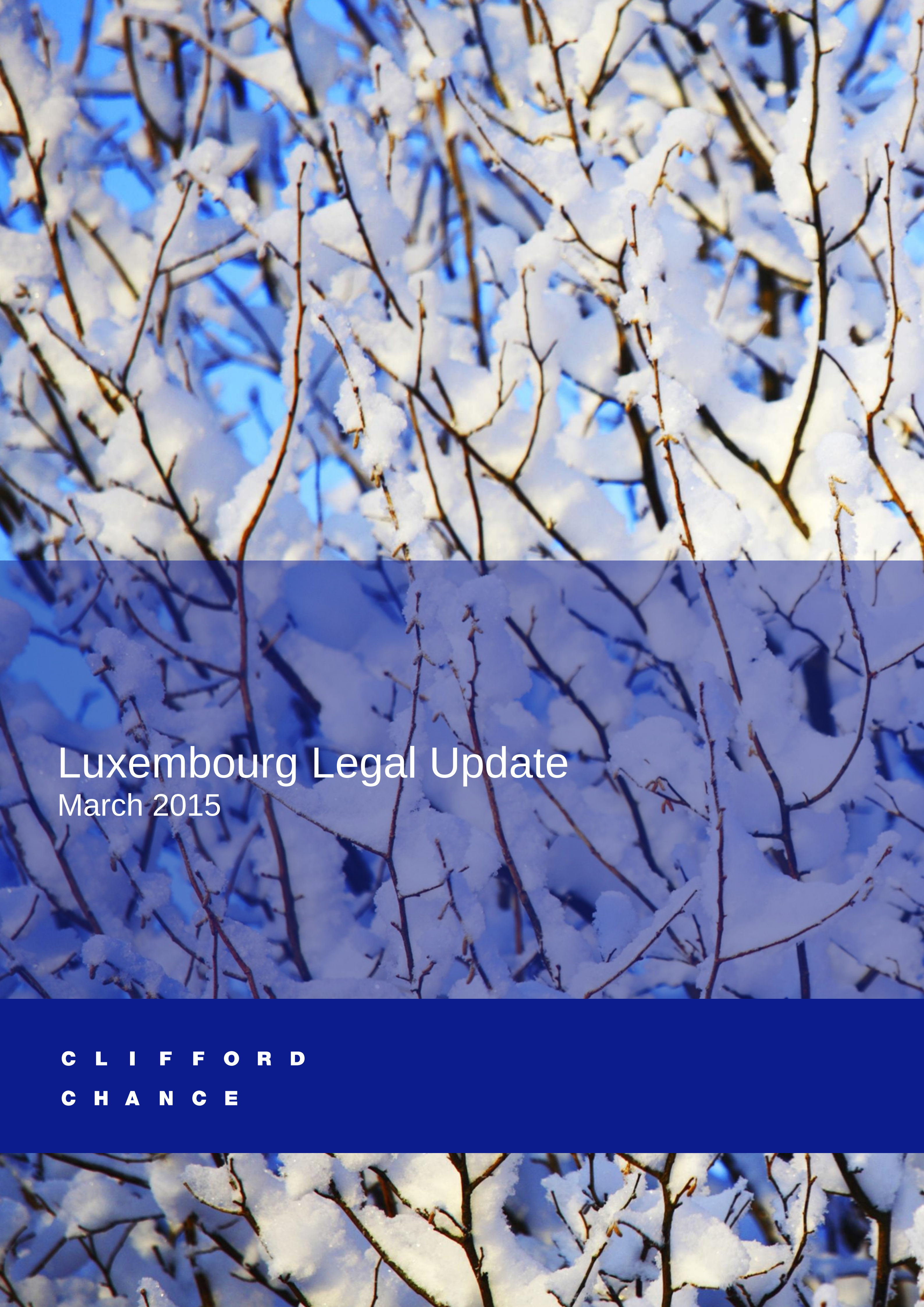

Luxembourg Legal Update

March 2015

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Contents

We are pleased to provide you with the latest edition of our Luxembourg Legal Update.

The newsletter provides a compact summary and guidance on new legal issues that could impact your business, particularly in relation to banking, finance, capital markets, corporate, litigation, employment, funds, investment management and tax law.

Banking, Finance and Capital Markets

EU Developments

Single Supervisory Mechanism (SSM): ECB Assumes Supervisory Functions

On 4 November 2014, the European Central Bank (ECB) assumed its supervisory functions under the Single Supervisory Mechanism (SSM). The ECB is now the direct supervisor for 120 significant banking groups in participating Member States, representing 82% (by assets) of the euro area banking sector. The ECB will also oversee the SSM and set and monitor supervisory standards for the supervision of the remaining 3500 banks within the SSM that are directly supervised by national competent authorities (NCAs). The ECB has re-issued its guide to banking supervision, previously published in September 2014, to coincide with the assumption of its new supervisory duties. The guide sets out:

- the ECB's supervisory principles
- the functioning of the SSM
- the conduct of supervision in the SSM, including authorisations and overall quality and planning control.

The ECB intends the guide to be a practical tool that will be updated regularly to reflect new experiences that are gained in practice.

MiFID II/MiFIR: Publication of ESMA Final Technical Advice and Consultation on Technical Standards

ESMA published on 19 December 2014 its final technical advice on the possible content of the delegated acts required by several provisions of the Markets in Financial Instruments Directive (MiFID II) and Regulation (MiFIR) following a public consultation on proposals published on 22 May 2014. The final report summarises the responses to the consultation and sets out ESMA's final technical advice, which will now be sent to the EU Commission in accordance with ESMA's mandate.

Along with the final technical advice, ESMA has also launched a consultation on draft Regulatory Technical Standards (RTS) and Implementing Technical Standards (ITS) under MiFID II/MiFIR.

The draft technical standards set out, among other things:

- a trading obligation for shares and a double volume cap mechanism for shares and equity-like instruments
- an obligation to trade derivatives on MiFID venues (regulated markets, multilateral (MTFs) or organised trading facilities (OTFs)) only
- increased transparency for trading non-equity instruments
- position limits and reporting requirements for commodity derivatives
- rules on high frequency trading
- provisions regulating access to central counterparties (CCPs), trading venues and benchmarks
- requirements for a consolidated tape of trading data.

Comments on the consultation are due by 2 March 2015.

Credit Rating Agencies (CRA) Regulation: Publication of RTS on Disclosure Requirements for Structured Finance Instruments in Official Journal

The RTS made under Article 8b of the CRA Regulation on disclosure requirements for structured finance instruments (SFIs) was published on 6 January 2015 in the Official Journal.

The RTS entered into force on 26 January 2015, but the reporting obligations apply from 1 January 2017. SFIs issued prior to 26 January 2015 or which cease to be outstanding prior to 1 January 2017 will not be subject to the reporting requirements.

Any SFI issued on or after 26 January 2015 and still outstanding on 1 January 2017 will be subject to the reporting requirements, though no backlog of information relating to the period between those two dates will need to be published. SFIs must, however, fit within one of the classes of SFI for which there is a reporting template and at least one of the issuer, originator or sponsor must be established in the EU. SFIs "of a private or bilateral nature" are also out of scope and subject to a "phase-in approach".

Reporting templates currently exist for residential mortgages, commercial mortgages, loans to SMEs, auto loans, loans to consumers, credit card loans and leases to individuals or businesses. All other asset classes are subject to the "phase-in approach" and further reporting templates may be published in future. It is not clear what grandfathering will be available for asset classes subject to the phase-in approach.

Reporting will take place on a website to be created by ESMA and the information will be accessible to the general public. Technical instructions on how to report on the website are required to be published by ESMA no later than 1 July 2016.

RTS on the periodic reporting on fees charged by CRAs and on the presentation of information CRAs make available to ESMA were also published in the Official Journal and will both apply from 26 January 2015.

PRIIPS Regulation: Publication of Regulation on Key Information Documents for Packaged Retail and Insurance-Based Investment Products (PRIIPS) in Official Journal

The Regulation on Key Information Documents for PRIIPs was published on 9 December 2014 in the Official Journal. The regulation, part of a package of measures to enhance consumer trust in financial markets, sets out to ensure that retail investors always receive the information they need to take informed decisions. In particular, key information documents should indicate:

- the nature and features of the product
- whether it is possible to lose capital
- the costs and risk profile of the product
- relevant performance information.

The regulation came into force on 29 December 2014 and will apply from 31 December 2016.

For further information, please refer to the Funds and Investment Management section of this Luxembourg Legal Update.

Other New Delegated, Implementing and other Regulations

Over the last few months, a number of other new Commission Delegated, Commission Implementing and other EU Regulations and texts have been published. These include, among others, the following:

CRD IV/CRR:

- N°1151/2014 of 4 June 2014 supplementing the Capital Requirements Directive (CRD IV) with regards to RTS on the information to be notified when exercising the right of establishment and the freedom to provide services
- N°1152/2014 of 4 June 2014 supplementing the CRD IV with regards to RTS on the identification of the geographical location of relevant credit exposures for calculating institution-specific countercyclical capital buffer rates
- N°1187/2014 of 2 October 2014 supplementing the Capital Requirements Regulation (CRR) as regards RTS for determining the overall exposure to a client or a group of connected clients in respect of transactions with underlying assets
- N°1222/2014 of 8 October 2014 supplementing the CRD IV with regards to RTS for the specification of the methodology for the identification of global systemically important institutions (G-SIIs) and for the definition of subcategories of G-SIIs
- N°2015/61 of 10 October 2014 supplementing the CRR with regards to liquidity coverage requirement for credit institutions
- N°2015/62 of 10 October 2014 amending the CRR with regards to the leverage ratio
- N°1317/2014 of 11 December 2014 on the extension of the transitional periods related to own funds requirements for exposures to central counterparties in CRR and EMIR
- Commission Implementing Decision of 12 December 2014 on the equivalence of the supervisory and regulatory requirements of certain third countries and territories for the purposes of the treatment of exposures according to CRR

- N°2015/79 of 18 December 2014 amending Implementing Regulation (EU) N°680/2014 laying down ITS with regards to supervisory reporting of institutions according to CRR as regards asset encumbrance, single data point model and validation rules.

SSM:

- ECB Regulation N°1163/2014 of 22 October 2014 on supervisory fees under the SSM.

SRM/SRB:

- Commission Delegated Regulation of 8 October 2014 on the provisional system of instalments for contributions to cover the administrative expenditures of the Single Resolution Board (SRB) under the Single Resolution Mechanism (SRM) Regulation.

Banking Union:

- EU Council Implementing Regulation 2015/81 of 19 December 2014 specifying uniform conditions of application of Regulation (EU) N°806/2014 of the European Parliament and of the Council with regards to *ex ante* contributions to the Single Resolution Fund.

BRRD:

- EBA draft RTS of 19 December 2014 on resolution planning and final guidelines on measures to reduce or remove impediments to resolvability under the BRRD.

Solvency II:

- Commission Delegated Regulation (EU) 2015/35 of 10 October 2014 supplementing the Solvency II Directive on the taking-up and pursuit of the business of insurance and reinsurance.

Short Selling:

- Commission Delegated Regulation (EU) 2015/97 of 17 October 2014 correcting Delegated Regulation (EU) N°918/2012 as regards the notification of significant net short positions in sovereign debt.

MAR/MAD 2:

- ESMA's technical advice of 3 February 2015 on possible delegated acts concerning the Market Abuse Regulation (MAR).

Legislation

Licensing and Operating Conditions for Insurance and Reinsurance Intermediaries and Insurance Sector Professionals

Grand-Ducal Regulation of 8 October 2014

A new Grand-Ducal Regulation dated 8 October 2014 on licensing and operating conditions for insurance and reinsurance intermediaries as well as professionals of the insurance sector (PSA, being certain professional service providers to insurance and reinsurance undertakings and being specifically regulated and supervised in Luxembourg) has been published in the Luxembourg official journal (*Mémorial A*).

The Regulation specifies the conditions and procedures for licence requests, professional liability insurance, change of address and licence transfers or returns with respect to (re-)insurance intermediaries as well as PSA. Furthermore, the Regulation provides for a transitional authorisation for heirs in case of death of a(n) (re-)insurance intermediary.

The Regulation is applicable from 18 October 2014 and repealed the modified Grand-Ducal Regulation of 24 November 2005 on licensing and operating conditions for insurance and reinsurance intermediaries.

Determination of Results and Distributable Reserves of Credit Institutions when Using the Fair Value Method for Statutory Accounts

CSSF Regulation N°14-02

The CSSF issued on 9 January 2015 Regulation N°14-02 with respect to the determination of results and distributable reserves of credit institutions when using the fair value method for their statutory accounts.

The Luxembourg law of 30 July 2013 reforming the commission of accounting norms and modifying *inter alia* the Law on the Register of Commerce and Annual Accounts introduced a set of new rules on determining distributable reserves in case companies use fair value valuation in their statutory accounts established in accordance with Lux GAAP (mixed regime) or IFRS.

The objective of the CSSF Regulation is to apply these rules to Luxembourg credit institutions as well. The CSSF Regulation has to be read in conjunction with CSSF Circular 08/340 and CSSF Regulation 14-01 implementing certain discretions contained in the Capital Requirements Regulation in Luxembourg. According to CSSF Circular 08/340, latent gains on certain balance sheet items valuated at fair value and included in the relevant reserve may not be distributed. According to CSSF Regulation 14-01, unrealised gains measured at fair value cannot be included in the calculation of the Common Equity Tier 1 items in the years 2014 to 2017.

The CSSF Regulation applies to accounting periods ending on 31 December 2014 and later of Luxembourg law credit institutions.

Regulatory Developments

CRR: Reporting Requirements for Credit Institutions

CSSF Circular 14/593

The CSSF published on 28 October 2014 circular 14/593 on reporting requirements applicable to credit institutions introduced or to be introduced in 2014. The circular aims to remind and inform credit institutions of recent and upcoming developments with regards to prudential reporting, including:

- prudential reporting requirements on an individual and consolidated basis in accordance with Commission Implementing Regulation (EU) N°680/2014 of 16 April 2014 laying down implementing technical standards with regards to supervisory reporting of institutions according to the CRR
- the implementation of the new reporting of financial information (FINREP) on an individual basis
- reporting tables introduced by the CSSF which are not covered by the harmonised European reporting and which remain applicable
- reporting tables supplementing Commission Implementing Regulation (EU) N°680/2014 as required by the CRR in different areas (e.g. asset encumbrance).

Furthermore, the CSSF draws the attention of institutions to its handbook on "Reporting requirements for credit institutions". The handbook is available on the CSSF's website and will be regularly updated (an automatic update notification feature is available for credit institutions). The CSSF also highlights the existence of the Q&A document on reporting requirements issued by the EBA in the context of the Single Rulebook, which is available on the CSSF's website. The CSSF announces that it will publish an additional Q&A document relating to reporting introduced by the CSSF. The CSSF moreover extends the notification threshold for large exposures on an individual basis and provides further detail on the transmission of prudential information to the CSSF in general.

Finally, the CSSF sets out a list of reporting tables and circular letters which are not applicable or repealed as of, respectively, 1 January 2014 and 1 July 2014.

Implementation of EBA Guidelines on the Applicable Notional Discount Rate for Variable Remuneration

CSSF Circular 14/594

The CSSF published on 30 October 2014 circular 14/594 implementing the EBA's guidelines on the applicable notional discount rate for variable remuneration (EBA Guidelines).

The EBA Guidelines have been issued in application of article 94(1)(g)(iii) second paragraph of the CRD IV which allows credit institutions and investment firms coming within the scope of the CRR to apply appropriate ratios between fixed and variable elements of the total remuneration of employees whose activities have a significant impact on the risk profile of the entity. The EBA Guidelines aim to explain the calculation and the application criteria of the notional discount rate.

The CRD IV leaves the choice to the Member States on whether or not to apply the notional discount rate for variable remuneration. Luxembourg has chosen to apply the notional discount rate for variable remuneration. Thus, the EBA Guidelines that entered into force on 1 June 2014 will be applicable to Luxembourg credit institutions and investment firms falling under the scope of the CRR.

Communication Regime under the SSM for Significant Entities

CSSF Circular 14/596

The CSSF published on 28 November 2014 circular 14/596 on the communication regime under the SSM for significant entities and the repeal of the VISA procedure for published annual accounts.

The circular makes banks aware of the new communication regime between significant banks and the different authorities in charge of prudential supervision after the introduction of the SSM on 4 November 2014.

Article 95 of the SSM Framework Regulation requires that all requests, notifications or applications, relating to the exercise of the tasks conferred to the ECB, shall be addressed directly to the ECB. The circular states that significant entities and their subsidiaries shall therefore send all communications to the addresses communicated to them by the ECB in August 2014. The circular further lists the exceptions to this principle under the SSM Framework Regulation for which the communication continues to take place directly between the credit institution and the CSSF (authorisations, passporting, acquisition of qualifying holdings, fit-and-proper assessments for managers, financial and prudential reporting) without prejudice to direct communication that may take place between the ECB granting the authorisations and the bank or applicant. The CSSF recommends that any communication by a significant entity is made in English.

The circular finally abolishes the VISA procedure for published annual accounts for all credit institutions (significant and less significant).

CRR: Accounting Treatment of Lump Sums and AGDL Provision for Prudential Reporting

CSSF Circular 14/599

The CSSF published on 19 December 2014 circular 14/599 on the accounting treatment of the lump sum provision and the AGDL provision in the context of prudential reporting. Both provisions are set up as a preventive measure in prosperous economic periods with the aim of using them in less favourable periods to face losses or possible insolvency situations.

The circular informs banks of the adaptation of the accounting treatment of the lump sum provision and the AGDL provision for the purposes of prudential reporting following the implementation of the CRR.

The adaptation involves the following three points:

- a technical adjustment in the FINREP reporting following the harmonisation of European reporting
- adapting the treatment of the lump sum provision with respect to own funds (*capitaux propres*)
- specifications in relation to the transition of the deposit protection scheme funded on the basis of provisions made to a deposit protection scheme funded ex ante by contributions to a fund.

Implementation of EBA Guidelines on Significant Credit Risk Transfer

CSSF Circular 15/600

The CSSF published on 7 January 2015 circular 15/600 on the implementation of the EBA's guidelines on significant credit risk transfer for traditional and synthetic securitisation transactions relating to Articles 243 and 244 of the CRR. The purpose of the guidelines is to provide clarifications on the assessment of the significant risk transfer (SRT) in accordance with Articles 243 and 244 of the CRR and to ensure harmonised assessment and treatment of SRT across all EU Member States.

The circular applies to credit institutions and investment firms which are originators of traditional or synthetic securitisations within the meaning of the CRR and requires such originator institutions to apply:

- the general requirements of the guidelines for all transactions claiming SRT under Article 243 or 244 of the CRR
- the specific requirements of the guidelines to achieve SRT to third parties in accordance with Article 243(4) or 244(4) of the CRR.

Originator institutions have to provide the CSSF or the ECB – depending on the division of competencies between both authorities under Regulation (EU) N°1024/2013 – with all information requested to enable them to assess the SRT to third parties as specified in Titles I to III of the guidelines. For such purposes, originator institutions must submit an Excel sheet named "Reporting template for originator institutions on significant risk transfer", attached to the circular, to the competent authority promptly after the initiation of the securitisation transaction.

In addition, originator institutions must notify the relevant competent authority of any securitisation for which they intend to demonstrate SRT that is not similar in structure and portfolio composition to previous transactions notified by the institution.

The circular entered into force on 7 January 2015.

CRD IV: Notification Procedure for an Increased Ratio Applicable to Remuneration Policy

CSSF Circular 15/601

The CSSF published on 14 January 2015 circular 15/601 on the notification procedure for an increased ratio applicable to the remuneration policy according to Article 94(1)(g)(ii) of the CRD IV.

The decision to increase the ratio of fixed to variable remuneration needs to be approved by the shareholders of the relevant institution, provided the global level of the variable component does not exceed 200% of the fixed component of the total remuneration.

In Luxembourg, any such approval of an increased ratio needs to be notified to the CSSF and exercised in accordance with the procedure foreseen in Article 94(1)(g)(ii) of the CRD IV. For that purpose, the CSSF has attached to the circular a draft double notification form to be completed with the information regarding the higher ratio, before being sent electronically and in a signed paper version to the CSSF. A first notification must be made to inform the CSSF of the increased ratio proposed to shareholders and a second notification must be made to inform the CSSF of the decision taken by the shareholders.

The circular and the notification obligation contained therein apply to credit institutions and investment firms as defined in Article 4(1), point 2) of the CRR.

The circular entered into force with immediate effect**.**

Documents to Be Submitted by Credit Institutions on an Annual Basis

CSSF Circular 15/602

The CSSF issued on 15 January 2015 circular 15/602 on the documents to be submitted by credit institutions on an annual basis. The CSSF reminded credit institutions that the VISA procedure for published annual accounts for all credit institutions was abolished by circular 14/596. The purpose of the circular is to set out the new practices concerning the various documents to be submitted to the regulator on an annual basis by all credit institutions established in Luxembourg.

Significant Luxembourg credit institutions must address all documents that must be submitted annually directly to the ECB and less significant Luxembourg credit institutions as well as branches of EU and non-EEA credit institutions must address all such documents to the CSSF.

The circular further reminds credit institutions of the different annual timelines for submission of the documents. Relevant documents to be submitted annually by Luxembourg credit institutions include, among others, the short form report on annual accounts, the summary reports drawn up by the internal auditors and the risk control function, the annual report of the compliance officer and the ICAAP report.

Enforcement Priorities of the 2014 Financial Information Published by Issuers of Securities Subject to the Luxembourg Transparency Law

CSSF Press Release 15/01

The CSSF issued on 8 January 2015 a press release on its enforcement plans regarding the 2014 financial information published by issuers of securities subject to the Luxembourg law of 11 January 2008 implementing the EU Transparency Directive 2004/109/EC (as amended).

The purpose of the press release is to draw the attention of issuers preparing their 2014 financial statements in accordance with International Financial Reporting Standards (IFRS) to a number of topics and issues that will be the subject of specific monitoring during the CSSF's enforcement campaign planned for 2015.

These issues mainly relate to:

- the new consolidation standards (especially IFRS 10 "Consolidated Financial Statements", IFRS 11 "Joint Arrangements"' and IFRS 12 "Disclosure of Interests in Other Entities") whose mandatory application has been effective since 1 January 2014
- the recognition and measurement of deferred tax assets under IAS 12 "Income Taxes".

These topics are also included among the priorities defined by the supervisory authorities of the European Member States and ESMA and published by ESMA on 28 October 2014.

Additionally, the CSSF has decided to focus on:

- the impairment of intangible assets according to IAS 36 "Impairment of Assets"
- the quality of information disclosed on methods and assumptions used for measuring fair value in accordance with the requirements of IFRS 13 "Fair Value Measurement"
- the relevance and completeness of the sensitivity analyses disclosed in the financial statements of issuers.

Financial Intelligence Unit Annual Report 2013

The Financial Intelligence Unit (*Cellule de Renseignement Financier*, CRF) of the State Prosecutor's office to the Luxembourg District Court published its annual report for 2013.

The document is available (only in French) at the following address: http://www.justice.public.lu/fr/publications/rapport-activites-crf/rapport-crf-2013.pdf.

The report sets out statistics on the FIU's activity during 2013 and main trends and phenomena in the area of money laundering. The report emphasises that suspicious transaction reports linked to cybercrime, in particular by hacking email accounts for the purposes of identity theft, increased significantly in 2013. Furthermore, following the introduction into Luxembourg law in 2013 of the new primary offence of abuse of weakness (*délit d'abus de faiblesse*), first suspicious transaction reports relating to such offences were submitted to the FIU in 2013.

EIOPA Guidelines on the Use of the Legal Entity Identifier

CAA Circular 14/11

The CAA issued on 17 December 2014 circular 14/11 with regards to the Guidelines issued by EIOPA on the use of the legal entity identifier (LEI).

The EIOPA Guidelines, published on 20 October 2014 and attached to the new circular, aim to establish the use of the LEI code as a unique identifier for insurance and reinsurance undertakings as well as pension funds for the purposes of:

- communicating prudential data to the supervisory authorities
- facilitating the establishment of annual reports
- improving the quality of the data to be processed by the supervisory authorities.

The CAA confirms that it will take account of the LEI code in its communication with EIOPA in accordance with EIOPA Guideline 4. The CAA also formally invites all insurance and reinsurance undertakings as well as pension funds to take all necessary measures to comply with the requirements arising from EIOPA Guidelines 1 and 2 and to request the allocation of a LEI code by the following deadlines:

- by 30 June 2015, at the latest, for insurance and reinsurance entities subject to Solvency II
- by 30 June 2016, at the latest, for all other entities (including, notably pension funds).

The LEI code is assigned by a "local operating unit" (LOU) upon specific request of the entities concerned. The request can be submitted to any LOU, whether in Luxembourg or abroad. The circular contains a web link to a list of LOUs.

Other Publications Concerning the Insurance Sector

The CAA further issued the following information notes:

- CAA information note dated 14 January 2015 on reporting requirements under the Solvency II regime
- CAA information note dated 21 January 2015 in relation to the Luxembourg law dated 28 July 2014 on the mandatory deposit and immobilisation of bearer shares and units.

Introduction of New Statistical Reporting on Renminbi-Denominated Operations

BCL Circular Letter 2015/238

The Central Bank of Luxembourg (CBL) published on 18 January 2015 circular 2015/238 introducing a new statistical reporting obligation for Luxembourg-established credit institutions with respect to renminbi-denominated operations.

In light of the memorandum of understanding between the CBL and the People's Bank of China (PBoC) on cooperation regarding the oversight, information exchange and assessment of the renminbi (CNY) market and the obligation of the CBL under the memorandum to monitor the Luxembourg renminbi market and to exchange information with the PBoC, the CBL requires an array of statistical information on the use of the renminbi in Luxembourg by both resident and non-resident counterparts. Such information essentially comprises data on loans, deposits and securities denominated in renminbi, as well as renminbi sale and purchase operations with resident and non-resident counterparties.

Rather than integrating the new reporting requirements into the existing statistical reporting framework, the new circular introduces a dedicated statistical report available on the CBL's website.

The new statistical reporting on renminbi-denominated operations must be implemented as of the reporting period June 2015.

Case Law

Pledge over Business – Priority – Confusion of Assets of Insolvent Debtor with Assets of other Insolvent Companies

Insolvency – Suspension of All Measures of Execution of Unsecured Creditors – Action in Court in View of Voiding a Contract

Securities' Deposit Contract – Proof of Orders Given by Client – Implied Ratification of Bank Statements Even in Case of Lack of Express Clause in General Conditions

Please refer to the Litigation section of this Luxembourg Legal Update for further details on the above.

Corporate and M&A

Legislation

Law of 28 July 2014

Law of 28 July 2014 on the Immobilisation of Bearer Shares and the Holding of a Register for Registered Shares and for Bearer Shares and Amending the Companies Law and the Financial Collateral Law:

The law of 28 July 2014 on the immobilisation of bearer shares, which entered into force on 18 August 2014, contains certain transitory provisions which may be of relevance for Luxembourg companies whose shares are issued under bearer form.

For a detailed presentation of the Law, we invite you to consult our client briefing on this Law, accessible at the following hyperlink.

Thus, bearer shares issued after 18 August 2014 must be deposited with a depositary fulfilling the requirements of the Law immediately upon issuance.

As regards bearer shares issued before 18 August 2014, their issuer must appoint a depositary fulfilling the requirements of the Law by 18 February 2015 and these bearer shares must be deposited with the appointed depositary by 18 February 2016.

Furthermore, voting and financial rights (such as distribution rights and rights to payment of redemption proceeds) attached to bearer shares which have not been immobilised with the depository by 18 February 2015 will automatically be suspended, respectively deferred, until they have been immobilised. Also, in case of suspension of voting rights, the relevant bearer shares will not be counted for the calculation of the quorum and of majorities during general shareholder meetings. Holders of such shares are not admitted to the general meetings.

Directive (2014/56/EU) and the Statutory Audit Regulation (537/2014)

The Directive (2014/56/EU) of the European Parliament and of the Council of 16 April 2014 amending Directive 2006/43/EC on statutory audits of annual accounts and consolidated accounts (the "**Directive**") and the Regulation (EU) N°537/2014 of the European Parliament and of the Council of 16 April 2014 on specific requirements regarding statutory audit of public-interest entities (the "**Regulation**") introduce **a prohibition of any clause restricting the choice by the general shareholders' meeting of its**

statutory auditors. It further provides that **any such existing clauses shall be null and void**.

The Directive

The Directive bans "any contractual clause restricting the choice by the general meeting of shareholders or members of the audited entity…to certain categories or lists of statutory auditors or audit firms." It further provides that "any such existing clauses shall be null and void", meaning the ban effectively has retrospective effect. Furthermore, the ban is broader than it may initially appear, because the purpose of the legislation is to avoid restrictions on the freedom of the shareholders/members to choose their own auditors freely. The result is that **any** contractual restriction on the choice of auditors is suspect and potentially null and void.

The Directive applies to any entity that is required to have a statutory audit under Union law, which will include any entity incorporated under EU law, but also most entities with transferable securities listed on regulated markets in the EU. Note that what is relevant is whether the audit is required under Union law, and **NOT whether the contract in question is governed by EU law**.

The Directive is required to be transposed into national law and the ban applied **no later than 17 June 2016**, but Member States can choose to apply it sooner. The prohibition contained in the Directive will be implemented into Luxembourg law and be of relevance at such moment.

The Regulation

The Regulation (directly applicable in member states without transposition into national law) is also relevant because it applies to a "public interest entity" or "PIE", which includes credit institutions, insurance undertakings, any entity governed by the law of a Member State with securities listed on a regulated market and any entity so designated (e.g. because of the nature of their business, their size or number of employees). In addition to a ban mirroring the one in the Directive, the Regulation requires PIEs to inform the competent authorities "without delay of any attempt by a third party to impose such a contractual clause or to otherwise improperly influence the decision of the general meeting of shareholders or members on the selection of a statutory auditor or audit firm."

The ban under the Regulation **applies from 17 June 2016**, and the requirement to report improper influence applies from 17 June 2017.

The important point is that we have a legally applicable text that renders such clauses null and void at a certain date in the future, i.e. June 2016. Therefore, if we have agreements containing such clauses today, it is an effect of the current legislation, even though that effect is postponed, that the clause will become null and void.

Bill of law

Bill N°6777 - Simplified Limited Liability Company ("S.à r.l.-S")

The Luxembourg Parliament is currently considering draft Bill N°6777 dated 2 February 2015, submitted to the Luxembourg Parliament by the Ministry of Justice, which aims to establish a simplified limited liability company by amending the Companies Law and the Law on Register of Commerce and Annual Accounts. By the establishment of this simplified form of *société à responsabilité limitée,* the government expects to boost economic growth by increasing the number of companies set-up by natural persons.

The key features of the S.à r.l.-S would be the following:

- a S.à r.l.-S would be incorporated under private seal or by way of a notarial deed
- the provisions of the Companies Law relating to the *société à responsabilité limitée* would apply unless specific provisions relating to the S.à r.l.-S apply
- only natural persons may be shareholders of a S.à r.l.-S and those natural persons cannot be shareholders of more than one S.à r.l. unless he/she has acquired shares by reason of death
- the object of the S.à r.l.-S shall be within the scope of the law of 2 September 2011 on business licenses. The provision of a business license would be a condition to be fulfilled to register a S.à r.l.-S with the RCSL
- the share capital amount shall be between EUR 1 and EUR 12,394.68 and be contributed by the shareholders by way of contribution in cash or kind. If following a capital increase the capital of the S.à r.l.-S is raised to an amount exceeding EUR 12,394.68, the provisions of the Companies Law relating to the S.à r.l.-S will no longer apply
- from the net profit of the S.à r.l.-S, five per cent would have to be deducted and allocated to a legal reserve fund. That deduction will cease to be mandatory when the amount of the legal reserve fund together with the amount of the share capital reaches EUR 12,394.68.

- only natural persons may be managers of a S.à r.l.-S.

Case Law

District Court, 8 December 2011

Loss of Half of the Corporate Capital – No Need of an Approved Balance Sheet to Ascertain the Loss – No Obligation for the Shareholders to Inject Additional Capital to Restore the Corporate Capital of the Company

Court of Appeal, 17 October 2012

Luxembourg Branch of a Belgium Company – Absence of Legal Personality – Inability to Initiate Legal Proceedings – Substantive Irregularity

Court of Appeal, 13 March 2013

Failure to Publish Annual Accounts – Offence – Rebuttable Presumption

Supreme Court, 4 July 2013

The Offence of Bankruptcy, an Instantaneous Offence – The Sole Failure to Publish Annual Accounts Constituting an Offence

Court of Appeal, 29 January 2014

Non Application of Article 495-1 of Luxembourg Commercial Code for not Keeping Regular Accounting Records and Books and not Publishing the Balance Sheets – Failure to Declare and to Pay VAT not Necessarily Constituting a Gross Negligence – the Fact not to Protest Against VAT Returns, Knowing that the Taxation Has Been Based on a Wrong Turnover, Constituting a Case of Gross Negligence – In Case Of Evidence of Gross Negligence, Presumption of Responsibility for the Whole Shortfall in Assets

Please refer to the Litigation section of this Luxembourg Legal Update for further details on the above.

Employment

Regulatory Developments

Implementation of EBA Guidelines on the Applicable Notional Discount Rate for Variable Remuneration

CSSF Circular 14/594

Please refer to the Banking, Finance and Capital Markets section of this Luxembourg Legal Update for further details on the above.

Funds and Investment Management

EU Developments

UCITS Issues

ESMA Final Report on UCITS V Delegated Acts on Depositary Regime

On 28 November 2014, ESMA issued a final report (ESMA/2014/1183) containing its technical advice to the EU Commission on possible delegated acts in the following two areas related to the depositary function under the so-called UCITS V Directive: the insolvency protection requirement and the independence requirement (Final Report).

As a reminder, the UCITS V Directive, which amends the UCITS regime to address perceived discrepancies across the EU on the duties and liability of depositaries, remuneration policy and sanctions, entered into force on 17 September 2014. The EU Member States now have 18 months, i.e. until 18 March 2016, to transpose the new directive into national law. However, UCITS management companies and self-managed UCITS are given until 18 March 2018 to appoint a depositary complying with the new UCITS V eligibility requirements if their existing depositary does not meet these requirements on 18 March 2016.

ESMA's advice as contained in the Final Report is summarised below.

Advice on UCITS V Insolvency Protection Requirement

In order to ensure that in the event of insolvency of a third party to whom safekeeping functions have been delegated by the depositary, the assets of a UCITS held in custody are not available for distribution among or realisation for the benefit of the creditors of that third party, the Final Report includes steps, measures and tasks to be undertaken by the third party, including, but not limited to, the following:

- whenever the applicable insolvency laws and jurisprudence are those of a non-EU jurisdiction, the third party shall make all reasonable efforts to verify, among others, that the applicable legal system:
  - recognises the segregation of the UCITS' assets from those of the third party (which is not located in the EU) and that of the depositary
  - recognises that the UCITS' segregated assets do not form part of the third party's estate in case of insolvency and are unavailable for distribution among or realisation for the benefit of the creditors of the third party (if the latter is not located in the EU).
- Whatever the applicable insolvency laws and jurisprudence (i.e. EU and non-EU jurisdictions), the third party shall:
  - always maintain accurate and up-to-date records and accounts of UCITS' assets that readily establish the precise nature, amount, location and ownership status of those assets
  - provide a statement to the depositary on a regular basis detailing the UCITS' assets held for or on behalf of such depositary
  - maintain appropriate arrangements to safeguard the UCITS' rights in its assets and minimise the risk of loss and misuse.

In addition to the tasks for the third party to which custody is delegated, the Final Report also proposes measures to be put in place by the depositary itself, including in particular the consideration to be paid to the following elements in the selection and appointment of the third party:

- the legal requirements or market practices related to the holding of client assets that could adversely affect the UCITS' rights during business as usual and in the event of insolvency of the third party
- the financial condition, expertise and market reputation of the third party
- the protection or lack thereof attendant upon the regulatory status of the third party.

If the third party is located outside the EU, ESMA further recommends that the depositary:

- makes all reasonable efforts to understand the material effects of the contractual provisions governing the arrangement with the third party on the UCITS' rights in respect of its assets
- in cases where the applicable legal regime does no longer recognise the segregation of the UCITS' assets in the event of insolvency of the third party or if the conditions set out under this legal regime are no longer fulfilled:
  - ensures that there are contractual provisions in its agreement with the third party which allow the termination of such agreement without undue delay and in the best interest of the UCITS and the investors
  - immediately informs the UCITS management company/self-managed UCITS of such a situation,

which shall in turn immediately notify its competent authority and consider all the appropriate measures in relation to the relevant assets of the UCITS, including their disposal by taking into account the need to act in the best interest of the UCITS and its investors.

Advice on UCITS V Independence Requirement

The UCITS V Directive requires that both the depositary and the UCITS management company/self-managed UCITS act independently in carrying out their respective functions and solely in the interests of the UCITS and its investors.

In its Final Report, ESMA has identified two types of links between the UCITS management company/self-managed UCITS and the depositary, namely:

- the common management and/or supervision
- the cross-shareholdings between these entities, which may jeopardise their independence

and recommends a combination of measures to be complied with in order to fulfil the independence requirement imposed by the UCITS V Directive.

As regards common management and/or supervision, the Final Report outlines that independence could be lost if any of the UCITS management company/self-managed UCITS and the depositary, by means of executive power or supervision, could control the action of the other entity, and suggests various means in order to ensure the separation of the management bodies of each of the UCITS management company/self-managed UCITS and the depositary. In particular, the Final Report prohibits any member of the management body of the UCITS management company/self-managed UCITS from being a member of the management body of the depositary and no member of the management body of one of these entities can be an employee of the other entity. In addition, certain restrictions will apply at the level of the members of the body in charge of the supervision of the UCITS management company/self-managed UCITS and the depositary in order to ensure their effective and impartial supervision.

As regards cross-shareholding, the Final Report determines that the UCITS management company/self-managed UCITS and the depositary may be part of the same group, and cross-shareholding of more than 10% of the capital or of the voting rights or enabling the exercise of a significant influence on the held entity are also allowed, provided reasonable steps are taken to avoid conflicts of interest and that the following arrangements are put in place by the UCITS management company/self-managed UCITS:

- demonstration to the competent authority of its home Member State that the depositary has been appointed in the sole interest of the UCITS and its investors, after comparing cost and qualitative aspects between that entity and its competitors
- disclosure to the investors of the existing link with the depositary
- justification of the choice of the depositary to investors upon request
- where the UCITS management company/self-managed UCITS and the depositary are part of the same group, ESMA requires minimum thresholds of independent members in the management bodies of these entities. These thresholds will differ depending on whether the members of the management body are in charge of supervisory functions or not. In this respect, the Final Report provides elements to assess the independence of the members of the management body of the UCITS management company/self-managed UCITS and of the depositary as well as of the members of the body in charge of the supervisory functions. For instance, they can be considered independent if they do not cumulate their mandate with additional memberships of management bodies, of bodies in charge of the supervisory functions, or with a position as employee in another entity within the group and are free of any business, family or other relationships within the group.

Next Steps

ESMA will now cooperate closely with the EU Commission in view of the transformation of its technical advice into formal delegated acts to be adopted by the EU Commission. In this respect, the EU Commission has indicated that the delegated act should be adopted by mid-2015.

ESMA Updated Q&A on ETFS and other UCITS Issues

On 9 January 2015, ESMA published an updated version of its Q&As on its guidelines on ETFs and other UCITS issues (ESMA/ 2015/12). The last updated questions clarify that:

- For the purpose of paragraph 39 of ESMA guidelines on ETFs and other UCITS issues, the counter-party to a financial derivative instrument has no discretion over the composition of the underlying assets of the financial derivative instrument. Indeed, the role of the counterparty only involves implementing a set of rules that is agreed in advance with the UCITS or its management company and does not allow the exercise of any discretion by the counterparty.

- Article 50(e)(iv) of the UCITS Directive also applies to short-term money market funds in which UCITS may reinvest cash collateral funds pursuant to paragraph 43 (j) of ESMA guidelines on ETFs and other UCITS issues, meaning that short-term money market funds should not invest more than 10% of their assets in aggregate in other money market funds.

ESMA Consultation on UCITS Share Classes

On 23 December 2014, ESMA issued a discussion paper on different share classes of UCITS (ESMA/2014/1577).

The discussion paper sets out ESMA's views on what constitutes a share class and provides possible approaches to the extent of differentiation that should be permitted between share classes. Indeed, the UCITS Directive recognises the possibility for UCITS to offer different share classes to investors but it does not prescribe whether, and to what extent, share classes of a given UCITS can differ from each other. ESMA has identified diverging national practices as to the types of share class that are permitted and sees merit in developing a common understanding of what constitutes a share class and of the other ways in which share classes may differ from each other.

ESMA will take into account feedback from stakeholders and the possible impact on current market practices when developing its final position. Comments on this discussion paper should be submitted by 27 March 2015.

Packaged Retail and Insurance-Based Investment Products

PRIIP KID Regulation Published in the Official Journal

The so-called PRIIP KID Regulation (Regulation (EU) N°1286/2014)[1] was published in the Official Journal of the EU on 9 December 2014 and entered into force on 30 December 2014. It shall apply from 31 December 2016.

As a reminder, the PRIIP KID Regulation is part of a package of measures to enhance consumer trust in financial markets and requires the provision of a KID to retail investors investing in packaged retail and insurance-based investment products (PRIIPs) in order to ensure that they always receive the basic information they need to take informed decisions. In particular, the KID shall indicate:

- the nature and features of the product
- whether it is possible to lose capital
- the costs and risk profile of the product
- relevant performance information.

To avoid uncertainty, UCITS funds will not be subject to the PRIIP KID Regulation for five years as they are already subject to the UCITS KIID under the UCITS Directive. As part of the review of the PRIIP KID Regulation, the EU Commission will assess whether the five-year transition for UCITS should be extended or not. According to the PRIIP KID Regulation, the above five-year transitional period and review should also apply to management companies, investment companies and persons selling or advising on units of non-UCITS funds when a Member State is applying rules on the format and content of the KIID document, as set out in articles 78 to 81 of the UCITS Directive. Other non-UCITS retail funds must issue a KID two years after the entry into force of the PRIIP KID Regulation, i.e. end of 2016.

Whilst the PRIIP KID Regulation sets out the overall principles, it is worth mentioning that it will be supported by detailed Level 2 and Level 3 measures in due course (see below). A review of the PRIIP KID Regulation will also be carried out by the EU Commission after four years to take

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[1] A corrigendum to the PRIIP KID Regulation has also been published in the Official Journal. It corrects the original text of the regulation by changing the deadline for the European Supervisory Authorities (ESAs) to submit RTS under article 8 to 31 March 2016.

account of market developments, such as the development of new types of PRIIPs.

For further information on the PRIIP KID Regulation, see the July 2014 edition of our Luxembourg Legal Update.

ESAs Consultation on PRIIP KID

On 17 November 2014, the Joint Committee of the European Supervisory Authorities (ESAs), comprising ESMA, EBA and EIOPA, published a discussion paper on the PRIIP KID (Discussion Paper). Said Discussion Paper is a first step in the ESAs' joint work on the broad issues to be considered in developing draft regulatory technical standards (RTS) that will contain detailed rules on the following three topics:

- content and presentation of the KID, including performance scenarios and cost disclosures
- review, revision and republication of the KID
- timing of delivery of the KID to retail investors.

Comments on the Discussion Paper were due by 17 February 2015. Now, the Joint Committee is expected to use the feedback received from stakeholders in preparing draft RTS that should be finalised and submitted to the EU Commission at the beginning of 2016, whilst the new KIDs should start being used around the end of 2016. Prior to this, however, a more technical discussion paper should be scheduled during spring of 2015, followed, after summer, by a consultation on the final RTS.

European Long-Term Investment Funds

Compromise Text of EU Parliament and Council on Proposed ELTIF Regulation

On 26 November 2014, the EU Parliament reached an agreement with the EU Council on the proposed regulation on European Long-Term Investment Funds (ELTIFs), which resulted in a compromise text finalised on 5 December 2014 (ELTIF Regulation). The EU Parliament and Council must now formally adopt the proposed ELTIF Regulation. Once adopted, the ELTIF Regulation will enter into force on the twentieth day following its publication in the Official Journal of the EU, which is expected in mid-2015. This being the case, the ELTIF Regulation will apply from six months after its entry into force, that is the end of 2015 or early 2016.

As a reminder, the objectives of the ELTIF Regulation, deposited initially by the EU Commission on 26 June 2013, are twofold. On the one hand, it is to create a legislative framework for long-term EU funds which only invest through certain qualifying assets in businesses that need money to be committed for long periods of time rather than focusing on short term capital gains, such as infrastructure and real estate projects. On the other hand, the ELTIF Regulation aims to increase the non-bank finance available for companies investing in the real economy within the EU.

To that end, a new "optional ELTIF regime" is introduced, which is some kind of hybrid between the existing institutional AIF product and the retail UCITS and PRIIP products. By definition, ELTIFs are EU AIFs that are managed by authorised EU AIFMs in accordance with the AIFM Directive. However, an EU AIFM which decides to manage an ELTIF product and to be authorised as ELTIF manager will have to comply with relatively complex requirements set out in the ELTIF Regulation in addition to the AIFM Directive requirements. These include, for example, the obligation in case of marketing to retail investors to have a depositary in accordance with the provisions of the UCITS V Directive and to produce a KID pursuant to the PRIIP KID Regulation. In exchange for complying with these rules, such EU AIFMs will benefit from an EU cross-border passport, allowing them to market their ELTIFs to all types of institutional and private investors across the EU.

Clifford Chance has prepared a briefing paper describing the main characteristics of the ELTIF Regulation. To view a copy of this briefing paper, please click here.

AIFM Directive

EU Commission Delegated Act on Information that NCAs Must Provide to ESMA

On 18 December 2014, the EU Commission adopted a delegated regulation on information that NCAs must provide to ESMA pursuant to article 67(3) of the AIFM Directive. The regulation sets out information that national competent authorities are required to report each quarter to ESMA on the AIFMs that are managing and/or marketing AIFs under their supervision, either under the application of the passport regime or under their national regimes.

ESMA Consultation on Segregation Requirements

On 1 December 2014, ESMA launched a consultation on asset segregation requirements under the AIFM Directive (ESMA 2014/1326). The consultation sets out ESMA's proposals for possible guidelines regarding the asset segregation requirements in case of delegation of safekeeping duties by the appointed depositary of an AIF.

ESMA is seeking feedback on two possible options:

- adelegated third party holding assets for multiple depositary clients would not be required to have separate accounts for the AIF assets of each of the delegating depositaries
- the account on which the AIF's assets are to be kept by the delegated third party may only comprise assets of the AIF and assets of other AIFs of the same delegating depositary. Assets of AIFs of other depositary clients would have to be kept in separate accounts.

Comments were due by 30 January 2015 and ESMA will consider the feedback with a view to finalising guidelines and publishing a final report in 2015.

ESMA Consultation on AIFMD Passport and Marketing of Non-EU AIFs by EU AIFMs in the EU

On 7 November 2014, ESMA opened a call for evidence to gather input for the opinion it must submit to the EU Commission by 22 July 2015 on:

- the functioning of the EU passport under the AIFMD
- the functioning of the marketing of non-EU AIFs by EU AIFMs in the EU and the management and/or marketing of EU and non-EU AIFs by non-EU AIFMs in the EU (ESMA/2014/1340).

Besides its opinion, ESMA must also issue advice on whether the passporting regime should be extended to the management and/or marketing of AIFs by non-EU AIFMs and to the marketing of non-EU AIFs by EU AIFMs.

ESMA will consider the feedback it receives to this call for evidence in Q1 2015 and expects to deliver the opinion and advice to the EU Commission by 22 July 2015.

ESMA Updated Q&As

On 11 November 2014 and 9 January 2015, ESMA published updated Q&As on the application of the AIFM Directive (ESMA/2015/11). The last updated questions concern the reporting obligations to national competent authorities as well as the calculation of the total value of assets under management.

EU Social Entrepreneurship Funds and EU Venture Capital Funds

ESMA Updated Q&As

On 11 November 2014, ESMA published updated Q&As on the application of the Regulation on European Social Entrepreneurship Funds (EuSEF) and the Regulation on European Venture Capital Funds (EuVECA) (ESMA/2014/1354).

The new updated Q&As essentially address the possibility for, and conditions applicable to, AIFMs above the EUR 500 million threshold of article 3(2)(b) of the AIFM Directive that manage and market EuSEFs and EuVECAs.

In particular, the Q&A clarifies that:

- The EuVECA and EuSEF designation is not exclusive to sub-threshold managers. Consequently, EuSEF and EuVECA managers that exceed the EUR 500 million threshold must be authorised as AIFMs in accordance with the AIFM Directive, but thereafter they can continue using the EuSEF and EuVECA label for the marketing of their funds as long as they comply with the requirements of the AIFMD Directive and of the EuVECA and EuSEF Regulations (as described below). From a regulatory and supervisory perspective, an authorisation under the AIFMD is more stringent than a registration under the EuVECA and EuSEF Regulation. Therefore, being authorised under the AIFM Directive should not trigger the process in article 21(1)(c) of the EuVECA Regulation and article 22(1)(c) of the EuSEF Regulation.
- Authorised AIFMs that manage and market EuVECAs and EuSEFs must comply with the requirements of the AIFM Directive and the following provisions of the two regulations: articles 3 (definitions), 5 (rules on non-qualifying assets, leverage and borrowing) and points (c) and (i) of article 13 (information to investors) of the EuVECA Regulation and articles 3 (definitions), 5 (rules on non-qualifying assets, leverage and borrowing), 10 (measurement of social impact), 13(2) and points (d), (e) and (f) of article 14(1) (information to investors) of the EuSEF Regulation.
- The type of investors that authorised AIFMs can target are:
  - investors under the AIFM Directive (i.e. MiFID professional investors plus those set out in national rules)
  - investors under the EuVECA and EuSEF Regulations (i.e. MiFID professional investors, investors aware of the risks that invest a minimum amount of EUR 100,000 and executives, directors or employees of the fund).

The Q&A further clarifies that the EuVECA and EuSEF Regulations should prevail over AIFM Directive provisions. As a result, AIFMs above the threshold of EUR 500 million of the AIFM Directive can market EuSEFs and EuVECAs to investors as defined in article 6 of the EuSEF and EuVECA Regulations.

EMIR

Please refer to the presentation made on this subject in the Banking, Finance and Capital Markets section of this Luxembourg Legal Update.

MiFID

Please refer to the presentation made on this subject in the Banking, Finance and Capital Markets section of this Luxembourg Legal Update.

Crowdfunding

ESMA Opinion and Advice on Crowdfunding

On 18 December 2014 ESMA published an opinion together with advice on investment-based crowdfunding.

The opinion clarifies the rules applicable to crowdfunding and is addressed to national competent authorities. It outlines how EU rules are likely to apply to crowdfunding platforms, depending on the business model chosen, and gives guidance on how to regulate platforms operating outside the scope of such rules.

The advice outlines issues to be considered by EU institutions with a view to achieving greater regulatory and supervisory convergences within the EU. In particular, it expresses the concern that incentives exist for platforms to set up outside the scope of regulations and underlines the investor protection risks this entails. It therefore asks for a reduction of these incentives through appropriate policies.

Luxembourg Legal and Regulatory Developments

CSSF Circular 14/598
Common Definition of EU Money Market Funds

Further to the official publication by ESMA, on 22 August 2014, of its opinion (ESMA/2014/1103) on how National Competent Authorities (NCAs) should apply the modification to CESR guidelines on a common definition of EU money market funds (CESR-10-049), the CSSF issued Circular 14/598 on 2 December 2014 in order to incorporate ESMA opinion into its supervisory practice.

As a reminder, ESMA indicated in its opinion that the original CESR guidelines on a common definition of EU money market funds had to be amended in order to ensure that UCITS management companies and self-managed UCITS implement their own internal assessment process to evaluate the credit quality of a money market instrument and to adequately document its outcome. However, where provided, external credit ratings issued by one or more recognised rating agencies shall also be taken into account. While there should be no mechanistic reliance on such external rating(s), a downgrade below the two highest short-term credit ratings by the rating agency should be reflected in the internal process and lead the manager to re-assess the credit quality of the money market instrument.

As an exception, ESMA has considered that money market funds not qualifying as "Short-Term Money Market Funds" (as such term is defined in CESR guidelines) may also invest in sovereign issuances of a lower internally assigned credit rating. Apart from that, however, sovereign issuances are still subject to the same rules as outlined above.

Circular 14/598 is applicable with immediate effect.

For further details on ESMA opinion and CESR guidelines on a common definition of EU money market funds, please refer to the presentation made on this subject in the November 2014 edition of our Luxembourg Legal Update.

CSSF FAQ and Press Release 15/09 concerning the Law of 28 July 2014
Compulsory Deposit and Immobilisation of Bearer Shares and Units

On 30 December 2014, the CSSF published a FAQ document in relation to Luxembourg regulated investment vehicles impacted by the law of 28 July 2014 (2014 Law) on the compulsory deposit and immobilisation of bearer shares and units.

In its FAQ, the CSSF requires, among others, that each Luxembourg regulated UCITS, UCI, SIF and SICAR incorporated in the form of an SA, SCA or FCP and which has issued or will issue bearer shares/units, informs its shareholders/unitholders in an adequate manner of the implications and deadlines of the 2014 Law, as well as of the identity of the depositary appointed for the immobilisation of the bearer shares/units. According to the CSSF FAQ, the prospectus of such investment vehicles has, in any case, to be amended in order to reflect the abovementioned information. In addition to the amendment of the prospectus, the CSSF also lists other possible means of informing investors.

On 26 January 2015, the CSSF published a press release in order to remind legal entities impacted by the 2014 Law of the legal deadline for the appointment of the depositary. In this press release, the CSSF also outlined the obligation for a Luxembourg domiciliary agent under the law of 31

May 1999 on the domiciliation of companies to take any appropriate action if it is aware that the management body of an entity falling within the scope of the 2014 Law and for which it is acting as domiciliary agent has failed to appoint a depositary.

For further details on the Luxembourg regime for compulsory deposit and immobilisation of bearer shares and units, please refer to the Corporate and M&A section of this Luxembourg Legal Update.

CSSF Updated FAQs on AIFM Law

On 29 December 2014, the CSSF published an updated version of its FAQs on the AIFM Law, which provide guidance on the notifications to the CSSF under articles 25 and 37 of the AIFM Law as well as some clarification on the so-called "depo-lite" regime applicable under article 37 of the AIFM Law and on the reporting obligations.

Article 25 Notification - Acquisition of Major Holdings and Control of Non-Listed Companies

Article 25 of the AIFM Law imposes notification obligations to:

- Luxembourg authorised AIFMs
- non-EU AIFMs which market AIFs to professional investors in Luxembourg without a passport under article 45 of the AIFM Law in the following situations:
  - an AIFM manages an AIF that acquires, disposes or holds major holdings in a non-listed company representing respectively the threshold of 10%, 20%, 30% 50% and 75% of the proportion of voting rights attached to the shares of the non-listed company held by the AIF
  - an AIFM manages one or more AIFs, which either individually or jointly, on the basis of an agreement aimed at acquiring control, acquire control of a non-listed company
  - an AIFM cooperating with one or more other AIFMs on the basis of an agreement pursuant to which the AIFs managed by those AIFMs jointly, acquires control of a non-listed company.

In its FAQs, the CSSF provides details regarding the definition of a "non-listed company" and the specific cases in which AIFMs acquiring major holdings and control of non-listed companies are not required to notify the CSSF under article 25 of the AIFM Law. The FAQ further describes the content of the notification that must be sent to the CSSF by using a specific form available on the CSSF website, as well as the applicable timeframe to do so. In particular, the CSSF indicates that notifications should be made as soon as possible, but no later than 10 working days after the date on which the AIF has reached, exceeded or fallen below the relevant major holdings threshold or has acquired control over the non-listed company.

Article 37 Notification - Marketing of non-EU AIFs to professional investors without a passport by Luxembourg and other EU AIFMs

The updated version of the CSSF FAQs determines that authorised Luxembourg and other EU AIFMs must notify the CSSF of their intention to market to professional investors in Luxembourg, without a passport, non-EU AIFs they manage or EU feeder AIFs whose master AIF is not an EU AIF or whose master AIF is not managed by an authorised Luxembourg/EU AIFM, pursuant to article 37 of the AIFM Law (respectively article 36 of the AIFM Directive).

The notification will be made by using a specific information form available on the CSSF website, including the following information:

- general information on the AIFM, such as the name, address, country and supervisory authority of the AIFM. For non-Luxembourg AIFMs, an attestation of the EU AIFM's supervisory authority must be attached.
- general information on each non-EU AIF in relation to which the marketing in Luxembourg is notified, such as the name, domicile, national competent supervisory authority of the non-EU AIF (if applicable) and ISIN code of the non-EU AIF (if applicable).
- information on the identity (i.e. name and domicile) of the entities responsible for carrying out the depo-lite services referred to in article 21(7) (cash-monitoring), (8) (safekeeping of assets) and (9) (oversight of certain operational functions) of the AIFM Directive. In this respect, the CSSF accepts that one or several entities can be appointed per non-EU AIF to perform the duty referred to under article 21 (8) (safekeeping of assets), which means that either a single depositary shall carry out this duty with regard to the AIF’s assets entrusted to it for safekeeping or, if several entities (different prime brokers, for example) have been appointed to perform this duty, each such entity shall carry out this duty with regard to the portion of the AIF’s assets that has been entrusted to it for safekeeping.

  However, as regards the duties referred to under article 21(7) (cash-monitoring) and (9) (oversight of certain operational functions), the CSSF only accepts a maximum of one entity per duty. To avoid uncertainty, there are no specific requirements with respect to the location of the entity(ies) so appointed to carry out the depo-lite services.

- confirmation that all the conditions of article 36(1) (a), (b) and (c) of the AIFM Directive are complied with, including in particular that the third country competent authority of the non-EU AIF has signed appropriate cooperation agreements with the CSSF and is not listed as a non-cooperative country by FATF.

In its FAQs, the CSSF determines that Luxembourg and EU AIFMs must inform the CSSF if they stop marketing non-EU AIFs in Luxembourg on the basis of article 37 of the AIFM Law. When informing the CSSF, the Luxembourg/EU AIFM must indicate the date from which it will stop marketing activities in Luxembourg under article 37 of the AIFM Law. Moreover, Luxembourg/EU AIFMs that marketed non-EU AIFs to professional investors in Luxembourg under the existing Luxembourg placement regime before 22 July 2013 will be required to send the information form to the CSSF if they intend to continue to market their non-EU AIFs in Luxembourg on the basis of article 37 of the AIFM Law.

According to additional guidance published by the CSSF for the use of the information form, it should be noted that:

- the information form must be completed regardless of the nationality of the relevant AIFM (Luxembourg or other EU AIFM)
- the content of the form must be filled out electronically. Once the form is properly filled out, a paper version should be dated and signed by the applicant. A scanned version of such form should then be sent to the CSSF electronically to the following e-mail address: aifm@cssf.lu. The subject of the e-mail containing the information form should contain the following information and keywords:
  – for Luxembourg AIFMs: "Article 36 marketing - [CSSF identification number] - [name of the AIFM]"
  – for EU AIFMs that are not domiciled in Luxembourg: "Article 36 marketing - [name of the AIFM]"
- no documents have to be attached to the information form except for EU AIFMs not domiciled in Luxembourg, which are required to attach an attestation from their supervisory authority. In addition, the CSSF may at any time require EU AIFMs to provide additional information as appropriate
- no more than four AIFs per information form should be declared. As a result, one or more additional information forms will have to be filled out and sent to the CSSF when the number of AIFs to be declared exceeds four

According to the information form and the Grand-ducal Regulation of 28 October 2013 relating to the fees to be levied by the CSSF, the following fees will be levied by the CSSF:

- single lump sum of EUR 2,650.- in the case of a traditional foreign AIF and EUR 5,000.- in the case of an umbrella AIF
- annual lump sum of EUR annual lump sum of EUR 2,650.- in the case of a traditional foreign AIF and EUR 5,000.- in the case of an umbrella AIF.

Reporting Obligations

The updated version of the CSSF FAQs specifies that AIFMs established before 22 July 2014 and authorised between 1 October 2014 and 31 December 2014 are required to submit their first report covering the period from 1 October 2014 to 31 December 2014 at the latest by 31 January 2015 (15 February 2015 where the AIF is a fund of funds).

CSSF Press Release 15/04 Concerning AIFMD Reporting Obligations

On 13 January 2015, the CSSF published a press release in which it reminded all Luxembourg domiciled AIFMs and all non-EU AIFMs that are marketing AIFs under article 42 of the AIFM Directive to assess their reporting obligations under the AIFM Directive.

This assessment must be made in accordance with the following provisions:

- article 3 (3)(d) of the AIFM Law for Luxembourg registered AIFMs
- article 22 (1), (2) and (4) of the AIFM Law for Luxembourg authorised AIFMs
- article 24 (1), (2) and (4) of the AIFM Directive for non-EU AIFMs.

In its press release, the CSSF also stressed that all AIFMs have at least an annual obligation to submit the AIFMD report which was due on 31 January 2015 at the latest (except for AIFs which are considered to be funds of funds and for which submission is accepted with a delay of 15 additional days).

To avoid uncertainty, AIFMs are requested to submit their files as described in circular CSSF 14/581 which was published on 13 January 2014 and deals with the technical aspects of AIFMD reporting.

First Luxembourg UCITS Authorised to Use the Shanghai-Hong Kong Stock Connect Programme

In a press release dated 2 December 2014, ALFI indicated that the first Luxembourg UCITS had received the authorisation of the CSSF to use the Shanghai-Hong Kong Stock Connect programme that provides mutual trading access between the Shanghai and Hong Kong stock markets.

The programme, launched on 17 November 2014, enables foreign investors to trade Shanghai-listed shares via the Hong Kong stock exchange, and mainland investors to invest in Hong Kong shares via the Shanghai stock exchange. It also offers an opportunity for UCITS to invest in A-shares listed on the Shanghai stock exchange alongside the existing investment schemes (such as QFII and RQFII).

However, there are a number of factors that require careful consideration by a Luxembourg UCITS, its management company (if any) and its depositary if it envisages accessing this market through the Shanghai Hong Kong Stock Connect. These factors, which will have to be adequately covered in the UCITS'/management company's risk management procedures, include:

- accounts opened by the depositary bank of the UCITS with a sub-custodian in Hong Kong are segregated at the level of the UCITS' sub-funds or structured as UCITS client assets omnibus accounts of the Luxembourg depositary with that sub-custodian
- the broker model involving delivery versus payment settlement must be chosen in order to limit counterparty risk
- the prospectus, and in particular the KIID, will contain a specific disclosure to inform investors of the specific legal risks linked to compulsory requirements of the local CSDs, HKSCC and ChinaClear for custody of securities on a cross-border basis.

Luxembourg UCITS whose investment policies already permit exposure to A-Shares and only need to adapt their prospectus and KIID to cater for access through the Shanghai-Hong Kong Stock Connect will benefit from a fast-track procedure when filing their application with the CSSF.

ALFI Position Paper on Luxembourg Implementation of Statutory Audit Regulation

On 19 December 2014, ALFI issued a position paper on the so-called "Statutory Audit Regulation" as it may significantly impact the governance of Luxembourg regulated investment funds.

As indicated in the Banking, Finance and Capital Markets section of this Luxembourg Legal Update, the Statutory Audit Regulation applies to PIEs, being basically credit institutions, insurance undertakings and entities with securities admitted to trading on a MiFID regulated market. Even if regulated investment funds (including UCITS and AIFs) are not listed as such in the definition of PIEs, these funds will nevertheless fall within the scope of the Statutory Audit Regulation when they are admitted to trading on a MiFID regulated market.

In its position paper, ALFI provides its views on the implementation of the different options of the Statutory Audit Regulation that are available to EU Member States. Moreover, ALFI expresses its concerns about the inclusion of AIFs and UCITS in the definition of PIEs. According to ALFI, such inclusion will imply disproportionate costs for the Luxembourg fund industry while the expected added benefits on the audit quality and reliability of the financial reporting over and above current arrangements is neither clear, nor proven. ALFI indicates that AIFs, UCITS and their related management companies operate in a strictly defined regulatory environment and are subject to specific governance mechanisms, including controls exercised by their depositary. Furthermore, because Luxembourg funds listed on stock exchanges (with the exception of ETFs) are not traded on the market, ALFI recommends excluding AIFs and UCITS not listed on any stock exchange as well as

AIFs and UCITS not actively traded on a stock exchange from the list of PIEs.

For further details on the Statutory Audit Regulation, please refer to the presentation made on this subject in the Banking, Finance and Capital Markets section of this Luxembourg Legal Update.

Case Law

Court of Appeal, 15 July 2014

No Right of Direct Action by Investor against the Depositary of a Luxembourg UCITS

Court of Appeal, 4 December 2013

Obligation and Liability of the Depositary of UCITS Fund and Management Company

Please refer to the Litigation section of this Luxembourg Legal Update for further details on the above.

Litigation

Court of Appeal, 26 November 2014, N°40142

Proving a Debt by Means of the Accounting Books of a Merchant

A commercial company had mentioned in its annual accounts that it was indebted to another (specifically designated) company for an amount of EUR 40,224. Subsequently, however, the company refused to pay said amount, alleging that it was not a debtor of the other company. The District Court and the Court of Appeal nevertheless ordered the commercial company to honour its commitment.

In order to do so, the Court of Appeal recalled that the Civil Code and the Commercial Code foresee that the account books held by merchants are evidence against them. The Court emphasised that, pursuant to these principles, the entries made by merchants in their accounting constitute an extra-judicial admission that binds the merchants. Merchants can only claim themselves relieved of their obligation if they show that the references result from an error of fact.

Banking, Finance and Capital Markets

Pledge over Business – Priority – Confusion of Assets of Insolvent Debtor with Assets of other Insolvent Companies

After the sale of an insolvent debtor's business by the insolvency administrator, a creditor having a pledge over the business asks to be paid before any other creditor.

The insolvency administrator refuses this on two grounds: firstly, there may be other creditors who should be preferred over a creditor with a pledge over the business and, secondly, he considers that a merging of insolvency proceedings in group companies (*confusion des patrimoines*) would also have some possible consequences on the ranking of the pledgee's claim.

The District Court holds that certain creditors may be preferable in rank to the creditor with a pledge over business. This is the case, among others, of creditors benefiting from a general preference regarding judicial fees (including the fees and costs of the bankruptcy receiver) incurred for the interest of all competing creditors, super-preferred claims of employees, employees' social contributions, treasury claims, employer's social contributions and any claims of a landlord secured over furniture. For this reason, the insolvency administrator does not have the right to pay the secured creditor with a pledge over business immediately. He must take into account the preferences of the different creditors and establish a ranking between them before paying out any sums.

With regards to the influence of the merging of insolvency proceedings, the Court holds that such a merger concerns the assets of the insolvency estates, but the creditors benefiting from a preference or a pledge may act directly on the assets subject to their preference. For this reason, even if there is a merger, only the creditors with a preference regarding the assets of the insolvent debtor's company may be paid out of the proceeds of the sale of this company's business.

Insolvency – Suspension of all Measures of Execution of Unsecured Creditors – Action in Court in View of Voiding a Contract

According to article 452 of the Luxembourg Commercial Code, after the opening of insolvency proceedings all measures of execution by unsecured creditors are suspended.

According to the District Court, this means that after the opening of insolvency proceedings, unsecured creditors may only act directly against the insolvency administrator. In particular, article 452 of the Commercial Code suspends any individual action for payment against the insolvency estate. All payments of unsecured creditors are prohibited. Such unsecured creditors are required to file proof of claims in the bankruptcy proceedings.

In the case at hand, the Court had to answer the question of whether article 452 of the Commercial Code also applies to an invalidity action regarding a contract which has been executed by the insolvent party and its debtor before the opening of the insolvency proceedings. According to the Court the purpose of such an action in court is not the establishment and payment of a claim, but to invalidate a contract and to put a stop to the position of debtor to the insolvent company. For this reason, it is not an action falling within the scope of article 452 of the Commercial Code.

Securities' Deposit Contract – Proof of Orders Given by Client – Implied Ratification of Bank Statements even in Cases of Lack of Express Clause in General Conditions

According to the Court of Appeal, with regards to a securities' deposit contract, a bank's client manages his portfolio personally: he gives orders himself or gives instructions to a professional acting on his behalf. The bank has an obligation to make aware, advise and inform its client. However if such obligation implies a duty to make the client aware in general terms, the bank has no duty to give advice on the purchase of a certain security. The advice given by the bank tends to help the client to understand the planned transaction, but the client takes the final decision himself. The client assumes the management risks. The bank's duty to inform the client depends on his competencies and his experience.

Orders given by the client to the bank with regards to a securities deposit contract may be evidenced by the implied ratification of bank statements sent to the client. A client who does not dispute the bank statements sent to him, or kept in his mailbox at the bank (at his request), is deemed to have tacitly approved the existence of the operation which is noted on the statement and the order relating thereto which has been given to the bank. Such ratification is possible even in the absence of contractual clauses to this effect in the bank's general conditions.

In the case at hand the bank’s general conditions require the client to dispute the statements within a certain time limit, if he does not approve them. However the clause does not state that if the client does not challenge them, he ratifies the operations noted on the statement. According to the Court, such ratification is taking place even in the absence of a clause to this effect.

Such ratification covers acts by the bank which go beyond the limits of its powers and even acts which the bank had no power to carry out. In both cases the bank is not acting as an agent but as a person acting without due authority in connection with the affairs of another person. Such persons' actions can be ratified in the same way.

Corporate and M&A

District Court, 8 December 2011

Loss of Half of the Corporate Capital – no Need of an Approved Balance Sheet to Ascertain the Loss – no Obligation for the Shareholders to Inject Additional Capital to Restore the Corporate Capital of the Company

Pursuant to article 100 of the Companies Law, in the event of a loss of half the corporate capital, the board of directors shall convene a general meeting of the shareholders so that it is held within a period not exceeding two months from the time at which the loss was or should have been ascertained by them and such meeting shall decide on the possible dissolution of the company.

On 8 December 2011, the District Court[2] confirmed the following principles with respect to article 100 of the Companies Law:

- Under Luxembourg law, in the event of a loss of half or the entire corporate capital, the company will not be dissolved automatically. Nor do shareholders have the obligation to inject capital into the company in order to restore the corporate capital of the company. The only obligation resulting from the loss of half or the entire corporate capital of the company is that the question of the continuation of the running of the company or its dissolution must be submitted to the general shareholders' meeting.
- Pursuant to article 100 of the Companies Law the loss of the company is assessed in relation to the corporate capital only, irrespective of the value of the assets held by the company. The corporate capital represents the monetary value establishing the sum of the contributions in cash or in kind contributed to the company at its incorporation or during its existence. The corporate capital is an accounting and legal concept which does not coincide with the concept of funds or assets which represents all the elements that constitute all the business assets of the company, including property assets.
- Pursuant to article 100 of the Companies Law, in the event of a loss of half of the corporate capital, the board of directors shall convene a general shareholders' meeting within a period not exceeding two months from the time the loss was or should have been ascertained by them. This article does not require that the loss be established on the basis of an approved balance sheet. To the contrary, the board of directors must react as soon as the loss is ascertained, failing which it may incur liability. Therefore, it is necessary for the board of directors to be able to ascertain the loss on the basis of any accounting records, without having to wait for the general shareholders' meeting to first approve the accounts.

[2] District Court, 8 December 2011, N°133408 and 134926.

Court of Appeal, 17 October 2012

Luxembourg Branch of a Belgium Company – Absence of Legal Personality – Inability to Initiate Legal Proceedings – Substantive Irregularity

On 22 May 2012, the President of the District Court granted a conditional payment order to the Luxembourg branch of a Belgian s.a. against an SARL for an amount of EUR 27,504.55 which relates to outstanding invoices. On 22 June 2012, an enforceable title[3] was granted to the Luxembourg branch following which the SARL lodged an appeal against this enforceable title and, in compliance with article 41 of the Luxembourg new civil procedure code, sued the Belgian s.a. before the Luxembourg Court of Appeal.

The Court of Appeal[4] stressed that judicial proceedings may only be initiated by either a physical or a legal person. It further stressed that it is the national law, the law of the registered office of the company concerned, that determines who has the legal capacity to bring a suit. Under Belgian law, a branch of a Belgian s.a. does not have the legal personality, since it is only a branch of a company characterised by the independence of its running and therefore, the branch does not have any capacity to take legal action.

This rule being a Belgian mandatory rule, if this rule is breached, the document initiating proceedings will be null and void. The breach of this rule does not only constitute a formal irregularity but rather a substantive irregularity. The lack of standing could not be covered by the fact that the act did not adversely affect the appellant.

The Court of Appeal further declared that the branch, having no own legal personality, its initial request, the conditional payment order and the enforceable title already obtained against the SARL are null and void.

Court of Appeal, 13 March 2013

Failure to Publish Annual Accounts – Offence – Rebuttable Presumption

Pursuant to article 163, 2 of the Companies Law, managers of a company who have failed to submit the annual accounts to the general shareholders' meeting within six

[3] Enforceable title N°388/2012.
[4] Court of Appeal, 17 October 2012, N°38759.

months of the end of the financial year and who have failed to publish such annual accounts may incur a fine of EUR 500 to EUR 25,000.

On 1 March 2012, the District Court[5] determined that the failure to publish the annual accounts of a company only constitutes a purely material offence.

The Court of Appeal[6] rejected this argument and reminded that it had already been decided that, "*where article 163 of the Companies Law is silent, the mental element of an offence consists of the material violation of the legal provision committed knowingly and purposefully; this implies that the accused can justify his behaviour by any cause excluding his misconduct, while not requiring him, pursuant to the principle of the presumption of innocence, to bring forward complete evidence of the justification; it shall be sufficient if he proves that the justification is credible*."

The manager of a SARL who did not publish the annual accounts in time is thus presumed to have committed an offence following the simple observation of the omission, which constitutes the misconduct. However, this presumption is not irrebuttable and could be rebutted by the manager by invoking that he did not act knowingly and purposefully, thus acting under the influence of a situation of justification such as constraint, force majeure or invincible error, which implies the absence of a previous fault of the manager, and in the case of the constraint and force majeure, the criterion of irresistibility. By contrast, the good faith of the manager is irrelevant as a credible justification.

Declaring that all the accounting records have been given to a fiduciary and that the fiduciary should have established the annual accounts and published them is pure allegation and contradicts the fact that there has never been any regular book-keeping, preventing the fiduciary from establishing the annual accounts. Such a declaration does not constitute evidence that the manager acted under the influence of a situation of justification.

[5] District Court, 1 March 2012, N°968/2012.
[6] Court of Appeal, 13 March 2013, N°150/13.

Supreme Court, 4 July 2013

The Offence of Bankruptcy, an Instantaneous Offence – the Sole Failure to Publish Annual Accounts Constituting an Offence

On 4 July 2013, the Supreme Court[7] confirmed that:

- the bankruptcy offence, constituted by the fact that the confession of the cessation of payments has not been made within the legal timeframe, is an instantaneous offence which is completed as soon as the confession of the cessation of payments has not been made during the legal timeframe, except if the accused invokes and proves that he has a credible justification, without having to bring forward the complete evidence of the justification. The only mental element required to constitute the bankruptcy offence is the simple "criminal fault" which exists as soon as the act is committed.

the offence of breaching article 163, 2 of the Companies Law is committed merely by ascertaining that the *de jure* director, acting on a voluntary and informed basis, has not published the annual accounts required by the law, except if he invokes and proves that he has a credible justification, without having to bring forward complete evidence of the justification. The fact that the director has instructed a third party to establish and to publish the annual accounts does not absolve him from his obligation and he is required to ensure that the third party proceeds to establish and publish the annual accounts correctly.

[7] Supreme Court, 4 July 2013, N°39/2013.

Court of Appeal, 29 January 2014

Non Application of Article 495-1 of Luxembourg Commercial Code for not Keeping Regular Accounting Records and Books and not Publishing the Balance Sheets – Failure to Declare and to Pay the VAT not Necessarily Constituting a Gross Negligence – the Fact not to Protest against VAT Returns, Knowing that the Taxation Has Been Based on an Incorrect Turnover, Constituting a Case of Gross Negligence – in Case of Evidence of Gross Negligence, Presumption of Responsibility for the whole Shortfall in Assets

Pursuant to article 495-1 of the Luxembourg code of commerce, when the bankruptcy of a company results in a shortfall in assets, the court can decide, at the request of the bankruptcy receiver, that the debt shall be carried, in whole or in part, with or without joint liability, by the managers against whom gross negligence has been established which has contributed to the bankruptcy.

On 8 July 2011, the District Court[8] determined that, pursuant to article 495-1 of the Luxembourg code of commerce, the manager of an SARL acted with gross negligence by not keeping regular accounting records, not publishing all required balance sheets and not paying VAT and social charges for the financial years 1999-2004. This gross negligence being in direct causal relation with the bankruptcy, it had necessary led to the opening of liquidation proceedings. The District Court therefore decided that the manager should support the whole shortfall in assets of the Company. The manager launched an appeal against the decision of the District Court.

The Court of Appeal[9] rejected most of the appeal and confirmed the application of article 495-1 of the Luxembourg code of commerce. The Court of Appeal indicated that the fact that the manager had failed to pay VAT and tax for certain financial years and that he did not make formal declarations on the official forms to the Luxembourg direct tax administration, did not constitute in itself gross negligence pursuant to article 495-1 of the Luxembourg commercial code if it was involuntary and a consequence of an adverse evolution of company business. By contrast, the non-payment of the social and fiscal charges does constitute gross negligence if it is a deliberately chosen method of financing. The fact of using the social and fiscal charges for other purposes (such as paying other creditors of the company) instead of passing them on to the Luxembourg direct tax administration must be considered a diversion of funds for the benefit of the employer and as a way to provide, unduly, through these misappropriated funds, a credit to the company.

Furthermore, the fact that the manager did not protest against the VAT returns issued by the Luxembourg tax administration, even though he knew that the taxation had been based on an incorrect turnover for the company, does also constitute gross negligence which led to the bankruptcy of the company pursuant to article 495-1 of the Luxembourg commercial code.

However, the Court of Appeal accepted the request of the appellant in relation to the accounting records and the balance sheets, specifying that the failure to keep regular accounting records or to publish the balance sheets did not contribute to the company's bankruptcy.

In relation to the amount of damages owed by the manager, the Court of Appeal underlines the fact that the bankruptcy receiver does not have to establish the link between the misconduct and the shortfall in assets. The manager is presumed, if the gross negligence has contributed to bankruptcy, to be responsible for the whole shortfall in assets, the Judge having a discretionary power of moderation.

Funds and Investment Management

Court of Appeal, 15 July 2014

No Right of Direct Action by Investor against the Depositary of a Luxembourg UCITS

On 15 July 2014, the Court of Appeal confirmed earlier decisions rendered on 4 March 2010 by the Luxembourg District Court in the context of the Madoff case, by declaring the claims filed by an investor of a Luxembourg UCITS SICAV against the depositary bank of such SICAV to be inadmissible.

The Court of Appeal first ruled against the appealing party's argument that article 36 of the 2002 Law entitled shareholders of a UCITS SICAV to directly action the liability of the depositary bank and excluded the existence of a direct legal action for the investor against the depositary bank of the SICAV based on the 2002 Law, both on a contractual and tort basis. Having reviewed the parliamentary works of the 2002 Law and Directive 85/611/EC, the Court confirmed in this respect the

[8] District Court, 8 July 2011.
[9] Court of Appeal, 29 January 2014, N°38130.

judgement of first instance that decided that where the investor in a SICAV is only a shareholder of the SICAV, the investor could only engage the liability of the depositary bank pursuant to the national law of the investment company, and more precisely pursuant to the applicable company law.

The Court of Appeal further declared the claim of the appealing party to obtain compensation for the damages indirectly suffered by the investment fund for which it is acting in its capacity as management company as a result of the loss in value of the shares it held in the SICAV to be inadmissible. According to the Court of Appeal, which confirmed the judgement of first instance, only the person suffering the damage, i.e. the SICAV itself, can act for the losses it may have suffered and as a result of which its shareholders are affected only indirectly. It follows that a shareholder cannot act for his part in the collective damage suffered by the SICAV, unless it suffers a prejudice that is specific, distinct and independent from the prejudice actually and initially suffered by the SICAV. As this condition was not fulfilled in the case at hand, the direct action of the shareholder against the depositary bank of the SICAV had to be dismissed. Indeed, the Court confirmed that the main loss alleged by the shareholder, i.e. the devaluation of its shares, constituted at the same time a loss of the assets of the SICAV, and this loss is only the corollary of the damage suffered by the SICAV and can therefore not be qualified as an individual prejudice of the shareholder.

The Court of Appeal also declared the claim of the appealing party, acting in its capacity as management company, for the loss of profit and interests following a redemption request that had not been executed by the SICAV which was put into liquidation in 2009 to be inadmissible. According to the Court, such damage to the investor resulting from the blocking of its debt in the collective proceedings of the debtor does not constitute a damage distinct from that of the other creditors.

Court of Appeal, 4 December 2013

Obligation and Liability of the Depositary of UCITS Fund and Management Company

On 4 December 2013, the Court of Appeal confirmed the judgement rendered on 8 April 2011 by the Luxembourg District Court in relation to bank transfers operated without instruction from the management company of a Luxembourg UCITS FCP by the depositary bank of such FCP. In the case at hand, the bank transfers were operated by the depositary both from the accounts opened by the Luxembourg management company on behalf of the FCP's sub-funds and also from the account opened by the management company in its own name and behalf.

In short, the Court of Appeal reaffirmed the following positions:

- A distinction should be made between:
  - the quality of the depositary bank pursuant to articles 1915 et seq of the Civil Code as regards the account opened by the management company in its own name and on its behalf
  - the quality of the depositary pursuant to articles 17 et seq of the 2002 Law as regards the safekeeping of the assets of the FCP. As a depositary pursuant to the Civil Code, the bank shall have obligation of result and be obliged to fully reimburse its client (obligation de restitution de résultat). In such a case, the sole fact of the non-execution/performance of its obligation, for instance failing to return a certain amount of cash to its client, constitutes misconduct/a wrongful act that is likely to engage its liability.
- It constitutes misconduct for a depositary bank of a UCI to act without instruction from the management company by:
  - transferring, in the first instance, the litigious amount from the accounts of the FCP to the unitholders registered in a non-official register of unitholders held by Dexia for the account of Clearstream (i.e. central depositary), thus overdrawing these accounts
  - withdrawing and transferring, in the second instance, to solve the said overdraw not conventionally agreed between the parties, the same amount from the account held in its own name and behalf by the management company.
- The depositary bank which has an obligation to fully reimburse its client (*obligation de restitution de résultat)* is then deemed liable and cannot discharge itself from its liability (partially or totally as the case may be), unless it can prove that its obligation to return the deposited assets was not fulfilled because of a force majeure event or due to the fact or the fault of its client. In the case at hand, however, the depositary bank could not invoke force majeure as the assets deposited with it were fungible assets (i.e. cash). As a consequence, the depositary bank sought to hold the management company liable for not having correctly

kept the register of unitholders to the extent that there were differences between the register of unitholders held by the management company and the register of unitholders held by Dexia for the account of Clearstream. In this respect, the Court indicated that the accurate record keeping and holding of the register of unitholders as well as the issuance of the certificates establishing the registration of the unitholders in the official register of unitholders is and remains, by virtue of Annex 2 of Directive 2009/65/EC, the obligation of the management company of the UCI. However, such official register of unitholders benefits from a rebuttable presumption of accuracy. This means that the official register of unitholders kept by the management company must be considered valid unless the opposite is proven, which the depositary bank failed to demonstrate.

Tax

International Legislation

Amendment of the Parent Companies Directive

European Council – Anti-Abuse Clause in the EU Parent Subsidiary Directive

On 9 December, the European Council approved the amendment of the Parent Subsidiary Directive (2011/96/EU) which aims to prevent tax avoidance and aggressive tax planning by corporate groups.

Article 1 paragraph 2 of the Parent Subsidiary Directive is removed and replaced by a new paragraph stating that Member States should not grant the benefit of the Directive to an arrangement or a series of arrangements which have been put in place for the sole purpose of obtaining a tax advantage and are not "genuine" as they do not reflect economic reality.

Council Directive 2014/107/EU Amending Mandatory Exchange of Information in the Field of Taxation

European Council – Exchange of Information in the Field of Taxation

On 9 December, the European Union's Council adopted Directive 2014/107/EU amending Directive 2011/16/EU relating to mandatory automatic exchange of information in the field of taxation. The new directive extends the scope of the automatic exchange of information to interest, dividends, gross proceeds from the sale or redemption of financial assets as well as account balances. This new directive is in line with the Common Reporting Standard developed by the OECD. Member States have until 31 December 2015 to implement this directive and it will apply from 1 January 2016.

Financial Transaction Tax – Update

European Council Meeting 7 November 2014 – Negotiation Progress on the Financial Tax Transaction (FTT)

During its meeting of 7 November 2014, the Council indicated its objective of having an agreement of the 11 Member States in the near future implementing the first phase of the FTT from 1 January 2016.

Action 4 of the Action Plan on Base Erosion and Profit Shifting (BEPS)

Public Discussion Draft on Interest Deductions and other Financial Payments

On 18 December 2014 the OECD released a public discussion draft on BEPS action 4 limiting base erosion due to interest deductions and other financial payments. The OECD is identifying the best practices to address the BEPS issues and requests input on a large number of questions ranging from the nature of the payments that economically qualify as interest to a potential exemption for small/low risk entities.

Action 6 of the Action Plan on Base Erosion and Profit Shifting

Public Discussion Draft on Preventing Treaty Abuse

On 21 November 2014 the OECD released a public discussion draft on BEPS Action 6 preventing treaty abuse. The discussion draft addresses the issues related to the limitation of benefits rule and the treaty entitlement of collective investment vehicles and non-collective investment vehicle funds. A revised version of the Action 6 report should be released during the course of 2015.

National Legislation

Automatic Exchange of Information under the Saving Directive

Bill N°6668

On 25 November 2014, Luxembourg formally adopted a law amending the Luxembourg laws of 21 June 2005 implementing the Council Directive 2003/48/EC of 3 June 2003 (the EU Savings Directive). The Law puts an end to the withholding tax regime under the EU Savings Directive as of 1 January 2015 and implements the automatic exchange of information as of that date.

Since 1 July 2005, the Directive 2003/48/EC has required Member States to exchange information automatically whenever an interest payment is made from one Member State to an individual or a residual entity established in another Member State. However, to date, Austria and Luxembourg have been benefiting from a special regime. Luxembourg was permitted to apply an optional information reporting system whereby if a beneficial owner, under the EU Savings Directive, does not comply with the reporting procedure, Luxembourg levies a withholding tax on payments to such a beneficial owner.

As of 1 January, Luxembourg will apply the automatic exchange of information on savings income, i.e. the paying agent will have to provide the following information to the tax authorities of the country where the beneficiary is tax resident:

- name and address of the beneficial owner
- name and address of the paying agent
- bank account of the beneficial owner or the receivable triggering the interest
- total amount of interest or similar income received by the beneficial owner further to disposal, sale or redemption.

However, despite the amendment of the law of 23 December 2005 through the adoption of the law of 25 November 2014, Luxembourg individual residents receiving interest payments will remain subject to a 10% withholding tax.

The Luxembourg Tax Authorities published circular RIUE-N°4 on 19 January 2015 explaining the major and practical consequences of adopting the law of 25 November 2014.

Net Wealth Tax Law

Bill N°6706

On 25 November 2014, Luxembourg Parliament adopted Bill N°6706 amending the Luxembourg net wealth tax Law.

Up to now the unitary value for net wealth tax was assessed every three years except in specific cases. However, from 1 January 2015 the unitary value will be assessed on a yearly basis.

As of 1 January 2015, if the net wealth tax does not exceed EUR 100, the tax will be paid in one instalment (on 10 November) and no longer on a quarterly basis.

Luxembourg taxpayers can benefit from a reduction of the net wealth tax burden if they allocate part of their profit to a specific reserve blocked for a five-year period. As of 1 January 2015, the net wealth tax reduction is limited to the corporate income tax (reduced by the minimum income tax) owed by the company for the preceding period instead of that owed for the same tax year. In this respect net wealth tax reductions for years 2014 and 2015 will both be computed based on the corporate income tax due for 2014.

Bill "*Paquet D'avenir*" – First Part

Bill N°6722

On 19 December 2014, the Luxembourg Parliament adopted Bill N°6722 amending both the Luxembourg

Income Tax Law (ITL) and the General Tax Law (*Abgabenordnung* - 22 May 1931).

Advance Tax Agreement

As of 19 December 2014, the General Tax Law officially details the legal basis for advance tax agreement. According to article 4 of Bill N°6722, the head of the Luxembourg tax authorities will be able to issue, upon receipt of written and motivated requests, Advance Tax Confirmations (ATC) regarding the application of specific Luxembourg Tax Law provisions.

These ATC cannot result in tax exemption or reduction and are only valid for a maximum of 5 years.

The Luxembourg Tax Authorities are bound by ATC unless:

- the factual background or the described transactions are incomplete or inaccurate
- the transactions implemented differ from those described in the ATC
- the ATC is no longer in line with the Luxembourg domestic law, European Union law or International law.

ATC regarding corporate tax will be subject to a fixed fee (between EUR 3,000 and EUR 10,000 depending on the complexity of the request).

A Grand Ducal Decree issued on 23 December 2014 provides additional details about the applicable procedure as of 1 January 2015.

An ATC request should at least contain:

- precise identification of the applicants (names, addresses, tax numbers) as well as all necessary information on third parties involved and a description of their respective activities
- a detailed description of the transaction and the anticipated structure of the group
- a detailed analysis of the tax issues and the anticipated tax treatment by the applicants
- a confirmation that the description of the facts is complete and in line with the factual background.

In this respect all ATC requests regarding corporate tax will be submitted to the ATC Commission (*Commission des Décisions Anticipées* – CDA). The CDA harmonises the application of Tax Law but the tax inspector remains responsible for granting an ATC.

ATC will be published as anonymous summary sheets in the annual activity report of the Luxembourg Tax Authorities.

Please note that the fee payable for ATC is not refundable even if the request is denied or withdrawn.

Transfer Pricing

Bill N°6722 amends article 56 of the Luxembourg ITL on transfer pricing. This new article defines more clearly in which cases companies are considered to be related parties.

According to the article, when a company participating directly or indirectly in the management, control or capital of another company, or when the same persons participate directly or indirectly in the management, control or capital of two companies and in both cases the companies are engaged in commercial or financial transactions with conditions that differ from those that would apply between independent companies, the profits of such companies should be determined and taxed based on conditions agreed between independent companies.

Moreover, Bill N°6722 provides a new paragraph in article 171 of the General Tax Law compelling taxpayers to provide the Luxembourg Tax Authorities with information and documentation in order to detail tax treatments for related parties' transactions.

State Budget Law

Bill N°6720

VAT Amendment

Bill N°6720 amends article 39 of the Luxembourg VAT Law by increasing VAT rates. As of 1 January 2015 the reduced, intermediary and standard VAT rates are increased by 2% i.e. rising respectively to 8%, 14% and 17%.

The 3% super-reduced rate remains but its application is subject to several modifications:

- services linked to the supply of alcoholic beverages in restaurants are now subject to a 17% VAT rate
- the super-reduced rate is only applicable to clothing for children under the age of 14
- VAT rate for construction and renovation work on a principal residence remains at 3%. However VAT increases to 17% for construction work on housing for rent. During a transitional period (until 31 December 2016) the 3% VAT rate may continue to apply if requested by the individuals before 1 January 2015.

This Bill introduced a new article 15bis providing a definition of telecommunication services. In fact, as of 1 January 2015 all telecommunications, broadcasting and electronic services will always be taxed in the country of the customer of the service.

Moreover a new claim procedure for VAT refunds is implemented through this Bill. According to the amended article 55 of the Luxembourg VAT Law, the tax authorities will have 4 months to agree or reject a claim for a refund after it is filed. The Tax Authorities can request further information from the taxpayer who will have a month to answer the request. Once the Tax Authorities are provided with the additional information they have a maximum of two months to give their decision. If the claim is accepted the Tax Authorities will have to make the refund within 10 days to avoid paying default interest to the taxpayer.

Minimum Corporate Income Tax Law

As of 1 January 2015, companies will be subject to EUR 3,210 (including solidarity tax) corporate income tax if their fixed financial assets, transferable securities, securities on related parties, bank deposit represent cumulatively at least 90% of their assets and EUR 350,000.

If the total financial assets of a company meet the 90% criteria but do not exceed EUR 350,000, the company will be subject to EUR 535 (including solidarity tax). All other companies not meeting both criteria will be subject to minimum corporate income tax depending on their total balance sheet (e.g. EUR 21,400 including solidarity tax for a total balance sheet of EUR 20,000,000).

Introduction of Temporary Tax “impôt d’équilibre budgetaire”

Bill N°6720 introduced a new temporary tax of 0.5% as of 1 January 2015. This tax will be levied:

- on professional and replacement income. The taxable basis is the total income exceeding the minimum social wage (calculations subject to some variations based on each individual situation)
- on income from capital of residents and non-residents.

The temporary tax benefits from a EUR 25 annual exemption.

The Luxembourg Tax Authorities published a circular IEBT 1 on 5 February 2015 explaining in greater detail the calculation of this temporary tax.

Withholding Tax Refund

Bill N°6720 amends article 154 of the Luxembourg ITL and adds a new paragraph 6a according to which withholding taxes on dividends will no longer be refundable for loss-making resident taxpayers. This amendment aims to eliminate the difference in tax treatment between residents and non-residents.

Double Tax Treaties

On 1 February 2015, Luxembourg signed a total of 75 Double Tax Treaties (DTT). In addition, negotiations with other states are under way to either amend the existing DTT or to adopt a new DTT.

Double Tax Treaty between Luxembourg and Estonia

On 8 December 2014, Estonia approved the new DTT between Luxembourg and Estonia which will replace the 2006 DTT between Luxembourg and Estonia once in force.

Protocol to Double Tax Treaty between Luxembourg and Lithuania

On 3 December 2014, Lithuania ratified the amending protocol to DTT between Luxembourg and Lithuania.

Protocol to Double Tax Treaty between Luxembourg and Denmark

On 28 December 2014, the protocol to DTT between Luxembourg and Denmark entered into force.

Protocol to the Double Tax Treaty between Luxembourg and Italy

On 25 October 2014 the protocol to the DTT between Luxembourg and Italy on the exchange of information upon request entered into force.

For additional information on the above DTTs and protocols, please refer to the June 2013, October 2013, February 2014 and November 2014 editions of our Luxembourg Legal Update.

Double Tax Treaty between Luxembourg and France

Parliamentary Question N°631 of 16 October 2014

On 16 October, the Luxembourg Parliament submitted a question to the Ministry of Finance about the current negotiations on the amendment of the DTT between Luxembourg and France. The Parliament seeks for the content of the amendment.

The Ministry of Finance indicated that the amendment, signed on 5 September 2014 introduced a new paragraph 4 to Article 3 of the DTT between Luxembourg and France, which determines that the right to tax capital gains realised upon disposal of real estate companies’ share is now exclusively allocated to the State where the real estate assets are located.

Circulars/Regulatory Developments

Low / Free Interest Loan

Grand Ducal Decree 23 December 2014

The Grand Ducal Decree dated 23 December 2014 amends the Grand Ducal Decree of 28 December 1990 on interest subsidy. As of 2015, the benefit in kind resulting from a free or low interest loan granted by an employer to its employee amounts to 1.5% of the amount of the loan instead of 2% before.

Luxembourg Limited Partnership

Circular L.I.R. N°14/4 of 9 January 2015

On 9 January 2015, the Luxembourg Tax Authorities issued the circular L.I.R. N°14/4 on the tax treatment of Luxembourg limited partnership (*Société en Commandite Simple – SCS*) and Luxembourg special limited partnership (*Société en Commandite Spéciale – SCSp*).

The circular confirms that the SCS and SCSp are tax transparent and not subject to Luxembourg corporate income tax. The circular also focuses on the criteria defining a commercial activity to determine in which case SCS and SCSp are subject to municipal business tax. SCS and SCSp will be deemed to have a commercial activity in two cases:

- when it renders a commercial activity as defined under article 14 (1) of Luxembourg ITL. According to this article 14, a commercial activity is rendered on an independent basis with a permanent intention to make profit and to participate in the general economic life
- when at least one general partner is a capital company owning at least 5% of the SCS / SCSp.

The circular outlines through different case law that the interpretation of these criteria is not unique and that all the facts and circumstances should be taken into account to determine the commercial nature of the activity. Moreover, the circular highlights that the sale of assets in a short time or possession of significant assets are not enough to conclude that the companies have a commercial activity.

The circular confirms that SCS and SCSp qualifying as AIFs under the Luxembourg Law dated 12 July 2013 are deemed to have no commercial activity under article 14 of Luxembourg ITL. However, if at least one general partner is a capital company that owns at least 5% of the SCS / SCSp, they will then realise a commercial profit and will be subject to municipal business tax. AIFs established outside of Luxembourg but managed from Luxembourg are exempt from Luxembourg business tax.

Foreign Account Tax Compliance (FATCA)

Draft Circular ECHA – N°2 and Draft Circular ECHA – N°3

On 6 January 2015, the Luxembourg Tax Authorities issued a draft Circular ECHA – N°2 on FATCA. The circular mostly translates into French the rules and definitions set out in the intergovernmental Agreement signed by Luxembourg and the Unites States of America on 28 March 2014. This circular describes the legal obligations that Luxembourg financial institutions must respect to be in line with FATCA.

The draft Circular ECHA – N°3 released on 2 February 2014 focuses on technical aspects of the transfer of information. In order for the Luxembourg Tax Authorities to meet their obligations and be able to transfer the information, processes must be followed by all Luxembourg reporting entities.

Benefit in Kind Granted by Employer

Circular L.I.R N°104/1 of 20 November 2014

On 20 November 2014 the Luxembourg tax authorities released a new circular 104/1 establishing flat rate assessment rules for benefit in kind. The new circular amends circular 104/1 of 18 February 2009 regarding benefit in kind linked to company cars.

The circular covers cars owned or leased by an employer for the benefit of its employee when it is used for professional business travel but also for private use. In this case, the company car is considered as a benefit in kind which can be assessed by two different methods:

- cost price per mile: the benefit in kind amounts to the number of miles covered for private travel times the cost price per mile

- flat rate assessment: the monthly benefit in kind amounts to 1.5% of the acquisition price of the car.

Contributions to the car's fixed costs by the employee can be deducted from the benefit in kind calculated but not contributions to variable costs (e.g. fuel, maintenance). Please note that the employee's contribution to the leasing costs is considered a contribution to fixed costs (with a deduction limit of 20% of the leasing cost).

The opportunity given to the employee at the end of the leasing to purchase the company car also constitutes a taxable benefit in kind. Following recent Luxembourg Administrative Court of Appeal decision (N°33654c dated 25 September 2014) it has been decided to cap this benefit in kind. This new circular explains how to proceed in order to determine the taxable benefit in kind at the time of the repurchase:

- Calculation of a theoretical benefit: market value of the car minus the repurchase option price at the end of the lease
- Calculation of the capped benefit : global acquisition price of the car minus benefit in kind already taxed during the leasing period and potential contribution of the employee to the acquisition price
- Comparison of the theoretical and capped benefit: the lower of the two is the amount of benefit in kind subject to taxation.

New VAT Measures of the State Budget law

Circular L.I.R. N°773 of 29 December 2014

On 29 December 2014, the Luxembourg Tax Authorities issued a new Circular L.I.R. N°773 to clarify the amendment of the VAT law following the State Budget law for 2015.

Please see above National Legislation – new Budget law.

C L I F F O R D
C H A N C E

Luxembourg Contacts

Banking, Finance & Capital Markets

Christian Kremer
Managing Partner
T : +352 48 50 50 201
E : christian.kremer@
cliffordchance.com

Steve Jacoby
Partner
T : +352 48 50 50 219
E : steve.jacoby@
cliffordchance.com

Marc Mehlen
Partner
T : +352 48 50 50 305
E : marc.mehlen@
cliffordchance.com

Stefanie Ferring
Counsel
T : +352 48 50 50 253
E : stefanie.ferring@
cliffordchance.com

Audrey Mucciante
Counsel
T : +352 48 50 50 409
E : audrey.mucciante@
cliffordchance.com

Udo Prinz
Counsel
T : +352 48 50 50 232
E : udo.prinz@
cliffordchance.com

Corporate/M&A/ Private Equity

Christian Kremer
Managing Partner
T : +352 48 50 50 201
E : christian.kremer@
cliffordchance.com

Claudie Grisius
Partner
T : +352 48 50 50 280
E : claudie.grisius@
cliffordchance.com

Dunja Pralong-Damjanovic
Counsel
T : +352 48 50 50 222
E : dunja.pralong-damjanovic@
cliffordchance.com

Gavin Solomons
Of Counsel
T : +352 48 50 50 427
E : gavin.solomons@
cliffordchance.com

Investment Funds

Joëlle Hauser
Partner
T : +352 48 50 50 203
E : joelle.hauser@
cliffordchance.com

Paul Van den Abeele
Partner
T : +352 48 50 50 478
E : paul.vandenabeele@
cliffordchance.com

Caroline Migeot
Counsel
T : +352 48 50 50 258
E : caroline.migeot@
cliffordchance.com

Jacques Schroeder
Of Counsel
T : +352 48 50 50 217
E : jacques.schroeder@
cliffordchance.com

Isabelle Comhaire
Counsel
T : +352 48 50 50 402
E : isabelle.comhaire@
cliffordchance.com

Claude Eischen
Counsel
T : +352 48 50 50 268
E : claude.eischen@
cliffordchance.com

Olivier Poelmans
Counsel
T : +352 48 50 50 421
E : olivier.poelmans@
cliffordchance.com

Sébastien Schmitz
Counsel
T : +352 48 50 50 455
E : sebastien.schmitz@
cliffordchance.com

Litigation, Employment

Albert Moro
Partner
T : +352 48 50 50 204
E : albert.moro@
cliffordchance.com

Tax

François-Xavier Dujardin
Partner
T : +352 48 50 50 254
E : francois-xavier.dujardin@
cliffordchance.com

Worldwide contact information
36* offices in 26 countries

Abu Dhabi
Clifford Chance
9th Floor, Al Sila Tower
Abu Dhabi Global Market Square
PO Box 26492
Abu Dhabi
United Arab Emirates
T +971 2 613 2300
F +971 2 613 2400

Amsterdam
Clifford Chance
Droogbak 1A
1013 GE Amsterdam
PO Box 251
1000 AG Amsterdam
The Netherlands
T +31 20 7119 000
F +31 20 7119 999

Bangkok
Clifford Chance
Sindhorn Building Tower 3
21st Floor
130-132 Wireless Road
Pathumwan
Bangkok 10330
Thailand
T +66 2 401 8800
F +66 2 401 8801

Barcelona
Clifford Chance
Av. Diagonal 682
08034 Barcelona
Spain
T +34 93 344 22 00
F +34 93 344 22 22

Beijing
Clifford Chance
33/F, China World Office Building 1
No. 1 Jianguomenwai Dajie
Beijing 100004
China
T +86 10 6505 9018
F +86 10 6505 9028

Brussels
Clifford Chance
Avenue Louise 65
Box 2, 1050 Brussels
Belgium
T +32 2 533 5911
F +32 2 533 5959

Bucharest
Clifford Chance Badea
Excelsior Center
28-30 Academiei Street
12th Floor, Sector 1,
Bucharest, 010016
Romania
T +40 21 66 66 100
F +40 21 66 66 111

Casablanca
Clifford Chance
169 boulevard Hassan 1er
20000 Casablanca
Morroco
T +212 520 132 080
F +212 520 132 079

Doha
Clifford Chance
Suite B
30th floor
Tornado Tower
Al Funduq Street
West Bay
P.O. Box 32110
Doha, Qatar
T +974 4 491 7040
F +974 4 491 7050

Dubai
Clifford Chance
Building 6, Level 2
The Gate Precinct
Dubai International Financial Centre
PO Box 9380
Dubai, United Arab Emirates
T +971 4 362 0444
F +971 4 362 0445

Düsseldorf
Clifford Chance
Königsallee 59
40215 Düsseldorf
Germany
T +49 211 43 55-0
F +49 211 43 55-5600

Frankfurt
Clifford Chance
Mainzer Landstraße 46
60325 Frankfurt am Main
Germany
T +49 69 71 99-01
F +49 69 71 99-4000

Hong Kong
Clifford Chance
27th Floor
Jardine House
One Connaught Place
Hong Kong
T +852 2825 8888
F +852 2825 8800

Istanbul
Clifford Chance
Kanyon Ofis Binasi Kat. 10
Büyükdere Cad. No. 185
34394 Levent, Istanbul
Turkey
T +90 212 339 0000
F +90 212 339 0099

Jakarta**
Linda Widyati & Partners
DBS Bank Tower
Ciputra World One 28th Floor
Jl. Prof. Dr. Satrio Kav 3-5
Jakarta 12940
T +62 21 2988 8300
F +62 21 2988 8310

Kyiv
Clifford Chance
75 Zhylyanska Street
01032 Kyiv,
Ukraine
T +38 (044) 390 5885
F +38 (044) 390 5886

London
Clifford Chance
10 Upper Bank Street
London
E14 5JJ
United Kingdom
T +44 20 7006 1000
F +44 20 7006 5555

Luxembourg
Clifford Chance
10 boulevard G.D. Charlotte
B.P. 1147
L-1011 Luxembourg
T +352 48 50 50 1
F +352 48 13 85

Madrid
Clifford Chance
Paseo de la Castellana 110
28046 Madrid
Spain
T +34 91 590 75 00
F +34 91 590 75 75

Milan
Clifford Chance
Piazzetta M. Bossi, 3
20121 Milan
Italy
T +39 02 806 341
F +39 02 806 34200

Moscow
Clifford Chance
Ul. Gasheka 6
125047 Moscow
Russia
T +7 495 258 5050
F +7 495 258 5051

Munich
Clifford Chance
Theresienstraße 4-6
80333 Munich
Germany
T +49 89 216 32-0
F +49 89 216 32-8600

New York
Clifford Chance
31 West 52nd Street
New York
NY 10019-6131
USA
T +1 212 878 8000
F +1 212 878 8375

Paris
Clifford Chance
9 Place Vendôme
CS 50018
75038 Paris Cedex 01
France
T +33 1 44 05 52 52
F +33 1 44 05 52 00

Perth
Clifford Chance
Level 7
190 St Georges Terrace
Perth WA 6000
Australia
T +618 9262 5555
F +618 9262 5522

Prague
Clifford Chance
Jungamannova Plaza
Jungamannova 24
110 00 Prague 1
Czech Republic
T +420 222 555 222
F +420 222 555 000

Riyadh
Clifford Chance
Building 15, The Business Gate
King Khaled International Airport Road
Cordoba District, Riyadh
P.O. BOX: 90239
Riyadh 11613
Kingdom of Saudi Arabia
T +966 11 481 9700
F +966 11 481 9701

Rome
Clifford Chance
Via Di Villa Sacchetti, 11
00197 Rome
Italy
T +39 06 422 911
F +39 06 422 91200

São Paulo
Clifford Chance
Rua Funchal 418 15ºandar
04551-060 São Paulo-SP
Brazil
T +55 11 3019 6000
F +55 11 3019 6001

Seoul
Clifford Chance
21st Floor, Ferrum Tower
19, Eulji-ro 5-gil, Jung-gu
Seoul 100-210
Korea
T +82 2 6353 8100
F +82 2 6353 8101

Shanghai
Clifford Chance
40th Floor, Bund Centre
222 Yan An East Road
Shanghai 200002
China
T +86 21 2320 7288
F +86 21 2320 7256

Singapore
Clifford Chance
Marina Bay Financial Centre
25th Floor, Tower 3
12 Marina Boulevard
Singapore 018982
T +65 6410 2200
F +65 6410 2288

Sydney
Clifford Chance
Level 16, No. 1 O'Connell Street
Sydney NSW 2000
Australia
T +612 8922 8000
F +612 8922 8088

Tokyo
Clifford Chance
Akasaka Tameike Tower
7th Floor
2-17-7, Akasaka
Minato-ku
Tokyo 107-0052
Japan
T +81 3 5561 6600
F +81 3 5561 6699

Warsaw
Clifford Chance
Norway House
ul.Lwowska 19
00-660 Warsaw
Poland
T +48 22 627 11 77
F +48 22 627 14 66

Washington, D.C.
Clifford Chance
2001 K Street NW
Washington, DC 20006 - 1001
USA
T +1 202 912 5000
F +1 202 912 6000

*Clifford Chance's offices include a second office in London at 4 Coleman Street, London EC2R 5JJ. **Linda Widyati and Partners in association with Clifford Chance.

C L I F F O R D

C H A N C E

www.cliffordchance.com

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J201502160046635