Newsletter

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BONN STEICHEN & PARTNERS

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SUMMARY

AML

FOURTH AML DIRECTIVE

The European Parliament vote on the final text of the fourth AML Directive ("the Fourth AMLD") is imminent.

The draft Fourth AMLD is based on the revised FATF recommendations (February 2012), but goes beyond. The current European legislation, known as the 'Third Anti-Money Laundering Directive', has been in force since 2005 and applies to banks and the entire financial sector as well as, among others, to lawyers, notaries, accountants, real estate agents, company service providers and all dealers in goods, when payments are made in cash in excess of EUR 15,000 ("the Obliged Professionals").

The following key changes are foreseeable:

- Inclusion of tax crimes is to become mandatory in the scope of national AML legislation. However, this will not entail any change in Luxembourg, as tax crimes are not likely to be defined as predicate offences: the aggravated tax fraud (*l'escroquerie fiscale*) is not specifically listed in article 506-1 of the Criminal code and the minimum sanction (imprisonment of at least one month) does not meet the criteria provided for by the same article 506-1);
- A greater emphasis is placed on a risk-based approach to better target money laundering. In Luxembourg, as far as the financial sector is concerned, a number of the related rules have already been anticipated by the CSSF regulation No. 12-02;
- The threshold for a single value cash transaction is to be reduced from EUR 15,000 to EUR 10,000, for high value goods dealers or service providers;
- Due diligence provisions regarding politically exposed persons ("PEPs") are to be extended to cover domestic PEPs (e.g. MPs, judges) who will be treated in the same way as foreign PEPs, meaning that they will be considered high risk from a due diligence perspective and additional measures will have to be followed to establish the source of their wealth and funds;
- Beneficial owners of companies are to be listed in centralised and interconnected registers in the European Union, accessible to the competent authorities, Obliged Professionals and also any person who can demonstrate a "legitimate interest" in suspected money laundering (it is not yet clear who such persons might be).

The initial draft of the Fourth AMLD (as proposed by the European Commission) required the Member States to ensure that corporate and other legal entities obtain and hold adequate, accurate and current information on their beneficial ownership and that this information is provided to Obliged Professionals when the latter are taking customer due diligence measures and is made available to competent authorities (regulators) and Financial Intelligence Units.

The European Parliament advocated for the registers of beneficial owners to become publicly available. With a view to enhancing transparency, beneficial ownership information should be recorded in specified locations (e.g. in the case of companies in a public central company registry). Currently professionals lack ways and means to verify the beneficial owners, which represents a disproportionate burden and liability for Obliged Professionals. Therefore the data gathered by businesses in Member States should be improved to include beneficial ownership information that would help both authorities and professionals to verify if criminals try to conceal their crimes behind companies.

Given the cross-border scope of business and the interconnectivity of the internal market, those registers should also be interconnected and accessible by the authorities and the Obliged Professionals throughout Europe. For the sake of data protection, Member States may grant access to the information to other parties and establish rules based on which the register can be accessed.

Last Autumn, negotiations were held between the European Council, the European Commission and the European Parliament. The deal concluded on December 2014 was endorsed by both the Economic and Monetary Affairs and Civil Liberties committees of the European Parliament in Brussels in January 2015.

The agreed compromise text states that the ultimate owners of companies will have to be listed in central registers in the European Union, accessible to the competent authorities and their Financial Intelligence Units (without any restriction), to Obliged Professionals, and also to any persons or organisations that can demonstrate a “legitimate interest”, such as investigative journalists. The aim is welcome, but these new rules will be very challenging for the fund industry in Luxembourg.

The final full European Parliament vote is likely to be held in April 2015 and is now anticipated to be a mere formality. The European Union Member States will have up to two years from the date of adoption to implement the Fourth AMLD into their national legislation. The most up-to-date draft of the text is available here: http://data.consilium.europa.eu/doc/document/ST-5116-2015-ADD-2/en/pdf

NEW FORM SUSPICIOUS TRANSACTION REPORT

On March 16th 2015, the Financial Intelligence Unit (“FIU”) of Luxembourg issued a new form to file suspicious transaction reports (“STR”). The Anti-money laundering Law of November 12th 2004 includes the obligation, for the subjected professionals, to inform without delay, on their own initiative, the FIU when they know, suspect or have reasonable grounds to suspect that money laundering or terrorist financing is being committed or has been committed or attempted, in particular in consideration of the person concerned, its development, the origin of the funds, the purpose, nature and procedure of the operation. This report must be accompanied by all supporting information and documents having prompted the report.

A writable PDF is made available in lieu of the template provided by the FIU when it issued circular 22-10. The content is essentially the same as for the initial document.

From now on, the STR itself has two new appendices, one dedicated to Legal Persons (LP) and another to Natural Persons (NP), to inform about the particulars of the persons subject to the suspicion or simply involved in the relationship with the professional who has a suspicion to report. One has to fill in (only in French) as many appendices as there are number of related persons.

This new set of forms is explained in a user’s guide provided by the FIU, available here: http://www.justice.public.lu/fr/formulaires/blanchiment-terrorisme/guide-utilisateur_declarations.pdf

CAPITAL MARKETS

MARKET ABUSE REGULATION – ESMA REPORT

On February 2nd 2015, the European Securities and Markets Authority ("ESMA") published its final report on possible delegated acts concerning the Market Abuse Regulation ("MAR"), following its publication of the Consultation Paper on July 15th 2014.

The content of the final report deals with the formal requests from the European Commission to provide technical advice on the delegated acts. In particular, the final report:

- specifies the indicators of market manipulation, and provides examples of practices that may constitute market manipulation;
- recommends to set the minimum thresholds exempting certain market participants in the emissions allowance market from the requirement to publicly disclose inside information;
- advises on the determination of the competent authority for the notifications of delays in the public disclosure of inside information;
- provides clarifications on the types of transaction which trigger the duty on persons discharging managerial responsibilities and persons closely associated with them, to notify the issuer and the competent authority of such transactions ; and
- proposes the procedures and arrangements for the reporting of infringements under the MAR regime.

In some cases, the final report also incorporated the suggestions provided by the market participants' responses. A summary of these responses and ESMA's own comments on questions included in the Consultation Paper are also contained in the report.

The delegated acts are expected to be adopted by the European Commission and enter into force by July 2016, 24 months after the publication of MAR, taking into account the right of the European Parliament and Council of the EU to object and propose revisions to a delegated act.

The final report is available at http://www.esma.europa.eu/system/files/2015-224.pdf

MAKING STRIDES TOWARDS A CAPITAL MARKETS UNION

OVERVIEW

On February 18th 2015, the European Commission set the wheels in motion for a fully functioning Capital Markets Union, through the launch of its green paper *Building a Capital Markets Union* (the "Green Paper").

The goal is to build a true single market for capital for all 28 Member States by 2019.

In the Green Paper the European Commission identifies five priorities for early action:

(i) lowering barriers to accessing capital markets ;
(ii) widening the investor base for SMEs ;
(iii) building sustainable securitisation ;
(iv) boosting long term investment ; and
(v) developing European private placement markets.

PROSPECTUS REGIME – CONSULTATION PAPER

With respect to (i) above (lowering barriers to accessing capital markets), the European

Commission has launched a parallel public consultation focusing specifically on the review of the current prospectus regime, *Consultation Document – Review of the Prospectus Regime* (the "PD Consultation Document"). The PD Consultation Document highlights several potential shortcoming of the current prospectus regime and identifies three fundamental aspects which need to be reviewed, specifically:

a) when a prospectus is need;
b) what information a prospectus should contain;
c) how prospectuses are approved.

SECURITISATION – CONSULTATION PAPER

With respect to item (iii) above (building sustainable securitisation), the European Commission has launched a second parallel public consultation to meet this objective, *Consultation Document – An EU Framework for simple, transparent and standardised securitisation* (the "Securitisation Consultation Document"). In the view of the European Commission, the development of a high quality securitisation market, which would rely on simple, transparent and standardised securitisation instruments, is an important step towards achieving a Capital Markets Union; a sustainable high quality securitisation market will promote further integration of the EU capital markets, support the diversification of funding sources, thereby freeing up capital and facilitate bank lending to those who need it.

The Securitisation Consultation Document asks a number of questions about the identification criteria for qualifying securitisation. It goes on to consider the prudential treatment of securitisations – including bank capital requirements – and the regulatory frameworks applicable to other institutional investors. Questions are also raised in relation to promoting SME securitisation. Apart from the above mentioned questions, the Securitisation Consultation Document includes also facts on securitisation markets in the US and in Europe. The Securitisation Consultation Document provides an overview of the framework for EU securitisation already in place. Relevant legislation includes, for example, the Capital Requirements Regulation for banks, the Solvency II Directive for insurers and AIFMD Directive for asset managers. Other legal provisions, notably on information disclosure and transparency, are laid down in the Credit Rating Agency Regulation (CRAIII) and the Prospectus Directive.

To sum up, the Securitisation Consultation Document seeks views from the stakeholders on how best to implement a high quality securitisation definition in EU legislation, and what requirements should apply to it – in terms of capital and solvency requirements, due diligence and transparency obligations.

The Green Paper is available at:
http://ec.europa.eu/finance/consultations/2015/capital-markets-union/index_en.htm.

The PD Consultation Document is available at:
http://ec.europa.eu/finance/consultations/2015/prospectus-directive/index_en.htm.

The Securitisation Consultation Document is available at:
http://ec.europa.eu/finance/consultations/2015/securitisation/index_en.htm.

INVESTMENT FUNDS

EUSEF AND EUVECA - UPDATE

On February 3rd 2015, the European Securities Markets Authority ("ESMA") issued its final report (the "Final Report") on ESMA's technical advice to the European Commission on the implementing measures of the Regulations on European Social Entrepreneurship Funds ("EUSEF") and European Venture Capital Funds ("EUVECA").

For information on the background please see our newsletter of February 2015.

The Final Report sets out ESMA's advice to the European Commission on the implementing measures concerning:

(i) the specification of the definition of qualifying portfolio undertaking for a EUSEF;
(ii) conflicts of interest for both EUSEF and EUVECA managers;
(iii) social impact measurement; and
(iv) information to EUSEF investors.

With regard to item No. (i) ESMA's advice is that the primary purpose of the enterprise into which the EUSEF wishes to invest shall be to address a social problem. The social mission of the enterprise should be the basis of its activities. The enterprise shall use its profits primarily to achieve its social objective. Ordinary companies having a positive social or environmental impact, including a corporate social responsibility plan that is incidental to their commercial activities shall not be accepted as a qualifying portfolio undertaking. The goods and services produced shall be addressed primarily to persons that are in a situation of exclusion, disadvantage or marginalisation or that are vulnerable. Where the goods and services are not so addressed this is still acceptable insofar as the primary purpose of the enterprise is to produce a positive social impact by other means.

With regard to item No. (ii) ESMA's advice is that both EUSEF and EUVECA managers shall establish a conflicts of interest policy in writing. The policy shall identify the circumstances that may give rise to a conflict of interest and shall include procedures and measures in order to prevent, manage and monitor such conflicts on an ongoing basis. ESMA provides examples of such measures including separating the supervision of relevant persons whose interest may conflict and removing links in the remuneration of relevant persons engaged in different activities where a conflict may arise. If there are conflicts of interest that cannot be avoided and the relevant manager chooses to carry on business regardless then the manager shall disclose these conflicts promptly to investors prior to undertaking the business on their behalf.

In the case of EUVECA managers they shall develop adequate and effective strategies for determining when and how any voting rights held in the EUVECA portfolio are to be exercised, to the exclusive benefit of the EUVECA concerned and its investors. These strategies should determine measures and procedures for monitoring relevant corporate actions, ensuring that the exercise of voting rights is in accordance with the investment objective and policy of the EUVECA and preventing or managing any conflicts of interest arising from the exercise of voting rights.

With regard to item No. (iii) ESMA advises that the EUSEF manager shall employ procedures to measure the extent to which the qualifying portfolio undertakings achieve the social impact to which they are committed. The measurement shall be performed by the EUSEF manager itself or by third parties. Investors shall be informed prior

to their investment decision about the methodologies that the EUSEF manager uses to measure social impacts. ESMA sets out steps which the chosen measurement methodology must follow.

Finally ESMA's advice on the information that the EUSEF manager shall provide to the investors sets out the information to be included on the investment strategy and objectives. Information on the positive social impact targeted and the projections of such outcomes as well as on the methodologies for measuring the social impact shall be presented in a clear and understandable manner.

The next step is for the European Commission to develop the delegated acts on the basis of ESMA's advice. ESMA will provide input as necessary on the development of such acts.

The text of the Final Report can be found at: http://www.esma.europa.eu/system/files/2015-esma-227_-_final_report_on_advice_on_eusef-euveca.pdf

CROWDFUNDING - EBA OPINION

Following on from the advice and the opinion of the European Securities and Markets Authority ("ESMA") on investment-based crowdfunding in December 2014, the European Banking Authority (the "EBA") issued its opinion on lending based crowdfunding in February 2015 (the "Opinion").

The EBA has identified crowdfunding – in particular lending based crowd funding - as a new form of financial activity that falls within its area of competence. The EBA has focused on the assessment of risks arising for market participants as well as the drivers of these risks and the extent to which these could be addressed in existing EU or national legislation.

The Opinion is addressed to the EU Commission, Council and Parliament with a view to achieving a coordinated approach to the regulatory and supervisory treatment of crowdfunding.

Following an analysis of lending based crowdfunding including the various business models, the risks to borrowers and lenders, regulatory measures to address the risks and the applicability of EU legislation the EBA came to the following conclusions:

- That the convergence of practices across the EU for the supervision of crowdfunding is desirable in order to avoid regulatory arbitrage, create a level-playing field, ensure that market participants can have confidence in this market innovation and contribute to the single European market.
- The EBA considers that at this stage, this convergence should be based on existing EU law and recommends that EU legislators provide clarity on the applicability of said law to lending-based crowdfunding.
- Should the legislators consider developing a possible regulatory framework the EBA proposes several regulatory measures which should be taken, in particular in relation to:
    - the lack of or insufficient information regarding lenders' and borrowers' rights, duties and risks;
    - a lack of or insufficient requirements on any due diligence process and assessment of borrowers' creditworthiness conducted by a platform;
    - a lack of or insufficient requirements on platforms complaints handling procedures;
    - a lack of or insufficient internal platform procedures (relating to document handling processes and records setting);
    - a lack of or insufficient safeguards against platform default; and

- a lack of or insufficient project safeguard clauses.

- The Payment Services Directive is the directive that is most feasibly applicable to lending-based crowdfunding activities. However lending related aspects are not covered by EU law leaving several risks unaddressed. The EBA also considers that there is a need for the EU legislators to provide clarification of certain matters in the Payment Services Directive including the scope of the distinction between "regular" and "main" activity, the application of the exemptions listed in the directive and the definition of payment services.
- The business models of lending based crowdfunding platforms do not fall inside the perimeter of credit institutions and their typical business model.

The EBA will continue to monitor the market and will revise its conclusions as and when required.

The text of the Opinion is available at: https://www.eba.europa.eu/documents/10180/983359/EBA-Op-2015-03+%28EBA+Opinion+on+lending+based+Crowdfunding%29.pdf

MMF REGULATION- ECON REPORT

On February 26th 2015, the Economic and Monetary Affairs Committee of the European Parliament ("ECON") voted on the draft report on the proposed draft regulation on Money Market Funds (the "MMF Regulation"). The text adopted by ECON on March 4th 2015 (the "Report"), will be voted by the European Parliament on April 28th 2015. Thereafter it will be negotiated with the Council of the European Union.

Taking into account that money market funds ("MMF") are an important source of short term funding for banks, corporates and governments, the aim of the changes introduced by ECON on the MMF Regulation has been to balance the rules addressed to protect investors with the viability of MMFs.

Both the European Commission and ECON were concerned about the feasibility to deliver a constant net asset value in today's low interest rate environment. While the European Commission solution to mitigate said risk was to maintain a constant NAV buffer of at least 3% of the total value of the CNAV MMF's assets, ECON believed that it would be a better solution to create a new category of MMF, the "Public Debt CNAV MMF".

The draft MMF Regulation now divides the CNAV MMFs into 3 categories:

- **Public Debt CNAV MMF** which shall invest 99.5% of its assets in public debt instruments and, by 2020, at least 80% of its assets in EU public debt instruments;
- **Retail CNAV MMF**, available for subscription only to charities, non-profit organisations, public authorities and public foundations; and
- **Low Volatility Net Asset Value MMF (LVNAV MMF)**, which may display a constant NAV if the following rules for the valuation of its assets are met:
  - use of the amortised cost method for the valuation of the assets with a residual maturity below 90 days and all assets with a residual maturity exceeding 90 days shall be priced using mark-to-market or mark-to-model prices;
  - rounding to two decimal places the valuation of its assets provided that the constant NAV per unit or share does not deviate from its actual NAV by more than 20 basis points and to four decimal places thereafter;

- redemptions or subscriptions at the constant NAV per unit or share provided that the constant NAV per unit or share does not deviate from its actual NAV by more than 20 basis points;
- redemptions or subscriptions at the actual NAV per unit or share which shall be rounded to four decimal places, or less where the constant NAV deviates from the actual NAV by more than 20 basis points;
- potential investors are warned in writing prior to the conclusion of the contract of the circumstances in which the fund will no longer redeem or subscribe at a constant NAV;
- the difference between the constant NAV per unit or share and the actual NAV per unit or share is continuously monitored and published daily on the website of the MMF.

The draft MMF Regulation prohibits external support for all MMFs and sets out transparency requirements such as daily disclosures, quarterly stress tests, etc.

The draft MMF Regulation also obliges MMFs to diversify their portfolio assets and provides for redemption gates and liquidity and concentration requirements. MMFs will have to invest in higher quality assets and assess internally the credit quality of money market instruments.

The Report consolidates the previous position of ECON and is available at: https://polcms.secure.europarl.europa.eu//cmsdata/upload/da4a2fd7-610f-433c-86a2-59a6c7caa3d8/A8-0041_2015_EN.pdf.

EMIR – MoUs IN RELATION TO NON-EU CCPS

Regulation (EU) No 648/2012 of the European Parliament and of the Council of July 4th 2012 on OTC derivatives, central counterparties and trade repositories ("EMIR") provides for cooperation arrangements to be established between the European Securities and Markets Authority ("ESMA") and non-EU authorities whose legal and supervisory framework for CCPs have been deemed equivalent to EMIR by the European Commission under the form of Memorandum of Understanding ("MoU").

The European Commission started its equivalence assessment in relation to such non-EU CCPs last October 30th 2014, where it has adopted four "equivalence" decisions (implementing acts) for the regulatory regimes for central counterparties ("CCPs") in Australia, Hong Kong, Japan and Singapore.

Further to the above equivalence assessments ESMA entered into a first MoU, established under Article 76 of EMIR, with the Australian Securities & Investments Commission ("ASIC") last November 2014.

On March 5th 2015, ESMA signed a second MoU of this kind with the Reserve Bank of Australia ("RBA") effective as of February 18th 2015 to allow the RBA to have access to data held in European trade repositories according to its mandate. The aim of this type of MoU is to ensure that third-country authorities that do not have any trade repository in their jurisdiction and who have established cooperation arrangements with ESMA, such as Australia, may access the information on derivatives contracts held in European trade repositories which is relevant for their mandates in a manner consistent with and permitted by article 76 of EMIR and other applicable laws and regulations.

On March 9th 2015, ESMA signed another type of MoU with the Monetary Authority of Singapore ("MAS") effective as of March 10th to ensure that (i) cooperation arrangements are established between the signatory authorities regarding CCPs in Singapore who are authorised by the MAS and have applied for recognition under EMIR and (ii) to provide ESMA with adequate tools to monitor the ongoing compliance of the CCPs with the recognition conditions.

The establishment of cooperation arrangements are a precondition for ESMA to recognise CCPs established in Singapore thus allowing them to provide services to clearing members or trading venues established in Europe.

The MoUs are available at:
www.esma.europa.eu/system/files/mou_signed_rba_-_esma.pdf and
www.esma.europa.eu/system/files/signed_mou_for_singapore_ccps_with_mas_20150210.pdf

ADOPTION OF ELTIF REGULATION

The proposed regulation (the "Regulation") on European Long-Term Investment Funds ("ELTIF") has been adopted by the European Parliament (the "EP") on March 10th 2015.

As further described in our our April-June 2014 Newsletter, the aim of the Regulation is to encourage professional/institutional and retail investors to invest in long-term infrastructure projects.

Several points of the Regulation have been amended since submission of the first draft to the EP on April 17th 2014 (the "Initial Draft").

The main amendment relates to the possibility for retail investors to ask for the redemption of their shares/units before the end of the life of the ELTIF. While the Initial Draft as amended by the EP was more open to this possibility, the Regulation now, in principle, prohibits early redemptions even for retail investors. The reason for this is that long term infrastructure projects require regular and stable financing which cannot be guaranteed in the presence of early redemption rights.

However, derogating from the general rule, ELTIFs may (but are not required to) offer the possibility for early redemptions if they comply with some additional requirements of the Regulation, such as establishing a liquidity management policy and limiting the amount of redemptions in a given period.

The units or shares of an ELTIF may be admitted to trading on a regulated market or a multilateral trading facility thus offering investors an alternative means of liquidity in the absence of redemption rights.

Only an authorised AIFM pursuant to Directive 2011/61/EU may manage an ELTIF.

The Regulation is to be considered as being in its final form.

The text of the Regulation can be found under: http://data.consilium.europa.eu/doc/document/PE-97-2014-INIT/en/pdf

The Regulation will now be submitted to the Council of the European Union for formal approval.

It shall thereafter be published in the *Official Journal of the European Union* and enter into force twenty days after such publication which is expected to occur on or around the end of 2015.

UCITS V - CSSF CIRCULAR 15/608

On March 23^{rd} 2015, the CSSF published Circular 15/608 (the "Circular"), which amends the date of entry into force of CSSF Circular 14/587 ("Circular 14/587") on the provisions applicable to credit institutions acting as custodian banks of Luxembourg undertakings for collective investment in transferable securities ("UCITS").

As further described in our newsletter dated September 2014, the aim of Circular 14/587 is to align the requirements applicable to UCITS custodian banks with the future requirements of Directive 2014/91/EU of July 23^{rd} 2014 on UCITS as regards depositary functions, remuneration policies and sanctions ("UCITS V Directive").

The initial deadline applicable to UCITS custodian banks in order to comply with Circular 14/587 was December 31^{st} 2015.

Considering the fact that the implementation of the UCITS V Directive in Luxembourg must occur by March 18^{th} 2016 and considering that the various delegated acts concerning the UCITS V Directive will only be published during the second and third trimester of 2015, the CSSF has adopted the Circular in order to align the deadlines, so that the entry into force of Circular 14/587 has been postponed to **March 18^{th} 2016**.

AIFMD

AIFMD REPORTING – CSSF FEEDBACK

Last January 31^{st} 2015 was the first reporting deadline for most Luxembourg market participants to file their alternative investment fund managers ("AIFMs") and alternative investment funds ("AIFs") reports under AIFMD.

When submitting their report, each participant concerned by the reporting (i.e. registered and authorised AIFMs and related AIFS) should receive an "OK no errors" response from the *Commission de Surveillance du Secteur Financier* ("CSSF") which confirms that after an automatic screening of the filing same has been successfully transmitted to the authorities before final analysis of the content.

In case the screening performed results in the presence of a field apparently not properly filled in the CSSF issues an error report which obliges the participant to resubmit an amended file.

Notwithstanding the presence of an error in the report the first filing is the one considered by the authorities for the purposes of assessing the date of submission of the file.

In connection with the above procedure, the CSSF made available last February, a document comprising all the different error messages that could be received by participants in connection with the submission of their AIFMD reporting.

The document describes the different return files and respective error codes and error messages. It describes the errors and the way to correct them.

The CSSF document is available at:
http://www.cssf.lu/fileadmin/files/AIFM/CSSF_ERROR_CODES_FEEDBACK_FILES_V_3_0.pdf

AIFMD – UPDATED ESMA Q&A

On March 26^{th} 2015, the European Securities and Markets Authority ("ESMA") published an updated questions and answers ("Updated Q&A") on the application of the Alternative Investment Fund Managers Directive ("AIFMD"). The update of the Q&A relates to reporting, notification,

leverage, additional own funds and scope of the directive.

Regarding the reporting aspect, the Updated Q&A clarifies that Alternative Investment Fund Managers (“AIFMs”) should take into account all the EU Alternative Investment Funds (“AIFs”) they manage and AIFs they market in the European Union to calculate the reporting frequency. The AIFM should therefore calculate a unique reporting frequency taking into account all the AIFs it markets in the Union and apply the same reporting frequency to all Member States where it markets its AIFs.

The Updated Q&A also provides clarification on reporting the total long and short value of exposures before currency hedging and reporting the results of stress tests.

The Updated Q&A explains that an AIFM that is already managing AIFs in a host Member State under Article 33 of the AIFMD and that wishes to manage a new AIF in that host Member State should not undertake a new notification under Article 33(2). The original notification should be considered valid for all the AIFs it intends to manage in that given Member State but an update should be sent to identify each new AIF to be managed and to clarify if the proposed new AIFs are of a different type from the ones specified in the original notification.

On the issue of the calculation of leverage the Updated Q&A clarifies that when calculating the exposure of an AIF in accordance with the gross method under Article 7(a) of Regulation 231/2013, the value of all cash and cash equivalents held in the base currency of the AIF should be excluded.

On the issue of additional own funds, the Updated Q&A indicates that AIFMs should exclude investments by AIFs in other AIFs they manage for the calculation of additional own funds. However, they should include investments by AIFs in other AIFs they manage for the calculation of additional own funds to cover potential liability risks arising from professional negligence under Article 9(7) of the AIFMD since this type of investment is viewed as increasing their operational risk.

Finally the updated Q&A clarifies that a Member State may allow authorised EU AIFMs to market to professional investors, in their territory only, units or shares of EU feeder AIFs which have a non-EU master AIF managed by a non-EU AIFM provided that the EU AIFM managing the EU feeder AIF fulfils certain conditions as set out in Article 36(1) (a) to (c).

It indicates that whether the non-EU AIFM managing the non-EU master AIFs has to be authorised or not under the AIFMD depends on the national law of the Member State transposing Article 36 of the AIFMD since Member States may impose stricter rules on the AIFM in respect of the application of Article 36 of the AIFMD.

The updated Q&A is available at: www.esma.europa.eu/system/files/2015-630_qa_aifmd_march_update.pdf

TAX

EUROPEAN COMMISSION PRESENTS A PROPOSAL FOR AUTOMATIC EXCHANGE OF TAX RULINGS

On March 18th 2015, the European Commission published a new initiative on tax transparency to fight tax evasion and avoidance. The initiative includes a proposal to extend the scope of the Directive on Administrative Co-operation in the field of direct taxation (2011/16/EU), amended by Council Directive 2014/107/EU (the “Directive”) by introducing an automatic exchange of information between Member States on their advance cross-border tax rulings (“Ruling”) and advance pricing arrangements (“APA”).

The Commission’s proposal (the “Proposal”) would require each Member State to communicate every 3 months the Rulings or APAs issued or amended after the date of entry into force of the Proposal. For Rulings and APAs that have been issued within the last ten years but are still valid on the date of entry into force of the Proposal, the information shall be exchanged before December 31st 2016.

Provided that unanimity is reached in the Council and the Proposal enters into force by the end of 2015, the amended Directive would be applicable as from January 1st 2016 and cover all Rulings and APAs that have been issued as from and including 2005.

Member States shall adopt by December 31st 2015 the legislation necessary to comply with the Proposal.

The exchange of information shall be carried out using a standard form that has to be adopted by the EU Commission. Also, the EU Commission will develop a database where information may be recorded and centralised for other Member States to detect certain abusive tax practices by companies and take the necessary action in response. If, after this initial exchange, a Member State believes that it needs more information on a particular Ruling or APA, it can request more details or the full text of the document.

Rulings and APAs that cover purely domestic transactions or cross-border rulings that exclusively concern and involve the tax affairs of natural persons are outside the scope of the current proposal and therefore not subject to exchange of information.

The Tax Transparency Package is the first step in a broad Commission agenda against corporate tax avoidance. The next step will be an Action Plan on corporate taxation, which is expected for summer 2015. It will include the launch of a debate on the Common Consolidated Corporate Tax Base (“CCCTB”) and ideas for integrating new OECD/G20 base erosion and profit shifting (“BEPS”) actions at EU level. A third step is a proposal to repeal the EU Savings Directive, since the recently revised Directive covers the same types of income and overlaps in its scope. Again, the goal of the Commission is to increase effectiveness of reporting mechanisms and to avoid parallel provisions that follow similar targets.

CERTIFICATES OF RESIDENCE FOR FUNDS

The Circular L.G. – A. n°61 issued on February 12th 2015 (hereafter the “Circular”) by the Luxembourg tax authorities (hereafter the “LTA”) aims at clarifying their position with regards to the issuance of certificates of residence for undertakings for collective investments (hereafter **“**UCIs**”**) as well as the specific procedure to be followed depending on the type of UCIs and the relevant country requesting the certificate of residence.

A certificate issued by the LTA only reflects the position of the LTA with regards to the residence and qualification of a UCI under a specific double tax treaty. This unilateral position may not be shared by the other treaty country.

In the Circular, the LTA sets out three different types of certificates of residence (an example of each is provided in the appendices to the Circular) that it issues depending on certain criteria detailed below.

The first type of certificate of residence (hereafter the **"Type 1 Certificate"**) is issued in cases where:

- the Luxembourg UCI is an incorporated UCI (i.e. either a UCITS or a SIF incorporated as a SICAV or a SICAF in accordance with the law of December 17th 2010 or the law of February 13th 2007 respectively);
- a double tax treaty between Luxembourg and the other country is in force; and
- the double tax treaty applies to UCIs.

The determination whether the double tax treaty applies to UCIs can be based either:

- on an express consent by the other country;
- on a clear provision in the respective double tax treaty (as understood by the LTA); or
- on the LTA's interpretation of the double tax treaty in the absence of a specific provision.

The second type of certificate of residence (hereafter the **"Type 2 Certificate"**) is issued for unincorporated UCIs, i.e. FCPs, in cases where:

- the relevant double tax treaty includes a specific provision that assimilates FCPs to an individual for the purpose of the double tax treaty; or
- the relevant double tax treaty includes a provision that includes all UCIs irrespective of their form (whether incorporated or unincorporated) in the definition of resident.

In order for the LTA to issue a Type 1 Certificate or a Type 2 Certificate, a request has to be filed with the tax office "Sociétés 6" together with a certificate from the CSSF that the UCI is subject to regulatory supervision.

The third type of certificate of residence (hereafter the **"Type 3 Certificate"**), that is solely based on domestic legislation, can be issued in cases where:

- the UCI is an incorporated UCI and is tax resident for Luxembourg tax purposes, by virtue of having either its statutory seat or its central administration located in Luxembourg; and
- either (i) no double tax treaty is in place with the country concerned or (ii) the certificate is required for non-double tax treaty purposes, such as withholding tax reclaims on the basis of the European fundamental freedoms, as evidenced by the ECJ's constant case-law such as the Aberdeen case (C-303/07 dated June 18th 2009) or the Santander case (C-338/11 dated May 10th 2012).

In order for the LTA to issue a Type 3 Certificate, a request has to be filed with the tax office "Sociétés 6" together with a regulatory supervision certificate from the CSSF. However, in addition to the above, a detailed explanation of the reason for which the certificate is required will also have to be provided, together with a reference to the foreign legal provision or to the double tax treaty that requires said certificate. A detailed listing of the income received by the UCI and for which the request is made will also have to be appended to the request.

In case the certificate is requested *ex-ante*, indications on the investment policy of the UCI have to be provided, together with the commitment that the detailed listing will be sent to the LTA at latest on June 30th of the subsequent year.

A list of the double tax treaties entered into by Luxembourg and their respective availability to UCIs can be found in the Circular as well as on the website of the LTA.

DTT WITH GERMANY - INTERPRETATION OF THE TERM *INVESTMENTVERMÖGEN*

The Luxembourg tax authorities released Circular L.G. – Conv. D.I. n°58 on February 9th 2015 (hereafter the "Circular") which aims at providing clarification with regards to the interpretation of the term *Investmentvermögen* used in the new double tax treaty signed between Luxembourg and Germany and effective since January 1st 2014 (hereafter the "DTT").

Article 1 §1 of the protocol to the DTT states that *Investmentvermögen* set up in accordance with the law of one of the contracting States (in Luxembourg an *Investmentvermögen* is a *fonds commun de placement*, commonly referred to as an FCP, i.e. an investment fund without a corporate form that is represented and managed by a management company) can request the benefits of the articles 10 (related to dividend distributions) and 11 (related to interest payments) provided that they are held by residents (as defined in article 3.d. of the DTT) of the same contracting State. In case the *Investmentvermögen* avails itself of the reduced treaty rates as regards dividends and interest payments, the investors lose their right to claim these treaty benefits.

Prior to the issuance of the Circular, there was some uncertainty as to whether Article 1 §1 created a special entitlement of the tax transparent *Investmentvermögen* itself to the benefits of the DTT and especially to the reduced withholding tax rate on dividend payments (irrespective of the actual percentage of ownership of each investor) or whether this confirmation is solely of a procedural nature, i.e. related to whom in practice <u>requests</u> the application of the DTT (as opposed to being <u>entitled</u> to its benefits).

As a result, the Luxembourg tax authorities clarified that the protocol to the DTT solely confirms that the *Investmentvermögen* is allowed to request the application of the benefits of the DTT on behalf of its investors (instead of each investor requesting it separately). As such, the reduced withholding tax rate of 5 % on dividend distributions is only applicable for investors in the *Investmentvermögen* that fulfil the condition of article 10, i.e. corporate investor holding at least 10% of the share capital of the distributing company (through the tax transparent *Investmentvermögen*.)

TAXATION OF BELGIAN COMMUTERS

The double tax treaty signed on September 17th 1970 between the Grand-Duchy of Luxembourg and the Kingdom of Belgium (the "DTT") provides in its article 15 that employment income derived by a resident of a contracting State in respect of an employment exercised in the other contracting State is in principle taxable in such other contracting State. However, in case the link between the employee and its State of employment is weak, the exclusive taxing right falls back to the State of residence. Such weak link is deemed to exist, in case three criteria are cumulatively fulfilled:

- The employee is present in the State of employment for less than 183 days in an aggregate 12-month period commencing or ending in the fiscal year concerned; and

- The remuneration is not paid by or on behalf of an employer who is established in the State of employment; and
- The remuneration is not borne by a permanent establishment which the employer has in the State of employment.

Further to the so-called "*Gäichel VIII*" agreement, the Luxembourg and Belgian governments agreed to consider a 24-days tolerance when applying the provisions of article 15 of the DTT, with retroactive effect as from January 1st 2015 onwards.

Where, prior to January 1st 2015, a Belgian resident employed by a Luxembourg company was taxable in Luxembourg only for the days worked physically in Luxembourg and in Belgium for any other days worked abroad, such employee will now remain taxable in Luxembourg on his or her entire employment income, provided he or she works outside Luxembourg for a maximum of 24 days in the relevant calendar year. In case the employee works abroad for 25 days or more during a calendar year, his or her remuneration related to those working days will become taxable in Belgium.

SUPER REDUCED VAT RATE NOT APPLICABLE TO E-BOOKS

By judgement dated March 5th 2015 (the "Judgement"), the Court of Justice of the European Union (the "ECJ") ruled that the Grand-Duchy of Luxembourg had failed to fulfil its obligations under the Council Directive 2006/112/EC of November 28th 2006 on the common system of value added tax (the "VAT Directive") by applying its super reduced VAT rate of 3% to digital books.

The Commission had brought an action for infringement of EU Law before the ECJ. According to the Commission, the application of the super reduced rate was incompatible with the provisions of articles 96 to 99, 110 and 114 of the VAT Directive.

Indeed, the ECJ followed the reasoning of the Commission by considering that the reduced VAT rate is applicable only to transactions consisting in the supply of a book on a physical medium. Even though, in order to be able to read an electronic book, physical support, such as a computer, is required, the ECJ noted that such support is not included in the supply of electronic books.

In addition, any provision regarding the application of reduced VAT rates is to be seen as an exception to the principle that Member States are to apply a standard rate of VAT to transactions subject to VAT and must therefore be interpreted strictly.

The ECJ finally concludes that the supply of electronic books has to be considered as an "*electronically supplied service*" within the meaning of article 98 (2) of the VAT Directive, as an electronic book cannot qualify as tangible property. Consequently, since the latter provision precludes the possibility of applying a reduced rate of VAT to such services, the Grand-Duchy of Luxembourg has failed to fulfil its obligations under the VAT Directive.

By circular letter n° 756bis dated March 16th 2015, the Luxembourg VAT authorities have confirmed that, as from May 1st 2015, the supply of e-books will be subject to the standard VAT rate of 17%. It has to be noted that, despite the recent increase from 15% to 17%, such standard VAT rate remains the lowest in Europe.

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