky, 2013, pp. 53-56). Therefore, Turn Around financing does not only consist in the provision of capital by investors, but also in the change of its corporate strategy to bring it back on track, i.e. to lead it back to a competitive level on a sustained basis and take it back to profitability (Renz, 2015, p. 20). The goal of Turn Around financing is to ensure short-term liquidity (Mezger-Boehringer, 2015, pp. 1-4) and, as in a medium term, a constant cash flow (Renz, 2015, p. 20). Among the applied corporate strategies are marketing strategies (Krämer C. , 1992, p. 123), repositioning on the market, and a new corporate structure (KMU-Kredite, 2014; Krämer C., 1992, p. 123). Executive consultants could, if applicable, point out which measures could be taken in regards to the company's situation (KMU-Kredite, 2014; Schneider, 2011, p. 78). Due to the fact that Turn Around capital is being invested in financially-troubled companies, it is to be considered risk capital, because the financial sustainability is by far not secured with the provision of Turn Around capital (KMU-Kredite, 2014; Hommel, Knecht, & Wohlenberg, 2006, p. 399). In order to find an investor for Turn Around capital, a very sophisticated financing concept (Meusel, 2009, p. 64) must be presented by the company accordingly (KMU-Kredite, 2014; Meusel, 2009, p. 64). Also noteworthy is the role Debt to Equity Swaps plays in Turn Around. This concept involves a transaction between a debitor and creditor, in which the creditor relinquishes the debt of the debitor in turn for shares in the company (Gruner, 2015, p. 15). When Turn Around does not materialize, the shares can be sold to another investor in what is called a secondary sale (Schneider L. , 2011, p. 51 et seqq). Because this capital is afflicted with higher risks (KMU-Kredite, 2014), it should be difficult to obtain external financing in the form of bank loans (Hommel, Knecht, & Wohlenberg, 2006, p. 399), which is also why Private Equity is to be considered especially for such restructuring projects (KMU-Kredite, 2014).

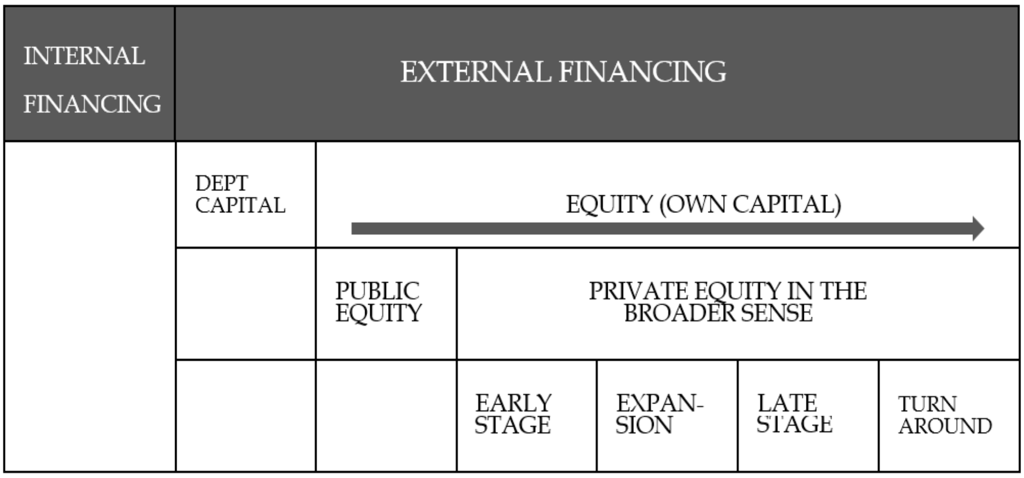
Buy and Build

The construct „Buy and Build" is classically known from the field of financial investors, especially from the Private Equity industry, and even emerged from it (Hoffmann N., 2008, p. 1-2). It designates a specific investment strategy, which is more than merely providing equity capital (Hoffmann N. , 2008, p. 39). This refers to any management services, which can be additionally provided. Such a strategy's goal is to acquire the company with complementary business models and thus consolidate fragmented and intransparent branches and markets (Karbenk, 2002, pp. 2-6). For Private Equity firms, this means that initially a financial investor identifies a fragmented – thus those which are fragmented and intransparent in itself – industry, which exhibits a high consolidation pressure (Moritz J. , 2008, pp. 373-391). Out of this industry, a company is then acquired which serves as a basis for further additional purchases of competitors and other target companies which prove to be reasonably supplemental for the business model (Borell & Heger, 2013). Jens Moritz (Moritz, 2008, pp. 373-391) means in his article "Private Equity und Mezzanine" (Picot G. , 2008), that a group of companies is established which reaches a critical mass within the formerly fragmented industry environment, and thus by using economies of scale – just those same positive effects, which result within the context of the dependence of the production volume on the quantity of applied production factors within a purposefully set up group of companies – holds a competitive advantage. While the term Buy and Build was heavily influenced by the financial investors, strategic investors are also increasingly taking over this concept (Jansen, 2008, p. 53). However, in this case, the search for a fragmented industry is not necessary. The initial acquisition of a base company is not required either, because the relevant company is already operating within a particular industry and acts insofar as a base company itself. Via this concept, respectively through these strategies, Private Equity can contribute to the fact, that competitiveness of enterprises in polypolistic markets is being increased (Beyer & Brüsken, 2011, p. 6).

Phases of a Private Equity Financing

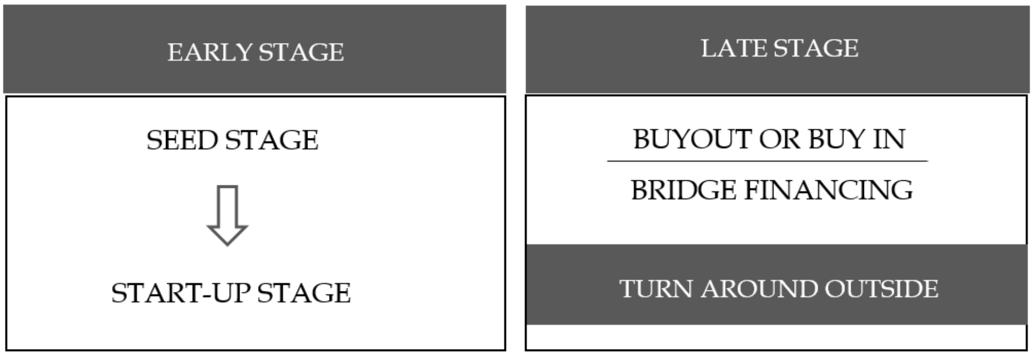
Figure 15 illustrates terminologically the development and financing phases (Philipp, 2012, pp. 8-12) of a company in this category (Reichling, Beinert, & Henne, 2005, p. 47) and where Private Equity (ITCONSULT, 2013) is located in the hierarchy of financing (Philipp, 2012, pp. 8-12; Tcherveniachki, 2007, p. 18).

Figure 15: Phases of Development of Private Equity



Source: Own representation based on Brettel et al., 2008, p. 14.

Figure 16: Earl Stage and Late Stage in the Norrow Sense



Source: Own representation.

A complementary graph (figure 16) shows the phases especially during the Early Stage (Kuntz, 2016, pp. 12-13), because of the participation of Venture Capital, the

Late Stage (Heister, 2010, p. 49), concerning Buyouts and Buy-Ins (Banks, 2010, p. 318) in detail, as well as Private Equity in the narrower sense; this is integrated in the next chapter.

For the use of Private Equity in the broader sense, the following phases are to be distinguished (Prym, 2011, p. 24), with the starting point being figure 15 (Brettel et al., 2008, p. 14).

- Early Stage (Lerch, 2011, p. 14),
- Expansion Stage,
- Late Stage,
- and Turn Around (Brettel et al., 2008, p. 14; Lerch, 2011, p. 14; Prym, 2011, p. 24).

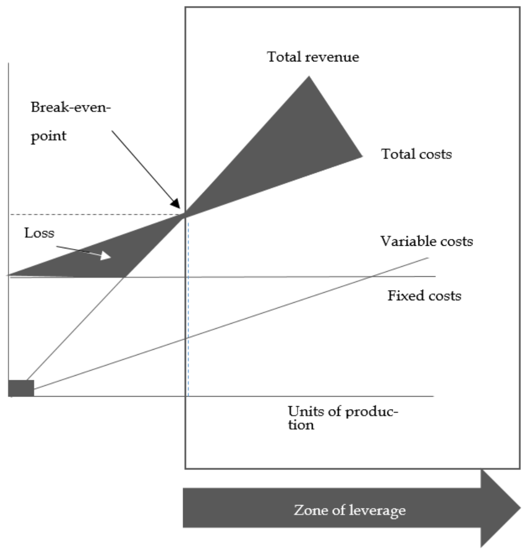
In the Early Stage (Kuntz, 2016, pp. 12-13), also chronologically as in figure 16, it is to be distinguished between the Seed Phase (Hahn C. , 2014, p. 83) and the Start-up Phase (Hahn, C.; 2014, p. 83; Lerch, 2011, p. 14, Prym, 2011, p. 24). The Seed Phase (Kaiser & Vöcking, 2002, p. 307) refers to the period of preparation specifically during the beginning of starting a business (Hahn, 2014, p. 83; Kaiser & Vöcking, 2002, p 307). Initially, the basics for the future company are being created here (Hahn, 2014, p. 83; Kaiser & Vöcking, 2002, p. 307).

In this phase (Seed), the product idea is being developed (Kollmann, 2004, p. 23), market analyses are being conducted (Heckmair, 2009, p. 10) and the business concept is being created (Kollmann, 2004, p. 23; Heckmair, 2009, p. 10). Regularly, the required capital is at least in part provided by the founders themselves or the personal environment of the founders at this stage (Saggau, 2007, pp. 13-15).

A commitment of Private Equity providers and Venture Capital companies at this Early Stage (Jacobi, 2010) is rather rare (Gaedke, Nöstlthaller-Kropf, Pinter, Rhomberg, & Weigl, 2012, p. 229). The Start-up Phase concerns the following development (Staroßom, 2013, p. 168) of a product to market maturity (Niederöcker, 2002, p. 214) and the creation of marketing concepts (Hahn, 2014, p. 68; Staroßom, 2013, p. 168; Niederöcker, 2002, p. 214). At this stage, the company is already heavily reliant on outside capital, as the running costs increase considerably, but at the same time (Busack & Kaiser, 2006, p. 20), no revenue is recorded (Busack & Kaiser, 2006, p. 20; Mes, 2011, p. 253).

During this Start-up Phase, a commitment by Venture Capital firms now occurs more often already (Hahn & Naumann, 2014, S. 127-128). The next phase describes the stage of growth (Weitnauer & Esser, 2008, p. 1017) of the young company after the successful market launch of the product, during which funds for the product expansion and the development of a larger sales market (Sacher, 2013, p. 12) are needed (Weitnauer & Esser, 2008, p. 1017; Sacher, 2013, p. 12).

Figure 17: Zone of Potential Leverage – Venture Capital Financing



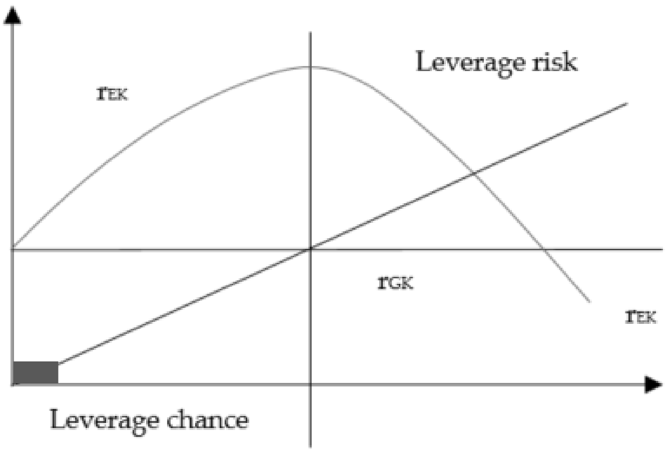
Source: Own model.

Already at this time, the borrowing of debt capital (Mayer M. D., 2003, p. 150) in addition to the financing by Venture Capital (Ege, 2003, p. 159) can be observed (Wenzl, 2010, p. 65). This (Kollmann, 2009, p. 51) is especially true with reaching the break-even point (Jennihsen, 1967, p. 81). Figure 17 shows the zone of the potentially appropriate application of debt capital. Depending on how the financing horizon is aligned, meaning the chosen form of participation (Saenger & Schewe, 2012, p. 307), the duration of the commitment (Lerch, 2011, p. 37) and the planned phasing out of the investment (Jesch, 2004, pp. 97 et seqq.), an increased application of debt capital from the break-even point may make sense (Renner, 2016, p. 63). Thinking about the locust debate (Maurenbrecher, 2008, p. 2) in regards to Leveraged Buyouts (Kaplan & Strömberg, 2009, pp. 121-146), this may not always be a positive signal (Maurenbrecher, 2008, p. 2; Kaplan & Strömberg, 2009, pp. 121-146). On the other hand, it certainly makes sense, especially in a dynamic market such as the high technology (Markert, 2009, p. 114) market for example, to apply, increasingly, capital from the break-even point on (Jürgens, 1994, p. 38), in order to conquer markets (Hackenberg & Empter, 2011, p. 124). In this regard, advantage could be taken from the Leverage effect (Murphy, 1968, pp. 121-123), which is known to state that through the application of debt capital (Sufana, 2013, pp. 783-787), the return on equity (ROE) on an investment can be increased (Cheng & Tzeng, 2014, pp. 1-63), where an investor can borrow debt capital at better rates than what the return on asset (ROA) will realize (Murphy, 1968, pp. 121-123; Sufan, 2013, pp. 783-787; Cheng & Tzeng, 2014, pp. 1-63). Under the premise that the borrowing interest remains constant even at a high debt-equity ratio (L), the following formula (Huch, Behme, & Ohlendorf, 1995, p. 188) applies (Wöhe, Bilstein, Ernst, & Häcker, 2010, pp. 42-49):

ROE = ROA + L * (ROA – return on borrowed capital).

It shall not be concealed at this point, that the application of debt capital in connection with Private Equity also harbors certain risks (Brettel, Kauffmann, Kühne, & Sobczak, 2008, p. 69). H. Kußmaul reconstructed a debt financed purchase (Kußmaul, Pfirmann, & Tcherveniachki, 2005, pp. 2533-2540) using the example of the take-over of Grohe AG (Kuttner R. , 2008, p. 122) in Germany, by the British Private Equity fund BC Partners (Kußmaul, Pfirmann, &. Tcherveniachki, 2005, pp. 2533-2540). Already in 1999, BC Partners (Sauermann, 2010, p. 218) acquired the company (Anonymous, 1999, p. 58), which had been profitable and expansive for decades (Kußmaul, Pfirmann, & Tcherveniachki, 2005, pp. 2533-2540). While the total capital amounted to approximately 1.1 billion D-mark in 1998, the equity ratio (Fisch & Roß, 2009, p. 256) ranged from 49.9% to 56.6% in the five years between 1994 and 1998 and the return on equity ranged from 29% to 31% (Jarass & Obermair, 2007, p. 43). The profit margin was 11% to 12% and the cash-flow increased steadily (Jarass & Obermair, 2007, p. 43). For the purchaser, this ongoing high cash-flow was an indication that they could service the liabilities resulting from debt financing of the purchase price with the cash-flow of the acquired company (Jarass & Obermair, 2007, p. 43). That led to the fact, that by 2003 the equity ratio was reduced to 6% and within a few years, the cash-flow was more than halved, as were the gross investments (Jarass & Obermair, 2007, p. 43). While from 1994 through 1998 significant annual surpluses had been earned, between 2000 and 2003 the company generated deficits (Jarass & Obermair, 2007, p. 43). At the end stood a heavily indebted company, which was sold for the purpose of restructuring (Jarass & Obermair, 2007, p. 44; Kuttner, 2008, p. 122). The result: many employees in Germany were laid off, plants were closed and productions moved abroad (Jarass & Obermair, 2007, p. 44). Therefore, an observation and a review of the funding situation of such transactions is crucially significant (Baumann R. , 2012, p. 57).

Figure 18: Risks of leveraging a Private Equity Transaction



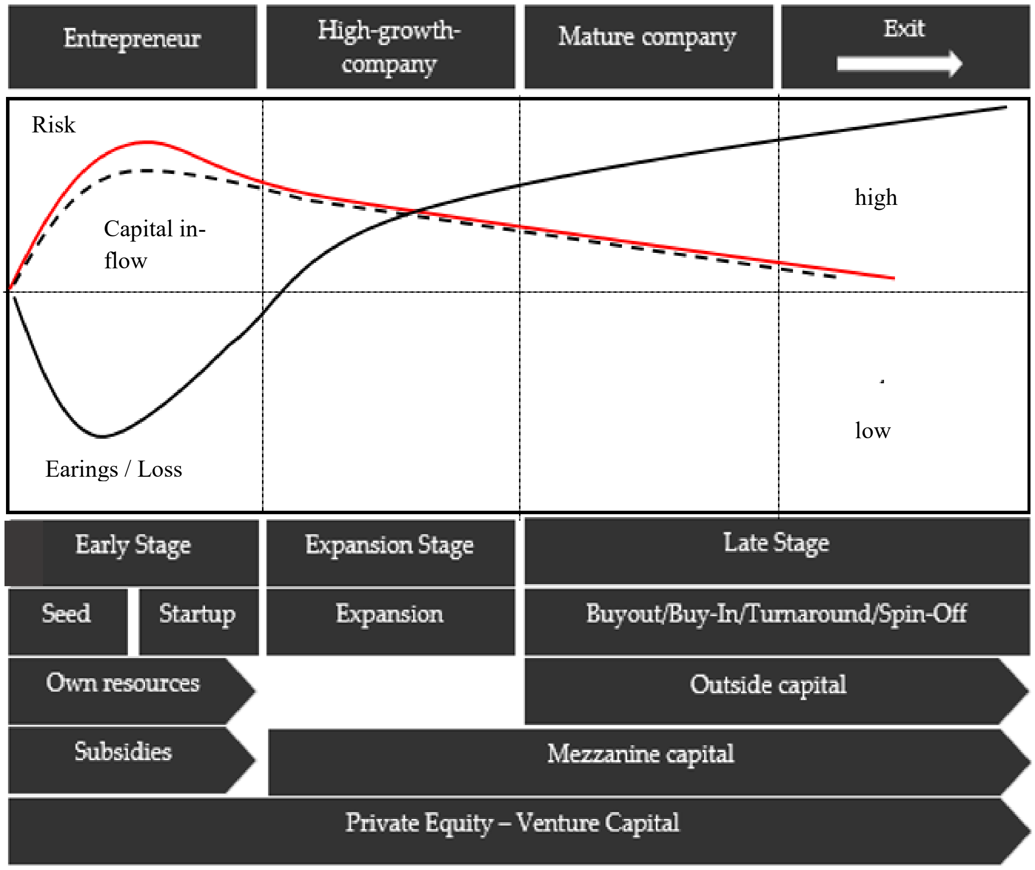
Source: Own representation based on Hofmann & Schmolz, 2014, p. 164.

Also, with a Private Equity (Hasan, 2014, pp. 73-101) transaction, the borrowing rate (Betge, 1998, p. 81) increases with the increase (Hutzschenreuter T. , 2009, p. 157) of the debt-equity ratio (borrowed capital/equity), since the default risk increases as well (Hasan, 2014, pp. 73-101; Betge, 1998, p. 81; Hutzschenreuter T.; 2009, p. 157). It can be realized in figure 18, that the return on equity (Nothacker, 2015, p. 111) only increases as long as the overall profitability (Köhler K. , 2014, p. 61) and the borrowing rate (Gaedke, Nöstlthaller-Kropf, Pinter, Rhomberg, & Weigl, 2012, p. 86) curve meet (Eichhorn, 2005, p. 220). The Leverage risk (Hofmann & Schmolz, 2014, p. 164) arises at ROA < I (Busse, 2003, p. 839). Therefore, at this point, the risk of over-indebtedness of the company occurs (Horst, 2014, p. 111), provided that the funding is taken from the cash-flow (Horst, 2014, pp. 113-115).

In the final stage of a company's development (Vater, 2003, p. 53), the Late Stage (Vogt, 2007, p. 14), the capital investments are being divided mainly (Harris T. J., 2002, S. 59-63) into two financing situations:

- Bridge Financing (Hockenbrink, 2015, p. 69; Bayaz, 2013, p. 41),
- and Management Buy-Ins (MBI), Management Buyouts (MBO), Spin Offs (Bayaz, 2013, p. 41; Herzog, 2014, p. 22).

Figure 19: Entire Course of a Private Equity Transaction



Source: Own model based on Hackl & Jandl, 2004, p. 194 et seqq.

Bridge Financing (Bayaz, 2013, p. 41; Hockenbrink, 2015, p. 69) is the provision of additional financing, which is required by more mature companies to overcome obstacles to growth or to prepare for the IPO (Rosenstein, Bruno, Bygrave, & Tylor, 1999, pp. 99-113). Figure 19 shows a possible course of a Private Equity transaction (Hackl & Jandl, 2004, p. 194 et seqq).

Management Buy-Ins (Robbie & Wright, 1996, p. 5) or Management Buyouts (Herzog, 2014, p. 22) serve, as already explained above, the financing of the acquisition of a company by an external or the existing management. Spin-Offs (Richards, 2008, p. 7), however, are spin-offs from companies, which concentrate increasingly on their core business (Bayaz, 2013, p. 41; Herzog, 2014, p. 22).

Finally, outside the normal business development is the so-called turnaround phase (Vater, 2003, p. 53; Bayaz, 2013, p. 41). Frequently, this term (Jesch, 2004,, p. 94) describes the time period in which a financially-stricken company is being led out of a period of losses by means of restructuring measures zone (Schneider L. , 2011, p. 11) and back into profit (Jesch, 2004, p. 94; Schneider L., 2011, p. 11).

2.1.2.4 Classification of Private Equity as Equity Capital

The 70s and 80s were characterized by an increasing demand for financing of expansion investments (Daniels, 2004, p. 12; Tcherveniachki, 2007, p. 17) of established companies (Seeburger, 2010, pp. 38-39), preparatory actions to initial public offers (IPOs) as well as leveraged and management Buyouts (Daniels, 2004, p. 12). Due to this fact, the term Private Equity (Bernhardt, 2010, p. 83) was developed, which was used until the mid-80s homonymous (Jugel, 2003, p. XI) with the term Venture Capital (Bernhardt, 2010, p. 83; Tcherveniachki, 2007, p. 17). After that, Private Equity proceeded to be applied as a general term for equity capital in the USA and Europe, under which - to complement the above discussion - at first the financing products Venture Capital and Buyout Capital were summarized (Krecek, 2005, pp. 6-7) as subordinate terms (Tcherveniachki, 2007, p. 17). Buyout Capital is understood as the provision of equity (Tcherveniachki, 2007, p. 17) that should serve to finance acquisitions (Jesch & Kreuter, 2002, pp. 407-412), if necessary in combination with substantial debt capital (Jesch & Kreuter, 2002, pp. 407-412; Tcherveniachki, 2007, p. 17). In addition, Private Equity companies have a focus on the capital structure if they want to make a Leveraged Buyout (Axelson, Jenkinson, Tim, Strömberg, & Weisbach, 2013, p. 2223). In this context, as a reminder, it is to be differentiated between Management Buyout (MBO), Management Buy-in – MBI – (Jesch, 2004, p. 91), and Leveraged Buyout – LBO – (Jesch, 2004, p. 93; Tcherveniachki, 2007, p. 17). While a MBO (Lujen, 1992, pp. 106-109) is always present when the company acquisition is being conducted by the existing company management

(Herzog, 2014, p. 20), MBI requires the participation of an external management in the acquisition (Tcherveniachki, 2007, p. 17; Lujen, 1992, pp. 106-109; Herzog, 2014, p. 20). LBO means that the company in question is overtaken by an external group of investors (Tasma, 2012, pp. 11-14), which in turn commissions the existing management or an external management team with the company management (Tchervenichki, 2007, p. 17; Tasma, 2012, pp. 11-14). In a leveraged Buyout, the target is acquired by a specialized investment firm using little equity (Tcherveniachki, 2007, p. 17) and more outside debt financing (Kaplan & Strömberg, 2009, p. 121).

Long ago, Mezzanine Capital had been included under the general term of Private Equity (Weißflog, 2015, p. 83), which is a hybrid form of financing, as stated above, which ranges between equity and debt capital (Weißflog, 2014, p. 83; Tcherveniachki, 2007, p. 17). Subordinate loans or convertible and option bonds (Guserl & Pernsteiner, 2004, p. 829) are to be mentioned (Dürr, 2007, p. 52) in this context as well (Tcherveniachki, 2007, p. 18; Guserl & Pernsteiner, 2004, p. 829; Dürr, 2007, p. 52). Usually, Venture Capital financing is being complemented (Lühn, 2013, p. 34) by Mezzanine Capital (Tcherveniachki, 2007, p. 18; Lühn, 2013, p. 34). The same applies for Buyout financing (Tcherveniachki, 2007, p. 18; Lühn, 2013, p. 34).

The following empirical study is to be drawn up to determine the interests of private equity companies. It is also intended to establish the extent to which the Ventura Capital activities of the investment companies under investigation are significant. At the beginning of the work, it was assumed that improved tax conditions also entail an increased commitment of the participating companies.

2.1.2.5 Forms of Participation – Empirical Analysis

Preliminary Remarks

At the beginning of their activities, Private Equity companies have a conception about which type of participation (Eilenberger & Haghani, 2008, p. 28) they want to incur (see 2.1.2.5). A number of investment types are available for this purpose (Matz, 2002, p. 41). Although there are hybrid forms of participation, the industry essentially relies on the standard forms of participation. Initially considering the willingness of portfolio companies to publicize their participation or not, a distinction is made between a direct open participation (Zepezauer, 2012, p. 163) and a silent partnership (Prätsch, Ludwig, & Schikorra, 2007, p. 208). In an open, specifically direct participation (figure 20), the affiliates acquire shares in a target company, in which they are to be co-shareholder for a limited time (Kienbaum & Börner, 2003, p. 364). The silent partnerships (Reichling, Beinert, & Henne, 2005, p. 254 et seqq) do not legally represent equity, however, are regarded as economic equity (Kollmann, 2005, p. 307) and thus have a positive impact, for example, on the credit rating of the target company (BVK, 2015). In this form of participation, the shareholders will post a deposit in the assets of the company without acquiring shares of the company (Wöhe G. , Bilstein, Ernst, & Häcker, 2013, p. 77).

Figure 20: Forms of Participations in Regards to Readiness to open

Source: Own representation based on Zepezauer, 2012, p. 163 and BVK, 2015.

Because of the definition of maturity and interest rate and other performance-based compensation, however, the silent (figure 20) participation (Sunderdieck, 2015, p. 65) is not dissimilar (Löffelholz, 1993, p. 12) to a traditional loan (BVK, 2015; Löffelholz, 1993, p. 12; Sunderdieck, 2015, p. 65). After the stipulated time, the target company will return the silent participation including accrued interest (BVK, 2015; Niederöcker, 2002, 239). As the name already implies, this participation (Paul, 2015, 223) remains mostly anonymous (Pleschak, 2001, p. 98). The shareholders will not be entered in the commercial register (Pleschak, 2001, p. 98) and usually do not represent the company externally (Schneider & Fritz, 2013, p. 135).

Depending on how the protagonists – that is, the holding company and the target company – have agreed upon, a further division (Gietl, 2009, p. 18) into majority interest and minority interest (Honold, 2012, p. 1) is being applied (Göppert & Müller, 2014, pp. 189-207). Simplified, a majority interest is on hand, if the ownership exceeds 50%, while a minority interest is on hand (Lucks & Meckl, 2015, p. 31), if the ownership is below 50% (Zentes & Swoboda, 2003, p. 532). The percentage of shares held triggers legal consequences, especially in terms of profit sharing and voting rights, as also in any other company (Kisslinger-Popp, 2014, p. 206). Blocking minorities can block decisions (Burger, Ulbrich, & Ahlemeyer, 2010, pp. 14-15) as well as some decisions require qualified majorities – that is, a participation quota of more than 75% (Ampenberger, 2010, p. 201). At this point allow for the participation arrangements not to be discussed at further length. Other forms of participation are participation certificates (Guserl & Pernsteiner, 2015, p. 404) and subordinated loans (Hoppe, 2005, p. 51), which are either part of the atypical silent partnership (participation certificates) or the typical silent partnership (subordinated loans), but are in either case attributable (BVK, 2013) to the Mezzanine Capital (BVK, 2013; Guserl & Pernsteiner, 2015, p. 404; Hoppe, 2005, p. 51). One specificity of participations is being scarcely or not at all discussed (equitrust, 2015) and thus rarely is being approached throughout pertinent literature – revenue sharing. This means that the participating company does not participate, as in all other assumptions, from the sale of the company or the sale of the shares, but permanently from future profits.

Analysis Design

Before the start of their commitment, it is of considerable importance for the Private Equity companies and their funds in which sector they would like to invest, whereas sector describes how and when they wish to participate in a target company. Hence, for this study it has been empirically examined, whether or not the type of participation (Grethe, 2010, p. 69) will also simultaneously trigger a particular financing purpose. The financing purposes from the view of the target company (Brettel, Kauffmann, & Kühn, 2008, p. 32) have already been discussed in the previous chapter. However, and slightly differing therefrom, the analysis is based on the chronological employment by the Private Equity companies (Lühr, 2010, p. 191).

The hypothesis, that Private Equity companies favoring a particular type of participation also prefer to invest at a particular time, respectively choose a particular financing purpose, constitutes the superior hypothesis.

Further hypotheses were proposed during the course of the study and are prepending the respective results. The selection of subject matter of these studies (Sellien & Sellien, 1980, p. 1362) first requires an objective, spatial and temporal delimitation of the population (Müller W. , 2005, pp. 1-122). Population describes the amount of analysis units considered, about which a statement is to be made (Bankofer & Vogel, 2008, p. 5). An analysis unit, in this context, denotes a subject, on which the measurements are to be taken (Bol, 2004, pp. 9-15). Initially, more than 300 records of as many Private Equity companies within Europe were examined. Changes in statements of the Private Equity companies made after June 30, 2016 have not been taken into account. In material terms, all companies listed in relevant member directories, such as those of the EVCA, respectively Invest Europe (Europe, 2016) or the BVK (BVK, 2016), have been examined. The first pre-selection reduced the volume of data records to little more than the above-mentioned 300. Out of these data records, 163 in turn proved to be valid and ultimately served for the analysis.

In addition to the company names, which of course remain unpublished herein, the following have been recorded:

- Type of investment.
- Equity investments.
- Managed capital.
- Transaction volume.
- Number of employees.
- Investors.
- Legal form.
- Turnover of the portfolio companies.

- Financing purposes.
- Industries.

Since only the interrelation between type of investment and financing purpose was to be examined, the remaining data were not subject to detailed analysis. However, subsequent to this study, they could certainly be helpful. Thus, further studies could possibly provide indications to the target company regarding the orientation and previous success of the Private Equity companies.

Regarding the types of participation, the following details of the Private Equity companies have been examined:

- Silent partnership.
- Direct open participation.
- Minority holding.
- Majority holding.
- Loans.
- Participation certificate / Mezzanine.

On part of the financing purposes, the following has been examined:

- Seed stage.
- Start-up Phase.
- Expansion phase.
- Bridge financing.
- Secondary Purchase (Daniels, 2004, p. 50; Manchot, 2010, p.2).
- Public to Private.
- Small Buyout.
- Mid-Buyout.
- Large Buyout.
- Turnaround.

The statistical data analysis and the presentation of the research results is done with Statistic R and Microsoft® Excel PowerPivot/View. First, the absolute frequency of participation types and financing purposes is presented. To determine the correlation between different types of investment and financing purposes, the chi-square test is being applied (Papula, 2016, p. 607). In mathematical statistics, the chi-square test denotes a group of hypotheses tests with X^2-distributed test statistics (Bleymüller, 2014, p. 127). In this case, X^2 (Henze, 2004, p. 247) describes the measure value originated from Karl Pearson (Porter, 2010) and is being determined in the calculation of one-dimensional frequency distribution (Hafner, 1992, p. 9 et seqq.) as follows:

Figure 21: Calculation of X^2 in One-Dimensional Frequency Distribution

$$X^2 = \sum_{j=1}^{J} \frac{(oj-ej)^2}{ej}.$$

Source: Own representation based on Hatzinger, Hornik & Nagel, 2011, p. 162.

It is being defined for (Hatzinger, Hornik, & Nagel, 2011, p. 162):

- oj = observed frequency for category j (o = observed),
- ej = expected frequency for category j (e = expected),
- J = overall quantity of categories.

The X^2 value provides us with information about the size of deviations between expected and observed frequencies (Hatzinger, Hornik, & Nagel, 2011, pp. 147-192). Based on the formula in figure 21 it can be observed that the size of deviations between expected and observed frequency increases (Hatzinger, Hornik, & Nagel, 2011, pp. 147-192). This value shall provide information about whether or not the deviations are significant (Hatzinger, Hornik, & Nagel, 2011, pp. 147-192).

2.1.2.5.1 Analysis and Assessment

The 163 Private Equity companies have been investigated regarding the type of investment and the financing purposes. First off, it was determined how frequently the individual types of investment do occur. The Private Equity companies could make multiple entries.

The following perception, often cited by politicians (Peters, 2008) and other critics (Heilmann, 2015) throughout the media, serves as a hypothesis:

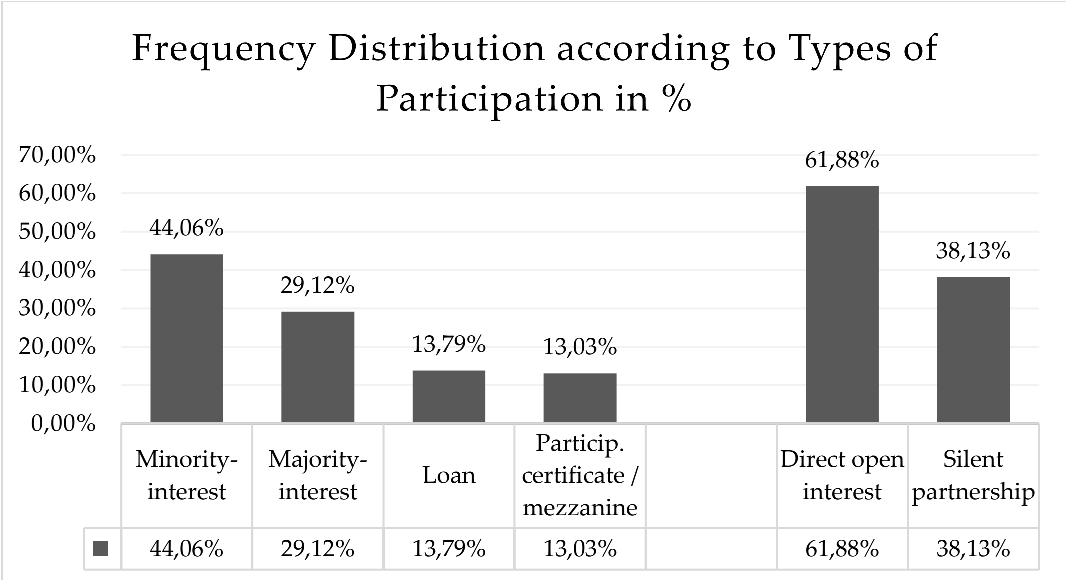
The majority holding – up to a takeover – is the most common type of investment.

Already in the first analysis it is clear that contrary to public opinion which states that Private Equity firms are primarily acquiring companies in order to profitably sell them again, obviously minority interest is the most common form of participation.

Even if direct (Reichling, Beinert, & Henne, 2005, p. 20) open (Investoren-Beteiligung, 2016) participation (Lessat, et al., 1999, p. 95) has been named more commonly, the silent partnership is still clearly not underrepresented.

According to this assessment, minority interests (Kauffmann, 2009, p. 37) still clearly take the lead over majority interests (Sacher, 2013, p. 10), which derive a value about a high as that of the subordinated loan (Haunerdinger & Probst, 2006, p. 92) with Mezzanine Capital (Dürr, 2007, p. 24). In terms of percentage this result displays a share of minority interest of approximately 44% while the majority interest reaches roughly 29%. However, with around 13% each, the remaining investment opportunities are not irrelevant either. Participation certificates and subordinated loans, as explained above, pertain to Silent Partnerships. This percentage evaluation for majority and minority interests only displays a tendency. Important in this figure is that it is evident that the subordinated loans and participation certificates as Silent Partnerships are equally often applied. Figure 22 shows the frequency distribution by type of participation, ie the type of participating most frequently occuring.

Figure 22: Frequency Distribution according to Types of Participation in %

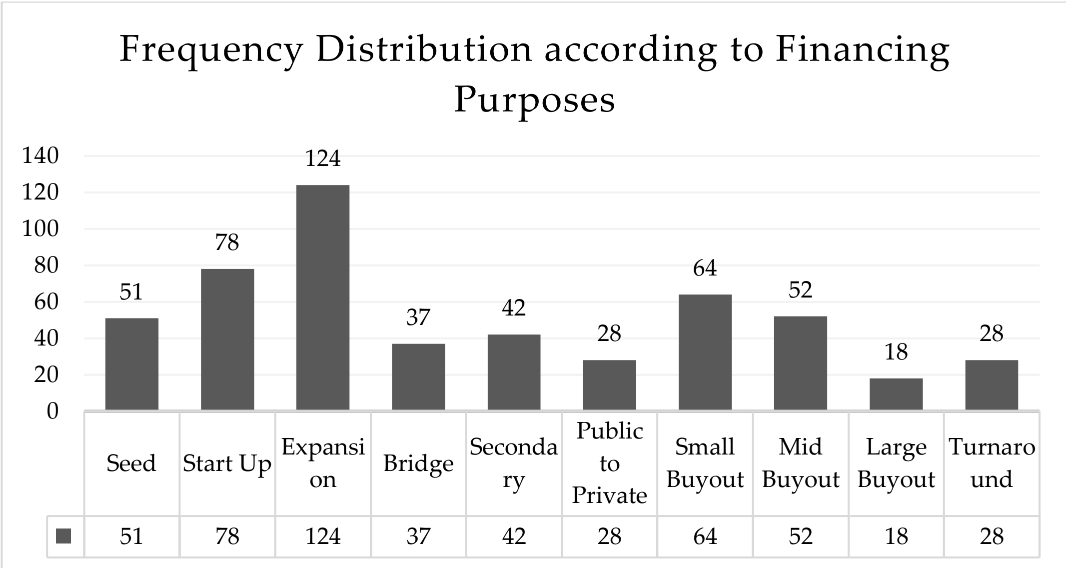


Source: Own representation.

On the other side, the data to be examined is the financing purposes. The assumption in the form of a hypothesis regarding the financing purposes shall be:

The most common type of participation on the side of the Private Equity companies takes place in the context of a Large Buyout (Fraser-Sampson, 2010, p. 61) - quasi corresponding to the assumption that all Private Equity companies are buying enterprises.

Figure 23: Frequency Distribution according to Financing Purposes



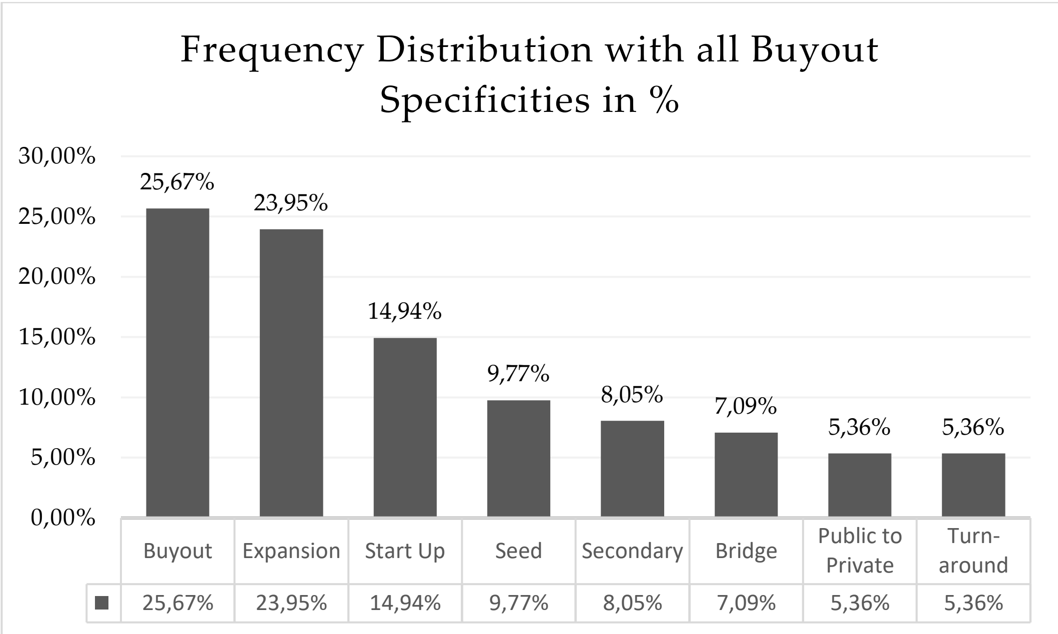
Source: Own representation.

Considering the analysis in such a detailed manner as shown in figure 23, the investment occurs very frequently during the expansion stage of a target company (Jesch, 2013, p. 97). According to the Private Equity companies, investments in target companies during the Start-up Phase (Weißflog, 2015, p. 83) come in second place. Thus, according to the above definition, a strong Venture Capital exposure may be assumed. The next examination is based on the assumption that all Buyouts total the largest share of responses regarding the financing purposes. Thus, the hypothesis is:

Private Equity companies invest from the outset on in target companies with the intention of a Buyout.

Taken the analysis in figure 24 any further assumption is not yet recognizable. This assumption, whether Private Equity companies select a preferred financing purpose next to a specific type of investment, is examined with the chi-square test. While at first it seemed as though the participation in expansions would be very distinct, the hypothesis that Private Equity companies preferably invest in target companies with the intent for a Buyout may be presumed appropriate.

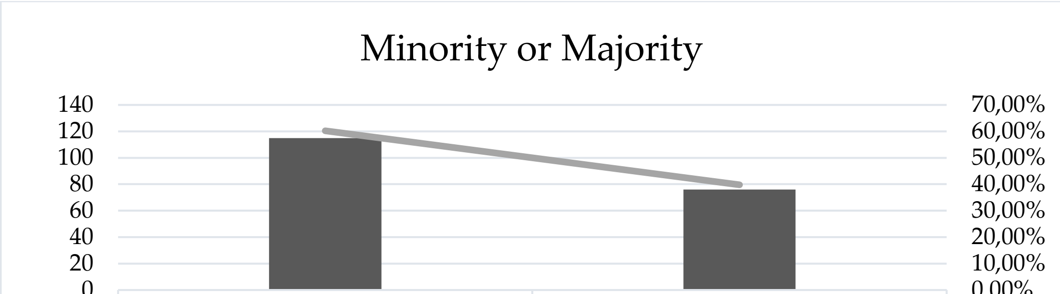
Figure 24: Frequency Distribution with all Buyout Specificities in %



Source: Own representation.

The representation of individual figures relevant to the majority and minority interest is shown in Figure 25.

Figure 25: Minority Interest or Majority Interest



	Minority-interest	Majority-interest
(bars)	115	76
(line)	60,21%	39,79%

Source: Own representation.

Post-Deliberation

During the investigation of participation types, the majority and minority interests were not extracted from the loans, participation certificates and Mezzanine Capital but analyzed according to the number of entries. Now considering the investments exclusively by their majority or minority character, in terms of the chi-square test it is already noticeable that there is no apparent connection yet between the majority interest and the Buyouts, at least by frequency.

2.1.2.5.2 Chi-Square Test

The following hypothesis has been the initial point of the considerations:

The investments made by Private Equity companies having a majority interest character, lead to a Buyout investment.

This test is based upon the above-mentioned data and is referred to as test x1. First, an active data matrix in terms of descriptive statistics was created, which only represents a summary statistic. The variables mean:

- MiHB = Minority Interest.
- MeHB = Majority Interest.
- DOB = Direct Open Participation.
- D = Loan.
- G.M = Participation Certificates / Mezzanine.
- SB = Silent Partnership.
- Br. = Bridge financing.
- Seed = Seed.
- SUP = Start Up.
- Expans. = Expansion.
- Second. = Secondary.
- PP = Public to Private.
- SM = Small Buyout.
- MB = Mid Buyout.
- LB = Large Buyout.
- TA = Turnaround.

```
MiHB    MeHB   DOB    D       G.M     SB      Br.     Seed    SUP    Expans. Second.
0: 48   0:87   0:64   0:127   0:129   0:102   0:126   0:112   0:85   0: 39   0:121
1:115   1:76   1:99   1: 36   1: 34   1: 61   1: 37   1: 51   1:78   1:124   1: 42
PP      SM     MB      LB      TA
0:135   0:99   0:111   0:145   0:135
1: 28   1:64   1: 52   1: 18   1: 28
```

In order to show a recognizable significance, Statistic R uses the function of a cross tabulation, which looks as follows for this test:

```
       SM
MeHB    0  1
   0   69 18
   1   30 46
```

and determines the test data:

```
        Pearson's Chi-squared test

data:  .Table
X-squared = 26.9942, df = 1, p-value = 2.041e-07.
```

In this case, the null hypothesis H_0 (Holling & Gediga, 2016, p. 23) is: The small Buyouts (Cendrowski, Petro, Martin, & Wadecki, 2012, p. 45) cannot be significantly linked to the majority interest. It is generally said, that if the p-value is large, the null hypothesis is retained, and if the p-value is small the null hypothesis is rejected.

Three figures are found in the output. The first, the x-squared (Wollschläger, 2016, p. 177), indicates the value 26.9942. This is Pearson X^2, thus the difference between the expected and observed frequencies. The second value, df, is the degree of freedom (Pesch, 2003, p. 120) and shows the number of categories minus 1 (Hatzinger, Hornik, & Nagel, 2011, p. 162). The third figure, the p-value (Browner, 2006, p. 63) is the most important here.

As comparison value for this test, 0.05 is specified. The significance level (Hatzinger, Hornik, & Nagel, 2011, p. 161) is thus 0.05 and means 5% probability that small Buyouts are not significantly often linked with majority interests.

Interpretation

The null hypothesis that small Buyouts do not significantly often correlate with majority interests had to be discarded due to a chi-square test (X^2 = 26,9942, p < 0,05). The data rather indicates that there is an interrelation between the participation type of majority interest and a small Buyout.

It has already been established in the previous analysis - frequency distribution - that in the accumulation of the different Buyout forms, the Buyout is the most common financing purpose, so that it is already clear that there is a correlation between

Buyouts and the form of participation – the majority interest. The reason behind this assumption is that the cumulative counting leads to the p-value getting even smaller.

To support this observation, the evaluations of the other two Buyout forms, Mid-Buyout and Large Buyout, are to be analyzed and reported at this point.

Mid—Buyout of majority interest:

```
    MB
MeHB  0  1
   0 82  5
   1 29 47


        Pearson's Chi-squared test

data:  .Table
X-squared = 58.7546, df = 1, p-value = 1.786e-14.
```

Large Buyout of majority interest:

```
    LB
MeHB  0  1
   0 87  0
   1 58 18

        Pearson's Chi-squared test

data:  .Table
X-squared = 23.1632, df = 1, p-value = 1.488e-06.
```

Both p-values are extremely small, so it is very plausible that the entire Buyouts are in distinct correlation with the commitment of Private Equity companies in majority interests.

Counter-Analysis

If the majority interests correlate with the Buyouts, the assumption is at hand that minority interests rather cannot be associated with Buyouts. This can be assumed with certainty. Therefore, the possible correlations of minority interest and the financing purposes exclusive of Buyouts were examined. However, only three financing purposes with a high probability of correlation with minority interests shall be displayed.

One assumption (hypothesis) is that:

Minority interests are often in correlation with an early stage of financing of a Private Equity target company.

The early stages of financing of a target company include the Startup phase, the Seed Phase and, as a transition phase, the Expansion phase.

The null hypothesis H_0 for a correlation between the Expansion phase and minority interest is:

Private Equity companies seeking a minority interest will not invest in target companies wishing to expand.

Expansion phase to minority interest:

```
     Expans.
MiHB   0   1
   0  20  28
   1  19  96


        Pearson's Chi-squared test

data:  .Table
X-squared = 11.7636, df = 1, p-value = 0.000604.
```

The null hypothesis H_0 for a correlation between the Seed Phase and minority interest is:

Private Equity companies seeking a minority interest will not invest in target companies being in the Seed Phase.

Seed phase to minority interest:

```
     Seed
MiHB  0  1
   0 42  6
   1 70 45


        Pearson's Chi-squared test

data:  .Table
X-squared = 11.1711, df = 1, p-value = 0.0008308.
```

The null hypothesis H_0 for a correlation between the Startup phase and minority interest is:

Private Equity companies seeking a minority interest will not invest in target companies in the Startup phase.

```
      SUP
MiHB  0  1
   0 32 16
   1 53 62


        Pearson's Chi-squared test

data:  .Table
X-squared = 5.7477, df = 1, p-value = 0.01651
```

Interpretation

Importance for Entrepreneurs

According to the analysis of these data, it seems as if a large part of the Private Equity companies actually intend to generate profits by buying companies or company shares and – presuming good intentions of the Private Equity firms – reselling them again after a certain time of the investment and management support. This business is being flanked by risky investments during the early stages of a company, which would explain the minority interest. Entrepreneurs are therefore well advised, should they have the option of choice, to take a careful and closer look at the investor. For the larger the participation of Buyout companies is, the larger the risk to suffer a similar fate as the Grohe AG (Regner, 2008, p. 71) in re gards to a leveraged Buyout.

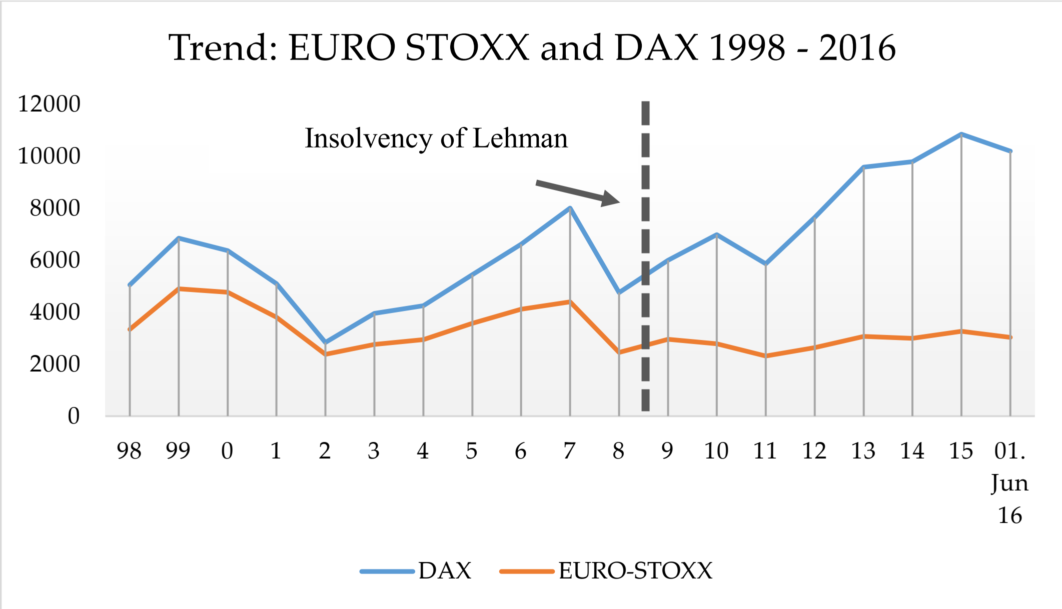
At the end of this study, the theoretical impact of changes in the tax environment will be re-examined with regard to the willingness to invest in venture capital and thus in entrepreneurs with regard to the above data. Here, too, the hypothesis is that, if the number of participating companies with the number x is involved in the current conditions with the volume y in the early stages of a target company, these investment companies will increase their number and scope in an improved framework for venture capital.

Another figure is important for entrepreneurs - but also for affiliates. In total, 2.435.214.550,00 euros were collected by the Member States examined in 2015. This money is preferably acquired by investment companies. That makes a per capita fundraising of 87,35 euros. For entrepreneurs, it is important that a larger share is invested in the direction of venture capital. At the moment, the share is slightly too low with a little over 22,00 euros (see chapter 4.1). The aim of this study is to extract better tax conditions. The associated hypothesis is if there are optimized tax conditions for venture capital, the interest of venture capital companies also increases. This would lead to more venture capital companies.

2.1.2.6 Digression: Private Equity as Asset Category

It is debatable whether and to what extent Private Equity constitutes an asset category of its own (Fleischhauer, 2008, pp. 1-6). At least it is widely agreed that Private Equity is to be classified as an alternative investment (Metrick & Yasuda, 2011, pp. 619-654) alongside Hedge funds (Kaiser D.G., 2004, p. 117) and derivatives. In this context, Hedge funds are to be understood as unregulated or hardly regulated investment funds, which are actively managed (Gülener, 2012, p. 5). According to its naming and the originally associated hedging, it is now hardly being communicated with such a vehicle (Kremer, 2014). In most cases, Hedge funds (Wellas, 2011, p. 238) are characterized by a particularly risky investment (Ruchay, 2014, p. 9) strategy (Ruchay, 2014, p. 9; Wellas, 2011, p. 238). The aforementioned collapse (Diaz-Bone & Krell, 2015, p. 299) of Lehman Brothers (Capek, 2010, p. 93) is attributed in no small measure to these funds, which is why they were, for instance in Germany until 2003 (Kamp & Krieger, 2005, p. 71), temporarily banned (Capek, 2010, p. 93; Diaz-Bone & Krell, 2015, p. 299; Kamp & Krieger, 2005, p. 71). Derivatives, however, are financial products whose price and development depend on the price of another financial product (Payami, 2013, p. 13), such as possibly a share (Bösch, 2014, pp. 2-5). It is, in a broader sense, a financial asset speculating on whether the price of a product increases or decreases in the future (Hull, 2009, p. 24). Lumping Private Equity together with these investment instruments would be almost unfair, if only for its initial positive overall orientation – supporting companies by providing equity.

Figure 26: Trend of EURO-STOXX and DAX from 1998 to June 2016



Source: Own representation. Data from boerse.de, 2016.

Private Equity transactions showed a positive average performance during the financial crisis in 2008 and thus outperformed the stock investments. This excess return is documented by a study of Golding Capital Partners and Oliver Gottschalg (HEC Paris), which was published on May 27, 2014 (Gottschalg & Golding Capital Partners, 2014). The study wanted to prove that Private Equity investments can achieve more Alpha than a comparable investment in equities. In order to apply a better classification, figure 26 displays the development of the Euro-STOXX. The German stock market index (DAX) is used as a reference (boerse.de, 2016). In each case, the final rate information of the last trading day of a year, respectively in 2016, the rates of the last observation in June (boerse.de, 2016), were taken into account.

In this study (Gottschalg & Golding Capital Partners, 2014), about 5.600 Private Equity transactions between the years 1977 through 2014 were examined, whereas one of the questions to be answered was whether the Alpha of Private Equity transactions (Buchner, 2014, pp. 1-58) is above comparable yields on the stock market and thus, whether this is repeatable. The study (Gottschalg & Golding Capital

Partners, 2014, pp. 1-5) provides a comparison of the two asset classes of Private Equity and shares. For this purpose, a similar investment in shares is derived for each Private Equity transaction, which takes the following factors into account:

1. Timing effect.
2. Industry effect.
3. Leverage effect.

In this context, the timing effect describes the respective points in time of in- and outflows (Gottschalg & Golding Capital Partners, 2014, p. 1), the industry effect the influence of the movement of the industry in which the company operates (Gottschalg & Golding Capital Partners, 2014, p. 1), and the leverage effect (Gottschalg & Golding Capital Partners, 2014, p. 1) – q.v. chapter 2.1.2.3 under Risks by Leverage at a Private Equity transaction – the level of indebtedness of the Private Equity investments compared to listed companies (Gresser, 2005, pp. 5-6). For this study (Gottschalg & Golding Capital Partners, 2014, pp. 1-5), the return rate of Private Equity transactions is being adapted by using the M-IRR (Modified Internal Rate of Return), whereas the M-IRR (Lin, 1976, pp. 237-248) represents a method to marshal alternative assets of equal volume (Askar & zu Knyphausen-Aufseß, 2008). The target is to map a realistic reinvestment (Gottschalg & Golding Capital Partners, 2014, p. 1). Basically, the Alpha refers to that part of the return which exceeds the calculated or assumed rate of return (faz.net, 2016). The share of the adjusted Private Equity returns which cannot be achieved by a similar investment on the stock market is the Alpha of Private Equity (Gottschalg & Golding Capital Partners, pp. 1-5). The question of the Alpha in respect to the financial crisis could be more nuanced (Gottschalg & Golding Capital Partners, pp. 1-5):

Will the results for the long-term Alpha, the Alpha over the cycle and the Alpha during the crisis remain stable?

For the analysis of persistence, that means a repetition of excess return (Kunze K.-K. , 2009, pp. 14-15), the following methods were used, see Golding Capital Partners, 2014:

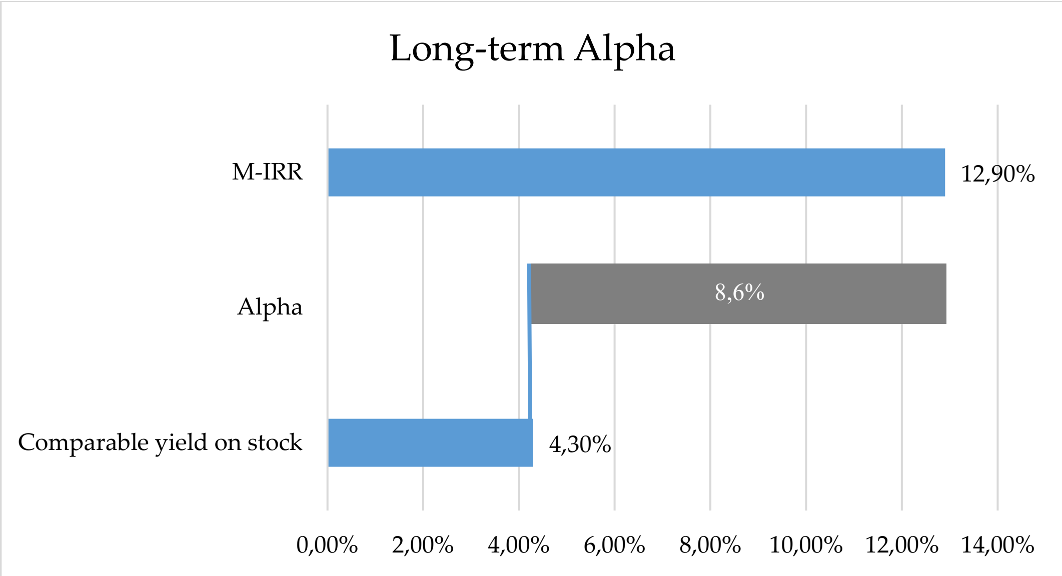
- the correlation of the examined variables of the previous period to the same variables of the subsequent period and
- the contribution to the portfolio return by the specific selection of fund managers whose performance is within a certain quartile[7] (in the case of the present study this performance ranks in the top quartile), with the subsequent calculation of the effect of these selections relative to an investment in the overall market (Gottschalg & Golding Capital Partners, 2014, pp. 1-5).

The result of this analysis brings to light that Private Equity transactions average a positive Alpha of 8.6% over the comparable (see figure 27) yield on the stock market (Gottschalg & Golding Capital Partners, 2014, pp. 1-5). The Alpha above the capital market cycle is shown in figure 28.

The return analysis shows that the transactions active at the height of the financial crisis could achieve an Alpha of 3.3% (see figure 29) over comparable returns on the stock market (Gottschalg & Golding Capital Partners, 2014, pp. 1-5). The absolute return for these very difficult transactions moves below the long-term average, however, remains positive at 5.3% (M-IRR), while the comparable stock return ranges in the negative (Gottschalg & Golding Capital Partners, 2014, pp. 1-5).

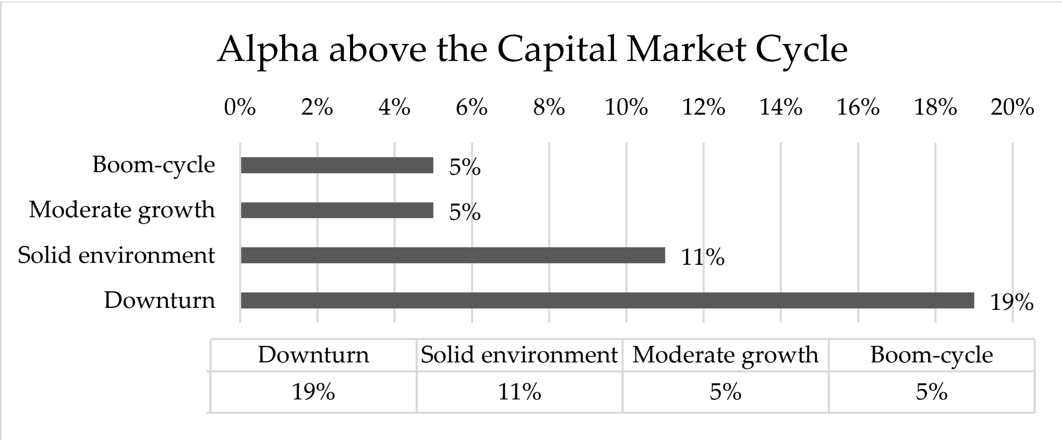
[7] Share quartile means the underlying distribution in four quarters. So a particular quartile is the boundary between two neighboring quarters of the distribution (Lohninger, 2016).

Figure 27: Long-term Alpha of Private Equity Investments



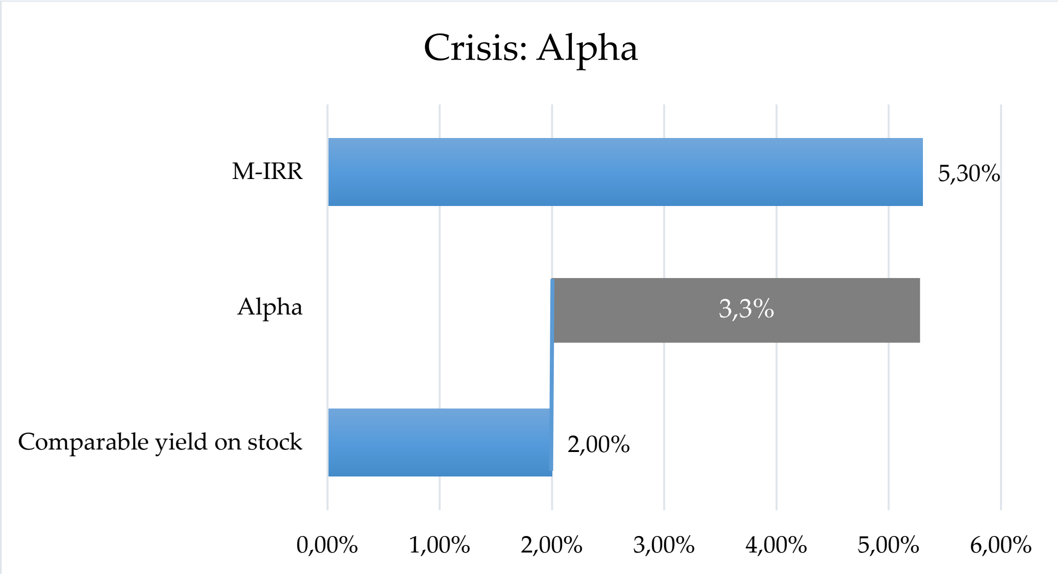
Source: Own representation based on Golding Capital Partners, 2014, pp. 1-5.

Figure 28: Alpha above the Capital Market Cycle



Source: Own representation based on Golding Capital Partners, 2014, pp. 1-5.

Figure 29: Alpha of Transactions Active during the Crisis



Source: Own representation based on Golding Capital Partners.

Thus, the study (Gottschalg & Golding Capital Partners, 2014, pp. 1-5) proves that Private Equity holds an overall positive Alpha over the entire cycle and the counter-cyclical development and stability of this Alpha is given in a year of crisis as in 2008 (Gottschalg & Golding Capital Partners, 2014, pp. 1-5). Consequentially, it can be derived that the success of Private Equity transaction – see also Saenger & Schewe (Saenger & Schewe, 2012, p. 302) - is repeatable (Gottschalg & Golding Capital Partners, 2014, pp. 1-5). These characteristics are highly relevant for institutional investors for inclusion in their portfolio (Gottschalg & Golding Capital Partners, 2014, pp. 1-5). So far, Private Equity investors have mostly made their investment decisions based on past performance (Maurenbrecher, 2008, p. 224; Gottschalg & Golding Capital Partners, 2014, pp. 1-5). This study provides strong evidence that a persistence in the performance of Private Equity funds actually exists (Gottschalg & Golding Capital Partners, 2014, pp. 1-5). Hence, a connection between the existing track records – thus, the previous results of investments (Müller F., 2010, p. 127) – and the expectations in future funds can be established (Gottschalg & Golding Capital Partner, 2014, pp. 1-5).

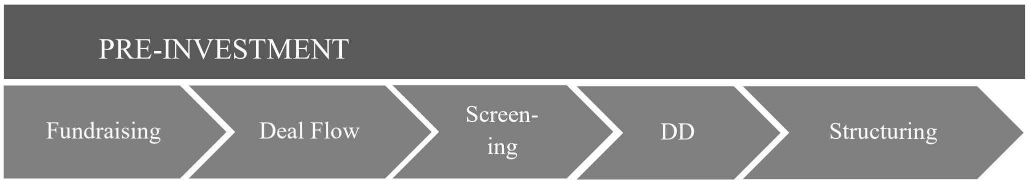
2.1.3 **Phases Prior to a Private Equity Investment**

2.1.3.1 Preliminary Remarks

After consideration and in-depth explanation of the participants in a Private Equity transaction in Chapter 1.1.2., (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 83; Sauermann, 2010, p. 4), the steps of such a transaction are highlighted below. Different views of the discussion about how to approach such a venture will not prevent the process in itself from looking basically the same.

While Becker et al (Becker, Schulte-Krumpen, & Graneß, 2011, p. 34) are regarding five phases as sufficient, Brettel et al (Brettel, Kauffmann, Kühn, & Sobczak, 2008, p. 18) divides it into into six. Weber and Hohaus (Weber & Hohaus, 2010, p. 62) summarizes it further in providing a division in three steps. An expanded chronological subdivision in two investments phases could look as displayed in figures 30 and 31.

Figure 30: Pre-Investment Phase of a Private Equity Transaction



Source: Own representation based on Staroßom, 2013, p. 171.

Whereas DD refers to Due Diligence, the financing is also essentially subsumed in the structuring.

Figure 31: Post-Investment Phase of a Private Equity Transaction

Source: Own representation based on Bayaz, 2013, p. 74 et seqq.

This model represents a Buyout (Zipser, 2008, p. 11) and displays the approach for a Leverage Buyout (Becker A. , 2009, p. 14). For the different financing needs, this financing model is adjusted accordingly. A consideration of how to proceed with the target company in the future regarding the restructuring, does not belong to this model. The – in connection with the locust debate publicly debated – Buy it, Strip it, Flip it (Essvale, 2010, p. 73) – scenario, whereby the investors blatantly convert the acquired companies (Henry & Thornton, 2006, pp. 1-5) by means of downsizing or the abolition of entire corporate departments, can be part of these restructuring procedures (Geisler, 2012, p. 32). However, more and more voices are being heard preferring a sustainability (Müller F. , 2009, p. 120) in context with the strategy. This strategy is consistently dedicated to growth through acquisitions by either the Private Equity Company (Schütte, 2013, pp. 12-14) or the target company (Herzog, 2014, p. 22; Tasma, 2012, p. 11 et seqq.).

2.1.3.2 Business Valuation

Prior to the detailed consideration of the stages of the process of a Private Equity transaction (Hehn, 2011, p. 50), it should be noted at this point that the Due Diligence (Niederdrenk & Müller, 2012, p. 28) shown in figure 30 could be preceded by another stage, if applicable – the business valuation (Bysikiewicz, 2008, p. 1). The business valuation (Tinz, 2010, p. 17 et seqq.) will disarrange the process actually shown in the above graph, since it can take place at different times, depending on priority, which is why it is preceded by reasons of neutrality and importance. The price expectations of buyer and seller (Wolter, 2011, p. 20) are relevant in determining (Kranebitter, 2007, p. 75) whether there will be a business transaction (Bayaz, 2013, p. 60; Kranebitter, 2007, p. 75; Wolter, 2011, p. 20). Experience has shown, that those expectations usually differ (Bayaz, 2013, p. 60; Kranebitter, 2007, p. 75, Wolter, 2011, p. 20). The amount of the purchase prices is often the reason for differences (Odenell, 2013, p. 1) between the former owner and the buyer (Faller, 2005, p. 35). The absolutely correct and objective business value will hardly ever be given (Hohenlohe, 2006, p. 91; Odenell, 2013, p. 1)). In general, the purchase prices are a result of long, often tough negotiations between seller and buyer (Bysikiewicz, 2008, p. 255; Odenell, 2013, p. 1)). Various methods are available for determining the enterprise value. Essentially known (Lorenz, 2009, p. 17) are the following methods (Voigt, Voigt, Voigt, & Voigt, 2005, pp. 19-21):

- Net Asset Value method
- Capitalized Earnings method
- Multiples method
- Discounted Cash Flow method

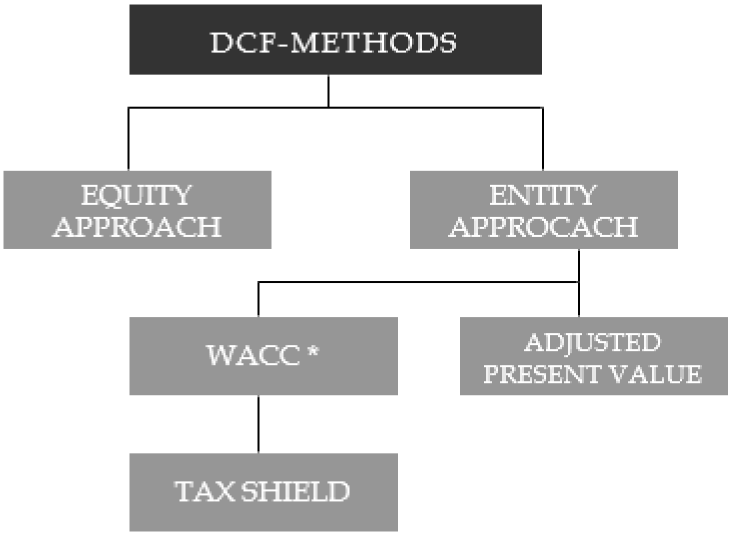
The net asset value method (Hutzschenreuter T. , 2009, p. 369) is again divided into a traditional asset value method (Heinrichs, 2008, p. 56) and the liquidation process (Kreyer, 2009, p. 21). With the former method, the sum of the company's existing assets minus liabilities are determined (Heinrichs, 2008, p. 56; Hutzschenreuter, 2009, p. 369, Odenell, 2013, p. 2)). The company's value is calculated according (Odenell, 2013, p. 2) to what a buyer would have to spend for the reproduction of the existing company (Sygusch, 2008, pp. 44-45). The liquidation process (Odenell, 2013, p. 2) involves the asset stripping (Heinrichs, 2008, p. 3) of a company (Henke, 2009, p. 79). The assets are being valued (Rose, 1990, p. 221) at selling price (Odenell, 2013, p. 2; Rose, 1990, p. 221). All arising costs are being deducted from the sales proceeds (Odenell, 2013, p. 2). This result represents (Brenner & Misu, 2015, p. 300) the absolute minimum value (Brenner & Misu, 2015, p. 300; Odenell, 2013, p. 2). With the capitalized earnings method (Reichmann, 2011, p. 244), the enterprise value is determined based (Schmidt A. , 2010, p. 185) on future surplus revenue (Odenell, 2013, p. 4; Reichmann, 2011, p. 244; Schmidt A., 2010, p. 185). In practice, there are different variants (Sommer, 2012, p. 163) of the multiples method (Odenell, 2013, p. 6; Sommer, 2012, p. 163). One variant (Schacht & Fackler, 2009, pp. 21-

22) is set on the operating income (Schwab, 2008, p. 117) – that is, the profit before tax (Goldammer, 2012, p. 25) – whereas imputed costs, in particular the imputed owner's salary (Peto, 2014, pp. 63-65), need to be taken into account (Goldammer, 2012, p. 25, Odenell, 2013, p. 6; Schacht & Fackler, 2009, pp. 21-22). Another multiplier, however (Odenell, 2013, p. 6), is set on the total revenue (Schacht & Fackler, 2009, pp. 21-22). The most commonly used method (Winter, 2009, p. 62) for determining the enterprise value is the discounted cash flow method (Dierkes & Schäfer, 2015, pp. 19-25). For the calculation (Pfeiffer, 2014, pp. 22-30), cash flows in the future are being discounted to the present day.

$$V_0 = \frac{I_1}{(1+Y)} + \frac{I_2}{(1+Y)^2} + \cdots + \frac{I_n + V_n}{(1+Y)^n}.$$

V_0 is the property value sought; n is the forecast period; I_1, I_2 are the cash flows; I_n is the cash flow for the last year of the projection period; Y is the rate of return on capital; and V_n means the cash flow arising from the resale of the property at the end of the forecast distance (Gribovsky, 2014, S. 61). In order to determine a fair value for the transaction, the balance sheets are being consulted as well, which in the context of business valuation is infrequently (Brückmann & Patzig, 2015, pp. 1-30) observed in literature, yet must not be underestimated. Through performance indicators and balance sheet analysis relatively reliable scenarios can certainly be developed. These figures are also necessary for the deal itself. Thus, a distinction is made between two types of deals. In an asset deal (Diller, 2014, p. 215), the investor buys all of the assets of a company such as machinery, vehicles, licenses but also the liabilities. Usually, however, the sale price exceeds the sum of the individual assets, because goodwill is added, which the buyer is willing to pay beyond the tangible and intangible assets. In a share deal, the company's shares are acquired, which are granting the purchaser certain rights such as the voting right or profit participation rights (Scholz, 2008, p. 93).

Figure 32: Characteristics of DCF Methods



*WACC: Weighted Average Cost of Capital.

Source: Own model based on Dierkes & Schäfer, 2014, pp. 19-25.

For the evaluation, it is essential that the payment claims are in the future and thus uncertain. Due to the unique capital market dominance in terms of future cash requirements – cash flow, the overall assessment process, such as the above exemplified DCF method (figure 32), has prevailed over the individual evaluation procedure (Everling & Jahn, 2009, p. 250).

2.1.3.3 *Fundraising*

Basically, fundraising is the acquisition of means (Schiemenz, 2015, p. 2) - the systematic analysis, planning, implementation and control of all activities - aimed at obtaining all resources necessary for the project (Erwin, 2013, p. 25) as economically as possible, whereas both monetary and contributions in kind as well as the provision of services (Urselmann, 2014, p. 1) can be exploited (Erwin, 2013, p. 25; Schiemenz, 2015, p. 2 et seqq.; Urselmann, 2014, p. 1 et seqq.). The raising of capital from investors is the basis for any investment activity of Private Equity funds. According to Brettel (2008, p. 23 et seqq.) such a collection of money until the closing of the fund generally lasts for more than fourteen months (Bayaz, 2013, p. 58; Brettel, 2008, p. 23 et seqq.). Investors (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2008, p. 77) in this context - see 2.1.3.2 - are mainly banks, pension funds, government institutions, insurance companies, but also, to a lesser degree, very wealthy individuals (Bayaz, 2013, p. 46-47; Thum, Timmreck, & Keul, 2008, p. 16). Especially independent Private Equity firms (Lerch, 2011, p. 7) which operate within the parameters of Buyouts (Farschtschian, 2010, p. 26) and which can rely neither on an industrial corporation nor a bank for safety reasons, are dependent on funds from external investors (Bayaz, 2013, p. 58; Grethe, 2012, p. 68)). To collect the equity (Bayaz, 2013, p. 58), the companies draw on placement agents which are considered experts for capital market communications (Bayaz, 2013, p. 58), to support and assist them (Bagley & Dauchey, 2012, p. 151) in the marketing of fund shares (Bagley & Dauchey, 2012, p. 151; Bayaz, 2013, p. 58). Initially, a paper is being drawn up (Achleitner, Schraml, & Tappeiner, 2011, p. 42), which regulates personal, legal, fiscal and financial aspects (Achleitner, Schraml, & Tappeiner, 2011, p. 42; Bayaz, 2013, p. 58; Grethe, 2010, p. 96). These issues include the formation of an investment team and associated advisory board, a possible administration fee, management fee (Bayaz, 2013, p. 58) and the carried interest (Pinilis, 2013, p. 23), meaning the amount of profit sharing for the fund company at the expense (Lawton, 2008, pp. 846-867) of the investors (Bayaz, 2013, p. 58; Lawton, 2008, pp. 846-867; Pinilis, 2013, p. 23). Especially for investors, it is important to know how successful an investment is (gruenderszene.de, 2015) or might be (Bayaz, 2013, p. 58). This information is also included in the paper. To do so, a so-called track record (Hochberg, Ljungquist, & Lu, 2007, p. 293) is being used representing an individual reference list of executed investments (Bayaz, 2013, ß. 58; Kauffmann et al, 2008, p. 22; Ljungjquist, & Lu, 2007, p. 293). Hence, it involves a record of previous investments by Private Equity companies (Bassi & Grant, 2006, p. 94). This track record reveals not only the successes of existing investments (Leleux, Swaay, & Megally, 2015, p. 220), the experience gained by the investor during these transactions are being listed therein (Bassi & Grant, 2006, p. 94; Leleux, Swaay, & Megally, 2015, p. 220). Depending on the scope of this track record it can be identified whether the investor is new to the market or an industry expert. In relation to fundraising within Private Equity transactions this means that this track record provides information about how previous funds were designed and how they performed (Kommer, 2012, p. 29). With all these features and findings, Private Equity companies will try to attract investors for their funds (Heckmair, 2009, p. 23). Especially industry experience is crucial when collecting equity (Tausend, 2006, p. 155). Further ways for fundraising are offered by specially organized fundraising days or conferences within the industry market (Haibach, 2012, p. 96).

2.1.3.4 Deal-Flow und Screening

After the fundraising, the collected funds will be invested on the basis of the investment strategy in participations in appropriate companies. To ensure a high selectivity, a large number of potential participation projects (Baumgärtner, 2005, p. 144) is being identified (Kauffmann et al, 2008, p. 31). Such a participation occurs rather seldom, just because of this stringent selection (Portisch, 2016, p. 295). A large selection in the context of the deal flow (Weber, Bender, Eitelwein, & Nevries, 2009, p. 51) supports the discovery of a hidden champion (Simon, 1996, pp. 1-8). The portfolio companies (Lohfert, 2003, p. 128) are identified through formal and informal networks, such as banks, accountants, tax and business advisers and other Private Equity funds, sometimes as well by the capital-seeking companies (Vater, 2003, p. 104) themselves (Weber, Bender, Eitelwein, & Nevries, 2009, p. 51). Thus, the portfolio companies are determined by active market analysis in cooperation with third parties and capital-seeking companies, whereas a Private Equity transaction is most commonly initiated through network activity (Metzger, Achleitner, Reiner, & Tchouvakhina, 2010, pp. 28-31). Prior to addressing the potential portfolio company with Due Diligence (Pomp, 2015, p. 2), an investor, respectively the Private Equity Company will conduct a screening for a first overview of the company (Kauffmann et al, 2008, p. 31).

Target of such a deal flow is always to reach a positive agreement between the potential portfolio company and the Private Equity firm (Bayaz, 2013, p. 59). Due to the participation of many third parties within the Private Equity industry, often a deal is being initiated that is potentially not profitable or too complicated (Bayaz, 2013, p. 59). Berens et al (Berens, Brauner, & Nevries, 2005, p. 115) are reducing the probability of a deal to a ratio of one to ten, so that for one company in which is being invested, ten more are believed to be not suitable (Bayaz, 2013, p. 59). Even and especially the most careful review of a potential investment object is the reason for the occurrence of such a disproportion.

2.1.3.5 Due Diligence as Hedging Instrument

Due Diligence (Remy, 2011, p. 23) – meaning a thorough examination – is applied in the context of a business purchase, but also in an extraordinary evaluation, like the evaluation of a target object (Kapoor, 2010, pp. 6-7) in connection with Private Equity. In order to assure the quality of an investment, an investor examines all relevant aspects of this project (gruenderszene.de, 2015). Through systematic analysis (Sinkon & Putney, 2014, pp. 26-29) and assessment of the strengths and weaknesses of the target company (Schramm & Hansmeyer, 2011, p. 154), it is tried to induce an alleged security for this deal (Schramm & Hansmeyer, 2011, p. 154; Sinkon & Putney, 2014, pp. 26-29; gruenderszene.de, 2015). Since primarily expert knowledge is needed in such an audit, preferably lawyers, accountants (Höhne, 2013, p. 17), industry experts or engineers are considered for this task (gruenderszene.de, 2015; Höhne, 2013. p. 17). The content of Due Diligence (Remy, 2011, p. 33 et seqq.) can be classified into diverse processes (gruenderszene.de, 2015; Remy, 2011, p. 33 et seqq.):

Market-related Due Diligence

Especially in a business purchase, the market of an investment is being examined (Velten, 2010, p. 108) in order to assure that there is a sufficiently large group of buyers and foremost, to define the competitors (gruenderszene.de, 2015; Velten, 2010, p. 108).

Corporate Legal Due-Diligence

This review serves to consider the legal (Gleich, Kierans, & Hasselbach, 2010, p. 22) structure (Rosenbloom, 2002, p. 6) of the target company (Scharfman, 2012, p. 209 et seqq.). All contracts, increases in capital stock and other measures on the capital side, as well as the resolutions of the shareholders and, if applicable, the Supervisory Board, are being examined (gruenderszene.de, 2015). Also the position of the shareholders is being analyzed under some circumstances (Gleich, Kierans, & Hasselbach, 2010, p. 22; gruenderszene.de, 2015; Scharfmann, 2012, p. 209 et seqq.; Rosenbloom, 2002, p. 6).

Financial Due Diligence

This analysis investigates the financial situation (Scott C. , 2002, p. 61) of the target company (Pomp, 2015, p. 25 et seqq.; gruenderszene.de, 2015; Rosenbloom, 2002, p. 101 et seqq.). In this, the investor screens all contracts, conclusions, liabilities (Schultz & Cantwell, 2014, pp. 69-84) and receivables including the budget, in order to obtain a tangible view of the profitability and financial situation (Wirtz, 2003, p. 189) of the enterprise (gruenderszene, 2015; Pomp, 2015, p. 25 et seqq.; Rosenbloom, 2002, p. 101 et seqq.; Scott C., 2002, p. 61; Schultz & Cantwell, 2014, pp. 69-84; Wirtz, 2003, p. 189).

Technical Due Diligence

To gain an overview of the technology (Sinewe, 2010, p. 44) and the products of the target company (Balz & Arlinghaus, 2007, p. 103), this assessment is primarily conducted by specialists (Böttcher, 2012, p. 55) and experts (Balz & Arlinghaus, 2007, p. 103; Böttcher, 2012, p. 55; gruenderszene.de, 2015). Here, the creation process is of utter importance since it might offer an approach for improvement (gruenderszene.de, 2015). Also, it is important to remember the expertise that Private Equity firms (Ott, 2010, p. 58) may yield (gruenderszene.de, 2015; Ott, 2010, p. 58).

In addition, and if needed, another IPR (Intellectual Property) Due Diligence (Sammons, 2005, p. 64) and/or environment-based Due Diligence (energy-base.org,

2014) is being conducted (gruenderszene.de, 2015; Sammons, 2005, p. 64). The IPR Due Diligence considers legal matters (gruenderszene.de, 2015) such as patents and copyrights (Spedding, 2004, p. 242) in the meaning of infringements to others (gruenderszene.de, 2015; Spedding, 2004, p. 242). If the investor is committed to ethical (Schnapf, 2000, pp. 80-83, 124-128) or sustainable investments, environmental issues need to be excluded (gruenderszene.de, 2015; Schnapf, 2000, pp. 80-83, 124-128). The Due Diligence report (Howson, 2003, p. 50) in which the individual reviews are being combined, is being accurately and in detail discussed by the management and is the basis for the investment decision (gruenderszene.de, 2015; Heister, 2010, p. 306). Since in this process the responsible parties of the potential target company should be present as well, a review in the sense of a personal Due Diligence (Berkman, 2013, p. 163) may be taken into consideration – namely if the investment should be an investment in the context of Venture Capital (Berkman, 2013, p. 163; gruenderszene.de, 2015). In such a case, the investor is investing into the human capital (Philipp, 2012, p. 22) of the target company due to lack of capital and material assets (gruenderszene.de, 2015; Philipp, 2012, p. 22).

2.1.3.6 *Structuring of a Buyout*

After taking a close look at the results of the Due Diligence, the investor will submit a final purchase price bid (Schütte, 2013, p. 12), provided the Private Equity firm has positively confirmed the results (Brettel, Kauffmann, Kühn, & Sobczak, 2008, p. 67; Schütte, 2013, p. 12).

Figure 33: Structuring Phases of a Buyout

Source: Own representation Herzog, 2014, p. 33 et seqq.

The actual takeover of a company proceeds in two phases, which may well happen parallel to each other (Becker, 2009, p. 42; Brettel, Kauffmann, Kühn, & Sobczak, 2008, p. 67). The two phases are the financial structure and the legal structure as shown in Figure 33.

Financial structure

The central performance figure with the investment in a company (Bitz, Ewert, & Terstege, 2002, p. 121 et seqq.) is the internal rate of return (IRR) of the capital employed (Wöltje, 2013, p.149). The internal rate of return (Glatte, 2014, p. 193), however, is the discount factor (Dernick, et al., 2016, p. 53). When applied, the discounted future payments correspond with the initial investment (Glatte, 2014, p.

193). If this rate of return is greater than the interest plus risk premium, the investment (Glatte, 2014, p. 193) is profitable (Geilhausen, Bränzel, Engelmann, & Schulze, 2015, p. 273).

In order to calculate the profitability of an investment decision, that interest rate r is sought at which the capital value of the project is equal to zero (Aucamp & Eckhardt Jr., 1976, p. 329), in which NPV represents the net present value and C represents the cash flow (Perridon, Steiner, & Rathgeber, 2014, p. 55):

$$NPV = \sum_{n=0}^{N} \frac{C_n}{(1+r)^n} = O.$$

The internal rate of return has its limits. The minimization of the probability of insolvency and maintaining adequate liquidity (Konrad, 2005, p. 159) in a Private Equity transaction takes priority – mainly because of the risks posed by Leverage in Buyouts.

Legal structure

The legal structure is dependent on the particular needs and objectives of the stakeholders (Becker, 2009, p. 50). These, often divergent interests, need to be taken into account (Becker, 2009, p. 50). While the objectives of the seller are primarily focused on the tax neutrality (Brück & Sinewe, 2010, p. 104) and the reduction of liability risks (Schumacher, Sobau, & Hänsler, 2011, p. 45), the buyer, in the first place, will pursue fiscal objectives, such as the deductibility of interest expense (Brück & Sinewe, 2010, p. 304), the conversion of the purchase prices in depreciable amount, which thus may be used for tax purposes, or will mobilize the corporate tax credit resting on already taxed reserves (Brettel, Kauffmann, Kühn, & Sobczak, 2008, p. 81 et seqq.). In doing so, the seller will choose a form of corporate sale that will grant him the lowest possible tax burden on the sale and will prefer the exemption of liability for past activities and quality defects of the company (Brettel, Kauffmann, Kühn, & Sobczak, 2008, p. 81 et seqq.). With forms of corporate sale, the asset deal or share deal is to be understood (Wilplinger, 2007, p. 106). In order to minimize liability risks, Due Diligence is helpful, but cannot eliminate all future liability issues, because as the legal successor, the buyer assumes all responsibilities arising from contractual agreements of the company (Brettel, Kauffmann, Kühn, & Sobczak, 2008, p. 81 et seqq.).

2.1.4 **Phases Following a Private Equity Investment**

2.1.4.1 Preliminary Remarks

The phase after a Private Equity investment is not only the longest, but also the most high-maintenance phase of a participation in a company. During a period of several years, the target company has to be supervised by the Private Equity firm or its affiliated management in the manner that it will grow consonantly with the objectives (Brettel, Kauffmann, Kühn, & Sobczak, 2008, p. 94). A prudent approach is particularly important for everyone involved. Especially, yet not only at an early stage participation – the Venture Capital commitment – it is necessary to protect the target company and the own high-risk capital (Ruppen, 2011). Therefore, the minimization of risks in the phase after the investment belongs to the main tasks of the Private Equity firm (Natter, 2003, p. 155). In contrast to capital providers such as banks, who may terminate their loans (Krepold & Fischbeck, 2011, p. 150) or shareholders of listed companies, who can sell their shares, this is not possible for an investor in a Private Equity commitment (Natter, 2003, pp. 134-141), because the capital is contractually promised for a long period of time (Heckmair, 2009, p. 30). Therefore, the maxim is:

The minimization of risks (Paxmann & Fuchs, 2010, p. 55) and the maximization of profits (Fleischer, 2009, p. 104) is the mission of a good portfolio company. It can only meet this task, if it has adequate impact on the target company (Wollersheim & Barthel, 2011, p. 6) without destroying it.

While investors of other persuasions are able to minimize their risks (Natter, 2003, pp. 134-141) by flexibly drawing capital in order to invest it more profitably or more securely, the Private Equity investor is reliant on carrying out a positive influence

(Hungenberg & Wulf, 2015, p. 123) on the development and business operations of the target company (Hehn, 2011, p. 54).

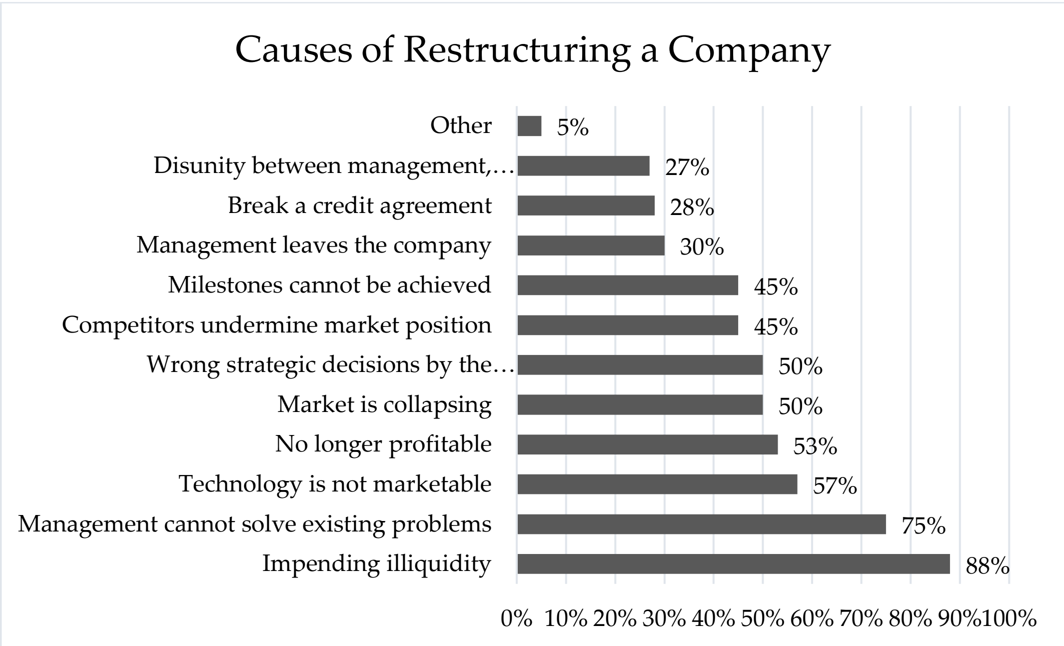
2.1.4.2 *Supervisory Approaches of Holding Companies*

After there had been hardly any categories at the beginning of professional participations, under which the Private Equity companies were divided in intense supervision and non-intense supervision, the Private Equity companies are now distinguishable in type classes. Today, a Venture Capital investment in a target company is no longer compatible with a more passive supervisory (Natter, 2003, p. 134 et seqq.) approach (Sauermann, 2010, p. 24). On the other hand, a medium-sized business owner who only needs monetary means for an investment that he cannot obtain through banks for various reasons, may not accept a co-determination by the investor (Hertz-Eichenrode, 2004, p. 217). This principal-agent problem led to Private Equity companies specializing themselves and possibly publicizing this information (Daniels, 2004, p. 42). This is confirmed by the study of the correlation between type of investment and financing purposes with its significances. An increasing number of potential target companies themselves take that step towards the Private Equity companies, inquiring about funding opportunities and funding arrangements. Nevertheless, skepticism is especially strong among small and medium-sized enterprises to see their future in Private Equity (Köhler P. , 2007, p. B2). Possible scenarios are manifold. Some entrepreneurs fear to lose their influence with the participation of another (Römermann & Praß, 2012, p. 56), while others are scared by the idea of ending up like the Grohe AG. Even if for the investor the investment and not the target company will always be in focus (Füglistaller, et al., 2008, p. 137), aiming at achieving his financial goals, all participants should provide acceptable conditions for both sides in order to be successful. The investor needs to understand that he should not completely dominate a company, which may have endured without him for decades, and the capital seeker should be aware that the investor will only hold a position in "his" company, because due to the know-how of the investor it will be for the best in regards to survival or advancement up to an increase in value.

2.1.4.3 Restructuring Considerations

It is the objective of restructuring (Wright, Cressy, Wilson, & Farag, 2014, pp. 109-129) to substantially increase the company through strategic or operational restructuring measures (Bayaz, 2013, p. 76; Wagner, 2014, p. 21)). Reasons for a restructure where already determined by KPMG in a survey in 2004, asking Private Equity firms how to create values by restructuring target companies (Scott, Andersch, & Jugel, 2004, p. 3). Often, the need for restructuring (Thoms, 2014, p. 1) is not identified early on (Scott, Andersch, & Jugel, 2004, pp. 1-8). Operational criteria such as imminent illiquidity or a lack of profitability take the spotlight (Scott, Andersch, & Jugel, 2004, pp. 1-8). Only in 50% of all cases will strategic questioning like the development of the market or the behavior of competitors trigger the restructuring (Scott, Andersch, & Jugel, 2004, pp. 1-8), shown in figure 34.

Figure 34: Causes of Restructuring a Company



Source: Own representation based on KPMG (Andersch, 2011, p. 13).

The reasons (Scott, Andersch, & Jugel, 2004, pp. 1-8) for a restructuring (Osterhage, 2009, p. 5) need correspond with a multitude of measures (Atiase, Platt, & Tse, 2004) in target companies (Paul & Weber, 2014, p. 77; Bayaz, 2013, p. 77 et seqq.):

- corporate governance structure (Henry D. , 2008, pp. 912-942),
- personnel (Bayaz, 2013, p. 77; Scott, Andersch, & Jugel, 2004, pp. 1-8),
- performance test (Scott, Andersch, & Jugel, 2004, pp. 1-8),
- company management (Scott, Andersch, & Jugel, 2004, pp. 1-8),
- structural and procedural organization (Hammann & Freiling, 2000, p. 88),
- production area (Bayaz, 2013, 77; Scott, Andersch, & Jugel, 2004, pp. 1-8),
- it-structure (Bayaz, 2013, p. 77; Osterhage, 2009, p. 5),
- company acquisitions and sales (Bayaz, 2013, p. 77; Thoms, 2014, p. 1),
- marketing area (Bayaz, 2013, p. 77; Scott, Andersch, & Jugel, 2004, pp. 1-8),
- capital measures,
- procurement,
- corporate culture,
- employee training,
- research and development (Wagner A. , 2014, p. 50; Bayaz, 2013, p. 77).

The implementation of these measures in the post-investment phase is always dependent on the size, orientation and the single problem of the target company (Krystek & Moldenhauer, 2007, p. 179).

2.1.4.4 Exit from Private Equity Financing

Preliminary Remarks

Private Equity transactions (Braun, Schmeiser, & Siegel, 2014, p. 115) have a specific investment horizon (Schramm, 2011, p. 216). This exit form of a Private Equity financing is referred to as exit (Jelic, 2011, p. 946) restrictive or divestment (Wagner W. , 2010, pp. 591-592). These processes are being traditionally summarized under the term Exit (Hess, 2007, p. 33). Only in the last phase of the investment process is the actual success of an equity interest in a portfolio company[8] finally for certain (Prym, 2011, p. 44), unless the Private Equity company has agreed on a profit-sharing, which is a participation in the profits of current and future operations. The different ways to withdraw from an investment are referred to as exit (figure 35) channels (Kußmaul, 2008, p. 516) and include the listing of the target company - IPO = Initial Public Offering - (Pagano, Panetta, & Zingales, 1998, p. 27) as well as the sale of the stake to other investors (Kollmann, 2011, p. 487) or the repurchase of the participation by the former owner (Kollmann, 2011, p. 490). Needless to say, a failure of the investment is also feasible and may lead to a total depreciation of the capital contributed (Bines & Thel, 2004, p. 483).

Figure 35: Private Equity Exit Variations

Source: Own representation based on Daniels, 2004, p. 44 et seqq.

[8] In this paper, the term target company is depending on the approach called portfolio company.

Initial Public Offering

The IPO is comparatively often named as the preferred exit variant (Bösl, 2004, p. 11) from a Private Equity investment (Bösl, 2004, p. 11; Hess, 2007, pp. 40-41). Empirical studies (Bygrave & Timmons, 1992, p. 167 et seqq.) have shown in the past that higher profits can be achieved with IPO than with other exit variations (Daniels, 2004, p. 46; Fueglistaller, et al., 2012, p. 396). The returns from sale are in comparison with exit options, not always higher than the returns from the sale on the stock market (Daniels, 2004, p. 46). This rather subjective position is in consideration of the fact that those target companies going public are particularly well-positioned companies (Daniels, 2004, p. 46). Besides the benefit of a supposedly higher sales price, the IPO has to offer additional advantages (Daniels, 2004, pp. 46-47):

- Congruity of interests (Daniels, 2004, pp. 46-47): If a company is being sold on the stock market, all parties involved wish to obtain a high rating and are also equally interested in the conclusion of the exit. Variables such as loss of position, power and influence do not play a role during and after the process (Gerig, 2003, p. 20).
- Capital market (Daniels, 2004, pp. 46-47): Once the company is listed on the stock market, it secures on a long-term basis the possibility of raising capital by increasing capital stock (Dworak, 2010, pp. 280-281). Listed companies are subject to strict disclosure requirements and are bound to the stock quotations as a subjective assessment approach, which can facilitate access to debt financing.
- Awareness level (Daniels, 2004, pp. 46.47): Through publications and the presence in the media, a publicly traded company has become better known immediately after the IPO (Wirtz & Salzer, 2001, p. 223), which has a positive effect on the contact with customers, suppliers or potential employees.
- Growth (Daniels, 2004, pp. 46-47): Since neither the former owners nor the Private Equity firms may sell their shares instantly in an IPO (Salzer, 2004, p. 84), they can participate in further growth (Daniels, 2004, p. 47).

The disadvantages of an IPO (Daniels, 2004, pp. 46-47) lie mainly in the high disclosure requirements and the high costs (Singh & Bhowal, 2010). The so-called lockup period – that is a ban on sale for Private Equity firms and the target company – holds the overall risk of the uncertainty of the stock market (Daniels, 2004, p. 47). In addition, the stock market access remains difficult even if there has been a facilitation of access for young and small enterprises (Freese, 2006, p. 17).

Trade Sale

A Trade Sale (Kollmann, 2004, p. 370) means the sale of shares in a target company to a strategically interested investor (Brechbühl & Wooder, 2004, p. 142), in most cases coming from an industrial background (Brechbühl & Wooder, 2004, p. 142; Daniels, 2004, p. 48; Kollmann, 2004, p. 370). Competitors, suppliers, customers (Hannich, 2012, p. 38) or other large enterprises (Breuer, 2001, p. 528) are possibilities (Breuer, 2001, p. 528; Daniels, 2004, p. 48; Hannich, 2012, p. 38). The objectives of these potential buyers are the realization of synergies, obtaining strategic advantages, the accelerated establishment in new markets or the acquisition of know-how that would possible not be available otherwise (Cumming & MacIntosh, 2012). Benefits of a trade sale are (Daniels, 2004, p. 49):

- Short transaction time
- Low transaction costs
- High company rating
- Complete exit as opposed to the IPO (Schalkowski, 2013, p. 43)

The biggest disadvantage (Daniels, 2004, p. 49) of a Trade Sale is the lack of congruency between the management of the target company and the Private Equity firm. Because a loss of influence is being apprehended, this exit variation is particularly at risk of falling through (Hannich, 2012, p. 40).

Buy Back

The repurchase of shares by the entrepreneur or company provides an alternative, but less popular or less used exit channel and is generally only used, if other exit options fail (Schlitt, 2014, p. 204). This circumstance is in consequence of competition and the strong position of the buyer, which is reflected in a lower purchase price (Herzog, 2014, p. 50).

Secondary Purchase

The Secondary Purchase (Philipp, 2012, p. 28) is the counter-model to a Trade Sale. Instead of a strategic investor, another financial investor takes over the target company for sale (Fraser-Sampson, 2010, p. 189). While previously and recently a Private Equity firm tried to support and raise the price of the target company, it is now succeeded by another financial investor, possibly another Private Equity firm, seeking to retrieve even more from the enterprise (Pott & Pott, 2012, p. 360). At this point, an investor will find a company which, as the case may be, is so far in debt through debt financing (Philipp, 2012, p. 28) that he will appear as a chief restructuring officer (CRO) and implement the above contemplated restructuring measures (Bauer & Düsterloh, 2013, p. 58).

Total loss

With this exit option surface, the risk and the liability issues for the portfolio company, which is simultaneously equity investor and shareholder and is liable with the equity capital (Gregoriou, Kooli, & Kraeussl, 2007, p. 385). A target company is considered a total loss, if no positive return is scored and the equity provided is partially or fully lost (Kiesel, Scherer, & Zagst, 2010, p. 25).

2.2 ECONOMIC AREA: EUROPEAN UNION

2.2.1 Preliminary Remarks

The European Union (Reichstein, 2012, p. 11) is an economic and political union of currently 28 European countries (Noack, 2014, p. 65)[9]. Initially, there were six states that established the so-called European Community (Eberstadt & Kuznetsov, 2008, p. 82). Already in the 1950s (Faber A. , 2005, p. 42), along with Belgium, France, Luxembourg and Germany, Italy and the Netherlands took this step (Eberstadt & Kuznetsov, 2008, p. 82; Faber A., 2005, p. 42). The reason and meaning behind this endeavor was to prevent political and military conflicts among each other by building strong economic ties (Schmidt & Schünemann, 2013, pp. 330-331; Bartl, 2015, p. 8). In addition, the economic growth was to be accelerated with the emergence of a larger market (Streit, 1988, p. 36; Reinhardt, 2015, p. 711). More and more states joined in until finally with the Treaty of Maastricht in 1992 the European Union was founded (Fröhlich, 2008, p. 12; Wessels, 2008, p. 89). Since that time, the European institutions were continuously democratized (Meyer & Eisenberg, 2009, p. 60). The European Union now also holds its own legal personality (Zerres & Zerres, 2015, p. 26) and holds the right of speech as well as the right of inspection with the United Nations (Lange, 2012, p. 4; Sinn, Wang, Wu, & Zöller, 2015, p. 16) and was awarded the 2012 Nobel Peace Prize (Greschkow, 2014, p. 7; Zerres & Zerres, 2015, p. 26). Taking the gross domestic product in consideration – which will be discussed in more detail in a later chapter of this paper - the European Single Market is currently the largest single market in the world (Stratenschulte, 2014, p. 2; Fröhlich, 2014, p. 11). The increasing democratization of the Institutions of the European Union naturally leads to more regulations, that must be employed and – in the case of the framework for Private Equity funds - need to be improved.

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9 There was a referendum in Britain. The majority of citizens has decided to leave the European Union. It will take a while until the United Kingdom is no longer a member of the European Union. It may take up to two years. Until then, all rights and obligations must be complied with (Harms, 2016, p. 1).

2.2.2 Areas of Activity and Members of the European Union

The current Member States of the European Union are Austria, Belgium, Bulgaria, Croatia, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Poland, Portugal, Romania, Slovakia, Slovenia, Spain, Sweden and United Kingdom.

With their almost innumerable institutions (Radicova, 2013, pp. 55-62) and organizations, the European Union acts by now in virtually every area which the national states also need to cover (Kuhn, 2010, p. 33). To enumerate all of them would go beyond the scope of this paper. However, those fields are to be mentioned, which are directly or indirectly influencing the subject of Private Equity, respectively investments and the labor market. Thus, e.g. The European Investment Fund 2012 launched a so-calle Fund for Business Angels (volume, 2012). The European Court of Justice has found a disadvantage for foreign corporations in Germany by the Treasury (Handelsblatt, 2012). The European Investment Bank is involved in almost 50 private equity funds with almost € 5 billion. The European Commission may need to approve private equity acquisitions and the European Central Bank intends to tighten up its supervision of the financing of private equity deals (Bamberg, 2017).

- the European Investment Fund (Ferruz, Ortiz, & Vicente, 2007, pp. 238-248),
- the European Court of Justice (Wilmott, 1984, pp. 211-218),
- the European Investment Bank (Robinson, 2009, pp. 651-673) ,
- the European Commission (Kostadinova, 2013, pp. 264-280),
- and especially (Hustedt, Wonka, Blauberger, Töller, & Reiter, 2014, p. 53),
- the European Central Bank (Kaltenthaler, Anderson, & Miller, 2010), based in Frankfurt (Europäische-Union, 2014).

The European Investment Bank (Hellmann, 2009, p. 442; Storck, 2001, p. 364) plays for example a crucial role in the interaction between economic recovery and growth in Europe (Berens R. E., 2014, p. 351; Hägele, 2003, p. 90). The European Commission's offer to build a new "European Fund for Strategic Investments (EFSI)" in cooperation with the European Investment Bank in order to boost growth and create jobs in Europe (EU-Kommission, 2014), is being discussed at present. To what extent this project will support those with the desire to set up a new business in Europe and whether it will bring forth manageable regulations, remains to be seen.

2.2.3 Macroeconomic Situation of the European Union

2.2.3.1 European Performance Strength

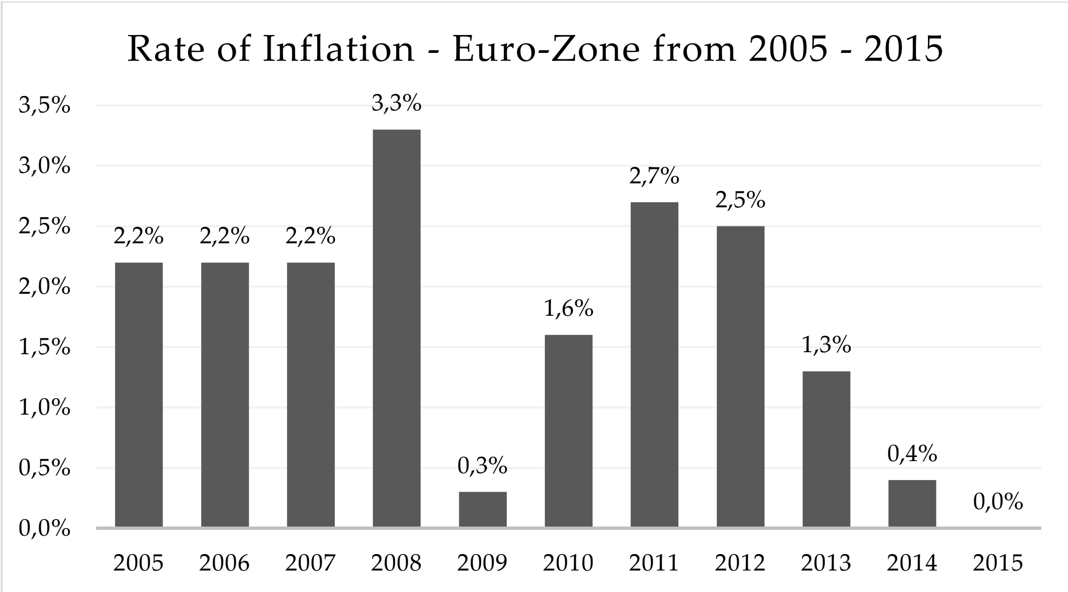
Olli Rehn, Member of European Parliament since 2014 (European-Parliament, 2014) and until recently a member and Vice-President of the European Commission (Kleinert, 2014, p. 56) is a Finnish politician of the Centre Party[10]. The political scientist and economist drew attention to himself with his dossier „Economic and Monetary Union and the Euro" (European-Commission, 2014), when he remarked:

> *„A well-functioning economic and monetary union and a strong and stable Euro are the basis for growth and employment in Europe". (Rehn, 2014, p. 2)*

The performance of the European Union is based on this simple formula. The Economic and Monetary Union is responsible for price stability (Schuppan & Tamm, 2014; Roy, 2002, p. 36; Dittrich, 2016, p. 60). The independent European Central Bank (ECB) is responsible for the monetary policy in the Euro-Zone (Thiemeyer, 2010, p. 177; Zierer, 2015, p. 210).

[10] The Finnish Centre Party is a rural-liberal party of the political center in Finland. She is a member of the Alliance of Liberals and Democrats for Europe (ALDE), the European Association of liberal parties (Luif, 2007, pp. 52-53, 96).

Figure 36: Rate of Inflation – Euro-Zone from 2005 to 2015



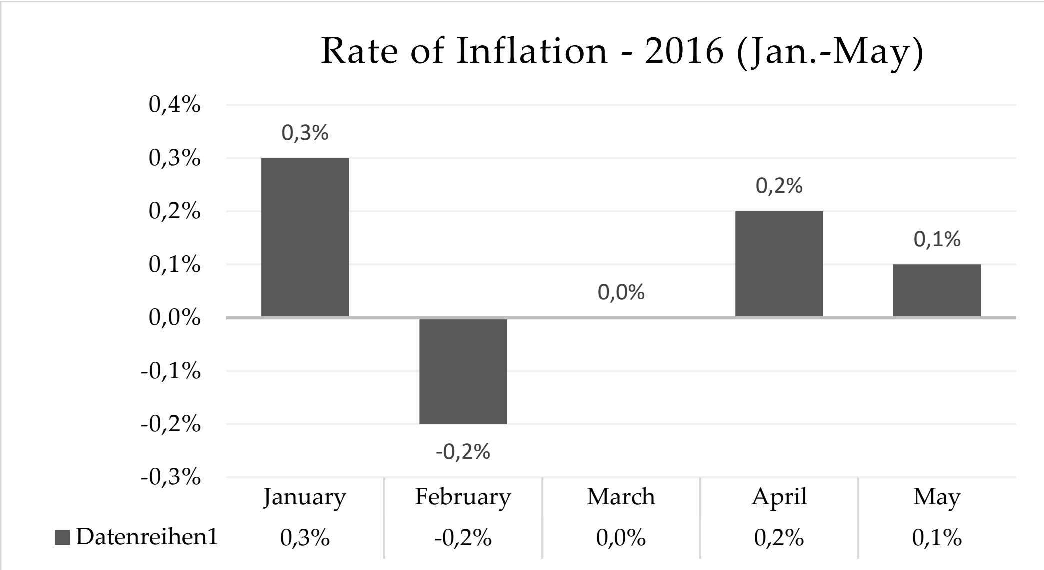
Source: Own representation based on Eurostat.

It can be implied that the major task and, at the same time, the main task of the ECB is to ensure the stability of consumer (Schmidt & Wollenschläger, 2016, p. 199) prices and to protect the Euro against loss of value (European-Commission, 2014, Schmidt & Wollenschläger, 2016, p. 199). Figure 36 shows the inflation rate of the Euro-Zone.

The ECB must and wants to ensure that the inflation rate permanently ranges around 2% (Mayer & Schiebler, 2008, p. 52; Holtmann, 2004, p. 223; Mayer T. , 2015, pp. 1-3). This assumption will be examined at this point, at which it should be first noted that in many European countries, two important inflation rates are determined (Wildmann, 2016, p. 53; Neubäumer & Hewel, 2005, p. 523). On one hand the consumer price index (CPI), and in opposition, the harmonized index (Lübke & Vogt, 2014, p. 57; Auer & Rottmann, 2015, p. 133) of consumer prices (HICP). While the CPI is rather determined by each country itself, the HICP is a performance figure to enable a comparison of the European inflation rates (Wildmann, 2016, p. 53; Neubäumer & Hewel, 2005, p. 523; Lübke & Vogt, 2014, p. 57; Auer &

Rottmann, 2015, p. 133). This experiment investigates the HICP (EUROSTAT, 2016), which relate the data from 2015 to the last entry.

Figure 37: Rate of Inflation – Euro-Zone 2016 Month



Source: Own representation based on Eurostat.

If the data from the years 2005 to 2015 are to serve as a basis for the determination of a mean value, that value of 18,7%/10 = 1,87% annual inflation rate comes very close to the self-declared goal to permanently pursue an inflation rate of 2%. If, however, the tendency of the figures from the recent past (EUROSTAT, 2016, pp. 1-4) is brought in, this figure is not as optimistic as the values in figure 37 and the mean value thereof demonstrate.

The mean value of the months January – May 2016 is 0.4%/5 = 0.08%, which is well below the targeted 2%-mark, which – according to the ECB – is the value where prices are stable as under the mark of the last months in 2016. Due to the corresponding low interest rates, the low inflation rate should stimulate. Nevertheless, the readiness to assume risk with regard to Private Equity remains subdued.

The Euro benefits Citizens

The fact that the Euro has a practical benefit to citizenry becomes evident when crossing former borders. The costs and expenses for the exchange (Weidel, 2011) of currencies (Hansen, 2010, p. 530) cease to apply (Hallepape, 2001, p. 19). The abolition of borders incidentally simplifies shopping and also important competitive price comparisons (European Commission, 2003). The Euro is providing Europe with more weight in world trade (Zierer, 2015, p. 210). Due to its strength, the assertiveness of Europe is significantly increased worldwide. As the economic and financial crisis (Kempf, Lüderssen, & Volk, 2010, p. 291) – among economists it is being discussed who the cause of the crisis (Schwarzbach, Rudschuck, & Schulenburg, 2012, p. 69) had been and whether it had not been and is both – has made clear, the European Union as a strong partner is quite capable of withstanding global shocks and to act as a corrective (Europäische-Kommission, 2015, pp. 1-20).

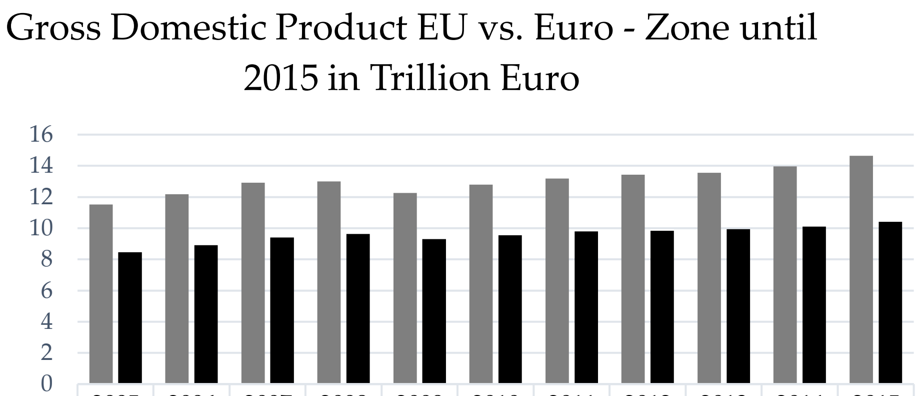
The Euro is good for Business as well

The Euro brings forth considerable benefits (Europäische-Kommission, 2015, pp. 1-20) for European companies (Mayer, 2013, p. 223). The Economic and Monetary Union and thereby especially the ECB provide the businesses (OECD, 2014, p. 74) with favorable (Lang, 2014, p. 218) interest rates (Heller, 2014, p. 27). This in turn favors (Europäische-Kommission, 2015, pp. 1-20) the creation of jobs (Götz, 2016, p. 45). Also, rivalries in monetary policies cease since its introduction, at least for the affected areas (Europäische-Kommission, 2015, pp. 1-20). The elimination of transaction costs (Weeber, 2015, p. 80; Brunner & Kehrle, 2014, p. 742) in the currency exchange is also felt on the employer's side, so that more money has become vacant for investments (Europäische-Kommission, 2015, pp. 1-20). The relative price stability in some areas also allows companies to engage in long-term planning (Janßen, 2012, p. 22), which has a positive effect on competitiveness, since focusing on the core business is no longer disturbed by minor issues, such as price adjustments and currency problems (Europäische-Kommission, 2015, pp. 1-20). Overall, the global competition for companies has been disburdened by the strong Euro (Europäische-Kommission, 2015, pp. 1-20).

2.2.3.2 Trend of the European Union and the Labor Market

As per communication of the European Commission (Europäische Kommission, 2015), which published the final Annual Growth Survey 2016 on 26.11.2015, a slow recovery is emerging. According to this report, the crisis has peaked and the incipient recovery is still moderate and fragile (European-Commission, 2014). In particular, the issues, necessarily important for this paper, still seem uncertain. The confidence in the resilience of the banking sector (Langley, 2014, p. 94) continues to be unabatedly deficient (Pätzold, 2010, p. 106). The fragmentation of financial systems and credit markets, the restructuring and adaptation of the financial sector (European-Commission, 2014) and high unemployment (Dörre, Jürgens, & Matuschek, 2014, p. 130) will continue to constrain growth (Sarfati, 2013, pp. 145-156; OECD, 2014, p. 116). The European Semester, which was launched in 2010 is the cornerstone for the coordination and monitoring of economic and budgetary policies of the Member States (Borchardt, 2012, p. 375; Lhotta, Ketelhut, & Schöne, 2013, p. 205). Public finances have made significant progress in consolidating (Krämer, 2013, p. 205) and Member States have, for example, introduced Youth Guarantees (Brenke, 2013, p. 16), which are intended to ensure that all young people under the age of 25 are offered a job position, advanced education, an apprenticeship or a traineeship of good quality within the first four months after completing their education or training or after the loss of a job (European-Commission, 2014). The situation of employment, however, will only gradually improve due to the time interval of the reforms regarding the economic recovery (European-commission, 2014). The statistics in figure 38 shows the overall situation in figures (eurostat, 2016). It shows the gross domestic product (GDP) of the European Union and the Euro Zone from 2005 to 2015 in trillion Euros. The GDP is the total value of all goods and services produced in that year within the national boundaries (Wildmann, 2010, p. 31 et seqq.). They must serve the final consumption. It is considered an important indicator of the economic power of a country (Wildmann, p. 31 et seqq.). In 2015, the GDP of the European Union was approximately 14.64 trillion Euros, while the Euro Zone came to about 10.4 trillion Euros (Eurostat, 2016).

Figure 38: Gross Domestic Product EU vs. Euro-Zone until 2015 in tn. Euro



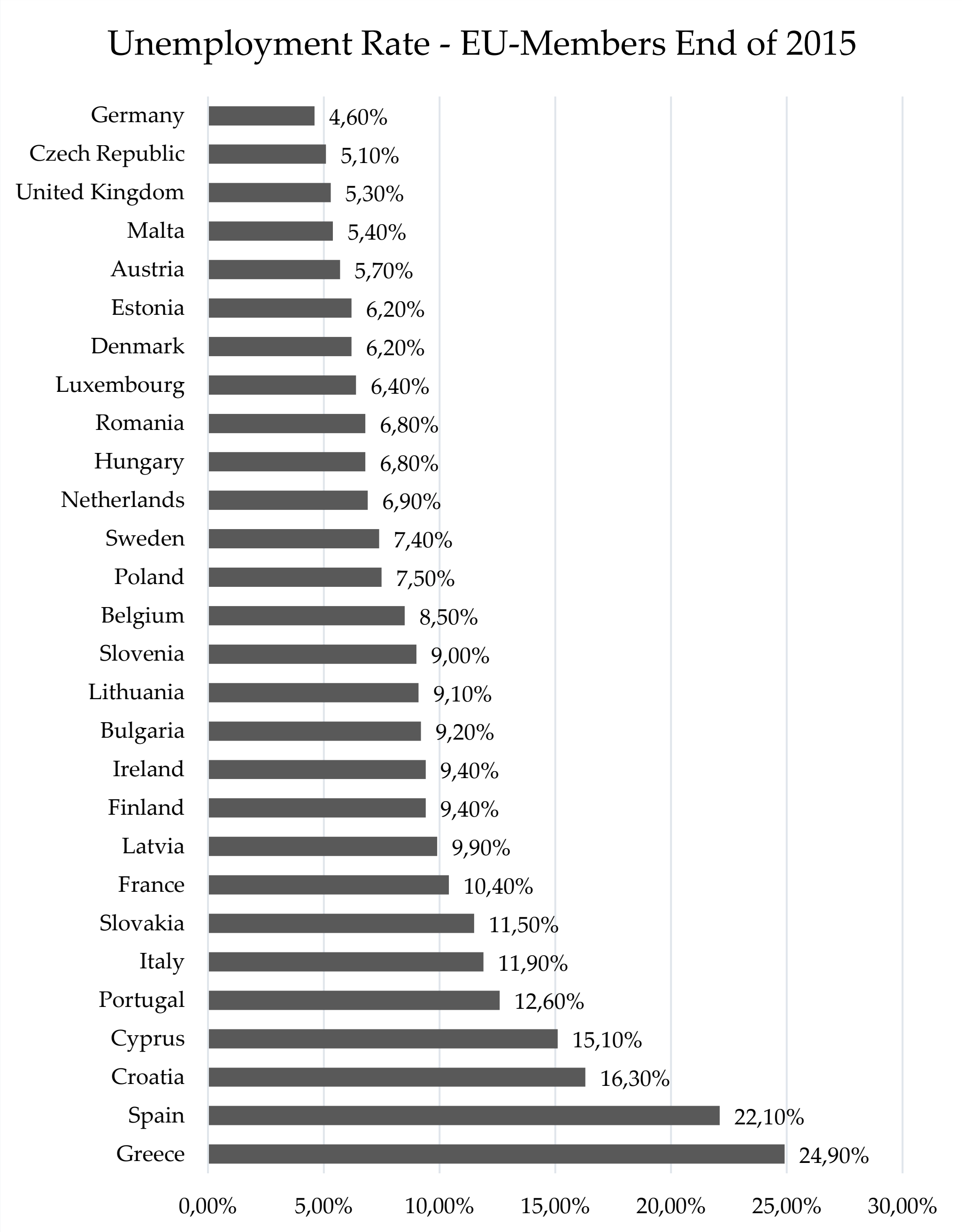
	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
EU	11,52	12,18	12,91	12,99	12,25	12,79	13,18	13,43	13,55	13,96	14,64
Euro-Zone	8,46	8,9	9,4	9,63	9,29	9,54	9,8	9,83	9,93	10,11	10,41

EU Euro-Zone

Source: Own representation based on Eurostat.

Right at the beginning of this paper it was noted that some areas are still awaiting adaption. Prices on the electricity market were mentioned as an example. The situation on the labor market is particularly striking. Fatal differences explain the discontent discussed in the introduction and supported by statistical data. Figure 39 shows the significant differences in employment (eurostat, 2016). No other figure can reveal the employment situation of a country or region as clearly as the unemployment statistics. This data is also important because it is not only the access to more venture capital (via the detour for private equity companies or funds) that is to be guaranteed by changing, improved, and optimized tax rates, but also higher investments and thus a higher gross domestic product (and vice versa). This will have a positive effect on the unemployment rate.

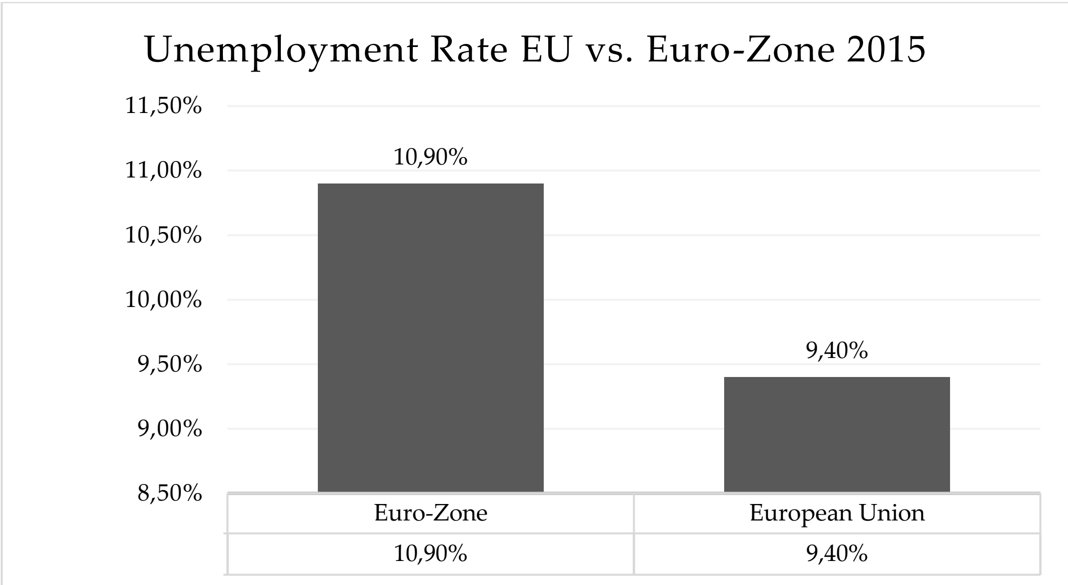
Figure 39: Unemployment Rate – EU-Members at the End of 2015



Source: Own representation based on Eurostat.

The extremely high unemployment rates in countries such as Greece and Spain even cause a very high unemployment rate in the European Union (figure 40), especially in the Euro-Zone, as is substantiated by the following chart.

Figure 40: Unemployment Rate – EU vs. Euro-Zone 2015



Source: Own representation based on Eurostat.

2.3 ECONOMIC CLASSIFICATION OF PRIVATE EQUITY WITHIN THE EUROPEAN UNION AND ECONOMIC GROWTH

2.3.1 **Preliminary Remarks**

For centuries economists have discussed the most diverse economic theories. Economists know many approaches to theories, wherein the, until recently preferred, neoclassic (Solo, 1975, pp. 627-644; Simpson, 1949, pp. 861-882) and the Keynesian theory (Keller, 1983, pp. 1087-1095; Fellner, 1957, pp. 67-95) are probably the best-known (Paesler, 2015, p. 29; Nissen, 1999, p. 295). Paul A. Samuelson described economics as follows (Plattner, 1989, p. 6):

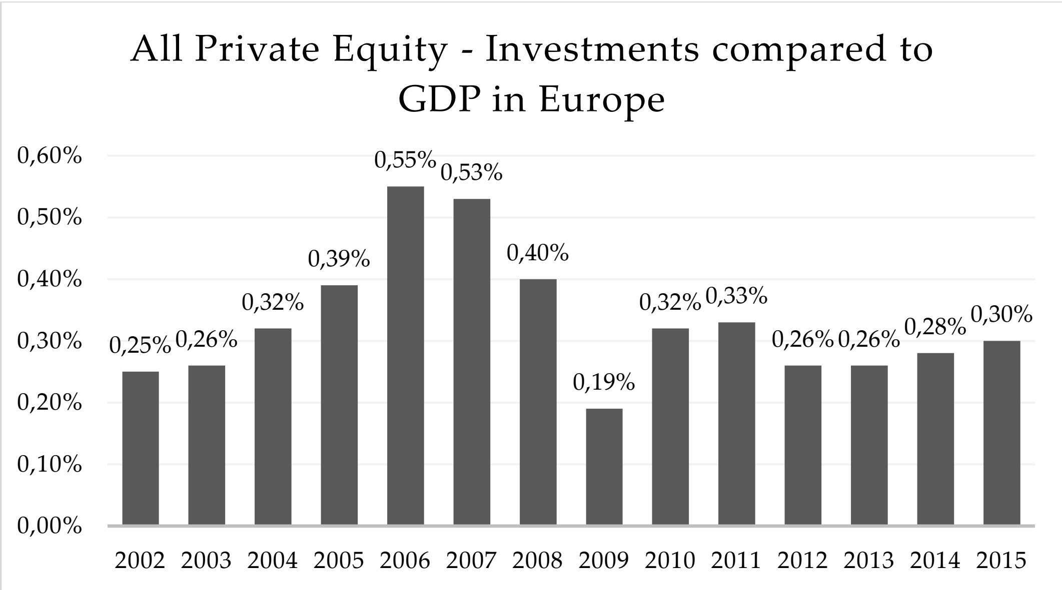
> *„Economics is the study of how men and society end up choosing with or without the use of money, to employ scarce productive resources which could have alternative uses, to produce various commodities and distribute them for consumption, now or in the future, among various people and groups in society."* (Samuelson, 2011)

A large number of people are trying to follow this general principle. However, with success? Judging by the problems the European Union is currently experiencing, it is somewhat doubtful that all possible efforts with respect to this maxim have been made. He, who wants to produce, needs money; he, who is in need of money, needs an investor. If this investor does not come from the banking sector, then what is left? Private Equity definitely is an alternative (Koziol, Proelss, & Schweizer, 2011, pp. 465-484) financing option (Englmaier, 2013, p. 1). Even the figures per se speak from themselves. That Private Equity even qualifies as an asset class has already been discussed in this paper, because Private Equity seems to perform better (Hedtstück, 2013) as an investment than comparable equity investments (Busack & Kaiser, 2006, p. 160). The economic and financial crisis has left its mark; it cannot suffice as reason for the reluctance of shareholders, investors and other participants (Acharya, Philippon, Richardson, & Roubini, 2009, pp. 89-137). What other model can provide such positive first impressions as Private Equity? First, Private Equity is an instrument used to aide companies in a particular situation where other financing options fail to be available. The reasons for this still not well-functioning financial system are well known and have been already discussed in this study. The regulation of investment funds itself, the regulations in the banking sector in general, are not without fault in this misery. Nevertheless, the Private Equity industry managed – although with greatest efforts – to revive a highly efficient market beyond the locusts' debate. Private Equity plays a significant role in Europe's economy (Wirtz, 2006, p. 159).

2.3.2 Economic Impact of Private Equity

Private Equity financed enterprises grow faster in comparison to other companies, create more jobs and are more export-oriented, therefore providing a strong economic momentum (Frommann & Dahmann, 2014). In the European context, the investment in Private Equity and thus primarily in Venture Capital (Sixt, 2014, p. 53) equals an investment in the future (Heimlich, 2013). Private Equity financed companies are often characterized by a high degree of innovation and offer new ideas in order to develop sustainable products and goods. Not only the innovation activities of Private Equity-backed companies are outstanding, they are not to be underestimated as creators of jobs (Schäfer, 2004). Studies of Buyouts showed that target companies could report an annual increase in employees of 4.5% while a control group of non-Private Equity financed enterprises merely achieved 2.2% in growth (Cressy, Munari, & Malipiero, 2011, pp. 1-22). A more critical point of view was offered by the evaluators of a study by the World Economic Forum, which came to the conclusion that employment specifically decreases during the first three years and can only compare itself with the other group in the following years (Davis, Haltiwanger, Jarmin, Lerner, & Mirander, 2014, pp. 41-61). Moreover, growing Private Equity-financed companies are involved in all other processes of an economy. Especially young high-technology companies need more than manpower. Adequate suppliers are necessary as well (Passarge, 2010, p. 21). So, with a growing Private Equity industry with all its participants, the Private Equity firms, the consultants, target companies, suppliers, customers, funds of funds, banks and not least the state participating from tax revenues, there can be hardly any figures which are rating this industry in a just way. However, if numbers are being involved (Investeurope, 2016, p. 41), the importance of Private Equity (Kaplan & Schoar, 2005, 1791-1823) becomes clear (Boué, et al., 2012, p. 61). For this purpose, first, all Private Equity investments in comparison to the total GDP (around 14.7 Trillion Euros in Europe shall be displayed in % (figure 41), followed by the investment of European countries, also compared to their own gross domestic products (GDP) in % (figures 42 and 43). In the analysis, generally two perspectives are being distinguished: Industry statistics (figure 42) and market statistics (figure 43). The industry statistics covers activities (investments, divestments) according to the place of business of the Private Equity Company – investments by country of management – and the market statistics according to the place of business of the financed enterprise – investment by country of portfolio management.

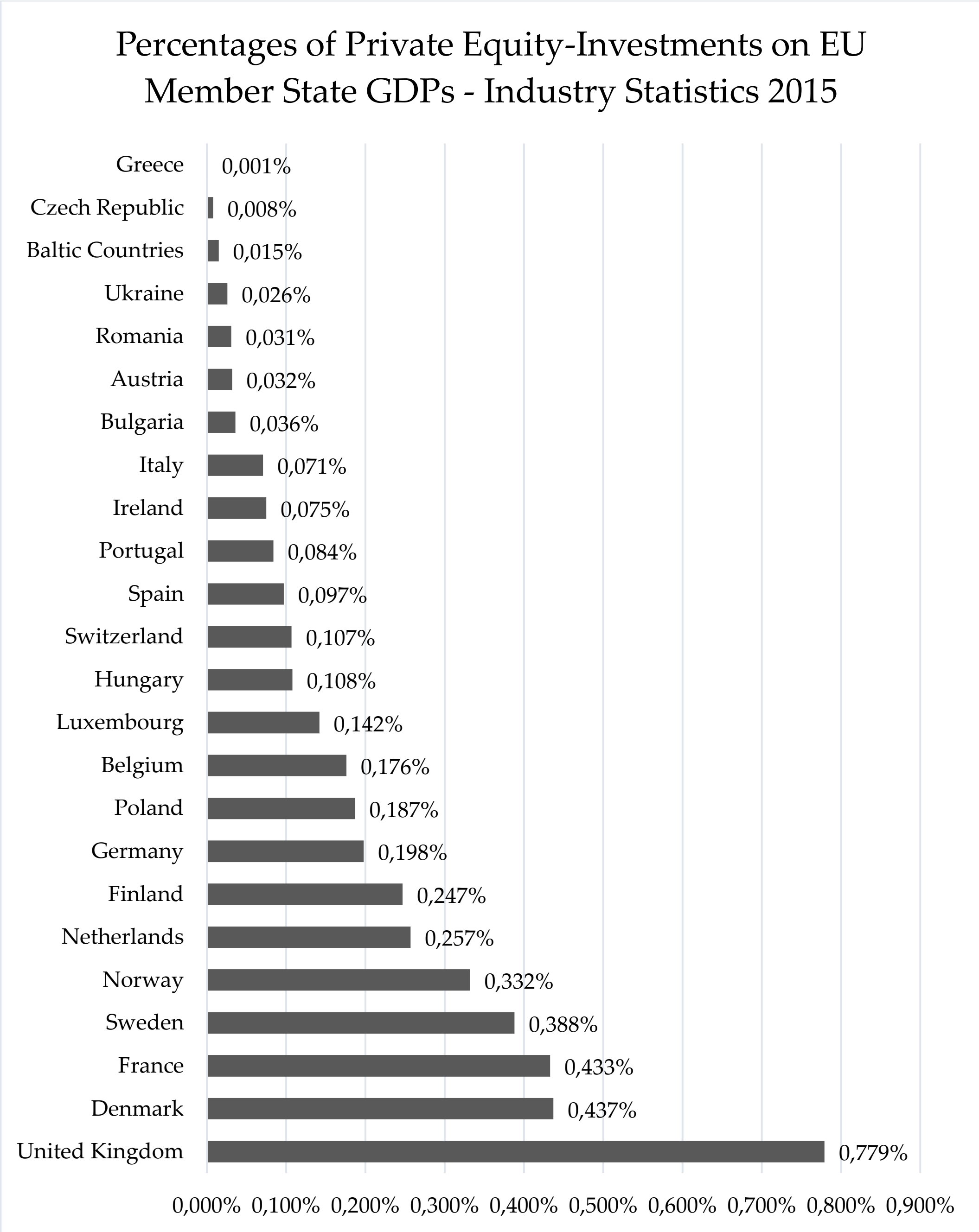
Figure 41: All Private Equity-Investments compared to GDP in Europe



Source: Own representation based on Invest Europe.

Apparently, companies were more willing to take a higher investment risk in the years 2006 and 2007 than it seems to be, following the financial crisis. Currently the industry is stagnating with a slightly positive trend. From 2002 through 2015, a mean value of 0.3314% of the GDP were investments in equity investments. This value is still higher than the current readiness in participations, despite the major slump in 2009, which indicates a stagnation at a low level.

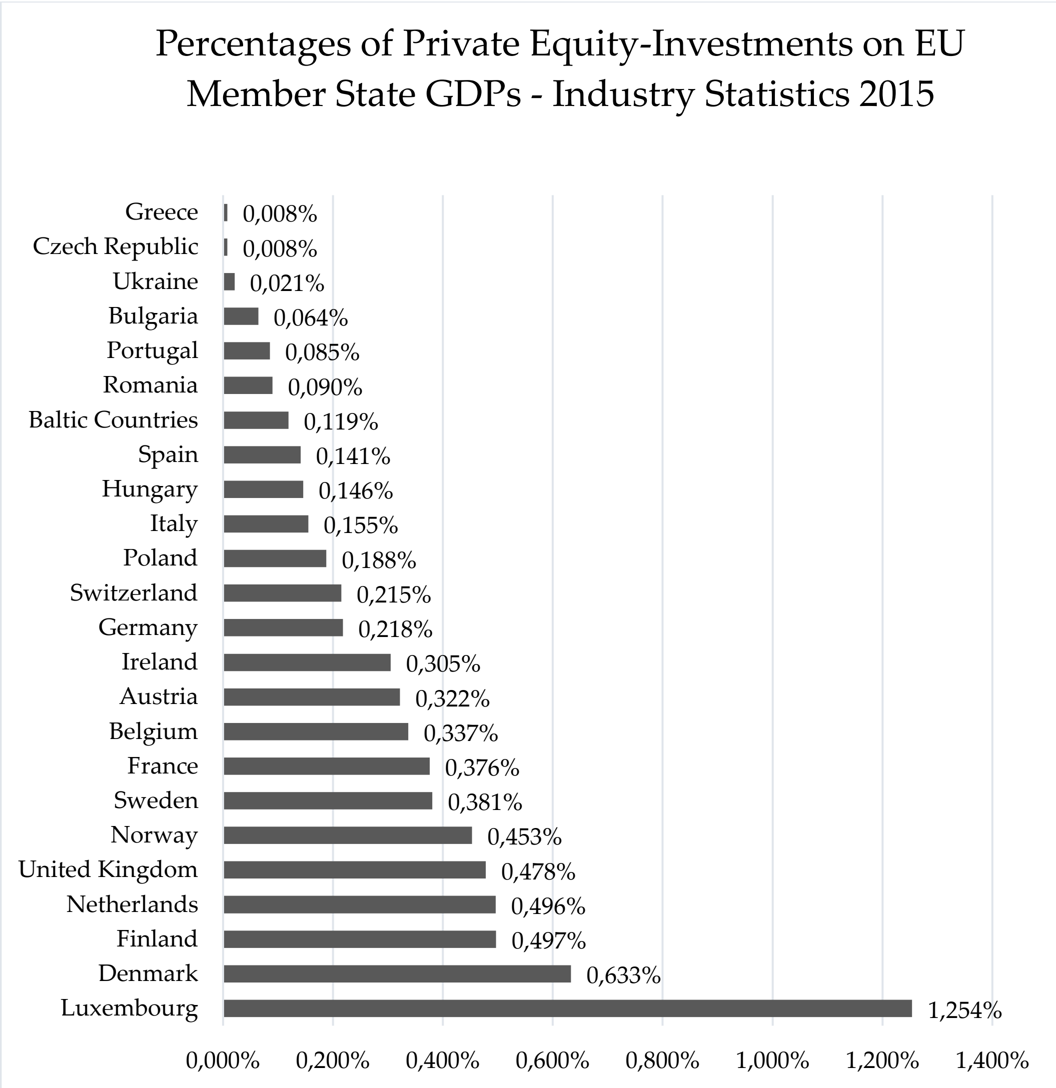
Figure 42: All Private Equity-Investments - Industry Statistics 2015



Source: Own representation based on Invest Europe.

Looking at the entire European area, this means (Investeurope, 2016, p. 42) that the United Kingdom carry forward to hold the top position in regards to willingness to enjoy drops in risk-bearing investments while Greece brings up the rear.

Figure 43: All Private Equity-Investments Market Statistics 2015



Source: Own representation based on Invest Europe.

So when it comes to companies financed, Luxembourg takes a comfortable lead, even ahead of the traditional market of Private Equity in the United Kingdom. The Danish Market seems to be especially attractive for investments. In contrast, economies like Germany and Italy, which have always been very strong (Investeurope, 2016, p. 46), perform rather poorly, which is in part certainly due to the regulatory and fiscal framework.

2.3.3 **Growth Theories**

2.3.3.1 Preliminary Remarks

At the beginning of the dissertation, it was pointed out that the growth theories play a role because the derivation of the formula is hardly conceivable for the GDP, which is important for this study without the addition of these theories and national accounts. The formula BIP = C + I + G + Ex - Im is both based on the overall economic demand Y = C + I + G + Ex - Im and in the same form for the net domestic product. Depending on the literature, they are used synonymously. At the end of the work, the GDP is calculated once again with the new tax findings. Since the GDP is considered a clear indicator of the growth of a society or a market, it is therefore essential to consider this. It should also be pointed out, at this juncture, that this investigation is aimed at the fact that the higher the gross domestic product, the higher the willingness is to invest. Of course, there is also a causal link in the reverse sequence. The higher the investments, the higher the gross domestic product. This is made clear by a calculation at the end of the dissertation, hence the title "... on the impact on market growth ....“.

2.3.3.2 Growth Theory According to Keynes

In his seminal body of work, “The General Theory of Employment, Interest and Money“, John Maynard Keynes (Keynes, 1936, p. 3) presents his theories on monetary, trade economic aspects and the labor market (Davidson, 2009, pp. 73-81). Therein, he explains reasons for unemployment and poverty (Levitt, 1954, p. 235). He advocates – and this is the primary goal of his theory – an expansionary economic policy of all countries, which stimulates an accelerated economy due to increasing demand (Keynes, 2008, p. 5).

Keynes is considered to be the founder of modern macroeconomics (Clement, Terlau, & Kiy, 2013, p. 8; Kruber, 2002, p. 63; Wiemann, 2011, p. 97). As opposed to neoclassical economics, Keynes considers that the subfields of the trade market, monetary market and labor market do not automatically lead to an equilibrium, because prices of goods and downward rigid wages are not flexible enough (Irwin, 2014, pp. 199-227; Peto, 2008, p. 45; Göckler, Rübner, Kohn, Jäger, & Franck, 2013, p. 64). The adjustment of wages to changes in the prices of goods occurs relatively slowly, thus decelerating the recovery of the economy (Wienert, 2008, p. 151). The market alone, in this context, generates no balance (Willke, 2002, pp. 1-8). Thus, an equilibrium on the trade market and the monetary market leads to an imbalance on the labor market (Siebe & Wenke, 2014, p. 146). The wage rate is not the decisive variable for the demand of labor, but rather the demand for consumer and capital goods. A decrease in nominal wages cannot create additional jobs (Peto, 2008, p. 45). Only if the demand for goods increases, new fields of activity, respectively jobs will emerge (Schnarrer, 1996, p. 209). Keynes is convinced (Vogt W. , 2016, pp. 1-44) that the reduction of the aggregate demand for goods is the main reason of a recession. Consequently, the level of production and employment depends on the aggregate demand (Keynes, 2009, p. XIV).

In contrast to the theory of Keynes, "Say's Law" states that supply creates its own demand (Cate, 2013, p. 621). The two elements of this theorem are:

- Production itself creates its own needs (Ehrlicher, Esenwein-Rothe, Jürgensen, & Rose, 1975, p. 184),
- by self-regulation of the market economy, not all sectors of the economy will generate an overproduction at the same time. An imbalance of supply and demand only occurs in specific sectors and this only on a temporary basis (Oppitz & Weigele, 2014, p. 54).

The state's role is to monitor the demand of goods and must, where appropriate and by way of example, reduce taxes, if the market cannot regulate the demand itself (Peto, 2008, p. 45). This measure could compensate for past deficits. For this reason Keynes favors the government playing a larger role in case of a market failure, if the economy is subject to a demand shock, in order to quickly restore full employment (Putnoki & Hilgers, 2013, p. 134). An economic recovery cannot always be achieved by increasing the money supply because economic entities retain the money – the so-called liquidity trap – while awaiting higher returns (Peto, 2008, p. 45). Therefore, the side of the demand for goods can be designated as the main focus of the Keynesian Theory (Peto, 2008, p. 45). In summary, the Keynes Theory demands

that the government has to apply an effective fiscal policy to increase investments in order to stimulate the demand on the labor market and thus to achieve full employment. Eliminating unemployment positively counters the economic crisis.

Looking at the current situation from the viewpoint of this theory, the current European economic situation could be soothed by creating jobs (Pollert, Kirchner, & Morato Polzin, 2013, p. 123). At the beginning of this paper it has already been pointed out, that entrepreneurs contribute a fundamental part (Balke, 2014, p. 8) to improving the job situation (Sahadev & Demirbag, 2011) through start-ups or further developments and could contribute significantly more, if the conditions for such companies, for example in regards to financing through Private Equity, would present themselves more favorable.

Model

An essential component of the Keynesian theory of income and employment is the aggregate consumption function (Kurihara, 2013, p. 161; Cezanne, 2005, p. 101; Below, Ebinger, Lorenz, & Pramann, 1977, p. 91).

The aggregate consumption C depends on the available income $Y^D := Y - T$ (taxes), whereas the average propensity to consume C/Y decreases with increasing income (Welfens, 2008, p. 274; Brunner & Kehrle, 2014, p. 27; Rogall, 2006, p. 70). The simplest form is (Welfens, 2008, pp. 274-275, Cezanne, 2005, p. 101):

$$C = \bar{C} + c(Y - \bar{T}), \qquad 0 < c < 1.$$

In this context, c is the marginal propensity (Brunner & Kehrle, 2014, pp. 26-27) to consume (Brunner & Kehrle, 2014, pp. 26-27; Cezanne, 2005, p. 101).

To get an understanding of a general nature of these formulas, it should be mentioned here, that a variable is called exogenous (Blanchard & Illing, 2009, p. 92), if it is not explained in the model (Erlei, 2010, p. 72), is thus determined from outside, and are marked with a bar. In contrast, a variable is endogenously called when it is explained in the model (Ernste, 2011, p. 194).

Suppose the prices and hence the price level is fixed and the investments and government spending are exogenous, the actual income Y adapts to the aggregate demand Y^N, because the production capacity is not fully utilized, denoting unemployment. Subsequently, this results in the condition of equilibrium (Wohltmann, 2005, p. 38; Kromphardt, Clever, & Klippert, 1979, p. 153; Bofinger, 2011, p. 504)

$$Y^N = Y.$$

The aggregated national demand in a closed economy is $Y^N = C + I + G$ (Wohltmann, 2005, p. 47, Brunner & Kehrle, 2014, p. 24)).

Using the linear consumption function and with exogeneity of I and G, this results in (Welfens, 2008, p. 274 et seqq.)

$$Y^N = \bar{C} + c(Y - T) + \bar{I} + \bar{G},$$

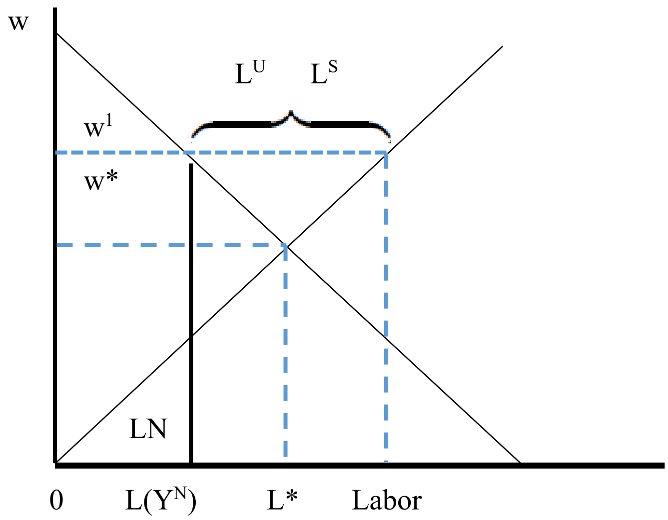
with the condition of equilibrium $Y^N = Y$ follows in equilibrium

$$Y = \frac{1}{1 - \mathrm{c}}(\bar{\mathrm{C}} - \mathrm{c}\bar{\mathrm{T}} + \bar{\mathrm{I}} + \bar{\mathrm{G}}).$$

Keynesian Labor Market Theory

Since the prices are not sufficiently flexible, it can lead to a lack of demand on the goods market for various reasons. Due to the correlation between goods market and labor market according to Keynes, the demand curve for labor experiences a kink, which is determined by the level of aggregate demand Y^N (Willke, 2012, pp. 81-94).

Figure 44: Labor Market Model according to Keynes



Source: Own representation based on Willke, 2012, pp. 83-88.

In figure 44 the demand for labor L (Y^N) becomes independent of the real wage rate. Even at a real wage rate w*, the demand for labor will therefore not suffice to ensure full employment. Unemployment is being identified in the respective area with L^U.

Solution:

The aggregate demand (Dümmler, Hotz-Hart, & Schmuki, 2006, p. 635) is strengthened (Friedmann, 1968) by fiscal policy; (Goerdeler, 1987, p. 157). A reduction of the real wage rate would further reduce the aggregate demand. This demand-oriented economic policy to that effect is not helpful.

The problem of economic policy is the question for the correct theory. An exact analysis is always required, since unemployment does have the same cause for all affected persons. A distinction has to be made between (Beck, 2008, pp. 319-320):

1. cyclical unemployment (Kölzer, 2014, p. 103; Beck, 2008, pp. 319-320),
2. structural unemployment (Beck B. , 2008, p. 320; Werding, 2006, p. 2),
3. and frictional unemployment (Späte, 2002, p. 41; Beck, 2008, pp. 319-320).

Whereas the cyclical unemployment (Mellenthin, 2006, p. 52 et seqq.) under 1. is to be understood as the lack of aggregate demand. A possible solution would be a reasonable Keynesian policy associated with a transition to flexible labor markets in combination with social support (Kölzer, 2014, p. 103, Mellenthin, 2006, p. 52 et seqq.).

With structural unemployment under 2. the qualifications do not correspond with the job specifications (Brandes & Weise, 1980, p. 81 et seqq.). Another issue is the lack of spatial mobility. One approach to solving that problem would be better education, better organization of training and promoting mobility (Brandes & Weise, 1980, p. 81 et seqq.; Beck, 2008, p. 320).

The frictional unemployment is the least problematic, since this applies to job seekers who are not acting imperatively (Beck, 2008, pp. 319-320, Späte, 2002, p. 41).

2.3.3.3 Deliberations on National Economics in the Sense of Neoclassic

Preliminary remarks

The neoclassical economic theory (Joas, 2007, p. 467; Vilks, 1991, p. 2 et seqq.; Huth T. , Berlin, p. 13 et seqq.) deals with the idea of economism of the early twentieth century (Zhan, 2014, pp. 51-80). With the „Chamberlain Revolution" (Brakmann & Heijdra, 2004, p. 135 et seqq.), the „Keynesian Revolution" (Laidler, 1999, p. 3 et seqq.) and the „Rational Expectations Revolution" (Mishkin, 1995, pp. 1-25; Cord, 2013, p. 4 et seqq.), modern economics (Gagliardi & Gindis, 2011, pp. 336-342) has undergone three major intellectual upheavals (Fazzari, 1985, pp. 66-80). They formed the theoretical framework, including both microeconomics and macroeconomics (Pindyck & Rubinfeld, 2009, p. 22). This framework is known as the neoclassical economics (Riese, 1979, p. 88 et seqq.; Hampicke, 1992, p. 21 et seqq.; Muther, 2010, p. 20 et seqq.). It strikingly differs from the classical economics known to this date (Stadermann & Steiger, 2006, p. 237). The neoclassical economics reflects the research and development of modern Western mainstream economics (Macharzina & Wolf, 2008, p. 54; Gläser, 2014, p. 9) over the past hundred years.

The common idea shared with classical economics is that of a free market economy and to combat the excessive governmental interference of Keynesianism (Buchholz, 2010). The central argument of the neoclassical theory can be summarized as follows (Simons-Kaufmann, 2003, p. 44 et seqq.):

Economic underdevelopment results from an incorrect price policy and excessive state interference in the governments of the Third World causes a misallocation of resources. Therefore, the respective roles of government and market must be re-evaluated with the economic development and market forces are to be used to solve development problems.

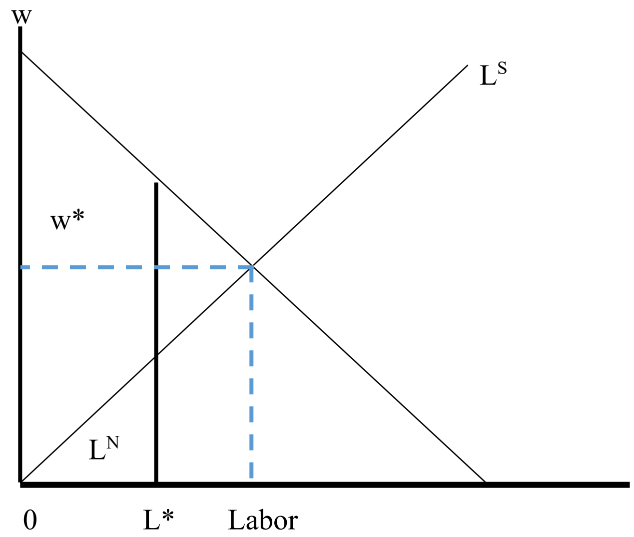
The neoclassical economics emphasizes the role of the market in terms of economic development, and only the market can control a balanced economic development (Fuchs, 2002, pp. 178-179; Beitzinger, 2004, p. 123 et seqq.). The price is regarded as the core factor of economic development in neoclassical economics (Bontrup, 2004, p. 367; Henning, 2005, p. 133; Lippold, 2015, p. 5 et seqq.). Therefore, price distortions in developing countries restrict a positive economic development the most. The most primary cause of price distortions is a false government policy (Shukla, 2010, pp. 71-74). Related to the European issues, this means a rethinking of the countries regarding their fiscal policies and – as discussed at the beginning based on the electricity rates – a quick reduction of price differences within the European Union.

Neoclassical Theory of the Labor Market

The neoclassic Labor Market Theory shall be become apparent with the help of figure 45. The labor supply L^S of employee's increases with the real wage rate w, the labor demand of the employers L^N decreases with the real wage rate (Bofinger &

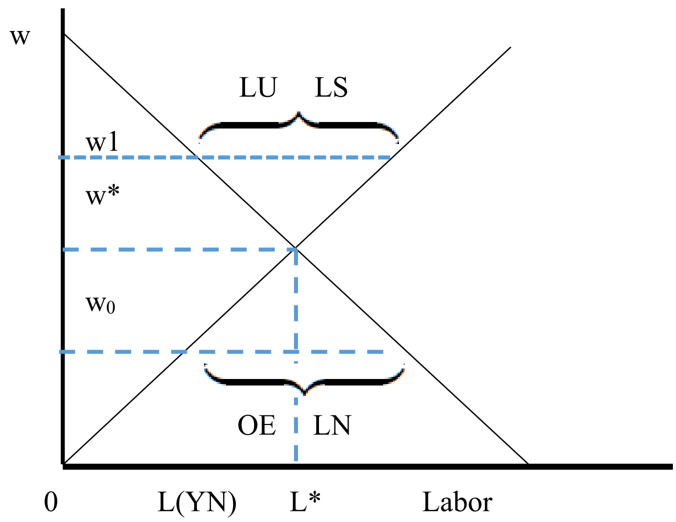
Meyer, 2011, p. 92; Mankiw, 1993, p. 383; Nissen, 1999, p. 240). If the labor market is left to itself, the result will be a balanced real wage rate w* with full employment L* (Biesecker & Kesting, 2003, pp. 355-360; Heine & Herr, 2013, p. 599; Ehreiser & Nick, 1978, p. 28 et seqq.).

Figure 45: Labor Market Model Neoclassic Part 1



Source: Own representation based on Biesecker & Kesting, 2003, pp. 355-360.

Figure 46: Labor Market Model Neoclassic Part 2



Source: Own representation based on Biesecker & Kesting, 2003, pp. 355-360.

At a lower real wage rate w^0 labor shortages (over-employment = OE see in figure 46) prevails, at a higher real wage rate, unemployment (L^U) prevails (Richert, 2007, p. 33). The cause for this condition are exemplary the high labor costs (Baumann M. , 2009, p. 140), but also the overly high wage demands (Fries, 2014, p. 34) by the unions (Lübke & Grossekettler, 1999). Due to the transition to flexible labor markets and the reduction of the real wage rate and wage labor costs, these supply-side economics could provide a solution.

2.3.3.4 Growth Considerations During the Crisis

These simplified models are based on the considerations of the different approaches in economics, which issue in part significantly divergent economic policy recommendations.

While the neoclassical economics propagates (Uchatius, 2005, pp. 1-2),

the deficit of today is the burden of tomorrow,

the Keynesian School teaches (Uchatius, 2005, pp. 1-2),

the debts of today are tomorrow's growth!

Comprehensive economic thought has been given to the current problems of the European Union. Up until the crisis, basically most scientists and other experts were predominantly neoclassical focused (Nienhaus, 2009, p. 80; Rürup, Hengsbach, Weingart, & Leif, 2010, p. 49 et seqq.). Since both the demand-side and the supply-side models always stood in discussion among each other, the return to Keynes (Tichy, 2012, p. 89) is certainly not to be understood as a complete paradigm shift (Piper, 2010). Nevertheless, the almost forgotten Keynes is receiving more attention again. Based on the above model, renowned representatives explain Keynes' comeback (Economist, 2009) as follows:

- The crisis has not been triggered by the misconduct of the central banks, the supervisory institutions or the rating agencies. The deregulation and subsequent failure of the markets is rather due to the dominance of neoclassical and neo-liberal assumptions (Wellas, 2012, p. 339).
- The financial market is not the cause of the problem, but the general undesirable development of the global economy. Here, the financial crisis is merely a symptom of social and global inequality (Behrmann, 2011).
- The market failure is responsible for the crisis, not the state like neoclassics maintains. Here, the deregulation of the economy is the cause (Schrüfer, 2010, p. 56).
- The world economic system must be fundamentally changed in order to get the problems under control. It is necessary to stronger regulate the financial sector (Mayert, 2011, p. 1).

In part, these considerations are several years old. However, these approaches are more present than ever. The very fact, that the regulation of the financial sector (Sender, 2012, pp. 98-117) was not least initiated by the AIFM Directive 2011/61/EU (Späth, 2013, p. 42) and has since been implemented for the most part, which will be discussed in this study as well (starting chapter 3), indicates that there has been a rethinking back to Keynes (Krugmann P. , 2009, p. 211; Plickert, 2008, pp. 1-2; Straubhaar, 2008, p. 1). It was tried to counteract the crisis with numerous stimulus packages (Steinbach, 2012, pp. 352-360) throughout Europe (Welfens, 2011, p. 16). Meanwhile, the politico-economic policy makers have accepted the recommendations of the economists which in majority have converted to the demand-oriented economic policy (Erber, 2013, p. 1).

2.3.4 **System of National Accounting**

2.3.4.1 Preliminary Remarks

The goal of National Accounting – NA – (Brümmerhoff & Grömling, 2011, p. 6; Schultz W. , 1990, p. 20; Perret & Welfens, 2016, p. 92 et seqq.) is the definition (Jones, 2000, pp. 167-178) and statistical measurement of macroeconomic income parameters such as the value calculation or flow figures. Generally, only goods and commodities produced in the respective period are being recorded, irrespective of their intended use (Thiele & Güntert, 2014, p. 54 et seqq.; Lachmann, 1990, p. 121; Richter J. , 2002, p. 99). The European System of Accounts (ESA) forms the reference base for the NA (Henkes, 2008, p. 543). With its introduction, the European Union expected and expects a harmonization (eurostat, 2016) of the European National Accounting (DESTATIS, 2014). The National Accounting (figure 47) is a value statement (figure 47), which means that the quantities produced are valued at prices (Woll, 2011, p. 283; Koschnick, 1998, p. 484; Schäfer M. J., 1996). Simply put:

Figure 47: Calculations of National Accounting

	Production	Unit price	Production value
CDs / XY-Ltd.	10.000 pieces	10,00 euro	100.000,00 euro
DVDs / XY-Ltd.	10.000 pieces	15,00 euro	150.000,00 euro
Blanks / Z-Ltd.	20.000 pieces	3,90 euro	78.000,00 euro
Pro. value			328.000,00 euro

Source: Own representation based on Schäfer M. J., 1996, p. 48 et seqq.

The value statement is the transition to value added and thus the gross domestic product (GDP). The measuring points for recording the value added are (Koschnick, 1998, p. 484):

- Production approach (production)
- Expenditure approach (consumption)
- Income breakdown (remuneration of production factors)

2.3.4.2 Measurand Gross Domestic Product

The following statement has proven itself as a definition of the GDP, the Gross Domestic Product (Cutler, 2013, pp. 19-24; Cao & Tate, 2016, pp. 1-14):

The GDP is the market value of all goods and services intended for consumers, which are being produced in a country during a given period. It is called nominal GDP if it is calculated at current prices and price-adjusted or real GDP, if it is calculated at previous prices (Wildmann, 2010, pp. 31-34; Hohlstein, Pflugmann-Hohlstein, Sperber, & Sprink, 2009, p. 120 et seqq.).

There are three calculation options for the GDP. For this, also see the preliminary observations of the previous chapter. There, the measuring points for the recording of the value added have been noted. Supplementary thereto (Koschnik, 1998, p. 484):

Production	= Production approach.
Consumption	= Expenditure approach.
Remuneration*	= Income breakdown (Woll, 2014, pp. 282-284).

*Remuneration means the payment of production factors.

Incidentally, all calculation methods lead to the same result as the following little calculation shows (production chain figure 48). As an example of a small economy, the data from figure 47 are intended. It is about the representation of the GDP. The

GDP is the value of all final goods. The GDP is the sum of all values added (Wünsche, 2009, p. 120 et seqq.).

Value added = sales revenue minus advance.

Figure 48: Production Chain

Z-Limited		XY-Limited	
Sales	78.000,00 euro	Sales	250.000,00 euro
Wages	60.000,00 euro	Wages	120.000,00 euro
Profit	18.000,00 euro	Basic materials	78.000,00 euro
		Profit	52.000,00 euro

Source: Own representation bases on Wünsche, 2009, p. 120 et seqq.

Production approach:

Value added Z-Limited = 78.000,00 euro – 0.00 euro = 78.000,00 euro.

Value added XY-Limited = 250.000,00 euro – 78.000,00 euro = 172.000,00 euro.

Sum of value added = GDP = 78.000,00 euro + 172.000,00 euro = 250.000,00 euro.

Flow statement:

The GDP resulting from the sum of uses.

GDP = consumption (C) + investments (I) + government spending on goods and services (G) + exports (Ex) – imports (Im).

In this simple example, there are only consumer spending totaling 250.000,00 euro.

Distribution calculation:

The GDP resulting from the sum of all income (labor income, capital income).

Labor income = wages Z-Ltd. + wages XY-Ltd. = 60.000,00 euro + 120.000,00 euro = 180.000,00 euro.

Capital income = profit Z-Ltd. + profit XY-Ltd. = 18.000,00 euro + 52.000,00 euro = 70.000,00 euro.

The sum of all incomes = 180.000,00 euro + 70.000,00 euro = 250.000,00 euro.

The development of the GDP in the European Union has already been graphically presented in the above chapter 2.2.3.2. In regard to the allocation of domestic products within the European Union it is important that in 2013 the Euro-Zone had a market share of 73.4%. The five biggest economies of the European Union - Germany, France, United Kingdom, Italy and Spain – accumulated 71.0% alone (eurostat, ec.europa.eu, 2014). The GDP of the European Union in 2014 increased by 3.0 percent. The distribution with respect to the Euro Zone (EUROSTAT, 2015) and the five largest economies has almost not changed (72.6% BIP ER-19, 71.4% Germany, France, UK, Italy and Spain). To determine the purchasing power, the GDP/capita (Cebula, 2013, pp. 368-372) is often used (Hanslik, 2012, p. 61). Because the fluctuations in the exchange rates of countries not parties to the Euro-Zone, this calculation, however, is uncertain. More suitable for the calculation of purchasing power is the Power Purchasing Standard (PPS). The PPS is a fictitious figure, independent of the national currency, which is eliminating distortions based on differences in price levels in different countries (OECD, 2007).

2.3.4.3 Measurand Net Domestic Product

The net domestic product (Rübel, 2013, p. 5; Sauerwald, 2014, p. 16; Eichberger, 2011, p. 110) at market prices equals the value sum of private consumption, public consumption, net investments and exported minus imported goods (Woll, 2014, p. 284; Wildmann, 2010, p. 36). It is also calculated by deducting the depreciation from the gross domestic product at market prices (Rübel, 2013, p. 5; Sauerwald, 2014, p. 16; Woll, 2014, p. 284; Wildmann, 2010, p. 36). After subtraction of indirect taxes minus subsidies, the net domestic product at factor prices (Fischbach & Wollenberg, 2007, p. 111 et seqq.) is attained (Rübel, 2013, p. 5; Sauerwald, 2014, p. 16; Woll, 2014, p. 284; Wildmann, 2010, p. 36; Fischbach & Wollenberg, 2007, p. 111 et seqq.). This is the value of all factor income incurred in a period in the domestic production process (Fischbach & Wollenberg, 2007, p. 111 et seqq.; Woll, 2014, p. 284). The factor income is the earned income plus the investment income and equals exactly the sum of factor costs (Fischbach & Wollenberg, 2007, p. 111 et seqq.) of all domestic economic sectors (Hardes & Uhly, 2007). Adding the factor income abroad of national residents and subtracting the domestic factor income of foreign nationals will equal the sum of all factor income accrued by national residents in that respective period, the national income. As a definition of the national domestic product (NDP) could apply (Rübel, 2013, p. 5; Sauerwald, 2014, p. 16; Woll, 2014, p. 284; Wildmann, 2010, p. 36; Fischbach & Wollenberg, 2007, p. 111 et seqq.):

The NDP is the measure for the actual aggregate income of an economy.
The NDP therefore is equivalent to

$$Y = C + I + G + Ex - Im.$$

Where C is consumption, I is the private investment, G stands for government spending, Ex - Im = net export, thus exports minus imports. According to the Keynesian theory, now sufficiently explained, the NDP is determined by demand (Wildmann, 2010, p. 112). The aggregate demand is composed of:

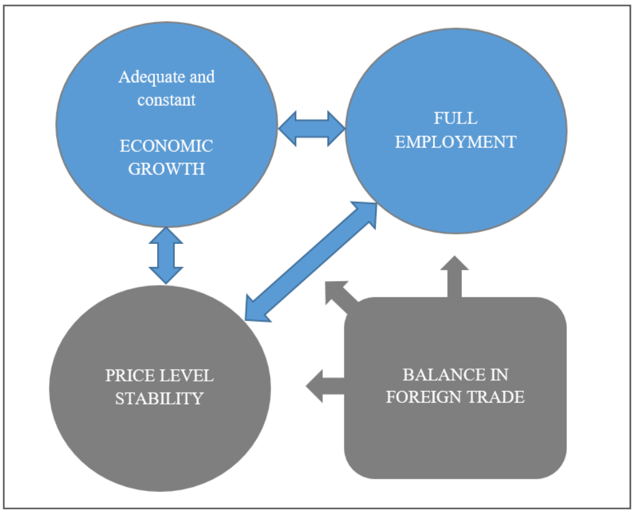
- Consumer demand
- Investment demand
- Government demand
- Foreign demand (Krugmann & Obstfeld, 2009, pp. 270-277)

In contrast, the neoclassic theory states that the NPD determines the level of expenditure (Heine & Herr, 2013, p. 272; Puhani, 2009, p. 88). Apparently, it seems to be no matter what kind of calculation is being applied, whether that might be the calculation of the GDP (gross domestic product) or the PPS (purchasing power standard) or even the NDP (net domestic product) – such a value always depends on the investments as well. Whether by individuals or entire corporations, the increase of these values within the European Union can only be accomplished by providing incentives for investments.

2.3.5 Economic Growth and Full Employment

Goals that are inherent in a market economy are values (Falk, 2016, p. 1) such as prosperity (Erhard, 1957, p. 9), freedom, security and justice (Hißler, 2014, p. 98). Especially for the European Union, with its still very different regional living standards, these values need to be a constant inducement. In this, dealing between Member States and those wishing to obtain membership needs to be optimized. Already, ancient societies have gained wealth by working with their near or distant neighbors, as economists of earlier years have observed. Adam Smith already noted in his work (chapter 3) from 1789 – An Inquiry into the Nature and Causes of Wealth of Nation – that the riches of e.g. ancient Egypt proved that a country could reach an especially high level of wealth, even if foreigners were in large part responsible for its export trades (Kiesewetter, 2006, p. 25). And some time later he notes that the North American and West Indian colonies would not have developed as quickly, if not for the use of foreign capital in order to export excess commodities (Smith, 2005, p. 314). From the above-mentioned values, the Magic Square (figure 49) has emerged. This square symbolizes the four main objectives (Bofinger, 2011, p. 273) of an economy and their relation with each other (Cezanne, 2005, p. 66) For this study, the relation between growth and employment is of significant importance. The fact that price stability is an important indicator, has already been recognized at the beginning. In any case, the balance of foreign trade is usually considered separately.

Figure 49: Magic Square – Economic System



Source: Own representation based on Bofinger, 2011. p. 273.[11]

Economic Growth

The traditionally most important indicator for the growth of an economy is the gross domestic product already discussed above (Wildmann, 2010, pp. 31-34)

- Appropriate economic growth means that not only the benefits but also the potential costs of growth must be taken into account. Here, the eco-political objectives need to be incorporated. Appropriate growth is being pursued to improve the material living standard (Weeber, 2009, p. 24; Föhl & Oppenländer, 1968, p. 22; Sandte, 1998, p. 183).
- Continuous growth (Herrmann F. , 2010, p. 194) is to alleviate the imbalance between aggregate demand and aggregate supply and to effectuate an interference-free dynamic process. Especially the degree of efficiency of the

[11] Cezanne has also inspired for this presentation. In the field of stabilizing it comes to avoid as possible, unpleasant side effects of the productive economy process such as unemployment, inflation, low growth and external imbalances. The policy objectives, that need to be achieved in the area of stabilization, are these four areas in figure 49 (Cezanne, 2005, p. 66).

macroeconomic production potential serves as an indicator (Ventzislavarova & Hensel, 2013, p. 25; Butschek, 2016, p. 29 et seqq.; Kirsch, Bamberger, Berg, & Weber, 1975, p. 129 et seqq.).

Full Employment

A key indicator of the employment situation is the unemployment rate already presented in chapter 2.2.3.2. However, when interpreting the unemployment rate as an indicator of underemployment (Wildmann, 2007, p. 84), there are still some forms of underemployment that need to be taken into account (Kasten, 1959, pp. 81-82; Friedrich H. , 1986, p. 28 et seqq.; Issing, 2011, p. 227). In particular, homemakers (Haustein-Teßmer, 2008, p. 1) and participants in government-funded employability measures remain unconsidered.

Growth and Employment

The link between economic growth and full employment is considered to be a harmonious target relationship (Puhani, 2009, p. 3; Maly, 1991). With the increase of production, the employment situation will improve (Baumohl, 2007, p. 131) – and vice versa (Cezanne, 2005, p. 500). However, economic growth must exceed a minimum value – the employment threshold (Klopmeier, 2014, p. 59; Bitting, 2009, p. 69; Frohn, et al., 2003, p. 161) – in order for employment to increase.

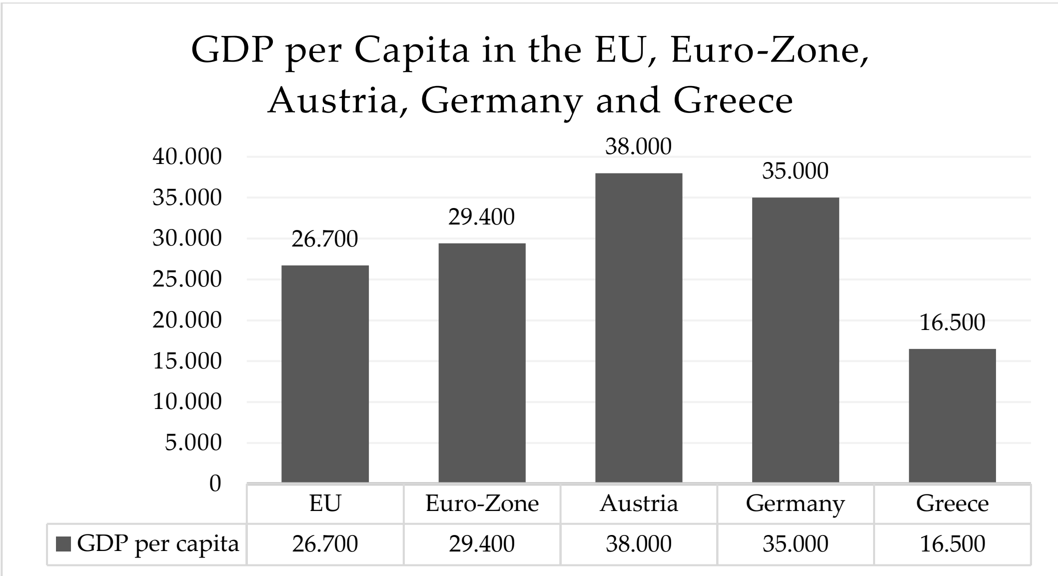
The employment threshold is the economic growth (Clement, Terlau, & Kiy, 2013, p. 551 et seqq.) *which needs to be reached at least, in order for employment to increase* (Klopmeier, 2014, p. 59; Bitting, 2009, p. 69; Frohn, et al., 2003, p. 161).

According to Verdoorn's law (Bairam, 1990, pp. 107-112) there is a linear relationship between labor productivity and the production growth (Pusse, 2002, pp. 71-78; Jungmittag, 2006, p. 20; Erber, Hagemann, & Seiter, 1998, p. 131). Assuming an aggregate economic growth, including that of employment, more labor productivity will lead to increased employment and, according to Keynes, to more demand. The study intends to show:

whether there is a relationship between labor productivity of individual countries – in this case, Austria, Germany and Greece – and the Gross Domestic Product, respectively the PPS,

and is not being conducted in the frame of a regression analysis (Schenderra, 2014, p. 36 et seqq.; Hatzinger, Hornik, & Nagel, 2011, p. 281 et seqq.), because the amount of data is too small.

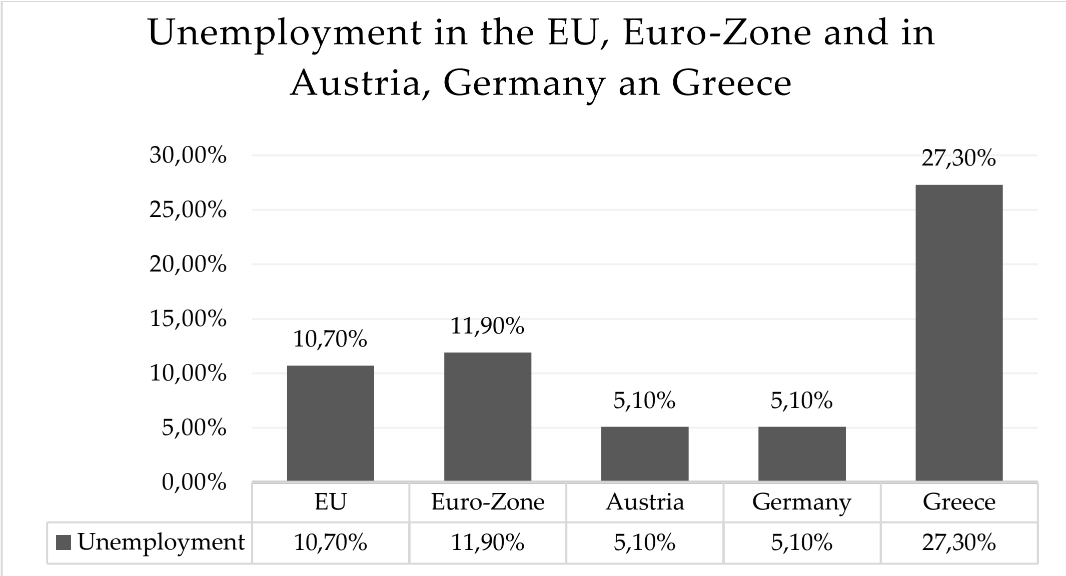
Figure 50: GDP per Capita in the EU, Euro-Zone, Austria, Germany and Greece



Source: Own representation based on Eurostat.

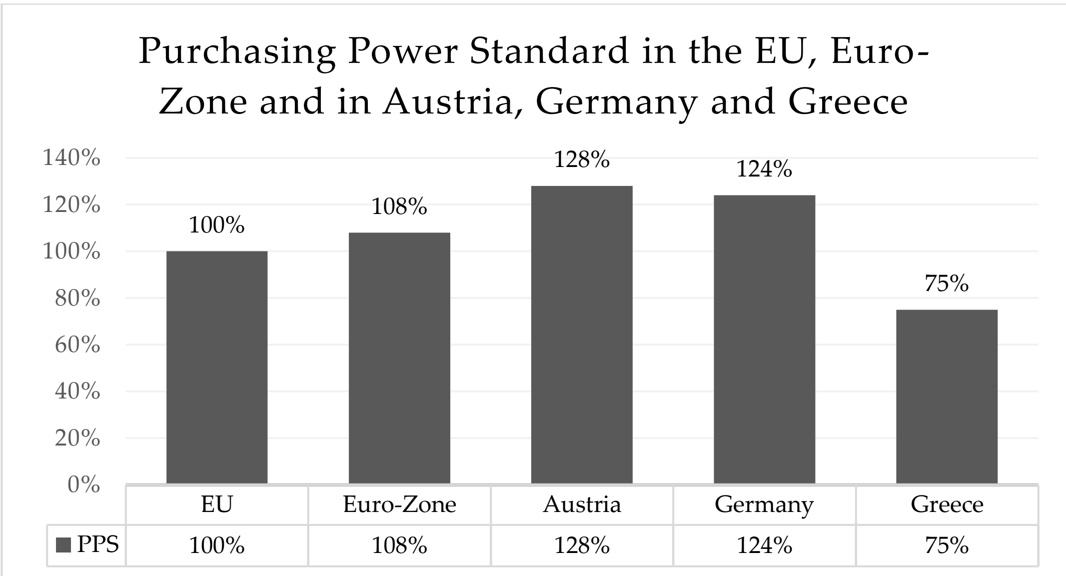
The gross domestic product per capital in the EU, Euro-Zone in Austria, Germany and Greece is shown in figure 50. In figure 51 the unemployment in this areas can be seen and in figure 52 the purchasing power standard.

Figure 51: Unemployment in selected Countries



Source: Own representation based on Eurostat.

Figure 52: Purchasing Power Standard (PPS)

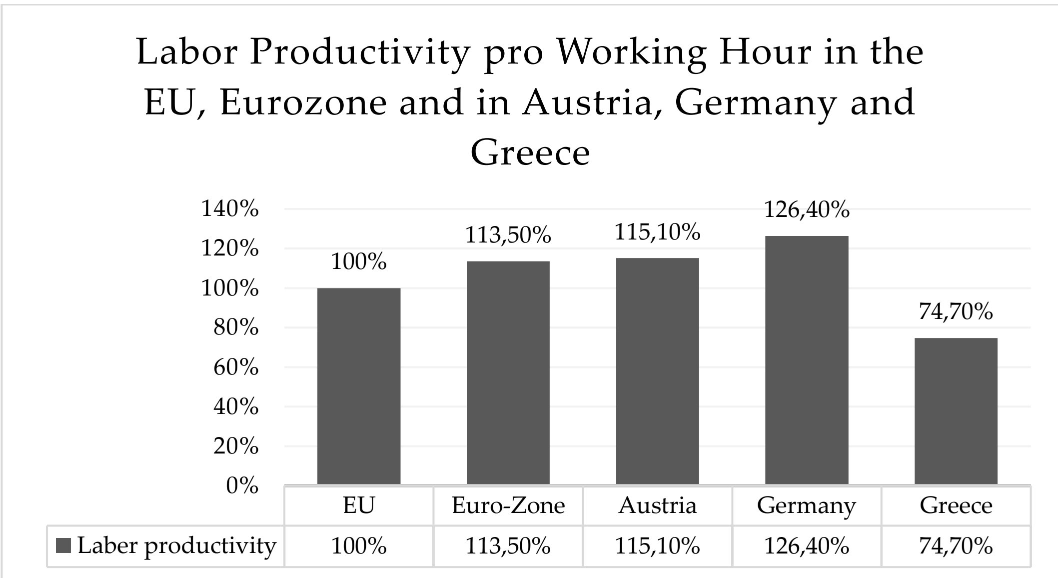


Source: Own representation based Eurostat.

A correlation analysis (Hatzinger, Hornik, & Nagel, 2011, p. 276 et seqq.) would be appropriate, however, the author wanted a distinct depiction of the values, which speak for themselves (the figures, in which the data are derived from 2013 and have been gathered from the pages of the European Union (eurostat, 2016). These figures are only intended to illustrate the principle. In this context, under labor productivity, it is to be understood as nominal labor productivity per hour work.

The study shows that, while Austria's PPS is higher than that of Germany and Greece, the labor productivity (figure 53) of the Austrians is at least lower than that of the Germans. Since Austria has a higher traditional gross domestic product than Germany and reports an identical unemployment rate, a correlation cannot be necessarily established when looking at one period. Recent figures also give no definitive statement about the consistency of the Verdoorn Law (Michie, 2013, p. 879) so there may be a correlation between the labor productivity and gross domestic product per capita and the purchasing power standard.

Figure 53: Labor Productivity pro Working Hour



Source: Own representation based on Eurostat.

Figure 54: Correlation Labor Productivity Austria – Germany

	GDP	Unemployment	PPS	Labor Productivity
■ Germany	3,71	4,6	1,25	1,264
□ Austria	3,91	5,7	1,27	1,148

■ Germany □ Austria

Source: Own representation based on Eurostat.

For 2015 – without Greece – the following figures represent Austria. Labor productivity is 114.8 with a gross domestic product of € 39.100, a PPS of 127 and an unemployment rate of 5.7%. In Germany the labor productivity is 126.4, with a gross domestic product of € 37.100, a PPS of 125 and an unemployment rate of 4.6%. The data are standardized for the graphics.

However, since the values of Austria and Germany are at a very high level as opposed to Greece, a basic correlation (figure 54) between a high labor productivity and the economic growth of country can be assumed. For the European Union and its Member States this could mean that investments in new production facilities and efforts to provide the operators of such enterprises – whether it be founders of new businesses or entrepreneurs or Private Equity firms – with reasonable framework, should be promoted and expedited.

3 LEGAL FRAMEWORK IN SELECTED COUNTRIES

3.1 PRELIMINARY REMARKS

This work aims to generate benefits for entrepreneurs – in terms of start-ups (Ripsas, 1997, p. 69; Gleißner, 2001; Hartmann, 2010, p. 72). For this purpose, a new fund form is to be created, which overcomes primarily the fiscal barriers. With the AIFM Directive 2011/61/EU (Buck-Heeb, 2014, p. 270; Berens R. E., 2014, p. 98; Schwarz, 2016, p. 168) the European legislator has created a set of rules forcing the national legislatures to act accordingly (Muller & Ruttiens, 2013, p. 1). However, this elaboration does not want to interfere with regulatory requirements, whether at EU level or national level. Rather, it should be noted at this point that the author explicitly aims at a new fiscal optimized fund structure which places the focus on the founders of new businesses. For this, it is necessary to recognize existing Private Equity structures and to take measures to create an exemplarily Private Equity fund providing policy recommendations, which allow those interested in Private Equity to combine investments into the future of the European Union with their own business interests.

Chapter 3 presents how much the provisions of the Member states of the European Union differ from each other in regards to Private Equity. In the course, regulatory and fiscal framework, without which at least in Germany a tax classification is hardly possible, will be in part discussed in detail.

The basis for the following explanations is the AIFM Directive 2011/61/EU, the directly flanking delegated regulation (EU) no. 231/2013 of the Commission of 19. December 2012 (with justification) and the ESMA guidelines 2013. Additional agreements and supplements as the delegated regulation (EU) no. 694/2014 or the corresponding implementing regulations would lead to a confusion, which is not conducive to the tax consideration.

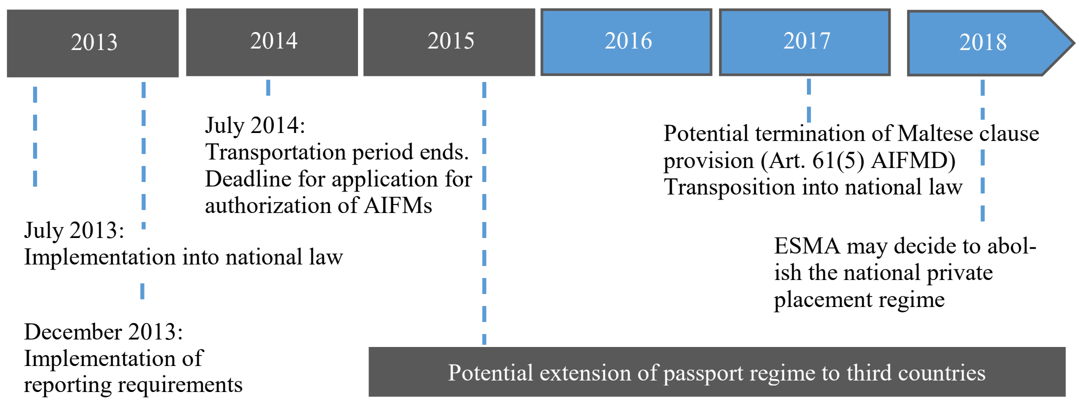
Thus, the chapter begins with a consideration of the rules, which have been provided by the European Union for its Member States. The following explanations were also treated in the publication "Income Tax Treatment of Private Equity Funds in Germany after Directive 2011/61/EU" by the author of this study (Mauer, 2015, pp. 135-154). Alternative Investment Fund Managers (AIFM) control significant parts of all investments (Mauer, 2015, p. 144) in Europe (kpmg, 2013) and linked by the EU Commission to the reasons of the financial crisis (fmm-magazin, 2012). These managers could influence the corporations in which they invest (Postler, 2015, p. 6) and increase the risks within the financial system (kpmg, 2013). In order to obtain comprehensive common supervisory rules, a framework had to be created to address these risks. The Alternative Investment Fund Manager Directive (AIFMD). In the context of the G20 summit in London and Pittsburgh in 2009 (Wallach, 2014, p. 96), the participating heads of State and government decided to regulate system-relevant financial institutions (Grüner, 2011, p. 274). At European level, the regulation of Alternative Investment Fund Managers (AIFM) was implemented in June 2011 by Directive 2011/61/EU (fundresearch.de, 2013). It defines the common requirements for the approval of managers (Tietje, 2015, p. 691; finanzen.net, 2013) and regulates their supervision (Sixt. 2014, p. 175). The goal is to ensure a common approach regarding the manager-associated risks (Glander, 2011, p. 1) and their effect for investors and markets in the EU (fundresearch.de, 2013; Mauer, 2015, p. 144).

The AIFM Directive already entered into effect on 21 July 2011 (Burgmaier & Hüthig, 2015, p. 40; EUR-Lex, 2016). This EU Directive in part leaves the regulations and supervision to the nations. For example, the AIFM Directive does not regulate Alternative Investment Funds (AIF) in regard to the form of organization (Casper, 2014, p. 136). Apart from that, the transition period into national law (Port & Steinlein, 2015, p. 80) expired on 22 July 2013 (Wallach, 2013, p. 96; Mauer, 2015, p. 144).

By the end of 2013, not all Member States had implemented this policy in its entirety, which certainly had a significant influence on this work. Prior to the beginning of this thesis, thus in the context of the exposé and the proposal, it was intended to select Spain and Germany for a closer review of the fiscal framework in particular. Since Spain had not yet fully implemented the AIFM Directive by the expected date, Germany however in any case had been first chosen; Austria and Luxembourg were chosen to accompany this work as reference countries. The qualification of Austria for this comparison is at hand. The close proximity to Germany might initially suggest that the regulations of the two countries are at a similar level. The cultural differences may not be as large, so one could assume the readiness to assume risks, which quite certainly has to be present for a commitment in Private Equity. In addition, Austria has already been examined in regards to growth and in the context of labor productivity in comparison with Germany, in which Austria has already provided surprising results compared to her neighbor. Austria and Luxembourg shall therefore now be examined along with Germany in terms of conditions regarding Private Equity. Luxembourg is considered the model country (Bernhard, 2010, p. 214) in terms of Private equity and has therefore been nominated. The cause that a major proportion of this chapter is devoted to Germany is simply due to the fact that the Federal Republic of Germany is in a difficult position with regard to Private Equity, despite its prominent position in terms of its gross domestic product (sozialpolitik-aktuell.de, 2015), which is probably due to its opaque regulation (Hinrichs, 2012, p. 1). Greece, being another candidate, was also removed from the inner circle during the investigation, since Greece on the one hand has only a few organized Private Equity firms and on the other hand is currently in such a poor economic condition in every respect, that an examination of the terms for Private Equity funds would be predicated on only few data. Nevertheless, Greece is even and especially most interesting for further investigations, since it is there that new conditions for Private Equity within the European Union could provide such an important revival, even though the continuing membership of Greece is yet undetermined (Rieth & Wittenberg, 2014, p. 750).

The AIFM Directive allows EU fund managers to sell Alternative Investment Funds under certain conditions, such as the mandatory use of an authorization process and under the control of national state regulatory, to professional investors (Lexology, 2016).

Figure 55: AIFMD Transposition Timeline



Source: Own representation based on Braun, Haas, & Hornsby, 2013, p. 5.

The timeline (figure 55) above illustrates (Braun, Haas, & Hornsby, 2013, p. 5) the transposition of the Directive.

3.2 LEGISLATIVE CONTENT OF THE AIFM DIRECTIVE

3.2.1 Background of the Establishment of the Directive and its Scope of Application

3.2.1.1 Backgrounds for the Necessity of Action

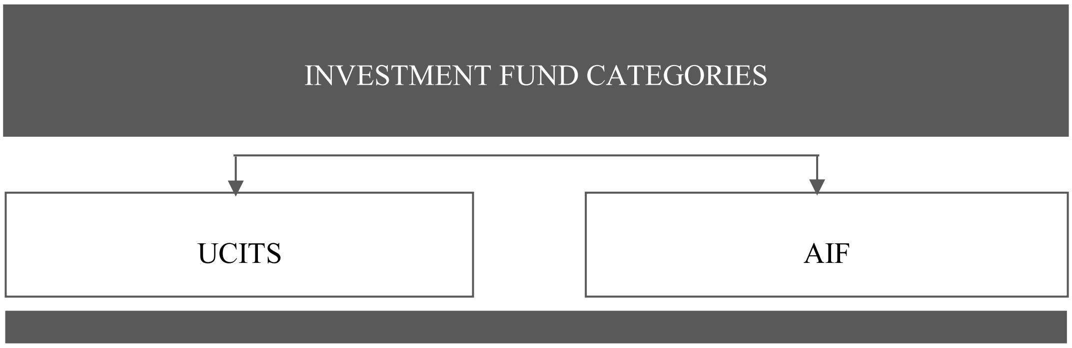
With the continuous development and innovation of the global financial industry, a variety of financial and investment institutions have emerged since the 21st Century as a counter-pole to the traditional banks (Schalast & Barten, 2008, p. 11). The new instruments have similar credit, financing and investment functions like the banks (Brettel et al, 2008, p. 14), but were not subject to formal regulation like the banks (Keuper & Puchta, 2010, p. 198). In the year 2007, these new financial institutions were still titled "Shadow Banks" by the Managing Director of the US Pacific Investment Management, Paul McCulley (Felsenheimer, Klopfer, Mirth, & Altenstadt, 2011, p. 388). These alleged shadow banks do encounter quiet some problems (Shiller, 2012, p. 70). Among those are non-standardized trade, high liquidity risk and a poor regulation of these potential risk factors and are therefore being partly held responsible for the outbreak of the financial crisis (Berg, 2009, p. 265).

For the European Union this also meant that a response was called for (Barnier, 2013). In reaction to the latest financial crisis, the EU legislator adopted Directive 2011/61/EU on Alternative Investment Fund Managers, the so-called AIFM-Directive (Ulmrich, 2013, p. 179). It, for example, introduced a license requirement for fund managers managing and/or distributing alternative investment funds, the so-called AIF (Bürgers & Körber, 2014, p. 20; Europäische Kommission, 2013, p. 2).

The Directive on Alternative Investment Fund Managers adjusts the needs for the natural or legal persons entrusted with the management and the administration of alternative investment funds distributed by professional investors in the EU (Braunberger, Everling, & Rieken, 2011, p. 47). For managers of AIF that are sold in accordance with national regulations to small investors, minimum standards are set (Ammon & Izzo-Wagner, 2015, p. 1408).

The directive applies to a wide diversity of AIF and extends from equity funds to funds that invest in non-liquid assets and their managers (Europäische Kommission, 2013, p. 2; Izzo-Wagner & Baas, 2015, p. 396 et seqq.). Illiquid assets in this context are for example real estate or Private Equity (Izzo-Wagner & Baas, 2015, p. 396 et seqq.; Delegated regulation, 2013, p. 2). The directive is to be applied to all investment strategies and legal types of AIFM and AIF (bafin.de, 2015). For Private Equity Companies, respectively their funds, this means that it regulates the future in a strict and controlled manner, (Izzo-Wagner & Baas, 2015, p. 396 et seqq.; Delegated regulation, 2013, p. 2) so they need in the future a license and a depositary (Izzo-Wagner & Baas, 2015, p. 396 et seqq.; Delegated regulation, 2013, p. 2). Thus, if the AIFM shall have an approval, it must comply with a few requirements (Izzo-Wagner & Baas, 2015, p. 396 et seqq.; Delegated regulation, 2013, p. 2). These include capital requirements, risk and liquidity management, and as already mentioned the appointment of a depositary and information requirements to investors and duties to inform the responsible agencies (Izzo-Wagner & Baas, 2015, p. 396 et seqq.; Delegated regulation, 2013, p. 2).

Figure 56: Categories of Investment Funds in Europe



Source: Own representation based on Buck-Heeb, 2014, p. 314 et seqq.

All investment funds in Europe are now divided by the AIFM Directive (Buck-Heeb, 2014, p.277) into two (figure 56) categories (Delegated regulation, p. 2)[12]. There are now the Undertakings for Collective Investment in Transferable Securities (UCITS) and the Alternative Investment Funds (PWC, 2014, p. 72), in which UCITS are regulated by the UCITS Directive (2009/65/EC) and may be sold on the retail market (Delegated regulation, p.2).

For the UCITS area, management assets exist (Moroni, 2015, p. 1) in the amount of nearly six trillion euros, (Delegated regulation, p.2), which is almost three times as much as for the AIF area (Chevalier & Sciales, 2010) with 2.2 trillion euros, (Delegated regulation, p.2). In 2010 – before the enacting of the AIFM Directive – the AIF-managed assets caught a total of 18 percent of the EU GDP and 68 percent of the assets of AIF were held by institutional investors, of which 70 percent were pension funds or insurance companies (Delegated regulation, 2012, p. 2). The AIFM Directive provides very detailed implementing measures affecting a wide range (Höring J. , 2013, p. 281) of issues, (Delegated regulation, p. 2), for example, including the calculation (Dietrich, 2016, p. 234) of assets under management (Bafin, 2013), measures for accurate alignment of leveraged investments, the determination of certain conditions for exercising the AIFM activity, the transfer of

[12] Delelierte Verordnung (EU) Nr. 231/2013 (EU, 2013) der Kommission vom 19. Dezember 2012 zur Ergänzung der Richtlinie 2011/61/EU (Commission Delegated Regulation (EU) No 231/2013 of 19 December 2012 supplementing Directive 2011/61/EU).

AIFM functions, special provisions for risk and liquidity management (pwc, 2014), clarification of roles and the liability of a depositary, transparency requirements and rules relating to third countries (Delegated regulation, 2012, p.2; pwc, 2014). The here-cited delegated regulation introduces, with regard to the authorization to adopt delegated acts, a uniform body of rules and regulations, ensuring that a level playing field for AIFM exists in the European Union (Delegated regulation, pp. 2-3). A rule is the appropriate legal instrument for establishing uniform rules applicable to the AIFM (Delegated regulation, p. 3). Since a regulation essentially requires no implementation (DNR, 2014), there is no risk of varied applications in the different Member States (Delegated regulation, p. 3). For AIFM it will be easier to cross-border (Volhard & Jang, 2013, pp. 218-219) manage and distribute AIF (Delegated regulation, p.3; Volhard & Jang, 2013, pp. 218-219). In principle, this approach can be viewed as a relief.

3.2.1.2 Scope of Application and Transitional Provisions

The scope of application of the Directive deals with the managers of alternative investment funds (Gubalke & Zander, 2013; Preisser, 2013, p. 217 et seqq.). Alternative investment funds are the collective assets that do not fall under the UCITS Directive (Höring J. , 2013, p. 282; Haase & Dorn, 2015, p. 18). For the period until the final implementation of the Directive, some special arrangements have been created, that are partly no longer valid now. Nevertheless, they should be briefly presented here.

This negative definition from above flows to an extremely broad construction. Among the managers are the managers of hedge funds or Private Equity funds, as well as those of open and closed-end funds and special funds, regardless of their form of organization (Verlag Versicherungswirtschaft, 2014, pp. 241-246; Andres, 2011, p. 95). A manager of an AIF means any legal or natural person (Dietrich, 2015, p. 1203) under the draft directive (Weiser & Jang, 2011). The normal activities of managers are to manage one or more AIF (Braunberger, Everling, & Rieken, 2011; Gubalke & Zander, 2011, pp. 1-5). AIFM may be a manager from outside who is instructed to the management of the AIF accordingly (Gubalke & Zander, 2011, pp. 1-5). Opposite, it may be the AIF itself, which shall then be admitted as AIFM, where the form of organization of the AIF allows an internal management (Gubalke & Zander, 2011, pp. 1-5). The governing body of the AIF (Gubalke & Zander, 2011, pp. 1-5) then decides not to appoint an external AIFM (Cruccolini, 2012, pp. 567-574).

The final draft provides facilitations in the context of the application of the AIFM Directive (Kramer & Recknagel, 2011, pp. 2077-2084; Gubalke & Zander, 2011, pp. 1-5)) when falling below certain thresholds of the total assets under management – the so-called small AIFM (Berk, 2013, pp. 20-21) – and in the management of certain, already existing, closed-end funds. In terms of the draft directive, it is such a small AIFM, if the total assets of all managed AIF do not exceed 100 million Euros or their managed, not leverage financed total assets do not exceed 500 million Euros and no redemption rights (Gubalke & Zander, 2011, pp. 1-5) have arisen during the first five years (Markert, 2010, p. 333). The manager of such AIF only has to register and provide certain information (Zetzsche, 2015, p. 416; Hutzschenreuter T. , 2015, p. 58).

Even when exceeding the thresholds, AIFM which managed funds already closed before the end of the two-year implementation period and which do not participate in additional investments after this period, do not require an authorization under the AIFM Directive (Bundesverband Öffentlicher Banken Deutschlands, 2014, pp. 108-111). Also, according to the AIFM Directive, AIFM which managed funds already closed prior to the end of the two-year implementation period – regardless of any successive investments – required no authorization, if the funds have been launched for a time period which expires latest three years after the two-year implementation period. In this case, however, Article 19 (Späth, 2013, p. 42) and – if necessary – Articles 26 through 29a are to be considered, which include inter alia the obligation to disclose the annual report and to verify the figures presented in the annual report within six months after the end of the financial year (Frick & Gericke, 2013, p. 89).

3.2.1.3 Accreditation Scheme for the Management and Distribution of AIF

The AIFM Directive regulates the principle that the management and the distribution of AIF requires accreditation (Kramer & Recknagel, 2011, pp. 2077-2084);

this means without authorization the future AIF funds may not be managed (Braunberger, Everling, & Rieken, 2011, p. 36) or sold in the European Union, (Kramer & Recknagel, 2011, pp. 2077-2084). In this context it is referred to the so-called disqualification with reservation of authorization (Götting, et al., 2015, p. 691), (Kramer & Recknagel, 2011, pp. 2077-2084). In addition to the requirement of certification for AIFM and thus the regulation of the market access, the Directive incorporates the following (Mayert, 2011, pp. 43-47; Kramer & Recknagel, 2011, pp. 2077-2084):

- Requirements of transparency (Dietrich, 2015, p. 40; Kramer & Recknagel, 2011, pp. 2077-2084)
- Conditions for the pursuit of activities as a manager (Dietrich, 2015, p. 513; Buck-Heeb, 2014, p. 270; Kramer & Recknagel, 2011, pp. 2077-2084)
- Special regulations for managers of non-leveraged AIF and Private Equity AIF (Kramer & Recknagel, 2011, pp. 2077-2084)
- Distribution rules and third country regulations (Kramer & Recknagel, 2011, pp. 2077-2084)
- Provisions (Kramer & Recknagel, 2011, pp. 2077-2084) on competent authorities (bafin.de, 2013)

Some of these requirements do not only apply for the management of funds, but they need to be partially taken into account with the investments of the AIF (EAPSPI, 2012, pp. 5-14) managed by the AIFM, (Kramer & Recknagel, 2011, pp. 2077-2084). With the acquisition of an authorization for the management and distribution of one or more AIF, many admission requirements are related to the directive (Kramer & Recknagel, 2011, pp. 2077-2084). This includes, inter alia, the stocking of a particular seed capital, reliability of directors, and the guarantee of control (Demgensky, 2014, p. 1) by the owners, (Kramer & Recknagel, 2011, pp. 2077-2084) and the place of the headquarters of the AIFM (Lutter, Bayer, & Schmidt, 2012, p. 316) in the same (Tietje, 2015, p. 79) Member State (Kramer & Recknagel, 2011, pp. 2077-2084; Article 8 Directive 2011/61/EU),.

With the permit application under the AIFM Directive, a large number of documents need to be presented (Article 7 para. 2 Directive 2011/61/EU; Kramer & Recknagel, 2011, pp. 2077-2084). This includes information on the managers and the owners of substantial holdings in the AIF, remuneration structures compliant with the regulations, a business plan, an organizational structure as well as information concerning the implementation and maintenance of an AIFM compliance and finally information (finanstilsynet.dk, 2013) on outsourcing issues (Kramer & Recknagel, 2011, pp. 2077-2084). In addition, information on the AIF to be managed are needed; they relate to the investment strategy, potential leverage, possible feeder- and master structures, the seat of the AIF, contractual terms, depositaries (Moloney, 2014, p. 294) and investor information (Article 7 para. 3 Directive 2011/61/EU; Kramer & Recknagel, 2011, pp. 2077-2084).

Alternative Investment Fund Manager (AIFM) as an internally administrated AIF need a capital stock of at least 300.000 Euro whereas an external AIFM has to provide seed capital (Hantschel, 2015) of 125.000 Euro (Kramer & Recknagel, 2011, pp. 2077-2084). If the account of the AIF portfolio administrated by the AIFM (Markert, 2009, p. 334) exceeds 250 million Euro (Kramer & Recknagel, 2011, pp. 2077-2084) further equity capital needs to be raised, whereas the Member States of the European Union can authorize that this may be made available for up to 50 percent through collateral of a credit institution (cssf.lu, 2013) or an insurance company (Article 9 para. 3 Directive 2011/61/EU; Article 6 Directive 2011/61/EU; Kramer & Recknagel, 2011, pp. 2077-2084). As may be the case there are liability risks, it can be covered by additional equity or by taking out liability insurance (Kramer & Recknagel, 2011, pp. 2077-2084). The forecited capital resources of the AIFM shall be invested in liquid assets and may not include notional positions (Kramer & Recknagel, 2011, pp. 2077-2084). Liable for the authorization process are the supervisory authorities at the registered office of the AIFM (Article 7 para. 1 Directive 2011/61/EU; Höring, 2013, p. 282; Kramer & Recknagel, 2011). This function is exemplified accepted and executed in Germany by the Federal Financial Supervisory Authority (BaFin) and in Austria (Wallach, 2013, pp. 104-112) by the FMA (Financial Market Authority).

3.2.2 General Principle of Regulations Regarding AIFM

3.2.2.1 Preliminary Remarks

The requirements for the pursuit of the AIFM activities (Haase & Dorn, 2015, p. 57) are generally formulated in chapter III (Buck-Heeb, 2014, p. 270) of the Directive 2011/61/EU of the European Parliament and Council (cssf.lu, 2013; Kramer & Recknagel, 2011, pp. 2077-2084). The complete catalog consists of good conduct and organizational obligations (Kramer & Recknagel, 2011, pp. 2077-2084) intended to ensure that an AIFM always fulfills his duties in a carefully competent, fair and honest manner in the best interest of the AIF and its investors and to avoid any conflicts of interest (Article 12 Directive 2011/61/EU; BaFin, 2013; Kramer & Recknagel, 2011, pp. 2077-2084). The following section describes the criteria for adequate remuneration structures, answering questions such as:

- How can conflicts of interests be avoided?
- How can risk and liquidity management be adequately implemented? (BaFin, 2013).

The crucial importance of the organizational structure of the AIFM is to functionally and hierarchically (Schmidt-Zango, 2013) separate (Kramer & Recknagel, 2011, pp. 2077-2084) the essential areas of operation according to its material definition of the portfolio and risk management in compliance with article 15 of the AIFM Directive (Schlitt, 2015, p.93; Kramer & Recknagel, 2011).

3.2.2.2 Avoiding Conflicts of Interest

The AIFM Directive requires the commission to establish the criteria (cssf.lu, 2013; Europäische Kommission, 2013, p. 7). By these the responsible authority is in a position to judge whether the AIFM act in abidance by their duties (BaFin, 2013; Europäische Kommission, 2013, p. 7). That is, if they candidly perform their duties with due skill, care, accurateness and act in the interest of the AIF (Braun & Kinsch, 2013, p. B8), as well as treat the investors fairly, using appropriate resources and procedures and to take measures relating to conflicts of interest (Braun & Kinsch, 2013, p. B8; Europäische Kommission, 2013, p.7). The delegated regulation (Delegated regulation (EU) No. 231/2013 of the commission from 19.12.2012) clearly describes, that the obligations primarily are intended to preserve the interests of the AIF or the investors, just as the fairness of the market (Europäische Kommission, 2013, p. 7). It settles the extent of due care in general and the extent of due diligence when investing in limited liquid assets and the choosing and nomination of prime brokers (Prassl, 2015, pp. 63-64) and counterparties (Prassl, 2015, pp. 63-64, Europäische Kommission, 2013, p. 7). In this context, the prime broker (Moloney, 2014, p. 275) is a service provider specializing both in the needs of hedge funds and the Private Equity funds (Kaiser D. G., 2004, p. 109; Curley, 2008, p. 61). This involves the raising of outside capital and the trade and custody of securities (Kaisser D.G.; 2004, p. 109; Curley, 2008, p. 61). The regulation also determines rules for the creation of incentives and the treatment of contracts, including reporting requirements for the implementation of subscription and redemption orders and regulations for the placement of trade orders of the AIF and their establishment, and the pooling and distribution of orders (Europäische Kommission, 2013, p. 7). It also clarifies which types of conflicts (Behme & Lichtenstein, 2015, p. 324 et seqq.) of interest may occur (Behme, 2015, p. 329; Europäische Kommission, 2013, p. 7). In addition, it also specifies the respective principles with measures and regulations. Thereby AIFM shall be implemented and applied in order to determine conflicts of interest (Dietrich, 2016, p. 93; Europäische Kommission, 2013, p. 7). This intends to prevent, manage, monitor and report conflicts of interest (Europäische Kommission, p. 7).

3.2.2.3 Requirements Regarding the Liquidity Management and the Risk Management

Subject of consideration of the requirements for risk management (Europäische Kommission, 2013, p. 7) are the regulation of the risk management function and its structural integration into the AIFM organization (Nack, 2012, pp. 351-363; Schwarz, 2016, p. 168; Preuß & Schöne, 2016, pp. 391-438). The main principles of the AIFM Directive are in the functional and hierarchical separation of the portfolio and risk management (Europäische Kommission, 2013, p. 8). Due to the increasing importance of the risk management function, it is necessary to enable

AIFM for a more independent and objective risk assessment (credit-suisse.com, 2014).

Managers of AIF are encouraged to divide the portfolio and risk management in different areas of responsibility and to execute a permanent risk management function (Stadter & Dirnaichner, 2011, pp. 1-33). If AIFM implements an unclear division of areas or executes those with disproportional efforts, precautions shall be conducted so as to ensure a minimum level of autonomy of the risk management function (Stadter & Dirnaichner, 2011, pp. 1-33). A conceivable measure would be to separate the conflicted areas of responsibility (Europäische Kommission, 2013, p. 8). The methods for this are the establishment of independent reporting channels and control mechanisms and the assessment of the risk management function by an independent third institution or by an internal panel (Goldbeck, 2013, pp. 17-22).

The assignment of the risk management function of the AIFM Directive is mainly the enforcement of the risk policy, which means the AIFM must create the conditions for an effective risk management (Schulz & Partner, 2015). The requirements are aimed at maintaining a typical risk profile (Hornschuh, et al., 2013, pp. 1-97). Based on the directive, AIFM can implement appropriate risk management processes, methods and systems about which written documentation are created (Europäische Kommission, 2013, p. 66; Article 15 Directive 2011/61/EU). The management should review these processes, systems and methods at least once every year in regards to their effectiveness (Bubel & Steinbissl, 2012, p. 67).

As established in the 2013 published final ESMA proposals (ESMA – European Securities and Markets Authority), AIFM are instructed to address especially non-payment risks in regards to the liquidity, the market and credits in the context of their risk management (esma, 2013, pp. 1-50). To comply with the AIFM typical risk profiles, qualitative and/or quantitative limits must be determined (esma, 2013, pp. 1-50). If then these limits are exceeded, AIFM must immediately report to the senior management. In addition, risk positions are to be quantified regularly (Article 15 Directive 2011/61/EU), in which the AIFM Directive expressly prescribes the application of stress tests (Stadter & Dirnaichner, 2011, pp. 1-33).

In the basic regulatory area of the AIFM Directive, the establishment and warranty of an adequate liquidity management is considered to be very important (Europäische Kommission, 2013, p. 12; Kramer & Recknagel, 2011, pp. 2077-2084). The mission of liquidity management is to create a balanced liquidity profile (Europäische Kommission, 2013, p. 24; Baur, 2015, p. 412; Braunberger, Everling, & Rieken, 2011, p. 38). This permits the manager of the AIF to fulfill the commitments of investors or creditors even under unusual market conditions. An effective liquidity management can assess the applicability of the methods and systems used and can identify and control liquidity risks at an early stage (Gehwald & Naumann, 2011, p. 18).

There is no "one size fits all" liquidity management (Glaser, 2015, p. 183). Therefore, the methods and systems must be individually tailored to the AIF (Stadter & Dirnaichner, 2011, pp. 1-33; Europäsiche Kommission, pp. 8, 73-75; Article 16 Directive 2011/61/EU). Consequently, there are no rigid regulations for the establishment of liquidity management, but rather more general specifications for its outline (Stadter & Dirnaichner, 2011, pp. 1-33; Europäsiche Kommission, pp. 8, 73-75; Article 16 Directive 2011/61/EU). These can be implemented depending on the size and structure of the AIF (Stadter & Dirnaichner, 2011, pp. 1-33; Europäsiche Kommission, pp. 8, 73-75; Article 16 Directive 2011/61/EU). The principle, measures and instruments finally proposed in the ESMA include (Stadter & Dirnaichner, 2011, pp. 1-33; Europäsiche Kommission, pp. 8, 73-75; Article 16 Directive 2011/61/EU):

- Provision of liquidity reserves must be tailored to the specifics of the AIF,
- the execution and verification of appropriate provisions and methods for the judgement of different risks (size and quality) requires the existing and planned positions. Stress tests must regularly be performed at least once per year,
- risk policy and risk management procedures must be documented and be subject to annual reviews,
- appropriate de-escalation procedures are to be established in order to detect conceivable liquidity shortages at an early stage (Stadter & Dirnaichner,

2011, pp. 1-33; Europäsiche Kommission, pp. 8, 73-75; Article 16 Directive 2011/61/EU).

Similar minimum requirements are already proclaimed by InvMARisk (Minimum Requirements for Risk Management) in its circular 5/2010 dated June 30th, 2010 (Wagner O. , 2015, pp. 73-96; Söbbing, 2015).

3.2.2.4 Remuneration Schemes within the AIFM Directive

Specific rules on remuneration policies and requirements for the design of bonus systems are defined in article 13 of the AIFM Directive and in annex II (Boué, Kehlbeck, & Leonhartsberger-Heilig, Lutter, 2012, 97; Bayer, & Schmidt, 2012, p. 317; Europäische Kommission, 2013, p. 41; Article 13 Directive 2011/61/EU; Appendix II Remuneration Policy AIFM Directive 2011/61/EU) of the same (Höring J. , 2013, pp. 273-286). To guarantee the properties of the risk management, the AIFM Directive, respectively the parties liable for the definition, has determined the following (Europäische Kommission, 2013, p. 41; Article 13 Directive 2011/61/EU; Appendix II Renumeration Policy AIFM Directive 2011/61/EU):

- The remuneration policy must match the business strategy, objectives, values and interests of the AIFM, the managed AIFs and their investors, incidentally avoiding conflicts of interest (Europäische Kommission, 2013, p. 41; Article 13 Directive 2011/61/EU; Appendix II Renumeration Policy AIFM Directive 2011/61/EU)
- The remuneration policy shall be subject for an internal review at least once a year (Europäische Kommission, 2013, p. 41; Article 13 Directive 2011/61/EU; Appendix II Renumeration Policy AIFM Directive 2011/61/EU).
- The wages of employees are performance related (Europäische Kommission, 2013, p. 41; Article 13 Directive 2011/61/EU; Appendix II Renumeration Policy AIFM Directive 2011/61/EU)
- For the compensation of the AIFM is not only crucial the total income, but also the performance of his staff (Europäische Kommission, 2013, p. 41; Article 13 Directive 2011/61/EU; Appendix II Renumeration Policy AIFM Directive 2011/61/EU)

- The total remuneration shall consist of two parts, the fixed and the variable components must be in an appropriate ratio to each other (Europäische Kommission, 2013, p. 41; Article 13 Directive 2011/61/EU; Appendix II Remuneration Policy AIFM Directive 2011/61/EU)
- An AIFM is required to constitute a remuneration committee according to size and complexity (Engert, 2014, pp. 108-122) of the business activities (Europäische Kommission, 2013, p. 41; Article 13 Directive 2011/61/EU; Appendix II Remuneration Policy AIFM Directive 2011/61/EU)

The guidelines of the remuneration policy, which are recorded in the AIFM Directive, were enacted by the ESMA (esma, 2013, pp. 1-50) in cooperation with the European Banking Authority (Article 13, para. 2 AIFM Directive in conjunction with recital 27 of the AIFM Directive). Thus, a coalescence in the assessment of remuneration policies between different supervisory authorities can be achieved (Article 13, para. 2 AIFM Directive in conjunction with recital 27 of the AIFM Directive). Outstanding for the remuneration policy is the requirement that at least 50 percent (Appendix II remuneration policy AIFM Directive 2011/61/EU) of the variable wages of the AIFM must derive from shares in the managed AIF or equivalent ownership interests (Volhard, Rodin, Jang, & Kruschke, 2013, p. 13). The background of the regulation may not be immediately comprehensible offhand. However, it is conceivable that the employees should be instructed to sustainability in handling the AIF. This allows them to directly and continuously approach the economic success of the AIF. A self-interest in an investment always leads to more diligence and also the dissolution of the one or other conflict (Engert, 2014, pp. 108-122).

3.2.2.5 Asset Evaluation of the AIF

The AIFM Directive on the assessment of the assets of AIFs shall foremost protect the investor interests (Dietrich, 2016, p. 1621 et seqq.; Dietrich, 2015, p. 632 et seqq.; Europäische Kommission, 2013, p. 74 et seqq.; preliminary AIFMD side note, para. 29 et seqq.; Kramer & Recknagel, 2011, pp. 2077-2084). Thereafter, the AIFM can impartially and carefully evaluate the assets with the expertise available

(Dietrich, 2016, p. 1621 et seqq.; Dietrich, 2015, p. 632 et seqq.; Europäische Kommission, 2013, p. 74 et seqq.; preliminary AIFMD side note, para. 29 et seqq.; Kramer & Recknagel, 2011, pp. 2077-2084). In compliance with the directive, the AIFM must ensure an adequate and coordinated process for independent and proper valuation of the assets for the AIF managed by it (Baur & Tappen, 2016, p. 1621 et seqq.; Dietrich, 2015, p. 632 et seqq.; Europäische Kommission, 2013, p. 74 et seqq.; preliminary AIFMD side note, para. 29 et seqq.; Kramer & Recknagel, 2011, pp. 2077-2084). To do so, the evaluation guidelines and processes for each form of the AIFM assets are to be transparent created and documented in written form (Nack, 2012, 359 et seqq.; Dietrich, 2016, p. 1621 et seqq.; Dietrich, 2015, p. 632 et seqq.; Europäische Kommission, 2013, p. 74 et seqq.; preliminary AIFMD side note, para. 29 et seqq.; Kramer & Recknagel, 2011, pp. 2077-2084).

With reference to the different assessment procedures in different jurisdictions and the variety of assets, ESMA has merely established general principles for the development and implementation of assessment procedures for an appropriate and autonomous assessment of the assets by the AIFM (Dietrich, 2016, p. 1621 et seqq.; Dietrich, 2015, p. 632 et seqq.; Europäische Kommission, 2013, p. 74 et seqq.; preliminary AIFMD side note, para. 29 et seqq.; Kramer & Recknagel, 2011, pp. 2077-2084). The different valuation expertise in the different European jurisdictions, especially in real estate AIFs, leads to inconsistent assessments; this can indirectly affect the value of shares of AIFs (Dietrich, 2016, p. 1621 et seqq.; Dietrich, 2015, p. 632 et seqq.; Europäische Kommission, 2013, p. 74 et seqq.; preliminary AIFMD side note, para. 29 et seqq.; Kramer & Recknagel, 2011, pp. 2077-2084). National legislators are therefore encouraged to endorse common assessment methods and procedures – either in the situs state or in the state of residence – for the evaluators (Dietrich, 2016, p. 1621 et seqq.; Dietrich, 2015, p. 632 et seqq.; Europäische Kommission, 2013, p. 74 et seqq.; preliminary AIFMD side note, para. 29 et seqq.; Kramer & Recknagel, 2011, pp. 2077-2084). If this happens, it might impede the documentation and inspection requirements of the AIFM, but at the same time will open conditions of competition that are marketable (bvi.de, 2012) in all of Europe (Dietrich, 2016, p. 1621 et seqq.; Dietrich, 2015, p. 632 et seqq.; Europäische

Kommission, 2013, p. 74 et seqq.; preliminary AIFMD side note, para. 29 et seqq.; Kramer & Recknagel, 2011, pp. 2077-2084).

According to ESMA, the AIFM has to guarantee that the assessment strategies and procedures are disposed in a stable and permanent manner (Dietrich, 2016, p. 1621 et seqq.; Dietrich, 2015, p. 632 et seqq.; Europäische Kommission, 2013, p. 74 et seqq.; preliminary AIFMD side note, para. 29 et seqq.; Kramer & Recknagel, 2011, pp. 2077-2084). The further provisions go towards evaluations strategies, procedures and methods being applied on a regular basis (Dietrich, 2016, p. 1621 et seqq.; Dietrich, 2015, p. 632 et seqq.; Europäische Kommission, 2013, p. 74 et seqq.; preliminary AIFMD side note, para. 29 et seqq.; Kramer & Recknagel, 2011, pp. 2077-2084). This means that at least once per year these strategies, procedures and methods are to be reassessed (Dietrich, 2016, p. 1621 et seqq.; Dietrich, 2015, p. 632 et seqq.; Europäische Kommission, 2013, p. 74 et seqq.; preliminary AIFMD side note, para. 29 et seqq.; Kramer & Recknagel, 2011, pp. 2077-2084). If new investment strategies are applied and investments are being placed in new asset categories not covered by the previous valuation principles, the assessment for an AIF (esma, 2012) shall be reviewed (Dietrich, 2016, p. 1621 et seqq.; Dietrich, 2015, p. 632 et seqq.; Europäische Kommission, 2013, p. 74 et seqq.; preliminary AIFMD side note, para. 29 et seqq.; Kramer & Recknagel, 2011, pp. 2077-2084).

In compliance with ESMA, the AIFM shall finally ensure that the values of all assets of the AIF managed by it are accurate (Dietrich, 2016, p. 1621 et seqq.; Dietrich, 2015, p. 632 et seqq.; Europäische Kommission, 2013, p. 74 et seqq.; preliminary AIFMD side note, para. 29 et seqq.; Kramer & Recknagel, 2011, pp. 2077-2084). The AIFM has to document each asset class, exactly as this must be done for the individual values (Dietrich, 2016, p. 1621 et seqq.; Dietrich, 2015, p. 632 et seqq.; Europäische Kommission, 2013, p. 74 et seqq.; preliminary AIFMD side note, para. 29 et seqq.; Kramer & Recknagel, 2011, pp. 2077-2084). The assessment schemes provide control processes for certain assets since complex and illiquid financial instruments (esma, 2014, pp. 1-3) present a significant risk in the estimate of inadequate values (Dietrich, 2016, p. 1621 et seqq.; Dietrich, 2015, p. 632 et seqq.; Europäische Kommission, 2013, p. 74 et seqq.; preliminary AIFMD side note, para. 29 et seqq.; Kramer & Recknagel, 2011, pp. 2077-2084).

This assessment must be carried out at least once a year (Dietrich, 2016, p. 1621 et seqq.; Dietrich, 2015, p. 632 et seqq.; Europäische Kommission, 2013, p. 74 et seqq.; preliminary AIFMD side note, para. 29 et seqq.; Kramer & Recknagel, 2011, pp. 2077-2084). For open AIFs the frequency of assets and the sale and repurchase cycle of the AIFs must be reasonable. With closed AIFs, a reassessment has to be conducted with changes in capital (Dietrich, 2016, p. 1621 et seqq.; Dietrich, 2015, p. 632 et seqq.; Europäische Kommission, 2013, p. 74 et seqq.; preliminary AIFMD side note, para. 29 et seqq.; Kramer & Recknagel, 2011, pp. 2077-2084).

The assessment for different types of assets may be implemented by different evaluators, externally or by the AIFM itself (Dietrich, 2016, p. 1621 et seqq.; Dietrich, 2015, p. 632 et seqq.; Europäische Kommission, 2013, p. 74 et seqq.; preliminary AIFMD side note, para. 29 et seqq.; Kramer & Recknagel, 2011, pp. 2077-2084). An external evaluator has to be independent and provide sufficient human and technical resources (Baur, 2015, p. 2002), as well as adequate expertise in order to provide an adequate and independent (Leißner, et al., 2012, pp. 1-39) assessment (Dietrich, 2016, p. 1621 et seqq.; Dietrich, 2015, p. 632 et seqq.; Europäische Kommission, 2013, p. 74 et seqq.; preliminary AIFMD side note, para. 29 et seqq.; Kramer & Recknagel, 2011, pp. 2077-2084). If the assessment is being conducted by the AIFM itself, the assessment of the portfolio management and remuneration policies needs to be ensured functionally independent (Dietrich, 2016, p. 1621 et seqq.; Dietrich, 2015, p. 632 et seqq.; Europäische Kommission, 2013, p. 74 et seqq.; preliminary AIFMD side note, para. 29 et seqq.; Kramer & Recknagel, 2011, pp. 2077-2084). In the process, conflicts of interest must be avoided and an undue influence of employees must be excluded (Dietrich, 2016, p. 1621 et seqq.; Dietrich, 2015, p. 632 et seqq.; Europäische Kommission, 2013, p. 74 et seqq.; preliminary AIFMD side note, para. 29 et seqq.; Kramer & Recknagel, 2011, pp. 2077-2084). The responsible parties can demand the review of the evaluation and the evaluation procedures by an independent evaluator (Dietrich, 2016, p. 1621 et seqq.; Dietrich, 2015, p. 632 et seqq.; Europäische Kommission, 2013, p. 74 et seqq.; preliminary AIFMD side note, para. 29 et seqq.; Kramer & Recknagel, 2011, pp. 2077-2084). Even if an AIFM commissions an external evaluator, he is in authority for the correct valuation of the assets of the AIFs (Dietrich, 2016, p. 1621 et seqq.; Dietrich, 2015, p. 632 et seqq.; Europäische Kommission, 2013, p. 74 et seqq.; preliminary AIFMD side note, para. 29 et seqq.; Kramer & Recknagel, 2011, pp. 2077-2084). However, the external evaluator is liable to losses of the AIFM (Leißner, et al., 2012, pp. 1-39) due to culpable nonfeasance (Dietrich, 2016, p. 1621 et seqq.; Dietrich, 2015, p. 632 et seqq.; Europäische Kommission, 2013, p. 74 et seqq.; preliminary AIFMD side note, para. 29 et seqq.; Kramer & Recknagel, 2011, pp. 2077-2084).

3.2.2.6 Transparency Requirements for an EU AIF

The transparency requirements represent another regulatory area of the AIFM Directive., which provides significantly more demanding requirements than, for example, the old German Investment Act used to provide (Europäische Kommission, 2013, p. 10 et seqq.; Article 19-24 AIFM Directive 2011/61/EU; Kramer & Recknagel, 2011, pp. 2077-2084; Dietrich, 2016, p. 610, Lutter, Bayer, & Schmidt, 2012, p. 317 recital 250).

Under article 19 of the AIFM Directive, an AIFM is required to submit an annual report in each fiscal year for each of the AIF managed and distributed throughout the European Union (Europäische Kommission, 2013, p. 10 et seqq.; Article 19-24 AIFM Directive 2011/61/EU; Kramer & Recknagel, 2011, pp. 2077-2084; Dietrich, 2016, p. 610, Lutter, Bayer, & Schmidt, 2012, p. 317 recital 250). The annual reports mainly serve the responsible authorities of the origin Member State of the AIFM, the authorities of the origin Member State of the AIF, and the investors (Europäische Kommission, 2013, p. 10 et seqq.; Article 19-24 AIFM Directive 2011/61/EU; Kramer & Recknagel, 2011, pp. 2077-2084; Dietrich, 2016, p. 610, Lutter, Bayer, & Schmidt, 2012, p. 317 recital 250). An AIFM must perform the information obligations towards the investors under article 20 AIFM Directive and towards the responsible authorities under article 21 of the AIFM Directive (Europäische Kommission, 2013, p. 10 et seqq.; Article 19-24 AIFM Directive 2011/61/EU; Kramer & Recknagel, 2011, pp. 2077-2084; Dietrich, 2016, p. 610, Lutter, Bayer, & Schmidt, 2012, p. 317 recital 250). For the acquisition of companies and in the application of leverage the information and communication obligations do not only apply towards the relevant authorities, but also towards the target companies and their investors, as well as the employees (Volhard & Jang, 2012/2013, pp. 218-219) respectively their representatives (Europäische Kommission, 2013, p. 10 et seqq.; Article 19-24 AIFM Directive 2011/61/EU; Kramer & Recknagel, 2011, pp. 2077-2084; Dietrich, 2016, p. 610, Lutter, Bayer, & Schmidt, 2012, p. 317 recital 250).

AIF managers are required to submit an annual report - latest sixth months after the last financial year (Europäische Kommission, 2013, p. 10 et seqq.; Article 19-24 AIFM Directive 2011/61/EU; Kramer & Recknagel, 2011, pp. 2077-2084; Dietrich, 2016, p. 610, Lutter, Bayer, & Schmidt, 2012, p. 317 recital 250). The authorities require in addition to a balance sheet, a division of property, and a comparison of income and expenses. In addition, the manager must also make detailed informations on the remuneration of employees, including carried interests (bvi, 2013) paid from the AIF (Europäische Kommission, 2013, p. 10 et seqq.; Article 19-24 AIFM Directive 2011/61/EU; Kramer & Recknagel, 2011, pp. 2077-2084; Dietrich, 2016, p. 610, Lutter, Bayer, & Schmidt, 2012, p. 317 recital 250).

It is not sufficient to fulfill the obligations above. Futher informations must be passed on to the investor (Europäische Kommission, 2013, p. 10 et seqq.; Article 19-24 AIFM Directive 2011/61/EU; Kramer & Recknagel, 2011, pp. 2077-2084; Dietrich, 2016, p. 610, Lutter, Bayer, & Schmidt, 2012, p. 317 recital 250). Therefore, it is necessary to communicate the objectives of the fund as well as the strategy of the investment (Europäische Kommission, 2013, p. 10 et seqq.; Article 19-24 AIFM Directive 2011/61/EU; Kramer & Recknagel, 2011, pp. 2077-2084; Dietrich, 2016, p. 610, Lutter, Bayer, & Schmidt, 2012, p. 317 recital 250). Particular importance is beyond the description of the assets in which the AIF may invest and all associated risks, information on liquidity management, cost and remuneration structures, and a description of the way the AIFM ensures a fair treatment of the investors (Europäische Kommission, 2013, p. 10 et seqq.; Article 19-24 AIFM Directive 2011/61/EU; Kramer & Recknagel, 2011, pp. 2077-2084; Dietrich, 2016, p. 610, Lutter, Bayer, & Schmidt, 2012, p. 317 recital 250). In addition, the AIFM has to regular forward information about the markets and instruments of each AIF he manages to the (Bank, 2014, p. 1) competent authorities (Europäische Kommission, 2013, p. 10 et seqq.; Article 19-

24 AIFM Directive 2011/61/EU; Kramer & Recknagel, 2011, pp. 2077-2084; Dietrich, 2016, p. 610, Lutter, Bayer, & Schmidt, 2012, p. 317 recital 250).

3.2.3 Special Regulations for the Administrators of Leveraged AIF and Private Equity AIF

3.2.3.1 Regulations for Leveraged Alternative Investment Funds

For the administration of a leveraged Alternative Investment Fund (AIF) (Sixt, 2014, p. 175; Zöbeley, 2014, p. 20) the Alternative Investment Fund Manager is subject to extended disclosure (Lutter, Bayer, & Schmidt, 2012, p. 317) obligations (Lutter, Bayer, & Schmidt, 2012, p. 37; Kramer & Recknagel, 2011, pp. 2077-2084) towards the competent authorities (Hornschu, et al., 2013) as well as towards the investors (Article 24 para. 4 Directive 2011/61/EU and Article 23 para. 5 Directive 2011/61/EU; Kramer & Recknagel, 2011, pp. 2077-2084; Hornschu, et al., 2013). The AIFM has the obligation to declare to the competent authorities (Dietrich, 2016, p. 660), that the scheduled limiting of the scope of leverage with each of the AIF managed by him is appropriate (Article 25 para. 3 Directive 2011/61/EU; Baur & Tappen, 2016, p. 660; Kramer & Recknagel, 2011, pp. 2077-2084). At the same time, the manager of Alternative Investment Funds is obliged to always comply with this limitation (Article 25 para. 3 Directive 2011/61/EU; Kramer & Recknagel, 2011, pp. 2077-2084). This information must be submitted to the competent authorities by the AIFM (Kramer & Recknagel, 2011, pp. 2077-2084). In the obligations governed by the AIFM Directive, the competent national authorities are to communicate with ESMA (Article 25 para. 2 Directive 2011/61/EU; Kramer & Recknagel, 2011, pp. 2077-2084) for information purposes so that systemic risks in the financial system, market disruptions or risks to the long-term economic growth (Zander, 2013, p. 43 et seqq.) through the use of leverage is reduced (Article 25 para. 1 Directive 2011/61/EU; Article 25 para. 2 Directive 2011/61/EU; Zander, 2013, p. 43. et seqq.; Kramer & Recknagel, 2011, pp. 2077-2084).

The authorities obtained with the AIFM Directive in accordance with article 25, para. 3, sentence 2 and para. 7 sanctions and intervention options (Dietrich, 2015, p. 132), go far beyond the information requirements and intervention (Dietrich, 2015, p. 132; Kramer & Recknagel, 2011, pp. 2077-2084). The sense of possible sanctions and interventions is to get stability in the financial systems (Kramer & Recknagel, 2011, pp. 2077-2084). Therefore, the amount of debt financing by an AIFM, shall be determined by the authorities (Article 25 para. 3 Directive 2011/61/EU; Dietrich, 2015, p. 132; Kramer & Recknagel, 2011, pp. 2077-2084). This intervention has enough potential for managers of alternative investment funds to be more cautious at the choice of investments (Dietrich, 2015, p. 132; Kramer & Recknagel, 2011, pp. 2077-2084).

Whether these mandatory rules are actually applied is still hotly debated (Kramer & Recknagel, 2011, pp. 2077-2084). Ambiguity, there is also the question – is such funding to limit – to the existing debt financing such investments (Kramer & Recknagel, 2011, pp. 2077-2084). Surely, it would not be a problem to replace this debt financing with equity. Nevertheless, this would require that equity exist.

3.2.3.2 Acquisition of Control over Companies by AIF

For the Alternative (Vancas, 2010, p. 1 et seqq.) Investment Fund (AIF), which takes over control of companies (Trübstein, 2015, p. 239), the AIFM Directive has regulated that the AIFM has increased information and notification obligations (Kramer & Recknagel, 2011, pp. 2077-2084). In addition, there is the ban (Zetzsche, 2015, p. 268) of the so-called asset stripping (Manchot, 2010, p. 59; Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 98), which indicates a process in which an undervalued company is bought with the intention of generating profits by selling (Coenen & Jovanovic, 2014) the assets (Kramer & Recknagel, 2011, pp. 2077-2084).

According to Article 27 para. 1 Directive 2011/61/EU and commented by Kramer & Recknagel (2011, pp. 2077-2084) the AIFM shall inform the competent authorities, if the proportion of voting rights of AIF exceeds certain values or falls (10, 20, 30, 50 and 75%). This applies to the purchase of shares in a non-listed company. Thus the reference to Private Equity would be restored.

Similar regulations are already being applied for stock companies - exemplary mentioned be at this point §20 of the German Stock Corporation Act (Diekmann, 2009, pp. 13-21) and similar provisions in the Companies Act of the

United Kingdom, the Companies Act in Austria or the Commercial Law in Luxembourg - as well as for listed companies - here in example §21 of the German Securities Trading Act of Germany (Brellochs, 2015, p. 1) - or legal norms (Bafin, 2013) of the Securities Exchange Act of Austria.

Meanwhile, the information obligation also extends to limited liability companies (Kramer & Recknagel, 2011, pp. 2077-2084). If the AIF is not managed itself, these information requirements are related to the manager of the AIF. If a manager of alternative investment funds acquire control (Altmeyer & Ngo, 2015, p. B4) of the company (Zeppenfeld & von Jacobs, 2011, p. 1) managing by him, so that manager is obliged to inform all parties about this change (Article 27 and 28 Directive 2011/61/EU; Kramer & Recknagel, 2011, pp. 2077-2084; Altmeyer & Ngo, 2015, B4). Therefore, it is henceforth no longer possible to take over virtually unnoticed without the knowledge of the management and the workers.

Of course, the normal rules of buying or selling of shares must be respected (Kramer & Recknagel, 2011, pp. 2077-2084). This of course includes the identity of the purchaser, the amount of voting rights, the conditions of the acquisition and the date on which control was acquired (Article 27 para. 2 and 3 Directive 2011/61/EU; Kramer & Recknagel, 2011, pp. 2077-2084). However, the directive also refers to further information requirements (Kramer & Recknagel, 2011, pp. 2077-2084). Therefore, it is in accordance with Article 28 para. 2 Directive 2011/61/EU essential that AIFM submit information for preventing and managing conclicts (Bundesrat, 2012, pp. 1-597) of interest between the parties (managers, funds and entrepreneur). This information must also include the taken security measures (Kramer & Recknagel, 2011, pp. 2077-2084). The details of the presentation of the information is not supplied (Kramer & Recknagel, 2011, pp. 2077-2084). Nevertheless, it is clear, that the legislature wants a strong exchange of information and thereby differ between companies, which are listed or not. The stricter obligation (Fundresearch, 2013) to provide information obtained AIFM for unlisted companies employees should be particular protected by the directive (Bundesregierung, 2012, pp. 1-406). According to Article 28 para. 2 letter c Directive 2011/61/EU, information should be provided about the external and internal communication

(Kramer & Recknagel, 2011, pp. 2077-2084). Regarding the procedure for the settlement of Grohe AG – see Regner (2008, p. 71) – that is a positive signal. That both the authorities and the investors must be informed of the financing of the transaction can also be understood as a step in the right direction (Article 28 para. 5 Directive 2011/61/EU; Fundresearch.de, 2013). Excluded from such notification requirements are the so-called SPE or SPV (Article 26 para. 2 Directive 2011/61/EU; Kramer & Recknagel, 2011, pp. 2077-2084) – special purpose entities or special purpose vehicles are legal entities created to fulfill narrow specific or temporary objectives (Lüdenbach, 2010, p. 341) – for the acquisition and holding of real estate and unlisted target companies, if this is a small or medium-sized company (Article 26 para. 2 Directive 2011/61/EU; BaFin, 2013; Kramer & Recknagel, 2011, pp. 2077-2084).

The asset stripping describes an activity of buying low-yield but substance-strong companies and are then breaking them down into its individual parts (Seffer & Gringel, 2014, pp. 1-16; Macharzina & Wolf, 2008, p. 717). The directive aims to prevent this approach by managers of alternaive investment funds, by prohibiting that the AIFM involved, that it comes in the target company to distributions that lead the net assets below the subscribed capital (Article 30 para. 1 Directive 2011/61/EU; Kramer & Recknagel, 2011, pp. 2077-2084). This includes measures (Behme, 2015, p. 114) such as dividends that exceed the profits or capital reductions (Article 30 para. 1 Directive 2011/61/EU; Kramer & Recknagel, 2011, pp. 2077-2084). Similarly, the directive prohibits the acquisition of own shares (Article 30 para. 1 Directive 2011/61/EU; Kramer & Recknagel, 2011, pp. 2077-2084). The reservation must be made that this prohibition applies just two years after receipt of the control of the company (Article 30 para. 1 Directive 2011/61/EU; Kramer & Recknagel, 2011, pp. 2077-2084; Seffer & Gringel, 2014).

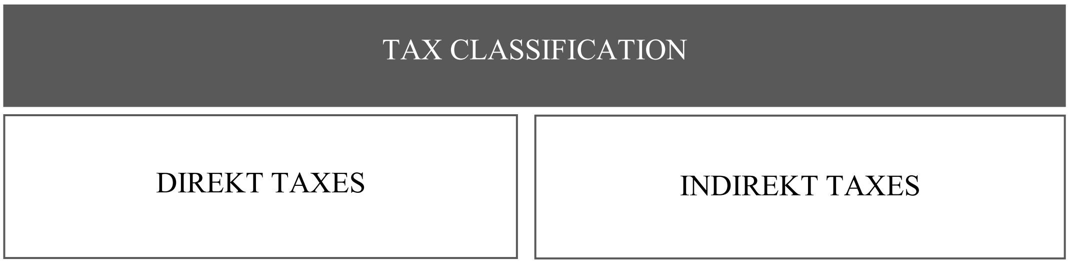
It also applies to the asset stripping that purpose entities for the acquisition and holding of real estate, and for small and medium enterprises, which are not listed, are not covered by this prohibition (Article 26 para. 2 Directive 2011/61/EU; cssf.lu, 2013; Kramer & Recknagel, 2011, pp. 2077-2084). Incidentally, it is not enough that the manager keeps those informed of such measures. Rather, the AIFM must co-operate actively to avert damage of the target company (Article 26 para. 2 Directive 2011/61/EU; cssf.lu, 2013; Kramer & Recknagel, 2011, pp. 2077-2084).

3.3 DEVELOPMENT OF TAX LAW IM THE EUROPEAN UNION

3.3.1 **Preliminary Remarks**

In order to be able to correctly put the states of Germany, Austria and Luxembourg, which are to be viewed at a later point in this work, and their regulations in regards to Private Equity in perspective after reflecting on the consequences of the AIFM Directive (Wallach, 2014, p. 96; Buck-Heeb, 2014, p. 270 recital 767), the development of the tax law in the European Union (Tumpel, 2016, p. 31; Jesgarzewski & Schmittmann, 2014, p. 27) shall be presented as well. The elaborations are aimed to make it clear, in regards to taxes as well, that in spite of great efforts on all ends, there are great difficulties to consolidate all trade routes and their side effects. The fiscal systems (Rose, 1999, pp. 32-33) in the industrialized countries (Fuest & Huber, 2003, pp. 378-390) – and this also means most of the states of the European Union (Strohmeier, 1994, p. 330) – are characterized by a large number of individual taxes (Kuhn, 2010, p. 65). One way to divide these types of taxes is to divide them into (figure 57) direct and indirect taxes (Birk, Desens, & Tappe, 2014, p. 16; Englisch, 2008, p. 559; Brauchle & Pifko, 2011, p. 215; Mick, 1995, p. 120 et seqq.). Another system is the division in taxes on income and wealth (Schneider D. , 1994, p. 87), taxes on assets (Bontrup, 2004, p. 652), taxation of goods and other services (Hahn & Kortschak, 2011, p. 1; Rose, 1997, pp. 18-19), the so-called sales, as well as taxes on production, consumption and expenditure (Fischer, Federspiel, Arnold, & Michaelis, 2012; Kreft, 2000, p. 290). In most states, the income tax and the sales tax (bmf, 2014) are of paramount (figure 58) importance (Schwinger, 1992, p. 85; Benz & Lehmbruch, 2002, p. 337 et seqq.).

Figure 57: Tax Classification in Direct and Indirect Taxes



Source: Own representation based on Englisch, 2008, p. 559.

Figure 58: Tax Importance in many European Countries

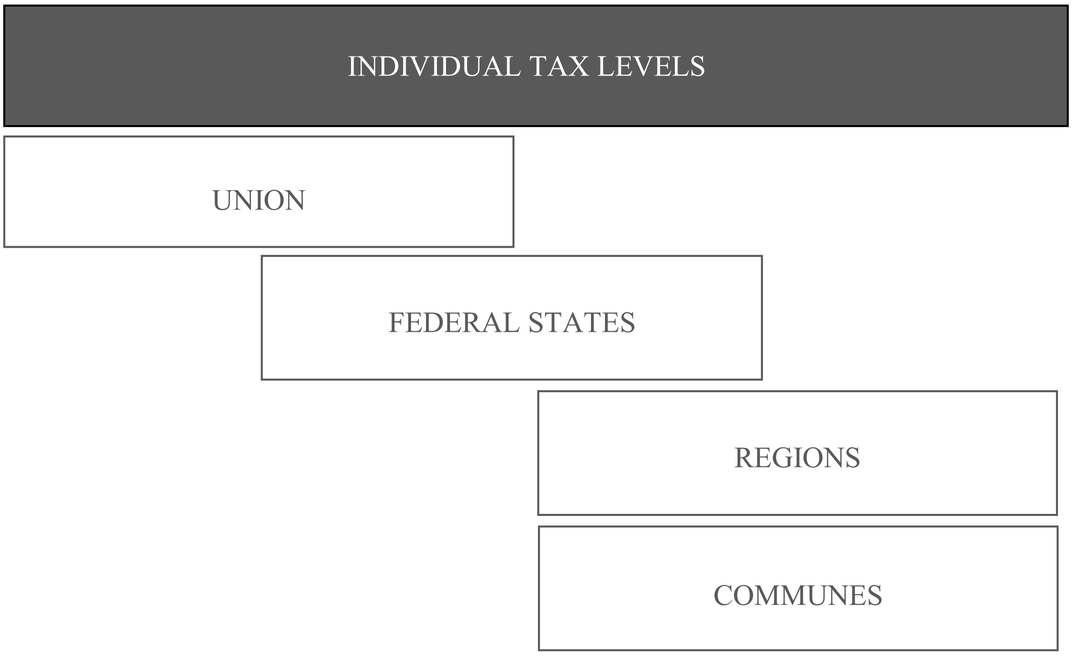
Source: Own representation.

The respective national tax laws are based on different basic legal principles (Brähler, 2014, p. 1; Scheffler, 2011, p. 201). Either they are influenced by financial constitutional laws or by the political-economic side, respectively by both of them (Seibold, 2002, p. 250). In this chapter, only those taxes are included that actually are or could be related to Private Equity. This takes into account that the Private Equity fund generally occurs initially in the form of a partnership (Hehn, Klein, Jaskiewicz, May, & von Schlippe, 2011, p. 27).

3.3.2 National Financial Constitutions

Throughout the different states of the European Union – and of course beyond – the fiscal competences are to be divided among the individual (figure 59) levels (Benz & Lehmbruch, 2002, p. 336; Förster J. , 2014, p. 3).

Figure 59: Individual Tax Levels



Source: Own representation based on Förster, 2014, p. 3.

The dispensing powers are not being equally treated in all countries of the European Union. For example, in Spain (Förster, 2014, p. 3), the regions and communes have more influence on fiscal regulations than in other states (Gabriel & Kropp, 2008, p. 587).

For the substantive tax law[13] (Dahm & Hamacher, 2014, p. 21 et seqq.; Kellersmann & Treisch, 2002, p. 131 et seqq.; Schwarz S. , 2004, p. 90 et seqq.) and tax administration, the principle of legality applies in all states, which states that taxes may be only levied (Dietrich, 2013, pp. 13-15), if they are authorized by a law (Dietrich, 2013, pp. 13-15; Förster, 2014, p. 3). In countries such as France (Hellio & Thill, 2002, p. 127 recital 402) or Belgium (Ihr Europa, 2015) and some other states, all taxes are

[13] The substantive tax law governs taxpayer, the taxable object, exemptions, tax base and tax rates of the different types of taxes (Dahm & Hamacher, 2014, p. 21 et seqq.; Kellersmann & Treisch, 2002, p. 131 et seqq.; Schwarz S. , 2004, p. 90 et seqq.).

annual taxes (Hellio & Thill, 2002, p. 127 recital 402; Förster, 2014, p. 3; Ihr Europa, 2015). Some countries regulate their taxes through ordinances (Förster, 2014, p. 3). The tax laws there only contain fiscal principles (Förster, 2014, p. 3). Of exorbitant importance in the fiscal practice is the fact that in many countries only through interpretations of these laws by tax authorities over decrees or the jurisdiction of fiscal courts a usable fiscal overview is being created (Förster, 2014, p. 3). Thus, for instance, the so-called "Private Equity Decree" of 2003 (Weißflog, 2015, p. 266; Jesch, 2004, p. 160) had a fulminant affect in Germany on the taxation of Private Equity funds and therefore widely cleared the question of how to differentiate between a business and an asset management fund vehicle (Autzen, 2005, p. 52).

3.3.3 Types of Taxes, Tax Determination and Tax Rates

3.3.3.1 Preliminary Remarks

Tax policy has to reflect the increasing financial needs (Käfer, 2015, p. 1; Schaltegger & Züricher, 2009, p. 1). In addition, the States are trying to master the national debt (Förster, 2014, p. 4) because a high national debt counteracts towards the envisaged economic growth throughout the countries and thus the European Union (Wellisch, 2000, p. 110; Wilkens, 1980, p. 171 et seqq.; Bensch, 2014, p. 1; Berschens & Grüttner, 2009, pp. 1-2; Thalemann, 2011, p. 172). The legislature is therefore forced to absorb these needs, among other things, with tax increases (Groels, 2001, pp. 34-35). On the other hand, the warranty of international competitiveness (Lachmann, 2014, p. 20; GDV, 2013, p. 1) cannot be achieved with tax increases (Förster, 2014, p. 4). Rather, this is being attempted (Allmendinger, Eichhorst, & Walwei, 2005, p. 92; Friederichs, 2012, pp. 97-98) with tax cuts (Förster, 2014, p. 4). This not only leads to more or less extensive tax reforms (Ludwig, 2011, p. 218; Arlt & Nehls, 1999, p. 292 et seqq.; Piller, 2014, p. 1; European Commission, 2015, pp. 1-130), but – as already discussed in regards to the issues for entrepreneurs at the very beginning of this study – also to frequent changes to existing or just reformed taxes (European Commission, 2015, pp. 1-130; Förster, 2014, p. 4; Ludwig, 2011, p. 218; Arlt & Nehls, 1999, p. 292 et seqq.; Piller, 2014, p. 1). Here, the concept of taxes intersperses with the definition of duties (Förster J., 2014, p. 4).

Taxes, actually though earmarked, flow into public budgets without earmarking and then are being quasi alienated for road construction (Förster, 2014, p. 4) or eco-political provisions (Daume, 2016, p. 169; Degenhart, 2015, p. 215 recital 562). The European Union lives on its cross-border trade (Europäische Union, 2015, p. 1; Die Bundesregierung, 2014, p. 1). In this context, fiscal problems have to be solved (Imhof, 2012, p. 284; Brähler, 2014, p. 96; Wehrße, 2011, p. 223), such as the avoidance of double taxation, as well as the prevention of non-taxation (Brähler, 2014, p. 96; Förster J., 2014, p. 4; Imhof, 2012, p. 284; Wehrße, 2011, p. 223).

3.3.3.2 Obligation to Submit the Tax Return

Tax payers are required to submit tax returns (Arndt, Jenzen, & Fetzer, 2016, p. 167 et seqq.; Boor, 2014, p. 42; Dittmann, Haderer, & Happe, 2015, p. 115 et seqq.; Förster J. , 2014, p. 4). In some countries, taxes are being calculated (Schäfers, 2013, p. 1) and paid by self-assessment (Förster J., 2014, p. 4; Schäfers, 2013, p. 1). In most countries, principally the due process of law (Buchwald, 2006, p. 88 et seqq.; Kaminski & Strunk, 2006, p. 47) applies in various specifications (Buchwald, 2006, p. 88 et seqq.; Förster J., 2014, p. 4; Kaminski & Strunk, 2006, p. 47). This implies that the taxation authorities – like in Germany (Förster J., 2014, p. 4) - have to determine the actual situation ex officio (Dittmann, Haderer, & Happe, 2013, p. 165).

Because of the international nature of the activities of the taxpayers, difficulties to obtain knowledge regarding certain revenue are increasing in all member states of the European Union (Förster, 2014, p. 4). This refers to income from foreign operation, investments abroad or dividends received from such (Förster J., 2014, p. 4). However, an international tendency towards an increase cooperation and mutual assistance between the tax authorities of the states (Förster H. , 2016, p. 1; Bundesministerium für Finanzen, 2014) has started to emerge, such as increased declaration and documentation obligations of taxpayers, particularly in the area of transfer pricing (Förster, 2014, p. 4). As can be observed in the Netherlands (brandeins, 2014, pp. 1-2), a trend can be observed to increasingly offer taxpayers the possibility to explicate the fiscal treatment of certain matters in advance with the tax authorities (Förster J., 2014, p. 4; brandeins, 2014, pp. 1-2).

3.3.3.3 *Income Tax in International Comparison*

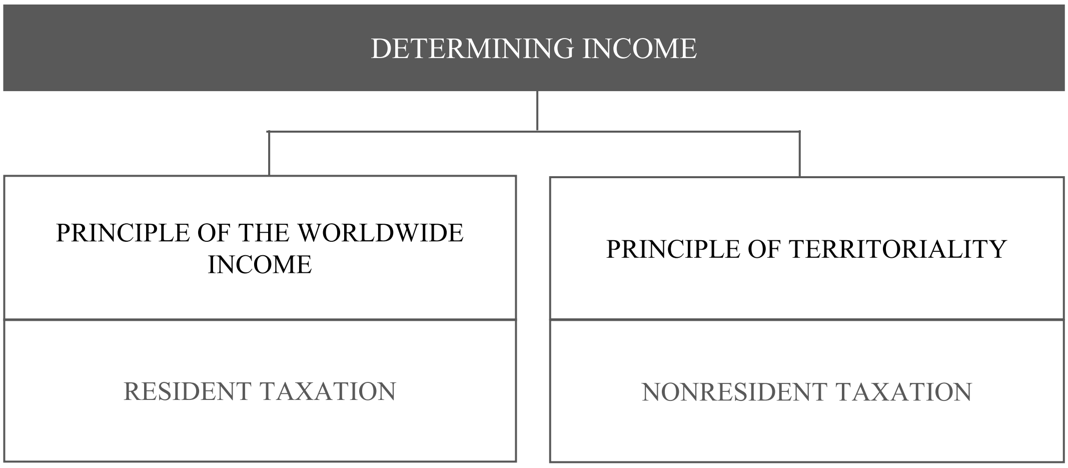
In the taxation of personal income, a certain approximation of the basic principles in international comparison (Dietl, Pauli, & Royer, 1999, p. 245) can be observed (Förster J., 2014, p. 4). The former, mainly in Romanesque States existing debt taxes, the so-called object taxes (Graf, 2005, p. 273; Wellisch & Kroschel, 2012, p. 9; Keser, 2011, p. 28) on individual income categories are indeed largely replaced by a progressive tax (Schön & Heber, 2015, p. 157 et seqq.) on total income, however, these principles have been continually modernized for some time (Förster J., 2014, p. 4; Graf, 2005, p. 273; Schön & Heber, 2015, p. 157 et seqq.; Wellisch & Kroschel, 2012, p. 9). Some states have introduced special collective agreement regulations for commercial gains, with which - as in Germany – an approximation (Richter A. , 2009, p. 18; Kaya, 2009, p. 77 et seqq.; Fischer L. , 1983, p. 77 et seqq.) of taxation of entrepreneurial activities of natural persons and corporations is sought (Fischer L., 1983, p. 77 et seqq.; Förster J., 2014, p. 5; Kaya, 2009, p. 77 et seqq.; Richter A., 2009, p. 18). In addition, there are, particularly for investment income and private capital gains (Brümmerhoff & Büttner, 2015, p. 440), special provisions (Förster J. , 2014, p. 5) for income determination and in the tariffs (Brümmerhoff & Büttner, 2015, p. 440; Förster J., 2014, p. 5).

In some countries, especially in Anglo-Saxon tax systems and in Nordic countries, the concept of income (Wehrheim, 2001, p. 15; Tumpel, 2016, p. 49; Kania, 2013, p. 29; Richter U. G., 1995, p. 254) is defined globally (Förster J., 2014, p. 5; Wehrheim, 2001, p. 15; Tumpel, 2016, p. 49; Kania, 2013, p. 29, Richter U.G., 1995, p. 254). This means that revenues are taken into account regardless of the source (Nickenig, 2015, p. 20) they are deriving from (Förster J., 2014, p. 5; Nickenig, 2015, p. 20)). This is done by identifying the main types (Gialouris, 2010, p. 83) of income (Gialouris, 2010, p. 83; Förster J., 2014, p. 5). In other states, all legally valid, thus taxable (Wünsche, 2015, p. 167; Sava, 2007, p. 5 et seqq.; Gabriel & Kropp, 2008, p. 681), types of income are listed (Dinkelbach, 2010, p. 79; Förster J.; 2014, p. 5). This fundamental difference has little meaning for the objective scope of income, merely in so far as there is no need for the global concept of income to assign each type of revenue to a particular type of income (Förster J.; 2014, p. 5). The principle of a single tax on total income with balancing positive and negative income from all sources of income within a year of assessment is in fact currently still predominant worldwide (Haase & Hofacker, 2012, p. 114; Scheffler, 2016, p. 144; Becker, Loitz, & Stein, 2009, p. 34), but is by now restricted in the majority of the countries and is becoming increasingly more limited (Becker, Loitz, & Stein, 2009, p. 34; Förster J., 2014, p. 5; Haase & Hofacker, 2012, p. 114; Scheffler, 2016, p. 144). Certain negative income is then only compensable within the same category of income (Thomas & Windhorst, 2007, p. 221; Tanski J. S., 2013, p. 43) and transferable on to past or future tax years (Förster J., 2014, p. 5; Tanski J.S., 2013, p. 43; Thomas & Windhorst, 2007, p. 221). A special role is being played by the very different treatment of tax-exempt income in the countries of the European Union, which counteracts the European equal treatment tending to converge (Förster J., 2014, p.5).

The Determination of Income

Basically, the domestic tax payer is being assessed with his domestic and foreign income (Dinkelbach, 2010, p. 10; Scheffler, 2011, p. 106; Möllenbeck, 2010, p. 125). In this, it is also spoken of the unlimited tax liability (Stober, 2007, p. 452; Jajesniak-Quast, Kiel, & Klodnicki, 2014, p. 94) – that is, the principle of global income (Förster J., 2014, p. 5; Scheffler, 2011, p. 106; Möllenbeck, 2010, p. 125; Stober, 2007, p. 452). In contrast, tax payers not residing domestically (Liebing, 2004, p. 3; Fleischer H. , 2001, p. 99 et seqq.; Schönwetter, 2009, p. 37 et seqq.) are being assessed with the statutorily recorded domestic income (Liebing, 2004, p. 3; Fleicher H., 2001, p. 99 et seqq.; Schönwetter, 2009, p. 37 et seqq.; Förster J., 2014, p. 5). This principal of territoriality leads (Lange C. , 2005, p. 83 et seqq.; Egner, 2015, p. 131 et seqq.) to a limited tax liability (Egner, 2015, p. 131 et seqq.; Förster J., 2014, p. 5; Lange C., 2005, p. 83 et seqq.). Should there be subordinate regional administration bodies (Nowotny, 1991, p. 109) levying own income taxes or surtaxes, the limited tax obligations generally apply (Förster J., 2014, p. 5; Nowotny, 1991, p. 109). For the income recognized in total income, the net principle applies (Hundsdoerfer, 2002, p. 81 et seqq.), which states that the expenses and impairment losses related to the earning of income are generally deductible (Hundsdoerfer, 2002, p. 81 et seqq.; Förster J., 2014, p.5). For the particular types of income different principles apply. This is especially true for the determination of net income of self-employed persons, the determination of income (figure 60) from employment (Förster J., 2014, pp. 5-6) and income derived from property ownership (Hey, 1998, p. 140).

Figure 60: Determining Income



Source: Own representation based on Scheffler, 2011, p. 106 et seqq.

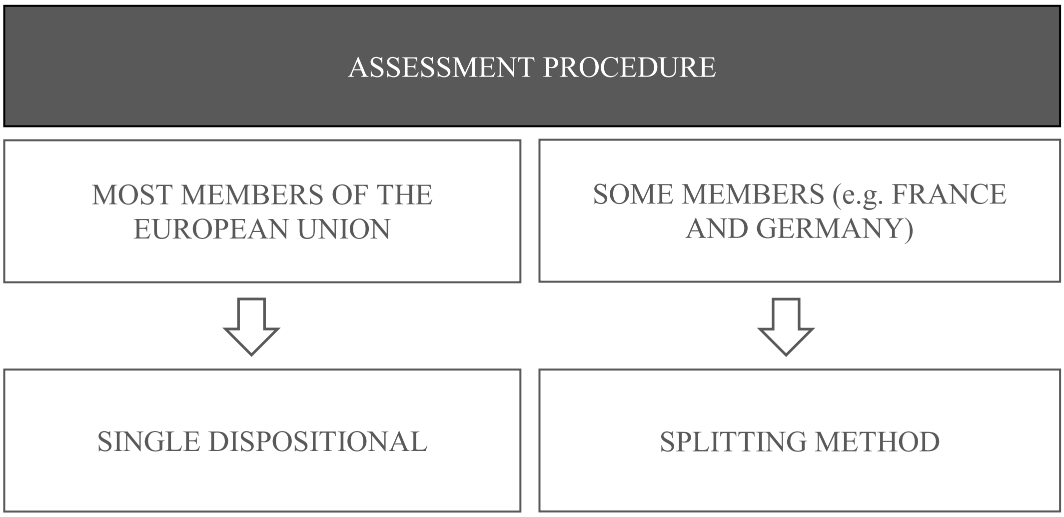
In some countries (Förster, 2014, p. 6) a deviant taxation (Kuhr, 2013, p. 66) under average rates is being applied for smaller and medium-sized commercial enterprises, especially in the agricultural sector (Wellisch & Kroschel, 2012, p. 73).

Also in some states income taxations can be observed which provide a wide variety of discounts, allowances and other reductions on income from employment and pensions and are being granted in addition to, for example, the income-related or special expenses (Brähler, 2014, p. 88 et seqq.; Scheffler, 2011, p. 218 et seqq.; Förster, 2014, p.6). Among the expenses relating to the aforementioned realized income, most states of the European Union (Frenz, 2004, p. 638 et seqq.) recognize contributions to any social insurance, whose deductibility may be limited in height depending on the characteristics and regulations of the Member State (Frenz, 2004, p. 638 et seqq.; Förster, 2014, p. 6). Interestingly, benefits from such insurances (Borrosch, 2015, p. 975) are in most cases taxable (Förster, 2014, p. 6).

To be fundamentally differed from the area of assessment of income are tax benefits relating to involuntary use of income or private provisions of the tax payer (Brähler, 2014, p. 76 et seqq.; Förster, 2014, p. 6). These expenses, in particular special expenses or exceptional debits, are taken into consideration – limited in height – or tax-free or flat-rate amounts are being granted (Scheffler, 2016, p. 127 et seqq.; Dinkelbach, 2010, p. 130 et seqq.; Förster, 2014, p. 6). Regulations regarding charitable donations (Meyn, Richter, Koss, & Gollan, 2013, p. 289 et seqq.; Walz, Auer, & Hippel, 2007, p. 188 et seqq.) are awaiting the adaptation to a respectively comparable level in the Member States of the European Union (Meyn, Richter, Koss, & Gollan, 2013, p. 289 et seqq.; Förster J.; 2014, p. 6; Walz, Auer, & Hippel, 2007, p. 188 et seqq.). Throughout the majority of the countries, the deduction of special expenses and exceptional debits (Dinkelbach, 2014, p. 187 et seqq.; Förster, 2014, p. 6) occurs from the total amount of income (Jannott & Frodermann, 2005, p. 515 et seqq.). Some states have begun to grant these discounts as deductions from the amount of tax in order to prevent the progression effect (Heuer, 2008, p. 274) of the income tax rate (Scheffler, 2011, p. 186; Förster, 2014, p. 6; Heuer, 2008, p. 274).

Also the financial burdens resulting from family, thus marriage or existing children (Richter & Hurrelmann, 2009, p. 224 et seqq.), are being taken into account under very different principles (Richter & Hurrelmann, 2009, p. 224 et seqq.; Förster, 2014, p.6). In most states the principle of individual person taxation applies as well to parents and children (Plenker, 2016, p. 345; Förster, 2014, p. 6). In those countries where married couples are being assessed jointly, the splitting (figure 61) method (Scheffler, 2009, p. 101 et seqq.) is being applied (Förster, 2014, p. 6; Scheffler, 2009, p. 101 et seqq.). This describes the method (Nowotny, 1999, p. 325) serving to determine the income tax of common households, thus especially families (Nowotny, 1999, p. 325; Förster, 2014, p. 6). The principle of who earns a lot may also dispense with a larger portion of his income, while the ability-to-pay principle (Coimbra, 2015, p. 101 et seqq.; Weber-Grellet, 2001), loses in justness on closer inspection of the family (Coimbra, 2015, p. 101 et seqq.; Förster, 2014, p. 6). The income of the primary earner is optionally distributed to the members of the family (Gerlach, 2004, p. 327). Thus the performance of this community is limited. This disadvantage shall largely be offset by the splitting method (Scheffler, 2012, p. 174).

Figure 61: Assessment Procedure



Source: Own representation.

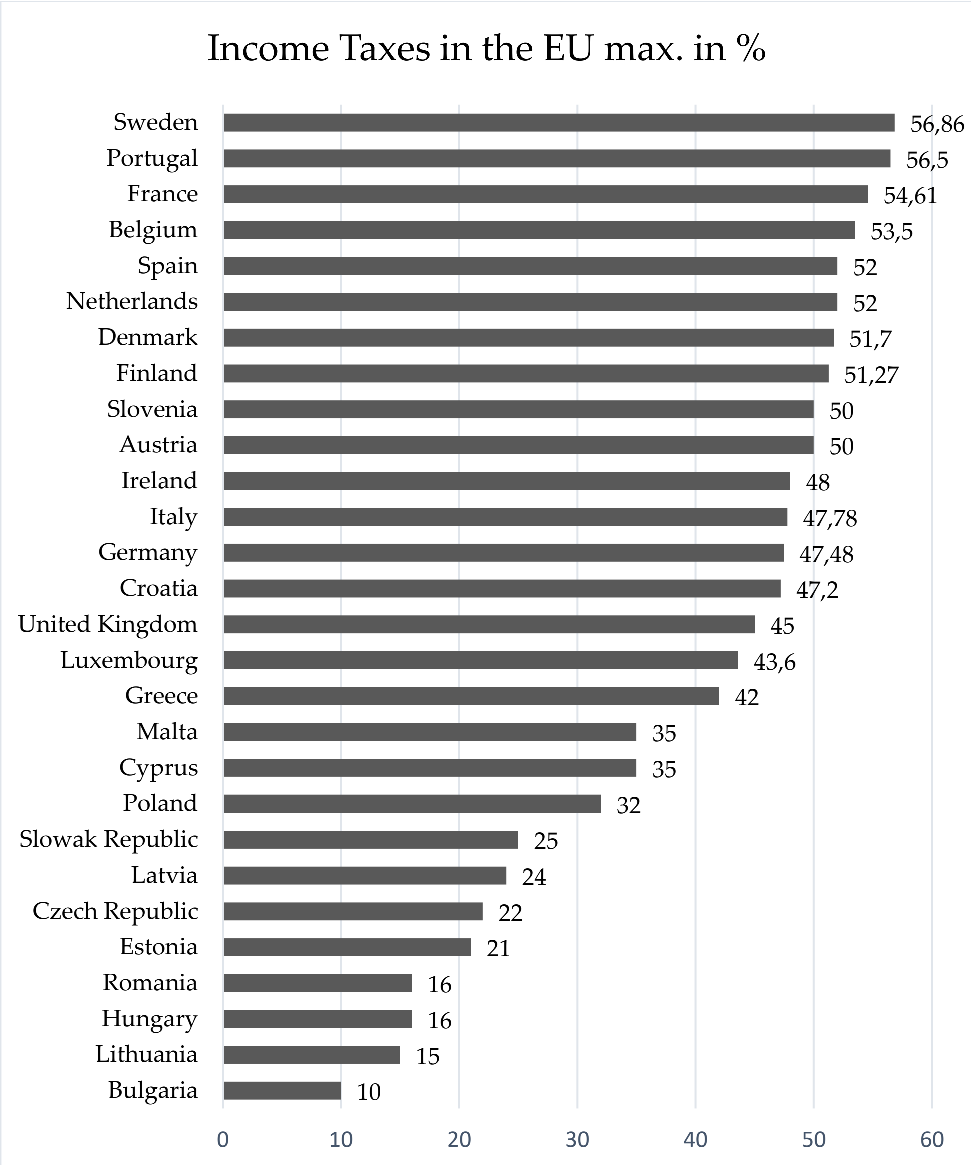
In most countries, the financial burdens resulting from family or other support payments are being considered as tax exempt amounts, so-called zone zero in rates or deductions from the tax amount, if the dependents have little or no income (Bundesfinanzministerium, 2015, pp. 1-60; Förster, 2014, p. 6). An exception is the child benefit, which is not taken into account (Bundesfinanzministerium, 2015, pp. 1-60; Förster, 2014, p. 6).

Income Tax Scale Organization of the States

In almost all countries, rates with an open subset graduation (Lieb, 1992, p. 121 et seqq.) apply for income taxes (Lieb, 1992, p. 121 et seqq.; Förster, 2014, p. 7). Progressive formula tariffs (Grossekettler, 2012, p. 678) as in Germany are rather rare (Förster, 2014, p. 7; Grossekettler, 2012, p. 678). The course of progression of the rates is greatly simplified in the majority of the countries in recent years, the subsets are significantly reduced and the peak rate is being lowered (Förster, 2014, p. 7).

The income taxes (figure 62) or surtaxes of subordinate regional administration bodies are usually based on proportional rates (Reif, 2005, p. 102 et seqq.; Förster J. , 2014, p. 7). The data (Denis, Hemmelgarn, & Sloan, 2015, pp. 1-154) are from the statistical utility Eurostat of the European Union of 2015 along with recorded numbers up until 2013 from the Federal Ministry (Bundesfinanzministerium, 2015, p. 34) of Finance (Bundesfinanzministerium).

Figure 62: Income Taxes in the European Union in %



Source: Own representation based on Bundesfinanzministerium, 2015, p. 34.

In countries such as Belgium, France or Great Britain, but also in Switzerland, special statutory provisions apply, under which an annual adjustment of certain tax elements to the development of consumer prices must be made (Förster, 2014, p. 7). This affects (Förster, 2014, p. 7) mainly those countries with progressive subset rates (wko, 2015, p. 1).

3.3.3.4 Corporate Income Tax in International Comparison

The corporate income tax as a business tax (Schreiber, 2012, p. 77 et seqq.; Stiehler, 2009, p. 18 et seqq.; Thomsen, 2009, p. 316 et seqq.) is far from being uniform throughout Europe, respectively the European Union (Bundesfinanzministerium, 2015, pp. 1-60; Förster, 2014, p. 7). In some countries, such as Spain (Justlanded, 2016, p. 1), actually private companies are considered under corporate income tax (Höhn & Höring, 2010, p. 239 et seqq.; Förster, 2014, p. 7; Justlanded, 2016, p. 1). Particular problems are especially economic double taxation through multiple taxation (Rehm & Nagler, 2013, p. 250 et seqq.) of distributed profits and the taxation of internationally intertwined corporations (Förster, 2014, p. 7; Rehm & Nagler, 2013, p. 250 et seqq.). In almost all states of the European Union, a governmental corporate income tax (Koch R. , 2010, p. 83; Bohn, 2009, p. 28) is imposed on the total income of corporations and other legal entities, partnerships and assets (Bohn, 2009, p. 28; Förster, 2014, p. 7; Koch R., 2010, p. 83). Corporate income tax (Senger, 2009, p. 86 et seqq.) and other surcharges are levied in some states at the level of subordinate local administrative bodies (Bundesfinanzministerium, 2015, p. 1-60; Förster, 2014, p. 7; Senger, 2009, p. 86). For the general scope of the objective tax liability, the principle of world income (Jacobs, 2011, p. 139; Lettmann, 1997, p. 388 et seqq.; Rek, Brück, Labermeier, & Pache, 2008, p. 145) and the territoriality usually applies (Jacobs, 2011, p. 138, Lettmann, 1997, p. 388 et seqq.; Förster, 2014, p. 8). This usually does not deviate from the principles of income tax (Förster, 2014, p. 7; Rek, Brück, Labermeier, & Pache, 2008, p. 145).

Determination of taxable Earnings

The principles of determining taxable earnings are generally based on the balance sheet comparison, partly flanked by the relevance of the trade balance with the profit and loss account (Dahlke, 2011, p. 145; Bambynek, 2011, p. 84; Peyerl, 2015, p. 38 et seqq.) based on commercial law (Dahlke, 2011, p. 145; Förster, 2014, p. 8; Bambynek, 2011, p. 84; Peyerl, 2015, p. 38 et seqq.). The fiscal special provisions, particularly in the areas of depreciation (Kuhr, 2013, p. 230 et seqq.), valuation of current assets (Lettmann, 1997, p. 126 et seqq.), investment incentives, reserves, recognition and assessment of provisions, hidden profit distributions, are in varying degree partially included in the laws, in part to be taken from the decrees of the tax authorities or the adjudication (Förster, 2014, p. 8; Kuhr, 2013, p. 230 et seqq.; Lettmann, 1997, p. 126 et seqq.). They apply equally, apart from the legal provisions and business processes only applicable for corporations, to sole proprietors and partnerships which keep or aare being required to keep accounts and are anchored in the income tax laws (Hausen, 2009, p. 394) in most states (Hausen, 2009, p. 394; Förster, 2014, p. 8).

The principle of accounting continuity (Steinbach A. , 1973, p. 69; Lutter, 2006, p. 177) applies practically everywhere (Förster, 2014, p. 8; Steinbach A., 1973, p. 69; Lutter, 2006, p. 177). It signifies (Vollmuth, 2009, p. 76 et seqq.; Hirschler, 2012, p. 53 et seqq.; Hilke, 1985, p. 32 et seqq.) that several chronologically successive annual financial statements of a company must have both the same structuring, the so-called formal accounting continuity – as well as they should follow similar valuations principles as much as possible – the so-called material accounting continuity (Förster, 2014, p. 8; Vollmuth, 2009, p. 76 et seqq.; Hirschler, 2012, p. 53 et seqq.; Hilke, 1985, p. 32 et seqq.). With regard to the depreciation (Schön & Osterloh-Konrad, 2010, p. 68 et seqq.), in most states, the linear or diminishing-balance method with specific annual rates by groups of assets is being applied (Förster, 2014, p. 8; Hellio & Thill, 2002, p. 98 et seqq.; Schön & Osterloh-Konrad, 2010, p. 68 et seqq.). In the Nordic countries, collective depreciation (Beeck, et al., 2004, p. 568; Leibfritz & Meurer, 1985, p. 54) is usually permitted and common (Beeck, et al., 2004, p. 568; Leibritz & Meurer, 1985, p. 54; Förster, 2014, p. 8).

Although some countries process profits gained in times of inflation according to the nominal value principle – thus, that for all fund the numerical value is relevant and that the tax due is just this money debt (Wolfersdorff, 2014, p. 63 et seqq.; Scheffler, 2014, p. 57 et seqq.) – this principle, however, is being modified through revaluation coefficients, especially in the determination of capital gains (Förster, 2014, p. 8; Reichmann, 2011, p. 104 et seqq.; Wolfersdorff, 2014, p. 63 et seqq.; Scheffler, 2014, p. 57 et seqq.).

General investment incentives (Birke, 2012, p. 44 et seqq.; Mroczek, Schuttenbach, & Ciurla, 2000, p. 300 et seqq.) exist in many countries in different forms (Förster, 2014, p. 8; Birke, 2012, p. 44 et seqq.; Mroczek, Schuttenbach, & Ciurla, 2000, p. 300 et seqq.). In particular, special depreciation (Wünsche S. , 2011, p. 169 et seqq.; Spengel, 2009, p. 69 et seqq.) and investment tax allowances (Wünsche S., 2011, p. 169 et seqq.; Spengel, 2009, 2009, p. 69 et seqq.; Förster, 2014, p. 8). In most countries, this investment incentive is not generally applicable, but coordinated with certain issues (Hörmann, Haslinger, & Hirschler, 2013, p. 91 et seqq.; Altenburger, Janschek, & Müller, 1999, p. 49 et seqq.) such as research funding (Hörmann, Haslinger, & Hirschler, 2013, p. 91 et seqq.; Altenburger, Janschek, & Müller, 1999, p. 49 et seqq.; Förster, 2014, p. 8). Another form of funding in the meaning of special depreciation or investment allowances also relates to the entrepreneurs (Zeh & Schnell, 2008, p. 99 et seqq.). This funding is usually limited in time or ceases as soon as the company has reached a certain size (Easson, 2004, p. 211; Haufe, 2016; Goldstein, 2016, p. 248).

Systems of Corporate Taxation

The corporate income tax (Kraft & Kraft, 2014, p. 143 et seqq.) includes the total income of corporations with a uniform tariff without distinction of reserved and distributed profits (Scheffler, 2016, p. 195 et seqq.; Kraft& Kraft, 2014, p. 143 et seqq.; Förster, 2014, p. 9). In some countries, this system is connected with very different principles of reduction or avoidance of economic double taxation (Haase, 2014, p. 14 et seqq.; Schüller, 2014, p. 151 et seqq.) with dividends distributed to the shareholders (Brähler, 2014, p. 16; Haase, 2014, p. 14 et seqq.; Förster, 2014, p. 8; Schüller, 2014, p. 151 et seqq.).

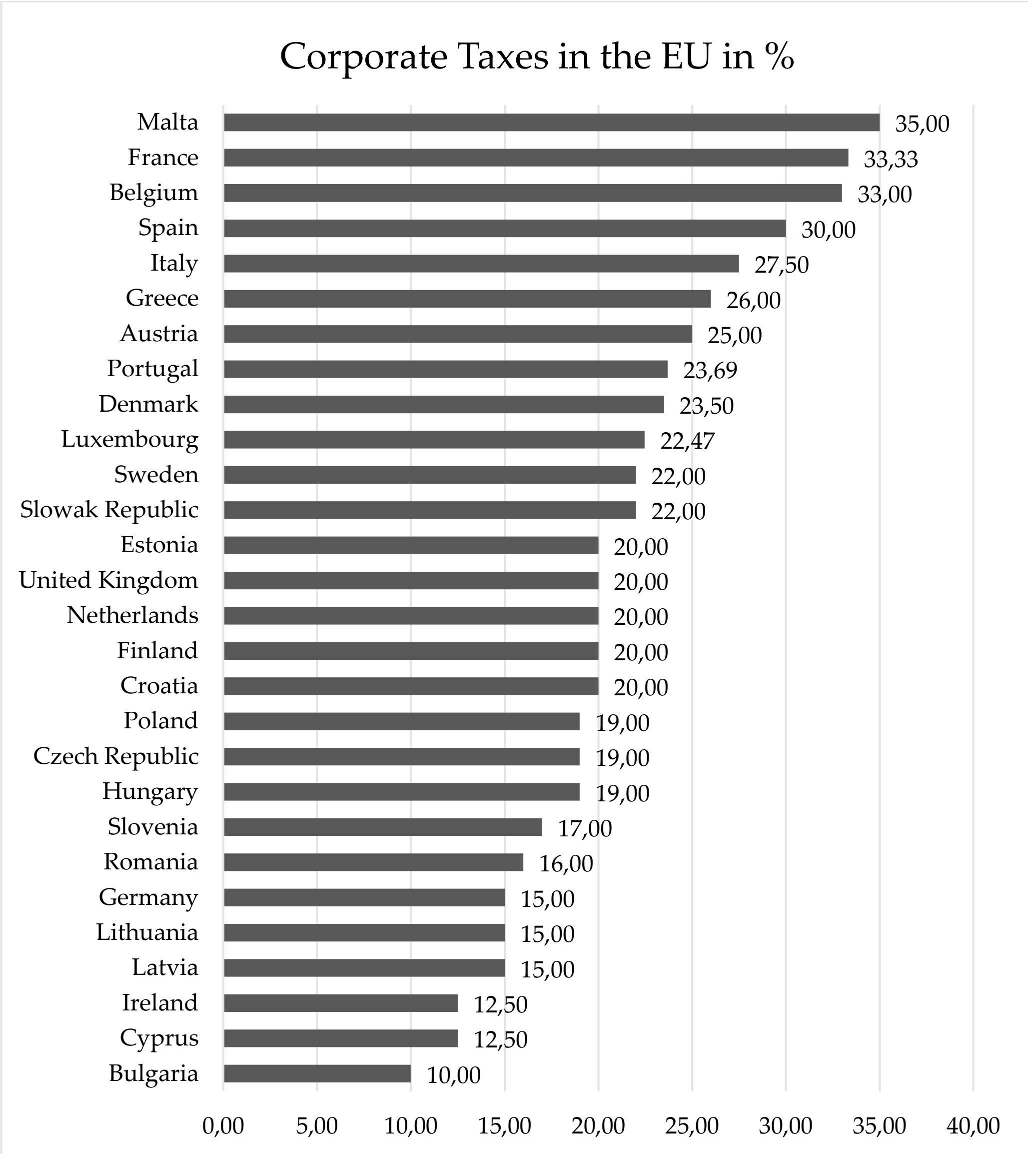
Some of these distributions are not included in part or in their entirety in determining the income (Kellersmann & Treisch, 2002, p. 112) of the shareholder (Kellersmann & Treisch, 2002, p. 112; Förster, 2014, p. 9). In part, there is a tax-credit for the shareholder on the corporation tax raised on the dividend, in part a partial offset of the corporation tax raised on the income from investments is granted (Kraft & Kraft, 2014, p. 143; Förster, 2014, p. 8). In some countries, a reduced tax rate (Stellpflug, 2001, p. 38 et seqq.) is applied on dividends distributed to domestic income tax payers (Förster, 2014, p. 9; Stellpflug, 2001, p. 38 et seqq.).

In order to prevent a multiple taxation of dividends (Schön, Schreiber, & Spengel, 2008, p. 55 et seqq.) between domestic corporations, it is partially necessary in the sense of the international intercorporate privilege (Brähler, 2012, p. 366 et seqq.) to keep minimum shares or to hold these shares over a certain period of time (Förster, 2014, p. 9; Schön, Schreiber, & Spengel, 2008, p. 55 et seqq.; Brähler, 2012, p. 366 et seqq.). This also applies to distributions from foreign affiliates to domestic parent companies (Förster, 2014, p. 9; Schön, Schreiber, & Spengel, 2008, p. 55 et seqq.; Brähler, 2012, p. 366 et seqq.). In some countries, there are certain, also quite conceivable for Private Equity structures, forms of unitary taxation for corporations depending on the scope, duration and type of investments (Schneider, 1994, p. 178; Förster, 2014, p. 9). These forms differ in so far as that partially the results, as it is in France, are being consolidated and in part the losses can be transferred through tax-effective contributions from affiliated partners, such as it is practiced in Sweden, or through intercompany assets, such as in the Netherlands (Satzger, 1999, p. 83 et seqq.), without fiscal consequences (Satzger, 1999, p. 83 et seqq.; Förster, 2014, p. 10).

Tariff Arrangement of Corporation Tax of the Countries

In general, proportional rates (Brähler, 2009, p. 60 et seqq.) apply for corporate income tax (Brähler, 2009, p, 60 et seqq.; Förster, 2014, p. 10). Only some states manage to work with reduced (Strassburger, 2012, p. 162 et seqq.; Blaschke, 2008, p. 41 et seqq.) tax rates (Förster, 2014, p. 10; Strassburger, 2012, p. 162 et seqq.; Blaschke, 2008, p. 41 et seqq.). As an example, Switzerland is to be cited as a country that is not a Member of the European Union (swissinfo, 2007), but has quite a significant impact in regards to the financial market. There, most cantons levy corporate tax (Bohley, 2003, p. 322; Nowotny, 1987, p. 168) at a progressive rate (Bohley, 2003, p. 322; Nowotny, 1987, p. 168; Förster, 2014, p. 10). In many states it was attempted to strengthen the competitiveness of domestic enterprises by means of an often significantly reduced (OECD, 2015, p. 103; Richter S. , 2011, p. 83) corporate income (figure 63) tax (Richter S., 2011, p. 83; Förster, 2014, p. 10).

Figure 63: Corporate Income Taxes EU Standard Rates in %



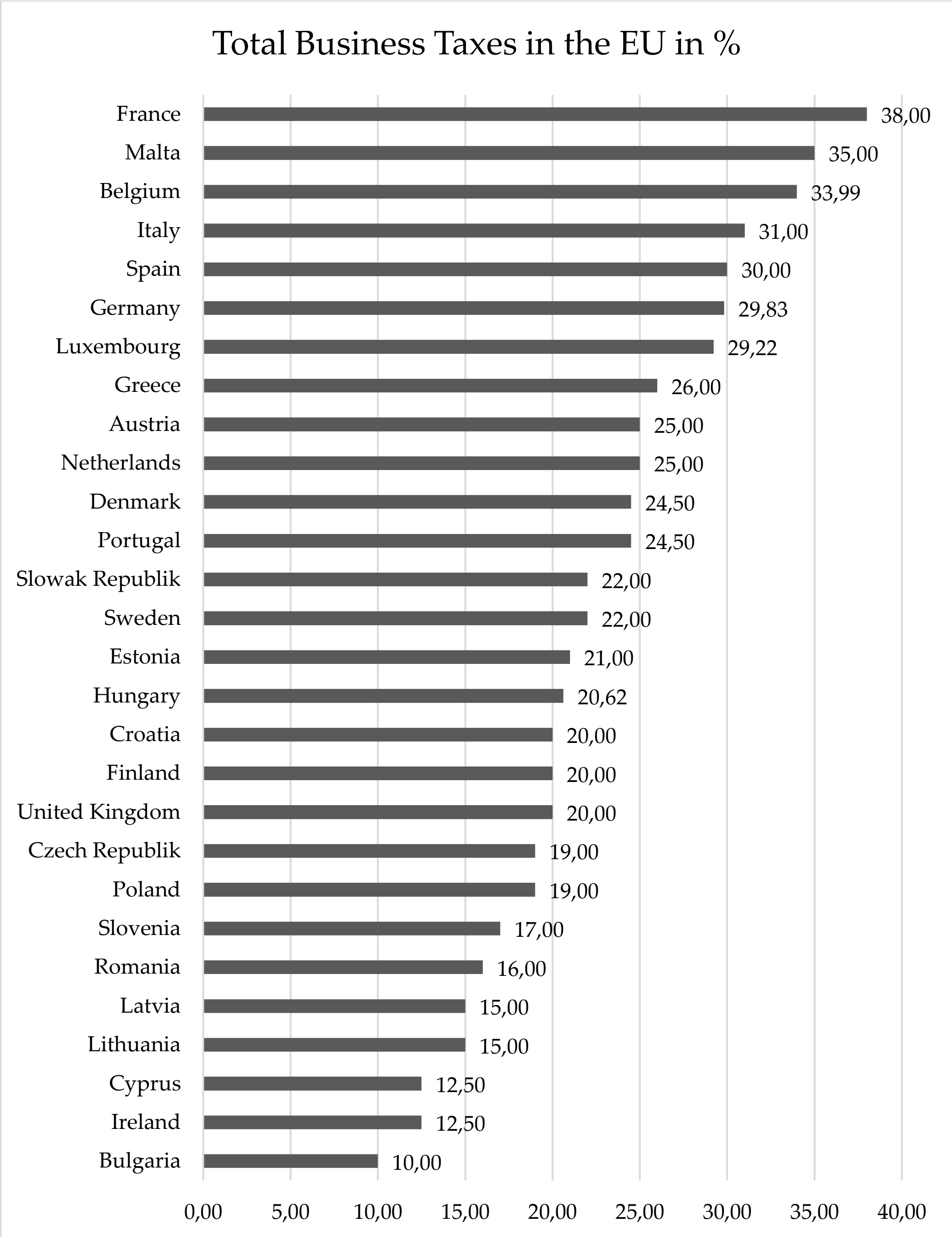
Source: Own representation based on Bundesfinanzministerium, 2015, p. 16.

3.3.3.5 Business Tax in International Comparison

Business taxes or similar taxes with different tax bases are still raised in several States of the European Union (Ruf M. , 2007, p. 159 et seqq.; Kudert, Jamrozy, & Glowienka, 2013, p. 408 et seqq.) for businesses and individual entrepreneurs today (Förster, 2014, p. 10; Ruf M.; 2007, p. 159; Kudert, Jamrozy & Glowienka, 2013, p. 408 et seqq.). They are considered one of the main sources of income (Nentwig & Werwath, 2016, p. 287 et seqq.; Meffert & Müller, 2008, p. 218) for local authorities (Nentwig & Werwath, 2016, p. 287 et seqq.; Meffert & Müller, 2008, p. 218; Förster, 2014, p. 10). The business tax in the German form is an international exception, even though many other countries with a federal structure – see figure Individual Tax Levels – provide similar taxes for businesses. As an example, the current circumstances in regards to the business tax (figure 64) of the countries of Germany, Austria and Luxembourg, which are being examined in this paper, as well as France, Spain, Italy and Switzerland are being described (Meister, 2015, pp. 106-109).

- Germany: the business tax is levied as trade income tax on the object profitability of a business enterprise in the amount of at least 7% of the revenue (Richter, 2008, pp. 93-104; Schmidt, Sigloch, & Henselmann, 2005, p. 201 et seqq.).
- Austria: The business tax was abolished in 1994 in favor of a municipal tax of 3% on the payroll (Dölker, 2012, p. 254; Madl, 2014, p. 71).
- Luxembourg: The business tax - impôt commercial – is similar to the Germany business tax and is also determined with a municipal rate fixed by the municipality (Höhn & Höring, 2010, pp. 168-169; Luxembourg Consulting Group, 2015).
- France: The imposed business tax, as taxe professionelle, is independent of the revenue (Huth A. H.-J., 1996, pp. 183-187; Cross Border Business Lawyers, 2015).
- Spain: The business tax – impuesto sobre actividades economicas – is a tax of the municipalities and independent of the revenue as well. However, and this could be of importance for start-up entrepreneurs whose net sales do not exceed 1 million Euro, it is exempted (Plattes, Fauteck, Strunk, & Fitzner, 2013, pp. 131-134) from tax (articulo 82 del Texto refundido de la Ley Reguladora de las Haciendas Locales).

Figure 64: Total Business Taxes in the EU in %



Source: Own representation based on Bundesfinanzministerium, 2015, p. 18.

- Italy: Here, a regional tax – imposta regionale sulle attività produttive – is being imposed, with which the creation of value is being taxed (Großmann, 2010, pp. 1-27; Hilpold, 1999, p. 264).
- Switzerland: With the exception of the cantonal regulated business tax, the Swiss do not impose business tax (iww, 2014; Hofert, 2012, p. 44 et seqq.).

3.3.3.6 Turnover Tax in International Comparison

With the turnover taxes, the value-added tax (VAT) in form of the all-phase net turnover tax (Birk, Desens, & Tappe, 2014, p. 474 et seqq.; Bühler, Loosli, Lüthi, & Pifko, 2008, p. 11 et seqq.) with input tax reduction has established itself in the European Union (Förster, 2014, p. 11; Birk, Desens, & Tappe, 2014, p. 474 et seqq.; Bühler, Loosli, Lüthi, & Pifko, 2008, p. 11 et seqq.). The standard rates and possible special rates of the value-added taxes, however, significantly differ from each other in some cases in European comparison (Seubert & Neureiter, 2010, pp. 1-48; Diemer, et al., 2016, p. 453 et seqq.). Thus, the Member States can be divided into different groups (figure 65).

Figure 65: Groups of Countries class-divided – Value-Added Tax

VALUE-ADDED TAX – COUNTRIES WITH		
flat tax rate,	reduced tax rate for certain goods and services beside the standard rate,	generally reduced and in-creased tax rate.

Source: Own representation based on Förster, 2014, p. 11.

The types and the extent of special regulations for certain business sectors or certain goods and services are still somewhat different in international comparison (Förster, 2014, p. 11). As for the tax liability, the tax base, the place of performance and the input tax refund is concerned, it is not least due to the value-added tax system policy, that an approximate harmonization has been achieved (Weimann, 2012, pp. 15-18; Sopp, 2010, p. 58 et seqq.) within the European Union (Förster, 2014, p. 11; Weimann, 2012, pp. 15-18).

The multitude of other taxes, such as alcohol and tobacco tax, insurance tax, environmental tax, inheritance and gift tax, etc. shall not be considered since they bear absolutely no relation to Private Equity or its operators. It should also be mentioned that in the wake of the financial crisis, the financial transaction tax was introduced in part (Port & Steinlein, 2015, p. 189). In other countries, the implementation of the same was being planned or discussed (Oppitz & Weigele, 2014, p. 153; FAZ, 2014). For instance, there was a proposal for a Directive of the European Commission dated February 14, 2013, which provided for establishing a common financial transaction tax system (Dengl, 2013, p. 1) in the context of enhanced cooperation (Dengl, 2013, p. 1; Förster, 2014, p. 11).

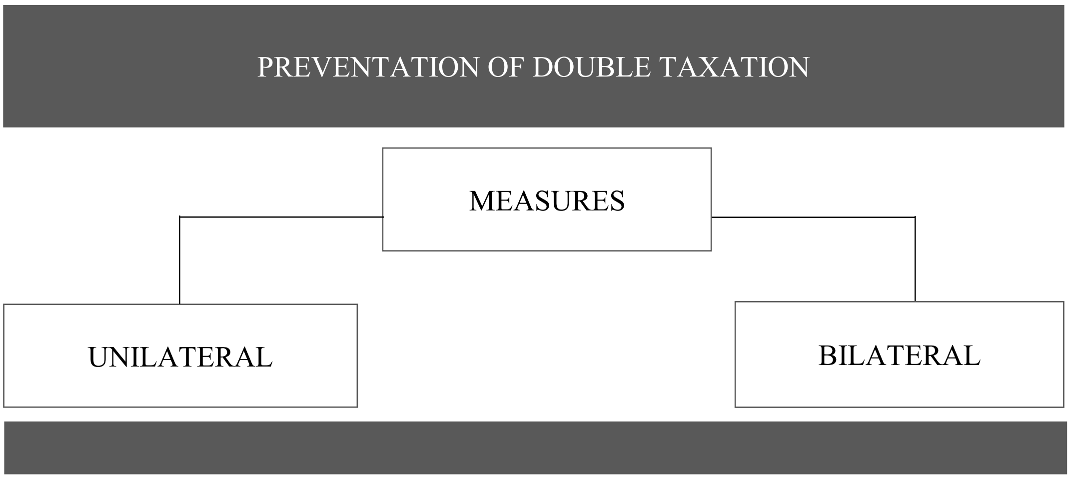
3.3.4 International Double Taxation – Background and Issues

If the same income or the same assets of the same person is taxed by at least two states it results in an international double taxation (Brähler, 2014, p 17; Haase, 2014, p. 16; Förster, 2014, p. 13). This triggered (Bredow, 2011, p. 96 et seqq.; Mach, 2008, p. 121 et seqq.) by the fact that the subjective tax liability in regards to direct taxes – that is, inter alia, the personal and corporate income taxes – is characterized by the two basic principles of the world's income and territoriality (Förster, 2014, p. 13; Bredow, 2011, p. 96 et seqq.; Mach, 2008, p. 121 et seqq.). The access to the taxes of its domestic natural and legal persons by the state does not only apply in regards to the domestic, but also in regards to foreign income and assets (Birk, Desens, & Tappe, 2014, p. 217; Förster, 2014, p. 13). This marks the initially mentioned unlimited tax liability (Birk, Desens, & Tappe, 2014, p. 217; Förster, 2014, p. 13). Non-domestic residents, however, are taxed only on the domestic income and the assets – the limited tax liability (Egner, 2015, p. 131; Birk, Desens, & Tappe, 2014, pp. 217-218; Förster, 2014, p. 13). Basically – there are special regulations, which are extensive and complicated in detail – the above principles apply to all States of the European Union (Rasmussen, Mogens, 2011, pp. 1-11). Thus, in these following cases, double taxations in the above-described sense arise (Förster, 2014, p. 13):

a. Two states compete in the wake of unlimited tax liability over the taxes on the same income of a tax payer (Wuntsch & Bach, 2012, p. 145), or
b. an unlimited and at the same time limited tax obligation of a tax payer is at hand (Brähler, 2014, p. 19 et seqq.),
c. or a limited tax obligation in more than one state applies (Brähler, 2014, p. 19 et seqq.).

In order to prevent (figure 66) or mitigate double taxation, agreements were created (Brähler, 2014, p. 96; Förster, 2014, p. 13; Schmidt, Sigloch, & Henselmann, 2005, p. 263 et seqq.). Thus the measures regarding double taxation are distinguished as follows (Brähler, 2014, p. 22):

Figure 66: Measures to avoid Double Taxation



Source: Own representation based on Brähler, 2014, p. 22.

Unilateral measures

National legislations to avoid international double taxations (Bundesfinanzministerium, 2015; Merten, 2012, p. 41 et seqq.) are in existence almost worldwide (Brähler, 2014, p. 96). This leads to the following activities (Förster, 2014, p. 14):

- Exemption of foreign income (Brähler & Lösel, 2008, p. 329).
- Foreign tax credit (Frotscher, Lüdicke, & Hummel, 2013, p. 122).
- Crediting of a fictitious (Günter & Geiß, 2010, p. 120) foreign tax (investment incentives).
- Deduction of foreign taxes on the determination of income (Haase, 2012, p. 1360).
- Reduction of domestic taxes (Egner, 2015; p. 15).

In many cases, double taxations (Bergemann & Wingler, 2012, p. 325) are only being reduced by these measures and not completely prevented, as these measures are often not able to compensate for the entire foreign tax burden (Bergemann & Wingler, 2012, p. 325; Förster, 2014, p. 14). Due to this bias and the lack of coordination (Brähler, 2014, pp. 21-22), the results are unsatisfactory (Brähler, 2014, pp. 21-22; Förster, 2014, p. 14).

Bilateral measures

While the previous little paragraph was about unilateral, thus one-sided national, measures, bilateral agreements refer to measures agreed upon by two countries together (Rose, 1982, p. 73 et seqq.; Gaida, Hille, & Mendl, 2001, p. 149 et seqq.; Tippelhofer, 2013, p. 1 et seqq.). These agreements have a greater effect because they conduct an allocation of taxing rights of the contracting states under certain objective criteria (Förster, 2014, p. 14). Through this international contractual limitation of national taxation law, a double taxation may already be prevented (Förster, 2014, p. 14). Double taxation only will come about, if the Double Taxation Agreement (DTA) assigns the right of taxation to both states (Förster, 2014, p. 14). This is the case for dividend income (Trennheuser, 2014, p. 159 et seqq.; Läufer, 2014, p. 23 et seqq.) in which the State of Residence shall have the right to impose taxes, while the state of source, however, is entitled to levy a withholding tax (Trennheuser, 2014, p. 159 et seqq.; Läufer, 2014, p. 23 et seqq.; Förster, 2014, p. 14). But even in these cases, the DTA has included regulations to avoid such double taxations (Förster, 2014, p. 15). Either the tax levied will be credited in the other state or the foreign income will be exempted with progression (Knobbe-Keuk, 1993,

p. 321 et seqq.) by one of the states involved (Förster, 2014, p. 15; Knobbe-Keuk, 1993, p. 321. et seqq.).

The international double taxation (Scholz S. , 2006, p. 58 et seqq.) is an international problem that called for appropriate action at an early stage (Schmidt, Sigloch, & Henselmann, 2005, p. 265 et seqq.; Schüller, 2014, p. 109; Förster, 2014, p. 15; Scholz S., 2006, p. 58 et seqq.). Example solutions for bilateral contracts were prepared. The most significant model convention is the OECD Model Convention of 1977 in the amendment of 2010 (Schüller, 2014, p. 106; Förster, 2014, p. 15). The European Union (European Commission, 2015) has, as opposed to the other world market, the USA, no own model (European Commission, 2015; Förster, 2014, p. 15). The Treaty on the Functioning of the European Union (TFEU (AEUV – Vertrag über die Arbeitsweise der Europäischen Union)) no longer provides for multilateral agreements (Haase, 2014, p. 402; Europäische Union, 2012) between Member States (Haase, 2014, p. 402; Förster, 2014, p. 16).

3.3.5 **Harmonization Measures of the European Union**

3.3.5.1 Preliminary remarks

The already-discussed development of the tax law shows, that even without explicit harmonization measures (Ritter, 1991, p. 11 et seqq.; Eiling, 2014, p. 25 et seqq.) – despite some major differences – an approximation of national fiscal regulations has been achieved (Förster, 2014, p. 17; Ritter, p. 11 et seqq.; Eiling, 2014, p. 25 et seqq.). It is, as already initially stated in this document, of sublime importance that the diverse views of cross-borders activities in the European Union need to be overcome on the fiscal side as well. Neumair, Schlesinger and Haas speak of, as noted during the introduction, the outstanding target to establish (Neumair, Schlesinger, & Haas, 2012, p. 460) a single European market meaning the free movement of goods, persons, services and capital (Liebert & Wolff, 2015, p. 178 et seqq.; Liebmann, 2015, p. 93) in conformity with the regulations of article 26, para. 2 TFEU (Neumair, Schlesinger, & Haas, 2012, p. 460; Förster, 2014, p. 17; Liebert & Wolff, 2015, p. 178 et seqq.; Liebmann, 2015, p. 93). Now, it is very easy to see that different taxation, or different treatment of vehicles or the taxation of such vehicles as it yet has to be the mandatory case with Private Equity Funds due to the intrinsically nation-state practices, opposes this request or rather this requirement. However, it remains unrevealed to the viewer why this contract only treats provisions of a fiscal nature (Niedobitek, 2014, p. 213) in an inadequate manner (Niedobitek, 2014, p. 213; Förster, 2014, p. 17).

3.3.5.2 Tax Harmonization: Impact on Private Equity Investments

Art. 113 TFEU (Arndt, Fetzer, & Fischer, 2015, p. 211; Frenz, 2011, p. 922 et seqq.; Lipp, 2014, p. 24 et seqq.) may well be described as the most important regulation in terms of the harmonization imperative (Arndt, Fetzer, & Fischer, 2015, p. 211; Förster, 2014, p. 17; Frenz, 2011, p. 922 et seqq.; Lipp, 2014, p. 24 et seqq.). It applies especially for the sales tax, excise duties (Streinz, 2016, p. 337) and other indirect taxes (Förster, 2014, p. 17; Frenz, 2011, p. 922 et seqq.; Streinz, 2016, p. 337). The agreement covers such content to the extent that such harmonization is necessary for the formation and the effective operation of the internal market and to avoid distortions of competition (Arndt, Fetzer, & Fischer, 2015, p. 211; Förster, 2014, p. 17; Frenz, 2011, p. 922 et seqq.; Lipp, 2014, p. 24 et seqq.). The tax harmonization mandate therefore relates only to those taxes levied on the price for goods and services in accordance with their statutory purpose (Arndt, Fetzer, & Fischer, 2015, p. 211; Förster, 2014, p. 17; Frenz, 2011, p. 922 et seqq.; Lipp, 2014, p. 24 et seqq.). As a result, a direct and immediate distortion of competition is created (Arndt, Fetzer, & Fischer, 2015, p. 211; Förster, 2014, p. 17; Frenz, 2011, p. 922 et seqq.; Lipp, 2014, p. 24 et seqq.). What the European Union committed itself to, namely the free movement of goods, the free movement of services and the free movement of capital with in the Union (Mick, 1995, pp. 129-132), is hardly supported or encouraged by this.

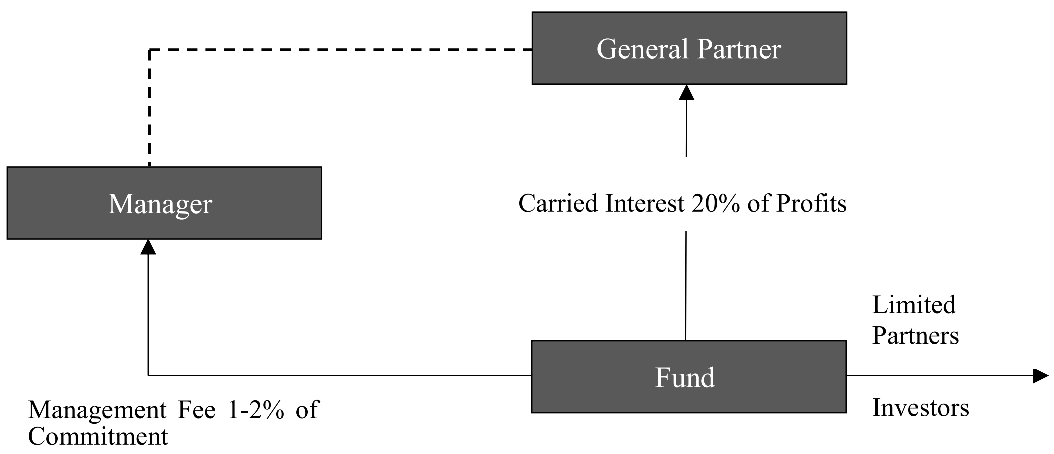
An express regulation in the TFEU concerning the harmonization of direct taxes (Europäisches Parlament Service, 2016) is not provided (Europäisches Parlament Service, 2016; Förster, 2014, p. 17). According to Art. 115 TFEU, this harmonization is given by the general legal basis for the adjustment of the laws (Arndt, Fetzer, & Fischer, 2015, p. 185, Förster, 2014, p. 17). In regards to the direct taxes, the harmonization competence (Behme, 2015, p. 272) of the European Union, thus, refers only to laws and regulations that are in direct wording directly and immediately affecting the formation or effective operation of the common market (Behme, 2015, p. 272; Förster, 2014, p. 14; Arndt, Fetzer, & Fischer, 2015, p. 185).

In principle, the TFEU has changed nothing in terms of allocation of powers between the European Union and the Member States (Förster, 2014, p. 18). For indirect taxes (Goez, 2007, p. 462 et seqq.), the principle of conferral continues to apply, while for direct taxes the legislative power remains with the Member States (Goez, 2007, p. 462 et seqq.; Förster, 2017, p. 18). In the field of taxation, the unanimity requirement under article 114, para. 2 (Frenz, 2011, p. 207 et seqq.) in conjunction with article 26 TFEU applies (Förster, 2014, p. 18; Frenz, 2011, p. 207 et seqq.). So far, a different political solution could not be brought about (Förster, 2014, p. 18). A majority decision (Europäisches Parlament Service, 2016), in which specification ever, could also be conceivable (Europäisches Parlament Service, 2016; Förster, 2014, p. 18). Because of this unanimity clause, it is difficult to harmonize taxation throughout the European Union (Europäisches Parlament Service, 2016; Förster, 2014, p. 18). It is quite noticeable that the fiscal autonomy is of the highest priority to the Member States and is being defended with all possible means (Europäisches Parlament Service, 2016; Förster, 2014, p. 18). Hence, Private Equity transactions are clearly subject to limitations. In particular, cross-border constructions, respectively commitments are massively complicated. Considering the difficulties of fiscal nature, a Private Equity firm encounters for example in Germany, one consequence could be that investors rather refrain from such an investment because of its fiscal opacity. That Private Equity is an instrument for investment also and especially for young companies, meaning start-ups, and that they would surely have a positive effect on the overall European market through their own efforts and the already discussed synergy effects, is indisputable. Therefore, the circumstance, that Member States rigidly stick to their tax system is a rather bad signal for entrepreneurs (Liebing, 2004, pp. 32-38).

3.3.6 Tax Tangents of Private Equity

To get an overview of the variety of taxes and thus the complexity of the tax environment for Private Equity transactions, the figure (67), which was already presented in chapter 1.1.2, is being consulted.

Figure 67: Tax Tangents of Private Equity



Source: Own representation based on own model in 2.1.3.5 figure 6.

Mindful of the actuality that there are various treatments of Private Equity constructs in the European Union (Leible & Lehmann, 2009, p. 28), it is necessary to identify all possible tax situations and explain those briefly. The graph shows the participants of an organized Private Equity business. For all participants there are reference points of a fiscal nature, which are to be observed.

Asset administrative or commercial

First of all, it is important to mention this situation, which essentially only exists in Germany. The distinction which divides between either fiscally transparent or not, does otherwise not exist in hardly any other country (Weißpflog, 2015, p. 264; Scheffler, 2016, p. 55 et seqq.; Moritz, 2004, p. 372 et seqq.). In this context, tax transparency means that the proceeds from e.g. the disposal of shares in a portfolio company are being considered within the framework of the partners and not at funds level (Deloitte, 2009, p. 2; Wallisch, 2009, p. 110 et seqq.). The company, therefore, is not taxable (Deloitte, 2009, p. 2; Wallisch, 2009, p. 110 et seqq.). Ergo, neither business tax is due (Deloitte, 2009, p. 2; Wallisch, 2009, p. 110 et seqq.). In the world's largest Private Equity markets, the USA (Jesch, 2004, p. 141 et seqq.), and in Europe, the UK (Jesch, 2004, p. 157 et seqq.), this transparency principle applies, regardless of whether the business activity is commercial or not (Rapp, 2009, p. 65; BVK, 2009, pp. 1-2).

Carried Interest

The carried interest (Pinkerton & Tuminez, 2003, p. 702 et seqq.; Veith & Schade, 2015) – also called carry – is a form of profit sharing of the fund company and its employees at the expense of the investors in a Private Equity fund (Pinkerton & Tuminez, 2003, p. 702 et seqq.; Veith & Schade, 2015; Deloitte, 2009, pp. 1-67; Renz, 2015, 26 et seqq.; Schalkowski, 2013, p. 28 et seqq.; Tcherveniachki, 2007, p. 27 et seqq.). Usually, the managers receive a share of up to 20% of the profit from the capital expenditure, the so-called Capital Gain (Deloitte, 2009, p. 43, Renz, 2015, 26 et seqq.). In most cases, the carry is only payable, if a predefined minimum interest rate – the hurdle rate – of the capital employed by the investors has been reached (Pinkerton & Tuminez, 2003, p. 702 et seqq.; Veith & Schade, 2015; Deloitte, 2009, pp. 1-67; Renz, 2015, 26 et seqq.; Schalkowski, 2013, p. 28 et seqq.; Tcherveniachki, 2007, p. 27 et seqq.). This minimum interest rate varies considerably, but in practice usually ranges between 6 to 8% per annum (Pinkerton & Tuminez, 2003, p. 702 et seqq.; Veith & Schade, 2015; Deloitte, 2009, pp. 1-67; Renz, 2015, 26 et seqq.; Schalkowski, 2013, p. 28 et seqq.; Tcherveniachki, 2007, p. 27 et seqq.). Affecting the carry as well, significant differences in taxation within the Private Equity market and thus also within the European Union are to be recognized (Pinkerton & Tuminez, 2003, p. 702 et seqq.; Veith & Schade, 2015; Deloitte, 2009, pp. 1-67; Renz, 2015, 26 et seqq.; Schalkowski, 2013, p. 28 et seqq.; Tcherveniachki, 2007, p. 27 et seqq.). For example, in Germany, the carried interest (Pinkerton & Tuminez, 2003, p. 702 et seqq.; Veith & Schade, 2015; Deloitte, 2009, pp. 1-67; Renz, 2015, 26 et seqq.;

Schalkowski, 2013, p. 28 et seqq.; Tcherveniachki, 2007, p. 27 et seqq.) is considered as income from self-employment pursuant to §18 para. 1 no. 4 EStG (Einkommensteuergesetz (Income Tax Act)). This income is subject to the so-called partial-income method (Rapp, 2009, p. 50 et seqq.; Wellisch & Kroschel, 2012, p. 320, Birk, Desens, & Trappe, 2014, p. 232). This means that 60% of these gains are to be taxed at the personal tax rate (Wellisch & Kroschel, 2012, p. 320; Birk, Desens, & Tappe, 2014, p. 232). However, Luxembourg differs between a general carry, which applies to employees of the AIF, and carry, assigned to a share or a stake in an AIF (Viard, 2008, pp. 445-460; Meyers, Kernet, Zanev, Merkus, & Loyens & Loeff, 2010, pp. 257-262).

Tax Loss Carry-forward

Also in regards to the possibility of offsetting tax losses in later years with then occurring profits, there are significant differences in among the respective countries. For example, in France, tax loss carry-forwards at the level of corporations – e.g. target companies for Private Equity investment, only cease to apply, if the company in question actually switches to a different industry (Tcherveniachki, 2007, p. 165 et seqq.; Deloitte, 2009, pp. 1-67, Boué, Kehlbeck, & Leonhartsberger, 2012, p. 189). On the contrary, such an elimination of tax losses carried forward in the UK is only imminent, if a large part of the participations in the relevant company is transferred and beyond that, major modifications are made (Tcherveniachki, 2007, p. 165 et seqq.; Deloitte, 2009, pp. 1-67, Boué, Kehlbeck, & Leonhartsberger, 2012, p. 189). Tax losses carried forward in Germany with regards to corporations are much more uncertain (Tcherveniachki, 2007, p. 165 et seqq.; Deloitte, 2009, pp. 1-67, Boué, Kehlbeck, & Leonhartsberger, 2012, p. 189). The current legal situation leads to a proportionate or complete elimination of tax loss carry-forwards, if shares of more than 25% respectively more than 50% are being acquired by states (Tcherveniachki, 2007, p. 165 et seqq.; Deloitte, 2009, pp. 1-67). With the European Union, Germany thus holds a significant locational disadvantage compared to those aforementioned Member States (Tcherveniachki, 2007, p. 165 et seqq.; Deloitte, 2009, pp. 1-67).

Interest expense

As Private Equity investments are relatively often connected with debt capital, the tax treatment of interest expense is an issue that is addressed in different ways in the European Union. So, under German tax law, the deductibility of interest expenses (Ernst, 2015, p. 57; Eicke, 2009, p. 257) as business expense has been limited by introducing a so-called interest barrier (Bohn, 2009, p. 275 et seqq.; Deloitte, 2009, pp. 1-67; Ernst, 2015, p. 57; Eicke, 2009, p. 257) under §4h EStG (Einkommensteuergesetz (Income Tax Act)). This interest barrier limits the tax interest expense deduction to 30% of the taxable earnings before interest, taxes, depreciation and amortization, the taxable EBITDA (Bohn, 2009, p. 275 et seqq.; Deloitte, 2009, pp. 1-67; Ernst, 2015, p. 57; Eicke, 2009, p. 257). This regulation applies to both corporations and partnerships (Bohn, 2009, p. 275 et seqq.; Deloitte, 2009, pp. 1-67; Ernst, 2015, p. 57; Eicke, 2009, p. 257). Although the motives for the interest barrier are understandable – as it serves the avoidance of cross-border arrangements that used to allow companies to claim deductible interest expenses (Müller, 2009, p. 135), while the interest income had been recorded abroad – it poses a rather unfavorable issue for Private Equity (Bohn, 2009, p. 275 et seqq.; Deloitte, 2009, pp. 1-67; Ernst, 2015, p. 57; Eicke, 2009, p. 257; Müller, 2009, p. 135).

France has taken a different path in regards to interest expenses (Marquart, 2013, p. 144 et seqq.). Under French law, the interest subsidy is restricted by the adequacy principle and the regulations on shareholder debt financing (Bohn, 2009, p. 123 et seqq.; Deloitte, 2009, pp. 1-67; Marquart, 2013, p. 144 et seqq.). Interest expenses that are paid to affiliated companies respectively to related parties are not tax-deductible (Müller, 2009, p. 135). This applies, if the underlying interest rate does not satisfy the arm's lengths principle and therefore the expenses are unreasonably high (Bohn, 2009, p. 123 et seqq.; Deloitte, 2009, pp. 1-67; Marquart, 2013, p. 144 et seqq.). As far as interest expenses cannot be claimed for tax purposes, there is, within certain limits, the possibility of an interest carryforward to subsequent years (Bohn, 2009, p. 123 et seqq.; Deloitte, 2009, pp. 1-67; Marquart, 2013, p. 144 et seqq.). Interest expense related to liabilities due to banks are always tax deductible without restrictions (Bohn, 2009, p. 123 et seqq.; Deloitte, 2009, pp. 1-67; Marquart, 2013, p. 144 et seqq.; Müller, 2009, p. 135)).

Sales Tax on Management Services

In the United Kingdom, remunerations received by personally liable partners – that is, the General Partners – of a Private Equity Fund Limited Partnership, for management and consulting benefits received by the corporation, are basically structured as profit distributions and are as such not subject to VAT (Deloitte, 2009, pp. 49-50). Also the management services, which are considered as special cases, to certain mutual funds in the form of special assets and the determination of divestments, are exempt from VAT within the meaning of Article 135 para. 1, letter g and f of the VAT Directive (Deloitte, 2009, pp. 1-67). Outside the European Union – particularly in the USA – a sales tax on management services, which are provided by the General Partner to the Private Equity fund, is not charged. In Germany, the VAT treatment is complicated, especially in regards to managing services. First, it should be noted that in opinion of the Federal fiscal court and the tax authorities, the director activities are incurred in the context of a paid exchange of services and are thus subject to VAT (Busack & Kaiser, 2006, p. 579; Deloitte, 2009, pp. 1-67). Only thereafter does it have to be examined whether these are applicable for a VAT exemption (Deloitte, 2009, p. 37 et seqq.). For the development of a funds structure, that is to be uniformed in the fiscal area, the extremely different treatments in the countries pose a protruding issue (Achleitner & Everling, 2004, p. 200; Deloitte, 2009, pp. 1-67).

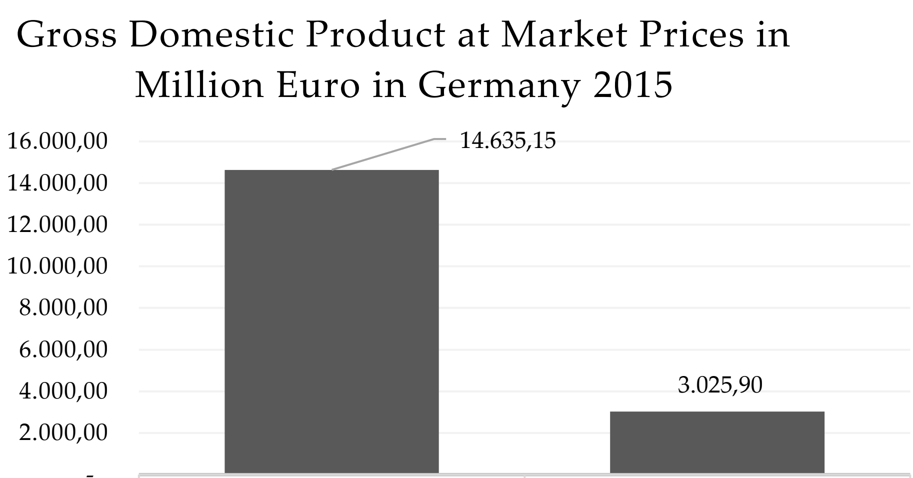
3.4 OVERVIEW AND REGULATORY ENVIRONMENT OF PRIVATE EQUITY IN GERMANY

3.4.1 **Performance Features: Private Equity in Germany**

3.4.1.1 Preliminary Remarks

The German Private Equity market – or better investment location - is especially interesting for foreign investors (Köhler K. , 2015, p. 142; EuroActiv, 2014; Ernst & Young, 2012, pp. 1-32). This is not surprising, since Germany represents the largest national economy in the European Union (Müller-Brandeck-Bocquet, 2010, p. 332; Beck H. , 2016, p. 245). This attracts investors from all over the world (Dencik & Spee, 2014, pp. 1-20). Figure 68 shows the Gross Domestic Product at market prices in Germany.

Figure 68: Gross Domestic Product at Market Prices in 2015 in Germany

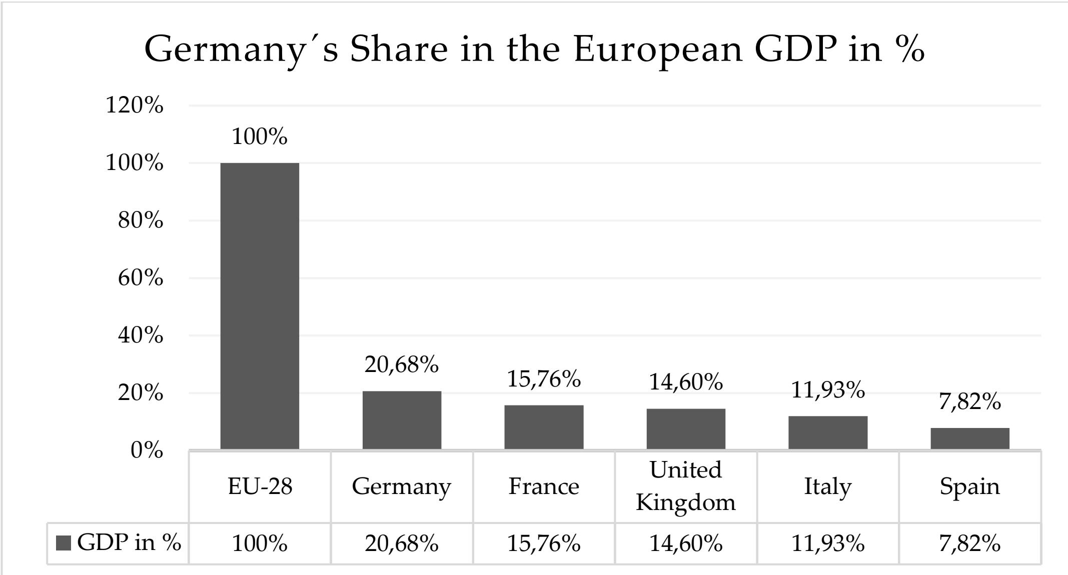


	European Union	Germany
GDP in Billion Euro	14.635,15	3.025,90

Source: Owen representation based on Eurostat.

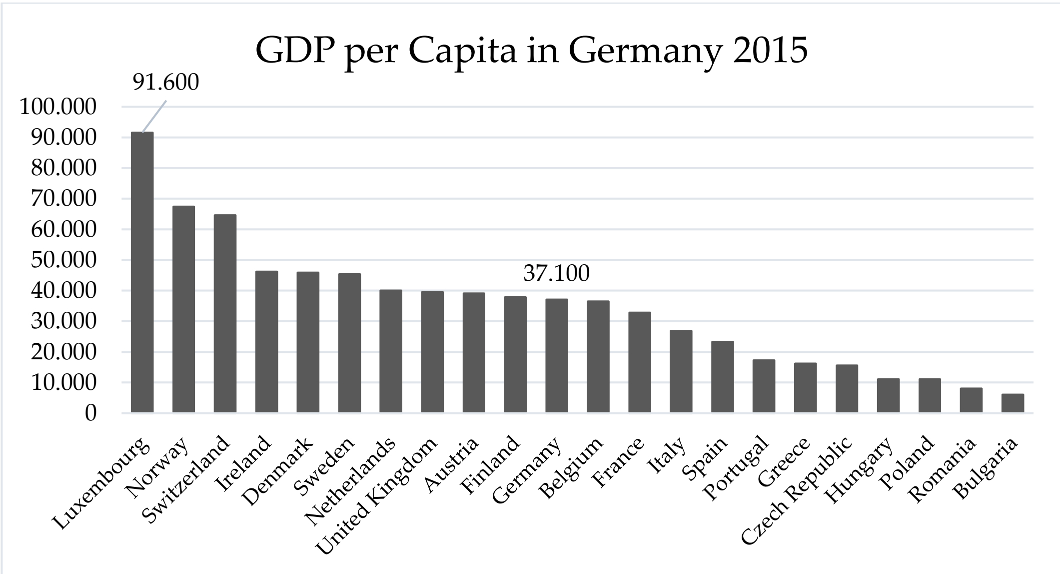
Considering merely the share of Germany's gross domestic product compared to the total volume of the European Union (Eurostat, 2016) clearly shows that Germany is playing a prominent role in the European Union (EU). The importance of the Federal Republic of Germany in the European context and her significance can almost better be gathered from the diagram in figure 69. With more than 20 percent of the total gross domestic product (GDP) of the European Union, with 28 Member States after all, Germany is followed by France and the United Kingdom, each with 15 percent. The top five are completed by Italy and Spain, with almost 12 percent, respectively, nearly 8 percent. In addition, it can be taken from this statistic that these five countries already account for approximately 70 percent of the total GDP in the European Union.

Figure 69: Germany´s Share in the European GDP in %



Source: Own representation own calculation based on Eurostat.

Figure 70: Gross Domestic Product per Capita in Germany 2015



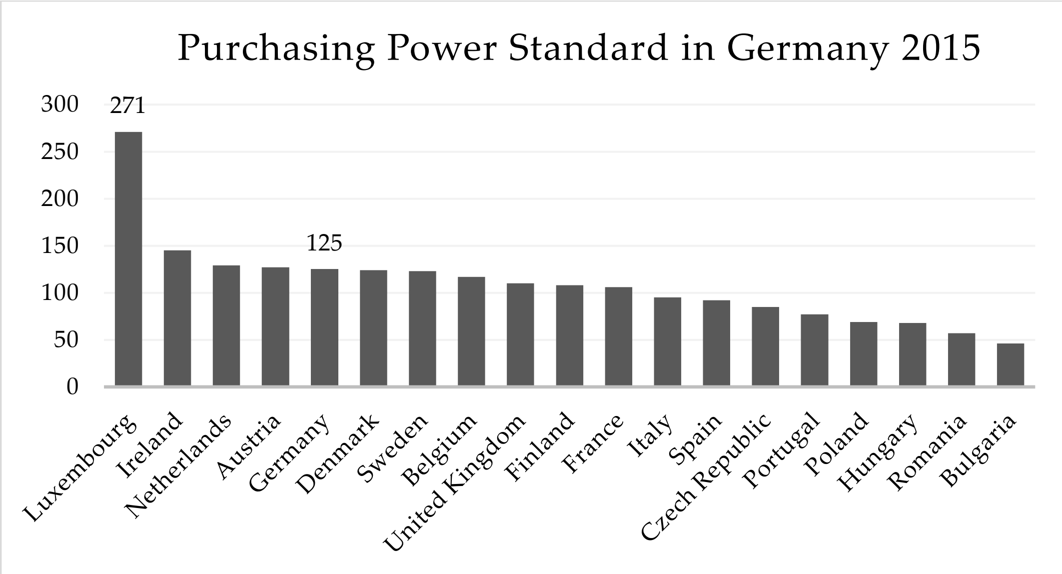
Source: Own representation based on Eurostat.

As for the performance of Germany, a performance figure needs to be taken as a basis which will address the readiness to invest in Germany, but could affect the willingness of Germans to invest in other countries. This refers to the per capita domestic product (Eurostat, 2016).

Taking into account the most important Private Equity countries of the European Union – considering how strong the total product of Germany is - Germany takes a surprisingly weak spot in the mid- ranks, which could be a slight indication of the lacking readiness to invest (figure 70).

To gain some more clarity (Eurostat, 2016; Steuerwald, 2016, p. 224; Haas, 2010, p. 6; Müller M. C., 2005, p. 19; Bundeszentrale für politische Bildung, 2015, p. 1), this is compared with the purchasing power standard (PPS) in figure 71. This fictitious monetary unit, independent from the national currency, eliminates distortions based on difference in price levels of different countries (Eurostat, 2016; Steuerwald, 2016, p. 224; Haas, 2010, p. 6; Müller M.C., 2005, p. 19; Bundeszentrale für politische Bildung, 2015, p. 1). The standard is based on average values and indexed at 100 in the European Union (Eurostat, 2016; Steuerwald, 2016, p. 224; Haas, 2010, p. 6; Müller M.C., 2005, p. 19; Bundeszentrale für politische Bildung, 2015, p. 1). A higher value indicates that a country has a higher purchasing power than the EU average and vice versa (Eurostat, 2016; Steuerwald, 2016, p. 224; Haas, 2010, p. 6; Müller M.C., 2005, p. 19; Bundeszentrale für politische Bildung, 2015, p. 1).

Figure 71: Purchasing Power Standard in Germany 2015



Source: Own representation based on Eurostat.

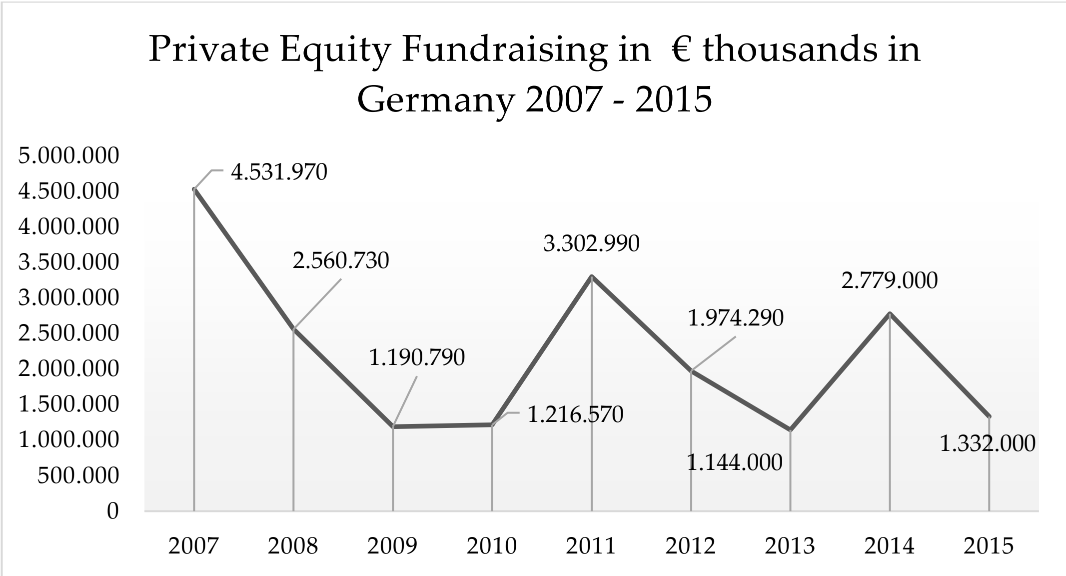
Among the same participating counties, Germany, again, shows only a marginal improvement in this comparison to the per capita gross domestic product, remaining in the middle ranks, so it must be stated that Germany, measured by per capita income and purchasing power and despite its supposed superior position in the European Union, seems not to be particularly suitable for investments in its own country or abroad.

Naturally, foreign investors have a different point of view because Germany is an industrialized nation with extensive investment possibilities (Köhler K. , 2015, p. 142; EuroActiv, 2014; Ernst & Young, 2012, pp. 1-32).

3.4.1.2 *Establishment of Private Equity in Germany*

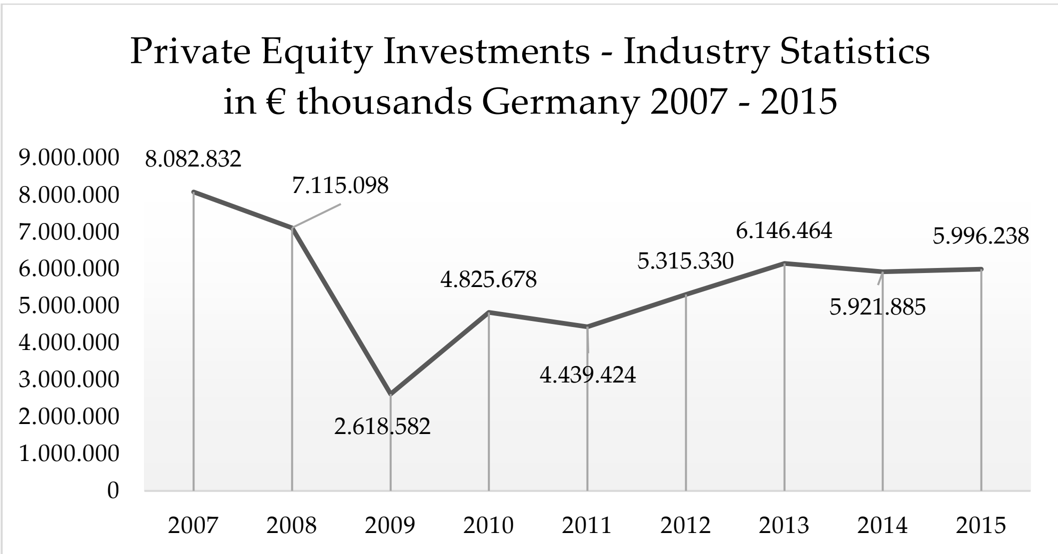
At the end of 2013, the national umbrella organization of German Private Equity companies (Bundesverband Deutscher Kapitalbeteiligungsgesellschaften (BVK)) determined that of 178 investment companies, there were 9 less organized compared to the previous year (bvk, 2014). In 2014 there are 187. However, the number dropped again in 2015 roughly to the previous level.

Figure 72: History of Private Equity Fundraising in Germany to 2015



Source: Own representation based on Invest Europe, 2016.

Figure 73: PE Investments by Country of Private Equity Firms Germany



Source: Own representation based on Invest Europe, 2016.

In this, another approximately 60 relevant investment companies which are organized in the BVK have not been taken into account. Nevertheless, by these figures the conclusion can be drawn that in regards to the German investment companies in their entirety, the market rather stagnates.

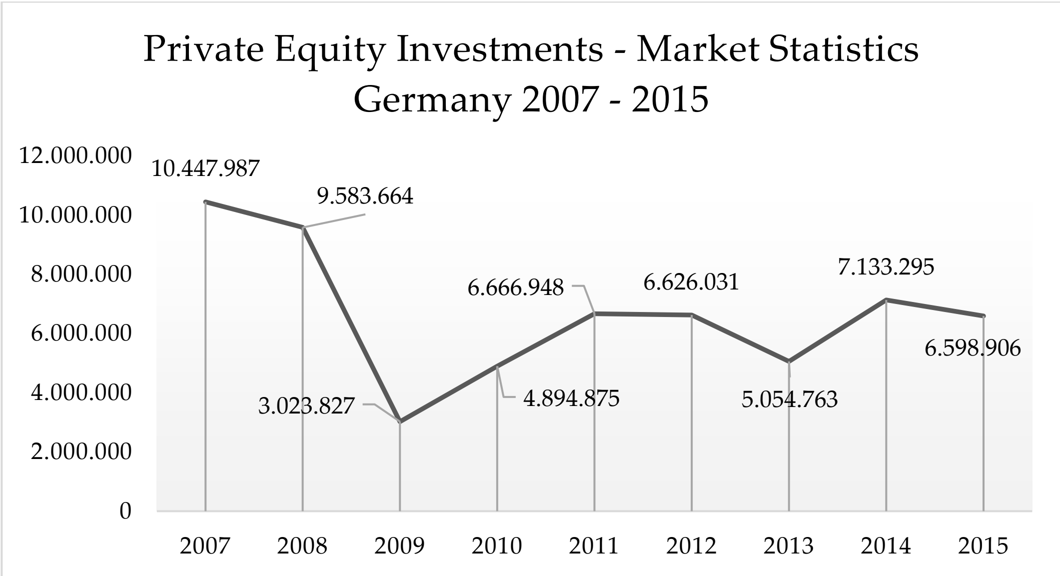
What this means in terms of collecting money – fundraising – is illustrated in figure 72, in which the numbers are to be understood in thousands of euros (Invest Europe, 2016).

After the crisis, the recovery of the Private Equity market in regards to fundraisings in 2011 and 2014 represents only a temporary phenomenon, so that Germany remains at about the same level, however reasonably instable, as in 2009-2010.

Fundraising represents currently only one parameter on the Private Equity market. In order to be capable of estimating the actual strength of the industry, investments and divestments need to be considered. As already explained, the investments are being assessed either from the point (location) of the investment company or the point (location) of the target company, depending on the point of view. The corresponding graph (figure 73) should provide an overview of the investment activities of Private Equity companies. In this figure as well, numbers are to be understood in thousands of euros.

It does not actually appear that the Private Equity companies are less active, once less money is being raised. On the contrary, the investment activities have been constantly increasing since the crisis. It is already now noticeable, that the investment activity of German Private Equity companies is many times higher than the fundraising.

Figure 74: PE Investments by Country of Portfolio Company Germany



Source: Own representation based on Invest Europe, 2016.

In figure 74, the investments in thousands of euros are being illustrated which are incurred in relation to the place of the portfolio company. Also in view from the perspective of the target company, there has been an increase in activity after the crisis. However, there is currently a slight downward trend to be seen.

Interpretation

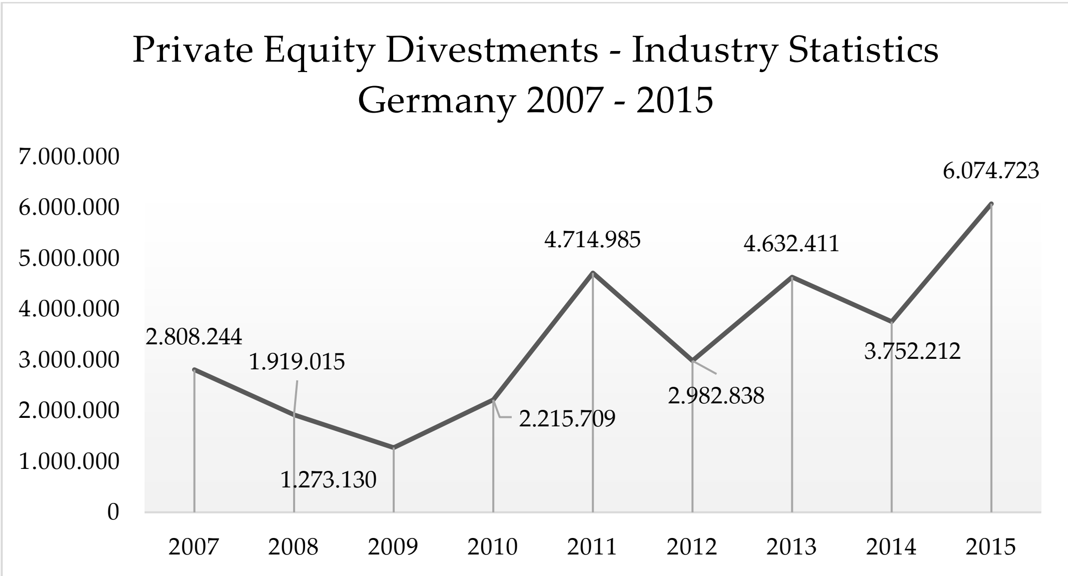
The nvestments were examined, specifically those which investment companies located in Germany execute as well as those investments received by portfolio companies in Germany. This data may only be correctly assessed by placing them in relation with other parameters. In this case, the gross domestic product (GDP) and the investment per capita is appropriate.

While in Germany the portion of investments by German Private Equity companies still amounted to 0.322% in 2007, it decreased, as a result of the crisis, to only 0.107% in 2009 and now 0.216% in 2013. In 2014 it was 0.203% and in 2015 0.198%. In 2007, 100.38 € were invested per capita. In 2009 that figure amounted to 32.52 € and 73.38 € in 2013. In 2014 it was 73.20 € and in 2015 73.93 €.

In 2007, 0.416% of the GDP had been invested in Germany-based portfolio companies, in 2009 that number was 0.123% and in 2013 0.180% of the GDP. In 2014 it was 0.245% and in 2015 0.218%. Per capita, 129.75 € were invested in 2007, in 2009 37.55 € and 61.19€ in 2013, in 2014 87.96 € and 2015 81.37 € in portfolio companies.

Overall, it can be stated that the willingness for an investment in terms of Private Equity in Germany is at a low level. Although the numbers slowly recover, the value attained prior to the crisis is still far away. Strikingly noticeable is the reticence with regard to investments in German portfolio companies.

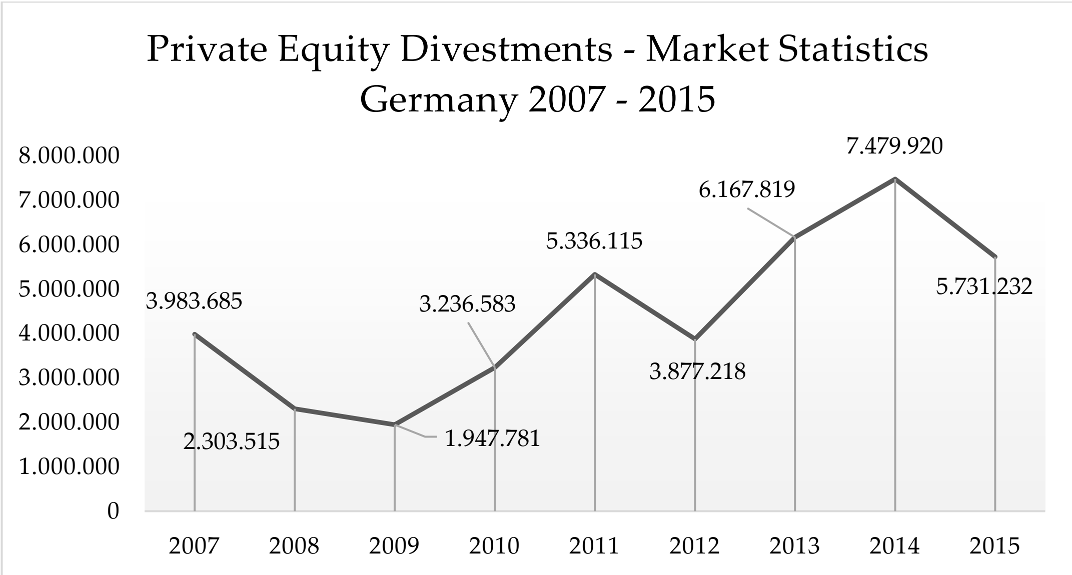
Figure 75: PE Divestments by Country of the Private Equity Firm Germany



Source: Own representation bases on Invest Europe, 2016.

Also very important is the differentiation of the divestments in market and industry statistics, in order to make investments and divestments comparable in the first place. Figure 75 shows in thousands of euros the divestments since 2007 up to the year 2015.

Figure 76: PE Divestments by Country of the Portfolio Company Germany



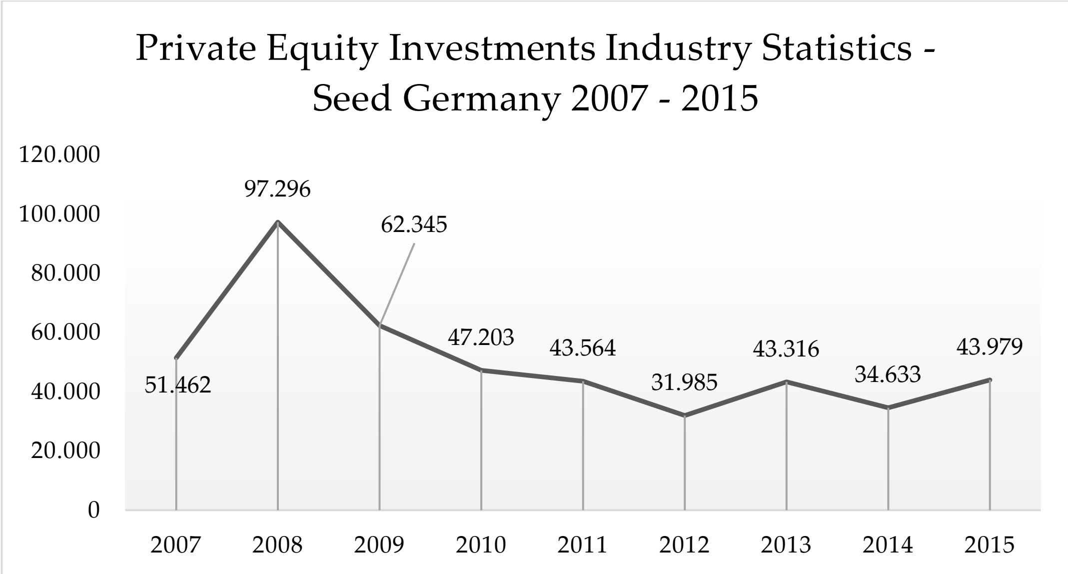
Source: Own representation based on Invest Europe, 2016.

The course of divestment in the industry statistics is apparently very similar to the course of investments in industry statistics. According to both statistics, values have been continuously rising since the crisis. Figure 76 shows, for comparison, the market statistics. Unlike the investments, markets statistics shows the same curve with divestments as with the examination regarding the location of Private Equity firms.

Early-stage financing

The willingness to invest in the early stages (Schüle, 2015, p. 17; Kuntz, 2016, p. 12) of a Private Equity transaction, which is particularly interesting for entrepreneurs, is illustrated in the following figures (Hoffmann, 2014, p. 112 et seqq.; Schüle, p. 17; Kuntz, 2016, p. 12; Invest Europe, 2016). First, the graphic of investments (figure 77) based on the place of Private Equity firms is shown.

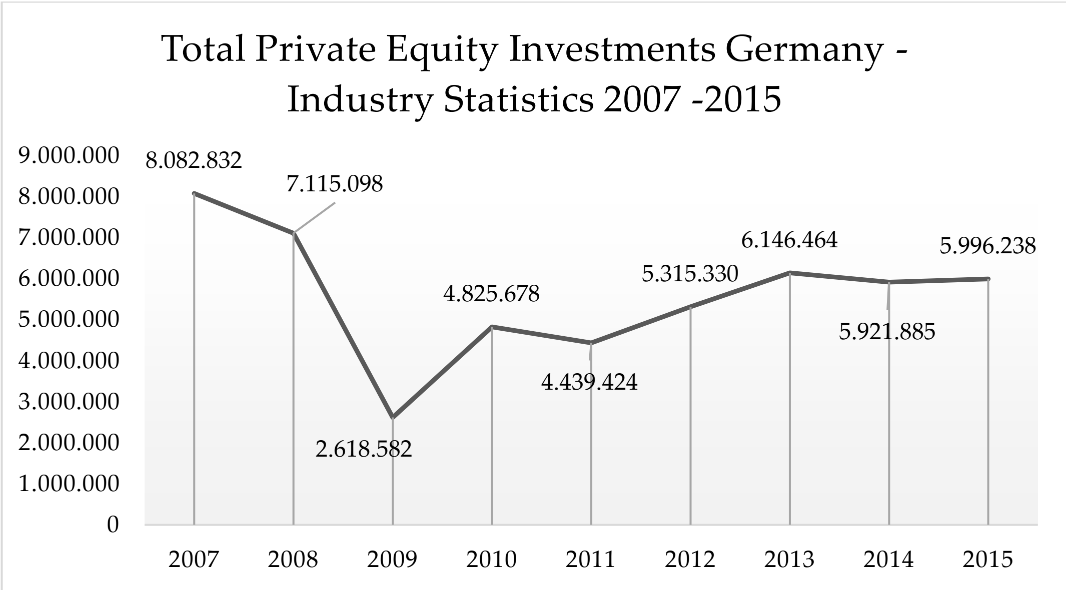
Figure 77: PE Investments by Country of Private Equity Firm – Seed Germany



Source: Own representation based on Invest Europe, 2016.

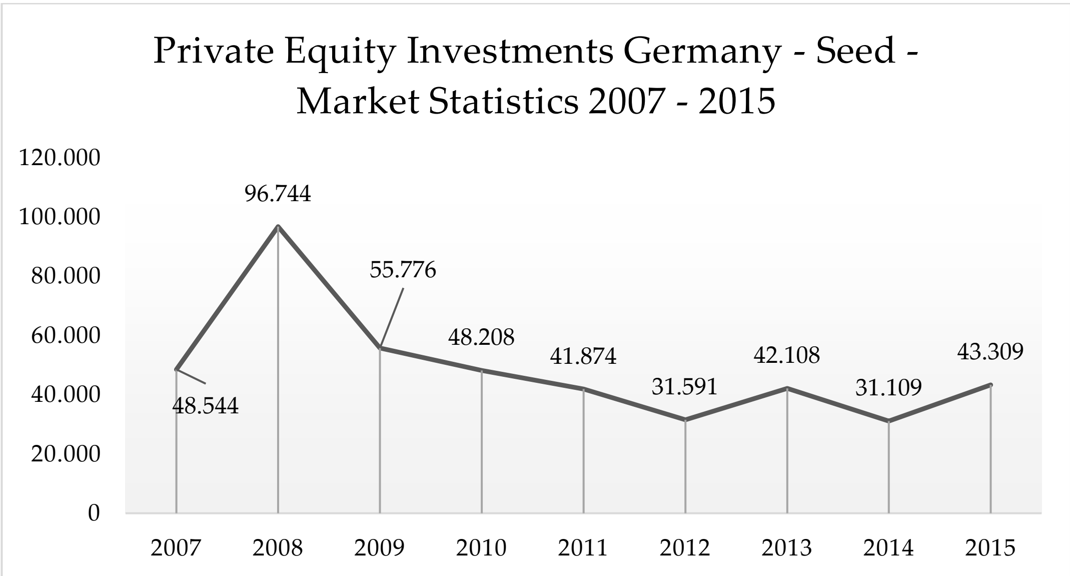
Considering the investments in the very early stages in comparison to the total investments in this segment in figure 78, the blatantly low proportion of investments during this start-up phase and the – in quotation marks – high proportion of seed investments in the phase – 2009 –, during which the total investments were lowest, can be noticed (Rudolph, 1998, p. 222 et seqq.; Kuntz, 2016, p. 12 et seqq.; Hofmann & Schmolz, 2014, p. 131 et seqq.). It can therefore be assumed that Private Equity firms invest only little in total during this phase – the reasons for this have already been explained – and that these companies evidently spur the investments entailing less risk in times of crisis in order to still remain in the field of Private Equity. Thus, the proportion of seed investment compared to the total investments in the sense of the Industry Statistic during its heyday in 2007 with 0.6% had been well below the value of 2009, when 2.4% of the total volume was invested in the seed segment.

Figure 78: Total PE Investments in Private Equity – Industry Statistics Germ.



Source: Own representation based on Invest Europe, 2016.

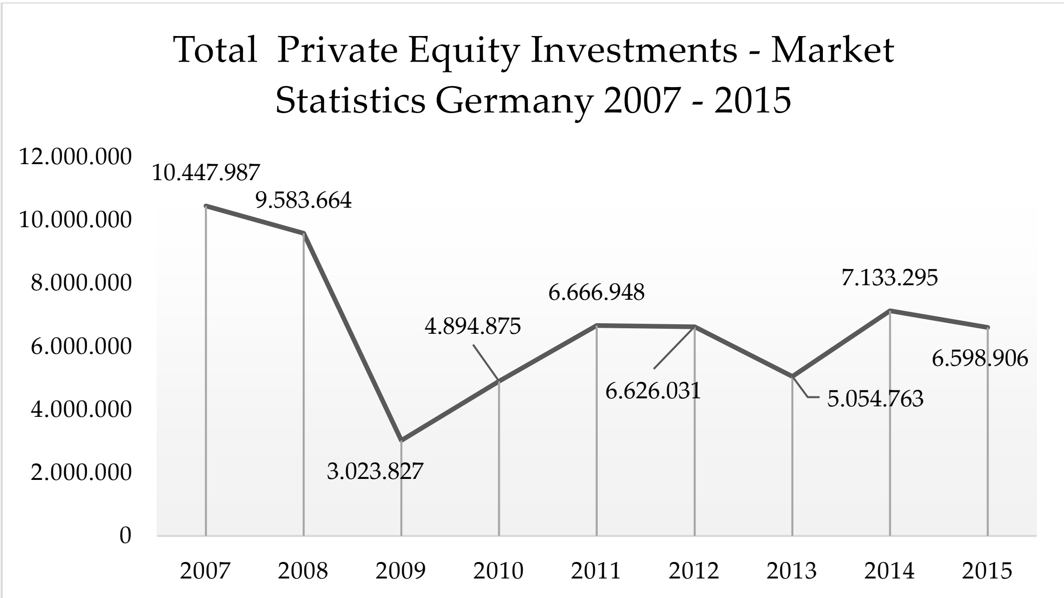
Figure 79: PE Investments by Country of Portfolio Company - Seed



Source: Own representation based on Invest Europe, 2016.

It is also striking that in terms of Private Equity firms, the seed investments recover even slower than the total investments in Private Equity in Germany, and that the percentage share of seed investments in the total volume of investments has moved downward again, despite the supposed high level during the crisis and the weak level of overall investments. This means nothing else but that German portfolio companies were more quickly willing again to invest, however less in companies during their early stages of investment. In regards to the market statistics – thus the statistics by country of Portfolio Company (figure 80) – it can be stated that the curve progression is almost identical, however with a higher overall volume of investments.

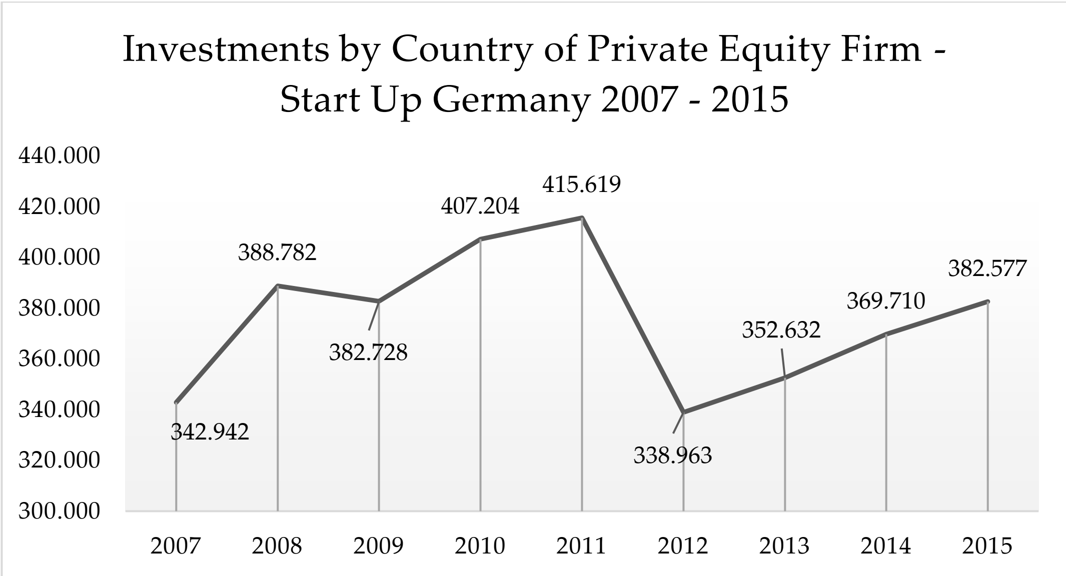
Figure 80: Total PE Investments in Private Equity – Market Statistics Germany



Source: Own representation based on Invest Europe, 2016.

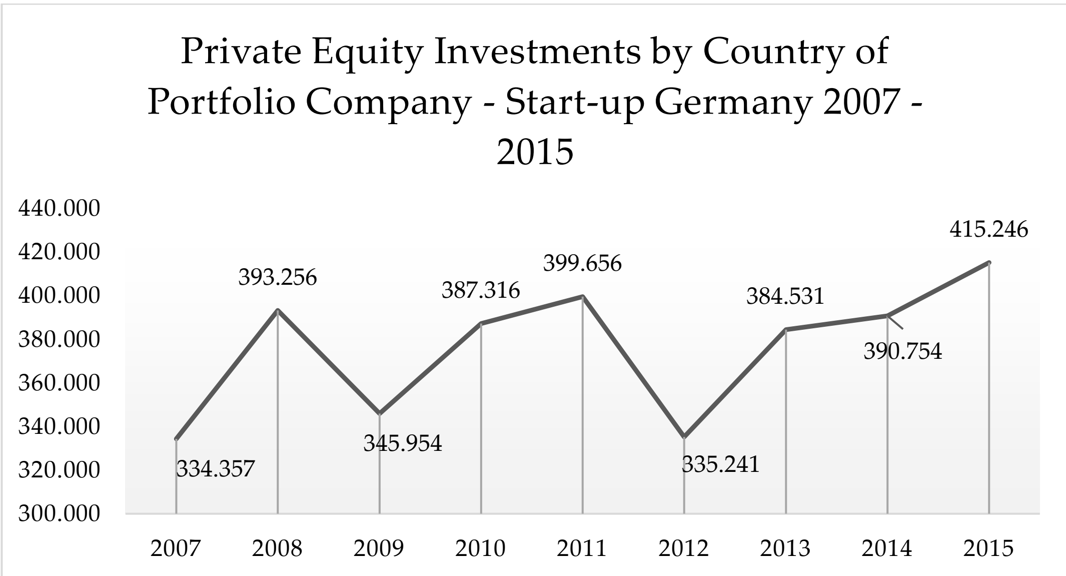
A very similar phenomenon at a slightly higher level can be observed with investments during the start-up phase (figure 81 and 82), whereas the curve differs slightly. In this segment as well, the propensity to invest during or immediately after the crisis is higher than before or thereafter.

Figure 81: Private Equity Investments Industry Statistics – Start-up Germany



Source: Own representation based on Invest Europe, 2016.

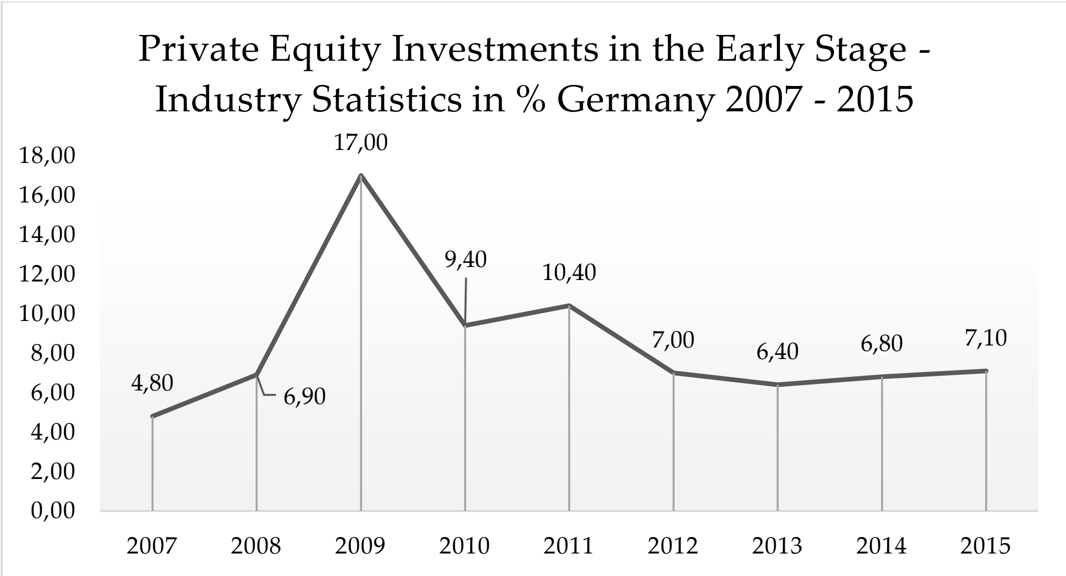
Figure 82: Private Equity Investments Market Statistics – Start-up Germany



Source: Own representation based on Invest Europe, 2016.

For the entrepreneur in Germany, this denotes that he may only hope for limited support through Private Equity in Germany during the early stage of his enterprise. However, this support is usually reliably offered by companies located in Germany.

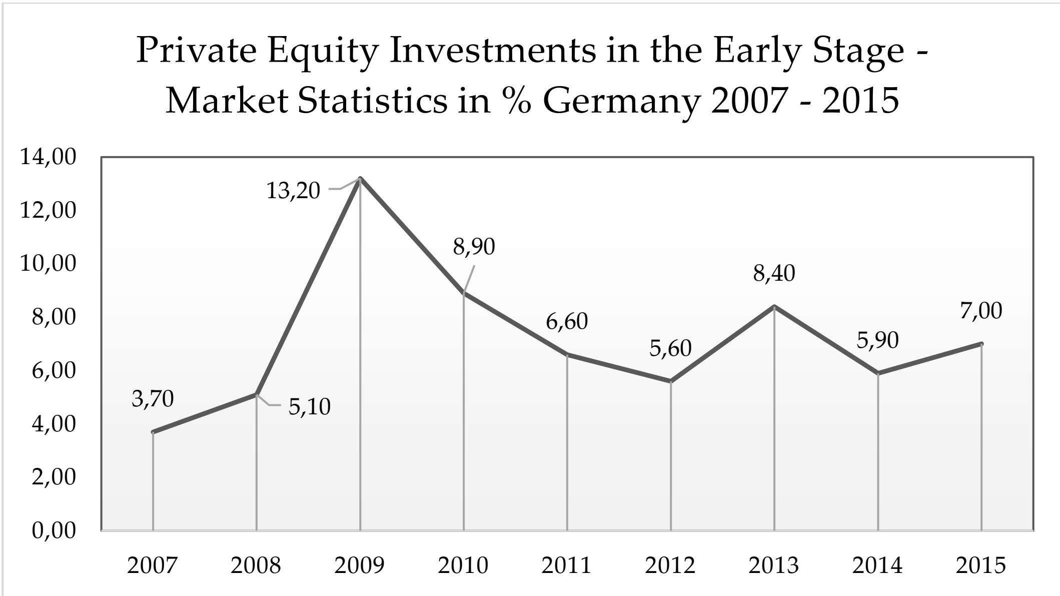
Figure 83: PE Investments in the Early Stage in % - Industry Statistics Germany



Source: Own representation based on Invest Europe, 2016.

For German founders, this statistic also indicates that foreign companies – from Member States of the European Union – are hardly interested in investing in young companies, either because of lack of information, lack of revenue opportunities or lack of interest in overcoming asymmetries in terms of e.g. the fiscal regulations. If the two early stages – which are defined at this point in seed and start-up – are being cumulated (figures 83 and 84), it will hardly result in a better outlook for entrepreneurs in Germany. Just at the point at which the investments are most necessary for founders, the willingness of portfolio companies to invest remains at a low level, whereas the investments during the early stages – according to market statistics - in Germany-based enterprises has actually increased.

Figure 84: PE Investments in the Early Stage in % - Market Statistics Germany



Source: Own representation based on Invest Europe, 2016.

As already indicated above, one reason for the restrained willingness to invest in Private Equity and therefore also in the early stages at all, could be that the Member States of the European Union are offering the most different tax conditions with respect to Private Equity funds. As the individual Member States have been forced by the AIFM Directive to act, Germany has reacted with the AIFM (Alternative Investment Fund Manager) tax adaption act (Ortmann-Babel, Franke, Bolik, & Zöller, 2013, p. 142 et seqq.).

3.4.2 **Promulgation of the AIFM Tax Adaption Act (AIFM-StAnpG)**

The AIFM Tax Adaption Act (AIFM-Steueranpassungsgesetz (AIFM-StAnpG)) was passed by the German Federal Council (Deutsche Bundestag) and the Federal Council (Bundesrat) on November 28th and 29th, 2013 (Dißmann, 2015; Fabry & Kaluzna, 2013, pp. 1-5; Haase & Dorn, 2015, p. 22 et seqq.; Weitnauer, Boxberger, & Anders, 2014, p. 1649 et seqq.). The law was promulgated in the Federal Gazette (Bundesgesetzblatt (BGBl.)) on December 23rd, 2013 (BGBl. I 2013, p.

4318) so that the entire AIFM Tax Adjustment Act (AIFM-StAnpG) became yet effective in 2013 (Fabry & Kaluzna, 2013, pp. 1-5; Dißmann, 2015; Haase, 2014, p. 197; Haase & Dorn, 2015, p. 22 et seqq.; Weitnauer, Boxberger, & Anders, 2014, p. 1649 et seqq.).

The Federal Council (Bundesrat) approved a proposed law for resubmission of the AIFM Tax Adaption Act (Bundesrat, 2013, pp. 1-137) on November 8th, 2013 (BR-Drs. 740/13 B). Resubmission had become necessary because the parties were unable to agree in the Conciliation Committee before the federal election (Simonis, Grabbe, & Faller, 2014, pp. 16-22). Since the original bill for the AIFM Tax Adaption Act (AIFM-StAnpG) could not be adopted in the same legislative session which saw the introduction of the Federal Council (Bundestag), the bill expired due to the so- called factual discontinuity (Ortmann-Babel & Bolik, 2013, pp. 1-6).

The AIFM Tax Adaption Act (AIFM-StAnpG) can be substantially viewed as an adjustment of the Investment Tax Act (Investmentsteuergesetz (InvStG)) to the Capital Investment Code (Kapitalanlagegesetzbuch (KAGB)), which was created (BGBL. I 2013, o, p. 1981) by the AIFM Implementation Act (AIFM-Umsetzungsgesetz (AIFM-UmsG)) and was promulgated on July 4th, 2013 and became effective on July 22nd, 2013. It provides tax restrictions associated with the raising of hidden liabilities (Fabry & Kaluzna, 2013, pp. 1-5; Dißmann, 2015; Haase, 2014, p. 197; Haase & Dorn, 2015, p. 22 et seqq.; Weitnauer, Boxberger, & Anders, 2014, p. 1649 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22; Ortmann-Babel & Bolik, 2013, pp. 1-6). The Act contains an amendment to the application regulation (Fabry & Kaluzna, 2013, pp. 1-5; Dißmann, 2015; Haase, 2014, p. 197; Haase & Dorn, 2015, p. 22 et seqq.; Weitnauer, Boxberger, & Anders, 2014, p. 1649 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22; Ortmann-Babel & Bolik, 2013, pp. 1-6) from the Corporate Tax Reform Act (Unternehmenssteuerreformgesetz (UntStRefG)) of 2012 (so-called VZ 2014 gap). In addition to the tax adjustments, the introduction of a Pension Asset Pooling Vehicle in Germany (Rhodius & Lofing, 2013, pp. 85-133) is being implemented (Fabry & Kaluzna, 2013, pp. 1-5; Dißmann, 2015; Haase, 2014, p. 197; Haase & Dorn, 2015, p. 22 et seqq.; Weitnauer, Boxberger, & Anders, 2014, p. 1649 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22; Ortmann-Babel & Bolik, 2013, pp. 1-6; Rhodius & Lofing, 2013, pp. 85-133).

3.4.3 Introduction of the Capital Investment Code (KAGB)

The AIFM Directive (AIFMD) came into effect on July 21st, 2013, the legislative process for its implementation (Körber, 2014, p. 20; Ebel, 2015, p. 430) had to be completed by July 22nd, 2013 (Weitnauer, Boxberger, & Anders, 2014, p. 1; Körber, 2014, p. 20; Ebel, 2015; p. 430). With the adoption of the European AIFM Directive the previously existing Investment Act (Investmentgesetz (InvG)) is abolished (Schindler & Hindelang, 2016, p. 54 et seqq.) in Germany (Weitnauer, Boxberger, & Anders, 2014, p. 3; Weißflog, 2015, p. 28 et seqq.; Schindler & Hindelang, 2016, p. 54 et seqq.). Therein contained regulations have been integrated in the Capital Investment Code (KAGB) since July 22nd, 2013 (Weitnauer, Boxberger, & Anders, 2014, p. 3; Weißflog, 2015, p. 28 et seqq.; Schindler & Hindelang, 2016, p. 54 et seqq.). The Act governs a total of 355 paragraphs, regulating open and closed-end funds and their manager for the first time (Weitnauer, Boxberger, & Anders, 2014, p. 3; Weißflog, 2015, p. 28 et seqq.; Schindler & Hindelang, 2016, p. 54 et seqq.). It was and still is hoped that this will fundamentally transform the fund industry (Weitnauer, Boxberger, & Anders, 2014, p. 3; Weißflog, 2015, p. 28 et seqq.; Schindler & Hindelang, 2016, p. 54 et seqq.). These provisions are intended to further develop the supervisory and regulatory framework conditions and to adapt them to the amended European requirements (Weitnauer, Boxberger, & Anders, 2014, p. 3; Weißflog, 2015, p. 28 et seqq.; Schindler & Hindelang, 2016, p. 54 et seqq.). The Capital Investment Code (KAGB) may thus provide a contribution to the achievement of the European single market in the investment fund sector (Weitnauer, Boxberger, & Anders, 2014, p. 3; Weißflog, 2015, p. 28 et seqq.; Schindler & Hindelang, 2016, p. 54 et seqq.). Moreover, it can also protect investors through a uniformly high standard (Weitnauer, Boxberger, & Anders, 2014, p. 3; Weißflog, 2015, p. 28 et seqq.; Schindler & Hindelang, 2016, p. 54 et seqq.). So, for the first time, managers of closed-end funds must meet the same requirements which must be met longstanding by open-end funds (Weitnauer, Boxberger, & Anders, 2014, p. 3; Weißflog, 2015, p. 28 et seqq.; Schindler & Hindelang, 2016, p. 54 et seqq.).

The Capital Investment Code (KAGB) differs (BVI, 2015, p. 1) between (Weitnauer, Boxberger, & Anders, 2014, p. 3; Weißflog, 2015, p. 28 et seqq.; Schindler &

Hindelang, 2016, p. 54 et seqq.; Weitnauer, Boxberger, & Anders, 2014, p. 6; BVI, 2015, p. 1) investment assets, known as Undertakings for Collective Investment in Transferable Securities (UCITS), and Alternative Investment Funds (AIF). Equity and debt security funds are frequently such undertakings for collective investment in transferable securities (Weitnauer, Boxberger, & Anders, 2014, p. 3; Weißflog, 2015, p. 28 et seqq.; Schindler & Hindelang, 2016, p. 54 et seqq.; Weitnauer, Boxberger, & Anders, 2014, p. 6; BVI, 2015, p. 1). Closed-end funds, however, are being classified as AIF (Weitnauer, Boxberger, & Anders, 2014, p. 3; Weißflog, 2015, p. 28 et seqq.; Schindler & Hindelang, 2016, p. 54 et seqq.; Weitnauer, Boxberger, & Anders, 2014, p. 6; BVI, 2015, p. 1). For UCITS managers and AIF, different admission requirements and reporting obligations do apply to whose attendance does not seem necessary at this point (Weitnauer, Boxberger, & Anders, 2014, p. 3; Weißflog, 2015, p. 28 et seqq.; Schindler & Hindelang, 2016, p. 54 et seqq.; Weitnauer, Boxberger, & Anders, 2014, p. 6; BVI, 2015, p. 1). After the entry into force (Weitnauer, Boxberger, & Anders, 2014, p. 3; Weißflog, 2015, p. 28 et seqq.; Schindler & Hindelang, 2016, p. 54 et seqq.; Weitnauer, Boxberger, & Anders, 2014, p. 6; BVI, 2015, p. 1) of the Capital Investment Code (KAGB) the previous Investment Companies (Kapitalanlagegesellschaften (KAGs)) became Capital Management Companies (Kapitalverwaltungsgesellschaften (KVGs)). These differentiate themselves in UCITS and AIF KVG (Kapitalverwaltungsgesellschaft) according to the type of managed investment assets (Böttcher, 2014, pp. 401-402).

3.4.4 Changes by the AIFM Tax Adaption Act

In addition to the regulations, which are in direct context to the adjustment to the provisions of the Capital Investment Code (KAGB), the legislature has used the AIFM Tax Adaption Act (AIFM-StAnpG) to implement further individual measures, such as regulations for the ending of the so-called bond stripping (Grill, Gramlich, & Eller, 1995, p. 296; Mertes, 2015, p. 816; Ossenbrink, 2016, p. 266), for a first-time legal regulation of an appropriation sequence with disbursements, for an alternative allocation of professional expenses as well as in regards to non-investment tax issues (Simonis, Grabbe, & Faller, 2014, pp. 16-22; Mardini, personal communication, 2014, May 28; Weitnauer, Boxberger, & Anders, 2014, p. 1649 et seqq.; Grill, Gramlich, & Eller, 1995, p. 296; Mertes, 2015, p. 816; Ossenbrink, 2016, p. 266). The area of non-investment tax issues concerns the standards for the fiscal treatment of commitment acquisitions, debt accessions and fulfillment commitments in terms of commitments, which were subject to approach prohibitions, restrictions or evaluations reserves under the original obligor issues (Simonis, Grabbe, & Faller, 2014, pp. 16-22; Mardini, personal communication, 2014, May 28; Weitnauer, Boxberger, & Anders, 2014, p. 1649 et seqq.; Grill, Gramlich, & Eller, 1995, p. 296; Mertes, 2015, p. 816; Ossenbrink, 2016, p. 266). The legislative body had to quickly move forward with the implementation in agreement with the judicature of the Federal Fiscal Court (Bundesfinanzhof (BFH)), if to yet prevent the resulting risks of high tax loss issues (Simonis, Grabbe, & Faller, 2014, pp. 16-22; Mardini, personal communication, 2014, May 28; Weitnauer, Boxberger, & Anders, 2014, p. 1649 et seqq.; Grill, Gramlich, & Eller, 1995, p. 296; Mertes, 2015, p. 816; Ossenbrink, 2016, p. 266). With the revision of the Investment Tax Act (InvStG), necessary adjustments were taken, which resulted from the national implementation of the AIFM Directive, thus as well from the Capital Investment Code (KAGB) issues (Simonis, Grabbe, & Faller, 2014, pp. 16-22; Mardini, personal communication, 2014, May 28; Weitnauer, Boxberger, & Anders, 2014, p. 1649 et seqq.; Grill, Gramlich, & Eller, 1995, p. 296; Mertes, 2015, p. 816; Ossenbrink, 2016, p. 266). As explained in the previous chapter, the Capital Investment Code (KAGB) has replaced the Investment Act (Investmentgesetz (InvG)) effective July 22, 2013 issues (Simonis, Grabbe, & Faller, 2014, pp. 16-22; Mardini, personal communication, 2014, May 28; Weitnauer, Boxberger, & Anders, 2014, p. 1649 et seqq.; Grill, Gramlich, & Eller, 1995, p. 296; Mertes, 2015, p. 816; Ossenbrink, 2016, p. 266).

3.4.4.1 Scope of the AIFM Tax Adaptation Act (AIFM-StAnpG)

The Investment Tax Act (Investmentsteuergesetz (InvStG)) is to be applied to organisms (Raab, 2010, p. 25; Hagen, Groseta, Schilling, & Jenett, 2015, p. 676; Jesch T. , 2015, p. 46) for collective investment in transferable securities (UCITS) as defined by §1 para. 2 Capital Investment Code (KAGB), as well as alternative investment funds (AIF) in §1 para. 2 clause 1 InvStG (Haase & Dorn, 2015, p. 39 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22; Raab, 2010, p. 25; Hagen, Groseta, Schilling, & Jenett, 2015, p. 676; Port & Steinlein, 2015, p. 79 et seqq.). Partial special assets (§96 para. 2, clause 1 KAGB) and sub funds, so-called sub fund assets, (§§ 117, 132 KAGB) as well as comparable foreign, legally separate units are considered as UCITS, respectively AIF (Haase & Dorn, 2015, p. 39 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22; Raab, 2010, p. 25; Hagen, Groseta, Schilling, & Jenett, 2015, p. 676; Port & Steinlein, 2015, p. 79 et seqq.).

In the reversal of understanding, the concept AIF includes all investment assets, with the exception of UCITS (Haase & Dorn, 2015, p. 39 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22; Raab, 2010, p. 25; Hagen, Groseta, Schilling, & Jenett, 2015, p. 676; Port & Steinlein, 2015, p. 79 et seqq.). An accordant definition (Haase & Dorn, 2015, p. 39 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22; Raab, 2010, p. 25; Hagen, Groseta, Schilling, & Jenett, 2015, p. 676; Port & Steinlein, 2015, p. 79 et seqq.) can also be found in the Capital Investment Code (KAGB, §1 para. 1 no. 3 KAGB). The German Federal Financial Supervisory Agency (Bundesanstalt für Finanzen (BaFin)) notes that the term organism in this context is neither concretized by the AIFM Directive nor by the Capital Investment Code (KAGB) and submits its opinion in its interpretative letter (BaFin, 2013) dated 14 June 2013 regarding the scope of the Capital Investment Code (KAGB) and the term of investment fund (Haase & Dorn, 2015, p. 39 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22; Raab, 2010, p. 25; Hagen, Groseta, Schilling, & Jenett, 2015, p. 676; Port & Steinlein, 2015, p. 79 et seqq.). To qualify as AIF, the following characteristics are required (Haase & Dorn, 2015, p. 39 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22; Raab, 2010, p. 25; Hagen, Groseta, Schilling, & Jenett, 2015, p. 676; Port & Steinlein, 2015, p. 79 et seqq.):

- Organism,
- for collective investments.
- collection of capital,
- from a number of investors,

- defined investment strategy,
- investment for the benefit of the investors,
- and no company operating outside the financial sector (Simonis, Grabbe, & Faller, 2014, pp. 16-22).

Although the Investment Tax Act (InvStG) should be unambiguous, it prevents a legally watertight tax law by including the non-definite terms AIF or UCITS, thus the lacking definition (Haase & Dorn, 2015, p. 39 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22; Raab, 2010, p. 25; Hagen, Groseta, Schilling, & Jenett, 2015, p. 676; Port & Steinlein, 2015, p. 79 et seqq.) of organism and investment asset criticized by the Federal Institute of Finance (Bundesanstalt für Finanzen (BaFin)). At this point it is necessary for the determination of the scope of the Investment Tax Act (InvStG) at a national as well as European level, to resort (Haase & Dorn, 2015, p. 39 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22; Raab, 2010, p. 25; Hagen, Groseta, Schilling, & Jenett, 2015, p. 676; Port & Steinlein, 2015, p. 79 et seqq.) to the interpretations of the regulatory authorities BaFin and ESMA (European Securities and Markets Authority).

Not included in this scope are corporate subsidiaries pursuant to §1a, para. 1 UBGG (Law on Investment Companies, Gesetz über Unternehmensbeteiligungsgesellschaften), which usually acquire, hold, manage or dispose of interests in companies (Haase & Dorn, 2015, p. 39 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22; Raab, 2010, p. 25; Hagen, Groseta, Schilling, & Jenett, 2015, p. 676; Port & Steinlein, 2015, p. 79 et seqq.). Furthermore, Venture Capital firms are excluded, which acquire interests with equity capital or state assistance in the public interest (Haase & Dorn, 2015, p. 39 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22; Raab, 2010, p. 25; Hagen, Groseta, Schilling, & Jenett, 2015, p. 676; Port & Steinlein, 2015, p. 79 et seqq.). Even companies, which - in accordance with §1 para. 19 no. 36 KAGB – sole purpose is to conduct securitization business, are not implicated (Haase & Dorn, 2015, p. 39 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22; Raab, 2010, p. 25; Hagen, Groseta, Schilling, & Jenett, 2015, p. 676; Port & Steinlein, 2015, p. 79 et seqq.; Jesch T., 2015, p. 46).

3.4.4.2 *Differentiation of Investment Vehicles*

Preliminary Remarks

The Investment Tax Act (InvStG) now differentiates between vehicles (Höring J. , 2016, p. 2; Otto, 2013, p. 253) that fulfill the fiscal criteria on so-called mutual funds pursuant to §1, para. 1b Investment Tax Act, and other investment funds in which these tight requirements are not given (Majcen, 2007, p. 47 et seqq.; Höring J., 2016, p. 2; Simonis, Grabbe, & Faller, 2014, pp. 16-22; Otto, 2013, p. 253; Baumhoff, Drücker, & Köhler, 2010, p. 122). Since the amendment, which was transitioned by the AIFM Directive, the term investment trust is being used for investment funds pursuant to §1 para. 1c Investment Tax Act (Majcen, 2007, p. 47 et seqq.; Höring J., 2016, p. 2; Simonis, Grabbe, & Faller, 2014, pp. 16-22; Otto, 2013, p. 253; Baumhoff, Drücker, & Köhler, 2010, p. 122). The Investment Tax Act (InvStG) so far included only the so-called limited transparency principle (Baumhoff, Drücker, & Köhler, 2010, p. 122) in regards to taxation (Majcen, 2007, p. 47 et seqq.; Höring J., 2016, p. 2; Simonis, Grabbe, & Faller, 2014, pp. 16-22; Otto, 2013, p. 253; Baumhoff, Drücker, & Köhler, 2010, p. 122). Now both, the taxation based on the limited transparency principle and the taxation for investment trusts are being regulated under the Investment Tax Act (Majcen, 2007, p. 47 et seqq.; Höring J., 2016, p. 2; Simonis, Grabbe, & Faller, 2014, pp. 16-22; Otto, 2013, p. 253; Baumhoff, Drücker, & Köhler, 2010, p. 122). Only for such investment funds that meet the strict requirements of a mutual fund, the limited transparency principle applies in accordance with §1 para. 1b clause 1 Investment Tax Act (Majcen, 2007, p. 47 et seqq.; Höring J., 2016, p. 2; Simonis, Grabbe, & Faller, 2014, pp. 16-22; Otto, 2013, p. 253; Baumhoff, Drücker, & Köhler, 2010, p. 122). For investment trusts that do not meet the restrictive fiscal requirements for their part, the legislative authorities have provided an innate form of taxation within the Investment Tax Act (Majcen, 2007, p. 47 et seqq.; Höring J., 2016, p. 2; Simonis, Grabbe, & Faller, 2014, pp. 16-22; Otto, 2013, p. 253; Baumhoff, Drücker, & Köhler, 2010, p. 122). The provisions hereto reverberate in §§18 and 19 of the Investment Tax Act (InvStG) and are being largely treated in the process as ordinary partnerships or corporations in fiscal matters (Majcen, 2007, p. 47 et seqq.;

Höring J., 2016, p. 2; Simonis, Grabbe, & Faller, 2014, pp. 16-22; Otto, 2013, p. 253; Baumhoff, Drücker, & Köhler, 2010, p. 122).

3.4.5 Subsumption in Germany Tax Regulations according to the AIFM Tax Adaption Act

3.4.5.1 Capital Investment Companies

Capital investment companies according to the definition of §19 para. 1 clause 1 InvStG (Investment Tax Act) are all companies including special assets characterized, which are in negative delimitation, not personal investment companies as defined in §18 InvStG (Kleine, Schulz, & Krautbauer, 2015, p. 140 et seqq.; Port & Steinlein, 2015, p. 79 et seqq.; Zetzsche, 2015, p. 466 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22).

Capital investment companies (Kapital-Investitionsgesellschaften) in the organization form of a domestic special asset are considered special-purpose assets and are subject to full tax obligations (Kleine, Schulz, & Krautbauer, 2015, p. 140 et seqq.; Port & Steinlein, 2015, p. 79 et seqq.; Zetzsche, 2015, p. 466 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22). Under certain circumstances, business tax is due as well (Kleine, Schulz, & Krautbauer, 2015, p. 140 et seqq.; Port & Steinlein, 2015, p. 79 et seqq.; Zetzsche, 2015, p. 466 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22). Thus, German special and mutual funds are not tax exempt a priori (Kleine, Schulz, & Krautbauer, 2015, p. 140 et seqq.; Port & Steinlein, 2015, p. 79 et seqq.; Zetzsche, 2015, p. 466 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22). Failure to discharge the exigencies for the characteristics as an investment fund poses a considerable tax risk (Kleine, Schulz, & Krautbauer, 2015, p. 140 et seqq.; Port & Steinlein, 2015, p. 79 et seqq.; Zetzsche, 2015, p. 466 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22). This is also the case, if the investors themselves are exempt from tax (Kleine, Schulz, & Krautbauer, 2015, p. 140 et seqq.; Port & Steinlein, 2015, p. 79 et seqq.; Zetzsche, 2015, p. 466 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22). Foreign capital investment companies that are not corporations are considered as assets which may be subject to taxation with their domestic income as an individual tax subject (Kleine, Schulz, & Krautbauer, 2015, p. 140 et seqq.; Port &

Steinlein, 2015, p. 79 et seqq.; Zetzsche, 2015, p. 466 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22; Höring J., 2013, p. 56 et seqq.) in accordance with §49 of the EStG (Einkommensteuergesetz (Income Tax Act)). Therefrom, four constructs can be derived (Kleine, Schulz, & Krautbauer, 2015, p. 140 et seqq.; Port & Steinlein, 2015, p. 79 et seqq.; Zetzsche, 2015, p. 466 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22; Höring J., 2013, p. 56 et seqq.):

- Domestic Investment Corporation.
- Domestic special assets.
- Foreign special assets in corporate form.
- Foreign special assets in contractual form (Höring J., 2013, p. 56 et seqq.).

Wherein the Luxembourg or French Fond Commun de Placement (FCP) characterizes such a contractually regulated construct in terms of a foreign investment fund (Kleine, Schulz, & Krautbauer, 2015, p. 140 et seqq.; Port & Steinlein, 2015, p. 79 et seqq.; Zetzsche, 2015, p. 466 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22; Höring J., 2013, p. 56 et seqq.). The current uncertainty regarding the qualification as a corporate tax subject was resolved by the AIFM Tax Adaption Act. Restrictively has to be noted that this regulation only applies to investment companies and by no means to investment funds (Kleine, Schulz, & Krautbauer, 2015, p. 140 et seqq.; Port & Steinlein, 2015, p. 79 et seqq.; Zetzsche, 2015, p. 466 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22; Höring J., 2013, p. 56 et seqq.).

For investors this new regulation now means that although the taxation is basically pursuing existing fiscal legal standards, it is subject to a number of special provisions (Kleine, Schulz, & Krautbauer, 2015, p. 140 et seqq.; Port & Steinlein, 2015, p. 79 et seqq.; Zetzsche, 2015, p. 466 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22; Höring J., 2013, p. 56 et seqq.). The applicability of the provisions for the determination of tax-sheltered income pursuant to §3 no. 40 EStG and §8 Corporate Tax Act (Körperschaftsteuergesetz, KStG) regarding received dividends and capital gains is dependent on the fact that the investor of capital investment companies, which are located in the European Union or the European Economic Area, provides evidence that this company is subject to corporation income tax at their place of registration and is not exempt from paying (Kleine, Schulz, & Krautbauer, 2015, p.

140 et seqq.; Port & Steinlein, 2015, p. 79 et seqq.; Zetzsche, 2015, p. 466 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22; Höring J., 2013, p. 56 et seqq.). If the capital investment company resides in a third country, the law requires the proof, that it is subject to taxation by at least 15% (Kleine, Schulz, & Krautbauer, 2015, p. 140 et seqq.; Port & Steinlein, 2015, p. 79 et seqq.; Zetzsche, 2015, p. 466 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22; Höring J., 2013, p. 56 et seqq.). It is not specifically regulated, whether it is to be based on the actual taxation or the nominal tax rate (Kleine, Schulz, & Krautbauer, 2015, p. 140 et seqq.; Port & Steinlein, 2015, p. 79 et seqq.; Zetzsche, 2015, p. 466 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22; Höring J., 2013, p. 56 et seqq.). Especially with accumulated losses or a different income determination, this can be significant (Kleine, Schulz, & Krautbauer, 2015, p. 140 et seqq.; Port & Steinlein, 2015, p. 79 et seqq.; Zetzsche, 2015, p. 466 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22; Höring J., 2013, p. 56 et seqq.). It stands to reason that the German legislature - in delimitation to the provisions of the Foreign Transactions Tax Act (Außensteuergesetz (AStG)), which will follow - did not want to underlay the determination of the actual taxation according to German tax principles, by stating in its legislative intent that the capital investment company has to be subject to "… a corporate tax rate of at least 15% if the residence is registered in a third country…" (Deloitte, 2014), in order to benefit from the fiscal advantages of §3 no. 40 EStG and §8b KStG (Kleine, Schulz, & Krautbauer, 2015, p. 140 et seqq.; Port & Steinlein, 2015, p. 79 et seqq.; Zetzsche, 2015, p. 466 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22; Höring J., 2013, p. 56 et seqq.).

In regards to the taxation of foreign sourced income, this means that even if tax exemptions on dividends and capital gains are denied, an applicability of the Germany Foreign Tax Act (Außensteuergesetz (AStG)) may occur (Kleine, Schulz, & Krautbauer, 2015, p. 140 et seqq.; Port & Steinlein, 2015, p. 79 et seqq.; Zetzsche, 2015, p. 466 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22; Höring J., 2013, p. 56 et seqq.). The occasion for this applicability is the fact that for capital investment companies notwithstanding §7 para. 7 AStG (Moser, 2015, p. 102 et seqq.; Cortez, 2013, p. 131 et seqq.), which generally declares that the Investment Tax Act (InvStG) takes priority over the Foreign Transaction Tax Act (AStG), the provisions regarding the taxation of foreign sourced income shall remain applicable (Kleine, Schulz,

& Krautbauer, 2015, p. 140 et seqq.; Port & Steinlein, 2015, p. 79 et seqq.; Zetzsche, 2015, p. 466 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22; Höring J., 2013, p. 56 et seqq.). To avoid a national double taxation in this context, the distributions and capital gains shall be tax-exempt in those cases where the Foreign Tax Act is applicable (Kleine, Schulz, & Krautbauer, 2015, p. 140 et seqq.; Port & Steinlein, 2015, p. 79 et seqq.; Zetzsche, 2015, p. 466 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22; Höring J., 2013, p. 56 et seqq.), however, a seven-year period must be observed for the exemption (Endres, 2014, pp. 86-87).

3.4.5.2 Investment Partnerships

Investment limited partnerships as well as comparable foreign legal forms which do not meet the provisions of §1 para. 1b InvStG (Investmentsteuergesetz (Investment Tax Act)) and therefore are subject to §18 clause 1 InvStG qualify as investment partnerships (Haase & Dorn, 2015, p. 197 et seqq.; Kleine, Schulz, & Krautbauer, 2015, p. 141 et seqq.; Zetsche, 2015, p. 467 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22). Their taxation, respectively the taxations of their investors follows the general principles for partnerships and demands a separate and uniform establishment of earnings as well as a potential business tax (Haase & Dorn, 2015, p. 197 et seqq.; Kleine, Schulz, & Krautbauer, 2015, p. 141 et seqq.; Zetsche, 2015, p. 467 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22).

Due to the reference to investment limited partnerships and similar foreign legal forms §18 clause 1 InvStG contains a restricted admission, so that all other legal forms are considered as capital investment companies as defined in §19 of the InvStG (Haase & Dorn, 2015, p. 197 et seqq.; Kleine, Schulz, & Krautbauer, 2015, p. 141 et seqq.; Zetsche, 2015, p. 467 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22; Dahm & Hamcher, 2014, p. 60 et seqq.; Moser, 2015, p. 102 et seqq.). The problem at this point is that if this rule would be taken very strictly, those closed-end funds which were launched in the form of a limited partnership (Gesellschaft mit beschränkter Haftung & Companie Kommanditgesellschaft (GmbH & Co. KG)) with a limited liability company as general partner prior to the introduction of the Capital Investment Code (KAGB) and were not yet converted under supervisory regulations or enjoy grandfathering terms of their legal form, would have to be classified as capital investment companies (Haase & Dorn, 2015, p. 197 et seqq.; Kleine, Schulz, & Krautbauer, 2015, p. 141 et seqq.; Zetsche, 2015, p. 467 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22; Dahm & Hamcher, 2014, p. 60 et seqq.; Moser, 2015, p. 102 et seqq.). The unusual case would arise, that a partnership, which represents a limited partnership (GmbH & Co. KG) with a limited liability company as general partner, would be classified as a capital investment company and thus would be subject to taxation of a corporation (Haase & Dorn, 2015, p. 197 et seqq.; Kleine, Schulz, & Krautbauer, 2015, p. 141 et seqq.; Zetsche, 2015, p. 467 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22; Dahm & Hamcher, 2014, p. 60 et seqq.; Moser, 2015, p. 102 et seqq.). The legislative authorities do leave a desideratum (Kleine, Schulz, & Krautbauer, 2015, pp. 141-142) here as well (Haase & Dorn, 2015, p. 197 et seqq.; Zetsche, 2015, p. 467 et seqq.; Simonis, Grabbe, & Faller, 2014, pp. 16-22; Dahm & Hamcher, 2014, p. 60 et seqq.; Moser, 2015, p. 102 et seqq.).

3.4.5.3 Income Tax Treatment of Private Equity Funds

Even after the implementation of the Capital Investment Code (KAGB) and the legal validity of the AIFM Tax Adaption Act (AIFM-StAnpG), Private Equity funds (Pelikan, 2007, p. 104 et seqq.) are usually constructed as a closed fund in the legal form of a partnership (Mardini, personal communication, 2014; February 27 and May 28; Haase, 2014, p. 197 et seqq.; Pelikan, 2007, p. 104 et seqq.; Tcherveniachki, 2007, p. 43 et seqq.). Typically, the General Partner is not an actual person, but a legal person (Mardini, personal communication, 2014; February 27 and May 28; Haase, 2014, p. 197 et seqq.; Pelikan, 2007, p. 104 et seqq.; Tcherveniachki, 2007, p. 43 et seqq.), the limited liability company (Gesellschaft mit beschränkter Haftung (GmbH)). Thus, the fund can be constituted as a limited liability company with a limited partnership company (GmbH & Co. KG), in which – in addition to the general provisions of the German Commercial Code (Handelsgesetzbuch (HGB)) for the limited partnership – some regulatory specificities by the Capital Investment Code (§§149 et seq. KAGB) are added (Mardini, personal communication, 2014; February 27 and May 28; Haase, 2014, p. 197 et seqq.; Pelikan, 2007, p. 104 et seqq.; Tcherveniachki, 2007, p. 43 et seqq.). The investment limited partnership (Mardini, personal communication, 2014; February 27 and May 28; Haase, 2014, p. 197 et seqq.; Pelikan, 2007, p. 104 et seqq.; Tcherveniachki, 2007, p. 43 et seqq.) can be marked as a supervisory modified special form of a normal limited partnership (with a limited liability company as general partner) according to the German Commercial Code (§§161 et seq. HGB). Through §18 Investment Tax Act (InvStG) the general tax regulations for partnerships are applied to a German investment limited partnership – and comparable foreign legal forms, in particular limited partnerships – as, for example, are applicable for normal limited partnerships (Mardini, personal communication, 2014; February 27 and May 28; Haase, 2014, p. 197 et seqq.; Pelikan, 2007, p. 104 et seqq.; Tcherveniachki, 2007, p. 43 et seqq.) with a limited liability company as general partners (Hechl, 2012, p. 13 et seqq.; Fehrenbacher & Tavakoli, 2014, pp. 20 et seqq., 74 et seqq.; Köllen, Vogl, & Wagner, 2010, pp. 17-18). The general partner (limited liability company) can participate (Mardini, personal communication, 2014; February 27 and May 28; Haase, 2014, p. 197 et seqq.; Pelikan, 2007, p. 104 et seqq.; Tcherveniachki, 2007, p. 43 et seqq.; Hechl, 2012, p. 43 et seqq.; Fehrenbacher & Tavakoli, 2014, pp. 20 et seqq.; Köllen, Vogl, & Wagner, 2010, pp. 17-18) with all its assets or a portion thereof in the limited partnership (Kommanditgesellschaft (KG)). Assets in kind may also be contributed (Hechl, 2012, p. 43 et seqq.; Fehrenbacher & Tavakoli, 2014, pp. 20 et seqq.; Köllen, Vogl, & Wagner, 2010, pp. 17-18). In the case of a conversion of an existing limited liability company (GmbH) to a limited partnership with a limited liability company as general partner (GmbH & Co. KG) it could well be to only contribute the current assets (Hechl, 2012, p. 43 et seqq.; Fehrenbacher & Tavakoli, 2014, pp. 20 et seqq.; Köllen, Vogl, & Wagner, 2010, pp. 17-18) of the limited liability company (GmbH) to the limited partnership (KG) and to leave the capital assets with the limited liability company (GmbH). In all cases, no contribution of the limited liability company (GmbH) must be made (Hechl, 2012, p. 43 et seqq.; Fehrenbacher & Tavakoli, 2014, pp. 20 et seqq.; Köllen, Vogl, & Wagner, 2010, pp. 17-18). The limited liability company (GmbH) could, as contribution to the limited partnership (KG) take over the management and the personnel (Hechl, 2012, p. 43 et seqq.; Fehrenbacher & Tavakoli, 2014, pp. 20 et seqq.; Köllen, Vogl, & Wagner, 2010, pp. 17-18). On the part of the limited partners, the compulsory contribution denotes the amount a limited partner has to contribute to the company (Hechl, 2012, p. 43 et seqq.; Fehrenbacher & Tavakoli, 2014, pp. 20 et seqq.; Köllen, Vogl, & Wagner, 2010, pp. 17-18). This value, also entered into the commercial register, is at once the sum with which the respective limited partner is personally liable (Hechl, 2012, p. 43 et seqq.; Fehrenbacher & Tavakoli, 2014, pp. 20 et seqq.; Köllen, Vogl, & Wagner, 2010, pp. 17-18). The limited partnership with a limited liability company as general partner (GmbH & Co. KG) is represented by the limited liability company (general partner), which typically (Hechl, 2012, p. 43 et seqq.; Fehrenbacher & Tavakoli, 2014, pp. 20 et seqq.; Köllen, Vogl, & Wagner, 2010, pp. 17-18) has the sole power (Lenz, 2015, p. 445 et seqq.; Rübenstahl, 2014, p. 1088 et seqq.) of management (§164 HGB). The limited partner is usually excluded from the management (Hechl, 2012, p. 43 et seqq.; Fehrenbacher & Tavakoli, 2014, pp. 20 et seqq.; Köllen, Vogl, & Wagner, 2010, pp. 17-18; Lenz, 2015, p. 445 et seqq.). Online, in exceptional business ventures,(Hechl, 2012, p. 43 et seqq.; Fehrenbacher & Tavakoli, 2014, pp. 20 et seqq.; Köllen, Vogl, & Wagner, 2010, pp. 17-18; Lenz, 2015, p. 445 et seqq.; Rübenstahl, 2014, p. 1088 et seqq.) he may exercise his veto right (§164 clause 1 HGB). This means, provided that there are not contractual agreements stating otherwise, that the director of the limited liability company (GmbH) is indirectly the managing director of the limited partnership (KG) as well (Hechl, 2012, p. 43 et seqq.; Fehrenbacher & Tavakoli, 2014, pp. 20 et seqq.; Köllen, Vogl, & Wagner, 2010, pp. 17-18; Lenz, 2015, p. 445 et seqq.; Rübenstahl, 2014, p. 1088 et seqq.). None of the shareholders in their own are entitled to these assets of the company (Hechl, 2012, p. 43 et seqq.; Fehrenbacher & Tavakoli, 2014, pp. 20 et seqq.; Köllen, Vogl, & Wagner, 2010, pp. 17-18; Lenz, 2015, p. 445 et seqq.; Rübenstahl, 2014, p. 1088 et seqq.). All partners are entitled to the assets in joint ownership (Hechl, 2012, p. 43 et seqq.; Fehrenbacher & Tavakoli, 2014, pp. 20 et seqq.; Köllen, Vogl, & Wagner, 2010, pp. 17-18; Lenz, 2015, p. 445 et seqq.; Rübenstahl, 2014, p. 1088 et seqq.). A typical feature of the company is that the limited liability company (GmbH), as a general partner, is not granted the participation in the sharing of assets (Hechl, 2012, p. 43 et seqq.; Fehrenbacher & Tavakoli, 2014, pp. 20 et seqq.; Köllen, Vogl, & Wagner, 2010, pp. 17-18; Lenz, 2015, p. 445 et seqq.; Rübenstahl, 2014, p. 1088 et seqq.). The treatment of the assets is regularly part of contractual agreement (Hechl, 2012, p. 43 et seqq.; Fehrenbacher & Tavakoli, 2014, pp. 20 et seqq.; Köllen, Vogl, & Wagner, 2010, pp. 17-18; Lenz, 2015, p. 445 et seqq.; Rübenstahl, 2014, p. 1088 et seqq.).

The ultimate goal of constructors of a limited partnership with a limited liability company as general partner (GmbH & Co. KG) in the context of Private Equity funds is the classification as an asset management company. If the activities of the fund are to be qualified as a business, the profit shares of the shareholders belong among the current income deriving from business activities pursuant to §15 para. 1, no. 2, clause 1 EStG (Bundesministerium für Finanzen, 2003; Zetsche, 2015, p. 464 et seqq.; Bernhardt, 2010, p. 141 et seqq.; Jesch, 2004, p. 157 et seqq.),

- if individuals are involved in the fund and if the dividend of the shareholder contains gains from the disposal of shares in corporations and dividends, then such gains are liable to the reg method in pursuant with §3, no. 40 EStG,
- if an incorporation is involved in the fund, dividends and profits from the disposal of shares in capital companies are free from tax by 95% pursuant to §8b KStG,
- and if taxpayers with a limited tax obligation are involved in a domestic Private Equity fund, the profits are to be participated as trading income pursuant to §49 para. 1, no. 2, letter a EStG (Bundesministerium für Finanzen, 2003; Zetsche, 2015, p. 464 et seqq.; Bernhardt, 2010, p. 141 et seqq.; Jesch, 2004, p. 157 et seqq.).

The fund's income is subject to trade tax (Bundesministerium für Finanzen, 2003; Zetsche, 2015, p. 464 et seqq.; Bernhardt, 2010, p. 141 et seqq.; Jesch, 2004, p. 157 et seqq.) in accordance with §2 para. 1 clause 2 Trade Tax Act (Gewerbesteuergesetz (GewStG)). This, naturally, does not apply for the targeted asset management company, which is exempt from trade tax (Bundesministerium für Finanzen, 2003; Zetsche, 2015, p. 464 et seqq.; Bernhardt, 2010, p. 141 et seqq.; Jesch, 2004, p. 157 et seqq.). If the occupations of the fund are classified as asset management in conformity with the overall picture of the operation, the current shares of the participants of the fund are classified as income deducted from §20 of the EStG, insofar as they are concerned with the bonus paid by the investee (Bundesministerium für

Finanzen, 2003; Zetsche, 2015, p. 464 et seqq.; Bernhardt, 2010, p. 141 et seqq.; Jesch, 2004, p. 157 et seqq.). These profits (Bundesministerium für Finanzen, 2003; Zetsche, 2015, p. 464 et seqq.; Bernhardt, 2010, p. 141 et seqq.; Jesch, 2004, p. 157 et seqq.) require in procedural regards a single, separate determination pursuant to §179, respectively §180 of the General Tax Code (Abgabenordnung (AO)).

If unlimited income tax payers are involved in the fund, which do not hold the participation in the fund in business assets, the sale of the investments in the portfolio companies only leads to taxable income, if it is a private disposal (§23 EStG) or a participation pursuant to §17 EStG (Bundesministerium für Finanzen, 2003; Zetsche, 2015, p. 464 et seqq.; Bernhardt, 2010, p. 141 et seqq.; Jesch, 2004, p. 157 et seqq.). The dividend is in full amount subject to the withholding tax of 25% (Bundesministerium für Finanzen, 2003; Zetsche, 2015, p. 464 et seqq.; Bernhardt, 2010, p. 141 et seqq.; Jesch, 2004, p. 157 et seqq.).

3.4.6 Fiscal Regulation Parameters for Private Equity Funds in Germany

Table 1: Taxation at a Private Equity Fund Level

TAXATION ON A PRIVATE EQUITY FUND LEVEL		
VAT ON MANAGEMT FEES	PAYMENT YES	RECLAIM YES
CAPITAL GAINS TAX	MIN 1,14%	MAX 1,65%
WITHHOLDING TAX	26,375%	
VALUE ADDED TAX		MAX 19%
STAMP DUTIES OR TRANSACTION TAXES	STAMP NO – TRANSACTION NO	
ANTI-ABUSE RULES	YES	

Source: Own representation based on EVCA Tax Benchmark Study, 2013.

Table 2: Taxation at a Company Level

TAXATION ON A COMANY LEVEL		
COMPANY TAX	MIN 22,825%	MAX 32,975%

Source: Own representation based on EVCA Tax Benchmark Study, 2013.

Table 3: Taxation of Employees

TAXATION OF EMPLOYEES		
INCOME TAX	MIN 0%	MAX 47,475%
CAPITAL GAINS TAX	MIN 26,375%	MAX 28,485%

Source: Own representation based on EVCA Tax Benchmark Study, 2013.

In order to capture the taxation of such a structure, one has to make a distinction between the taxation at company level (table 2) and the taxation at fund level (table 1). Herein, mainly the capital gains tax, the corporation tax, as well as the value added tax - which is responsible to management fees and amounts according to §12 para. 1 UStG (Umsatzsteuergesetz (Value Added Tax Act)) 19% in Germany - and the withholding tax need to be observed (Deloitte, 2009, pp. 1-67; Bernhardt, 2010, p. 136 et seqq.). Since the GmbH & Co. KG (Limited Partnership with a limited liability company as general partner) represents a partnership, the taxation of the shareholders is undoubtedly interesting (Deloitte, 2009, pp. 1-67; Bernhardt, 2010, p. 136 et seqq.). The spreadsheets above require some explanation: for example, it needs to be added, that at fund level profit distributions are tax-free in accordance with §8b KStG (Körperschaftsteuergesetz (Corporate Tax Act)). However, in compliance with §8b para. 3 KStG, this tax exemption is limited to 95% of the gross revenue (Grützner, 2014, p. 94 et seqq.). The figures relating to the capital gains in table 1 result from the corporate tax rate according to §23 para. 1 KStG of 15% plus a solidarity surcharge of 5.5% (Grützner, 2014, p. 94; EVCA, 2013, p. 84) and the trade tax at a tax rate between 7% and 17.15% (§16 GewStG –Gewerbesteuergesetz (Trade Tax Act)). To obtain the tax rates for capital gains (EVCA, 2013, p. 84), the result of corporate tax (EVCA, 2013, p. 84) plus solidarity surcharge must be multiplied by 5% and supplemented by the respective trade tax (15% * 5,5% + 7% = 22,825% * 5% = 1,14% or the very + 17,15% trade tax = 32,975% * 5% = 1,65%). The fact that at this point the corporate taxes are higher than shown in chapter 3.3.3.5 is due to an almost unique principle (Collier, Schulemann-Adlhoch, Fresow, &

Bergup, 2012, p. 162 et seqq.) of a levy rate in Germany in accordance with §16 GewStG (Grützner, 2014, p. 116 et seqq.; EVCA, 2013, pp. 82-86). This municipal rate differs from city to city (Bergemann & Wingler, 2012, p. 694 et seqq.; Janson, 2009, p. 108 et seqq.) and also changes the corporate tax rate. The calculation of the withholding tax, however, is quite simple. The base tax rate according to §32d para. 1 EStG (Einkommensteuergesetz (Income Tax Act) of 25% will be supplemented by the solidarity tax already mentioned above, adding up to a rate of 26.375% (Birk, Desens, & Tappe, 2014, p. 238 et seqq.; Grützner, 2014, p. 94). The fiscal treatment at company level can be gathered from the previous elucidations (22,825%-32,975%). Although individuals (table 3) will hardly be involved in such a transaction, the tax rates shall be explained briefly for reason of comparison. The 47.475% results from the arithmetic operation of the top tax rate of 45% plus 5.5% solidarity surcharge (Wildmann, 2015, p. 210 et seqq.), whereas such a top tax rate is applied only for very high-income individuals.

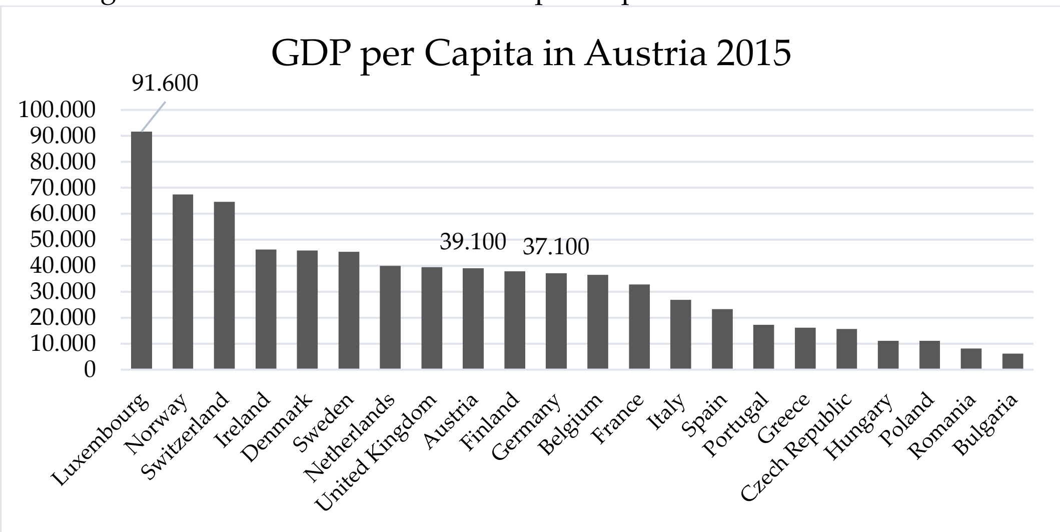
3.5 OVERVIEW AND REGULATORY ENVIRONMENT FOR PRIVATE EQUITY IN AUSTRIA

3.5.1 **Performance Features: Private Equity in Austria**

3.5.1.1 Preliminary Remarks

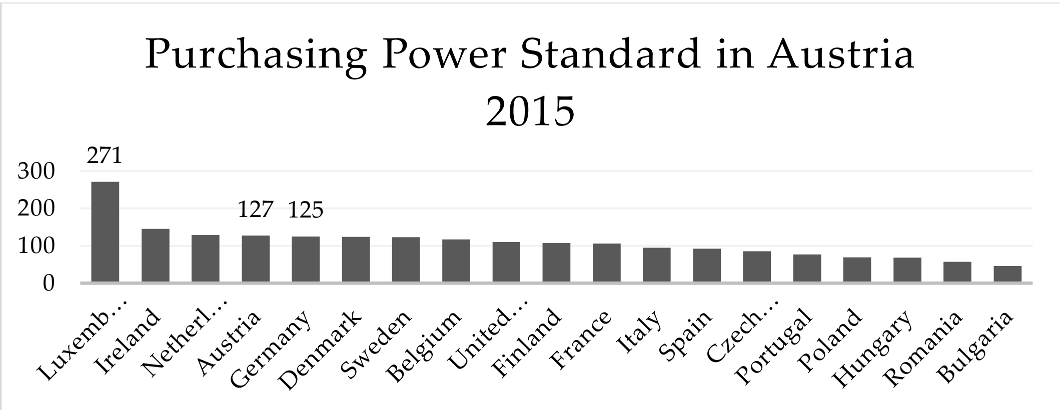
At first glance, Austria is not the first choice when it comes to undertaking investments. In this context, other countries are often mentioned as an economic and financial location. Mostly Germany, the UK, France, Luxembourg, or outside the European Union (EU), Switzerland or the USA are identified. Funds, especially Private Equity funds are rarely associated with Austria (Boué A. R., 2013, p. 1; Haider, 2011, p. 1). However, considering the economic data, at least in terms of investment opportunities, a whole different picture presents itself. As a parameter for the economic performance of a country, the gross domestic product (GDP) is being applied. With its GDP of approximately 340 billion Euros at market prices, Austria does not approach the big five of the European Union, but competes within the range of Member States such as Poland and Belgium in the lower third, although these states achieve an even higher GDP (Eurostat, 2016). However, if the performance is considered from a more differentiated view – namely in relation to the GDP per capita – Austria is performing relatively well within the EU (figure 85).

Figure 85: Gross Domestic Product per Capita in Austria 2015



Source: Own representation based on Eurostat, 2015.

Figure 86: Purchasing Power Standard in Austria 2015



Source: Own representation based on Eurostat, 2015.

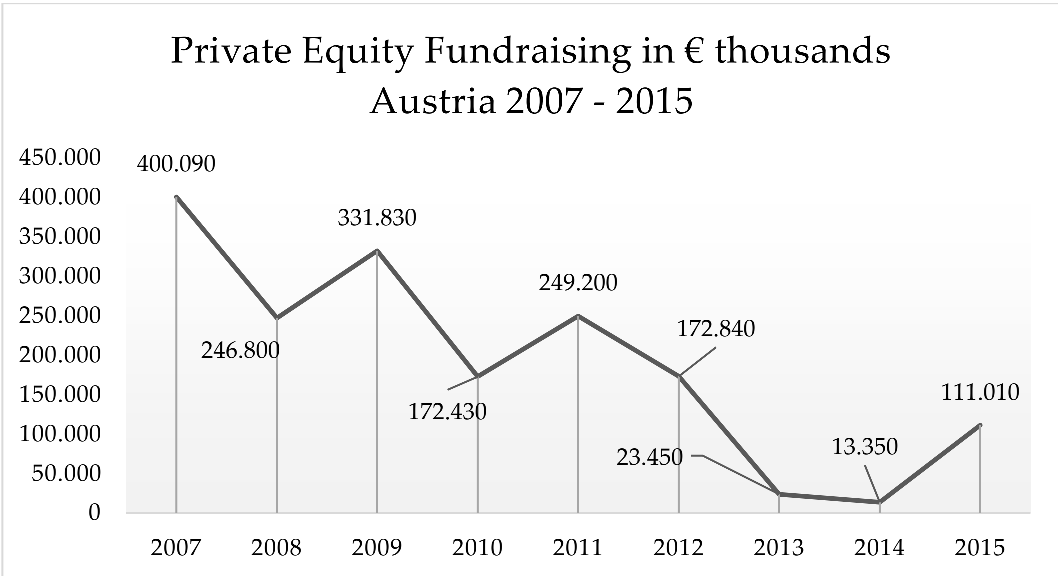
With this indicated value, Austria takes one of the top places – apart from Luxembourg – and does so relatively well ahead of the overall product leader Germany (Bergau, 2015, p. 2). Measured in purchasing power standard (PPS), Austria ranks even a bit better in the leading group of the entire European Union (figure 86).

So based on these parameters and evaluated by its political-economic options, Austria is quite capable of turning towards the undisputedly growth-effective Private Equity transactions. Whether this succeeds in Austria shall be examined as part of a positioning.

3.5.1.2 Positioning of Private Equity in Austria

The leading players of the Austrian Private Equity industry are organized (Jungwirth, 2006, p. 95 et seqq.; AVCO, 2016) in the Austrian Private Equity and Venture Capital Organization (AVCO).

Figure 87: History of Private Equity Fundraising to 2015 Austria



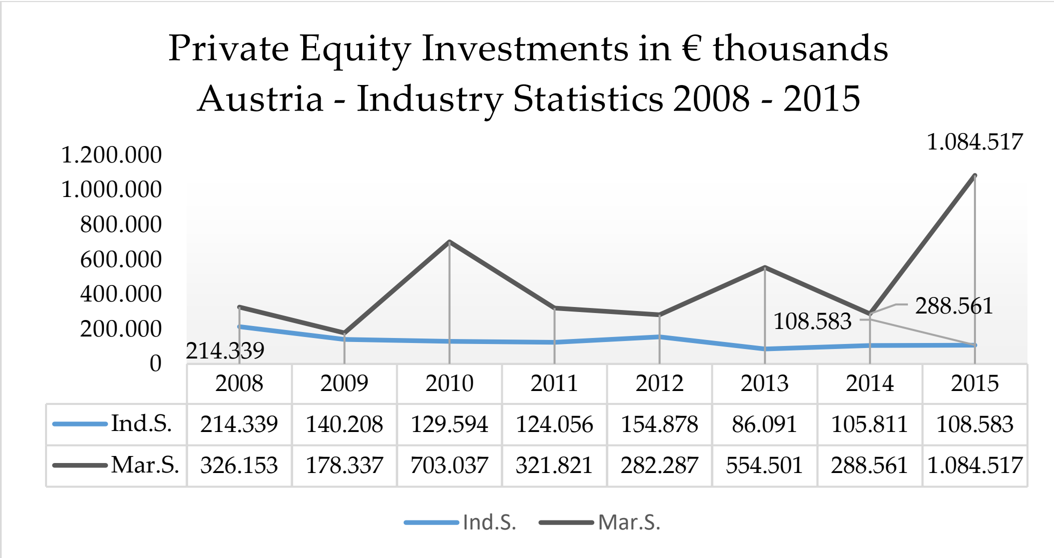
Source: Own representation based on Invest Europe, 2016.

Among these members are, besides consultants, Private Equity firms (Jungwirth, 2006, p. 95 et seqq.; AVCO, 2016).

The sums of money collected for their funds can be taken from figure 87, whereas the numbers are to be understood in thousands of euros.

Also in Austria, fundraising recovered temporarily shortly after the crisis, just to crash in to near insignificance thereafter, compared to the pre-crises times (Komarek, 2011). In 2015, it was slightly better. Figure 88 presents the investment activities of the Private Equity firms since 2008 in terms of the industry statistics and market statistics.

Figure 88: PE Investments Industry Statistics and Market Statistics Austria



	2008	2009	2010	2011	2012	2013	2014	2015
Ind.S.	214.339	140.208	129.594	124.056	154.878	86.091	105.811	108.583
Mar.S.	326.153	178.337	703.037	321.821	282.287	554.501	288.561	1.084.517

Source: Own representation based on Invest Europe, 2016.

The Austrian Private Equity market invests a majority within its own country and - according to Bernd Lechner (Lechner, 2011, pp. 1-32) investment manager (vc-magazin, 2011, pp. 1-3) with EK fin – also concentrates on already existing portfolios. This adoption is also assisted by the fact that the fundraising is almost equal to the investment of the Austrian-based investment companies (see also the figures 87 and 88). It can therefore be understood as a very cautious market. Also in figure 88, the investments in thousands of euros are present which have incurred according to the place of the portfolio company.

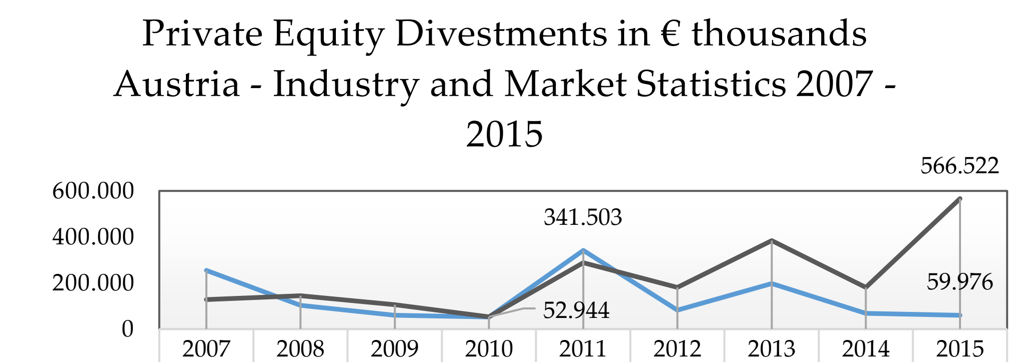
The approach from the perspective of the target companies also shows that there was growth in activity after the crisis. However, Austrian up- and downward movements are particularly due to individual investments. If it had not been for an investor from the United States in 2010, the trend towards fewer investments would have continued on (avco.at).

Interpretation

In 2008, the share of investments of Austrian holding companies in the gross domestic product (GDP) in Austria amounted to a mere 0.139%. In the following years like the post-crisis year 2009 it was 0.05% and 2013 0.03%. In 2015 it was 0.032%. Thus, in 2008, 46.60 €, 16.59 € in 2009 and just 10.19 € in 2013 were invested per capita. In 2015 it was 12.66 €.

In Austria-based portfolio companies, the share of investments in the GDP in 2008 amounted to 0.321%, 0.06% in 2009 and 0.172% in 2013. In 2015 it was 0.321%. Thus, in 2007, 107.14 €, 21.10 € in 2009 and 65.61 € in 2013 were invested per capita. In 2015 it was 126.40 €.

Figure 89: PE Divestments – Industry and Market Statistics Austria



	2007	2008	2009	2010	2011	2012	2013	2014	2015
Ind.S.	254.330	102.237	60.052	52.104	341.503	82.049	197.503	67.376	59.976
Mar.S.	128.547	144.899	105.755	52.944	287.441	180.850	384.779	181.494	566.522

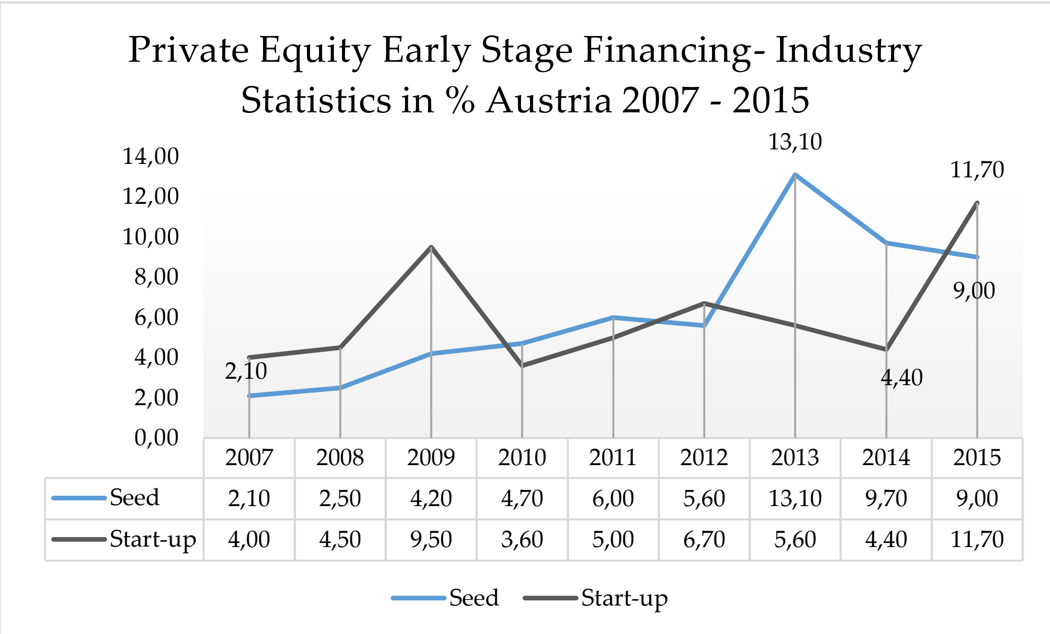
Source: Own representation bases on Invest Europe, 2016.

The initially discussed question whether Austria invests well in Private Equity due to its high per capita GDP and high productivity can be negated. This also eliminates that Austria achieves such high marks in the above parameters due to its growth-pushing Private Equity engagement, and in conclusion, roams the market with even less commitment than Germany. Austria thus remains below its potential. The divestments shown in figure 89 rather do not have such a significant informational value in the Austrian area, precisely because the few large players invest in and out.

Early-stage Financing

It must be examined at this point whether the weak Private Equity market in Austria uses the few resources that are being provided at least in the Early Stage financing (figure 90). It was investigated how high the proportion of the total investment in the Early Stages in percent really is.

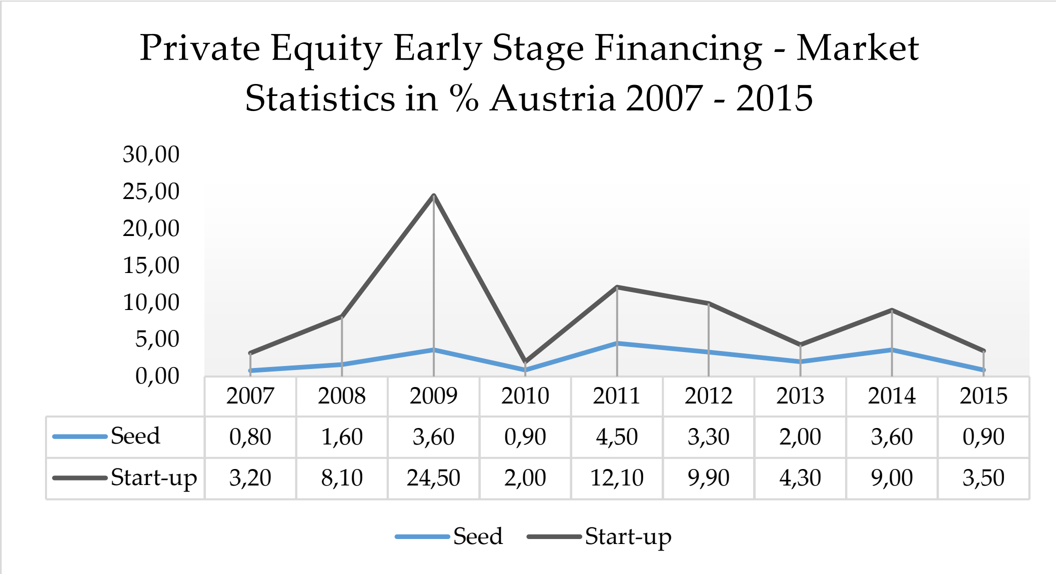
Figure 90: PE Early Stage Financing – Industry Statistics in % Austria



	2007	2008	2009	2010	2011	2012	2013	2014	2015
Seed	2,10	2,50	4,20	4,70	6,00	5,60	13,10	9,70	9,00
Start-up	4,00	4,50	9,50	3,60	5,00	6,70	5,60	4,40	11,70

Source: Own representation based on own calculation.

Figure 91: PE Early Stage Financing Market Statistics Austria in %



	2007	2008	2009	2010	2011	2012	2013	2014	2015
Seed	0,80	1,60	3,60	0,90	4,50	3,30	2,00	3,60	0,90
Start-up	3,20	8,10	24,50	2,00	12,10	9,90	4,30	9,00	3,50

Source: Own representation based on own calculation.

In principle, it is observed that in Austria – if based on the total investments of the holding companies and those invested in portfolio companies – the investment behavior during the Early Stages seed and start-up – see figure 90 and figure 91 – is inversely related to the total investments. This means that the investments in the early stages increase as the overall willingness to invest decreases. It is particularly striking that – similar to Germany – there was an increase in investments during the crisis situation. It is well noticeable that last in 2013, Austrian investment companies invested a great percentage of the total investments – 12.97% (in 2015, the number is with 9.0% slightly lower) of all investments, after all – in the seed phase of companies.

For the Austrian entrepreneur this means that in Austria– provided that, despite the low propensity to invest, he can organize the financing of his project via means of Private Equity at all – he generally must hope for a knock-on financing during the early stages of his business. In Austria, there is a pronounced uncertainty regarding not only the tax regulation of Private Equity funds (Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 18).

3.5.2 Alternative Investment Fund Managers Act (AIFM-G)

3.5.2.1 Preliminary Remarks

Austria responded to the AIFM Directive and passed a bill just before the expiration of the deadline for the implementation of appropriate measures to regulate the managers of all alternative investment products, including Private Equity funds (Majcen & Bohrn, 2013, pp. 1-9). It was designed to implement this Directive. The Alternative Investment Fund Managers Act (Alternative Fonds Manager Gesetz (AIFM-G)) became effective on July 22, 2013 (Majcen & Bohrn, 2013, pp. 1-9; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 196) and organized the managers of alternative investment funds (AIF). It shall be repeated shortly that AIF represents all collective investments that are not undertakings (Majcen & Bohrn, 2013, pp. 1-9; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, pp. 1 et seqq.; Trübestein, 2012, p. 355) for collective investment in transferable securities (UCITS). UCITS are known in Austria as investment funds and are arranged by the Investment Funds Act (Majcen & Bohrn, 2013, pp. 1-9; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, pp. 1 et seqq.; Trübestein, 2012, p. 355; Busack & Kaiser, 2012, p. 614). The primary goal of the AIFMA is therefore, to regulate the aforementioned manager Act (Majcen & Bohrn, 2013, pp. 1-9; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, pp. 1 et seqq.; Trübestein, 2012, p. 355; Busack & Kaiser, 2012, p. 614). This law requires managers of alternative investment funds to hold a specific AIFM concession with the Financial Market Supervision Act (Majcen & Bohrn, 2013, pp. 1-9; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, pp. 1 et seqq.; Trübestein, 2012, p. 355; Busack & Kaiser, 2012, p. 614).

The scope of the AIFM-G is rather broad. There are quite occasional difficulties in distinguishing whether a product belongs to the area of application of the AIFM-G Act or to another regulation (Majcen & Bohrn, 2013, pp. 1-9; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, pp. 1 et seqq.; Trübestein, 2012, p. 355; Busack & Kaiser, 2012, p. 614). The scope includes highly liquid hedge funds as well as funds that invest in illiquid assets such as real estate, infrastructure or indeed Private Equity Act (Majcen & Bohrn, 2013, pp. 1-9; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, pp. 1 et seqq.; Trübestein, 2012, p. 355; Busack & Kaiser, 2012, p. 614).

3.5.2.2 Scope of Application of the AIFM-G

Right at the beginning of the AIFM-G, the AIF is defined; the AIF is considered as such if it is an undertaking for collective investment, not a UCITS and collects capital from many investors who invest in it for the benefit according to a predetermined investment strategy without serving directly to the operating activities (Majcen & Bohrn, 2013, pp. 1-9; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, pp. 1 et seqq.; Trübestein, 2012, p. 355; Busack & Kaiser, 2012, p. 614). It makes no difference whether the AIF is constructed as an open- or closed-end type, in which contractual form it was established and which legal structure the manager of the AIF has (Majcen & Bohrn, 2013, pp. 1-9; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, pp. 1 et seqq.; Trübestein, 2012, p. 355; Busack & Kaiser, 2012, p. 614).

The most important features for the presence of an AIF (Gunter, 2007, p. 93) are that (Majcen & Bohrn, 2013, pp. 1-9; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, pp. 1 et seqq.; Trübestein, 2012, p. 355; Busack & Kaiser, 2012, p. 614, Gunter, 2007, p. 93)

- capital is collected from some investors, whereas there is no precise information about how many investors there may disire. If ergo no number designation is made, it can be assumed that even a small number of investors will suffice,
- a predetermined investment strategy is followed for the gain of the investors,
- the collected capital is not "directly" served in operating activities. The term "directly" clearly points out that the investments used to invest in turn in other projects do not constitute directness. Consequently, a Private Equity fund is to be understood as AIF, since the directness is not given,

- it does not matter which legal form is at hand. Since this has been defined more than once, it can be assumed that exceptions should be rather excluded Fund Structures in Austria (Majcen & Bohrn, 2013, pp. 1-9; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 1 et seqq.; Trübestein, 2012, p. 355; Busack & Kaiser, 2012, p. 614, Gunter, 2007, p. 93).

3.5.2.3 Preliminary Remarks

Venture Capital funds can be set in at least three different ways (Brechbühl & Wooder, 2004, p. 37; Brähler, 2006, p. 230 et seqq.; Halbmeyer, 2014, p. 29 et seqq.) in Austria (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Tojner & Moser, 2013, p. 13 et seqq.). Specifically, for Venture Capital activities an option was created. The others denote forms of company law, which are open to any company for the design of its fiscal and legal framework. Starting with the specific risk capital structure, the three alternatives involve (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Tojner & Moser, 2013, p. 13 et seqq.; Brechbühl & Wooder, 2004, p. 37; Brähler, 2006, p. 230 et seqq.; Halbmeyer, 2014, p. 29 et seqq.):

- SME Financing Corporation (Mittelstandsfinanzierungsgesellschaft (MFG)),
- Austrian Joint Stock Corporation (österreichische Kapitalgesellschaft) and the
- Austrian Asset Management Partnership (österreichische vermögensverwaltende Personengesellschaft).

Which of these alternatives is particularly useful and beneficial for Private Equity, can be ascertained based on standards (Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 1 et seqq.). If these standards are checked, respectively applied in advance, then a compatibility will emerge. Accordingly, relevant standards for Private Equity are (Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 1 et seqq.):

- Private Equity funds are usually limited partnership constructions,
- organized as closed-end funds,
- the cash flows of fund are following the principle of Capital Call and Return on Exit,
- Private Equity funds are tax-efficient as far as possible and,
- justify no permanent establishment for international investors (Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 1 et seqq.).
- Corporate Governance provides executive committees (Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 1 et seqq.).

Private Equity funds avoid undue restrictions of the investment activities (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.)

3.5.2.4 SME Financing Corporation (MFG)

To finally build a bridge to a Private Equity structure reasonable for the future, not only existing structures need to be investigated, but also former promising approaches. Such an approach (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.) may have been the Austrian SME finance corporation (Mittelstandsfinanzierungsaktiengesellschaft (MiFiG)). It was regulated in the Corporate Tax Act (Körperschaftssteuergesetz (KStG)) pursuant to §5 n. 14 in conjunction with §6b KStG (Körperschaftsteuergesetz old) and has existed in this form only in Austria. Created in 1993, the MiFiG once was the dominant fund structure in Austria, which was used by the vast majority of the Austrian Venture Capitalists (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.). One of its outstanding characteristics was that it was exempt from corporate taxation in regards to income from investments (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner &

Moser, 2013, p. 13 et seqq.). In addition, this structure possessed the concession of a start-up period for income from assessment of liquid assets, provided the various regulatory provisions and relations of §6b KStG, were adhered to in the course of the fund activities (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.). Provided that certain conditions were met, an exemption from capital tax and the transaction fees for certain transactions flanked these benefits (Boué, Kehlbeck, & Leonharts-berger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.).

These advantages have also been noticed by the European Commission (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.). Already at the beginning of the new millennium, this construct was under examination because it was suspected that it would violate the European State Aid Law (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.). The assumptions and suspicions were confirmed and the European Commission and the Austrian authorities finally agreed to abolish the MiFiG (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesen-bichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.). There was a transition period until December 31, 2013 for this construct (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.). Simultane-ously, with the State Aid Law-compliant SME Financing Corporation (MFG) a new vehicle was created (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.). The new regulation is based on the Community Guidelines on State Aid to deliver risk capital investments in small and medium-sized enterprises (Official Journal No. C 194 of August 18, 2006), whose objectives are state aid risk capital to eliminate market failure (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.).

However, the MFG regulations provide for a tax exemption of income just as before. Nevertheless, some new regulatory provision in some aspects are restrictive (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.):

- Under company law, a MFG has to be arranged in the form of a corporation or a limited liability company (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.).
- The acquisition or increase of holdings shall not exceed 1.5 million euros per year (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.).
- Investments may not be concluded committed to, as far as this predetermined maximum extend has already been exhausted by participation in one or more SME financing companies or the provision of other aid (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.).
- Investments may at maximum amount to 49% of the operating assets or the nominal capital of the investee and may not provide a dominant position (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.).

- Investments may not be provided to companies in difficulties according to the Guidelines on State Aid for rescuing and restructuring of firms in difficulty, as well as to enterprises in the fields of shipbuilding, coal and steel (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.).
- Shares may only be acquired in unlisted small and medium-sized enterprises with residence in Member States of the European Union or States of the European Economic Area under observation of certain investment provision (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.).
- Furthermore, the MFG and the MFG Law 2007 do not constitute a perpetual right, because the provisions were only effective until the end of 2013, respectively for investments existing at this time until the first fiscal year beginning after December 31, 2018 (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.).

Now that those provisions are interwoven with the previously described standards for risk capital activities, it is clear that there are merely some cases that produce compatibility (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.). While usually, the forms of Private Equity funds are limited partnerships, MFG must be constructed as corporations (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.). More important in this context however is that corporations are characterized by the maintenance of capital principle, which is why a Capital Call and Return on Exit can only be prepared with difficulty (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl &

Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.). Dividend distributions are possible only after a shareholders' meeting and only where there is a cumulative profit at the previous reporting date and not after each conducted exit, as is customary in Private Equity funds (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.). Capital injections require a considerable administrative effort and are not easily used for management fees or the financing of a planned Venture Capital transaction (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.).

A well-nigh fulminant downside is that corporations are not, as already negatively noted in regard to German constructions, tax transparent, but pose at the level of the fund a taxable entity (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.). Through the additional regulation, that the income from investment is tax-exempt, this is mitigated to some extent (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.).

The above-mentioned management fee is first and foremost to be charged with the sales tax (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.). Just as the MiFiG, the MFG provides no special provisions for VAT (value added tax (VAT), Umsatzsteuergesetz (UStG)) exemption in this regard (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.). The fiscal authority causes some legal uncertainty regarding the VAT handling of management fees, as it has become – contrary to previous practices to grant sales tax exemptions under §6 para. 1 no. 8 respectively, §6 para.1 no. 28 UStG – increasingly critical (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.). Mainly affected are the fund managers who usually charge this as a fixed fee (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.). This fragile handling causes a relative planning and legal uncertainty (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.).

These described restrictions create on one hand corresponding additional financial expenditures for the fund management which has to be absorbed (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.). On the other hand, substantial difficulties arise due to the limitations of the current investment activities under the MFG-structure corresponding to the European legal provisions regarding state aid (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.). Additionally, there are also the time constraints due to the expiry of the MFG regulations (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.). To establish an order of magnitude for individual holdings, specific activity segments or even regional areas for investment companies means to significantly limit the scope of action for Private Equity, respectively for the investors (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.).

If a fund management risks an investment with its investment strategy despite all those regulations and restrictions, it cannot respond in situations where a portfolio company requires an increase in capital (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.). Even if a syndication with a company that is not a MFG is theoretically possible, the risk remains to weaken its own position under company law in the course of an increase in capital (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.). If the corporation is a MFG, however, syndication is not possible (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.). A key point in the consideration of this construct is, that by the minority interest rule, whereas the interest may not be higher than 1.5 million euros, as listed above under the new regulations, a restriction on funding opportunities will be made in a target company (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.). This may carry glaring drawbacks for the evolution and growth of these start-up enterprises and for the investors (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.). Thus, if a Private Equity investor would want to setup an MFG in Austria, he would experience difficulties in fundraising (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.). Through the accumulation of all these constraints it is likely that the willingness to invest in terms of such a construct will be rather modest, since these regulations and restrictions do not lead to a fund management being able to establish itself or to deliver a brilliant performance (Boué, Kehlbeck, & Leonhartsberger-Heilig, 2012, p. 58 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 141 et seqq.; Brechbühl & Wooder, 2004, p. 37; Tojner & Moser, 2013, p. 13 et seqq.).

Conclusion: The MFG or MiFiG (both names are used interchangeably from Jud, Marchart, Friesenbichler, & Peneder) is not well received in Austria. The new regulations, such as the funding restrictions or the lack of syndication possibilities cause mistrust in this type of legal form and hardly lead to the willingness to invest (Tojner & Moser, 2013, pp. 15-16).

3.5.2.5 Austrian Joint Stock Corporation

In principle, the Austrian Joint Stock Corporation (österreichische Kapitalgesellschaft) is structurally for Private Equity funds to be rated the same as the MFG (Brähler, 2006, p. 230 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 145). This, however, is also true for the administrative difficulties with the preservation of capital (Brähler, 2006, p. 230 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 145). The difference is that the Austrian Joint Stock Corporation, as opposed to the MFG, is not exempt from taxes (Brähler, 2006, p. 230 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 145). It would be more advantageous, however, that this legal form is not restrictively affected by restrictive regulations and therefore can invest in conceivable businesses (Brähler, 2006, p. 230 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 145). It could also utilize general tax advantages, such as the international intercorporate privilege (Brähler, 2006, p. 230 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 145). As this corporation lacks tax transparency and is thus often subject to withholding tax, it cannot be said that it is – especially for international investors – worth investing in such forms (Brähler, 2006, p. 230 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 145). Some barriers shall be mentioned here (Brähler, 2006, p. 230 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 145):

- Equity injections cause 1% corporation tax on the proprietary equity investment (Brähler, 2006, p. 230 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 145).
- The management fee for independent management companies is VAT-burdened and increases the costs of the fund management by 20%, since the

fund vehicle has no or only limited tax deduction (Brähler, 2006, p. 230 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p.).

- Company law provisions provide significant discrepancies with the Corporate Governance Standards of Private Equity business (Brähler, 2006, p. 230 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 145).

As part of a joint-stock company, the supervisory board has in contrast to the advisory board significant decision-making authority, which in particular involves the obligation to obtain consent to corporate investments (Brähler, 2006, p. 230 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 145). As part of a limited liability company, the management or in case of Private Equity funds, the fund management, is bound by instructions to the owners, respectively the investors (Brähler, 2006, p. 230 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 145). These company law provisions are in contradiction to the separation of decision and control usually found in Private Equity business (Häberle, 2008, p. 661).

Conclusion: Although the Austrian corporation may invest in all companies regardless of size or type, it holds major disadvantages caused by lack of tax transparency (Brähler, 2006, p. 230 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 145). The fact that restrictive regulations impede the work, complicates matters even more so that this type of legal from for Private Equity transactions is rather unattractive from the standpoint of an investor (Brähler, 2006, p. 230 et seqq.; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 145).

3.5.2.6 Austrian Asset Management Partnership

Internationally, being a Limited Partnership (LP), describes the Austrian partnership in form of a Private Limited Partnership (KG) in Austria (Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 146 et seqq.). As in Germany it operates usually as a GmbH & Co. KG (Baumann, Raab, & Simader, 2013, p. 291; Brinskele, 2011, p. 10 et seqq.). Like the Limited Partnership (Boué, Kehlbeck & Leonhartsberger-Heilig), the Austrian Asset Management Partnership (österreichische vermögensverwaltende Personengesellschaft) is characterized by the principle of capital maintenance (Frank, 2009, p. 35) so it can be designed as a closed –end fund without major administrative expenses in which the cash flows are organized according to the Capital Call and Return on Exit system (Baumann, Raab & Simader, 2013, p. 292). The Corporate Governance can be set according to the usual principles of the Private Equity business (Sullivan & Lim, 2014), because it allows for the relations between the stakeholders and the processes within a partnership to be designed by contract and the investment activities of the investors are not restricted by special provisions (Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 146).

Partnerships are tax transparent according to Austrian income tax principles (Bendlinger & Kofler, 2005). The problem regarding permanent establishment could still occur. This, however, applies only to foreign investors. A permanent establishment exists, if the partnership qualifies as commercially active and not only as asset management. The Austrian Income Tax Regulations only provide a general abstract guidance for distinguishing between commercial operations and asset management (Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 146).

3.5.2.7 Income Tax Treatment of Private Equity Funds

The Income Tax Directive (Einkommensteuerrichtlinie - EStR Rz 5418 et seqq.) reads:

Asset management occurs if assets are used and defines an activity directed at collecting benefits from intrinsic values which are to be maintained (Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 146). *Operative activities based in the assets are characterized by exploitation of substantial assets through reallocation or through additional activities and services beyond the duties and responsibilities of the administration* (Österreichischer Steuerverein, 2015).

There is a significant legal uncertainty – as in Germany (Zagl, 2010, p. 922) – in the assessment whether it is a commercial activity or straight asset management (Rapp, 2009, p. 58). In Austria it is handled in such a way that in assessing the facts, the appropriate tax office is called upon in advance to discuss the situation (Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 146). It has been shown that the tax offices in Austria react very differently to this subject (Österreichischer

Steuerverein, 2015; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 146 et seqq.; Zagl, 2010, p. 922 et seqq.). As an appealable information notice in accordance with §118 Federal Tax Code (Bundesabgabenordnung (BAO)) cannot be obtained, it results in the unsatisfactory situation that the fund initiator would have to hope on a tax office to act in his favor (Österreichischer Steuerverein, 2015; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 146 et seqq.; Zagl, 2010, p. 922 et seqq.).

It is possible that capital gains from investments in foreign target companies are tax-exempt (Varga, 2005, p. 1) for Austrian investors (Österreichischer Steuerverein, 2015; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 146 et seqq.; Zagl, 2010, p. 922 et seqq.). This is the case, if an investor, for example, holds a share of 20% in a fund designated as Austrian asset management limited partnership and this fund in turn holds 50% in a holding company (Österreichischer Steuerverein, 2015; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 146 et seqq.; Zagl, 2010, p. 922 et seqq.). Then, the stake in the company calculated through the tax-transparent partnership would be 10%, which in turn corresponds to the minimum contribution for the application of the international intercorporate privilege (Österreichischer Steuerverein, 2015; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 146 et seqq.; Zagl, 2010, p. 922 et seqq.). The sale proceeds of any such participation ratio would thus be tax-exempt for the concerned investor, if the other requirements of §10 KStG are met (Österreichischer Steuerverein, 2015; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 146 et seqq.; Zagl, 2010, p. 922 et seqq.). For instance, if the partner with unlimited liability would plead a management fee with regard to the fund (EVCA, 2013, pp. 33-37), which founded as a limited partnership, it would be free from VAT so that this criterion of tax optimizing (Beiser, 2009, pp. 268-274) would also be discharged (Beiser, 2009, pp. 268-274; EVCA, 2013, pp. 33-37). In such an approach, the management company accepts full liability for the liabilities of the fund (Österreichischer Steuerverein, 2015; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 146 et seqq.; Zagl, 2010, p. 922 et seqq.).

If such a fund is designed as a GmbH & Co. KG, it is liable to corporation tax and thus not entirely tax transparent (Österreichischer Steuerverein, 2015; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 146 et seqq.; Zagl, 2010, p. 922 et seqq.). Similar as in Germany, this structure is quite well a suitable medium for Private Equity (Sauermann, 2010, p. 15). Also in Austria, it takes a negative effect that significant legal uncertainties arise in regard to the assessment of the fund as commercially active or asset management (Österreichischer Steuerverein, 2015; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 146 et seqq.; Zagl, 2010, p. 922 et seqq.; Sauermann, 2010, p. 15).

Conclusion: The Austrian Asset Management Partnership has, as in Germany, the best basis constellation for the Private Equity business (Österreichischer Steuerverein, 2015; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 146 et seqq.; Zagl, 2010, p. 922 et seqq.; Sauermann, 2010, p. 15). The simple design of a closed-end fund is part of this as it is the fiscal transparency regarding income taxation (Österreichischer Steuerverein, 2015; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 146 et seqq.; Zagl, 2010, p. 922 et seqq.; Sauermann, 2010, p. 15). As an obstacle for extensive Private Equity commitments could be the legal uncertainty, which is even greater than in Germany, regarding the assessment of the fund (Österreichischer Steuerverein, 2015; Jud, Marchart, Haslinger, Friesenbichler, & Peneder, 2012, p. 146 et seqq.; Zagl, 2010, p. 922 et seqq.; Sauermann, 2010, p. 15).

3.5.3 Fiscal Regulation Parameters for Private Equity Funds in Austria

Table 4: Taxation at a Private Equity Fund Level

TAXATION AT A PRIVATE EQUITY FUND LEVEL		
VAT ON MANAGEMT FEE	PAYMENT YES	RECLAIM NO
CAPITAL GAINS TAX	25%	
WITHHOLDING TAX	25%	
VALUE ADDED TAX		MAX 20%
STAMP DUTIES OR TRANSACTION TAXES	STAMP YES – TRANSACTION NO	
ANTI-ABUSE RULE	YES	

Source: Own representation based on EVCA Tax Benchmark Study, 2013.

Table 5: Taxation at a Company Level

TAXATION AT A COMANY LEVEL		
COMPANY TAX	25%	

Source: Own representation based on EVCA Tax Benchmark Study, 2013.

Table 6: Taxation of Employees

TAXATION OF EMPLOYEES		
INCOME TAX	MIN 0%	MAX 50%
CAPITAL GAINS TAX	25%	

Source: Own representation based on EVCA Tax Benchmark Study, 2013.

In order to capture the taxation of such a structure, one has to make a distinction between the taxation at company level (table 5) and the taxation at fund level (table 4). Herein, mainly the capital gains tax, the corporation tax, as well as the value added tax – which is applicable to management fees and amounts in according to §10 UStG (Umsatzsteuergesetz (Value Added Tax Act)) 20% in Austria (Kailer & Weiß, 2014, p. 166 et seqq.) – and the withholding tax need to be observed. Although the taxation in Austria is comparatively simple, the origin shall be briefly explained. Thus, capital gains achieved by corporations are subject to the Corporate Tax Act with a tax rate in compliance with §22 KStG (Körperschaftsteuergesetz (Corporate Tax Act)). At fund level, this applies to both, capital gains as well as the withholding tax, which also is based at a tax rate of 25%. The Austrian fiscal authority is restricted to this tax rate even at company level (Lang, Schuch, & Staringer, 2009, p. 50 et seqq.). Workers (table 6) are subject relatively early to the top tax rate of 50% (55% for income above one million Euro) in accordance to §33 para. 1 Income Tax Act (Rogall, 2013, p. 328 et seqq.).

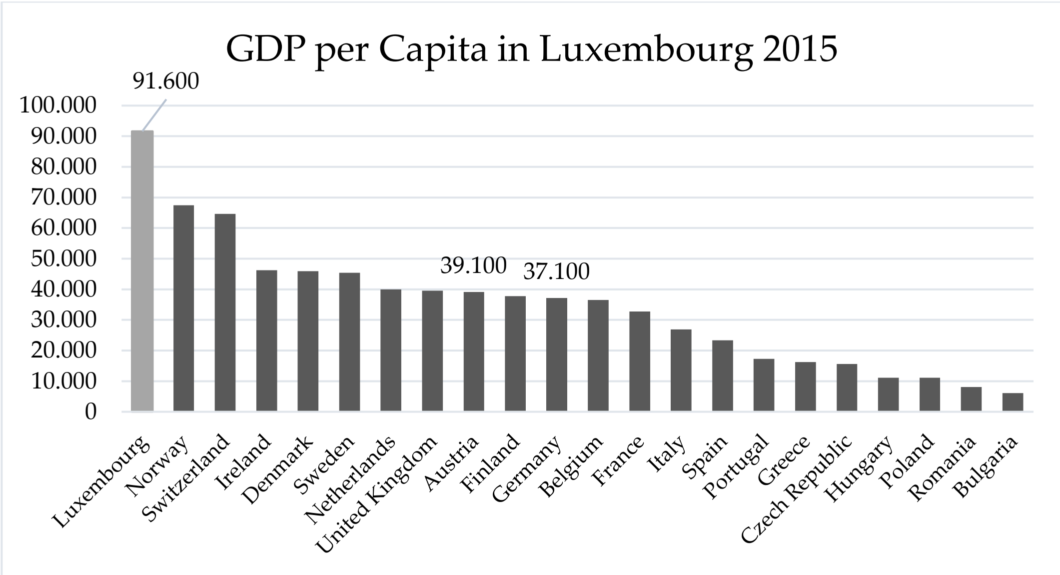
3.6 OVERVIEW AND REGULATORY ENVIRONMENT OF PRIVATE EQUITY IN LUXEMBOURG

3.6.1 **Performance Features: Private Equity in Luxembourg**

3.6.1.1 Preliminary Remarks

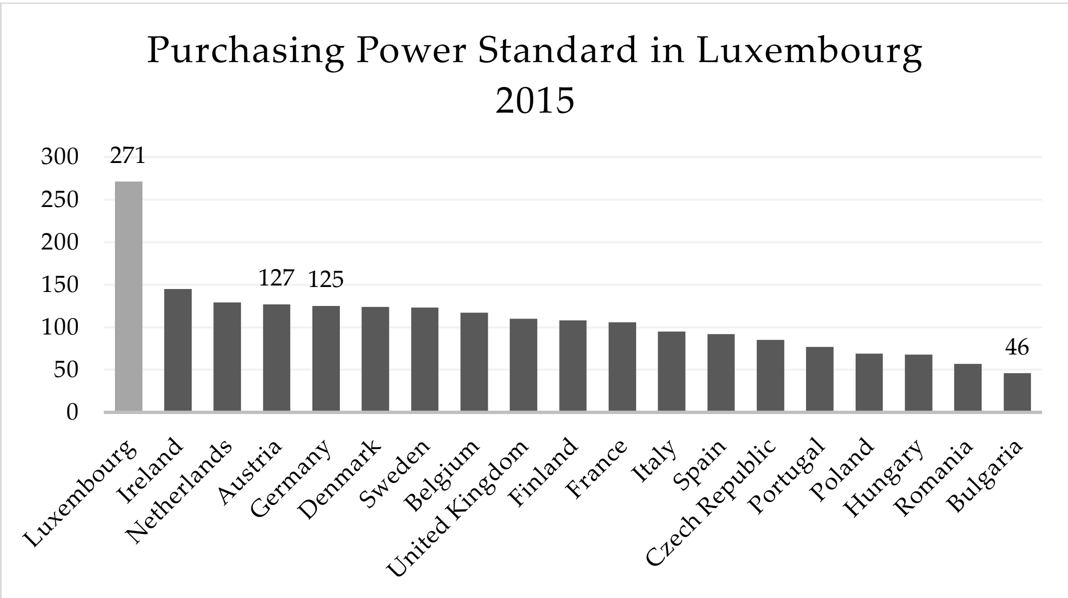
Luxembourg is considered the flag ship country of the Private Equity scene in the European Union. Therefore, Luxembourg is understood as the first address for funds of all kinds – and thus also for Private Equity funds. Beyond that, the economic capacity of this Member State of the European Union is of special interest (Bernhard, 2010, p. 214). At first glance, this small county, spanning merely 2.586 km², with its little more than 500.000 inhabitants has (gouvernement, 2015) compared to the big five – Germany, Great Britain, France, Italy and Spain - a relatively low gross domestic product (GDP). This impression is clearly invalidated by the study of per capita GDP, as figure 92 proves (Eurostat, 2016).

Figure 92: Gross Domestic Product per Capita in Luxembourg 2015



Source: Own representation based on Eurostat.

Figure 93: Purchasing Power Standard in Luxembourg 2015



Source: Own representation based on Eurostat.

Considering the most significant Private Equity countries of the European Union, Luxembourg takes first place by a large margin. In other words, in terms of per capita income of its citizens, Luxembourg is the richest country of the EU. Much responsible for this result is the main industry of Luxembourg - the financial and insurance industries (debelux, 2016; Auswärtiges Amt, 2016).

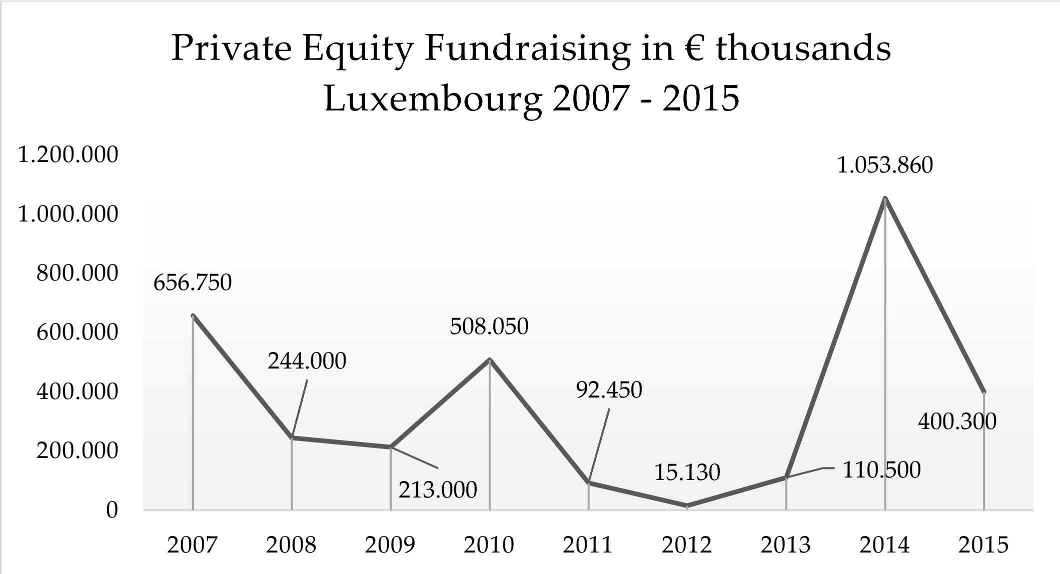
Therefore, the high purchasing power of the country does not come as a surprise. The purchasing power standard (PPS) is, as already explained in chapter Performance features: Private Equity in Germany, a fictitious monetary unit that eliminates distortions from different countries and states 100 as reference (Eurostat, 2016). The higher this value, the higher the purchasing power is above average (Gumpert, 2013, p. 16 et seqq.; Rippl & Seipel, 2008; eurostat, 2015). Luxembourg has the above-average value of 271 (see figure 93).

Whereas the overall GDP was still moderate, the more meaningful GDP per capita and, as shown in figure 93, the purchasing power in Luxembourg are far above those of the countries studied, and thus takes a prominent position in the EU. Is that why Luxembourg holding companies invest a great deal and investments in portfolio companies in Luxembourg are particularly high? According to the per capita income the Luxembourgers could also invest strongly per capita. As part of the positioning, this will be examined.

3.6.1.2 Positioning of Private Equity in Luxembourg

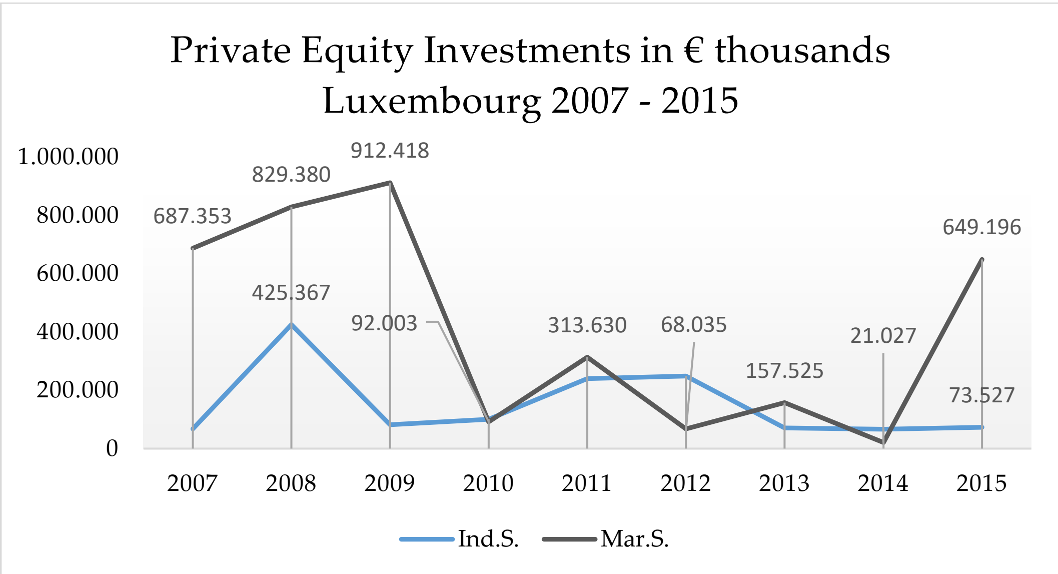
Since 2010, the interests of the Private Equity branch in Luxembourg have been represented by the Luxembourg Private Equity & Venture Capital Association as part of a membership (LPEA, 2015). Among these members are – besides consultants – Private Equity firms. The sums of monies collected by them for their funds can be taken (BVK, 2010, p. 3) from figure 94, whereas the numbers (investeurope, 2016) are to be understood in thousands of euros.

Figure 94: History of Private Equity Fundraising to 2015 Luxembourg



Source: Own representation based on Invest Europe, 2016.

Figure 95: PE Investments Industry Statistics and Market Statistics 2015 Lux.



Source: Own representation based on Invest Europe, 2016.

After the crisis, the recovery of the Private Equity market in regards to fundraising in 2011 represents only a temporary phenomenon. The progress of the curve is similar to that of the German fundraising with the difference that the fundraising appears to be recovering in Luxembourg. However, there are wide variations. An overview of the investments by holding companies and in portfolio companies is given by figure 95. Whereas the numbers are to be understood in thousands of euros.

Regardless of the collected capital, especially during the crisis years, investments were quite high. This is true for the holding companies in 2008 as well as for the investments in portfolio companies, which reached its peak in 2009. This is in stark contrast to the German market, which plummeted during the crisis. Overall, investments range more in the context of fundraising than it is the case, for example, in Germany.

Interpretation

Under examination were the investments executed by Luxembourg-based holding companies and those investments received by portfolio companies in Luxembourg. The Luxembourg data as well are based on the gross domestic product (GDP) and the per capita investment.

While in 2007 the share of investments by Luxembourg holding companies in Luxembourg amounted to 0.188%, the result for 2009 showed a figure of 0.228% and 0.156% in 2013. In 2015 it was 0.14%. Investments per capita amounted to 125.05 € in 2007, 152.32 € in 2009 and 130.95 € in 2013. In 2015 it was 130.60 €.

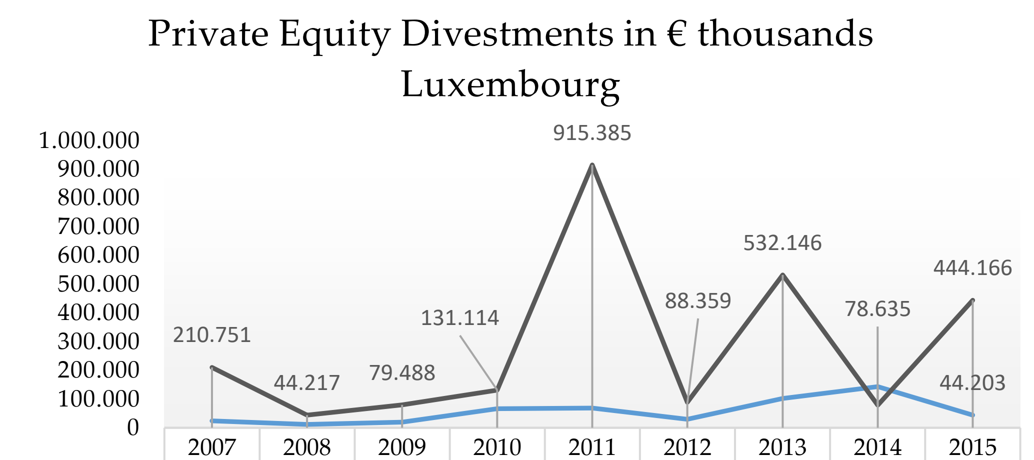
In 2007, 1.91% of the GDP were invested in Luxembourg-based portfolio companies, in 2009 2.53% and in 2013 the percentage amounted to 0.35%. In 2015 it was 1.25%. In 2007, 1272.88 €, in 2009 1689.67 € and 291.71 € in 2013 were invested per capita. In 2015 it was 1.153,10 €.

Overall, it can be stated that the willingness to investment within the meaning of Private Equity is at a higher level in Luxembourg than the Member States previously considered. The percentage of GDP is not strikingly different from, for example, Germany, which is said to show a lower Private Equity commitment.

However, the per capita investments are appreciably higher than in Austria and Germany.

For completion, the divestments shall be shown in figure 96, presenting all divestments in the years from 2007 through 2015 and is also to be understood in thousands of euros.

Figure 96: PE Divestments – Industry Statistics and Market Statistics Luxemb.



	2007	2008	2009	2010	2011	2012	2013	2014	2015
Ind. S.	24.366	11.846	19.277	66.884	68.858	29.845	101.664	143.442	44.203
Mar. S.	210.751	44.217	79.488	131.114	915.385	88.359	532.146	78.635	444.166

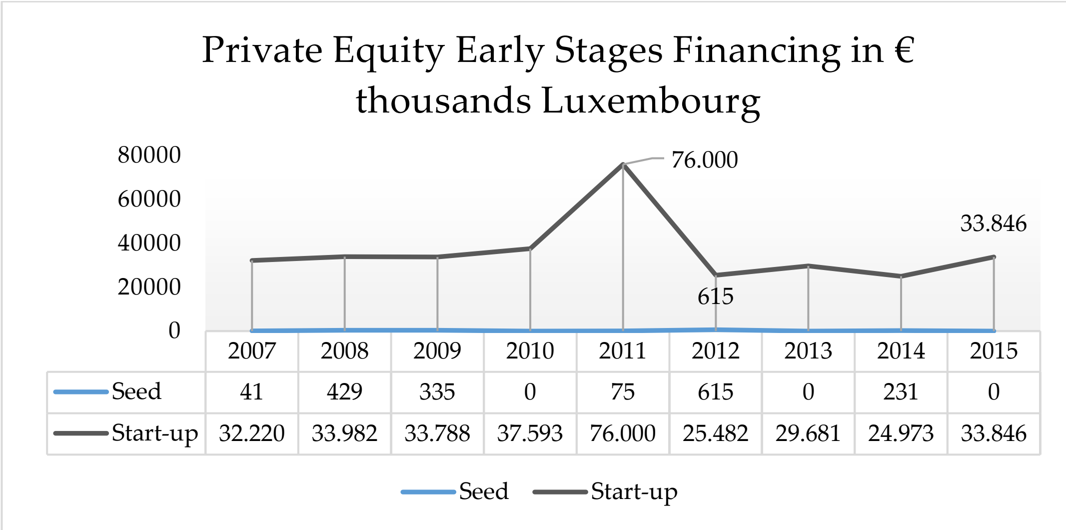
Source: Own representation bases on Invest Europe, 2016.

The divestments – relating to the industry statistics – are stable (see figure 96). This figure follows the investments of the holding companies in Luxembourg.

Early-stage financing

At this point, it is to be investigated if and to what dimension the funds provided in Luxembourg are being engaged in the early stages of a Private Equity financing. In this context, seed and start-up are defined as the early stage (Tcherveniachki, 2007, p. 18 et seqq.; Lerch, 2011, p. 13 et seqq.). The data relating to the industry statistics are shown in figure 97, the data regarding the Luxembourg-based portfolio companies in figure 98.

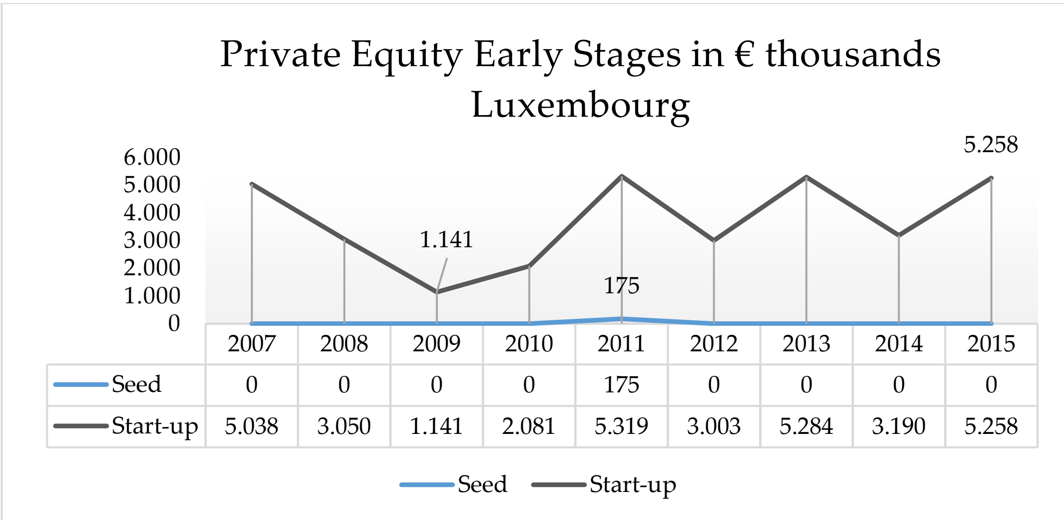
Figure 97: PE Early Stage Financing Industry Statistics Luxembourg



	2007	2008	2009	2010	2011	2012	2013	2014	2015
Seed	41	429	335	0	75	615	0	231	0
Start-up	32.220	33.982	33.788	37.593	76.000	25.482	29.681	24.973	33.846

Source: Own representation based on Invest-Europe, 2016.

Figure 98: PE Early Stage Financing Market Statistics Luxembourg



	2007	2008	2009	2010	2011	2012	2013	2014	2015
Seed	0	0	0	0	175	0	0	0	0
Start-up	5.038	3.050	1.141	2.081	5.319	3.003	5.284	3.190	5.258

Source: Own representation based on Invest Europe, 2016.

In principle, it can be observed that in Luxembourg – if based on the total investments of the holding companies and those invested in portfolio companies – the investment behavior during the early stages, seed and start-up, is similar to the total investments with a slight recovery trend after the interim low in 2012. Particularly striking, yet at the same time little surprising just like the low proportion of investments in the seed stage, is the stronger commitment in the start-up phase. Especially in 2011, divestments were at a higher level, consequently knock-on financing increased and the start-up are received more attention. As Luxembourg is not an industrial country in the classical sense of production and trade, the early stage financings in the country are spread especially among the areas of communications and computer & consumer electronics (OECD, 2010, p. 120).

For the Luxembourg entrepreneur this means, that he has good chances in Luxembourg – provided that he belongs to one of the above mentioned branches – to accomplish his financing through Private Equity. Otherwise, investments – even in the early stage – will probably be targeted abroad. Although the regulations and fiscal environment in Luxembourg may be perceived as exemplary from the outside, Luxembourg was forced to implement the AIFM Directive 2011/61/EU of the European Parliament and Council (Braun K. , 2014, p. 1).

3.6.2 Alternative Investment Fund Manager Act (AIFM-A)

3.6.2.1 Preliminary Remarks

The Börsen-Zeitung reported already on November 23, 2013, that Luxembourg implemented the AIFMD directive on July 10, 2013 as one of the first financial centers in Europe (Kriegmann & Warny, 2013, p. B 7). This early approach – ie the realiziation of the AIFM Directive into Luxembourgian law – was intended to provide transparent and predictable basis for all market participants (Kriegmann & Warny, 2013, p. B 7). In addition, Luxembourg has taken the opportunity to arrange some other parameters. The current laws around the undertakings for collective investment, the funds and the companies for investment in venture capital were basically adapted and the fiscal framework for the established limited partnership was not only modernized, it was introduced to a new special limited partnership, which was then without legal personality (Loyens & Loeff, 2013, p. 1). The new regulations, which caused the AIFM Directive, dealing especially the manager of the fund companies, so that in this context the tax interpretation of profit sharing was clarified (Loyens & Loeff, 2013, p. 1). An essential point of the AIFM Directive is the depositing of assets (Dietrich, 2016, p. 638 et seqq.). Much of the assets represent in Luxembourg alternative investment funds (Arendt & Medernach, 2015, pp. 23-24), which are not financial instruments, so new regulations were introduced (Loyens & Loeff, 2013, p. 1).

3.6.2.2 Implementation of the Alternative Investment Fund Manager Act (AIFM-A)

In order to assess the implementation of the AIFM Directive 2011/61/EU in Luxembourg, it must first be clarified once again, what an AIF and the trustee or manager of such an AIF means. According to Article 4 para. 1 letter a no. i and ii Directive 2011/61/EU investment funds are undertakings for collective investments which collect money from investor and invested for the benefit of investors (Loyens & Loeff, 2013, pp. 1-10; Ende, Niedner, Renner, & Schwabe, 2013, pp 1-69; Kinsch & Nell-Breuning, 2010, p. B4). Beyond this definition, this fund does not require an authorization pursuant to Article 5 of Directive 2009/65/EG, because this authorization is limited to UCITS (Loyens & Loeff, 2013, pp. 1-10; Ende, Niedner, Renner, & Schwabe, 2013, pp 1-69; Kinsch & Nell-Breuning, 2010, p. B4). This opens up the negative delimitation, which has already been discussed elsewhere, also technically (Loyens & Loeff, 2013, pp. 1-10; Ende, Niedner, Renner, & Schwabe, 2013, pp 1-69; Kinsch & Nell-Breuning, 2010, p. B4). The Luxembourgian law firm Loyens & Loeff is in their article on the implementation of the AIFM Directive by definition beyond the explanation of the manager of alternative investment funds, that the Directive (Article 4 para. 1 letter b Directive 2011/61/EU) has to offer, and accordingly states that such a manager can be any legal entitiy which deals mainly with the administration of the above fund. Loyens & Loeff believe that such a manager can be both (Loyens & Loeff, 2013, pp. 1-10; Ende, Niedner, Renner, & Schwabe, 2013, pp 1-69; Kinsch & Nell-Breuning, 2010, p. B4),

- a legal person who has been commissioned by the fund with the management of the fund, i.e. coming from outside, or
- the fund itself occurs as a manager. However, the fund must have the legal conditions for such internal management (Loyens & Loeff, 2013, pp. 1-10; Ende, Niedner, Renner, & Schwabe, 2013, pp 1-69; Kinsch & Nell-Breuning, 2010, p. B4).

Interestingly, the makers of the directive have asked for exceptions in its rules, before the definitions (Article 3 Directive 2011/61/EU). According to Article 3 para. 1 Directive 2011/61/EU, this directive does not apply to managers who manage one or more funds and are even the single investor (Loyens & Loeff, 2013, pp. 1-10; Ende, Niedner, Renner, & Schwabe, 2013, pp 1-69; Kinsch & Nell-Breuning, 2010, p. B4). This also applies to structures with parent companies or affiliates of the manager. As an exception, even those managers can apply, managing the funds, whose (Loyens & Loeff, 2013, pp. 1-10; Ende, Niedner, Renner, & Schwabe, 2013, pp 1-69; Kinsch & Nell-Breuning, 2010, p. B4).

- administrated assets do not exceed a threshold of 100 million euros, or
- whose administrated assets do not exceed a threshold of 500 million euros, do not consist of leveraged funds, and may not exercise any redemption rights for a period of five years from the date of the initial investment in each of such AIF (Loyens & Loeff, 2013, pp. 1-10; Ende, Niedner, Renner, & Schwabe, 2013, pp 1-69; Kinsch & Nell-Breuning, 2010, p. B4).

The manager could cancel the exception regarding the thresholds, unless he fully submits the provisions of the directive to Article 3 para. 4 Directive 2011/61/EU (Loyens & Loeff, 2013, pp. 1-10; Ende, Niedner, Renner, & Schwabe, 2013, pp 1-69; Kinsch & Nell-Breuning, 2010, p. B4). The fact, that the implementation law has extended the Luxembourgian company law to a special limited partnership, is the most spectacular phenomenon (Loyens & Loeff, 2013, pp. 1-10; Ende, Niedner, Renner, & Schwabe, 2013, pp 1-69; Kinsch & Nell-Breuning, 2010, p. B4).

If he does not, however, he is committed to register with the competent authority – in this case the CSSF (Commission de Surveilance du Secteur Financier. During this registration, information is given as (Loyens & Loeff, 2013, pp. 1-10; Ende, Niedner, Renner, & Schwabe, 2013, pp 1-69; Kinsch & Nell-Breuning, 2010, p. B4):

- name and number of funds,
- investment strategy of the fund,

which are incidentally reviewed regularly for their risks (Loyens & Loeff, 2013, pp. 1-10; Ende, Niedner, Renner, & Schwabe, 2013, pp 1-69; Kinsch & Nell-Breuning, 2010, p. B4). The implementation itself is divided into two parts, in which the second part – the change in the laws on UCITS, SIF, SICAR and on commercial companies – has been already discussed in the preliminary remarks. Luxembourg has taken very stringent in its implementation and has implemented the AIFM Directive literally (Loyens & Loeff, 2013, pp. 1-10; Ende, Niedner, Renner, & Schwabe, 2013, pp 1-69; Kinsch & Nell-Breuning, 2010, p. B4).

3.6.2.3 Adjustment SIF Act and SICAR Act

The implementation of the AIFM Directive in respect of all SIFs - Specialized Investment Funds - (Brown & Snyder, 2012, p. 277) brought the following regulations with it and applies for all special funds managers in accordance with the AIFM Directive (Loyens & Loeff, 2013, pp. 1-10):

1. The Commission (CSSF) may approve a SIF (cssf, 2015), whose central management is not located in Luxembourg, if it has appointed an AIFM with its administration who is in compliance with the requirements according (Majcen, 2007, p. 44) to the AIFM Act (Loyens & Loeff, 2013, p. 1-10; Majcen, 2007, p. 44),
2. the valuation principles of the AIFM Act apply together with the current valuation principles of the SIF Act (Loyens & Loeff, 2013, p. 5),
3. the contents of the annual report (Elvinger, Hoss, & Prussen, ehp.lu, 2007, p. 14) of a SIF must completely concur with the AIFM Act (Loyens & Loeff, 2013, p. 1-10),
4. the information to be conveyed to the SIF investors must concur with the exigencies of the AIFM Act (Loyens & Loeff, 2013, p. 5),

5. for the SIF, the swap rules contained in the AIFM Act are in force in addition to the regulation on delegation in Art. 42 SIF Act (fdc, 2015, pp. 1-27),
6. he benefits from the AIFM marketing pass (Marjcen, 2013), and
7. he has to adapt his custodian bank regime to the AIFM Act (Saluzzi, Weiland, Bock, & Schäfer, 2013, pp. 1-47).

The amendments to the SICAR Act go hand in hand with the creation of two types of SICARs (Loyens & Loeff, 2013, pp. 1-10):

a. A SICAR (Busack, 2006, p. 654) managed by a fund manager and
b. a SICAR not managed by a fund manager (Loyens & Loeff, 2013, pp. 4-8).

Otherwise, the amendments of the SICAR Act are substantially the same as for the SIF Act.

3.6.3 **Fund Structures in Luxembourg**

3.6.3.1 Preliminary Remarks

The Grand Duchy of Luxembourg is the leading fund center in Europe, thus naturally in the European Union, and to United States the second largest in the world (Muggli, 2014, pp. 79-80; Kinsch, Nell-Breuning, & Lakebrink, 2014, p. B5). UCITS, which are marketed to approximately 75% world-wide out of Luxembourg, are established globally as a regulated fund vehicle for decades (Kinsch, Nell-Breuning, & Lakebrink, 2014, B5; Kaiser, 2004, p. 41; Port & Steinlein, 2011, p. 83; Rehkugler, 2009, p. 572; Götzenberger, 2008, p. 147). For the investment type Private Equity and Venture Capital, Luxembourg is positioned in a leading role in the area of regulated fund vehicles since the Act of June 2004 on Venture Capital companies – the SICAR Act – February 2007 on Specialized Investment Funds – the SIF Act (Kinsch, Nell-Breuning, & Lakebrink, 2014, B5; Kaiser, 2004, p. 41; Port & Steinlein, 2011, p. 83; Rehkugler, 2009, p. 572; Götzenberger, 2008, p. 147). In the field of unregulated Private Equity structures, Private Equity firms from around the world have been utilizing financing and investment companies from Luxembourg for decades (Kinsch, Nell-Breuning, & Lakebrink, 2014, B5; Kaiser, 2004, p. 41; Port & Steinlein, 2011, p. 83; Rehkugler, 2009, p. 572; Götzenberger, 2008, p. 147).

With the provision of regulated investment companies – FCP, SICAV, SICAR – and unregulated holding companies – SOPARFI – for alternative asset classes, Luxembourg has designed lucrative structures (Kinsch, Nell-Breuning, & Lakebrink, 2014, B5; Kaiser, 2004, p. 41; Port & Steinlein, 2011, p. 83; Rehkugler, 2009, p. 572; Götzenberger, 2008, p. 147).

- FCP – the Fonds Commun de Placement (Kaiser D. G., 2004, p. 41; München, 2016, p. 511) is an investment fund founded under French or Luxembourg law (EVCA, 2013, pp. 124-132; Kaiser, 2004, p. 41),
- SICAV – the Société d'Investissement à Capital Variable (Port & Steinlein, 2011, p. 83) is an investment company with mutable capital founded under French, Belgian, Luxembourg, Swiss, Maltese or Italian law (EVCA, 2013, pp. 124-132; Port & Steinlein, 2011, p. 83),
- SICAR – the Société d'Investissement en Capital à risqué (Rehkugler, 2009, p. 572) is an investment company for engagement in Venture Capital (EVCA, 2013, pp. 124-132; Rehkugler, 2009, p. 572),
- SOPARFI – the Société de Participations Financieres is not a new form of corporation. It is applied on corporations with financial participations (Götzenberger, 2008, p. 147; EVCA, 2013, pp. 124-132).

Under the Act on Alternative Investment, fund managers of July 12, 2013, the Limited Partnership, anchored in the Luxembourg Trade Act for nearly 100 years was-significantly reformed and the so-called SCSp (société en commandite spéciale (Special Limited Partnership)) was created as a specialized partnership (Kinsch, Nell-Breuning, & Lakebrink, 2014, B5; Kaiser, 2004, p. 41; Port & Steinlein, 2011, p. 83; Rehkugler, 2009, p. 572; Götzenberger, 2008, p. 147). The SCSp is based on the Anglo-Saxon model of a Limited Partnership and offers its flexibility now to Private Equity companies in Luxembourg as well (Kinsch, Nell-Breuning, & Lakebrink, 2014, B5; Kaiser, 2004, p. 41; Port & Steinlein, 2011, p. 83; Rehkugler, 2009, p. 572; Götzenberger, 2008, p. 147). In the unregulated form, the specialized partnership may optionally be set up with or without legal personality (Kinsch, Nell-Breuning, & Lakebrink, 2014, B5; Kaiser, 2004, p. 41; Port & Steinlein, 2011, p. 83; Rehkugler, 2009, p. 572; Götzenberger, 2008, p. 147). In the regulated form, the SCSp may be equally used in the form of a SICAR or a specialized fund – SIF (Coekelbergs & Lakebrink, 2014).

3.6.3.2 SIF – Specialized Investment Funds

Preliminary Remarks

The Specialized Investment Funds – SIF – were first introduced with a law of February 13, 2007 regarding Specialized Investment Funds – the SIF Act (Elvinger, Reuter, Juncker, & Burgener, 2012, p. 4). Since then, this instrument (Elvinger, Reuter, Juncker, & Burgener, p. 4; Majcen, 2007, p. 42 et seqq.; Schirmacher, 2008, p. 47) is extremely favorable, because of its flexibility in conditions of structuring and opportunity set and it profits from economical tax regulations and an ordinary supervision (Schirmacher, 2008, p. 47). The group of suitable investors does not include intuitional financer, but any other categories of investors – which however must demonstrate competence – and private investors, which preferably are also required to bring forth expertise, respectively experience with such instruments (Elvinger, Reuter, Juncker, & Burgener, p. 4; Majcen, 2007, p. 42 et seqq.; Schirmacher, 2008, p. 47). These SIF regulations have been changed by a law of March 26, 2012, which got legal validity on 1 April 2012 (Elvinger, Reuter, Juncker, & Burgener, p. 4; Majcen, 2007, p. 42 et seqq.; Schirmacher, 2008, p. 47). It brought forth some changes offering even more flexibility in terms of structuring and operation of SIFs (Elvinger, Reuter, Juncker, & Burgener, p. 4; Majcen, 2007, p. 42 et seqq.; Schirmacher, 2008, p. 47). Other changes, however, extend the regulatory powers of the aforementioned commission – the CSSF (Elvinger, Reuter, Juncker, & Burgener, p. 4; Majcen, 2007, p. 42 et seqq.; Schirmacher, 2008, p. 47). New duties of the SIFs according to the Directive on Alternative Investment Fund Managers – the AIFM Directive – were already inwrought in this (Elvinger, Reuter, Juncker, & Burgener, p. 4; Majcen, 2007, p. 42 et seqq.; Schirmacher, 2008, p. 47).

Scope of Application

The SIF regime finds application to Undertakings for Collective Investment – UCI – whose shares are only for one or more qualified investors and whose constitutional documents are subjected to the SIF regime (Elvinger, Reuter, Juncker, & Burgener, p. 4 et seqq.; Majcen, 2007, p. 42 et seqq.; Schirmacher, 2008, p. 47; Dietrich M., 2016, p. 12 et seqq.; Kleine, Schulz, & Krautbauer, 2015, p. 140 et seqq., Götzenberger, 2008, p. 119 et seqq.).

- Undertakings for Collective Investment (Dietrich M. , 2016, p. 12 et seqq.)

SIFs are a particular class of UCI, underlying to the convention of balancing of portfolio. This status may be relevant, in particular in view of the non-application of various European Directives – such as the Prospectus Directive 2003/71/EC (Elvinger, Reuter, Juncker, & Burgener, p. 4 et seqq.; Majcen, 2007, p. 42 et seqq.; Schirmacher, 2008, p. 47).

- Qualified Investor (Majcen, 2007, p. 42, et seqq.; Kleine, Schulz, & Krautbauer, 2015, p. 140 et seqq.; Götzenberger, 2008, p. 119 et seqq.)

SIFs are only for qualified, competent investors, which are capable of adequately assessing risks in connection with investments in such an investment vehicle (Elvinger, Reuter, Juncker, & Burgener, p. 4 et seqq.; Majcen, 2007, p. 42 et seqq.; Schirmacher, 2008, p. 47; Dietrich M., 2016, p. 12 et seqq.; Kleine, Schulz, & Krautbauer, 2015, p. 140 et seqq., Götzenberger, 2008, p. 119 et seqq.).

- Optional Regime (Elvinger, Hoss & Prussen, 2012, p. 4 et seqq).

The submission to the SIF regime is optional (Elvinger, Reuter, Juncker, & Burgener, p. 4 et seqq.; Majcen, 2007, p. 42 et seqq.; Schirmacher, 2008, p. 47; Dietrich M., 2016, p. 12 et seqq.; Kleine, Schulz, & Krautbauer, 2015, p. 140 et seqq., Götzenberger, 2008, p. 119 et seqq.). If this option is taken, it must be noted in the constitutional documents, thus at least in the statutes and in the sales documents (LCG, 2013, pp. 1-6) for this investment (Elvinger, Reuter, Juncker, & Burgener, p. 4 et seqq.; Majcen, 2007, p. 42 et seqq.; Schirmacher, 2008, p. 47; Dietrich M., 2016, p. 12

et seqq.; Kleine, Schulz, & Krautbauer, 2015, p. 140 et seqq., Götzenberger, 2008, p. 119 et seqq.).

Investment Rules

The SIF Act allows for UCI to pursue the traditional investment as well as alternative investment strategies (Elvinger, Reuter, Juncker, & Burgener, p. 4 et seqq.; Majcen, 2007, p. 42 et seqq.; Schirmacher, 2008, p. 47; Dietrich M., 2016, p. 12 et seqq.; Kleine, Schulz, & Krautbauer, 2015, p. 140 et seqq., Götzenberger, 2008, p. 119 et seqq.). With the SIF regime – not exhaustively – real estate funds, hedge funds, microfinance funds, environmental funds and, indeed, Private Equity fund can be designed and it therefore offers great variability in matters of investments, in which a SIF may invest (Elvinger, Reuter, Juncker, & Burgener, p. 4 et seqq.; Majcen, 2007, p. 42 et seqq.; Schirmacher, 2008, p. 47; Dietrich M., 2016, p. 12 et seqq.; Kleine, Schulz, & Krautbauer, 2015, p. 140 et seqq., Götzenberger, 2008, p. 119 et seqq.).

A SIF must correlate with the convention of balancing of portfolio. The CSSF (Muller & Ruttiens, 2013, p. 35) has issued regulatory guidelines in this respect (Elvinger, Reuter, Juncker, & Burgener, p. 4 et seqq.; Majcen, 2007, p. 42 et seqq.; Schirmacher, 2008, p. 47; Muller & Ruttiens, 2013, p. 35)

A. The fund is limited in its investment. The fund cannot invest more than 30% (CSSF, 2007, pp. 1-2) of its assets in securities of the same type. However, this does not apply to securities issued by a Member State of the OECD – Organization for Economic Co-operation and Development – or the EU. Moreover, this does not apply to investments, which are similar to the SIF (Elvinger, Reuter, Juncker, & Burgener, p. 4 et seqq.; CSSF, 2007, pp. 1-2).
B. Bear sales may never implicate in the SIF keeping an open post in commercial papers of the equal kind and by the same emitter, which constitute more than 30% of its assets (Elvinger, Reuter, Juncker, & Burgener, p. 4 et seqq.; CSSF, 2007, pp. 1-2).

C. If derivative financial instruments – see derivates – are to be used as SIF, a comparable risk diversification must be ensured by an adequate distribution of underlying assets (Elvinger, Reuter, Juncker, & Burgener, p. 4 et seqq.; CSSF, 2007, pp. 1-2).

Available Legal Structures

The SIF Act expressly mentions investment funds – FCP – and investment companies with changeable capital – SICAV – but therewith does not construct the types of legal frameworks a SIF may have (Elvinger, Reuter, Juncker, & Burgener, 2012, p. 6). It is therefore conceivable and possible to use other legal forms (Elvinger, Reuter, Juncker, & Burgener, p. 4 et seqq.; CSSF, 2007, pp. 1-2; Majcen, 2007, p. 42 et seqq.; Rehkugler, 2009, p. 574; Müller N., 2016, p. 125 et seqq.).

A FCP (Müller N. , 2016, p. 125 et seqq.) is not an incorporated enterprise, but consists of special assets, which is held and managed for commitment of its joint-owners by a corporation of administration (Elvinger, Reuter, Juncker, & Burgener, p. 4 et seqq.; CSSF, 2007, pp. 1-2; Majcen, 2007, p. 42 et seqq.; Rehkugler, 2009, p. 574; Müller N., 2016, p. 125 et seqq.). This is either a corporation of administration whose corporate purpose includes not only the management of the SIF, but also the administration of at least one UCITS – Undertakings for Collective Investment in Transferable Securities – or a corporation of administration, which exclusively manages SIFs (Elvinger, Reuter, Juncker, & Burgener, p. 4 et seqq.; CSSF, 2007, pp. 1-2; Majcen, 2007, p. 42 et seqq.; Rehkugler, 2009, p. 574; Müller N., 2016, p. 125 et seqq.). On the other hand, a SIF can either be founded as a mutual fund with its own legal personality, ergo a legal person (Elvinger, Reuter, Juncker, & Burgener, p. 4 et seqq.; CSSF, 2007, pp. 1-2; Majcen, 2007, p. 42 et seqq.; Rehkugler, 2009, p. 574; Müller N., 2016, p. 125 et seqq.). A mutual fund which is succumbed to the SIF regulations, may be equipped with either changeable capital – SICAV – or with constant capital – SICAF (Elvinger, Reuter, Juncker, & Burgener, p. 4 et seqq.; CSSF, 2007, pp. 1-2; Majcen, 2007, p. 42 et seqq.; Rehkugler, 2009, p. 574; Müller N., 2016, p. 125 et seqq.). Basically, mutual funds are succumbed to the regulations of the Luxembourg Corporate Law, unless the SIF Act provides otherwise (Elvinger, Reuter, Juncker, & Burgener, p. 4 et seqq.; CSSF, 2007, pp. 1-2; Majcen, 2007, p. 42 et seqq.; Rehkugler, 2009, p. 574; Müller N., 2016, p. 125 et seqq.). The SIF Act provides other provisions, if for no other reason than to preserve flexibility of the corporate law framework (Elvinger, Reuter, Juncker, & Burgener, p. 4 et seqq.; CSSF, 2007, pp. 1-2; Majcen, 2007, p. 42 et seqq.; Rehkugler, 2009, p. 574; Müller N., 2016, p. 125 et seqq.). Incidentally, the SIF Act expressly provides the possibility to build a SIF with multiple sub-funds (gruenderportal-luxemburg.com, 2015).

Regulatory Characteristics

As a regulated investment vehicle, SIFs are succumbed to the control of the CSSF (Müller N., 2016, p. 196 et seqq.; Majcen, 2007, p. 43; Elvinger, Reuter, Juncker, & Burgener, p. 4 et seqq.) which however, is not constructed as restrictively as other UCI, because qualified and competent investors do not need such protection as retail investors (Elvinger, Reuter, Juncker, & Burgener, 2012, p. 9). Since April 1, 2012, a SIF must obtain the approval of the CSSF prior to beginning its placement and investment activities (Müller N., 2016, p. 196 et seqq.; Majcen, 2007, p. 43; Elvinger, Reuter, Juncker, & Burgener, p. 4 et seqq.). The CSSF has to approve the constitutional documents, the election of managing directors and executive directors, the responsible persons for the portfolio management, the Central Administration Agent, the depositary and the auditor of the SIF (Müller N., 2016, p. 196 et seqq.; Majcen, 2007, p. 43; Elvinger, Reuter, Juncker, & Burgener, p. 4 et seqq.). If changes need to be made, these must also be approved (Müller N., 2016, p. 196 et seqq.; Majcen, 2007, p. 43; Elvinger, Reuter, Juncker, & Burgener, p. 4 et seqq.). In order to concur with the AIFM Directive, newly established SIFs are succumbed to particular instructions concerning the assignment of functions since April 1, 2012 (Müller N., 2016, p. 196 et seqq.; Majcen, 2007, p. 43; Elvinger, Reuter, Juncker, & Burgener, p. 4 et seqq.). Most notably, a new SIF may delegate its administrative task only to asset managers, which are accredited for portfolio management and are succumbed to control by a regulatory agency (Fischer & Friedrich, 2012, pp. 386-393), which cooperates with the CSSF (Fischer & Friedrich, 2012, pp. 386-393; EVCA, 2013, pp. 124-132).

3.6.3.3 SICAR

The Société d´Investissement en Capital à Risqué – SICAR (Dietrich M. , 2016, p. 211 et seqq.) – is a Luxembourg investment company (Busack & Kaiser, 2006, pp. 653-654; Dietrich, 2016, p. 2011 et seqq.; Höring, 2013, p. 128 et seqq.; LCG, 2013, p. 43 et seqq.; EVCA, 2013, pp. 124-132). However, it does not illustrate a recent kind of corporation. Rather, it is a tool for investing exclusively in Venture Capital (Busack & Kaiser, 2006, pp. 653-654; Dietrich, 2016, p. 2011 et seqq.; Höring, 2013, p. 128 et seqq.; LCG, 2013, p. 43 et seqq.). This investment company is regulated by the SICAR Act with its own legal personality separated from its investors, which purpose is to invest its funds in risk assets aimed at distributing the earnings generated among qualified investors in compensation for the risk it bears (LCG, 2013, p. 3). The SICAR is only permitted in Venture Capital investments (Busack & Kaiser, 2006, pp. 653-654; Dietrich, 2016, p. 2011 et seqq.; Höring, 2013, p. 128 et seqq.; LCG, 2013, p. 43 et seqq.). Whereas in this context, risk capital describes that contribution which directly or indirectly benefits a company – Private Equity. If property or real estate is to be permitted as an investment, certain conditions need to be fulfilled (Busack & Kaiser, 2006, pp. 653-654; Dietrich, 2016, p. 2011 et seqq.; Höring, 2013, p. 128 et seqq.; LCG, 2013, p. 43 et seqq.). Thus investments are possible only as indirect investments through companies which invest in or hold venture capital in real estate assets as well as capital investment in real estate companies (Busack & Kaiser, 2006, pp. 653-654; Dietrich, 2016, p. 2011 et seqq.; Höring, 2013, p. 128 et seqq.; LCG, 2013, p. 43 et seqq.). Completely ruled out, however, is the direct holding of property (Busack & Kaiser, 2006, pp. 653-654; Dietrich, 2016, p. 2011 et seqq.; Höring, 2013, p. 128 et seqq.; LCG, 2013, p. 43 et seqq.). Unlike other corporate or fund forms, the SICAR in Luxembourg is under no obligation to observe the principle of diversification in their choice of investment and may invest in one or more undertakings (Busack & Kaiser, 2006, pp. 653-654; Dietrich, 2016, p. 2011 et seqq.; Höring, 2013, p. 128 et seqq.; LCG, 2013, p. 43 et seqq.). If the financing constitutes a Venture Capital investment, any type of financing like (LCG, 2013, p. 3)

- Bonds,
- Bridging loans,

- Capital contributions,
- Mezzanine capital, etc.

are permissible (Busack & Kaiser, 2006, pp. 653-654; Dietrich, 2016, p. 2011 et seqq.; Höring, 2013, p. 128 et seqq.; LCG, 2013, p. 43 et seqq.).

The Luxembourg investment vehicle SICAR is reserved for qualified and competent investors in the sense of professional investors as well as institutional investors such as banks and insurance companies (Busack & Kaiser, 2006, pp. 653-654; Dietrich, 2016, p. 2011 et seqq.; Höring, 2013, p. 128 et seqq.; LCG, 2013, p. 43 et seqq.). However, it is possible for natural persons with a certificate of competence, investing a minimum of 125.000 Euro, to obtain access (Eicke, 2009, p. 154).

Available Legal Structures

A Luxembourg SICAR is established as a corporation or partnership (Busack & Kaiser, 2006, pp. 653-654; Dietrich, 2016, p. 2011 et seqq.; Höring, 2013, p. 128 et seqq.; LCG, 2013, p. 43 et seqq.). It may not be organized in contractual form, i.e. as a mutual fund managed by a corporation of administration – the FCP. Accordingly, the following legal forms can be considered for the SICAR (LCG, 2013, p. 4):

- Stock Corporation (société Anonyme (SA)),
- Limited Liability Company (société à responsabilité limitée (SARL)),
- Partnership Limited by shares (société en commandite par actions (SCA)),
- Cooperative in the organization form of a stock corporation (société coopérative d`actions (SCOSA)) and the
- Limited Partnership (société en commandite simple (SECS)) – (EVCA, 2013, pp. 124-132).

In addition, it is possible to structure a Luxembourg SICAR as a fund of funds with several sub-funds, each with its own specific investment strategy and investment manager, independent from each other (Busack & Kaiser, 2006, pp. 653-654; Dietrich, 2016, p. 2011 et seqq.; Höring, 2013, p. 128 et seqq.; LCG, 2013, p. 43 et seqq.). There is so far a similarity to the structuring possibilities of the Luxembourg special fund SIF (Busack & Kaiser, 2006, pp. 653-654; Dietrich, 2016, p. 2011 et seqq.;

Höring, 2013, p. 128 et seqq.; LCG, 2013, p. 43 et seqq.). Home and head office of the SICAR must be located in Luxembourg (Busack & Kaiser, 2006, pp. 653-654; Dietrich, 2016, p. 2011 et seqq.; Höring, 2013, p. 128 et seqq.; LCG, 2013, p. 43 et seqq.). This includes the preparation and safekeeping of all documents intended for the investors and the execution of the issuance and redemption of shares, respectively participations (Busack & Kaiser, 2006, pp. 653-654; Dietrich, 2016, p. 2011 et seqq.; Höring, 2013, p. 128 et seqq.; LCG, 2013, p. 43 et seqq.). The SICAR company has to carry the abbreviation SICAR in its name (Trübestein, 2012, p. 326).

Regulatory Characteristics

It can well be considered as an advantage that the SICAR, unlike other regulated investment vehicles in Luxembourg, are subject to much less stringent (LCG, 2013, p. 5) supervisory rules (Höhn & Höring, 2010, p. 196; Bernhardt, 2010, p. 216; Zetsche, 2015, p. 373 et seqq.; LCG, 2013, p. 43 et seqq.). The SICAR is under the constant supervision of the Financial Market Authority – the CSSF – and requires their prior approval (Höhn & Höring, 2010, p. 196; Bernhardt, 2010, p. 216; Zetsche, 2015, p. 373 et seqq.; LCG, 2013, p. 43 et seqq.). Following the admission by the CSSF, the SICAR may be quoted on the Luxembourg Stock Exchange – as long as they will operate as SA (Höhn & Höring, 2010, p. 196; Bernhardt, 2010, p. 216; Zetsche, 2015, p. 373 et seqq.; LCG, 2013, p. 43 et seqq.). The year-end accounts of a Luxembourg SICAR must be audited by an independent auditor and published within the next half year in the new fiscal year (Höhn & Höring, 2010, p. 196; Bernhardt, 2010, p. 216; Zetsche, 2015, p. 373 et seqq.; LCG, 2013, p. 43 et seqq.). Furthermore, the Luxembourg SICAR must prepare a prospectus with all essential data – which incidentally must contain the constitutional documents – so that it is feasible for investors to be able to carry out an informed assessment of the capital asset and the risks (Höhn & Höring, 2010, p. 196; Bernhardt, 2010, p. 216; Zetsche, 2015, p. 373 et seqq.; LCG, 2013, p. 43 et seqq.).

3.6.3.4 Income Tax Treatment of Private Equity Funds

The Luxembourg special fund – SIF – is exempt from Luxembourg income tax. There will be no tax imposed on income and capital gains (Dietrich & Müller, 2016, p. 220 et seqq.; LCG, 2013, p. 43 et seqq.). The SIFs are succumbed to yearly standing order duty – the so-called taxe d'abonnement – of 0.01%, which is charged adapted from the net assets each calendar quarter (Elvinger & Prussen, 2015, p. 16; Dietrich & Müller, 2016, p. 220 et seqq.; EVCA, 2013, pp. 124-132). In this point as well, the SIF clearly differs from other UCI, which is typically subject to a tax of 0.05% (Elvinger, Reuter, Juncker, & Burgener, 2012, p. 10). The part of the assets, which are investing in other Luxembourg UCI which are already subject to this tax as well as certain institutional money market funds, microfinance funds and pension funds, are exempted from the subscription tax under the SIF Act (Dietrich & Müller, 2016, p. 220 et seqq.; LCG, 2013, p. 43 et seqq.). Furthermore, individual sub-funds or classes, serving as retirement provisions, can be tax-exempt (Dietrich & Müller, 2016, p. 220 et seqq.; LCG, 2013, p. 43 et seqq.).

Concerning the withholding tax, it is to be emphasised that the Luxembourg SIF does not plan deduction at source for the distributions of a SIF to investors and the disbursements of the earnings on redemption shares, respectively participations (Dietrich & Müller, 2016, p. 220 et seqq.; LCG, 2013, p. 43 et seqq.).

Special funds – SIF – which have been founded in the legal status of an investment corporation – SICAF or SICAV – do fall within the area of the so-called Savings Directive – Directive 2003/48/EC, whereas SIFs in form of a FCP are well succumbed to the same (Dietrich & Müller, 2016, p. 220 et seqq.; LCG, 2013, p. 43 et seqq.). With regard to the Luxembourg SICAR corporation, it is in principle subject to an income tax of 29.22%, composed of the corporate tax – 21% for income over 15.000 euros, respectively 20% for income up to 15.000 euro – and is increased by 7% unemployment fund and trade tax of 6.75% (Dietrich & Müller, 2016, p. 220 et seqq.; LCG, 2013, p. 43 et seqq.). Income from securities of a Luxembourg SICAR as well as income resulting from the sale, transfer or liquidation of its securities do not substantiate taxable income (LCG, 2013, p. 4). If the creation of a Luxembourg SICAR is established in the form of a limited partnership, it will be treated fiscally transparent and is not subject to corporation and trade tax, whereas the tax transparency – as above – implies that the limited partnership itself is not a taxable entity subject to income tax and the investors are being taxed in the country of their residence (Dietrich & Müller, 2016, p. 220 et seqq.; LCG, 2013, p. 43 et seqq.).

Analyzing all individual considerations, it can be quickly realized that the Luxembourg model appears to offer the best opportunities for Private Equity transactions (Dietrich & Müller, 2016, p. 220 et seqq.; LCG, 2013, p. 43 et seqq.). The figures regarding the per capita gross domestic product in relation to the Private Equity involvement alone clearly shows that the two other countries examined – Germany and Austria – are clearly lagging behind with their regulations, especially fiscal regulations (Dietrich & Müller, 2016, p. 220 et seqq.; LCG, 2013, p. 43 et seqq.). The opacity of regulations appears to be a reliable indicator of an ailing Private Equity market in the European Union – not only in Germany and Austria, by the way (Dietrich & Müller, 2016, p. 220 et seqq.; LCG, 2013, p. 43 et seqq.). If there is an agreement – and there will be little doubt on that – that growth can be achieved especially through entrepreneurs, because they create jobs and promote synergy in terms of suppliers, consultants, banks and state; the financing of entrepreneurs should be ensured by the appropriate instruments (Dietrich & Müller, 2016, p. 220 et seqq.; LCG, 2013, p. 43 et seqq.).

3.6.4 Fiscal Regulation Parameters of Private Equity Funds in Luxembourg

Table 7: Taxation at a Fund Level

TAXATION AT A PRIVATE EQUITY FUND LEVEL		
VAT ON MANAGEMT FEES	NO	
CAPITAL GAINS TAX	MIN 0%	MAX 29.22%
WITHHOLDING TAX	MIN 0%	MAX 35%
VALUE ADDED TAX		17%
STAMP DUTIES OR TRANSACTION TAXES	STAMP YES – TRANSACTION NO	
ANTI-ABUSE RULES	YES	

Source: Own representation based on EVCA Tax Benchmark Study, 2013.

Such an instrument could be a fund which applies for the European Union and creates, above all, a uniform tax environment, so that the access for investors and thus for entrepreneurs could be facilitated (LCG, 2013, pp. 1-6).

Table 8: Taxation at a Company Level

TAXATION ON A COMANY LEVEL		
COMPANY TAX	MIN 28.15%	MAX 29.22%

Source: Own representation based on EVCA Tax Benchmark Study, 2013.

Table 9: Taxation of Employees

TAXATION OF EMPLOYEES		
INCOME TAX	MIN 0%	MAX 43.6%
CAPITAL GAINS TAX	MIN 0%	MAX 43.6%

Source: Own representation based on EVCA Tax Benchmark Study, 2013.

In order to capture the taxation of such a structure, one has to make a distinction between the taxation at company level (table 8) and the taxation at fund level (table 7). Herein, the value added tax – neither for SICAR nor for SIF management services are subject to VAT (LCG, 2013, p. 6; LCG, 2013, p. 5) – and the withholding tax need to be observed. In Luxembourg, there are two preferred fund structures with different fiscal observation periods (Richards D. , 2013, p. 1). The investment company SICAR is charged with income tax, mainly the capital gains tax, the corporation tax, amounting to 29.22% (Gruenderportal-Luxemburg, 2016, p. 1). The tax rate is calculated from the base rate of the corporation tax of 21% (LCG, 2013, p. 6) and the unemployment fund of 7% (yields 22.47%). Moreover, the business tax at rate of 6.75% (Dietrich, 2016, p. 221) is applied (22.47% + 6.75% = 29.22%). The SICAR is not subject to corporate tax and trade tax if established in the form of a limited partnership and therefore is tax transparent (EVCA, 2013, pp. 124-132). However, the SICAR is exempt from the withholding tax (Dietrich, 2016, p. 211 et seqq.). Unlike the mutual fund SICAR, the special fund SIF is free from income tax and withholding tax (LCG Luxembourg, 2016; EVCA, 2013, pp. 124-132). Basically, the exemption from withholding tax (which otherwise amounts to 15% and may increase to a 20% rate on Supervisory or Management Board Remunerations) on the distribution of dividends applies only for non-resident investors (EVCA, 2013, p. 124-132). However, it will be succumbed to the Tax d'Abonnement amounting to 0.01% of the net assets (Dietrich, 2016, p. 221), which is payable annually. The taxation at company level results from the calculation already made above – the combination of corporate tax plus unemployment fund and the business tax – and, consequently, amounts to 29.22% respectively 28.15% as long as the lower tax rate of 20% is used as a basis, which is the case if the taxable base falls short of 15.000 Euros (LCG, 2013, p. 6). The taxation of the employees is shown in table 9.

4 DEVELOPMENT OF THE "FUND EUROPAEA"

4.1 OBJECTIVES OF THE EMIPIRICAL STUDY

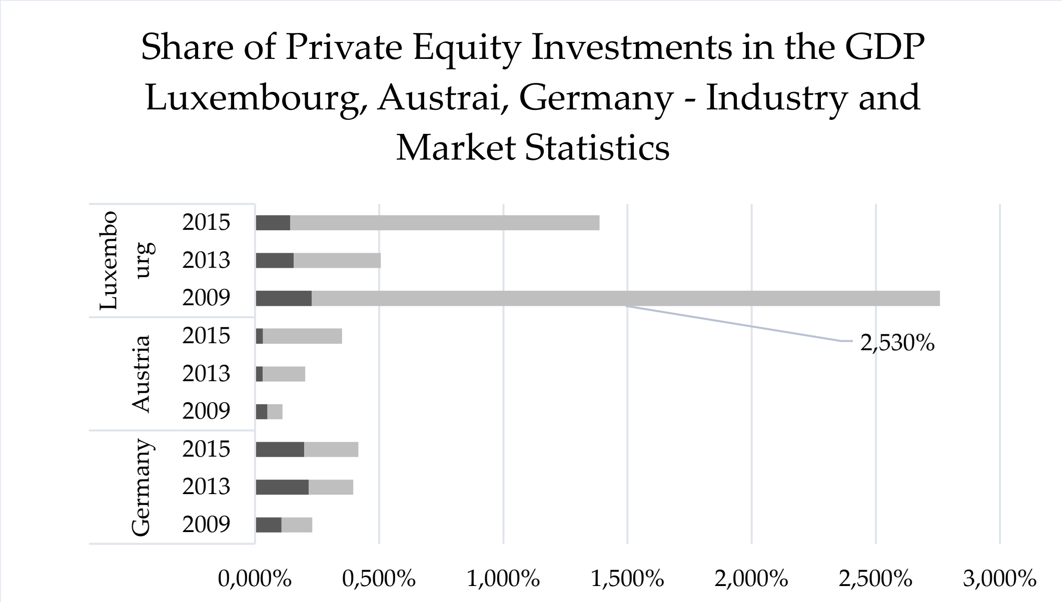
It shall be the objective of this study to empirically determine the impact and effect of different parameters on the investment behavior of those countries of the European region, respectively of the European Union, which currently hold a significant Private Equity market, and to develop a fund which will be a novelty in regards to fiscal regulations from these findings - see also "Private Equity in den USA" from Jesch (2004, p. 157)[14]. Taxes are an important criterion for the place of business of a company (Bungartz, 2012, p. 409 et seqq.; Dowling & Drumm, 2003, p. 59). The goal – a tax-optimized model – for Private Equity firms, their funds and therefore for the entrepreneurs, is achieved, when the fiscal regulations overcome the language barriers, personal interests, and national borders. The current formalities – as exemplary and in detail examined by the examples of Germany, Austria, and Luxembourg – are neither rudimentary uniform, even if the European Union (EU) strives for a tax harmonization, nor understandable. The very fact that there is no consensus among the Member States of the EU as to whether and in what form a tax transparency should be accepted, reduces the chances of success for Private Equity transactions. In some countries, the management fee is succumbed to sales tax, while in other countries this is not possible (Buge, 2016, p. 1). National occurrences prevent access to this growth potential (exemplary in Austria (Tojaner & Moser, 2013, p. 34)).

Constrictively, it has to be respected that the fiscal regulations are not solely responsible for the lack of commitment in Private Equity. It is rather the totality of regulations and the standing of the different countries of the European Union,

[14] Jesch stated that taxation in the United States is easier than it is in the European Union (EU). In the EU, the players have to deal with issues such as trade and asset management, tax harmonization, tax treaties and domestic taxes, althougt uniformity would represent a significant simplification in terms of Private Equity. Simple and above all uniform rules regarding Private Equity would mean more exposure to young innovative enterprises, which in turn would ensure growth in the right direction.

pushing that readiness or not (Hinrichs & Schatz, bvkap.de, 2015, pp. 1-20). Interrelations, as between the gross domestic products and the readiness to invest, could already be sufficiently substantiated in this research study. The performance of a country is not necessarily dependent only on the amount of the total domestic product, rather the per capita domestic product is crucial for the readiness to invest; this performance figure plays a prominent role.

Figure 99: Share of PE Investments in the GDP – Industry and Market Statistics



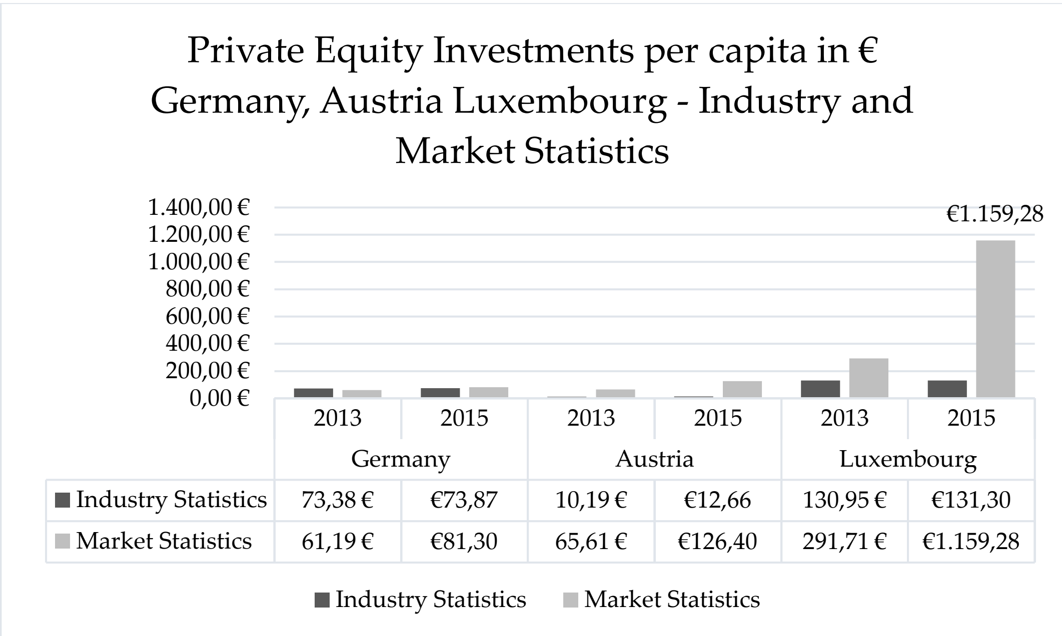
	Germany			Austria			Luxembourg		
	2009	2013	2015	2009	2013	2015	2009	2013	2015
Industry statistics	0,107%	0,216%	0,198%	0,050%	0,030%	0,032%	0,228%	0,156%	0,141%
Market statistics	0,123%	0,180%	0,218%	0,060%	0,172%	0,319%	2,530%	0,350%	1,246%

Source: Own representation based on Eurostat and Invest Europe.

If taking the gross domestic product as reference, the Big Five would protrude in terms of risk capital. How different the perception is with a per capita analysis (for example for the three countries mentioned above), is shown with figures 99 and

100, which feature Luxembourg in the far lead with its high gross domestic product per capita. The aim of this study is to extract optimized tax conditions. The corresponding hypothesis is if the gross domestic product per capita increases, the willingness to invest per capita is also higher.
One can see the data (Eurostat, 2016; Invest Europe, 2016) resulting from the arithmetic operation investments in total * 100 / GDP (gross domestic product), or from the operation investment / population.

Figure 100: PE Investments per capita – Industry and Market Statistics



Source: Own representation based on Eurostat and Invest Europe.

The analysis of the effect of the parameters investments, fundraising, taxes, gross domestic product, gross domestic product per capita on the propensity to invest in Venture Capital is differentiated and carried out according to the individual characteristics of these parameters. The research results shall allow the reader to identify potential influence and to anticipate the consequential prospective success.

The investment in venture capital (venture capital) per capita occupies a prominent position in this study. The per capita investment is € 13.51 per annum (taking into account all 22 countries surveyed) and € 8.79 for the Market Statistic. This makes a total investment in this sector of € 22.30. The initial value was 279.23 euros for the Industry Statistic and 193.42 euros for the Market Statistic total per year. The aim of this study is to extract optimized tax conditions for venture capital: the associated hypothes is that if there are tax-optimized conditions for venture capital, investment in this area would also be higher.

4.2 DESIGN OF THE EXAMINATION

The selection initially requires – as already described above in the chi-square analysis – a factual, spatial and temporal differentiation of the population. This refers to the amount of investigation units, about which the statements are to be made. An investigation unit is to be interpreted as an object on which measures are to be taken. In spatial terms, a limitation on the European Union – with a little excurse to the European neighborhood – is to be carried out, in order to reduce the data collection effort to a reasonable level on one hand and on the other to clarify, which market is being observed (Bourier, 2014, p. 5 et seqq.; Kuß, Wildner, & Kreis, 2014, p. 67 et seqq.). In terms of time, the population is set to the year 2015. Changes in population were not to be expected and therefore not taken in to consideration, which also applies to the data after December 31, 2015. In factual terms, the population principally encompasses all countries of the European Union and, beyond that, in Europe. Total registration, however, is fraught with considerable difficulties. Not all Member States have an adequate Private Equity market, so that in the presentation major outliers would occur. Thus, the Baltic States, as well as the former Yugoslavia and some others are underrepresented. The author therefore refers to those Member States that have a significant Private Equity market or, like Greece, seem to be important based on their particularly difficult situation, so that ultimately 22 countries have been selected for the study.

The collection of data is carried out via the relevant literature from the ranks of the European Union, the national Private Equity and Venture Capital Associations, the European Venture Capital Association (EVCA), currently Invest Europe, the national legislations and the accompanying literature. Accompanied and discussed was the provision of data from and with the heads of relevant organizations, in their own environment – crowdfunding, economic and tax advice.

The analysis of the data was performed within a descriptive analysis. The statistical analysis and presentation of the research results is carried out by means of Statistics R as part of a cluster analysis and Microsoft Power View / Pivot.

4.3 ANALYSIS INSTRUMENT: CLUSTER ANALYSIS

4.3.1 **Preliminary Remarks**

It is the objective of the cluster analysis to create clusters of observation units, in which clusters are groups of observation units, which are usually described by many variables. This grouping should of course happen in a way that (Hatzinger, Hornik, & Nagel, 2011, p. 416).

- The members of a group are similar to each other, thus displaying a homogeneity and
- the groups differ from each other as much as possible, therefore creating a heterogeneity between the groups.

A multitude of possibilities to measure similarities between clusters is given here as the possibility to allow for the most different interpretations within the clusters where necessary.

In essence, the accumulation of clusters, thus groups, can be formed by partitioning method or hierarchically. In hierarchical clustering, the clusters are composed of sub-clusters, so that a tree structure is created. In order to summarize the objects into clusters, they must be divided at an appropriate position, wherein the number of clusters is not set at this point.

In the partitioning method, the number of clusters is already defined at the beginning of the examination. In order to obtain adequate, intentional or different results, the objects are moved within the individual clusters (Bacher, Pöge, & Wenzig, 2010, pp. 15-32).

4.3.2 Hierarchical Clustering Methods

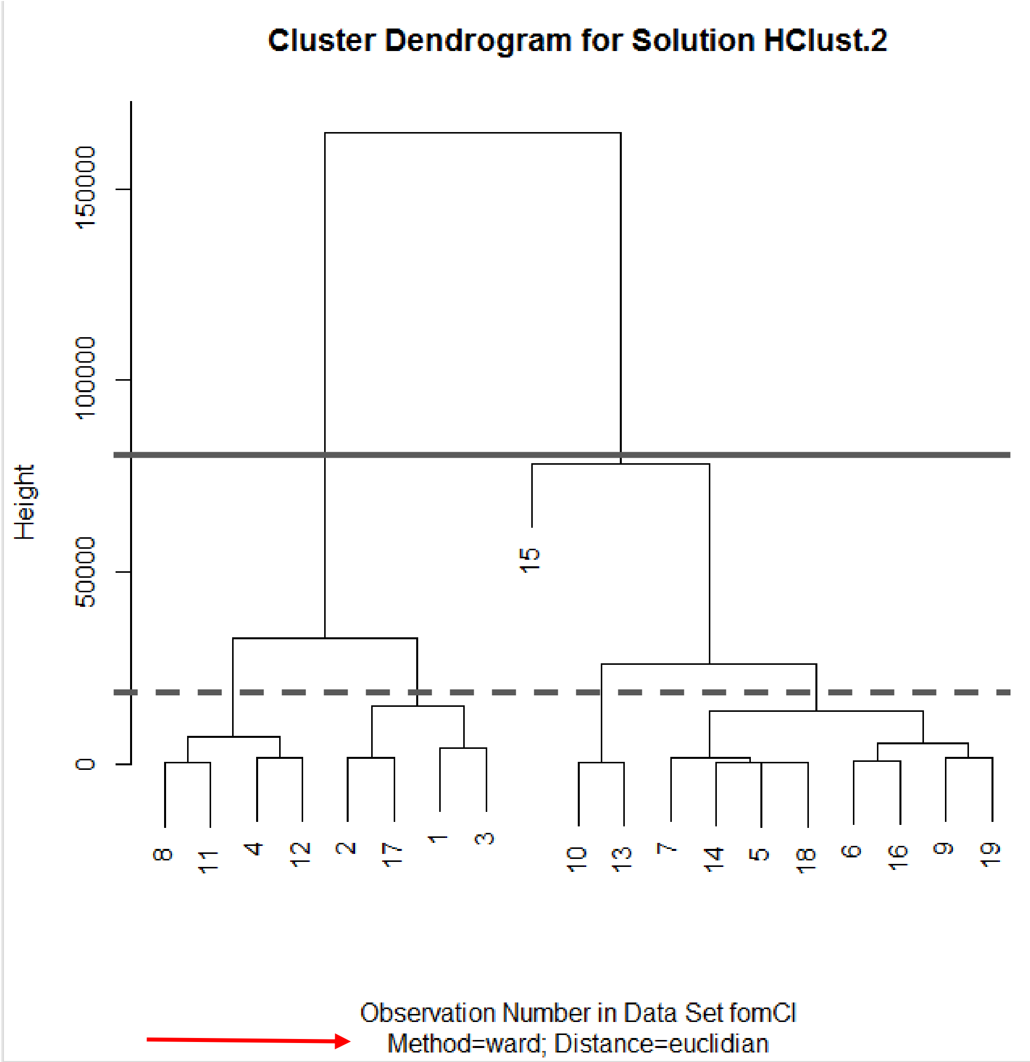
In the hierarchical method, a hierarchical structure is established, in which clusters are composed of sub-clusters (Bühl, 2008, p. 550 et seqq.). There are two kinds of methods (Bühl, 2008, p. 550 et seqq.; Behnisch, 2007, p. 49 et seqq.). On the one hand, there is the agglomerative method (bottom-up), in which each object constitutes an individual cluster at the beginning (Bühl, 2008, p. 550 et seqq.; Behnisch, 2007, p. 49 et seqq.). The most similar clusters are being iteratively – thus gradually converging – grouped into larger clusters remains (Behnisch, 2007, p. 49). At the end, only a single cluster remains (Bühl, 2008, p. 550 et seqq.; Behnisch, 2007, p. 49 et seqq.).

The second procedural tool are the divisive methods (top-down) starting with a single cluster which contains all objects (Bühl, 2008, p. 550 et seqq.; Behnisch, 2007, p. 49 et seqq.). Henceforth, these are then again (Behnisch, 2007, p. 49) split into sub-clusters.

In these processes, a tree structure is being obtained that must be split at an appropriate point in order to obtain an adequate clustering (Bühl, 2008, p. 550 et seqq.; Behnisch, 2007, p. 49 et seqq.). Depending on where this is done, various clustering are possible (Bühl, 2008, p. 550 et seqq.; Behnisch, 2007, p. 49 et seqq.). Usually, it is divided where two merged clusters are relatively dissimilar (Bühl, 2008, p. 550 et seqq.; Behnisch, 2007, p. 49 et seqq.). The dendrogram represents a tool for finding those positions. Figure 101 shows which clusters are being merged and where a division can take place if necessary. The length of the edges from a node to its branches provides information on how similar the clusters are that are merged into this one cluster. It concerns the analysis of investments by European Member States in Venture Capital per capita, considering the per capita gross domestic product in compliance with industry statistic. The dendrogram shows well, that an outlier slightly blocks the view. Under certain circumstances, these outliers are responsible for distortions and where appropriate, should be removed for the examination. Nevertheless, a classification into two clusters is necessary and appropriate for the present purpose. To make this clear, an auxiliary line, as can be seen in the figure, could create an even clearer demarcation. A division in five clusters, shown below beneath the dashed line, could be possible as well. For this purpose, however, number 15, the outlier, would have to be removed.

For the presentation of the dendrogram in the context of this process, the selection of an appropriate reference for the similarity of clusters is of paramount importance (Bühl, 2008, p. 550 et seqq.; Behnisch, 2007, p. 49 et seqq.).

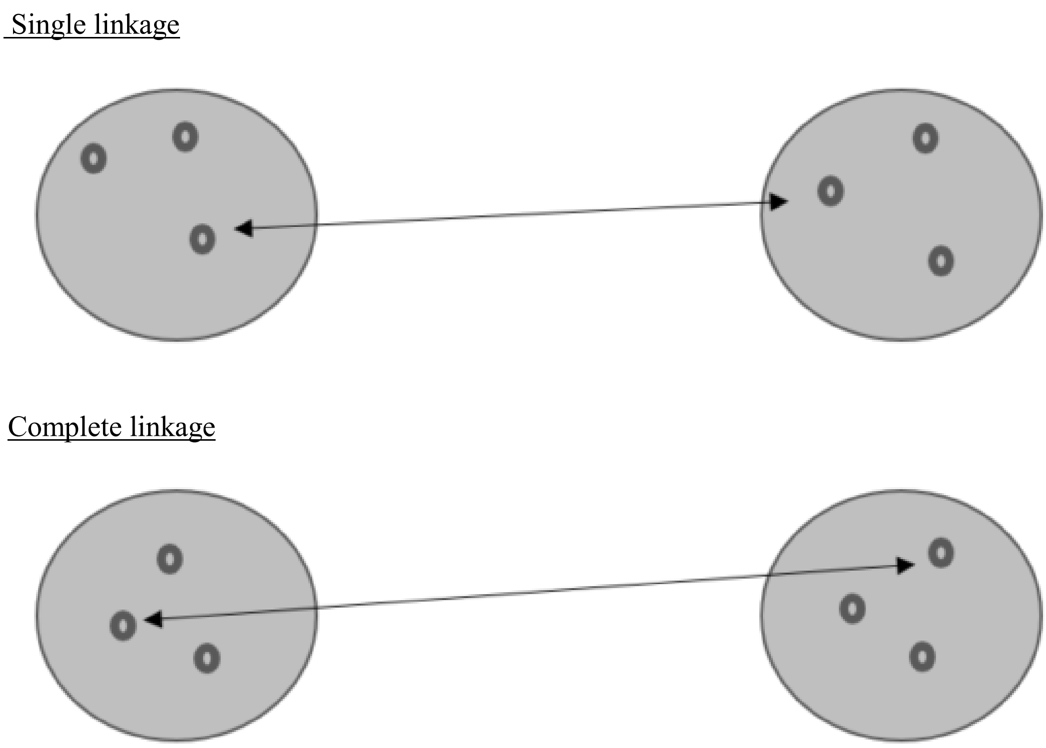
Figure 101: Exemplary Dendrogram



Source: Own representation created with Statistics R.

These reference methods differ in part considerably (Bühl, 2008, p. 550 et seqq.; Behnisch, 2007, p. 49 et seqq.; Schendera, 2010, p. 23 et seqq.; Bortz, 1985, p. 697 et seqq.). The common feature of these methods is the measurement of the distance (Schendera, 2010, pp. 23-33). One method (Götze, Deutschmann, & Link, 2002, p. 340; Püschel, 2011, pp. 58-59) measures the minimum distance (single linkage), the other the maximum distance (complete linkage) of the cluster or, as in figure 101 (arrow), the ward method (Bortz, 1985, p. 697), also called minimum-variance-method, calculates the quadratic Euclidean distance between all objects (Bühl, 2008, p. 550 et seqq.; Behnisch, 2007, p. 49 et seqq.; Schendera, 2010, p. 23 et seqq.; Bortz, 1985, p. 697 et seqq.).

Figure 102: Distance Measurements – Cluster Analysis



Source: Own representation based on Püschel, 2011, pp. 58-59.

There are other methods (Behnisch, 2007, p. 49), which are not considered at this point. As an example here, the single and complete linkage methods are pictorially shown (figure 102).

4.3.3 Partitioning Cluster Method

In the partitioning method, a number of start clusters are predefined, to which the objects to be grouped are being assigned according to the applied distance measure (Kudraß, 2007, p. 463). Subsequently, it is being interactively tried to improve the respective grouping by moving individual objects from one cluster to another (Behnisch, 2007, p. 49 et seqq.; Kudraß, 2007, p. 463 et seqq.; Fett, 2008, p. 26 et seqq.). The process ends when a group can no longer be improved by further repositioning of objects (Behnisch, 2007, p. 49 et seqq.; Kudraß, 2007, p. 463 et seqq.; Fett, 2008, p. 26 et seqq.). With this method, the assignment of an object to a cluster is not final, but may be changed as often as desired (Fett, 2008, pp. 26-27).

In order to be able to measure the quality of the computed cluster solutions, a number of criteria are available to select from (Behnisch, 2007, p. 49 et seqq.; Kudraß, 2007, p. 463 et seqq.; Fett, 2008, p. 26 et seqq.):

- The variance criterion or inverse square criterion calculates for each cluster the squared deviations of the objects of a cluster from the cluster centroid and adds these deviations on all clusters together, whereas that portioning is sought, for which the sum of squared deviations is minimal,
- the trace criterion, which aims to maximize inter-group heterogeneity, and
- the Wilks Lamda criterion or the determinant criterion, which achieves particularly good results with correlated characteristics (Fett, 2008, pp. 26-28).

4.4 INVESTIGATIVE RESULTS

4.4.1 Preliminary Remarks

In this paper, the hierarchical cluster analysis has been applied, in which in addition to the national data – such as population number, size of the country, population per square kilometer and Euro membership – of the selected Member States of the European Union, the following parameters as variables – 63 parameters in total were examined – have been investigated in terms of correlations:

In general

- Gross Domestic Product (GDP),
- Gross Domestic Product per capita,
- Unemployment rate,
- Purchasing power.

Specifically, Private Equity

- Fundraising,
- Fundraising, measured by GDP,
- Fundraising per capita,
- Investments industry statistics,
- Investments industry statistics per capita,
- Investments industry statistics venture capital,
- Investments industry statistics venture capital per capita,
- Investments industry statistics others (buy out, growth etc.),
- Investments industry statistics others per capita,
- Investments market statistics,
- Investments market statistics per capita,
- Investments market statistics venture capital,
- Investments market statistics venture capital per capita,
- Investments market statistics others (buy out, growth etc.),
- Investments market statistics others per capita.

Taxes

- Value Added Tax,
- Corporate Income Tax,
- Total Corporate Income Tax,
- Capital Gains Tax,
- Withholding Tax,
- Sales Tax on Management Fees, yes or no.

The countries examined were (these countries must have numbers to find it again in the dendrogram):

1. Spain,
2. Portugal,
3. Italy,
4. Bulgaria,
5. Ireland,
6. France,
7. Finland,
8. Poland,
9. Belgium,
10. Sweden,
11. Hungary,
12. Romania,
13. Denmark,
14. Netherlands,
15. Luxembourg,
16. United Kingdom,
17. Czech Republic,
18. Austria,
19. Germany,
20. Greece,
21. Norway, and
22. Switzerland.

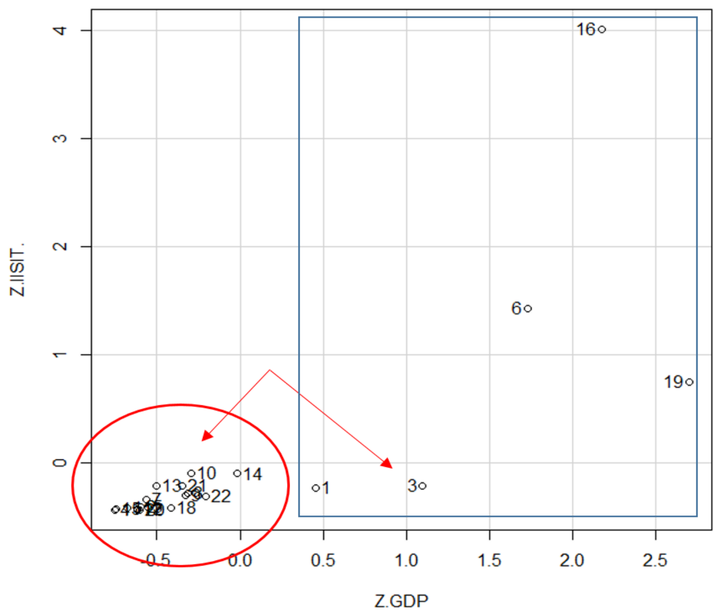
All data have been used for finding similarities among Member States of the European Union, in order to relate them in interpretations to the above, already as importantly recognized, gross domestic product and finally to taxes again. Since there is a multitude of different data, these were partially standardized. For the individual studies, fundraising remained unconsidered. In the following sections only the analyses which are important for this work are shown. These are above all the venture capital investments per capita, while taking into account GDP per capita as well as venture capital investments per capita, while also taking into account capital gains taxes and withholding taxes. Nevertheless, the total investment (also per capita) was analyzed at this point, while taking into account the GDP (also per capita). These analyzes serve, firstly, to recognize that the analyses with the total volume produce completely different results than the per capita view, and secondly to look at whether, according to the consideration of private equity (ie all investments) per capita countries which are not expected there. All of these analyses are carried out individually. Only in the final analysis are the venture capital investments per capita taking into account the relevant taxes (ie the above-mentioned capital gains taxes and withholding taxes still company taxes and the respective minimum and maximum values), the gross domestic product per capita and the purchasing power standard (PPS) considered as a whole. In the end, the venture capital investment is the main reason for the fact that venture capital is essential for the financing of target companies in the early stages. Since venture capital per definition is a part of private equity in this development, the results and statements are to be understood as analogous.

4.4.2 Investments under Consideration of the Gross Domestic Product (GDP)

4.4.2.1 Total Investments of Countries under Consideration of the Gross Domestic Product – Industry Statistics

The total investments of the holding companies of the countries under consideration of the GDP represent the investment behavior, thus whether the investments depend on the gross domestic product (figure 103).

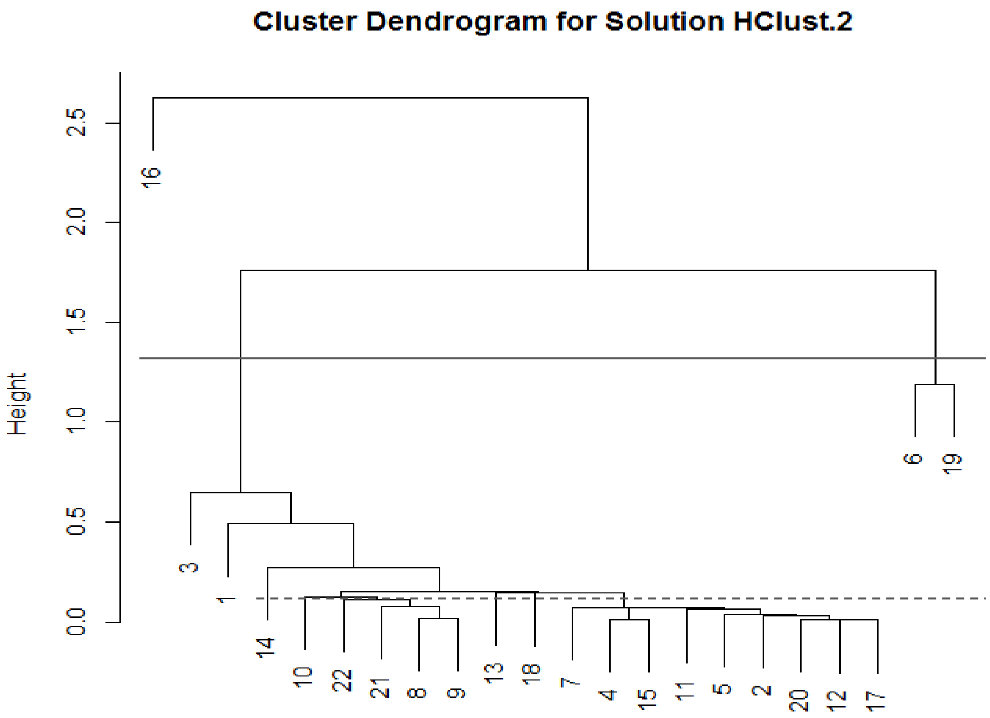
Figure 103: Scatter Diagram Total PE Investment – Gross Domestic Product



Source: Own representation created with Statistics *R*.

Due to the fact that British (16) holding companies invest significantly more compared to those of other European countries, there is indeed a slight distortion, but is also well recognized that most of the observed countries remain in a group, such as the position of the five largest economies of the EU – Spain (1), Italy (3), France (6), Germany (19) and the United Kingdom (16). However, it can already be noted that Sweden (10), Denmark (13), the Netherlands (14), Belgium (9) and – outside of the European Union – Switzerland (22) do play a role in part even ahead of Italy and Spain in regards to the investments of holding companies.

Figure 104: Total PE Investment – Gross Domestic Product / Industry Statistic



Source: Own representation created with Statistics *R*.

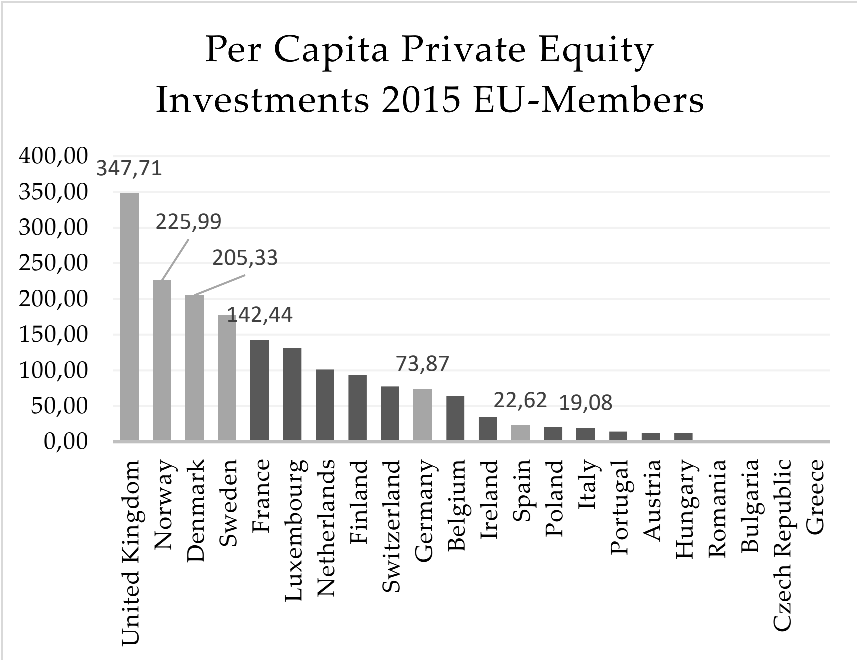
Method=single; Distance=euclidian

The clustering process in the single linkage method (figure 104) has clearly than e.g. the ward method of outliers. Refering to the distances, there are mainly similarities between Germany (19) and France (6). They form a cluster. Their willingness to invest is similar. This similarity can also be seen between Italy (3) and Spain (1).

4.4.2.2 *Per Capita Investments under Consideration of the Gross Domestic Product per Capita – Industry Statistics*

Preliminary studies have shown that examinations with aggregates such as the gross domestic product (GDP) do not make sense.

Figure 105: Per Capita Private Equity Investments – Industry Statistics 2015



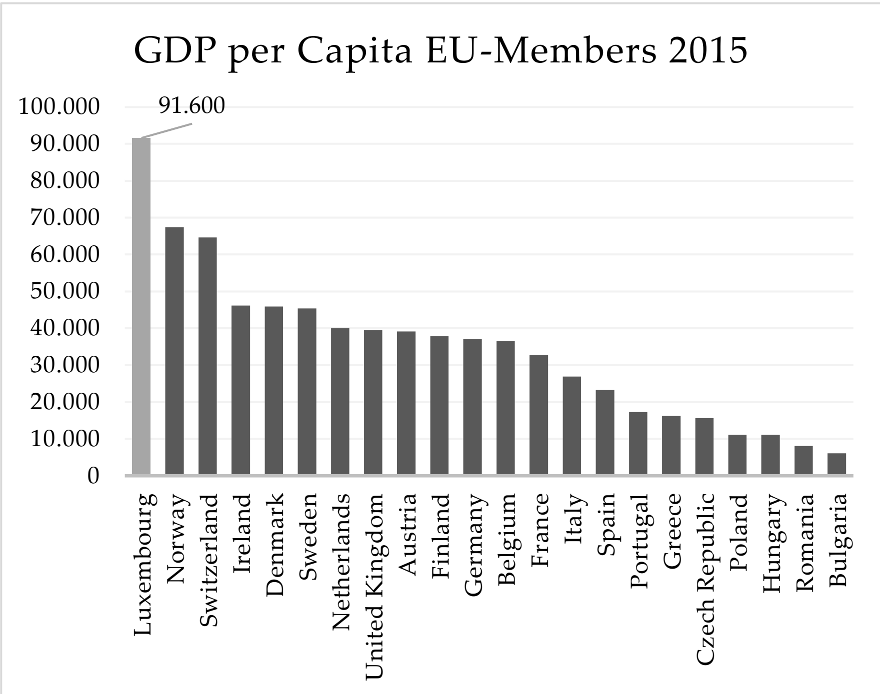
United Kingdom	347,71
Norway	225,99
Denmark	205,33
Sweden	176,57
France	142,44
Luxembourg	131,30
Netherlands	101,05
Finland	93,63
Switzerland	77,50
Germany	73,87
Belgium	64,10
Ireland	34,75
Spain	22,62
Poland	21,10
Italy	19,08
Portugal	14,31
Austria	12,66
Hungary	11,98
Romania	2,49
Bulgaria	2,22
Czech Republic	1,22
Greece	0,01

Source: Own representation based on Eurostat.

A high GDP does not demonstrate the actual performance of a country. Only the GDP per capita – thus the division of the gross domestic product by the number of inhabitants – or the purchasing power standard are showing how resilient the individual is within the Union. Therefore, the gross domestic product per capita of a country is applied for further examinations from now on. In addition, the purchasing power standard is sided with the Gross Domestic Product. Chapter 4.4.2.1 only served for the classification of the major economies of the European Union and already permitted to draw conclusions that a high GDP in relation does not yet result in a readiness to invest by itself.

The indicators per-capita-investments under consideration of the per capita gross domestic product and the purchasing power (see later) standard are therefore significant. Figures 105 and 106 show the corresponding data graphically resolved.

Figure 106: GDP per Capita EU-Members – Industry Statistics 2015

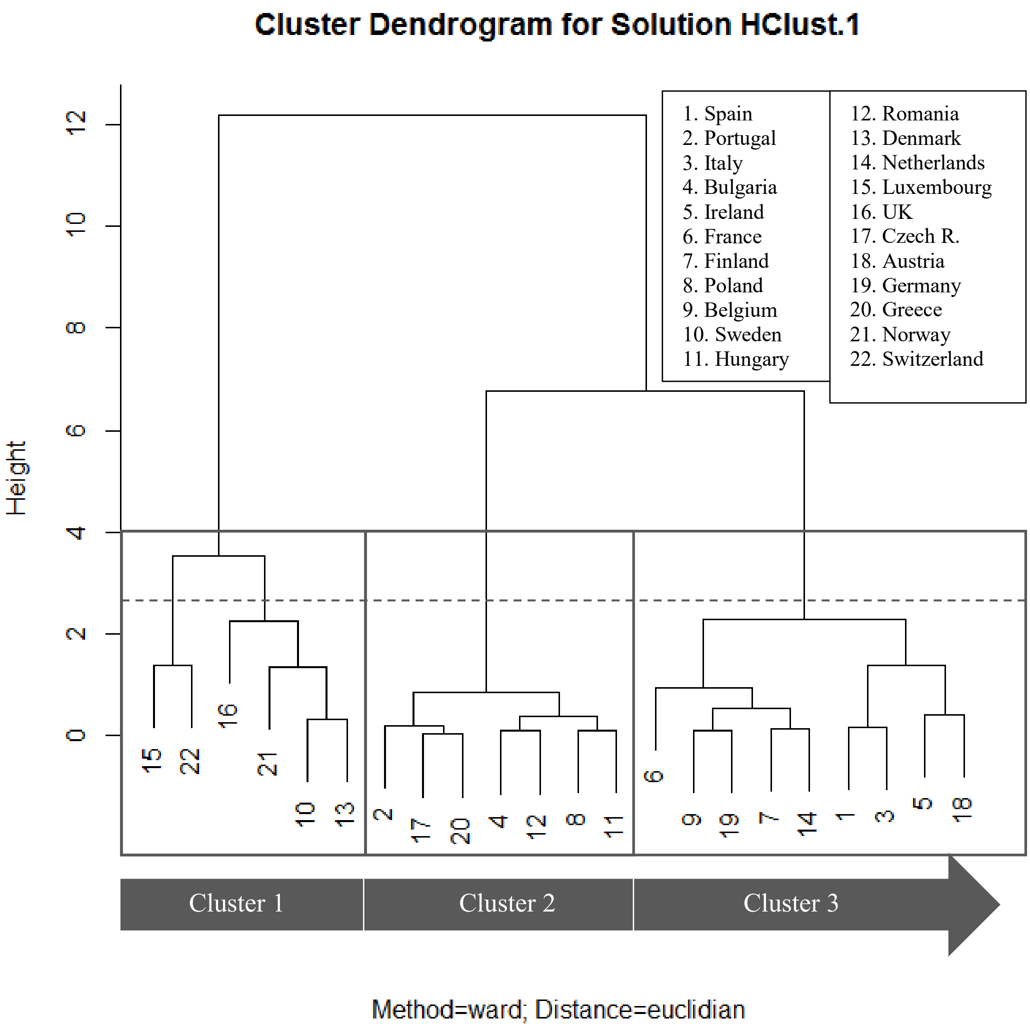


Luxembourg	91600
Norway	67400
Switzerland	64600
Ireland	46200
Denmark	45900
Sweden	45400
Netherlands	40000
United Kingdom	39500
Austria	39100
Finland	37800
Germany	37100
Belgium	36500
France	32800
Italy	26900
Spain	23300
Portugal	17300
Greece	16200
Czech Republic	15600
Poland	11100
Hungary	11100
Romania	8100
Bulgaria	6100

Source: Own representation based on Eurostat.

When consulting the per capita parameters, the result shows that completely different players reach top positions. Thus, Denmark is one of the top-three in the list of per capita investments – reminiscing of chapter 2.3.2, where Denmark was well forward in the percentage charts of total investments in the GDP – and Luxembourg is taking the far lead on the list of per capita gross domestic product.

Figure 107: Per Capita PE Investments – GDP per Capita / Industry Statistics



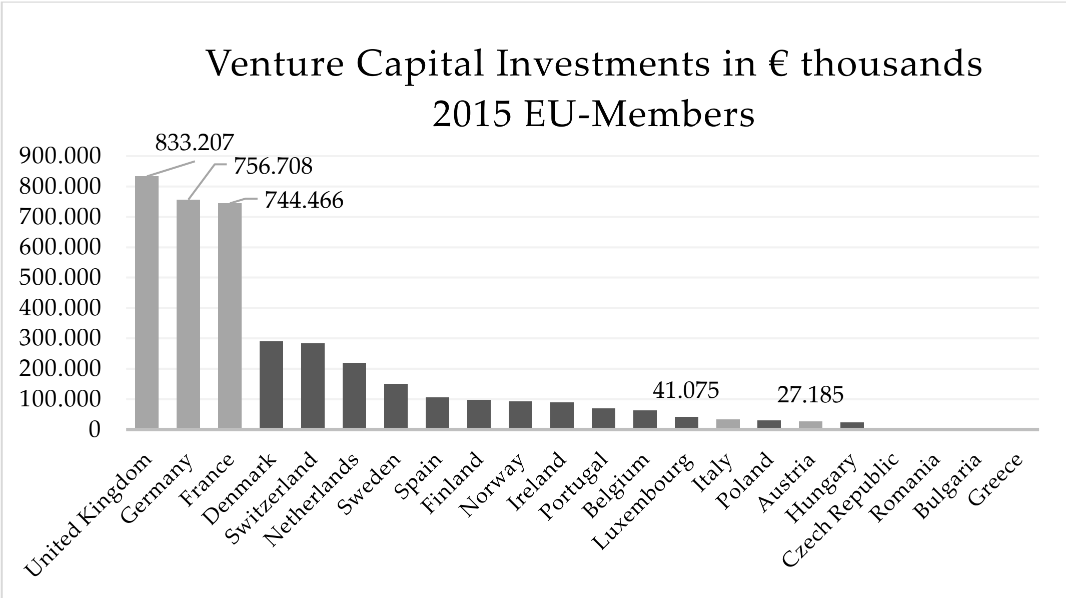
Source: Own representation created with Statistics *R*.

In order to determine groups with similar parameters among the 22 states, an agglomerative hierarchical clustering method has been applied. The dendrogram in figure 107, indicating the cluster merging process, suggests a stop at a height of either about 2.5 or 4. This corresponds to an allocation of either three, four or six clusters. Another step would lead to significantly more heterogeneous clusters. The downward shift, however, is not necessary as it can be well noted that a very different picture presents itself (Bacher, Pöge, & Wenzig, 2010, p. 237 et seq.). With three clusters, distinct structures are already visible. There are almost exclusively the East European countries plus Greece and Portugal, which are showing similarities to each other in cluster 2. Cluster 3 contains the actual surprises. Thus, regarding their investment activities of domestic affiliated companies with respect to the per capita gross domestic product, Spain and particularly Italy are perceptively less connected with Germans and French People, both perceived as particularly wealthy. The Scandinavian countries – excluding Finland – are grouped together in cluster 1, which suggests a strong similarity in the context of investments per capita and per capita GDP from holding companies domiciled domestically. It can be interpreted in such a way that the readiness to invest is not as pronounced in structurally weaker countries as it is in structurally strong countries. Two outliers are to be noted. Although Sweden would form its own cluster together with Denmark – with an even more expansive resolution – it is a positive example that with a medium high per capita income, the readiness to invest in Private Equity is particularly high. In Austria, the investments measured by GDP per capita, are particularly low for a Western country. Otherwise, there are quite some indications, that the GDP per capita is significantly involved in the willingness to invest.

4.4.2.3 Venture Capital Investments per Capita under Consideration of the per Capita Gross Domestic Product – Industry Statistics

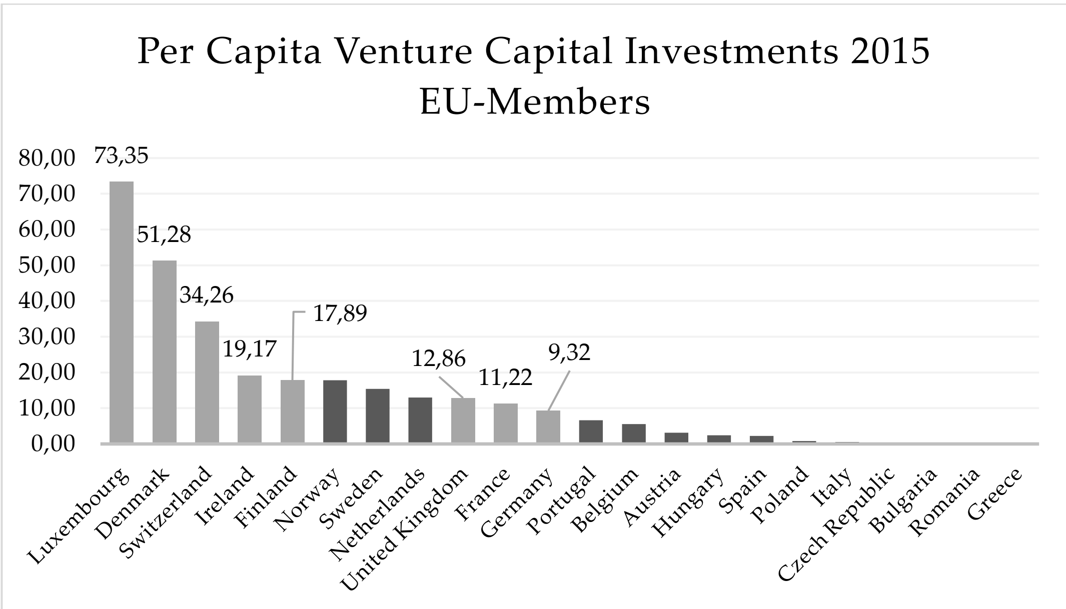
The consideration of Venture Capital investments is especially important for the entrepreneurs. The founders and developers of a company are an indicator for the growth of a corporation. Again, especially the major economies – see figure 108 – are largely responsible for the highest total investments in the Venture Capital field.

Figure 108: Venture Capital Investments – Industry Statistics 2015



Source: Own representation based on Invest Europe, 2016.

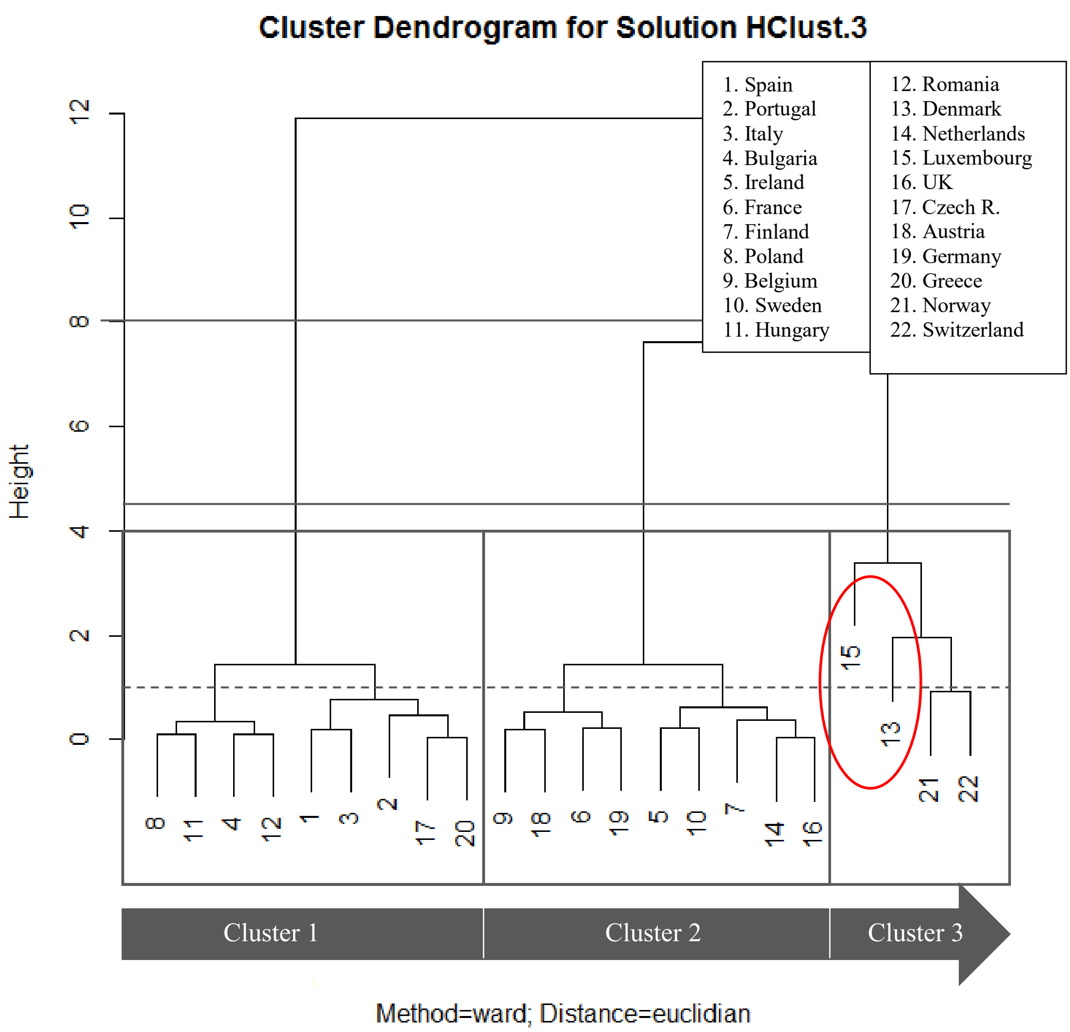
Figure 109: Per Capita Venture Capital Investments – Industry Statistics



Source: Own representation based on own calculation.

Even if the three largest economies, France, Germany, and the United Kingdom account for a large proportion of the Venture Capital investments in the European Union, it does not warrant the same facts for the per capita investments, as is proven in figure 109. On the contrary, France, Germany, and Great Britain clearly fall short of the top positions.

Figure 110: VC Investments / per Capita GDP – Industry Statistics



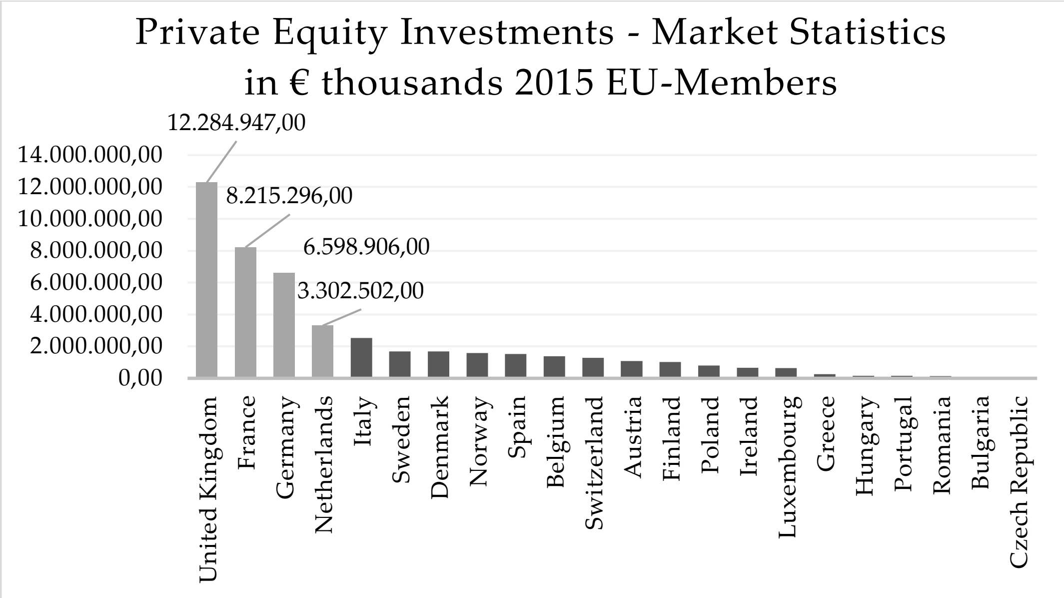
Source: Own representation created with Statistics R.

In order to determine groups with similar key figures among the 22 states, an agglomerative hierarchical clustering method has been applied at this point as well. The dendrogram of figure 110, indicating the cluster merging process, suggests a stop at either about 4 or approximately 8. This corresponds to an allocation of either two or three clusters. Everything beyond this shifts the similarities towards a greater heterogeneity, however in this examination it could make sense for clusters 1 and 2. A high resolution towards more clusters seems appropriate. Those countries classified as rather structurally weak are roughly grouped together in cluster 1. Their similarities among each other are also explicit in relation to the Venture Capital investments. Equally clear are Germany and Great Britain relatively close together within a cluster. Particularly striking are the similarities, which are apparently shared by Luxemburg and Denmark with regard to the total investment in the Venture Capital area. In this field, the most important one to entrepreneurs – the per capita Venture Capital investments concerning the per capita GDP – those two candidates are significantly close to each other in their similarities, as has already been noted at some other point. The conditions for investments in the early stages of such a transaction seem to be especially good in Luxembourg and Denmark.

4.4.2.4 *Per Capita Investments under Consideration of the per Capita Gross Domestic Product – Market Statistics*

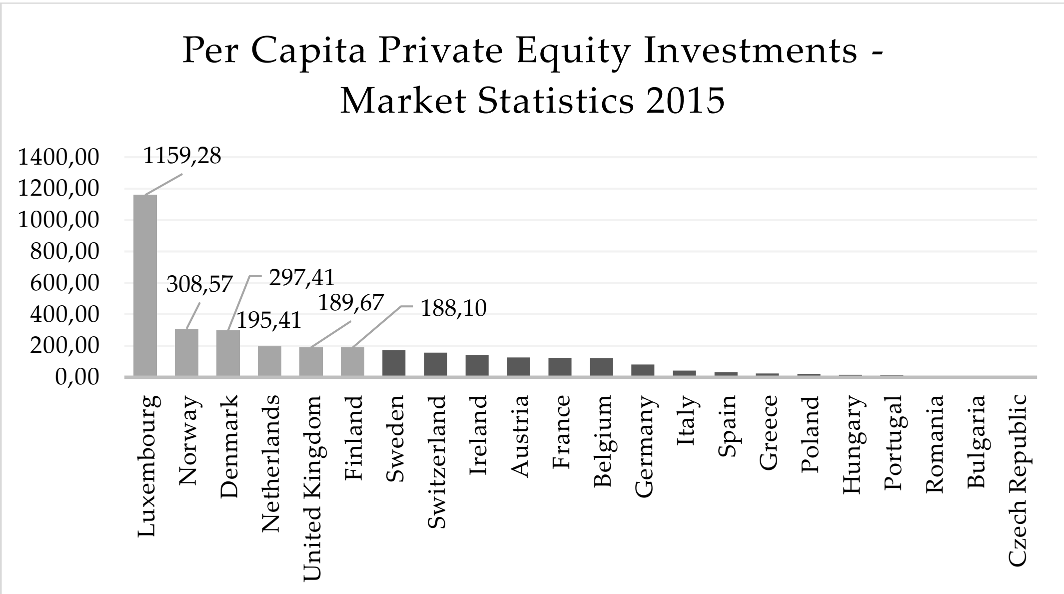
The following examinations apply to those investments executed in domestic portfolio companies. It is applicable to speak in this context of a willingness to invest in companies, which are domiciled in their own country. In figure 111 the overall investments in portfolio companies are presented and compared to the per capita investments in figure 112. The higher the willingness, the more favorable – with few exceptions – the conditions for these investments seem to be. The figures at this point are also in thousands of euros.

Figure 111: Private Equity Investments – Market Statistics 2015 EU Members



Source: Own representation based on Invest Europe.

Figure 112: Per Capita Private Equity Investments – Market Statistics 2015

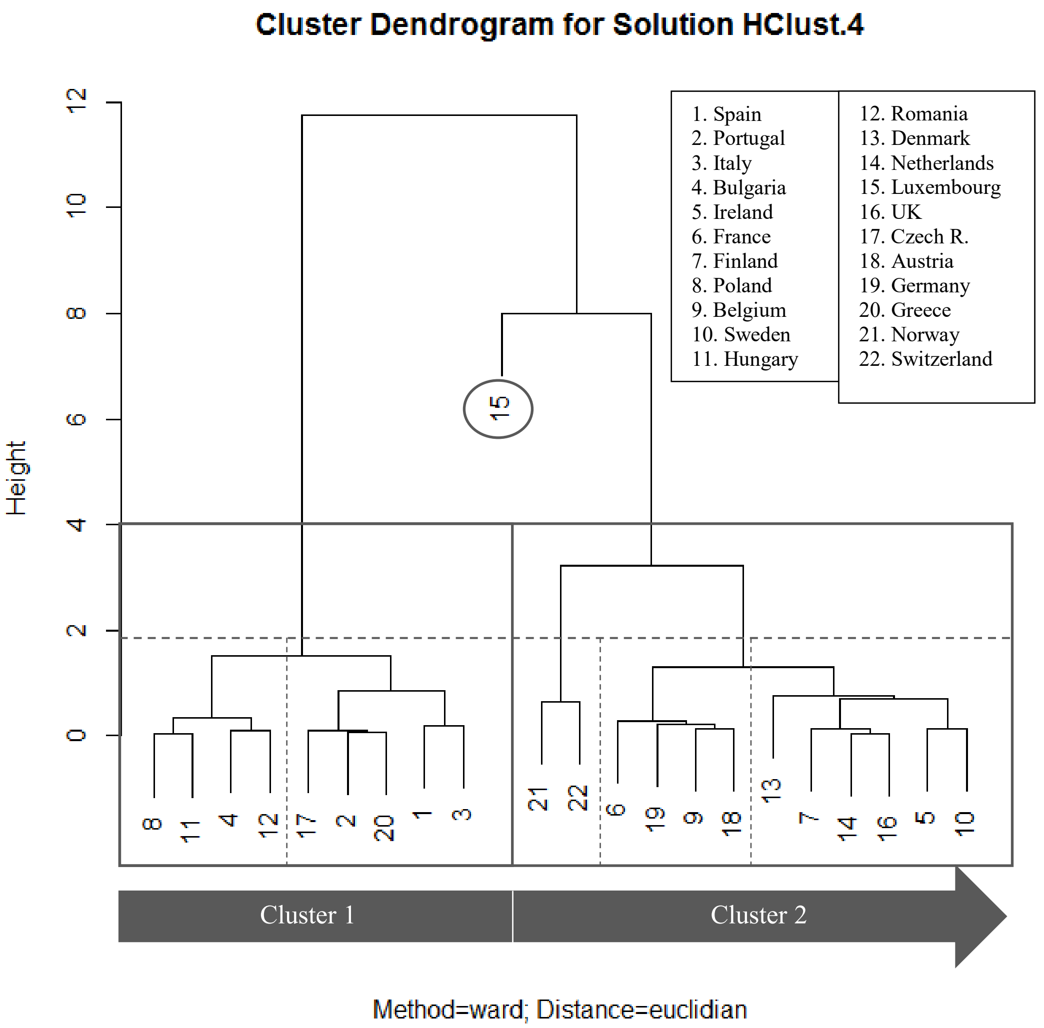


Source: Own representation based on own calculation.

In order to build a bridge to the per capita investments in domestic portfolio companies and to further raise awareness of the distortion caused by global figures, the total investments in this segment were investigated. The three largest economies are back at the top of the investments. That this representation reflects itself also in the per capita analysis may already be doubtful now, because the smaller economy of the Netherlands exposes itself in the front of the field.

Overall, the Scandinavian countries are in the lead again. Norway, as a non-EU member has established itself alongside the Danes, who obviously have a strong interest in investing in companies domiciled domestically; they make that quite clear by showing an increased commitment in Private Equity. Luxembourg completes the trio although Luxembourg – given its size – should have actually less investment potential in those companies. This shows the weakness of the French that much clearer and even more blatantly that of Germany, which falls back behind Austria in the per capita statistics, which had been noticed as less willing to invest. So, cautiously expressed, this leads to the reversal conclusion, that the willingness to invest in companies requiring domestic capital – Great Britain excepted at this point – is not particularly high with the big players and especially in Germany.

Figure 113: PE Investments per Capita / GDP per Capita – Market Statistics



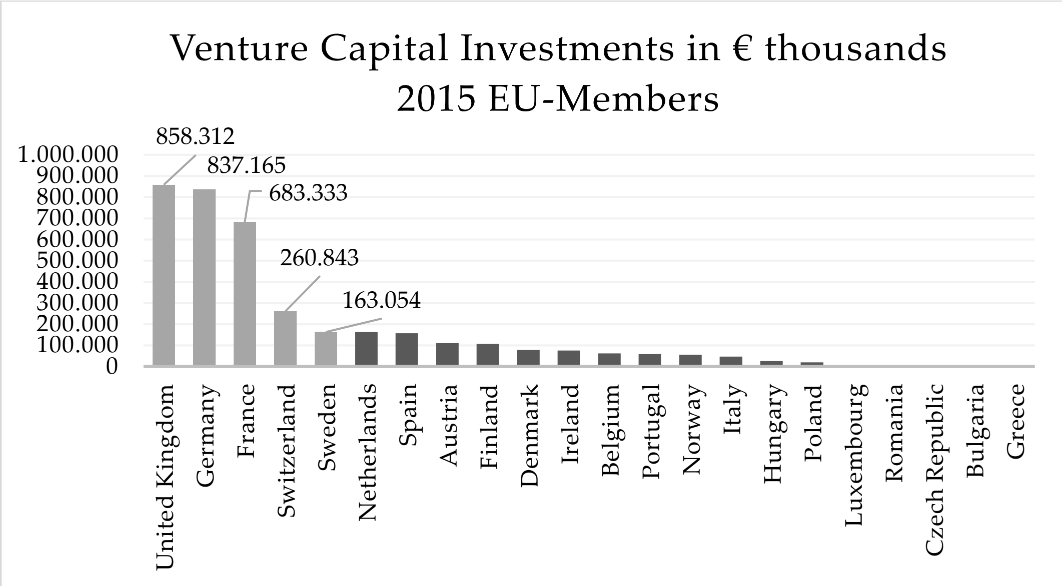
Source: Own representation created with Statistics R.

Groups were sought that show similarities in terms of their willingness per capita to invest in domestic-based portfolio companies considering the per capita gross domestic product. The agglomerative hierarchical clustering method used in figure 113 shows through merger processes in the corresponding dendrogram that a stop at the level of about 2 or about 4 seems likely. This corresponds to a division in either two or six clusters. Everything beyond this shifts the similarities towards a greater heterogeneity. However, Luxembourg could also be viewed as a separate cluster – therefore, four clusters are also labeled in the illustration – since the distance to the next level of similarity is apparently relatively large. This confirms the investigation of the total investments in this sector and emphasizes the trend that the conditions for investments in Luxembourg in the Private Equity field are particularly good. In cluster 1, the structurally weaker countries are represented, while in cluster 2 those countries are showing similarities among each other, which belong to the western and northern European sphere. The fact, that Norway is showing strong similarities to the Switzerland can be regarded just as remarkable as the fact that Germany has more similarities with Austria or Belgium. This in turn, due to the weaker investment propensity of Austrians and the current general structural weakness of Belgium, does not provide a positive signal in regards to the willingness to invest Venture Capital in own companies.

4.4.2.5 Per Capita Venture Capital Investments under Consideration of the per Capita Gross Domestic Product – Market Statistics

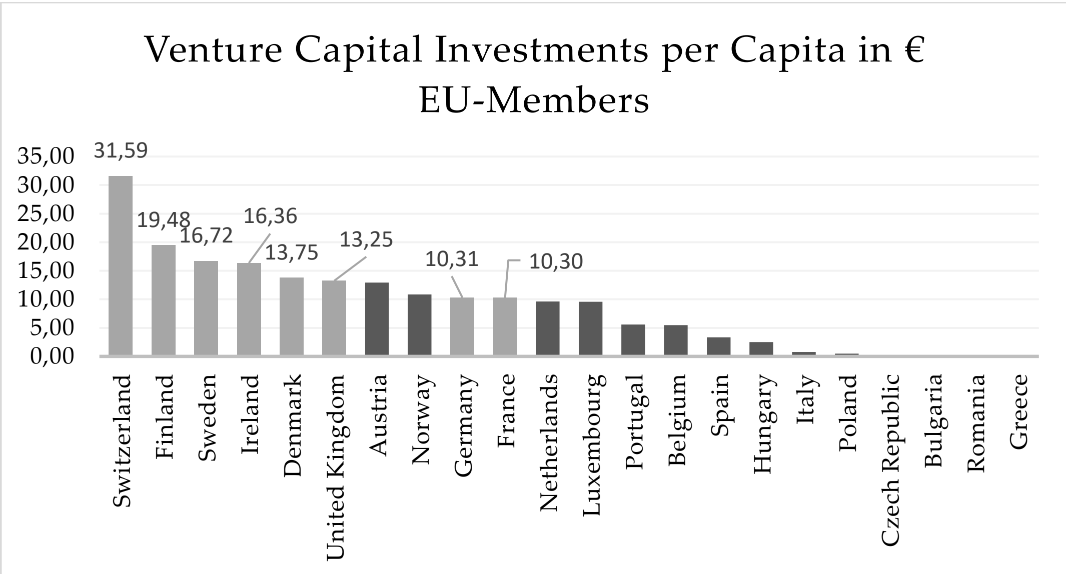
Since the Venture Capital activities are of particular interest and importance in connection with entrepreneurs, the investigative studies of the same in regards to similarities are of equal importance in order to determine where the breeding ground for the investments in young companies with risk-carrying capital will be most productive. In this, the total investment volume needs to be considered, although it does not reflect the willingness to invest, but does convey an impression of what could be possible when considering the potential.

Figure 114: Venture Capital Investment – Market Statistics EU-Members



Source: Own representation based on Invest Europe.

Figure 115: Venture Capital Investments per Capita – Market Statistics



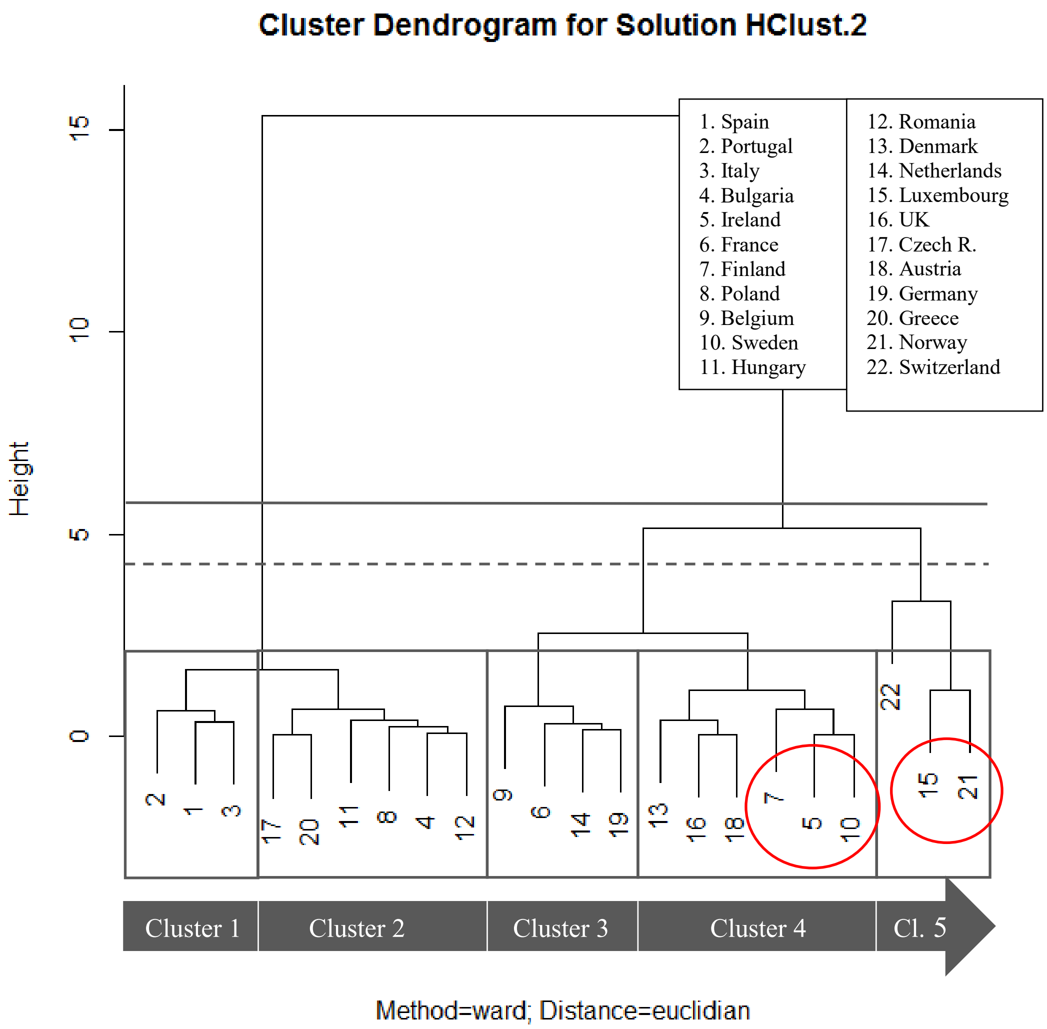
Source: Own representation based on own calculation.

The graph in figure 114 shows United Kingdom as the top leader in terms of Venture Capital investments in domestic portfolio companies. Not only are France, and Germany in the statistics very close by, but it is already clear at this point that these statistics do not represent the true performance of a country. It is also from this thesis that Germany is significantly more populous than France is. Nevertheless, the two EU Member States, with respect to investments in young companies, are tight by a narrow margin. This already suggests that the major economies do not move as much in this segment, as can be seen in figure 115.

Concerning the investments in young companies in the own country, the Scandinavian countries are positioning themselves at the forefront with Finland, and Sweden taking the lead behind the Switzerland. Almost on par, Ireland presents itself – an EU Member State who was not too long ago operating under the EU bailout fund. Ireland as well had been the first country to leave this rescue fund again. When considering investments in young companies domiciled domestically, it appears as if Ireland has done many things right with its program and that there is a relationship between the outstanding positioning in these statistics and the overall economic revival. It is quite noticeable that the three largest economies – led by Germany and France– do not score well at all.

Sweden, Finland and Ireland are very similar in their investment behavior and therefore from a separate sub cluster - in cluster 1. To find even other groups among the 22 states with similar operating figures, an agglomerative hierarchical clustering method was used. The dendrogram of figure 116, indicating the cluster merging process, suggests a stop at a height of either a little above 1 or at approximately 2. This corresponds to a division into four or five or six clusters. A higher resolution would be possible as well, but is not necessary since it becomes already clear which countries undertake special efforts with regard to Venture Capital activities that benefit domestic enterprises. The similarities that Sweden, Finland and Ireland and Luxembourg and Norway are bearing concerning the Venture Capital investments under consideration of the per capita gross domestic product are quite large. Also, the distances to the following countries are large enough to allow for the statement that for these countries, which are executing for entrepreneurs outstandingly important investments in young companies, applies that the conditions prevailing there are significantly better than in other countries of Europe.

Figure 116: VC Investments per Capita / GDP per Capita – Market Statistics



Source: Own representation with Statistics R

However, Norway is not a EU member and can therefore be considered only conditionally.

4.4.2.6 Interim Conclusion I

The previous studies have clearly shown that the investment activities of domestic investment companies also significantly depend on the gross domestic product of each country. Thus, the three largest economies also house the three largest investment volumes of the European Union and even Europe. The more meaningful performance figure gross domestic product per capita however, does recalibrate the circumstances. In the industry statistics, Denmark is very far forward in per capita investments. Overall, the Scandinavian countries present themselves at the top, framed by Luxembourg and the United Kingdom. In terms of per capita investments of the above-mentioned holding companies in the early stages of financing, the Scandinavian countries are once again among the top players - with Luxembourg taking the lead now and joined by Ireland, which is obviously making strong efforts to support their founders. All of them are, in part clearly, ahead of alleged tradition markets of France, Germany or even Great Britain, which afford to jointly bring up the rear of the upper half together with Germany. Ironically, the three big players show an ailing interest concerning entrepreneurs. Since it has been shown during the recent analysis that these three countries – examining the investments under consideration of the per capita gross domestic product – have found themselves usually in one cluster, it can be already concluded at this point, that the much-discussed basic conditions play little or no role, or else that they are significantly worse in these countries compared to the Scandinavian countries, Luxembourg or Ireland. During the previous studies in and around this thesis it could not be determined that particularly the Venture Capital transactions in Great Britain, Germany or France were at a disadvantage compared to the other transactions. On the contrary, the tax environment for Private Equity as a generic term do also apply to Venture Capital. Only special legal arrangements, such as in Germany the distinction between commercial and asset management, or the treatment of loss carry forwards could be an obstacle in this regard. Otherwise it is necessary, to take into account those taxes that apply to Private Equity as well as Venture Capital funds. To be considered, and therefore to be examined at a later point are the already mentioned taxes listed below:

- Capital Gains Tax,
- Withholding Tax,
- VAT and Corporate Income Taxes.

It is especially important to investigate whether there is relevant evidence that these taxes, individually or in total, affect the willingness to invest in the form of volume or not.

First, however, the investment activities in portfolio companies under consideration of the per capita domestic products shall be analyzed. As far as the market statistics are concerned – thus the willingness of the countries, or rather the willingness of the inhabitants of these countries, to invest in domestic portfolio companies – it can be stated that in the sense of the total volume, the three largest economies once again take the lead, while the so-called little ones seem to be underrepresented; this changes completely with the per capita. Denmark is one of the tops of the statistics for those countries that invest in domestic portfolio companies. In the Venture Capital field, however, this turns out differently. Where founders are participating the most – i.e. the commitment of the responsible heads in young companies in a country, which are in one of the early stages of the financing needs – Denmark is still found in the upper third, however, it has strong competition from the field of EU Member States with Sweden, Ireland and Finland.

The three latter countries were able to convince by far and are initially the first choice for the examination of appropriate fiscal framework. Since the Scandinavian countries – plus Ireland – collectively perform strong, and according to previous finding, a selection of their fiscal parameters in favor of a new fiscal treatment of Private Equity funds and their operators could make sense, provided that favorable tax conditions positively affect the investment behavior. The investigation of tax parameters as an influencing factor will be conducted following the examination of the investment behavior of countries under consideration of the purchasing power. In the process, the coherencies between the purchasing power and the investment will be examined to the effect that exclusively the per capita Venture Capital investments of holding companies within the country and the Venture Capital investments in domestic portfolio companies are put in relation to the purchasing power. This serves to make it clear that especially the early-stage financing is important for growth. It is demonstrated adequately and convincingly that the conditions apply to all financing stages, so that the different results from the industry statistics and the market statistics are not exclusively attributed to them.

4.4.3 Investments under Consideration of the Purchasing Power Standard (PPS)

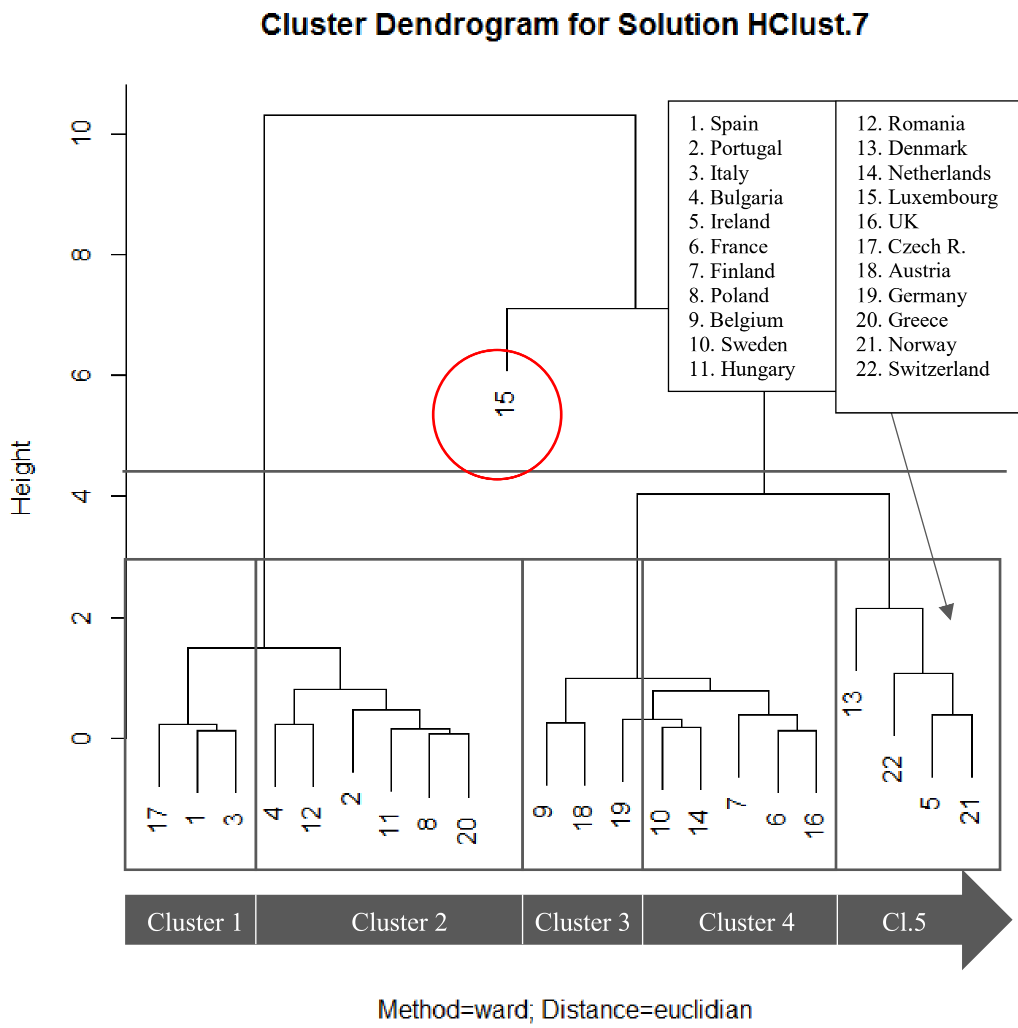
4.4.3.1 Per Capita Venture Capital Investments under consideration of the Purchasing Power Standard (PPS) – Industry Statistics

Since the ranking of countries examined in terms of purchasing power standard differs only insignificantly from that of the per capita gross domestic product, the investments under consideration of the PPS will be examined only in terms of Venture Capital. The purchasing power standard is to eliminate the distortions that occur due to different price levels in different countries. The data for Venture Capital can be found in the previous chapters.

The dendrogram of figure 117, indicating the cluster merger process, suggests a stop either at a level of about two or at approximately four. This corresponds to a division into four or five clusters. In this case, a higher resolution is inconceivable.

If the indicators – thus the ratio of the two parameters to each other – Venture Capital investments per capita are being viewed in relation to the purchasing power standard, the result is a clustering in pure form as expected. Taken the previous results into account, the fact elucidates itself that the conditions for Venture Capital concerning the domestic holding companies are particularly well suited for Denmark, Norway and Switzerland and that the Scandinavian countries and Ireland linger in close proximity. Luxembourg belongs in this series. Because Luxembourg has an extremely high PPS, this country is displayed as an outlier. So far, a difference from the parameter gross domestic product per capita is barely visible.

Figure 117: VC Investments per Capita / PPS –Industry Statistics



Source: Own representation created with Statistics R.

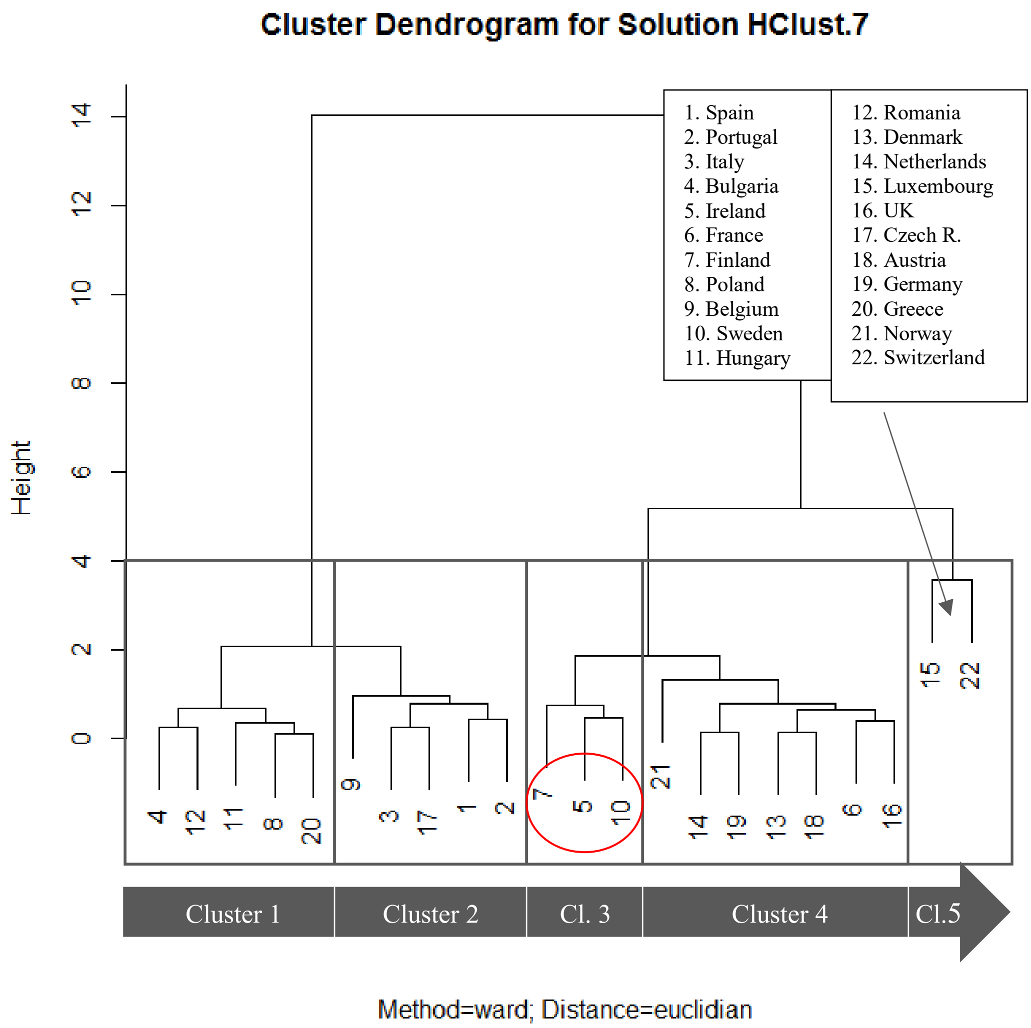
This in turn leads to the conclusion that the gross domestic product per capita is not only permissible, but also advisable as an appropriate instrument to conduct a subsequent examination under consideration of taxes.

4.4.3.2 *Per Capita Venture Capital Investments under Consideration of the Purchasing Power Standard (PPS) – Market Statistics*

The more interesting variant of consideration for entrepreneurs – that is, the investments in target companies – shall at this point be illustrated through the formation of groups within the meaning of Venture Capital investments under consideration of the purchasing power standard (PPS). This investigation shall confirm or refute that the investments in the early stages of a Private Equity financing is consistent with the previous findings. Therefore, whether, as in this case, an above-average Purchasing Power leads to an above-average Venture Capital commitment per capita.

The dendrogram of figure 118, indicating the cluster merger process, suggests a stop either at a level of about two or at approximately four or six. This corresponds to a division into four or five clusters. A higher resolution in this case is conceivable and, in the case of Denmark, desirable. Nevertheless, even now, a clear tendency could be made visible. This examination has confirmed, which was already illustrated with the examination of the Venture Capital activities under consideration of the per capita gross domestic product. Sweden, Ireland and Finland are from one group when it comes to willingness to invest in target companies. They do so at such a high level that the gap to the next group is clearly significant. The fact that Switzerland is a member of a group with Luxembourg indicates conditions that can also be found outside the European Union.

Figure 118: VC Investments per Capita– PPS – Market Statistics



Source: Own representation created with Statistics R.

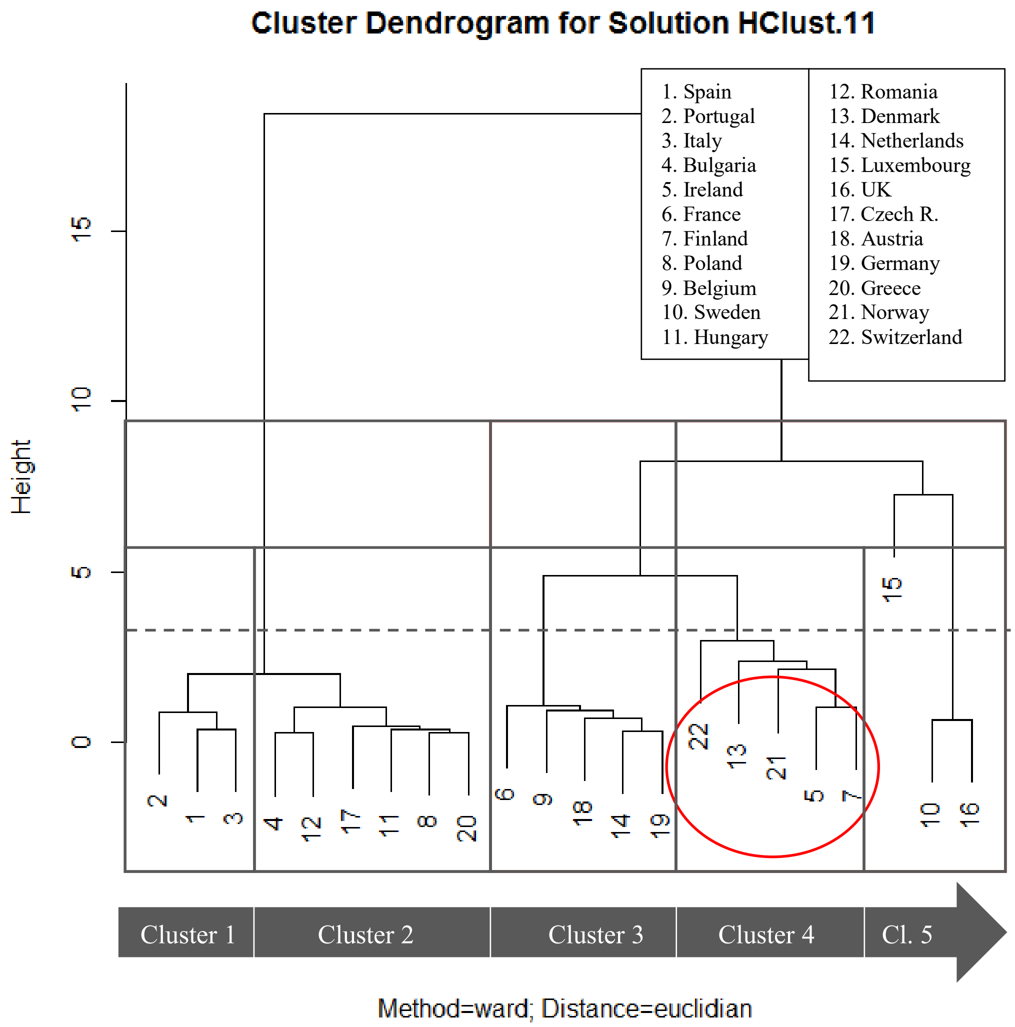
There are apparently no sufficiently enough differentiated basic conditions for Venture Capital within the Union.

4.4.3.3 Interim Conclusion II

So far, the investment behavior was analyzed based on the gross domestic product. The expansion of the investigation on to the purchasing power standard can be viewed as an attempt to support the previous studies. If the purchasing power standard is considered in itself, it is noticeable that none of the countries, which are regarded as one of the major economies in the European Union, are among the top three countries having the highest purchasing power standard. That the Scandinavian countries, Ireland and Benelux countries (Belgium, Netherlands, and Luxembourg) are far ahead has been noticed in other evaluation horizons. When now consulting the data, which are related to the purchase price standard, so it has to be stated that the Scandinavian countries exposes themselves in every respect.

However, it is not true that those Scandinavian countries, which are taking the lead in regards to investments of domestic holding companies, are also leading the board in the field of investments in domestic target companies. Rather, Denmark is investing strongly in terms of their holding companies; while it is Sweden, whose target companies are very benefitting from the investments. It must be taken in to consideration that for the two forms of statistics – the industry statistics and the market statistics – in all previous investigations no distinction had been made, whether and to what extent the investments derive from abroad. Thus, it is especially the market statistics, which is at some risk to be misinterpreted. It involves, for example, investments that are aimed at domestic target companies. It is not only feasible, but a fact that of course foreign holding companies invest in target companies which are declared domestic in this thesis. On the other hand, the high propensity, respectively the medium-high willingness to invest, will be dependent on the particular parameters of the countries under review, so it is safe to assume that holding companies, domiciled domestically will be the first to perceive a good market in that country. This means: if the conditions in a country are good, then they will be preferably so for nationals and foreigners. As it has turned out that the two examination parameters, gross domestic product per capita and purchasing power standard, have not led to significantly different results; it can be safely assumed that investments, in whatever direction, clearly depend on the gross domestic product, respectively the purchasing power.

Figure 119: VC Investments / PPS / GDP - per Capita



Source: Own representation with Statistics R.

A high standard leads to high investments. However, in this study it is to be made clear that the efforts of a country are mainly recognized by how much the individual is willing to support these efforts. This is done by the observation per capita. If the investments depend on the above parameters, it is just as certain that investments can produce variable results through taxes, which rightly assumes that taxes can reduce the gross domestic products per capita or the standard. To do so, the investments under consideration of the already listed fiscal parameters are being investigated hereinafter. Prior to that, however, it is being examined which groups form under consideration of all previously, in detail investigated parameters relating to Venture Capital. Thus, this cluster analysis incorporates the fundraising per capita – which was not examined separately – the Venture Capital investments per capita in regards to the purchasing power standard and the gross domestic product per capita. With this analysis, the above-mentioned variables are taken into account both in the industry statistics and the market statistics. Naturally, the data were again standardized because of their existing diversity.

A clustering (figure 119) in two or four groups does not seem to be indicated at this point, since the exposed position of the countries Denmark, Ireland, Norway, Switzerland, and Finland would be somewhat dissolved by it. Rather, particularly these five countries showed clear similarities in the previous examinations. The three EU countries Denmark, Ireland and Finland did this at such a high level that it can be suggested that obviously conditions can be found there which seem to appear particularly favorable even with respect to several variables. Since this analysis is divided very delicately – in five clusters – it is rather not necessary to present the stops in detail. On the contrary, clusters can be merged again.

Therefore, clusters 1 and 2 – also from the experience of previous investigations – can be merged again. The similarities overall between the eastern and southern European countries are significant. Applicable here as well: the structurally weaker Member States of the European Union are also very similar to each other in terms behavior regarding the Venture Capital commitment. Particularly striking is the fact that – under consideration of all Venture Capital parameters and their reference variables – two of three of the largest economies of the EU eventually group together again. Flanked by Belgium, the Netherlands, and Austria the conditions – despite different assessments in some areas – seem to very similar for Venture Capital, which is proven by the small gaps.

4.4.4 Investments under Consideration of Taxes

4.4.4.1 Per Capita Venture Capital Investments Taking into Account Capital Gains Taxes

Capital gains taxes are taxes on income (Eggert, 2016, p. 1). This means that when a sale of assets occurs – which of course also includes investments – a tax is payable on the appreciation (Eggert, 2016, p. 1). This form of taxes is perceived very differently in the countries of the European Union (EU). So, in some countries of the EU such as Italy, Finland, and the UK there is no approach for this type of taxes, while other countries provide quite a taxing of the profit shares (EVCA Tax Benchmark Study, 2013). If the capital gains taxes of the countries examined above, Germany, Luxembourg, and Austria, are being considered, distinct differences are to be noted already (EVCA Tax Benchmark Study, 2013).

Germany

Five percent of the capital gains are not deductible operating expenses, which affect the corporate income tax and the trade tax of the particular corporation (Braun, Dennerlein, & Wünsche, 2012, p. 137 et seqq.; Graw, 2009, p. 30 et seqq.; Büsching, 2014, p. 14 et seqq.; Grützner, 2014, p. 55 et seqq.; EVCA, 2013, pp. 82-86). This results in effective tax rates between 1.14% and 1.65%, whereas this is being calculated (see 3.4.6 Fiscal Regulation Parameters of Private Equity Funds in Germany) as follows (Braun, Dennerlein, & Wünsche, 2012, p. 137 et seqq.; Graw, 2009, p. 30 et seqq.; Büsching, 2014, p. 14 et seqq.; EVCA, 2013, pp. 82-86; Grützner, 2014, p. 55 et seqq.):

The output variables are: corporate income tax of 15% in addition to 5.5% solidarity surcharge and trade tax (EVCA, 2013, pp. 82-86), varying from 7.0% to up to 17.15%. 15% plus 5.5% result in 15.825%. By adding the trade tax of either 7.0% or even 17.15%, it results in a percentage of 22.825% or 33.035%. 5% of which are those 1.14% respectively 1.65% (Braun, Dennerlein, & Wünsche, 2012, p. 137 et seqq.; Graw, 2009, p. 30 et seqq.; Büsching, 2014, p. 14 et seqq.; EVCA, 2013, pp. 82-86; Grützner, 2014, p. 55 et seqq.).

Luxembourg

Luxembourg does not have any specific form of taxation of this type (Merten, 2004, p. 48 et seqq.; Höhn & Höring, 2010, p. 172 et seqq.; Fort, 2014, p. 21 et seqq.). However, it is feasible that the profits on realization that are reached by resident or non-resident Luxembourg investors will be succumbed to income tax or corporation tax (Fort, 2014, p. 21 et seqq.; Merten, 2004, p. 48 et seqq.; Höhn & Höring, 2010, p. 172 et seqq.; EVCA, 2013, pp. 124-132). If a nonlocal shareholder has his tax domicile in a state that has a double-tax agreement with Luxembourg, so generally, the taxation characteristics of the nation of domicile of the financers apply (Fort, 2014, p. 21 et seqq.; Merten, 2004, p. 48 et seqq.; Höhn & Höring, 2010, p. 172 et seqq.; EVCA, 2013, pp. 124-132). If the external participator has his tax domicile in a state that has no double-tax agreement with Luxembourg, the capital gains from the disposal of shares in a Luxembourgian corporation are assessable in Luxembourg. If the non-local shareholder – equal well whichever way – owns an equity holding of more than ten percent as a participation in a Luxembourgian corporation and if one of the succeeding terms are fulfilled (Fort, 2014, p. 21 et seqq.; Merten, 2004, p. 48 et seqq.; Höhn & Höring, 2010, p. 172 et seqq.; EVCA, 2013, pp. 124-132):

- if the investor abolishes its holdings within a period of a half year after the acquisition,
- if the investor for more than fifteen years pays taxes in Luxembourg. However, it can give deductions at this point in connection with the disposal of the shares - see 3.6.4 Fiscal Regulation Parameters of Private Equity Funds in Luxembourg.

Profit on realization from a completely assessable company, which has its domicile in Luxembourg, is essentially succumbed to corporate taxes with a composed tax rate of 29.22% (Fort, 2014, p. 21 et seqq.; Merten, 2004, p. 48 et seqq.; Höhn & Höring, 2010, p. 172 et seqq.; EVCA Tax Benchmark Study, 2013, pp. 124-132). Capital gains of these companies may be exempted from the corporate income tax and from municipal tax (Fort, 2014, p. 21 et seqq.; Merten, 2004, p. 48 et seqq.; Höhn & Höring, 2010, p. 172 et seqq.; EVCA Tax Benchmark Study, 2013, pp. 124-132).

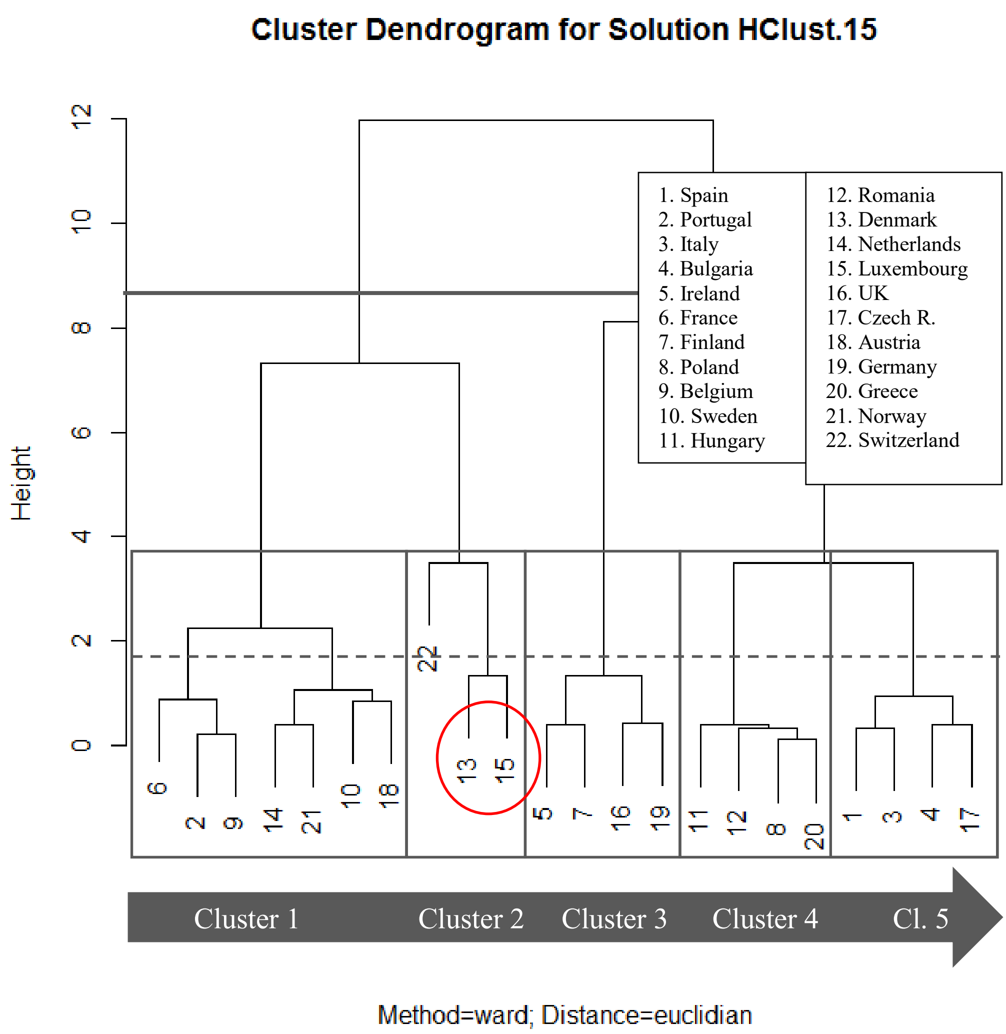
Austria

Profit on realization that are realized by private financiers are succumbed to capital gains tax (Gierhake, 2014, p. 251 et seqq.; Dziurdz, 2014, p. 80 et seqq.; Kirchmayr, 2014, p. 33 et seqq.; EVCA, 2013, pp. 33-37). Regulated by the kind of capital asset, the deduction is mandatory (Kirchmayr, 2014, p. 33 et seqq.; Gierhake, 2014, p. 251 et seqq.; Dziurdz, 2014, p. 80 et seqq.; EVCA, 2013; pp. 33-37). Profit on realization realized by corporations are succumbed to corporate income tax at a standard rate of 25% (Kirchmayr, 2014, p. 33 et seqq.; Gierhake, 2014, p. 251 et seqq.; Dziurdz, 2014, p. 80 et seqq.; EVCA, 2013; pp. 33-37). However, there are exceptions for qualified international investments (Kirchmayr, 2014, p. 33 et seqq.; Gierhake, 2014, p. 251 et seqq.; Dziurdz, 2014, p. 80 et seqq.; EVCA, 2013; pp. 33-37). Otherwise, there are no further taxes on capital gains (Kirchmayr, 2014, p. 33 et seqq.; Gierhake, 2014, p. 251 et seqq.; Dziurdz, 2014, p. 80 et seqq.; EVCA, 2013; pp. 33-37). Domestic dividends between Austrian companies are tax-exempt (Kirchmayr, 2014, p. 33 et seqq.; Gierhake, 2014, p. 251 et seqq.; Dziurdz, 2014, p. 80 et seqq.; EVCA, 2013; pp. 33-37). Capital gains of Austrian companies from the disposal of another corporation are also succumbed to a tax rate of 25% (Kirchmayr, 2014, p. 33 et seqq.; Gierhake, 2014, p. 251 et seqq.; Dziurdz, 2014, p. 80 et seqq.; EVCA, 2013; pp. 33-37).

The market is very dynamic (Paul H. , 2013, p. 1) and thus is the legislation of the individual countries of the EU. Although there are or should be national variations in regards to the Private Equity vehicles and their treatment, the tax treatment within the European Union is far from being uniform as can be seen based on the above considerations. Only three of the Member States have been touched and examined. The inconsistency – case with respect to the capital gains taxes – became evident in the preliminary assessment. At this point, an investigation is necessary, which looks in to the per capita Venture Capital investments in relation to the capital gains taxes. Initially the highest conceivable tax rate is taken into account.

The dendrogram of figure 120, indicating the cluster merging process, suggests a stop at a level of either about 1.8, 3.8 or – which is hardly helpful – close to about 8. This corresponds to a division in to five groups. A different resolution (in six or seven groups) would be feasible, but is neither required nor appropriate, since the resolution in five clusters – or six, when taking Switzerland as an outlier into account – already confirms similarities of groups which have already resulted from the investigations without the consideration of taxes.

Figure 120: Per Capita VC Investments / Capital Gains Taxes



Source: Own representation with Statistics R.

Therefore, the countries Denmark, Luxembourg and Switzerland are very close to each other even when taking the capital gains tax into account and form their own cluster. The two very strong Venture Capital states, by volume, Germany and Great Britain are forming a group.

The amount of investments of domestic investment companies in Venture Capital and the Venture Capital activities in domestic portfolio companies has already been examined elsewhere in this paper. It turned out that the countries of Denmark, Luxembourg and Sweden are each among the top 5 of the EU Member States in regards to the willingness to invest. Their proximity to one another, even after the investigation including any capital gains taxes, shows that the conditions for the participation in Venture Capital for investment companies from these countries and investments in domestic portfolio companies is particularly good and stable.

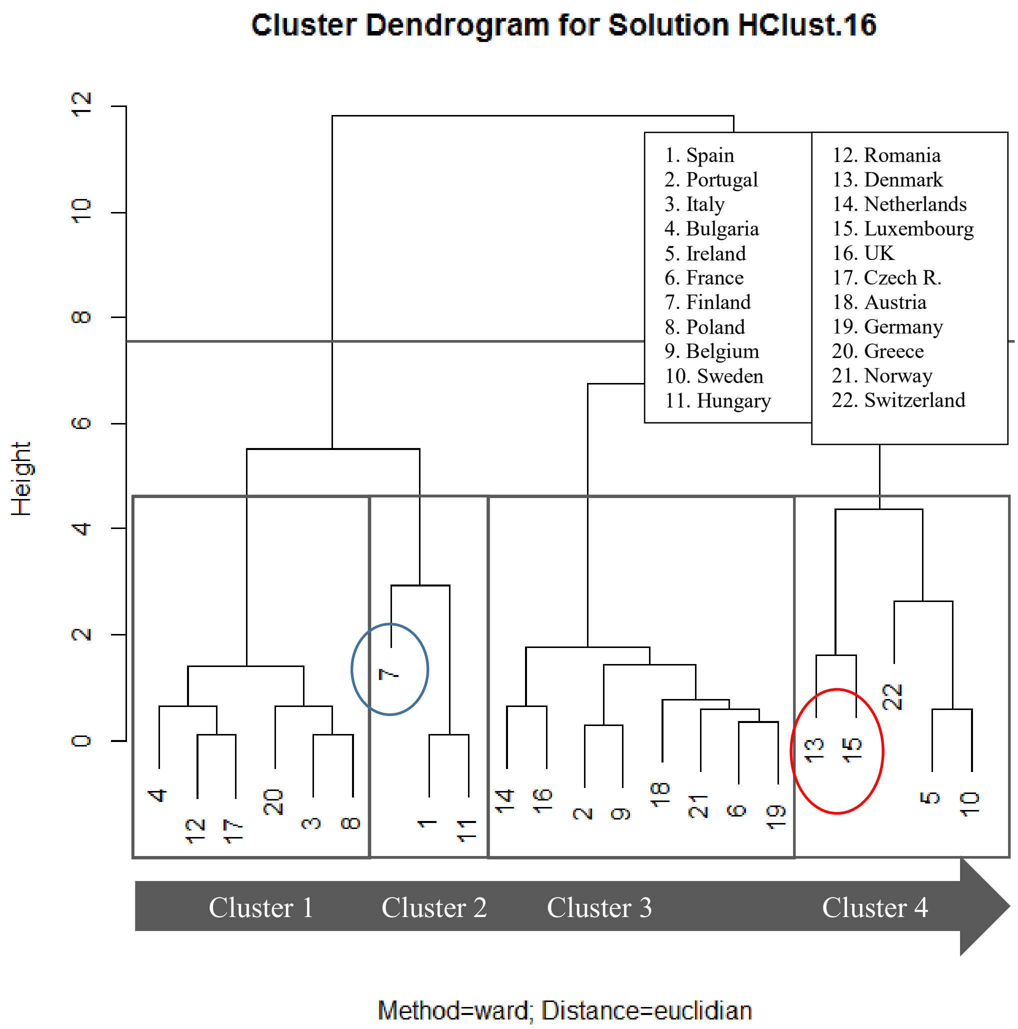
If the gross domestic product per capita of these countries is consulted, it is striking that the countries named at this point are among the best which allows for the thesis that a high per capita gross domestic product promotes a high propensity to invest, but also that a high willingness to invest attracts a high gross domestic product per capita.

4.4.4.2 Per Capita Venture Capital Investments under Consideration of the Withholding Taxes

In addition to the capital gain taxes, the withholding taxes and the VAT on management fees are the most important taxes in the consideration at fund level. For withholding taxes, the same conditions apply as for the capital gains taxes. There is a minimum value and a maximum value. While it remains unchanged in Germany with 26.375% and in Austria with 25%, in Luxembourg there are either 0% or 35% withholding tax (Jarass & Obermair, 2015, p. 70 et seqq.; EVCA Tax Benchmark Study, 2013). The data have been standardized for the analysis, because Luxembourg is relatively far off with the per capita Venture Capital investments of domestic holding companies and there might be no withholding tax (Jarass & Obermair, 2015, p. 70 et seqq.). The standardization changes the dendrogram only insignificantly, however, puts the outlier Luxembourg closer to the visible range of the analysis.

The dendrogram in figure 121, indicating the cluster merging process, suggests a stop at a level of about four. A different resolution is hardly conceivable, since the distances to each other are too big. This results in four clusters.

Figure 121: Per Capita VC Investments / Withholding Taxes



Source: Own representation created with Statistics R.

A particular prominence is the gathering of Ireland and Switzerland, both of which are known for their strong Venture Capital commitment, but also possibly impose high tax burdens on companies. The second unusual event is that the withholding taxes unites the Scandinavian countries. Denmark and Sweden which show great similarities in Venture Capital investments under considerations of the withholding tax and thus move more and more into the focus of interest in regards to optimized – now also in a fiscal aspect – conditions, are now joined by Finland, which presents quite some similarities to the above-mentioned countries. Finland had moved closer to the best, but is an outlier in this analysis. This can be explained, however, with the extremely low withholding taxes. Other countries with large similarities and higher per capita income, tend to have higher tax rates.

However, a balanced ratio, and therefore a balanced fiscal framework is sought, as is being suggested in Sweden and Denmark.

4.4.4.3 Per Capita Venture Capital Investments under Consideration of the Relevant Taxes and the Reference Parameter GDP and PPS

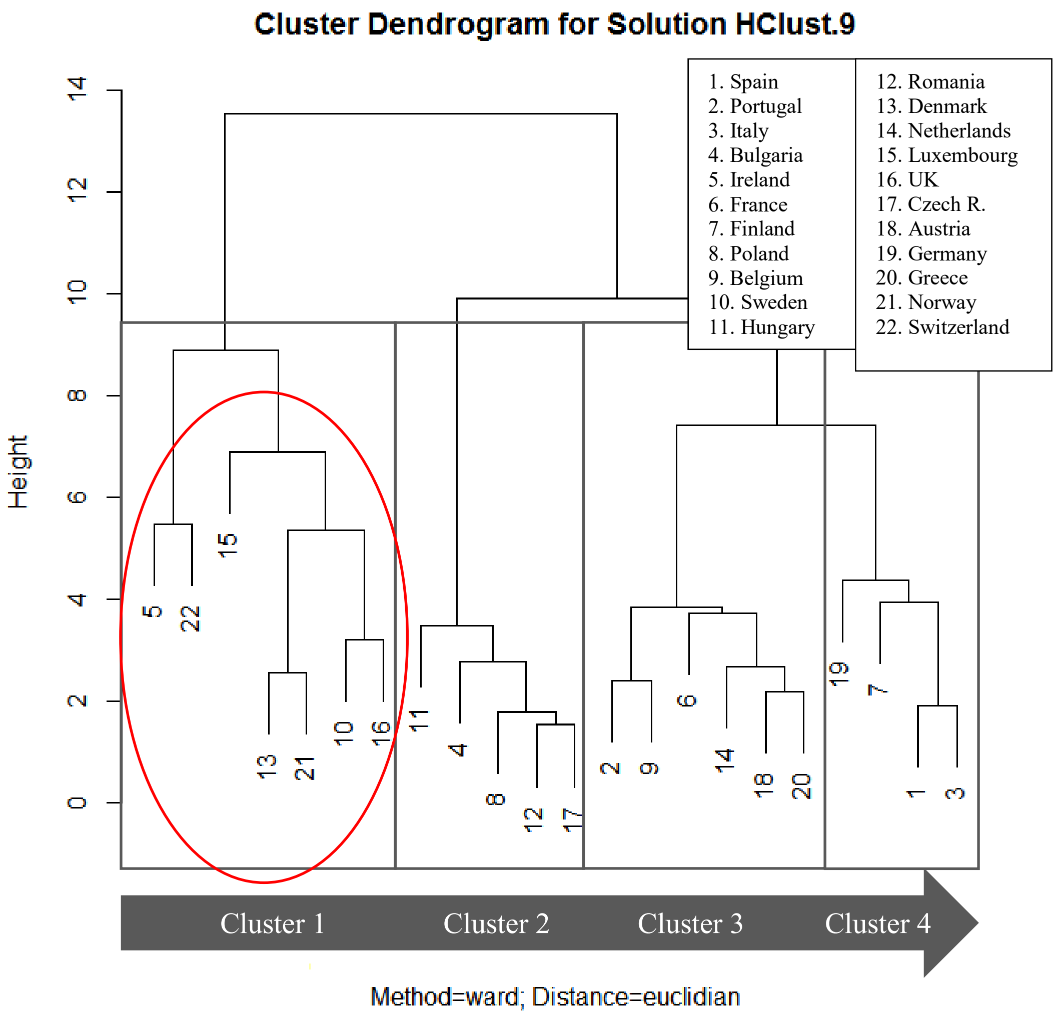
The finale of this detailed study presents the analysis of Venture Capital investments under consideration of the tax variables, the gross domestic product, the purchasing power standard and the fundraising. To be more specific:

- Gross Domestic Product per capita (GDPPC),
- Purchasing Power Standard (PPS),
- Fundraising per capita (FPC),
- Corporate income taxes in % (CITax%),
- Total corporate income taxes in % (TCITax%),
- Value added tax in % (VAT%),
- Capital gains tax max in % (CGtax%max),
- Capital gains tax min in % (CGtax%min),
- Withholding tax max in % (WHtax%max),
- Withholding tax min in % (WHtax%min).

The question to this investigation under consideration of all parameters (variables) has to be:

Which countries within the European Union and beyond are measurably successful in regards to Venture Capital investments and have such similiarities among each other that their conditions for optimized fiscal conditions may taken under consideration?

Figure 122: Per Capita VC Investments / all relevant Taxes



Source: Own representation created with Statistics R.

The dendrogram in figure 122, indicating the cluster merging process, suggests a stop at a level of approximately 9. This corresponds to a division into four clusters.

Other resolutions are possible, but not expedient for the planned tax optimization. All countries involved in cluster 1 have dominated in part during this investigation and have always had a close proximity to each other. Thus, it was stated that Ireland and Norway overall display a strong Venture Capital commitment and Luxembourg is showing a particularly strong willingness to invest in Venture Capital when it comes to domestic holding companies. Sweden, Denmark and Switzerland agree in regards to investment, also when it involves the consideration of capital gains tax. Great Britain is located, in each case, in the upper middle, in regards to the per capita Capital Venture investments; it joins in with Sweden in particular and the others mentioned in the overall context and therefore seems to do something right when it comes to investing in entrepreneurs.

4.4.4.4 Interim Conclusion III

Taking into account the capital gains tax, withholding tax, corporate income tax and value added tax, it has been shown that in regards to the fiscal framework especially the Scandinavian countries expose themselves, where they are being flanked by Luxembourg, Switzerland, and Great Britain. Of the three major economies which accounted for the largest share of the Private Equity transactions at the beginning of the investigation, only the United Kingdom remains as a traditional market for Private Equity and in particular for Venture Capital. Germany and France seem not to offer themselves to contribute to the development of an optimized tax regime in regards to Private Equity, respectively Venture Capital.

Ireland has earned the participation in the design recommendations in such a way that this country has, after its own crisis – up to EU aid – found means to return to good growth. This is confirmed by the now good gross domestic product per capita and is obviously owed to the strong commitment in companies. This commitment is to be observed particularly distinctively during the early phases of companies, so that at this point the relationship between the participation of companies in entrepreneurs and the growth of an economy is significantly noticeable. The goal of this paper is to create tax structures for a fund that holds universal validity for all investments in this segment. The target is to optimize those taxes, which are relevant on the level of a Private Equity fund in such a way that an average tax rate arises, promising a good investment readiness. In the design recommendations, those optimizations are being conducted.

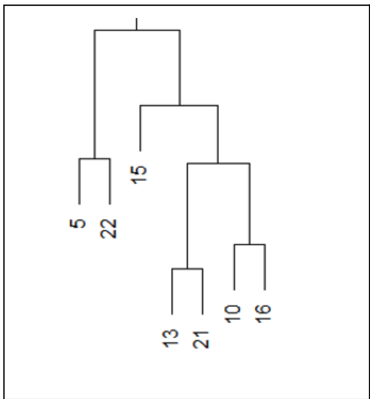
4.5 DESIGN RECOMMENDATIONS FOR A PRIVATE EQUITY FUND

4.5.1 **Preliminary Remarks**

The design recommendations for a tax-optimized Private Equity fund are principally targeted at determining the average tax rates at fund level and company level and to adjust them in such a way, that the desired result – namely, the creation of a tax-uniform fund, which has general validity throughout the European Union – occurs. In order to obtain the relevant data, those countries of the European Union were determined via a series of cluster analyses, which are similar in their behavior. For the derivation of design recommendations, the fiscal particularities, respectively, the fiscal framework at fund level and company level of the individual countries need to be taken into account, of which it can be expected that they will increase the economic growth in the European Union. The further this influence and the effect of the measures of fiscal adaptations are apart from each other, the more important, but also the more difficult is the anticipation of the relation between affect and effect. In addition, the expected relations could change over time of a Private Equity transaction, so that the expected effects are subject to change. Therefore, design recommendations need to have sufficient flexibility in order to be able to make necessary changes in design, if those are required and called for. So with the creation of a fund it must be observed for tax purposes, that average tax rates thus are changeable when the chosen national states change their tax rates or are no longer within the circle of those countries that hold a high level of similarities to each other. This could be counteracted through a binding commitment of states. The fund EUROPAEA is thereby rendered immune to changing trends such as intra-European changes. This focus of this study was to extract those countries that are similar in objective success, in spite of many different parameters. The design recommendations for a tax-efficient Private Equity fund are therefore focused to consolidate the best of the guild. It is expected that such an association will contribute to a positive development of the market, because it is certain that growth means to learn from others. If those countries with the best conditions for Venture Capital funding serving as a model, then the mixture of the best results in a – urgently needed – positive development of the market. In this respect, design approaches subsequently should be derived based on the theory-driven findings and empirical investigations – the situation itself should change – can be adjusted variably.

According to the last study unit, the following countries (figure 123) lend themselves to tax optimization:

Figure 123: Qualified Countries



5	- Ireland
10	- Sweden
13	- Denmark
15	- Luxembourg
16	- United Kingdom
21	- Norway
22	- Switzerland

Source: Own representation created with Statistics R.

The country codes are already listed elsewhere, but should be listed – only the eligible – again for clarity.

Norway and Switzerland will have to be left out of the design recommendations. There are no members of the European Union (EU). However, they form a common cluster with the above states of the EU with regard to the similarities in the investigation of Venture Capital investments.

4.5.2 Design Recommendation: Capital Gains Tax

Parameter Ireland

Ireland imposes capital gains tax of 33% on the sale of assets (Revenue, 2016, p. 1; Tipp, 2014, p. 19 et seqq.). A domestic investor agrees to pay the capital gains tax of 33%, if it is a direct investment or an investment with a transparent structure (EVCA, 2013, pp. 99-106; Revenue, 2016, p. 1; Tipp, 2014, 19 et seqq.). Another tax liability amounting to 36% is produced in a UCITS / QIF (EVCA, 2013, pp. 99-106; Revenue, 2016, p. 1; Tipp, 2014, 19 et seqq.). Non-domestic investors which invests in assets that are not income-taxable subjects have to pay the capital gains tax only on particular investments (EVCA, 2013, pp. 99-106; Revenue, 2016, p. 1; Tipp, 2014, 19 et seqq.). This includes the Irish real estate (EVCA, 2013, pp. 99-106; Revenue, 2016, p. 1; Tipp, 2014, 19 et seqq.).

If a holding corporation in a distributive group is holding a corporation not less than five percent of the capital stock for minimum one year, an exemption is possible for this participation, if certain terms are fulfilled (EVCA, pp. 99-106; Revenue, 2016, p. 1; Tipp, 2014, 19 et seqq.). This enables a company, having achieved a capital gain from the sale to realize the same without capital gains tax (EVCA, 2013, pp. 99-106; Revenue, 2016, p. 1; Tipp, 2014, 19 et seqq.). However, should the shares derive their price or the majority of their price from these investments as specified – be it directly or indirectly – they no longer qualify for this type of exemption (EVCA, 2013, pp. 99-106; Revenue, 2016, p. 1; Tipp, 2014, 19 et seqq.).

Parameter Sweden

Generally, all earnings realized by an internal investor are taxable with corporate income tax (Polster, 2016, p. 168 et seqq.) amounting to 22% (Polster, 2016, p. 168, et seqq.; EVCA, 2013, pp. 182-186). The Swedish law has created for shares in unlisted corporations an exemption stating that participation, profit on realization and all bonuses are tax-free (Polster, 2016, p. 168, et seqq.; EVCA, 2013, pp. 182-186). Swedish investors and foreign limited partnerships also benefit from this exemption (Polster, 2016, p. 168, et seqq.; EVCA, 2013, pp. 182-186). Capital gains of partnerships in the European Economic Area are exempt from tax, if they are held by a qualified investor (Polster, 2016, p. 168, et seqq.; EVCA, 2013, pp. 182-186). Capital gains are for partnerships in Sweden not always a tax problem. It achieves namely the partnership gains from the sale of its shares; these gains may be free from tax. The situation is similar with distributions, which a partnership received. (EVCA Tax Benchmark Study, 2013, pp. 182-186). They behave quite differently in terms of capital gains and dividends, in relation to the tax rules in Sweden for individuals. Although there are a number of special tax rules for certain types of taxpayers, normally a tax rate of 30 percent on income from above applies (EVCA, 2013, pp. 182-186). There are separate rules in this context of mutual funds and insurance (EVCA, 2013, pp. 182-186). Investors who do not come from Sweden and are not established there, but investing for capital gains there, are not subject to taxation (EVCA, 2013, pp. 182-186). These investors achieve beyond dividends, while the withholding tax must be paid (EVCA, 2013, pp. 182-186).

Parameter Denmark

Domestic institutional investors holding under ten percent of the shares in a listed company are being taxed (Schulze, 2014, p. 37 et seqq.) at a tax rate of 25% when selling the shares (Schulze, 2014, p. 37 et seqq.; EVCA, 2013, pp. 60-64). The sale of unlisted shares is tax-free (Schulze, 2014, p. 37 et seqq.; EVCA, 2013, pp. 60-64). For a Danish investor, the tax debt will not change if the profit is not obtained from an immediate investment, but from an engagement in a Danish internal or external fund, which is tax-transparent, and allocates the receipts of the profits to the Danish investor (Schulze, 2014, p. 37 et seqq.; EVCA, 2013, pp. 60-64).

Parameter Luxembourg

The capital gains tax parameter in Luxembourg have already been dealt with in chapter in 3.6.4 and in 4.4.4.1 and are not to be summarized again at this point. It should be recalled, that Luxembourg has no special tax of this kind.

It is possible that the profit on realization achieved by residential or non-residential investors in Luxembourg will be succumbed to income tax or corporation tax (Fort, 2014, p. 21 et seqq.; Merten, 2004, p. 48 et seqq.; Höhn & Höring, 2010, p. 172 et seqq.; EVCA, 2013, pp. 124-132). Generally, the taxation characteristics of the state of domicile of the participator are being relegated to, if the nonlocal participator has his tax domicile in a state that has a double-tax arrangement with Luxembourg (Fort, 2014, p. 21 et seqq.; Merten, 2004, p. 48 et seqq.; Höhn & Höring, 2010, p. 172 et seqq.; EVCA, 2013, pp. 124-132). If the external participator has his fiscal residence in a country not holding a double taxation agreement with Luxembourg, the profit on realization kept from the disposal of participations in a Luxembourgian corporation are assessable in the inland, if the non-residential shareholder holds a participation in a Luxembourgian company of ten percent or more and if the participator has again sold the participations within a distance of half a year after the acquisition or the investor has a fiscal residency over fifteen years (Fort, 2014, p. 21 et seqq.; Merten, 2004, p. 48 et seqq.; Höhn & Höring, 2010, p. 172 et seqq.; EVCA, 2013, pp. 124-132).

Profit on realization from an assessable company, which has its residency in Luxembourg, are generally succumbed to corporate taxes (Fort, 2014, p. 21 et seqq.; Merten, 2004, p. 48 et seqq.; Höhn & Höring, 2010, p. 172 et seqq.; EVCA, 2013, pp. 124-132). The rate is consolidated and has an amount of 29,22 percent (Fort, 2014, p. 21 et seqq.; Merten, 2004, p. 48 et seqq.; Höhn & Höring, 2010, p. 172 et seqq.; EVCA, 2013, pp. 124-132). This tax rate is calculated by the corporate tax of 21% and the contract for unemployment fund for corporate tax 1.07% and trade tax of 7% (Fort, 2014, p. 21 et seqq.; Merten, 2004, p. 48 et seqq.; Höhn & Höring, 2010, p. 172 et seqq.; EVCA, 2013, pp. 124-132). Profit on realization of these companies may be free from corporate income tax and trade tax (Fort, 2014, p. 21 et seqq.; Merten, 2004, p. 48 et seqq.; Höhn & Höring, 2010, p. 172 et seqq.; EVCA, 2013, pp. 124-132).

Parameter United Kingdom

ELPs (English Limited Partnerships) and SLPs (Scottish Limited Partnerships) are usually transparent in the sense of the British taxation of income (Alberts, 2014, p. 34 et seqq.) and capital gains (Alberts, 2014, p. 34 et seqq.; EVCA, 2013, pp. 194-201). Investors are being taxed addicted on the kind of the profits of the fund (Alberts, 2014, p. 34 et seqq.; EVCA, 2013, pp. 194-201). British corporations and also private persons – are subject to capital gains tax (Alberts, 2014, p. 34 et seqq.; EVCA, 2013, pp. 194-201). In essence, the British taxation does not distinguish between individuals and companies, however, individuals are as opposed to companies directly charged with capital gains taxes (Alberts, 2014, p. 34 et seqq.; EVCA, 2013, pp. 194-201). United Kingdom companies are liable for corporate income tax (Alberts, 2014, p. 34 et seqq.; EVCA, 2013, pp. 194-201). This is collected at the relevant tax rate (Alberts, 2014, p. 34 et seqq.; EVCA, 2013, pp. 194-201). In 2013, the relevant tax rates amounted to 24% for large corporations and 20% for small enterprises (Alberts, 2014, p. 34 et seqq.; EVCA, 2013, pp. 194-201). In April 2014, this tax rate was reduced to 21% and in April 2015 (Polster, 2016, p. 163) to 20% (Alberts, 2014, p. 34 et seqq.; EVCA, 2013, pp. 194-201; Polster, 2016, p. 163).

Certain items, like British pension funds are free from the assessment of taxable gains (Alberts, 2014, p. 34 et seqq.; EVCA, 2013, pp. 194-201). Contingent on the circumstances, British investors keeping shares of minimum ten percent in a company over a distance of minimum one year may suitable for tax-exemption of profits (Alberts, 2014, p. 34 et seqq.; EVCA, 2013, pp. 194-201).

For individual British partipants, profits on realization are not to be treated with the identical tax rate as dividends (Alberts, 2014, p. 34 et seqq.; EVCA, 2013, pp. 194-201). Also, from the situation, earnings from distributions may be free from taxes for British institutional investors (Alberts, 2014, p. 34 et seqq.; EVCA, 2013, pp. 194-201). This income would be burdened with the tax rate of the corporation, if this income would not be exempt (Alberts, 2014, p. 34 et seqq.; EVCA, 2013, pp. 194-201). In addition, no municipal, local, social or business tax in the sense of the British fiscal law is levied on taxable profits (Alberts, 2014, p. 34 et seqq.; EVCA, 2013, pp. 194-201).

Design Recommendations

As already noted earlier, the taxation of capital gains shows distinct differences. In order to obtain a uniform tax rate, the capital gains taxes of those member states of the European Union that have offered themselves suitable after the in-depth investigation - thus, Ireland, Sweden, Denmark, Luxembourg, and Great Britain – were determined, added and divided by the number of positions. In this – to obtain a representative average – the maximum and minimum tax rates have been recorded.

Considering all capital gains tax of these countries, a tax rate of 14.288% has been determined (table 10). In order to obtain an average willingness to invest, this results in a recommended tax rate of 14.29% for the assessment of capital gains. At this point, the investments per capita industry statistic and their positions in inter-European comparison (EU) in Venture Capital of domestic affiliated companies are included as an example.

Table 10: Capital Gains Taxes of the qualified Countries in %

	Capital Gains Tax max.	Capital Gains Tax min.	IISVCpc	Pos.
Ireland	33.33	33,33	19.17 €	4
Sweden	22.00	0.00	15.40 €	7
Denmark	25.00	0.00	51.28 €	2
Luxembourg	29.22	0.00	73.35 €	1
United Kingdom	0.00	0.00	12.86 €	9
Interim result	109.55	33.33	164.70 €	
Total	142.88			
On average	14.288		34.41 €	4,6

Source: Owen representation.

4.5.3 Design Recommendations: Withholding Tax

Parameter Ireland

Ireland imposes withholding taxes in the amount of 20% on dividends (Tipp, 2014, p. 26 et seqq.), interest and licence fee (Tipp, 2014, p. 26 et seqq.; EVCA, 2013, pp. 99-106). There is a quantity of exonerations from tax for non-residential companies regarding the withholding tax (Tipp, 2014, p. 26 et seqq.; EVCA, 2013, pp. 99-106). This is particularly applicable for in Ireland non-resident companies holding their residency in a state with which the inland has entered a double-tax arrangement (Tipp, 2014, p. 26 et seqq.; EVCA, 2013, pp. 99-106). Ireland may well be regarded as the surprise in this study. The strong venture capital commitment and the high per capita domestic product shows that they do things right. This correlates in most cases with good and manageable control agreements. Those companies – non-resident – can usually retrieve the withholding tax on dividends in their country of residence, provided that the company in question is not being controlled by an Irish corporation (Tipp, 2014, p. 26 et seqq.; EVCA, 2013, pp. 99-106). The same applies, if the control is with a company listed at a recognized stock exchange (Tipp, 2014, p. 26 et seqq.; EVCA, 2013, pp. 99-106).

In case those withholding taxes are being imposed in the context of payments to transparent companies, for example a limited partnership, problems in retrieving the tax may occur (Tipp, 2014, p. 26 et seqq.; EVCA, 2013, pp. 99-106). Further taxes on outbound payments do not exist in Ireland (Tipp, 2014, p. 26 et seqq.; EVCA, 2013, pp. 99-106).

Parameter Sweden

Sweden appears to be more balanced than Ireland. Nevertheless, this country also shows strong efforts in venture capital and presents itself otherwise very well. That apparently works even if the withholding tax is higher. Sweden levies a withholding tax of 30 percent on dividends of foreign investors (EVCA, 2013, pp. 182-186). For income from interest, the tax is not applicable (EVCA, 2013, pp. 182-186). In cooperation with other countries of the European Union thes taxes are often not charged. Due to the fact that the withholding tax may be reduced or omitted entirely on double-tax agreement, the high rate is relativized (EVCA, 2013, pp. 182-186).

Parameter Denmark

Dividend income (boerse.de, 2016) is succumed to a withholding tax of 27 percent (EVCA, 2013, pp. 60-64). However, a withholding tax of 25% may be levied on certain Danish investors (EVCA, 2013, pp. 60-64). It is possible, that 15% of these taxes can be retrieved, if an individual request is made at investor level (EVCA, 2013, pp. 60-64). If the Danish tax authorities agree, a reduction at source is possible (EVCA, 2013, pp. 60-64). The Danish Tax Law provides that companies that hold at least ten percent of the capital of a Danish company, not be burdened with the withholding tax (EVCA, 2013, pp. 60-64). The prerequisite is that the company that obtains this revenue has a tax agreement with Denmark (EVCA, 2013, pp. 60-64). The companies from the countries in the European Union basically fall under this regulation, shows that the outstanding efforts regarding venture capital in Denmark are not limited to the national territory (EVCA, 2013, pp. 60-64).

However, Denmark supports some particularities of withholding tax. For example, interest could arise from a loan that was awarded within a company, which is subject to such tax (EVCA, 2013, pp. 60-64). When considering these guidelines and agreements, it is possible that the tax burden may fall to zero percent (EVCA, 2013, pp. 60-64). Such regulations have simpler provisions, which can help the Venture Capital industry. These simplified rules can help the entrepreneurs as well.

Parameter Luxembourg

If a Luxembourgian company is paying dividends, these dividends are in principle subject to a dividend (Lipp, 2014, p. 269 et seqq.) withholding tax rate of fifteen percent (EVCA, 2013, pp. 124-132). This tax rate may be reduced by an applicable double taxation agreement or are subject to the participation exemption of Luxembourg (Fort, 2014, p. 48 et seqq.).

The exemption from withholding tax in Luxembourg is dependent on several conditions. Dividends from unlimited taxable corporations reduce this burden when (EVCA Tax Benchmark Study, 2013, pp. 124-132):

- the respective company has its headquarters in a European Union country and falls under Article 2 of the EU Parent-Subsidiary Directive[15] (European Commission, 2015). This also applies to companies, which are taxable in Luxembourg. Moreover, that is applicable in limited companies whose seat

[15] Council Directive 2003/123/EC of December 2003 amending Directive 90/435/EEC on the common system of taxation applicable in the case of parent companies ans subsidiaries of different Member States. It is essentially a matter for Member States to notify the Commission of their national laws.

lies in a country within the European Economic Area (including Switzerland). In addition, there are special agreements with countries that have similar tax regulations in their country. Smaller companies are unfortunately not addressed here,

- the respective company has a minimum ten percent share (this does not apply if the acquisition value exceeds 1.2 million euros) on a tax-transparent company,
- or the respective company holds the participation without interruption for a period of at least one year (EVCA, 2013, pp. 124-132).

As opposed to a SIF (Dietrich & Müller, 2016, p. 221 et seqq.), the entitlement to dividends from a company fully taxable in Luxembourg are free from withholding tax on dividends with a SICAR (Dietrich & Müller, 2016, p. 221 et seqq.), if the minimum requirement for the investment income taxation are fulfilled (EVCA, 2013, pp. 124-132).

With insecurities about the soaking time, it is feasible to raise the mandatory withholding tax and seek reimbursement later, if the at least soaking time (Mach, 2008, p. 111 et seqq.) has actually been fulfilled because the distribution has been disbursed (EVCA, 2013, pp. 124-132).

If the Luxembourgian fund structures SIF or SICAR distribute money, then those revenues mostly are not subject of the withholding tax (EVCA, 2013, pp. 124-132). In this case, it does not matter where the company that gets money, has its headquarters (EVCA, 2013, pp. 124-132).

Local companies that do not have interest income are not subject to this tax (EVCA, 2013, pp. 124-132). Exceptions are the revenues from profit sharing bonds and payments to silent shareholders (EVCA, 2013, pp. 124-132). Furthermore, constructive dividends must be taxed (EVCA, 2013, pp. 124-132). The tax rate is then fifteen percent (EVCA, 2013, pp. 124-132). But also in this case is a reduction in control conceivable (EVCA, 2013, pp. 124-132), which is always the case when there are agreements with the respective countries (EVCA, 2013, pp. 124-132). For covert dividend, there is the possibility to get on the box privilege Luxembourg advanteges (Fort, 2014, p. 48 et seqq.) This instrument is partly responsible for the popularity of Luxembourg as a financial location (Schaffner, 2007, p. 1).

Although Luxembourg is considered the motherland of private equity in Europe, there are a lot of regulations. Thus Luxembourg is subject to the provisions of chapter 3 of the EU Savings Directive 2003/48/EC (Kudert & Kopec, 2014, p. 1), the aim of which is, taxing income from interest payments effectively taxing (EVCA, 2013, pp. 124-132). Special constructions like paying agents must pay tax on income from interest in Luxembourg (EVCA, 2013, pp. 124-132). After the legal situation of the investigation from the EVCA (2013) dividends distributed by SIF or SICAR, are not subject by this directive (EVCA, 2013, pp. 124-132). However, fonds commun de placement are at risk and could under certain conditions fall under this taxation (EVCA, 2013, pp. 124-132).

With the Luxembourgian law of December 23, 2005 (Spuerkeess, 2015, pp. 1-19), a withholding tax of 10% was imposed on interest income made by Luxembourg paying agents to Luxembourg-established resident individuals (EVCA, 2013, pp. 124-132).

It should also be noted that companies do not have to pay taxes for licensing fees (Jarass & Obermair, 2015, p. 70 et seqq.). It is noteworthy, that remunerations of members of a supervisory board or the directors of a supervisory board are subject to a withholding tax of 20% (EVCA, 2013, pp. 124-132).

Parameter United Kingdom

Great Britain is the largest volume Private Equity market in the European Union and in Europe. As the exit of Britain affects this market and how the tax parameters react remains to be seen.

Should corporations in Great Britain distribute dividends, the receiver shall not expect that withholding tax is charged initially. (Alberts, 2014, p. 60 et seqq.). However, a tax rate (Alberts, 2014, p. 60 et seqq.; EVCA, 2013, pp. 194-201) applies to distributions under the UK Real Estate Investment Trusts (REITs). On certain royalties, a tax rate of 20% may be applied (Alberts, 2014, p. 60 et seqq.; EVCA, 2013, pp. 194-201). This includes patents and some copyrights (Alberts, 2014, p. 60 et seqq.; EVCA, 2013, pp. 194-201). All proceeds from bank loans are provided with a tax rate of 20 percent (Alberts, 2014, p. 60 et seqq.; EVCA, 2013, pp. 194-201). This 20% also applies to interest income from corporate bonds (Alberts, 2014, p. 60 et seqq.; EVCA, 2013, pp. 194-201). The United Kingdom makes an exception (2013) for interest income from qualified Euro bonds, these bonds are tax-free (Alberts, 2014, p. 60 et seqq.; EVCA, 2013, pp. 194-201). A tax rate of 20% is available for interest income on bank deposits (Alberts, 2014, p. 60 et seqq.; EVCA, 2013, pp. 194-201). It may be stated that the UK takes control of 20 percent, where it is not free, while the same goes for income from the rental of buildings or other objects (Alberts, 2014, p. 60 et seqq.; EVCA, 2013, pp. 194-201). However, this remains limited to nonlocal companies (Alberts, 2014, p. 60 et seqq.; EVCA, 2013, pp. 194-201).

Although there are a number of regulations that classify the tax, it is equally feasible that corporations are free from withholding tax (Alberts, 2014, p. 60 et seqq.; EVCA, 2013, pp. 194-201). This could be done through national law or through agreements with the concernced countries (Alberts, 2014, p. 60 et seqq.; EVCA, 2013, pp. 194-201).

Design Recommendations

The withholding taxes in the states of the European Union are also assessed quite differently (EVCA, 2013). There are fluctuations noted ranging from no taxes at all, over a variety of design options to tax rates above 30% (EVCA Tax Benchmark Study, 2013). In order to obtain a uniform tax rate, the withholding taxes of those member states of the European Union that have offered themselves suitable after the in-depth investigation – thus, Ireland, Sweden, Denmark, Luxembourg, and Great Britain – were determined, added, and divided by the number of positions. In this – to obtain a representative average – the maximum and minimum tax rates have been recorded.

Considering all withholding taxes of these countries, a tax rate of 14.60% has been determined. Calculation: all withholding taxes – minimum and maximum – of the five countries, give a factor of 146.00%, divided by 10 (five maximum withholding taxes and five minimum withholding taxes), gives an average tax rate of 14.60%. In order to obtain an average willingness to invest (all investments in Venture Capital per capita = 81.06 € divided by 5 = an average investment of 16.21 € per capita), this results in a recommended tax rate of 17.90% for the taxation at source.

Table 11: Withholding Taxes of the qualified Countries in %

	Whtax max	Whtax min	IMSVCpc	Pos.
Ireland	36.00	0.00	16.36 €	4
Sweden	30.00	0.00	16.72 €	3
Denmark	25.00	0.00	13.75 €	5
Luxembourg	35.00	0.00	9.57 €	12
United Kingdom	20.00	0.00	13.25 €	6
Interim result	146.00	0.00	69.65 €	
Total		146.00		
On average		14.60	13.93 €	6.0

Source: Own representation.

At this point, the investments and their positions in inter-European comparison (EU) in Venture Capital of domestic affiliated companies are included as an example.

4.5.4 Design Recommendations: Company Tax

Parameter Ireland

The corporation tax rate (Tipp, 2014, p. 34 et seqq.; Lorenz, 2014, p. 152 et seqq.) for trading activities of the companies is 12.5% (Tipp, 2014, p. 34 et seqq.; Lorenz, 2014, p. 152 et seqq.; EVCA, 2013, pp. 99-106). Income that is not due to the original activities of the company will be taxed at 25% (Tipp, 2014, p. 34 et seqq.; Lorenz, 2014, p. 152 et seqq.; EVCA, 2013, pp. 99-106). Examples include rental income, capital gains or interest income (Tipp, 2014, p. 34 et seqq.; Lorenz, 2014, p. 152 et seqq.; EVCA, 2013, pp. 99-106). In certain cases, there is a surcharge of 20% (Tipp, 2014, p. 34 et seqq.; Lorenz, 2014, p. 152 et seqq.; EVCA, 2013, pp. 99-106). Dividends paid between two Irish companies (Tipp, 2014, p. 34 et seqq.; Lorenz, 2014, p. 152 et seqq.; EVCA, 2013, pp. 99-106) are free from corporate income tax (CIT). There are a number of different types of gains. Depending on the kind, the domestic company makes profits and will turn the tax burden for the company when it receives income from dividends from abroad (Tipp, 2014, p. 34 et seqq.; Lorenz, 2014, p. 152 et seqq.; EVCA, 2013, pp. 99-106). Dividends from trading profits are taxed at 12.5% (Tipp, 2014, p. 34 et seqq.; Lorenz, 2014, p. 152 et seqq.; EVCA, 2013, pp. 99-106). When these incomes are not from trading profits, the tax rate amount to twenty-five percent (Tipp, 2014, p. 34 et seqq.; Lorenz, 2014, p. 152 et seqq.; EVCA, 2013, pp. 99-106). Somewhat more complicated is the treatment of the so-called portfolio dividends. These distributions come from a holding in a company that is less than five percent. Conditions for an exemption for these distributions is that this company either comes from an EU member state, or has other tax agreements with Ireland (Tipp, 2014, p. 34 et seqq.; Lorenz, 2014, p. 152 et seqq.; EVCA, 2013, pp. 99-106).

The local authorities in Ireland impose a little fee adapted from the area and the location of the business premises (Tipp, 2014, p. 34 et seqq.; Lorenz, 2014, p. 152 et seqq.; EVCA, 2013, pp. 99-106). With the exception of local property taxes, no other taxes are levied besides these taxes (Tipp, 2014, p. 34 et seqq.; Lorenz, 2014, p. 152 et seqq.; EVCA, 2013, pp. 99-106). Like almost everywhere property taxes are also levied (Tipp, 2014, p. 34 et seqq.; Lorenz, 2014, p. 152 et seqq.; EVCA, 2013, pp. 99-106). This tax is calculated in Ireland on the value of the building or dwelling, the market is currently willing to pay (Tipp, 2014, p. 34 et seqq.; Lorenz, 2014, p. 152 et seqq.; EVCA, 2013, pp. 99-106).

Parameter Sweden

Corporate income tax is being levied with a flat rate of 22% (EVCA, 2013, p. 184; Berndt, Fantapié Altobelli, & Sander, 2016, p. 40 et seqq.).

Parameter Denmark

In Denmark, a corporation tax of 25% is being applied (Schulze, 2014, p. 61/1 et seqq.; Berndt, Fantapié Altobelli, & Sander, 2016, p. 40 et seqq.). There are no further municipal, local, social or business taxes (Schulze, 2014, p. 61/1 et seqq.; EVCA,

p. 60-64). There is no special tax rate for small or medium-sized enterprises (SME), which are defined according to the EU legislation or for other small enterprises according to other criteria (Schulze, 2014, p. 61/1 et seqq.; EVCA, 2013, p. 60-64).

Parameter Luxembourg

The total corporate tax rate (Dietrich & Müller, 2016, p. 221 et seqq.; EVCA, 2013, p. 124-132; Fort, 2014, p. 43 et seqq.), including trade tax (Fort, 2014, p. 43 et seqq.), in Luxembourg is 29.22% (corporate income tax base 21%, plus employment fund surcharge 1.47%, plus municipal business tax 6.75%, see below). There is an allowance of 17.500 euros and for tax transparent corporations 40.000 euros to be removed from the basis for the dimensioning of the control (Dietrich & Müller, 2016, p. 221 et seqq.; EVCA, 2013, p. 124-132; Fort, 2014, p. 43 et seqq.).

The tax rate from above is calculated from different parts (Dietrich & Müller, 2016, p. 221 et seqq.; EVCA, 2013, p. 124-132; Fort, 2014, p. 43 et seqq.). On the one hand, to the corporation tax itself and on the other side from a kind of pension fund (Dietrich & Müller, 2016, p. 221 et seqq.; EVCA, 2013, p. 124-132; Fort, 2014, p. 43 et seqq.). Moreover, Luxembourg is considered one of the only countries in the world and European Union that elevates trade taxes (Dietrich & Müller, 2016, p. 221 et seqq.; EVCA, 2013, p. 124-132; Fort, 2014, p. 43 et seqq.). A prominent example of the elevation of commercial control is Germany (Dietrich & Müller, 2016, p. 221 et seqq.; EVCA, 2013, p. 124-132; Fort, 2014, p. 43 et seqq.). In Luxembourg, there is a 21 percent (Dietrich & Müller, 2016, p. 221 et seqq.; EVCA, 2013, p. 124-132; Fort, 2014, p. 43 et seqq.) corporation tax (if the base is less than 15.000 euros). If this value is higher, this rate drops to 20 percent (Dietrich & Müller, 2016, p. 221 et seqq.; EVCA, 2013, p. 124-132; Fort, 2014, p. 43 et seqq.). The payment to the pension fund is calculated from corporation tax (7 percent of the corporation tax) and trade tax amounts to 6.75 percent (Dietrich & Müller, 2016, p. 221 et seqq.; EVCA, 2013, p. 124-132; Fort, 2014, p. 43 et seqq.).

The lowest tax is 3.000 euros, which – together with the fund of 7% - adds up to 3.210 euros (Dietrich & Müller, 2016, p. 221 et seqq.; EVCA, 2013, p. 124-132; Fort, 2014, p. 43 et seqq.). This applies to companies whose assets consist of more than 90% of financial assets, intercompany receivables, cash and cash equivalents, bank balances and bank deposits (Dietrich & Müller, 2016, p. 221 et seqq.; EVCA, 2013, p. 124-132; Fort, 2014, p. 43 et seqq.). Nevertheless, if companies are not included in the area of application, then the have to pay at least 500-20.000-euro tax depending on the corporate valuation (Dietrich & Müller, 2016, p. 221 et seqq.; EVCA, 2013, p. 124-132; Fort, 2014, p. 43 et seqq.). Elvinger, Hoss & Prussen (2012, p. 1) comment on the recent Luxembourgian law-environment to the effect that the carrying value of investments whose returns are not taxed in Luxembourg (Dietrich & Müller, 2016, p. 221 et seqq.; EVCA, 2013, p. 124-132; Fort, 2014, p. 43 et seqq.) are found in accordance with the applicable concluded by Luxembourg double-tax arrangement, that the minimum CIT does not apply (pwc, 2012, pp. 1-2). The minimum CIT represents a tax prepayment for future fiscal years. A tax refund is not provided, rather a tax credit is granted (Dietrich & Müller, 2016, p. 221 et seqq.; EVCA, 2013, p. 124-132; Fort, 2014, p. 43 et seqq.).

Parameter United Kingdom

The main tax rate of the corporation tax was 24% with effect of April 1, 2012 (Kania, 2013, p. 177 et seqq.; Alberts, 2014, p. 65 et seqq.; Rödl & Partner, 2015, pp. 1-82). This rate was reduced to 23% effective on April 1, 2013 (Kania, 2013, p. 177 et seqq.; Alberts, 2014, p. 65 et seqq.; EVCA, 2013, pp. 194-201; Rödl & Partner, 2015, pp. 1-82). This rate was again reduced to 21% on April 1, 2014. On April 1, 2015 (Schmidt-Soltau & Altmann, 2016, pp. 1-26), this rate was again reduced to 20% (Kania, 2013, p. 177 et seqq.; Alberts, 2014, p. 65 et seqq.; EVCA, 2013, pp. 194-201; Rödl & Partner, 2015, pp. 1-82).

Companies with a converted profit over 1.7 million euros are succumbed to the basis rate of these tax (Kania, 2013, p. 177 et seqq.; Alberts, 2014, p. 65 et seqq.; EVCA, 2013, pp. 194-201). Small enterprises, balancing a profit of less than 350.000 euros are succumbed to the rate of twenty percent (Kania, 2013, p. 177 et seqq.; Alberts, 2014, p. 65 et seqq.; EVCA, 2013, pp. 194-201). The threshold of 1.7 million euros and 350.000 euros reduced itself according to the quantity of aggregated corporations in that group (Kania, 2013, p. 177 et seqq.; Alberts, 2014, p. 65 et seqq.; EVCA, 2013, pp. 194-201).

Companies, making a profit between 300.000 and 1.5 million pounds are bound to the main tax rate and can undergo minor tax relief (Kania, 2013, p. 177 et seqq.; Alberts, 2014, p. 65 et seqq.; EVCA, 2013, pp. 194-201).

As in Ireland and in the UK there are no efforts to secure additional revenues from communal taxes or business taxes. (Kania, 2013, p. 177 et seqq.; Alberts, 2014, p. 65 et seqq.; EVCA, 2013, pp. 194-201).

Design Recommendations

The company taxes in the countries of the European Union are also assessed quite differently. There are fluctuations noted ranging from no taxes at all, over a variety of design options to tax rates above 30%. In order to obtain a uniform tax rate, the company taxes of those member states of the European Union that have offered themselves suitable after the in-depth investigation – thus, Ireland, Sweden, Denmark, Luxembourg, and Great Britain – were determined, added and divided by the number of positions. In this – to obtain a representative average – the maximum and minimum tax rates have been recorded.

Table 12: Company Taxes of the qualified Countries in %

	TCITax min.	TCITax max.	IMSVCpc	Pos.
Ireland	12.50	25.00	16.36 €	4
Sweden	22.00	22.00	16.72 €	3
Denmark	25.00	25.00	13.75 €	5
Luxembourg	28.15	29.22	9.57 €	12
United Kingdom	20.00	20.00	13.25 €	6
Interim result	107.65	121.22	69.65 €	
Total	228.87			
On average	22.887		13.93 €	6.0

Source: Own representation.

Considering all company taxes of these countries, a tax rate of 22.887% has been determined. In order to obtain an average willingness to invest, this results in a recommended tax rate of 22.89% for the taxation at source. At this point, the investments and their positions in inter-European comparison (EU) in Venture Capital of domestic affiliated companies are included as an example.

Design Recommendation: Summary

If the design recommendations are summarized, the result shown in table 13 present themselves.

Table 13: Summary Tax Rates

	Capital Gains Tax in % max.	Capital Gains Tax in % min.
Ireland	33.33	33.33
Sweden	22.00	0.00
Denmark	25.00	0.00
Luxembourg	29.22	0.00
United Kingdom	0.00	0.00
Interim result	109.55	33.33
Total	142.88	
On average	14.288	

	TCITax in % min.	TCITax in % max.
Ireland	12.50	25.00
Sweden	22.00	22.00
Denmark	25.00	25.00
Luxembourg	28.15	29.22
United Kingdom	20.00	20.00
Interim result	107.65	121.22
Total	228.87	
On average	22.887	

	Whtax max in %	Whtax min in %
Ireland	36.00	0.00
Sweden	30.00	0.00

Denmark	25.00	0.00
Luxembourg	35.00	0.00
United Kingdom	20.00	0.00
Interim result	146.00	0.00
Total		146.00
On average		14.60

Source: Own representation.

If, in regards to the taxable management fees, the sales tax rates (VAT) would be taken into consideration as well, the average value would amount to 24.00% (Sweden 25.00% and Ireland 23.00% = 48.00/2 = 24.00%). However, this average value is not representative, as Luxembourg, Denmark and the United Kingdom to not impose sales tax on management fees, while Ireland and Sweden certainly do raise this tax.

At tax rates of 14.29% capital gains tax, 14.60% withholding tax and a company tax of 22.89%, the below shown, statistical values are being expected. In that, a wholly owned dependence of the investments, the gross domestic product and the purchasing power are being assumed. This, of course, is not the case. However, a tendency can be deduced from these figures, since the taxes do influence the gross domestic product, and the gross domestic product is significantly involved in the willingness to invest in Venture Capital.

Table 14: Average Figures Investments, GDP and PPS

	IISVCpc in €	Pos.	IMSVCpc in €	Pos.
Ireland	19.17	4	16.36	4
Sweden	15.40	7	16.72	3
Denmark	51.28	2	13.75	5
Luxembourg	73.35	1	9.57	12
United Kingdom	12.86	9	13.25	6
Total	172.06	23	69.65	30
On average	34.41	4,6	13.93	6.0

	GDPpc in €	Pos.	PPS	Pos.
Ireland	46.200	4	145	4
Sweden	45.400	6	123	9
Denmark	45.900	5	124	8
Luxembourg	91.600	1	271	1
United Kingdom	39.500	8	110	11
Total	268.600	24	773	33
On average	53.720	4.8	154.6	6.6

	IISVC/GDP	Pos.	IMVC/GDP	Pos.
Ireland	0.04%	3	0,04%	2
Sweden	0.03%	4	0,04%	1
Denmark	0,11%	1	0,03%	3
Luxembourg	0,08%	2	0,01%	5
United Kingdom	0,03%	5	0,03%	4
Total	0,29%	15	0,15%	15
On average	0,0599%	3	0,0292%	3

		Total Pos.	Total Inv.pc	Pos.
Ireland		5	0.0769%	2,5
Sweden		5	0.1047%	2,5
Denmark		4	0.1416%	2
Luxembourg		7	0.0905%	3,5
United Kingdom		9	0,0661%	4,5
Total		30	0,4459%	
On average		6	*0,0891%*	

Source: Own representation.

In view of the overall economic growth, the permanent deployment of about 0,09% of gross domestic product (GDP) in Venture Capital investments is necessary to increase the wealth of nations within the European Union (EU). Denmark and Sweden have exposed themselves in such a way, that they – on a national basis – could be further leading the way in the future.

The investigation extracted those countries, which essentially show the most similarities to each other regarding the willingness to invest in the context of Private Equity and Venture Capital in particular under consideration of the gross domestic product per capita and the relevant taxes. Average figures were determined. It makes sense, that for portfolio companies from a country with a low purchasing power, a set of harmonized tax is not necessarily helpful, if the money for the investment is not available. It is conceivable to make an adjustment within the meaning of the code. This figure could be a kind of distribution key for the Member States. To achieve this goal – an equal per capita domestic product in all countries – the states have been paying into these "relief fund for investment" in accordance with this allocation. The countries that received the money have to repay this investment help. The repayment of this money is interest and tax-free or adapted to the particular key interest rate. If that is the care, it can be expected that the growth rate of the national markets, with the support of the European market, will be higher than the actual key interest rate, resulting in a steady approximation of the economic wealth of the individual states.

4.5.5 Impact on Investment Companies, Gross Domestic Product and Investment Behavior

If, therefore, approximately 0,09% of the gross domestic product is invested in venture capital, then a gross domestic product per capita of 53.720,00 euros and a purchasing power standard of 154,6 (reference size, as stated, is 100) can be expected under the new tax conditions, ie the "FUND EUROPAEA". In order to look at the hypotheses from the chapters 2.1.2.5 and 4.1, they are listed here again.

If there are better tax conditions for venture capital, the interest of investment companies in venture capital will also increase. Therefore, there will be more venture capital companies.

The total GDP per capita of the 22 countries studied amounted to 759.000 euros. If this sum is divided by 22, an average gross domestic product of 34.527,27 euros is obtained. If this sum is compared with the per capita GDP, the expected gross domestic product per capita of 53.720,00 euros under the new tax conditions (with permanent application) forces one to recognize the potential that also exists for investment companies. It is assumed that this domestic product is dependent on the accumulated money (it is because this accumulated money is related to the investments which, according to GDP, are the result of a higher GDP, BIP = C + I + G + Ex-Im), then the factor would be 1,56 (53.720,00 / 34.527,27), and thus, the factor for fundraising could go up. This means that the collected money would increase from 87,35 euros (see chapter 2.1.2.5) to 135,91 euros (87,35 * 1,56). At the same time, the number of participating companies would also increase by at least a factor of 1,56. However, since the tax conditions were preferably extracted for the "FUND EUROPAEA", an increase of especially the venture capital companies is to be expected. This would be equivalent to a shift of the current fundraising ratio of 87,35 euros per capita, of which 22,30 euros is spent on venture capital investments in the countries included in this study.

If the tax conditions for venture capital are optimized, gross domestic product per capita increases. If the gross domestic product per capita rises, the gross domestic product rises as well.

Thus, if the gross domestic product (GDP) per capita increases as a result of the new tax conditions for venture capital, the gross domestic product also increases correspondingly. The new GDP per capita amounts to 53.720,00 euros. If this number is multiplied by 22, you get 1.181.840,00 euros. This is the total gross domestic product per capita of the countries included in this study; this is a significant increase compared to the 790.000,00 euros from above. This means that the total gross domestic product of the European Union would rise from 1.52264E + 13 to 2.69935E + 13 euros.

If the tax conditions for venture capital are optimized, the average willingness to invest in companies that are in the early stages of its existence increases.

The current willingness to invest (2015) of the 22 countries studied is 13,51 euros per capita in the Industry Statistic and 8,79 euros in the Market Statistic. If these figures are compared with the data obtained in this study, it can be seen that the optimized tax conditions (tax expenditures) lead to a significantly higher level of investment readiness. The industry statistic has now changed to 34,41 euros, while the willingness to invest in target companies (Market Statistic) has risen to 13,93 euros.

In addition, the unemployment rate mentioned in Chapter 2.2.3.2 will fall. The entrepreneurs will already create jobs, and the suppliers required at the beginning will also need more staff. There will also be synergy with external consultants, banks and the state, so that positive signals for the labor market can be expected at this point. However, in this context, no figures can be mentioned – even in statistical terms – as a linear increase in employment is not achieved at the expected growth rates of investment and gross domestic product.

All these figures show that tax-optimized conditions (in this case, average tax rates of those countries which are similar to one another on a high level) can lead both to an increased willingness to invest and a higher GDP - and thus also per capita (the actual key figure that takes into account the prosperity of the individual) also leads to higher willingness to invest.

5 CONCLUSION AND OUTLOOK

The objective of this study was to develop a theory-based and empirical analysis of the influence and impact of taxes in regards to a Private Equity fund and analogous Venture Capital fund. Based on theoretical and empirical findings, tax rates were derived for the design of tax optimized Venture Capital funds, which create the conditions for the successful development of Venture Capital funds, and thus, the development of entrepreneurs and in turn the development of the economy of the European Union.

In summary, the following findings result from the influence and effect analysis and the derivation of the design recommendations:

A. Characteristics of Private Equity:

1. Private Equity describes a form of temporary provision of capital for equity financing of companies – and in that also and especially important for entrepreneurs and young companies (Hehn, 2011, p. 40 et seqq.; Natter, 2003, p. 10 et seqq.). Opposite of Public Equity, which aims at the equity for listed companies, Private Equity refers to off-exchange equity for unlisted companies. Private Equity can be divided – see also Tcherveniachki or Weber (2007, p. 18 et seqq.; 2009, p. 23 et seqq.) or Gladstone & Gladstone in their Entrepreneur´s Guide to Raising Venture Capital (2002, p. 7 et seqq.) – into Private Equity, Venture Capital, Buyout and Mezzanine Capital.
2. Suppliers and consumers of off-exchange capital – also Zipser (2008, p. 1 et seqq.) or Reimers (2004, p. 4 et seqq.) – meet on the market for Private Equity. Consumers are companies with demand for capital which cannot be covered by own or borrowed funds. On the supplier side, there are the institutional investors (Tausend, 2006, p. 13 et seqq.) and private investors (Lerch, 2011, p. 6 et seqq.).

3. With regard to the classification of Private Equity in the financing structure and the financing stages it can be stated that the provision of equity, depending on the financing situation, is often carried out with borrowed funds – not always safe as well Regner says (2008, p. 71 et seqq.) – to finance the companies. Especially for the realization of the above-indicated buyouts – which are to be divided in management buy-out, management buy-in and leveraged buy-out – the proportion of borrowed funds is often substantial. The use of the leveraged effect – while taking all due caution into account – promotes the financing through borrowed funds. The funding is dependent on the accession of the investor into the financing. Thus, these funds are either provided during the early stages of a company in terms of a start-up funding or at later stages, which begin from the phase of expansion on and possibly end with the financing of an IPO.

4. The fact that companies engage in financing outside the classical methods of financing – such as a bank loan – is based on the fact that those enterprises may not be able to provide the appropriate collaterals (Bösch, 2009, p. 203 et seqq.) to qualify for further loans (Prümer, 2005, p. 108 et seqq.). Reasons for such considerations are – non-exhaustive – the difficulties of an enterprise to find a suitable successor for the continuation of the business activities or that it might require monies for the expansion of the production or services offered, for going public or – in case of declining activities or structural and cyclical upheavals – for a Turn Around.

5. A large part of the portfolio companies generate profit by acquiring companies or shares, selling them again after a certain holding period in connection with the support through the apposition of expertise (Geidner, 2009, p 9 et seqq.). This goes hand in hand with a majority stake. This activity is accompanied by riskier investments in the early stages of a company constituting a minority stake. This information is especially important for entrepreneurs, because this specialization restricts the choice of the future provider of capital to minimize the risk of a failing leveraged buy-out early on.

6. Private Equity is quite suitable as a separate asset class (Tausend, 2006, 13 et seqq.). In part, Private Equity investments can perform better during crises than comparable investments in stock. This positive characteristic might induce investors to consider their own investment decisions under different aspects than the practice to rely on the performance of Private Equity from the past. Thus, Private Equity may therefore not only enrich the portfolio as a whole.

B. Regulations of Private Equity within the European Union:

1. The European Union is an economic and political union of currently 28 – United Kingdom has exited via a referendum – European states. Taking the gross domestic product into account, the economic power or the size of the European Union has expanded in such a way that this market is regarded as the largest common market in the world (Ekardt, 2014, p. 113 et seqq.). Those institutions, which are especially important for Private Equity, are the European Investment Fund, the European Court of Auditors, the European Investment Bank, the European Commission, The European Council, the European Economic and Social Committee, The European Parliament, and especially the European Central Bank (European Union, 2013).
2. Companies financed by Private Equity, respectively Venture Capital, show a faster growth compared to other companies. They create more jobs and are aligned more export-oriented (Brehm, 2012, p. 1 et seqq.). Thus, they provide a strong economic momentum. In the European context, the investment in Private Equity and especially in Venture Capital means an investment in the future. The power of new ideas for products and sustainable services is outstanding.
3. For the European area, United Kingdom – whether it stays that way, is to be seen – is the most important market as far as the willingness to participate in risk-bearing investments is concerned, while Greece is located at the bottom end of this scale. On the other hand, there is Denmark, which takes

the lead regarding companies financed. Countries, which actually are traditionally strong economies such as Germany and Italy, do poorly in this context.

4. From an economic perspective, many efforts have been strained to battle the current problems of the European Union. Until recently, most scientists and other experts were of the opinion that the only way out of this dilemma in an economical sense, could only be by taking the neoclassical approach. Meanwhile, more attention is being paid to the almost forgotten Keynes approach (Weizäcker, 2013, pp. 1-2).

5. With the continuous development and innovation of the global financial industry, many different financing and investment institutions emerged as opponents for the traditional banks. To take appropriate counteractions against those alleged shadow banks, the European Union (EU) has had to respond with some regulations. To the latest financial crisis, the EU legislator responded with Directive 2011/61/EU on Alternative Investment Fund Manager – the so-called AIFMD. The scope of this directive applies to the manager of alternative investment funds, in which alternative investment funds in a negative accrual are collective investments, which are not covered by the UCITS Directive (Buck-Heeb, 2014, p. 276 et seqq.).

C. *Affects and Effects of Taxes on Private Equity within the European Union*

1. The tax law had to follow those regulations. A large number of individual taxes characterizes the tax systems in the industrialized countries, as are most EU countries. Concerning tax tangents to Private Equity, the distinction of Private Equity funds in commercial or asset management is of paramount importance in parts of the EU – and especially in Germany (Bohn, 2009, p. 196 et seqq.). Moreover, the carried interest (Heim, 2015, p. 124 et seqq.) has to be mentioned, which constitutes a profit sharing of up to 20%. Losses carried forward, the treatment of interest expenses and the VAT

treatment of management services are further areas of the fiscal observatory horizon.

2. The incidence of influence and effect in relation to the investment behavior depends on many different parameters. The gross domestic product and, above all, the gross domestic product per capita, has a strong impact on the willingness to invest. Taxes have an impact on the gross domestic product and therefore more or less directly on the investment behavior of the countries.

3. Empirically, it has been shown that the investment activities of domestic holding companies are largely dependent on the gross domestic product of the respective country. Overall, it could be depicted that in this segment, the Scandinavian countries expose themselves; however, they are framed by Luxembourg and the United Kingdom. The same is true for the investments in the early stages of an enterprise, with Ireland joining the group, which apparently is undertaking great efforts to support its start-up entrepreneurs. With regard to the willingness of countries to invest in domestic portfolio companies it could be determined that Denmark shows a strong commitment. However, rather not as far as the financing in the early stages is concerned. Overall, this in turn resulted in a group with mainly Scandinavian countries and Ireland.

4. Empirically it could also be noted that the under consideration of the taxes, relevant for Private Equity, respectively Venture Capital, that yet again the Scandinavian countries next to Great Britain show high level similarities to each other. Of the three major economies, although they account for the majority of Private Equity transactions, only Great Britain remains at the forefront, if the investigation is extended to include the gross domestic product.

5. The design recommendations for the effect of taxes on the willingness to invest are aimed to summarize the tax rates for capital gains tax, withholding tax and for the company taxes of the countries determined to average

rates. In this, the peculiarities such as the taxation of 0% to 36 % in the above-mentioned tax territories of each country are to be considered, so that uniform tax rates for the extracted areas are created.

The findings gained throughout this study are the basis for further research approaches to reveal the relevance of Private Equity and especially Venture Capital as a financing alternative in the context of the growth of markets within the European Union. During this study, the effect of the gross domestic product per capita on the willingness of the countries to invest has been examined and from that, a fiscal relevance has been derived. This results in further questions beyond the influence-effect-relation. Tax –adapted conditions create an equality of opportunity. Not yet resolved, however, is:

- Who has access to this tax-optimized FONDS EUROPAEA?
- Which regulatory framework must be adapted in order to bring this fund on the market?
- Does this fund apply parallel to the current arrangements or is this fund to be applied without alternatives?

A wide variety of literature has been read and processed on this study. Here, many laws were discovered and deemed interesting and in part even included in this study. For example, the Verdoorn´s Law was incorporated in chapter 2.3.5 Economic Growth and Full Employment to illustrate the economic growth. According to this law, there is a linear relationship between labor productivity and the growth of production. In the consideration of Austria and Germany, this relationsip could not be imperatively established. At least for the satisfaction of the own interest but also beyond, it could be examined in more detail whether the Law of Kaldor is actually an axiom.

A large part of the cluster analysis made have not found their place in this study. This is not based on them being nondescriptive or ineffective. That's quite the contrary. Most of these analyses, which, incidentally are provided in the annex, have enough potential to be not only interpreted but could lead to investigations of their own. As an example, the examination of the per capita capital investments under consideration of the unemployment rate in appendix 1 may be mentioned at this point. The correlation between per capita gross domestic product and the willingness to invest is clearly discovered in this present study. Therefrom, it could easily be deducted that a high unemployment rate suggests a lower per capita domest product, which in turn leads to a lower propensity to invest. In this case, as well, this study has indicated the contrary in some part. The behavior of France and Finland can be interpreted as an outlier. However, this seems to be insufficient. Rather the time factor could play an important role. Finland has already shown a positive trend for some years and is no doubt slowly being rewarded for the Venture Capital efforts. France, being a traditional Private Equity market, potentially has supported the volume of large transactions too extensively over time. This time-effect-relation could also lead to further investigations such as the fundamental questions of the performance of the countries and individuals. For this, the gross domestic product per capita depicts a brilliant model, especially the placement of France or Germany compared to Ireland in this category for instance.

The BVK (Bundesverband Deutscher Kapitalbeteiligungsgesellschaften) has positively assessed the various initiatives on part of the German Federal Government. However, in his paper "BVK draft for a venture capital law", he clarified that all these measures are only a small step in the right direction. For example, BVK – and this goes without saying for the other member states of the European Union in a similar form – speaks of legislative competence which is always a hurdle for renewal. The Income Tax Act, the Corporate Income Tax Act, the Value Added Tax Act and the Investment Tax Act should be amended. In addition, the Trade Tax Act would also have to be reorganized. Compatibility with the law of the European Union and international treaties should be examined. On the other hand, the results of the present study are not intended to interfere with the respective legal positions of the individual Member States, but rather as an additional tool, possibly centrally managed, to give the venture capital industry a different look. Uniform tax rates applicable only to this “FUND EUROPAEA”.

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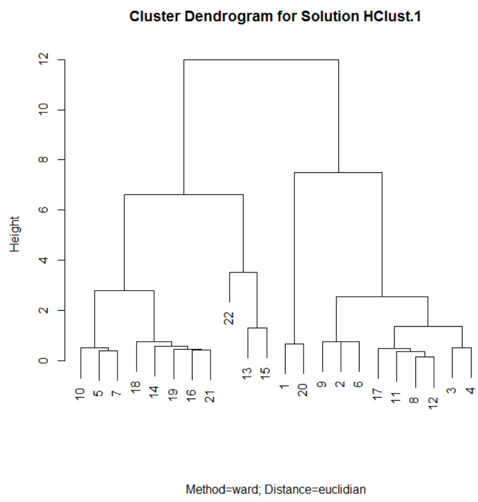
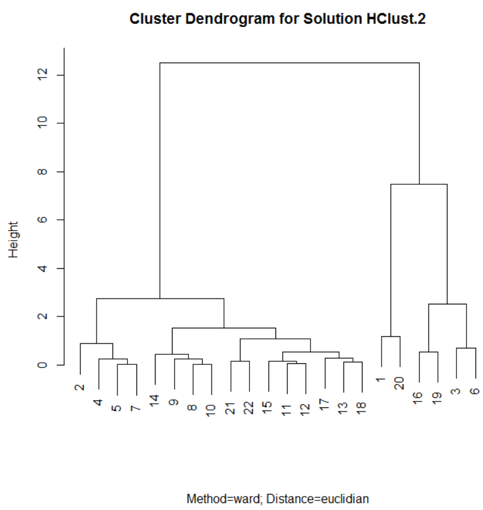
Appendix 59: Capital Gains Tax max - IMSVCIT – Unemployment Rate 385
Appendix 60: Capital Gains Tax max – IMSVCPC – Unemployment Rate 385

Appendix 1: Per Capita VC Investments – Unemployment Rate



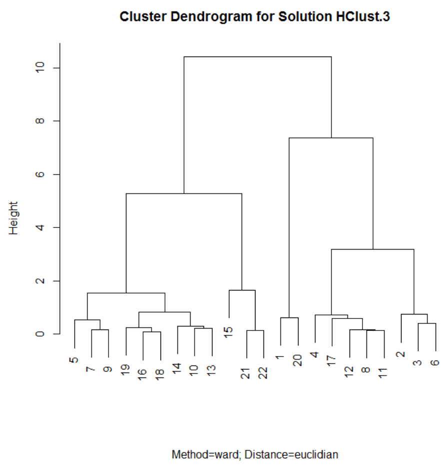
Source: Own representation with Statistics R.

Appendix 2: Gross Domestic Product – Unemployment Rate



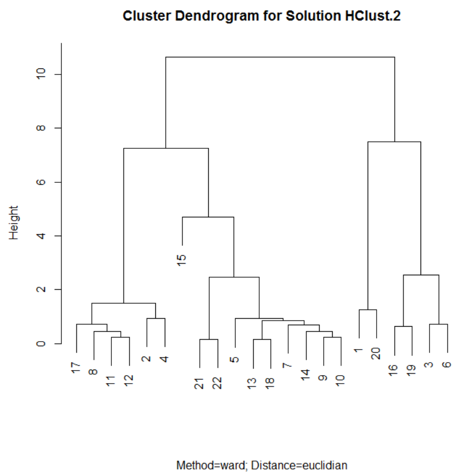
Source: Own representation with Statistics R.

Appendix 3: Gross Domestic Product per Capita – Unemployment Rate



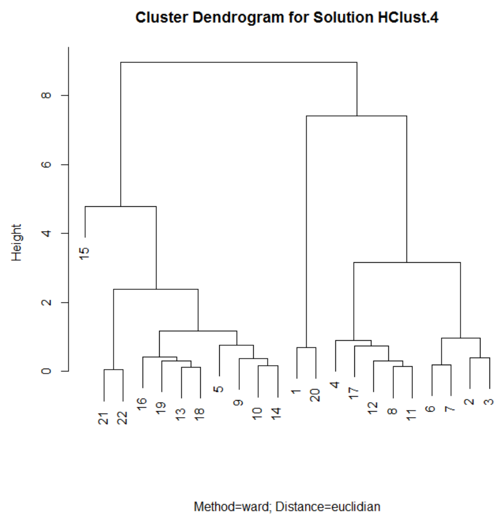
Source: Own representation created with Statistics R.

Appendix 4: Purchasing Power Standard – GDP - Unemployment Rate



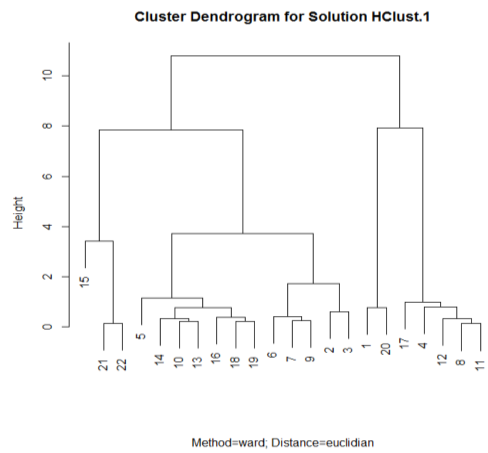
Source: Own representation created with Statistics R.

Appendix 5: Purchasing Power Standard – Unemployment Rate



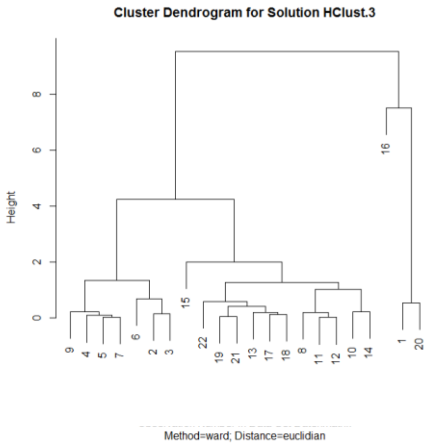
Source: Owen representation created with Statistics R.

Appendix 6: PPS – Unemployment Rate – GDP per Capita



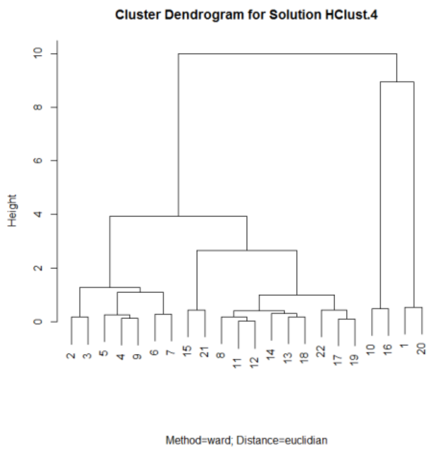
Source: Owen representation created with Statistics R.

Appendix 7: Fundraising – Unemployment Rate



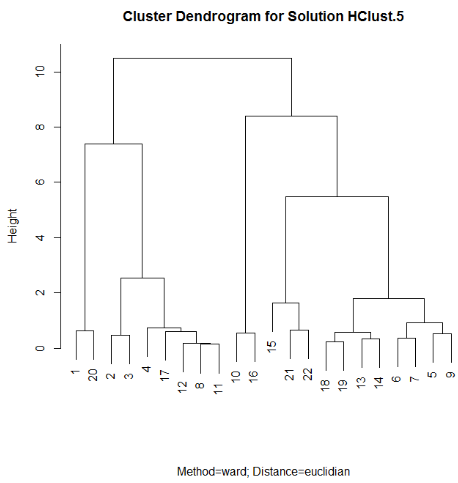
Source: Own representation created with Statistics R.

Appendix 8: Fundraising per Capita – Unemployment Rate



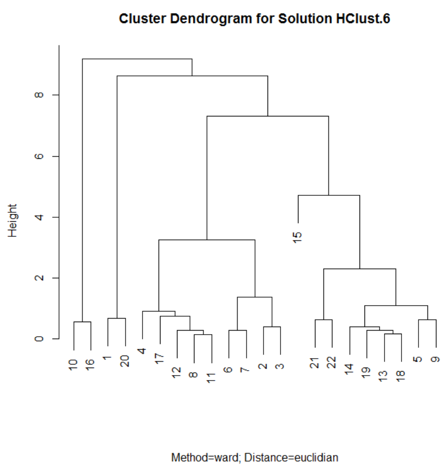
Source: Own representation created with Statistics R.

Appendix 9: Fundraising per Capita – GDP per Capital – Unemployment Rate



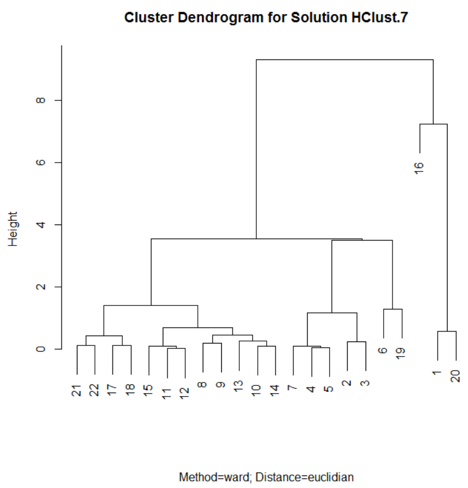
Source: Owen representation created with Statistics R.

Appendix 10: PPS – Fundraising per Capita – Unemployment Rate



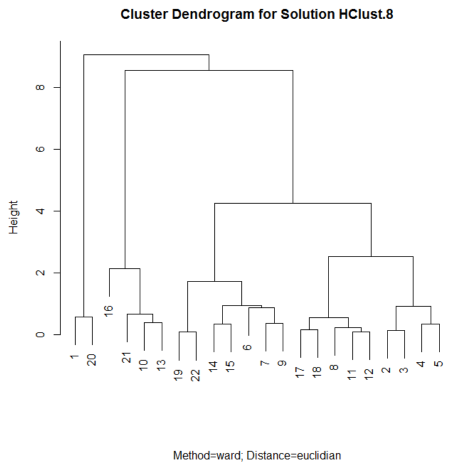
Source: Owen representation created with Statistics R.

Appendix 11: Investments Industry Statistics – Unemployment Rate



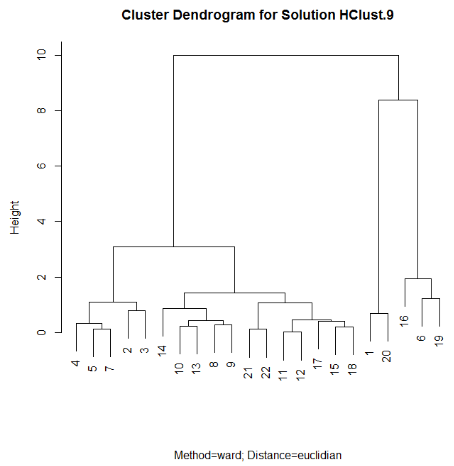
Source: Owen representation created with Statistics R.

Appendix 12: Investments per Capita Industry Statistics – Unemployment Rate



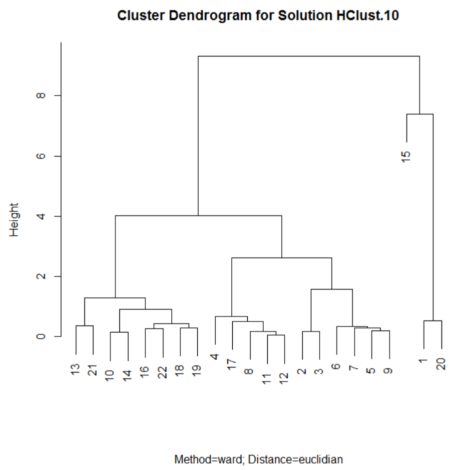
Source: Owen representation created with Statistics R.

Appendix 13: Investments Market Statistics – Unemployment Rate



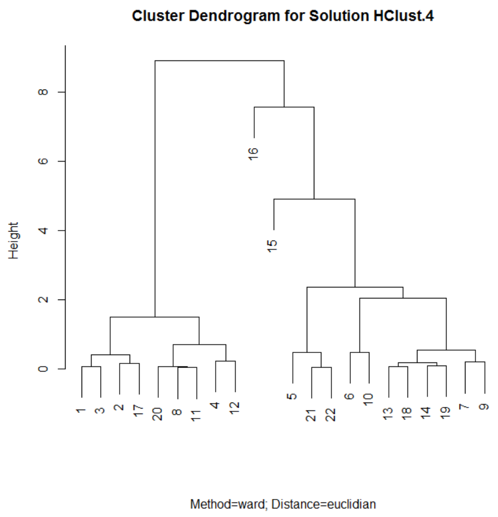
Source: Owen representation created with Statistics R.

Appendix 14: Investments per Capita Market Statistics – Unemployment Rate



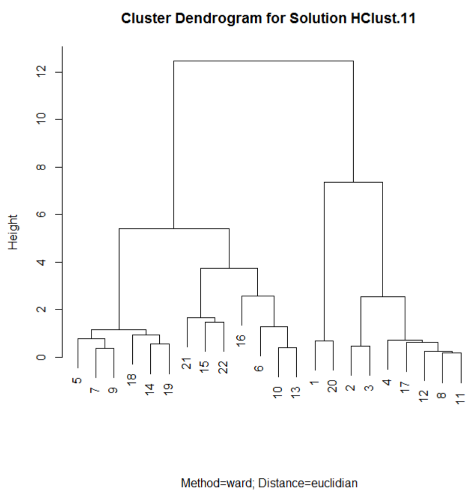
Source: Owen representation created with Statistics R.

Appendix 15: IISPC – GDP – Unemployment Rate



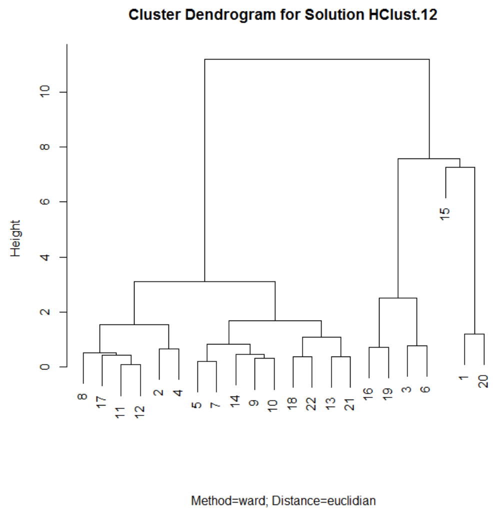
Source: Owen representation created with Statistics R.

Appendix 16: IISPC – GDP per Capita – Unemployment Rate



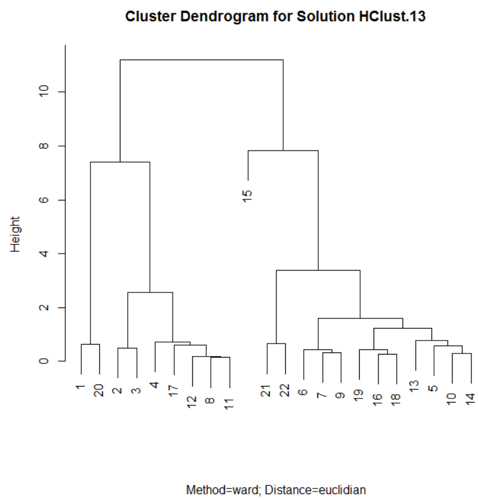
Source: Owen representation created with Statistics R.

Appendix 17: IMSPC – GDP – Unemployment Rate



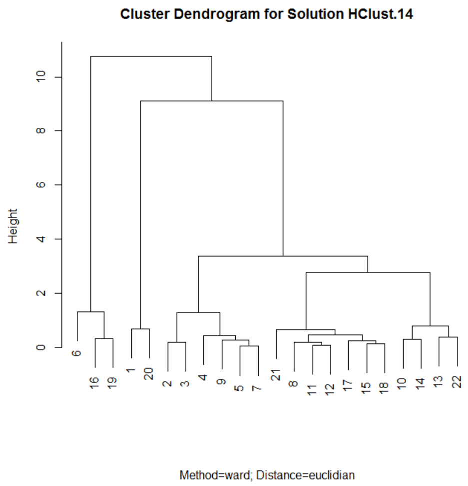
Source: Owen representation created with Statistics R.

Appendix 18: IMSPC – GDP per Capita – Unemployment Rate



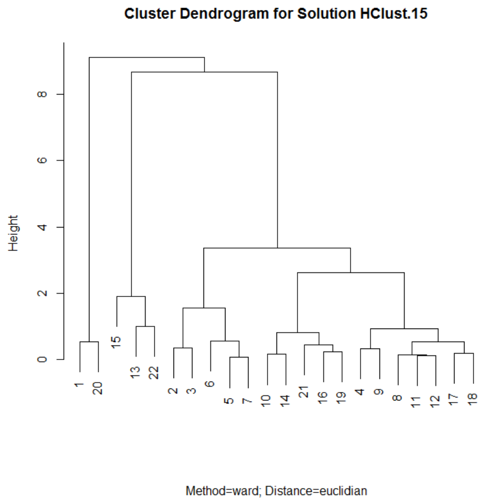
Source: Owen representation created with Statistics R.

Appendix 19: Investments Venture Capital Industry Statistics – Unemployment Rate



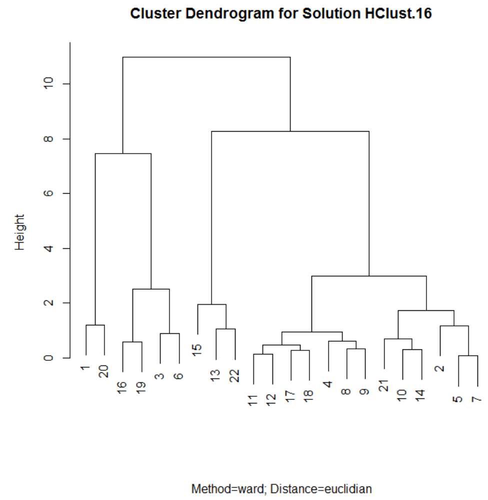
Source: Owen representation created with Statistics R.

Appendix 20: IISVCPC – Unemployment Rate



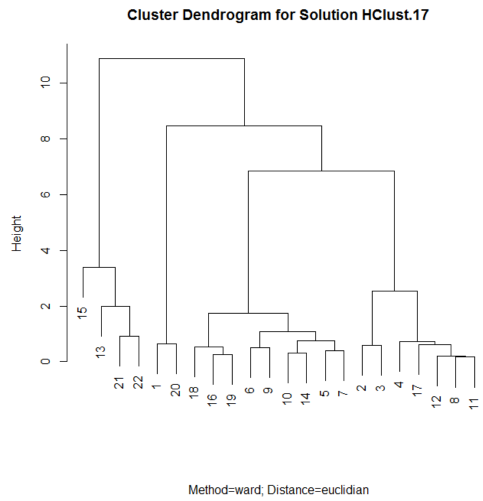
Source: Owen representation created with Statistics R.

Appendix 21: IISVCPC – GDP – Unemployment Rate



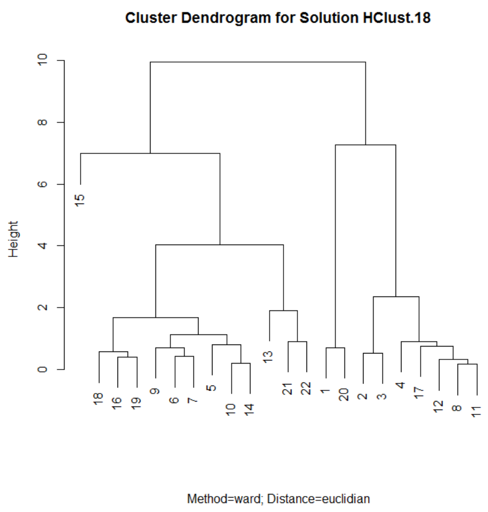
Source: Owen representation created with Statistics R.

Appendix 22: IISVCPC – GDP per Capita – Unemployment Rate



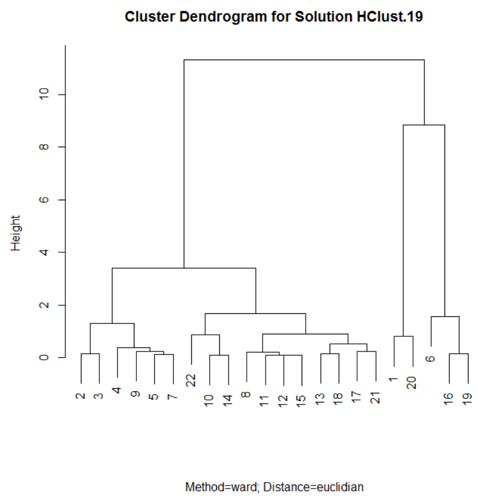
Source: Owen representation created with Statistics R.

Appendix 23: IISVCPC – PPS – Unemployment Rate



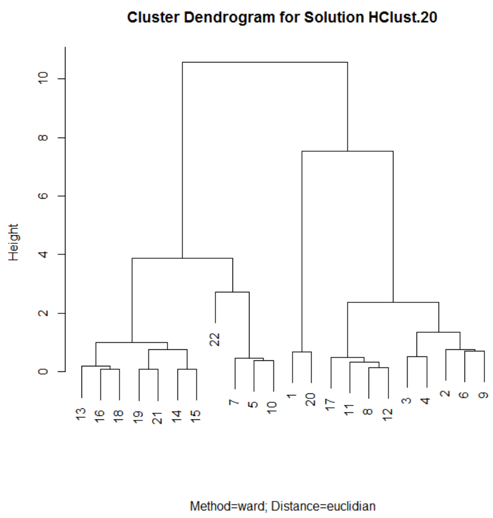
Source: Owen representation created with Statistics R.

Appendix 24: Investments Venture Capital Market Statistics – Unemployment Rate



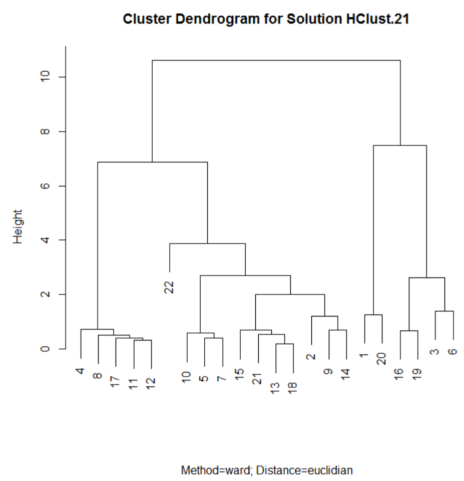
Source: Owen representation created with Statistics R.

Appendix 25: IMSVCPC – Unemployment Rate



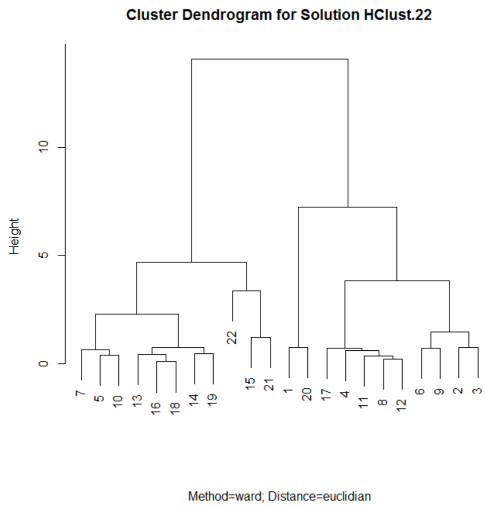
Source: Owen representation created with Statistics R.

Appendix 26: IMSVCPC – GDP – Unemployment Rate



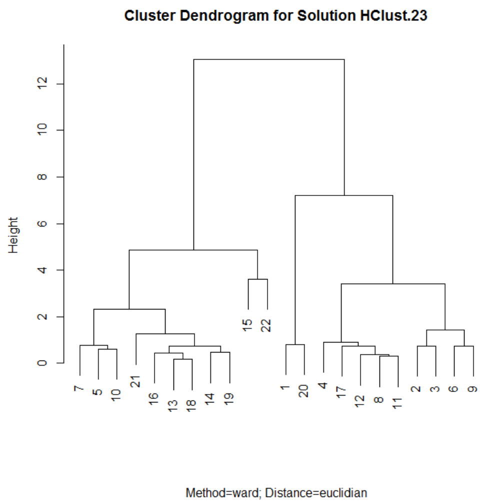
Source: Owen representation created with Statistics R.

Appendix 27: IMSVCPC – GDP per Capita – Unemployment Rate



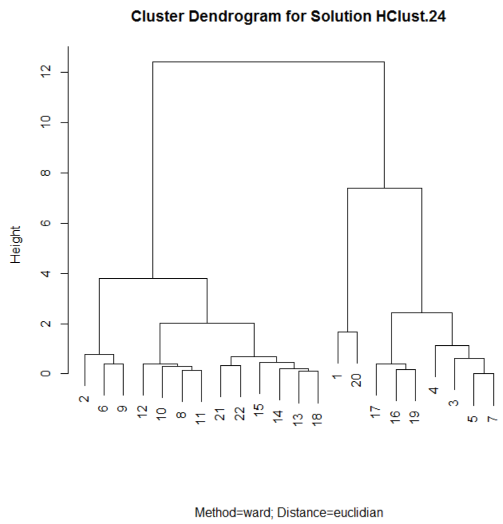
Source: Owen representation created with Statistics R.

Appendix 28: IMSVCPC – PPS – Unemployment Rate



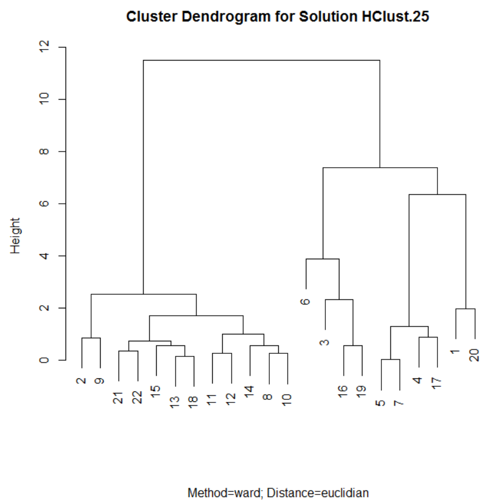
Source: Owen representation created with Statistics R.

Appendix 29: Capital Gains Tax max – Unemployment Rate



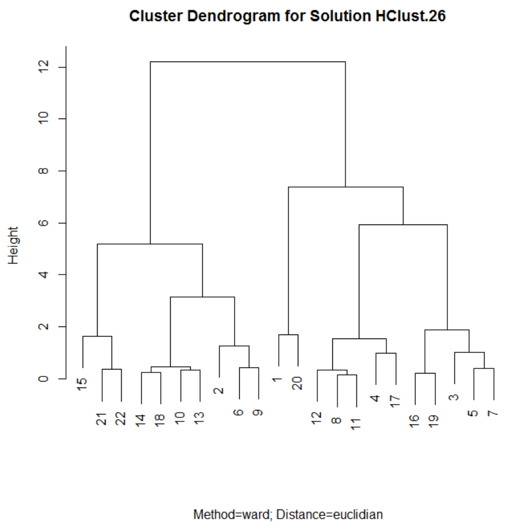
Source: Owen representation created with Statistics R.

Appendix 30: Capital Gains Tax max – GDP – Unemployment Rate



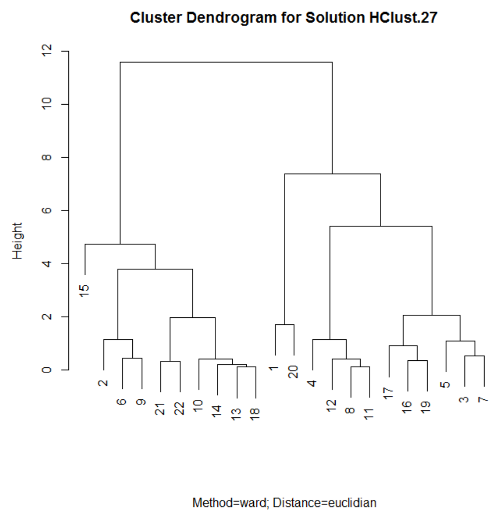
Source: Owen representation created with Statistics R.

Appendix 31: Capital Gains Tax max – GDP per Capita – Unemployment Rate



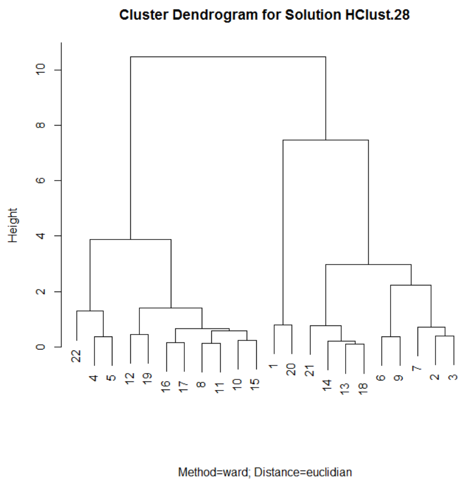
Source: Owen representation created with Statistics R.

Appendix 32: Capital Gains Tax max – PPS – Unemployment Rate



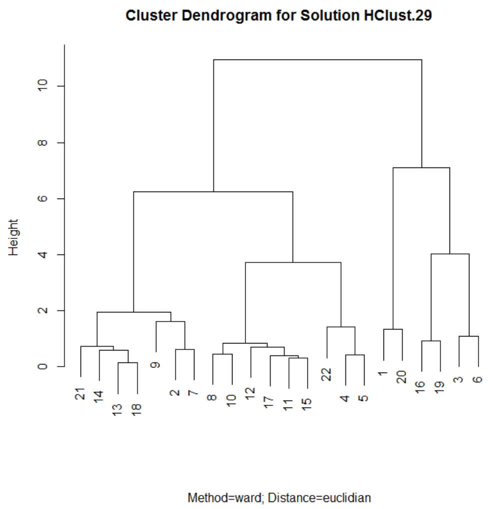
Source: Owen representation created with Statistics R.

Appendix 33: Corporate Income Tax – Unemployment Rate



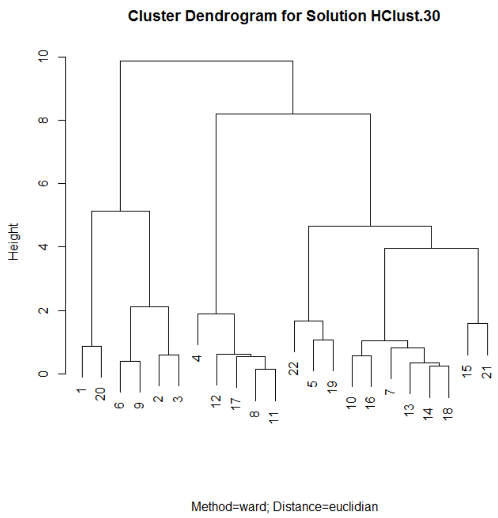
Source: Owen representation created with Statistics R.

Appendix 34: Corporate Income Tax – GDP – Unemployment Rate



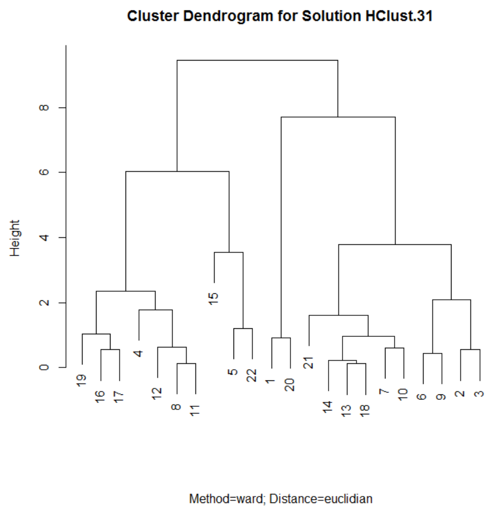
Source: Owen representation created with Statistics R.

Appendix 35: Corporate Income Tax – GDP per Capita – Unemployment Rate



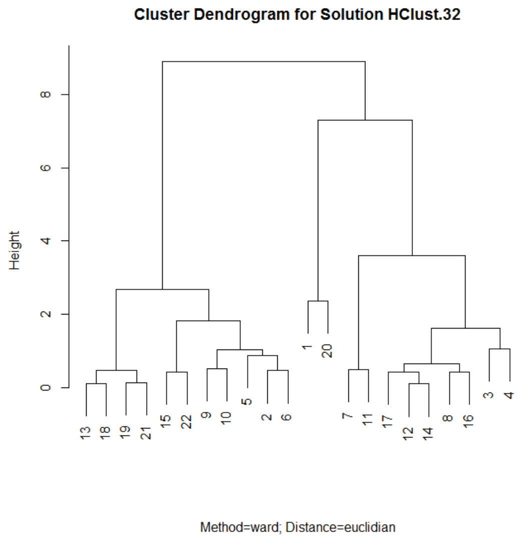
Source: Owen representation created with Statistics R.

Appendix 36: Corporate Income Tax – PPS – Unemployment Rate



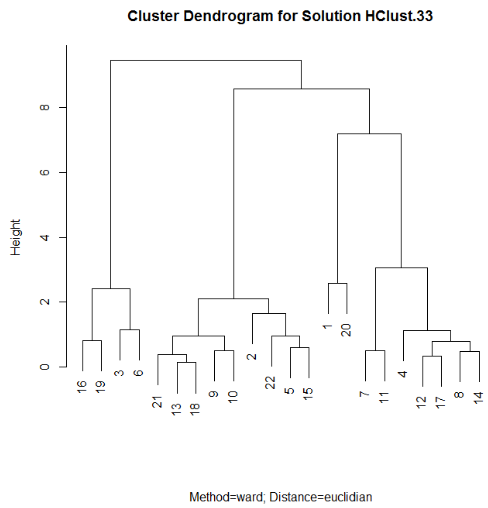
Source: Owen representation created with Statistics R.

Appendix 37: Withholding Tax – Unemployment Rate



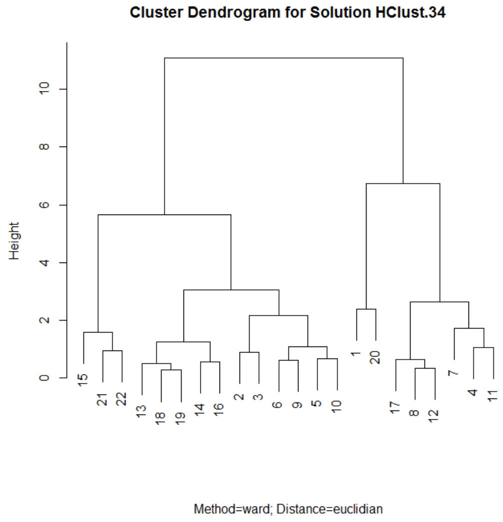
Source: Owen representation created with Statistics R.

Appendix 38: Withholding Tax – GDP – Unemployment Rate



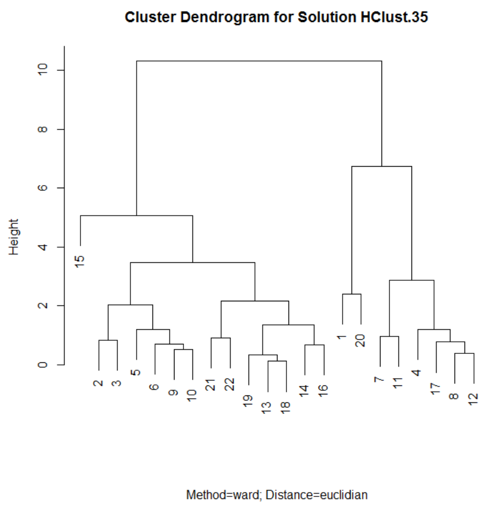
Source: Owen representation created with Statistics R.

Appendix 39: Withholding Tax – GDP per Capita – Unemployment Rate



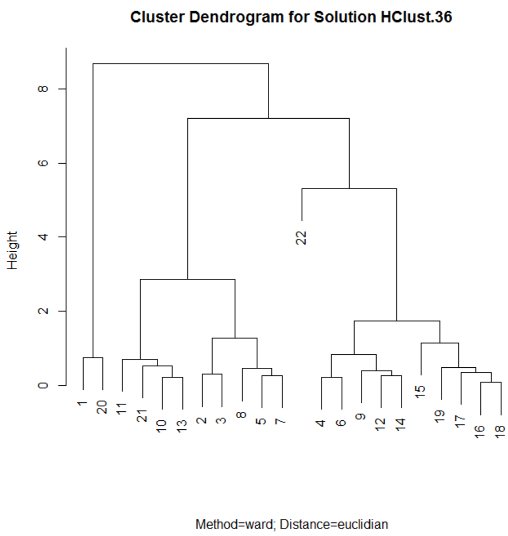
Source: Owen representation created with Statistics R.

Appendix 40: Withholding Tax – PPS – Unemployment Rate



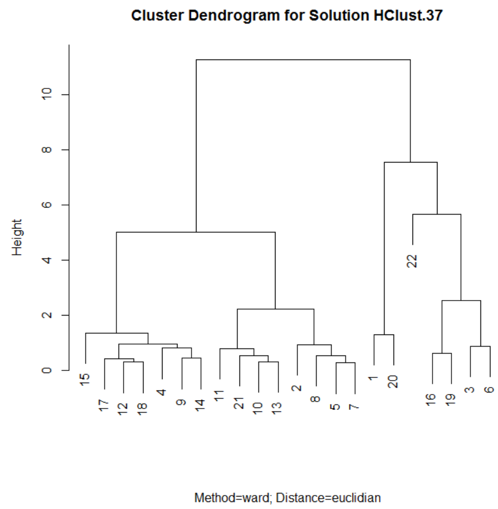
Source: Owen representation created with Statistics R.

Appendix 41: Value Added Tax – Unemployment Rate



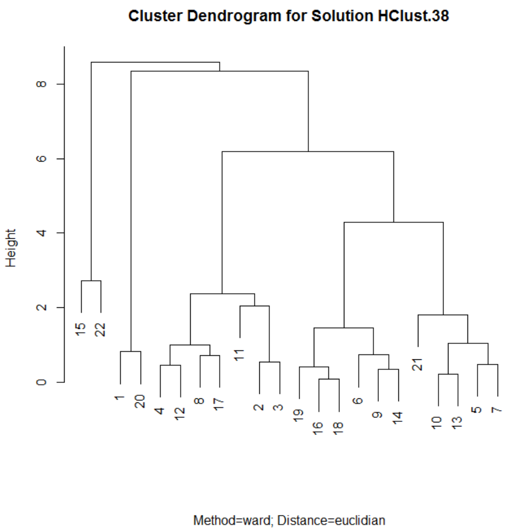
Source: Owen representation created with Statistics R.

Appendix 42: Value Added Tax – GDP – Unemployment Rate



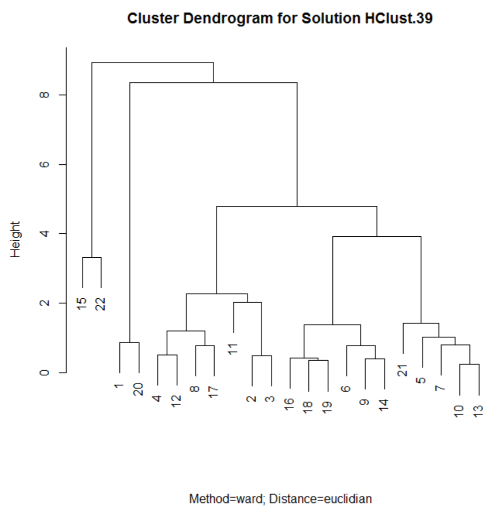
Source: Owen representation created with Statistics R.

Appendix 43: Value Added Tax – GDP per Capita – Unemployment Rate



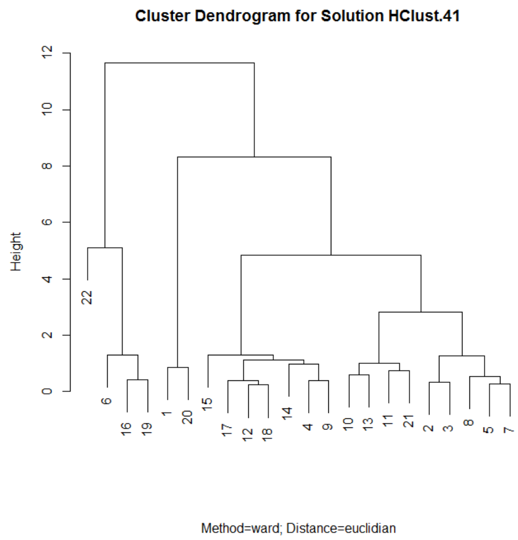
Source: Owen representation created with Statistics R.

Appendix 44: Value Added Tax – PPS – Unemployment Rate



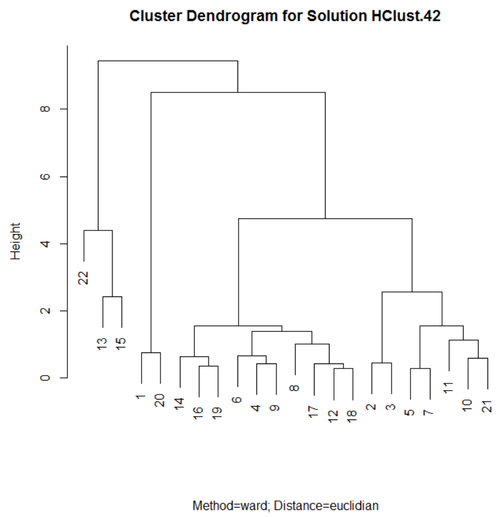
Source: Owen representation created with Statistics R.

Appendix 45: Value Added Tax – IISVCIT – Unemployment Rate



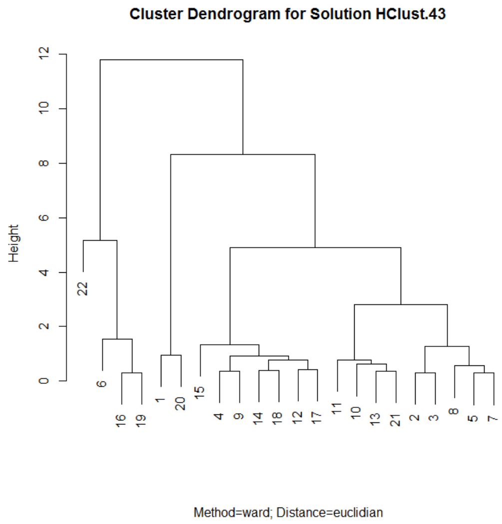
Source: Owen representation created with Statistics R.

Appendix 46: Value Added Tax - IISVCPC – Unemployment Rate



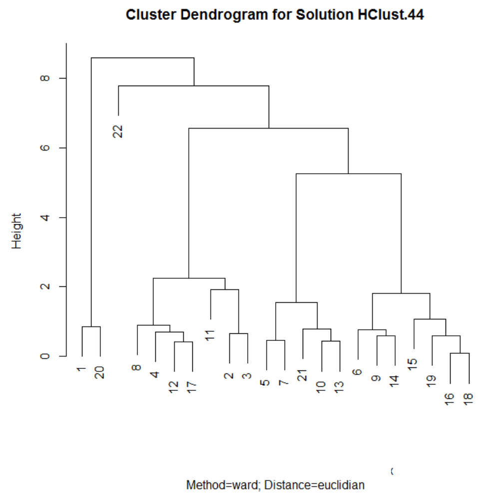
Source: Owen representation created with Statistics R.

Appendix 47: Value Added Tax – IMSVCIT – Unemployment Rate



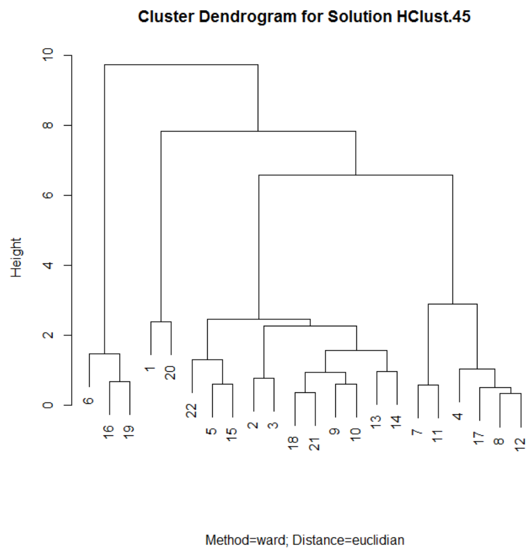
Source: Owen representation created with Statistics R.

Appendix 48: Value Added Tax – IMSVPC – Unemployment Rate



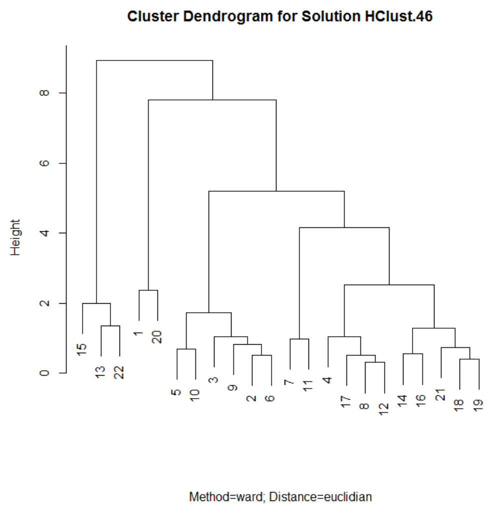
Source: Owen representation created with Statistics R.

Appendix 49: Withholding Tax – IISVCIT – Unemployment Rate



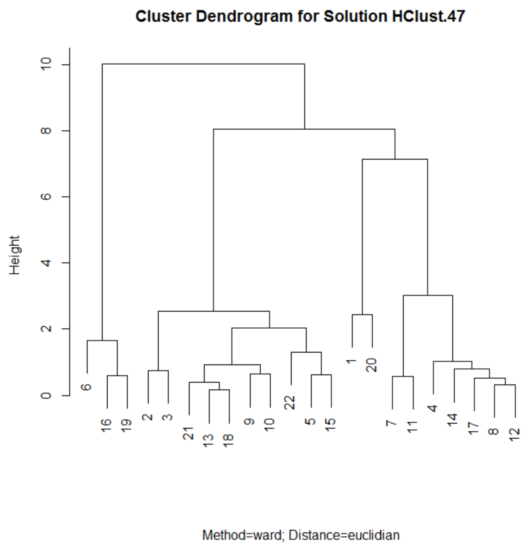
Source: Owen representation created with Statistics R.

Appendix 50: Withholding Tax – IISVCPC – Unemployment Rate



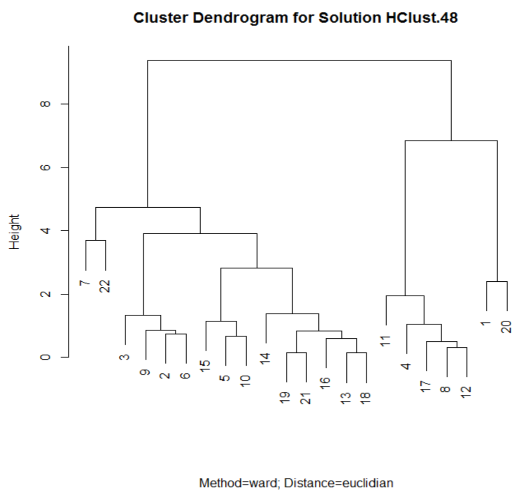
Source: Owen representation created with Statistics R.

Appendix 51: Withholding Tax – IMSVCIT – Unemployment Rate



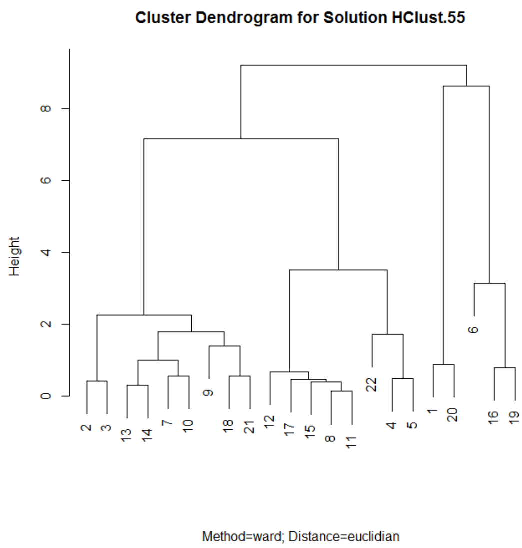
Source: Owen representation created with Statistics R.

Appendix 52: Withholding Tax – IMSVPC – Unemployment Rate



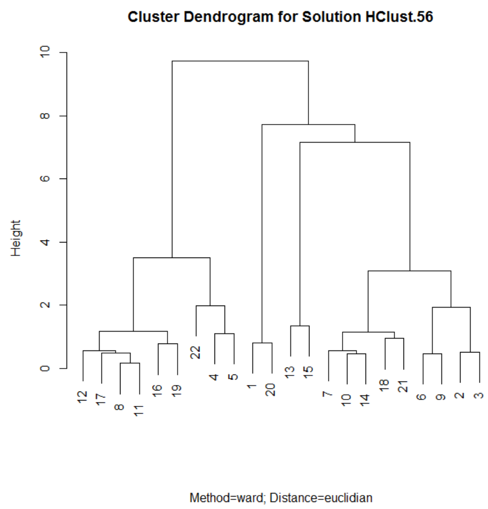
Source: Owen representation created with Statistics R.

Appendix 53: Corporate Income Tax – IISVCIT – Unemployment Rate



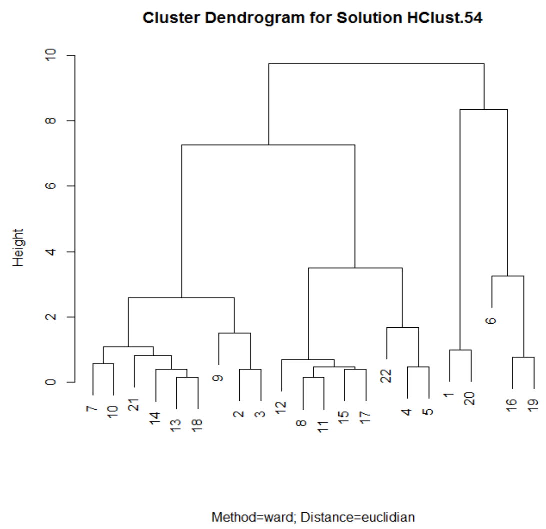
Source: Owen representation created with Statistics R.

Appendix 54: Corporate Income Tax – IISVCPC – Unemployment Rate



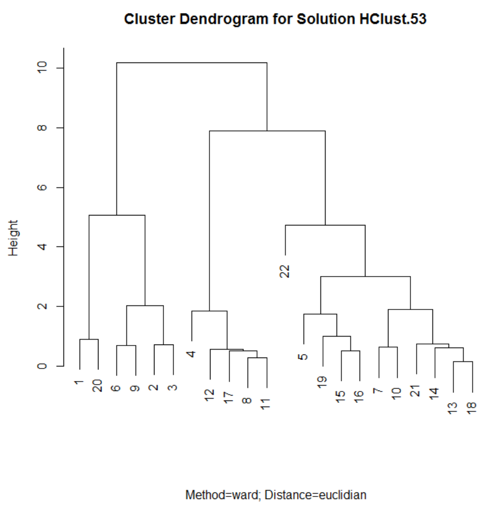
Source: Owen representation created with Statistics R.

Appendix 55: Corporate Income Tax – IMSVCIT – Unemployment Rate



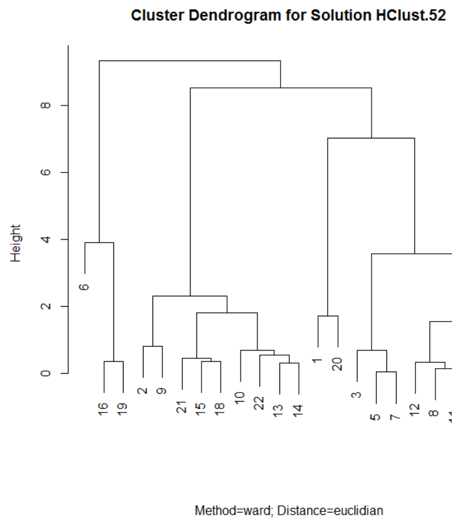
Source: Owen representation created with Statistics R.

Appendix 56: Corporate Income Tax – IMSVCPC – Unemployment Rate



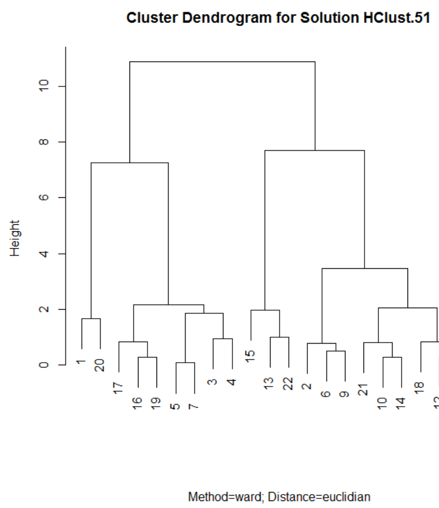
Source: Owen representation created with Statistics R.

Appendix 57: Capital Gains Tax max – IISVCIT – Unemployment Rate



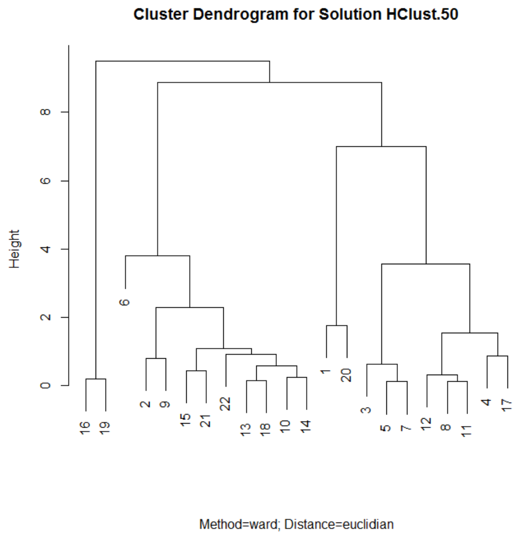
Source: Owen representation created with Statistics R.

Appendix 58: Capital Gains Tax max – IISVCPC – Unemployment Rate



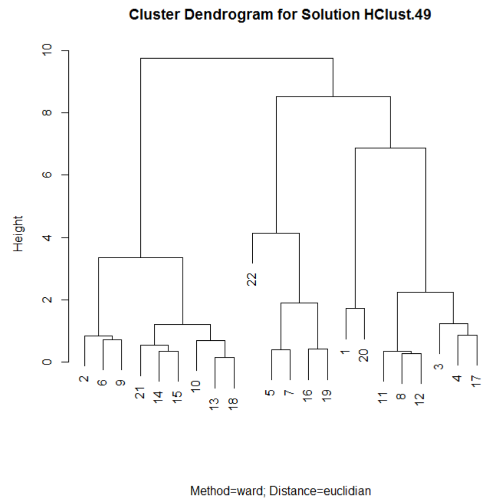
Source: Owen representation created with Statistics R.

Appendix 59: Capital Gains Tax max - IMSVCIT – Unemployment Rate



Source: Owen representation created with Statistics R.

Appendix 60: Capital Gains Tax max – IMSVCPC – Unemployment Rate



Source: Owen representation created with Statistics R.

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