COMMISSION de SURVEILLANCE du SECTEUR FINANCIER

Annual Report 2007

Commission de Surveillance du Secteur Financier

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Despite the US subprime mortgage crisis and the subsequent widespread distortions of the financial markets, the Luxembourg financial sector's situation is enviable as at 31 December 2007: banks made profits comparable to those of 2006, investment funds boomed and PFS developed swiftly so that the range of their activities is growing continuously.

However, let's not deceive ourselves into thinking that the direct and indirect consequences of the subprime crisis on the international banking sector did not reach Luxembourg. Notable changes brought about by the crisis in the financial markets' functioning shook the "traditional" operational rules which seemed immutable until now and this situation is likely to persist.

Nevertheless, the crisis allowed to draw two major conclusions.

Firstly, the crisis brought out the responsibility of the credit grantor and the importance of appropriate risk assessment by the banks at the end of the chain that buy complex financial products. Lured by high yields, too many bankers lost sight of the underlying assets' intrinsic quality and volatility. This confirmed the fact that earning a lot of money is only possible by taking high risks. Let's hope that in the future, shareholders and bank managers will not be blinded by high short-term yields to the detriment of a medium and long-term view.

Secondly, complex financial products should be more transparent in order to bring out the risks that these products imply.

Considering the strictly Luxembourg situation, I must highlight the considerable growth in the investment fund industry. The EUR 2,000 billion mark has been topped in 2007 and the number of applications to create new funds exceeded 900, an all-time record. The unusual volume of work that this expansion implied was handled by the CSSF's agents in co-operation with the investment fund industry and again, the private sector and the supervisory authority were able to co-operate remarkably well.

I would like to thank all the CSSF's agents for their dedication and personal commitment. By adapting continually to the new challenges, they contributed to keeping our financial centre at a high level, thereby allowing it to continue to compete with other prime international financial centres.

I also thank the government for granting the necessary means in terms of human resources and technical infrastructures to the CSSF. The CSSF thus hired 27 new agents in 2007 and bought the "Aubépines" building close to the building currently occupied. In my eyes, the CSSF is thus properly equipped to continue to act serenely in the interest of the Luxembourg financial centre.

Jean-Nicolas SCHAUS
Director General

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Arthur PHILIPPE

Director

Jean-Nicolas SCHAUS

Director General

Simone DELCOURT

Director

CORPORATE GOVERNING BODIES OF THE COMMISSION DE SURVEILLANCE DU SECTEUR FINANCIER

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EXECUTIVE BOARD

Director General	Jean-Nicolas SCHAUS
Directors	Arthur PHILIPPE, Simone DELCOURT

CHAPTER I

SUPERVISION OF THE BANKING SECTOR

1. DEVELOPMENTS IN THE BANKING SECTOR IN 2007

1.1. Characteristics of the Luxembourg banking sector

The Luxembourg banking legislation provides for three types of banking licences, namely licences governing the activities of universal banks (151 institutions had this status on 31 December 2007), those governing the activities of banks issuing mortgage bonds (5 institutions had this status on 31 December 2007) and those governing the activities of banks issuing electronic means of payment (no institution had this status on 31 December 2007).

The banks fall under three categories according to their legal status and geographical origin:

- banks incorporated under Luxembourg law (113 on 31 December 2007);
- branches of banks originating from a Member State of the European Union or assimilated (35 on 31 December 2007);
- branches of banks originating from non-Member States of the European Union (8 on 31 December 2007).

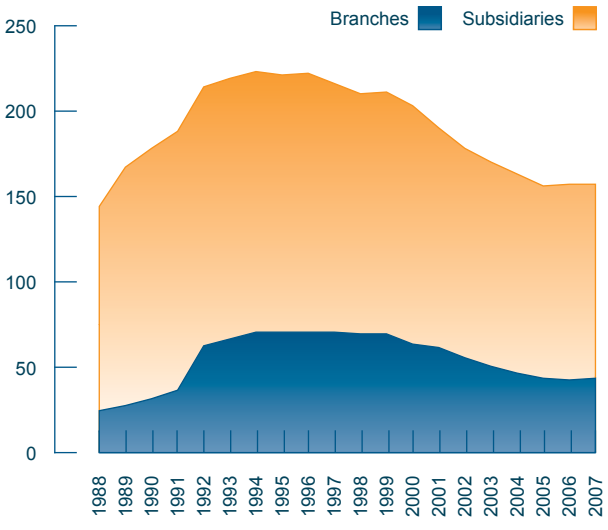
The *caisses rurales* (13 on 31 December 2007) and their central establishment, Banque Raiffeisen, which, according to the law on the financial sector, are to be considered as a single credit institution, constitute a special case.

1.2. Development in the number of credit institutions

The downward trend in the number of credit institutions established in Luxembourg observed at the beginning of the decade has stopped since 2006. With 156 entities authorised at the end of the financial year 2007, the number of banks remained unchanged as at 31 December 2006. Among those 156 entities, 113 are banks incorporated under Luxembourg law (2006: 114) and 43 are branches (2006: 42).

Development in the number of banks established in Luxembourg

Year	Branches	Subsidiaries	Total
1988	24	119	143
1989	27	139	166
1990	31	146	177
1991	36	151	187
1992	62	151	213
1993	66	152	218
1994	70	152	222
1995	70	150	220
1996	70	151	221
1997	70	145	215
1998	69	140	209
1999	69	141	210
2000	63	139	202
2001	61	128	189
2002	55	122	177
2003	50	119	169
2004	46	116	162
2005	43	112	155
2006	42	114	156
2007	43	113	156



The following events had an impact on the development of the number of credit institutions.

- One bank decided to cease its activities and two banks merged with other banks of the financial centre.
- Three banks have been granted their establishment authorisation.

Three banks were thus withdrawn from the official list during the year:

• Banca Nazionale del Lavoro International S.A.	Merger with BNP Paribas on 31 March 2007
• BPU Banca International S.A.	Merger with UBI Banca International S.A. on 1 October 2007
• Banque BI&A S.A.	Cessation of activities on 21 December 2007

Three new banks started their activities in 2007:

• PayPal (Europe) S.à r.l. et Cie, S.C.A.	1 July 2007
• Dexia LdG Banque S.A.	3 July 2007
• PFPC Bank Limited, Luxembourg Branch	17 September 2007

PayPal (Europe) S.à r.l. et Cie, S.C.A., a company belonging to the eBay group, operates an Internet platform specialised in electronic payments between professionals and individuals at European level.

Following the creation of Dexia LdG Banque S.A., a bank issuing covered bonds belonging to the Dexia group, the number of banks issuing covered bonds in the financial centre rose to five (please also refer to point 1.10. "Banks issuing covered bonds").

By opening PFPC Bank Limited, Luxembourg Branch, the Irish group already present in Luxembourg with a branch of PFPC International Limited intends to offer its clients depositary bank services as well.

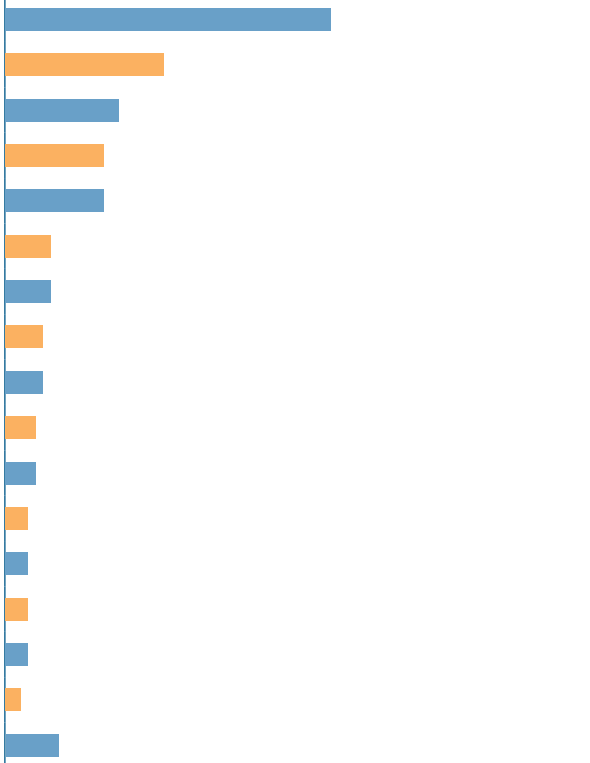
The following credit institutions changed their name in 2007:

Former corporate name	New corporate name (date of change)
F. van Lanschot Bankiers (Luxembourg) S.A	Van Lanschot Bankiers (Luxembourg) S.A. (01.01.2007)
Nord Europe Private Bank S.A.	Nord Europe Private Bank (31.01.2007)
Banca Antoniana - Popolare Veneta, CSpA aRL, Padova (Italie), succursale de Luxembourg	BANCA ANTONVENETA S.p.A., Padova (Italie), succursale de Luxembourg (09.03.2007)
NATEXIS LUXEMBOURG S.A.	NATIXIS LUXEMBOURG S.A (20.02.2007)
Bank of Tokyo-Mitsubishi (Luxembourg) S.A.	Mitsubishi UFJ Global Custody S.A. (02.04.2007)
Mutuel Bank Luxembourg S.A.	Banque Transatlantique Luxembourg S.A. (01.05.2007)
Natixis Private Banking Luxembourg S.A.	Natixis Private Banking International (03.05.2007)
Bank Sal. Oppenheim jr. & Cie (Luxembourg) S.A.	Sal. Oppenheim jr. & Cie S.C.A. (01.07.2007)
Banca Lombarda International S.A.	UBI Banca International S.A. (28.06.2007)
Bank Sarasin Europe S.A.	Crédit Agricole Luxembourg Bank (02.07.2007)
ABN AMRO Mellon Global Securities Services, Luxembourg branch	BNY Mellon Asset Servicing B.V., Luxembourg Branch (19.12.2007)
Crédit Industriel d'Alsace et de Lorraine S.A., succursale de Luxembourg	Banque CIC Est, succursale de Luxembourg (31.12.2007)

The breakdown of credit institutions according to their geographical origin has changed as follows (2006 figures between brackets). Banks of German origin remain the highest in number with 43 (45) entities, followed by Belgian and Luxembourg banks with 21 (18) entities. 15 (15) banks originate from France, 13 (15) from Italy, 13 (13) from Switzerland, and 6 (6) from Sweden as well as from the United Kingdom.

Geographical origin of banks

Country	Number
Germany	43
Belgium / Luxembourg	21
France	15
Italy	13
Switzerland	13
Sweden	6
United Kingdom	6
United States	5
Japan	5
China	4
Netherlands	4
Brazil	3
Iceland	3
Israel	3
Portugal	3
Denmark	2
Others	7
Total	**156**



In 2007, the number of banks originating from Germany decreased by two entities. Both banks were shifted to the group Luxembourg/Belgium as the CSSF is henceforth the authority that has the ultimate responsibility for the supervision of those banks, which are Sal. Oppenheim jr. & Cie S.C.A. whose group head was transferred to Luxembourg and Clearstream Banking S.A. for which the CSSF is the ultimate group supervisory authority.

1.3. Development in the local branches network in Luxembourg

The downward trend in the branches network since the 1990s also continued in 2007.

	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Local branches	254	240	231	226	225	214	207	200	253*	246*	234*	229*
Banks concerned	11	11	11	10	9	9	8	8	9	9	9	9

* including the Caisses Rurales Raiffeisen affiliated to Banque Raiffeisen and the local branches of these Caisses Rurales.

1.4. Development in banking employment

The total number of persons employed by Luxembourg credit institutions as at 31 December 2006 reached 24,752, which represented an increase of 1,525 employees (+6.56%) over a year. At the end of 2007, the total number of employees of Luxembourg credit institutions reached 26,139, which represents a further increase of 1,387 employees, i.e. +5.60% over a year.

Banking employment had strongly dropped during 2002 and 2003. The total loss of about 1,300 jobs came in a difficult economic context, together with reorganisations of the production structure that led to the transfer of a substantial number of jobs to other entities of the financial sector, notably to PFS and management companies. The improvement in banking employment that took place in the favourable business climate of 2005 and even accelerated in 2006, suggests that the consolidation of banking staff before 2005 was to a large extent due to temporary, economic concerns. This growth continued in 2007, although to a lesser extent than in 2006.

Among the credit institutions registered on the official list as at 31 December 2007, 75% maintained, or even increased, their staff. This percentage was 74% in 2006 and 63% in 2005. The banks that increased their staff substantially are mainly those active in the investment funds sector and those that are developing their presence in Luxembourg, such as the Icelandic banks, Sal. Oppenheim jr. & Cie S.C.A. and Compagnie de Banque Privée.

The breakdown of total employment shows that the share of executives within total employment continued to grow. It rose from 22.5% to 23.5% during 2007. The female employment rate remained almost unchanged with 45.6% (45.7% in 2006).

Breakdown of the number of employees per bank

	Number of banks					
Number of employees	**2002**	**2003**	**2004**	**2005**	**2006**	**2007**
> 1,000	4	4	4	4	5	5
500 to 1,000	6	4	2	6	7	9
400 to 500	3	4	6	4	3	2
300 to 400	7	6	8	7	8	10
200 to 300	9	11	8	7	10	9
100 to 200	18	19	19	20	18	18
50 to 100	23	21	21	18	18	21
< 50	105	100	94	89	87	82
Total	**175**	**169**	**162**	**155**	**156**	**156**

Situation of employment in credit institutions

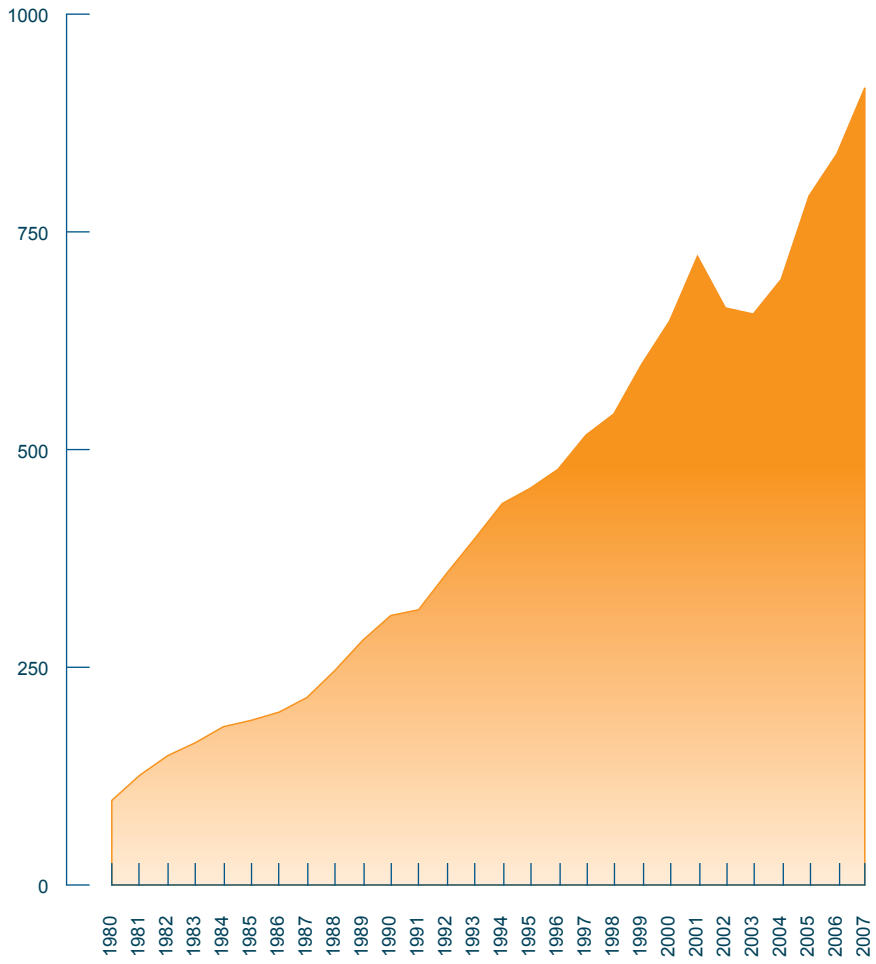
	Total		Management			Office staff			Technical staff			Total staff		
	Luxemb.	Foreigners	Men	Women	Total	Men	Women	Total	Men	Women	Total	Men	Women	Total
1995	8,170	10,113	2,533	451	2,984	7,318	7,813	15,131	49	119	168	9,900	8,383	18,283
1996	8,113	10,469	2,658	490	3,148	7,476	7,809	15,285	48	101	149	10,182	8,400	18,582
1997	8,003	11,086	2,765	547	3,312	7,631	8,013	15,644	44	89	133	10,440	8,649	19,089
1998	7,829	12,005	2,900	577	3,477	7,846	8,377	16,223	47	87	134	10,793	9,041	19,834
1999	7,797	13,400	3,119	670	3,789	8,362	8,961	17,323	34	51	85	11,515	9,682	21,197
2000	7,836	15,232	3,371	783	4,154	9,030	9,801	18,831	35	48	83	12,436	10,632	23,068
2001	7,713	16,148	3,581	917	4,498	9,222	10,046	19,268	33	62	95	12,836	11,025	23,861
2002	7,402	15,898	3,654	977	4,631	8,941	9,657	18,598	25	46	71	12,620	10,680	23,300
2003	7,117	15,412	3,720	1,049	4,769	8,486	9,211	17,691	23	40	63	12,229	10,300	22,529
2004	7,001	15,553	3,801	1,111	4,912	8,451	9,138	17,589	19	34	53	12,271	10,283	22,554
2005	6,822	16,405	3,948	1,183	5,131	8,641	9,397	18,038	20	38	58	12,609	10,618	23,227
2006	6,840	17,912	4,280	1,294	5,574	9,153	9,974	19,127	19	32	51	13,452	11,300	24,752
2007	6,962	19,177	4,669	1,475	6,144	9,525	10,407	19,932	32	31	63	14,226	11,913	26,139
	Quota													
2002	31.8%	68.2%	78.9%	21.1%	19.9%	48.1%	51.9%	79.8%	35.2%	64.8%	0.3%	54.2%	45.8%	100.0%
2003	31.6%	68.4%	78.0%	22.0%	21.2%	48.0%	52.1%	78.5%	36.5%	63.5%	0.3%	54.3%	45.7%	100.0%
2004	31.0%	69.0%	77.4%	22.6%	21.8%	48.0%	52.0%	78.0%	35.8%	64.2%	0.2%	54.4%	45.6%	100.0%
2005	29.4%	70.6%	77.0%	23.1%	22.1%	47.9%	52.1%	77.7%	34.5%	65.5%	0.2%	54.3%	45.7%	100.0%
2006	27.6%	72.4%	76.8%	23.2%	22.5%	47.9%	52.1%	77.3%	37.3%	62.7%	0.2%	54.3%	45.7%	100.0%
2007	26.6%	73.4%	76.0%	24.0%	23.5%	47.8%	52.2%	76.3%	50.8%	49.2%	0.2%	54.4%	45.6%	100.0%

1.5. Development in the balance sheets

The balance sheet total of credit institutions rose to EUR 915,445 million at the end of 2007 against EUR 839,574 million at the end of 2006, which represents an increase of 9.0% over the year.

Development in the balance sheet total of credit institutions – in billion EUR

1980	97.10
1981	125.95
1982	148.41
1983	163.41
1984	181.73
1985	189.09
1986	198.49
1987	215.32
1988	246.36
1989	281.04
1990	309.37
1991	316.09
1992	357.56
1993	397.15
1994	438.01
1995	455.47
1996	477.37
1997	516.59
1998	540.89
1999	598.01
2000	647.63
2001	721.98
2002	662.70
2003	655.60
2004	695.36
2005	791.25
2006	839.57
2007	**915.44**



Aggregated balance sheet total – in million EUR

ASSETS	2006	2007[1]	Variation	LIABILITIES	2006	2007[1]	Variation
Loans and advances to credit institutions	409,719	446,232	8.9%	Amounts owed to credit institutions	384,145	439,485	14.4%
Loans and advances to customers	159,439	194,565	22.0%	Amounts owed to customers	293,032	302,610	3.3%
Fixed-income securities	198,172	207,797	4.9%	Amounts owed represented by securities	85,497	89,328	4.5%
Variable-yield securities	16,368	9,924	-39.4%	Various items	19,796	22,537	13.8%
Participating interest and shares in affiliated undertakings	9,693	10,843	11.9%	Permanent means (*)	57,104	61,484	7.7%
Fixed assets and other assets	46,182	46,084	-0.2%	*of which profit for the year*	*5,671*	*5,124*	*-9.8%*
Total	**839,574**	**915,445**	**9.0%**	**Total**	**839,574**	**915,445**	**9.0%**

(*) Including share capital, reserves, subordinated debt and provisions.

Assets

As far as assets are concerned, the growth in the business volume could be observed in particular with respect to **loans and advances to customers**, which increased by 22% to EUR 194,565 million (against EUR 159,439 million in 2006). This item thus confirms its increasing importance for banking business which has been observed since 2004.

The upward trend in loans and advances to customers can be observed in the majority of banks. Given the diversity of activities performed in the financial centre, the reasons for this growth are manifold. In general, it can be observed that certain banking groups continue to develop their credit activities within their Luxembourg establishment.

Representing 48.7% of the balance sheet total, **loans and advances to credit institutions** remain stable compared to 2006. This figure bears witness to the sustained importance of interbank positions for the Luxembourg financial centre, which can be mainly explained by a group cash management logic and by the structure of the legal entities that take part in this management (notably the double presences of credit institutions in Luxembourg). Thus, 77% of interbank assets (69% in 2006) and 68.3% (60% in 2006) of interbank liabilities constitute transactions with banks of the group.

Qualitative breakdown of interbank assets

	2005	2006	2007*
Central and multilateral banks	0.08%	0.10%	0.10%
Banks zone A[2]	98.19%	98.05%	96.90%
Banks zone B[3]	1.73%	1.85%	3.00%

(*) preliminary figures

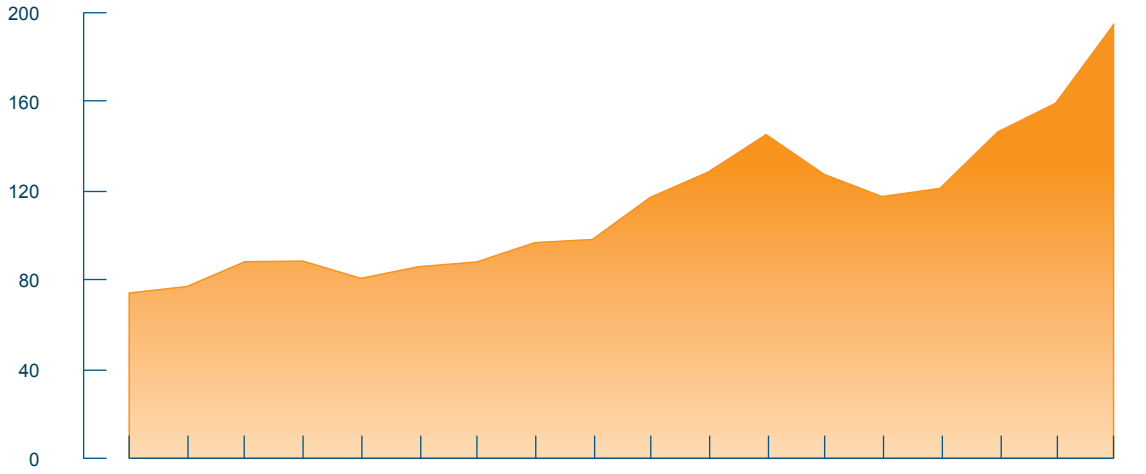
[1] Preliminary figures for the end of 2007.

[2] Countries zone A: Australia, Austria, Belgium, Canada, Czech Republic, Denmark, Finland, France, Germany, Greece, Hungary, Iceland, Ireland, Italy, Japan, Liechtenstein, Luxembourg, Mexico, Netherlands, New Zealand, Norway, Poland, Portugal, Saudi Arabia, Slovakia, South Korea, Spain, Sweden, Switzerland, Turkey, United Kingdom, United States.

[3] Countries zone B: all countries other than those of zone A.

This breakdown shows that the vast majority of loans and advances to credit institutions consist of commitments on zone A banks, i.e. banks of industrialised countries. The breakdown in relative terms remained relatively stable over the last three years, even though commitments on zone B banks slightly rose in 2007.

Long-term development in loans and advances to customers – in billion EUR



	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Loans and advances to customers	74.1	77.1	88.3	88.5	80.7	86.0	88.1	96.8	98.2	117.1	128.5	145.3	127.5	117.5	121.1	146.5	159.4	194.6

Breakdown of loans and advances to customers

	2005	2006	2007*
Public authorities zone A	6.99%	6.08%	4.24%
Public authorities zone B	0.03%	0.11%	0.05%
Private customers & Financial institutions	92.97%	93.81%	95.71%
of which: legal persons	*48.66%*	*49.90%*	*49.44%*
of which: natural persons	*20.78%*	*19.77%*	*17.42%*
of which: financial institutions	*30.27%*	*30.27%*	*33.08%*
of which: leasing	*0.27%*	*0.06%*	*0.06%*

(*) preliminary figures

Qualitative breakdown of loans and advances to private customers and financial institutions

	2005	2006	2007*
Secured by public authorities	2.51%	2.22%	1.71%
Secured by credit institutions	14.94%	15.33%	16.89%
Secured by real estate mortgages	12.38%	12.03%	10.90%
Secured by other tangible guarantees	28.41%	28.47%	29.56%
Unsecured	41.76%	41.96%	40.94%

(*) preliminary figures

The qualitative breakdown of loans and advances hardly changed over the year 2007.

The portfolio of the **fixed-income securities** recorded a slight increase (+4.9%) in 2006, amounting to EUR 207,797 million (against EUR 198,172 million in 2006) and representing 22.7% of the balance sheet total in 2007, 95% of which representing securities of zone A issuers.

Qualitative breakdown of fixed-income securities

	2005	2006	2007*
Public sector zone A	29.88%	25.15%	18.83%
Public sector zone B	0.40%	0.24%	0.35%
Credit institutions zone A	43.58%	44.90%	46.04%
Credit institutions zone B	0.62%	0.49%	0.77%
Other issuers zone A	21.86%	25.44%	29.31%
Other issuers zone B	3.65%	3.78%	4.70%

(*) preliminary figures

The volume of the portfolio of **variable-yield transferable securities**, i.e. shares, remained marginal for Luxembourg banks (1.1% of the balance sheet total). Following the substantial increase last year owing to some important structured transactions, the volume of this portfolio fell back to EUR 9,924 million in 2007 (-39.4% compared to 2006).

The item **participating interest and shares in affiliated undertakings** increased to EUR 10,843 million in 2007 (EUR 9,693 million in 2006) which is a 11.9% growth.

The item **fixed assets and other assets** practically stagnated at EUR 46,084 million at the end of 2007.

Liabilities

On the liabilities side, **amounts owed to credit institutions** recorded the most notable rise, in terms of volume (+EUR 55,340 million) as well as in relative terms (+14.4%), while amounts owed to customers grew by 3.3% only.

With 48% of liabilities (against 45.8% in 2006), the interbank market underscored its importance in the refinancing of the banking activities in Luxembourg and gained ground again compared to amounts owed to customers, which represented 33.1% of liabilities (against 34.9% in 2006).

Amounts owed to customers reached EUR 302,610 million at the end of 2007, against EUR 293,032 million in 2006. Amounts owed to legal entities grew by 2.6% only, even though their growth was a lot more sustained in 2006 (+20.2%) and 2005 (+14.5%). On the other hand, amounts owed to natural persons increased by 12.7% in volume year-on-year and thereby confirm their relative importance compared to amounts owed to the public sector.

Breakdown of amounts owed to customers

	2005	2006	2007*
Amounts owed to the public sector	3.01%	2.83%	1.37%
Amounts owed to legal persons	75.23%	77.84%	77.48%
Amounts owed to natural persons	21.76%	19.34%	21.14%

(*) preliminary figures

Amounts owed represented by securities grew slightly by 4.5% compared to 2006. With EUR 89,328 million, those amounts now only represent 9.8% of the total balance sheet (against 10.2% in 2006), but remain an interesting refinancing mode, notably for banks issuing mortgage bonds.

Permanent means mainly encompass subscribed capital, reserves, provisions and subordinated debts. They grew by 7.7% over the year to EUR 61,484 million at the end of 2007, compared to EUR 57,104 million in 2006 and EUR 52,111 million in 2005. This rise is mainly due to two factors:

- the growth in subscribed capital, a part of which is related to the establishment of the German group Sal. Oppenheim in Luxembourg;
- a growth in the volume of subordinated debt.

1.6. Development in the profit and loss account

The analysis of the banking sector's results presented in this Annual Report is based on provisional and, for the most part, non-audited figures, available as at 6 February 2008. As soon as final figures are established by the banks and audited by external auditors, these final figures are sent to the CSSF. Given the subprime crisis and the difficulties to assess certain assets, the final results are expected to be lower than the provisional result published here, owing to additional provisions to be made. The final profit and loss account for 2007 will be published in the CSSF's Annual Report 2008.

Net profit of the Luxembourg banking sector in 2007 reached EUR 5,124 million, which represents a 9.6% fall compared to the previous year.

The 2007 profit and loss account reflects three major developments:

- the expansion of intermediation activities and portfolio management that is being reflected in the growth of interest margin and commission income;
- the absence of other income as substantial as in 2006;
- financial turmoil linked to subprimes that resulted in a fall in income from financial operations and a substantial increase in creation of provisions.

Development in the profit and loss account – in million EUR

	2005	Relative share	2006	Relative share	2007*	Relative share	Variation 2006/2007
Interest and dividends received	35,228		48,715		61,558		
Interest paid	31,323		43,885		55,576		
Interest-rate margin	**3,905**	**47%**	**4,830**	**45%**	**5,982**	**54%**	**23.8%**
Commission income	3,209	39%	3,674	34%	4,018	36%	9.4%
Income from financial operations	628	8%	616	6%	75	1%	-87.9%
Other income	548	7%	1,722	16%	936	9%	-46.0%
Banking income	**8,290**	**100%**	**10,842**	**100%**	**11,010**	**100%**	**1.6%**
General administrative expenses	3,419	41%	3,754	35%	4,173	38%	11.0%
of which: staff costs	*1,945*	*23%*	*2,160*	*20%*	*2,381*	*22%*	*10.2%*
of which: other administrative expenses	*1,474*	*18%*	*1,594*	*15%*	*1,792*	*16%*	*12.5%*
Depreciation	274	3%	227	2%	247	2%	8.6%
Result before provisions	**4,597**	**55%**	**6,862**	**63%**	**6,591**	**60%**	**-3.9%**
Creation of provisions	1,142	14%	1,107	10%	1,507	14%	36.1%
Write-back of provisions	846	10%	802	7%	897	8%	11.9%
Taxes	803	10%	885	8%	857	8%	-3.2%
Result for the financial year	**3,498**	**42%**	**5,671**	**52%**	**5,124**	**47%**	**-9.6%**

(*) preliminary figures

The **interest-rate margin,** which amounted to EUR 5,982 million as at 31 December 2007, increased by 23.8% as compared to the previous year, owing to two concurring developments: the rise in the pure interest-rate margin and the growth in holding income. The pure interest-rate margin, excluding income from dividends, increased by 15.9% in a context that remained generally favourable to intermediation activities, as reflected by the rise in the aggregate balance sheet. Dividends received on holdings[4] increased by 36.9% over a year. This growth in mainly due to the restructuring of a German banking group whose profits are now received by the Luxembourg entity. A fifth of the interest-rate margin is attributable to these dividends.

(in million EUR)	**2005**	**2006**	**2007***
Dividends received on participating interest	578	982	1,345

(*) preliminary figures

Although the stock market environment was less favourable than in 2006, it has nevertheless contributed to the vigour of portfolio management and brokerage during 2007. Carried by the businesses of depositary bank and brokerage, **commission income** grew by 9.4% year-on-year. In 2007, banks in the financial centre thus earned EUR 4,018 million in commission income.

However, this substantial increase in operating income was offset by the fall in income from financial operations and other income. The item **income from financial operations**, which includes trading income, particularly suffered from the depreciation of bond portfolios categorised into trading and investment portfolio. Those drops are due to the subprime turmoil.

Other income was boosted in 2006 by extraordinary capital gains arising from the disposal of holdings. As those capital gains are non-recurrent, other income dropped by 46% in 2007 year-on-year.

As far as expenses are concerned, **general administrative expenses** increased substantially. This growth concerned especially staff costs (+10.2%), which increased under the effect of wage adjustments and the rise in banking employment, and the other general costs that rose by 12.5%. The rise in general administrative expenses (+11%) thus exceeded by far that of banking income (+1.6%), resulting in a 3.9% decrease of **profit before provisions and taxes**.

Since summer 2007, the intrinsic value of US subprime mortgage loans, largely distributed in the world through securitised structured products, fell sharply owing to the substantial rise in recorded or possible payment defaults. This downward trend is not in the least limited to the subprime segment itself, but has spread to structured products that contain subprime risks, as well as counterparts directly or indirectly exposed to subprime risks. In addition, the generalised risk re-assessment further deteriorated because of the fundamental uncertainty concerning the future performance of subprime debt and because of investors that are wary about investing before knowing the full extent of the subprime crisis. Those developments left their mark on the profit and loss account of Luxembourg credit institutions whose structured products and financial securities portfolios suffer indirectly from the subprime crisis. As a result, income from financial operations dropped substantially by EUR 541 million (-87.9%) and **net creation of provisions** grew considerably by EUR 304 million (+99.6%).

[4] Dividends relating to participating interests and interests in affiliated undertakings.

Long-term development of profit and loss accounts – in million EUR

	1999	2000	2001	2002	2003	2004	2005	2006	2007*	Variation 2006/2007
Interest and dividends received	35,943	47,996	51,942	41,257	34,071	29,218	35,228	48,715	61,558	26.4%
Interest paid	32,664	44,467	47,560	37,116	29,991	25,306	31,323	43,885	55,576	26.6%
Interest-rate margin	**3,279**	**3,529**	**4,382**	**4,141**	**4,080**	**3,913**	**3,905**	**4,830**	**5,982**	**23.8%**
Commission income	2,338	3,035	2,792	2,615	2,533	2,771	3,209	3,674	4,018	9.4%
Income from financial operations	563	488	355	261	481	582	628	616	75	-87.9%
Other income	255	465	410	1,044	496	184	548	1,722	936	-45.6%
Banking income	**6,435**	**7,517**	**7,939**	**8,061**	**7,590**	**7,450**	**8,290**	**10,842**	**11,010**	**1.6%**
General administrative expenses	2,627	3,016	3,227	3,182	3,095	3,174	3,419	3,754	4,173	11.2%
of which: staff costs	*1,444*	*1,588*	*1,758*	*1,809*	*1,752*	*1,798*	*1,945*	*2,160*	*2,381*	*10.2%*
of which: other administrative expenses	*1,183*	*1,393*	*1,470*	*1,373*	*1,342*	*1,375*	*1,474*	*1,594*	*1,792*	*12.5%*
Depreciation	283	306	396	308	290	288	274	227	247	8.6%
Result before provisions	**3,525**	**4,195**	**4,316**	**4,571**	**4,206**	**3,989**	**4,597**	**6,862**	**6,591**	**-3.9%**
Creation of provisions	1,095	1,520	1,261	1,824	1,389	1,098	1,142	1,107	1,507	36.1%
Write-back of provisions	577	767	725	658	751	754	846	802	897	11.9%
Taxes	977	1,013	920	685	694	778	803	885	857	-3.2%
Result for the financial year	**2,030**	**2,429**	**2,861**	**2,720**	**2,874**	**2,866**	**3,498**	**5,671**	**5,124**	**-9.6%**
Net creation of provisions	518	753	536	1,166	638	345	296	305	610	99.6%
Dividends relating to participating interest and interest in affiliated undertakings	226	433	652	499	628	643	578	982	1,345	36.9%

(*) preliminary figures

Structural ratios

	2005	2006	2007*
Cost / income ratio	44.55%	36.71%	40.14%
Profit before taxes / assets	0.54%	0.78%	0.65%
Profit before taxes / risk-weighted assets	26.95%	41.07%	30.54%
Profit before taxes / tier-1 capital	15.94%	22.13%	18.34%
Income excluding interest / banking income	52.90%	55.45%	45.67%
Creation of provisions for loans and advances to customers[5]	0.54%	0.39%	0,38%
Creation of provisions for participating interest and interest in affiliated undertakings[6]	12.90%	12.68%	5.11%

(*) preliminary figures

Development of certain indicators of the profit and loss account by employee

(in million EUR)	2005	2006	2007*
Banking income / employee	0.357	0.438	0.421
Staff costs / employee	0.084	0.087	0.091

(*) preliminary figures

1.7. Off-balance sheet items and financial derivatives

The banks of the financial centre used derivatives for a nominal amount of EUR 1,032 billion in 2007 against EUR 1,026.5 billion in 2006. The use of derivatives thus almost stagnated as compared to the previous year (+0.5% only). Following sustained increases of 6.5% in 2003, 14.4% in 2004, 14.1% in 2005 and 7.7% in 2006, and given the substantial 9% balance sheet growth, derivative instruments represented 112.7% only of the total balance sheet in 2007 in terms of volume. In 2006, this percentage exceeded the 120% mark.

Interest rate swaps remain the most used instruments in terms of nominal volume (56% of the total volume), although receding by more than EUR 10 billion (-1.8%) compared to 2006.

Forward foreign exchange remained attractive, representing 33.3% of the total volume (30.9% in 2006). Although growing by 8.4% to EUR 343.5 billion (against EUR 316.8 billion in 2006), it could not offset the substantial fall by EUR 34 billion in interest futures and forward rate agreements (-52.9% compared to 2006). Some EUR 20 billion of those EUR 34 billion are attributable to OTC transactions, which fell by 86.2% to almost EUR 3 billion, as against EUR 23.4 billion in 2006.

The surge in futures (other rates) (+45%) and in options (currencies, interest and other rates) (+40.9%) was remarkable as well, even though both instruments still only represent 1.9% (EUR 19.8 billion) and 5.8% (EUR 60.3 billion) of the total volume.

Instruments dealt over the counter remained the most used products (92.7% of the total nominal amount in 2007 against 92.1% in 2006), reaching a volume of EUR 956.9 billion against EUR 945.3 billion in 2006.

[5] As a % of the gross amount.

[6] As a % of the gross amount.

Use of financial derivatives by credit institutions

	2006		2007*	
	in billion EUR	as a % of balance sheet total	in billion EUR	as a % of balance sheet total
Interest rate swaps	589.0	70.2%	578.2	63.2%
Futures (interest) and forward rate agreements	64.3	7.7%	30.3	3.3%
of which:OTC	*23.4*	*2.8%*	*3.2*	*0.4%*
of which: regulated market	*41.0*	*4.9%*	*27.1*	*3.0%*
Forward exchange	316.8	37.7%	343.5	37.5%
of which: OTC	*316.6*	*37.7%*	*343.4*	*37.5%*
Futures (other rates)	13.6	1.6%	19.8	2.2%
Options (currencies, interest, other rates)	42.8	5.1%	60.3	6.6%
of which: OTC	*16.4*	*2.0%*	*32.1*	*3.5%*
of which: regulated market	*26.4*	*3.1%*	*28.1*	*3.1%*

(*) preliminary figures

Assets deposited by customers: off-balance sheet

(in billion EUR)	2006	2007*	Variation
Assets deposited by UCIs	1,790.5	1,966.0	9.8%
Assets deposited by clearing or settlement institutions	417.6	465.7	11.5%
Assets deposited by other professionals acting in the financial markets	5,494.0	6,090.4	10.9%
Other deposited assets	434.8	395.9	-8.8%

(*) preliminary figures

1.8. Development in own funds and in the solvency ratio

1.8.1. Number of banks required to meet a solvency ratio

As at 31 December 2007, 114 banks were required to meet a non-consolidated solvency ratio, including 113 banks incorporated under Luxembourg law and one branch of non-EU origin. 103 banks carry out limited trading activities, and are therefore authorised to calculate a simplified ratio. Actual trading activities remain confined to a limited number of banks. Among the 31 banks that also calculate a consolidated solvency ratio, ten are required to calculate an integrated ratio.

Number of banks required to meet a solvency ratio	Integrated ratio		Simplified ratio		Total	
	2006	2007	2006	2007	2006	2007
Non-consolidated	22	11	93	103	115	114
Consolidated	14	10	16	21	30	31

1.8.2. Development in the solvency ratio

The figures below are based on consolidated figures for banks required to meet a consolidated solvency ratio.

In 2007, the solvency ratio remained almost at the same level as in 2006. Indeed, the rise in capital requirements could not be totally offset by the increase in eligible own funds. Thus, the solvency ratio reached 14.5%, easily exceeding the minimum threshold of 8% required under the existing prudential regulations. Taking into account core capital (Tier 1) alone, the aggregate ratio for the financial centre increased from 11.6% at the end of 2006 to 11.7% at the end of 2007.

Capital requirements for credit risk grew by 8.3% in 2007, reflecting an upturn in lending operations. Besides, lending operations alone continue to make up the bulk of capital requirements. Capital requirements for the banks' trading portfolios, negligible in terms of volume, remained more or less stable. Capital requirements for foreign exchange risk remain marginal, although their marked downward trend between 2000 and 2004 has been interrupted since 2005.

Eligible own funds continued their positive development of the previous years (+7.4%). Original own funds, which represented 84.8% of total eligible own funds, grew by 10% due to the rise of the items "Paid-up capital" and "Reserves". As in the previous years, the banks hoarded a large part of their profits. Hybrid capital instruments confirm their downward trend. Following an increase in 2006, additional own funds (after capping) decreased again. There has also been a marginal use of sub-additional own funds, as in the two previous years. Finally, items to be deducted from own funds have been on the rise since 2003 and recorded a volume of EUR 1,625 million in 2007 (against EUR 1,341 million in 2006), owing to the growth in the item participating interest in other credit and financial institutions exceeding 10% of the capital. The impact on the solvency ratio denominator is significant as the participations concerned are to be fully deducted from eligible own funds.

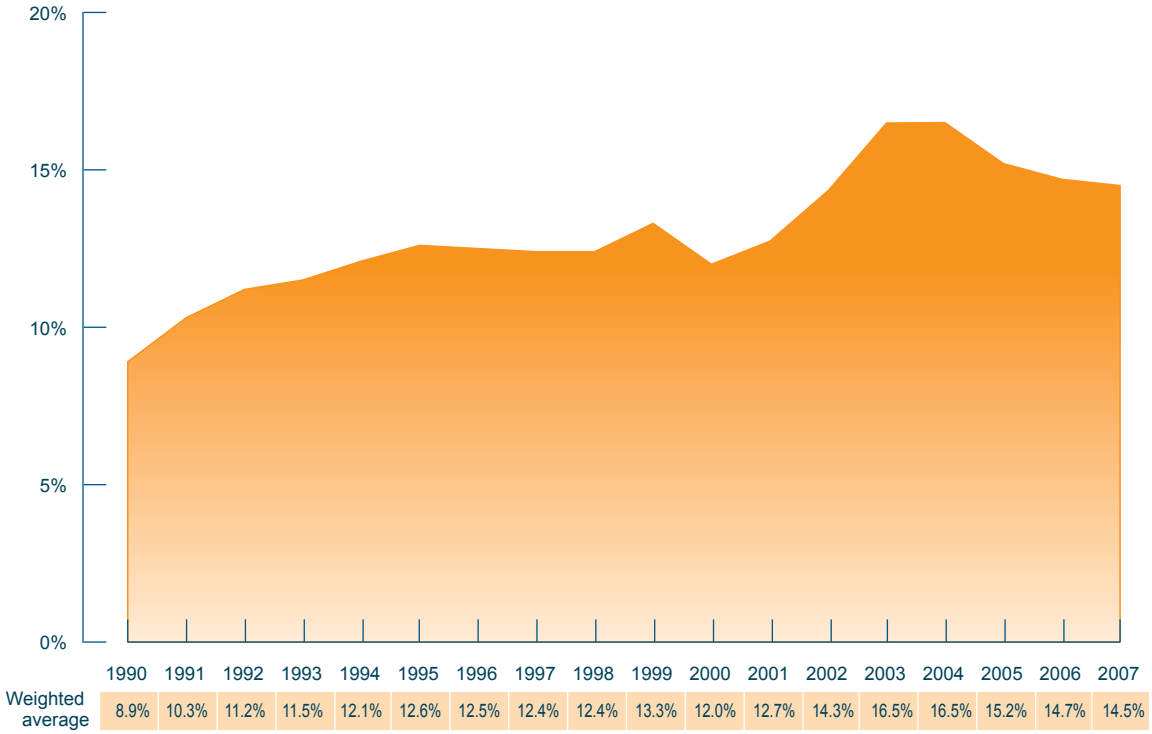
(in million EUR)

Numerator	2006	2007
Original own funds before deductions	***30,651***	***34,248***
Paid-up capital	10,022	11,153
Silent participation ("Stille Beteiligung")	2,320	1,771
Share premium account, reserves and profits brought forward	15,680	19,126
Funds for general banking risks	1,315	1,416
Profits for the financial year	1,019	781
Specific consolidation items	294	396
Items to be deducted from original own funds	***-1,024***	***-1,582***
Own shares	-35	0
Intangible assets	-444	-932
Losses brought forward and loss for the financial year	-112	-139
Specific consolidation items	-433	-511
ORIGINAL OWN FUNDS (TIER 1)	**29,627**	**32,666**
Additional own funds before capping	***7,579***	***7,514***
Upper TIER 2	3,957	4,121
of which : cumulative preference shares with no fixed maturity	*29*	*27*
of which: subordinated upper TIER 2 debt instruments	*2,879*	*2,997*
Lower TIER 2	3,622	3,393
Lower TIER 2 subordinated debt instruments and cumulative preference shares with fixed maturity	*3,622*	*3,393*
ADDITIONAL OWN FUNDS AFTER CAPPING (TIER 2)	**7,578**	**7,460**
Sub-additional own funds before capping	***30***	***69***
SUB-ADDITIONAL OWN FUNDS AFTER CAPPING (TIER 3)	**30**	**33**
OWN FUNDS BEFORE DEDUCTIONS (T1+T2+T3)	**37,235**	**40,160**
ITEMS TO BE DEDUCTED FROM OWN FUNDS	**1,341**	**1,625**
Items of share capital in other credit and financial institutions in which the bank owns interest exceeding 10% of their share capital	1,164	1,395
Items of share capital in other credit and financial institutions in which the bank owns interest less or equal to 10% of their share capital	177	231
ELIGIBLE OWN FUNDS	**35,895**	**38,534**
Denominator		
TOTAL CAPITAL ADEQUACY REQUIREMENT	**19,587**	**21,204**
of which: to cover credit risk	19,094	20,688
of which: to cover foreign exchange risk	80	101
of which: to cover trading risk	413	414
Ratio		
SOLVENCY RATIO (base 8%)[7]	**14.7%**	**14.5%**
SOLVENCY RATIO (base 100%)	**183.3%**	**181.7%**

[7] Eligible own funds/(total capital adequacy requirement * 12.5).

The graph below plots the development of the solvency ratio (base 8%) since 1990. The weighted average is the ratio of total eligible own funds in the financial centre and total weighted risks. This average takes into account all credit institutions according to their business volume.

Development in the solvency ratio (base 8%)



	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Weighted average	8.9%	10.3%	11.2%	11.5%	12.1%	12.6%	12.5%	12.4%	12.4%	13.3%	12.0%	12.7%	14.3%	16.5%	16.5%	15.2%	14.7%	14.5%

1.8.3. Development in the solvency ratio distribution (base 8%)

In non-aggregate terms, the high solvency ratio in the financial centre includes a limited number of banks whose ratio is situated within the weak capitalisation bands, i.e. below 10%. For instance, as at 31 December 2007, the percentage of banks with a solvency ratio below this 10% threshold was only 16.7%. Conversely, more than 51% of credit institutions of the financial centre recorded a solvency ratio exceeding 15%. However, this figure decreased slightly compared to 31 December 2006, when it exceeded 57%.

	2006		2007	
Ratio	**Number of banks**	**as % of total**	**Number of banks**	**as % of total**
<8%	0	0.0%	0	0.0%
8%-9%	4	3.5%	6	5.3%
9%-10%	9	7.8%	13	11.4%
10%-11%	10	8.7%	6	5.3%
11%-12%	9	7.8%	8	7.0%
12%-13%	6	5.2%	5	4.4%
13%-14%	5	4.3%	11	9.6%
14%-15%	6	5.2%	6	5.3%
15%-20%	20	17.4%	20	17.5%
>20%	46	40.0%	39	34.2%
Total	**115**	**100.0%**	**114**	**100.0%**

1.9. International expansion of Luxembourg banks

Number of branches established in the EU/EEA as at 31 December 2007

Country	Luxembourg branches established in the EU/EEA	Branches of EU/EEA banks established in Luxembourg
Austria	2	-
Belgium	6	1
Finland	-	1
France	1	5
Germany	1	16
Greece	1	-
Ireland	3	1
Italy	4	2
Netherlands	1	2
Portugal	2	2
Spain	3	-
Sweden	1	1
United Kingdom	4	4
Total	**29**	**35**[8]

Freedom to provide services within the EU/EEA as at 31 December 2007

Country	Luxembourg banks providing services in the EU/EEA	EU/EEA banks providing services in Luxembourg
Austria	29	21
Belgium	55	21
Bulgaria	5	-
Cyprus	10	2
Czech Republic	12	-
Denmark	33	7
Estonia	11	-
Finland	28	6
France	57	71
Germany	55	44
Gibraltar	2	3
Greece	29	1
Hungary	12	2
Iceland	5	1
Ireland	28	29
Italy	45	7
Latvia	11	-
Liechtenstein	2	2
Lithuania	11	-
Malta	9	3
Netherlands	44	25
Norway	13	3
Poland	15	1
Portugal	30	8
Romania	5	-
Slovakia	12	1
Slovenia	11	-
Spain	45	6
Sweden	27	3
United Kingdom	45	84
Total number of notifications	**696**	**351**
Total number of banks concerned	**75**	**351**

[8] Including an EU financial institution according to article 31 of the law of 5 April 1993 on the financial sector, as amended.

1.10. Banks issuing covered bonds (*Banques d'émission de lettres de gage, Pfandbriefbanken*)

Banks issuing covered bonds continued their development in 2007, notably following the increase in the number of players in the financial centre and owing to a rise in the volume of public sector covered bonds (*lettres de gage publiques)* issued.

Firstly, it must be noted that a new entity, namely Dexia LdG Banque S.A., a subsidiary of Dexia Banque Internationale à Luxembourg S.A. joined the other four banks issuing covered bonds already active in the financial centre. Dexia LdG Banque S.A. was granted authorisation as bank issuing covered bonds in July 2007 and launched its first issue, rated AAA, in the fourth quarter of 2007.

As at 31 December 2007, the balance sheet of those five banks totalled EUR 50.6 billion (against EUR 44 billion at the end of 2006). The total of public sector covered bonds issued (and in circulation) by these banks amounted to EUR 32.6 billion compared to EUR 27.5 billion at the end of 2006.

Issues of covered bonds are guaranteed by ordinary cover assets and by substitute cover assets. As at 31 December 2007, public sector covered bonds in circulation benefited from an over-collateralisation (nominal value) of EUR 5.8 billion. Over-collateralisation calculated according to the current value amounted to EUR 4.6 billion as at 31 December 2007.

The ordinary cover assets of public sector covered bonds for the five issuing banks break down as follows:

- claims on or guaranteed by public organisations: EUR 10.4 billion;
- bonds issued by public organisations: EUR 20.7 billion;
- public sector covered bonds of other issuers: EUR 1.4 billion;
- derivative transactions: EUR 2.5 billion.

Besides these ordinary cover assets, the banks used substitute cover assets to cover their public sector covered bonds amounting to EUR 3.5 billion as at 31 December 2007.

Erste Europäische Pfandbrief- und Kommunalkreditbank, Aktiengesellschaft in Luxembourg continued to be the only bank issuing mortgage covered bonds (*lettres de gage hypothécaires*). The cover assets of these mortgage covered bonds are exclusively made up of other mortgage covered bonds complying with the provisions of article 43(4) of the law of 20 December 2002 on undertakings for collective investment, as amended. As at 31 December 2007, the total volume of mortgage covered bonds issued reached EUR 150 million; these bonds are guaranteed by cover assets worth EUR 183.9 million. Over-collateralisation (nominal value) represented EUR 33.9 million, while over-collateralisation according to the current value was EUR 33 million as at 31 December 2007.

Owing to the faultless quality of investments of the specialised banks and the scale of over-collateralisation in relation to the covered bonds issued, public sector and mortgage covered bonds continue to receive an AAA rating from the rating agency Standard & Poor's. Moreover, the covered bonds issued by EUROHYPO Europäische Hypothekenbank S.A. also received an AAA rating from a second rating agency, namely FITCH IBCA.

2. PRUDENTIAL SUPERVISORY PRACTICE

2.1. Objectives of the supervisory practice

The purpose of supervising banks is to:

- ensure the security of the public's savings by monitoring the solvency and prudent management of the banks;
- ensure financial stability and proper functioning of the banking system as a whole;
- protect the reputation of the financial sector by penalising ethically unacceptable conduct.

In order to achieve these objectives of public interest, the CSSF monitors the implementation by credit institutions of the laws and regulations relating to the financial sector.

2.2. Major events in banking supervision in 2007

The year 2007 was marked by substantial changes in EU regulations that required sustained efforts both from banks and from the regulator. These regulations are highly complex and intended to regulate every aspect down to the smallest detail.

Firstly, there is the Basel II regime that came into effect on 1 January 2008 and whose purpose is to improve the sensitivity of regulatory capital requirement with respect to the risks that credit institutions really incur. Banks wishing to use their internal models for the purpose of calculating the capital requirement had to obtain validation from the CSSF. The CSSF carried out validation processes for 23 banks (cf. point 2.8. below). A certain number of those missions were performed in co-operation with other European authorities. Great efforts were made by CSSF agents to become familiar with the new regulations. Those efforts should continue in the coming years as experience shows that several years of concrete work with complex regulations are necessary to get an in-depth knowledge thereof.

The second pillar of the Basel II regime, the supervisory review and evaluation process, will be implemented in the course of 2008.

Secondly, there are the MiFID regulations. This set of regulations, supposed to improve the protection of consumers using financial services, required substantial efforts from professionals, which had to be compliant as from 1 November 2007. In accordance with its supervisory model, the CSSF requires external auditors to monitor compliance with those provisions, and to report thereon in their analytical reports. In order to fulfil European requirements, the CSSF will probably have to check compliance with MiFID provisions itself as well.

Thirdly, the recast of prudential reporting through the introduction of COREP (capital ratio) and FINREP (financial reporting) tables in 2008 must be mentioned. The purpose of both reportings, developed at CEBS level, is, among others, to lighten the administrative burden of banks by harmonising reportings throughout the EU. While the introduction of COREP was required under Basel II, FINREP, which must be based on IFRS, was introduced following consultation of the industry, the majority of which was in favour of a reporting based on IFRS.

Last but not least, turmoil in the subprime mortgage market, whose effects are described in point 2.17.2 below, came to the fore in the middle of 2007.

2.3. Monitoring of quantitative standards

Quantitative standards, designed to ensure financial stability and risk spreading by credit institutions, cover:

- evidence of minimum equity capital;
- a maximum ratio between own funds on the one hand and capital requirements on the other hand;
- limitation of risk concentration on a single debtor or a group of associated debtors;
- liquidity ratio;
- limitation of qualifying holdings.

In the year under review, the CSSF intervened only once in writing with respect to non-compliance with the capital ratio to request explanations on the measures envisaged in order to settle the situation within a reasonable time-frame.

In 2007, the CSSF intervened four times in writing with respect to non-compliance with the liquidity ratio, compared to five times in 2006.

In all instances of exceeding a ratio, the CSSF required the institution concerned to provide information on the measures taken to remedy the situation. Those situations have been sorted out either immediately or within the allocated time-frame where acceptable explanations could be given.

Within the scope of monitoring compliance with large exposure limits, the CSSF intervened 12 times (38 in 2006) in writing, either to inform that the maximum level of large exposures had been exceeded and to request the bank concerned to provide information on the measures taken to bring back the commitments within the limits, or to reply to banks on the interpretation of rules. Where such interpretation results in an overrun of large exposure limits, the bank concerned must provide information on the measures it intends to implement to bring back the commitments within the regulatory limits.

A case worth describing further concerns the indirect concentration risk that a bank may incur.

In general, a bank must not be exposed to a risk exceeding 25% of own funds on an individual counterparty. Where a bank's commitment is covered by the pledging of a securities portfolio, the amount to be considered for the limitation of large risks may take into account the amount of that securities portfolio. Care must be taken however that the bank does not incur an indirect concentration risk on issuers of the pledged securities by this means. This can be avoided in particular through adequate diversification of the pledged portfolios. In any case, it must be ensured that the default of an issuer does not entail any cumulated loss exceeding 25% of own funds, taking into account all the credits that are pledged by portfolios containing securities of that issuer.

The CSSF expects banks, whose pledged assets structure gives reason to presume indirect concentration risk, to perform stress tests on a regular basis. Moreover, the CSSF regularly requires to be provided with the detail of the pledged portfolios for credits that exceed, before weighting, the 25% own funds limit.

2.4. Monitoring of qualitative standards

The CSSF relies on several instruments to assess the quality of the banks' organisation:

- analytical reports prepared by external auditors;
- management letters and similar reports prepared by external auditors;
- on-site inspections undertaken by CSSF agents;
- reports prepared by internal auditors of the banks.

These reports are processed according to a methodology laid down in the CSSF's internal procedures. The CSSF's response depends on the seriousness of the problem raised and whether it is repetitive in nature. It varies from simple monitoring of the problem on the basis of reports, through the preparation of deficiency letters, to convening the bank's management or on-site inspections undertaken by CSSF agents. Where necessary, the CSSF may use its formal powers of injunction and suspension.

During 2007, the CSSF sent 87 deficiency letters to banks based on shortcomings in terms of organisation.

2.5. Analytical reports

The analytical report prepared by the external auditor is one of the most important instruments to assess the quality of the organisation and the exposure to different risks. The CSSF requires an analytical report on a yearly basis for every Luxembourg credit institution as well as for the Luxembourg branches of non-EU credit institutions. Furthermore, credit institutions supervised on a consolidated basis are required to submit a yearly consolidated analytical report and individual analytical reports of each subsidiary included in the consolidation and carrying out an activity of the financial sector.

Analytical reports were made compulsory in 1989 through a circular, which was recast in 2001 (circular CSSF 01/27) in order to take account of the regulatory and prudential developments.

In 2007, the CSSF analysed 133 individual analytical reports (119 in 2006), 30 consolidated analytical reports (25 in 2006) and 109 analytical reports of subsidiaries of Luxembourg banks (80 in 2006).

2.6. Co-operation with external auditors

Article 54 of the law on the financial sector governs the relationship between the CSSF and the external auditors. This article confers upon the CSSF the power to establish the rules relating to the scope of the audit mandate and the content of the audit report. The professionals supervised shall communicate all the reports issued by the external auditor within the course of the audit of the accounting documents to the CSSF.

Furthermore, the external auditors are required by law to inform the CSSF swiftly of any serious facts, defined more specifically under article 54(3) of the aforementioned law, which have come to their attention in the course of their duties.

The supervision of the CSSF is thus based to a large extent on the work of the external auditors and their reports. Since 2002, the CSSF holds annual meetings with the main audit firms in order to exchange opinions on specific issues encountered within the supervised institutions. Discussions also address the quality of the reports produced and the results of the inspections.

2.7. On-site inspections

The programme of inspections to be carried out during the year is set up at the beginning of the year and is based on the assessment of the risk areas of the various credit institutions. Inspections carried out by CSSF agents generally follow standard inspection procedures, in the form of discussions with the people responsible, assessment of procedures and verification of files and systems.

Since 2004, inspections focus on the internal governance of credit institutions, i.e. the functioning of the banks' bodies, the position of the bank within the group, as well as the efficiency of the control functions such as internal audit. Indeed, the verification of the proper operation of internal governance and control functions has proved to present the best means used/results ratio for the CSSF teams.

During the year under review, 52 controls were made, against 36 in 2006. As in 2006, the purpose of some controls was to analyse "credit" activity, especially Lombard loans and mortgage loans. Moreover, the internal model validation missions within the scope of the implementation of the Basel II framework continue to absorb an important part of the capacities (cf. point 2.8. below).

In addition to the actual on-site inspections, the CSSF also visits the newly established banks on their premises.

2.8. Basel II missions

Circular CSSF 06/273 of 22 December 2006 transposed into Luxembourg legislation the parts of Directives 2006/48/EC and 2006/49/EC (also known as "Basel II") that concern capital ratios. This new regime introduced a material change as the banks may opt to use internal ratings-based systems (IRB) and internal models to estimate certain parameters that are included in the calculation of the capital requirement. These models must meet a large number of quantitative and qualitative criteria and be subject to validation by the supervisory authority.

As the banks established in Luxembourg are very often subsidiaries of European groups, this validation process takes place in close consultation between the home and host authorities, in accordance with Directive 2006/48/EC. It should be noted that for the time being the validation process only concerns EU banks.

Great efforts were made in 2007 to validate IRB systems and models developed by banks.

Various cases may exist which are handled differently. First, a distinction must be made between IRB systems and models to calculate the capital requirement for credit risk and the models to calculate the capital requirement for operational risk. Then, for both types of models, a distinction should be made between the following cases:

a) *use by a local subsidiary of a model developed by the group*

In this case, the parent's home authority validates the model's theoretical bases while the CSSF's role is limited to verifying its local use. The models must also be used for day-to-day risk management in order to be eligible for computing regulatory capital requirements. Verification of the local use of credit risk management models thus mainly covers the following points: the use of the models for risk management and the experience gained (use test and experience test), coverage of all the exposures by the models, allocation of exposures to the relevant grades and pools, stress tests and internal governance relating to those models. As regards the operational risk management models, the CSSF's mission mainly concerns the use of the model on a day-to-day basis, the processes of stocktaking and of reporting of operational losses, and the internal capital allocation system. The results of this mission are then communicated to the home authority and to the bank.

b) *use by a local subsidiary of a model developed at local level*

In this case, the CSSF's mission, besides the use test described in point (a) above, consists in checking the model's theoretical bases. This mission thus mainly concerns the development and internal validation process review, internal governance (role of the management, the risk management functions and the internal audit), conception (philosophy of internal ratings, masterscale) and methodologies (expert models, statistics, neurals, causals, etc.). The observations made are then communicated to the home authority and to the bank.

c) model development by a bank where the CSSF is the home authority

In that case, the validation process is the same as that described in points (a) and (b), except for the communication to a home authority of course.

In 2007, the CSSF carried out validation missions with 23 banks. In six cases, only the local application of a credit risk management model was verified. The local application of an operational risk management model was verified in eight cases. The local application of models both for credit risk and operational risk management was verified within one bank.

Seven banks developed a credit risk management model locally and one bank developed an operational risk management model locally.

2.9. Combating money laundering

Article 15 of the law of 12 November 2004 concerning the fight against money laundering and financing of terrorism provides that the CSSF is the relevant authority to ensure compliance with professional obligations as regards the fight against money laundering and financing of terrorism by every person subject to its supervision. However, non-compliance with the professional obligations in full knowledge falls under the penal law and relevant proceedings thus fall within the competence of the State Prosecutor's office.

Before the adoption of this law, non-compliance with professional obligations, even unintentional, was subject to criminal sanctions and the State Prosecutor's office was consequently responsible for prosecution.

The CSSF uses the following instruments to supervise compliance with these rules: reports of external auditors and those prepared by internal auditors, as well as the inspections made by CSSF agents.

During the year under review, the CSSF sent 12 letters to banks in relation to shortcomings concerning money laundering. These letters, based on on-site inspections and/or external or internal audit reports, listed the shortcomings identified and enquired about the corrective measures envisaged. The most frequently observed deficiencies concern, among others, incomplete documentation of customer files, incomplete anti-money laundering procedures and absence of qualitative monitoring of client transactions as opposed to purely quantitative monitoring.

The yearly analytical report prepared by external auditors must specifically cover compliance with legal requirements and the adequate implementation of internal procedures concerning the prevention of money laundering.

The law of 12 November 2004 requires banks with branches or subsidiaries abroad to ensure that these entities comply with Luxembourg professional obligations, as far as these subsidiaries or branches are not subject to equivalent professional obligations provided for by the laws applicable at the place of their establishment. The CSSF verifies compliance with this requirement by means of analytical reports of external auditors to be prepared for each subsidiary carrying out an activity of the financial sector. Furthermore, the CSSF requires that the internal audit of the Luxembourg parent company periodically verify that subsidiaries and branches abroad comply with the group's anti-money laundering directives. The results of these inspections must be included in the summary report which has to be submitted to the CSSF on an annual basis.

2.10. Management letters

Management letters drawn up by external auditors for the attention of the banks' management are an important source of information as regards the quality of the credit institutions' organisation. In these reports, the external auditors point out weaknesses they observed in the internal control system in the course of their assignment. During 2007, the CSSF analysed 68 management letters and similar documents.

2.11. Meetings

The CSSF regularly holds meetings with bank executives to discuss business and any problems. It also requires prompt notification by the banks if a serious problem arises. In 2007, 224 meetings were held between CSSF representatives and bank executives.

2.12. Specific controls

Article 54(2) of the law of 5 April 1993 on the financial sector, as amended, allows the CSSF to require an external auditor to conduct a specific audit in a given institution. The CSSF did not make use of this power in 2007. However, on two occasions it has invited banks to specifically appoint their external auditor to audit specific business areas and to submit the results thereof to the CSSF.

2.13. Internal audit and compliance reports

The CSSF takes into account the work of the internal audit when assessing the quality of the organisation and risk management by analysing the summary report which the internal auditor must prepare every year, as well as the report of the Compliance officer. In 2007, the CSSF analysed 126 summary reports (125 in 2006). It also requested 34 specific internal audit reports in order to obtain more detailed information on particular subjects.

2.14. Supervision on a consolidated basis

As at 31 December 2007, 34 banks under Luxembourg Law (33 at the end of 2006), two financial holding companies under Luxembourg law (*idem* in 2006), as well as one financial holding company incorporated under foreign law (*idem* in 2006) were supervised by the CSSF on a consolidated basis.

The conditions governing submission to a consolidated supervision, the scope, content and methods of supervision on a consolidated basis are laid down in Part III, Chapter 3 of the law of 5 April 1993 on the financial sector, as amended. The practical application of the rules governing supervision on a consolidated basis is explained in circular IML 96/125.

As circular IML 96/125 does not take into account the amendments of the legislation introduced by the law of 7 November 2007 (the "Basel II law") transposing Directive 2006/48/EC into national law, this circular is being recast. The major amendments are in relation to the following points:

- enhanced co-operation between prudential supervisory authorities with respect to consolidated supervision (article 50-1 of the law on the financial sector);
- extension of the scope of consolidated supervision which now also includes capital adequacy for operational risk, the internal capital adequacy assessment process and internal governance (article 51 of the law on the financial sector).

The CSSF pays particular attention to the "group head" function set up at the Luxembourg establishment falling under its consolidated supervision. Thus, the CSSF sees more specifically to the way the Luxembourg parent company communicates its policies and strategies to its subsidiaries as well as to the controls set up at the Luxembourg parent company in order to monitor the organisation and activities of the subsidiaries, and their exposures.

The means the CSSF may use for its supervision on a consolidated basis are manifold:

- The CSSF requires periodic reports reflecting the financial situation and the consolidated risks of a group subject to its consolidated supervision.
- The reports prepared by the external auditors are another source of information. Circular CSSF 01/27 defining the mission of the external auditor requires that an annual consolidated analytical report of a group subject to the consolidated supervision of the CSSF must be drawn up. The purpose of this consolidated report is to provide the CSSF with an overview of the group's situation and to inform on the risk management and risk structure of the group.
- The CSSF requires an individual analytical report for each major subsidiary.
- By virtue of circular IML 98/143 on internal control, a summary report on the activities carried out by the internal audit department is to be communicated to the CSSF on an annual basis. The CSSF requires that the scope of intervention of the internal audit of the Luxembourg parent company be extended also to the subsidiaries in Luxembourg and abroad. This report must mention the controls carried out within the subsidiaries and the results thereof. The main observations made within the subsidiaries as regards the compliance function defined in circular CSSF 04/155 shall also be mentioned therein.
- The CSSF's information is supplemented by contacts, exchange of letters and meetings with supervisory authorities of the subsidiaries' host countries. Within the scope of its supervision on a consolidated basis, the CSSF expects to systematically obtain, from the banks and financial holding companies subject to consolidated supervision, information on any intervention of the host country authorities with the subsidiaries, where these interventions concern non-compliance with domestic regulations and aspects regarding organisation or risks of these subsidiaries.
- As regards groups with an important network of subsidiaries, the CSSF follows the development of the financial situation and the risks of the subsidiaries included in the consolidated supervision by means of regular meetings with the management of the credit institution or of the financial holding company under consolidated supervision.
- The CSSF performs on-site inspections that cover, on the one hand, the manner in which the parent company sets up its policies and implements its strategies within the subsidiaries and, on the other hand, the follow-up applied to the subsidiaries.

Until now, the CSSF has not carried out itself any on-site inspection at the premises of foreign subsidiaries of Luxembourg banks.

The CSSF also investigates indirect participations of banks subject to its consolidated supervision in accordance with the terms of circular IML 96/125.

The law of 5 November 2006 on the supervision of financial conglomerates and amending the law of 5 April 1993 on the financial sector requires the CSSF to verify henceforth that Luxembourg credit institutions whose parent undertaking is a credit institution or a financial holding company having its head office in a third country, are subject to a consolidated supervision by the competent authority of that third country that is equivalent to the consolidated supervision performed by the CSSF on credit institutions and financial holding companies. If there is no equivalent consolidated supervision by the third country, the CSSF must perform a consolidated supervision of this group or apply another method in order to achieve the objectives of consolidated supervision.

2.15. Supplementary supervision of financial conglomerates

The law of 5 November 2006 on the supervision of financial conglomerates introduces a supplementary supervision on financial conglomerates into Luxembourg law. A financial conglomerate is a group that includes at least one important regulated entity within the banking or investment services sector and one important entity within the insurance sector.

The law requires the CSSF to perform a supplementary supervision of the financial conglomerates for which it exercises the role of coordinator of the supervision, the coordinator being the authority responsible for the coordination and supplementary supervision of the financial conglomerate.

The CSSF's supplementary supervision of financial conglomerates does not affect at all the sectoral prudential supervision, both on the individual and consolidated level, by the relevant competent authorities.

The practical consequences of this law for Luxembourg credit institutions and investment firms are limited as things stand at present. Indeed, the CSSF has not identified any financial conglomerate for which it should exercise the role of coordinator of this supplementary supervision at this stage.

2.16. International co-operation in matters of banking supervision

International co-operation, which has already been very comprehensive in the past, was further strengthened by Directive 2006/48/EC relating to the taking up and pursuit of the business of credit institutions. There are three types of co-operation:

- the traditional bilateral co-operation as performed since the beginning of the 1980s;
- the strengthened multilateral co-operation with respect to certain groups; and
- the co-operation as set out in article 129 of the above-mentioned Directive.

2.16.1. Traditional bilateral co-operation

Following the implementation of the second banking Directive, the CSSF has concluded memoranda of understanding with the banking supervisory authorities of several Member States of the European Economic Area[9] in the 1990s, with a view to specifying the terms of co-operation. These memoranda concern in particular the supervision of credit institutions involved in cross-border operations by way of the freedom to provide services or through the creation of branches.

Moreover, in accordance with the legal provisions in force, the CSSF co-operates and exchanges information on an informal basis with a number of other counterpart authorities.

In 2007, the CSSF held three bilateral meetings with banking supervisory authorities in order to exchange prudential information on supervised institutions having a presence in both countries.

Besides the consultations required under the European Directives, the CSSF also informs the relevant authorities of all significant facts relating to supervision. In particular, it consults the relevant authorities regarding acquisitions of major holdings and restructurings of share ownerships.

[9] Belgium, Finland, France, Germany, Ireland, Italy, Netherlands, Norway, Portugal, Spain, Sweden and the United Kingdom.

2.16.2. Strengthened multilateral co-operation with respect to certain groups

The decentralised organisation of operational management units and centres of competence of certain banking groups called for an adaptation of the co-operation and prudential supervisory modes of the activities of these groups. In this context, the CSSF has signed specific co-operation agreements with:

- the Belgian and French authorities for the supervision of the DEXIA group;
- the Belgian and Dutch authorities for the supervision of the FORTIS group;
- the German authority for the supervision of the Clearstream group;
- the Canadian and Belgian authorities for the supervision of the RBC Dexia group.

The key objective of such specific co-operation agreements is to ensure that all banking activities of these groups are adequately supervised. To this end, the authorities ensure in particular that the various sets of regulations are applied in a consistent manner in order to avoid any unbalanced treatment within the groups.

Co-operation between authorities is enacted on several levels:

- close consultation between the authorities in order to coordinate and align their prudential supervision;
- continuous and systematic exchange of information on any significant event likely to impact the group or its main constituent entities;
- regular consultation for the principal purpose of updating the list of points requiring the attention of the authorities within these groups, co-ordinating the drafting of control plans and, finally, examining the appropriateness of on-site inspections to be carried out by the competent authority in close co-operation with the other relevant authorities.

Besides frequent exchanges of information between the persons directly responsible for the supervised entities at each authority, the CSSF attended 27 meetings within the framework of this specific co-operation. It should be noted that in 2007, a high number of these meetings between authorities exclusively concerned their co-operation with respect to the implementation of new risk management models implemented by those banking groups, in order to prepare for the Basel II rules.

2.16.3. Co-operation in accordance with article 129 of Directive 2006/48/EC

Co-operation between European competent authorities assumes a new dimension under article 129 of Directive 2006/48/EC which requires intensive co-operation between the relevant competent authorities of cross-border banking groups and strives towards a more centralised supervision of these large cross-border groups at EU level.

Thus, the competent authority for the consolidated supervision of a European banking group shall henceforth plan and coordinate the prudential activities in co-operation with the other relevant competent authorities. In 2007, the CSSF participated in six meetings concerning each a large banking group and which were held within the context of strengthening the co-operation between European authorities for the purpose of consolidated supervision.

Similarly, for cross-border banking groups seeking to use advanced approaches for the calculation of capital requirements for credit risk or operational risk, European regulations require that the competent authorities co-operate closely to decide on authorising the use of these advanced approaches by the banking group. In the absence of a joint decision, the authority competent for the consolidated supervision of the banking group makes its own decision, which must be recognised by the other competent authorities as final and be applied by these authorities. In this context, the CSSF verified in 2007 the local use by the Luxembourg entity of those new risk management models and capital measurement models implemented by various banking groups and communicated its conclusions to the competent authorities in charge of the consolidated supervision (please also refer to point 2.8. "Basel II missions").

2.17. Special points and decisions

2.17.1. Solo consolidation

The law of 7 November 2007 transposing into the law of 5 April 1993 on the financial sector, as amended, the Directives commonly called Basel II, introduced the possibility to apply the transparency principle to the calculation of capital requirements for the purpose of computing the non-consolidated capital ratio, also known as "solo consolidation".

Article 51(9) of the law on the financial sector allows parent credit institutions to include the assets of certain subsidiaries in the calculation of capital requirement on an individual basis (non-consolidated) where these subsidiaries meet certain conditions and where there are material exposures and liabilities to those parent credit institutions. The application of the transparency principle is subject to prior authorisation by the CSSF.

Up to now the CSSF received only one request to apply the transparency principle, to which it responded positively.

2.17.2. Turmoil in the US subprime mortgage market

The turmoil in the financial markets caused by the US subprime segment came to the fore in July 2007 with the problems experienced by two Bear Stearns funds and the rescue of the German bank IKB. The market liquidity of ABS dried up rapidly and their conduits had to face refinancing problems through short-term securities issues, requiring them to use credit lines granted by banks. The lack of information on the exposures of the different banking groups in the subprime market led to a confidence crisis and a disruption in the interbank market. Finally, an extension of the spreads provoked a generalised devaluation of the bond market, extending also to issuers without visible solvency problems.

From the beginning of August 2007, the CSSF had a complete view of the subprime exposures of Luxembourg banks, i.e. the banks whose solvency is supervised by the CSSF, excluding EU branches. These exposures amounted to EUR 2.5 billion and were concentrated within a limited number of specialised banks. They take very different forms, which makes it difficult to compare risks, i.e. credit lines to conduits, capital notes of conduits, AAA-rated MBS securities, etc. The relevant information was transmitted immediately to the supervisory authority competent for the consolidated supervision of those banks. The CSSF continues to monitor the situation within the banks concerned.

Following the extension of bond spreads, a certain number of banks incurred valuation losses on their securities portfolio, without those securities being affected by a solvency risk of their issuer. According to the assessment method applied, those capital losses put a more or less serious strain on net results.

The following preliminary conclusions can be drawn at prudential level from the turmoil.

Risk management based on external ratings is quite insufficient. Every exposure, be it in the form of loans, securities, credit lines, guarantees, etc., must be subject to an in-depth analysis of individual credit risk by the bank itself. At the most, external ratings should be used as additional information, but must not replace the banks' own risk analysis.

The liquidity of financial instruments cannot be presupposed. Past experience shows how fast apparently liquid markets can dry up and force banks to honour credit lines. Risk management models must take into account a sudden lack of market liquidity.

The EU prudential regulations under Basel I provided for a 0% risk weighting for short-term credit lines (less than one year) for the calculation of the capital ratio, which paved the way for the incurrence of major risks versus own funds. As this provision was laid down in an EU Directive, it was very difficult for supervisory authorities to object to its implementation without being accused of practising gold-plating. The introduction of Basel II in 2008 will change that situation.

2.17.3. Securities portfolio valuation

In 2007, the CSSF authorised the banks that requested it to valuate without restriction their portfolios of debt securities held as financial fixed assets according to the provisions of the law of 17 June 1992 relating to the annual accounts and consolidated accounts of credit institutions, as amended.

This law, which transposed Directive 86/638/EEC into national law, provides for the valuation at purchase price of the debt securities held as financial fixed assets without prejudice to value adjustments for permanent value reduction. In its reporting instructions issued in 1992, the IML (the CSSF's predecessor) submitted this valuation method to certain restrictions that were not provided for by the law and which imposed a quite large use of this lower of cost or market valuation method. The CSSF chose to abandon those restrictions for the following reasons:

- a general willingness to stop introducing, and even to abolish existing requirements or restrictions that are not provided for by European Directives;
- the entry into force of the law of 16 March 2006 relating to the introduction of international accounting standards, which introduces an enhanced valuation transparency and imposes the disclosure of the latent non-provisioned capital loss, as well as the basis for expecting that the book value will be recovered.

2.17.4. Professional secrecy and cascade outsourcing

The law of 13 July 2007 on markets in financial instruments (MiFID Law) automatically extended the exception to professional secrecy to the banks within the scope of a service contract. This implies that a Luxembourg bank under a subcontracting agreement with another Luxembourg bank is allowed to transmit confidential information to the service providing bank without violating its professional secrecy.

This new provision calls for some warnings and clarifications. Considering in particular the practice of cascade outsourcing, care must be taken to differentiate between the confidential character of the data transmitted and the responsibility of the various parties involved.

It is therefore highly recommended that the bank that transmits its data obtains information from the service provider whether it practices cascade outsourcing. If so, the bank that is subcontracting must assess whether it is allowed thereto or obliged to request authorisation from its customers. It is not enough to consider that transmitting confidential data to a service provider is legally allowed. In addition, the bank must verify whether the contractual relations with clients do not prohibit such outsourcing.

Moreover, the service providing bank that practises cascade outsourcing must inform the client bank thereof and assess whether the data provided can be transmitted to another service provider. If so, it must verify that the client bank has the necessary authorisation from its clients to make those outsourcings.

Finally, it is highly recommended to lay down in the service agreement the nature of the data transmitted and the authorisation or prohibition made to the service provider to transmit data to another service provider.

The CSSF considers that the responsibility for confidential data protection lies both with the bank that practises outsourcing and with the service provider.

From a legal point of view, the bank that transmits data out of the Luxembourg financial sector is responsible for safeguarding professional secrecy and must therefore ensure that the data is transmissible, i.e. it must ensure that the data does not fall under the Luxembourg banking secrecy, or that the necessary authorisations have been obtained from the clients.

CHAPTER II

SUPERVISION OF UNDERTAKINGS FOR COLLECTIVE INVESTMENT

1. DEVELOPMENTS IN THE UCI SECTOR IN 2007

1.1. Major events in 2007

In 2007, the sector of undertakings for collective investment (UCIs) recorded a growth of 11.63% in the net assets managed and of 28.15% in the number of UCIs. 57.64% out of the 2,868 UCIs registered on the official list as at 31 December 2007 were UCITS governed by Part I of the law of 20 December 2002, as amended.

The impact of the subprime and credit crises on the Luxembourg UCI sector remains very limited. A survey carried out by the CSSF in July and August 2007 indicated that only 0.14% of the total net assets of Luxembourg UCIs were invested in subprime securities. Nevertheless, in a climate of uncertainty and risk aversion, the credit crisis spread to other segments of the financial market and for some segments of the securitisation market, market liquidity is still missing. As a consequence of the subprime crisis, seven sub-funds of Luxembourg UCIs had to request the suspension of the redemptions and one UCI liquidated two sub-funds.

From an economic point of view, a slowdown in the demand for variable-yield UCIs and fixed-income UCIs has been registered in 2007 as compared to 2006. This slowdown in the demand for bond and equity UCI products mainly appeared in the third and fourth quarter of 2007 and is a direct consequence of the subprime and credit crises which affected all financial markets in 2007. Confronted with the uncertainties on financial markets, the demand for UCIs switched in 2007 to monetary UCIs and to UCIs with a diversified investment policy.

As regards the supply in new UCI products, the launch of UCI products with a diversified investment policy registered the most important growth as compared to any other UCI category in 2007. Guarantee-type UCIs as well soared in 2007. Moreover, UCIs with a 130/30 investment strategy whose objective is to reach a performance higher than traditional funds, while limiting risks, appeared recently.

At European level, Directive 2007/16/EC, transposed in Luxembourg through Grand-ducal regulation of 8 February 2008 as well as document CESR/07-044 contributed to remove certain legal uncertainties on the possibilities for UCIs to invest in financial instruments such as securities backed by other assets, index-based derivatives, credit derivatives, etc. Document CESR/07-434 clarified the conditions under which hedge fund indices may constitute eligible assets for UCITS. In this context, reference should also be made to circular CSSF 08/339.

The impact of Directive 2004/39/EC of 21 April 2004 on markets in financial instruments (MiFID Directive), transposed in Luxembourg by the law of 13 July 2007 on markets in financial instruments, on the Luxembourg UCI industry mainly affects management companies which perform a discretionary portfolio management activity.

At national level, the law of 13 February 2007 on specialised investment funds replaced the law of 19 July 1991 concerning UCIs the securities of which are not intended to be placed with the public. UCIs that were subject to the law of 19 July 1991 now fall *ipso jure* under the regime of the new law. Moreover, the law of 13 February 2007 on specialised investment funds presents a new legal framework for the launch of UCIs whose units or shares are intended for well-informed investors.

1.2. Development in the UCI sector

The number of UCIs registered on the official list amounted to 2,868 UCIs as at 31 December 2007 against 2,238 UCIs at the end of 2006, representing an increase of 630 entities. The number of newly registered UCIs recorded an upward trend with a total of 824 entities. The number of withdrawals amounted to 194 entities.

The inflow of new capital and the performance of the main financial stock exchanges led to a growth by EUR 214.6 billion in total net assets of Luxembourg UCIs in one year to reach EUR 2,059.4 billion as at 31 December 2007. This 11.6% increase originates for 87.8% from net issues and for 12.2% from the rise in stock markets. Net capital investment in Luxembourg undertakings for collective investment amounted to EUR 188.5 billion in 2007.

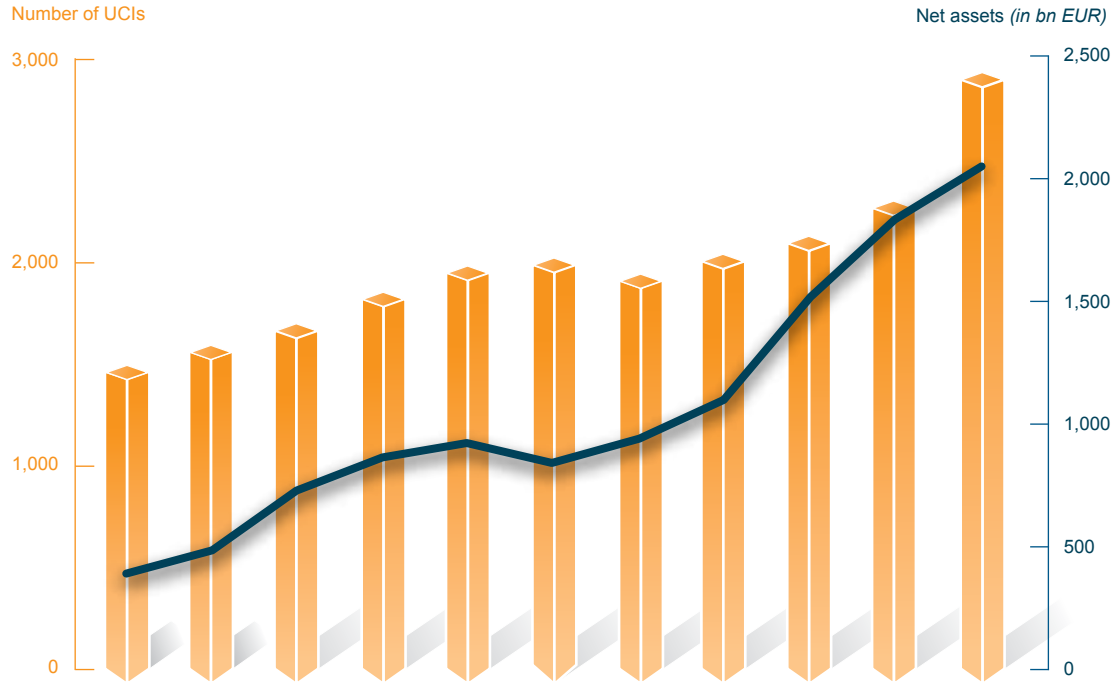
Development in the number and net assets of UCIs

	Number of UCIs	Registrations on the list	Withdrawals from the list	Net variation	in %	Net assets *(in bn EUR)*	Net issues *(in bn EUR)*	Variation in net assets *(in bn EUR)*	in %	Average net assets per UCI *(in bn EUR)*
1997	1,426	193	151	42	3.0%	391.8	50.1	83.2	26.9%	0.275
1998	1,521	234	139	95	6.7%	486.8	84.1	95.0	24.3%	0.320
1999	1,630	265	156	109	7.2%	734.5	140.1	247.7	50.9%	0.451
2000	1,785	278	123	155	9.5%	874.6	168.1	140.1	19.1%	0.490
2001	1,908	299	176	123	6.9%	928.4	121.7	53.8	6.2%	0.487
2002	1,941	222	189	33	1.7%	844.5	57.3	-83.9	-9.0%	0.435
2003	1,870	175	246	-71	-3.7%	953.3	82.6	108.8	12.9%	0.510
2004	1,968	202	104	98	5.2%	1,106.2	113.7	152.9	16.0%	0.562
2005	2,060	266	174	92	4.7%	1,525.2	236.3	419.0	37.9%	0.740
2006	2,238	345	167	178	8.6%	1,844.8	241.3	319.6	21.0%	0.824
2007	2,868	824	194	630	28.2%	2,059.4	188.5	214.6	11.6%	0.718

Over the last ten years, the number of UCIs has grown by 1,442 entities to 2,868 entities in 2007, which corresponds to an average growth of 10.1% per year.

Net assets have increased over the past ten years by EUR 1,667.6 billion, representing an average growth of EUR 166.8 billion per year. It should be pointed out that principally the years 2005 and 2006 experienced a strong growth, with + EUR 419 billion in 2005 and + EUR 319.6 billion in 2006.

Development in the number and net assets of UCIs



	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Units	1,426	1,521	1,630	1,785	1,908	1,941	1,870	1,968	2,060	2,238	2,868
Net assets	391.8	486.8	734.5	874.6	928.4	844.5	953.3	1,106.2	1,525.2	1,844.8	2,059.4

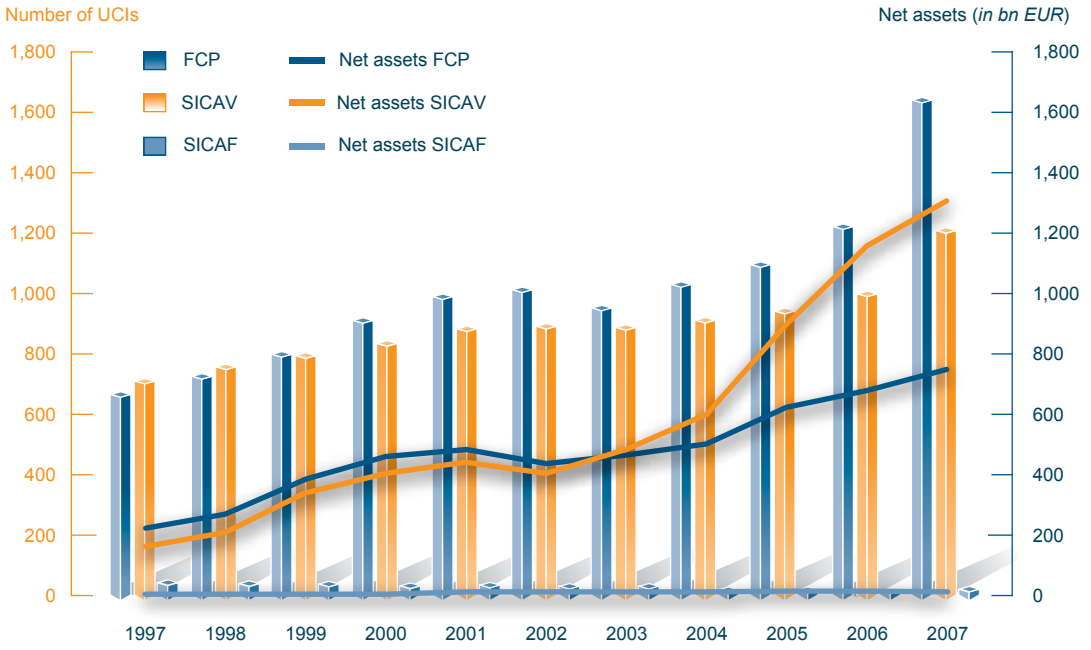
The breakdown of UCIs in *fonds communs de placement* (FCP), *sociétés d'investissement à capital variable* (SICAV) and *sociétés d'investissement à capital fixe* (SICAF) reveals that as at 31 December 2007, FCPs were still the prevailing form with 1,645 entities out of a total of 2,868 active UCIs, against 1,211 entities operating as SICAVs and 12 as SICAFs.

	FCP		SICAV		SICAF		Total	
	Number	Net assets *(in bn EUR)*	Number	Net assets *(in bn EUR)*	Number	Net assets *(in bn EUR)*	Number	Net assets *(in bn EUR)*
1997	668	225.0	718	161.1	40	5.7	1,426	391.8
1998	727	270.8	758	210.3	36	5.7	1,521	486.8
1999	800	385.8	795	341.0	35	7.7	1,630	734.5
2000	914	462.8	840	404.0	31	7.8	1,785	874.6
2001	994	482.1	885	441.5	29	4.8	1,908	928.4
2002	1,017	435.8	896	405.5	28	3.2	1,941	844.5
2003	957	466.2	888	483.8	25	3.3	1,870	953.3
2004	1,036	504.0	913	600.3	19	1.9	1,968	1,106.2
2005	1,099	624.3	946	898.2	15	2.7	2,060	1,525.2
2006	1,224	681.3	1,000	1,161.1	14	2.4	2,238	1,844.8
2007	1,645	748.7	1,211	1,308.4	12	2.3	2,868	2,059.4

FCPs' net assets reached EUR 748.7 billion, representing 36.4% of the total net assets of UCIs as at 31 December 2007. SICAVs' net assets amounted to EUR 1,308.4 billion at the end of the year 2007, representing 63.5% of the UCIs' total net assets. SICAFs' net assets amounted to EUR 2.3 billion as at 31 December 2007.

In terms of net assets, SICAVs strengthened their leading position with a 12.7% growth rate.

Breakdown of UCIs by legal status



The following table illustrates the distribution of UCIs depending on whether they fall within the scope of Part I or II of the law of 20 December 2002, as amended, or the law of 13 February 2007 relating to specialised investment funds (SIFs).

Breakdown of UCIs according to Parts I and II of the law and specialised investment funds

	Part I		Part II		SIF	
	Number	Net assets (in bn EUR)	Number	Net assets (in bn EUR)	Number	Net assets (in bn EUR)
1997	980	280.4	367	102.2	79	9.2
1998	1,008	360.2	400	111.0	113	15.6
1999	1,048	564.2	450	137.0	132	33.3
2000	1,119	682.0	513	153.3	153	39.3
2001	1,196	708.6	577	178.2	135	41.6
2002	1,206	628.9	602	171.6	133	44.0
2003	1,149	741.1	583	169.3	138	42.9
2004	1,303	929.3	516	131.2	149	45.7
2005	1,358	1,260.0	524	204.0	178	61.2
2006	1,469	1,516.5	552	249.9	217	78.4
2007	1,653	1,646.4	643	295.9	572	117.1

UCIs falling under Part I of the law of 20 December 2002, as amended, are those which comply with the provisions of the EU Directive on UCITS and which can therefore benefit from the marketing facilities provided. Part II encompasses all the other UCIs which solicit the public for the subscription of their units, whereas specialised investment funds are UCIs whose securities are reserved to well-informed investors according to the criteria set out in article 2 of the law of 13 February 2007.

Breakdown of UCIs and their net assets according to legal status and law applicable

Situation as at 31 December 2007	Number of UCIs				Net assets *(in bn EUR)*			
	FCP	SICAV	SICAF	Total	FCP	SICAV	SICAF	Total
Part I	1,064	589	0	1,653	567.647	1,078.694	0.000	1,646.341
Part II	246	388	9	643	109.590	184.097	2.252	295.939
SIF	335	234	3	572	71.434	45.646	0.035	117.115
Total	**1,645**	**1,211**	**12**	**2,868**	**748.671**	**1,308.437**	**2.287**	**2,059.395**

57.6% of UCIs registered on the official list as at 31 December 2007 were UCITS governed by Part I of the law of 2002 and 22.4% were other UCIs governed by Part II (non-coordinated UCIs). Specialised investment funds represented 20% of the 2,868 Luxembourg UCIs. Net assets were distributed at the same date as follows: 79.9% for UCIs under Part I, 14.4% for UCIs under Part II and 5.7% for specialised investment funds.

The following table compares the development in 2007 of the number of UCIs and net assets according both to the legal status and scope of the laws.

Breakdown of UCIs according to Parts I and II of the law and specialised investment funds

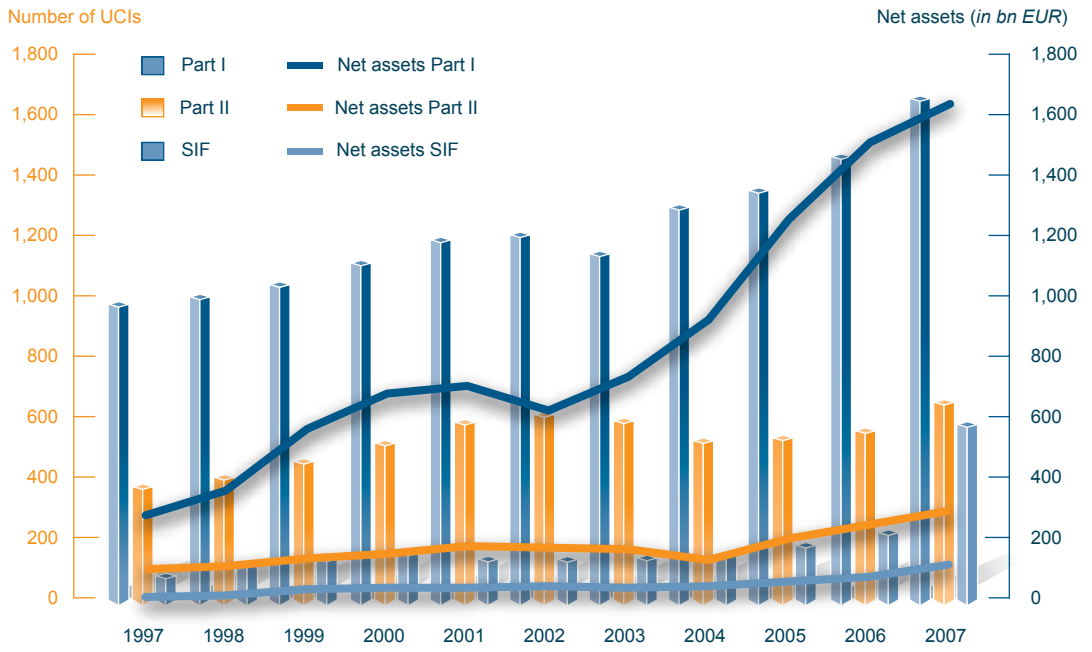
	2006				2007				Variation 2006/2007			
Number of UCIs	FCP	SICAV	SICAF	Total	FCP	SICAV	SICAF	Total	FCP	SICAV	SICAF	Total
Part I	915	552	2	1,469	1,064	589	0	1,653	16.28%	6.70%	-100.00%	12.53%
Part II	177	364	11	552	246	388	9	643	38.98%	6.59%	-18.18%	16.49%
SIF	132	84	1	217	335	234	3	572	153.79%	178.57%	200.00%	163.59%
Total	**1,224**	**1,000**	**14**	**2,238**	**1,645**	**1,211**	**12**	**2,868**	**34.40%**	**21.10%**	**-14.29%**	**28.15%**
Net assets *(in bn EUR)*	FCP	SICAV	SICAF	Total	FCP	SICAV	SICAF	Total	FCP	SICAV	SICAF	Total
Part I	532.457	984.024	0.059	1,516.540	567.647	1,078.694	0.000	1,646.341	6.61%	9.62%	-100.00%	8.56%
Part II	98.102	149.458	2.356	249.916	109.590	184.097	2.252	295.939	11.71%	23.18%	-4.41%	18.42%
SIF	50.778	27.577	0.039	78.394	71.434	45.646	0.035	117.115	40.68%	65.52%	-10.26%	49.39%
Total	**681.337**	**1,161.059**	**2.454**	**1,844.850**	**748.671**	**1,308.437**	**2.287**	**2,059.395**	**9.88%**	**12.69%**	**-6.81%**	**11.63%**

As far as Part I is concerned, the number of UCIs rose by 12.5% as compared to the end of the previous year and net assets recorded an increase of 8.6%. The number and net assets of UCIs under Part II increased by 16.5% and 18.4% respectively.

As a consequence of the replacement of the law of 19 July 1991 concerning UCIs the securities of which are not intended to be placed with the public by the law of 13 February 2007 on specialised investment funds (SIFs), the number of SIFs experienced a strong growth of 163.6% and an increase in their net assets of 49.4%.

It should be borne in mind in this context that the law of 20 December 2002, as amended, allows the creation of sub-funds and classes of units reserved to one or several institutional investors with respect to the UCIs under this law. However, the current reporting of UCIs does not allow to discern institutional investors in Parts I and II of the law of 20 December 2002, as amended.

Breakdown of UCIs according to Parts I and II of the law and specialised investment funds



In 2007, EUR 106.28 billion or 56.4% of net issues were registered for UCIs set up under Part I of the law of 20 December 2002 (EU UCIs), mainly for UCIs in the form of SICAVs. UCIs under Part II showed net issues totalling EUR 44.25 billion while net issues of specialised investment funds amounted to EUR 37.96 billion.

Breakdown of net issues according to Parts I and II of the law and specialised investment funds

(in million EUR)	FCP	SICAV	SICAF	Total	in %
Part I	37,987	68,332	-39	106,280	56.4%
Part II	11,409	32,956	-116	44,249	23.5%
SIF	20,754	17,205	0	37,959	20.1%
Total	**70,150**	**118,493**	**-155**	**188,488**	**100.0%**

1.3. Development in umbrella funds

In 2007, the number of umbrella funds increased by 301 entities. This structure, which brings together under the same legal entity several sub-funds centered on investment in a given currency, geographical region or economic sector, enables investors to re-focus their investment without having to switch to another investment fund. Promoters may thus offer, within a single entity, a whole range of sub-funds investing in equities, debt securities, money market securities or even sometimes warrants, thereby enabling investors to benefit from the best perspectives of return. The structure of umbrella funds also enables promoters to create new sub-funds and to manage a collective pool of assets which were normally not large enough for a separate management in a traditionally structured fund.

Umbrella funds

	Total number of UCIs	Number of umbrella funds	as % of total	Number of sub-funds	Average number of sub-funds per umbrella fund	Total number of entities	Net assets of umbrella funds *(in bn EUR)*	as % of total	Net assets per sub-fund *(in bn EUR)*
1997	1,426	711	49.9	3,903	5.49	4,618	296.1	75.6	0.076
1998	1,521	797	52.4	4,454	5.59	5,178	384.3	78.9	0.086
1999	1,630	913	56.0	5,119	5.61	5,836	604.9	82.4	0.118
2000	1,785	1,028	57.6	6,238	6.07	6,995	739.1	84.5	0.118
2001	1,908	1,129	59.2	6,740	5.97	7,519	797.8	85.9	0.118
2002	1,941	1,190	61.3	7,055	5.93	7,806	724.8	85.9	0.103
2003	1,870	1,180	63.1	6,819	5.78	7,509	820.9	86.1	0.120
2004	1,968	1,226	62.3	7,134	5.82	7,876	962.8	87.0	0.135
2005	2,060	1,298	63.0	7,735	5.96	8,497	1,341.4	87.9	0.173
2006	2,238	1,387	62.0	8,622	6.22	9,473	1,639.6	88.9	0.190
2007	2,868	1,688	58.9	9,935	5.89	11,115	1,812.4	88.0	0.182

The development of umbrella funds continued both in number and net assets managed.

As at 31 December 2007, 1,688 UCIs out of 2,868 had adopted an umbrella structure, representing a 21.7% increase as compared to last year. The number of traditionally structured UCIs increased from 851 to 1,180 entities. Moreover, the number of active sub-funds rose from 8,622 to 9,935, which represents a 15.2% growth as compared to 31 December 2006. Like the number of UCIs registered on the official list as at 31 December 2007, the number of active economic entities reached a record high with 11,115 entities at the same date.

The average number of sub-funds per umbrella fund decreased slightly and amounted to 5.89 as at 31 December 2007. However, this figure conceals a wide dispersion between the smallest and largest UCIs.

As at 31 December 2007, umbrella fund net assets totalled EUR 1,812.4 billion, i.e. an increase of 10.5% compared with the previous year-end. Net assets of traditionally structured UCIs recorded a 20.5% increase over the same period.

The average net assets per traditional UCI amounted to EUR 209 million and thereby exceeded the average net assets per sub-fund of umbrella funds (EUR 182 million).

1.4. Valuation currencies used

As regards the valuation currencies used, the proportions in terms of entities remain the same as in 2006. Most entities (7,625 out of a total of 11,115) are denominated in euros, followed by those in US dollars (2,347) and those in Swiss francs (287). In terms of net assets, the entities denominated in euros encompass EUR 1,313.061 billion of a total EUR 2,059.395 billion, ahead of entities expressed in US dollars (EUR 579.186 billion), in Japanese yen (EUR 50.862 billion) and in Swiss francs (EUR 50.029 billion).

1.5. UCIs' investment policy

The table below describes the development in the number of UCIs and net assets according to their investment policy. It should be noted that UCIs investing in other assets notably include UCIs investing in venture capital and UCIs investing in insurance contracts or in debts.

Net assets and entities of UCIs according to their investment policy

	2006		2007		Variation in %	
	Number of entities	Net assets *(in bn EUR)*	Number of entities	Net assets *(in bn EUR)*	Number of entities	Net assets
Fixed-income TS[1]	3,019	743.461	3,189	783.528[2]	5.63%	5.39%
Variable-yield TS	3,183	741.524	3,534	772.522[3]	11.03%	4.18%
Mixed TS	1,437	171.920	2,199	259.692[4]	53.03%	51.05%
Fund of funds	1,543	162.260	1,811	192.455[5]	17.37%	18.61%
Cash	100	7.689	132	15.109	32.00%	96.50%
Real estate	64	8.057	104	15.446	62.50%	91.71%
Futures, options, warrants	111	8.973	124	19.483	11.71%	117.13%
Others	16	0.966	22	1.160[6]	37.50%	20.08%
Total	**9,473**	**1,844.850**	**11,115**	**2,059.395**	**17.33%**	**11.63%**

The following table illustrates, per quarter, the annual flow of subscriptions and redemptions divided into the main investment policies:

1 - Variable-yield transferable securities (equities)
2 - Fixed-income transferable securities (excluding money market instruments and other short-term securities)
3 - Mixed transferable securities
4 - Cash, money market instruments and other short-term securities
5 - Other securities

in million EUR

	1st quarter 2007			2nd quarter 2007			3rd quarter 2007			4th quarter 2007			Totals		
Pol.	subscr.	red.	n. iss.	subscr.	red.	n. iss.	subscr.	red.	n. iss.	subscr.	red.	n. iss.	subscr.	red.	n. iss.
1	120,861	117,738	3,123	127,099	123,653	3,446	119,572	126,882	-7,310	132,051	135,644	-3,593	499,583	503,917	-4,334
2	96,841	84,431	12,410	93,322	77,292	16,030	81,270	99,988	-18,718	72,446	79,869	-7,423	343,879	341,580	2,299
3	45,319	23,680	21,639	38,164	18,971	19,193	42,804	30,114	12,690	50,064	32,743	17,321	176,351	105,508	70,843
4	325,050	306,626	18,424	336,634	326,517	10,117	388,872	372,212	16,660	432,608	427,232	5,376	1,483,164	1,432,587	50,577
5	31,798	21,184	10,614	39,003	23,380	15,623	46,181	26,173	20,008	50,851	27,993	22,858	167,833	98,730	69,103
Total	619,869	553,659	66,210	634,222	569,813	64,409	678,699	655,369	23,330	738,020	703,481	34,539	2,670,810	2,482,322	188,488

In 2007, net issues have experienced a decrease (-21.9%) as compared to net issues in 2006. During the third and fourth quarter 2007, net redemptions have been registered for UCIs investing in variable-yield transferable securities and for UCIs investing in fixed-income transferable securities. In 2007, the most interest was registered for UCIs investing in mixed transferable securities, followed by UCIs investing in other securities.

[1] Transferable securities.
[2] Including EUR 252.380 billion in money market instruments and other short-term securities.
[3] Including EUR 3.303 billion in non-listed securities and EUR 0.355 billion in venture capital.
[4] Including EUR 1.061 billion in non-listed securities and EUR 0.303 billion in venture capital.
[5] Including EUR 0.031 billion in non-listed securities.
[6] Including EUR 0.059 billion in venture capital.

UCIs' investment policy

Situation as at 31 December 2007	**Number of entities**	**Net assets** *(in bn EUR)*	**Net assets** *(in %)*
UCITS subject to Part I			
Fixed-income transferable securities[7]	2,450	677.030	32.9
Variable-yield transferable securities	3,097	713.040	34.6
Mixed transferable securities	1,490	208.488	10.1
Fund of funds	550	37.463	1.8
Cash	19	2.991	0.1
Futures and/or options	36	7.329	0.4
UCITS subject to Part II[8]			
Fixed-income transferable securities[9]	410	76.029	3.7
Variable-yield transferable securities	220	34.227	1.7
Mixed transferable securities	369	27.199	1.3
Fund of funds	923	127.140	6.2
Cash	100	12.056	0.6
UCITS subject to Part II[10]			
Non-listed transferable securities	24	2.704	0.1
Venture capital	11	0.415	0.0
Other UCIs subject to Part II			
Real estate	21	7.315	0.4
Futures, options, warrants	72	8.433	0.4
Other securities	6	0.421	0.0
Specialised investment funds			
Fixed-income transferable securities[11]	329	30.468	1.5
Variable-yield transferable securities	175	21.597	1.0
Mixed transferable securities	316	22.641	1.1
Non-listed transferable securities	22	1.691	0.1
Fund of funds	337	27.822	1.4
Cash	13	0.062	0.0
Venture capital	11	0.302	0.0
Real estate	83	8.131	0.4
Futures and/or options	16	3.721	0.2
Other securities	15	0.680	0.0
Total	**11,115**	**2,059.395**	**100.0**

[7] Including EUR 208.844 billion in money market instruments and other short-term securities (276 entities).

[8] UCITS excluded from Part I of the law of 20 December 2002, as amended, pursuant to article 3, points 1 to 3, i.e. closed-ended UCITS, not promoted in the EU or only sold to individuals in third-party countries outside the EU.

[9] Including EUR 38.432 billion in money market instruments and other short-term securities (117 entities).

[10] UCITS excluded from Part I of the law of 20 December 2002, as amended, pursuant to article 3, point 4, i.e. UCITS under one of the categories laid down by circular CSSF 03/88 owing to their investment and loan policy.

[11] Including EUR 5.104 billion in money market instruments and other short-term securities (11 entities).

1.6. Development in guarantee-type UCIs

Given the fluctuations inherent in financial markets, guarantee-type UCIs aim to offer investors greater security than that offered by traditional collective management products. According to the investment policy pursued by the funds concerned, the guarantee ensures that the subscriber is reimbursed either a proportion of the capital invested or is fully reimbursed his initial investment or even receives a return on his investment at the end of one or several pre-determined periods.

In 2007, the number of guarantee-type UCIs rose from 121 to 154 and the number of entities from 297 to 360. In terms of entities, the rise is attributable to the launch of 103 new entities, while the guarantee given came to maturity or has not been extended for 40 entities.

As at 31 December 2007, these 360 entities comprised 35 entities guaranteeing investors only a proportion of the invested capital, 142 entities guaranteeing repayment in full of the invested capital (money-back guarantee) and 183 entities offering their investors a surplus as compared to the initial subscription price.

UCIs offering their investors a surplus compared to their initial investment remain thus dominant. These funds generally track a stock market index and, through the use of derivatives, enable investors to participate to some extent in the growth of this index.

Net assets of guarantee-type UCIs increased by EUR 11.17 billion to EUR 43.73 billion in 2007, i.e. an increase of 34.3%. It is also worth noting that guarantee-type UCIs created by German promoters alone accounted for 85.6% of the total net assets of guarantee-type UCIs.

Development in guarantee-type UCIs

	Number of UCIs	Number of economic entities	Net assets *(in bn EUR)*
1997	70	90	11.47
1998	86	99	15.00
1999	85	116	17.13
2000	79	119	14.30
2001	74	115	17.09
2002	75	151	17.40
2003	76	166	20.89
2004	90	207	21.41
2005	104	248	24.69
2006	121	297	32.56
2007	154	360	43.73

1.7. Promoters of Luxembourg UCIs

The breakdown of Luxembourg UCIs according to geographic origin of their promoters highlights the multitude of countries represented in the financial centre. Promoters of Luxembourg UCIs spread over 42 countries.

The main countries actively promoting UCIs in Luxembourg are Germany, Switzerland, Belgium, France, the United States, Great Britain and Italy.

Origin of promoters of Luxembourg UCIs

Situation as at 31 December 2007	**Net assets** *(in bn EUR)*	**in %**	**Number of UCIs**	**in %**	**Number of entities**	**in %**
United States	391.278	19.0%	129	4.5%	940	8.5%
Germany	391.051	19.0%	1,344	46.8%	2,367	21.3%
Switzerland	364.938	17.7%	340	11.9%	1,982	17.8%
Great Britain	218.278	10.6%	163	5.7%	856	7.7%
Italy	186.779	9.1%	92	3.2%	809	7.3%
Belgium	171.876	8.4%	157	5.5%	1,556	14.0%
France	141.569	6.9%	203	7.1%	965	8.7%
Netherlands	66.842	3.2%	56	2.0%	350	3.1%
Sweden	30.439	1.5%	78	2.7%	225	2.0%
Luxembourg	25.658	1.2%	73	2.5%	259	2.3%
Others	70.687	3.4%	233	8.1%	806	7.3%
Total	**2,059.395**	**100.0%**	**2,868**	**100.0%**	**11,115**	**100.0%**

1.8. Marketing of Luxembourg UCIs and marketing of foreign UCIs in Luxembourg

Luxembourg UCITS seeking to market their units/shares in another Member State of the European Union must comply with the notification procedure in accordance with the CESR guidelines (Committee of European Securities Regulators) to simplify the notification procedure of UCITS published on 29 June 2006 (document CESR/06-120b). This new procedure has been transposed by circular CSSF 07/277.

Moreover, the CSSF recommends UCITS to refer to the websites of the host supervisory authorities for additional information relating to the applicable notification letter and the national marketing rules or other specific regulations to comply with in the host countries. Where no specific indications are given by the host supervisory authority in this respect, the Luxembourg-based UCITS seeking to market their units/shares in another EU Member State must use the standard notification letter according to annexe II of the CESR document, a copy of which may be downloaded from the CSSF website.

In the context of the new notification procedure, the CSSF sent 2,860 certification letters, as provided for in annexe I of the CESR document, to 1,362 different UCITS. Indeed, in addition to the new establishments of UCITS, UCITS structures are regularly adapted and amended.

As regards foreign UCITS marketed in Luxembourg at the end of 2007, 202 foreign UCITS took advantage of the marketing facilities provided for by the Directive to offer their units/shares in Luxembourg.

Moreover, 14 non-coordinated foreign UCIs (eight of German origin and six of Swiss origin) were authorised to market their units/shares in Luxembourg at the end of 2007.

Marketing of foreign UCIs in Luxembourg

	2004	2005	2006	2007
EU UCITS				
Country of origin				
Germany	69	63	67	60
France	27	28	35	44
Ireland	31	33	41	42
Sweden	0	0	5	19
Belgium	10	11	13	14
Great Britain	6	6	7	9
Norway	0	0	6	6
Finland	0	0	4	5
Denmark	0	0	0	1
Sub-total	**143**	**141**	**178**	**202**
Other foreign UCIs				
Country of origin				
Germany	9	9	8	8
Switzerland	9	6	6	6
Belgium	1	0	0	0
Sub-total	**19**	**15**	**14**	**14**
Total	**162**	**156**	**192**	**217**

2. NEWLY CREATED ENTITIES APPROVED IN 2007

2.1. General data

2,878 new entities[12] were approved in 2007, representing 759 entities more than in 2006 and 1,072 entities more than in 2005. In relative terms, this corresponds to an increase of 35.8% as compared to 2006 and 59.4% as compared to 2005.

59% of the newly approved entities are UCIs set up under Part I of the law of 20 December 2002, 26% are specialised investment funds (SIFs) and 15% UCIs under Part II of the law.

	2003	2004	2005	2006	2007
Newly approved entities	1,086	1,434	1,806	2,119	2,878
of which: launched in the same year	*637*	*961*	*1,022*	*1,263*	*1,916*
In %	58.7%	67.0%	56.6%	59.6%	66.6%

1,916 out of the 2,878 newly approved entities, representing 66.6%, have been launched in the same year. Given that the lapse between the authorisation of a new entity and its effective launch can be explained, *inter alia*, by the period of time promoters have to wait between the notification to the host country's authority pursuant to European regulations and the effective marketing of units/shares in the host country, a high number of approved entities is expected to be launched in the first months of 2008.

[12] The term "entity" refers both to traditional UCIs and to sub-funds of umbrella funds. The number of new "entities" therefore means, from an economic point of view, the number of economic vehicles created.

2.2. Analysis of the investment policy of new entities

The share of entities having opted for investment in mixed transferable securities increased by 10.4% and shows a positive trend of 1,004 entities in 2007. More than one third of the newly approved entities in 2007 are thus UCIs investing in mixed transferable securities.

The share of entities having opted for investment in variable-yield transferable securities increased by 2.9%, i.e. +804 entities as compared to 2006. Similarly, the share of entities investing in other UCIs registered a 1.4% increase (+496 entities as compared to 2006).

Although the number of newly approved entities intending to invest in fixed-income transferable securities rose by 420 entities in 2007, this type of UCIs registered, in relative terms, a substantial downturn of 12.1% as compared to 2006.

The number of entities whose investment policy provides for investment in cash, money market instruments and other short-term securities remained more or less stable as compared to 2006.

The number of entities investing in derivative instruments, which recorded a strong growth in 2006, suffered a substantial decrease. Their share does not exceed 1% of the newly approved entities in 2007.

Investment policy	2006		2007	
	Number of entities	As a % of total	Number of entities	As a % of total
Fixed-income transferable securities (excluding money market instruments and other short-term securities)	566	26.71%	420	14.59%
Variable-yield transferable securities	530	25.01%	804	27.94%
Mixed transferable securities	518	24.45%	1,004	34.89%
Fund of funds	335	15.81%	496	17.23%
Cash, money market instruments and other short-term securities	58	2.74%	69	2.40%
Futures, options, warrants	82	3.87%	26	0.90%
Others	30	1.42%	59	2.05%
Total	**2,119**	**100.00%**	**2,878**	**100.00%**

3. CLOSED DOWN ENTITIES IN 2007

3.1. General data

The number of entities closed down in 2007 increased as compared to the previous year (+109 entities or +16%). The number of liquidated entities, matured entities and merged entities grew by 2.9%, 84.4% and 26.5% respectively, as compared to 2006.

	2001	2002	2003	2004	2005	2006	2007
Liquidated entities	367	490	643	393	426	412	424
Matured entities	53	49	47	64	70	45	83
Merged entities	337	326	488	237	202	223	282
Total	**757**	**865**	**1,178**	**694**	**698**	**680**	**789**

3.2. Investment policy of the closed down entities

The distribution by investment policy of the entities closed down in 2007 shows that the share of "fund of funds" entities significantly increased as compared to 2006. Most of the closed down entities had invested in fixed-income transferable securities or in variable-income transferable securities.

Among the 241 closed down entities whose investment policy provided for investment in fixed-income transferable securities, 119 were liquidated, 72 merged and 50 matured. As regards the category of entities investing in variable-yield transferable securities, 119 entities were liquidated, 117 merged and 5 matured.

Investment policy	2006		2007	
	Number of entities	As a % of total	Number of entities	As a % of total
Fixed-income transferable securities (excluding money market instruments and other short-term securities)	206	30.29%	241	30.55%
Variable-yield transferable securities	250	36.76%	241	30.55%
Mixed transferable securities	104	15.29%	110	13.94%
Fund of funds	71	10.44%	136	17.24%
Cash, money market instruments and other short-term securities	44	6.47%	39	4.94%
Derivative instruments	5	0.74%	21	2.66%
Real estate	0	0.00%	1	0.12%
Total	**680**	**100.00%**	**789**	**100.00%**

4. SPECIALISED INVESTMENT FUNDS (SIFS)

4.1. Law of 13 February 2007 on specialised investment funds

The law of 13 February 2007 on specialised investment funds introduced a new type of UCI intended for investors that are better informed than those of UCIs subject to the law of 20 December 2002 on undertakings for collective investment.

The law indeed aims at extending the concept of eligible investors in order to include, in addition to institutional investors, professional investors and other well-informed investors in accordance with the criteria set out in further detail in article 2 of that law. The law on specialised investment funds thus represents an autonomous legal framework designed to regulate a type of investment fund reserved for sophisticated clients, which do not require the same level of protection, nor the same risk diversification rules as those foreseen for UCIs subject to the law of 20 December 2002.

Moreover, the object of the law of 13 February 2007 was to replace the former law of 19 July 1991 relating to undertakings for collective investment the securities of which are not intended to be placed with the public. This law was repealed on 13 February 2007 as a consequence of the expiry of the law of 30 March 1988 relating to undertakings for collective investment, on which the law of 1991 was based in relation to the rules applicable to the operation and supervision of UCIs set up under this regime.

4.2. Development of specialised investment funds in 2007

The demand by better informed clients to invest in a more flexible investment vehicle resulted in an increase in the number of specialised investment funds, which amounted to 572 funds as at 31 December 2007 against 217 funds as at 31 December 2006, representing an increase of 355 funds.

In terms of assets under management, specialised investment funds collected EUR 38.75 billion in 2007 to reach a total of EUR 117.1 billion in assets under management as at 31 December 2007, against EUR 78.4 billion as at 31 December 2006, i.e. an increase by 49.39%. In terms of assets, specialised investment funds represented 5.7% of the total UCI assets (EUR 2,059.4 billion as at 31 December 2007). The share of specialised investment funds thus only increased by 1.7% as compared to 2006 despite the important growth in number of this type of funds.

4.3. Identification of well-informed investors within the meaning of article 2(1) of the law of 13 February 2007

The CSSF considers that specialised investment funds are responsible for ensuring that investors are effectively investors within the meaning of the law of 13 February 2007 and that they must set up procedures to ensure that the final investors of specialised investment funds comply with the requirements of article 2 of that law.

4.4. Central administration of specialised investment funds

As per the law 13 February 2007, the central administration of a specialised investment fund must be located in Luxembourg. The professionals providing central administration services to specialised investment funds must comply with the same requirements as those applicable to UCI central administration.

5. UCIS INVESTING PRINCIPALLY IN REAL ESTATE ASSETS

The interest of promoters in creating Luxembourg UCIs whose main object is to invest in the real estate sector did not decrease in 2007. The statistical data shows that this trend, which began in 2004, intensified last year. In 2007, net assets of UCIs investing mainly in real estate assets thus increased by more than 90%.

Development of UCIs investing mainly in real estate assets

	Number of real estate UCIs	of which active entities	of which Part II	of which SIFs	**Net issues** *(in bn EUR)*	**Net assets** *(in bn EUR)*
2003	14	13	6	8	0.322	2.865
2004	23	22	7	16	0.173	3.130
2005	52	41	16	36	1.591	5.287
2006	76	64	22	54	2.653	8.057
2007	104	80	21	83	6.497	15.446

As for the creation of new UCIs investing mainly in real estate assets, it is interesting to note that in 2007 promoters chose almost exclusively to subject UCIs to the requirements of the law of 13 February 2007, rather than to the provisions of Part II of the law of 20 December 2002. One reason is the greater flexibility offered in terms of investment policy. Consequently, at the end of 2007, 80% of real estate UCIs were specialised investment funds.

Net assets of UCIs investing mainly in real estate assets and subject to the provisions of the law of 13 February 2007 increased considerably in 2007, growing from EUR 3.307 billion to EUR 8.131 billion, representing a 145% increase.

Net assets of UCIs investing mainly in real estate assets and subject to the provisions of Part II of the law of 20 December 2002 increased from EUR 4.750 billion to EUR 7.315 billion, representing a growth of 54%, despite the fact that the number of entities remained stable.

6. PERFORMANCE ANALYSIS OF THE MAJOR LUXEMBOURG UCI CATEGORIES IN 2007

6.1. Objectives and methodology

The objective of this section is to analyse the performance distribution of several Luxembourg UCI categories in relation to their investment policy.

The UCI categories selected are the following:

Monetary UCIs	Bond UCIs	Equity UCIs
EURO	Europe	Europe
	Global	Global
	Emerging markets	Emerging markets

The category "European equity" only takes into account entities investing in standard European equity. Entities investing in Midcap and Smallcap shares have not been considered.

The category "European bonds" only takes into account entities investing in standard European bonds. Entities investing in High Yield bonds have not been considered.

For the analysis of the results, it is important to highlight that past performances do not presume future performances.

Methodological aspects:

- Base currency: to measure the performance of the various UCI categories, the Euro has been used as base currency.
- Population considered: the population considered is composed of a total of EUR 489.241 billion net assets and 1,463 entities. The entities with no performance in all 12 months of 2007 have not been taken into consideration.
- The average return and the average standard deviation per UCI category have been calculated with the weighting of the entities' average net assets.
- To compare the performances of the various investment policies, a risk-performance indicator is applied, i.e. the Sharpe ratio.

The Sharpe ratio was developed by William Sharpe, Nobel Laureate in Economics in 1990. The Sharpe ratio divides the difference between the return of a securities portfolio and a risk-free rate, i.e. a fixed-rate investment, by the portfolio standard deviation. It measures in this manner the excess return, realised per risk unit considered. The Sharpe ratio is calculated as follows:

$$\text{Sharpe ratio} = \frac{\text{Portfolio return} - \text{Risk-free rate}}{\text{Portfolio standard deviation}}$$

The 12-month money market rate applicable beginning of January 2007, i.e. 4.005%, has been used as risk-free rate.

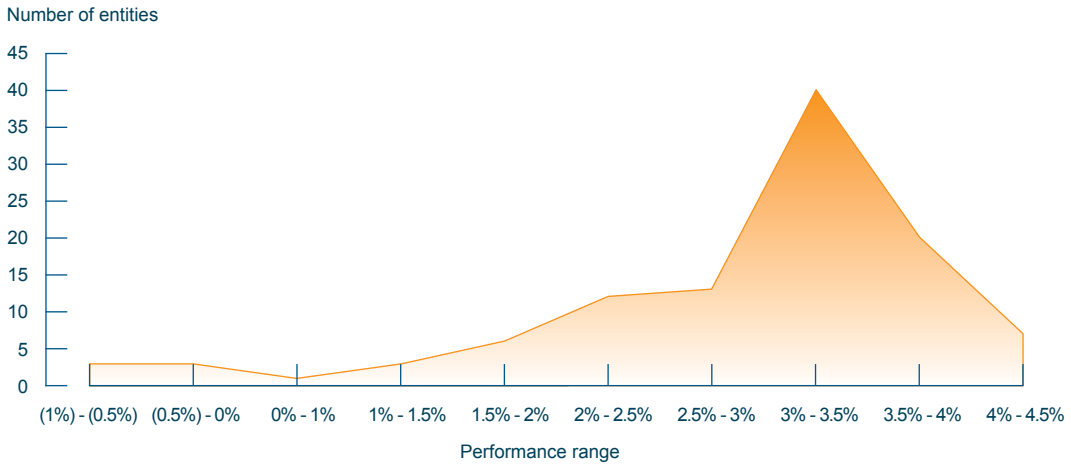
- For the maximum performance calculation of a UCI category, the average of the highest performance classes has been used and for the minimum performance calculation of a UCI category, the average of the lowest performance classes has been considered.
- Source of UCI data: CSSF database.
- For entities investing in equity, MSCI indices are used as benchmark.
- For entities investing in bonds, Lehman Brothers indices are used as benchmark.
- For the categories "international bonds" and "emerging market bonds", hedged indices are used in order to exclude the influence of currency movements on the performance of the benchmark.
- The term "entity" refers both to traditional UCIs and to sub-funds of umbrella funds.

6.2. Performance of the major Luxembourg UCI categories in 2007

6.2.1. Entities whose investment policy consists in investing in Euro money market instruments

The following graph illustrates the performance distribution of entities whose investment policy consists in investing in Euro money market instruments.

Performance of entities investing in Euro money market instruments in 2007



The average performance realised in 2007 by entities whose investment policy consists in investing in Euro money market instruments is of 3.15%. The average performance of the maximum return class amounts to 4.34% whereas the average performance of the minimum return class is of -0.77%. The standard deviation of the performance of these entities amounts to 1.25%.

Central values and dispersion characteristics

Average performance of the whole population	3.15%
Average performance of maximum return class	4.34%
Average performance of minimum return class	-0.77%
Standard deviation of performance	1.25%
Performance spread	5.11%
Statistical population	108

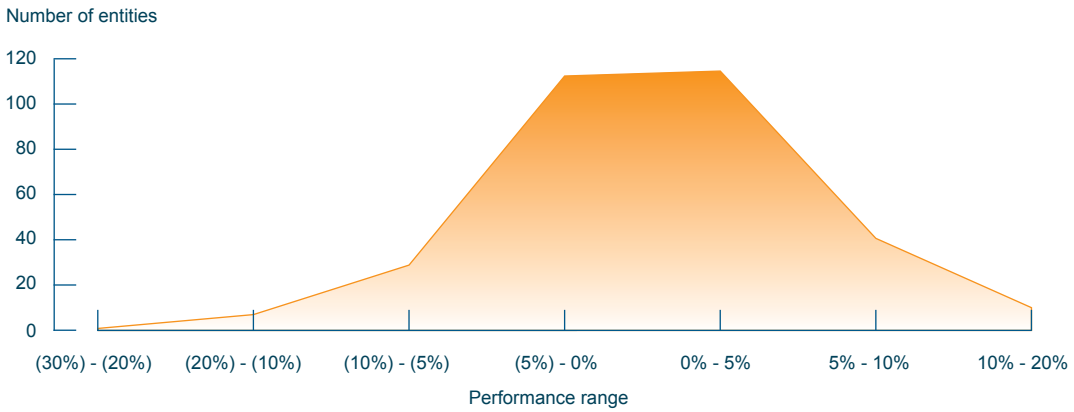
Statistical performance distribution of entities investing in money market instruments

Performance	Number of entities			
Return classes	Absolute frequency	Relative frequency	Cumulative absolute frequency	Cumulative relative frequency
-1% to -0.5%	3	2.78%	3	2.78%
-0.5% to 0%	3	2.78%	6	5.56%
0% to 1%	1	0.93%	7	6.48%
1% to 1.5%	3	2.78%	10	9.26%
1.5% to 2%	6	5.56%	16	14.81%
2% to 2.5%	12	11.11%	28	25.93%
2.5% to 3%	13	12.04%	41	37.96%
3% to 3.5%	40	37.04%	81	75.00%
3.5% to 4%	20	18.52%	101	93.52%
4% to 4.5%	7	6.48%	108	100.00%
Total	**108**	**100.00%**		

6.2.2. Entities whose investment policy consists in investing in European equity

The following graph illustrates the performance distribution of entities whose investment policy consists in investing in European equity. It should be noted that entities investing in European Smallcap and Midcap shares are not included in this category.

Performance of entities investing in European equity in 2007



The average performance realised in 2007 by entities whose investment policy consists in investing in European equity is of 0.11%. The average performance of the maximum return class amounts to 15.69% whereas the average performance of the minimum return class is of -18.92%. The standard deviation of the performance of these entities amounts to 5.25%.

Central values and dispersion characteristics

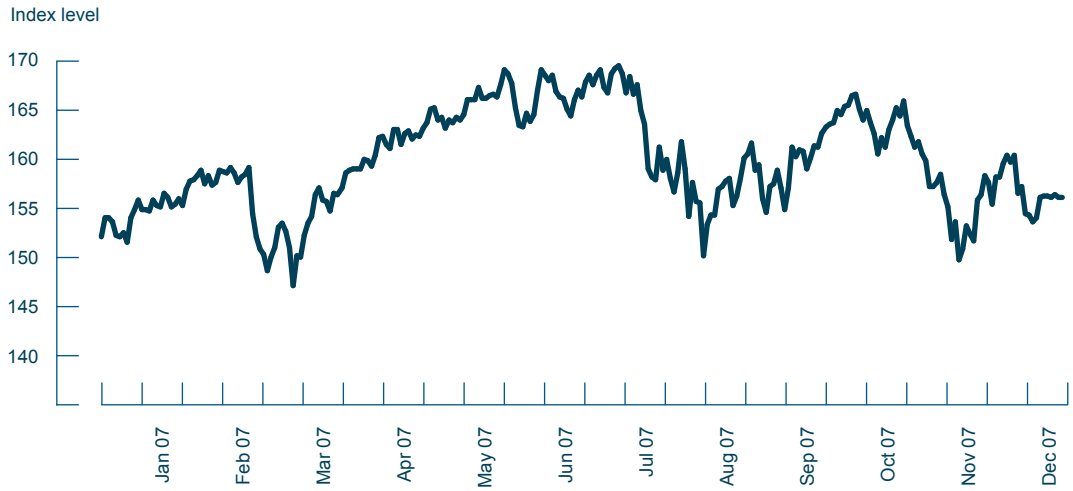
Average performance of the whole population	0.11%
Average performance of maximum return class	15.69%
Average performance of minimum return class	-18.92%
Standard deviation of performance	5.25%
Performance spread	34.61%
Statistical population	316

Statistical performance distribution of entities investing in European equity

Performance	Number of entities			
Return classes	Absolute frequency	Relative frequency	Cumulative absolute frequency	Cumulative relative frequency
-30% to -20%	1	0.32%	1	0.32%
-20% to -10%	7	2.22%	8	2.53%
-10% to -5%	29	9.18%	37	11.71%
-5% to 0%	113	35.76%	150	47.47%
0% to 5%	115	36.39%	265	83.86%
5% to 10%	41	12.97%	306	96.84%
10% to 20%	10	3.16%	316	100.00%
Total	**316**	**100.00%**		

The MSCI Europe Net Index (EUR), which includes dividends, realised a performance of 2.69% in 2007. 92 entities investing in European equity, i.e. 29.11% of all entities, have realised a higher performance than the MSCI Europe Net Index (EUR). The market volatility for European equity is of 15.85% (source: MSCI Barra, CSSF calculation).

MSCI Europe Net Index (EUR) 2007



Source: MSCI Barra[13]

Interpretation of the Sharpe ratio:

The population of UCI entities investing in European equity realised in 2007 on average a negative return of -0.38% per risk entity considered. For the performance of the maximum return class, a positive return of 1.28% on average could be observed per risk entity. For the performance of the minimum return class, a negative return of -1.51% on average could be observed per risk entity considered.

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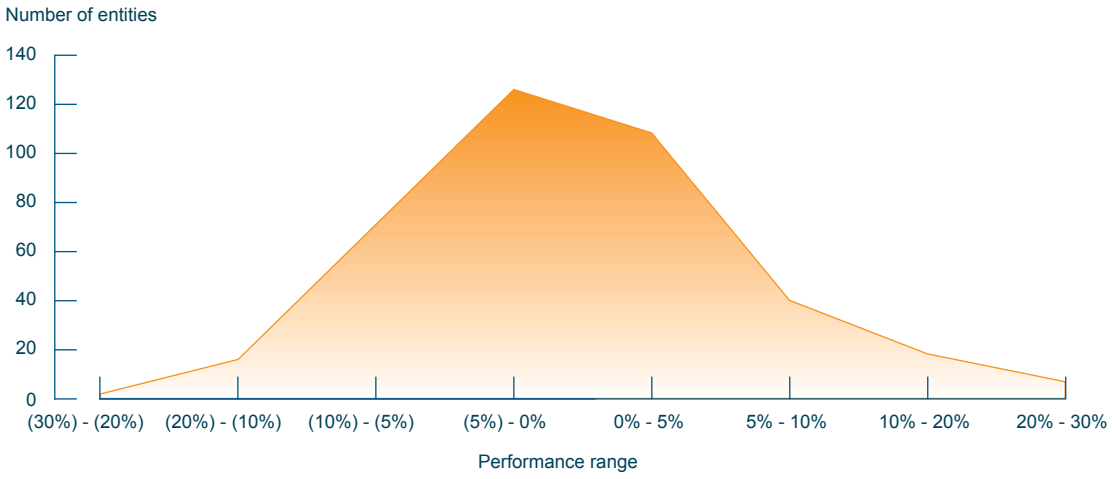
Summary table of the category of entities investing in European equity

Average performance of the whole population	0.11%
Average performance of maximum return class	15.69%
Average performance of minimum return class	-18.92%
Standard deviation of performance	5.25%
Performance spread	34.61%
Statistical population	316
MSCI Europe Net Index (EUR) performance	2.69%
Market volatility	15.85%
Number of entities with higher performance than MSCI Europe Net Index (EUR)	92
Sharpe ratio – average performance	-0.38
Sharpe ratio – maximum return class	1.28
Sharpe ratio – minimum return class	-1.51

6.2.3. Entities whose investment policy consists in investing in international equity

The following graph illustrates the performance distribution of entities whose investment policy consists in investing in international equity.

Performance of entities investing in international equity in 2007



The average performance realised in 2007 by entities whose investment policy consists in investing in international equity is of -1.21%. The average performance of the maximum return class amounts to 26.82% whereas the average performance of the minimum return class is of -23.68%. The standard deviation of the performance of these UCIs amounts to 6.95%.

Central values and dispersion characteristics

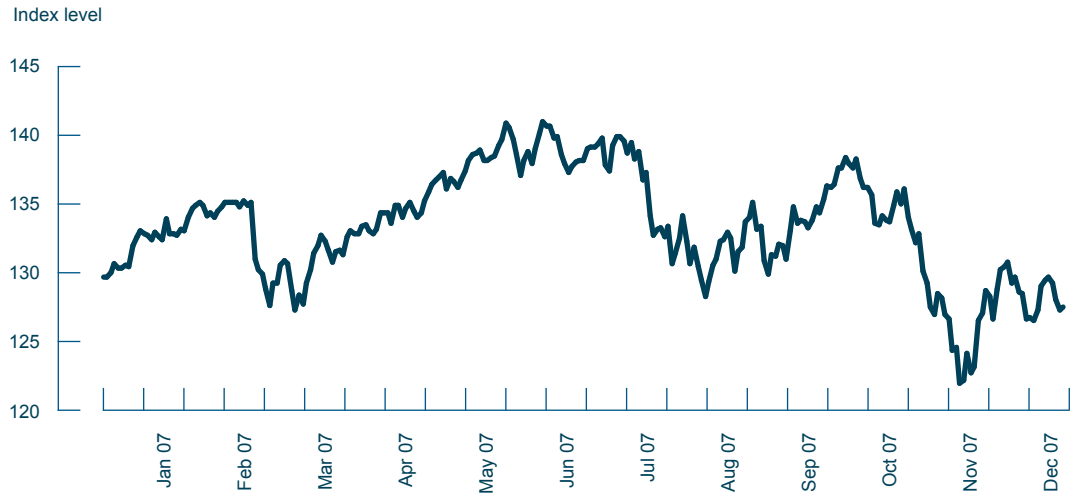
Average performance of the whole population	-1.21%
Average performance of maximum return class	26.82%
Average performance of minimum return class	-23.68%
Standard deviation of performance	6.95%
Performance spread	50.50%
Statistical population	388

Statistical performance distribution of entities investing in international equity

Performance	**Number of entities**			
Return classes	Absolute frequency	Relative frequency	Cumulative absolute frequency	Cumulative relative frequency
-30% to -20%	2	0.52%	2	0.52%
-20% to -10%	16	4.12%	18	4.64%
-10% to -5%	71	18.30%	89	22.94%
-5% to 0%	126	32.47%	215	55.41%
0% to 5%	108	27.84%	323	83.25%
5% to 10%	40	10.31%	363	93.56%
10% to 20%	18	4.64%	381	98.20%
20% to 30%	7	1.80%	388	100.00%
Total	**388**	**100.00%**		

The MSCI World Index Net (EUR), which includes dividends, realised a performance of -1.66% in 2007. 220 entities investing in international equity, i.e. 56.70% of all entities, have realised a higher performance than the MSCI World Index Net (EUR). The market volatility for international equity is of 12.54% (source: MSCI Barra, CSSF calculation).

MSCI World Index Net (EUR) 2007



Source: MSCI Barra

Interpretation of the Sharpe ratio:

The population of UCI entities investing in international equity realised in 2007 on average a negative return of -0.57% per risk entity considered. For the performance of the maximum return class, a positive return of 1.39% on average could be observed per risk entity. For the performance of the minimum return class, a negative return of -1.90% on average could be observed per risk entity considered.

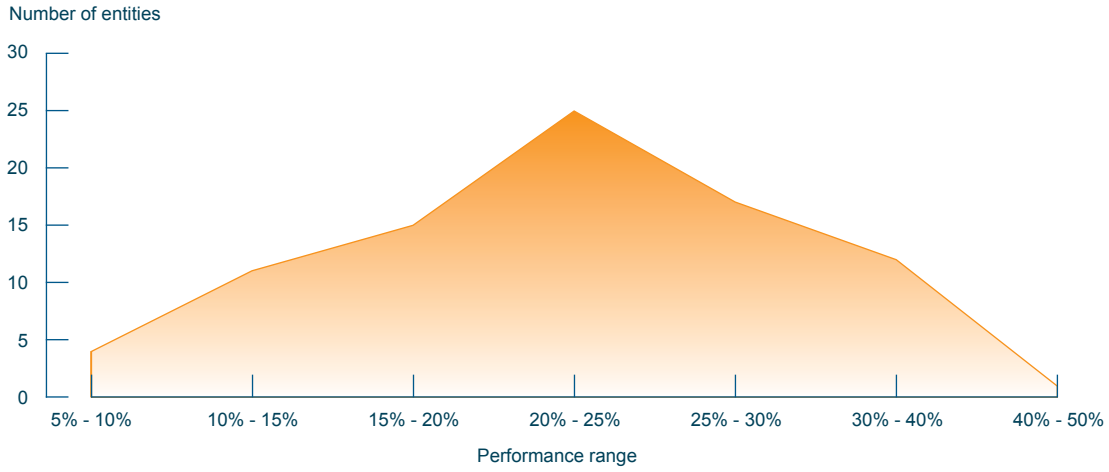
Summary table of the category of entities investing in international equity

Average performance of the whole population	-1.21%
Average performance of maximum return class	26.82%
Average performance of minimum return class	-23.68%
Standard deviation of performance	6.95%
Performance spread	50.50%
Statistical population	388
MSCI World Index Net (EUR) performance	-1.66%
Market volatility	12.54%
Number of entities with higher performance than MSCI World Index Net (EUR)	220
Sharpe ratio – average performance	-0.57
Sharpe ratio – maximum return class	1.39
Sharpe ratio – minimum return class	-1.90

6.2.4. Entities whose investment policy consists in investing in emerging market equity

The following graph illustrates the performance distribution of entities whose investment policy consists in investing in emerging market equity.

Performance of entities investing in emerging market equity in 2007



The average performance realised in 2007 by entities whose investment policy consists in investing in emerging market equity is of 25.37%. The average performance of the maximum return class amounts to 40.92% whereas the average performance of the minimum return class is of 8.27%. The standard deviation of the performance of these entities amounts to 7.43%.

Central values and dispersion characteristics

Average performance of all population	25.37%
Performance of maximum return class	40.92%
Performance of minimum return class	8.27%
Standard deviation of performance	7.43%
Performance spread	32.65%
Statistical population	85

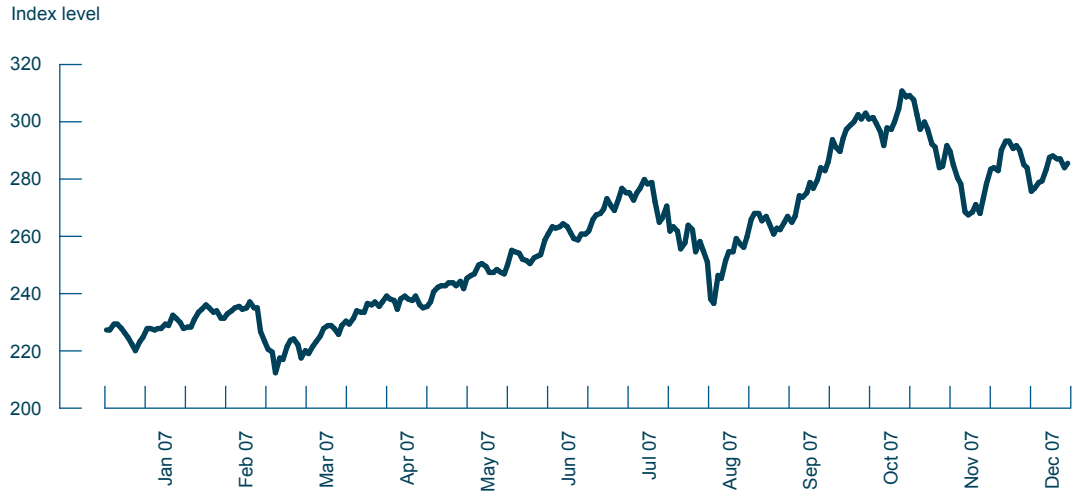
Statistical performance distribution of entities investing in emerging market equity

Performance	**Number of entities**			
Return classes	Absolute frequency	Relative frequency	Cumulative absolute frequency	Cumulative relative frequency
5% to 10%	4	4.71%	4	4.71%
10% to 15%	11	12.94%	15	17.65%
15% to 20%	15	17.65%	30	35.29%
20% to 25%	25	29.41%	55	64.71%
25% to 30%	17	20.00%	72	84.71%
30% to 40%	12	14.12%	84	98.82%
40% to 50%	1	1.18%	85	100.00%
Total	**85**	**100.00%**		

It should be noted that entities investing in BRIC countries (Brazil, Russia, India and China) are included in this category and have realised the highest performance of entities investing in emerging markets in 2007.

The MSCI Emerging Markets Net Index (EUR), which includes dividends, realised a performance of 25.72% in 2007. 30 entities investing in emerging market equity, i.e. 35.29% of all entities, have realised a higher performance than the MSCI Emerging Markets Net Index (EUR). The market volatility for emerging market equity is of 19.58% (source: MSCI Barra, CSSF calculation).

MSCI Emerging Markets Net Index (EUR) 2007



Source: MSCI Barra

Interpretation of the Sharpe ratio:

The population of UCI entities investing in emerging market equity realised in 2007 on average a positive return of 1.22% per risk entity considered. For the performance of the maximum return class, a positive return of 1.64% on average could be observed per risk entity. For the performance of the minimum return class, a positive return of 0.30% on average could be observed per risk entity considered.

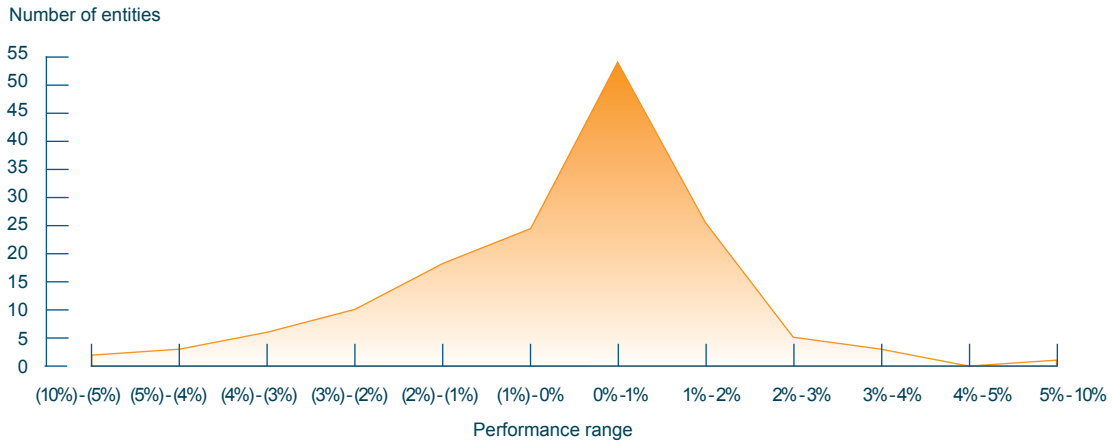
Summary table of the category of entities investing in emerging market equity

Average performance of the whole population	25.37%
Performance of maximum return class	40.92%
Performance of minimum return class	8.27%
Standard deviation of performance	7.43%
Performance spread	32.65%
Statistical population	85
MSCI Emerging Markets Net Index (EUR) performance	25.72%
Market volatility	19.58%
Number of entities with higher performance than MSCI Emerging Markets Net Index (EUR)	30
Sharpe ratio – average performance	1.22
Sharpe ratio – maximum return class	1.64
Sharpe ratio – minimum return class	0.30

6.2.5. Entities whose investment policy consists in investing in EUR-denominated bonds

The following graph illustrates the performance distribution of entities whose investment policy consists in investing in EUR-denominated bonds. It should be noted that entities investing in High Yield bonds are not included in this category.

Performance of entities investing in EUR-denominated bonds in 2007



The average performance realised in 2007 by entities whose investment policy consists in investing in EUR-denominated bonds is of 0.13%. The average performance of the maximum return class amounts to 4.05% whereas the average performance of the minimum return class is of -7.76%. The standard deviation of the performance of these entities amounts to 1.94%.

Central values and dispersion characteristics

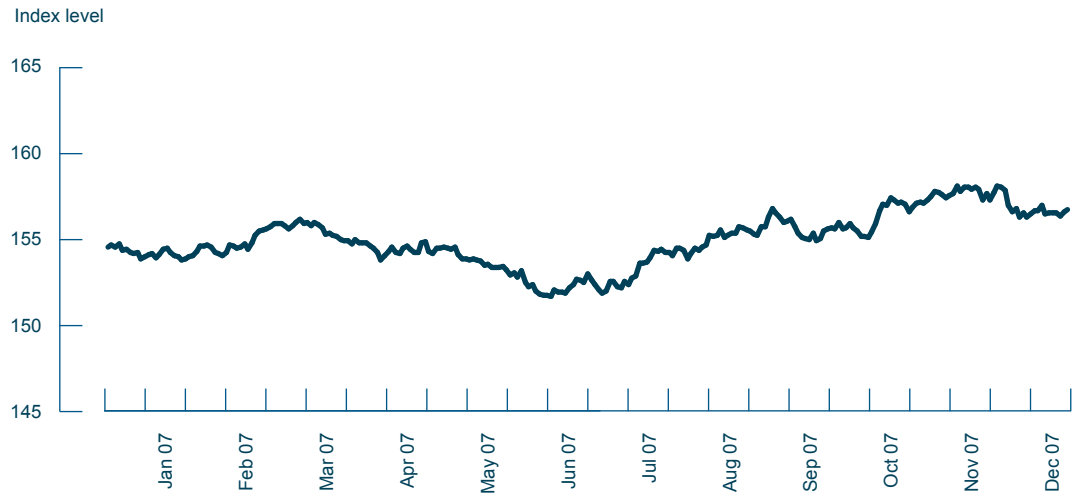
Average performance of the whole population	0.13%
Performance of maximum return class	4.05%
Performance of minimum return class	-7.76%
Standard deviation of performance	1.94%
Performance spread	11.81%
Statistical population	150

Statistical performance distribution of entities investing in EUR-denominated bonds

Performance	**Number of entities**			
Return classes	Absolute frequency	Relative frequency	Cumulative absolute frequency	Cumulative relative frequency
-10% to -5%	2	1.33%	2	1.33%
-5% to -4%	3	2.00%	5	3.33%
-4% to -3%	6	4.00%	11	7.33%
-3% to -2%	10	6.67%	21	14.00%
-2% to -1%	18	12.00%	39	26.00%
-1% to 0%	24	16.00%	63	42.00%
0% to 1%	53	35.33%	116	77.33%
1% to 2%	25	16.67%	141	94.00%
2% to 3%	5	3.33%	146	97.33%
3% to 4%	3	2.00%	149	99.33%
4% to 5%	0	0.00%	149	99.33%
5% to 10%	1	0.67%	150	100.00%
Total	**150**	**100.00%**		

The Lehman Brothers Euro-Aggregate - Index Level, EUR, Unhedged realised a performance of 1.45% in 2007. 18 entities investing in European bonds, i.e. 12% of all entities, have realised a higher performance than the Lehman Brothers Euro-Aggregate - Index Level, EUR, Unhedged. The market volatility for European bonds is of 2.71% in 2007 (source: Lehman Brothers, CSSF calculation).

Lehman Brothers Euro-Aggregate - Index Level, EUR, Unhedged, 2007



Source: Lehman Brothers

Interpretation of the Sharpe ratio:

UCIs investing in EUR-denominated bonds realised in 2007 on average a negative return of -1.59% per risk entity considered. For the performance of the maximum return class, a slightly positive return of 0.03% on average could be observed per risk entity. For the performance of the minimum return class, a negative return of -2.04% on average could be observed per risk entity considered.

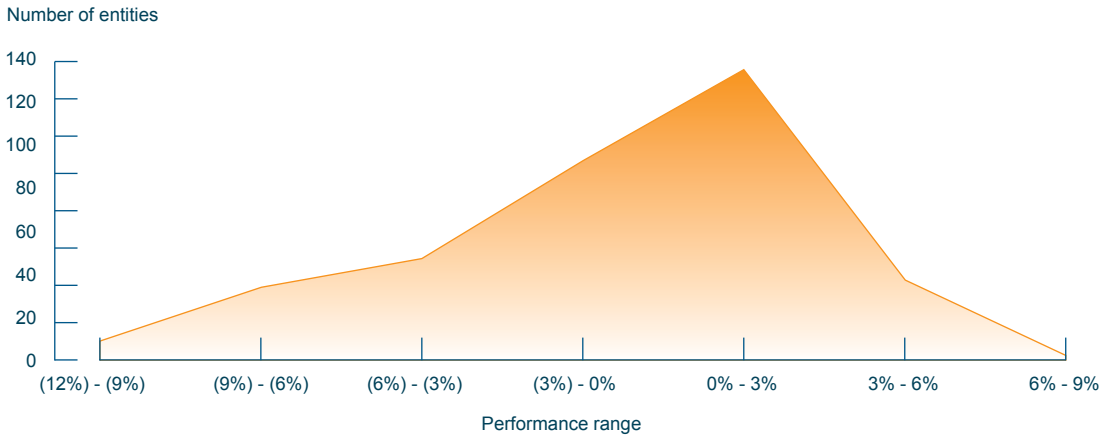
Summary table of the category of entities investing in EUR-denominated bonds

Average performance of the whole population	0.13%
Performance of maximum return class	4.05%
Performance of minimum return class	-7.76%
Standard deviation of performance	1.94%
Performance spread	11.81%
Statistical population	150
Lehman Brothers Euro-Aggregate - Index Level, EUR, Unhedged performance	1.45%
Market volatility	2.71%
Number of entities with higher performance than Lehman Brothers Euro-Aggregate - Index Level, EUR, Unhedged	18
Sharpe ratio – average performance	-1.59
Sharpe ratio – maximum return class	0.03
Sharpe ratio – minimum return class	-2.04

6.2.6. Entities whose investment policy consists in investing in international bonds

The following graph illustrates the performance distribution of entities whose investment policy consists in investing in international bonds.

Performance of entities investing in international bonds in 2007



The average performance realised in 2007 by entities whose investment policy consists in investing in international bonds is of 1.83%. The average performance of the maximum return class amounts to 6.17% whereas the average performance of the minimum return class is of -10.35%. The standard deviation of the performance of these entities amounts to 1.95%.

Central values and dispersion characteristics

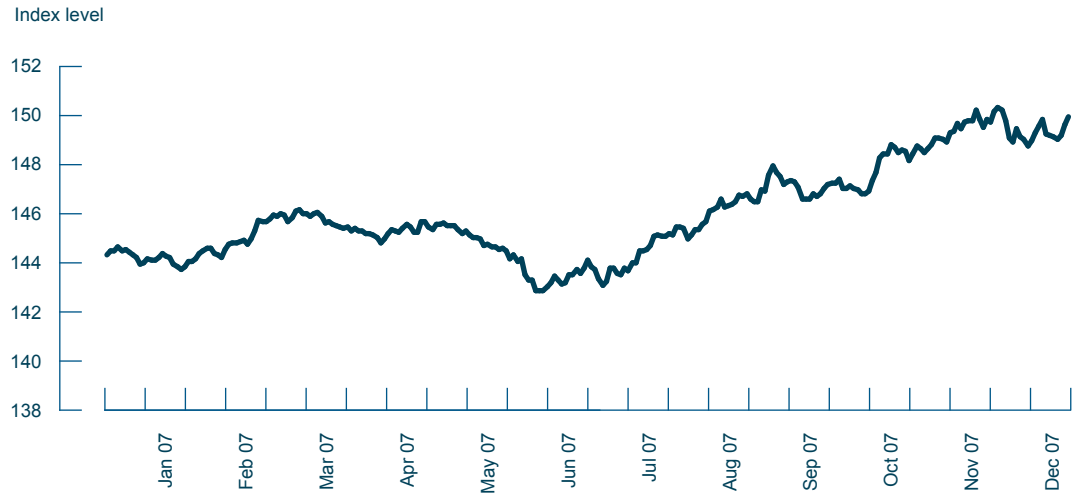
Average performance of all population	1.83%
Performance of maximum return class	6.17%
Performance of minimum return class	-10.35%
Standard deviation of performance	1.95%
Performance spread	16.52%
Statistical population	357

Statistical performance distribution of entities investing in international bonds

Performance	Number of entities			
Return classes	Absolute frequency	Relative frequency	Cumulative absolute frequency	Cumulative relative frequency
-12% to -9%	9	2.52%	9	2.52%
-9% to -6%	34	9.52%	43	12.04%
-6% to -3%	47	13.17%	90	25.21%
-3% to 0%	93	26.05%	183	51.26%
0% to 3%	135	37.82%	318	89.08%
3% to 6%	37	10.36%	355	99.44%
6% to 9%	2	0.56%	357	100.00%
Total	**357**	**100.00%**		

The Lehman Brothers Global Aggregate - Index Level, EUR, Hedged realised a performance of 3.89% in 2007. 18 entities investing in international bonds, i.e. 5.04% of all entities, have realised a higher performance than the Lehman Brothers Global Aggregate - Index Level, EUR, Hedged. The market volatility for international bonds is of 2.39% (source: Lehman Brothers, CSSF calculation).

Lehman Brothers Global Aggregate - Index Level, EUR, Hedged, 2007



Source: Lehman Brothers

Interpretation of the Sharpe ratio:

UCIs investing in international bonds realised in 2007 on average a negative return of -0.71% per risk entity considered. For the performance of the maximum return class, a positive return of 0.48% on average could be observed per risk entity. For the performance of the minimum return class, a negative return of -3.28% on average could be observed per risk entity considered.

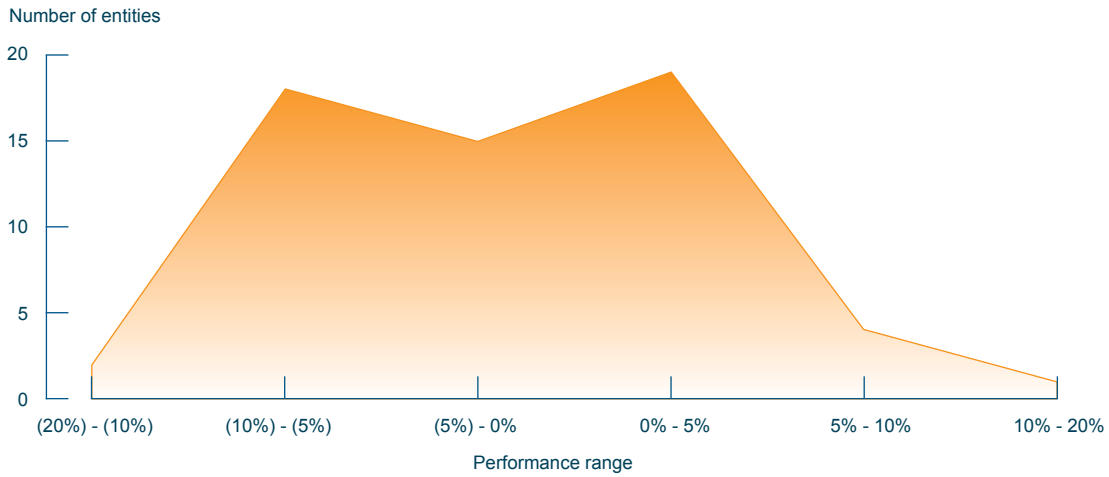
Summary table of the category of entities investing in international bonds

Average performance of the whole population	1.83%
Performance of maximum return class	6.17%
Performance of minimum return class	-10.35%
Standard deviation of performance	1.95%
Performance spread	16.52%
Statistical population	357
Lehman Brothers Global Aggregate - Index Level, EUR, Hedged performance	3.89%
Market volatility	2.39%
Number of entities with higher performance than Lehman Brothers Global Aggregate - Index Level, EUR, Hedged	18
Sharpe ratio – average performance	-0.71
Sharpe ratio – maximum return class	0.48
Sharpe ratio – minimum return class	-3.28

6.2.7. Entities whose investment policy consists in investing in emerging market bonds

The following graph illustrates the performance distribution of entities whose investment policy consists in investing in emerging market bonds.

Performance of entities investing in emerging market bonds in 2007



The average performance realised in 2007 by entities whose investment policy consists in investing in emerging market bonds is of -0.73%. The average performance of the maximum return class amounts to 9.35% whereas the average performance of the minimum return class is of -9.87%. The standard deviation of the performance of these entities amounts to 4.97%.

Central values and dispersion characteristics

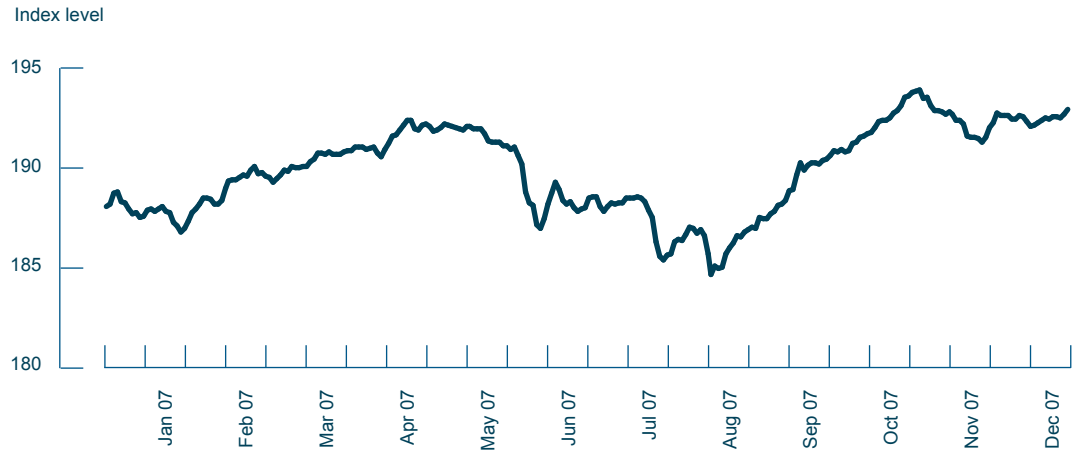
Average performance of the whole population	-0.73%
Performance of maximum return class	9.35%
Performance of minimum return class	-9.87%
Standard deviation of performance	4.97%
Performance spread	19.22%
Statistical population	59

Statistical performance distribution of entities investing in emerging market bonds

Performance	Number of entities			
Return classes	Absolute frequency	Relative frequency	Cumulative absolute frequency	Cumulative relative frequency
-20% to -10%	2	3.39%	2	3.39%
-10% to -5%	18	30.51%	20	33.90%
-5% to 0%	15	25.42%	35	59.32%
0% to 5%	19	32.20%	54	91.53%
5% to 10%	4	6.78%	58	98.31%
10% to 20%	1	1.69%	59	100.00%
Total	**59**	**100.00%**		

The Lehman Brothers Global Emerging Markets - Index Level, EUR, Hedged realised a performance of 2.7% in 2007. 12 entities investing in emerging market bonds, i.e. 20.34% of all entities, have realised a higher performance than the Lehman Brothers Global Emerging Markets - Index Level, EUR, Hedged. The market volatility for emerging market bonds is of 2.53% (source: Lehman Brothers, CSSF calculation).

Lehman Brothers Global Emerging Markets - Index Level, EUR, Hedged, 2007



Source: Lehman Brothers

Interpretation of the Sharpe ratio:

UCIs investing in emerging market bonds realised in 2007 on average a negative return of -0.98% per risk entity considered. For the performance of the maximum return class, a positive return of 1.03% on average could be observed per risk entity. For the performance of the minimum return class, a negative return of -2.27% on average could be observed per risk entity considered.

Summary table of the category of entities investing in emerging market bonds

Average performance of the whole population	-0.73%
Performance of maximum return class	9.35%
Performance of minimum return class	-9.87%
Standard deviation of performance	4.97%
Performance spread	19.22%
Statistical population	59
Lehman Brothers Global Emerging Markets - Index Level, EUR, Hedged performance	2.70%
Market volatility	2.53%
Number of entities with higher performance than Lehman Brothers Global Emerging Markets - Index Level, EUR, Hedged	12
Sharpe ratio – average performance	-0.98
Sharpe ratio – maximum return class	1.03
Sharpe ratio – minimum return class	-2.27

7. MANAGEMENT COMPANIES AND SELF-MANAGED INVESTMENT COMPANIES

7.1. Self-managed investment companies

Whereas at 31 December 2006, 102 investment companies qualified themselves as "self-managed investment company" (SMIC), their number increased to 193 as at 31 December 2007. These 193 SMIC represented 1,484 entities and their net assets amounted to EUR 309 billion.

7.2. Management companies set up under Chapter 13 of the law of 20 December 2002, as amended

7.2.1. Development in number

After the expiry of the UCITS III Directive compliance deadline of 13 February 2007 for management companies, the year 2007 was marked by the return to normal as concerns the introduction of new requests for the setting-up of management companies under Chapter 13 of the law of 20 December 2002, as amended.

In 2007, 18 applications for approval as management companies in accordance with the provisions of Chapter 13 of the law of 20 December 2002 as amended (72 in 2006) were submitted to the CSSF, consisting of:

- thirteen projects for the setting-up of a new management company, of which nine projects from financial players which were not yet established in Luxembourg, and
- five management companies set up under Chapter 14 of the law of 2002 as amended which decided to extend their authorisation to a management company subject to Chapter 13 of this law.

Considering the files opened in 2006 and finalised in 2007, 31 new entities have been registered in 2007 on the official list of management companies under Chapter 13 of the law of 2002. The number of management companies authorised as at 31 December 2007 in accordance with Chapter 13 of the law of 2002 amounted to 180 entities.

Development in the number of management companies under Chapter 13 of the law of 2002

	2003	2004	2005	2006	2007
Registrations	3	23	47	80	31
Withdrawals	/	/	1	3	/
Total	**3**	**26**	**72**	**149**	**180**

Ten out of the 31 new authorisations have been granted to financial players which established for the first time in Luxembourg.

The authorisations of 27 out of the 31 newly registered management companies in 2007 cover exclusively the activity of collective management pursuant to article 77(2) of the law of 2002 and the authorisations of four management companies cover, in addition to collective management, also one or several services referred to under article 77(3).

As for management companies benefiting from extended activities, the progression which started in 2006 did not continue in 2007. Three management companies have abandoned their authorisation to provide discretionary portfolio management services in 2007, as the activity was not as successful as expected.

Development in the number of management companies whose authorisation covers, in addition to the activity of collective management, one or several services referred to in article 77(3) of the law of 2002

	2003	2004	2005	2006	2007
Registrations	2	6	5	10	4
Cessation of extended activities	/	/	/	/	3
Total	**2**	**8**	**13**	**23**	**24**

7.2.2. Geographical origin of management companies

In 2007, management companies of German and Swiss origin remained predominant on the Luxembourg market, followed by entities from France and Italy. It should be noted that management companies of French origin outnumbered the management companies of Italian origin and reached the third position at the end of 2007.

Breakdown of management companies under Chapter 13 of the law of 2002 according to their geographical origin

Country	2004	2005	2006	2007
Belgium	2	4	5	7
Canada	/	/	/	1
Denmark	1	2	3	3
France	3	5	14	20
Germany	8	15	39	42
Great Britain	3	6	7	8
Greece	/	/	1	2
Iceland	/	/	1	1
Italy	3	8	17	19
Japan	/	/	1	1
Liechtenstein	/	/	1	1
Luxembourg	/	1	8	9
Netherlands	2	3	3	4
Portugal	/	/	/	2
Spain	/	1	2	3
Sweden	2	4	5	6
Switzerland	1	18	35	44
United States	1	5	7	7
Total	**26**	**72**	**149**	**180**

7.2.3. Assets managed

As at 31 December 2007, the total net assets managed by management companies set up under Chapter 13 of the law of 2002 amounted to EUR 1,476.8 billion, against EUR 1,306.0 billion at the end of 2006, representing an increase of 13.1%. Considering total net assets of EUR 2,059.4 billion invested as at 31 December 2007 in Luxembourg UCIs, management companies set up under Chapter 13 of the law of 2002 managed two thirds of the total assets of Luxembourg UCIs.

Development in the net assets of management companies

(in billion EUR)	**2006**	**2007**	**Variation 2006/2007**
Net assets	1,306.0	1,476.8	13.1%
of which:			
in "fonds communs de placement"	*594.6*	*657.0*	*10.5%*
in investment companies	*711.4*	*819.8*	*15.3%*

Distribution of management companies in terms of assets under management as at 31 December 2007

Assets under management	**Number of management companies**	
	2006	2007
< 100 million EUR	15	32
100 - 500 million EUR	30	26
500 - 1,000 million EUR	13	25
1 - 5 billion EUR	34	40
5 - 10 billion EUR	23	21
10 - 20 billion EUR	16	15
> 20 billion EUR	18	21
Total	**149**	**180**

7.2.4. Movements in staff numbers

The total number of employees working for management companies amounts to 2,348 people as at 31 December 2007 (2,069 as at 31 December 2006), which represents an increase of 279 employees (+13.4%) over a year. Except for nine entities which registered a slight decrease in the number of staff employed, 2007 has been characterised by a general increase in employment at management companies.

7.2.5. International expansion

- ***Right of establishment***

Six management companies incorporated under Luxembourg law (four in 2006) introduced an application in 2007 in order to establish a branch abroad:

- Assenagon Asset Management S.A. notified its intention to set up a branch in Germany;
- Creutz & Partners, Global Asset Management S.A. operates in Germany through a branch;
- Casa 4 Funds Luxembourg European Asset Management opened a branch in Switzerland;
- Dexia Asset Management Luxembourg S.A. set up in Poland by means of a branch;
- Fortis Investment Management S.A. established a branch in Greece, and
- JPMorgan Asset Management (Europe) S.à r.l. opened a branch in Greece.

On the other hand, the management company Camfunds S.A. transformed its British branch into a subsidiary having the status of an investment firm in Great Britain in 2007.

As at 31 December 2007, the following management companies were represented in one or several countries abroad by means of a branch:

- Assenagon Asset Management S.A.	Germany
- Casa 4 Funds Luxembourg European Asset Management	Switzerland
- Creutz & Partners Global Asset Management S.A.	Germany
- Dexia Asset Management Luxembourg S.A.	Germany, Italy, Netherlands, Poland, Spain, Sweden, Switzerland
- Eurizon Capital S.A.	Chile, Singapore
- Fortis Investment Management S.A.	Greece
- JPMorgan Asset Management (Europe) S.à r.l.	Austria, France, Germany, Greece, Italy, Netherlands, Spain, Sweden

No management company of another EU Member State established a branch in Luxembourg in 2007.

- ***Freedom to provide services***

Three management companies incorporated under Luxembourg law introduced a notification to carry on their activities in one or several EU countries by way of free provision of services in 2007. These notifications concerned portfolio management and other ancillary services.

In 2007, the number of notifications to freely provide services in Luxembourg introduced by management companies from other EU Member States registered an increase as compared to 2006. Indeed, 23 management companies (ten in 2006) of other EU Member States have notified their intention to provide services in Luxembourg by way of free provision of services. The majority of these notifications were submitted by French and Spanish management companies and concerned discretionary portfolio management activities.

- ***Representative offices***

In 2007, three management companies have opened representative offices abroad:

- Dexia Asset Management Luxembourg S.A.	Canada
- Ökoworld Lux S.A.	Germany
- Sparinvest S.A.	Austria

7.2.6. Supervisory practice

- ***Management company and MiFID***

Following the entry into force of the law of 13 July 2007 on markets in financial instruments, amending, among others, the law of 20 December 2002 concerning undertakings for collective investment, management companies set up under Chapter 13 of the law of 2002, whose authorisation includes discretionary portfolio management, fall under the scope of certain provisions of MiFID Directives 2004/39/EC and 2006/73/EC. As a result, these management companies must, among other things, comply with the related articles of Grand-ducal regulation of 13 July 2007 on organisational requirements and rules of conduct in the financial sector.

In this respect, the CSSF decided that the management companies concerned must inform it of the names of the persons in charge of the compliance, risk management and internal audit functions. In this context, it should be mentioned that circular CSSF 04/155 on the compliance function applies *mutatis mutandis* to the above management companies.

- ***Shareholders***

The CSSF now accepts that natural persons hold indirectly, through the intermediary of a holding company, a qualifying holding in a management company on the following conditions:

- the identity of the natural persons holding the management company through a holding company must be known;
- the shareholder structure composed of natural persons must present all required parameters to ensure sound and prudent management of the management company, and
- the CSSF must be in a position to effectively exercise its prudential control.

- ***Financing the capital of a management company through a loan***

The CSSF considers that the capital of a management company must be "at free disposal" in order to ensure a sound and prudent management of the entity. The capital of a management company shall thus not originate from a bank loan contracted by the shareholder(s) of the management company.

- ***Assimilation of subordinated loans to own funds of a management company***

The CSSF accepts subordinated loans to be assimilated to own funds of management companies under Chapter 13 of the law of 2002 on condition that they comply with the criteria and limits listed in Directive 2006/48/EC of 14 June 2006.

8. DEVELOPMENTS IN THE REGULATORY FRAMEWORK

8.1. Grand-ducal regulation of 8 February 2008 concerning certain definitions of the law of 20 December 2002 relating to undertakings for collective investment, as amended, and transposing Directive 2007/16/EC of 19 March 2007 implementing Directive 85/611/EEC on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) as regards the clarification of certain definitions

The Grand-ducal regulation clarifies certain definitions of the law of 20 December 2002 relating to undertakings for collective investment, as amended, and transposes the provisions of Directive 2007/16/EC which do actually not bring about any new obligation for the supervisory authority or the market players in terms of operating methods or with regard to the operational aspect. Indeed, Directive 2007/16/EC aims essentially at clarifying certain definitions of the amended Directive 85/611/EEC in order to ensure uniform application of this Directive.

The Grand-ducal regulation includes in particular clarifications on the following eligible assets in relation to UCITS: transferable securities, money market instruments, liquid financial assets, transferable securities embedding a derivative instrument (embedded derivatives), techniques and instruments and index-replicating UCITS.

The Grand-ducal regulation entered into force four days after its publication in the *Mémorial* on 19 February 2008. UCITS already set up at the entry into force of the Grand-ducal regulation benefit from an extension until 23 July 2008 at the latest to comply with the provisions of this regulation.

8.2. Circular CSSF 07/308 concerning the rules of conduct to be adopted by undertakings for collective investment in transferable securities with respect to the use of a method for the management of financial risk, as well as the use of derivative financial instruments

The purpose of circular CSSF 07/308 of 2 August 2007, intended for all Luxembourg undertakings of collective investment in transferable securities (UCITS) and those involved in the operation and supervision of such undertakings, is to provide UCITS subject to Part I of the law of 2002 additional information with respect to the use of a method for the management of financial risks within the meaning of article 42(1) of the law of 2002, as well as the use of derivative financial instruments as referred to in article 41(1)g) of this law.

The circular provides UCITS with rules of conduct to be followed when implementing a risk management structure. It is limited to the financial risks directly covered by the law of 2002, namely global exposure, counterparty risk and concentration risk. Moreover, its purpose is to clarify the requirements with respect to the coverage of derivative financial instruments, a corollary to article 52 of the law of 2002, as well as the obligation to perform a daily valuation of the OTC derivative financial instruments arising from articles 41(1)g) and 42(1) of this law.

8.3. Circular CSSF 08/339 on the guidelines of the Committee of European Securities Regulators (CESR) concerning eligible assets for investment by UCITS

Circular CSSF 08/339 dated 19 February 2008 draws the attention of UCITS on the publication of the following guidelines issued by the Committee of European Securities Regulators (CESR):

- "CESR's guidelines concerning eligible assets for investment by UCITS", March 2007 (Ref.: CESR/07-044); these guidelines provide additional clarifications in relation to the provisions of Grand-Ducal regulation of 8 February 2008 transposing Directive 2007/16/EC relating to eligible assets for investment by UCITS covered by Directive 85/611/EEC, as amended;
- "CESR's guidelines concerning eligible assets for investment by UCITS - The classification of hedge fund indices as financial indices", July 2007 (Ref: CESR/07-434); these guidelines provide further specific details on the eligibility of hedge fund indices as underlying instruments of derivatives.

The circular moreover underlines that UCITS must take into account those guidelines when assessing whether a specific financial instrument can be considered as an eligible asset for investment within the meaning of the relevant provisions of the law of 2002.

9. PRUDENTIAL SUPERVISORY PRACTICE

9.1. Prudential supervision

9.1.1. Standards to be observed by UCIs

One of the fundamental duties of the CSSF in the supervision of UCIs is to ensure application of the laws and regulations relating to UCIs. The aim of this supervision is to ensure adequate investor protection as well as stability and security in the UCI sector.

9.1.2. Instruments of prudential supervision

The CSSF's permanent supervision aims to ensure that UCIs subject to its supervision observe all legislative, regulatory and contractual provisions relating to the organisation and operation of UCIs, as well as to the distribution, investment or sale of their securities. This supervision is based in particular on:

- the examination of the periodic financial information which UCIs must submit to the CSSF on a monthly and annual basis;
- the analysis of annual and semi-annual reports which UCIs must publish for their investors;
- the analysis of the management letters issued by the external auditor, which must be communicated immediately to the CSSF;
- the analysis of the statements made in accordance with the circular on the protection of investors in case of a NAV (net asset value) calculation error and correction of the consequences resulting from non-compliance with the investment rules applicable to UCIs;
- on-site inspections carried out by CSSF agents.

9.1.3. Means of control

- ***Review of semi-annual and annual reports***

The review of semi-annual and annual reports carried out by the CSSF shows that these reports are in general drawn up in accordance with the applicable legal rules.

- ***Review of financial information for the CSSF and STATEC***

In accordance with circular IML 97/136 and pursuant to article 118 of the law of 2002, as amended, the central administrations of Luxembourg UCIs must transmit financial information by electronic means to the CSSF, on a monthly (tables O 1.1.) and yearly (tables O 4.1. and O 4.2.) basis. The deadline to transmit the monthly financial information is twenty days following the reference date, which is in principle the last day of each month. As regards yearly financial information, the reference date is the date of the close of the financial year and the time limit is four months.

As far as monthly financial information is concerned, the CSSF considers that UCIs must, on the one hand, scrupulously observe the allocated deadline to submit table O 1.1. and, on the other hand, pay due attention when drawing up this table so as to ensure that the format and content are correct. For information, the format and content of about 11,000 files, representing nearly 23,000 types of units/shares, are controlled every month.

- ***Surveys on Late Trading and Market Timing***

In accordance with circular CSSF 04/146 concerning the protection of UCIs and their investors against Late Trading and Market Timing practices, two cases of potential Market Timing and a notification of Late Trading have been reported to the CSSF in 2007. Upon examination, the CSSF was able to close the files without taking any further action.

- ***Meetings***

In 2007, 159 meetings were held between representatives of the CSSF and intermediaries of UCIs. These meetings concerned the presentation of new UCI projects, restructurings of UCIs, but also the application of the laws and regulations of UCIs.

9.2. Circular CSSF 02/77 on the protection of investors in case of NAV calculation error and correction of the consequences resulting from non-compliance with the investment rules

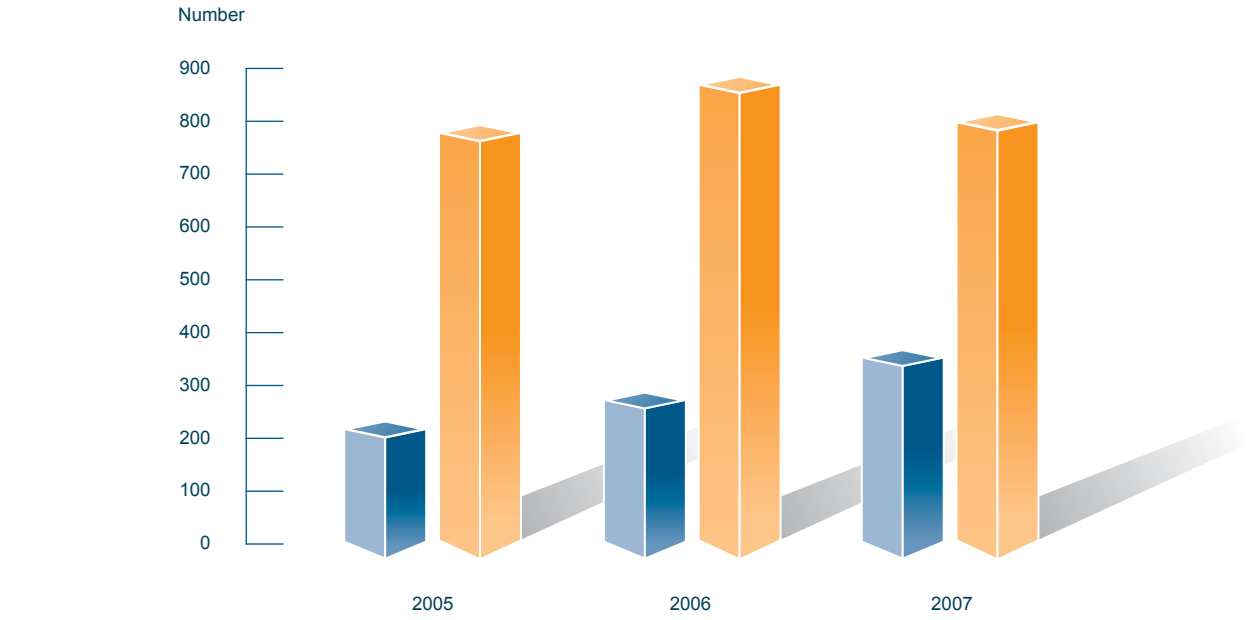
The figures for the year 2007 included in this section refer to the period from 1 January 2007 to 30 November 2007.

9.2.1. Reports made in 2007 on the basis of circular CSSF 02/77

From 1 January to 30 November 2007, the CSSF received 1,160 statements on the basis of circular CSSF 02/77, against 1,150 statements in 2006, representing an increase of 1%.

Among these reports, 353 cases (274 in 2006) concerned NAV calculation errors and 807 cases (876 in 2006) non-compliance with investment rules. The following graph shows the development in the number of NAV calculation errors and cases of non-compliance with investment rules which have been reported to the CSSF over the last three years.

Development in the number of NAV calculation errors and cases of non-compliance with investment rules over the last three years



	2005	2006	2007
NAV calculation errors	219	274	353
Non-compliance with investment rules	784	876	807

As far as the number of NAV calculation errors is concerned, the rising trend which began in 2005 was confirmed in 2007. This growth should however be seen in the light of the number of registered UCIs, which is increasing as well.

The number of instances of non-compliance with investment rules again exceeded 800 reports.

As regards more particularly the reports received until 30 November 2007, 115 out of the 353 reported cases of NAV calculation errors and 107 out of the 807 cases of non-compliance with investment rules could not be closed at 30 November 2007, as the CSSF was still awaiting either further information, or the report(s) of the external auditor or the management letter, or the long form report following the application of the simplified procedure as provided for by circular CSSF 02/77.

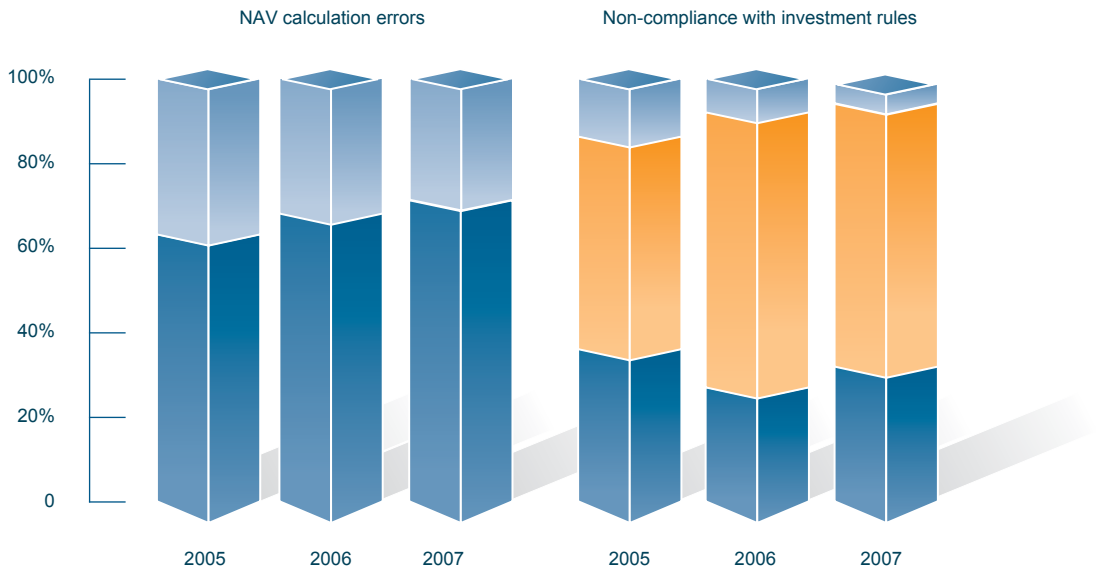
Indeed, circular CSSF 02/77 introduced a simplified procedure for cases of NAV calculation errors or non-compliance with investment rules that entail losses for the UCI, where the indemnification amount does not exceed EUR 25,000 and the amount to be reimbursed to an investor does not exceed EUR 2,500.

In this event, no corrective action plan needs to be submitted to the CSSF, but the central administration must notify the occurrence of the calculation error or non-compliance to the CSSF and promptly take the measures necessary to correct the calculation error or non-compliance and arrange the indemnification of the damages occurred. The external auditor of the UCI must review the correction process and state in his long form report whether, in his opinion, the correction process is appropriate and reasonable.

In 2007, 251 out of 353 cases of NAV calculation errors fell within the scope of the simplified procedure (185 cases out of 274 in 2006). 261 out of 807 cases of non-compliance with investment rules have also applied this procedure (237 cases out of 876 in 2006).

The following graph plots the proportion of the cases of simplified procedure compared to the total number of reports received over the last three years.

Simplified procedure

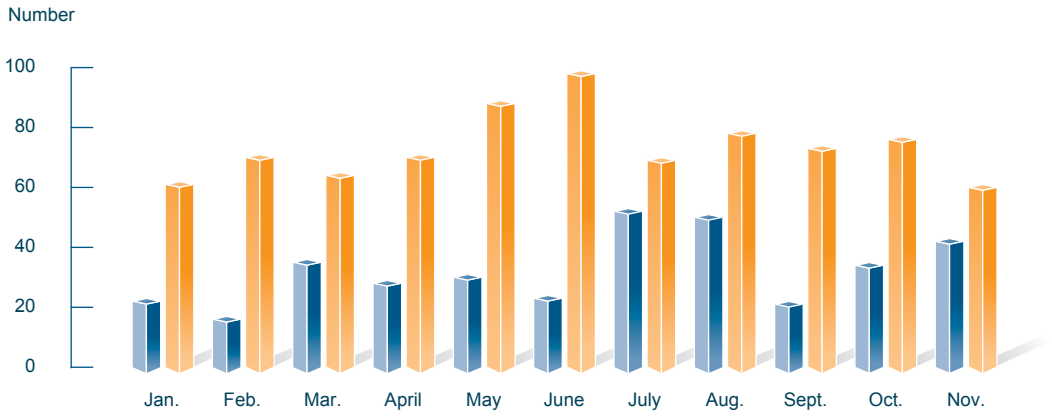


	NAV calculation errors			Non-compliance with investment rules		
	2005	2006	2007	2005	2006	2007
Normal procedure	37%	32%	29%	14%	8%	6%
Non-compliance without prejudice	-	-	-	50%	65%	62%
Simplified procedure	63%	68%	71%	36%	27%	32%

Thus, from 1 January to 30 November 2007, 71% of the statements of NAV calculation errors fell within the scope of the simplified procedure (68% in 2006 and 63% in 2005). As regards the cases of non-compliance with investment rules, 32% of the cases met the criteria of the simplified procedure (27% in 2006 and 36% in 2005) and 62% of the cases could be regularised without harming the investors nor the UCIs (65% in 2006 and 50% in 2005).

The following graph sets out in detail the reports made from 1 January to 30 November 2007.

Development in the errors and instances of non-compliance notified in 2007



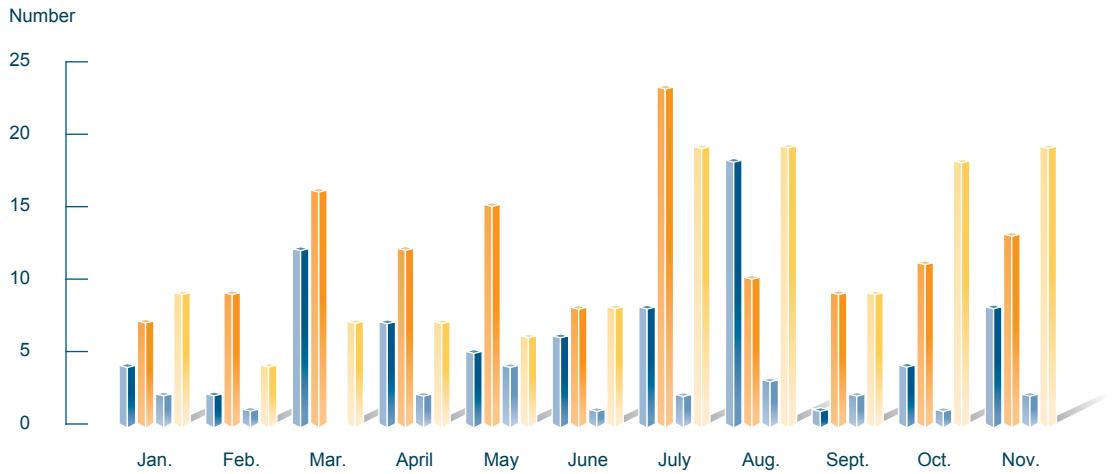
	Jan.	Feb.	Mar.	April	May	June	July	Aug.	Sept.	Oct.	Nov.
NAV calculation errors	22	16	35	28	30	23	52	50	21	34	42
Non-compliance with investment rules	61	70	64	70	88	98	69	78	73	76	60

42% of the reports were made during the months of May to August 2007. This can be explained, among others, by the fact that the finalisation works for the UCI long form report start during this period and that the auditor detects only at that moment the NAV calculation errors or the instances of non-compliance with the investment restrictions that have not been previously identified.

NAV calculation errors may be linked to four different causes: pricing errors, booking errors, errors in the calculation of costs and accruals and other errors, for example in the valuation of swaps or futures.

The following graph plots the different causes of NAV calculation errors recorded during the period from 1 January to 30 November 2007.

Development of the causes for NAV calculation errors in 2007

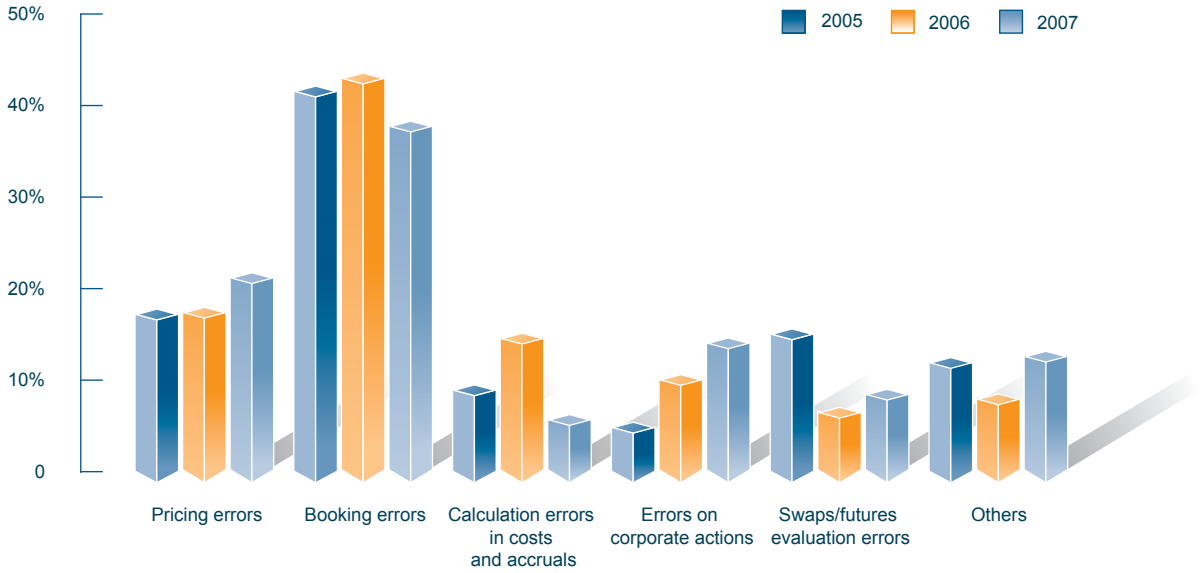


	Jan.	Feb.	Mar.	April	May	June	July	Aug.	Sept.	Oct.	Nov.
Pricing errors	4	2	12	7	5	6	8	18	1	4	8
Booking errors	7	9	16	12	15	8	23	10	9	11	13
Calculation errors in costs and accruals	2	1	0	2	4	1	2	3	2	1	2
Other	9	4	7	7	6	8	19	19	9	18	19

During the relevant period, 21% of NAV calculation errors were due to pricing errors, 38% to booking errors and 6% to calculation errors in costs and accruals. Among the other causes of error, problems linked to corporate actions represent 14% of the cases reported and errors in the valuation of swaps and futures account for 8% of the NAV calculation errors.

The following table shows the development of the causes of NAV calculation errors recorded since 2005.

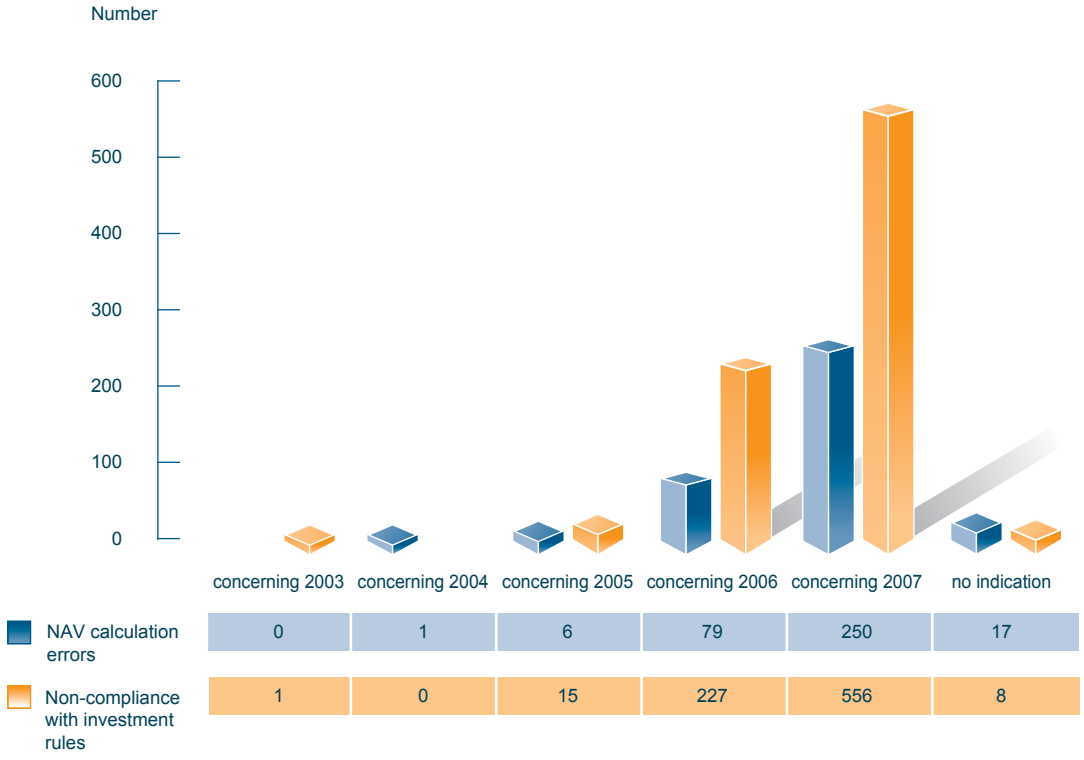
Development of the causes of NAV calculation errors over the last three years



Over the last three years, booking errors and errors in the valuation of securities held by UCIs were the main causes for NAV calculation errors. Whereas the number of errors relating to problems in the valuation of swaps/futures decreased substantially in 2006 as compared to 2005, the number of this type of errors recorded a slight increase in 2007. However, the increase in the errors originating from corporate actions, already registered in 2006, was confirmed in 2007. Concerning the errors in costs and accruals, a significant decrease could be noticed in 2007.

It should be noted that reports made during 2007 do not always refer to errors and instances of non-compliance that occurred during 2007. Indeed, they can also relate to errors or instances of non-compliance detected in 2007, but which relate to errors or instances of non-compliance that occurred previously, as shown in the graph below.

Reports made from 1 January 2007 to 30 November 2007



Out of 1,160 reports received from 1 January to 30 November 2007, 0.1% were related to errors and 0.1% to instances of non-compliance that had already occurred in 2003 or in 2004. 1.8% and 26.4% of the reports concerned errors or instances of non-compliance which occurred in 2005 and 2006, while 69.5% related to errors or instances of non-compliance that had actually occurred in 2007.

9.2.2. Compensation paid following regularisation of NAV calculation errors or instances of non-compliance with investment rules

The table below sets out the compensation amounts notified in 2006 and 2007. It has to be noted that it is based on data available to the CSSF as at 31 December 2006 and 30 November 2007 respectively, while the compensation amounts had not yet been notified in certain cases.

Compensation paid following NAV calculation errors

	Investors		UCI/Sub-fund	
	2006	**2007**	**2006**	**2007**
EUR	3,628,317.75	3,020,854.98	4,039,577.26	3,074,267.50
USD	1,076,828.98	3,224,771.49	3,401,307.28	2,315,064.03
GBP	1,040.00	8,672.43	143.00	149,875.36
CHF	65,759.29	-	76,626.73	-
Other currencies*	145,719.45	488,096.45	17,780.20	205,190.56
Total *(in EUR**)*	**4,634,146.84**	**6,742,395.36**	**6,687,873.99**	**5,744,403.27**

Compensation paid following non-compliance with investment rules

	Investors		UCI/Sub-fund	
	2006	2007	2006	2007
EUR	1,449.26	3,564.09	1,781,131.53	1,763,450.19
USD	-	-	706,293.98	1,401,569.82
GBP	43.14	-	39,900.93	7,885.63
CHF	484.46	-	33,160.81	8,145.57
Other currencies*	-	-	185,579.98	1,871.95
Total *(in EUR**)*	**1,814.99**	**3,564.09**	**2,583,058.65**	**3,639,777.29**

* converted in EUR at the exchange rate applicable on 31 December 2007 and 31 December 2006 respectively.

** exchange rate as at 31 December 2007 and 31 December 2006 respectively.

The increase of the amounts paid out as a compensation following non-compliance with investment rules which was emerging in 2006 was confirmed in 2007. However, it should be noted that the compensation amounts linked to only two instances of non-compliance with investment rules represented 61% of the total amount paid out to sub-funds.

As regards the increase of the amounts paid out as a compensation following NAV calculation errors, it should be noted that the compensation amounts linked to only five NAV calculation errors represented 40% of the total amount paid out to investors and 52% of the total amount paid out to sub-funds.

9.2.3. Management letters

Chapter P of circular IML 91/75 of 21 January 1991 states that UCIs must automatically and immediately communicate to the CSSF the management letters issued by external auditors in the context of the audits which the latter are obliged to undertake pursuant to article 113 of the law of 2002.

The analysis below is based on the data of the year 2006, since these are more pertinent. Indeed, most UCIs close their financial year on 31 December so that the data relating to 2006 are established by the CSSF in 2007.

As in the previous years, many management letters, namely 73%, are management letters that contain no recommendations, i.e. the external auditor has not detected any irregularities in the management of the UCIs. 18% are management letters with recommendations by which the external auditors have reported irregularities of various types. 9% of the management letters have not been submitted yet.

With regard to management letters with recommendations, the irregularities pointed out by external auditors can be divided into four main categories: overstepping of statutory or regulatory limits, NAV calculation errors, non-compliance with investment policy and problems in the organisation of UCIs.

9.3. Long form reports

Circular CSSF 02/81 of 6 December 2002 sets out the rules concerning the scope of the audit of the annual accounting documents and the content of the long form reports to be drawn up pursuant to the law on UCIs. The circular, which applies to all Luxembourg UCIs, takes account of the fact that in practice, the role and function of the external auditor are one of the pillars of the prudential supervision of UCIs.

The purpose of the long form report introduced by circular CSSF 02/81 is to report on the findings of the auditor in the course of its audit concerning the financial and organisational aspects of the UCI comprising *inter alia* its relationship with the central administration, the depositary bank and other intermediaries (investment managers, transfer agents, distributors, etc.).

The reports enable the CSSF to strengthen the supervision of UCIs as they provide detailed information on the organisation of UCIs and on their relationships with the central administration, the depositary bank or any other intermediary.

9.4. Enforcement of the legislation concerning UCIs

9.4.1. Circular CSSF 02/77 on the protection of investors in case of NAV calculation error and correction of the consequences resulting from non-compliance with the investment rules applicable to undertakings for collective investment

In relation to the concept of materiality in the context of net asset value (NAV) calculation errors, the CSSF informs that it reviewed its position on the establishment of a materiality threshold and that it now accepts the approach consisting in an analysis of the nature of the underlying in order to define the materiality threshold applicable to NAV calculation errors. In this case, the CSSF accepts the materiality threshold to be defined in relation to the underlying assets of a derivative financial instrument (look-through principle), provided the return of the underlying assets represents a major part of the UCI's performance. This condition is complied with if the return linked to the underlying assets reflects at least 80% of the UCI's performance.

The law of 20 December 2002 relating to undertakings for collective investment, as amended, provides for a certain number of cases where the investment must observe various distinct limitations, notably article 43(2) of the law, which provides that the total value of transferable securities and money market instruments held by a UCITS in the issuing bodies in each of which it invests more than 5% of its assets must not exceed 40% of the value of its assets. As far as the corrective actions of the active excess of such investment limitations is concerned, it might be acceptable that the UCI remedies the non-compliance with investment limits by realising another asset than the one which was at the basis of the excess. In this case, the UCI must be in a position to justify that it takes due account of the investors' interests when remedying the non-compliance.

9.4.2. Circular CSSF 02/81 on the guidelines concerning the task of auditors of undertakings for collective investment

Circular CSSF 02/81 provides in its point 2.3. the control of the risk management system. Hence, with reference to circular CSSF 07/308 on the rules of conduct to be adopted by UCITS with respect to the use of a method for the management of financial risk, as well as the use of derivative financial instruments, the auditor shall verify the risk management method implemented by UCITS in application of the rules and principles set out in this circular. The CSSF considers that the auditor shall proceed to this verification as from the entry into force of circular CSSF 07/308 on 2 August 2007.

9.4.3. Investment within the meaning of article 41(2)a) of the law of 20 December 2002, as amended

Article 41(1)g) of the law of 2002 provides that derivative financial instruments are eligible provided that "the underlying consists of instruments covered by Article 41, paragraph (1), financial indices, interest rates, foreign exchange rates or currencies, in which the UCITS may invest according to its investment objectives as stated in the UCITS' constitutitive documents". The CSSF considers that derivative financial instruments the underlying of which is not eligible within the meaning of this article may be accepted within the meaning of article 41(2)a) of the law of 2002, provided that the underlying asset of the derivative financial instrument is an eligible asset within the meaning of article 41(2)a) of this law.

Moreover, the CSSF had to express an opinion on the eligibility of deposits with a credit institution which is not a credit institution within the meaning of article 41(1)d) of the law of 2002. Article 41(1) d) states that deposits with credit institutions are eligible if "the credit institution has its registered office in a Member State of the European Union or, if the registered office of the credit institution is situated in a non-EU Member State, provided that it is subject to prudential rules considered by the CSSF as equivalent to those laid down in Community law". The CSSF considered that the deposits with a credit institution which does not comply with the criteria set out in this article constitute, in principle, eligible investments within the meaning of article 41(2)a) of the law of 2002.

9.4.4. Unit responsible for risk management within the meaning of circular CSSF 07/308

With reference to circular CSSF 07/308 on the rules of conduct to be adopted by UCITS with respect to the use of a method for the management of financial risk, as well as the use of derivative financial instruments, and in particular section II of this circular which refers to the implementation of a risk management process, the CSSF specifies that the depositary bank of a UCITS may in principle not be appointed as unit responsible for the risk management of UCITS as defined in this section.

9.4.5. Notion of regulated market

In 2007, the CSSF analysed the implications of the provisions of Directive 2004/39/EC (MiFID Directive) on the criteria defining a regulated market in article 41(1), points a) and b) of the law of 2002.

Regulated markets within the meaning of Directive 2004/39/EC which are specifically mentioned on the related list published and updated by the European Commission shall be considered as regulated markets referred to in article 41(1)a).

Moreover, the Euro MTF market may be considered as other market of an EU Member State, which is regulated, operates regularly and is recognised and open to the public, as referred to in article 41(1)b) of the law of 2002. Indeed, this market is registered on the official list of multilateral trading systems (MTF) operated in Luxembourg in accordance with the law of 13 July 2007 on markets in financial instruments (MiFID).

9.4.6. Frequency of the communication of information to the CSSF on the risk management process in accordance with point V of circular CSSF 07/308

In accordance with point V of circular CSSF 07/308, each management company and self-managed investment company (SMIC) must provide to the CSSF clear and precise documentation with respect to the risk management and control process (Risk Management procedure) which has been implemented in application of the rules and principles set out in this circular. A paper version and an electronic version of this documentation must be made available to the CSSF.

The documentation must cover, at any given time, all UCITS (including UCITS' sub-funds) for which they are responsible. For any new UCITS (including sub-funds), the management company or, where applicable, the SMIC, must ensure the appropriateness of the risk management and control process with respect to this new product. Should this not be the case, the necessary adjustments need to be made and incorporated into the above documentation. This updated version must be submitted to the CSSF.

Management companies and SMIC authorised by the CSSF before the entry into force of circular CSSF 07/308 must carry out an internal self-assessment in order to identify potential discrepancies with the provisions of this circular. Such discrepancies must be dealt with and an updated version (in "track changes" mode) of the above documentation must be sent to the CSSF at the earliest opportunity.

The Risk Management procedure must include at least the information indicated under points V.1 to V.6. of the above circular.

In accordance with point V.1. "Implementation of a risk management process", the CSSF requires, among other things, a summarising list of the UCITS to which the Risk Management procedure applies, indicating at least the following information for each UCITS (or sub-fund):

- name of the UCITS (or sub-fund);
- risk profile of the UCITS (sophisticated, non-sophisticated);
- global exposure calculation method (commitment, relative VaR, absolute VaR);
- maximum limit: the maximum limit must not exceed the regulatory limit as defined in point III.1. of the circular (100% for the commitment approach, 200% relative VaR, 20% absolute VaR); however, the CSSF expects the maximum limit set by the UCITS to be compliant with the given risk profile, which may mean that, according to its risk profile, a UCITS defining the global exposure through VaR will have to set a limit which is lower than the regulatory limit in order to ensure profile/limit consistency;
- reference portfolio (if limitation of relative VaR);
- exposure (i.e. use of the maximum limit).

This list must be established on an annual basis, the first reference date being 31 December 2007. It should be noted that the CSSF reserves the possibility to request the lists on a more frequent basis.

CHAPTER III

SUPERVISION OF PENSION FUNDS

1. DEVELOPMENTS IN THE PENSION FUNDS SECTOR IN 2007

1.1. Pension funds

As at 31 December 2007, 13 pension funds subject to the law of 13 July 2005 on institutions for occupational retirement provision in the form of pension savings companies with variable capital (sepcav) and pension savings associations (assep) were registered on the official list of pension funds, against 14 in 2006, the assep K BRIDGE having been withdrawn from the list in 2007.

In general, the pension funds sector stagnated in 2007. The entry into force on 23 September 2005 of Directive 2003/41/EC on the activities and supervision of institutions for occupational retirement provision (IORP Directive), which confers a European passport on institutions for occupational retirement provision, did not yet entail a sustained development of the pan-European pension funds market.

The CSSF expects a positive but slow development of the pension funds activity in the coming year, through the development of the existing pension funds' activities, as well as through the establishment of new entities in Luxembourg.

1.2. Liability managers

There has been no new registration in 2007 on the official list of professionals authorised to act as liability managers for pension funds subject to the law of 13 July 2005 as amended. Consequently, the number of liability managers of pension funds approved by the CSSF amounted to 12 as at 31 December 2007.

2. INTERNATIONAL CO-OPERATION

Work in progress at the Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS)

The Occupational Pensions Committee, a sub-committee of CEIOPS, is dealing more specifically with rules and principles regarding prudential supervision of the activities of institutions for occupational retirement provision.

In 2007, the Occupational Pensions Committee was mapping out the prudential approaches across Member States in the following areas:

- scope of the Directive;
- application of investment rules (prudent person rule);
- application of the rules regarding minimum funding and calculation of technical provisions;
- possibility for an institution for occupational retirement provision to benefit from funding through subordinated loans;
- insolvency protection institutions;
- application of ring-fencing rules;
- use of depositaries for institutions for occupational retirement provision;
- information to members and beneficiaries;
- reports to submit to the supervisory authorities;
- application of the provisions regarding cross-border activities.

The purpose of this mapping out is to examine the manner in which various provisions of the IORP Directive have been transposed in the Member States in order to achieve a common understanding of the Directive as well as progressive convergence in supervisory practices. The mapping exercise also covered topics that the European Commission is to review in 2008 in the light of Directive 2003/41/EC in order to consider, if need be, a modification of the relevant provisions of the Directive.

A report setting out the main observations, conclusions and recommendations was drawn up and will be released, in principle, on CEIOPS' website in spring 2008 (www.ceiops.eu).

In 2007, the Occupational Pensions Committee created a sub-committee whose task is to examine issues relating to provisions of the IORP Directive on the solvency of institutions for occupational retirement provision in the light of the developments in other sectors. This sub-committee examined the systems in place in the Member States to ensure solvency of institutions for occupational retirement provision. Its conclusions are expected in spring 2008 and an extensive consultation on this issue is planned.

For 2008, the Occupational Pensions Committee will decide on the follow-up to the observations and recommendations included in those reports and continue its fact-finding mission with respect to other topics. To this end, a study is currently being carried out on the content of social and labour laws applicable to institutions for occupational retirement provision in the Member States. Two new projects will analyse the provisions applicable in the Member States with respect to outsourcing and the internal control and risk management requirements for institutions for occupational retirement provision.

Other works include drawing up a preliminary assessment of the Budapest Protocol[1], assessing the effectiveness of the notification procedure among Member States, solving various issues regarding definitions and introducing a procedure for cross-border member and beneficiary complaint handling.

Last but not least, CEIOPS henceforth publishes periodical releases on the development of cross-border activities of institutions for occupational retirement provision (www.ceiops.eu).

[1] Protocol relating to the Collaboration of the Relevant Competent Authorities of the Member States of the European Union in Particular in the Application of the Directive 2003/41/EC of the European Parliament and of the Council of 3 June 2003 on the Activities and Supervision of Institutions for Occupational Retirement Provision (IORPs) Operating Cross-Border (http://www.ceiops.org/media/files/publications/protocols/CEIOPS-DOC-08-06BudapestProtocol.pdf).

CHAPTER IV

PRUDENTIAL SUPERVISION OF SICARS

1. DEVELOPMENTS IN THE SICAR SECTOR IN 2007

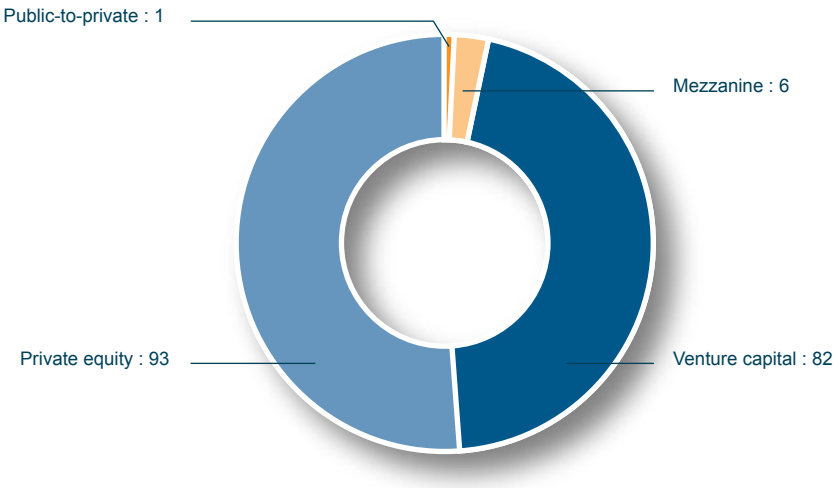
In 2007, the CSSF received 69 files from SICARs applying for registration on the CSSF's official list of SICARs, ten of them having however been abandoned, at the initiators' request, during the scrutiny process.

The number of SICARs registered on the CSSF's official list grew from 115 entities as at 31 December 2006 to 182 entities as at 31 December 2007. At that date, some forty SICAR files were still being processed.

The following graphs break down the 182 SICARs registered on the official list as at 31 December 2007 according to investment policy and investment strategy.

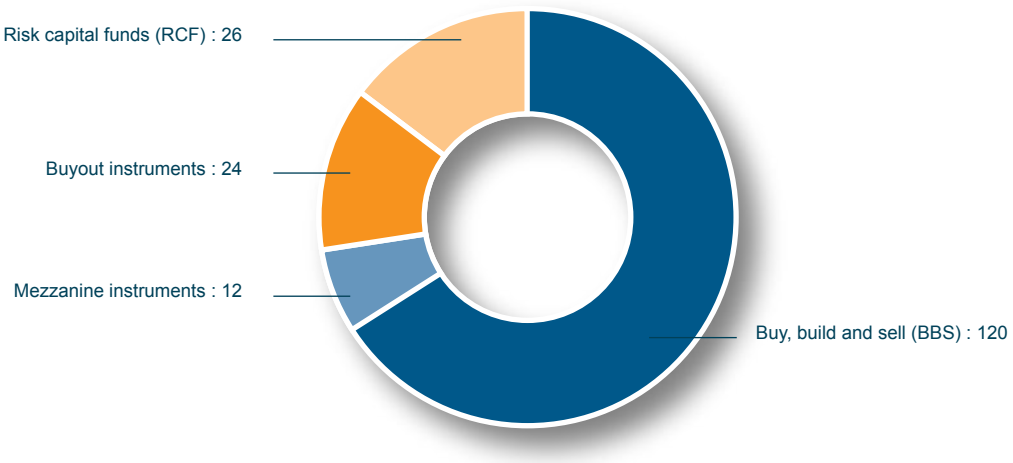
As regards the investment policy, the graph highlights a slight preference for private equity, followed by venture capital, without however revealing an actual trend for a specific investment policy.

Investment policy



As regards the investment strategy, it can be observed that SICARs choose either to limit their policy to a particular strategy (buy, build and sell, buyouts, mezzanine financing, risk capital funds, etc.), or to adopt a combination of strategies generally used in the field of risk capital.

Investment strategy



As regards the sector-based distribution, a significant number of SICARs would rather not limit their investment policy to a particular investment sector. Among the SICARs having adopted a specialised policy, a certain concentration can be identified in the real estate and technology sectors.

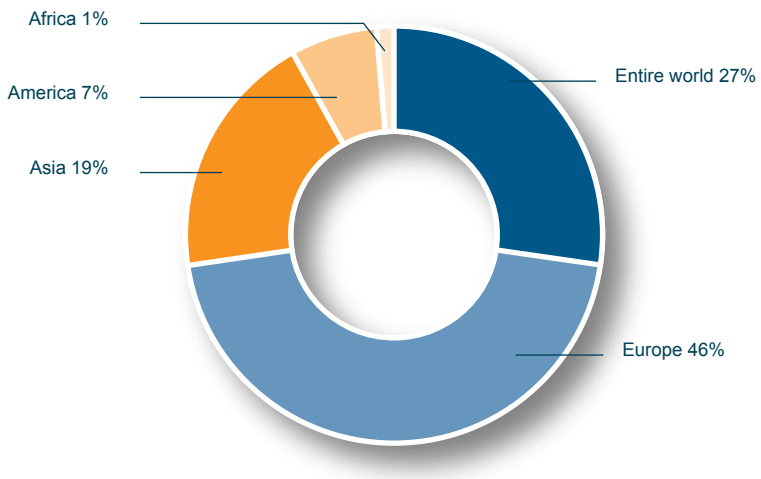
Moreover, there has been a significant increase in SICARs investing in the (renewable) energy sector in 2007. The objective of SICARs that take an interest in renewable energy is to invest in entities fighting climate change, *inter alia* the reduction in greenhouse gases, or to foster the use of renewable energy.

Sector-based distribution

Sector	Number
All sectors	89
Real estate	35
Technology	20
Energy	9
Industry	9
Finance	4
Science	4
Services	4
Microfinance	2
Precious metals and gemstones	2
PPP	2
Sports	2
Total	**182**

As far as the geographical area of the investments is concerned, 46% of the SICARs invest in Europe, whereas 27% of the SICARs are not limited to a specific region. It should be noted that almost 20% of SICARs explicitly aim at investments in Asia.

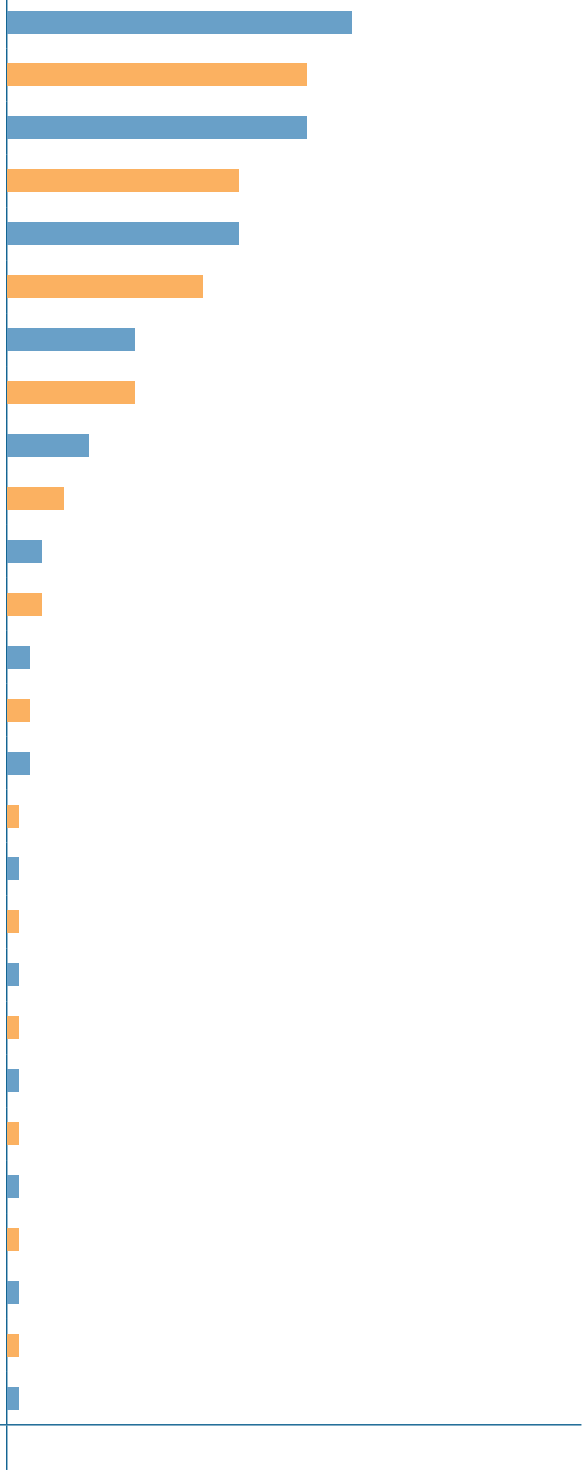
Investment region



As far as the geographical origin of the initiators is concerned, those from Europe are largely predominant, followed by US initiators.

Geographical origin of the initiators

Country	as a % of total
France	15.2
Luxembourg	13.2
Germany	13.2
United States	10.2
Switzerland	10.2
Italy	8.6
Belgium	5.6
Great Britain	5.6
Spain	3.6
Austria	2.5
Netherlands	1.5
Russia	1.5
Denmark	1.0
Finland	1.0
Turkey	1.0
Australia	0.5
Egypt	0.5
Greece	0.5
Guernsey	0.5
British Virgin Islands	0.5
India	0.5
Iceland	0.5
Kuwait	0.5
Latvia	0.5
Poland	0.5
Portugal	0.5
Slovenia	0.5
Total	**100%**

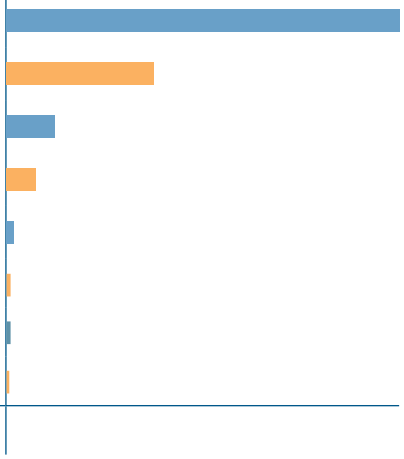


Based on the provisional figures as at 31 December 2007, the capital commitments of SICARs reached EUR 11,375.43 million and the balance sheet total (subscribed capital unpaid excepted) amounted to EUR 18,527.18 million. Total net assets amounted to EUR 17,371.62 million.

The following graph breaks down net assets of SICARs according to investment policy.

Breakdown of net assets according to investment policy

Investment policy	**Net assets** *(in mn EUR)*
Private equity	10,882.72
Private equity + venture capital	4,087.95
Venture capital	1,357.57
Private equity + public-to-private	816.92
Mezzanine	102.65
Private equity + venture capital + mezzanine	67.09
Private equity + mezzanine	52.38
Mezzanine + private equity + venture capital	4.35
Total	**17,371.62**



As at 31 December 2007, 75% of the SICARs had started the investment process.

Investment in risk capital amounted to EUR 17,148.96 million, while the funds awaiting investment amounted to EUR 589.80 million.

It should be noted that SICARs are mainly financed by their investors. Total financing by banks only amounted to EUR 1,125.24 million, representing 6.07% of the SICARs' balance sheet total.

2. REGULATORY FRAMEWORK

Fight against money laundering and terrorist financing

By amending the law of 12 November 2004 on the fight against money laundering and terrorist financing, the law of 13 July 2007 on markets in financial instruments extended the professional obligations as regards the fight against money laundering and terrorist financing to SICARs.

SICARs are thus required to set up appropriate procedures to meet those professional obligations.

3. PRUDENTIAL PRACTICE

3.1. Introduction of a standardised reporting for SICARs

In December 2007, the CSSF invited the SICARs registered on the official list to submit henceforth half-yearly financial information to the CSSF in a standardised format and by electronic means. This half-yearly financial information will be used by the CSSF for prudential supervisory and statistical purposes.

To this end, SICARs, or their central administrations, are invited to download the Microsoft ® Excel template corresponding to the SICAR's capital structure (table K 3.1 or K 3.2) published on the CSSF's website (www.cssf.lu) under the heading Legal reporting/Periodic reporting/SICAR. This half-yearly financial information should be transmitted to the CSSF within 45 calendar days after the reference dates, i.e. 30 June and 31 December every year.

When saving the relevant table, care must be taken to observe the nomenclature described in the Schedule of conditions published on the CSSF's website under the heading Legal reporting/Periodic reporting/SICAR.

It should be noted that the new regime for the SICARs' half-yearly financial reporting does not modify the other reporting obligations of SICARs on an annual basis (annual accounts and reports, management letters issued by external auditors) and *ad hoc* reports (copy of reports to investors).

3.2. SICAR investment policies

The CSSF is regularly solicited for diverse interpretation requests concerning the eligibility of certain SICAR investment policies.

In general, the law obliges SICARs to invest exclusively in assets constituting risk capital with the sole exception of funds awaiting investment.

According to the legislator, a SICAR is indeed a specialised investment company whose exclusive purpose is to invest in risk capital. The CSSF therefore considers that the investment policies of SICARs must reflect the philosophy underlying the SICAR vehicle and that the policies must be defined with a certain rigour in order to avoid denaturing the vehicle. Consequently, SICARs must not adopt any accessory investment policy implying the investment in assets which are not representative of risk capital, even to a negligible extent.

3.2.1. Special case: investment in risk capital *via* private equity funds or other intermediary investment companies

The investment policy of a certain number of SICARs provides for investment in risk capital *via* funds or other investment companies investing in private equity assets. In this context, the question arose as to which eligibility criteria apply to these indirect investments, owing to the difficulty to always exclude the risk that the intermediary investment vehicles invest a limited part of their assets in assets that do not meet the "risk capital" criteria as defined in the SICAR law. Indeed, the SICAR does not always have substantial influence on the investment decisions or even on the definition of the policy.

In accordance with the general principles above, the CSSF considers that in order to be eligible, a target fund must qualify as pure private equity or venture capital fund. It is thus not possible to invest in intermediary vehicles whose investment policy explicitly envisages the possibility to invest, even on an ancillary basis, in assets that do not represent risk capital within the meaning of the SICAR law. Nevertheless, the adopted approach does not necessarily imply a formalisation of the policy of the underlying funds with reference to the concept of risk capital within the meaning of the SICAR law.

3.2.2. Funds awaiting investment in risk capital

As the investment policy of a SICAR must be centred on risk capital, any other investment can only be temporary. As a consequence, the management of funds awaiting investment must be made in accordance with the prudent person rule aiming to preserve the capital for the amounts invested on a temporary basis. For example, the placement of funds awaiting investment into current or deposit bank accounts, in money market instruments or liquid bonds issued by high-quality issuers is acceptable in principle, while investment in shares or other securities treated as shares is not.

3.2.3. Eligibility of accessory policies: special case of a SICAR investing *via* private equity real estate funds

The CSSF had to handle the concrete case of a real estate SICAR investing *via* private equity real estate funds and wishing to reserve the possibility (i) to invest, on an ancillary basis, part of its assets in core real estate assets, which are not considered as risk capital within the meaning of article 1 of the law of 15 June 2004, and (ii) to invest liquidities awaiting investment in shares of REITS (Real Estate Investment Trusts).

In accordance with the general principles above, the CSSF did not accept that a real estate SICAR would allow direct or indirect investment, even to a limited extent, in core real estate assets. Likewise, investing all or part of the funds awaiting investment in REITS is not accepted, as those securities are subject to a price risk.

3.3. External audit

3.3.1. External auditor's whistle-blowing duty

Article 27(3) of the law of 15 June 2004 relating to the investment company in risk capital imposed on the external auditor of a SICAR the obligation to report to the CSSF any fact or decision of which he becomes aware while carrying out the audit of the accounting information or any other legal task concerning a SICAR.

More specifically, paragraph 5 of article 27(3) provides that the "auditor shall moreover be obliged to provide the CSSF with all information or certificates required by the latter on any matters of which the auditor has or ought to have knowledge in connection with the discharge of his duties. The same applies if the auditor ascertains that the assets of the SICAR are not or have not been invested according to the regulations set out by the law or the prospectus".

These provisions raise the question of the extent of the external auditor's obligation to report in case the SICAR does not comply with its investment policy or is breaching the law as it invests in assets that are not risk capital.

The CSSF wishes to clarify in this context that the external auditor is required to inform the CSSF promptly and on his own initiative if he becomes aware that the SICAR's assets are not or have not been invested according to the regulations set out by the law or the prospectus.

3.3.2. Management letters issued by external auditors

The CSSF reiterates that SICARs are required to submit to the CSSF, on reception and spontaneously, the management letters issued by external auditors in the course of their audit of annual accounts. It should be specified that where no management letter has been issued by the external auditor, the CSSF requires a written statement from the external auditor confirming that no such letter has been issued.

3.4. Verification of the status of well-informed investor

The CSSF's opinion was sought as regards the conditions that apply to the verification of the criteria of "well-informed investor" for a SICAR likely to be held at 100% by a listed company.

The CSSF considers that a SICAR can be held by a company without a verification of the criteria of "well-informed investor" being required at shareholder level, where it is established that the structure set up does not aim to elude the restrictions of article 2 of the SICAR law.

In particular, verification is not called for where the SICAR's shareholder is an institutional or professional investor or a "large company" in accordance with Annexe II of the MiFID Directive or where the company concerned is able to demonstrate that its investment or commercial activity is not limited to investment in a SICAR.

The reasoning above is valid irrespective of the fact that the company holding the SICAR is a listed company or not.

3.5. Information to include in the application file

In addition to the information provided in its Annual Report 2006 as regards the content of application files, the CSSF specifies that it requires the following additional information.

- Under the authorisation procedures, the CSSF requires the managers proposed for the SICAR to provide, in addition to the *curriculum vitae* and the extract from their police record, a declaration of honour stating on the one hand that the person concerned has not had any criminal conviction, but also that he/she is currently not being prosecuted.
- Moreover, the CSSF needs to be informed on the marketing of the SICAR's securities, notably whether the SICAR markets its securities itself or whether the distribution is made *via* e.g. a banking network or other professionals of the financial sector.

CHAPTER V

SUPERVISION OF SECURITISATION UNDERTAKINGS

1. DEVELOPMENTS IN THE SECTOR OF AUTHORISED SECURITISATION UNDERTAKINGS

In 2007, six securitisation undertakings governed by the law of 22 March 2004 on securitisation have been granted authorisation by the CSSF, namely the following multiple-compartment securitisation undertakings, which have all been incorporated in the legal form of a public limited company:

- Lifemark S.A.
- AIV S.A.
- BlueOrchard Loans for Development S.A.
- Levade S.A
- Alceda Star S.A.
- DWS Access S.A.

The authorisation of these new securitisation undertakings brought the total number of authorised securitisation undertakings to 17 as at 31 December 2007. The total balance sheet of authorised securitisation undertakings exceeded EUR 15.3 billion at the end of 2007.

The submitted application files reveal that securitisation transactions mainly consist in the securitisation of debt, loans and other comparable assets, as well as in repackaging transactions in the form of structured products issues linked to various financial assets.

In general, the securities issued by securitisation undertakings are bonds and subject to foreign law. In the vast majority of cases, the articles of incorporation nevertheless reserve the right for the securitisation undertaking to execute securitisations by issuing shares. Some securitisation undertakings also have the possibility to issue warrants.

To date, the CSSF has not received any application file for the authorisation of a fiduciary-representative under Luxembourg law, even though the law of 22 March 2004 on securitisation has established a specific legal framework for these independent professionals in charge of representing investors' interests. Authorised securitisation undertakings usually appoint a trustee governed by foreign law.

The CSSF expects a moderate growth of securitisation activities in 2008, a trend that is being confirmed by several application files currently under review.

2. PRUDENTIAL SUPERVISORY PRACTICE

2.1. Scope

The law of 22 March 2004 on securitisation (the "Law") set up a specific legal framework governing asset securitisation.

Securitisation undertakings that fit the definition of the Law and whose articles of incorporation, management regulations or issue documents provide that they are subject to the provisions of the Law benefit from a specific legal framework governing their activity. It is however still possible to execute securitisation transactions according to common law outside the scope of the Law.

Securitisation undertakings governed by the Law must be authorised and supervised by the CSSF as soon as they fulfil the criteria of the Law, i.e. as soon as they issue securities to the public on a continuous basis. Certain provisions of the Law thereby apply to all securitisation undertakings, whether they are subject to the supervision of the CSSF or not, while other provisions only apply to the securitisation undertakings subject to the licensing requirement.

As regards the persons covered, the Law only applies to securitisation undertakings having their registered office in Luxembourg. Where a securitisation is realised by means of an issuing vehicle and an acquisition vehicle of which only one is situated in Luxembourg, the Law only governs that one.

2.2. Definition of securitisation and securitisation undertakings

2.2.1. Securitisation

Article 1 of the Law defines securitisation as *"the transaction by which a securitisation undertaking acquires or assumes, directly or through another undertaking, risks relating to claims, other assets, or obligations assumed by third parties or inherent to all or part of the activities of third parties and issues securities, whose value or yield depends on such risks".*

There are thus two aspects to a securitisation transaction: assumption of risks and issuance of securities.

a. Assumption of risks

General principles

The purpose of the Law is to allow the securitisation of a large variety of risks relating to all types of assets, tangible or intangible, and of claims, as well as relating to obligations assumed by or activities of third-party activities. The techniques to assume those risks have not been limited either. Assumption of risks by the securitisation undertaking may result from a transfer of assets, but also from other forms of risk transfer by which the securitisation undertaking notably provides security to the undertaking that wishes to be discharged thereof. Besides the traditional true sale securitisation through the assignment of assets to the securitisation undertaking, the Law allows for "synthetic" securitisations, where only the risk linked to the assets is transferred, as well as whole business securitisations or partial business securitisations where the risk assumed by the securitisation undertaking lies in the profitability of all or part of the activity performed by the third party.

In order to categorise a transaction as a securitisation, the CSSF does not consider the nature of the securitised assets nor the risk transfer mode, but the structure of the transaction and the origin of the risk that is the object of the securitisation.

The specific nature of the securitisation undertaking's activity requires that the risks securitised by the securitisation undertaking exclusively result from assets or claims or obligations assumed by third parties or inherent to all or part of the activities of the third parties, but that they cannot be generated by the securitisation undertaking or result as a whole or in part from the securitisation undertaking's activity itself acting as entrepreneur.

Thus, except for securitisation undertakings whose purpose is to manage financial assets portfolios according to the conditions described in the second last paragraph of this section, any management by the securitisation undertaking of claims, assets or activities of third parties that creates an additional risk owing to the activity of the securitisation undertaking on top of the risk relating to the risk inherent to these claims, assets or activities or which aims to create additional wealth or promote the commercial development of the securitisation undertaking's activities, would be incompatible with the purpose of the Law, notwithstanding the fact that the actual management of the assets, claims and activities has been delegated to an external service provider.

The role of the securitisation undertaking shall thus be limited to the administration of financial flows linked to the securitisation transaction itself and to the 'prudent-man' management of the securitised risks, except for any activity likely to qualify the securitisation undertaking as entrepreneur.

While the securitisation of claims implies in general the acquisition of a credit portfolio from an originator, the structures in which formally the securitisation undertaking itself grants the credits instead of acquiring them on the secondary market, may also be considered as securitisations provided that those credits are put in place upstream by or through a third party, and that the documentation relating to the issue either clearly defines the assets on which the service and the repayment of the credits granted by the securitisation undertaking will depend, or describes the criteria according to which the creditors will be selected, so that the investors are adequately informed of the risks and profitability of their investment. In both cases, information on the characteristics of the loans granted must be provided.

A securitisation undertaking may also securitise existing portfolios of partially drawn credits and of automatically revolving credits, provided that there is a predetermined framework for lending operations and that there is no discretionary power for the securitisation undertaking as regards the choice of the debtor and the credit terms. In both cases, the securitisation undertaking's action must be limited to a 'prudent man' management of an existing portfolio, irrespective of the fact that this management is delegated to a professional acting on behalf of the securitisation undertaking. In certain cases, this management may include for example the re-negotiation of the schedule of repayments or the credit terms in cases such as financial difficulties of a debtor, but it cannot lead by any means to the securitisation undertaking performing a professional credit activity on own account.

The structures whose object is the securitisation of intra-group credits also constitute securitisation transactions provided that the risk assumed by the securitisation undertaking is actually transferred by a legally distinct entity of the group and that a substantial part of the securities issued by the securitisation undertaking is placed with third-party investors, without prejudice to the ability of the originator to subscribe part of the securities issued (typically, but not exclusively the equity portion).

Transactions through which the securitisation undertaking acquires goods or equipment it makes available to an operational company against the payment of a rent are also accepted, provided that those transactions are structured in a way similar to a leasing operation and that their purpose is the financing of the operational company.

Similarly, transactions through which the securitisation undertaking acquires commodities or other goods of this type, also qualify as securitisations, provided that the purpose of such acquisition is to set up a financing or re-financing structure for which the commodities or goods are a guarantee of repayment by third parties of the funds that are made available and that it generates financial flows to the benefit of the investors.

Repackaging structures consisting in setting up issuance platforms for structured products for instance are also admitted. As regards structured products, the securitisation undertaking typically issues securities whose value and/or yield is linked to indices, baskets of shares or derivatives. The purpose of other securitisation undertakings can be the management of a financial asset portfolio, e.g. in the case of a portfolio composed of actively managed collateral debt obligations. In this case, the articles of incorporation or the issue documents of the securities must describe the selection criteria, as well as the composition of the managed portfolio, where applicable, according to the classes of assets. They must also lay down conditions and criteria according to which the assets composing this portfolio can be assigned, in accordance with article 61 of the Law.

In practice, the assumption of risks linked to holdings of shares and parts of undertakings for collective investment, hedge funds and limited partnerships or other companies holding the securitised risks can also be considered as securitisation transaction, provided that the securitisation undertaking does not actively intervene with the management of the entities in which it holds, directly or indirectly, a holding. The securitisation undertaking is only allowed to exercise its shareholder rights (voting right, right to a dividend) linked to the interest it holds and is not allowed to exercise any managing function in the company's bodies or provide services of whatever nature. A majority representation of the managers of the securitisation undertaking in the managing bodies of companies in which the securitisation undertaking holds an interest would not be acceptable.

b. ***Techniques and derivative instruments***

As regards the ancillary activities of a securitisation undertaking such as concluding transactions on derivative instruments or forward transactions with a view to cover or effectively manage the asset portfolio, or such as to perform repurchase agreements concluded and securities lending activities, the specialisation principle applying to securitisation undertakings implies that they must limit those activities to the strict minimum, i.e. where these activities have been made necessary by or are an integral part of the securitisation transactions. Moreover, those activities must be performed pursuant to article 61(1) of the Law which provides that a securitisation undertaking can assign its assets only pursuant to the provisions laid down in its articles of incorporation or its management regulations.

c. ***Issuance of securities***

The assumption of risks by the securitisation undertaking must be financed by issuing securities whose value or yield depends on those risks.

Under the principle of *lex contractus*, securities that are subject to foreign law and recognised as transferable securities by the applicable law are also considered as securities within the meaning of the Law. In addition, financial instruments likely to be traded on a market and which are transferable, i.e. abstract enough so that their assignment is not subject to specific formalities which would make them comparable to a contract assignment, can be considered as securities within the meaning of the Law.

Units and bonds issued by a securitisation undertaking set up as a private limited liability company are also considered to be securities within the meaning of the Law.

2.2.2. Securitisation undertakings

Are considered to be securitisation undertakings within the meaning of the Law those undertakings that perform securitisation transactions in full or by assuming all or part of the securitised risks (acquisition vehicles) or by issuing securities to ensure the financing thereof (issuing vehicles). Thereby, the securitised risks can be lodged in an undertaking that is distinct from the undertaking issuing securities, provided that both undertakings link their respective interventions.

2.3. Functioning of securitisation undertakings

2.3.1. Financing of securitisation undertakings

The securitisation undertaking shall be financed by the issue of securities whose value or yield depends on the risks assumed by the securitisation undertaking or, where applicable, the acquisition vehicle where the assets are held by an undertaking different from the one issuing the securities.

However, it is acceptable that securitisation undertakings use, on a transitional basis, lending or intra-group financing in order to pre-finance the acquisition of risks to be securitised while awaiting to issue securities to investors (warehousing) within an appropriate timeframe by taking account of the market conditions.

To supplement financing through the issue of securities, a securitisation undertaking can also use borrowing on a lasting, but limited and ancillary basis. Borrowing may be used either within the context of setting up the initial structure, e.g. where the initiator grants a subordinated loan at the moment the structure is set up as an alternative to a direct investment in the equity tranche, or as a temporary liquidity facility, notably where there is no perfect matching between the financial flows relating to the securitised assets and financial flows relating to the securities issued by the securitisation undertaking. It is also acceptable to use borrowing in order to create leverage with the purpose of improving investors' yield. Nevertheless, borrowing is acceptable only if the financing of the securitisation transaction also includes issuing securities for a proportionally substantial amount. In any case, the documents relating to the issuance of securities must inform investors sufficiently on the additional risk they incur due to the securitisation undertaking borrowing, as well as on the limits imposed on the indebtedness and on the credit terms.

As regards the nature of the financing through securities issues, the Law allows the securitisation undertaking to issue trackers, i.e. securities whose yield or value is linked to one or several specific compartments, or to certain assets or risks belonging to the securitisation undertaking irrespective of the value and yield of the undertaking or of its compartments.

The securitisation undertaking may also issue subordinated securities (tranching), i.e. securities whose repayment is subordinated to the prior repayment of other securities, certain claims or classes of shares.

The Law also allows securitisation undertakings, including securitisation companies, to issue shares and bonds that do not have an equal value. In that case, the voting right must be proportionate to the portion of share capital or bonds represented.

2.3.2. Management of securitised risks

The securitisation undertaking may manage its assets itself or entrust third parties with the management of its assets, including the assignor, within the limits defined in point 2.2.1.a above. This management of assets is subject to article 61 of the Law which notably requires that the articles of incorporation of the securitisation undertaking lay down, at least in principle, the possibility and procedure for asset assignment covering the investors' rights. However, the CSSF accepts that the articles of incorporation refer to the issue documents, which must provide the decision-making procedure, as well as the asset assignment procedure for every issue.

Security interest may not be created over its assets except in favour of investors and their representatives, as well as creditors whose intervention is necessary or useful to realise a securitisation transaction.

2.3.3. Limited right of recourse

The rights of a securitisation undertaking's investors and creditors are limited to the assets of the securitisation undertaking or to the compartment to which they are attached.

Creditors and investors can accept to subordinate the repayment of their claims to that of other creditors, or certain investors.

Investors and creditors may validly renounce expediting implementing measures against the securitisation undertaking and petitioning for its bankruptcy.

2.3.4. Compartments

The Law allows securitisation undertakings to create one or more compartments corresponding each to a distinct part of their assets and liabilities designated to receive the assets and liabilities linked to the related transactions and that benefit from an independent management of its assets and liabilities.

The assets of a compartment are exclusively available to satisfy the rights of investors in relation to that compartment, and, between investors, each compartment shall be treated as a separate entity, except otherwise provided for in the constitutional documents.

The Law provides for the mandatory segregation of compartments with regard to creditors of the securitisation undertaking by prohibiting creditors whose claims have arisen in connection with the creation, the operation or the liquidation of a compartment to act on the assets of another compartment.

The possibility to create compartments must be laid down in the articles of incorporation or the management rules of the securitisation undertaking. The decision to create compartments lies with the board of directors or the management company and may be taken throughout the existence of the securitisation undertaking.

The articles of incorporation of multi-compartment securitisation undertakings must, in principle, include a clause laying down how the general expenses of the securitisation undertaking that do not relate to a compartment, should be allocated.

Multi-compartment securitisation undertakings are required to draw up financial statements for every compartment. The annual accounts and the relating financial notes must clearly state the financial data for each compartment.

2.3.5. Representative of the holders and fiduciary-representative

Where a securitisation undertaking issues debt instruments, the Law provides the holders of those securities with the benefit of representation as set down by articles 86 and following of the amended law of 10 August 1915 on commercial companies. The investors can also choose another form of representation by entrusting the protection of their interest to a fiduciary-representative whose status is defined by the Law. The CSSF also accepts the designation of a foreign trustee acting in the interest of the investors provided that the terms of this representation are laid down in the agreements relating to the issue of securities.

As regards the representation regime, investors may depart in the articles of incorporation, the issuing agreements or the deed of appointing the fiduciary-representative from the representation regime laid down in the law on commercial companies, whether or not the issue is subject to foreign law.

The articles of incorporation or issue documents can also depart from the application of articles 86 to 97 of the amended law of 10 August 1915 on commercial companies without foreseeing any other organisation of bondholders, provided that a warning for potential investors is included in the issuing agreements. In that case, investors are still able to act individually and to designate a fiduciary-representative at a later stage, if deemed necessary.

2.3.6. Dissolution and liquidation

Securitisation undertakings shall be deemed to continue to exist for the purpose of their liquidation.

The liquidation of a compartment of a securitisation undertaking does not have any consequence on other compartments, i.e. a compartment can be liquidated separately.

In the case of a securitisation company, the liquidation of the last compartment does not result in the liquidation of the company itself. On the other hand, the liquidation of the last compartment of a securitisation fund entails the liquidation of the fund itself, as a securitisation fund without legal personality does not consist of any other assets except of those formed by the compartments.

The liquidators of authorised securitisation undertakings must be authorised by the CSSF and have the necessary good repute and professional qualifications. The liquidation shall be subject to the supervision of the CSSF.

2.4. Obligation and conditions for an authorisation

2.4.1. Obligation for an authorisation

Under article 19 of the law of 22 March 2004 on securitisation, only the "*securitisation undertakings which issue securities to the public on a continuous basis must be authorised by the CSSF to exercise their activities.*" Both criteria, "on a continuous basis" and "to the public", must be fulfilled simultaneously to trigger the requirement for obtaining the CSSF's authorisation.

In order to assess whether it needs to be submitted to the supervision of the CSSF, the securitisation undertaking must determine if, in practice, it issues securities to the public on a continuous basis. Such assessment does not need to be submitted to the CSSF for validation.

It is not required either, in order to avoid the authorisation obligation, that the constitutional documents or issue documents specifically exclude the possibility to issue securities on a continuous basis to the public.

It should be noted that in a dual cross-border structure, where the acquisition vehicle is located in Luxembourg and the issuing vehicle abroad, the Law implies that the acquisition vehicle located in Luxembourg is not subject to the authorisation obligation, even if the foreign issuing vehicle issues securities to the public on a continuous basis.

Once authorised, the securitisation undertaking remains in principle under the supervision of the CSSF until its liquidation. However, if, at one point, the securitisation undertaking does not issue new securities on a continuous basis to the public, and on the condition that all the securities that the securitisation undertaking has issued to the public during the time it was subject to supervision have matured and been refunded, the securitisation undertaking may request to be withdrawn from the official list of authorised securitisation undertakings.

In order to assess the authorisation obligation, the CSSF extracted the following presumptions:

a. *Issuance of securities on a continuous basis*

The CSSF considers that the criterion of issue "on a continuous basis" is assumed to be fulfilled when the securitisation undertaking makes more than three issues per year to the public. The number of issues to consider is determined by the total number of issues of all compartments of the securitisation undertaking.

Moreover, the CSSF considers that the setting-up of an issuance programme cannot be considered as equivalent to one single issue. In order to determine the number of annual issues of a securitisation undertaking issuing securities under a programme, the nature of the programme and of the different series of issues must be analysed in order to assess whether the characteristics of these issues allow to consider that they constitute one single issue and not several separate issues.

b. *Issuance of securities to the public*

Concerning the issuance of securities to the public, the CSSF set down the following criteria:

- issues to professional clients within the meaning of Annexe II to Directive 2004/39/EC (MiFID) are not issues to the public;
- issues whose denominations equal or exceed EUR 125,000 are assumed not to be placed with the public;
- the listing of an issue on a regulated or alternative market does not *ipso facto* entail that the issue is deemed to be placed with the public;

- issues distributed as private placements, whatever their denomination, are not considered as issues to the public. The CSSF assesses whether the issue is to be considered as a private placement on a case-by-case basis according to the communication means and the technique used to distribute the securities. However, the subscription of securities by an institutional investor or financial intermediary for a subsequent placement of such securities with the public constitutes a placement with the public.

2.4.2. Authorisation requirements and procedure

a. Approval of the articles of incorporation

The CSSF approves the articles of incorporation or the management regulations of the securitisation undertaking and authorises, where applicable, the management company. Any change to the management regulations or articles of incorporation is subject to the prior approval of the CSSF.

The same procedure applies to existing securitisation undertakings that seek authorisation only after having made securitisation transactions as non-supervised entities. In that case, the application file must include information on the issues already made.

b. Organisation and administration

The securitisation undertaking must have an adequate organisation and human and material resources to correctly and professionally exercise its activities.

The structuring of the technical aspects of the securitisation transactions, as well as the management of the assets of an authorised securitisation undertaking may be delegated, including to foreign professionals. In that case, an appropriate information exchange mechanism between the delegated functions and the Luxembourg entity administrating the securitisation undertaking must be set up as from the inception of the securitisation undertaking.

The organisational and administrative structure in Luxembourg of a securitisation undertaking subject to authorisation must be sufficient to allow the external auditor and the CSSF to exercise their supervisory tasks. The CSSF assesses the administrative structure of the securitisation undertaking on a case-by-case basis.

c. Managers and shareholders

The securitisation undertaking must notify the CSSF of the identity of the securitisation project's initiator in order for the CSSF to assess the quality and seriousness of the initiator.

The securitisation undertaking can be set up as an orphan company with, for instance, charity institutions as shareholders.

There must be at least three directors in a securitisation company or management company of a securitisation fund. The directors must be of good repute and have the adequate experience and means required for the performance of their duties. The CSSF accepts that the directors' mandates are given to legal persons exclusively. In such case, the CSSF assesses the criteria regarding the directors' competence and good repute at the level of the legal persons and at the level of the natural persons designated to represent the legal persons.

d. Custody of assets

Article 22 of the Law provides that *"authorised securitisation undertakings must entrust the custody of their liquid assets and securities with a credit institution established or having its registered office in Luxembourg".*

The Law does not introduce a specific regime for the custody of assets of authorised securitisation undertakings. Consequently, the credit institution that has been entrusted with the custody of the liquid assets and securities of a securitisation undertaking is not subject to any supervisory duty except the duty of proper safeguarding of the assets entrusted into custody.

An authorised securitisation undertaking may designate, for the custody of its assets, a different banking institution for every compartment.

The Luxembourg credit institution may entrust a third party with all or part of the liquid assets and securities deposited by the securitisation undertaking provided that it takes on the ultimate responsibility for the custody of these assets. Indeed, the Luxembourg credit institution's responsibility for the proper custody of the securitisation undertaking's assets is not affected by the fact that all or part of the assets it is safeguarding has been entrusted to a third party.

e. *Documents to be included in the approval file of a securitisation undertaking*

The request for approval must contain all the data necessary to its scrutiny. It must at least include the following elements:

- the articles of incorporation or the management rules of the securitisation undertaking or their drafts;
- the identity of the members of the board of directors of the securitisation undertaking or of its management company, as well as the identity of the other managers of the securitisation undertaking or of its management company, their *curriculum vitae* and an extract from their police record;
- the identity of the shareholders that are in a position to exercise a significant influence on the business conduct of the securitisation undertaking or of its management company and their articles of incorporation;
- the identity of the initiator and, where applicable, its articles of incorporation;
- information concerning the credit institution responsible for the custody of assets;
- information concerning the administrative and accounting organisation of the securitisation undertaking;
- the agreements or draft agreements with service providers;
- the identity of the external auditor;
- the draft documents relating to the first issue of securities or, for active securitisation undertakings, the agreements relating to the issue of securities and other documents relating to securities already issued.

The CSSF reserves the right to request any other information it deems necessary to review the authorisation file.

2.5. Prudential supervision

The prudential supervision exercised by the CSSF aims at ascertaining that the authorised securitisation undertakings comply with the law and their contractual obligations.

Any change to the articles of incorporation of the securitisation undertaking, to its managing body or its external auditor must be notified forthwith to the CSSF and is subject to the CSSF's prior approval. Any change in control of the securitisation company or management company is subject to the CSSF's prior approval.

As soon as they are available, securitisation undertakings must provide the CSSF with the following documents:

- a copy of the final issue documents for each issue of securities, irrespective of a possible prior notification of those documents to the CSSF within the scope of an offer to the public or an admission to trading;
- a copy of the financial reports drawn up by the securitisation undertaking for its investors and rating agencies, where applicable; and
- a copy of the annual reports and documents issued by the external auditor in the course of the audit of annual statements. In this context, the CSSF wishes to receive the management letter drawn up by the external auditor in the course of its audit, or where no such management letter has been issued, a written statement of the external auditor confirming that fact.

In addition, securitisation undertakings must provide the CSSF with the following documents on a half-yearly basis:

- a listing of the new issues of securities, of other outstanding issues and issues that matured during the period under review. This report must indicate for every issue the nominal amount issued and the nature of the securitisation transaction, the investor profile and, where applicable, the compartment concerned. In connection with every issue, information should be included regarding the initial issue price and the current market price (if available) of each outstanding issue, or on the redemption price of each matured issue, as well as information on any issues (or certain tranches of an issue) for which the securitisation undertaking was not able to realise the projected yield rate or to guarantee the final redemption price. In such cases, details on the effective yield or redemption value are to be indicated;
- a summary of the financial situation of the securitisation undertaking including notably a breakdown of its assets and liabilities, by compartment, where applicable;
- at the closing date of the financial year, a draft balance sheet and profit and loss account of the securitisation undertaking.

The CSSF may also require any other information or perform on-site inspections and review any document of a securitisation company, management company or credit institution in charge of safekeeping the assets of the securitisation undertaking so as to verify compliance with the provisions of the Law and the rules laid down in the articles of incorporation or management rules and securities issue agreements, as well as the accuracy of the information that have been communicated.

CHAPTER VI

SUPERVISION OF THE OTHER PROFESSIONALS OF THE FINANCIAL SECTOR

1. Developments in 2007 of the other professionals of the financial sector (PFS)
2. Prudential supervisory practice
3. Support PFS

1. DEVELOPMENTS IN 2007 OF THE OTHER PROFESSIONALS OF THE FINANCIAL SECTOR (PFS)

The following other professionals of the financial sector fall under the scope of the prudential supervision of the CSSF:

- PFS incorporated under Luxembourg law (the activities performed by these institutions in another EU/EEA Member State, by means of a branch or under the freedom to provide services, are also subject to the prudential supervision of the CSSF; certain aspects of the prudential supervision, in particular compliance with the rules of conduct for the provision of investment services to clients, fall under the competence of the supervisory authority of the host Member State[1]);
- branches of investment firms from non-EU/EEA countries;
- branches of PFS other than investment firms originating from EU/EEA or from non-EU/EEA countries.

The supervision of branches set up in Luxembourg by investment firms originating from another EU/EEA Member State is based on the principle of the supervision by the home Member State authority. Nevertheless, certain specific aspects of the supervision fall under the competence of the CSSF as supervisory authority of the host Member State[2].

The law of 13 July 2007 on markets in financial instruments (MiFID Law) transposing into Luxembourg law Directive 2004/39/EC of 21 April 2004 on markets in financial instruments, introduced a certain number of amendments, effective as from 1 November 2007, to the law of 5 April 1993 on the financial sector, as amended.

One of the objectives of the new law was to review certain PFS statuses based on the new requirements arising from Directive 2004/39/EC as well as on the CSSF's experience in exercising its supervisory mission.

New PFS statuses have thus been introduced into the law of 5 April 1993 on the financial sector, as amended, i.e. financial intermediation firms, investment firms operating an MTF (multilateral trading facility) in Luxembourg and operators of a regulated market authorised in Luxembourg. The first two categories are classified as investment firms and consequently benefit from the European passport.

The denomination and/or definition of certain existing PFS categories have been amended by the MiFID Law. Registrar and transfer agents, now denominated registrar agents, and professional custodians of financial instruments have been switched from the investment firms category to the category "PFS other than investment firms", thereby losing the benefit of the European passport.

Other statuses have been transferred from the category "PFS other than investment firms" to the category "investment firms". This was the case for investment advisers, brokers in financial instruments and market makers, which now benefit from the European passport.

A differentiation at the level of the activity of IT systems and communication networks operators of the financial sector implied a split of this category into two new statuses, i.e. primary IT systems operators of the financial sector and secondary IT systems and communication networks operators of the financial sector.

[1] In accordance with the law of 13 July 2007 on markets in financial instruments transposing into Luxembourg law Directive 2004/39/EC on markets in financial instruments.

[2] Idem.

Moreover, the MiFID Law decreased the initial capital requirements applicable to PFS to the minimum thresholds provided for in Directive 2006/49/EC of 14 June 2006 on the capital adequacy of investment firms and credit institutions.

Summary of the PFS categories referred to in Part I, Chapter 2, Section 2 of the law of 5 April 1993, as amended by the MiFID Law of 13 July 2007

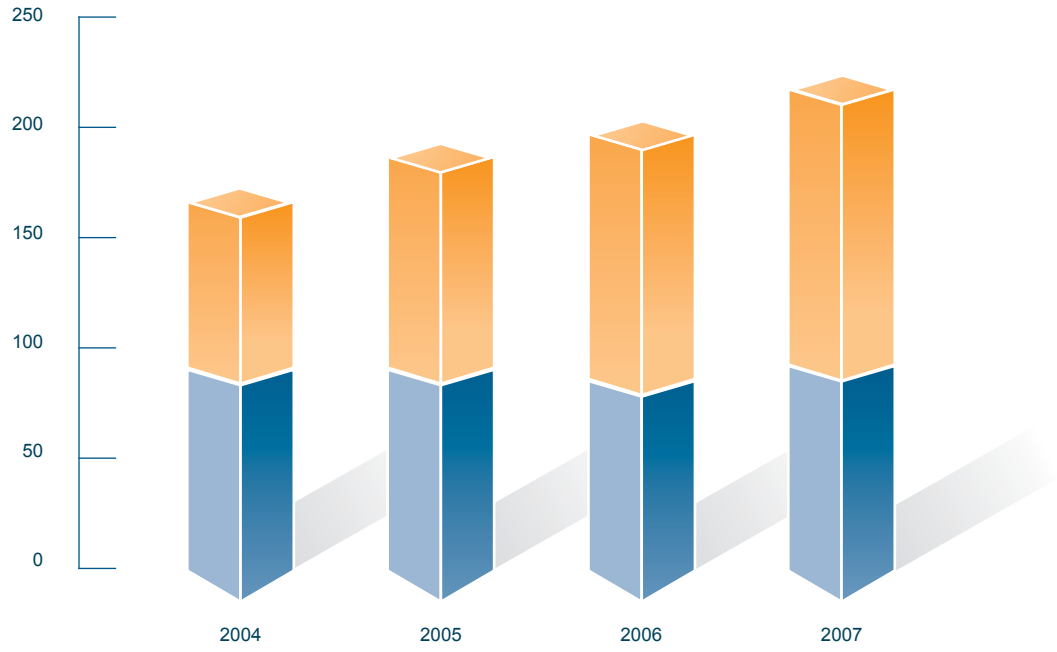
Investment firms	Article of the law
Investment advisers	24
Brokers in financial instruments	24-1
Commission agents	24-2
Private portfolio managers	24-3
Professionals acting for their own account	24-4
Market makers	24-5
Underwriters of financial instruments	24-6
Distributors of units/shares of UCIs	24-7
Financial intermediation firms	24-8
Investment firms operating an MTF in Luxembourg	24-9
Certain PFS other than investment firms	
Registrar agents	25
Professional custodians of financial instruments	26
Operators of a regulated market authorised in Luxembourg	27
Operators of payment or securities settlement systems	28-1
Currency exchange dealers	28-2
Debt recovery	28-3
Professionals performing credit offering	28-4
Professionals performing securities lending	28-5
Professionals performing money transfer services	28-6
Administrators of collective savings funds	28-7
Management companies of non-coordinated UCIs	28-8
PFS carrying out a connected or complementary activity to the financial sector	
Domiciliation agents of companies	29
Client communication agents	29-1
Administrative agents of the financial sector	29-2
Primary IT systems operators of the financial sector	29-3
Secondary IT systems and communication networks operators of the financial sector	29-4
Professionals performing services of setting up and management of companies	29-5

1.1. Development in the number of the other professionals of the financial sector

The continuous interest in the Luxembourg financial centre was confirmed by the positive development in the number of PFS under the prudential supervision of the CSSF. The year 2007 reasserted the rising trend already registered in the previous years with an increase in the number of financial actors still higher than in 2006. The interest, even though less pronounced, for PFS categories performing a connected or complementary activity to the financial sector cristallised for the second consecutive year, many entities authorised during the last 12 months having opted for one of these statuses.

The number of PFS thus rose from 196 entities as at 31 December 2006 to 215 as at 31 December 2007. The number of entities having been authorised in 2007 is the same as the number of entities having been authorised in the previous year (29 companies in 2007 as in 2006). Ten entities abandoned their PFS status in 2007, a decreasing figure as compared to the 18 status withdrawals in 2006.

Development in the number of PFS



	2004	2005	2006	2007
Investment firms	90	88	85	92
Other PFS	76	97	111	123
Total	**166**	**185**	**196**	**215**

The breakdown of PFS in investment firms and other PFS shows that the positive trend in the total number of PFS was closely linked to the new authorisations of other PFS, which show a continuous growth since 2004. The number of investment firms, on the other hand, remained more or less stable over the past years.

This development shows the growing interest in the activities of PFS other than investment firms and in activities connected or complementary to a financial sector activity, which gain in importance in the financial centre.

Breakdown of PFS by geographical origin

Country	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Belgium	25	24	21	22	22	18	21	23	28	32
France	10	10	11	14	13	9	12	12	12	14
Germany	6	7	11	11	10	10	10	13	18	20
Luxembourg	12	17	22	31	31	32	48	56	66	72
Netherlands	3	3	7	12	15	15	18	19	17	18
Switzerland	4	4	7	11	10	10	10	12	11	11
United Kingdom	9	8	8	9	10	11	8	8	8	8
United States	4	3	4	8	8	8	11	13	12	13
Others	10	14	22	27	26	29	28	29	24	27[3]
Total	**83**	**90**	**113**	**145**	**145**	**142**	**166**	**185**	**196**	**215**

The upward trend in the number of Luxembourg PFS continued, rising from 66 entities as at 31 December 2006 to 72 entities as at 31 December 2007. The regular growth registered over the past years allowed Luxembourg entities to still represent a large majority of entities.

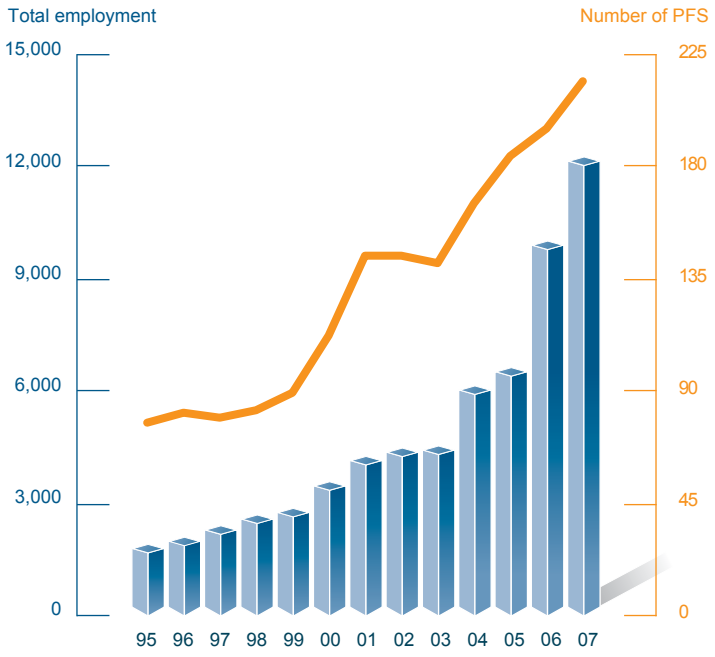
The interest in the Luxembourg financial centre at international level and, more specifically, in the neighbouring countries was confirmed in 2007. Belgian PFS recorded a growth of four entities, whereas German and French PFS increased by two entities each.

1.2. Development in employment of the other professionals of the financial sector

The year 2007 was again characterised by an increase in employment, though less important than in 2006. Indeed, the number of people employed rose from 9,928 as at 31 December 2006 to 12,174 as at 31 December 2007, which represents an annual growth of 22.62%. This positive development is only partially attributable to PFS newly registered on the official list. Rather, it is the increase of people employed with PFS already active before 2007 that explains the total growth in the number of staff. Indeed, with the exception of around twenty entities which show a slight decline in their employment figures, a general employment growth was registered with these PFS in 2007. Certain entities active in the investment funds field recruited massively.

Summary of employment per year and compared to the development in the number of PFS

Year	Number of PFS	Total employment
1995	78	1,827
1996	82	2,017
1997	80	2,323
1998	83	2,612
1999	90	2,788
2000	113	3,499
2001	145	4,176
2002	145	4,399
2003	142	4,455
2004	166	6,059
2005	185	6,547
2006	196	9,928
2007	**215**	**12,174**



[3] of which Italy (4 entities), Sweden (4 entities), Denmark (3 entities).

Considering the development in staff numbers during the year under review, a growth of 367 people in the first quarter and an increase by 417 people in the second quarter could be registered, bringing the total employment for PFS to 10,712 as at 30 June 2007. This progression in the first half-year can be essentially explained by the increase of the employment with several PFS performing tasks in the investment funds sector and, to a lesser extent, by the authorisation of new PFS during this same period.

In the second half-year, a more substantial rise in the number of staff employed by PFS was registered, rising from 10,712 people as at 30 June 2007 to 11,783 people as at 30 September 2007 and reaching 12,174 people as at 31 December 2007. Newly authorised PFS during the second half-year as well as an increase in employment for existing PFS explain this development. Personnel have been recruited mainly by certain support PFS and by several traditional PFS operating in the UCI field, in particular through the transfer agent and central administration activities.

1.3. Changes in the official list of PFS in 2007

1.3.1. Luxembourg PFS having started their activities in 2007

- ***Investment firms and other PFS*** (except PFS with only one or several support PFS statuses, as referred to in articles 29-1, 29-2, 29-3 and 29-4 of the law on the financial sector; support PFS have been considered in a distinct table)

Name of the PFS	Start of business
AB Fund Consulting S.à r.l.	August 2007
Access Partners S.A.	March 2007
AZTEC Financial Services (Luxembourg) S.A.	October 2007
BISA S.A.	July 2007
Carey S.A.	February 2007
Elite Advisers S.A.	April 2007
GIP Invest S.A.	January 2007
GPB Asset Management S.A.	July 2007
HSH Financial Markets Advisory	November 2007
Intruma Administrations (Luxembourg) S.à r.l.	March 2007
Luxembourg Financial Group A.G.	April 2007
Maples Finance Luxembourg S.A.	February 2007
Mutualité d'Assistance aux Commerçants S.C.	November 2007
Nobis Asset Management S.A.	June 2007
Sireo Financial Services S.A.	March 2007
Smart Private Managers (Luxembourg) S.A.	March 2007
Société de la Bourse de Luxembourg S.A.	November 2007
Société Générale d'Arbitrages et de Participations (SGAP) Luxembourg S.A.	April 2007
Structured Finance Management (Luxembourg) S.A.	February 2007
Telecom Italia LAB S.A.	March 2007
Vectis PSF S.A.	March 2007

It should be noted that institutions cumulating one or more support PFS statuses with one or more other PFS statuses are included in the table above.

- ***Support PFS***

Support PFS are PFS authorised only as client communication agent (article 29-1 of the law of 5 April 1993 on the financial sector, as amended), administrative agent of the financial sector (article 29-2), primary IT systems operator of the financial sector (article 29-3) or secondary IT systems and communication networks operator of the financial sector (article 29-4), excluding any other PFS status. Entities cumulating one or several of those four statuses are also considered as support PFS. This support PFS grouping allows to better consider the specificities of these activities and their importance in the financial sector.

During 2007, the following support PFS started their activities:

Name of the PFS	Start of business
CSC Computer Sciences Luxembourg S.A.	June 2007
Econocom PSF S.A.	July 2007
EMC Luxembourg PSF S.à r.l.	January 2007
Express Services S.A.	May 2007
Faber Digital Solutions S.A.	January 2007
Guidance S.A.	September 2007
SIT PSF S.A.	January 2007
Verizon Business Security Solutions Luxembourg S.A.	March 2007

1.3.2. PFS having abandoned their status in 2007

Ten institutions, of which four investment firms, abandoned their PFS status in 2007 for the following reasons:

- change or cessation of activities, no longer requiring an authorisation as PFS as not falling anymore under the scope of application of the law of 5 April 1993 on the financial sector, as amended

  Mr. Jean-Paul Frisch

  KBC Conseil-Service S.A.

  Stradivari Advisors S.A.

  Telecom Italia LAB S.A.

  Mr. Tommy Schank

- liquidation

  LGT Trust & Consulting S.A.

  Sogen Finance Luxembourg S.A.

- conversion into management company

  Creutz & Partners, Global Asset Management S.A.

- merger

  IKB Financial Products S.A. (merger with IKB International S.A., bank incorporated under Luxembourg law)

- conversion into a branch active in Luxembourg

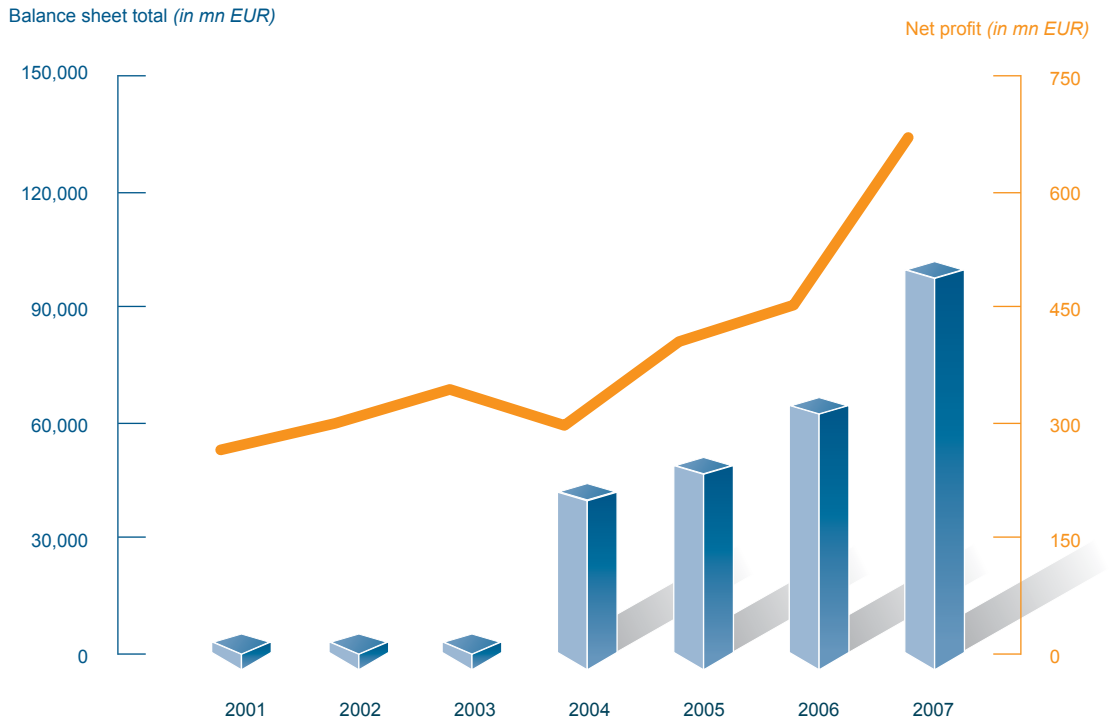
  Tullett Prebon (Luxembourg) S.A.

1.4. Development of balance sheets and profit and loss accounts

As at 31 December 2007, the balance sheet total of PFS established in Luxembourg (215 entities as at 31 December 2007) reached EUR 107,703 million as compared to EUR 69,854 million as at 31 December 2006, representing an increase of 54.18%. This substantial increase was mainly linked to the substantial growth in the business volume of the institution authorised as professional performing securities lending. The positive variation in the number of PFS during the year, rising from 196 entities as at 31 December 2006 to 215 entities as at 31 December 2007, represented another factor explaining, though to a lesser extent, the increase in the balance sheet total over a twelve-month period.

The growth in the balance sheet total in 2007 goes together with an increase in the financial players' net profit. Net profit thus reached EUR 715.7 million as at 31 December 2007 against EUR 483.9 million as at 31 December 2006, representing a considerable growth of 47.90% over one year. This positive development mainly results from the high profitability of an important player operating as professional custodian of financial instruments. Professionals acting for their own account and the PFS newly authorised in 2007 also contributed to the overall profit increase for all PFS over one year.

Year	Balance sheet total (in mn EUR)	Net profit (in mn EUR)
2001	2,316	283.52
2002	2,292	320.23
2003	2,482	367.17
2004	45,131	317.37
2005	53,421	433.34
2006	69,854	483.90
2007	107,703	715.70



1.5. Expansion of PFS at international level

- ***Subsidiaries created during 2007 involving a consolidation***

The investment firm HSH Investment Management S.A., authorised to perform the activities as private portfolio manager, commission agent, broker in financial instruments and investment adviser, opened a subsidiary in the United States of America in 2007.

- ***Freedom of establishment***

In 2007, seven investment firms incorporated under Luxembourg law established a branch in one or more EU/EEA countries based on the freedom of establishment.

Name of the PFS	Country of branch location
Farad Investment Advisor S.A.	Italy
Fidessa Asset Management S.A.	Netherlands
HSH Financial Markets Advisory	Germany
HSH Investment Management S.A.	Germany, United Kingdom
Luxembourg Financial Group A.G.	United Kingdom
Rhein Asset Management (Lux) S.A.	Germany
Vontobel Europe S.A.	Spain, United Kingdom

Notz, Stucki Europe S.A. closed its branch in Italy in 2007 and is no longer registered on the list of investment firms incorporated under Luxembourg law having a branch in one or several EU/EEA countries (see below). Following its conversion into a management company in 2007, Creutz & Partners, Global Asset Management S.A. is no longer registered either.

Having no longer the status of investment firm as a consequence of the amendment to the law of 5 April 1993 on the financial sector by the law of 13 July 2007 on markets in financial instruments, Clearstream International S.A. is no longer registered as an investment firm with a branch abroad.

As at 31 December 2007, the following Luxembourg investment firms were represented in one or several EU/EEA countries by means of a branch:

Name of the PFS	Country of branch location
BNP Paribas Fund Services, in abbreviated form "BPFS"	Spain
Compagnie Financière et Boursière Luxembourgeoise S.A., in abbreviated form "Cofibol"	Belgium
Createrra S.A.	Belgium
European Fund Services S.A.	Germany, Ireland
Fidessa Asset Management S.A.	Netherlands
Foyer Patrimonium S.A.	Belgium
Farad Investment Advisor S.A.	Italy
HSH Financial Markets Advisory	Germany
HSH Investment Management S.A.	Germany, United Kingdom
IAM Strategic S.A.	Sweden
Luxembourg Financial Group A.G.	United Kingdom
Moventum S.C.A.	Germany

Name of the PFS	Country of branch location
Rhein Asset Management (Lux) S.A.	Germany
SZL S.A.	Belgium
Vontobel Europe S.A.	Germany, Austria, Italy, Spain, United Kingdom
WH Selfinvest S.A.	Belgium

As regards non-EU/EEA countries, one investment firm incorporated under Luxembourg law, namely Privalux Management S.A., is represented through a branch in Switzerland.

It should be further added that three PFS which are not investment firms were registered by means of a branch in an EU/EEA country as at 31 December 2007.

The number of branches established in Luxembourg by investment firms originating from another EU/EEA Member State registered an important positive development in 2007, counting eleven entities as at 31 December 2007 against six entities as at 31 December 2006. Indeed, five branches of UK origin started their activities in Luxembourg during 2007, namely AIG Investments Europe Ltd, Eiger Securities LLP, Nevsky Capital LLP, Thames River Capital LLP and Tullet Prebon (Europe) Ltd.

Name of the branch	Country of origin
Aberdeen Asset Managers Limited	United Kingdom
AIG Investments Europe Ltd	United Kingdom
Eiger Securities LLP	United Kingdom
Gadd Capital Management Ltd	Gibraltar
Mellon Fund Administration Limited	Ireland
Morgan Stanley Investment Management Limited	United Kingdom
Nevsky Capital LLP	United Kingdom
PFPC International Limited	Ireland
T. Rowe Price Global Investment Services Limited, in abbreviated form "TRPGIS"	United Kingdom
Thames River Capital LLP	United Kingdom
Tullett Prebon (Europe) Ltd	United Kingdom

- ***Freedom to provide services***

In 2007, thirteen investment firms incorporated under Luxembourg law requested to carry on their activities in one or several EU/EEA countries by way of free provision of services. The total number of investment firms active, following a notification, in one or more EU/EEA countries amounted to 42 entities as at 31 December 2007. The majority of the investment firms concerned performed their activities in several EU/EEA countries by way of free provision of services.

The total number of investment firms established in the EU/EEA and authorised to perform activities under the freedom to provide services within the Luxembourg territory amounted to 1,410 entities as at 31 December 2007 (against a total of 1,175 entities as at 31 December 2006).

As at 31 December 2007, the global situation relating to free provision of services in or from the EU/EEA was as follows:

Country	Luxembourg investment firms providing services in the EU/EEA	EU/EEA investment firms providing services in Luxembourg
Austria	9	31
Belgium	27	16
Bulgaria	-	-
Cyprus	1	10
Czech Republic	2	-
Denmark	6	10
Estonia	-	-
Finland	5	4
France	18	62
Germany	22	45
Gibraltar	-	2
Greece	2	6
Hungary	2	-
Iceland	1	-
Ireland	3	40
Italy	13	7
Latvia	1	-
Liechtenstein	1	2
Lithuania	2	-
Malta	-	1
Netherlands	15	70
Norway	4	24
Poland	3	-
Portugal	3	3
Romania	-	-
Slovakia	1	-
Slovenia	1	2
Spain	11	9
Sweden	8	14
United Kingdom	8	1,052
Total number of notifications	**169**	**1,410**
Total number of investment firms concerned	**42**	**1,410**

The geographical breakdown of EU/EEA investment firms active by way of free provision of services in Luxembourg reveals that UK investment firms are by far the most important in number. Similarly, among the 369 new notifications for free provision of services on the Luxembourg territory received in 2007 (increasing number as compared to the 127 notifications in 2006), those originating from the United Kingdom represented a large majority. An important number of notifications by UK investment firms was received when Directive 2004/39/EC on markets in financial instruments came into force on 1 November 2007. This development can be explained by a review of the activities and/or policy by the UK entities concerned.

The United Kingdom is followed by countries close to Luxembourg: the Netherlands, France and Germany. A certain number of investment firms established in Nordic countries, such as Norway, Sweden and Ireland, also showed an interest in exercising their activities in Luxembourg by way of free provision of services.

The target countries of investment firms incorporated under Luxembourg law, whose total number of notifications amounted to 169 as at 31 December 2007, are Luxembourg's neighbouring countries (Belgium, Germany and France). The Netherlands and Italy follow closely with 15 and 13 notifications, respectively, for the free provision of services on their territory. The interest shown by Luxembourg investment firms to provide services in the new EU Member States is still limited.

2. PRUDENTIAL SUPERVISORY PRACTICE

The aspects of the prudential supervisory practice concerning support PFS, i.e. PFS that are authorised only as client communication agents (article 29-1 of the law of 5 April 1993 on the financial sector, as amended), administrative agents of the financial sector (article 29-2), primary IT systems operators of the financial sector (article 29-3) or secondary IT systems and communication networks operators of the financial sector (article 29-4), excluding any other status, are described under point 3 below.

2.1. Instruments of prudential supervision

Prudential supervision is exercised by the CSSF by means of four types of instruments:

- financial information to be submitted periodically to the CSSF enabling it to continuously monitor the activities of PFS and the inherent risks, as well as the periodic control of capital ratios pursuant to article 56 of the law of 5 April 1993 on the financial sector, as amended;
- the annual report drawn up by the external auditor (including a certificate relating to the fight against money laundering and a certificate concerning compliance with the rules of conduct in the financial sector; as regards investment firms, the auditors' report shall moreover include a description and a comment on the Compliance function in accordance with circular CSSF 04/155);
- the internal audit reports relating to audits carried out during the year and the management's report on the state of the internal audit of the PFS;
- on-site inspections carried out by the CSSF.

2.2. On-site inspections

The CSSF attaches particular importance to this instrument of continuous supervision, as it allows a global and direct view of the situation and functioning of the PFS in practice.

In 2007, the CSSF carried out six on-site inspections in relation to five PFS incorporated under Luxembourg law.

The purpose of one on-site inspection was to make sure that adequate documentation relating to the holdings of the PFS was available on its premises and to assess its inherent risks.

Two on-site inspections at one PFS were carried out in relation to a specific UCI sub-fund for which the concerned PFS exercises the central administration function.

The CSSF carried out an on-site inspection at a securitisation undertaking subject to its supervision and domiciled with a PFS. The inspections concerned, among other things, the administrative and accounting organisation of the securitisation undertaking.

The controls carried out at a further PFS were more specifically linked to the validation of the models used by another entity of the group for the credit risk calculation through the internal ratings-based approach. The entity not being operational, the CSSF reviewed the operational aspects of the management and internal ratings systems of exposures at the PFS level.

It should also be noted that a management interview has taken place at a PFS in the context of the preparation of an international meeting in relation to the prudential process implementation provided for by "Pillar 2" (2nd pillar of the three-pillar structure of the new solvency standards, commonly known as "Basel II", proposed by the Basel Committee on banking supervision in November 2005).

2.3. Meetings

151 meetings related to the activities of professionals of the financial sector were held at the CSSF's premises during the year under review.

Most of these meetings were held in the context of applications for approval as PFS, submitted either by companies newly incorporated or to be incorporated, or by existing entities that intend to carry out financial activities requiring prior approval. This figure also includes the meetings that were held with entities enquiring whether the activities performed fall under the scope of the law of 5 April 1993 on the financial sector, as amended. The major part of these meetings concerned the legal qualification or requalification of the activities performed, in the context of the amendment of the law on the financial sector by the law of 13 July 2007 on markets in financial instruments.

The remainder of the meetings covered the following areas in particular:

- planned changes notably relating to business activities, shareholders and daily management;
- presentation of the general context and activities of the companies concerned;
- requests for information within the scope of the prudential supervision carried out by the CSSF;
- courtesy visits.

2.4. Specific controls

Article 54(2) of the law of 5 April 1993 on the financial sector, as amended, entitles the CSSF to require external auditors to carry out a specific audit at a financial professional, covering one or several specific aspects of the business or operation of the entity concerned. The ensuing costs are to be borne by the professional concerned. The CSSF has not made formally use of this right in 2007.

2.5. Supervision on a consolidated basis

The supervision of investment firms on a consolidated basis is governed by the law of 5 April 1993 on the financial sector, as amended, and in particular by Chapter 3a of Part III. The relevant articles define the conditions governing the supervision of investment firms on a consolidated basis and its scope. The form, extent, content and means of supervision on a consolidated basis are also laid down therein.

The CSSF carries out supervision on a consolidated basis for investment firms falling under the scope of application of the above-mentioned law. An in-depth study of the financial groups to which most PFS investment firms belong was required in order to determine whether, at what level and in what form, consolidation should apply. For the investment firms concerned, circular CSSF 00/22 on the supervision of investment firms on a consolidated basis specifies the practical aspects of the rules as regards this type of supervision. Many companies supervised on a consolidated basis belong to major groups operating in the financial sector and whose ultimate parent company is usually a credit institution.

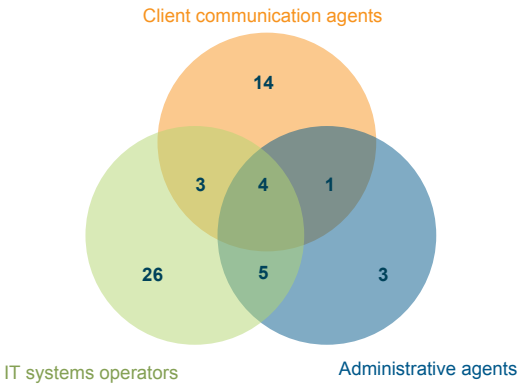
3. SUPPORT PFS

Support PFS include financial professionals which have been authorised only under articles 29-1, 29-2, 29-3 or 29-4 of the law of 5 April 1993 on the financial sector, as amended. The term "support" has been defined by the market in agreement with the CSSF. One characteristic of support PFS is that they do not receive deposits from the public and act mainly as subcontractor of operational functions on behalf of other financial professionals.

The number of support PFS did not substantially change in 2007 with only eight entities authorised during the year, i.e.:

- two client communication agents (ACC);
- five IT systems and communication networks operators (OSIRC);
- one entity cumulating the status as administrative agent (AA), client communication agent (ACC) and IT systems and communication networks operator (OSIRC).

As at 31 December 2007, 55 entities cumulating 73 different statuses were active, distributed as follows:



The relatively modest development in the number of support PFS at the beginning of 2007 originates from the changes expected in the law of 5 April 1993 in the financial sector, as amended, during the year and finally entered into force on 1 November 2007. The perspective of a change in legal conditions (with a substantial reduction of capital requirements, the abrogation of the exclusivity condition, a new status as secondary IT systems and communication networks operator of the financial sector (OSIS) and the inclusion of service provision to insurance and reinsurance undertakings) has certainly reduced the applications for obtaining new authorisations before this date. This has been confirmed at the end of the year, when the number of authorisation requests sharply rose. This trend should moreover be confirmed in 2008.

3.1. Major events in 2007

The law of 13 July 2007 not only transposed the MiFID Directive but it also amended the law of 5 April 1993 on the financial sector in relation to the capital requirements and statuses applicable to support PFS. The major amendments affecting support PFS are the following:

- split of the status of IT systems and communication networks operator of the financial sector (OSIRC) into two new statuses, i.e. primary IT systems operator of the financial sector (OSIP) (new article 29-3) and secondary IT systems and communication networks operator of the financial sector (OSIS) (new article 29-4);

- withdrawal of article 29-3(2) on the operator's exclusive service provision to the financial sector; OSIP and OSIS are now authorised to contract, for service provision, with firms outside the financial sector;
- reduction in the capital required to EUR 370,000 for OSIP and EUR 50,000 for OSIS (formerly EUR 1,500,000 for OSIRC);
- IT systems and communication networks operators of the financial sector authorised under the former article 29-3 at the entry into force of the law of 13 July 2007 fully benefited from the status as primary IT systems operators of the financial sector.

3.2. Creation of the department "IT and support PFS supervision"

The increasing number of entities having opted for a support PFS status over the last years, the specificity of their business and the particular competence which is required for their supervision have led the CSSF to create the department "IT and support PFS supervision" on 1 January 2007. The new department cumulates the competences previously jointly performed by the "IT audit" function and the department "Supervision of the other professionals of the financial sector".

The department "IT and support PFS supervision" remains in charge of the prudential supervision of IT systems, whose major events of 2007 are set out in Chapter VIII "IT systems supervision" of this Annual Report.

3.3. Compliance improvements: setting up of internal control

The new tasks of the department and the specificity of the entities to be supervised have led it to re-focus the entities' supervision on a more operational than financial aspect. In this context, the department focuses, and will further focus, more specifically on the importance of the implementation of an adequate internal control environment (in compliance with circular CSSF 98/143).

This approach aims at an improved mastery of the activities performed by the supervised entities and, despite the non-negligible cost such an implementation might generate, it allows PFS to improve their risk management, as well as the quality and mastering of the services offered, by distinguishing themselves from their competitors.

3.4. Development of prudential supervision

Given the considerable widening of the range of activities provided by support PFS to sectors which do not necessarily depend from the financial industry due to the abrogation of the exclusivity condition to this sector, the CSSF is currently thinking on focussing the prudential supervision more precisely on services provided to the sector under its supervision. To this end, the supervision could be directed towards an approach based on the risks generated towards the financial sector (risk based approach). The details of this prudential supervision development should be available in 2008 after market consultation.

3.5. Merger of entities

The abrogation of the exclusive service provision condition to the financial sector for IT systems and communication networks operators led several PFS to consider the merger of the entities located in Luxembourg. To this end, it should be noted that the law of 10 August 1915 on commercial companies is applicable in the case of a merger between two entities, of which one is authorised as support PFS. In this case, it is important for the merger to be made under the regime of the merger by takeover (Section XIV, sub-section 1), the support PFS taking over the company not authorised as PFS, in order to ensure the continuity of the authorisation based on the law relating to the financial sector.

Moreover, the takeover of the non-PFS must not create any issues at the level of the continuous compliance with the PFS licence conditions. The merger shall not influence the quality nor introduce risks at the level of the services provided to entities of the financial sector.

3.6. Use of cash pooling

Certain PFS belonging to an international group use their group's cash pooling function in order to manage their surplus cash position. It should be noted that, although such practice is not prohibited, the PFS shall, at any time, be able to provide evidence of an own capital base of an amount which is higher or equal to the capital requirement. The use of cash pooling can thus only be possible for the part of liquidity exceeding this amount. Moreover, the amount of this cash pooling shall appear in the monthly reporting under the heading 3.3.4 "Loans to/amounts owed to undertakings affiliated (or with which the company is linked by virtue of a participating interest)" and not under the heading 4.3 "Debtors", which shall be considered for commercial debts.

CHAPTER VII

SUPERVISION OF SECURITIES MARKETS

1. Reporting of transactions in financial instruments
2. Supervisory practice
3. Developments in the regulatory framework

1. REPORTING OF TRANSACTIONS IN FINANCIAL INSTRUMENTS

1.1. Obligation to report transactions in financial instruments

Following the entry into force of the law of 13 July 2007 on markets in financial instruments ("MiFID Law") transposing, among others, Directive 2004/39/EC of 21 April 2004 on markets in financial instruments ("MiFID Directive"), a new reporting regime for transactions in financial instruments is applicable as from 1 November 2007.

The main legal framework of this new regime is set down in Luxembourg by article 28 of the MiFID Law and by Chapter III (Transaction reporting) of Regulation (EC) No 1287/2006 of 10 August 2006 implementing the MiFID Directive ("Regulation (EC) No 1287/2006"). Article 28 of the MiFID Law, which transposes article 25 of the MiFID Directive, specifies the obligation for credit institutions and investment firms to report to the CSSF the transactions carried out in financial instruments admitted to trading on a regulated market of the European Economic Area. These arrangements are completed by the more detailed implementing measures of Regulation (EC) No 1287/2006 which clarify in particular the definition of transaction and specify the content and form of the reports.

The new regime of the MiFID Directive also introduces a regime for the exchange of information on transactions between the relevant competent authorities so as to enable these authorities to perform their supervisory tasks. As such, the CSSF makes available to the competent authority of the most relevant market in terms of liquidity for a specific financial instrument the information relating to the transactions in this financial instrument that have been reported to it. Likewise, the CSSF transmits the information received from the Luxembourg branches of credit institutions and investment firms authorised in another Member State to the home Member State authority. The exchange of this information is organised through the TREM system (Transaction Reporting Exchange Mechanism) implemented by the Committee of European Securities Regulators (CESR) according to the format and the methods set out for this purpose.

The application of the reporting requirements is defined in circular CSSF 07/302 of 17 July 2007. This circular, which repeals circular CSSF 99/7 of 27 December 1999 and circular letter of 23 May 2001, provides further details on:

- the persons subject to the reporting obligation and the competent authority to receive reports from branches;
- the transactions falling within the scope of the reporting obligation, specifying in particular the definition of transaction and execution;
- the types of financial instruments concerned by the reporting obligation;
- the content and form of the reports, including a description of the fields of Table 1 of Annexe I to Regulation (EC) No 1287/2006 and of the standard identification codes which are mandatory for reporting purposes;
- the methods and arrangements for the transmission of the reports which shall be made only in an electronic form;
- the time limit for transaction reporting and safekeeping of transaction-related data.

The circular also considers the CESR guidelines ("CESR Level 3 Guidelines on MiFID Transaction reporting" published on 29 May 2007, reference CESR/07-301) on reporting requirements of branches pursuant to article 32(7) of the MiFID Directive, the definition of execution of a transaction for the purposes of reporting and the process for approval of reporting systems already authorised in another Member State.

The new reporting regime presents a major difference as compared to the previous regime due to the fact that only transactions where the credit institutions and investment firms execute transactions directly with an execution venue (i.e. a regulated market, an MTF, a systematic internaliser, or a market maker or other liquidity provider, or an entity that performs, in a third country, similar functions to the functions performed by any of the foregoing) and/or conclude transactions on their own account, must be reported. Hence, certain entities subject to the reporting obligation under the previous regime will no longer or to a lesser extent be subject to the reporting obligation under the new regime considering their transaction execution procedures.

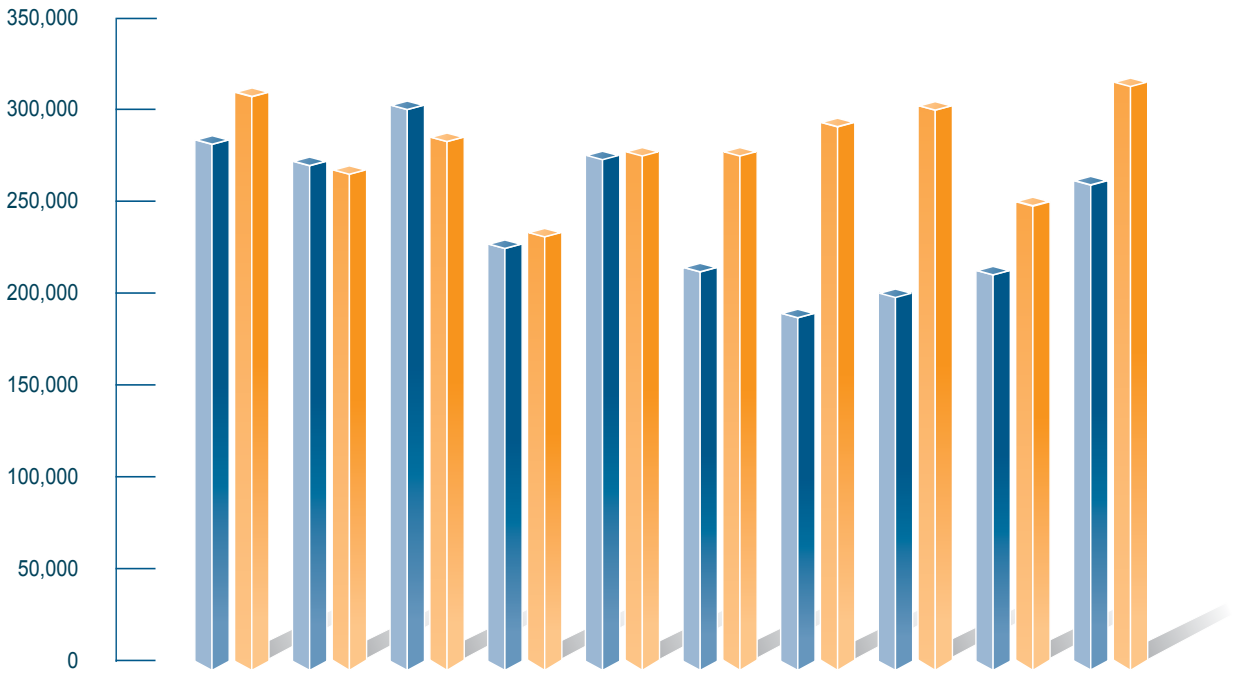
Finally, the technical arrangements relating, among others, to the electronic file format (XML) as well as to the transmission channels and the certificates to be used when sending files to the CSSF are described in detail in the *Recueil d'instructions TAF* now called "Transaction in Financial Instruments Reporting (TAF) – Electronic Reporting Instructions" which has been introduced by circular CSSF 07/306 of 27 July 2007. Circular CSSF 08/334 of 4 January 2008 details the encryption specifications. Due to the extent of the technical modifications required in the existing transaction reporting systems, a transition period for the compliance of these systems with the new requirements has been defined.

In order to ensure the implementation of the new requirements, the CSSF sent, at the end of September 2007, a questionnaire on the entry into force on 1 November 2007 of the transaction reporting in financial instruments under the MiFID Law to the institutions subject to the reporting obligation. Institutions had to provide details on their activities and procedures of execution related to transactions in financial instruments, the date of implementing a reporting system compliant with the MiFID Law as well as details on the progress of the project. After having evaluated the replies to the questionnaires and referring to the feedback received from the institutions, the CSSF published in the first quarter of 2008 a circular letter including a first set of Frequently Asked Questions providing clarifications on certain regulatory provisions and reminding the institutions of their responsibility to comply with the implementation deadline for a transaction reporting system compliant with the MiFID Law.

1.2. Development in the number of trades reported

The number of trades reported between 1 January and 31 October 2007, i.e. compliant with the provisions applicable before the entry into force on 1 November 2007 of the new requirements of the MiFID Law, amounted to 2,805,443 against 2,433,759 trades reported for the same period in 2006.

Monthly volume of trades reported



	January	February	March	April	May	June	July	August	September	October
2006 (1.1-31.10)	283,178	272,482	302,355	226,738	275,124	214,479	189,348	200,388	210,239	259,428
2007 (1.1-31.10)	307,132	267,509	284,948	232,603	277,516	277,949	293,124	302,134	250,007	312,521

Breakdown of transactions by type of instrument

Type of instrument	**Number of transactions reported** *(as a % of the total)*	
	2006 (1.1-31.10)	2007 (1.1-31.10)
Shares	70.49%	74.20%
Bonds	23.75%	18.90%
Futures	1.00%	1.70%
Options	1.97%	2.00%
Warrants	2.79%	3.20%

The reported data allow to monitor the trends of the European markets and more particularly the Luxembourg market. The main purpose of the supervision of the securities markets is to prevent and detect infringements of financial and stock market laws and regulations. In this context, monthly internal reports, as well as specific internal reports, based on the trades reported, are drawn up. These *ex post* analyses of transactions on financial instruments can be used as a starting point for inquiries of the CSSF.

2. SUPERVISORY PRACTICE

2.1. Supervision of stock exchanges

Until the entry into force on 1 November 2007 of the MiFID Law, the establishment of a stock exchange in Luxembourg was subject to a concession to be granted by Grand-ducal decree. The only company licensed under Luxembourg law was the *Société de la Bourse de Luxembourg S.A.* ("SBL"). The SBL still operates a first market named "*Bourse de Luxembourg*" (Luxembourg Stock Exchange) which is a "regulated market" within the meaning of the European Directives and a second market called "Euro MTF", the operating rules of which are defined in the Rules and Regulations of the SBL. These Rules and Regulations have been amended with effect from 1 November 2007 to take into account in particular the MiFID Law. The CSSF had been informed beforehand of the amendment to the operating rules of the markets operated by the SBL. This new version of the Rules and Regulations thus replaced the version approved by ministerial order dated 2 April 2007 and entered into force on 1 November 2007.

Upon the entry into force of the MiFID Law, the establishment of a regulated market in Luxembourg is subject to a written authorisation of the Minister responsible for the CSSF. The authorisation as regulated market is granted upon written request by the market operator and upon scrutiny by the CSSF of the conditions required under Chapter I of Title I of the MiFID Law. In accordance with the authorisation conditions, the operator of the regulated market and the systems of the regulated market must comply with the requirements of the MiFID Law, and the regulated market must have its registered office or, where applicable, its central administration in Luxembourg. The acts relating to the organisation and operation of the regulated market are supervised by the CSSF.

The regulated markets for which Luxembourg is the home Member State and which are not legal persons themselves must be operated by a market operator which, if established in Luxembourg, must obtain an authorisation in Luxembourg as "PFS other than an investment firm" according to the authorisation procedure provided for in the law of 5 April 1993 on the financial sector, as amended. Indeed, the new article 27(1) of this law introduces and defines a new PFS category.

The MiFID Law adds the operation of a multilateral trading facility ("MTF") to the list of investment services and activities in accordance with the MiFID Directive it transposes. Indeed, the emergence of a new generation of organised trading systems alongside regulated markets gave rise to the demand, at European level, for a certain legal framework similar to that of regulated markets, while recognising the need for softer and more flexible rules, taking into account the different parties on these markets and their level of professionalism. MTFs may be operated either by a market operator, or by a credit institution or investment firm. Except for the differences linked to the markets' structure and the persons authorised to operate them, regulated markets differ from MTFs mainly in that the admission to trading of a financial instrument on a regulated market is the element triggering the application of a certain number of harmonised provisions at EU level, as for example the provisions relating to international accounting standards which do not necessarily apply to MTFs or only apply to a lesser extent.

Where the regulated market is not a legal person, the operator of this market must ensure that the regulated market complies with the requirements of Chapter I of Title I of the MiFID Law and must be entitled to exercise the rights that the law confers to the regulated market it operates.

In most Member States, including Luxembourg, regulated markets are currently trading systems which are not legal persons themselves, but are operated by legal persons. In Luxembourg, the regulated market "*Bourse de Luxembourg*" (Luxembourg Stock Exchange) is operated by the SBL. According to article 175 of the MiFID Law, the regulated market "*Bourse de Luxembourg*" operated by the SBL is considered as having received the written authorisation of the Minister responsible

for the CSSF. The SBL is considered as having received the written authorisation of the Minister as operator of a regulated market authorised in Luxembourg. It is moreover considered as being authorised to operate the MTF "Euro MTF". Additionnally, the above markets and their operator must comply with the provisions of Title I of the MiFID Law, notably as regards the organisation, the governance and the withdrawal of the authorisation, as well as with the provisions of the law of 5 April 1993 on the financial sector, as amended.

Moreover, on 6 April 2006, the SBL and the pan-European stock exchange Euronext already announced the signature of a Memorandum of Understanding to enhance the co-operation between their markets. The agreement covers the exchange of listing and trading technology, as well as joint efforts to develop the corporate bond market. The first practical step of this co-operation has been taken in May 2007 with the changeover of all securities listed on the markets operated by the SBL to the NSC® platform for cash trading of NYSE Euronext; the members of both partners may benefit from the cross-membership rights to the different markets concerned. In relation to post-trade activities, the partnership continues in 2008 with the introduction of possibilities to use central counterparty services on the Luxembourg stock market. In this context, the CSSF contacted the French authorities in order to clarify the supervision procedures for the activities concerned.

In the context of its markets supervision mission, the CSSF is kept informed of market activities and related issues on a daily basis by means of an activity report provided by the SBL to the CSSF.

As far as market activities are concerned, the trading turnover on the two markets operated by the SBL reached EUR 652.00 million in 2007 (against EUR 1,500.47 million in 2006). Trading on Luxembourg shares represented 25.60% of the total.

At the end of December 2007, the SBL counted 66 members, of which 11 were cross-members.

2007 was again characterised by intense activity as regards admissions to the markets operated by the SBL with 13,353 new admissions (10,544 in 2006). As at 31 December 2007, both markets operated by the SBL totalled 45,573 listings (against 39,860 in 2006), i.e. 31,469 bonds, 292 shares, 6,440 warrants and rights and 7,372 Luxembourg undertakings for collective investment and sub-funds and foreign UCIs. The regulated market accounted for 41,330 out of the 45,573 listings, and the Euro MTF for 4,243.

2.2. Investigations conducted by the CSSF at national and international level

Since end of May 2006, the CSSF is the administrative authority competent for the enforcement of the law of 9 May 2006 on market abuse upon the entry into force of this law. The purpose of the law on market abuse is to combat insider dealing and market manipulation ("market abuse") in order to ensure the integrity of financial markets, to enhance investor confidence in those markets and thereby to ensure a level playing field for all market participants.

In the context of its supervision of securities markets, the CSSF either initiates inquiries itself or conducts them in response to a request for assistance from a foreign administrative authority within the framework of international co-operation. The decisions to open an investigation or to intervene against a professional of the financial sector are first based on analytical reports of daily trading activity at the Luxembourg Stock Exchange, as well as on the analysis of trades reported to the CSSF. After its assessment of all the available information, the CSSF decides on the appropriateness of an intervention.

2.2.1. Inquiries initiated by the CSSF

In 2007, the CSSF opened five inquiries into insider dealing and/or price manipulation. The information obtained in relation to three inquiries allowed the CSSF to close these inquiries without taking any further action. The examinations made by the CSSF in the context of the other inquiries opened in 2007 continue in 2008.

Moreover, the information obtained in relation to two inquiries already opened in 2006 allowed the CSSF to close these inquiries without taking any further action.

2.2.2. Inquiries conducted by the CSSF at the request of a foreign authority

- ***Inquiries into insider dealing***

In 2007, the CSSF processed 50 requests concerning inquiries into insider dealing (against 34 in 2006). The CSSF handled all these requests with the necessary diligence befitting co-operation between authorities and no major issues relating to the requests of information submitted to the involved financial institutions have arisen.

- ***Inquiries into price manipulation, fraudulent public offers, breaches of the requirement to report major shareholdings and other breaches of the law***

The CSSF received five inquiries into breaches of the requirements to report major shareholdings, two inquiries into price manipulation and three other inquiries relating to Luxembourg-incorporated companies. The CSSF responded to all these requests within the scope of its legal competence.

2.2.3. Notifications of suspicious transactions under the law on market abuse

In accordance with article 12 of the law on market abuse, any credit institution or other professional of the financial sector established in Luxembourg shall notify the CSSF if it reasonably suspects that a transaction might constitute insider dealing or market manipulation. In this context, circular CSSF 07/280, as amended, specifies the application of this article.

Based on this provision, the CSSF received 26 suspicious transaction reports in 2007 (against seven between end of May and end of December 2006). For underlying financial instruments admitted to one or several foreign markets, the notified information was transmitted to the competent authorities of the market(s) concerned, thereby observing the obligation to co-operate referred to in the law on market abuse. This information can, where necessary, lead these authorities to open inquiries.

In 2007, the CSSF received only one notification on a financial instrument admitted to the Luxembourg regulated market from a foreign authority.

2.3. Approval of prospectuses relating to offers to the public or admissions to trading on a regulated market

2.3.1. Application of the Prospectus Directive (Directive 2003/71/EC)

Since 1 January 2006, when the CSSF became the sole intervening party[1] in the approval of prospectuses relating to offers to the public and admissions to trading to a regulated market of securities, the team in charge of this activity within the department "Supervision of securities markets" continued to improve its organisation and working methods aiming at an utmost efficiency. Today, in terms of timeliness and quality, the reactions of the market players towards the approval procedure are positive and encouraging.

Moreover, the relations between the file managers and their direct discussion partners at the applicants' (agents entrusted with the introduction of the files by issuers, lawyers, etc.) have been strengthened and the latter no longer hesitate to submit requests for advice, the answers of which contribute to enhance the file preparation.

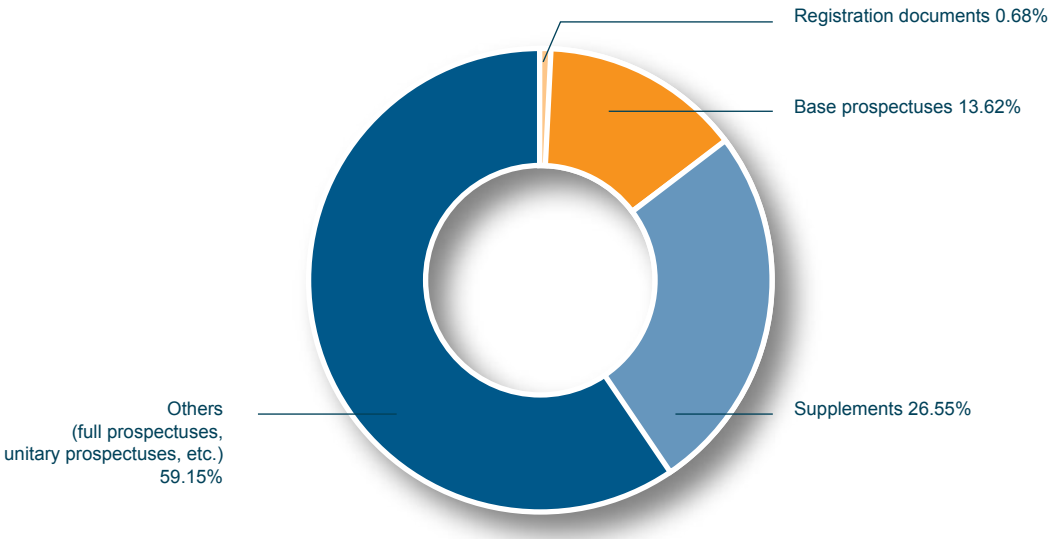
As far as the internal coordination between the different file managers and their training is concerned, discussion forums have been put in place within the department in order to align the file managers' experiences, to clarify a certain number of interpretation questions between the managers responsible for the approval of prospectuses and to refine their knowledge of more complex subjects, with a view to ensuring a balanced verification quality of the documentation to be approved.

2.3.2. Approvals and notifications in 2007

- ***Documents approved by the CSSF in 2007***

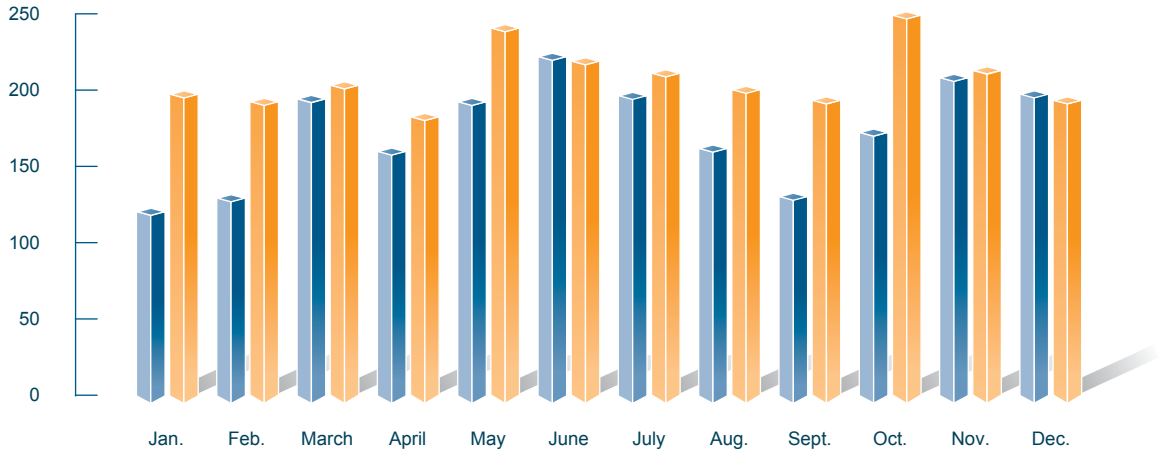
In 2007, 2,482 documents were approved by the CSSF, i.e. 1,468 prospectuses, 338 base prospectuses, 17 registration documents and 659 supplements. An increase of 20.19% was registered as compared to 2006 when the number of documents approved by the CSSF amounted to 2,065.

Distribution of files approved in 2007



[1] Until 31 December 2005, the Luxembourg Stock Exchange was in charge of performing the preliminary review of the documents filed for approval.

Development in the number of files approved by the CSSF

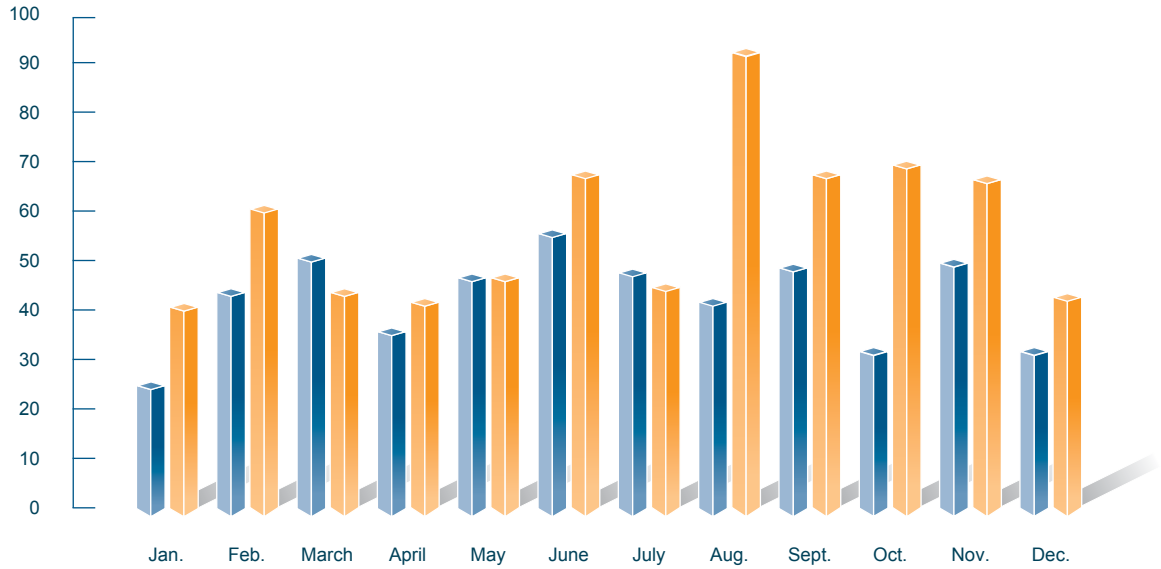


	Jan.	Feb.	March	April	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.
2006	118	127	193	158	191	221	195	160	128	171	207	196
2007	196	191	202	181	240	218	210	199	192	249	212	192
Variation in %	*66.10*	*50.39*	*4.66*	*14.56*	*25.65*	*-1.36*	*7.69*	*24.38*	*50.00*	*45.61*	*2.42*	*-2.04*

- ***Documents drawn up under the European passport regime in 2007***

In 2007, the CSSF received 677 notifications from the relevant authorities of several EU Member States as compared to 500 notifications in 2006, representing a 35.40% increase.

Development in the number of notifications received by the CSSF



	Jan.	Feb.	March	April	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.
2006	24	43	50	35	46	55	47	41	48	31	49	31
2007	40	60	43	41	46	67	44	92	67	69	66	42
Variation in %	*66.67*	*39.53*	*-14.00*	*17.14*	*0.00*	*21.82*	*-6.38*	*124.39*	*39.58*	*122.58*	*34.69*	*35.48*

Development in the number of notifications received by the CSSF

	2006	2007	Variation in %
Prospectuses and base prospectuses	290	283	-2.41%
Supplements	210	394	87.62%
Total	**500**	**677**	**35.40%**

In 2007, the CSSF sent notifications for 900 documents[2] it approved to the relevant authorities of EU Member States as compared to 610 documents[3] in 2006, representing a 47.54% increase.

Development and breakdown of the notifications sent by the CSSF

	2006	2007	Variation in %
Prospectuses and base prospectuses	352	514	46.02%
Supplements	258	386	49.61%
Total	**610**	**900**	**47.54%**

- ***Approvals delegated to the CSSF***

The Prospectus Directive allows the competent authority of a home Member State[4] to transfer the approval of a prospectus to the competent authority of another Member State, subject to the agreement of that authority.

The competent authority of the home Member State notifies this transfer to the issuer, the offeror or the person asking for admission to trading on a regulated market within three working days from the date of its decision.

In accordance with article 13(5) of this Directive, a competent authority requested two transfers of approval for a base prospectus and a registration document of the same issuer on 29 March 2007.

The motivation of this transfer of approval request being linked to the fact that an issuer issuing securities of a denomination of less than EUR 1,000 and having its registered office in the Member State of the requesting authority was included in an issuance programme of several issuers having already opted for the CSSF as competent authority, the CSSF consented to this request on 30 March 2007.

2.3.3. Some interpretation issues raised in 2007

The main interpretation issues have been included in the update of the FAQ "The new prospectus regime: FAQ – Part III" dated 16 October 2007 and published on the CSSF website (www.cssf.lu).

The CSSF received a large number of questions on the equivalence of accounting standards due to the development of the legal framework in 2007, following the entry into force of Regulation (EC) No 1569/2007 of 21 December 2007 establishing a mechanism for the determination of equivalence of accounting standards applied by third country issuers of securities pursuant to Directives 2003/71/EC and 2004/109/EC.

A description of this mechanism for the determination of equivalence of accounting standards is given under point 3.3. below.

[2] This figure corresponds to the number of documents for which the CSSF sent one or several notifications. Where notifications have been sent at different dates and/or in several Member States, only the first notification is included in the statistical calculations. Each document notified in one or several Member States is thus only counted once.

[3] The number of documents notified differs from the figures included in the CSSF Annual Report 2006 due to a change in the calculation method.

[4] Depending on the type of securities and their denomination per unit, the home Member State is defined in relation to the registered office of the company or the country where the securities are offered to the public or where the securities are to be admitted to trading.

2.4. Takeover bids

2.4.1. Offer documents approved by the CSSF

On 21 May 2007, COFINIMMO S.A. ("Cofinimmo"), an investment company with fixed capital incorporated under Belgian law, announced, in accordance with article 6(1) of the law of 19 May 2006 implementing Directive 2004/25/EC of 21 April 2004 on takeover bids ("Law on takeover bids"), a voluntary takeover bid ("Offer") on all distribution and capitalisation shares issued by IMMO-CROISSANCE ("Immo-Croissance"), an investment company with variable capital incorporated under Luxembourg law. After this initial announcement, Cofinimmo reviewed the financial conditions of the Offer on 21 June 2007, and finally launched it on 26 June 2007 through the publication of an offer document as approved by the CSSF. Subsequently, additional competing takeover bids on the Immo-Croissance shares had been announced by the company Leasinvest Real Estate SCA, a Belgian Sicafi ("Leasinvest") in the evening of 26 June 2007 ("First Competing bid") and by Baugur Group hf ("Baugur") in the morning of 27 June 2007 ("Second Competing bid" or "Baugur Offer"). On 28 June 2007, the CSSF was officially informed by the managing director of Leasinvest Real Estate Management NV, statutory manager of Leasinvest, that the Board of Directors of the statutory manager of Leasinvest had realised on 27 June 2007 that the prices offered in the context of the Second Competing bid were higher than the prices offered by Leasinvest and decided thus to withdraw the First Competing bid in accordance with article 13(e)(i) of the Law on takeover bids. The CSSF had also been informed by Cofinimmo that the management committee of the company had decided on 28 June 2007, based on a resolution of the Board of Directors dated 27 April 2007, to withdraw the Offer in accordance with article 13(e)(i) of the Law on takeover bids. As a consequence of this withdrawal, the Offer acceptance period was closed and all Immo-Croissance shareholders that had accepted the Offer were automatically released from their acceptance, in accordance with article 13(c) of the Law on takeover bids.

After the announcement of the offer by Baugur (the "Offeror") on 27 June 2007, in accordance with article 6(1) of the Law on takeover bids, the offer document for the Baugur Offer was approved by the CSSF and recognised by the CBFA (*Commission bancaire, financière et des assurances,* Belgium) on 17 July 2007 and the Baugur Offer was finally launched on 18 July 2007 by this Icelandic investment company. A positive reasoned opinion on the Baugur Offer was also published by the Board of Directors of the target company, in compliance with the Law on takeover bids. After the extension of the Baugur Offer until 26 September 2007 and the relaunch of the offer as provided for in article 7(3) of the Law on takeover bids, having received subscription commitments representing in total 90.18%, the Offeror announced the details of the right to sell-out on 7 November 2007, in accordance with article 16 of the Law on takeover bids, granting the remaining shareholders the right to sell their shares within three months from 7 November 2007 until 7 February 2008 inclusive.

In compliance with the provisions of Luxembourg law on sell-out procedures, Baugur placed a general purchase order on the relevant markets of the Luxembourg Stock Exchange and the Brussels Stock Exchange for the three-month period ending 7 February 2008. These orders were settled in compliance with the rules applicable on each relevant market. The mandatory sell-out period ended on 7 February 2008 at market closing time and on 7 February 2008, the Offeror exercised its right of squeeze-out in respect of the Immo-Croissance distribution shares on the remaining holders of this share category in accordance with article 15 of the Law on takeover bids, based on the results known by the Offeror at that date. On 8 February 2008, the final results of the Baugur Offer (including the results of the sell-out requested by shareholders), according to which the Offeror acquired 95.95% of the distribution shares and 93.92% of the capitalisation shares of Immo-Croissance and managed to collect in total 95.69% of the consolidated voting rights of the company, have been published. The remaining distribution shares which had not been presented to the Offer nor sold-out pursuant to article 16 of the Law on takeover bids have been transferred to the Offeror in accordance with article 15 of the Law on takeover bids. The Offeror then announced that the price would be paid out by paying agents during a certain period and that the non-allocated funds during this period would be transferred to the *Caisse de Consignation* in Luxembourg.

2.4.2. File for which the CSSF was consulted under article 6(2) of the Law on takeover bids and offer not falling within the scope of application of the Law on takeover bids

- In the event of a takeover bid for which the CSSF is not competent, the offer document is recognised in Luxembourg subject to its approval by the competent authority and, where applicable, its translation into Luxembourgish, French, German or English, where the securities of the offeree company are admitted to trading in Luxembourg, without need to obtain the CSSF's approval. The CSSF may require the inclusion of additional information in the offer document only if such information is specific to the Luxembourg market and relates to the formalities to be accomplished in order to accept the bid and to receive the consideration due at the close of the bid, and to the tax arrangements to which the consideration offered to the holders of the securities will be subject. The offeror must however notify the CSSF in good time by communicating all the necessary documents, thereby enabling the CSSF to inform the offeror if it requires any additional information and to verify, where applicable, if the additional information it required has actually been inserted in the offer document. One particular case occurred in 2007: the offer document for the combined takeover bid of Barclays PLC on ABN AMRO Holding N.V. intended for holders of shares and several other securities issued by the target company in different jurisdictions (including the Grand-Duchy of Luxembourg). In addition to the offer document, a Barclays PLC prospectus on the "proposed issue of up to 4,901,278,058 new ordinary shares and up to 808,191,360 new preference shares in Barclays in connection with the proposed merger with ABN AMRO and application for admission of up to 4,901,278,058 new ordinary shares in Barclays to the Official List and to trading on the London Stock Exchange's main market for listed securities" was notified in Luxembourg under the Prospectus Directive.

- One offer has been made outside the scope of the Law on takeover bids, namely the cash purchase offer of the Companhia de Bebidas das Américas ("AmBev") for the remaining shares of Quilmes Industrial ("Quinsa"). Upon preliminary discussions in mid-December 2007 on the content of the document to be used, a draft offer document was submitted on 27 December 2007 to the CSSF in its capacity as competent authority under Luxembourg law, in accordance with, in particular, the law of 23 December 1998 establishing a supervisory commission of the financial sector and the law of 13 July 2007 on markets in financial instruments. The CSSF indicated on 27 December 2007 that it did not have any objection to the offer being made in Luxembourg on the basis of this offer document. The offer period started on 28 December 2007 and the offer document was submitted at the same time to the SEC. Subsequent amendments to the offer document have been included

in a supplement published in the United States and in Luxembourg. On 12 February 2008, the Luxembourg company Quinsa announced having been informed that AmBev had managed to acquire, after the close of the offer on 11 February 2008, 99.56% of Quinsa voting rights and 99.26% of financial interests. It should be noted that this offer was governed by the general provisions of the Luxembourg financial law without falling into the scope of the Law on takeover bids, as AmBev aimed at strenghtening its control over Quinsa which it already held before this purchase offer. Indeed, according to article 1 of the Law on takeover bids, the latter "relates to takeover bids for the securities of companies governed by the laws of "Member States", where all or some of those securities are admitted to trading on a regulated market in one or more Member States". Article 2(1)(a) of the Law on takeover bids specifies that for the purposes of this law, a "takeover bid" shall mean "a public offer (…) made to the holders of the securities of a company to acquire all or some of those securities, whether mandatory or voluntary, which follows or has as its objective the acquisition of control of the offeree company in accordance with national law." This definition, taken word for word from the European directive, thus only provides for two very precise cases: (i) the case of a mandatory offer which follows the acquisition of control and thus triggering article 5(1) of the Law on takeover bids and (ii) the case of a voluntary offer having as objective the acquisition of control of the target company.

2.5. Supervision of issuers whose securities are admitted to trading on a regulated market and for which the CSSF is the competent authority pursuant to the law of 11 January 2008 on transparency requirements for issuers of securities

Since the entry into force of the law of 11 January 2008 on transparency requirements for issuers of securities ("Transparency Law"), the CSSF is in charge of the supervision of listed companies falling into the scope of this law. The Grand-ducal regulation on transparency requirements for issuers of securities ("Grand-ducal Transparency Regulation"), which provides additional technical details to the provisions of the law, entered into force on the same day as the Transparency Law (i.e. on 19 January 2008). The requirements regarding periodic and ongoing information set out in the new legislation applicable to the issuers concerned have been considerably widened. For further details relating to these requirements, reference should be made to point 3.2. below and to circular CSSF 08/337 of 6 February 2008 on the entry into force of the Transparency Law and the Grand-ducal Transparency Regulation, which explains the regulatory framework laid down by the two legal texts and provides further details.

As regards the differences compared to the former regime, it should first be noted that the scope of the Transparency Law is wider than the scope of article 7 of the law of 23 December 1998 relating to the supervision of securities markets, as amended, which has been repealed by the MiFID Law. The CSSF is thus henceforth the competent authority not only for the supervision of listed companies incorporated under Luxembourg law, but also for the supervision of all the companies for which Luxembourg is the home Member State pursuant to the Transparency Law. This automatically includes all Luxembourg issuers of shares, the Luxembourg issuers of debt securities the denomination per unit of which is less than EUR 1,000, as well as the issuers whose registered office is in a third country (i.e. outside the European Economic Area) and which chose Luxembourg as home Member State pursuant to article 2(1)h) of the Prospectus Law. Moreover, any other issuer whose securities are admitted to trading on a regulated market of the European Union and whose registered office is in Luxembourg or whose securities are admitted to trading on the regulated market operated by the *Société de la Bourse de Luxembourg* may choose Luxembourg as its home Member State.

As regards periodic information, the publication deadlines for financial reports have been shortened and the majority of issuers are now required to draw up half-yearly reports in addition to the annual report. Issuers of shares must in addition publish either an interim management statement, or a quarterly report. In 2007, an important number of issuers contacted the CSSF to request information on the temporal scope of the new requirements relating to the periodic reports. On 20 February 2008, the CSSF thus published a first list of FAQs which will be regularly updated and which concerns practical questions which come up in the context of the new regulation. The first question indicates in particular that all the new requirements on periodic information apply to the annual financial reports which refer to financial years having started on 1 January 2008 or later, as well as to all reports relating to periods having started on 19 January 2008 or later. Simplified regimes have been set up for the periods having started in 2007. For example, the annual reports referring to the year 2007 do not necessarily need to be compliant with the provisions of the Transparency Law as far as their content and publication deadline are concerned. However, these reports must be disclosed, stored and filed with the CSSF in accordance with the Transparency Law.

As regards ongoing information, it must be mentioned that the law of 4 December 1992 on reporting requirements concerning the acquisition and disposal of major holdings in a listed company, as amended, has been repealed by the Transparency Law. In this respect, the scope of application has also been widened as compared to the former legislation, as a greater number of issuers are concerned by the Transparency Law. Moreover, the minimum threshold which triggers the obligation for notification of major holdings has now been fixed at 5%, against 10% in the former regime.

Other changes concern the disclosure of information (which the Transparency Law qualifies as regulated information) that issuers have to make available to investors. Regulated information must be disseminated in a manner ensuring that it is capable of being disseminated to as wide a public as possible in all Member States of the European Union, and as close to simultaneously as possible. Besides, it must be stored in a central place and remain available to the public for five years. Finally, all this information must be filed with the CSSF *via* e-mail to the address transparency@cssf.lu. The publication, as well as the storage of regulated information, are two recurrent topics in the questions submitted to the CSSF in relation to the requirements of the Transparency Law.

In view of the above, the extent of the requirements imposed henceforth on companies the securities of which are admitted to trading on a regulated market has been substantially modified, so that the activity of the CSSF in relation to supervision of companies and control of information which the latter must provide will further develop in the coming years.

3. DEVELOPMENTS IN THE REGULATORY FRAMEWORK

3.1. Law of 13 July 2007 on markets in financial instruments

The law of 13 July 2007 on markets in financial instruments ("MiFID Law"), which entered into force on 1 November 2007, is subdivided into two titles, Title I concerning markets in financial instruments and replacing the law of 23 December 1998 relating to the supervision of securities markets, as amended. The MiFID Directive distinguishes between three order execution arrangements, i.e. regulated markets, multilateral trading facilities (MTF) and order internalisation by credit institutions or investment firms. Title I of the MiFID Law covers each of these three regimes in a different chapter. Chapter 4 of Title I concerns more specifically the post-trade requirement applicable to credit institutions and investment firms, the transaction reporting requirement and the professional secrecy obligation for financial players. The competences and powers of the CSSF are dealt with in chapter 5. The final chapter of Title I covers different aspects, such as the keeping of an official listing, the external audit of the financial statements of companies incorporated under Luxembourg law, futures markets, the right of appeal against decisions taken by regulated markets, MTFs and their operators, administrative and criminal sanctions and fiscal exemption. The categories of entities authorised to operate markets in financial instruments are governed by Title II of the MiFID Law which includes in particular amending provisions to the law of 5 April 1993 on the financial sector.

3.2. Law of 11 January 2008 on transparency requirements for issuers of securities ("Transparency Law")

The main purpose of the Transparency Law is to transpose into Luxembourg law Directive 2004/109/EC of 15 December 2004 on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market and amending Directive 2001/34/EC ("Transparency Directive"). The aim of this Directive, which is part of the Financial Services Action Plan, is to introduce a level of transparency and information adapted to the objectives of investor protection and market efficiency.

The Transparency Law addresses issuers of securities admitted to trading on a regulated market established or operating in a Member State of the European Union and for which Luxembourg is the home Member State. It does not apply to units issued by undertakings for collective investment other than the closed-end type, nor to units acquired or disposed of in such undertakings for collective investment. In Luxembourg, the sole regulated market currently existing is the market operated by the *Société de la Bourse de Luxembourg*, the market Luxembourg Stock Exchange. The Transparency Law does not apply to issuers whose securities are admitted to trading on the Euro MTF market, which is also operated by the *Société de la Bourse de Luxembourg*.

Issuers that are governed by the Transparency Law are required to provide ongoing and periodic information, defined as "regulated information". Regulated information notably includes periodic financial reports, information to be provided in relation to major holdings and inside information. As regards regulated information, the Transparency Law imposes three obligations on issuers:

- publish the regulated information;
- make this information available to an Officially Appointed Mechanism ("OAM") for the central storage of regulated information, and
- file the regulated information with the competent authority of the relevant home Member State.

As regards periodic information, the Transparency Law introduces shorter disclosure deadlines for annual reports which differ, for listed companies incorporated under Luxembourg law, from those laid down in the law of 19 December 2002 concerning the register of commerce and companies as well as bookkeeping and annual accounts of companies, and in the law of 10 August 1915 on commercial companies. Moreover, issuers of shares and issuers of debt securities must henceforth draw up half-yearly reports, the details of which are defined in the Transparency Law. Finally, issuers of shares for which Luxembourg is the home Member State must provide interim financial reports. In this context, they may opt to draw up either an interim management statement in each half-year period of the financial year, or quarterly financial reports. In relation to periodic reports, it is interesting to note that companies falling under the scope of application of the Transparency Law and which draw up consolidated accounts in accordance with the national law of the Member State in which they are incorporated, are now obliged to apply IAS/IFRS international accounting standards.

As regards ongoing information, the Transparency Law extends the notification regime as regards threshold crossing laid down by the law of 4 December 1992 on reporting requirements concerning the acquisition and disposal of major holdings in a listed company (which it repeals) by introducing new notification thresholds and by covering a larger circle of holders and issuers of shares. Indeed, henceforth, the notification obligations apply to all the issuers for which Luxembourg is the home Member State and whose shares are admitted to trading on a regulated market (provided that voting rights are attached thereto).

As regards the thresholds provided for in the Transparency Law, it should be noted that the minimum threshold was amended from 10% to 5%. Moreover, shareholders must notify major holdings where the proportion of voting rights held, directly or indirectly, as a result of the acquisition or disposal of shares to which voting rights are attached reaches, exceeds or falls below the thresholds of 5%, 10%, 15%, 20%, 25%, 33 1/3%, 50% and 66 2/3%. The notification requirements also apply to persons holding specific financial instruments that result in an entitlement to acquire shares to which voting rights are attached. The issuers of shares are required to disclose, store and file with the CSSF, as soon as possible, all the information contained in a shareholder's notification.

In addition to the notification of major holdings, issuers are subject to certain requirements on the exercise of the voting rights attached to their securities as regards ongoing information. These provisions mainly concern the obligations relating to general meetings and the exercise of voting rights.

The provisions of the Transparency Law have been completed by the provisions of the Grand-ducal Transparency Regulation, which has been published at the same time as the law. The main object of the Grand-ducal Transparency Regulation is to transpose Directive 2007/14/EC of 8 March 2007 laying down detailed rules for the implementation of certain provisions of the Transparency Directive. The issues taken up from this Directive relate to the content of the half-yearly financial reports, the notifications of major shareholdings and the methods to disclose regulated information. Moreover, the Grand-ducal Transparency Regulation covers the conditions to be met by the regulations of third countries in order to be considered to impose requirements equivalent to those set out in the Transparency Law. Besides transposing this Directive, the Grand-ducal Transparency Regulation defines the minimum content and the publication deadlines for quarterly financial reports, as provided for by the Transparency Law.

Circular CSSF 08/337 of 6 February 2008 draws the attention to the entry into force of the Transparency Law and Grand-ducal Transparency Regulation and replaces and repeals circular CAB 93/4 of 4 January 1993. The purpose of this circular is to describe the new requirements on periodic and ongoing information for issuers whose securities are admitted to trading on a regulated market and for which Luxembourg is the home Member State. Moreover, it details the procedures to be followed by issuers in order for them to comply with the obligations imposed by the law, i.e. disclose the regulated information, make it available to an OAM and file it with the CSSF. Finally, this circular introduces certain obligations imposed only on companies incorporated under Luxembourg law and informs on a Decision and a Regulation of the European Commission on the equivalence of accounting standards in respect of third countries.

In the context of the Transparency Law, and more specifically as regards the availability of the regulated information with an appointed storage mechanism, it should be noted that the European Commission issued the Recommendation of 11 October 2007 on the electronic network of officially appointed mechanisms for the central storage of regulated information referred to in Directive 2004/109/EC. This recommendation aims at drawing up minimum technical standards with which OAMs should comply in order to effectively interconnect all OAMs operating in the various Member States in a single electronic network within the Community. Currently, no mechanism for the central storage of regulated information has been officially appointed in Luxembourg.

3.3. Developments in the regulatory framework relating to the prospectuses for securities

3.3.1. Regulation (EC) No 211/2007 of 27 February 2007 amending Regulation (EC) No 809/2004 implementing Directive 2003/71/EC as regards financial information in prospectuses where the issuer has a complex financial history or has made a significant financial commitment

This amendment to the Prospectus Regulation specifies that an issuer provides further information when the historical financial information included in the prospectus does not allow investors to make an informed assessment of the actual financial situation of the latter. This is in particular the case for issuers having made one or more significant acquisitions during the year, for newly incorporated holding companies, for companies placed under common control but which never formed a legal group and for companies having been formed as a separate legal entity following the division of an existing business.

3.3.2. Regulation (EC) No 1569/2007 of 21 December 2007 establishing a mechanism for the determination of equivalence of accounting standards applied by third country issuers of securities pursuant to Directives 2003/71/EC and 2004/109/EC

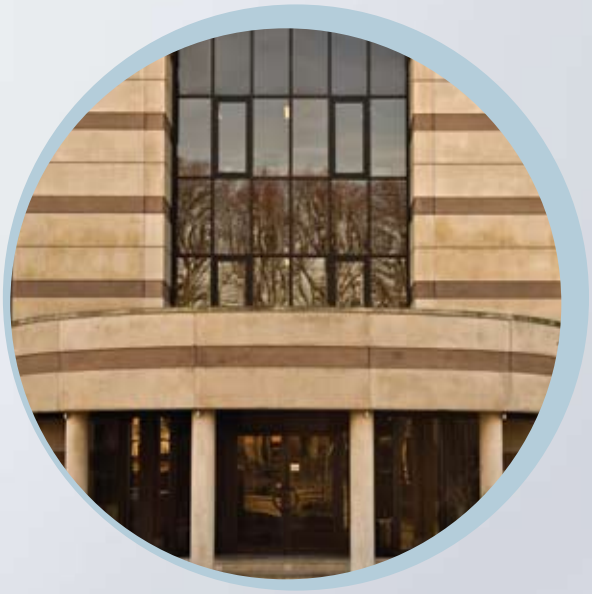
This Regulation lays down the conditions under which the Generally Accepted Accounting Principles of a third country may be considered equivalent to IAS/IFRS and introduces a mechanism for the determination of such equivalence. In order to ensure that a determination of the equivalence of third country accounting standards is made, the European Commission should assess the equivalence of third country accounting standards either upon a request from the competent authority of a Member State or an authority responsible for accounting standards or market supervision of a third country, or on its own initiative.

In accordance with this Regulation, the Generally Accepted Accounting Principles of a third country may be considered equivalent if the financial statements drawn up in accordance with these principles enable investors to make a similar assessment of the assets and liabilities, financial position, profit and losses and prospects of the issuer as would financial statements drawn up in accordance with IAS/IFRS, with the result that investors are likely to make the same decisions about the acquisition, retention or disposal of securities of an issuer.

3.4. *Ad hoc* legal interpretation group(s) on the legislation relating to capital markets

Following the successful experience of the *ad hoc* interpretation group on the new prospectus legislation created and mainly operating in 2005 and of the *ad hoc* group on the market abuse legislation, mainly operating in 2006, the CSSF consulted these same groups on various documents through written procedure in 2007. Moreover, in 2007, two meetings of the *ad hoc* group had been organised on the interpretation of the new provisions relating to takeover bids. The *ad hoc* group continued its work in an intensive way at the beginning of 2008 with meetings on the interpretation of the transparency legislation. Additional meetings on the transparency legislation and on the new provisions on the supervision of securities markets are planned.

CHAPTER VIII



SUPERVISION OF INFORMATION SYSTEMS

1. ACTIVITIES IN 2007

The law of 2 August 2003 amending the law of 5 April 1993 on the financial sector, as amended, introduced the notion of PFS performing a connected or complementary activity of the financial sector. At that time, the support PFS included domiciliation agents of companies (article 29), client communication agents (article 29-1), administrative agents of the financial sector (article 29-2), IT systems and communication networks operators of the financial sector (article 29-3) and professionals performing services of setting-up and of management of companies (article 29-4).

The law of 13 July 2007 on markets in financial instruments also amended the law of 5 April 1993 as concerns support PFS, removing the status of IT systems and communication networks operator of the financial sector and replacing it by two complementary statuses, i.e. the status of primary IT systems operator of the financial sector (new article 29-3) and the status of secondary IT systems and communication networks operator of the financial sector (new article 29-4). Professionals performing services of setting-up and of management of companies have been maintained under the new article 29-5.

The four PFS categories referred to in articles 29-1, 29-2, 29-3 and 29-4 of the law of 5 April 1993 on the financial sector, as amended, have been designated as "support PFS" by the professionals themselves in agreement with the CSSF. This denomination emphasises the main characteristic of these PFS, i.e. the provision of support services to financial professionals without accepting or managing financial assets of clients or investors.

The services offered by support PFS being more related to organisational and technical aspects, rather than financial ones, an appropriate supervision requiring specific IT competences was needed to take into account the different nature of risks encountered and the importance of IT systems for these PFS.

Through an internal reorganisation, the CSSF created a new department called "Supervision of IT and support PFS" grouping the previously existing IT supervision function and the support PFS supervision.

The setting-up of a dedicated supervision for support PFS also emphasises the growing importance of this activity within the financial sector. The reader may refer to point 3 of Chapter VI "Supervision of the other professionals of the financial sector" for the 2007 review of the supervision of support PFS by the new department.

1.1. Meetings and participation in national and international groups

In 2007, the department "Supervision of IT and support PFS" took part in 119 meetings, 30 national meetings and four international meetings, i.e. a total of 153 meetings. The agents of the department also attended 25 conferences or seminars related to IT systems security, financial tools or applications, and to the Luxembourg economic outlook, notably on research in the fields of IT, communication and security. The department also participated in two reviews of the Basel II risk models of Luxembourg banks belonging to international groups, initiated by the department "Supervision of banks", in co-operation with the foreign prudential supervisory authorities.

In 2007, the meetings related to IT supervision, except for those concerning authorisation requests or support PFS supervision, mainly focussed on the issues of mobility, architecture and security of websites, and the outsourcing of IT functions with third parties or within the group abroad.

As far as national meetings are concerned, the department in charge of IT supervision represents the CSSF within the following committees, commissions, associations or working groups:

- ABBL's *Commission Moyens de Paiement* (CMP, Payment Means Commission) in which the CSSF participates as observer. The Commission deals with topics relating to payment and clearing systems, credit cards, direct debit and especially the European project SEPA (Single European Payment Area) coordinated by EPC (European Payment Council). The aspects of vulnerabilities specific to the use of financial services *via* the Internet are also reviewed.
- The *Fonds National de la Recherche* (FNR, National Research Fund). The CSSF participates in the FNR Foresight initiative. The department in charge of IT supervision helps to identify the research domains with medium-term interest in the area of IT.
- CRP Henri Tudor. In 2007, the CRP started a research programme INNOFinance within the current economic and political context fostering the identification and promotion of services for which the Luxembourg financial centre intends to prove its excellence. Fostering excellence of services at an international level should lead to insourcing decisions, i.e. concentration of service provision activities in Luxembourg. The CSSF is involved in the strategic orientation of the INNOFinance projects. The CSSF also takes part in the strategic sub-committees in the fields of IT systems security and service quality.
- ANSIL/CNLSI/CNLQSI. The *Association de Normalisation pour la Société de l'Information Luxembourg* (ANSIL) is active in the standardisation works in the field of IT quality and systems security. ANSIL federates the standardisation initiatives of two working groups, namely CNLSI, working on the standards ISO/IEC of the SC27 group and CNLQSI, which deals with quality (SC7 group of ISO).
- The Operational Crisis Prevention Group for the financial sector (OCPG) under the aegis of the Luxembourg Central Bank. The mission of OCPG consists in identifying the risks supported by the financial sector in relation to critical infrastructures, in order to suggest measures enabling to prevent a possible operational crisis which would disrupt the functioning of the financial professionals and jeopardise the proper settlement of monetary operations.

1.2. International co-operation

The department in charge of the supervision of IT systems takes part in the annual international conference Supervisory Group on IT (ITSG), which gathers the persons responsible within the different authorities for the prudential supervision of the IT systems.

The aim of this group is to foster the exchange of information regarding the current technological stakes and covers aspects such as business continuity plans, electronic banking, countermeasures against the phishing phenomenon and, in general, the specific weaknesses of banking IT, as well as the supervision of cross-border IT outsourcing. Throughout the year, the group's members share information concerning IT and Internet-related frauds, attacks on information systems, identity thefts or weaknesses of certain systems. In 2007, the group focussed on the security of client authentication for internet banking services, mainly due to the waves of phishing and identity theft attempts by Trojan horse which have been reported in the summer of 2007.

1.3. Developments in the regulatory framework

Directive 2004/39/EC of 21 April 2004 on markets in financial instruments (MiFID) and article 52 of Directive 2006/73/EC of 10 August 2006 implementing Directive 2004/39/EC, have been transposed by the law of 13 July 2007, also known as the "MiFID Law".

Grand-ducal regulation of 13 July 2007 details the organisational requirements and rules of conduct applicable to investment firms, transposing Directive 2006/73/EC of 10 August 2006 implementing Directive 2004/39/EC. This regulation defines, notably in articles 13, 14 and 15 of Section 2, the notion of outsourcing of critical or important operational functions. The CSSF underlines that the IT function should be considered *a priori* as a critical operational function. Any outsourcing of a critical IT function within the meaning of this regulation shall meet the requirements set out in the regulation.

2. SUPERVISORY PRACTICE

Supervision covers verifying that the supervised entities comply with the legal and regulatory framework, with the direct or indirect purpose to maintain or improve the professionalism of the activities, focussing in particular on aspects relating to implemented technologies as regards information systems and by taking into account the specificities of the outsourcing of these services with support PFS or third parties, outside or within the group.

2.1. Mobility and remote access to IT services

In 2007, the department in charge of the prudential supervision of information systems was approached on several occasions with requests for advice on projects related to the mobility either of financial partners or of employees of the relevant financial professional.

The reasons for current mobile applications focus are more and more linked to:

- A greater availability of financial information and services to delocated financial partners and intermediaries.

  Certain projects related to the access to banking applications for professional use, i.e. financial services accessible *via* the Internet, mainly web-based, but intended for a professional use and allowing an intermediary to deal with several customers of the bank. The services typically involve the access or management of client accounts by account managers or other professionals in charge of these duties. These applications require a high level of protection as they give access to the data of several clients and sometimes allow the execution of transactions on their behalf. Client-related data is therefore anonymised.
- A flexibility in the accessibility of working tools for employees, mainly for a faster action whenever technical problems occur, but also in order to increase the efficiency of executives who are on a business trip within the group abroad.

  This flexibility consists in allowing certain employees to have a remote access to certain systems or to access certain applications. Internal e-mail and internal support functions, such as intranet consultation, are the most commonly related applications. In particular, certain executives have the possibility to access applications related to their field of responsibilities in order to be able to rapidly analyse a situation or solve an urgent issue.

  In most cases, remote access to systems for employees of the IT or security department are justified by the increase of cross-border employees which live far from their working place and for which the intervention time linked to commuting, especially during the night, affects the time left for solving the problem before the institution opens on the next morning.

Every mobility project submitted to the CSSF is analysed on a case-by-case basis due to the diversity of applications considered and technical solutions proposed. As the concept of mobility implies in most cases a cross-border access, the CSSF reminds that the mobility solutions must forbid any access outside the national borders to confidential data which may jeopardise the professional secrecy obligations as described under article 41 of the law of 5 April 1993 on the financial sector, as amended. This essential point must be taken into account when defining the access rights to the systems, databases and applications, but also when accessing company e-mails, which must not contain any reference which might reveal the identity of a client.

The introduction of a mobility solution should, in accordance with carefulness principles, implying that mobility today carries a higher risk of identity theft or power usurpation due to human and technical vulnerabilities, respect the following points:

- The user's access rights should be limited as compared to those available to the user when he/she is on-site, remaining nevertheless consistent with the intended use.
- The access hours and the geographical location of the identified user should be correlated to the intended use in order to avoid or to emphasise any abuse, attempt of fraud or of threat towards this user. A user connecting to the system during working hours while he/she supposedly has a day off, may thus be considered as abnormal. There should, of course, never be more than one simultaneous connection per user.
- The mobile access equipment of the user must be secured, which implies :
  - An encryption of the storage media, e.g. disks or random access memory.
  - No possibility, for a user or a third party other than the authorised administrator, to modify a component which would lower the security level, for example the BIOS, the operating system, the security applications (anti-virus and fire-walls), etc.
  - A strong authentication to the systems and applications accessed. The resistance of the authentication mechanism to any type of fraud should be proportionate to the risk incurred by the financial institution in relation to the application concerned. A user remotely accessing multiple anonymous client accounts presents thus fewer risks in case of identity theft than orders given on derivative products for portfolios managed by pooling.
  - A fair assessment of residual risk linked to the implemented solution is recommended. An underestimation of risks, in particular due to the unawareness of the threats, is likely to have a major impact on the activity. Considering the development of threats, it is useful to reassess the residual risks based on a schedule, which varies according to the reported IT hacking trends.
  - A security policy or a review of the existing security policy should be provided for, including at the same time a formal commitment by the user to the specific obligations linked to the mobile use of the functions and equipment made available to him/her.
  - An encryption of communications, as provided for in circular CSSF 05/178. An SSL cryptography is not always sufficient however, notably due to the weaknesses linked to the protocol and the attention required when installing the remote certificate. A VPN connection (L2TP/IPSec or other) is recommended.
  - It is recommended, whenever possible, not to grant direct access to an application in web or console mode. A session or screen presentation solution (like Citrix ®) reduces the risk of malicious code injection into the central system and has the advantage of a light client application.

Even though mobility represents, *a priori*, considering the current cyber-criminal threats, an additional risk, it nevertheless constitutes a first resiliency element in the event of a crisis, e.g. a pandemic or eventual office access problems.

2.2. Simultaneous outsourcing of accounting, payment and reconciliation systems

As European regulation requires the disclosure of the payer's identity in order to ensure the traceability of transfers of funds in the context of the fight against money laundering and terrorist financing, the professionals concerned, and in particular the banks, were required to inform their clients of this situation. Indeed, the client information is necessary in order to ensure that he/she receives a reasoned advice on the consequences of a transfer of funds and that these transfers be then considered as including an implicit mandate to provide identity information falling under professional secrecy, with the aim to allow the finality of the transaction, i.e. the transfer of funds or other values.

Hence, a certain number of banks belonging to international groups have optimised their payment systems and relocated their SWIFT access with their parent company or with a specialised entity of the group.

The CSSF reminds that such relocation is possible, even though confidential data might be passed-through, to the extent that the payers are aware of the fact that the transfer includes this implicit mandate. The financial professional relocating its payment systems or its access points to a payment system will nevertheless have to be prudent as far as the consequences of a possible leak of information are concerned, which might occur outside the strict scope of the transfer, as the finality of the transfer will have been reached and the leak will occur *a posteriori*, due to an inappropriate choice in the outsourcing. In this context, the CSSF reminds that the storage and archiving of transfer transactions should not be done abroad.

An additional risk consists in an accrued traceability of all the transactions of a client, who can henceforth be identified following a transfer whenever the payment system is relocated within the same jurisdiction as the main information or transaction reconciliation system. A reconstruction of the clients' historical movements and their total transparency to third parties becomes then possible. Such situation is not compatible with the prudence required by the professional secrecy and the CSSF may thus not support outsourcing which combines at the same time the delocated access to payment systems and to the main information system of a financial professional.

2.3. State of the vulnerabilities reported in Internet-based financial services

The year 2007 was distinguished by a wave of attempted fraud by criminals trying to steal authentication data of clients in order to place transactions on their behalf.

Whereas the previous years were characterised by waves of phishing, i.e. misleading e-mails prompting bank clients to connect to an illegal website in order to enter their authentication credentials, 2007 saw the development of Trojan horses, also called "trojans", specialised in stealing information. A Trojan horse is a programme created by a criminal with the aim of taking control of an infected PC. The PC is infected by exploiting the vulnerabilities of its operating system or certain commonly used applications. A common infection method consists in hacking a well-known website and inserting a link with an IFRAME, so that each user visiting this site and insufficiently protected by an anti-virus is re-directed to the website indicated in the link and downloads the first Trojan horse.

The investigations on the reported cases have shown that the first Trojan horse allows the criminal to install further Trojan horses of his choice, remotely. The criminals have thus the possibility to test different methods to steal the data they are interested in. The reader may refer to the website www.cases.lu of the Ministry of Economy for further information on IT security.

All the actors concerned, including the CSSF, take this opportunity to reassert that it is more and more crucial for users of Internet-based financial services to protect their PC with a high-quality and regularly updated anti-virus. The additional installation of a firewall is also recommended in order to limit illicit access from the network.

The development of fraud mechanisms imposes a review of the recommendations made by the CSSF in its specific report dated December 2001, titled "Internet-based financial services, Results of the Internet survey of 31 December 2000 and recommendations regarding prudential issues", and in particular of point C. "Client authentication/access to confidential data" which describes the authentication mechanisms. The CSSF had recommended at that time the use of a "2FA", i.e. a Two Factors Authentication based on two characteristics: what you know (password) and what you have (digit card or electronic token). This recommendation is today insufficient due to the nature of frauds.

There are two categories of frauds currently reported:

- Identity theft through phishing which works only if the client has been lured by an e-mail requesting him/her to identify himself/herself on his/her usual banking website, but where the link points on a perfect copy of this site put in place by the criminal. This type of ploy is working less and less, as clients are better informed.
- Identity theft by Trojan horse eavesdropping all actions undertaken on the infected PC of the client. In this case, the sophistication of the Trojan horse may vary and evolve. The client may block these attacks with a high-quality and regularly updated anti-virus.
  - The Trojan horse may simply transmit the data inputed with the keyboard (keylogger) to the criminal. A virtual keyboard appearing on the screen is an adequate solution.
  - The Trojan horse may be able to send a screen shot and the movements or clicks of the mouse to the criminal. The virtual keyboard should include several characters per key in order to reduce the probability to find out the code.
  - The Trojan horse may intercept the information before the SSL/TLS cryptography of the communication. In this case, the mechanism must ensure that the Trojan horse does not read the characters transmitted, which correspond to those of the digit card (TAN-Card), allowing thus to restore the card. A position in the keyboard (changing at each new session) will thus have to be transmitted to the server of the bank rather than the character of the card. The use of a one time password for the session will also allow to counter this type of Trojan horses.
  - The Trojan horse may intercept the information and interfere to modify the transactions. In this case, the countermeasure consists in signing the transaction through a mechanism which cannot be attacked by the Trojan horse. The use of a one time password for the session will be insufficient as the criminal takes control of the session in progress.

It is hence not easy to find a countermeasure to stop the development of Trojan horses, but it is essential to anticipate the potentiality of these viruses and to know the weaknesses and limits of the authentication system currently in place.

The financial professionals that want to reduce their risk at this level should also think about the different techniques related to the client's behavioural pattern. Fraudulent transactions based on identity theft are often atypical, in particular if a client is considered to be less inclined to mobility (in terms of transfer origin/destination or connection).

Similarly, good practice recommends that any transaction which continues from a different access point than the one initially identified for the authentication be refused. This measure hinders the session hijacking when the criminal interferes from another PC into a transaction initiated by the client. The IP address is in this case different from the login IP address.

The CSSF reminds that reputational risk must not be neglected, even if financial risk remains limited, owing notably to an adequate limit management and the possibility to stop transactions in case a fraud is detected.

For on-line brokerage services (e-brokerage), the CSSF reminds that the nature of the risk is different. Indeed, these services do often only allow the transformation of assets (securities portfolio to and from current account) without transfers to third parties, but identity theft allows criminals to manipulate stock prices through a simultaneous action on several victims and several e-brokerage websites, buying or selling listed securities which are sensitive to fluctuations. This manipulation is called pump & dump. The financial cost for the financial professional concerned may turn out to be very important, in particular if it has to execute reverse market transactions and restore its clients' current account at market value after the manipulation. For these financial services, a very strong authentication, above "2FA" is necessary.

The above *ad hoc* report of the CSSF already indicated on page 54 that "It is not excluded that future viruses will aim at stealing the credentials of the targeted financial institutions' clients. Institutions should thus be responsible for measuring the impact at client level of the technologies currently used and, where appropriate, to inform them on the risks incurred and how to protect themselves." The current situation of frauds reported confirms the anticipation of 2001. The financial professionals concerned should thus adapt to this situation and not under-estimate the capabilities of Trojan horses and the competence of criminals which have shown their ability to adapt their Trojan horses very rapidly to minor changes to the authentication mechanisms.

Educating clients on internet risks should allow them to better protect their PCs. This protection is the key element that will allow to block future criminal attacks currently under development.

2.4. Use of interim competences over an extended period of time

In circular CSSF 06/240, the CSSF specified the conditions allowing a company to provide interim staff/services to financial professionals without being considered as a service provider for which a support PFS authorisation is required, and in particular, as IT systems operator.

The CSSF wishes to inform financial professionals resorting regularly to interim staff/service provisions over extended periods of time, beyond one year, even though it might not be the same individual who realises the tasks entrusted by the financial professional, that the interim activity does not fall under the services for which an authorisation is required.

As a consequence, the financial professional must:

- Be cautious whenever it prompts its service provider to obtain a support PFS status in order to reduce its own risk related to professional secrecy. Indeed, the authorisation granted to the service provider will become null if the latter does not have a contract within twelve months for a service provision falling under the scope of the authorisation. This situation is adverse to the two parties in the medium-term.
- Consider the dependency risk towards temporary staff. The longer the period, the greater the dependency risk. The financial professional must ensure to retain the knowledge allowing the perenniality of its activities.
- Be cautious in relation to one's obligations to professional secrecy towards temporary staff, in particular, if the latter may come across confidential data.

Irrespective of the dependency problem linked to temporary staff, the financial professional may solve its legal risk linked to the confidentiality obligations through the implementation of a legal and organisational environment which assimilates temporary staff to employees. Temporary staff will then have to be trained individually to their obligations as regards confidentiality and anti-money laundering and will have to respect the internal rules and regulations of the financial professional.

This assimilation of temporary staff to the obligations and status of other employees enables to avoid requiring from the service providers to be licensed as support PFS.

CHAPTER IX

MEANS OF SANCTION AVAILABLE TO THE CSSF

1. Means of intervention available to the CSSF
2. Sanctions imposed in 2007

1. MEANS OF INTERVENTION AVAILABLE TO THE CSSF

The following means of intervention are available to the CSSF to ensure that the persons subject to its supervision comply with the laws and regulations relating to the financial sector:

- injunction, sent by registered letter, requesting the establishment concerned to remedy the particular situation;
- suspension of persons, suspension of the voting rights of certain shareholders or suspension of the activities or of a sector of activities of the establishment concerned.

In addition, the CSSF has the right to:

- impose or ask the Minister of Treasury and Budget to impose disciplinary fines on the persons in charge of the administration or management of the establishments concerned;
- under certain conditions, apply to the District Court responsible for commercial affairs for suspension of payments of an establishment;
- ask the Minister of Treasury and Budget to refuse registration on or to withdraw registration from the official list of credit institutions or the other professionals of the financial sector, if an establishment does not fulfil or no longer fulfils the conditions for being or continuing to be registered on the official list in question;
- refuse registration on or to withdraw registration from the official list of undertakings for collective investment, pension funds, management companies (Chapter 13 of the law of 20 December 2002 as amended), SICARs or securitisation undertakings, if an establishment does not fulfil or no longer fulfils the conditions for being or continuing to be registered on the official list in question;
- in extreme cases and under precise conditions laid down by law, request the District Court responsible for commercial affairs to order the winding up and liquidation of an undertaking.

Moreover, the CSSF informs the State Prosecutor of any instance of non-compliance with legal provisions relating to the financial sector, giving rise to penal sanctions and that could entail prosecution against the implicated persons. The following cases are concerned:

- persons performing an activity of the financial sector without holding a licence;
- persons active in the field of company domiciliation without belonging to any of the professions entitled by the law of 31 May 1999 governing the domiciliation of companies as amended to carry on this activity;
- persons other than those registered on the official lists of the CSSF, who use a title or appellation, thereby breaching article 52(2) of the law of 5 April 1993 on the financial sector, as amended, that gives the appearance that they are authorised to perform one of the activities reserved for persons registered on one of the lists;
- attempted fraud.

2. SANCTIONS IMPOSED IN 2007

2.1. Credit institutions

In 2007, the CSSF did not need to order fines nor to impose sanctions against managers (idem in 2006). Neither did the CSSF impose any injunction, even though it did exercise this right in one instance in 2006 and 2005 respectively.

2.2. Other professionals of the financial sector (PFS)

During 2007, the CSSF did not exercise the right of injunction nor the right of suspension under article 59 of the law of 5 April 1993 on the financial sector, as amended. Neither did it impose disciplinary fines under article 63 of that law on persons responsible for the administration or management of PFS.

In 2007, the CSSF filed seven complaints with the State Prosecutor's office for illegal exercise of financial sector activities. The majority of the entities concerned were either performing financial advisory services or private portfolio management without being authorised thereto.

2.3. Undertakings for collective investment

In 2007, the CSSF did not need to order fines nor to impose sanctions against UCIs.

CHAPTER X

GENERAL SECRETARIAT

1. Activities in 2007
2. Customer complaints
3. Reports related to the fight against money laundering and terrorist financing

1. ACTIVITIES IN 2007

The responsibilities of the General Secretariat (SG) cover the following fields:

- **General Secretariat**

The SG's task is to coordinate the external relations and communications of the CSSF, which includes contacts with foreign supervisory authorities, national and international administrations, professional associations, as well as with any other counterparty that does not fall within the remit of the other functions and departments of the CSSF.

In 2007, the SG has thus had contact, in writing, with the supervisory authorities of 45 different countries on subjects as diverse as the organisation of co-operation meetings between the CSSF and homologous authorities as home or host authorities, consultation procedures laid down in the European Directives, notifications regarding the freedom to provide services and establish branches, requests for information relating to national laws and regulations or authorised entities and natural persons, etc..

Moreover, the SG answers the requests for general information of the public in relation to the CSSF's activities or the financial centre.

The SG is also in charge of producing, where applicable in co-operation with the other functions and departments concerned, the CSSF's publications in the broad sense (annual report, brochures, press releases, monthly Newsletter, management of the website, etc.).

- **Legal issues**

The SG deals with general legal issues and cases of presumption of fraudulent and illegal activities in the financial sector (such as the conduct of unauthorised or illegal activities), including the response to be given, if necessary, by the CSSF.

- **Professional obligations and consumer protection**

The SG handles concrete files relating to professional obligations, conduct of business rules and consumer protection.

In this context, it deals with the complaints of customers against professionals under the supervision of the CSSF (credit institutions, UCIs, PFS, SICARs, pension funds, securitisation undertakings) and intercedes with the professionals with a view to reaching an amicable settlement in accordance with article 58 of the law of 5 April 1993 on the financial sector, as amended (please refer to point 2 hereinafter).

Furthermore, based on concrete files (*inter alia*, on reports to the State Prosecutor and observations following on-site inspections), the SG controls compliance with anti-money laundering rules (please refer to point 3 below) and conduct of business rules.

2. CUSTOMER COMPLAINTS

The CSSF acts as an intermediary in the conflict settlement between the professionals subject to its supervision and their customers. This mission is conferred on the CSSF by article 58 of the law of 5 April 1993 on the financial sector, as amended, which provides that the CSSF "shall be competent to receive complaints by clients of persons subject to its supervision and to approach those persons with a view to achieving an amicable settlement of such complaints." In drawing up this law, the legislator had followed a recommendation of the European Commission which advocated that extra-judicial conflict settlement means be set up. It considered that customers of the professionals of the financial sector had the right to bring their dispute before a public authority.

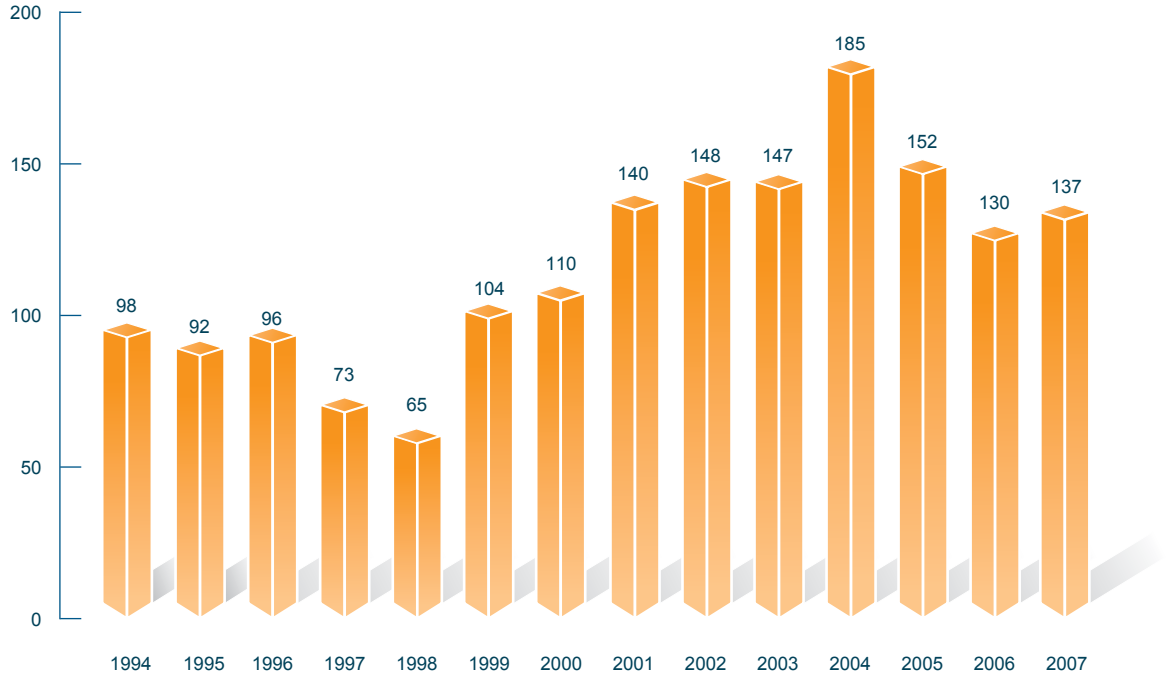
In order to put holders of units in UCIs on equal footing with the customers of the professionals subject to the law of 5 April 1993, as amended, an identical provision was introduced into the law of 20 December 2002 relating to undertakings for collective investment. Article 97(3) thus provides that "the CSSF is competent to receive complaints from holders of units of UCIs and to intercede with such UCIs in order to resolve such complaints amicably".

In order to avoid that the same people handle the complaints and perform the daily supervision of the professionals concerned, the CSSF entrusted the General Secretariat with the former task in accordance with the principle of task segregation.

2.1. General data

In 2007, the number of complaints increased slightly compared to the previous year from 130 in 2006 to 137 in 2007.

Development in the number of complaints



It is important to note in this context that apart from the complaints that are submitted to the General Secretariat in a formal manner, the latter also receives a large number of phone calls from customers who, on the one hand, are not always informed about the existence of the CSSF's procedure or who, on the other hand, wish to obtain the CSSF's opinion on a specific issue they have with a professional. Many phone enquiries thus concerned the regulations in force, the conformity of the fees applied or the consequences of the enhancement of certain measures aiming at fighting money laundering and terrorist financing (control of accounts, ID, etc.).

125 of the 137 complaints received in 2007 were lodged by natural persons and 12 by legal persons. 17 complainants contacted the CSSF through a lawyer. Of those 137 complaints, 109 concerned credit institutions, 14 concerned PFS and 14 concerned UCIs.

Taking into account the 48 open files from 2006 in addition to the 137 complaints received in 2007, a total of 185 files have been dealt with in 2007.

Among the 185 files handled in 2007, 137 have been closed, with the following outcome or reason for closing:

Files closed in 2007	**137**
Unjustified complaints[1]	64
Amicable settlement[2]	33
Amicable settlement following the CSSF's opinion	10
Contradictory positions	4
Withdrawal by client[3]	23
Non-article 58	3
Open files carried forward into 2008[4]	**48**
Total files handled in 2007	**185**

In 64 of the 137 files closed in 2007, the CSSF did not conclude to misconduct of the professional. In ten cases, the CSSF considered the reproaches against the professionals justified and sent a reasoned opinion to the latter. This opinion has been accepted in nine cases. In 33 other cases, the CSSF did not have to state its view, as the professional submitted a spontaneous proposal for an amicable settlement to the client. In four cases, the CSSF concluded that the positions of the parties were contradictory so that it could not decide in favour of any party. As a conclusion, it can be said that the CSSF's intervention contributes to working out an acceptable solution for the parties concerned. Even if its positions are not binding on the professionals, the CSSF's advice is nevertheless largely followed. Where professionals refuse to follow its advice, the CSSF terminates its intervention as its means of intervention under article 58 are exhausted.

The CSSF also receives many requests from persons residing abroad who are seeking out accounts in Luxembourg that belonged to a deceased close relative. In such case, the CSSF only provides general indications as to how to proceed in their search and provides them with a list of the professionals of the financial sector that they could contact. In addition, the CSSF informs the persons concerned of the documents they should append in order to prove that they are the heirs, and to obtain an answer from the professionals. The figures presented in this chapter do not include these requests for assistance, but only the cases where concrete problems arose between heirs and a professional in the context of the settlement of a succession.

Moreover, it must be noted that the CSSF's intervention under article 58 of the law of 5 April 1993 on the financial sector, as amended, only covers disputes in relation with the financial activities of the supervised entities. This notably applies with regard to the credit institution PayPal (Europe) S.à r.l. & Cie, S.C.A., established in Luxembourg since 1 July 2007 and running a platform that is specialised in electronic payments between professionals and individuals. The CSSF is thus not competent to deal with complaints regarding the commercial activities between sellers and buyers at the origin of the payment made through PayPal.

It should also be noted that the CSSF does not answer questions concerning the quality or performances of a professional, its solvency or soundness, and does not pass judgment on the quality of the products offered. Its mission is limited to complaints between customers and professionals, and aims to work out concrete solutions.

[1] Unjustified complaints are those for which the CSSF did not conclude to misconduct of the professional.

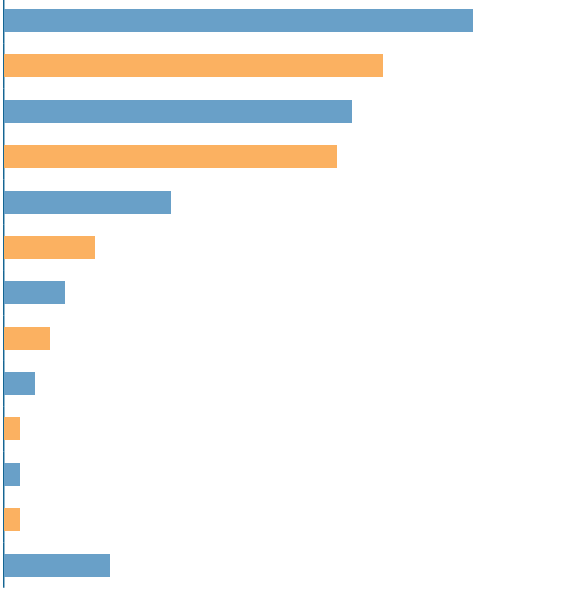
[2] Spontaneous proposal for an amicable settlement by the professional, before a reasoned opinion was issued by the CSSF.

[3] This category includes 20 complaints on which the complainant did not follow up and three complaints where the client decided to refer the matter directly to the courts, thus putting an end to the CSSF's intervention.

[4] 22 out of the 48 files carried forward into 2008 could be closed until 1 March 2008.

Breakdown of the complaints closed in 2007 according to the complainants' country of residence[5]

Country	Number
Germany	31
Luxembourg	25
France	23
Belgium	22
United Kingdom	11
Italy	6
Sweden	4
Spain	3
Netherlands	2
Denmark	1
Portugal	1
Czech Republic	1
Others (non EU)[5]	7



Breakdown of complaints closed in 2007 according to their object

	Number	
Transferable securities		**68**
Discretionary management	11	
Advisory management	4	
Various securities transactions	37	
UCIs	16	
Banking accounts and investments		**17**
Savings account	4	
Current account	13	
Various banking transactions		**19**
Inheritance	6	
Account blocking	4	
Counter transactions	9	
Payments		**30**
Transfers	27	
Cheques	1	
Bank cards	1	
Domiciliation	1	
Credits		**3**
Total		**137**

[5] Switzerland, Thailand, Bahamas, China, Turkey, South Africa, Israel.

2.2. Analysis of the complaints handled in 2007

2.2.1. Transfers

In one case submitted to the CSSF, a bank had transferred a certain amount from a company's account to another company. The originator company then objected to this transfer on the grounds that the transfer order had been signed by a person that did not have power of signature. Following the CSSF's intervention, an agreement could be reached and the disputed amount was returned.

Another complaint concerned the fact that a bank had executed transfer operations and closed the accounts of the complainant based on instructions given by phone, although the bank had first required a written instruction to close the account. The account holder, having learnt that his accounts had been closed, objected to having given such instructions and concluded having been the victim of a fraud. After having obtained a copy of the written instruction, the client pointed out several anomalies: the address mentioned was not his present one, although the bank had been informed of his new address, the mobile phone number stated was not his and the post box number was not correct. Moreover, the instruction did not state the amount to be transferred. It simply requested the closure of the savings account and the immediate transfer of all the funds to an account with another bank abroad. In its complaint, the client considered that the bank employee should have remembered that the person having given him the disputed written instruction had contacted him two weeks earlier to enquire about the amount deposited in the savings account. The complainant also considered that the bank had failed its due diligence obligation by calling back the person who had transmitted the instruction at the phone number stated on the instruction itself, although this number was different from the number that had been given to the bank. The complainant also claimed that even though the bank had called back the person who had sent the instruction to close the account, the purpose of that call was not to verify that that person really was the account holder. After analysing the file, the CSSF concluded that the bank had failed its due diligence obligation towards the complainant. The bank accepted to compensate the complainant for the damage sustained owing to its executing the closing and account transfer instructions without having received any written instruction.

In another complaint lodged with the CSSF, a customer claimed that his bank account had never been credited with a fund transfer made in his favour. At the CSSF's request of the bank's position, the latter answered that it did not have the documents relating to the customer's account anymore, nor the documents relating to the transfer orders and withdrawals made by the customer, as the compulsory period for record-keeping of ten years had been exceeded. The complaint had indeed been lodged after that time limit. The CSSF concluded that the bank had not made any mistake by destroying the documents relating to that account. Indeed, past this ten-year period, the bank was no longer subject to the record-keeping obligation.

2.2.2. Portfolio management

In the context of a complaint regarding portfolio management, the complainant reproached the bank for not having informed him of the events concerning the issuer of the bonds in which he had invested. The CSSF considered that the bank was not obliged to inform its client of events concerning the company issuing securities deposited with the bank, as long as those events did not call for a statement of the client.

2.2.3. Interest rates

Several customers of professionals in the financial centre voiced their discontent with the professionals' interest rates policy. Thus, they reproached the professionals either for keeping high lending interest rates on their loan accounts, or for applying deposit rates to their savings accounts that they consider to be too low. The CSSF informed these complainants that determining the interest rate applied by a professional is subject to the professional's internal commercial policy and that the CSSF may not intervene in this policy, unless the professional breached its price policy communicated to the customers or a legal provision. It should be noted that as far as an adjustment of the lending interest rate following a reduction decided by the European Central Bank is concerned, the professional is not obliged to follow this adjustment and to apply the decrease in the key interest rate to every existing loan.

2.2.4. Internet banking

A customer who had bought securities through an Internet bank complained that the bank had granted him overdraft facilities unbeknown to him, and then settled his portfolio to cover this overdraft. However, the CSSF considered that the customer was free to manage his portfolio and that he was therefore supposed to be aware of the status of his account and to monitor his securities in order to be able to act accordingly and within his limits. Moreover, the bank concerned provides for the possibility to view up-to-date account statements online 24 hours a day, 7 days a week. Given the frequency of orders passed by the customer, the CSSF considered that the customer must have consulted his account online often enough to be aware that the execution of his successive transactions required substantial overdraft facilities. The overdraft increasing with the transactions could therefore not have escaped his attention. According to the different conversations and letters of the bank, the client could not pretend to be unaware of the successive calls to cover the granted overdraft. Following the various calls to cover the overdrafts ignored by the customer, the bank then legitimately liquidated the customer's portfolio in accordance with its terms and conditions signed by the customer and which notably refer to the policy relating to overdraft facilities. The CSSF did not decide on any misconduct of the bank.

Another interesting case concerned a customer who complained that the online portfolio management system of a bank did not execute certain sell orders and that he had therefore suffered a substantial material loss. According to the bank, orders are blocked every time the proceeds from the sale of the securities pledged do not allow to offset the account/credit overdraft. The system refuses to execute those orders, while inviting the customer to get in touch with his account manager, in order for the latter to record and validate the order manually in the bank's IT system. The bank explained that it had not yet found a possibility to allow the customer to modify the blocking system, but that it was actively searching for an IT solution complying with its internal procedures. The operating costs of a fully automated IT system being less important than those generated by a manual order execution by the account manager, the bank charged the costs due in case of automatic execution to the customer in order to compensate for the inconvenience caused. Following the CSSF's intervention, the bank made a commercial gesture in favour of the customer by abandoning in addition the commissions due under the agreement concluded with the customer. In the context of the very same complaint, the customer wondered why the system concerned did not execute certain limit orders. In this context, the bank referred to a note published on its website stating that this is a specificity of the stock exchange concerned, which sets down, on a daily basis, a percentage limiting the tolerated price spread for limit orders, which may vary in accordance with the securities' volatility. This percentage may be adjusted in the course of the session. The bank warns its customers on its website and advises them, in order to avoid that their orders be rejected by the market, to indicate a limit above the latest quote in case of buy or below the latest quote in case of sell. This blocking system actually allows to protect the least informed investors. As the bank

had explained to the customer that he should contact his account manager if he wished to pass an order that would not meet the above criteria and given the explanations provided, the CSSF did not decide on any misconduct by the bank.

2.2.5. Banking secrecy

In the context of the settlement of a succession, the heirs of a trust refused to sign the final agreement as certain points relating to the decrease in the trust's capital did not seem clear to them. The heirs obtained statements including notably annual investments made for the account of the trust and the list of the beneficiaries. As the heirs could not obtain a copy of the letter of intent signed by the deceased, they lodged a complaint with the CSSF. Indeed, they sought to get acquainted with the content of the letter of intent in order to be able to assess whether the bank had exercised its mandate properly and to verify that the many withdrawals were indeed allowed under the letter of intent. The bank explained that by setting up the trust, the customer deprived himself of his assets in favour of the trustee who managed the trust and who became the bank's customer and contact person. From then on, the bank was no longer entitled to disclose information on the trust's assets to the heirs for banking secrecy reasons. The heirs must directly contact the trustee to obtain any information on the trust. The CSSF explained to the customers that it shared the bank's view.

Another complaint dealt with the refusal of a bank to communicate to the customer the name of the remitter of a bearer security while the customer had placed a stop on the security. The bank explained that the customer's stop had no effect as the security concerned had become fungible before the stop and that the banking secrecy prevented the bank from disclosing the remitter's identity to the customer. The CSSF adhered to the bank's position.

2.2.6. UCIs

As regards UCIs, a complainant blamed a bank for having advised him to subscribe for units of a fund that was not approved for marketing in Germany. This situation gave rise to a dispute with the German tax authorities which considered that the fund's revenues were not subject to flat-rate taxation. The bank explained that its advice only concerned the portfolio management and did not take into account the customers' tax situation. Moreover, the offering prospectus drew the attention of the interested subscribers to the fact that the bank would not be responsible for any legal or fiscal consequences and invited subscribers to request appropriate assistance from their legal, accounting or tax counsels at their place of residence. The bank also asserted that at that time, free provision of services was not well developed and the sale of funds took place exclusively in Luxembourg. The CSSF did not consider the bank's behaviour as misconduct.

2.2.7. Joint account

In a case submitted to the CSSF, the complainant and his sister held a non-trading real estate investment company (*société civile immobilière*, hereinafter "SCI") for which they had opened a bank account. The Luxembourg District Court ordered the winding-up and liquidation of the company. Both partners of the SCI agreed in a private deed that the entire bank account would fall to one of them, namely the complainant, less the fees of their respective lawyers and of the liquidator. This deed has been confirmed by court ruling. When the complainant turned to the bank to obtain what he considered his due, the bank refused and informed the complainant that it would only transfer the funds once it was aware of the positions of all the parties concerned, including notably the position of the lawyer of the complainant's sister. Nevertheless, the lawyer did not feel entitled to agree to the liquidation of the disputed account as his client could not be reached and he thought not to be able to take an initiative without her instruction. Moreover, as he awaited to be paid by his client, the joint account could possibly not be liquidated according to the explicit terms of the said deed, which provided that the liquidation of the account would take

place after deduction of the lawyers' fees. Finally, the sister's lawyer submitted the ethical questions to the President of the Bar Council who broke the deadlock by inviting the lawyer to agree to the liquidation of the account.

2.3. FIN-NET network, the cross-border out-of-court complaints network for financial services

The Fin-net network, which was set up by the European Commission in 2001, gathers all bodies responsible for the out-of-court settlement of cross-border disputes between consumers and financial services providers of the European Economic Area. The CSSF and the Commissariat aux Assurances are members representing Luxembourg. The Fin-net members met twice in 2007: once on the premises of the European Commission in Brussels and once in London within the scope of the International Financial Ombudsman Conference. The meetings notably dealt with sharing experience in the area of network operation and with recent developments in the field of extra-judicial dispute settlement, as well as in more general fields of financial services at the level of the European Union.

3. REPORTS RELATED TO THE FIGHT AGAINST MONEY LAUNDERING AND TERRORIST FINANCING

Analysing the reports of the professionals of the financial sector with respect to the fight against money laundering and terrorist financing submitted to the CSSF under article 5 of the law of 12 November 2004 on the fight against money laundering and terrorist financing is part of the CSSF's prudential supervision of the financial sector, in addition to the review of analytical reports submitted to the CSSF and the inspections carried out on the premises of the professionals. By means of concrete files, this allows to verify the compliance of professionals of the financial sector with their legal and regulatory obligations in that field. The review of the documents mainly covers the efforts made with respect to due diligence, the quality of Know Your Customer (KYC) information collected and the compliance with internal procedures set up by the professionals. By ensuring that the professionals perform their obligations properly, the CSSF contributes to the fight against the use of lawful financial circuits for the purpose of money laundering or terrorist financing.

At national level, the CSSF was consulted in the context of the drawing up of bill no. 5811 transposing Directive 2005/60/EC of 26 October 2005 on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing and Directive 2006/70/EC of 1 August 2006 laying down implementing measures for Directive 2005/60/EC as regards the definition of "politically exposed person" and the technical criteria for simplified customer due diligence procedures and for exemption on grounds of a financial activity conducted on an occasional or very limited basis.

As far as international activities are concerned, the CSSF took part in 2007 in the meetings and work notably of:

- the Financial Action Task Force (FATF);
- the Committee on the Prevention of Money Laundering and Terrorist Financing (CPMLTF) of the European Commission set up in view of the transposition of Directive 2005/60/EC;
- the European Anti-Money Laundering Task Force (AMLTF) set up by CESR, CEBS and CEIOPS;
- the AML/CFT Expert Group of the Basel Committee on Banking Supervision (AMLEG); and
- the Wolfsberg Group.

As far as the statistical data for 2007 are concerned, the CSSF received 546 reports relating to the fight against money laundering and terrorist financing in the broadest sense. This number is on the rise as compared to the previous years (490 reports in 2005 and 481 in 2006).

Overall, 89 professionals of the financial sector transmitted a report to the CSSF in 2007 (against 102 in 2006), namely:

- 66 credit institutions (156 credit institutions being registered on the official list as at 31 December 2007);
- 18 PFS (214 PFS being registered on the official list as at 31 December 2007); and
- 5 management companies governed by Chapter 13 of the law of 2002 (180 management companies being registered on the official list as at 31 December 2007).

Although these figures reveal a substantial increase in the volume of reports in absolute terms in 2007, it has to be noted that this surge results from a growth in the volume of reports recorded per reporting professional and not from a rise in the number of professionals having submitted reports.

In this respect, ten banks and one PFS each made more than ten reports in 2007, representing 64% of the total number of reports received in that year. Even if the same comment has already been made in the previous year, it should be specified that these are not exactly the same professionals.

The CSSF observed that about 84% of the reports were made spontaneously by the professionals based on concrete suspicions, in accordance with article 5(1)(a) of the law of 12 November 2004. The other reports were made owing to the fact that information relating to a client had been obtained:

- through circulars issued by the Financial Intelligence Unit (FIU) of the State Prosecutor's Office;
- through circulars issued by the CSSF in relation to restrictive measures (financial embargoes);
- following a notification of seizure and search warrant in the context of an either national or international investigation (international letters rogatory); and
- based on a request for information from the FIU.

CHAPTER XI

GENERAL SUPERVISION AND CSSF INVOLVEMENT IN INTERNATIONAL GROUPS

1. General Supervision
2. Co-operation within European institutions
3. Multilateral co-operation

1. GENERAL SUPERVISION

The transversal function "General Supervision" (SGE) deals, on a horizontal basis, with prudential supervisory, accounting and reporting issues common to all the CSSF's departments. In particular, it is in charge of the international groups and the development and interpretation of national and international regulations.

The objective of this "think tank", which proposes approaches, instruments for analysis and assessment, is thus to develop the competence fields that require specific knowledge and experience, to provide methodological support for the day-to-day performance of prudential supervision, to transmit the knowledge acquired at internal training sessions and to join in on-site inspections that deal with more complex subjects, such as the validation of risk management models.

- ***Activities in 2007***

In 2007, the SGE, which comprises 27 agents, sent 449 letters stating the CSSF's position with respect to prudential and accounting supervision. Moreover, SGE agents have attended 72 meetings that were held in Luxembourg with representatives of the banking industry and international bodies.

SGE agents attended 188 meetings of international groups (cf. points 2. and 3. below) in 2007, in addition to the meetings relating to reviews of internal rating systems and advanced measurement approaches (AMA).

Besides coordinating the applications for authorisation of the internal-ratings based approaches for credit risk and advanced measurement approaches for operational risk in accordance with the provisions of circular CSSF 06/260, SGE agents reviewed, together with agents of the department "Supervision of banks", internal rating systems and models of credit institutions.

The SGE's missions also covered, *inter alia*, the following areas: internal governance, development and monitoring process, databases-related aspects, methods adopted, internal validation, qualitative and quantitative aspects of AMA models, documentation of internal rating systems and/or models.

The function SGE carried out 82 inspections on the premises of nine credit institutions in Luxembourg and abroad with respect to credit risk.

As far as operational risk is concerned, the SGE function participated in the review of the models used by the banks having adopted advanced measurement approaches (AMA). In this context, it paid 39 visits to 13 credit institutions in Luxembourg and abroad.

Lastly, a great deal of the SGE's resources were put into drawing up circulars CSSF 08/340, 08/338, 07/331, 07/324, 07/319, 07/317, 07/316, 07/301 and 07/279. These circulars have been described in the monthly CSSF Newsletters, while the circulars drawn up by the function SGE with respect to markets in financial instruments (MiFID law), i.e. circulars CSSF 07/305, 07/307, 07/325 and 07/326, are described in detail in this Annual Report (cf. point 1. of Chapter XII "Banking and financial legislation and regulations").

2. CO-OPERATION WITHIN EUROPEAN INSTITUTIONS

Article 3 of the law of 23 December 1998 creating a Commission de Surveillance du Secteur Financier as amended appoints it, *inter alia*, to deal with and participate in the negotiations concerning the financial sector issues, at both EU and international level. In accordance therewith, the CSSF participates in the work of the following forums.

2.1. Committee of European Banking Supervisors (CEBS)

The Committee of European Banking Supervisors (CEBS) was established by Commission Decision 2004/5/EC of 5 November 2003. Its duties encompass reflecting, discussing and giving advice to the European Commission in the fields of banking regulation and supervision. The Committee also co-operates with the other competent committees in banking matters, notably with the European Banking Committee established by Commission Decision 2004/10/EC.

The term of Mrs Danièle Nouy (Commission Bancaire, France) having expired, Mrs Kerstin af Jochnik (Finansinspektionen, Sweden) took the chair of CEBS in January 2008. Vice Chairman is Mr Andrzej Reich (National Bank of Poland, Poland). Mr Andrea Enria (Banca d'Italia, Italy) is General Secretary. The Chair is supported by the Bureau comprising Mr Thomas Huertas (Financial Services Authority, United Kingdom), Mr Giovanni Carosio (Banca d'Italia, Italy), Mr Rudi Bonte (Commission bancaire, financière et des assurances, Belgium) and Mr Jukka Vesala (Financial Supervision Authority, Finland). The Committee's Secretariat is based in London.

CEBS' aim is to fulfil the Level 3 functions for the banking sector under the Lamfalussy procedure, its mission being the following:

- to advise the European Commission either at the Commission's request, within the time limit that the Commission may lay down according to the urgency of the matter, or on the Committee's own initiative, in particular as regards the preparation of draft implementing measures in the field of banking activities;
- to contribute to the consistent application of European Directives and to the convergence of Member States' supervisory practices throughout the European Community;
- to enhance supervisory co-operation, in particular through the exchange of information.

As CESR, CEBS created a group named Review Panel in 2007, whose purpose is to assist CEBS in ensuring the consistent and equivalent transposition of EU legislation in Member States and in assessing the degree of convergence reached by CEBS members in the implementation of guidelines and best practices adopted by CEBS.

In 2007, CEBS published a mediation protocol between banking supervisors, thereby adopting the mediation mechanism set up by CESR by adapting it to the specificities of banking supervision. The system will be used to solve supervisory disputes.

Furthermore, in response to calls for advice from the European Commission, CEBS published a series of surveys and advice:

- 20 April 2007: opening of a public consultation on amendments to the guidelines on financial reporting;
- 15 June 2007: publication of a consultation paper on commodities business and firms carrying out commodities business;
- 19 December 2007: publication of a proposal to harmonise the remittance dates and periods for COREP information and opening of a prior public consultation.

CEBS published the following documents together with CESR (Committee of European Securities Regulators) and CEIOPS (Committee of European Insurance and Occupational Pensions Supervisors):

- 24 May 2007: public consultation on a joint 3L3 Committee (CEBS-CEIOPS-CESR) impact assessment;
- 28 January 2008: joint consultation with CEIOPS on the recommendations of the Interim Working Committee on Financial Conglomerates (IWCFC) on the capital of financial conglomerates.

2.1.1. CEBS – *Groupe de contact*

Since its inception in 1972, the *Groupe de Contac*t has been used as forum for informal co-operation between banking supervisory authorities at EU level. Following the enlargement of the European Union, it now also comprises the representatives of the new Member States' authorities. The *Groupe* is chaired by Mr Jukka Vesala (Financial Supervision Authority, Finland) since the end of 2006.

Within the new European banking supervisory structure, the *Groupe* henceforth acts as general working group of the Committee of European Banking Supervisors. In that capacity, it assists CEBS in order to achieve convergence of the prudential supervisory practices in the European Union. The *Groupe* also continues to be a platform appreciated for informal exchanges concerning the situation of individual credit institutions, particularly in the event of problems. It follows the development of national regulations, discusses practical aspects of prudential supervision of credit institutions and conducts general comparative studies.

The *Groupe* continues to focus on the implementation of the supervisory review process, Pillar 2 of the new capital adequacy framework, on the convergence and on the co-operation between supervisory authorities. In this context, it must be pointed out that a great deal of efforts has been made by its subgroup Supervisory Operational Network (SON) to achieve closer co-operation between supervisory authorities for the major banking groups.

Another important part of the *Groupe*'s responsibilities concerns the exchange of information regarding specific problems encountered by one or several authorities on topical issues. This exchange of information between members, as well as between the *Groupe* and CEBS, continued in 2007.

- ***Groupe de contact - Task Force on Liquidity Risk Management***

On 5 March 2007, CEBS received a call for advice from the European Commission on liquidity risk management, covering two areas, namely a survey of the regulatory frameworks adopted and an in-depth analysis of selected topics related to liquidity risk management.

The working group delivered the report of the survey of regulatory frameworks adopted by EU Member States in June 2007. Given the turmoil in markets at the end of summer 2007, especially as regards liquidity, the working group deferred the works relating to the second part of the call for advice and focused, at CEBS' express request, on analysing liquidity risk management practices of banks during that period. The group submitted its report on these practices and their efficiency in November 2007.

Since the third quarter of 2007, the task force has been analysing specific factors affecting liquidity risk and its management, by reviewing in particular collateral management, the interaction between the liquidity financing risk and the market liquidity risk, the use of internal bank liquidity risk management methods and the impact of the developments of payment and settlement systems on liquidity risk.

- ***Groupe de contact - Crisis Management Task Force (CMTF)***

The working group's objective is to study the existing crisis management practices and co-operation between supervisory authorities in order to identify the best practice in this field, and to provide recommendations in view of harmonising practices.

2.1.2. CEBS - Expert Group on Capital Requirements (EGCR)

In 2007, the work of the EGCR, one of the three permanent CEBS sub-working groups, focused mainly on "own funds" and "large exposures" within the subgroups Working Group on Own Funds and Working Group on Large Exposures that are presented below.

At the request of the European Commission, the group created the subgroup Working Group on Options and National Discretions (WGOND) to look into a possible harmonisation of national discretions under Directives 2006/48/EC and 2006/49/EC.

- ***EGCR Working Group on Own Funds***

Under a mandate given by the European Commission in June 2005, the working group carried out a quantitative analysis of the elements of own funds held by EU credit institutions. A more detailed analysis focused on Tier 1 hybrid instruments. These surveys were published in June 2007 and March 2007 respectively. Following the quantitative survey on hybrid instruments, the European Commission, together with the European Banking Committee (EBC), invited CEBS in a letter of 10 April 2007 to consider whether further convergence can be achieved in the regulatory treatment of those instruments across Europe.

The working group thus defined harmonised criteria concerning the main characteristics of hybrid instruments, namely:

- the loss absorbency of hybrid instruments;
- the permanence of hybrid instruments;
- the flexibility of payments to be made by the issuer of hybrid instruments.

Moreover, the group made proposals for the limitation of the inclusion of Tier 1 hybrid instruments into original own funds of credit institutions. The group also dealt with the appropriate grandfathering of already issued instruments that would not comply with the new criteria.

The industry was involved in the different work levels, notably through open hearings and bilateral meetings with investment banks and rating agencies. In December 2007, CEBS published a public consultation paper on harmonised criteria. The public consultation ended in February 2008 and the final advice was transmitted to the European Commission in March 2008.

- ***EGCR Working Group on Large Exposures***

The discussions of the working group relate to the second call for advice on large exposures received from the European Commission in 2006. With a view to an in-depth recast of the large exposure regime, CEBS was invited to analyse, among other things, the purpose of the large exposure regime, whether or not credit risk should be taken into account to a greater extent, the adequacy of current limits, as well as the determination of exposure values. Moreover, the call for advice also covered the reporting framework of large exposures, credit risk mitigation and the treatment of intra-group exposures, as well as interbank exposures.

This call for advice is part of the "Better Regulation" agenda of the European Commission and is a pilot project for CEBS as regards the application of the Impact Assessment Guidelines developed by the three level 3 committees (3L3).

The industry was consulted throughout the drafting of CEBS' technical advice. Public hearings were held and a work session organised with representatives of European banking federations.

The first part of CEBS' technical advice was submitted to public consultation in summer 2007 and published on 6 November 2007. The public consultation on the second part of CEBS' technical advice started on 7 December 2007 and ended on 22 February 2008. CEBS submitted its final advice to the European Commission in March 2008.

2.1.3. CEBS - BSC Joint Task Force on the Impact of the new Capital Framework (TFICF)

The task force's mission tallies with that of the Capital Monitoring Group established at Basel Committee level, although the circle of countries that participate in the regular analysis of the development of own funds and regulatory capital requirements is limited to EU Member States as far as the task force is concerned.

2.1.4. CEBS - CESR - CEIOPS Cross-Border Mergers and Acquisitions Task Force

In 2007, CEBS mandated a new working group to perform certain works to ensure consistent implementation of the prudential provisions introduced by Directive 2007/44/EC. The working group was converted in January 2008 into a joint 3L3 group.

The purpose of the working group is to define, on the one hand, the common principles concerning the proportionate information to be requested by the supervisory authorities of EU Member States for the prudential assessment of mergers and acquisitions and, on the other hand, all the procedures and processes in view of a close co-operation of the different authorities in the assessment of the acquirer. In addition, the working group issues recommendations in order to be able to implement a common interpretation as regards the assessment criteria set down by Directive 2007/44/EC.

2.1.5. CEBS - Expert Group on Financial Information (EGFI)

The working group assists CEBS in achieving its work programme as regards financial information, including the fields of accounting, prudential reporting and auditing.

The main activities of EGFI's three working subgroups are set forth below.

- ***CEBS - EGFI Subgroup on Accounting***

As regards accounting standards, the subgroup drew up comment letters for the International Accounting Standards Board (IASB) in response to the call for comments of the latter on the discussion paper "Preliminary Views on Insurance Contracts" and on the "Statement of Financial Accounting Standard 157, Fair Value Measurements (SFAS 157)" of the US accounting standard setter, the Financial Accounting Standards Board (FASB). These comment letters are available for consultation on CEBS' website (www.c-ebs.org/comment_letters/intro.htm).

Moreover, CEBS published a report drawn up by the subgroup detailing the findings of an analysis with regard to prudential filters in October 2007[1]. The purpose of this report is to assess the compliance of supervisory authorities' filters with the guidelines published by CEBS in December 2004 and to present their impact in quantitative terms on regulatory own funds. It also provides a basis for discussion on the possible scope for further convergence of these filters in the EU. A public hearing was held on 16 October 2007 to discuss the report and its conclusions. The report is available on CEBS' website (www.c-ebs.org/press/05102007_prudentialfilters.htm).

[1] In December 2004, CEBS issued guidelines on the use of prudential filters for regulatory capital. The objective of these prudential filters is to maintain the definition and quality of regulatory capital for institutions using IFRS for prudential reporting.

- ***CEBS - EGFI Subgroup on Reporting***

The subgroup sees to the proper transposition of the guidelines and standards published by CEBS on the common European reporting frameworks FINREP and COREP, including the development of XBRL taxonomies (eXtensible Business Reporting Language), and proposes, if necessary, updates of the reporting schemes. As regards the common framework FINREP, the subgroup assesses in particular the impact of the amendments to the relevant international accounting standards on the banking sector.

The versions of the common reporting frameworks FINREP and COREP in force were published by CEBS on 24 July 2007 and 16 October 2006 respectively and are available on CEBS' website (www.c-ebs.org/standards.htm).

The subgroup also answers questions concerning the practical application regarding the implementation of the FINREP and COREP frameworks. The answers to these questions are available on CEBS' website (www.c-ebs.org/implementationquestions).

The subgroup participated in drawing up a questionnaire for the study "Assessment of convergence on Supervisory Reporting" whose aim is to identify the level of convergence achieved with respect to harmonised reporting frameworks among the Member States. The study was published on 8 October 2007 and is available on CEBS' website (www.c-ebs.org/standards.htm).

- ***CEBS - EGFI Subgroup on Auditing***

The subgroup monitors the developments at Community and international level in the area of audit and statutory audit in order to assess the consequences thereof from a banking supervisory standpoint.

In 2007, the subgroup continued its work with respect to international accounting standards and prepared 17 comment letters for the International Auditing and Assurance Standards Board (IAASB) concerning ISA standards that are being revised under the "Clarity Project"[2] and proposed amendments to other standards. These comment letters are available for consultation on CEBS' website (www.c-ebs.org/comment_letters/Auditing.htm).

2.2. Committee of European Securities Regulators (CESR)

Established under the terms of the European Commission Decision of 6 June 2001, CESR (Committee of European Securities Regulators) took over from FESCO (Forum of European Securities Commissions) in September 2001. CESR is one of the two committees envisaged in the Committee of Wise Men's Report, which was endorsed by the Stockholm resolution of 23 March 2001. Composed of representatives of 29 supervisory authorities of securities markets in the European Economic Area (Member States of the European Union, Norway and Iceland), CESR is an independent body, which assists the European Commission in preparing implementing measures relating to Community legislation on transferable securities, and is entrusted with ensuring the timely implementation of Community legislation in the Member States. CESR also works towards improving coordination among supervisory authorities. Since January 2007, Mr Eddy Wymeersch (Commission bancaire, financière et des assurances, Belgium) chairs CESR. Mr Carlos Tavares (Comissão do Mercado de Valores Mobiliários, Portugal) is CESR's Vice Chairman.

CESR continued its Level 3 works by drawing up recommendations, standards, common interpretations and procedures for the co-operation in different areas in order to enhance regulatory convergence within the EU.

[2] Proposed amendments to the Preface to the International Standards on Quality Control, Auditing, Assurance and Related Services and the four proposed redrafted ISAs (The Clarity project).

In order to develop a common approach among supervisory authorities, CESR adopted a report on the human resources network in May 2007 to facilitate the exchange of staff between members by means of temporary secondments and study visits.

In order to protect investors, CESR worked on the project "Investor's corner" which will be integrated into CESR's website. This portal will allow cross-border retail investors to have access to useful information.

CESR also kept up its contacts with CEBS and CEIOPS according to the joint protocol signed on 24 November 2005 in order to take into account the sectoral market integration and the interrelationship of financial activities within the European Union.

Moreover, CESR continued discussions with the SEC (Securities and Exchange Commission) in different areas. In September 2007, CESR thus published a framework protocol covering the exchange of confidential information regarding listed companies in an EU Member State and in the Unites States. The purpose of the framework protocol is to facilitate the negotiation and the conclusion of a bilateral agreement between individual CESR members on the one hand and the SEC on the other, in order to enable close co-operation between parties as regards US GAAP and IFRS application in the relevant States. In addition, CESR began discussions with the SEC on the mutual recognition of regulatory regimes of financial markets.

CESR also submitted its contribution on the evaluation of the Lamfalussy process to the European institutions in November 2007, concerning in particular a proposal relating to the strengthening of the European supervision of financial markets beyond 2007.

The Market Consultative Panel, a committee comprising 15 market participants appointed in a personal capacity, established in 2002 following a suggestion of the European Parliament and the Committee of Wise Men, is charged with assisting CESR. The panel's three 2007 meetings addressed in particular takeover bids, transparency and disclosure rules applicable to hedge funds, public oversight of auditors, the needs and costs of a public oversight board, corporate governance, CESR's role in evaluating the Lamfalussy procedure, general discussions on the developments in financial markets, the transatlantic dialogue CESR/US SEC, as well as CESR's 2008 work programme.

2.2.1. Groups established within CESR

- ***CESR MiFID Level 3 Expert Group***

In order to guarantee an efficient and convergent implementation of the framework Directive and its implementing measures in accordance with the Lamfalussy procedure, CESR set up a MiFID Level 3 expert group in 2006.

The expert group dealt with technical and operational Level 1 and 2 issues for which a consistent and convergent interpretation and application had to be achieved before the implementation of the MiFID Directive on 1 November 2007, in order to provide European operators with greater certainty as regards their strategies.

The MiFID requires the European Commission to provide, among others, a certain number of analyses and reports on instruments and financial markets. At the request of the European Commission, the expert group notably discussed the possible extension of the transparency regime to transactions in classes of financial instruments other than shares.

The expert group is assisted by two working groups for the preparation of guidelines, namely the Intermediaries group and the Markets group. An Implementation forum was set up to assist the relevant authorities in the implementation of MiFID regulations.

As regards "**Intermediaries**", the following documents were finalised for their approval by CESR's Chairmen:

- The papers on the use of the European passport (Ref.: Passport under MiFID - Recommendations for the implementation of the Directive and Statement on practical arrangements regarding the late transposition of MiFID - 07-337b; Protocol on MiFID Passport Notifications - revised - 07-317b) setting out practical proposals to facilitate, among other things, the notification procedures for cross-border services, as well as for the establishment of branches. Moreover, CESR members signed a Protocol on the supervision of branches in order to ensure the future collaboration of host and home authorities to allow adequate supervision of the proper application of the rules of conduct and the organisational requirements of investment firms that use the passport (Ref.: Protocol on the supervision of branches under MiFID - 07-672).
- A paper on inducements (Ref.: Recommendations - Inducements under MiFID - 07-228b), which allowed to clarify the relation of this regime with the rules governing conflicts of interest. It also allowed to define the circumstances in which investment firms may receive from third parties fees or other benefits in relation to the provision of investment services and, finally, to illustrate *via* concrete examples, the compatibility of certain practices with the MiFID Directive.
- Details have been provided as regards Best Execution, in particular on the application of this requirement in specific situations, such as trading on own account based on proposed prices (Ref.: Q&A on Best Execution - 07-320).

As regards "**Markets**", a paper on the publication and consolidation of trade information that trading systems have to publish in accordance with MiFID in order to preclude obstacles which may prevent the data consolidation at European level was finalised in February 2007 (Ref.: CESR's Level 3 Guidelines and recommendations on Publication and Consolidation of MiFID market transparency data - 07-043).

As far as transparency is concerned, the group responded to the second call for assistance of the European Commission regarding the possible extension of the scope of the MiFID provisions concerning pre- and post-trade transparency obligations to transactions in classes of financial instruments other than shares (Ref.: Technical advice on Non-equities transparency - 07-284b).

The group finalised its works on transaction reporting, and more specifically on transaction reports to be made by branches of investment firms, on the definition of "execution of a transaction" as well as on the approval of the reporting channels (Ref.: Guidelines - CESR Level 3 Guidelines on MiFID Transaction Reporting - 07-301). The group co-operated actively with CESR-Tech which deals with the technical aspect of transaction reporting.

The group also participated in the definition and the setting-up of a public database containing information on shares admitted to trading on a regulated market of the European Union, as well as the lists of systematic internalisers, regulated markets, multilateral trading facilities (MTF) and central counterparties. A consultation paper was published in December 2007 in order to collect the interested parties' opinion on aspects regarding the improvement of the content and search functions of the database (Ref.: Consultation Paper on Improving the functioning of the MiFID database - 07-832).

- ***CESR Expert Group on Investment Management***

In 2007, the expert group, chaired by the Chairman of the Italian Commissione Nazionale per le Società e la Borsa (Consob), has in particular worked on the following three areas:

- clarification of definitions concerning eligible assets for UCITS;
- changes to the regime applying to simplified prospectuses (Key Information Document);
- operational prudential supervision (Operational Task Force).

Three working groups have been created to specifically treat these subjects. The CSSF took part in the work of the expert group as well as in that of the three sub-working groups. These groups met 20 times in 2007 in total.

The expert group is assisted by a consultative group consisting of 16 industry experts, including one representative of the Luxembourg investment fund sector. In 2007, one meeting was held between the expert group and the consultative group.

The expert group also discussed the proposed amendments to the UCITS Directive on several occasions. The European Commission announced that a proposal for a Directive, to be called UCITS IV, will be published in April 2008.

Working group dealing with the clarification of the definitions concerning eligible assets for UCITS

The working group, under the coordination of the British Financial Services Authority (FSA) and the French Autorité des Marchés Financiers (AMF), finalised its works in 2007.

Following the works already achieved in 2006, the working group notably addressed the question whether derivative financial instruments on hedge fund indices may constitute eligible assets for investment by UCITS. CESR published a consultation paper on this subject and held an open hearing in 2007. At the close of the consultation procedure and following discussions at the level of the working group and the Expert Group on Investment Management, CESR concluded that derivative financial instruments on hedge fund indices can constitute eligible assets for UCITS.

Based on the works of the Expert Group on Investment Management on the clarification of definitions concerning eligible assets for investment by UCITS, the European Commission adopted Directive 2007/16/EC of 19 March 2007 implementing Directive 85/611/EEC on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) as regards the clarification of certain definitions. This Lamfalussy Level 2 Directive is available on the European Commission's website (http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2007:079:0011:0019:EN:PDF).

In the context of clarification of definitions concerning eligible assets for investment by UCITS, CESR adopted two Level 3 texts which include the guidelines applicable in this field. The texts "CESR's guidelines concerning eligible assets for investment by UCITS" (Ref.: 07-044) and "CESR's guidelines concerning eligible assets for investment by UCITS - The classification of hedge fund indices as financial indices" (Ref.: 07-434) are available on CESR's website (www.cesr.eu).

It has been decided that Directive 2007/16/EC and CESR guidelines must enter into force simultaneously as a package. In Luxembourg, Directive 2007/16/EC was transposed by Grand-ducal regulation of 8 February 2008 on certain definitions of the law of 20 December 2002 on undertakings for collective investment, as amended, and transposing Directive 2007/16/EC of 19 March 2007 implementing Directive 85/611/EEC on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) as regards the clarification of certain definitions.

Working group concerning the Key Information Document

This working group, coordinated by the British Financial Services Authority (FSA) and the French Autorité des Marchés Financiers (AMF), was set up following two workshops on simplified prospectuses organised by the European Commission in 2006. Following those workshops in which the CSSF participated as active member, the European Commission decided to reconsider the issue of simplified prospectus and investor information from another angle in order to improve UCITS investor information.

The European Commission specified that it intended to replace the simplified prospectus by a document containing key information on UCITS. It was decided to name this document Key Information Document (KID) and it is planned that the amended UCITS Directive requires that this document be given (and not only offered) to investors before subscription. In this context, the European Commission requested assistance from CESR on the form and content of the KID.

CESR prepared a consultation paper on the KID and held an open hearing.

On 15 February 2008, CESR released its advice on the content and form of the KID. In its advice, which is available on CESR's website (www.cesr.eu, Ref.: 08-087), CESR recommends that the KID should be a single document with a maximum of two pages, and that the presentation should follow a standardised format of subjects in a given order. CESR recommends that the KID be as harmonised as possible and that no other information as that requested should be included in the KID.

On a certain number of points, CESR's advice presents two options that will be tested with investors in order to assess their comprehension of certain elements. In particular, CESR's advice sets out different options for the content of the KID, the fee structure, the presentation of past performance and the risks. CESR considers introducing a synthetic risk indicator.

Testing with investors will take place in 2008. CESR's final advice is expected in spring 2009 and will be based on the test results and on the comments and responses of investors and representatives of the UCITS industry.

Operational Task Force

This working group, coordinated by the Italian Commissione Nazionale per le Società e la Borsa (Consob), was created to strengthen co-operation between financial supervisory authorities with respect to the practical and operational aspects of prudential supervision.

The group's works aim to achieve convergence of the CESR members' prudential supervision of investment funds. The group conducted a questionnaire-based mapping exercise to better understand the relevant approaches of CESR members in the field of prudential supervision of investment funds. The group also started works in the context of risk management and risk assessment procedures. Moreover, it discusses innovating funds and the interpretation of the UCITS Directive.

It is foreseen to publish the major decisions of this group relating to the interpretation of the UCITS Directive on CESR's website.

- ***CESR Expert Group on Transparency***

Having responded already in 2006 to all the calls for advice it had received from the European Commission, the expert group reoriented its activity in 2007. The new focus of the working group thus became the transposition and implementation of Directive 2004/109/EC of 15 December 2004 on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market and amending Directive 2001/34/EC (Transparency Directive, Level 1 Directive), as well as of Directive 2007/14/EC of 8 March 2007 laying down detailed rules for the implementation of certain provisions of Directive 2004/109/EC (Level 2 Directive).

Thus, a call for evidence was published in July 2007, requesting the public's views regarding the possible Level 3 work under those Directives. The majority of the 21 responses having been in favour of such Level 3 work, CESR approved a new mandate for the expert group during its October 2007 meeting. The newly structured group then defined the following Level 3 work streams:

- a mapping exercise with the purpose of drawing up a comparative table on the transposition of the Transparency Directive in Member States;
- discussion of practical questions with respect to the Level 1 and Level 2 Directives in order to achieve common approaches where possible;
- the establishment of an EU electronic network of Member States' officially appointed mechanisms for the storage of regulated information required by the Transparency Directive.

- ***CESR Expert Group on Credit Rating Agencies***

On 4 January 2007, CESR released its first report to the European Commission on the compliance of credit rating agencies with the IOSCO Code (CESR/06-545). The report provides a clear analysis of the four credit rating agencies that have chosen to adhere to the voluntary framework in relation to the IOSCO Code.

On 7 May 2007, CESR received a formal request from the European Commission to prepare a second report by the end of 2007. This deadline was postponed to 30 April 2008.

In this context, CESR worked in particular on analysing the rating process as regards structured finance instruments (e.g. quality of the rating process, conflicts of interest). To this effect, CESR published a questionnaire on 22 June 2007 regarding the rating of structured finance instruments, in order to gather information from interested parties on this specific segment of the credit rating business. The responses to this questionnaire were published on 24 August 2007.

On 11 September 2007, having regard to the subprime crisis, the European Commission submitted an additional request to CESR to review the role of credit rating agencies, in particular in the following areas:

- transparency of rating methodologies;
- human resources allocated to rating and monitoring;
- periodic monitoring of ratings and timeliness of rating decisions;
- potential conflicts of interest (e.g. remuneration of credit rating agencies).

The responses of the four credit rating agencies to the list of questions received from CESR in November 2007 were published on 13 December 2007 on CESR's website.

- ***CESR-Tech***

The purpose of CESR-Tech is to strengthen CESR's information technology governance structure. This group enables CESR to work on IT-related issues more quickly and efficiently and to manage IT projects that CESR undertakes in conjunction with its members. CESR-Tech has thus been established to deal with any form of pan-EU IT projects stemming from EU legislation (either current or future) and any other area where CESR members consider it necessary or useful to work together on IT issues.

CESR-Tech is composed of senior CESR representatives who have experience, knowledge and expertise in IT project management, financial markets and supervisory related issues.

The main tasks of CESR-Tech are:

- allocation and use of the IT budget on a project-by-project basis;
- operational issues related to the management and running of IT projects;
- technical issues that arise during the course of specific projects;
- setting-up of operational working methods necessary to achieve its objectives.

The major CESR-Tech project that started in June 2006 and concerned the exchange of transaction reporting between CESR members in accordance with article 25 of the MiFID Directive, led to the setting-up of the Transaction Reporting Exchange Mechanism (TREM).

The hub, operated by CESR's secretariat, became operational on 1 November 2007. On that date, the majority of authorities started exchanging transactions on a daily basis. Some authorities were unable to join on time because of gaps in their national reporting framework. The CSSF started exchanging as from the first day.

The TREM project is evolving, in particular to allow exchanges of transactions on derivative instruments, for which consensus was reached with the industry in order to determine a single identifier for every instrument, called Alternative Instrument Identifier (AII).

At the end of 2007, CESR-Tech started to define identifiers for reported securities which must be used as single basis to identify the securities and authorities concerned. Indeed, the diversity of instruments and characteristics do not allow, *a priori*, to find a unique reference database with a provider at reasonable costs. The project consists in constructing the reference database based on the data collection at every authority knowing the securities it supervises.

- ***Prospectus contact group***

In 2007, the contact group continued its main mission which is to ensure a consistent and convergent implementation of the European provisions relating to prospectuses for securities. To this effect, its members continued to meet on a quarterly basis to discuss the practical application of the Prospectus Directive and its implementing Regulation. The creation of an Agenda sub-working group, in which the CSSF took part and which is in charge of preparing the topics to address in the contact group's plenary meetings, facilitated and sped up discussions.

The works and various consultations, among the authorities or of the public, initiated by the contact group in 2007 led to the following publications, which are available on CESR's website (www.cesr.eu):

- publication of the common positions agreed by CESR members on issues regarding the implementation of the Prospectus Directive, *via* three updates of the CESR FAQs on 16 February, 21 September and 20 December 2007;

- publication of a detailed report on the functioning of the Prospectus Directive on 13 June 2007;
- publication of a list of national requirements regarding notifications on 13 December 2007, allowing issuers to verify that they met all the conditions (language, translation of the summary, etc.) so that the notification may be made without problems.

Moreover, at the European Commission's request, the contact group was mandated to take a common position with respect to employee share schemes. In December 2007, a press release was published to inform market participants on those works and to invite them to submit their advice by 31 January 2008.

- ***Takeover bids network***

Two meetings regarding the practical implementation of Directive 2004/25/EC of 21 April 2004 on takeover bids were held in Paris on 15 March and 4 July 2007. CESR had invited the representatives of the authorities responsible for takeover bids in their Member State, whether CESR members or not, in order to discuss any practical issues arising from the application of this Directive. Thus, the creation of a European network of experts in this field is planned to allow the exchange of experiences and discussions in the areas that require the most co-operation.

- ***CESR Review Panel***

Established following the decision of CESR's Chairmen in December 2002, the Review Panel is responsible for assisting CESR in its task to ensure consistent and harmonised implementation of EU legislation in the Member States.

On 1 April 2007, the Review Panel published its protocol setting out the role of the Review Panel, the purpose of its work, its working procedures, as well as the commitment of CESR member authorities to ensure that the Review Panel fulfils its role. The main role of the Review Panel is to monitor the consistent and timely implementation of Community legislation and CESR measures with the purpose of fostering a common and uniform day-to-day application and enhancing supervisory convergence within the European Economic Area.

The Review Panel continued its mapping of the powers of the supervisory authorities under the Market Abuse Directive and the Prospectus Directive. The reports and conclusions were published on 21 June 2007. The reports also describe the daily exercise of the supervisory powers by the competent authorities in order to achieve a supervisory convergence. The results of the reports were presented to the Financial Services Committee (FSC).

In addition, the Review Panel started its peer review of the transposition and application of CESR's guidelines to simplify the notification procedure of UCITS.

Lastly, the Review Panel was given mandate by CESR's Chairmen to revise CESR standards, guidelines and recommendations (CESR standards) in the light of the legislative texts of the Financial Services Action Plan (FSAP). The work concerned the analysis of CESR standards in order to identify whether they are fully covered by a FSAP legislative text and can thus be abolished, or whether the standards must be kept as they are, updated or repealed as they have become obsolete.

These reports are available on CESR's website (www.cesr.eu).

2.2.2. Operational groups established within CESR

- ***CESR-Fin***

As CESR member, the CSSF takes part in the meetings of CESR-Fin, the permanent operational committee that coordinates CESR's work in all financial reporting areas in Europe.

In 2007, CESR-Fin met four times and its activities can be summarised as follows.

Joint CESR-SEC sessions

CESR-Fin's activities include regular meetings with the SEC, the financial reporting supervisory authority of the United States. As many European companies are also listed in the United States, co-operation and discussion with the SEC are essential in order to avoid diverging interpretations of the IAS/IFRS standards. To this end, a co-operation protocol between the SEC and CESR-Fin members is still being discussed.

Equivalence and convergence of accounting standards

The assessment of equivalence of accounting standards of certain third countries with IAS/IFRS standards, as required by the Transparency Directive and the Prospectus Directive, is a lengthy project which continued throughout 2007.

Following Commission Decision (EC) No 2006/891/EC of 4 December 2006 and by virtue of Regulation (EC) No 1787/2006 of 4 December 2006, CESR received a call for advice from the European Commission on the equivalence of accounting standards in certain countries under the Transparency and Prospectus Directives.

In accordance with this mandate, CESR submitted on 6 March 2007 a first advice to the European Commission on the work programmes of the Canadian, Japanese and US standard setters, the definition of equivalence and the list of third-country GAAPs currently used on the EU capital markets.

On 25 May 2007, CESR published its second advice to the European Commission on a mechanism for determining the equivalence of the generally accepted accounting principles of third countries, following which the European Commission published Regulation (EC) No 1569/2007 of 21 December 2007. This Regulation provides that third-country issuers may continue to prepare their financial statements according to national GAAP other than IFRS until 31 December 2011 at the latest, if certain conditions are complied with, such as the existence of a convergence programme.

The European Commission must deliver a report on the equivalence of third-country GAAPs by 1 April 2008. Finally, it must ensure that by 30 June 2008, the necessary analyses of third-country GAAPs to be assessed for equivalence purposes have been completed in accordance with the definition and mechanism of equivalence.

In line with the foregoing, CESR published a consultation paper on the equivalence of Chinese, Japanese and US GAAPs on 18 December 2007.

European Enforcers Coordination Sessions (EECS)

EECS, which met eight times in 2007, continued to discuss the practical and technical issues that arise from the day-to-day enforcement of financial reporting in each jurisdiction.

As in the previous years, the competent authorities for the enforcement of the correct application of the IFRS standards continued in 2007 to feed the database with decisions taken at a national level and/or accounting topics that gave rise to discussions.

In December 2007, CESR published a second extract from the EECS database containing 11 decisions taken with respect to financial information enforcement.

CESR-Fin activities at EU level

CESR-Fin continued to closely follow the discussions of the European Commission at ARC level (Accounting Regulatory Committee) on subjects such as the amendments of standards and new draft standards, as well as the discussions at AuRC/EGAOB level.

Moreover, CESR-Fin took an active part in the meetings of the temporary Round table set up by the European Commission and acting as informal Forum of professionals and European accounting experts to rapidly identify emerging accounting issues and potential concerns requiring the intervention of the regulator (IASB/IFRIC).

Auditing

CESR-Fin closely follows the developments of the legislation relating to the auditing of companies listed in the European Union and in the other main jurisdictions.

In particular, CESR-Fin decided to closely follow the work of or to participate in the new working group created by the international standard-setter IAASB, i.e. the Task force on auditing standards for prospectus reporting.

The different working groups created in the wake of the eighth Directive on audit continued their work on the assessment of the equivalence of auditor supervision in third countries.

Moreover, CESR approved the conclusions of the survey on the direct communication of auditors with the public on the statutory audit of annual accounts or consolidated accounts of listed companies. The report is available on CESR's website.

The consultations of the European Commission on the responsibility of auditors and on the impact on European capital markets, as well as on the implementation of articles 45 to 47 of Directive 2006/43/EC relating to the co-operation with third countries on the oversight of auditors, are dealt with in comment letters drawn up by CESR.

- ***CESR-Pol***

CESR-Pol's purpose is to enhance sharing of information, co-operation and coordination of supervision and enforcement activities between CESR members. A major priority of CESR-Pol is to ensure the effective day-to-day implementation of the Market Abuse Directive at Level 3 of the Lamfalussy process.

In accordance with its work programme published on 26 July 2007, CESR-Pol started more detailed work on the list of insiders to foster harmonisation at European level, suspicious transactions reporting, stabilisation and buy-back regimes as provided for in Regulation (EC) No 2273/2003 and the two-fold notion of inside information contained in Directive 2003/6/EC on insider dealing and market manipulation.

Moreover, based on a mandate received from CESR's Chairmen, CESR-Pol started to draw up a technical report on the functioning of Directive 2003/6/EC and the European Commission's Directives and implementing Regulation (Market Abuse Directive). CESR's technical report will be used in the preparation of the Commission's report on the proper operation and on the deficiencies of that Directive.

On 22 November 2007, CESR-Pol published a report on the administrative measures and sanctions, as well as criminal sanctions applicable in CESR's Member States following the entry into force of Directive 2003/6/EC.

The permanent work group **Surveillance and Intelligence Group** (S & I Group), set up in 2005, allowed to exchange practical experience in co-operation, daily supervision of investment firms and financial markets and unauthorised offers of financial services by persons or investment firms that have not been granted adequate authorisation. CESR-Pol has also continued to establish an **Urgent Issues Group** every time several authorities of different Member States are involved in an investigation and it became necessary to ensure swift co-operation and to take prompt measures in cases of threats to one or several securities markets.

Furthermore, CESR-Pol continued to develop its network for the dissemination of warnings relating to illicit offers of financial services by investment firms or individuals that have not been granted the required authorisations.

CESR-Pol has also continued to enhance its dialogue with IOSCO in order to improve co-operation and exchange of information with non-co-operative countries and to coordinate the measures to be taken in this respect. The report and work programme are available on CESR's website (www.cesr.eu).

2.3. Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS)

The Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS) comprises high level representatives from the insurance and occupational pensions supervisory authorities from EU Member States. The Committee's objectives are to advise the European Commission, either at the European Commission's request or on the Committee's own initiative, as regards the preparation of implementing measures in the fields of insurance, reinsurance and occupational pensions, to contribute to the consistent implementation of EU Directives and to the convergence of Member States' supervisory practices and to constitute a forum for supervisory co-operation, including the exchange of information on supervised institutions.

Additional explanations on the works performed in 2007 by CEIOPS are given in Chapter 3 "Supervision of pension funds".

2.4. Capital Requirements Directive Transposition Group (CRDTG)

Established in December 2005, the purpose of the group is to provide all interested parties with responses as regards the implementation and interpretation of Directives 2006/48/EC and 2006/49/EC that transpose Basel II into European legislation. To this end, the European Commission and its working group co-operate closely with CEBS.

The answers prepared by the group have been published on the website of the European Commission (http://ec.europa.eu/internal_market/bank/regcapital/transposition_en.htm).

2.5. Capital Requirements Directive Working Group (CRDWG)

The European Commission set up the Working Group on the Capital Requirements Directives 2006/48/EC and 2006/49/EC in order to discuss with the Member States the amendments it wishes to make to those Directives. The group's first meeting was held in November 2007, followed by a series of meetings in 2008. Discussions mainly concerned the following three areas:

- Tier 1 hybrid instruments: the European Directives currently do not address these instruments which were recognised by the Basel Committee on Banking Supervision through a press release in 1998;
- large exposures: the European Commission and the Member States decided on an in-depth recast of the large exposure regime in 2006;
- enhanced co-operation between authorities in the field of crisis management and technical amendments to Directive 2006/48/EC.

2.6. Committee on the prevention of money laundering and terrorist financing

The Committee on the prevention of money laundering and terrorist financing was established by Directive 2005/60/EC of 26 October 2005 on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing. The Committee assists the European Commission in relation with the implementing measures for Directive 2005/60/EC.

The Committee held five meetings in 2007. Its works referred, among others, to the practical implementation of Directive 2005/60/EC and the follow-up of the works of the Financial Action Task Force (FATF).

2.7. CEBS-CEIOPS-CESR Task Force on Anti-Money Laundering Issues

The Task Force on Anti-Money Laundering Issues, created in September 2006, met four times in 2007. This task force is an intersectoral working group that gathers the representatives of the Member States' supervisory authorities and assists the 3L3 committees (CEBS, CEIOPS and CESR) on issues relating to the implementation of Directive 2005/60/EC of 26 October 2005. The task group continued to work on issues relating to the practical implementation of the risk-based approach in the field of Know Your Customer and Customer Due Diligence and worked on issues concerning the implementation of Regulation (EC) No 1781/2006 of 15 November 2006 relating to the information on the payer accompanying transfers of funds.

2.8. Accounting Regulatory Committee / Contact Committee on Accounting Directives

The objective of the Accounting Regulatory Committee (ARC), established by the European Commission in accordance with Article 6 of the IAS Regulation, is to provide advice on the proposals of the European Commission in order to adopt one or several international accounting standards IAS/IFRS of the International Accounting Standards Board (IASB).

In 2007, the Accounting Regulatory Committee met six times, together with the Contact Committee on Accounting Directives, instituted under article 52 of the fourth Company Law Directive (Directive 78/660/EEC). These meetings mainly addressed the adoption of the IASB standards, the discussions of the Round Table for a consistent application of the IAS/IFRS standards within the European Union, as well as the convergence between the IAS/IFRS standards and third-country GAAPs, in particular US GAAP.

The current status of the approval process of the international accounting standards in the European Union, as well as the works of the Accounting Regulatory Committee are available on the European Commission's website (http://europa.eu.int/comm/internal_market/accounting/ias_en.htm) as well as the summary records of the meetings (http://ec.europa.eu/internal_market/accounting/committees_en.htm).

2.9. European Group of Auditors' Oversight Bodies (EGAOB)

The European Group of Auditors' Oversight Bodies (EGAOB) was established by Decision 2005/909/EC of 14 December 2005 of the European Commission. The expert group advises the European Commission on any issue relating to the preparation of measures implementing the modernised eighth Directive on statutory audit of annual accounts and consolidated accounts and amending Directives 78/660/EEC and 83/349/EEC. It also provides technical support for the setting-up of comitology measures, in particular with respect to issues relating to the assessment and approval of international audit standards in view of their adoption at Community level, the assessment of third-country public oversight systems, as well as international co-operation between Member States and third countries in this area. In addition, the group is also an exchange platform for representatives of auditors and supervisory authorities of third countries. In 2007, the group met with representatives

of different European auditor organisations (FEE, ECG, EGIAN, EFAA), as well as with the authorities of the United States (PCAOB) and Japan (JFSA).

The group's summary records are available on the European Commission's website (http://ec.europa.eu/internal_market/auditing/egaob/index_en.htm).

The expert group has set up sub-working groups whose main activities are set forth below.

2.9.1. EGAOB - Subgroup on Co-operation

The objective of this subgroup is to facilitate co-operation between public auditors' oversight bodies at Community level and between European and third-country regulators.

In 2007, the subgroup continued analysing the equivalence of public oversight systems for third-country auditors of companies established outside the European Union and whose securities are admitted to trading on European regulated markets. The assessment of the equivalence, under article 46 of the amended eighth Directive, aims to exempt, on the basis of reciprocity, third-country auditors from EU registration requirements, public oversight, quality assurance and investigations and penalties. In addition, in order to avoid over-regulating the audit sector which would be likely to increase the costs of supervision and to undermine the EU markets' attractiveness for third-country issuers, the subgroup is currently discussing several approaches to organise co-operation between Member States as regards registration of third-country auditors that are found not to comply with the requirements of the eighth amended Directive.

2.9.2. EGAOB - Subgroup on International Auditing Standards (ISAs)

As the modernised eighth Directive requires the application of international audit standards within the scope of statutory audit, this subgroup analyses the international audit standards and the developments in this field, with a view to their adoption at Community level.

2.9.3. EGAOB - Subgroup on Quality Assurance

The modernised eighth Directive allows to set up diverse public oversight systems. In view of an efficient and balanced co-operation between EU and third-country regulators, the subgroup drew up a proposal for a European recommendation laying down the specific qualitative aspects that Member States must meet with respect to public oversight of statutory auditors and audit firms auditing public interest entities.

This proposal provides that statutory auditors and audit firms auditing public interest entities that have not issued securities admitted to trading on a regulated market can be exempted. *A priori*, it will thus only apply to statutory auditors and audit firms auditing public interest entities issuing listed transferable securities. It also lays down certain requirements concerning the independence of the quality assurance system as such and that of inspectors working for the supervisory authority, as well as the scope of quality assurance assessments. Moreover, it defines the measures available to authorities to ensure transparency on the overall supervisory results.

The new European recommendation, which is expected to be published in the first quarter of 2008, will replace Commission Recommendation 2001/256/EC on minimum requirements with respect to quality assurance for the statutory audit in the European Union.

2.10. Banking Supervision Committee of the European Central Bank

The Banking Supervision Committee of the European Central Bank is a committee comprising high level representatives of the banking supervisory authorities and the central banks of Member States. The committee is chaired by Mr Praet, Executive Director of the National Bank of Belgium since June 2007. The missions concerning prudential supervision conferred by the Treaty and the statutes of the European Central Bank on the ESCB (European System of Central Banks) are carried out by the Banking Supervision Committee on behalf of the ESCB. The Committee is a forum for the exchange of opinions on the supervisory policies and practices in Member States and should be consulted on proposals for Directives and bills tabled by Member States on matters within its competence.

The Banking Supervision Committee was chiefly assisted in carrying out its mandate in 2007 by two working groups comprising members of the central banks and national supervisory authorities, i.e. the Working Group on Macro-Prudential Analysis (WGMA) and the Working Group on Developments in Banking (WGDB).

In order to systematise the analysis of macro-economic data with a view to identifying, as far as possible in time, the factors likely to weaken the financial institutions as a whole and thereby the financial system, the Working Group on Macro-Prudential Analysis monitors the macro-economic environment and reports to the Committee on trends and facts likely to be relevant to the prudential supervision of the financial sector.

The WGMA contributed to the financial sector stability reports in June 2007 and December 2007, as well as to the stability report on the European banking sector. These reports are discussed within the ECB's Executive board and published under the aegis of the Banking Supervision Committee.

The group's discussions mainly dealt with the impact of US subprimes on the stability of the European financial sector. In co-operation with the International Monetary Fund, the WGMA organised the Workshop on Credit Growth in Central and Eastern European Countries which was held from 29 to 30 January 2008 in Vienna. It also finalised the list of projects to be dealt with in 2008.

As in the previous years, the Working Group on Developments in Banking focused on drawing up its structural report during the first half of 2007. This annual report aims at identifying and monitoring the structural trends marking the European banking sector as a whole. The 2007 report dealt more specifically with the liquidity management of European banks operating cross-border, as well as with the distribution channels of retail banks. In the second half of the year, the group dealt with the diversification of income within European banking groups.

3. MULTILATERAL CO-OPERATION

3.1. Basel Committee on Banking Supervision

In 2007, the Basel Committee's activities mainly focused on the following areas:

- the follow-up on the implementation of the new capital adequacy regime. In this context, the Committee has published guidelines for computing the incremental default risk in the trading book, for consultative purposes. The Basel Committee has issued principles for home-host supervisory co-operation for the implementation of the advanced measurement approach for operational risk in a cross-border banking group. In addition, works started on a new definition of prudential own funds;
- the need, following the recent subprime crisis, to develop adequate rules to address risks to which banks are exposed;
- the dialogue with countries that are not members of the Committee, as well as with the banking industry.

Moreover, the Basel Committee released the following working papers in 2007:

- the consultative paper "Principles for home-host supervisory co-operation and allocation mechanisms in the context of Advanced Measurement Approaches (AMA)" in February 2007;
- the consultative paper "Guidelines for Computing Capital for Incremental Default Risk in the Trading Book" in October 2007;
- the final paper "Principles for home-host supervisory co-operation and allocation mechanisms in the context of Advanced Measurement Approaches (AMA)" in November 2007.

The Basel Committee has organised its work under four main permanent subgroups, namely the Accord Implementation Group (AIG), the Policy Development Group (PDG), the Accounting Task Force (ATF) and the International Liaison Group (ILG).

3.1.1. Policy Development Group (PDG)

The Policy Development Group, which started working in February 2007, coordinates the Basel Committee's works on supervisory policies. It is the highest technical group under the Basel Committee. Besides its role as coordinator of the subgroups, the PDG is invited to start, on its own initiative, works on supervisory policies and to exchange information on developments in the financial markets and risk management. The developments in credit markets in 2007 in particular attracted the attention of the group which met four times during the year.

- ***Capital Monitoring Group (CMG)***

The mission of the Capital Monitoring Group consists in analysing the impact of the transition from Basel I to Basel II rules on regulatory capital, as well as on the capital requirements for credit institutions. In 2007, the CMG continued its work by developing templates synthesising the information necessary to perform its mission. These templates are based on the information reported by credit institutions to the supervisory authorities. The CMG uses this information to explain the development of certain key indicators it has developed. In 2007, the CMG also set up the necessary infrastructure for the first survey that is planned for the end of the first half of 2008.

- ***Definition of Capital Subgroup***

The initial task of this new subgroup was to take stock of the instruments eligible for inclusion in the regulatory own funds of credit institutions of the subgroup's 16 member jurisdictions. This analysis was based on a detailed survey among the supervisory authorities concerned. In addition, the group defined four work streams dedicated to the issue of Tier 1 hybrid instruments and to the experience of the different market participants with these instruments. The initial work phase should end at the beginning of 2008 with the preparation of an internal report intended to assist the Basel Committee in its decision regarding the extent of future works on the definition of own funds.

- ***Working Group on Liquidity (WGL)***

The working group's mandate is to take stock of liquidity supervision across member countries. This included an evaluation of the type of approaches and tools used by supervisors to evaluate liquidity risk and banks' management of liquidity risks arising from financial market developments.

Recent events related to subprimes highlight the links between funding and market liquidity risk, the interrelationship of funding liquidity risk and credit risk, and the fact that liquidity is a key determinant of the soundness of the banking sector.

Based on the group's works, the Basel Committee published the document "Liquidity Risk: Management and Supervisory Challenges" in February 2008. This document summarises the results of the stock-taking of national liquidity regimes and the observation of liquidity risk management practices during the subprime turmoil.

The working group is reviewing the 2000 publication "Sound Practices for Managing Liquidity Risk in Banking Organisations". While the guidance remains overall relevant, the working group identified areas that warrant updating and strengthening. The Basel Committee will publish a revised version of the 2000 guidance for consultation in summer 2008.

- ***Risk Management and Modelling Group (RMMG)***

The Risk Management and Modelling Group's mandate is to monitor the progress made in internal risk management within credit institutions. It informs the Basel Committee of these advances and, where applicable, submits proposals to maintain the consistency of prudential requirements and internal risk management practices. In 2007, the group studied the modelling techniques of economic capital used under Pillar 2 of the new capital adequacy rules.

3.1.2. Accord Implementation Group (AIG)

The Accord Implementation Group was created to promote a consistent implementation of the new capital adequacy rules at international level.

In its four 2007 meetings, the Accord Implementation Group closely monitored the transition to the new capital requirements (Pillar 1) for banking groups operating cross-border. Pillar 1 being implemented, the group's works are now focused on the supervision of capital adequacy as a whole (Pillar 2) and market transparency (Pillar 3). The group stays in touch with the professional associations and endeavours to foster consistency in the practical implementation of Basel II.

- ***AIG - Validation Subgroup (AIGV)***

In 2007, AIGV's works focused on certain specific topics whose implementation remains problematic for most of the banks using IRB approaches. In particular, the group studied the LGD estimation techniques used by banks, and notably economic downturn LGD.

The AIGV also served as a forum for exchanging members' information on the requests to use IRB approaches (number of requests granted and, where applicable, refused, conditions linked to partial use, etc.). The group also discussed the role of supervisory authorities after the adoption of the IRB approaches by the banks on 1 January 2008.

During the first half-year of 2008, the AIGV will give priority to supervisory approaches regarding securitisation and will endeavour to set up principles guiding the works of supervisory authorities in this field.

- ***AIG - Operational Risk Subgroup (AIGOR)***

AIGOR focuses on the challenges associated with the development, implementation and maintenance of the operational risk management framework meeting the requirements of Basel II, particularly as they relate to the advanced measurement approaches (AMA). Four meetings took place in 2007 gathering experts of Member States.

In November 2007, AIGOR published the document "Principles for home-host supervisory co-operation and allocation mechanisms in the context of Advanced Measurement Approaches (AMA)" the primary objectives of which are to (1) clarify the key elements of supervisory co-operation with respect to the implementation of AMA, (2) establish a framework of principles to facilitate information sharing in the assessment and approval of AMA methodologies and (3) establish a set of principles to promote the development and assessment of allocation mechanisms incorporated in a hybrid AMA.

3.1.3. Accounting Task Force (ATF)

As regards accounting standards, the Accounting Task Force drew up comment letters in response to the call for comments of the International Accounting Standards Board (IASB) on the discussion paper "Preliminary Views on Insurance Contracts" and on the "Statement of Financial Accounting Standard 157, Fair Value Measurements (SFAS 157)" of the US accounting standard setter, the Financial Accounting Standards Board (FASB). Moreover, the ATF closely monitors and contributes to the development of a new conceptual framework by the IASB and FASB.

As regards audit standards, the group issued comment letters on the exposure drafts of the International Auditing and Assurance Standards Board (IAASB) in the context notably of the consultation on ISA 540 "Auditing accounting estimates, including fair value accounting estimates, and related disclosures" and "Improving the Clarity of IAASB Standards". Given the objective of improving audit quality at international level, the group also issued comment letters on the exposure drafts of the International Ethics Standards Board for Accountants (IESBA), more particularly in the context of the consultation on section 290 of the Code of Ethics "independence - audit and review engagements" and section 291 of the Code of Ethics "independence - other assurance engagements". These comment letters are available on the Basel Committee's website (www.bis.org/bcbs/commentletters/commentletters.htm).

At the end of 2007 and the beginning of 2008, the ATF also researched on audit quality.

Moreover, the ATF and the Risk Management and Modelling Group are gaining a deeper understanding of banks' practices related to modelling fair values for complex and/or illiquid products.

The Committee will also provide resources to a working group to be created within the IAASB in order to improve guidance on auditing fair value estimates.

Lastly, the ATF carried out a survey among its members and members of the International Liaison Group (ILG) to summarise the implementation progress of the guidance "Compliance and the compliance function in banks" published by the Basel Committee in April 2005, as well as recent incidents and challenges the industry has to contend with as regards compliance. A summary version of this report will be published soon on the Basel Committee's website.

3.2. International Organisation of Securities Commissions (IOSCO)

3.2.1. XXXIInd Annual Conference of IOSCO

The securities and futures regulators as well as other members of the international financial community met in Mumbai, India, from 9 to 12 April 2007, on the occasion of the XXXIInd Annual Conference of IOSCO.

As regards IOSCO's strategy, the operational priorities have been confirmed. The objective is to maintain IOSCO's role as standard and international benchmark setter for securities regulation by improving enforcement-related cross-border co-operation and implementing IOSCO's objectives and principles. It was also decided to foster IOSCO's profile at international level and to enhance dialogue with the financial sector.

The implementation of the objectives and principles of securities regulation (IOSCO Principles) is an important priority for IOSCO. The objective of the principles is to encourage countries to improve the quality of their securities regulation. They represent the principal international benchmark on prudential supervision of securities markets. In 2005, IOSCO created the Principles Assessment and Implementation Program in order to help jurisdictions implement these principles. At present, the level of demand from members for assisted assessments as part of the Program far exceeds IOSCO's resources. In response, IOSCO is exploring different options to ensure that more technical assistance is available to work with the members. At the same time, IOSCO continues to explore opportunities for funding by a number of international institutions and regional development banks.

At the XXXIInd Annual IOSCO Conference, the CSSF was accepted, together with other IOSCO members, as signatory to the MMoU[3]. This memorandum of understanding is one of IOSCO's major contributions in the area of regulatory co-operation and effective cross-border enforcement. There are currently 41 members that have signed the MMoU. Fifteen other members have expressed their commitment to sign the MMoU in accordance with its Appendix B.

IOSCO continued its confidential dialogue with certain countries with which specific co-operation issues have been experienced. At the XXXIInd Annual Conference, substantial progress has been made with a number of regulators with which dialogue has been ongoing. Progress that has been made with the Financial Services Commission of the British Virgin Islands was such that it has been welcomed into IOSCO as new ordinary member.

As regards corporate governance, IOSCO published a report in 2007 entitled "Board Independence of Listed Companies".

In 2007, IOSCO also published a report on non-audit services.

IOSCO will continue its works on rating agencies with a view of publishing a report on the implementation of the IOSCO Credit Ratings Agency Code of Conduct and with a view of publishing a report on the role of credit rating agencies in relation to structured financial products.

[3] Multilateral Memorandum of Understanding (MMoU) concerning consultation and co-operation and the exchange of information.

Moreover, IOSCO has established a new task force in the field of private equity. The purpose of the task force is to explore the risks associated with private equity markets and to determine how supervisory authorities should deal with them.

IOSCO remains active in the area of the implementation of the International Financial Reporting Standards (IFRS), the international debt disclosure principles, the accounting and non-financial statements for special purpose entities, the regulation of secondary markets and bond markets, the compliance function at market intermediaries and conflicts in securities offerings.

Moreover, IOSCO continued its works as regards boiler rooms, hedge funds and governance for investment funds. As regards the latter, IOSCO published a report on the principles of governance for investment funds in 2007.

3.2.2. IOSCO groups

The CSSF is a member of two IOSCO groups, i.e. the Standing Committee no. 1, dealing, among others, with subjects concerning accounting, and the Standing Committee no. 5 concerning UCIs and collective management.

- ***Standing Committee no. 1 (SC1)***

As member of the permanent committee SC1, the CSSF attends the meetings of the subcommittees on disclosure, accounting, auditing, as well as the implementation of IAS/IFRS. The year 2007 was mainly marked by market turmoil due to the subprime crisis which led IOSCO to create a Task Force on the Subprime Crisis.

Disclosure Subcommittee

In 2007, the subcommittee continued its works on the periodic disclosure principles by issuers. In this context, the fears and tensions provoked by the subprime crisis led the subcommittee to add another heading to that project, namely the exposure of issuers to market risk associated with their derivative instruments activities.

Auditing

In the field of auditing, the Auditing subcommittee (AuSC) continued its review of the standard-setting activities of the International Auditing and Assurance Standards Board (IAASB) on auditing, including notably:

- the consultation of the International Ethics Standards Board of Accountants (IESBA) on its Strategy and Operational Plan 2008-2009, following its comments on the first and second set of proposed amendments;
- the IAASB consultation paper on its strategy for 2009-2011 following the completion of the Clarity project in 2008;
- any work relating to non-audit services, as the working group of Chairmen on non-audit services was dissolved by the Technical Committee.

Other subjects in close relation with auditing that SC1 works in are:

- the PIOB (Public Interest Oversight Body) and the Monitoring Group;
- the International Forum of Independent Audit Regulators (IFIAR).

Discussions on a possible recognition, even endorsement, of the International Standards on Auditing (ISA) by IOSCO continue in parallel. In this context, SC1 prepared a note on which IOSCO's statement of 9 November 2007 on International Auditing Standards was based.

Accounting

The Accounting subcommittee (ASC) continued to follow the works of the International Accounting Standards Board (IASB), the International Financial Reporting Interpretations Committee (IFRIC) and the Standard Advisory Committee (SAC) as regards accounting regulation and submitted its advice to SC1 on the discussion papers and projects.

The subcommittee notably dealt with the following IASB/IFRIC activities and projects:

- the review of the IASC Foundation's constitution;
- the discussion paper on insurance contracts;
- the project on joint arrangements;
- the proposed amendments to IAS 39;
- the project on proposed improvements of IFRS;
- IFRIC interpretations involving, among others, IAS 39, IAS 27, IAS 18 and IAS 19.

Moreover, ASC's members take part as observers in seven advisory/working groups of the IASB, namely the Standards Advisory Council, the Financial Instruments Working Group, the Insurance Working Group, the Joint International Group on Performance Reporting, the Extractive Activities, the Lease Accounting and the Employee Benefits.

Lastly, with ASC's help, the SC1 drew up a document on which IOSCO's public statement should be based on urging publicly traded companies to provide investors with clear and accurate information on the accounting standards used in the preparation of their accounts, even more so where those differ from IFRS as issued by the IASB.

IFRS Regulatory Interpretation and Enforcement

The subcommittee continued to explore the means to transfer decisions from CESR's database to IOSCO's.

- ***Standing Committee no. 5 (SC5)***

The CSSF is a member of the permanent committee SC5 Investment Management which dealt with the following topics in 2007: Principles for the Valuation of Hedge Fund Portfolios, Point of Sale Disclosure to Retail Investors, Funds of Hedge Funds, Exchange Traded Funds, Real Estate Funds, Soft Commissions and Identification of Strategic Priorities.

IOSCO published the following documents in 2007:

- the final report "Examination of Governance for Collective Investment Schemes Part II" in February 2007;
- the consultation report "An Overview of the Work of the IOSCO Technical Committee" in March 2007;
- the consultation report "Call for Views on Issues that could be addressed by IOSCO on Funds of Hedge Funds" in April 2007;
- the consultation report "An Experiment within the Technical Committee Standing Committee on Investment Management (SC5) to establish a Framework for Identifying Strategic Priorities" in April 2007;
- the final report "Principles for the Valuation of Hedge Fund Portfolios" in November 2007, which follows the consultation report on that subject released in March 2007;
- the final report "Soft Commissions Arrangements for Collective Investment Schemes" in November 2007.

The documents concerned are available on IOSCO's website (www.iosco.org).

In addition, the CSSF attended the following IOSCO public hearings: Hearing on Funds of Hedge Funds in Paris in October 2007, Hearing of Experts of the Asian Funds of Hedge Funds Industry in Hong Kong in November 2007.

3.3. Extended contact group "Undertakings for collective investment"

The CSSF attended the annual meeting of the extended contact group "Undertakings for collective investment" that was held from 3 to 5 October 2007 in Cape Town. The subjects discussed were the following: questions relating to prudential supervision, conflicts of interest/code of conduct, legal issues, financial issues, reporting and disclosure, management and administration of investment funds, UCITS and special investment funds.

3.4. AML/CFT Expert Group

The CSSF is represented within the AML/CFT Expert Group, a working group on anti-money laundering, created within the Bank for International Settlements (B.I.S.). The group is responsible for monitoring AML/CFT issues that have a bearing on banking supervision.

3.5. *Institut Francophone de la Régulation Financière* (IFREFI)

The *Institut Francophone de la Régulation Financière* (IFREFI, Francophone institute for financial regulation), gathering the financial markets regulatory authorities of 16 French-speaking countries (Algeria, Belgium, Bulgaria, Cameroon, France, Guinea, Luxembourg, Moldavia, Monaco, Morocco, Quebec, Rumania, Switzerland, Tunisia, the West African Monetary Union, the Economic and Monetary Community of Central Africa) was created in 2002 by a charter. IFREFI is a flexible structure of co-operation and dialogue and aims at furthering the exchange of knowledge and experience, drawing up studies and exchanging essential information relating to the financial markets between the Member States of the Institute. According to the charter, IFREFI also aims at promoting professional training by organising training seminars on specific topics.

The annual meeting of IFREFI chairmen, which took place in Tunis on 14 June 2007, concentrated on sharing the recent regulatory progress within each Member State and at international level (IOSCO works). It was also the occasion to summarise the current economic and financial international situation and to discuss corporate governance, thereby allowing to compare the relevant experience of regulators in the field of governance and internal control.

It should be noted that the Financial Supervisory Commission of Bulgaria was admitted as sixteenth IFREFI member.

A training seminar followed the annual meeting addressing international accounting standards, international auditing standards and corporate governance.

CHAPTER XII

BANKING AND FINANCIAL LEGISLATION AND REGULATIONS

1. Major events in 2007
2. Directives adopted by the Council and the European Parliament but not yet implemented under national law
3. Laws passed in 2007

1. MAJOR EVENTS IN 2007

The year 2007 was characterised by the implementation of three main sets of rules, namely:

- the rules related to Basel II;
- the new prudential reporting regarding capital adequacy and the new prudential financial reporting;
- the provisions of the MiFID Directive.

These sets of rules entered into force on 1 January 2008, except for the MiFID, which entered into force on 1 November 2007.

Whereas the implementation milestones of the provisions of Directives 2006/48/EC and 2006/49/EC (Basel II) were set for credit institutions in 2006 through circular CSSF 06/273, an equivalent circular for investment firms and management companies within the meaning of Chapter 13 of the law of 20 December 2002, as amended, was published in 2007. Circular CSSF 06/273 intended for credit institutions has been amended by circular CSSF 07/317, which added an amendment to the first circular following the transposition of Directive 2007/14/EC as well as numerical examples for the capital adequacy ratio calculation. The CSSF carried out inspections in the context of advanced measurement approach requests for the calculation of capital requirements for credit and operational risks concerning credit institutions established in Luxembourg.

Moreover, the CSSF specified in circular CSSF 07/301 its expectations in relation to the Internal Capital Adequacy Assessment Process (ICAAP).

In this same field, it is worth mentioning the adoption of the law of 7 November 2007 (transposition of the rules on consolidated supervision and on the competences of supervisory authorities).

Finally, in the context of Directives 2006/48/EC and 2006/49/EC, the CSSF introduced by way of circular CSSF 08/338 a new half-yearly reporting in order to receive the results of the stress test aiming at assessing the interest rate risk arising from non-trading book activities.

The second set of provisions published in 2007 by the CSSF includes six circulars related to the prudential reporting regarding capital adequacy and the prudential financial reporting. These circulars follow the adoption of Basel II at European level and the introduction of European regulation in relation to IAS/IFRS. In this context, it should be noted that the new prudential reporting tables on capital adequacy are based on the European COREP scheme (COmmon REPorting) as defined by CEBS whereas the new financial reporting tables are based on the common European FINREP scheme (FINancial REPorting).

Moreover, at the beginning of 2008, the CSSF published circular CSSF 08/340 which clarifies certain issues related to the legal publication of accounts. It is hence important to distinguish the legal publication of accounts, which is the main subject of that circular (and of Chapter III of circular CSSF 05/227), from the prudential financial reporting to be submitted to the CSSF, which is the subject of circulars CSSF 05/227 (Chapters I and II), 07/279, 07/316, 07/319, 07/324 and 07/331. As from January 2008, the prudential financial reporting shall be established according to IAS/IFRS whereas, in relation to the legal publication of accounts, credit institutions may choose to publish their accounts according to LUX GAAP, LUX GAAP combined with one or more IAS/IFRS provisions (LUXGAAP with IAS options), or IAS/IFRS.

The last main set of new provisions credit institutions and investment firms have to comply with relates to MiFID. The law of 13 July 2007 on markets in financial instruments transposing Directive 2004/39/EC of 21 April 2004 and the Grand-ducal regulation of 13 July 2007 on the organisational requirements and rules of conduct in the financial sector transposing Directive 2006/73/EC of 10 May 2006 entered into force on 1 November 2007. These measures constitute, together with Regulation (EC) No 1287/2006 of 10 August 2006 implementing Directive 2004/39/EC, the new MiFID legislation that credit institutions and investment firms of the financial centre have to comply with whenever they provide investment services or perform investment activities.

The MiFID sets down a more complete regulatory framework, imposes higher standards as compared to the previous Directive 93/22/EC on investment services and expands the list of financial instruments submitted to its regulation. Its purpose is to strengthen the harmonisation of European regulation and to foster fair, transparent, efficient and integrated capital markets within the European Union. The MiFID also aims at protecting investors and upholding market integrity, by setting harmonised requirements for the activity of authorised intermediaries. It establishes the obligation to report transactions and maintain records.

It puts in place a "unique passport" system allowing investment firms to offer their services throughout the European territory. It sets minimum standards as regards the mandate of national supervisory authorities and establishes procedures for the co-operation between authorities in the context of investigations on breaches of the Directive.

In 2007, the CSSF published five circulars which provide details on certain subjects included in the MiFID:

- **Circular CSSF 07/302** provides further clarifications on the obligation to report transactions on financial instruments. The new reporting regime's main difference compared to the former regime is that only transactions where the credit institutions and investment firms concerned are market facing and/or execute transactions on their own account must be reported. The credit institutions and investment firms concerned shall have in place an adequate system for reporting transactions and adhere to the new version of the *Recueil d'instructions TAF* (Transaction in Financial Instruments Reporting (TAF) – Electronic Reporting instructions) published on the CSSF website. The *Recueil* specifies the details of the communication system implemented between the reporting firms and the CSSF and sets out the information to report to the CSSF and the technical arrangements to report transactions. Article 28 of the law of 13 July 2007 also determines the rules regarding the exchange of information between the relevant competent authorities so as to enable these authorities to perform their supervisory tasks. The CSSF made the necessary internal arrangements in order to ensure that the information received is made available to the competent authority of the most relevant market in terms of liquidity for the financial instrument concerned. In addition, the CSSF transmits the information received from the Luxembourg branches of credit institutions and investment firms authorised in another Member State to the competent authority of their home Member State, unless the relevant competent authority decides that it does not want to receive this information.

- **Circular CSSF 07/305** draws the attention of the interested parties to the publication of the law of 13 July 2007 on markets in financial instruments, whose first objective is to define a set of rules aiming at strengthening investor protection and thus enhancing investor confidence in financial markets. Among those rules are the more detailed and extensive conduct of business rules, the strengthened rules on best execution of client orders, the management of conflicts of interest. The second objective of the MiFID law is to promote investors' interests, market efficiency and competition between the different order execution regimes by creating a level playing field. The law establishes an overall regulatory framework for order execution whose purpose is to promote competition at EU and domestic level between regulated markets, multilateral trading facilities and internal trading systems set up by credit institutions and investment firms. Moreover, the MiFID law introduces a certain number of amendments to the law of 5 April 1993 on the financial sector, as amended. These amendments mainly relate to the introduction of new PFS categories, changes to certain PFS categories, the reduction of the initial capital requirement for PFS, the extension of the list of financial instruments and the change to the organisational and conduct of business rules.

- **Circular CSSF 07/307** explains and specifies the conduct of business rules in the financial sector. The new article 37-3(1) of the law of 5 April 1993 on the financial sector, as amended, requires credit institutions and investment firms, when providing investment services to clients and, where applicable, ancillary services, to act honestly, fairly and professionally in the best interest of clients. This general principle was already the key principle of the professional requirements introduced in 1998 and specified in circular CSSF 2000/15 on the rules of conduct in the financial sector, repealed as of 1 November 2007 and replaced by circular CSSF 07/307 which entered into force at the same date. These explanations concern, *inter alia*, the responsibility of the board of directors and the authorised management, the audit by the external auditor, the classification of clients, the assessment whether the service provided suits the client or is appropriate, conflicts of interest, inducements, the best execution requirement, client order execution rules, informing of existing and potential clients, the need for a written agreement on rights and obligations of the parties, the reports to provide to clients, record-keeping and rules to observe in specific competitive situations. The recommendations published by the Committee of European Securities Regulators (CESR) as regards inducements, best execution and specific records are appended to the circular and are an integral part of circular CSSF 07/307.

- **Circular CSSF 07/325** describes the provisions relating to credit institutions and investment firms of EU origin, established in Luxembourg by way of branches or exercising their activities by way of free provision of services and replaces and repeals circulars IML 93/100 and IML 98/147. Credit institutions and investment firms that benefit from the European passport can provide their banking and investment services/activities in any Member State based on the principle of supervision by the home supervisory authority. In this context, the circular details, for the attention of the branches of credit institutions and investment firms whose head office is in another Member State, the provisions that their Luxembourg branches must comply with under the new framework of the law of 13 July 2007. Indeed, certain areas of supervision fall within the remit of the CSSF, considered as the authority that is the closest to the branch and better placed to detect issues and intervene in order to ensure compliance with the rules imposed on branches.

- **Circular CSSF 07/326** specifies the provisions relating to Luxembourg incorporated credit institutions and investment firms established in another Member State by way of branches or exercising their activities in another Member State by way of free provision of services and replaces and repeals circulars IML 93/99 and IML 98/148. It informs on the role of the CSSF as competent authority of the home Member State and draws the attention of Luxembourg credit institutions and investment firms to the provisions to be complied with under the new framework set up by the law of 13 July 2007 when establishing a branch or providing services in another Member State of the European Union. The forms to be used by Luxembourg institutions to notify the establishment of a branch or the free provision of services are appended to the circular. It should be noted that those forms have been drawn up by CESR in order to harmonise the content of the information to be sent by the competent home authority to the competent host authority within the scope of the notification procedure.

2. DIRECTIVES ADOPTED BY THE COUNCIL AND THE EUROPEAN PARLIAMENT BUT NOT YET IMPLEMENTED UNDER NATIONAL LAW

This section includes the directives adopted by the Council and the European Parliament but not yet implemented under national law and of particular relevance in the context of the supervisory mission of the CSSF.

2.1. Directive 2005/60/EC of 26 October 2005 on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing

The third Directive on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing aims to incorporate the June 2003 revision of the Forty Recommendations of the Financial Actions Task Force (FATF) into EU legislation. More detailed information on the Directive has been provided in the CSSF Annual Report 2005.

A draft law aiming to transpose the Directive into Luxembourg law has been submitted to the *Chambre des Députés*.

2.2. Directive 2006/43/EC of 17 May 2006 on statutory audit of annual accounts and consolidated accounts, amending Council Directives 78/660/EEC and 83/349/EEC (modernised eighth Directive)

The new eighth Company Law Directive on the statutory audit aims at enhancing and harmonising the statutory audit function throughout the European Union. It sets out principles for public supervision in all Member States, introduces a requirement for external quality assurance and clarifies the duties of statutory auditors. More detailed information has been provided in the CSSF Annual Report 2006.

2.3. Directive 2006/46/EC of 14 June 2006 amending Directives 78/660/EEC on the annual accounts of certain types of companies, 83/349/EEC on consolidated accounts, 86/635/EEC on the annual accounts and consolidated accounts of banks and other financial institutions and 91/674/EEC on the annual accounts and consolidated accounts of insurance undertakings

This Directive has been discussed in detail in the CSSF Annual Report 2006.

2.4. Directive 2006/70/EC of 1 August 2006 laying down implementing measures for Directive 2005/60/EC as regards the definition of "politically exposed persons" and the technical criteria for simplified customer due diligence procedures and for exemption on grounds of a financial activity conducted on an occasional or very limited basis

The purpose of this Directive is to implement Directive 2005/60/EC of 26 October 2005 on the fight against money laundering and terrorist financing which provides for this possibility in order to ensure a consistent implementation and to take into account the technical development in the field of combating money laundering and terrorist financing. Directive 2006/70/EC thus specifies the notion of "politically exposed persons" (already defined in Directive 2005/60/EC) by introducing a list of prominent political functions and by specifying the concept of family and close associates of politically exposed persons. The other provisions of the Directive set out information on customers presenting a low risk of money laundering and terrorist financing and on the persons carrying out a financial activity, but who, based on specific criteria, do not fall within the scope of Directive 2005/60/EC.

A draft law aiming to transpose the Directive into Luxembourg law has been submitted to the *Chambre des Députés*.

2.5. Directive 2007/44/EC of 5 September 2007 amending Directive 92/49/EEC and Directives 2002/83/EC, 2004/39/EC, 2005/68/EC and 2006/48/EC as regards procedural rules and evaluation criteria for the prudential assessment of acquisitions and increase of holdings in the financial sector

The purpose of this Directive is to facilitate cross-border consolidations in the financial sector. To this end, the Directive clarifies the prudential authorisation process of acquisitions and increase of qualifying holdings in the financial sector and enhances transparency in order to strengthen the legal certainty for the parties concerned. The directive sets out in detail the procedure to be applied by the competent authorities for the prudential assessment of acquisitions. It puts in place a limited set of assessment criteria allowing to harmonise the handling of merger and acquisition requests in the Member States.

2.6. Directive 2007/64/EC of 13 November 2007 on payment services in the internal market

The Payment Services Directive (PSD) provides the legal framework necessary to the implementation of a single European payment services market. It aims to establish a complete and detailed set of rules applicable to all payment services throughout the European Union. Its aim is to make cross-border payments as easy, efficient and safe as the payments executed within a Member State. The directive also aims at stimulating competition by opening the payments markets to new payment services providers.

3. LAWS PASSED IN 2007

3.1. Law of 13 February 2007 on specialised investment funds

The law of 13 February 2007 on specialised investment funds replaces the law of 19 July 1991 relating to undertakings for collective investment the securities of which are not intended to be placed with the public. While the law of 19 July 1991 mainly refers to the provisions of the law of 30 March 1988 relating to undertakings for collective investment with respect to the rules applicable to UCIs created under its regime, its replacement became necessary following the abrogation of the 1988 law as from 13 February 2007, owing to the transitional provisions set down in the law of 20 December 2002 relating to undertakings for collective investment, which transposed the amended Directive 85/611/EC concerning UCITS into Luxembourg law.

The law on specialised investment funds establishes a legal framework to promote the development in Luxembourg of investment products reserved to "well-informed investors".

In order to allow UCIs subject to the law of 19 July 1991 to continue to perform their activities, the law of 13 February 2007 provides that these UCIs fall *ipso jure* under the new regime relating to specialised investment funds.

3.2. Law of 13 July 2007 on markets in financial instruments

The law of 13 July 2007 on markets in financial instruments (MiFID Law) implementing Directive 2004/39/EC of 21 April 2004 is explained in detail under point 1. above and under Chapter VII "Supervision of securities markets", as well as in circular CSSF 07/305 of 27 July 2007 on the coming into force of the law of 13 July 2007.

3.3. Law of 7 November 2007 transposing into the law of 5 April 1993 on the financial sector, as amended, Directive 2006/48/EC of 14 June 2006 relating to the taking up and pursuit of the business of credit institutions, and Directive 2006/49/EC of 14 June 2006 on the capital adequacy of investment firms and credit institutions

The law transposes into Luxembourg law the provisions on internal governance (article 22 of Directive 2006/48/EC), on the powers of the CSSF (article 136 of Directive 2006/48/EC) and the different provisions relating to consolidated supervision, including notably article 129 of Directive 2006/48/EC.

However, two major changes to the current situation should be pointed out. Firstly, the law strengthens the co-operation between competent authorities involved in the supervision of European banking groups. Secondly, article 15 of the law provides, in accordance with article 129 of Directive 2006/48/EC it transposes, that the Luxembourg supervisory authority must implement the decisions taken by a EU supervisory authority competent for the prudential supervision of the parent undertaking of a credit institution or investment firm authorised in Luxembourg, in the event of disagreement on the validation of a model used by a bank or an investment firm for the purpose of calculating capital requirements.

3.4. Law of 11 January 2008 on transparency requirements for issuers of securities

Grand-ducal regulation of 11 January 2008 on transparency requirements for issuers of securities, transposing Directive 2007/14/EC laying down detailed rules for the implementation of certain provisions of Directive 2004/109/EC on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market

The law and the Grand-ducal regulation which completes it by laying down certain rules for the execution of the provisions are explained in detail in Chapter VII "Supervision of securities markets" and in circular CSSF 08/337 of 6 February 2008 on the entry into force of the law of 11 January 2008 and of the Grand-ducal regulation of 11 January 2008 on transparency requirements for issuers of securities.

AGENTS HIRED IN 2007 AND 2008

IT coordination, Executive secretariat, Departments "Supervision of banks", "Supervision of UCIs", "Supervision of securities markets", "Supervision of pension funds, SICARs and securitisation vehicles", "Administration and finance", "Information Technology"

First row, left to right:	Nadja TRAUSCH, Sandra PREIS, Yves BARTRINGER, Ricardo OLIVEIRA, Christelle HUTMACHER, Mendaly RIES
Second row, left to right:	Patrick KLEIN, Nicole THINNES, Emile BARTOLE, Françoise JAMINET, Cédric BRANDENBOURGER, Laurent MAYER, Tom BECKER, Jim NEVEN
Absent:	Sergio DE ALMEIDA, Francis FRIDRICI

CHAPTER XIII

INTERNAL ORGANISATION OF THE CSSF

1. Functioning of the CSSF
2. Human resources
3. IT systems
4. Staff members
5. Internal committees

1. FUNCTIONING OF THE CSSF

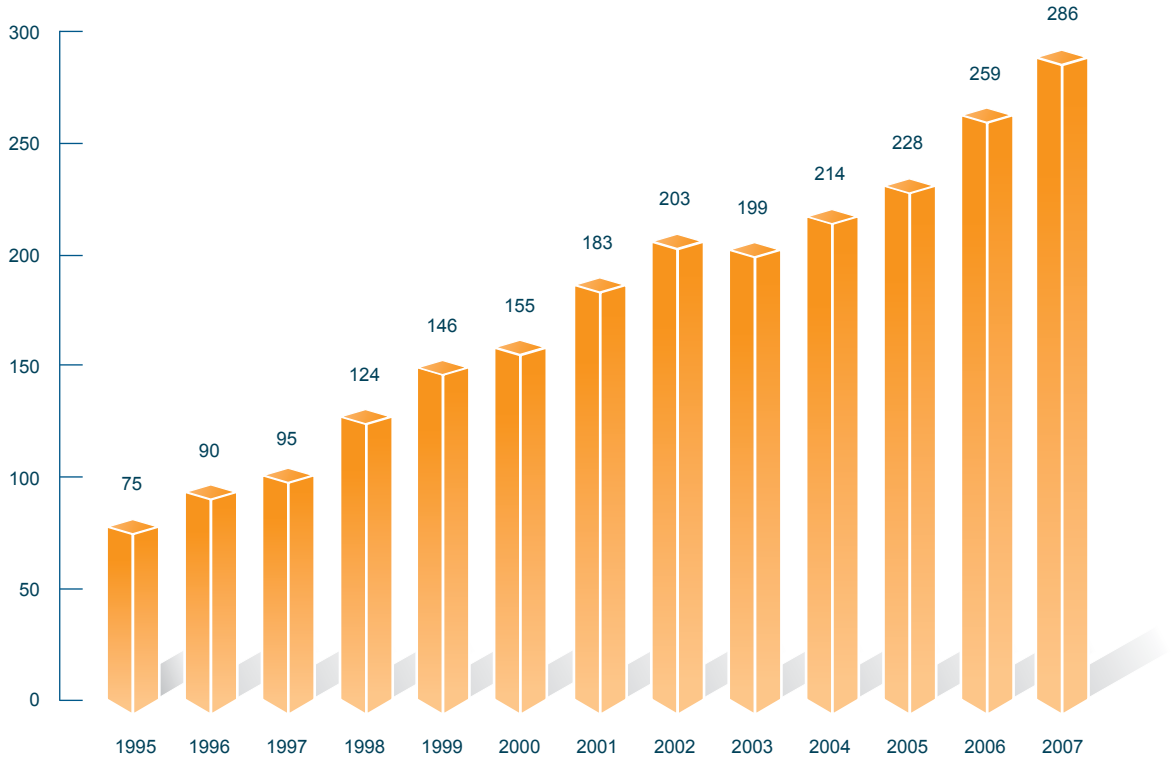
The CSSF's administrative and management organisation is described in detail in the sub-section "Corporate governance and functioning" of the CSSF website (www.cssf.lu, section "About the CSSF").

2. HUMAN RESOURCES

The CSSF's staff rose again sharply in 2007. Indeed, following the competitive examinations held in autumn 2006, 19 agents were hired at the beginning of 2007. Another competitive examination held on 28 April 2007 for the *carrière supérieure* allowed to hire six additional agents, namely three economists, two legal experts and an IT specialist. In addition, two agents were transferred to the CSSF under a *changement d'administration* (change of administration) and one agent was hired as *employé de l'Etat*. The CSSF deplored the death of an agent in 2007.

The CSSF thus had a staff of 286 as at 31 December 2007, representing 253.3 full-time positions.

Movements in staff numbers (at the end of the year)



In addition to the training programme offered to the new trainee agents, the CSSF organised 129 seminars for continuous training. 63% of these training sessions focused on economic and finance matters, 13% on IT, 7% on management and 6% on languages; 11% concerned other areas.

1,098 participations in training sessions were recorded in 2007, representing an average of three days of training per agent, and a total of 865 training days.

3. IT SYSTEMS

The CSSF's IT department is in charge of installing, maintaining and developing the CSSF's internal IT infrastructure.

The new European Directives, i.e. the Capital Requirements Directive (CRD) and the Directive on markets in financial instruments (MiFID), did not pass unnoticed in the CSSF's IT department. Thus, the new COREP and FINREP reporting that banks must submit as from 1 January 2008 was defined in close co-operation with the department "General Supervision". The XBRL taxonomies describing the data to be transmitted to the CSSF have been published on the CSSF's website in September 2007. These taxonomies are based on an EU development to harmonise reporting in the different EU Member States. The XBRL format stood out because of its flexibility to adapt the common proposal to the different national needs. In parallel, the CSSF adapted its internal system in order to receive, control and inject XBRL data into its own system. This system, which was set up on 1 January 2007 on basis of the existing reporting framework, is designed to receive the new data without too many changes to be made.

The major challenge of the year 2007 was without a doubt the new reporting of financial information under the MiFID Directive which had to be finalised by 1 November 2007, date of the entry into force of the Directive at EU level. This reporting, replacing the existing TAF reporting, adds a European dimension in that the transactions on instruments admitted to trading in another Member State are forwarded by the authority of the country in which the transaction took place. A whole security infrastructure had to be set up for this exchange. Following the deployment of substantial means, the system was finalised by the IT department in less than ten months. Further projects are planned for 2008.

The IT department also worked on the reporting systems for PFS and SICARs, in order to allow the automatic processing of incoming files and their monitoring by the data flow managers. In addition, preparations have been made to allow the protection of files by Luxtrust certificates and their collection through the transmission channels.

In the field of document processing, the automated publication of prospectuses for securities approved by the CSSF on the systems of the Luxembourg Stock Exchange via the "e-file" platform should also be noted.

In addition to setting up new applications, it became necessary to update the technical infrastructure, notably through the acquisition of new servers and their back-up. The CSSF team mastered the increasing complexity of the infrastructure without major incidents. As certain IT systems are reaching their limit however, considering notably the substantial growth in the volume of data to be stored and saved, studies to enlarge and renew certain systems have been launched.

Lastly, the fitting out of an additional floor of the CSSF's building for 57 agents and the subsequent move of other users on other floors represented an exceptional work load for the IT department, as regards the coordination, as well as the setting up and extension of the IT networks and infrastructures.

4. STAFF MEMBERS (AS AT 1 MARCH 2008)

MANAGEMENT

Director General	Jean-Nicolas Schaus
Directors	Arthur Philippe, Simone Delcourt
Executive secretaries	Joëlle Deloos, Karin Frantz, Marcelle Michels, Monique Reisdorffer
Employee	Francis Fridrici
Internal audit	Marie-Anne Voltaire
Director General's advisors	Jean-Marc Goy, Geneviève Pescatore, Marc Weitzel
IT coordination	Emile Bartolé
Systems security	Constant Backes, Marco Valente

GENERAL SUPERVISION

Head of function	Claude Simon
Deputy head	Romain Strock

Division 1 - International and policy department

Head of division	Romain Strock
	Ngoc Dinh Luu, Nadia Manzari, Judith Meyers, Vincent Thurmes, Pierre van de Berg, Karin Weirich

Division 2 - Accounting, reporting and audit

Head of division	Danièle Goedert
	Ana Bela Ferreira, Marguy Mehling, Christina Pinto, Diane Seil, Martine Wagner, Stéphanie Weber

Division 3 - Special functions

Didier Bergamo, Alain Hoscheid, Gilles Jank, Ronald Kirsch, Nicole Lahire, Marco Lichtfous, Joëlle Martiny, Pierrot Rasqué, Edouard Reimen, Davy Reinard, Joé Schumacher, Claude Wampach

Secretary Micheline de Oliveira

DEPARTMENT SUPERVISION OF BANKS

Head of department	Frank Bisdorff
Deputy head of department	Ed. Englaro

Division 1 - Supervision of credit institutions 1

Head of division	Ed. Englaro
	Anouk Dondelinger, Françoise Jaminet, Isabelle Lahr, Jean Ley, Jacques Streweler

Division 2 - Supervision of credit institutions 2

Head of division	Jean-Paul Steffen
	Joan De Ron, Jean-Louis Duarte, Jean Mersch, Michèle Trierweiler, Alain Weis

Division 3 - Supervision of credit institutions 3

Head of division	Nico Gaspard
	Marco Bausch, Jean-Louis Beckers, Françoise Daleiden, Claude Moes, Stéphanie Nothum

Division 4 - Supervision of credit institutions 4

Head of division Patrick Wagner
Carlos Azevedo Pereira, Monica Ceccarelli, Steve Polfer, Marina Sarmento, Yves Simon, Claudine Tock

General studies and issues Marc Wilhelmus

Statistics and IT issues Claude Reiser

Secretaries Michèle Delagardelle, Steve Humbert, Claudine Wanderscheid

DEPARTMENT SUPERVISION OF UNDERTAKINGS FOR COLLECTIVE INVESTMENT

Head of department Irmine Greischer
Deputy heads of department Claude Steinbach, André Schroeder, Jean-Paul Heger

Practical studies and specific aspects
Alain Bressaglia

IT systems Nico Barthels, Danièle Christophory

General organisation – Management and operation of databases
Claude Steinbach
Head of division Jolanda Bos
Adrienne André-Zimmer, Marie-Louise Baritussio, Patrick Bariviera, Christiane Cazzaro, Nicole Grosbusch, Claude Krier, Danielle Neumann, Géraldine Olivera, Sabine Schiavo, Marc Schwalen, Claudine Thielen, Nadja Trausch, Suzanne Wagner

Instruction and supervision of UCIs and management companies
Coordination of Divisions 1 to 6 Jean-Paul Heger

Division 1 - UCIs

Head of division Anica Giel-Markovinovic
Paul Hansen, Patricia Jost, Nathalie Reisdorff, Alain Strock, Daniel Wadlé, Claude Wagner, Nathalie Wald, Alex Weber

Division 2 - UCIs

Head of division Charles Thilges
Yolanda Alonso, Nathalie de Brabandere, Claude Detampel, Joël Goffinet, Dominique Herr, Sophie Leboulanger, Francis Lippert, Diane Reuter, Marc Siebenaler, Christel Tana

Division 3 - UCIs

Head of division Ralph Gillen
Isabelle Dosbourg, Michel Friob, Martin Mannes, Carine Peller, David Phillips, Laurent Reuter, Daniel Schmitz, Roberta Tumiotto, Michèle Wilhelm, Florence Winandy

Division 4 - UCIs

Head of division Francis Gasché
Robert Brachtenbach, Marie-Rose Colombo, Serge Eicher, Nicole Gengler, Martine Kerger, Robert Köller, Thierry Quaring, Marc Racké, Pascale Schmit

Division 5 - UCIs

Head of division	Guy Morlak
	Géraldine Appenzeller, Nathalie Cubric, Marc Decker, Jean-Claude Fraiture, Damien Houel, Jean-Marc Lehnert, Gilles Oth, Pierre Reding, Thierry Stoffel

Division 6 - Authorisation and supervision of management companies

Head of division	Pascal Berchem
	Anne Conrath, Pascale Felten-Enders, Anne-Marie Hoffeld, Roberto Montebrusco, Eric Tanson

Legal and economic aspects	André Schroeder
	Jacqueline Arend, Stéphanie Bonifas, Angela De Cillia, François Hentgen, Joëlle Hertges, Laurent Mayer, Fabio Ontano, Christian Schaack, Christiane Streef
Secretaries	Sandy Bettinelli, Carole Eicher, Sandra Ghirelli, Simone Kuehler, Sandra Preis

DEPARTMENT SUPERVISION OF THE OTHER PROFESSIONALS OF THE FINANCIAL SECTOR

Head of department	Sonny Bisdorff-Letsch
Deputy head of department	Denise Losch
	Gérard Brimeyer, Carlo Felicetti, Simone Gloesener, Sylvie Mamer, Anne Marson, Claudia Miotto, Carole Ney, Luc Pletschette, Mariette Thilges
Secretary	Emilie Lauterbour

GENERAL SECRETARIAT

Head of department	Danièle Berna-Ost
Deputy head of department	Danielle Mander
	Carmela Anobile, Carine Conté, Natasha Deloge, Jean-François Hein, Nadine Holtzmer, Patrick Hommel, Benoît Juncker, Iwona Mastalska, Christiane Trausch, Anne Wagener
Secretary	Steve Humbert

DEPARTMENT SUPERVISION OF SECURITIES MARKETS

Head of department	Françoise Kauthen
Deputy head of department	Annick Zimmer

Legal issues and takeover bids	Marc Limpach

Division 1 - Approval of prospectuses

Head of division	Jean-Christian Meyer
Group 1	Fanny Breuskin, Frédéric Dehalu, Patrick Fricke, Yves Hansen, Jim Neven, Jerry Oswald, Manuel Roda
Group 2	Claude Fridrici, Joëlle Paulus, David Schmitz

Division 2 - Approval of prospectuses

Head of division Gilles Hauben

Group 1 Olivier Ferry, Stéphanie Jamotte, Daniel Jeitz, Julien May, Marc Reuter, Cyrille Uwukuli, Olivier Weins

Group 2 Michèle Debouché, Estelle Gütlein-Bottemer

Supervision of listed companies David Deltgen, Maureen Wiwinius

Inquiries and other functions of supervision of securities transactions

Laurent Charnaut, Giang Dang, Eric Fritz, Andrea Haris, Sylvie Nicolay-Hoffmann, Mendaly Ries, Maggy Wampach

Supervision of persons performing stock exchange activities

Mylène Hengen

Secretaries Christine Jung, Marie-Josée Pulcini

DEPARTMENT SUPERVISION OF PENSION FUNDS, SICARS AND SECURITISATION UNDERTAKINGS

Head of department Christiane Campill

Deputy head of department Marc Pauly

Authorisation and supervision of pension funds and securitisation undertakings

Son Backes, Tom Becker, Cliff Buchholtz, Marc Pauly, Natalia Radichevskaia, Isabelle Maryline Schmit

Authorisation and supervision of SICARs

Daniel Ciccarelli, Josiane Laux, Carole Lis, René Schott, Martine Weber

Secretary Carla Dos Santos

DEPARTMENT SUPERVISION OF IT AND SUPPORT PFS

Head of department David Hagen

Deputy head of department Claude Bernard

Division 1

Head of division Claude Bernard

Paul Angel, Marc Bordet

Division 2

Head of division Pascal Ducarn

Martine Simon

Administration and secretariat Elisabeth Demuth

DEPARTMENT ADMINISTRATION AND FINANCE

Head of department Edmond Jungers

Deputy head of department Georges Bechtold

Division 1 - Human resources and day-to-day management

Head of division Georges Bechtold

Paul Clement, Sergio De Almeida, Raul Domingues, Alain Kirsch, Patrick Klein, Vic Marbach, Ricardo Oliveira

Division 2 - Financial management

Head of division	Jean-Paul Weber
	Tom Ewen, Carlo Pletschette
Secretary	Milena Calzettoni
Switchboard	Yves Bartringer, Nicole Thinnes

DEPARTMENT INFORMATION TECHNOLOGY

Head of department	Jean-Luc Franck
Deputy head of department	Sandra Wagner

Division 1 - Analysis and development

Head of division	Marc Kohl
	Cédric Brandenbourger, Romain De Bortoli, Luc Prommenschenkel, Guy Wagener

Division 2 - Management of databases

Sandra Wagner

Division 3 - Operating systems

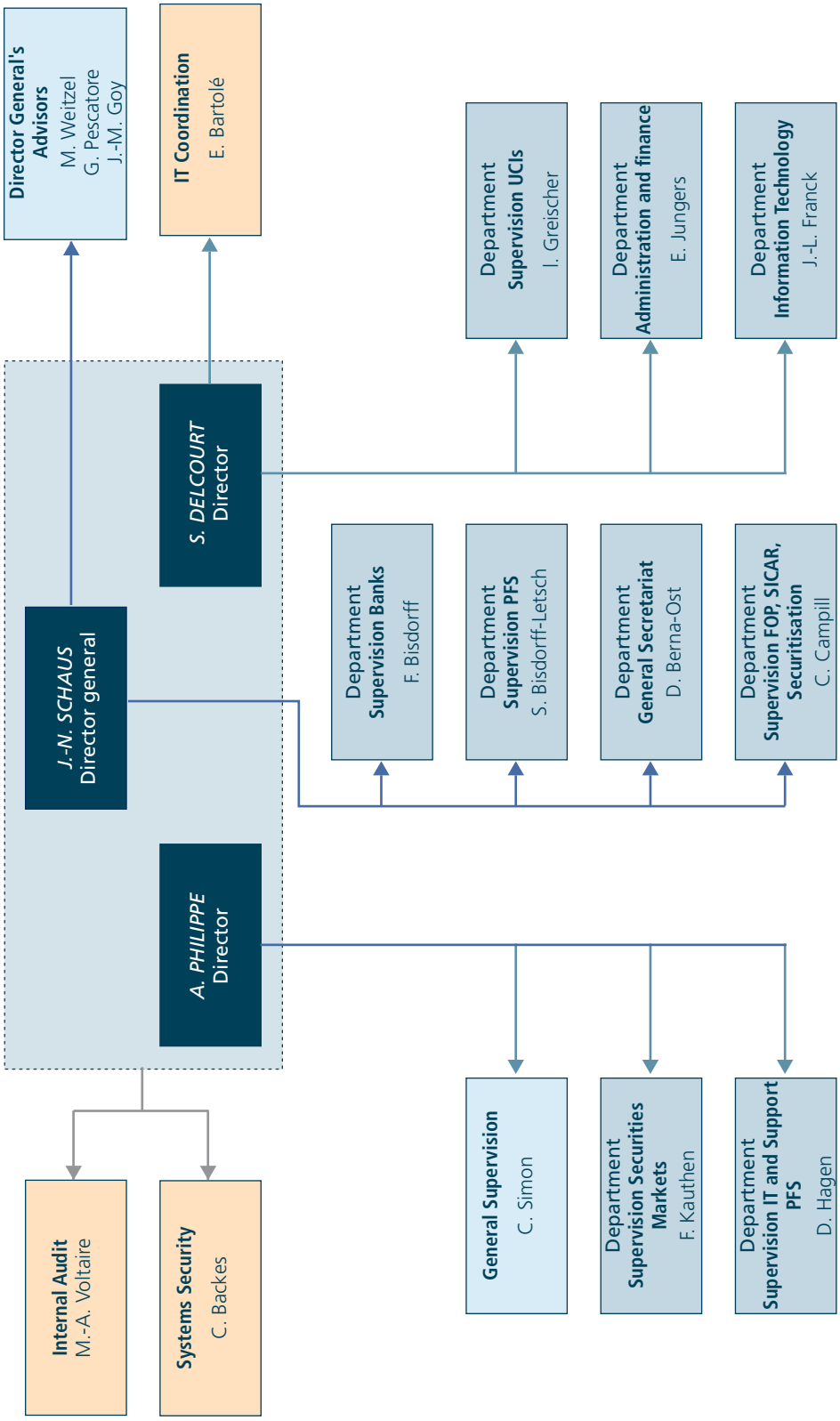
Head of division	Guy Frantzen
	Frank Brickler, Jean-François Burnotte, Jean-Jacques Duhr, Nadine Eschette, Steve Kettmann, Edouard Lauer

Division 4 - Dataflow management

Head of division	Joao Pedro Almeida
	Christelle Hutmacher, Karin Proth, Carine Schiltz
Secretary	Christelle Hutmacher

FINANCIAL CONTROLLER KPMG

ORGANISATION CHART



5. INTERNAL COMMITTEES

Consultative committee for prudential regulation

Chairman	Jean-Nicolas SCHAUS
Members	Alain FEIS, Rafik FISCHER, Jean GUILL, Michel MAQUIL, Jean MEYER, Arthur PHILIPPE, Jean-Jacques ROMMES, Camille THOMMES
Secretary	Danielle MANDER

Consultative committee Anti-Money Laundering

Chairman	Jean-Nicolas SCHAUS
Members	Claude BIRNBAUM, Pia HAAS, Charles HAMER, Roger HARTMANN, Jean-François HEIN, Jean-Luc KAMPHAUS, Pierre KRIER, Jean-Marie LEGENDRE, François PAULY, Marc PECQUET, Arthur PHILIPPE, Jean-Jacques ROMMES, Thomas SEALE, Claude SIMON, Romain STROCK, Lucien THIEL, Marc WEITZEL, André WILWERT
Secretary	Geneviève PESCATORE

Committee Other Professionals of the Financial Sector

Chairman	Jean-Nicolas SCHAUS
Members	Pierre-Yves AUGSBURGER, Sonny BISDORFF-LETSCH, Freddy BRAUSCH, Jean BRUCHER, Henri DE CROUY-CHANEL, Alain FEIS, Jean FUCHS, Irmine GREISCHER, Didier MOUGET, Jean-Michel PACAUD, Geneviève PESCATORE, Arthur PHILIPPE
Secretary	Denise LOSCH

Committee Banks

Chairman	Arthur PHILIPPE
Members	Stéphane BOSI, Ernest CRAVATTE, Serge DE CILLIA, Jean-Claude FINCK, Charles HAMER, Roger H. HARTMANN, Pierre KRIER, André MARC, Paul MOUSEL, Frédéric OTTO, Philippe PAQUAY, Jean-Nicolas SCHAUS, Claude SIMON, Romain STROCK, Carlo THILL, Klaus-Michael VOGEL, Ernst-Dieter WIESNER
Secretary	Martine WAGNER

Committee Compliance

Chairman	Arthur PHILIPPE
Members	Patrick CHILLET, Alain HONDEQUIN, Jean-Marie LEGENDRE, Jean-Noël LEQUEUE, Thierry LOPEZ, Vafa MOAYED, Didier MOUGET, Marc OLINGER, Jean-Jacques ROMMES, Jean-Nicolas SCHAUS, Claude SIMON, Jean STEFFEN, Romain STROCK, Marie-Anne VOLTAIRE, Marco ZWICK
Secretary	Ronald KIRSCH

Committee Banking Accounting

Chairman	Arthur PHILIPPE
Members	Volkert BEHR, André-Marie CRELOT, Eric DAMOTTE, Serge DE CILLIA, Doris ENGEL, Frank BISDORFF, Carlo LESSEL, Bernard LHOEST, Vafa MOAYED, Carole ROEDER, Daniel RUPPERT, Jean-Nicolas SCHAUS, Thomas SCHIFFLER, Claude SIMON, Romain STROCK, Alain WEBER
Secretary	Danièle GOEDERT

Committee Company domiciliation

Chairman	Jean-Nicolas SCHAUS
Members	Gérard BECQUER, Carlo DAMGE, Johan DEJANS, Lucy DUPONG, Victor ELVINGER, Guy HARLES, Rüdiger JUNG, Jean LAMBERT, Carlo SCHLESSER, Christiane SCHMIT, André WILWERT, François WINANDY
Secretary	Luc PLETSCHETTE

Committee Pension funds

Chairman	Jean-Nicolas SCHAUS
Members	Freddy BRAUSCH, Christiane CAMPILL, Simone DELCOURT, Jacques ELVINGER, Rafik FISCHER, Fernand GRULMS, Robert HOFFMANN, Claude KREMER, Anne-Christine LUSSIE, Jacques MAHAUX, Olivier MORTELMANS, Geneviève PESCATORE, Arthur PHILIPPE, Jean-Paul WICTOR, Claude WIRION
Secretary	Marc PAULY

Committee Information Technology

Chairman	Simone DELCOURT
Members	Nico BARTHELS, Virginie BLAISE, Jean-Luc FRANCK, Damien GHIELMINI, David HAGEN, Marc HEMMERLING, Bruno LEMOINE, Jean-Luc MARTINO, Claude MELDE, Renaud OURY, Alain PICQUET, François SCHWARTZ, Bernard SIMON, Dominique VALSCHAERTS, Serge WEBER
Secretary	Emile BARTOLE

Committee Legal experts

Chairman	Jean-Nicolas SCHAUS
Members	Philippe BOURIN, Maria DENNEWALD, Philippe DUPONT, Irmine GREISCHER, André HOFFMANN, Rüdiger JUNG, Jean-Luc KAMPHAUS, Christian KREMER, Jacques LOESCH, André LUTGEN, Yves PRUSSEN, Jean STEFFEN, Romain STROCK, Marc WEITZEL
Secretary	Geneviève PESCATORE

Committee Covered Bonds

Chairman	Arthur PHILIPPE
Members	Janine BIVER, Serge DE CILLIA, Reinolf DIBUS, Thomas FELD, Roby HAAS, Jean-François HEIN, Marc HENRY, Hans-Dieter KEMLER, Raymond SCHADECK, Jean-Nicolas SCHAUS, Thomas SCHIFFLER, Hagen SCHMIDT, Claude SIMON, Romain STROCK, Bruno STUCKENBROEKER, Markus THESEN
Secretary	Michèle TRIERWEILER

Committee Securities Markets

Chairman	Arthur PHILIPPE
Members	Danièle BERNA-OST, André BIRGET, Daniel DAX, Serge DE CILLIA, Vincent DECALF, Axel FORSTER, Patrick GEORTAY, Robert HOFFMANN, Philippe HOSS, Françoise KAUTHEN, Claude KREMER, François LENERT, Jean-Nicolas SCHAUS, Richard SCHNEIDER, Jean-Marie SCHOLLER, Christiane SCHON, Claude SIMON, Henri WAGNER, Marco ZWICK
Secretary	Annick ZIMMER

Committee Undertakings for Collective Investment

Chairman	Jean-Nicolas SCHAUS
Members	Freddy BRAUSCH, Simone DELCOURT, Jacques DELVAUX, Jacques ELVINGER, Rafik FISCHER, Jean-Michel GELHAY, Irmine GREISCHER, Joëlle HAUSER, Robert HOFFMANN, Rüdiger JUNG, Georges KOHR, Claude KREMER, Julian PRESBER, Marc SALUZZI, Gilbert SCHINTGEN, Alex SCHMITT, Thomas SEALE, Claude SIMON, Bernard TANCRE, Camille THOMMES, Dominique VALSCHAERTS, Eric VAN DE KERKHOVE, Paolo VINCIARELLI, Julien ZIMMER, Patrick ZURSTRASSEN
Secretary	Jean-Marc GOY

Committee Support PFS

Chairman	Arthur PHILIPPE
Members	Sonny BISDORFF-LETSCH, Marc BREDEN, Alain DE FRENNE, Jean-Marc FANDEL, David HAGEN, Pierre HENIN, Gérard HOFFMANN, Renaud JAMAR DE BOLSEE, Patrick JOST, Marc LAMESCH, Charles MANDICA, Marcel ORIGER, Geneviève PESCATORE, Yves REDING, Gérard B. RIVOLLIER, Jean-Nicolas SCHAUS
Secretary	Claude BERNARD

Committee SICAR

Chairman	Jean-Nicolas SCHAUS
Members	Freddy BRAUSCH, Christiane CAMPILL, Daniel DAX, Simone DELCOURT, Jacques ELVINGER, Amaury EVRARD, Alain KINSCH, Claude KREMER, Arthur PHILIPPE, Mark TLUSZCZ
Secretary	Daniel CICCARELLI

Committee Securitisation

Chairman	Jean-Nicolas SCHAUS
Members	Christiane CAMPILL, Philippe DUPONT, Philippe HOSS, Christian KREMER, Isabelle LEBBE, Marc LIMPACH, Tom LOESCH, André PRÜM, Alex SCHMITT, Günter SIMON, Tom VERHEYDEN, Henri WAGNER
Secretary	Cliff BUCHHOLTZ

APPENDICES

APPENDICES

1. THE CSSF IN FIGURES

	Prudential Supervision							Support departments		Matters of general interest			
	General supervision	Supervision of banks	Supervision of UCIs	Supervision of PFS	Supervision of securities markets	Supervision of pension funds, SICARs and securitisation undertakings	Supervision of IT and support PFS	Administration and Finance	IT systems	Management	Director General's advisors	General Secretariat	TOTAL
Letters	449	1.782	16.727	1.051	4.029	1.311	486	765	189	70	264	3.385	30.508
Meetings	72	224	159	151*	53	25	119	108	60		154*	10	984
On-site inspections	117	52	2	6		1							178
Internal committee meetings													
> Committee Banks	2												2
> Committee Banking Accounting	3												3
> Committee Covered Bonds		2											2
> Committee PFS				2									2
> Committee Securities Markets					1								1
> Committee SICAR						2							2
> Committee Securitisation						7							7
> Committee Information Technology									1				1
> Consultative committee Anti-Money Laundering											1		1
> Committee Legal experts											6		6
> Committee UCIs											4		4
> Consultative committee for prudential regulation												4	4
National meetings	25		1	1	2	4	30		12			5	80
International meetings	200		6		25	7	4		9	4	23	18	296
Meetings with homologous authorities		30	1	2							17		50
Speeches	15	1			2	2	25		3	6	6	3	63
Articles published	1		1									1	3

* Including the joint meetings of the departments and functions concerned.

2. THE FINANCIAL CENTRE IN FIGURES

Situation as at 31 December 2007

BANKS

Number	156
Balance sheet total	EUR 915.445 billion
Net profit	EUR 5.124 billion
Employment	26,139 people

UNDERTAKINGS FOR COLLECTIVE INVESTMENT (UCI)

Number	2,868
Number of entities	11,115
Total assets	EUR 2,059.395 billion

MANAGEMENT COMPANIES

Number	180
Employment	2,348 people

PENSION FUNDS

Number	13

INVESTMENT COMPANIES IN RISK CAPITAL (SICAR)

Number	182
Balance sheet total	EUR 18.527 billion

SECURITISATION UNDERTAKINGS

Number	17

OTHER PROFESSIONALS OF THE FINANCIAL SECTOR (PFS)

Number	215
Balance sheet total	EUR 107.703 billion
Net profit	EUR 715.702 millions
Employment	12,174 people

Total employment in supervised entities	40,661 people

3. CONTACT TELEPHONE NUMBERS

Commission de Surveillance du Secteur Financier

Address	110, route d'Arlon L-1150 Luxembourg
Postal address	L-2991 Luxembourg
Switchboard	26 25 1 - 1
Fax	26 25 1 - 601 (executive board) - 603 (general supervision / banks) - 604 (UCI) - 605 (pension funds, SICAR and securitisation) - 606 (securities markets) - 607 (PFS) - 601 (support PFS) - 608 (administration) - 614 (IT)

The full directory of the CSSF is available on the website www.cssf.lu under the heading "Contact".