ATOZ

TAX ADVISERS LUXEMBOURG

INSIGHTS

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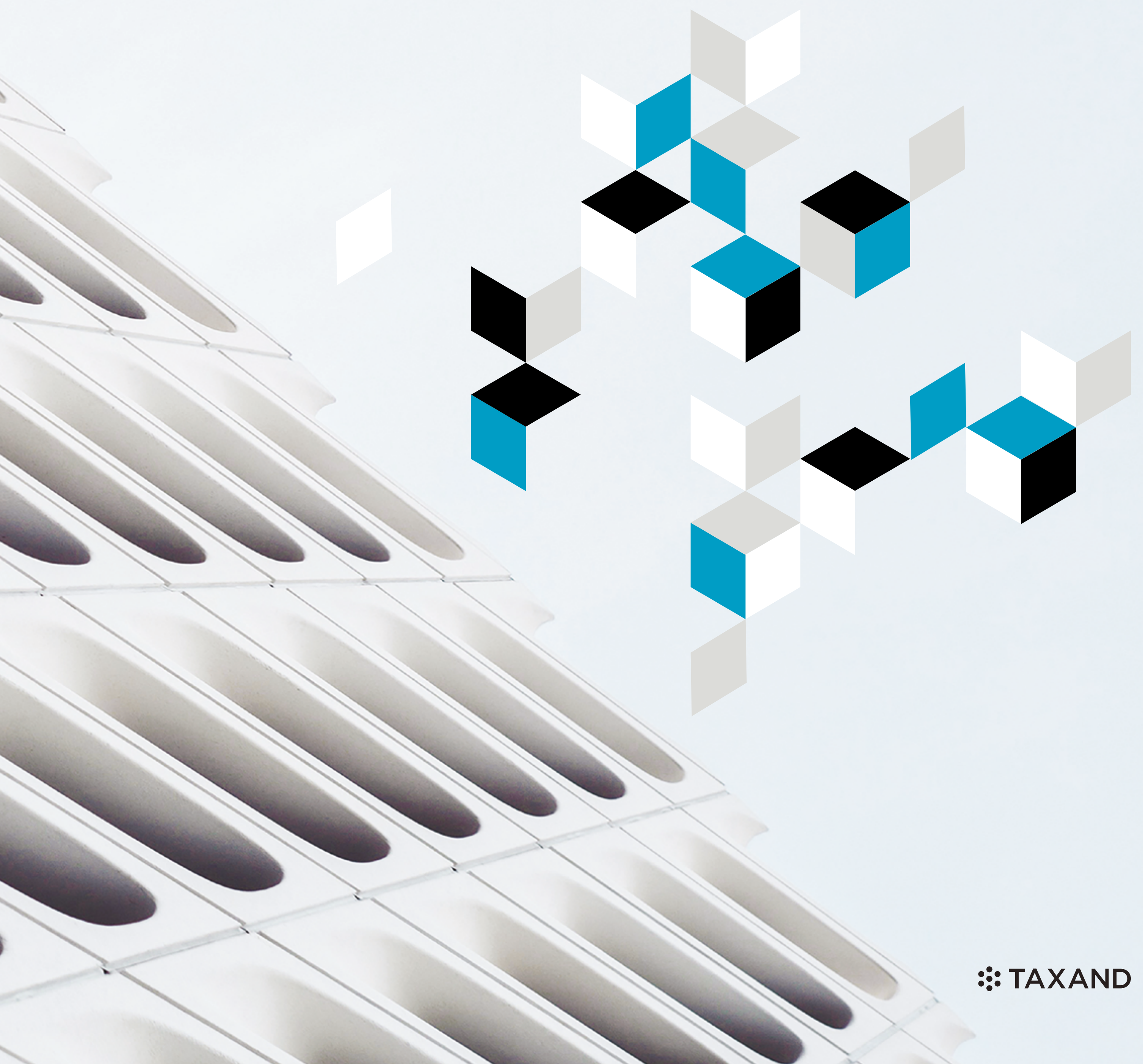

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EDITORIAL

Greetings,

The last couple of months have been atypical and unprecedented, evolving in ways none of us could have imagined. Public health and economic development concerns have become the most important priority across the world. Luxembourg is no exception, recently recognising that now is not the right time to increase taxes and/or perform big tax reforms.

A number of recent news items are summarised below and described in more detail in this newsletter.

On 14 October 2020, the 2021 budget draft law was presented to Parliament. The draft budget introduces a number of important tax measures, some of which were already announced in the 2018 coalition agreement: changes in the taxation of Luxembourg real estate investments held by investment funds, repeal of the "warrant" regime, reform of the impatriate regime and introduction of a reduced rate of subscription tax for sustainable funds.

A draft law introducing a new rule denying the corporate income tax deduction of interest and royalty paid to entities in non-cooperative tax jurisdictions, should soon be passed.

On 6 October 2020, the Court of Justice of the European Union ruled on questions raised by the Administrative Court of Luxembourg in relation to the 2014 Luxembourg law on exchange of information upon request. The Court decided that law partly infringed the right to an effective remedy and provided a definition of the concept of "foreseeable relevance" required for a request for exchange of information to be valid.

The cost of the health crisis makes it urgent for most countries to find new sources of income. The pressure on international organisations to find a global solution to tax the digital economy is increasing.

From a corporate legal perspective, the Covid-19 pandemic continues to impact the governance of legal entities. The Luxembourg Government decided to extend the possibility for companies and other legal entities to hold statutory meetings remotely until 30 June 2021.

The Luxembourg Government recently presented a draft law to modernise the law of 6 April 2013 on dematerialised securities. This is part of a continued modernisation of the legal framework of financial transactions in the context of the digitalisation and new technologies.

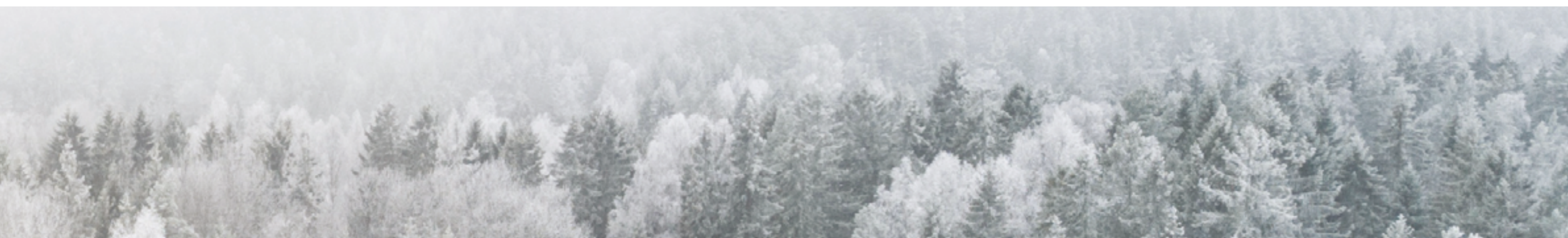
From a regulatory point of view, the European Securities and Markets Authority have made some recommendations to the European Commission on amendments of the Alternative Investment Fund Managers Directive that are needed in order to remove some important issues identified since the implementation of the AIFMD.

Finally, given the significant impact it had on the regulatory environment and on investment managers, we review Luxembourg CSSF circular n°18/698 (23 August 2018) relating to the authorisation and organisation of investment fund managers.

We hope you enjoy reading our insights.

Stay safe.

The ATOZ Editorial Team



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Budget 2021: tax measures

OUR INSIGHTS AT A GLANCE

- On 14 October 2020, the 2021 budget draft law (the "draft law") was presented to Parliament. Given the current context of crisis, the Government decided that it was not the right time to increase taxes and/or perform a big tax reform and decided to postpone the introduction of some expected tax measures such as the reform of the tax class system for individuals. Therefore, the Luxembourg Government gives a positive message that increasing taxes now is not the right way to recover from the crisis. This is consistent with international recommendations.
- The draft budget still introduces a number of important tax measures, some of which were already announced in the 2018 coalition agreement: changes in the taxation of Luxembourg real estate investments held by investment funds, repeal of the "warrant" regime, reform of the impatriate regime and introduction of a reduced rate of subscription tax for sustainable funds.
- While it is true that some taxes will be increased (e.g. taxation of income and gains on Luxembourg real estate assets held by exempt investment funds, taxation of certain real estate transfers, bonuses paid by "warrants"), the 20% new tax on income and gains arising from Luxembourg real estate should have a limited financial impact for the investment fund industry, given that only very few Luxembourg funds invest in Luxembourg real estate assets.

On 14 October 2020, the 2021 budget draft law (the "draft law") was presented to Parliament. Given the current context of crisis, the Government decided that it was not the right time to increase taxes and/or perform a big tax reform and decided to postpone the introduction of some expected tax measures such as the reform of the tax class system for individuals. However, the draft budget still introduces a number of important tax measures, some of which were already announced in the 2018 coalition agreement: changes in the taxation of Luxembourg real estate investments held by investment funds, repeal of the "warrant" regime, reform of the impatriate regime and the introduction of a reduced rate of subscription tax for sustainable funds. We provide an overview of the main tax measures to be introduced as from 2021. However, the proposed rules may still evolve throughout the legislative process.

Real estate taxation

- **Taxation of Luxembourg real estate investments held by certain investment funds**

With effect as from 1 January 2021, a new annual 20% real estate withholding tax *(prélèvement immobilier)* will be levied on income and gains arising from real estate assets situated in Luxembourg and realised directly or indirectly by certain investment vehicles (hereafter "Investment Vehicles").

The new real estate withholding tax will apply to the following Investment Vehicles:

- Undertakings for Collective Investment ("UCI") within the meaning of Part II of the law of 17 December 2010 (except Luxembourg partnerships, *sociétés en commandite simple*, "SCS");
- Specialised Investment Funds ("SIF") within the meaning of the law of 13 February 2007 (except Luxembourg partnerships, *sociétés en commandite simple*, "SCS"); and
- Reserved Alternative Investment Funds ("RAIF") within the meaning of article 1 of the law of 23 July 2016 (except Luxembourg partnerships, *sociétés en commandite simple*, "SCS"). Since the draft law specifies that the new tax is an exception to the provisions of article 45 of the RAIF law, it is our understanding that the new tax will only apply to those RAIFs which are exempt from

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corporate income tax based on article 45 of the RAIF Law and not to the fully taxable ones only investing in risk capital and subject to the specific tax rules of article 48 of the RAIF law.

The real estate withholding tax will only apply to the extent that the Investment Vehicle has a personality separate from those of its partners (typically excluding FCPs or SCSp). In addition, as mentioned above, Investment Vehicles set up as an SCS are expressly out of the scope of the measure.

The Investment Vehicle will be subject to an annual real estate withholding tax of 20% on income arising from Luxembourg real estate assets (rental income and capital gains) held directly or indirectly through tax transparent entities within the meaning of article 175-1 of the Income Tax Law ("ITL") or through FCPs.

The real estate withholding tax will also apply to gains realised by the Investment Vehicle on the disposal of an interest in the 175-1 ITL tax transparent entity or of units in the FCP but only up to the portion of the gain corresponding to the value increase of the Luxembourg real estate asset.

In addition, when a Luxembourg real estate asset is held by an Investment Vehicle through a chain of several tax transparent entities within the meaning of article 175-1 ITL or FCPs, the Luxembourg Investment Vehicle will also be subject to the 20% real estate withholding tax on the gains realised on the disposal of any indirect interest through the chain but only up to the portion of the gain corresponding to the value increase of the Luxembourg real estate asset.

When income or gains are realised indirectly, the taxable income or gain is computed in proportion with the interest held in the entity(ies) holding the Luxembourg real estate.

The following new reporting and payment obligations will be introduced in respect of the new real estate withholding tax:

- At the latest on 31 May of the year following the one during which the real estate income has been realised, the Investment Vehicle will have to file a tax return with the withholding tax office of the Luxembourg tax authorities *(Administration des Contributions Directes, Bureau de la retenue d'impôt sur les intérêts)* including detailed information on the income subject to the real estate tax as well as on the amount of tax to be paid; an external auditor *(réviseur d'entreprise agréé)* will have to certify in a report that the real estate income has been computed in accordance with the provisions of the law introducing the real estate withholding tax. This report will have to be filed together with the tax return.

- The related real estate withholding tax will have to be paid at the latest on 10 June.

- All Investment Vehicles, no matter whether they realise (directly or indirectly) Luxembourg real estate income and no matter whether they hold (directly or indirectly) Luxembourg real estate assets, have to file an additional return including information on whether they have been (or not) holding (directly or indirectly) Luxembourg real estate assets during the calendar years 2020 and 2021. This tax return has to be filed by 31 May 2022 at the latest.

- Finally, Investment Vehicles must inform the Luxembourg tax authorities if they change their legal form and become a tax transparent entity within the meaning of article 175-1 ITL or an FCP in the course of the calendar years 2020 and 2021. This requirement only applies to the extent that the Investment Vehicles hold (directly or indirectly) at least one Luxembourg real estate asset at the time of the change of their legal form.

- **Real estate registration taxes on "share deals"**

Currently, the contribution remunerated by shares of a real estate asset situated in Luxembourg to a Luxembourg or foreign civil or commercial company upon its incorporation or capital increase (*Apport pur et simple*, so-called "share deal") is subject to a proportional registration tax of 0.5% + 2/10 as well as to 0,5% transcription tax (i.e. a total of 1.1% registration taxes) while the contribution of a real estate asset situated in Luxembourg (so-called "asset deal") remunerated by other means than shares *(Apport à titre onéreux)* is subject to a proportional registration tax of 5% + 2/10 as well as to 1% transcription tax (i.e. a total of 7% registration taxes).

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With effect as from 1 January 2021, the tax treatment of share deals (in the context of investments in Luxembourg real estate) will be amended to reduce the inequal tax treatment between share deals and asset deals for registration taxes.

In the case of capital contributions of real estate assets to a civil or commercial company, the registration duties will be increased from 0.5% + 2/10 to 2% +2/10 and the transcription tax will be increased from 0.5% to 1%. As a consequence, registration taxes applicable to such capital contributions will become 3 times higher (3.4% instead of 1.1%).

- **SPF regime & real estate investments**

With effect as from 1 July 2021, private wealth management companies ("SPF") will not be allowed to hold real estate investments indirectly via one or more (Luxembourg or foreign) partnerships or FCPs (direct investments into real estate are already prohibited by the SPF law of 11 May 2007).

New amortisation and deduction rules for residential investments

The accelerated amortisation rules applicable to rental housing investments will be amended with effect as from tax year 2021. The amortisation rate for new real estate investments allocated to rental housing will be brought down from 6 to 4% as from tax year 2021. To be considered as a new residential investment, the real estate cannot be older than 5 years (instead of 6 years currently).

These new rules will also apply to expenditures made for the renovation of old dwellings, provided that they do not exceed 20% of the acquisition price or cost of the building. However, for renovation of rental accommodation to allow use of sustainable energy, an amortisation rate of 6% of the expenses (instead of the current 4% of 20% of the renovation expenses) will apply.

In addition to the amendment of the amortisation rules, the draft law introduces a special deduction for investments in real estate not older than 5 years and allocated to rental housing *(abattement immobilier special)*. This deduction amounts to 1% of the value used as a basis for the calculation of the accelerated depreciation of 4%, without however being able to exceed EUR 10,000 (i.e. 1% of EUR 1.000.000).
As a result, real estate investments in rental housing not older than 5 years will benefit from a combined amortisation and deduction as follows:
Value < 1.000.000: 5%
Value > 1.000.000: 4% plus a deduction of EUR 10.000.

Employee taxation

- **Stock options/warrants**

The so called "warrant regime", which evolved from a circular introduced in 2002, will be repealed as from 1 January 2021. The repeal of the circular was announced in the commentary to the draft law but it will be necessary to await the release of a repealing circular (most probably before year-end) in order to know more about the impact of the repeal, especially on the stock option plan regime which is also covered in the circular to be repealed.

- **Employee profit share**

With effect as from tax year 2021, a new profit share (*prime participative*) will be introduced for employees and will be 50% exempt under certain conditions.

The amount of profit share payable in the form of a bonus and benefiting from the 50% exemption will be subject to the 2 following cumulative limits:

- The total amount of profit share paid by the employer to its employees will not be able to exceed 5% of the accounting profits of the employer as of the end of the accounting year preceding the allocation of the profit share; and

- The amount of profit share paid by the employer to an employee will not be able to exceed 25% of the annual salary (excluding the amount of profit share) of the employee concerned.

In our view, these two limits should be interpreted in such a way that should one or two of them be exceeded, only the exceeding part will be fully subject to tax and the part up to the limits will still benefit from the 50% exemption.

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This approach should also be true in respect of the tax deduction of the profit share at the level of the employer: while the draft law specifies that the profit share within the meaning of the new draft law article is tax deductible at the level of the employer, the part of the profit share which exceeds the 5% and 25% limits mentioned above should still remain tax deductible at the level of the employer under the standard tax deduction rules applicable to the payment of salary and bonuses.

As soon as the profit share has been put at the disposal of the employees, the employer will have to provide the Luxembourg tax authorities with a list of all employees who benefited from it as well as with all the information needed to evidence that the conditions required to benefit from the 50% exemption are met.

- **Impatriate regime amended**

With effect as from tax year 2021, the tax regime of impatriates will be amended. It will no longer be governed by a circular but, instead, by a new article of the Luxembourg income tax law.

A 50% exempt impatriate premium will be introduced which an employer will be able to grant under certain conditions to its employees. To benefit from the partial exemption regime, the premium should not exceed 30% of the annual remuneration of the impatriate.

Most of the conditions of the impatriate regime currently in force will remain unchanged. However, to benefit from the regime under the new rules, the impatriate will have to have an annual remuneration of minimum EUR 100,000 (instead of EUR 50,000) and he/she will be able to benefit from the regime during a time period of up to 8 tax years (instead of currently 5 tax years).

Green taxation

- **Investment funds & subscription tax**

As from 1 January 2021, sustainable funds set up as UCIs within the meaning of the law of 17 December 2010 will benefit from a lower rate of subscription tax *(taxe d'abonnement)* - the standard rate being 0.05% - which will vary from 0.04 to 0.01% of the net asset value ("NAV"), depending on the level of sustainable activity (within the meaning of article 3 of EU Regulation 2020/852) of the fund or its individual compartment:

- 0.04% if at least 5% of the NAV of the fund, or of its individual compartment, is invested in sustainable economic activities;
- 0.03% if at least 20% of the NAV of the fund, or of its individual compartment, is invested in sustainable economic activities;
- 0.02% if at least 35% of the NAV of the fund, or of its individual compartment, is invested in sustainable economic activities; and
- 0.01% if at least 50% of the NAV of the fund, or of its individual compartment, is invested in sustainable activities.

Only the portion of the net assets invested in sustainable economic activities will benefit from the reduced rates mentioned above.

The portion of sustainable economic activities will be determined based on the situation as of the last day of the financial year of the UCI and will have to be certified by an external auditor.

- **Environmental taxation**

As from 1 January 2021, a CO2 tax will be introduced which should add around 5 cents per litre to the cost of petrol and diesel.

- **Tax credits**

As a measure to counterbalance the effects of environmental taxation on Luxembourg households, as from tax year 2021, the income tax credits available to employees, self-employed and retired persons which vary progressively depending on the level of annual income will be increased by EUR 96.

Other measures

- **Tax consolidation regime amended to reflect latest CJEU case law**

The provisions of the Luxembourg corporate income tax law dealing with the tax consolidation regime will be amended

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with effect as from tax year 2020 to reflect the recent decision of the CJEU regarding the consequences of the change from "vertical" to "horizontal" tax consolidation. The new provision confirms that the change will not entail any negative tax consequences for the members of the tax consolidated group, provided certain conditions are met.

- **Vat exemption for small businesses extended**

The VAT exemption *(Franchise)* regime which applies in accordance with article 57 of the Luxembourg VAT law to small businesses currently defined as businesses with an annual turnover not exceeding EUR 30,000, will apply as from 1 January 2021 to businesses with a turnover not exceeding an annual turnover of EUR 35,000.

Implications

With the tax measures included in its 2021 budget, the Luxembourg Government gives a positive message that increasing taxes now is not the right way to recover from the crisis. This is consistent with international recommendations. The majority of taxpayers should not suffer a higher tax burden and should be able to keep on investing to achieve a financial recovery in the longer term.

While it is true that some taxes will be increased (e.g. taxation of income and gains on Luxembourg real estate assets held by exempt investment funds, taxation of certain real estate transfers, bonuses paid by "warrants"), the reasons of such tax increases are different: it is more about removing inappropriate or anomalous tax treatments that developed over time, rather than collecting additional tax revenues. In particular, the 20% new tax on income and gains arising from Luxembourg real estate should have a limited financial impact for the investment fund industry, given that only very few Luxembourg funds invest in Luxembourg real estate assets.

As a last remark, we are of the view that some of the positive measures introduced could be improved. For example, the new employee profit share regime has a scope of application which is, to us, too restrictive: the limitation to 5% of the profits of the employer means that start-ups, small businesses and companies not aiming at making profits because of the role they play within a group (e.g. cost centres) will often not be able to make their employees benefit from the regime. Therefore, some adjustments to the regime, either in the course of the legislative process or as part of a subsequent reform, would be welcome.

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Measure denying the tax deduction of interest and royalties to entities in blacklisted jurisdictions: scope updated

OUR INSIGHTS AT A GLANCE

- A draft law adopted by the Luxembourg Government in March 2020, which should be passed soon, will introduce a new Luxembourg tax measure denying under certain conditions the corporate income tax deduction of interest and royalty expenses directed at entities located in non-cooperative tax jurisdictions.
- The list of non-cooperative tax jurisdictions is determined at EU level and updated twice a year. Following the latest update of the EU list on 6 October 2020, the scope of the new measure has changed: while interests and royalties to entities located in the Cayman Islands and Oman will finally be out of the scope of the measure, interests and royalties to entities located in Anguilla and Barbados will now be within the scope when the measure will enter into force, i.e. on 1 January 2021.
- Given the regular updates to the list, the scope of application of the new rules will keep on evolving, even after the new rules have entered into force. The timing of transactions will be key to determine the potential Luxembourg tax impact and the analysis will change from time to time.
- Therefore, Luxembourg taxpayers with investments into and from non-cooperative jurisdictions should seek advice from their tax advisers in order to analyse the potential impact of the new provisions on their investments and take action, if necessary. Also the evolution of the legislation of jurisdictions under the radar of EU institutions should be closely monitored in order to anticipate an addition to or a removal from the EU list of non-cooperative tax jurisdictions in the future.

A draft law adopted by the Luxembourg Government in March 2020, which should be passed soon, will introduce a new Luxembourg tax measure denying under certain conditions the corporate income tax deduction of interest and royalty expenses directed at entities located in non-cooperative tax jurisdictions.

Background

The list of non-cooperative tax jurisdictions is determined at EU level. It is a result of a thorough screening and dialogue process with non-EU countries, to assess them against agreed criteria for good governance relating to tax transparency, fair taxation, the implementation of OECD BEPS measures and substance requirements for zero-tax countries. The list is updated twice a year, taking into consideration the evolving deadlines for jurisdictions to deliver on their commitments and the evolution of the listing criteria that the EU uses to establish the list. Given those regular updates, the scope of application of the new Luxembourg measure will constantly evolve over time.

As of 6 October 2020 (date of the latest update of the list), the list included the twelve following jurisdictions: American Samoa, Anguilla, Barbados, Fiji, Guam, Palau, Panama, Samoa, Seychelles, Trinidad and Tobago, US Virgin Islands and Vanuatu.

In parallel, in December 2019, the Council produced guidance on further coordination of national defensive measures in the tax area regarding non-cooperative jurisdictions and invited EU Member States to apply one of the following legislative defensive measures in taxation vis-à-vis the listed jurisdictions as of 1 January 2021, with the aim of encouraging those jurisdictions' compliance with the Code of Conduct screening criteria on fair taxation and transparency:

- non-deductibility of costs;
- CFC rules;
- withholding tax measures;
- limitation of the participation exemption on profit distributions.

It is in this context that the Luxembourg Government has decided to introduce the first of these measures, i.e. the non-deductibility of costs.

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Presentation of the new measure

As from 1 January 2021, interest and royalties due to entities located in non-cooperative tax jurisdictions will no longer be tax deductible, if the following cumulative conditions are met:

- The beneficiary of the interest or royalty is a collective undertaking within the meaning of article 159 Income Tax Law, “ITL”, which means that tax transparent partnerships are out of scope; if the beneficiary is not the beneficial owner, then the beneficial owner has to be taken into account;
- The beneficiary of the interest or royalty is an associated enterprise within the meaning of article 56 ITL; and
- The collective undertaking which is the beneficiary of the interest or royalty is established in a country or territory which is on the list of non-cooperative tax countries and territories.

Interest and royalties will remain tax deductible to the extent that the taxpayer can demonstrate that the operation to which the interest or royalties relate has been put in place for valid economic reasons which reflect economic reality.

Interest is defined as follows: “interest due relating to debt claims of every kind, whether or not secured by a mortgage and whether or not carrying a right to participate in the debtor’s profits, and, in particular, interest from bonds or debentures, including premiums and prizes attaching to such securities. Penalties for late payments shall not be regarded as interest payments.”

Royalty is defined as follows: “remuneration of any kind due as a consideration for the use of, or the right to use, any copyright of literary, artistic or scientific work including cinematograph films, any patent, trademark, design or model, plan, secret formula or process, or for information concerning industrial, commercial or scientific experience.”

These two definitions are largely inspired by the definitions included in the EU Interest and Royalty Directive and in the OECD Model Tax Convention.

Timing for application

The new measure will apply to interest and royalties due as from 1 January 2021.

The list of non-cooperative tax jurisdictions to be taken into account will be the latest EU list available at the time of the entry into force of the law. Since no further update of the list is expected before year-end, the countries to be taken into account as from 1 January 2021 will be the twelve countries mentioned above and listed as of 6 October 2020.

As from 1 January of the following years, the same principle will apply, i.e. the measure will apply to interest and royalties due to countries listed as of the latest list available at that time and published in the Official Journal of the European Union.

What is the effect of a country being added or removed from the list?

- Countries added will be taken into account for interest and royalties due as from 1 January of the following year (i.e. there will be no retroactive nor immediate effect but only an impact as from the following calendar year);
- Countries removed will no longer be taken into account for interest and royalties due as of the date of the publication of the relevant EU list in the Official Journal (i.e. the removal will have an immediate effect).

Implications

Luxembourg taxpayers with investments into and from non-cooperative jurisdictions should seek advice from their tax advisers in order to analyse the potential impact of the new provisions on their investments and take action, if necessary. The evolution of the legislation of jurisdictions under the radar of the EU Council should also be closely monitored in order to anticipate an addition to or a removal from the EU list of non-cooperative tax jurisdictions in the future and thus a change in the scope of application of the new Luxembourg measure.

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Exchange of information upon request: consequences of the Berlioz 2 case

OUR INSIGHTS AT A GLANCE

- On 6 October 2020, the Court of Justice of the European Union ruled on prejudicial questions raised by the Administrative Court of Luxembourg in relation to the Luxembourg law on exchange of information upon request dated 2014.
- The CJEU recognised the right to an effective remedy to information holders to which information requests are sent by tax authorities but also to taxpayers and to concerned third parties.
- The CJEU decided that the Luxembourg law infringed the right to an effective remedy to the extent information holders to whom information requests are sent cannot challenge the requests in front of a tribunal, unless they breached such requests by refusing to respond to it and being exposed to sanctions for not conforming with it.
- The CJEU also concluded that Luxembourg may disallow any direct action against an information order by a taxpayer provided the taxpayer has a right of appeal against any subsequent tax assessment at the end of the investigation, and by third parties provided that such third parties have an alternative remedy enabling them to obtain effective respect of their fundamental rights, such as an action to establish liability.
- Finally, the CJEU gave details on the concept of foreseeable relevance of a request for exchange of information.

On 6 October 2020, the Court of Justice of the European Union ("CJEU") ruled on prejudicial questions raised by the Administrative Court of Luxembourg (the "Court") in relation to the Luxembourg law on exchange of information upon request. These questions relate to the law of 25 November 2014 on exchange of information upon request (the "2014 Law") which was amended since then, following the well-known Berlioz case law, to bring it in line with the European law. What are thus the consequences of this new CJEU decision?

Background

It is not the first time that the Luxembourg rules on exchange of information upon request have been under scrutiny by the CJEU. On 16 May 2017, in the Berlioz case (C-682/15), the CJEU judged that the Luxembourg rules on exchange of information upon request in force at that time were not in line with the Charter of Fundamental Rights of the European Union (the "Charter"). According to the CJEU, the right to an effective remedy and to a fair trial laid down in article 47 of the Charter must be interpreted as meaning that a relevant person on whom a pecuniary penalty has been imposed for failure to comply with an administrative decision directing that person to provide information ("information order") in the context of an exchange between national tax administrations pursuant to Directive 2011/16 is entitled to challenge the legality of that decision. However, such challenge was prohibited under the 2014 Law.

As a result, several amendments to the 2014 Law were introduced by the law of 1 March 2019 (the "2019 Law"). Now, based on the new rules, information holders can contest information requests received from the Luxembourg tax authorities and the Luxembourg tax authorities must check the foreseeable relevance of the information requested by foreign tax authorities (see ATOZ Insights February 2019, May 2019 and June 2017 for more details).

However, on 14 March 2019, less than one month after the 2014 Law was amended, the Court referred

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new questions to the CJEU in relation to said law. On 6 October 2020, the CJEU answered these prejudicial questions in what is called the "Berlioz 2 case" (Joined Cases C 245/19 and C 246/19).

The "Berlioz 2 case"

- **Existence of a judicial remedy against information requests for the information holder**

One of the prejudicial questions referred to the CJEU relates to the compliance of the 2014 Law (before being amended by the law of 1 March 2019) with the Charter to the extent that the Luxembourg rules excluded any recourse, including judicial, by the third party holder of the information against the request of the Luxembourg tax authorities to provide information in order to respond to a request for exchange information from another EU Member State.

In the "Berlioz 2 case", the CJEU recognises the right to an effective remedy for information holders to whom information requests are sent by tax authorities and contemplates that none of the provisions of the Directive 2011/16, that is implemented by the 2014 Law, aims to limit such right. On the contrary, the Directive 2011/16 refers to the European regulation on the protection of individuals with regard to the processing of personal data which emphasises that any person should have the right to an effective remedy in the case that the rights guaranteed are breached and any limitation to the rights and liberties guaranteed by the Charter should respect the core content of these latter.

According to the CJEU, the core content of the right to an effective remedy includes amongst others, the possibility to have access to a competent tribunal that will assess all the factual and legal questions relevant to solve the issue raised. Moreover, to have access to this tribunal, people should not be forced to infringe a rule or a legal obligation and expose themselves to the sanction attached to this offense.

As a result, the CJEU confirms its decision taken in the Berlioz case. Under the 2014 Law, information holders to whom information requests were sent did not benefit from the right to an effective remedy because they could not challenge the requests in front of a tribunal, unless they breached such requests by refusing to respond to it and being exposed to sanctions for not conforming with it.

- **Existence of a judicial remedy against information requests for any person concerned (and not only the information holder)**

The draft law released at the end of 2017 in reaction to the Berlioz case law in respect of the lack of an effective judicial remedy initially reintroduced a possibility for any person concerned by the information request to contest the information request (e.g. on the ground that the information request would not meet the foreseeable relevance principle) before Luxembourg courts. However, over the legislative process, the Luxembourg legislator decided to go a step back and to only grant this possibility to the information holder in the 2019 Law and no longer to any other person concerned (such as the taxpayer itself).

Questions dealt with by the CJEU referred precisely as to whether the Charter prohibits a rule that precludes any recourse, including judicial, by the taxpayer under investigation in the requesting Member State and by any third party concerned, against a decision through which the competent authority of that Member State requires an information holder to provide information with a view to respond to a request for exchange of information from another Member State.

According to the CJEU, like for the information holder, the right to an effective remedy should be recognised for the taxpayer under investigation and any third party concerned and such right may be limited by excluding such taxpayer or third party from bringing a direct appeal against the information order if the scope of this limitation is clearly and precisely defined by the law.

Nevertheless, the CJEU makes a difference between the information holder on one hand, and the taxpayer under investigation and any third party concerned on the other hand. Indeed, the latter are not the addressees of the order to provide information and are not subject to any

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legal obligation by the request, nor, therefore, to the risk of being penalized in the event of non-compliance with it. Therefore, they are not forced to infringe the law to be able to exercise their right to an effective remedy. And the CJEU concludes that Luxembourg may thus disallow any direct action against an information order by a taxpayer, provided the taxpayer has a right of appeal against any subsequent tax assessments at the end of the investigation, and by third parties, provided that such third parties have an alternative remedy enabling them to obtain effective respect of their fundamental rights, such as an action to establish liability.

Indeed, according to the CJEU, the right to an effective remedy does not imply, as such, that the holder of that right has a direct remedy with the main purpose being to challenge a given measure, in so far as there is elsewhere, before the various competent national courts, one or more means of appeal enabling it to obtain, incidentally, a judicial review of this measure ensuring respect for the rights and freedoms guaranteed by Union law, without having to run the risk of being sanctioned for this purpose in the event of non-compliance with the measure in question. According to the CJEU, this approach would also be in line with the objective of fighting international tax evasion and avoidance.

The CJEU's decision contrasts with the opinion of the Advocate General ("AG") Kokott in this case, according to which, the taxpayer and the third parties should also have a right to challenge such a decision in front of the courts of the requested Member State and the exclusion of legal protection for the taxpayer concerned and for concerned third parties infringes article 47 of the Charter. According to the AG, the possibility of challenging any subsequent tax assessments does not provide sufficient protection of the taxpayer's fundamental right to data protection.

'foreseeable relevance'

Finally, the Court ruled that an information order sent with a view to follow up on a request for exchange of information is to be regarded as relating to information that is 'foreseeably relevant', within the meaning of Directive 2011/16, where it states:

- the identity of the person holding the information in question;
- the identity of the taxpayer subject to the investigation giving rise to the request for exchange of information;
- the period covered by that investigation; and
- where it relates to contracts, invoices and payments which, although not expressly identified, are defined by personal, temporal and material criteria establishing their links with the investigation and the taxpayer subject to that investigation.

According to the CJEU, that combination of criteria is sufficient to consider that the information requested is not manifestly devoid of any foreseeable relevance, so that a more precise definition of that information is not necessary.

Consequences

As the new version of the 2014 Law, modified by the 2019 Law, already deals with the issue, by allowing the information holder to contest information requests received from the Luxembourg tax authorities, the answers of the CJEU on this specific topic should have no practical consequence. It is indeed no longer debatable that the right to an effective remedy implies that the national court must be able to examine the legality of the injunction decision in order to satisfy the requirements of Article 47 of the Charter.

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It remains to be seen how the Luxembourg courts will apply the Berlioz 2 case law in practice and how they will verify that taxpayers and third parties concerned have, in concreto, the "possibility to obtain, incidentally, a judicial review of this measure ensuring respect for the rights and freedoms guaranteed by Union law". Taking into account that taxpayers targeted by information requests are mainly foreigners, this appreciation will be challenging for the Luxembourg courts. And what if their conclusion is that a taxpayer or a third party concerned does not have such possibility?

Finally, in a case involving an information request by the Swiss tax authorities, on 10 January 2019, the Luxembourg Tribunal referred two questions to the Luxembourg Constitutional Court on the conformity of the 2014 Law to the Luxembourg Constitution in so far as it does not allow for an injunction of the Luxembourg tax authorities to provide information to be challenged. As of today, the Luxembourg Constitutional Court has not yet ruled on this case and this decision could still change the state of play…

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Digital tax: what is the state of play?

OUR INSIGHTS AT A GLANCE

- Addressing the tax challenges raised by digitalisation is one of the top priorities for the OECD/G20 Inclusive Framework and the EU Commission.
- Despite the fact that good progress has been made at the level of the OECD's initiatives, called Pillar One and Pillar Two, important technical and administrative issues as well as policy issues remain to be solved.
- If these issues are not addressed successfully by mid-2021 at OECD level, there is no doubt that the EU Commission as well as various individual countries will propose their own digital levy.

Since years now, addressing the tax challenges raised by digitalisation is one of the top priorities for the OECD/G20 Inclusive Framework, and has been a key area of focus of the BEPS Project since its beginning. The OECD has been dedicated to finding a comprehensive, consensus-based solution to the challenges arising from digitalisation and committed to deliver this solution before the end of 2020. In the meantime, the European Commission agreed to hold on with its proposal to tax the digital economy until an agreement will be reached at OECD level.

So, where are we?

On 12 October 2020, the OECD published a Report on the Pillar One Blueprint and a Report on the Pillar Two Blueprint dealing with tax challenges arising from digitalisation (the "Reports") which reflect a consensus on various key policy features, principles and parameters of both Pillars.

Pillar One deals with the re-allocation of taxing rights on MNE's profits from automated digital services or "consumer facing businesses". In this framework, Pillar One tries to address the questions of business presence and activities without physical presence, of the place where tax should be paid and on what basis and which share of the profits could or should be taxed in the jurisdictions where customers and/or users are located.

On the other hand, Pillar Two targets global anti-base erosion mechanisms. It aims to help stop the shifting of profits to low or no tax jurisdictions facilitated by new technologies, to ensure that a minimum level of tax is paid by multinational enterprises (MNEs) and to level the playing field between traditional and digital companies. Pillar Two aims to give States the right to tax where other States have not exercised their primary taxing rights or where the profits are generally subject to a low effective taxation. Pillar Two is articulated around income inclusion rules and an undertaxed payment rule (referred to collectively as the Global Anti-Base Erosion ("GloBE") rules) and a subject to tax rule. (For more information on Pillar One and Pillar Two, please read our ATOZ Insights from December 2019).

Good progress has been made in respect of practical, administrative and definitional issues. The Reports provide now some additional information notably on the scope of the Pillars. In that respect, clarifications are still required. For instance, the current scope of the GloBE rules provides for an exclusion for certain ultimate parent entities, such as investment and pension funds. While the current definition of investment funds would require that such entities be subject to a regulatory regime, it would be relevant for the Fund industry in Luxembourg to get further clarification on whether unregulated investment funds may also benefit from that exclusion.

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Nevertheless, the Reports identify remaining important technical and administrative issues as well as policy issues where divergent views still need to be bridged before a political agreement be achieved. For example, while the United States proposes that Pillar One be implemented on what it refers to as a safe harbour basis, thus allowing any MNE to apply Pillar One on an optional basis, many other jurisdictions have expressed skepticism about an elective approach. Similarly, it is still necessary to find a consensus on definitive thresholds or on minimum tax rates, including on whether a phase in/transition period is appropriate and, if so, its design.

What is expected next?

The OECD aims now to address issues and come to a successful conclusion by mid-2021. For that purpose, a public consultation has been opened and the public is invited to provide written comments on the Reports by Monday 14 December 2020 at the latest. The remaining work includes resolving technical issues, developing model draft legislation, guidelines, international rules and processes as necessary. As a result, it seems an incredibly tight timeline given the complexities and issues still to be addressed.

As until now, the EU Commission actively supports the global discussions led by the OECD and the G20 but stands ready to take action if no global agreement is reached. In July 2020, the Commission announced that it will set out, before year end, the next steps, in an Action Plan for Business Taxation for the 21st century. On many occasions, the Commission re-affirmed that it will go ahead with its own digital tax early next year if the OECD does not reach a global agreement. the Commission will propose a digital levy in the first half of next year.

In parallel, the EU Commission is working on the modification of the proposal on administrative cooperation which extends EU tax transparency rules to digital platforms ("DAC7"). This proposal will ensure that Member States automatically exchange information on the revenues generated by sellers on online platforms. This exchange of information will help in implementing the OECD and EU new digital taxes as it will help tax administrations verify that those who earn money through digital platforms pay their appropriate share of taxes.

With the sanitary crisis, the need of most countries for revenue makes it urgent for them to find new income and the pressure on the OECD and the EU Commission to find a solution to tax the digital economy is increasing. In the absence of agreement, we could see various national digital service taxes arising across the world which would be very difficult to handle for most of the targeted businesses.

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COVID-19: Luxembourg extends the possibility to hold company meetings remotely until 30 June 2021

OUR INSIGHTS AT A GLANCE

- Since the Covid-19 pandemic continues to impact the good governance of legal entities, the Luxembourg Government decided to extend the possibility for companies and other legal entities to hold their corporate body meetings remotely until 30 June 2021.
- To this effect, on 25 November 2020, a draft law was passed by the Parliament which amends the law of 23 September 2020 so as to extend its application and thus the exceptional measure it provides until 30 June 2021, which allows the holding of corporate body meetings without any physical presence. The measure initially only applied until 31 December 2020.
- This new law will allow companies and other legal entities to hold their general meetings and their management body meetings remotely (i.e. without any physical presence) until 30 June 2021.

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Companies and other legal entities will be able to hold their general meetings and their management body meetings remotely (i.e. without any physical presence) until 30 June 2021 as follows:

General meetings

Even if the articles of association do not provide any such possibility and no matter the number of attendees at these meetings, until 30 June 2021, companies and any other legal entities will be able to hold their general meetings remotely. They will be able to require their shareholders and other participants to attend the meetings and exercise their rights through one or more of the following forms:

- remotely, by vote in writing or in electronic form, provided that the full text of the resolutions or decisions to be taken has been published or communicated to the participants; or
- by video conference or other means of telecommunication allowing the identification of the participants; or
- through a proxy appointed by the company.

Management body meetings

Notwithstanding any contrary provision in the articles of association, until 30 June 2021, it will also be possible to hold meetings of management bodies remotely and companies will be able to require their participants to exercise their rights remotely as follows:

- by means of written circular resolutions; or
- by video conference or any other means of telecommunications allowing the identification of participants.

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This measure will allow the bodies of any company or legal person to hold their meetings without requiring the physical presence of their members while guaranteeing their effective participation and the exercise of their rights. Remote participants will be considered as present for the purposes of computing quorums and majorities.

Implications

While the extension of the exceptional measure on the holding of corporate body meetings remotely is positive as the current Covid-19 pandemic makes it often difficult, if not impossible, to have all company meetings taking place physically, one should still manage the organisation of such meetings carefully given the potential negative tax implications of holding such meetings remotely, i.e. shift of the place of effective management of a company outside Luxembourg (for more information on these potential negative tax implications, please refer to our 23 September 2020 ATOZ Alert).

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ESMA's recommendations on the AIFMD review

OUR INSIGHTS AT A GLANCE

- On 18 August 2020, the European Securities and Markets Authority (ESMA) sent a letter to the European Commission dealing with the review of the Alternative Investment Fund Managers Directive (AIFMD).
- In its letter, ESMA used the opportunity of the AIFMD review to make some recommendations to the European Commission on the amendments needed in order to remove some important issues identified since the implementation of the AIFMD, such as issues in relation to leverage, the concept of semi-professional investors, delegation and substance and regarding the scope of entities in ESMA's register. ESMA further presented the key reporting issues identified where improvements could be made.
- While these suggested improvements would be positive as they should provide EU investors with a more secured regulatory framework, these improvements would also most probably mean an increase in the burden of AIFMs.

On 18 August 2020, the European Securities and Markets Authority (ESMA) issued a letter to the attention of Mr. Valdis Dombrovskis (ESMA's letter), the European Commission's Executive Vice-President for an Economy that Works for People, whose explicit subject is attached to the review of the Alternative Investment Fund Managers Directive (AIFMD or, as the case may be, the Directive).

As a reminder, the AIFMD[1] appeared in the European legislative and regulatory framework on 8 June 2011. The main purposes of the Directive were numerous and included, notably: (i) a greater protection of investors through the introduction of stricter compliance and reporting requirements, bound to the systemic risk analysis and (ii) the implementation of a primary regulation of alternative investment funds (AIFs) through their managers. The Directive was transposed into Luxembourg legislation by the law of 12 July 2013.

The content of ESMA's letter is twofold. Attention is (i) firstly brought to "ESMA's proposed changes to AIFMD" which include an introductory analysis of the main issues raised by the implementation of the Directive since 2011; and (ii) secondly to "ESMA's proposed changes to AIFMD regarding the reporting regime and data use", in other words to more technical aspects regarding information provided to national competent authorities (NCAs).

In this perspective, we shall discuss the concept of "leverage". Then, we will focus on the concept of semi-professional investors, which is notably subject to different approaches in Member States' laws. We shall further discuss the delegation and substance's challenges that arose and we shall lastly refer to the expected expansion of ESMA's register's scope regarding entities which should report information.

Leverage: concept and potential improvements

It is acknowledged that the AIFMD includes two measures of leverage calculation for reporting purposes. ESMA explicitly takes up the recommendations issued previously by the International Organization of Securities Commissions[2] (IOSCO) which point out a two-step approach.

The first step of such process should lead to use "baseline analytical tools to identify funds that may pose a risk to

1 Directive 2011/61/EU of the European Parliament and of the Council of 8 June 2011 on Alternative Investment Fund Managers and amending Directives 2003/41/EC and 2009/65/EC and Regulations (EC) No 1060/2009 and (EU) No 1095/2010.

2 The related IOSCO recommendations, issued in December 2019, are available at: https://www.iosco.org/library/pubdocs/pdf/IOSCOPD645.pdf

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financial stability". In accordance with the systemic risk analysis purposes of the Directive set forth above, it may be appropriate or necessary for NCAs to "capture significant leverage-related risks of a fund (or group of funds) to give regulators the tools to assess these risks for financial stability purposes". To that extent, it is understood that targeted AIFs should at least reach a certain sensitivity threshold as regards systemic risk threat. It therefore appears relevant to use proportionality's criteria.

The second step is bound to the related risk-based analysis of AIFs which would be identified within the implementation of the first step. Regulators should then resort to the two aforementioned measures of leverage calculation.

Such two-step assessment process, based on leverage, would aim at largely facilitating regulators' analysis work.

Semi-professional investors in the light of the dual approach drawn up by MIFID II[3]

MIFID II drew up a dual approach regarding investors being either (i) professional investors or (ii) retail investors.

A new concept that can be placed between these two was developed from practitioners under the term of "semi-professional investors". It is acknowledged that no such definition currently exists under the AIFMD. Within the context of its review, ESMA points out the fact that different approaches were and are still noticed in EU Member States' regulations with regards to "professional investors", which shall therefore have consequences on the definition of "semi-professional" investors.

To that end, a greater convergence of the definition of "professional investors" is duly expected, by means of clarifications, so as to align the status' treatments of such investors within the EU.

In addition, concerning the introduction of the concept of "semi-professional" investors, it is expressly reminded that "any possible introduction of any new categories of investors under the AIFMD [...] should be accompanied by appropriate investor protection rules".

Arisen challenges on delegation and substance

Two relevant matters regarding delegation and substance are addressed in this section: the extent of delegation and the use of seconded staff.

- **Extent of delegation**

It is recognised that AIFMs usually delegate collective portfolio management functions to third parties while keeping an internal control function within their ranks. Such delegation can be made within or outside the group of AIFMs. We may note that a further increase of delegation to non-EU entities is expected, mainly due to Brexit's impacts.

Some issues are raised by ESMA on delegation and substance, especially on whether authorised AIFMs are the direct employers of the staff attached to such delegated functions or not. Indeed, the majority of human and technical resources are sustained by a third party, i.e. by the delegate. Consequently, a great portion of management fees which are granted to AIFMs is reassigned to delegates.

Although the advantages of such a process are well understood by ESMA, as an easier access to external expertise and efficiency gains, operational and supervisory risks remain significant to the point of wondering whether AIFs can still be managed by the related authorised AIFM.

Following these observations, it can be concluded that there is a need to clarify the scope of delegation in order to "maintain sufficient substance in the EU". According to ESMA, this could include (i) qualitative and quantitative criteria or (ii) a list of core critical functions that should always be performed internally by AIFMs.

- **Use of seconded staff**

Practice has notably reflected that staff from professional services firms are often seconded to AIFMs on a temporary basis. Issues on substance and delegation rules under the Directive are also raised here, in particular when seconded staff are not operating in the authorised AIFM's EU Member State or even when the staff are operating outside of the EU. The situation is all the trickier when this staff carry on its work from usual offices outside the EU.

To that end, ESMA calls for further legislative clarifications for the sake of legal certainty.

3 Directive 2014/65/EU of the European Parliament and the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU.

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Expansion of ESMA's register's scope

Currently, the scope of AIFMs and the AIFs they manage which shall be submitted to ESMA's register regarding reporting requirements is quite limited. Actually, ESMA specifies that (i) sub-thresholds AIFMs i.e. AIFMs that manage AIFs whose assets under management do not exceed, as the case may be, EUR 500 Mio or EUR 100 Mio[4], (ii) AIFMs under the national private placement regime[5] (NPPR) and (iii) non-EU AIFs managed by a non-EU AIFM with a passport do not fall within the scope of entities that should be referenced in ESMA's register.

However, it is expressly reminded that such entities shall comply with the related reporting requirements.

These shortcomings mostly lead to a reduction of transparency on (i) the status of these entities and (ii) the scope of their marketing activities from a geographical point of view. Furthermore, due diligences are rendered unavailable for marketing participants and financial supervisors are provided with too limited information.

Nonetheless, ESMA recognises that including these entities into its register shall generate additional costs and/or risks, in particular due to the timeliness with which the information is to be provided to NCAs and ESMA, the required modification of IT systems and lastly to the lack of clear identification of the regime under which these entities operate.

As a conclusive statement, some improvements under the regime set up by the Directive would be welcome, essentially with the aim of granting a more secured regulatory framework to EU investors. However, should these recommended amendments be introduced, it should be kept in mind that, unavoidably, it would also likely place an additional burden on AIFMs.

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4 Art. 3 (2) of Dir. 2011/61/EU of 8 June 2011 on Alternative Investment Fund Managers, op. cit., p. 1.
5 Art. 42 of Dir. 2011/61/EU of 8 June 2011 on Alternative Investment Fund Managers, op. cit., p. 1.

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Luxembourg: a new hub for fintech businesses and issuers willing to use new technologies for issuing their securities?

OUR INSIGHTS AT A GLANCE

- The Luxembourg Government recently presented a new bill of law n° 7637 (the "Bill of Law") with the aim to modernise the law of 6 April 2013 on dematerialised securities.
- The Bill of Law forms part of a continued modernisation of the legal framework of financial transactions and is a continuation of the law of 1 March 2019, stating in essence that account keepers may hold securities accounts and register securities within or through secure electronic recording systems, including distributed ledgers or databases.
- This initiative supports the players concerned and, more generally, the financial place in the digitalisation and use of new technologies in the field of issuance and circulation of dematerialised securities.
- The Bill of Law introduces changes regarding issuance accounts and it broadens the scope of entities able to act as central account keeper for debt securities.

The Luxembourg Parliament published a new bill of law n° 7637 (the "Bill of Law") with the aim to modernise the law of 6 April 2013 on dematerialised securities. This Bill of Law forms part of a continued modernisation of the legal framework of financial transactions and is a continuation of the law of 1 March 2019, stating in essence that account keepers may hold securities accounts and register securities within or through secure electronic recording systems, including distributed ledgers or databases. This initiative supports the players concerned and, more generally, the financial place in the digitalisation and use of new technologies in the field of issuance and circulation of dematerialised securities.

The Bill of Law is an important new step for the Luxembourg financial centre in its desire to meet the challenges and opportunities resulting from the digitalisation of the financial sector in order to enable it to position itself actively in relation to recourse to secure electronic recording mechanisms in the issuance of securities.

Two material changes shall be introduced.

Issuance accounts

It is necessary to keep record of the number and type of dematerialised securities. The issuance or conversion of dematerialised securities is carried out by registering the securities in an issuance account held with a settlement institution or a central account holder. The dematerialised securities are represented by an entry in the security account. The issuance account is not a security account. The issuance account enables verification that in the securities account there are not more securities in circulation than securities issued.

By means of a clarification of the legal definition of issuance accounts, the Bill of Law expressly recognises the ability to use new technologies to secure electronic records, such as distributed ledger technology or electronic databases, as part of the issue of dematerialised listed and unlisted securities.

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As per this definition, an issuance account is an account held with a settlement provider or central bookkeeper which allows for the recording of dematerialised securities by secured electronic recordings (including distributed ledger technology). The Bill of Law highlights the technological neutral character of this new framework. This novelty will allow for a variety of technologies to be adopted.

Opening of the activity of central account keeper

Currently, the activity of central account keeper is restricted to certain Luxembourg service providers, provided they obtain a specific license to allow performance of this function. For non-listed debt securities, the Bill of Law opens access to the activity of central account keeper to European Member States investment firms and credit institutions.

Since the opening of the role of central account keeper to new players should not give rise to a lower quality of services provided by these new actors, they are required to have adequate control and security systems in place for the issuance accounts in order to ensure the registration of the integral amount of the issued securities, the circulation of securities and the verification of the issuance amounts in the issuance account against the securities accounts of the holders.

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Investment Fund Managers faced with increasing obligations in the fight against money laundering and terrorist financing

OUR INSIGHTS AT A GLANCE

- Circular 18/698 of the Luxembourg *Commission de Surveillance du Secteur Financier* (CSSF) relating to the authorisation and organisation of investment fund managers had a significant impact on the Luxembourg regulatory environment and the obligations it introduced are still very relevant today.
- The Circular has a broad scope of application as it applies to management companies subject to Chapter 15 and Chapter 16 of the Law of 17 December 2010 relating to undertakings for collective investment and alternative investment fund managers authorised under Chapter 2 of the Law of 12 July 2013 on alternative investment fund managers.
- On 25 November 2019, the CSSF released an FAQ on the persons involved in the fight against money laundering (AML) and terrorist financing for Luxembourg regulated funds and investment fund managers (IFM) that went even further than the Circular and the AML legislation, the obligations deriving from the latter being built on a principle of proportionality based on the size and nature of the activities performed by the IFM.

On 23 August 2018, the Luxembourg *Commission de Surveillance du Secteur Financier* (CSSF) published the long-awaited circular 18/698 relating to the authorisation and organisation of investment fund managers (the Circular). We would like to come back to this Circular given the significant impact it had on the regulatory environment and since it is still very important that investment managers covered by this Circular comply with the obligations it introduced, especially after the more recent CSSF FAQ on the persons involved in the fight against money laundering for Luxembourg regulated funds and IFMs, which increased these obligations.

The Circular applies to a series of investment fund managers (IFMs) incorporated under Luxembourg law, among which management companies subject to Chapter 15 and Chapter 16 of the Law of 17 December 2010 relating to undertakings for collective investment (the 2010 Law) and alternative investment fund managers authorised under Chapter 2 of the Law of 12 July 2013 on alternative investment fund managers (the 2013 Law).

The entities referred to in Article 3 of the 2013 Law are excluded from the scope of application of the Circular. These entities are IFMs managing (i) closed-ended and unleveraged alternative investment funds (an AIF) whose assets under management (AuM) do not exceed EUR 500mio, or (ii) AIFs whose AuM, including any assets acquired through the use of leverage, do not exceed EUR 100mio (Small AIFMs).

The purpose of the Circular was to provide clarifications on certain conditions for authorisation, more particularly on the shareholding structure, the minimum own funds requirements, the administrative bodies, the arrangements concerning the central administration and governance and the rules governing the delegation framework.

Furthermore, the Circular clarified certain rules pertaining to the organisation of the fight against money laundering and terrorist financing (AML/FT). The Circular provides in this respect that every IFM is subject to the laws and regulations in force regarding the fight against money laundering and terrorist financing, including the Law of 12 November 2004 on the fight against money laundering and terrorist financing, as amended (the AML Law).

The professional obligations laid down in the AML Law must be implemented effectively by every IFM. Compliance with these obligations must be subject to regular monitoring and verifications at a frequency determined according to

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the risks to which the IFM is exposed. Also, every IFM must implement due diligence measures, in particular, on clients, initiators of undertakings for collective investment ("UCIs"), portfolio managers to whom it delegates the management and on investment advisers.

The IFM must also adopt the joint guidelines issued by the three European Supervisory Authorities (the European Banking Authority, "EBA", the European Securities and Markets Authority, "ESMA", and the European Insurance and Occupational Pensions Authority, "EIOPA") on money laundering and terrorist financing risk factors.

Pursuant to point 313 of the Circular, every IFM must designate an AML/FT Compliance Officer at senior management level as well as an AML/FT Compliance Officer who must have sufficient experience and knowledge of the Luxembourg and EU legal and regulatory framework on AML/FT.

On 25 November 2019, the CSSF released an FAQ (the 2019 FAQ) on the persons involved in AML/FT for Luxembourg regulated funds and IFMs that went even further than the Circular and the AML Law, the obligations deriving from the latter being built on a principle of proportionality based on the size and nature of the activities performed by the IFM.

In order to take the results of the National Risk Assessment regarding in particular the AML/FT risk exposure of the sector of collective investments into consideration, the CSSF states in its FAQ that every IFM is legally required to appoint two persons in charge of AML/FT:

- one person at management level responsible for compliance with AML/FT obligations (referred to as an RR, from the French *responsable du respect*); and
- one person at the appropriate hierarchical level in charge of controlling the compliance with AML/FT obligations (referred to as an RC, from the French *responsable du contrôle du respect des obligations*).

For AIFs and IFMs supervised by the CSSF, the RR can be the entire board acting as a collegial body or one of its members.

The RC shall be mandated *intuitu personae* by the board of the AIF (or shall be the Compliance Officer with respect to IFMs). It shall have sufficient AML/FT knowledge and expertise and shall be knowledgeable about the investments and distribution strategies of the AIF or about the services offered by the IFM.

The 2019 FAQ is of particular importance for Small AIFMs. Indeed, it is worth noting that Small AIFMs being subject to the AML Law, and as soon as the CSSF no longer applies the principle of proportionality with respect to IFMs, Small AIFMs must also abide by the obligation to appoint two persons in charge of AML/FT, regardless of the size and nature of their activities.

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