BSP Newsletter

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FINE-TUNED
LEGAL ADVICE
MADE IN
LUXEMBOURG

SUMMARY

PUBLICATION OF THE LUXEMBOURG LAW TRANSPOSING CRD V AND BRRD II

On 21 May 2021, the Luxembourg law of 20 May 2021, transposing:

- 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**)",

was published in *Mémorial A* No. 384 (the "**Law**").

In a previous newsletter published on 15 October 2020, we have set out some of the highlights of the Law.

The Law brings substantial changes to the regulatory environment, including, *inter alia*, new minimum capital requirements applicable to all institutions subject to Directive 2013/36/EU (the so-called Capital Requirements Directive) and introduces new rules on systemic risk buffers and, among others, establishes the requirement for financial and mixed financial holding companies to be approved (or exempted from approval) by their consolidating supervisor (the consolidating supervisor in Luxembourg, as the case may be, being either the European Central Bank or the CSSF).

Please find the coordinated law of 5 April 1993 on the financial sector (French and English versions), including the changes brought about by the Law here.

NEW LUXEMBOURG DRAFT LAW ON COVERED BONDS

With a view to align the national legislation with the EU legal framework on the issuance of covered bonds, the Luxembourg Minister of Finance submitted draft law 7822 (the "**Draft Law**") to the Luxembourg Parliament (*Chambre des Députés*) on 7 May 2021. If adopted, the Draft Law will result in substantive amendments to the national legal regime applicable to the issuance of covered bonds currently in force.

The purpose of the Draft Law is to:

- transpose into Luxembourg law Directive (EU) 2019/2162 of 27 November 2019 on the issue of covered bonds and covered bond public supervision (the "**Directive (EU) 2019/2162**"); and
- operationalise the Regulation (EU) 2019/2160 of 27 November 2019 as regards exposures in the form of covered bonds (the "**Regulation (EU) 2019/2160**").

BACKGROUND

Under the Luxembourg legal framework currently in force, the issuance of covered bonds (*lettres de gage*) is primarily regulated by articles 12-1 to 12-12 of the Law of 5 April 1993 on the financial sector, as amended (the "**Financial Sector Law**"). According to these provisions, the issuance of covered bonds is restricted to credit institutions specifically authorised as covered bond banks (*banques d'émission de lettres de gage*), whose range of activity is limited to mortgage and public sector lending, including funding loans purchased from other credit institutions.

More specifically, credit institutions authorised in Luxembourg as covered bond banks may issue the following types of covered bonds, with respect to the category of assets, which makes up the cover pool:

- "mortgage bonds" (*lettres de gage hypothécaires*) secured by claims resulting from loans secured by rights in rem over real estate;
- "public-sector covered bonds" (*lettres de gage publiques*) secured by claims resulting from loans to public sector entities;
- "moveable-property covered bonds" (*lettres de gage mobilières*) secured by claims resulting from loans secured by rights in rem over movable property;
- "common covered bonds" (*lettres de gage mutuelles*) secured by claims resulting from loans granted to credit institutions, which are members of a system of mutual guarantee; and
- "renewable energy covered bonds" (*lettres de gage énergies renouvelables)* secured by claims resulting from loans secured by rights in rem or charges over assets generating renewable energy.

KEY CHANGES

The Draft Law adopts a product-based approach to the issuance of covered bonds. Thus, the relevant legal provisions will be extracted from the Financial Sector Law and a separate law will be dedicated to the issuance of covered bonds.

NEW FINANCING OPPORTUNITIES FOR UNIVERSAL BANKS

Pursuant to Article 3 of the Draft Law, the issuance of covered bonds will no longer be restricted to specialised credit institutions. Henceforth, all Luxembourg banks (including credit institutions specifically authorised as covered bond banks) will be able to issue covered bonds, without a need to obtain previous authorisation as specialised covered bond banks. Thus, the current regime of specialised covered bond banks will remain in force and will apply in parallel with the new regime designed to allow universal banks to access the activity of issuance of covered bonds. However, universal banks wishing to engage in this activity must ensure that the aggregate cover asset pools linked to covered bonds will not at any time represent more than 20% of the bank's total commitments, including own funds, but deducting eligible deposits.

NEW TYPES OF COVERED BONDS AVAILABLE TO INVESTORS

As Directive (EU) 2019/2162 does not preclude the maintenance of existing national frameworks on covered bonds, insofar as they do not contradict with the EU provisions, its implementation will result in the combined application of the existing provisions on

NEW LUXEMBOURG DRAFT LAW ON COVERED BONDS

covered bonds with the provisions resulting from Directive (EU) 2019/2162. Thus, the current types of covered bonds, as described above, will continue to exist (with the exception of common covered bonds, which are being abolished), while the implementation of Directive (EU) 2019/2162 will result in the introduction of two additional types of covered bonds:

- the "European covered bonds" (*obligations garanties européennes*); and
- *the "(high-quality) European covered bonds" (obligations garanties européennes (de qualité supérieure)).*

While the "European covered bonds" and "(high-quality) European covered bonds" always qualify as covered bonds (*lettres de gage*) under Luxembourg Law, the existing types of covered bonds under Luxembourg Law may not always qualify as covered bonds for the purposes of Directive (EU) 2019/2162. This is explained by the fact that the "European covered bonds" and "(high-quality) European covered bonds" comply at the same time with the existing national legal rules on covered bonds and the additional requirements deriving from Directive (EU) 2019/2162, particularly in relation to the quality and segregation of cover pools, bankruptcy remoteness of covered bonds, the asset and liability risks affecting cover pools and disclosure of the composition of cover pools.

DRAFT LAW TO IMPLEMENT EU CROWDFUNDING REGULATION

The purpose of the draft law 7825, submitted to the Luxembourg Parliament (*Chambre des Députés*) on 21 May 2021 (the "**Draft Law**"), is to operationalise Regulation (EU) 2020/1503 of 7 October 2020 on the European crowdfunding service providers for business (the "**Crowdfunding Regulation**").

BACKGROUND

The Crowdfunding Regulation, which will be directly applicable in all Member States as of 10 November 2021, aims to foster the development of crowdfunding platforms and to establish a safe legal framework for crowdfunding activity across the EU.

The Crowdfunding Regulation, once applicable, will establish a new legal status of European crowdfunding service providers (the "**ECSPs**") and will allow ECSPs to offer cross-border crowdfunding services based on a single set of rules under the European passport mechanism.

More information on the Crowdfunding Regulation is available here.

LICENCING REGIME AND SUPERVISION OF ECSPS

As of 10 November 2021, the provision of crowdfunding services from Luxembourg will be subject to the previous acquisition of a license as ECSP. The Draft Law designates the CSSF as the competent authority for the prudential supervision of ECSPs.

In order to ensure compliance with the provisions of the Crowdfunding Regulation, the CSSF shall be vested with all necessary supervisory and investigative powers listed in Article 30(1) and (2) of the Crowdfunding Regulation, consisting mainly of:

- requesting information and documents;
- conducting investigations and on-site inspections in order to gain access to documents or other data in any form;
- suspending or prohibiting crowdfunding offers, marketing communications, as well as the provision of crowdfunding services, depending on the gravity of the infringement;
- publicising the failure of an ECSP to comply with its obligation under the Crowdfunding Regulation;
- transferring existing contracts to another ECSP subject to the agreement of the clients and the receiving ECSP in cases of licence withdrawal; and
- the transmission of information to the State Attorney, which may result in criminal prosecution.

Furthermore, pursuant to Article 20-17 of the Draft Law, if an ECSP does not comply with its obligations under the Crowdfunding Regulation or refuses to cooperate during an investigation or a request for the provision of information and documents, the CSSF shall have the power to impose the following administrative sanctions:

- a public statement indicating the name of the natural or legal person responsible for the violation, and the nature of the violation;
- an order requiring the natural or legal person to cease the conduct constituting the infringement and to desist from a repetition of that conduct;
- a professional ban on exercising management functions within an ECSP for a maximum period of five years (5) against any member of the management body of the legal person responsible for the violation or any other natural person held responsible for the violation;
- an administrative fine up to EUR 500,000 or up to 5 % of the total annual turnover as shown in the last available financial statements approved by the management body for legal persons or up to EUR 500,000 for natural persons; and
- an administrative fine which can be up to two times the benefit derived from the violation, if this can be determined, even if this amount exceeds the maximum amounts referred above.

ENHANCED INVESTOR PROTECTION

The new legal regime will result in enhanced investor protection. More specifically, investors on Crowdfunding platforms will benefit from strengthened protection as a result of the enhanced CSSF supervision and sanctioning powers and the introduction of clear rules on information disclosure and liability regime of project owners and ECSPs.

MiFID II AND MiFIR | ESMA UPDATED Q&AS ON INVESTOR PROTECTION AND INTERMEDIARIES TOPICS

On 29 March 2021 and on 28 May 2021, ESMA updated its Questions and Answers ("**Q&As**") concerning investor protection and intermediaries topics under Directive 2014/65/EU of 15 May 2014 on markets in financial instruments (“**MiFID II**”) and Regulation (EU) 600/2014 of 15 May 2014 on markets in financial instruments (“**MiFIR**”).

The updated version of the Q&As on MiFID II and MiFIR investor protection and intermediaries’ topics includes two new Q&As.

INDUCEMENTS

In Question 8 of Chapter 12 related to inducements (updated on 29 March 2021), ESMA provides guidance on the application of three important elements contained in Article 11(2) (a) of the MiFID II Delegated Directive (2017/593/EU) (the “**MiFID II Delegated Directive**”), notably:

- an additional or higher-level service;
- provided to the relevant client;
- proportional to the level of inducements received.

ESMA makes clear that the above requirements apply together with the other requirements referred to in Article 11(2) of the MiFID II Delegated Directive, which specify when an inducement can be considered as designed to enhance the quality of the relevant service to the client.

According to ESMA, an “additional” or “higher level” service requires that the quality enhancement goes beyond aspects of the firm’s organisation, or services that are legally required, or that can be considered as essential for its functioning. Thus, the provision of services consisting merely in providing regulatory documents, such as a prospectus or a KID (Key Information Document), or disclosure documents, such as costs and charges disclosures, are not considered as “additional” or “higher level” services for the purposes of justifying an inducement, because such aspects are required by law. On the other hand, the provision of educational material or services aimed at increasing the financial knowledge of the client, such as free access to trainings, seminars or conferences or access to staff bringing specific expertise on special matters, is an example of provision of quality enhancing service.

Furthermore, the “additional” or “higher-level” service should be actively and effectively offered and brought to the attention of the relevant client. At this point, ESMA makes clear that the quality enhancement can also be provided to a segment of clients, provided that this segment is sufficiently homogeneous, i.e. the quality enhancements provided must be relevant for all clients that belong to this segment.

The third element laid down in Article 11(2) (a) of the MiFID II Delegated Directive requires that the added value is proportional to the level of inducements received. ESMA emphasizes that the determining factor is the level of inducements received by the firm, rather that the client’s investment amount. In particular, all firms shall be able to demonstrate that the quality enhancements provided to the client are proportional to the level of inducements received.

Although the assessment whether a particular service complies with these elements is ultimately assessed on a case-by-case basis, ESMA considers that firms shall take into account the guidance provided in the new Q&A, in order to ensure a consistent application of the requirements.

INFORMATION ON COSTS AND CHARGES

In Question 34 of Chapter 9 related to information on costs and charges (updated on 28 May 2021), ESMA clarified that where a firm provides both investment advice and RTO/execution services related to the same transaction(s), the *ex-ante* cost and charges information to be provided to the client should cover the costs and charges associated with:

- the service, including the transaction costs to be incurred by the client if the recommended transaction were carried out; and
- the financial instrument(s).

In ESMA’s view, the requirement to inform the client about all costs and associated charges in good time before the provision of investment advice applies irrespective of whether the client will be subsequently provided with an RTO or execution service relating to the same transaction(s).

However, when both investment advice and RTO/execution services are provided, *ex-ante* cost and charges information already disclosed to the client in the context of investment advice, do not need to be provided a second time in the context of the subsequent RTO or execution service, if the following conditions are met:

- both services relate to the same transaction(s);
- both services are provided within a reasonably short time period; and
- the *ex-ante* cost and charges information is still accurate and complete at the time of the provision of the subsequent RTO or execution service.

SECURITISATION REGULATION | UPDATE OF ESMA Q&A'S

On 28 May 2021, ESMA published updates to its Questions and Answers (the "**Q&A**") 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 (the "**Securitisation Regulation**").

The following summarises ESMA's updates and modifications to the Q&A:

HOW TO HANDLE CHARACTER LIMITATIONS IN CERTAIN FIELDS - Q5.1.27

The new question 5.1.27 tackles the practical problem in relation to character limitation in a field preventing to provide the full name and description. ESMA affirmed it will consider enabling additional characters in fields where justified. In the meantime, it is suggested:

i. where the name exceeds 100 characters, to only enter the first 100 characters of the name of the entity;

ii. if the description of cashflow item (VSF4) exceeds 1000 characters, to provide the description of the cashflow item in the "Any other information Section" of the "Inside information or significant event report".

REPORTING OF GEOGRAPHIC REGION FIELDS – Q5.2.1

In question 5.2.1, ESMA addressed the need for geographical region fields to be populated with information regarding the primary obligor in case of multiple obligors. ESMA emphasised that this is still the case where the main obligor is located outside EU and a secondary obligor is located inside the EU.

OBLIGOR BASEL III SEGMENT – ARREARS 1-29 DAYS – Q5.3.21

In question 5.3.21, ESMA readdressed the question regarding the exclusion from disclosure of fully performing loans, i.e. those with zero arrears. ESMA explained that fully performing loans shall not be included in the numerator (which is the total outstanding principal amount as at the data cut-off date of the exposures of this type and in this category of arrears), but in the denominator (which is the total outstanding principal amount of all exposures of this type).

ANNEXES 5 AND 8: UNDERLYING EXPOSURES - AUTOMOBILE AND LEASING - YEAR OF REGISTRATION - Q5.7.4

In the new question 5.7.4, ESMA explained that the first date of registration should always be provided in the case of used cars.

SECURITISATION REGULATION | JOINT COMMITTEE Q&A

On 26 March 2021, the three European supervisory authorities - European Banking Authority (EBA), European Securities and Markets Authority (ESMA) and European Insurance and Occupational Pensions Authority (EIOPA), published Joint Questions and Answers (the "**Q&A**") 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 (the "**Securitisation Regulation**"). All the answers to questions in this Q&A fall outside of the exclusive competence of those three authorities and aim to promote common supervisory approaches and practices in the application of Securitisation Regulation.

The Q&A provides the following:

- a summary of the underlying documentation to have for the understanding of a transaction;
- required level of completeness of the information described in points (b), (c) and (d) of the first subparagraph of Article 7(1) of the Securitisation Regulation;
- guidance on underlying exposure documentation (such as facility agreements, intercreditor agreements, mezzanine debt documents, hedging documents) as part of Article 7(1)(b) of the Securitisation Regulation;
- guidance on the STS requirements - application of Article 21(9) of the Securitisation Regulation on transaction documentation;
- guidance on the provision of STS+ certification by third party verifier agent (TPV).

PROSPECTUS REGULATION | UPDATE OF ESMA'S Q&A

On 31 March and 5 May 2021, respectively, ESMA published updates to its Questions and Answers (the "**Prospectus Q&A**") relating to 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**") and to Commission Delegated Regulation (EU) 2019/980 of 14 March 2019 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 (the "**Supplementing CDR**"). In total, seven new questions and relating answers have been added to the Prospectus Q&A.

The following summarises ESMA's updates:

DETERMINATION OF HOME MEMBER STATE IN RELATION TO GLOBAL DEPOSITORY RECEIPTS OVER SHARES ("GDRS") – Q6.2

GDRs are generally issued by a trust or custodian, which in most cases is neither the issuer of the underlying shares nor an entity belonging to that issuer's group. Hence, the GDRs shall qualify as non-equity securities (Article 2(c) of the Prospectus Regulation) rather than equity securities (Article 2(b) of the Prospectus Regulation). In consequence, a trust or custodian shall look to Article 2(m) of the Prospectus Regulation, when determining its home Member State.

NO SUPPLEMENT TRIGGER IN CASE OF PUBLICATION OF NEW AUDITED ANNUAL FINANCIAL STATEMENTS DURING THE PERIOD OF VALIDITY OF A BASE PROSPECTUS OR A NON-EQUITY PROSPECTUS – Q8.5

ESMA confirms that, notwithstanding any of the provisions in Article 18(1)(a) of the Supplementing CDR, the publication of new audited annual financial statements during the period of validity of a base prospectus or a non-equity prospectus does not automatically trigger the obligation to produce a supplement. Whether a supplement is necessary or not shall be determined by the assessment based on its own significance/materiality in accordance with Article 23(1) of the Prospectus Regulation.

APPLICATION OF THE PROSPECTUS REGULATION IN THE CASE OF ADMISSIONS TO TRADING OF GDRS WHERE THE NUMBER OF GDRS IN ISSUE FLUCTUATES AS A RESULT OF INVESTORS EXCHANGING SHARES FOR GDRS (AND VICE VERSA) ON A CONTINUOUS BASIS – Q14.11

A person applying for admission to trading of GDRs may produce a prospectus covering the admission of an "up to" number of GDRs, which can be no more than an amount equivalent to 100% of the issued capital of the issuer at the date of the GDR prospectus. The prospectus can be used for admission(s) as long as the total number of GDRs in issue does not exceed the limit set out in the prospectus. The use of the "up to" number shall facilitate market activity in that it enables shareholders to exchange their shares for GDRs.

IMPACT OF RESTRICTIVE SHAREHOLDERS' AGREEMENTS ON THE STATUS OF SHARES AS 'TRANSFERABLE SECURITIES' – Q14.12

Overall, while the ability to transfer a security may be reduced (e.g. through a shareholders' agreement), securities offered with certain restrictions remain "transferable securities" within the definition of securities in Article 2(a) of the Prospectus Regulation and, hence, fall within the scope of the Prospectus Regulation.

However, certain restrictions may be so extensive (e.g. certain lock-up agreements) that they result in the impossibility to consider the securities in question as freely transferable. Such securities shall be considered outside the scope of the Prospectus Regulation.

CREDIT RATING DISCLOSURE IN PROSPECTUSES – Q14.13

ESMA confirms that Article 4(1) of the Regulation (EC) 1060/2009 of 16 September 2009 on credit rating agencies applies to any credit rating mentioned in a prospectus. In fact, whenever a credit rating is included in a prospectus, regardless of whether it is included pursuant to the Supplementing CDR,

PROSPECTUS REGULATION | UPDATE OF ESMA'S Q&A

'prominent and clear' information should be provided to indicate whether the credit rating is issued by a registered credit rating agency established in the EU.

CONVERSION OR EXCHANGE OF NON-TRANSFERABLE SECURITIES AND EXEMPTION FROM PUBLISHING A PROSPECTUS – Q15.4

ESMA improves clarity about the application of exemption provided by Article 1(5)(b) of the Prospectus Regulation. As defined in Article 2(a) the Prospectus Regulation only concerns "transferable securities", therefore this article does not apply to cases of non-transferable securities converted into shares.

DISSEMINATION OF AN AMENDED ADVERTISEMENT THROUGH AT LEAST THE SAME MEANS AS THE PREVIOUS ADVERTISEMENT WHERE THE ADVERTISEMENT IN QUESTION IS A ROADSHOW – Q17.1

An exemption exists where an advertisement was orally delivered as part of a roadshow. There shall be no requirement to hold a new roadshow in view of disseminating an amended advertisement. This exemption also applies to visual or printed elements used during a road show, as the overall nature of the advertisement is that it is delivered in an oral context.

This exemption shall however not mean that no dissemination of an amended advertisement shall be necessary. It shall mean instead that the amended advertisement should be disseminated through means, which the issuer/offeror/person asking for admission to trading on a regulated market considers most suitable to reach the participants of the roadshow.

CIRCULAR CSSF 21/771 | APPLICATION OF ESMA'S GUIDELINES ON DISCLOSURE REQUIREMENTS UNDER THE PROSPECTUS REGULATION

On 20 April 2021, the Luxembourg CSSF published Circular 21/771 (the "**Circular**") on the application of the guidelines of the European Securities and Markets Authority (ESMA) on disclosure requirements 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, and repealing Directive 2003/71/EC (the "**Guidelines**" and the "**Prospectus Regulation**", respectively). By way of this Circular, the CSSF informs all persons or entities subject to the Prospectus Regulation that the Guidelines, applicable since 5 May 2021, have been integrated into its administrative practices and regulatory approach.

SCOPE AND PURPOSE OF THE GUIDELINES

The Guidelines apply to competent authorities as defined in the Prospectus Regulation and to market participants, including the persons responsible for a prospectus under Article 11(1) of the Prospectus Regulation.

The purpose of the Guidelines is to help market participants to comply with the disclosure requirements set out in Commission Delegated Regulation (EU) 2019/980 (the "**Supplementing CDR**"), as well as to enhance consistency and efficiency across EU Member States in the way that the annexes to the Supplementing CDR are understood. The Guidelines furthermore promote effective supervisory convergence and practices assessing the comprehensibility and consistency of information prospectuses across the Union. A prospectus containing the necessary information for investors to make an informed assessment of the assets shall be made following the Guidelines' content.

SELECTION OF KEY CHANGES INTRODUCED BY THE GUIDELINES

The Guidelines update and replace the recommendations of the Committee of European Securities Regulators (ESMA's predecessor) and introduce the following substantive changes:

- **Integration of ESG information**

The increasing importance placed on ESG in the EU and international capital markets has led ESMA to include express reference on disclosure relating to ESG matters in the Guidelines. The Guidelines now provide for disclosure on how an issuer's earnings, cash flows, material business assets and liabilities could potentially be impacted by its non-financial objectives and strategy, facilitating an investor's assessment of the future sustainability of earnings and cash flows of an issuer.

- **Working capital**

The Guidelines put focus on the robustness of preparation and the clarity of working capital statements, which shall not be open to more than one interpretation. Distinction is made between 'clean' and 'qualified' working capital statements, i.e. whether an issuer can or cannot state without qualifying wording that it has sufficient working capital to meet its present requirements.

- **Profit forecasts, estimates and historical financial information**

The persons responsible for the prospectus shall ensure that profit forecasts and estimates are (i) understandable, (ii) reliable, (iii) comparable and (iv) relevant. Moreover, issuers shall specify whether profit forecasts and/or estimates have been audited or subject to review.

Any profit forecasts or estimates disclosed by an issuer should be comparable with its historical financial information. An issuer that intends to adopt a new accounting framework shall integrate into its prospectus the related historical financial information for their next published financial statements. Where the prospectus is required to include historical financial information for three financial years, and not all of those years of financial information are restated, the persons responsible for the prospectus shall make use of the so-called 'bridge approach', i.e. they should present and prepare the middle period under both the current and the new accounting framework and

CIRCULAR CSSF 21/771 | APPLICATION OF ESMA'S GUIDELINES ON DISCLOSURE REQUIREMENTS UNDER THE PROSPECTUS REGULATION

should present and prepare the last period only under the new accounting framework.

- **Pro forma**

The disclosure of pro forma financial information for multiple transactions undertaken by an issuer, which collectively constitute a variation of more than 25% in one or more indicators of the size of the issuer's business (i.e. its total assets, revenue or profit and loss) is compulsory, unless it is disproportionately burdensome for the persons responsible for the prospectus to produce such pro forma financial information. The determination of whether the 25% threshold is reached should be based on the size of a transaction relative to the historical financial information before such transaction took place.

HOLDING MEETINGS IN COMPANIES

EXTENSION

While the coronavirus pandemic situation continues to have an impact on the sound governance of companies and other legal entities, the Luxembourg legislator decided to extend the possibility for the companies to hold their general meetings and other necessary meetings without physical presence.

These measures were initially provided by the Grand-Ducal Regulation of 20 March 2020 introducing measures concerning the holding of meetings in companies and other legal persons and was extended several times. The latest extension enacted by the law of 23 September 2020 ceased its effect on 30 June 2021.

Hence, due to the still running pandemic situation, the Luxembourg legislator by the law of 30 June 2021 has decided to extend once again the possibility for Luxembourg-based companies to hold virtual board and shareholder meetings until 31 December 2021.

VIDEO CONFERENCE MEETINGS

Rules regarding the convening and holding of meetings for corporate organs as well as shareholders' meetings are provided in the law dated 10 August 1915 regarding commercial companies, as amended as well as the law of 24 May 2011 on the exercise of certain rights of shareholders at meetings general information of listed companies (the "**Laws**").

For various reasons, including amongst other substance or sound corporate governance, holding of physical meetings was the rule and only in restricted cases, provided in the Laws and with a necessary specific dispositions in the articles of association of companies, option was granted to hold video conference meetings or similar.

Despite the improvement of the pandemic in Luxembourg, it is fair to say that the situation is not yet solved, therefore, considering the need to provide for legal certainty to companies with respect to the possibility to hold general meetings by videoconference or written resolutions when the articles of association do not provide for such option, it was of paramount importance to extend the right to hold virtual board and shareholder meetings longer. Such right is extended until 31 December 2021.

ENTRY INTO FORCE

The law of 30 June 2021 entered into force on 30 June 2021 and shall remain in force until 31 December 2021 inclusive.

AML/CFT | EBA OPINION ON THE RISKS AFFECTING THE EUROPEAN UNION'S FINANCIAL SECTOR

On 3 March 2021, the European Banking Authority (EBA) issued its third Opinion on the risks of money laundering and terrorist financing affecting the European Union's Financial Sector (the "**Opinion**"). Both the European Securities and Markets Authority (ESMA) and the European Insurance and Occupational Pensions Authority (EIOPA) were also closely involved in the process.

Art. 6(5) of Directive 2016/849 (AMLD4) requires the EBA to issue, every two years, an opinion on the ML/TF risks affecting the EU's financial sector, and is included in its new mandate to lead, coordinate and monitor the fight against ML/TF in the financial system at the EU level.

The Opinion is based on the analysis and the findings detailed in the annexed EBA Report (the "**Report**"). Both the Opinion and the Report cover i) the nine sectors included in the EBA's scope of action (credit institutions, payment institutions, e-money institutions, bureaux de change, investment firms, fund managers, credit providers other than credit institutions, life insurance undertakings and life insurance intermediaries) and ii) cross sectoral risks.

In drafting this Report EBA took into account:

- the view expressed by the competent authorities, engaged through a questionnaire related to ML/TF risks and supervisory activities carried out in 2018 and 2019;
- a combination of data analytics software (with the specific aim to realize a cross-sectoral assessment, including risk associated with virtual currencies, new technologies – FinTech and RegTech – terrorist financing, ML/FT risks arising from the withdrawal of the United Kingdom from the UE and de-risking);
- subject-specific expert reports, needed in order to support the analysis of the information received by the competent authorities.

The aim of the Opinion is to: a) assess how the ML/FT risk has evolved since the last Joint Opinion of the European Supervisory Authorities, released on October 2019; b) to describe the risks to which both credit and financial institutions and other various sectors are exposed (cross sectoral risk); c) propose actions addressed to the competent authorities, the financial institutions.

EBA's attention focused on the impact that new technologies and assets connected with digital finance (in a broad sense) produce in terms of increasing risks.

With particular regard to the cross-sectoral risks, EBA notes that some of them have been further increased since the Joint Opinion of 2019; this is the case for virtual currencies and FinTech/RegTech Firms. In these sectors the increase of the risks is mainly due to the limited transparency of the transactions and the identity of the end customer involved and to the provision of unregulated products and services, a lack of understanding of Fintech firm's ML/TF obligations, and an over-reliance of some firms on outsourcing arrangements without adequate oversight.

In other cross-sectors the perception of the risks didn't change in any relevant way; this is the case of terrorist financing risks arising from the withdrawal of the United Kingdom from the EU, risks arising from de-risking (i.e. the decision by firms to refuse or to terminate business relationships with some categories of customers they associate with higher ML/TF risk), risks arising from legislative divergence and divergent supervisory practices (above all in sectors in which EU regulations are very young, such as the regulation on crowdfunding platforms) and tax related crimes.

Lastly, with regard to the cross-sectoral risks, EBA draws attention to the risks associated with the COVID 19 pandemic, as an example of risk that can emerge unexpectedly and that can impact firms' ability to ensure adequate AML/CFT compliance and competent authorities' ability to ensure ongoing supervision of firms in the current context of restrictions on movement.

MONEY MARKET FUNDS | CSSF COMMUNIQUE - REPORTING INSTRUCTIONS

According to Article 37 of Regulation (EU) 2017/1131 of the European Parliament and of the Council of 14 June 2017 on money market funds ("**MMFR**"), the manager of a money market fund ("**MMF**") must report certain information to the competent authority of the MMF.

On 4 May 2021, the CSSF published a "user guide concerning reporting under article 37 of the MMFR" (the "**User Guide**") and a list of "MMFR Error Codes" on its website.

The purpose of these documents is to provide MMF with an explanation on recurring problems encountered with the MMFR reporting and the full list of ESMA error messages.

The User Guide *inter alia* provides for the deadline of the submission of the MMFR reports and the entity required to submit the MMF report.

The User Guide furthermore covers some more practical and technical aspects such as how the file should be named and gives further details and explanations as to what is exactly to be included in the report.

Finally, through the User Guide, the CSSF also reminds that it is performing some verifications on the information contained and filled in in the forms.

CSSF UPDATED Q&A | APPLICATION OF MIFID II

On 10 June 2021, the *Commission de Surveillance du Secteur Financier* (the "**CSSF**") published 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 FAQ**") and an updated version of its Frequently Asked Questions concerning the Luxembourg Law of 12 July 2013 on alternative investment fund managers (the "**AIFM FAQ**").

With this update CSSF clarifies the application of the Directive 2014/65/EU ("**MIFID II**") to Luxembourg UCITS management companies and alternative investment fund managers (the "**IFMs**"), their third party delegates and their investment advisers.

PORTFOLIO MANAGEMENT

The CSSF confirmed that the management of collective funds by IFMs is not a service under MiFID II. IFMs and their UCIs are therefore exempted from the scope of MiFID II when performing the functions included in the collective portfolio management themselves. However, the exemption does not cover the functions of collective portfolio management: undertaken by an authorised IFM under a delegation arrangement from another authorised IFM or, delegated by an authorised IFM to a third party.

MARKETING

Marketing of funds is part of the functions included in the collective portfolio management. Therefore, if the authorisation of an IFM includes the marketing function, the IFM can perform the marketing for the funds under its management and this activity will benefit from the exemption.

However, if the IFM does not perform the marketing function itself, the exemption foreseen above does not apply and MiFID II rules may apply to the entity undertaking the marketing function depending on where and to whom the funds are distributed.

Where a Luxembourg IFM markets funds that are not under its management, as a delegate of another IFM, authorisation under Article 101 (3) of the Law of 17 December 2010 or Article 5 (4) of the Law of 12 July 2013 will be required (authorisation to provide discretionary portfolio management and non-core services), depending on the fund type and services offered.

INVESTMENT ADVICE

Third parties that provide investment advice relating to financial instruments are in principle subject to MiFID II rules to the extent such advice enables the IFM to take an investment decision and qualify as personal recommendations issued to a client under MIFID II.

TIMELINE

IFMs are expected to comply with the CSSF FAQ as soon as possible and by 31 December 2021 at the latest, considering the best interests of investors. Therefore, IFMs should as soon as possible analyse their organisation model in order to assess:

- the need for an authorisation to provide services under Article 101 (3) of the Law of 17 December 2010 or under Article 5 (4) of the Law of 12 July 2013;
- appropriate compliance, by any third country entity acting as their delegate or undertaking services on their behalf, with the third country regime.

BENCHMARK REGULATION | UPDATE TO ESMA'S Q&A

On 28 May 2021, ESMA published an updated version of the Questions & Answers (hereinafter the "**Q&A**") on the implementation of the Regulation (EU) 2016/1011 of 8 June 2016 on indices used as benchmarks in financial instruments and financial contracts or to measure the performance of investment funds (hereinafter referred to as the "**Benchmarks Regulation**").

Some of the key changes reflected in the updated Q&A are as follows:

I. Transitional provisions applicable to third country benchmarks – modifying the answer to Question 9.3, ESMA clarifies that the meaning of the term "*where the benchmark is already used in the Union*" in Article 51(5) of the Benchmarks Regulation is "*where the benchmark is already used in the Union on or before 31 December 2023*" and not "*where the benchmark is already used in the Union on or before 31 December 2021*" as it used to be the case before.

   This change clarifies that, in the absence of an equivalence decision as referred to in Article 30 (2) or (3) of the Benchmarks Regulation or unless an administrator has been recognised or endorsed pursuant to Articles 32 and 33 of the Benchmarks Regulation respectively, the use in the European Union by supervised entities of a benchmark provided by an administrator located in a third country is only permitted for such financial instruments, financial contracts and measurements of the performance of an investment fund that already reference such benchmark or which add a reference to such benchmark prior to, 31 December 2023.

II. Questions and Answers on EU Climate Transition Benchmarks, EU Paris-aligned Benchmarks and sustainability-related disclosures for benchmarks – ESMA included a new set of questions & answers on ESG related matters, addressing the following, inter alia, subjects:

   - It was confirmed that an administrator does not have to take into account all the ESG factors listed in Annex II of the Delegated Regulation (EU) 2020/1816 when publishing or making available an explanation of how the key elements of the methodology reflect ESG factors. An administrator only needs to provide information on those ESG factors that are taken into account in the benchmark methodology for the selection, the weighting and any exclusion of the underlying assets.
   - ESMA clarified that it does not consider that the list of ESG factors in Annex II of the Delegated Regulation (EU) 2020/1816 is an exhaustive list to be considered for the methodology and that an administrator can take into account in the key elements of the methodology additional ESG factors that are not included in that list.
   - If an administrator provides benchmarks that do not take into account any of the ESG factors listed in Annex II of the Delegated Regulation (EU) 2020/1816, it can still disclose the information on these other ESG factors in the template of the Delegated Regulation (EU) 2020/1817 detailing how these factors are taken into account for the selection, weighting or exclusion of the underlying assets. In addition, this administrator should disclose in the benchmark statement the score of these other ESG factors.
   - ESMA clarified that when a benchmark pursues ESG objectives, its administrator should provide in its benchmark statement as a minimum all the ESG factors (as well as the scores of such factors) listed in Annex II of the Delegated Regulation (EU) 2020/1816 that are not flagged as voluntary, in order to ensure the comparability of the information provided for different benchmarks and to allow investors to make informed choices.
   - On the contrary, ESMA clarified that in case a benchmark pursues ESG objectives

BENCHMARK REGULATION | UPDATE TO ESMA'S Q&A

without taking into account any of the factors listed in Annex II of the Delegated Regulation (EU) 2020/1816, then the administrator of such benchmark should nevertheless disclose the score of the list of ESG factors that are not flagged as voluntary according to said Annex, and in case the administrator discloses additional ESG factors (which are not listed in said Annex) in the key elements of the methodology used then this administrator should also disclose the score of these additional ESG factors in its benchmark statement.

- ESMA emphasised that by 31 December 2021, all benchmark administrators, with the exception of administrators of interest rate and foreign exchange benchmarks, should indicate in their benchmark statement how their methodology takes into account the target of carbon emissions or how it attains the objective of the Paris Agreement as well as disclose the elements detailed in Section 3 of Annex I of the Delegated Regulation (EU) 2020/1816.
- ESMA clarified that, as there is no identified field in the relevant template referred to in the Delegated Regulation (EU) 2020/1817 for disclosing whether a benchmark pursues ESG objectives so as to comply with Article 1 (5) of the said regulation, administrators should disclose separately in the key elements of the methodology whether they do or do not pursue ESG objectives.
- Another important clarification given by ESMA is that, in the absence of specific standards that administrators should use for the calculation of the ESG factors listed in Annex II of the Delegated Regulation (EU) 2020/1816, these standards could include, where relevant: (i) the details of the key elements of the methodology used to compute the ESG factors and the main assumptions and the precautionary principles underlying the estimations; (ii) the international standards on which the computation is based; (iii) the percentage of reported vs estimated data used for the calculation; and (iv) any specific definition used in the calculation of the ESG factors.

ESG NEW EUROPEAN COMMISSION PACKAGE OF MEASURES

On the 21 April 2021, the European Commission released a package of measures to help improve the flow of money towards sustainable activities across the European Union, in line with the European Commission Sustainable Finance Action Plan which had already implemented the Taxonomy Regulation, the Climate Benchmarks Regulation and the Sustainable Finance Disclosure Regulation (SFDR).

The 2021 package of measures aims to enable investors to re-orient investments towards more sustainable technologies and businesses. These measures will be instrumental in making Europe climate neutral by 2050. They will make the EU a global leader in setting standards for sustainable finance.

The package will include:

- **The EU Taxonomy Climate Delegated Act.** This aims to support sustainable investment by making clearer the technical screening criteria for certain economic activities. The Delegated Act provides detailed technical screening criteria for the environmental objectives of (i) climate change adaptation and (ii) climate change mitigation (Annex 1 of the EU Taxonomy Climate Delegated Act). It is expected to apply from 1 January 2022. The technical screening criteria for the other four taxonomy environmental objectives will come into effect from 1 January 2023 (requiring another delegated act).
- **A proposal for a Corporate Sustainability Reporting Directive (CSRD).** This proposal aims to improve the flow of sustainability information in the corporate world by revising the Non-Financial Reporting Directive (NRFD). It will make sustainability reporting by companies more consistent, so that financial firms, investors and the broader public can use comparable and reliable sustainability information for the benefit of investors and stakeholders. The scope will be expanded from large EU public interest entities to all large companies whether they are listed or not and without the previous 500 employees threshold. It would mean that all large companies are publicly accountable for their impact on people and the environment. In addition the EU Commission is proposing to extend the scope to include listed SMEs, with the exception of listed micro-entreprises. SMEs may then report according to standards that are simpler than the standards that apply to large companies. The European Financial Reporting Advisory Group (EFRAG) will be responsible for developing these draft standards. This proposal would ensure that companies report the information that investors and other financial market participants subject to the sustainable finance disclosure regulation (SFDR) need. This means that the reporting standards would include indicators that correspond to the indicators contained in the SFDR. The timeline will depend on how the Parliament and Council progress. If they reach agreement in the first half of 2022, the EU Commission should be able to adopt the first set of reporting standards under the new legislation by the end of 2022, which would mean that companies would apply the standards for the first time to reports published in 2024 covering the 2023 financial year.

Finally, **six amending Delegated Acts** :

1. Regarding sustainability risks and factors for UCITS, Commission Delegated Directive amending Directive 2010/43/EU as regards the sustainability risks and sustainability factors to be taken into account for Undertakings for Collective Investment in Transferable Securities (UCITS). We refer to our Sustainable Finance Newsflash Series number 5. No substantial changes have been made since then.

2. Regarding sustainability risks and factors for AIFM, Commission Delegated Regulation amending Delegated Regulation (EU) No 231/2013 as regards the sustainability risks and sustainability factors to be taken into account by Alternative Investment Fund Managers. We refer to our Sustainable Finance Newsflash Series Number 4. No substantial changes have been made since then.

3. Regarding the integration of sustainability factors into products oversight and governance, Commission Delegated Regulation amending Delegated Regulations (EU) 2017/2358 and (EU) 2017/2359 as regards

ESG NEW EUROPEAN COMMISSION PACKAGE OF MEASURES

the integration of sustainability factors, risks and preferences into the product oversight and governance requirements for insurance undertakings and insurance distributors and into the rules on conduct of business and investment advice for Insurance-based investment products. The ESG considerations mentioned in the Sustainable Newsflash Series under point 4 and 6 would also apply to insurance undertakings.

4. Regarding the integration of sustainability factors into products governance obligations, Commission Delegated Directives amending Delegated Directive (EU) 2017/593 as regards the integration of sustainability factors into the product governance obligations. We refer to our Sustainable Newsflash Series number 13.

5. Regarding the integration of sustainability risks in the governance of insurance and reinsurance undertakings, Commission Delegated Regulation amending Delegated Regulation (EU) 2015/35 as regards the integration of sustainability risks in the governance of insurance and reinsurance undertakings. The ESG considerations mentioned in the Sustainable Newsflash Series under point 4 and 6 would also apply to insurance and reinsurance undertakings.

6. Regarding the integration of sustainability factors into organisational requirements and condition for investment firms, Commission Delegated Regulation amending Delegated Regulation (EU) 2017/565 as regards the integration of sustainability factors, risks and preferences into certain organisational requirements and operating conditions for investment firms. We refer to our Sustainable Newsflash Series Number 13.

The Delegated Acts and the Taxonomy Regulation Delegated Acts, will have to be approved by the Council and the Commission before being published in the Official Journal. These six amending Delegated Acts are expected to start applying from October 2022

PERFORMANCE FEES | ESMA UPDATES UCITS AND AIFMD Q&A

Since the publication of our last newsletter in March 2021, the European Securities and Markets Authority ("**ESMA**") has updated its Questions and Answers on Application of the UCITS Directive (the "UCITS Q&A") and its Questions and Answers on Application of the AIFMD (the "AIFMD Q&A") (together the "**Q&As**"), on 30 March and 28 May. The purpose of both updates was to provide clarification on the ESMA Guidelines on performance fees in UCITS and certain type of AIFs (the "**Guidelines**") which are effective since 5 February 2021.The Guidelines provide common supervisory rules in the field of performance fees and apply to both UCITS and certain types of AIFs. Despite several amendments made to the draft text of the Guidelines following feedback received during a public consultation in the Summer of 2019, the text of the Guidelines still leaves room for uncertainties. By adding a new dedicated section to each of the Q&As, ESMA has now provided clarification on the scope of the Guidelines, whether a performance fee can be paid during the Reference Period (see below), the timeline for the application of first the Reference Period and whether the Reference Period can be reset in case of UCITS mergers.

SCOPE OF THE GUIDELINES FOR AIFS/AIFMS

The Guidelines provide that they apply to AIF managers ("**AIFMs**") which manage alternative investment funds ("**AIFs**") whose shares are marketed to retail investors except for AIFs which are:

- closed-ended;
- open-ended AIFs that are EuVECAs and other type of venture capital AIFs, EUSEFs, or implement a private equity or real estate strategy.

ESMA has now clarified that the Guidelines are applicable to European Long Term Investment Funds ("**ELTIFs**") that do not meet the above conditions.

As to which AIFMs fall into the scope of the Guidelines, it has now been confirmed that they do not apply to registered AIFMs referred to in article 3(2) of the AIFMD (so-called below threshold or *de minimis* AIFMs).

PAYMENT OF A PERFORMANCE FEE DURING THE REFERENCE PERIOD

The Reference Period is the time horizon over which the performance of a fund is measured and in case of underperformance, the time horizon over which losses shall be recouped before a performance fee can be paid. The Guidelines set such duration to at least 5 years or if the fund has a life duration of less than 5 years, to the life duration of the fund.

The Q&As provide that managers do not have to wait for the end of the Reference Period to receive a performance fee which can be paid if all the conditions provided under the Guidelines and the fund offering documentation are met. National regulators remain free to apply stricter rules and to require that the performance fee can only be paid after the end of the Reference Period. Should they do so they must ensure that this requirement does not jeopardize the rules on cross border distribution.

The Q&As also clarify when the Reference Period can be reset, *ie* the underperformances are cancelled and brought back to 0, when the performance fee is calculated on the basis of a benchmark model and concrete and illustrative examples have been inserted in the Q&As. The examples show that the reset can take place after the end of the Reference Period calculated as of the last time a performance fee was paid (N) (eg: for a Reference Period of 5 years, at N+5).

TIMELINE FOR THE APPLICATION OF THE FIRST REFERENCE PERIOD

Funds which were already compliant with the Guidelines regime before the application date of the Guidelines should look at the last years of the duration of their Reference Period to calculate their performance fee (eg: for a Reference Period of 5 years and a fund existing for more than 5 years: 5 years prior to 2021 / for a fund existing since shorter than its Reference Period: since the inception of the fund).

For funds not compliant with the Guidelines at the time they became applicable, the Reference Period should start at the beginning of the financial year when they will comply for the first time.

PERFORMANCE FEES | ESMA UPDATES UCITS AND AIFMD Q&A

RESET OF THE REFERENCE PERIOD IN CASE OF UCITS MERGERS

ESMA also clarified that a reset of the Reference Period should not be authorised in case of mergers between UCITS in case the receiving fund is a newly established fund with no performance fee and the merger does not substantially change the investment policy of the merged UCITS.

All EU and EEA regulators have now notified ESMA of their compliance or intention to comply with the Guidelines with the exception of a very limited situation for Sweden.

EST | JOINT CONSULTATION PAPER ON TAXONOMY RELATED SUSTAINABILITY DISCLOSURES

CONTEXT

On 15 March 2021, the European Supervisory Authorities ("**ESAs**") published a joint consultation ("**JC**") paper on Taxonomy-related sustainability disclosures on new regulatory technical standards ("**RTS**") regarding content and presentation of sustainability disclosures under Articles 8(4), 9(6) and 11(5) of the Sustainable Finance Disclosure Regulation ("**SFDR**") inviting stakeholders to respond to proposed changes integrating Taxonomy considerations to the SFDR regulatory technical standards ("**SFDR RTS**").

The SFDR provides detailed requirements for pre-contractual and periodic report disclosures of products promoting environmental or social characteristics and products having a sustainable investment objective. For more information on the SFDR RTS, please refer to BSP's Sustainability update of 15 March 2021. Regulation (EU) 2020/855 (the "**Taxonomy Regulation**") amended the SFDR and required that the ESAs develop additional pre-contractual and periodic disclosure requirements for products investing in economic activities that contribute to an environmental investment objective. For more information on the amendments brought about by the Taxonomy Regulation, we refer to BSP Sustainable Finance Insight Series number 7 & 8.

The central objective of the JC is to consolidate two sets of RTS: the existing draft SFDR RTS and the taxonomy-related RTS.

NEW DISCLOSURE REQUIREMENTS

The main disclosure requirements foreseen by the JC relating to taxonomy are to provide precise information on the environmental objectives to which the investment products contribute, as well as quantify the extent to which activities financed by the product are aligned with the taxonomy. The requirements on alignment reporting may be summarized as follows:

- Graphical representation of taxonomy alignment;
- Systematic and consistent use of key performance indicators (KPI) to calculate taxonomy alignment of investee companies that are non-financial undertakings;
- Statement of activities funded by the product labelled as environmentally sustainable.

In addition, the ESAs provide standardized templates for the pre-contractual and periodic disclosures in the annexes to the JC paper.

ENTRY INTO FORCE OF THE RTS

The deadline for submitting comments was 12 May 2021. The draft taxonomy-related RTS are being finalised for submission to the European Commission and are expected to enter into force at the dates foreseen in the drafts.

The JC foresees two dates of entry into force. The taxonomy-related RTS shall apply from 1 January 2022, except for regulations on reporting of value chain green house gas emissions, which apply from 1 January 2023.

The SFDR RTS will enter into force from 1 January 2022 in respect of the climate change mitigation and climate change adaptation environmental objectives.

The SFDR RTS will enter into force from 1 January 2023 in respect of the sustainable use and protection of water and marine resources, circular economy, pollution prevention and control and protection and restoration of biodiversity and ecosystems environmental objectives.

THE NEW RULES TO FACILITATE CROSS-BORDER DISTRIBUTION OF INVESTMENT FUNDS

On 21 May 2021, the Luxembourg Parliament (*Chambre des Députés*) published an amended version of the Draft Law 7737 transposing the directive (UE) 2019/1160 of the European Parliament and of the Council of 20 June 2019 amending Directives 2009/65/EC and 2011/61/EU with regard to crosborder distribution of collective investment undertakings (the "**Directive**") and amending the amended law of 17 December 2010 regarding undertakings for collective investment (the "**OPC Law**") and the amended law of 12 July 2013 related to alternative investment fund managers (the "**AIFM Law**") (the "**Draft Law**"). The Draft Law aims to transpose the Directive into Luxembourg Law. The regulation 2019/1156 of the European Parliament and of the Council of 20 June 2019 on facilitating cross-border distribution of collective investment undertakings and amending Regulations (EU) 345/2013, (EU) 346/2013 and (EU) 1286/2014 (the "**Regulations**"), for which no transposition is needed, completes the Directive. Further information on the Directive and the Regulations can be found in our previous newsletters here and here.

THE TRANSPOSITION OF THE DIRECTIVE INTO LUXEMBOURG LAW

The Draft Law proposes to implement all the provisions of the Directive with no additional clarification. The text of the Draft Law as adopted by the Luxembourg Parliament on 21 May is unlikely to change at this stage and a promulgation of the final law can be expected relatively soon, and in any cases, by the deadline posed by the Directive.

Therefore as of 2 August 2021 the following changes should be effective in Luxembourg:

- The discontinuation of marketing will move to a regulator-to-regulator procedure. Under the new regime UCITS or AIFM will notify the CSSF of their intention to stop the marketing of shares identifying the relevant Member States. Upon verification that the conditions provided by the law have been meet, the CSSF will then notify the relevant Member States regulator.
- UCITS and AIFM targeting retail investors will no longer be required to appoint local agents in the Member States where they want to market shares. The functions and services previously rendered by local agents will in the future be performed directly by the UCITS or the AIFM, who may delegate such functions.
- The CSSF will now have 15 business days to inform a UCITS or an AIFM that it should not proceed with a contemplated amendment to the marketing notification letter if it deems that the UCITS or the AIFM will no longer comply with applicable law, as a result of this change.
- The new harmonised regime for pre-marketing to professional investors will apply in Luxembourg. It will not be necessary to inform the CSSF before starting such activities. No subscriptions shall be accepted during the pre-marketing phase. The same rules will apply across the EU and Luxembourg based AIFMs will be authorised to undertake pre-marketing activities in other EU Member States within the same limits. Luxembourg based AIFMs will have to inform the CSSF within 2 weeks as of the start of pre-marketing activities that those activities are taking or took place. AIFMs which have undertaken pre-marketing activities in a Member State will not be able to rely on the reverse solicitation for a period of 18 months.

THE OTHER RULES IMMEDIATELY APPLICABLE AS OF 2 AUGUST 2021

The Regulation establishes uniform rules on marketing communications addressed to investors, the publication of national provisions concerning marketing requirements for collective investment undertakings, as well as common principles concerning fees and charges levied on fund managers in relation to their cross-border activities. It also provides for the establishment of a central database on the cross-border marketing of collective investment undertakings.

As of 2 August 2021:

- All marketing communications addressed to inves-tors must be identifiable as such and comply with

THE NEW RULES TO FACILITATE CROSS-BORDER DISTRIBUTION OF INVESTMENT FUNDS

the requirements in terms of information to include, presentation of the information and consistency with the prospectus and other specific fund documentation and with the Guidelines to be issued by ESMA on this topic. In this respect, ESMA published on 27 May 2021 the Final Report on Guidelines on marketing communications under the Regulation including the final text of the Guidelines which will apply 6 months after the publication of their translated version on ESMA's website.

- The CSSF will be authorised to require a prior notification of marketing communication to verify whether they comply with the Regulation. It is not yet known at this stage whether the CSSF will make use of this opportunity offered by the Regulation.
- Finally the amendments of the EUVECA and EUSEF regulations providing for the provisions related to pre-marketing will be effective.

PROPOSED CHANGES TO COMMENTARIES IN THE OECD MODEL TAX CONVENTION

The Working Group on Tax Conventions and Related Questions (the "**Working Group**") of the Organisation for Economic Co-operation and Development (the "**OECD**"), the subsidiary body of the OECD Committee on Fiscal Affairs in charge of the Model Tax Convention, has recently undertaken work to amend the Commentary on Article 9. The changes put forward in the consultation are expected to be included in the next update to the OECD Model Tax Convention.

BACKGROUND

The proposed changes to the OECD Model Tax Convention are designed to provide guidance on the application of Article 9 as it relates to domestic laws on interest deductibility, including laws aimed at preventing tax avoidance described in Action 4 of the OECD's base erosion and profit shifting (BEPS) project. The discussion draft includes several revisions to the commentary under Article 9 and related articles.

The Working Group invited interested parties to send their comments on this discussion draft before 28 May 2021. On 3 June 2021, the Working Group confirmed it will consider these comments as it finalizes its work in this area with the expectation that revised commentaries will be included in the next update of the OECD Model Tax Convention.

PROPOSED AMENDMENTS

To put it in a nutshell, the proposed changes to the commentary on Article 9 of the OECD Model aim at replacing paragraph 3 of the Article 9 commentary, with new wording regarding the determination of arm's length interest payments. Accordingly, in assessing whether an interest payment can be regarded as an arm's length amount, a jurisdiction should typically examine the terms and conditions of the loan agreement such as the rate of interest. It may also need to examine, based on the facts and circumstances, whether a loan should be regarded as a loan or as another kind of transaction, such as a contribution to equity capital. In this context, while making a determination as to the extent to which a loan is regarded as a loan, a jurisdiction should take into account factors discussed in its domestic laws (including judicial doctrine), or in the OECD Transfer Pricing Guidelines.

Moreover, the proposed changes further clarify that Article 9 does not deal with the issue of whether expenses are deductible when computing the taxable income. The conditions for the deductibility of expenses are a matter to be determined by domestic law, subject to the provisions of the Convention and, in particular, paragraph 4 of Article 24. Henceforth, when domestic law limits the deductibility of otherwise arm's-length payments, this would not lead to economic double taxation for purposes of paragraph 2 of Article 9 of the OECD Model Tax Convention and therefore a corresponding adjustment would not have to be made.

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

As previously detailed, *inter alia*, in our newsflash dated 19 March 2020 (as updated), the Luxembourg Government has once again found an agreement on the "exceptional measures" put in place with the Belgian, French and German Governments regarding the taxation of 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. Since then, four renewals of agreements have been signed with Belgium and France. The last ones, signed respectively on 11 and 15 June 2021, provide for an extension of these exceptional measures until 30 September 2021. The measure applying to German cross-border workers is 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 terminates the agreement.

As a reminder, the agreements signed with Belgium, France and Germany to maintain the exceptional arrangement not to take into account teleworking days linked to the COVID-19 pandemic for the determination of the social security legislation applicable to cross-border workers remain applicable until 31 December 2021 (publication dated 15 January 2021).

COURT DECISION ON THE CONCEPT OF ACQUISITION PRICE IN RELATION WITH CONTRIBUTIONS TO THE ACCOUNT 115

On 11 May 2021, the Lower Administrative Court (*Tribunal administratif*) ruled that contributions to the Account 115 should not be taken into account when determining whether the acquisition price of shares necessary to qualify for the participation exemption regime for withholding tax has been reached.

The case concerned a Luxembourg private limited company ("**Company A**") that acquired shares in a Luxembourg public limited company ("**Company B**") on 11 April 2014. On the same day, Company A made cash and in-kind contributions to Company B's Account 115. As a reminder, the Account 115 is an entry line in the equity section foreseen by the Luxembourg Standard Accounting Plan (*Plan comptable normalisé*), where contributions without the issuance of shares are to be recorded. Any contributions made by the shareholders to the company that do not take the form of a capital increase or a payment into the share premium account are recorded therein, given that no counterparty is received by the shareholder for those contributions (except the increase of value of the subsidiary) and that the contribution is definitive (i.e. no right of reclaiming the contribution until a distribution, capital reduction or liquidation occurs).

On 8 September 2015, Company A acquired additional shares in Company B. After this additional acquisition, Company A held 4.5% in the share capital of Company B. Without taking into account the contributions to the Account 115, the price that Company A paid for the shares in Company B was less than EUR 1.2 million, so that the thresholds foreseen under the participation exemption regime were not met. On 14 January 2016, Company B distributed dividends on which it withheld withholding tax. When Company A claimed the refund of this withholding tax, the relevant tax office denied the refund. Contrary to Company A's opinion, the tax office considered that the contributions to the Account 115 are not to be taken into account when determining whether the acquisition price of the shares of EUR 1.2 million has been reached to qualify for the exemption from withholding tax provided for by article 147 of the Luxembourg Income Tax Law ("**LITL**"). Company A's complaint before the Director of the Direct Tax Administration was rejected as unjustified. Consequently, Company A filed an action before the Lower Administrative Court against the decision of the Director of the Direct Tax Administration.

In its decision, the Lower Administrative Court considers that two conditions should be met by Company A in order to qualify for the exemption from withholding tax foreseen by Article 147 LITL. Firstly, Company A must have had a direct participation in the share capital of Company B. Secondly, the acquisition price of the participation in the share capital must be at least EUR 1.2 million. Even though the judges considered that first condition was met because Company A acquired shares in Company B on two occasions, they followed the position of the Direct Tax Administration and considered that the threshold of EUR 1.2 million was not reached. According to the judges, in the absence of a direct link between the price paid and the contribution to Account 115, the latter cannot be taken into consideration when determining the acquisition price of the share according to article 147 LITL.

This judgement has been perceived as surprising as the judges seem to have added a time congruence requirement to the concept of acquisition price as defined by article 25 LITL, that is not clearly foreseen. As a reminder, article 25 LITL states that the acquisition price should include not only the price directly paid to acquire an asset but also all incidental expenses incurred to bring the asset into the condition it is at the moment of valuation.

CIRCULAR ON TAX DEDUCTIBILITY OF CERTAIN EXPENSES MADE BY INDIVIDUALS

On 4 June 2021, the Director of the Luxembourg tax authorities issued circular LIR No.105/2 regarding the tax treatment of certain expenses incurred by individuals (the "**Circular**").

GENERAL TAX TREATMENT OF EXPENSES BORNE BY INDIVIDUALS

Before entering into more details as described below, the Circular recalls the general principle applicable to expenses borne by individuals under Luxembourg tax law. Indeed, expenses incurred by individuals may be deducted from their net income (such as net employment income) only when such costs are borne exclusively or quasi-exclusively to directly acquire, secure and retain the income. Such would typically be the case for specific professional clothing, contributions paid to professional chambers, etc. The term "quasi-exclusively" means the expenditure's use is at least 90% dedicated for professional purposes.

In addition, where expenses are borne partially for professional and partially for private purposes, a breakdown between the private and professional purposes of the expenditure is required to allow for the tax deductibility of said part. In cases where no breakdown is possible or where the expense is solely attributable to private purposes, the expense is considered as an expense of the taxpayer's lifestyle, and thus not deductible, even if it is made with a view to benefiting or is likely to benefit his profession or activity.

THE CONTEXT OF THE CIRCULAR

In the context of the COVID-19 pandemic, a number of employees had to incur expenses in order to work remotely as they were constrained in traveling to their professional office. Although it seems at a first glance that said expenses have been incurred for professional purposes, it does not necessarily mean that those expenses can be deemed to be exclusively or quasi-exclusively incurred for professional purposes. The Circular's main aim is to provide guidance on the tax deductibility (or not) of certain typical expenses made by taxpayers, notably with respect to computers and home office cabinets.

Besides the above, the Circular also confirms (i) the positions previously taken in a repealed circular dated 1998, according to which the procurement costs in relation to income from movable property benefiting from the tax-free tranche are deductible and (ii) the distinction between deductible professional development trainings (*Fortbildungskosten*) and the non-deductible education expenditure (*Ausbildungskosten*).

THE MAIN TAKEAWAYS OF THE CIRCULAR

- *With respect to working tools* :

The working tools specifically targeted by the Circular are computers, software and internet subscriptions, where the distinction between private and professional use is not straightforward.

With respect to personal computers, and for simplification purposes, the Luxembourg tax authorities took the position that the acquisition of a computer is always made for private use absent pertinent justification/proof of the exclusive use for professional purposes. Indeed, the Luxembourg tax authorities consider that using the computer in order to exchange private emails is by itself sufficient to bring the private use of the computer above the 10% threshold, thus denying the "quasi-exclusively" professional purposes of the computer.

In this context, the LTA also clarifies that they are not controlling the appropriateness of the expense as long as the latter was made exclusively or quasi-exclusively for professional purposes.

- *With respect to home office cabinet* :

The principle of an exclusive or quasi-exclusive use for professional purposes applies equally to maintaining a home office and thus request deductibility for e.g. procurement costs. The Luxembourg tax authorities confirmed that they will base their judgement on whether the home office is used exclusively for professional purposes on a bundle of indicators, such as the size of the home office, the separation of the home office from the rest of the taxpayers home, etc.

According to the Circular, not only the expenditure exclusively incurred for the furnishing of the home office, but also the portion of the general expenses of the taxpayers home in relation to the home office may be deducted as procurement costs (e.g. rent, utilities, maintenance costs, etc.). Please however note that taxpayers with an office at the place of work are considered as unable to deduct expenses for a home office given the availability of a work place.

COMMUNICATION OF THE EUROPEAN COMMISSION ON BUSINESS TAXATION FOR THE 21ST CENTURY

The European Commission has taken the opportunity in the post-pandemic context to publish a communication on 18 May 2021 in which it sets out its future projects in the field of taxation in the European Union. The communication contains both short and long-term measures that take into account not only the known challenges (environment, population ageing, digitalisation, etc.) but also the economic difficulties that the market is currently facing due to the pandemic.

In addition to setting out, in general terms, the policy that the European Commission intends to adopt on taxation in the coming century, the communication contains a number of more concrete measures that the Commission intends to put into practice over the next two years.

As a first step, the Commission intends to submit a legislative proposal in the course of 2022 that would oblige large companies to publish their effective corporate tax rate. The aim is to increase transparency and allow citizens to check the amount of tax paid in relation to the profit that these companies generate in Europe.

Secondly, the Commission intends to submit a proposal for the ATAD 3 Directive in the fourth quarter of 2021. The objective of this Directive would be to combat the abusive use of shell companies, i.e. companies that have no or minimal substantial presence and no real economic activity in order to reduce tax liability. In this context, the Commission intends to introduce new reporting obligations as well as limiting the tax benefits to these companies, etc.

In addition, the Commission is planning to issue a recommendation for Member States on the domestic treatment of losses, in particular to help companies that have been most economically affected by the pandemic (e.g allow loss carry-back for businesses to at least the previous fiscal year).

Furthermore, the Commission noticed that many businesses are over-indebted so that they face the risk of insolvency. In order to address this problem, the Commission intends to issue in the first quarter of 2022 a legislative proposal to address the debt-equity bias in corporate taxation, via an allowance system for equity financing.

Finally, the Commission briefly presented its project entitled "Business in Europe: Framework for Income Taxation", which aims to harmonize corporate taxation in the European Union and replaces the current project entitled "Common Consolidated Corporate Tax Base".

LOWER ADMINISTRATIVE COURT FINDS MPRS QUALIFY AS EQUITY FOR TAX PURPOSES

On 10 May 2021, the Lower Administrative Court (*Tribunal administratif*) handed down a judgment addressing (a) the equity/debt qualification for tax purposes of Mandatorily Redeemable Preferred Shares ("**MRPS**") and (b) whether a shareholding in a French *Société à Prépondérance Immobilière à Capital Variable (SPPICAV)* could qualify as an exempted shareholding for net wealth tax ("**NWT**") purposes.

MPRS

On the first question, **the Lower Administrative Court concluded that the MRPS issued by the Luxembourg company and subscribed by its sole shareholder should be qualified as an equity instrument**. The Lower Administrative Court reiterated that Luxembourg courts are not bound by the legal qualifications decided by the parties but can reclassify a transaction or instrument based on its economic and financial characteristics. The Lower Administrative Court recalled the criteria usually applied to distinguish debt and equity instruments in Luxembourg law:

- The attribution of voting rights to the lender/ subscriber;
- The exposure of the lender/subscriber to profits or losses of the issuer;
- The right to receive a liquidation dividend;
- The level of subordination of the instrument compared to equity;
- The long-term maturity date of the instrument;
- The option to unilaterally convert the instrument into capital;
- The possibility for the issuer to reimburse the instrument by issuing shares;
- The presence of a stapling clause.

In the case at hand, the Lower Administrative Court acknowledged that according to a formal analysis the MRPS had many characteristics of a debt instrument such as a fixed term maturity date and a fixed return but concluded that the MRPS should be regarded as equity for tax purposes. In particular, the Lower Administrative Court noted that **the MRPS were issued in the context of a capital increase and did not follow the usual formal requirements of a debt instrument such as a loan agreement including contractual guarantees in the event of default**. Further, the Court remarked that the taxpayer had not established that the MRPS's return rate was in line with the arm's length principle and that the company's sole shareholder was also the sole subscriber of the MRPS.

NWT

Furthermore, the **Lower administrative Court held that a shareholding in a French SPPICAV was not exempt from net wealth tax**. Luxembourg law provides that shareholdings held in companies referred to in Article 2 of the Directive 2011/96/EU of 30 November 2011 on the common system of taxation applicable in the case of parent companies and subsidiaries of different Member States (the "**Parent Subsidiary Directive**") are exempt from net wealth tax. However, the Lower Administrative Court found that since **the French SPPICAV benefits from an exemption from tax in France, it does not fall within Article 2 of the Parent-Subsidiary Directive and should therefore be included in the tax base for the determination of net wealth tax.**

G7 NATIONS AGREE TO SET A GLOBAL MINIMUM CORPORATE TAX RATE AT 15%

INTRODUCTION

On 5 June 2021, the G7 had a summit in London during which the Finance Ministers agreed on the implementation of **a global corporate minimum tax of 15%** (the "**global minimum tax rate**") as detailed in a Communiqué released shortly thereafter (the "**G7 Communiqué**").

Although the negotiation process has not yet ended, any final agreement on a global tax rate could result in **significant changes in tax policies worldwide**.

CONTEXT

Through this measure, G7 countries **aim at discouraging MNEs**, with a particular focus on digital services, **from shifting taxable revenues to low-tax countries without regard to where their sales are realized**. **Income derived from intangible sources is specifically targeted in the G7 *Communiqué*** (i.e., drug patents, software and royalties on intellectual property) as such revenues are highly volatile and a trend towards migrating them to low-tax jurisdictions is observed. Hence, by doing so, some **MNEs manage to avoid paying the higher tax rates in the countries** where they usually operate i.e., their respective home countries or the countries where their client base resides.

BACKGROUND

The Organization for Economic Cooperation and Development (the "**OECD**") has been coordinating tax negotiations **among 140 countries over the past several years on rules for taxing cross-border digital services and tax evasion, including a global minimum tax rate**.

The OECD and G20 countries aim to reach consensus on both by mid-year 2021. The OECD has estimated that the introduction of a global minimum tax rate of 15% could **allow for additional tax receipts of USD 50 billion to USD 80 billion worldwide**.

PRACTICAL IMPLEMENTATION OF THE GLOBAL MINIMUM TAX RATE

The global minimum tax rate **would apply to overseas profits**. However, G7 countries should not be bound to apply specific rules for the application of the global minimum tax rate. The sole requirement would be to **increase any MNEs' tax liabilities currently incurred in their respective residence country to the global minimum tax vis-à-vis profits deemed shifted to low-tax jurisdictions**.

The OECD stated that all G7 countries appear confident on the design of this new worldwide minimum income tax but not on the actual rate. **The G7 countries are currently facing internal pressure for a consensus around the 15% rate**.

Additionally, **numerous items still remain under discussion notably on** : whether investment funds and real estate investment trusts should be covered under the anticipated measures, the interaction of the global minimum tax rate with upcoming US tax reforms (i.e., The Made in America Tax Plan proposals) and the contemplated application date of the G7's engagement.

NEXT STEP

A G20 meeting is scheduled in Venice in the course of July 2021 to assess whether G7 can rely on broader support from the world's biggest developing and developed countries. More specifically, the G7 Communiqué included an expression of strong support for the ongoing work of the G20 through the **OECD Inclusive Framework** (i.e., **BEPS Action Plan 15 on the introduction of the multilateral instrument**), addressing the tax challenges of the digitalization of the economy. Still within the context of G20/OECD Inclusive Framework, **the G7 Communiqué related its willingness to reach an equitable solution on the allocation of taxing rights**, with market countries awarded **taxing rights on at least 20% of profit exceeding a 10% margin for the largest and most profitable MNEs**.

PROVISIONAL AGREEMENT ON PUBLIC COUNTRY-BY-COUNTRY REPORTING

CONTEXT

On 1 June 2021, public country-by-country reporting (**"CbCR"**) has been proposed as an amendment to the **Accounting Directive 2013/34/EU** (the **"Accounting Directive"**) through the introduction of a proposed directive on the disclosure of income tax information by certain undertakings and branches, commonly referred as the **Proposed CbCR Directive**. This latest proposal could mean that the publication of **Multinational Enterprises' tax information** becomes a reality.

BACKGROUND

The question of whether CbCR of multinational companies' tax affairs should be made public has been a recurrent topic in tax **debates for years**.

The **European Commission** has made a very first attempt on 12 April 2016 by proposing an amendment to the Accounting Directive. The proposal built on the Base Erosion and Profit Shifting (the "**BEPS**") work of the Organisation for Economic Co-operation and Development (the "**OECD**") and G20, in particular on **BEPS Action Plan 13 on CbCR.** In particular, the implementation of the BEPS Action Plan 13 on CbCR in the EU legal framework gave rise to **the adoption of Directive 2016/881** (the "**DAC4 Directive**") amending Directive 2011/16/EU as regards mandatory automatic exchange of information in the field of taxation. As a reminder, the DAC4 Directive requires **MNEs located in the EU** or with operations in the EU, with **total consolidated revenue equal or higher than EUR 750 million to file a CbBR** with the EU tax authorities competent in their respective EU Member State of residence.

However, the new amendment to the Accounting Directive proposed by the European Commission went beyond the **OECD/G20 BEPS standards**, requiring large multinational enterprises and stand-alone undertakings operating in the EU to draw up and publicly disclose on their website income tax information, including a breakdown of profits, revenues, taxes paid and employees per country. As a result, **the European Commission's proposal** could never go through due to the implementation of a **very long administrative and negotiating process** between the European Commission, the EU Parliament and the Competitiveness Council (the "**COMPET**").

Further to very recent developments, the Representatives of the Portuguese presidency of the EU Council have finally reached **a provisional political agreement with the European Parliament's** negotiating team on the public CbCR through the introduction of the proposed CbCR Directive.

SCOPE OF THE PROPOSED CBCR DIRECTIVE

The agreed text of the proposed CbCR Directive recalls the provisions currently foreseen under the DAC4 Directive as it **requires MNEs or standalone undertakings with a total consolidated revenue of more than EUR 750 million in each of the last two consecutive financial years**, whether headquartered in the EU or outside, **to publicly disclose income tax information in each EU Member State**, as well as in **each third country listed in Annex I of the Council conclusions on the EU list of non-cooperative jurisdictions for tax purposes** or listed for two consecutive years in Annex II of these Council conclusions.

Practical aspects of the proposed reporting

Such reporting shall take place by means of **a common EU template** and in machine readable **electronic formats**.

In order to avoid a disproportionate administrative burden on the companies involved and to limit the disclosed information to what is absolutely necessary to enable effective public scrutiny, the proposed CbCR Directive provides for a complete and final list of information to be disclosed.

The reporting will take place within 12 months from the date of the balance sheet of the financial year in question. The directive sets out the conditions under which **a company may obtain the deferral of the disclosure** of certain **elements for a maximum of five years**.

PROVISIONAL AGREEMENT ON PUBLIC COUNTRY-BY-COUNTRY REPORTING

EU Member States will have eighteen months to transpose the proposed CbCR Directive, once a dopted, into national law. Four years after the date of its transposition, the European Commission shall report on the result of the application of the proposed CbCR Directive.

NEXT STEPS

The provisionally agreed text will **now be submitted to EU Council and of the European Parliamen**t for political endorsement. If such endorsement takes place, the EU Council will adopt its position at first reading on the basis of the agreed text (subject to standard legal-linguistic scrutiny). The European Parliament should then approve that EU Council's position and **the proposed CbCR Directive should be deemed to have been adopted.**

ECJ JUDGMENT ON SCOPE OF VAT EXEMPTION FOR SPECIAL INVESTMENT FUND MANAGEMENT SERVICES

Following two preliminary references from Austrian courts, the European Court of Justice ("**ECJ**") ruled in a judgment handed down on 17 June 2021 that certain tax services and the granting of a licence for risk-management software may fall within the VAT exemption for the management of special investment funds, if these services form a distinct whole, and are specific to, and essential for, the management of special investment funds.

In the first case K (C-58/20), an investment management company, which managed a mutual fund (*fonds commun de placement*) had outsourced to a third party the task of calculating and preparing certain tax information for unitholders. The investment management company remained the tax representative of the mutual fund and filed the relevant tax information with the tax authority, based on the work of the third party.

In the second case DBKAG (C-59/20), a third party was contracted by an investment management company to provide risk management software to a mutual fund. This software was specifically adapted to investment funds and to the complex regulatory environment but required significant input from the investment management company.

First of all, the ECJ held that the requirement that a service be "distinct" did not require the service in question to be outsourced in its entirety. The fact that the management company still performed some tasks or retained some responsibility related to the outsourced service did not preclude the application of the VAT exemption.

On whether the services in question were specific to and essential for the management of investment funds, the ECJ restated that administrative or legal services, including tax compliance services, may fall within the scope of exempt services. However, the ECJ added that services, which are not specific to the activity of a mutual fund, but are simply inherent to any type of investment activity, should be excluded from the scope of the exemption.

While the ECJ did not reach a final determination on the facts of the cases, it noted that the national court should verify whether the tax services fulfilled the specific and distinct tax obligations applicable to mutual funds according to Austrian law. Regarding the grant of a software licence, the national court should verify whether the software was essential for the investment management company to perform its risk management functions as prescribed by Austrian law.

While these cases offer some welcome clarifications, a case-by-case analysis will nevertheless remain necessary to determine whether services fall within the VAT exemption for investment management services.

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