Luxembourg

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Bill 6846 on OTC derivatives, central counterparties and trade repositories

On 5 August 2015 the bill 6846 on OTC derivatives, central counterparties and trade repositories has been deposited with the Chambers of Deputies (the **"Bill"**).

1. Objectives of the Bill

The Bill aims to ensure the transposition and implementation of a series of European measures ensuring financial stability, in particular Regulation (EU) No 648/2012 of the European Parliament and the Council of 4 July 2012 on OTC derivatives, central counterparties and trade repositories (the "**EMIR**"). Furthermore it provides changes to existing laws in the financial sector in consideration to the evolution of European law with regard to the supervision of financial conglomerates.

The *Commission de Surveillance du Secteur Financier* (the "**CSSF**") and the *Commissariat aux Assurances* (the "**CAA**") will get new powers as well as a panel of sanctions, in order to fulfil their new control missions.

2. Objectives of EMIR

The objective of EMIR is to mitigate the risk of contagion by introducing measures to promote an efficient, robust and transparent derivatives market. It requires the clearing of standardized derivatives agreements through central counterparties (the "**CCPs**") and establishes bilateral risk management requirements for other OTC derivative agreements. Counterparties to derivative agreements must now declare essential information to repositories related to these agreements. EMIR also defines the legal framework governing the activity of CCPs.

3. Roles of CSSF and CAA

In its role as competent authority the CSSF is responsible to ensure the application of EMIR, without prejudice to the statutory powers devolving on the Luxembourg Central Bank as a member of the European system of central banks and the legal powers that the Bill grants to the CAA.

3.1. New Powers of CSSF and CAA

Therefore, the CSSF is vested with all powers of supervision, intervention, inspection and investigation necessary to exercise its functions within the limits defined by EMIR.

The powers of the CSSF with regard to financial counterparties, CCPs and trading platforms as well as the powers of the CAA with regard to the financial counterparties include the rights to:

1. have access to any document in any form and to receive the respective copy;

2. request information to the respective parties mentioned above subject to its supervision, including those who are successively involved in the transmission of orders or conduct of the operations concerned, as constituents thereof and, if necessary, to call a person and hear it;

3. conduct on-site inspections and surveys of the respective parties;

4. require the respective parties of telephone communication and existing computer records;

5. require to cease any practices contrary to EMIR.

3.2. New Sanction Regime

3.2.1. Requirements

Sanctions by the CAA in relation to financial counterparties and by the CSSF relating to financial and non-financial counterparties as well as CCPs can be made in case those parties do not meet the provisions of EMIR. Furthermore sanctions by the CAA regarding financial counterparties and by CSSF in case of trading venues can be made, if the respective parties:

a) publish information which is proved to be incomplete, inaccurate or false;

b) refuse to provide documents and other information requested;

c) have provided documents or other information which is proved to be incomplete, inaccurate or false;

d) impede the exercise of powers of surveillance, intervention, inspection and investigation of the CSSF/CAA;

e) do not follow the injunctions of the CSSF/CAA.

3.2.2. Severity

The sanctions by the CSSF and the CAA shall be in order of severity:

a) a warning;

b) a reprimand;

c) an administrative fine which may not be less than EUR 125 nor more than EUR 1.5 million or if the offense has provided a financial benefit, directly or indirectly, to persons referred to in Article 3 of the Bill, the amount of a fine cannot be less than the amount of profit made nor more than five times that amount;

d) a ban limited in time or permanent performing one or more activities or one or more operations on a class of financial instruments or providing certain services.

In the pronouncement of the sanction certain factors such as the nature, duration and gravity of the offense, the conduct and background of the person or entity to the sanction, financial loss to third parties and the benefits or potential or actual gains derived from the offense are to be taken into account.

The CSSF and the CAA publicize the penalties for infringements of Article 4, 5 or 7-11 of EMIR, unless such publication not seriously disrupts the financial market or causes disproportionate damage to the parties.

4. Other amendments by the Bill

Finally, various laws governing financial services are modified by the Bill in order to cover the developments in European law on the supervision of financial conglomerates. According to the Bill and its comments on the articles, the following changes exist with regard to other laws:

4.1. Law of 10 November 2009 on payment services (the “2009 Law”)

The Bill amends the 2009 Law in order to:

- insert the new interoperability rules of the systems provided for in EMIR, implementing the Regulation (EU) No 260/2012;
- remove any ambiguity as to the choice of the depositary, payment institutions are using to protect the funds they have received in exchange for payment transactions or issuing electronic money;
- facilitate the smooth functioning of TARGET2-Securities is a Eurosystem project to create a technical platform on which the central securities depositories will entrust the management of their settlement activity of securities in central bank money according to harmonized modalities.

4.2. Regulation (EC) No 1060/2009 on credit rating agencies (the “CRA 3 Regulation”)

The Bill also transposes into Luxembourg law Directive 2013/14/EU of 21 May 2013 and implements certain provisions of Regulation (EU) No 462/2013 of the European Parliament and of Council of 21 May 2013 amending the CRA 3 Regulation. Its implementation is essentially a modification of Article 2-1 of the Law of 23 December 1998 establishing a financial sector supervisory commission, while the transposition of Directive 2013/14/EU requires specific modifications in several laws governing financial services.

On 20 October 2010 the Financial Stability Board issued recommendations to reduce the excessive dependence of financial actors in respect of credit ratings and to eliminate as far as possible credit ratings resulting as of automation, especially in the assessment of credit risk. Directive 2013/14/EU and the CRA 3 Regulation are to implement these recommendations at the European level. Directive 2013/14/EU introduced requirements for methods and risk management systems of institutions for occupational retirement, management companies of mutual funds and alternative investment fund managers to improve the quality of investments by these entities and thereby protect investors.

The desire to reduce excessive reliance on credit ratings has led the CRA 3 Regulation to the introduction of an obligation to publish relevant information by issuers, originators and sponsors of structured finance instruments. The objective is to provide investors with sufficient information which puts

them in a position to assess, knowingly, credit quality in order to reduce their vis-à-vis credit ratings dependence. The CRA 3 Regulation also aims to encourage the use of smaller credit rating agencies in order to promote competition in a market currently dominated by a very small number of large credit rating agencies.

5. Conclusion

The adoption of the Bill will constitute a qualitative step forwards in the transposition and implementation of a series of European measures ensuring financial stability by providing the CSSF and CAA with new powers and modifying its sanction possibilities.

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Overview of the new staff representation legislation

On 23rd July 2015, i.e. more than two years after the filing of the draft bill n° 6545 and the formal objections made by the State Council against the provisions of the draft bill, the new law concerning the reform of social dialogue (hereinafter the "**Law**") was enacted.

The Law, which will come into force on 1st January 2016, provides major changes to the rules governing staff representation. However, certain provisions (e.g. the appointment, the organisation and the functioning of the staff delegations) will only take effect at the same time as the elections of staff representatives scheduled in 2018 (except in case of anticipated elections),the current provisions on Joint Works Council being applied until the next social elections.

Here is an overview of the important modifications and innovations introduced by the Law.

1. Structuring of the staff delegations:

Any company (instead of "establishment" in the current legislation), regardless of its business sector or legal form, with a workforce of at least 15 employees during the 12 months preceding the first day of the month of the posting announcing the elections' date will be required to set up a staff delegation.

When several companies constitute an "economic and social entity" (hereinafter the "**ESE**")[1], a delegation may be established at the ESE level further to the request of at least two staff delegations of the ESE. The aim of this delegation is to represent the interests of all employees working in the various companies of the ESE and to exchange information between various staff delegations.

2. Abolition of some delegations:

In order to increase the efficiency of social dialogue and simplify staff representation, the Law will abolish the central delegations, the divisional delegations, the young staff

[1] For more details about the concept of ESE, please refer to the Newsletter 4. Quarter 2014 available on Luther's website http://www.luther-lawfirm.lu/en/publications/newsletters/list/luxembourg.html.

delegations and the joint workers council as from the new elections fixed in 2018.

As a consequence, only the staff delegations, the delegations at the ESE level and the administrators of the public limited companies (*Sociétés Anonymes*) will represent the employee's interest as from the elections in 2018. As a consequence, the powers which were reserved to the abolished bodies will be automatically transferred to the staff delegations.

Furthermore, it is important to note that a voting right will be granted, according to the Law, to employees of 16 years of age (instead of 18 in the current legislation).

3. Fulfilment of the mandate:

According to the Law, the employer will have, without his/her prior agreement, to let and pay the staff delegates the necessary time to perform their missions.

The time-off credit hours has been increased. In fact, the employer will have to grant to the staff delegates time-off credit paid hours proportional to the number of employees represented on the basis of:

- 40 hours per week for 500 employees for companies which workforce doesn't exceed 149 employees; and
- 40 hours per week for 250 employees for companies which workforce is between 150 and 249 employees.

The Law has also reduced the thresholds above which employers must release a delegate from his/her work. For example, the employer will have to release one delegate if the number of employees is comprised between 250 (instead of 501 in the current legislation) and 500 (instead of 750 in the current legislation).

Regarding the delegates' training, the Law aims to provide additional training hours to (i) deputy staff delegates, (ii) security and health delegates and (iii) newly elected staff delegates during the first year of their mandate.

4. Special protection:

As in the current legislation, staff delegates will continue to benefit from a special protection against dismissal. This protection has been reinforced as employers will also be prohibited to make an unfavourable amendment of an essential clause of their employment agreement[2].

Moreover, the unfairly dismissed staff delegate will not only be entitled to request his/her reinstatement before the President of the Labour Court, as detailed under the current legislation but, according to the Law, the latter can, instead of such reinstatement, obtain the allocation of damages for unfair dismissal.

Finally, the Law adds that, in case of dismissal for gross misconduct, the dismissal staff delegate will benefit, during 3 months following the notification of his/her layoff, from remuneration and other advantages to which he/she would have been entitled to, if the employment agreement would have remained in force. Within one month following the layoff, the employee may request, by a simple request to the President of the Labour Court, to decide on the maintenance or the suspension of his/her remuneration until the final resolution of the litigation case.

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[2] For more details about the modification process of an employment agreement, please refer to the Newsletter 1st Quarter 2015 available on Luther's website http://www.luther-lawfirm.lu/en/publications/newsletters/list/luxembourg.html

CSSF and ESMA Updates on AIFMD

1. Update of the ESMA Q&As

On 21 July 2015, the European Securities and Markets Authority ("**ESMA**") published an updated version of its Questions and Answers (the "**Q&As**") (ESMA/2015/1137) with regards to the application of the Alternative Investment Fund Managers Directive (the "**AIFMD**"). The updates and clarifications concern reporting to the national competent authorities, as well as the calculation of the total value of the assets under management (the "**AuM**").

With regard to the reporting to national competent authorities, several questions have been added and/or updated as follows:

- One question has been updated to provide that when a Member State applies the ESMA's opinion on collection of additional information under Article 24(5) of the AIFMD (ESMA/2013/1340), Alternative Investment Fund Managers ("**AIFMs**") should also report information on non-EU master alternative investment funds ("**AIFs**") not marketed in the EU that have either EU feeder AIFs or non-EU feeder AIFs marketed in the EU.

- A new question has been added to clarify the procedures for converting the total value of AuM expressed in foreign currencies into Euro.

- A new question has also been added to confirm that AIFMs should include AIFs created during a specific reporting period in the total value of AuM of the AIFM for that reporting period.

Regarding the calculation of the total value of AuM, one question has been updated in order to clarify that AIFMs should include in such calculation any assets received pursuant to a short sale.

The latest version of the Q&As is available on the ESMA's website.
https://www.esma.europa.eu/system/files/2015-1137_qa_on_the_application_of_the_aifmd.pdf

2. ESMA Advice and Opinion

On 30 July 2015, ESMA published its advice (ESMA/2015/1236) (the "**Advice**") relating to the extension of the EU marketing passport under AIFMD (the "**Passport**") and its opinion (ESMA/2015/1235) (the "**Opinion**") relating to the functioning of the Passport and of the national private placement regimes ("**NPPRs**").

The Advice and the Opinion were published pursuant to Article 67 of the AIFMD requiring ESMA to produce such documents to the European Parliament, the Council and the Commission for their consideration, following which the Commission should adopt a delegated act, as the case may be.

2.1. The ESMA Advice

The purpose of the Advice is to analyse whether the Passport, which is currently applicable only to EU AIFMs and EU AIFs, shall be extended to non-EU AIFMs and non-EU AIFs managed by EU AIFMs which are subject to NPPRs.

ESMA's assessment of six non-EU countries has been made considering key issues such as investor protection, market disruption, obstacles to competition and monitoring of systemic risk.

ESMA concluded that no obstacles existed to the extension of the Passport to Guernsey and Jersey, whereas Switzerland could benefit from the Passport after removal of certain regulatory obstacles. No definitive view has, however, been reached on the other three jurisdictions under review (i.e. Hong Kong, Singapore and the United States).

2.2. The ESMA Opinion

ESMA considers in the Opinion that it is too early to draw final conclusions of the functioning of the Passport and of the NPPRs due to the short period of time elapsed since the AIFMD implementation in the Member States. ESMA thus recommends conducting a new assessment in the future.

3. Update of the CSSF FAQs

3.1. Background

On 10 August 2015, the *Commission de Surveillance du Secteur Financier* (the "**CSSF**") published an updated version

of its Frequently Asked Questions (the "**FAQs**") on the Law of 12 July 2013 on alternative investment fund managers.

Several general questions have been amended in the FAQs concerning *inter alia* (i) the status of credit institutions and investment firms, (ii) the carrying out of depositary functions, (iii) certain reporting matters and (iv) initial own capital. The FAQs also provides new guidance on marketing and reverse solicitation with regard to AIFs.

3.2. Marketing

According to the CSSF, marketing takes place when the AIF, the AIFM or an intermediary on their behalf, seeks to raise capital by actively making units or shares of an AIF available for firm purchase by a potential investor.

Nevertheless, the CSSF considers that the following do not constitute a marketing activity:

- the providing of draft documents to potential investors, provided the investors would not be able to subscribe shares or units of the AIF based on such documents;
- the investments made, in the context of a discretionary mandate, for the management of individual investment portfolios where the investment is at the initiative of the investment manager;
- the proposal to invest in an AIF, in the context of an investment advisory agreement, is made at the initiative of the advisor;
- the investments in targeted AIFs made, in the context of the collective portfolio management of an undertaking for collective investment ("**UCI**") or an AIF, at the initiative of the UCI/AIF or its management company, AIFM, portfolio manager or other agent; and
- secondary trading of units or shares of an AIF, except where there is an indirect offering or placement through an intermediary acting for the AIFM or the AIF.

The marketing activity is considered to be done in Luxembourg provided such activity takes place on the Luxembourg territory and is carried out by authorised intermediaries, but does not require the physical presence of the AIFM in Luxembourg.

According to the CSSF, distance marketing may qualify as marketing in Luxembourg when (i) the activity takes place by any means of communication which does not require simultaneous physical presence of the AIFM, AIF (or their intermediary) and the investor, and when (ii) the investor is domiciled or has its registered office in Luxembourg.

3.3. Reverse solicitation

The CSSF underlines that reverse solicitation (concept also known as "passive marketing") shall in no case be invoked to circumvent provisions of the AIFMD.

According to the CSSF, reverse solicitation consists in providing information regarding AIFs and making units or shares of AIFs available for purchase following an initiative of the investor or its representative without any solicitation made by the AIF or its AIFM. The burden of proof is placed on the AIFM in this regard.

The latest version of the FAQs is available on the CSSF's website.
http://www.cssf.lu/fileadmin/files/AIFM/FAQ_AIFMD.pdf

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Innovative Companies in Luxembourg are about to benefit from EUR 110 million EU-guaranteed loans

Luxembourg is a prime location for start-ups and innovative companies.

Cutting-edge infrastructures, the presence of business angels and venture capital as well as a favourable and stable tax regime (including an advantageous IP tax regime and the lowest VAT rate in Europe) are the cornerstones of Luxembourg's economy.

The country has a long track record of anticipating economic and financial trends and welcoming innovative industries and businesses from all over the world.

In the first Semester 2015, the European Investment Fund ("**EIF**") has signed two agreements with Banque Internationale à Luxembourg S.A. ("**BIL**") and ING Luxembourg S.A. ("**ING**") in order to provide a total of EUR 110 million of loans over a two year period to (i) innovative small and medium sized companies ("**SME**") and (ii) Small Mid-cap companies ("**Small Mid-cap**").

According to these agreements, the EIF will cover 50% of all the losses that BIL and ING might incur on any loan backed by the InnovFin SME Guarantee (the "**Guarantee**").

1. Key elements:

1.1. Eligible loans:

Term loans, revolving facilities and financial leases (refinancing loans are excluded) are eligible to benefit from the Guarantee, provided that they are used for the following purposes:

- investments, such as the acquisition of tangible and intangible assets (including goodwill);
- the provision of working capital; and
- business transfers (up to 100% of the purchase price of a target company).

1.2. Eligible borrowers:

1.2.1. Primary criteria:

- Size of the borrower: the borrower must either be (i) an SME with less than 250 employees (at the SME's group level) and have an annual turnover below EUR 50 million or a balance sheet total below EUR 43 million or (ii) a Small Mid-cap (*i.e.* a company that is not an SME and that has less than 499 employees).
- Nationality of the borrower: ING requires that the borrower is incorporated in Luxembourg. BIL requires that the borrower is incorporated in the greater-region (SaarLorLux-Wallonia).
- Amount of the loan: at least EUR 25,000, up to a maximum of EUR 7.5 million.
- Maturity of the loan: at least 1 year, up to a maximum of 10 years.

1.2.2. Innovation related criteria (non-cumulative)

The EIF has established the following eligibility criteria:

- The borrower is an SME and intends to use the loan to invest in producing or developing new or substantially improved products, processes or services that are innovative and where there is a risk of technological or industrial failure as evidenced by an evaluation carried out by an external expert, or
- The borrower must be a "fast-growing enterprise", which is an SME or a Small Mid-cap operating in a market for less than 12 years following its first commercial sale and with an average annualised endogenous growth in employees or in turnover greater than 20% a year, over a three-year period, and with ten or more employees at the beginning of the observation period, or
- The borrower is an SME or a Small Mid-cap operating in a market for less than 7 years following its first commercial sale and its R&I costs represent at least 5% of its total operating costs in at least one of the three preceding years or in the case of a start-up enterprise without any financial

history, in the audit of its current fiscal period, as certified by an external auditor, or

- The borrower shall have a significant innovation potential or be an "R&I-intensive enterprise", by satisfying at least one of the following conditions:

  - The borrower's R&I annual expenses are equal or exceed 20% of the loan amount as per the borrower's latest certified financial statements, under the condition that the borrower's business plan indicates an increase of its R&I expenses at least equal to the loan amount; or
  - The borrower undertakes to spend an amount at least equal to 80% of the loan amount on R&I activities as indicated in its business plan and the remainder on costs necessary to enable such activities; or
  - The borrower has been formally awarded grants, loans or guarantees from European R&I support schemes or through their funding instruments or regional, national research or innovation support schemes over the last thirty-six (36) months, under the condition that the loan is not covering the same expense; or
  - The borrower has been awarded an R&D or Innovation prize provided by an EU institution or an EU body over the last twenty-four (24) months; or
  - The borrower has registered at least one technology right (such as patent, utility model, design right, topography of semiconductor products, supplementary protection certificate for medicinal products or other products for which such supplementary protection certificates may be obtained, plant breeder's certificate or software copyright) in the last twenty four (24) months and the loan purpose is to enable, directly or indirectly, the use of this technology right; or
  - The borrower is an early stage SME and has received an investment over the last twenty-four (24) months from a venture capital investor or from a business angel being a member of a business angels network; or such venture capital investor or business angel is a shareholder of the borrower; or
  - The borrower requires a risk finance investment which, based on a business plan prepared in view of entering a new product or geographical market, is higher than 50% of its average annual turnover in the preceding 5 years; or
  - The borrower is an SME and its R&I costs represent at least 10% of its total operating costs in at least one of the three preceding years, or in the case of a start-up enterprise without any financial history, in the audit of its current fiscal period, as certified by an external auditor; or
  - The borrower is a Small Mid-cap and its R&I costs represent (i) at least 15% of its total operating costs in at least one of the three preceding years; or (ii) at least 10% per year of its total operating costs in the three preceding years.

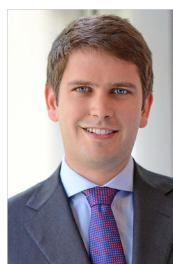
2. Key advantages:

- Guarantee backed loans offer the most competitive interest rates;
- Guarantee backed loans offer a high level of transparency (*e.g.* the loans' repayment conditions, interest rates, etc.);
- Guarantee backed loans will facilitate access to funding at an earlier stage;
- Guarantee backed loans may be complementary to angel investor or venture capital funding (*e.g.* business angels might team-up with the banks offering Guarantee backed loans).

3. Target beneficiaries of the Innov Fin SME Guarantee (i.e. potential borrowers):

- Research-based and innovative SMEs;
- Companies with a real commitment into innovation; and
- Companies having already raised funds (VC/BA).

The Guarantee provides an unprecedented opportunity for innovative SMEs to get access to cheap capital.



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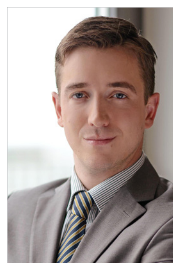

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