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Banks and investment firms
Regulatory update

Topics covered in this issue

AML

1. *Adoption of a new position on rules aimed at preventing money laundering and terrorist financing*
2. *CSSF Circular 15/607*

BRRD

3. *Circular CSSF 15/610 Ad hoc data collection within the context of Directive 2014/59/EU*

FATCA

4. *Luxembourg draft Law available – Deadlines, data protection obligations and sanctions framework detailed*

Outsourcing

5. *CSSF Circular 15/611 and domiciliation agents*

Single Supervisory Mechanism (SSM)

6. *Regulation (EU) 2015/534 of the European Central Bank of 17 March 2015 on reporting of supervisory financial information (ECB/2015/13)*

Transparency

7. *CSSF Circular 15/605 on conditions for the disclosure of unencumbered assets*

UCITS

8. *CSSF Circular 15/608 - Change of deadline for compliance with CSSF Circular 14/587 and subsequent amendments to this Circular*

AML

1. Adoption of a new position on rules aimed at preventing money laundering and terrorist financing

On 20 April 2015, the Council of the European Union has adopted its position on the rules aimed at preventing the use of the financial system for the purpose of money laundering or terrorist financing. The Directive aims at addressing the threat of money laundering by laying down additional measures; the Directive will repeal Directives 2005/60/EC and 2006/70/EC.

The position of the Council follows the Proposal for a Directive of the European Parliament and of the Council adopted on 05/02/2013. Main observations are as follows:

1. Retailers of high value goods and providers of gambling services

The new Directive broadens its scope to comprise unconventional channels to launder illicit proceeds. Retailers of high value goods and high value service providers apply customer due diligence when dealing with natural or legal persons trading in goods and carrying out transactions in cash of EUR 10 000 or more (whether in one transaction or in multiple transactions which appear to be linked). The Council has raised the threshold originally (in a former draft version) proposed of EUR 7500.

Providers of gambling services (including, but not limited to, casinos) are obliged to carry out customer due diligence. Member States may exempt certain providers of gambling services from these obligations, if the nature and the scale of the activity is at low risk. The use of exemptions should be considered as an exception and applied in a strict manner. Casinos can never be assimilated to a low risk activity. Customer due diligence is carried out when conducting transactions of EUR 2 000 or more (whether in one transaction or in multiple transactions which appear to be linked). The identity of the customer must be linked to the transactions carried out.

2. PEPs

Individuals who hold prominent public functions are exposed to greater risk of money laundering; they may transmit this risk to the financial sector when entering into a business relationship with an entity or professional of the financial sector. As a method of prevention, enhanced due diligence should be applied to politically exposed persons regardless whether they are domestic PEPs or PEPs residing in another Member State or in a third country.

3. Risk assessment

With the aim of identifying the risks of money laundering across Member States, the Council encourages a more centralised approach to risk assessment, which conceives a strengthened role of the Commission in coordinating cross-border risk assessment. A biennial report will indicate the sectors mostly at risk, the associated risks and the means used by criminals to launder illicit proceeds. The Commission will update its report with the intent of encouraging an effective response of national legislators and stakeholders. Similarly, Member States detect the threats of money laundering to which they are exposed and adopt appropriate countermeasures on a national level. This information is shared with the Commission, the European Supervisory Authority and the other Member States.

4. Tax crimes

The extended scope of the directive encompasses tax crimes within the definition of “criminal activity” with the intent of including tax crimes within the predicate offenses to money laundering. The text disregards the amendment of the European Parliament pointing to “tax offenses” (infractions fiscales pénales). Tax crimes constitute “criminal activity” when:

- Related to direct or indirect taxes;
- Punishable by deprivation of liberty or detention order for a maximum of more than 1 year; or
- Punishable by deprivation of liberty or detention order for a minimum of more than 6 months.

Despite Member States independently designate the conducts constituting tax offenses, differences in national laws cannot hamper cooperation exchange of information between FIUs.

5. Beneficial ownership

In line with the latest FATF Recommendations, the identification of the natural person, who ultimately owns or controls a legal entity or a transaction, is crucial to the fight against money laundering. A central register in each Member State will collect the information which will be accurate and kept up to date. Member States are responsible for the arrangement of the central register, however they may hold obliged entities accountable for its compilation. Competent authorities, FIUs, obliged entities (and, to a certain extent, any person or organisation that can demonstrate a legitimate interest) will have access to the register. The consultation of the register does not fulfil in itself customer due diligence obligations. The mechanism aims at combating the misuse of legal persons and legal arrangements and at increasing transparency.

6. Sanctions

Competent authorities should impose administrative sanctions of different type and extent; when the infringing conduct is subject to criminal sanctions under national law, Member States can decide if they want to impose also administrative sanctions in addition. However, if no criminal sanction is foreseen, administrative sanctions become mandatory. Sanctions can be applicable to legal persons, to management bodies and to natural persons engaged in the breach.

Future developments

The European Parliament will be able to adopt the directive at second reading at a forthcoming plenary session. Member States will have two years for the transposition into national law.

2. CSSF Circular 15/607

The FATF maintains its position that the AML / CFT regimes of **Iran** and the **Democratic People's Republic of Korea** ("DPRK") continue to have substantial and strategic deficiencies and maintains the application of counter-measures against **Iran** and **DPRK**.

Algeria, Ecuador and Burma / Myanmar have strategic deficiencies in AML / CFT and have not made sufficient progress or have not committed to an action plan developed with the FATF to address their deficiencies.

Jurisdictions with strategic deficiencies in terms of AML / CFT for which they have developed an action plan with the FATF to address the shortcomings, are:

Afghanistan, Angola, Guyana, Indonesia, Iraq, Lao People's Democratic Republic, Panama, Papua New Guinea, Sudan, Syria and Yemen.

The FATF considers **Uganda** as a jurisdiction whose progress regarding AML / CFT are deemed insufficient.

Due to the substantial efforts demonstrated by **Albania, Cambodia, Kuwait, Namibia, Nicaragua, Pakistan and Zimbabwe**, these jurisdictions are no longer subject to the monitoring process of the FATF but will continue to work with the FATF- style regional organisations.

This circular repeals CSSF Circular 14/595 of 30 October 2014.

BRRD

3. Circular CSSF 15/610 Ad hoc data collection within the context of Directive 2014/59/EU

This circular is intended to solicit information of credit institutions, and Luxembourg branches of credit institutions having their head office in a third country, to prepare the work of the CSSF as a future resolution authority under the BRRD, for:

- the preparation of resolution plans in accordance with Articles 10 and 12 of the BRRD;

- calculating the minimum requirement for own funds and eligible liabilities ("MREL") according to Article 45 of the BRRD.

The circular covers the following two points:

a) Disclosures for the establishment of resolution plans;

b) Information relating to the MREL.

The required information is to be transmitted to the CSSF by 30 May 2015 at the latest.

FATCA

4. Luxembourg draft law available – Deadlines, data protection obligations and sanctions framework detailed

Already in March 2014, Luxembourg signed a Model 1 IGA with the U.S., in order to implement automatic exchange of information in the context of FATCA.

The Council of the Luxembourg Government reached agreement on 6 March 2015 on the draft law ratifying and implementing the Luxembourg IGA. The draft law was rendered public on 27 March 2015. The package also contains the French language version of the Luxembourg IGA.

Other than approving the text of the Luxembourg IGA and reconfirming certain principles and flexibilities of this IGA (such as the option to apply the definitions of the IRS Regulations instead of the definitions of the IGA), the draft Law contains the following new proposed provisions:

- **Deadline for reporting and zero reporting:** the draft Law confirms the annual reporting deadline of 30 June (as already announced in the draft Circular Letter ECHA 2 released by the Luxembourg tax authorities). The Commentaries to the draft Law also confirm that a zero reporting obligation would be maintained.

- **Data protection – information obligations:** the draft Law contains explicit reference to the data protection law of 2 August 2002 (as amended), in order to remind reporting financial institutions of their obligation to inform each reportable individual on the information that will be collected and transferred according to the IGA. This notification will need to be made in advance, according to the principles of the above-mentioned law. Additionally, both the Luxembourg tax authorities and any reporting financial institution are obliged to inform reportable individuals on any security breach related to his data in case this security breach could harm the individual's personal data protection or private life. Reporting financial institutions will need to ensure to cover these obligations in their FATCA procedures urgently, as the information obligations will need to be met before the first FATCA reporting deadline of 30 June 2015.

  Similar obligations will also apply relating to the Council Directive 2014/107/EU of 9 December 2014 amending Directive 2011/16/EU as regards mandatory automatic exchange of information in the field of taxation (i.e. in the context of application of the Common Reporting Standard (CRS) according to this Directive), that will be applicable as from 1 January 2016.

- **Tax audits and sanctions:** the draft Law explicitly refers to the fact that the Luxembourg tax authorities will verify the procedures put in place by financial institutions to meet the automatic exchange of information obligations under the Luxembourg IGA, and the reasonable diligence applied in respect of these obligations. Additionally, the draft Law mentions that Luxembourg tax authorities will in particular verify whether financial institutions did not implement mechanisms to avoid data communication would take place. The Commentaries contain an illustrative example of such avoidance, where a financial institution would immobilise its bearer securities with a depository institution that is not a reporting financial institution.

The draft Law also contains the sanctions framework. On the one hand, in case reasonable diligence obligations would not be met, or in case exchange of information mechanisms would not have been sufficiently implemented, a reporting financial institution could incur an administrative fiscal fine of maximum 250.000€. On the other hand, in case reporting obligations would not have been met, or in case of late, incomplete or incorrect exchange of information, a reporting financial institution would be exposed to an administrative sanction of 0,5% of the amounts that should have been communicated, with a minimum of 1.500€.

Next steps

As a next step, the draft Law should go through the Parliamentary approval process. However, it seems the legal reference of the IGA would first be changed, and an additional exchange of letters between the US and Luxembourg will take place. The signed Luxembourg IGA indeed refers to the Protocol of 20 May 2009 to the Luxembourg-US double taxation treaty. This Protocol was ratified by Luxembourg in 2010, but has still not been ratified today by the US. An alternative (unsigned) version of the Luxembourg IGA, appended to the draft Law, therefore refers to the legal basis of the Convention of 25 January 1988 on Mutual Administrative Assistance in Tax Matters instead.

To be noted that, at this stage, it can also not be excluded that certain modifications would still be made to the text of the draft Law.

Once the draft Law is voted, the Luxembourg Tax Authorities will likely quickly release the two draft circular letters published earlier this year (draft Circular Letters ECHA-2 and ECHA-3) in their final version.

Outsourcing

5. CSSF Circular 15/611 and domiciliation agents

On 16 April 2015, the CSSF published Circular 15/611 (the circular) on managing the risks related to the outsourcing of systems that allow the compilation, distribution and consultation of management board/strategic documents (the systems).

The circular intends to draw the attention of all entities subject to CSSF supervision, and especially domiciliation agents, to the risks associated with the outsourcing of these systems often marketed as virtual data rooms or digital board packs. Indeed, these systems are commonly used to compile, distribute and consult documents containing sensitive data, such as strategic company data which are not and might never be released to the public.

For most types of entities (except domiciliation agents), the CSSF considers that it is the choice of the entity, after performing a thorough due diligence, to decide on whether or not to store its data on a system hosted at and operated by a service provider who do not necessarily have a Support PSF license and may even not be located in Luxembourg.

For domiciliation agents, the CSSF considers the activity for which these systems are used, in this case the compilation, distribution and compilation of management board/strategic documents, is a core activity of such a domiciliation agent and, therefore, domiciliation agents are required to choose a service provider that complies with the conditions set out in **Circular CSSF 05/178** concerning the outsourcing of IT services to a third party.

In addition, the CSSF would like to remind all entities that it is their responsibility not to disclose any information that is considered confidential under Article 41 of the Law of 5 April 1993 on the financial sector to a service provider who is not subject to professional secrecy obligations.

The circular is already applicable.

Single Supervisory Mechanism (SSM)

6. Regulation (EU) 2015/534 of the European Central Bank of 17 March 2015 on reporting of supervisory financial information (ECB/2015/13)

This Regulation lays down requirements concerning reporting of supervisory financial information to be submitted to National competent authorities (NCAs).

As an exception, supervised entities that have been given a waiver regarding the application of prudential requirements on an individual basis, shall not be required to report supervisory financial information in accordance with this regulation.

This Regulation shall not affect the accounting standards applied by supervised groups and entities in their consolidated accounts, nor change the accounting standards applied for supervisory reporting. A supervised entity or supervised group shall be classified as significant 18 months after a decision has been notified. This regulation also defines the format and frequency of reporting on a consolidated basis and reference dates and remittance dates for significant supervised group/ for entities which are part or not of a less significant supervised applying IFRS or national accounting frameworks. It also sets out the format and frequency of reporting on an individual basis for:

- entities which are not part of a significant group;
- entities which are part of a significant supervised group

and the reference dates and remittance for significant supervised entities/ for less significant supervised entities. The first reporting reference date are 31 December 2015 for significant supervised groups and significant supervised entities which are not part of a supervised group. For significant supervised entities which are part of a supervised group and subsidiaries of significant groups established in a non-participating Member State or a third country it shall be the 30 June 2016 and for less significant supervised groups and less significant supervised entities it shall be the 30 June 2017.

This Regulation entered into force on 1 April 2015.

Transparency

7. CSSF Circular 15/605 on conditions for the disclosure of unencumbered assets

On 20 February 2015, the CSSF published **CSSF Circular 15/605 on conditions for the disclosure of unencumbered assets** applicable to Luxembourg credit institutions publishing Pillar III report, active in collateralised transactions (repurchase agreements, derivatives, securitisations, covered bonds and financing transactions with Central Bank).

According to EBA **Guidelines on Disclosure of Encumbered and Unencumbered Assets** issued on 27 June 2014 related to the implementation of Article 443 of CRR, institutions subject to disclosure requirements in Part 8 of the CRR, will be required to disclose publicly asset encumbrance information within their Pillar III report.

Four templates are included as appendix to disclose information:

- **Template A:** encumbered and unencumbered assets in carrying and fair value amounts by broad categories of asset type;
- **Template B:** collateral received by an institution, by broad categories of product type;
- **Template C:** carrying amount of encumbered assets/collateral received and associated liabilities; and
- **Template D:** business commentary on the impact of the business model on encumbrance levels and relevance of encumbrance on the funding model.

Subsequently and by 1 January 2016, the EBA will deliver draft regulatory technical standards to the Commission which will replace these guidelines.

Until then, the institutions concerned shall comply with the EBA Guidelines attached in the appendix of the Circular.

This circular came into force on 20 February 2015.

UCITS

8. CSSF Circular 15/608 – Change of deadline for compliance with CSSF Circular 14/587 and subsequent amendments to this Circular

On 23 March 2015, the CSSF published CSSF Circular 15/608 amending CSSF Circular 14/587 applicable to Luxembourg credit institutions acting as depositary of UCITS under Part I of the Law of 17 December 2010.

The purpose of this Circular is to amend point 187 of CSSF Circular 14/587 regarding the deadline for compliance with the provisions of CSSF Circular 14/587 and to inform Luxembourg credit institutions acting as depositaries of UCITS about the subsequent amendments to the Circular.

1) Extended deadline for compliance with CSSF Circular 14/587:

Point 187 of CSSF Circular 14/587 is amended, as follows:

"187: The recipients of this Circular shall comply with the provisions thereof at the latest on 18 March 2016. Chapter E of IML Circular 91/75 shall no longer apply to UCITS as from this date."

2) Subsequent amendments to CSSF Circular 14/587:

The CSSF will amend in due course and with an effective date of 18 March 2016 CSSF Circular 14/587 in order to adapt its provisions to the depositary aspects of UCITS V Directive and related delegated acts.

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