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### **Venture capital funds operating as an alternative investment company**

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## **Summary**

The subject of this dissertation is the functioning of venture capital funds operating as an alternative investment company. This is a topic of great practical importance, which has been steadily gaining popularity over the past few years, but has not yet been comprehensively reviewed in literature, in particular in the context of venture capital funds. On June 4, 2016, the amendment to the Polish Act on investment funds and management of alternative investment funds entered into force as part of the implementation into the Polish legal system of Directive 2011/61/EU of the European Parliament and of the Council of June 8, 2011. As a result of the abovementioned amendment, a new category of entities has emerged. It included companies conducting investment activities in Poland, not yet regulated under the Polish public law regime – i.e. alternative investment companies, which are supposed to be an alternative especially to closed-end investment funds.

The dissertation has been structured in accordance to the criterion of describing the subject matters from the most general to the most detailed ones. First of all, the broadest issue was characterized, concerning the first part of the topic, i.e. the concept of the venture capital fund, and then the second - an alternative investment company, which has a normative definition contained in Polish Act on investment funds. In next chapter, the most important issues related to functioning of venture capital funds in the form of an alternative investment company and in the form of a closed-end investment fund, in particular a closed-end fund of non-public assets, were compared. After that, a legal comparative analysis of the subject matter was presented. Then, two most extensive and detailed chapters were depicted, concerning the core of the issues discussed, and at the same time the most

complicated as, as they were almost unreviewed in legal doctrine. Therefore, the conditions for qualifying the entity as an alternative investment company on the basis of the statutory definition, supplemented with ESMA guidelines, Polish Financial Supervision Authority positions and literature, were analyzed. Then, the detailed regulations on conducting the operational activities of alternative investment companies in Poland were discussed. Finally, to complete the examination on the theses of this paper, an empirical analysis of the subject matter has been presented. The detailed structure of the dissertation is as follows:

In the first chapter, the conceptual issues of key importance for the discussed topic were presented. The interpretation of the venture capital fund definition was analyzed along with a description of the obligatory elements forming its definition. Moreover, the differences between the terms of venture capital and private equity, which are often mistakenly identified as being identical, were highlighted. Types of venture capital funds were also listed by comparing them with the most important divisions of investment funds distinguished in the literature on the subject. Due to the large number of typologies, they were divided based on legal and economic criteria. The most important definitions related to the discussed issues were also examined, i.e. the definition of an investment fund and a specification of its corporate bodies and basic operating principles; definition of an alternative investment fund, along with a further division of this conceptual category into its specific types; the definition of an alternative investment company manager, as well as the concept of startup, which is devoid of the normative definition and was supplemented by the definition of small and medium-sized enterprises as defined by the EU legislator.

The second chapter of this dissertation presents a comparison of benefits and losses, which from the perspective of investors considering conducting investment activities in the venture capital sector are associated with the choice of the legal form of an alternative investment company instead of a closed-end investment fund, in particular a closed-end fund of non-public assets. Before the implementing alternative investment companies to the Polish legal system, many venture capital funds were functioning as a closed-end investment fund of non-public assets. The advantages and disadvantages of both legal forms in the context of starting a business, investment restrictions, information and reporting obligations, as well as costs related to conducting business, have been compared in that chapter.

In the third chapter the functioning of venture capital funds in a comparative legal approach was discussed.– a comparative analysis of legislation in Luxembourg, Germany, France, Great Britain and the United States was conducted. The regulations there have been examined not only to assess the provisions in force in Poland in the field of the subject matter, but also to answer the question, whether from the perspective of Polish venture capital funds, it is worth considering the creation of cross-border legal structures headquartered abroad. In each of the abovementioned countries, the functioning of the venture capital market, the regulations applicable to them, available legal structures were analyzed. Therefore, the regulations on alternative investment funds and possible differences in this area were examined among the abovementioned countries.

The fourth chapter was devoted to discussing the complex, and in practice extremely problematic, conditions of qualifying a given entity as an alternative investment company, which causes the potential manager an obligation to submit an appropriate application to Polish Financial Supervision Authority. The concept of collective investment institutions, the premise of a multitude of investors, collecting assets, investing them in the interest of investors and having a specific investment policy were analyzed accordingly. The definition of a professional client has also been explored, to whom the title legal form is addressed in particular. It is possible to introduce an alternative investment company to trading among non-professional clients, i.e. retail clients, but the Act on investment funds enables such a possibility only in exceptional circumstances. The subject definition's restrictions and exclusions regarding alternative investment company were also presented. To complement the interpretation of the premises, ESMA guidelines and Polish Financial Supervision Authority positions regarding their interpretation were also cited.

The fifth chapter, which is also the most extensive, presents the key issue for the subject matters from the point of view of legal regulations - conducting the activities of managers of alternative investment companies in Poland. Therefore, the admissible organizational structures were discussed, i.e. conducting such a business in the form of an externally managed alternative investment company and internally managed alternative investment company management, along with the basic problems that arise in this context of both structures. Then, the regulations concerning the two modes of regulation of the title activity

were reviewed –the permit to conduct the activities of managing an alternative investment company, as well as operating as such entity on the basis of an entry in the alternative investment company managers' register. The most important problematic issues that may arise when submitting by the manager of the alternative investment company an application for such an entry in the register or for obtaining a permit for such activity have been presented.

In the last, sixth chapter of the dissertation, an empirical analysis of the subject matter was carried out, both in terms of the activities of entities entered in the alternative investment company managers' register, and venture capital funds operating without being entered into this register. Based on publicly disclosed information, publications and industry reports, a specific empirical study of the subject was carried out to verify the statistics relevant to this dissertation. Therefore, all managers of alternative investment companies operating in Poland and all active venture capital funds were examined.

As one of the conclusions that can be drawn from this dissertation, it could be stated that the alternative investment company is currently the optimal legal form for conducting the activities of a venture capital fund in Poland. In particular, the choice of this legal form is, from the perspective of its managers and investors, more advantageous than operating as a closed-ended investment fund, including closed-end fund of non-public assets. To such conclusions lead both examined legal regulations regarding the subject matter, as well as analysis of current market practice in this field. To emphasize the accuracy of the thesis stated above, an alternative investment company was compared with its potentially largest competitor, which is a closed-end investment fund. It allowed for a clear display of specific aspects of the business conducted in both legal forms, indicating which of the requirements are less inconvenient for managers and investors.

Moreover, it should be concluded, that the majority of alternative investment company managers currently registered in Poland are either venture capital fund managers (externally managing the alternative investment company) or entities that themselves conduct venture capital activities (internally managing the alternative investment company). In addition, this state of affairs works also in the opposite direction, i.e. most venture capital funds currently operating in Poland operate in the form of an alternative

investment company. Empirical study of alternative investment companies entered into the register kept by Polish Financial Supervision Authority, as well as venture capital funds functioning in Poland in other legal forms, proved extremely helpful to emphasize the thesis stated above.

Apart from the above, the scope of the definition of an alternative investment company adopted by the Polish legislator in the Act on investment funds and management of alternative investment funds is wide enough to cover all types of activities intended by the legislator, and at the same time, narrow enough not to unreasonably include in these regulations all other small investors. An analysis of the conditions for qualifying the entity as an alternative investment company leads to such a conclusion. In the context of the implementation of the AIFM Directive into the Polish legal system, it should be mentioned that it truly deserves an approval. Its impact on the overall functioning of the capital market in Poland appears to be definitely positive. Consequently, to state that the introduction of the possibility of conducting the title activity in the form of an alternative investment company has facilitated the functioning of many business entities, including in particular venture capital funds, it should be added that the impact that the amendment of Act on investment funds has had an undoubtedly beneficial impact on the capital market regulations in Poland. One of the basic effects of this change is the increase in public confidence in joint investment institutions as a result of including them in the scope of entities supervised by the Polish Financial Supervision Authority. It is worth mentioning that before the implementation of the AIFM Directive into the Polish legal order, venture capital funds conducted venture capital investments either in the form of closed-end investment funds or in the form of non-regulated commercial law companies.

In the scope of the definition of the alternative investment company, all entities that may generate systemic risk signaled by the European, as well as Polish legislator have been included, which should therefore be considered as meeting the primary objective of these regulations. It is worth bearing in mind, that for fulfilling by a given entity the definition of an alternative investment company, it is necessary for it to meet all the conditions that constitute it. It has been broadly emphasized, including by the European Commission. At the same time, the alternative investment company should be considered an investment vehicle designed for

professional investors, mainly institutional, who have knowledge and experience in the field of functioning of capital market. This has also been confirmed by the Polish Financial Supervision Authority, which stated that the managers of alternative investment companies are supervised in a very limited way and the entities entered into the investment company managers' register do not have reporting obligations enabling Polish Financial Supervision Authority to exercise ongoing supervision over the way they conduct their business activities. From the perspective of venture capital funds, this is therefore a definitely beneficial legal form that will probably be used in Poland to an increasingly wide extent.

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