# NEWSLETTER

October 2020

Right by you in Luxembourg

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# COVID-19

**PLEASE REFER ALSO TO OUR BSP COVID-19 DEDICATED NEWSLETTER FOR MORE INFO ON LATEST LUXEMBOURG DEVELOPMENTS WITHIN THE COVID-19 EMERGENCY.**

## EXTENSION OF TELEWORKING FOR BELGIAN, FRENCH AND GERMAN CROSS-BORDER WORKERS IN THE CONTEXT OF THE COVID-19 PANDEMIC

As previously stated in our newsflash dated 19 March 2020 (as updated), the Luxembourg Government has agreed on an "exceptional measure" with the Belgian, French and German Governments regarding the taxation of Belgian, French and German cross-border commuters normally working in Luxembourg and now teleworking from their homes.

As a result, as of 14 March 2020, any days of presence of a cross-border worker at his home, in particular to carry out teleworking, are not to be taken into account for the calculation of the 24-day (Belgium) or 29-day (France) period. The measures applying to French and Belgian cross-border workers were applicable until
31 August 2020. By renewal agreements signed with Belgium and France, respectively on
24 August 2020 and 27 August 2020, the measures have been extended until 31 December 2020.

The measure applying to German cross-border workers was applicable as of 11 March 2020 and lasted until 30 April 2020, at which point an automatic monthly renewal took place, which will continue unless Germany or Luxembourg terminate the agreement.

Likewise, on 25 August 2020, agreements have also been extended with the aforementioned countries with respect to social security. Following the agreement signed in July 2020 with Belgium, France and Germany to maintain the exceptional arrangement not to take into account teleworking linked to the COVID-19 pandemic for the determination of the social security legislation applicable to cross-border workers until 31 August 2020, an extension until 31 December 2020 of said arrangement has also been agreed. In concrete terms, a cross-border worker who carries out his work from home will continue to be affiliated to the Luxembourg social security system until the end of the year.

## THE PROPOSED EU RECOVERY PROSPECTUS

### THE EU RECOVERY PROSPECTUS HAS BEEN PROPOSED BY THE EUROPEAN COMMISSION IN DIRECT RESPONSE TO THE COVID-19 PANDEMIC

The goal of the proposed Regulation which would amend Regulation (EU) 2017/1129 (the "**Prospectus Regulation**") as regards the EU Recovery prospectus and targeted adjustments for financial intermediaries to help the recovery from the COVID-19 pandemic (the "**Proposal**") is to help companies to access new funding in a short time period to facilitate the economic recovery from the COVID-19 pandemic. In particular, it aims to help companies raise equity so that they can restore sustainable debt-to-equity ratios and become more resilient.

### CONTENT

The proposal aims at simplifying the procedure for issuers to quickly raise capital by the creation of a new type of short-form prospectus (the "**EU Recovery Prospectus**") as well as targeted amendments to release pressure on financial intermediaries (notification of supplements and non-equity issuances by credit institutions).

The EU Recovery Prospectus aims to focus on essential information and would only be available **for secondary issuances of shares**. Provided that issuers have shares already admitted to trading on a regulated market or an SME growth market continuously for at least the last 18 months, the alleviated disclosure is expected to reduce the cost of drawing up a prospectus and to make the document easier to understand. The EU Recovery Prospectus is expected to be a single document with a maximum of **30 pages**, and a short summary of two pages. Additionally, the proposed EU Recovery Prospectus regime intends to shorten prospectus approval to **5 working days**. This new type of prospectus would also benefit from the EU single passport of approved prospectuses for cross-border offers and admissions to trading.

Article 1(1) of the Proposal deals with non-equity securities issued by credit institutions in a continuous or repeated manner (Article 1(4) of the Prospectus Regulation).

An offer of such securities is, under certain conditions, not subject to the obligation of publishing a prospectus if the total consideration is less than EUR 75 million per credit institution calculated over a period of 12 months. A targeted increase of the threshold from EUR 75 million to EUR 150 million is proposed. As this measure is limited to the recovery phase, it would therefore be available for a limited time period of 18 months. Articles 1(2) and 1(3) of the Proposal deal with technical adjustments on the materiality test (Article 6 of the Prospectus Regulation) and summary (Article 7 of the Prospectus Regulation) in relation with the EU Recovery Prospectus regime.

Article 1(4) of the Proposal creates a new regime for the EU Recovery Prospectus (Article 14a of the Prospectus Regulation).

The EU Recovery Prospectus regime should expire after an **18 months** period of application (Article 47a of the Prospectus Regulation).

## Next steps

The next step is for the European Parliament and the Council to agree to the legislative text of the Proposal. If and when the Proposal is adopted and enters into force, the changes to the Prospectus Regulation will apply directly in the Member States.

# AML

## AML | CSSF CIRCULAR 20/746 ON FATF STATEMENTS

On 9 July 2020, the CSSF published Circular CSSF 20/746 (repealing Circular CSSF 20/738 of 6 March 2020) updating all professionals under the supervision of the CSSF on the recent statements made by the Financial Action Task Force ("**FATF**") on jurisdictions identified with strategic deficiencies in their regimes to counter money laundering, terrorist financing, and proliferation financing.

### HIGH-RISK JURISDICTIONS ON WHICH ENHANCED DUE DILIGENCE AND, WHERE APPROPRIATE, COUNTER-MEASURES ARE IMPOSED

***Democratic People's Republic of Korea***

The FATF maintains its position that the AML/CFT regime of the Democratic People's Republic of Korea ("**DPRK**") continues to have substantial and strategic deficiencies, requesting jurisdictions to take measures to close existing subsidiaries, branches or representative offices of DPRK banks, where applicable, within their respective territories.

The CSSF urges professionals to pay additional attention to business relationships and transactions with DPRK, including with companies and financial institutions from this jurisdiction and those acting on their behalf. The CSSF further emphasises the need for applying enhanced due diligence and monitoring measures to such business relationships and to inform the CSSF in case of a correspondent banking relationship with a credit institution from the DPRK.

***Iran***

Despite a political commitment in 2016 by Iran towards FATF to address its strategic AML/CFT deficiencies, it has not yet fully addressed them in full. For this reason, FATF will keep Iran on its list of countries with AML/CFT deficiencies until FATF is of the opinion that Iran has efficiently addressed such deficiencies identified by FATF.

Similar with the case of DPRK, CSSF urges professionals to continue taking into account the risks arising from the strategic deficiencies of the AML/CFT regime of Iran and to apply enhanced due diligence and monitoring measures to business relationships and transactions with this jurisdiction, including with companies and financial institutions from this jurisdiction and those acting on their behalf.

Moreover, the CSSF expects professionals to inform the former (i) in case of a correspondent banking relationship with a credit institution from Iran and (ii) in case of use of a third party located in Iran and conducting elements of the due diligence process (third-party introducers and/or outsourcing).

### JURISDICTIONS UNDER INCREASED MONITORING OF THE FATF

The FATF decided to remove Iceland and Mongolia from its list of countries with AML/CFT deficiencies as they demonstrated that substantial efforts have been made in addressing the deficiencies in their regimes to counter money laundering, terrorist financing, and proliferation financing as identified by the FATF.

The following jurisdictions currently have strategic AML/CFT deficiencies for which they have developed an action plan with the FATF: Albania, Bahamas, Barbados, Botswana, Cambodia, Ghana, Jamaica, Mauritius, Myanmar, Nicaragua, Pakistan, Panama, Syria, Uganda, Yemen and Zimbabwe.

The CSSF requests professionals to consider, where appropriate, the deficiencies identified by the FATF in its statements and the risks arising from them for their business relationships and transactions with these jurisdictions.

Below are FATF's full decisions and statements:

- http://www.fatf-gafi.org/publications/high-risk-and-other-monitored-

jurisdictions/documents/call-for-action-june-2020.html
- http://www.fatf-gafi.org/publications/high-risk-and-other-monitored-jurisdictions/documents/increased-monitoring-june-2020.html

## AML | CSSF REGULATION 20-05 AND GDR OF 14 AUGUST 2020

### REGULATIONS AMENDING CSSF REGULATION 12-02 OF 14 DECEMBER 2012 AND GRAND DUCAL REGULATION OF 1 FEBRUARY 2010 ON THE FIGHT AGAINST MONEY LAUNDERING AND TERRORIST FINANCING

CSSF Regulation 20-05 of 14 August 2020 ("**CSSF Regulation**") amending CSSF Regulation No 12-02 of 14 December 2012 on the fight against money laundering and terrorist financing and Grandducal Regulation of 14 August 2020 ("**GD Regulation**") amending Grandducal Regulation of 1 February 2010 providing details on certain provisions of the Law of 12 November 2004 on the fight against money laundering and terrorist financing, as amended ("**AML Law**") entered into force on 24 August 2020.

Both the CSSF and GD Regulations follow the entry into force of the Luxembourg laws of (i) 25 March 2020 transposing into national law certain provisions of the Directive (EU) 2018/843 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing (5th AML Directive) and (ii) 10 July 2020 setting up a register of fiduciaries and trusts.

Professionals who fall in scope of the AML Law are impacted by the following **key** changes/clarifications brought by both the CSSF and GD Regulations:

### CLARIFICATIONS ABOUT THE IMPLEMENTATION OF THE RISK-BASED APPROACH

- Determination of the risk-based approach to be taken by a professional must, at all times, be based on its money laundering ("**ML**")/terrorist financing ("**TF**") risk appetite, which must be duly approved by the professional's board of directors and put into place by its authorised management. Implementing risk management procedures, the professional shall take into consideration various sources e.g. the Supranational Risk Assessment, the National Risk Assessment and sub-sector Risk Assessments.
- Professionals must ensure that they annually complete the CSSF questionnaire about the collection of information on ML/TF, and submit this questionnaire to the CSSF within the required deadlines.
- Where a business relationship presents a low risk of ML/TF and the professional applies simplified customer due diligence ("**CDD**") measures accordingly, the professional must be able to justify and demonstrate this business relationship's low risk of ML/TF to the competent Luxembourg authorities for AML/CTF.
- The risk assessment carried out by a professional does not, under any circumstances, entitle the professional to waive enhanced CDD measures where such measures are expressly prescribed under the AML Law.

### CLARIFICATIONS ON CDD MEASURES

- "Customer" is now defined as a natural or legal person with whom a business relationship exists or for whom an occasional transaction is carried out, including persons purporting to act on behalf of the customer (or investors, in the case of investment funds).
- Professionals must review and update the information on the customer at least every seven years, without prejudice to higher frequency depending on the risk assessment. The GD Regulation sets out examples of situations where updated information may be required.
- Virtual asset service providers must apply CDD measures when carrying out

occasional transactions exceeding a threshold of EUR 1,000 (instead of the usual EUR 15,000 threshold).

- Regarding CDD measures applicable to an intermediary acting on behalf of its customers, these CDD measures must be applied to the intermediary on a two-level basis: (a) the intermediary, the persons purporting to act on behalf of this intermediary and the beneficial owners of the intermediary must be identified, and their identities verified, on a risk-based basis; and (b) enhanced CDD measures must be implemented for business relationships viewed as similar to correspondent relationship with the intermediary.
- Professionals are required to perform an analysis of the ML/TF risk related to a given investment and implement CDD measures in accordance with the risk-based approach. Such risk analysis carried out on investments must be reviewed both annually and each time that a particular event requires a review.
- Professionals may now accept a customer presenting a low risk of ML/TF on the basis of an automated acceptance process which does not involve the intervention of a natural person at the level of the professional, provided that such process has previously been duly configured and tested and is reviewed on a regular basis by the professional.
- The use of electronic identification means (e.g. relevant trust services as set out in Regulation (EU) No 910/2014), or any other secure, remote or electronic identification process that is regulated, recognised, approved or accepted by the relevant national authorities is permitted for the verification of a customer's identity.
- The use of central registers as the sole means of verifying the identities of a customer's beneficial owners is not sufficient to constitute due compliance with the obligation to take reasonable measures to verify the identities of such beneficial owners – a standard ML/TF risk-based approach still needs to be followed.
- The CSSF Regulation introduces a list of examples of simplified CDD measures which may be applied by professionals with respect to low risk business relationships. It is further specified that, regardless of the frequency of review of the business relationship, professionals must verify at least once a year that the conditions justifying the application of simplified CDD measures are still present.
- The CSSF Regulation provides examples of enhanced CDD measures to be applied by professionals with respect to high-risk business relationships (e.g. obtaining additional information or documentation on the source of the funds involved and of wealth); it is further specified that CDD measures applied to politically exposed persons (PEP) must be carried out at least every six months.

## INCLUSION OF THE RULES ON THE TRANSFER OF FUNDS

Professionals shall take note of the rules under Regulation (EU) 2015/847 on the transfers of funds which were added to the text of CSSF Regulation No 12-02 of 14 December 2012 on the fight against money laundering and terrorist financing.

## SPECIFICATIONS RELATING TO THE USE OF OUTSOURCING ARRANGEMENTS

For funds specifically, the board of directors (or equivalent body) of a fund and/or the investment fund manager will be required to ensure that outsourcing arrangements contain the relevant detailed clauses specifying the roles and responsibilities of each party, and that such arrangements permit them to access any information deemed necessary for the performance of their function. They will also be required to perform ongoing, formalised monitoring of the delegated third party.

## SPECIFICATIONS RELATING TO SYSTEMS FOR THE SUPERVISION OF BUSINESS RELATIONSHIPS AND TRANSACTIONS

- Formalising what is CSSF practice, the CSSF Regulation now specifically provides that professionals are required to appoint both (i) a person responsible for compliance with the AML-CTF professional obligations at the level of the authorised management or board of directors and (ii) a compliance officer in charge of the control of compliance with the AML-CTF professional obligations and further defines such functions.
- The AML-CTF governance and internal organisation must follow the "three-lines defence" model:
    a) a first line of defence based on operational units, i.e. the persons in charge of business execution which are in direct contact with customers and which require a good understanding of the ML-TF risks;
    b) a second line of defence based on the person in charge of control, including other support, monitoring and compliance functions involved in AML-CTF matters, consisting of providing support, verifying the controls carried out by the first line of defence, and contributing to an independent control of the risks. The level of involvement of the second line of defence must increase with the customer's risk level;
    c) a third line of defence based on the internal audit function which independently assesses the first two lines of defence and also verifies the effectiveness of the professional's AML-CTF policies, procedures and programmes.

# BANKING & FINANCE

## NEW LUXEMBOURG DRAFT LAW TRANSPOSING CRD V AND BRRD II

### THE PURPOSE OF THE DRAFT LAW 7638, SUBMITTED TO THE LUXEMBOURG PARLIAMENT (*CHAMBRE DES DÉPUTÉS*) ON 27 JULY 2020 (THE "DRAFT LAW") IS TO TRANSPOSE INTO LUXEMBOURG LAW

- Directive (EU) 2019/878 of 20 May 2019 amending Directive 2013/36/EU as regards exempted entities, financial holding companies, mixed financial holding companies, remuneration, supervisory measures and powers and capital conservation measures ("**CRD V**"); and
- Directive (EU) 2019/879 of 20 May 2019 amending Directive 2014/59/EU as regards the loss-absorbing and recapitalisation capacity of credit institutions and investment firms and Directive 98/26/EC ("**BRRD II**").

### A BRIEF OVERVIEW OF CRD V AND BBRD II

CRD V, the so called capital requirements directive, in particular amends the provisions relating to the measurement of interest rate risk inherent to non-trading book positions, strengthens the supervisory framework for holding companies and creates an obligation for certain third-country banking groups to set up a single intermediary parent company in the European Union.

Additionally, CRD V further integrates the principle of proportionality into banking regulations, notably in the area of requirements applicable to remuneration policies, and reinforces the obligations of cooperation and information exchange between prudential authorities and authorities in charge of the fight against money laundering and terrorist financing.

BRRD II, the bank recovery and resolution directive, for its part, pursues the objective of strengthening the effectiveness of bank resolution in a crisis. To this end, it strengthens the rules on loss-absorbing capacity in order to allow for a restructuring of defaulting institutions that is less onerous for the resolution fund and to better protect depositors and other non-subordinated creditors of banks.

### HIGHLIGHTS OF THE RESULTING DRAFT LAW

The Draft Law, which mainly amends the Luxembourg law of 5 April 1993 on the financial sector, *inter alia* strengthens one of the pillars of banking supervision, i.e. additional capital requirements, by introducing the possibility for the CSSF to impose capital recommendations in addition to capital requirements.

The tools of macro-prudential supervision are reviewed in order to delineate them more clearly those of micro-prudential supervision and to make them more coherent by aligning and simplifying certain decision-making procedures and clarifying the articulation of the different capital cushions.

The Draft Law further aims to adapt the modalities related to the determination of minimum capital requirements and eligible instruments specific to each institution in order to ensure an efficient application of the bail-in tool.

Beyond the transposition of CRD V and BRRD II, the Draft Law includes, *inter alia*, propositions:

- to strengthen depositor protection by setting up an additional safety net for the benefit of the deposit guarantee fund; and
- to make targeted amendments to other laws, including but not limited to the Luxembourg law of 23 December 1998 establishing a financial sector supervisory commission ("*Commission de surveillance du secteur financier*"), as amended, with a view to facilitating, where appropriate, the implementation of crisis management mechanisms.

## SECURITISATION REGULATION | ELEMENTS OF NEW REGIME ENTER INTO FORCE

Following the publication in the EU Official Journal of seven technical standards relating to Regulation (EU) 2017/2402 of 12 December 2017 laying down a general framework for securitisation and creating a specific framework for simple, transparent and standardised securitisation, as amended (“**the Securitisation Regulation**”), the following elements of the new regime entered into force on 23 September 2020:

- The opening of applications for entities to register as a securitisation repository (“**SR**”), and
- The entry into force of new disclosure templates.

Indeed, on 23 September 2020, ESMA already announced that it had received its first application for registration as an SR and will further announce when the first SR is registered. Until that time, the relevant information must be made available via a website that meets specific requirements.

Regarding the disclosure templates, the transitional arrangements allowing reporting in other formats no longer apply. As from 23 September 2020 the disclosure templates annexed to the technical standards must be used. Guidance on how to complete these templates can be found in the Q&A on the Securitisation Regulation, last updated on 5 October 2020.

# CAPITAL MARKETS

## COMMISSION DELEGATED REGULATIONS AMENDING THE PROSPECTUS DELEGATED REGULATIONS (RTS)

### COMMISSION DELEGATED REGULATIONS AMENDING THE PROSPECTUS RTS REGULATION

Published on 14 September 2020 in the Official Journal of the EU, Commission Delegated Regulation (EU) 2020/1272 brought several modifications to Commission Delegated Regulation (EU) 2019/979 of 14 March 2019 supplementing Regulation (EU) 2017/1129 with regard to regulatory technical standards on key financial information in the summary of a prospectus, the publication and classification of prospectuses, advertisements for securities, supplements to a prospectus, and the notification portal, and repealing Commission Delegated Regulation (EU) No 382/2014 and Commission Delegated Regulation (EU) 2016/301 (the "**RTS**").

It amends Article 18(1) of the RTS by removing all references to issuers of securities convertible or exchangeable into third party shares.

Article 18(1) of the RTS lists the situations in which an issuer is required to publish a supplement to its prospectus. In its most recent version, issuers of securities convertible or exchangeable into shares of third parties were required to do so. Yet, Commission Delegated Regulation (EU) No. 382/2014 with regard to regulatory technical standards for publication of supplements to the prospectus, subsequently replaced by the RTS, did not require such issuers to publish a supplement to their prospectus. As these former rules have proven to be efficient and have not diminished the level of investor protection, Commission Delegated Regulation (EU) 2020/1272 deleted all references to issuers of securities convertible or exchangeable into shares of third parties from the list in Article 18(1) of the RTS.

It also inserts a new article 22a in the RTS dealing with summaries of prospectuses approved between 21 July 2019 and 16 September 2020 for non-financial entities.

The Commission Delegated Regulation (EU) 2020/1272 entered into force on 17 September 2020, but some of the amendments to Article 18(1) and Article 21 apply retrospectively, with effect from 21 July 2019.

### COMMISSION DELEGATED REGULATION AMENDING DELEGATED REGULATION 2019/980 SUPPLEMENTING THE PROSPECTUS REGULATION

Commission Delegated Regulation (EU) 2020/1273 was published on 14 September 2020 in the Official Journal of the EU and it modifies Commission Delegated Regulation 2019/980 supplementing Regulation (EU) 2017/1129 as regards the format, content, scrutiny and approval of the prospectus to be published when securities are offered to the public or admitted to trading on a regulated market, and repealing Commission Regulation (EC) No 809/2004, by adding new articles and correcting others.

Commission Delegated Regulation (EU) 2020/1273 entered into force on 17 September 2020. However, Article 1(1) to (8) (amendments to Articles 2, 4, 12, 13, 24, 25, 28 and 30) and Article 2 (amendments to Article 33 and 42(2)(g)) apply retrospectively, with effect from 21 July 2019.

## ESMA GUIDELINES ON DISCLOSURE REQUIREMENTS UNDER THE PROSPECTUS REGULATION

On 15 July 2020, ESMA published its final report on guidelines on disclosure requirements (the "**Guidelines**") under Regulation (EU) 2017/1129 of 14 June 2017

on the prospectus to be published when securities are offered to the public or admitted to trading on a regulated market (the "**Prospectus Regulation**").

## PURPOSE AND SCOPE

The Guidelines (which update and replace the recommendations of CESR, ESMA's predecessor (the "**CESR Recommendations**")) are intended to provide guidance on the various disclosure requirements pursuant to the Prospectus Regulation and related legislation, in particular Commission Delegated Regulation (EU) 2019/980 of 14 March 2019 supplementing the Prospectus Regulation.

## CONTENT AND KEY CHANGES

The content of the Guidelines generally carries over the content of the CESR Recommendations, but in a limited number of cases, ESMA included new Guidelines as well as added some new content in the explanatory text. In particular, changes were introduced in Guidelines 11 and 13 relating to profit forecasts, Guideline 18 relating to *pro forma* financial information, Guidelines 33, 36 and 37 relating to working capital statements and Guidelines 38 and 39 relating to capitalisation and indebtedness statements. The content of some Q&As from ESMA's Question and Answers on prospectuses were (in some cases only partially) also carried over to the Guidelines.

A couple of sections of the CESR recommendations were not carried over. In particular, the CESR recommendations relating to selected financial information (paragraphs 20-26) were not converted into the Guidelines, because selected financial information is not required under the Prospectus Regulation.

## NEXT STEPS

The Guidelines will become effective two months after their publication on ESMA's website in all the official languages. From that time and unlike the CESR Recommendations, the *comply or explain principle* will apply to the Guidelines.

# INVESTMENT MANAGEMENT

## UCITS | UPDATED CSSF FAQ

On 7 August 2020, the CSSF issued an updated version of its Frequently Asked Questions concerning the Luxembourg Law of 17 December 2010 relating to undertakings for collective investment schemes (the "**UCITS Law**" and the "**FAQ**").

With this update (the ninth) CSSF introduces a new FAQ (1.13 FAQ), stating that loans cannot be considered eligible assets for UCITS under Article 41 (1) and (2) of the UCITS Law.

The CSSF clarifies that the **loans cannot be qualified** as:

- **money market instruments** as defined in Article 1 (23) of the UCITS Law (instruments normally dealt in on the money market which are liquid and have a value that which can be accurately determined at any time) and in Articles 3 and 4 of the GrandDucal Regulation of 8 February 2008 (the "**Regulation**"), clarified by the CESR guidelines concerning eligible assets for investment by UCITS (the "**CESR Guidelines**"); neither as
- **transferable securities** as defined in Article 1 (34) of the UCITS Law (shares in companies or other equivalent securities, bonds and other form of securitised debt, other negotiable securities which carry the right to acquire such transferable securities by subscription or exchange) and in Article 2 of the Regulation, as further clarified by the CESR Guidelines.

The statement impacts all the Luxembourg domiciled UCITS, and the FAQ provide that:

- UCITS that are invested in loans are required to sell them by 31 December 2020, taking into account the best interest of investors;
- the prospectuses of the UCITS that provide for investments in loans have to be updated by 31 March 2021.

No reference has been made to KIIDs, but it's to be expected that KIIDs will also have to be updated.

## MMF | ESMA STATEMENT ON EXTERNAL SUPPORT

On 9 July 2020, ESMA issued a public statement on external support under Article 35 of the money market funds ("**MMF**") regulation ("**MMF Regulation**"). This statement was released in relation to financial markets authorities' recent actions to mitigate the impact of COVID-19 on the EU's financial markets. ESMA deemed it relevant to clarify the potential interaction between the intermediation of credit institutions and the requirements of Art. 35 of the MMF Regulation on external support.

ESMA highlights that the statement also aims to coordinate the supervisory approaches of national competent authorities ("**NCAs**") in light of liquidity challenges for MMFs in the context of the current COVID-19 pandemic.

In the second half of March 2020, certain MMFs faced significant liquidity challenges. MMFs also faced sizable redemptions from their investors, while on the asset side, liquidity deteriorated quickly in money markets in particular in the commercial paper market in the EU and the US.

### BANKING INTERMEDIATION IN THE PURCHASE OF MMFS' SHORT-TERM ASSETS

ESMA takes the view that it is important to clarify the potential interaction between the intermediation of credit institutions and the requirement of article 35 of the MMF Regulation.

According to Article 35 of the MMF Regulation, MMFs are unable to receive external support, defined as "*direct or indirect support offered to an MMF by a third party, including a sponsor of*

*the MMF, that is intended for or in effect would result in guaranteeing the liquidity of the MMF or stabilising the NAV per unit or share of the MMF".*

According to article 35 of the MMF Regulation, external support shall include:

a) cash injections from a third party;
b) purchase by a third party of assets of the MMF at an inflated price;
c) purchase by a third party of units or shares of the MMF in order to provide liquidity to the fund;
d) issuance by a third party of any kind of explicit or implicit guarantee, warranty or letter of support for the benefit of the MMF;
e) any action by a third party the direct or indirect objective of which is to maintain the liquidity profile and NAV per unit or share of the MMF.

ESMA clarified in relation to point b) above that transactions with third parties relating to the assets of the MMF are not purchased at an inflated price where they are executed at arm's length conditions. ESMA further clarified that where third parties execute transactions solely with the MMFs to which they are affiliated it is indicative of a direct or indirect objective to maintain the liquidity profile and NAV per unit or share of the MMF, referred to in e) above.

ESMA, together with the NCAs, will continue to closely monitor the situation and will take or recommend any measures necessary to mitigate the impact of COVID-19.

## ESG | TAXONOMY REGULATION

On 22 June 2020, the European Union published the long-awaited Regulation (EU) 2020/852 on the establishment of a framework to facilitate sustainable investment (the "**EU Taxonomy Regulation**"), and amending Regulation (EU) 2019/2088 on sustainability-related disclosures in the financial services sector.

This is the world's first-ever "green list" classification system for sustainable economic activities. It provides a general framework that will allow for the progressive development of an EU-wide classification system for environmentally sustainable economic activities.

For more details on the Taxonomy Regulation please refer to BSP Sustainable Finance Insight Series number 7.

## AIFMD | ESMA RECOMMENDS PRIORITY TOPICS IN AIFMD REVIEW

On 18 August 2020, ESMA wrote to the European Commission, highlighting areas to consider during the forthcoming review of the Alternative Investment Fund Managers Directive ("**AIFMD**").

ESMA recognises that the AIFMD has provided a solid framework for alternative investment funds in Europe since 2011. However, ESMA thinks that they, and the national competent authorities, have gained experience of the framework and have identified areas that could be improved to enhance the supervision of alternative fund managers in Europe.

ESMA's letter includes recommendations for changes in 19 areas including, harmonizing the AIFMD and UCITS regimes, delegation and substance (including more specific requirements on white-label service providers), liquidity-management tools, a new category of investors called "semi-professional investors", leverage, the AIFMD reporting regime, the harmonization of supervision of cross-border entities and clarification on the reverse solicitation.

Many of the recommendations made also require consideration of changes to the UCITS legislative framework.

Annex I to the letter sets out ESMA's recommendations to the legislative framework currently in place and recommendations regarding the reporting regime are made in Annex II.

ESMA encourages the European Commission to support the areas identified in the letter in order to improve the effectiveness and soundness of the AIFMD.

The next step in the AIFMD review process is a public consultation, which is planned to be launched during autumn 2020.

# TAX

## HIGHER ADMINISTRATIVE COURT JUDGMENT ON ABUSE OF LAW AND THE USE OF LUXEMBOURG SPF

In its judgment of 14 July 2020, the Luxembourg Higher Administrative Court (*Cour Administrative*) assessed whether the subscription of bonds by a Luxembourg family wealth management company, a *société de gestion de patrimoine familial* ("**SPF**") and the deduction of interest at the level of the issuer, a Luxembourg civil company held by the same individuals as the SPF, can be considered as an abuse of law under §6 of the Luxembourg *Steueranpassungsgesetz ("StAnpG")*.

In its judgment, the Court confirms the judgment of the Lower Administrative Court (*Tribunal Administratif*), which found the structuring to be an abuse of law within the meaning of §6 of the *StAnpG* (see our newsletter dated 4 December 2019). In contrast to the Lower Administrative Court, the Higher Administrative Court analysed whether the entities involved were legally entitled to issue and subscribe to the bonds.

The Court began by analysing the right for a Luxembourg civil company to issue bonds. It concluded that Luxembourg company law foresees the possibility to issue bonds exclusively by commercial companies, so that a civil company does not have the right to finance itself by issuing bonds.

The Court continued by assessing whether in the case at hand the SPF was entitled to subscribe to the bonds. The Court points out that pursuant to the law of 11 May 2007 on SPF companies ("**SPF Law**"), SPFs are in principle entitled to subscribe to bonds. The Court added that this right has to be refused, if the subscription of bonds seeks to circumvent the prohibition for an SPF to grant remunerated loans foreseen by the commentary to the SPF Law. The Court therefore analysed if the bonds in question meet the main characteristic of bonds, namely the collective nature of the debt and the negotiability of the bonds. The Court considered that in the case under consideration, the existence of a single bondholder, the SPF, is not prejudicial to the collective nature of the debt. The collective nature must however be denied if, as in the present case, the creditor and debtor are identical because they have the same shareholders and managers. With regard to the negotiability of the bonds, the Court concludes that the quality of the bondholders, which are members of the same family, makes it illusory that they could actually be transferred to a third party.

Finally, the Court considered that the conditions for abuse of law within the meaning of §6 of the *StAnpG* are met in the present case. It considered that the structure constituted a use of private law forms or institutions, which made it possible to circumvent or reduce the tax liability of the taxpayer. This structuring was contrary to the legislator's intention since the legislator's intention was to prohibit a civil company from issuing bonds and to prohibit an SPF to function as a financing vehicle by granting remunerated loans to other companies of the group.

The judgment illustrates the importance that the Court attaches to the fact pattern underlying a case in determining whether there has been an abuse of law. It is also worthwhile to note that the Court equated the possibility to postpone taxation until a distribution from the SPF to the shareholders, to a tax advantage that fulfils the conditions of the abuse of law provision.

## LUXEMBOURG LOWER COURT DELIVERS JUDGMENT ON THE SCOPE OF HIDDEN DIVIDEND DISTRIBUTIONS

In its judgment handed down on 25 September 2020, the Lower Administrative Court (*Tribunal Administratif*) considered the scope of hidden dividend distributions under Luxembourg law.

In the case at hand, the taxpayer (a company) had booked in its 2013 and 2014 financial accounts provisions for bonuses to be paid to its managing director (who was also the shareholder) and to the managing director's wife (who was an employee of the company), that the company had not yet paid out. The Luxembourg tax administration took the view that these bonuses were excessive compared to market practice and **sought to requalify the deemed excessive part of the provisions as hidden dividend distributions and subject them to 15% withholding tax**.

At issue was therefore (i) whether the wife, who was not a shareholder, could fall within the scope of "interested person" for the purposes of the definition of dividend distribution and (ii) whether accounting provisions could fall within the meaning of hidden dividend distributions.

The Lower Administrative Court confirmed a number of interesting points. First, Article 164(3) of the Luxembourg income tax law defines hidden dividend distributions as an advantage conferred directly or indirectly by the company to a shareholder, group company or interested person that a third party would not have received. **As regards the meaning of "interested person" the Court held that no direct relationship between the company and that person is required but that the advantage must be motivated by a shareholder interest - thus a person with sufficiently close links with a shareholder (such as a spouse) may receive a hidden dividend distribution.**

However, the Lower Administrative Court also held that, in the absence of effective payment to the intended recipient, **the provisioning of bonuses could not be lawfully qualified as a hidden dividend distribution since it did not give rise to an effective distribution, i.e. an impoverishment of the company to the benefit of a third party**. The Court acknowledged that while the provisions had diminished the company's profits, it took the view that only effective payment of the bonuses could give rise to a hidden dividend distribution. Implicit in the Court's reasoning is that the shareholder and his spouse had not in fact received an advantage from the company.

## PRELIMINARY QUESTION ON THE VAT REGIME APPLICABLE TO COMPANY CARS MADE AVAILABLE TO EMPLOYEES

On 17 September 2020, Advocate General Szpunar published his opinion in the case C-288/19 of the European Court of Justice ("**ECJ**") regarding the VAT regime applicable to the private use, by employees, of company cars.

In the case at hand, a company established in the Grand Duchy of Luxembourg had made company cars available to two employees residing in Germany for private and professional purposes. The company was subject to the simplified VAT regime, which did not allow it to deduct input VAT. The first employee was not paying any consideration for the private use of the company car, which was treated as a benefit in kind. The second employee had to contribute to the leasing costs, a portion of which were deducted from the employee's salary.

The question referred by a German court to the CJEU for a preliminary ruling was to determine whether the concept of "hire of a means of transport to a non-taxable person", referred to in Article 56 of Directive 2006/112, includes the provision of a vehicle free of charge by a taxable person to his employee for both business and private purposes. The reasoning of the Advocate General recalls that VAT applies only to transactions performed for a consideration. He concludes that the mere provision of a company car, which has not given rise to a payment or a reduction in remuneration, does not make it possible to

confirm that it is for consideration and therefore is not subject to VAT.

For completeness, and although not explicitly covered by the question referred to by the German court, the Advocate General also analysed the situation of the second employee. He concluded, first of all, that the transaction may, subject to the referring court's factual assessment whether the employee's payment actually reflected the value of the service received, be qualified as carried out for consideration and thus as falling within the scope of VAT. The taxable basis would, in the Advocate General's view, be in principle the amount of the employee's contribution to the leasing costs incurred by the company. Regarding the nature of the service, the Advocate General proposed to consider that if a vehicle belonging to its business is provided by a taxable person for the private use of one of his employees for a period of more than 30 days for consideration, the transaction should be qualified as "other than short-term hiring of a means of transport". As a result, the place of supply would be the Member State of permanent residence of the employee, potentially triggering therefore, registration and VAT collection obligations abroad for the employer in a cross-border situation.

While the Advocate General opinion is not binding for the CJEU, the CJEU tends to follow his opinions. In such case, this decision might affect the way remuneration packages offered by companies to employees, and especially to cross-border commuters, will be structured going forward.

## ECJ | CONTRACT TERMINATION FEES CONSTITUTE A SUPPLY OF SERVICES FOR CONSIDERATION SUBJECT TO VAT

On 11 June 2020, the European Court of Justice ("**ECJ**") rendered its judgment in the case '*Vodafone Portugal – Communicaçoes Pessoais SA v Autoridade Tributária e Aduaneira''* (C-43/19) following a request for a preliminary ruling. The judgment addresses the question as to whether termination fees are subject to value added tax ("**VAT**") pursuant to Article 2(1)(c) of the Council Directive 2006/112/EC of 28 November 2006 on the common system of value added tax (the "**VAT Directive**").

Vodafone Portugal supplied electronic communication services, fixed telephony, and wireless internet access. Some of the service contracts concluded with its customers included special promotions, usually related to the price payable for the contracted services, subject to conditions that tie these customers in for a predetermined minimum period ("**tie-in-period**"). In case customers fail to comply with the tie-in period, they need to pay an amount defined in the contracts. Such amount is calculated in conformity with national law in proportion to the completed part of the tie-in period, based on the benefits granted to the customers under the contract that are quantified therein. It may not exceed the costs incurred by Vodafone Portugal to install the service.

In November 2016, Vodafone self-assessed VAT based on the amounts received in respect of non-compliance with the tie-in period. In October 2017, it then challenged such self-assessment arguing that the amounts at issue were not subject to VAT. Following the rejection of the appeal, Vodafone brought an action before the Portuguese Tax Arbitration Tribunal, which then referred the preliminary question to the ECJ on the following:- in a scenario where amounts are received by an economic operator in the event of an early termination of a services contract, for reasons specific to the customer, and that services contract requires compliance with a tie-in period in exchange for granting that customer advantageous commercial conditions, should the VAT Directive be interpreted to mean that the amounts received by the economic operator must be considered to constitute a remuneration for a supply of services for consideration subject to VAT within the meaning of Article 2(1)(c) of the VAT Directive?

According to the ECJ, the amount payable in the event of early termination reflects the recovery of some of the costs associated with the supply of the services, which the operator has provided to his customers and which the latter committed to reimburse in the event of such a termination.

The Court takes on the perspective of economic reality stating that the amount due on the contract's early termination seeks to guarantee the operator a minimum contractual remuneration for the service provided. Therefore, it must be considered as constituting an integral part of the price that the customer committed to pay to the supplier to fulfil its contractual obligations. In the ECJ's view, both the service to be provided and the consideration for the right to benefit from that service are determined when the contract is concluded between Vodafone and its customers. In particular, the consideration for the service is determined according to well-established criteria, which define both the monthly instalments and the way in which the amount for early termination must be calculated. Thus, the amount due must be considered as a remuneration received by an operator for the supply of services for consideration and subject to VAT within the meaning of the VAT Directive.

## UPDATE OF EU LIST OF NON-COOPERATIVE JURISDICTIONS FOR TAX PURPOSES

On 6 October 2020, the EU Council updated its previously adopted list of non-cooperative jurisdictions for tax purposes. Said list was initially drawn up in December 2017 and updated most recently on 18 February 2020. The main change from the previous version is the withdrawal of the Cayman Islands and Oman from the list of non-cooperative jurisdictions and the addition of Anguilla and Barbados. As a result, the list currently stands as follows:

- American Samoa
- Anguilla
- Barbados
- Fiji
- Guam
- Palau
- Panama
- Samoa
- Seychelles
- Trinidad and Tobago
- US Virgin Islands
- Vanuatu

This list, which is subject to bi-annual updates, with the next update expected early 2021, serves *inter alia* as a basis, not only for certain hallmarks under the EU directive 2018/822 (DAC 6) reporting obligations (please refer to our newsletter dated 16 August 2019), but also under the draft law providing for a refusal of deductibility on payments made to non-cooperative jurisdictions for tax purposes (please refer to our newsletter dated 26 March 2020 for more details).

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