

**ANNUAL
REPORT
2013**



**COMMISSION
DE SURVEILLANCE
DU SECTEUR
FINANCIER**

Commission de Surveillance du Secteur Financier

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PREFACE

For the Luxembourg financial centre, 2013 will be remembered as a good vintage year after which most indicators were positive.

Indeed, as it appears from the detailed information and figures included in this report, it can be noted that the number and profits of the banks established in the financial centre increased substantially, as well as the volume of assets entrusted to the management of the different types of Luxembourg undertakings for collective investment, including specialised funds and SICARs, pension funds and securitisation undertakings. This healthy financial sector as a whole had also an impact on the development of the three PFS categories and on the performances of the financial markets.

2013 can rightly be regarded as having been both a consolidation year because the financial centre strengthened its foundation and extended its diversification and as a transition year as the financial centre firmly focusses on a future marked by a standardised supervision and regulation as well as by an increased innovation and transparency of the financial services.

In its recent evaluation report on Luxembourg, the International Monetary Fund certified the resilience of the financial centre and emphasised the extent to which it is important that the CSSF, as regulator of this financial centre, continues to impose high standards, ahead of the requirements imposed by the EU and international authorities. Indeed, compliance with such standards at the highest quality level is essential to maintain the confidence of the markets. An international financial centre, all the more so if it hardly has a domestic market, would simply put itself offside and jeopardize its reputation if it ran after the illusion that it can exploit a poorly understood regulatory arbitrage.

In order to ensure the sustainability of private banking and wealth management in Luxembourg, 2013 was the right time for the Luxembourg authorities to turn the page and align Luxembourg with a generally accepted tax transparency approach, without reservations, restrictions or doubts which have been overcome and which were finally harmful for the financial centre. The noticeable replacement of old clients with clients with a different profile, the arrival of many financial institutions from different countries, the enhancement of the financial centre's image prove the Luxembourg authorities to be right. They should not miss the opportunity to complete this movement by taking, without further delay, the necessary concrete measures in order to eliminate the texts and administrative practices which, rightly or wrongly, may be perceived to be, from the outside, barriers to the highly-affirmed principles of transparency in the fields of tax or of the fight against money laundering.

Henceforth, even more than in the past, the success of the financial centre will depend on the quality of the products and services offered. The private sector faces the challenge to provide the evidence that it knows better or otherwise than the competition. For the authorities, even if their action is considered, by definition, as undertaken in the public interest, and always concerns, directly or indirectly, financial product and service consumer protection, this aspect of their mission has taken on a new dimension. The CSSF intends to continue to strengthen its interventions in this respect, that have led it, in 2013, inter alia, to draft a regulation on out-of-court customer complaint settlement and to develop proposals to improve financial education.

Maintaining the attractiveness of the financial centre requires continuing the enhancement of a governance which allows developing its assets such as consistency in the various components of the financial centre thanks to their proximity, the speed of response to innovations, the reliability and reachability of the authorities.



First and foremost, the Government and Parliament will face, shortly, a huge legislative programme in the financial sector which arises from the great regulatory thrust from the EU bodies. If Luxembourg managed to position itself advantageously by transposing, within the relevant time-frame, the directive on alternative investment funds, which offers promising prospects, it should not relent in the often-thankless efforts of the efficient introduction into national law of EU texts. The CSSF is equipped to give a hand for this task.

There are also areas for the legislator which are not yet fully harmonised and which allow thus to stand out by benefiting from the wide-ranging expertise of the private sector, with however this warning that it is the actors of the public sector themselves which should hold the feather in the legislative drafting. There are also aspects which require investments other than regulatory investments, such as infrastructures, in particular in the field of new technologies and which are crucial for the financial centre.

The regulator has to play its role in the governance of the financial centre. The CSSF has focussed on every aspect, whether by showing its openness with respect to innovations such as virtual currencies, crowdfunding or the implementation of venues for the trading of various financial products, provided that they comply with the rules and standards to be marketed, or by raising the perception of Luxembourg through the organisation of events such as the IOSCO Annual Conference which brought together regulators from around the world in Luxembourg.

The supervisory authority must help to ensure and justify this necessary confidence the professionals and their customers have placed in the financial centre. To fulfil this mission, it must have the independence, powers and resources that are commensurate with the requirements of its peers, which enable it to maintain itself in particular within the European supervisory authorities and, in the first place, in the context of the Single Supervisory Mechanism under the aegis of the European Central Bank. Without an increase of the CSSF's powers to sanction or reorganise, liquidate or resolve entities in an irregular or dangerous situation, it will not be able to fully meet the expectations.

The CSSF has already invested a lot and continues to invest significantly in material resources. It puts priority on the IT developments supporting its own agents, but also all the players of the financial centre. The construction of the new building which is necessary to provide the staff with the best possible working conditions is progressing in accordance with the timeline.

Above all, the CSSF's agents are to be kept front and foremost. By exceeding 500 people, their number is ever increasing and this increase reflects the multiplicity and complexity of the tasks incumbent on them. Beyond the number, the CSSF seeks and manages to find a staff with high professional qualifications and experience. A special emphasis is also given to the development of the working methods which allows either staff member to make full use of his/her talents by benefiting as much as possible from cross-cutting cooperation and synergies between the departments. The current context is however such that workload is high for everybody, but everybody should be allowed to feel proud about his/her professional contribution to building a better finance in service of the public. Consequently, the Executive Board of the CSSF would like to thank any of its agents for their work over the past year.

Jean GUILL
Director General



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SUMMARY

For the Luxembourg financial centre, 2013 represented a consolidating as well as a transitional year with a positive end.

Indeed, the number and the results of banks established in the centre increased as did the volume of assets entrusted to the management of the different types of Luxembourg undertakings for collective investment including specialised investment funds, SICARs, pension funds and securitisation undertakings. The well-being of the whole financial sector also influenced positively the development of the PFS (investment firms, specialised PFS and support PFS) as well as the financial markets' performance.

In a future characterised by a harmonisation of the supervision and regulation and by an intensification of innovation and transparency in the financial services, the success of the financial centre will mainly depend on a good governance and on the quality of the products and services provided.

International aspects of supervision

2013 was characterised, on the one hand, by works at European level in order to put in place the Single Supervisory Mechanism and the Single Resolution Mechanism and, on the other hand, by the intensification of the activity of the European supervisory authorities (the EBA, ESMA and EIOPA) in order to harmonise the regulations and implement regulatory and implementing technical standards. The cooperation between national authorities within supervisory colleges for banking groups operating on a cross-border basis consumed a significant amount of the CSSF's resources. It should also be noted that in September 2013, the 38th Annual Conference of IOSCO was held in Luxembourg which gathered about 700 representatives of the authorities for the regulation of securities markets and futures markets as well as members of the international financial community from 113 jurisdictions around the world.

147 credit institutions

Balance sheet total: EUR 713.38 billion

Net profit: EUR 3,565 million

The number of banks increased by six entities and reached 147 entities as at 31 December 2013. Nine banks started their activities whereas three banks ceased their activities during the year.

The aggregated balance sheet total reached EUR 713.4 billion at the end of 2013, i.e. a decrease of 2.9% compared to 2012. This decrease was shared by 42% of the banks of the financial centre, a majority of which belong to the banking groups established in the euro area. The decreases in the activities reflect the necessity for certain European banks to adapt their risks and structures of the balance sheet to their capacity to manage and support these risks (deleveraging). However, the increase in the balance sheet total of certain banks resulted, among others, from the takeover of activities or development of new activities. In the latter case, the banks concerned generally originated from non-EU countries.

Net profit of the Luxembourg banking sector reached EUR 3,565 million (-0.9% compared to 2012). This result is the conjugation of two opposite developments: the decrease of the interest margin which results from the decrease of the balance sheet and from the very low level of interest rates and the increase of the net commissions received and of the other net income in the wake of the good stock market performance which positively influenced the value of banking assets and assets under management. It should be noted that the downward trend in 2013 does not concern all banks of the financial centre, as shown by the 44% of banks whose net result increased over one year.

314 PFS (107 investment firms, 126 specialised PFS, 81 support PFS)

Balance sheet total:

Investment firms: EUR 3.09 billion; specialised PFS: EUR 10.88 billion; support PFS: EUR 1.09 billion

Net profit:

Investment firms: EUR 157.3 million; specialised PFS: EUR 219.3 million; support PFS: EUR 42.9 million

With 20 new entities authorised in 2013 and 24 which gave up their authorisation, the number of PFS of all categories decreased in 2013. The net development in the number thus turned negative for the investment firms (-2 entities) and support PFS (-4 entities) whereas the rising trend of the number of specialised PFS was maintained with +2 entities.

The aggregated balance sheet total of investment firms reached EUR 3.09 billion as at 31 December 2013, as against EUR 3.62 billion at the end of 2012. This decrease of 14.4% mainly results from the transformation of two investment firms with a significant balance sheet total into management companies (authorised under Chapter 15 of the law of 17 December 2010 relating to UCIs). The aggregated balance sheet total of specialised PFS increased from EUR 9.46 billion at the end of 2012 to EUR 10.88 billion at the end of 2013 (+15%), due, among others, to the increase in the volume of activities as regards lending operations and securities lending. The aggregated balance sheet total of support PFS also increased from EUR 1.01 billion at the end of 2012 to EUR 1.09 billion as at 31 December 2013 (+7.8%).

Net results of investment firms dropped by 50.7% largely due to the transformation of two significant players into management companies. However, the majority of investment firms reported a stable net result compared to the previous year. Some even reported a slight increase. The aggregated net result of specialised PFS registered a considerable decrease of 39.1%, 90% of which is attributable to one big entity. Except for the development of this entity, the majority of specialised PFS reported an increase in net results compared to 2012. For support PFS, the net results increased by 19.8% and amounted to EUR 42.9 million at the end of 2013.

6 payment institutions

5 electronic money institutions

The number of payment institutions and electronic money institutions registered on the official list slightly increased in an emerging market which seeks its cruising speed. The CSSF noticed a certain interest from several players to establish themselves in Luxembourg to benefit from this market opportunity.

3,902 UCIs

13,685 units

Total net assets: EUR 2,615.4 billion

195 management companies

12 alternative investment fund managers (AIFMs)

In 2013, the UCI sector registered a 9.7% growth in net assets under management, originating for 83.6% from net subscriptions and for 16.4% from the positive performance of financial markets.

After a slowdown in 2012, the number of UCIs improved again by 1.6% (i.e. +61 entities). Taken separately, the number of specialised investment funds (SIFs) increased by 5.2% (+77 entities). SIFs now represent 40.0% in terms of number of UCIs; in terms of managed assets, their share totals 11.7%. When taking into account umbrella funds, a total of 13,685 economic entities were active on 31 December 2013, which represents a new record.

With 195 active entities, the number of management companies authorised pursuant to Chapter 15 of the law of 17 December 2010 relating to UCIs increased by 15 entities following 21 new authorisations and six deregistrations mainly due to the restructuring of different groups resulting in mergers and cessation of business.

On the regulatory level, it is important to mention the entry into force of the law of 12 July 2013 on alternative investment fund managers (AIFM Law) which transposes the AIFM Directive into Luxembourg law. The aim is to submit the managers of alternative investment funds to a harmonised regulatory framework at the European level and, at the same time, to introduce a European passport which will enable these managers to provide their management services and to distribute the alternative investment funds they manage in all EU Member States. Following the entry into force of the AIFM Law, 12 entities were authorised as alternative investment fund manager during the year.

279 SICARs

Balance sheet total: EUR 30.4 billion

With 22 new entities authorised in 2013 and 19 deregistrations, the number of investment companies in risk capital (SICARs) slightly increased compared to the previous year (+3 entities). When taking into account umbrella SICARs, a total of 363 economic entities were active on 31 December 2013. As regards the investment policy, SICARs showed a clear preference for private equity.

31 authorised securitisation undertakings

In the light of one new authorisation and two deregistrations, the number of authorised securitisation undertakings fell by one entity during the year. However, the balance sheet total of authorised securitisation undertakings increased by EUR 3.7 billion and amounted to EUR 19.6 billion at the end of the year.

14 pension funds

Whereas the number of pension funds remained the same with 14 entities authorised as at 31 December 2013, the activities and the volume of the pension funds slowly improved during the year.

Total employment in the supervised entities: 44,222 people

(of which banks: 26,237 people, investment firms: 2,560 people, specialised PFS: 3,201 people, support PFS: 8,971 people, management companies: 3,253 people)

Total employment in the financial sector improved by 0.5%, i.e. 218 people, during 2013. However, depending on the category of financial players, the situation diverges.

Employment in the banking sector dropped by 1.1% due mainly to staff cuts in 12 banks. Another major factor which explains the decrease in employment is the ongoing restructuring and consolidation of the activities following mergers and acquisitions. Other banks, active in investment funds, preferred to rationalise processes by increasingly using automation and by outsourcing certain functions to financial centres with lower costs, due to control in staff costs. Finally, the three banks which ceased their activities in 2013 also contributed to the decrease in the banking employment. This decrease was not compensated by the creation of jobs in the nine banks which started their activities during the year.

The number of jobs in investment firms decreased by 3.8%. This decrease is mainly due to three investment firms with a high number of staff which were transformed into management companies. However, the staff of specialised PFS increased by 5.1% as a result of a transfer of activities and of the relevant personnel from a

bank to a specialised PFS. These developments show that there is a transfer of activities between the different categories of professionals with no impact on the total number of staff in the financial sector.

The staff of support PFS slightly decreased by 0.5%.

The positive development of staff in management companies (+18.6% in 2013) is mainly due to the change of status of three investment firms resulting in a transfer of personnel as well as to the reorganisation of certain big groups in Luxembourg with, as a consequence, the internal assignment of personnel to the management companies. The efforts made by the management companies to continuously enhance their organisational environment are also a factor to be taken into account in this context.

1,630 prospectuses, base prospectuses and other approved documents

631 supervised issuers

0.96 million reported transactions in financial instruments

The number of files submitted in Luxembourg for the approval of prospectuses to be published when securities are offered to the public or admitted to trading on a regulated market rose compared to 2012 (+9.2%).

The CSSF supervises issuers whose securities are admitted to trading on a regulated market and whose home Member State is Luxembourg for the purposes of the Transparency Law. Their number reached 631, of which 229 Luxembourg issuers. The supervision involves a general follow-up of regulated information to be published by issuers as well as the enforcement of the financial information, i.e. the assessment of compliance of the financial information with the relevant reporting framework, namely the applicable accounting standards.

As regards the supervision of markets and market operators, the CSSF received about 0.96 million reports on transactions in financial assets which allow the observation of market trends and the identification of possible offences. In the framework of the law on market abuse, the CSSF opened three investigations in relation to insider dealing and/or market manipulation and dealt with 61 requests from foreign authorities.

Public oversight of the audit profession

The public oversight of the audit profession covered 69 *cabinets de révision agréés* (approved audit firms) and 227 *réviseurs d'entreprises agréés* (approved statutory auditors) as at 31 December 2013. The oversight also includes 47 third-country auditors and audit firms duly registered in accordance with the law of 18 December 2009 concerning the audit profession.

As regards the missions performed in the framework of statutory audits and other missions exclusively entrusted to them by law, the *réviseurs d'entreprises agréés* and *cabinets de révision agréés* are subject to a quality assurance review, organised according to the terms laid down by the CSSF in its capacity as supervisory authority.

611 customer complaints

Pursuant to its specific competence as regards consumer complaint handling, laid down in CSSF Regulation N° 13-02 relating to the out-of-court resolution of complaints, the CSSF received 611 complaints last year, a majority (52%) of which concerned payment service issues. Complaints related to private banking come second with 12% of the total of complaints handled.

493 agents**Operating costs of the CSSF in 2013: EUR 56.4 million**

2013 was marked by the ongoing increase in the CSSF's staff (+58 agents) in order to face the growing workload resulting notably from the implementation of the Single Supervisory Mechanism at European level, the introduction of new prudential requirements and, in general, the increase in the volume and complexity of financial products. The workload is also supplemented by numerous on-site inspections, which became an important pillar of the prudential supervision exercised by the CSSF.

CHAPTER I

GOVERNANCE AND FUNCTIONING OF THE CSSF



1. Principles
2. Governing bodies
3. Committees
4. Human resources
5. CSSF library
6. New CSSF headquarters
7. Information systems
8. Annual accounts of the CSSF - 2013

1. PRINCIPLES

The CSSF, established by the law of 23 December 1998, with effect on 1 January 1999, is a public institution with legal personality and financial autonomy. It operates under the authority of the Minister responsible for the financial centre, i.e. the Minister of Finance Mr Pierre Gramegna.

1.1. CSSF bodies

The CSSF's board of directors is composed of seven members appointed by the Grand Duke on the proposal of the Government in Council for a period of five years. The powers conferred upon the board of directors notably include the annual adoption of the CSSF's budget and the approval of the financial statements and of the report of the CSSF's executive board, which are submitted to the board of directors before their presentation to the Government for approval. It also sets the general policy as well as the annual and long-term investment programmes which are submitted to it by the executive board before being submitted for approval to the Minister of Finance. Meetings and deliberations of the board of directors take place according to its internal rules. The board of directors is not competent to intervene in the CSSF's prudential supervisory matters.

The senior executive authority of the CSSF is the executive board, composed of a director general and between two and four directors, appointed by the Grand Duke on the proposal of the Government in Council for a period of five years. The executive board works out measures and takes the decisions it deems useful and necessary for the fulfilment of the CSSF's mission and for its organisation. Moreover, it sets up a five-year "target contract" with the Minister of Finance. The executive board is responsible for the reports and proposals it is obliged to address to the board of directors and the Government.

1.2. Decision-making process

According to its internal rules, the executive board must meet collectively at least once a week to take the decisions required to accomplish the mission of the CSSF. The executive board is responsible collectively even if each individual member runs one or several departments.

The decisions taken in the context of the CSSF's mission may be referred to the *Tribunal administratif* (Administrative Court), which decides on the merits of the case. These recourses must be instituted, under penalty of foreclosure, within a month from the notification of the decision.

1.3. Drawing-up of regulations

The CSSF has the power to make regulations within the limits of its competences and missions, in accordance with Article 9(2) of the law of 23 December 1998. Draft regulations must be submitted to the Consultative committee for prudential regulation or the Consultative committee for the audit profession. The CSSF regulations are published in the *Mémorial*.

The legislative framework applicable to the financial sector is complemented by circulars issued by the CSSF with a view to specifying how legal provisions should be applied and issuing recommendations on conducting business in the financial sector.

Following the example of international forums and counterpart authorities, the CSSF has established a broad consultation procedure, which involves, during the stage of drawing-up the regulations and circulars, the professionals of the financial sector, as well as any other person concerned, notably via expert committees and ad hoc working groups.

1.4. Financing of the CSSF and account auditing

The CSSF is authorised to levy taxes on supervised persons and undertakings to cover its staff, financial and operating costs. The Grand-Ducal regulation of 28 October 2013 lays down the amounts applicable and

guarantees full financing of the operating costs.

The Government appoints a *réviseur d'entreprises agréé* (approved statutory auditor) on the proposal of the CSSF's board of directors for a period of three years. The mission of the *réviseur d'entreprises agréé* is to audit and certify the CSSF's accounts and to submit a detailed report on the CSSF's accounts to the board of directors and the Government at the close of the financial year. The *réviseur d'entreprises agréé* may be charged by the board of directors with making specific checks.

The CSSF is subject to the control of the Court of Auditors (*Cour des comptes*) as to the appropriate use of the public financial participation it receives.

2. GOVERNING BODIES

Board of Directors

Chairwoman	Sarah KHABIRPOUR	Premier Conseiller de Gouvernement, Ministry of Finance (until 28 February 2014)
Vice-Chairwoman	Isabelle GOUBIN	Conseiller de direction 1 ^{ère} classe, Ministry of Finance
Members	Rima ADAS	Institut des Réviseurs d'Entreprises
	Ernst Wilhelm CONTZEN	Chairman of the Luxembourg Bankers' Association, Luxembourg
	Marc SALUZZI	Chairman of the Association of the Luxembourg Fund Industry
	Marny SCHMITZ	Attachée d'administration, Ministry of Finance
	Claude WIRION	Member of the Executive Committee of the Commissariat aux Assurances
Secretary	Danielle MANDER	

Executive Board

Director General	Jean GUILL
Directors	Simone DELCOURT, Andrée BILLON, Claude SIMON



Executive Board of the CSSF

Left to right: Andrée BILLON, Jean GUILL, Simone DELCOURT, Claude SIMON

3. COMMITTEES

3.1. Consultative committees

3.1.1. Consultative committee for prudential regulation

The Government may seek advice from the committee, constituted by the law of 23 December 1998 establishing a financial sector supervisory commission (Commission de surveillance du secteur financier), on any draft law or Grand-Ducal regulation in the field of the financial sector falling within the competence of the CSSF. The CSSF's executive board shall seek an opinion from the committee on any draft regulation of the CSSF other than related to statutory audits and the audit profession. Members of the committee may also seek its advice concerning the setting-up or application of prudential regulations overall or for specific issues. The external members of the committee are appointed by the Minister of Finance.

Committee composition:

Executive board of the CSSF:	Jean Guill (Chairman), Andrée Billon, Simone Delcourt, Claude Simon
Members:	Nicolas Buck, Serge de Cillia (from 6 February 2014), Alain Feis, Georges Heinrich, Jean-Jacques Rommes (until 5 February 2014), Robert Scharfe, Carlo Thill, Camille Thommes
Secretary:	Danielle Mander

3.1.2. Consultative committee for the audit profession

The Government may seek advice from the committee, established by the law of 18 December 2009 concerning the audit profession, on any draft law or Grand-Ducal regulation related to statutory audits and the audit profession subject to the oversight of the CSSF. The CSSF's executive board shall seek an opinion from this committee on any draft regulation of the CSSF related to statutory audits and the audit profession. Members of the committee may also seek its advice concerning the setting-up or application of the regulation of public oversight of the audit profession overall or for specific issues. The external committee members are appointed in accordance with Article 15-1 of the law of 23 December 1998 establishing a financial sector supervisory commission (Commission de surveillance du secteur financier).

Committee composition:

Executive board of the CSSF:	Jean Guill (Chairman), Andrée Billon, Simone Delcourt, Claude Simon
Members:	Anouk Agnes (from 1 January 2014), Serge de Cillia, Philippe Meyer (until 31 December 2013), Sophie Mitchell, Jean-Michel Pacaud, Victor Rod, Daniel Ruppert, Marny Schmitz, Philippe Sergiel (from 1 January 2014), Anne-Sophie Theissen, Camille Thommes (until 31 December 2013)
Secretary:	Danielle Mander

3.2. Permanent and ad hoc expert committees

The expert committees shall assist the CSSF in analysing the development of the different areas of the financial sector, give their advice on any issue relating to their activities and contribute to the drawing-up and interpretation of the regulations relating to areas covered by the respective committees. In addition to the permanent committees listed below, ad hoc committees are formed to examine specific subjects.

The permanent expert committees are the following:

- Anti-Money Laundering Committee;
- Banks Issuing Covered Bonds Committee;
- Banks and Investment Firms Committee;
- Bank and Investment Firm Accounting Committee;
- Depositories Committee;
- Pension Funds Committee;
- Corporate Governance Committee;
- Undertakings for Collective Investment Committee;
- Financial Consumer Protection Committee;
- SICAR Committee;
- Audit Technical Committee;
- Securitisation Committee.

In 2013, the following people took part in the different expert and ad hoc committees of the CSSF:

ALONSO SANZ Elisa Nomura Bank (Luxembourg) S.A.	COLETTE Pierre-Louis Crédit Agricole Luxembourg
ADAS Rima Institut des réviseurs d'entreprises	CONTZEN Ernst Wilhelm The Luxembourg Bankers' Association
AREND Pascale Commissariat aux Assurances	CREPIN Jean-Marc Brown Brothers Harriman (Luxembourg) S.C.A.
BARBIER Jean-Louis Banque Raiffeisen	CROISÉ Daniel BDO Audit
BASENACH Karin European Consumer Centre	DANLOY Sébastien RBC Investor Services Bank S.A.
BECHET Marc-André Banque Degroof Luxembourg S.A.	DE CILLIA Serge The Luxembourg Bankers' Association
BIRASCHI Sonia State Street Bank Luxembourg S.A.	DE CROUY-CHANEL Henri Aurea Finance Company
BOSI Stéphane Banque de Patrimoines Privés	DELVAUX Jacques Notary
BOURIN Catherine The Luxembourg Bankers' Association	DOBBINS Martin State Street Bank Luxembourg S.A.
BRAUSCH Freddy Linklaters LLP	DOGNIEZ Nathalie KPMG Luxembourg
BRUCHER Jean Brucher Thieltgen & Partners	DOLLE Emmanuel KPMG Luxembourg
CARRÉ Olivier PricewaterhouseCoopers	DONDELINGER Germain Ministry of Higher Education and Research
CHAN YIN Victor KPMG Luxembourg	DUPONT Philippe Arendt & Medernach
CIMINO Pierre CACEIS Bank Luxembourg	DUREN Philippe PricewaterhouseCoopers
COLBERT Cheryl Ministry of Higher Education and Research	DUSEMON Gilles Arendt & Medernach

EDGE Christopher J. P. Morgan Bank Luxembourg S.A.	KREBS Bob Banque centrale du Luxembourg
ELVINGER Jacques Elvinger, Hoss & Prussen	KREMER Claude Arendt & Medernach
ENGEL Doris Banque et Caisse d'Épargne de l'État	KREMER Christian Clifford Chance
FEIS Alain Interinvest S.A.	KRIER Pierre PricewaterhouseCoopers
FISCHER Rafik KBL European Private Bankers S.A.	LACROIX Yves Arendt & Medernach
FLAUNET Martin Deloitte	LAM Benjamin Deloitte
GEBHARD Gerd Pecoma International S.A.	LANZ Christoph Banque Privée Edmond de Rothschild Europe
GEORTAY Patrick Linklaters LLP	LEBBE Isabelle Arendt & Medernach
GOEDERT Guy Union Luxembourgeoise des Consommateurs	LEFEVRE Olivier Deloitte
GOUBIN Isabelle Ministry of Finance	LEQUEUE Jean-Noël Association Luxembourgeoise des Compliance Officers du Secteur Financier
GRAND Samuel ABN Amro Bank (Luxembourg) S.A.	LHOEST Bernard Ernst & Young
GUAY Michel Institut des réviseurs d'entreprises	LIFRANGE Frédérique Elvinger, Hoss & Prussen
GUERRIER Eric Banque Privée Edmond de Rothschild Europe	LOPEZ Thierry Banque Internationale à Luxembourg
HAAS Christophe Institut des réviseurs d'entreprises	LUSSIE Anne-Christine BGL BNP Paribas
HALMES-COUMONT Claudia Pecoma International S.A.	MICALLEF David The Bank of New York Mellon (Luxembourg) S.A.
HAUSER Joëlle Clifford Chance	MISSON Christopher Pictet & Cie (Europe) S.A.
HENGEN Marc Association des Compagnies d'Assurances	MITCHELL Sophie Institut des réviseurs d'entreprises
HOFFMANN Guy Banque Raiffeisen	MOUSEL Paul Arendt & Medernach
HOFFMANN Robert Loyens & Loeff	MULLER Charles KPMG Luxembourg
HOSS Philippe Elvinger, Hoss & Prussen	NOCKELS Roland Banque centrale du Luxembourg
JANSEN Laurent BGL BNP Paribas	NOSBUSCH Danièle Ministry of Finance
JORDANT Olivier Ernst & Young	ORIGER Paul-Charles Association des Compagnies d'Assurances
KAYSER Nicki Linklaters LLP	PAULY François Banque Internationale à Luxembourg
KHABIRPOUR Sarah Ministry of Finance	PEPIN Andy Ministry of Finance
KOHL Aly Banque et Caisse d'Épargne de l'État	PETRY Pierre Banque Internationale à Luxembourg

PERARD Frédéric BNP Paribas Securities Services, succursale de Luxembourg	TESTA Sylvie Ernst & Young
PIERRE Gilles The Luxembourg Bankers' Association	THILL Carlo BGL BNP Paribas
PITSAER Yves KBL European Private Bankers S.A.	THOMA Patrick Ministry of Family, Integration and Greater Region
PRUM André University of Luxembourg	THOMMES Camille Association of the Luxembourg Fund Industry
RENAULT Olivier Société Générale Bank & Trust	THOUVENOT Thierry Institute of Internal Auditors
RIES Marie-Josée Ministry of Economy	TIXIER Valérie PricewaterhouseCoopers
ROMMES Jean-Jacques The Luxembourg Bankers' Association	VALSCHAERTS Dominique Société de la Bourse de Luxembourg S.A. / Finesti
RONKAR Marc Banque centrale du Luxembourg	VINCIARELLI Paolo Banque et Caisse d'Épargne de l'État
RUPPERT Daniel Ministry of Justice	VOGEL Klaus-Michael Deutsche Bank Luxembourg S.A.
SALUZZI Marc Association of the Luxembourg Fund Industry	VONCKEN Marc PricewaterhouseCoopers
SAUVAGE Benoît The Luxembourg Bankers' Association	WAGNER Henri Allen & Overy
SCHARFE Robert Société de la Bourse de Luxembourg S.A.	WATELET Patrick Citibank International Plc, Luxembourg branch
SCHINTGEN Gilbert UBS Fund Services (Luxembourg) S.A.	WEBER Alain Banque LBLux S.A.
SCHMITT Alex Bonn & Schmitt	WILLEM Vincent Institute of Internal Auditors
SCHMITZ Marny Ministry of Finance	WIRION Claude Commissariat aux Assurances
SEALE Thomas European Fund Administration S.A.	YIP Johnny Deloitte
SERGIEL Philippe PricewaterhouseCoopers	ZIMMER Julien DZ PRIVATBANK S.A.
SIMON Günter PricewaterhouseCoopers	ZURSTRASSEN Patrick Institut Luxembourgeois des Administrateurs
SIX Jean-Christian Allen & Overy	ZWICK Marco Association of Luxembourg Risk Management
TERWAGNE Benoît Esofac Luxembourg S.A.	

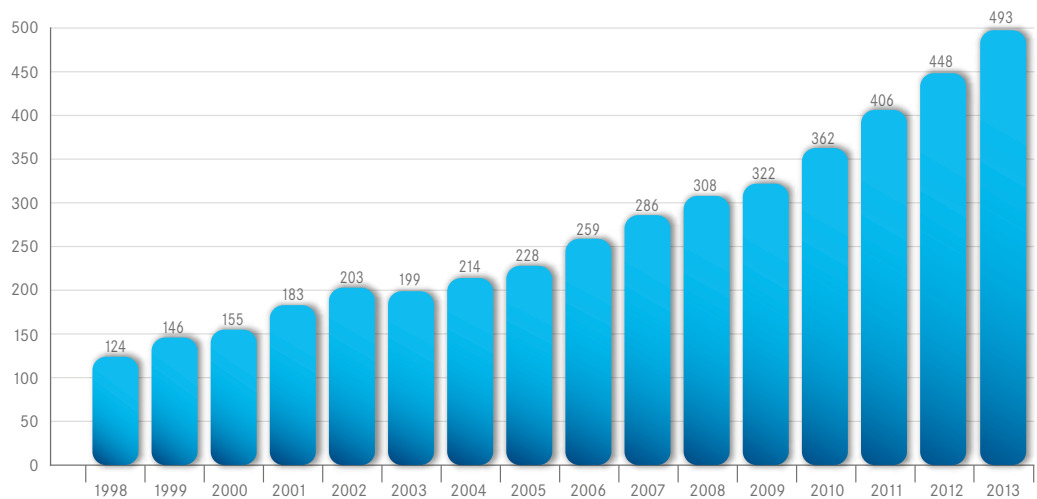
4. HUMAN RESOURCES

4.1. CSSF staff

As far as human resources are concerned, and as in the previous years, 2013 was marked by a significant rise in the number of staff. Thus, 58 agents were recruited. Following the resignation of 13 agents over that period, total employment reached 493 units as at 31 December 2013, representing a 10.04% increase compared to 2012. This is the equivalent of 435.70 full-time jobs, i.e. a 10.22% increase compared to 2012.

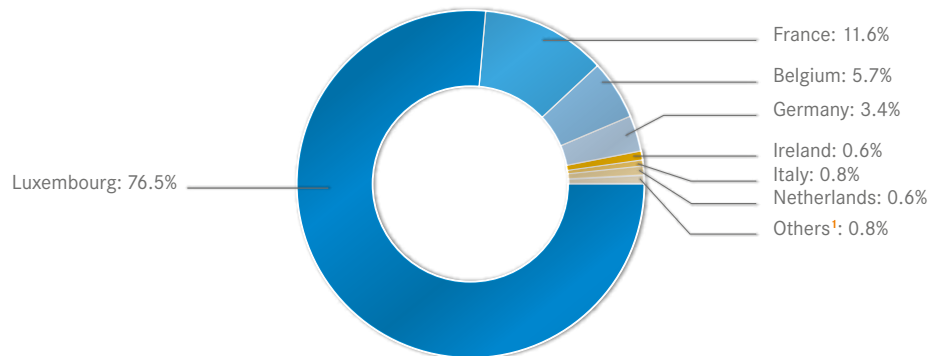
It must be highlighted that in the course of the year, the CSSF received around 1,868 job applications, including 285 spontaneous applications. As in the previous years, recruitment mainly focused on University degrees and candidates' competence.

Movements in staff numbers



CSSF agents represent 11 nationalities, the Luxembourg nationality being the most represented with 76.47% of the total staff.

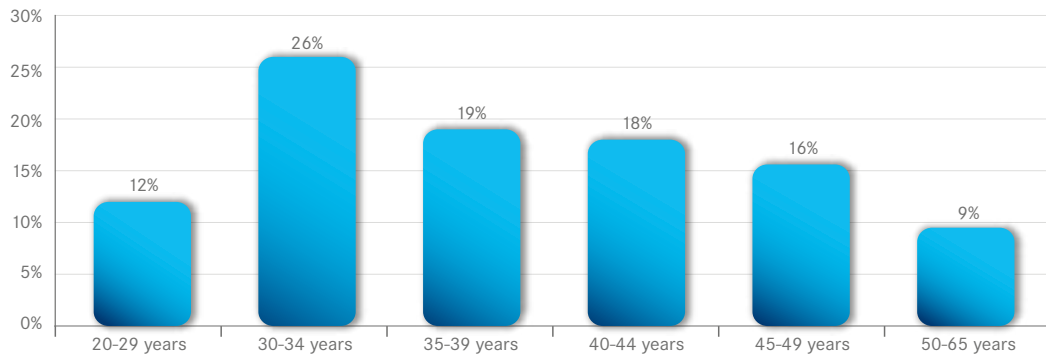
Breakdown of staff by nationality



The average age of CSSF staff members slightly decreased from 38.32 years as at 31 December 2012 to 38.17 years at the end of 2013. Women make up 49.69% of total staff and men 50.31%.

¹ Austria, Portugal, Romania, Spain.

Breakdown of staff by age



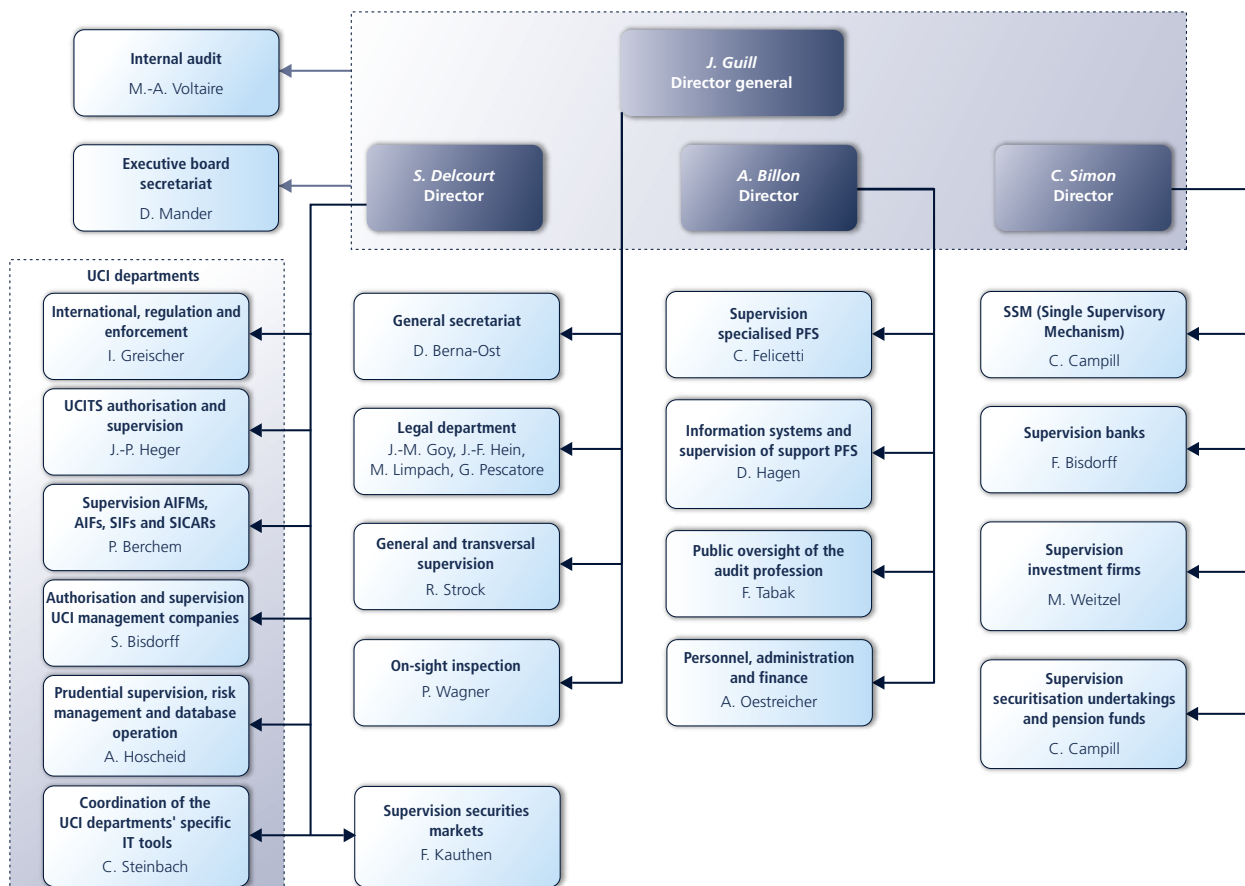
4.2. Staff training

CSSF staff followed 430 training courses in 2013.

Most of these courses were part of the lifelong training possibilities offered to CSSF agents. 58.31% of the courses were dedicated to finance, accounting and law, 8.34% to IT/office automation, 11.47% to management and human resources and 16.13% to languages. The remaining 5.75% covered subjects such as the security and professional techniques.

3,411 participations in training sessions were recorded in 2013. The CSSF staff counted a total of 1,749 ongoing training days, representing an average of 4.13 ongoing training days per agent.

4.3. Organisation chart



Detailed information on the CSSF's organisation is available on the CSSF website in the section "About the CSSF", sub-section "Structure/Organisation".

5. CSSF LIBRARY

The CSSF library is a reference library which is part of the Luxembourg libraries' network bibnet.lu since 2009. It is specialised in banking and financial law as well as financial economy. It contains more than 2,000 books and around 50 periodicals and update publications. The library has also a certain number of specialised electronic databases.

All the books in the library are listed in the general catalogue of the bibnet.lu network. The unified search engine of the collections of the network (www.a-z.lu) enables an easy search of the books available in the CSSF library and in all Luxembourg libraries.

The library is open to the public on prior request and by appointment, Monday through Friday from 9 a.m. to 11 a.m. and from 2 p.m. to 4 p.m..

6. NEW CSSF HEADQUARTERS

With a view to streamlining and efficiency, so as to concentrate on a single site the activities which, at a given time, were spread over on three different sites, the CSSF decided in 2011 to build new headquarters to cope with the increasing number of its agents and to enhance the processes and, therefore, the efficient functioning of the CSSF when carrying out the missions assigned to it.

The new building will provide about 7,000 square meters of office space (i.e. about 620 workstations), a canteen, a fitness room, a public library and many meeting, conference and training rooms.

Strong emphasis was placed on the energy concept of the building in order to reach a high level of performance combined with a maximum comfort, by minimising energy losses and consumption.

The demolition works and earthworks were completed in 2013 as scheduled.

The structural work is currently under way and its progress corresponds to the contract execution schedule.

As all authorisations have been granted and insofar as there is currently no delay as to the initial schedule, the receipt of the new headquarters is planned for the end of June 2015, so that the CSSF will be able to move into its new offices as from this date.



Demolition works



Earthworks

Construction of the 1st floor

Courtyard



7. INFORMATION SYSTEMS

The division in charge of the CSSF's IT systems is part of the department "IT systems and supervision of support PFS". This division is in charge of installing, maintaining and developing the CSSF's internal IT infrastructure as well as managing the electronic reporting of supervised entities.

7.1. Project "Registry"

In the European context, the CSSF responded to the exchange requirements of ESMA which, in 2012, initiated the project "Registry" (formerly "Omnibus") covering the needs arising from the AIFMD, UCITS Directives and MiFID, i.e. in particular the creation of a register allowing the identification of AIFMs, management companies of UCITS, investment firms under MiFID and the collection of prospectuses approved in accordance with the Prospectus Directive. ESMA set 24 February 2014 as the start-up date of the project "Registry". The "Registry"

is now operational and the CSSF provides ESMA with the information as regards the approved prospectuses. As regards the AIFM part, developments are under way in order to meet the deadlines set by ESMA, i.e. the end of 2014.

7.2. Legal Entity Identifier

The Legal Entity Identifier (LEI), created by the Financial Stability Board (FSB), enables the identification of the persons involved in financial transactions for the purpose of identifying the systemic risk. It will be used more systematically for reportings to be sent either to ESMA or the EBA.

The assignment of a pre-LEI at Luxembourg level did not take place in 2013 but this should change in 2014 as certain foreign bodies (particularly in France and in Germany) have already positioned on the market to propose these identifiers.

In Luxembourg, the work relating thereto is carried out under the aegis of the BCL. The CSSF is willing to contribute to this project, in particular as regards the transmission to the future operator of the supervised entities' public reference data, allowing thus a verification of the data provided by these entities when requesting a LEI assignment.

7.3. FINREP and COREP

The EBA published the XBRL taxonomies applicable to the new FINREP and COREP at the beginning of December 2013. The current version (V2.0.1)² will be used for COREP reportings of the first quarter 2014 as well as the subsequent reports.

The CSSF will request XBRL instances that are fully compatible with these taxonomies, including concerning compliance with the additional rules set out in the document "XBRL Filing Rules. COREP and FINREP Taxonomy 2.0.0"³ of the EBA and compliance with the formulas in the various taxonomies.

Given the fairly high risk that at least a few of the many formulas may, in some cases, fail while the underlying figures are actually correct, the CSSF has put in place the necessary mechanisms to disable certain taxonomy rules. Thus, if the EBA informs that certain rules are to be considered as disabled, the CSSF's configuration will be updated accordingly. Consequently, the CSSF recommends that reporting entities should make arrangements to send a report to the CSSF even if certain validation rules of the formula linkbase of the taxonomies fail.

In accordance with the "Recommendation On the use of the Legal Entity Identifier (LEI)" of the EBA, the CSSF requests the entities concerned by FINREP and COREP to use the LEI code to identify themselves within the XBRL instances.

The EBA plans to publish a version V2.1.0 of the set of taxonomies that should define (1) the corrections to the COREP reports and the validation rules, (2) the final version of the FINREP report and (3) the final version of the Asset Encumbrance (AE) report. This version is planned for all reports as from June 2014 (COREP and AE) and September 2014 (FINREP).

The CSSF's production chain was adapted in order to receive the COREP reports. The adaptation to FINREP and to AE will take place as soon as the final and official version V2.1.0 of the EBA is published.

² Internet link: <http://www.eba.europa.eu/-/eba-publishes-xbrl-taxonomy-for-remittance-of-supervisory-reporting-by-competent-regulatory-authorities>.

³ Internet link: <http://www.eba.europa.eu/documents/10180/502670/EBA+XBRL+Filing+Rules+for+v2.0.0.pdf>.

8. ANNUAL ACCOUNTS OF THE CSSF – 2013

BALANCE SHEET AS AT 31 DECEMBER 2013

<i>Assets</i>	<i>EUR</i>
Fixed assets	
- Intangible assets	
Payments on account and intangible assets in progress	2,125,288
	<u>2,125,288</u>
- Tangible assets	
Land and constructions	18,161,560
Other fixtures, fittings, tools and equipment	712,791
Payments on account and tangible assets in progress	8,408,027
	<u>27,282,378</u>
- Financial assets	3,000
	<u>3,000</u>
Current assets	
- Trade debtors	
with a residual term of up to one year	2,325,651
- Other debtors	
with a residual term of up to one year	203,159
- Cash at banks, in postal cheque accounts, cheques in hand	34,517,841
	<u>37,046,651</u>
Prepayments and accrued income	2,879,008
Balance sheet total (Assets)	<u>69,336,325</u>
<i>Liabilities</i>	
Own capital	
- Profit brought forward	12,216,035
- Result for the financial year	22,175,571
	<u>34,391,606</u>
Non-subordinated liabilities	
- Amounts owed to credit institutions	29,881,046
	<u>29,881,046</u>
- Debts on purchases and provision of services	
with a residual term of up to one year	2,868,192
- Tax and social security debts	
Social security creditors	1,959,012
- Other debts	
with a residual term of up to one year	236,469
	<u>5,063,673</u>
Balance sheet total (Liabilities)	<u>69,336,325</u>

PROFIT AND LOSS ACCOUNT AS AT 31 DECEMBER 2013

Charges

Consumption of merchandise and consumable raw materials	229,652
Other external charges	9,361,959
Staff costs	
- Wages and salaries	42,135,064
- Social security costs attributable to wages and salaries	2,396,712
Value adjustments on	
- Formation expenses and tangible and intangible fixed assets	166,273
Other operating charges	994,057
Interests and other financial charges	
- Other interests and charges	1,115,009
Total charges	56,398,726

Income

Net turnover	78,242,747
Other operating income	268,729
Other interest and financial revenues	62,821
Total income	78,574,297
Result for the financial year	22,175,571

Financial controller Deloitte Audit

CHAPTER II

EUROPEAN DIMENSION OF THE SUPERVISION OF THE FINANCIAL SECTOR



1. Supervision of banks
2. Supervision of financial markets
3. Cooperation within European bodies
4. List of European groups in which the CSSF participates

1. SUPERVISION OF BANKS

1.1. Banking Union

The Banking Union, which addresses the need for a harmonised regime for the supervision and management of banking crises, will be achieved through three pillars, namely the creation of a Single Supervisory Mechanism (SSM) for the single bank supervision, a Single Resolution Mechanism (SRM) for the common bank crisis management and resolution system, and a uniform system for protecting depositors' savings (DGS).

While the SSM, placed under the aegis of the European Central Bank (ECB), is already well under way, the negotiations concerning the SRM, which complements the SSM, ended only recently in a political agreement between the Council and the European Parliament. The SRM should be fully operational and the SRM Regulation should fully apply as from 1 January 2016, provided that enough Member States have ratified the intergovernmental agreement on the Single Resolution Fund for banks at that date.

Finally, the negotiations on the directive on deposit guarantee schemes ended at the end of 2013. This new directive is the basis for a possible third pillar of the Banking Union.

1.2. Single Supervisory Mechanism (SSM)

Effective 1 May 2013, i.e. 18 months before the ECB starts acting as supervisor of the banking sector, a new department called "SSM" (Single Supervisory Mechanism) was set up within the CSSF.

The task of the SSM department is to manage the role of the CSSF as member of the new architecture for the prudential supervision of banks in the EU under the aegis of the ECB and to follow the work of the EBA and the European Systemic Risk Board (ESRB) in this context.

The department also ensures a regulatory and coordinating mission for the regulation of banks at national and international level.

The SSM department prepares the meetings of the SSM's Supervisory Board and contributes to the setting-up and subsequent functioning of the SSM via its participation in committees and working groups within the ECB. Moreover, it coordinates the cooperation with the BCL in SSM matters. It should be stressed that in its capacity as member of the SSM's Supervisory Board, the CSSF will be asked to take up a position on draft decisions relating to all the banks in the participating Member States.

The CSSF also strengthened its capacities in terms of human resources within the department in charge of supervising banks and that in charge of on-site inspections.

1.2.1. Key principles of the organisational structure of the new supervisory regime

The ECB will be responsible for the efficient and consistent functioning of the SSM as a whole. It should assume its banking supervision responsibilities as of 4 November 2014. The single supervision will be exercised in two manners under the responsibility of the ECB.

- **Direct supervision of significant institutions under the oversight of the ECB, assisted by the national supervisory authorities**

The ECB will directly supervise the significant credit institutions of the participating countries, i.e. around 130 banking groups, representing almost 85% of total banking assets in the euro area.

In cooperation with the national competent authorities, the ECB will assess all the banks in the participating countries which are likely to be considered as significant according to the criteria laid down in the SSM Regulation and detailed in the Framework Regulation. Deciding whether a bank is significant or not will be based on the following criteria: (1) the total value of its assets; (2) the importance for the economy of the country in which it is located or the EU as a whole; (3) the significance of its cross-border activities; (4) whether or not it has requested and/or received public financial assistance from the European Stability

Mechanism (ESM) or the European Financial Stability Facility (EFSF); and (5) the fact that it is one of the three most significant banks of the country.

A list of the significant banks subject to the direct prudential supervision of the ECB will be published on the ECB's website. The classification of the credit institutions as significant or less significant will be reviewed on an annual basis. If, for three consecutive calendar years, a significant credit institution has not met any of the relevant thresholds for significance, the national competent authority becomes competent to directly supervise the entity concerned. Conversely, as soon as a less significant bank meets one of these thresholds, it will be considered as significant. Transfer of prudential supervisory tasks for a significant bank may be anticipated in exceptional circumstances, if it is obvious that the bank will no longer meet any of the relevant thresholds (if, for example, its total assets fall below the defined threshold following the sale of a significant operational unit).

Following the launch of the SSM, the ECB will have to ensure that the significant institutions have in place robust governance processes and mechanisms, including strategies and processes for assessing and maintaining the adequacy of their internal capital. To this end, Joint Supervisory Teams (JSTs) will be set up for the day-to-day supervision of every significant entity or group subject to the ECB's oversight. Every JST is composed of employees of the competent authorities involved in the supervision of the entity/group concerned and members of ECB staff. As the JSTs will be one of the main forms of cooperation between national competent authorities and the ECB, experienced CSSF agents will participate in the various supervisory teams for the institutions concerned.

• **Supervision by national authorities of “less significant” institutions under the oversight and within the framework laid down by the ECB**

The CSSF will be in charge of directly supervising all the other Luxembourg banks which are considered as “less significant”. As the ECB is responsible for ensuring the efficient and consistent functioning of the SSM, it will also ensure in this context that the applicable prudential rules and principles are complied with. The working methods of the CSSF will need to be in line with the instructions or guidelines laid down by the ECB. To this end, the ECB oversees the exercise of the supervision by the national authorities and the CSSF will regularly provide the ECB with the following information:

- key financial and regulatory information on the institutions (balance sheet, profit and loss account, risk indicators, prudential ratios);
- information on the decisions taken (either ex post or ex ante on topics deemed significant);
- assessment of the risk profile of every institution.

The CSSF shall also inform the ECB of any rapid and significant deterioration of the financial situation of a less significant bank.

The ECB may decide to take up direct supervision of any less significant bank when necessary, to ensure consistent application of the high prudential supervisory standards.

The SSM Regulation and the Framework Regulation do not modify in any way the prudential supervisory missions that are not defined in the SSM Regulation. Consequently, missions such as consumer protection and anti-money laundering remain with the CSSF.

1.2.2. Governance structures of the SSM

In accordance with the SSM Regulation, the planning and execution of the tasks conferred on the ECB shall be fully undertaken by the Supervisory Board as an internal body of the ECB.

The Supervisory Board has been operational since 30 January 2014. It is composed of Mrs Danièle Nouy, Chair, Mrs Sabine Lautenschläger, Vice-Chair, four ECB representatives and one representative of the national competent authority of each participating Member State. Where the national competent authority is not a central bank, the member of the Supervisory Board may decide to bring a representative from the Member State's central bank; this representative shall not have a voting right. Mr Claude Simon, Director, represents the CSSF at the Supervisory Board.

Executive decisions of the Supervisory Board shall be taken by a simple majority of its members according to the “one member, one vote” principle and by a qualified majority as defined in Article 16.4 of the EU Treaty for votes on regulations. Draft decisions proposed by the Supervisory Board shall be submitted to the Governing Council of the ECB for adoption; they shall be deemed adopted unless the Governing Council objects within a maximum period of ten working days.

1.2.3. Regulation

Under the terms of Regulation (EU) No 1024/2013 of 15 October 2013 conferring specific tasks on the ECB concerning policies relating to the prudential supervision of credit institutions (SSM Regulation), the EU establishes the SSM for the banks of the euro area and of the other EU Member States that wish to adhere to this mechanism. The SSM, composed of the ECB and the national competent authorities, is in charge of the prudential supervision of credit institutions in the participating countries.

Other provisions designed to organise the functioning of the SSM in greater detail are being adopted. Under the SSM Regulation, the ECB must adopt and publish a regulatory framework defining the arrangements for the cooperation between the ECB and the national competent authorities within the SSM (Framework Regulation). The final version of this document, which was submitted for public consultation, shall be published by 4 May 2014 at the latest.

Other substantive rules will be dealt with in separate legal acts, such as the draft regulation of the ECB on the supervisory fees, the rules of procedure of the Supervisory Board, amendments to the internal rules of the ECB, the internal confidentiality regime and information exchanges between monetary policy and supervisory tasks.

1.2.4. Implementation of the cooperation between national supervisors and the ECB

The ECB set up transitory structures to prepare for the start of the SSM, thereby enabling a smooth entry into force of the SSM Regulation on 3 November 2013. The preparatory work undertaken by the ECB in close cooperation with the national competent authorities allowed achieving significant progress in the operational implementation of the SSM.

For its part, the CSSF allocated substantial resources to these tasks, inter alia through the creation of the SSM department, notably in order to contribute to the different workstreams of the ECB.

At the European level, preparations have been steered by a High-Level Group on Supervision, chaired by the ECB President and comprising representatives from the national competent authorities (NCAs) and central banks (NCBs) of the euro area. A Task Force on Supervision, including senior representatives of NCAs and NCBs and reporting to the High-Level Group, has conducted the technical preparatory work¹.

The Task Force organised the technical work into the following five Workstreams (WS).

- **Initial mapping of the euro area banking system (Workstream 1 - WS1)**

Article 6(4) of the SSM Regulation lays down criteria for the classification of supervised entities. The ECB must draw up a list of significant institutions, as well as a list of institutions considered less significant. It is therefore necessary that it has the required information in order to be able to perform the calculations.

WS1 was set up to gather the necessary data to draw up a preliminary list of significant institutions. The collection of data also included information that allows drawing up a detailed and comprehensive overview of the banking system in the euro area, i.e. the composition of banking groups in the euro area and their cross-border activities.

National competent authorities were called upon to communicate the information required by WS1 by 13 September 2013, by means of the forms drawn up by the group. Based on this information, the ECB drew up the list of banks subject to the comprehensive assessment which will be undertaken before the ECB fully

¹ Source: SSM Quarterly Report, Progress in the operational implementation of the Single Supervisory Mechanism Regulation, 2014/1.

assumes the supervisory tasks under the SSM. The start of this comprehensive assessment was announced on 23 October 2013.

The mandate of WS1 has been adapted since then. It is notably in charge of updating the collected quantitative data, including the figures relating to total assets, and to complete them based on the data of 31 December 2013.

• SSM legal framework (Workstream 2 - WS2)²

The SSM Regulation provides that the ECB must adopt, in consultation with the NCAs and on the basis of a proposal from the Supervisory Board, the framework which will set out the practical arrangements for the implementation of Article 6 of the SSM Regulation. WS2, composed of legal experts, has been established to facilitate these legal preparations, to draw up a draft framework in the form of an ECB regulation (Framework Regulation) which will define the procedures governing the cooperation between the ECB and the NCAs and which will also include provisions directly applicable to banks, as well as to provide legal advice concerning the other preparatory work.

The Framework Regulation will cover the aspects expressly referred to in Article 6(7) of the SSM Regulation, i.e. the methodology for the assessment of the significance of credit institutions, the cooperation procedures for the supervision of significant credit institutions and the cooperation procedures for less significant institutions. Moreover, the Framework Regulation will also deal with aspects that go beyond those expressly mentioned in Article 6 of the SSM Regulation. Such aspects include, for example, issues relating to the procedures for investigatory powers, authorisations, qualifying holdings, withdrawal of authorisations, the regime for administrative penalties, as well as macroprudential supervision and close cooperation. The Framework Regulation will also lay down the main due process rules for the adoption of the ECB's supervisory decisions, e.g. the right to be heard, access to files and language regime.

Before adopting the Framework Regulation, the ECB has conducted a public consultation in February 2014.

• Development of a supervisory model for the SSM (Workstream 3 - WS3)³

One of the main priorities of the preparatory work has been the development of the main features of the operational model for supervision which will guide the functioning of the SSM. This work was carried out by WS3 and is reflected in the SSM Supervisory Manual, which covers the general principles, processes and procedures as well as the methodology for the supervision of significant and less significant institutions, taking into account the principles for the functioning of the SSM. It describes the procedures for cooperation within the SSM and with authorities outside the SSM. While the Supervisory Manual is in the first instance an internal document for SSM staff, it is the intention to prepare a public version.

A significant part of the Supervisory Manual is dedicated to the SSM Supervisory Review and Evaluation Process (SSM SREP), which was developed in order to guide the supervisory review of significant and less significant credit institutions and the requirement of specific additional own funds, disclosure, liquidity, or other measures if needed.

The SSM SREP encompasses:

- a risk assessment system (RAS);
- a methodology for the quantification of capital and liquidity buffers (SREP quantification);
- an approach to integrate the RAS, the SREP quantification and the stress test outcomes.

The SSM SREP will take an integrated approach that relies on an extensive set of information provided by the RAS, the quantifications for capital and liquidity buffers – including the banks' internal capital adequacy assessment process (ICAAP) and internal liquidity adequacy assessment process (ILAAP) – and the top-down stress test outcomes. It will combine them in a meaningful way to quantify the adequate capital and liquidity levels and to devise the Supervisory Examination Plan, given the broader assessment of risks under Pillar 2 of the Basel framework, as implemented in the EU by the Capital Requirements Directive/Capital Requirements Regulation. The integration of these dimensions is achieved at the risk-by-risk level and at the overall level.

² Source: SSM Quarterly Report, Progress in the operational implementation of the Single Supervisory Mechanism Regulation, 2014/1.

³ Source: SSM Quarterly Report, Progress in the operational implementation of the Single Supervisory Mechanism Regulation, 2014/1.

- **Development of a supervisory reporting framework for the SSM (Workstream 4 - WS4)⁴**

The purpose of WS4 was to assess the different reporting systems available in the euro area in order to identify the main practices and to set up a supervisory reporting framework of the SSM. In 2013, several pilot exercises collected prudential information from participating Member States, notably via their existing national reporting framework.

In parallel, WS4 is preparing a system allowing the storage, processing and dissemination of supervisory banking data while ensuring data confidentiality. This data system will comprise data based on the ITS as published by the EBA in July 2013 and other supervisory data which have not been harmonised by the EBA.

- **Initial preparation of the comprehensive assessment of the credit institutions (Workstream 5 - WS5)**

WS5 is in charge of the initial preparation of the comprehensive assessment of credit institutions focussing on Asset Quality Review (AQR). In 2013, several meetings were held at the ECB. The final document drawn up by WS5 specified the key elements of the AQR such as:

- the goals of the AQR;
- capital thresholds;
- “within the scope” and “outside the scope” assets;
- interactions with other supervisory initiatives;
- three-phases approach: (1) portfolio selection, (2) on-site review and (3) processing of results;
- organisation of the project at European and national level;
- involvement of third parties.

This document was adopted by the High-Level Group on Supervision in October 2013.

1.2.5. Comprehensive assessment of banking assets⁵

In accordance with the SSM Regulation, a comprehensive assessment will be performed before the start of the SSM. It involves 128 banking groups in the euro area, including six Luxembourg institutions. The overall assessment started in November 2013 and will end in November 2014.

The assessment comprises three elements:

- **Asset Quality Review (AQR)**

The purpose of the AQR is to enhance the transparency of bank exposures. This review will be broad and inclusive, comprising credit and market exposures, on- and off-balance sheet positions and domestic and non-domestic exposures. All asset classes, including non-performing loans, restructured loans and sovereign exposures, will be covered. The results of the review will be based on a capital threshold of 8% Common Equity Tier 1, using the definition given in the CRR and applicable as from 2014.

- **Stress test performed in cooperation with the EBA**

The stress test will be performed in close cooperation with the EBA. The ECB and the EBA have already communicated further details on the methodology and the corresponding capital adequacy thresholds (8% and 5.5% Common Equity Tier 1 for the baseline scenario and adverse scenario respectively).

⁴ Source: SSM Quarterly Report, Progress in the operational implementation of the Single Supervisory Mechanism Regulation, 2014/1.

⁵ Source: SSM Quarterly Report, Progress in the operational implementation of the Single Supervisory Mechanism Regulation, 2014/1.

• Supervisory risk assessment

Supervisory risk assessment, depending on the availability of relevant data, could support the comprehensive assessment through a control/consistency check for the results of the first two pillars. It aims at addressing the banks' key risks, including liquidity risk, leverage risk and funding risk. It embodies a quantitative and qualitative analysis based on backward- and forward-looking information aimed at assessing a bank's intrinsic risk profile, its position in relation to peers and its vulnerability to a number of exogenous factors.

The results for all the elements of the assessment will be published in November 2014.

1.3. European Banking Authority - EBA

The EBA was established by Regulation (EU) No 1093/2010 of 24 November 2010 and is operational since 1 January 2011. The EBA is chaired by Mr Andrea Enria and the functions of Executive Director are performed by Mr Adam Farkas. Mr Claude Simon, Director, represents the CSSF at the Board of Supervisors.

In 2013, the EBA dealt with a growing work load stemming from the numerous mandates resulting from the sectoral legislation, including, inter alia, Regulation (EU) No 575/2013 of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (CRR), Directive 2013/36/EU of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC (CRD IV), the proposal for a directive establishing a framework for the recovery and resolution of credit institutions and investment firms (BRRD) and the proposal for a directive on deposit guarantee schemes (recast) (DGSD).

In the context of the setting-up of the Banking Union and notably its first pillar, the SSM, the internal governance structures of the EBA (including the decision-making structures) underwent ad hoc changes⁶. At the same time, the list of the EBA's tasks and mandates was extended to include the drawing-up of a European Supervisory Handbook on the supervision of institutions for the EU as a whole. The European Supervisory Handbook should identify best practices as regards supervisory methodologies and processes used by the national authorities.

The CSSF participated, in its capacity of member, in the work of the Board of Supervisors of the EBA, its four permanent committees, the Review Panel as well as an increasing number of permanent and ad hoc sub-working groups. For the year 2013, the following topics should be highlighted in relation to the activities of the EBA working groups.

1.3.1. Standing Committee on Regulation and Policy (SCRePol)

SCRePol contributes to the EBA's work in the areas related to the drawing-up of rules regarding the financial sector (including payment services and electronic money) as well as regarding the recovery and resolution of credit institutions and deposit guarantees.

Thus, in 2013, SCRePol and its subgroups analysed the underlying issues of the mandates given to the EBA through the aforementioned legislative texts, the drawing-up of draft technical standards deriving from these mandates, as well as public consultations on these draft standards. Among the draft technical standards already finalised and which should be issued in the form of European Commission regulations in the coming months, are the following:

- Regulatory Technical Standards on own funds;
- Regulatory Technical Standards on own funds requirements for investment firms based on fixed overheads;
- Regulatory Technical Standards on the calculation of specific and general credit risk adjustments;
- a set of Technical Standards in relation to market risk;

⁶ Regulation (EU) No 1022/2013 of 22 October 2013 amending Regulation (EU) No 1093/2010 establishing a European Supervisory Authority (European Banking Authority) as regards the conferral of specific tasks on the European Central Bank pursuant to Council Regulation (EU) No 1024/2013.

- Regulatory Technical Standards on the retention of net economic interest and other requirements relating to exposures to transferred credit risk;
- Regulatory Technical Standards in the field of large exposures defining the conditions and methodologies used to determine the overall exposure to a client or group of connected clients resulting from an exposure to a transaction with underlying assets;
- Regulatory Technical Standards on the method for the identification of the geographical location of the relevant credit exposures;
- Regulatory Technical Standards on certain aspects of remuneration policy requirements.

As regards implementing technical standards, the following should be noted:

- Implementing Technical Standards with regard to disclosure of own funds requirements for institutions;
- Implementing Technical Standards on additional liquidity monitoring metrics;
- Implementing Technical Standards on the hypothetical capital of a central counterparty;
- Implementing Technical Standards on closely correlated currencies.

The work on many other technical standards started in 2013 and is still underway.

In addition to the work on technical standards, which is a transversal task that occupied all the subgroups to a greater or lesser extent, SCRePol and its subgroups developed a range of reports and studies, either under mandates given to the EBA through European legislative texts or by the European Commission, or on its own initiative.

• Own funds

On the basis of Article 26(3) of the CRR, the Subgroup on own funds drew up a list of all the forms of capital instruments which, in each Member State, are eligible as Common Equity Tier 1 instruments. This list will be published for the first time in 2014. In general, institutions may only consider the types of instruments included in this list for the calculation of Common Equity Tier 1.

• Liquidity

The Subgroup on liquidity drew up two reports that were published on 20 December 2013, namely (1) on the impact assessment for liquidity coverage introduced by the CRR and (2) on appropriate uniform definitions of extremely high quality liquid assets and high quality liquid assets. These two reports provide the European Commission with recommendations for the purpose of its forthcoming delegated act in order to make the Liquidity Coverage Requirement (LCR) operational and binding in 2015.

Overall, the report on the impact assessment for liquidity coverage requirements shows that the introduction of general liquidity requirements within the EU is not likely to have a material detrimental impact on the stability and orderly functioning of financial markets or on the European economy. To a large extent, this can be explained by the fact that EU banks already show liquidity ratios above the average target ratio. In this report, the EBA therefore concludes that the calibration of the LCR, as defined by the Basel Committee, is appropriate across the EU and all Member States.

• Remuneration policies

On 15 July 2013, the Subgroup on governance and remuneration published a report on the results of the data collection exercise regarding high earners, i.e. on the number of persons earning EUR 1 million or more per financial year, according to the data of the financial years 2010 and 2011. The report on the results of the same exercise but based on the financial year 2012 was published on 29 November 2013. These reports allowed analysing the remuneration structures in the EU.

Within the scope of this subgroup, the CSSF also contributed to an exercise consisting in collecting data from the institutions under its supervision allowing the EBA to benchmark remuneration policies and practices at European level.

Finally, the subgroup started revising and updating the guidelines on remuneration policies and practices (initially published by the Committee of European Banking Supervisors) in the light of the requirements laid down in CRD IV.

• Crisis Management

The future directive setting up a framework for the recovery and resolution of credit institutions and investment firms (BRRD) will require the EBA to develop, besides technical standards, also guidelines and reports in the field of recovery and resolution. Overall, over 30 documents need to be drawn up. In addition, there will be a certain number of mandates resulting from the directive on deposit guarantee schemes (DGSD).

In 2013, the Subgroup on crisis management carried on working on the guidelines concerning the range of scenarios to be used in recovery plans. These guidelines will complement two technical standards to be drawn up by the EBA and deal with the content and assessment of recovery plans. The work on the draft guidelines on the interpretation of the different situations in which an institution is failing or likely to fail is also worth mentioning.

1.3.2. Standing Committee on Oversight and Practices (SCOP)

SCOP's mission is to assist, advise and support the EBA (including in the development of technical standards) in the following areas:

- permanent risk assessment in the banking system, including development of instruments in this respect;
- promoting cooperation among authorities, including the strengthening of colleges and common assessments and decisions;
- reinforced convergence of supervisory practices;
- following up on recommendations and warnings of the ESRB.

The main topics dealt with by SCOP in 2013 were the following:

- risks and vulnerabilities of the European banking sector;
- discussion of reports on supervision of foreign currency lending, banks' business models, long-term refinancing plans for banks, functioning of colleges of supervisors and relating processes, common procedures for the prudential supervision and assessment (including liquidity) and recovery plans for banks;
- monitoring work progress on the following technical standards: joint decision on capital requirements, joint decision on liquidity, information exchange on branches, passport notification, operational functioning of colleges and identification of the global systemically important institutions (G-SIIs) and of the other systemically important institutions (O-SIIs);
- discussions on individual banks.

1.3.3. Standing Committee on Accounting, Reporting and Auditing (SCARA)

SCARA's mission is to assist, advise and support the EBA in completing its working programme with respect to financial information in the following areas:

- accounting: monitor, assess and comment on any development in relation to accountancy and more specifically international accounting standards;
- reporting: develop and update prudential reporting schemes and develop draft implementing technical standards;
- audit: monitor, assess and comment on the developments at Community and international level as regards audit;
- transparency: assess the transparency of banks in their information published vis-à-vis financial market participants within the context of Pillar 3 of Basel II.

In respect of the subgroups of SCARA, the following work is worth noting for the year 2013.

• **Accounting**

In the area of accounting, the CSSF contributed to different technical analyses of the EBA regarding the accounting implications of the CRR and CRD IV as well as the comment letters of the EBA on the draft accounting standards of the International Accounting Standards Board (IASB).

• **Reporting**

With respect to prudential reporting, the EBA developed draft implementing technical standards specifying uniform formats, frequencies, dates and harmonised definitions for prudential reporting (ITS on supervisory reporting), as required under the CRR. The draft ITS on supervisory reporting were published on 26 July 2013 by the EBA. In addition to their publication, the EBA submitted the draft ITS to the European Commission for approval.

To enhance harmonisation at European level, the EBA also developed technical reporting solutions such as the data point model (including validation rules) as well as an XBRL taxonomy.

• **Transparency**

The CSSF contributed to the annual exercise of the EBA whereby the transparency of the banks' disclosures to financial market participants within the context of Basel II Pillar 3 is assessed. The exercise was based on a sample of 19 European banks with cross-border activities, including one Luxembourg credit institution.

The annual review ended with the publication of the report "Follow-up review of banks' transparency in their 2012 Pillar 3 reports" on 9 December 2013.

1.3.4. Standing Committee on Consumer Protection and Financial Innovation (SCCONFIN)

The purpose of SCCONFIN is to coordinate and validate the projects of its subgroups, namely the Subgroup on Consumer Protection (SGCP) and the Subgroup on Innovative Products (SGIP). The CSSF is a member of SCCONFIN as well as of both subgroups.

• **Subgroup on Consumer Protection (SGCP)**

The role of the SGCP is to identify the subjects relating to banking activities or products likely to cause damage to consumers and to cooperate in establishing a coordinated system of prudential rules aiming to ensure an effective consumer protection across the Member States.

The SGCP's work resulted in the following publications in 2013:

- an opinion on good practices for responsible mortgage lending, and
- an opinion on good practices for the treatment of borrowers in mortgage payment difficulties.

In December 2013, the SGCP launched a consultation (until March 2014) on the draft Regulatory Technical Standards (RTS) on a minimum monetary amount of the professional indemnity insurance for mortgage credit intermediaries. These RTS were developed in accordance with Article 29(2)(a) of the directive on credit agreements for consumers relating to residential immovable property.

In 2012, the SGCP created the Consumer Trends Workstream to draw up the annual Consumer Trends Report. In 2013, this group reflected on the best means to implement the requirement, laid down in Article 9 of the EBA Regulation, to collect, analyse and report on consumer trends. It has thus developed a new method to analyse consumer trends taking into account not only the reports of Member States, but also various sources of external data, such as market research produced by independent research institutions, data collected from financial ombudsmen, etc..

• Subgroup on innovative products (SGIP)

The purpose of the SGIP is to identify the risks for banks and consumers linked to innovative banking products and to help developing a coordinated system of prudential rules aiming to warn banks across Member States. Based on the work of this group, the EBA published the following in 2013:

- an opinion on good practices for ETF Risk Management;
- a warning of the EBA and ESMA on contracts for difference (CfDs); and
- a warning to consumers on virtual currencies.

Currently, the SGIP includes several workstreams dealing with the following topics:

- structured products: this group sent a questionnaire on structured products to several banks in order to collect data allowing it to analyse to what extent banks tend to use this type of product as a source of funding;
- crowdfunding: this group will conduct a thorough analysis jointly with ESMA, to identify the national and European regulations in this area;
- virtual currencies: this group will analyse whether virtual currencies can and ought to be regulated.

In 2013, the SGIP identified mobile payments and other topics related to payment services as new priority for 2014, notably given the mandates proposed to be assigned to the EBA in the current version of the proposed recast of the Payment Services Directive. In order to better cover the different aspects in this area, it has been decided to set up a Task Force in 2014 which will exclusively deal with the topics related to payment services.

1.3.5. Review Panel

The Review Panel assists the EBA in its task to ensure consistent and harmonised implementation of EU legislation in the Member States. To this end, peer review exercises are conducted on a self-assessment basis for specific topics as regards the compliance with EU legislation and CEBS and EBA guidelines. These peer reviews are explicitly provided for in the EBA Regulation. They cover some or all of the activities of the competent authorities in order to further strengthen consistency in supervisory outcomes. Based on the peer reviews, the EBA may issue guidelines and recommendations and disclose the best practices highlighted by the outcome of the work.

In 2013, the CSSF took part in a peer review on the implementation of guidelines 18, 19 and 20 of the “CEBS Guidelines on Stress Testing” (GL32). The Review Panel analysed the assessments by the competent authorities of the stress test programmes performed by credit institutions. The best practices identified were published in the EBA report of 12 November 2013. According to the report, the competent authorities that took part in the peer review, in general, largely apply the aforementioned guidelines.

Work on a peer review on the implementation of guidelines 7 and 8 of the “CEBS Guidelines on the management of concentration risk under the supervisory review process” (GL31) started in 2013 and will be finalised in the course of 2014.

1.3.6. Working groups reporting directly to the Board of Supervisors

• Network on Single Rulebook Q&As

Developing a single set of rules (the Single Rulebook), comprising above all European regulations that are directly applicable in all Member States, is a major step towards a harmonised approach of banking supervision in Europe and is one of the cornerstones of the Banking Union. The EBA plays a key role in ensuring a uniform and effective application of the regulatory framework within the single market.

Through the Q&A tool available on the EBA's website since 4 July 2013, the institutions, competent authorities as well as any other stakeholder can submit questions relating to CRD IV, the CRR, the related Regulatory and Implementing Technical Standards as well as the EBA's Guidelines. The answers provided by the EBA and published on the EBA's website are the result of an ongoing cooperation between the EBA, the national authorities and the European Commission in order to ensure their consistency with the European regulatory framework.

The CSSF participates actively in the Network on Single Rulebook Q&As at the EBA, which consists of experts of national authorities whose role is to develop a preliminary draft answer to any question submitted to the EBA. Every draft answer is then discussed within the relevant working groups before being approved by the Board of Supervisors and published. Since the introduction of the Q&A tool in July 2013, more than 800 questions have been submitted.

• Impact Study Group (ISG)

The ISG deals with the cyclicalities of the components of the Basel II solvency ratio and analyses the potential pro-cyclical effects of the Basel II regulations on credit markets.

In 2013, the ISG performed empirical studies on the impact of Basel II rules on the components of prudential ratios and on the potential pro-cyclicality of the solvency regulations.

• Task Force for Consistency of Outcomes of Risk-Weighted Assets (TCOR)

The objective of the TCOR's mandate is to identify differences in the computations of Risk-Weighted Assets (RWAs), to understand the sources of such differences and, if need be, to formulate the necessary policy solutions to enhance convergence between banks.

While differences in risk parameters, and thus RWAs, between banks applying internal ratings-based approaches are not a sign of inconsistency per se, a substantial divergence may signal that the methodologies used for estimating risk parameters require, in some cases, further analysis.

A deeper understanding of what drives differences in risk parameters will allow the EBA to explore a number of options to address existing concerns. These include enhancing convergence in the computation of RWAs and improving Pillar 3 disclosures.

Part of the work mentioned above was finalised and published by the EBA in December 2013.

The potential pro-cyclicality of capital requirements under the internal ratings-based approach was the subject of a separate publication. In addition, a report analysing the impact of the prudential rules and regulations on the computation of RWAs, whose purpose is to contribute to harmonising supervisory practices, completed the studies above. This report is based on the analysis of the Task Force on Model Validation, operating under SCRePol, concerning divergences in national supervisory practices regarding the validation of internal ratings systems.

All EBA publications are available on the website www.eba.europa.eu.

1.4. European Systemic Risk Board (ESRB)

The legislation establishing the European Systemic Risk Board entered into force on 16 December 2010. The legislation comprises Regulation (EU) No 1092/2010 of 24 November 2010 on European Union macroprudential oversight of the financial system and establishing a European Systemic Risk Board, and Regulation (EU) No 1096/2010 of 17 November 2010 conferring specific tasks upon the European Central Bank concerning the functioning of the European Systemic Risk Board.

The ESRB is part of the European System of Financial Supervision (ESFS), the purpose of which is to ensure supervision of the financial system within the European Union⁷. Its aim is to identify systemic threats at an early stage, thus enabling proactive measures to be taken and limiting the impact of uncontrolled developments⁸.

⁷ <http://www.esrb.europa.eu/about/background/html/index.fr.html>.

⁸ <http://www.esrb.europa.eu/pub/pdf/ar/2012/esrbar2012fr.pdf?842e063b65b5f93730d3a7ac25f5d668>.

The CSSF is a non-voting member of the ESRB General Board.

The ESRB General Board published three new recommendations: the Recommendation of 20 December 2012 on money market funds (ESRB/2012/1, OJ 2013/C 146/01), the Recommendation of 20 December 2012 on funding of credit institutions (ESRB/2012/2, OJ 2013/C 119/01) and the Recommendation of 4 April 2013 on intermediate objectives and instruments of macroprudential policy (ESRB/2013/1, OJ 2013/C 170/01).

The purpose of draft law No 6653, submitted on 28 February 2014 to the *Chambre des Députés* (Luxembourg Chamber of Deputies) is to implement in Luxembourg the Recommendation of the ESRB of 22 December 2011 on the macroprudential mandate of national authorities (ESRB/2011/3), which requires Member States to set up a national macroprudential authority, as well as the Recommendation of the ESRB of 4 April 2013 on intermediate objectives and instruments of macroprudential policy (ESRB/2013/1).

On 4 November 2013, the ESRB also published a follow-up report in relation to the Recommendation on lending in foreign currencies (ESRB/2011/1). In this respect, reference is made to item 1.1.3., paragraph “Other risks” of Chapter IV “Supervision of banks”.

The publications of the ESRB are available on the website www.esrb.europa.eu.

2. SUPERVISION OF FINANCIAL MARKETS

2.1. European Securities and Markets Authority - ESMA

ESMA was established by Regulation (EU) No 1095/2010 of 24 November 2010 and is operational since 1 January 2011. ESMA is chaired by Mr Steven Maijoor and the functions of Executive Director are performed by Mrs Verena Ross. Mr Jean Guill, Director General, represents the CSSF in the Board of Supervisors. Mr Guill is also a member of ESMA's Management Board.

The Securities and Markets Stakeholder Group, which is composed of 30 stakeholders appointed in a personal capacity, including one Luxembourg representative, aims to facilitate the consultation with stakeholders in areas relevant to ESMA's tasks. The group is also consulted on matters covered by regulatory technical standards and implementing technical standards.

In 2013, the CSSF participated as a member in the work of ESMA and its permanent standing committees with their task forces/working groups (permanent or ad hoc).

All publications of ESMA are available on the website www.esma.europa.eu. For 2013, the following topics should be noted in relation to the activities of ESMA, its working groups and its sub-working groups.

2.1.1. Review Panel

The Review Panel, chaired by Mr Guill, is responsible for assisting ESMA in its task to ensure consistent and harmonised implementation of EU legislation in the Member States. Its role was strengthened by Regulation (EU) No 1095/2010 of 24 November 2010 establishing ESMA.

In 2013, the Review Panel launched a peer review on the supervisory good practices for conduct of business rules under MiFID, and more specifically on the practices with regard to the rules on fair, clear and not misleading information. In this context, ESMA has, for the first time, conducted on-site visits at the premises of certain supervisory authorities, which are assessed based on the answers provided and on the outcome of the on-site visits.

Moreover, a peer review on MiFID conduct of business rules dealing notably with best execution has been initiated.

In order to allow the Review Panel to fulfil its task more efficiently, ESMA developed a new methodology (ESMA 2013/1709) published on 25 November 2013. Under the new methodology, the work of the Review Panel may concern, where applicable, only specific parts of a subject or only certain competent authorities because the relevant national financial markets are more concerned by some European provisions than others.

Moreover, on-site visits to the competent authorities may be organised more systematically, ensuring that all the competent authorities are submitted to such an on-site visit over a certain period. The ESMA Board of Supervisors, upon a proposal by the Review Panel, decides on on-site visits, on the competent authorities to be visited and on the subjects of the visits. ESMA's assessment work is thus no longer limited to the answers provided by the authorities, but also includes the results of on-site visits.

Finally, the Review Panel started a peer review of ESMA guidelines relating to systems and controls in an automated trading environment.

2.1.2. Market Integrity Standing Committee (MISC)

The MISC has taken over most of the work of ESMA-Pol. Under the terms of reference (ESMA/2013/BS/42) of 14 March 2013, the MISC notably contributes to ESMA's work on issues relating to market integrity. It facilitates enhanced cooperation between national competent authorities as regards investigations, coordination of supervision and enforcement actions in the fields of market abuse and short selling. Moreover, the MISC contributes to ESMA's development of a single rulebook in the fields of market abuse, transaction reporting (TAF) under MiFID and short selling. Through the enhancement of supervisory convergence and exchange of supervisory practices, the MISC also promotes the building of a common culture on market integrity supervision and enforcement. In addition, the MISC works to improve ESMA's involvement in non-cooperative jurisdictions in matters related to market abuse investigations.

The development of the 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 continued.

The MISC has also continued ESMA-Pol's work in the fields of short selling and certain aspects of credit default swaps (CDS). In this context, ESMA published, on 30 April 2013, its Opinion on the emergency measure by the Greek HCMC under Section 1 of Chapter V of Regulation (EU) No 236/2012. Moreover, on 3 June 2013, ESMA published, upon a request of the European Commission and following its call for evidence, its Technical Advice evaluating the impact of Regulation (EU) No 236/2012 of 14 March 2012 on short selling and certain aspects of credit default swaps (ESMA/2013-614). On 19 June 2013, ESMA published a compliance table of national competent authorities in relation to ESMA's Guidelines on Exemption for market making activities and primary market operations under Regulation (EU) No 236/2012 of 14 March 2012 (Guidelines compliance table, Ref.: ESMA/2013/765).

Finally, work continued to draw up regulatory technical standards for the proposed Market Abuse Regulation (MAR) and for which ESMA received a formal mandate from the European Commission. With a public consultation in mind, ESMA published, on 14 November 2013, a Discussion Paper on its policy orientations on possible implementing measures under the proposed Market Abuse Regulation (ESMA/2013/1649) and organised an open hearing on 15 January 2014. The CSSF continues its participation in the working group and closely follows the work in question.

2.1.3. Corporate Reporting Standing Committee (CRSC)

As high-quality financial statements are important for the smooth operation of the financial markets, ESMA is involved in the process of drawing up financial information standards and cooperates in this respect, inter alia, with the IASB (International Accounting Standards Board) and EFRAG (European Financial Reporting Advisory Group).

Thus, through its permanent committee CRSC, ESMA developed comment letters on various discussion papers and exposure drafts of the IASB and EFRAG.

Moreover, through its subgroup European Enforcers Coordination Sessions (EECS), the CRSC ensures that the financial information standards are consistently applied in the EU.

In this respect, ESMA took the following initiatives.

- **Consultation Paper “ESMA Guidelines on Enforcement of Financial Information”**

On 19 July 2013, ESMA published a consultation paper on the review of Standards No 1 and 2 on the enforcement of financial information. The CESR standards, as issued by the predecessor of ESMA in 2005, will be transformed into ESMA Guidelines in order to reinforce their status.

- **Public statement “European common enforcement priorities for 2013 financial statements”**

On 11 November 2013, ESMA published the list of priorities to be taken into account for the review of the financial statements of issuers as at 31 December 2013 by the national competent authorities, in order to promote the consistent application of the IFRS. The priorities are as follows: measurement of financial instruments and disclosure of related risks, impairment of non-financial assets, measurement and disclosure of post-employment benefit obligations, fair value measurement and disclosure related to significant accounting policies, judgments and estimates.

- **Report “Comparability of IFRS Financial Statements of Financial Institutions in Europe”**

On 18 November 2013, ESMA published a report on the accounting practices related to financial instruments in 2012 financial statements of a sample of 39 major European financial institutions. The report covers, more specifically, the level of comparability and the quality of the disclosures and includes recommendations to enhance the transparency of financial information.

2.1.4. Corporate Finance Standing Committee (CFSC)

The CFSC is in charge of the work regarding Directive 2003/71/EC (Prospectus Directive), some aspects of Directive 2004/109/EC (Transparency Directive) and corporate governance.

- **Prospectus**

The CFSC’s work on the Prospectus Directive are conducted by a permanent operational working group (OWG) and specific temporary working groups (Task Forces) in which the CSSF participates actively.

In 2013, the CFSC finalised some work started by the Task Forces that had been created the previous year. At the outcome of this work, ESMA published:

- a technical advice on a delegated act concerning disclosure requirements for convertible debt securities on 9 January 2013. The delegated act was adopted by the European Commission and published in the Official Journal of the EU on 8 August 2013 (Delegated Regulation (EU) No 759/2013 of 30 April 2013 amending Regulation (EC) No 809/2004 as regards the disclosure requirements for convertible and exchangeable debt securities);
- an update of the CESR recommendations for mineral companies (ESMA/2013/319) on 20 March 2013;
- the final report on the comparison of liability regimes in Member States in relation to the Prospectus Directive (ESMA/2013/619) on 10 June 2013.

The OWG was entrusted with drawing up draft regulatory technical standards to specify situations where a significant new factor, material mistake or inaccuracy relating to the information included in the prospectus requires a supplement to the prospectus to be published. After a consultation of stakeholders, ESMA published, on 20 December 2013, these draft standards that the European Commission intends to adopt in the form of a delegated act.

Following the work of the OWG and in order to promote common approaches between national supervisory authorities, ESMA published questions and answers relating to:

- definition of profit estimate;
- agreement of the independent accountant/auditor where a profit estimate is included in a prospectus;

- age of the last audited financial information of small and medium-sized companies and of companies with reduced market capitalisation under the proportionate disclosure regime;
- applicability of the summary element requiring the disclosure of the expenses charged by a financial intermediary in a retail cascade;
- inclusion of pro forma financial information in certain defined cases;
- level of disclosure concerning price information of shares when the price is not included in the prospectus;
- applicability of the proportionate disclosure regime of pre-emptive rights to new shares that have been subscribed, after the issue of pre-emptive rights, pursuant to an exempt offer under the Prospectus Directive;
- applicability of the proportionate disclosure regime of pre-emptive rights for the admission to trading on the regulated market of shares that have been subscribed, pursuant to an exempt offer under the Prospectus Directive;
- format of the summary relating to several securities that differ only in some very limited details;
- applicability of the registration document schedule where convertible debt securities are issued.

In addition, ESMA published two opinions in 2013:

- the first one, published on 20 March 2013, lays out the approach according to which ESMA determines whether the information contained in a prospectus drawn up in accordance with the legislation of a third country, may be considered as equivalent to the information required under the Prospectus Directive; and
- the second one, published on 18 December 2013, specifies that drawing up a base prospectus consisting of separate documents is not compliant with the Prospectus regulations.

As in the previous years, ESMA published statistical data in relation to the prospectuses approved and passported by the different Member States for the year 2012 and for the period from January 2013 to June 2013.

Finally, the CFSC created a Task Force for the drawing-up of several draft regulatory technical standards laid down in the Omnibus II Directive. These draft standards should specify:

- the information to be incorporated in a prospectus by reference;
- the prospectus approval processes and the conditions in accordance with which time limits for the prospectus approval decision may be adjusted;
- the provisions relating to the publication of a prospectus;
- the provisions relating to the dissemination of advertisements announcing the intention to offer securities to the public or the admission to trading on a regulated market.

• Transparency

A working group was created at the beginning of 2013 whose objective is to develop draft Regulatory Technical Standards (RTS) relating to the new notification rules for major holdings under the provisions of the Transparency Directive as amended by Directive 2013/50/EU of 22 October 2013 (revised Transparency Directive).

The RTS to be drafted under the revised Transparency Directive concern the following:

- the method of calculation of the 5% threshold for the market maker and trading book exemptions;
- the method of calculating voting rights in case of financial instruments which are referenced to a basket of shares or an index;
- the methods of determination of delta for the purposes of calculation of voting rights relating to financial instruments which provide exclusively for a cash settlement;
- the cases in which exemptions apply to financial instruments held by a natural person or a legal entity fulfilling orders received from clients or responding to a client's requests to trade otherwise than on a proprietary basis, or hedging positions arising out of such dealings.

The working group is also in charge of establishing an indicative list of financial instruments subject to notification requirements under Article 13(1) of the revised Transparency Directive. This list should be periodically updated by ESMA, taking into account technical developments on financial markets. In this context, the working group published a consultation paper on 21 March 2014.

- **Corporate governance**

The Advisory Group on Corporate Governance delivered its final report on proxy advisors.

- **Takeover Bids Network (TBN)**

The CSSF participated in the discussions of this group composed of representatives of the competent authorities on takeover bids in the Member States, whether they are members of ESMA or not. Exchanges notably covered the draft opinion concerning the concept of “acting in concert” developed by a TBN subgroup. This responds to the concern of the European Commission to clarify this concept. Following the TBN’s work, ESMA published, on 12 November 2013, a statement based on the information and common approaches of the TBN members and which contains a “White List” of activities that cooperating shareholders can undertake without triggering the presumption of acting in concert.

2.1.5. Investor Protection and Intermediaries Standing Committee (IPISC)

In 2013, the IPISC developed guidelines on remuneration policies and practices (Ref. ESMA/2013/606). The purpose of these guidelines is to converge the interests of the clients, investment firms and banks in the provision of investment services and the sale of financial instruments, as well as to prevent misselling.

The EBA and ESMA published a joint warning on Contracts for Difference (CFD). Indeed, these contracts are financial instruments bearing considerable risks, notably owing to their particularly high leverage and their high volatility.

The IPISC launched a public consultation on the acquisition and rise of cross-border holdings in investment firms established in the EU, aiming at facilitating this type of transaction. ESMA submitted its final report on this topic with draft regulatory technical standards to the European Commission.

Finally, in January 2014, a warning on risks linked to investing in complex products was published.

2.1.6. Secondary Markets Standing Committee (SMSC)

In order to adopt the new regulations governing markets in financial instruments (being discussed at European level), the SMSC has already started preparations for the drafting of the technical standards and of the technical advice to be provided to the European Commission, thereby completing MiFID and MiFIR once they have been adopted. The SMSC met industry stakeholders several times in order to be able to ask detailed questions during the official consultation which will be launched by ESMA once the Level 1 final texts of MiFID/MiFIR will be published.

2.1.7. Post-Trading Standing Committee (PTSC)

The PTSC notably studied the application of EMIR. As regards central counterparties (CCPs), it drafted guidelines and recommendations for establishing consistent, efficient and effective assessments of interoperability arrangements, as well as guidelines and recommendations regarding written agreements between members of CCP colleges.

A first consultation paper on the clearing obligation was published on 12 July 2013 in order to collect market advice. Given the many questions raised by the market participants concerning the application of certain EMIR provisions, the PTSC worked on a Frequently Asked Questions document, which is regularly updated.

On 18 November 2013, the draft regulatory technical standards on contracts with direct, substantial and foreseeable effect within the EU and non evasion of any EMIR provision was transmitted to the European Commission. Finally, the PTSC participated in the drafting of technical advices relating to the equivalence between third country regulatory regimes and EMIR.

In addition, the PTSC oversaw the initial work of the CSD Task Force in charge of drafting the technical standards for the regulation on improving securities settlement in the EU and on central securities depositories (CSD).

2.1.8. Investment Management Standing Committee (IMSC)

In 2013, the IMSC worked in particular on the following topics:

- ESMA guidelines and regulatory technical standards that aim to clarify certain topics under Directive 2011/61/EU of 8 June 2011 on alternative investment fund managers (AIFMD);
- ESMA guidelines on ETFs and other UCITS issues.

• ESMA guidelines and regulatory technical standards under AIFMD

The AIFMD (Level 1) entered into force on 1 July 2011. On 19 December 2012, the European Commission adopted Delegated Regulation (EU) No 231/2013 (Level 2) supplementing the AIFMD with respect to exemptions, general terms of business, depositories, leverage, transparency and supervision. The AIFMD regime is applicable since 22 July 2013.

In this context, ESMA has been called upon to develop and adopt opinions, recommendations, guidelines and regulatory technical standards that must clarify certain subjects and ensure consistent application of the provisions of the AIFMD. These (Level 3) documents are drafted by the IMSC (and its subgroup, the Operational Working Group on Supervisory Convergence). Once finalised, they will be submitted for final approval to the Board of Supervisors of ESMA.

After its consultation published on 19 December 2012, ESMA submitted to the European Commission, on 2 April and 13 August 2013, (amended) draft regulatory technical standards on types of AIFMs under Article 4(4) of the AIFMD. Under the directive, the managers must follow specific rules according to the type of alternative investment fund they are managing (open-ended/closed-ended) and it is therefore important to determine whether an investment manager is managing AIFs of the open-ended or closed-ended type. Consequently, based on ESMA's draft regulatory technical standard, the European Commission adopted a delegated regulation on 17 December 2013 supplementing the AIFMD with respect to the regulatory technical standards in order to determine if an AIFM is managing open-ended or closed-ended AIFs.

Furthermore, ESMA developed and published the following guidelines concerning the AIFMD regime:

- Guidelines on sound remuneration policies under the AIFMD (Ref. ESMA/2013/232);
- Guidelines on key concepts of the AIFMD (Ref. ESMA/2013/611);
- Guidelines on reporting obligations under Articles 3(3)(d) and 24(1), (2) and (4) of the AIFMD (Ref. ESMA/2013/1339) as well as documents with IT technical guidance concerning reporting under the AIFMD;
- Guidelines on the model MoU concerning consultation, cooperation and the exchange of information related to the supervision of AIFMD entities (Ref. ESMA/2013/998).

Finally, with respect to the latter, the AIFMD requires that cooperation agreements be signed between the national authorities responsible for the regulation of the securities markets in the EU and that of third countries. This cooperation covers third-country AIFMs that manage or market AIFs in the EU, as well as EU AIFMs that manage or market AIFs outside the EU. The agreements include the exchange of information, cross-border on-site visits, mutual assistance in the enforcement of supervisory legislation of all parties to the agreement, as well as the cooperation in the cross-border supervision of depositories and the AIFMs' delegates. European regulators entrusted ESMA with the negotiation on their behalf with every third country based on the guidelines of the ESMA Board of Supervisors. At the end of 2013, ESMA negotiated agreements with 35 non-EU regulators. All the agreements have been signed by the CSSF.

• ESMA Guidelines on ETFs and other UCITS issues

The ESMA guidelines were published on 18 December 2012 (Ref. ESMA/2012/832) and entered into force on 18 February 2013. These guidelines cover ETFs and other UCITS issues as well as the final guidelines regarding repurchase and reverse repurchase agreements.

ESMA provided additional clarifications on the practical aspects of these guidelines through the document “Questions and Answers - ESMA’s Guidelines on ETFs and other UCITS issues”, which is regularly updated. The last update was on 27 November 2013 (Ref. ESMA/2013/1547). Moreover, ESMA launched a consultation on 20 December 2013 on the revision of the provisions on diversification of collateral in ESMA’s guidelines on ETFs and other UCITS issues (Ref. ESMA/2013/1974).

Finally, as regards UCITS, ESMA also published an update of the Questions and Answers relating to the Risk Measurement and Calculation of Global Exposure and Counterparty Risk for UCITS (Ref. ESMA/2013/1950) on 19 December 2013.

2.1.9. Financial Innovation Standing Committee (FISC)

FISC’s mission is to perform the tasks conferred on it by Article 9 of Regulation (EU) No 1095/2010 establishing ESMA in order to assist ESMA in its tasks and responsibilities relating to consumer protection.

As part of these tasks, it collects, analyses and reports on investor trends. In 2013, FISC improved its reporting system in order to monitor consumer trends throughout the European market.

The Consultative Working Group, gathering industry professionals and academics, assists FISC in many areas of its work. The group worked, in particular, on the following: financial innovation framework, index innovation, crowdfunding and collateral transformation.

Within FISC, the Workstream on Structured Retail Products drew up a draft Opinion on Good Practices regarding product governance arrangements and transmitted it to IPISC for review and finalisation if need be.

2.1.10. Credit Rating Agencies Technical Committee (CRA TC)

In 2013, the CRA TC focussed, in particular, on the development of regulatory technical standards for the implementation of the CRA3 Regulation. Thus, on 11 February 2014, the “Consultation Paper on CRA3 Implementation” on draft technical standards was published. The Consultation Paper covered:

- disclosure requirements on structured finance instruments (SFIs);
- the European Rating Platform (ERP); and
- the periodic reporting on fees charged by CRAs.

The draft technical standard on disclosure requirements on structured finance instruments (SFIs) needs to be highlighted more specifically. Indeed, the disclosure of information by the originator, the issuer and/or sponsor if one of these entities is established in the EU aims at (1) providing the elements necessary to investors to allow them to make their own assessment of the credit quality of the SFIs and reduce the over-reliance on external credit ratings, and (2) fostering competition among credit rating agencies and unsolicited credit ratings.

Moreover, the CRA TC drafted Questions and Answers relating to the implementation of the CRA3 Regulation which are updated regularly.

In this context, it must be highlighted that the Joint Committee of the three European supervisory authorities (EBA, ESMA and EIOPA) published, on 6 February 2014, a report on the mechanistic references to credit ratings in the ESAs’ guidelines and recommendations which could trigger sole and mechanistic reliance on such ratings, while the CRA3 Regulation prohibits such references.

2.1.11. Market Data Reporting Working Group (MDR WG)

The MDR WG took over the work of ESMA-Pol relating to the improvement and harmonisation of transaction reporting (TAF) under MiFID. Moreover, the working group continued the discussions started by ESMA-Pol on the drafting of regulatory technical standards within the scope of the proposed regulation on markets in financial instruments (MiFIR) for which ESMA will receive a formal mandate from the European Commission.

The work mainly focuses on:

- the specification of the fields of transaction reports, as well as their content, including, among others, the client identification code and the necessary details of the identity of the clients;
- the designation of algorithms or persons within an investment firm or bank, responsible for the decision making and trade;
- the rules applicable to the transaction reporting by branches;
- the designation and content of information to be kept with respect to transactions (order book data).

The CSSF closely follows this work with a view of complying with the data protection rules.

2.1.12. IT Management and Governance Group (ITMG)

Additional explanations on the work performed in 2013 by ITMG are provided under item 1.3.1. of Chapter XI "Supervision of information systems".

3. COOPERATION WITHIN EUROPEAN BODIES

3.1. European Insurance and Occupational Pensions Authority (EIOPA)

EIOPA, composed of the representatives of the EEA insurance and occupational pensions authorities, assists the European Commission in the preparation of technical measures relating to EU legislation on insurance and occupational pensions. Its mission is to ensure the harmonised and continuous application of the European legislation in the Member States. One main objective of EIOPA is the protection of the policyholders as well as of the members and beneficiaries of occupational pension schemes.

In 2013, the CSSF participated as a member in the work of EIOPA and of the following permanent working groups.

3.1.1. Occupational Pensions Committee (OPC)

In July 2013, EIOPA presented the results of its quantitative impact study in order to sustain its recommendation to introduce a harmonised and risk-based supervision of institutions for occupational retirement provision (IORP), based on the concept of a holistic balance sheet, which will allow recording and measuring on a consistent basis the obligations and resources (including both assets and security mechanisms) of an IORP. In this context, EIOPA came to the conclusion that the results are not such as to allow a conclusive assessment of the feasibility of the concept of a holistic balance sheet for IORPs. In light of these conclusions, EIOPA decided to continue working on different aspects of this issue in order to present, possibly, new opinions to the European Commission.

Pending the publication by the European Commission of its proposed review of the IORP Directive, the OPC continued its work on the development of best practices concerning the content and format of the information to be provided to members of defined contributions schemes, as well as its research on the use of default investment options in defined contributions pension schemes in which the members bear the investment risk. In this context, EIOPA published two reports in February and April 2013. Moreover, the OPC drew up a report on market development in 2013 which is in line with a set of reports allowing monitoring the changes in cross-border activities of IORPs since March 2007.

In 2013, EIOPA also developed its first implementing technical standard on reporting by the national competent authorities of national provisions of prudential nature relevant to the field of occupational pension schemes.

3.1.2. Review Panel

In 2013, the CSSF contributed to the finalisation of the peer review concerning the means and powers of intervention that national supervisory authorities have for the prudential supervision of IORPs. The results were published by EIOPA in July 2013.

During 2013, the CSSF also participated in a new EIOPA peer review in the field of IORPs concerning the conditions of operation and the cross-border activities of IORPs. The outcome of this exercise should be published in the second quarter of 2014.

3.2. Joint Committee of the European supervisory authorities EBA, ESMA and EIOPA

3.2.1. Sub-Committee on Financial Conglomerates (JCFC)

The CSSF takes part in the meetings of the JCFC but it should be noted that to date, no financial conglomerate has been identified for which the CSSF would need to act as coordinator.

The JCFC worked on draft technical standards on the uniform conditions of application of the calculation methods for determining the amount of capital required at the level of the financial conglomerate. The draft standards were published on 29 July 2013. In addition, the JCFC worked on several guidelines, in particular the guidelines for the convergence of supervisory practices relating to the consistency of supervisory coordination arrangements.

3.2.2. Sub-Committee on Consumer Protection and Financial Innovation (SC CPFI)

The work of this sub-committee, the mission of which is the trans-sectoral intervention in areas relating to consumer protection and financial innovation, focuses on the following subgroups:

- PRIPs: The group awaits the adoption of the text of the European regulation before starting identifying products likely to fall under the scope of the text and the relevant marketing techniques.
- Product Oversight and Governance: The joint position of the EBA, ESMA and EIOPA as regards product oversight and governance processes, published in 2013, contains high-level principles for the three European supervisory authorities. The latter must take these principles into consideration when they will be called upon to develop more detailed texts for product oversight and governance.
- Consumer Protection: Publication of guidelines for complaints-handling for the securities and banking sectors.

In 2014, two new subgroups will be created with the aim of dealing with cross-selling and self-placement.

3.2.3. Anti-Money Laundering Committee (AMLC)

As regards AML/CFT, the CSSF contributed in 2013 to the work of the Anti-Money Laundering Committee (cf. item 2.1.2. of Chapter XIV "Fight against money laundering and terrorist financing").

3.3. European Group of Auditors' Oversight Bodies (EAOB)

In 2013, the CSSF took part in the work of the European Group of Auditors' Oversight Bodies (EAOB) and its sub-working group, the EAOB Preparatory.

The subgroup EAOB Preparatory continued analysing the equivalence of public oversight systems for third-country auditors and audit entities of companies established outside the EU and whose securities are

admitted to trading on European regulated markets. This analysis was conducted pursuant to Article 46 of Directive 2006/43/EC which provides, under certain conditions, the option to exempt third-country auditors from public oversight requirements on the basis of reciprocity.

The transitional period was extended by the Commission Implementing Decision of 13 June 2013 (2013/288/EU) until 31 July 2016 for seven countries. This decision allows audit entities of these countries to pursue their activities by means of a simplified registration only until the end of the transitional period.

Following the Commission Implementing Decision of 19 January 2011 as amended by the decision of 13 June 2013, the following third countries meet the definition of equivalent third countries: Australia, Canada, China, Japan, Singapore, South Africa, South Korea, Switzerland, the United States (until 31 July 2016), Abu Dhabi, Brazil, Dubai International Financial Centre, Guernsey, Indonesia, Isle of Man, Jersey, Malaysia, Taiwan and Thailand.

The following third countries meet the definition of transitional third countries: Bermuda, Cayman Islands, Egypt, Mauritius, New Zealand, Russia and Turkey.

The equivalence assessment for the following countries has been interrupted: Argentina, Bahamas, Chile, Kazakhstan, Morocco, Mexico, Pakistan, Ukraine, Hong Kong, India and Israel.

3.4. Accounting Regulatory Committee

The CSSF participates as a member in the work of the Accounting Regulatory Committee of the European Commission.

3.5. Committee on the Prevention of Money Laundering and Terrorist Financing (CPMLTF)

As regards AML/CFT, the CSSF contributed in 2013 to the work of the CPMLTF of the European Commission (cf. item 2.1.3. of Chapter XIV “Fight against money laundering and terrorist financing”).

4. LIST OF EUROPEAN GROUPS IN WHICH THE CSSF PARTICIPATES

At the European level, the CSSF participates as a member in the work of the following committees, working groups and subgroups.

European Systemic Risk Board (ESRB)

- **General Board**
 - **Advisory Technical Committee and the subgroups**
 - Task Force on Stress Testing
 - Expert Group on Money Market Funds
 - Expert Group on Shadow Banking
-

European Banking Authority (EBA)

- **Board of Supervisors**
- **Standing Committee on Regulation and Policy (SCRePol) and the subgroups**
 - Subgroup on Own Funds
 - Subgroup on Credit Risk
 - Subgroup on Crisis Management
 - Subgroup on Governance and Remuneration
 - Subgroup on Operational Risk

Subgroup on Liquidity
 Subgroup on Securitisation and Covered Bonds
 Network on ECAIs (External Credit Assessment Institutions)
 Network on Supervisory Disclosure
 Subgroup on Market Risk
 Task Force on Leverage Ratio
 Task Force on Model Validations
 Task Force on Consistency of Outcomes in Risk-Weighted Assets
 Task Force on Macroprudential Matters
 Project Team on CRR Article 513

- Standing Committee on Oversight and Practices (SCOP) and the subgroups

Subgroup on Vulnerabilities and ongoing assessment of risk
 Subgroup on Microprudential analysis tools and data
 Subgroup on Home-host and colleges
 Subgroup on Risk assessment systems under Pillar 2
 Subgroup on Implementation and supervisory practices

- Standing Committee on Accounting, Reporting and Auditing (SCARA) and the subgroups

Subgroup on Accounting
 Subgroup on Reporting
 Subgroup on Auditing
 Subgroup on Transparency
 Network on COREP
 Network on FINREP

- Standing Committee on Consumer Protection and Financial Innovation (SCONFIN) and the subgroups

Subgroup on Consumer Protection
 Subgroup on Innovative Products

- Standing Committee on IT/IT Sounding Board and the subgroups

IT Security Task Force
 Subgroup on XBRL
 Eurofiling Initiative

- Review Panel and the subgroup

Workstream 2

- Impact Study Group (ISG)

- Expert Group on EU-wide stress-testing

- Network on Single Rulebook Q&A

- Task Force on Virtual Currencies

- Task Force on Stress Test Methodology

- Credit Institutions Register

- Asset Quality Review

- Human Resources Network

- Press officers

European Securities and Markets Authority (ESMA)

- **Board of Supervisors**
- **Board of Directors**
- **Review Panel**
- **Market Integrity Standing Committee (MISC) and the subgroups**
 - Task Force on MoU
 - Working Group on Market Abuse Regulation
- **Corporate Reporting Standing Committee (CRSC) and the subgroups**
 - Project Group on IFRS
 - European Enforcers Coordination Sessions
 - Audit Task Force
 - Task Force EEAP (European Electronic Access Point)
 - Task Force ESEF (European Single Electronic reporting Format)
 - Task Force on ESMA guidelines on enforcement of financial information
- **Corporate Finance Standing Committee (CFSC) and the subgroups**
 - Task Force on Omnibus II related Prospectus issues
 - Task Force on Mineral Companies
 - Task Force on Liability Regimes
 - Task Force on Transparency
 - Task Force on Convertible Debt Securities
 - Task Force on Retail Cascades
 - Takeover Bids Network
 - Advisory Group on Corporate Governance
 - Consultative Working Group
 - Prospectus Operational Working Group and the subgroup
 - Subgroup concerning drafting of an RTS on specific situations that require publication of a supplement
- **Investor Protection and Intermediaries Standing Committee (IPISC) and the subgroup**
 - IPISC Task Force
- **Secondary Markets Standing Committee (SMSC) and the subgroup**
 - Pre-trade Transparency Waiver Review Group
- **Post-Trading Standing Committee (PTSC) and the subgroup**
 - Task Force on CSD
- **Investment Management Standing Committee (IMSC) and the subgroups**
 - Operational Working Group on Supervisory Convergence
 - Task Force on AIFMD Reporting
- **Financial Innovation Standing Committee (FISC)**
- **Committee for Economic and Markets Analysis (CEMA)**
- **IT Management and Governance Group**
- **Credit Rating Agencies Technical Committee**

- **Market Data Reporting Working Group and the subgroups**

- EMIR reporting Subgroup
- Transaction reporting Subgroup
- Instrument reference Subgroup
- Order book Subgroup

- **Human Resources Network**

- **ESMA Legal Network**

- **ESMA Consumer Network**

- **ESMA International Relations Network**

- **Press Officers**

European Insurance and Occupational Pensions Authority (EIOPA)

- **Board of Supervisors**

- **Occupational Pensions Committee (OPC) and the subgroup**

- Workstreams recast IORP Directive

- **Financial Stability Committee**

- **Review Panel**

- **Press Officers**

Joint Committee of the three European Supervisory Authorities EBA, ESMA, EIOPA

- **Sub-Committee on Financial Conglomerates**

- **Anti-Money Laundering Committee (AMLC) and the subgroup**

- Risk Based Supervision Working Group

- **Sub-Committee on Consumer Protection and Financial Innovation**

European Central Bank (ECB)

- **Supervisory Board**

- **Task Force on SSM and the subgroups**

- SSM Workstream 1
- SSM Workstream 2
- SSM Workstream 3
- SSM Workstream 4
- SSM Workstream 5

- **European Forum on the Security of Retail Payments (SecuRe Pay Forum)**

- **ELIS – Task Force on SSM relevant legislation**

- **Target 2 Securities cooperative oversight between CBs and SR**

European System of Central Banks (ESCB)

- **Eurosystem/ESCB Communications Committee (ECCO)**
 - **Financial Stability Committee (FSC) and the subgroup**
FSC Expert Group on legal acts
 - **Information Technology Committee in SSM composition and the subgroup**
Working Group on Statistical Information Management
 - **Human Resources Conference in SSM composition**
 - **Internal Auditors Committee in SSM composition (IAC)**
 - **Legal Committee (LEGCO)**
 - **Statistics Committee (STC)**
 - **Human Resources Conference (HRC)**
-

Council of the EU

- **Investor Compensation Schemes**
 - **MiFID II**
 - **Venture Capital and Social Entrepreneurship Funds**
 - **Market Abuse Regulation (MAR)**
 - **PRIPS**
 - **Directive on banking resolution and recovery**
 - **Ad hoc Working Party on the Banking Supervision Mechanism**
 - **Deposit Guarantee Schemes**
 - **Central Securities Depositories Regulation**
 - **Regulation on European Long Term Investment Funds**
 - **Benchmark Regulation**
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European Commission

- **Capital Requirements Directive Working Group (CRDWG)**
- **Accounting Regulatory Committee (ARC)**
- **Audit Regulatory Committee**
- **European Group of Auditors' Oversight Bodies (EAOB) and the subgroups**
EAOB Preparatory
European Audit Inspection Group (EAIG)
- **Committee on the Prevention of Money Laundering and Terrorist Financing (CPMLTF)**
- **Expert Group on Money Laundering and Terrorist Financing (EGMLTF)**

- Working Party on Financial Services - SEPA
 - Working Party on Financial Services - CSDR
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European Financial Reporting Advisory Group (EFRAG)

- Consultative Forum of Standard Setters
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Others

- Passport Experts Network
 - PSD Passport Liaison Group
 - FIN-NET
-



CSSF's heads of department

Left to right: Sonny BILDORFF-LETSCH, Carlo FELICETTI, Jean-Marc GOY, Françoise KAUTHEN, Marc LIMPACH, Christiane CAMPILL, David HAGEN, Danielle MANDER, Marc WEITZEL, Geneviève PESCATORE, Alain OESTREICHER, Marie-Anne VOLTAIRE, Frank BILDORFF, Jean-François HEIN, Danièle BERNA-OST, Romain STROCK, Irmine GREISCHER, Frédéric TABAK

Absent : Patrick WAGNER

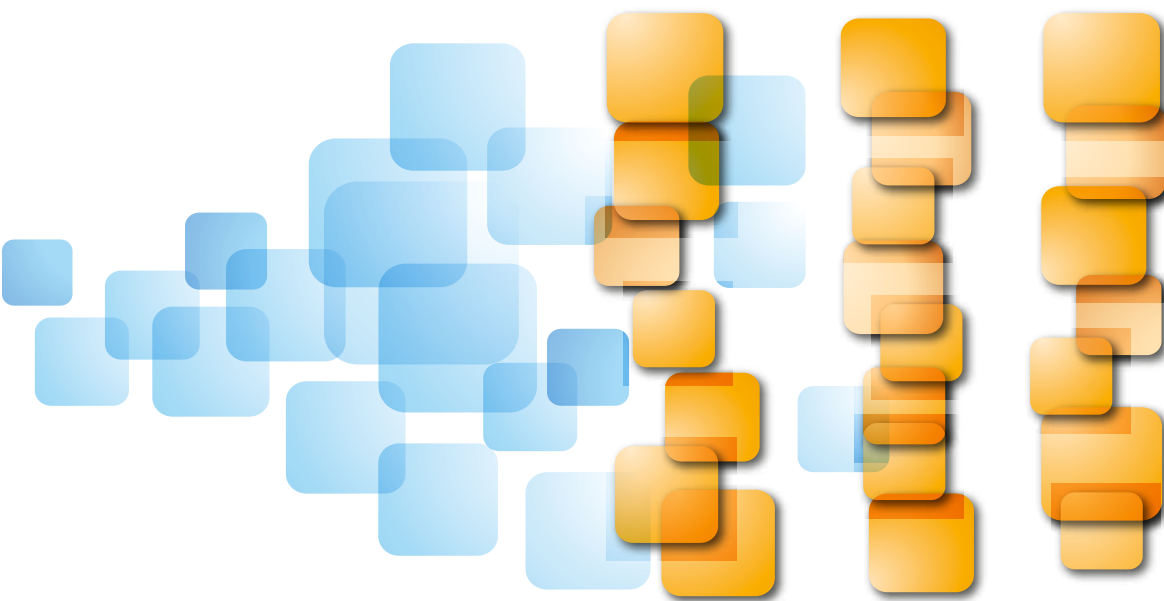


Heads of UCI Department

Left to right: Jean-Paul HEGER, Claude STEINBACH, Sonny BILDORFF-LETSCH, Pascal BERCHEM, Irmine GREISCHER, Alain HOSCHIED

CHAPTER III

THE INTERNATIONAL DIMENSION OF THE CSSF'S MISSION



1. Cooperation within international institutions
2. List of international groups in which the CSSF participates

1. COOPERATION WITHIN INTERNATIONAL INSTITUTIONS

Article 3 of the law of 23 December 1998 establishing a financial sector supervisory commission (“Commission de surveillance du secteur financier”) appoints the CSSF, inter alia, to deal with and take part in the negotiations on the financial sector issues at international level. In accordance therewith, the CSSF participates in the work of the international fora mentioned below.

1.1. Basel Committee on Banking Supervision

The Basel Committee is chaired by Mr Stefan Ingves (Sweden). Mr Claude Simon, Director, represents the CSSF in the Basel Committee.

On 21 January 2013, the Basel Committee adopted a new charter which defines its role, missions and governance. All publications by the Basel Committee and information on its organisational structure are available on the website www.bis.org.

The CSSF participates in the work of the Basel Committee, of the main sub-committees (Accounting Experts Group, Supervision and Implementation Group and Policy Development Group) and of some sub-working groups which are particularly relevant for the prudential supervision in Luxembourg, notably the Working Group on Liquidity, Working Group on Operational Risk, Large Exposures Working Group and Working Group on Supervisory Colleges.

In 2013, the issues dealt with by the Basel Committee were largely dominated by the reform agenda adopted by the G20 as a response to the financial crisis. The works mentioned hereafter are of particular interest for the Luxembourg banking sector.

1.1.1. Large exposures

The rules published by the Basel Committee on sound management of concentration risk towards a counterparty or a group of connected counterparties used to be published as mere guidelines which allowed a wide measure of discretion in their application. The financial crisis, which revealed the existence of excessive risk concentrations towards connected counterparties, showed that a stricter regulatory response was needed.

The work the Basel Committee initiated on these “large exposures” led to the publication of a consultation paper (March 2013) which proposes an international regulatory framework on large exposures. The key topic of the “Supervisory framework for measuring and controlling large exposures” is the limitation of any large exposure to a certain percentage of a bank’s own funds. This type of regulation already exists in the EU. Indeed, Article 395 of Regulation (EU) No 575/2013 does not, as a general rule, allow banks to incur an exposure to a client (or group of connected clients) the value of which exceeds 25% of their eligible capital.

The consultation period for the above-mentioned document was closed at the end of June 2013 and the Basel Committee is expected to publish its final regulatory framework in the first half of 2014. It should be noted that intra-group exposures, very common within Luxembourg banks, will not be covered by this regulation. The Basel Committee intends to consider large intra-group exposures in its forthcoming works.

1.1.2. Liquidity

In December 2010, as a response to the financial crisis which revealed that the regulatory liquidity framework was insufficient, the Basel Committee suggested the introduction of two minimum liquidity standards at an international level: the Liquidity Coverage Ratio (LCR) imposing banks to hold a certain stock of liquid assets allowing them to face significant liquidity shortfalls on the short-term and the Net Stable Funding Ratio (NSFR) which requires banks to refinance at least a proportion of their long term assets through stable resources.

The work on the LCR ended on 7 January 2013 with the publication of the final text which governs the LCR. In accordance with paragraph 10 of the document “Basel III: The Liquidity Coverage Ratio and liquidity risk monitoring tools”, the LCR will be introduced as a (minimum) requirement for liquidity on 1 January 2015.

However, the implementation of this requirement will be based on a graduated approach. The LCR, whose minimum threshold will be set at 60% as from 1 January 2015, will rise in equal annual steps of 10% to reach 100% on 1 January 2019. At EU level, Article 460 of Regulation (EU) No 575/2013 provides for the introduction of the LCR by means of a delegated act. This act should be largely based on the Basel Committee's works including, nevertheless, a requirement for European banks to reach the threshold of 100% as from 1 January 2018 (instead of 1 January 2019).

It should also be noted that the second part of the document "Basel III: The Liquidity Coverage Ratio and liquidity risk monitoring tools" includes a certain number of monitoring tools for liquidity risk that supervisory authorities are required to implement in order to complete the partial liquidity measures of the LCR and NSFR standards.

Having completed the LCR, the Basel Committee doubled its efforts to conclude its proposal on stable funding. The works on NSFR have led to the publication of a consultative document in January 2014. The text titled "Basel III: The Net Stable Funding Ratio" follows the key guidelines of the proposal made in December 2010. However, it can be noted that the liabilities that are considered as stable have, generally speaking, received a more favourable treatment as compared to the 2010 proposal. This is especially the case for operational deposits which are of a particular importance for the Luxembourg financial centre and which are henceforth recognised at 50%.

1.1.3. Basel III Regulatory Consistency Assessment Programme

The work on the Basel III Regulatory Consistency Assessment Programme (RCAP), initiated in 2012, progressed at a sustained pace in 2013.

First, the reports on the consistency of national regulations with Basel III have been published for four member states of the Basel Committee, i.e. Brazil, China, Switzerland and Singapore. These reports aim at assessing and documenting to which extent domestic rules which result from the transposition of the Basel III agreement comply with this agreement; the objective is to ensure, through common rules, a fair competition between banking groups that act on a cross-border basis. The public document titled "Basel III Regulatory Consistency Assessment Programme (RCAP)" (October 2013) details the approach implemented by the Basel Committee to this effect.

Then, the Basel Committee finalised three analyses¹ on the differences between banks as regards regulatory capital requirements for market risk and credit risk determined by the so-called advanced approaches. Whereas a major part of these differences appear to be linked to the risk profile of each bank, it turns out that major discrepancies exist at the level of the risk quantification practices. The study carried out on the banking portfolio (excluding trading portfolio) estimates that these diverging practices may be the cause of substantial variations among banks' solvency ratios, ranging from 150 to 200 basis points. As these differences do not directly reflect the underlying risk, they raise questions on their legitimacy in terms of financial stability and level playing field. Based on these preliminary results, the Basel Committee decided to investigate further in order to identify undesirable practices from a prudential point of view. As a result of these analyses, it is expected that the Basel Committee will take safekeeping measures aiming at guaranteeing that the use of advanced approaches remains compatible with the objectives of financial stability and level playing field.

These developments are of particular importance for Luxembourg banks that use advanced approaches or that interact with third-country banks. For the banks using advanced approaches, the above studies allow situating their own advanced approaches. For the banks interacting with third-country banks, the assessment of consistency of the country of origin of their counterparty provides key information allowing a better apprehension of the financial situation of these counterparties.

1.1.4. Other publications of general interest

The recent efforts by the Basel Committee to increase regulatory risk sensitivity implies that certain aspects of the regulatory framework have become more complex. In this context, the Basel Committee raised the question to know whether its regulatory framework still ensures an adequate balance between the complementary

¹ These analyses are published under the generic title "Regulatory Consistency Assessment Programme (RCAP) - Analysis of risk-weighted assets".

objectives of risk sensitivity, simplicity and comparability. The discussion paper “The regulatory framework: balancing risk sensitivity, simplicity and comparability” which was published by the Basel Committee in July 2013 invites stakeholders worldwide to participate in this far-reaching debate on the future direction of international banking regulation.

1.1.5. AML/CFT Expert Group (AMLEG)

In 2013, the CSSF participated in the work of this group of experts in AML/CFT of the Basel Committee (please refer to item 2.1.4. of Chapter XIV “Fight against money laundering and terrorist financing”).

1.2. International Organisation of Securities Commissions (IOSCO)

1.2.1. 38th IOSCO Annual Conference

From 15 to 19 September 2013, the CSSF organised the 38th IOSCO Annual Conference in Luxembourg which attracted some 700 representatives of the regulatory authorities of the securities and futures markets, as well as other members of the international financial community from 113 jurisdictions worldwide. Since the creation of IOSCO in 1983, the annual conference was held for the first time in Luxembourg. The organisation and the conference itself were both a great success. The public events included the speeches of the Luxembourg Prime Minister and Finance Minister, as well as presentations and discussions in panels with speakers from Europe, the Americas, Asia, Africa and Australia.



IOSCO confirmed its position as global key reference as concerns securities regulation. The Board Chair of IOSCO reminded that IOSCO's role has been recognised by the G20 during the summit held in Saint Petersburg.

During this annual conference, the importance of the IOSCO Multilateral Memorandum of Understanding (IOSCO MMoU) has been stressed again and IOSCO pursued its efforts to reach its stated objective of all ordinary members signing the Memorandum. After the 38th annual conference, the number of signatories amounted to 99 (Appendix A). During the annual conference, IOSCO adopted Graduated Additional Measures with the aim to encourage the 26 members who still had not signed the Memorandum to sign the MMoU until 30 September 2014 at the latest. After that date, the voting rights of the non-signatory members will be

suspended. The list of the non-signatory members to the MMoU is available on the IOSCO website. Mr Gérard Rameix, Chairman of the Autorité des marchés financiers (France) was elected Chair of the MMoU Monitoring Group. He succeeds Ms Jackie Mesa of the US Commodities Futures Trading Commission.

The “Self Regulatory Organizations Consultative Committee” has been renamed “Affiliate Members Consultative Committee” and its role increased.

IOSCO and the IFRS Foundation agreed on a set of protocols under which the two organisations will deepen their cooperation in developing and implementing the IFRS principles (International Financial Reporting Standards) and join their efforts to pursue their shared commitment to the highest standards of financial reporting and to promote adherence to these IFRS.

The Institut Nacional Andorrà de Finances (Andorra) has been admitted as new ordinary member of IOSCO.

The 39th IOSCO Annual Conference will be held in Rio de Janeiro from 28 September to 2 October 2014.

1.2.2. Committee 1 on Issuer Accounting, Audit and Disclosure

The Accounting subcommittee (ASC) closely follows the activities of the IASB (International Accounting Standards Board), especially by analysing the exposure drafts and discussion papers issued by the IASB and submitting comment letters relating thereto.

The Audit subcommittee (AuSC) follows the development of the auditing and independence standards issued by the IAASB (International Auditing and Assurance Standards Board) and IESBA (International Ethics Standards Board for Accountants) of IFAC (International Federation of Accountants).

1.2.3. Committee 5 on Investment Management

The Committee 5, chaired by the Autorité des marchés financiers - AMF France, met three times in 2013, in Madrid in February, in London in June and in Hong Kong in November. It focused on the following topics:

- Principles for the Valuation of Collective Investment Schemes (CIS);
- Liquidity Risk Management of CIS;
- Methodology for Assessing Systemically Important CIS other than Hedge Funds;
- Principles for the Regulation of Exchange Traded Funds (ETFs);
- Developments concerning Money Market Funds;
- Reducing Reliance on Credit Rating Agencies;
- Safekeeping of Assets of CIS;
- Fees and Expenses for CIS;
- Termination of CIS.

Within the Committee 5, the CSSF notably participates in the working groups Good Practices of Custodians, Framework for the Termination of CIS and Fees and Expenses for CIS. Moreover, the CSSF is a member of the common working group composed of the Committee 5 and the IOSCO Task Force on Unregulated Financial Entities (TFUFE) on “Systematically important financial institutions” (SIFIs).

In 2013, IOSCO published the following documents which had been prepared by the Committee 5:

- final report on the “Principles of Liquidity Risk Management for Collective Investment Schemes” (4 March 2013);
- final report on the “Principles for the Valuation of Collective Investment Schemes” (3 May 2013);
- final report on the “Principles for the Regulation of Exchange Traded Funds” (24 June 2013).

IOSCO published on 21 October 2013 a second report on hedge funds (“Report on the Second IOSCO Hedge Fund Survey”) which collects data (with the participation of the CSSF for the Luxembourg data collection) on hedge fund managers as at 30 September 2012.

Finally, on 8 January 2014, IOSCO and the Financial Stability Board (FSB) published a consultation paper titled “Proposed Assessment Methodologies for Identifying Non-Bank Non-Insurer Global Systemically Important Financial Institutions” whose consultation period will end on 7 April 2014.

1.2.4. Committee 8 on Retail Investors

The CSSF also participates in the works of the Committee 8 (cf. item 1.1.2. of Chapter XV “Financial consumer protection”).

1.2.5. Assessment Committee

The CSSF is a member of the IOSCO Assessment Committee and of the sub-committee Implementation Task Force Committee which met three times in 2013. Their objective is to foster a full, efficient and consistent implementation of the IOSCO Principles and standards among its members. In 2013, the CSSF notably participated in the works of the committee which led to the publication of a report on the thematic review on the implementation of IOSCO Principle 6 (monitoring, mitigating and managing systemic risk) and Principle 7 (reviewing the perimeter of regulation) which had been included in the IOSCO Principles and standards in 2010 as part of its response to the financial crisis.

1.3. Enlarged Contact Group “Undertakings for Collective Investment”

The CSSF attended the annual meeting of the Enlarged Contact Group “Undertakings for Collective Investment” which was held from 2 to 4 October 2013 in Zurich. The following topics were discussed: issues relating to supervision, conflicts of interests/code of conduct, legal topics, financial issues, reporting and disclosure, management and administration of investment funds and UCITS and other investment funds.

1.4. Others

In 2013, the CSSF participated in the work of the Institut francophone de la régulation financière (IFREFI), the Groupe des Superviseurs Bancaires Francophones (GSBF, Group of francophone banking supervisors), the FSB Regional Consultative Group² for Europe, the IT Supervisors Group and the International Forum of Independent Audit Regulators (IFIAR).

Furthermore, within the context of the fight against money laundering and terrorist financing, the CSSF contributed to the work of the Financial Action Task Force (FATF) of the OECD and its subgroups and to those of the Wolfsberg Group (cf. item 2.1. of Chapter XIV “Fight against money laundering and terrorist financing”).

The CSSF also contributes to the work of several international groups whose objective is the protection of the financial consumer and the development of financial education (cf. item 1.1. of Chapter XV “Financial consumer protection”).

² Cf. item 1.3.2. of Chapter XI “Supervision of information systems”.

2. LIST OF INTERNATIONAL GROUPS IN WHICH THE CSSF PARTICIPATES

At international level, the CSSF participates as a member in the works of the following committees, working groups and subgroups.

Basel Committee on Banking Supervision

- **Policy Development Group (PDG) and the subgroups**
 - Leverage Ratio Working Group
 - Risk Measurement Working Group
 - Working Group on Large Exposures
 - Working Group on Liquidity
 - Definition of Capital Subgroup
 - Capital Monitoring Working Group
 - Corporate Governance Group
 - Cross-Border Bank Resolution Group
 - QIS Working Group
 - Task Force on Interest Rate Risk in the Banking Book (TFIR)
 - Task Force on Standardized Approaches (TFSA)
- **Supervision and Implementation Group (SIG) and the subgroups**
 - Working Group on Operational Risk
 - Working Group on Pillar 2
 - Working Group on Supervisory Colleges
- **Accounting Experts Group (AEG) and the subgroup**
 - Audit Subgroup
- **AML/CFT Expert Group (AMLEG)**

Financial Stability Board

- **European Regional Consultative Group**

International Organisation of Securities Commissions (IOSCO)

- **IOSCO Annual Conference**
 - **IOSCO European Regional Conference**
 - **Committee 1 on Issuer Accounting, Audit and Disclosure and the subgroups**
 - Accounting Subcommittee
 - Auditing Subcommittee
 - IOSCO IFRS Database
 - **Committee 5 on Investment Management**
 - **Committee 8 on Retail Investors**
 - **Assessment Committee and the subgroup**
 - Implementation Task Force Subcommittee
-

Financial Action Task Force (FATF)

- Plenary Meeting
- International Cooperation Review Group
- Policy Development Group
- Evaluation and Compliance Group
- Risks, Trends and Methods
- Global Network Coordination Group

Organisation for Economic Cooperation and Development (OECD)

- Working Group on Private Pensions
- Task Force on Financial Consumer Protection and the subgroups
 - Subgroup on Principle 6 : Responsible Business Conduct of Financial Service Providers and Authorised Agents
 - Subgroup on Principle 9 : Complaints Handling and Redress
- International Network on Financial Education (INFE)

Others

- Enlarged Contact Group “Supervision of Undertakings for Collective Investment”
 - IT Supervisors Group
 - International Forum of Independent Audit Regulators (IFIAR)
 - Institut francophone de la régulation financière (IFREFI)
 - Groupe des Superviseurs Bancaires Francophones (GSBF - Group of francophone banking supervisors)
 - The Wolfsberg Group
 - Financial Consumer Protection Network (FinCoNet) and the subgroup
 - Working Group 2 – Strengthen supervisory tools by identifying gaps and weaknesses
 - Child and Youth Finance International
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CHAPTER IV

SUPERVISION OF THE BANKING SECTOR



1. Developments in the banking sector in 2013
2. Prudential supervisory practice

1. DEVELOPMENTS IN THE BANKING SECTOR IN 2013

1.1. Major events in 2013

1.1.1. Comprehensive Assessment

In accordance with the regulation implementing the Single Supervisory Mechanism (SSM Regulation), the European Central Bank (ECB) shall undertake a comprehensive assessment of the significant banks before the transfer of the supervision responsibility within the SSM.

This assessment of the 128 banking groups of the euro area, including six Luxembourg institutions is carried out in collaboration with the national competent authorities (NCAs) of the Member States participating in the SSM, i.e. the CSSF in Luxembourg.

The goals of the comprehensive assessment are threefold: (1) to foster transparency, that is, enhancing the quality of information available concerning the condition of banks; (2) where needed, to repair balance sheets, by identifying and implementing the necessary corrective actions; (3) to foster confidence by guaranteeing the stakeholders that the banks are basically sound and credible.

The comprehensive assessment includes three elements:

- A supervisory risk assessment: this assessment depends on the availability of relevant data. It could support the comprehensive assessment through a consistency control/check for the results of the Asset Quality Review (AQR) and the stress test.
- A banks' AQR in order to enhance the transparency of bank exposures: this review concerns in particular the appropriateness of the valuation of the assets and guarantees as well as provisions. In 2013, the CSSF took part in a working group of the ECB which initially prepared the methodology and organisation of this review at European and national level. This broad and inclusive review comprises credit and market risk exposures, on- and off-balance sheet positions and domestic and non-domestic risk exposures. The AQR is clearly the element that implies the greatest workload for the NCAs. For reasons of objectivity and in order to ensure an independent judgment, the ECB expressly asked the NCAs to seek assistance from external auditors. The CSSF's internal organisation includes a National Steering Committee, six Bank Teams, a Quality Assurance team and a Project Management Organisation team. The selection procedure of the risky portfolios, which was launched in December 2013, and the call for tenders for external auditors were brought to a successful close in February 2014.
- A stress test aiming to analyse the resilience of banks' balance sheets under stress scenarios: this test will be coordinated by the ECB and the EBA and will start in April 2014.

The ECB intends to publish the results of this comprehensive assessment before assuming its new prudential supervisory tasks in November 2014.

1.1.2. Single rulebook for banks

The EU introduced the Basel III standards at European level by way of a single rulebook for the banking sector including Directive 2013/36/EU (CRD IV) and Regulation (EU) No 575/2013 (CRR). It shall apply as from 1 January 2014.

The directive, currently being transposed into national law, covers some areas regarding capital adequacy and also includes new elements like the strengthening of governance, provisions relating to sanctions and capital buffers.

The European regulation covers, among others, the definition of own funds and regulatory capital requirements, the ratios applicable to liquidity risk as well as the leverage ratio. This regulation, the purpose of which is maximum harmonisation, will be directly applicable to banks in the EU Member States; no national transposition will be needed so that discrepancies in national transpositions will be limited. Consequently, it replaces some of the provisions of the CSSF circulars, including Circular CSSF 06/273.

The European regulation also includes the obligation for the EBA to develop binding technical standards aiming to define the manner in which some aspects (e.g. in the area of prudential reporting) will be implemented. Upon approval of these implementing technical standards by the European Commission, they will be directly applicable to banks and do not need to be transposed by the EU Member States. The EBA issued 35 binding technical standards in 2013 and intends to issue 67 in 2014.

In July 2013, the EBA launched an online application called Single Rulebook Q&A, whereby the institutions, the supervisors and any other person concerned may submit questions as regards the Single Rulebook as well as the binding technical standards and the guidelines relating thereto. The purpose is to create a common legal framework as well as a common culture and uniform supervisory practices throughout the EU.

1.1.3. Risks in the Luxembourg banking sector

The notion of risk refers, in this case, to banking commitments or activities the nature of which may jeopardise the financial stability of some individual credit institutions or of the entire banking sector in case these commitments or activities develop in an extremely adverse manner. Whereas such an adversity cannot be excluded, its imminence is generally difficult to predict. Hence, the CSSF does not venture to make predictions but ensures that banks duly take inherent risks of their commitments into account.

There are no risk-free banking activities. The analysis of the risk structure in the Luxembourg banking sector reveals mainly three risk concentrations which require a particular management and monitoring by the relevant Luxembourg credit institutions, namely: sovereign risks, risks linked to the financing of residential real estate in Luxembourg and intra-group risks. The nature and the level of these “systemic” risks vary greatly among banks and according to the activities performed.

• Sovereign risks

Sovereign risks are credit exposures to the public sector which include central, regional and local administrations.

For a majority of Luxembourg banks, part of the excess structural liquidity gathered within the context of wealth management activities is reinvested in sovereign debt. In theory, a sovereign State is able to meet its financial obligations by giving effect to its taxing rights to this end. The sovereign exposure thus appears as less risky and better suited for the conservative risk profile of Luxembourg banks. However, in the event of an opposite trend, like the sovereign debt crisis in Europe, an increased focus on sovereign debtors may jeopardise the financial stability.

Overall, the sovereign risks incurred by the banks of the Luxembourg financial centre do not challenge the financial stability of the sector as a whole. However, for a limited number of banks taken individually, these exposures represent a more significant risk concentration. This is the case for banks issuing public-sector covered bonds whose business model corresponds precisely to the public sector financing.

At the end of 2013, the aggregated exposure of Luxembourg banks to the public sector amounted to EUR 57 billion, which represents an increase of 3% over one year. Like last year, the allotment of this amount between the different sovereign debtors is carried out by increasingly favouring the public sector of big European countries less affected by the sovereign debt crisis. Consequently, the exposure of the Luxembourg banking sector towards higher-risk countries decreased. For the group of countries GIIPSC (Greece, Ireland, Italy, Portugal, Spain and Cyprus), the exposure decreased from EUR 18 billion in December 2010 to EUR 13 billion at the end of 2013.

As at 31 December 2013, the main sovereign debtors of Luxembourg banks were as follows.

Exposures of Luxembourg banks to the public sector

Public sector	Exposures (in million EUR)
France	9,060
Italy	8,879
Germany	6,882
United States	4,055
Luxembourg	3,774
Belgium	3,221
United Kingdom	3,099
Spain	2,939
Canada	1,866
Netherlands	1,097

As a result of the new liquidity regulatory standards, as provided for in the Basel III framework, the sovereign risk exposure should increase. Indeed, these standards provide that banks hold liquidity buffers made up of “high-quality liquidity assets” which include mainly low-credit risk sovereign and supranational debt securities. The pride of place given to sovereign exposures in banking regulations is therefore strengthened.

As regards solvency regulatory standards, Article 114(4) of Regulation (EU) No 575/2013 maintains a 0%-preferential risk weight assigned to exposures to central administrations of Member States denominated and funded in the domestic currency of that central administration.

While regulations provide for specific treatments to sovereign risks, the CSSF would like to remind banks of their own risk assessment obligations. In this respect, banks shall assess their risks, the link to the bank’s business model and the bank’s ability to manage these risks and to face risk materialisation in an adverse situation. This ability is reflected in particular in the liquidity and capital buffers which banks hold in order to face the incurred risks and which shall adequately reflect the concentration risk, for example the fact that the sovereign exposure represents a significant portion of the equity capital.

- **Risks linked to residential real estate in Luxembourg**

The local mortgage market is served only by a limited number of the financial centre’s banks. The activity on this market remains sustained as shown by the 9%-increase over a year of the mortgage loans that these banks granted to their retail customers. Since the end of 2008, the volume of these loans has increased by about 65%.

In the past, granting mortgage loans generally presupposed an own contribution by the future buyer amounting to about 20% of the value of the real estate. Over the last ten years, this practice has been replaced by more developed funding models which provide for, in extreme cases, the full funding without any personal contribution. This practice raises for the bank a greater risk insofar as the reduction of the own contribution of the acquirer coincides with the decrease in the net value of the guarantee for the bank. Where this safety cushion disappears and in the event of defaults, the bank is protected against decreases in value of the mortgaged property only up to the capital requirements determined in accordance with Regulation (EU) No 575/2013. For Luxembourg banks, these capital requirements, which are intended to cover losses in the event of severe downturn in the real estate market, represent, on average, only between 1% and 3% of the total amount of their mortgage loans.

Circular CSSF 12/552 that introduces new real estate financing rules is the first step toward a reinforcement of mortgage granting policies in Luxembourg. The CSSF will assess to what extent these new rules, which entered into force on 1 July 2013, must be strengthened in the future. While awaiting the results from these assessments, the CSSF took advantage of the entry into force of Regulation (EU) No 575/2013 and of Directive 2013/36/EU to activate the capital conservation buffer as from 1 January 2014. In accordance with Article 6 of CSSF Regulation N° 14-01, Luxembourg banks, including those operating on the residential mortgage market, must hold a core Tier 1 capital buffer equal to 2.5% of the amount of their total risk

exposure. This measure replaces and reinforces a previous decision of the CSSF, which, since 2009, imposed on banks that are highly exposed to the local real estate sector compliance with a total capital ratio of 10% corresponding to an additional capital buffer of 2% as compared to the regulatory minimum.

• Risks linked to intra-group exposures

The Luxembourg banking centre includes many subsidiaries of large international banking groups. Generally, these subsidiaries have no competence in investment banking in Luxembourg and the deposits they receive in the context of the wealth management services they provide are lent to the group. In this context, the CSSF normally accepts, in accordance with the intra-group exemption provided for in the European regulations governing large exposures, that a portion of these deposits be invested by a Luxembourg banking subsidiary with its parent company, up to an amount exceeding the 25% limit of own funds usually applicable under the regulations on large exposures. This position is justified by inside information that the CSSF has on the risks associated with these investments, in particular through the colleges of supervisors of the banking groups in question, as compared to other types of investment which offer less visibility and carry potentially higher risks.

The intra-group exemption is subject to requirements of sound and prudent management of the intra-group exposures, particularly in relation to the absence of risky business of maturity transformation and high credit risk-taking.

This approach is not challenged due to the entry into force of Regulation (EU) No 575/2013. Article 20 of CSSF Regulation N° 14-01 on the implementation of certain discretions of Regulation (EU) No 575/2013 provides for the process and conditions relating to the intra-group exemption. Paragraph (2) of this article thus provides that intra-group exposures are exempted provided that:

- a) the counterparty is itself a CRR institution¹, a third-country credit institution or a third-country investment firm;
- b) the financial situation in terms of risks and solvency and the liquidity situation of the counterparties in question does not present disproportionate credit risks for the CRR institution;
- c) financing the exposures in question does not present significant liquidity risks in terms of currency and maturity mismatches for the CRR institution; and
- d) the exposures in question would have no disproportionate negative impact on the CRR institution if a resolution procedure were to be applied to all or part of the group to which the CRR institution belongs.

It should also be noted that pursuant to Regulation (EU) No 575/2013, all intra-group exposures remain subject to regulatory capital requirements.

Besides the above-mentioned risks, the following risks are also worth mentioning.

• Economic risks

When economic conditions worsen, the number of borrowers experiencing difficulties in fulfilling their commitments tends to grow. Sometimes banks can be accommodating and allow such debtors to adjust their repayment plans. This practice may be beneficial for both the borrower and the bank if it allows continuing the underlying transaction and making mutual inherent profit. However, this practice is not acceptable when it leads to considering non-performing loans as performing, to impeding the assessment of the assets' quality and to avoiding making the necessary provisions or depreciations.

With the entry into force of Circular CSSF 12/552 on 1 July 2013², banks are required to have an IT management system that allows them to monitor the impact of their accommodative practices on the quality of their assets, to regularly assess the quality of these assets based on the arrangements made and to appraise the need or opportunity to make provisions or depreciations. These elements will be subject to harmonised legal definitions and reporting based on implementing technical standards that the EBA has developed in accordance with Article 99(4) of Regulation (EU) No 575/2013³. Once adopted by the European Commission,

¹ CRR institutions are the institutions referred to in point (3) of Article 4(1) of Regulation (EU) No 575/2013 as well as Luxembourg branches of these institutions having their registered office in a third country.

² Cf. in particular points 224 to 227 of Circular CSSF 12/552.

³ Cf. "EBA Final draft Implementing Technical Standards on Supervisory reporting on forbearance and non-performing exposures under Article 99(4) of Regulation (EU) No 575/2013 (EBA/ITS/2013/03)".

the standards in question will be part of the reporting on financial information FINREP which will be applicable as from 1 July 2014. However, the part relating to the asset quality should enter into force only in September 2014 with a first remittance planned for 31 December 2014.

Given the EU's economic situation, the EBA published recommendation EBA/REC/2013/04 in October 2013, which requires supervisory authorities to undertake AQRs of their banks. These reviews aim precisely to identify risky accommodative practices and to take, where appropriate, the required prudential measures to restore full public confidence in the European banking sector weakened by the sovereign debt crisis. Within the context of the implementation of the Single Supervisory Mechanism, this review is carried out by the ECB in accordance with Article 33(4) of Regulation (EU) No 1024/2013 (cf. item 1.1.1. above).

In Luxembourg, the share of loans in arrears for more than 90 days stood at 0.5% as at 31 December 2013. This figure remained steady as compared to 2012.

• Risks related to the activity of a depositary bank

The custody activity carried out by Luxembourg banks providing wealth management services amounts to around EUR 3,028 billion. By adding the assets deposited in connection with payment and securities settlement transactions to the previous figure, the total amounts to EUR 13,662 billion.

Given the high amount of assets deposited with the Luxembourg banks, an interruption of the service provided by the depositary bank might jeopardise the orderly functioning of the global financial markets. Contrary to the aforementioned risks, the business continuity risk of a depositary bank is mainly a risk that the financial centre implies for the global financial system.

This risk is limited by rules that aim to safeguard depositors' ownership rights and to ensure business continuity. Thus, the legal obligation for banks as regards infrastructure in accordance with Article 5(1a) of the law of 5 April 1993 on the financial sector includes business continuity management. The sixth indent of point (10) of Circular CSSF 12/552 specifies that business continuity management arrangements, which apply, in particular, to the activity of depositary banks, aim to limit the risks of serious disruption of business activities and to maintain key operations. As regards the depositors' protection, the Luxembourg regulations include, in addition to the texts of general application, sectoral rules as per Article 37-1 of the law of 5 April 1993 which relates to the provision of investment services or the performance of investment activities, or Section 4 of Chapter 3 of the law of 12 July 2013 on alternative investment fund managers.

These regulatory requirements will be further strengthened, in particular within the context of the implementation of efficient recovery and resolution mechanisms.

The function of depositary bank is a key activity at the intersection of the banking and investment fund sector. Identifying these points of intersection is paramount when it comes to assessing the financial stability of the Luxembourg market as a whole and the risk of contagion between sectors in particular. Intersections which are important for the financial stability of banks include loan commitments to investment funds as well as deposits received from investment funds. On the asset side, when a bank grants a loan to an investment fund (or promises such a commitment), the assets of the fund act as collateral. On the basis of a cautious over-collateralisation policy, banks are assured of recovering all amounts lent. It should be reminded that the UCIs referred to in Part I of the law of 17 December 2010 relating to undertakings for collective investment, which represent the major portion of the assets under management, are required under Article 50(2)(a) of that law to comply with an upper indebtedness limit set at 10% of their assets. The result is de facto an over-collateralisation of the loans which would be granted by banks to these investment funds and, consequently, a very limited credit risk for the lending credit institution. It should also be noted that as regards the loan commitments, no (depositary) bank has the legal obligation to support the investment funds whose assets have been deposited with such bank. Any contractual commitment in this regard shall remain compatible with the legal requirements aiming to ensure the financial stability of the lending institution. On 31 December 2013, the loans granted by the Luxembourg banks to investment funds amounted only to EUR 8.6 billion. On the liability side, the deposits of investment funds with Luxembourg banks are more significant. They amounted to EUR 93 billion which represent 3.6% of investment funds' net assets. However, these are mostly "operational deposits" which investment funds maintain permanently with their depositary banks for their day-to-day operations. These deposits represent, due to their stability, a limited liquidity risk (deposit withdrawal risk).

• Other risks

Following the two recommendations adopted by the General Board of the European Systemic Risk Board (ESRB) in 2011 concerning lending in foreign currencies (ESRB/2011/1) and funding of credit institutions in US dollars (ESRB/2011/2), the CSSF published, in collaboration with the BCL, Circular CSSF 12/537 on US dollar denominated funding of credit institutions and Circular CSSF 12/538 on lending in foreign currencies which implement the two ESRB recommendations in Luxembourg. The CSSF also put in place a prudential monitoring framework for these risks in accordance with the ESRB requirements. However, it should be noted that these risks are less important in Luxembourg.

As regards the first recommendation, the ESRB published its follow-up report on 4 November 2013, showing that Luxembourg is deemed to be compliant with the requirements set out in Recommendation ESRB/2011/1.

In addition to the two aforementioned recommendations, which already include a section on sound liquidity management, the General Board of the ESRB approved a new recommendation on the funding of credit institutions (ESRB/2012/2). This recommendation requires that the supervisory authorities strengthen their assessment of the funding and liquidity risks incurred by credit institutions as well as that of their funding risk management, with a particular attention to the feasibility of the funding plans, innovative funding instruments and uninsured deposit-like financial instruments which are sold to retail customers. Moreover, it is recommended that the supervisory authorities monitor the asset encumbrance and require credit institutions to implement policies and procedures to manage this encumbrance risk. The timetable provided by this recommendation imposes an implementation of the measures by credit institutions in 2014 and a follow-up by the supervisory authorities in 2014 and 2015.

1.2. Characteristics of the Luxembourg banking sector

The Luxembourg banking legislation provides for two types of banking licences, namely: that of universal banks (141 institutions had this status on 31 December 2013) and that of banks issuing covered bonds (six institutions had this status on 31 December 2013). The main features of the banks issuing covered bonds are: prohibition to collect deposits from the public and monopoly of covered bonds issuance (cf. item 1.9. below).

Depending on their legal status and geographical origin, banks in Luxembourg belong to one of the following three groups:

- banks incorporated under Luxembourg law (109 on 31 December 2013),
- branches of banks incorporated in an EU Member State or assimilated (30 on 31 December 2013),
- branches of banks incorporated in a non-EU Member State (8 on 31 December 2013).

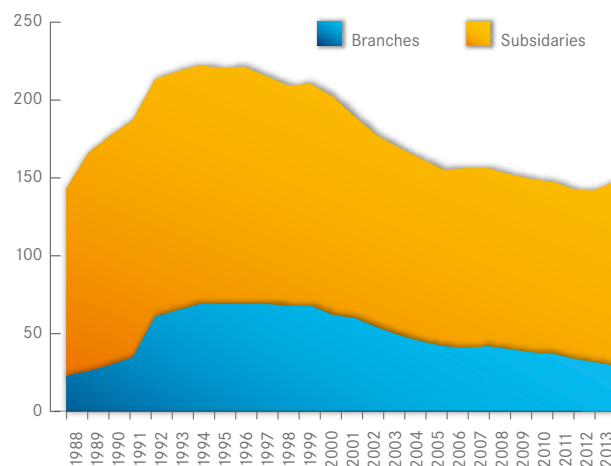
Furthermore, there is one special case: the *caisses rurales* (13 on 31 December 2013) and their central establishment, Banque Raiffeisen, are to be considered as a single credit institution, according to the law on the financial sector.

1.3. Development in the number of credit institutions

With 147 entities authorised at the end of the financial year 2013, the number of banks increased by six entities as compared to 31 December 2012 (141 entities).

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
2008	41	111	152
2009	39	110	149
2010	38	109	147
2011	36	107	143
2012	35	106	141
2013	38	109	147



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

- Lloyds TSB Bank plc, Luxembourg Branch
- Banque de l'Europe Méridionale, succursale de Luxembourg
- Hauck & Aufhäuser Banquiers Luxembourg S.A.

Cessation of activities as at 28 February 2013.

Activities taken over by BEMO EUROPE – BANQUE PRIVEE as at 1 April 2013.

Activities taken over by Hauck & Aufhäuser Privatbankiers KGaA, Niederlassung Luxembourg as at 29 August 2013.

Nine banks started their activities in 2013:

- Banco Safra S.A., Luxembourg Branch
1 February 2013: the bank governed by Brazilian law took over the trade financing activity carried out by another entity of the group.
- BEMO EUROPE – BANQUE PRIVEE
1 April 2013: transfer of the registered office from Paris to Luxembourg.
- Standard Chartered Bank, Luxembourg Branch
3 June 2013: the bank governed by English law carries out the activity of UCI depository bank.
- China Construction Bank (Europe) S.A.
13 August 2013: the bank of Chinese origin is mainly active in corporate banking, but intends also to provide subsequently private banking services; it is aimed to supervise ultimately the European network of the group.
- Hauck & Aufhäuser Privatbankiers KgaA, Niederlassung Luxemburg
29 August 2013: the bank governed by German law took over the activities of Hauck & Aufhäuser Banquiers Luxembourg S.A.
- HSBC Bank Plc, Luxembourg Branch
2 September 2013: the bank governed by English law carries out corporate banking activities.
- Société Générale Financing & Distribution S.A.
24 September 2013: the bank of French origin is specialised in the acquisition of credits, which comes from the Société Générale Group, with a view to transferring them to external investors.
- China Construction Bank Corporation, Luxembourg Branch
1 October 2013: the Chinese bank is mainly active in corporate banking.
- GPB International S.A.
21 October 2013: the bank of Russian origin is active in corporate banking.

1.4. Development in banking employment

As at 31 December 2013, the Luxembourg credit institutions employed 26,237 people. Compared to the situation as at 31 December 2012 when banking employment registered 26,537 people, it decreased by 300 people over a year.

Following the decreases in 2009 (-785 entities), 2010 (-166 entities) and 2012 (-158 entities) and a slight increase in 2011 (+441 entities following the transfer of a certain number of jobs from the PFS sector to the banking sector), banking employment registered a new year-on-year decline which was largely the result of a reduction in staff numbers by a dozen of banks. Part of the reduction can be explained by continuous restructuring and consolidation of activities following mergers and acquisitions. Other banks, which are active in the investment fund field, have preferred to streamline processes by way of increasing automation and to outsource some functions to financial centres at lower cost for staff's cost efficiency reasons.

Finally, the three banks which ceased their activities in 2013 also contributed to the decrease in banking employment.

This decrease was not offset by job creation in the nine credit institutions which started their activities in Luxembourg in 2013.

At a disaggregated level, banks are experiencing contrasting trends in employment. Thus, 44% of the credit institutions increased their staff over a year. This proportion increased as compared to the figure recorded in 2012 (40%). Even though the percentage of institutions which maintained or increased their staff remained steady at 61%, it compares, nonetheless, unfavourably to the pre-crisis period when it exceeded 70%. In 2013, almost 39% of institutions reduced their staff.

The breakdown of aggregated employment shows that the female employment rate remained steady, up from 45.8% to 46.1%. The share of executives in total employment also remained virtually unchanged at 27.2% (against 26.7% in 2012).

Breakdown of the number of employees per bank

Number of employees	Number of banks							
	2006	2007	2008	2009	2010	2011	2012	2013
> 1,000	5	5	5	5	6	6	5	5
500 to 1,000	7	9	8	9	8	9	10	9
400 to 500	3	2	4	3	1	3	3	2
300 to 400	8	10	11	9	9	7	6	7
200 to 300	10	9	8	8	7	5	7	8
100 to 200	18	18	16	18	16	15	17	18
50 to 100	18	21	20	20	21	21	16	15
< 50	87	82	80	77	79	77	77	83
Total	156	156	152	149	147	143	141	147

Situation of employment in credit institutions

	Total		Management			Employees			Total staff			Variation	
	Luxemb.	Foreigners	Men	Women	Total	Men	Women	Total	Men	Women	Total	in number	in %
1998	7,829	12,005	2,900	577	3,477	7,893	8,464	16,357	10,793	9,041	19,834	745	3.9%
1999	7,797	13,400	3,119	670	3,789	8,396	9,012	17,408	11,515	9,682	21,197	1,363	6.9%
2000	7,836	15,232	3,371	783	4,154	9,065	9,849	18,914	12,436	10,632	23,068	1,871	8.8%
2001	7,713	16,148	3,581	917	4,498	9,255	10,108	19,363	12,836	11,025	23,861	793	3.4%
2002	7,402	15,898	3,654	977	4,631	8,966	9,703	18,669	12,620	10,680	23,300	-561	-2.4%
2003	7,117	15,412	3,720	1,049	4,769	8,509	9,251	17,754	12,229	10,300	22,529	-771	-3.3%
2004	7,001	15,553	3,801	1,111	4,912	8,470	9,172	17,642	12,271	10,283	22,554	25	0.1%
2005	6,822	16,405	3,948	1,183	5,131	8,661	9,435	18,096	12,609	10,618	23,227	673	3.0%
2006	6,840	17,912	4,280	1,294	5,574	9,172	10,006	19,178	13,452	11,300	24,752	1,525	6.6%
2007	6,962	19,177	4,669	1,475	6,144	9,557	10,438	19,995	14,226	11,913	26,139	1,381	5.6%
2008	6,898	20,307	5,101	1,672	6,773	9,673	10,759	20,432	14,774	12,431	27,205	1,066	4.1%
2009	6,599	19,821	5,221	1,781	7,002	9,199	10,219	19,418	14,420	12,000	26,420	-785	-2.9%
2010	6,623	19,631	5,048	1,875	6,923	9,033	10,298	19,331	14,081	12,173	26,254	-166	-0.6%
2011	6,270	20,425	5,175	1,905	7,080	9,265	10,350	19,615	14,440	12,255	26,695	441	1.7%
2012	6,220	20,317	5,122	1,966	7,088	9,258	10,191	19,449	14,380	12,157	26,537	-158	-0.6%
2013	6,082	20,155	5,163	1,982	7,145	8,987	10,105	19,092	14,150	12,087	26,237	-300	-1.1%

1.5. Development of balance sheet and off-balance sheet accounts
1.5.1. Balance sheet total of credit institutions

As at 31 December 2013, the total assets of credit institutions amounted to EUR 713.4 billion against EUR 734.8 billion as at 31 December 2012. This represents a decrease of 2.9% over a year. Thus, the banking sector resumed the downward trend recorded in 2012 (-7.3%), 2010 (-3.8%) and 2009 (-14.7%).

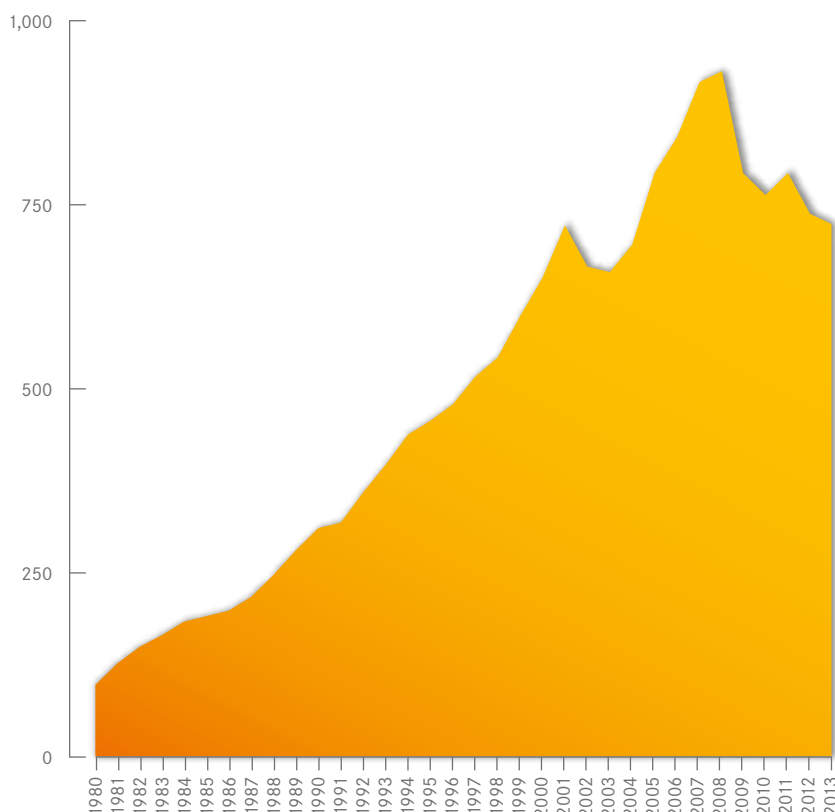
The decrease of the balance sheet total in 2013 was shared by 42% of the banks of the financial centre, a majority of which belong to banking groups established in the euro area. These reductions in activities reflect

the necessity for certain European banks to adapt their risks and balance sheet structure to their capacity to manage and support these risks (deleveraging).

However, the increase in the balance sheet total of certain banks resulted, among others, from the takeover of activities or development of new activities. In the latter case, the banks concerned generally originated from non-EU countries.

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	915.34
2008	929.45
2009	792.54
2010	762.32
2011	792.89
2012	734.77
2013	713.38⁴



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1.5.2. Development of the structure of the aggregated balance sheet

On the **asset** side, the decline of the activity was reflected in all the items, except for loans and advances to credit institutions. The decline in the total balance sheet (-2.9% year-on-year) was dependent on the decreases recorded in loans and advances to customers (-2.9%), fixed-income transferable securities (-7.3%) and loans and advances to central banks and central governments (-25.9%), these items forming almost 47% of the balance sheet assets.

Loans and advances to credit institutions increased by 4.3% over a year to EUR 341.4 billion at the end of December 2013. Despite the increase of EUR 14.2 billion over a year, it represents however a decrease of 11.0% as compared to the situation at the end of 2011. Dominated by intra-group commitments, interbank loans and advances remained predominant on the asset side with 47.9%.

Loans and advances to customers, which include corporates and retail customers, declined by 2.9% to EUR 158.2 billion at the end of 2013 (against EUR 162.9 billion in 2012). Among those loans and advances, the exposures to retail customers, which were mainly from Luxembourg, rose by 5.6% over a year. These

⁴ Preliminary figure.

exposures, which had grown by almost 2.9% in 2012, were worth EUR 43.1 billion as at 31 December 2013. On the other hand, loans and advances to corporates decreased by 7.8% over a year (compared to 11.4% in 2012). This decrease occurred predominantly in Luxembourg banks belonging to foreign banking groups forced to reduce their financial intermediation business. As regards the balance sheet structure, the proportion of loans and advances to customers remained steady with 22.2% of the balance sheet total as at 31 December 2013.

At the end of 2013, **loans and advances to central banks and central governments** reached EUR 40.0 billion against EUR 54.0 billion at the end of 2012. Among these loans and advances, deposits with central banks represented 79.3%, i.e. EUR 31.7 billion. The partial easing of the European sovereign debt crisis explains why some banks, which invested excess liquidity with the BCL at the peak of the crisis, decreased these investments. This is particularly the case for certain Swiss banking groups using Luxembourg as an entry point into the European System of Central Banks. The trend was not the same for all the banks in the financial centre, 20% of which continued to increase their deposits with the BCL in 2013. It should also be noted that exposures in the form of loans and advances to central administrations decreased by 7.7% to EUR 8.3 billion at the end of 2013.

Fixed-income securities, which represented over 90% of the total transferable securities, dropped by 7.3% during 2013. The positions in sovereign bonds continue to rise (+5.3% in 2013 and +14.4% in 2012) compared to 2011, when the depreciation of the Greek debt and the active reduction of certain positions in sovereign debt securities considered incompatible with the risk profile of Luxembourg banks induced a 19.2% decrease of positions in sovereign bonds. For positions of Luxembourg banks in bonds issued by banks or corporates, the trend is still heading downwards with -14.7% for banking counterparties and -9.6% for corporates. These decreases were higher than in 2012 (-4.6% and -8.3%). These developments should be addressed within the context of the introduction of the liquidity ratio LCR (Liquidity Coverage Requirement) in 2015.

Since the decline in the fixed-income transferable securities portfolio exceeded the fall in the aggregated balance sheet, the portion of fixed-income transferable securities in the balance sheet total decreased to 19.1% (compared to 20.0% at the end of 2012). The sector-based composition of this portfolio continued to show mainly bank (44%) and government (35%) securities.

Due to the reduction of their assets, the banks in the financial centre requested less external funding than in 2012. The reduction of the external **funding sources** concerned amounts owed to related credit institutions and amounts owed to central banks.

Amounts owed to credit institutions, mainly in the form of intra-group operations, dropped by 7.2% to EUR 284.1 billion at the end of December 2013. These amounts represented 39.8% of the Luxembourg banks' balance sheet total against 41.7% at the end of 2012.

Amounts owed to customers, mainly consisting of corporate deposits, wealth management structures and retail customers, rose by 6.1%. These amounts reached EUR 276.4 billion as at 31 December 2013. As in the past, the volume of deposits from customers (38.7%) played a prominent role among the refinancing means of the banking activities of the financial centre and allowed the Luxembourg banking sector to easily fund its loans and advances to customers.

Amounts owed to central banks reached EUR 7.6 billion as at 31 December 2013. Even if there was a drop by 42.9% over a year, these amounts represented only 1.1% of the aggregated liabilities. The CSSF continues to discourage banks from using this type of financing due to the leverage triggered by these operations.

Following the decline that began in 2012, banks continued to reduce their reliance on **debt securities** in 2013. With -7.7%, the decrease was more significant than in 2012 (-1.9%). The decline was part of a market context characterised, on the one hand, by weak demand for banks' debt securities and, on the other hand, by slower credit activity, reducing thus the banks' funding needs. With a total of EUR 60.1 billion, they represented 8.4% of the aggregated liabilities as at 31 December 2013 (against 8.9% in 2012).

Provisions amounted to EUR 4.7 billion. This figure includes an amount of EUR 973 million for the lump sum provision and an amount of EUR 686 million for the deposit guarantee (AGDL). These two instruments enable banks to manage, in a countercyclical manner, the financial shortfalls they may face. In order to face financial losses in an adverse situation, banks set up provisions in benign times. This allows them to absorb the impact of such losses on their financial situation. This was the case in 2011 with the losses on Greek debt and in 2008 with the involvement of the deposit guarantee scheme when the Icelandic banks collapsed. In 2013, the banks increased the volume of these provisions by EUR 133 million. It should be noted in this context that the

CSSF now requires that the AGDL provision of each bank represents at least 1% of its guaranteed deposits. The stock of provisions arising therefrom shall enable the quick and smooth compliance by the Luxembourg deposit guarantee scheme with the future pre-financing requirements defined at European level.

At the end of 2013, **equity** accounted for EUR 51.6 billion of the aggregate liabilities of the financial centre's banks. Equity increased by 5.2% under the effect of hoarding transactions and represented 7.2% of the balance sheet total as at 31 December 2013.

Aggregate balance sheet total – in million EUR

ASSETS	2012	2013 (*)	Variation	LIABILITIES	2012	2013 (*)	Variation
Loans and advances to central banks and central governments	54,022	40,008	-25.94%	Amounts owed to central banks	13,350	7,618	-42.93%
Loans and advances to credit institutions	327,207	341,389	4.33%	Amounts owed to credit institutions	306,066	284,117	-7.17%
Loans and advances to customers	162,892	158,209	-2.87%	Amounts owed to customers	260,524	276,384	6.09%
Financial assets held for trading	14,951	11,775	-21.24%	Amounts owed represented by securities	65,121	60,081	-7.74%
Fixed-income transferable securities	147,129	136,393	-7.30%	Liabilities (other than deposits) held for trading	14,093	11,000	-21.95%
Variable-yield transferable securities	13,825	12,438	-10.03%	Provisions	4,445	4,693	5.57%
Fixed assets and other assets	14,742	13,167	-10.69%	Subordinated debts	6,788	5,912	-12.91%
				Other liabilities	15,288	11,928	-21.98%
				Capital and reserves	49,093	51,648	5.20%
Total	734,768	713,378	-2.91%	Total	734,768	713,378	-2.91%

(*) Preliminary figures

Structure of the aggregate balance sheet

ASSETS	2012	2013 (*)	LIABILITIES	2012	2013 (*)
Loans and advances to central banks and central governments	7.35%	5.61%	Amounts owed to central banks	1.82%	1.07%
Loans and advances to credit institutions	44.53%	47.86%	Amounts owed to credit institutions	41.65%	39.83%
Loans and advances to customers	22.17%	22.18%	Amounts owed to customers	35.46%	38.74%
Financial assets held for trading	2.03%	1.65%	Amounts owed represented by securities	8.86%	8.42%
Fixed-income transferable securities	20.02%	19.12%	Liabilities (other than deposits) held for trading	1.92%	1.54%
Variable-yield transferable securities	1.88%	1.74%	Provisions	0.60%	0.66%
Fixed assets and other assets	2.01%	1.85%	Subordinated debts	0.92%	0.83%
			Other liabilities	2.08%	1.67%
			Capital and reserves	6.68%	7.24%
Total	100.00%	100.00%	Total	100.00%	100.00%

(*) Preliminary figures

1.5.3. Use of derivative financial instruments by credit institutions

Banks in the financial centre used derivative financial instruments for a total nominal amount of EUR 638.5 billion in 2013, representing a fall of EUR 23.5 billion over a year, i.e. -3.6%. The use of derivative instruments by credit institutions mainly takes place in the context of hedging of existing positions and transactions on behalf of their clients. The use of derivative financial instruments recorded a drop for all categories of instruments, except for interest rate-related instruments.

Use of derivative financial instruments by credit institutions

Notional amounts (in billion EUR)	2012	2013 (*)	Variation		Structure	
			in volume	in %	2012	2013 (*)
Transactions related to interest rate	171.2	176.2	5.0	2.9%	25.9%	27.6%
<i>of which: options</i>	3.9	6.6	2.7	69.7%	2.3%	3.7%
<i>of which: interest rate swaps</i>	158.8	154.6	-4.2	-2.7%	92.8%	87.7%
<i>of which: future or forward rate agreements (FRA)</i>	0.7	0.4	-0.3	-40.7%	0.4%	0.2%
<i>of which: interest rate futures</i>	7.9	14.7	6.8	86.9%	4.6%	8.3%
Transactions related to title deeds	14.8	13.6	-1.2	-8.3%	2.2%	2.1%
<i>of which: futures</i>	6.4	6.9	0.5	7.8%	42.9%	50.4%
<i>of which: options</i>	8.5	6.7	-1.7	-20.4%	57.1%	49.6%
Transactions related to exchange rates	445.8	432.8	-13.0	-2.9%	67.3%	67.8%
<i>of which: forward foreign exchange transactions</i>	363.8	352.9	-10.9	-3.0%	81.6%	81.5%
<i>of which: cross-currency IRS</i>	72.7	70.4	-2.3	-3.2%	16.3%	16.3%
<i>of which: options</i>	9.3	9.5	0.3	2.8%	2.1%	2.2%
Transactions related to credit quality	30.2	15.9	-14.3	-47.3%	4.6%	2.5%
Total	662.0	638.5	-23.5	-3.6%	100%	100%

(*) Preliminary figures

1.5.4. Off-balance sheet

As at 31 December 2013, the contingent exposure of the Luxembourg banking sector through loan commitments and financial guarantees given amounted to EUR 123.6 billion, against EUR 117.7 billion at the end of 2012, which represented a 5.0% increase over a year.

The assets deposited by UCIs and the assets deposited by other professionals acting on financial markets increased by 10.2% and 4.8% in 2013, respectively (+18.2% and +7.8% in 2012). These rises reflected the development of stock prices of certain assets under custody as well as the development of activities by some depositary banks.

Assets deposited by customers as in the off-balance sheet - in billion EUR

	2012	2013 (*)	Variation	
			in volume	in %
Assets deposited by UCIs	2,437.8	2,686.6	248.8	10.2%
Assets deposited by clearing or settlement institutions	1,188.1	1,204.2	16.1	1.4%
Assets deposited by other professionals acting in the financial markets	6,928.7	7,260.7	332.0	4.8%
Other deposited assets	334.4	340.9	6.5	1.9%

(*) Preliminary figures

1.6. Development in the profit and loss account

The profit and loss account of the Luxembourg banking sector showed a net result of EUR 3,565 million as at 31 December 2013, i.e. a slight decrease of EUR 32 million (-0.9%) compared to 2012.

The 2013 profit and loss account combines two opposite developments: the decrease of the interest-rate margin that results from the decrease in the balance sheets and the very low level of interest rates and the increase of the net commissions received and other net income in the wake of good stock market performance which positively influenced the value of the banking assets and assets under management.

Development in the profit and loss account – in million EUR

	2012	Relative share	2013 (*)	Relative share	Variation 2012/2013	
					in volume	in %
Interest-rate margin	5,551	56%	5,061	48%	-490	-8.8%
Net commissions received	3,705	38%	3,984	38%	279	7.5%
Other net income	578	6%	1,437	14%	859	148.6%
Banking income	9,834	100%	10,482	100%	648	6.6%
General expenses	-5,017	-51%	-5,229	-50%	211	4.2%
<i>of which: staff costs</i>	-2,637	-27%	-2,772	-26%	136	5.2%
<i>of which: general administrative expenses</i>	-2,381	-24%	-2,456	-23%	75	3.2%
Result before depreciation	4,816	49%	5,253	50%	437	9.1%
Net depreciation	-761	-8%	-924	-9%	162	21.3%
Taxes	-458	-5%	-765	-7%	306	66.9%
“Real” tax burden ⁵	-544		-547		3	0.6%
Net result for the financial year	3,597	37%	3,565	34%	-32	-0.9%

(*) Preliminary figures

As far as income is concerned, the **interest-rate margin**, which amounted to EUR 5,061 million, dropped by 8.8% over a year. This development was due both to the market conditions where the margins of intermediation continued to be low and to the decrease of the aggregate balance sheet. Since its highest level reached in 2008, the interest-rate margin decreased by about one-third. The persistence of extremely low interest rates, which reduces the profitability of the intermediation activity significantly, poses now a real challenge to banks. Moreover, it implies that the part of the **net commissions received** in the recurring banking income increases significantly. Its level increased from 40% in 2010-2012 to 44% in 2013. It should be reminded that the net commissions received mainly result from asset management activities on behalf of private and institutional clients, including services provided to investment funds. Within a very favourable stock market context, this income reached EUR 3,984 million, i.e. a 7.5%-increase over a year. This positive stock market context also explains the increase of the **other net income**. The highly volatile item includes, in 2013, non-recurring effects recorded by a limited number of banks. The annual growth of this income reached EUR 859 million, half of which is the result of latent gains inherent in positions valued at market price. It furthermore corresponds to gains on securities which some banks decided to realise within a favourable market context.

The total operating income, as measured by the banking income, amounted to EUR 10,482 million as at 31 December 2013. Similarly to 2012, the rise of the banking income largely results from the increase in other net income, which, in general, is a non-recurrent volatile component of the profit and loss account.

In respect of general expenses, the increase reached 4.2%. This increase is due to banking staff restructuring. In the light of activity and income curtailment, the banks seek to reduce their costs, including staff costs. At first, the staff reductions result in additional but not recurring fees.

Given the development of the general expenses, the **gross profit before provisions and taxes** increased by 9.1% over a year.

⁵ As from 1 January 2008, the prudential reporting is based on the IFRS standards. These standards allow, in particular, activating future tax charges by crediting the tax charges account. Due to these positive tax expenses, there are, depending on the year, material differences with the “real” tax burden which, based on the Lux-GAAP standards, is used to determine the basis for the calculation of the taxes due to the tax administration.

As at 31 December 2013, **net depreciation** reached EUR 924 million, i.e. a 21.3%-increase compared to 2012. This increase, restricted to a limited number of banks, is attributable to reasons specific to each bank. It is not the result of an overall deterioration in the asset quality, as evidenced by the very low rate (0.5%) of loans exceeding 90 days past due. This rate remained steady compared to last year.

Tax charges recorded in the 2013 profit and loss account amounted to EUR 765 million. This amount represents the overall booked tax charges, including taxes due in Luxembourg and abroad, without distinction between current and deferred taxes. Current taxes in Luxembourg, which represent the accounting based estimate of the taxes due in Luxembourg for the financial year 2013, reached EUR 547 million, i.e. an amount which is in line with the tax burden relating to the financial year 2012.

Overall, the above indicated factors taken as a whole resulted in a **net income** decrease of 0.9% compared to last year. The downward trend was not the same for all the banks in the financial centre, as appears from 44% of the banks whose net results continued to increase over a year.

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

	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013 (*)
Interest-rate margin	4,080	3,913	3,905	4,830	6,002	7,298	6,571	5,479	5,865	5,551	5,061
Net commissions received	2,533	2,771	3,209	3,674	4,010	3,644	3,132	3,587	3,832	3,705	3,984
Other net income	942	734	1,140	2,296	964	-505	85	483	-830	578	1,437
Banking income	7,554	7,418	8,255	10,800	10,976	10,437	10,553	9,549	8,868	9,834	10,482
General expenses	-3,385	-3,461	-3,693	-3,981	-4,420	-4,560	-4,451	-4,609	-4,789	-5,017	-5,229
<i>of which: staff costs</i>	-1,752	-1,798	-1,945	-2,160	-2,372	-2,461	-2,449	-2,497	-2,535	-2,637	-2,772
<i>of which: general administrative expenses</i>	-1,632	-1,663	-1,748	-1,821	-2,048	-2,099	-2,002	-2,112	-2,253	-2,381	-2,456
Result before depreciation	4,170	3,957	4,562	6,819	6,556	5,877	6,102	4,939	4,080	4,816	5,253
Net depreciation	-637	-344	-296	-305	-1,038	-5,399	-3,242	-498	-1,572	-761	-924
Taxes	-658	-746	-768	-843	-780	-259	-804	-625	-18	-458	-765
"Real" tax burden ⁶						-654	-449	-599	-503	-544	-547
Net result for the financial year	2,874	2,866	3,498	5,671	4,739	218	2,056	3,817	2,490	3,597	3,565

(*) Preliminary figures

1.7. Development in own funds and in the solvency ratio

1.7.1. Number of banks required to meet a solvency ratio

As at 31 December 2013, the number of banks required to meet a non-consolidated solvency ratio stood at 112 (107 in 2012). Among these banks, 87 carried out limited trading activities (compliance with *de minimis* conditions) and were therefore authorised to calculate a simplified ratio. Actual trading activities remained confined to 25 banks, i.e. two entities more than in 2012. However, these activities are of lesser significance for the Luxembourg banking centre. Among the 26 banks that also calculate a consolidated solvency ratio, 12 were required to calculate an integrated ratio.

Number of banks required to meet a non-consolidated and/or consolidated solvency ratio

	Integrated ratio		Simplified ratio		Total	
	2012	2013	2012	2013	2012	2013
Non-consolidated	23	25	84	87	107	112
Consolidated	12	12	14	14	26	26

⁶ As from 1 January 2008, the prudential reporting is based on the IFRS standards. These standards allow, in particular, activating future tax charges by crediting the tax charges account. Due to these positive tax expenses, there are, depending on the year, material deviations from the "real" tax burden which, based on the Lux-GAAP standards, is used to determine the basis for the calculation of the taxes due to the tax administration.

1.7.2. Development of the solvency ratio

The figures below are based on the consolidated figures of banks required to calculate their solvency ratio on a consolidated basis. The periodic information is to be provided to the CSSF within a time limit that should allow banks to gather and validate the requested information. As these deadlines are longer for consolidated figures, the consolidated figures as at 31 December 2013 are available only after the cut-off date for the CSSF's annual report. As a consequence, the figures below reflect the situation as at 31 December 2013 except for banks required to calculate their solvency ratio on a consolidated basis. The data of the latter relate to 30 June 2013, which is the last available reporting.

• Aggregate solvency ratio

The aggregate solvency ratio, which measures the volume of own funds compared to the total minimum own funds requirements according to Circular CSSF 06/273, reached 19.7% as at 31 December 2013 and thus largely exceeded the minimum of 8% as required under the existing prudential regulations. This ratio increased by 200 basis points compared to 31 December 2012 after it remained steady between 2009 and 2012. The increase was due to the combined effects of the increase in own funds and a decrease in the capital requirements.

With 17.2% as at 31 December 2013, the Tier 1 ratio, the numerator of which only includes own funds which absorb losses in going-concern situations, also increased compared to 31 December 2012 (15.5%). The average Core Tier 1 ratio was 17.1% as at 31 December 2013, original own funds (Tier 1) only marginally being constituted of instruments which are not eligible as original own funds under the future Basel III framework (for example hybrid instruments).

Ratio	2012	2013
Solvency ratio	17.7%	19.7%
Tier 1 ratio	15.5%	17.2%
Core Tier 1 ratio	15.3%	17.1%

• Own funds

Aggregate own funds, eligible for the purpose of complying with prudential standards in terms of solvency, amounted to EUR 49,002 million as at 31 December 2013. The 7.3%-growth compared to 31 December 2012 was mainly due to the increase of paid-up capital (+EUR 2,029.5 million). Thus, a certain number of institutions carried out capital increases to reach the 9%-ratio of core capital required by the CSSF. Moreover, about half of the increase comes from banks which started their activities in 2013.

As regards the quality of aggregate own funds, this rise of the paid-up capital increased the total amount of original own funds by 7.6% as compared to the end of 2012. In terms of distribution of own funds, the portion of original own funds has consequently slightly risen to 87.4% of own funds before deductions at the end of the financial year 2013 (87% in 2012). Additional own funds (Tier 2) and sub-additional own funds (Tier 3) only represented 12.5% and 0.02% of own funds before deductions.

Own funds - in million EUR

Numerator	2012	2013
<i>Original own funds</i>	44,956.6	47,373.6
Paid-up capital	16,980.7	19,010.2
Silent participation (<i>Stille Beteiligungen</i>)	330.6	143.3
Share premium account	8,090.8	8,375.6
Reserves (including funds for general banking risks)	18,672.8	18,747.4
Prudential filters	-274.9	-60.5
Gains and losses brought forward for the financial year	-56.1	-46.9
Minority interests	1,212.7	1,204.4
<i>Items to be deducted from original own funds</i>	-5,145.9	-4,525.6
Own shares	-1.6	-1.6
Intangible assets	-3,095.2	-3,076.7
Other deductions from original own funds	-2,049.1	-1,447.3
ORIGINAL OWN FUNDS (Tier 1)	39,810.7	42,848.0
<i>Additional own funds before capping</i>	6,846.1	6,877.9
Upper Tier 2	5,134.4	5,151.7
Lower Tier 2: Lower Tier 2 subordinated debt instruments and cumulative preference shares with fixed maturity	1,711.6	1,726.2
<i>Additional own funds after capping</i>	6,588.9	6,615.7
Deductions from additional own funds	-624.3	-469.3
ADDITIONAL OWN FUNDS after capping and after deductions (Tier 2)	5,964.6	6,146.4
Sub-additional own funds before capping	297.4	364.5
SUB-ADDITIONAL OWN FUNDS after capping (Tier 3)	7.8	8.4
<i>Own funds before deductions (Tier 1 + Tier 2 + Tier 3)</i>	45,783.1	49,002.8
Deductions from the total of own funds	-119.6	-0.9
ELIGIBLE OWN FUNDS (numerator of integrated ratio/simplified ratio)	45,663.5	49,001.8

• Capital requirements

The minimum own funds requirements decreased by 3.2% between the end of 2012 and the end of 2013 and reached EUR 19,936 million. This decrease is mostly due to the balance sheet restructuring of a local bank through the disposal of the legacy portfolio, and to the run-off in certain activities considered to be of secondary importance by some banks.

As regards the components of capital requirements, the credit risk exposures still triggered the most important capital requirements. Their proportion in the total requirement amounted to 86.4% as at 31 December 2013. Owing to the activities carried on in the financial centre, the other minimum capital requirements remained marginal, except for the requirements to cover operational risk that represented 8.5% of total minimum capital requirements. The minimum own funds requirements to cover market risk represented 0.4% of the total amount of capital requirements.

The “other capital requirements” which include, inter alia, the additional capital requirements for exceeded limits on large exposures and additional capital requirements under capital floors calculated based on capital requirements under Basel I, only represented 3.1% of total minimum capital requirements. It should be noted that the capital floors limit the prudential recognition of the reducing effects of minimum capital requirements that could result from the implementation of advanced measurement methods such as the internal ratings-based approach for credit risk or advanced measurement approaches for operational risk.

Capital requirements - in million EUR

Denominator	2012	2013
TOTAL CAPITAL ADEQUACY REQUIREMENT	20,602.3	19,935.8
Requirement to cover credit risk	18,214.8	17,227.7
Requirement to cover foreign exchange risk	72.6	55.7
Requirement to cover interest rate risk	27.5	21.7
Requirement to cover the risk in relation to equities	6.3	7.3
Requirement to cover the risk in relation to commodities	0.5	0.3
Requirement according to internal models	37.8	33.1
Requirement to cover settlement/delivery risk	1.9	0.1
Requirement to cover operational risk	1,600.4	1,691.2
Other capital adequacy requirements (among others exceeding large exposures, Basel II floor level, etc.)	640.6	898.7

As at 31 December 2013, 18 banks had obtained the authorisation to use an internal ratings-based approach for credit risk according to Basel II, 10 of which have used advanced methods allowing not only own estimates of probabilities of default but also of the loss given default and/or of the conversion factors. These 18 banks represented 35.9% of the balance sheet total of the financial centre as at 31 December 2013.

As regards operational risk, 11 banks were authorised to use the advanced measurement approach (AMA). The other banks used the basic indicator approach (65 banks) and the standardised approach (36 banks) to determine the capital requirements.

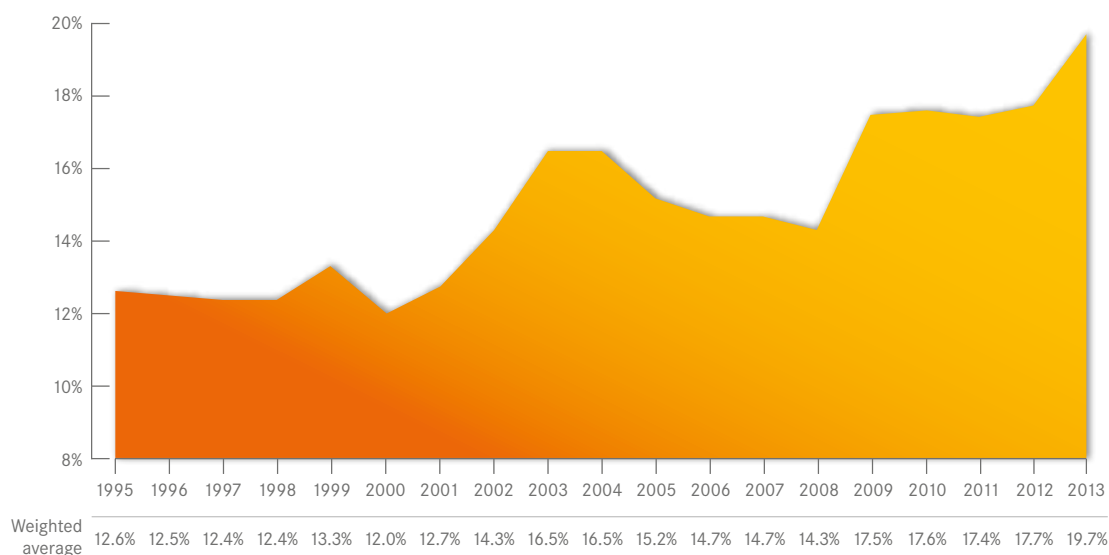
Basel II calculation methods implemented by the banks of the financial centre

	Number of banks
Credit risk	
Standardised approach	94
Internal ratings-based approach	18
<i>of which: foundation approach (F-IRB)</i>	8
<i>of which: advanced approach (ADV-IRB)</i>	10
Operational risk	
Basic indicator approach	65
Standardised approach	36
Advanced measurement approaches	11

1.7.3. Long-term development of the solvency ratio

The following graph illustrates the development in the solvency ratio since 1995. The weighted average is the ratio of total eligible own funds in the financial centre over total risk weighted exposure amounts. This average takes into account credit institutions based on volume and level of risk of their business.

Development in the solvency ratio



1.7.4. Development in the solvency ratio distribution

The high level of capitalisation, as shown by the aggregate solvency ratio, is also reflected at disaggregated level. Thus, only four banks had a solvency ratio within the weak capitalisation bands, i.e. below 10% but not below 8%. This number has decreased by three entities since the financial year 2012. At the other extreme, i.e. in the high capitalisation end, 77% of the banks had a ratio above 15%.

Distribution of the solvency ratio

Ratio	2012		2013	
	Number of banks	as % of total	Number of banks	as % of total
<8%	0	0%	0	0%
8%-9%	2	2%	0	0%
9%-10%	5	5%	4	4%
10%-11%	2	2%	4	4%
11%-12%	5	5%	2	2%
12%-13%	7	7%	8	7%
13%-14%	6	6%	2	2%
14%-15%	7	7%	6	5%
15%-20%	21	20%	23	21%
>20%	52	49%	63	56%
Total	107	100%	112	100%

1.7.5. Transition to the solvency regime provided for in Regulation (EU) No 575/2013

As from 1 January 2014, the solvency of banks in the EU is determined by new rules. These rules, which are provided for in Regulation (EU) No 575/2013, reflect the Basel III agreement developed internationally in response to the financial crisis. As regards solvency, they provide for the strengthening of both the capital base, in qualitative and quantitative terms, and capital requirements, in particular for counterparty credit risk.

On the basis of the analyses carried out by the CSSF, it appears that the Luxembourg banking sector is well positioned to meet the new solvency standards⁷. All but a very few of the Luxembourg banks have already complied with the regulatory requirements which will wholly apply as from 2018/2019.

Given the position of the Luxembourg financial centre which is based on management activities on behalf of third parties, it is crucial to safeguard the financial centre's reputation and, in particular, to preserve these third parties' confidence in the banking sector. To this end, the CSSF decided to anticipate the implementation of the capital conservation buffer which, in accordance with European regulations, is to be fully implemented in stages by 1 January 2019 at the latest. The requirement in question, as laid down in Article 6 of CSSF Regulation N° 14-01 on the implementation of certain discretions of Regulation (EU) No 575/2013, provides that Luxembourg banks shall hold as from 1 January 2014 Common Equity Tier 1 Capital (CET1) up to 7% of their capital requirements (the minimum threshold to be complied with is 4.5%; a capital conservation buffer of 2.5% is added to this threshold). All banks of the financial centre comply with the CET1 requirements of 7%. However, half a dozen of banks, while complying with the 8%-minimum threshold of overall capital requirements have a total capital ratio below 10.5% (the minimum threshold to be complied with is 8%; a capital conservation buffer of 2.5% must be added to this threshold). In accordance with the aforementioned European regulations, these banks are therefore subject to constraints as regards their dividend and remuneration policies (bonus payments). It should also be noted that the leading banks which serve the local market fully comply with all the aforementioned requirements.

1.8. International presence of Luxembourg banks

Branches established in the EU/EEA as at 31 December 2013

Country	Branches of Luxembourg banks established in the EU/EEA	Branches of EU/EEA banks established in Luxembourg
Austria	2	-
Belgium	13	1
Denmark	1	-
France	4	3
Germany	4	14
Greece	1	-
Ireland	4	-
Italy	5	-
Netherlands	4	1
Poland	2	-
Portugal	3	2
Spain	9	1
Sweden	2	2
United Kingdom	3	5
Total	57	29

⁷ Article 92 of Regulation (EU) No 575/2013 introduces three regulatory minimum amounts, i.e. a Common Equity Tier 1 capital ratio of 4.5%; a Tier 1 capital ratio of 6% and a total capital ratio of 8%. The European regulations also provide for the implementation of capital buffers, including the capital conservation buffer.

Freedom to provide services within the EU/EEA as at 31 December 2013

Country	Luxembourg banks providing services in the EU/EEA	EU/EEA banks providing services in Luxembourg
Austria	41	30
Belgium	60	22
Bulgaria	23	-
Croatia	1	-
Cyprus	25	3
Czech Republic	24	-
Denmark	43	7
Estonia	23	1
Finland	41	8
France	64	79
Germany	66	58
Gibraltar	1	4
Greece	40	2
Hungary	24	8
Iceland	7	1
Ireland	37	32
Italy	50	13
Latvia	24	3
Liechtenstein	9	8
Lithuania	25	1
Malta	25	7
Netherlands	52	33
Norway	20	1
Poland	26	1
Portugal	42	7
Romania	26	-
Slovakia	23	1
Slovenia	23	-
Spain	50	8
Sweden	38	8
United Kingdom	52	81
Total number of notifications	1,005	427
Total number of banks concerned	79	427

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

In 2013, the market of banks issuing covered bonds developed only moderately. The Luxembourg financial centre includes six banks issuing covered bonds which are divided into two types, namely banks that manage their existing cover assets or reduce their portfolios (controlled run-off) and those wishing to take advantage of the possibilities offered by the Luxembourg legislator and seek to further develop their activities in the years to come.

As at 31 December 2013, the aggregate balance sheet total of the six banks issuing covered bonds amounted to EUR 36.2 billion. The volume of public-sector covered bonds issued by the six banks slightly dropped to reach EUR 21 billion at the end of 2013 against EUR 24.2 billion at the end of 2012.

Issues of covered bonds were guaranteed by total cover assets amounting to EUR 23.9 billion. Consequently, covered bonds benefited on average from an over-collateralisation of 13.8% according to the nominal value and from an over-collateralisation of 15.5% according to the net present value as at 31 December 2013.

As the activities of the banks issuing covered bonds are limited to financing the public sector at the moment, it should be noted that the crisis affecting certain central, regional and local administrations within and outside the euro area (such as for example Detroit) and the consistent value adjustments to be carried out had also an impact on the performance of some banks and, in general, continue to present risks for this type of banks. The rating of the issues of the different banks varies from AAA to BBB and banks willing to maintain their best quality rating shall do so by offsetting their risks within the cover assets by a considerable level of over-collateralisation.

On 27 June 2013, the Luxembourg legislator adopted a law reforming banks issuing covered bonds. This reform covers, among others, two points, i.e.:

- the dissolution and liquidation regime for banks issuing covered bonds which is aligned with the recently reformed German framework consisting in maintaining the banking status for the part constituted by cover assets and the covered bonds issued in case of liquidation of a bank issuing covered bonds;
- the introduction of a new category of covered bonds, i.e. mutual covered bonds; it should be noted that for the time being, no bank expressed an interest in issuing mutual covered bonds.

2. PRUDENTIAL SUPERVISORY PRACTICE

2.1. Purpose of prudential supervision

It is commonly accepted that the purpose of the prudential supervision of banks is to maintain financial stability and protect the public's savings, i.e. to preserve the non-professional customers' deposits. This objective is an obligation of means, not of results. Prudential supervision is not an absolute guarantee against bank failures involving losses for depositors.

2.2. Monitoring of quantitative standards

In order to ensure financial stability and risk spreading, credit institutions must observe the following quantitative standards:

- minimum equity capital;
- capital ratio;
- limitation of risk concentration to a single debtor or a group of associated debtors;
- liquidity ratio;
- limitation of qualifying holdings;
- a reference limit set at 20% of own funds for non-trading book interest rate risk (cf. item 2.6. below).

The CSSF monitors compliance with these standards and follows the banks' activities by means of a reporting harmonised at European level. This reporting includes the Financial Reporting (balance sheet, profit and loss account and related detailed tables) and the Common Reporting (detailed calculation of the solvency ratio). In addition, the CSSF requires periodic tables on, among other things, currency positions, large exposures and liquidity.

Within the scope of monitoring compliance with large exposure limits, the CSSF intervened 18 times in writing in 2013 (21 times in 2012), notably to inform that the maximum level of large exposures had been exceeded and to request the bank concerned to provide information on the measures it intended to take to bring the commitments back within the regulatory limits.

The sanctions imposed by the CSSF on Luxembourg banks for non-compliance with the regulatory provisions are described in Chapter XIII "Instruments of supervision".

2.3. Monitoring of qualitative standards

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

- long form reports prepared by the *réviseurs d'entreprises* (statutory auditors);
- management letters and similar reports prepared by the *réviseurs d'entreprises*;
- on-site inspections at the banks' premises by CSSF agents;
- reports prepared by the banks' internal auditors;
- compliance reports;
- ICAAP reports.

All these reports are analysed 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 based on reports, through the preparation of deficiency letters, to convening the bank's management or on-site inspections undertaken by the CSSF agents. Where necessary, the CSSF may use its formal powers of injunction, suspension and sanction.

During 2013, the CSSF sent 219 deficiency letters to banks based on shortcomings in terms of organisation or due to the conduct of business.

The CSSF intervened 29 times with respect to quality deficiencies of internal reports, notably ICAAP reports. As regards the ICAAP, the CSSF requested a more precise description of:

- the stress tests and their inclusion in the day-to-day management,
- the management of concentration risk, including the indirect concentrations resulting from risk mitigation techniques,
- the plans for the management of capital and liquidity crises, and
- the definition of risk appetite.

These subjects are generally dealt with in the ICAAP report, but their description does not always adequately reflect the specificity of the business model of banks and all inherent risks.

The sanctions imposed by the CSSF on banks for non-compliance with the regulatory provisions are described in Chapter XIII "Instruments of supervision".

2.4. Supervisory review process

The term "Supervisory Review Process" (SRP) refers to the assessments, controls and measures as a whole, implemented by the CSSF in order to assess and preserve the capacity of a credit institution to manage and support the risks it incurs.

In 2013, the CSSF did not bring any major change to the SRP methodology. With the entry into force of the fourth review of Directive 2006/48/EC as at 1 January 2014 and the publication of Regulation (EU) No 1024/2013 implementing the Single Supervisory Mechanism (SSM), this methodology is however expected to evolve.

Directive 2013/36/EU (CRD IV) includes the basic rules applicable to the SRP operated by the supervisory authorities in the EU. These rules laid down in Article 97 to 101 of CRD IV shall also apply to the European Central Bank where it will become, as from November 2014, the competent authority within the SSM. These articles largely reflect the SRP as it existed in the European texts relating to Directive 2006/48/EC. However, CRD IV brings some significant innovations, in particular:

- a formal decision-making process as regards liquidity adequacy;
- a formal review of the authorisations granted as regards internal models to determine capital requirements;
- a more important role given to stress tests which, in accordance with Article 100 of CRD IV, are to be applied by the CSSF at least once a year based on the SRP;

- an analysis of the business model of banks aiming to establish the sustainable character of the activities;
- the explicit consideration of systemic risk;
- the consideration of excessive leverage risk.

As regards liquidity, CRD IV restores a balance between the risk mitigation mechanisms which are own funds and liquidity buffers. With Directive 2006/48/EC, regulators mainly focussed on own funds as safety cushion against the risks involved. European rules broadly based on the Basel II framework therefore required that banks put in place an Internal Capital Adequacy Assessment Process (ICAAP) which the supervisory authorities were in charge of monitoring. The financial crisis triggered by problem loans (subprime) strongly reminded that financial stability is based on two safeguard pillars, i.e. own funds and liquidity. Today, Article 105 of CRD IV provides supervisory authorities with a broad legal base to impose specific requirements on banks when the Internal Liquidity Adequacy Assessment Process (ILAAP)⁸ of banks shows weaknesses. At the same time, the decisions taken together by supervisory authorities, acting as a college, in respect of capital adequacy (and surcharge) are extended to the liquidity area.

As regards the internal models to determine regulatory capital requirements, Article 101 of CRD IV provides for a review on a regular basis, and at least every three years, of authorisations relating thereto. Moreover, Article 78 requires in-scope banks to participate in a benchmarking exercise coordinated by the EBA on an annual basis. This exercise aims to better monitor calculation practices which, today, benefit from greater flexibility and to identify and address the calculation methods deemed less conservative and that would distort competition among banks, forcing all the actors to align *in fine* on undesirable practices in prudential terms.

The consideration of systemic risk is part of the efforts which have been made since the Larosière report to include a macroprudential dimension to the control of the European financial system. In Luxembourg, the analysis and monitoring of this risk should be carried out, in future, at the level of the entire financial centre through a systemic risk committee as provided for in draft law No 6653. Up to now, the CSSF has been fulfilling its own legal responsibilities as regards the financial stability on the basis of Article 3-2 of its statutory law of 23 December 1998. Pursuant to this article, the CSSF shall cooperate with the government, the BCL and the other national supervisory authorities “in order to contribute to ensuring financial stability” through its supervisory mission. In very concrete terms, the CSSF identifies the systemic risks at the level of the Luxembourg banking sector and decides on the measures which it considers necessary in order to manage these risks. Moreover, the CSSF participates in the implementation, at national level, of the recommendations of the ESRB where it sits as an observer and monitors, at national level, the risks identified by the ESRB (cf. item 1.1.3 above for more details). The efforts made at national level complement international initiatives. Many Luxembourg banks are part of big banking groups to which additional regulatory requirements for “global systemically important institutions” apply within the meaning of Article 131 of CRD IV. These requirements include in particular the compliance with the solvency ratios which exceed the regulatory minimum amounts defined in Article 92 of Regulation (EU) No 575/2013. The systemic risk mitigation which results therefrom has an indirect but positive impact on the financial stability of the Luxembourg subsidiaries of these groups. It should also be noted that with the implementation of the SSM, the ECB receives macroprudential prerogatives in addition to the national competences which will be assigned to the systemic risk committee in Luxembourg.

As regards excessive leverage risk, CRD IV does not, to date, provide any operational definition. Until the Basel Committee on banking supervision establishes a harmonised standard in this respect, which would then be adopted at EU level as a binding standard as from 2018, the CSSF considers that the leverage is excessive when the ratio of the regulatory capital determined in accordance with Article 72 of Regulation (EU) No 575/2013 to the total assets on the balance sheet and off-balance sheet commitments and guarantees is no more than 3%. In such a case, the CSSF analyses whether the excessive leverage represents a risk and decides, where appropriate, whether prudential measures should be applied. In accordance with the first paragraph of Article 451 of Regulation (EU) No 575/2013, banks shall publish detailed information on leverage as from 1 January 2015.

It should also be noted that the aforementioned points are still subject to implementation work at European and international level which should result in new regulatory rules or guidelines aiming to clarify their implementation. Moreover, with the implementation of the SSM, the CSSF expects the SRP to be governed

⁸ By reference to the ICAAP, the Internal Liquidity Adequacy Assessment Process (ILAAP) is the internal process which shall enable the banks to judge the adequacy of their liquidity situation (and liquidity reserves). In accordance with items 6 and 10 of Circular CSSF 09/403, this analysis is to be included in the ICAAP report following Circular CSSF 07/301.

by procedures specific to the SSM. These developments should include significant changes brought to the national SRP in the months to come.

The SRP still includes an annual review of the capital and liquidity adequacy of the financial centre's banks. On this occasion, the CSSF sets possible capital surcharges or specific liquidity requirements in addition to the quantitative requirements laid down in Regulation (EU) No 575/2013.

In July 2013, the EBA published recommendation EBA/REC/2013/03 on the preservation of Core Tier 1 capital during the transition to the CRD/CRR legal framework. The capital preservation requirement which is included therein replaces the EBA recommendation of 8 December 2011 which required big European banks to comply with a Core Tier 1 capital ratio of 9% after careful consideration of the sovereign risks. As an extension to this recommendation, the CSSF issued its general recommendation of a Core Tier 1 capital ratio of 9% for all Luxembourg banks.

As a consequence of recommendation EBA/REC/2013/03, the CSSF had to review its own prudential response which today can be broken down into two requirements: the preservation of actual own funds in accordance with Article 77 of Regulation (EU) No 575/2013 and the implementation of a capital floor, which represents an additional buffer as compared to the strict minimum provided for in the European regulations within the meaning of the two aforementioned EBA recommendations. The CSSF met the latter requirement through the anticipation, on 1 January 2014, of the capital conservation buffer which, in accordance with European regulations, is to be fully implemented in stages on 1 January 2019 at the latest. The requirement in question is laid down in Article 6 of CSSF Regulation N° 14-01 on the implementation of certain discretions of Regulation (EU) No 575/2013.

2.5. Developments regarding liquidity supervision

The overall liquidity situation in the Luxembourg banking sector may be considered as comfortable. 2013 did not experience any particular event leading to liquidity strains for banks of the financial centre.

Due to their wealth management activities and investment fund activities, most credit institutions in Luxembourg have liquidity surpluses which guarantee them a stable refinancing. This liquidity surplus is invested in securities portfolios or invested on the interbank market with counterparties which generally belong to the same group as the bank in Luxembourg. As regards the banks which, as a result of their credit activities, experience a funding gap, their liquidity shortage is covered by using resources of the group or, in the specific case of covered bond banks by the use of market-based financing. The liquidity management of Luxembourg banks thus forms widely part of that of their respective group.

The CSSF monitors the development of the liquidity situation of banks mainly through existing prudential reportings and self-assessments to be provided in the context of ICAAP reports which must include an assessment on the materiality, the management and the mitigation of the liquidity risk. In addition to this permanent supervision, the CSSF performs, in cooperation with the BCL, on-site inspections in order to assess, in a detailed manner, the situation and management of the liquidity risk within credit institutions. The seven on-site inspections carried out in 2013 show that there are still some gaps at the level of the quality of the liquidity risk management of some banks. These gaps often arise from an inaccurate consideration of the local specificities when applying, within the subsidiaries, procedures and strategies prepared and implemented at group level. Moreover, a certain lack of detail in the liquidity crisis management plans was identified.

In 2013, the regulatory framework which is the basis for the liquidity supervision remained mainly defined in four circulars: Circulars CSSF 07/301 and 13/568 which lay down the main guiding principles regarding internal governance and sound risk management, Circular CSSF 09/403 which provides for the qualitative requirements as regards sound liquidity risk management and Circular IML 93/104 which limits the structural liquidity risk by imposing a liquidity ratio (table B1.5).

With the progressive implementation of Regulation (EU) No 575/2013 as from 1 January 2014, the quantitative liquidity requirements will change significantly. Indeed, ratio B1.5 will be replaced by two liquidity ratios referred to as Liquidity Coverage Requirement (LCR) and Net Stable Funding Requirement (NSFR). Article 412(1) of the aforementioned regulation, which refers to the LCR, requires credit institutions to hold liquid assets which are adequate to face any possible short-term imbalance between liquidity inflows and

outflows under severe stress. As regards the NSFR, Article 413(1) requires banks to ensure that long-term obligations are adequately met with a diversity of stable funding instruments under both normal and stressed conditions.

The LCR will become mandatory in 2015 with a threshold set at 60%. This threshold shall be raised in stages to reach 100% as at 1 January 2018. The entry into force of the NSFR is also planned for 2018. The partial impact assessment carried out in this field by the CSSF and the BCL shows that there is today a large discrepancy as regards compliance with the future liquidity ratios. However, the liquidity situation is generally comfortable and the compliance with the standards in question is within the reach of all Luxembourg banks subject to the reinvestment of their current liquidity surplus in eligible liquid assets in accordance with Regulation (EU) No 575/2013. It should be noted that as from 2014, i.e. before the LCR and NSFR standards become binding, banks must report the calculation items of these two ratios in the form of a regular reporting which will begin on the basis of the situation on 31 March 2014.

Finally, it should be noted that CRD IV requires, as from 1 January 2014, a formal decision from the supervisory authorities as regards the adequacy of the liquidity management and liquidity buffers of credit institutions. This decision takes the form of a joint decision between the relevant supervisory authorities as regards banks with a supervisory college in accordance with Article 113(1)(b) of CRD IV.

2.6. Supervision of interest rate risk according to Circular CSSF 08/338

In Luxembourg, the diversification of the traditional banking activity, by means of private banking and investment fund services, entails that the interest rate risk is overall less marked. Moreover, the wide range of available interest rate risk hedging instruments allows efficient reduction of this risk. On the other hand, these instruments could be used to take higher interest rate risk positions.

To enable a consistent supervision of (non-trading book) interest rate risk, Circular CSSF 08/338 of 19 February 2008 on the implementation of a simulation of interest rate changes (stress test) in order to assess the interest rate risk arising from non-trading book activities requires banks to submit on a half-yearly basis the results of a stress test to the CSSF. On the basis of these results, it is possible to determine to what extent the interest rate risk is likely to result in a decline in the economic value of an institution. Article 98(5) of CRD IV confirmed the requirement of this stress test.

The CSSF analyses the results of these stress tests based on a ratio whose numerator is the result of the simulation of interest rate changes according to Circular CSSF 08/338 and whose denominator is given by the own funds defined in Article 72 of Regulation (EU) No 575/2013. This ratio measures the percentage of own funds mobilised through the (unrealised) value losses resulting from an adverse change in interest rates. According to Article 98(5) of CRD IV, the CSSF shall “take measures” when this ratio falls below -20%. Such measures aim to ensure that the own funds of an institution remain adequate with respect to its overall risk situation, which includes in particular non-trading book interest rate risk. It should be borne in mind that the non-trading book interest rate risk is not subject to a regulatory capital requirement according to Regulation (EU) No 575/2013, as opposed to trading book interest rate risk.

The analysis of the stress test results according to Circular CSSF 08/338 as at 31 December 2012 and 30 June 2013 confirmed that the Luxembourg banking sector as a whole is only moderately exposed to structural interest rate risk. Indeed, average assessment ratios amounted to -3.59% on a stand-alone basis and -4.18% on a consolidated basis as at 30 June 2013. The impact of an immediate 2%-rise in overall interest rates would cut the intrinsic value of the financial centre’s banks only by about 4.18% of their own funds.

On 30 June 2013, the structural interest rate risk, on a stand-alone basis, was essentially the same as compared to the results as at 31 December 2012 where the average ratio was -3.57%. As far as dispersion of results is concerned, 74% of the banks of the financial centre had a ratio higher than or equal to -5% and only 5% of the banks had a ratio of less than -15% as at 30 June 2013. The average assessment ratios, on a consolidated basis, amounted to -4.23% as at 31 December 2012. Moreover, the dispersion showed that 75% of the banks had a ratio above -5% and 4% of the banks had a ratio below -15% as at 30 June 2013. One single bank in the financial centre had an outlier ratio below the threshold of -20%.

In 2013, the CSSF carried out two on-site inspections on structural interest rate risk. The objective of these inspections was to verify, on-site, the accuracy of atypical results due to their volatility or their sign

(positive - counter-intuitive - impact in an interest-rate hike scenario). These controls confirmed that the calculation methods for stress tests were consistent and complied with Circular CSSF 08/338. The CSSF required that the banks in question provide, in the future, detailed explanations for each stress test when results with atypical profiles are obtained. The supervision of the non-trading book interest rate risk did not result in prudential measures.

2.7. Developments regarding operational risk supervision

As the Luxembourg financial centre is strongly involved in wealth management activities, the management of operational and compliance risks is imperative. Given this importance, in 2013, the CSSF carried out, in addition to its regular controls, four specific on-site inspections covering mainly specific aspects of operational risk management. These on-site inspections were performed, inter alia, to assess the level of consideration of the specificities of the Luxembourg subsidiaries in the operational risk management at group level, which are subsequently applied at the level of the local entity. Moreover, within the context of a credit institution's request to use the advanced measurement approach (AMA), as provided for in Article 312(2) of Regulation (EU) No 575/2013, a series of on-site inspections were carried out to assess compliance with both the qualitative and quantitative requirements imposed by the regulations. In general, during the on-site inspections, the CSSF was satisfied with the measures and controls in place. For these supervised entities, operational risk is considered to be an important risk that should not be neglected and is constantly evolving.

For the banks that have opted for the AMA approach, the CSSF insists on the active and reactive management of operational risks in Luxembourg. Beyond the application of a management model generally set by the parent undertaking, the CSSF ensures that within the Luxembourg entity, the capital allocated to operational risks is duly analysed, argued and justified as to its adequacy for the entity's operation in Luxembourg. The capital allocated to operational risks, which arises from internal management processes, pursuant to an AMA approach, should fully and accurately reflect the specific risk profile. This is true in particular for the mandatory consideration of worst-case scenarios within the AMA approaches. It is essential that these scenarios correspond to the intrinsic risks of the Luxembourg entity. More generally, the comparison of scenarios with historic losses, the extent of expected losses as well as the analysis of adequacy of scenarios with local characteristics shall enable Luxembourg banks to make judgments on the adequacy of the AMA approach implemented at local level and, in case of identified shortcomings, to strive for improvement, as required.

In all cases, the CSSF ensures that Luxembourg subsidiaries are not confined to exclusively providing data to be integrated in its group's model but seek to better understand, quantify and manage operational risks, allowing them to take the necessary measures, at local level, to mitigate or to reduce these risks.

The same principle applies to the own funds which Luxembourg banks hold on the basis of the ICAAP process as provided for in Article 73 of CRD IV. The internal capital allocated locally to operational risks, which arises from the ICAAP, should, in general, exceed the regulatory capital requirements determined on the basis of an AMA model of the group due to less risk diversification at the local level alone.

Finally, the CSSF notes that an increasing number of banks aim to integrate the AMA approach. Although the AMA method generally reduces regulatory capital, it also allows the local entities to develop their own empirical models and promotes a better identification and management of operational risks by local entities.

2.8. Cooperation with other authorities

Besides the institutionalised cooperation in colleges (cf. item 2.19. below), the CSSF works closely with the foreign supervisory authorities within the context of the consultations provided for by the European directives and in all circumstances in which cooperation is needed. Cooperation generally takes place in the form of requests for advice, information or assistance initiated or received by the CSSF. In this context, the CSSF sent 187 letters to supervisory authorities in 2013.

The CSSF also cooperates with the national judicial and law enforcement authorities in accordance with Article 2 of the law of 23 December 1998 establishing a financial sector supervisory commission (Commission de surveillance du secteur financier) and Article 9-1 of the law of 12 November 2004 on the fight against money laundering and terrorist financing. Moreover, within the context of the assessment of the professional standing

conditions to be complied with by the persons called upon to form part of the authorised management and/or the board of directors of a bank, the CSSF sent eight letters to the State Prosecutor's office of the *Tribunal d'Arrondissement* (Luxembourg District Court) and eight to the Grand-ducal police.

2.9. Intervention in the business model

One of the important lessons to be learnt from the 2008 financial crisis is that prudential supervision must not be limited to verifying compliance with regulations. Some banks had to be supported by their respective State or have their payments suspended despite their strict compliance with prudential regulations. Within the process of prudential supervision laid down in Circular CSSF 07/301, the CSSF requires banks to maintain a sound relation between their risk exposures and their capacity to bear these risks. As indicated in item 2.4. above, Article 98(1)(c) of CRD IV includes the control and assessment of the banks' business model in the scope of application of the SRP. This analysis aims to establish the viable and sustainable nature of the business model.

During 2013, the CSSF intervened 10 times (17 times in 2012) to require actions to be taken such as restricting the payment of dividends, reducing risks, setting up the maximum framework of risks, covering risks through dedicated own funds or increasing the level of own funds.

2.10. Long form reports

The long form report drawn up by the *réviseur d'entreprises* contributes to the assessment of the quality of the organisation and of the different risks of credit institutions. The CSSF requires, on a yearly basis, a long form report from every Luxembourg credit institution as well as from Luxembourg branches of non-EU credit institutions. Furthermore, the credit institutions supervised on a consolidated basis are required to submit, on a yearly basis, a consolidated long form report and individual long form reports for each subsidiary included in the consolidation and carrying out an activity of the financial sector.

The CSSF examines the individual and consolidated long form reports drawn up by the *réviseurs d'entreprises agréés* (approved statutory auditors) as well as the long form reports of Luxembourg banks' subsidiaries. It takes these conclusions into account for the overall assessment of the supervised institution's situation. The CSSF intervenes at the institution, where appropriate.

2.11. Cooperation with *réviseurs d'entreprises*

Article 54 of the law of 5 April 1993 on the financial sector governs the relationship between the CSSF and the *réviseurs d'entreprises*. All reports prepared by the *réviseur d'entreprises* in connection with the audits of accounting documents are to be communicated to the CSSF by the supervised professionals.

Furthermore, the *réviseurs d'entreprises* are required by law to promptly inform the CSSF of any serious findings, defined more specifically under Article 54(3) of the aforementioned law, which have come to their attention in the course of their duties.

The CSSF holds annual meetings with the main audit firms in order to exchange opinions on specific issues encountered at the supervised institutions. The discussions may also cover the quality of the reports produced.

2.12. On-site inspections

The yearly programme of inspections to be carried out by CSSF agents is drawn up at the beginning of the year. This programme is based on the assessment of the risk areas of the various credit institutions. On-site inspections generally follow standard inspection procedures, in the form of interviews with the people responsible, the assessment of procedures and the verification of files and systems.

Detailed explanations on on-site inspections are provided in Chapter XIII "Instruments of supervision".

2.13. Management letters

Management letters drawn up by the *réviseurs d'entreprises* for the attention of the banks' management are an important source of information on the quality of the credit institutions' organisation. The CSSF analysed these management letters in which, for instance, the external auditors listed the internal control system weaknesses identified during their audit.

2.14. Meetings

The CSSF attaches particular importance to meetings with bank managers in order to discuss the course of business as well as any other issue. It also requires prompt notification by the banks if a serious problem arises. These meetings include "structured dialogues" through which the CSSF presents the results and prudential measures arising from its assessment of the financial soundness and the risks of the different banks to the authorised bank managers.

In 2013, 218 meetings were held between CSSF's representatives and bank managers (168 in 2012). Moreover, 68 meetings with, among others, external auditors, foreign authorities, the BCL, applicants for the establishment of a bank, rating agencies or supranational organisations took place on the CSSF's premises in 2013.

2.15. Specific audits

Article 54(2) of the law of 5 April 1993 on the financial sector allows the CSSF to require a *réviseur d'entreprises* to conduct an audit on a specific subject in a given institution. In 2013, the CSSF made use of this right once, against twice in 2012.

2.16. Internal audit and compliance reports

The CSSF takes the work of the internal audit into account, when assessing the quality of the organisation and the risk management, by analysing the summary report drawn up by the internal auditor, on an annual basis, as well as the report of the Compliance officer. It requests, where relevant, specific reports from the internal audit in order to have more detailed information on certain subjects.

2.17. Supervision on a consolidated basis

As at 31 December 2013, 24 Luxembourg-incorporated banks (26 in 2012), as well as three Luxembourg-incorporated financial holding companies (*idem* in 2012) were supervised by the CSSF on a consolidated basis.

The conditions for submission to consolidated supervision, the scope, content and methods of supervision on a consolidated basis were laid down until the end of December 2013 in Chapter 3 of Part III of the law of 5 April 1993 on the financial sector. As from 1 January 2014, the procedures for implementing the prudential consolidation are specified in Chapter 2 of Title II of Part I of Regulation (EU) No 575/2013. The practical arrangements for implementing the rules governing supervision on a consolidated basis remain specified in Circular IML 96/125.

In accordance with the new European regulations, the main prudential standards and norms to be complied with by an institution or a financial holding company at a consolidated level concern:

- consolidated own funds;
- large exposure control requirements on a consolidated basis;
- arrangements concerning exposures to transferred credit risk;
- consolidated liquidity;
- consolidated leverage ratio;
- information to be published (Pillar III).

The CSSF pays particular attention to the “group head” function set up at the Luxembourg institution falling under its consolidated supervision and takes a particular interest in the way the Luxembourg parent company communicates its policies and strategies to its subsidiaries as well as in 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 available to the CSSF to exercise 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.
- Pursuant to Circular CSSF 07/301, the ICAAP report shall provide an assessment of the consolidated capital adequacy in relation to the risks taken by the group or sub-group. Part of this report concentrates on the consolidated risk profile of the group or sub-group subject to the consolidated supervision.
- Circular CSSF 12/552 on the central administration, internal governance and risk management applies to a banking group, i.e. the entire group represented by the parent undertaking and the legal entities attached thereto. Thus, the internal control functions (risk, compliance and internal audit) which are in place at group level shall also include, in their reports to be submitted annually to the CSSF, the aspects which concern more specifically consolidated entities or risks.
- The reports prepared by the external auditors represent another source of information. Circular CSSF 01/27 on practical rules regarding the mission of the *réviseur d'entreprises* requires that a consolidated long form report of a group subject to the consolidated supervision of the CSSF is drawn up. The purpose of this consolidated report is to provide the CSSF with an overview of the group's situation and to provide guidance on the risk management and structures of the group.
- The CSSF requires, moreover, an individual long form report to be drawn up for each major subsidiary.
- 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 banks and financial holding companies subject to consolidated supervision, information on any intervention of the host Member State authorities with the subsidiaries, where these interventions concern non-compliance with local regulations and organisational and risk aspects 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 holding regular meetings with the management of the credit institution or of the financial holding company under its consolidated supervision.
- The CSSF performs on-site inspections that cover, on the one hand, the manner in which the parent company establishes its policies and implements its strategies within the subsidiaries and, on the other hand, the follow-up applied to the subsidiaries.

The CSSF also analyses, in accordance with the provisions of Circular IML 96/125, application files for indirect participations from banks under its consolidated supervision.

2.18. Supplementary supervision of financial conglomerates

Chapter 3b of Part III of the law of 5 April 1993 on the financial sector requires the CSSF to carry out a supplementary supervision of financial conglomerates. A financial conglomerate is defined as 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 those financial conglomerates for which it exercises the role of coordinator of the supervision, the coordinator being the authority responsible for the coordination and the supplementary supervision of the financial conglomerate.

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

At current stage, the practical consequences of these provisions for Luxembourg credit institutions and investment firms are limited. 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.

2.19. International cooperation in matters of banking supervision: colleges of supervisors

Until the end of 2013, Articles 128 to 132 of Directive 2006/48/EC governed the cooperation between European competent authorities. Since the beginning of 2014, this cooperation, which may also extend to non-European authorities, is governed by Articles 112 to 118 of the new Directive 2013/36/EU. These articles require an intensive cooperation between the competent authorities of cross-border banking groups and strive towards a more centralised and harmonised supervision of these large cross-border groups at EU level via, among others, the establishment of colleges of supervisors for these cross-border groups.

In 2013, the CSSF organised five colleges of supervisors for the supervision of banking groups for which it exercises an ultimate consolidated supervision at European level (RBC Investor Services Ltd, State Street Bank Luxembourg S.A., KBL European Private Bankers S.A., Quilvest Wealth Management S.A., EFG Investment (Luxembourg) S.A.).

As a very large number of banking groups are present in the Luxembourg financial centre via subsidiaries which, on the one hand, are subject to the supervision of the CSSF on an individual basis, and, on the other hand, belong to the perimeter of consolidated supervision carried out by their home authorities, the CSSF participates, as host supervisor, in many colleges of supervisory authorities set up for these banking groups. In 2013, the CSSF participated in 51 meetings of colleges of supervisors (54 in 2012), among which three colleges of supervisors organised by supervisory authorities from non-EEA countries, which concerned 39 banking groups.

The establishment and functioning of the colleges are based on written agreements (Memorandum of Understanding, MoU) signed between the different authorities participating in the colleges. In 2013, the CSSF was a signatory to 45 MoUs (idem in 2012). It should be noted that not all colleges of supervisors necessarily meet physically or hold conference calls. In these cases, the tasks of the colleges of supervisors are carried out through letters or emails.

Since 2011, the EBA has contributed to promoting the establishment of colleges of supervisors and controls their effective, efficient and consistent functioning. To this end, it is a full member of the colleges.

The objectives of the colleges of supervisory authorities are mainly the Joint Risk Assessment and the Joint Capital Decision. As from 2014, the colleges will also be required to give their opinion on the adequacy of the institutions' liquidity. The college must achieve a joint assessment of the financial situation, the organisation and the risks of a banking group carrying out cross-border activities and of its individual banking subsidiaries. To that end, the different authorities which are members of the colleges provide the authority in charge of the consolidated supervision (home supervisor) with their risk assessment. The latter aggregates the information received by taking into account the entities established in its own country. Based on this Joint Risk Assessment, the college assesses the capital adequacy of the banking group and of its subsidiaries to face the incurred risks as well as its liquidity situation. The college must reach a Joint Decision on Capital and Liquidity which either confirms the adequacy or imposes capital surcharges that the banking group and/or its subsidiaries must comply with at a consolidated and/or individual level. This Joint Decision on Capital and Liquidity, which states the underlying motivations of the decision, is formally transmitted to the banking group and its subsidiaries.

Furthermore, the colleges are responsible for promoting the joint missions carried out by the authorities from different countries participating in the colleges, as well as the delegation of work between authorities.

With the implementation of the Single Supervisory Mechanism (SSM), the colleges will continue to exist because only 12% of the current supervisory colleges concern banks which are only present in SSM countries. The ECB will thus be called upon to assume the role of either the authority responsible for the consolidated supervision or the host authority for banking groups and sub-groups for which it takes over supervision. As regards the banks which will not be directly supervised by the ECB, the local authorities will continue to play their current role at the colleges. In order to improve the functioning of the colleges of supervisors, the EBA is drawing up Binding Technical Standards (BTS) on the functioning of the colleges.

2.20. Review of risk management models

In 2013, the CSSF continued its review of the risk management models⁹. In this context, a distinction should be made between the risk management models eligible for the calculation of regulatory capital requirements (Pillar 1 models) and the models which may be used for the calculation of internal capital requirements (economic capital models or Pillar 2 models).

The risk management models used for Pillar 1 purposes cover three categories of risks¹⁰, namely:

- credit risk with models relating to the internal rating systems (internal ratings-based approach – IRB approach) as well as the internal model method (IMM) for the calculation of the exposure value with respect to counterparty credit risk¹¹;
- market risk with the “internal models” to cover general and specific market risks, including the stress value-at-risk as well as incremental default and migration risks for the trading book positions of the credit institution (incremental risk charge – IRC); and
- operational risk with the advanced measurement approach (AMA).

As banks established in Luxembourg are often subsidiaries of European banking groups, the review of risk management models is carried out in close coordination between the CSSF and the home supervisory authorities of these groups in the framework of colleges of supervisors pursuant to Directive 2013/36/EU.

As regards the sharing of tasks between authorities, three different cases may arise:

- a) A local subsidiary uses a risk management model developed by the group.

In this case, the parent’s home authority reviews the model’s theoretical bases while the CSSF’s role is limited to verifying its local use. To use the models for the calculation of regulatory capital requirements, credit institutions must prove that they are actually used for internal governance and daily risk management.

The review of the local application for models relating to internal ratings-based systems mainly covers the following points: the internal governance, the representativeness of the model compared to the local population, the daily use of the models for risk management and the experience acquired during their use (use test and experience test), a sufficient overall coverage of exposures by the models, the allocation of exposures to the relevant grades and pools, stress tests and the internal model governance.

As regards operational risk management models, the CSSF’s mission mainly concerns the use of the model in the day-to-day management, the process of collecting and of reporting of operational losses, and the methodology regarding the allocation of capital requirements¹².

The findings of these missions are then communicated to the home authority and to the bank.

- b) A local subsidiary uses a risk management model developed locally.

In this case, the CSSF’s mission consists in reviewing the model’s theoretical foundations in addition to reviewing the use test described in point a) above. Thus, this mission mainly concerns the review, by the CSSF, of the bank’s internal development and validation process, of the internal governance (role of the management, risk management functions and internal audit) and of the conception and methodologies. The findings made are then communicated to the home authority and to the bank.

- c) The CSSF is the home authority of a bank that develops a risk management model.

In this case, the review process is the same as that described in points a) and b) except, of course, for the communication process with the home authority

As regards the review of the internal models for market risk, credit institutions must calculate, in accordance with Part XIV of Circular CSSF 06/273, capital requirements for a stress value-at-risk in addition to the “current” value-at-risk, and, as far as specific interest rate risk is concerned, an incremental risk charge (IRC) for default and migration risk inherent in the trading book positions.

⁹ Cf. also Chapter XIII “Instruments of supervision” for on-site inspections.

¹⁰ Cf. also item 1.7. of this chapter.

¹¹ No bank established in Luxembourg has so far submitted an application file to the CSSF in order to use the internal model method (IMM).

¹² Cf. also item 2.7. of this chapter.

Furthermore, monitoring the compliance with the qualitative and organisational requirements of credit institutions, which have already received authorisation to use the models for the calculation of the regulatory capital requirements, is an integral part of the supervisory review process (SRP) carried out by the CSSF. In this context, the CSSF is currently fine-tuning its analysis tools based on the existing periodic reporting (notably COREP and FINREP) in order to identify important developments of the risk parameters, in particular between credit institutions (comparative analysis) as well as between different reporting dates. Outliers and anomalies which are identified may lead the CSSF to request further information or to conduct specific and targeted on-site missions.

In addition to the risk management models used within the context of Pillar 1, the CSSF regularly monitors the results of the models for the calculation of internal capital. These figures form an integral part of the reporting on risk management and capital (ICAAP report) such as described in points 17 and 26 of Circular CSSF 07/301.

It is important to note that, unlike the risk management models used in the framework of Pillar 1, the models used in the framework of Pillar 2 are not subject to an explicit authorisation procedure on the part of the authorities. The purpose of the review of these models lies with the more general and less prescriptive assessment of the internal governance and the sound risk management. Thus, the review of the methodology is performed by the home authority in most cases. In the particular case of joint missions between authorities, the participation by the CSSF is usually limited to local aspects and to risk models which have a particular importance for the activities of Luxembourg subsidiaries¹³.

¹³ In most cases, those aspects deal with the definition of internal capital and with operational, reputational and liquidity risks.

CHAPTER V

SUPERVISION OF PFS



1. Investment firms
2. Specialised PFS
3. Support PFS

1. INVESTMENT FIRMS

Pursuant to Part I, Chapter 2, Section 2, Sub-section 1 of the law of 5 April 1993 on the financial sector, the professionals of the financial sector falling within the following categories are defined as investment firms:

- investment advisers (Article 24);
- brokers in financial instruments (Article 24-1);
- commission agents (Article 24-2);
- private portfolio managers (Article 24-3);
- professionals acting for their own account (Article 24-4);
- market makers (Article 24-5);
- underwriters of financial instruments (Article 24-6);
- distributors of units/shares of UCIs (Article 24-7);
- financial intermediation firms (Article 24-8);
- investment firms operating an MTF in Luxembourg (Article 24-9).

The scope of the CSSF's prudential supervision of investment firms governed by Luxembourg law includes the activities performed by these institutions in another EU/EEA Member State, both by means of a branch or under the freedom to provide services. Certain aspects of the prudential supervision, in particular compliance with the rules of conduct for the provision of investment services to clients, fall however within the jurisdiction of the supervisory authority of the host Member State¹.

Conversely, the supervision of branches set up in Luxembourg by investment firms originating from another EU/EEA Member State is performed by the home Member State authority. Nevertheless, certain specific aspects of the supervision of these branches fall within the competence of the CSSF in its capacity as host Member State authority².

Furthermore, the prudential supervision carried out by the CSSF also extends to Luxembourg branches of investment firms originating from non-EU/EEA countries.

1.1. Development of investment firms in 2013

1.1.1. Key figures

As at 31 December 2013, the 107 investment firms subject to the prudential supervision of the CSSF employed 2,560 persons in total. This figure decreased slightly compared to the previous year, but it does not necessarily reflect a loss of jobs in the financial sector, as explained in item 1.1.3. hereafter.

Investment firms showed a significant decrease in their net profit, which fell from EUR 319.4 million as at 31 December 2012 to EUR 157.3 million as at 31 December 2013. The balance sheet total of all investment firms also recorded declining figures and amounted to EUR 3,092 million as at 31 December 2013 as against EUR 3,616 million as at 31 December 2012.

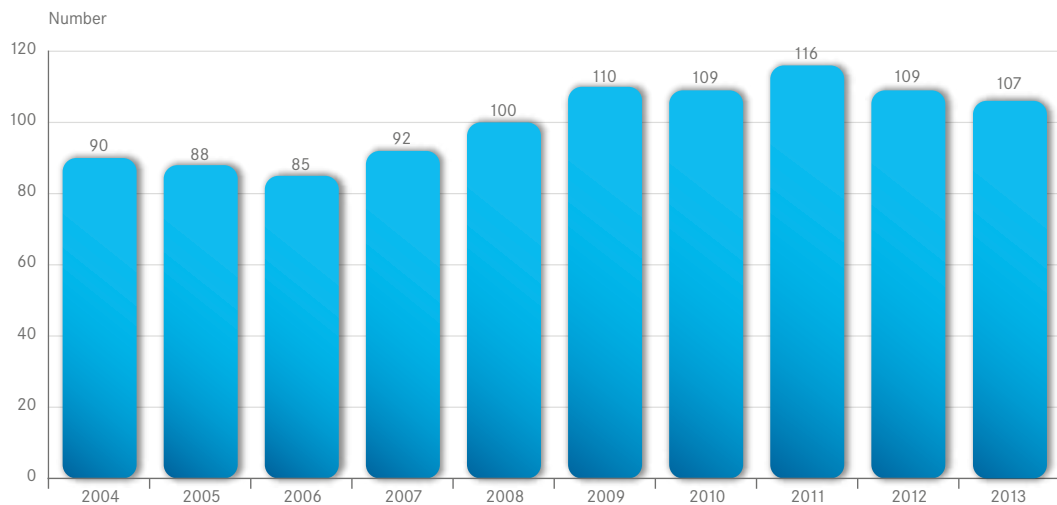
1.1.2. Development in the number of investment firms

The declining trend in the number of investment firms which had begun in 2012 continued in 2013, at a slower pace though. Indeed, the number of investment firms subject to the supervision of the CSSF decreased from 109 entities as at 31 December 2012 to 107 entities at the end of 2013. The number of entities which have been granted an authorisation as investment firm in 2013 decreased slightly compared to the previous year (six new entities in 2013 as against eight in 2012). Eight entities abandoned their investment firm status during the year under review compared to 15 in 2012.

¹ In accordance with the law of 13 July 2007 on markets in financial instruments transposing the MiFID into Luxembourg law.

² Cf. footnote No. 1 above.

Development in the number of investment firms



Among the investment firms, the activity of private portfolio manager was found most widely with 79 entities authorised in this respect as at 31 December 2013. It should be noted that half of the new entities registered on the official list adopted the status of private portfolio manager.

The following six investment firms were registered on the official list in 2013:

- Arche Wealth Management S.A.
- ECP International S.A.
- FinDeal Advisers S.A.
- Global Asset Advisors & Management S.A.
- Instituut voor Beleggingsstrategie B.V. Luxembourg Branch
- Oddo Services Luxembourg S.A.

The following eight entities abandoned their status of investment firm in 2013:

- a) change or cessation of activities, so that the entity no longer required an authorisation as investment firm, because it no longer fell within the scope of the law of 5 April 1993 on the financial sector (two entities):
 - Greenleaf Financial Luxembourg S.A.
 - Valbay International S.A.
- b) judicial winding-up (one entity)
 - H CTG S.A.³
- c) transformation into a management company under Chapter 15 of the law of 17 December 2010 relating to undertakings for collective investment (four entities):
 - Carmignac Gestion Luxembourg
 - Franklin Templeton International Services S.A.
 - Notz, Stucki Europe S.A.
 - GBP Asset Management S.A.
- d) closing of the branch Eiger Securities LLP, Luxembourg Branch, originating from the United Kingdom.

³ Upon having ordered the suspension of payments of H CTG S.A. on 20 March 2013 (lodged by the institution itself), the Luxembourg district court (*Tribunal d'arrondissement*) sitting in commercial matters, ordered the dissolution and judicial liquidation of H CTG S.A. on 30 April 2013.

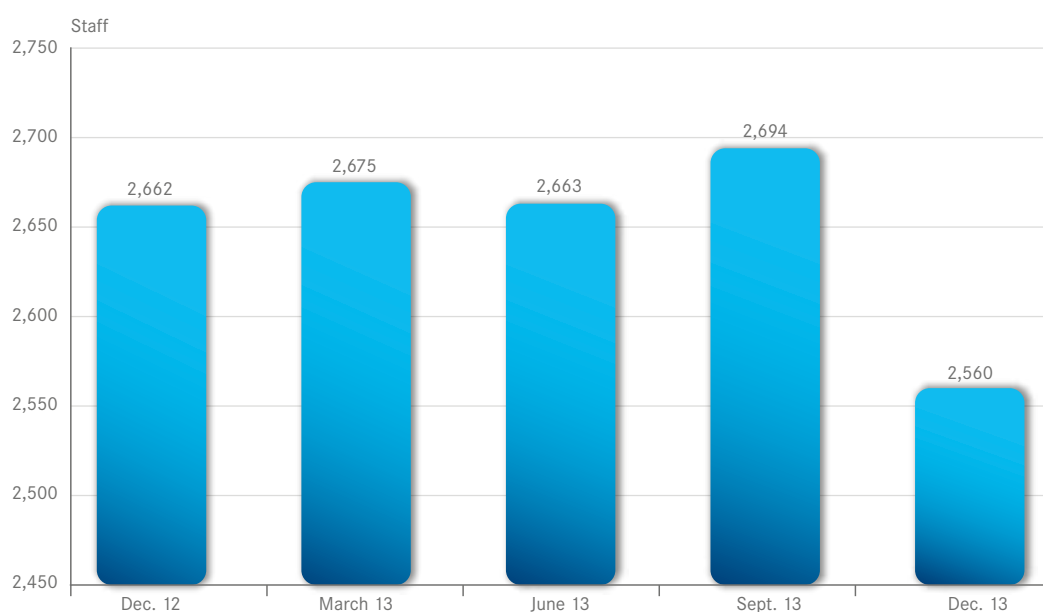
1.1.3. Development in employment

Employment in all investment firms amounted to 2,560 persons as at 31 December 2013 as against 2,662 persons at the end of December 2012, which represents a decrease of 102 jobs, equivalent to -3.8% over one year. This decrease mainly reflects transfers of activities which, however, had no impact on the aggregate number of jobs in the financial sector, but only changed the breakdown among the entities of the financial sector, as set forth below.

Employment in investment firms

Year	Number of investment firms	Total staff
2010	109	2,358
2011	116	2,411
2012	109	2,662
2013	107	2,560 ⁴

Quarterly development in employment



During the first three quarters of 2013, employment in investment firms remained relatively stable, shifting from 2,662 persons as at 31 December 2012 to 2,675 as at 31 March 2013, to 2,663 persons as at 30 June 2013 and to 2,694 persons as at 30 September 2013.

The last quarter was characterised by a decrease in the total employment, falling from 2,694 persons as at 30 September 2013 to 2,560 persons as at 31 December 2013. The transformation of three investment firms with a high number of employees into management companies under Chapter 15 of the law of 17 December 2010 relating to undertakings for collective investment during the last months of the year 2013 was the main reason for the decline in the employment figures of investment firms. Thus, these transfers of activities do not impact the employment in the financial sector as a whole, but only affect the breakdown between the different categories of financial players. In the last quarter of 2013, some slight variations in the number of employees of a limited number of investment firms allowed to partially compensate the decrease in employment linked to the above mentioned status changes.

It should also be noted that, as at 31 December 2013, about half the investment firms had eight or less employees.

⁴ Preliminary figures.

1.1.4. Development of balance sheets and profit and loss accounts

The provisional balance sheet total of all investment firms established in Luxembourg reached EUR 3,092 million⁵ as at 31 December 2013, against EUR 3,616 million as at 31 December 2012, i.e. a decrease of 14.4%. This decrease was mainly linked to the transformation into management companies (under Chapter 15 of the law of 17 December 2010 relating to undertakings for collective investment) of two investment firms with significant balance sheet totals. The considerable growth of the balance sheet of one financial player which had been authorised in 2010 compensated this negative trend only slightly.

Investment firms also recorded a negative development in their net results. Indeed, provisional net results amounted to EUR 157.3 million⁶ as at 31 December 2013, against EUR 319.4 million as at 31 December 2012, representing a substantial fall of 50.7% over a year. These figures have been heavily affected by two major players which converted into management companies in 2013. The majority of investment firms do nevertheless show a stable net result as compared to the previous year, or even slight increases for some of them. It should also be noted that a little less than one third of the investment firms, including notably the entities authorised during the last three years, registered negative results as at 31 December 2013.

Development of the balance sheet total and of the net results of investment firms

<i>(in million EUR)</i>	2012	2013	Variation en %
Balance sheet total	3,616	3,092	-14.4%
Net results	319.4	157.3	-50.7%

1.1.5. International expansion of investment firms

• Subsidiaries created and acquired abroad during 2013

In 2013, one Luxembourg investment firm opened a subsidiary in Switzerland.

• Freedom of establishment

In 2013, three branches have been established in other EU/EEA Member States by investment firms incorporated under Luxembourg law and three branches have been closed. Moreover, following the transformation of three investment firms into management companies in 2013, their four branches are no longer registered on the list of investment firm branches incorporated under Luxembourg law established in one or more EU/EEA countries at the end of 2013. The total number of branches of Luxembourg investment firms in other EU/EEA Member States amounted to 29 entities at the end of the year, compared to 33 entities as at 31 December 2012.

Following the opening of a branch originating from the Netherlands and the closing of a branch originating from the United Kingdom in 2013, the number of branches established in Luxembourg by investment firms originating from another EU/EEA Member State did not change and remained at 10 entities as at 31 December 2013.

⁵ The figures of the branches established in Luxembourg by investment firms originating from another EU/EEA Member State and included since 2009 in the total number of investment firms are not included in these figures.

⁶ Cf. footnote No. 5 above.

Branches established in the EU/EEA as at 31 December 2013

Country	Branches of Luxembourg investment firms established in the EU/EEA	Branches of EU/EEA investment firms established in Luxembourg
Austria	3	1
Belgium	10	-
France	3	-
Germany	4	-
Italy	2	-
Netherlands	1	1
Spain	2	-
Sweden	2	1
United Kingdom	2	7
Total	29	10

As regards non-EU/EEA countries, one investment firm incorporated under Luxembourg law is represented by a branch in Switzerland.

- **Free provision of services**

In 2013, 15 investment firms incorporated under Luxembourg law applied to pursue business in one or several EU/EEA Member States by way of free provision of services. The total number of investment firms which are active in one or more EU/EEA countries following a notification amounted to 71 entities as at 31 December 2013 (same figure as in 2012). The majority of the investment firms concerned carried out their activities in several EU/EEA countries by way of free provision of services.

The target countries of investment firms incorporated under Luxembourg law, whose total number of notifications amounted to 540 units as at 31 December 2013, are mainly Luxembourg's neighbouring countries (Belgium, France and Germany). Luxembourg investment firms also show major interest in the Netherlands, the United Kingdom, Italy and Spain.

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 2,601 entities at the end of 2013 (against 2,447 entities as at 31 December 2012).

The geographical breakdown of EU/EEA investment firms operating 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 304 new notifications for free provision of services on the Luxembourg territory received in 2013 (slightly increasing number as compared to the 292 new notifications in 2012), those originating from the United Kingdom represented a large majority. Apart from the United Kingdom, the significant upward trend observed for Cyprus since 2010 was once again confirmed in 2013 with 22 new entities. Moreover, entities of countries close to Luxembourg like Germany, France and also the Netherlands show ongoing interest in exercising their activities in Luxembourg by way of free provision of services.

As at 31 December 2013, 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	21	25
Belgium	53	14
Bulgaria	9	5
Croatia	2	-
Cyprus	12	101
Czech Republic	12	2
Denmark	20	29
Estonia	9	1
Finland	17	8
France	44	90
Germany	41	142
Gibraltar	-	13
Greece	12	7
Hungary	13	2
Iceland	5	-
Ireland	13	54
Italy	30	7
Latvia	10	1
Liechtenstein	6	21
Lithuania	10	1
Malta	12	9
Netherlands	32	112
Norway	14	29
Poland	15	2
Portugal	17	4
Romania	9	3
Slovakia	11	2
Slovenia	11	2
Spain	28	22
Sweden	23	12
United Kingdom	29	1,881
Total number of notifications	540	2,601
Total number of investment firms concerned	71	2,601

1.2. Prudential supervisory practice

1.2.1. Instruments of prudential supervision

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

- financial information submitted periodically to the CSSF enabling it to continuously monitor the activities of investment firms and the inherent risks, and the periodic control of the capital adequacy ratio and large exposure limits as laid down in Article 56 of the law of 5 April 1993 on the financial sector;

- the documents established yearly by the *réviseur d'entreprises agréé* (statutory auditor): the audit report and audited annual accounts, the long form report and, where applicable, the management letter;
- the internal audit reports relating to the audits carried out during the year, the compliance confirmation signed by all the members of the authorised management as provided for in point 61 of Circular CSSF 12/552 (as amended by Circular CSSF 13/563), the summary report of the Compliance function, the summary report of the risk management function as well as the authorised management's report on the implementation of the internal capital adequacy assessment process (ICAAP)⁷;
- the introductory visits and on-site inspections carried out by the CSSF.

1.2.2. Compliance with the quantitative standards by investment firms

• Capital base

In accordance with Articles 24 to 24-9 of the law of 5 April 1993 on the financial sector, the authorisation of investment firms is subject to the production of evidence showing the existence of minimal capital base. This capital base consisting of a subscribed and paid-up capital, share premiums, legally formed reserves and profits brought forward, after deduction of possible losses for the current financial year, shall be permanently available to the investment firm and invested in its own interest.

Based on the financial data that the investment firms shall provide to the CSSF on a monthly basis in accordance with Circular CSSF 05/187, the CSSF verifies particularly the compliance of investment firms with the minimal capital base conditions. In 2013, the CSSF intervened at seven investment firms for non-compliance with the legal provisions relating to capital base.

In this context, the CSSF reminds that subordinated loans or the profits for the current financial year shall not be taken into account for the determination of the minimum capital base of a professional of the financial sector⁸.

• Capital adequacy ratio

Investment firms falling under the scope of Circular CSSF 07/290 (as amended by Circulars CSSF 10/451, 10/483, 10/497 and 13/568) defining the capital ratios pursuant to Article 56 of the law of 5 April 1993 on the financial sector shall permanently have eligible own funds at least equal to the global capital requirement.

During 2013, the CSSF recorded 11 cases of non-compliance with the capital adequacy ratio. Most investment firms concerned already regularised the situation of non-compliance or are in the process of being regularised shortly. The CSSF attaches particular importance to compliance with the structural ratios that investment firms are required to observe in compliance with Article 56 of the law on the financial sector and closely monitors the regularisation processes undertaken by investment firms in case of solvency ratio deficiency.

• Large exposures limits

In the context of the supervision of compliance with the large exposures limits⁹, the CSSF took action in relation to two investment firms which exceeded the limit of 25% of own funds, as defined in point 7, Part XVI of Circular CSSF 07/290 on the definition of capital ratios pursuant to Article 56 of the law of 5 April 1993 on the financial sector.

1.2.3. Meetings

During the year under review, a total of 78 meetings in relation to investment firms activities took place on the CSSF's premises. In the context of a closer dialogue, the CSSF attaches particular importance to these meetings with the financial players subject to its supervision.

⁷ This ICAAP report shall be established by the investment firms falling within the scope of Circular CSSF 07/290 defining capital ratios pursuant to Article 56 of the law of 5 April 1993 on the financial sector.

⁸ Pursuant to Article 20(5) of the law of 5 April 1993 on the financial sector.

⁹ Pursuant to Circular CSSF 07/290 as amended by Circular CSSF 10/483, investment firms whose authorisation does not allow either the dealing on own account or the underwriting of financial instruments and/or the placing of financial instruments on a firm commitment no longer fall within the scope of the regulations governing large exposures since 31 December 2010.

The meetings with investment firm representatives covered the following areas:

- information requests on the qualification of the activities performed (scope of the law of 5 April 1993 on the financial sector);
- new requests for authorisation;
- initial meetings with the persons in charge of the newly authorised investment firms in order to deal with the practical aspect of ongoing supervision;
- changes to the authorisation of active investment firms (activity, acquisition of subsidiaries, legal form, etc.);
- planned changes notably relating to the shareholding structure, day-to-day management and internal control;
- discussions concerning problems or specific points noticed in the framework of the prudential supervision exercised by the CSSF;
- information requests in the context of prudential supervision;
- presentation of the general context and activities of the companies concerned;
- courtesy visits.

1.2.4. Specific controls

Article 54(2) of the law of 5 April 1993 on the financial sector entitles the CSSF to require a *réviseur d'entreprises agréé* 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 formally made use of this right once in 2013.

1.2.5. 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 and in particular by Chapter 3a of Part III. The relevant articles define the conditions governing the supervision 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 within the scope of application of the above-mentioned law. An in-depth study of the financial groups to which most investment firms belong is required in order to determine whether or not, 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.

As at 31 December 2013, the following 11 investment firms were submitted to the supervision on a consolidated basis by the CSSF:

- Allfunds International S.A.
- CapitalatWork Foyer Group S.A.
- CBRE Global Investors Luxembourg S.à r.l.
- Crédit Agricole Luxembourg Conseil S.A., in abbreviated form CAL Conseil
- European Value Partners S.A.
- FIL (Luxembourg) S.A.
- Fuchs & Associés Finance S.A.
- Fund Channel S.A.
- Hottinger & Cie Groupe Financière Hottinguer Société Anonyme
- Petercam (Luxembourg) S.A.
- Ycap Asset Management (Europe)¹⁰

¹⁰ Consolidated supervision by the CSSF on the parent financial holding company in Luxembourg.

2. SPECIALISED PFS

Pursuant to Part I, Chapter 2, Section 2, Sub-section 2 of the law of 5 April 1993 on the financial sector, the professionals of the financial sector falling within the following categories are defined as specialised PFS:

- registrar agents (Article 25);
- professional depositaries of financial instruments (Article 26);
- professional depositaries of assets other than financial instruments (Article 26-1);
- operators of a regulated market authorised in Luxembourg (Article 27);
- currency exchange dealers (Article 28-2);
- debt recovery (Article 28-3);
- professionals performing lending operations (Article 28-4);
- professionals performing securities lending (Article 28-5);
- Family Offices (Article 28-6);
- mutual savings fund administrators (Article 28-7);
- management companies of non-coordinated UCIs (Article 28-8);
- corporate domiciliation agents (Article 28-9);
- professionals providing company incorporation and management services (Article 28-10);
- professionals of the financial sector authorised to exercise any activity referred to in Part I, Chapter 2, Section 1 of the law of 5 April 1993 on the financial sector, with the exception of the categories of PFS also referred to in Section 2 of the same chapter (Article 13);
- establishments authorised to exercise all the PFS activities permitted by Article 1 of the law of 15 December 2000 on postal financial services.

The prudential supervision of the CSSF extends to specialised PFS incorporated under Luxembourg law, including the activities which they carry out by means of a branch, and to Luxembourg branches of entities originating from abroad.

2.1. Development of specialised PFS in 2013

2.1.1. Major events in 2013

• Development in the legal framework

The law of 12 July 2013 on alternative investment fund managers (AIFM Law) transposing Directive 2011/61/EU of 8 June 2011 on Alternative Investment Fund Managers, introduces into the law of 5 April 1993 on the financial sector a new Article 26-1, creating the status of professional depositary of assets other than financial instruments as a new specialised PFS category. As regards this new PFS category, the depositary activity is limited to the assets of certain types of investment funds, listed exhaustively in Article 26-1, for which different conditions concerning the duration of the fund and its investment policy have to be complied with.

As far as the status of management companies of non-coordinated UCIs is concerned, the AIFM Law completed Article 28-8 of the law of 5 April 1993 on the financial sector, by specifying that the professionals authorised under this status and exercising before 22 July 2013 the activity of alternative investment fund manager within the meaning of Directive 2011/61/EU shall have time to comply with the AIFM Law until 22 July 2014, notably by requesting, where applicable, an authorisation as AIFM within the meaning of that law.

Finally, the AIFM Law specifies in Chapter 13 “Repealing and final provisions” that Article 28-8 of the law of 5 April 1993 on the financial sector shall be repealed with effect from 22 July 2014.

As concerns the authorisation procedure in order to be granted the status of professional depositary of assets other than financial instruments, the CSSF developed a specific questionnaire in order to evaluate whether the applicant fulfils all the legal conditions deriving from the law of 5 April 1993 on the financial sector and the AIFM Law. This questionnaire may be downloaded from the CSSF website.

• Key figures

The sector of specialised PFS experienced an overall positive year 2013.

Thus, as at 31 December 2013, 126 specialised PFS were subject to the prudential supervision of the CSSF. They employed a total of 3,201 persons, which is slightly more than in the previous year but this increase does not fully correspond to a net creation of new employments as explained under item 2.1.3. below.

The balance sheet total of all specialised PFS amounted to EUR 10,875 million as at 31 December 2013 as against EUR 9,457 million as at 31 December 2012. The aggregate net results decreased from EUR 360.1 million as at 31 December 2012 to EUR 219.3 million as at 31 December 2013.

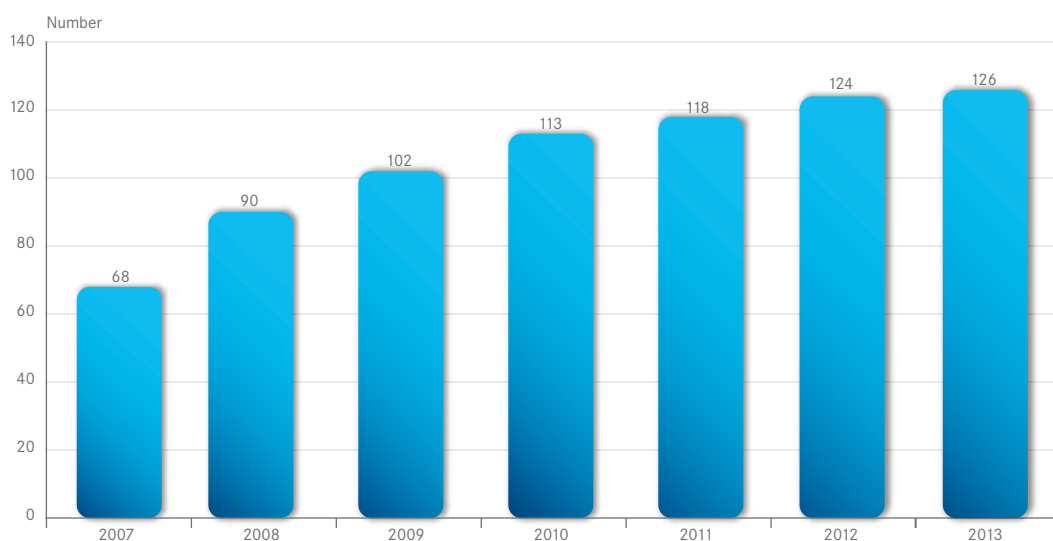
2.1.2. Development in the number of specialised PFS

The upward trend in the number of specialised PFS that had been recorded over the last few years continued, but at a slower pace than in the last two years. Thus, the number of specialised PFS rose from 124 entities as at the end of 2012 to 126 entities as at 31 December 2013.

The number of entities which received an authorisation as specialised PFS in 2013 slightly decreased compared to the previous year (seven new entities in 2013 against 10 in 2012). One support PFS extended its scope of activity by adding the statuses of corporate domiciliation agent and professional providing company incorporation and management services.

Six entities abandoned their specialised PFS status during the year under review against four in 2012.

Development in the number of specialised PFS



Among all specialised PFS, the corporate domiciliation agent activity is the most widespread with 94 entities authorised under this status as at 31 December 2013, followed by the registrar agent activity which can be automatically cumulated with the activities of administrative agent of the financial sector and client communication agent.

The following seven entities were registered on the official list of specialised PFS in 2013:

- Arche Family Office S.A.
- IF-Fund Services S.A.
- MDO Services
- ME Business Solutions S.à r.l.
- Ogier Fiduciary Services (Luxembourg) S.à r.l.
- RSM Financial Services Luxembourg S.A.
- SS&C Globeop (Luxembourg)

Five of them have, among others, requested the status of corporate domiciliation agent.

The following six entities abandoned their status of specialised PFS in 2013:

- Companies & Trusts Promotion S.A. Voluntary renunciation of the PFS authorisation; continuation of corporate domiciliation agent activities under the status of chartered accountant and member registered with the OEC.
- Fidugia S.A. Voluntary renunciation of the PFS authorisation; change of corporate purpose.
- Kinetic Partners (Luxembourg) S.à r.l. Transformation into a management company under Chapter 15 of the law of 17 December 2010 relating to undertakings for collective investment.
- MDO Services S.A. Abandonment of status following a demerger-merger.
- Vectis PSF S.A. Voluntary renunciation of the PFS authorisation; change of corporate purpose.
- Trust Alliance Luxembourg S.A. Voluntary winding-up.

2.1.3. Development in employment

During 2013, the number of people employed by all specialised PFS rose by 155 units, representing an increase of 5% as compared to the end of 2012.

Employment in specialised PFS

Year	Number of specialised PFS	Total staff
2010	113	3,552
2011	118	3,127
2012	124	3,046
2013	126	3,201 ¹¹

In relation to the decreases recorded in the number of people employed in 2011 and 2012, it should be borne in mind that these contractions were linked to two major financial players: the first one merged with a bank and the second one changed its status to be authorised as an investment firm. Since then, the staff of these two entities has been taken over in the statistics relating to banking employment and investment firm employment. These restructurings did thus not impact the employment figures in the financial sector taken as a whole, but only affected the breakdown between the different categories of financial players.

Similarly, the increase in employment figures registered during 2013 partly results from the transfer of activities and personnel of a bank to a specialised PSF. The seven entities authorised in 2013 contributed by one third to the total increase in employment.

¹¹ Preliminary figures.

According to the figures as at 31 December 2013, nine specialised PFS employed more than 100 people and half of the specialised PFS employed 10 or less people.

2.1.4. Development of balance sheets and profit and loss accounts

The provisional balance sheet total of all specialised PFS established in Luxembourg reached EUR 10,875 million as at 31 December 2013, as against EUR 9,457 million as at 31 December 2012, i.e. an increase of EUR 1,418 million (+14.99%). This positive trend is mainly linked to the increase in the volume of activities developed by some important financial players authorised as professionals performing lending operations and professionals performing securities lending.

Over one year, the specialised PFS recorded a drop in their net results. Indeed, the provisional net results amounted to EUR 219.3 million as at 31 December 2013 as against EUR 360.1 million as at 31 December 2012, representing a decrease by EUR 140.8 million (-39.10%). This decrease is attributable for 90% to one major entity. Except for the development of this particular entity, most specialised PFS show a net result which increased as compared to last year.

2.1.5. International expansion of specialised PFS

As at 31 December 2013, two specialised PFS (idem in 2012) were represented by means of branches abroad, one in the United Kingdom and the other one in Switzerland.

Six specialised PFS have one or more subsidiaries outside Luxembourg.

2.2. Prudential supervisory practice

2.2.1. Instruments of prudential supervision

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

- financial information submitted periodically to the CSSF enabling it to continuously monitor the activities of the supervised entities and the inherent risks, in addition to the monthly control of compliance with the minimum own funds requirement;
- the documents established yearly by the *réviseur d'entreprises agréé*, including the audit report and audited annual accounts, the control report relating to the fight against money laundering and terrorist financing and, where applicable, the management letter;
- the internal audit reports relating to the audits carried out during the year and the management's report on the state of the internal audit of the specialised PFS;
- the introductory visits and on-site inspections carried out by the CSSF.

2.2.2. Compliance with the quantitative and qualitative standards by specialised PFS

• Capital base

In accordance with Article 20 and Articles 25 to 28-10 of the law of 5 April 1993 on the financial sector, the authorisation of specialised PFS is subject to the production of evidence showing the existence of minimum capital base.

The concept of capital base includes the own assets of a specialised PFS authorised as a natural person as well as the own funds of a specialised PFS established as a legal person.

Own funds within the meaning of the law of 5 April 1993 on the financial sector shall mean: the subscribed and paid-up share capital, share premiums, legally formed reserves and profits brought forward after deduction of

possible losses for the current financial year. Subordinated loans or the profits for the current financial year shall not be taken into account for the determination of the own funds of a PFS.

Pursuant to Article 20(4) of the above mentioned law, own funds must be available to the PFS permanently and invested in its own interest. In this context, the CSSF specifies that the legislator indicated in the comment to that article that “(...) the first requirement aims at ensuring that the capital base is not invested in participations nor blocked for credits granted. The second requirement aims at ensuring that the capital base is used in the interest of the PFS and of its clients and not in the interest of its shareholder or its group”.

The CSSF points out that the funds invested in a participation shall be deducted from the capital base of the PFS, where applicable.

If the own funds (legal person) or the own assets (natural person) become less than the minimum legal requirement, the CSSF may, where the circumstances so warrant, grant a time-limit within which the PFS shall regularise its situation or cease its business.

Based on the financial data that the specialised PFS shall provide to the CSSF on a monthly basis in accordance with Circular CSSF 05/187, the CSSF verifies compliance with the minimum capital base condition. During 2013, the CSSF recorded 14 cases of non-compliance with the legal provisions relating to own funds. The CSSF had to urge three of these entities several times to obtain a satisfactory regularisation of the situation.

• Compliance of the day-to-day management

For the purpose of assessing the day-to-day management of specialised PFS, the CSSF bases its opinion on all the information which it receives in the context of the prudential supervision of the entity, including in particular the authorisation requests relating to the members of the corporate bodies, the reports and information transmitted in the context of the year-end closing documents (including, among others, the management letters and similar reports issued by the *réviseurs d'entreprises agréés* and the internal auditors) and the information gathered during the introductory visits and on-site inspections carried out by the CSSF.

Following the analysis of this information and depending on the seriousness of the problem identified, the CSSF's reaction may vary from the mere follow-up of the problem over the drawing-up of deficiency letters up to the convening of the management or a specific on-site inspection.

In 2013, the CSSF intervened 13 times, either by way of deficiency letters or by means of an injunction letter due to non-compliance as regards the day-to-day management of specialised PFS.

In this context, the CSSF wishes to remind that, pursuant to Article 19 of the law of 5 April 1993 on the financial sector, the day-to-day management of a PFS must be carried out by at least two persons and those persons must be empowered to effectively direct the business of the PFS. This two-man management principle allows mutual control and common decision-taking, but it does not necessarily imply that these two persons must act together to commit the PFS. The persons in charge of the day-to-day management of a PFS are thus jointly and directly responsible for all the activities exercised by a PFS despite their respective powers of signature. However, in practice, this does not prevent each manager to focus more specifically on one particular business area.

The persons in charge of the day-to-day management must be permanently based at the PFS's registered office. However, the CSSF accepts that during the start-up phase (i.e. during the first six months after the issuance of the ministerial authorisation), one of these persons does not reside in Luxembourg or that s/he is employed on a part-time basis.

2.2.3. Meetings

The CSSF attaches particular importance to meetings with the managers of specialised PFS in order to discuss the context of an application file for authorisation, the state of business, upcoming amendments to the shareholding structure or internal organisation, new ongoing projects and any serious issues that arise.

During the year under review, 39 meetings were held (40 in 2012) with representatives of specialised PFS. They covered the following areas:

- presentation of application files for authorisation as specialised PFS;
- initial meetings with the persons in charge of the newly authorised specialised PFS in order to deal with the practical aspect of ongoing supervision;
- changes in the authorisation of active PFS (takeover of business portfolio, acquisition of subsidiaries, legal form, etc.);
- planned changes relating notably to the shareholding structure, day-to-day management and internal control;
- problems or specific points identified in the framework of the prudential supervision exercised by the CSSF;
- information requests in the context of prudential supervision;
- presentation of the general context and activities of the entities concerned;
- courtesy visits.

2.2.4. Specific controls

Article 54(2) of the law of 5 April 1993 on the financial sector entitles the CSSF to require a *réviseur d'entreprises agréé* 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.

In 2013, the CSSF did not make use of this right with any specialised PFS.

3. SUPPORT PFS

Pursuant to Part I, Chapter 2, Section 2, Sub-section 3 of the law of 5 April 1993 on the financial sector, the professionals of the financial sector falling within the following categories are defined as support PFS:

- client communication agents - ACC (Article 29-1);
- administrative agents of the financial sector - AA (Article 29-2);
- primary IT systems operators of the financial sector - OSIP (Article 29-3);
- secondary IT systems and communication networks operators of the financial sector - OSIS (Article 29-4).

One characteristic of support PFS is that they do not as such exercise a financial activity themselves, but act as subcontractors of operational functions on behalf of other financial professionals.

3.1. Development in the number of support PFS

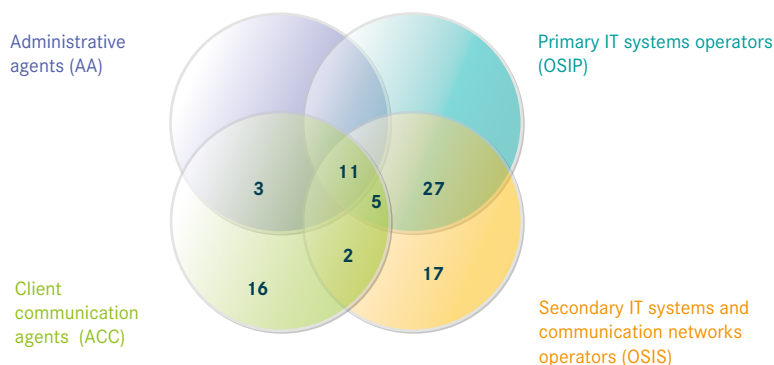
In 2013, the total number of support PFS, for the second time since the creation of the status and for the second consecutive year, has slightly decreased from 85 entities as at 31 December 2012 to 81 entities as at 31 December 2013.

Six new support PFS received an authorisation in 2013:

- one client communication agent of the financial sector (ACC);
- five secondary IT systems and communication networks operators of the financial sector (OSIS).

Nine support PFS were deregistered from the official list in 2013, seven of which after ceasing their activities over the year and two due to mergers within the group. One support PFS has obtained an additional authorisation as broker in financial instruments during the year. This entity is henceforth supervised as an investment firm and is therefore no longer registered as a support PFS.

As at 31 December 2013, the 81 support PFS broke down as follows:



One of the entities, authorised for the four support PFS activities, is additionally authorised to perform the activities of corporate domiciliation agent (Article 28-9) and professional providing company incorporation and management services (Article 28-10).

It should be noted that administrative agents are *ipso jure* authorised to exercise the activities of client communication agents. As a result, no entity has only the status of administrative agent. The same applies to primary IT systems operators which are *ipso jure* authorised to carry out the activities of secondary IT systems and communication networks operators of the financial sector.

3.2. Development in support PFS employment

The number of staff of support PFS declined from 9,016 persons as at 31 December 2012 (85 active entities) to 8,971 persons as at 31 December 2013 (81 active entities), representing an annual decrease of 45 positions (-0.50%).

Leaving aside the support PFS which received authorisation in 2013 and those which abandoned or relinquished their authorisation over the year, the recorded decrease concerned 83 positions which means on average one person leaving per support PFS in 2013.

Employment in support PFS

	2012			2013			Variation
	Luxembourg	Foreigners	Total	Luxembourg	Foreigners	Total	
Executives	123	462	585	131	455	586	0.17%
Employees	1,038	7,393	8,431	1,065	7,320	8,385	-0.55%
<i>of which part-time</i>	80	769	849	79	771	850	0.12%
TOTAL	1,161	7,855	9,016	1,196	7,775	8,971	-0.50%
<i>of whom men</i>	951	6,107	7,058	984	6,083	7,067	0.13%
<i>of whom women</i>	210	1,748	1,958	212	1,692	1,904	-2.76%

3.3. Development of balance sheets and profit and loss accounts

The balance sheet total of all support PFS established in Luxembourg reached EUR 1,085.3 million as at 31 December 2013 as against EUR 1,007.2 million as at 31 December 2012, i.e. an increase of 7.75%.

Over one year, support PFS also increased their net results which rose from EUR 35.8 million as at 31 December 2012 to EUR 42.9 million as at 31 December 2013 (+19.83%).

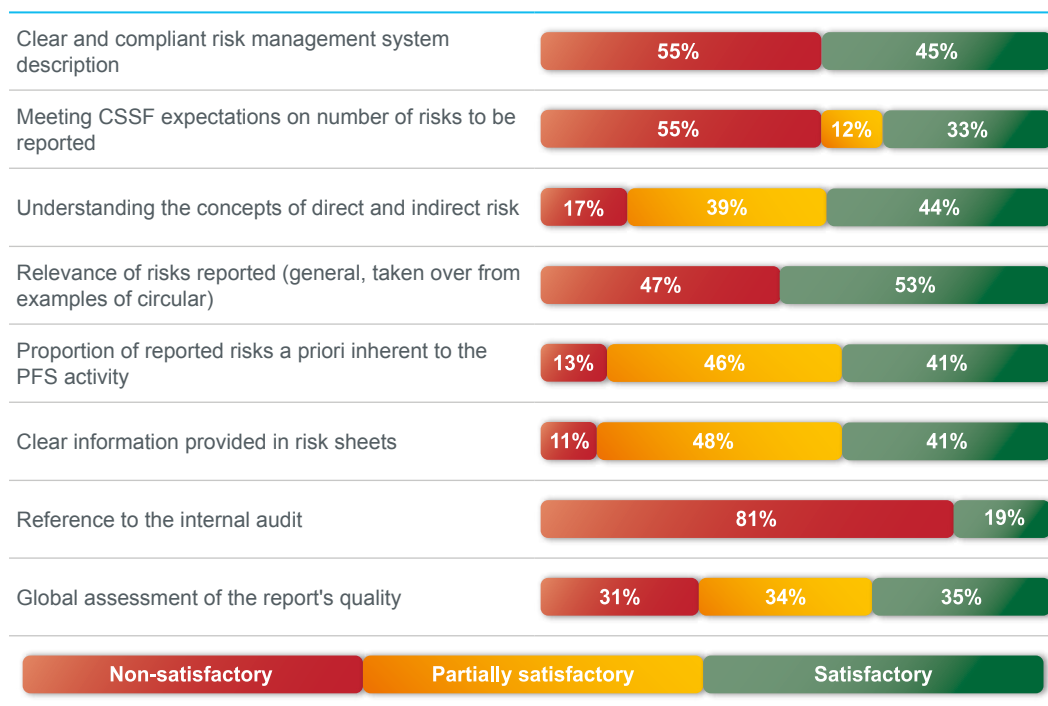
3.4. Preliminary examination of the risk assessment reports and descriptive reports

This examination concerns the 75 risk assessment reports (“RARs”) received and analysed (fully or in part). The difference between the 81 support PFS registered on the official list as at 31 December 2013 and the 75 RARs received is due to six support PFS which had not yet been authorised on the publication date of Circular CSSF 12/544 and were thus not subject to the obligation to provide an RAR for 2013.

The descriptive reports (“DRs”) have been dealt with principally in the section relating to compliance with deadlines. The sample covers 72 DRs received.

It should also be noted that the below comments concern mainly compliance with the structure set out in Circular CSSF 12/544. Indeed, the circular lists a number of items to be covered in the RAR and a specific structure to comply with, in particular as concerns the risk sheet. In this context, the CSSF came to the conclusion that improvements have to be made on a certain number of items in the coming years.

Aggregate results of RAR analysis



3.4.1. Compliance with deadlines

The vast majority of support PFS met the RAR submission deadlines. Thus, 77% of the support PFS (i.e. 58 RARs) complied with the initial deadline. Among the 23% (i.e. 17 RARs) which did not respect the initial deadline, 47% (i.e. 8 RARs) requested a derogation and 53% (i.e. 9 RARs) did not.

As far as the submission of DRs is concerned, 71% of the support PFS met the deadline (representing 51 DRs) whereas 29% (i.e. 21 DRs) did not respect the initial deadline. Among the latter, only 62% (i.e. 13 DRs) requested and were granted an extended deadline and 38% (i.e. 8 DRs) did not request any extension.

3.4.2. RAR analysis

In its general principles which refer to both RAR and DR, Circular CSSF 12/544 requires the management to be responsible for the truthfulness of all the elements included in these two reports by having the reports signed by all the members of the authorised management. It is important to note that this point has often not been considered.

a) Description of the risk management system

As regards the description of the risk management system, Circular CSSF 12/544 requires that at least the following items be included:

- the roles and responsibilities of the various stakeholders to this system;
- the implemented methods and procedures for the identification, assessment, validation, limitation, monitoring and reporting of risks;
- the tools which are possibly used for the management and documentation of risks.

However, the RAR analysis revealed that only a weak majority of support PFS provided a sufficiently clear description of their risk management system which would allow an external person to understand the method used. Hence, the CSSF considers that more than half of the PFS do not comply or comply only partially with Point II.A. of Circular CSSF 12/544.



The main problems resulted from a too generic and often not sufficiently detailed description of the risk management system. This made it difficult to understand the risk identification processes, their analysis and monitoring, as well as the roles and responsibilities of the different parties concerned.

b) Self-assessment of direct and indirect risks

• Number of risks reported

In accordance with Point II.B. of Circular CSSF 12/544, each PFS shall report the 20 direct risks and five indirect risks having received the highest scores during the calculation of the net materiality. Moreover, any direct or indirect risk the net impact of which is equal to or higher than six and which has at the same time a net probability equal to or higher than five is also to be reported (additionally to the 25 risks mentioned above).

In practice, only 33% of the RARs analysed included the expected number of risks. However, it should be noted that 12% of the RARs included partially overlapping risks. This is in particular the case for support PFS which actually reported 20 direct risks as provided for in the circular, but for which the CSSF considered that a certain number of them could be grouped into one single risk. This is also the case where the CSSF considered that part of the direct risks indicated should be requalified as indirect risks.

Consequently, this means that more than half of the RARs, i.e. 55%, were not compliant.



• Understanding the concepts of direct and indirect risk

In 44% of the RARs analysed, the support PFS seem to have correctly understood the concepts of direct and indirect risk. The aim was to distinguish between (1) the risks directly related to the activities carried out in the

financial sector and which have a direct impact on the clients benefiting from these activities and (2) the risks related to the organisation and administration of the support PFS or its service provisions outside the financial sector and whose impact creates an indirect risk for its financial sector professional clients.

Of the remaining 56%, a minority of 17% did apparently not understand those concepts and mixed up direct and indirect risks. 39% categorised wrongly certain direct and indirect risks.



• Type of risks reported

In nearly half of the RARs analysed (47%), the support PFS reported mainly:

- generic risks;
- risks of a very global nature; or
- risks taken over from the examples mentioned in Circular CSSF 12/544.

However, the sole purpose of the risk categories set out in the circular was to group the types of risks to be identified by support PFS homogeneously.

In 13% of the RARs, the risks reported were not or only partially relevant and did not, a priori, concern the financial sector (the most significant examples are: theft of rolling stock, legislative change, office space-health, safety and well-being, recruitment of personnel with no valid driving licence, risk that premises no longer comply with ITM regulations, goods forgotten in the company vehicle, etc.).

Finally, for only 41% of the RARs, the risks reported were clearly linked to the entity's activities.



• Clear and understandable information in risk sheets

Only 41% of the risk sheets were complete and clear enough to allow an analysis. At this level, two major problems arose.

The first problem concerned the description of risks, of their mitigation techniques and/or the action plans which have not been detailed further (48%) and do thus not allow an external person to understand the issue raised and analyse it properly.

The second problem concerned, in 11% of the cases, probability and impact assessments that did not, a priori, seem consistent with the nature of the risk described.

For a better understanding of this point, the most significant examples are detailed below.

The CSSF was confronted with risk probabilities which seemed clearly overestimated, as for example a risk probability of an attack assessed at 9/10 or a risk probability of a fire at 10/10, which means that the fire risk is of 100% over a fixed period of time (in general one year as the RAR is an annual report).

Then, the CSSF noticed that other impacts had not been taken into consideration. This was the case for a configuration/set-up error risk which included certain impacts (legal, financial, etc.) but for which the operational impact was nil. Another example was a risk describing confidentiality issues of client data linked to an unrestricted access to all client data for all technical staff, and for which the support PFS did only take into account the operational impact and ignored all other possible impacts.



• Reference to the internal audit

Circular CSSF 12/544 lays down that each risk sheet must provide a reference to the internal audits carried out to check the existence and efficiency of these mitigation aspects. However, the CSSF realised that this requirement was missing in 81% of the risk sheets of the RARs analysed.



3.4.3. Conclusions relating to the RAR analysis

The CSSF considers that only 35% of the RARs have been drawn up with sufficient care to be used without any further major comments.

Conversely, in 31% of the cases, the CSSF considers that the support PFS did not make the necessary efforts to draw up an exploitable RAR, meeting a minimum quality standard. A deficiency letter will be issued for these RARs in order to request that future RARs be drawn up in compliance with the CSSF requirements.

Finally, following the analysis performed by the CSSF, 34% of the RARs do not provide sufficient added value to allow drawing conclusions on the entity's risk profile, risk management and future development of risks.



3.4.4. Perspectives

The CSSF considers that the information provided in the risk sheets has to be improved significantly in order to allow a fully exploitable analysis. Support PFS will also have to improve significantly the descriptions of the probability and impact assessments reported in order to make them fully understandable to a third party. This work is essential to allow, in the future, an analysis of the RARs that focuses more on the "qualitative" aspect of risks rather than on the formal structure of the report set out in Circular CSSF 12/544.

In parallel, support PFS are also requested to comply with all the provisions of Circular CSSF 12/544 in the future, in particular as regards the documents to be attached, the information to provide in the risk sheet and the number of risks to report, with the purpose to improve the handling and analysis of the RARs and DRs.

For DRs in particular, support PFS are invited to provide the DR of the second year in a marked-up version indicating the changes compared to the DR of the previous year (only if the quality of the initial DR had been considered satisfactory).

As regards future circulars, Circular CSSF 12/544 already anticipated that a new circular will define the practical rules concerning the mission of the *réviseurs d'entreprises agréés* with support PFS. The drawing-up of this circular appears to be more difficult than initially planned, but it should, once finalised, solve the issues linked to the mission to be carried out by the *réviseur d'entreprises agréé* by adopting the principle of the agreed upon procedures.

The CSSF is also working on the drawing-up of a circular relating to the electronic reporting of risk sheets, the risk register and the list of names of the clients of the financial sector. Work is still ongoing and should be concluded before the last quarter of 2014.



Agents hired in 2013 and 2014: Departments “Information systems and supervision of support PFS” and “Public oversight of the audit profession”

Left to right: Juscelino LEAL, Patrick-Laurent SANDBRINK, Eugénie MAUBERT, Antoine WATELLIER, Virginie DAROCOURT, Marion LEENAERT, François LOURTIE, Sophie TERRASSIER, Paolo GODONE, Grégory MOUSLER

Absent : Xavier WIGNY



Agents hired in 2013 and 2014: Department “Supervision of banks”

Left to right: Amar RADONCIC, Bob MÜLLER, Pierre AUBERTIN, Emmanuel GIROT, Tom STEICHEN, Max SCHMITZ, Natalia KATILOVA, Dominique STREVELER, Marine VIEGAS, Clément ROYER DE LA BASTIE

CHAPTER VI

SUPERVISION OF PAYMENT INSTITUTIONS AND ELECTRONIC MONEY INSTITUTIONS



1. Payment institutions
2. Electronic money institutions

1. PAYMENT INSTITUTIONS

1.1. Regulatory framework

The law of 10 November 2009 on payment services transposed into national law Directive 2007/64/EC of 13 November 2007 on payment services in the internal market. This directive aims to set up a coherent legal framework in order to establish a single European market for payment services and to ensure its proper functioning.

The law of 10 November 2009 introduced a new financial institution status, i.e. the payment institutions authorised to carry out payment services activities, and imposes authorisation, exercise and supervisory conditions on them. The payment services concerned are specifically listed in the annexe to the law.

Article 31(1) of the law designates the CSSF as the competent authority for the supervision of payment institutions.

The main prudential provisions applicable to payment institutions may be summarised as follows:

- quantitative prudential standards, i.e. minimum capital and capital requirements calculated according to one of the three methods provided by the law; the CSSF monitors the proper application and compliance with these quantitative standards based on a specific reporting pursuant to Circular CSSF 11/511;
- rules for the protection of funds received for the execution of payment transactions;
- rules related to the fight against money laundering and terrorist financing;
- guarantee of a sound and prudent management and existence of a robust internal governance system.

As regards the last indent, the rules are, in principle, those applicable to credit institutions and investment firms but they are applied to payment institutions according to a proportionality principle based, among others, on the type of payment services provided and the risks incurred.

The activities exercised by the Luxembourg payment institutions in another EU/EEA Member State through the establishment of a branch, through the intermediary of an agent or by way of free provision of services, are also subject to the prudential supervision of the CSSF.

By way of compensation for the simplified rules to access the profession and the lighter prudential supervision compared to those applicable to credit institutions, the payment institutions are subject to activity restrictions and prohibitions:

- strict control of credit granting according to the provisions of Article 10(3) of the law of 10 November 2009;
- prohibition to conduct the business of taking deposits or other repayable funds within the meaning of Article 2(3) of the law of 5 April 1993 on the financial sector;
- exclusive use of payment accounts opened by payment institutions for payment transactions;
- rules for the protection of funds for the execution of activities other than the provision of payment services in accordance with Articles 10 and 14 of the law of 10 November 2009.

On 7 December 2012, the CSSF published Circular CSSF 12/550 relating to the practical rules concerning the mission of the *réviseurs d'entreprises agréés* (approved statutory auditors) of payment institutions, the purpose of which is to specify the scope of the mandate for the audit of annual accounting documents and to set the rules relating to the content of the long form report that payment institutions have to communicate to the CSSF pursuant to Article 37 of the law of 10 November 2009.

1.2. Payment institutions authorised in Luxembourg

As at 31 December 2013, five payment institutions incorporated under Luxembourg law (four as at 31 December 2012) were listed in the public register of payment institutions established in Luxembourg:

- Digicash Payments S.A.,
- Diners Club Beneflux S.A.,

- FIA-NET Europe S.A.,
- Olky Payment Service Provider S.à r.l.¹,
- SIX Payment Services (Europe) S.A..

In addition, there is Deutsche Post Zahlungsdienste GmbH, Niederlassung Luxemburg, a branch of a payment institution under German law.

It should be noted that the company Cetrel S.A. acts as an agent on behalf of SIX Payment Services (Europe) S.A..

2. ELECTRONIC MONEY INSTITUTIONS

2.1. Regulatory framework

Directive 2009/110/EC of 16 September 2009 on the taking up, pursuit and prudential supervision of the business of electronic money institutions repealing the first Directive 2000/46/EC on electronic money, was transposed into national law by a law of 20 May 2011 amending the law of 10 November 2009 on payment services.

The major purpose of this new directive is to provide electronic money with a sustainable and attractive regime and, in particular, to make the prudential supervisory regime of electronic money institutions (EMIs) consistent with that applicable to the payment institutions governed by Directive 2007/64/EC (i.e. simplified rules to access the profession and lighter prudential supervision compared to those applicable to credit institutions).

These new provisions create an autonomous regime for the EMIs which are no longer considered as credit institutions. At national level, the CSSF has been designated as the competent authority to supervise EMIs.

Following the entry into force of Directive 2009/110/EC, electronic money is viewed from a wider perspective insofar as the definition given by the directive covers, in principle, all the situations where an issuer of electronic money issues a prepaid stored value in exchange for funds. Electronic money is defined as a monetary value represented by a claim on the issuer, which is:

- stored electronically, including magnetically;
- issued upon receipt of funds for the purpose of making payment transactions; and
- accepted by a natural or legal person other than the electronic money institution.

Pursuant to Article 24-6 of the law of 10 November 2009, EMIs are entitled to carry out, in addition to the issuance of electronic money, each of the following activities:

- the provision of payment services listed in the annexe to the law;
- the granting of credit subject to compliance with the provisions of Article 24-6(1)(b) of the law;
- the provision of operational services and ancillary services closely related to the issuance of electronic money or to the provision of payment services;
- the management of payment systems;
- other commercial activities.

The law imposes authorisation, exercise and supervisory conditions on EMIs. The main prudential provisions applicable to EMIs may be summarised as follows:

- quantitative prudential standards, i.e. minimum capital and capital requirements in accordance with Articles 24-11 and 24-12; the CSSF monitors the proper application and compliance with these quantitative standards based on a specific reporting pursuant to Circular CSSF 11/522;
- rules for the protection of funds received in exchange for electronic money in accordance with the provisions of Article 24-10;
- rules related to the fight against money laundering and terrorist financing;
- guarantee of a sound and prudent management and existence of a robust internal governance system.

¹ Payment institution authorised in 2013.

As regards the last indent, the rules are, in principle, those applicable to credit institutions and to investment firms but they are applied to EMIs according to a proportionality principle based, among others, on the type of risks incurred.

The protection of funds as mentioned in the second indent above is a key element of the electronic money regime. The purpose of this regime is to guarantee electronic money holders the redemption of their funds in case of insolvency of the EMI.

In accordance with this requirement, the funds received by the EMI in exchange for electronic money may either be deposited in a separate bank account, in order not to be commingled with the funds of persons other than electronic money holders, or invested in certain assets according to the criteria defined in Article 24-10(1)(a) of the law or covered by an insurance policy. Consequently, the funds thus segregated shall not form part of the EMI's own assets and shall be deducted, in the sole interests of the electronic money holders, from the claims of other creditors of the institution. Investments of these funds are legally limited to investments in "secure and low-risk assets".

The activities exercised by Luxembourg EMIs in another EU/EEA Member State through the establishment of a branch, through intermediaries or agents or by way of free provision of services, are also subject to the prudential supervision of the CSSF.

Similarly to payment institutions, EMIs are subject to activity restrictions:

- prohibition to conduct the business of taking deposits or other repayable funds within the meaning of Article 2(3) of the law of 5 April 1993 on the financial sector;
- strict control of credit granting according to the provisions of Article 24-6(1) of the law of 10 November 2009.

EMIs shall comply with the provisions of Article 48-2 of the law of 10 November 2009 relating to the issuance and redeemability of electronic money. Moreover, they are not allowed granting interest or any other benefit related to the length of time during which an electronic money holder holds electronic money.

On 8 July 2013, the CSSF published Circular CSSF 13/569 relating to the practical rules concerning the mission of the *réviseurs d'entreprises agréés* (approved statutory auditors) of electronic money institutions, the purpose of which is to specify the scope of the mandate for the audit of annual accounting documents and to set the rules relating to the content of the long form report that EMIs have to communicate to the CSSF pursuant to Article 37 of the law of 10 November 2009.

2.2. Electronic money institutions authorised in Luxembourg

As at 31 December 2013, five EMIs (idem as at 31 December 2012) were listed in the public register of EMIs authorised in Luxembourg:

- Amazon Payments Europe S.C.A.,
- Leetchi Corp S.A.,
- MOBEY S.A.,
- PayCash Europe S.A.,
- YAPITAL Financial AG.

It should also be noted that one of the main activities of the company PayPal (Europe) S.à r.l. et Cie, S.C.A., authorised as a credit institution in Luxembourg, is the issuance of electronic money.

All EMIs authorised in Luxembourg issue electronic money in accordance with point 29) of Article 1 of the law of 10 November 2009. The methods of use of electronic money may nevertheless vary according to the corporate model of each EMI. Thus, according to the EMI's business model chosen, electronic money holders may:

- carry out money transfers from one electronic money account to another electronic money account (transfers between individuals);

- make payments related to online shopping;
- make payments via a mobile phone, for instance via QR code reading (Quick Response Code);
- make payments via a prepaid card which may be linked to the electronic money account.



Agents hired in 2013 and 2014: Legal Department and Department "On-site inspection"

Left to right: Jean-Claude ROMMES, Ibrahim FOFANA, Véronique LEGRAND, Ben RODERES, Carine VAN MULDER-S-PEIFFER, Rachel PORTÉ, Bruno MARTINS, Claude KREMER, Naïla MALTI, Markus THESEN, Stéphane HARMELIN

Absent: Sophie BAUWENS, Sandra WIRBEL

CHAPTER VII

SUPERVISION OF UCIS AND SICARS



1. Evolution of the UCI and SICAR sector in 2013
2. Management companies and alternative investment fund managers
3. Developments in the regulatory framework
4. Prudential supervisory practice
5. IT system for the supervision of UCIs

1. EVOLUTION OF THE UCI AND SICAR SECTOR IN 2013

1.1. Major events in 2013

In Luxembourg, the UCI sector (including undertakings for collective investment in transferable securities (UCITS), UCIs authorised under Part II of the law of 17 December 2010 relating to undertakings for collective investment (2010 Law) and specialised investment funds (SIFs)) recorded a 9.7% increase of the net assets and the number of UCIs rose by 1.6% in 2013.

As far as the evolution of the financial markets is concerned, some differences between the developed markets and the emerging markets were noticed in 2013. Thus, the financial markets of developed countries recorded on average positive performances following the favourable macroeconomic development as, for example, the exit of the euro area from the recession or the growth stability in the United States. This positive development was supported by accommodating monetary policies of the main central banks. However, the financial markets of the emerging countries mostly recorded negative performances in 2013, due mainly to the difficulties encountered by the economies of some emerging countries and to some extent to the announcement made by the US Federal Reserve that it will contemplate a more restrictive monetary policy if the economic recovery in the United States is confirmed.

Overall, the global equity index “MSCI WORLD Standard (Large + Mid Cap)” improved by 21.2% whereas the global bond index “JPMorgan GBI Global Traded Index Hedged Index Level Euro” slightly decreased by 0.5% in 2013.

As regards the development of the Luxembourg UCI sector, the inflow of new capital and the performance of the major financial stock markets resulted in the annual increase in Luxembourg UCIs’ global net assets of EUR 231.6 billion to reach EUR 2,615.4 billion as at 31 December 2013. A positive net capital investment of EUR 193.6 billion and a positive impact of financial markets of EUR 38.0 billion were responsible for this increase.

Although the category of diversified UCIs recorded the most significant inflow of capital with EUR 63.5 billion, the categories of equity and bond UCIs also registered a positive net capital investment of EUR 55.9 billion and EUR 51.2 billion, respectively. However, under the effect of the very low, even negative, return rates, the UCIs active in the monetary markets faced a net capital disinvestment of EUR 18.0 billion in 2013.

At the end of 2013, the total number of UCIs reached 3,902 against 3,841 at the end of the previous year, i.e. a net increase of 61 entities. Taken separately, the number of SIFs, however, increased by 77 entities.

46.6% of the 3,902 UCIs registered on the official list as at 31 December 2013 were UCITS governed by Part I of the 2010 Law.

As far as SICARs are concerned, the number of SICARs registered on the official list increased by three entities to reach 279 entities as at 31 December 2013 (276 entities as at 31 December 2012) which represents EUR 30.4 billion in terms of net assets (EUR 29.9 billion as at 31 December 2012). 224 SICARs have a traditional structure whereas 55 were incorporated as SICARs with multiple compartments with 139 active compartments at the end of 2013.

As regards management companies authorised under Chapter 15 of the 2010 Law, 21 new companies were set up in Luxembourg, while six ceased their activities.

At the regulatory level, the law on alternative investment fund managers (AIFM Law) transposing Directive 2011/61/EU on alternative investment fund managers (AIFMD) entered into force on 12 July 2013. The purpose of AIFMD is to submit the AIFMs to a regulatory framework harmonised at European level and at the same time to introduce a European passport which will allow these managers to provide management services and to distribute the alternative investment funds under their management in all the EU Member States.

Following the entry into force of the AIFM Law, 12 entities were authorised as AIFM in 2013. However, in light of the application files dealt with since the beginning of 2014, the number of entities will quickly rise during the year.

The CSSF continued to focus particularly on the compliance of the management companies of UCITS with Circular CSSF 12/546 on the authorisation and organisation of management companies. The CSSF applies the provisions of Circular CSSF 12/546 also in the context of the review of files for authorised AIFMs. It considers

that the players concerned must comply with the above-mentioned circular, allowing thus the development of the quality of services provided by these players.

1.2. Evolution of the UCI sector

1.2.1. Evolution of the number of UCIs

As at 31 December 2013, 3,902 UCIs were registered on the official list against 3,841 UCIs at the end of the previous year, representing an increase of 61 entities (+1.6%). During the year, 362 UCIs were registered and 301 entities were deregistered from the official list.

Evolution of the number of UCIs

	Number of UCIs	Registrations on the list	Deregistrations from the list	Net variation	in %
2003	1,870	175	246	-71	-3.7%
2004	1,968	202	104	98	5.2%
2005	2,060	266	174	92	4.7%
2006	2,238	345	167	178	8.6%
2007	2,868	824	194	630	28.2%
2008	3,371	712	209	503	17.5%
2009	3,463	408	316	92	2.7%
2010	3,667	471	267	204	5.9%
2011	3,845	469	291	178	4.9%
2012	3,841	381	385	-4	-0.1%
2013	3,902	362	301	61	1.6%

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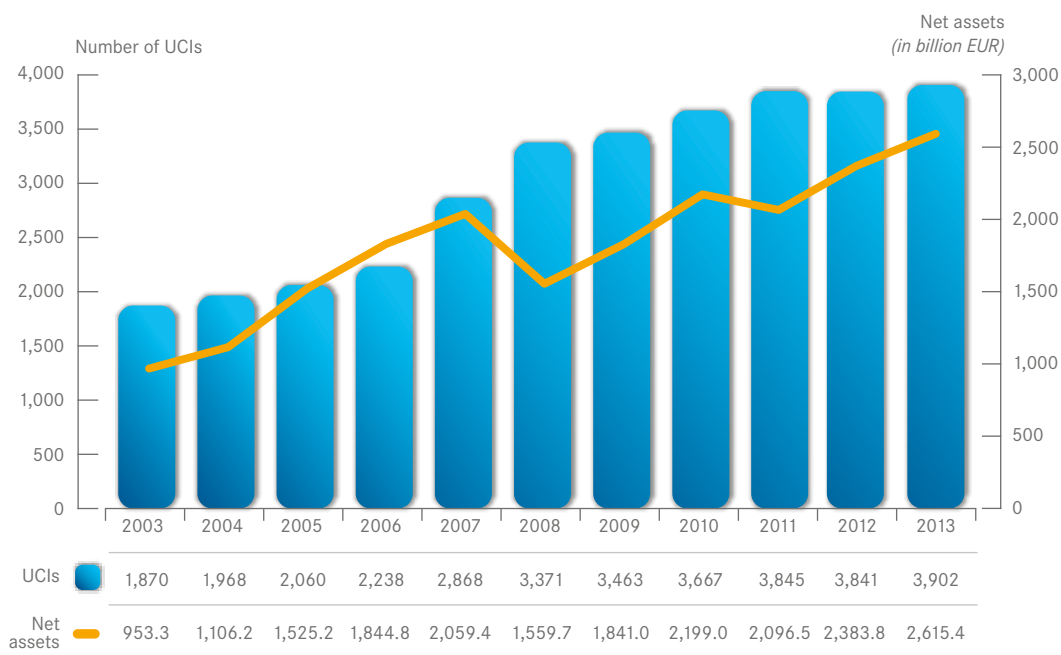
1.2.2. Evolution of the net assets of UCIs

Through the inflow of new capital and the positive developments in the financial markets, the total net assets of Luxembourg UCIs grew by EUR 231.6 billion over one year to EUR 2,615.4 billion as at 31 December 2013 (+9.7%). This increase originates partially from net subscriptions (83.6%) and partially from a positive impact of the financial markets (16.4%). Net capital investments in Luxembourg UCIs amounted to EUR 193.6 billion in 2013, which proves the investors' confidence in the financial markets.

Evolution of UCI net assets - in billion EUR

	Net assets	Net subscriptions	Net asset variation	in %	Average net assets per UCI
2003	953.3	82.6	108.8	12.9%	0.510
2004	1,106.2	113.7	152.9	16.0%	0.562
2005	1,525.2	236.3	419.0	37.9%	0.740
2006	1,844.8	241.3	319.6	21.0%	0.824
2007	2,059.4	188.5	214.6	11.6%	0.718
2008	1,559.7	-77.2	-499.7	-24.3%	0.463
2009	1,841.0	84.4	281.3	18.0%	0.532
2010	2,199.0	161.6	358.0	19.4%	0.600
2011	2,096.5	5.3	-102.5	-4.7%	0.545
2012	2,383.8	123.1	287.3	13.7%	0.621
2013	2,615.4	193.6	231.6	9.7%	0.670

Evolution of the number and net assets of UCIs



1.2.3. Evolution of the number of UCI entities¹

As at 31 December 2013, 2,529 out of 3,902 UCIs had adopted an umbrella structure. As the number of operating sub-funds rose from 12,041 to 12,312 (+2.3%), the total number of entities grew from 13,420 as at 31 December 2012 to 13,685 as at 31 December 2013 (+2.0%), notwithstanding the fall in the number of traditionally structured UCIs from 1,379 to 1,373 entities.

¹ The term "entity" refers to both traditional UCIs and sub-funds of umbrella funds. The number of new "entities" therefore means, from an economic point of view, the number of economic vehicles created.

Evolution of the number of UCI entities

	Total number of UCIs	of which traditionally structured UCIs	as % of total	of which umbrella funds	as % of total	Number of sub-funds	Average number of sub-funds per umbrella fund	Total number of entities	Variation in %
2003	1,870	690	36.9%	1,180	63.1%	6,819	5.78	7,509	-3.8%
2004	1,968	742	37.7%	1,226	62.3%	7,134	5.82	7,876	4.9%
2005	2,060	762	37.0%	1,298	63.0%	7,735	5.96	8,497	7.9%
2006	2,238	851	38.0%	1,387	62.0%	8,622	6.22	9,473	11.5%
2007	2,868	1,180	41.1%	1,688	58.9%	9,935	5.89	11,115	17.3%
2008	3,371	1,352	40.1%	2,019	59.9%	10,973	5.43	12,325	10.9%
2009	3,463	1,355	39.1%	2,108	60.9%	10,877	5.16	12,232	-0.8%
2010	3,667	1,365	37.2%	2,302	62.8%	11,572	5.03	12,937	5.8%
2011	3,845	1,418	36.9%	2,427	63.1%	11,876	4.89	13,294	2.8%
2012	3,841	1,379	35.9%	2,462	64.1%	12,041	4.89	13,420	0.9%
2013	3,902	1,373	35.2%	2,529	64.8%	12,312	4.87	13,685	2.0%

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1.2.4. Evolution of UCIs and their net assets according to legal form and applicable law

• Evolution of UCIs and their net assets according to legal form

The breakdown of UCIs between common funds (*fonds communs de placement* (FCP)), *sociétés d'investissement à capital variable* (SICAV) and *sociétés d'investissement à capital fixe* (SICAF) reveals that, on 31 December 2013, SICAVs were still the prevailing form with 2,032 entities out of a total of 3,902 active UCIs, against 1,831 entities operating as FCPs and 39 as SICAFs.

At the end of 2013, FCPs' net assets represented 26.5% of the total net assets of UCIs and SICAVs' net assets represented 73.0% of the total net assets of UCIs. SICAFs' net assets remained low with 0.5% of the total net assets of UCIs.

• Evolution of UCIs and their net assets according to applicable law

UCIs break down as follows according to applicable law: they fall either under Part I of the 2010 Law or under Part II of the same law or under the law of 13 February 2007 relating to specialised investment funds (SIF Law).

UCIs subject to Part I of the 2010 Law are governed by the provisions of the EU Directive on UCITS and can therefore benefit from the marketing facilities provided therein. Part II encompasses all the other UCIs which solicit the public for the subscription of their units, whereas SIFs are UCIs whose securities are reserved for well-informed investors according to the criteria set out in Article 2 of the SIF Law.

At the end of 2013, 46.6% of UCIs registered on the official list were UCITS governed by Part I of the 2010 Law and 13.4% were other UCIs governed by Part II (non-coordinated UCIs). SIFs represented 40.0% of the 3,902 Luxembourg UCIs.

Net assets were distributed at the same date as follows: 81.1% for UCIs under Part I, 7.2% for UCIs under Part II and 11.7% for SIFs.

As regards Part I, the number of UCIs increased by 0.89% compared to 2012 and net assets increased by 10.89%, whereas the number of UCIs under Part II decreased by 5.77% and their net assets by 3.30%. The number of SIFs increased by 5.19% and their net assets by 10.67%.

The following table compares the evolution in 2013 of the number of UCIs and net assets according to both the legal form and applicable law.

Evolution of the number of UCIs and their net assets according to legal form and applicable law

Number of UCIs	2012				2013				Variation 2012/2013			
	FCPs	SICAVs	SICAFs	Total	FCPs	SICAVs	SICAFs	Total	FCPs	SICAVs	SICAFs	Total
Part I	1,061	740	0	1,801	1,046	771	0	1,817	-1.41%	4.19%	0.00%	0.89%
Part II	273	278	4	555	256	263	4	523	-6.23%	-5.40%	0.00%	-5.77%
SIFs	525	928	32	1,485	529	998	35	1,562	0.76%	7.54%	9.38%	5.19%
Total	1,859	1,946	36	3,841	1,831	2,032	39	3,902	-1.51%	4.42%	8.33%	1.59%

Net assets (in billion EUR)	2012				2013				Variation 2012/2013			
	FCPs	SICAVs	SICAFs	Total	FCPs	SICAVs	SICAFs	Total	FCPs	SICAVs	SICAFs	Total
Part I	473.70	1,439.39	0.00	1,913.09	483.41	1,638.05	0.00	2,121.46	2.05%	13.80%	0.00%	10.89%
Part II	77.05	115.75	0.97	193.77	76.91	109.59	0.88	187.38	-0.18%	-5.32%	-9.28%	-3.30%
SIFs	118.35	147.58	11.04	276.97	131.69	162.07	12.76	306.52	11.27%	9.82%	15.58%	10.67%
Total	669.10	1,702.72	12.01	2,383.83	692.01	1,909.71	13.64	2,615.36	3.42%	12.16%	13.57%	9.71%

1.2.5. Net subscriptions

In 2013, UCIs under Part I of the 2010 Law recorded net subscriptions totalling EUR 158.09 billion. However, UCIs under Part II showed net redemptions totalling EUR 5.01 billion. Net subscriptions of SIFs amounted to EUR 40.49 billion.

Breakdown of net subscriptions according to Parts I and II of the 2010 Law and SIFs

(in billion EUR)	FCPs	SICAVs	SICAFs	Total	in %
Part I	-0.63	158.72	0.00	158.09	81.67%
Part II	2.75	-7.73	-0.03	-5.01	-2.59%
SIFs	16.67	21.73	2.09	40.49	20.92%
Total	18.79	172.72	2.06	193.57	100.00%

1.2.6. Valuation currencies used

As regards the valuation currencies used, most entities (9,015 out of a total of 13,685, i.e. 65.9%) were denominated in euro, followed by those in US dollars (3,393, i.e. 24.8%) and those in Swiss francs (319, i.e. 2.3%).

In terms of net assets, the entities denominated in euro accounted for EUR 1,397.1 billion of a total of EUR 2,615.4 billion (i.e. 53.4%), ahead of entities expressed in US dollars (EUR 1,001.7 billion, i.e. 38.3%) and in yen (EUR 53.5 billion, i.e. 2.0%).

1.2.7. 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 include UCIs investing in venture capital and UCIs investing in insurance contracts or in debt.

Net assets and entities of UCIs according to their investment policy

	2012		2013		Variation in %	
	Number of entities	Net assets (<i>in billion EUR</i>)	Number of entities	Net assets (<i>in billion EUR</i>)	Number of entities	Net assets
Fixed-income transferable securities	2,994	808.78	3,105	838.19	3.71%	3.64%
Variable-yield transferable securities	3,543	657.13	3,520	791.97	-0.65%	20.52%
Mixed transferable securities	3,918	443.97	4,050	510.80	3.37%	15.05%
Fund of funds	2,037	153.65	2,043	175.87	0.79%	14.46%
Money market instruments and other short-term securities	308	257.62	307	232.98	-0.32%	-9.56%
Cash	81	5.90	66	4.24	-18.52%	-28.12%
Real estate	244	25.93	279	30.47	14.34%	17.55%
Futures, options, warrants	174	17.31	166	13.34	-4.60%	-22.96%
Other assets	131	13.54	149	17.50	13.74%	29.23%
Total	13,420	2,383.83	13,685	2,615.36	1.97%	9.71%

Most UCI categories, and in particular those investing in variable-yield transferable securities, benefited from quite significant net subscriptions and a positive development of financial markets in 2013.

However, some UCI categories, including particularly those investing in money market instruments and in other short-term securities or derivatives, suffered withdrawals of capital while the inflow of new capital benefited other categories, including those investing in real estate.

Investment policy of UCIs according to Parts I and II of the 2010 Law and SIFs

Situation as at 31 December 2013	Number of entities	Net assets (in billion EUR)	Net assets (in %)
UCITS subject to Part I			
Fixed-income transferable securities	2,262	747.42	28.6%
Variable-yield transferable securities	2,976	718.05	27.5%
Mixed transferable securities	2,496	364.64	13.9%
Fund of funds	804	79.83	3.0%
Money market instruments and other short-term securities	213	203.51	7.8%
Cash	22	2.26	0.1%
Futures and/or options	59	4.80	0.2%
Other assets	4	0.95	0.0%
UCITS subject to Part II²			
Fixed-income transferable securities	269	31.85	1.2%
Variable-yield transferable securities	117	20.37	0.8%
Mixed transferable securities	427	47.97	1.8%
Fund of funds	558	49.32	1.9%
Money market instruments and other short-term securities	77	25.18	1.0%
Cash	29	1.61	0.1%
UCITS subject to Part II³			
Non-listed transferable securities	19	2.30	0.1%
Venture capital	4	0.01	0.0%
Other UCIs subject to Part II			
Real estate	27	1.73	0.1%
Futures and/or options	48	4.98	0.2%
Other assets	14	1.97	0.1%
SIFs			
Fixed-income transferable securities	574	58.92	2.2%
Variable-yield transferable securities	349	45.50	1.7%
Mixed transferable securities	1,073	93.11	3.6%
Fund of funds	659	45.80	1.7%
Money market instruments and other short-term securities	17	4.29	0.2%
Cash	15	0.37	0.0%
Non-listed transferable securities	111	10.87	0.4%
Venture capital	21	0.94	0.0%
Real estate	252	28.74	1.1%
Futures and/or options	59	3.56	0.1%
Other assets	130	14.42	0.6%
Total	13,685	2,615.36	100.0%

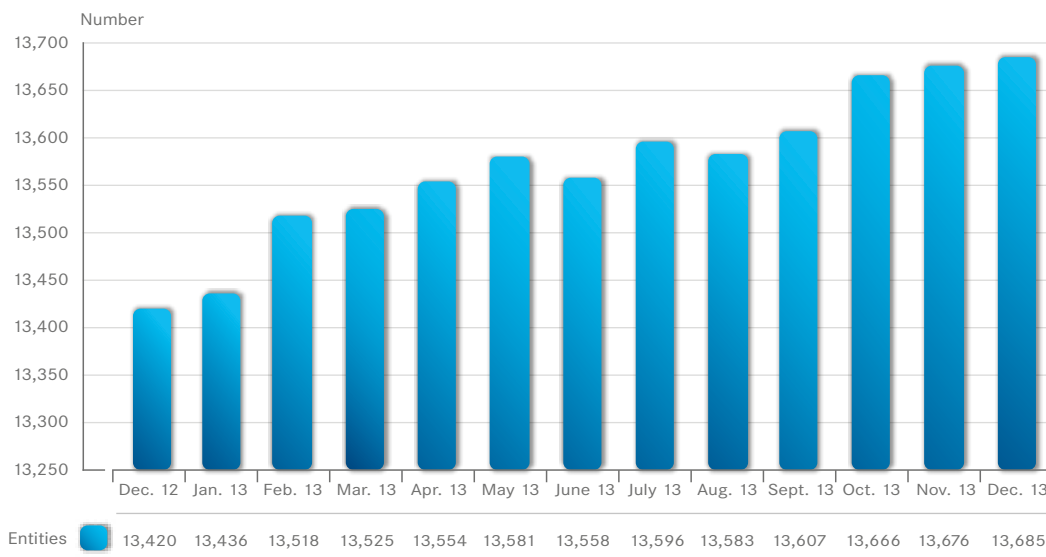
² UCITS excluded from Part I of the 2010 Law, pursuant to Article 3, indents 1 to 3, i.e. UCITS closed for redemptions, not promoted in the EU or only sold to individuals in countries outside the EU.

³ UCITS excluded from Part I of the 2010 Law, pursuant to Article 3, indent 4, i.e. UCITS under one of the categories laid down by Circular CSSF 03/88, owing to their investment and loan policy.

1.2.8. Evolution of UCI entities

In 2013, the number of entities grew by 265 (+1.97%) to 13,685 entities at the end of the year.

Monthly evolution of the number of entities



• Entities approved in 2013

In 2013, 2,051 new entities were authorised. In absolute terms, this figure represents a decrease of 46 entities (-2.19%) compared to the previous year. 1,268 out of the 2,051 entities approved in 2013, i.e. 61.8%, were launched in the same year.

	2008	2009	2010	2011	2012	2013
Newly approved entities	3,361	1,999	2,362	2,158	2,097	2,051
<i>of which launched in the same year</i>	2,008	1,068	1,343	1,343	1,144	1,268
in %	59.7%	53.4%	56.9%	62.2%	54.6%	61.8%

The breakdown by investment policy of entities authorised in 2013 shows that the proportion of entities investing in mixed transferable securities increased compared to 2012. The proportion of new entities investing in fixed-income transferable securities and that of entities investing in variable-yield transferable securities remained stable in 2013.

Investment policy of entities approved in 2013

Investment policy	2012		2013	
	Number of entities	As % of total	Number of entities	As % of total
Fixed-income transferable securities (excluding money market instruments and other short-term securities)	576	27.47%	541	26.38%
Variable-yield transferable securities	401	19.12%	429	20.92%
Mixed transferable securities	581	27.71%	690	33.64%
Fund of funds	345	16.45%	249	12.14%
Money market instruments and other short-term securities	33	1.57%	13	0.63%
Cash	6	0.29%	3	0.15%
Real estate	69	3.29%	63	3.07%
Futures, options, warrants (derivative instruments)	43	2.05%	26	1.27%
Other assets	43	2.05%	37	1.80%
Total	2,097	100.00%	2,051	100.00%

• Entities closed in 2013

In 2013, 1,441 entities were closed, which was 36 entities less (-2.44%) than in the previous year.

	2007	2008	2009	2010	2011	2012	2013
Liquidated entities	424	752	968	633	747	919	863
Matured entities	83	84	92	111	143	157	135
Merged entities	282	485	482	380	511	401	443
Total	789	1,321	1,542	1,124	1,401	1,477	1,441

The breakdown by investment policy shows that most of the entities closed in 2013 had invested in mixed transferable securities.

Investment policy of entities closed in 2013

Investment policy	2012		2013	
	Number of entities	As % of total	Number of entities	As % of total
Fixed-income transferable securities (excluding money market instruments and other short-term securities)	310	20.99%	332	23.04%
Variable-yield transferable securities	327	22.14%	381	26.44%
Mixed transferable securities	465	31.48%	424	29.42%
Fund of funds	262	17.74%	203	14.09%
Money market instruments and other short-term securities	43	2.91%	25	1.74%
Cash	2	0.14%	19	1.32%
Real estate	9	0.61%	10	0.69%
Futures, options, warrants (derivative instruments)	38	2.57%	31	2.15%
Other assets	21	1.42%	16	1.11%
Total	1,477	100.00%	1,441	100.00%

1.2.9. Evolution of several specific categories of UCIs

• Guarantee-type UCIs

The purpose of guarantee-type UCIs is to offer investors some security in light of the fluctuations inherent in financial markets. According to the investment policy pursued by the UCIs concerned, the guarantee ensures that the investor is reimbursed a proportion of the invested capital or is fully reimbursed the initial investment or even receives a return on the investment at the end of one or several pre-determined periods.

In 2013, the number of guarantee-type UCIs fell from 168 to 154 and the total number of entities from 297 to 276. The fall in entities can be explained by the launch of 27 new entities whereas the guarantees either expired or were not extended for 48 entities.

As at 31 December 2013, the 276 entities broke down into 38 entities guaranteeing unitholders only a proportion of the capital commitment, 138 entities guaranteeing repayment in full of the capital commitment (money-back guarantee) and 100 entities offering their investors a return in addition to the initial subscription price.

As at 31 December 2013, net assets of guarantee-type UCIs decreased by EUR 1.4 billion to EUR 36.1 billion, i.e. by 3.7%. It is also worth noting that guarantee-type UCIs set up by German promoters alone accounted for 93.5% of the total net assets of all guarantee-type UCIs.

Evolution of guarantee-type UCIs

Year	Number of UCIs	Number of economic entities	Net assets (in billion EUR)
2005	104	248	24.69
2006	121	297	32.56
2007	154	360	43.73
2008	176	382	44.83
2009	194	409	45.83
2010	192	400	41.99
2011	190	360	40.27
2012	168	297	37.54
2013	154	276	36.13

• Real estate UCIs

In 2013, net assets of UCIs investing mainly in real estate increased by 17.6%. It should be noted that SIFs remain the preferred vehicles for real estate investments.

Evolution of real estate UCIs

Year	Number of entities	of which active entities	of which Part II	of which SIFs	Net subscriptions (in billion EUR)	Net assets (in billion EUR)
2005	52	41	16	36	1.59	5.29
2006	76	64	22	54	2.65	8.06
2007	104	80	21	83	6.50	15.45
2008	137	111	16	121	7.13	20.93
2009	150	125	15	135	1.98	18.96
2010	179	149	13	166	0.04	21.43
2011	210	192	27	183	2.92	24.06
2012	244	220	26	218	2.00	25.93
2013	279	253	27	252	5.86	30.47

• Sharia UCIs

The number of sharia UCIs and entities grew by nine entities in 2013 and the net assets rose by 48.8%.

Evolution of sharia-compliant UCIs

Year	Number of sharia entities	Net assets (in million EUR)
2005	7	74.5
2006	8	93.6
2007	9	202.2
2008	22	212.8
2009	23	308.3
2010	24	472.8
2011	24	525.3
2012	28	1,276.7
2013	37	1,899.3

• Microfinance UCIs

The number of UCIs investing in microfinance decreased slightly in 2013, whereas the net assets rose by 15.0%.

Evolution of UCIs in the microfinance sector

Year	Number of microfinance entities	Net assets (in million EUR)
2005	3	104.8
2006	11	505.3
2007	15	771.1
2008	18	1,200.3
2009	29	1,675.7
2010	32	1,937.8
2011	30	2,429.7
2012	36	3,130.0
2013	34	3,599.3

• Money market UCIs

The number of UCIs which comply with the rules of “CESR’s Guidelines on a common definition of European money market funds” remained stable in 2013, whereas the net assets decreased by 11.47%. Given the very low, and even negative, yields on money markets, this category of UCI recorded a net disinvestment like in 2012.

Evolution of money market UCIs

	2012		2013		Variation in %	
	Number of entities	Net assets (in billion EUR)	Number of entities	Net assets (in billion EUR)	Number of entities	Net assets
Short-term money market funds	91	176.42	89	143.17	-2.20%	-18.85%
Money market funds	107	44.79	109	52.66	1.87%	17.57%
Total	208	221.21	208	195.83	0.00%	-11.47%

1.2.10. Initiators of Luxembourg UCIs

The breakdown of Luxembourg UCIs according to the geographic origin of their initiators highlights the multitude of countries represented in the financial centre. Initiators of Luxembourg UCIs spread over 64 countries.

Initiators of UCIs in Luxembourg are mostly from the United States, Germany, United Kingdom, Switzerland, Italy, France and Belgium.

Origin of the initiators of Luxembourg UCIs

Situation as at 31 December 2013	Net assets (in billion EUR)	in %	Number of UCIs	in %	Number of entities	in %
United States	594.145	22.7%	153	3.9%	953	7.0%
Germany	397.428	15.2%	1,524	39.1%	2,890	21.1%
United Kingdom	396.053	15.1%	274	7.0%	1,425	10.4%
Switzerland	372.735	14.3%	514	13.2%	2,524	18.5%
Italy	210.357	8.0%	151	3.9%	1,170	8.6%
France	194.195	7.4%	261	6.7%	1,182	8.6%
Belgium	123.931	4.7%	177	4.5%	1,180	8.6%
Luxembourg	61.603	2.4%	192	4.9%	482	3.5%
Netherlands	56.216	2.2%	52	1.3%	203	1.5%
Sweden	55.172	2.1%	100	2.6%	280	2.0%
Others	153.528	5.9%	504	12.9%	1,396	10.2%
Total	2,615.363	100.0%	3,902	100.0%	13,685	100.0%

1.2.11. Impact of the implementation of Directive 2009/65/EC (UCITS Directive) on the Luxembourg UCITS sector

With the implementation of the UCITS Directive transposed by the law of 17 December 2010 relating to undertakings for collective investment, the regulatory framework for Luxembourg UCITS was supplemented with a series of new measures in order to allow the management companies to develop their cross-border activities, to create a framework for cross-border mergers of UCITS, to allow the use of master-feeder structures and to remove the administrative barriers to the cross-border distribution of UCITS.

In 2013, several Luxembourg UCITS used these measures and changed their operating models with the view to achieving economies of scale and at the same time consolidating the managed assets.

• European passport for management companies of UCITS

In 2013, the number of management companies which are established in another EU Member State and which exercised their activities via the free provision of services in Luxembourg amounted to 26.

As at 31 December 2013, the situation of Luxembourg UCITS managed by a foreign management company was as follows.

Home Member State of the management company	Number of management companies managing Luxembourg UCITS	Number of managed UCITS	Total net assets managed (in million EUR)
France	20	113	12,200.0
Italy	3	87	12,507.8
United Kingdom	3	26	16,387.9

Moreover, one management company from another Member State (Malta) opened a branch in Luxembourg.

In 2013, six Luxembourg management companies notified their intention to manage UCITS in another EU Member State through free provision of services.

Four Luxembourg management companies submitted an application to open a branch in one or several other EU Member States in 2013.

	2011	2012	2013
Luxembourg management companies which notified their intention to manage a UCITS from another EU Member State	-	3	6
Luxembourg management companies which notified their intention to establish a branch in another EU Member State	8	3	4

As at 31 December 2013, 17 Luxembourg management companies were represented by a branch in one or several other EU Member States, which represents a total of 40 branches.

• Cross-border mergers and creation of master-feeder structures

The mergers undertaken in 2013 were mainly motivated by the search for economies of scale, particularly by pooling UCITS' assets, which offer similar or even identical investment policies, into one UCITS in Luxembourg so as to create a group UCITS platform specifically intended for international distribution.

Similarly, in order to seek economies of scale, some initiators of UCITS interested in limiting parallel and redundant structures chose to create master-feeder structures.

In 2013, the CSSF dealt with the following merger projects pursuant to the provisions and terms of Chapter IV of the UCITS Directive:

- 41 cross-border merger projects from Spain, Finland, France, Ireland, Netherlands, United Kingdom and Sweden;
- six cross-border merger projects aimed at UCITS from France, United Kingdom and Sweden.

As regards master-feeder structures, the CSSF replied to 46 requests of Luxembourg UCITS to certify that they are eligible to act as master UCITS in accordance with Article 58 of the UCITS Directive. The home Member States of feeder UCITS are Germany, Finland, France, Italy and Sweden.

• Notification procedure of Luxembourg UCITS

Luxembourg UCITS wishing to market their units in another EU Member State must comply with the notification procedure provided for in the UCITS Directive. Notifications are made directly between the supervisory authorities of the Member States by means of a complete file that the UCITS must submit to the supervisory authority of the home Member State.

In 2013, the CSSF received a total of 4,567 notification requests. 2,659 requests were sufficiently complete to be transmitted, without further intervention, to the relevant competent authorities of the host Member States. The other applications had to be returned to the intermediary in order to correct the mistakes in the formats and/or to complete the content in accordance with the rules into force.

One of the aims of the UCITS regulation is to speed up the registration procedure for UCITS in another EU Member State. Thus, the CSSF has five days to process a notification request. In practice, the CSSF has set itself the objective to process a notification request within 24 hours (one working day). Given the deadlines imposed by the regulation, a notification request addressed to the CSSF is transmitted to the competent authority of the host Member State only if it is complete and compliant with the regulatory requirements. An incomplete application will be rejected and returned to the intermediary. The reasons of refusal are communicated to the intermediary which submitted the request. A notification request duly completed and corrected may be submitted at any time and the above-mentioned legal deadline starts to run afresh.

Unfortunately, the CSSF notes that almost 42% of the notification requests must be returned at least once to the applicant for correction before it can be transmitted to the competent authority of the host Member State. The CSSF considers that the objective to simplify the standardised notification procedure, as provided for by the UCITS Directive in order to facilitate the marketing without hindrance of UCITS in another Member State is not yet achieved satisfactorily.

A great number of requests must be rejected because the technical rules which are described in Circulars CSSF 11/509 and CSSF 08/371 and with which the CSSF verifies the compliance when receiving a request, are not observed. Among the most frequent reasons for refusal is the fact that the essential documents like the prospectus, the key investor information document (KIID), the management rules or the articles of incorporation and the financial reports included in the notification request submitted to the CSSF were not yet subject to prior submission to the CSSF as laid down in Circulars CSSF 11/509 and CSSF 08/371 or the prior submission was not yet validated due to the use of a non-compliant nomenclature.

The CSSF recommends to the professionals that they submit a notification request to the CSSF only after having received all the guarantees of internal quality tests that all the technical conditions of the above-mentioned circulars are fulfilled.

2,573 of the 2,659 complete notifications that the CSSF transmitted in 2013 to the competent authorities of the host Member States were accepted without any objection. In order to further improve this rate, the CSSF recommends to the professionals to carefully analyse the motives for refusal which were communicated to them and to put in place appropriate internal controls in order to ensure that, from the first notification, the rules laid down for the marketing of UCITS comply with the laws, regulations and administrative provisions applicable in the host Member State concerned.

Breakdown of the notifications accepted per EU/EEA Member State

Member State	Number
Germany	315
Italy	282
France	220
Spain	204
United Kingdom	203
Austria	202
Sweden	163
Belgium	150
Finland	144
Netherlands	139
Norway	113
Denmark	105
Ireland	66
Portugal	49
Greece	35
Liechtenstein	31
Czech Republic	20
Cyprus	18
Estonia	18
Hungary	18
Poland	15
Slovakia	13
Bulgaria	10
Latvia	10
Lithuania	10
Iceland	8
Gibraltar	5
Malta	4
Slovenia	3
Total	2,573

1.3. Evolution of the SICAR sector

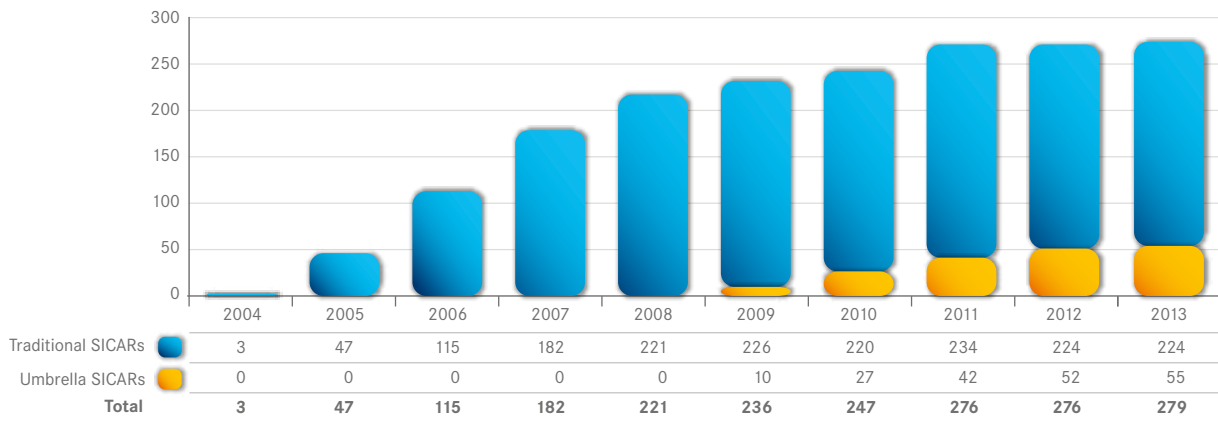
In 2013, the CSSF received 28 files from SICARs applying for registration on the CSSF's official list of SICARs against 29 files in 2012. 12 out of the 28 applications for registration related to umbrella SICARs. Nine files were withdrawn, at the initiators' request, during the scrutiny process.

In 2013, 22 SICARs, including four umbrella SICARs, have been authorised.

19 SICARs were deregistered from the official list for the following reasons: two were in judicial liquidation, four abandoned their SICAR status and 13 opted for voluntary liquidation.

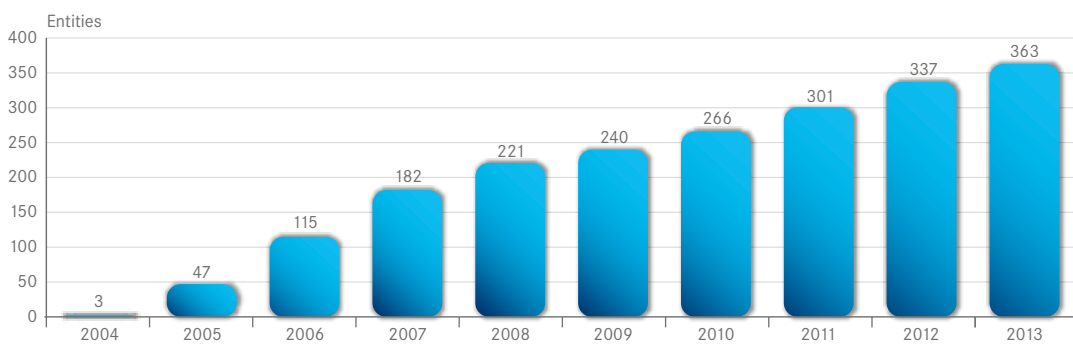
The number of SICARs registered on the CSSF's official list thus slightly rose with 279 SICARs as at 31 December 2013 (276 as at 31 December 2012). These 279 SICARs were subdivided into 224 traditional SICARs and 55 umbrella SICARs. The latter totalled 139 active compartments (113 as at 31 December 2012).

Evolution of the number of SICARs



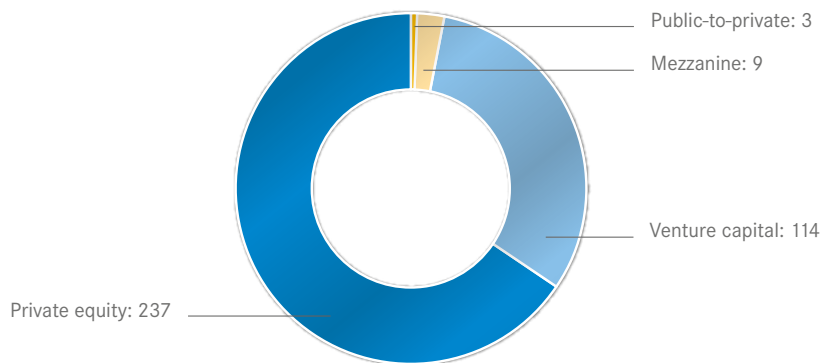
The following statistical information is based on data available from the 224 traditional SICARs and 139 active compartments of the 55 umbrella SICARs which makes a total of 363 “entities”.

Evolution of the number of entities



As far as the entities’ investment policy is concerned, the following graph reveals a preference - in terms of entities - for private equity, the net assets of these entities having increased by 8.86% compared to 2012. Venture capital ranks second, with, however, net assets which decreased by 9.61%. It should be pointed out that net assets of mezzanine grew by 11.47% whereas those of PPP decreased by 86.92%.

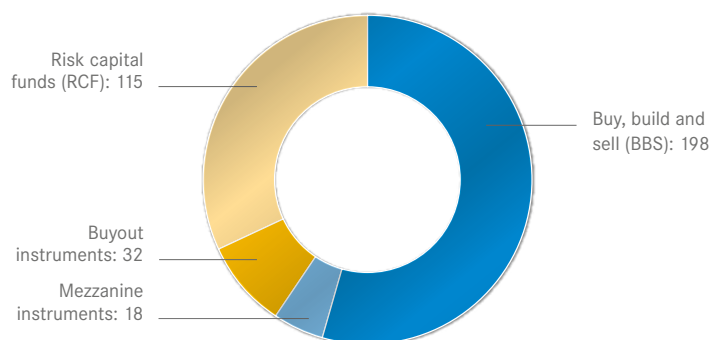
Investment policy - by entities



Investment strategies inherent in the entities may be broken down into four main types: buy, build and sell; buyout instruments; mezzanine instruments and risk capital funds. In practice, combined strategies are

generally used for risk capital. In terms of net assets, buyout instruments recorded an increase by 27.16% and risk capital funds recorded an increase by 45.16% in 2013, whereas buy, build and sell decreased by 19.14% and mezzanine instruments dropped by 34.11%.

Investment strategy - by entities



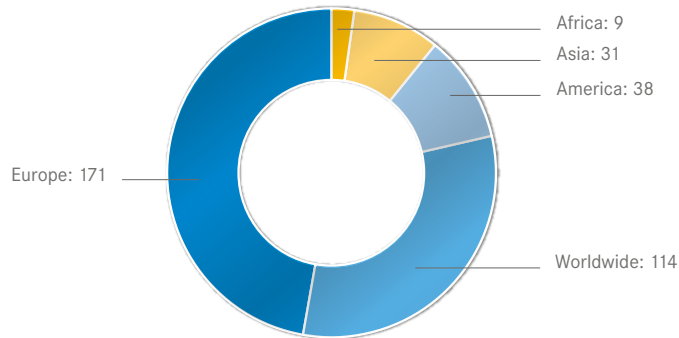
As regards the sector-based distribution, 180 entities preferred not to limit their investment policy to a particular investment sector. Among the entities having adopted a specialised policy, there was a certain concentration in the “Real estate”, “Services”, “Technology” and “Energy” sectors.

Sector-based distribution - by entities

Sector	Number
All sectors	180
Real estate	41
Services	38
Technology	31
Energy	20
PPP	17
Industry	13
Sciences	10
Microfinance	5
Finance	3
Precious metals and gemstones	2
Education and sports	1
Security	1
Sharia	1

As for the geographical area of investments, 47.11% of the 363 entities invested in Europe, whereas 31.40% of entities chose to have the possibility to invest worldwide.

Investment region - by entities



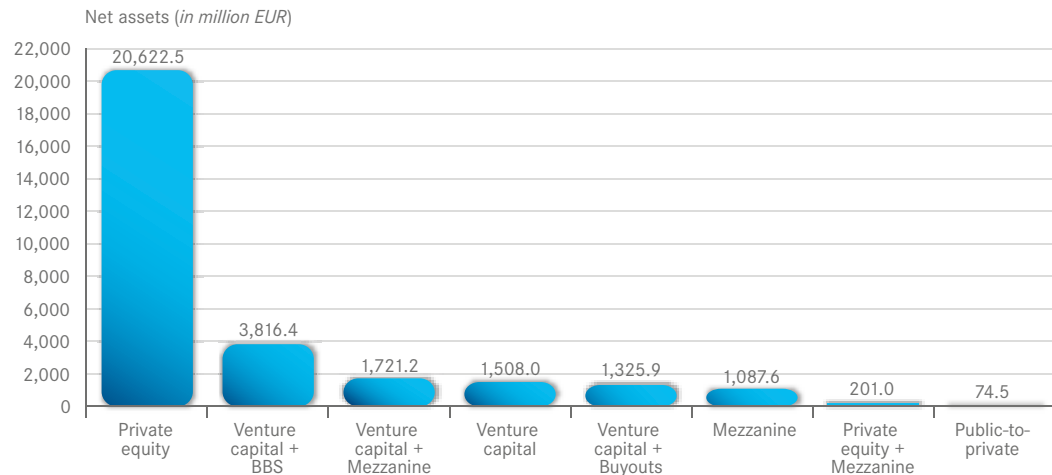
As far as the geographical origin of the initiators is concerned, those from Europe are largely predominant with 88.24%, followed by US initiators with 8.05%.

Geographical origin of the initiators

Country/region	As % of total
France	19.20%
Switzerland	18.27%
Germany	10.53%
Luxembourg	8.67%
Other countries of the euro area	7.74%
United States	6.81%
Spain	5.26%
Italy	5.26%
United Kingdom	4.95%
Belgium	4.33%
Other countries in Europe	4.02%
Rest of the world	2.79%
BRICS ⁴	2.17%
Total	100.00%

Based on the figures available as at 31 December 2013, the capital commitments in entities reached EUR 20.5 billion and their balance sheet total amounted to EUR 32.3 billion.

Breakdown of net assets of entities according to the investment policy



⁴ Brazil, Russia, India, China, South Africa.

2. MANAGEMENT COMPANIES AND ALTERNATIVE INVESTMENT FUND MANAGERS

2.1. Management companies set up under Chapter 15 of the law of 17 December 2010

2.1.1. Evolution in number

As at 31 December 2013, the number of authorised management companies totalled 195 entities against 180 as at 31 December 2012.

Among the 21 management companies newly approved in 2013, 10 entities either changed from investment firms or from management companies set up under Chapter 16 of the 2010 Law or were the result of the restructuring of financial sector entities belonging to the same group. Seven authorisations were granted to players which established in Luxembourg for the first time and which considered the creation of a management company as the logical corollary to the launch of their funds in Luxembourg.

The deregistration of six management companies in 2013 is, as in the past, mainly due to the restructuring within the different groups which led to mergers and cessations of business.

Evolution of the number of management companies set up under Chapter 15 of the 2010 Law

Year	Number of management companies	Registrations on the official list	Deregistrations from the official list	Companies providing collective management services	Companies benefiting from the extended scope of activity	Companies authorised as AIFM
2011	179	11	11	158	21	-
2012	180	6	5	157	23	-
2013	195	21	6	165	30	10

2.1.2. Scope of activity

The corporate purpose of 16 out of the 21 management companies approved in 2013 exclusively covers the collective management within the meaning of Article 101(2) of the 2010 Law. Five entities benefited from the extended scope of activity.

It should also be noted that three existing management companies extended their scope of activity to discretionary management and/or investment advice whereas one management company gave up its authorisation to provide discretionary management services.

The law of 12 July 2013 on alternative investment fund managers gives the management companies subject to Chapter 15 of the 2010 Law the possibility to also adopt the status of AIFM. As at 31 December 2013, 10 out of the 195 management companies were authorised as AIFM.

2.1.3. Geographical origin

Over the last years, the management companies from Germany, Switzerland, France and Italy were predominant in Luxembourg.

This trend was confirmed in 2013 with over one-third of the 21 newly authorised management companies coming from these countries. It can also be noted that other countries like the United States or Sweden are currently increasing their presence in Luxembourg through the creation of management companies.

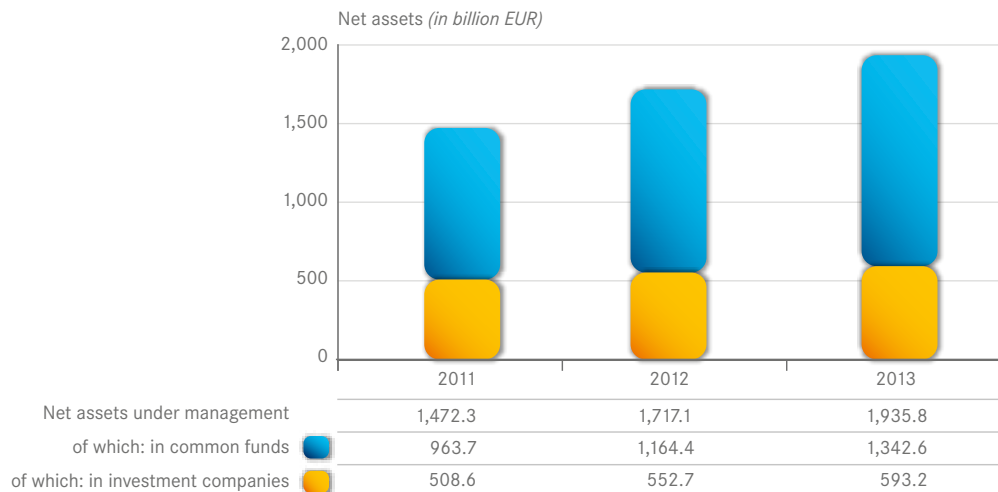
Geographical origin of management companies

Country	2011	2012	2013
Germany	41	40	38
Switzerland	31	30	31
France	18	20	23
Italy	21	19	20
United Kingdom	12	12	13
United States	7	9	12
Luxembourg	8	8	10
Belgium	8	8	9
Others	33	34	39 ⁵
Total	179	180	195

2.1.4. Assets under management

As at 31 December 2013, the management companies subject to Chapter 15 of the 2010 Law manage 74% of the net assets of UCIs (i.e. EUR 1,935.8 billion against EUR 1,717.1 billion in 2012). This increase of EUR 218 billion is not exclusively attributable to positive net subscriptions and to the increase in stock markets. The increase is also linked to the companies newly authorised following changes in the existing structures and the integration of old self-managed investment companies to the management company of their choice after abandoning their status, insofar as they all already had their asset portfolio under management.

Evolution of the net assets of management companies



⁵ Andorra (1), Austria (1), Bermuda (1), Canada (2), Denmark (4), Greece (3), Iceland (2), Japan (2), Jersey (1), Liechtenstein (2), Malta (1), Netherlands (4), Norway (1), Portugal (2), Republic of Mauritius (1), Russia (2), Spain (3), Sweden (5), United Arab Emirates (1).

Breakdown of management companies in terms of assets under management

Assets under management (in EUR)	2011	2012	2013
> 20 billion	24	26	30
10 to 20 billion	14	15	14
5 to 10 billion	10	10	22
1 to 5 billion	48	52	52
500 million to 1 billion	19	14	9
100 to 500 million	30	32	32
< 100 million	34	31	36
Total	179	180	195

2.1.5. Evolution of employment

Management company staff recorded an upward trend in 2013. The number of employees rose from 2,743 as at 31 December 2012 to 3,253 as at 31 December 2013, i.e. an increase by 510 people over a year. The positive development is partially due to the change of status of some investment firms resulting in a transfer of personnel as well as to the reorganisation of certain big groups in Luxembourg with, as a consequence, the internal assignment of personnel to the management companies. The efforts made by the management companies to continuously enhance their organisational environment is also a factor to be taken into account in this context.

2.1.6. Compliance with Circular CSSF 12/546

Following the publication of Circular CSSF 12/546, the management companies subject to Chapter 15 of the 2010 Law had to submit a file showing that they comply with the circular concerned until 15 April 2013 at the latest.

The analysis made by the CSSF in 2013 in order to verify if the management companies fulfil the requirements of the circular in terms of substance and organisation revealed that the companies made efforts to comply with all the points. The compliance came together with the enhancement of the substance corresponding to an increase in staff, particularly so as to ensure the follow-up of the delegates, the presence of two resident directors and own premises. With a few exceptions, all the management companies subject to Chapter 15 of the 2010 Law showed that they comply with the requirements of Circular CSSF 12/546. Through compliance with Circular CSSF 12/546, these management companies contribute to achieving the objective which is to maintain a high level of investor protection following the abandonment of the concept of promoter.

Whereas the majority of management companies complied with the provisions of Circular CSSF 12/546, 18 management companies were still in the process of becoming compliant. The CSSF would like to specify that it considers as very important the fact that the management companies get the necessary human resources and technical infrastructure that allow them to assume their responsibilities.

It is interesting to note the impact of Circular CSSF 12/546 on the investment companies which did not designate a management company within the meaning of Article 27 of the 2010 Law (self-managed SICAV - SIAG). Indeed, over two-thirds of SIAGs decided in 2013 to designate a management company subject to Chapter 15 of the 2010 Law or to create such a management company. A smaller number of SIAGs chose to designate a management company which is authorised for the management of UCITS in another EU Member State and which exercises its activities under the free provision of services pursuant to Directive 2009/65/EC.

2.1.7. Balance sheet and profit and loss account

The provisional balance sheet total of management companies reached EUR 9,865 million as at 31 December 2013, compared with EUR 7,502 million as at 31 December 2012.

The provisional aggregate net profits amounted to EUR 2,012 million as at 31 December 2013, against EUR 1,768 million as at 31 December 2012. This growth resulted from the rise in net assets under management boosting current operating income.

2.2. Alternative investment fund managers subject to the law of 12 July 2013 on alternative investment fund managers

2.2.1. Number of alternative investment fund managers (AIFMs)

The year 2013 was marked by the entry into force of the law of 12 July 2013 on alternative investment fund managers (AIFM Law). Due to the entry into force of the law in the second half of the year under review, the number of entities authorised at the end of the year remained limited. Thus, as at 31 December 2013, 12 entities were approved as AIFM. Most of these entities already benefited from another authorisation with the CSSF and wished to complete or transform their existing structures. The profile of these companies was as follows:

- 10 requests from management companies set up under Chapter 15 of the 2010 Law;
- one request concerned the setting-up of a management company under Chapter 16 of the 2010 Law, completed by an AIFM licence;
- one request from a management company set up under Chapter 16 of the 2010 Law.

Moreover, all these entities requested an authorisation as external AIFM within the meaning of Article 4(1)(a) of the AIFM Law. However, as at 31 December 2013, no entity was authorised by the CSSF as an internal AIFM within the meaning of Article 4(1)(b) of the AIFM Law. For further explanations on the difference between an external and an internal AIFM, reference is made to item 2.2.9. below and to Question 1.e) of the “Frequently Asked Questions” (FAQ) on alternative investment fund managers published by the CSSF.

2.2.2. Analysis of the AIFM authorisation files

Access to the AIFM activity, whether for an external or an internal AIFM, is subject to prior authorisation granted by the CSSF. To this end, a qualitative analysis of the authorisation file is made by the CSSF which is particularly focussed on the following elements:

- the transparency of the direct and indirect shareholder structure of the AIFM;
- the quality of the shareholders that have a qualifying holding in the AIFM;
- the persons composing the AIFM bodies;
- the internal organisation of the AIFM with the number of persons, including the managers, employed by the AIFM in Luxembourg, the setting-up of an administrative and decision-making centre at the level of the AIFM, the internal governance framework of the AIFM;
- the extent of the activities in relation to portfolio management and risk management that are delegated, and
- the risk management method.

In order to meet the qualitative criteria listed above, reference is made to Circular CSSF 12/546 that the CSSF applies by analogy to the authorisation requests and organisation of AIFMs. Similarly to the management companies of UCITS, the CSSF insists that AIFMs, that are established in Luxembourg or that have to adapt to the AIFM Law, set up the necessary substance to provide quality services to alternative investment funds that they manage and to assume their responsibilities.

2.2.3. AIFM activities

As regards the main activities of AIFMs as defined in Annex I of the AIFM Law, most of the entities authorised as at 31 December 2013 chose to carry out internally the activities of risk management. The activities of portfolio management are either partially or entirely delegated to entities of the group or to specialised managers.

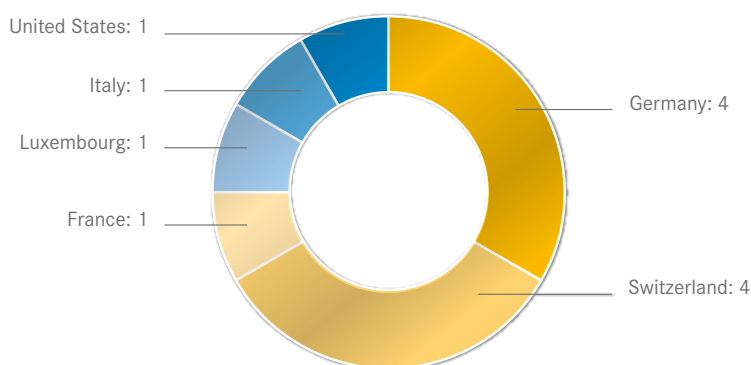
In addition, among the 12 entities authorised as at 31 December 2013, only one entity decided to extend its scope of activities to discretionary management.

2.2.4. Geographical origin of AIFMs

Since 10 out of the 12 authorised AIFMs were already approved as management companies subject to Chapter 15 of the 2010 Law, there is a correlation between the geographical origin of AIFMs and the management companies subject to Chapter 15 of the 2010 Law. Thus, the main countries of origin of AIFMs are Germany, Switzerland and France.

It should also be noted that at the end of 2013, one non-EU manager decided to be established in Luxembourg.

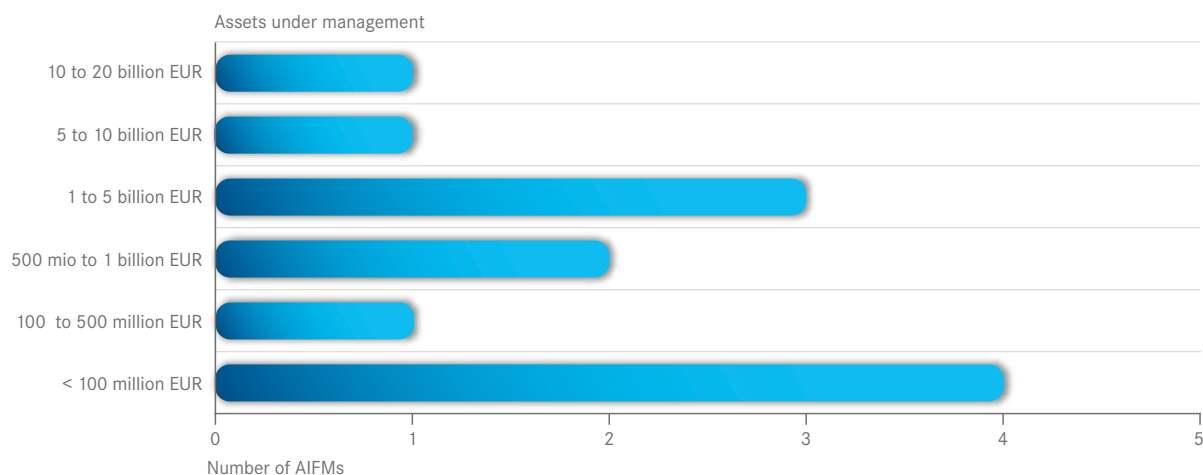
Geographical origin of AIFMs



2.2.5. Assets managed by AIFMs

As at 31 December 2013, total net assets of alternative investment vehicles managed by AIFMs amounted to EUR 26.9 billion. It should be noted that five out of the 12 AIFMs manage assets amounting to over one billion euros.

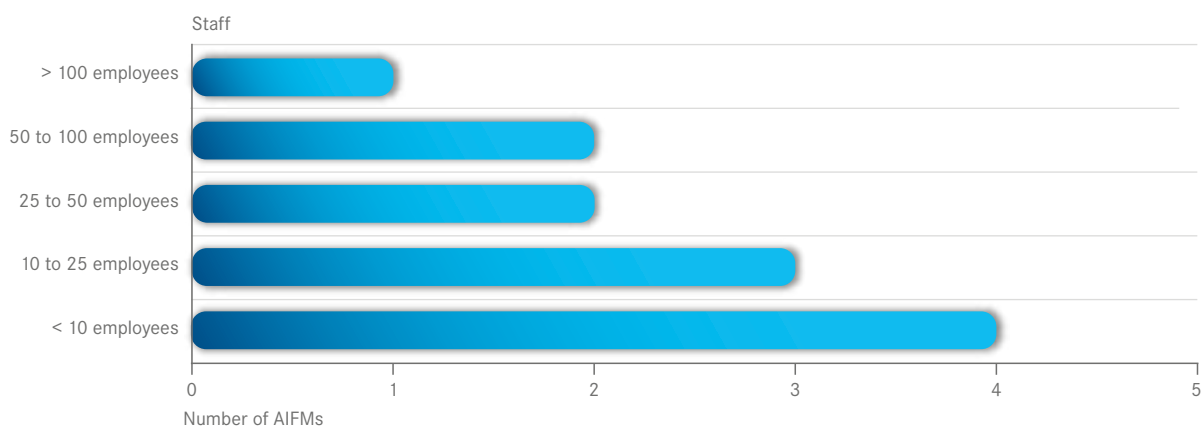
Breakdown of AIFMs in terms of assets under management



2.2.6. AIFM employment

The average staff of AIFMs as at 31 December 2013 amounted to 35 people. However, this average must be put in perspective, as one player has a total staff of over 100 people.

Breakdown of AIFMs per number of employees



2.2.7. EuVECA and EuSEF

As at 31 December 2013, no authorisation request for an EuVECA in accordance with Regulation (EU) No 345/2013 of 17 April 2013 on European venture capital funds or for an EuSEF in accordance with Regulation (EU) No 346/2013 of 17 April 2013 on European social entrepreneurship funds was submitted to the CSSF.

2.2.8. Publication of Frequently Asked Questions (FAQ) on AIFMs

Since 18 June 2013, the CSSF publishes FAQs relating to AIFMs on its website. These FAQs are updated regularly and available at <http://www.cssf.lu/en/supervision/ivm/aifm/faq/>.

2.2.9. External/internal management under the AIFM Law as regards common funds (FCP) and limited partnerships

Among the FAQs mentioned under item 2.2.8. above, the CSSF would like to point out, in particular, the question on the difference between an external and internal AIFM.

In accordance with the AIFM Law, each alternative investment fund (AIF) established in Luxembourg whose management is subject to the scope of application of the AIFM Law, must have one single AIFM responsible to ensure the compliance with the provisions of the law. This AIFM is either external or, where the legal form of the AIF permits an internal management and where the AIF's governing body chooses not to appoint an external AIFM, the AIF itself which is then authorised or registered as AIFM.

The CSSF considers that the legal form of an FCP does not permit an internal management given that the FCP is not a legal person and is, therefore, not qualified as AIFM as defined in Article 1(46) of the AIFM Law. Consequently, the AIFs which adopted the form of an FCP must be AIFs with an external AIFM. The prospectus or the issue document of the AIF-FCP concerned must clearly indicate the manager to consider as external AIFM of the FCP.

Furthermore, the CSSF considers that the legal form of a special limited partnership does not permit an internal management given that the latter is not a legal person and falls, therefore, not under the definition of AIFM as provided for in Article 1(46) of the AIFM Law.

The CSSF considers that the AIFs which adopted the legal form of a partnership limited by shares or a limited partnership are, in principle, AIFs with an external AIFM. As these legal forms allow also an internal management within the meaning of the AIFM Law, it is possible that such an AIF can qualify as an internal AIFM. As it is considered that the governing body of the AIF is the governing body of the manager, the business purpose of the latter must be limited to the management of the single AIF.

For further information on the legal persons likely to be appointed as AIFMs, reference is made to question 1.e) of the FAQs published on the CSSF website at: http://www.cssf.lu/fileadmin/files/AIFM/FAQ_AIFMD.pdf.

3. DEVELOPMENTS IN THE REGULATORY FRAMEWORK

3.1. Circular CSSF 13/557

Circular CSSF 13/557 of 23 January 2013 concerns Regulation (EU) No 648/2012 of 4 July 2012 on OTC derivatives, central counterparties and trade repositories (EMIR).

3.2. Circular CSSF 13/559

Circular CSSF 13/559 of 18 February 2013 transposes into the Luxembourg legislation applicable to UCITS subject to Part I of the 2010 Law the “Guidelines for competent authorities and UCITS management companies - Guidelines on ETFs and other UCITS issues” (ref. ESMA/2012/832EN) published by ESMA on 18 December 2012. These guidelines are appended to the circular.

3.3. Circular CSSF 13/564 - Circular BCL 2013/231

The purpose of Circular CSSF 13/564 of 28 March 2013 published together with the BCL is to modify the statistical data collection from money market funds and non-money market funds.

3.4. Circular CSSF 14/581

Circular CSSF 14/581 of 13 January 2014 concerns the new reporting obligations for alternative investment fund managers. The purpose is to clarify the technical details that AIFMs need in order to fulfil their reporting obligations.

4. PRUDENTIAL SUPERVISORY PRACTICE

4.1. Prudential supervision

4.1.1. Objectives and instruments of supervision of UCIs and SICARs

The CSSF's permanent supervision aims to ensure that UCIs and SICARs subject to its supervision observe all legal, regulatory and contractual provisions relating to the organisation and operation of UCIs and SICARs, as well as to the distribution, investment or sale of their securities. The aim of this supervision is to ensure adequate investor protection as well as stability and security in the sector. This supervision is based, among others, on:

- the examination of the periodic financial information which UCIs and SICARs must submit to the CSSF;
- the analysis of the information collected by the CSSF with respect to the specific reporting (e.g. leveraged UCITS, money market UCIs) and ad hoc reporting;
- the analysis of annual reports which UCIs and SICARs must publish for their investors;

- the analysis of the long form reports of UCIs and management letters of UCIs and SICARs issued by the *réviseur d'entreprises* (statutory auditor) and that must be immediately transmitted to the CSSF;
- the analysis of statements made in accordance with the circular on the protection of investors in the case of a NAV (net asset value) calculation error and correction of the impacts of non-compliance with the investment rules applicable to UCIs;
- the on-site inspections carried out by CSSF agents.

4.1.2. Objectives and instruments of supervision of management companies subject to Chapter 15 of the 2010 Law and AIFMs

The CSSF ensures that the management companies subject to Chapter 15 of the 2010 Law and the AIFMs comply with all the legal and regulatory provisions relating to their organisation and operation. This permanent supervision is based in particular on:

- the verification of compliance with the conditions for obtaining and maintaining the authorisation of a management company and an AIFM;
- the examination of the annual financial reports which the management companies and AIFMs must submit to the CSSF;
- the analysis of the reports drawn up by the internal audit during the past year;
- the analysis of the information on the state of the compliance function and on the main observations made in this context;
- the analysis of the risk management procedures;
- the on-site inspections carried out by CSSF agents.

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4.2. Review of financial information for the CSSF and the STATEC

In accordance with Circulars IML 97/136, CSSF 07/310 and CSSF 08/348 and pursuant to Article 147 of the 2010 Law and Article 58 of the SIF Law, the head offices of Luxembourg UCIs must transmit financial information to the CSSF by electronic means, on a monthly (tables O1.1.) and a yearly (tables O4.1. and O4.2.) basis. The deadline to transmit the monthly financial information is 10 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. The deadline to transmit the information is four months for UCITS governed by Part I of the 2010 Law and six months for UCIs governed by Part II of the 2010 Law and SIFs.

As far as monthly financial information is concerned, the CSSF considers that UCIs must, on the one hand, strictly observe the defined deadline for the transmission to the CSSF and, on the other hand, pay due attention when preparing the above-mentioned table so as to ensure that the format and content are correct.

The CSSF carries out quality and coherence controls of the data received and takes, where necessary, sanction measures in case the reporting entities do not comply with their obligations.

In this context, the CSSF would also like to remind that it published “FAQ concerning O1.1. Reporting” in order to clarify some recurring questions in relation to table O1.1..

4.3. 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 generally drawn up in accordance with the applicable legal rules.

In the framework of the annual reports drawn up by SIFs, the CSSF noted a certain trend to present the SIF's exposure to its final investments too shortly.

Even if the SIF Law does not include the obligation to report each line of the investment portfolio in the annual report, the CSSF reminds that pursuant to Article 52(4) and the Annex to the SIF Law, this report must

comprise any significant information, including, among others, qualitative and/or quantitative information on the investment portfolio, enabling investors to make an informed judgment on the development of the activities and the results of the SIF.

In this context and in accordance with the SIF Law, the CSSF expects also that these annual reports adopt a look-through approach at the level of the subsidiaries held by the SIF (as, for instance, ad hoc entities) in order to facilitate its investments in the underlying investments of the subsidiary.

Similarly to the SIFs' obligations, the CSSF requires the same level of transparency to be applied in the annual reports of SICARs.

Finally, the CSSF requires that the model of the report of the *réviseur d'entreprises agréé* (approved statutory auditor), specifically laid down for UCIs (UCITS, UCIs Part II and SIFs) in the Technical Note NT2011-05 of the Council of the IRE, also be used for the reports of the *réviseur d'entreprises agréé* on SICARs.

4.4. Specific supervision carried out in 2013 based on the long form report in accordance with Circular CSSF 02/81 and the management letters of UCIs and SICARs

4.4.1. Context and submission deadline

Introduced by Circular CSSF 02/81 of 6 December 2002 which sets the practical rules concerning the mission of the *réviseur d'entreprises* of UCIs, the purpose of the long form report is to inform of the observations that the *réviseur d'entreprises agréé* made during his/her audit relating to the financial and organisational aspects of the UCI, among which, in particular, the relations with the central administration, the depositary bank and the other intermediaries (managers, transfer agents, distributors, etc.).

The CSSF would like to remind that the deadline for the transmission of the annual report of UCIs subject to Part II of the 2010 Law changed following the amendment of Article 150(2) of that law when the AIFM Law entered into force. Thus, for UCIs subject to Part II of the 2010 Law, the CSSF considers that the deadline of four months for the submission of the long form report and the management letter is also extended to six months. For UCIs subject to Part I of the 2010 Law, the deadline for the submission of the long form report and the management letter remains at four months.

It should be borne in mind that UCIs and SICARs must transmit to the CSSF, forthwith and spontaneously, the management letters issued by the *réviseur d'entreprises agréé* in the context of the audits that the latter performs in accordance with the regulatory requirements.

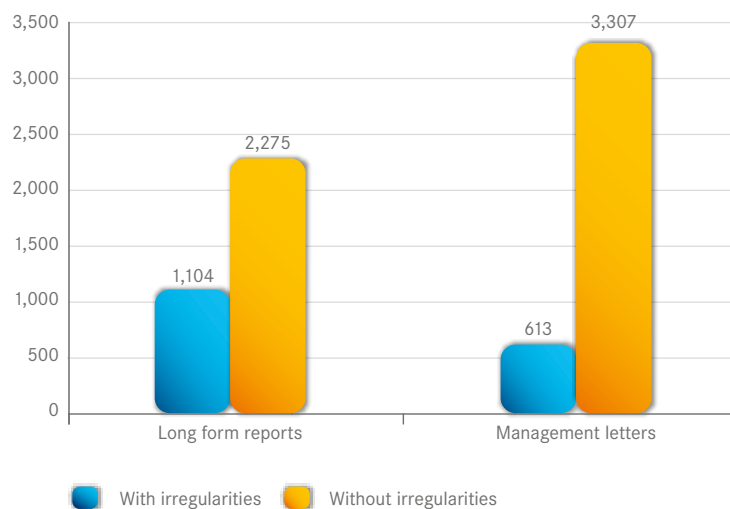
4.4.2. Results of the specific supervision

• UCIs

In the framework of the review of the long form reports and management letters of UCIs, the CSSF had to take decisions, in the form of injunctions, formal requests and recommendations to the attention of directors of some UCIs. These decisions aim to remedy organisational deficiencies noted by the *réviseur d'entreprises agréé* in the reports and management letters. In 2013, the CSSF sent 194 letters to require changes in order to remedy the situation described by the *réviseur d'entreprises agréé*.

The following table highlights the number of long form reports and the number of management letters in which one or several deficiencies were noted by the *réviseur d'entreprises agréé* and which were subject to a review by the CSSF. It should be noted that the reports or management letters received in 2013 mainly concerned the year 2012.

Long form reports and management letters received in 2013



In 2013, the proportion of long form reports in which the *réviseur d'entreprises agréé* observed a deficiency or a point to improve was 33% of all the reports received. 16% of the management letters received included a comment by the *réviseur d'entreprises agréé*, of which a large proportion in relation to the simplified procedures within the scope of Circular CSSF 02/77.

As far as the data of the table below is concerned, it should be pointed out that each intervention may have covered several recommendations or formal requests.

Breakdown of interventions according to themes

Theme	Relative share
Circular CSSF 02/77	24.7%
Accounting	12.7%
AML/CFT	11.0%
Fees and commissions	8.8%
Reconciliation	8.1%
Legal	7.8%
Valuation	7.5%
Prospectus	5.2%
Investments	4.9%
Annual reports	3.9%
Risk management	2.3%
Portfolio turnover	2.3%
Late trading/Market timing	1.0%
Total	100.0%

• SICARs

In the framework of the review of the annual reports and management letters of SICARs, the CSSF had to take decisions, in the form of injunctions, formal requests and recommendations to the attention of the directors of some SICARs. These decisions aim to remedy deficiencies (for example, organisational) noted by the *réviseur d'entreprises agréé* in the reports or management letters. In 2013, the CSSF sent 75 letters to require explanations and/or measures to be taken in order to remedy the situation described by the *réviseur d'entreprises agréé*.

The following table highlights the number of annual reports and management letters of SICARs in which one or several deficiencies were noted by the *réviseur d'entreprises agréé* and which were subject to a review and follow-up by the CSSF. It should be noted that 12% of the management letters received included comments made by the *réviseur d'entreprises agréé* on one or several deficiencies or one or several points to be improved, a large part of which relates to the compliance with the legal and regulatory provisions as well as to valuation issues.

It should be noted that the reports and management letters received in 2013 mainly concerned the year 2012.

In 2013, the proportion of the annual reports of SICARs in which the *réviseur d'entreprises agréé* issued a modified opinion or an impossibility to express an opinion or in which s/he included a paragraph with observations was 14% of all the annual reports received.

Breakdown of the specific interventions for SICARs

	Number	in %
Annual reports received in 2013	257	
Management letters	32	12%
Accounting or valuation problems	8	
Non-compliance with the legal/regulatory provisions	15	
Weaknesses in relation to internal control and/or procedures	4	
Problems in relation to the supervision and control by the management body	1	
Problems in relation to the business continuity or financial situation	3	
Miscellaneous	1	
Management letters that contain no recommendations	225	88%
Interventions⁶ in relation to the management letter	32	
Interventions⁶ in relation to the report of the <i>réviseur d'entreprises agréé</i>	43	

4.4.3. Requests for derogation from the obligation to submit a long form report in accordance with Circular CSSF 02/81

In accordance with Circular CSSF 02/81, all UCIs (except SIFs) must submit a long form report for each financial year, including the partial financial year following the liquidation of a UCI, a dissolution or a merger. The CSSF may allow the derogation, based on a case-by-case analysis, from the obligation to submit a report for such shortened financial years provided that a formal request be made to the CSSF during the procedure of deregistration from the official list.

It is also specified that the CSSF does not grant the derogation from the obligation governing UCIs and SICARs to submit for each financial year, including the last shortened financial year, the management letter or the written declaration from the *réviseur d'entreprises* where that said letter was not issued.

⁶ Each intervention could have covered several recommendations or formal requests.

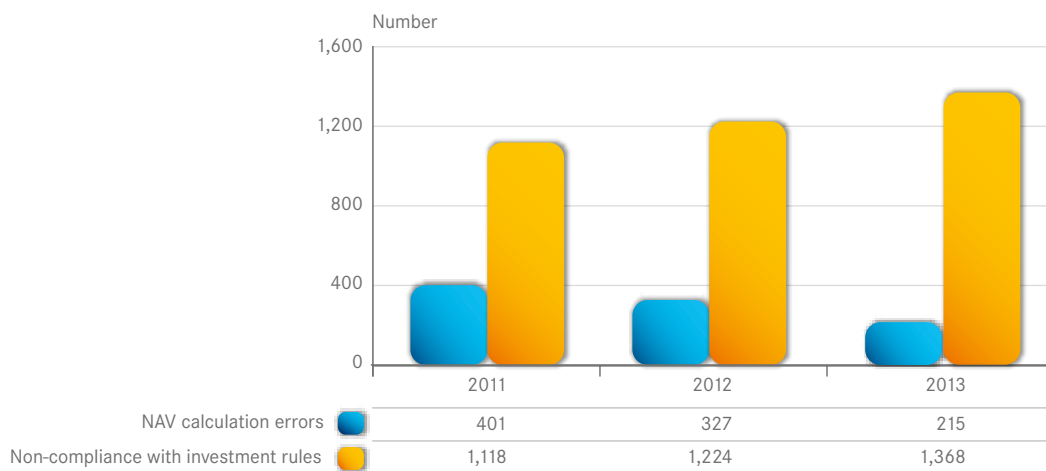
4.5. Circular CSSF 02/77 on the protection of investors in case of NAV calculation error and correction of the consequences resulting from non-compliance with the investment rules applicable to UCIs⁷

4.5.1. Declarations made in 2013 on the basis of Circular CSSF 02/77

In 2013, the CSSF received 1,583 declarations on the basis of Circular CSSF 02/77, compared with 1,551 declarations in 2012, representing a slight increase (+2.1%) similar to the one from the previous year.

Among these declarations, 215 cases (327 in 2012) concerned NAV calculation errors and 1,368 cases (1,224 in 2012) concerned non-compliance with investment rules.

Evolution of the number of NAV calculation errors and cases of non-compliance with investment rules reported to the CSSF over the last three years



In 2013, the number of cases of non-compliance with investment rules increased (+11.8%) compared to 2012, mostly due to an increase in non-compliance with the investment policy as laid down in the prospectus. NAV calculation errors decreased by 34.3% compared to the previous year, which confirms the trend observed the past few years. This decrease may be, at least partially, explained by an enhancement of the controls at some central administrations with which the CSSF intervened in order to request a reinforcement of the arrangements in place.

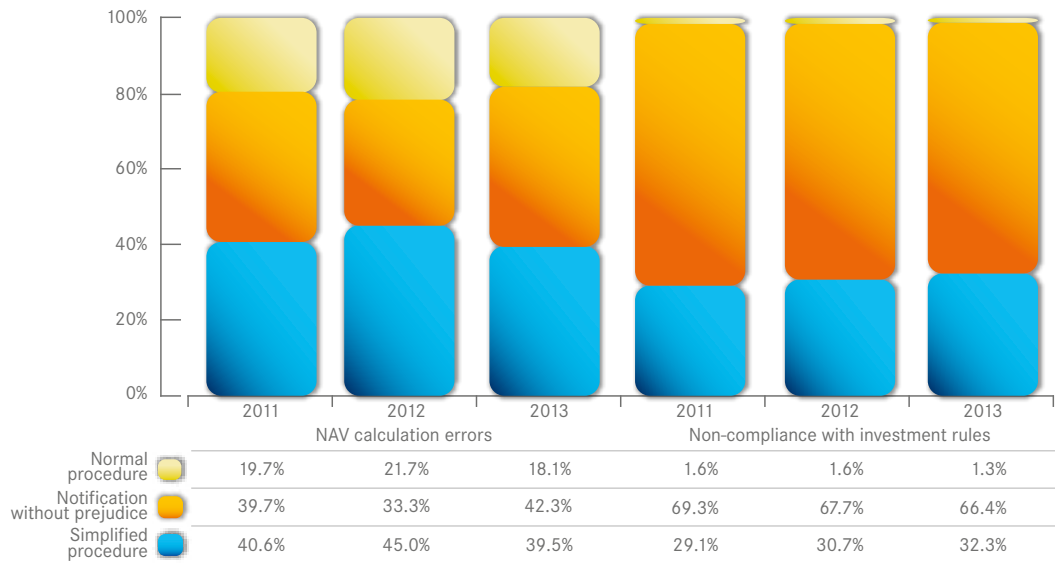
As regards more particularly the declarations of NAV calculation errors received in 2013, seven cases among the declarations for which the normal procedure is applicable could not be closed on 31 December 2013. This is mainly due to the fact that the CSSF is still awaiting either further information or confirmations from the *réviseur d'entreprises* (as provided for in Circular CSSF 02/77).

In 2013, 176 cases out of 215 NAV calculation errors (256 cases out of 327 cases in 2012) applied the simplified procedure, in that the compensation amounts did not exceed EUR 25,000 and the amounts to be reimbursed to an investor did not exceed EUR 2,500. Out of the 1,368 cases of non-compliance with investment rules, the simplified procedure was also applied in 1,350 cases, of which 908 cases (67%) did not cause any prejudice to the investor or UCI.

The following graph plots the proportion of the cases of simplified procedure compared to the total number of declarations received over the last three years, as well as the instances of non-compliance with investment rules that were resolved without harming the investors and the UCIs.

⁷ On this topic, please refer also to item 5. of Chapter XII "Public oversight of the audit profession".

Simplified procedure

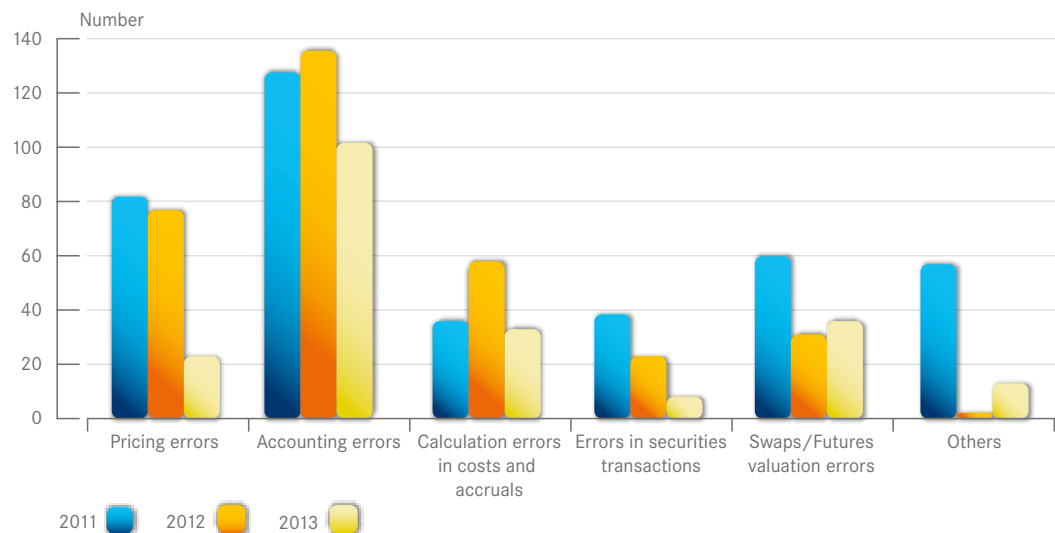


The origin of NAV calculation errors can be divided into five categories: pricing errors, accounting errors, errors in the calculation of costs and accruals, errors in the valuation of swaps or futures and other errors.

During the relevant period, NAV calculation errors were mainly due to accounting errors (47%), errors in the valuation of swaps/futures (17%) and errors in the calculation of costs and accruals (15%).

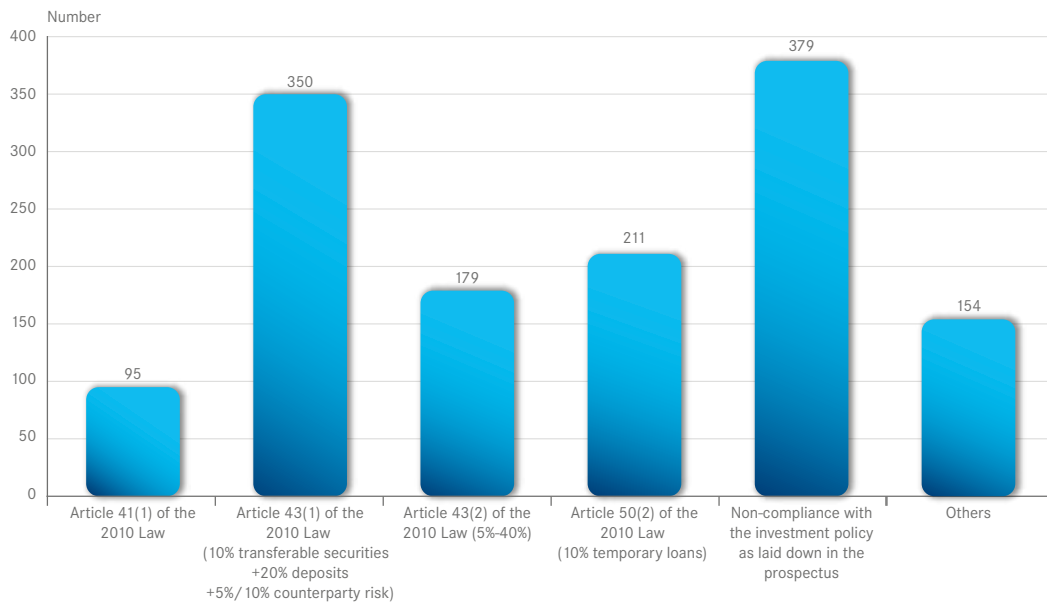
The following table shows the development of the origin of NAV calculation errors as from 2011 and highlights that accounting errors, which decreased compared to 2012, were the main causes of NAV calculation errors. Pricing errors recorded a strong decrease compared to the previous year.

Evolution of the origin of NAV calculation errors over the last three years



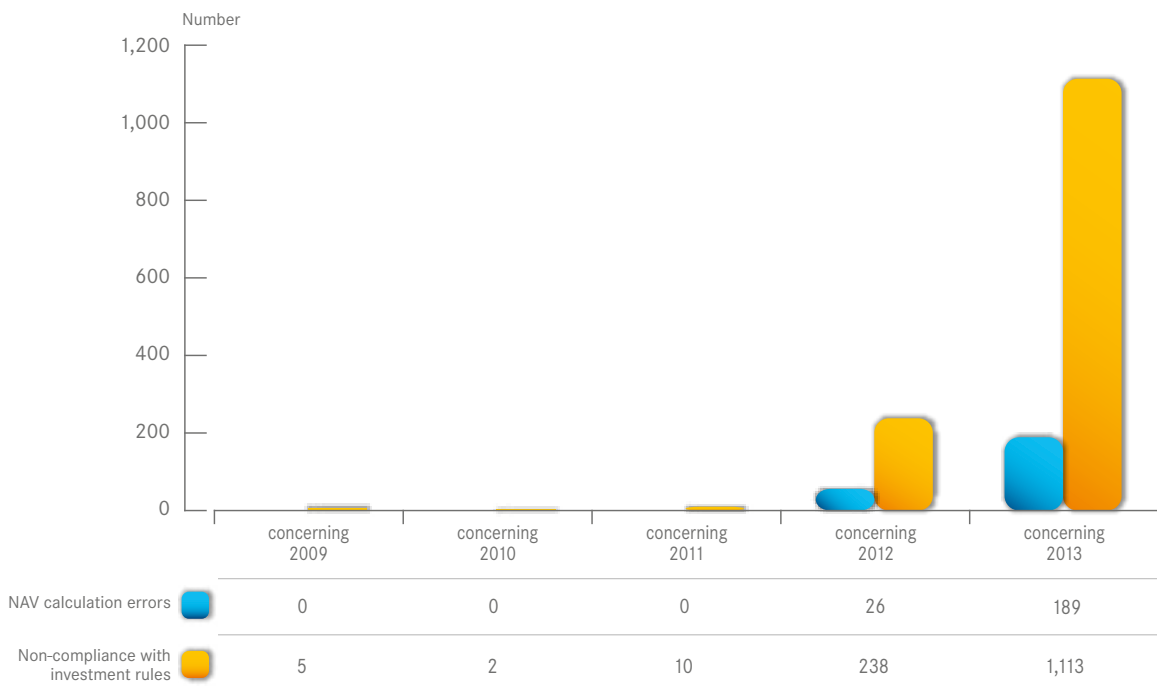
The following graph shows the origin of the non-compliance with the investment rules which were recorded in 2013 and highlights that this non-compliance was mainly due to the non-compliance with the investment policy as laid down in the prospectus (28%) as well as the non-compliance by UCITS of the legal limits provided for in the 2010 Law, such as the 20% limit in deposits laid down in Article 43(1).

Origin of non-compliance with investment rules in 2013



It should be noted that the declarations of NAV calculation errors and of non-compliance with investment rules received in 2013 not only related to errors and instances of non-compliance which actually occurred in 2013. They may in fact relate to errors or instances of non-compliance which were detected in 2013, but which occurred in a previous period. The following graph highlights this effect of timing difference.

Declarations submitted in 2013



During the period concerned, the CSSF noted some delays in the process for notification of NAV calculation errors and non-compliance with investment rules.

The CSSF would like to remind that, in accordance with Circular CSSF 02/77, “as soon as a significant calculation error is discovered, the head office of the UCI must immediately advise the promoter and the custodian of the UCI as well as the CSSF of the occurrence of the error”. The CSSF considers that non-compliance with investment rules must also be reported immediately.

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

The table below sets out the detailed compensation amounts notified in 2012 and 2013. It should be stressed that the CSSF data as at 31 December 2012 and 31 December 2013 are not complete as the final compensation amounts had not been finalised for a certain number of files.

<i>(in EUR)</i>	Investors ⁸		UCI/Sub-fund	
	2012	2013	2012	2013
Total amount of compensation following NAV calculation errors	4,118,620.48	1,662,958.78	3,647,417.21	2,702,763.08
Total amount of compensation following non-compliance with investment rules	592,034.05	4,081.88	2,987,118.47	1,743,320.53

As regards the NAV calculation errors, the compensation amounts paid out in the context of the declarations made in 2013 fell significantly compared to those paid for declarations made in 2012. This variation is proportionate to the decrease in the number of notifications relating to NAV calculation errors.

As regards instances of non-compliance with investment rules, the compensation amounts paid out in the context of the declarations made in 2013 also fell significantly compared to those paid for declarations made in 2012. This decrease was mainly due to two UCIs impacted in 2012 by a non-compliance with investment limits that required major compensation to be paid out for the consequences of non-compliance with investment rules.

4.5.3. Application of Circular CSSF 02/77 to SIFs

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 does not automatically apply to SIFs. However, the CSSF considers that SIFs may either opt for the application of Circular CSSF 02/77 or set other internal rules that must remain within reasonable limits with respect to the SIF’s investment policy.

In this context, the CSSF considers that SIFs that did not set specific internal rules must apply Circular CSSF 02/77. Moreover, as regards the notification process, any NAV calculation error as well as any instance of non-compliance with investment rules by a SIF must be subject to a notification to the CSSF, whether the SIF chose to apply Circular CSSF 02/77 or to set other specific internal rules.

4.5.4. Application of the “economic” method in the framework of the correction of an instance of non-compliance with investment rules in accordance with Circular CSSF 02/77

As regards the determination of the compensation in case of non-compliance with investment rules, the CSSF would like to remind that pursuant to Circular CSSF 02/77, “the damage must be determined in principle by reference to the loss of the UCI resulting from the realisation of the non-authorised investments. By exception to the preceding principle and to the extent there is adequate justification therefore, methods other than those described above may be used to determine the suffered damage including in particular the method which

⁸ The compensation paid to investors results from instances of non-compliance, where the compensation paid to the UCI/sub-fund had a significant impact leading to a NAV calculation error.

consists in determining the damage by reference to the performance which would have been realised if the non-authorised investment had been subject to the same fluctuations as the portfolio invested in compliance with the investment policy and investment restrictions provided for by the law or the prospectus”.

Such a comparative performance, pursuant to the method commonly known as “economic method” may only be accepted if it is exclusively in the interest of the investors and compliant with the principles of the fund’s investment policy as laid down in the offering document. The method must be either laid down directly in the prospectus of the fund pursuant to a given performance benchmark, or chosen so as to accurately reflect the fund’s investment policy.

The CSSF also reminds that the chosen method must be maintained in order to ensure coherence in time for dealing with non-compliance with investment rules concerning a given UCI.

Moreover, the CSSF expects that the management companies and investment companies have a duly documented internal policy governing the dealing with non-compliance with investment rules. This policy must, for each UCI and preferably as soon as the UCI is launched, cover, among others, the choice of the method for determining the compensation, including the comparative performance to be used once the decision was made to use the “economic method”.

Then, the mandated *réviseur d’entreprises* of the UCI must verify in the context of the works laid down in Circular CSSF 02/77 that the method for determining the compensation and the comparative performance used did not prejudice the investors’ interests.

4.6. Meetings

In 2013, 303 meetings were held between representatives of the CSSF and intermediaries of UCIs and SICARs. These meetings concerned the presentation of new projects of UCIs and SICARs, restructurings of UCIs and SICARs and the application of the laws and regulations pertaining to UCIs and to SICARs.

4.7. Eligibility of US ETFs under Article 41(1)(e) of the 2010 Law

ESMA specified in its opinion called “Article 50(2)(a) of the Directive 2009/65/EC” (ESMA 2012/721) of 20 November 2012 that Article 50(2)(a) only refers to transferable securities and money market instruments other than those referred to in Article 50(1)(a) to (d) and Article 50(1)(h) of Directive 2009/65/EC and that it does not apply to units of UCIs.

Following this opinion and the CSSF’s press release 12/46, the CSSF received several requests for reclassification of UCIs which were until then considered as UCIs eligible under Article 41(2)(a) of the 2010 Law. These requests aimed at knowing if US ETFs were UCIs eligible under Article 41(1)(e) of the 2010 Law.

In order to be eligible under Article 41(1)(e) of the 2010 Law, US ETFs must qualify as UCIs within the meaning of Article 2(2) of this law and must fulfil the conditions laid down in Article 41(1)(e).

The CSSF notes that the offering documents of US ETFs, notably the prospectus and the Status of Additional Information (SAI), generally grant facilities which are not equivalent to the requirements applicable to UCITS and which do not support the conclusion that these US ETFs comply with Articles 2(2) and 41(1)(e) of the 2010 Law.

Indeed, as regards the equivalence of the level of protection for unitholders of US ETFs and that for unitholders of UCITS, US ETFs generally provide for, in their prospectus or their SAI, the possibility to make use in some cases of loans up to 33.33% of their net assets.

Moreover, the prospectus or the SAI of some US ETFs does not prohibit loans or short selling of transferable securities and money market instruments. Similarly, in some cases, US ETFs may invest in commodities.

In addition, the prospectus or the SAI of US ETFs limits the investment in funds to 10% of their net assets, except in case of money market funds for which there is no limit.

However, it should be noted that even if the prospectus or the SAI provides for the use of these facilities, US ETFs actually do not always use these facilities.

Moreover, the CSSF considers that US ETFs must comply with the risk-diversification principle which does not mean that US ETFs must be subject to the same diversification rules as UCITS but that they must be subject to equivalent diversification rules.

In light of the foregoing, the CSSF considers that even if the offering documents of US ETFs allow the use of such facilities, these US ETFs in principle qualify as “other UCIs” provided that they comply in practice with the provisions of Article 2(2) and 41(1)(e) of the 2010 Law.

Given the specificities of each individual US ETF, an eligibility analysis must be carried out on a case-by-case basis and the UCITS is responsible for ensuring that the US ETF, the acquisition of which is contemplated, qualifies as “other UCI” within the meaning of Article 2(2) of the 2010 Law and complies, in practice, with all the criteria of Article 41(1)(e) of this law.

When the prospectus or the SAI of a US ETF provides for more flexibility compared to the requirements applicable to UCITS, the CSSF recommends that the UCITS continuously ensures that the investment rules applied are equivalent to the investment rules applicable to UCITS, for example, via a system of compliance control or a written confirmation of the US ETF or its manager.

4.8. Investment in China A shares for UCITS subject to Part I of the 2010 Law

In 2013, the CSSF was contacted by UCITS subject to Part I of the 2010 Law which wanted to benefit from the Chinese programme Renminbi Qualified Foreign Institutional Investor (RQFII) in order to invest up to 100% in China A shares.

The CSSF considers that the measures regulating the RQFII programme, in particular, the absence of a lock-up period for the repatriation of funds, do not limit the overall liquidity of the portfolio of the UCITS and that the capacity of the UCITS to be able to face redemption requests from investors is not compromised.

In this context, the CSSF decided that UCITS subject to Part I of the 2010 Law, whose manager is authorised as RQFII by the China Securities Regulatory Commission, may, in principle, invest up to 100% of their net assets in China A shares.

The CSSF is of the opinion that investments of a UCITS in China A shares by a RQFII manager qualify as transferable securities within the meaning of Article 41(1)(c) of the 2010 Law and Article 2(1) of the Grand-ducal Regulation of 8 February 2008, as completed by point 17 of the document “CESR’s guidelines concerning eligible assets for investment by UCITS - March 2007 (updated September 2008)” (ref.: CESR/07-044b), included in Circular CSSF 08/380.

4.9. Review of the descriptions of the risk management system of SIFs pursuant to Article 42a of the SIF Law

4.9.1. Context

Article 42a(1) of the SIF Law requires that SIFs put in place appropriate risk management systems in order to identify, measure, manage and monitor the risks arising from positions and their contribution to the general risk profile of the portfolio.

CSSF Regulation N° 12-01 laying down detailed rules for the application of Article 42a of the SIF Law concerning the requirements regarding risk management and conflicts of interest specifies the CSSF’s expectations regarding the risk management system and indicates, in particular in Article 4(6), that SIFs must provide a description of the risk management system as part of their application for authorisation and that any subsequent major change to it must be notified to the CSSF.

As a reminder, following the publication of the CSSF’s press release 12/16 aiming to bring to the fund industry’s attention the amendment of the SIF Law and to specify the information to be notified to the CSSF in this context, the SIFs had to provide the CSSF with a concise description of their risk management system put in place by the 30 June 2012 at the latest.

4.9.2. Review of the descriptions of the SIFs' risk management systems

In the framework of the review of the description of the SIFs' risk management systems, the CSSF noted some deficiencies compared to the requirements into force. These deficiencies concern notably the following topics:

- Insufficient accuracy and clarity as regards the organisation of the risk management function

The CSSF expects that the description of the risk management system includes a clear and accurate description of the organisation of the risk management function of the SIF, which includes notably the allocation of the responsibilities and the relations between the different participants, particularly in case of delegation of the risk management activities. The CSSF noted a regular lack of clarity on this topic.

- Deficiencies in the identification of risks likely to have a significant impact for SIFs

The CSSF noted that some specific risks likely to have a significant impact for SIFs and resulting from investment strategies or particular assets, were not always identified or mentioned, as, for example, for funds investing in real estate, the risks linked to the financing or to the due diligence procedure. The CSSF would like to point out that an exhaustive identification process for risks is of critical importance in the framework of a risk management system.

- Lack of details on the risk management process for identified risks

The CSSF expects to receive information on the manner in which the different risks identified and mentioned in the description of the risk management system are detected, measured, managed and monitored.

4.10. Requirements regarding a stress testing programme in relation to UCITS

In accordance with CSSF Regulation N° 10-04 and Circular CSSF 11/512, management companies subject to Chapter 15 of the 2010 Law (hereafter management company) and investment companies which did not designate a management company within the meaning of Article 27 of this law (hereafter SIAG) must carry out periodically, where appropriate, stress tests and scenario tests in order to take into account the risks resulting from the possible developments of the market conditions likely to have a negative impact on the UCITS that they manage.

In this context, the CSSF would like to point out that the stress tests and scenario analysis (hereafter stress testing programme) must be an integral part of the general governance and risk management framework and must promote the identification and control of risks in addition to the other elements of the risk management framework. The analysis of the results of the stress testing programme must be subject, where appropriate, to concrete actions and influence the decision-taking, and particularly those linked to the strategic investment choice.

Moreover, in accordance with CSSF Regulation N° 10-04, the stress testing programme must, where appropriate, encompass the liquidity risk in order to carry out stress tests which would allow the assessment of the liquidity risk to which the UCITS are exposed in exceptional circumstances so as to comply, at all times, with the obligation laid down in Article 11(2) or Article 28(1)(b) of the 2010 Law.

Finally, pursuant to the ESMA guidelines titled "CESR's Guidelines on Risk Measurement and the Calculation of Global Exposure and Counterparty Risk for UCITS" (ref. CESR/10-788), the CSSF points out that the management companies and SIAGs which manage UCITS whose overall risk of Article 42(3) of the 2010 Law is calculated according to the Value-at-Risk method must draw up and put in place a stress testing programme fulfilling the general quantitative and qualitative requirements laid down in these guidelines. This stress testing programme must, in particular, be adapted to the risk profile and to the portfolio of each UCITS by taking into account unexpected events which might trigger significant losses for the UCITS or even jeopardise its feasibility. To this end and taking into account the investment strategy of the UCITS, it should cover different risk parameters be it for individual positions or for the portfolio and include the different types of scenarios (mono- and multi-factors), or even have an approach which is forward-looking and/or of reverse stress testing.

5. IT SYSTEM FOR THE SUPERVISION OF UCIS

In January 2013, a new department called “Coordination of the UCI departments’ specific IT tools” (UCI SI department) was created within the UCI departments in order to support them in their different missions and tasks of supervision and review. From a historic point of view, this approach is not necessarily new insofar as, in the previous department, people who were competent and interested in IT had been developing for years applications which allowed an automatic and easy workflow and an acceleration of the procedures in place. The new aspect resides in the fact that the people of this department may now fully concentrate on the development of new applications and on the technical assistance for users of these applications. Consequently, the UCI SI department is responsible for the planning, initialisation, management and coordination of IT projects from all the UCI departments.

In the framework of its mission, the UCI SI department works together with the department “Information systems and supervision of support PFS” of the CSSF which provides the necessary support for training the users and makes the systems and applications available.

Besides the general aspects mentioned above, the UCI SI department is responsible, in particular, for projects in relation to the maintenance of the management system for electronic documents, of e-file and of the applications of the UCI departments and their functional development according to the needs expressed by the UCI departments. It ensures the implementation of templates for letters and forms in the systems and their link to the applications concerned. During 2013, several forms were drawn up, allowing the collection of information in electronic form from the intermediaries so as to ensure a faster and more efficient processing.

The UCI SI department also closely cooperates with the transmission channels, as, for example, the UCITS notifications and the developments relating to the new information transmission obligations required by the AIFMD. It draws up solutions in relation to the electronic signature of the UCI departments and manages the communication with the foreign authorities as regards the verification of the electronic signature. The department contributes to the development and the implementation of the prudential reporting and represents, in this matter, the UCI departments in the relevant groups of ESMA and other competent institutions. Moreover, the department supports the developments in the realisation of the electronic archiving for existing paper files and an electronic mail management system.

Finally, the UCI SI department is in charge of the organisation of training and teaching programmes in order to initiate the agents of the UCI departments to the IT systems and applications of the UCI departments and of the CSSF.

CHAPTER VIII

SUPERVISION OF SECURITISATION UNDERTAKINGS



1. Developments of authorised securitisation undertakings
2. Prudential supervisory practice

1. DEVELOPMENTS OF AUTHORISED SECURITISATION UNDERTAKINGS

In 2013, the CSSF received three applications for registration on the official list of authorised securitisation undertakings subject to the law of 22 March 2004 on securitisation.

One securitisation undertaking was granted authorisation by the CSSF in 2013, namely the multiple-compartment securitisation undertaking

- Argentum Capital S.A.

The securitisation undertakings H.E.A.T. Mezzanine S.A. and Market Vectors SA were deregistered from the official list of authorised securitisation undertakings in 2013.

The liquidation, ordered on 11 May 2012 by the *Tribunal d'Arrondissement siégeant en matière commerciale* (District Court sitting in commercial matters), of the securitisation undertaking Lifemark S.A., which was withdrawn from the official list of authorised securitisation undertakings on 10 February 2012 following the conclusion of the *administrateur provisoire* (provisional administrator) that the restructuring of its activities was not possible, was closed on 20 December 2013.

As at 31 December 2013, 31 securitisation undertakings were registered on the official list of securitisation undertakings, against 32 entities at the end of 2012. The balance sheet total of authorised securitisation undertakings exceeded EUR 19.6 billion at the end of 2013, which is an increase of EUR 3.7 billion compared to 2012.

The submitted application files reveal that securitisation transactions mainly consist in repackaging transactions in the form of structured products issues linked to various financial assets, notably equity indices, baskets of shares or units of undertakings for collective investment, as well as in securitisation of debt, loans and other comparable assets. Repackaging transactions are predominantly synthetic securitisation transactions as far as the risk transfer technique is concerned.

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. As at 31 December 2013, 10 out of the 31 authorised securitisation undertakings issued securities admitted to trading on a regulated market.

To date, no application file for a securitisation fund has been submitted to the CSSF. Neither has the CSSF received any application file for 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.

The CSSF expects activities to continue their slow but steady pace in 2014.

• New facts since the decision to refuse to register ARM Asset Backed Securities S.A. on the official list

On 29 August 2011, the CSSF decided to refuse to register the securitisation undertaking ARM Asset Backed Securities S.A. (ARM) on the official list of authorised securitisation undertakings. On 29 November 2011, ARM brought a *recours administratif* (petition) before the *Tribunal Administratif* (administrative tribunal) against the CSSF's decision. On 6 December 2012, the *Tribunal Administratif* declared the petition lodged by ARM before the *Tribunal Administratif de première instance* (administrative first instance court) to be unfounded and that the expenses of this judgment were to be borne by ARM. On 16 January 2013, ARM lodged an appeal with the *Cour Administrative* (administrative court of appeal) against the judgment of the *Tribunal Administratif*.

On 21 August 2013, the *Cour Administrative* confirmed the first instance judgment of the *Tribunal Administratif*, so that the CSSF's decision to refuse a licence of 29 August 2011 became final. On 4 September 2013, the CSSF asked the Public Prosecutor to request the *Tribunal d'Arrondissement de Luxembourg siégeant en matière commerciale* (District Court sitting in commercial matters) to order the dissolution and liquidation of ARM. On 24 September 2013, the CSSF released an FAQ on this matter.

On 4 October 2013, ARM lodged a petition at the High Court of Justice of England and Wales to appoint Messrs. Mark Shaw and Malcolm Cohen of BDO LLP as joint provisional liquidators. On 9 October 2013, they were appointed as joint provisional liquidators by the court. The website of the joint provisional liquidators is www.bdo.co.uk/arm-abs-sa.

The judgment of the *Cour Administrative* of 21 August 2013 does not have an impact on the appeal ARM has lodged with the *Cour d'appel siégeant en matière commerciale* (Court of appeal sitting in commercial matters) against the judgment of the *Tribunal d'Arrondissement* of 10 November 2011, which confirmed that the protective measures listed in Article 28 of the law of 22 March 2004 on securitisation are applicable to the *société anonyme* ARM and which accepted the request of the CSSF to be replaced as *commissaire de surveillance* (supervisory commissioner). The regime of suspension of payments by ARM and prohibition for ARM, under penalty of voidance, to take any measures other than protective measures, unless otherwise authorised by Ernst & Young acting as supervisory commissioner, remain in place.

Please refer to the CSSF's website, section "Publications", sub-section "Press releases" for any news relating to ARM.

2. PRUDENTIAL SUPERVISORY PRACTICE

2.1. Regulatory aspects

In 2013, no changes have been made to the legal framework governing securitisation undertakings. However, the Frequently Asked Questions on securitisation were updated in October 2013. The major change is a new question 19 which deals with the impact of the law of 12 July 2013 on alternative investment fund managers (AIFM Law) on the securitisation undertakings within the meaning of the law of 22 March 2004 on securitisation.

In this context, the CSSF adopted, subject to any future development or clarification at European level, the following positions:

- A securitisation undertaking that meets the definition of "securitisation special purpose entity" under the AIFM Law, can not qualify as an alternative investment fund (AIF) within the meaning of the AIFM Law, as Article 2(2)(g) of that law provides that "securitisation special purpose entities" are exempt from its scope.

"Securitisation special purpose entities" are defined as entities whose sole purpose is to carry on a securitisation or securitisations within the meaning of Article 1(2) of Regulation (EC) No 24/2009 of the European Central Bank of 19 December 2008 concerning statistics on the assets and liabilities of financial vehicle corporations engaged in securitisation transactions (ECB/2008/30) and other activities which are appropriate to accomplish that purpose (ECB Regulation).

According to the ECB Regulation, "securitisation" is "a transaction or scheme whereby an asset or pool of assets is transferred to an entity that is separate from the originator and is created for or serves the purpose of the securitisation and/or the credit risk of an asset or pool of assets, or part thereof, is transferred to the investors in the securities, securitisation fund units, other debt instruments and/or financial derivatives issued by an entity that is separate from the originator and is created for or serves the purpose of the securitisation; and:

a) in case of transfer of credit risk, the transfer is achieved by:

- the economic transfer of the assets being securitised to an entity separate from the originator created for or serving the purpose of the securitisation. This is accomplished by the transfer of ownership of the securitised assets from the originator or through sub-participation, or
- the use of credit derivatives, guarantees or any similar mechanism;

and

- b) where such securities, securitisation fund units, debt instruments and/or financial derivatives are issued, they do not represent the originator's payment obligations".

According to the clarifications given by the ECB in its “Guidance note on the definitions of ‘financial vehicle corporation’ and ‘securitisation’ under Regulation ECB/2008/30”, point 4.1 on page 3, a securitisation vehicle issuing collateralised loan obligations would indeed fall under the definition of the ECB Regulation, so that these vehicles are not AIFs.

However, according to the same Guidance note (point 4.1 and 4.3 on pages 3 and 4), securitisation undertakings whose core business is to securitise loans they grant themselves (securitisation undertakings acting as first lender) do not meet the definition of the ECB Regulation and can thus not benefit from the exemption. The same applies to securitisation undertakings issuing structured products that primarily offer synthetic exposure to non-credit related assets and where the credit risk transfer is incidental.

- Irrespective of whether or not they meet the definition of “securitisation special purpose entities” under the AIFM Law, securitisation undertakings issuing debt instruments only do not qualify as AIFs, as it appears that the European legislator did not intend to qualify undertakings issuing such instruments as AIFs. In this respect, reference is made to the Questions/Answers of the European Commission of 25 March 2013 (Questions on Single Market Legislation; General question on Directive 2011/61/EU; ID 1169, Scope and exemptions), in which the European Commission considers that any type of security not representing an ownership interest in the securitisation undertaking should be excluded from the scope of Directive 2011/61/EU.
- Irrespective of whether or not they fall under the definition of “securitisation special purpose entities” under the AIFM Law, securitisation undertakings that are not managed according to a “defined investment policy” within the meaning of Article 4(1)(a) of the AIFM Law are not AIFs. In order to determine whether they are managed according to a “defined investment policy” within the meaning of the AIFM Law, reference is made to the “Guidelines on key concepts of the AIFMD” published by ESMA on 13 August 2013.

Subject to the criteria laid down in the ESMA Guidelines, securitisation undertakings issuing structured products offering synthetic exposure to assets (such as shares, indices, commodities), based on a pre-defined formula, and that acquire underlying assets and/or enter into swap agreements for the sole purpose of hedging their payment obligations under the issued structured products, shall be considered as not being managed according to a “defined investment policy”.

- It is recalled that each securitisation undertaking shall carry out a self-assessment to determine whether it qualifies as AIF. Reference is made for this specific issue to the Frequently Asked Questions published on the CSSF’s website.

CHAPTER IX

SUPERVISION OF PENSION FUNDS



1. Developments of pension funds in 2013
2. Developments of liability managers in 2013

1. DEVELOPMENTS OF PENSION FUNDS IN 2013

1.1. Major events and trends observed in 2013

As at 31 December 2013, 14 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, including 11 assep and three sepcav.

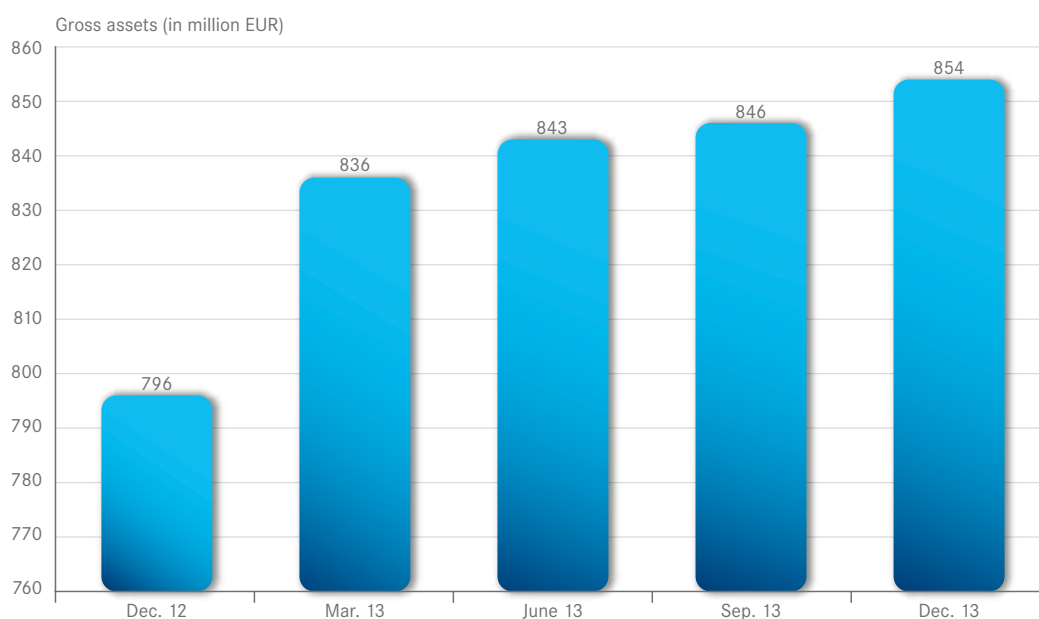
As at 31 December 2013, one pension fund managed cross-border pension schemes. It provides services to sponsoring undertakings established in Ireland, the Netherlands and Greece.

In 2013, the development of the activities and volume of the pension funds registered on the official list of pension funds was slow, but steady. Moreover, the CSSF observed an increased interest in the establishment of pan-European pension funds, apparently motivated by the will to cut costs that were deemed excessive owing to the coexistence of many national pension schemes managed in disparate ways. In this context, two new applications for authorisation of pan-European pension funds were submitted to the CSSF in 2013.

1.2. Developments of pension fund assets

At the end of 2013, gross assets of pension funds totalled EUR 854 million against EUR 796 million as at 31 December 2012, representing a 7.3% growth.

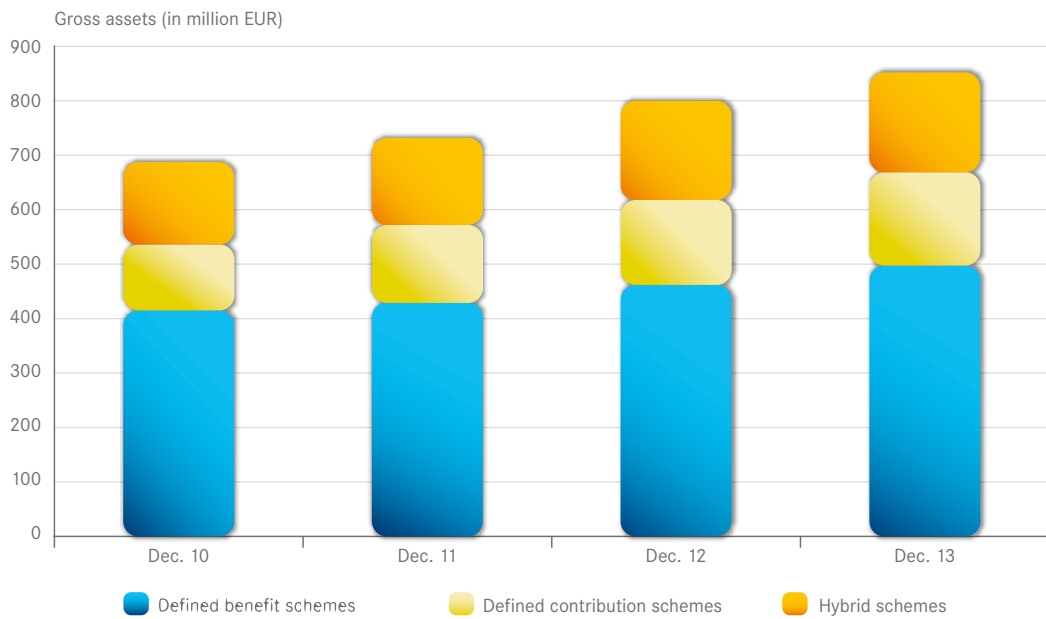
Developments of pension fund assets



1.3. Developments of assets according to the type of pension scheme

The following table highlights that gross assets of defined benefit schemes amounted to EUR 499 million at the end of 2013 and represented 58.5% of overall gross assets of pension funds. Assets of defined contribution schemes amounted to EUR 173 million as at 31 December 2013.

Developments of assets according to the type of pension scheme

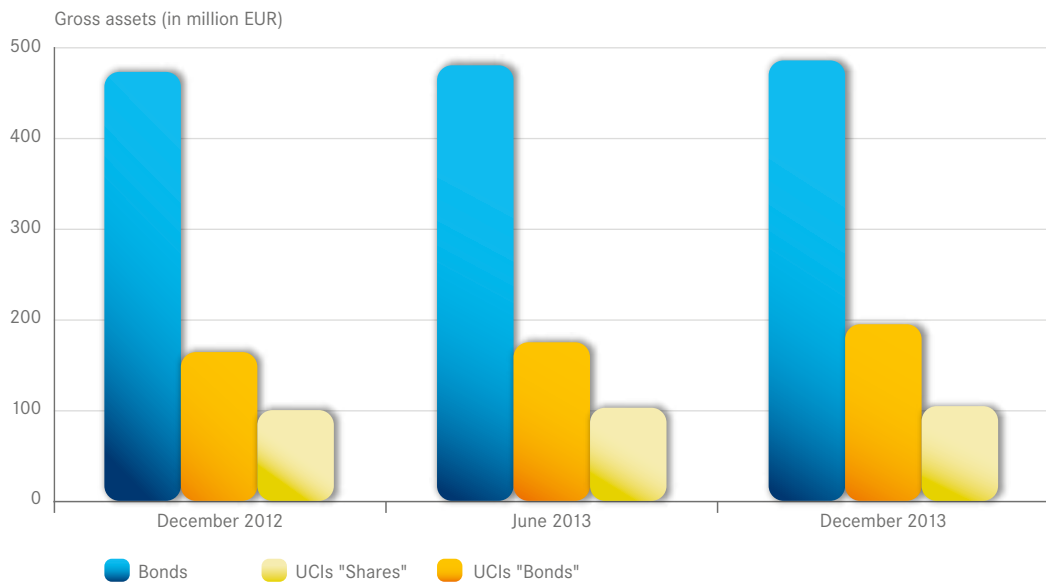


1.4. Allocation of pension fund assets

In 2013, pension funds invested primarily in bonds, representing a total of EUR 486 million, i.e. 57 % of total gross assets of pension funds. The total amount of investments of pension funds in investment funds amounted to EUR 314 million as at 31 December 2013, of which EUR 195.5 million in share funds and EUR 105.7 million in bond funds.



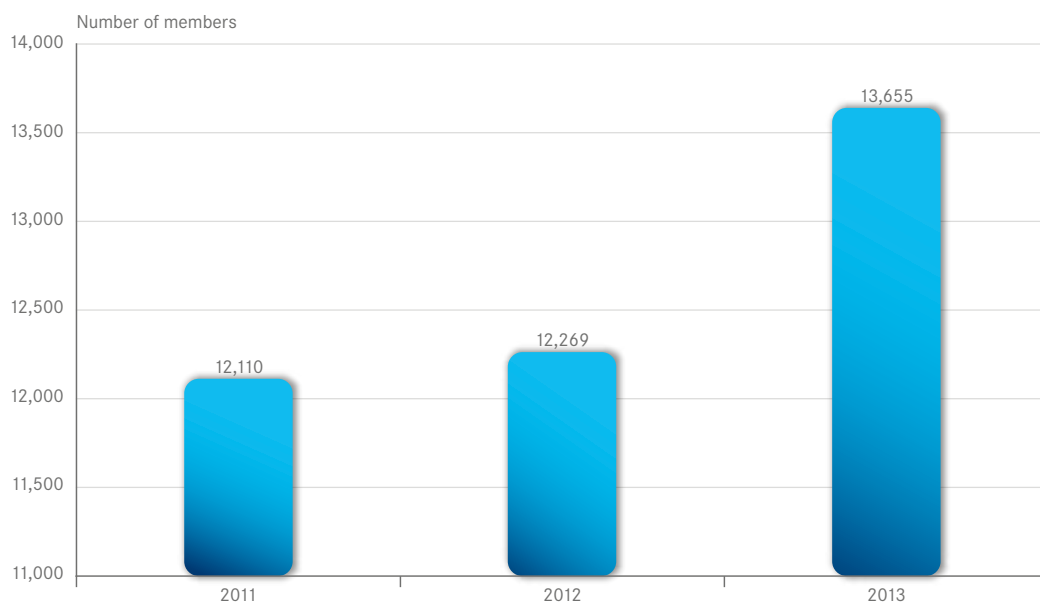
Allocation of pension fund assets



1.5. Development in the number of pension fund members

At the end of 2013, pension funds had 13,655 members against 12,269 members as at 31 December 2012, which is an 11.3% growth over a year. This rise can be explained, inter alia, by the creation of a new pension scheme within an existing pension fund.

Developments in the number of pension fund members



2. DEVELOPMENTS OF LIABILITY MANAGERS IN 2013

In 2013, no new liability manager has been registered on the official list of professionals authorised to act as liability managers for pension funds subject to the law of 13 July 2005.

The number of liability managers for pension funds authorised by the CSSF amounted to 15 as at 31 December 2013.

CHAPTER X

SUPERVISION OF SECURITIES MARKETS



1. Approval of prospectuses for securities relating to offers to the public or admissions to trading on a regulated market
2. Takeover bids
3. Mandatory squeeze-out and sell-out of securities
4. Supervision of issuers of securities of which the CSSF is the competent authority
5. Enforcement of financial information
6. Supervision of markets and market operators
7. Investigations and cooperation

1. APPROVAL OF PROSPECTUSES FOR SECURITIES RELATING TO OFFERS TO THE PUBLIC OR ADMISSIONS TO TRADING ON A REGULATED MARKET

1.1. Application of the Prospectus Law

Unlike in 2012, there were no great changes in the regulation applicable to prospectuses for securities in 2013. Indeed, only the Commission Delegated Regulation (EU) No 759/2013 of 30 April 2013 amending Regulation (EC) No 809/2004 as regards the disclosure requirements for convertible and exchangeable debt securities was published.

Following the entry into force of the law of 3 July 2012 transposing Directive 2010/73/EU and amending the law of 10 July 2005 on prospectuses for securities (Prospectus Law), some issuers have benefited from a grandfathering clause in relation to the adaptation of the update of their base prospectus to the new regulation until the end of June 2013. A lot of these issuers did not wait until the end date of June 2013 to submit their first base prospectus under the new regulation but had already submitted their draft base prospectus in March 2013 so as to avoid being under pressure if an unexpected event occurs due to the changes to be made pursuant to the new regulation. However, issuers which are less active in issues decided to delay the introduction of their documents until the summer period. Hence, the requests for approval of base prospectuses were, unlike in 2012, more spread in time which allowed the CSSF to manage the related additional workload well.

It was also noted that while many issuers, which, at first, chose to group all their products likely to be issued by them in one single base prospectus, finally decided in 2013 to divide it into several documents so as to better take into account the new regulatory provisions. This shift happened because the drawing-up of base prospectuses that encompass all possible products of an issuer has become much more complicated under the new regulation. In practice, these divisions provide investors with a better readability and understanding of the base prospectuses. Moreover, it should be pointed out that the number of base prospectuses relating to the issues of asset-backed securities decreased by half. The requirements as regards the presentation of the documents being much more stringent since the implementation of the new regulation, many issuers gave up using this type of prospectus for securitisation issues. Still, with regard to base prospectuses, the CSSF, like several other competent authorities, accepted the tripartite base prospectuses while waiting for a clear decision by ESMA on the compliance of this structure with the regulation on prospectuses. However, on 18 December 2013, ESMA published an opinion which specifies that the drawing-up of a base prospectus which consists of separate documents is not compliant with the regulation on prospectuses. Consequently, the CSSF informed the issuers concerned that the tripartite base prospectuses will no longer be accepted for approval and that those which were already approved could not be notified in other Member States any more.

The efforts in relation to the recruitment and training of agents in charge of prospectus approvals continued in 2013, thus contributing to controlling the workload which is getting greater. Therefore, and due to joint commitments of all the readers, the deadlines for processing the prospectuses and base prospectuses were reduced again so that they are now at a satisfying level for the market players and correspond to the situation as it was before the entry into force of the new regulation in 2012.

Throughout 2013, the department "Supervision of securities markets" together with the IT department of the CSSF actively worked on the "Register" project launched by ESMA pursuant to the requirements defined by Directive 2010/78/EU. Since 24 February 2014, ESMA is publishing the list of prospectuses approved by the competent authorities of the Member States as well as possible related supplements or notifications on its website for a minimum period of 12 months. In order to fulfil this obligation, ESMA developed an IT tool via which the competent authorities of the Member States must notify the requested information. In this context, the CSSF has identified and transmitted all the data required by ESMA which represented a significant volume of information due to the increased approval activity in 2013.

The same trend as for the deposits of prospectuses was recorded for requests for an opinion which increased considerably (253 in 2013 against 166 in 2012, i.e. an increase of 52.41%). A great portion of these requests concerned the circumstances under which a supplement is required according to Article 13 of the Prospectus Law and the financial information regarding issuers or guarantors to be submitted. Many questions relating to the new regulation were also asked, particularly on the manner in which to structure base prospectuses.

Some positions adopted by the CSSF within the context of these requests for an opinion are detailed under item 1.3. of this chapter.

In 2013, the CSSF received six requests for the omission of information pursuant to Article 10 of the Prospectus Law. Detailed justifications in relation to these requests allowed the CSSF to grant them.

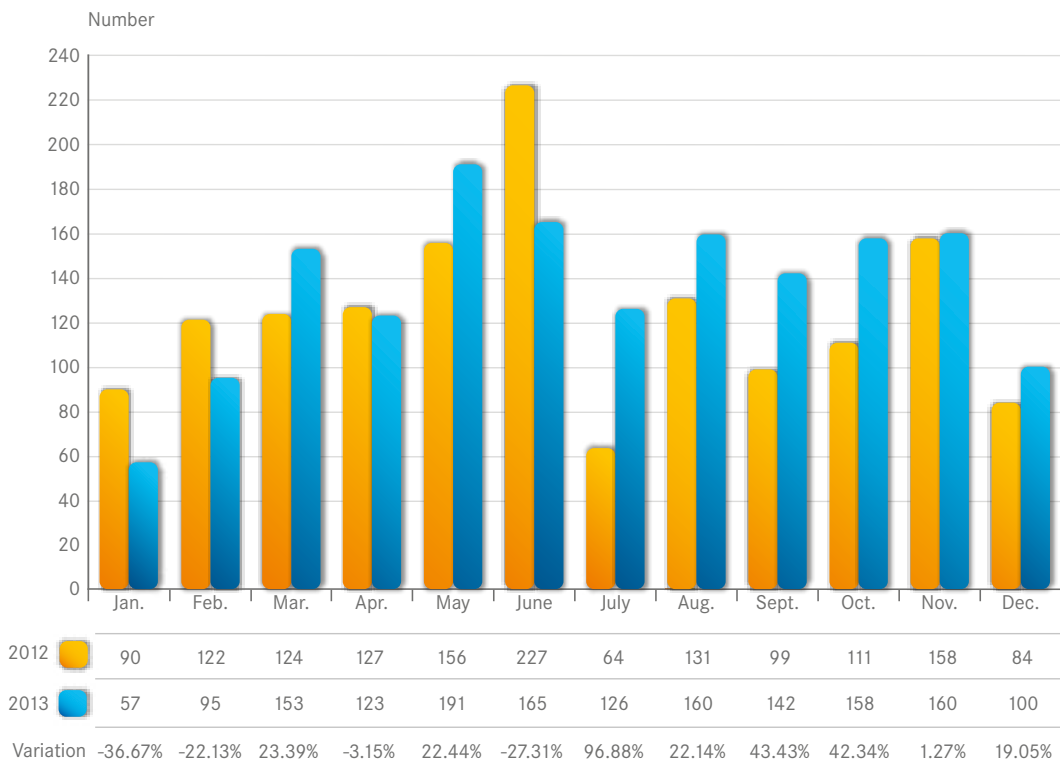
Moreover, in accordance with Article 23(4) of the Prospectus Regulation, the CSSF approved three prospectuses, each including an omission of information due to non-pertinence.

1.2. Approvals and notifications in 2013

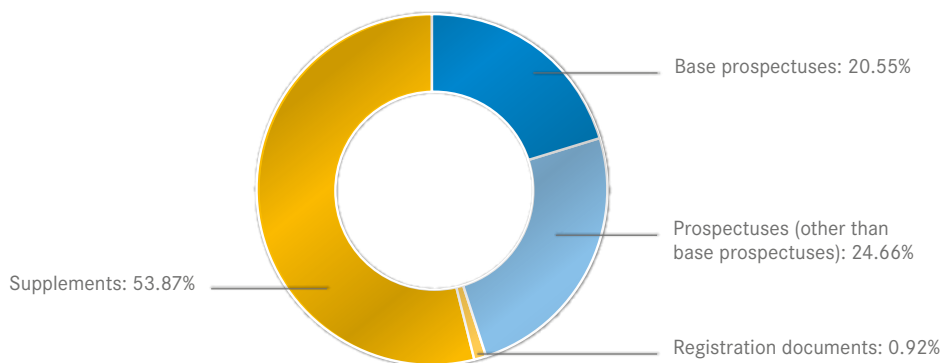
1.2.1. Documents approved by the CSSF in 2013

The number of documents approved by the CSSF slightly increased compared to 2012, amounting to a total of 1,630 approved documents in 2013 (of which 402 prospectuses, 335 base prospectuses, 15 registration documents and 878 supplements) against 1,493 the previous year (+9.18%). This increase mainly results from the number of approved prospectuses (+46.18%).

Development in the number of documents approved by the CSSF



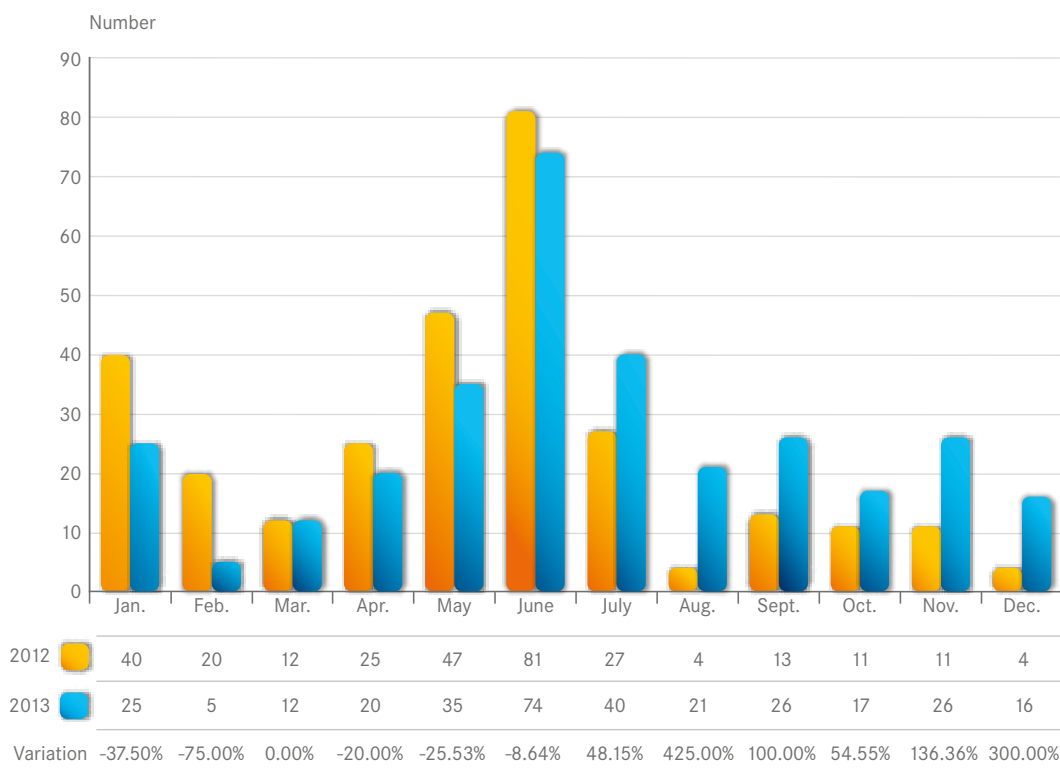
Distribution of documents approved in 2013



1.2.2. Documents drawn up under the European passport regime in 2013

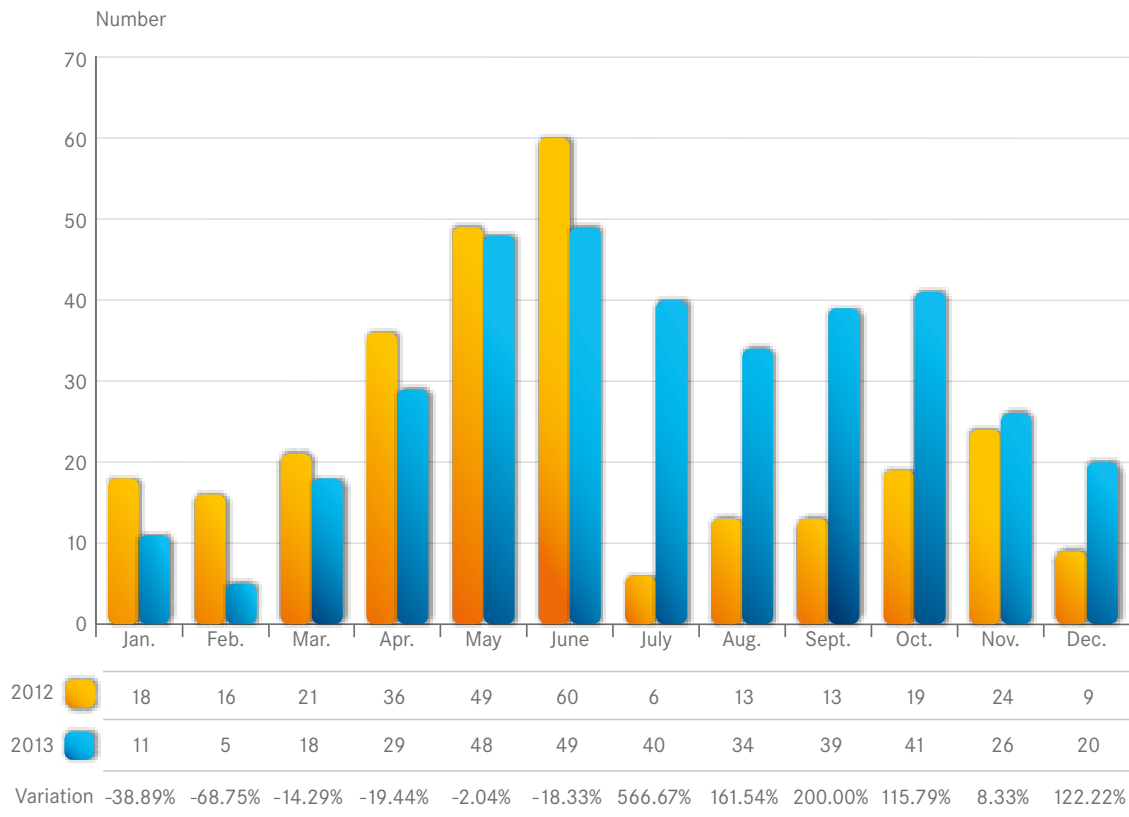
In 2013, the CSSF received 1,914 notifications (relating to 317 prospectuses and base prospectuses and 1,597 supplements) from the competent authorities of several EEA Member States against 1,913 notifications (relating to 295 prospectuses and base prospectuses and 1,618 supplements) in 2012.

Development in the number of notifications (prospectuses and base prospectuses) received by the CSSF



In 2013, the CSSF sent notifications for 883 CSSF-approved documents (360 prospectuses and base prospectuses and 523 supplements) to the competent authorities of the EEA Member States, against 799 documents (284 prospectuses and base prospectuses and 515 supplements) in 2012, representing a 10.51% increase. The number of notifications relating to prospectuses and base prospectuses alone significantly rose by 26.76%.

Development in the number of notifications (prospectuses and base prospectuses) sent by the CSSF



1.2.3. Approvals

By analysing the 2013 figures relating to the approved documents to be published in case of offers to the public or admissions to trading of securities on a regulated market, it appears that the CSSF managed to retain a great number of issuers which use base prospectuses. Thus, the number of base prospectuses and supplements approved by the CSSF remained stable. The approvals of prospectuses or standardised prospectuses recorded, however, a significant increase (+49.67%) due mainly to eight very active issuers which represented 44.78% of these approvals. Furthermore, German issuers, boosted by the strong growth of bond issues of SMEs, represented 18.4% of these approvals.

In this context, it should be noted that the prospectuses relating to the issue of asset-backed securities recorded a significant increase, unlike the situation described under item 1.1. for base prospectuses relating to this category of issue. Indeed, some issuers of this type of securities preferred to use the stand alone documentation which is better adapted to securitisation than the base prospectuses.

In particular, the CSSF approved 299 files relating to Luxembourg issuers, among which 123 prospectuses, 43 base prospectuses, 4 registration documents and 129 supplements. It should be noted that 11 of these files were submitted for a public offer or admission to trading of shares.

Among the most advertised files are, on the one hand, the approval in April 2013 of the prospectus relating to the offer to the public of the shares of the RTL group in Luxembourg and Germany as well as their admission on the regulated market of Frankfurt (in addition to the admissions on the regulated markets of Brussels and Luxembourg) and, on the other hand, the approval, in January 2014, of the prospectus relating to the offer to the public of shares of the cable operator Altice S.A. in the Netherlands and their admission on the regulated market of Euronext Amsterdam.

1.3. Questions regarding base prospectuses raised in 2013

1.3.1. In which situations does a supplement to a base prospectus introduce a new type of product?

It results from Article 13(1) of the Prospectus Law that it is impossible to draw up a supplement to a base prospectus in order to include therein a new type of product. In this context, the CSSF bases itself, among others, on the following criteria to determine if the changes made via a supplement are to be considered as an introduction of a new type of product:

- the necessity to use a new annex to Regulation (EC) No 809/2004 in order to verify the changes made in the supplement;
- the addition of a great number of conditions leading to a fundamental change of the characteristics of the securities already described in the base prospectus; and
- the quantity and volume of the changes made to the securities and documentation.

The last two points must be assessed by the CSSF on a case-by-case basis.

1.3.2. Are there any specific requirements when a supplement to a base prospectus introduces changes relating to the conditions of the securities?

When an issuer decides to include changes amending the conditions of the securities in a supplement to a base prospectus, it must specify in this supplement that the changes in question can only affect the securities to be issued after the approval of this supplement via the Final Terms.

2. TAKEOVER BIDS

2.1. Offer documents approved by the CSSF

In 2013, the CSSF did not have to approve or recognise any offer document in relation to takeover bids under the law of 19 May 2006 implementing Directive 2004/25/EC of 21 April 2004 on takeover bids (Law on Takeover Bids).

2.2. Files for which the CSSF was competent as authority of the Member State in which the target company has its registered office

In 2013, the CSSF was competent as authority of the Member State in which the target company has its registered office in the context of two takeover bids, namely (1) the takeover bid by Hercules Discovery Ltd. on the shares of the Luxembourg company Discovery Offshore S.A. admitted to trading on the Oslo stock exchange for which the offer document was published on 11 July 2013 and (2) the takeover bid by Merck 15. Allgemeine Beteiligungs-GmbH on the shares of the Luxembourg company AZ Electronic Materials S.A. admitted to trading on the London stock exchange for which the offer document was published on 20 December 2013.

In the first file, the CSSF cooperated with the Oslo stock exchange and intervened, particularly, in the determination of the fair price for the exercise of the right of squeeze-out by Hercules Discovery Ltd. pursuant to the Law on Takeover Bids. In the second file, the CSSF cooperated with the UK Takeover Panel and intervened as the competent authority on a certain number of aspects covered by Article 4(2)(e) of the Law on Takeover Bids.

2.3. Offer file not falling under the scope of the Law on Takeover Bids

On 13 September 2013, the company BIP Investment Partners S.A. announced its intention to make a limited and conditional buyback offer concerning a certain amount of shares and to launch a process aiming to withdraw all its shares from trading on the regulated market and from the official listing on the Luxembourg stock exchange. The buyback offer started on 21 October 2013 and closed on 15 November 2013, whereas the last day of trading of the BIP Investment Partners S.A. shares on the Luxembourg stock exchange was on 28 February 2014.

The buyback offer was carried out outside the scope of the Law on Takeover Bids. Nevertheless, the CSSF had to review the documentation and monitor the buyback offer process and the above-mentioned withdrawal in its capacity as competent authority under Luxembourg law, particularly, pursuant to the law of 23 December 1998 establishing a financial sector supervisory commission (Commission de surveillance du secteur financier), the law of 13 July 2007 on markets in financial instruments, the law of 11 January 2008 on transparency requirements for issuers of securities and the law of 9 May 2006 on market abuse.

2.4. Questions regarding the Law on Takeover Bids raised in 2013

In the framework of a file on takeover bids, the CSSF had the opportunity to reiterate that the contracts, generally known as break fees agreements, signed in the context of a takeover bid falling under the scope of the Law on Takeover Bids between a target company and the offeror, are likely to constitute a breach in the general principles of the Law on Takeover Bids. The CSSF considers, however, that such contracts must be analysed on a case-by-case basis according to their particular terms and the situation of the different parties concerned by the takeover bid. In this particular case, the CSSF considered that the agreement as described in the documentation did not contravene the provisions of the Law on Takeover Bids having regard in particular to the compliance with certain conditions, among which:

- the managing body of the target company considered the conclusion of such a contract as being in the interest of the company and its shareholders and in line with the principle of equal treatment;
- the compensation was to be paid only in case of success of a competing takeover bid which would have superseded that of the offeror (the shareholders remaining free to reject the offer made by the offeror);
- the compensation did not exceed 1% of the share capital of the target company subject to the offer and was inferior to the costs actually incurred by the offeror in the framework of its takeover bid; and
- the absence of deterrent effect which such a compensation would have had towards a possible initiator of a counter-offer.

The CSSF also dealt with several requests for advice relating to transactions likely to fall under the scope of the Law on Takeover Bids. These advice requests concerned, among others:

- the kinds of motivation likely to justify a request for derogation from the obligation to launch a mandatory takeover bid in accordance with the provisions of Article 4(5) of the Law on Takeover Bids;
- the securities concerned by a mandatory takeover;
- the applicable rules related to the mandatory squeeze-out according to Article 15 of the Law on Takeover Bids (notably according to the application of the presumption provided for in Article 15(5) of the Law on Takeover Bids);
- the concepts of acting in concert, acquisition of control or change of control.

The CSSF took the nature and specific structure of the transactions concerned into account for its answers.

Moreover, the CSSF contributed to the works of ESMA seeking, in particular, to clarify the concept of persons acting in concert as defined in Directive 2004/25/EC of 21 April 2004 on takeover bids (cf. “ESMA public statement; Information on shareholder cooperation and acting in concert under the Takeover Bids Directive”, ESMA/2013/1642 dated 12 November 2013).

3. MANDATORY SQUEEZE-OUT AND SELL-OUT OF SECURITIES

3.1. Results related to the application of the law of 21 July 2012 on mandatory squeeze-out and sell-out of securities of companies currently admitted or previously admitted to trading on a regulated market or having been offered to the public (Squeeze-Out/Sell-Out Law)

Pursuant to Article 6 of the Squeeze-Out/Sell-Out Law, the CSSF is the competent authority to ensure that the provisions of this law are applied. Among the competences conferred to the CSSF under this legislation is the reception of notifications to be made by any majority shareholder in accordance with the provisions of Article 3(1), completed by Article 10(1) as regards the transitional regime of the Squeeze-Out/Sell-Out Law. These notifications are part of the pre-requisites of information which must be complied with prior to any exercise of the mandatory squeeze-out right or sell-out right of securities and aim to ensure the possibility for the different parties concerned by this legislation to exercise their respective rights. As at 1 March 2014, the CSSF received 27 notifications from nine different majority shareholders made pursuant to Articles 3(1) and 10(1) of the Squeeze-Out/Sell-Out Law.

The CSSF must also be informed of the exercise of any mandatory squeeze-out right or sell-out right pursuant to the provisions of Article 4(3) of the Squeeze-Out/Sell-Out Law as regards any exercise of the mandatory squeeze-out right by a majority shareholder and Article 5(2) as regards the exercise of the mandatory sell-out right by a holder of securities. During 2013, two procedures of mandatory squeeze-out were started and finalised by the respective majority shareholders of the companies Plantations des Terres Rouges S.A. and Old Town. As at 1 March 2014, a mandatory squeeze-out procedure is still in process. This mandatory squeeze-out procedure concerns the shares of Utopia S.A. for which the above-mentioned mandatory squeeze-out procedure was started by the majority shareholder of the company on 10 December 2013. Since the entry into force of the Squeeze-Out/Sell-Out Law, no mandatory sell-out procedure within the meaning of Article 5 of this law was formally launched.

3.2. Some interpretation questions raised since the entry into force of the Squeeze-Out/Sell-Out Law

In the framework of one specific mandatory squeeze-out procedure, the CSSF specified that the consideration must be in cash while admitting that it is possible for the majority shareholder to carry out concomitantly but outside the scope of the Squeeze-Out/Sell-Out Law an offer to the public for the exchange of securities of the company concerned provided that such offer does not affect the rights of the securities holders concerned by the mandatory squeeze-out procedure within the meaning of the Squeeze-Out/Sell-Out Law.

In the framework of the mandatory squeeze-out procedures and notifications of the majority shareholders or in case of information requests regarding the application of the Squeeze-Out/Sell-Out Law, the CSSF also had to decide on the application of a certain number of provisions of the Squeeze-Out/Sell-Out Law, including, in particular, those concerning the application conditions under which the notification obligations set out in Articles 3 and 10 of this law apply, the publication and communication obligations of the majority shareholders and the company concerned, the treatment of shares without voting rights or the treatment of shares held in treasury by the company concerned in the framework of a mandatory squeeze-out procedure and the conditions relating to the experience and independence of the expert responsible for the drawing-up of the valuation report. When dealing with the different questions, the CSSF took into account the nature and the specific structure of each transaction as well as the situation of the parties concerned.

3.3. Disclosure of information relating to the Squeeze-Out/Sell-Out Law

The Squeeze-Out/Sell-Out Law, Circular CSSF 12/545 as well as other information in relation to this regulation are available on the CSSF website under the section "Squeeze-out/Sell-out". The list of companies for which the information was validly notified to the CSSF pursuant to Articles 3(1) and 10(1) of the Squeeze-Out/Sell-Out Law is also available under this section. Similarly to the practices set up in other areas, any person concerned by the Squeeze-Out/Sell-Out Law may send requests and questions related to this law to the CSSF via email at: retrait.rachat@cssf.lu.

4. SUPERVISION OF ISSUERS OF SECURITIES OF WHICH THE CSSF IS THE COMPETENT AUTHORITY

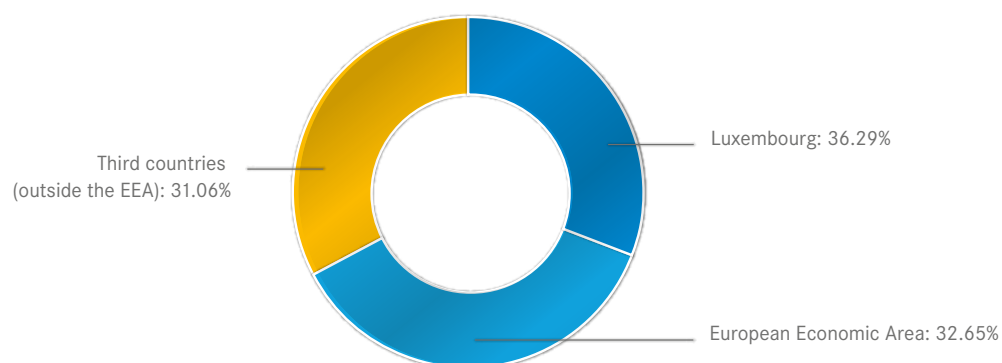
4.1. Issuers subject to supervision

Pursuant to the law of 11 January 2008 on transparency requirements for issuers of securities (Transparency Law), the CSSF is in charge of the supervision of issuers falling under the scope of this law. As at 6 March 2014, 631 issuers were subject to the supervision of the CSSF as Luxembourg was their home Member State within the meaning of this law. In 2013, Luxembourg was confirmed as the home Member State for 51 issuers, whereas 83 issuers no longer fell within the scope of the Transparency Law, mainly because the securities issued by these entities matured or were redeemed early. The list of issuers supervised by the CSSF is published on the CSSF's website (section "Supervised Entities").

Out of the 631 issuers supervised by the CSSF, 229 are Luxembourg issuers, of which 47 issuers of shares and one issuer whose shares are represented by Fiduciary Depositary Receipts admitted to trading on a regulated market. Among these Luxembourg issuers, 15 are banks, 10 are securitisation undertakings authorised pursuant to Article 19 of the law of 22 March 2004 on securitisation, 43 are unauthorised securitisation undertakings and 6 are UCIs.

206 issuers have their registered office in another EEA Member State and 196 issuers are established in a third country (outside the EEA).

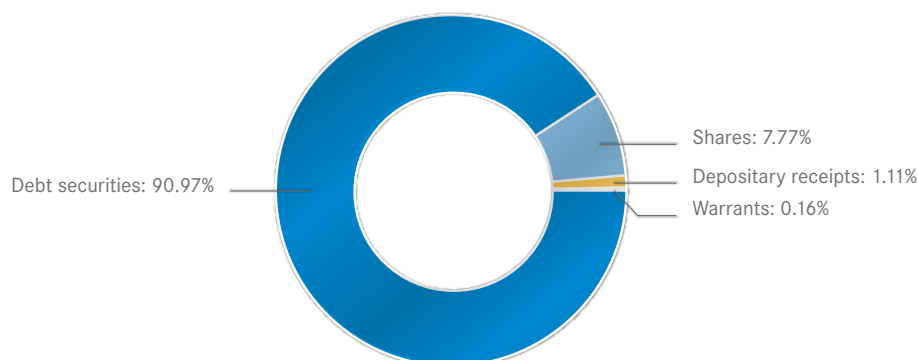
Breakdown of issuers according to country



In 2013, two issuers of shares were added to the list of issuers subject to the supervision of the CSSF.

During the same period, six Luxembourg issuers of shares were excluded from the scope of the Transparency Law, either because the issuer decided to delist or because the issuing company was liquidated or because the company transferred its securities from the regulated market to the Euro-MTF market.

Breakdown of issuers according to type of securities admitted to trading



4.2. Reviews in relation to the Transparency Legislation

The review of the periodic information to be drawn up by issuers of securities of which Luxembourg is the home Member State pursuant to the Transparency Law continued during the 2013 review campaign. The CSSF sent 51 reminders, issued 20 injunctions and imposed 11 administrative fines pursuant to Article 25 of the Transparency Law related to annual and half-yearly financial reports. These figures have declined compared to 2012, whereas the number of issuers subject to the supervision of the CSSF remained approximately the same continuing the trend observed the past few years. This shows that the issuers are more and more aware of their obligations in relation to the Transparency Legislation and have improved their compliance in this regard.

As announced in the press release of 5 February 2013 and in the 2012 Annual Report, the CSSF continued, during its 2013 review campaign, its reviews of the content of the management reports, in particular the information to be published pursuant to Articles 11(1) and (2) of the Law on Takeover Bids by the companies mentioned in Article 1(1) of this law. The reviews carried out were successful since the annual reports of the supervised issuers relating to the financial year 2012 are now overall compliant with the requirements of Articles 11(1) and (2) of the Law on Takeover Bids.

In addition to the existing publication of the names of Luxembourg issuers which failed to publish their annual financial report, the CSSF also decided to publish the names of the Luxembourg issuers subject to the Transparency Law and which failed to publish their half-yearly financial report as required by Article 4 of the Transparency Law, for the periods ending on 30 June 2013 or after that date (press release of 2 August 2013).

A press release as well as new FAQs were published on 25 February 2014 in order to remind the issuers benefiting from an exemption set out in Articles 7 or 30(6) of the Transparency Law the position of the CSSF as regards the regulated information that they must publish in accordance with the Transparency Law (inside information, financial reports and documents made available in the framework of the preparation of the general meeting).

The notifications relating to the acquisition or disposal of major holdings and, more generally, the requirements of the Transparency Law relating to information on major holdings, were subject to more thorough reviews and to exchanges with a certain number of issuers and holders of shares. There are still too many infringements in this matter and several notification omissions and/or late notifications were sanctioned or were subject to a warning. These reviews are going to be further intensified in 2014.

Finally, in 2013, the CSSF carried out an assessment of the dissemination channels of companies specialised in the dissemination of regulated information, the list of which is published on the CSSF website. All the dissemination channels were compliant with the criteria mentioned in the FAQ No 10 regarding transparency and fulfil the requirements of Article 13(2) of the Grand-ducal Transparency Regulation. Thus, the names of these specialised companies were kept on the list published by the CSSF on its website. The CSSF plans to do such an assessment every two years henceforth.

4.3. Review of the Transparency Directive

Directive 2013/50/EU of 22 October 2013 which mainly amends the Transparency Directive (2004/109/EC) was published on 6 November 2013. The purpose of the directive is to ensure greater efficiency of certain requirements of the Transparency Directive and to enhance legal clarity in order to guarantee a high level of investor protection.

In this context, it should be noted that, even if the purpose of Directive 2013/50/EU is to make certain requirements applicable to small and medium issuers more proportionate, the latter are however not subject to a specific regime and must thus be compliant with all the rules laid down in order to guarantee a high level of investor protection.

The main amendments introduced by Directive 2013/50/EU which must be made applicable in Luxembourg through changes in the provisions of the Transparency Law, concern the following points.

• Home Member State

In order to avoid that certain issuers escape supervision by a competent authority of a Member State as long as they do not choose and disclose the home Member State, the definition of the “home Member State” hence provides that any issuer omitting to disclose its choice of home Member State within a period of three months shall have as home Member State any Member State in which its securities are admitted to trading on a regulated market until the choice of home Member State has been made and disclosed. If the securities of the issuer are already admitted to trading on a regulated market, the deadline of three months will start as from 27 November 2015.

The rules concerning the disclosure of the choice of home Member State were also amended in order to ensure that the competent authorities of all Member States concerned (home, host Member State and Member State of the registered office of the issuer) are informed of the choice of the issuer’s home Member State. Other amendments introduce, in some cases, a larger flexibility as regards the period of three years during which the choice of an issuer’s home Member State remains valid.

• Duration of the storage

The issuers which publish annual or half-yearly financial reports must henceforth ensure that these reports remain available to the public for at least 10 years instead of the previous five years.

• Deadline for the publication of the half-yearly reports

The time limit to publish the half-yearly financial reports covering the six first months of each financial year is set at three months as from the end of the half-year in question instead of the current two months. This longer deadline should offer more flexibility to issuers and reduce their administrative burden.

• Interim management statements

The obligation to publish the interim management statements or the quarterly financial reports is repealed, which should allow reducing short-term pressure on issuers and foster a longer term vision for the investors.

• Notification of major holdings

Several amendments were made regarding the obligation to notify major holdings in order to ensure adequate transparency and to take into account financial innovation. The definition of financial instruments was amended in order to cover all instruments with similar economic effect to holding shares to which voting rights and entitlements to acquire such shares are attached. For financial instruments which provide exclusively for a cash settlement, the new rules lay down that the number of voting rights is calculated on a “delta-adjusted” basis in order to reflect the exposure of the holder to the underlying instrument. Furthermore, unlike the current provisions still applicable in Luxembourg which do not provide for an aggregation, the amendments lay down that the number of voting rights held directly or indirectly is aggregated with the number of voting rights relating to financial instruments held directly or indirectly. ESMA is responsible for the preparation of several technical standards in order to ensure a consistent harmonisation of the regime for the notification of major holdings.

• Reports on payments to governments

Issuers active in the extractive or logging of primary forest industries must draw up, on a yearly basis, a report at consolidated level on payments made to governments in order to enhance the transparency for these types of payments. This report is made public at the latest six months after the end of each financial year and remains available to the public during at least 10 years.

• **New loan issues**

The obligation to disclose new loan issues could have led to certain procedural implications. This requirement is repealed.

• **Amendments to the statutes**

The obligation to communicate any amendment to the instrument of incorporation or statutes of the issuer to the competent authorities of the home Member State is also repealed. Indeed, this obligation duplicated the requirements of Directive 2007/36/EC on the exercise of certain rights of the shareholders in listed companies and created confusion regarding the role of the competent authority.

• **Penalties and disclosure of decisions**

The sanctioning powers are enhanced in order to improve compliance with the requirements of the Transparency Directive. Each sanction or measure imposed following the infringement of the transparency legislation will be disclosed at the earliest opportunity and will include information on the type and nature of the infringement as well as the identity of the natural or legal persons responsible. Such a disclosure may however be postponed or published anonymously in certain cases.

5. ENFORCEMENT OF FINANCIAL INFORMATION

5.1. Consistent enforcement of accounting standards

5.1.1. General framework

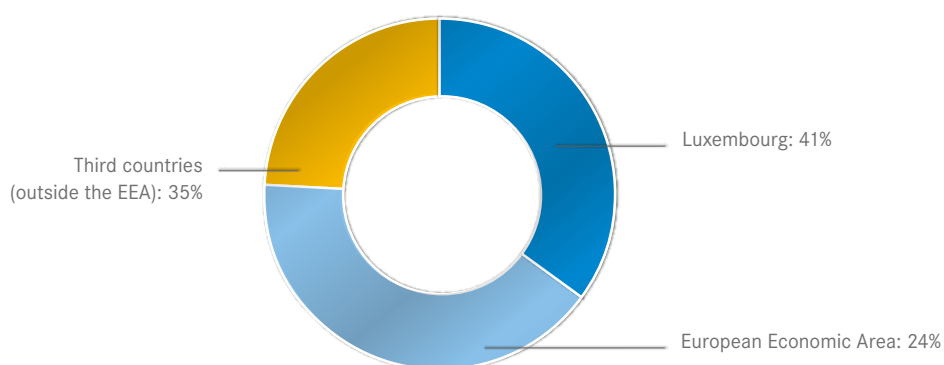
• **Legal and regulatory framework and pursued objectives**

Within the context of its mission of supervising securities markets, the CSSF is in charge of examining the financial information published by issuers of securities. For a detailed description of the context and objectives of this activity, known in this chapter under the generic term of “enforcement”, please refer to item 4.1.1. of Chapter IX of the CSSF’s Annual Report 2011.

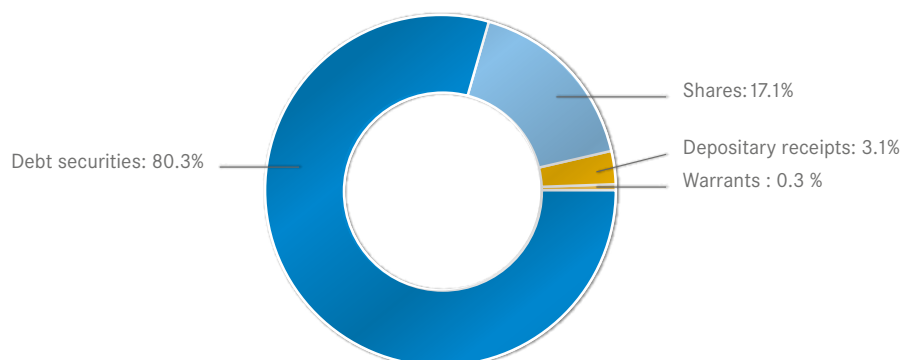
• **Population subject to enforcement**

Under the Transparency Law, and by taking into account the exemptions provided for in Article 7 of this law, the population of issuers falling within the scope of enforcement as at 1 January 2013 amounted to 304 entities (2012: 321) with the following characteristics.

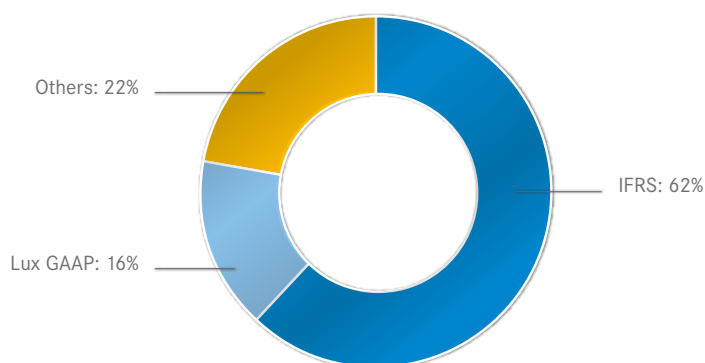
Breakdown of the 304 issuers according to country of registered office



Breakdown of the 304 issuers according to the type of securities admitted to trading



Breakdown of the 304 issuers according to the accounting framework used for the preparation of financial information



5.1.2. Remit of the CSSF and appropriate measures

• Powers and penalties

The powers and penalties available to the CSSF as regards enforcement are set out in Articles 22, 25 and 26 of the Transparency Law.

For a detailed description of the principles applied by the CSSF in this context, please refer to item 4.1.2. of Chapter IX of the CSSF's Annual Report 2011.

• Types of reviews

For the selected issuers within the context of the Transparency Law, the actual reviews follow a risk-oriented approach as the degree of intensity of the controls carried out is correlated with the acknowledged risky and sensitive nature of the issuer.

The review programme, defined every year for the selected issuers, includes:

- global reviews of the proper application of the accounting standards applicable to the issuer, where all the aspects of the issuer's financial statements can be examined (hereafter "general reviews");
- reviews of one or several specific aspects of the issuer's financial information predefined according to their importance, their potential impact, etc. (hereafter "specific reviews");
- thematic reviews during which the CSSF reviews the practices followed by a sample of issuers concerning specific items (hereafter "thematic reviews"); and
- follow-up reviews during which the CSSF ensures that the issues identified during the previous reviews were appropriately dealt with and taken into account by the issuers concerned.

Depending on the intensity of work or the cases analysed, these reviews will include many direct and repeated contacts (meetings, exchange of mail, conference calls) with representatives of the issuer and/or its external auditor in order to analyse the most sensitive problems and issues and obtain information, documents and other objective evidence required to perform the review. Some reviews may also lead to on-site inspections at the issuers concerned. In 2013, about 20% of the general reviews carried out led to on-site inspections.

5.1.3. Enforcement process

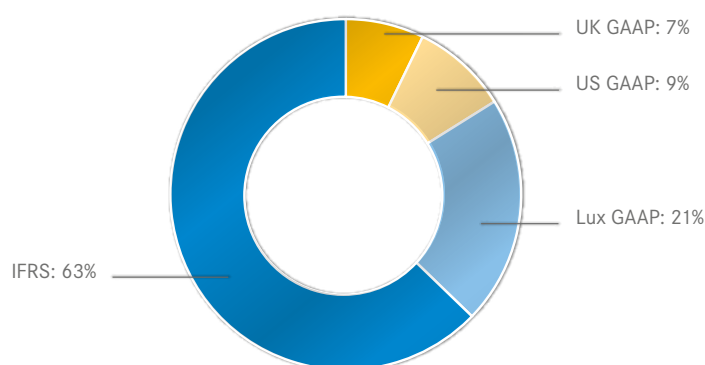
- **Selection mode**

The selection mode for issuers subject to enforcement within the context of the Transparency Law follows a risk-oriented approach, completed by a rotation and a random sampling method.

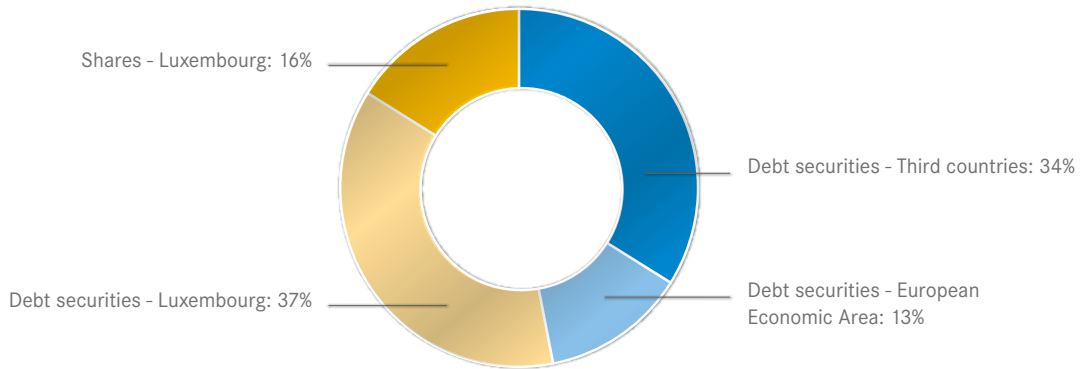
- **Reviews performed in 2013**

In 2013, the general reviews performed covered more than one-third of the issuers which the CSSF considers, on the basis of its specific approach, as the riskiest. These general reviews were supplemented by specific reviews covering other issuers. For the issuers concerned, the reviews carried out in 2013 covered the 2012 annual financial statements as well as the half-yearly financial statements for the financial years 2012 and 2013, if these were available at the date the reviews were performed. Thus, almost 20% of the issuers falling under the scope of enforcement were subject to a general or specific review in 2013, against a little over 10% during the previous campaign in 2012. The general and specific reviews concerned different categories of issuers and accounting standards used, covering a representative sample of the population of issuers supervised by the CSSF.

Breakdown of general and specific reviews according to the accounting standards used by the issuers



Breakdown of general and specific reviews by issuer type (according to the type of securities admitted to trading and registered office)



A thematic review of the half-yearly financial statements under IFRS of a large sample of issuers was also carried out in 2013. Thus, the CSSF has assessed the compliance of the half-yearly financial statements of some 115 issuers with the main disclosure requirements of IFRS standards, among which IAS 34 “Interim Financial Reporting”, focussing particularly on the impact of the implementation, in 2013, of new standards and amendments to the existing standards.

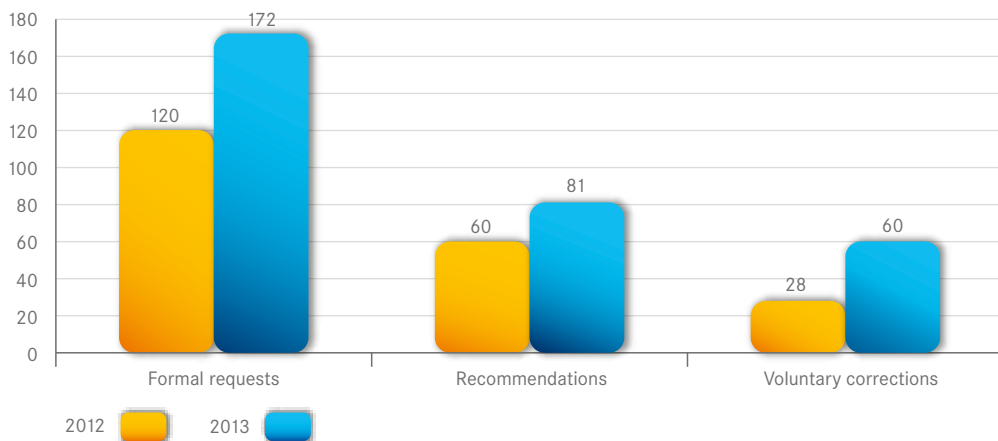
5.2. Result of works carried out in 2013

5.2.1. General and specific reviews
















Within the context of these reviews, the CSSF had to take decisions vis-à-vis certain issuers, aiming to either correct the identified errors or amend and improve the subsequent published financial statements. These decisions took the form of formal requests, recommendations and follow-up of corrections or improvements proposed by the issuer itself.

It should be noted that each issuer having been reviewed may have received several formal requests, recommendations or may have undertaken to amend or correct by itself several identified infringements.

Breakdown of decisions taken by the CSSF after the general and specific reviews carried out in 2012 and 2013



Breakdown of decisions taken in 2013 according to the relevant accounting standards

Standards	Number	
Lux GAAP	76	
IAS 1	50	
IFRS 7	46	
IAS 36	25	
IAS 7	24	
IAS 34	10	
IAS 10	9	
IFRS 13	7	
IFRS 8	6	
IAS 40	5	
IAS 39	5	
IAS 24	5	
IAS 19	5	
IAS 12	5	
Others	35	

5.2.2. Thematic reviews

The results of the thematic review of the half-yearly financial statements prepared according to IFRS standards led the CSSF to require from eight issuers corrected half-yearly financial statements as at 30 June 2014 by taking into account the requirements of IAS 34.

In addition, on 29 November 2013, the CSSF published Press release 13/51 listing the main breaches identified as well as the relevant requirements to fulfil.

5.2.3. Follow-up review

Issuers that were subject to a review during the 2012 campaign, and whom the CSSF requested to change or improve the 2012 financial statements concerned, were subject to a follow-up review in order to ensure compliance with the decisions taken by the CSSF.

In this context, administrative fines were imposed on three issuers that did not comply with certain formal requests of the CSSF as regards the improvement of the financial information in their 2012 financial statements or in their 2013 half-yearly financial statements.

5.2.4. Reviews within the context of the issue of prospectuses

As in the previous years, in 2013, enforcement reviews were performed within the context of the prospectus approval process, and in particular in the event of an application for the admission to trading on a regulated market. Besides the aspects directly related to accounting standards, the following subjects were also covered:

- preparation of pro forma data;
- treatment of business combinations under common control;
- consolidation; and
- equivalence to IFRS standards.

5.3. Main findings and recommendations in relation to the application of IFRS standards

The decisions taken following the works carried out in 2013, such as described above, covered the issues set by the CSSF at priority level for its 2013 enforcement campaign. The findings and recommendations described below provide an indication of the main observations made by the CSSF and must be taken into account by the issuers which publish their financial information according to IFRS standards. These being, however, specific questions, they will not necessarily apply to all issuers and they must be considered in view of their relevance and materiality.

These recommendations must not be considered as interpretations or definitions of the international accounting standards for which only the IASB and its interpretation committee IFRS IC are competent.

5.3.1. General recommendations

The question of the volume of information included in the financial statements under IFRS is regularly asked and an analysis of this problem is currently undertaken, particularly by the IASB. In this context, the CSSF reminds that, considering the requirements of IFRS standards, the materiality and specificities of the information provided in the financial statements should be taken into account in order to favour the relevance of the information disclosed rather than an essentially exhaustive approach aiming at including all the requirements and descriptions presented in the standards. Indeed, this approach does not or only marginally allow the identification of serious issues and topics which are specific to the issuer.

In this context, IAS 1 “Presentation of the Financial Statements” specifies that the objective of the financial statements is to provide information about the financial situation and performance of an entity which is useful to a wide range of users in making economic decisions. It also introduces the notion of materiality by indicating that the omissions or inaccuracies of elements in the financial statements are significant if they can influence individually or collectively the economic decisions that users make on the basis of the financial statements.

Thus, the CSSF recommends issuers to ensure that the information presented in their financial statements is relevant to their understanding and that it allows the users to focus on the most significant issues.

5.3.2. Specific recommendations following enforcement reviews

• Presentation of the information related to financial instruments and their inherent risks

As specified in Press release 13/51 listing the set priorities, in 2013, the CSSF focussed in particular on the qualitative and quantitative information provided by the issuers regarding the exposure to risks related to financial instruments as well as on valuation and impairment issues related to these instruments.

Fair values of financial instruments

The CSSF noted that the information relating to fair values of financial assets and financial liabilities provided in the financial statements were often too general, not specific enough or insufficient, notably for fair values classified at levels 2 and 3 which are more based on judgments and hypotheses.

The CSSF reminds that the information presented in the annexe to the financial statements must allow reaching the detailed objectives through IFRS 7 “Financial instruments: Disclosure” and IFRS 13 “Fair Value Measurement” applicable as at 1 January 2013 in a forward-looking manner, namely understanding the valuation techniques and the entry data used to measure the fair values as well as, as regards the recurring measurements made based on significant unobservable data, the impact of these valuations on the net results or other elements of the overall result of the period (IFRS 13.91). It should also be noted that IFRS 13 is particularly rigorous in terms of information to be provided for the fair value accounting of assets and liabilities and classified at level 3: paragraph 93 of IFRS 13 requires quantitative information on the main unobservable parameters used and qualitative information on the sensitivity of the fair value to the variations of the main unobservable parameters in case of potentially significant impacts. The CSSF requests thus that the issuers particularly focus on information to be provided related to the valuation at fair value of their financial assets and financial liabilities.

Risks linked to financial instruments

As regards the information linked to the risks inherent to the financial instruments, the CSSF noted that the information given to comply with certain provisions of IFRS 7 could sometimes be improved. Indeed, the CSSF considered that the information presented in the annexe to the financial statements of certain issuers did not always allow the users to precisely assess the nature and extent of the risks arising from financial instruments to which these issuers are exposed, as required by paragraph 31 of IFRS 7. For each type of risk (credit risk, liquidity risk, market risk, concentration risk, etc.), the CSSF expects the issuers to provide sufficient qualitative and quantitative information which is adapted to the specificities of their financial instruments and of the sector of activity in which these issuers operate. The CSSF recommends to certain bond issuers to focus particularly on this problem, notably in case the amount of repayments of certain debt instruments issued is conditional on the value of the financial instruments held.

Other focal points

In October 2013, ESMA published a comparative study on the financial statements of some 40 financial institutions of Europe. Some findings and observations included in this study were also made by the CSSF, namely those regarding qualitative and quantitative information in relation to:

- liquidity risk to which an entity is exposed through its financial instruments; thus, as required by paragraphs 39(a) and (b) and B11D of IFRS 7, the issuers must provide an analysis of the maturities of the (derivative or non-derivative) financial liabilities which show the remaining contractual maturities which must correspond to the non-current contractual cash flow;
- dealing with renegotiation of loans in the lenders' accounts (hereafter "forbearance"). The CSSF is expecting that the issuers who are significantly concerned by these problems present the required information, i.e. a definition of forbearance, a description of the related applied accounting method as required by paragraph 21 of IFRS 7 and the qualitative and quantitative information required by paragraph 34 of IFRS 7.

• **Statement of cash flows**

The statement of cash flows is a tool which is particularly useful for the analysis of the performance of an entity, notably in difficult financial periods. It facilitates the understanding of the causes of cash variation over a given period. This information allows notably the users of the financial statements to determine how much the entity generated cash and informs of the use of the available cash.

During the review of the statements of cash flows prepared by some issuers, the CSSF particularly ensured compliance with the following requirements for the financial statements of every selected issuer:

- the general presentation of the table of cash flows in accordance with IAS 7;
- the classification of the cash flows according to their nature, to the most appropriate manner for the issuer's activity and to the operating, investing and financing activities;
- the identification of cash equivalents;
- the description of the accounting methods applicable for the determination of the cash and cash equivalents composition;
- the relevance of the adjustments made to the results of the entity when the indirect method is used for the presentation of the cash flows for operating activities;
- the consistency of the reconciliation of the amounts presented in the table of cash flows with the elements presented in the balance sheet as well as in the notes to the financial statements;
- the inclusion of other additional information which may be relevant for the users of the financial statements.

The population reviewed by the CSSF covered a sample of issuers from different activity sectors (banks, commercial companies, financing companies, real estate companies, etc.).

Generally, the reviewed issuers presented satisfactorily all the cash flows over the period by allocating them appropriately in the three categories provided (operating, investing and financing activities) in accordance with the nature of their activities. However, some problems were identified with a few issuers.

Cash equivalents

The CSSF would like to remind that an investment normally qualifies as a cash equivalent only when it has a short maturity of, say, three months or less from the date of acquisition. In most cases, the issuers concerned considered the investments whose residual maturity was less than three months as cash equivalents whereas the maturity date must be analysed from the date of acquisition of the investment. Moreover, the IFRS Interpretation Committee confirmed this requirement in its press release of May 2013.

Reporting cash flows from operating activities

The CSSF also noted that most issuers used the indirect method to report the cash flows linked to their operating activities. However, the adjustments for the effects of transactions of a non-cash nature, any deferrals or accruals of past or future operating cash receipts or payments, and items of income or expense associated with investing or financing cash flows that the use of this method implies were not systematically presented in a proper manner. The CSSF recommends that the issuers concerned present these adjustments in a clear and adequate manner, in line with the requirements of paragraph 20 of IAS 7 in order to provide information which is relevant for the understanding of these cash flows for operating activities. The CSSF reminds also the issuers that the use of the direct method, whereby major classes of gross cash receipts and gross cash payments are disclosed, is encouraged by paragraph 19 of IAS 7.

Other disclosures

Finally, the CSSF noted in several cases that the cash flows from interest and dividends received or paid were not disclosed separately in the table of cash flows as required by paragraph 31 of IAS 7. The CSSF reminds that these flows must be disclosed separately and classified in a consistent manner from period to period as either operating, investing or financing activities.

• Impairment of non-financial assets

Another priority in the controls made by the CSSF in 2013 was the depreciation of intangible assets, among which goodwill and other intangible assets with indefinite life.

During the controls made of the issuers concerned by this problem, the CSSF noted that improvements were necessary particularly for the following disclosures:

- key assumptions for the estimation of recoverable amounts

The CSSF reminds that paragraph 134 of IAS 36 "Impairment of assets" requires, in particular, to disclose for each cash-generating unit for which a significant or intangible asset with indefinite life is allocated, the key assumption on which the entity has based its determination of the recoverable amount, the approach used to determine these key assumptions by mentioning for each assumption if the affected value reflects past experience or is consistent with external sources of information and a sensitivity analysis of recoverable amount to possible assumption changes. The CSSF would also like to point out that in cases where the chosen key assumptions significantly differ from past performances, paragraphs 134(d)(ii) and (e)(ii) require to explain these differences.

- the sensitivity analysis of recoverable values to possible assumption changes

For some reviewed issuers, the CSSF noted that the disclosures on the sensitivity of the impairment test results to key assumption variations and on the existing security margin did not completely comply with the requirements of the relevant paragraphs of IAS 36. The CSSF asks the issuers to ensure that they provide the information necessary for the appropriate understanding of the challenges of the issuers concerned.

• Half-yearly financial statements according to IAS 34

During the thematic review relating to the half-yearly financial statements drawn up according to IAS 34, the CSSF paid particular attention to the impact, in the 2013 half-yearly financial statements, of the entry into force of the new standards applicable to the financial years starting after 1 January 2013. Thus, the CSSF noted that some infringements were directly related to these standards.

The CSSF reminds that in case of changes in the accounting or calculation methods adopted in the interim financial statements, IAS 34 requires a description of these changes and their effects. Thus, the CSSF has noted that, among the main effective amendments applicable in many 2013 half-yearly financial statements, the impacts of the first application of the revised IAS 19 “Employee Benefits”, of IFRS 13 and the amendments to IAS 1, have not always been sufficiently described, in particular when these impacts were important in the half-yearly financial statements for the issuer.

Besides the description of the new accounting methods, the information on fair value of financial instruments was sometimes incomplete or even absent for a great number of reviewed half-yearly financial statements. Yet, paragraph 16A(j) of IAS 34 requires the disclosure in interim statements of certain information in relation to the fair value of financial instruments as provided for by IFRS 7 and IFRS 13.

The CSSF also noted that the requirement of paragraph 82A of IAS 1 requiring separate disclosure of the items that compose the “other comprehensive income” and that will be reclassified subsequently to profit or loss and those which cannot be reclassified in profit or loss were not always applied by the issuers.

The CSSF also noted recurring breaches or inconsistencies. Thus, some issuers have not yet reported the right comparative periods in the half-yearly financial statements as laid down in paragraph 20 of IAS 34.

5.4. Prospects for the 2014 campaign

The enforcement campaign for the financial year 2014 will follow an approach similar to the one of the preceding financial years. The selected issuers will be subject to general reviews and more targeted specific reviews. In the framework of the thematic reviews, the CSSF decided to examine once more the compliance with the requirements of IAS 34 in the published interim financial statements, in particular in order to follow up the controls made in 2013.

In addition, within the context of the 2013 closing of accounts, the CSSF, through Press release 14/02 published on 8 January 2014, decided to draw the attention of issuers, preparing their financial statements in accordance with IFRS standards, to a certain number of topics and issues which will be specifically monitored during its 2014 enforcement review campaign.

Moreover, some priority issues were identified by ESMA for the assessments carried out by the national competent authorities and were described in detail in ESMA’s press release of 11 November 2013.

5.5. European cooperation: works of the Corporate Reporting Standing Committee (CRSC) on the financial and accounting information

ESMA’s work in the field of accounting, auditing, periodic information and storage of the regulated information is led by the CRSC (cf. item 2.1.3. of Chapter II “European dimension of the supervision of the financial sector”). Enforcement-specific topics are discussed within the EECS forum (European Enforcers Coordination Sessions).

The EECS forum is composed of 38 members representing the different national competent authorities in the enforcement field, including the CSSF. Its purpose is to list and share the main decisions on the application of IFRS standards to guarantee a convergent approach of the supervision, by the national competent authorities, of the application of IFRS standards by companies listed on a regulated market.

Even if the group does not make decisions directly, the EECS forum allows the national competent authorities to discuss the decisions taken by the other members in their respective jurisdictions and to share their experience and knowledge.

In 2013, the main activities of the EECS forum covered the following topics:

- discussion of decisions taken and specific issues encountered by the national competent authorities during their enforcement reviews;
- meetings with the representatives of the IFRS Interpretation Committee to discuss complex practical cases identified by the members of the forum during their work;

- publication of reports and studies on specific issues such as the review of the information provided by the financial institutions in the financial statements drawn up according to IFRS; and
- studies performed on the practical application of some IFRS standards such as the review of impairment of goodwill and other intangible assets in the IFRS financial statements.

The decisions presented and discussed during the EECS forum meetings are entered into a dedicated database which already comprises 716 decisions taken by the national competent authorities. Since 2007, the EECS has been publishing extracts of its database on a regular basis. Thus, 21 decisions were published in 2013, bringing the number of decisions published to 161.

It should be pointed out that the CSSF participates in the specific working group on the revision of the standards on enforcement. This working group reviews the existing standards in order to enhance the common review methodology and their practical application so as to reinforce convergence of the enforcement of the financial information in Europe. These future guidelines consist of instructions issued by ESMA whose compliance must be subject to a confirmation by the national competent authorities to which they apply. The current draft instructions were subject to a publication for consultation by ESMA in July 2013. The comments received are currently being analysed within the working group.

6. SUPERVISION OF MARKETS AND MARKET OPERATORS

6.1. Reporting of transactions in financial instruments

6.1.1. Obligation to report transactions in financial instruments

The reporting regime in respect of transactions in financial instruments is mainly set down in Article 28 of the law of 13 July 2007 on markets in financial instruments (MiFID Law) which transposes Article 25 of Directive 2004/39/EC of 21 April 2004 on markets in financial instruments (MiFID). This article lays down the obligation for credit institutions and investment firms to report to the CSSF the transactions in financial instruments admitted to trading on a regulated market. The details set out in Article 28 were completed by the implementing measures of Regulation (EC) No 1287/2006 of 10 August 2006 implementing MiFID and clarified by the instructions set out in Circular CSSF 07/302.

Within the context of the review of MiFID, the European Commission published a proposal for a regulation (MiFIR) on 20 October 2011, which includes new obligations regarding the reporting of transactions in financial instruments to the competent authorities. These new obligations were discussed in detail in the CSSF's Annual Report 2011.

6.1.2. Credit institutions and investment firms concerned by the obligation to report transactions in financial instruments

As at 31 December 2013, 242 entities (credit institutions and investment firms incorporated under Luxembourg law and Luxembourg branches of credit institutions and investment firms incorporated under foreign law) fell within the scope of Article 28 of the MiFID Law and were potentially concerned by the transaction reporting regime (238 entities in 2012), including 147 credit institutions (141 in 2012) and 95 investment firms (97 in 2012). It should be noted that among the investment firms, only those authorised to carry out transactions in financial instruments, i.e. commission agents, private portfolio managers, professionals acting for their own account, market makers, underwriters of financial instruments and distributors of units/shares of UCIs, are subject to the reporting obligation.

As at 31 December 2013, 99 entities (101 in 2012), of which 87 credit institutions (89 in 2012) and 12 investment firms (idem in 2012), were required to send their transaction reports to the CSSF as their interventions are to be considered as "executions of transactions" within the meaning of the MiFID Law, as specified by Circular CSSF 07/302. The difference compared to the number of entities that are potentially concerned by the reporting regime results from the fact that, in practice, a certain number of entities, mainly investment firms,

are not subject to the obligation to report transactions in financial instruments because they do not conclude immediate market facing transactions and do not execute transactions on own account.

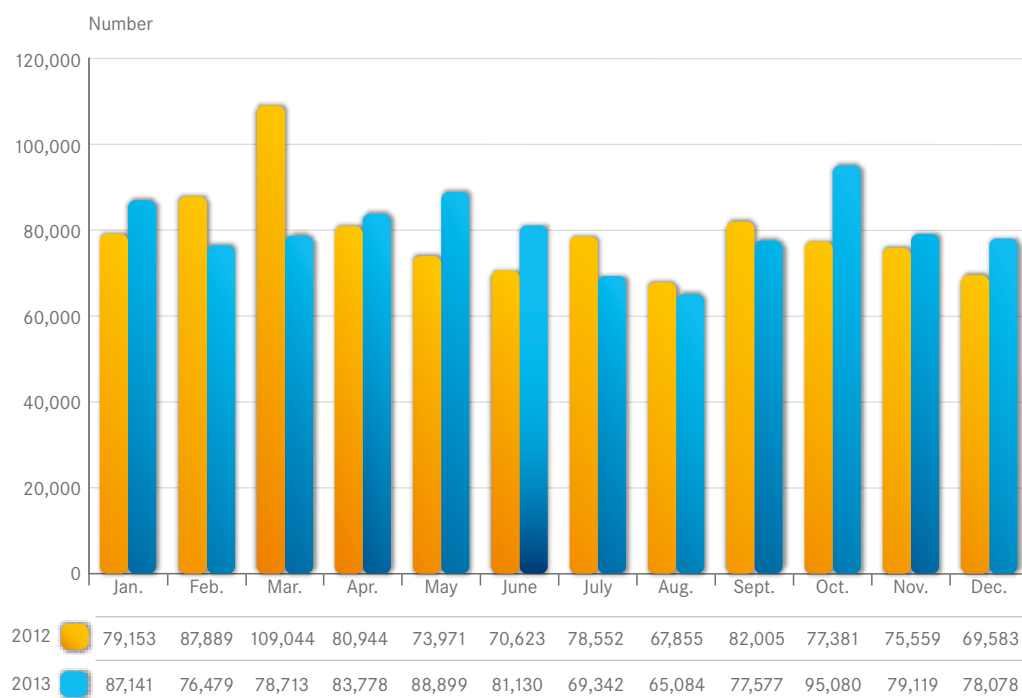
In 2013, the CSSF carried out two consistency tests campaigns aiming to check and improve the quality of the data on transactions in financial instruments. The CSSF also carried out one-off controls mainly aiming to identify the following shortcomings: irregular dispatch of transaction report files and missing reports on transactions executed by a member of the market *Bourse de Luxembourg*. In the framework of the controls carried out in relation to MiFID reporting in 2013, the CSSF intervened at 23 entities for which shortcomings were detected. In this context, 16 entities received deficiency letters.

Based on the controls carried out in 2013, the CSSF would like to remind the reporting entities that they must also comply with the instructions and procedures defined in the *Recueil des instructions TAF*. Thus, the entities must systematically check the return files generated by the CSSF following the dispatch of transaction report files and correct the errors according to the mechanisms defined for these purposes and within the deadlines set by the regulation in force.

6.1.3. Development in the number of transaction reports in financial instruments

In 2013, the number of transaction reports sent by the entities and accepted by the CSSF reached 960,400 (+0.82% compared to 2012).

Monthly volume of MiFID reports accepted in 2012 and in 2013

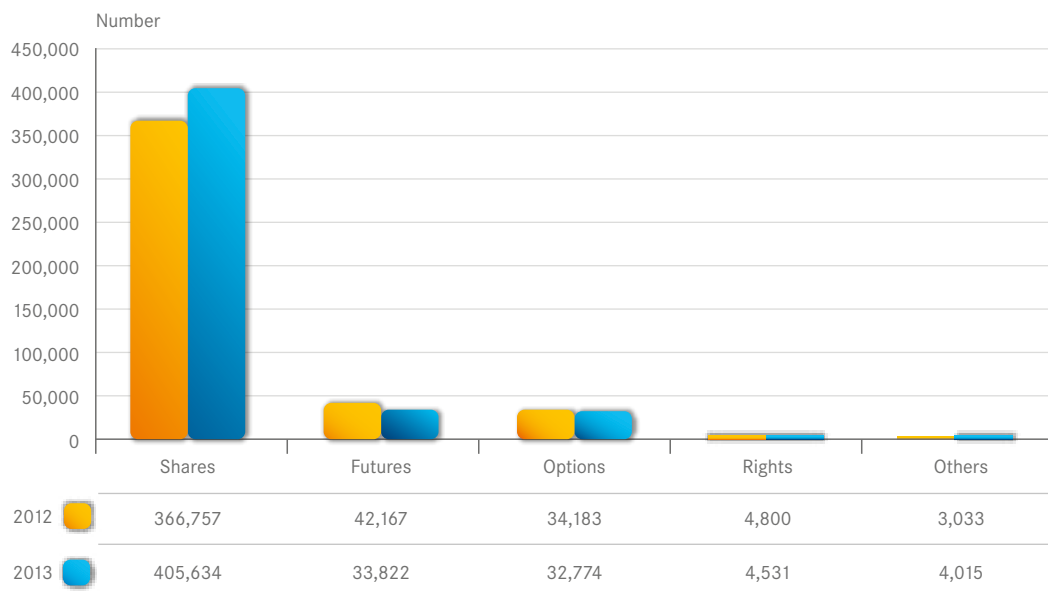


Breakdown of transactions by month and by type of instrument in 2013

	Bonds	Shares	Futures	Options	Rights	Others	Monthly total
CFI Code	(Dxxxxx)	(Exxxxx)	(Fxxxxx)	(Oxxxxx)	(Rxxxxx)	(Mxxxxx)	
January	46,086	36,169	1,935	2,208	400	343	87,141
February	36,280	34,637	2,778	2,377	136	271	76,479
March	39,667	33,240	2,849	2,247	168	542	78,713
April	43,874	33,968	2,807	2,484	283	362	83,778
May	43,716	38,129	2,826	2,992	878	358	88,899
June	44,737	27,534	5,136	2,937	329	457	81,130
July	42,302	19,629	3,456	3,186	457	312	69,342
August	30,766	28,135	2,966	2,718	289	190	65,064
September	35,903	36,098	2,668	2,251	377	280	77,577
October	42,562	47,462	1,973	2,181	540	362	95,080
November	37,109	37,352	1,697	2,251	408	302	79,119
December	36,622	33,281	2,731	4,942	266	236	78,078
Annual total	479,624	405,634	33,822	32,774	4,531	4,015	960,400

In relative terms, the majority of the 2013 reports concerned transactions in bonds (49.94%), followed by transactions in shares (42.24%). Transactions in other types of instruments represented only a small part (futures: 3.52%; options: 3.41%; rights: 0.47%; others: 0.42%).

Annual comparison of transactions by type of instruments



This data as well as the evaluation of the information received via TREM (Transaction Reporting Exchange Mechanism), set up between competent authorities for their respective supervisory missions, reveal the trends on European markets and, particularly, on the Luxembourg market. The main purpose of the supervision of the 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 are drawn up on the basis of the received reports. These ex post analyses of transactions in financial instruments can be used as a starting point for the CSSF's inquiries.

6.2. Supervision of stock exchanges

The establishment of a regulated market in Luxembourg is subject to a written authorisation of the Minister responsible for the CSSF. Chapter 1 of Title 1 of the MiFID Law sets out the authorisation conditions and requirements applicable to regulated markets. Where the operator of such a regulated market is established in Luxembourg, it must also obtain an authorisation as specialised PFS in accordance with the law of 5 April 1993 on the financial sector. The acts relating to the organisation and operation of the regulated market are supervised by the CSSF.

Pursuant to the provisions of the MiFID Law, the operation of a multilateral trading facility (MTF) is part of the investment services and activities defined in that law. MTFs may be operated either by a market operator, or by a credit institution or investment firm.

There are currently two markets operated in Luxembourg by the same operator, namely Société de la Bourse de Luxembourg S.A. (the SBL): 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.

The SBL is also the only company holding an authorisation as operator of a regulated market authorised in Luxembourg as defined in Article 27 of the law of 5 April 1993 on the financial sector. In this capacity, it is registered on the official list of specialised PFS.

On the basis of the analytical reports transmitted by the SBL and the electronic access to the information on market transactions, the CSSF monitors the market activities and the problems encountered in relation to these activities. The assessment of the SBL’s financial situation is performed, in particular, via the monthly reporting sent by the SBL.

In the context of its supervisory mission, the CSSF had several meetings and exchanges of mail with the SBL regarding, in particular, the creation of the subsidiary Fundsquare S.A., the practical arrangements concerning the cooperation under Article 4 of the law of 12 July 2013 on short selling of financial instruments and certain items included in the financial reporting.

As at 31 December 2013, the SBL had 61 members (among which nine market makers) authorised to trade on the SBL’s markets.

As far as market activities are concerned, the trading turnover on both markets operated by the SBL reached EUR 481.20 million in 2013 against EUR 451.73 million in 2012. Fixed-income securities represented almost 76% of the total volume traded in terms of amounts.

As at 31 December 2013, both markets operated by the SBL totalled 40,312 listings, against 42,061 in 2012, divided into 26,684 bonds, 7,036 warrants and others, 6,274 UCIs and 318 shares and certificates.

In 2013, 8,317 new issues were admitted to official listing against 8,121 in 2012. Instruments admitted in 2013 can be broken down as follows: 5,650 bonds, 1,647 warrants and others, 1,001 UCIs and 19 shares and certificates.

Among the admissions to trading on the regulated market operated by the SBL, a particular reference is made to the sovereign bond issues of the Grand Duchy of Luxembourg in March and July 2013. Moreover, the SBL continued in 2013 to admit the bond issues of the European Stability Mechanism (ESM) to trading on its regulated market as part of the ESM’s debt issuance programme.

The LuxX index closed the financial year 2013 with 1,448.94 points, i.e. a 16.10% increase over a year.

Since 1 April 2013, the criteria used to determine the composition of the LuxX index were changed. Thus, the distinction between Luxembourg and foreign shares is no longer made. In accordance with the management rules of the LuxX index, the SBL revised the LuxX index on 1 July 2013 and 2 January 2014.

Since 1 July 2013, the SBL has issued a new index, the “Lux RI Fund index” dedicated to the market of investment funds domiciled in Luxembourg and operating in the responsible investment sectors, mainly environment, ethics and social.

6.3. Short selling

The short selling regime covering also certain aspects of credit default swaps is mainly defined in Regulation (EU) No 236/2012 of 14 March 2012 on short selling and certain aspects of credit default swaps. In accordance with the law of 12 July 2013 on short selling of financial instruments, implementing Regulation (EU) No 236/2012, the CSSF is the competent authority in Luxembourg for the application of this regulation. The above-mentioned law also provides for a regime of sanctions and administrative measures applicable in case of non-compliance with the provisions of Regulation (EU) No 236/2012 or measures taken pursuant to the latter.

The CSSF publishes on its website under “Short selling” the relevant documentation and information relating to short selling and certain aspects of credit default swaps in Luxembourg as well as all the decisions to impose or renew the measures that the CSSF takes in accordance with the provisions of Regulation (EU) No 236/2012, including the notification, disclosure and restriction measures adopted in exceptional circumstances. Under this section, the CSSF also publishes a list of issuers of shares and issuers of sovereign debt for which the CSSF is the relevant competent authority under Regulation (EU) No 236/2012. Moreover, the CSSF Short Selling Platform for the notification of net short or uncovered positions or the disclosure of net short positions in accordance with Regulation (EU) No 236/2012 is available at <http://shortselling.cssf.lu>.

As at 31 December 2013, 74 position holders were validly registered on the CSSF Short Selling Platform to notify or disclose net short positions or uncovered positions. In 2013, the CSSF received 41 notifications of net short positions in accordance with Articles 5 to 9 of Regulation (EU) No 236/2012. 23 disclosures of net short positions in accordance with Article 6 of Regulation (EU) No 236/2012 were made on the CSSF Short Selling Platform.

In 2013, the CSSF did not adopt notification, disclosure or restriction measures laid down in the provisions of Regulation (EU) No 236/2012 in exceptional circumstances.

As at 31 December 2013, nine authorised primary dealers which validly notified the CSSF that they intend to use the exemption under Article 17(3) of Regulation (EU) No 236/2012 in relation to the issued sovereign debt of the European Financial Stability Facility and/or of the European Stability Mechanism fulfilled the conditions for this exemption.

7. INVESTIGATIONS AND COOPERATION

The mission of the CSSF is to combat insider dealing and market manipulation 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 following a request for assistance from a foreign administrative authority within the framework of international cooperation.

Based on Article 23(2) of the Code of Criminal Procedure, some facts which may constitute a breach of the Luxembourg criminal provisions and which were noted during the aforementioned investigations are also brought to the attention of the State Prosecutor.

7.1. Investigations initiated by the CSSF

In 2013, the CSSF opened three investigations into insider dealing and/or market manipulation. These investigations are still in progress. Moreover, verifications in relation to an investigation initiated in 2010 will continue.

7.2. Investigations conducted by the CSSF upon request of a foreign authority

In 2013, the CSSF received the following requests: 37 requests regarding insider dealing (39 in 2012), 13 requests regarding market manipulation (16 in 2012), three requests regarding breaches of the requirements to report major holdings (four in 2012), two requests regarding financial fraud, two requests regarding short selling, one request regarding takeover bids, one request regarding the approval of prospectuses and two requests regarding the dissemination of financial information. Eight of these requests came from administrative authorities of non-EEA States.

The CSSF processed all the requests with the necessary diligence befitting cooperation between authorities.

The CSSF received one request relating to a Luxembourg company which was outside its legal competences and, therefore, the requested information was not transmitted to the requesting authority.

7.3. Suspicious transaction notifications

Based on Article 12 of the law on market abuse, the CSSF received 14 suspicious transaction reports in 2013 (19 in 2012). For underlying financial instruments admitted to trading on one or several foreign markets, i.e. a regulated market within the meaning of MiFID or another foreign market for which the provisions and prohibitions related to market abuse are similar to the requirements set out in the law on market abuse, the CSSF transmitted the notified information to the competent authorities of the market(s) concerned, thereby observing the cooperation obligation referred to in the law on market abuse and the relevant multilateral cooperation agreements. This information can lead these authorities to open investigations.

In 2013, the CSSF also received nine notifications of suspicious transactions transmitted by foreign authorities (13 in 2012) and analysed them with the necessary diligence.

In the context of its controls of compliance with the requirement arising from Article 12 of the law on market abuse and the implementation of internal procedures in order to comply with the professional requirements arising from the law on market abuse, the CSSF noted weaknesses in relation to the practical application of the provisions of the above-mentioned law by different Luxembourg entities. Consequently, the CSSF intervened with the entities concerned pursuant to the powers vested in it under the law on market abuse. The CSSF would like to draw the attention of the market participants to the fact that following the observations made, it will enhance its control in this area and invites all credit institutions and other professionals of the financial sector to verify the means implemented for compliance with the requirements they are subject to under the law on market abuse, including in particular those under Article 12.

In the context of the controls of compliance with the requirements arising from the above-mentioned Article 12, the CSSF issued four injunctions and two administrative fines for the non-compliance with the injunctions against institutions subject to its prudential supervision.



*Agents hired in 2013 and 2014: Departments “Supervision of specialised PFS”,
“Supervision of securities markets” and “Single Supervisory Mechanism (SSM)”*

Left to right: Jill DE MICHELE, Federico GENTILE, Anne-George KUZUHARA, Sandra JAKOBI,
Vania TINOCO PEREIRA, Cyrille TONNELET, Jérôme PICOT

Absent: Karol NASIOLKOWSKI, Karolina SZPINDA, Paul WILTZIUS

CHAPTER XI

SUPERVISION OF INFORMATION SYSTEMS



1. Activities in 2013
2. Supervision of information systems in practice

1. ACTIVITIES IN 2013

This chapter deals with the supervision of information systems of financial professionals, including mainly credit institutions, investment firms, specialised PFS, payment institutions and electronic money institutions. As regards the specific supervision of support PFS, please refer to item 3. of Chapter V “Supervision of PFS”.

1.1. Processing of requests for advice or authorisation

In 2013, the division “Supervision of information systems” processed 153 requests, namely:

- 60 applications for authorisation (IT part) for different types of entities (credit institutions, electronic money institutions, payment institutions, PFS);
- 93 requests for advice concerning IT projects submitted by supervised entities (IT outsourcing, websites, major system changes, etc.) and interventions to support the CSSF’s supervisory departments regarding specific IT issues (such as critical items of a management letter of a *réviseur d’entreprises agréé* (statutory auditor)).

The division also participated in 107 meetings (41 concerning application or business qualification files and 66 concerning specific projects presented to the CSSF) and in one introductory visit.

Due to an increasing number of files with growing complexity and the emergence of new technologies, the division enhanced its technical expertise in the areas of virtualization technologies, secure communication protocols, encryption protocols and algorithms, solutions for access tools to IT resources, and the aspects of confidentiality and control of distributed solutions (such as VoIP).

Finally, the department attended 15 national and international conferences on various topics, in addition to the national and international groups mentioned below.

1.2. Participation in national groups

In 2013, the department “Information systems and supervision of support PFS” represented the CSSF within the following committees, commissions, associations or working groups:

- the ABBL - Payments, ICT & Standardisation Committee. The Commission in which the CSSF participates as an observer devoted the bulk of its work to the European project SEPA (Single European Payment Area), coordinated by the EPC (European Payment Council) which entered into force on 1 February 2014. Other topics discussed on a regular basis included the security of online financial services as well as proposals for new European directives on payment services (PSF2) and on interchange fees.
- Operational Crisis Prevention Group for the financial sector (OCPG) under the aegis of the Luxembourg Central Bank. The mission of the OCPG consists in identifying the risks borne by the financial sector in relation to critical infrastructures, in order to suggest measures to prevent a possible operational crisis which would disrupt the functioning of the financial professionals and jeopardise the proper settlement of monetary operations. Following 2012, during which its work mainly consisted in defining communication procedures among its members in the event of a crisis, the OCPG tested these communication procedures in 2013 and also researched, identified and tested a tool allowing their automation.
- ALMUS (Association Luxembourgeoise des Membres et Utilisateurs SWIFT), which is the national association representing the interests of Luxembourg SWIFT users. The CSSF participates as an observer in the Board of Directors of ALMUS.

1.3. International cooperation

1.3.1. Coordination of pan-European information exchange projects

The evolution of the European legal framework calls for the launch of new pan-European projects for information exchange, as it almost systematically requires the creation of central registers by the European

microprudential supervisory authorities. Expert groups created within ESMA and the EBA coordinate these projects among national authorities.

• ESMA - IT Management and Governance Group (ITMG)

The ITMG is the ESMA governance body in charge of information system technology and ensures, as its main task, the coordination and follow-up of pan-European projects including, in particular, the exchange of transaction reports on financial assets and the collection of statistics on short selling.

In 2013, the ITMG introduced the SARIS system (Suspension And Restoration Information System) in accordance with Article 41 of MiFID. SARIS collects the notifications of suspension or deregistration of financial instruments and immediately informs the competent authorities of the other Member States.

The ITMG also monitored the implementation of the “Register” project in accordance with the requirements of Directive 2010/78/EU (cf. Chapter X “Supervision of securities markets”).

• EBA - IT Sounding board (ITSB)

The ITSB is in charge of coordinating the EBA’s pan-European projects that require the development of homogeneous IT solutions for regulators.

In 2013, the EBA started work to migrate its data collection platform to a new operator (to be defined). The CSSF, in order to ensure IT systems security, participates in the work of the IT Security Task Force launched at the beginning of 2014.

The CSSF also contributed to the update of the Financial Reporting (FINREP) and Common Reporting (COREP) taxonomy through its participation in the XBRL subgroup of the ITSB. The collection of the necessary data will start in 2014.

• ECB - IT Committee (ITC)

The ITC contributes to the development, implementation and maintenance of the IT networks and communication infrastructures used by the members of the European System of Central Banks (ESCB). The CSSF contributes to this committee whose work consists in setting up the Single Supervisory Mechanism (SSM) and the corresponding exchange of information required as from 2014.

1.3.2. International cooperation relating to the supervision of the supervised entities’ IT systems

Given the fast and continuous evolution of technologies, bringing about new forms of financial services (mobile payments) or more complex operational models (mutualisation of equipment) that are exposed to new risks, it is in the interest of any supervisory authority to take part in working groups allowing it to exchange information with its peers and benefit from each other’s experience. In view of the above, the CSSF takes part in the groups presented below.

• IT Supervisors Group (ITSG)

The CSSF has been participating in the international working group ITSG for several years. The annual international meeting, which was held in Beijing under the aegis of the China Banking Regulatory Commission (CBRC), allowed taking stock and exchanging information among regulators. The results of a preliminary investigation, carried out by the CBRC among the supervisory authorities, revealed that the three risks perceived as being the most significant are cybercrime, durability of systems and outsourcing.

These exchanges also allowed comparing the evolution of the use of cloud computing in the financial sector. The usage of a cloud is considered as outsourcing. The financial professional must be capable of performing effective controls in full transparency of how services are provided by the cloud provider, and the regulator must have a right of control of the cloud environment. The major providers of cloud-based services often lack transparency and do not allow the right of control. Some of these providers now wish to start discussions with

the national authorities of different countries in order to understand the expectations of the authorities and to offer their services to the banking sector.

Discussions also covered the availability of critical infrastructures for financial services, more specifically Distributed Denial of Service (DDoS) type attacks. Understanding the mechanisms that lead to a DDoS attack is crucial in order to anticipate attacks and implement preventive and defensive actions.

One country suffered such an attack which kept it isolated from the rest of the world for several days. A number of financial institutions, including some in Europe, have also been victims of this type of attack, of which, according to analyses, 80% are volumetric (system floods) and 20% application-level floods. The motivations of attackers are manifold and not always known: loss of reputation of the attacked financial institution with impact on stock markets, extortion, revenge, etc..

In the field of payment systems, the authorities exchanged their views on the emergence of new money-laundering mechanisms, notably through the use of virtual currencies.

Some authorities also presented their IT supervisory methods, which has allowed understanding, for areas which are identical among authorities, the link between the chosen method and the specificities of the financial sector (size and diversity of stakeholders, culture, acceptance of regulations, etc.).

• ECB - European Forum on the Security of Retail Payments (Forum SecuRe Pay)

Set up in 2011 on the initiative of the Payment and Settlement Systems Committee (PSSC) of the ECB, the Forum is chaired by the ECB. Luxembourg is represented by the CSSF and the BCL as active members. The Forum is a voluntary cooperative initiative between authorities and aims to facilitate common knowledge and understanding, in particular between national central banks and supervisors of payment service providers, of the risks and challenges related to the security of retail payments. The Forum deals with the challenges relating to electronic payment instruments and services available within the EU/EEA Member States or provided by service providers located in an EU/EEA Member State. The Forum's work focuses on the whole processing chain of retail electronic payment services (excluding cheques and cash), irrespective of the payment channel used. The Forum aims to address, in particular, areas where major weaknesses and vulnerabilities are detected, and, where appropriate, issues recommendations in order to remedy these weaknesses and vulnerabilities. The ultimate aim is to foster the establishment of a harmonised EU-wide minimum level of security among the authorities concerned. The members of the Forum commit to support the implementation of the recommendations issued by the Forum in their respective jurisdictions.

At the beginning of 2013, the Forum finalised its work on the security of Internet Payment services and published its final report "Recommendations for the security of Internet Payments" on the ECB's website. In order to facilitate and harmonise the assessment of the level of compliance of payment service providers (PSP), the Forum drafted, in 2013, a guide specifying each recommendation for use by the EU authorities concerned. This "Assessment guide for the security of internet payments" is available on the ECB's website since 4 February 2014 and may help PSPs as well as any other interested party (such as the external auditors of these entities) in self-assessing their compliance.

In 2013, the Forum has also pursued the following projects, initiated in 2012:

- Security of Payment Account Access services by persons (service providers) other than the account holders in the context of services offered by these service providers. These services consist in: (i) providing a consolidated view of all the assets held by a person owning several accounts with several institutions (account information services), and/or (ii) initiating payment transactions via the Internet on behalf of the account holder (payment initiation services). In January 2013, the Forum published, for public consultation, a draft report which presents a set of recommendations in order to improve the security of these services within the EU. In order to finalise its position on this subject, the Forum took into account all the comments received, as well as the proposed review of the European payment services directive (PSD2), which, unlike the currently applicable PSD, considers these services as payment services and will regulate these service providers. The Forum's position will be published soon.
- Security of mobile payments. The Forum's work on this subject resulted in November 2013 in the publication of a draft report "Recommendations for the security of Mobile Payments", which was subsequently submitted

for public consultation ending on 31 January 2014. The scope of this report covers three categories of mobile payments, namely (i) contactless payments, e.g. using NFC technology, (ii) payments using a specific mobile payment application (“app”) previously downloaded onto the customer’s mobile device and (iii) payments via Mobile Network Operators’ channels (e.g. SMS, USSD, etc.) without a specific “app” previously downloaded onto the customer’s mobile device. The Forum envisages finalising this report in 2014, taking into account the comments received following public consultation.

Finally, the year 2013 was devoted to discussions on whether and how to exchange information between authorities related to incidents and major security threats encountered by supervised entities, with the purpose of preventing and/or limiting the impact on other entities. The Forum also focussed on the latest legislative developments linked to its mandate, namely the proposed payment services directive (PSD2), the network and information security directive (NIS Directive) and the proposed regulation on interchange fees (IF Regulation).

• **EBA - Subgroup on Implementation and Supervisory Practices (SGISP)**

The EBA’s SGISP working group launched, in 2013, a study on the supervisory policies and practices in place in Member States related to IT risks within banks. The CSSF takes part in this Task Force composed of 11 authorities, representing nine Member States, and representatives of the EBA.

First of all, the Task Force drafted a questionnaire for all Member States. 25 countries participated in this study and returned their duly filled-in questionnaire by the end of 2013. The Task Force is currently compiling and analysing the information collected, with the aim of submitting a final report to the EBA in June 2014.

1.4. Developments in the regulatory framework

On 7 January 2013, the CSSF published Circular CSSF 13/554¹ on the evolution of the usage and control of resources access tools. During the year, discussions with the associations of professionals of the financial sector (CPSI, CLUSIL) confirmed the need to provide guidance on the circular in the areas of access to data and the related technical elements. This guidance will be made available as FAQs which are being finalised and which will be published on the CSSF’s website in 2014.

In the meantime, the CSSF reiterates that Circular CSSF 13/554 is applicable since the date of its publication, independently of the publication of the planned FAQs. Institutions falling under the scope of this circular may not invoke the absence of the FAQs in order to avoid assessing their compliance with the circular in question. The CSSF invites all institutions that are not yet compliant to come forward as soon as possible and to submit a plan to ensure compliance within a reasonable time. Failing this, sanctions will be imposed. Pending the publication of the FAQs, the CSSF is available to answer any question relating to Circular CSSF 13/554.

2. SUPERVISION OF INFORMATION SYSTEMS IN PRACTICE

Supervision includes verifying that supervised entities comply with the legal and regulatory framework, with the direct or indirect purpose to maintain or improve the professionalism of their activities. It focuses, in particular, on the technologies implemented for the information systems and takes into account the specific nature of the outsourcing of these services to support PFS or third parties, outside or within the group.

2.1. Proper use of encryption algorithms

The use of cryptography has nowadays become quite common, be it to protect data inside systems, such as in the form of files within applicative processing, or to ensure the confidentiality of data when outside of the environment controlled by the entity. Despite the wide-spread use of cryptographic technologies, the CSSF noted that in some cases obsolete protocols were implemented, or encryption algorithms and key sizes

¹ See also item 2.4.1. of this chapter.

were no longer in line with best practices. Transport media that are commonly reputed as secure, and were therefore generally non-encrypted by financial professionals, proved after thorough analysis to be insecure.

The CSSF reiterates that point-to-point encryption, subject to proper use, is currently the only way to effectively protect the confidentiality of information and the flows for which the entity is responsible in accordance with professional secrecy obligations. The entity has thus a means to guarantee its data confidentiality throughout the whole confidential data handling process, irrespective of the networks used.

This is particularly important in the cases where an entity is unable to demonstrate the end-to-end confidentiality of a technical solution or where a part of the solution is outside the entity's control. Solutions should therefore, as far as confidentiality is concerned, not be implemented solely based on their security reputation.

The CSSF invites the entities to systematically verify the cryptography used, the cryptographic applications, the security protocols and their encryption algorithms, the encryption key sizes, the best practices in terms of encryption implementation, etc..

Cryptography is a dynamic area impacted by the advancement of cryptanalytic processing powers and the detection of weaknesses in encryption mechanisms and encryption applications where components are regularly outdated. Entities must thus monitor the technical obsolescence of their applications, protocols, algorithms and key sizes and keep updating them if necessary.

The CSSF invites all entities to systematically describe, in the requests addressed to the CSSF, the protocols, algorithms and key sizes that they use within the scope of their solutions.

As an example, the CSSF draws the attention of the entities to the following aspects.

- **Protocols, algorithms and encryption keys**

- Obsolete protocol and algorithms:

The WEP (Wired Equivalent Privacy) protocol, as well as the symmetric encryption algorithms DES (Data Encryption Standard) and the stream cipher RC4 (Rivest Cipher 4) are, for example, considered as obsolete.

- Algorithms and key sizes currently deemed acceptable:

At present, an example of an acceptable symmetrical encryption algorithm is AES (Advanced Encryption Standard) with a key size of 256 bits. An example of an acceptable asymmetrical encryption algorithm is RSA (Rivest Shamir Adleman) with a minimum key size of 2,048 bits.

- **Server negotiation in an HTTPS connection**

When establishing an HTTPS connection, the communication protocol ensures that the server and the client negotiate the applicable level of security (encryption algorithm, key size). The server must be configured in such a way so as to ensure that neither key sizes below the minimum sizes defined above, nor obsolete encryption algorithms are accepted.

- **Remote connection protocols**

Remote connection protocols may, just as encryption algorithms, become obsolete. Entities must therefore regularly check the solutions they have implemented. The PPTP protocol (Point to Point Tunneling Protocol) is considered obsolete. It is recommended to use protocols such as IPsec or SSL, for instance.

- **MPLS Protocol (Multiprotocol Label Switching)**

MPLS networks may not, in themselves, be considered as secure. They are not capable of ensuring by themselves the confidentiality of the data flows they have been entrusted with. Confidential information that transits through MPLS networks must therefore be encrypted before entering the MPLS networks.

These examples are representative rather than exhaustive of the appraisals to be made of the IT infrastructures. Supervised entities need to have a complete overview of their use of cryptography. A good practice is to use the information security policy of the entity to centralise, formalise and manage these aspects.

2.2. Online financial services

In general, there are three categories of websites that offer financial services:

- informative websites that usually present the company and its products as well as other general, public information;
- consultative websites that require user identification and authentication allowing the user to access personal information such as, for instance, account or portfolio consultation;
- transactional websites that allow users, through authentication, to make banking transactions including notably transfers and securities transactions.

Until now, consultative and transactional websites were considered to be more vulnerable due to the fact that IT threats focussed on identity theft through phishing or trojans. These attacks targeted financial services customers.

However, fraudsters seem to refocus by attacking entities directly, for example by using security weaknesses of an informative website to access the company's internal network, e.g. through SQL injection. This method of attack exploits the programming weaknesses of applications and web servers visible on the Internet to reach the most sensitive points of the internal network. This makes it possible to obtain high-level accesses such as those of the administrators, to access to client data or even to payment systems in order to execute fraudulent transactions.

Another type of attack consists in embedding viruses, trojans or other types of malware in PDF files, for instance. Through this method, the fraudster hopes to gain, when the file is opened, access to the IT equipment of the customer or even to the databases containing confidential files of the financial professional.

The CSSF insists that all entities offering financial services through the Internet perform a penetration test when implementing or making major changes to the configuration of the chosen solution. The results of the penetration test shall be systematically submitted to the CSSF.

2.3. Electronic Mail and VoIP systems: confidentiality and outsourcing

As regards the confidentiality of messaging systems of companies, an essential distinction must be made between external and internal messaging systems.

Concerning external messaging systems, i.e. the messages received from and sent to outside the entity, the CSSF considers that clients of the financial professionals are aware of the risks of information disclosure on the Internet when they choose to communicate with the financial professional via e-mail or other types of electronic online communication (e.g. online messaging service). The integrity and confidentiality of electronic mail transiting through the Internet may not be guaranteed without setting up particular technical measures. The CSSF considers that it is the duty of the financial professional to inform its client of the risks inherent in this type of communication where the financial professional allows for communication between both parties by this means. This needs to be stated in the agreement signed between the client and the financial professional. The financial professional should also set its own limits to the use of the Internet e-mail system, even if its client deems this unnecessary. For example, the financial professional may prohibit the use of the Internet e-mail system to transmit orders to execute financial transactions, as the financial professional may not be able to guarantee the legitimacy of the message received from the client. It is quite easy for cybercriminals to create a false message and send it to the financial professional. Informed clients could consider their financial professional negligent and unprofessional, if the financial professional exposes themselves to the risks related to unrestricted e-mail communication over the Internet. The financial professional runs a reputation risk in this context.

However, the CSSF wishes to reiterate its position concerning the confidential nature of the internal messaging system. Internal messaging, used by the employees of the professional of the financial sector to communicate within the company, may contain confidential information related to customers, within the message itself as well as in any attachments. This is also true for support PFS whose clients are other professionals of the financial sector (e.g. a bank). Internal messages between support PFS employees may contain information

that is deemed just as confidential as information of individual clients. Such information could for example be the commercial purpose of the support PFS's client banks, their IT infrastructure chart or their internal IP addresses.

While the client of the professional of the financial sector is expected to know and accept the information disclosure risks within the Internet (external messaging), the confidentiality of its data within the professional of the financial sector is supposed to be guaranteed (internal messaging).

Consequently, if a professional of the financial sector wishes to entrust a third party with the management of the internal messaging server, the professional must comply with the applicable requirements relating to IT outsourcing (Circulars CSSF 12/552 or 05/178 depending on the status of the professional of the financial sector). Notably, and in any case, the PFS must guarantee the confidentiality of the client data by outsourcing:

- either to an institution authorised to access this information by the law of 5 April 1993 on the financial sector (Luxembourg credit institution or operator of secondary IT systems according to Article 29-4 of this law);
- or to an entity of its group, whereby the data is encrypted and the encryption keys are solely controlled by the Luxembourg entity and the encryption/decryption processes are located in Luxembourg (this solution is nevertheless quite unrealistic from a technical point of view for a messaging system);
- or to an entity of its group with full data access, on the explicit condition that the formal and informed consent has been obtained from all the clients concerned by this outsourcing and its consequences. Details on the characteristics of such a client agreement are given in item 2.6. below.

By analogy with the messaging systems, the CSSF makes the following distinction regarding VoIP systems:

- internal VoIP flows (i.e. between employees of the same legal entity) that may contain confidential information covered by the professional secrecy, as defined in Article 41 of the law of 5 April 1993 on the financial sector;
- external VoIP flows (i.e. between a person of the entity and an external person) that may transit outside the entity, meaning over a telecom network whose operator is subject to the telecommunications secrecy (to be distinguished from the professional secrecy under the aforementioned Article 41).

For any outsourcing project of a VoIP system, a professional of the financial sector shall make sure to comply with the same rules as those applicable to messaging systems.

2.4. Group relations

2.4.1. Control of IT systems

Articles 5 and 17 of the law of 5 April 1993 on the financial sector state that credit institutions and investment firms ("the institutions") must have in place control and security arrangements for information processing systems. Circulars CSSF 12/552 (point 85) and CSSF 05/178 (point 4.5.2.) specify that the institutions and other financial professionals must organise their IT function so as to be in control of it.

Circular CSSF 13/554 reiterates that the professionals of the financial sector must always have full control over the resources under their responsibility and the corresponding access to these resources, primarily for compliance and governance reasons and secondly in order to protect confidential data subject to professional secrecy.

Control over an IT system implies access to this system and corresponding rights to act on the system. When the system is shared or partly located in the group to which the entity belongs, the control by the entity becomes ambiguous.

Some of the proposed solutions claim to provide the entity with control through technical and additional organisational security measures. These solutions certainly add efficient intermediary access controls, however they do not remove the ultimate possibility of access by external persons to the Luxembourg entity and for interventions outside its control (access of Enterprise Administrators, for instance, or access to digital safes).

Thus, the concepts of least privilege, delegations, group policies, “four-eyes” principle or break-glass procedures are used either to deactivate or prevent privileged accesses (administrators) or to prevent control being taken over from outside. If these solutions are implemented within the group and managed by the group, they may not be invoked as security measures pretending to preserve total control at the level of the Luxembourg entity. In this case, the ultimate control remains outside the entity, i.e. within the group. Firstly, it is not the entity itself, but an administrator belonging to the group that implements the least privilege or the “four-eyes” principle. Then, once unlocked, these privileged accesses allow interventions without control by the Luxembourg entity.

For this reason, when considering a solution, it should always be considered where the ultimate means for obtaining access rights (privileged or not) to IT resources of the Luxembourg entity is located. This must always be under the control of the Luxembourg entity.

Taking into account these aspects is particularly important when choosing and implementing solutions for access tools to resources, notably with regard to the compliance with Circular CSSF 13/554.

2.4.2. Remote professional applications (encrypted), outsourced abroad within the group

In order to perform their business tasks, entities use specialised professional applications. These applications use, process, exchange and contain the business information of the entity, i.e. confidential data of its clients, subject to professional secrecy (Article 41 of the law of 5 April 1993 on the financial sector).

In some cases, these applications are installed and managed by the group outside of Luxembourg, the Luxembourg entity being able to use, through remote access, these applications as a service offered by the group. The mutualisation of resources and the technical feasibility seem to be simple and sufficient reasons of groups to be able to implement this operational model. However, besides the specific problems arising from remote use which are not reiterated at this stage, the main problem remains data confidentiality and keeping compliant with professional secrecy.

For some models, a simple anonymisation is not possible as data processing is complex. While data may be delivered to the application in encrypted form, the application needs them in clear form (i.e. readable) for processing. The application therefore needs to decrypt the information locally in order to make it available, making it at the same time accessible to the group’s employees (notably the IT administrators), thereby creating a professional secrecy issue.

Some applications integrate encryption/decryption features and claim to technically guarantee confidentiality within the application. The technical implementation of such applications is very specific and establishing whether it is compliant with the requirements of the Luxembourg financial sector remains complicated. In any case, it is not possible to technically prove that confidentiality is ensured in an unrestricted manner by these technical solutions presented by the providers.

For their part, service and application providers cannot claim to provide generic solutions that comply with the CSSF’s requirements as every implementation has to be reviewed in its own right. In 2013, the CSSF identified several difficult cases where providers presented allegedly compliant solutions which were accepted by entities but which were finally denied by the CSSF.

The CSSF reiterates that the entities remain in charge of demonstrating and proving that the solutions they wish to implement are compliant with the legislation, including at the technical level.

2.5. Continuity

2.5.1. Business Continuity Plan and emergency workstations

In 2013, the CSSF was called upon several times to comment on Business Continuity Plans (BCP) that, should the premises of the financial professional be unavailable, provide for the use of emergency workstations located abroad, notably to benefit from group installations or installations from another entity.

The CSSF reiterates that the entities must, at any time, and thus also when the BCP is activated, have their central administration in Luxembourg and guarantee the control and confidentiality of information.

The CSSF specifies that the emergency premises activated under a BCP must be located in Luxembourg, meet the standards of professional offices and guarantee the same level of security as the usual offices, while taking into account the proportionality with the usual business. This concerns, among other things, the physical security of the premises and their content (computers, confidential documents in paper format, etc.), as well as the security and redundancy of the new means of connection to the IT system from the emergency premises.

The CSSF insists that emergency premises envisaged in private homes or public places, such as restaurants or hotels, for example, are not acceptable.

Finally, the CSSF repeats that, in any event, the provisions of the law of 5 April 1993 on the financial sector (including the professional secrecy requirement) remain applicable in case of national catastrophe, without prejudice to any exceptional decisions that might be taken in such a crisis situation.

2.5.2. Continuity risk linked to dependence on a provider of a core business software

The professionals of the financial sector are using specialised business applications that are critical to their operations. A professional using an application provided by a third company becomes dependent on the provider of this critical application for its business. Should the provider default, the professional may encounter operating problems. The level of risk is proportionate to the level of dependency of the professional which, itself, depends on the criticality of the activity and historical information in the application.

Consequently, a professional must be able to detect this type of dependence and organise the continuity of the concerned activity, e.g. through anticipating the conditions of a migration to an alternative solution. This could be conditions linked to the application itself (discontinuation of the product, obsolescence, etc.) as well as conditions linked to the provider (bankruptcy, takeover, merger, etc.). Specific clauses must be included in the agreements to take into account such events which should not lead to a prohibition to use the product or to a contractual imbalance (substantial increase of prices in case of renegotiation of an agreement that became null and void). These clauses should also leave sufficient time to the financial professional to migrate to another system in sound conditions. The contractual management is of particular importance in a context of high, or even total dependency, on the IT means concerned.

It should be noted that dependency on business software also exists in the case of proprietary software. The risk mentioned above cannot be completely avoided. Indeed, lack of or insufficient internal risk management linked to a dependency may lead the financial professional to the same business continuity problems and jeopardise production. This is particularly true for old applications, written in an obsolete language or applications that centralise a core business activity for the professional.

2.6. Explicit customer consent (within the scope of third-party access to confidential data)

Circular CSSF 12/552, as amended by Circular CSSF 13/563, concerning central administration, internal governance and risk management applies to all credit institutions, investment firms and professionals carrying on lending operations.

Point 193 of this circular specifies that “the institutions may contractually use services for the management/operation of their systems [...] in Luxembourg [...] and abroad from an entity of the group to which the institution belongs provided that these systems do not include any readable confidential data on customers other than institutional customers, unless explicit consent is given by the customer or the owner of the data or his/her proxy, on the basis of an informed opinion on the purpose of this outsourcing, the specific nature of the final goal, of the content of the provided information, of the recipient and location as well as of the sustainability; in respect of institutional customers, the specific characteristics of this outsourcing shall be made explicit in the agreement.”.

Following various questions received in 2013 as regards the “explicit consent given by the customer” mentioned above, the CSSF wishes to specify the following.

For professionals of the financial sector other than credit institutions, investment firms and professionals carrying on lending operations, the question of access to confidential data by third parties within the scope of IT outsourcing is governed by Circular CSSF 05/178. Although this circular does not mention the possibility to obtain client consent for confidential data readable by the entity of the group providing the services, the CSSF considers that these other professionals may also consider this option. In this case, the definition of consent (explicit and informed) as provided for in point 193 of Circular CSSF 12/552, as well as the details given hereafter remain applicable as well.

The requirement of a consent applies to clients covered by the professional secrecy as defined in Article 41 of the law of 5 April 1993 on the financial sector. Thus, in the field of investment funds with an international customer base, the main focus remains to the Luxembourg banking relationship of the client which is subject to confidentiality. Fund unit holders operating from a Luxembourg banking relationship must therefore be covered by the professional secrecy of Article 41.

As regards the “explicit” character of the consent to be obtained, the following must be specified:

- a) A consent must be requested for any type of client, be it an institutional client or a natural/private person.
- b) This consent is required for all former, existing or future customers. For former customers whose data are, a priori, archived, if it is not possible anymore to obtain their consent, the contractual relation being terminated, the system concerned by the outsourcing may not contain their data.
- c) For private customers, “explicit consent is given by the customer or the owner of the data or his/her proxy, on the basis of an informed opinion on the purpose of this outsourcing, specific nature of the final goal, the content of the provided information, the recipient and location as well as of the sustainability” is required.
 - The agreement of the client must be sought in a visible place and may not only be part of the terms and conditions. As regards transfer agent activities, the agreement may, for instance, be integrated into the distribution contracts for fund managers and in the subscription/redemption forms for investors.
 - Existing private customers must receive and sign a specific consent document.
- d) For institutional clients, point 193 of Circular CSSF 12/552 simply states that “in respect of institutional customers, the specific characteristics of this outsourcing shall be made explicit in the agreement”.
 - A clause in the contract is thus sufficient, but it is clearly an explicit consent through the signature of the contract and not a simple implicit information or tacit consent.
 - Existing institutional clients must also receive and sign a specific document of consent, which may, for instance, be an annex to the contract.

2.7. Remote access to IT services (mobility and teleworking)

The CSSF reiterates the rules defined in the Annual Report 2007 (Chapter VIII, item 2.1.) concerning the remote access to IT services. These rules apply to all the professionals of the financial sector, including support PFS, and are still in force.

The CSSF notably reiterates that the number of persons benefiting from these remote accesses as well as the systems that can be accessed must both be limited. While these remote accesses are mainly used by IT personnel for urgent interventions or by senior executives when travelling abroad within the group, the CSSF observed that some institutions intend to use them henceforth by business teams on a regular basis. The CSSF considers that this type of use, which can be considered as teleworking, increases the risk of confidential data disclosure. Moreover, the central administration of the entity concerned, which must remain on the Luxembourg territory, is no longer guaranteed.

In any case, a professional of the financial sector that wishes to put in place a mobility/remot access project must take into account the elements above and shall submit its project to the CSSF beforehand.

CHAPTER XII

PUBLIC OVERSIGHT OF THE AUDIT PROFESSION



1. Regulatory framework of the audit profession
2. Quality assurance review
3. Overview of the population of *réviseurs d'entreprises* (statutory auditors) in Luxembourg
4. Cooperative agreements
5. Practice of public oversight of the audit profession

1. REGULATORY FRAMEWORK OF THE AUDIT PROFESSION

1.1. European Commission proposal for the audit reform

Following many meetings of the European Council, a compromise text was approved during the meeting of the Permanent Representatives Committee (Coreper) on 18 December 2013 as regards the proposed directive on statutory audits of annual accounts and consolidated accounts and the proposed European regulation on statutory audits of Public-Interest Entities.

In the end, the definition of Public-Interest Entity (PIE) was not amended and remains the same as in the current directive. Undertakings for collective investment and other alternative funds are not specifically referred to as PIEs in the current text.

The other amendments to the proposed directive will only slightly affect the audit profession in Luxembourg as regards the Code of ethics and internal organisation of the audit firms which were greatly modelled on the Code of ethics of the IESBA (International Ethics Standards Board for Accountants) and on the internal standard of quality control (ISQC 1). These standards have already been adopted via CSSF Regulation N° 13-01 and are applicable within *cabinets de révision agréés* (approved audit firms). It is the same for the organisation of the public oversight of the audit profession which complies entirely with the requirements of the proposed directive.

As far as the proposed regulation is concerned, it introduces strict restrictions for PIEs as regards the provision of services other than audit as well as the limitation of these services to 70% of the fees paid by these entities for the statutory audit of their accounts. This limit shall not be exceeded on average over the last three consecutive financial years subject to an audit. The fees received for the statutory audit as well as the provision of services other than audit to the parent company and to the subsidiaries must be taken into account for the calculation of this limit.

Tax services, services involving the participation in the management of the audited entity, the preparation of the accounting records, the preparation of the annual accounts, the calculation of the salary, the drawing-up and implementation of internal procedures, assessment services, legal services, internal audit services and human resources services of the PIE are prohibited. Nevertheless, the Member States have the possibility to waive this principle for tax and assessment services when these service provisions have little impact on the audited financial statements and when they do not trigger a risk of self-review.

Finally, a compulsory rotation of the audit firms will be implemented with a maximum period of 10 years renewable once and lasting as much, provided that it complies with the procedure for tenders.

1.2. Developments in the regulatory framework in 2013

1.2.1. Access to the profession

The Grand-ducal Regulation of 15 February 2010 determining the requirements for the professional qualification of *réviseurs d'entreprises* was repealed and replaced by the Grand-ducal Regulation of 9 July 2013 in order to guarantee appropriate training for candidates *réviseurs* (auditors).

Indeed, the situation assessed after the three first years of this regime shows that many trainees did not have an adequate university degree and that the high number of failures in the exams of the *certificat de formation complémentaire* was a consequence thereof.

Thus, the Grand-ducal Regulation of 9 July 2013 specifies and enhances the requirements for the professional training:

- To be admitted to the training, the candidates must henceforth prove that they have completed at least 10 out of the 15 subjects of the administrative certificate referred to in Article 2(2) of the above-mentioned regulation.
- As regards the complementary training certificate to be completed during the training, the trainees have a maximum of six academic semesters to complete all subjects of the certificate and the tests of each subject can be taken up to six times only, bearing in mind that the ordinary test and the remedial examination are

counted individually. After six failures in one subject, the candidate must complete again all the subjects passed until that date. Moreover, an unjustified absence at a session shall be considered as failure.

- For the examination of professional competence, the registered candidate who does not attend the written test will be totally referred, except if s/he provides a valid reason for his/her absence. The jury will assess the validity of the reason given by the candidate during its deliberation.

Furthermore, the third-country approval holders must henceforth submit the same complementary training certificate as the approval holders from an EU or an EEA Member State.

The CSSF regulations relating to the establishment of a consultative committee, to the establishment of a list of diplomas and approvals and to the training log, as well as the CSSF Circular presenting the law and regulations relating to the audit profession were amended accordingly.

The new CSSF regulation on the training log removes, for the trainees, the annual assessment to be submitted to the CSSF and reduces the number of information as regards the assignments to be included in the training log.

1.2.2. Activities carried out only by *réviseurs d'entreprises agréés* (approved statutory auditors) and *cabinets de révision agréés* (approved audit firms)

During 2013, the CSSF repealed and replaced the CSSF Regulation N° 11-01 of 8 July 2011 relating to the standards governing the audit profession by the CSSF Regulation N° 13-01 of 20 August 2013 in order to adopt:

- ISA 610 (revised) "Using the work of internal auditors" and
- ISA 315 (revised) "Identifying and Assessing the Risks of Material Misstatement through Understanding the Entity and Its Environment"

which apply to the financial years closing after 15 December 2013.

Similarly, following the entry into force of the Grand-ducal Regulation of 7 August 2012 defining the intervention thresholds, the annual financial ceiling, the non-financial local contribution as well as the audit obligations within the context of the co-financing of the programmes or projects submitted by the non-governmental development organisations pursuant to the amended law of 6 January 1996 on development cooperation and humanitarian activity, a new assignment was exclusively entrusted to the *réviseurs d'entreprises agréés*, namely the limited review engagement of the annual accounts of non-governmental development organisations which receive an annual co-financing of between one hundred thousand and five hundred thousand euros. In the framework of this engagement, the standard ISRE 2400 "Engagement to review historical financial statements" was also adopted.

1.3. Contribution to the regulatory framework

1.3.1. Common positions of the European regulators on international standards

In 2013, the CSSF signed joint letters with its European counterparts in the framework of the cooperation platform of the EAIG (European Audit Inspection Group) following the consultations organised by the body which draws up the international audit standards, namely the IAASB (International Audit and Assurance Standards Board).

• Diligences with respect to the information accompanying the audited financial statements

A letter of recommendations by the European regulators on the scope of information to be verified by the auditor, the diligences required from the auditor and the elements to be included in the audit opinion was addressed to the IAASB on 14 March 2013 in response to the draft on revised ISA 720 "The auditor's responsibilities relating to other information in documents containing or accompanying audit financial statement and the auditor's report thereon", issued in November 2012.

- **Framework for audit quality**

In January 2013, the IAASB published a consultation paper on the implementation of a framework for audit quality. In a letter dated 11 June 2013, the European regulators drew the attention of the IAASB to the necessity to clarify the ultimate purpose and status of this document with respect to the international standards on auditing, to the emphasis on key elements contributing to audit quality and to the key role of the auditors in delivering audit quality.

- **Development of the reporting on audited financial statements**

In July 2013, the IAASB published a proposal for revised international standards on auditing regarding the reporting on audited financial statements. This publication follows the public consultation of June 2012 in which the IAASB proposed to improve the audit report and to which the members of the EAIG (including the CSSF) answered in October 2012.

After examining the IAASB's proposal and discussing with the members of the EAIG, the CSSF signed a joint letter which was sent on 20 November 2013. The letter presents the recommendations of the European regulators as regards the key audit matters likely to be mentioned in the report, the inclusion of an explicit statement on the auditor's independence and compliance with ethical requirements, the information on materiality, the desirable provisions relating to going concern, the description of responsibilities of the parties and the structure of the report. This proposal was also subject to a joint comment letter of the members of the IFIAR (International Forum of Independent Audit Regulators) which includes the CSSF.

1.3.2. European database of the quality assurance review

In 2013, the 27 European regulators which met in the EAIG created a database in order to collect and exchange the national results of the quality assurance reviews relating to the PIEs for the 10 biggest European audit networks.

This database allows the EAIG to collect the results of the quality assurance reviews per network or per subject. It facilitates a common approach for the reviews, for their results and for the contemplated corrective measures. It enhances the exchanges between the EAIG, the audit networks and the international bodies such as the IAASB and the IESBA.

The observations made during these quality assurance reviews at European level were presented by the EAIG to the representatives of the IAASB and the IESBA during the annual meeting which took place in Paris in November 2013 and in which the CSSF participated.

2. QUALITY ASSURANCE REVIEW

2.1. Scope

2.1.1. General framework

By virtue of the law of 18 December 2009 concerning the audit profession (Audit Law), *réviseurs d'entreprises agréés* and *cabinets de révision agréés* are subject to a quality assurance review, organised according to the terms laid down by the CSSF in its capacity as supervisory authority of the audit profession, for assignments concerning statutory audits as well as for any other assignments which are conferred exclusively on them by the law.

The quality assurance review takes place at least every six years. This cycle of review has been brought down to three years for *réviseurs d'entreprises agréés* and *cabinets de révision agréés* that audit PIEs.

• Population of *cabinets de révision agréés* and *réviseurs d'entreprises agréés* concerned by the quality assurance review

The population of *cabinets de révision agréés* and *réviseurs d'entreprises agréés* that carry out statutory audits and other assignments conferred exclusively upon them by the law is as follows (as at 31 December 2013):

- Number of approved audit firms: 69, including 15 that audit PIEs;
- Number of approved independent *réviseurs*: 3, none of which audits PIEs.

Based on the data collected through the “Annual Annexes” for the year 2013, the statutory audit assignments break down as follows between *cabinets de révision agréés* and independent *réviseurs d'entreprises agréés*:

- 83% of the assignments are carried out by the “Big 4”¹;
- 11% of the assignments are carried out by medium-sized audit firms², and
- 6% of the assignments are carried out by the other audit firms and independent *réviseurs*.

2.1.2. Scope of the quality assurance review

The CSSF follows a global approach of control in which the audit firm is the entry point for the periodical quality assurance review.

The control of the audit firm consists in:

- appraising the existence within the firm, of an organisation, policies and procedures aimed to ensure the quality of the statutory audit assignments and the fact that it is designed and operating effectively, and the independence of the *réviseur d'entreprises agréé/cabinet de révision agréé* in accordance with the International Standard on Quality Control ISQC 1;
- verifying, based on a sample of assignments, the proper execution of certain assignments by the audit partners (*réviseurs d'entreprises agréés*);
- assessing the content of the transparency report for the *cabinets de révision agréés* concerned, based on the review work performed.

2.1.3. Organisation of the quality assurance review

A quality assurance review of an audit firm includes several stages:

- collection of preliminary information from audit firms;
- elaboration of a control plan;
- on-site inspections;
- presentation of the observations made;
- gathering the audit firm's responses to the CSSF's observations; and
- writing and issuing the report.

2.1.4. Conclusion of the quality assurance review

After the quality assurance review, the CSSF issues, on the one hand, conclusions for the reviewed *réviseurs d'entreprises agréés* that were subject to observations and, on the other hand, a summary for the audit firm.

Conclusions for the *réviseurs d'entreprises agréés* may impose different types of safeguards according to the deficiencies identified in the course of the assignments. Without being exhaustive, these safeguards may be

¹ Deloitte, Ernst & Young, KPMG and PWC.

² Firms that carry out more than 100 assignments reserved by the law to *réviseurs d'entreprises agréés* and *cabinets de révision agréés*. As at 31 December 2013, five firms were concerned.

training plans, internal reviews of files by another partner before issuing an opinion, a double signature of audit reports; they may be complemented, where applicable, by a specific follow-up in accordance with the provisions of Article 60 of the Audit Law.

The summary for the audit firm includes:

- the main deficiencies of the firm's internal organisation identified during the quality assurance review and for which the CSSF requires that corrective measures be taken;
- the list, where applicable, of the *réviseurs d'entreprises agréés* for which a specific conclusion has been issued, requiring an action plan from the firm to remedy the situation.

2.1.5. Follow-up on the conclusions of the quality assurance reviews of the previous financial years

A follow-up is set up to verify that the firms concerned have taken appropriate corrective measures and that the professionals for which deficiencies have been identified in the course of their statutory audit assignments address these shortcomings.

Where the weaknesses are not considered as being material, the corrective measures taken by the audit firms will be followed up during the next periodic quality assurance review scheduled within the legal deadlines. In case of material weaknesses, a specific follow-up will be programmed within 12 months from the date of issue of the report.

A specific follow-up may be programmed for the *cabinet de révision agréé* and/or for a *réviseur d'entreprises agréé* of the *cabinet de révision agréé*.

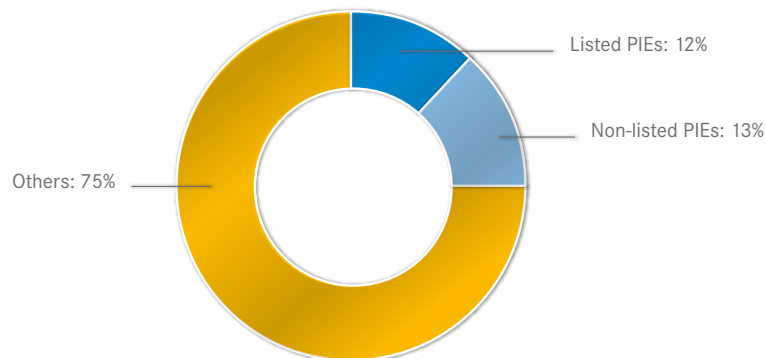
2.2. Activity programme for 2013

The CSSF set down a multiannual programme for the control of *cabinets de révision agréés/réviseurs d'entreprises agréés* which aims at observing the legal quality assurance review cycle, this cycle being three years for firms that audit PIEs and six years for the other ones. This programme was based on the information transmitted by audit firms and *réviseurs* through the "Annual Annexes" relating to their activity.

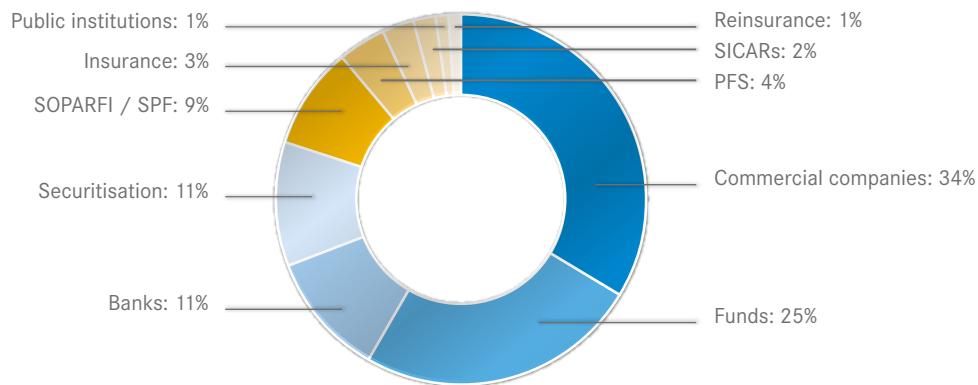
Activity programme for 2013	Key data
<p>The quality assurance reviews according to the 2013 programme covered:</p> <ul style="list-style-type: none"> - the understanding and documentation of the organisation, policies and procedures established by the reviewed firms in order to assess compliance with the requirements of the International Standard on Quality Control (ISQC 1); - the review of a sample of audit files relating to statutory audit assignments of the financial year 2012 (or 2011, where applicable); - the review of a sample of audit files carried out in the framework of the assignments reserved by the Audit Law to the <i>réviseurs d'entreprises agréés</i> and <i>cabinets de révision agréés</i>; and - the setting-up of a specific follow-up for professionals for which material weaknesses were noted in the previous financial year. 	19 reviewed firms, 6 of which audit PIEs and 11 are members of an international network
<p>The 19 reviewed audit firms reported³ a total of 9,257 mandates falling within the scope of public oversight of the CSSF, including 412 in relation to PIEs. These mandates include 8,193 statutory audits, of which 393 concern PIEs.</p>	211 controlled mandates, including 53 PIEs
<p>The quality assurance reviews started in April 2013 and were carried out by seven CSSF inspectors with professional audit experience and expert knowledge in the business areas of the financial centre.</p>	6,032 hours

³ Based on the statements of *cabinets de révision agréés* (Annual Annexes) as at 31 December 2012.

Breakdown of audit files reviewed by the CSSF in 2013 per entity type



Breakdown of audit files reviewed by the CSSF in 2013 per sector



2.3. Conclusions of the 2013 campaign of quality assurance reviews

Among the 19 firms reviewed in 2013, five were subject to a specific follow-up due to conclusions from preceding campaigns. The specific follow-up was maintained for three of these firms due to material shortcomings in the ISA 600 “Special considerations - audits of group financial statements (including the work of component auditors)”.

Six *réviseurs d’entreprises agréés* were subject to a specific follow-up in 2013, two of them being subject to the double signature measure. Following the observations made, the specific follow-up is upheld for two of the six *réviseurs d’entreprises agréés* concerned and the double signature measure is upheld for one *réviseur d’entreprises agréé*.

For the 2013 campaign, the following specific conclusions were transmitted to the *réviseurs d’entreprises agréés*:

- a training plan was given to seven *réviseurs d’entreprises agréés*;
- one *réviseur d’entreprises agréé* had to have his/her files internally reviewed by a second partner before the issue of the opinion together with a specific follow-up;
- six *réviseurs d’entreprises agréés* were subject to the double signature measure together with a specific follow-up.

The CSSF ordered a firm to leave four of its mandates due to non-compliance with the independence rules. Another firm was called to order and ordered to remedy the self-review situation.

The CSSF imposed a fine on one *réviseur d’entreprises agréé* for significant breach of the standards governing the audit profession.

2.4. Major issues identified during the quality assurance reviews of 2013

2.4.1. International Standard on Quality Control (ISQC 1)

The quality control systems of the overseen *cabinets de révision agréés* are mostly compliant with the provisions of the ISQC 1. Nevertheless, the CSSF noted some deficiencies in the procedures for accepting and continuing client relationships and specific assignments. The CSSF insists on the fact that these diligences be carried out sensibly and rigorously and that they be always finalised prior to any assignments, even if it is recurring.

Progress must also be made as regards the identification of the files which have to be submitted to a quality control review as well as the extent of the diligences to be carried out by the persons in charge of the quality control reviews of these assignments.

2.4.2. Audit files

During its controls, the CSSF noted that some auditors used information without first assessing whether it is sufficiently reliable and conclusive to address the needs of the audit. For these purposes, the CSSF reminds that the reliability of the information to be used as evidence is influenced by its source and nature as well as by the circumstances in which it was gathered, including by the controls carried out on its preparation and follow-up. As regards evidence produced internally, its reliability is notably increased when the internal controls mentioned above are efficient. This observation is made very often for evidence gathered in relation to the assertion “valuation” of the financial instruments. On this point and in order to continue to improve the quality of audits which face these problems, the CSSF encourages the auditors to take into account the guidelines of the International Auditing Practice Note 1000 “Special Considerations in Auditing Financial Instruments (IAPN 1000)” and of the technical note 2013-04 of the IRE “Additional guidelines in relation to the valuation of specific assets/instruments”.

When identifying and assessing risks of material misstatements due to fraud, the auditor must, based on the presumption that there are risks of fraud in the revenue recognition, assess which revenues, operations or assertions relating to revenues may cause such risks. The CSSF observed a trend of minimising or even ignoring the fraud risks so as to not implement the complementary audit procedures whose nature, timing and extent specifically address these risks at the level of the assertions concerned. Finally, where fraud in the revenue recognition is not considered as a risk of significant misstatement, the CSSF reiterates that appropriate evidence must be documented in the audit file.

Shortcomings continued to be noted during the tests of the procedures aiming to check the efficient functioning of the internal controls relevant to the audit. The identified errors come from, among others:

- the non-identification of the measures of relevant internal control addressing a risk of material misstatements at the assertion level;
- the inappropriate conception of implemented tests which do not allow the collection of evidence on (i) the manner in which the controls were carried out at relevant moments during the audit period, (ii) the continuity with which they were applied or (iii) by whom or how they were carried out. When the procedure tests were carried out at an intermediary period, the CSSF draws the attention, in particular, to the necessity to inquire about the significant changes which appeared after the intermediary period and to define supplementary evidence to be collected for the remaining period;
- the non-implementation of verifications of internal controls addressing the risks related to the transaction flows managed in an entirely computerised environment, particularly when the documentation of the transactions is not materialised or kept otherwise than in the IT system.

The CSSF also noted frequent shortcomings concerning the audit of long-term contracts. Based on the control files reviewed, the main weaknesses encountered concerned: (i) the lack of critical thinking skills and of analysis of the compliance with the conditions and the reliability of the data which are needed to recognise the revenues according to completion method and (ii) insufficient audit works carried out on the percentage of completion of the projects and on the identification and right evaluation of possible losses at completion.

The CSSF identified shortcomings as regards substantive analytical procedures. In that respect, the CSSF reminds that these procedures are generally more adapted to significant volumes of transactions the trend of

which is foreseeable and insists on the fact that these procedures must be implemented in compliance with the objectives and rules described in ISA 520.

For that purpose, the auditor must among others:

- assess the reliability of data on which the auditor's expectation is based;
- develop an expectation of recorded amounts or ratios and evaluate whether the expectation is sufficiently precise to identify a misstatement that, individually or when aggregated with other misstatements, may cause the financial statements to be materially misstated; and
- determine the amount of any difference of recorded amounts from expected values that is acceptable without further investigation.

In 2013, the CSSF continued its controls of audits of groups whose decision-making and administrative centre is abroad. It noted shortcomings similar to those identified in 2012, such as:

- an insufficient involvement of the auditor responsible for the group audit in the work of the other auditor established in the country from where the group steers its operations, and
- a review of the works of other auditors which is too superficial, a posteriori and insufficiently documented.

The most serious shortcomings in these assignments were observed when the Luxembourg audit team and that from the country from where the group steers the operations did not constitute an integrated audit team, i.e. a team led and supervised by the partner in charge of the audit group and using a common work space accessible to all the members of the team appointed for the audit of the group.

In such an environment, the CSSF noted that the auditors gathered a posteriori brief information from the component auditors and did not play an active role during the whole mission, in accordance with the requirements of ISA 600 "Special considerations - Audits of group financial statements (including the work of component auditors)". In order to be able to accept such assignments, the CSSF reminds that this standard requires from the partner responsible for the group audit that s/he defines if sufficient and appropriate evidence in relation to the consolidation process and financial information of components may be properly collected. The CSSF will maintain its vigilance as regards the quality of these missions in 2014.

The CSSF regularly noted shortcomings in the documentation of material professional judgments carried out during the audit and reminds that the professional judgment cannot be used as justification for the decisions taken which are not supported by facts and circumstances of the mission or by sufficient and appropriate conclusive elements.

The CSSF specifies that the items mentioned above were noted in big as well as in small audit firms.

2.4.3. Theme of the 2013 campaign

In the framework of its activity programme, the CSSF carried out a thematic review regarding the provision of non-audit services to audit clients. This examination focussed on the following items:

- the compliance, for the controlled assignments, with the standards on ethics and on internal quality control applicable in Luxembourg;
- the quality of the diligences carried out aiming to identify and document the threats to the independence of the firm or the members of the audit team that may arise due to these assignments;
- the efficiency of the safeguards implemented in order to clear or reduce to an acceptable level the identified threats;
- the quality of the information gathered during the acceptance of these assignments;
- the validation of the acceptance procedures before the start of the works;
- the communication to the partner responsible for the audit of the useful information in order to allow him/her to identify and assess the circumstances which threaten the independence of the firm or of its team;
- the possible consultations carried out at the "risk management" or "independence" unit when the provision of non-audit services are critical or unusual;

- the adequacy of the assessment of the non-audit services to be performed during the acceptance of the assignment and the adequacy of the description in the engagement letter of the service to be performed with the service actually provided;
- the appropriateness of the notes to the accounts reporting the fees of the *réviseurs d'entreprises agréés* per type of assignment;
- the required communications to the persons in charge of the corporate governance in order to carry out these engagements.

The CSSF insists on the essential importance for audit firms to ensure full compliance with the independence principles laid down in the Code of ethics for the audit profession in fact as well as in appearance.

Out of the 79 non-audit services that were subject to the CSSF's thematic review, the following items were noted:

- one assignment was performed without carrying out the acceptance procedures of the firm;
- 18 assignments started before the acceptance procedures were finalised and validated by the partner in charge;
- as regards 11 forms for the acceptance of non-audit services, the collected information was insufficient and not precise enough, which did not allow the proper identification of the threats to the independence caused by the specificities of the envisaged service provision;
- as regards three services, the safeguards envisaged by the professionals were not observed;
- as regards eight services, the partner in charge of the audit was not informed *ex ante* of the non-audit services which will be provided to his/her client; thus s/he was not able to identify and assess the circumstances which might threaten his/her independence;
- one service consisted of drawing up internal procedures for a management company: during the acceptance of this mandate, the professionals could not sufficiently prove that a member of the management was indeed in charge of making important judgments and taking significant decisions related to the design and implementation of the internal control;
- one service consisted of the analysis and definition of the risk management process for a specialised investment fund (SIF): during the acceptance of this mandate, the professionals could not sufficiently prove the involvement of the management of the SIF in the process and did not assess the threat related to the self-review generated by this provision due to the fact that the information drawn up based on advice was laid down in the notes to the annual accounts of the SIF drawn up under the IFRS. The CSSF considered that no safeguards were likely to reduce the independence threats to an acceptable level.

3. OVERVIEW OF THE POPULATION OF *RÉVISEURS D'ENTREPRISES* (STATUTORY AUDITORS) IN LUXEMBOURG

Within the scope of its public oversight of the audit profession, the CSSF assumes the following responsibilities:

- access to the profession and organisation of the examination of professional competence;
- granting the professional title of *réviseur d'entreprises* and *cabinet de révision*;
- granting the approval and registration of *réviseurs d'entreprises agréés* and *cabinets de révision agréés*;
- registration of third-country auditors and third-country audit entities; and
- keeping of the public register.

In this regard, the following statistics have been extracted for the year 2013.

3.1. Access to the profession

3.1.1. Activities of the Consultative Commission for the access to the audit profession

The Consultative Commission's task is, among others, to verify the theoretical and professional qualification of the candidates for the access to the audit profession in Luxembourg, as well as that of the service providers from other Member States wishing to exercise by way of free provision of services.

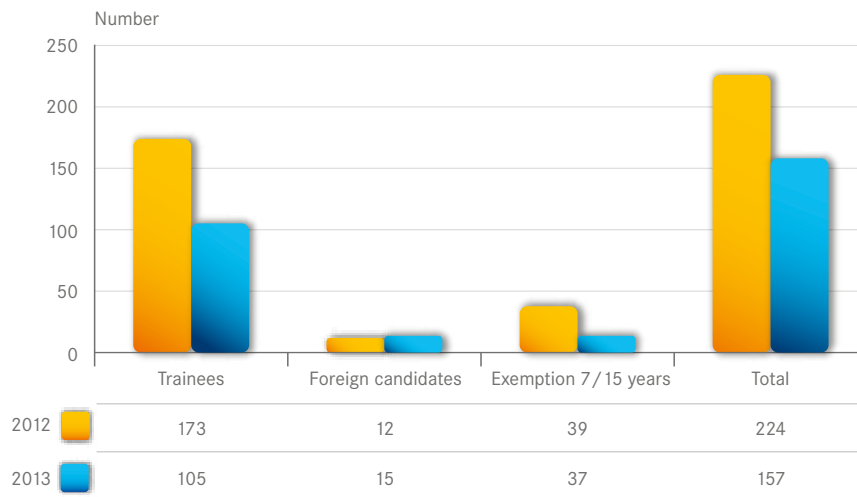
The commission met seven times in 2013 and analysed the files of 157 candidates, against 224 in 2012, representing a drop of 30%. This significant drop follows the entry into force of the Grand-ducal Regulation of 9 July 2013 determining the requirements for the professional qualification of *réviseurs d'entreprises* (statutory auditors) (cf. item 1.2.1. above) which introduced more strict measures for the admission to professional training.

Consequently, the access to training was refused to 37 candidates (23.6%) between September 2013 and December 2013 because the number of subjects to be completed based on their administrative certificate was greater than five.

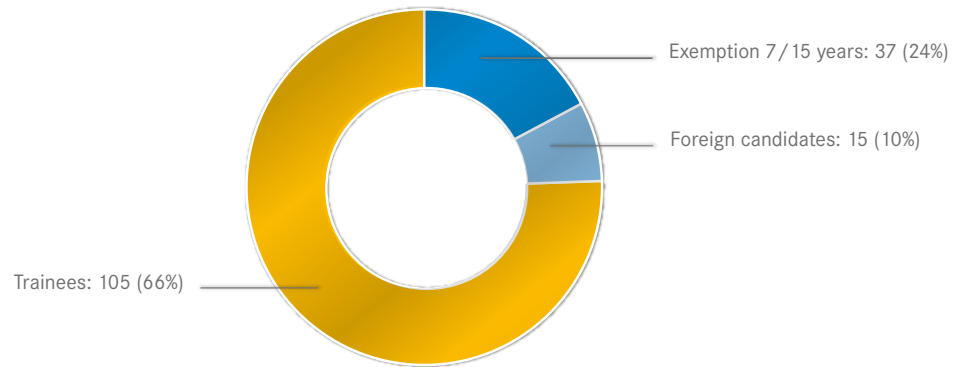
There are four categories of candidates:

- trainee *réviseurs d'entreprises*;
- foreign candidates;
- candidates applying for exemptions based on their professional experience of either seven or fifteen years; and
- candidates requesting to exercise assignments reserved by the law to *réviseurs d'entreprises agréés* and *cabinets de révision agréés*, by way of the free provision of services (no such file was analysed in 2013).

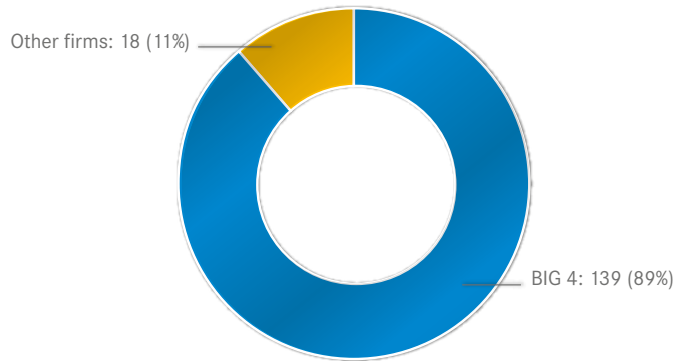
Development in the number of application files submitted to the Consultative Commission



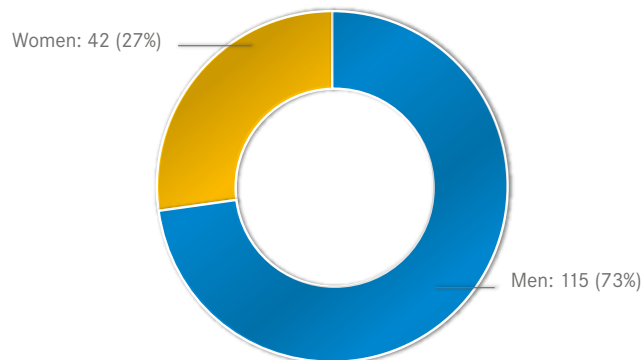
Breakdown of candidates per category



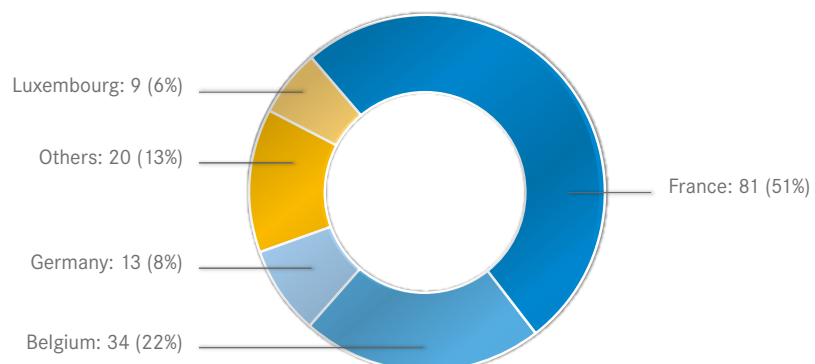
Breakdown of candidates per firm



Breakdown of candidates per gender



Breakdown of candidates per nationality



3.1.2. Examination of professional competence in 2013

The CSSF administers the examination of professional competence in accordance with Articles 5 and 6 of the Grand-ducal Regulation of 9 July 2013 determining the requirements for the professional qualification of *réviseurs d'entreprises* (statutory auditors).

In this context, the examination jury communicated the following results with respect to the 2013 examination of professional competence to the CSSF:

- Out of the 50 registered candidates, two candidates withdrew their candidature at the beginning of the procedure.
- Ordinary session: 48 candidates took the written exam, 25 of whom have been admitted to the oral exam. In total, 18 candidates passed the exam, seven failed partially (possibility to take the extraordinary session).
- Extraordinary session: seven candidates took the written exam, one of whom was admitted to the oral exam. In total, no one passed the exam of the extraordinary session.

Thus, all sessions included, 18 candidates passed the examination of professional competence in 2013 successfully.

Having passed this examination, candidates may request the CSSF to be granted the title of *réviseur d'entreprises*.

The graduation ceremony was held on 6 March 2014 in the presence of the Minister of Finance Mr Pierre Gramegna.

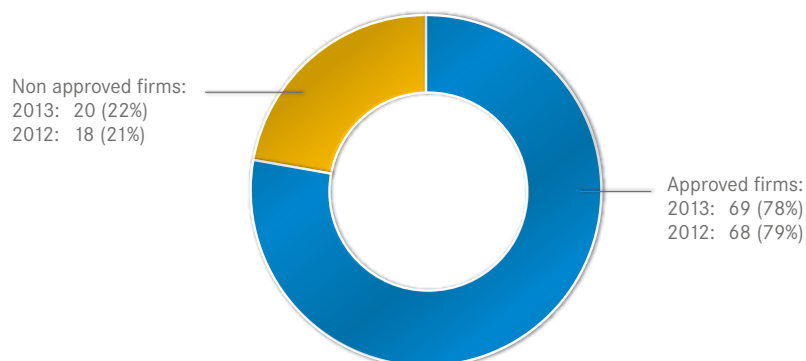
3.2. Public register

The public register of *réviseurs d'entreprises agréés*, *cabinets de révision agréés* and third-country auditors and audit entities is available on the CSSF's website in the section "Public oversight of the audit profession", sub-section "Public register".

3.2.1. National population as at 31 December 2013

• Development in the number of *cabinets de révision* and *cabinets de révision agréés*

The total number of *cabinets de révision* and *cabinets de révision agréés* amounted to 89 as at 31 December 2013 against 86 as at 31 December 2012, i.e. a 3.5% increase.



The following firms were approved in 2013:

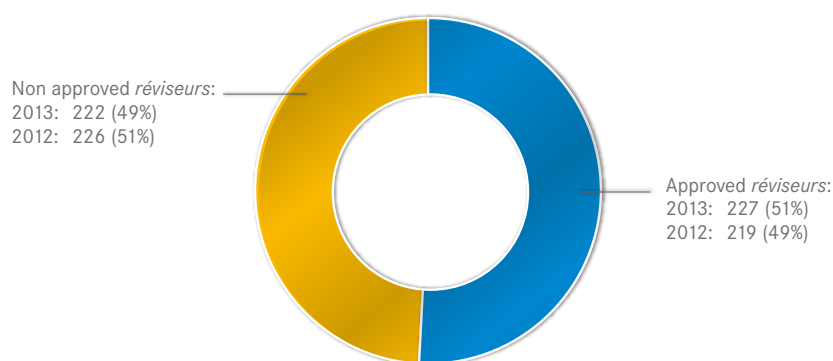
- VPC Luxembourg
- INSCOPE S.à r.l.
- CLERC Luxembourg S.A.

- AUDIT AND TRUST SERVICES S.à r.l.
- PRO FIDUCIAIRE Auditing & Accounting S.à r.l.
- LUXEMBOURGEOISE D'AUDIT ET DE RÉVISION S.à r.l. (in abbreviated form "Flux-Audit")
- FIDUCIA AUDIT S.à r.l.
- AUMEA PARTNER S.à r.l.

In 2013, seven firms gave up their approval, two of which have also abandoned the title of *cabinet de révision*.

• **Development in the number of *réviseurs d'entreprises* and *réviseurs d'entreprises agréés***

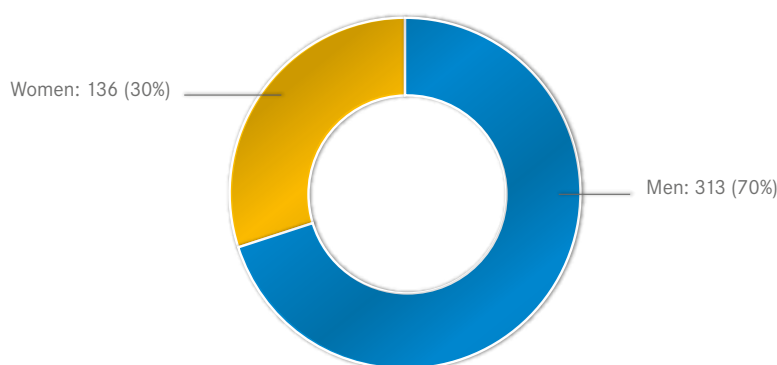
The total number of *réviseurs d'entreprises* and *réviseurs d'entreprises agréés* amounted to 449 as at 31 December 2013 against 445 as at 31 December 2012, which is a 0.9% increase.



In 2013, the CSSF granted the title of *réviseur d'entreprises* to 14 persons and approved 18 *réviseurs d'entreprises agréés*.

During the year under review, 10 *réviseurs d'entreprises agréés* gave up their approval, including four that also gave up their title.

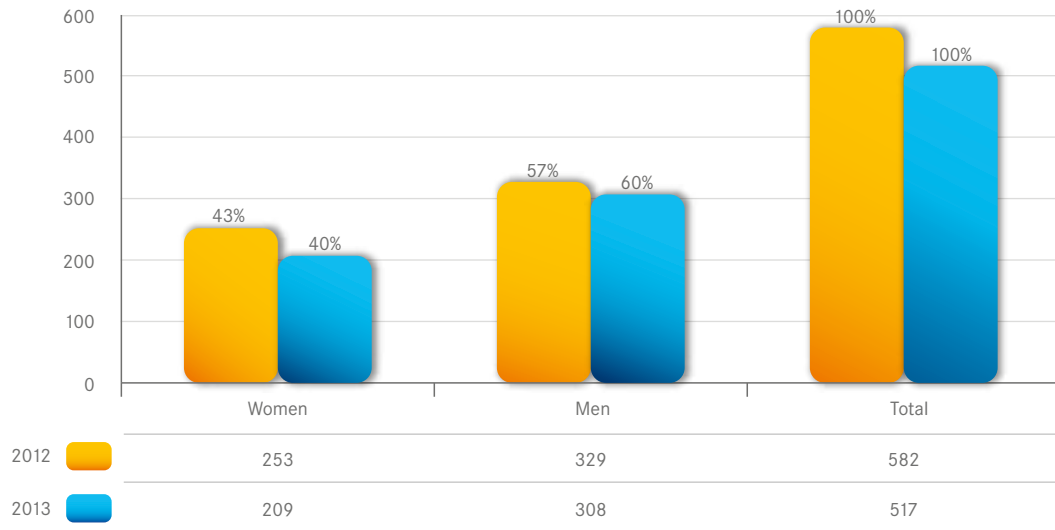
• **Breakdown of *réviseurs* according to gender**



The average age of *réviseurs* is 40.1 years for women and 45.3 years for men.

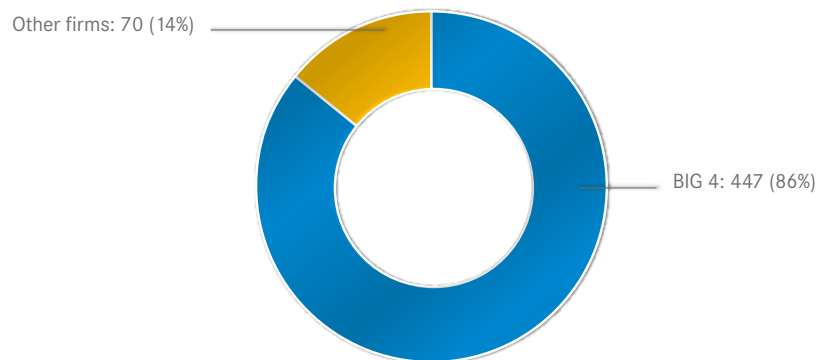
• **Development in the number of trainee *réviseurs d'entreprises***

The total number of trainee *réviseurs d'entreprises* amounted to 517 as at 31 December 2013, against 582 as at 31 December 2012, which is an 11.2% decrease.

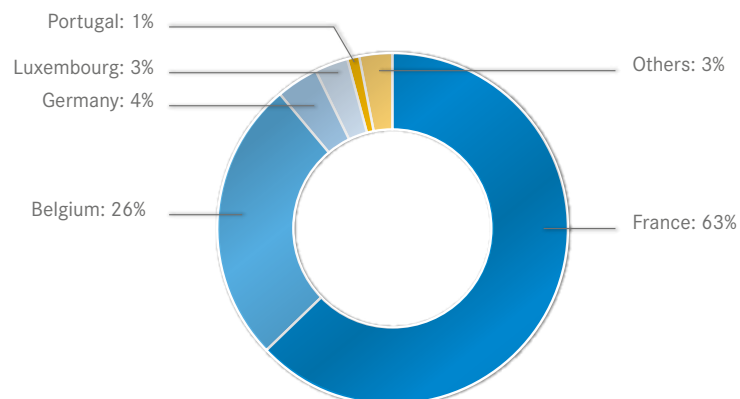


The average age of trainees is 29.6 years for women and 29.8 years for men.

• **Breakdown of trainees per firm**



• **Breakdown of trainees per nationality**



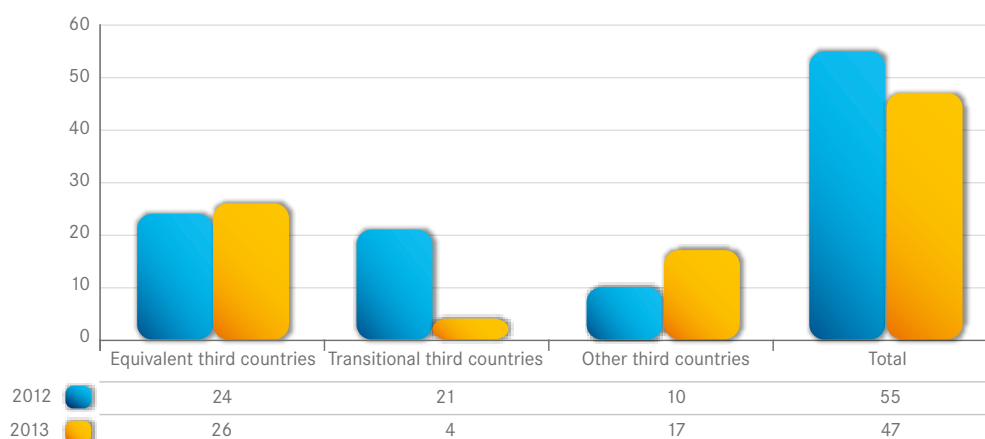
3.2.2. Third-country auditors and audit firms

The registration procedure for third-country auditors and audit firms that provide an auditor’s report on the annual or consolidated accounts of a company incorporated outside EU Member States, whose securities are admitted to trading on the regulated market of the Luxembourg Stock Exchange (“third-country auditors”) continued in 2013.

Thus, the CSSF received two new applications for registration from auditors located in third countries which have public oversight, quality assurance, investigation and penalty systems which are considered as equivalent to the systems in the EU (“equivalent third countries”). These two files resulted in a registration.

Moreover, except for the 10 third-country auditors whose activities did not fall any more within the scope of Directive 2006/43/EC, all the third-country auditors previously registered have renewed their registration.

The public register of all the third-country auditors registered by the CSSF (47 auditors as at 31 December 2013, including 26 from equivalent third countries, four from transitional third countries within the meaning of Commission Implementing Decision 2013/288/EU of 13 June 2013 and 17 from other third countries) is available on the CSSF’s website.



4. COOPERATION AGREEMENTS

The cooperation between the European supervisory authorities and those from third countries is laid down in Article 47 of Directive 2006/43/EC on statutory audits of annual accounts and consolidated accounts. This directive provides, among others, the possibility, under certain conditions, for Member States to allow the transfer to the competent authorities of a third country of audit documents or other documents held by statutory auditors or audit firms. These conditions include the requirement to sign an agreement between the competent authority of a Member State and the competent authority of a third country.

Following the European Commission decisions of 5 February 2010 and 19 January 2011 which recognise the adequacy of the competent authorities and the equivalence of the public oversight of Japan and Switzerland, the CSSF signed cooperation agreements with its Japanese and Swiss counterparts. Thus, on 2 August 2013, the CSSF exchanged letters with the Financial Services Agency (FSA) and the Certified Public Accountants and Auditing Oversight Board (CPA/OB) of Japan which also include a commitment regarding the protection of personal data. On 26 September 2013, the CSSF signed a cooperative agreement with the Swiss Federal Audit Oversight Authority (FAOA). These bilateral agreements are available on the CSSF’s website.

In addition, following the European Commission decisions of 11 June 2013 on adequacy and equivalence, the CSSF continued its negotiations with its American counterparts in order to sign a bilateral cooperative agreement. In order to reach a target of mutual recognition of the two parties' oversight systems, the negotiations also concerned joint controls in Luxembourg and the United States of audit firms subject to the oversight of both authorities.

The cooperation agreement will be accompanied by a specific agreement which will guarantee compliance with national regulations on the protection of personal data. This specific agreement was subject to prior authorisation by the national commission for data protection (Commission nationale pour la protection des données; CNPD)

5. PRACTICE OF PUBLIC OVERSIGHT OF THE AUDIT PROFESSION

Circular CSSF 02/77 introduced, for Luxembourg UCIs, the concept of materiality and set, at the same time, the tolerance threshold to different levels depending on the types of UCIs. In parallel, the concept of materiality thresholds is crucial for the financial audit since it influences directly the amount from which an anomaly will require an adjustment of the financial statements but also the nature, the timing and extent of the audit works to be undertaken. The CSSF considers that it would not be relevant and that it might be deceiving for the users of annual accounts that the concept of material anomalies to which reference is made in the audit opinion be different from the materiality applicable in the framework of the treatment of NAV calculation errors.

Pursuant to Circular CSSF 02/81, the *réviseur d'entreprises* must indicate the NAV calculation errors noted during his/her control and which were not reported to the CSSF in accordance with the provisions of Circular CSSF 02/77. In the event the *réviseur d'entreprises* uses a different materiality threshold for the audit of annual accounts, s/he will not be able to comply with this requirement. Furthermore, the audited annual accounts are an important instrument of the prudential supervision. In this regard, the CSSF considers that the *réviseurs d'entreprises* must adopt a harmonised approach relating to the determination of the materiality thresholds for funds with similar characteristics.

In this context, the CSSF requests that the materiality thresholds for the audit of annual accounts of Luxembourg UCIs be set at the same level as the thresholds laid down pursuant to Circular CSSF 02/77.



Agents hired in 2013 and 2014: Departments “Prudential supervision, risk management and database operation”, “International, regulation and enforcement” and “Authorisation and supervision of UCI management companies”

Left to right: Vicky ELSÉN, Jennifer BURR, Laurence BEREND, Marie LICHTEROWICZ, Cédric LASSELOT, Julie LEBESGUE, Michel STEICHEN, Sandra PELET, Chris DIEDERICH, Daniela KOHN, Karine ARENDT-HYARDIN, Pierre TROVATO



Agents hired in 2013 and 2014: Departments “Authorisation and supervision of AIFMs, AIFs, SIFs and SICARs not qualified as AIFs” and “Authorisation and supervision of UCITS”

Left to right: François CALTEUX, Magali RENNOIR, Paul HENDEL, Simon EMERI, Aurélie FLAMANT, Volker SAUER, Claudie FLAMAND, Céline CAM, Sophie HOARAU, Tobias SCHELL, Jacques HEMMER

CHAPTER XIII

INSTRUMENTS OF SUPERVISION

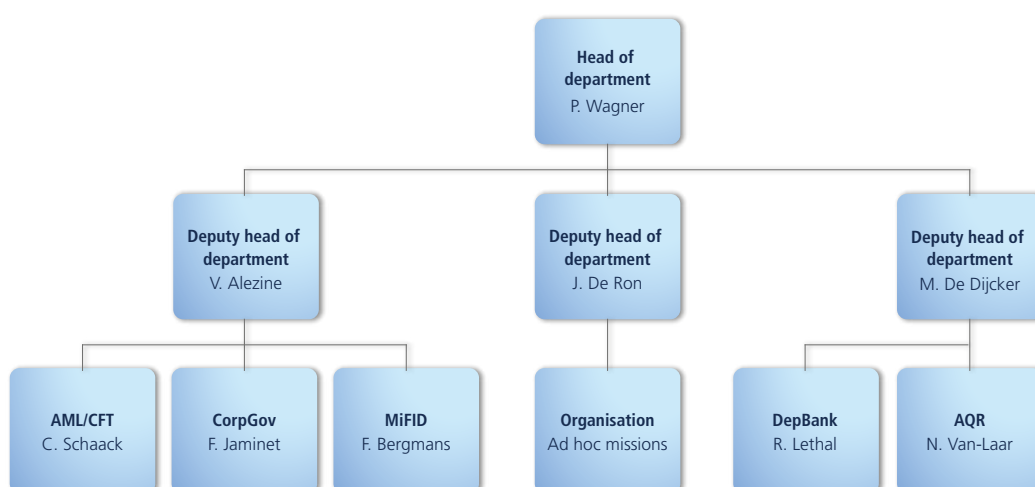


1. On-site inspections
2. Means of administrative police

1. ON-SITE INSPECTIONS

As a result of the significant increase, in 2013, in the number of staff of Division 4 of the “General Supervision” department in charge of on-site inspections, the Executive Board of the CSSF decided, at the beginning of 2014, to create a new department called “On-site Inspection”. This department is now in charge of planning and coordinating all on-site inspections carried out by the CSSF in banks, UCIs and SICARs as well as their management companies, investment firms, specialised PFS, support PFS, pension funds, securitisation undertakings and financial market participants. It carries out on-site inspections itself, notably missions relating to “Anti-money laundering and counter-terrorist financing” (AML/CFT), “Corporate governance”, “Depository bank function”, “Asset quality review” and “MiFID”.

The organisation chart of the “On-site Inspection” department is as follows:



The teams responsible for on-site inspections are formed according to the nature, scale and scope of the missions and involve the participation of agents from the supervisory departments as well as from the “On-site Inspection” department.

After each on-site inspection, the team in charge of the mission draws up an internal report indicating any flaws and weaknesses identified during the mission. Generally, all on-site inspections are followed by observation letters¹ sent to the controlled professional. In the event of more serious flaws, the CSSF analyses whether there is a need for an injunction procedure or a non-litigious administrative procedure in order to impose an administrative sanction pursuant to Article 63 of the law of 5 April 1993 on the financial sector.

In 2013, the CSSF carried out a total of 152 on-site visits and inspections that concerned, in particular, the topics set out below.

1.1. Introductory visits

Introductory visits are aimed at new players of the financial centre that received their authorisation recently. Usually carried out within the first six months following the professional’s authorisation, the purpose of these missions is to follow the newly set up professionals in the start-up phase of their activities.

Introductory visits usually take the form of management interviews and allow an assessment of the professional’s compliance with the provisions laid down in the law of 5 April 1993 on the financial sector and in other sectoral laws, as well as with professional obligations, particularly in terms of organisation. They also allow the CSSF to understand the professional’s organisation and activities and to check whether the development of the activities and the strategies correspond to the forecasts set out in the application file.

During the year under review, the CSSF undertook 25 introductory visits of new players of the financial centre.

¹ There are some rare cases of non-observation letters.

Breakdown of the introductory visits by type of entity

Type of entity controlled	Introductory visits
Banks	4
Payment institutions	1
Investment firms	5
Specialised PFS	7
Support PFS	8
Total	25

The introductory visits revealed, in some cases, weaknesses relating to the organisation of the day-to-day management, relating to the consistency of the entities' activities with the scope of authorisation or relating to their procedures.

1.2. Ad hoc control missions

Ad hoc control missions are on-site inspections intended to investigate a specific or even worrying situation/problem related to the professional itself. The particular situation/problem has, in principle, already been observed during the off-site prudential supervision. Such missions may either be planned in advance or occur unexpectedly. The nature and scale of ad hoc missions may vary significantly and will subsequently determine the composition of the on-site teams.

In 2013, the CSSF carried out 32 ad hoc missions. Some of these missions were very large in scope and required the use of significant human resources.

Breakdown of the ad hoc control missions by type of entity

Type of entity controlled	Ad hoc on-site inspections
Banks	16
Electronic money institutions	1
UCIs	4
Management companies	1
Investment firms	2
Specialised PFS	3
Pension funds	1
Securitisation undertakings	2
Financial markets	2
Total	32

The ad hoc missions performed within banks concerned different topics such as contracts for difference, the business model or the recovery plan. These missions were aimed at identifying specific situations of supervised entities. One ad hoc mission within a bank was in relation with another ad hoc mission within an investment firm.

The ad hoc missions within UCIs and management companies concerned, in particular, the risk management procedures in place.

The two ad hoc missions within investment firms concerned various topics. Given the relatively broad scope of these missions, the CSSF has not yet drawn its final conclusions.

With respect to two missions carried out within specialised PFS, the analysis of the files is being finalised and a letter reminding of the applicable legal provisions will be sent to the two relevant entities shortly. One mission that had started at the end of 2013 was continued in 2014.

With regard to pension funds, the CSSF carried out an on-site inspection of a service provider engaging in central administration and domiciliation agent activities for one pension fund. The purpose was to assess the pension fund's administrative and accounting organisation.

As regards authorised securitisation undertakings, the CSSF carried out an on-site inspection within an authorised securitisation undertaking as well as a service provider acting as administrative agent for seven authorised securitisation undertakings. The purpose of the two missions was to assess the administrative and accounting organisation.

The missions regarding the supervision of financial markets concerned enforcement reviews of the financial statements of two entities subject to the prudential supervision of the CSSF.

1.3. “Liquidity” control missions

The “Liquidity” on-site inspections were carried out together with the Banque centrale du Luxembourg (BCL). These inspections were aimed at assessing the situation and management of the liquidity risk of credit institutions.

In 2013, the CSSF carried out seven on-site inspections in this field².

1.4. “Interest rate risk” control missions

“Interest rate risk” or “Interest rate risk in the banking book (IRRBB)” controls aim to assess the interest rate risk arising from non-trading activities and the results of stress tests.

In 2013, the CSSF carried out two “Interest rate risk” on-site inspections.

1.5. “Validation of credit risk management and operational risk management models” on-site inspections

In 2013, the CSSF carried out one inspection as regards a credit risk management model.

The operational risk inspections covered specific aspects of the risk management of credit institutions that apply the advanced measurement approach (AMA) or the standardised approach (TSA)³. In 2013, the CSSF carried out a total of five on-site inspections in this matter, four of which concerned the advanced approach and one the standardised approach.

1.6. “Credits” on-site inspections

The purpose of “Credits” on-site inspections is to verify the sound and prudent credit management within banks of the financial centre. The processes relating to the granting and monitoring of credits and the acceptance and monitoring of guarantees are analysed on the basis of samples. The different internal reports relating to these processes are also reviewed during those missions.

Following the entry into force of Circular CSSF 12/552, the CSSF focuses on the credit risk principles which are set out in Part III thereof and verifies that they are complied with in practice.

In 2013, the CSSF carried out “Credits” missions in seven banks of the financial centre. These missions, that concerned subjects such as real estate development, lombard loans and corporate banking loans, led to a better view of the credit risk incurred by these professionals.

A certain number of flaws were highlighted, the most important of which concerned, in particular, the quality of the information available within the internal systems, the grouping of connected counterparties, the quality of the guarantees accepted, the content of the internal reports and the update of the procedures manual.

1.7. “Corporate governance” on-site inspections

“Corporate governance” on-site inspections aim to analyse the quality of the governance arrangements set up by professionals pursuant to the regulatory requirements. An on-site inspection may target the governance

² See also item 2.4. of Chapter IV “Supervision of the banking sector”.

³ See also item 2.6. of Chapter IV “Supervision of the banking sector”.

of a Luxembourg entity, the group head function exercised by a Luxembourg entity or the organisation and effectiveness of the internal control functions of an entity as well as the implementation of a new governance model as a result of the reorganisation of a banking group.

In 2013, the CSSF carried out 20 “Corporate governance” on-site inspections in banks and management companies subject to Chapter 15 of the law of 17 December 2010.

Breakdown of the “Corporate governance” control missions by type of entity

Type of entity controlled	“Corporate governance” on-site inspections
Banks	18
Management companies	2
Total	20

Recurrent flaws were noted especially as regards internal audit and compliance. Indeed, the CSSF noted that:

- the long-term audit plans did not always cover all activities and areas within a reasonable timeframe;
- the compliance risk identification was not based on a structured methodology;
- the information transmitted to the board of directors was not comprehensive enough and/or not sufficiently clear for an overall and complete view of the manner in which the authorised management implements the required corrective measures to address the shortcomings identified by the internal control functions;
- as regards entities with a group head function, the transmission of the shortcomings identified throughout the group to the authorised management and the board of directors was not properly performed by the internal control functions.

In some cases, the CSSF noted that the members of the authorised management did not have a veto in their capacity as members of the management committees which are larger than the sole authorised management. In other cases, the CSSF had to reiterate the importance of the principle of segregation of duties between the members of the authorised management in order to avoid any possible conflict of interests.

In two cases, the CSSF decided to initiate an injunction procedure pursuant to Article 59 of the law of 5 April 1993 on the financial sector and a non-litigious administrative procedure, respectively, in order to impose an administrative sanction pursuant to Article 63 of the law due to significant flaws identified in the internal audit function.

1.8. “MiFID” on-site inspections

In 2013, the CSSF carried out three on-site inspections regarding the MiFID rules of conduct, including two in banks and one in an investment firm.

For two inspected entities, it was found that their terms and conditions gave insufficient information on benefits and were drafted in a mostly incomprehensible manner for the average investor.

The two entities established suitability test arrangements that did not enable to clearly determine the financial instruments that were actually suitable for customers.

One credit institution issuing structured products and subsequently organising the secondary market for these structured products did not identify the conflicts of interests that arose from that activity. Controls on the price of the structured products offered to customers as regards their fair value were lacking. Moreover, the bank had to implement measures aiming to avoid that completely illiquid structured products presented for redemption by certain customers were offered by the bank to other customers because it did not want to take risks by acquiring these products for its own account.

One mission was carried out in a bank together with the German prudential supervisory authorities.

An administrative fine of EUR 10,000 was imposed on an investment firm that refused to communicate the results of the suitability test to its current and potential customers. In this case, the customer should at least have been informed of the appropriate asset allocation as a result of the suitability test.

1.9. “Depository bank” on-site inspections

During 2013, the CSSF carried out 12 on-site inspections regarding the “Depository bank” function.

Eight missions were aimed at understanding the general organisation of the activities exercised by the relevant depository banks. During these inspections, the CSSF reviewed the depository bank’s process of acceptance of new assignments, the procedures in place to guarantee the custody of the different types of assets as well as the specific supervisory and monitoring duties.

The other four missions exclusively concerned the asset-custody function. During these inspections, the CSSF more specifically analysed the selection and supervision process of the sub-custodians and third-party custodians involved in the custody of the different types of assets and reviewed a sample of files in this regard. It also carried out tests in order to verify how depository banks ensure that they are, at any time, aware of how assets of UCIs are invested and where and how these assets are available.

The CSSF noted that the banks are reorganising their depository bank activities under the impetus of the new requirements due to the transposition of the AIFMD. Consequently, most of them have already started remedying certain flaws identified within the scope of the CSSF’s control missions, as regards the supervision of sub-custodians and/or third-party custodians or as regards the formalization of the process of acceptance of new assignments.

1.10. “Anti-money laundering and counter-terrorist financing” (AML/CFT) on-site inspections

“AML/CFT” on-site inspections of all players of the financial centre are carried out in order to assess the quality of the AML/CFT framework implemented with respect to the legal and regulatory requirements. The controls cover both private banking business (portfolio management, domiciliation, etc.) and registrar agent activities.

In 2013, the CSSF carried out 38 “AML/CFT” on-site missions⁴ broken down by type of entity as set out below.

The AML/CFT team also carried out five ad hoc missions dealing largely with AML/CFT issues. These missions are included in the ad hoc missions listed in item 1.2. above.

Breakdown of the “AML/CFT” on-site missions by type of entity

Type of entity controlled	“AML/CFT” on-site inspections
Banks	8
Investment firms	11
Specialised PFS	17
SICARs	1
UCIs	1
Ad hoc	5
Total	43

In 2013, a significant number of on-site inspections were carried out in investment firms and specialised PFS. In 2014, special emphasis will be put on on-site inspections in banks.

The most significant flaws that were identified during “AML/CFT” on-site missions in 2013, be it as a result of their frequency or their seriousness, were the following: lack of documentation and/or difficulties in obtaining information relating to the origin of the funds, insufficient documentation in relation to the verification of the identity of legal persons and beneficial owners, absence of controls allowing to determine whether a customer, beneficial owner or representative became a politically exposed person during the business relationship, absence of verification of permanent compliance with the conditions for the application of simplified customer due diligence measures during the business relationship, lack of name matching checks as regards the official lists (non-exhaustiveness of the controlled lists, absence of controls at the publication of official lists, lack of formalization) and insufficient involvement of the compliance officer in the supervision of transactions.

⁴ Among which five follow-up missions of previous “AML/CFT” missions.

In 2013, the CSSF decided, within the context of 12 on-site inspections⁵, to initiate an injunction procedure pursuant to Article 59 of the law of 5 April 1993 on the financial sector or a non-litigious administrative procedure in order to impose an administrative sanction pursuant to Article 63 of the aforementioned law. In six cases⁶, this procedure led the CSSF to impose an administrative fine and, in one case, a reprimand was given to a manager⁷.

For two files being processed, the above-mentioned procedure is still likely to be initiated.

In five cases, the CSSF transmitted a suspicious transaction report pursuant to Articles 23(2) and/or 23(3) of the Code of Criminal Procedure or a notification to the Financial Intelligence Unit pursuant to Article 9-1 of the law of 12 November 2004 on the fight against money laundering and terrorist financing regarding the cooperation between competent authorities.

1.11. “Risk management processes” on-site inspections

“Risk management processes” on-site inspections are, inter alia, aimed at ensuring the implementation by management companies and self-managed SICAVs of a risk management method in accordance with the laws and regulations.

In 2013, the CSSF carried out three such missions in management companies.

1.12. “UCI central administration function” on-site inspections

“UCI central administration function” on-site inspections are, inter alia, aimed at ensuring the legal and regulatory compliance of the internal organisation of authorised entities in order to exercise the central administration function on behalf of Luxembourg UCIs. Such an on-site inspection consists, in particular, in verifying the operating procedure in place and assessing the quality of the administrative and accounting procedures.

In 2013, the CSSF carried out two such missions, one within a management company and the other within a professional of the financial sector.

2. MEANS OF ADMINISTRATIVE POLICE

2.1. Legal framework

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 identified situation;
- suspension of persons, suspension of the voting rights of certain shareholders or suspension of the activities or of a business sector of the establishment concerned.

In addition, the CSSF has the right to:

- impose administrative fines on legal or natural persons subject to the CSSF supervision and on persons in charge of the administration or management of the establishments concerned;
- apply, under certain conditions, to the *Tribunal d'arrondissement* (District Court) sitting in commercial matters for suspension of payments of an establishment;
- ask the Minister of Finance to refuse registration on or to withdraw registration from the official list of credit institutions or 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;

⁵ Among which two dated from 2011 and four from 2012.

⁶ Among which one case dated from 2011 and three from 2012.

⁷ As regards a mission conducted in 2012.

- to refuse registration on or to withdraw registration from the official lists of entities subject to the supervision of the CSSF, if the conditions for being or continuing to be registered on the official list in question are not or no longer fulfilled;
- request, under precise conditions laid down by law, the *Tribunal d'arrondissement* (District Court) sitting in commercial matters to order the dissolution and the winding-up of an establishment.

Moreover, the CSSF informs the State Prosecutor of any instance of non-compliance with the legal provisions relating to the financial sector, giving rise to criminal sanctions and that could, where applicable, entail prosecution against the implicated persons. The following cases are concerned:

- persons performing an activity of the financial sector without holding the required licence;
- persons active in the field of domiciliation of companies without belonging to any of the professions entitled to carry on this activity pursuant to the law of 31 May 1999 governing the domiciliation of companies;
- persons other than those registered on official lists of the CSSF, who use a title or name, thereby breaching Article 52(2) of the law of 5 April 1993 on the financial sector, purporting to indicate that they are authorised to perform any of the activities reserved to persons registered on such a list;
- attempted fraud.

2.2. Decisions taken in 2013

In 2013, the CSSF took the following decisions with respect to administrative police. It should be noted that the total amount of administrative fines imposed in 2013 reached EUR 667,650 against EUR 562,375 in 2012.

2.2.1. Credit institutions

In 2013, the CSSF imposed three administrative fines pursuant to Article 63 of the law of 5 April 1993 on the financial sector, each amounting to EUR 60,000, EUR 25,000 and EUR 20,000, respectively, due to non-compliance with the professional obligations regarding AML/CFT.

A formal reprimand was given to a manager of a credit institution for serious breach of the obligation to submit the information requested by the CSSF.

Moreover, in 2013, the CSSF filed two complaints with the State Prosecutor due to illegal exercise of banking and financial activities by non-authorised entities.

2.2.2. Electronic money institutions

In 2013, the CSSF imposed one administrative fine of EUR 25,000 pursuant to Article 63 of the law of 5 April 1993 on the financial sector. This fine was imposed due to non-compliance with the professional obligations regarding AML/CFT.

2.2.3. Investment firms

In 2013, the CSSF imposed five administrative fines pursuant to Article 63 of the law of 5 April 1993 on the financial sector. Four of these fines (one of EUR 1,500 and three of EUR 2,000) were imposed for refusal to communicate, within the deadlines set, the documents requested by the CSSF in the framework of its prudential supervisory mission. The other fine amounting to EUR 10,000 was imposed for non-compliance with certain requirements provided for in Article 37-3(3) of the aforementioned law.

Moreover, the CSSF imposed two administrative fines of EUR 5,000 each, pursuant to Article 33.3 of the law of 9 May 2006 on market abuse, on investment firms which failed to act in response to an injunction from the CSSF for non-compliance with the obligations incumbent upon them under Article 12 of the aforementioned law.

All these fines were imposed on investment firms as legal persons.

The CSSF used its right of injunction in accordance with Article 59 of the law of 5 April 1993 on the financial sector on one occasion. The imposed injunction concerned the non-compliance with the AML/CFT laws and regulations.

With respect to investment firms, the CSSF filed three reports with the State Prosecutor in 2013, pursuant to Articles 23(2) and 23(3) of the Code of Criminal Procedure.

Furthermore, the CSSF filed three complaints with the State Prosecutor regarding entities which provided investment services without authorisation.

2.2.4. Specialised PFS

During 2013, the CSSF used its right of injunction in accordance with Article 59(1) of the law of 5 April 1993 on the financial sector on 10 occasions.

In three cases, the injunctions were issued due to non-compliance of the day-to-day management with the applicable law. In two cases, the injunctions concerned the setting in compliance with the capital base requirements of the specialised PFS. The CSSF imposed two injunctions for non-compliance with the AML/CFT professional obligations. One injunction concerned the exercise of an activity that was not covered by the PFS authorisation in question and, in two cases, the injunction aimed at shareholders who no longer fulfilled the required criteria of professional repute.

In 2013, the CSSF imposed three administrative fines on two specialised PFS, in accordance with Article 63 of the law of 5 April 1993 on the financial sector, amounting to EUR 10,000, EUR 15,000 and EUR 3,000, respectively. One fine originated in the non-compliance with an injunction imposed as a result of the exercise of an activity that was not covered by the authorisation of the specialised PFS in question. One fine was imposed due to non-compliance with the AML/CFT professional obligations and another fine concerned recurrent delays in the transmission of the prudential reporting to the CSSF.

All the fines were imposed on specialised PFS as legal persons.

In 2013, the CSSF withdrew, for two specialised PFS, the professional repute of certain members belonging to corporate bodies and of potential shareholders. In another case, the CSSF initiated, in 2013, a procedure for the withdrawal of the professional repute of an authorised manager and of potential shareholders. This procedure led, at the beginning of 2014, to the withdrawal of the professional repute of the persons in question. In each of the aforementioned cases, the persons concerned provided, within the context of an authorisation request, a declaration of honour that was incomplete, or even inaccurate.

2.2.5. Undertakings for collective investment

In accordance with Article 51(1) of the law of 13 February 2007 relating to specialised investment funds and Article 148(1) of the law of 17 December 2010 relating to undertakings for collective investment, the CSSF imposed administrative fines on the members of the management board of the general partner of 15 investment companies and the members of the board of directors of 15 investment companies, as well as on the members of the management board and the board of directors of the respective management company of three *fonds communs de placement* (mutual funds) for non-filing of the management letter. In total, 33 supervised entities were targeted by these administrative fines for non-filing of the management letter that amounted, as the case may be, to EUR 500, EUR 2,000 and EUR 4,000.

Pursuant to Article 51(1) of the law of 13 February 2007 relating to specialised investment funds and Article 148(1) of the law of 17 December 2010 relating to undertakings for collective investment, the CSSF imposed administrative fines on the directors of a management company of two *fonds communs de placement*, the directors of three investment companies, the members of the management board of the general partner of 19 investment companies and the board of directors of 19 investment companies, as well as the members of the management board of the management company of a *fonds commun de placement* for non-filing of the annual financial report. In total, 44 supervised entities were targeted by these administrative fines for

non-filing of the annual financial report that amounted, as the case may be, to EUR 500, EUR 2,000 and EUR 4,000.

In accordance with Article 148(1) of the law of 17 December 2010 relating to undertakings for collective investment, the CSSF imposed administrative fines of EUR 500 on the directors of the management company of a *fonds commun de placement* for non-filing of the UCI long form report within the regulatory deadlines.

In accordance with Article 51(1) of the law of 13 February 2007 relating to specialised investment funds, the CSSF imposed administrative fines of 2,000 on the members of the management board of an investment company for non-filing of the information requested by the CSSF.

In accordance with Article 148(1) of the law of 17 December 2010 relating to undertakings for collective investment, the CSSF imposed an administrative fine of EUR 4,000 on a natural person for filing of an incomplete declaration of honour.

During 2013, the CSSF decided to withdraw three SIFs from the official list for non-compliance with the legal provisions governing SIFs. Moreover, it refused registration of one entity on the official list of SIFs.

2.2.6. Management companies

In accordance with Article 148(1) of the law of 17 December 2010 relating to undertakings for collective investment, the CSSF imposed administrative fines of EUR 500 each on the members of the management board of a management company for non-filing of the annual financial report and of EUR 2,000 each on the members of the board of directors of three management companies for non-filing of the information requested by the CSSF.

2.2.7. Investment companies in risk capital (SICARs)

In accordance with the provisions of Article 17(1) of the law of 5 June 2004 relating to the Investment company in risk capital (SICAR), the CSSF imposed an administrative fine amounting to EUR 500 on each of the directors of a SICAR for non-compliance with the provisions of the law of 12 November 2004 on the fight against money laundering and terrorist financing.

Moreover, during 2013, the CSSF decided to withdraw one SICAR from the official list for non-compliance with the legal provisions governing SICARs.

2.2.8. Securities markets

Within the framework of cooperation between competent authorities as regards prospectuses for securities, an injunction as regards the filing and communication of the final terms was imposed on an issuer following the detection of infringements of the provisions of Article 8(4) of the Prospectus Law.

The review of financial reports under the Transparency Law led the CSSF to issue 20 injunctions, mainly due to delays in the disclosure and filing of annual and half-yearly financial reports. As a result of non-compliance with some of these injunctions, 11 administrative fines totalling EUR 42,500 were imposed pursuant to Article 25 of the Transparency Law.

Issuers that were subject to enforcement review (consistent enforcement of accounting standards) during the 2012 campaign, and whom the CSSF requested to change or improve the 2012 financial statements, were subject to a follow-up review in order to ensure compliance with the decisions taken by the CSSF. In this context, administrative fines totalling EUR 21,250 were imposed on three issuers that did not comply with certain formal requests of the CSSF as regards the improvement of the financial information in their 2012 financial statements or in their 2013 half-yearly financial statements. As regards the other specific enforcement measures, reference should be made to item 5. of Chapter X “Supervision of securities markets”.

As regards market abuse, six injunctions, mainly in connection with the control of the internal procedures implemented in order to comply with the professional obligations arising from the law on market abuse, were imposed in 2013. In accordance with Article 33.3 of this law, the CSSF imposed two administrative fines of EUR 5,000 each on institutions subject to its prudential supervision which failed to act in response to injunctions.

2.2.9. Audit profession

In accordance with Article 67(c) of the law of 18 December 2009 concerning the audit profession (Audit Law), the CSSF imposed, in 2013, five administrative fines of EUR 1,500 each and one administrative fine of EUR 3,000 for failure to disclose requested documents or other requested information. These fines were published in *Mémorial B* – No 37 of 10 April 2013 and *Mémorial B* – No 71 of 17 July 2013.

Pursuant to Article 67(d) of the Audit Law, the CSSF imposed on a *réviseur d'entreprises agréé* (approved statutory auditor) the suspension of the authorisation referred to in Article 5 of the aforementioned law and the striking-off from the public register for one year. This penalty was published in *Mémorial B* – No 71 of 17 July 2013.

In accordance with Article 67(e) of the Audit Law, the CSSF imposed, in 2013, (and following sanctions already imposed in 2012 and 2013) on a *réviseur d'entreprises agréé* the final withdrawal of his authorisation. This penalty was published in *Mémorial B* – No 71 of 17 July 2013. The *réviseur d'entreprises agréé* was also permanently removed from the public register maintained by the CSSF and from the list of IRE members.

Pursuant to Article 62 of the Audit Law, the CSSF imposed an injunction on a *cabinet de révision agréé* (approved audit firm) to resign from four of its mandates as statutory auditor of the annual accounts taking into account the breach of the principle of professional independence as defined in Article 19 of the above-mentioned law.

In accordance with Articles 62 and 63 of the Audit Law, the CSSF called a *cabinet de révision agréé* to order for breach of the principle of professional independence defined in Article 19 of the aforementioned law and requested it to remedy the situation.

CHAPTER XIV

FIGHT AGAINST MONEY LAUNDERING AND TERRORIST FINANCING



1. Amendments to the regulatory framework regarding the fight against money laundering and terrorist financing
2. Participation of the CSSF in meetings regarding the fight against money laundering and terrorist financing

Pursuant to Article 2 of the law of 23 December 1998 establishing the CSSF, the supervision by the CSSF pursues an objective of prevention of the use of the financial sector for criminal purposes and in particular for money laundering and terrorist financing purposes. Thus, as in previous years, the CSSF has implemented a comprehensive framework in order to fulfil this mission while following a risk-adapted supervisory approach in this respect. Some of these measures and sanctions are presented in more detail in this report under the respective chapters on the various activities of the financial sector.

1. AMENDMENTS TO THE REGULATORY FRAMEWORK REGARDING THE FIGHT AGAINST MONEY LAUNDERING AND TERRORIST FINANCING

1.1. Law of 12 November 2004 on the fight against money laundering and terrorist financing

The scope of application of the law of 12 November 2004 was extended in order to take account of the activity carried out by a new category of professionals of the financial sector, i.e. the alternative investment fund managers pursuant to the law of 12 July 2013 on alternative investment fund managers.

1.2. Criminal Code

The chapter of the Criminal Code relating to terrorism (Book II, Title 1, Chapter III-1.) underwent several changes following the entry into force, at the beginning of 2013, of the law of 26 December 2012 approving the Council of Europe Convention on the prevention of terrorism signed in Warsaw on 16 May 2005.

Consequently, in addition to the approval of the aforementioned Convention, this law, inter alia, criminalised some acts related to terrorist activities in order to henceforth cover the acts of provocation, recruitment or training for terrorism. The text relating to the terrorism offence has been revised in order to ensure that the definition of terrorist group can be applied starting the implication of two persons.

The aforementioned law also extended the terrorist-financing offence to cover the acts of terrorist financing even in the absence of one or several specific terrorist acts. These offences henceforth also constitute underlying money-laundering offences (Article 506-1 of the Criminal Code).

1.3. Code of Criminal Procedure

The law of 26 December 2012 approving the Council of Europe Convention on the prevention of terrorism signed in Warsaw on 16 May 2005 abandoned the exclusive territorial jurisdiction of the State Prosecutor and the investigating judge with the *Tribunal d'Arrondissement* (district court) of Luxembourg to hear cases relating to money laundering. It confers jurisdiction in this field also on counterpart authorities with the *Tribunal d'Arrondissement* of Diekirch.

However, for the sake of effectiveness and consistency, terrorism and terrorist financing offences remain the exclusive territorial jurisdiction of the State Prosecutor with the *Tribunal d'Arrondissement* of Luxembourg. Similarly, the Financial Intelligence Unit (FIU) remains exclusively empowered to receive reports of money laundering and terrorist financing suspicions in accordance with Article 5(1) of the law of 12 November 2004.

1.4. Ministerial regulations

In 2013, the Ministry of Finance issued 12 ministerial regulations implementing UN Resolutions 1988 (2011) (Taliban) and 1989 (2011) (Al-Qaida).

1.5. CSSF Regulation N° 12-02 of 14 December 2012 on the fight against money laundering and terrorist financing

For more details as regards CSSF Regulation N° 12-02 of 14 December 2012 on the fight against money laundering and terrorist financing which entered into force on 12 January 2013, reference should be made to the CSSF's Annual Report 2012.

1.6. CSSF Circulars and other published information

In 2013, the CSSF published three circulars (Circulars CSSF 13/573, 13/567 and 13/561) relating to the statements of the Financial Action Task Force (FATF) on:

- jurisdictions with substantial and strategic deficiencies in their anti-money laundering and terrorist financing (hereafter "AML/CFT") regimes;
- jurisdictions not making sufficient progress;
- jurisdictions whose AML/CFT regimes are not satisfactory.

Circular CSSF 13/556 of 16 January 2013 informed on the entry into force of CSSF Regulation N° 12-02 of 14 December 2012 on the fight against money laundering and terrorist financing and the repeal of Circulars CSSF 08/387 and 10/476.

On 20 January 2014, the CSSF published a press release drawing the attention of professionals and, in the first place, that of banks to the publication by the Basel Committee of the new recommendations on the sound management of risks related to money laundering and terrorist financing (cf. below).

2. PARTICIPATION OF THE CSSF IN MEETINGS REGARDING THE FIGHT AGAINST MONEY LAUNDERING AND TERRORIST FINANCING

2.1. International AML/CFT working groups

Following the adoption by the Financial Action Task Force (FATF) of the new AML/CFT recommendations (in 2012) and its new methodology (in 2013), the relevant organisations at international and European level, including the working groups of the FATF itself, continued the significant updating exercise of their own standards.

2.1.1. Financial Action Task Force (FATF) and its working groups

During the FATF's plenary meeting in February 2013, the new FATF "Methodology" on the basis of which the mutual evaluations will be carried out as from 2014 was formally adopted. Even if it is primarily targeted to the assessors and countries assessed by laying down precise evaluation criteria, it also includes clarifications on the interpretation of the new recommendations and examples of implementation that may be of interest for professionals.

Now a distinction should be made between, on the one hand, the technical compliance assessment as regards the 40 recommendations and, on the other hand, the assessment of the effectiveness of the AML/CFT framework put in place by the countries under review. As regards effectiveness, 11 major objectives were thus determined in accordance with the 40 recommendations. During the fourth round of mutual evaluations, these objectives shall be reached by the countries assessed in order to demonstrate their effectiveness. According to the FATF, the effectiveness assessment aims to: (1) further draw the FATF's attention to AML/CFT outcomes, (2) identify to what extent the national AML/CFT system meets the objectives of the FATF's standards and identify the systemic weaknesses, and (3) enable countries to prioritise the measures aiming to improve their system.

The FATF's statements relating to the different high-risk and non-cooperative countries and territories in 2013 were updated during the FATF meetings in February, June and October 2013 based on the conclusions of the ICRG (International Cooperation Review Group) working group. By way of three circulars published following these plenary meetings, the CSSF drew the attention of the supervised professionals to these countries and territories.

As regards the evaluation of Luxembourg, the FATF adopted the fifth follow-up report on the Luxembourg AML/CFT framework in February 2013. This report is part of the follow-up procedure as determined by the FATF plenary meeting following the mutual evaluation report of Luxembourg adopted in February 2010. During the plenary meeting of February 2014, the FATF accepted Luxembourg's request to get out of the regular monitoring process based on a sixth follow-up report drawn up by the FATF Secretariat and published on the FATF website. This complete follow-up report shows all the efforts made by Luxembourg to remedy the deficiencies identified by the FATF in its 2010 report. In that report, it came to the conclusion that Luxembourg addressed many major deficiencies as regards the key and core recommendations and thus raised the Luxembourg AML/CFT framework to a level that at least equals a "largely compliant" rating. Consequently, Luxembourg took the necessary measures to be withdrawn from the (annual) regular follow-up process.

Among the documents finalised in 2013 by the FATF and its working groups, the following should be mentioned:

- the guidelines on the fight against money laundering and terrorist financing and financial inclusion,
- the guidelines on a risk-based approach to pre-paid cards, mobile payments and Internet-related payment services,
- the guidelines on the implementation of the financial provisions of the United Nations Security Council Resolutions to counter the proliferation of weapons of mass destruction,
- the guidelines on politically exposed persons,
- the guidelines on the national risk assessment,
- the best practices in the fight against the misuse of non-profit organisations,
- the best practices on the targeted financial sanctions related to terrorism and terrorist financing,
- the best practices on the use of the FATF Recommendations to support the fight against corruption,
- the report on the vulnerabilities in terms of money laundering and terrorist financing of legal professionals,
- the report on the vulnerabilities in terms of money laundering and terrorist financing related to counterfeiting of money,
- the report on terrorist financing in West Africa,
- the report on Hawala's role and other similar service providers in money laundering and terrorist financing,
- the report on money laundering and terrorist financing through trade in diamonds.

As far as the organisation is concerned, it should be noted that the Organization for Security and Cooperation in Europe (OSCE) was received as observer member and that the first analyses on the study of the limited extension of the FATF members were carried out in 2013. The FATF emphasised, once again, on the significance of a close cooperation with regional organisations such as the FATF.

The FATF also dealt with the involvement of the private sector and general public within the context of its work. In this respect, a large public consultation took place on 24 to 26 April 2013 that focussed primarily on the new recommendations and the new FATF methodology.

Finally, the cooperation between the FATF and the G20 was further intensified in 2013. One of the key topics of this close cooperation concerns the fight against corruption. A third expert meeting in this respect was held in October 2013.

2.1.2. Anti-Money Laundering Committee (AMLC)

The AMLC dedicated to the fight against money laundering and terrorist financing is a sub-committee of the Joint Committee of the three European supervisory authorities (ESMA, EBA and EIOPA). In 2013, the committee met

on four occasions. In addition to the exchange of confidential information between supervisory authorities and the follow-up of other relevant bodies' work, for example within the context of the recast of the third AML/CFT Directive and the recast of the second directive relating to payment services, the new methodology of the committee was included in the agenda. Indeed, from the outset, it is worth underlining the key role that will be conferred in this regard on this committee in accordance with the proposed text for the fourth AML/CFT Directive which, in its current version, provides that the European supervisory authorities are in charge of preparing both simple reports or studies and binding technical standards, opinions and recommendations in this area.

The CSSF participated in the plenary meetings of the AMLC as well as in the working group dedicated to the study on the implementation of the risk-based approach within the context of the AML/CFT supervision. The mandate of this working group as well as that relating to payment institutions were renewed in 2013 and a new working group dedicated to the study of AML/CFT risk factors was created.

In 2013, the AMLC prepared the following reports:

- Preliminary report on AML/CFT Risk Based Supervision,
- Report on the application of Article 26 of the Payment Services Directive (PSD),
- Report on cost coverage of AML supervisory inspections of agents of payment institutions,
- Report on non face-to-face customer due diligence measures,
- Study of reasonable grounds for informing negatively on agents of payment institutions under the PSD.

These studies and reports serve, inter alia, as a support for the recast of the third AML/CFT Directive and the second directive on payment services.

2.1.3. Committee on the Prevention of Money Laundering and Terrorist Financing (CPMLTF) / Expert Group on Money Laundering and Terrorist Financing (EGMLTF)

The CPMLTF met once in 2013. In view of the rules on comitology procedure and the provisions of the Treaty of Lisbon, this committee shall be convened, in future, only to assist the European Commission in the exercise of its executive powers. For this reason and in order to also allow, in future, the assistance to the European Commission in the preparation and implementation of its policies, a new committee was put in place, i.e. the EGMLTF which met three times in 2013.

The items on the agenda included the follow-up of the negotiations relating to the proposal for the fourth AML/CFT Directive, the AML/CFT risk assessment at European level, as well as the preparation of the FATF's plenary meetings.

2.1.4. AML/CFT Expert Group (AMLEG)

The AML/CFT Expert Group of the Basel Committee on banking supervision met twice in 2013. The group discussed and finalised the new recommendations on the sound management of AML/CFT risks. The document entitled "Sound Risk Management relating to Money Laundering and Terrorist Financing", which was subject to a broad public consultation in summer 2013, was published on 15 January 2014. It includes the two previous documents "Customer Due Diligence for Banks" of October 2011 and "Consolidated KYC Risk Management" of October 2004 and includes two annexes with specific directives relating to correspondent banking relationship and the reliance by professionals on third parties for the performance of AML/CFT due diligence measures.

Moreover, given the group's expertise and for the purpose of best coordinating the various international initiatives, the group now actively participates in the FATF's working groups on the directives relating to the risk-based approach in the banking sector.

2.1.5. The Wolfsberg Group

The traditional plenary meeting of the Wolfsberg Group, composed of 11 banks that are significant in terms of their size and active worldwide, was held in May 2013. The topics discussed in the dedicated workshops included the effectiveness of the AML/CFT frameworks and the role and responsibilities of the AML/CFT compliance function as well as the international financial sanctions, the correspondent banking relationships and the issue of politically exposed persons (PEP).

In January 2014, the Wolfsberg Group published directives on the payment services provided via Internet or mobile phones. The documents relating to the correspondent banking relationships (the principles of the Wolfsberg Group, the frequently asked questions and a questionnaire relating thereto) were reviewed and a new version was published in February 2014.

2.2. National AML/CFT working groups

2.2.1. Coordination for the purpose of the FATF's work

Several coordination and consultation meetings were held in 2013 in order to take account of the numerous works and reports to be completed for the different FATF's groups.

2.2.2. Follow-up committee on international restrictive measures

As a member of the Follow-up committee on international restrictive measures established pursuant to the Grand-ducal regulation of 29 October 2010 enforcing the law of 27 October 2010, the CSSF took part in the two meetings held in 2013. The exchange of views between the members of the Follow-up committee concerned in particular the implementation of the old SR II and SR III recommendations of the FATF on the fight against terrorism and the financial sanctions relating thereto, the suspicious transaction reports as regards the fight against terrorist financing and the transposition into national law of the FATF's requirements as regards the fight against the proliferation of weapons of mass destruction and its financing. In respect of the implementation of international financial sanctions, the sanctions against the regimes in Iran and Libya were still current and were also on the agenda.

2.2.3. Meetings with the Financial Intelligence Unit (FIU)

In addition to the informal regular contacts, the enhanced cooperation between the FIU and the CSSF on the basis of Article 9-1 of the AML/CFT law of 12 November 2004 was enforced in practice by two formal meetings held in 2013. During these meetings, an exchange of views took place on the implementation and compliance of the professionals under the supervision of the CSSF. This information is taken into account within the context of the AML/CFT risk-adapted supervision by the CSSF. Besides concrete files on suspicious transaction reports, topics of legal interpretation and coordination of the approaches of the two authorities were also on the agenda.

2.2.4. AML/CFT Technical Committee of the Commissariat aux Assurances

The CSSF is represented within the Technical Committee "Fight against money laundering and the financing of terrorism" of the Commissariat aux Assurances. This committee met twice in 2013 with regard to the preparation of CAA Regulation N° 13/01 of 23 December 2013 on the fight against money laundering and financing of terrorism.

CHAPTER XV

FINANCIAL CONSUMER PROTECTION



1. Financial consumer protection
2. Out-of-court resolution of complaints

1. FINANCIAL CONSUMER PROTECTION

Even if, albeit indirectly, one of the objectives of prudential supervision has always been financial consumer protection, this objective has become, over the years, an explicit mission for regulators at international as well as national level. Such is also the case for the CSSF.

At the same time as the importance of financial consumer protection emerges, the idea that financial consumers will have more confidence in the financial system as they are able to understand basic principles is strengthening.

Concluding that financial consumer protection is closely intertwined with financial education is taking it only one step further; and this step has been taken easily as is reflected by the importance that financial education has taken recently.

1.1. Financial consumer protection and financial education at international level

The CSSF contributes to the work of several international groups the purpose of which is financial consumer protection and the spread of financial education.

1.1.1. Task Force on consumer protection of the OECD Committee on Financial Markets

As agreed in the Action Plan drawn up and endorsed by the G20 in 2012, the Task Force has developed a first set of Effective Approaches dealing with three of the ten G20 High-Level Principles, namely “Disclosure and Transparency” (Principle 4), “Responsible Business Conduct of Financial Services Providers and Authorised Agents” (Principle 6) and “Complaints Handling and Redress” (Principle 9).

In order to develop Effective Approaches for the application of each of the three principles above, expert working groups were created. The CSSF took part in the work of the working groups “Disclosure and Transparency” and “Complaints Handling and Redress”.

The work of the working groups helped the Task Force in drawing up a progress report. To this end, the Task Force met in plenary sessions in March, May and June 2013 at the OECD headquarters in Paris. Finally, the progress report was presented at the meeting of the G20 Finance Ministers in Moscow in July 2013 before being transmitted to the G20 Heads of State at the Summit in Saint Petersburg in September 2013.

In October 2013, the Task Force, in plenary session, decided to pursue its work on the Effective Approaches for the application of the G20 High-Level Principles. A survey was drawn up in order to gather information on effective approaches from members for the application of the following seven remaining High-Level Principles: “Legal, Regulatory and Supervisory Framework” (Principle 1), “Role of Oversight Bodies” (Principle 2), “Equitable and Fair Treatment of Consumers” (Principle 3), “Financial Education and Awareness” (Principle 5), “Protection of Consumer Assets against Fraud and Misuse” (Principle 7), “Protection of Consumer Data and Privacy” (Principle 8) and “Competition” (Principle 10).

1.1.2. Committee on Retail Investors - IOSCO C8

The needs in relation to financial education have never been as important as today. Indeed, financial products are growing more and more complex as the financial markets develop and globalise. The retail investor needs to have a more and more sophisticated understanding of financial concepts in order to make the right choices and to avoid being the victim of his/her ignorance in financial matters. In order to meet these challenges, the IOSCO Council decided in May 2013 to create a special committee called Committee on Retail Investors (C8).

The primary mandate of the committee is to conduct the IOSCO policy as regards financial education of retail investors. The secondary mandate is to advise the IOSCO Council on new issues relating to investor protection.

1.1.3. International Network on Financial Education of the OECD (INFE)

In 2013, the CSSF became a full member of the INFE, whose objective is to monitor the developments in financial education worldwide and the exchange of experiences between members. The goal is to develop a consolidated set of political and methodological instruments to implement financial education. Moreover, the INFE also contributes to the promotion of financial education at regional level.

1.1.4. Child and Youth Finance International (CYFI)

The CSSF supports the non-profit association Child and Youth Finance International based in the Netherlands and which operates as a global network. Its objective is twofold: CYFI aims, on the one hand, to ensure access of young people to appropriate products and services (financial inclusion), and, on the other hand, to promote their financial education. Every year in March, CYFI organises a week dedicated to financial issues, i.e. the Global Money Week. Many events are organised during that week in order to raise the awareness of young people with regard to money and, eventually, to improve their knowledge in terms of finance.

1.2. Consumer protection at national level

1.2.1. Financial Consumer Protection Committee (CPCF)

As financial consumer protection concerns many sectors, the CSSF considered it useful to bring together, within the same committee, the main stakeholders in order to discuss the various approaches and, where appropriate, to coordinate future actions. The CSSF chairs the committee composed of delegates of the following authorities, institutions and associations:

- The Luxembourg Bankers' Association;
- Association des Compagnies d'Assurances;
- Association Luxembourgeoise des Compliance Officers du secteur financier;
- Association of the Luxembourg Fund Industry;
- Banque centrale du Luxembourg;
- European Consumer Centre;
- Commissariat aux Assurances;
- Commission de Surveillance du Secteur Financier;
- Ministry of Economy;
- Ministry of National Education, Childhood and Youth;
- Ministry of Family, Integration and the Greater Region;
- Ministry of Finance;
- Union Luxembourgeoise des Consommateurs;
- University of Luxembourg.

It is not the CPCF's goal to interfere in the work of the various stakeholders but to exchange information, identify areas for improvement, coordinate certain initiatives or even carry out joint projects. The aim is to set up a dialogue which would, ultimately, lead to concrete results (adaptation of regulatory texts, improvement of the published information, achievement of joint projects in the field of financial education).

In this context, the Ministry of National Education requested the CPCF to draw up proposals in order to integrate certain elements of financial education into secondary school. The CPCF thus set up an ad hoc group which met several times to determine the competences that students should have in terms of financial education. In May 2013, the CPCF submitted a document to the Minister presenting several modules allowing a great flexibility in the drawing-up of financial education programmes.

Moreover, the CSSF invited financial education experts from neighbouring countries in 2013. Representatives from “My Finance Coach” (Germany), and “La finance pour tous” (France) presented the initiatives taken in this area in their countries. Representatives of the Conférence Nationale des Professeurs de Sciences économiques et sociales, the CNP-Formations administratives et commerciales, the Inter-Actions and the Ligue Médico-Sociale took part in these presentations as well.

1.2.2. Direct intervention of the CSSF as regards financial consumer protection

In 2013, the CSSF intervened with a bank under its supervision because a merchant offered a “free credit at 0%” in an advertising brochure in partnership with the bank. This advertising is a breach of the Consumer Code which prohibits, in its Article L-224-5, any offers mentioning “free credit” or an equivalent statement.

As Article 311-5 (§1) of the Consumer Code provides that the CSSF is competent to ensure compliance by the persons under its supervision with the laws protecting consumer interests and as Circular CSSF 05/177 provides that the CSSF has the power to demand the withdrawal of any misleading advertising used by the persons and undertakings under its supervision, the CSSF decided to handle this matter.

As the CSSF could not take action against the merchant directly, the latter not being under its supervision, it required the bank to take the following measures immediately:

- stop the offer in its current form, or require the merchant who initiated this advertising to stop the advertising in its current form;
- stop, if necessary, any credit offer stating “free credit” or an equivalent statement.

The bank complied immediately.

2. OUT-OF-COURT RESOLUTION OF COMPLAINTS

Since its inception, the CSSF plays the role of intermediary in the out-of-court resolution of complaints against professionals under its supervision. With the adoption of CSSF Regulation N° 13-02 relating to the out-of-court resolution of complaints which entered into force on 1 January 2014, the CSSF has a detailed regulatory framework covering this area.

2.1. CSSF Regulation N° 13-02 relating to the out-of-court resolution of complaints

The purpose of CSSF Regulation N° 13-02, published in *Mémorial A* - N° 187 of 28 October 2013 is, primarily, to update and regulate in detail the framework under which the customer complaints are dealt with by the CSSF.

The relevant provisions are laid down in Sections 1 and 3 of the regulation and entered into force on 1 January 2014. The regulation notably provides that the CSSF must address a reasoned conclusion for every request that had been properly submitted.

In addition, the regulation specifies the obligations of the professionals in relation to the internal handling of the customer complaints they receive. The relevant provisions are laid down in Section 2 of the regulation and enter into force on 1 July 2014 in order to allow the professionals to bring their internal procedures into line with the new requirements. Circular IML 95/118 will be repealed at the same date. The new requirements notably include the obligation for every professional to have a proper internal complaint management policy. All the complaints lodged with the professional, as well as all the measures taken to handle them, must be properly registered.

It is essential that a sound internal organisation for complaint handling be set up in order to ensure full compliance with the provisions of CSSF Regulation N° 13-02.

Every professional shall appoint a person, at management level, in charge of setting up an appropriate structure and internal procedure for complaint handling.

It should be stressed in this context that the manager responsible for complaint handling has a key function in the professional's complaint management. Indeed, the manager in charge must inform the staff concerned of the policies and procedures required by CSSF Regulation N° 13-02. Moreover, the professional's internal procedure must address the communication to the responsible manager in charge of all the necessary information concerning the complaints received at any level of the undertaking. The manager in charge shall thus follow up on the complaints internally and shall remain, in principle, the sole contact person of the CSSF within the scope of the procedure.

Through his/her hierarchical position, the manager in charge has a certain degree of independence with respect to the complaints lodged against operational units of the professional (agents, client managers, etc.). His/her position also gives him/her decision-making authority regarding transactions should the professional decide to make an offer to compensate the loss suffered by the complainant.

Moreover, the professionals must analyse the data relating to complaint handling on a permanent basis in order to be sure to identify and deal with any recurring or systemic problem that this analysis could reveal. The manager in charge is required to communicate to the CSSF, on an annual basis, a table stating the number of complaints registered by the professional, classified by type of complaints, as well as a summary report of the complaints and of the measures taken to handle them.

2.2. Statistics regarding CSSF complaint handling in 2013

Until 2013, the CSSF handled complaints according to the procedure laid down in Circular IML 95/118 on customer complaint handling. This procedure was not fundamentally different from the new procedure described in CSSF Regulation N° 13-02. Thus, the requirement that every complaint must be handled beforehand by a member of the management in charge of complaints in the entity concerned by the complaint, is a requirement set out in the former procedure and which is also included in the new one. This requirement makes it easier to seek an amicable settlement at the highest hierarchical level of the professional concerned by the complaint.

In 2013, the CSSF received 611 complaints from customers of the Luxembourg financial centre against entities under its supervision. It closed 525 files over the course of the year. These numbers are a continuation of those registered in 2012 and confirm that the consumers, as well as the professionals of the financial sector, are keenly interested in the intervention of the CSSF in disputes.

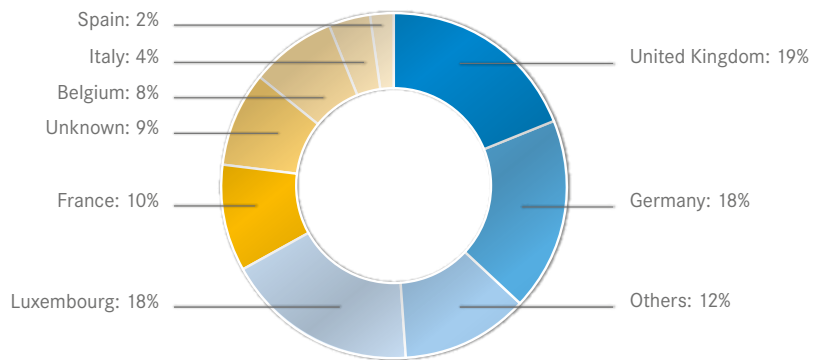
Outcome of the CSSF's intervention/reasons for closing the files

Results	Number	
Acknowledgement of receipt without further response from the client	378	
Conclusion of the CSSF in favour of the professional	48	
Amicable settlement	48	
Withdrawal by complainants	38	
Outside the scope of the CSSF's powers	11	
Contradictory positions of the parties	1	
Referral to the court	1	

When the CSSF receives a complaint from a consumer, its first approach consists in encouraging the parties to reach a bilateral agreement. Thus, the fact that a high number of acknowledgements of receipt sent by the CSSF remained unanswered is probably due to the fact that complainants often obtained satisfaction from the professionals after having contacted the manager in charge of complaints as indicated by the CSSF in the acknowledgement of receipt. Indeed, in most cases where the complainant communicated the reason thereof to the CSSF, the withdrawals resulted from the fact that the complainant had received an acceptable settlement proposal from the professional. This approach thus allows solving many issues between customers and finance professionals.

It should be noted that in 2013, the CSSF did not have to deal with any case where an opinion it had issued against a professional of the financial sector had not been acted upon. This demonstrates that the CSSF's opinions, although they are, in principle, not legally binding on the parties, have some moral authority in the Luxembourg financial sector.

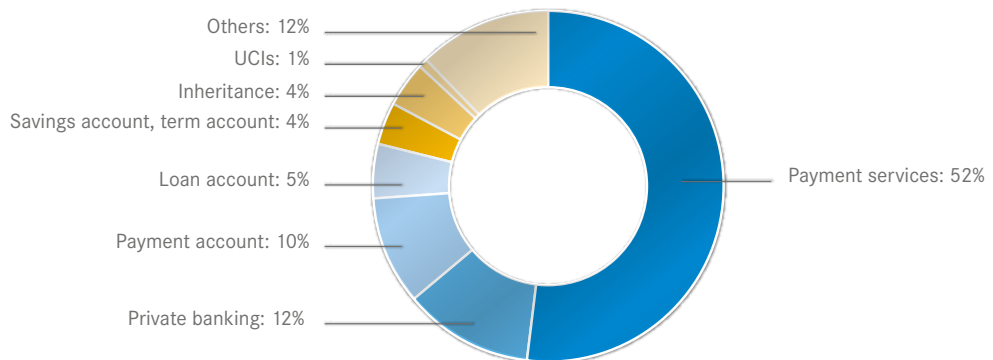
Breakdown of the complaints according to the complainant's country of residence



In 2013, the number of complaints lodged by British residents dropped significantly compared to 2012 (-30%). Nevertheless, the share of complaints from the United Kingdom remains high compared to the complaints from Luxembourg or from neighbouring countries, which accounts for the relatively large number of disputes related to electronic payment services which are specifically used in the United Kingdom.

The reason why in 9% of the cases the country of residence of the complainants is unknown is mainly because these complainants addressed the CSSF by way of emails without indicating their country of residence. Finally, it is worth mentioning that the category "Others" covers about 28 different countries.

Breakdown of complaints according to their object



As in the past years, the bulk of the complaints handled in 2013 concerned payment services related problems, even though, in absolute terms, the number of this type of complaints slightly fell compared to the previous

years. In this context, it should be highlighted that in 2013, the CSSF developed its website in order to provide consumers with additional information in the form of FAQs on the main problems they may encounter when using electronic payment services.

The share of complaints related to private banking remained stable with 12%. The percentage of complaints in connection with UCIs remained very low as compared to the importance of the UCI sector in Luxembourg.

2.3. Analysis of the complaints dealt with in 2013

It has been observed that financial consumers are increasingly aware of their rights and inclined to turn to the supervisory authority of the financial sector to assert their rights, without being willing to make concessions. Consequently, the CSSF is increasingly approached by financial consumers, not to help them find an amicable settlement with the professionals with which relationships deteriorated, but to pass judgement on their claims with the hope that the CSSF decides in their favour and orders the professionals of the financial sector to compensate them fully.

The analysis of the cases dealt with in 2013 focuses on the following points:

- obligation of the professional to provide information to its customers;
- asset management by the customer or by the professional;
- issues concerning housing savings schemes;
- fraudulent transfers;
- investor profiles;
- repayment problems faced by borrowers in financial distress.

2.3.1. Obligation of the professional to provide information to its customers

The CSSF received a complaint from a customer who had subscribed a financial product issued by a bank, called Euro Medium Term Note (EMTN) with a full capital repayment guarantee at maturity.

At the subscription of the EMTNs, the complainant received a brochure from the bank informing him on the financial product concerned. The customer could read under title “Terms and conditions” that “The commitment of the Bank as regards capital repayment (...) is only valid at maturity (...). In case of redemption before maturity, the Bank does neither guarantee full repayment of the nominal amount, nor payment of any minimum yield as specified in these terms and conditions. The redemption will be made at market value less an early redemption amount (...).”

When the complainant requested the bank to sell the financial product concerned before maturity, the bank refused. The complainant did not accept the refusal and requested the CSSF to appraise the bank’s behaviour.

The complainant put forward that he could reasonably understand from the information received from the bank that he had the possibility to sell the EMTNs early, at any moment, even though he might not receive the amount originally invested, it being understood that the repayment guarantee would only be valid at maturity.

The CSSF had to take an opinion as to whether the bank had indeed informed the customer of the liquidity risk of EMTNs and to assess whether the bank had clearly informed the customer that selling his EMTNs could be an issue as he would not necessarily find a buyer for these at the precise moment he wished to sell them.

The CSSF considered that the bank had not observed the Grand-ducal regulation of 13 July 2007 relating to organisational requirements and rules of conduct in the financial sector which provides in Article 36(3)(b) that credit institutions must inform their customers on any limitations on the available market on which such financial instruments may be traded and in Article 34(4) that the information concerned must, in principle, be provided on a durable medium. Indeed, the bank was not able to prove that it had informed the customer on a durable medium on the liquidity risk of EMTNs.

Moreover, the bank invoked as a defence the issue prospectus of the EMTNs, a 171-page long document written in a very technical English, in which the liquidity risks of EMTNs were mentioned. Nevertheless, as

the bank had not been able to prove that it had given this issue prospectus to the customer, the CSSF has concluded in favour of the customer.

2.3.2. Asset management by the customer or by the professional

In 2013, a complaint was lodged with the CSSF through which the complainant, disappointed by the results of the discretionary management of his portfolio, requested the CSSF to appraise whether the bank charged with this portfolio management had failed its contractual commitments by investing his assets in products that had not been agreed upon in the discretionary management.

In this specific case, the discretionary management agreement laid down that the client portfolio should be composed of shares, bonds and liquid assets. However, the CSSF noticed on a detailed account statement that the bank had delivered to the complainant that the bank had invested the client's assets not only in shares and bonds, but also in convertible bonds, structured bonds, equity funds, bond funds and "diverse" and "mixed" funds.

There was no doubt for the CSSF that the bank had overstepped its rights under the discretionary management agreement by investing its client's assets in products that are outside the scope of the discretionary management agreement and requested the bank to propose an amicable settlement to the complainant.

By doing so, the CSSF had also rejected the bank's defence which consisted in claiming that, as the client had not disputed the litigious investments within the time limits laid down in the terms and conditions, i.e. within 30 days, the client was estopped from acting. The CSSF noted, in this context, that the bank's behaviour was obviously faulty at the origin and that it could therefore not claim that the contractual time limit of 30 days had expired.

Where clients manage their assets themselves, they must carefully consider the instructions they give to the professionals of the financial sector in charge of executing these instructions. They must also properly understand the technical terms they may have to use.

In 2013, the CSSF handled thus a complaint where it was clear that the complainant had not understood the meaning of the stock market stop loss order he had given the bank. In this case, the complainant who used the bank's online services had given a stop loss order to sell, fixed at EUR 30, in the afternoon when the last market price of the security stood at EUR 34.10. The following morning, the first trade in this security was executed at EUR 8.10, i.e. a much lower price than the closing price the day before. This trade triggered the stop loss order and the sale instruction of the complainant was executed at a price of EUR 7.80. The complainant considered that he should have been informed by the bank of the deep fall of the price before executing the stop loss order.

The CSSF was of the opinion that the bank was not at fault by executing the stop loss order without informing the customer beforehand of the price fall. The CSSF considered that the customer could not ignore that a stop loss order to sell or buy securities becomes active as soon as the indicated price, called stop price, is reached. Furthermore, the complainant could not ignore that once activated, the stop loss order would be transformed into an order to be executed in principle at the next quoted price, whether that price is lower or higher than the stop order price.

Moreover, the CSSF recognised that the bank's terms and conditions, which had been accepted by the client, contained basic information on stop loss orders. In addition, the bank's terms and conditions drew the attention of the reader to the fact that stop loss orders must be used only on very liquid markets.

2.3.3. Issues concerning housing savings schemes

In 2013, various complaints related to housing savings schemes.

Thus, a complainant had signed a mortgage agreement with a housing savings scheme with a (variable) borrowing rate of 2.3%. Moreover, the complainant had concluded a housing savings contract with the same scheme with a fixed loan rate of 3% per year. The housing savings scheme had then raised, unilaterally, the

borrowing rate, previously fallen to 2.05%, to 3%. The complainant objected to this rise with the housing savings scheme, which responded that the rise from 2.05 to 3% was notably due to the fact that the scheme could not, ultimately, subsidize the financing of the complainant's construction. The complainant then addressed the CSSF with his complaint.

In order to ensure that the housing savings scheme had not overstepped its rights, the CSSF requested the scheme to explain on which contractual basis it had decided to raise the borrowing rate from 2.05 to 3% and to state the calculation basis used to determine the rise of the borrowing rate.

The housing savings scheme could not invoke any contractual provisions justifying this rise before the CSSF. It explained that the mortgage rate was adapted according to the interest rate granted to the complainant on his savings.

As the housing savings scheme was not able to provide the CSSF with contractual provisions or another valid basis justifying the litigious rise of the borrowing rate, the CSSF concluded that the rise from 2.05 to 3% was not justified.

In another case, a customer of a housing savings scheme disputed the indemnity for early repayment that the scheme had debited from his account according to a house loan and savings contract that the client had repaid before expiry of the terms laid down in the agreement.

The complainant requested the CSSF to be informed if the early repayment indemnity could legitimately be claimed by the housing savings scheme although he had never accepted such an indemnity in an agreement.

The housing savings scheme, questioned by the CSSF, invoked a document called "Application for a house loan and savings contract". Although the document in question had indeed been signed by the complainant, it did not include an early repayment indemnity clause. Moreover, the document referred to the terms and conditions of the housing savings scheme which did not include an early repayment indemnity clause either. In its position vis-à-vis the CSSF, the housing savings scheme also referred to a document called "European Standardised Information Sheet on early repayment" which, indeed, laid down certain provisions concerning an indemnity for early repayment. However, as this sheet had not been signed by the complainant and as the documents he had signed did not refer, in any way, to this sheet, the CSSF finally concluded that the early repayment indemnity debited by the housing savings scheme was not justified.

The housing savings scheme finally admitted that it should review its contracts and reimburse the amount of the early repayment indemnity to the client.

In another case, the complainant's housing savings scheme had unilaterally terminated the house loan and savings agreement. The client had saved the capital that entitled him to a home loan, but showed no interest in such a loan.

However, the contract signed by the complainant with the housing savings scheme did not provide for any term of the contract. The customer claimed that in such circumstances, the contract continued to be effective without limitations. The housing savings scheme, however, considered that the open-ended contract could be terminated at any given time and unilaterally without having to justify this termination. It invoked a jurisprudence according to which it could terminate the open-ended contract in its sole discretion, as long as the contract was not abruptly terminated. In this case, the housing savings scheme had terminated the contract with a three months' notice.

The CSSF believed that the three months' notice was acceptable. Furthermore, it considered that the housing savings scheme could validly terminate the contract as in this case, the purpose of the housing savings contract was no longer to obtain a housing loan, but to receive interesting interest on the savings.

2.3.4. Fraudulent transfers

In 2013, a complaint was lodged with the CSSF against a bank that had executed a transfer order on the account of a customer; the customer then considered that this order had been given without his knowledge by a fraudster. The question for the CSSF was to determine if the bank should have performed certain verifications with the account holder before executing that order.

The CSSF thus verified if the transfer order contained any anomalies that should have led the person executing the order in the bank to question the authenticity of the order received. The CSSF's examination focussed in particular on the circumstances surrounding the disputed order.

In this particular case, the transfer order had been faxed. However, the client did not use this means of communication with the bank for transfer orders. Indeed, the complainant usually sent his orders per post and these orders were confirmed orally by the complainant who contacted his account manager subsequently. The CSSF also analysed the details of the fax containing the disputed order. Thus, it was unusual that the order consisted of an urgent transfer of a substantial amount on the account of an individual in Spain with whom the complainant had not interacted before. Furthermore, the approximate syntax, some typing errors and uncertain punctuation should also have triggered doubts concerning the authenticity of the order in the mind of the person in charge of executing the order within the bank.

After having analysed the different elements of this file, the CSSF concluded that the bank should have contacted the concerned accountholder before executing the disputed order, which the bank had failed to do. The CSSF thus decided on a misconduct of the bank.

In another case of a (supposed) fraudulent transfer, the CSSF drew the attention of the bank which executed the disputed transfer to the following facts: the country of destination of the disputed transfer was a European country very far from the complainant's country of residence and the complainant had until then only made one single transfer from his account over a period of ten years. Moreover, this previous transfer had been explained beforehand through a telephone call by the complainant.

The CSSF confronted the bank with a case law according to which the banker is not only supposed to control the form and appearance of the document (in this case a fax containing a fraudulent order), but also the general circumstances surrounding the transaction (judgment of the Court of Appeal of 27 January 2005, No 25363 of the case list). In this context, the CSSF also referred to a judgment of the Court of Appeal of 11 November 2009 according to which it is a principle that the depositary bank shall not be discharged from its repayment obligation by proving that it is not at fault and that a total or partial discharge of the bank is only possible upon demonstration that the payment was the result of a fault attributable to the client.

It should be noted that in both cases of fraudulent transfers, the respective banks of the clients offered to settle the dispute amicably.

2.3.5. Investor profiles

The banks usually define the investor profile of their clients by letting them fill out forms. Clients thereby provide information on their risk appetite/aversion, their willingness to invest at short, medium and long term or their liquidity requirements.

The CSSF draws the attention of the financial consumer to the fact that it attaches great importance to this form, commonly known as "investor profile", as this form is especially useful when the CSSF is called upon to decide on a dispute between a finance professional and a financial consumer. The client should be well aware that he weakens his position in case of dispute if he does not take this exercise seriously.

In a complaint handled in 2013, a client complained that his bank had advised he should invest in a financial product that he found to be too risky afterwards. In its position communicated to the CSSF, the bank produced a document signed by the complainant in which the latter accepted investments in products with above-average risks. Questioned by the CSSF, the complainant finally admitted having signed the investor profile concerned, but that at the time the contract was signed, he had orally concluded something else with his adviser. The CSSF considered that the bank was not at fault as the product suggested to the client was in line with the investor profile signed. The CSSF could not take into account the complainant's statements, which, in the absence of evidence, could only be considered as mere allegations.

In another case, the investor profile contained contradictory statements. In one section of the investor profile, the client stated that he did not wish to have his assets invested in high-risk products as he wished to keep his capital for his retirement. In another section, the client accepted a so-called "Chance" profile, declaring his willingness to accept asset management allowing him to yield above-average gains and losses.

Called upon to assess whether or not the professional had advised products to the complainant that were too risky for his profile, the CSSF pointed out that both the complainant and the professional should have noticed the inconsistencies in the investor profile.

In another complaint lodged with the CSSF, the complainant claimed that the investor profile had been filled in without his knowledge by his account manager at the bank whom he trusted fully at the time. The CSSF drew the attention of the complainant to the fact that the investor profile had apparently been signed by him for approval. The complainant explained that he had signed a “blank” investor profile, i.e. without knowing the content of the profile, leaving it to his adviser at the bank to fill in the form. The CSSF can only warn of this kind of blind faith and recommends consumers to pay close attention to the filling-in of the form called “investor profile”. Clients should only sign the profiles when they fully agree with the content.

2.3.6. Repayment problems faced by borrowers in financial distress

The CSSF is increasingly faced with problems of borrowers experiencing financial difficulties.

In one case which is quite typical for this type of complaint, a complainant informed the CSSF that he had entered into a mortgage credit agreement with his bank in order to finance the construction of a house. Part of the payment should be made through the sale of another house belonging to the complainant, but this house had finally been sold at a lower price than that estimated.

In this difficult situation, the bank agreed to renegotiate the mortgage loan. Moreover, it granted an additional loan to the client which should enable him to pay the various bills pertaining to the construction of the new house.

Having lost his job and accumulated delays in the repayment of the granted loans, the client submitted to the bank a request to fully defer the repayment of the loan, and, alternatively, a debt rescheduling. An amicable settlement could be reached with the bank but eventually, it appeared that the complainant was unable to repay the loans granted by the bank.

The complainant then requested the bank to spread the loan over a longer duration than that initially laid down, in order to decrease the monthly rates. The bank refused to grant the request, as it had observed substantial delays in the repayment of the loan and pointed out that the complainant did not fulfil the age criteria allowing it to extend the duration of the loan repayment.

Finally, the complainant, who considered that the bank had not sufficiently considered his difficult situation, lodged a complaint with the CSSF. The CSSF recognised that the bank’s refusal was based on the observation that the sale of the first house had not yielded the expected revenue, that the completion of the construction of the new house had been much more expensive than foreseen and that the revenues of the complainant had decreased so that the complainant could no longer repay his financial commitments.

The CSSF closed this complaint by concluding that the bank could not be blamed for having refused to extend the duration of the loan, as the complainant had not been able to demonstrate that he could benefit from additional revenue, possibilities of external support or the possibility of refinancing by a third party.

It should be noted, in the context of this complaint, that the matter of mortgage credits should evolve in the short term, notably with the adoption of Directive 2014/17/EU of 4 February 2014 on credit agreements for consumers relating to residential immovable property.

This directive forms part of the actions of the European institutions to create an internal market of mortgage credit, in the context of the financial crisis. It requires lenders to assess the consumer’s ability to repay the credit, taking into account his personal situation and making sure to have sufficient information. In addition, the directive requires the lender to refuse to grant the credit if the results of this assessment are negative.

2.4. FIN-NET

FIN-NET, which was launched by the European Commission in 2001 focuses on the out-of-court financial dispute resolution. It is composed of bodies established in EEA countries which aim to resolve disputes arising between consumers and financial services providers out-of-court.

Within FIN-NET, the bodies cooperate to provide consumers with easy access to out-of-court complaint procedures in cross-border cases. If a consumer residing in a Member State has a dispute with a financial services provider from another Member State, FIN-NET members will put the consumer in touch with the relevant out-of court complaint settlement body and provide any necessary information in this context.

In its capacity as FIN-NET member, the CSSF took part in the two annual meetings of the network, one in Brussels in March 2013 and the other one in London in November 2013. These meetings concerned, inter alia, the legislative developments, Directive 2013/11/EU of 21 May 2013 on alternative dispute resolution for consumer disputes and amending Regulation (EC) No 2006/2004 and Directive 2009/22/EC, and Regulation (EU) No 524/2013 of 21 May 2013 on online dispute resolution for consumer disputes and amending Regulation (EC) No 2006/2004 and Directive 2009/22/EC.

The EBA and ESMA also took part in the meeting which was held in London. This participation marked the beginning of a cooperation with the FIN-NET members. Various other topics such as the sale of complex products to inexperienced consumers or the development of the ODR platform (in accordance with the regulation on online dispute resolution for consumer disputes) have also been discussed in London.

CHAPTER XVI

BANKING AND FINANCIAL LAWS AND REGULATIONS



1. Directives and regulations under discussion at EU level
2. Directives to be transposed under national law
3. Laws and regulations adopted in 2013

1. DIRECTIVES AND REGULATIONS UNDER DISCUSSION AT EU LEVEL

The CSSF participates in the groups examining the following proposals for directives or regulations.

1.1. Proposal for a regulation on key information documents for investment products (PRIIPs)

The proposal for a regulation, which was published on 3 July 2012, was discussed in detail in the CSSF's Annual Report 2012.

1.2. Proposal for a directive establishing a framework for the recovery and resolution of credit institutions and investment firms and amending Directive 82/891/EEC as well as Directives 2001/24/EC, 2002/47/EC, 2004/25/EC, 2005/56/EC, 2007/36/EC, 2011/35/EU, 2012/30/EU and 2013/36/EU and Regulations (EU) No 1093/2010 and (EU) No 648/2012 (BRRD)

The proposal for a directive was discussed in detail in the CSSF's Annual Report 2012. The Council, the European Parliament and the European Commission reached a political agreement in December 2013. The directive shall be transposed into national law by 31 December 2014 at the latest.

1.3. Proposal for a directive amending Directive 2009/65/EC on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS V Directive)

The proposal for a directive, which was published on 3 July 2012, was discussed in detail in the CSSF's Annual Report 2012. The Council, the European Parliament and the European Commission reached a political agreement in February 2014. The directive shall be transposed into national law, in principle, by mid-2016.

1.4. Proposal for a directive amending Directives 2003/71/EC and 2009/138/EC in respect of the powers of the European Securities and Markets Authority and the European Insurance and Occupational Pensions Authority (Omnibus Directive II)

The proposal for a directive was discussed in detail in the CSSF's Annual Report 2010.

1.5. Proposal for a directive on deposit guarantee schemes (recast)

The proposal for a directive was discussed in detail in the CSSF's Annual Report 2010. The final agreement within the Trialogue was reached in December 2013. As regards the financing of the deposit guarantee schemes, it should be noted that the target level of the ex ante-financed funds was adapted downwards compared to the original proposal of the European Commission and is now set at 0.8% of the guaranteed deposits.

1.6. Proposal for a directive amending Directive 97/9/EC on investor-compensation schemes

The discussions which had been put on hold since 2012 did not restart in 2013. The proposal for a directive was discussed in detail in the CSSF's Annual Report 2010.

1.7. Proposal for a directive on markets in financial instruments repealing Directive 2004/39/EC (MiFID II)

Proposal for a regulation on markets in financial instruments and amending Regulation EMIR on OTC derivatives, central counterparties and trade repositories (MiFIR)

A political agreement was reached at the beginning of 2014 but needs further discussion at technical level.

The proposal for a directive and the draft regulation were discussed in detail in the CSSF's Annual Report 2011.

1.8. Proposal for a regulation on insider dealing and market manipulation (market abuse)

Proposal for a directive on criminal sanctions for insider dealing and market manipulation

A political agreement on the proposal for a regulation was reached on 10 September 2013 between the European Parliament, the Council and the European Commission.

The proposal for a directive was adopted on 4 February 2014 by the European Parliament.

Both texts were discussed in detail in the CSSF's Annual Report 2011.

1.9. Proposal for a directive amending Directive 2006/43/EC on statutory audits of annual accounts and consolidated accounts

Proposal for a regulation on specific requirements regarding statutory audit of public-interest entities

The proposals for a directive and a regulation are further detailed under point 1.1. of Chapter XII "Public oversight of the audit profession".

1.10. Proposal for a directive on the transparency and comparability of payment account fees, payment account switching and access to a basic payment account

This proposal for a directive whose negotiations have started at the beginning of September 2013 aims to establish rules as regards the comparability and transparency of the fees to be borne by consumers with regard to their payment accounts held in the EU. Moreover, it provides for rules simplifying customer mobility within a Member State. Finally, it tends to lay down rules guaranteeing the access to payment accounts with basic features in the EU.

1.11. Proposal for a directive as regards disclosure of non-financial and diversity information by certain large companies and groups

On 16 April 2013, the European Commission published a proposal to amend existing accounting legislation (fourth and seventh accounting directives on the annual accounts and consolidated accounts - 78/660/EEC and 83/349/EEC) in order to improve the transparency of certain large companies on social and environmental matters. This proposal for a directive is, among others, the result of a wide public consultation, carried out by the European Commission with the Member States, firms, investors, preparers of financial statements and any other relevant party, which has started in November 2010.

Thus, in accordance with the proposal for a directive, certain large companies will have to include in their management report non-financial information relating to social, human rights and anti-corruption matters in addition to environment and employee-related aspects. Given that the selected approach is to limit the administrative burden on companies, this requirement only applies to large companies with more than 500 employees and either a total balance sheet over EUR 20 million or a net turnover over EUR 40 million. As regards the transparency on diversity within the decision-making bodies, the proposal for a directive will require large listed companies to disclose information on their diversity policy covering age, gender, geographical origin, educational and professional background. The information provided shall be included in the corporate

governance statement and describe the objectives of such a policy, its implementing arrangements and the results obtained.

The information to be provided is brief and is not aimed to impose an administrative burden which is out of all proportion on companies. Thus, if a company is not concerned by a specific area, it will not be required to disclose this information; it will merely have to explain the reason why it is not concerned.

Similarly, the proposal for a directive leaves companies considerable leeway for disclosing the information in question. As no strict framework is imposed on companies, they can decide freely what guiding principles should be applied: national, European or international principles.

1.12. Proposal for a regulation establishing uniform rules and a uniform procedure for the resolution of credit institutions and certain investment firms in the framework of a Single Resolution Mechanism and a Single Bank Resolution Fund and amending Regulation (EU) No 1093/2010 (SRM Regulation)

On 10 July 2013, the European Commission presented a proposal for a regulation aiming to establish a single resolution mechanism, with a view to the Banking Union, including a single bank resolution fund. This mechanism would complement the Single Supervisory Mechanism (SSM) which, from November 2014, will see the European Central Bank (ECB) directly supervise banks in the euro area and in other Member States which decide to join the Banking Union. If a bank subject to the SSM faced serious difficulties, the Single Resolution Mechanism (SRM) would enable - notwithstanding stronger supervision - the bank's resolution in an efficient way and with minimal costs for taxpayers and the real economy.

The SRM, as proposed by the European Commission, is based on the following principles:

- within the framework of the SRM, the uniform substantive rules laid down by the future directive establishing a framework for the recovery and resolution of credit institutions and investment firms (BRRD) will apply to the participating Member States as they will apply to the whole internal market;
- a Single Resolution Board will prepare, where appropriate, the resolution of a failing bank and will monitor the execution of the resolution plan by the national resolution authorities. The proposal also provides for detailed rules as regards the composition and the decision-making process of this Board;
- the action of the Single Resolution Board will be underpinned by the principle under which the losses, costs and other charges relating to the use of the resolution tools are to be borne by the shareholders and the creditors of the institution concerned and, as a last resort, by the financial sector, if need be. In order to guarantee short- and medium-term financial assistance or the provision of guarantees to potential acquirers of the institution concerned, a single bank resolution fund will be put in place under the control of the Single Resolution Board. This fund shall not be considered as a rescue fund. It will be financed by contributions from the banking sector and will replace the national resolution funds of the participating Member States. Detailed rules governing the functioning of the single bank resolution fund will be subject to an intergovernmental agreement. The methods for calculating the contributions from banks will be detailed through secondary legislation.

On 18 December 2013, the Member States agreed on a general SRM approach. On 20 March 2014, the European Parliament and the Council reached a political agreement on the SRM regulation. The SRM should become fully operational and the SRM Regulation be fully applied on 1 January 2016 provided that a sufficient number of Member States has ratified the intergovernmental agreement on the single bank resolution fund at this date.

1.13. Proposal for a regulation on the European long-term investment funds (ELTIFs)

The proposal for a regulation, published on 26 July 2013, aims to create a regulatory framework for a new form of long-term investment vehicles, the European long-term investment funds (ELTIFs) available to both professional and retail investors throughout the EU who/which are willing to invest their money into companies or projects for the long term, subject to compliance with certain requirements set out in the regulation in question.

These requirements concern, in particular, the categories of long-term assets and companies in which an ELTIF is authorised to invest (infrastructure, transport or sustainable energy projects, for example), how it should diversify its investments to minimise the risk thereof and the information it should provide to investors.

The purpose of this new regulatory framework governing ELTIFs is to create a second “passport” for the access to retail investors, according to the approach based on product standards and on risk spreading, which has proven its worth in the UCITS field. At the same time, it is proposed that only a EU AIF under the AIFMD may become an authorised ELTIF and this only if it is managed by an AIFM which is established within the EU and has been authorised pursuant to the AIFMD.

1.14. Proposal for a regulation on indices used as benchmarks in financial instruments and financial contracts

The proposal for a regulation, published on 18 September 2013, aims to improve the functioning and governance of benchmarks (used for the pricing of many financial instruments, such as interest rate swaps, for commercial and non-commercial contracts, such as loans and mortgages, and in risk management) and to ensure that benchmarks produced and used in the EU are robust, reliable, representative and that they are not subject to manipulation.

2. DIRECTIVES TO BE TRANSPOSED UNDER NATIONAL LAW

2.1. Directive 2011/89/EU of 16 November 2011 amending Directives 98/78/EC, 2002/87/EC, 2006/48/EC and 2009/138/EC as regards the supplementary supervision of financial entities in a financial conglomerate (FICOD 1)

Directive 2011/89/UE was discussed in detail in the CSSF’s Annual Report 2010. It is being partially transposed by draft law No 6456 on the insurance sector (which transposes into Luxembourg law Directive 2009/138/EC, also referred to as “Solvency II Directive” amended by Directive 2011/89/EU, the draft law taking into account the amendments brought about by the latter) as well as by draft law No 6660 mainly aiming to transpose into Luxembourg law the provisions of CRD IV.

2.2. Directive 2013/11/EU of 21 May 2013 on alternative dispute resolution for consumer disputes and amending Regulation (EC) No 2006/2004 and Directive 2009/22/EC

The directive was discussed in detail in point 2.3 of Chapter XV “Financial consumer protection” of the CSSF’s Annual Report 2012.

2.3. Directive 2013/14/EU of 21 May 2013 amending Directive 2003/41/EC on the activities and supervision of institutions for occupational retirement provision, Directive 2009/65/EC on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) and Directive 2011/61/EU on Alternative Investment Funds Managers in respect of over-reliance on credit ratings

The directive was discussed in detail in the CSSF’s Annual Report 2011.

2.4. Directive 2013/34/EU of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC and repealing Directives 78/660/EEC and 83/349/EEC

The directive was discussed in detail in the CSSF’s Annual Report 2011

2.5. Directive 2013/36/EU of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC (CRD IV)

Draft law No 6660 submitted to the *Chambre des Députés* (Luxembourg Chamber of Deputies) on 28 February 2014 primarily aims to transpose into Luxembourg law the provisions of CRD IV. Moreover, it repeals the legal provisions which have been superseded by the entry into force (and the direct applicability in national law) of Regulation (EU) No 575/2013 of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (CRR).

Since 1 January 2014, CRD IV and the CRR form the European legal framework for the authorisation and the prudential supervision of credit institutions and investment firms (without prejudice to the applicable provisions of the MiFID) in compliance with Basel III. Moreover, CRD IV and the CRR serve as a basis for the single rulebook on prudential supervision of institutions, which is the cornerstone on which the Banking Union is based.

The key elements of draft law No 6660 include among others:

- introduction of capital buffer requirements (in addition to the minimum ratios imposed by the CRR) providing an additional protection to institutions, thereby contributing to the maintenance of the high level of own funds that characterises Luxembourg institutions, or even to the financial stability of the financial sector as a whole;
- enhanced internal governance requirements in order to prevent the impact poorly designed corporate governance systems may have on sound risk management at the level of the institutions concerned;
- introduction of provisions relating to the remuneration policies of certain categories of staff, including in particular a maximum ratio of 100%, or 200% in exceptional cases, which limits the variable component (boni, stock options, etc.) of the remuneration compared to the non-variable component of the remuneration;
- adaptation of the administrative monetary penalty regime to the minimum harmonisation requirements included in CRD IV;
- targeted amendments to the authorisation conditions for credit institutions and, in particular, the requirement that the capital base of credit institutions must henceforth be constituted of a fully paid up share capital of EUR 8.7 million.

The transposition of CRD IV will be supplemented by CSSF regulations on more technical aspects of the directive.

2.6. Directive 2013/50/EU of 22 October 2013 amending 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, Directive 2003/71/EC on the prospectus to be published when securities are offered to the public or admitted to trading and Directive 2007/14/EC laying down detailed rules for the implementation of certain provisions of Directive 2004/109/EC

The directive is further detailed under point 4.3. of Chapter X “Supervision of securities markets”.

2.7. Directive 2014/17/EU of 4 February 2014 on credit agreements for consumers relating to residential immovable property and amending Directives 2008/48/EC and 2013/36/EU and Regulation (EU) No 1093/2010

This directive must be transposed into national law by 21 March 2016.

3. LAWS AND REGULATIONS ADOPTED IN 2013

3.1. Law of 6 April 2013 on dematerialised securities

The law aims to modernise Luxembourg securities law by introducing the generalised option for Luxembourg capital companies to issue equity securities in dematerialised form and for any other issuer to issue dematerialised debt securities governed by Luxembourg law.

Following the example of Belgian law, dematerialised securities are considered, under the law, as being a specific type of securities, in addition to bearer securities and registered securities. In order to guarantee investors' rights, the law requires that dematerialised securities are issued by a professional that is specifically authorised to this end. Thus, the issuing account can only be opened with a clearing institution (mandatory for securities listed on a regulated market or multilateral trading facility) or a central account keeper (only possible for non-listed securities). In this respect, the law amends the law of 5 April 1993 on the financial sector in order to introduce a new status of professional of the financial sector (Article 28-11): the central account keeper. The law does not provide for a mandatory dematerialisation but a mandatory conversion procedure if the issuer so decides. In order to maintain regime unity among the securities subject to the factual dematerialisation and the securities which are dematerialised *de jure*, the legislation on the circulation of securities provided by the law of 1 August 2001 on the circulation of securities and other fungible instruments is extended to dematerialised securities.

This law also incorporates a certain number of principles included in the International Convention on securities signed in Geneva on 9 October 2009 in order to increase the legal certainty of securities transactions. The text also takes account of the European Commission's work with a view to drawing up a directive referred to as "Securities Law Directive", which will incorporate a large proportion of the rules set down by the International Convention on securities into Community law.

3.2. Regulation (EU) No 345/2013 of 17 April 2013 on European venture capital funds (EuVECA) Regulation (EU) No 346/2013 of 17 April 2013 on European social entrepreneurship funds (EuSEF)

These texts were discussed in detail in the CSSF's Annual Report 2011.

On 2 August 2013, the CSSF published a press release in order to recall the date of application of the two regulations in question, i.e. 22 July 2013 and to inform that the CSSF is the competent authority for the managers established in Luxembourg which are willing to market their funds under the name "EuVECA" or "EuSEF". It should be noted, in this context, that these managers must comply with the requirements of the AIFMD.

3.3. Regulation (EU) No 462/2013 of 21 May 2013 amending Regulation (EC) No 1060/2009 on credit rating agencies (CRA III)

The regulation was discussed in detail in the CSSF's Annual Report 2011.

3.4. Regulation (EU) No 524/2013 of 21 May 2013 on online dispute resolution for consumer disputes and amending Regulation (EC) No 2006/2004 and Directive 2009/22/EC

The regulation was discussed in detail in point 2.3 of Chapter XV "Financial consumer protection" of the CSSF's Annual Report 2012.

3.5. Law of 27 June 2013 on banks issuing covered bonds

The law reforms the regime applicable to banks issuing covered bonds in particular as regards the following two points:

- the dissolution and liquidation regime for banks issuing covered bonds is aligned with the newly reformed German framework which consists in maintaining the banking status for the part constituted by collateral and covered bonds issued, in case of the liquidation of the bank issuing covered bonds;
- the introduction of a new category of covered bonds, namely mutual covered bonds.

3.6. Law of 12 July 2013 on alternative investment fund managers

The law mainly aims to transpose Directive 2011/61/EU on alternative investment fund managers (AIFMD) into Luxembourg law.

The AIFMD aims at providing a harmonised regulatory and supervisory framework which alternative investment fund managers (AIFMs) have to comply with within the EU. AIFMs are legal persons whose regular professional business is managing alternative investment funds (AIFs). This directive applies to all AIFMs established in the EU and to all AIFMs established outside the EU which have at least part of the activities exercised within the EU (either through the management of European AIFs or through the marketing of AIFs in the EU).

The AIFMD sets out the rules on the organisation and conduct of the business for the management of AIFs. In return, the managers of these funds are offered new opportunities through a European passport which allows them to provide management services and to offer their funds to well-informed investors in all the EU Member States.

The provisions of the directive cover, among others, the authorisation conditions for AIFMs, the capital requirements, the requirements as regards liquidity and risk management, the requirements in relation to valuation, depositaries, delegation arrangements, disclosure of information, restrictions on the use of leverage and the clauses for non-EU countries.

The AIFMD provides for a lighter regime for managers where the cumulative AIFs under management fall below a threshold of EUR 100 million and for AIFMs that manage only unleveraged AIFs that do not grant investors redemption rights during a period of 5 years where the cumulative AIFs under management fall below a threshold of EUR 500 million. These managers need no full agreement (with complete submission to the directive) but must be registered (with a simplified reporting regime) with the competent authority.

Moreover, the law of 12 July 2013 aims to achieve several other objectives. Thus, it introduces a new type of professional of the financial sector, i.e. the professional depositary of assets other than financial instruments (Article 26-1 of the law of 5 April 1993 on the financial sector). Other noteworthy innovations are the creation under Luxembourg law of a *société en commandite spéciale* (special limited partnership) without a legal personality and the modernisation of the regime of *sociétés en commandite simple* (limited partnerships). The law finally defines a special tax regime providing managers with, *inter alia*, a reduced tax regime on carried interests in order to attract financial professionals to Luxembourg.

On 18 July 2013, the CSSF published two press releases on the entry into force of the law of 12 July 2013 and the registration or authorisation procedures as AIFM under this law, with the AIFMD Guidance for Luxembourg entities which potentially qualify as such managers.

Moreover, on 18 June 2013, the CSSF already published a press release in order to inform companies willing to be authorised under the AIFMD that they can submit an application with the CSSF and download the necessary forms on its website.

The CSSF also published frequently asked questions (in English) as regards the law of 12 July 2013 and Commission Delegated Regulation (EU) No 231/2013 supplementing the AIFMD with regard to exemptions, general operating conditions, depositaries, leverage, transparency and supervision. These regularly updated FAQs as well as application forms for authorisation and application forms for registration as alternative investment fund managers are available on the CSSF website under the section "AIFM".

3.7. Law of 12 July 2013 on short selling of financial instruments implementing Regulation (EU) No 236/2012 of 14 March 2012 on short selling and certain aspects of credit default swaps

This law implements certain provisions of Regulation (EU) No 236/2012 on short selling and certain aspects of credit default swaps. More specifically, it designates the CSSF as the competent authority in Luxembourg to ensure that the provisions of Regulation (EU) No 236/2012 are applied and provides for measures and powers of intervention specific to short selling and credit default swaps, as well as administrative measures and administrative penalties in case of non-compliance with the provisions of the regulation.

3.8. Law of 30 July 2013 reforming the *Commission des normes comptables* (accounting standards board) and amending various provisions relating to accounting and annual accounts of firms as well as to consolidated accounts of certain types of companies

The law of 30 July 2013 (CNC Law) supplements the modernisation of the legal provisions on corporate accounting following the entry into force of the law of 10 December 2010 relating to the introduction of the international accounting standards for companies.

The CNC Law includes three parts:

- a reform of the *Commission des normes comptables* (CNC - accounting standards board);
- the determination of the distributable reserves when using the fair value measurement method or international accounting standards in general;
- various amendments to accounting and annual accounts of firms as well as to the consolidated accounts of certain types of companies.

The purpose of reforming the CNC is mainly in line with the plan to create a consultative commission that is consistent with the accounting standards framework and the accounting law and to provide Luxembourg with an autonomous modern accounting body both from an operational and financial point of view. This body should also be independent from a legal point of view, allowing it to take position quickly and in its name in European and international accounting bodies.

Thus, the new CNC is organised in the form of a *groupement d'intérêt économique* (economic interest group) in accordance with the law of 25 March 1991, the purpose of which is to promote the accounting doctrine in Luxembourg, to advise, where appropriate, the Government (either on the latter's request or on its own initiative), to participate in discussions on accounting within European and international bodies and to undertake all the research and studies necessary to fulfil its mission.

The CNC grouping is managed by a Management Board which constitutes the executive body of the CNC and comprises 12 members appointed by the general meeting. The composition of the Management Board reflects a balance of the (public and private) stakeholders interested in accounting. The Management Board is in charge, in the exercise of its powers, of the determination of the working programme of the CNC, the supervision of the work carried out by the experts within the working groups as well as doctrinal opinions and other recommendations.

Working groups were created within the CNC group in which experts participate, namely the following:

- Working group No 1 "Draft laws and accounting doctrine";
- Working group No 2 "SCA and filing procedures";
- Working group No 3 "Derogations Article 27¹";
- Working group No 4 "European and international affairs".

The CSSF is represented in the Management Board of the CNC as well as in the various working groups.

Moreover, two accounting elements included in the CNC Law to which the CSSF, through the press release of 17 January 2014, drew the supervised entities' attention, should be noted in particular:

¹ Derogations in accordance with Article 27 of the law of 19 December 2002 concerning the trade and companies register as well as the accounting and annual accounts of companies.

- determination of distributable reserves when using the fair value measurement method or international accounting standards in general;
- the requirement for support PFS publishing their annual accounts according to Lux GAAP, to deposit account balances according to the standard chart of accounts with the trade and companies register which implies, furthermore, a deposit of the balance sheet, profit and loss account and standard chart of accounts in a structured form.

3.9. CSSF Regulation N° 13-02 of 15 October 2013 relating to the out-of-court resolution of complaints

The regulation is further detailed under point 2.1. of Chapter XV “Financial consumer protection”.

3.10. Regulation (EU) No 1024/2013 of 15 October 2013 conferring specific tasks on the European Central Bank concerning policies relating to the prudential supervision of credit institutions (Single Supervisory Mechanism SSM) (SSM Regulation)

The SSM Regulation, which is directly applicable in Luxembourg as from 3 November 2013, was discussed in detail in the CSSF’s Annual Report 2012. It should be noted that an ECB regulation, which was adopted on 4 May 2014, aims to implement certain provisions of the aforementioned European Regulation. More detailed information on these texts is available in point 1.2. dedicated to the SSM in Chapter II “European dimension of the supervision of the financial sector”.

3.11. Regulation (EU) No 1022/2013 of 22 October 2013 amending Regulation (EU) No 1093/2010 establishing a European Supervisory Authority (European Banking Authority) as regards the conferral of specific tasks on the European Central Bank pursuant to Regulation (EU) No 1024/2013

This regulation which aims to amend Regulation (EU) No 1093/2010, in particular on the voting modalities in order to ensure fair and efficient decision-making between the EU supervisory authorities following the implementation of the SSM, is directly applicable in Luxembourg since 3 November 2013.

3.12. Regulation (EU) No 575/2013 of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (CRR)

The CRR is entered into force on 1 January 2014 and is directly applicable to Luxembourg credit institutions and investment firms within the meaning of the CRR.

Since 1 January 2014, CRD IV and the CRR form the European legal framework for the authorisation and the prudential supervision of credit institutions and investment firms (without prejudice to the applicable provisions of MiFID) in compliance with Basel III.

Thus, the CRR lays down uniform rules concerning the general prudential requirements that all the institutions subject to supervision in accordance with CRD IV must comply with, notably in terms of own funds, capital requirements, large exposures, exposures to transferred credit risk, liquidity risk, leverage risk, as well as in terms of reporting and disclosure requirements. As an example, since 1 January 2014, the solvency ratio is calculated in accordance with the provisions of the CRR supplemented by CSSF Regulation N° 14-01 and the technical standards of the EBA.

Some provisions of the CRR and of CRD IV are further specified through technical standards developed by the EBA and issued by means of regulations of the European Commission which are directly applicable to CRR institutions. These regulations of the European Commission are available on the website of the Official Journal of the EU (<http://eur-lex.europa.eu>) as well as on the CSSF website (<http://www.cssf.lu/en/documentation/regulations/laws-regulations-and-other-texts/>).

3.13. CSSF Regulation N° 14-01 on the implementation of certain discretions of Regulation (EU) No 575/2013

CSSF Regulation N° 14-01, which is in force since 24 February 2014, follows the entry into force of the CRR on 1 January 2014.

It provides for the rules applicable in Luxembourg regarding Member States discretions, and even competent authorities discretions, included in the CRR. CSSF Regulation N° 14-01 thus supplements the CRR in this respect. It includes, in particular, provisions relating to capital requirements and capital buffers applicable since 1 January 2014 as well as exposures exempted from obligations as regards large exposures.

With some very specific exceptions, CSSF Regulation N° 14-01 anticipates, to a very large extent, the fully phased-in regime as included in the CRR.

Among the salient provisions of CSSF Regulation N° 14-01, it should be noted that in accordance with Article 6, the institutions are required to have, from February 2014, in addition to the amount of own funds held to comply with the solvency ratios, a conservation capital buffer, made of Common Equity Tier 1 capital equal to 2.5% of their total risk exposure amount calculated in accordance with Article 92(3) of the CRR.

Finally, Article 20 of CSSF Regulation N° 14-01 includes a series of conditions which are to be complied with by the institutions in order to be able to benefit from the group exemption as regards large exposures. These conditions concern both the (normal) scenario of going concern and the scenario of application of a resolution procedure and aim to guarantee basic safeguards relating to the use of this exemption.

ANNEXE

LIST OF ABBREVIATIONS



LIST OF ABBREVIATIONS

AGDL	Association pour la garantie des dépôts, Luxembourg – Deposit Guarantee Association Luxembourg
AIF	Alternative Investment Fund
AIFM	Alternative Investment Fund Manager
AML/CFT	Anti-Money Laundering and Counter-Terrorist Financing
AQR	Asset Quality Review
ASSEP	Association d'épargne-pension – Pension savings association
BCL	Banque centrale du Luxembourg – Luxembourg Central Bank
BTS	Binding Technical Standards
COREP	Common Reporting
CRD	Capital Requirements Directive
CRR	Capital Requirements Regulation (575/2013)
CSSF	Commission de Surveillance du Secteur Financier – Financial sector supervisory commission
EAIG	European Audit Inspection Group
EBA	European Banking Authority
EC	European Community
ECB	European Central Bank
EEA	European Economic Area
EFRAG	European Financial Reporting Advisory Group
EIOPA	European Insurance and Occupational Pensions Authority
EMI	Electronic Money Institution
EMIR	European Market Infrastructure Regulation
ESFS	European System of Financial Supervision
ESMA	European Securities and Markets Authority
ESRB	European Systemic Risk Board
ETF	Exchange Traded Fund
EU	European Union
EUR	Euro
FATF	Financial Action Task Force
FCP	Fonds commun de placement – common fund
FINREP	Financial Reporting
FIU	Financial Intelligence Unit
FSB	Financial Stability Board
IAASB	International Auditing and Assurance Standards Board
IAPN	International Auditing Practice Note
IAS	International Accounting Standards
IASB	International Accounting Standards Board
ICAAP	Internal Capital Adequacy Assessment Process
IESBA	International Ethics Standards Board for Accountants
IFAC	International Federation of Accountants
IFRS	International Financial Reporting Standards

ILAAP	Internal Liquidity Adequacy Assessment Process
IML	Institut Monétaire Luxembourgeois – Luxembourg Monetary Institute (1983-1998)
IORP	Institution for Occupational Retirement Provision
IOSCO	International Organisation of Securities Commissions
IRE	Institut des réviseurs d'entreprises – Luxembourg institute of registered auditors
ISA	International Standards on Audit
ISQC	International Standard on Quality Control
LCR	Liquidity Coverage Requirement
LEI	Legal Entity Identifier
MiFID	Markets in Financial Instruments Directive
MiFIR	Markets in Financial Instruments Regulation
MTF	Multilateral Trading Facility
NAV	Net Asset Value
NCA	National Competent Authority
NSFR	Net Stable Funding Requirement
OEC	Ordre des experts-comptables – Institute of chartered accountants
OECD	Organisation for Economic Cooperation and Development
PFS	Professional of the Financial Sector
PIE	Public Interest Entity
RTS	Regulatory Technical Standards
SBL	Société de la Bourse de Luxembourg – Luxembourg Stock Exchange
SEPA	Single European Payments Area
SEPCAV	Société d'épargne-pension à capital variable – Pension savings company with variable capital
SIAG	Société d'investissement auto-gérée – Investment company which has not designated a management company within the meaning of Article 27 of the law of 17 December 2010
SICAF	Société d'investissement à capital fixe – Investment company with fixed capital
SICAR	Société d'investissement en capital à risque – Investment company in risk capital
SICAV	Société d'investissement à capital variable – Investment company with variable capital
SIF	Specialised Investment Fund
SME	Small and Medium-sized Enterprises
SREP	SSM Supervisory Review and Evaluation Process
SRM	Single Resolution Mechanism
SRP	Supervisory Review Process
SSM	Single Supervisory Mechanism
TREM	Transaction Reporting Exchange Mechanism
UCI	Undertaking for Collective Investment
UCITS	Undertaking for Collective Investment in Transferable Securities
VaR	Value-at-Risk
XBRL	eXtensible Business Reporting Language



**COMMISSION DE SURVEILLANCE
DU SECTEUR FINANCIER**

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