Repealed by the Law of 13 February 2007

LAW OF 19TH JULY, 1991 CONCERNING UNDERTAKINGS FOR COLLECTIVE INVESTMENT THE SECURITIES OF WHICH ARE NOT INTENDED TO BE PLACED WITH THE PUBLIC

Art. 1. This Law is applicable to all undertakings situated in the Grand-Duchy of Luxembourg, the sole object of which is the collective investment of their funds in assets in order to spread the investment risks and to ensure for their investors the benefit of the results of the management thereof, and which restrict their units to one or several institutional investors.

Art. 2. There shall be regarded as a common fund for the application of this Law any undivided collection of assets made up and managed according to the principle of risk spreading on behalf of joint owners who are liable only up to the amount contributed by them and whose rights are represented by units restricted to one or several institutional investors.

Art. 3. Articles 61, 62 and 63 of the Law of 30th March, 1988 relating to undertakings for collective investment are applicable to the undertakings referred to in Article 2.

Art. 4. Investment companies with variable capital shall be taken to mean, for the purpose of this Law, those companies which have adopted the form of a public limited company (*société anonyme*) governed by Luxembourg law,

- the exclusive object of which is to invest their funds in assets in order to spread the investment risks and to ensure for their investors the benefit of the results of the management thereof, and
- the shares of which are restricted to one or several institutional investors, and
- whose articles of incorporation provide that the amount of the capital shall at all times be equal to the value of the net assets of the company.

Art. 5. Articles 65 and 66 of the Law of 30th March, 1988 relating to undertakings for collective investment are applicable to the undertakings referred to in Article 4.

Art. 6. Undertakings which are subject to this Law and which have adopted neither the legal form of a common fund nor of an investment company with variable capital, are subject to Articles 68 and 69 of the Law of 30th March, 1988 relating to undertakings for collective investment.

Art. 7. Save for Chapter 19 thereof, the provisions of Part IV of the Law of 30th March, 1988 relating to undertakings for collective investment are applicable to the undertakings subject to this Law.

GRAND-DUCAL REGULATION OF 14TH APRIL, 2003 ESTABLISHING THE TERMS AND AMOUNT OF THE FIXED CAPITAL DUTY PAYABLE PURSUANT TO ARTICLE 128 OF THE LAW OF 2OTH DECEMBER, 2002 RELATING TO UNDERTAKINGS FOR COLLECTIVE INVESTMENT

Art. 1. The fixed capital duty payable pursuant to Article 128 of the Law of 20th December, 2002 relating to undertakings for collective investment is fixed at 1,250 euro.

The fixed duty is payable at the constitution and covers any aggregation of capital which may be carried out by an undertaking for collective investment, *inter alia* where the capital is increased, where an undertaking subject to the aforementioned law is transformed into another undertaking subject to that law and where such undertakings merge.

Art. 2. In respect of the aggregation of capital effected after 1st October, 1983 in undertakings for collective investment existing at that date, capital duty paid on formation by such undertakings has the same effects as those set out in paragraph 2 of Article 1 and which derive from the payment of the fixed capital duty referred to in paragraph 1 of such Article.

Art. 3. The transformation of an undertaking for collective investment governed by the Law of 30th March 1988 on undertakings for collective investment or by the Law of 19th July 1991 concerning undertakings for collective investment the securities of which are not intended to be placed with the public into an undertaking governed by the Law of 20th December 2002 relating to undertakings for collective investment does not cause the fixed capital duty referred to in Article 1 to become payable.

Art. 4. The conversion of a civil company[111] or of a commercial company not governed by the Law of 20th December, 2002 relating to undertakings for collective investment into an undertaking subject to the provisions of such law, triggers the fixed capital duty referred to in Article 1.

Art. 5. The transformation of an undertaking for collective investment subject to the Law of 20th December, 2002 relating to undertakings for collective investment into a civil or commercial company not subject to the provisions of such law, triggers the capital duties which according to the Law of 29th December, 1971 on the tax levied on the aggregation of capital in civil and commercial companies would have been payable on the aggregation of capital effected during the period in which the relevant undertaking was subject to the particular conditions of undertakings for collective investment. The fixed capital duty of Article 1 will not be set off against the duties due.

Art. 6. The grand-ducal regulation of 30th March, 1988 is abrogated effective 13th February, 2007.

Art. 7. Our Minister of the Treasury and Budget is responsible for the execution of the present regulation which will be published in the *Mémorial*.

111 *Société civile*

GRAND-DUCAL REGULATION OF 14TH APRIL, 2003 DETERMINING THE CONDITIONS AND CRITERIA FOR THE APPLICATION OF THE SUBSCRIPTION TAX REFERRED TO IN ARTICLE 129 OF THE LAW OF 20TH DECEMBER, 2002 RELATING TO UNDERTAKINGS FOR COLLECTIVE INVESTMENT

Art. 1. "Money market instruments" as referred to in the provisions of Article 129, paragraph (2), of the Law of 20th December, 2002 relating to undertakings for collective investment, means any debt securities and instruments, irrespective of whether they are transferable securities or not, including bonds, certificates of deposits, deposit receipts and all other similar instruments, provided that, at the time of their acquisition by the relevant undertaking, their initial or residual maturity does not exceed twelve months, taking into account the financial instruments connected therewith, or the terms and conditions governing those securities provide that the interest rate applicable thereto is adjusted at least annually on the basis of market conditions.

Art. 2. The *Commission de Surveillance du Secteur Financier* establishes a list of undertakings for collective investment governed by the Law of 20th December, 2002, which fulfill the conditions required to benefit from the reduced rate, for the purpose of calculating the annual subscription tax. The inscription on the appropriate list is carried out at the request of the undertakings concerned which are undertakings the exclusive object of which either is the collective investment in money market instruments and the placing of deposits with credit establishments or is the collective placing of deposits with credit establishments. This inscription is subject to the condition that the prospectus of the applying undertaking specifically indicates its investment policy.

The provisions of the preceding paragraph apply *mutatis mutandis* to the individual compartments of an undertaking for collective investment with multiple compartments.

Art. 3. In order to obtain application of the exemption from the subscription tax in respect of the value of the assets represented by units of other undertakings for collective investment which are already submitted to the subscription tax provided for by Article 129 of the Law of 20th December, 2002, the undertakings which hold such units must declare their value separately in the periodical declarations they file with the *Administration de l'Enregistrement et des Domaines.*

Art. 4. The amended grand-ducal regulation of 14th April, 1995 adopted pursuant to the amended Law of 30th March, 1988 relating to undertakings for collective investment is repealed effective 13th February, 2007.

Art. 5. Our Ministry of the Treasury and Budget is responsible for the execution of the present regulation which will be published in the *Mémorial*.

CSSF CIRCULAR 02/77 OF 27TH NOVEMBER, 2002 CONCERNING THE PROTECTION OF INVESTORS IN CASE OF NAV CALCULATION ERROR AND CORRECTION OF THE CONSEQUENCES RESULTING FROM NON-COMPLIANCE WITH THE INVESTMENT RULES APPLICABLE TO UNDERTAKINGS FOR COLLECTIVE INVESTMENT

Luxembourg, 27th November, 2002

To: All Luxembourg undertakings for collective investment and all parties involved in the operation and supervision of such undertakings

CSSF CIRCULAR 02/77

Concerns: Protection of investors in case of NAV calculation error and correction of the consequences resulting from non-compliance with the investment rules applicable to undertakings for collective investment.

Ladies and Gentlemen,

The purpose of this circular is to set out the minimum rules of conduct to be followed by collective investment professionals in Luxembourg in case of errors in the administration or management of the undertakings for collective investment ("UCIs") for which they are responsible.

Errors which occur in practice are essentially those resulting from the incorrect calculation of the net asset value ("NAV") or from non-compliance with the investment rules applicable to UCIs. In most cases, non-compliance is caused either by investments which are not in compliance with the investment policy which the UCIs define in their prospectus or because of a breach of the investment or borrowing restrictions provided for by law or their prospectus.

It is the responsibility of the UCIs' promoters to ensure that any errors are correctly dealt with in strictest compliance with the rules of conduct specified in this circular. This is of a primordial importance not only because the interests of the UCIs and/or of the investors having suffered a loss need to be protected, but it must be ensured that investors maintain their trust in the integrity of collective management professionals which exercise their activities in Luxembourg and the effectiveness of the supervision exercised over UCIs.

The corrective and compensatory actions to be taken in case of NAV calculation errors or in case of non-compliance with the investment rules applicable to UCIs are separately dealt with under sections I. and II. hereafter. That presentation is necessary to take account of the fact that this circular takes a different approach to deal with losses in each of the two situations.

This circular replaces and supersedes CSSF circular 2000/8 of 15th March, 2000.

I. The treatment of NAV calculation errors

1. Definition of a calculation error

It is reminded that the NAV per unit/share of UCIs is obtained by dividing the value of their net assets, meaning assets less liabilities, by the number of units/shares outstanding.

Unless provided differently in their constitutional documents, the valuation of the assets of UCIs, whose investment policy provides for the investment in transferable securities, must be based, in case of securities admitted to official stock exchange listing, on the last known price on such stock exchange, unless such price is not repre-

sentative. Securities which are not so listed or securities which are so listed but of which the last price is not representative, are valued on the basis of the reasonably foreseeable sale's price which must be determined prudently and in good faith.

It is presumed that the NAV is correctly calculated where the rules provided for its determination in the constitutional documents and prospectus of the UCI are strictly applied, consistently and in good faith, on the basis of the most current and most reliable information available at the time of the calculation.

An error in the NAV calculation occurs as a result of one or more factors or circumstances which cause the calculation to yield an incorrect result. Generally, these factors and circumstances are related to inadequate internal control procedures, management shortfalls, imperfections or deficiencies in the operation of the IT, accounting or communication systems as well as to non-compliance with the valuation rules provided in the constitutional documents and the prospectus of UCIs.

2. The materiality concept in the context of the NAV calculation errors

It is generally recognised that the NAV calculation process is not an exact science and that the result of the calculation constitutes the closest possible approximation of the true market value of the assets of a UCI. The level of precision with which the NAV is calculated will indeed depend on a series of external factors more or less linked to the complexity of each particular UCI such as volatility of the markets on which an important part of the assets of the UCI are invested in, the availability at the appropriate time of up-to-date information on market prices and/or other elements relevant for the calculation of the NAV as well as the reliability of the price information sources used.

In consideration of these factors, it is accepted in the majority of the principal collective management industry centres that only those calculation errors, which have a material impact on the NAV and whose proportion compared to the NAV reaches or exceeds a certain threshold, referred to as the materiality or tolerance threshold, must be notified to the CSSF and corrected in order to protect the interests of the investors concerned while it is indeed considered that in all other cases, the immateriality of the errors does not justify the recourse to relatively long and costly administration procedures which must be put into place in order to recalculate incorrect NAVs and indemnify affected investors.

Following the use and practices adopted abroad, this circular introduces the materiality concept for Luxembourg UCIs whilst determining acceptable tolerance thresholds at different levels depending on the type of UCI concerned by the NAV calculation error. This differentiating approach is justified to the extent that the implicit level of imprecision in each NAV calculation can vary from one type of UCI to the next by virtue of the external factors referred to above and in particular market volatility. That factor is indeed of a primordial importance in this context as it is generally admitted that the volatility of a market depends to a large extent on the risks associated with the financial assets dealt on that market and that such volatility increases depending on whether those assets are money market instruments, bonds/debt securities or shares and other types of securities.

In conformity with that approach, different tolerance thresholds are provided for UCIs which invest in money market instruments and/or cash assets ("money market UCIs/cash funds"), UCIs which invest in debt obligations and/or similar debt instruments ("bond UCIs"), UCIs which invest in shares and/or financial assets other than those referred to above ("equity or other financial assets' UCIs") and UCIs which follow a mixed investment policy ("mixed UCIs").

For each of these types of UCIs the tolerance threshold is specified hereunder:

money market UCIs/cash funds:	0.25% of NAV
bond UCIs:	0.50% of NAV
shares and other financial assets' UCIs:	1.00% of NAV
mixed UCIs:	0.50% of NAV.

The introduction of the materiality concept does not mean that UCI promoters will in case of calculation errors be obliged to apply the tolerance thresholds specified above. Promoters are on the contrary free to apply less high tolerance thresholds or even not apply any at all.

It is the responsibility of the governing bodies of Luxembourg UCIs whose units/shares are admitted to distribution abroad to ensure that the tolerance thresholds they propose to adopt in case of NAV calculation errors are not in conflict with the requirements that may be applicable in those circumstances in the host countries.

3. Procedures to be followed for the correction of calculation errors which have a material impact on the NAV.

The indications given under the points below relate to the principal stages of the correction process and fix in detail the rules of conduct to be followed in the correction of the calculation errors whose impact on the NAV reaches or exceeds the acceptable tolerance threshold as specified above and which are thereby considered to constitute material errors. These rules of conduct concern in particular

- the information to be furnished to the promoter and the custodian of the UCI and to the CSSF;
- the determination of the financial impact of the calculation errors;
- the indemnification of the damages which result from the calculation errors for the UCI and/or its investors;
- the implication of the external auditor in the monitoring of the correction process and
- the communications to be made to those investors which have to be indemnified.

Significant errors not only means isolated calculation errors which have a significant impact on the NAV but also unprocessed simultaneous or successive calculation errors which each remain below the acceptable tolerance threshold but which, if considered on an aggregate basis, reach or exceed that threshold.

The correction procedures must form an integral part of the internal control procedures which the head office of UCIs must put into place to limit as much as possible the risk for calculation errors and detect any errors that occur.

(a) The information to be furnished to the promoter and the custodian of the UCI and to the CSSF

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 and submit to the promoter and the CSSF a corrective action plan dealing with the steps which are proposed or have been taken to cure the problems which have caused the ascertained calculation error and to put into place the improvements to the administrative and control structures which are necessary to avoid the subsequent occurrence of the same problems.

The corrective action plan must also specify the steps which are proposed or which have been taken to

- identify in the most appropriate way the different categories of investors who are affected by the errors,
- recalculate the NAVs which have been applied to subscription and redemption requests received during the period starting on the date on which the error became significant and the date on which it was corrected ("the error period");
- determine, on the basis of the recalculated NAVs, the amounts which have to be repaid to the UCI and the amounts payable by way of indemnity to investors who have suffered a loss as result of the error;
- notify the error to the supervisory authorities of the countries in which the units/shares of the UCI are authorised for distribution, to the extent the latter so require;
- notify the error to the investors who have to be indemnified and inform them on the steps that will be put into place for indemnifying their losses.

If, following an NAV calculation error, the indemnification amount does not exceed EUR 25,000 and the amount to be reimbursed to an investor does not exceed EUR 2,500, no corrective action plan as detailed hereabove needs to be submitted to the CSSF. In that case the head office must notify the occurrence of the material calculation error to the CSSF and must quickly take the measures necessary for correcting the calculation error and for arranging the indemnification of the damages incurred as provided in items b), c), and e) hereafter.

(b) The determination of the financial impact of significant calculation errors

In case of a material calculation error, the head office of the UCI must as quickly as possible take the steps necessary to correct the error. In particular, it must recalculate the NAVs which have been determined during the error period and quantify the loss for the UCI and/or its investors on the basis of the corrected NAVs, provided however that the recalculation of incorrect NAVs is required only in case subscription or redemption requests have been processed during the error period.

In determining the financial impact of calculation errors, the head office of the UCI must fundamentally distinguish between

- investors which have joined the UCI before the error period and which have redeemed their units/shares during such period and
- investors which have joined the UCI during the error period and which continued to hold their units/shares after such a period,

provided that investors other than those belonging to the above categories may be affected depending on actual circumstances.

The indications below give an overview of the situation of the UCI and the concerned investors in the following cases:

Cases where the NAV is undervalued.

In that case,

- investors which have joined the UCI before the error period and which have redeemed their units/shares during such period, must be indemnified of the difference between the recalculated NAV and the undervalued NAV which was applied to the redeemed units/shares ;

– the UCI must be indemnified of the difference between the recalculated NAV and the undervalued NAV which has been applied to units/shares subscribed to during the error period and which remained outstanding beyond that period.

In case the NAV is overvalued.

In that case,

– the UCI must be indemnified of the difference between the overvalued NAV which was applied to units/shares redeemed during the error period but which were subscribed to before that period and the recalculated NAV;
– investors which have joined the UCI during the error period and which have held their units/shares beyond such period must be indemnified of the difference between the overvalued NAV applied to the units/shares subscribed to and the recalculated NAV.

The investors having suffered a loss as a result of a calculation error may be indemnified out of the assets of the UCI in case the payments due to the relevant investors correspond to excess sums within the assets of the UCI and the payment of which can therefore not affect the interests of the other investors. It remains nevertheless that the head office of the UCI or, as the case may be, its promoter may decide to themselves support the payments necessary to indemnify affected investors.

There is an open issue as to whether the UCI affected by a calculation error has the right to require investors who have involuntarily benefited from that error to subsequently pay to the UCI the amount not paid by them in respect of units/shares subscribed by them on the basis of an undervalued NAV or to repay the excess of the sums received by them in respect of units/shares redeemed at an overvalued NAV. Since this is a controversial issue to which no clear response can be given in the absence of a court precedent, it is not recommended to call upon the investors concerned to indemnify the UCI for its losses, unless the beneficiaries are institutional investors or other sophisticated investors who accept in full knowledge of the circumstances to cover the loss of the UCI.

In those circumstances, it is in principle the obligation of the head office of the UCI or as the case may be of its promoter, to make the payments due to the UCI in lieu of the investors who have benefited from the error. This solution is particularly justified because any claim on the investors having benefited from the error could have a negative effect on the promoter's reputation and result therefore in a non negligible commercial prejudice for the promoter.

As soon as the operations consisting in the recalculation of the incorrect NAVs and the computation of the losses resulting from the calculation error for the UCI and/or its investors have been concluded, the head office of the UCI must make the entries in the accounts of the UCI which are necessary to reflect the payments to be received and the payments to be made by the UCI.

(c) The correction of the consequences for the UCI and/or its investors of calculation errors

The compensation for damages is only compulsory by reference to the specific dates on which NAV calculation errors were significant. Insofar as other dates are concerned, it is the responsibility of the governing bodies of the UCI to determine whether it is necessary to determine the financial impact of the error and establish an indemnification plan.

The head office of the UCI must diligently put into place the measures provided for in the correction plan referred to in item a) above for the recalculation of the incorrect NAVs and the determination of the loss suffered by the UCI and/or the affected investors.

It must also act with diligence in the organisation of the indemnity payments due to the UCI and/or the affected investors, provided however that these payments can only be made after the external auditor has completed his special report referred to in item d) below.

In order to accelerate the process of calculation error correction, the head office of the UCI can initiate the different stages of that process without having obtained the prior consent of the CSSF. It suffices in that case that the CSSF is informed of the steps taken subsequently thereto.

If, following a NAV calculation error, the total indemnification amount does not exceed EUR 25,000 and the amount to be reimbursed to an investor does not exceed EUR 2,500, the head office must be diligent in operating the payment of the amounts due as indemnification to the UCI and/or to affected investors as soon as the sums payable as indemnification will have been determined.

It remains however that the CSSF can intervene in the correction process on a subsequent basis if it deems such intervention necessary in order to preserve the interests of the UCI and/or the affected investors.

In most of the main centres for collective management, UCIs are authorised by the CSSF to apply the *de minimis* rule to the amounts to which individual investors can pretend.

In accordance with that rule, the UCIs which benefit from such an authorisation may decide not to pay to individual investors sums which do not exceed a specific amount, the level of which is generally fixed as a lump sum figure, referred to as the *de minimis* amount. That lump sum figure is applied in order to avoid that investors who have a right to be paid lesser amounts, end up with no real benefit because of the bank charges (cheque collection charges for cheques issued to their order or bank transfer charges) and other costs they have to bear.

For the reasons specified in the preceding paragraph, Luxembourg UCIs can also take advantage of the *de minimis* rule. This document does however not introduce a single lump sum for the *de minimis* amount Luxembourg UCIs can apply.

It is therefore the responsibility of each UCI to determine itself, with the approval of the CSSF, the lump sum of *de minimis* amount it intends to apply provided that, in determining such lump sum, it must take into account the level of bank charges and other costs which are charged to investors to whom payments are made. This approach is justified because a large majority of Luxembourg UCIs are distributed abroad and that the level of those charges can appreciably vary between UCIs depending on the geographic location of investors.

Concerning the indemnification of investors who already hold units/shares at the moment of payment of the amounts due to them, UCIs may decide the attribution to them of new units/shares (or, as the case may be, fractions of units or shares) instead of making a payment by cheque or bank transfer. For those investors, recourse to this particular method of indemnification is even recommended since such investors then avoid the bank charges which would otherwise be charged to them and since it additionally allows a complete indemnification without any consideration being given to the actual amounts they are entitled to, as in those circumstances there is no justification to apply a *de minimis* amount.

It is clear that UCIs which issue new units/shares to indemnify affected investors may not deduct commissions or other entry costs in respect to those units/shares.

Where affected investors have subscribed units/shares through a "nominee", the head office of the UCI must remit to such "nominee" the amounts which are intended for the relevant investors. In such cases, the "nominee" must commit to the head office that it will forward the amounts received by it to the persons effectively entitled thereto.

The term "nominee" as used herein means an intermediary who intervenes between the investors and the UCI they have selected and who offers nominee services which the investors may use in the conditions set out in the prospectus of the UCI.

The *de minimis* rule can in no case be used to refuse payment to investors of amounts which are less than the *de minimis* amount applicable to such investors in case such investors expressly claim such payment.

(d) The implication of the external auditor in the monitoring of the correction process

At the same time as the head office notifies the promoter and the custodian of the UCI and the CSSF of the occurrence of a significant calculation error, the head office of the UCI must also notify the UCI's external auditor and instruct him to report on the adequacy of the method it intends to use in order to

– identify the different categories of investors affected by the error;

– recalculate the NAVs applied to subscription and redemption requests received during the error period; and

– determine, on the basis of the recalculated NAVs, the amounts which must be repaid to the UCI and the amounts payable on an indemnity basis to investors who have suffered a significant loss because of the error.

The conclusions of the external auditor on the proposed methods must be documented in writing and must be attached to the correction plan referred to in item a) above.

When the calculation error is discovered by the external auditor, the external auditor must immediately notify the head office of the UCI thereof and request it to immediately inform the promoter, the custodian and the CSSF thereof. If the external auditor realises that the head office does not comply with that request, the external auditor must notify this fact to the CSSF.

As soon as the head office of the UCI has carried out the entries in the accounts of the UCI which are necessary to correct the calculation error, the external auditor must draw up a special report in which he opines whether the correction process is appropriate and reasonable or not. This opinion must address the following:

– the methods referred to above,

– the incorrect NAVs which have been recalculated,

– the losses suffered by the UCI and/or its investors.

The head office must forward a copy of the special audit report to the CSSF as well as to the supervisory authorities of those countries in which the units/shares of the UCI are admitted for distribution, in case such authorities so request.

Finally, the external auditor must establish a confirmation in which he certifies that the amounts due on an indemnity basis to the UCI and/or affected investors have effectively been paid.

A copy of that confirmation must also be forwarded to the CSSF and, as the case may be, the foreign regulatory authorities referred to above.

In the context of an NAV calculation error for which the indemnification amount does not exceed EUR 25,000 and the amount to be reimbursed to an investor does not exceed EUR 2,500, the external auditor must review the correction process in the course of its annual audit of the UCI. The external auditor must in the report on its review state whether, in its opinion, the process of correction is or is not appropriate and reasonable. This statement must cover the following items:

– the methods referred to above;
– the incorrect NAVs which have been recalculated;
– the losses suffered by the UCI and/or its investors; and
– the payment of the amounts due as indemnification.

(e) The communications to be made to those investors which have to be indemnified

Significant calculation errors must be brought to the attention of the investors who are to be indemnified.

If applicable, the communications which are made for that purpose through individual notices and/or by publication in the press must *inter alia* include particulars on the calculation error and the steps taken to correct it and to indemnify the UCI and/or the affected investors accordingly.

These communications must be submitted in draft form to the CSSF and, as the case may be, the supervisory authorities of those countries in which the units/shares of the UCI are admitted for distribution, in case such authorities so request.

4. Responsibility for the costs resulting from the correction operations of a calculation error

The costs caused by the correction operations of a calculation error, including the costs associated with the intervention of the external auditor, cannot be charged to the assets of the UCI. These costs must be fully supported by the head office of the UCI, failing which, by the promoter of the UCI, in each case irrespective of the impact of the error on the NAV.

The external auditor will be responsible to ascertain within the framework of the audit of the accounting information contained in the annual reports of the UCI that the costs referred to herein will not be charged to the UCI.

II. The compensation of the consequences resulting from non-compliance with the investment rules applicable to UCIs

Promptly upon discovering a non-compliance with investment rules, the directors[112] of the UCI concerned must take the steps which are necessary to regularise the situation of the UCI caused by such non-compliance.

112 The original circular uses the term "*dirigeant*" which includes directors, managers and officers.

In case the ascertained non-compliance results from investments which do not comply with the investment policy defined in the prospectus, the UCI must realise those investments.

In case the investment restrictions provided for by law or by the prospectus are breached in circumstances other than those referred to in Article 46 of the Law of 30th March, 1988 concerning undertakings for collective investment, the UCI must realise the excess positions.

Where the borrowing limits provided for by law or by the prospectus are breached, the UCI must reduce its borrowings to the authorised limit.

In the three circumstances referred to above, the UCI must be indemnified to the extent of any damage suffered.

In the first two circumstances, the damage must be determined in principle by reference to the loss of the UCI resulting from the realisation of the non-authorised investments. In the third circumstance, the UCI must in principle be indemnified to the extent of its interest and other charges resulting from the non-authorised portion of the borrowings.

In the presence of a number of simultaneous breaches of investment rules, the indemnity, if any, is to be calculated in respect of the net result of the corrective actions concerning all the breaches.

In case the corrective actions have a net positive result for the UCI, it will retain the benefit thereof. In those circumstances, it suffices for the head office of the UCI to notify the CSSF and the external auditor.

By exception to the preceding principle and to the extent there is adequate justification therefor, methods other than those described above may be used to determine the suffered damage including in particular the method which 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 the investment restrictions provided for by law or the prospectus.

The tolerance levels which are provided for NAV calculation errors cannot be applied to damages of UCIs resulting from non-compliance with investment rules.

Because they did not comply with their obligations it is the responsibility of the persons who have caused the losses to ensure that such losses are repaid. In case this principle cannot be applied, the promoters will have to indemnify.

The principles which determine the procedures to be followed for the processing of NAV calculation errors and the treatment of NAV calculation errors for which the total indemnification amount does not exceed EUR 25,000 and the indemnification amount to be paid to one investor does not exceed EUR 2,500 will apply *mutatis mutandis* in all cases where a UCI suffers a loss as a result of non-compliance with investment rules. The principles referred to herein which have to be applied are in particular those concerning

- the information to be furnished to the promoter and the custodian of the UCI and to the CSSF;
- the identification of the categories of investors which are affected because of the loss suffered by the UCI;
- the determination of the financial impact of the loss for individual investors and the measures to be taken for their indemnification;
- the implication of the independent auditor in the monitoring of the correction process;
- the communications to be made to those investors which have to be indemnified.

As regards the procedures for indemnifying investors, the rules set out in Section I. 3. (c) of this circular will apply.

III. Final Provisions

1. Repealment provision

CSSF circular 2000/8 is repealed.

2. Entry into force

The provisions of this circular are immediately applicable in their entirety.

CSSF CIRCULAR 02/80 OF 5TH DECEMBER, 2002 CONCERNING THE SPECIFIC RULES APPLICABLE TO LUXEMBOURG UNDERTAKINGS FOR COLLECTIVE INVESTMENT ("UCIS") PURSUING ALTERNATIVE INVESTMENT STRATEGIES

Luxembourg, 5th December, 2002

To all persons and companies supervised by the CSSF

CSSF CIRCULAR 02/80

Concerns: Specific rules applicable to Luxembourg undertakings for collective investment ("UCIs") pursuing alternative investment strategies.

Ladies and Gentlemen,

Preamble

The Law of 30th March, 1988 relating to UCIs does not comprise any provisions regarding restrictions applicable to UCIs governed by Part II of such law. Such restrictions are set out in the IML Circular 91/75 of 21st January, 1991 applicable to UCIs. However, the UCIs who adopt alternative investment strategies are not specifically covered by the provisions of the above-mentioned circular. Therefore, in the past, the investment restrictions applicable to UCIs pursuing so called alternative investment strategies were dealt with by the Commission for the Supervision of the Financial Sector ("CSSF") on a case-by-case basis.

Considering the increasing number of applications for the creation and authorisation of Luxembourg UCIs which pursue investment strategies akin to those pursued by "hedge funds"[113] or "alternative investment funds"[113], the CSSF intends to clarify the legal and regulatory framework applicable to such UCIs.

This circular is issued in the context of the existing legal framework and its purpose is to clarify the specific rules applicable to Luxembourg UCIs which pursue so-called alternative investment strategies. In this context and due to the high investment risks which the investment strategies pursued by the UCIs concerned by this circular may entail, the CSSF will pay attention to the reputation, experience and financial standing of the promoters of such UCIs. Moreover, the CSSF considers that the professional qualification and the experience of the directors[114] of the management bodies, and, if applicable, of the investment managers and the investment advisers are particularly important in relation to such UCIs.

For the avoidance of doubt, it is to be understood that the rules laid down in Chapter I of IML Circular 91/75 of 21st January, 1991 applicable to UCIs other than UCITS and providing for specific rules for three types of specialised UCIs remain unchanged. Such rules are not applicable to UCIs concerned by this circular. UCIs which pursue so-called alternative investment strategies are subject to Part II of the Law of 30th March, 1988 relating to UCI as the rules set forth in Chapter 5 of such law are not appropriate for such UCIs.

Although these UCIs have no obligation to borrow, their investment policy may provide for the possibility to borrow on a permanent basis for investment purposes.

Such UCIs have to comply with the provisions of this circular. However, the CSSF may grant derogations from the provisions set forth hereafter on the basis of an appropriate justification or impose additional investment restrictions.

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113 In English in the French text.

114 The French version of this circular uses the term "*dirigeant*" which term includes directors, managers and officers.

A. Risk diversification rules regarding short sales

A.1. Short sales may, in principle, not result in the UCI holding:

a) a short position on transferable securities which are not admitted to official stock exchange listing or dealt in on another regulated market, which operates regularly and is recognised and open to the public. However the UCI may hold short positions on transferable securities which are not quoted or not dealt in on a regulated market if such securities are highly liquid and do not represent more than 10% of the assets of the UCI;

b) a short position on transferable securities which represent more than 10% of the securities of the same type issued by the same issuer;

c) a short position on transferable securities of the same issuer, (i) if the sum of the prices at which the short sales have been carried out represents more than 10% of the assets of the UCI or (ii) if the short position represents a commitment exceeding 5% of the assets.

A.2. The commitments arising from short sales on transferable securities at a given time correspond to the cumulative non-realised losses resulting, at that time, from the short sales made by the UCI. The non-realised loss resulting from a short sale is the positive amount resulting from the difference between the market price at which the short position can be covered and the price at which the relevant transferable security has been sold short.

A.3. The aggregate commitments of the UCI resulting from short sales may at no time exceed 50% of the assets of the UCI. If the UCI enters into short sales transactions, it must hold sufficient assets enabling it at any time to close the open positions resulting from such short sales.

A.4. The short sales of transferable securities for which the UCI holds adequate coverage are not to be considered in the calculation of the total commitments referred to above. For the avoidance of doubt, it is to be noted that the fact for a UCI to grant a security, of whatever nature, on its assets to third parties in order to secure its obligations towards such third parties, is not to be considered as adequate coverage for the UCI's commitments.

A.5. In connection with short sales on transferable securities, UCIs are authorised to enter, as borrower, into securities lending transactions with first class professionals specialised in this type of transactions. The counterparty risk resulting from the difference between (i) the value of the assets transferred by a UCI to a lender as security in the context of the securities lending transactions and (ii) the debt of the UCI owed to such lender may not exceed 20% of the assets of the UCI. For the avoidance of doubt, it is to be noted that UCIs may, in addition, give security by using security arrangements which do not result in a transfer of ownership or which limit the counter-party risk by other means.

B. Borrowings

UCIs concerned by this circular may borrow permanently and for investment purposes from first class professionals specialised in this type of transaction.

Such borrowings are limited to 200% of the net assets of the UCI. Consequently, the value of the assets of the UCI may not exceed 300% of its net assets. UCIs pursuing a strategy with a high level of correlation between long positions and short positions are authorised to borrow up to 400% of their net assets.

The counterparty risk resulting from the difference between (i) the value of the assets transferred by the UCI to a lender as security in the context of borrowing transactions and (ii) the debt of the UCI owed to such lender may not exceed 20% of the assets of the UCI. For the avoidance of doubt, it is to be noted that UCIs may, in addition, give security by using security arrangements which do not result in a transfer of ownership or which limit the counterparty risk by other means.

The counterparty risk resulting from the sum of (i) the difference between the value of the assets transferred as security in the context of securities lending transactions and the amounts due referred to under item A.5 above and (ii) the difference between the assets transferred as security and the amounts borrowed referred to above may not, in respect of a single lender, exceed 20% of the assets of the UCI.

C. Restrictions applicable to investments in UCIs ("target UCIs")

The UCIs referred to in this circular may, in principle, not invest more than 20% of their net assets in securities issued by the same target UCI. For the purpose of the application of this 20% limit, each compartment of a target UCI with multiple compartments is to be considered as a distinct target UCI provided that the principle of segregation of the commitments of the different compartments vis-à-vis third parties is ensured. The UCI may hold more than 50% of the units of a target UCI provided that, if the target UCI is a UCI with multiple compartments, the investment of the UCI concerned by this circular in the legal entity constituting the target UCI must represent less than 50% of the net assets of the UCI concerned by this circular.

These restrictions are not applicable to the acquisition of units of open-ended target UCIs if such target UCIs are subject to risk diversification requirements comparable to those applicable to UCIs which are subject to part II of the Law of 30th March, 1988 and if such target UCIs are subject in their home country to a permanent supervision by a supervisory authority set up by law in order to ensure the protection of investors. This derogation may not result in an excessive concentration of the investments of the UCI in one single target UCI provided that for the purpose of this limitation, each compartment of a target UCI with multiple compartments is to be considered as a distinct target UCI on the condition that the principle of segregation of the commitments of the different compartments towards third parties is ensured.

UCIs which principally invest in other UCIs must make sure that their portfolio of target UCIs presents appropriate liquidity features to enable the UCIs to meet their obligation to redeem its shares. Their investment policy must comprise an appropriate description in that respect.

D. Additional Investment Restrictions

UCIs concerned by this circular shall, in principle, not:

a) invest more than 10% of their assets in transferable securities which are not admitted to official listing on a stock exchange or dealt in on another regulated market, which operates regularly and is recognised and open to the public,

b) acquire more than 10% of the securities of the same kind issued by the same issuer,

c) invest more than 20% of their assets in securities issued by the same issuer.

The restrictions set forth under a), b) and c) above are not applicable to securities issued or guaranteed by a member State of the OECD or its local authorities or by public international bodies with EU, regional or worldwide scope.

The restrictions set forth under a), b) and c) above are not applicable to units or shares issued by target UCIs. The restrictions set forth in section C. above are applicable to investments in target UCIs.

E. Use of derivative financial instruments and other techniques

The UCIs concerned by this circular are authorised to employ derivative financial instruments and use the techniques specified hereafter.

These derivative financial instruments may, amongst others, include options, financial futures and related options as well as swap contracts by private agreement on any type of financial instruments. In addition, such UCIs may employ techniques consisting in securities lending transactions as well as in sales with right of repurchase transactions and repurchase transactions[115]. UCIs which employ such derivative financial instruments and techniques must state in their prospectus the total leverage which may not be exceeded and include in their prospectus a description of the risks arising from the transactions which they intend to pursue. The derivative financial instruments must be dealt in on an organised market or contracted by private agreement with first class professionals specialised in this type of transactions.

The aggregate commitments resulting from short sales of transferable securities together with the commitments resulting from financial derivative instruments entered into by private agreement and, if applicable, the commitments resulting from financial derivative instruments dealt in on an organised market may not at any time exceed the value of the assets of the UCI.

E. 1. Restrictions relating to derivative financial instruments

1. Margin deposits in relation to derivative financial instruments dealt on an organised market as well as the commitments arising from derivative financial instruments contracted by private agreement may not exceed 50% of the assets of the UCI. The reserve of liquid assets of such UCIs must represent an amount at least equal to the margin deposits made by the UCI. Liquid assets do not only comprise time deposits and regularly negotiated money market instruments the remaining maturity of which is less than 12 months, but also treasury bills and bonds issued by Member States of the OECD or their local authorities or by public international bodies with EU, regional or worldwide scope as well as bonds admitted to official listing on a stock exchange or dealt in on a regulated market, which operates regularly and is open to the public, issued by first class issuers and which are highly liquid.
2. The UCI may not borrow to finance margin deposits.
3. The UCI may not enter into contracts relating to commodities other than commodity futures contracts. However, the UCI may acquire, for cash consideration, precious metals which are negotiable on an organised market.
4. The premiums paid for the acquisition of options outstanding are included in the calculation of the 50% limit referred to under item 1. above.
5. The UCI must ensure an adequate spread of investment risks by sufficient diversification.

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115 The French text refers to "*opérations à réméré*" and *"opérations de mise en pension*". For the distinction between the two, see the description under E.3. below.

6. The UCI may not hold an open position in anyone single contract relating to a derivative financial instrument dealt in on an organised market or in a single contract relating to a derivative financial instrument entered into by private agreement for which the required margin or the commitment taken, respectively, represents 5% or more of its assets.
7. Premiums paid to acquire options outstanding having identical characteristics may not exceed 5% of the assets.
8. The UCI may not hold an open position in derivative financial instruments relating to a single commodity or a single category of financial futures for which the required margin (in relation to derivative financial instruments dealt in on an organised market) as well as the commitment (in relation to derivative financial instruments entered into by private agreement) represent 20% or more of the assets.
9. The commitment in relation to a transaction on a derivative financial instrument entered into by private agreement by the UCI corresponds to the non-realised loss resulting, at that time, from the relevant transaction.

E. 2. Securities lending transactions

The UCI may enter into securities lending transactions in accordance with the provisions set forth in IML Circular 91/75. However, the limitation that securities lending transactions may not extend beyond a period of 30 days is not applicable where the UCI has the right, at any time, to terminate the lending transaction and obtain the restitution of the securities lent.

E. 3. Sale with right of repurchase transactions *(opérations à réméré)* and repurchase transactions *(opérations de mise en pension)*.

The UCI may enter into sale with right of repurchase transactions[116] which consist in the purchase and sale of securities where the terms reserve the right to the seller to repurchase the securities from the buyer at a price and at a time agreed between the two parties at the time when the contract is entered into. The UCI can also enter into repurchase transactions[117] which consist in transactions where, at maturity, the seller has the obligation to take back the asset sold whereas the original buyer either has a right or an obligation to return the asset sold.

The UCI can either act as buyer or as seller in the context of the aforementioned transactions. Its participation in the relevant transactions is however subject to the following rules:

1. Rules to bring the transactions to a successful conclusion

   The UCI may participate in sale with right of repurchase transactions or repurchase transactions only if the counterparties in such transactions are first class professionals specialised in this type of transactions.

2. Conditions and limits of these transactions

   During the duration of a sale with right of repurchase agreement where the UCI acts as purchaser, it may not sell the securities which are the subject of the contract before the counterparty has exercised its right to repurchase the securities or until the deadline for the repurchase has expired, unless the UCI has other means of

116 opérations à réméré

117 opérations de mise en pension

coverage. If the UCI is open for redemption, it must ensure that the value of such transactions is kept at a level such that it is at all time able to meet its redemption obligation. The same conditions are applicable in the case of a repurchase transaction on the basis of a purchase and firm re-sale agreement where the UCI acts as purchaser (transferee).

Where the UCI acts as seller (transferor) in a repurchase transaction, the UCI may not, during the whole duration of the repo, transfer the title to the security under the repo or pledge them to a third party, or repo them a second time, in whatever form. The UCI must at the maturity of the repurchase transactions hold sufficient assets to pay, if appropriate, the agreed upon repurchase price payable to the transferee.

3. Periodical information of the public

In its financial reports, the UCI must separately, for its sale with right of repurchase transactions and for its repurchase transactions, indicate the total amount of the open transactions at the date as of which the relevant reports indicate are issued.

F. Breach of investment limits otherwise than by investment decisions

If the percentage limits referred to above are exceeded for reasons other than investment decisions (market fluctuations, redemptions), the priority objective of the UCI must be to remedy the situation, taking due account of the interests of the investors.

G. Management and supervisory bodies

Concerning their professional qualification, the directors[118] of the management bodies and, if applicable, the investment managers and investment advisers, must have a confirmed experience in the area of the proposed investment policy.

H. Specific rules

H.1. The issue prospectus must contain a description of the investment strategy of the UCI concerned as well as a description of the specific risks inherent to its investment policy. The prospectus must, if applicable, provide that:

- the potential losses resulting from unsecured sales on transferable securities differ from the possible losses resulting from the investment of liquid assets in such transferable securities. In the first case, the loss may be unlimited whereas, in the second case, the loss is limited to the amount of liquid assets invested in the transferable securities concerned;
- leverage generates an opportunity for higher return and therefore more important income, but, at the same time, increases the volatility of the value of the assets of the UCI and, hence, the risk to lose capital. Borrowings generate interest costs which may be higher than the income and capital gains produced by the assets of the UCI;
- due to the limited liquidity of the assets of the UCI, it may not be in a position to meet the redemption requests of its units which may be presented to it by its investors.

118 See footnote 114.

H.2. In addition, the prospectus must state that the investment in the relevant UCI entails an above-average risk and is only appropriate for persons who can take the risk to lose their entire investment. If appropriate, the issue prospectus must contain a description of the investment strategy in futures and options pursued by the UCI as well as the investment risks resulting from the investment policy. It must for example be mentioned that the futures and options markets are extremely volatile and that the risk to incur a loss in relation to such markets and/or in relation to uncovered sales is very high.

CSSF CIRCULAR 02/81 OF 6TH DECEMBER, 2002 CONCERNING THE GUIDELINES CONCERNING THE TASK OF AUDITORS OF UNDERTAKINGS FOR COLLECTIVE INVESTMENT

Luxembourg, 6th December, 2002

To all Luxembourg undertakings for collective investment

CSSF CIRCULAR 02/81

Concerns: Guidelines concerning the task of auditors of undertakings for collective investment.

Ladies and Gentlemen,

The purpose of this circular it to set out the rules concerning the scope of the audit of the annual accounting documents and the content of the audit reports to be drawn up in this context, pursuant to the Law of 30th March, 1988 relating to undertakings for collective investment ("UCIs"), as amended by the Law of 17th July, 2000.

This circular intends to define the role and task of the auditor in the context of the audit of the accounting documents provided for by law. The task of the auditor is not limited to the audit of the accounting documents but also covers the analysis of the operation and procedures of the UCI.

It is understood that the task of the auditor may vary depending on the risks existing in the markets in which the UCI is active and the quality of the control mechanisms implemented at the level of the UCI.

This circular does not amend the contents of the reports on the annual accounts to be established pursuant to Schedule B as provided for by the law, but aims to specify the subjects which need to be developed in the long form report[119] because that report constitutes, together with the report on the annual accounts and the management letter, an important source of information for the CSSF in the performance of its supervisory functions.

119 The circular uses the term "report on the audit of the activities of the UCI" but the term used in the industry is "long form report" and that term will be used in this translation.

Repealed by the Law of 13 February 2007

CONTENTS

I. Mandate

The auditor is appointed by the general meeting of shareholders of the UCI. For common funds, the auditor is appointed by the board of directors of the management company. The board of directors of the UCI or of the management company of the UCI must subsequently specify in writing to the auditor the terms of engagement which shall contain at least the following provisions:

1. The audit of the annual accounts has to be undertaken in accordance with the working recommendations of the Luxembourg Auditors' Institute[120]. In this context, the IRE provides for the application of the International Standards on Auditing (ISAs) published by IFAC ("International Federation of Accountants"), adapted or completed, if needed, by national legislation or practice.
2. The audit has to cover all categories of operations of the UCI whether these operations are accounted for on the balance sheet or are recorded off-balance sheet. The mandate given to the auditor cannot exclude from its scope a category of operations or a specific operation. The audit must also cover all risks incurred by the UCI.
3. The audit must cover all aspects of the organisation and verification of the procedures which apply to the UCI. The analysis must *inter alia* cover the procedures concerning compliance with the investment restrictions, control of the calculation of the NAV and reconciliations as well as the procedures relating to the valuation methods. The audit must indeed enable all information to be provided which is required for the report on the annual accounts and the long form report.
4. The mandate for the annual audit must specifically include the following tasks:
   – to check compliance with the principles established by the circulars of the supervisory authority concerning the fight against money laundering, including in particular circular IML 94/112 concerning the fight against money laundering and the prevention of the use of the financial sector for money laundering purposes and its supplements, circulars BCL 98/153, CSSF 00/21, CSSF 01/40 and CSSF 02/78, as well as the correct application of internal procedures for the prevention of money laundering;
   – to check compliance with all other circulars applicable to UCIs.
5. The audit of the annual accounts as defined hereabove has to be documented on the one hand by a report on the annual accounts (see Chapter II. hereunder) and on the other hand by a long form report (see Chapter III. hereunder).

   In general, the UCI must immediately inform the CSSF in case the auditor resigns from its mandate before the end of the term or if the auditor envisages not to seek a re-appointment.

   In the same way, the UCI must notify the CSSF, with an indication of the reasons, of its intention to terminate the appointment of the auditor. The CSSF will in respect of each request for replacement of the auditor analyse the reasons for the proposed change and will assess if the UCI has, in the procedure for the appointment of a new auditor, given due regard to the competence and resources of the latter in view of the type and volume of the activities of the UCI.

II. Report on the annual accounts

The report on the annual accounts contains the auditor's attestation *(attestation du réviseur d'entreprises, Bestätigungsvermerk*) and is to be published in accordance with Article 85 (1) of the Law of 30th March, 1988 relating to undertakings for collective investment.

120 Institut des Réviseurs d'Entreprises luxembourgeois (IRE)

In the report on the annual accounts, the auditor issues its attestation in accordance with the ISA 700[121] standards as adopted by IRE.

In accordance with Article 86 (2) of the Law of 30th March, 1988 relating to UCIs, the report on the annual accounts has to contain a balance sheet or a statement of assets and liabilities, a detailed income and expenditure account for the financial year, a report on the activities of the financial year and the other information provided for in Schedule B annexed to the prementioned law, as well as any significant information which will enable investors to make an informed judgement on the development of the activities and the results of the UCI.

In case the auditor announces to the UCI that it will issue a qualified attestation or that it will refuse to certify the accounts, the UCI concerned must immediately inform the CSSF (see also Chapter IV. "Reporting to the CSSF pursuant to Article 89 (3) of the law relating to UCIs" hereunder).

The report on the annual accounts has in any case to be submitted to the CSSF within a period of four months from the end of the period to which such report relates.

III. Long Form Report

A. General principles

The purpose of the long form report is to report on the findings of the auditor in the course of its audit concerning the financial and organisational aspects of the UCI comprising *inter alia* its relationship with the head office, the custodian and the other intermediaries (the investment managers, the transfer agents, the distributors, etc.).

The long form report must be concise, clear and critical.

It is not intended to be made available to the public. It is issued for the exclusive use by the board of directors of the UCI or the management company of the UCI as well as the CSSF.

It must detail for every item listed under III.B., the verifications which are essential to permit a precise and informed judgement on the organisation and the financial statements of the UCI.

The auditor must, in the context of its usual audits carried out in accordance with recommendations RRC n° 21[122] of IRE, give its opinion on the compliance with the investment restrictions set out by law and/or regulations and must also obtain the assurance that the systems which have been put into place permit a proper calculation of the net asset value.

The auditor has to indicate the NAV calculation errors and the infringements to the investment restrictions which it will have ascertained during its audit and which have nevertheless not been notified to the CSSF in accordance with CSSF circular 02/77.

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121 International Standard on Auditing n° 700: The Auditor's report on financial statements (footnote appearing in the circular as footnote 1).

122 Recommendation on accounting audit n° 21: The audit of the financial statements of the UCIs (footnote appearing in the circular as footnote 2).

In the long form report, the auditor must also analyse the NAV calculation errors or the failures to comply with investment rules which have been the subject of a notification in application of CSSF circular 02/77, but for which the amount of indemnification did not exceed EUR 25,000 and for which the amount to be reimbursed to any one shareholder did not exceed EUR 2,500 as set out in CSSF circular 02/77.

The auditor has to communicate in detail the weaknesses and the areas to be improved which it will have ascertained during its audit. This communication can be made in the context of the long form report or through a letter of recommendation[123] addressed to the board of directors of the UCI or the management company of the UCI. The findings of the auditor must mandatorily be supplemented by comments of the board of directors of the UCI or the management company of the UCI. In case a management letter is drawn up, it must be annexed to the long form report. If the auditor does not issue a management letter, this must be expressly noted in the long form report.

In accordance with Chapter P of circular IML 91/75 of 21st January, 1991[124], the UCI must immediately communicate to the CSSF, without having been invited to do so, all other documents issued by the auditor in the context of its annual audit as referred to hereabove.

The long form report has to be remitted to the CSSF within a period of four months from the end of the period to which the report refers.

B. Structure of the long form report

The long form report must be drawn up in accordance with the lay out featured below. The layout corresponds to the minimum information to be detailed by the auditor in its report. However, the layout of the report can be adapted to the volume and the complexity of the activity and to the structure of the UCI. If appropriate, the auditor will have to supplement the layout set out below by those items which it will find necessary. If one particular item of the layout does not apply to a UCI, the auditor will have to explicitly mention this fact under the item concerned.

1. Organisation of the UCI
   - 1.1. Head office
     - 1.1.1. Situation where the auditor of the UCI relies on the audit report of the auditor of the central administration
     - 1.1.2. Situation where the audit and verifications are made by the auditor of the UCI
       - 1.1.2.1. Assessment of procedures
       - 1.1.2.2. Computer systems
   - 1.2. Custodian
     - 1.2.1. Situation where the auditor of the UCI relies on the audit report of the auditor of the custodian

123 commonly referred to as a “management letter”.

124 Circular IML 91/75 relating to the revision and remodeling of the rules to which undertakings for collective investment governed by the Law of 30th March, 1988 on undertakings for collective investment are subject to. (This footnote appears as footnote 3 in the circular.)

1.2.2. Situation where the audit and verifications are made by the auditor of the UCI

1.2.2.1. Assessment of procedures

1.2.2.2. Computer systems

1.2.2.3. Result of the reconciliations

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1.4. Relationship with other intermediaries

2. Audit of the operations of the UCI

2.1. Control of anti-money laundering rules

2.2. Valuation methods

2.3. Audit of the risk management system

2.4. Specific audits

2.5. Assets and liabilities and profit and loss account

2.6. Publication of the NAV

3. Internet

4. Complaints from investors

5. Follow-up on problems identified in preceding long form reports

6. General conclusion

C. Explanatory comments on the structure of the long form report

1. Organisation of the UCI

The operations of a UCI require the recourse to specialised service providers in Luxembourg and abroad.

Under the provisions of the Law of 30th March, 1988 relating to undertakings for collective investment (as amended), the head office of the UCI must be located in Luxembourg. The prementioned law also provides that the custodian of a UCI must be established in Luxembourg. The entities which exercise one or several functions in relation with the head office and/or the custody for the UCI play a significant role in the operation of a UCI.

To the extent that the custodian and the professional of the financial sector which carries out the head office duties for the UCI have been subjected by their auditor to an audit on the activities exercised for UCIs which covers at least the items detailed under paragraphs 1.1.2. and 1.2.2. herebelow, the auditor of the UCI may refer to the long form reports of the auditor of the custodian or the professional of the financial sector on dealing with the services provided to undertakings for collective investment.

In case the auditor of the UCI does not make use of that possibility and considering the important role in the organisation of the UCI assumed by the entities which carry out the function of head office and/or custodian, the auditor must itself undertake the verifications and controls detailed in the pre-mentioned paragraphs. In that case the auditor of the UCI will have to advise the board of directors of the UCI or the management company of the UCI that it needs to have access to certain information on the entity concerned in order to carry out the verifications

and audits required by this circular. The board of directors of the UCI or of the management company of the UCI must in that case request the entity concerned to provide access to the information which is necessary for the auditor of the UCI to accomplish its mission.

For common funds the management of which is performed by a management company, the auditor of the UCI will have to carry out certain audits and verifications as defined under paragraph 1.3. hereafter. The auditor of the UCI may for these tasks refer to the long form report of the auditor of the management company if such report covers at least the items detailed under paragraph 1.3. In case it does not make use of that possibility, it must call upon the board of directors of the management company of the common fund. The board of directors of the management company must then make available to the auditor all information necessary in relation to the activities exercised by the management company for the common fund and, in case the management company has delegated certain important administration functions to a specialised entity, the board will have to request that entity to provide access to the information required.

It also must be noted, that in case the various head office functions are performed by more than one professional of the financial sector, the auditor of the UCI must give its opinion on the procedures regarding the coordination and general supervision of the activities of the UCI.

In respect of the relationship of the UCI with other service providers established in Luxembourg and/or abroad, reference is made to paragraph 1.4. below.

1.1. Head office

1.1.1. *Situation where the auditor of the UCI relies on the audit report of the auditor of the head office*

The auditor of the UCI must, in its long form report, specify the audit report of the auditor of the head office he has relied upon. He must in this context provide the following data:

- the name of the auditor of the head office
- the date of the audit report
- if applicable, the audit report in accordance with international standard ISA 402, type B or in accordance with US standard SAS 70, type 2, or in accordance with any other equivalent standard, as well as the name of the auditor which has established that report.

In cases where the head office functions are fulfilled by more than one entity, the auditor of the UCI has to indicate in its long form report the data mentioned hereabove in respect of each of these entities individually.

1.1.2. *Situation where the audit and verifications are made by the auditor of the UCI*

1.1.2.1. Assessment of procedures

In its long form report, the auditor must indicate the exact functions performed by the head office on behalf of the UCI. In case these functions are split among more than one professional of the financial sector and/or

management body of the fund, the auditor must in its report indicate the allocation of the tasks between the different parties.

The auditor must specify if the head office or the different parties are in possession of a procedures manual describing the functions which they perform on behalf of the UCI and which are, *inter alia*, set forth in Chapter D. of IML Circular 91/75.

In addition, the auditor has to verify if specific procedures have been established in connection with the following items:

a) internal control procedure on the origin of funds (anti-money laundering procedures),

b) valuation procedure of the portfolio by the accounting agent, distinguishing between the different types of investment and insisting in particular on unquoted and illiquid securities,

c) internal control procedures on the investment policy and restrictions,

d) internal control procedure on the accuracy of the NAV calculation,

e) recording and settlement procedure of subscription/redemption orders of units/shares,

f) validation and recording procedure in relation to the acquisition and sale of securities.

The auditor must give its opinion on the adequacy of the procedures put in place.

Finally, the auditor must indicate if the human resources made available are sufficient to ensure a proper execution of the contractual obligations of the entity for the relevant UCI.

In case of splitting of the head office functions, it goes without saying that, in addition, the auditor must give its opinion on the procedures regarding the coordination and the general supervision of the activities of the UCI.

1.1.2.2. Computer systems

As regards computer systems, the auditor will give a brief description of the software used by the head office and of the functions for which the software is used.

The auditor must indicate whether, during the financial year under review, significant changes have occurred with respect to the computer system and whether problems were encountered at the time of migration from one system to another.

The auditor must also give its opinion on the adequacy of the computer system in consideration of the volume of the activities of the relevant UCI and, if applicable, in respect of pooling or co-management techniques.

With regard to the accounting system for the calculation of the NAV, the auditor will give its opinion on whether the accounting system is adequate in view of the type of investments made by the UCI. Manual accounting operations and valuations and the internal control procedures relating thereto must be pointed out.

The auditor must also verify if appropriate measures to safeguard the confidentiality of information have been put into place.

In addition, the auditor must outline the general principles of the contingency plan in place which should permit the head office to operate normally in case of a breakdown of its computer systems, including its Internet connections.

When use is made of an external processing unit, whether based in Luxembourg or abroad, the auditor must clearly indicate which functions have been sub-delegated and to whom.

The auditor must furthermore give its opinion on compliance with the provisions of item III.1. of Chapter D. of IML Circular 91/75.

Generally, the auditor must highlight the significant deficiencies which it will have detected during its audit and must describe them in a detailed manner so that the CSSF can assess the situation.

1.2. Custodian

1.2.1. *Situation where the auditor of the UCI relies on the audit report of the auditor of the custodian*

The auditor of the UCI must in its long form report, specify the audit report of the auditor of the custodian he has relied upon. He must in this context provide the following data:

- the name of the auditor of the custodian
- the date of the audit report
- if applicable, the audit report in accordance with international standard ISA 402, type B, or in accordance with US standard SAS 70, type 2 or in accordance with any other equivalent standard, as well as the name of the auditor which has established the report.

The auditor of the UCI must in any case give its opinion on the result of the reconciliations between assets accounted for by the UCI and the assets deposited with the custodian as well as on the off-balance sheet operations of the UCI.

In case the auditor, during its audit, notes serious problems at the level of the reconciliation between the positions accounted for by the UCI and those registered with the custodian, it must make a detailed description of those problems in the long form report.

1.2.2. *Situation where the controls and verifications are made by the auditor of the UCI*

1.2.2.1. Assessment of procedures

The long form report indicates if the entity is in possession of a procedures manual describing the duties of the custodian and whether this manual includes general procedures and specific procedures relating to the activities undertaken.

The long form report will describe in particular the correspondent bank network. The long form report will describe the policy of the entity as

regards the selection criteria of those counterparties. The auditor will give an outline of the third parties with which the entity has entered into a relationship and it will indicate if these counterparties have been retained in accordance with the policy of the entity.

In case the custodian exercises also part or all of the head office functions, the long form report has to provide explanations on the separation of duties, specifically between custody and head office duties.

In case the auditor notes deficiencies, the auditor will have to indicate exactly which obligation(s) the custodian has not complied with.

1.2.2.2. Computer Systems

As regards computer systems, the auditor will give a brief description of the software used by the custodian.

The auditor must indicate whether, during the financial year under review, significant changes have occurred with regard to the computer system and whether problems were encountered at the time of migration from one system to another.

The auditor must give its opinion on the adequacy of the computer system and the available human resources for ensuring the proper execution by the credit institution of its contractual obligations towards the UCI concerned.

1.2.2.3. Result of the reconciliations

The auditor must indicate whether the custodian has established procedures concerning the reconciliation of positions accounted for by the UCI and those registered with the custodian. It will also give an opinion on the adequacy of those procedures.

The auditor must give its opinion on the results of the reconciliation between the positions accounted for by the UCI and the positions registered with the custodian.

In case the auditor would during its audit identify serious problems as regards the reconciliation between the positions accounted for by the UCI and those registered with the custodian, the auditor must give a detailed description of the problems in the long form report.

1.3. Relationship with the management company

The auditor verifies whether the management company assumes its functions in compliance with legal and contractual obligations.

It indicates in its long form report which functions are performed by the management company on behalf of the UCI. To the extent that the management company performs all or part of the administration functions, the auditor has to proceed as provided for under item 1., paragraph 1.1.1. or 1.1.2. hereabove.

In case the auditor becomes aware of major problems, it has to provide a detailed description of those problems in the long form report of the UCI.

1.4. Relationship with other intermediaries

In the context of the relationship of the UCI with other intermediaries, comprising *inter alia* the investment managers, the distributors, etc., the auditor must indicate in its long form report if the activity of the UCI has been hindered by major problems encountered in the course of the operations conducted with these other intermediaries.

If this is the case, the auditor must describe in a detailed manner the problem(s) encountered during its analysis in order to enable the CSSF to assess the situation.

2. Audit of the operations of the UCI

2.1. Audit of anti-money laundering rules

As the head office of a UCI deals with subscription, redemption and transfer requests of units or shares of UCIs, it has to ensure compliance with the provisions set forth in the circulars relating to the fight against money laundering, comprising circulars IML 94/112, BCL 98/153, CSSF 00/21, CSSF 01/40 and CSSF 02/78.

IML circular 94/112 has however taken into account the specific manner in which UCIs are marketed, by dispensing the head office of a UCI in Luxembourg under certain conditions from the obligation to carry out itself the identification of investors in case it makes use of professionals of the financial sector subject to identification obligations equivalent to those provided for by Luxembourg law. In this context, it has to be reminded that in respect of all intermediaries participating in the placement of the units or shares of UCIs, the head office has to systematically verify the conditions provided for by circular IML 94/112 concerning equivalent identification. That verification has to cover *inter alia* the status of the intermediary and its submission to the FATF recommendations. If the conditions of an equivalent identification provided for by circular IML 94/112 are not met, the head office of the UCI in Luxembourg must itself carry out the identification of the investors in the UCI.

On the basis of the description provided by the head office, the auditor must analyse the distribution channel of units or shares of the UCI in order to determine if the head office complies with its obligations concerning the fight against money laundering.

In addition, the auditor must check whether the head office supervises abnormal transactions.

In this context, the auditor has to indicate its method of selection of sample files checked and the percentage of the total transactions covered.

In case a non-compliance is noted, the auditor will have to provide precise indications to the CSSF enabling it to make an appreciation of the situation (number of files which are incomplete, detail of the failures noted, etc.).

In case the auditor of the UCI makes use of the possibility to base itself on the audit report of the auditor in charge of the review of the entity which is

responsible for compliance with anti-money laundering rules, the long form report must provide the following details:

- name of the auditor of the entity in question
- date of the audit report

2.2. Valuation methods

The Law of 30th March, 1988 provides that, unless otherwise provided for in the management regulations or the articles of incorporation, the valuation of the assets shall be based 'in case of officially quoted security' on the latest known stock exchange quotations unless such quotations are not representative. For securities not so quoted and for securities which are so quoted but for which the latest quotation is not representative, these articles provide that the valuation must be based on the probable realisation value which must be estimated with care and in good faith.

The auditor will thus check if the valuation methods are applied in accordance with the procedures and the rules determined by the management regulations or the articles of incorporation and if these methods are also applied in a consistent manner.

The auditor must *inter alia* verify the application and the sincerity of the valuation rules of the securities portfolio, securities' lending/borrowing, repurchase and reverse repurchase agreements, sale with right of repurchase agreements, transactions, futures, swaps and options.

In connection with the valuation of portfolio securities, it must in particular insist on unquoted securities and illiquid securities.

In addition, the auditor will request the board of directors of the UCI or the management company of the UCI to provide details on the transactions undertaken by the UCI to enable the auditor to verify by sample tests if these transactions were undertaken at arm's length.

In case of non-compliance with the valuation methods described in the procedures or in the management regulations or the articles of incorporation, the auditor must provide detailed information enabling the CSSF to assess the situation.

2.3. Control of the risk management system

The board of directors of the UCI or of the management company of the UCI is supposed to have put into place the necessary controls to ensure compliance with the investment restrictions and policies of the UCI as well as the management of the risks encountered by the UCI. Either it assumes itself all or part of the above mentioned controls or it delegates this duty to one or several third parties.

The auditor must indicate the responsible persons/entities appointed by the board of directors of the UCI or the board of directors of the management company of the UCI which are entrusted with the control of the different risks for which the UCI is exposed. The auditor will also have to specify the frequency with which risk controls are made.

The long form report must indicate whether the control system put into place within those entities covers at least the risks inherent to the policy

and the investment risks of the UCI concerned, such as:

– credit/counterparty risk
– market risk
– settlement risk
– foreign exchange risk

If appropriate:

– interest rate risk
– liquidity risk
– risk on derivative instruments

The long form report must provide an analysis and an assessment of the systems put in place by the UCI to control and manage the different risks to which the UCI is exposed when it carries out its activities.

If shortfalls are noted, the auditor must give precise indications enabling the CSSF to assess of the situation.

2.4. Specific audits

In the context of his mission, the auditor must also proceed to specific audits. These are the audit of the compliance with the investment policy and the investment restrictions and the audit of the calculation of the NAV.

The auditor must under this item analyse every NAV calculation error and every non-compliance with the investment rules for which the amount of indemnification did not exceed EUR 25,000 and for which the amount to be reimbursed to any one investor did not exceed EUR 2,500 as set out in CSSF circular 02/77.

Under this item, the auditor must also indicate the following:

– material errors which the auditor has detected during its mission and which should have been notified in accordance with the provisions of CSSF circular 02/77;
– cases of non-compliance which the auditor has detected during its mission and which should have been notified in compliance with the provisions of CSSF circular 02/77.

In those cases, the auditor will in its long form report describe the material errors and the cases of non-compliance with investment rules identified during its audit and which have not been notified to the CSSF in compliance with CSSF circular 02/77. The auditor will thereafter deal with these errors and cases of non-compliance with the investment rules in accordance with the procedures set forth in CSSF circular 02/77.

In case no significant NAV error or in case of non-compliance with the investment policy will have been identified, the auditor must expressly state so in its long form report of the UCI.

2.5. Assets and liabilities and profit and loss account

The auditor will comment the different items of the consolidated[125] balance sheet in a clear and precise manner. The auditor must check the

125 UCIs are not required to produce consolidated accounts. What is meant here is the combined balance sheet of the multiple compartment UCIs consisting in the combination of the balance sheets of each compartment.

existence of those items, their amounts and their adequate accounting treatment, as well as the consistent application of accounting principles.

In addition, the auditor must examine the sale and purchase transactions of securities made during the two weeks preceding and the two weeks following the end of the financial year (this period needs to be extended if suspicious operations have been detected), in order to determine whether transactions have been entered into for the purpose of "window dressing".

Furthermore, the auditor will have to collect statistics on portfolio turnover in order to make an appreciation whether transactions have been entered into for the purpose of "churning".

The auditor must also comment on the various items of the combined profit and loss account. The auditor will have to check the existence of those items, their amounts and their adequate accounting treatment, as well as the consistent application of the accounting principles.

During its mission, the auditor will have to pay particular attention to the performance fees which may be payable to the investment managers.

The auditor will also have to receive from the board of directors of the UCI or of the management company of the UCI a confirmation to the effect that neither the investment managers nor any of their connected parties have received rebates from brokers and a confirmation on any arrangements concerning the payment of "soft commissions" in the context of the activities of the UCI. In case "soft commissions" are paid, the auditor will have to describe in the long form report the arrangements in relation thereto.

In addition, the auditor will need to receive from the board of directors of the UCI or the management company of the UCI a confirmation indicating whether there have been any commission rebates and, in the affirmative, describe the nature thereof.

Finally, the auditor will ask for a list of all costs, comprising transaction costs, which have been allocated to the UCI. It is recommended that this list refers where possible to the gross amount of the costs payable by the UCI. In relation to the most significant costs, the auditor will have to determine whether they have been calculated in compliance with the provisions of the applicable agreements.

In case of irregularities or shortfalls, the auditor will have to provide precise indications enabling the CSSF to assess the situation.

2.6. Publication of the NAV

The auditor shall indicate if the UCI has published its NAV in accordance with Article 92 of the Law of 30th March, 1988.

In case of non-compliance with this legal requirement, the auditor will indicate in detail the origin of this shortfall.

3. Internet

The long form report will indicate whether the UCI makes directly use of the Internet as a communication or distribution channel.

4. Complaints from investors

The auditor will query with the board of directors of the UCI or of the management company of the UCI whether, during the course of the financial year under review, complaints have been received by the head office in Luxembourg and to which the UCI had to respond.

If this is not the case, the auditor will specifically mention this in its long form report.

If complaints have been received, the auditor will indicate how many complaints have been received by the UCI in Luxembourg.

5. Follow-up on problems identified in preceding reports on the audit of the activities of the UCI

The auditor indicates in this part of its long form report the follow-up on irregularities and important weaknesses identified during its preceding auditors and which are detailed either in an earlier long form report or in a separate management letter addressed to the board of directors of the UCI or of the management company of the UCI (see also Chapter III.A. “General Principles” hereabove).

6. General conclusion

In its general conclusion the auditor must give its opinion on all the important items of its control in order to give a general view on the situation of the UCI.

More specifically, the auditor must summarise the main comments and conclusions contained in the long form report. It will also indicate the main recommendations and observations made to the board of directors of the UCI or the management company of the UCI as well as the latter’s response thereto. In case the auditor issues a separate management letter to the board of directors of the UCI or of the management company of the UCI, it is sufficient that the general conclusion refers, for this part, to that document which, in such case, must be annexed to the long form report (see also Chapter III.A. “General Principles” hereabove).

IV. Reporting to the CSSF pursuant to Article 89(3) of the law relating to UCIs

In compliance with paragraph (3) of Article 89 as amended of the law on UCIs, introduced by the Law of 29th April, 1999[126] , the auditor must report to the CSSF any fact or decision it has become aware while carrying out the audit of the accounting information contained in the annual report of an UCI or any other legal task concerning an UCI where such fact or decision is liable to:

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126 Law of 29th April, 1999

- implementing Directive 95/26/EC concerning the reenforcement of prudential supervision into the Law of 5th April, 1993 relating to the financial sector (as amended) and into the Law of 30th March, 1988 on undertakings for collective investment (as amended);

- partially implementing Article 7 of Directive 93/6/EEC on the capital adequacy of investment firms and credit institutions into the Law of 5th April, 1993 relating to the financial sector (as amended);

- operating certain other amendments to the Law of 5th April, 1993 relating to the financial sector (as amended);

- amending the grand-ducal regulation of 19th July, 1983 relating to fiduciary contracts of credit institutions. (This footnote appears in the circular as footnote 4).

– constitute a material breach of the provisions of the law on UCIs or the regulations adopted for its execution, or
– affect the continuous functioning of the UCI, or
– lead to a refusal to certify the accounts or to the expression of reservations therein.

The auditor shall likewise have the duty to report to the CSSF any fact or decision concerning the UCI and meeting the criteria mentioned hereabove of which it has become aware while carrying out the audit of the accounting information contained in the annual report of another undertaking having close links resulting from a control relationship with the UCI for which it carries out a legal task or while carrying out any other legal task concerning such other undertakings.

"Close link" resulting from a control relationship shall mean the link which exists between a parent undertaking and a subsidiary in the cases referred to in Article 77 of the amended Law of 17th June, 1992 relating to the annual accounts and the consolidated accounts of credit institutions or as a result of a relationship of the same type between any individual or legal entity and an undertaking; any subsidiary undertaking of a subsidiary undertaking is also considered a subsidiary of the parent undertaking which is at the head of those undertakings. A situation in which two or more individuals or legal persons are permanently linked to one and the same person by a control relationship shall also be regarded as constituting a close link between such persons.

In addition, if in the discharge of its duties the auditor ascertains that the information provided to investors or to the CSSF in the reports or other documents of the UCI does not truly describe the financial situation and the assets and liabilities of the UCI, it shall be obliged to inform the CSSF forthwith.

The auditor shall moreover be obliged to provide the CSSF with all information or certificates required by the latter on any matters of which the auditor has or ought to have knowledge in connection with the discharge of its duties. The same applies if the auditor ascertains that the assets of the UCI are not or have not been invested according to the regulations set out by the law or the prospectus.

In return for the duty to report to the CSSF, paragraph (3) also provides that any disclosure in good faith to the CSSF by the auditor of any fact or decision referred to in paragraph (3) does not constitute a breach of professional secrecy or of any restriction on disclosure of information imposed by contract and will not result in liability of any kind of the auditor.

V. Final provisions

The provisions of the present circular have to be complied with in their entirety for the annual accounts of the financial years ending on or after 31st December, 2003.

CSSF CIRCULAR 03/87 OF 21ST JANUARY, 2003 CONCERNING THE COMING INTO FORCE OF THE LAW OF 20TH DECEMBER 2002 RELATING TO UNDERTAKINGS FOR COLLECTIVE INVESTMENT.

Luxembourg, 21st January, 2003

To all undertakings for collective investment and to those who act in relation to the operation and supervision of such undertakings.

CSSF CIRCULAR 03/87

Concerns: Coming into force of the Law of 20th December, 2002 relating to undertakings for collective investment

Ladies and Gentlemen,

We would like to draw your attention to the enactment of the Law of 20th December, 2002 relating to undertakings for collective investment (Mémorial A - N° 151 of 31st December, 2002).

This Law of 20th December, 2002 implements into Luxembourg law Directives 2001/107/EC and 2001/108/EC and brings about a number of changes to the Luxembourg legal framework of undertakings for collective investment (UCIs).

The purpose of this circular is to present, in summary form, to the professionals of collective management, the main changes introduced by this Law of 20th December, 2002 and which relate to:

I. the definitions set forth in the text of the law
II. the extension of the investment policy of UCIs subject to Part I of the law
III. the rules concerning management companies
IV. the simplified prospectus and the publication of documents of UCIs
V. the transitional provisions.

I. Definitions

Article 1 of the law comprises a number of definitions, most of which have been taken from Directives 2001/107/EC and 2001/108/EC.

The law comprises, *inter alia*, a definition of the term "transferable securities".

Pursuant to Article 1, item 26)[127], "transferable securities" shall mean:

- shares and other securities equivalent to shares ("shares"),
- bonds and other debt instruments ("bonds")[128],
- any other negotiable securities which carry the right to acquire any such transferable securities by subscription or exchange,

excluding however the techniques and instruments referred to in Article 42 of the law.

127 Item 29 in the English translation of the law.

128 The law, the French version of amended Directive 85/611/EEC and the circular use "bonds" (*obligations*) as a defined term whereas the English version of the Directive uses the term "debt securities".

II. Extension of the investment policy of UCITS subject to Part I of the law

Compared to the amended Law of 30th March 1988 relating to UCIs, the law extends the range of assets in which UCITS subject to Part I of the law can invest in, and permits, under certain conditions, the investment in money market instruments, in units of UCITS and/or other UCIs, in deposits and in derivative financial instruments.

The transferable securities and other liquid financial assets in which UCITS subject to Part I of the law may invest, must meet a certain number of criteria which are set forth in Article 41 (1) of the law.

While extending the eligible investments for UCITS subject to Part I, the law adjusts the specific investment limits applicable to investments in such transferable securities and other liquid financial assets referred to in Article 41 (1).

The law also permits UCITS subject to part I to derogate, within specified conditions, from certain investment limits in order to permit them to replicate a recognised index of shares or bonds.

The detailed rules applicable to the investment policy and the investment restrictions applicable to UCITS subject to Part I are referred to under Chapter 5 of the law.

III. Rules regarding management companies

Part IV of the law (Chapters 13 and 14), which provides for detailed rules applicable to management companies, distinguishes between management companies which act as management company for one or several UCITS complying with the amended Directive 85/611/EEC and the other management companies subject to Luxembourg law which do not act as management company for UCITS complying with the aforesaid Directive.

A. Common provisions applicable to all management companies

The law provides that the activity of a management company to manage at least one UCI subject to Luxembourg law, requires a prior authorisation to be granted by the CSSF.

Under the provisions of the law, the CSSF may only grant its authorisation if the management company has its head office and registered office in Luxembourg.

The law specifies that the application for authorisation must describe the structure of the organisation of the management company.

The authorisation is subject to the condition that the management company entrusts the audit of its annual accounting documents to one or more auditors *(réviseurs d'entreprises)*, who can justify of an adequate professional experience.

Management companies which exist at the date of entry into force of the law must within 12 months from the date of entry into force of the law comply with the requirement to entrust the audit of their accounting documents to one or more auditors.

B. Provisions concerning management companies complying with Directive 2001/107/EC

Chapter 13 of the law provides for detailed rules applicable to management companies complying with Directive 2001/107/EC. It is applicable to all management companies which manage at least one UCITS complying with the amended Directive 85/611/EEC. These management companies may also manage UCIs which do not comply with the amended Directive 85/611/EEC.

The law extends the permitted activities of management companies complying with Directive 2001/107/EC. The law provides that these management companies may, in addition to the collective management for UCIs, undertake discretionary management activities for the account of individual and institutional investors, including pension funds.

The law specifies the conditions for taking up business and the operating conditions applicable to management companies complying with Directive 2001/107/EC.

Article 78 of the law deals with the conditions for taking up business and comprises, *inter alia*, the capital requirements applicable to such management companies which manage one or several UCITS complying with the amended Directive 85/611/EEC.

These capital requirements refer to the initial capital and the additional amount of own funds required if the assets under management exceed 250 million Euro.

For the purpose of the calculation of the amount of own funds, the assets the management of which is delegated, are taken into account, whereas the assets managed by delegation are not taken into account.[129]

The law provides that the own funds of the management company shall never be less than the amount prescribed in Annex IV of Directive 93/6/EEC.

Article 78, paragraph (1), item b) provides that the persons who effectively conduct the business of the management company and who are at least two, must be of sufficiently good repute and experience also in relation to the type of UCITS managed.

IV. Simplified prospectus and publication of the documents of UCIs

The law introduces the simplified prospectus which must include, in summary form, the information necessary for investors to be able to make an informed judgment of the investment proposed to them and, in particular, of the risks attached thereto.

The requirement to publish a simplified prospectus is however not applicable to UCIs subject to Part II of the law, and therefore only UCITS subject to Part I of the law must publish a simplified prospectus, whereas UCIs subject to Part II of the law may, but are not obliged to publish such a simplified prospectus.

The simplified prospectus is structured and written in such way that it can be easily understood by the average investor. It can be attached to the full prospectus as a removable part of it.

It is to be noted that the simplified prospectus can be used as a marketing tool designed to be used in all Member States of the European Union without any alterations except for its translation.

The content of the simplified prospectus is described in Schedule C of Annex I of the law.

With respect to the publication of documents of UCIs, Article 114 of the law introduces a new provision pursuant to which the CSSF may publish or arrange the publication of the documents of UCIs by all means which the CSSF deems appropriate.

The purpose of this text is to avoid possible legal hurdles relating to the publication of UCI documents in the context of a project commonly referred to as *"référentiel de la place"* (reference data base)[130] which is intended to form a data base centralising the information on Luxembourg UCIs.

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129 See footnote under Article 78 (1)(a) of the law.

130 See CSSF circular 03/97.

V. Transitional provisions

The law is applicable as from 1st January, 2003.

For reasons relating, *inter alia,* to the implementation provisions provided for by the two Directives 2001/107/EC and 2001/108/EC, it was decided to adopt a new law on UCIs, rather than to modify the amended Law of 30th March 1988.

To the extent that the two Directives 2001/107/EC and 2001/108/EC include transitional provisions which provide for a deadline expiring on 13th February, 2007 to permit UCITS existing on 13th February, 2002 and management companies authorised prior to 13th February, 2004 to comply with the new provisions, the law comprises in its transitional and repealing provisions, a number of provisions implementing the transitional provisions of the Directives.

A. Transitional provisions concerning UCIs

The law provides that UCITS subject to Part I of the amended Law of 30th March, 1988 relating to UCIs, as amended established before 13th February, 2002, may elect until 13th February, 2007 to remain governed by the amended Law of 30th March, 1988 or to be governed by the Law of 20th December, 2002.

As from 13th February, 2007, they will *ipso jure* be governed by the Law of 20th December, 2002.

The law provides that the establishment of a new compartment does not affect the foregoing election. This option must be exercised in respect of the UCITS as a whole in its entirety, including all its compartments.

UCITS subject to Part I of the Law of 30th March, 1988 relating to UCIs, as amended and established between 13th February, 2002 and 1st January, 2003 may elect until 13th February, 2004, to remain governed by the amended Law of 30th March, 1988 or to be governed by the Law of 20th December, 2002.

As from 13th February, 2004, they will be governed by the Law of 20th December, 2002 by operation of law.

UCITS within the meaning of Article 1 of the amended Law of 30th March, 1988 relating to UCIs, excluding those concerned by Article 2 of such same law, and established between 1st January, 2003 and 13th February, 2004 may elect to be governed by the amended Law of 30th March, 1988 or by the Law of 20th December, 2002.

As from 13th February, 2004, they will be governed by the Law of 20th December, 2002 by operation of law.

UCIs established prior to 1st January, 2003 and subject to Part II of the amended Law of 30th March, 1988 remain governed by the provisions of the amended Law of 30th March, 1988 relating to UCIs until 13th February, 2004. They may however be governed by the Law of 20th December, 2002 as from 1st January, 2003.

As from 13th February, 2004, they will be governed by the Law of 20th December, 2002 by operation of law.

UCIs established between 1st January, 2003 and 13th February, 2004 may elect to be governed by the provisions of the Law of 20th December, 2002 or by the provisions of the amended Law of 30th March, 1988 relating to UCIs.

As from 13th February, 2004, they will be governed by the Law of 20th December, 2002 by operation of law.

All UCIs established as from 13th February, 2004 are governed by the Law of 20th December, 2002, unless they are governed by a special law.

An investment company is deemed to be established as from the date of its incorporation before notary.

A common fund is deemed established as from the date of execution of its management regulations or from the date of entering into force of its management regulations if the management regulations specifically provide for such date.

B. Transitional provisions concerning management companies

Management companies existing on 1st January, 2003 are subject, by operation of law, to the provisions of Chapter 14 and are deemed authorised in accordance with Article 91 (1) of the Law of 20th December, 2002.

To the extent they manage UCITS governed by the amended Directive 85/611/EEC, such management companies must comply, at the latest by 13th February, 2007, with the provisions of Chapter 13 of the Law of 20th December, 2002.

Management companies authorised between 1st January, 2003 and 13th February, 2004 which act as management company for UCITS governed by the amended Directive 85/611/EEC must comply, at the latest by 13th February, 2007, with the provisions of Chapter 13.

In this context, it is important to note that the amended Law of 30th March, 1988 will remain in force until 13th February, 2007 and that, as a consequence there will be, until such date, two laws which will, on a parallel basis, regulate matters regarding UCIs.

It is the intention of the CSSF to clarify by means of circulars a number of other items referred to in the Law of 20th December, 2002. Accordingly, other CSSF circulars will provide further clarifications, *inter alia*, on the following subjects:

– the rules regarding management companies governed by Luxembourg law
– the rules of conduct applicable to professionals of collective management in Luxembourg
– the risk management methods and valuation methods applicable to transactions on derivative instruments.

The rules set forth in Circular IML 91/75 will also be amended and adjusted by means of a new CSSF circular.

CSSF CIRCULAR 03/88 OF 22ND JANUARY, 2003 CONCERNING THE CLASSIFICATION OF UNDERTAKINGS FOR COLLECTIVE INVESTMENT SUBJECT TO THE PROVISIONS OF THE LAW OF 20TH DECEMBER 2002 RELATING TO UNDERTAKINGS FOR COLLECTIVE INVESTMENT.

Luxembourg, 22nd January 2003

To all Luxembourg undertakings for collective investment and to those who act in relation to the operation and supervision of such undertakings.

CSSF CIRCULAR 03/88

Concerns: Classification of undertakings for collective investment subject to the provisions of the Law of 20th December, 2002 relating to undertakings for collective investment

Ladies and Gentlemen,

The purpose of this circular is to clarify the classification of undertakings for collective investment (UCIs) which are subject to the Law of 20th December, 2002 which entered into force on 1st January 2003. The main changes introduced by the Law of 20th December, 2002 are described in CSSF circular 03/87.

The amended Law of 30th March, 1988 relating to UCIs (hereafter the "Law of 30th March, 1988") will remain in force until 13th February, 2007 and, as a consequence, until such date two distinct laws will, on a parallel basis, regulate matters regarding UCIs. Pursuant to the transitional provisions set forth in the Law of 20th December, 2002, the following UCIs established under the Law of 30th March 1988 must comply with the new legal provisions by 13th February 2004 at the latest:

- UCITS subject to Part I of the Law of 30th March 1988 established between 13th February 2002 and 1st January 2003;
- UCITS within the meaning of Article 1 of the Law of 30th March 1988, excluding those referred to in Article 2 of such law, established between 1st January, 2003, and 13th February, 2004, which in a first stage had elected to be governed by the Law of 30th March 1988;
- UCIs existing on 1st January, 2003, subject to Part II of the Law of 30th March, 1988 which qualify as UCITS under Part I of the Law of 20th December, 2002;
- UCIs existing on 1st January, 2003, subject to Part II of the Law of 30th March, 1988 which qualify as UCIs subject to Part II of the Law of 20th December, 2002;
- UCIs established between 1st January 2003 and 13th February 2004, which qualify either as UCITS under Part I of the Law of 20th December, 2002 or as UCIs under Part II of the Law of 20th December, 2002 and which in a first stage elected to be governed by the Law of 30th March 1988 (Part II).

All undertakings for collective investment established on and after 13th February, 2004 are subject, by operation of law, to the Law of 20th December, 2002 and must comply with the provisions thereof as from the date of their establishment.

UCITS subject to Part I of the Law of 30th March, 1988 established prior to 13th February, 2002 may elect, until 13th February, 2007, either to remain subject to the Law of 30th March, 1988 or to be governed by the Law of 20th December, 2002.

I. General considerations

A UCI shall be deemed to be situated in Luxembourg if the registered office of the management company of the common fund or of the registered office of the investment company is situated in Luxembourg.

Depending on their characteristics, Luxembourg UCIs governed by the Law of 20th December, 2002 will be subject either to Part I or to Part II of such law.

This classification permits to distinguish between:

– undertakings within the meaning of Council Directive 85/611/EEC of 20th December, 1985 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS), as amended;
– the other undertakings which do not fall within the scope of application of Directive 85/611/EEC, as amended.

II. Definition of UCIs governed by Part I of the Law of 20th December, 2002

Part I of the Law of 20th December, 2002 applies to all UCIs the exclusive object of which is the investment in transferable securities and/or the other liquid financial assets referred to in Article 41 (1) of the law.

Considering this aforementioned definition, the criterium which determines whether a UCI is subject to Part I or Part II of the Law of 20th December, 2002 is the intended investment objective. If the UCI invests in transferable securities and/or the other liquid financial assets referred to in the aforesaid Article 41 (1) of the Law of 20th December, 2002, it is subject to Part I save for the exceptions commented in section III. below.

UCITS subject to Part I of the Law of 20th December, 2002 are of the open-ended type since the rules to which they are subject provide that they, directly or indirectly, redeem their units or shares at the request of the investors.

Due attention must be given to the abovementioned transitional provisions of the Law of 20th December, 2002 and, in particular, to Article 134 (5) concerning UCIs which exist on the date of the entry into force of such law and which are capable of becoming UCITS subject to Part I as a result of the extension of the concept of eligible assets.

Accordingly, a UCI which is presently governed by Part II of the Law of 30th March, 1988 may have to submit itself, because of its investment policy, by 13th February, 2004 at the latest to the provisions of Part I of the Law of 20th December, 2002, unless it is excluded from Part I pursuant to Article 3 of such law.

III. Definition of UCIs subject to Part II of the Law of 20th December, 2002

Part II of the Law of 20th December, 2002 applies to all UCIs the principal object of which is the investment in securities other than transferable securities and/or the other liquid financial assets referred to in Article 41 (1) of the law, as well as to all UCITS excluded from Part I.

In its Article 3, the Law of 20th December, 2002 provides for exceptions to the basic rule reproduced in section II. above by excluding from the scope of application of Part I certain categories of UCITS.

The cases of exclusion, which relate to the four categories described below, are identical to those provided for by the Law of 30th March, 1988. They were described in detail in IML circular 91/75. The first three categories described hereafter remain fundamentally identical to their description in IML circular 91/75. The fourth category has been adjusted to take account of the extension of the concept of eligible assets of UCITS as a result of which certain UCIs which were excluded from Part I of the Law of 30th March, 1988 are no longer excluded from Part I of the Law of 20th December, 2002.

UCITS excluded from Part I of the Law of 20th December, 2002 relate to the four following categories:

1. UCITS of the closed-ended type.

   These UCITS can be defined by distinguishing them from open-ended UCITS which, directly or indirectly, redeem their units or shares at the request of investors.

   The reimbursement to investors after a decision of the UCITS is not tantamount to a redemption if such reimbursement occurred without any request from investors pursuant to a redemption right.

   If the securities of a UCITS of the closed-ended type are redeemed at the request of investors after a certain date, such UCITS shall fall within the scope of application of Part I of the law from such date onwards, unless it belongs to one of the other categories of UCITS referred to in paragraphs 2. to 4. hereafter. In case this feature is established at inception, the prospectus must, from the outset, draw the investors' attention to that fact and to the possible consequences arising therefrom, including those relating to the investment policy.

2. UCITS which raise capital without promoting the sale of their units or shares to the public within the European Union ("EU") or any part of it.

   The exclusion from Part I of the law does not dispense the UCITS concerned from the condition of the collection of public savings which all undertakings must comply with in order to qualify as UCI; it simply prohibits the UCITS concerned to engage in any promotional activity within the EU as this concept is defined in each Member State. In Luxembourg, the concept of "promotional activity" refers in particular to the use of advertisement methods such as the press, radio, television or advertisement circulars. It does however not refer to offers of subscription which are addressed to a limited, particularly knowledgeable circle of investors.

   It follows from the above that the UCITS concerned hereby are those which, even though they are addressed to the public, renounce to any promotional activity within the EU.

3. UCITS the units or shares of which may, under their constitutional documents, only be sold to the public in countries which are not members of the European Union.

   The exclusion only applies subject to the condition that the management regulations or the articles of incorporation of these UCITS expressly provide that the sale of their units or shares is limited to the public of countries which are not members of the European Union and of the European Economic Area.

Are also covered by this category, UCITS the units or shares of which are listed on the Luxembourg Stock Exchange and which market those units or shares solely outside the European Union and the European Economic Area.

4. Categories of UCITS determined by the CSSF for which the rules laid down in Chapter 5 of the Law of 20th December, 2002 are inappropriate in view of their investment and borrowing policies.

   UCITS covered by this exclusion belong to one of the following categories:

   4.1. UCITS the investment policy of which permits the investment of 20% or more of their net assets in securities other than in transferable securities and/or other liquid financial assets referred to in Article 41 (1) of the Law of 20th December, 2002.

   4.2. UCITS the investment policy of which permits the investment of 20% or more of their net assets in venture capital. Investment in venture capital shall be taken to mean investment in securities of companies which have been recently formed or which are still in the course of development.

   4.3. UCITS the investment policy of which permits the borrowing, on a permanent basis and for investment purposes, of amounts representing at least 25% of their net assets.

   4.4. Multiple compartment UCITS, one compartment of which is not subject to Part I of the Law of 20th December, 2002 by reason of its investment or borrowing policy.

CSSF CIRCULAR 03/97 OF 28TH FEBRUARY, 2003 CONCERNING THE PUBLICATION BY UNDERTAKINGS FOR COLLECTIVE INVESTMENT IN THE REFERENCE DATABASE *("RÉFÉRENTIEL DE LA PLACE")* OF THE SIMPLIFIED PROSPECTUSES AND THE FULL PROSPECTUSES AS WELL AS THE ANNUAL AND SEMI-ANNUAL REPORTS.

Luxembourg, 28th February, 2003

To all Luxembourg undertakings for collective investment and to those who act in relation to the operation and supervision of such undertakings.

CSSF CIRCULAR 03/97

Concerns: **Publication by undertakings for collective investment in the reference database *("référentiel de la place")* of the simplified prospectuses and the full prospectuses as well as the annual and semi-annual reports**

Ladies and Gentlemen,

The purpose of this circular is to clarify the method of publication of simplified prospectuses and full prospectuses as well as the annual and semi-annual reports which undertakings for collective investment (UCIs) must publish for the benefit of their investors pursuant to Chapter 17 of the Law of 20th December, 2002 relating to undertakings for collective investment (the Law of 20th December 2002).

That law provides in its Article 114 that:

(1) UCIs must send their simplified and full prospectuses and any amendments thereto, as well as the annual and semi-annual reports, to the CSSF.

(2) The CSSF may publish or cause the publication of the aforesaid documents by such means as it shall consider adequate.

To take into account the evolution of information technology, a reference database has been put in place by the *Centrale de Communication Luxembourg S.A.* (CCLux) in order to create an infrastructure which permits investors and professionals of the industry to have access, by electronic means, to all prospectuses and annual and semi-annual reports of Luxembourg UCIs.

This platform is in line with the new European trends aiming at facilitating the distribution and the inspection of prospectuses and annual and semi-annual reports by means of electronic support such as the Internet.

The CSSF considers that this reference database strengthens the transparency of the information relating to UCIs subject to Luxembourg law and facilitates the access to such information for investors.

On the basis of Article 114 (2) of the Law of 20th December, 2002, the simplified prospectus and the full prospectus, as well as the annual and semi-annual reports of the UCIs subject to the aforesaid law must be published in the reference database. This compulsory publication is not applicable to UCIs subject to the Law of 19th July, 1991 relating to UCIs the securities of which are not intended to be placed with the public.

It is strongly recommended that UCIs subject to the Law of 30th March, 1988, relating to undertakings for collective investment (the Law of 30th March, 1988) also comply with this obligation of publication in the reference database.

The publication of the prospectus must be made once the latter has been approved by the CSSF. To the extent notified by a UCI to the CSSF, the publication of the prospectus is postponed until, at the latest, the start date of the distribution of the units of the UCI.

The annual and semi-annual reports must be published within the deadlines set forth in Article 109 (2) of the Law of 20th December, 2002 and in Article 85 (2) of the Law of 30th March, 1988.

The CSSF may, on the basis of an adequate justification, grant a derogation in relation to the obligation to publish the prospectuses and the annual and semi-annual reports in the reference database.

A separate circular will be issued at the time when the reference database will become operational and will deal with the methods of transmission of the prospectuses and the annual and semi-annual reports of UCIs to the CSSF and to CCLux.

CSSF CIRCULAR 03/108 OF 30TH JULY, 2003 CONCERNING LUXEMBOURG MANAGEMENT COMPANIES SUBJECT TO CHAPTER 13 OF THE LAW OF 20TH DECEMBER, 2002 RELATING TO UNDERTAKINGS FOR COLLECTIVE INVESTMENT AS WELL AS LUXEMBOURG SELF-MANAGED INVESTMENT COMPANIES SUBJECT TO ARTICLE 27 OR ARTICLE 40 OF THE LAW OF 20TH DECEMBER, 2002 RELATING TO UNDERTAKINGS FOR COLLECTIVE INVESTMENT.

Luxembourg, 30th July, 2003

To all UCIs and management companies subject to Luxembourg law

CSSF CIRCULAR 03/108

Concerns: **Luxembourg management companies subject to the provisions of Chapter 13 of the law of 20th December, 2002 relating to undertakings for collective investment as well as self-managed investment companies subject to the provisions of article 27 or article 40 of the law of 20th December, 2002 relating to undertakings for collective investment.**

Ladies and Gentlemen,

The main purpose of this circular is to clarify the way of application of certain articles of Chapter 13 of the law of 20th December, 2002 relating to undertakings for collective investment and amending the amended law of 12th February, 1979 on value added tax (the "Law of 20th December, 2002") which introduces a specific regime applicable to management companies managing UCITS governed by Directive 85/611, as amended (hereafter the "Directive 85/611"). In addition, the circular specifies the financial information that management companies which are subject to chapter 13 must communicate to the CSSF.

Chapter 13 of the law of 20th December, 2002 is applicable to all management companies subject to Luxembourg law which manage at least one UCITS authorised in accordance with Directive 85/611, as well as their branches.

Management companies which are subject to Chapter 14 of the law of 20th December, 2002 and management companies which manage neither a Luxembourg UCI nor a UCITS, are not subject to the provisions of this circular.

It is to be noted that pursuant to the transitional provisions of Article 135 of the law of 20th December, 2002, management companies which are authorised or which will be authorised until 13th February, 2004 have the option to submit themselves to Chapter 13 or to Chapter 14 of the law of 20th December, 2002. To the extent that they are subject to Chapter 14 and that they manage UCITS governed by Directive 85/611, they must comply with the provisions of Chapter 13 no later than 13th February, 2007. Management companies which manage UCITS and which are authorised after 13th February, 2004 are automatically subject to Chapter 13 of the law of 20th December, 2002.

In addition, this circular is applicable mutatis mutandis to investment companies subject to Directive 85/611 as amended by the directive of the European Parliament and Council of 21st January, 2002, and which have not designated a management company (Articles 27(2) and 40), except for items 1.4 (shareholding), 1.6 (own funds) and II. (prudential supervision of a management company subject to Chapter 13 of the Law of 20th December, 2002.

Finally, the transitional provisions of article 134 applicable to them must also be considered.

I. Conditions for obtaining and maintaining authorisation for management companies which do not engage in activities other than collective portfolio management as provided for by article 77(2).

1. Basic principles

Access to business of management companies within the meaning of Chapter 13 of the Law of 20th December, 2002 ("management companies"), is subject to prior authorisation by the CSSF (Article 77).

Prior authorisation is also required for the opening by Luxembourg management companies of agencies in Luxembourg or branches abroad.

The right of establishment and the freedom to provide services are applicable to Luxembourg branches of management companies managing UCITS and which are authorised and supervised by the competent authorities of another Member State.

2. Programme of activity

The application for authorisation must be accompanied by a programme of activity as referred to in Article 78(1)c) which provides, in particular, a description of a plan for development of the activities. The activity programme comprises information relating to:

a) the scope of the proposed services for the three next accounting periods concerning the collective portfolio management (number of UCITS managed directly and under delegation, laws under which such UCITS have been set up, their net assets as well as the number and net assets of UCITS, either managed directly or under delegation, created at the initiative of a company which is not part of the same group than the management company);

b) the investment policies of the UCITS managed as well as the financial instruments and markets concerned;

c) the risk management process (Article 42(1)).

3. Head office and infrastructure

The head office of a management company must be situated in Luxembourg. This requirement implies that a management company may not have in Luxembourg a registered or statutory office only. This concept must be understood in a broad sense and comprises in particular the fields of infrastructure and accounting and electronic data processing systems (Article 78(1)).

a) human infrastructure

The staff of the management company must be permanent and must be adapted to the contemplated activities. The CSSF must be informed about the number of persons working for the management company. The staff is, in principle, employed[131] by the company.

131 The French original of the circular uses in this sentence the term "*salarié*" which implies an employer/employee relationship between the management company and its staff.

The CSSF can grant a derogation from this requirement and can authorise that the staff, in part or entirely, is either on secondment[132] or made available by an entity of the same group or by a non-affiliated company. In this case, the contract governing this secondment or availability arrangement must be submitted to the CSSF. In addition, this contract must comprise rules governing conflicts of interest between the persons concerned and the entity if the latter is part of the same group.

The CSSF must be informed on the identity of the persons who conduct the business of the management company. The conduct of the company's business must be decided by at least two persons meeting the conditions of reputation and professional experience as described under item 5 of this circular. The CSSF must be able to contact directly the persons who conduct the business of the management company. These persons must be in a position to provide all the information which the CSSF considers essential for the performance of its supervision. At least one of these persons must be on site[133].

They must not necessarily be employees of the management company the business of which they conduct, provided that there exists an agreement which precisely defines their rights and obligations and, if applicable, with whom there exists a hierarchical connection. It is also not excluded that the persons concerned conduct the business of several management companies, provided that the CSSF has sufficient evidence that each of these persons is in a position to accomplish at all times his functions, taking in particular into account the activities of the management companies concerned.

The principle of independence of the management company from the depositary does not permit for the persons who conduct the business of the management company to be employed by the custodian of a UCITS which it manages[134].

b) technical infrastructure

The CSSF must receive a description of the IT equipment, the information sources and the softwares which are being used.

The management company must have sound administrative and accounting procedures, control and safeguard arrangements for electronic data processing and adequate internal control mechanisms; it must be structured and organised in such way as to minimise the risk of UCITS' or clients' interests being prejudiced by conflicts of interest between the management company and its clients, between one of its clients and another, between one of its clients and a UCITS or between two UCITS (Article 84(1)). These prudential rules will be specified at a later stage in a circular.

c) preconditions for authorisation of delegation

Management companies are authorised to delegate to third parties, for the purpose of a more efficient conduct of their business, the power to carry out on their behalf one or more of their own functions (Article 85(l)).

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132 The French original of the circular uses the word "*détaché*" which implies that the staff must not be employees in the sense of footnote 131.

133 The French original of the circular uses the terms "*sur place*". This implies that the relevant person must usually work in Luxembourg but can reside either in Luxembourg or in one of its neighbour countries.

134 The French original of the circular refers to "*dont elles assurent la gestion*" which, from a French grammar point of view, would imply that this portion of the sentence refers to the persons who conduct the business. In fact the sentence makes only sense if the portion of this sentence refers to the management company.

The management company's and the depositary's liability shall not be affected by the fact that the management company has delegated any functions to third parties.

For obtaining an authorisation of delegation from the CSSF, the following preconditions must be complied with:

- *General preconditions to the authorisation of delegation*
  - The CSSF must be informed in an appropriate manner about the delegation of functions. To that effect, the management company must submit, in relation to each UCITS which it manages, to the supervisory authority[135] a description with details on the functions which it intends to delegate, the entities to which the functions will be delegated as well as the procedures available to the management company to control the activities of the enterprises[136] to which mandates will be given. This description must comprise all details necessary to permit the CSSF to verify whether the conditions for delegation are complied with.
  - The mandate may not prevent the effectiveness of supervision over the management company, and in particular, it must not prevent the management company from acting, or the UCITS from being managed, in the best interest of the investors.

    In that context, the delegation must be structured in a manner that the compliance with the rules of conduct set forth in Article 86 is ensured and can be controlled at any time.

    The rules of conduct will be specified at a later stage in a circular.
  - There exist measures which enable the persons who conduct the business of the management company to monitor effectively at any time the activity of the enterprise to which the mandate is given.

    This requirement imposes on the management company to put in place a monitoring infrastructure which enables its directors[137] to have access to the data relating to the activities performed by the agent or agents in the name and on behalf of the management company and the UCITS which it manages.

    Depending on the delegated functions, the directors will receive on a regular basis, in relation to each of the UCITS managed by the management company, detailed reports which enable them to assess in particular:
    * that the assets of the UCITS are invested in accordance with its constitutive documents and the applicable laws;
    * that there exists and is employed a risk management process which enables the monitoring and measurement at any time of the risk of the positions and their contribution to the overall risk profile of the portfolio of the UCITS;
    * the monitoring of the marketing policy of the UCITS.

    The frequency and the detail of such reports shall be dictated by the characteristics of the UCITS and the risks associated therewith.

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135 i.e. the CSSF

136 The French original of the circular generally uses, in the same manner as Directive 85/611 and the Law of 20th December, 2002, the term "*entreprise*" but sometimes also the word "*entité*". In the same manner as the English version of Directive 85/611 the term "enterprise" is used in this translation on a consistent basis.

137 The French original of the circular uses the word "*dirigeant*". They are the persons (at least two) referred to in 3.a) above who are referred to in this section.

The delegation of certain functions to third parties must not prevent the persons who conduct the activity of the management company to have access, either on a real time basis or upon simple request, to the accounting documents relating to the UCITS.

- The mandate shall not prevent the persons who conduct the business of the management company to give at any time further instructions to the enterprise to which functions are delegated and to withdraw the mandate with immediate effect when this is in the interest of investors.

  The content of the delegation agreement must take into account these requirements and provide for the details thereof, comprising the circumstances in which the contract can be terminated with immediate effect.
- The enterprise to which functions will be delegated must be qualified and capable of undertaking the functions in question, having regard to the nature of the functions to be delegated.

  In addition to the authorisations which may be required by applicable regulations, the enterprises to which functions have been delegated must bring evidence that they have appropriate human and technical resources, having regard to the delegated functions.
- The prospectuses of the UCITS list the functions which the management company has been permitted to delegate.

  The CSSF may require, if the interest of investors so warrants, that the identity of the enterprises to which functions have been delegated by the management company are published in the prospectus.

- *Preconditions specific to the investment management function*
  - When the delegation concerns the management of investments, the mandate may only be given to entities which are authorised or registered for the purpose of asset management and are subject to prudential supervision.

    To that effect, the enterprises to which investment management functions have been delegated must have the necessary authorisations required under their national laws and, if applicable, any other laws applicable to the services provided.

    The enterprises to which investment management functions have been delegated must be submitted in their home state to a permanent supervision performed by a supervisory authority set up by law in order to ensure the protection of investors.
  - The identity of the enterprises to which investment management functions have been delegated must, in principle, be published in the prospectus of the UCITS concerned.
  - The delegation must be in accordance with investment-allocation criteria periodically laid down by the management company.

    Therefore, the delegation agreement shall indicate the investment policy and the investment restrictions applicable to the UCITS (and each compartment if the delegation concerns one or several compartments of a UCITS with multiple compartments[138]) and, if applicable, specific investment rules ("asset allocation criteria") determined by the board of directors. These provisions can be included in the delegation agreement by means of a reference to the provisions in the prospectus of the UCITS concerned, without prejudice to specific instructions which may be given from time to time by the board of directors of the management

138 These are commonly referred to as umbrella funds.

company or by the persons who conduct the business of the management company. In case of an amendment of such rules, the agreement will be amended in due time to permit the delegates to comply with the new rules immediately when they come into force.

- Where the mandate concerns the management of investments and is given to a third country enterprise, cooperation between the CSSF and the supervisory authority of that country must be ensured.

  The CSSF will determine which supervisory authorities meet such condition.
- A mandate with regard to the core function of investment management shall not be given to the depositary or to any other enterprise whose interests may conflict with those of the management company or the unitholders.

  This provision does not prohibit the delegation of the investment management function to a company which is part of the same group as the depositary. In such a situation, the CSSF will authorise the delegation only if it has evidence that measures have been put in place to protect the interests of the management company and the unitholders.

4. Shareholding

The CSSF shall not grant authorisation to take up the business of a management company until it has been informed of the identities of the shareholders or members, whether direct or indirect, natural or legal persons, that have qualifying holdings and of the amounts of those holdings (Article 79(1)). The CSSF must be satisfied that the shareholders who have a qualifying holding must not only be of sufficiently good repute, but will perform their powers in a manner to ensure the sound and prudent management of the management company. A qualifying holding means any direct or indirect holding in a management company which represents 10% or more of the capital or of the voting rights or which makes it possible to exercise a significant influence over the management of the management company in which that holding subsists (Article 1(23))[139].

In addition, it is required that the structure of the direct and indirect shareholding is organised in a manner that the authorities responsible for the prudential supervision of the management company, and, if applicable, the persons with whom the management company has close links are clearly determined and that such supervision can be undertaken without hindrance (Article 78(2)).

Finally, the management company must inform the CSSF about any change in the persons that have qualifying holdings or holdings which make it possible to exercise a significant influence, as soon as it becomes aware thereof (Article 83(1)).

5. Good professional repute and professional experience

The directors of the UCITS must be of sufficiently good repute and have sufficient experience, also in relation to the type of UCITS concerned. To that end, the names of the directors, and of every person succeeding them in office, must be communicated forthwith to the CSSF

139 In the English translation of the law of 20th December, 2002 prepared by the authors of this translation, the term qualifying holding is defined in article 1(18).

(Article 93(3)). "Directors" shall mean those persons who, under law or the constitutional documents, represent the UCITS, in this case the members of the board of directors, or those who effectively determine the conduct of the activities of the UCITS.

The persons who conduct the business of the management company must also be of sufficiently good repute and be sufficiently experienced in relation to the type of UCITS managed by the management company concerned (Article 78(1)b)) in order to be authorized by the CSSF prior to their appointment.

6. Own funds

The requirements relating to the own funds of the management company are one of the major changes of the new text. There is now a requirement for an initial capital of at least 125,000 Euro and an additional amount of own funds must be provided according to the portfolios under management (Article 78(1)a)).

Irrespective of the amount of these requirements, the own funds of the management company shall never be less than the amount prescribed in Annex IV of Directive 93/6/EEC[140].

In case a management company of UCITS provides, in addition, services of management of portfolios of investments on a discretionary client-by-client basis, including those owned by pension funds, in accordance with a mandate given by investors, the provisions of circular CSSF 00/12 defining the ratios of own funds applicable by virtue of Article 56 of the amended law of 5 April 1993 relating to the financial sector are applicable.

7. External audit

Management companies must entrust the audit of their annual accounting documents to one or more *réviseurs d'entreprises* (external auditors) who can justify of an adequate professional experience (Article 80(1)).

II. Conditions for obtaining and maintaining authorisation for management companies which engage in activities of collective portfolio management and in the management of portfolios of investments on a discretionary client-by-client basis as contemplated in Article 77(3).

All the conditions set forth in chapter I remain applicable. In addition, requirements specific to the activity of portfolio management on a discretionary client-by-client basis are applicable.

Especially, the activity programme as described in Chapter 1.2. comprises, in addition, information on the scope of the proposed services for the next three accounting periods as regards:

- the management of portfolios of investments on a discretionary client-by-client basis (number of private clients, institutional clients and pension funds as well as the assets managed for each type of client);
- if applicable, the proposed non-core services.

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140 Investment firms shall be required to hold own funds equivalent to one quarter of their preceding year's fixed overheads. The competent authorities may adjust that requirement in the event of a material change in the firm's business since the preceding year. Where a firm has not completed a year's business, including the day it starts up, the requirement shall be a quarter of the fixed overheads projected in its business plan unless an adjustment to that plan is required by the authorities.

In addition, to the extent that the services in which the management companies subject to this chapter engage are in respect of the management on a discretionary client-by-client basis the same services as those in which engage portfolio managers[141] falling within the scope of Article 24 B) of the amended law of 5 April 1993 relating to the financial sector, the same prudential rules are, in principle, also applicable to them.

For example, the two persons who conduct the business of the management must be on site. The details of such specific additional requirements will, if necessary, be specified in a circular at a later stage.

III. Prudential supervision of a management company subject to Chapter 13 of the law of 20th December, 2002.

Article 82(2) provides that the prudential supervision of a management company shall be the responsibility of the CSSF. The management companies, as well as their branches, must from now on provide the CSSF with financial information which has to be drawn up on a quarterly basis. This financial information will be used by the CSSF for the purpose of its prudential supervision of the management companies.

The schedules of financial information which must be remitted periodically to the CSSF are attached hereto. The information concerned is divided in two parts.

The first part is applicable on a general basis to all management companies of UCITS and concerns the "Financial situation of the management company" (Table SG 1A), the "Profit and loss account" (Table SG 1 B) and the "Management of UCIs" (Table SG 1C). The second part concerns the financial information relating to other possible activities in which the management company engages (Table SG 2).

All tables have to be drawn up on a quarterly basis. The reference dates of the reports are the last day of each calendar quarter, i.e. 31st March, 30th June, 30th September and 31st December; the tables must be received by the CSSF for the 20th day of the month which follows the reference date. The tables have to be submitted to the CSSF for the first time on 31st December, 2003.

IV. Prudential supervision of a self-managed investment company in transferable securities (SIAG)[142].

Articles 27 and 40 impose on SIAGs to comply with all the provisions applicable in relation to prudential supervision. The SIAGs, comprising their branches, must provide the CSSF with specific financial information which has to be drawn up on a quarterly basis. This financial information will be used by the CSSF for the purpose of its prudential supervision of the SIAGs.

The schedules of financial information which must be remitted periodically to the CSSF are attached hereto. Such information concerns the "Financial situation of the SIAG" (Table SIAG 1A) and the "Profit and loss account" (Table SIAG 1B).

The tables must be drawn up on a quarterly basis. The reference dates are the last day of each calendar quarter, i.e. 31st March, 30th June, 30th September and 31st December; the tables must be received by the CSSF for the 20th day of the month which follows the reference date. The tables have to be submitted to the CSSF for the first time on 31st December, 2003.

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141 *Gérants de fortune*

142 The French original of the circular uses the term "*société d'investissement en valeurs mobiliéres autogérée*" and the abbreviation "*SIAG*".

Repealed by the Law of 13 February 2007

Annex 1

Table SG 1A

FINANCIAL SITUATION ON …
(in the currency of the capital)

Company:
Person in charge:
Periodicity: quaterly

ASSETS	AMOUNT
1. Subscribed capital unpaid	
2. Incorporation expenses	
3. Fixed assets	
3.1. Fixed intangible assets	
3.2. Fixed tangible assets	
3.3. Financial fixed assets	
Units in affiliated undertakings	
Loans and advances to affiliated undertakings	
Participating interests	
Loans and advances to undertakings in which the company has participating interests	
Securities held as fixed assets	
Others	
4. Current assets	
4.1. Cash	
4.2. Balances in banks, balances in postal cheques accounts	
4.3. Loans and advances	
4.4. Transferable securities	
4.5. Others	
5. Prepayments and accrued income	
6. Various	
7. Loss for the financial year	
Total general (1+2+3+4+5+6+7)	

LIABILITIES	AMOUNT
1. Equity capital	
1.1. Subscribed capital or endowment capital	
1.2. Share premium	
1.3. Revaluation reserve	
1.4. Legal reserve	
1.5. Other reserves	
1.6. Profit or loss brought forward	
2. Subordinated debts	
3. Provisions for liabilities and charges	
3.1. Provisions for pensions and similar commitments	
3.2. Provisions for taxes	
3.3. Other provisions	
4. Debts	
5. Profit for the financial year	
Total general (1+2+3+4+5)	

Repealed by the Law of 13 February 2007

Annex 2

Table SG 1B

PROFIT AND LOSS ACCOUNTS ON …
(in the currency of the capital)

Company:
Person in charge:
Periodicity: quarterly

WORDING		AMOUNT
1. Interests and commissions receivable	+	
2. Interests and commissions payable	-	
3. Other operating income	+	
4. Gross profit or gross loss		
5. Income from transferable securities	+	
a) income from participating interests		( )
b) income from other transferable securities		( )
c) income from participating interests or from units in affiliated undertakings		( )
6. General administrative expenses	-	
6.1. Staff costs		
Wages and salaries		( )
Social security costs		( )
Social security costs relating to general pensions		( )
6.2. Other administrative expenses		( )
7. Value adjustments in respect of:	-	
7.1. Intangible and tangible assets		( )
7.2. Financial fixed assets and transferable securities being part of the current assets		( )
7.3 Others		( )
8. Value re-adjustments	+	
9. Provisions for general risks	-	
10. Tax on profit on ordinary activities	-	
11. Profit or loss on ordinary activities after tax	+/-	
12. Extraordinary income	+	
13. Extraordinary charges	-	
14. Extraordinary profit or loss	+/-	
15. Tax on extraordinary profit or loss	-	
16. Other taxes not shown under the proceeding items	-	
17. Profit or loss for the financial year	+/-	

Repealed by the Law of 13 February 2007

Annex 3

Table SG 1C

MANAGEMENT OF UCIs ON …
(in the currency of the capital)

Company:
Person in charge:
Periodicity: quarterly

Portfolio of the UCIs managed	**Number**	**Evaluation value**
I. UCIs managed		
FCP Part I		
Others		
SICAV Part I		
Others		
Other UCIs		
Total		
II. UCIs managed under delegation		

	Amount
Own funds of the management company	

Note:

UCIs managed: concern the UCIs managed by the management company including portfolios for which it has delegated the management function but excluding portfolios that it is managing under delegation.

UCIs managed under delegation: concerns UCIs managed by the management company under delegation.

Repealed by the Law of 13 February 2007

Annex 4

Table SG 2 **OTHER ACTIVITIES ON …**
(in the currency of the capital)

Company:
Person in charge:
Periodicity: quarterly

	Number	Amount
1. Management of portfolios of investment		
Management mandate		
Of which: pension funds		
Fees received during the quarter	Xxxxxxxxxxxx	
2. Investment advice		
Existing investment advisory agreements		
Fees received during the quarter		
3. Safekeeping and administration of UCI units		
Deposits of UCI units		
Fees received during the quarter	Xxxxxxxxxxxx	

Note:

1. Management of portfolios of investment

1) The total of the assets under management must correspond to the market value at the time of the drawing up of the table.

2) With respect to the fees received during the quarter, the table must indicate the gross amount of the fees received (management fees, performance fees, etc.) for the management of assets during the quarter for which the table is drawn up.

2. Investment advice

1) Investment advisory agreements: it concerns agreements made with a client in order to provide him investment advice for a determined or undetermined period of time on instruments listed in section B of annex II of the amended law of 5th April, 1993 relating to the financial sector.

2) Amount: one should indicate the average volume during the current accounting year of the portfolio for which investment advice has been provided which means that there should be calculated at the end of each months an average of the value of the portfolio of all clients advised during the current accounting year including the amount of the portfolio at the date of closing of the previous accounting year.

3) Amount of the fees received during the current month: the table must indicate the amount of advisory fees received during the current quarter until the date as of which the table is drawn up.

3. Safekeeping and administration of UCI units

1) Deposits of UCI units: one should indicate the number of deposits, as well the evaluation value of these deposits.

2) Fees received during the quarter: the table must indicate the amount of the fees received in the context of the deposit service provided for UCI units at the date of the drawing up of the table.

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Annex 5

Table SIAG 1A

FINANCIAL SITUATION ON …
(in the currency of the capital)

Company:
Status: ☐ SICAV ☐ Others
Person in charge:
Periodicity: quarterly

ASSETS	AMOUNT
1. Incorporation expenses	
2. Fixed asset	
2.1 Fixed intangible assets	
2.2 Fixed tangible assets	
2.3 Financial fixed assets	
3. Current assets	
3.1 Portfolio Securities	
3.1.1 Shares and other variable-yield securities	
3.1.1.1. Shares other than units of UCIs	
3.1.1.2. Shares admitted to listing or dealt in on another regulated market	
3.1.1.3. Shares not admitted to listing	
3.1.1.4. Other participating interests	
3.1.1.5. Units of UCIs	
3.1.2 Bonds and other debt securities	
3.1.2.1 Short term securities (initial due date: one year or more)	
3.1.2.2 Medium/long term securities (initial due date: more than one year)	
3.1.3 Money market instruments	
3.1.4 Warrants and other rights	
4. Financial instruments	
4.1. Option contracts	
4.1.1. Options purchased	
4.1.2. Options sold	
4.2. Forward contracts	
4.3. Others	
5. Liquid assets	
6. Other assets	
Total general (1+2+3+4+5+6)	
LIABILITIES	AMOUNT
1. Debts	
2. Loans	
3. Provisions for liabilities and charges	
3.1. Provisions for pensions and similar commitments	
3.2. Provisions for taxes	
3.3. Other provisions	
4. Debts	
5. Profits for the financial year	
Total general (1+2+3+4+5)	

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Annex 6

Table SIAG 1B

PROFIT AND LOSS ACCOUNTS ON …
(in the currency of the capital)

Company:
Status: ☐ SICAV ☐ Others
Person in charge:
Periodicity: quarterly

	AMOUNT
Total income	
1. Dividends	
2. Interest on bonds and other debt securities	
3. Interest from banks	
4. Other income	
a) Fees received	
b) Others	
Total charges	
1. Fees	
a) Advisory and/or management fees	
b) Depositary bank fees	
c) Other fees	
2. Administration charges	
a) Head office (central administration) charges	
b) Audit and controlling charges	
c) Other administration charges	
3. Taxes	
a) Annual subscription tax (taxe d'abonnement)	
b) Other taxes	
4. Interest paid	
5. Other charges	
Net profit or net loss on investment	
6. Realized net profit or loss	
7. Variation of unrealized net profit or loss	
Net profit or net loss on operations	

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Association Luxembourgeoise des Fonds d'Investissement

Carré Bonn
20, rue de la Poste
L-2346 Luxembourg
Tél. +352 22 30 26-1
Fax +352 22 30 93
info@alfi.lu
www.alfi.lu

Société de la Bourse de Luxembourg SA

11, av. de la Porte-Neuve
BP 165
L-2011 Luxembourg
Tél. +352 47 79 36-1
Fax +352 47 32 98
info@bourse.lu
www.bourse.lu