

COLLECTIVE INVESTMENT SCHEMES  
IN LUXEMBOURG

Law and Practice

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# COLLECTIVE INVESTMENT SCHEMES IN LUXEMBOURG

Law and Practice

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## INTRODUCTION TO THE FIRST EDITION IN ENGLISH

Eight years have passed since the publication of the first edition of our compendium on undertakings for collective investment (UCIs) in French.

Many new laws and regulations have been adopted during this period, mainly at the initiative of the EU authorities. This prompted the publication of a second edition in French in 2006.

It is not by accident that this book has come about. Although undertakings for collective investment have a long history in the Grand Duchy of Luxembourg, they had never previously been the subject of a systematic review and legal analysis. We could not allow this opportunity and challenge to pass.

Drafted by and for practitioners, this work is a handbook rather than a treatise. Its purpose is to enable the interested reader to understand the legal operation of UCIs and to provide immediate and practical answers. The law on UCIs is discussed by theme, from the creation of a UCI to its liquidation. The obligations connected with banking secrecy and the prevention of money laundering are discussed in detail, as are the tax rules governing UCIs and their participants. The impact of Community law on these aspects is explained in a separate chapter.

This edition also reflects recent legislative changes in the European Union and in the Grand Duchy of Luxembourg which impact on UCIs. Recent EU directives which affect UCIs include the 'Prospectus', 'MiFID', and 'Savings Taxation' Directives. Legislation passed in the Grand Duchy of Luxembourg in 2007 created the framework for the so-called 'specialized' investment funds, thereby increasing the types of UCIs available to qualified investors.

This edition in English is the result of a strong demand from all those market participants who are not familiar with the French language. It has been updated from the second edition in French published in November 2006 in all major aspects which are relevant, although some of them could not be analysed in as much detail as we would have liked. Furthermore, the proposed new regulation on coordinated UCITS, generally referred to as 'UCITS IV', has not been addressed, as, at the time of writing this introduction, no formal proposals from the European Commission have been adopted.

The English used in this edition has been monitored and improved by Denise Kinsella, an Irish lawyer based in Dublin. Denise is a former partner of the law firm Dillon Eustace and currently works as an independent director of, and consultant to, several Irish investment funds. We are most grateful for the significant improvements made by Denise, not only from a language point of view, but also in terms of clarity.

We also wish to thank our partners and associates at Arendt & Medernach for their specialist contributions to the contents of the book. We are extremely grateful for their support without which this work could not have been accomplished.

Last but not least, we would like to thank the readers of the previous editions—clients and friends—whose constructive comments have, we hope, allowed us to provide a more thorough analysis of the laws on collective investment schemes.

Claude Kremer and Isabelle Lebbe  
Luxembourg  
June 2008

## PREFACE TO THE FIRST EDITION IN FRENCH

This work written jointly by Maîtres Claude Kremer and Isabelle Lebbe immediately impressed me on account of its thoroughness and, in particular, its scope. Whilst undertakings for collective investment have been the subject of many dissertations, I am not aware of any work that covers all of their aspects so completely.

The growing importance of UCIs for the financial market renders the contribution made by this book even more significant: designed as a reference tool, it can be used to track the development of a sector which has undergone persistent and permanent change in recent years. For that reason, I am convinced that it will become the virtually indispensable companion of practitioners, both in Luxembourg and elsewhere.

These pages show that Luxembourg has not only managed to create a general environment and a legal framework in which undertakings for collective investment can prosper, but that it has also built up a relevant body of legal opinion, which is explained clearly and fully in this book.

In conclusion, I sincerely hope that other authors will follow this example and write handbooks of similar quality for other market activities.

Jean-Nicolas Schaus  
Director General  
Commission de Surveillance du Secteur Financier  
June 2000

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## LIST OF ABBREVIATIONS

### General

|                              |                                                                                                                                                                                                                                                                                     |
|------------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| ABBL                         | <i>Association Luxembourgeoise des Banques et Banquiers</i><br>(Luxembourg Bankers' Association)                                                                                                                                                                                    |
| <i>Act dr</i>                | <i>Actualités du droit</i> (Belgium)                                                                                                                                                                                                                                                |
| ALFI                         | Association of the Luxembourg Fund Industry                                                                                                                                                                                                                                         |
| <i>Bull François Laurent</i> | <i>Bulletin du Cercle François Laurent</i> (Luxembourg)                                                                                                                                                                                                                             |
| <i>Cah dr eur</i>            | <i>Cahiers de droit européen</i> (Belgium)                                                                                                                                                                                                                                          |
| CA                           | Court of Appeal (Luxembourg)                                                                                                                                                                                                                                                        |
| Cass b                       | <i>Cour de cassation belge</i> (Belgian Supreme Court of Appeal)                                                                                                                                                                                                                    |
| Cass fr                      | <i>Cour de cassation française</i> (French Supreme Court of Appeal)                                                                                                                                                                                                                 |
| Cass lux                     | <i>Cour de cassation luxembourgeoise</i> (Luxembourg Supreme Court of Appeal)                                                                                                                                                                                                       |
| CESR                         | Committee of European Securities Regulators                                                                                                                                                                                                                                         |
| CJEC                         | Court of Justice of the European Communities                                                                                                                                                                                                                                        |
| CSSF                         | <i>Commission de Surveillance au Secteur Financier</i> (Commission for the Supervision of the Financial Sector)                                                                                                                                                                     |
| <i>D</i>                     | <i>Recueil Dalloz</i> (France)                                                                                                                                                                                                                                                      |
| <i>DAOR</i>                  | <i>Droit des affaires—Ondernemingsrecht</i> (Belgium)                                                                                                                                                                                                                               |
| EC                           | European Communities                                                                                                                                                                                                                                                                |
| ECR                          | European Court Reports                                                                                                                                                                                                                                                              |
| EEA                          | European Economic Area, ie the EU Member States plus Iceland, Liechtenstein and Norway                                                                                                                                                                                              |
| Eligible Assets Directive    | Commission Directive (EC) 2007/16 (see 'Legislation and Circulars' below)                                                                                                                                                                                                           |
| ESC                          | European Securities Committee                                                                                                                                                                                                                                                       |
| EU                           | European Union, ie Austria, Belgium, Bulgaria, Czech Republic, Cyprus, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Poland, Portugal, Romania, Slovakia, Slovenia, Spain, Sweden, United Kingdom |
| FATF                         | Financial Action Task Force on money laundering                                                                                                                                                                                                                                     |
| FCP                          | <i>Fonds commun de placement</i> (common fund)                                                                                                                                                                                                                                      |
| IML                          | <i>Institut Monétaire Luxembourgeois</i> (Luxembourg Monetary Institute), subsequently renamed the <i>Commission de Surveillance du Secteur Financier</i>                                                                                                                           |
| <i>JCP</i>                   | <i>Jurisclasseur périodique (La semaine juridique)</i> (France)                                                                                                                                                                                                                     |
| <i>JDF</i>                   | <i>Journal de droit fiscal</i> (Belgium)                                                                                                                                                                                                                                            |

## List of Abbreviations

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|------------------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| <i>JT</i>              | <i>Journal des tribunaux</i> (Belgium)                                                                                                                                                                                                                                                                                                                                          |
| <i>Larcier cass</i>    | <i>Larcier cassation</i> (Belgium)                                                                                                                                                                                                                                                                                                                                              |
| LIR                    | Act of 4 December 1967 concerning the taxation of the income of natural persons and companies ( <i>Tax Code</i> , volume 2, Editions de l'Imprimerie St-Paul)                                                                                                                                                                                                                   |
| <i>Mémorial</i>        | <i>Mémorial, Journal officiel du Grand-Duché de Luxembourg</i> (official journal of the Grand Duchy of Luxembourg). The <i>Mémorial</i> encompasses the following three compendiums: the legislative compendium ( <i>Mémorial A</i> ), the administrative and economic compendium ( <i>Mémorial B</i> ), and the compendium of companies and associations ( <i>Mémorial C</i> ) |
| MiFID Directive        | Directive (EC) 2004/39 (see 'Legislation and Circulars' below)                                                                                                                                                                                                                                                                                                                  |
| MTF                    | Multilateral trading facility                                                                                                                                                                                                                                                                                                                                                   |
| NAV                    | Net asset value                                                                                                                                                                                                                                                                                                                                                                 |
| OECD                   | Organisation for Economic Cooperation and Development                                                                                                                                                                                                                                                                                                                           |
| OJ                     | Official Journal of the European Communities, subsequently renamed Official Journal of the European Union                                                                                                                                                                                                                                                                       |
| <i>Pas</i>             | <i>Pasicrisie</i> (Belgium)                                                                                                                                                                                                                                                                                                                                                     |
| <i>Pas lux</i>         | <i>Pasicrisie luxembourgeoise</i> (Luxembourg)                                                                                                                                                                                                                                                                                                                                  |
| <i>RCJB</i>            | <i>Revue critique de jurisprudence belge</i> (Belgium)                                                                                                                                                                                                                                                                                                                          |
| <i>RDC</i>             | <i>Revue de droit commercial belge</i> (Belgium)                                                                                                                                                                                                                                                                                                                                |
| <i>Rec Lég Pl Fin</i>  | <i>Recueil de la législation sur la place financière de Luxembourg</i> , Central Legislation Department, 2006                                                                                                                                                                                                                                                                   |
| <i>Rec Lég Soc</i>     | <i>Recueil de la législation des sociétés et associations</i> , Central Legislation Department, 2003                                                                                                                                                                                                                                                                            |
| <i>Rép not</i>         | <i>Répertoire notarial</i> (Belgium)                                                                                                                                                                                                                                                                                                                                            |
| <i>Rev Banque</i>      | <i>Revue de la Banque</i> (Belgium)                                                                                                                                                                                                                                                                                                                                             |
| <i>Rev prat soc</i>    | <i>Revue pratique des sociétés</i> (Belgium)                                                                                                                                                                                                                                                                                                                                    |
| <i>Rev soc</i>         | <i>Revue des sociétés</i> (France)                                                                                                                                                                                                                                                                                                                                              |
| <i>Rev trim dr civ</i> | <i>Revue trimestrielle de droit civil</i> (France)                                                                                                                                                                                                                                                                                                                              |
| SA                     | <i>Société anonyme</i> (limited company)                                                                                                                                                                                                                                                                                                                                        |
| SARL                   | <i>Société à responsabilité limitée</i> (private limited company)                                                                                                                                                                                                                                                                                                               |
| SCA                    | <i>Société en commandite par actions</i> (partnership limited by shares)                                                                                                                                                                                                                                                                                                        |
| SCS                    | <i>Société en commandite simple</i> (limited partnership)                                                                                                                                                                                                                                                                                                                       |
| SE                     | <i>Société européenne</i> (European company)                                                                                                                                                                                                                                                                                                                                    |
| SICAF                  | <i>Société d'investissement à capital fixe</i> (investment company with fixed capital)                                                                                                                                                                                                                                                                                          |
| SICAR                  | <i>Société d'investissement en capital à risque</i> (investment company in risk capital)                                                                                                                                                                                                                                                                                        |
| SICAV                  | <i>Société d'investissement à capital variable</i> (investment company with variable capital)                                                                                                                                                                                                                                                                                   |
| SIF                    | Specialized investment fund                                                                                                                                                                                                                                                                                                                                                     |
| Trib arr               | <i>Tribunal d'arrondissement</i> (District Court)                                                                                                                                                                                                                                                                                                                               |

## *List of Abbreviations*

|       |                                                                  |
|-------|------------------------------------------------------------------|
| UCI   | Undertaking for collective investment                            |
| UCITS | Undertaking for collective investment in transferable securities |
| VAT   | Value added tax                                                  |
| VaR   | <i>Value at Risk</i>                                             |

### **Legislation and Circulars**

|                         |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                         |
|-------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 1915 Act                | Act of 10 August 1915 on commercial companies ( <i>Rec Lég Soc</i> 41)                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                  |
| 1929 Act                | Act of 31 July 1929 on the taxation of financial holding companies ( <i>Rec Lég Soc</i> , 249)                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                          |
| 1983 Act                | Act of 25 August 1983 on undertakings for collective investment ( <i>Mémorial A</i> 1983, 1462)                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                         |
| 1988 Act                | Act of 30 March 1988 on undertakings for collective investment ( <i>Rec Lég Soc</i> , 375)                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                              |
| 1991 Act                | Act of 19 July 1991 on undertakings for collective investment the securities of which are not intended to be placed with the public ( <i>Rec Lég Soc</i> , 463)                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                         |
| 1993 Act                | Act of 5 April 1993 on the financial sector ( <i>Rec Lég Pl Fin</i> 97)                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                 |
| Act of 23 December 1998 | Act of 23 December 1998 establishing a supervisory commission for the financial sector ( <i>Commission de Surveillance du Secteur Financier</i> ) ( <i>Mémorial A</i> 1998, 2985)                                                                                                                                                                                                                                                                                                                                                                                                                                                                                       |
| 2002 Act                | Act of 20 December 2002 on undertakings for collective investment and amending the Act of 12 February 1979, as amended, on value added tax ( <i>Rec Lég Soc</i> 413)                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                    |
| Act of 22 March 2004    | Act of 22 March 2004 on securitisation and amending: <ul style="list-style-type: none"> <li>• the Act of 5 April 1993, as amended, on the financial sector;</li> <li>• the Act of 23 December 1998, as amended, creating a commission for the supervision of the financial sector (<i>Commission de Surveillance du Secteur Financier</i>);</li> <li>• the Act of 27 July 2003 on trusts and fiduciary contracts;</li> <li>• the Act of 4 December 1967, as amended, on income tax;</li> <li>• the Act of 16 October 1934, as amended, on wealth tax;</li> <li>• the Act of 12 February 1979, as amended, on value added tax;</li> </ul> ( <i>Mémorial A</i> 2004, 720) |
| Act of 15 June 2004     | Act of 15 June 2004 on the investment company in risk capital (SICAR) ( <i>Mémorial A</i> 2004, 1568)                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                   |
| Act of 12 November 2004 | Act of 12 November 2004 on the prevention of money laundering and terrorist financing, transposing Directive (EC) 2001/97 of the European Parliament and of the Council of 4 December 2001 amending Council Directive                                                                                                                                                                                                                                                                                                                                                                                                                                                   |

(EEC) 91/308 on prevention of the use of the financial system for the purpose of money laundering and amending:

- the Criminal Code;
  - the Criminal Investigation Code;
  - the Act of 7 March 1980, as amended, on the judicial organization;
  - the Act of 23 December 1998, as amended, creating a commission for the supervision of the financial sector (*Commission de Surveillance du Secteur Financier*);
  - the Act of 5 April 1993, as amended, on the financial sector;
  - the Act of 6 December 1991, as amended, on the insurance sector;
  - the Act of 9 December 1976, as amended, on the organization of the notarial profession;
  - the Act of 10 August 1991, as amended, on the legal profession;
  - the Act of 28 January 1984, as amended, on the organization of the profession of independent auditors;
  - the Act of 10 June 1999 on the organization of the profession of qualified accountants;
  - the Act of 20 April 1977, as amended, on the exploitation of gambling and betting on sports;
  - the General Tax Code (*Abgabenordnung*);
- (*Mémorial A* 2004, 2766)

Act of 10 July 2005

Act of 10 July 2005 on prospectuses for transferable securities:

- transposing Directive (EC) 2003/71 of the European Parliament and of the Council of 4 November 2003 on the prospectus to be published when securities are offered to the public or admitted to trading and amending Directive (EC) 2001/34;
- amending the Act of 23 December 1998 creating a commission for the supervision of the financial sector (*Commission de Surveillance du Secteur Financier*);
- amending the Act of 23 December 1998 on supervision of the markets in financial assets;
- amending the Act of 30 March 1988 on undertakings for collective investment;
- amending the Act of 20 December 2002 on undertakings for collective investment;
- amending the Act of 15 June 2004 on investment companies in risk capital;
- amending the Act of 10 August 1915 on commercial companies;

(*Mémorial A* 2005, 1726)

- Act of 25 August 2006      Act of 25 August 2006:
- on the European company (SE), the *société anonyme à directoire et conseil de surveillance* and the *société anonyme unipersonnelle*;
  - amending the amended Act of 10 August 1915 on commercial companies and certain other legal provisions;
  - amending the Act of 19 December 2002 on the Trade and Companies Register and the accounting and annual financial statements of companies;
  - amending the amended Act of 30 March 1988 on undertakings for collective investment;
  - amending the Act of 20 December 2002 on undertakings for collective investment;
  - amending the Act of 25 July 1990 on the status of directors representing the State or a legal person under public law in an SA;
  - amending the Act of 4 December 1992 on the information to be disclosed when acquiring and divesting a material holding in a company listed on the stock exchange;
  - amending the Act of 13 July 2005 on professional retirement institutions in the form of SEPCAVs and ASSEPs;
- (*Mémorial A* 2006, 2684)
- Act of 13 February 2007      Act of 13 February 2007 relating to specialized investment funds (SIFs) and amending:
- the amended Act of 20 December 2002 on undertakings for collective investment;
  - the amended Act of 12 February 1979 concerning value added tax;
- (*Mémorial A* 2007, 368)
- Act of 13 July 2007      Act of 13 July 2007 on markets in financial instruments transposing:
- Directive (EC) 2004/39 of the European Parliament and of the Council of 21 April 2004 on markets in financial instruments amending Council Directives (EEC) 85/611 and (EEC) 93/6 and Directive (EC) 2000/12 of the European Parliament and of the Council and repealing Council Directive (EEC) 93/22;
  - Article 52 of Commission Directive (EC) 2006/73 of 10 August 2006 implementing Directive (EC) 2004/39 of the European Parliament and of the Council as regards organizational requirements and operating conditions for investment firms and defined terms for the purposes of that Directive;

|                |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                            |
|----------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
|                | and amending:                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                              |
|                | <ul style="list-style-type: none"> <li>• the Act of 5 April 1993, as amended, on the financial sector,</li> <li>• the Act of 20 December 2002, as amended, on undertakings for collective investment,</li> <li>• the Act of 12 November 2004 on combating money laundering and terrorist financing,</li> <li>• the Act of 31 May 1999, as amended, on company domiciliation,</li> <li>• the Act of 23 December 1998, as amended, creating a commission for the supervision of the financial sector (<i>Commission de Surveillance du Secteur Financier</i>),</li> <li>• the Act of 6 December 1991, as amended, on the insurance sector,</li> <li>• the Act of 3 September 1996 concerning the involuntary dispossession of bearer securities,</li> <li>• the Act of 23 December 1998 concerning the monetary status and the central bank of Luxembourg (<i>Banque centrale du Luxembourg</i>),</li> </ul> |
|                | and repealing:                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                             |
|                | <ul style="list-style-type: none"> <li>• the Act of 23 December 1998, as amended, on supervision of the markets in financial assets,</li> <li>• the Act of 21 June 1984, as amended, on futures markets (<i>Mémorial A 2007</i>, 2076)</li> </ul>                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                          |
| Circular 91/75 | IML Circular 91/75 of 21 January 1991                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                      |
| Circular 00/14 | CSSF Circular 00/14 of 27 July 2000 on the adoption of the Act of 17 July 2000 amending certain provisions in the Act of 30 March 1988 with regard to undertakings for collective investment                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                               |
| Circular 02/77 | CSSF Circular 02/77 of 27 November 2002 on the protection of investors in the event of NAV calculation error and correction of the consequences resulting from non-compliance with the investment rules applicable to undertakings for collective investment                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                               |
| Circular 02/80 | CSSF Circular 02/80 of 5 December 2002 on the specific rules applicable to Luxembourg undertakings for collective investment ('UCI') pursuing alternative investment strategies                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                            |
| Circular 02/81 | CSSF Circular 02/81 of 6 December 2002 on guidelines concerning the duties of auditors of undertakings for collective investment                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                           |
| Circular 03/87 | CSSF Circular 03/87 of 21 January 2003 on the coming into force of the Act of 20 December 2002 on undertakings for collective investment                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                   |
| Circular 03/88 | CSSF Circular 03/88 of 22 January 2003 on the classification of undertakings for collective investment governed by the                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                     |

## *List of Abbreviations*

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|                 |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                    |
|-----------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
|                 | provisions of the Act of 20 December 2002 on undertakings for collective investment                                                                                                                                                                                                                                                                                                                                                                                                |
| Circular 03/97  | CSSF Circular 03/97 of 28 February 2003 on the publication in the electronic database for the financial centre ( <i>'référentiel de la place'</i> ) of simplified and full prospectuses and the annual and half-yearly reports by undertakings for collective investment                                                                                                                                                                                                           |
| Circular 03/108 | CSSF Circular 03/108 of 30 July 2003 on Luxembourg management companies subject to Chapter 13 of the Act of 20 December 2002 on undertakings for collective investment, and Luxembourg self-managed investment companies subject to Article 27 or Article 40 of the Act of 20 December 2002                                                                                                                                                                                        |
| Circular 03/122 | CSSF Circular 03/122 of 19 December 2003 on clarifications concerning the simplified prospectus                                                                                                                                                                                                                                                                                                                                                                                    |
| Circular 04/146 | CSSF Circular 04/146 of 17 June 2004 on the protection of undertakings for collective investment and their investors against late trading and market timing practices                                                                                                                                                                                                                                                                                                              |
| Circular 04/151 | CSSF Circular 04/151 of 13 July 2004 on the information to be published in the listing particulars of the securities specified below: <ul style="list-style-type: none"><li>• shares and units of foreign UCIs whose securities are not publicly available, offered or sold in or from Luxembourg, and</li><li>• securities redeemable or exchangeable for shares or units of UCIs or whose income and/or redemption is/are linked to underlying shares or units of UCIs</li></ul> |
| Circular 04/155 | CSSF Circular 04/155 of 27 September 2004 on the compliance function                                                                                                                                                                                                                                                                                                                                                                                                               |
| Circular 05/176 | CSSF Circular 05/176 of 5 April 2005 on the rules of conduct to be adopted by undertakings for collective investment in transferable securities in relation to the use of financial derivative instruments                                                                                                                                                                                                                                                                         |
| Circular 05/177 | CSSF Circular 05/177 of 6 April 2005 on the abolition of any prior approval by the CSSF of advertising material issued by persons and companies supervised by the CSSF; revocation of point II of Chapter L of IML Circular 91/75; revocation of the two last sentences of point IV 5.11 of CSSF Circular 2000/15                                                                                                                                                                  |
| Circular 05/178 | CSSF Circular 05/178 of 11 April 2005 on administrative and accounting organization; outsourcing of IT services; revocation of point 4.5.2 of IML Circular 96/126 and replacement by point 4.5.2 of this Circular                                                                                                                                                                                                                                                                  |
| Circular 05/185 | CSSF Circular 05/185 of 24 May 2005 on Luxembourg management companies subject to the provisions of                                                                                                                                                                                                                                                                                                                                                                                |

|                 |                                                                                                                                                                                                                                                                                                                                                                                                            |
|-----------------|------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
|                 | Chapter 13 of the Act of 20 December 2002 relating to undertakings for collective investment, as well as Luxembourg self-managed investment companies subject to the provisions of Article 27 or Article 40 of the Act of 20 December 2002 relating to undertakings for collective investment                                                                                                              |
| Circular 05/186 | CSSF Circular 05/186 of 25 May 2005 on the guidelines of the Committee of European Securities Regulators (CESR) regarding the application of transitional measures resulting from Directives (EC) 2001/107 and (EC) 2001/108 (UCITS III) amending Directive (EEC) 85/611 (UCITS I)                                                                                                                         |
| Circular 05/188 | CSSF Circular 05/188 of 27 May 2005 on the coming into force of the Act of 12 November 2004 on combating money laundering and terrorist financing                                                                                                                                                                                                                                                          |
| Circular 05/210 | CSSF Circular 05/210 of 10 October 2005 on the drawing-up of a simplified prospectus within the scope of Chapter 1 of Part III of the Act on prospectuses for securities                                                                                                                                                                                                                                   |
| Circular 05/211 | CSSF Circular 05/211 of 13 October 2005 on combating money laundering and terrorist financing and prevention of the use of the financial sector for the purpose of money laundering and terrorist financing                                                                                                                                                                                                |
| Circular 05/225 | CSSF Circular 05/225 of 16 December 2005 on the concept of 'offer to the public of securities' as defined in the Act on prospectuses for securities and the consequential 'obligation to publish a prospectus'                                                                                                                                                                                             |
| Circular 05/226 | CSSF Circular 05/226 of 16 December 2005 on a general overview of the Act on prospectuses for securities and technical specifications regarding communication to the CSSF of documents with a view to authorization or for filing and of notices for offers to the public and admissions to trading on a regulated market                                                                                  |
| Circular 06/241 | CSSF Circular 06/241 of 5 April 2006 on the concept of risk capital under the Act of 15 June 2004 relating to the investment company in risk capital (SICAR)                                                                                                                                                                                                                                               |
| Circular 06/267 | CSSF Circular 06/267 of 22 November 2006 on technical specifications regarding the filing with the CSSF, in accordance with the Act on prospectuses for securities, of documents for approval or notification purposes and of notices for offers to the public of units/shares of Luxembourg closed-end UCIs and admissions of units/shares of Luxembourg closed-end UCIs to trading on a regulated market |
| Circular 06/272 | CSSF Circular 06/272 of 21 December 2006 on technical specifications regarding the filing with the CSSF, in accordance with the Act on prospectuses for securities,                                                                                                                                                                                                                                        |

|                 |                                                                                                                                                                                                                                                                                                                                                                                                   |
|-----------------|---------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
|                 | of documents for approval or notification purposes and of notices for offers to the public of securities issued by SICARs and admissions of securities issued by SICARs to trading on a regulated market                                                                                                                                                                                          |
| Circular 07/277 | CSSF Circular 07/277 of 9 January 2007 on the new notification procedure following guidelines issued by the Committee of European Securities Regulators (CESR) regarding the simplification of the UCITS notification procedure                                                                                                                                                                   |
| Circular 07/283 | CSSF Circular 07/283 of 28 February 2007 on the entry into force of the Act of 13 February 2007 relating to specialized investment funds                                                                                                                                                                                                                                                          |
| Circular 07/290 | CSSF Circular 07/290 of 3 May 2007 on the definition of capital ratios pursuant to Article 56 of the amended Law of 5 April 1993 on the financial sector (application to investment firms and management companies subject to Chapter 13 of the Law of 20 December 2002, as amended)                                                                                                              |
| Circular 07/307 | CSSF Circular 07/307 of 31 July 2007 on the MiFID: Conduct of business rules in the financial sector                                                                                                                                                                                                                                                                                              |
| Circular 07/308 | CSSF Circular 07/308 of 2 August 2007 on the rules of conduct to be adopted by undertakings for collective investment in transferable securities with respect to the use of a methodology for the management of financial risk, and the use of derivative financial instruments                                                                                                                   |
| Circular 07/309 | CSSF Circular of 3 August 2007 on risk spreading in the context of specialized investment funds (SIFs)                                                                                                                                                                                                                                                                                            |
| Circular 07/310 | CSSF Circular of 3 August 2007 on financial information to be provided by specialized investment funds (SIFs), as amended by CSSF Circular 08/348                                                                                                                                                                                                                                                 |
| Circular 08/339 | CSSF Circular 08/339 of 19 February 2008 on the guidelines of the Committee of European Securities Regulators (CESR) concerning eligible assets for investment by UCITS                                                                                                                                                                                                                           |
| Circular 08/348 | CSSF Circular 08/348 of 17 April 2008 on the changes to circulars IML 97/136 and CSSF 07/310                                                                                                                                                                                                                                                                                                      |
| Circular 08/350 | CSSF Circular 08/350 of 22 April 2008 on clarifications relating to the amendments introduced by the Act of 13 July 2007 on markets in financial instruments to the status of professionals of the financial sector (PFS) referred to in Articles 29-1, 29-2, 29-3, or 29-4 and designated as 'support PFS', as well as on the amendment to the prudential supervisory procedures for support PFS |
| Circular 08/356 | CSSF Circular 08/356 of 4 June 2008 regarding rules applicable to UCIs which employ certain techniques and instruments relating to transferable securities and money market instruments                                                                                                                                                                                                           |

### *List of Abbreviations*

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|----------------------------|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| Directive 85/611           | Council Directive (EEC) 85/611 of 20 December 1985 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS), as amended [1985] OJ L375/3                                                                                                                                              |
| Directive 93/22            | Council Directive (EEC) 93/22 of 10 May 1993 on investment services in the securities field [1993] OJ L141/27. Directive (EEC) 93/22 was repealed by Directive (EC) 2004/39 (MiFID). Its repeal took effect on 1 November 2007 (Article 69 of Directive (EC) 2004/39 as amended by Directive (EC) 2006/31 of 5 April 2006 [2006] OJ L114/60                                               |
| Directive 2001/97          | Directive (EC) 2001/97 of the European Parliament and of the Council of 4 December 2001 amending Directive (EEC) 91/308 of the Council on prevention of the use of the financial system for the purpose of money laundering [2001] OJ L344/76                                                                                                                                             |
| Directive 2001/107         | Directive (EC) 2001/107 of the European Parliament and of the Council of 21 January 2002 amending Council Directive (EEC) 85/611 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) with a view to regulating management companies and simplified prospectuses [2002] OJ L41/20 |
| Directive 2001/108         | Directive (EC) 2001/108 of the European Parliament and of the Council of 21 January 2002 amending Council Directive (EEC) 85/611 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS), with regard to investments of UCITS [2002] OJ L41/35                                       |
| Directive 2003/6           | Directive (EC) 2003/6 of the European Parliament and of the Council of 28 January 2003 on insider dealing and market manipulation (market abuse) [2003] OJ L96/16                                                                                                                                                                                                                         |
| Directive 2003/48          | Directive (EC) 2003/48 of the European Parliament and of the Council of 3 June 2003 on the taxation of savings income in the form of interest payments [2003] OJ L157/38                                                                                                                                                                                                                  |
| Directive 2003/71          | Directive (EC) 2003/71 of the European Parliament and of the Council of 4 November 2003 on the prospectus to be published when securities are offered to the public or admitted to trading, and amending Directive (EC) 2001/34 [2003] OJ L345/65                                                                                                                                         |
| Directive 2004/39 or MiFID | Directive (EC) 2004/39, 'MiFID' (Market in Financial Instruments Directive) of the European Parliament and of the Council of 21 April 2004 on markets in financial instruments amending Council Directives (EEC) 85/611 and (EEC) 93/6 and Directive (EC) 2000/12 of the European                                                                                                         |

|                                                |                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                                         |
|------------------------------------------------|-----------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
|                                                | Parliament and of the Council and repealing Council Directive (EEC) 93/22 [2004] OJ L145/1 with effect from 1 November 2007 (Article 69 of Directive (EC) 2004/39 as amended by Directive (EC) 2006/31 of 5 April 2006 [2006] OJ L114/60)                                                                                                                                                                                                                                                                                               |
| Directive 2006/48                              | Directive (EC) 2006/48 of the European Parliament and of the Council of 14 June 2006 relating to the taking up and pursuit of the business of credit institutions (recast) [2006] L177/1                                                                                                                                                                                                                                                                                                                                                |
| Directive 2006/73                              | Commission Directive (EC) 2006/73 of 10 August 2006 implementing Directive (EC) 2004/39 of the European Parliament and of the Council as regards organizational requirements and operating conditions for investment firms and defined terms for the purposes of that Directive [2006] OJ L241/26                                                                                                                                                                                                                                       |
| Directive 2007/16 or Eligible Assets Directive | Commission Directive (EC) 2007/16 of 19 March 2007 implementing Council Directive (EEC) 85/611 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) as regards the clarification of certain definitions [2007] OJ L79/11                                                                                                                                                                                                        |
| EC Treaty                                      | Treaty constituting the European Community, consolidated version published in 2002 OJ C325/33                                                                                                                                                                                                                                                                                                                                                                                                                                           |
| Grand-Ducal Regulation of 13 July 2007         | Grand-Ducal Regulation of 13 July 2007 relating to the organizational requirements and the rules of conduct in the financial sector and transposing Commission Directive (EC) 2006/73 of 10 August 2006 implementing Directive (EC) 2004/39 of the European Parliament and of the Council as regards organizational requirements and operating conditions for investment firms and defined terms for the purposes of that Directive ( <i>Mémorial A</i> 2007, 2134)                                                                     |
| Grand-Ducal Regulation of 8 February 2008      | Grand-Ducal Regulation of 8 February 2008 relating to certain definitions of the law of 20 December 2002 as amended concerning undertakings for collective investment and implementing Commission Directive (EC) 2007/16 of 19 March 2007 implementing Council Directive (EEC) 85/611 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS) as regards the clarification of certain definitions ( <i>Mémorial A</i> , 2008, 303) |

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# 1

## INTRODUCTION

|                                                                                                                        |      |                                                                               |      |
|------------------------------------------------------------------------------------------------------------------------|------|-------------------------------------------------------------------------------|------|
| <b>Definition of Undertaking for Collective Investment</b>                                                             |      | Act of 20 December 2002 with regard to undertakings for collective investment | 1.46 |
| <b>Investment</b>                                                                                                      | 1.01 |                                                                               |      |
| <i>Collective investment of savings</i>                                                                                | 1.03 | Act of 13 February 2007 relating to specialized investment funds              | 1.66 |
| <i>Investment according to the principle of risk spreading</i>                                                         | 1.05 | Circulars issued by the supervisory authorities                               | 1.67 |
| <i>Raising capital from the public</i>                                                                                 | 1.06 | <i>Laws and regulations not limited to UCIs</i>                               | 1.74 |
| <b>Historical Background</b>                                                                                           | 1.13 | <b>Role of the CSSF</b>                                                       | 1.77 |
| <b>Legal Sources</b>                                                                                                   | 1.23 | <i>General presentation</i>                                                   | 1.77 |
| <i>Specific laws and regulations applicable to UCIs</i>                                                                | 1.23 | <i>Supervision of UCIs</i>                                                    | 1.81 |
| Chronological record of laws and regulations                                                                           | 1.23 | UCIs established in the Grand Duchy of Luxembourg                             | 1.81 |
| Grand-Ducal Decree of 22 December 1972 concerning the supervision of investment funds                                  | 1.23 | UCIs established in foreign countries                                         | 1.86 |
| 1983 Act concerning undertakings for collective investment                                                             | 1.26 | Coordinated UCITS                                                             | 1.86 |
| 1988 Act concerning undertakings for collective investment                                                             | 1.32 | Other UCIs under foreign law                                                  | 1.89 |
| Act of 19 July 1991 concerning undertakings for collective investment whose securities are not intended for the public | 1.45 | <i>Supervision of management companies</i>                                    | 1.91 |
|                                                                                                                        |      | Management companies established in the Grand Duchy of Luxembourg             | 1.91 |
|                                                                                                                        |      | Management companies established in foreign countries                         | 1.94 |

### Definition of Undertaking for Collective Investment

Rather than introducing a general definition of undertaking for collective investment (UCI), the authors of the 2002 Act, in line with the 1988 Act, sought to define its constituent elements. Three basic criteria are required to constitute a UCI. A UCI is an investment structure: **1.01**

- (1) the exclusive object of which is the collective investment of savings;

- (2) which invests in assets (transferable securities or other assets) and operates in accordance with the principle of risk spreading;
- (3) the funds of which, used for collective investment, have been raised from the public.

**1.02** The first two criteria must always be met. The last—the raising of funds from the public—may be dispensed with in certain cases specified by law. All of these criteria were considered and clarified by the CSSF, the prudential authority for UCIs, in Circular 91/75.<sup>1</sup>

### *Collective investment of savings*

**1.03** The collective investment of savings is defined as the common investment of a number of individual investment contributions raised from the public. They may be invested in transferable securities or other assets.

**1.04** Investment suggests that the purchase or sale of portfolio assets is carried out solely with the objective of generating a yield or capital gains. In contrast with other types of financial vehicles, a UCI does not acquire interests in order to obtain influence or control, albeit certain UCIs, such as those investing in venture capital assets, can in fact hold significant interests in certain companies. However, even in those circumstances, the UCI's main purpose is not to exercise control over the target company but rather to generate a return. The objective of a UCI is to show a capital gain once the company is sufficiently mature.

### *Investment according to the principle of risk spreading*

**1.05** Spreading investment risks avoids the excessive concentration of a UCI's investments and reduces investment risk. A minimum level of diversification of investments between assets of different types and issuers is required, although this requirement is interpreted differently, depending on the type of UCI.

### *Raising capital from the public*

**1.06** Capital is raised from 'the public' when it is raised from a group of investors which extends beyond a 'small circle of persons'.<sup>2</sup> There is no fixed minimum threshold beyond which the target investors cease to be a 'small circle of persons'.

---

<sup>1</sup> Ch B, I, Circular 91/75. A fourth criterion, not included as such in Circular 91/75, stipulates that Luxembourg-based UCIs must issue units or securities in accordance with Arts 2(2), 65(1), 69, and 73 of the 2002 Act. This requirement excludes certain structures from the scope of the legislation governing UCIs. See 2.161 below.

<sup>2</sup> Ch B, I, Circular 91/75.

The threshold in question is considered on a case-by-case basis by the CSSF, which does not, for example, regard family holding companies and investment clubs as collecting savings from the public albeit they are 'pursuing the objective of the collective investment of savings'.<sup>3</sup>

In the course of Parliamentary debates prior to the enactment of the 2002 Act it had been proposed not to regulate groups of investors comprising fewer than twenty persons.<sup>4</sup> An undertaking that does not wish to place its units with a larger number of investors therefore would not have come within the sphere of the 2002 Act. However, the legislation did not expressly provide for this clarification. **1.07**

In addition the launch by a promoter of a UCI intended to be sold only to entities within its own group, is not a 'public' offering of units. Investors should be sought from 'outside' the group of companies rather than 'within' the relevant corporate group. A public offer is effected only when marketing efforts are targeted at a promoter's clientele or the clientele of one or more group entities. **1.08**

A UCI must intend to place its units or shares with the public, regardless of whether or not it achieves this result. Failure to sell to the public does not automatically result in failure to satisfy the requirement, provided the UCI can demonstrate its bona fide intention to market its units or shares to the public. **1.09**

There is no other definition of the term 'public'. The investor can be either institutional or private and an investor in the case of a 'public' offer is not required to meet any requirement as to status or capacity. **1.10**

However, the term 'public' can have several meanings in the context of UCIs, depending on the situation. For example, in the context of raising funds for a UCI, it means a relatively large group of persons. In contrast, in other circumstances, it can be used to distinguish the type of investor concerned, for example to draw a distinction between well-informed investors and the 'general public'. This distinction is highly relevant in differentiating the scope of the 2002 Act and the Act of 13 February 2007 respectively. The 2002 Act refers to the public as an 'unrestricted circle of persons' whereas the Act of 13 February 2007, in limiting the eligibility of investors in funds authorized under the Act of 13 February 2007, to well-informed investors, refers to 'the public' as any investor who is not well informed. **1.11**

Thus, it is not always necessary for a UCI to raise capital from the 'public'. The Act of 13 February 2007 permits the creation of UCIs 'whose units or shares are sold to one or more well-informed investors', and UCIs authorized under the Act of **1.12**

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<sup>3</sup> Ch B, II, Circular 91/75.

<sup>4</sup> This figure is mentioned in the Parliamentary documents for the Act of 2 August 2003, which amended the 1993 Act (*Parliamentary doc* No 5085, Explanatory Statement, 14).

13 February 2007 will therefore not necessarily raise funds from ‘an unrestricted circle of persons’, ie the ‘public’ as defined in the 2002 Act,<sup>5</sup> and can, indeed must, target a select investor group.<sup>6</sup>

## Historical Background

- 1.13** UCIs have existed since the late nineteenth century, even though they only came into their own in the twentieth century. For instance, the years between 1880 and 1900 saw the rise in Scotland of the investment trust company whose objective was to invest in farm mortgages.<sup>7</sup> This Scottish innovation subsequently crossed the Atlantic to the United States, where it became a popular investment vehicle, especially after the First World War. Emboldened by their success, the managers of such investment companies borrowed increasingly large amounts for investment purposes. The assets managed by some of those companies were out of all proportion to their share capital, resulting in their demise during the Wall Street crash of 1929.
- 1.14** The Wall Street crash led to an increased interest by US investors in another type of UCI, the unit trust rather than a corporate structure. First constituted in England in 1868, this type of UCI initially ran into legal difficulties. One judge considered it a breach of English company law. While that judgment was overturned on appeal, it prompted the conversion into limited liability companies or liquidation of many such trusts.
- 1.15** In unit trusts, securities are bought and vested in a trustee, generally a regulated institution such as a bank or an insurance company. In return for payment/subscriptions for units, investors become the trust’s beneficiaries and are issued with ‘units’ representing their rights. The management of a trust’s portfolio is entrusted to a management company separate and distinct from the trustee.
- 1.16** The unit trust structure offered two major advantages compared with investment companies. First, securities acquired by a trust were held in the custody of a trustee

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<sup>5</sup> An investment structure that does not canvass the public is not necessarily governed by the Act of 13 February 2007. An undertaking engaged in the collective investment of assets according to the principle of risk spreading, which reserves its units or shares for well-informed investors and does not canvass the public for funds, may either opt for application of the Act of 13 February 2007 and the regulations laid down by the CSSF or adopt, for example, the status of a non-regulated financial company whose activity is not supervised by the CSSF. For further explanations about these aspects, see 2.85 and 2.86 below.

<sup>6</sup> Art 1(1), Act of 13 February 2007, under which SIFs may reserve their securities for ‘one or several well-informed investors’.

<sup>7</sup> The following discussion is mainly drawn from CO Merriman, *Unit Trusts and How They Work* (Pitman & Sons, 2nd edn, 1959) 1–10.

who was independent from the management company. Secondly, trust participants could at any time sell their units back to the trust, whereas an investment company was not entitled to buy back its own shares.

It was another fifty years before these structures re-emerged in Europe. The first Swiss trust was created in 1930. Similarly, the successful sale in Great Britain of units in US trusts prompted British financiers to revive this type of product in 1931. **1.17**

Nevertheless, the British investment community quickly distinguished itself from its American counterpart. Chastened by the lessons learnt from the crash of 1929, the Americans had laid down extremely rigid management rules, whereas the British introduced ever greater flexibility. In a US trust, the composition of the portfolio had to be settled once and for all, and securities could be sold only under extremely strict conditions. The conditions imposed on trusts set up under English law were, from the outset, more flexible. The managers of English trusts were gradually authorized to sell portfolio securities when they considered this to be in the best interests of the unitholders, thereby boosting the popularity of this type of trust, of which there were 98 in England by 1930, covered by special regulations under the Prevention of Fraud (Investments) 1939 Act, which came into force on 8 August 1944. **1.18**

The fund industry has continued to grow steadily ever since. In 1940, there were 111 investment funds in the United States, comprising 43 companies and 68 trusts. By 1957, there were 167 funds, comprising 24 companies and 143 trusts.<sup>8</sup> **1.19**

1959 saw the creation of the first investment fund in the Grand Duchy of Luxembourg, under the prescient name 'FCP Eurunion'.<sup>9</sup> Broadly inspired by the trust structure described above, this was built around three components: **1.20**

- (1) a depositary bank responsible for keeping the securities in safe custody and overseeing their management;
- (2) a management company responsible for managing and building up the portfolio;
- (3) unitholders, the joint owners of the securities portfolio.

The relationships between the three parties were governed by management regulations.

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<sup>8</sup> *ibid* 13.

<sup>9</sup> M-J Chèvremont, 'Évolution de l'industrie des fonds d'investissement en Europe et au Luxembourg en particulier', in *Les fonds d'investissement, réglementation-fiscalité-évolution*, Seminar held on 24 and 25 November 1988, *Association Luxembourgeoise des Juristes de Banque* (ALJB), *Institut Universitaire International Luxembourg* (IUIL) 5.

- 1.21** During the same period, ie in 1959 and 1960, the first incorporated investment funds emerged in the Grand Duchy of Luxembourg. In contrast with the English model, such companies were able to repurchase their own shares indirectly from their shareholders, under a structure involving the creation of a separate company known as a 'repurchase company'. Having waited a long time before creating a UCI based on the British model, the Grand Duchy of Luxembourg thus took an additional step, offering investors an opportunity that English investment companies were unable to provide.
- 1.22** Investment funds soon became an integral part of Luxembourg's investment scene, helped by a flexible and robust legal and regulatory environment, attractive tax treatment and the steadily growing expertise of local service providers. In 1970, there were 102 UCIs in the Grand Duchy of Luxembourg. In 2008, there are 3,105,<sup>10</sup> with aggregate net assets of €1,996,959 billion,<sup>11</sup> placing the Grand Duchy of Luxembourg second in the world behind the United States in terms of fund volumes.

## Legal Sources

### *Specific laws and regulations applicable to UCIs*

#### Chronological record of laws and regulations

##### *Grand-Ducal Decree of 22 December 1972 concerning the supervision of investment funds*

- 1.23** The Grand-Ducal Decree of 22 December 1972<sup>12</sup> was the first Luxembourg regulation to be adopted with regard to UCIs.<sup>13</sup> Prior to the adoption of that Decree, corporate UCIs had been created under the 1915 Act and for tax purposes were governed by the 1929 Act. This infrastructure was complemented by administrative decisions and recommendations, *inter alia*, from the Treasury Minister, the registration authority,<sup>14</sup> and the Banking Commissioner. This legal framework contained numerous loopholes and, especially for FCPs, turned out to be inadequate, as revealed by the IOS scandal towards the end of the 1960s.<sup>15</sup>

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<sup>10</sup> This figure comprises 1,259 traditional UCIs and 10,457 sub-funds of umbrella UCIs.

<sup>11</sup> Figures for 31 May 2008; source: monthly press release published by the CSSF on the general situation of UCIs (July 2008 edition).

<sup>12</sup> Grand-Ducal Decree of 22 December 1972 concerning the supervision of investment funds (*Mémorial A* 1972, 2112).

<sup>13</sup> In the Grand Duchy of Luxembourg, the term *fonds d'investissement*, which is a literal translation of the English *investment fund*, was used until the 1983 Act introduced the concept of 'undertaking for collective investment', also found in Directive (EEC) 85/611.

<sup>14</sup> *Administration de l'Enregistrement*.

<sup>15</sup> Following a large-scale advertising campaign, Investors Overseas Services (IOS) persuaded more than 700,000 persons to subscribe for units in two FCPs it had created in the Grand Duchy of Luxembourg: the International Investment Trust and the Fund of Funds. Management of these

The Grand-Ducal Decree of 22 December 1972 was adopted in response to the IOS scandal. The 1972 Decree defined the meaning of ‘investment funds’ for the first time<sup>16</sup> and conferred on the Banking Commissioner supervisory authority over all Luxembourg-based UCIs (whether of a contractual, corporate, or other type) and all foreign investment funds whose units or shares were offered to the public in or from the Grand Duchy of Luxembourg.<sup>17</sup> The Grand-Ducal Decree further required UCIs to have their accounts audited by an independent expert who, ‘whilst providing assurances as to his probity and professional qualifications’,<sup>18</sup> was also obliged to provide the Banking Commissioner with ‘all information or certificates required by the Commissioner in the areas of expertise of the expert in the performance of the audit’.<sup>19</sup> **1.24**

In regulations issued on 8 November 1974,<sup>20</sup> the Banking Commissioner set out the rules governing the monthly financial reports to be prepared and submitted by UCIs under his supervision. **1.25**

*1983 Act concerning undertakings for collective investment*

The rapid development of UCIs in the 1970s evidenced the need for more systematic regulation of the organization, operation, and supervision of collective investment undertakings. Initially presented in Parliament on 31 December 1979,<sup>21</sup> comprehensive legislation was finally adopted four years later in the form of the 1983 Act. **1.26**

In the preamble to the Bill, the government noted the absence of specific regulations governing UCIs and stated that ‘in order to protect savings, there is clearly an urgent need to specify the legal basis for such undertakings and to enact operating rules to eliminate any legal uncertainty in this area’.<sup>22</sup> **1.27**

At the time, the government was aware of the need to align the regime for Luxembourg-based UCIs with European Community law. In Parliamentary documents, it stressed the need to ‘provide the parties concerned with an instrument capable of surviving, without amendment, the transposition into national law of EEC directives’.<sup>23</sup> **1.28**

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UCIs was a disaster. Moreover, their assets had no genuine substance. The investors lost nearly their entire investment.

<sup>16</sup> Art 1(1) of the Grand-Ducal Decree of 22 December 1972 concerning the supervision of investment funds (*Mémorial A* 1972, 2112).

<sup>17</sup> *ibid* Art 1(2).

<sup>18</sup> *ibid* Art 3(1).

<sup>19</sup> *ibid* Art 3(2).

<sup>20</sup> Approved by Ministerial Decree of 19 November 1974 concerning the approval of Banking Commissioner Reg No VM/1 of 8 November 1974 concerning the monthly financial reports to be prepared and submitted by the investment funds under his supervision (*Mémorial A* 1974, 1718).

<sup>21</sup> *Parliamentary doc* No 2366, Contents, 1.

<sup>22</sup> *ibid* Preamble, 18.

<sup>23</sup> *ibid* Preamble, 17.

- 1.29** The 1983 Act specifically governed the operation of FCPs. It introduced the SICAV, inspired by French legislation, into Luxembourg law. It also provided the legal framework for the other structures available to Luxembourg-based UCIs, and confirmed earlier regulations on the public offerings of units or shares in foreign UCIs in or from the Grand Duchy of Luxembourg.
- 1.30** The Grand-Ducal Regulation of 25 August 1983<sup>24</sup> determined the amount of fixed capital duty applicable to UCIs governed by the 1983 Act.
- 1.31** This was followed by the Grand-Ducal Regulation of 29 December 1983,<sup>25</sup> which laid down the rules governing the publication and filing of financial statements and reports by UCIs subject to supervision by the *Institut Monétaire Luxembourgeois*, which had succeeded<sup>26</sup> the Banking Commissioner under the Act of 20 May 1983.<sup>27</sup>

*1988 Act concerning undertakings for collective investment*

- 1.32 Content** Already in the pipeline when the 1983 Act was approved, Directive 85/611 (the UCITS Directive) was adopted two years later and transposed into Luxembourg law by the 1988 Act.
- 1.33** The Directive coordinates the legislation of EEA Member States with regard to UCIs which invest in transferable securities and—since 2003—in other liquid financial assets (UCITS). It does not deal with other types of UCI, which Member States are free to regulate under local law and regulation.
- 1.34** Directive 85/611 could have been transposed into Luxembourg law simply by amending the 1983 Act. The government nevertheless felt that, ‘in order to improve the previous regime in certain areas and . . . to permit broader application of the instrument of undertakings for collective investment’, it was necessary to ‘review the entire subject-matter and to develop a law governing all undertakings for collective investment’.<sup>28</sup>

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<sup>24</sup> Grand-Ducal Regulation of 25 August 1983 determining the fixed duty applicable to the capital collected in undertakings for collective investment governed by the Act of 25 August 1983 (*Mémorial A* 1983, 1476).

<sup>25</sup> Grand-Ducal Regulation of 29 December 1983 concerning the publication and periodic submission of financial statements and reports by UCIs subject to supervision by the *Institut Monétaire Luxembourgeois* (*Mémorial A* 1983, 2676).

<sup>26</sup> Art 30, Act of 20 May 1983.

<sup>27</sup> Act of 20 May 1983 concerning the creation of the *Institut Monétaire Luxembourgeois* (*Mémorial A* 1983, 915), as amended by the Acts of 24 December 1984 (*Mémorial A* 1984, 2103), 22 December 1986 (*Mémorial A* 1986, 2403), 21 September 1990 (*Mémorial A* 1990, 734), 16 August 1991 (*Mémorial A* 1991, 1253), 5 April 1993 (*Mémorial A* 1993, 462), 23 December 1995 (*Mémorial A* 1995, 2303) and 22 April 1998 (*Mémorial A* 1998, 466).

<sup>28</sup> *Parliamentary doc* No 3172, Preamble, 32.

A Grand-Ducal Regulation of 30 March 1988<sup>29</sup> determined the amount of the fixed capital duty applicable to UCIs governed by the 1988 Act, without changing the situation which had existed since 1983. **1.35**

The 1988 Act was repealed by the 2002 Act with effect from 13 February 2007. During the interim period, the two laws coexisted under a parallel system. **1.36**

Because the 2002 Act contains most of the provisions of the 1988 Act, many comments on the 1988 Act, particularly the Parliamentary documents preceding its enactment, remain relevant and the 1988 Act will be frequently referred to in this work. **1.37**

### Amendment of the 1988 Act

*Act of 23 December 1994* The Act of 23 December 1994<sup>30</sup> introduced the first change in the rate of the annual subscription tax paid by Luxembourg-based UCIs, as this tax had proved to be a disincentive for certain types of UCI wishing to establish in the Grand Duchy of Luxembourg, particularly in money market funds. **1.38**

This Act reduced the subscription tax to 0.03 per cent for UCIs investing in money market instruments or cash and subscriptions by Luxembourg UCIs into other Luxembourg-based UCIs. The conditions for the application of the reduced tax rate and the qualifying criteria for money market instruments were set out in a Grand-Ducal Regulation of 14 April 1995.<sup>31</sup> **1.39**

*Act of 24 December 1996* The Act of 24 December 1996<sup>32</sup> further reduced the subscription tax rate for certain types of Luxembourg-based UCIs to 0.01 per cent.<sup>33</sup> This reduction applied to UCIs investing in money market instruments and/or demand or time deposits, and institutional UCIs within the meaning of the 1991 Act which provided a framework for funds sold solely to institutional investors. In addition, subscriptions by Luxembourg UCIs into other Luxembourg-based UCIs were entirely exempted from subscription tax. **1.40**

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<sup>29</sup> Grand-Ducal Regulation of 30 March 1988 determining the fixed duty applicable to the capital collected in undertakings for collective investment governed by the Act of 30 March 1988 (*Mémorial A* 1988, 168).

<sup>30</sup> Art 12, Act of 23 December 1994 concerning State revenues and expenditure for the 1995 fiscal year (*Mémorial A* 1994, 2481), amending Art 108, 1988 Act.

<sup>31</sup> Grand-Ducal Regulation of 14 April 1995 adopted in application of Art 108 of the Act of 30 March 1988 concerning undertakings for collective investment, as amended by the Act of 23 December 1994 concerning State revenues and expenditure for the 1995 fiscal year (*Mémorial A* 1995, 906).

<sup>32</sup> Art 5, Act of 24 December 1996 amending certain direct and indirect tax provisions (*Mémorial A* 1996, 2911).

<sup>33</sup> For the sequence and stages of the reduction, see 11.63 *et seq* below.

- 1.41** Issued on the same day, another Grand-Ducal Regulation<sup>34</sup> defined the concept of a ‘money-market instrument’ and set out the terms and conditions governing the reduced tax rate.<sup>35</sup>
- 1.42** *Act of 29 April 1999* The Community legislature did not remain idle after adopting Directive 85/611. The scope of certain Community standards, including Directive 85/611, was extended to the EEA within the framework of the Agreement on the European Economic Area signed in Porto on 2 May 1992. Pursuant to Annexe IX to that Agreement and Protocol 1 on horizontal adaptations, all references in Directive 85/611 to the ‘Community’ or the ‘common market’ were deemed to refer to the EEA. The subsequent bankruptcy of Bank of Credit and Commerce International (BCCI) necessitated the increased supervision of financial intermediaries. This, in turn, necessitated the removal of obstacles such as business secrecy and bars on the disclosure of information between supervisory authorities. After Directive 85/611 had been modified to reflect these changes, the Luxembourg legislature had to make the corresponding adjustments to Luxembourg’s national standards. This was the underlying purpose of the Act of 29 April 1999,<sup>36</sup> which amended the 1988 Act in the following areas:
- (1) detailed provisions were added to step up cooperation between supervisory authorities;
  - (2) the audit obligations of UCI auditors were broadened;
  - (3) references in the 1988 Act to the EEC were partly replaced by references to the EEA.
- 1.43** *Act of 17 July 2000* Independently of the various Community initiatives, the Act of 17 July 2000<sup>37</sup> amended several further aspects of the 1988 Act, and included the following changes:
- (1) the subscription tax was reduced to 0.01 per cent for sub-funds or unit classes sold to institutional investors in UCIs governed by the 1988 Act;<sup>38</sup>

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<sup>34</sup> Grand-Ducal Regulation of 24 December 1996 adopted in application of amended Art 108, Act of 30 March 1988 concerning undertakings for collective investment, as amended by the Act of 24 December 1996 (*Mémorial A* 1996, 2914).

<sup>35</sup> The content of the Grand-Ducal Regulation of 24 December 1996 is identical to that of the Grand-Ducal Regulation of 14 April 1995, adopted in application of the Act of 23 December 1994.

<sup>36</sup> Act of 29 April 1999 concerning: (1) transposition of Directive (EC) 95/26 concerning the reinforcement of prudential supervision, in the amended Act of 5 April 1993 concerning the financial sector and in the amended Act of 30 March 1988 concerning undertakings for collective investment; (2) partial transposition of Art 7, Directive (EEC) 93/6 on the capital adequacy of investment firms and credit institutions, in the amended Act of 5 April 1993 concerning the financial sector; (3) various other modifications in the amended Act of 5 April 1993 concerning the financial sector; (4) modification of the Grand-Ducal Regulation of 19 July 1983 concerning the fiduciary contracts of credit institutions (*Mémorial A* 1999, 1301 *et seq*).

<sup>37</sup> Act of 17 July 2000 amending certain provisions of the Act of 30 March 1988 concerning undertakings for collective investment (*Mémorial A* 2000, 1226 *et seq*); commented upon in Circular 00/14.

<sup>38</sup> Art 108, para 3, 1988 Act.

- (2) in umbrella UCIs, sub-funds were segregated vis-à-vis third parties so that the assets of an individual sub-fund could only be used to offset the liabilities of that particular sub-fund unless otherwise provided in the constitutive documents.<sup>39</sup>

*Act of 21 December 2001* The Act of 21 December 2001<sup>40</sup> significantly changed the tax regime of UCIs by reducing the subscription tax rate across the board from 0.06 to 0.05 per cent (other than in respect of money market funds and funds sold to institutional investors to which the reduced subscription tax rates referred to above continued to apply).<sup>41</sup> **1.44**

*Act of 19 July 1991 concerning undertakings for collective investment whose securities are not intended for the public*

The 2002 Act and, before it, the 1988 Act apply only to UCIs whose units are intended to be placed with the public. They do not cover investment structures sold to a small circle of informed investors. Because such structures could also benefit from the UCI regulatory infrastructure, the 1991 Act introduced the concept of institutional UCIs into Luxembourg law. It was replaced some fifteen years later by the Act of 13 February 2007 relating to specialized investment funds. **1.45**

*Act of 20 December 2002 with regard to undertakings for collective investment*

**Content** Despite a few upgrades, Directive 85/611 enjoyed limited success as regards its stated objective of the free marketing of UCIs throughout Europe. **1.46**

The UCI markets had grown considerably since 1985, with UCIs investing in an increasingly diversified range of securities. Some of these, such as money market instruments, were still not considered transferable securities in all Member States. A UCI whose sole purpose was to invest in money market instruments was not freely able to distribute throughout Europe using the 'UCITS' passport in all markets. It could only claim the general principle of free movement of capital under the EC Treaty more or less respected by each host country. This was a frustrating situation for both the promoters of the relevant UCIs and the Community authorities, who wanted to give such products broader access to the internal market. **1.47**

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<sup>39</sup> Art 111(2), 1988 Act.

<sup>40</sup> Art 10, Act of 21 December 2001 reforming certain direct and indirect tax provisions (*Mémorial A* 2001, 3312 *et seq*), which amends Art 108(1), 1988 Act.

<sup>41</sup> Since the coming into force of the 2002 Act, which abolishes the 1988 Act with effect from 13 February 2007, the latter has been amended again by the Act of 19 December 2003 (Art 12, Act of 19 December 2003 concerning the State revenue and expenditure budget for the fiscal year 2004 (*Mémorial A* 2003, 3687 *et seq*)). The Act of 19 December 2003 grants total exemption from subscription tax to certain categories of institutional money market funds, amending both Art 129(3), Act of 2002 and Art 108(3), 1988 Act. The 1988 Act was then amended by the Act of 10 July 2005.

- 1.48** It was further felt that investor protection would be strengthened by regulating the status of management companies.
- 1.49** In addition, the fund industry expressed the need to simplify disclosure requirements, and called, *inter alia*, for the introduction of a simplified prospectus which could be provided to investors instead of the complete prospectus, thereby also facilitating the marketing of UCITS.
- 1.50** The overhaul of Directive 85/611 turned out to be a long and laborious process, finally culminating in two directives amending Directive 85/611, ie Directive 2001/107 and Directive 2001/108. The 2002 Act transposed these two directives into Luxembourg law following the structure of the 1988 Act other than in relation to new changes introduced to comply with new Community standards.
- 1.51** The 2002 Act is divided into five parts. Part I on UCITS transposed the new regime introduced by Directives 2001/107 and 2001/108 while retaining provisions from Part I of the 1988 Act which were not affected by the new Community legal framework. The changes mainly concerned the investment policies of UCITS to reflect the expanded range of authorized investments and related investment restrictions.
- 1.52** It is still possible to establish UCIs outside the Community framework pursuant to Part II of the 2002 Act, which, for the most part, is identical to Part II of the 1988 Act.
- 1.53** As in the 1988 Act, Part III contains a single provision with regard to the inward marketing into Luxembourg of foreign UCIs which are not UCITS.
- 1.54** A new Part IV on management companies reflects the new Community requirements for companies managing UCITS. It also covers the standards governing other types of management companies (ie those managing only UCIs other than UCITS), merging provisions from the 1988 Act with new provisions derived from Directive 2001/107.
- 1.55** Part V is very similar to Part IV of the 1988 Act and contains general rules applicable to UCITS and other UCIs. The new provisions inserted by the Luxembourg legislature deal with the simplified prospectus introduced under Directive 85/611, cooperation between the CSSF and foreign management company supervisory authorities, and new methods of publishing UCI sales documents.
- 1.56** Lastly, the law has two annexes. The first lists information to be supplied in sales documents (Schedule A to Directive 2001/107), periodic reports (Schedule B to Directive 2001/107), and the simplified prospectus (Schedule C to Directive 2001/107). The second annexe repeats the collective portfolio management functions listed in Directive 2001/107.

The 2002 Act came into force on 1 January 2003. Its implementation has been relatively complex in the light of the transition regime flowing from Directives 2001/107 and 2001/108 and included transitional arrangements to allow existing UCITS to conform to the new standards while also providing the benefit of UCITS authorization and a European passport under Directives 2001/107 and 2001/108 for UCITS authorized under the 2003 Act. **1.57**

To facilitate transitional arrangements, the Acts of 1988 and 2002 both had legal effect for a period of time until 13 February 2007 when the 1988 Act was finally repealed. **1.58**

UCITS authorized between 13 February 2002 and 13 February 2004 were allowed to opt to operate under the 1988 Act until 13 February 2004 when they were obliged to conform to the new UCITS rules. UCITS authorized before 13 February 2002 (the effective date for Directives 2001/107 and 2001/108) were allowed to opt to operate under the 1988 Act until 13 February 2007 at which date they had to conform with the 2002 Act. **1.59**

Management companies were also subject to a number of new rules under the 2002 Act. Companies managing UCIs other than UCITS have been governed by the 2002 Act since its effective date, ie 1 January 2003. Companies authorized before 13 February 2004 and mainly set up to manage one or more UCITS were permitted to postpone application of the new regime until 13 February 2007. As long as they operated under the old rules, they were not entitled to apply for a European passport. A UCITS governed by the 2002 Act could, until 13 February 2007, be managed by a management company not yet in compliance with the new rules.<sup>42</sup> **1.60**

#### **Acts amending the 2002 Act**

*Act of 19 December 2003* The Act of 19 December 2003<sup>43</sup> exempted certain categories of institutional money market funds from subscription tax, provided their residual portfolio maturity did not exceed ninety days and they had obtained the highest possible rating from a recognized rating agency. **1.61**

*Act of 15 June 2004* The Act of 15 June 2004<sup>44</sup> extended the exemption from subscription tax to UCIs established as pension pooling vehicles. **1.62**

*Act of 10 July 2005* The Act of 10 July 2005 transposes Directive 2003/71,<sup>45</sup> generally referred to as the 'Prospectus Directive'. It sets out rules on the contents **1.63**

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<sup>42</sup> This discussion needs to be considered in the light of the interpretations supplied by the CESR. See Circular 05/186, which includes the CESR's recommendations.

<sup>43</sup> Art 12, Act of 19 December 2003 concerning the State revenue and expenditure budget for the fiscal year 2004 (*Mémorial A* 2003, 3687 *et seq*).

<sup>44</sup> Art 45, Act of 15 June 2004 amending Art 129(3), 2002 Act.

<sup>45</sup> Directive (EC) 2003/71 of the European Parliament and the Council of 4 November 2003 on the prospectus to be published when securities are offered to the public or admitted to trading and amending Directive (EC) 2001/34 ([2003] OJ L345/64 *et seq*).

and dissemination of a prospectus in the case of a public offering or listing of transferable securities on a regulated market in Luxembourg. Insofar as they are governed by special legislation, UCIs generally fall outside its sphere of application with the exception of closed-end UCIs, ie UCIs whose unitholders are not allowed to redeem their units under any circumstances.<sup>46</sup> To avoid a combination of requirements for the issue of prospectuses by closed-end UCIs under both the 2002 Act and the Act of 10 July 2005, the 2002 Act was amended so that the issue of prospectuses by closed-end UCIs is exclusively governed by the Act of 10 July 2005.

- 1.64** The Act of 10 July 2005 also modified the treatment of foreign UCIs (other than coordinated UCITS) which are closed-ended within the meaning of the Act of 10 July 2005, to permit the marketing of their units in or from Luxembourg provided such closed-end UCIs comply with the Act of 10 July 2005.<sup>47</sup>
- 1.65** *Act of 13 February 2007* The Act of 13 February 2007 slightly amended the 2002 Act, so as to exempt from subscription tax an investment in a SIF made by a UCI.<sup>48</sup>

*Act of 13 February 2007 relating to specialized investment funds*

- 1.66** The 1991 Act dealing with funds sold to institutional investors is a precise piece of legislation containing only seven articles and cross-referring for the most part to the 1988 Act. As a result of the repeal and replacement of the 1988 Act with new legislation on UCIs in 2002, it was necessary to amend the 1991 Act and the Luxembourg legislature took the opportunity of adopting a comprehensive and independent body of rules to replace the 1991 Act. This provided an opportunity to modernize the rules applying to institutional funds, bringing a larger pool of well-informed investors<sup>49</sup> within its scope, and to classify institutional funds as 'specialized investment funds'. The governing rules for specialized investment funds were simplified, although largely modelled on Part II of the 2002 Act. The main objective was to adapt the rules on institutional funds to meet an increased

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<sup>46</sup> Closed-end UCIs are determined in juxtaposition to open-end UCIs, defined by Directive (EC) 2003/71 as follows: 'collective investment undertaking other than the closed-end type' means unit trusts and investment companies: (1) the object of which is the collective investment of capital provided by the public, and which operate on the principle of risk-spreading; (2) the units of which are, at the holder's request, repurchased or redeemed, directly or indirectly, out of the assets of these undertakings.

<sup>47</sup> Art 76, 2002 Act.

<sup>48</sup> Art 72, Act of 13 February 2007.

<sup>49</sup> For further details concerning the concept of well-informed investor, see 2.61 *et seq* below.

demand for alternative investment structures, such as hedge funds, real estate funds or private equity funds.<sup>50</sup>

### Circulars issued by the supervisory authorities

Since the end of the 1970s, the supervisory authority has laid down, in the form of circulars, the rules governing the operation of UCIs and SICARs. However, the concept of a circular does not technically form part of Luxembourg's legal panoply. **1.67**

The 2002 Act<sup>51</sup> permits the adoption of standards governing the operation or risk diversification of certain types of UCIs in the form of Grand-Ducal regulations subject to the recommendation of the supervisory authority. However, the CSSF has always preferred to issue circulars in order to ensure optimum flexibility and adaptability of its rules rather than recommending the adoption of Grand-Ducal regulations. **1.68**

In the 1970s and 1980s, numerous circulars were issued by the CSSF (and its predecessors, the *Institut Monétaire Luxembourgeois* and the Banking Commissioner). Circular 91/75 of 21 January 1991 revised and reviewed the rules applicable to Luxembourg-based UCIs governed by the 1988 Act. The same circular repealed and replaced previous circulars. The application and interpretation of the 2002 Act is not yet covered by a general circular such as Circular 91/75, so that Circular 91/75 largely remains in force. **1.69**

The main circulars on UCIs and SICARs currently in force are as follows: **1.70**

- IML Circular 91/75 of 21 January 1991;
- CSSF Circular 00/14 of 27 July 2000 on the adoption of the Act of 17 July 2000 amending certain provisions of the Act of 30 March 1988;
- CSSF Circular 02/77 of 27 November 2002 on the protection of investors in the event of net asset value calculation error and the correction of consequences resulting from non-compliance with the investment rules applicable to UCIs;
- CSSF Circular 02/80 of 5 December 2002 on the specific rules applicable to Luxembourg UCIs pursuing alternative investment strategies;
- CSSF Circular 02/81 of 6 December 2002 on guidelines concerning the duties of auditors of UCIs;

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<sup>50</sup> For further details on the genesis of the Act of 13 February 2007, see M Moulla and M Chantalangsy, 'Presentation of the law of 2007 compared to other existing legislation governing collective investment structures—historical overview of the law of 2007' in *Specialised Investment Funds* (Arendt & Medernach, 2007) 14, 15.

<sup>51</sup> Arts 67, 72, and 75, 2002 Act.

- CSSF Circular 03/87 of 21 January 2003 on the coming into force of the 2002 Act;
- CSSF Circular 03/88 of 22 January 2003 on the classification of UCIs governed by the provisions of the 2002 Act;
- CSSF Circular 03/97 of 28 February 2003 on the publication in the electronic database for the financial centre (*Référentiel de la place*) of simplified and full prospectuses and the annual and half-yearly reports by UCIs;
- CSSF Circular 03/108 of 30 July 2003 on Luxembourg management companies subject to the provisions of Chapter 13 of the 2002 Act, and Luxembourg self-managed investment companies subject to Article 27 or Article 40 of the 2002 Act;
- CSSF Circular 03/122 of 19 December 2003 on clarifications concerning the simplified prospectus;
- CSSF Circular 04/146 of 17 June 2004 on the protection of UCIs and their investors against late trading and market timing practices;
- CSSF Circular 04/151 of 13 July 2004 on the information to be published in the listing particulars of the securities listed below:
  - shares and units of foreign UCIs whose securities are not publicly available, offered or sold in or from Luxembourg, and
  - securities redeemable or exchangeable for shares or units of UCIs or whose income and/or redemption is/are linked to underlying shares or units of UCIs;
- CSSF Circular 04/155 of 27 September 2004 on the compliance function;
- CSSF Circular 05/176 of 5 April 2005 on the rules of conduct to be adopted by UCITS in relation to the use of financial derivative instruments;
- CSSF Circular 05/177 of 6 April 2005 on the abolition of any prior approval by the CSSF of advertising material used by persons and companies supervised by the CSSF; revocation of point II of Chapter L of IML Circular 91/75; revocation of the two last sentences of point IV 5.11 of CSSF Circular 2000/15;
- CSSF Circular 05/178 of 11 April 2005 on administrative and accounting organization; outsourcing of IT services; revocation of point 4.5.2 of IML Circular 96/126 and substitution with point 4.5.2 of Circular 05/178;
- CSSF Circular 05/185 of 24 May 2005 on Luxembourg management companies subject to the provisions of Chapter 13 of the 2002 Act, and Luxembourg self-managed investment companies subject to the provisions of Article 27 or Article 40 of the 2002 Act;
- CSSF Circular 05/186 of 25 May 2005 on the guidelines of the Committee of European Securities Regulators (CESR) regarding the application of transitional

- measures resulting from Directives (EC) 2001/107 and (EC) 2001/108 (UCITS III) amending Directive (EEC) 85/611 (UCITS I);
- CSSF Circular 05/188 of 27 May 2005 on the coming into force of the Act of 12 November 2004;
  - CSSF Circular 05/210 of 10 October 2005 on the drawing-up of a simplified prospectus within the scope of Chapter 1 of Part III of the Act on prospectuses for securities;
  - CSSF Circular 05/211 of 13 October 2005 on combating money laundering and terrorist financing and the prevention of the use of the financial sector for money laundering and terrorist financing purposes;
  - CSSF Circular 05/225 of 16 December 2005 on the concept of 'offer to the public of securities' as defined in the Act on prospectuses for securities and the consequential 'obligation to publish a prospectus';
  - CSSF Circular 05/226 of 16 December 2005 on the general overview of the Act on prospectuses for securities and technical specifications regarding communications to the CSSF of documents with a view to authorization or for filing and of notices for offers to the public and admissions to trading on a regulated market;
  - CSSF Circular 06/241 of 5 April 2006 on the concept of risk capital under the Act of 15 June 2004;
  - CSSF Circular 06/267 of 22 November 2006 on technical specifications regarding the filing with the CSSF, in accordance with the Act on prospectuses for securities, of documents for approval or notification purposes and of notices for offers to the public of units/shares of Luxembourg closed-end UCIs and admissions of units/shares of Luxembourg closed-end UCIs to trading on a regulated market;
  - CSSF Circular 06/272 of 21 December 2006 on technical specifications regarding the filing with the CSSF, in accordance with the Act on prospectuses for securities, of documents for approval or notification purposes and of notices for offers to the public of securities issued by SICARs and admissions of securities issued by SICARs to trading on a regulated market;
  - CSSF Circular 07/277 of 9 January 2007 on the new notification procedure following guidelines issued by the Committee of European Securities Regulators (CESR) regarding the simplification of the UCITS notification procedure;
  - CSSF Circular 07/283 of 28 February 2007 on the entry into force of the Act of 13 February 2007;
  - CSSF Circular 07/290 of 3 May 2007 on the definition of capital ratios pursuant to Article 56 of the 1993 Act (application to investment firms and management companies subject to Chapter 13 of the 2002 Act, as amended);

- CSSF Circular 07/307 of 31 July 2007 on the MiFID Directive: Conduct of business rules in the financial sector;
  - CSSF Circular 07/308 of 2 August 2007 on the rules of conduct to be adopted by UCITS with respect to the management of financial risk and the use of derivative financial instruments;
  - CSSF Circular 07/309 of 3 August 2007 on risk-spreading in the context of SIFs;
  - CSSF Circular 07/310 of 3 August 2007 on financial information to be provided by SIFs, as amended by CSSF Circular 08/348;
  - CSSF Circular 08/339 of 19 February 2008 on the guidelines of the Committee of European Securities Regulators (CESR) concerning eligible assets for investment by UCITS;
  - CSSF Circular 08/348 of 17 April 2008 on the changes to Circulars IML 97/136 and CSSF 07/310;
  - CSSF Circular 08/350 of 22 April 2008 on clarifications relating to the amendments introduced by the Act of 13 July 2007 to the status of professionals of the financial sector (PFS) referred to in Articles 29-1, 29-2, 29-3, or 29-4 and designated as ‘support PFS’, and on the amendment to the prudential supervisory procedures for support PFS;
  - CSSF Circular 08/356 of 4 June 2008 regarding rules applicable to UCIs which employ certain techniques and instruments relating to transferable securities and money market instruments.
- 1.71** The circulars are a highly appropriate regulation tool for UCIs, which require a legal framework that can be easily and rapidly adapted to needs of the investment industry.
- 1.72** Since the constitutional reform of 19 November 2004,<sup>52</sup> the CSSF has been authorized to adopt regulations within the framework of its responsibilities, provided it has the necessary regulatory authority under the relevant law.
- 1.73** While the Constitution only refers to the adoption of regulations by the CSSF this does not of itself mean that the CSSF is restricted from prescribing circulars in areas where it has regulatory authority. Circulars are typically used to specify certain legal norms whereas the CSSF has adopted circulars as a means of informing

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<sup>52</sup> Art 108*bis* of the Constitution, amended by the Act of 19 November 2004 with regard to (1) amendment of Arts 11(6), 32, and 76 of the Constitution; and (2) the creation of a new Art 108*bis* in the Constitution (*Mémorial A* 2004, 2784). This constitutional amendment followed the decision of 7 March 2003 of the Constitutional Court of the Grand Duchy of Luxembourg (*Mémorial A* 2003, 656) that the power to adopt regulations and decisions to implement legislation in accordance with Art 36 of the Constitution is in the hands of the Grand Duke. A law or regulation entrusting this power to an authority other than the Grand Duke is unconstitutional.

third parties of its general policy positions on various matters. As derogations from such positions are possible, it is difficult to argue that they decree or specify rigid legal norms. Circulars as issued by the CSSF are not so much a form of regulation as a tool to ensure transparency and adaptability.

*Laws and regulations not limited to UCIs*

Though not specifically limited to UCIs, two additional bodies of rules also apply in all standards governing such funds. **1.74**

The first is the 1915 Act, which has the status of a supplementary standard vis-à-vis UCIs.<sup>53</sup> It applies to situations not specifically legislated for by the 2002 Act and the Act of 13 February 2007. **1.75**

The second is the Luxembourg Civil Code, which governs the contractual structure underlying FCPs. It also governs civil companies in general and as such applies to investment companies, save to the extent otherwise provided for by the 1915 Act, the 2002 Act, or the Act of 13 February 2007. **1.76**

**Role of the CSSF**

*General presentation*

The CSSF is a public law body established with legal status by the Luxembourg State. Its object is to maintain prudential supervision of the financial sector.<sup>54</sup> Within this role, it oversees UCIs established or marketing their units in the Grand Duchy of Luxembourg.<sup>55</sup> It also supervises management companies of UCIs.<sup>56</sup> **1.77**

The CSSF actively engages in its supervisory duties in connection with UCIs. Its duties and involvement vary under the applicable regulations depending on whether the UCI is based in Luxembourg<sup>57</sup> or is a non-Luxembourg coordinated UCITS with a European passport, or a non-Luxembourg UCI which is not a UCITS. **1.78**

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<sup>53</sup> Arts 26, 40, and 71, 2002 Act.

<sup>54</sup> Arts 2 and 3, Act of 23 December 1998 concerning the creation of a Commission for the supervision of the financial sector (*Mémorial* A 1998, 2985).

<sup>55</sup> For other comments on this issue, see 8.01 *et seq* below. See also A Elvinger, 'Le rôle des autorités de surveillance' *ALFI Yearbook* 1994, 33; C Kremer and J Baden, 'The role of the Luxembourg Monetary Institute in the supervision of undertakings for collective investment,' (February 1995) 3, 63, *World Fund Industry/Gestion collective internationale*.

<sup>56</sup> Arts 77 to 92, 2002 Act.

<sup>57</sup> Part I or Part II, 2002 Act or Act of 13 February 2007.

- 1.79** The CSSF also supervises management companies for UCIs based in Luxembourg. It supervises foreign entities only when operating under the European passport introduced by Directive 85/611. In such cases, its intervention is minimal as the primary regulatory authority is the supervisory authority in the company's home State.
- 1.80** Generally speaking, the CSSF has very extensive powers in its interpretation of the Act of 13 February 2007 and the 2002 Act. In the exercise of those powers, it has specified the meaning of certain concepts, such as overall risk connected with derivatives.<sup>58</sup> The 2002 Act also enables it to designate UCITS classes, which, whilst investing in transferable securities, cannot be regarded as coordinated UCITS entitled to the European passport under Directive 85/611. Last but not least, the 2002 Act refers to a proposed Grand-Ducal regulation to be issued in order to lay down specific rules with regard to certain provisions of the Act. As mentioned above, rather than recommending the adoption of a Grand-Ducal regulation, the CSSF has issued various circulars<sup>59</sup> detailing the principles adopted by it in its supervisory role in relation to matters not settled by the Act.

### *Supervision of UCIs*

#### **UCIs established in the Grand Duchy of Luxembourg**

- 1.81** The CSSF is responsible for authorizing UCIs established in the Grand Duchy of Luxembourg. Accordingly, it receives the incorporation documents and various other documents and information about each UCI. If, after examining such papers, it believes that the investor information is adequate and reflects the applicable legal standards, it adds the UCI to the official list of UCIs. However, registration does not indicate approval of a UCI's investment objectives or investments, or of its ability to meet its objectives.
- 1.82** UCIs remain on the official list as long as they comply with the rules governing their operation and sales of units. The CSSF checks compliance against the monthly, semi-annual, and annual reports received from each UCI and against any other information requested by it. Similarly, it authorizes in advance proposed modifications to incorporation documents.
- 1.83** In addition, the CSSF is authorized to grant certain derogations from the 2002 Act.<sup>60</sup> It may waive the application of certain legal requirements for UCITS covered by Part I of the 2002 Act. It has more extensive powers in this regard with respect to UCIs governed by Part II of the 2002 Act and the Act of 13 February 2007.

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<sup>58</sup> Circular 05/176.

<sup>59</sup> Primarily Circular 91/75 and, as regards SIFs, Circular 07/309.

<sup>60</sup> Arts 45(1) and 116, 2002 Act.

The CSSF exerts wider control over so-called ‘self-managed’ investment companies, which are subject to similar share capital and management obligations as management companies themselves.<sup>61</sup> **1.84**

The CSSF also has the power to impose penalties. In particular, it may remove a UCI from the official list if it violates the laws and regulations governing its operation or the sale of its units. **1.85**

### **UCIs established in foreign countries**

#### *Coordinated UCITS*

Coordinated UCITS benefit from the rules governing the free movement of capital and freedom to provide services under Directive 85/611. This allows coordinated UCITS approved by the supervisory authority of the Member State in which they are established (the ‘home State’) to market their units freely in another Member State of the EEA (the ‘host State’). **1.86**

Only those aspects not covered by Directive 85/611 remain under the supervisory authority of the host State, such as information to be provided to the public, as to which the supervisory authority of the host State may lay down special requirements.<sup>62</sup> **1.87**

Pursuant to those principles, the CSSF has only limited authority over foreign UCITS governed by Directive 85/611. Foreign UCITS must nevertheless inform the CSSF of their intention to market their units in the Grand Duchy of Luxembourg and provide it with certain documents. The CSSF may prohibit marketing only on the grounds listed in Directive 85/611.<sup>63</sup> **1.88**

#### *Other UCIs under foreign law*

Foreign open-end UCIs, within the meaning of the Act of 10 July 2005, other than coordinated UCITS, must be authorized by the CSSF if they wish to market their units in the Grand Duchy of Luxembourg. They are only authorized by the CSSF when subject, in their home State, to permanent supervision by a supervisory authority created by law to protect investors. Such UCIs remain on the official list of the CSSF as long as they comply with the Luxembourg rules governing their operation and sales of units.<sup>64</sup> **1.89**

Foreign closed-end UCIs, within the meaning of the Act of 10 July 2005, may market their units in the Grand Duchy of Luxembourg subject to compliance **1.90**

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<sup>61</sup> Art 27, 2002 Act. For details see 6.77 *et seq* below.

<sup>62</sup> Art 58, 2002 Act.

<sup>63</sup> Art 60, 2002 Act.

<sup>64</sup> Art 76, 2002 Act.

with the Act of 10 July 2005. They are not subject to the supervisory authority provided for by the 2002 Act.<sup>65</sup>

### *Supervision of management companies*

#### **Management companies established in the Grand Duchy of Luxembourg**

- 1.91** The right to carry on the activity of a management company established in Luxembourg is subject to prior authorization. This is granted either by the CSSF or by the Minister with responsibility for the CSSF (in the case of a management company for foreign UCIs other than coordinated UCITS).<sup>66</sup> All applications are reviewed by the CSSF, whether or not the UCI in question is established in Luxembourg or another jurisdiction. This said, companies which only manage foreign UCIs other than coordinated UCITS require another type of authorization in Luxembourg than that for UCITS management companies. UCITS management companies may also manage UCIs other than coordinated UCITS, in which case they are subject to slightly different rules.
- 1.92** A management company seeking authorization must comply with a series of conditions set out in the 2002 Act<sup>67</sup> or, when it only engages in the management of foreign UCIs other than UCITS, the 1993 Act.<sup>68</sup> The same rules apply to a management company wishing to retain its authorization.<sup>69</sup> On an ongoing basis, the CSSF checks compliance by management companies with their obligations, particularly through the quarterly information they are obliged to supply.<sup>70</sup> The auditor of the relevant management company in fulfilling the auditor's role envisaged under the Acts of 2002<sup>71</sup> and 1993<sup>72</sup> also plays an important role in the continued retention of a management company's authorization.
- 1.93** Withdrawal of a management company's authorization is the ultimate penalty for non-compliance with the laws and regulations governing its authorization and activities. The CSSF determines whether an authorization should be withdrawn, although it does not have discretionary power to do so. An authorization may only be withdrawn when the CSSF observes that the management company in question comes within one of the situations listed in the 2002 Act<sup>73</sup> or in the 1993 Act,<sup>74</sup> as

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<sup>65</sup> *ibid.*

<sup>66</sup> Arts 77(1) and 91(1), 2002 Act; Art 14(1), Act of 1993.

<sup>67</sup> Arts 77–80, 91, and 92, 2002 Act.

<sup>68</sup> Arts 15 to 22-1 and 28-8, 1993 Act.

<sup>69</sup> Arts 82–86, 91, and 92, 2002 Act; Art 23(4), 1993 Act.

<sup>70</sup> Section III, Circular 03/108.

<sup>71</sup> Arts 80 and 92, 2002 Act.

<sup>72</sup> Art 22, 1993 Act.

<sup>73</sup> Arts 78(5) and 91(5), 2002 Act.

<sup>74</sup> Art 23, 1993 Act.

the case may be. Under the 2002 Act the CSSF may grant management companies a limited period to comply with the applicable laws and regulations or to cease their activity.<sup>75</sup>

### **Management companies established in foreign countries**

Management companies of UCITS approved as such in foreign countries may, by virtue of their European passport, establish themselves in Luxembourg or provide in Luxembourg the services set out in Directive 85/611 without having to seek additional authorization from the CSSF.<sup>76</sup> The notification procedure by which the authorities in the home State inform the CSSF, as set out in Directive 85/611, is the only applicable formality.<sup>77</sup> The CSSF has limited powers in this respect. It informs the management company of the general interest rules governing its activity in Luxembourg and any applicable rules of conduct if the company in question engages in Luxembourg in portfolio management for entities other than UCIs, the provision of investment advice or the acceptance of deposits.<sup>78</sup> The CSSF may decline permission to a management company wishing to market units of UCIs managed by it, if the CSSF notes that the activity violates the relevant provisions in Directive 85/611.<sup>79</sup> **1.94**

The CSSF authorizes foreign management companies other than coordinated management companies when they want to manage a UCI in Luxembourg other than a coordinated UCITS<sup>80</sup> or a SIF. In principle, the CSSF requires such companies to be subject to prudential control in their country of origin, allowing it to trust in supervision it has every reason to consider effective. **1.95**

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<sup>75</sup> eg this power can be exercised by the CSSF when a management company no longer complies with the legal requirements with respect to share capital (Art 82, 2002 Act).

<sup>76</sup> See 6.195 below.

<sup>77</sup> Art 6a, Directive (EEC) 85/611.

<sup>78</sup> *ibid* Arts 6a, points 4 and 6, and 6b, points 3 and 4.

<sup>79</sup> *ibid* Art 6a, point 5.

<sup>80</sup> Art 93(3), 2002 Act.

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