NEWSLETTER

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ELVINGER, HOSS & PRUSSEN
LUXEMBOURG LAW FIRM

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CAPITAL MARKETS

1. ENFORCEMENT OF THE 2012 FINANCIAL INFORMATION

On 9 January 2013, the CSSF issued Press Release 13/01 relating to the enforcement of the financial information prepared by issuers of securities subject to the law of 11 January 2008 on transparency requirements for issuers of securities ("**Transparency Law**").

This Press Release is particularly addressed to those issuers who prepare their financial statements in accordance with the International Financial Reporting Standards ("**IFRS**") for the 2012 fiscal year.

Following the topics identified by ESMA as priorities within the scope of the supervision exercised by the national competent authorities, the CSSF will review, among other things, the following issues:

- financial instruments: the CSSF will continue to focus on the qualitative and quantitative information provided regarding the exposure to risks related to financial instruments as well as on valuation and impairment issues related to these instruments;
- non-financial assets, with a specific focus on the accounting treatment of the impairment of tangible and intangible assets, including goodwill and other intangible assets with an indefinite useful life;
- valuation of pension obligations related to defined benefit plans, in particular regarding the discount factors to be applied;
- the information to be provided within the framework of the standard IAS 37 for each type of provision, contingent asset and contingent liability.

Regarding the valuation of investment property, the CSSF will also review in detail the methods and assumptions made by the issuers when calculating the fair value of these assets.

More details as to specific standards of IFRS to be particularly reviewed by the CSSF are given in the Press Release as well as in the annual reports of the CSSF which are available on its website.

2. CONTENT OF THE MANAGEMENT REPORTS

On 5 February 2013, the CSSF published Press Release 13/09 on the review of the management reports published by the issuers of shares or depositary receipts in respect of shares subject to the Transparency Law.

This document can be viewed under:
http://www.cssf.lu/fileadmin/files/Publications/Communiques/Communiques_2013/CP_1309_review_management_reports_ENG.pdf

3. DERIVATIVES - EMIR

On 23 January 2013, the CSSF published Circular 13/557 ("**Circular**") regarding the EU Regulation 648/2012 of 4 July 2012 on OTC derivatives, central counterparties and trade repositories (commonly referred to as the European Market Infrastructure Regulation or "**EMIR**"). The Circular highlights the key obligations under EMIR and outlines its scope of application. It also gives information on the status of the additional implementing and delegated regulations which are required to be adopted within the framework of EMIR.

The objectives of EMIR are to increase transparency in the derivatives market and to make it safer by reducing counterparty credit risk and operational risk.

The main obligations under EMIR are the following:

- clearing: obligation to clear certain classes of OTC derivatives through a CCP[1] . ESMA will specify the class of OTC derivatives which will be subject to a central clearing obligation;
- risk management and collateral requirements: implementation of risk management and risk mitigation procedures for OTC derivatives which are not centrally cleared; and
- reporting: obligation to report all derivative transactions.

In order to promote common supervisory approaches and practices in the application of EMIR, ESMA recently published a Q&A on the practical implementation of EMIR (ESMA/2013/324).

The Circular can be viewed under:
http://www.cssf.lu/fileadmin/files/Lois_reglements/Circulaires/Hors_blanchiment_terrorisme/cssf13_557.pdf

The Q&A can be viewed under:
http://www.esma.europa.eu/system/files/2013-324.pdf

4. SHORT SELLING

On 30 January 2013, ESMA published an updated version of the Q&A on short selling and certain aspects of credit default swap.

This document can be viewed under:
http://www.esma.europa.eu/content/QA-Implementation-Regulation-short-selling-and-certain-aspects-credit-default-swaps-2nd-upda

On 1 February 2013, ESMA also published Guidelines on the exemption for market making activities and primary market operations under Regulation 236/2012 on short selling.

This document can be viewed under:
http://www.esma.europa.eu/content/Guidelines-exemption-market-making-activities-and-primary-market-operations-under-Regulation

5. DEMATERIALISED SECURITIES

On 21 March 2013, the Luxembourg law on dematerialised securities was adopted by the Luxembourg Parliament. The law has not yet been published in the official journal (i.e. the *Mémorial*) but the final report of the relevant parliamentary commission relating to the law can be viewed under:
http://www.ehp.lu/fileadmin/user_upload/legal_topics/corporate/PL_6327_Titres_dematerialises_Rapport.pdf

An analysis of the law will be published in the next edition of the Newsletter.

[1] CCP is defined in Article 2(I) of EMIR

FINANCIAL INSTITUTIONS

1. THE POWERS OF THE EUROPEAN SUPERVISORY AUTHORITIES

By a Law dated 21 December 2012[2], Luxembourg authorities implemented the omnibus Directive 2010/78/EU[3]. The Law specifies the powers of the new European Supervisory Authorities ("**ESAs**"), i.e. the European Banking Authority ("**EBA**"), the European Insurance and Occupational Pensions Authority ("**EIOPA**"), and the European Securities and Markets Authority ("**ESMA**"). These powers include the development of draft technical standards which have to be adopted by the European Commission in the form of regulations or of decisions via the procedures of Articles 290 and 291 of the Treaty on the Functioning of the European Union.

In order for the ESAs to work effectively, changes had to be made to existing financial services directives and to national legislations. The Law of 21 December 2012 reflects these changes.

This Law is currently only available in French and can be viewed under:
http://www.legilux.public.lu/leg/a/archives/2012/0275/a275.pdf

2. ANTI-MONEY LAUNDERING

The CSSF Regulation 12-02 of 14 December 2012 regarding the fight against money laundering and terrorist financing ("**Regulation**") was published on 9 January 2013 and entered into effect on 13 January 2013.

This Regulation intends to reinforce and complete the applicable regulatory framework in Luxembourg with regard to the fight against money laundering and terrorist financing ("**AML/CTF**"). It forms part of the measures undertaken in order to improve the Luxembourg AML/CTF device further to the mutual evaluation report of Luxembourg adopted by the FATF (*GAFI*) in February 2010.

The Regulation confers a formal and legally binding nature on existing professional obligations set out previously by CSSF circulars. CSSF Circulars 08/387 and 10/476 are consequently repealed. Generally, the existing professional obligations remain applicable.

The main changes and novelties introduced by the Regulation concern the following topics:

- The risk-based approach has been extended. Professionals are required to perform a risk assessment (i) of their customers according to a certain level of risk, taking into account a consistent combination of risk categories and determined risk variables, and (ii) of countries in order to determine if equivalent obligations are applicable (EU Member States are considered as equivalent except when relevant information proves otherwise).
- Some customer due diligence obligations have been specified. Professionals should implement a client acceptance policy and obtain information regarding (i) natural and legal persons (the Regulation contains a defined list of minimum information to be obtained and provides that clients should sign a declaration stating explicitly that they act for themselves or on behalf of other persons and commit to communicate any subsequent changes without delay), (ii) the proper identity of beneficial owners (threshold of ownership and control may be below the 25% threshold), and (iii) the origin of funds of the customers and the type of transactions envisaged.
- With regard to adequate internal organisation, the Regulation provides that professionals should implement a hiring

[2] The Law of 21 December 2012 was published in the *Mémorial A* on 28 January 2012. This law also introduces new requirements applying to Luxembourg advisers (see section "Other Regulated Activities")
[3] Directive 2010/78/EU of 24 November 2010 amending Directives 98/26/EC, 2002/87/EC, 2003/6/EC, 2003/41/EC, 2003/71/EC, 2004/39/EC, 2004/109/EC, 2005/60/EC, 2006/48/EC, 2006/49/EC and 2009/65/EC in respect of the powers of EBA, EIOPA and ESMA

procedure and a written training programme for the members of the staff, and an AML/CTF policy tailored according to the professional activity, structure, size, internal organisation and resources, covering all professional obligations.

- Cooperation with authorities has been strengthened and covers also the situations where a professional gets in touch with a person without establishing a business relationship.
- The auditing of financial statements by the *réviseur d'entreprises agréé* covers compliance with AML/CFT obligations and regulatory provisions. This annual control shall include the subsidiaries and branches of the professional abroad.

3. DEPOSIT GUARANTEE: INTRODUCTION OF A "SINGLE CUSTOMER VIEW" FILE

On 8 January 2013, the CSSF published Circular 13/555 on the implementation of the decision made by the board of directors of the *Association pour la Garantie des Dépôts, Luxembourg (AGDL)* to introduce a "Single Customer View" file within the framework of the deposit guarantee.

This document is currently only available in French and can be viewed under: http://www.cssf.lu/fileadmin/files/Lois_reglements/Circulaires/Hors_blanchiment_terrorisme/cssf13_555.pdf

4. EVOLUTION, CONTROL AND MANAGEMENT OF RESOURCE ACCESS TOOLS

On 7 January 2013, the CSSF published Circular 13/554 on the evolution of the usage and control of tools for managing information technology resources and the management of access to these resources.

This document can be viewed under: http://www.cssf.lu/fileadmin/files/Lois_reglements/Circulaires/Hors_blanchiment_terrorisme/cssf13_554eng.pdf

5. CENTRAL ADMINISTRATION, INTERNAL GOVERNANCE AND RISK MANAGEMENT

The CSSF Circular 12/552 of 11 December 2012 on central administration, corporate governance and risk management implements the updated Guidelines on Internal Governance by the European Banking Authority ("**EBA**") of 27 September 2011 and the revised supervisory guidance of the Basel Committee on Banking Supervision ("**BCBS**") of 28 June 2012.

At the same time the CSSF took the opportunity to consolidate and further detail the existing Luxembourg requirements relating to internal governance and risk management of credit institutions and investment firms and outsourcing by such undertakings.

The CSSF Circular 12/552 replaces the existing circulars applicable to banks and investment firms in these fields. In addition, the CSSF Circular 12/552 contains certain provisions on basic prudential principles to be applied by the banks and investment firms in the granting of credits, with a special focus on real estate credits in Luxembourg, and private wealth management.

The CSSF Circular 12/552 was updated on 19 March 2013 by Circular 13/563 which incorporates the EBA guidelines on the assessment of the suitability of members of the management body and key function holders (EBA/GL/2012/06) and the ESMA Guidelines on certain aspects of the MiFID compliance function requirements (ESMA/2012/388).

According to the CSSF, Circular 12/552 is a "*first step towards a consolidated regulatory handbook on internal governance, in its broadest sense*". The next steps of the CSSF will be to supplement it by the requirements on risks, risks measurement and their management on which the current provisions of the Circular 12/552 remain rather general.

The Circular 12/552, as amended by Circular 13/563, is applicable as from 1 July 2013 except for the following requirements for which the circular provides for a transitory period until 1 January 2014:

- composition and qualification of the board of directors;
- the establishment of special committees (such as credit institution committees, risk committees, remuneration committees, human resources committees) and the provisions relating thereto , except for the internal audit committees which shall be put in place as from 1 July 2013;
- prohibition to combine the mandate as chairman of the board of directors of the undertaking with the capacity of member of the authorised management;
- the requirement to establish in writing guidelines on (i) organisational and operational structure and information technology systems (including arrangements on security, internal communication and internal alert) (ii) internal control and remuneration policies, escalation procedures and sanctions as well as internal rules of conduct (iii) central administration in Luxembourg, including administrative, accounting and IT organisation and outsourcing (iv) business continuity plan and (v) appointment and replacement of key functions of executives of the undertaking, including authorised executive management and members of the board of directors, and procedures governing the board of directors (including composition, responsibilities, organisation and operating).

For further details, you may refer to the updated version of Circular 12/552 published on the website of the CSSF (only in French): http://www.cssf.lu/fileadmin/files/Lois_reglements/Circulaires/Hors_blanchiment_terrorisme/cssf12_552_upd190313.pdf

6. NEW MIFID REQUIREMENTS: SUITABILITY TEST

The CSSF Circular 13/560 (published on 19 February 2012) implements ESMA's "Guidelines on certain aspects of the MiFID suitability requirements", published on 6 July 2012, into Luxembourg regulations by adding them as Annex IV to Circular CSSF 07/307. These guidelines concern Chapter 6 of Circular CSSF 07/307 and aim at clarifying the suitability requirements for a service to a client. More specifically, ESMA's guidelines concern information to clients about the suitability assessment, as well as updating of client information. Moreover, the guidelines relate to the arrangements necessary to enable investment firms to understand the essential facts about their clients and the characteristics of the financial instruments available for those clients, as well as the qualifications of the staff involved in the suitability assessment.

The guidelines are available on ESMA's website (reference ESMA/2012/387) at www.esma.europa.eu.

The CSSF Circular 13/560 can be viewed under: http://www.cssf.lu/fileadmin/files/Lois_reglements/Circulaires/Hors_blanchiment_terrorisme/cssf13_560eng.pdf

INVESTMENT VEHICLES

1. UCITS

1. Investments in open-ended funds subject to Article 50(2)(A) of the UCITS Directive ("Trash Ratio")

According to the ESMA Opinion 2012/721 dated 20 November 2012, UCITS may only invest in units or shares of collective investment undertakings as defined in Article 50(1)(e) of the UCITS Directive (as transposed via Article 41(1)e) of the Luxembourg Law of 17 December 2010 relating to undertakings for collective investment) (see our Newsflash of 21 November 2012).

On 23 November 2012, the CSSF published Press Release 12/46 drawing attention to ESMA's Opinion (see our Newsflash of 28 November 2012).

2. ETF and other UCITS issues: ESMA Guidelines for competent authorities and UCITS management companies (ESMA/2012/832)

On 17 December 2012, ESMA published Guidelines for competent authorities and UCITS management companies. These guidelines can be viewed under: http://www.esma.europa.eu/content/Guidelines-ETFs-and-other-UCITS-issues.

These guidelines were transposed into Luxembourg legislation by the CSSF Circular 13/559. An English version is available on our website: http://www.ehp.lu/uploads/media/CIRC_CSSF_13-559_OPC_ENG.pdf

3. ETF and other UCITS issues: ESMA Guidelines on repurchase and reverse repurchase agreements (ESMA/2012/722)

On 4 December 2012, ESMA published Guidelines on repurchase and reverse repurchase agreements.

These guidelines can be viewed under: http://www.esma.europa.eu/content/Guidelines-repurchase-and-reverse-repurchase-agreements

4. ETF and other UCITS issues : Q&A on ESMA's Guidelines (ESMA/2013/314)

On 15 March 2013, ESMA published Q&A on Guidelines on ETFs and other UCITS issues. This Q&A can be viewed under: http://www.esma.europa.eu/system/files/2013-314.pdf

5. ALFI GUIDELINES FOR UCITS LIQUIDITY RISK MANAGEMENT

The purpose of these Guidelines, which were published on ALFI's website on 7 March 2013, is to provide guidance to the Luxembourg fund industry, with regard to liquidity risk management for UCITS. Particular features of non-UCITS or ETF structures are not, however, addressed in this document.

These guidelines can be viewed under: http://www.alfi.lu/node/2247

6. UCITS MANAGEMENT COMPANIES AND SELF-MANAGED SICAVs: FORM FOR COMPLIANCE WITH CIRCULAR 12/546

On 12 March 2013, the CSSF published a form to be completed by Chapter 15 management companies and UCITS self-managed SICAVs to confirm their compliance with CSSF Circular 12/546. Chapter 15 management companies and UCITS self-managed SICAV will have to provide the CSSF with the detailed information required pursuant to CSSF Circular 12/546 and this questionnaire by 15 April 2013.

This questionnaire is only available in English. It can be found on the following link: http://www.cssf.lu/fileadmin/files/Formulaires/Form_for_compliance_circular_12_546.doc

2. AIFMD

1. AIFMD consolidated brochure

For a detailed regulatory overview on the AIFMD, see our AIFMD consolidated brochure: http://www.ehp.lu/uploads/media/Directive_2011_61_EU_Consolidated_version.pdf

2. AIFMD level 2 and level 3 measures

On 19 December 2012, the EU Commission published the long-awaited and important set of level 2 AIFMD measures. The delegated regulation further specifies the following topics: AIFMD exemptions, general operating conditions, depositaries, leverage, transparency and supervision. The delegated regulation will enter into force on 22 July 2013, without the need for any transposition into national law.

This document can be viewed under: http://eur-lex.europa.eu/JOHtml.do?uri=OJ:L:2013:083:SOM:EN:HTML

This first set of AIFMD level 2 measures was completed in February 2013 by the publication of level 3 measures, i.e. the ESMA Guidelines on sound remuneration policies under the AIFMD (ESMA 2013/201);

On the same day as the publication of the AIFMD level 2 measures, ESMA published two consultation papers:

- Consultation paper on draft regulatory technical standards on types of AIFMs (ESMA 2012/844) and
- Consultation paper on draft guidelines on key concepts of the AIFMD (ESMA/2012/845)

Although not yet final, these two consultation papers also constitute an important source of information. The consultation on draft guidelines on key concepts of the AIFMD in particular provides clarification on each of the concepts used in the definition of an alternative investment fund, i.e. the notion of "collective investment undertaking", "raising capital", "number of investors" and "defined investment policy".

3. Cooperation arrangements with third country supervisors

Cooperation arrangements have been concluded by ESMA with Switzerland (ESMA/2012/798) and Brazil (ESMA 16 January 2013).

OTHER REGULATED ACTIVITIES

1. FAMILY OFFICE: A NEW REGULATED ACTIVITY IN LUXEMBOURG[4]

By a law of 21 December 2012 relating to the activity of Family Office (the "**Family Office Law**"), Luxembourg created a legal framework for Family Offices by regulating a certain type of "Family Office activity" and reserving the provision of those services to a limited number of regulated professionals.

While recognising that it is not possible to give a universal definition of the "Family Office activity" (which comprises a large spectrum of services (ranging from simple concierge type services to regulated investment management services)) and while admitting the difficulty to define the concept of "family" (which has different scopes depending on jurisdiction and nationality and the limits of which are arbitrary), the Luxembourg legislator endorsed the political will of the government to support the positioning of Luxembourg as a premier centre for private banking and to be the first European country to create a new regulated profession under the label of "Family Office" in Luxembourg.

While other countries such as the USA or Dubai have regulations submitting "Family Offices" to supervision by regulated authorities when they carry out investment management activities (which is anyhow already a regulated activity in Luxembourg), the new Family Office Law adopts a novel approach and submits to regulated supervision Family Office activities to the extent only that the relevant estate to which the activity relates comprises financial assets and limits the provision of services related thereto to certain regulated professionals subject to adequate professional obligations and supervision.

[4] This Article was published in AGEFI Luxembourg of February 2013

1. Family office: a regulated activity to the extent that it relates to estates comprising financial assets

Not all family office type activities are regulated under the new law.

According to article 1 of the Family Office Law, the activity consists in providing, on a professional basis, advice or services of a patrimonial nature (*de nature patrimoniale*) to physical persons, families or estate entities which belong to any of them or on which they are founders or beneficiaries.

The Family Office Law does not contain a definition of the "family" and thus allows a flexible application of the new law where the regulator will be in a position to fine-tune the concept according to the needs of the practitioners while remaining within the spirit of the new law.

The definition of services which will fall within the scope of the Family Office Law includes (i) advice in estate planning or organisation and the administrative or financial follow up thereof or (ii) the coordination among professionals servicing an estate and the follow up or evaluation of their respective performances (excluding any regulated financial activity such as investment advice or portfolio management). The definition specifies that the activity is regulated only as long as it relates to an estate which comprises cash or financial instruments.

Accordingly, other services, which are included in what is commonly understood as family office activity, such as "concierge type activities" or other activities solely related to assets other than cash or financial instruments (e.g. real estate) do not fall within the scope of the newly regulated activity in Luxembourg. Similarly, the Family Office Law excludes from its scope Family Offices set up for a single family, as well as mandates assumed in companies, foundations, trusts, fiduciary contracts and judicial mandates (e.g. activity as a guardian). However, while exercising an activity outside of the Family Office Law, professionals still need to consider whether they would not need another licence for carrying out a professional or commercial activity and more importantly, the relevant persons may not use the "Family Office" label which is reserved to professionals under the new law.

2. Family Office: a label reserved to certain types of regulated professionals

Only a limited number of professionals, while exercising the Family Office activity as described under (1) above, may use the label of "Family Office":

- banks, investment advisers or managers;
- corporate domiciliation agents or professionals providing company formation or management services;
- lawyers or notaries;
- auditors or chartered accountants; as well as
- the new category of specialised professionals of the financial sectors licensed as "Family Office".

The last indent refers to a newly created category of licensed professionals of the financial sector ("**PSF**") subject to the law of 5 April 1993 relating to the financial sector which carry out on a professional basis the activity of Family Office as defined under the new Family Office Law. These professionals will be under the supervision of the CSSF to the same extent as other specialised PSF including registrar agents, corporate domiciliation agents etc. Regulated Family Offices do however not qualify as an investment firm and will not benefit from a European passport.

The use of the label of Family Office while carrying out the activities defined in the Family Office Law is reserved to the professionals listed above. Conversely, any person exercising on a professional basis an activity which falls under the scope of the Family Office Law and which is not a regulated professional listed above, will, until 30 June 2013, have to seek a licence as "Family Office" by applying to the CSSF.

3. Family Office: a recognised legal framework offering adequate protection to investors

By reserving the activity of Family Office to a limited number of regulated professionals, the Luxembourg legislator has chosen to offer adequate guarantees to investors and thereby grant a competitive advantage to its financial sector.

The new Family Office Law specifies that the relevant professionals are subject to basic professional duties including anti-money laundering obligations and confidentiality duties in a similar fashion as those applicable throughout the financial sector in Luxembourg. In addition, each professional concerned will be subject to its supervisory authority which will supervise the activities of family office by each professional under its supervision.

In conclusion, the new category of Family Office PSF regulated by the CSSF will raise a particular interest and allow the financial sector supervisory authority to set out basic professional rules and guidelines which need to be followed to guarantee adequate investor protection. The supervision will enhance the trustworthiness of the Family Office activities and add an element to the reliance in the private banking activities of the Luxembourg financial centre.

For more information on the scope and entry into force of the Family Office Law:

CSSF Circular Letter 21 January 2013 (in French)

CSSF Press Release 13/03

2. LUXEMBOURG ADVISERS OF UCI[5] AND SIF[6]

On 10 January 2013, the CSSF published a press release ("**Press Release 13/02**") to alert Luxembourg investment advisers of UCI and SIF ("**Advisers**") to the entry into force of the Law of 21 December 2012 transposing Directive 2010/78/EU of the European Parliament and of the Council of 24 November 2010 ("**2012 Law**"). The 2012 Law amends, inter alia, the Law of 5 April 1993 on the financial sector ("**1993 Law**") by removing advisers of UCI and SIF from the list of persons specifically excluded from the scope of the 1993 Law by virtue of Article 1-1 (2) of the 1993 Law.

Advisers have until 30 June 2013 to regularise their situation, where appropriate. The Advisers concerned were invited to contact the CSSF before 1 March 2013 in order to enable the smooth processing of their request.

As a result of the applications received, the CSSF published an additional press release ("**Press Release 13/12**") on 6 March 2013, whereby the CSSF stated that most of the applications received had come from entities whose activities do not meet the definition of an investment adviser within the meaning of Article 24 of the 1993 Law, to the extent that they do not provide personal recommendations to investor clients and that they are not subject to the rules governing the provision of investment services under the legislation on financial instruments markets. According to the Press Release 13/12, such entities which only advise UCI or SIF do not require authorisation under Article 24 of the 1993 Law.

The CSSF announced that it will soon be issuing a questionnaire seeking information from UCI and SIF on their advisers in order to establish whether some of these require authorisation under the amended 1993 Law, particularly if they provide advice outside the SIF group or UCI group to which they belong.

[5] UCI means undertakings for collective investment subject to the Luxembourg Law of 17 December 2010 on undertakings for collective investment
[6] SIF means specialised investment funds subject to the Luxembourg Law of 13 February 2007 on specialised investment funds

Apart from the impact in terms of authorisation requirements, the actual scope of activities performed by an Adviser needs to be assessed as to its tax impact, notably from a VAT perspective. For further details in that respect, readers are invited to refer to the Tax section of this Newsletter (See ECJ Case -275/11).

The updated version of the 1993 Law can be viewed under:
http://www.cssf.lu/fileadmin/files/Lois_reglements/Legislation/Lois/L_050493_lfs_upd211212.pdf

The CSSF Press Release 13/02 can be viewed under:
http://www.cssf.lu/fileadmin/files/Publications/Communiques/Communiques_2013/PR1302_Advisers.pdf

The CSSF Press Release 13/12 is currently only available in French and can be viewed under:
http://www.cssf.lu/fileadmin/files/Publications/Communiques/Communiques_2013/CP_1312_Conseillers_OPC_FR.pdf

TAX

1. NEW TAX MEASURES APPLICABLE IN 2013

A law dated 21 December 2012 has introduced a number of important new tax measures applicable to both individuals and companies as from 1 January 2013. (see our Newsflash of 9 January 2013). French and German translations of our Newsflash are now also available.

2. ECJ C-275/11 – CASE GFBK – INVESTMENT FUND ADVISORY SERVICES MAY BE VAT EXEMPT

On 7 March 2013, in the case GfBk (C-275/11), the Court of Justice of the European Union (the "**Court**") ruled on an important issue concerning the scope of the VAT exemption applicable for the management of investment funds. (See our Newsflash of 8 March 2013).

1. Factual background

The investment manager of an investment fund had delegated some advisory and information services to an external investment adviser. The investment adviser provided sale and purchase recommendations on transferable securities to the fund manager. However, the investment adviser had no power to buy and sell securities on behalf of the fund.

The German tax authorities had refused to allow the benefit from the VAT exemption on management of investment fund to these services because they were not actual management services but only advisory services.

2. Ruling of the Court

The Court clearly stated that "*advisory services concerning investment in transferable securities, provided by a third party to […] the manager of a special investment fund, fall within the concept of 'management of special investment funds' for the purposes of the* [VAT] *exemption laid down in that provision, even if the third party has not acted on the basis of a mandate*".

The Court recalled the conditions for outsourced services to benefit from the VAT exemption, i.e. the advisory services must be specific to, and essential for, the management of the investment fund. In the case at hand, the Court considered that the direct advice given as to the purchase or sale of transferable securities has an intrinsic connection with the management of the investment fund.

This judgment clearly validates the existing Luxembourg practice and secures the current structuring of many Luxembourg investment funds.

3. TAX TREATIES NEWS

On 15 January 2013, the Luxembourg government tabled a bill 6501 approving the new tax treaties with Germany (replacing the current Treaty of 23 August 1958), Kazakhstan (including the Protocol of 3 May 2012), the Lao People's Democratic Republic, the Republic of Macedonia, the Seychelles, the Democratic Socialist Republic of Sri Lanka and Tajikistan and approving the amendments to the existing tax treaties with Canada, South Korea, Italy, Malta, Poland, Romania, Russia and Switzerland.

The new double tax treaty with Germany will enter into force the year following its ratification by both countries and subsequent exchange of the instruments of ratification. Hence, the new treaty shall enter into force on 1 January 2014 at the earliest. The key amendments to the double tax treaty were highlighted in the July 2012 edition of our Newsletter.

The treaties with Canada, Italy, Malta, Romania and Switzerland are aligned with OECD standards (Article 26 of the OECD Model Convention) with respect to the exchange of information procedure. These provisions create an obligation for the contracting states to exchange information that is relevant to the correct application of a tax treaty and for the administration and enforcement of domestic tax laws. Countries may not, however, engage in "fishing expeditions" and the requesting State must demonstrate the foreseeable relevance of the requested information.

The key amendments to the double tax treaty with Poland were highlighted in the November 2012 edition of our Newsletter.

The protocol of 21 November 2011 (the "**Protocol**") to the Luxembourg-Russia double tax treaty was adopted by Russia by a law dated 2 January 2013. This Protocol should hence enter into force as of 1 January 2014, to the extent that the instruments of ratification will be exchanged during the course of 2013.

The key features of the Protocol can be summarised as follows:

- revised definition of dividends by inclusion of payments made in relation to depositary receipts and payments made in relation to shares/units of investment funds (other than those investing mainly in real estate);
- reduction of dividend withholding tax from 10% to 5% for a direct shareholding of at least 10% and of a value of at least 80,000 euros (or the equivalent in Roubles);
- introduction of a source State taxation of capital gains on the sale of shares from real estate companies which derive more than 50% of their value (directly or indirectly) from real estate assets located in the other contracting State;
- alignment with OECD standards with respect to the exchange of information; and
- new limitation on benefits provisions: implicit confirmation that SICAV/Fs shall benefit from treaty protection.

A more detailed analysis of the changes to be introduced by the Protocol was made in the December 2011 edition of our Newsletter.

4. STOCK OPTIONS: NEW CIRCULAR

On 20 December 2012, the Luxembourg tax authorities issued an amended version of Circular L.I.R 104/2 on the taxation of stock options (the "**Circular**"), which replaces Circular L.I.R 104/2 of 11 January 2002.

Until now, freely transferable stock options (not listed on a stock exchange) which are taxable at grant were valued for personal income tax purposes at 7.5% of the value of the underlying shares/assets (unless a valuation was realised by application of a recognised valuation method, such as the valuation methods of the US economists Myron Scholes and Fischer Black or any other comparable valuation method). The Circular is modified on this point and provides that the options are now to be valued at 17.5% of the value of the underlying shares/assets (unless a valuation based on a recognised valuation method is made). The Circular (in the same way as the former circular) gives no further explanation on what grounds this lump sum valuation is based. It is debatable whether such a lump sum valuation could be upheld in court proceedings.

The provisions of the circular applicable to non-freely transferable options and other employee participation plans are not affected by the amended circular. The grant of non-transferable stock options is not considered as a taxable event by the Luxembourg tax authorities. However, where the strike price of the option is lower than the fair market value of the shares, the employee will in principle be subject to taxation and social security contributions at the moment of exercise. Indeed, the difference between the fair market value and the strike price is considered as an advantage in kind (*avantage en nature*) derived from a salaried occupation (*revenu d'une occupation salariée*) and taxed in the same way as an ordinary salary. Where the shares acquired remain unalienable following exercise, an abatement corresponding to 5% of the fair market value of the shares acquired is available for each year that the shares remain locked up. The maximum abatement, however, is capped at 20%. The Circular allows only the serious sickness, disability or death of the employee as permitted early exit scenarios without abatement recapture. Capital gains realised on a disposal of the shares and dividends derived from the shares are not considered as salary and taxed in accordance with ordinary tax provisions. Hence, capital gains are in principle tax exempt, provided the sale occurs more than 6 months after acquisition of the shares.

5. LOSSES CARRIED FORWARD IN CASE OF HEREDITARY TRANSMISSION OF A BUSINESS OR AN ESTABLISHMENT

On 22 November 2012, the Luxembourg tax authorities issued Circular L.I.R. 114/3 to clarify the position that they will adopt regarding the use of tax losses in case of hereditary transmission of a business or an establishment.

Pursuant to Article 114 sub-paragraph 2 n° 3 of the Luxembourg income tax law ("**LITL**"), in the case of transmission of a business or an establishment by way of succession, the entrepreneur's successor is only allowed to use the tax losses realised by that business or establishment insofar as the successor was taxed collectively with the *de cujus* entrepreneur at the time of the realisation of the tax losses.

The Luxembourg tax authorities have declared that, in view of the position taken by the European Court of Justice, they will, until legislative changes to this provision, no longer apply the condition for the successor and the *de cujus* entrepreneur to be taxed collectively and accept the use of the tax losses carried forward by the successor. The tax authorities also confirm that this condition may be viewed as a discriminatory provision if the successor was not a Luxembourg tax resident at the time of the realisation of the tax losses which as such could not be taxed collectively with the *de cujus* entrepreneur.

6. QUALIFICATION OF A SHAREHOLDER'S DEBT WAIVER

On 7 February 2013, the Luxembourg Administrative Court rendered its decision on the tax qualification of a partial shareholder debt waiver including a clause of "better fortune" and overruled the decision of the Administrative Tribunal which concluded in its decision of 12 July 2012 that a shareholder debt waiver is a taxable event.

The Administrative Court considered, by referring to the parliamentary documents relating to Article 42 of the LITL, that a shareholder debt waiver may qualify as a hidden capital contribution as the receivables and debts stemming from the operation are part of the invested assets by destination and are thus, in accordance with Article 18 LITL, to be deducted from the taxable result of the company.

The Administrative Court furthermore analysed the clause of "better fortune" included in the debt waiver as the tax authorities were maintaining that the waiver was not final and could thus not, as a result, be considered as a non-taxable contribution.

The Court referred to the case-law of the German Supreme Court of 23 May 1984[7] which considered a debt waiver as an additional contribution and the clause of "better fortune" as a drawdown of the assets (at the time of its exercise). According to the German Supreme Court, these are two different transactions each with their own tax consequences.

The Court concluded that in principle a partial shareholder debt waiver is to be considered as a non-taxable hidden contribution and shall thus be deducted in accordance with Article 18 of the LITL from the taxable results within the limits of its valuation.

[7] Bundesfinanzhof (BFH 23.5.1984 BSt Bl II, 723ff)

LITIGATION

1. IMPACT OF THE ENTRY IN FORCE OF REGULATION (EU) 1215/2012 (BRUSSELS I BIS)

On 12 December 2012, the European Parliament and the Council adopted Regulation (EC) 1215/2012 which replaces Regulation (EC) 44/2001 on jurisdiction and recognition and enforcement of judgments in civil and commercial matters (Brussels I Regulation).

The principal objective of this Regulation is to facilitate the free circulation of judgments and to further enhance access to justice.

The most important changes are:

1. Abolition of the exequatur procedure

The exequatur is the procedure for the declaration of enforceability of a judgment given in another Member State. With this Regulation, a judgment given in a Member State which is enforceable in that Member State shall be enforceable in the other Member States without a declaration of enforceability being required, upon production of a copy of the judgment which satisfies the conditions necessary to establish its authenticity and a certificate to be issued by the court of origin (Article 37). However, this Regulation provides several grounds (Article 45 and Article 46) for refusal to recognise and/or enforcement of judgments on the application of any interest party. Such is the case for example when the decision was given in default of appearance and the defendant was not served with the document which instituted the proceedings or with an equivalent document in sufficient time and in such a way as to enable him to arrange for his defence, unless the defendant failed to commence proceedings to challenge the judgment when it was possible for him to do so.

2. Jurisdiction over consumer contracts and individual contracts of employment

National rules of jurisdiction may no longer be applied by Member States in relation to consumers and employees domiciled outside the EU (Article 18 and Article 21). Such uniform rules of jurisdiction will also apply in relation to parties domiciled outside the EU in situations where the courts of a Member State have exclusive jurisdiction under the Regulation or where such courts have had jurisdiction conferred on them by an agreement between the parties.

3. Lis Pendens

Introduction of a rule of international *lis pendens* which will allow the courts of a Member State to stay the proceedings and eventually dismiss the proceedings in a situation where a court of a third state has already been seised either of proceedings between the same parties involving the same object and the same cause (Article 33) or of a related action (Article 34) at the time the court of a Member State is seised.

4. Choice of jurisdiction

The courts of a Member State must stay legal proceedings until a court of another Member State to which an agreement confers exclusive jurisdiction declares that it has no jurisdiction under the agreement. Where the court designated in the agreement has established jurisdiction in accordance with the agreement, any court of another Member State must decline jurisdiction in favour of that court (Article 31).

5. Confirmation of the arbitration exception

This Regulation does not apply to arbitration. As indicated in the Preamble, when seised of an action in a matter in respect of which the parties have entered into an arbitration agreement, the courts of a Member State should refer the parties to arbitration, stay or dismiss the proceedings, or examine whether the arbitration agreement is null and void, inoperative or incapable of being performed in accordance with their national law.

This Regulation shall only apply to legal proceedings instituted on or after 10 January 2015 (Article 66).

In accordance with Article 3(2) of the Agreement of 19 October 2005 between the European Community and the Kingdom of Denmark on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters, Denmark has by letter of 20 December 2012 notified the Commission of its decision to implement the contents of Regulation (EU) 1215/2012. This means that the provisions of Regulation (EU) 1215/2012 will be applied to relations between the Union and Denmark.

2. OVER-INDEBTEDNESS LAW (*SURENDETTEMENT*)

The Law of 8 January 2013 on over-indebtedness introducing a civil brankruptcy regime for private persons was published in the *Mémorial A* on 13 February 2013. This law replaces the previous Law of 8 December 2000 on over-indebtedness and amends amongst others Article 2016 of the Luxembourg Civil Code with respect to the validity of a guarantee (*cautionnement*) granted by a physical person.

It shall enter into force in January 2014.

This document can be viewed under:
http://www.legilux.public.lu/leg/a/archives/2013/0026/a026.pdf

3. LAW ON COMBATING LATE PAYMENT IN COMMERCIAL TRANSACTIONS

On 20 March 2013, the Luxembourg law on combating late payment in commercial transactions was adopted by the Luxembourg Parliament. This law implements the Directive 2011/7/EU of 16 February 2011 on combating late payment in commercial transactions and amends the law dated 18 April 2004 on payment terms and late payment interest.

The new law has not yet been published in the official journal (i.e. the *Mémorial*) but the final report which refers to the law can be viewed under:
http://www.ehp.lu/fileadmin/user_upload/legal_topics/other_areas/PL_6437_Lutte_contre_le_retard_de_paiement_Rapport.pdf