Newsletter

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SUMMARY

CAPITAL MARKETS

TRANSPOSITION OF THE TRANSPARENCY AND PROSPECTUS AMENDMENT DIRECTIVE

On August 17th 2015, draft law N° 6860 (the "Draft Law") was introduced to the Luxembourg Parliament. The Draft Law will transpose

(i) Directive 2013/15/EU (the "Transparency and Prospectus Amendment Directive") and
(ii) the first article of Directive 2014/51/EU amending Directives and Regulations in respect of the powers of European Supervisory Authorities.

The Transparency and Prospectus Amendment Directive must be transposed into Luxembourg national law by November 27th 2015.

The provisions of Chapter 1 of the Draft Law concern amendments to the Luxembourg law of January 11th 2008 on transparency requirements for issuers of securities (the "Transparency Law"). The proposed amendments to the Luxembourg law of July 10th 2005 on prospectuses for securities, as amended (the "Prospectus Law") are dealt with in Chapter 2 of the Draft Law, and finally Chapter 3 deals with the entry into force of one of the new requirements under the Draft Law.

<u>Chapter 1 of the Draft Law</u>

A few of the main changes to the Transparency Law are as follows:

- The definition of "issuer" will be extended to include "natural persons" and to clarify that in the case of depository receipts admitted to trading on a regulated market, the issuer means the issuer of the securities represented, whether or not those securities are admitted to trading on a regulated market.
- The definition of Home Member State will be modified in order to clarify and simplify the determination of the Home Member State of an issuer of a third country. Importantly, for issuers who have not yet informed the competent authorities of their choice of Home Member State within three months from the date that issuer's securities are first admitted to trading on a regulated market, the Home Member State shall be the Member State where the issuer's securities are admitted to trading.
- The annual financial report required under Article 3 of the Transparency Law and the half-yearly financial reports required under Article 4 of the Transparency Law will need to remain available to the public for ten years (instead of five years).
- The half-yearly financial reports required under Article 4 of the Transparency Law must be made public at the latest three months after the end of the relevant period, instead of two months;
- Interim management statements/quarterly financial reports under Article 5 of the Transparency Law will no longer be required.
- To reinforce transparency as regard payments made to governments, issuers whose securities are admitted to trading on a regulated market and who have activities in the extractive and logging of primary forest industries will be required to disclose in a separate report on an annual basis, payments made to governments in the countries in which they operate; such payments shall be reported on a consolidated level.
- It will be clarified that the notification requirements of the acquisition and disposal of major holdings, do not apply to voting rights attached to shares acquired for stabilisation purposes provided that the voting rights attached to those shares are not

exercised or otherwise used to intervene in the management of the issuer.

- The definition of financial instruments will be extended for the purposes of the major-holdings notification requirements under Article 8 of the Transparency Law to cover all instruments with similar economic effect to holding shares and entitlements to acquire shares.
- An issuer who proposes to amend its articles of incorporation shall no longer be required to provide a draft of such amendment to the CSSF in advance, as currently required under Article 18(1) of the Transparency Law.
- The sanctioning powers of the CSSF will be extended and strengthened.

<u>Chapter 2 of the Draft Law</u>

The Draft Law provides for an amendment of the definition of home Member State in the Prospectus Law so as to ensure consistency between the Transparency Law and the Prospectus Law. The new definition of Home Member State in the Prospectus Law will provide for more flexibility where the securities of an issuer of a third country are no longer admitted to trading on the regulated market in its Home Member State but instead are admitted to trading in one or more other Member States.

<u>Chapter 3 of the Draft Law</u>

Finally, pursuant to Article 22 of the Draft Law, the requirement for reports on payments made to governments under the new Article 5 of the Transparency Law, will apply for financial years commencing January 1st 2016 or during the course of 2016.

CORPORATE

MODERNISATION OF LUXEMBOURG COMPANY LAW

The most recent amendments to the draft law (*Projet de Loi*) N° 5730 regarding, notably, the updating of the Law of August 10th 1915 (as amended) on commercial companies were proposed by the parliamentary sub-commission on the modernisation of Luxembourg corporate law in April 2015 (Document 5730/05) and are now subject to further discussions before, hopefully, being adopted by the end of 2015.

The bill as it presently stands will provide legal certainty for certain practises that are already well established under Luxembourg law. At the same time the draft law seeks to modernise and introduce new provisions to re-inforce the competitive edge of Luxembourg corporate law.

The most important provisions that are proposed to be introduced are the following:

<u>In relation to private limited companies (S.à r.l.s):</u>

- maximum number of shareholders is raised from 40 to 100;
- possibility to issue redeemable shares;
- possibility to issue debt securities to the public (but not shares or beneficial parts);
- legal rules introduced re the delegation of daily management and use of telecommunication devices in board and shareholder meetings;
- possibility to have an authorised capital extended to S.à r.l.s (subject to approval of new shareholders);
- the payment of interim dividends is subject to the same rules currently applicable to S.A.s.

<u>In relation to public limited companies (S.A.s):</u>

- possibility to issue shares at below par value (subject to reports by the board of directors and an independent auditor);
- introduction of regime for the allocation of free shares to employees;
- recognition of clauses providing for restrictions on the transferability of shares, beneficial parts or debt securities provided these are limited in time;
- greater flexibility to regime of non-voting shares (abolition of limitation to 50% of capital and need to attach preferential financial rights to such shares);
- recognition of the creation of committees and delegation to a general director and a management committee (with greater powers than a daily manager);
- introduction of the possibility for shareholders/holders of beneficial parts holding at least 10% of votes to take legal action against management.

<u>In relation to both types of company:</u>

- possibility to have "tracking" shares;
- possibility to issue shares of unequal value;
- express rules introduced in relation to beneficial parts (with or without voting rights);
- possibility to suspend voting rights of shareholders where such shareholders do not comply with their obligations and express recognition that shareholders may waive exercise of their voting rights;
- unanimity of votes no longer required for change of nationality of a company;
- new regime regarding issue of bonds and convertible securities;
- possibility for shareholders to take legal action to declare void the decisions taken at general meetings;
- authorisation can be set out in articles to allow the board to decide on a change of registered office within the Grand Duchy of Luxembourg and the related change of articles.

The draft law also introduces a new form of company into Luxembourg law, the "*société par action simplifiée*". While based on the rules governing the SA, the articles can freely determine how the corporate governance is to be organised.

If the draft law is passed in the present form, then existing companies will need to amend their articles of incorporation (in accordance with the legal procedures required for a change of articles) to comply with the new provisions within two years from the date on which the law takes legal effect. Past this deadline the provisions of the articles conflicting with the new law are deemed to be invalid and the new legal rules become directly applicable.

LAW OF 25 JULY 2015 RELATING TO ELECTRONIC ARCHIVING

After more than two years of discussion the law of July 25th 2015 relating to electronic archiving and amending Article 1334 of the Civil Code, Article 16 of the Commercial Code and the amended law of April 5th 1993 relating to the financial sector (the "Law"), entered into force on August 7th 2015.

As Article 1 provides, the Law pursues 3 objectives:

- Defining the digitisation conditions for documents under private signature and any document referred to under Article 16 of the Commercial Code, as well as the storage conditions for copies of any electronic

document under private signature or of any document originally created in digitised form;

- Determining the conditions for those copies to benefit from the legal presumption of conformity to their originals; and
- Fixing the rules governing the activity of the digitisation or storage service providers.

Excluded from the Law's scope are the activities of simple data storage without keeping an electronic copy or a digitised original by securing its integrity.

The Grand-Ducal regulation of July 25th 2015 relating to the digitisation and the storage of documents (entering into force in November 2015) purports to achieve the first objective. Said regulation sets out:

(i) the necessary characteristics to qualify as "'probative value copy",
(ii) the conditions of authenticity and durability for the digitised or micrographic reproductions of original documents or for digitised originals, and
(iii) applicable rules for probative value copies by micrographics.

The second objective is realised by the reversal of the burden of proof in favour of "probative value copies": the new Article 1334-1 of the Civil Code (just as the new third paragraph of Article 16 of the Commercial Code) creates a rebuttable presumption of probative value equivalent to original documents for digitised copies that are made by a duly certified and registered digitisation or storage service provider. On the other hand any service provider who has not been duly certified and/or registered on the special ILNAS list does not benefit from the legal presumption that its electronic copies have the same probative value as the original documents or deemed equivalent thereto.

As regards the last objective, the Law first regulates the status of digitisation or storage service providers (*"prestataires de services de dématérialisation ou de conservation"* – PSDC). To this effect, a second grand-ducal regulation of July 25th 2015 specifies the certification conditions to be met by the PSDC. Furthermore, those PSDC operating in the financial sector will need to qualify as one of the two new categories of support professionals of the financial sector under the 1993 law. Secondly the Law lays down the following obligations to be complied with by the PSDC:

(i) the obligation to provide information on the conditions of digitisation and storage covered by the certification prior to any new contract with clients;
(ii) the professional secrecy obligation (except vis-à-vis ILNAS in its capacity as supervisory authority for the PSDC);
(iii) the obligation to fully own the equipment or media on which at least one copy of all probative value copies and digitised originals is kept and not to guarantee or pledge said equipment or media; and
(iv) certain obligations in case of transfer or cessation of the PSDC activities.

Being innovative compared to other EU Member States, the Grand Duchy expects to attract international companies to centralise their electronic archiving in Luxembourg with substantial cost and space savings.

INVESTMENT MANAGEMENT

CASE LAW - INDIVIDUAL CLAIMS AGAINST BANKS AND PSF BASED ON BREACHES OF RULES OF CONDUCT

Luxembourg's highest Courts issued on February 25th and March 26th 2015, two different rulings which override the past position that refused the possibility for individuals to base a civil claim against a bank or other professionals of the financial sector ("Professionals") for reason of a breach of rules of conduct and/or organizational rules (the "Rules").

Under Luxembourg law, Professionals shall, on a permanent basis, comply with the Rules contained in the amended law of April 5th 1993 on the financial sector ("Banking Law") and the law of November 12th 2004 on the fight against money laundering and terrorist financing ("AML Law"), as well as with all the relevant implementing regulations and circulars issued by the *Commission de Surveillance du Secteur Financier* (the "CSSF").

Previously, Luxembourg Courts took the position that it was not possible for individuals to base a civil claim against a Professional on the fact that such Professional was in in breach of the Rules.

It had been held that the Rules did not constitute per se a legal base for individual claims before courts, as they were created for the protection of the public interest and not of private interests. The non-respect of the Rules was to be sanctioned exclusively by the CSSF, as they were considered to be of a purely administrative nature.

However, since 2008, some rulings started to gradually soften this approach, on the ground that, even though the Rules did not provide individuals with the right for direct action, Courts could use them in order to look for the existence of fault in the behaviour of a Professional, independently from the contractual provisions stipulated between parties.

In February 2015, the Luxembourg Court of Appeal ruled that individuals are allowed to invoke directly the liability of a Professional, on the ground of a breach to the rules of conduct provided for in Article 37 of the Banking Law (ruling N° 39014).

Moreover, on March 2015, the Luxembourg Supreme Court reaffirmed this principle, granting the right for compensation to an individual who claimed a breach of the Banking Law and the AML Law. According to the Supreme Court, "the fact that a rule is enacted for the protection of the public interest does not exclude that this same rule shall also protect private interests and give rise to the right for compensation to those individuals who have suffered damages due to the violation of this rule" (ruling N° 24/15).

The Luxembourg position follows the tendency in European law to strengthen the possibility for individuals to invoke the liability of the Professionals directly before the courts. The UCITS V Directive goes in this direction, giving the right to all investors (and not just unitholders in funds in contractual form) to invoke directly the liability of depositary banks.

Ruling N° 24/15 of the Luxembourg Supreme Court is available at: http://www.justice.public.lu/fr/jurisprudence/cour-cassation/commercial/2015/03/3420/COM20150326_3420a-24.pdf

AIFMD

UPDATED ESMA Q&A

On July 21st 2015, the European Securities and Markets Authority ("ESMA") published an updated version of its questions and answers ("Updated Q&A") on the application of the Alternative Investment Fund Managers Directive ("AIFMD"). The Updated Q&A contains clarifications on the reporting and on the calculation of the total value of assets under management ("AUM").

When reporting information to the national competent authorities of an EU Member State under Article 42 of the AIFMD, a non-EU AIFM marketing AIFs in EU Member States under the national private placement regime will only have to report the information regarding the AIFs that are marketed in this Member State. However, if that Member State applies ESMA's opinion on collection of information for the effective monitoring of systemic risk the non-EU AIFM should also report information on non-EU master AIFs which are not marketed in the EU but that have either EU feeder AIFs or non-EU feeder AIFs marketed in the Union.

It has also been clarified how the AIFMs should convert the total value of assets under management into Euro. It is recommended that the AIFM presents the rounded values of the AIFs in their base currency divided by the corresponding value of one Euro into the base currency of the AIF. Both the rounded values in the base currency and in Euro must be reported for the purpose of questions 33, 34 and 48 of the consolidated reporting template for AIF-specific information. The exchange rate used for the conversion should be reported in questions 37 and 50.

ESMA also confirms that AIFMs should include AIFs created during the reported period in the total value of assets under management of the AIFM for that reporting period, even if there is no obligation to report specific information on such AIFs. As a consequence, the total value of AUM of the AIFM at the reporting date will not match the sum of the values of AUM of the AIFs reported for the same period.

Finally, with regard to the calculation of the total value of assets under management, ESMA has clarified that AIFMs should include short non-derivative positions when calculating the total value of AUM.

The Updated Q&A is available at:
https://www.esma.europa.eu/system/files/2015-1137_qa_on_the_application_of_the_aifmd.pdf

AMENDMENT TO AIFM LAW

The law of July 23rd 2015 which implements Directive 2013/36 on credit institutions (commonly referred to as CRD IV) amends Article 5(6) of the AIFM Law.

A new paragraph is inserted providing that Article 101 (4) second paragraph of the law of December 17th 2010 relating to undertakings for collective investment applies to AIFMs that provide discretionary portfolio management in accordance with Article 5(4)(a) of the AIFM Law.

This amendment was to rectify an error in transposing the AIFMD into Luxembourg law and what it means in practice is that such AIFMs have to comply with rules relating to capital adequacy requirements.

ESMA ADVICE ON THE EXTENSION OF THE PASSPORT

On July 30th 2015, the European Securities and Markets Authority ("ESMA") published its advice to the European institutions on the application of the AIFMD passport with regard to non-EU AIFMs and AIFs ("Advice") and its Opinion ("Opinion") on

the functioning of the AIFMD passport and the National Private Placement Regimes (“NPPRs”).

In the Opinion, ESMA evaluated the functioning of the EU passport and the NPPRs and while some issues were identified none were considered major. ESMA referred to the problem of different approaches to marketing rules in Member States such as: wide differences in the fees charged by national regulators and differences in interpretation of what activities constitute “marketing”. There are also differences in the definition of a professional investor.

However, ESMA was of the view that only one year of passport use is insufficient to allow for a full analysis and suggests that a better view might be formed over a longer period of time, after which a new Opinion should be prepared.

In the Advice, ESMA explains that it has conducted a country-by-country assessment, taking into account the different circumstances of each non-EU jurisdiction regarding the regulatory issues to be considered (i.e. investor protection, competition, potential market disruption and the monitoring of risk). In this first round of jurisdiction reviews ESMA only assessed six jurisdictions: Guernsey, Hong Kong, Jersey, Singapore, Switzerland and the United States.

Those initial countries were chosen due to a number of factors, such as:

- the level of activity already being carried out by entities from those countries under the NPPRs,
- EU national authorities’ and regulators’ knowledge and experience of dealing with their counterparts in the non-EU countries, and
- the level of engagement with ESMA’s review process by market participants, including AIFMs, from those countries.

The Advice that ESMA gives to the European Parliament, the Council and the Commission is that:

- there are no apparent obstacles to the passport being extended to AIFMs or AIFs established in Guernsey and Jersey ; and
- other than an amendment to the Swiss Federal Act on Stock Exchanges and Securities Trading, which becomes effective on January 1st 2016, there are no obstacles to the passport being extended to AIFMs or AIFs established in Switzerland.

However, ESMA was unable to reach a conclusion regarding Hong Kong, Singapore and the United States because of concerns regarding competition, regulatory issues and a lack of sufficient evidence to properly assess the relevant criteria. ESMA stated that it will finalise its analysis of those and other non-EU countries as soon as possible.

The Advice and Opinion are currently being considered by the European Commission, Parliament and Council, which will offer their views in due course as to whether they believe that EU law needs to be amended to extend the passport.

The Commission should adopt a delegated act within 3 months of ESMA’s Advice. However, ESMA suggests that the European institutions may consider waiting to take a decision on extending the passport to non-EU jurisdictions until it has delivered positive advice on a sufficient number of non-EU countries and territories, to avoid any adverse market impact that might result from a decision to extend the passport to only a few non-EU countries.

The Opinion is available at:
http://www.esma.europa.eu/system/files/2015-1235_opinion_to_ep-council-com_on_aifmd_passport_for_publication.pdf

The Advice is available at:
http://www.esma.europa.eu/system/files/2015-1236_advice_to_ep-council-com_on_aifmd_passport.pdf

UPDATED CSSF FAQ

On August 10th 2015 the CSSF issued an updated, 9th version of its Frequently Asked Questions (the "FAQ") concerning the Luxembourg Law of July 12th 2013 on alternative investment fund managers (the "AIFM Law") as well as the Commission Delegated Regulation (EU) N° 231/2013 of December 19th 2012 (the "Level 2 Regulation").

The FAQ confirm, that neither credit institutions nor investment firms established under the Law of April 5th 1993 on the financial sector, as amended (the "1993 Law") can obtain an alternative investment fund manager (the "AIFM") authorisation. However they are allowed to register as an AIFM. They may also manage alternative investment funds ("AIF") on the basis of a delegation agreement.

The updated FAQ clarify that depositaries of assets other than financial instruments (the "PDAOFI") can be appointed as depositaries for AIFs, when the following conditions are fulfilled:

- no redemption right exercisable in the AIF for five years from the date of the initial investments, and
- the main investment policy of such AIFs is either generally not to invest in assets which shall be held in custody or generally to invest in issuers or non-listed companies to eventually acquire control.

PDAOFI, when acting as a depositary for eligible AIFs, are responsible for the safekeeping of the assets which are financial instruments. In such case it would have to delegate the custody of such assets to an eligible delegate.

Also, PDAOFI can act as delegate for the safekeeping of assets other than financial instruments for any type of AIF.

The FAQ confirm the legislation to be taken into account for the purpose of assessing the initial capital and own funds requirements applicable to external AIFMs. For external AIFMs that are not Chapter 15 management companies, the only relevant regulatory provisions are those laid down in the AIFM Law and the Level 2 Regulation. Chapter 15 management companies that are authorised as an AIFM also have to take the provisions of the law of December 17th 2010 relating to undertakings for collective investment, into account.

On reporting, the CSSF confirmed that, based on the provisions of Article 45 of the AIFM Law, a non-EU AIFM will have to report to the CSSF only in the case where this non-EU AIFM is marketing AIFs to professional investors in Luxembourg and as long as the passport regime is not available to non-EU AIFMs.

Additionally, a non-EU AIFM that manages or markets a feeder AIF (whether EU or non-EU) in Luxembourg will also have to report to the CSSF on the non-EU master AIF(s) of such feeder, even if the non-EU master AIF is not marketed in the EU.

Finally the CSSF has also updated its guidance on marketing and reverse solicitation. It is clarified that marketing in Luxembourg does not require physical presence of the AIFM on the Luxembourg territory. However, the marketing activity must take place on the Luxembourg territory. The presentation of draft documents in relation to an AIF by the AIFM to prospective investors does not constitute a marketing activity, provided that such draft documents can't be used by the investors to

formally subscribe or commit to subscribe shares or units of the AIF.

The CSSF provides that reverse solicitation consists in providing information regarding an AIF and making units or shares of that AIF available for purchase to a potential investor following an initiative of that investor (or an agent of that investor) without any solicitation made by the AIF or its AIFM (or an intermediary acting on their behalf) in relation to the relevant AIF. The burden of proof rests with the AIFM.

The FAQ are available at:
http://www.cssf.lu/fileadmin/files/AIFM/FAQ_AIFMD.pdf

EMIR – DRAFT LAW

On August 5th 2015, the Luxembourg government introduced before the Parliament the draft law N° 6846 on OTC derivatives, central counterparties and trade repositories and modifying certain laws of the financial sector ("Draft Law").

The main aim of the Draft Law is to give to the relevant authorities the powers required for the accomplishment of their mission under regulation (EU) N° 648/2012 of the European Parliament and of the Council of July 4th 2012 on OTC derivatives, central counterparties and trade repositories ("EMIR"). In this regard the Draft Law appoints the *Commission de Surveillance du Secteur Financier* ("CSSF") as the authority in charge of supervising the correct application of EMIR and it empowers the latter to exchange information and cooperate with the competent authorities of other EU Member States and with the relevant European authorities for the purposes of and within the limits set forth by EMIR.

The above appointment is done without prejudice to the powers of the Central Bank of Luxembourg and to the legal powers that have been given to the *Commissariat aux Assurances* in respect of the entities that fall under its supervision.

The Draft Law grants to the CSSF and the *Commissariat aux Assurances* the power to sanction the non-respect of EMIR by entities subject to their supervision.

In addition the Draft Law foresees amendments to the law of December 17th 2010 on undertakings for collective investment ("2010 Law") and the law of July 12th 2013 on alternative investment fund managers ("AIFM Law"), aimed at reducing the excessive dependence of financial institutions on credit ratings.

These amendments aim at preventing the systematic recourse to credit agency ratings by management companies, AIFMs and investment companies established in Luxembourg, when assessing the risks associated with the portfolio composition. The Draft Law also indicates that the investment policies of UCITS and AIFs, with references to ratings, will be closely supervised by the CSSF who shall try to reduce the mechanical and systematic recourse to credit rating agency ratings where possible.

The Draft Law further amends several Luxembourg laws of the financial sector in order to transpose and apply in Luxembourg different European texts.

The Draft Law is available here (only in French):
http://www.chd.lu/wps/PA_RoleEtenduEuro/FTSByteServingServletImpl/?path=/export/exped/sexpdata/Mag/179/461/147680.pdf

EUROPEAN LONG-TERM INVESTMENT FUNDS – DRAFT REGULATORY TECHNICAL STANDARDS

Regulation 2015/760 (the "Regulation") on the European Long-Term Investment Fund ("ELTIF") entered into force on June 9th 2015.

Following the entry into force of the Regulation, the European Securities and Markets Authority ("ESMA") released on July 31st 2015 a consultation paper (the "Consultation Paper") on draft regulatory technical standards ("RTS"). The RTS shall regulate various aspects which are "*critical for the functioning of the Regulation*".

Such various aspects can be summarised as follows:

1. The criteria for establishing the circumstances in which the use of financial derivatives serves hedging purposes:

Pursuant to Article 9(2) and 9(3) of the Regulation, the use of financial derivatives by an ELTIF is only permitted for hedging purposes.

In considering the term "hedging" ESMA considers a number of pieces of existing legislation and regulation and proposes that a financial derivative instrument shall be considered as serving the purpose of hedging if two cumulative criteria are met:

(i) it qualifies as a hedging instrument that is eligible for hedge accounting purposes pursuant to IFRS standards; and
(ii) it mitigates the risks arising from the potential impact on the value of the other investments of the ELTIF resulting from fluctuation of hedged items.

Risks to be covered not only include currency, inflation and interest rate risks but should also take into account the nature of the long-term and real estate investments.

2. The criteria for establishing the circumstances in which the life of an ELTIF is considered sufficient in length:

Basically the life of an ELTIF should be set in a way that takes into account each and all of the individual assets of the ELTIF portfolio, as stated in Article 18(3) of the ELTIF Regulation. Therefore, ESMA proposes to determine the life of the ELTIF in accordance with the life of the asset which has the longest life-cycle.

In addition, ESMA further proposes that ELTIFs should not invest in assets which have a life-cycle which exceeds the residual time of the ELTIF.

3. Orderly disposal of the ELTIF assets:

The draft RTS includes criteria on the valuation of the assets to be divested in order to ensure the orderly disposal of the ELTIF assets at the end of the life-cycle of the ELTIF.

4. Costs disclosure:

Pursuant to Article 25 of the ELTIF Regulation, the prospectus of an ELTIF shall prominently inform investors of the level of the different costs borne directly or indirectly by them. Pursuant to the Regulation ESMA should take into account certain regulatory technical standards under the PRIIPs regulation. However those standards are not yet available so ESMA sought inspiration from the existing legislation and regulation concerning the Key Investor Information Document. For the most part ESMA are proposing that costs be expressed as a percentage of the capital of the ELTIF (called and uncalled). The RTS set out how the overall ratio of the costs is to be calculated and provides that such ratio shall be calculated at least once a year.

5. The facilities available to retail investors:

The draft RTS further specify the facilities that have to be available to retail investors for making subscriptions, making payments to unit - or shareholders, repurchasing or redeeming units or shares and making available the regulatory information.

Comments should be sent to ESMA on or before October 14th 2015.

The consultation paper is available at http://www.esma.europa.eu/system/files/2015-1239.pdf.

UCITS V

GUIDELINES ON SOUND REMUNERATION POLICIES

Further to the entry into force of Directive 2014/91/EU of the European Parliament and of the Council of July 23rd 2014 (“UCITS V Directive”), the European Securities and Markets Authority (“ESMA”) released on July 23rd 2015 a consultation paper (the “Consultation Paper”) on sound remuneration policies under the UCITS V Directive.

The aim of the Consultation paper is to obtain feedback from market participants in respect of the draft guidelines on remuneration (which are attached to the Consultation Paper) proposed by ESMA (the “UCITS Remuneration Guidelines”).

The UCITS Remuneration Guidelines do not differ substantially from the equivalent guidelines applicable to alternative investment fund managers under Directive 2011/61/EU which were published on July 3rd 2013 (“AIFMD Remuneration Guidelines”).

The UCITS Remuneration Guidelines will apply to management companies and to investment companies which have not appointed a management company. In line with the AIFMD Remuneration Guidelines, the UCITS Remuneration Guidelines impact the remuneration paid to so-called *identified staff* but also impose obligations on management companies/investment companies to establish or amend certain internal procedures.

Identified staff are within the management of a UCITS the “*categories of staff, including senior management, risk takers, control functions and any employee receiving total remuneration that falls into the remuneration bracket of senior management and risk takers, whose professional activities have a material impact on the management company’s risk profile or the risk profiles of the UCITS that it manages* [*and to the delegates thereof …*]”.

The UCITS Remuneration Guidelines shall apply to any type of remuneration paid to *identified staff*, including performance fees and any transfer of shares/units of the UCITS.

In order to avoid circumvention of the remuneration rules, the UCITS Remuneration Guidelines require management companies/investment companies to ensure that their service providers are subject to similar rules and that appropriate contractual arrangements are put in place.

The main requirements of the UCITS Remuneration Guidelines can be summarised as follows:

- UCITS management companies/investment companies shall identify the persons qualifying as “identified staff”;
- UCITS management companies/investment companies shall enact a remuneration policy which takes into consideration the factors

mentioned in the UCITS Remuneration Guidelines, e.g. the remuneration must be related to the impact of the identified staff on the risk profile of the UCITS;

- The *supervisory function* shall approve and maintain the remuneration policy as well as supervise its effective implementation;
- Requirement to set up a remuneration committee for certain management companies;
- Clarification on the role of the control functions (such as the internal audit function, the risk management function, etc.) in the design, oversight and review of the remuneration policy;
- Clarifications on best practice when implementing performance related remuneration mechanisms such as deferral and retention mechanisms; and
- Clarification of the proportionality principle which allows the non-implementation of certain guidelines in light of the relatively small size of the relevant UCITS management company/investment company.

The UCITS Remuneration Guidelines do not impose any reporting duties on the management companies/investment companies but they are required to disclose the policy internally, and to a certain extent, externally (e.g. stating the main principles in the annual report).

The consultation is open until October 23rd 2015 and the guidelines in their final form are expected to enter into force on the transposition deadline for UCITS V being March 18th 2016.

A copy of the consultation paper is available at http://www.esma.europa.eu/system/files/2015-1172_cp_on_ucits_v__aifmd_remuneration_guidelines.pdf.

DRAFT LAW

On August 5th 2015, the government introduced the draft law 6845 which aims at transposing Directive 2014/19/UE of the European Parliament and of the Council of July 23rd 2014 (the "UCITS V Directive"), amending the 2009/65/CE Directive, into Luxembourg Law (the "Draft Law") .

The Draft Law implements the UCITS V Directive into Luxembourg law while amending the law of December 17th 2010 on undertakings for collective investment (the "UCI Law") and the law of July 12th 2013 on alternative investment fund managers (the "AIFM Law").

1. Amendment of the UCI Law

- The introduction of a new depositary regime

The Draft Law transposes faithfully the text of the UCITS V Directive. It clarifies the notion of the safekeeping of assets, regulates the regime of delegation and sub-delegation and introduces the obligation for the segregation of assets held in custody. In addition, it prohibits the re-use of assets by the depositary itself, unless certain conditions are met. This differs from the AIFM Directive, where the re-use of assets is permitted after prior consent of the AIF or the AIFM acting on the AIF's behalf.
Most importantly, in case of loss caused by an event which is not beyond its reasonable control, the Draft Law provides for the obligation to return financial instruments held under custody, of an identical type or corresponding amount.
In general, the new regime of liability of the depositary of UCITS is largely based on the provisions of the AIFM Law although in this case the depositary is not allowed to discharge its liability.

- The harmonisation of the rules regarding remuneration policies

The rules introduced concerning the remuneration of individuals aim to prevent excessive risk taking and situations involving conflicts of interests.

They introduce, among other provisions, the obligation to apply remuneration policies which are compatible with sound and effective risk management.
The new rules apply to UCITS management companies and self-managed SICAV.

- The harmonisation of administrative sanctions

The new regime of administrative sanctions include a list of breaches and minimum sanctions harmonised at a European level and rules concerning the publication of sanctions, encouraging the reporting of breaches to the CSSF.

2. Amendment of the AIFM Law

The Draft Law further proposes some amendments to the AIFM Law that are not related to the implementation of the UCITS V Directive: alternative investment fund managers, to have their accounting documents audited by an independent auditor: (i) the possibility for AIFM to provide on a cross-border basis certain investment services such as the management of individual portfolios and investment advice which for the moment may only be performed in the country where they are authorised.

AMENDMENT OF THE DOUBLE TAX CONVENTION BETWEEN LUXEMBOURG - SPAIN

On July 21st 2015, the Luxembourg tax administration issued Circular L.-G. – Conv. D.I. n° 52 (the "Circular") on the application of the Luxembourg - Spain Income and Capital Tax Treaty (1986) (the "Treaty") and its final protocol (the "1986 Protocol"). With the Circular, which applies immediately as from its date of issuance (i.e. July 21st 2015), the Luxembourg tax administration determines treaty access of Luxembourg investment vehicles.

The Circular states that, through the exchange of letters of April 15th 2015 and May 13th 2015, the tax authorities of both countries have agreed that the Treaty does not apply to:

1. Certain undertakings for collective investments ("UCIs") governed by part II of the Luxembourg law of 17th December 2010 relating to undertakings for collective investments, as amended (the "2010 Law").

2. Certain specialised investment funds ("SIFs") governed by the Luxembourg law of 13th February 2007 relating to specialised investment funds, as amended (the "2007 Law").

3. Family wealth management companies (*société de gestion de patrimoine familial*, "SPF").

Therefore, Paragraph 1 Ad articles 1, 3 and 4 of the 1986 Protocol now precise that the Treaty will not be applicable to SIFs and UCIs organised as investment companies with variable capital ("SICAVs") and investment companies with fixed capital ("SICAFs") as of July 21st 2015.

As regards the exclusion of the UCIs and SIFs, from treaty access, the Circular merely confirms the position that was already specified in previous circulars (e.g. circular L.-G. -A. N° 61 of 12th February 2015).

The Circular of July 21st 2015 can be found at http://www.impotsdirects.public.lu/legislation/legi15/index.html#circulaires

The circular of February 12th 2015 can be found at http://www.impotsdirects.public.lu/legislation/legi15/Circulaire-LG-A-n_-61-du-12-fevrier-2015.pdf

The Treaty and the 1986 Protocol can be found at http://www.impotsdirects.public.lu/conventions/conv_vig/index.html

LABOUR LAW

WORKING TIME DIRECTIVE – TRAVEL TO PLACE OF WORK

Directive 2003/88/EC of the European Parliament and of the Council of November 4th 2003 concerning certain aspects of the organisation of working time (the "Directive") defines working time as "*any period during which the worker is working, at the employer's disposal and carrying out his activity or duties (…)*". A rest period is any period which is not deemed working time.

A recent case before the European Court of Justice (the "ECJ") concerned a company employing technicians to install and maintain security equipment on premises located within a geographical area assigned to them, meaning that they did not have a fixed place of work.

Previously, the employees might have used a company vehicle for travelling from the company's office to the various places of work and for returning to the company's office at the end of the day.

During that time, the employees' daily working time started when they arrived at the office and ended when they returned to the office in the evening. Hence, the travel from the office to the first customer was considered as working time, as well as the travel from the last customer back to the office.

However, in 2011, the company closed some regional offices and assigned all of its employees to the central office in Madrid.

Since then, for calculating the number of daily working hours of the concerned employees, the company took into consideration the time elapsing between when its employees arrived at the first customer and when they left the last customer, ignoring the time spent travelling between home and customers.

The question that arose in this case is whether the time spent by the employee travelling at the beginning and at the end of the day must be regarded as working time within the meaning of the Directive?

In its judgment, the ECJ declares that, where employees do not have a fixed or habitual place of work, the time spent by those employees travelling each day between their homes and the premises of the first and last customers constitutes working time within the meaning of the Directive.

According to the ECJ, since these employees carry out their duties over the whole duration of the journeys, they are acting on the instructions of the employer and are at the employer's disposal for the whole time of the journeys. Therefore, they are not able to use their time freely and pursue their own interests.

In this case, the fact that the employees begin and finish the journeys at their homes stems directly from their employer's choice to close some offices and not from the desire of the employees themselves. Consequently, travelling is a part of the employees' duties, and the time spent travelling between home and customers must be considered as working time. Indeed, the place of work of the concerned employees cannot be reduced to the physical areas of their work on the premises of the employer's customers, especially since the journeys of the employees at the beginning and at the end of the day to or from customers were regarded as working time before the closure of the regional offices.

The judgement is available at the following link: http://curia.europa.eu/juris/liste.jsf?language=en&num=C-266/14&td=ALL

TAX

NEW CORPORATE TAX MEASURES

On August 5th 2015, a new draft law (draft law N°6847 hereafter referred to as the "Draft Law") was presented to the Luxembourg Parliament. The Draft Law introduces (i) the new general anti-abuse rule ("GAAR") and anti-hybrid rules of the EU Parent-Subsidiary Directive, (ii) horizontal tax consolidation and (iii) various corporate tax measures.

TRANSPOSITION OF NEW GAAR AND ANTI-HYBRID RULES OF THE EU PARENT-SUBSIDIARY DIRECTIVE

The Draft Law proposes to amend both the Luxembourg withholding tax exemption and the Luxembourg dividend exemption regime, in order to include the new anti-hybrid and anti-abuse rules that were added to the Parent-Subsidiary Directive (hereafter the "PSD") in 2014 and beginning of 2015 respectively. The Draft Law does not amend the grand-ducal Decree providing for capital gains exemption nor article 115 al. 15a of the Luxembourg income tax law which provides for a 50% dividend exemption.

Pursuant to the Draft Law, dividend distributions received by a qualifying Luxembourg resident company and dividend distributions made by a qualifying Luxembourg resident company would not be exempt from corporate income taxes or withholding taxes if the income is received or the dividend is distributed by virtue of *"an arrangement or a series of arrangements which, having been put into place for the main purpose or one of the main purposes of obtaining a tax advantage that defeats the object or purpose of this Directive, are not genuine having regard to all relevant facts and circumstances. An arrangement or a series of arrangements shall be regarded as not genuine to the extent that they are not put into place for valid commercial reasons which reflect economic reality"*.

As regards the anti-hybrid rules, the Draft Law provides that the dividend exemption regime (provided that all other requirements are met) should only apply, if the dividend received by the qualifying Luxembourg resident entity was not deductible at the level of the non-resident EU subsidiary.

The new GAAR and anti-hybrid rules would only apply to dividend distributions received from or made to non-Luxembourg resident EU subsidiaries or parent companies, falling within the scope of the EU Parent-Subsidiary Directive. As a result, the existing exemption regime would remain applicable to domestic as well as non-EU structures.

If adopted, these amendments would apply to any dividend income and distribution taking place after December 31st 2015.

HORIZONTAL TAX CONSOLIDATIONS

The Draft Law proposes to amend the existing tax consolidation regime, in order to allow for horizontal consolidation of Luxembourg resident entities held by a common parent company established in the European Economic Area (hereafter the "EEA"), provided the latter is subject to a corporate income tax that is comparable to the Luxembourg corporate income tax.

In practice, one could thus form a fiscal unity between Luxembourg sister companies without the need to include the common foreign parent company. As a consequence, the integrating head of the fiscal unity would not be the parent entity, but one of the Luxembourg sister companies designated in the tax consolidation request.

Given that the proposed horizontal tax consolidation would also include, as integrated entities, Luxembourg permanent establishments of EEA resident parent companies, provided that they are subject to a corporate income tax comparable to the Luxembourg corporate income tax, the same would apply to the current vertical tax consolidation regime.

The Draft Law also extends the right of recovery of tax claims to all the members of a tax consolidation.

If the Draft Law is adopted, the above amendments would apply as of the tax year 2015.

INVESTMENT TAX CREDITS FOR VESSELS / EXIT TAX / UNEMPLOYED INDIVIDUALS TAX CREDIT

The Draft Law proposes to extend the Luxembourg investment tax credit regime to the lessor of vessels used in international traffic. This amendment shows the continued commitment of the legislator to strengthen the Luxembourg maritime industry. This amendment would apply as of the tax year 2015.

Additionally, the Draft Law enlarges the exit tax deferral mechanism to migrations to non-European countries, provided that Luxembourg either entered into a double tax treaty including an exchange of information clause that follows the OECD Model or signed a bilateral / multilateral tax information exchange agreement with that country. This amendment should be applicable as of the tax year 2016.

Lastly, the Draft Law proposes to extend the tax credit for the hiring of unemployed individuals for another two years until December 31st 2016.

EU-FATCA AND THE OECD MULTILATERAL COMPETENT AUTHORITY AGREEMENT - DRAFT LAW

With draft law N° 6858 (the “Draft Law”), which was submitted to Parliament on August 14th 2015, Luxembourg aims at enhancing its commitment with regard to international exchange of information. The goal of the Draft Law is to implement Directive 2014/107/EU which significantly enlarges the scope of Council Directive 2011/16/EU on administrative cooperation in the field of taxation, which has been implemented by the laws dated March 29th 2013 (the “2013 Law”) and March 26th 2014.

If adopted, any Luxembourg reporting financial institution, as defined in Annex I and II of the Draft Law, will be required to provide to the Luxembourg Tax Authorities (*Administration des Contributions Directes*, “ACD”) the same information as foreseen in Art. 2 N°2 of the FATCA intergovernmental agreement concluded between the United States and Luxembourg. This includes notably the name, address, birth date and birthplace of the account holder and its taxpayer identification number, the account number, name and ID of the Reporting Luxembourg Financial Institution, the account balance or value, the total gross amount of interest, dividend, other income generated with respect to the assets held in the account, and the total gross proceeds from the sale or redemption of property paid or credited to the account.

In addition, the Draft Law also aims at implementing the multilateral competent authority agreement (“MCAA”), which Luxembourg signed on October 29th 2014 in Berlin, in order to automatically exchange information based on Article 6 of the Multilateral Convention on Mutual Administrative Assistance in Tax Matters and promoting the automatic exchange of information as the global new

standard and going hand in hand with the common reporting standard (“CRS”) developed by the OECD.

The information regarding the reportable accounts are to be provided by the Luxembourg reporting financial institution to the ACD by June 30th of the year following the year to which the information relates, and subsequently exchanged by the ACD by September 30th following the year to which the information relates, for the first time in September 2017 regarding fiscal year 2016.

Information will be exchanged automatically with all Member States of the European Union (on the basis of Council Directive 2014/107/EU), and with all other jurisdictions (i) having entered the MCAA and (ii) having implemented adequate national legislation allowing the exchange of information under the MCAA.

FATCA – ENTRY INTO FORCE

The intergovernmental agreement (“IGA”), its annexes and the “Memorandum of Understanding”, all signed on March 28th 2014 between the US and Luxembourg as regards FATCA was voted by Parliament on July 1st 2015 and was promulgated as Luxembourg law of July 24th 2015 (the “Law”). With the exchange of diplomatic notes between the government of Luxembourg and the United States on March 31st 2015, article 10 of the IGA has been amended and the ratification of the Double Tax Treaty protocol by the United States as a condition for the entry into force of the IGA has been abolished. Therefore, Luxembourg has completed the necessary internal procedures and the IGA effectively entered into force on July 29th 2015.

As a consequence, Luxembourg financial institutions are now obliged to provide the information as defined in the IGA by June 30th following the year to which the information relates. For 2015 the reporting deadline was postponed twice by the Luxembourg tax authorities to finally be set at August 31st 2015. The information received by the Luxembourg Tax Authorities was due to be exchanged with the IRS by September 30th 2015.

In addition to the Law, the Luxembourg Tax Authorities issued the final versions of the Circular Letters ECHA 2 and ECHA 3 on July 31st 2015 (the “Circular Letters”). Circular letter ECHA 2 provides more detailed guidance as to which Luxembourg institution and which accounts are within the scope of the IGA, what due diligence procedures need to be followed and to what extent the exchange of information takes place. Circular letter ECHA 3 deals with the technical aspects and the form which the Luxembourg financial institutions need to comply with for the exchange of information under FATCA.

TAX TREATY UPDATE

With draft law N° 6826 (the “June Draft Law”), which was submitted to Parliament on June 9th 2015, Luxembourg aims at expanding further its already comprehensive double tax convention network. The Draft Law, if adopted, would ratify and add or replace another four new double tax treaties concluded with Andorra, Croatia, Estonia and Singapore, and six new protocols amending existing tax treaties with France, Ireland, Lithuania, Mauritius, the United Arab Emirates and Tunisia. All these new treaties and amending protocols follow the OECD Model Tax Convention.

Luxembourg currently has an impressive network of 76 tax conventions in force and 29 treaties under negotiation.

As regards the six protocols, Luxembourg shows an ongoing commitment to include exchange of

information provisions in line with the OECD standards in the tax treaties. That's why five out of the six new protocols deal mainly with an exchange of information provision. The protocol amending the tax treaty with France mainly targets capital gains realised upon the sale of shares or other rights in real estate companies, which shall be taxed in the country where the real estate is located.

VAT: EXPENSES RELATED TO THE ACQUISITION OF SHARES

On July 16th 2015, the European Court of Justice delivered its judgement in the joined cases Larentia + Minerva (C-108/14) and Marenave (C-109/14) and extended its series of rulings on the deductibility of input VAT by holding companies. This article only covers the input VAT deductibility question which was referred for a preliminary ruling. Two other questions were referred to the ECJ: (i) can a member State exclude partnerships from the VAT consolidation and may such a consolidation be limited to persons in a relationship of control and subordination and (ii) can a taxable person rely directly on the article of the VAT Directive providing for VAT consolidation.

Both German companies, Larentia + Minerva GmbH & Co. KG and Marenave Schiffahrts AG, held shares in subsidiaries to whom they rendered administrative services. Both companies were originally refused permission to deduct (at least part of) the input VAT related to expenses in relation with the raising of capital to fund the acquisition of their shareholdings. An action was brought before the *German Bundesfinanzhof*, which asked for a preliminary ruling.

The ECJ first recalled that, as opposed to the mere acquisition and holding of shares in a company, the involvement of a holding company in the management of companies in which it has acquired a participation constitutes an economic activity within the meaning of the VAT Directive.

On the main question, the ECJ then decided that holding companies, charging administrative and management services to their subsidiaries, should be allowed to fully deduct input VAT on costs related to the acquisition of shareholdings, except in cases where the services provided by said companies include VAT exempt supplies.

The Court further held that, in case a holding company provides management services to only some of its subsidiaries but not to all of them, input VAT should only be partially deductible. An allocation of the costs and input VAT incurred between:

(i) the economic activity of the company, being the holding of shares in subsidiaries to which VAT taxable services are rendered and
(ii) the non-economic activity of mere holding of the shares in the remaining subsidiaries, to which no services are rendered, should be carried out according to specific criteria determined by the Member States but the method of calculation must objectively reflect the part of the services to be actually attributed respectively to the economic and non-economic activities.

LUXEMBOURG CASE LAW

APPLICATION OF THE NEW PROCEDURE ON EXCHANGE OF INFORMATION ON DEMAND

On August 13th 2015, the Luxembourg Administrative Court (*tribunal administratif)* (the "Court") took the first decision in the matter of exchange of information in application of the law of November 25th 2014 relating to the new procedure applicable to exchange of information

on demand (the "Law"). The Law significantly reduces the rights of taxpayers to appeal against a request of information on demand and provides for an administrative fine in case of non-communication of the required information. For more information please refer to [our newsletter of February 2015](#).

In the case at hand the company refused to communicate certain information requested by the tax authorities on the ground that they were not foreseeably relevant. The tax authorities consequently imposed an administrative fine of EUR 250,000 in application of the Law. The company appealed against the decision of the tax authorities before the Administrative Court.
The Court held that the foreseeable relevance of the request of information can no longer be contested in application of Article 6 of the Law.

The Court also confirmed that the request of information is a preliminary tax decision which cannot be challenged on the ground of Article 6 of the European Convention on Human Rights ("ECHR"); the application of Article 6 ECHR being excluded in tax matters and from the preliminary stages of a procedure.

The analysis of the Court was therefore limited to the validity of the administrative fine against which an appeal is possible under the Law.

In this respect, the Court referred to an instruction issued by the head of the Luxembourg tax authorities detailing the criteria relevant for the determination of the amount of an administrative fine in the framework of a request of exchange of information (the "Instruction") and concluded that by immediately imposing the highest fine on the company, the proportionality and progressivity rules expressly mentioned in the Instruction were not respected. The Court decided that the fine was excessive and reduced it to an amount of EUR 150,000.

CLARIFICATIONS ON THE APPLICATION OF ARTICLES 23 (3) AND 41 LITL

On May 21st 2015, the Luxembourg Higher Administrative Court ("*Cour Administrative*" - the"Court"*)* took a decision on the valuation and classification of a receivable denominated in a currency other than Euro.

A Luxembourg company (the "Company") initially recorded a CHF denominated receivable as a short-term receivable in its 2007 and 2008 accounts. From an accounting perspective, the receivable was converted in EUR by using the applicable foreign exchange rate at the end of the financial year. Latent foreign exchange gains and losses were taken into account for the determination of the income taxable basis. The Company made a claim against the tax assessments arguing that the receivable was erroneously recorded as a short-term asset valued at the year-end foreign exchange rate. The receivable should have been instead recorded as a financial asset and valued at its historical rate.

The Court confirmed that the provisions of Article 23 (3) of the Luxembourg income tax law ("LITL") concerning the valuation of assets are applicable to all the assets other than the depreciable assets. Article 23 (3) LITL is thus applicable regardless of the classification of the receivables as a short-term asset or as financial asset. For tax purposes, a non-EUR denominated receivable has to be recorded at a value not exceeding its acquisition price which is determined in EUR by using the foreign exchange rate applicable at the time of the receivable was accounted for. In application of the prudence principle, latent foreign exchange gains are not taken into account unlike the latent foreign exchange losses.

The Court also ruled on the request of the Company to reclassify the receivable as a long-term asset rather than a short-term asset in application of Article 41 LITL even though this

classification has no influence on the valuation of the receivable for tax purposes.

According to the Court, the modification of the tax balance sheet is, as per Article 41 (2) LITL, allowed, if (i) the initial balance sheet complies with the provisions of the tax law and (ii) such changes are justified by serious economic reasons.

The Court concluded that in the case at hand the first condition was met since

(i) the initial classification of the receivable as a short-term asset and its valuation at the year-end foreign exchange rate was not against the provisions of Articles 21 and 23 (3) LITL and the related applicable accounting principles and
(ii) its reclassification as a financial asset to give a true and fair view of the accounting and financial situation of the Company and to prevent negative economic consequences of the erroneous classification of the receivable on the calculation of the financial ratio and the evaluation of the assets and activities of the Company by third-parties, were serious economic reasons in the meaning of Article 41 (2) LITL.

The Court also added that although it is not expressly required by the law but as a result of the principle of "*accrochement du balance fiscal au bilan commercial",* the modification of the tax balance sheet in application of Article 41 LITL requires the parallel modification of the commercial balance sheet.

All the required conditions being met, the Court held that the receivable of the Company denominated in CHF could be:

(i) valued at its historical cost determined by using the foreign exchange rate applicable at the time of the transaction and in parallel
(ii) classified in the balance sheet as a financial asset.

CONFIRMATION OF THE ESTABLISHED CASE LAW IN THE MATTER OF ABUSE OF LAW

On July 15th 2015, the Administrative Court took a decision on the application of the concept of the abuse of law to transactions performed by a Luxembourg taxpayer.

In the case at hand, a Luxembourg company (the "Company") entered into an advisory agreement with a company located in the British Virgin Islands (the "BVI Company") according to which the BVI Company was assisting the Company in the development of consumer financing and insurance activities through one of its indirect subsidiaries. Due to the financial crisis, this activity was eventually not successful for the Company. The tax administration rejected the deductibility of the fees paid by the Company to the BVI Company under the advisory agreement, requalified them as a hidden dividend distribution and considered that these transactions were constitutive of an abuse of law according to §6 of the Adaptation Law (*Steueranpassungsgesetz*).

The Court reiterated the well-established four cumulative criteria used to qualify a specific case as an abuse of law:

- the use of forms and institutions of private law,
- a reduction of tax,
- the use of an inappropriate "path";
- the absence of non-tax reasons justifying the use of the chosen "path".

The Court took the position that, in the matter of abuse of law, the burden of proof is split between

the tax administration and the taxpayer. The Company having provided the contracts, a structure chart and explanations in order to justify the economic reality of the transaction, the tax authorities should have provided concrete points supporting the argument against the economic reality of the transaction. The fact that the BVI Company is not subject to an effective taxation and is domiciled in a country (the BVI) where there is no double tax treaty providing for the automatic exchange of information is not sufficient to conclude that the BVI company is a shelf company and the payments made to the BVI Company are constitutive of an abuse of law.

In addition, the Court concluded that the tax authorities did not demonstrate that the legal structure was set up solely for tax purposes which is an essential requirement to qualify a legal construction as an abuse of law and in the case at hand it was *prima facie* in the economic interest of the Company and the BVI Company to have the services described in the advisory agreement becoming successful.

APPLICATION OF ARTICLE 50 BIS LITL TO IP RIGHTS ACQUIRED IN EXCHANGE OF SHARES

On June 16th 2015, the Administrative Court (*Tribunal Administratif)* (the “Court”) took a decision on the application of the provisions of Article 50 Bis of the Luxembourg Income Tax Law (“LITL”)

In the case at hand, a Luxembourg permanent establishment of a UK company was contributed to a newly created Luxembourg company (“Tax Payer”) in exchange for newly issued shares of the Tax Payer. The main assets of the permanent establishment were trademarks, patents, patterns and domain names (the “IP rights”). The Tax Payer acquired these assets at their book value in application of Article 172§4 LITL.

Pursuant to Article 170§5 and 172§4 LITL, the Tax Payer acquired the IP rights from the UK company in tax neutrality and recorded them at their historical acquisition cost. The tax authorities denied the application of Article 50 Bis LITL to the income derived from the IPs on the ground that the IP rights were acquired from a related company. Since the Tax Payer booked the IP rights at their historical acquisition price, the tax authorities considered that the condition prescribed in Article 50 Bis LITL that the IP rights shall not be acquired from a related party, had to be examined on the date of the initial acquisition by the UK Company. Since the IP rights were acquired by the UK company from a sister company, the tax authorities concluded that the IP rights had been acquired from a related company and that the condition of Article 50bis §5 LITL was not met.

The Court held that the legal fiction provided by Article 170§5 LITL which allows the transfer of assets in tax neutrality if the transferee records the assets at their historical acquisition price, is of strict interpretation and is therefore limited to the acquisition date of the assets transferred. Any other elements of the initial acquisition such as the contracting parties or their shareholding relationship is irrelevant for the application of Article 170§5 LITL.

The Court concluded therefore that in case of transfer of IP rights in tax neutrality, the condition relating to the shareholding relationship between the parties set forth in Article 50§5 LITL shall not be analysed at the time of the initial transaction but immediately before the contribution.

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