NEWSLETTER

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BANKING & FINANCE

THE LAW OF 16 JULY 2019 | IMPLEMENTATION OF EU SECURITISATION REGULATION

On 18 July 2019, the Law of 16 July 2019 (the "**New Law**") implementing, among others, 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**") was published in the Luxembourg Official Gazette.

We previously discussed the Securitisation Regulation in our January 2019 Newsletter but to give a short recap: the aim of the Securitisation Regulation is to strengthen the legislative framework implemented after the financial crisis to address the risks inherent in highly complex, opaque and risky securitisation. It was considered essential to ensure that rules would be adopted to better differentiate simple, transparent and standardised products from complex, opaque and risky instruments and to apply a more risk-sensitive prudential framework. Although being directly applicable in the Member States, the Securitisation Regulation contains certain provisions which require further transposition into national law, which Luxembourg has done pursuant to the New Law.

The New Law designates the competent authorities in Luxembourg, i.e. the CSSF and the "*Commissariat aux Assurances*" (the "**CAA**") responsible for supervising compliance with the obligation laid down in Articles 6 to 9 of the Securitisation Regulation. The CSSF is also the competent authority responsible for supervising compliance with Articles 18 to 28 of the Securitisation Regulation. The New Law empowers both the CSSF and the CAA with the supervisory and investigative powers necessary for the exercise of their respective tasks within the limitation of the Securitisation Regulation. Both authorities are granted the power to impose administrative sanctions and other administrative measures. The securitisation entity and members of its management body/ies (including natural persons) can be subject to sanctions under the New Law. The New Law also provides the right of recourse which allows the subject to challenge the decision made by the CSSF and the CAA within one month in front of the administrative court. Furthermore, it regulates the publication of sanctions.

The New Law entered into force on 22 July 2019.

MIFID II AND MIFIR | UPDATE OF ESMA Q&A & CSSF CIRCULAR

ESMA Q&A

Since our last newsletter, ESMA updated its Q&A on the Market in Financial Instruments Directive 2014/65/EU of 15 May 2014 ("**MiFID II**") and on the Markets in Financial Instruments Regulation 600/2014 of 15 May 2014 ("**MiFIR**"), on the following topics:

- Q&A on MiFID II and MiFIR transparency topics;
- Q&A on MifID II and MiFIR market structures topics; and
- Q&A on MiFIR data reporting.

The new Q&As provide clarification on the following topics:

- The use of pre-arranged transactions for non-equity instruments (Amendment to an existing Q&A);
- The hedging exemption of Article 8 of MiFIR;
- The treatment of constant maturity swaps;
- The application of the tick size regime to periodic auction systems; and
- The clarifications in relation to the requirements for submission of reference data under MiFIR. In particular, the Q&As

relate to reporting obligations for financial instruments without a defined expiry date.

CSSF CIRCULAR 19/723

On 18 July 2019, the CSSF published CSSF Circular 19/723 (the "**Circular**") transposing ESMA guidelines on the application of the definitions of commodity derivatives in Sections C6 and C7 of Annex I of MiFID II (the "**Guidelines**") into Luxembourg regulations.

The Guidelines relate to the application of the definitions of commodity derivatives and their classification under points 6 and 7 of Section C (Financial Instruments) of Annex I of MiFID II – they update the guidelines adopted by ESMA in October 2015 to adapt them to the new MiFID II regulatory framework without changing the substance.

The Circular (which repeals CSSF Circular 15/615 of 11 June 2015) entered into force on the day of its publication, 18 July 2019.

CAPITAL MARKETS

PROSPECTUS LAW | ENTRY INTO FORCE AND CSSF CIRCULAR

As anticipated in our July 2019 Newsletter, the new Luxembourg law on prospectuses (the "**New Prospectus Law**") implementing 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**") entered into force on 21 July 2019, having been published in the Official Journal on 18 July 2019.

Just in time for the entry into force of the New Prospectus Law, the CSSF helpfully published Circular CSSF 18/724 setting out technical specifications regarding the submission of documents to the CSSF under the Prospectus Regulation (the "**New Circular**") which repealed and replaced CSSF Circular 12/539 (as amended) setting out technical specifications regarding the submission of documents to the CSSF under the old prospectus law regime (the "**Previous Circular**").

The structure of the New Circular is similar to the Previous Circular in that it is composed of two parts: the first part presenting the regulatory framework governing prospectuses and the CSSF's competences and missions in that context, and the second part detailing the technical procedure governing the submission of documents to the CSSF for the purposes of approval, notification or filing in the context of offers of securities to the public and admission of securities to trading on a regulated market.

The process for filing documents with the CSSF remains largely unchanged. However, the New Circular lays out some particularities in case of a filing of a universal registration document and the CSSF has also updated its Entry Form which must be submitted with every application for approval of a registration document, universal registration document, prospectus, base prospectus, supplement, simplified registration document, simplified prospectus or simplified base prospectus.

Importantly (and as stressed by the CSSF in the New Circular), the New Circular should be read in conjunction with Delegated Regulation (EU) 2019/980 of 14 March 2019.

PROSPECTUS REGULATION | UPDATE OF ESMA Q&A

In July 2019, ESMA updated its Questions and Answers on the Prospectus Regulation (the "**PR 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**").

This new version of the PR Q&A is divided into separate subject matters as follows:

- Grandfathering/Implementation of the Prospectus Regulation
- Status of Level 3 guidance following the transition from the PD to the PR
- Updating information in an RD or URD
- Public offer
- Incorporation by reference
- Home Member State
- Financial Information
- Supplements
- Passporting
- Responsibility for a prospectus
- Final terms/base prospectus
- Derivatives, indices, underlyings & related disclosure
- Summaries
- Other

ESMA will continue to publish Questions and Answers on Prospectuses in relation to Directive 2003/71/EC (the "**PD Q&A**") for so long as prospectuses which have been

approved under that directive continue to be valid (July 2020).

ESMA will continue to analyse the PD Q&A and either update them and carry the amended version of themforward to the PR Q&A or not carry them forward. ESMA has already opted not to carry forward 28 Q&As from the PD Q&A to the PR Q&A. ESMA reasoned that, where the Prospectus Regulation sufficiently clarifies an issue or ESMA considers that the market is already aware of how a particular issue should be addressed, there is no need for further clarification in the PR Q&A.

SHAREHOLDERS' RIGHTS LAW | ENTRY INTO FORCE

The Luxembourg law of 1 August 2019 (the "**New Law**") amending the law of 24 May 2011 (the "**2011 Law**") on the exercise of certain rights of shareholders in general meetings of listed companies was published on 20 August 2019 and entered into force on 24 August 2019.

The New Law adds new provisions rather than significantly amend the provisions of the 2011 Law. Whereas the 2011 law principally established requirements in relation to the exercise of certain shareholder rights in general meetings, the New Law sets out specific requirements to encourage long-term engagement of shareholders, relating to shareholder identification, transmission of information, facilitation of exercise of rights transparency of institutional investors, assets managers and proxy advisors, executive compensation and transactions with related parties.

NEXT STEPS FOR LUXEMBOURG LISTED COMPANIES

The most immediate concern for Luxembourg listed companies subject to the New Law is to ensure compliance with the new requirements on transparency and approval of material transactions between such companies and related parties. Since the entry into force of the New Law, such transactions are subject to prior approval of the board of directors and public disclosure requirements. An internal procedure should be established by the board of directors to assess whether approval and transparency requirements apply to transactions or whether such transactions are exempt due to being carried out in the ordinary course of the company's business and under normal market conditions.

The next concern for Luxembourg listed companies subject to the New Law, in view of their next general meeting of shareholders, will be the establishment of a remuneration policy and the drawing up of a remuneration report. The vote of the general meeting on the remuneration policy and the remuneration report shall only be of an advisory nature. However, in the subsequent remuneration report, an explanation must be included as to how the advisory vote was taken into consideration.

Directors of listed companies should not delay in taking action to comply with the New Law, and should be mindful of Article 11*ter* of the 2011 Law, as amended by the New Law, pursuant to which directors shall be held jointly and severally liable for any damages resulting from the violation of their obligations under that law.

INTERNATIONAL LABOUR LAW

ILO VIOLENCE AND HARASSMENT CONVENTION, 2019 (NO. 190)

On 21 June 2019, the International Labour Organization ("**ILO**") adopted Convention No.190 concerning the elimination of violence and harassment in the world of work (hereafter the "**Convention**") and the associated recommendation No. 206 (hereafter the "**Recommendation**").

CONTENT

The Convention recognises the right of everyone to a world of work free from violence and harassment. Any such conduct that may constitute a "*human rights violation or abuse is a threat to equal opportunities and is unacceptable and incompatible with decent work*". It is the first time that the right of everyone to a world of work free from violence and harassment is clearly recognised in an international treaty.

The Recommendation is not legally binding but provides indications about how the Convention should be applied.

DEFINITION

The Convention defines violence and harassment as "*a range of unacceptable behaviours and practices, or threats thereof, whether a single occurrence or repeated, that aim at, result in, or are likely to result in physical, psychological, sexual or economic harm, and includes gender-based violence and harassment*". Gender-based violence and harassment is defined as "*violence and harassment directed at persons because of their sex and gender, or affecting persons of a particular sex or gender disproportionately, and includes sexual harassment*".

SCOPE OF PROTECTION

The Convention takes an inclusive approach and extends the protection to all workers irrespective of their contractual status, including trainees, interns, apprentices, workers whose employment has been terminated, volunteers, jobseekers and persons exercising the authority of an employer. The protection applies to the public and private sectors, the formal and informal economy, and urban and rural areas.

The scope of protection established by the Convention is particularly broad as it not only covers violence and harassment occurring in the workplace but also, in the course of, linked with, or arising out of, work.

The Convention also recognizes that violence and harassment may involve third parties.

Finally, domestic workers will also benefit from the protection established by the Convention, as it includes *"public and private spaces where they are a place of work*". Indeed, the Convention notes that domestic violence has an impact on workers and their livelihoods and lays out measures that governments, employers and workers organizations can take to support survivors of domestic violence.

POLICY FOR PREVENTING AND ELIMINATING VIOLENCE AND HARASSMENT IN THE WORLD OF WORK

Each member of the ILO who ratifies the Convention (each a "**Member**") shall adopt, in accordance with national law and in consultation with representative employers' and workers' organizations an "*inclusive, integrated and gender-responsive approach*" to prevent and eliminate violence and harassment in the world of work. The Convention elaborates on what may be included in such an approach.

PROTECTION AND PREVENTION

Each Member shall adopt laws and regulations requiring employers to take appropriate steps to prevent violence and harassment in the world of work, including gender based violence and harassment by:

- adopting and implementing, in consultation with workers and their representatives, a workplace policy on violence and harassment;
- taking into account violence and harassment and associated psychosocial risks in the management of occupational safety and health;
- identifying hazards and assess the risks of violence and harassment, with the participation of workers and their representatives, and take measures to prevent and control them; and
- providing to workers and other persons concerned information and training, in accessible formats as appropriate, on the identified hazards and risks of violence and harassment and the associated prevention and protection measures.

ENTRY INTO FORCE

The Convention is an international legally binding instrument and will enter into force 12 months after the first two Members have ratified it. We will provide further updates if, and/or when, Luxembourg opts to ratify the Convention.

INVESTMENT FUNDS

HARMONISED RULES FOR CROSS – BORDER MARKETING OF INVESTMENT FUNDS

The long expected Directive (EU) 2019/1160 regarding cross-border distribution of collective investment funds amending the UCITS Directive and the AIFM Directive (the "**Directive**") as well as the Regulation (EU) 201/1156 on facilitating cross-border distribution of collective investment funds and amending the EuVECA and the EuSEF Regulations (the "**Regulation**") were published in the Official Journal of the European Union on 12 July 2019. The objective of the Directive and Regulation is to remove barriers to cross-border distribution of investment funds and provide adequate protection to investors.

The new rules laid down by the Directive and Regulation applies to alternative investment fund managers, UCITS management companies, EuVECA managers and EuSEF managers.

Further information on the Directive and the Regulation can be obtained in the previous BSP newsletter of July 2019 .

The full application of the Regulation and the Directive will be as of 2 August 2021.

CSSF CIRCULARS 19/721 AND 19/725 ON DEMATERIALISATION OF REQUESTS TO THE CSSF

On 1 July 2019, the CSSF published Circular 19/721 (the "**Circular**") regarding dematerialisation of requests to the CSSF. The Circular establishes an eDesk portal to serve as a tool of communication between the CSSF and all Luxembourg regulated funds (UCITS, Part II UCIs, SIFs, SICARs) as well as securitisation vehicles, management companies and AIFMs. The Circular obliges all such entities to regularly consult the home page of the eDesk portal for various requests published there by the CSSF. The transmission of the required information must be performed exclusively in accordance with the instructions on the eDesk portal and other means of communication in this respect will not be accepted. An annex to the Circular contains further information on registration to the portal and opening two types of user accounts available to the in-scope entities and their employees.

On 29 July 2019, the CSSF published Circular 19/725 which extends availability of the eDesk portal and all obligations related to it to credit institutions and investment firms incorporated under Luxembourg law and Luxembourg branches of credit institutions and investment firms having their registered office in an EU country or a third country.

CSSF FAQ | SWING PRICING MECHANISM

BACKGROUND AND DEFINITION

On 30 July 2019, the CSSF published a new FAQ Document on swing pricing mechanisms which is applicable to all regulated funds (UCITS, UCIs part II and SIFs) ("**UCI**") making use of it in Luxembourg.

Swing pricing is a mechanism designed to protect long-term shareholders from dilution caused by trading costs generated by the subscription and redemption activity on the fund by other shareholders' activity.

1. ARTICLES OF INCORPORATION AND MANAGEMENT REGULATIONS

The CSSF clarified that the articles of incorporation or the management regulations of an UCI should allow adjustments to the net asset value ("**NAV**") in order to counter the dilution effects of capital activity.

2. MANDATORY INFORMATION IN THE PROSPECTUS

Any UCI using swing pricing should at least mention in their prospectus the following information:

- Details on the NAV adjustment mechanism in case of net subscriptions or redemptions;
- The use of any specific subscription/redemption threshold before the application of the swing pricing mechanism;
- The impacts and potential benefits to the investor due to the use of this mechanism;
- The maximum swing factor applicable (as a percentage of the NAV or in monetary value);
- An indication of the components underlying the swing factor;
- An indication of the decision process;
- The sub-funds of a UCI in scope of the swing pricing mechanism (this information may be shared as well through a reference to a website).

The CSSF also recommends disclosing in the prospectus that any performance fee will be charged on the basis of the unswung NAV.

3. DISCLOSURE IN ANNUAL AND SEMI-ANNUAL REPORTS

Annual and semi-annual reports should provide for a description of the swing pricing mechanism, including at least details on the NAV adjustment mechanism in case of net subscriptions or redemptions, specific subscription and redemption threshold before the swing pricing mechanism becomes applicable; and the maximum swing factor applicable.

In addition, investors should be provided with a list of sub-funds that have applied the mechanism.

4. APPLICATION OF CSSF CIRCULAR 02/77 TO AN ADMINISTRATIVE ERROR

If an administrative error (by using the swing pricing mechanism) leads to a material NAV calculation error, the procedures provided for in the CSSF Circular 02/77 should be applicable.

However, the CSSF considers that if the impact of the swing pricing mechanism error is below the materiality threshold as determined in accordance with CSSF Circular 02/77, the UCI should still be compensated when it was not protected from the level of dilution it should have been.

5. ORGANISATIONAL REQUIREMENTS

In accordance with the requirements of the laws governing UCIs, to have sound administrative and accounting procedures as well as adequate internal control mechanisms, investment fund managers should have robust policies and procedures governing the application of any swing pricing mechanism. A detailed swing pricing mechanism policy should be approved by the board of the investment fund managers and the board of the fund.

ESMA GUIDELINES ON MMF REGULATION

On 19 July 2019, the ESMA issued its final report on the guidelines on the reporting procedure to competent authorities under Article 37 of the Regulation (EU) 2017/1131 of the European Parliament and of the Council of 14 June 2017 on money market funds (“**MMF Regulation**”). These guidelines apply as of 19 September 2019.

ESMA also published on the same day its updated final report on the guidelines on stress test scenarios in relation to Article 28 of the MMF Regulation.

These guidelines are addressed to competent authorities, MMFs and MMF managers and aim to ensure the uniform application of Articles 28 and 37 of the MMF Regulation.

GUIDELINES ON REPORTING

Pursuant to Article 37 of the MMF Regulation, the manager of a money market fund (”**MMF**”) shall report information to its national

competent authority (the "**NCA**") on at least an annual or a quarterly basis.

An Implementing Regulation set out technical standards (the "**ITS**") with regard to the template to be used for such reporting.

The guidelines on the reporting procedure provide complementary guidance on the contents of the fields of such template so that managers of MMF have all necessary information to fill in the reporting template and send it to the NCA.

The guidelines cover on the one hand general principles regarding the reporting and the reporting periods, and on the other hand specifications in relation to each block of fields of the reporting template.

ESMA have confirmed that managers of MMFs will be allowed to report quarterly, even if they are subject to yearly reporting and the first quarterly reports to the NCA are due at the end of Q1 2020.

These guidelines are supplemented by related technical reporting instructions.

GUIDELINES ON STRESS TEST SCENARIOS

The updated guidelines on stress test scenarios establish common reference parameters for the stress test scenarios to be applied by the MMFs.

ESMA introduced new scenarios and factors that need to be considered in the performance of stress tests, which include hypothetical redemption levels, liquidity risks changes, credit risk, changes in the interest rates and exchange rates.

The guidelines contain new requirements on how the stress tests should be calibrated in order to establish common reference parameters of the stress test scenarios within the EU, the results of which need to be reported to the NCA.

In order to ensure that the calibration of the stress test scenarios remains adequate over the years, the guidelines will be updated on an annual basis.

These old guidelines on the stress tests for money market funds are already part of the CSSF Circular 18/696 since 20 July 2018.

UPDATE OF ESMA'S Q&A ON THE IMPLEMENTATION OF EMIR

On 15 July 2019, ESMA published an updated version of the Questions & Answers (hereinafter the "**Q&A**") on the implementation of the Regulation (EU) 648/2012 of 4 July 2012 on OTC derivatives, central counterparties and trade repositories (hereinafter referred to as "**EMIR**") following the introduction of the Regulation (EU) 2019/834 of 20 May 2019 as regards the clearing obligation, the suspension of the clearing obligation, the reporting requirements, the risk-mitigation techniques for OTC derivative contracts not cleared by a central counterparty, the registration and supervision of trade repositories and the requirements for trade repositories (hereinafter referred to as the "**EMIR Refit**"). The EMIR Refit effectively amended EMIR as of 17 June 2019 to a certain extent.

The following provides for a non-exhaustive summary of the key changes reflected in the updated Q&A:

i. General questions – Question 1 (a) was amended in order (i) to clarify that institutions for occupational retirement provision (hereinafter the "**IORPs**") can also be considered as counterparties to a derivative transaction in the context of EMIR, (ii) to clarify that the phrase 'fund managers' covers a UCITS management company, an AIFM and an authorised entity that is responsible for managing and acting on behalf of an IORP and (iii) to clarify that for the purposes of reporting to the trade repositories (hereinafter the "**TRs**"), the fund manager must report to TRs on behalf of funds
ii. OTC questions – Question 17 on the frontloading requirement was deleted, as

frontloading is no longer a requirement under the EMIR Refit

iii. OTC questions – Question 20 (b) was amended to reflect the new conditions under which a swap which results from the exercise of a swaption is subject to the clearing obligation when both the swap and the corresponding swaption are entered into on or after the date on which the clearing obligation takes effect

iv. TR – Question 4 on the backloading requirement was deleted, as backloading is no longer a requirement under EMIR Refit

v. TR – Question 13 was amended in order to clarify that intragroup trades are not subject to the relevant reporting obligations where at least one of the counterparties is a non-financial counterparty or would be qualified as a non-financial counterparty if it were established in the European Union

vi. TR – Question 39 was amended to clarify that the fund manager must report to the relevant trade repository on behalf of the individual fund, where the block trade was concluded by a fund manager and then allocated to individual funds

vii. TR – a new Question 52 has been inserted into the Trade Repository section concerning the notional amount field for credit index derivatives

Changes (i) and (vi) will take effect as of 18 June 2020.

ESMA FINAL REPORT | GUIDELINES ON LIQUIDITY STRESS TESTING IN UCITS AND AIFS

On 2 September 2019, ESMA published the Final Report on the Guidelines on liquidity stress testing in UCITS and AIFs (hereinafter the "**Guidelines**"), taking into account the feedback received by ESMA's earlier consultation paper further to the recommendations by the ESRB in April 2018 in introducing minimum standards for liquidity stress testing (hereinafter "**LST**") in AIFs and UCITS funds in Europe. The Guidelines, expected to apply as of 30 September 2020, provide clarifications and guidance on LTS practices to managers of AIFs and UCITS (hereinafter the "**Managers**"), depositaries and EU national competent authorities (hereinafter the "**NCAs**").

ESMA expects that the Guidelines will ensure overall lower liquidity risk in the broader financial market and strengthen the ability of relevant entities to manage liquidity in the best interests of the investors, by ensuring common, uniform and consistent standards, approach and practices with respect to LST. ESMA further anticipates that any initial and ongoing cost to be incurred by the managers by virtue of implementing the Guidelines will be balanced by the reputational and other benefits which arise from improved liquidity management when minimum LST standards are met.

The Guidelines, aimed to be adapted depending on the nature, scale and complexity of the managed fund at stake, provide for a list of non-exhaustive recommendations and suggestions to the Managers, inter alia:

- possible determining factors to be taken into consideration when designing LTS models and how Managers can overcome limitations with respect to the availability of data;
- LST to be properly integrated and embedded into the fund's risk management framework supporting liquidity management and be subject to appropriate governance and oversight, including appropriate reporting and escalation procedures;
- LST to be documented in a dedicated LST policy, which in turn be subject to periodical review and adaptation, if necessary;
- LST to be carried out on an annual basis at all times and preferably on a quarterly basis, unless a higher or lower frequency is justified by the characteristics of the fund at stake;

- how LST can be best adapted to and customised for each managed fund;
- possible LST scenarios to be taken into account (i.e. rising interest rates, credit spread widening or political events) and how consequent LST outcomes can be interpreted and hence prepare Managers for a potential crisis; and
- the incorporation of scenarios relating to the liabilities of the fund, the risks factors related to the investor type and concentration.

Furthermore, the Guidelines suggest that depositaries should set up appropriate verification procedures to check that the relevant Manager has in place documented procedures for its LST programme and that NCAs can request the submission of a Manager's LST to help demonstrate that a managed fund will be likely to comply with applicable rules, including regarding the ability of the fund to meet redemption requests in normal and stressed conditions.

The Guidelines must now be translated into each of the official languages of the European Union and then published on ESMA's website, taking effect two months after the publication. NCAs must within two months as of the publication of the Guidelines in all EU official languages notify ESMA as to whether they intend to comply with the Guidelines, and if not, the reasons for non-compliance.

THE PAN-EUROPEAN PERSONAL PENSION PRODUCT REGULATION

BACKGROUND

According to the Press Release of the European Commission on Pan-European Personal Pension Products, only 27% of Europeans between 25 and 59 years old have currently enrolled themselves in a pension product. This is the context in which the Regulation (EU) 2019/1238 of 20 June 2019 on a pan-European Personal Pension Product (the "**PEPP Regulation**") entered into force on 25 July 2019.

The PEPP Regulation aims to provide for the creation of a pan-European personal pension product ("**PEPP**") which will have a long-term retirement nature taking into account environmental, social and governance factors and will offer EU citizens an additional opportunity to save for their retirement.

A PEPP, defined as "*an individual non-occupational pension product subscribed to voluntarily by a PEPP saver in view of retirement*" shall only be complementary to public pension systems. Early withdrawal of capital should be limited and might be penalised.

CONTRACTUAL FRAMEWORK

A PEPP will be provided by an eligible financial undertaking, and subscribed to by a PEPP saver, or by an independent PEPP savers association on behalf of its members, in view of retirement, and will have no or strictly limited possibilities for early redemption.

The PEPP contract between the saver and the provider shall include a large amount of information relating to costs and fees, the investment option, alternative investment options, retirement benefits and portability options.

REGISTRATION REQUIREMENTS

A PEPP may only be provided and distributed once it has been registered in the central register kept by the European Insurance and Occupational Pensions Authority. Only financial undertakings such as credit institutions, insurance undertakings, institutions for occupational retirement provisions, investment firms, investment companies or management companies authorised pursuant to Directive 2009/65/EC and AIFMs are allowed to submit an application for registration of a PEPP to their competent authorities.

Once the national competent authority has granted its authorisation, the PEPP will be registered in a central public register and the

registration will be valid in all Member States, subject to the PEPP having notified the host Member State of its intention to open in the host Member State a sub-account.

BENEFITS OF THE NEW PEPP RULES FOR PEPP PROVIDERS

PEPP providers will be able to distribute PEPPs that they have created and, in certain cases, PEPPs that they have not created within the territory of a host Member State under the freedom to provide services or the freedom of establishment.

PORTABILITY

PEPP savers shall have the right to use a portability service which gives them the right to continue contributing into their existing PEPP account, when changing their residence to another Member State. Within three years of the date of application of the Regulation, each PEPP provider shall offer national sub-accounts for at least two Member States upon request addressed to the PEPP provider.

CONSUMER PROTECTION

The PEPP Regulation foresees strong consumer protection. PEPP savers have to be provided with a key information document (the "**KID**") before the conclusion of the PEPP contract. The PEPP KID should replace and adapt the key information document for packaged retail and insurance-based investment products under Regulation (EU) 1286/2014 of 26 November 2014 on key information documents for packaged retail and insurance-based investment products ("**PRIIPs**") which, as a consequence, would not have to be provided for PEPPs.

General advice and personalised pension benefit projections for the recommended product shall also be provided to the PEPP saver, allowing it to make a clear and appropriate judgement of the product before entering into a contract with a service provider.

PRIIPs ASSESSMENT REQUEST FROM CSSF

On 1 July 2019, the CSSF issued press release 19/28 (the "**Press Release**") relating to an assessment of the impact of Regulation (EU) 1286/2014 of the European Parliament and of the Council of 26 November 2014 on key information documents for packaged retail and insurance-based investment products (the "**PRIIPs**") on SIFs, SICARs and Part II UCIs.

To this end, all SIFs, SICARs and Part II UCIs are obliged to fill in an online assessment form available on the CSSF's eDesk portal (the "**PRIIPS Assessment**"). The PRIIPs Assessment replaces the previous document named "Self-assessment confirmation on exclusive professional investor status for the purposes of Regulation EU 1286/2014 on PRIIPs". Nevertheless, the entities which have completed the previous self-assessment are not exempted from the requirement to fulfil the PRIIPS Assessment and should do so via the eDesk portal by 31 October 2019. Instructions as to the method of transmission of the required information as well as a dedicated user guide are available at the home page of the eDesk portal.

In the Press Release, the CSSF indicated that the PRIIPS Assessment will be initially available to central administrators and would be opened to management companies and other concerned entities at a later stage. At the point of drafting, the PRIIPS Assessment is available to all in-scope investment vehicles as well as credit institutions and investment firms as further described in CSSF press release 19/39 dated 29 July 2019.

CSSF UPDATED FAQs | OBLIGATIONS OF PROFESSIONAL SECRECY

On 2 September 2019, the CSSF updated the below sets of frequently asked questions (the "**FAQs**") for the purposes of, adding a new

question regarding obligations to be complied with in case of data transfers by a central administration or a depositary to another service provider:

a) Frequently Asked Questions concerning Specialised Investment Funds ("**SIFs**") under the Luxembourg law of 13 February 2007 and Investment Companies in Risk Capital ("**SICARs**") under the Luxembourg law of 15 June 2004 that do not qualify as Alternative Investment Funds ("**AIFs**");
b) Frequently Asked Questions concerning the Luxembourg Law of 12 July 2013 on alternative investment fund managers as well as the Delegated Regulation (EU) 231/2013 of 19 December 2012 with regard to exemptions, general operating conditions, depositaries, leverage transparency and supervision; and
c) Frequently Asked Questions concerning the Luxembourg Law of 17 December 2010 relating to undertakings for collective investment ("**UCITS**").

The FAQs emphasize the need for a service provider (hereinafter the "**Service Provider**") acting as the central administration or depositary bank to obtain the prior consent from the board of directors of the relevant fund or its management company or AIFM for further outsourcing certain assigned services (hereinafter the "**Client Consent**"). The Client Consent should refer to the Service Provider's services to be outsourced, the scope of data to be transferred in light of such outsourcing arrangement as well as the country of establishment of such outsourcing third party(ies) pursuant to Article 41 (2a) of the Law of 5 April 1993 on the financial sector, as amended.

Prior to granting such Client Consent to the Service Provider, it is vital for the relevant fund's investors to have consented to the prospective transfers of their personal and confidential data in advance

(i) through an explanatory letter by the fund to each of their existing investors including a possibility to object to such transfer within a reasonable timeframe,
(ii) through informative provisions to this end within the relevant subscription documents or the offering memorandum for future investors,
(iii) by modifying the prospectus at the first available occasion.

Before outsourcing the services, the Service Providers should obtain the commitment of the relevant fund or management company, where relevant, that investors have been informed of and consented to the transfer of their personal and confidential data.

BSP

TAX

HIDDEN DIVIDEND DISTRIBUTIONS AND TRANSFER PRICING REPORTS

In a recent decision (No. 42043C dated 17 July 2019), the Higher Administrative Court (*Cour Administrative*) ruled that the tax administration is entitled to requalify interest payments into a hidden distribution, if a taxpayer is not able to provide sufficient supporting documentation proving that transactions between related parties are taking place according to the arm's length principle.

In the case at hand, a Luxembourg company held a real estate asset in France and refinanced a bank loan through a shareholder loan granted by its sole shareholder. The activity of the company was limited to the holding of this sole property. The shareholder loan was neither secured nor guaranteed with collateral and carried a fixed interest rate of 12%. The representatives of the Luxembourg company asked two service providers to determine an arm's length interest rate on said loan. The first expert determined that an arm's length interest rate would be in the range of 3.21% to 7.88% per year by using the "CUP" method and the second report, prepared during the litigation phase, determined that the arm's length interest rate would be in a range between 9.95 and 19.61% by using the "Capital Asset Pricing Model" and taking into account the subordination of the shareholder loan to a bank loan.

The tax authorities on the other hand determined the applicable interest rate based on the LIBOR rate increased by a spread linked to the subordination of the lender, which seems to be a "standard spread" ranging between 0.5% and 2%, which lead to a final interest rate of 3.57%. Indeed, in a previous decision (No. 23053C dated 13 June 2007), the same spread was used by the tax authorities, despite the fact that taxpayers in both cases had different activities and probably different risk profiles. In the framework of the litigation, the tax authorities or the government representative had not provided any additional details or insights on the determination of the spread applied on the LIBOR. The Higher Administrative Court nonetheless followed the tax authorities' position, based on the fact that (i) the first transfer pricing report did not support the interest rate applied by the taxpayer and actually included the interest rate used by the tax authorities in the arm's length range and (ii) the second transfer pricing report used comparable transactions that were not sufficiently similar to the situation of the company.

In conclusion, while certain taxpayers are still coming to terms with the obligation to maintain proper transfer pricing documentation, the Higher Administrative Court demonstrated that it is not the existence of a transfer pricing study (or two) that is the relevant aspect, but rather the quality and adequacy of the comparable used. The fact that the interest expenses were in any case non-deductible as they were in direct economic relationship with a real estate asset located in a country with which Luxembourg concluded a double tax treaty that prevents Luxembourg from taxing the income deriving therefrom, does not prevent the requalification of the excessive part of the interest into hidden dividend distributions should also not be doubted anymore.

CIRCULAR ON THE NEW IP TAX REGIME

Following the adoption of the new law on the Intellectual Property Tax Regime ("**IP Regime**") on 22 March 2018 (please refer to our March 2018 newsletter on that topic), the Luxembourg Tax Administration published on 28 June 2019 Circular L.I.R. n° 50ter/1 clarifying the application of the IP Regime.

Guidance has been provided especially with regard to the application of the nexus ratio, the

foreign tax credit, adjustments of the eligible net asset income, the compensation mechanism as well as qualifying costs under the IP Regime. With regard to the compensation mechanism allowing to determine the new eligible adjusted and compensated IP income, the Circular provides guidance on specific cases such as cases where one of the eligible assets realises a negative adjusted net income and at least one other eligible asset generates a positive income.

With respect to the qualifying costs, the Circular provides a list of what could constitute qualifying costs, such as salary costs of researchers and their support staff, acquisition costs of required instruments and equipment or costs related to the building of prototypes.

Finally, the Circular emphasises that taxpayers will need to provide detailed supporting documentation regarding the eligible expenditures, total expenditures, and eligible income in relation to each qualifying IP right (family or products or services in certain specific cases).

Finally, the Circular also provides guidance on the specificities related to the transition from the previous tax regime into the new IP Regime. Taxpayers concerned should carefully consider if and when to transition from one regime to the other, if possible, as such a choice is irrevocable.

JUDGMENT OF THE HIGHER ADMINISTRATIVE COURT ON HIDDEN DIVIDEND DISTRIBUTIONS

By judgement dated 31 July 2019 (No. 42326C), the Luxembourg Higher Administrative Court (*Cour Administrative*) reiterated its interpretation of Article 164 of the Luxembourg income tax law regarding hidden dividend distributions.

In the matter at hand, the taxpayer, a Luxembourg resident company for the tax years in question (2013 and 2014) who since migrated to Malta, had waived receivables it held towards its subsidiaries. In addition thereto, the taxpayer had booked value adjustments on its shareholding in three other subsidiaries.

The aforementioned transactions had been requalified by the tax authorities as hidden dividend distributions, based on the mere assumption that these transactions would not be justified by economic reason. The consequence was thus that the tax deduction derived from those expenses was rejected and added back to the tax base of the company. In addition, the tax authorities applied a withholding tax on the hidden dividend distribution. The case was brought first to the Lower Administrative Court (*Tribunal Administratif*), which ruled in favour of the tax authorities and which ruling the taxpayer appealed.

The Higher Administrative Court first recalled that the burden of proof in matters of hidden dividend distributions lies with the tax authorities. It is only once the tax authorities have brought sufficient elements in order to demonstrate that a hidden distribution occurred, that the burden of proof is shifted to the taxpayer who can then rebut the findings and arguments of the tax authorities. The Higher Administrative Court added that, without denying that the above-mentioned transactions may legitimately lead the tax authorities to request additional information, the fact remains that the justifications provided by the taxpayer, even if only partially complete, are likely to justify the economic reality of the transactions at hand. As a result, the Higher Administrative Court confirmed the absence of hidden dividend distributions in the case at hand.

In conclusion, the Higher Administrative Court once again reiterated that hidden dividend distributions cannot be merely alleged by the tax authorities, but that an obligation lies on the tax authorities to proceed to a diligent analysis of the facts brought by the taxpayer. The mere unconventional appearance of a

transaction does not replace the need for said diligent analysis of all facts and circumstances.

INPUT VAT ON FEES RELATING TO THE INVESTMENT OF DONATIONS AND ENDOWMENTS

On 3 July 2019, the ECJ published a judgment (C‑316/18 *University of Cambridge* v *HMRC*) clarifying whether input VAT relating to fees, paid by a not-for-profit educational establishment in the context of the investment of donations and endowments in a fund, may be deducted. The case concerned the University of Cambridge, which finances itself in part through donations and endowments, which are placed into a fund with the aim of generating resources. That fund is managed by a third party. In March 2009, the University of Cambridge submitted a claim requesting the deduction of the VAT relating to the fees paid for the management of the relevant fund, arguing that the income generated by that fund had been used to finance the whole range of its activities, including not only educational services, but also VAT taxable operations such as, for example, the sale of publications, advice and lease of material and installations. The Commissioners rejected that claim on the ground that the costs were directly and exclusively attributable to the investment activity, which does not fall within the scope of VAT.

In this context, the ECJ was requested to clarify whether input VAT, paid in respect of the costs associated with the investment of donations and endowments in a fund with the aim of generating resources intended to finance the whole range of activities of an educational establishment, is deductible.

In its response, the ECJ recalled that Article 168 of the Directive 2006/112/EC of 28 November 2006 on the common system of value added tax (the "**VAT Directive**") clearly provides that the right to deduct arises only in so far as the goods and services are used for the purpose of taxable transactions. By way of exception, a taxable person also has a right to deduct even where there is no direct and immediate link between a particular input transaction and a taxable output transaction, if the costs of the goods or services in question are part of his general costs and are, as such, components of the price of the goods or services which he supplies.

However, in the case at hand, the ECJ found that the donations and endowments were not consideration for any economic activity. The investment of the donations and endowments may be directly linked to their collection and, consequently, was considered a direct continuation of that non-economic activity by the ECJ.

The ECJ conceded that costs which are incurred in the context of a non-economic activity may give rise to deduction to the extent these costs are incorporated into the overall price of goods and services provided by the taxable person in the context of its economic activity. However, given that the costs at issue were used to generate resources, financing all of that university's output transactions, thus allowing the price of the goods and services provided by the latter to be reduced, the ECJ concluded that those costs cannot be considered to be components of those prices and, consequently, do not form part of the taxpayer's general costs.

NEW ECJ DECISION ON THE ABUSE OF LAW IN THE CONTEXT OF VAT

In a judgment handed down on 10 July 2019 (C-273-19, *SIA Kuršu zeme*), the European Court of Justice ("**ECJ**") ruled that, in case of a chain of successive supplies of goods, the fact that the final purchaser acquired possession of the goods in the warehouse of a person forming part of the chain that does not appear on the invoice as the supplier, is not in itself sufficient to conclude that the transaction is abusive. The underlying factual situation

concerned goods sold by a Lithuanian company, Baltfisher, to two Latvian companies. The same goods were then sold to another Latvian company and finally acquired by the plaintiff, Kuršu zeme (the "**Buyer**"). The Buyer arranged for transport of the goods from Lithuania to its factory in Latvia. Not having been able to find any logical explanation for that chain of transactions, the Latvian tax authorities considered them as a sham. They therefore concluded that the Buyer had in practice acquired the goods at issue directly from Baltfisher and treated the acquisitions at issue as intra-Community acquisitions. As a consequence, deduction of the input VAT paid by the Buyer to the Latvian intermediary supplier was denied.

In its judgment, the ECJ first recalls the fundamental nature of the input VAT deduction right. Further, the ECJ points out that, by way of exception, VAT authorities may refuse the right of deduction, if they establish, on the basis of objective evidence, that the right of deduction is invoked in a fraudulent or abusive manner. The tax authorities must thus establish that, (i) despite the formal application of the conditions laid down in the VAT legislation, the taxable person obtains a tax advantage, contrary to the objective pursued by the VAT legislation and that, (ii) on the basis of objective elements, the essential purpose of the transaction constitutes the obtaining of that tax advantage.

In the present case, the ECJ concludes that the Latvian VAT authorities had not established the tax advantage that Kuršu zeme or any other entity involved in the transaction chain would have received. In the absence of any such evidence, the input VAT deduction right could not be denied to the taxpayer.

Finally, the ECJ recalls that in case of a chain of supplies involving a single intracommunity transport, only one supply will qualify as an exempt intracommunity supply of goods. The national jurisdictions should determine which of the successive supplies must be treated as an exempt intracommunity supply on the basis of the factual circumstances. In case the last supply qualifies as intra-Community transaction, the final purchaser will not be able to deduct any VAT unduly charged by and paid to the supplier. Nonetheless in such circumstances, the purchaser must be able to claim a refund of the unduly paid VAT from his supplier or, if reimbursement by the supplier is impossible or excessively difficult, from the tax authority to which the VAT has effectively been paid.

ENTRY INTO FORCE OF THE US - LUXEMBOURG DOUBLE TAX TREATY

On 9 September 2019, the Luxembourg Finance Minister Pierre Gramegna and the United States ("**U.S**.") Ambassador to Luxembourg exchanged ratification instruments of the Protocol amending the Double Taxation Convention between Luxembourg and the United States, thereby bringing into force the Protocol.

This Protocol, which was agreed in 2009, replaces Article 28 concerning exchange of information with one that follows the OECD Model Tax Convention and the U.S. Model Income Tax Convention.

The new exchange of information article allows the U.S. and Luxembourg's respective tax authorities to request information regardless of whether the state from whom the information is requested needs the information for its own tax purposes and that such request cannot be declined solely because the information is held by a bank or other financial institution.

The amended double tax treaty applies to requests for information made on or after the date of entry into force and concerning the tax years beginning on or after 1 January 2009.

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