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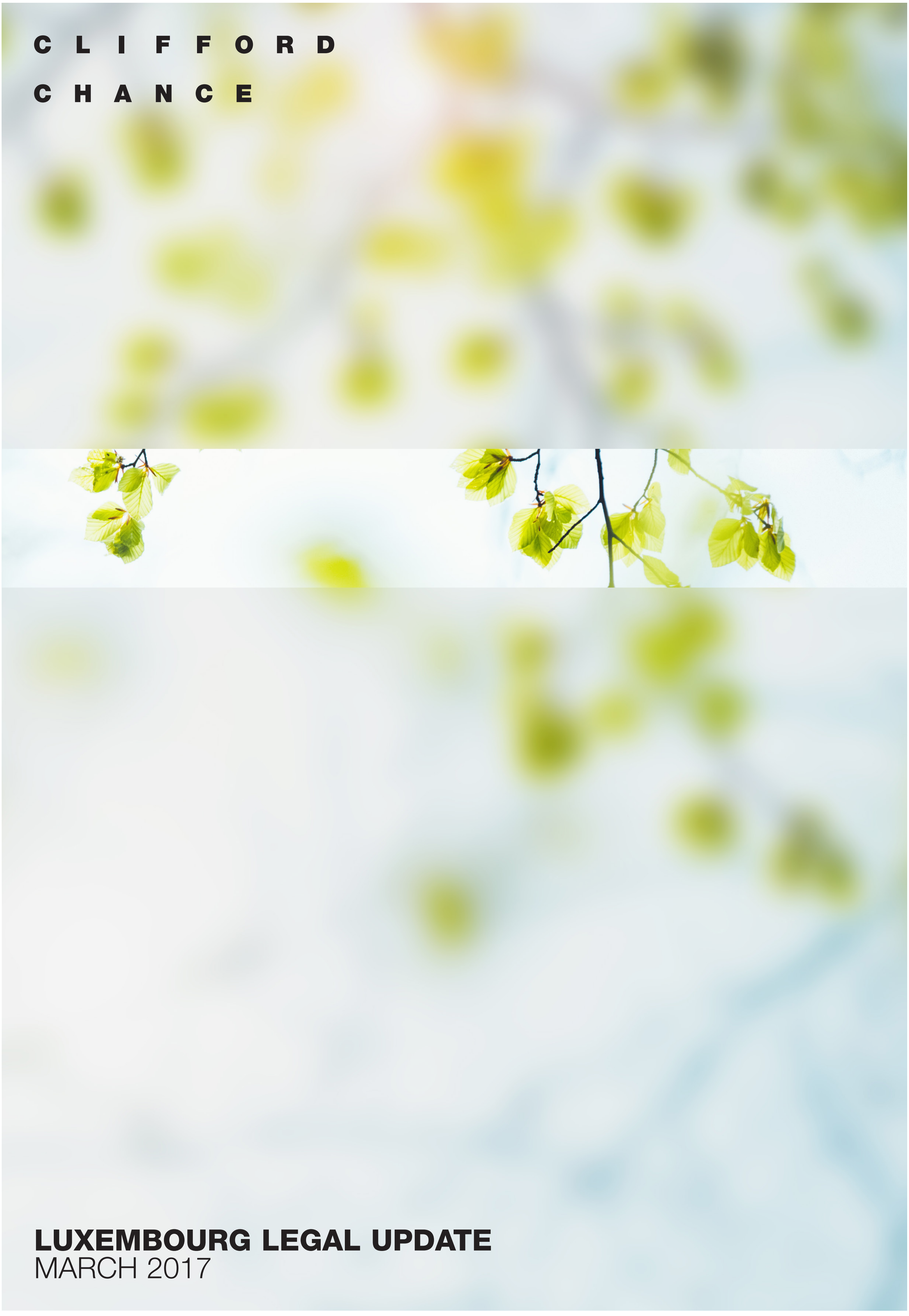

LUXEMBOURG LEGAL UPDATE
MARCH 2017

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BREXIT topic guide

Make sure to regularly visit our dedicated Brexit topic guide to keep up to date with the most recent developments relating to the outcome of the 23 June 2016 referendum in the UK.

Online resources

To view the **client briefings** mentioned in this publication, please visit our website www.cliffordchance.com

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

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

Banking, Finance and Capital Markets

International and EU Developments

New Delegated, Implementing and other EU Regulations and EU and International Texts

Over the past few months, a number of new Commission Delegated, Commission Implementing and other EU Regulations as well as EU and international texts have been published. These include, amongst others, the following:

Financial Stability Board (FSB):

- Annual lists of 21 November 2016 by the FSB regarding global systemically-important banks (G-SIBs) and global systemically-important insurers (G-SIIs)
- Basel Committee of Banking Supervision (BCSB):
- FAQs of 26 January 2017 on market risk capital requirements
- CRD IV/CRR:
- N°2016/2070 of 14 September 2016 laying down ITS for templates, definitions and IT solutions to be used by institutions when reporting to the EBA and to competent authorities
- N°2017/72 of 23 September 2016 supplementing the CRR with regard to RTS specifying conditions for data waiver permissions
- N°2017/180 of 24 October 2016 supplementing CRD IV with regard to RTS for benchmarking portfolio assessment standards and assessment-sharing procedures
- N°2017/208 of 31 October 2016 supplementing the CRR with regard to RTS for additional liquidity outflows corresponding to collateral needs resulting from the impact of an adverse market scenario on an institution's derivatives transactions
- N°2016/2358 of 20 December 2016 amending Implementing Decision 2014/908/EU as regards the lists of third countries and territories whose supervisory and regulatory requirements are considered equivalent for the purposes of the treatment of exposures
- N°2017/461 of 16 March 2017 laying down ITS with regard to common procedures, forms and templates for the consultation process between the relevant competent authorities for proposed acquisitions of qualifying holdings in credit institutions
- EBA list of public sector entities for the calculation of capital requirements of 18 November 2016
- SSM:
- ECB Guideline (EU) 2016/1993 of 4 November 2016 laying down the principles for the coordination of the assessment pursuant to the CRR and the monitoring of institutional protection schemes including significant and less significant institutions
- ECB Guideline (EU) 2016/1994 of 4 November 2016 on the approach for the recognition of institutional protection schemes for prudential purposes by national competent authorities pursuant to the CRR
- CRD V/BRRD II:
- EU Commission legislative proposals of 23 November 2016 intended to further strengthen the resilience of EU banks by amending CRD IV and CRR, as well as the BRRD and the SRMR
- MiFID2 and MiFIR:
- N°2016/2020 of 26 May 2016 supplementing MiFIR with regard to RTS on criteria for determining whether derivatives subject to the clearing obligation should be subject to the trading obligation
- N°2016/2021 of 2 June 2016 supplementing MiFIR with regard to RTS on access in respect of benchmarks

- N°2016/2022 of 14 July 2016 supplementing MiFIR with regard to RTS concerning the information for registration of third-country firms and the format of information to be provided to the clients
- ESMA Q&A paper of 18 November 2016 on transparency and markets structures topics under MiFID 2 and MiFIR

EMIR:

- N°2016/2227 of 9 December 2016 on the extension of the transitional periods related to own funds requirements for exposures to central counterparties set out in the CRR and EMIR
- N°2016/2251 of 4 October 2016 supplementing EMIR with regard to RTS for risk-mitigation techniques for OTC derivative contracts not cleared by a central counterparty
- N°2017/104 of 19 October 2016 amending Delegated Regulation (EU) 148/2013 supplementing EMIR with regard to RTS on the minimum details of the data to be reported to trade repositories
- N°2017/105 of 19 October 2016 amending Implementing Regulation (EU) 1247/2012 laying down ITS with regard to the format and frequency of trade reports to trade repositories according to EMIR
- N°2017/323 of 20 January 2017 correcting Delegated Regulation (EU) 2016/2251 supplementing EMIR with regard to RTS for risk-mitigation techniques for OTC derivative contracts not cleared by a central counterparty

CSDR:

- N°2017/389 of 11 November 2016 as regards the parameters for the calculation of cash penalties for settlement fails and the operations of CSDs in host Member States
- N°2017/390 of 11 November 2016 with regard to RTS on certain prudential requirements for central securities depositories and designated credit institutions offering banking-type ancillary services
- N°2017/391 of 11 November 2016 with regard to RTS further specifying the content of the reporting on internalised settlements
- N°2017/392 of 11 November 2016 with regard to RTS on authorisation, supervisory and operational requirements for central securities depositories
- N°2017/393 of 11 November 2016 laying down ITS with regard to the templates and procedures for the reporting and transmission of information on internalised settlements
- N°2017/394 of 11 November 2016 laying down ITS with regard to standard forms, templates and procedures for authorisation, review and evaluation of central securities depositories, for the cooperation between authorities of the home Member State and the host Member State, for the consultation of authorities involved in the authorisation to provide banking-type ancillary services, for access involving central securities depositories, and with regard to the format of the records to be maintained by central securities depositories
- ESMA Q&A paper of 13 March 2017 on the implementation of CSDR on improving securities settlement in the EU and on central securities depositories

PRIIPs:

- N°2016/2340 of 14 December 2016 amending PRIIPs as regards the date of its application (now: 1 January 2018)

AML/CTF:

- FATF Guidance on correspondent banking services of October 2016
- Final ESA guidelines of 18 November 2016 on anti-money laundering and counter-terrorist financing supervision

Solvency II:

- N°2017/309 of 23 February 2017 laying down technical information for the calculation of technical provisions and basic own funds for reporting with reference dates from 31 December 2016 until 30 March 2017 in accordance with Solvency II

Transparency Directive:

- ESMA practical guide of 3 February 2017 on national rules on notifications of major holdings under the Transparency Directive

Fintech:

- ESMA report of 7 January 2017 on the distributed ledger technology applied to securities markets
- IOSCO research report of February 2017 on the use and impact of financial technologies on the financial services industry

Legislation

Mortgage Credit Directive Implementation

Law of 23 December 2016 on Credit Agreements for Consumers Relating to Residential Immovable Property

A new law on credit agreements for consumers relating to residential immovable property and a supplementary Grand Ducal regulation modifying the regulatory part of the Luxembourg Consumer Code, entered into force. The law and regulation were both published in the *Mémorial* on 28 December 2016.

The law implements the Mortgage Credit Directive 2014/17/EU (MCD) in Luxembourg through new provisions in the Luxembourg Consumer Code, including, but not limited to:

- standard pre-contractual information for consumer borrowers through a European standardised information sheet (ESIS)
- a pre-contractual obligation to assess the creditworthiness of the consumer
- rules for the calculation of the annual percentage rate of charge (*taux annuel effectif global*)
- an early repayment right for consumers, in case of exercise of which, the creditor is entitled to compensation for the costs incurred, limited to a certain level.

The law applies to consumer credit agreements secured by either consumer mortgage or another comparable security or right on residential immovable property or to credit agreements the purpose of which is to acquire or retain property rights in land or in an existing or planned building. The law also introduces the immovable property credit intermediary in relation to such consumer credit agreements as a new category of a regulated financial sector professional, benefitting from the European passport under the MCD.

The Regulation contains an ESIS template, further specifications and instructions for its use and detailed rules for the calculation of the annual percentage rate of charge.

The law and the regulation entered into force on 1 January 2017, subject to certain rules of transitional and retroactive application.

MAR Supporting Legislation

Law of 23 December 2016 on Market Abuse

The law of 23 December 2016 on market abuse supporting the MAR and implementing the criminal sanctions for the MAD, as well as Commission Implementing Directive (EU) 2015/2392 on reporting to competent authorities of actual or potential infringements was published in the *Mémorial* on 27 December 2016.

The law repeals the Luxembourg market abuse law of 9 May 2006 that implemented the Market Abuse Directive 2003/6/EC in Luxembourg.

The law entered into force on 31 December 2016, subject to the transitional regime foreseen therein.

For more information on the CSMAD and MAR and on their impact on investment funds, please also refer to the July 2016 and November 2016 editions of our Luxembourg Legal Update.

Payment Accounts Directive Implementation

Bill N°7103

A new bill on payment accounts (Bill N°7103) was submitted to the Luxembourg Parliament on 16 December 2016.

The bill will implement Directive 2014/92/EU on the comparability of fees related to payment accounts, payment account switching and access to payment accounts with basic features, and modify the Luxembourg law of 15 December 2000 on postal financial services (as amended).

The publication of the bill constitutes the start of the legislative procedure.

Out-of-Court Complaints Resolution

CSSF Regulation N°16-07

CSSF Regulation N°16-07 relating to out-of-court complaint resolution adopted by the CSSF on 26 October 2016 was published in the *Mémorial* on 11 November 2016.

The new CSSF Regulation replaces CSSF Regulation N°13-02 and updates and amends the framework in which complaints are received and processed by the CSSF, amongst others with regards to:

- the complaints' admissibility requirements
- the timeframe for the different procedural steps
- the language in which the procedure is conducted

- the professionals' information obligations towards their clients.

The CSSF Regulation entered into force on 11 November 2016.

For more information on the new CSSF Regulation, please also refer to the November 2016 edition of our Luxembourg Legal Update.

CRD IV/CRR: Systemically Important CRR Institutions Authorised in Luxembourg

CSSF Regulation N°16-08

On 1 December 2016 the CSSF published a new regulation N°16-08 dated 8 November 2016 on systemically important institutions authorised in Luxembourg.

The CSSF sets out therein that no CRR institution authorised in Luxembourg is identified as a "global systemically important institution" (G-SII), within the meaning of the Financial Sector Law.

The new regulation further identifies six CRR institutions authorised in Luxembourg as "other systemically important institutions" (O-SIIs), and sets forth the capital buffer rates applicable to each of them with a gradual implementation over three years, as of 1 January 2016.

The new regulation entered into force on 1 January 2017.

CRD IV/CRR: Reciprocity of the Systemic Risk Buffer Rate

CSSF Regulation N°16-14

CSSF Regulation N°16-14 on the reciprocity of the systemic risk buffer rate of 1% adopted by the Central Bank of Estonia adopted by the CSSF on 19 December 2016 was published in the *Mémorial* on 27 December 2016.

The CSSF recognises and applies the systemic risk buffer rate of 1%, adopted by the Central Bank of Estonia in accordance with Article 133 of CRD IV, to both credit institutions authorised in Luxembourg, and to individual exposures located in Estonia exceeding the threshold of EUR 200 million.

CRD IV/CRR: Setting of Countercyclical Buffer Rate

CSSF Regulation N°16-15

CSSF Regulation N°16-15 on the setting of the countercyclical buffer rate for the first quarter of 2017 adopted by the CSSF on 21 December 2016 was published in the *Mémorial* on 27 December 2016.

The CSSF regulation provides that the countercyclical buffer rate applicable to the relevant exposures located in Luxembourg remains at 0% for the first quarter of 2017.

Eurosystem Refinancing and Eligible Guarantees: Modification of BCL Regulation

BCL Regulation 2016/N°22

A new regulation of the BCL 2016/N°22 was published in the *Mémorial* on 28 December 2016 and entered into force on 2 January 2017.

The regulation amends BCL Regulation 2014/N°18 to implement the modifications made to the ECB guideline on supplementary temporary measures concerning the refinancing operations of the Eurosystem and the eligibility of guarantees (ECB/2014/31).

Regulatory Developments

CRD IV/CRR: Central Administration, Internal Governance and Risk Management

CSSF Circular 16/647

On 22 December 2016, the CSSF issued Circular 16/647 updating CSSF Circular 12/552 on central administration, internal governance and risk management following the adoption of the EBA guidelines on limits on exposures to shadow banking entities that carry out banking activities outside a regulated framework under Article 395(2) of CRR (EBA Guidelines – EBA/GL/2015/20).

The EBA Guidelines entered into force as from 1 January 2017 and the CSSF states in its Circular that it has committed to fully comply with these guidelines. The EBA Guidelines apply to all CRR institutions to which the CRR large exposure provisions (Part IV) apply.

The EBA Guidelines define the notion of so-called "shadow banking entities" and specify the principles that institutions have to apply to manage and measure individual and concentration credit risk that can result from exposures on shadow banking entities. For these purposes, the EBA Guidelines specify the internal control principles on which institutions have to base their risk management. The EBA Guidelines also specify the manner in which exposures on shadow-banking entities shall be treated in the context of the regulation on large exposures under the CRR.

Shadow banking entities are defined in the EBA Guidelines as undertakings that:

- carry out credit intermediation activities, defined as bank-like activities involving maturity transformation, liquidity transformation, financing of investments with leverage, credit risk transfer or similar activities; and

- are neither within the scope of prudential consolidation nor subject to solo prudential requirements under specified EU legislation (or equivalent third country legal frameworks)

it being understood that entities referred to in Article 2(5) and Article 9(2) of CRD IV, as well as other entities defined as "excluded undertakings" in the EBA Guidelines are not to be regarded as shadow banking entities.

The EBA Guidelines also indicate that investment funds shall, in principle, be considered to fall within the scope of the definition of shadow banking entities, except if they are:

- UCITS
- AIFs meeting the criteria mentioned in the definition of excluded undertakings, i.e. AIFs with limited leverage and/or AIFs which are not entitled to grant loans or purchase third party lending exposure onto their balance sheet
- ELTIFs, EuVECAs and/or EuSEFs

unless the above investment funds qualify as Money Market Fund (MMF) within the meaning of the EU Commission's proposal for a regulation on MMFs (see in the Investment Funds section of this Luxembourg Legal Update). EBA considers that all MMFs, regardless of whether they operate under the rules of the UCITS Directive or other rules, shall be within the scope of the shadow banking entities definition for the purposes of the EBA Guidelines.

The Circular further modifies the risk management provisions of Circular 12/552, notably by introducing a new chapter in relation to the risks associated with so-called "shadow banking entities". The Circular finally invites institutions to update their internal processes and procedures in order to comply with the EBA Guidelines as from 1 January 2017, and encloses an updated version of, and showing the changes to, Circular 12/552.

MiFID/MiFIR: Transaction Reporting Obligation in MiFIR

CSSF Press Release 16/43

On 13 December 2016, the CSSF issued a press release on Article 26 of MiFIR. This provision obliges credit institutions and investment firms which execute transactions in financial instruments to report complete and accurate details of such transactions to the competent authority. The CSSF draws attention further to the draft regulatory technical standards for the reporting of transactions to the competent authorities (RTS 22) and further guidelines and technical reporting instructions provided by ESMA, which may still be modified.

The CSSF announces that it will implement forthcoming ESMA guidelines by way of a circular, that the CSSF's reporting system will be based on ESMA's technical reporting instructions, that the current file transport system will remain unchanged, and that there will be a transition period until 3 January 2018 after which the MiFID transaction reporting system will be switched off. The CSSF provides further information on transaction reporting by Luxembourg credit institutions and investment firms with branches in other Member States, and announces that it will provide further guidance on issues requiring national coordination in this context as soon as possible.

MAR: Delay in the Disclosure of Inside Information

CSSF Circular 16/646

On 20 December 2016, the CSSF issued circular 16/646 implementing the ESMA Guidelines on the delay in the disclosure of inside information in accordance with MAR.

The circular is addressed to all relevant issuers of financial instruments and entered into force on 20 December 2016.

MAR: ESMA Market Soundings Guidelines

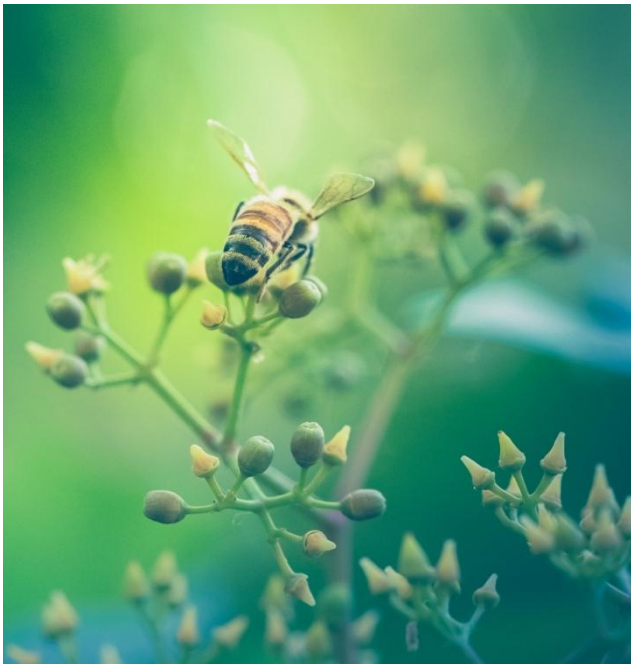
CSSF Circular 17/648

On 11 January 2017, the CSSF issued circular 17/648 on the implementation of ESMA guidelines on persons receiving market soundings (ESMA/2016/1477) under the MAR into Luxembourg regulation.

The circular is addressed to all market participants, in particular persons receiving market soundings, and sets out:

- factors that such persons have to take into account when information is disclosed to them as part of a market sounding in order to assess whether the information constitutes inside information
- steps that such persons should take if inside information has been disclosed to them in order to comply with Articles 8 and 10 of MAR
- records that should be maintained in order to demonstrate compliance with Articles 8 and 10 of MAR.

The circular entered into force on 11 January 2017.



MAR: ESMA Guidelines on information relating to commodity derivatives markets or related spot markets

CSSF Circular 17/653

On 14 March 2017, the CSSF issued circular 17/653 implementing the ESMA MAR guidelines – Information relating to commodity derivatives markets or related spot markets for the purpose of the definition of inside information on commodity derivatives (ESMA/2016/1480) into Luxembourg regulation.

The circular is addressed to all relevant market participants. It explains that the guidelines concern one of the criteria of the definition of inside information relating to commodity derivatives under Article 7(1)(b) of MAR: The guidelines provide in particular a non-exhaustive and indicative list of information which is reasonably expected or is required to be disclosed in accordance with the legal or regulatory provisions in Union or national law, market rules, contract, practice or custom, be it on the relevant commodity derivatives markets or on the spot markets as referred to in Article 7(1)(b) of MAR.

The circular entered into force on 14 March 2017.

BRRD: EBA Guidelines on the Provision of Information in Summary or Collective Form

CSSF Circular 17/649 and CSSF-CODERES Circular 17/3

On 9 February 2017, the CSSF and the Luxembourg Resolution Board (*Conseil de Résolution*) issued circular 17/649, respectively Circular 17/3, to implement the EBA guidelines on the provision of information in summary or collective form for the purposes of Article 84(3) of the BRRD (EBA/GL/2016/03).

The circulars are addressed to credit institutions, investment firms and financial conglomerates.

The circulars set out that, within the context of the professional secrecy obligation of, *inter alia*, resolution authorities and competent authorities, provided for in Article 84(1) of the BRRD, the EBA guidelines aim to establish certain factors to be taken into account in order to ensure that the information in summary or collective form is disclosed such that individual institutions or entities within the scope of the BRRD cannot be identified.

The EBA guidelines entered into force on 19 January 2017.

Single Resolution Board: Information Gathering for 2017 Ex-Ante Single Resolution Fund Contribution Calculation

CSSF-CODERES Circular 16/2

The CSSF acting for the Luxembourg Resolution Board (*Conseil de Résolution*) issued on 15 November 2016 Circular 16/2. The circular was addressed to all credit institutions subject to the SRM Regulation (EU) N°806/2014, and entered into force with immediate effect. By means of this circular, the Single Resolution Board gathered information for the calculation of the 2017 *ex ante* contributions according to Articles 4 and 14 of Commission Delegated Regulation (EU) 2015/63 to the Single Resolution Fund.

Deposit Guarantee Scheme: Survey on Amount of Covered Deposits Held Quarterly during 2016

CSSF-CPDI Circular N°16/04

On 23 November 2016, the CSSF, acting in its function as depositor and investor protection council (*conseil de protection des déposants et des investisseurs*) (CPDI) issued circular CSSF-CPDI 16/04 conducting a survey on the amount of covered deposits held quarterly during 2016.

The circular was addressed to all members of the Luxembourg deposit protection scheme *Fonds de garantie des dépôts Luxembourg* (FGDL). Members were requested to provide the data:

- at the level of their legal entity, comprising branches located within other Member States, for the 18 January 2017 at the latest
- for each and any branch located within other Member States separately, by 28 February 2017.

In order to transmit the data, institutions were kindly requested to complete the table attached to the circular, also available on the CSSF website.

The purpose of the data collection was to enable the CPDI to establish the FGDL's annual target level for 2017. The average amount of covered deposits calculated quarterly was further transmitted to the Single Resolution Board by 31 January 2017 and will be used to determine the Single Resolution Fund’s annual target level for 2017.

AML/CTF: Financial Intelligence Unit

2015 Annual Report

In November 2016, the Luxembourg Financial Intelligence Unit (FIU) (*Cellule de Renseignement Financier (CRF)*) of the State Prosecutor's Office to the Luxembourg District Court published its annual report for 2015.

The report sets out statistics on the FIU's activity during 2015, including, amongst others, statistics on suspicious transaction reports received during the past year, as well as information on main trends and phenomena in the area of money laundering and terrorism financing.

Furthermore, the report provides information on CRF's participation in the pilot project "cross border" initiated by the EU Commission and developed by FIU.net. This application, operational since March 2015, is used by all FIUs in the EU member states.

The 2015 report finally highlights that, from 1 January 2017, CRF uses goAML to receive all suspicious transactions reports. goAML is the United Nations Office on Drugs and Crime's (UNODC) standard software system available for FIUs to counter money laundering and terrorism financing.

AML/CTF: Blocking of Suspicious Transactions

CRF Guideline

On 31 December 2016, the CRF issued a new guideline on the blocking of suspicious transactions.

The guideline is addressed to all professionals subject to the law of 12 November 2004 on the fight against money laundering and combating the financing of terrorism, and aims to provide guidance on the status and management of blocked suspicious transactions.

The guideline sets out:

- the nature of transactions subject to an execution blocking
- the rights and obligations of professionals in case of blocked transactions
- the effects of a blocking
- the blocking procedure, i.e. in particular when a blocking occurs, how the FIU communicates its blocking instruction to the professional, and when such instruction ceases to have effect.

The guideline entered into force on 1 January 2017.

AML/CTF: Primary Tax Offences

CSSF Circular 17/650

On 17 February 2017, the CSSF issued circular 17/650 on the application of the AML Law and the related implementing Grand Ducal regulation on primary tax offences.

The circular, jointly prepared with the CRF, is addressed to all CSSF-supervised professionals subject to the AML Law. It has been released in the context of the law of 23 December 2016 on the Luxembourg fiscal reform 2017, which introduced, as of 1 January 2017, serious tax offence (*fraude fiscale aggravée*) and tax fraud (*escroquerie fiscale*) as primary tax offences pursuant to Article 506-1 of the Luxembourg Criminal Code.

The circular provides practical guidance for professionals when implementing the AML Law, and establishes a list of indicators relevant when reporting suspicious transactions related to the new primary tax offences.

In particular, the circular specifies the scope of customer due diligence requirements for new, existing and closed business relationships with resident and non-resident clients. It further points out that internal policies, procedures and measures need to be extended to cover primary tax offences, and provides additional practical guidance on the reporting of suspicious transactions to the competent authorities.

The circular entered into force on 17 February 2017.

MCD: Law of 23 December 2016 on Credit Agreements for Consumers Relating to Residential Immovable Property

CSSF Circular 17/651

On 22 February 2017, the CSSF issued circular 17/651 on the law of 23 December 2016 on credit agreements for consumers relating to residential immovable property and transposing the MCD in a new Chapter 6 of the Luxembourg Consumer Code.

Pursuant thereto, the CSSF is appointed as competent authority for the execution of Chapter 6 of the Consumer Code.

The circular, addressed to all CSSF-supervised professionals, presents the new Chapter 6 and highlights the entry into force of several guidelines issued by the EBA in relation to pre-contractual information requirements for real estate loans, information on interest rates, execution and enforcement, as well as real estate consumer credit intermediaries (including conduct of business rules and educational requirements). It further sets out the features of the representative example (*exemple représentatif*) provided for in Article L. 226-6(2) of the Consumer Code on the publicity of credit agreements relating to immovable property.

More specifically, the circular also points out that the provisions of Chapter 6 of the Consumer Code are mandatory and any clause or combination of clauses in the credit agreement contrary to these provisions may be declared void.

The circular finally clarifies the staggered entry into force of the various provisions of the new Chapter 6.

The circular entered into force on 22 February 2017.

MCD: Real Estate Consumer Credit Intermediaries

CSSF Press Release 17/09

On 28 February 2017, the CSSF issued a press release announcing the introduction of the new regulated profession of real estate consumer credit intermediaries by the law of 23 December 2016 on credit agreements for consumers relating to residential immovable property.

The CSSF highlights that real estate consumer credit intermediary activities are subject to a prior authorisation requirement granted by the Minister of Finance following an instruction of the file by the CSSF. In order to obtain authorisation and benefit from the European passport, applicants must produce evidence of their professional reputation, of an appropriate level of knowledge and experience in the field of real estate consumer credit agreements, as well as of a central administration located in Luxembourg.

Professionals exercising the activity of a real estate consumer credit intermediary prior to the entry into force of the law had until 21 March 2017 to comply with the new requirements.

Authorised credit intermediaries are subject to the supervision of the CSSF, which disposes of sanction powers, including the power to impose an administrative fine of up to EUR 250,000.

Transparency Law: Enforcement of the 2016 Financial Information Published by Issuers

CSSF Press Release 17/03

On 16 January 2017, the CSSF issued a press release on the enforcement of the 2016 financial information published by issuers subject to the Transparency Law.

The CSSF draws the attention of issuers and auditors on identified financial reporting topics which should be taken into consideration when preparing and auditing, respectively, the International Financial Reporting Standards (IFRS) financial statements for the year ending 31 December 2016.

The CSSF sets out several criteria, on the basis of which it is going to perform its analysis. The press release discusses the priorities governing the CSSF's enforcement campaign, in particular on presentation of financial performance, the distinction between equity instruments and financial liabilities, business combinations, continued uncertainty in financial markets conditions and disclosures of the impact of the new standards on IFRS financial statements.

Solvency II: Technical Interest Rates Applicable to Reinsurance Undertakings

CAA Circular 16/10

On 24 October 2016, the CAA issued circular 16/11 modifying circular letter 15/12 on the annual review by the CAA of the technical interest rates applicable to reinsurance undertakings.

Solvency II: Filing of the First Report on the Own Risk and Solvency Assessment (ORSA)

CAA Information Note of 4 November 2016

On 4 November 2016 the CAA issued an information note on the ORSA.

The information note is a reminder that, in line with the provisions of the Solvency II guidelines published by the European Insurance and Occupational Pensions Authority on 14 September 2015, which the CAA fully endorses, Luxembourg insurance and reinsurance undertakings need to prepare an ORSA report at least once per year.

The CAA sets out the formalities and deadlines for the submission of such a report.

The information note finally provides that supervised undertakings, having already prepared a report but which has not yet been approved by their boards of directors, are invited to provide a copy of such report to the CAA and to subsequently provide the CAA with the approved report once available.

Solvency II: Maximum Technical Interest Rates Applicable to New Life Insurance Contracts

CAA Circular 16/12

On 25 November 2016, the CAA issued circular 16/12 modifying and supplementing the amended circular letter 98/1 on technical interest rates by redefining the most common maximum technical interest rates being used for calculating the technical provisions for new life insurance contracts applicable as of 1 January 2017.

The last general determination of the technical interest rates had been made by CAA circular 15/7 dated 13 May 2015. The redefinition of such rates in relation to certain currencies has to be seen against the background of a continuous decrease of interest rates since then for such currencies.

Solvency II: Modifications to Exemption Conditions for Providing Information on External Ratings in Detailed Reports on Investments and Derivatives

CAA Circular 17/1

On 8 February 2017, the CAA issued circular 17/1 modifying its circular 16/5 specifying the exemption conditions for providing information on external ratings in the detailed reports on investments and derivatives.

The circular, addressed to insurance and reinsurance undertakings, extends the exemption from reporting information on external ratings in the reports on investments and derivatives, provided for in circular 16/5, to the reporting due in the course of 2017. According to the CAA, this extension is required since there has been no development, for the time being, towards an overall solution on how to avoid the disproportionate costs for insurance and reinsurance undertakings due to such reporting.

The circular entered into force on 8 February 2017.

Solvency II: Yearly Reporting of Reinsurance Undertakings

CAA Circular 17/2

On 28 February 2017, the CAA issued circular 17/2 modifying the amended circular letter 99/6 on the yearly reporting of reinsurance undertakings.

The circular, addressed to reinsurance undertakings, makes minor amendments to the annual reporting tables for reinsurance undertakings (table A on general expenses, table E on gross provisions, information sheets, abolition of triangular tables on provisions for incurred but not declared accidents, updating cross-references to the amended insurance sector legislation) to adapt them to the new Solvency II requirements.

The circular also abolishes and replaces circular 16/3 and applies, for the first time, to the 2016 annual accounts.

Solvency II: Separate Report by External Auditor of Reinsurance Undertakings

CAA Circular 17/3

On 28 February 2017, the CAA issued circular 17/3 modifying the amended circular letter 09/2 on the separate report to be provided by the external auditor of reinsurance undertakings.

In particular, the circular makes some formal amendments to Circular 09/2 due to the new Solvency II regime.

The circular further sets out new rules as regards the transmission of the separate report to the CAA: Part 1 of the report shall be henceforth transmitted via one of the SOFiE/E-File secured transmission channels, instead of via encrypted email; Part 2 of the report shall, in addition to transmission to the CAA via email, be also submitted via SOFiE/E-File.

The circular also abolishes and replaces circular 13/5 and applies, for the first time, to the 2016 separate report.

Solvency II: Annual Report by Insurance Brokers

CAA Circular 17/4

On 9 March 2017, the CAA issued circular 17/4 on the annual reporting (*compte rendu*) by insurance brokers (natural persons and legal entities).

The circular abolishes and replaces circular 12/6, given the necessity to update the terminology in order to bring it in line with the amended insurance sector legislation post Solvency II implementation and with the aim to improve the statistical value of the data provided. The circular further amends the existing reporting template by extending the scope of information brokers have to provide on their employees and other collaborators, and introducing a requirement to provide information on brokerage agreements concluded with insurance undertakings. Finally, the circular contains general guidance on the reporting as well as detailed item by item explanations on the information to be provided in the different modules of the reporting template.

The circular applies for the first time to the 2016 report due to be provided to the CAA on 28 April 2017.

The New Market Abuse Law

"The new Luxembourg law of 23 December 2016 *relative aux abus de marché* (the "**New Market Abuse Law**") has officially repealed the former Luxembourg law of 9 May 2006 on market abuse, as amended (the "**Former Market Abuse Law**").

The New Market Abuse Law implements into Luxembourg law Directive 2014/57/EU of the European Parliament and of the Council of 16 April 2014 on criminal sanctions for market abuse, which has also been known as the *Market Abuse Criminal Sanctions Directive*, as well as Commission Implementing Directive (EU) 2015/2392 of 17 December 2015 on Regulation N°596/2014 of the European Parliament, and of the Council as regards reporting to competent authorities of actual or potential infringements of that Regulation.

With the entry into force of the New Market Abuse Regulation, Luxembourg has now effectively implemented the entire new market abuse regime introduced by Regulation (EU) N°596/2014 of the European Parliament and of the Council of 16 April 2014 on market abuse (the "**Market Abuse Regulation**") together with its related implementing and delegated regulations, the Market Abuse Regulation having already come into force on 3 July 2016 and being directly applicable in Luxembourg.

The principal differences introduced by the New Market Abuse Law are, among others, the following ones:

Sanctions corresponding to the New Scope of the Market Abuse Regulation

The New Market Abuse Law extends the scope of application of the former rules to the much wider scope of application set out in the Market Abuse Regulation, particularly with respect to relevant trading venues (the scope of application of the Market Abuse Regulation in addition to regulated markets also encompasses multilateral trading facilities (MTFs) and other types of organised trading facilities (OTFs). Additionally, the Market Abuse Regulation applies to emission allowances or auction products based thereon, spot commodity contracts and related financial instruments and benchmarks.

Therefore, the widened scope of prohibited actions pursuant to the Market Abuse Regulation has now been duly reflected by the list of potential sanctions set out in the New Market Abuse Law.

Increased Administrative and Criminal Sanctions

Administrative (i.e. non-criminal) sanctions will not exceed the minimum limit that Member States have to establish as a minimum measure pursuant to the Market Abuse Criminal Sanctions Directive. However, both the administrative and the criminal sanctions provided for in the New Market Abuse Law have increased considerably to ensure compliance with market abuse rules. Serious forms of market abuse, in particular offences committed intentionally, potentially entail criminal sanctions. Sanctions can be imposed in this respect on both natural and legal persons.

Due to the coexistence of administrative and criminal sanctions, the New Market Abuse Law contains a detailed consultation procedure between the CSSF and the state prosecutor.

Supervisory Powers

The New Market Abuse Law also extends the supervisory and investigatory powers of the administrative authorities responsible for the prevention of market abuse, in particular the powers of the CSSF. The CSSF has now been empowered to consult with external experts in connection with specific questions which arise during an inquiry/investigation with respect to any infringement of the provisions of the Market Abuse Regulation.

Amendment of the Luxembourg Transparency Law

Issuers, for which Luxembourg is the home Member State for the purposes of Directive 2004/109/EC of the European Parliament and of the Council of 15 December 2004 on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market and amending Directive 2001/34/EC, as amended (the "**Transparency Directive**"), must take into account that the definition of the notion of regulated information has now been extended by the coming into force of the New Market Abuse Law as it now also includes the notifications which an issuer (or any other person having applied for the admission to trading on a regulated market of securities without the relevant issuer's consent) is required to disclose for the purposes of the so-called *PDMR Notifications* set out in Article 19 of the Market Abuse Regulation (i.e. transactions conducted by persons discharging managerial responsibilities and persons closely associated with them).

Consequently, such information must be treated as regulated information by:

- publishing it pursuant to effective dissemination methods
- storing it with the OAM operated by the Luxembourg Stock Exchange
- filing it with the CSSF in its capacity as Luxembourg's transparency supervisory authority.

Case Law

Loan – Absence of Repayment Date

Luxembourg District Court, 7 May 2015, N°68561

Fraud and Mistake – Subscription Order – Investment Advice – Investment in Shares Representing an Exceptional Risk

Court of Appeal, 4 February 2016, N°40600

Financial Collateral Directive – Possession and Control – Insolvency

ECJ, 10 November 2016, C 156/15[1]

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

[1] For a more detailed analysis, please refer to Clifford Chance London Client Briefing November 2016.

Corporate

Circulars / Regulatory Developments

CSSF Regulation N°16-12 of 21 November 2016

Since the enactment of the law of 18 December 2009, the CSSF has been in charge of the supervision of the audit profession and has issued several recommendations and circulars in this respect.

On 5 December 2016, the CSSF published five Regulations (Regulations N°16-09, N°16-10, N°16-11, N°16-12 and N°16-13) on the enforcement of the Law of 23 July 2016 transposing the EU Directive 2014/56 on Audit Profession and the Regulation (EU) N°537/2014 of 16 April 2014 on specific requirements regarding the statutory audit of public-interest entities.

The Law of 23 July 2016 transposing the Directive 2014/56/EU on statutory audits (audits of annual accounts or consolidated accounts) and the EU Regulation 537/2014 on the specific requirements applicable to the statutory audit of public interest entities was published in the *Mémorial* on 28 July 2016 and entered into force on 1 August 2016.

Key changes of the European rules may be summarised as follows:

- open the European Market of the Audit services
- resolve the weaknesses of the Audit identified in light of the financial crisis
- increase the quality of Audit
- increase transparency
- prevent conflict of interest.

A particular focus should be put on the Regulation N°16-12 relating to the audit profession (abridging the former regulation N°13-01 on the audit profession) whereby

- it updates the international accounting rules which are applicable in Luxembourg
- provides some guidance to independent approved auditors with respect to these activities and updates the code of deontology for the audit profession.

Update of international accounting rules (ISA)

According to regulation N°16-12, the "Introduction" part, the "Objective" part, the "Definition" part and the "Requirements" part of the international accounting rules (ISA) as established by the International Auditing and Assurance Standards Board (IAASB) and published in the "Handbook of International Quality Control, Auditing, Review, Other Assurance, and Related Services Pronouncements – 2015 Edition" of the International Federation of Accountants (IFAC) are now applicable in Luxembourg with regard to the audit profession as of 17 June 2016. An anticipatory implementation of these rules is possible.

Update of the code of ethics of the audit profession

The CSSF clarifies the International Standard on Quality Control (ISQC 1) established by the International Auditing and Assurance Standards Board (IAASB) and published in the "Handbook of International Quality Control, Auditing, Review, Other Assurance, and Related Services Pronouncements – 2015 Edition" of the International Federation of Accountants (IFAC) applicable in Luxembourg.

The CSSF also confirms the application of the deontology code adopted in 2015 and subsequently amended on 29 May 2015 by the International Ethics Standards Board for Accountants (IESBA) to the audit profession in Luxembourg.

As to the medium-term objective, the European legislator wishes to make all legal control of accounts governed by those international accounting rules adopted by the European Commission.

Penalties for Late Publication to the Luxembourg Trade and Companies Register

RCSL Circular 16/03 of 11 November 2016

The purpose of the circular N°16/03, published on 11 November 2016, is to set out the details of the implementation of the extra fees for late publication of financial data to the Luxembourg Trade and Companies Register (RCSL). These penalties are applicable as of 1 January 2017.

Any legal entities which have not filed their financial information within the time limits prescribed by law will support an increase of the fees.

Scope of the circular

The publications that are targeted by the circular are:

- the annual accounts
- the consolidated accounts.

The penalties only apply to legal entities, to the exclusion of certain types of associations, including the following:

- Non-profit associations
- Foundations.

Assessment of the late publication

The assessment of the late publication depends on the following objective criteria:

- the date of closing of the relevant financial year
- the maximum legal period of time of seven months prescribed by law to file the financial statements, starting from the date of the closing of the financial year for the companies
- the date at which the company submit its request of publication to the RCSL.

Costs

Annex J of the amended Grand Ducal regulation of 23 January 2003 determines the costs for filing on time and for late filing as follows:

- EUR 19 for on-time filing
- EUR 50 for one month of delay
- EUR 200 for between two and four months of delay
- EUR 500 for more than four months of delay.

Case Law

Labour – Employment Contract – Combination of a Corporate Mandate with an Employment Contract – Conditions – Subordination Relationship – Sole director (no) – Art. L.121-1 Labour Code – Law of 10 August 1915, Art.51

Court of Appeal, 12 November 2014, N°40366

Commercial Companies – Voluntary Liquidation – Complete Settlement of Liabilities – Provision for Potential Future Liabilities – Liability of the Liquidator –

Discharge Given by Shareholders – Third Party Action – Law of 10 August 1915, Art.147 to 149

Court of Appeal, 21 January 2015

Commercial Companies – Public Limited Liability Company – Responsibility of the directors – *Actio Mandati* – Action suit from the Company – Free Decision – Requirement – General Shareholders' Meeting – Law of 10 August 1915, Art.59 and 63

District Court, 26 February 2015, N°136378

Transfer of Branch of Activity – Notary Deed – Absence of Capacity to Act – Transfer of all Assets and Liabilities – Law of 10 August 1915, Art.285 to 308

Court of Appeal, 1 April 2015, N°39461

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

Employment

Law of 28 October 2016 on Professional Qualifications Recognition

The law of 28 October 2016 on professional qualifications recognition[2], which entered into force on 18 November 2016, implements the Directive 2013/55/EU of 20 November 2013 on the recognition of professional qualifications.

This new law aims at reducing and facilitating the steps and rules relating to the recognition of professional qualifications acquired by a person in a EU Member State, for the purpose of strengthening the freedom of movement of workers and, therefore, facilitating access to a regulated profession in Luxembourg.

The principal modifications introduced by the Directive of 2013 and faithfully implemented in national law by the new law are, amongst others:

- the recognition of professional qualifications of the holders of certain academic titles in a Member State
- the recognition of professional internships performed in another Member State, to the extent that the access to a regulated profession in that Member State is also subject to the completion of a professional internship
- the limit of the control of language skills to the knowledge of an official or administrative language of the host Member State
- the introduction of a European professional card delivered on demand.

Reform of the Organization of the Criminal Records

As from 1 February 2017 and the entry into force of the law dated 23 July 2016 amending the law dated 29 March 2013 regarding the organization of criminal records and the exchange of information included in the criminal record between Member States of the EU (the "2013 Law"), the employer's right to request a criminal record from a candidate/employee has been restricted.

[2] Memorial A N°231 of 2016

The following provisions of the 2013 Law are worth to mention:

- As a general principle, the employer may only request from the candidate/employee to be provided with the 3rd category of criminal record ("bulletin N°3") (The criminal record will now be divided into 5 different categories ("bulletins") each reporting different information – Bulletin N°3 will contain information on certain crimes). However in specific cases, where a driving license is specifically required for the job, the employer may also request from the candidate/employee to be provided with the 4th category of criminal record ("bulletin N°4").
- The employer's request to be provided with the candidate/employee's criminal record must be made in writing. The relevance of the request with regard to the employee's position must be evidenced (i.e. such a request cannot be made for all positions and it will be incumbent on the employer to evidence that the production of the criminal record is justified in light of the role/function to be fulfilled by the candidate ("proportionate test")) . The fact that the criminal record will be requested from the candidate must already be stated in the job offer (and hence also in the *déclaration de poste vacant*).
- During the employment relationship, the employer may only request to be provided with the employee's criminal record:
  - when legally provided
  - in case of a change of the employee's position justifying a new control of the employee's integrity and respectability.
- Period of retention of the criminal record:
  - one month as of the conclusion of the employment contract
  - immediate destruction if no hiring of the candidate
  - in case the criminal record is provided during the employment relationship: two months from its production except if otherwise provided for by law.
- Infringements to the provisions of the 2013 Law are criminally sanctioned.

Funds and Investment Management

International and EU Developments

UCITS

ESMA Opinion on UCITS Share Classes

Following the consultations which were organised in December 2014 and April 2016, ESMA issued its final opinion on the common principles for the setting up of share classes in UCITS on 30 January 2017[3].

In its opinion, ESMA has identified four high-level principles that should be observed by UCITS when setting up different share classes, as summarised below.

Common Investment Objective

Share classes of the same UCITS fund (or sub-fund) should have a common investment objective reflected by a common pool of assets. In this respect, ESMA indicates that hedging arrangements at share class level are not compatible with the requirement for a fund (or sub-fund) to have a common investment objective, with the exception of currency risk hedging which is accepted by ESMA at the level of a share class.

[3] ESMA34-43296

Non-Contagion

UCITS management companies should implement appropriate procedures to minimise the risk that features specific to one share class could have a potentially adverse impact on other share classes of the same fund (or sub-fund).

In particular, ESMA points out that, due to the lack of asset segregation between share classes, the potential counterparty risk inherent to a derivative contract could "contaminate" other share classes. Hence, any additional risk introduced to the fund (or sub-fund) through the use of a derivative overlay should be mitigated and appropriately monitored, and it should be ensured that the risk is only borne by the investors in the respective share class in the event of its materialisation.

In this respect, ESMA recommends that the following minimum operational principles are observed by UCITS management companies in order to minimise the additional risk of contagion linked to the currency hedging:

- to limit the amount of collateral engaged in the derivative agreement to the maximum pool of collateral on which the investors of the share class have a claim
- to put in place proper operational and accounting segregation of assets, liabilities and profit/loss to the respective share classes on an ongoing basis, and, at the very least at the same valuation frequency of the fund
- to implement stress tests to quantify the impact of losses (relating to share class-specific assets that exceed the value of the respective share class) on all investor classes
- to implement the derivative hedge according to a detailed, pre-defined and transparent hedging strategy.

Moreover, to nonetheless ensure that the above operational principles are met, ESMA takes the view that UCITS management companies should, at the level of the share class with a derivative overlay:

- ensure that the exposure to any counterparty of a derivative transaction is in line with the limits laid down in Article 52 of the UCITS Directive in respect to the net asset value of the share class
- ensure that over-hedged positions do not exceed 105% of the net asset value of the share class
- ensure that under-hedged positions do not fall short of 95% of the portion of the net asset value of the share class which is to be hedged against currency risk
- keep hedged positions under review on an ongoing basis, at least at the same valuation frequency as the fund, to ensure that over-hedged or under-hedged positions do not exceed/fall short of the permitted levels stated above
- incorporate a procedure in said review to rebalance the hedging arrangement on a regular basis to ensure that any position stays within the permitted position levels stated above and is not carried forward from month to month.

Pre-Determination

All features of the share class should be pre-determined before the fund (or sub-fund) is set up in order to allow the potential investor in the fund (or sub-fund) to gain a full overview of the rights and/or features attributed to his investment.

In share classes with hedging arrangements, this pre-determination should also apply to the currency risk which is to be hedged out systematically, meaning that there should be no discretion of the UCITS management company/self-managed SICAV in regard to the risk to be hedged. However, according to ESMA, this does not limit the UCITS management company/self-managed SICAV discretion as to the type of derivative instrument used to hedge the currency risk, nor its operational implementation.

Transparency

Differences between share classes of the same fund (or sub-fund) should be disclosed to investors when they have a choice between two or more classes in order to allow them to be informed about the existence and nature of all existing share classes, whether they invest in this share class or not. According to ESMA, new and existing investors should be informed about the creation and existence of such share classes in a timely fashion, including updates in periodic reports.

ESMA is also of the view that the following operational principles should be observed by a fund (or sub-fund) with multiple share classes in order to ensure a common level of transparency vis-à-vis all their investors:

- the information about existing share classes should be made available in the prospectus
- the management company should provide and maintain an up-to-date list of share classes with a contagion risk in the form of readily available information which should be kept up-to-date

- the stress tests results should be made available to national competent authorities upon request.

Transitional Provisions

ESMA considers that share classes established prior to 30 January 2017 and which do not comply with the above principles should be allowed to continue in order to mitigate the impact on investors. However, such share classes should be closed to subscriptions by new investors by 30 July 2017 and to additional subscriptions by existing investors by 30 July 2018.

ESMA Updated Q&As on UCITS Directive

On 21 November 2016, ESMA published an updated version of its Q&A on the application of the UCITS Directive[4], in which ESMA clarifies that the following investment limits should apply at sub-fund level rather than at umbrella fund level when a UCITS invests in an umbrella fund:

- The limit laid down in Article 56(2)(c) of the UCITS Directive (according to which a UCITS may acquire no more than 25% of the units of any single UCITS or other UCI) should apply at the level of the individual sub-fund of the umbrella UCITS/other UCI, the units of which are to be acquired.
- The limit laid down in Article 55(1) of the UCITS Directive (according to which a UCITS may acquire the units of UCITS or other UCIs referred to in Article 50(1)(e) provided that no more that 10% of its assets are invested in units of a single UCITS or other UCI) should also apply at the individual sub-fund level rather than at the umbrella fund level.

AIFMD

ESMA Updated Q&As on AIFMD

On 16 November and 16 December 2016, ESMA published updated versions of its Q&A on the application of the AIFMD[5], including new questions and answers on the cross-border marketing of AIFs, the delegation of functions by AIFMs to AIFs or third parties, and the reporting obligations by non-EU AIFMs.

Cross-Border Marketing of AIFs

As regards the cross-border marketing of AIFs, ESMA clarifies that:

- Where an AIF is marketed in a host Member State by way of the AIFMD marketing passport, the creation of a new class of shares/units, which is to be marketed cross-border within an already notified AIF or AIF's sub-fund, does not constitute a material change that would require a new notification pursuant to Article 32 of the AIFMD.
- When an AIFM wishes to notify a material change to a notification made to the competent authority of its home Member State, the AIFM must provide the full set of information and documentation required by Articles 32 and 33 of the AIFMD, and must also highlight the information which differs from the first notification letter and its related documents.

Delegation of Functions by AIFMs

As regards delegation, ESMA clarifies that an externally managed AIF cannot perform itself the functions listed in Annex I of AIFMD (including, amongst others, the risk management and portfolio management functions) or be considered as a third party to whom the appointed external AIFM could delegate these functions, since the AIF is not itself regulated as an AIFM. On the contrary, an internally managed AIF is allowed to perform the functions listed in Annex I of AIFMD.

Surprisingly, ESMA also indicates that where a function listed in points 1 and 2 of Annex I of the AIFMD is not performed by the AIFM itself (thus including also administration, marketing and other services relating to the AIF's assets), this function should be considered as being delegated by the AIFM to the third party who is performing such function. According to ESMA, the AIFM should thus not be released from, but should remain responsible for, ensuring compliance with the delegation requirements set out in Article 20 of AIFMD even for these functions as well as with the principle expressed in Article 5(1) of AIFMD according to which the single AIFM appointed for an AIF is responsible for ensuring compliance with the AIFMD. There have been some discussions in the industry recommending to wait and see how national competent authorities will apply ESMA's Q&A before AIFMs take action in this respect to the extent that ESMA's position seems contrary to the one that most national competent authorities and the market have taken so far.

[4] ESMA/2016/1586
[5] ESMA/2016/1576 and ESMA/2016/1669

Reporting Obligations by Non-EU AIFMs

As regards reporting obligations by non-EU AIFMs, ESMA clarifies the circumstances under which information on EU master AIFs should be reported to competent authorities under Article 42 of AIFMD. According to ESMA, AIFMs should also report information on non-EU master AIFs not marketed in the EU that have either EU feeder AIFs or non-EU feeder AIFs marketed in the EU under Article 42. Non-EU AIFMs should apply the same principle if the master AIF is established in the EU and not marketed in the EU (i.e., they should report information on the EU master AIF not marketed in the EU).

PRIIPs

PRIIPS KID Regulation published

Regulation (EU) 2016/2340 of 14 December of the EU Parliament and Council, amending the PRIIPs KID Regulation as regards its date of application, was published in the Official Journal on 23 December 2016 and entered into force on 24 December 2016.

As a result, the PRIIPs KID Regulation will now be applied from 1 January 2018, instead of 31 December 2016 as initially stipulated. This one-year delay will enable regulatory technical standards to be defined, and is expected to leave sufficient time for the industry to adapt to the new rules.

EU Commission Draft RTS

On 8 March 2017, the EU Commission adopted a revised draft delegated regulation supplementing the PRIIPs KID Regulation by laying down regulatory technical standards (RTS) with regard to the presentation, content, review and revision of KIDs for packaged retail and insurance-based investment products (PRIIPs).

This revised draft delegated regulation follows the EU Parliament's decision in September 2016 to reject the original RTS adopted by the EU Commission in June 2016 and to return them to the EU Commission for revision. The EU Commission's key amendments concern multi-option PRIIPs, performance scenarios, comprehension alert and presentation of administrative costs in relation to biometric components of insurance-based investment products.

The EU Parliament and Council have now to approve the revised draft delegated regulation that is due to apply as from 1 January 2018.

For more information on the PRIIPs KID Regulation and its implementing measures, please refer to the July 2016 edition of our Luxembourg Legal Update and to our last briefing papers Implementing PRIIPs – the uncertainty persists and The PRIIPs KID Regime.

AML/CTF

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

EMIR

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

MiFID 2/MiFIR

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

Transparency Directive

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

Other Relevant Topics

FSB Recommendations concerning Structural Vulnerabilities from Asset Management Activities

On 12 January 2017, the Financial Stability Board (FSB) published its final policy recommendations to address structural vulnerabilities from asset management activities.

As a reminder, the FSB published proposed policy recommendations for public consultation in June 2016, to which ALFI responded. The final recommendations published in January 2017 reflect a number of changes to the recommendations proposed initially and sets out 14 final policy recommendations to address the following structural vulnerabilities from asset management activities that could potentially present financial stability risks:

- *Liquidity mismatch between fund investments and redemption terms and conditions for open-ended fund units*: These recommendations are designed to increase information and transparency to both authorities and investors with respect to open-ended funds as well as to strengthen liquidity risk management frameworks and practices of those funds. They also address the potential use of system-wide stress testing by authorities.

- *Leverage within investment funds*: These recommendations focus on the measurement and monitoring of leverage within investment funds.
- *Operational risk and challenges at asset managers in stressed conditions*: These recommendations would help ensure that risk management frameworks and practices are commensurate with the level of risks that an asset manager's activities pose to the financial system.
- *Securities lending activities of asset managers and funds*: These recommendations focus on situations where indemnifications are provided by asset managers to their clients in relation to securities lending activities.

IOSCO Final Report on Loan Funds Survey

In February 2017, IOSCO published its final report including the findings of its survey on loan funds as part of its effort to build a sustainable system of market-based finance. The report describes how the market for loan funds has evolved in different jurisdictions and sets out how regulators are addressing the risks associated with these funds.

The report identifies two types of loan funds. Loan originating funds can grant, restructure and acquire loans, while loan participating funds can acquire and restructure partially or entirely existing loans originated by banks and other institutions, either directly from the lender or on secondary markets.

The report identifies the following risks associated with loan funds:

- liquidity risk, i.e. loans are hard to value and, since they are also hard to trade, are very illiquid assets
- credit risks, i.e. the risk of a default of the borrower
- systemic risks from excessive credit growth
- regulatory arbitrage.

Many jurisdictions consider their general rules for funds to be sufficient to address the risks associated with loan funds, and so the report concludes that further work on loan funds is not warranted at this stage. Considering the specific risks identified in the report, IOSCO will continue to monitor the issue with a view to possibly revisiting it for future work should it be called for by market developments.

Luxembourg Legal and Regulatory Developments

Market Abuse

Law of 23 December 2016

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

For more information on the CSMAD and MAR and on their impact on investment funds, please also refer to the July 2016 and November 2016 editions of our Luxembourg Legal Update.

Mortgage Credit Directive Implementation

Law of 23 December 2016

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

Implementation of ESMA Guidelines on Delay in Disclosure of Inside Information under MAR

CSSF Circular 16/646

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

Central Administration, Internal Governance and Risk Management

CSSF Circular 16/647

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

Implementation of ESMA Guidelines on Persons Receiving Market Soundings under MAR

CSSF Circular 17/648

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

Primary Tax Offences related to Money Laundering

CSSF Circular 17/650

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

CSSF Authorisation for UCITS to access CIBM without QFII or RQFII Quotas

Further to the revised rules issued by the People's Bank of China (the "**PBoC**"), which allow foreign institutional investors to directly invest into the China Interbank Bond Market (the "**CIBM**") by direct registration with the PBoC, the CSSF now authorises Luxembourg UCITS to invest directly in RMB fixed income securities dealt on the CIBM, without the need to use their QFII or RQFII licences and quotas.

Apart from the specific conditions and constraints imposed by the PBOC, this new direct registration route with the PBoC may only be used by managers of Luxembourg UCITS with the CSSF's prior approval. Such approval is subject, among others, to appropriate references in the prospectus of the relevant UCITS to the use of such direct access to CIBM and to the associated risks.

Investment Funds qualifying as PIEs

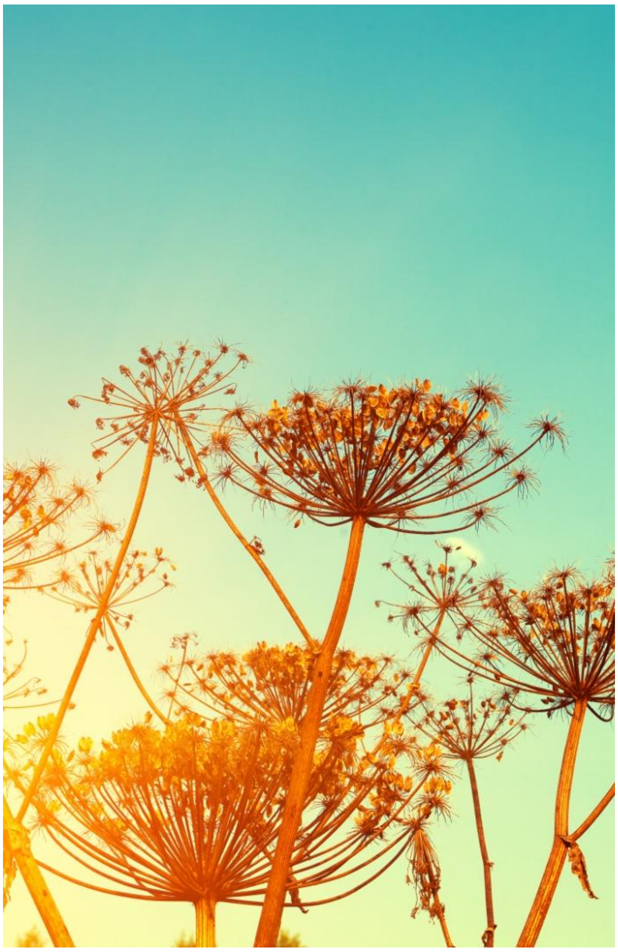
CSSF Press Release 16/45

On 16 December 2016, the CSSF issued Press Release 16/45 relating to investment funds qualifying as public-interest entities (PIEs) within the meaning of Directive 2006/43/EC on statutory audits of annual accounts and consolidated accounts as amended by Directive 2014/56/EC (Audit Directive), and of Regulation (EU) N°37/2004 on specific requirements regarding statutory audit of public interest entities (PIE Regulation).

As a reminder, the CSSF clarified in its FAQ on UCITS dated 24 August 2016 that UCITS funds having their units admitted to trading on a regulated market within the meaning of point 14 of Article 4(1) of MiFID qualify as PIEs and have to comply with the relevant requirements of the Audit Directive and PIE Regulation applicable to PIEs. In its press release, the CSSF highlights further diligences to be performed by the approved statutory auditor (*réviseur d'entreprises agréé*) of investment funds qualifying as PIE, including:

- the completion of an engagement quality control review prior to the issuance of the audit report as per Article 8 of the PIE Regulation
- the internal rotation of the key audit partner responsible for carrying out the audit as per Article 17 of the PIE Regulation
- the inclusion in the transparency report of these PIEs.

These measures will be applicable for periods beginning on or after 17 June 2016.



New CSSF Form File Procedure in relation to CSSF Circular 02/77

CSSF Press Release 17/01

CSSF Press Release 17/01 of 3 January 2017 informed investment funds that notifications in the framework of CSSF Circular 02/77 relating to NAV calculation errors and non-compliance with the investment rules must now be made by completing and sending by e-mail to the CSSF a specific notification form file (available on the CSSF website).

The CSSF also published additional explanations in relation to this new form file in which it clarifies that the new notification procedure is applicable to all UCITS, Part II UCIs and SIFs. Indeed, according to the CSSF regulatory practice, SIFs that did not set specific internal rules in case of NAV calculation error and for the correction of the consequences resulting from non-compliance with their investment rules must apply Circular CSSF 02/77 by default. Moreover, as regards the notification process, the CSSF considers that any NAV calculation error as well as any instance of non-compliance with investment rules by SIFs must be subject to a notification to the CSSF, whether the relevant SIF chooses to apply CSSF Circular 02/77 or to set other specific internal rules.

The CSSF further indicates that the notification procedure must start immediately after the NAV calculation error or the non-compliance with the investment rules is discovered by sending the specific form file to the CSSF. In case not all the information is available at that time, the notification will be completed as soon as possible by sending a new form file duly completed with the missing information and data.

The new notification procedure and the use of the specific form file are mandatory as from 1 March 2017.

ESMA opinion on UCITS share classes

CSSF Press Release 17/06

Further to the publication by ESMA of its opinion on UCITS share classes, the CSSF issued press release 17/06 on 13 February 2017.

In its press release, the CSSF indicates that it expects Luxembourg UCITS to take the necessary measures to comply with the transitional provisions set forth in the ESMA opinion for setting up share classes in UCITS funds. Like ESMA, the CSSF also indicates that new share classes of UCITS have to comply immediately with ESMA opinion.

For more information on ESMA opinion on UCITS share classes, please see sub-section titled "ESMA Opinion on UCITS Share Classes" of this Luxembourg Legal Update.

CSSF New Application Questionnaire for Part II UCIs, SIFs and SICARs

CSSF Press Release 17/07

On 15 February 2017, the CSSF issued press release 17/07 announcing that a new application form is available and has to be used and submitted as from 15 March 2017 to the CSSF for the setting-up of any new Part II UCI, SIF or SICAR.

Similarly to the previous ones, the new application form aims at collecting the full information required by the CSSF to open and examine a file for approval of a new Part II UCI, SIF or SICAR in accordance with the relevant Luxembourg laws. To a large extent, the procedure for submitting the application form by electronic means (secure channels or e-mail at the setup.uci@cssf.luaddress) is still the same, except for application filed via e-mail for which a nomenclature specified in the “Documents” tab of the application file must be followed to name the e-mail and documents in attachment.

Financial Intelligence Unit (FIU) Guidelines on the Blocking of Suspicious AML/CTF Transactions

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

Litigation

Enforcement Proceedings

Regulation (EU) N°655/2014 of 15 May 2014 establishing a European Account Preservation Order Procedure and Bill N°7083 of 27 October 2016

On 18 January 2017, Regulation (EU) N°655/2014 of 15 May 2014 establishing a European account preservation order procedure to facilitate cross-border debt recovery in civil and commercial matters came into effect.

The Regulation establishes a uniform European procedure for the preservation of funds held in bank accounts in cross-border cases, meaning where the bank account(s) to be preserved is/are maintained in a Member State other than:

- the Member State of the court seized of the application for a preservation order
- the Member State in which the creditor is domiciled.
- However, the procedure will not be available to creditors domiciled in the United Kingdom or in Denmark, and will not extend to bank accounts maintained in the United Kingdom or in Denmark.

The Regulation establishes an additional and optional preservation procedure for creditors, who remain entitled to make use of any preservation measures under national law.

The Regulation applies to monetary claims in civil and commercial matters. Among other things, it does not extend to claims held against a debtor against whom bankruptcy, insolvency or similar proceedings have been opened.

Creditors domiciled in a Member State may apply to the courts of a Member State for a European account preservation order for monetary claims that have fallen due, or that arise from a past event or transaction and the amount of which is determinable, and will need to evidence that their claim is in urgent need of judicial protection.

The Regulation further sets forth a procedure allowing a creditor to request that the information necessary to identify the debtor's bank or banks and the debtor's account or accounts be obtained by the court from a designated information authority of the Member State in which the creditor believes the debtor to hold an account. A similar means of ensuring the transparency of the debtor's assets, and collecting information on where the debtor's assets are located, does not exist under the Luxembourg national procedure applied for preserving bank accounts (the so-called *saisie-arrêt*).

A European account preservation order may be issued for the amount of the creditor's claim or for a lower amount. Any funds in the account(s) to be preserved which exceed the amount of the creditor's claim remain unaffected. By contrast, under the Luxembourg national procedure applied for preserving bank accounts, all of the assets in the bank account(s) preserved are blocked.

Upon being served with a European account preservation order, and within three days of preserving the amount specified therein, banks are required to issue a declaration indicating to the issuing court and to the creditor whether and to what extent funds in the debtor's account(s) have been preserved. By contrast, under the Luxembourg national procedure applied for preserving bank accounts, banks may be required to declare whether the debtor indeed holds an account with them, and whether the account holds any funds, only once creditors have obtained an authentic deed confirming their claim against the debtor, and there is no set timeframe within which banks are required to issue said declaration.

The debtor is notified of the European account preservation procedure only once the bank has preserved the account(s), and issued the aforementioned declaration.

European account preservation orders issued in a Member State have the same rank as equivalent national orders, and benefit from automatic recognition and enforcement in the other Member States.

Bill N°7083 implementing the Regulation was introduced on 27 October 2016, and proposes to amend the provisions of the Luxembourg New Code of Civil Procedure and of the Luxembourg law of 23 December 1998 establishing a financial sector supervisory commission, as amended.

The Luxembourg local courts, namely the judges presiding over the Luxembourg District Courts, will be competent to issue, revoke and/or modify a European account preservation order, and/or limit or terminate the enforcement thereof, in Luxembourg, depending on whether or not a claim exceeds EUR 10,000.

The CSSF will be the authority competent to obtain account information, and banks established in Luxembourg will be required to disclose, upon request of the CSSF, whether the debtor holds an account with them.

Payment of the Debt of Others – Personal Legal Action in Repayment

Court of Appeal, 14 December 2016, N°43639

In the case at hand, the *Fond National de Solidarité* had advanced to a former spouse the maintenance allowance due by her former husband. The law provides that the Fund is entitled to an action by way of subrogation in the rights of the maintenance creditor to obtain the repayment by the real debtor of the sums paid by the Fund. In that case, the Fund had summoned the former husband in repayment, but the debt of the former spouse was time barred and the Fund could therefore no longer base its action on the action by way of subrogation.

The Fund has thus argued that it was entitled to a personal action in repayment of the sums that it had paid against the maintenance debtor.

The Court of Appeal granted the claim stating that "the third payor may normally bring a personal action against the debtor, that it is the case for the one who pays the debt of others without free intention and that the subrogation completes the personal action and does not make it disappear", and that "the third payor who paid the debt of others from his own expenditure has a recourse against the debtor which could be due by the sole fact of the payment", generating a new obligation separate from the one extinguished by the payment.

Banking, Finance and Capital Markets

Loan – Absence of Repayment Date

Luxembourg District Court, 7 May 2015, N°68561

In 2009, a company received a loan of EUR 1.65 million. No repayment date was provided for by the parties. In 2013, the lender requested repayment and, in 2015, he sent a formal notice to pay to the borrower.

According to the Luxembourg district court, the parties may choose not to determine a term for the repayment of a loan. This choice does not imply the absence of a term, as a perpetual loan would be a donation. If it is clear that the contract is a loan, it is possible to infer a tacit term. In such case, according to Article 1900 of the Luxembourg Civil Code the judge may determine a payment term taking into account the circumstances. A judge may also consider that the payment term has already lapsed at the date of the judgment. However, the payment term may not be situated at a date prior to the judgment. In the case at hand, the district court decides that the date of the judgment is also the date of the payment term.

Fraud and Mistake – Subscription Order – Investment Advice – Investment in Shares Representing an Exceptional Risk

Court of Appeal, 4 February 2016, N°40600

In 2007, a client opened an account with a bank with a view to investing EUR 500,000. According to the evaluation by the bank, the client had a "low risk" investment profile. Shortly after the opening of the account, the bank suggested to the client to invest in two alternative investment funds. The bank indicated that they did not correspond to the client's profile, but underlined the good performance and the controlled risk of the investments and suggested to the client that he should sign a waiver with regard to his investment profile. The client relied on the bank's recommendations, instructed the bank to buy the products up to EUR 250,000 each, and signed a waiver.

Given that the first investment fund suffered important losses during summer 2008, the client asked the bank to sell this product, and asked the bank about the performance of the second product. In autumn 2008, the client wanted the other product to be repurchased. However, the second investment fund had invested its assets with Bernard Madoff Investment Securities and, because of delays, the repurchase order could not be taken into account.

The client considered that his investment contract with the bank was void because of misrepresentation (*dol*) by the bank or because of a mistake (*erreur*).

With regard to misrepresentation, the Court considered that, even though the information provided to the client by the bank was insufficient with regard to his knowledge, there was no evidence that the bank was not only negligent, but also acting on purpose with a view to deceiving the client.

With regard to mistake, the Court held that it is necessary to appreciate the situation of the victim of the mistake, and takes into account the investment profile as well as the profession and behaviour of the client. The Court concluded that the client had no knowledge regarding alternative investment products. The Court also decided that the information provided to the client by the bank was not sufficient with regard to the client's low level of knowledge of this kind of product. According to the Court, the client was not aware that the investment products that he invested into were "really risky", and that this was contrary to his "low risk" profile, to the aim of his investment and to his aim to limit risks. Additionally, the Court held that the bank could not rely on the waiver which, even if written in a language that is technically correct and comprehensible to people with knowledge in the financial area, is inappropriate with regards to the client and her partner, who, as is clear from the correspondence between him and the bank, did not have more knowledge than the client.

According to the Court, banks are held by an obligation to inform clients and they cannot avoid liability if they ask clients with little knowledge to sign a waiver of this type without explaining them the risks linked to this type of alternative investment product in a language that is adapted to the client's knowledge.

The Court held that the client had committed a mistake and that the contract regarding the purchase of the product was void. As a consequence, the bank was sentenced to repay the amount of EUR 250,000 as well as interest to the client.

Financial Collateral Directive – Possession and Control – Insolvency

ECJ, 10 November 2016, C 156/15

On 14 April 2007, a client opened a current account with a Latvian bank. The account terms contained the following clause:

"The Customer's moneys in the Account, present and future, shall be pledged to the Bank as financial collateral and shall cover all debts owed by the Customer to the Bank. In the event that the Customer fails to provide the moneys necessary to make the payments in the current account, or in any other situation in which, pursuant to the present contract or any other contracts entered into with the Bank, or on any other legal basis, a debt owed by the Customer to the Bank arises, the Bank shall be entitled to settle that debt by enforcing the financial collateral arrangement, that is to say, the Bank shall be entitled, without giving prior notice to the Customer, to debit (transfer) from the Account the amount owed. …"

On 25 October 2010, the client was declared insolvent. The client's insolvency administrator opened a new account with the bank on the same terms. On 8 June 2011 the bank debited 192.30 Latvian lats (approximately EUR 274) from the client's account for account fees that were incurred by the client prior to the insolvency.

The Latvian court referred a number of questions to the ECJ.

One question is of particular interest. The Latvian court asked the ECJ to confirm whether, in so far as it applies to cash, the Financial Collateral Directive is restricted to cash credited to bank accounts used for securities settlement or whether it also extends to ordinary bank accounts.

When answering this question, the ECJ addresses two interesting issues.

First, the ECJ held that, in the absence of any express reference to the laws of the Member States, the criterion of "possession and control" under the Financial Collateral Directive must be given an autonomous and uniform interpretation throughout the European Union which takes into account its wording, context and objective. The requirement relating to the provision of financial collateral is designed to ensure that the collateral taker identified in the financial collateral arrangement is actually in a position to dispose of the collateral when an enforcement event occurs. According to the Court, the taker of collateral in the form of moneys lodged in an ordinary bank account may be regarded as having acquired "possession or control" of the moneys only if the collateral provider is prevented from disposing of them.

Secondly, according to the Court, money credited to a bank account can only constitute financial collateral within the scope of the Financial Collateral Directive where the money was deposited in that account before the commencement of the insolvency proceedings or where it was deposited on the day those proceedings commenced in cases where the collateral taker proves that it was not aware nor should have been aware of the commencement of proceedings at the time of the credit.

For a more detailed analysis, please refer to Clifford Chance London Client Briefing of November 2016.

Corporate

Labor – Employment Contract – Combination of a Corporate Mandate with an Employment Contract – Conditions – Subordination Relationship – Sole director (no) – Art. L.121-1 Labor Code – Law of 10 August 1915, Art.51

Court of Appeal, 12 November 2014, N°40366

On 12 November 2014, the Court of Appeal confirmed its position of 10 February 2011 with regards to the possibility to combine, for the same person, a mandate of director and an employment contract within the same company.

The Court of Appeal's position was a reminder that one can only cumulate a mandate of director and a status as employee of the same company if the employment contract is serious and actually reveals a subordination tie to the employer, who gives orders and controls the execution of the tasks given to the employee and assesses the results. Consequently, the director-employee cannot be the sole director of the company.

Commercial Companies – Voluntary Liquidation – Complete Settlement of Liabilities – Provision for Potential Future Liabilities – Liability of the Liquidator – Discharge Given by Shareholders – Third Party Action – Law of 10 August 1915, Art.147 to 149

Court of Appeal, 21 January 2015

In the case at hand, the Court of Appeal had to decide whether, in the context of a voluntary liquidation, the liquidator of a company knew about the existence of a debt at the moment of the closure of the liquidation procedure, and consequently, whether he can be held liable.

The Court of Appeal ruled that the liquidator should be aware of the existence of the debt, or at least could not ignore it, in order to be held liable. In addition, the debt of the company does not need to be due at the time of the closure of the liquidation procedure; it can even be a contingent liability.

Considering the facts of the case, the Court of Appeal decided that the liquidator could not ignore the existence of the debt and therefore had to take it into account through a provision for potential future liabilities in the liquidation accounts. Furthermore, the Court ruled that any discharge given by the shareholders to the liquidator prevents them from issuing a claim against him; however, this did not prevent any third parties from doing so. As a consequence, the liquidator was held liable.

Commercial Companies – Public Limited Liability Company – Responsibility of the board members – *Actio Mandati* – Action suit from the Company – Free Decision – Requirement – General Shareholders' Meeting – Law of 10 August 1915, Art.59 and 63

District Court, 26 February 2015, N°136378

On 26 February 2015, the District Court clarified the rules relating to the initiation of the *actio mandati*.

The District Court emphasised that a liability claim against directors only belongs to the injured party, which means that in the event that all the shareholders suffer damages, the claim belongs to the company itself; in the event one or more shareholders only suffer damages, the claim belongs to those shareholders only.

In the case at hand, the District court decided that the alleged misconducts were within the scope of the company's interest, which means that the *actio mandati* can only be exercised by the company.

The company is free to exercise the *actio mandati* or not, subject to the condition that any waiver shall not be detrimental to creditors.

Moreover, the involvement of the general meeting of shareholders is necessary, it being understood that the *actio mandati* is only admissible with a decision of the general meeting of the shareholders authorising the company to exercise it.

The District Court further considered that such rule is confirmed by the provisions of Article 63 of the 1915 law and is applicable both to the actions exercised against the current board members and against the former board members.

Transfer of Branch of Activity – Notary Deed – Absence of Capacity to Act – Transfer of all Assets and Liabilities – Law of 10 August 1915, Art.285 to 308

Court of Appeal, 1 April 2015, N°39461

On 1 April 2015, the Court of Appeal clarified the scope of the transfer of the branch of activity of a company based on Article 308bis-5 of the 1915 Law.

In the case at hand, an agreement was signed between an individual and a bank for, *inter alia*, investment operations.

On June 2008 the bank transferred its branch of activity of "Private and Corporate Banking" to another bank by a notary deed and decided that this transfer shall be governed by the rules of the de-merger. Nevertheless, the individual considered that he had a right to compensation against the initial bank due to the loss of the expected profit, on the basis of Article 289 (3) (b) of the 1915 Law which provides that in the event where a liability is not allocated in the draft terms of de-merger and where the interpretation of these terms does not make a decision on its allocation possible, each of the recipient companies shall be jointly and severally liable therefor.

However, the deed of assignment provided that, pursuant to Article 308bis-5 of the 1915 Law, the branch of activity was fully transferred with all assets and liabilities attaching thereto.

Therefore, the Court of Appeal considered that the appellant's action against the initial bank with which he signed an agreement, was not admissible, considering that the liabilities were transferred to the beneficiary bank.

Tax

The World Duty Free and Banco Santander Cases, and the Spanish Financial Goodwill Amortisation Regime, constitute a Fiscal State Aid

European Court of Justice, 21 December 2016, Joined Cases C-20/15 P and C-21/15 P

On 21 December 2016, the European Court of Justice ruled in favour of the EU Commission and set aside the two judgments rendered by the EU General Court (GC) that found the Spanish financial goodwill amortisation regime as not being fiscal state aid.

On 28 October 2009, the EU Commission considered that the Spanish financial goodwill amortisation regime allowing companies to deduct from their taxable basis financial goodwill arising from acquisition of non-Spanish EU shareholding was incompatible with the State aid rules. On 7 November 2014, the EU GC annulled the EU's state aid decision by considering that the fiscal advantage under the Spanish tax regime was not selective and that the EU Commission had failed to identify a particular category of companies entitled to benefit from the tax measure.

In the case at hand, the ECJ recalled that the selectivity of a tax measure can only be determined on the basis of whether it favours certain companies over other companies which are in a comparable factual and legal situation – having regard to the objective pursued by the general tax system concerned – provided that this difference in treatment results in discrimination against the companies excluded from the application of the tax measure. The ECJ then concluded that the EU Commission is not required to identify a particular category of companies entitled to benefit from a specific tax measure but must rather identify whether the tax measure represents a discrimination against companies that are excluded from it.

Following the judgment, the ECJ has sent back the cases to the EU GC for new hearings.

VAT Deduction Right for Holding Companies involved in the Management of its Subsidiaries

Order of the European Court of Justice, 12 January 2017, Case C-28/16

On 12 January 2017, the European Court of Justice (sixth chamber) rendered its order in Case C-28/16. In the case at hand, a Hungarian holding company active in the energy sector was carrying on a taxable business activity, but was also involved in the management of its subsidiaries without charging a fee for those services (being legal, business-management and public-relations services). The holding company was of the view that it had a full input VAT deduction right taking into account the fact that it was performing only taxable activities and that all services received were linked to such activity. The Hungarian tax authorities, however, refused to grant the holding company with a VAT deduction right on the services linked to the management of its subsidiaries, claiming that the holding company did not perform an economic activity (the services were provided for free). The Supreme Court of Hungary referred to the ECJ by filing a preliminary ruling.

The ECJ gave its answer in the form of an order by considering that the questions referred by the Hungarian Supreme Court had already been answered in prior rulings and case laws. In its answer, the ECJ restates the general rule for input VAT recovery right requiring a direct and immediate link between input transactions and output transactions in order to have a right of deduction. In addition, the ECJ recalled that the mere acquisition and holding of shares in a company is not to be regarded as an economic activity for the holding company. However, when a holding company is directly (or indirectly) involved in the management of its subsidiaries, such management activity must be considered as an economic activity provided that the holding company charges a fee to its subsidiaries. In this respect, the mere involvement of a holding company in the management of its subsidiaries will not be considered as an economic activity if such holding company does not charge any fee (i.e. subject to VAT) as remuneration for its management services. As a result, the holding company will have no right to deduct input VAT for the costs linked to such activity (as long as no fees are charged to the subsidiaries).

Independent Group of Persons: the Luxembourg VAT Cost Sharing Exemption Incompatible with EU VAT Directive

Opinion of Advocate General of the European Court of Justice, 6 October 2016, *Case* C-274/15

On 6 October 2016, the Advocate General of the European Court of Justice gave her opinion in the case C-274/15 where the EU Commission brought an infringement proceeding against Luxembourg and its domestic VAT rules applicable to an independent group of persons (also known as the VAT cost-sharing exemption as provided by Article

132(1)(f) of the EU VAT Directive and implemented in Luxembourg VAT law under Article 44(1)(y)).

The VAT cost-sharing exemption applies when two or more persons with VAT exempt and/or non-business activities join together on a cooperative basis to form an independent group of persons (IGP). The Luxembourg VAT cost-sharing exempts from VAT the supply of services by the IGP to its members provided that the members' taxed activities do not exceed 30% (or 45% under certain conditions) of their annual turnover. However, under EU law, in order to benefit from the VAT exemption, the services provided by the IGP to its members should be "directly necessary" to the members' exempt or non-business activities only.

In her opinion, the Advocate General concurred with the EU Commission by considering that the Luxembourg VAT cost-sharing exemption was not in line with the EU VAT directive and, in particular, on the basis that:

- The Luxembourg cost-sharing exemption is not restricted to services supplied by the IGP for the benefits of its members' exempt or non-business activities only.
- The IGP is a taxable person which is independent from its members and cannot transfer a deduction right to its members which it cannot exercise itself. Only the IGP has a right to deduct input VAT charged on the services it receives. In this respect, members of the IGP are not entitled to deduct VAT charged to the IGP on the purchase of goods and services from third parties up to their recovery VAT right.
- Costs deriving from services received by the IGP's member itself but on behalf of the IGP and which are thus recharged to the IGP must be subject to VAT. Luxembourg currently applies an administrative practice which, in the case of purchasing goods or services by a member itself but on behalf of the IGP, considers the recharge of costs to the IGP as not falling within the VAT scope.

If the ECJ follows the opinion of the Advocate General, the existing Luxembourg VAT cost-sharing exemption would have to be amended triggering implications for existing IGPs, which would have to be analysed on a case-by-case basis.

Securitisation Tax Regime Denied for Net Wealth Tax Purposes

Administrative Court of Luxembourg, 4 October 2016, N°36590

On 4 October 2016, the Administrative Court of Luxembourg ruled on whether a Luxembourg company, being subject to the securitisation law of 22 March 2004, as amended, should automatically benefit from the net wealth tax exemption.

In the case at hand, the Luxembourg company was at first incorporated as a fully taxable company but in order to realise securitisation investments it changed its legal status on 20 October 2009.

In 2014, the Luxembourg tax administration issued a net wealth tax bulletin for the fiscal year 2010 denying the Luxembourg securitisation tax regime applicable to the Luxembourg company. In fact, the Luxembourg tax administration claimed that the company, despite having the legal form of a securitisation company, never performed securitisation activities and could thus not benefit from the securitisation tax regime. In this respect, the Luxembourg tax authorities do not simply rely on the legal qualification given to a securitisation company but also analyse the economic nature of any transaction by considering its actual business.

In other words, making a reference to the securitisation law in the by-laws of a securitisation company would not be sufficient in order to benefit from the specific securitisation tax regime if the company does not perform a real securitisation activity *per se*.

Retroactive Effect of a Merger

Administrative Court of Luxembourg, 21 December 2016, N°36930

On 21 December 2016, the Administrative Court of Luxembourg ruled on the retroactive effect of merger by considering that from a tax perspective, the merger would be effective as from its approval by the shareholders notwithstanding the fact that a retroactive effect could be applicable from an accounting perspective.

In the case at hand, a merger of two companies was achieved on 7 March 2012 further to the approbation by the shareholders during the last extraordinary meeting. However, as indicated in the merger's project and pursuant to Article 261 (2) of the Luxembourg company law dated 10 August 1915, as amended, the merger was given with an accounting retroactive effect as from 30 November 2011.

Nonetheless, the Luxembourg tax authorities took the view that, from a tax perspective, the merger was only effective as from 7 March 2012, and considered that both companies still existed on 1 January 2012 and were liable for net wealth tax.

The Administrative Court of Luxembourg ruled in favour of the tax authorities by considering that the accounting effect of a merger is not binding for the Luxembourg tax authorities. As a result, the merger of two companies is effective, from a tax perspective, as from the date of approval of the merger (i.e. 7 March 2012 in the case at hand). This decision follows the judgment dated 2 June 1999 – N°10788.

Real Estate

Tax Reform 2017: the Registration of a Lease Agreement is no longer an Obligation

Until 31 December 2016, any lease agreement entered into in Luxembourg was subject to an obligation of registration before the registration office (*Administration de l'enregistrement et des domaines*) within three months of its signature. The duties to be paid as a result of registration amounted to 0.6% of the cumulated amounts of the rents, unless the parties asked for and obtained a VAT option, in which case the fees amounted to a fixed rate of EUR 12.

This obligation has now been abolished, as of 1 January 2017.

The parties remain, however, free to register their lease agreement in order for their lease to acquire an official date and thus make it effective/enforceable against third parties.

In case the parties voluntarily register their lease agreement, registration duties remain due and continue to be calculated at the above-mentioned rates.

Law of 3 March 2017 called "Omnibus"

The new law of 3 March 2017 called "Omnibus" modifies 11 laws, impacting in particular several real estate and environmental matters. The law aims, amongst others, at simplifying, accelerating and shortening administrative procedures, dematerialising several documents for more transparency and accessibility to the public, reducing delays for administrations and facilitating the procedure to adopt urban planning instruments in Luxembourg (in particular, general land-use plan (*PAG)* and specific land-use plans (*PAP)*), introducing a principle of tacit approvals. The law also modifies some laws regarding nature and natural resources protection, water, the municipal law, protection of national sites and monuments.

The new enters into force on 1 April 2017.

Tax

International Legislation

Multilateral Convention to implement Tax Treaty related Measures to prevent BEPS

OECD adopts the Multilateral Convention

On 24 November 2016, the OECD adopted the multilateral convention to implement tax treaty related measures to prevent BEPS. This multilateral instrument published with explanatory statements will swiftly implement a series of tax treaty measures to update international tax rules and lessen the opportunity for tax avoidance by multinational enterprises.

Instead of having the OECD countries individually renegotiating their tax treaties, more than 100 countries have ratified the multilateral convention that will update their existing bilateral tax treaties in order to bring them into line with the BEPS recommendations. The OECD anticipates that up to 2000 treaties could be amended in this way.

The multilateral convention will cover some of the BEPS recommendations, including those on hybrid mismatch (BEPS Action 2), treaty abuse (BEPS Action 6 – minimum standard), in particular the limitation-on-benefits and principle purpose test rules or the anti-abuse rule for permanent establishments situated in third jurisdictions, the avoidance of permanent establishment status (BEPS Action 7), and finally the improvement of dispute resolution (BEPS Action 14 – minimum standard).

The existing tax treaties will directly be amended in order to reflect the minimum standards as provided by the multilateral convention. The countries will have to notify the OECD of all the tax treaties they wish to have covered by the multilateral convention, as well as the BEPS measures to be implemented. It should be noted that the countries would have the possibility, in certain circumstances, to opt in or opt out of the provisions to the extent that the existing ones are already in line with the minimum standards.

The multilateral convention has been open for signature by any country since 31 December 2016. It will enter into force upon five or more countries having ratified it. It will enter into effect further to reciprocal implementation by countries of the multilateral convention within domestic laws and after expiration of a certain period (e.g. three to four months).

Amendments to the Anti-Tax Avoidance Directive as regards Hybrid Mismatches with Third Countries

Political Agreement on the ATAD II in the ECOFIN Council

On 21 February 2017, the EU finance ministers in the ECOFIN meeting have reached agreement on the proposal for a Council Directive extending hybrid mismatch anti-avoidance provisions to third countries ("**ATAD II**").

The proposal for the ATAD II was first presented on 25 October 2016 as part of the EU Commission's corporate tax reform package. The ATAD II proposes to extend the hybrid mismatches, as provided by Council Directive 2016/1164 on rules against tax avoidance ("**ATAD I**"), to third countries by including rules to determine which of the two jurisdictions concerned should deny the deduction or (as appropriate) tax the corresponding income. These new rules as set out by the ATAD II are modelled on the rules contained in the BEPS report on Action 2.

The proposal for the ATAD II provides, *inter alia*, the following elements:

- Extension of the ATAD I's scope by including rules on hybrid mismatches between EU Member States and third countries that apply to taxpayers subject to corporate tax in one or more Member States, including permanent establishments (PEs) of non-EU entities.
- The rules would only apply in the case of a hybrid mismatch between a taxpayer and an "associated enterprise" or in the case of "structured arrangements" between the parties involved but also to entities treated as tax transparent by a Member State.
- Extension to hybrid mismatches in order to include arrangements involving PEs, hybrid transfers, imported mismatches, and reverse hybrid entitles. In this respect, mismatches between head office and PE, between PEs, between associated enterprises and those resulting from structured arrangements would be covered. Finally, mismatches resulting from the existence of hybrid entities will only be covered where one of the associated enterprises has effective control over the other associated enterprises. Deduction without inclusion arising due to the tax exempt status of a payee will not be treated as a hybrid mismatch.

In order to be implemented, the ATAD II should first be adopted by the EU Parliament. Once approved, the EU Member States will need to implement it into their domestic law for a first application as from 1 January 2020 (except for the specific reverse hybrid entity rule which would be as from 1 January 2022).

National Legislation

Luxembourg Tax Reform for 2017

Law of 23 December 2016

On 23 December 2016, the Luxembourg Parliament formally adopted the bill of law N°7020 implementing the 2017 tax reform, including changes to Luxembourg corporate and individual tax systems but also the VAT system. We have summarised below some of the changes that entered into force on 1 January 2017. For further information, please see the November 2016 edition of our Luxembourg Legal Update.

The main changes for corporate taxation are as follows:

- Reduction of the corporate income tax rate from 21% to 19% for the tax year 2017 and to 18% for the tax year 2018 for companies with taxable income exceeding EUR 30,000. As a result, the overall corporate tax rate (including the solidarity surcharge of 7% and the municipal business tax of 6.75% for companies located in Luxembourg City) amounts to 27.08% for 2017 and to 26.01% as from 2018.
- In addition, the minimum corporate income tax rate should be reduced from 20% to 15% as from fiscal year 2017 for companies with taxable income below EUR 25,000 (currently EUR 15,000).
- The minimum net wealth tax increases from EUR 3,210 to EUR 4,815 for any company whose financial assets (i.e. assets to be accounted for in accounts 23, 41, 50 and 51 of the *Plan Comptable Normalisé*) represent more than 90% of its balance sheet and a minimum amount of EUR 350,000.
- As from tax year 2017, the losses would be carried forward for a maximum period of 17 years. Losses realised between 1 January 1991 and 31 December 2016 would be carried forward without limitation.
- Deferred amortisation/deprecation: The taxpayer could opt to defer the deduction allowed by amortisation/depreciation of an asset for a given year until the end of the useful life of such asset.
- Extension of the scope of Article 54bis of the Luxembourg income tax law (i.e. the deferral of taxation of foreign exchange gains derived from assets denominated in a foreign currency) to all companies as from tax year 2016.
- The 0.24% registration duty on the transfer, use or capitalisation of claims would be abolished.
- Managers (but also liquidators and trustees) are liable for the fulfilment by the company of its VAT obligations and especially for the payments of such VAT. The liability would be personal and joint. The range of the fixed penalties is increased from EUR 50/5,000 to EUR 250/10,000.

The main changes for corporate taxation are as follows:

- New income tax rates for taxable income exceeding EUR 150,000 and EUR 200,004 (respectively, 41% and 42%).
- The 0.5% temporary budget tax is abolished as from tax year 2017.
- The withholding tax rate on interest income received by a Luxembourg resident is increased from 10% to 20%.

Luxembourg implements Country-by-Country Reporting

Law of 23 December 2016

On 23 December 2016, the Luxembourg Parliament formally adopted the bill of law N°7031 introducing in the Luxembourg domestic law the country-by-country reporting ("**CbC Law**") as provided by EU Directive 2016/881 of 25 May 2016 regarding the automatic exchange of information in the field of taxation (known as DAC4).

According to the CbC Law, Luxembourg ultimate parent entities of multinational companies (i.e. multinational companies with a consolidated group revenue above EUR 750 million and at least two companies whose tax residency is in a foreign country) should file an annual country-by-country report with the Luxembourg Tax Administration. Such country-by-country reports should include the following information:

- aggregate information relating to the amount of revenue, profit/(loss) before income tax, income tax paid, income tax accrued, stated capital, accumulated earnings, number of employees, and tangible assets other than cash or cash equivalents with regard to each jurisdiction in which the multinational company operates
- a list of all the companies that are part of the multinational company including their tax residences, the jurisdictions under the laws of which those companies are organised, and the nature of their main business activity

- any additional necessary clarification required to understand the information provided.

The country-by-country report should be filed within 12 months after the last day of the tax year. In cases of late filing or default of filing, a maximum penalty of EUR 250,000 could be applied.

On 27 December 2016, in connection with the publication of the law in Memorial (N°280), the Luxembourg tax authorities published on their website guidelines and FAQ in relation to obligations deriving from the country by country reporting law. Accordingly, the filing deadline for the country-by-country report for fiscal year 2016 has been extended to 31 March 2017. In this respect, no penalty for late filing shall apply until this date.

For further information, please see the November 2016 edition of our Luxembourg Legal Update.

New Transfer Pricing Provisions introduced in Luxembourg Domestic Law

Law of 23 December 2016

On 23 December 2016, the Luxembourg Parliament formally adopted the bill of law N°7050 introducing new transfer pricing provisions in Luxembourg domestic law.

Up to now, only Article 56 LITL has addressed the transfer pricing principles in the Luxembourg domestic law by defining the concept of arm's-length transactions. This law introduces a new Article 56bis in LITL, including reference to key principles of the OECD transfer pricing guidelines recently updated by Actions 8-10 of the OECD Base Erosion and Profit Shifting (BEPS) Action Plan, together with the comparability analysis for determining arm's-length remuneration.

This new Article 56bis LITL is complemented by the new transfer pricing Circular L.I.R. N°56/1 – 56bis/1 published on 27 December 2016. For further information on the transfer pricing circular, see below (Regulatory).

For further information, please see the November 2016 edition of our Luxembourg Legal Update.

Small Enterprise VAT Regime

Law of 23 December 2016

On 23 December 2016, the Luxembourg Parliament formally adopted the bill of law N°7050 increasing the annual turnover threshold from EUR 25,000 to EUR 30,000 in order to benefit from the VAT regime for small enterprises.

In connection with the above, on 6 January 2017, the European Commission sent a proposal for a Council Implementing Decision to the EU Council to authorise Luxembourg to continue derogating from Article 285 of the EU Directive 2006/112/EC on the common system of value added tax, as amended. Luxembourg was initially granted this derogation by Council Implementing Decision 2013/677/EU of 15 November 2013, under which Luxembourg was authorised to exempt from VAT those taxable persons whose annual turnover was not higher than EUR 25,000, although it expired on 31 December 2016. Luxembourg has requested that the measure be extended as of 1 January 2017 and, in addition, that the threshold be increased up to EUR 30,000 of annual turnover. Such new derogation would be applicable until 31 December 2019.

Double Tax Treaties

Luxembourg had a total of 77 Double Tax Treaties (DTT) in force, most of them being in line with the OECD exchange of information standards. In addition, negotiations with other states are under way to either amend existing DTTs or to adopt new DTTs.

Double Tax Treaty between Luxembourg and Australia – Negotiations

On 29 September 2016, Luxembourg and Australia expressed their intention to negotiate and sign a DTT further to a meeting held in Sydney between officials of both countries.

Protocol to Double Tax Treaty between Luxembourg and Ukraine – signed and ratified by Luxembourg

On 30 September 2016, Luxembourg and Ukraine signed an amending protocol to the (not yet in force) DTT signed on 6 September 1997. The protocol provides for an extension of the definition of "permanent establishment", a new exchange of information clause (Article 26), together with application of the following withholding tax rate:

- 15% on dividends or 5% if the receiving company owns at least 20% of the capital of the company paying the dividends
- 10% on interest paid, but 5% on interest paid in connection with the sale on credit of industrial, commercial or scientific equipment or interest on bank loans
- 10% on royalties paid, but 5% on royalties regarding copyright on scientific work, patent, trademark, secret

formula or process information concerning industrial, commercial or scientific experience.

On 23 December 2016, Luxembourg ratified the protocol. Further to national implementations in both countries, the protocol should enter into force 15 days following the last notification of implementation given by one of the two states.

Double Tax Treaty between Luxembourg and Iran – Negotiations

On 17 October 2016, Luxembourg and Iran have expressed their intention to negotiate and sign a DTT further to a meeting held in Tehran between officials of both countries.

Protocol to Double Tax Treaty between Luxembourg and Tunisia entered into force

On 30 November 2016, the protocol signed on 8 July 2014 amending the DTT between Luxembourg and Tunisia entered into force further to reciprocal implementation by both countries of the protocol within their domestic laws. The protocol shall have effect on 1 January 2017.

Please refer to the November 2014, July 2015 and April 2016 editions of our Luxembourg Legal Update for further details on the above.

Double Tax Treaty between Luxembourg and Serbia entered into force

On 27 December 2016, the DTT between Luxembourg and Serbia signed on 15 December 2015 entered into force further to reciprocal implementation by both countries of the DTT within their domestic laws. The DTT shall have effect on 1 January 2017.

Please refer to the April 2016 edition of our Luxembourg Legal Update for further details on the above.

Double Tax Treaty between Luxembourg and Uruguay – ratified by Luxembourg

On 23 December 2016, Luxembourg ratified the DTT signed on 10 March 2015. Further to national implementations in both countries, the DTT should enter into force on 11 January 2017.

Please refer to the July 2015 and April 2016 editions of our Luxembourg Legal Update for further details on the above.

Double Tax Treaty between Luxembourg and Brunei Darussalam entered into force

On 26 January 2017, the DTT between Luxembourg and Brunei Darussalam signed on 14 July 2015 entered into force further to reciprocal implementation by both countries of the DTT within their domestic laws. The DTT shall have effect on 1 January 2018.

Double Tax Treaty between Hungary and Luxembourg entered into force

On 26 January 2017, the DTT between Luxembourg and Hungary signed on 10 March 2015, which replaced the DTT signed on 15 January 1990 entered into force further to reciprocal implementation by both countries of the DTT within their domestic laws. The DTT shall have effect on 1 January 2018.

Please refer to the July 2015 edition of our Luxembourg Legal Update for further details on the above.

Circulars/Regulatory Developments

Circular confirming the Abolition of the Temporary Budget Tax

Circular IEBT 2 of 24 January 2017

Further to the adoption of the bill of law N°7020 on 14 December 2016 (enacted on 23 December 2016), (please refer to the November 2016 edition of our Luxembourg Legal Update for more information) and as confirmed by Circular IEBT 2, the temporary tax to balance the state budget (*impôt d'équilibrage budgétaire temporaire*) of 0.5% which applied to all categories of income received by individuals in Luxembourg was abolished. This tax was, therefore, levied for two years (2015 and 2016).

New Luxembourg Transfer Pricing Circular

Transfer pricing circular L.I.R. N°56/1 – 56*bis*/1 of 27 December 2016

On 27 December 2016, the Luxembourg tax authorities issued a new transfer pricing circular (Circular N°56/1 – 56*bis*/1 replacing the previously applicable transfer pricing circulars N°164/2 of 28 January 2011 and 164/2 *bis* of 8 April 2011) aimed at clarifying the tax treatment applicable to companies realising intra-group financing transactions, effective from 1 January 2017. The new transfer pricing circular which is based on Article 56bis LITL provides for additional guidance in terms of substance and transfer pricing requirements in order to be in line with the key principles of the OECD transfer pricing guidelines. The key elements are the following:

- Credit risk: Repeal of the minimum equity at risk of at least 1% of the financing investments (e.g. loan receivables) or EUR 2 million and replaced by a "genuine" equity at risk approach, i.e. to be evaluated on a case-by-case basis taking into account the facts and circumstances of a specific transaction (pursuant to a comparability analysis).

- Comparability analysis: New methodology to be applied in order to determine the arm's-length margin; such analysis is a two-pronged analysis which is based on, notably, the economic background, the contractual terms of the financing, the functional analysis (i.e. to identify the economically significant activities, responsibilities and functions, the assets used or provided and the risks assumed by the parties in the context of the transaction) and the risk analysis in financial relationship (including the substance level of the company).
- Substance: Set of criteria on substance further elaborated in order to ensure that the Luxembourg group financing company has the decision-making capabilities to execute the transaction and to monitor the credit risk but also to ensure its actual presence in Luxembourg (e.g. majority of its board composed of members being either Luxembourg tax residents or having at least 50% of their professional income taxed in Luxembourg; key decisions for the management taken in Luxembourg and adequately documented).
- Arm's-length remuneration: for simplification purposes, the circular provides for a minimum remuneration that would be considered at arm's length. In this respect, a minimum return of 2% after tax on the financed assets received by a Luxembourg company acting solely as an intermediary (i.e. uses loans or advances from related entities to grant loans or advances to related entities) would be considered as acceptable. This minimal return is only a benchmark, and another return adequately documented could always be applied.
- Validity of existing advance pricing agreements ("**APA**"): APAs are no longer applicable as from 1 January 2017. Companies wishing to obtain an APA must file a new request before the Luxembourg tax authorities and comply with the new requirements set by the new Circular.

FATCA – Luxembourg and United States

Amendments to the Administrative Circular ECHA N°3 describing the Technical Implementation Aspects of the Exchange of Information under FATCA

On 19 January 2017, the Luxembourg tax administration published amendments to Circular ECHA N°3 describing the technical aspects of the exchange of information under FATCA and to be used by financial institutions for submitting the required information to the Luxembourg tax administration. The amended Circular ECHA N°3 mainly deals with the application of a new format for the exchange of information.

CRS – Luxembourg

Administrative Circular ECHA N°4 published by Luxembourg Tax Authorities

On 6 February 2017, the Luxembourg tax authorities published the Administrative Circular ECHA N°4 on Common Reporting Standard (CRS) reporting which sets the format to be used by Luxembourg reporting financial institutions in order to submit the required information to the Luxembourg tax administration.

Publication of Circular ECHA N°4 has the purpose of correctly putting into application the law of 18 December 2015 on automatic exchange of financial account information and implementation of EU Directive 2014/107/EU amending EUR Directive 2011/16/EU regarding mandatory automatic exchange of information in the field of taxation.

Please refer to the November 2015 and April 2016 editions of our Luxembourg Legal Update for further details on the above.

Grand Ducal Decree of 23 December 2016 – Update of the Participating Jurisdictions under CRS

On 23 December 2016, a new Grand Ducal Decree amending the Grand Ducal Decree of 15 March 2016 was published, which updated the list of participating jurisdictions with which Luxembourg will effectively exchange information for the purpose of CRS.

Functional Currency for Tax Purposes

Appendix to Circular L.G. N°60 on the use of Non-Euro Functional Currency for Tax Purposes

On 20 January 2017, the Luxembourg tax authorities issued Circular L.G. – A N°60bis/2 as appendix to Circular L.G. N°60 providing for the 2016 foreign exchange rates (at closing of 2016 or an average rate thereabouts) published by the European Central Bank and to be used for tax purposes (e.g. 2016 tax returns).

Tax Reform 2017: Registration Duties and Inheritance Taxes

Circular N° 782 of 2 January 2017

On 27 January 2017, the director of the Luxembourg indirect tax administration (*administration de l'enregistrement et des domaines*) issued Circular N°782 clarifying amendments to the registration duties and inheritances taxes made by the law of 23 December 2016 implementing the 2017 tax reform which provides for the abolition of:

- the mandatory registration of any deed used
- the registration of lease agreements.

Until 1 January 2017, any private deed such as debt claims was subject to either a fixed or *ad valorem* registration duty as a result of its usage. According to the so-called usage theory (*théorie de l'usage*), a deed, which by its form or nature was not legally subject to registration, was nonetheless required to be registered if such deed was referred to in a public deed or used in front of courts.

As from 1 January 2017, the private deeds would no longer be subject to the usage theory. However, the circular clarifies that the "usage theory" would continue to apply to deeds that must legally be registered within a certain deadline. In addition, any deed (including, thus, private deeds) would have to be registered if the deed is attached (*annexé*) to a deed subject to a mandatory registration (e.g., public deed) or lodged with a notary's records (*déposé au rang des minutes d'un notaire*), in which case a fixed or *ad valorem* registration duty will still be due. Finally, one should recall that a voluntary registration of a deed, including private deeds, would continue to trigger registration duties.

With respect to lease agreements, the three-month legal period to mandatorily register a lease has been abolished for any lease agreement executed as from 1 January 2017. However, the circular also clarifies that the same rule applies to lease agreement concluded after 30 September 2016 but not registered before 31 December 2016. For further details, please refer to the Litigation section of this Luxembourg Legal Update.

The Luxembourg Tax Authorities clarifies the Withholding Tax Regime on Directors' Fees

Circular L.I.R. N° 45/2 – 152/1 – 168/1 of 14 February 2017

On 14 February 2017, the director of the Luxembourg tax administration issued circular N°45/2 – 152/1 – 168/1 on the withholding tax treatment applicable to directors' fees. Such circular follows the publication of circular N°781 on the VAT treatment of directors' fees published on 30 September 2016. The latter confirmed that independent directors who perform directorship services realise an economic activity subject to VAT and are thus VATable persons taxable for VAT purposes. As a result, the directors are required to be VAT registered and must comply with all VAT formalities. Please refer to the November 2016 edition of our Luxembourg Legal Update for further details.

This new circular clarifies the impact of VAT to directors' fees from a direct tax perspective for both the independent directors and the debtor.

With respect to the independent directors:

- Any director fee paid is subject to a 20% withholding tax. The taxable basis on which the withholding tax is levied corresponds to the gross income payable but not including the VAT to be applied.
- The 20% withholding tax is final for Luxembourg tax residents if the net director fee does not exceed EUR 1,500 per annum (EUR 100,000 for Luxembourg non-tax residents provided that the director did not earn any other Luxembourg source income). If the director has to file a tax return, the director's fee to be reported would correspond to the gross income including VAT. VAT would, however, be deductible as a professional expense.

With respect to the debtor (e.g. Luxembourg paying company):

- Directors' fees paid would not be tax-deductible for corporate tax purposes. As for the input VAT paid on the directors' fees, if such VAT is non-VAT deductible (e.g. the company does not have any VAT deduction right), it would also not be tax deductible for corporate tax purposes. On the contrary, if the paying company has a full VAT deduction right (or only partial), the input VAT would be fully tax deductible (or partially deductible) for corporate tax purposes.

The Luxembourg Tax Authorities issued a New Circular on the Final Withholding Tax Regime applicable to Saving Income

Circular Relibi N°1 of 27 February 2017

On 27 February 2017, the Luxembourg tax authorities issued a new circular on the final withholding tax regime applicable to savings income replacing the Circular Relibi N°1 dated 4 February 2009.

This circular clarifies the application of the law of 23 December 2005, as amended (the "**Relibi Law**") following the repeal of the law of 21 June 2005 in 2016 but also the increase of the withholding tax rate from 10% to 20% (further to the implementation of the law of 23 December 2016). The new circular essentially restates what the Circular Relibi N°1 dated 4 February 2009 was providing and, in particular, makes reference to each article of the Relibi Law with clarifications and practical explanations.

Electronic VAT Filing

Press Release of 19 January 2017 from the VAT Authorities

On 19 January 2017, the VAT administration published a press release reminding taxable persons required to file VAT returns that, as from 1 January 2017, all VAT returns, annexes and supporting documents would have to be filed electronically.

Glossary

ABBL: Luxembourg Banks and Bankers' Association

ACA: *Association des Compagnies d'Assurance*, Luxembourg Association of Insurance Undertakings

AIFM: Alternative Investment Fund Managers

AIF: Alternative Investment Fund

AIFM Directive: Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on alternative investment fund managers

AIFs: Alternative Investment Funds

ALFI: Association of the Luxembourg Fund Industry

AML Law: Luxembourg law of 12 November 2004 (as amended) on the fight against money laundering and terrorism financing

AML/CTF: Anti-Money Laundering and Counter-Terrorism Financing

AMLD 4: Directive (EU) 2015/849 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing

Bank Resolution: Luxembourg law of 18 December 2015 law on the failure of credit institutions and of certain investment firms implementing the BRRD and DGSD 2

BCBS: Basel Committee on Banking Supervision

BCL: *Banque Centrale du Luxembourg*

Benchmark Regulation: Regulation (EU) 2016/1011 of the European Parliament and the Council of 8 June 2016 on indices used as benchmarks in financial instruments and financial contracts

BRRD: Directive 2014/59 of 15 May 2014 establishing a framework for the recovery and resolution of credit institutions and investment firms

CCCTB: Common Consolidated Corporate Tax Base

CESR: Committee of European Securities Regulators (replaced by ESMA)

CAA: *Commissariat aux assurances*, the Luxembourg insurance sector regulator

Companies Law: Luxembourg law of 10 August 1915 (as amended) on commercial companies

Consumer Act: Luxembourg law of 25 August 1983 (as amended) concerning the legal protection of the Consumer

Collective Bank Bargain Agreement: *La convention collective du travail applicable aux banques*

CRA: Credit Rating Agencies

CRD: Capital Requirements Directives 2006/48/EC and 2006/49/EC

CRD III: Directive 2010/76/EU amending the CRD regarding capital requirements for the trading book and for resecuritisations, and the supervisory review of remuneration policies

CRR/CRD IV Package: Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC and Regulation (EU) N° 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms, and amending Regulation (EU) N°648/2012 Text with EEA relevance

CSDR: Regulation (EU) N°909/2014 of the European Parliament and of the Council of 23 July 2014 on improving securities settlement in the European Union and on central securities depositories and amending Directives 98/26/EC and 2014/65/EU and Regulation (EU) No 236/2012

CSSF: *Commission de Surveillance du Secteur Financier*, the Luxembourg supervisory authority of the financial sector

Data Protection Law: Luxembourg law of 2 August 2002 (as amended) on the protection of persons with respect to the processing of personal data

DGSD 2: Directive 2014/49 of 16 April 2014 on deposit guarantee schemes

EBA: European Banking Authority

ECB: European Central Bank

ECJ: European Court of Justice

EIOPA: the European Insurance and Occupational Pensions Authority

ESMA: European Securities and Markets Authority

ESRB: European Systemic Risk Board

ETDs: Exchange Traded Derivatives

ETFs: Exchange Traded Funds

EUIR: European Union Insolvency Regulation: Council regulation (EC) N° 1346/2000 of 29 May 2000 on insolvency proceedings

EUIR (Recast): Regulation (EU) 2015/848 of the European Parliament and of the Council of 20 May 2015 on insolvency proceedings

FATF: Financial Action Task Force/*Groupe d'Action Financière* (FATF/*GAFI*)

FCP: *Fonds Commun de Placement or mutual fund*

Financial Collateral Directive: Directive 2002/47/CE of 6 June 2002 on financial collateral arrangements

Financial Collateral Law: Luxembourg law of 5 August 2005 (as amended) on financial collateral arrangements

Financial Sector Law: Luxembourg law of 5 April 1993 (as amended) on the financial sector

ICMA: International Capital Market Association

Insolvency Regulation: Council Regulation (EC) 1346/2000 of 29 May 2000 on insolvency proceedings

Insurance Sector Law: Luxembourg law of 6 December 1991 (as amended) on the insurance sector

IORP Directive: Directive 2003/41 of the European Parliament and the Council dated 3 June 2003 on the activities and supervision of institutions for occupational retirement provision

IRE: *Institut des Réviseurs d'Entreprises*

KIID: Key Investor Information Document (within the meaning of the UCITS Directive) that aims to help the investors to understand the key features of their proposed UCITS investment

Law on the Register of Commerce and Annual Accounts: Luxembourg law of 19 December 2002 (as amended) relating to the register of commerce and companies and the accounting

RCSL or **Register of Commerce**: Luxembourg register of commerce and companies (*Registre de commerce et des sociétés de Luxembourg*)

Law on the Registration of Real Estate: Luxembourg law of 25 September 1905 (as amended) on the registration of real estate rights *in rem* (*loi du 25 septembre 1905 sur la transcription des droits reels immobiliers*)

MiFID: Directive 2004/39/EC of the European Parliament and of the Council dated 21 April 2004 on markets in financial instruments, amending Council Directives 85/611/EEC and 93/6/EEC and Directive 2000/12/EC of the European Parliament and of the Council, and repealing Council Directive 93/22/EEC

PFS: Professional of the Financial Sector other than a credit institution and subject to CSSF's supervision in accordance with the Financial Sector Law

Public Contracts Law: Luxembourg law of 25 June 2009 (as amended) on government contracts

Public Contracts Regulation: The Grand-Ducal Regulation of 3 August 2009 implementing the Law of 25 June 2009 on public contracts

Public Interest Entities:

a) entities governed by the law of a EU member state, whose securities are admitted to trading on a regulated market of a member state within the meaning of article 4, paragraph 1, point 21 of the directive 2014/65/EU

b) credit institutions as defined under article 1, point 12 of the law of 5 April 1993 on the financial sector as amended, other than the institutions covered by article 2 of the directive 2013/36/EU

c) insurance and reinsurance undertakings as defined under article 32, paragraph 1, points 5 and 9 of the law of 7 December 2015 on the insurance sector, to the exclusion of the entities covered by articles 38, 40 and 42, of the pension funds covered by article 32, paragraph 1, point 14, of the insurance captive companies covered by article 43, point 8 and reinsurance captive companies covered by article 43, point 9 of the law dated 7 December 2015 on the insurance sector.

Prospectus Regulation: Regulation (EC) N°809/2004 of 29 April 2004 implementing the Directive as regards information contained in prospectuses as well as the format, incorporation by reference and publication of such prospectuses and the dissemination of advertisements

Rating AgencyPRIIPs KID Regulation: Regulation (EC) N°1060/2009EU) N°1286/2014 of the European Parliament and of the Council OF 26 November 2014 on key information documents for packaged retail and insurance-Based investment products

Rating Agency Regulation: Regulation (EC) N°1060/2009 of the European Parliament and the Council on credit rating agencies

RCSL or **Register of Commerce**: Luxembourg register of commerce and companies (*Registre de commerce et des sociétés de Luxembourg*)

REMIT: Regulation (EU) N°1227/2011 of 25 October 2011 on wholesale energy market integrity and transparency

SFTR: Regulation (EU) No 2015/2365 of the European Parliament and the Council of 25 November 2015 on transparency of securities financing transactions and of their reuse and

SICAR Law: Luxembourg law of 15 June 2004 (as amended) on investment companies in risk capital

SIF Law: Luxembourg law of 13 February 2007 (as amended) relating to specialised investment funds

Takeover Law: Law of 19 May 2006 on public takeover bids

SRB: the Single Resolution Board

SRF: the Single Resolution Fund

SRM: the Single Resolution Mechanism

SSM: the Single Supervisory Mechanism

Transparency Law: Luxembourg law of 11 January 2008 (as amended) on the transparency obligations concerning information on the issuers of securities admitted to trading on a regulated market

UCI Law: Luxembourg law of 17 December 2010 (as amended) on undertakings for collective investment

UCITS Directive: Directive 2009/65/EC of 13 July 2009 of the EU Parliament and of the Council on the coordination of laws, regulations and administrative provisions relating to UCITS

UCITS V Directive: Directive 2014/91/EU of the European Parliament and Council of 23 July 2014 amending Directive 2009/65/EC as regards depositary functions, remuneration policies and sanctions

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