Newsletter

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SUMMARY

CAPITAL MARKETS

EUROPEAN COMMISSION PROPOSAL FOR REVISION OF THE SHAREHOLDER RIGHTS DIRECTIVE

On April 9th 2014, the European Commission published a proposal for the revision of Directive 2007/36/EC (the "Shareholder Rights Directive") with a view to tackling corporate governance shortcomings relating to listed companies and their boards, shareholders (institutional investors and asset managers), intermediaries and proxy advisors (i.e. firms providing services to shareholders, notably voting advice).

The proposed revisions to the Shareholder Rights Directive are aimed at enhancing long-term sustainability of listed companies in the EU and creating an attractive environment for shareholders. Key elements of the proposal include stronger transparency requirements for institutional investors and asset managers on their investment and engagement policies in addition to a framework to make it easier to identify shareholders. The proposals would make it easier for shareholders to use their existing rights over companies and enhance those rights where necessary.

One of the main revisions includes a proposal for a European "say on pay" policy that would require each listed company in the EU to put its remuneration policy to a binding shareholder vote every three years. This proposal aims to address what is seen as currently an insufficient link between management pay and performance which can encourage harmful short term tendencies.

Once the remuneration policy has been approved by shareholders, a company would not be permitted to pay remuneration to directors other than in accordance with that approved policy. Shareholders would also have the right to vote on a company's remuneration report, which would describe how the remuneration policy had been applied in the last year. The vote on the remuneration report would be an advisory-only vote and not binding.

While no binding cap on executive remuneration at an EU level is proposed, the remuneration policy would nonetheless need to set a maximum level for executive pay. Companies would also have to outline how their remuneration policy contributes to their long-term interests and sustainability, and how the pay and employment conditions of employees were taken into account when setting the policy including explaining the ratio between average pay of full-time employees and that of executives. The policy could in exceptional circumstances refrain from referring to such a ratio but in such a case would have to explain why no such ratio had been included and what equivalent measures have been implemented.

Other proposals include:

- That certain related party transactions would obligatorily have to be put to a shareholders' vote;
- That proxy advisors adopt and implement adequate measures to guarantee that their voting recommendations are accurate and reliable;
- That intermediaries offer to listed companies the possibility to have their shareholders identified.

The Commission's proposal is available at: http://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52014PC0213&from=EN

PROSPECTUS DIRECTIVE – ECJ JUDGEMENT

A request for a preliminary ruling regarding Directive 2003/71/EC on the prospectus to be published when securities are offered to the public or admitted to trading, as amended (the "Prospectus Directive") was filed with Court of Justice of the European Union ("ECJ") by Hoge Raad der Nederlanden (the Supreme Court of the Netherlands) on October 3rd 2012. The request concerned proceedings between Dutch companies Almer Beheer BV and Daedalus Holding BV ("Almer and Daedalus") and Van den Dungen Vastgoed BV and Oosterhout II BVBA; it related to the claim by Almer and Daedalus that the enforced sale of securities held by them should be subject to the obligation to publish a prospectus.

A preliminary ruling was requested on two questions of interpretation under the Prospectus Directive (specifically concerning Article 3(1) and Article 1(2)(h)):

1. Must Article 3(1) of the Prospectus Directive be interpreted as meaning that the obligation to publish a prospectus laid down therein is also applicable in principle (that is to say, apart from the exemptions and exceptions for certain cases referred to in that directive) to an enforced sale of securities?
2. If the answer to Question 1 is yes, (a) should the concept of "the total consideration of the offer" used in Article 1(2)(h) of the Prospectus Directive then be interpreted as meaning that the sums deriving from an enforced sale of securities must be those reasonably to be expected, with due regard for the particular nature of an enforced sale, even if the sums reasonably to be expected are well below the real economic value? (b) If the answer to Question 1 is yes, but the answer to Question 2(a) is no, how should "the total consideration of the offer" referred to in Article 1(2)(h) of the Prospectus Directive be construed, particularly in the case of an enforced sale of securities?

In respect of the first question, the Second Chamber of the ECJ considered the objectives of the Prospectus Directive and concluded, for various reasons, that a sale of securities in the context of enforcement does not form part of the objectives of the Prospectus Directive and, accordingly, does not fall within the scope of that Directive.

Therefore, the ECJ ruled on September 17th 2014 that "Article 3(1) of Prospectus Directive must be interpreted as meaning that the obligation to publish a prospectus prior to any offer of securities to the public is not applicable to an enforced sale of securities, such as that at issue in the main proceedings".

As the answer to Question 1 was negative, the ECJ did not need to answer Question 2. However it is interesting to note Advocate General Sharpston's view on Question 2, which she expressed in her opinion delivered on June 19th 2014. In short, she concluded that the Prospectus Directive "does not apply to a situation in which securities are to be sold by auction in order to raise a sum which is known in advance to be below the threshold of EUR 5,000,000 laid down in Article 1(2)(h) of the Prospectus Directive".

The ECJ judgment in this case (C-441/12) is available at the following link: http://eur-lex.europa.eu/legal-content/EN/TXT/?qid=1411120460179&uri=CELEX:62012CJ0441.

The opinion of Advocate General E. Sharpston is available at the following link: http://eur-lex.europa.eu/legal-content/EN/TXT/?qid=1411460631236&uri=CELEX:62012CC0441.

UNCERTAINTIES ON DEFINITION OF FX FINANCIAL INSTRUMENTS

On July 23rd 2014 the European Commission ("EC") wrote to ESMA regarding the definition of a financial instrument relating to foreign currency ("FX Contract"). Please refer to our newsletters of March and June 2014 for background information on this topic.

ESMA had suggested that the EC use the powers granted to it under MIFID I to provide clarity on this definition and in particular to determine the boundaries between FX contracts that can be considered as financial instruments and FX spot contracts that are not considered as financial instruments.

In its letter the EC explained that the powers of the EC to adopt implementing measures in relation to MIFID I had ceased to apply on December 1st 2012. As a consequence the only solution to clarify the definition would be to do so during the implementation process of MIFID II.

In the letter the EC suggests that ESMA issue, pending the entry into force of MIFID II, interim guidelines that could help Member States to reach a common approach on this definition.

The drawback of having such interim guidelines is that Member States could adopt changes in the market and legal practice that might then need to be amended after the entry into force of MIFID II.

Nonetheless, the EC noted that the question of how to define a FX contract has already been extensively discussed during the public consultation on MIFID II and that a "broad consensus" seems to have been reached along the following lines with respect to defining FX spot contracts:

- defining FX transactions in major currency pairs as spot trades provided their settlement is two days after the trade date;
- using the "standard delivery period" for all other currency pairs to define a FX spot contract;
- using the accepted market settlement period of that transferable security to define a FX spot contract, subject to a cap of 5 days, where contracts for the exchange of currencies are used for the sale of a transferable security;
- considering a FX contract that is used as a means of payment to facilitate payment for goods and services as a FX spot contract.

At the moment it is still uncertain whether interim guidelines will be issued by ESMA before January 2017 the date for implementation of MIFID II.

The responses to the EC's consultation are available at:http://www.esma.europa.eu/consultation/Consultation-Paper-MiFID-IIMiFIR#responses

The letter from the EC is available at: http://www.esma.europa.eu/system/files/ec_letter_to_esma_on_classification_of_financial_instruments_23_07_2014.pdf.

CORPORATE

FLOATING FINANCIAL YEAR

The Luxembourg Accounting Standards Board, *Commision des Normes Comptables* ("CNC") issued on April 2nd 2014 a general notice (CNC 0172014) regarding the accounting term of floating financial year. The notices issued by the CNC aim at creating an accounting doctrine and represent the opinion of the CNC on a certain matter, with no binding effect.

The floating financial year is not fixed by reference to specific dates (for instance closing date of September 30th), but is determined pursuant to a floating date (for instance the last Friday of September).

Given that the Luxembourg Trade and Companies Register ("*Registre du Commerce et des Sociétés" – "RCS"*) requires from all undertakings to file with the RCS the relevant starting and ending dates of their financial year, the entities adopting the floating principal would need to file on an annual basis with the RCS the necessary adjustment to their financial year opening and closing dates.

International accounting standards (such as international financial reporting standards - IFRS) already implement the floating financial year principal. According to the CNC, there should therefore also be a possibility for every Luxembourg entity using LUX GAAP to use the floating principal when establishing its annual accounts. However, the following conditions have to be fulfilled:

- The duration of the floating financial year must be:
    i. close to the duration of a civil year; and
    ii. comparable from one year to the other; and
- The dates of opening and closing of the floating financial year have to be determinable and predictable.

DATA PROTECTION

LAW DATED JULY 18TH 2014 APPROVING CONVENTION ON CYBERCRIME

The Law dated July 18th 2014 ("the Law") was published in the Official Gazette on July 25th 2014 (*Mémorial A n°133 p. 2134*) and republished with appended Convention on Cybercrime signed in Budapest on November 23rd 2001 ("the Convention") in the Official Gazette on August 12th 2014 (*Mémorial A n°157 p. 2406*).

The Convention is the first international treaty on crimes committed via the Internet and other computer networks, dealing particularly with infringements of copyright, computer-related fraud, child pornography and violations of network security. It also contains a series of powers and procedures such as the search of computer networks and interception. The Convention was open for signature by the member States of the Council of Europe and by non-member States which have participated in its elaboration in Budapest, on November 23rd 2001.

Its main objective is to pursue a common criminal policy aimed at the protection of society against cybercrime, especially by adopting appropriate legislation and fostering international co-operation.

The Law addresses the threat against computer systems by:

- amending the existing provisions of the Criminal Code (recognition of phishing, inclusion of electronic keys in the list of items that can be used by perpetrators of racket, theft or breach of trust, and increase of the fine relating to the forgery of electronic keys);
- adding new offences (interception of computer data, misuse of devices, and misuse of electronic signature).

The Law has an impact on AML legislation as it broadens the scope of the primary offences which will include child pornography, illegal access, interception or interference into a computer system, and certain related provisions of the law on electronic trade and the law on data protection.

Procedural tools are provided for by the Law, like expedited preservation of stored computer data (including traffic data), production order, search and seizure of stored computer data, real time collection of computer data or traffic data, interception of content data, and a 24/7 technical assistance network among others.

Cyber risk increasingly presents a major risk to the economic environment, regardless of industry.

In the context of M&A, dealmakers (whether buyer or seller) should seriously consider this threat on cyber security. They should therefore implement an appropriate due diligence. Criminals, hacktivists, competitors or even States are among the concerns to take into consideration when an M&A deal is contemplated. Data-driven businesses should be assessed from this point of view, and the evaluation of cyber risk should be performed in the same way as any other risk affecting the value of a target company.

INVESTMENT FUNDS

CIRCULAR 14/589 – OUT OF COURT SETTLEMENT

Following the release of CSSF regulation 13-02 dated October 15th 2013 relating to the out-of-court settlement of claims (the "Regulation"), the CSSF issued at the end of June 2014, circular 14/589 (the "Circular") which further clarifies some aspects of the Regulation.

The Regulation describes the out-of-court settlement procedure applicable to retail clients which have a claim against a financial actor.

The Regulation enumerates the formal steps to be undertaken with the CSSF and the organisational requirements applicable to financial actors which enable them to handle customer complaints.

In this respect, the Circular clarifies the responsibilities applicable to the members of management responsible for the internal claims handling procedure.

In addition, the Circular lays down the information which must be reported on an annual basis to the CSSF in respect of such internal procedure, and a template of such report is annexed to the Circular.

Further information on the Regulation can be found in our newsletter of January 2014 and the Circular is available at: http://www.cssf.lu/fileadmin/files/Lois_reglements/Circulaires/Hors_blanchiment_terrorisme/cssf14_589.pdf

CSSF CIRCULAR 14/587 – NEW RULES APPLICABLE TO DEPOSITARY BANKS

On July 15th 2014 the *Commission de Surveillance du Secteur Financier* (the "CSSF") issued a new Circular 14/587 (the "Circular") which is applicable to UCITS' depositary banks and to the UCITS themselves regarding their relationship with their depositaries.

The aim of the Circular is to align the requirements applicable to UCITS' depositaries with the requirements imposed by Directive 2011/61/EU on alternative investment fund managers ("AIFMD"). Such alignment anticipates the implementation of the UCITS V Directive into Luxembourg law.

The Circular will supersede the previous IML Circular 91/75. Such new Circular represents a shift from the previous "principle-based approach" to more stringent and detailed rules.

The Circular focuses on the four following points:

- Asset segregation within the depositary
  In line with what is foreseen in UCITS V and in the AIFMD, the obligations to which the depositary bank is subject change according to the nature of the assets held in custody. Thus, a distinction has to be drawn between assets which are physically held by the depositary and those that are to be held by sub-depositaries or specialised third parties.
  In addition, the Circular introduces a new mechanism which foresees a level-by-level problem solving which involves the depositary, the fund's management company and the financial regulators in order to deal with the loss of assets in custody.

- Initial and continuing due diligence procedure on all sub-depositaries and other appointed service providers
  As stated above, the "principle-based approach" has been abandoned, so that the Circular now clarifies the minimum rules that must be included in a depositary's due diligence procedure. The requirements applicable to due diligence procedures include, among others, criteria which enable

the depositary to select its service providers and a description of the organisational resources that such service provider must have (e.g. in order to ensure the proper exchange of information on the assets).

- Conflicts of interest policy
  The Circular takes into account the fact that a depositary may perform several functions which might result in conflicts of interest. Those functions include for example prime brokerage services, collateral management services and administrative agency services.
  The Circular also deals with procedures in respect of conflicts that may rise from the sub-delegation of services by the depositary.

- Accounting and follow-up of the cash/liquidity flows
  A description of the infrastructure and of the organisational resources which must be implemented within the depositary and its service providers is further set out in the Circular. The aim of these requirements is to ensure that the above financial actors are able to properly monitor the cash and liquidity flows.

The depositary's liability regime shall not be affected by the Circular. The liability regime remains subject to the Law of December 17th 2010 on undertakings for collective investment.

Luxembourg credit institutions and UCITS **have until December 31st 2015 to comply** with the requirements of the Circular. At that time, Chapter E of IML Circular 91/75 shall no longer be applicable.

AIFMD

UPDATED CSSF FAQ

On July 18th 2014 the Commission de Surveillance du Secteur Financier ("CSSF") published an updated version of its frequently asked questions ("Updated FAQ") concerning the Luxembourg law of July 12th 2013 on alternative investment fund managers ("AIFM Law") as well as the Commission Delegated Regulation (EU) No 231/ 2013 of December 19th 2012.

Two new questions have been added and one general question has been amended in the Updated FAQ. The amended question relates to reporting by non-EU AIFMs marketing AIFs in Luxembourg. The Updated FAQ clarifies that:

- a non-EU AIFM will have to report to the CSSF only in the case where it is marketing to professional investors in Luxembourg;
- the information to be reported should only cover the data for those AIFs that are marketed in Luxembourg;
- the date of the information form provided to the CSSF prior to the commencement of marketing (see below) is considered as the start date for the reporting period; and
- the reporting frequency and periods for non EU-AIFMs are the same as those applicable to Luxembourg AIFMs.

The first new question (Q 17.) deals with initial capital, own funds requirements and coverage of potential professional liability risks applicable to AIFMs. The Updated FAQ sets out the exact initial capital and own funds required for either a chapter 15 Manco with a licence as AIFM or an external AIFM which does not hold a licence as a Chapter 15 Manco (i.e. Chapter 16 Mancos or other Luxembourg based AIFMs).

The second question (Q 18.) relates to the marketing of AIFs to professional investors in Luxembourg without a passport by non-EU AIFMs on the basis of article 45 of the AIFM Law. The CSSF confirmed that non-EU AIFMs are allowed to do so provided that the conditions of article 45 of the AIFM law are met, but such non-EU AIFMs have to:

(i) inform the CSSF prior to any marketing activity using the information form that has been made available on the CSSF's website;
(ii) communicate to the CSSF the end-date of marketing activity in Luxembourg; and
(iii) report to the CSSF periodically in accordance with article 24 of the AIFM Directive.

The full text of the Updated FAQ is available at: http://www.cssf.lu/en/aifm.
The information form can be downloaded from the website of the CSSF at: http://www.cssf.lu/en/supervision/ivm/aifm/forms.

UPDATED ESMA Q & A

The "Questions and Answers" document (the "FAQ Document") of the European Securities and Markets Authority ("ESMA") in respect of Directive 2011/61/EU on alternative investment fund managers ("AIFMD") was updated on July 18th 2014.

The following topics have been newly included/updated:

- Reporting to national competent authorities under articles 3, 24 and 42 of the AIFMD: an additional 14 questions have been added to this section of the FAQ Document, providing information on the practical content of the reporting documents which must be submitted by alternative investment fund managers (AIFMs) to their regulatory authority.
- The FAQ Document now provides a new section on the depositary regime. Questions regarding the scope, the extent of permitted delegation and the custodial function in general are being answered.
- In addition the FAQ Document now provides clarifications on the method of calculation of leverage for the purpose of the AIFMD and related rules and regulations.

The updated Q&A can be found at: http://www.esma.europa.eu/system/files/2014-esma-868__qa_on_aifmd_july_update.pdf

ESMA GUIDELINES ON REPORTING OBLIGATIONS

On August 8th 2014, the European Securities and Markets Authority ("ESMA") published the translations of the guidelines on the reporting obligations for alternative investment fund managers ("AIFM") under the AIFM Directive.

National competent authorities have two months from such date to confirm whether they comply with the Guidelines. The CSSF have already issued Circular 14/581 on new reporting obligations for AIFMs (see our newsletter of March 2014).

The final guidelines are available at: http://www.esma.europa.eu/content/Guidelines-reporting-obligations-under-Articles-33d-and-241-2-and-4-AIFMD-0

CSSF CIRCULAR 14/591 – MATERIAL CHANGES TO UCIS

On July 22nd 2014, the *Commission de Surveillance du Secteur Financier* ("CSSF") issued Circular 14/591 (the "Circular") on protection of investors in case of a material change to an open-ended undertaking for collective investment ("UCI"). The Circular sets out in print what the de facto

position of the CSSF has always been in dealing with changes to open ended UCIs.

The purpose of the Circular is to clarify and set out the administrative practice when there is a material change to investors' interests in an open-ended UCI governed by the law of December 17th 2010 relating to UCIs, as amended. To assess whether a change will be a material one to their structure, organisation or operations, UCIs should:

(i) consider whether the contemplated change has an impact on an investor's interest causing him to reconsider his investment, and
(ii) submit the proposed change to the CSSF together with the reasons for such change.

If the CSSF is of the view that such change is deemed material, then the CSSF requests that a notification be sent to investors and the change will be implemented only after the end of the notification period, which must be at least one month. The Circular also provides that the notification period is without prejudice to the notification periods required by law for investors to pre-approve such events.

During the notification period, the investors have the right to request:

(i) the repurchase,
(ii) the redemption of their units free of charge, or
(iii) the conversion of such units into units which are not affected by such material change.

On a duly substantiated request of a UCI, the CSSF may grant the following derogation from the general regime set out in the Circular:

- if all investors in the relevant UCI agree with the contemplated change, the CSSF may permit the UCI not to redeem, repurchase or convert the units of investors free of charge ; or
- the CSSF may require that investors are notified, but without the possibility of having their units redeemed or converted free of charge.

The Circular is available at: http://www.cssf.lu/en/search/?id=1056&L=1&search=14%2F591&x=0&y=0

ESMA OPINION - COMMON DEFINITION OF EUROPEAN MMFS

On August 22nd 2014 the European Securities and Markets Authority ("ESMA") issued an opinion (the "Opinion") on the application of guidelines issued by the Committee of European Securities Regulators ("CESR") in May 2010, on a common definition of European money market funds ("MMF") (Ref. CESR/10-049, hereafter the "CESR guidelines"). The CESR guidelines entered into force on July 1st 2011.

The CESR guidelines set out criteria that money market instruments should respect in order to be considered as eligible investments for short term money market funds ("ST MMF") and MMF.

The Opinion is intended to modify the CESR guidelines, regarding the assessment of the credit quality of money market instruments and is as a result of the report of the Joint Committee of the three European Supervisory Authorities issued earlier this year. According to the CESR guidelines, a money market instrument should not be considered to be of high quality by managers of ST MMF and MMF unless it has been awarded one of the two highest available short-term credit ratings by each recognised credit rating agency that has rated the instrument.

The Opinion considers that when analysing whether a money market instrument is of high

quality, the management company should take into account the credit quality of the instrument by performing its own documented assessment and on the basis of previous ratings of the instrument, carried out by credit rating agencies registered and supervised by ESMA. While there should be no mechanistic reliance on such external ratings, a downgrade below the two highest short-term credit ratings by any agency registered and supervised by ESMA that has rated the instrument should lead the manager to undertake a new assessment of the credit quality of the money market instrument to ensure it continues to be of high quality.

The Opinion further points out that as an exception to the above, sovereign issuance assessed as being of a lower internally-assigned credit quality may be held by a MMF.

The CESR guidelines will not be amended. National competent authorities will not have to notify ESMA whether or not they comply or intend to comply with the amended version of the CESR guidelines. However, ESMA will monitor the application of the Opinion by national competent authorities.

The Opinion can be found in the following link http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2013:146:0001:0033:EN:PDF.

UCITS V ADOPTED

We reported in our newsletter of June 2014 that on April 15th 2014 the European Parliament adopted the Directive of the European Parliament and of the Council amending Directive 2009/65/EC on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) as regards depositary functions, remuneration policies and sanctions (UCITS V Directive).

Since then, the Council of the European Union (Council) has formally approved, on July 23rd 2014, the text with the required qualified majority. On August 28th 2014 the UCITS V Directive was published in the Official Journal of the European Union (Official Journal) and entered into force on September 17th 2014. The Member States have to transpose it into national law by March 18th 2016 at the latest.

The full text of the UCITS V Directive is available at: http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=uriserv:OJ.L_.2014.257.01.0186.01.ENG

EMIR

CLEARING OBLIGATIONS

On July 11th 2014 ESMA issued two consultation papers with the aim of drafting regulatory standards ("RTS") on the clearing obligations under Regulation (EU) No 648/2012 on OTC derivatives, central counterparties ("CCPs") and trade repositories ("EMIR").

These first two public consultations relate to the categories of OTC derivative contracts that should be made subject to the mandatory clearing obligations under EMIR.

These long awaited papers, which cover OTC interest rate derivatives, OTC credit derivatives, and OTC equity derivatives aim at providing clarity on the frontloading obligation and the timelines applicable to the different market players in relation to their clearing obligations.

The first paper published on July 11th covers the clearing obligation for certain interest rate OTC

derivatives classes. The consultation was closed on August 18th.

The second paper, also published on July 11th, covers the clearing obligation for certain credit OTC Derivatives. This consultation closed on September 18th.

The publication of the final RTS, following endorsement by the European Commission is expected to happen between December 2014 and February 2015 at the latest.

To allow for a smooth process of application, it is suggested that the clearing obligation apply in stages to different market participants following the entry into force of the RTS, as follows:

- Category 1 – Clearing members- grace period of 6 months, clearing to start around June 2015 at the earliest;
- Category 2 – Non-clearing members - grace period of 18 months, clearing to start around June 2016 at the earliest;
- Category 3 – Non-clearing members that are non-financial counterparties - grace period of 36 months, clearing to start around December 2017 at the earliest.

The text of the Consultation Papers and the public responses are available at: http://www.esma.europa.eu/consultation/Consultation-paper-Clearing-Obligation-no1-IRS#responses http://www.esma.europa.eu/consultation/Consultation-paper-Clearing-Obligation-no2-CDS

EMIR- LEGAL ENTITY IDENTIFIERS

Under the European Market Infrastructure Regulation ("EMIR") all EEA counterparties subject to reporting need to provide a pre-legal entity identifier ("LEI") pending the finalisation of a global LEI, to meet the reporting obligations. The pre-LEI are issued by Local Operating Units ("LOU") which are endorsed for the purposes thereof.

The LEI has the form of a 20-digit code that connects to key reference information, enabling the clear and unique identification of legal entities.

The LEI regulatory oversight committee ("ROC"), a committee of authorities from around the world, is the entity in charge of endorsing the LOUs for issuance of pre-LEIs.

On August 26th the ROC announced the endorsement of LuxCSD, an entity sponsored by the Central Bank of Luxembourg as a pre-LOU.

LuxCSD will therefore provide the LEI issuance service for Luxembourg-domiciled entities and investment funds via luxcsd.com so that now, entities will be able to use Luxembourg LEIs for reporting financial transactions on an international level rather than just for domestic transactions.

The ROC's announcement is available at: http://www.leiroc.org/publications/gls/lou_20140826-1.pdf

GUIDELINES ON ETFS AND OTHER UCITS ISSUES

On August 1st 2014 (The "Publication Date"), the European Securities and Markets Authority ("ESMA") published the revised guidelines on ETFs and other UCITs issues (including translations thereof). Please see our newsletter of June 2014 for information on the content of the revised guidelines.

The new provisions on diversification of collateral received by UCITS in the context of efficient portfolio management techniques and over-the-

counter financial derivative transactions shall therefore apply from October 1st 2014.

UCITS that exist before the Publication Date have 12 months to comply with the collateralisation and disclosure rules.

The CSSF on September 30th 2014 issued Circular 14/592 which implements the revised guidelines into Luxembourg regulation. The Circular comes into effect from the same date as the revised guidelines i.e. October 1st 2014.

The revised guidelines are available at: http://www.esma.europa.eu/content/Guidelines-ETFs-and-other-UCITS-issues-0

The Circular is available at: http://www.cssf.lu/fileadmin/files/Lois_reglements/Circulaires/Hors_blanchiment_terrorisme/cssf14_592.pdf

APPLICATION QUESTIONNAIRE FOR UCITS

On September 1st 2014, the *Commission de Surveillance du Secteur Financie*r (the "CSSF") published Press Release 14/47 (the "Press Release") relating to the introduction of a new form "Application questionnaire to set up an UCITS" (the "New Application Questionnaire"). This New Application Questionnaire replaces the current form "Application questionnaire for the setup of an undertaking for collective investment" and has to be used as from September 1st 2014 for submitting to the CSSF an application for approval to set-up an UCITS.

The New Application Questionnaire is an Excel spreadsheet where all the contents and topics necessary for the examination of a file are compiled in different tabs, each tab offering a series of footnotes and drop-down lists. The CSSF advises the applicants to file their application only once all the components of the projects are fully available and stable; otherwise the start or the swift progress of the approval process may be jeopardized and unexpected delays may occur.

Application files are to be submitted by electronic means and in case of application filed via e-mail a nomenclature specified in the "Documents" tab of the New Application Questionnaire has to be followed to name the e-mail and the documents in attachment.

Requests in preparation using the previous application form were accepted by the CSSF until September 30th 2014 but after this date the use of the New Application Questionnaire is mandatory.

The Press Release and application questionnaire are available at: http://www.cssf.lu/fileadmin/files/Publications/Communiques/Communiques_2014/PR1447_OPCVM_Application_questionnaire_010914_EN.pdf

TAX

"REAL ESTATE RICH COMPANIES" CLAUSE - PROTOCOL TO THE INCOME TAX TREATY WITH FRANCE

Luxembourg signed a protocol to the income tax treaty with France on September 5th 2014 ("French Protocol").

The French Protocol introduces a so called "real estate rich company" clause. Under the present version of the income tax treaty with France, Luxembourg is authorized to tax capital gains realised by a Luxembourg resident upon disposal of shares held in a company holding real estate in France. Under the French Protocol, the "real estate rich company" clause shifts the right to tax such capital gains to the source state (in our case France).

Under the French Protocol, capital gains derived from the alienation of shares or other rights in a company, trust or any other legal person the assets of which are composed, in value, for more than 50% - directly or through the interposition of one or more companies or legal persons - of immovable property situated in a contracting state, are only taxable in such state. Immovable property allocated by the "real estate rich" company" to its own commercial activity is however not taken into account.

The French Protocol also provides that the "real estate rich company" clause should not conflict with the application of the council directive 2009/133/CE (so-called EU Merger Directive). The French Protocol will enter into force on the first day of the month following the completion of the ratification process by Luxembourg and France and its provisions will apply as from the following year.

UPDATE OF THE OECD MODEL TAX CONVENTION

On July 15th 2014, the OECD published its 2014 update of the Model Tax Convention ("2014 OECD Update"). This update is the outcome of the work accomplished between 2010 and the end of 2013. It does not however take into account the OECD conclusions of the "*Action Plan on Base Erosion and Profit Shifting*" (BEPS).

The 2014 OECD Update will be of interest to Luxembourg practitioners for various reasons. Aside from helpful clarifications in the field of taxation of *Artists and Sportsmen* (article 17) and some other questions of rather marginal interest regarding *emissions permits/credits*, the update is of major interest in relation to three recurrent problems in Luxembourg tax practice.

With respect to exchange of information, the update includes modifications to article 26 and its commentary which have been agreed by the OECD Council on July 17th 2012. The question on "*foreseeable relevance*", which is key in order to allow exchange of information upon request in the banking sector, remains at the heart of the issue, together with the requirement to identify, to a certain extent, the relevant taxpayer. The 2014 OECD Update should however not substantially impact Luxembourg judicial practice in this field, which, like the 2014 OECD Update, tries to balance providing as much international assistance as possible with preventing fishing expeditions.

The details included in the 2014 OECD Update regarding the definition of "*beneficial ownership*" will be of major interest for practitioners. It is common knowledge nowadays that the sole payment of income from movable property (royalties, interest, dividends) to a Luxembourg resident recipient is not enough to allow for entitlement to the double tax treaty benefits (reduction or elimination) with regard to the withholding tax suffered in the source country.

One needs to make sure that the recipient of the income is also the “beneficial owner”. The 2014 OECD Update stresses that the concept of “*beneficial ownership*” needs its own, independent and autonomous definition instead of referring to the legislation of the source country. This is rather good news for Luxembourg companies, because the simple reference to national laws would have left Luxembourg without any means of recourse in case of future changes of legislation by our tax treaty partners. Another interesting and important change is the fact that the concept of “*beneficial ownership*” for international tax treaty purposes is not the same as the concept of “*economic owner*ship” for anti-money laundering purposes. This small detail is of importance, because otherwise all Luxembourg entities not having a listed company as ultimate shareholder would have been exposed to a certain risk.

The treatment of indemnities paid upon the termination of an employment contract has also been modified in the sense that the indemnities are taxable in the country where the employment activity was carried out provided that the indemnities are economically linked to the employment, irrespective of whether they have been paid after termination of the employment contract (e.g. indemnities paid with respect to the period during which the employee is discharged from work).

The 2014 OECD Update, which was validated by the OECD Committee on Fiscal Affairs on June 26th, will be included in a “revised version of the Model Tax Convention” to be published in the upcoming months.

THE LUXEMBOURG FREEPORT AND ITS PREFERENTIAL VAT SUSPENSION REGIME

On September 17th 2014, the Grand-Duchy of Luxembourg inaugurated its Freeport, a facility constructed at the Luxembourg airport next to the Air Cargo Terminal for storage, handling and trading of goods such as works of art, precious metals, wine, jewellery and other valuable goods.

Within the context of the creation of the Freeport, the Luxembourg government had enacted with the law of July 28th 2011 a particular VAT regime which, in line with EU Customs and Tax Regulations, provides for a suspension of VAT and customs duties on goods introduced into a free zone from third countries or originating in the EU. This special regime applies as long as the goods remain in storage in the Luxembourg Freeport. VAT is also suspended on storage and other value added services while the goods remain in custody at the Luxembourg Freeport. The Luxembourg Freeport is operated under the supervision of the Luxembourg Customs Authorities, which inspect the goods that enter or exit the facility on-site and are endowed with an unlimited right to access the goods. Upon exit of the goods from the Freeport, the temporary suspension of the VAT is to be regularised, which however remains without consequences if the goods are exported outside of the EU.

CLARIFICATION REGARDING THE IP TAX REGIME

On July 30th 2014 the Higher Administrative Court of Luxembourg (*Cour Administrative*) ("the Higher Court") issued a decision (“Decision 33148C”) on the application of the Luxembourg intellectual property tax regime that grants a 80% tax exemption of the income deriving from qualifying intellectual property rights ("IP").

This decision was issued following an appeal filed by the Luxembourg government against the decision of the Lower Administrative Court (*Tribunal Administratif*) of June 27th 2013. For details of this decision please refer to our newsletter of September 2013.

In the case at hand, a Luxembourg company ("the Company") was selling, since its incorporation in 1994, products under its own trademark, the registration of which had only been made in 2008. The Court had to decide which date is decisive for the determination of the date of creation of the IP considering that the IP regime is only available for IP created after December 31st 2007.

The Higher Court confirmed that the date of creation of a trademark under Article 50bis (4) of the Luxembourg Income Tax Law ("LIR") is the date of its registration.

The Higher Court however overruled the decision of the Lower Administrative Court on the basis that not all the other conditions of article 50 bis LIR were met.

The Company had entered into a license agreement with a sister company three days after the registration of the trademark. Significant royalties were agreed between the parties for the use of the trademark. However the sister company's activities were limited to affixing the trademark on goods sold exclusively to the Company. The Higher Court considered that this was not an effective "use of the trademark" and that therefore the royalties were not paid for the use of an IP. The Higher Court therefore decided that the royalties paid to the Company do not qualify for the partial tax exemption provided under the Luxembourg IP tax regime.

DRAFT LAW N°6706 ON THE ANNUAL NET WEALTH TAX ASSESSMENT

Draft law n°6706 dated July 17th 2014 (the "Draft Law") intends to modify the net wealth tax assessment procedure in order to simplify and accelerate the assessment process.

Since 2006, Luxembourg net wealth tax only applies to corporations subject to corporate income tax. Net wealth tax for individuals has been abolished.

Currently, the net wealth tax law of October 16th 1934 ("*Vermögensteuergesetz"*) provides that net wealth tax is determined on a three-year basis through a so-called general tax assessment ("*Hauptveranlagung"*). A new tax assessment ("*Neuveranlagung"*) is only necessary if, within the three-year period, the net wealth of the corporate taxpayer varies beyond certain limits. The determination of the unitary value, which serves as net wealth tax base in line with the valuation law of October 16th 1934 ("*Bewertungsgesetz"*), follows the same rules.

As from January 1st 2015, the determination of the unitary value as well as the resulting net wealth tax assessment will be established on an annual basis.

The Draft Law furthermore intends to adapt the rules governing the advance net wealth tax payments. Some piecemeal amendments *i.a.* to the collection procedure for income tax and excise duties, as well as to the regime concerning the interruption of the limitation period, are also foreseen.

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