THE ASSET MANAGEMENT REVIEW

EIGHTH EDITION

Editor
Paul Dickson

THE LAWREVIEWS

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PREFACE

Despite significant improvements in the global economic landscape in the years since the global financial crisis some ten years ago, the macroeconomic position is looking increasingly complex and global growth has been hampered by various geopolitical factors, including political uncertainty and the rise of populist movements in Europe. As the UK prepares for Brexit, absent any agreement to the contrary currently set to take place at the end of October 2019, political uncertainty remains around the form and extent of any UK–EU deal relating to financial services, and as to whether any transition period (during which UK firms would remain able to access to EU markets on current terms) will be agreed. This has had, and is likely to continue to have, a potentially destabilising effect on the UK asset management sector and its clients. The impact of the UK's decision to leave the EU is thus already being felt, not only in the UK and across the European continent, but also more widely.

Nevertheless, the importance of the asset management industry continues to grow. Nowhere is this truer than in the context of pensions, as the global population becomes larger, older and richer, and government initiatives to encourage independent pension provision continue. Both industry bodies and legislators are also increasingly interested in pursuing environmental, social and governance (ESG) goals through private sector finance. For example, the European Commission has proposed a package of measures seeking to introduce sustainable finance into current regulations to make it easier for investors to identify and invest in such projects.

This should not be a surprise: lack of shareholder engagement has been identified as one of the key issues contributing to the governance shortcomings during the financial crisis. Given the importance of the asset management industry in investing vast amounts on behalf of clients, the sector is the natural focus of regulatory and governmental initiatives to promote effective stewardship and take the lead in instilling a corporate cultural focus on sustainability and ESG initiatives.

The activities of the financial services industry remain squarely in the public and regulatory eye, and the consequences of this focus are manifest in ongoing regulatory attention around the globe. Regulators are continuing to seek to address perceived systemic risks and preserve market stability through regulation. In Europe, further significant changes to the regulatory landscape for investment services were introduced by the revised Markets in Financial Instruments Directive regime (known as MiFID II), which has applied since 3 January 2018. In the UK, the Financial Conduct Authority continues to focus on the asset management industry. In 2017, it published its asset management market study on the performance of the asset management market for retail and institutional investors, and is beginning to implement its findings during the course of 2018. In contrast, the Trump administration in the US has signalled a deregulatory agenda, which includes plans to

repeal the Wall Street Reform and Consumer Protection Act of 2010 (also known as the Dodd-Frank Act).

It is not only regulators who continue to place additional demands on the financial services industry in the wake of the financial crisis: the need to rebuild trust has led investors to call for greater transparency around investments and risk management from those managing their funds. Senior managers at investment firms are, through changes to regulatory requirements and expectations as to firm culture, increasingly being seen as individually accountable within their spheres of responsibility. Industry bodies have also noted further moves away from active management into passive strategies, illustrating the ongoing pressure on management costs. This may, in itself, be storing up issues for years to come.

The rise of fintech and other technological developments, including cryptocurrencies, data analytics and automated (or 'robo') advice services, is also starting to have an impact on the sector, with asset managers looking to invest in new technologies, seeking strategies to minimise disruption by new entrants, or both. While regulators are open to the development of fintech in the asset management sector, they also want to ensure that consumers do not suffer harm as a consequence of innovations. Regulators across various jurisdictions are working together to develop a global sandbox in which firms can test their new technologies.

This continues to be a period of change and uncertainty for the asset management industry, as funds and managers act to comply with regulatory developments and investor requirements, and adapt to the changing geopolitical landscape. Although the challenges of regulatory scrutiny and difficult market conditions remain, a return of risk appetite has also evidenced itself and the global value of assets under management continues to increase year on year. The industry is not in the clear but, prone as it is to innovation and ingenuity, it seems well placed to navigate this challenging and rapidly shifting environment.

The publication of the eighth edition of *The Asset Management Review* is a significant achievement, which would not have been possible without the involvement of the many lawyers and law firms who have contributed their time, knowledge and experience to the book. I would also like to thank the team at Law Business Research for all their efforts in bringing this edition into being.

The world of asset management is increasingly complex, but it is hoped that this edition of *The Asset Management Review* will be a useful and practical companion as we face the challenges and opportunities of the coming year.

Paul Dickson
Slaughter and May
London
August 2019

Chapter 15

NORWAY

Peter Hammerich and Markus Heistad[1]

I OVERVIEW OF RECENT ACTIVITY

The Norwegian asset management industry is, as other parts of the Norwegian economy, interconnected with the Norwegian oil and oil services industry, as well as a state active in the financial markets. The state has substantial net financial assets in its sovereign investment fund, the Petroleum Fund, with a current value of over approximately 9 trillion kroner (see Section VI.v). This is, at least partly, because of income from oil and gas extraction, and the high level of activity related to this sector for several years until 2015. The Petroleum Fund does not invest in the Norwegian economy, but the economic growth spurred by the oil and gas sector benefits the mainland economy as a whole, making Norway (relative to its size) an attractive investor market for both foreign and domestic asset managers. However, with a combination of an open market for foreign actors and a less developed legal framework for Norwegian asset managers, the Norwegian asset management industry has only partially been able to capitalise on a strong domestic market to make significant forays into other investor markets.

The abrupt and relatively large drop in crude prices that started at the end of 2014 has had its effects felt in the Norwegian 'real' economy. In 2016, for the first time since the inception of the Petroleum Fund, more money was transferred out of the Fund (for public spending) than into it (petroleum-derived income), and this was also the case in 2017. Oil exploration was reduced (with a number of fields proving unsustainable under current oil prices) and activity in the oil services industry, where several companies are private equity-owned, was severely reduced. This development brought with it reduced investment activity by private equity funds with respect to oil and gas. Since 2016, however, crude prices have risen from the low thirties to the high seventies per barrel. This has led to resumed activity in the sector and several large deals and, in 2018, more money was deposited to the Petroleum Fund than transferred out.

After record fundraising levels in 2016, totalling 17 billion kroner over nine funds,[2] the level of fundraising decreased in 2017 to a total of 899 million kroner before increasing again to 4.5 billion kroner in 2018. As Norway is a small market and the number of Norwegian managers of private funds is relatively low, there are generally large variations year on year. Both 2017 and 2018 saw a decrease in investment activity by Norwegian private equity firms

1 Peter Hammerich is a partner and Markus Heistad is an attorney at Advokatfirmaet BAHR AS.

2 Norwegian Venture Capital Association.

with 8.5 billion kroner and 8.1 billion kroner respectively, compared to the highest ever recorded investment activity by Norwegian private equity firms with 11.7 billion kroner in 2016.

At the end of 2019, there were 29 authorised mutual fund management companies and 423 mutual funds established and registered in Norway. The Norwegian mutual funds market is, however, dominated by a small number of large managers, such as the major banks and credit institutions present in Norway (e.g., DNB, KLP and Nordea). The previously independent management company Skagen was acquired by insurance group Storebrand in 2017, meaning that the market is largely divided between these four, together representing approximately 75 per cent of total assets under management. Total assets under management by Norwegian mutual fund managers amounted to 1.140 trillion kroner at the end of 2018.[3] 2018 marked a slight increase from 1.138 trillion kroner at year-end 2017. The timid results reflect a volatile stock market throughout 2018.

No new hedge funds managed by Norwegian managers have been established since the Incentive Active Value Fund was launched in 2014, managed by Incentive AS under Sector Asset Management AS' umbrella. This may be related to the international trend of investors generally reducing their allocation to hedge funds. As Norwegian insurers now are under the Solvency II freedom of investment rules, as are Norwegian pension funds (as of 1 January 2019), the marketability of such products may increase as such investors are searching for better returns, provided managers are capable of offering sufficient reporting facilities for regulated clients to perform a 'look-through' to the underlying investments.

Unregulated funds make up a significant portion of collective investments in Norway in both the retail and professional markets. This is particularly the case within real estate investments, which is an important asset category in both the institutional and retail investor markets. For such funds, few official or public figures currently exist. With the implementation of the Alternative Investment Fund Managers Directive (AIFMD)[4] and reporting requirements for all Norwegian alternative investment fund managers (AIFMs), statistics have become available, creating a more transparent fund landscape across different segments. At the end of 2018, a total of 39 managers were authorised as AIFMs (including managers of regulated mutual funds that are AIFs) by the Financial Supervisory Authority of Norway (FSAN). A total of 99 AIFMs were registered and 351 alternative investment funds established in Norway (including regulated mutual funds that are AIFs) were registered. Although no official statistics exist, the number of real estate funds has been reduced over the past couple of years, due mainly to developments in the credit and real property markets.

Assets under management by Norwegian investment firms offering (individual) portfolio management amounted to 92 billion kroner at the end of 2018, compared to 106 billion kroner at the end of 2017.[5] This previous reduction was primarily caused by regulatory changes, as the largest Norwegian investment firms providing portfolio management have been consolidated into asset management companies and regulated as either undertakings for collective investment in transferable securities (UCITS) management

3 Norwegian Fund and Asset Management Association, Statistics Norway.

4 Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Fund Managers.

5 FSAN statistics.

companies or AIFMs providing individual portfolio management as an ancillary service.[6] The continued reduction into 2018 may indicate that smaller asset managers are losing ground to the larger bank-integrated investment managers.

II GENERAL INTRODUCTION TO THE REGULATORY FRAMEWORK

Norway is a Member State of the European Economic Area (EEA). As such, the main body of legislation regulating asset management (whether as part collective investment schemes or insurance companies and pension funds) consists of EU legislation implemented in Norwegian law.

Since the entry into force of the EEA Agreement in 1994, Norway has generally implemented EU legislation with great assiduity, and often chosen stricter regulation where possible. This changed significantly following the establishment of the EU system of financial supervision in 2011. The EU supervisory organisations, the European Banking Authority, the European Securities and Markets Authority, the European Insurance and the Occupational Pensions Authority, hold competences that are partly supranational. These run afoul of the principle of the EEA Agreement, whereby no sovereignty shall be relinquished by the EEA Member States, and which was an important issue for Norwegian authorities when entering into the EEA Agreement (after EU membership was rejected by referendum in 1994, for the second time).

The European Free Trade Association and the EU did not reach an agreement concerning the incorporation of the EU Regulations establishing the European Supervisory Authorities into the EEA Agreement and integration into the EU system of financial supervision before 14 October 2014.[7] The Agreement was approved by the Parliament in June 2016, but EU financial regulations passed since 2015 largely continue to see delays in being incorporated into the EEA agreement (see Section V).

The following is restricted to Norwegian law, and where stated, Norwegian regulation of foreign entities' activity in Norway on a cross-border basis.

Collective investment schemes are both regulated and unregulated under Norwegian law (at the fund level). From a regulatory point of view, a distinction can be made between three types of collective investment schemes: mutual funds that are UCITS funds,[8] non-UCITS mutual funds and other collective investment schemes. Norwegian law will reflect the additional EU fund types as European venture capital funds (EuVECAs), European social entrepreneurship funds (EuSEFs), European long-term investment funds (ELTIFs), and money market fund regulations are incorporated into the EEA Agreement and implemented in Norwegian law.

UCITS funds and non-UCITS mutual funds fall within the scope of the Norwegian Investment Fund Act (IF Act). Such funds may (if established in Norway) only be organised, managed and marketed according to the rules of the IF Act (and appurtenant regulations). Whether a collective investment scheme is a mutual fund falling within the scope of the IF

6 FSAN.

7 www.efta.int/about-efta/news/eea-efta-and-eu-ministers-reach-agreement-european-supervisory-authorities-3211.

8 Mutual funds complying with Norwegian rules implementing EEA rules corresponding to Directive 2009/65/EC of the European Parliament and of the Council of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to UCITS.

Act (or rather an unregulated alternative investment fund) must be assessed on a case-by-case basis. As a general rule, all open-ended funds investing in financial instruments[9] and bank deposits fall within the scope of the IF Act. Managers of non-UCITS mutual funds exceeding the threshold values of the AIFMD (€100 million under management) are regulated by the Norwegian Alternative Investment Fund Manager Act (AIF Act), implementing the AIFMD, meaning that such managers must be authorised AIFMs and comply with the AIF Act. Sub-threshold managers may 'opt in' to benefit, in the future, from the marketing provisions of the AIF Act in other EEA jurisdictions.

Currently, several categories of investment funds (at the fund level) are unregulated in Norway (all types of funds other than mutual funds regulated under the IF Act). Closed-ended funds and open-ended funds investing in asset classes other than financial instruments and bank deposits (e.g., real property, commodities (directly and not in derivatives)), generally fall outside the scope of the IF Act. Such collective investment schemes are unregulated in Norway. Following the entry into force of the AIF Act on 1 July 2014, the management and marketing of shares in such funds are regulated under the AIF Act.

The AIF Act and the implementation of the AIFMD in Norway are to a large extent based on a copy out approach, with little to no 'gold-plating'. Norway has implemented the AIFMD thresholds, allowing for light-touch regulation of asset managers of smaller funds that are not mutual funds (in simple terms, less than €500 million for closed-ended funds and less than €100 million for open-ended funds). Managers of sub-threshold funds may 'opt in' to benefit from the marketing provisions of the AIF Act. Management of Norwegian unregulated funds by managers falling below the threshold values of the AIFMD and that are established in Norway will remain unregulated (although the manager will have to register with the regulator, the FSAN).

The AIF Act and its marketing rules have had a substantial impact in the Norwegian market. While marketing of unregulated funds previously could be made without specific restrictions (other than prospectus rules, rules concerning investment services and general marketing law), the AIF Act introduced common marketing rules for all types of alternative investment funds (both those falling within and outside the scope of the IF Act). The FSAN has focused on monitoring marketing carried out by sub-threshold managers, as such managers no longer may market to non-professional investors (without opting in), and in particular reliance upon reverse solicitation practices.

The marketing rules are dependent upon the jurisdiction of the manager and the fund. Norway has implemented the 'private placement' provisions of the AIFMD with respect to funds and managers established outside the EEA. On this point, however, the rules are somewhat more strict than under the AIFMD, as they require prior authorisation from the FSAN to market, rather than relying on notification. In addition, for fund managers established outside the EEA, there is a requirement that they are registered with a competent authority and subject to prudential supervision in their home state for the purposes of asset management. If the interests issued by unregulated investment funds are financial instruments (shares), then services related to such shares (such as arrangement services or second-hand share sales) constitute investment services that fall within the scope of the Securities Trading Act (ST Act). There is a relatively large number of funds authorised for marketing in Norway under these rules. A revised ST Act, implementing the substantive rules of MiFID II entered

9 As defined in Directive 2004/39/EC of the European Parliament and of the Council of 21 April 2004 on Markets in Financial Instruments, implemented in the Norwegian Securities Trading Act.

into force on 1 January 2019 (see Section V). In addition, the offer of such shares may trigger a requirement to publish a prospectus under the public offering rules of the ST Act, unless an appropriate exemption is available. Shares in limited partnerships are not viewed as financial instruments (transferable securities) under Norwegian law, meaning that prospectus requirements do not apply to offerings of interests in such funds. No change has been made to this through the implementation of MiFID II. Rules implementing the Prospectus Regulation have recently been adopted and are expected to enter into force shortly.

Provision of investment services as a regular occupation (i.e., not in an incidental manner) related to limited partnership interests requires a corresponding licence under the ST Act (alternatively for foreign firms, a passport for providing such services in Norway). A licence is not required when services are provided in relation to interests with a minimum commitment of 5 million kroner (or the equivalent in another currency), or if the client is a professional client as defined in MiFID Annex II Section I (per se professional clients and not elective professional clients). The purpose of this requirement was to regulate retail sales of closed-ended funds after what has been perceived as mis-selling of shares in such funds to retail clients, especially with respect to closed-ended real property funds, feeder funds of private equity funds or fund of funds in such categories. After the entry in effect of the AIF Act, this is largely regulated by the marketing rules of that Act (with respect to the primary market), and the FSAN has recently announced change of practice to regulate a wider array of collective investments under the AIF Act (see Section VI.v).

Individual portfolio management is an investment service under the ST Act, and subject to the rules and appurtenant regulations of the ST Act. Only investment firms and credit institutions authorised under the ST Act, management companies for mutual funds or AIFMs authorised to provide portfolio management (as an ancillary service) may provide individual portfolio management services.

Activity falling within the scope of the IF Act, the AIF Act and the ST Act is under the supervision of the FSAN.

Asset management carried out by insurance companies and pension funds is regulated through the insurance company legislation and under the supervision of the FSAN. Norway has implemented the Solvency II capital adequacy rules for insurance companies with effect from 1 January 2016 (on a 'lookalike' basis: see Section V). The main rule applicable to their asset management is the prudent person principle. This requirement concerns both the investment process and the placements themselves. Pension funds are are, as of 1 January 2019, subject to a risk-sensitive capital requirement under freedom of investment based on a Solvency II 'light'.

III COMMON ASSET MANAGEMENT STRUCTURES

As mentioned in Section II, collective investment schemes established in Norway either fall within the IF Act, or outside specific regulation (at the fund level).

Funds that are regulated under the IF Act are required to be organised as contractual (rather than corporate) mutual funds under that Act. This is a specific form of organisation that, as a general observation, implies a high degree of connectedness between the management company and the funds managed by such company. For example, shareholders in the funds are entitled to elect a number of members of the board of the management company (and the management company obliged to appoint such board members). The fund has a legal personality, but all dispositions shall be taken by the management company.

Norwegian company law is generally not adapted to organise open-ended fund structures, as Norwegian limited company law does not allow for limited companies with variable capital. Unregulated (closed-ended) funds are almost without exception organised as corporate structures (private limited companies), partnerships or silent limited partnerships. In recent years, some fintech actors have begun structuring crowdfunding vehicles as cooperatives, because shares in cooperatives may be marketed and sold without restriction under the prospectus rules or the ST Act.

Before June 2010, Norwegian legislation did not allow for the establishment of hedge funds in Norway. Pursuant to an amendment of the IF Act enacted in 2010, such funds may be established and marketed under the IF Act. Because of this legislation having entered into effect relatively recently, many Norwegian promoters of hedge funds have traditionally chosen to establish funds in other fund jurisdictions, such as Ireland, Luxembourg or Malta. Such funds have been, and continue to be, managed by Norwegian teams under delegation arrangements with self-managed corporate fund structures (plc or SICAV). Such managers were previously subject to the ST Act, and required to be authorised as an investment firm providing the investment service of portfolio management. Following the entry into effect of the AIF Act, such managers will typically (depending on the organisation of the relevant fund structure) be required to be authorised under the AIFMD as an alternative investment fund manager.

No changes have been made to the IF Act with the implementation of the AIFMD (except certain changes to the marketing rules). Nor has any new fund legislation been proposed or passed. Norway therefore lacks appropriate legislation (or infrastructure) to be an attractive jurisdiction for fund establishment, compared to other jurisdictions. The Ministry of Finance is currently in the process of implementing the regulations underpinning EuVECAs, EuSEFs and ELTIFs. These EU regulations will represent wholly new types of regulated investment vehicles in Norwegian law. Due to the delay in incorporating these regulations into the EEA Agreement, such rules will likely not enter into force until 2020.

Authorised AIFMs are required to appoint a depositary to their funds. This includes unregulated funds not previously subject to such a requirement. Although there is a limited number of available service providers in this segment in Norway, this has not proven to be a bottleneck for the establishment of new funds.

Since the entry into force of a new Act on Financial Undertakings and Financial Groups on 1 January 2016, Norwegian law no longer allows for the establishment of securitisation vehicles, and securitisation outside covered bonds is generally not possible on suitable terms. It is expected that Norway will implement any EU securitisation rules if and when they are proposed as part of the Capital Markets Union initiative. Whether there will be a delay in implementation of such rules, as with other financial regulations these past few years, remains to be seen. Rules governing synthetic securitisation will be implemented upon incorporation of the Capital Requirements Regulation into the EEA Agreement and full transposition of the regulation into Norwegian law.

Individual portfolio management is mainly restricted to institutional clients (pension funds) and high-net-worth investors through private banking offerings. The structuring of investments will typically be bespoke and adapted to the client at hand.

In the retail segment of asset management, significant amounts are invested through unit-linked insurance policies. Several Norwegian insurance companies offer unit-linked life insurance, which offers policyholders the opportunity to invest in a number of assets (although mainly mutual funds and listed instruments) as underlying in a unit-linked

insurance contract. Tax rules make holding investments through a unit-linked insurance policy more favourable (for private individuals) compared to holding such investments directly or through mutual funds. Insurers generally provide web-based tools for investors to monitor and make changes to their portfolio, without triggering taxation. The government has enacted changes to the applicable tax rules to avoid different tax treatment of what – in substance – are similar-type investment products which require that the relevant unit link policy has a larger insurance element. Whereas previously the contracts promised a 101 per cent payout upon an insurance event, the new rules require a payout of 150 per cent for the insurance policy to qualify. In this context, the Ministry of Finance also adopted rules for an 'equities savings account', which is a specific tax treatment of securities accounts of private individuals containing only equity instruments and equities mutual funds. This provides more favourable tax treatment for investments in such asset classes than direct investment. Investments are made directly in the name of the investors (as is the case for individual portfolio management), and may be offered by credit institutions, investment firms and management companies for mutual funds.

IV MAIN SOURCES OF INVESTMENT

Sources of investment into managed investment products may be divided in several categories, but the main distinction is between retail investors and professional and institutional investors. High-net-worth individuals and family offices will often be a residual category, where the size of the portfolio will be the main differentiator. One key trend, only recently reversed, has been a decline in funds stemming (directly) from retail investors. Indirect investments from such clients have, however, continued to grow as defined contribution pension schemes (rather than defined benefit) have become the norm for all employees.

Through various investment companies and schemes, the government is also a sizeable investor in the Norwegian financial markets in listed securities, private equity and the venture and seed segment (see Section VI.v).

It is worth noting that the government is also a heavy investor in Norwegian private equity funds (e.g., through the government-owned investment company Argentum Fondsinvesteringer AS and its affiliates). The government has established a seed fund initiative through Innovasjon Norge (a government-funded initiative for the development of Norwegian businesses). Alliance Venture Spring and ProVenture Management have been appointed as the managers for the new seed funds. Each fund will have commitments equal to approximately 500 million kroner, of which 50 per cent will be subscribed by the government.

With regard to Norwegian mutual funds, the majority of assets under management stem from Norwegian institutional clients (representing 626 billion kroner at the end of 2018, compared to 631 billion kroner the previous year, and 564 billion kroner the year before that).[10] At the end of 2018, Norwegian retail investors held 420 billion kroner (including holdings through pension savings schemes where the client elects underlying, compared to 398 billion kroner the year before and 316 billion kroner in 2016), while foreign investors (all categories) at the end of 2018 held 117 billion kroner of assets under management in

10 Norwegian Fund and Asset Management Association annual statistics for 2016, 2017 and 2018. Institutional clients are defined as all non-retail clients.

Norwegian mutual funds, compared to 109 billion kroner in 2017 and 102 billion kroner in 2016. These figures do not include mutual funds established in other states and managed by a Norwegian manager (see Section VI.iii).

One notable absence is the lack of investment in infrastructure through market-based vehicles. This may change with the implementation of the ELTIF regulation, which allows for marketing to non-professional investors. Insurance companies and pension funds were prohibited from owning more than 15 per cent of an issuer conducting business other than insurance activities. This rule has effectively prohibited life insurance companies from making appropriate investments into infrastructure, both directly and through collective investment undertakings. Following action by the EFTA surveillance authority citing the provisons of freedom of investment under Solvency II the government proposed to repeal the restriction and the amendment entered into effect on 1 January 2019. Norwegian life insurance companies and pension funds may now benefit more fully from the Solvency II infrastructure investment risk weights.

V KEY TRENDS

i Intensified competition

In general, the Norwegian economy weathered the effects of the global financial crisis without experiencing significant difficulties. This is at least partly because of Norway's income from oil and gas extraction, providing the state with significant and steady tax income. With respect to the asset management industry, the market turmoil of 2008 led to a shrinking market, and increased competition among asset managers and managers of mutual funds for the remaining market share. This was compounded by the effect of the fall in oil prices since 2014.

The fall in oil prices was a negative factor for issuers listed on the Oslo Stock Exchange, and losses typically led to mutual funds falling out of favour with retail investors in the short term. The total number of funds was reduced from 441 in 2014 to 404 at the end of 2015, illustrating a consolidation.[11] This increased since to 433, but has decreased again to 423.

Combined with generally low returns in fixed income markets, the value reductions have led to investors across all categories to be more aware of the level of fees. In the retail market, the Norwegian Consumer Council has focused on a long-time practice among Norwegian managers of mutual funds to levy success fees without implementing a high-water mark, meaning that volatility will benefit the manager and be to the detriment of investors. This practice has not been present in the institutional market, but larger investors are increasingly pushing for lower management fees for all fund types.

On the regulatory side, the FSAN has compelled both DNB Asset Management (the asset management arm of Norway's largest bank) and Nordea to take fee cuts on some of their mutual fund offerings boasting 'active management'. The FSAN found the funds to be 'closet index funds', where the fees imposed on investors did not provide the investors with any realistic chance for higher returns. The consumer organisation Forbrukerrådet has since led a class action lawsuit against DNB claiming damages on behalf of 150,000 investors. On 2 June 2017, the appellate court upheld the decision by the city court to approve the class action lawsuit (which is the first class action lawsuit in Norway) sponsored by the Norwegian

11 FSAN.

Consumer Council, which it lost in the judgment of the city court on 12 January 2018. The verdict was appealed by Forbrukerrådet, and in its judgment on 8 May 2019, the appellate court awarded damages to the relevant clients. DNB has decided to appeal to the Supreme Court.

It remains to be seen whether the regulator will take any further initiatives concerning costs and fees in collective investment schemes as has been done in other jurisdictions. Notwithstanding, the advent of the requirement to produce a key information document under the Packaged Retail and Insurance-based Investment Products (PRIIPs) Regulation (albeit in the retail market) will provide additional transparency and may favour investment in low-cost index funds. As with other EU regulations, the implementation of this Regulation is delayed, and will likely not happen before 2020.

ii Regulatory delay

As a member of the EEA, Norway is required to implement EU financial sector legislation. Norwegian authorities are currently working on the implementation of the backlog of EU financial legislation, which has been delayed by the EU financial supervisory system (see Section II). This concerns both legislation that has been implemented on a lookalike basis (such as the Capital Requirements Directive (CRD IV along with delegated acts), the European Market Infrastructure Regulation (EMIR)), MiFID II/MiFIR, and legislation that has not yet been implemented in any way (e.g., the PRIIPS Regulation, the EuVECA, EuSEF, ELTIF and MMF Regulations, and the Securities Financing Transactions Regulation).

Legislation of particular interest to the legislator has been implemented in Norwegian law on a lookalike basis (e.g., Solvency II,[12] CRD IV, the Capital Requirements Regulation and the revised Payment Services Directive). Often, this approach leads to certain discrepancies in the rules, which may be problematic in some cases.

The high level of change in EU financial legislation since the financial crisis in 2008, combined with the long-time unresolved supervisory question, have led to long delays in the implementation of several pieces of EU financial legislation in Norway.

Following the agreement concerning the EU financial supervisory system, outstanding legislation is expected to be incorporated into the EEA Agreement as soon as possible. The combined effect of more extensive EU financial sector legislation than before, and trying to 'catch up' with the EU, has put a strain on the resources of the FSAN and the Ministry of Finance. Together, this negatively affects the asset management industry and the Norwegian financial industry as a whole, which must cope with higher regulator fees and reduced service.

VI SECTORAL REGULATION

i Insurance and pensions

Norwegian insurance companies and pension funds are regulated under the Act on Insurance Activity[13] with appurtenant regulations and the Act on Financial Undertakings and Financial Groups, which contains the 'institutional' rules and capital requirements. Together, these acts implement Solvency II, including the rules concerning investment freedom and qualitative investment rules (the 'prudent person principle').

12 Directive 2009/138/EC on the taking-up and pursuit of the business of Insurance and Reinsurance.

13 Act on Insurance Activity No. 44 of 10 June 2005.

Before Solvency II, for both life and non-life companies, a maximum of 10 per cent of their total technical reserves could be invested in 'miscellaneous assets'. This category consisted of non-listed equity and fixed income investments, including loans and various collective investment vehicles that fell outside UCITS. Hence, investments in, inter alia, private equity funds, offshore funds, European or offshore domiciled hedge funds (including special funds: see below) fell into this category of investments. The new rules have not yet produced any significant changes to the asset allocation of insurers, but this may change over time.

Pension funds were, until the end of 2018, subject to Solvency I-based legislation and provisions, requiring that assets covering technical reserves are invested prudently, duly taking into account security (risk), diversification, liquidity and potential return. Further regulations contained specific quantitative investment restrictions for assets covering technical reserves. As of 1 January 2019, pension funds are subject to a Solvency II 'lite', with risk-sensitive capital requirements combined with investment freedom. The new rules are more complex than before, and while they may provide pension funds with more flexible rules to maximise returns and match their assets with their liabilities, they represent a high cost for the many small pension funds. Whether this may force a consolidation of smaller pension funds into larger entities, or an accelerated winding-down of defined benefit plans that such funds have traditionally offered, remains to be seen.

Pensions and their costs have become increasingly important subjects in public debate, in particular following the insolvency of Norwegian pension insurance company Silver Pensjonsforsikring AS, where the estate was bought by Storebrand. The bankruptcy was directly connected to obligations relating to closed pension schemes with defined benefits stemming from conversion to defined contribution schemes or where employees have left the relevant employer. Norwegian occupational pension rules were generally poorly adapted to the situation where employees have several employers throughout their career. The government has tried to remedy this with new rules on pension accounts for defined contribution schemes, whereby pension contributions are allocated to a personal account for each employee, with individual rights to transfer the account between offerors (also outside the insurer chosen by the employer).

ii Real property

There is no specific regulation of real property funds established in Norway (see Section II). Such funds typically fall outside current investment fund regulation (as they normally are closed-ended).

Norwegian real property funds are typically unlisted private limited companies, but public companies also exist.[14] The sale of shares in such companies will be subject to public offering rules, and services related to such shares (e.g., brokerage services) are investment services subject to the ST Act, unless the fund in question is established as a limited partnership.

The management and marketing of real property funds are regulated by the AIF Act. Additional requirements concerning marketing to non-professional investors, requiring that

14 See, for example, Norwegian Property ASA, listed on the Oslo Stock Exchange.

managers are authorised under the AIFMD, has led to changes in governance for funds directed at such investor categories. Specifically, management is now typically undertaken by an external and authorised manager.

iii Hedge funds

Prior to July 2010, the establishment and marketing of mutual funds that employed investment strategies similar to those used by funds regularly referred to as hedge funds were not allowed in (or into) Norway. As of 1 July 2010, amended legislation was enacted that allowed the establishment and marketing of such funds to investors qualifying as professional clients under the ST Act (both per se and elective professional clients). These rules essentially widened the scope of the IF Act to include mutual funds with investment strategies typical of hedge funds. The IF Act refers to this category of funds as special funds, and both the management and marketing of shares in such funds are regulated under the IF Act. This means that special funds are subject to regulation based on the UCITS rules, but with wide exemptions concerning investment strategies.

Special funds established in Norway may only be managed by management companies authorised under the IF Act, or foreign management companies authorised under equivalent rules in their home state. In practice, only management companies established in another EEA Member State will be eligible. Managers exceeding the threshold values of the AIF Act (€100 million or €500 million under management) must be authorised in accordance with the AIF Act (or local legislation implementing the AIFMD).

The marketing of shares in hedge funds to professional investors is (for above-threshold managers) subject to the provisions of the AIF Act. It may be noted that the FSAN has held that the marketing rules of the IF Act apply to marketing of such funds. The rules are, however, substantively similar. Different marketing rules apply depending on the jurisdiction of establishment of the fund and the AIFM.

Sub-threshold managers may market shares in hedge funds pursuant to the rules of the IF Act. This requires prior authorisation from the FSAN, and such authorisation may only be granted if, inter alia, an agreement on supervision has been entered into between Norway and the home state of the manager of the foreign special fund, and the foreign special fund and its manager are subject to home state regulation that grants investors in Norway protection at least on par with that offered by the IF Act. In practice, authorisation may only be obtained if the manager is subject to AIFM-level regulation.

iv Private equity

There is no specific regulation of private equity funds in Norway (see Section II). Such funds typically fall outside the current fund regulation (as they normally are closed-ended). However, the management and marketing of such funds is now regulated in the AIF Act.

Norwegian private equity funds have traditionally been organised according to the typical private equity fund organisation, consisting of a fund and an adviser. The fund will then be organised as a Norwegian partnership, silent limited partnership or similar foreign entity (e.g., Guernsey or Jersey limited partnership). The AIF Act, implementing the AIFMD, relies on a different system, whereby the fund is expected to have one single manager responsible for both risk management and portfolio management, the latter including taking investment decisions on behalf of the fund. This has required some adaptations for Norwegian sponsors to comply with the AIF Act, while still offering investors a model they are used to. Certain advisers have chosen to offshore their operations in order to avoid changes.

v Other sectors

Other than what has been described above, there is no other general regulation of asset management activity in Norway, with the exception of individual portfolio management, which is an investment service subject to the ST Act. With the implementation of the AIFMD, one relatively common investment product has received added regulatory scrutiny, namely project finance or syndicated projects.

Project finance has been a traditional product in the Norwegian investment market, attracting investors to invest in special purpose vehicles holding typically one or a few capital-intensive assets, often called single asset funds. The management and marketing of funds not falling within the IF Act had been unregulated in Norway prior to the advent of the AIF Act. Consequently, there have been few regulatory concerns. In May 2019, the FSAN issued a circular in which it clarified that it considered most typical project finance and syndicated investments to fall within the definition of an 'alternative investment fund'. This means that the special purpose vehicle must appoint a manager that is either registered or authorised. Further, marketing of alternative investment funds to non-professional investors may only be done with prior authorisation from the FSAN. This may produce a decrease in products offered in the retail segment until the relevant actors have obtained the necessary approvals and completed any reorganisations that may be required. FSAN scrutiny may also mean that some products with inappropriate risk-reward profiles are denied marketing authorisation.

The Government Pension Fund Global: the Petroleum Fund

The Petroleum Fund is a sovereign wealth fund established on the basis of a special act.[15] As such, it is not a fund in the traditional sense, but a body of assets owned by the government and deposited in an account with the Central Bank of Norway. Further, it is not a pension fund in the traditional sense; it is not liable to earmarked payments, but is rather a tool for government savings and value preservation.

There is broad political consensus concerning an 'action rule' on the use of the state's income from oil extraction. This action rule sets out that the annual use of funds from such income shall not exceed an estimated return on the investment of the fund. For several years this has been set to 4 per cent of the value of the fund, but was lowered to 3 per cent in 2017, as returns over time have been lower than 4 per cent. The object of the action rule is to avoid macroeconomic stress and inflation in Norway as a result of excess public spending. Although a political majority may choose to reorganise or liquidate the Petroleum Fund in part or in whole, the curbed spending of income from oil and the current organisational model of placing the state's income from oil extraction in the Fund are subject to broad political consensus.

The management of the Fund is delegated to the Ministry of Finance, which has in turn delegated its duties to the Central Bank via a regulation.[16] The Fund is managed by a department of the Central Bank called Norges Bank Investment Management (NBIM). On 23 June 2017, a working group headed by a former chair of the Central Bank delivered its report assessing the Central Bank Act and the organisation of the management of the Petroleum Fund. The working group proposed spinning off NBIM into a separate company

15 Act No. 123 of 21 December 2005 on the Government Pension Fund.

16 Regulation No. 1414 of 8 November 2010.

(to be wholly owned by the government) in order to separate the Central Bank from the management of the Petroleum Fund. The government, however, chose not to propose any substantive changes to the current model, whereby the management of the fund is carried out by an internal departement. The question of the governance and supervision of the Fund are also likely to be a question going forward, irrespective of whether the Fund should grow (by deposits or profits), or decrease (through consumption or in particular underperformance).

The Ministry of Finance has appointed a strategy council to advise on the investment strategy of the Fund. Further, the Ministry has adopted ethical guidelines for the Fund, and an ethics council has been appointed.

The investment mandate of the Petroleum Fund has been under continuous development. In December 2014, a committee appointed by the Ministry of Finance delivered a report concerning exclusion of oil and coal extraction from the investment universe of the Fund as a tool to combat climate change. This has also been linked to the more prosaic concern of delinking the Fund from exposure to the oil extraction industry, towards which the Norwegian economy is already broadly exposed. An expert committee proposed to exclude such shares in upstream companies from the investment universe of the Fund. This report is currently subject to a public consultation. In April 2016, the Ministry slightly changed the allocation of the fund to increase the maximum exposure to real estate (to 7 per cent). At the same time, the Ministry concluded that the investment universe should not be expanded to investments in infrastructure. The Petroleum Fund is prohibited from investing in Norway.

The Government Pension Fund Norway

The Government Pension Fund Norway constitutes part of the Government Pension Fund, and is based on the same act as the Petroleum Fund.[17] As such, it is not a fund in the traditional sense, but a body of assets owned by the government that manages capital in its own name.

The mandate of the Fund is specified in a regulation.[18] The capital can be placed in equity instruments taken up to trade in regulated marketplaces in Norway, Denmark, Finland and Sweden, and in interest-bearing instruments where the issuer is resident in Norway, Denmark, Finland or Sweden, or has equity capital taken up to trade in regulated market places in those countries. The Government Pension Fund Norway owns approximately 5 per cent of the market value of the Norwegian stock market and 10 per cent of the main index on the Oslo Stock Exchange.

Argentum Fondsinvesteringer and Investinor

Argentum Fondsinvesteringer AS, an important government-owned private equity investor, has developed into a private equity actor in its own right by expanding from primary investments to co-investments with funds in which Argentum is an investor, and due to its relatively high investment activity in the secondary market. Argentum has also established investment programmes whereby other investors are invited to invest alongside Argentum. The value of its investment portfolio at the end of 2017 was 7.6 billion kroner, marking the best ever results of that company with 1.6 billion kroner in profits.

17 Op. cit. 11.

18 Regulation No. 1790 of 21 December 2010.

Investinor AS was established by the government as an investment fund to invest directly in Norwegian businesses with essentially a venture fund investment strategy, investing in the early growth and expansion stage of such businesses. Investinor is the largest investor in the Norwegian venture and expansion market, managing, as at the end of 2018, approximately 4.2 billion kroner.

VII TAX LAW

Taxation under Norwegian tax law of collective investment schemes will depend on whether the scheme is regarded as opaque or transparent for tax purposes. Mutual funds are not tax-transparent, while private equity funds are either organised as tax-transparent entities (silent partnerships or similar) or opaque entities (limited liability companies). Tax transparency implies that the fund is not a separate taxpayer, and that the investors are taxed directly on the profits of the fund.

The rules concerning taxation of mutual funds were changed with effect from the 2016 tax year. The previous rules resulted in non-Norwegian 'combination funds' (funds investing both in equities and fixed income instruments) being a tax-favourable alternative for Norwegian investors. The new rules aim at neutralising the favourable tax treatment of foreign combination funds. Under the new rules, all mutual funds shall be treated equally for Norwegian tax purposes. All types of mutual funds shall be subject to the tax exemption method, but the taxation of investors will depend on the actual allocation of a fund's portfolio of equity investments and fixed income investments. The rules imply that investors will not be subject to taxation on a running basis, but only upon distribution or realisation, or both, as under the previous rules.

With respect to taxation of Norwegian investors, the rules imply that distributions from mutual funds with an equities portion higher than 80 per cent are taxed as share distributions in full (at a rate of 0.66 per cent for corporate investors and 31.68 per cent for individual investors on distributions that exceed a tax-free allowance). Distributions from mutual funds with an equities portion lower than 20 per cent are taxed fully as interest income (at a flat rate of 22 per cent for both corporate and individual investors). Distributions from mutual funds with an equities portion between 20 and 80 per cent are divided into one part that is taxed as share distribution and one part that is taxed as interest, calculated proportionally based on the value of the fund's equities portion compared with the total value of the fund at 1 January of the relevant income year (where cash is excluded from the fund's total value). The simplified rule for determining the fund's equities portion applies correspondingly for the taxation of any gain upon realisation, however, so that only the equities portion in the year of purchase and the year of realisation is relevant.

The proportion of equity investments of a fund must be reported to the Norwegian tax authorities. Foreign funds will not have an automatic reporting obligation, but can report voluntarily. If not, the reporting obligation lies with the Norwegian investors. Failing to provide sufficient documentation implies that distributions and gains will be fully taxed as interest income.

Non-Norwegian investors in Norwegian mutual funds and private equity funds organised as opaque entities are only taxable in Norway on any distribution of dividends from the fund (Norway does not currently impose withholding tax on capital gains and

interest income). The domestic tax rate is 25 per cent, but is reduced to 15 per cent (or lower) in most tax treaties. In addition, corporate investors resident in the EU or EEA may be exempt from dividend withholding tax under specific rules.

Non-Norwegian investors in Norwegian private equity funds organised as tax-transparent entities may have tax liability in Norway for a fund's income (irrespective of whether the income of the fund is distributed to the investors or not) due to participation in a business being managed from Norway. However, for corporate investors, capital gains on shares are as a main rule tax-exempt, while dividends are as a main rule taxed at an effective rate of 0.66 per cent. The same 0.66 per cent tax rate also applies to distributions from a private equity fund to corporate investors.

Norwegian asset managers (and other financial sector undertakings) are subject to a 'financial sector tax', effective as of 2017, originally as a result of the long-standing discussion of introducing VAT on financial services.

VIII OUTLOOK

i Regulatory waiting game

The Norwegian asset management industry (and indirectly investors, both Norwegian and foreign) has been affected by the delay in implementing EU asset management and securities legislation. Tellingly, EMIR entered into force in Norway on 1 July 2017, several years later than in the EU. Neither the revised EU Transparency Directive nor the updated market abuse rules of the EU Market Abuse Regulation have been implemented or incorporated into the EEA Agreement. As the regulations concerning EuVECA, EuSEF and ELTIF funds have not yet been implemented, Norwegian fund managers have not been able to pursue these opportunities yet. As providing loans is a regulated activity in Norway, these new fund types may have a particular use under Norwegian law, providing managers with greater flexibility in their investment activity in the unlisted markets. For managers of open-ended funds investing essentially in listed markets, there is uncertainty as to the impact of MiFID II in terms of costs and benefits. The new rules on inducements under MiFID II may also affect asset managers in terms of how they distribute funds in a cost-effective manner.

For asset managers active in the retail markets the impact of the PRIIPs Regulation may introduce increased competition and cost transparency. It remains to be seen whether the increased transparency will also affect the marketability of different segment (and higher cost) funds in the retail markets, and whether this transparency will also affect the approach of institutional investors, especially smaller institutional investors that are not large enough to directly influence costs of management.

Recent government initiatives in the retail segment may lead to increased inflows into mutual funds: the rules concerning an 'equities savings account' for private individuals (see Section III) as well as rules for a new personal pension plan for private individuals with tax incentives. Increased focus on pension savings is likely to contribute to growth in these sectors. The regulator has also alluded to adopting rules for a mandatory key information document for pension products. Towards the end of 2018, approximately half of all assets in Norwegian equities mutual funds held by natural persons were held outside an equities account, and the transitional rule to transfer shares into such account has been extended by a year, to year-end 2019.

There are several underlying trends of increased use of delegation and possible offshoring among Norwegian asset management and financial services providers; necessary

software solutions are increasingly migrating to 'cloud services', and may present a better value proposition for firms. The financial sector tax will increase costs for each Norwegian employee. This may be compounded by the expected strain – and necessarily reduced responsiveness – of the Norwegian regulatory authorities, who will be required to implement a quite large backlog of EU legislation into Norwegian law. It is uncertain how the future exit of the United Kingdom from the EU will affect the Norwegian asset management industry. The traditional close relationship and extensive trade between Norway and the UK lead us to believe that Norwegian authorities will strive to achieve a solution securing free trade to the greatest extent possible.

ii Nascent comparative advantages

Recent developments may provide Norway, as an asset management jurisdiction, with some advantages compared to neighbouring jurisdictions. These developments span from the general legislative landscape to tax law and regulator scrutiny.

The authorities have for some time endeavoured to simplify company law and the administrative burden of private companies. These measures are beginning to show results, with more flexible capital rules for limited liability companies and better online tools for establishing the legal entities necessary for an asset management structure. Increasingly, Norwegian asset managers establish Norwegian structures for co-investments that foreign and foreign institutional investors have accepted. Broader investor acceptance of Norwegian structures will likely provide for easier transitioning to such structures going forward.

Further, legal certainty for private equity managers has been strengthened following decisions by Norwegian courts that carried interest shall not be taxed as personal income, and that such amounts shall also be within the scope of the tax-exemption method, provided a beneficiary is sufficiently exposed to financial risk through his or her investment.

Finally, the Norwegian regulator has been both pragmatic and focused in its supervisory action in the asset management field. Case handling times have been relatively low, with reasonable documentation requirements, the regulator seemingly having focused on products in the retail segment. We do, however, expect that the regulator will intensify its review of AML measures in the sector going forward.

Provided the Norwegian legislature is able to keep pace with the EU in terms of transposition of EU law and securing passporting rights for Norwegian actors, Norway will be advantageous from a regulatory perspective as it relies solely on EU law and avoids gold-plating or other more stringent rules.

Appendix 1

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Peter Hammerich has been the head of BAHR's asset management and private equity group since its inception in 2005. He has extensive experience within financial services and regulation and the asset management industry generally, advising domestic and international asset managers, investment banks, insurers, pension plans, funds and government-sponsored enterprises across their operations. Peter's areas of expertise include industry-wide regulations, compliance, fund formation, employment and executive compensation, pension and tax. He has for many years been recognised in independent rankings as one of the leading Nordic advisers within these fields.

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