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DU SECTEUR
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Commission de Surveillance du Secteur Financier

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PREFACE

Looking back on the year 2010, we may note that the Luxembourg financial centre showed a solid resilience against challenges that the changes caused by the financial crisis of 2008 brought.

Admittedly, the results of banks were more modest, showing the noticeable decrease of their intermediation activity. Consequently, the national economic growth will have to put up with a lesser contribution of the financial sector as long as employment in the financial sector will be affected by the ongoing restructuring and relocation and the tax revenue from the good years will be replaced by those from the years marked by the crisis. As this trend is not likely to change soon, a responsible policy is required to block this trend by improving the competitiveness of the Luxembourg economy.

The nevertheless positive assessment of the behaviour of banks established in Luxembourg results from the fact that the latter were forced to reconsider the reason for their presence in the financial centre and this reconsideration led most of them to adopt a proactive strategy in order to bring their investment in Luxembourg to full fruition. Thus, they managed to maintain confidence of the clients who, although their number decreased, still have important assets. The sustainability of the Luxembourg banking sector thus improved.

This observation is supported by the constant performance of the different types of undertakings for collective investment, including specialised funds and SICARs, pension funds and securitisation undertakings, which continued making money regularly and whose investment value reached new records. Moreover, the sustained activity of UCIs is also a major reason for the creation of many new professionals of the financial sector which have the status of, among others, registrar agent or support PFS, particularly in the IT sector.

It is important that the Luxembourg financial sector regains solid bases because the national and international economic environment, as well as the fact that the Luxembourg entities belong to groups and their activities often require an advanced specialisation, imply that these entities are subject to considerable risk concentrations. In the light of these elements and the numerous interconnections between the Luxembourg financial centre and the global financial system, the conclusions and recommendations to be drawn from the thorough assessment of our financial sector carried out by the International Monetary Fund in 2010, which included stress tests broader than those performed at EU level, shall be analysed and closely followed as from their publication in 2011. At this point, we may assert that the preliminary observations of this assessment show a systemic stability of the financial centre which, overall, complies with the principles and objectives set out at international level as regards the supervision of banks and of financial markets.

2010 was also marked by the quick progress in enhancing the regulations and the supervision of the financial sector. This enhancement is the logical consequence requested by the public and the political authorities following the financial crisis triggered by the irresponsible behaviour of many economic players. In order to enhance financial stability, banks shall meet stricter requirements as regards own funds, liquidity, risk coverage and protection of depositors. Investors' protection is enhanced, *inter alia*, as regards information, liability of the depositaries, supervision of managers and functioning of the markets.

Finally, in the framework of the European Union, 2010 ended with the implementation of the European System of Financial Supervisors (ESFS) which includes the three sectoral authorities and the European Systemic Risk Board (ESRB).

The CSSF fully accepts its responsibilities by ensuring that all players of the Luxembourg financial sector observe all the applicable laws and regulations. In that respect, it should be borne in mind that, as from 2010, the audit professionals are subject to public oversight, change of paradigm for the whole profession but also for the authority in charge of the oversight, namely the CSSF. Generally, the CSSF has systematically enhanced its field presence by doubling its team dedicated to on-site inspections. "On-site visits" performed by the CSSF at the newly established professionals turned out to be very useful for both parties. The CSSF has also reformed its internal procedures so as to be able to treat the files within a shorter time limit and also to intervene more quickly and efficiently when it notices irregularities, weaknesses or risks at the entities subject to its supervision. In the course of the development of its website, the CSSF also chose to make more information and practical services available to the supervised entities and to contribute to a better financial education of the public. Moreover, as announced, it prepared a draft law completing the measures of administrative police which are at its disposal and substantially improving the texts governing the sanctions in case of non-compliance with the financial sector regulation.

A small number of players of the financial sector may not have yet understood the reason for and the necessity of on-site inspections and more thorough CSSF interventions. They seem to consider it as an obstacle for their business. Should we remind that Luxembourg would probably not have been withdrawn from the procedure leading to the registration on the FATF grey list, if all the authorities concerned had not made an extraordinary effort to enhance the legislative arsenal and to concretely implement it through a close supervision followed, if necessary, by effective sanctions? The reputation of the financial sector and its acceptance by its peers and competitors implies zero tolerance for behaviour which is reprehensible or clearly illegal. The main leaders of the financial professions are fully aware of this situation and encourage the efforts of the supervisory authority.

These efforts will not be mastered without reinforcing the CSSF resources. In 2010, several recruitment campaigns led again to an increase in the CSSF staff. The executive board would like to thank all the CSSF agents who show an ongoing commitment as regards the performance of their duties which are more and more complex. The current studies and steps for the construction of a new CSSF head office reflect the future of the institution.

Jean GUILL

Director General

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CORPORATE GOVERNING BODIES OF THE CSSF

Board of Directors

Chairman	Etienne REUTER	Premier Conseiller de Gouvernement, Ministry of Finance
Vice-chairman	Gaston REINESCH	General administrator, Ministry of Finance
Members	Ernst-Wilhelm CONTZEN	Chairman of the Association des Banques et Banquiers, Luxembourg
	Rafik FISCHER	Member of the Board of Directors of the Association Luxembourgeoise des Fonds d'Investissement
	Jean FUCHS	Chairman of the Association Luxembourgeoise des Professionnels du Patrimoine
	Sarah KHABIRPOUR	Conseiller de direction adjoint, Ministry of Finance
	Claude WIRION	Member of the Executive Committee of the Commissariat aux Assurances
Secretary	Danielle MANDER	

Executive Board

Director General	Jean GUILL
Directors	Simone DELCOURT
	Andrée BILLON
	Claude SIMON

Executive Board of the CSSF
Left to right: Andrée BILLON, Jean GUILL, Simone DELCOURT, Claude SIMON

SUMMARY

In 2010, the Luxembourg financial centre showed a solid resilience against the challenges posed by the changes resulting from the financial crisis in 2008 and against difficulties peculiar to the financial year 2010, of which notably the uncertainties related to the development of public finances in Europe. Besides the results realised by the banking sector, although more modest than before the crisis, it is mainly worth mentioning that the investment fund sector in a broad sense, which is somehow the driving force of the Luxembourg financial sector, improved. It is important now to consolidate these experiences in order to rebuild solid bases which allow the financial sector to compare positively to foreign rival financial sectors and the financial players to assert themselves in the international groups to which they belong.

International aspects of supervision

The harmonisation of existing regulations remains of utmost importance at international level, notably as regards risk management and coverage. Moreover, the functioning of the colleges of supervisors for cross-border banking groups has strengthened the cooperation between the national supervisory authorities and increased the European and international dimensions of prudential supervision. As from 2011, the European dimension will be further enhanced by the implementation of the new European supervisory authorities EBA, ESMA and EIOPA.

147 credit institutions
Balance sheet total: EUR 766.4 billion
Net profit: EUR 3,849 million

The number of banks decreased by two entities and reached 147 entities as at 31 December 2010. During the year, four banks started their activities while four banks merged with other banks of the financial centre and two banks terminated their activities.

The aggregated balance sheet total decreased by 3.4% in 2010, i.e. a drop less marked than in 2009. This fall is recorded in a context of uncertainties as regards the public finances in Europe, which reduced the intermediation activity, as well as in a post-crisis context which is synonymous with cessation of activities and reduction of risks for a certain number of banks. However, it should be borne in mind that 60% of the banks registered a rise in their balance sheet which suggests a trend reversal.

Net profit of the Luxembourg banking sector reached EUR 3,849 million in 2010. This remarkable improvement compared to 2009 mainly results from the strong drop in creation of provisions. Indeed, due to more favourable forecasts in relation to growth, financial valuation and economic data, the need for additional provisions is diminished. Nevertheless, 45% of banks ended their financial year with a decreased net result compared to the previous year.

3,667 UCIs
12,937 units
Total net assets: EUR 2,199.0 billion

In 2010, the UCI sector registered a 19.4% growth in net assets, originating for 45% from net subscriptions and for 55% from the positive performance of stock exchanges. Net capital investments in Luxembourg UCIs amounted to EUR 161.6 billion in 2010, which proves the investors' renewed confidence in the markets.

The number of UCIs grew by 5.9% during the year. This growth almost entirely results from the continuing boom of the specialised investment funds which represent 32.5% of the total number of UCIs (in terms of net assets, they represent 9.7%). Taking into account umbrella funds, a total of 12,937 economic entities were active on 31 December 2010, which represents a new record.

179 management companies

The number of management companies authorised in accordance with Chapter 13 of the law of 20 December 2002 relating to UCIs decreased from 192 as at 31 December 2009 to 179 at the end of 2010, as a result of seven new authorisations and twenty withdrawals mainly due to mergers and the rationalisation of the Luxembourg structures initiated by the promoters. The management companies focus on collective management and slowly abandon the ancillary activities set out in the law.

15 pension funds

The pension funds sector stagnated in 2010 since no new pension fund was authorised during the year.

247 SICARs
Balance sheet total: EUR 25.1 billion

The number of investment companies in risk capital (SICAR) continued to grow with 31 new authorisations against twenty withdrawals during 2010. Most initiators of SICARs are French, followed by Swiss, German and Luxembourg. As regards the investment policy, the SICARs prefer private equity.

26 authorised securitisation undertakings

The slow but ongoing development of the securitisation activity, at least as regards the part subject to authorisation and supervision, continued with three new securitisation undertakings authorised in 2010.

301 PFS (109 investment firms, 113 other PFS, 79 support PFS)
Balance sheet total: EUR 11.42 billion
Net profit: EUR 1,452.3 million

With 33 new entities authorised during 2010 and 18 withdrawals, the PFS sector continued attracting new promoters. The positive development in the number is mainly attributable to PFS other than investment firms and, to a lesser extent, to support PFS.

The aggregated total balance sheet of PFS reached EUR 11.42 billion as at 31 December 2010, as against EUR 22.46 billion at the end of 2009. This important drop of 49.14% is mainly attributable to the decrease of the business volume of one professional performing credit offering.

The net results of PFS also fell but to a lesser extent (-7.91%). This development hides some differences between the various categories of PFS: the net results of investment firms and support PFS remained stable or registered even a slight increase, whereas the negative development of the other PFS' results is mainly due to two large financial players.

Total employment in the supervised entities: 42,752 people
(of which banks: 26,254 people, PFS: 14,159 people, management companies: 2,339 people)

Total employment in the financial sector improved by 1.3%, i.e. 539 people. However, depending on the category of financial players, the situation diverges.

Following the economic restructuring and cost reduction measures caused by the financial crisis, the downward trend in the banking employment continued in 2010 (-0.6%) even though the drop is more moderate than the previous year. 59.8% of banks maintained or increased their staff in 2010 by taking advantage of the opportunities offered at the moment by the labour market.

Employment in the PFS sector increased by 5.0% mainly due to support PFS (+768 jobs). However, this increase does not correspond to the creation of as many jobs in the sector of support PFS. Indeed, a large part of this rise is attributable to support PFS newly authorised in 2010, among which are companies already active before. The existing staff of these companies is included, as from the date of the authorisation, in the statistics regarding support PFS.

Employment in management companies slightly increased in 2010 (+1.3%).

1,390 prospectuses, base prospectuses and other documents approved

723 supervised issuers

1.1 million of transactions in financial instruments reported

The number of files submitted in Luxembourg for the approval of prospectuses to be published when securities are offered to the public or admitted to trading on a regulated market remained stable compared to 2009.

The CSSF supervises issuers whose transferable securities are admitted to trading on a regulated market and for which Luxembourg is the home Member State for the purposes of the Transparency law. Their number reached 723, of which 244 Luxembourg issuers. The supervision involves a general follow-up of regulated information to be published by issuers as well as the enforcement of the financial information, i.e. an assessment of compliance of the financial information with the relevant reporting framework.

As part of its supervision of markets and market operators, the CSSF received about 1.1 million transaction reports in 2010 which allow following the trends on the markets and detecting possible offences. In the framework of the law on market abuse, the CSSF opened eight investigations in relation to insider dealing and/or market manipulation and dealt with 48 requests from foreign authorities.

Public oversight of the audit profession

The public oversight of the audit profession covers 74 *cabinets de révision agréés* (approved audit firms) and 232 *réviseurs d'entreprises agréés* (approved statutory auditors) as at 31 December 2010. The oversight covers also 48 third-country auditors and audit firms duly registered in accordance with the law of 18 December 2009 concerning the audit profession.

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

499 customer complaints

By virtue of its specific task of mediating as regards handling of customer complaints, the CSSF received 499 complaints during the previous year. The main part of the complaints concerned e-banking. Complaints in relation to private banking were also a greater part of the files dealt with by the CSSF.

362 employees

Operating costs of the CSSF in 2010: EUR 37.8 million

2010 was marked by the ongoing increase in the CSSF's human resources (+40 agents) in order to face the growing workload resulting notably from the introduction of new prudential requirements, the cooperation between supervisory authorities, the active participation in international forums and, in general, from the increase in volume and complexity of the financial products. In addition, numerous on-site inspections are carried out which have become an important part of the prudential supervision exercised by CSSF.

CSSF's heads of department

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

GENERAL SUPERVISION AND INTERNATIONAL COOPERATION

01

1. General Supervision
2. Cooperation within European institutions
3. Multilateral cooperation

1. GENERAL SUPERVISION

The department "General supervision" (SGE) deals transversally with issues relating to prudential supervision, accounting and reporting common to the CSSF's departments. In particular, it is in charge of the international groups and the development and interpretation of national and international regulations.

Each division of the department, apart from division 4, is responsible, within its given area, for the development and interpretation of national and international regulation, for the treatment of general methodology issues related to prudential supervision, for the rules of conduct and professional obligations in the financial sector as well as for the elaboration of statistical analyses and global studies on professionals of the financial sector and on the financial markets and products. Division 4 is responsible for the planning, coordination and carrying out of on-site inspections.

In 2010, the SGE sent 301 letters outlining the CSSF's position with respect to prudential and accounting supervision. Moreover, SGE agents attended 173 meetings of international bodies. As in previous years, SGE agents were also asked to draft circulars or preparatory texts for new laws.

1.1. Division 1: International matters

This division deals with a large amount of international files relating to the CSSF's mission, among which, in particular, those dealt with by the following bodies: the European Commission, the Council of the EU, CEBS, CESR, CEIOPS, the *Institut francophone de la régulation financière*, IOSCO, OECD, the Basel Committee and the European Central Bank. In addition, the division is responsible for the coordination of preparatory meetings which define the CSSF's stances to be taken during meetings at the highest level of the above-mentioned bodies.

The division prepares the transposition of international regulation into national law and monitors the national and international developments in the areas within the CSSF's competences and duties. In this context, the division closely cooperates with the departments responsible for the prudential supervision. It provides these departments with its expertise, assists them with subjects within its competence and organises trainings for the agents concerned.

In particular, the division cooperates with the departments "Supervision of banks" and "Supervision of securities markets" regarding questions about the CSSF's general policy in relation to international cooperation and, if necessary, more practical aspects in this matter. In the context of the CEBS and CESR Review Panel missions, the division closely works with the departments concerned on issues subject to peer reviews.

During 2010, the work of division 1 was mainly dedicated to:

- the participation in international groups which it deals with;
- the transposition of European directives and guidelines, particularly from CEBS and CESR, in the form of circulars or laws; and
- the provision of information and support to the departments in charge of prudential supervision or directly to the supervised entities in relation to issues on the implementation and application of new laws and regulations.

The transposition of the directives known as CRD II and CRD III, presented in more detail in Chapter XIV of this report, can be cited as an example of the division's organisation of work in prudential regulation. Thus, the agents of division 1 participated as experts in meetings at the European Commission and the Council of the EU, ensured the transposition of these directives into national law and held trainings for the departments responsible for the supervision of credit institutions and investment firms concerned by this new legislation. Furthermore, the agents of division 1 also provided answers to many questions and uncertainties encountered by the supervised entities as regards the new provisions in relation to the regulation on large exposures likely to have a considerable impact on the financial sector.

In addition, the division is responsible for the national part of the supervisory framework for credit rating agencies introduced by Regulation (EC) No 1060/2009. It ensures the international cooperation between authorities in this area.

1.2. Division 2: Accounting, reporting and audit

Division 2 is responsible for the follow-up at national level (*Commission des Normes Comptables*, Luxembourg Central Bank) and international level (European Commission, Council of the EU, CEBS, CESR, IOSCO, Basel Committee, EFRAG) of all regulations relating to (1) accounting and financial information to be disclosed by professionals of the financial sector and by listed companies and (2) audit matters in relation to supervision of entities in the financial sector.

The division prepares instructions, circulars and draft laws on reporting and accounting by professionals of the financial sector, designs new prudential tables and redefines the structure and content of existing tables. The division also deals with issues relating to accounting and financial information to be published and to prudential reporting.

The division cooperates with the department "Supervision of securities markets" which is responsible for the enforcement of financial information of companies whose securities are admitted to trading on the regulated market of the Luxembourg Stock Exchange.

The division is responsible for all questions relating to the elaboration and definition of the content of analytical reports prepared by *réviseurs d'entreprises agréés* (approved statutory auditors). The division is also responsible for the centralisation of information concerning *réviseurs d'entreprises agréés* which are authorised to audit the accounts of professionals of the financial sector and for processing, together with the departments concerned, the authorisation requests for *réviseurs d'entreprises agréés* wishing to audit the accounts of professionals of the financial sector.

During 2010, division 2 contributed to the CEBS works on the FINREP reporting scheme which consist, in particular, of including the amendments resulting from the project to replace IAS 39 (which is expected to be finalised in 2011) in the FINREP reporting scheme.

1.3. Division 3: Rules of governance, electronic payments and crisis management

The mission of division 3 concentrates on the methodology, on global studies and on assisting other departments on matters which require specific knowledge and expertise.

Within the context of its mission, the division ensures the follow-up of principles and standards commonly accepted in corporate governance and of compliance with rules of conduct which stem, *inter alia,* from EU texts.

During 2010, division 3 carried out three on-site inspections in relation to the MiFID Directive. On some occasions, it appeared that the client suitability test has not been performed prior to the provision of an asset management service. In one case, a credit institution recommended a complex financial instrument, i.e. a structured product, to its clients without providing clear information about any limitations of the secondary market during a future disposal or about the possible losses in case of bankruptcy of a company which is included in the basket of equities forming the underlying of the structured product. Following the CSSF's intervention, the institutions concerned took the necessary measures to comply with the MiFID provisions.

The division is also responsible for questions in relation to payment institutions and electronic money institutions. Thus, it reviewed several authorisation files for the status of payment institution set out in the law of 10 November 2009 on payment services. The CSSF noted that the files were often incomplete and their quality unsatisfactory, not allowing it thus to issue a favourable opinion. In particular, it was noted that many applicants were not aware of the fact that the authorisation is subject to the production of evidence of the existence in Luxembourg of the central administration and the registered office of the institution to be authorised.

The division contributes to the drawing-up of crisis management procedures and the organisation of stress tests. Thus, the members of the division were asked to participate in international groups dealing with crisis management and with drafting the EU legal proposals in relation to crisis resolution tools.

The division contributes to the revision of the deposit guarantee schemes and investor-compensation schemes at EU level. It will organise the implementation of the new schemes in the relevant legislation.

During 2010, division 3 analysed the remuneration policies of credit institutions and investment firms which had to disclose their remuneration policy to the CSSF in accordance with Section IV of Circular CSSF 10/437 concerning the remuneration policies in the financial sector. The division also drew up an FAQ on the practical application of the circular, which includes notably Question 26 indicating to the institutions concerned the elements which have to be part of their policy.

The analysis of the different policies clearly showed that some requirements imposed by the circular were often not fulfilled. Indeed, the following elements were often missing: the definition of the material risk takers and their number, the variable remuneration rate in % of the total annual remuneration for these persons, the total variable remuneration rate in % of the total annual remuneration for the whole staff. The description of the performance criteria as well as their risk weight and the description of the performance assessment procedure were generally insufficiently dealt with by the institutions. The CSSF asked these institutions to review their remuneration policy and to take into account, during this revision, the new rules set out in circulars CSSF 10/496 and CSSF 10/497 which transpose Directive 2010/76/EU of 24 November 2010.

1.4. Division 4: On-site inspections

In 2010, the CSSF Executive board decided to strengthen the team of division 4 in order to increase the frequency and to widen the scope of on-site inspections and particularly the control missions regarding the fight against money laundering and terrorist financing (AML/CFT). The number of agents of division 4 went thus progressively up to ten.

The organisation of division 4 was consequently refined. Besides the general unit composed of three agents responsible for "introductory visits" at the newly authorised professionals, for *ad hoc* missions and for thematic missions about subjects other than money laundering and terrorist financing, a group specialised in AML/CFT was created which is composed of six agents exclusively in charge of on-site inspections in this area.

In addition to the members of division 4, agents from the department directly in charge of the supervision of the controlled entity also participate in the on-site inspections. Moreover, other agents of the CSSF, as for example the agents of the Legal Department, may be asked to intervene during the preparation, the course or the follow-up of the on-site inspection.

The annual programme of on-site inspections, approved by the Executive board, is drawn up based on suggestions from the CSSF's heads of departments and according to a risk-based approach.

During 2010, division 4 carried out 76 on-site inspections. The following table breaks down these on-site inspections according to the type of controlled entity and the type of mission.

Type of controlled entity	Type of mission		
	Fight against money laundering and terrorist financing	Introductory visit	*Ad hoc* mission
Credit institutions	15	5	9
Investment firms	6	3	3
Support PFS	-	1	3
Other PFS	4	8	3
UCIs, SIFs	3	-	1
SICARs	1	-	7
Management companies	2	-	2
Total	**31**	**17**	**28**

2. COOPERATION WITHIN EUROPEAN INSTITUTIONS

Article 3 of the law of 23 December 1998 establishing a financial sector supervisory commission ("Commission de surveillance du secteur financier"), appoints the CSSF, *inter alia*, to deal with the files and participate in the negotiations concerning financial sector issues, at both EU and international level. In accordance therewith, the CSSF participates in the work of the following fora.

2.1. Committee of European Banking Supervisors (CEBS)

The Committee of European Banking Supervisors (CEBS) was established by Commission Decision 2004/5/EC of 5 November 2003. CEBS' aim is to fulfil the Level 3 functions for the banking sector under the Lamfalussy procedure, its missions being the following:

- to advise the European Commission, in particular as regards the preparation of draft implementing measures for banking activities;
- to contribute to the consistent application of European directives and to the convergence of Member States' supervisory practices throughout the European Community; and
- to improve cooperation as regards prudential supervision.

Mr Giovanni Carosio (Banca d'Italia, Italy) was the Chairman of CEBS in 2010.

During 2010, the CSSF participated as a member in the work of CEBS, its permanent working groups and sub-working groups (permanent or *ad hoc*) below:

- Review Panel;
- *Groupe de Contact* (and its subgroups: Subgroup on Operational Networks, Pillar 2 Convergence Network, Liquidity Risk Management Task Force, Internal Governance Task Force);
- Expert Group on Prudential Regulation (and its subgroups: Subgroup on Own Funds, Subgroup on Operational Risk, Subgroup on Credit Risk, Subgroup on Market Risk, Task Force on Securitisation, Working Group on ECAIs[1]);
- Expert Group on Financial Information (and its subgroups: Subgroup on Accounting, Subgroup on Auditing, Task Force on Procyclicality and Accounting, Reporting Subgroup, Transparency Subgroup, COREP Network, FINREP Network, XBRL Network).

Among the activities of CEBS and of its working groups in 2010, the following subjects are of particular interest for the Luxembourg financial centre and/or resulted in the publication of CEBS guidelines on which the CSSF representatives actively cooperated.

It should be noted that all CEBS publications may be viewed on the website www.eba.europa.eu.

2.1.1. Capital adequacy

In the context of capital adequacy (directives known as CRD, CRD II and CRD III), CEBS published, among others, guidelines meant to clarify the provisions in the context of the definition of capital ("CEBS Guidelines on instruments referred to in Article 57a of the CRD" of 14 June 2010), of large exposures ("CEBS Guidelines on Article 106(2) (c) and (d) of the CRD" of 28 July 2010) and of securitisation ("CEBS Guidelines on the application of Article 122a of the CRD" of 31 December 2010).

In the specific context of the supervisory review process, CEBS published guidelines in relation to risk management ("CEBS High Level Principles for risk management" of 16 February 2010), stress testing ("CEBS Revised Guidelines on stress testing" of 26 August 2010) and management of concentration risk ("CEBS Revised Guidelines on the management of concentration risk" of 2 September 2010).

[1] External Credit Assessment Institutions.

2.1.2. Prudential reporting

In 2010, CEBS undertook the revision of FINREP rev2, the provisional revised version of the FINREP reporting scheme applicable as from 1 January 2012, in order to take into account the IASB changes, particularly the replacement of IAS 39 and IAS 1 that was scheduled to be finalised in 2010. However, as IASB has, so far, not finalised the above replacement projects, CEBS has decided that a new revised financial reporting framework (FINREP rev3) will be published by EBA[2] by the end of 2011, with an application date set on 1 January 2013. Following this decision, the CSSF decided not to implement FINREP rev2 as from 1 January 2012.

2.1.3. Supervisory colleges / cross-border banking groups

CEBS published guidelines on the functioning of supervisory colleges ("CEBS Guidelines for the operational functioning of colleges" of 15 June 2010) and on the cooperation of supervisory authorities (in supervisory colleges) for the supervisory review process and the assessment regarding the capital adequacy of cross-border groups ("CEBS Guidelines for the joint assessment and joint decision regarding the capital adequacy of cross-border groups" of 22 December 2010).

2.1.4. Remuneration

The work of the CEBS Internal Governance Task Force resulted in the publication of guidelines regarding remuneration policies and practices which were implemented in Luxembourg through circulars CSSF 10/496 and CSSF 10/497 transposing Directive 2010/76/EU, commonly known as CRD III (cf. Chapter XIV "Banking and financial laws and regulations"). The purpose of these guidelines ("CEBS Guidelines on remuneration policies and practices" of 10 December 2010) is to facilitate, for the persons concerned, the application of sound remuneration policies which comply with the principles included in points 23 and 24 of Annex V to Directive 2010/76/EU.

2.1.5. Joint task forces

In 2010, the CSSF was a member of the Joint Task Force on the Impact of the new Capital Framework (TFICF), a joint group of CEBS and the Banking Supervision Committee of the European Central Bank. This group carried out two empirical studies on the impact of Basel II regulations on the different components of prudential ratios and was also in charge of leading an impact study on the consequences of the proposed Basel III rules.

In 2010, the CSSF was also a member of the Joint Committee on Financial Conglomerates (JCFC), a joint group of CEBS and CEIOPS regarding the supervision of financial conglomerates.

Furthermore, in the context of the fight against money laundering and terrorist financing, the CSSF participated in the work of the Anti-Money Laundering Task Force (AMLTF), a joint group of CEBS, CESR and CEIOPS (cf. Chapter XIII "Fight against money laundering and terrorist financing").

2.2. Committee of European Securities Regulators (CESR)

The Committee of European Securities Regulators (CESR) which is composed of representatives of 29 supervisory authorities of securities markets in the European Economic Area (EU Member States, Norway and Iceland) assists the European Commission in preparing implementing measures relating to Community legislation on transferable securities and is entrusted with ensuring the harmonised and continuous application of Community legislation in the Member States. CESR also works towards improving coordination among supervisory authorities. On 1 August 2010, Mr Carlos Tavares (CMVM, Portugal) has replaced Mr Eddy Wymeersch (CBFA, Belgium) as Chairman of CESR. Mr Jean Guill (CSSF, Luxembourg) replaced Mr Carlos Tavares as Vice Chairman.

In 2010, CESR continued its Level 3 work by drawing up recommendations, standards, common interpretations and procedures for the practical cooperation in different areas in order to enhance regulatory convergence at European level.

[2] EBA (European Banking Authority) has taken over all tasks and responsibilities from CEBS as from 1 January 2011. For further details on the new European authorities, please refer to point 2.6. of this Chapter.

The Market Consultative Panel, a committee comprising 17 market participants appointed in a personal capacity, among which one Luxembourg representative, is charged with assisting CESR. The three meetings of the committee mainly dealt with the financial crisis, the review of the Transparency Directive, the packaged retail investment products (PRIPs), the high frequency trading, the credit default swaps (CDS) and subjects in relation to the markets' infrastructure based on the White Paper.

The CSSF attends the meetings of the Review Panel and of the eight working groups: CESR-Pol, CESR Standing Committee on corporate reporting, CESR Standing Committee on corporate finance, CESR Standing Committee on credit rating agencies, CESR Standing Committee on secondary markets, CESR Standing Committee on post-trading, CESR Standing Committee on investor protection and intermediaries and CESR Standing Committee on investment management. Moreover, the CSSF contributed to the work of some sub-working groups of the above-mentioned groups. The CSSF also attended the meetings of the takeover bids network.

Within the scope of the works carried out by the above groups, the following subjects should be pointed out.

2.2.1. Review Panel

The Review Panel, chaired by Mr Guill since 1 August 2010 in his capacity as Vice Chairman of CESR, is responsible for assisting CESR in ensuring consistent and harmonised implementation of EU legislation in the Member States. The Review Panel finalised the work on the comparison of the implementation and application of options and discretions as well as gold plating in the context of the Market Abuse Directive and of its implementing measures. The final report was published on 6 April 2010 (CESR/09-1120).

On 29 November 2010, the Review Panel published a summary regarding the work on the selective mapping with regard to the Prospectus Directive (CESR/10-123).

Finally, on 18 January 2011, the Review Panel published a summary of the report on the mapping of the authorities' powers in crisis situations (ESMA/2011/26).

2.2.2. CESR-Pol

On 2 March 2010, CESR-Pol published its report (CESR/10-088) on the implementation of a regime of reporting to the competent authority and of disclosure of short positions in shares that are admitted to trading on an EEA regulated market and/or an EEA MTF ("short selling" regime). On 26 May 2010, CESR published a report on the technical details regarding short selling (CESR/10-453). Based on the work of CESR-Pol, CESR recommended to the European Commission to introduce such a regime on short selling (CESR/10-618).

CESR-Pol also dealt with the transaction reporting in the framework of the questions raised by the European Commission on the project to review the MiFID Directive during 2011. In this context, it should be noted that CESR intends to require that all Member States introduce a mandatory client identification code for transaction reportings. However, the CSSF objects thereto. In case of transmission of transaction orders from one intermediary to another, the work also includes proposals to transmit details of the client identification code from one financial intermediary to another or that each intermediary intervening in the chain transmits these details to its competent authority. The proposals also refer to the introduction of a third trading capacity (riskless principal) and the extension of the transaction reporting obligation to all members of regulated markets or MTFs, even if these members are not investment firms. Based on this work, CESR recommended to the European Commission to amend the above-mentioned four points in the MiFID Directive (CESR/10-808).

Finally, CESR-Pol prepared the CESR recommendation to the European Commission as regards the review of the MiFID Directive on the standardisation and organisation of trading platforms, the trading of over-the-counter (OTC) derivatives, the pre- and post-trading transparency obligations, the standards regarding client categorisation, the extension of transaction reporting to derivatives which are not admitted to trading on a regulated market but which have an underlying admitted to trading on a regulated market and to financial instruments which are only admitted to trading on an MTF as well as on the extension of the transaction and position reporting regarding commodities markets firms (CESR/10-1254).

2.2.3. CESR Standing Committee on corporate reporting

Within the scope of the works of the CESR Standing Committee on corporate reporting, the CSSF joined a new working group called CESR Task Force on Storage of Regulated Information which deals with issues on the future development of the electronic network linking the Officially Appointed Mechanisms (OAMs) for storage of regulated information as referred to in Commission Recommendation 2007/657/EC of 11 October 2007. In addition, this group analyses the appropriateness of introducing a standardised electronic language for the publication of financial information.

The working group published the consultation paper "Development of Pan-European Access to Financial Information Disclosed by Listed Companies", on 2 August 2010, which describes the two options for the storage of regulated information at European level. The CSSF points out its preference for the model of a European network linking national OAMs.

2.2.4. Corporate Finance Standing Committee (CFSC)

The CFSC is in charge of the work regarding the Prospectus Directive, some aspects of the Transparency Directive and corporate governance.

- **Prospectus**

In 2010, the CFSC took part in the drawing-up of good practices proposed by the Review Panel, thus fulfilling its main mission of ensuring consistent and convergent implementation of the European provisions relating to prospectuses for securities.

Furthermore, the following documents were published:

- data on prospectuses approved and passported in the different Member States from July 2009 to December 2009 and from January 2010 to June 2010;
- update of the list of national requirements concerning notifications (language, translation of the summary, etc.) on 6 October 2010;
- public consultation on proposed amendments to CESR's recommendations regarding mineral companies on 23 April 2010;
- common positions on questions raised in the context of the implementation of the Prospectus Directive by updating the CESR FAQ twice, in July and November 2010. The updates dealt with:
  - the responsibility of the translation quality of passported prospectuses;
  - language requirements relating to documents incorporated by reference; and
  - validity period of a prospectus composed of separate documents.

In addition, on 19 January 2011, the European Commission sent a mandate to ESMA for advice on possible delegated acts concerning the Prospectus Directive as amended by the Directive 2010/73/EU of 24 November 2010. In the context of this mandate, the CFSC created a specific temporary Task Force in order to prepare the proposal for advice for the European Commission. The CFSC decided to primarily deal with the following aspects:

- the format of the Final Terms of a base prospectus;
- the format of the summary of the prospectus and the specific form and detailed content of the key information to be included in the summary;
- the proportionate disclosure regime as set forth in Article 7 of Directive 2010/73/EU.

The Task Force decided to create three subgroups, each dealing with one of the above aspects. Luxembourg was appointed coordinator of the first subgroup in charge of the Final Terms.

Finally, in September 2010, a Consultative Working Group (CWG) was created within CFSC. The CWG was set up so as to allow the CFSC to take into account the advice and expertise of specialists among the different market participants. Luxembourg is represented by a lawyer who is partner in one of the major law firms of the financial centre.

- **Transparency**

In May 2010, the CSSF attended two meetings of the CESR Drafting Group responsible for analysing the answers received following the public consultation prepared by CESR in 2009 to extend the scope of the disclosure requirements of major shareholdings arising from the Transparency Directive.

Moreover, in May 2010, the European Commission started a public consultation to modernise the Transparency Directive. The CSSF participated in the preparation of an answer by the CESR Transparency Task Force (TD review) to this consultation.

- **Corporate governance**

At the end of 2010, the Advisory Group on Corporate Governance was set up in order to deal with certain aspects of corporate governance. Particular interest was to analyse in-depth the problems related to proxy advisors whom many investment fund managers designate to vote in general meetings and extraordinary general meetings of companies held in their investment portfolio. Indeed, such an analysis is necessary since many of these proxy advisors make voting recommendations for institutional investors and advise at the same time some target companies of the institutional investors on corporate governance. In addition, the proxy advisory services are a highly concentrated market.

2.2.5. CESR Investor Protection and Intermediaries Standing Committee

This committee works to a great extent on questions asked by the European Commission in the context of the MiFID Directive review project.

The following documents were published, among others:

- "Report – Inducements: Good and poor practices" (CESR/10-295, 29 April 2010);
- "CESR Technical Advice to the European Commission in the context of the MiFID Review – Investor Protection and Intermediaries" (CESR/10-859, 29 July 2010);
- "CESR's Responses to Questions 15-18 and 20-25 of the European Commission to the Review of MiFID" (CESR/10-860, 6 May 2010).

It is also worth mentioning the document "CESR's Responses to Questions 15-18 and 20-25 of the European Commission Request for Additional Information in Relation to the Review of MiFID" where the CSSF expressed reservations to the prohibition to receive retrocessions of management commissions, also known as trailer fees, paid by the investment fund managers in the context of discretionary management.

2.2.6. CESR Standing Committee on Secondary Markets

The CESR Standing Committee on Secondary Markets drew up the consultation paper "CESR Technical Advice to the European Commission in the Context of the MiFID Review - Equity Markets" (CESR/10-394) which includes, among others, the creation of an EU mandatory consolidated tape (MCT) to which regulated markets (including the Luxembourg Stock Exchange), MTFs and Approved Publication Arrangements (APAs) shall report transactions in the required format. The purpose of this proposal is to remove the barriers to consolidation of post-trade transparency information.

As the MCT will have to be a non-profit-making entity, the profits made, after deduction of the operational expenses and costs in capital, will be redistributed to the regulated markets, the MTFs and the APAs which contributed to the MCT, according to the number/volume of transactions.

2.2.7. Investment Management Standing Committee

The Investment Management Standing Committee and its sub-working groups dealt, among others, with the following four subjects:

- Key Investor Information Document;
- procedures on risk management and measurement;
- Alternative Investment Fund Managers Directive (AIFM);
- operational prudential supervision (Operational Task Force).

The committee is assisted by a consultative group consisting of 23 industry experts, including one representative of the Luxembourg investment fund sector.

On 19 May 2010, CESR published its guidelines on the common definition of “money market funds” (“CESR Guidelines on a common definition of European money market funds” - CESR/10-049).

CESR’s guidelines on a common definition of money market funds set out an approach leading to two categories of money market funds: “short-term money market funds” and “money market funds”. The purpose of CESR’s guidelines is to improve investor protection. These guidelines lay down the criteria to fulfil in order to use the label “short-term money market funds” and “money market funds”. They are applicable to UCITS covered by the UCITS Directive as well as to investment funds not covered by this Directive.

The guidelines enter into force on the same date as Directive 2009/65/EC, i.e. on 1 July 2011. However, money market funds which existed before 1 July 2011 benefit from a six-month transition period, i.e. until 31 December 2011, in order to comply with some requirements of the guidelines. As Directive 2009/65/EC has already been transposed in Luxembourg by the law of 17 December 2010, the CSSF will apply CESR’s guidelines to money market funds which submit themselves to the law of 17 December 2010 before 1 July 2011. As regards money market funds which will be governed by the law of 17 December 2010 only from 1 July 2011, the CSSF will apply the CESR guidelines from this date onwards.

The following documents published in 2010 may also be pointed out:

- “CESR Guidelines on the methodology for the calculation of the synthetic risk and reward indicator in the Key Investor Information Document” (CESR/10-673, 1 July 2010);
- “CESR Guidelines on the methodology for calculation of the ongoing charges figure in the Key Investor Information Document” (CESR/10-674, 1 July 2010);
- “CESR Guidelines on Risk Measurement and the Calculation of Global Exposure and Counterparty Risk for UCITS” (CESR/10-788, 28 July 2010);
- “CESR Guidelines on the Selection and presentation of performance scenarios in the Key Investor Information document (KII) for structured UCITS” (CESR/10-1318, 20 December 2010);
- “CESR Guidelines on the Transition from the Simplified Prospectus to the Key Investor Information document” (CESR/10-1319, 20 December 2010);
- “CESR’s guide to clear language and layout for the Key Investor Information document” (CESR/10-1320, 20 December 2010);
- “CESR’s template for the Key Investor Information document” (CESR/10-1321, 20 December 2010).

These documents are referred to in Circular CSSF 11/498. The CSSF will apply the above-mentioned guidelines without any further transposition.

The European Commission asked ESMA for advice on delegated acts set out in the AIFM Directive. ESMA is also asked to participate in the drawing-up of regulatory technical standards and implementing technical standards in relation to the AIFM Directive. Finally, ESMA will prepare guidelines and recommendations in the context of the AIFM Directive.

The Investment Management Standing Committee set up four Task Forces where the CSSF actively participates and which deal with:

- the scope of the AIFM Directive;
- the authorisations under the AIFM Directive and general operating conditions;
- the depositaries under the AIFM Directive;
- the leverage, transparency, risk management and information to be provided under the AIFM Directive.

All the documents are available on ESMA's website (www.esma.europa.eu).

2.3. Capital Requirements Directive Working Group (CRDWG)

This working group, which was set up by the European Commission in 2007 in order to discuss with Member States the amendments it wished to make to the CRD Directives (2006/48/EC and 2006/49/EC), intensified its work in 2010. At the same time as discussions on Basel III took place at the Basel Committee on banking supervision, the CRDWG discussed the same subjects at European level. Thus, the discussions covered, among others, regulatory capital, the new liquidity ratios and the leverage ratio. The CSSF is represented in the CRDWG and is an active member of several thematic subgroups created to assist the European Commission in the elaboration of the draft European legislation (commonly known as CRD IV) which will transpose Basel III into European legislation.

Further to Basel III, CRD IV will also include provisions pursuant to the single European rule book aiming to reduce the differences in the banking regulation between the Member States. These provisions will mainly reduce the number of national options and discretions included in CRD.

CRDWG's work should result in a proposal for CRD IV by the European Commission before summer 2011. The scope of the draft CRD IV will have an impact on all the institutions of the Luxembourg financial centre, since CRD IV will be the basis for future regulations applicable to institutions.

2.4. European Group of Auditors' Oversight Bodies (EGAOB)

During 2010, the CSSF participated in the works of the European Group of Auditors' Oversight Bodies (EGAOB) and its sub-working groups EGAOB - Subgroup on Cooperation on Third Countries, EGAOB - Subgroup Intra EU members and EGAOB - Subgroup on Inspections.

EGAOB - Subgroup on Cooperation on Third Countries continued analysing the equivalence of public oversight systems for third-country auditors of companies established outside the EU and whose securities are admitted to trading on European regulated markets. This exercise was conducted pursuant to Article 46 of Directive 2006/43/EC which provides, under certain conditions, the option to exempt third-country auditors from public oversight requirements on the basis of reciprocity.

The Decision 2008/627/EC of the European Commission of 29 July 2008 granted a transition period to 34 third countries. This decision allows audit firms from these countries to pursue their audit activity and to delay their registration until 1 July 2010, in accordance with the transition period. A new decision granting an extension of the transition period to 20 third countries was taken on 19 January 2011. In this decision, ten third countries were recognised as equivalent (Australia, Canada, China, Croatia, Japan, Singapore, South Africa, South Korea, Switzerland, the United States of America).

EGAOB - Subgroup on Inspection listed the common problems which supervisory authorities are faced with and initiated the development of means to remedy these situations. These works at a European level also aim to harmonise the approach of the supervisory authorities of the different Member States as regards inspections.

2.5. Others

In addition to the above-mentioned committees and groups, the CSSF agents are also members and participate in the works of the following fora:

- Banking Supervision Committee of the European Central Bank;
- Accounting Regulatory Committee of the European Commission;
- CRD Transposition Group of the European Commission.

As regards AML/CFT, the CSSF contributed in 2010 to the works of the Committee for the prevention of Money Laundering and Terrorist Financing (cf. Chapter XIII “Fight against money laundering and terrorist financing”).

2.6. The new structure of the financial sector supervision in the EU

1 January 2011 was a turning point for the structure of the financial sector supervision in the EU and particularly for the cooperation between the different authorities at EU level. The three Level 3 committees, i.e. CEBS, CESR and CEIOPS, on which this cooperation, which became stronger over the last years, was based, will not be active as from 2011 any more.

Indeed, the proposal by the high-level group, chaired by Mr Jacques de Larosière and mandated by the European Commission to analyse the future of the European financial sector regulation and supervision, became reality through the publication of the regulations (EC) No 1092 to No 1095 of the European Parliament and of the Council of 15 December 2010. These four regulations have instituted, as from 1 January 2011, the European Systemic Risk Board (ESRB) and the three new European supervisory authorities: the European Banking Authority (EBA), the European Insurance and Occupational Pensions Authority (EIOPA) and the European Securities and Markets Authority (ESMA) which together form the new European system for the financial supervision.

As regards the European cooperation, these three new European authorities, each run by a Board of Supervisors composed of a high representative of the national supervisory authorities of each Member State will replace CEBS, CEIOPS and CESR.

Thus, the three new authorities will take over the functions and activities of the former Level 3 committees, including the different expert groups which worked under these committees. However, they have additional competences and, in particular, they will be able to draw up proposals for binding technical standards and act as a mediator (in some cases with a decision-making power) in case of disagreement between national supervisory authorities. They may also act as coordinators in emergency situations and carry out peer reviews. Moreover, ESMA will have direct supervisory powers in relation to credit rating agencies as from the second half of 2011.

ESMA is chaired by Mr Steven Maijoor from the Netherlands. Mr Jean Guill, Director General, represents the CSSF in the Board of Supervisors and has also been appointed member of ESMA’s Management Board.

Mr Claude Simon, Director, represents the CSSF in the Board of Supervisors of EBA, chaired by Mr Andrea Enria from Italy.

3. MULTILATERAL COOPERATION

3.1. Basel Committee on banking supervision

In 2010, the Basel Committee continued working on strengthening the regulation, control and management of risks in the banking sector in the light of the weaknesses observed during the crisis of the financial markets. On 16 December 2010, the Basel Committee published the final version of the new regulatory framework, commonly known as Basel III. The recommended measures, which include a microprudential and a macroprudential part, aim at improving the banking sector's resilience against shocks from financial and economic stress and at improving risk management and governance.

The new Basel III regulation (which will be transposed into EU legislation through CRD IV which is currently being elaborated) is based, on the one hand, on rules concerning the capital composition and adequacy and, on the other hand, on rules concerning liquidity management.

The three main components of the new framework, i.e. the amendments regarding regulatory capital, the leverage ratio and the liquidity ratio are described below.

3.1.1. Regulatory capital

The quality and level of the capital base are raised by insisting on the predominance of common equity and by restricting the definition of this element of capital and also of other constituting elements of tier 1 capital. Thus, particular attention is given to the capacity of loss absorbency of tier 1 capital. Innovative hybrid instruments and dated hybrid instruments may not be included in tier 1 capital. Call options on tier 1 or tier 2 capital instruments are only allowed under strict conditions. Tier 3 capital is abolished. Moreover, elements to be deducted from capital shall henceforth be deducted from common equity and not from the total tier 1 capital or total capital. Finally, the minimum level of common equity that the banks shall have (after deduction) amounts to 4.5% of risk-weighted assets; the minimum level of tier 1 capital amounts to 6%. Besides these two ratios, banks shall continue to observe the capital ratio of 8%. It should be pointed out that each of these three ratios is increased by 2.5% if the capital conservation buffer of 2.5% is added to it.

These new measures concerning the definition of capital probably do not have a significant impact on most of the Luxembourg banks, the capital of which is already mainly made up of common equity. This does not exclude a more substantial impact on specific banks.

The capital conservation buffer will consist of common equity amounting to 2.5% of risk-weighted assets. Restrictions in payment of dividends and bonuses will affect the banks which have insufficient capital compared to the capital required by the buffer. The new regulation also introduces a countercyclical buffer which will depend on a macroeconomic variable.

3.1.2. Leverage ratio

The leverage ratio shall enter into force as a Pillar I measure in 2018 after a monitoring period carried out by the competent authorities which will begin in 2011 and a parallel calculation period between 2013 and 2017. Basel III also sets out the publication of the leverage ratio by the banks as from 2015.

The reasons for the introduction of the leverage ratio are as follows:

- to prevent an excessive leverage of the banking sector during an important economic and financial growth in order to limit negative impacts of the de-leveraging process during financial difficulties;
- to put in place safeguarding measures against model risk and measurement errors in general.

The numerator of the leverage ratio is composed of tier 1 capital. The denominator includes balance sheet and off-balance sheet items. During the monitoring period, the CSSF will pay particular attention to the impact of the leverage ratio on some business models present in the Luxembourg financial centre.

3.1.3. Liquidity ratios

For the first time, the Basel Committee will set up explicit quantitative requirements in relation to liquidity by introducing two liquidity ratios, namely the Liquidity Coverage Ratio (LCR) and the Net Stable Funding Ratio (NSFR). The LCR is a short-term ratio the goal of which is to guarantee that a bank has sufficient liquid assets to cope with liquidity deficiencies during stress. The NSFR is a long-term ratio the goal of which is to limit an excessive dependency on short-term inter-bank (market) financing by determining an acceptable minimum amount of stable financing.

According to the first CSSF estimates, an application of these new liquidity standards to all credit institutions, on a consolidated and individual basis, will have a significant impact on the Luxembourg banking sector. In case of application on an individual basis, the banks, whichever their size, will have to maintain adequate liquidity reserves and may not rely on a liquidity supply from their parent company any more.

It should be noted that the impacts of these two liquidity ratios will nevertheless be reduced by the extension of their introductory dates. The implementation of the LCR is set for 1 January 2015 and that of the NSFR for 1 January 2018.

The CSSF agents contributed to the work of the Basel Committee and of several sub-committees and sub-working groups, among which the Standards Implementation Group, the Accounting Task Force, the Risk Management and Modelling Group, the Working Group on Liquidity, the Definition of Capital Group, the Capital Monitoring Group, the Quantitative Impact Study Group and the Corporate Governance Task Force.

The works of these groups mainly consisted in the elaboration of the above-mentioned Basel III documents. In this context, impact studies were carried out by the Capital Monitoring Group and the Quantitative Impact Study Group on the impact of Basel II regulation on the different components of prudential ratios and the possible side-effects of the introduction of the new Basel III standards. A Luxembourg bank was involved in these studies.

All the publications by the Basel Committee and information on its organisational structure are available on the website www.bis.org.

3.2. International Organisation of Securities Commissions (IOSCO)

3.2.1. 35th IOSCO Annual Conference

The securities and futures regulators, among which the CSSF, and other members of the international financial community met in Montreal from 6 to 10 June 2010, on the occasion of the 35th Annual Conference of IOSCO. On this occasion, IOSCO decided to organise its 38th Annual Conference in Luxembourg.

IOSCO has reformulated its strategic missions and goals for the next five years, in order to take into account IOSCO's increased role in: maintaining and improving the international regulatory framework for securities markets by setting international standards; identifying and addressing systemic risks; advancing implementation of the IOSCO Objectives and Principles of Securities Regulation; and pursuing full implementation of the IOSCO's Multilateral Memorandum on cooperation[3].

During the last months, IOSCO covered, among others, the following subjects:

- IOSCO Objectives and Principles of Securities Regulation

  During the 35th Annual Conference, the Presidents' Committee has approved the revised IOSCO Objectives and Principles of Securities Regulation, which include eight new principles as well as a number of revisions to existing principles. The new IOSCO principles increased focus on systemic risk in securities markets. Additionally, the new principles address credit rating agencies, hedge funds and auditor oversight and independence. The new principles address as well conflicts of interest, also related to securitised products.

[3] Multilateral Memorandum of Understanding (MMoU) Concerning Consultation and Cooperation and the Exchange of Information.

- IOSCO Multilateral Memorandum on cooperation

  The list of signatories of IOSCO's Multilateral Memorandum on cooperation is available on IOSCO's website (www.iosco.org). IOSCO's target is that all ordinary members and associate members, with primary responsibility for securities regulation in their jurisdiction, become full signatories of the memorandum by 1 January 2013.

- Systemic risk

  IOSCO's Technical Committee set up a working group which will study the role of the securities regulators with respect to systemic risk.

3.2.2. IOSCO groups

The CSSF is a member of the Standing Committees SC1 (dealing with subjects related to accounting) and SC5 (regarding UCIs and collective management).

3.3. Extended Contact Group "Undertakings for Collective Investment"

The CSSF attended the annual meeting of the Extended Contact Group "Undertakings for Collective Investment" that was held from 6 to 8 October 2010 in Saint Helier, Jersey. The following matters were discussed: questions relating to supervision, conflicts of interest/code of conduct, legal topics, financial issues, reporting and disclosure, management and administration of investment funds, UCITS and other investment funds.

3.4. Others

In addition to the above-mentioned committees and groups, the CSSF agents also participated in the works of the *Institut francophone de la régulation financière* (IFREFI) and the International Forum of Independent Audit Regulators (IFIAR) in 2010.

Furthermore, in the context of the fight against money laundering and terrorist financing, the CSSF contributed, in 2010, to the works of the Financial Action Task Force (FATF) and its subgroups, of the Basel Committee's AML/CFT Expert Group, of the Wolfsberg Group and of the UN Counter-Terrorism Committee (cf. Chapter XIII "Fight against money laundering and terrorist financing").

Agents hired in 2010 and 2011 - Department "General supervision"
Left to right: Sonja KINN, Guido KRUSE, Sophie SCHILTZ, Charles KRIER, Carole PHILIPPE, Françoise BERGMANS, Nicolas VAN LAAR, Annick BOVÉ

Absent: Magali DE DIJCKER

SUPERVISION OF THE BANKING SECTOR

02

1. Developments in the banking sector in 2010
2. Prudential supervisory practice

1. DEVELOPMENTS IN THE BANKING SECTOR IN 2010

1.1. Major events in 2010

1.1.1. The various risks in the Luxembourg banking sector

Even though the Luxembourg banking sector globally shows a good resilience, some risk concentrations need careful management and follow-up. The nature and the level of these risks may substantially vary between banks and according to the exercised activities. They include sovereign risks, risks linked to the financing of residential real estate in Luxembourg, intra-group risks and risks related to the activities of depositary banks.

- **Sovereign risks**

Sovereign risks are credit exposures to the public sector which include central, regional and local administrations. These exposures represent about 8% of the aggregated assets of banks of the financial centre. They mainly consist of loans granted to eurozone Member States, the United States, Canada and Switzerland.

In the wake of the financial crisis, the deterioration of public finances resulted in a downgrading of the credit quality of the public sector in general. Insofar as this deterioration may, in extreme cases, jeopardise a State's solvency, the lending banks are subject to the risk that the loans granted to these States may not be fully repaid resulting in the need of value adjustments.

The CSSF continues to carefully monitor sovereign risk exposures of Luxembourg banks and if necessary, intervenes at the banks in order to keep the concentration risk on the public sector within acceptable limits. In this context, the CSSF draws attention to the acceptable balance that banks must keep between their own funds and their exposure to the most vulnerable countries. When the loan is to be granted, the banks must ensure that they possess a sound recognition of the sovereign risk involved. They cannot merely rely on the existence of support measures or conditional guarantees in favour of debtors, as is the case of the European mechanism for financial stabilisation.

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

The local market of residential real estate mortgage financing is assured only by a limited number of the financial centre's banks. Insofar as these loans represent a significant concentration on this sector, they require a sound granting practice and follow-up policy by the banks. In the interest of the banks, as well as of the borrowers, a sensible business policy should be implemented by the banks in order to ensure that the risks involved can be assumed.

The exposure of Luxembourg banks to the domestic real estate sector includes two aspects: the financing of residential real estate and the financing of property development.

When financing residential real estate mortgages, the banks need to make sure that the borrower will still be in a position to service his debt, even if adverse economic conditions or social developments should occur which might reduce the latter's available income, for instance in case of an increase of interest costs. Under a sound loan granting policy, no loan should exceed 85% of the value of the mortgaged object.

As regards property development, it is particularly important that the risk be, ultimately and for the most part, not assumed by the banks. It presupposes that the banks receive solid guarantees (pre-sale or pre-lease levels covering the finishing costs of the shell, personal guarantees easily realisable), and that they require an adequate personal contribution of the developer and set a timely deadline in the near future for the start of the building phase. After this deadline has elapsed, banks must make provision for all unpaid accrued interest. Under no circumstances can unpaid accrued interest be capitalised or settled by a loan extension.

The determination of the capital requirements regarding mortgage loans, as set out in Circular CSSF 06/273, follows the logic of adequate exposure diversification. This logic not being observed for mortgage loan

portfolios concentrated in Luxembourg, the CSSF decided in 2009 to adapt these requirements accordingly. In 2010, the CSSF confirmed this policy of additional capital requirements for banks which hold substantial credit portfolios of the local real estate sector.

- **Risks linked to intra-group exposures**

As far as the Luxembourg banking sector is concerned, the service provision related to wealth management activities involves a large collection of deposits. In accordance with the logic of efficient work division, the Luxembourg banks receiving these deposits often transfer them to their respective parent company which reallocates the deposits within the entities of the group in charge of investment activities. The result is a concentrated exposure of Luxembourg banks to banking groups which have establishments specialised in wealth management in Luxembourg. Globally, assets of Luxembourg banks held by related parties represent about half of the aggregated assets of the Luxembourg banking sector.

While the CSSF does not practise general ring fencing for banks established in Luxembourg, the management of local banks is nevertheless responsible for the safeguard of the interests of the Luxembourg bank's business activity by practising a sound liquidity risk management according to the guidelines set out in sub-chapter II.4 of Circular CSSF 09/403 on sound liquidity risk management. It should be borne in mind, in this context, that the CSSF continues its general policy of intervening at the banks which carry out a risky business of maturity transformation which occurs when short-term customer deposits are invested as long-term loans, or when used to finance peripheral group entities in which the Luxembourg banks have no direct interest.

- **Risks related to the activity of depositary bank**

The activity of depositary bank carried out by Luxembourg banks in the framework of their services related to wealth management concerns global assets amounting to around EUR 2,600 billion. By adding the assets deposited during payment and securities settlement transactions to the previous figure, the total amounts to EUR 10,600 billion.

As regards the rules governing the holding of financial assets for the account of third parties, the Luxembourg banks are subject in particular to the provisions of Article 37-1(7) of the law of 5 April 1993 on the financial sector: the Luxembourg credit institutions "shall make appropriate arrangements so as to safeguard clients' ownership rights, especially in the event of insolvency of the credit institution". These requirements which are also applied in case of delegation of tasks, where the bank uses sub-depositaries, are specified in Section 3 of Chapter II of Grand-ducal regulation of 13 July 2007 relating to organisational requirements and rules of conduct in the financial sector.

In view of the high amount of values deposited with the Luxembourg banks, an interruption of the service provision by the depositary bank may jeopardise the orderly functioning of the global financial markets. In order to reduce this impact, the Luxembourg banks are requested to take into account the above requirements for their business continuity policy as set out in Article 5(3) of the above-mentioned Grand-ducal regulation.

1.1.2. New regulation concerning large exposures

Among the new provisions introduced by Directive 2009/111/EC (CRD II), the rules on the monitoring of large exposures are those which have the greatest impact on the banks' day-to-day business.

In particular, the repeal of the exemption for interbank exposures with initial maturity of less than a year could have triggered a great number of excesses on the date of implementation of the directive, i.e. on 31 December 2010. Aware of the impact of these changes on the business model of many banks, the CSSF drew the attention of credit institutions to the new rules by issuing Circular CSSF 10/450 of 16 April 2010. All the provisions relating to own funds of Directive 2009/111/EC have been transposed by Circular CSSF 10/475 of 20 July 2010.

Henceforth, the risk taken by credit institutions on other banks or other investment firms are limited to 25% of the own funds. This absolute limit does not take into account the risk weight or degrees of risk related to the quality of the counterparty and should limit the contagion in the banking system in case of failure of a counterparty.

However, there are four exceptions to the new provisions:

1. Very short-term exposures related to money transfer including the execution of payment services, clearing, settlement and custody services for clients are exempt in order to facilitate the smooth functioning of financial markets and of the related infrastructure.
2. For small institutions, i.e. those whose own funds are less than EUR 600 million, the maximum limit is raised to 100% of their own funds or EUR 150 million, whichever the smaller.
3. Overnight deposits in currencies other than major exchange currencies are exempted, provided that they do not represent the own funds of the counterparty.
4. National authorities may exempt the exposure on entities of the group to which the credit institution belongs if these entities are included in the consolidated supervision pursuant to EU or equivalent rules. Since being part of a banking group is an essential feature of the business model of many banks active in the financial centre, the CSSF continues to use this national discretion.

   However, some risks may ensue from the use of this exemption, such as the failure of the Luxembourg subsidiary in case of bankruptcy of the parent company, with, as possible consequences, the failure to repay the creditors of the Luxembourg subsidiary and the intervention of the Luxembourg deposit-guarantee scheme. During the transposition of CRD II, the CSSF discussed the maintenance of this exemption at the meeting of the ad hoc CRD II Committee. The representatives of the industry did not object to its maintenance.

1.1.3. Supervision of the new provisions regarding securitisation

Since the entry into force, on 1 January 2011, of Circular CSSF 10/475 which transposed CRD II and amended Circular CSSF 06/273, credit institutions must observe new provisions regarding securitisation:

i. details on the concept of "transfer of a significant part of credit risk", limited to credit institutions acting as originators;

ii. rules relating to the "retention of net economic interest", some requirements of which refer to credit institutions acting as originators, investors or sponsors.

These provisions apply to all new securitisations issued as from 1 January 2011 and, as regards the application of the retention rule, to all securitisations existing after 31 December 2014 if the underlying exposures are replaced or completed by new exposures after this date.

Credit institutions acting as originators must make a preliminary application for the intended exclusion of the securitised exposures from the capital requirements calculations. Among others, this application must supply proof of:

i. compliance with the requirements regarding the "transfer of a significant part of credit risk"; and

ii. compliance with the requirements relating to the rule of retention by referring also to CEBS guidelines in this matter[1].

Credit institutions that wish to invest in new securitisation issues must comply with the above-mentioned CEBS guidelines and communicate to the CSSF the relevant data which allow the verification that the circular's provisions are observed.

1.1.4. Consequences of the financial crisis

By order of 7 February 2011, the District Court of Luxembourg sitting in commercial matters has declared that a dividend of 100% may be paid to unsecured creditors whose claims have been admitted to the liabilities of

[1] The guidelines CEBS GL40, Guidelines on the Application of Article 122a of the Capital Requirements Directive.

the judicial liquidation of Landsbanki Luxembourg S.A.. The depositors of Landsbanki Luxembourg S.A. were, thus, able to get back 100% of their deposits.

Following the solution found in the case of Landsbanki Luxembourg S.A., the depositors of the three banks subject to the suspension of payments since October 2008, namely Kaupthing Bank Luxembourg S.A., Glitnir Bank Luxembourg S.A. and Landsbanki Luxembourg S.A., have been repaid in full.

1.1.5. Supranational supervision in relation to financial stability

Article 3-1 of the law of 23 December 1998 establishing a financial sector supervisory commission (*Commission de surveillance du secteur financier*) provides that the CSSF shall contribute to ensure financial stability at national, Community and international level. This financial stability is particularly assessed in the light of the stress tests which evaluate the degree of the banks' resilience against particularly unfavourable developments (stress).

The CSSF's contribution to the assessment and to the safekeeping of the financial stability in the Luxembourg financial sector is increasingly subject to supranational supervision aiming at ensuring the quality of the procedures applied by the CSSF. In 2010, the CSSF contributed twice, namely for the bank stress tests made at European level by the Committee of European Banking Supervisors (CEBS) and for the financial sector assessment program of the International Monetary Fund (IMF).

- **Macroeconomic stress test carried out for CEBS**

Under the mandate from the European Council of Ministers of Finance (ECOFIN), CEBS published the results of the macroeconomic stress test of the European banking sector in July 2010. This test, carried out in cooperation with the European Central Bank (ECB) and the European Commission, assessed the ability of the European banks to face a new economic deterioration which is synonymous with impaired credits. The publication of individual results per bank aimed at providing the financial markets with further transparency as regards the future solvency of the European banks, in particular in view of the issues raised during the adverse evolution of the European public finances.

In terms of coverage, the Luxembourg banking sector was largely represented in this exercise by its local and its cross-border activities. The CEBS sample which included the main European parent companies of Luxembourg banks, based on their consolidated situation comprising Luxembourg subsidiaries and branches, covered over 70% of the aggregated balance sheet total of the Luxembourg banking sector. The participation of Banque et Caisse d'Épargne de l'État (BCEE) and of Banque Raiffeisen ensured, moreover, an almost total coverage of the banks active on the national credit market.

The stress tests were carried out based on the risk parameters (default and loss experience in case of failure) jointly determined by CEBS and the ECB based on macroeconomic forecasts which set as benchmark scenario a slight economic recovery and as adverse scenario the worsening of the economic recession that the European economy suffered in 2008-2009. Thus, under the benchmark scenario, the GDP of the eurozone would increase by 0.7% in 2010 and by 1.5% in 2011. Under the adverse scenario, the GDP would decrease by 0.2% in 2010 and by 0.6% in 2011. In the adverse hypothesis, a deterioration of the public finances of Member States would be added which would result in the refinancing rate rising by 125 basis points for short-term interest rates and by 75 basis points for long-term interest rates, with increasing specific risk premiums reaching 70 basis points in average in the eurozone. In accordance with these hypotheses, the sovereign exposures assessed according to the market price (and held in the trading portfolio of the banks) would suffer a corresponding value decrease.

In Luxembourg, the CSSF carried out the calculation tests regarding BCEE and Banque Raiffeisen for CEBS. The results set out by the CSSF and confirmed by CEBS show that the two banks are resilient to these possible adverse shocks and stay well above the current 4% Tier 1 threshold (11.3% for BCEE and 8.2% for Banque Raiffeisen). All in all, the European banking groups BNP Paribas, Dexia, ING, BPCE and Caixa Geral De Depósitos, which are among the 91 EU banks included on a consolidated basis in the sample and have

Luxembourg entities with significant market shares in the domestic credit market and deposit taking, are resilient to the adverse developments according to the results of the CEBS stress test. The Luxembourg entities of these banking groups are BGL BNP Paribas, Dexia Banque Internationale à Luxembourg, ING LUXEMBOURG S.A., Banque BCP S.A. and Caixa Geral de Depósitos SA, Lisboa (Portugal), Luxembourg branch.

On 1 January 2011, the European system of financial supervisors was created. As a result, the tasks and responsibilities previously assumed by CEBS were transferred to the European Banking Authority (EBA) created by Regulation (EU) No 1093/2010 of 24 November 2010. The revision of the mandate of the European stress tests by EBA resulted, in January 2011, in keeping BCEE as the only domestic Luxembourg bank in the stress test programme of EBA, the whole sample, thus, observing the representation criteria defined by EBA on European and national level.

- **Financial Sector Assessment Program by the IMF**

Against a background of financial and economic crisis, the leaders of the G20, established in 1999 following the Asian crisis, firmly committed, in November 2008, to closely cooperate in order to promote a growth in the world economy which will be strong, lasting and balanced at the same time. The reforms particularly concentrate on the international financial system in order to make it more resilient and to subject the system to an efficient supranational supervision, a task assigned to the IMF by the G20. In September 2010, the IMF Executive Board announced that its reviewed "Financial Sector Assessment Program" (FSAP) will be mandatory for 25 countries considered as systemic due to their important financial sector[2]. Luxembourg, which is part of these countries, shall, thus, be subject to a FSAP inspection at least every five years.

In November 2010, the IMF performed in Luxembourg a first FSAP inspection following the new methodology. On this occasion, the CSSF provided the results of various stress tests based on scenarios drawn up by the IMF. These scenarios comprised the simulation of the impact of adverse macroeconomic developments on the solvency and liquidity of Luxembourg banks, including the simulation of cross-border contagion effects. The final results of the FSAP will only be published by mid 2011, by which date the final report should be adopted by the IMF.

Analysis of the effects of adverse macroeconomic scenarios on the solvency of Luxembourg banks

With respect to the assessment of the resilience of the Luxembourg banking sector against adverse macroeconomic developments, the IMF considered a deviation of 3% of the eurozone growth rate (adverse scenario) compared to the growth forecast by IMF analysts (benchmark scenario). While the benchmark scenario anticipated a cumulated progress of 3.4% of the GDP in the eurozone over two years, the adverse scenario expected an annual growth which would slow down at 0.8% in the first year and which would become negative (-0.4%) in the following year. As regards interest rates of the eurozone, the adverse scenario contemplated a progress of 140 basis points on the short part and of 160 basis points on the long part of the rate curve. These hypotheses were converted in risk parameters by the CSSF (default and loss experience in case of failure) according to a methodology jointly adopted by CEBS and the ECB for CEBS' macroeconomic stress test of 2010. These parameters were used afterwards to quantify the impact of the adverse scenario on the solvency of the Luxembourg banks, pursuant to the Basel II framework (Circular CSSF 07/273).

Moreover, contrary to the hypotheses chosen in the CEBS stress test, the IMF expressly requested that the sovereign exposures, no matter the accounting treatment, be subject to a hypothetical reassessment according to discounts which reflect the significant deterioration of the public finances mainly in Europe. Pursuant to the adverse scenario chosen by the IMF, these discounts were set in a range of 4% to 30%, corresponding to an extension of the spread of between 90 and 760 basis points, depending on the counterparty.

The results established by the CSSF and discussed with the IMF confirm the solid resilience of the Luxembourg banking sector regarding the largely adverse macroeconomic developments. Under the adverse hypotheses adopted by the IMF, the cumulated losses would reach EUR 12 billion, of which EUR 7 billion would result from sovereign exposures. Consequently, the aggregated solvency ratio would decrease by 270 basis points to 16.7%. This level is comfortably above the legal minimum of 8%. Among all the Luxembourg banks, only four would suffer a reduced solvency in this extremely adverse scenario.

[2] IMF press release No 10/357 of 27 September 2010. Until that date, the FSAP, set up in 1999, was carried out on a voluntary basis. Luxembourg, which was assessed in 2001, was informed by the IMF that its "financial sector is robust, efficient and well supervised".

Analysis of contagion effects resulting from hypothetical shock scenarios on solvency and/or liquidity of Luxembourg banks

In accordance with the methodology set out in IMF Working Paper 10/105[3], the CSSF performed two sets of stress tests for the IMF. The aim of these stress tests was to analyse and quantify the presence of contagion effects within the Luxembourg banking sector. Insofar as this analysis needed the manual collection and treatment of all registered asset and liability counterparties of the banks, the exercise was performed based on a reduced number of banks. The latter were selected according to size, as well as interbank and intra-group relations. In the end, the sample included twenty Luxembourg banks of systemic importance which have material commercial relations with 3,000 different asset and liability counterparty groups.

The risk parameters of the analysis were defined by the IMF based on a severe deterioration scenario of the credit quality of a central administration of the eurozone the effects of which affected the entire counterparties located in the home country of this central administration and, *via* inducement, the counterparties of other countries according to the relations of these counterparties with the affected country. This scenario particularly influenced the level of the rate of deposit withdrawals of different liability counterparties of Luxembourg banks as well as the discounts applied to liquid assets held by the Luxembourg banks and recorded on the asset's side of the balance sheet.

A first range of stress tests consisted in simulating the sequential failure of each of the 3,000 counterparties. The failure of a counterparty results in a provisioning of loans granted by the banks to this counterparty (deterioration of the solvency), in a decrease of the liquidity reserves up to the amount of the liquid assets issued by this counterparty (deterioration of the liquidity) and in the necessity to provide for the replacement of the amounts deposited by this counterparty, whether through liquid assets subject to repurchase agreements or through the forced sale of assets according to the risk parameters determined by the IMF (deterioration of the liquidity and solvency). When, after the failure of a counterparty, the deterioration of the liquidity or the solvency of one or several of the twenty sample banks leads to an insolvency report or liquidity deficit of these banks, these "failures" are themselves reflected in the situation of the banks which remained liquid and solvent. These consequences allow simulating and estimating the contagion effects which possibly exist in the Luxembourg banking sector.

The results of this first range of tests confirm the good resilience of the Luxembourg banks against external shocks and the absence of contagion effects leading to subsequent failures. It should be borne in mind that, in accordance with the expectations, the failure of the parent company of one of the banks from the sample generally results in the failure of the Luxembourg subsidiary.

In the second range of stress tests, the different counterparties, faced with a general liquidity crisis, simultaneously and massively withdraw their deposits. The simulations in this range vary according to the applied withdrawal scenarios, from the simple scenario with a regular withdrawal rate (including intensity of withdrawal rate from 5% to 15%) to more complex models which link the withdrawal rate to the vulnerability of the counterparty and of the bank which holds the deposits.

The results of these stress tests carried out according to the second range show, in the more adverse simulations, the possible vulnerabilities as regards the liquidity of five systemic banks of the financial centre. As expected, these vulnerabilities generally stem from intra-group relations. It should be pointed out that the chosen calculation methodology did not take into account the implementation of corrective measures pursuant to which the Luxembourg banks, when facing massive intra-group withdrawals, consequently decrease their own exposures to their group, in accordance with the operational modalities for the liquidity management of these groups and with the CSSF expectations as set out in Circular CSSF 09/403 regarding the sound liquidity risk management. Like the stress tests of the first range, the results of the second range did not reveal contagion effects in the Luxembourg banking sector.

[3] M.A. Espinosa-Vega and J. Solé (2010), Cross-border Financial Surveillance: A Network Perspective, IMF Working Paper 10/105.

1.2. Characteristics of the Luxembourg banking sector

The Luxembourg banking legislation provides for three types of banking licences, defined by the nature of their activity, namely: universal banks (141 institutions had this status on 31 December 2010), banks which issue mortgage bonds (five institutions had this status on 31 December 2010) and banks which issue electronic means of payment (one institution had this status on 31 December 2010).

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

- banks incorporated under Luxembourg law (109 on 31 December 2010);
- branches of banks incorporated in an EU Member State or assimilated (31 on 31 December 2010);
- branches of banks incorporated in a non-EU Member State (7 on 31 December 2010).

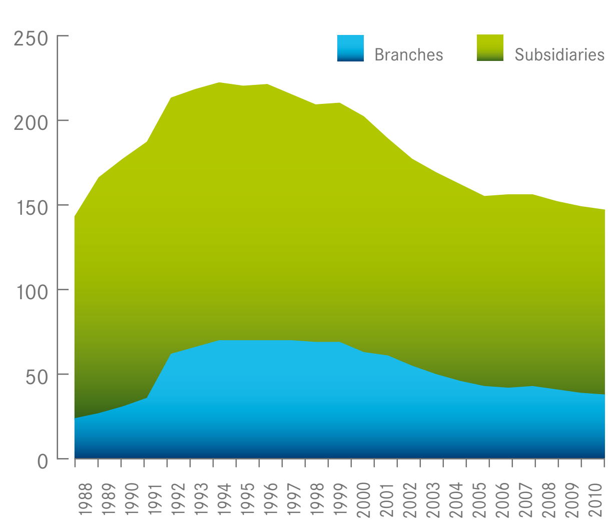
Furthermore, there is one special case: the *caisses rurales* (13 on 31 December 2010) and their central establishment, Banque Raiffeisen, are to be considered as a single entity, according to the law on the financial sector.

1.3. Development in the number of credit institutions

With 147 entities authorised at the end of the financial year 2010, the number of banks decreased by two entities as compared to 31 December 2009 (149). Among those 147 entities, 109 are banks incorporated under Luxembourg law (110 in 2009) and 38 are branches (39 in 2009).

Development in the number of banks established in Luxembourg

Year	Branches	Subsidiaries	Total
1988	24	119	143
1989	27	139	166
1990	31	146	177
1991	36	151	187
1992	62	151	213
1993	66	152	218
1994	70	152	222
1995	70	150	220
1996	70	151	221
1997	70	145	215
1998	69	140	209
1999	69	141	210
2000	63	139	202
2001	61	128	189
2002	55	122	177
2003	50	119	169
2004	46	116	162
2005	43	112	155
2006	42	114	156
2007	43	113	156
2008	41	111	152
2009	39	110	149
2010	38	109	147



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

• Dresdner Bank Luxembourg S.A.	Merger with Commerzbank International S.A. on 1 April 2010
• Sanpaolo Bank S.A.	Merger with State Street Luxembourg S.A. on 18 May 2010
• Sella Bank Luxembourg S.A.	Abandoned the status of bank following the split-up of the company on 30 June 2010
• NATIXIS Luxembourg S.A.	Transfer of its activity to Natixis Bank on 30 September 2010
• BNP Paribas Luxembourg	Merger with BGL BNP Paribas on 1 October 2010
• Banco di Brescia S.p.A. , succursale de Luxembourg	Ceased its activity on 9 December 2010

Four new banks started their activities in 2010:

• Keytrade Bank Luxembourg S.A.	6 January 2010
• AndBanc Luxembourg S.A.	14 April 2010
• Banque BPP S.A.	1 July 2010
• Amazon Payments Europe S.C.A.	24 September 2010

Keytrade Bank Luxembourg S.A., which is active in online brokerage, is the result of the transformation of the PFS Keytrade Luxembourg S.A. into a credit institution.

AndBanc Luxembourg S.A. is a subsidiary of the Andorran bank Andorra Banc Agricol Reig and is mainly active in private banking. Its creation is part of the international expansion of the group.

Banque BPP S.A. is the result of the split-up of the banking activities of the former Sella Bank Luxembourg S.A..

Amazon Payments Europe S.C.A. is a subsidiary of the Amazon group; it is the first company to receive the status of electronic money institution in Luxembourg.

The following eight credit institutions changed their names in 2010:

Former denomination	New denomination (date of change)
CALYON, succursale de Luxembourg	Crédit Agricole Corporate and Investment Bank Luxembourg Branch (6 February 2010)
Sal. Oppenheim jr. & Cie, succursale de Luxembourg	Sal. Oppenheim jr. & Cie. AG & Co. KGaA, succursale de Luxembourg (16 June 2010)
DZ Bank International S.A.	DZ PRIVATBANK S.A. (1 July 2010)
Fortis Prime Fund Solutions Bank (Ireland) Ltd., Luxembourg branch	ABN AMRO Bank (Ireland) Ltd, Luxembourg Branch (5 July 2010)
PNC International Bank Limited, Luxembourg Branch	BNY Mellon International Bank Limited, Luxembourg Branch (28 July 2010)
Natixis Private Banking International	Natixis Bank (30 September 2010)
Banco Bradesco Luxembourg S.A.	BANCO BRADESCO EUROPA S.A. (4 October 2010)
Nord Europe Private Bank	UFG-LFP Private Bank (20 October 2010)

Geographical origin of banks

Country	Number
Germany	44
France	13
Switzerland	11
Belgium	10
Italy	9
Untited Kingdom	8
Sweden	7
United States	7
Japan	5
Luxembourg	5
China	4
Netherlands	4
Israel	3
Brazil	2
Denmark	2
Ireland	2
Norway	2
Portugal	2
Andorra	1
Belgium / Canada	1
Canada	1
Greece	1
Liechtenstein	1
Russia	1
Turkey	1
Total	**147**

1.4. Development in banking employment

After five consecutive years on the up, employment in the Luxembourg banking sector has suffered a decrease since the last quarter of 2008. In the context of the financial crisis, employment shrank by 785 units (-2.9%) in 2009. In 2010, this downward trend continued at a more moderate rate (-0.6% or -166 units). As at 31 December 2010, the Luxembourg credit institutions employed 26,254 people.

In non-aggregated terms, employment in banks is disparate. Thus, 59.8% of credit institutions registered on the official list as at 31 December 2010 maintained or even increased their staff over a year. Even though this percentage is rather steady compared to 2009 where it reached 61.1%, it is worse than during the pre-crisis period when it exceeded 70%. Compared to 2009 when new employment only reached 461 units, the banks created 1,675 new employments in 2010. However, this increase is not sufficient to compensate the 1,841 job losses registered in 2010. Consequently, employment in the banking sector fell by 166 units in 2010.

Economic restructurings and cost cuts due to the financial crisis are responsible for the decrease in employment. Banks that are hiring benefit from the current market situation which allows them to fulfil their internal needs in human resources that were difficult to supplement in the preceding months.

The breakdown of aggregated employment shows that the female employment rate slightly rose from 45.4% to 46.4%. The share of executives in total employment remained almost unchanged at 26.4% (26.5% in 2009).

Situation of employment in credit institutions

	Total		Management			Office staff			Technical staff			Total staff		
	Luxbg.	Foreigners	Men	Women	Total	Men	Women	Total	Men	Women	Total	Men	Women	Total
1996	8,113	10,469	2,658	490	3,148	7,476	7,809	15,285	48	101	149	10,182	8,400	18,582
1997	8,003	11,086	2,765	547	3,312	7,631	8,013	15,644	44	89	133	10,440	8,649	19,089
1998	7,829	12,005	2,900	577	3,477	7,846	8,377	16,223	47	87	134	10,793	9,041	19,834
1999	7,797	13,400	3,119	670	3,789	8,362	8,961	17,323	34	51	85	11,515	9,682	21,197
2000	7,836	15,232	3,371	783	4,154	9,030	9,801	18,831	35	48	83	12,436	10,632	23,068
2001	7,713	16,148	3,581	917	4,498	9,222	10,046	19,268	33	62	95	12,836	11,025	23,861
2002	7,402	15,898	3,654	977	4,631	8,941	9,657	18,598	25	46	71	12,620	10,680	23,300
2003	7,117	15,412	3,720	1,049	4,769	8,486	9,211	17,691	23	40	63	12,229	10,300	22,529
2004	7,001	15,553	3,801	1,111	4,912	8,451	9,138	17,589	19	34	53	12,271	10,283	22,554
2005	6,822	16,405	3,948	1,183	5,131	8,641	9,397	18,038	20	38	58	12,609	10,618	23,227
2006	6,840	17,912	4,280	1,294	5,574	9,153	9,974	19,127	19	32	51	13,452	11,300	24,752
2007	6,962	19,177	4,669	1,475	6,144	9,525	10,407	19,932	32	31	63	14,226	11,913	26,139
2008	6,898	20,307	5,101	1,672	6,773	9,658	10,729	20,387	15	30	45	14,774	12,431	27,205
2009	6,599	19,821	5,221	1,781	7,002	9,184	10,199	19,383	15	20	35	14,420	12,000	26,420
2010	6,623	19,631	5,048	1,875	6,923	9,019	10,282	19,301	14	16	30	14,081	12,173	26,254

Breakdown of the number of employees per bank

	Number of banks						
Number of employees	**2004**	**2005**	**2006**	**2007**	**2008**	**2009**	**2010**
> 1,000	4	4	5	5	5	5	6
500 to 1,000	2	6	7	9	8	9	8
400 to 500	6	4	3	2	4	3	1
300 to 400	8	7	8	10	11	9	9
200 to 300	8	7	10	9	8	8	7
100 to 200	19	20	18	18	16	18	16
50 to 100	21	18	18	21	20	20	21
< 50	94	89	87	82	80	77	79
Total	**162**	**155**	**156**	**156**	**152**	**149**	**147**

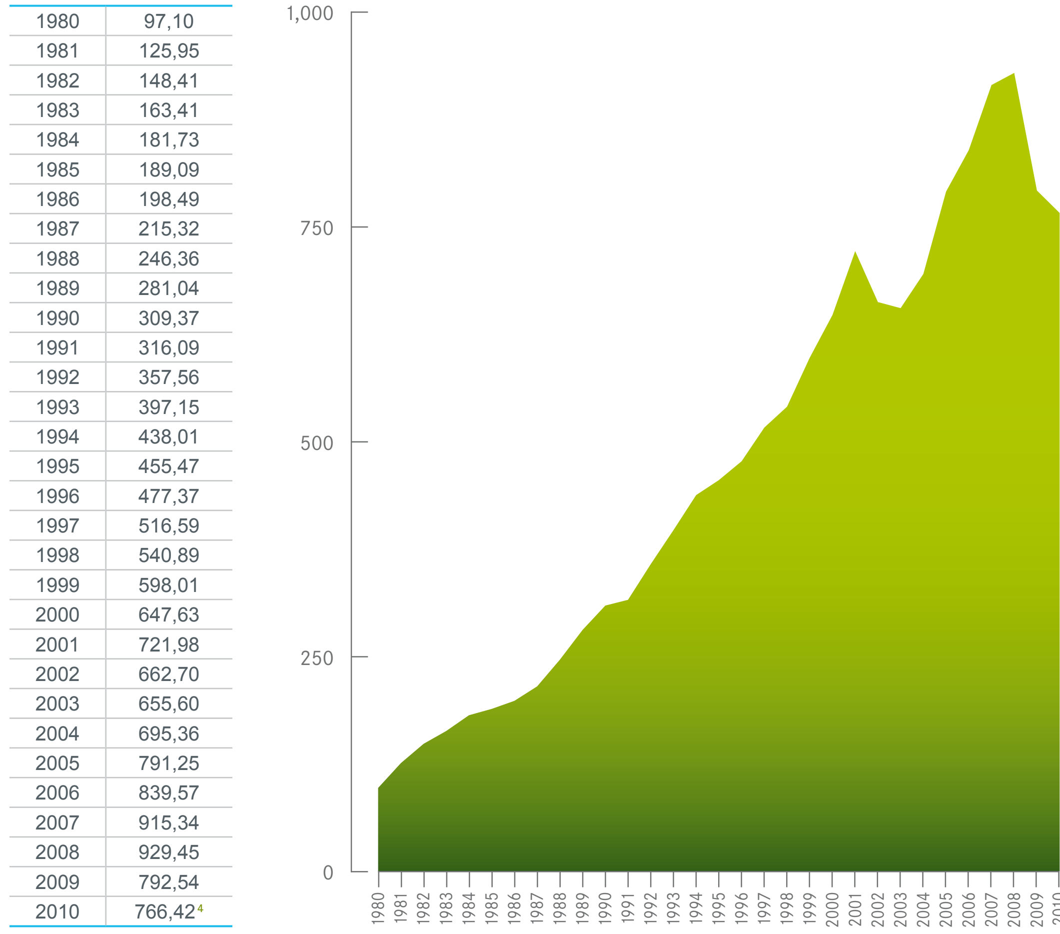
1.5. Development of balance sheet and off-balance sheet accounts

1.5.1. Balance sheet total of credit institutions

As at 31 December 2010, the balance sheet total of credit institutions amounted to EUR 766.4 billion against EUR 792.5 billion as at 31 December 2009. Between October 2008 when the aggregated balance sheet total exceeded EUR 1,000 billion and December 2010, the intermediation activity of the Luxembourg banks dropped by almost a quarter. It should be pointed out that the rate of decrease of the balance sheet total slowed down on an annual basis: -3.4% in 2010 against -14.7% in 2009.

The development of the balance sheet total of Luxembourg banks shows two contrasting trends in 2010. During the first half of 2010, the balance sheet total registered a slight increase (+2.7%), whereas, during the second half, the intermediation activity declined, in particular in the context of the uncertainties triggered by the adverse developments of the European public finances.

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



1980	97,10
1981	125,95
1982	148,41
1983	163,41
1984	181,73
1985	189,09
1986	198,49
1987	215,32
1988	246,36
1989	281,04
1990	309,37
1991	316,09
1992	357,56
1993	397,15
1994	438,01
1995	455,47
1996	477,37
1997	516,59
1998	540,89
1999	598,01
2000	647,63
2001	721,98
2002	662,70
2003	655,60
2004	695,36
2005	791,25
2006	839,57
2007	915,34
2008	929,45
2009	792,54
2010	766,42[4]

[4] Preliminary figure

During the post-crisis period, the annual decrease of the balance sheet total, which reached EUR 26.9 billion in 2010, is synonymous with activity cessation and a significant reduction of risks for the banking groups greatly affected by the crisis. This phenomenon, which affects only a few banks of the financial centre, is the result either of a restructuring imposed by the European Commission or of a reassessment of the business model due, in particular, to the refinancing difficulties in the market. The consequent consolidation is partially carried out in favour of banking groups which were more resilient to the economic and financial crisis. In the context of the supportive financial markets, it is also worth mentioning the positive development of wealth management and services provided to investment funds even if the latter are only partially reflected in the balance sheets.

The development of the aggregated balance sheet hides important differences between banks of the financial centre. About 60% of the Luxembourg banks registered an increase of their activities over a year (+ EUR 81.6 billion). However, this increase is not sufficient to compensate for the drop in the balance sheets registered by other banks of the financial centre (- EUR 108.6 billion). 2010 may, nevertheless, indicate a change of trend with a majority of credit institutions registering an increase in their balance sheet.

1.5.2. Development of the structure of the aggregated balance sheet

The decrease of the balance sheets on the **asset** side is mainly caused by a reduction of exposures to credit institutions and companies, all loans and transferable securities taken together. On the contrary, loans to retail customers increased noticeably in 2010.

In the context of the consolidation of the banking activity, **loans and advances to credit institutions** fell by 2.1% over a year and reached EUR 347.6 billion at the end of December 2010. Given the stronger decline of the total balance sheet, loans and advances to credit institutions kept their prevailing weight in the structural balance sheet of the banking sector. At the end of 2010, they represented 45.4% of the total assets.

Fixed-income securities which represent over 90% of the total of transferable securities, dropped by 10.3% during 2010. This substantial drop shows the efforts to reduce risk made by some banking groups in Luxembourg. This drop is mainly registered for banking counterparties and companies. Consequently, the importance of the securities portfolio in the balance sheet assets declined and reached 22.5% at the end of 2010 (against 24.3% at the end of 2009). The sectoral composition of the securities portfolio continues to show mainly government (26%) and bank (44%) securities.

The volume of **loans and advances to customers** which include corporate and retail customers slightly improved and reached EUR 174.5 billion. Among these loans and advances, retail exposures which are mainly from Luxembourg, increased by 9% over a year, whereas the corporate loans and advances were slightly declining. They lost 2.8% and reached EUR 121.5 billion at the end of 2010. In the structural balance sheet, loans and advances to customers continued to grow and amounted to 22.8% of the balance sheet total.

It should also be pointed out that, towards the end of the crisis, the Luxembourg banks show greater preference for liquidity as is reflected in the substantial assets held with central banks. The amount of these assets represents the double of the pre-crisis amount.

Aggregated balance sheet total – in million EUR

ASSETS	2009	2010 (*)	Variation	LIABILITIES	2009	2010 (*)	Variation
Loans and advances to central banks and central governments	26,454	26,488	0.1%	Amounts owed to central banks	18,627	8,852	-51.8%
Loans and advances to credit institutions	355,187	347,635	-2.1%	Amounts owed to credit institutions	348,015	338,403	-2.8%
Loans and advances to customers	173,121	174,474	0.8%	Amounts owed to customers	254,493	255,639	0.4%
Financial assets held for trading	13,626	15,210	11.6%	Amounts owed represented by securities	81,141	71,842	-11.5%
Fixed-income securities	192,320	172,603	-10.3%	Liabilities (other than deposits) held for trading	13,839	15,584	12.6%
Variable-yield securities	16,218	15,193	-6.3%	Provisions	5,873	6,005	2.2%
Fixed assets and other assets	16,429	14,819	-9.8%	Subordinated debts	10,858	9,719	-10.5%
				Other liabilities	15,272	14,741	-3.5%
				Equities	44,679	45,638	2.1%
Total	**792,538**	**766,422**	**-3.3%**	**Total**	**792,538**	**766,422**	**-3.3%**

(*) Preliminary figures

The decrease of assets comes with a lower level of **refinancing needs** which, in 2010, are made of equal parts of amounts owed to central banks, amounts owed to credit institutions and amounts owed represented by securities.

The downward trend of the **amounts owed to central banks** reached 51.8% over a year. The refinancing that the Luxembourg banks ensure *via* funds made available by central banks thus reached a historically low level. These amounts owed represented just about 1.2% of the aggregated liabilities on 31 December 2010. The drop concerned at the same time the volume of the amounts owed to central banks and the number of banks which refinanced through central banks during the year.

The amounts **owed to credit institutions**, mainly in the form of intra-group transactions, registered a decline of 2.8%. They amounted to EUR 338.4 billion at the end of December 2010. Similarly to the loans and advances to credit institutions, the decline in the volume of the interbank amounts owed largely resulted from mergers and acquisitions in the Luxembourg banking sector. Moreover, the decrease of the interbank amounts owed is only observed at a small number of banks which are still concerned with a reduction of activities and risk. Despite the slight decline, the use of bank counterparties remained the main means of refinancing of the balance sheet activities of Luxembourg banks with 44.2% of the balance sheet total.

As regards the **amounts owed represented by securities**, the fall reached 11.5% over a year. It concerns most of the banks which use this form of refinancing. Compared to the balance sheet total, the debts represented by securities decreased in importance: they represent 9.4% of the aggregated liabilities with EUR 71.8 billion as at 31 December 2010.

The **amounts owed to customers** mainly consisting of corporate deposits, wealth management structures and retail customers, remained, with EUR 255.6 billion, almost unchanged over a year. As in the past, the volume of the amounts owed to customers played a prominent role among the refinancing means of the banking activities of the financial centre and allowed the Luxembourg banking sector to easily refinance its loans and advances to customers.

Equities only slightly increased under the effect of the hoarding transactions (2.1%). They amounted to EUR 45.6 billion in the aggregated liabilities of the financial centre's banks.

Structure of the balance sheet

ASSETS	2009	2010 (*)	LIABILITIES	2009	2010 (*)
Loans and advances to central banks and central governments	3.34%	3.46%	Amounts owed to central banks	2.32%	1.15%
Loans and advances to credit institutions	44.82%	45.36%	Amounts owed to credit institutions	43.91%	44.15%
Loans and advances to customers	21.84%	22.76%	Amounts owed to customers	32.11%	33.35%
Financial assets held for trading	1.72%	1.98%	Amounts owed represented by securities	10.24%	9.37%
Fixed-income securities	24.27%	22.52%	Liabilities (other than deposits) held for trading	1.75%	2.03%
Variable-yield securities	2.05%	1.98%	Provisions	0.74%	0.78%
Fixed assets and other assets	2.07%	1.93%	Subordinated debts	1.37%	1.27%
			Other liabilities	1.93%	1.92%
			Equities	5.64%	5.95%
Total	**100.00%**	**100.00%**	**Total**	**100.00%**	**100.00%**

(*) Preliminary figures

1.5.3. Use of derivative financial instruments by credit institutions

The banks of the financial centre used derivatives for a total nominal amount of EUR 721.7 billion in 2010 against EUR 681.0 billion in 2009. This improvement is due to the increased use of forward foreign exchange transactions by a limited number of banks in order to cover exchange risk. The net market value of the derivative financial instruments, included in the balance sheet items according to the IFRS standards, represents liabilities of EUR 4.7 billion as at 31 December 2010, a level similar to the one registered at the end of 2009.

Use of derivative financial instruments by credit institutions

Notional amounts *(in billion EUR)*	2009	2010 (*)	Variation		Structure	
			in volume	in %	2009	2010
Transactions related to interest rate	**305.4**	**245.7**	**-59.7**	**19.5%**	**45%**	**34%**
of which: options	8.4	5.5	-2.9	34.1%	3%	2%
of which: interest rate swaps	283.5	230.6	-52.9	18.7%	93%	94%
of which: future or forward rate agreements (FRA)	1.6	0.7	-0.9	55.0%	1%	0%
of which: interest rate futures	11.9	8.9	-3.0	25.4%	4%	4%
Transactions related to title deeds	**19.9**	**19.3**	**-0.6**	**-3.1%**	**3%**	**3%**
of which: futures	9.8	9.4	-0.4	-4.3%	49%	49%
of which: options	10.1	9.9	-0.2	-1.9%	51%	51%
Transactions related to exchange rates	**355.7**	**456.7**	**101.0**	**28.4%**	**52%**	**63%**
of which: forward foreign exchange transactions	289.4	382.6	93.2	32.2%	81%	84%
of which: cross-currency IRS	55.1	63.0	7.9	14.3%	15%	14%
of which: options	11.2	11.1	-0.1	-1.0%	3%	2%
Total	**681.0**	**721.7**	**40.7**	**6.0%**	**100%**	**100%**

(*) Preliminary figures

1.5.4. Off-balance sheet

As at 31 December 2010, the incidental exposure of the Luxembourg financial sector through loan commitments and financial guarantees given amounted to EUR 136.9 billion. This exposure increased by 9.1% compared to 31 December 2009 when it amounted to EUR 125.4 billion.

As regards assets deposited by customers, the assets deposited by UCIs and the assets deposited by other professionals acting on the financial markets improved by 20.2% and by 15.2% respectively compared to the end of 2009. Forming almost 85% of total third-party assets under management, the growth of these two items is largely influenced by the banks specialised in investment funds.

Assets deposited by customers as in the off-balance sheet

(in billion EUR)	2009	2010 (*)	Variation
Assets deposited by UCIs	1,875.2	2,253.9	20.2%
Assets deposited by clearing or settlement institutions	1,277.2	1,150.8	-9.9%
Assets deposited by other professionals acting in the financial markets	6,040.2	6,960.9	15.2%
Other deposited assets	294.3	282.6	-4.0%

(*) Preliminary figures

1.6. Development in the profit and loss account

The profit and loss account of the Luxembourg banking sector shows a net result of EUR 3,849 million as at 31 December 2010, i.e. an increase of EUR 1,793 million (+87.2%) compared to 2009.

In 2010, two trends characterise the profit and loss accounts of the Luxembourg banks: a sharp decline of the intermediation income, partially compensated by increased commissions received, and a substantial drop of the risk cost as shown by the decrease of net impairments.

Development in the profit and loss account – in million EUR

	2009	Relative share	2010 (*)	Relative share	Variation 2009/2010	
					in volume	in %
Interest-rate margin	6,571	62%	5,482	57%	-1,089	-16.6%
Net commissions received	3,132	30%	3,611	38%	480	15.3%
Other net income	850	8%	470	5%	-379	-44.6%
Banking income	**10,553**	**100%**	**9,564**	**100%**	**-989**	**-9.4%**
General expenses	-4,451	42%	-4,615	48%	-164	3.7%
of which: staff costs	*-2,449*	*23%*	*-2,500*	*26%*	*-51*	*2.1%*
of which: general administrative expenses	*-2,002*	*19%*	*-2,114*	*22%*	*-113*	*5.6%*
Result before provisions	**6,102**	**58%**	**4,949**	**52%**	**-1,153**	**-18.9%**
Net depreciation	-3,242	31%	-493	5%	-2,749	-84.8%
Taxes	-804	8%	-607	6%	-197	-24.6%
Net result for the financial year	**2,056**	**19%**	**3,849**	**40%**	**1,793**	**87.2%**

(*) Preliminary figures

The **interest-rate margin**, which amounted to EUR 5,482 million, fell by 16.6% over a year. This development essentially reflects the reduction in the intermediation activity which the Luxembourg banks incurred since the financial crisis. Indeed, at the beginning of 2009, the balance sheet total, which roughly allows measuring the intermediation activity, exceeded EUR 900 billion. At that time, banks recorded substantial intermediation revenues, which resulted in a high interest-rate margin for 2009. In 2010, with an average aggregated balance sheet of EUR 790 billion, the volume of intermediation activity strongly decreased. Furthermore, in a context of less favourable interest rates, the commercial margin from which banks benefit on intermediation transactions, was reduced. The decline of the interest-rate margin affects two thirds of the Luxembourg banks.

Net commissions received are mainly resulting from asset management activities on behalf of private and institutional clients, including the services provided to investment funds. They increased by EUR 480 million (+15.3%) over a year. This progress broke with the two previous financial years which, under the economic and financial crisis, registered a drop by 20% of net commissions over two years. The increase of net commissions received is generalised; it concerns 70% of the financial centre's banks.

The **other net income** whose positive development largely sustained the banks' profits in 2009, decreased to EUR 470 million in 2010. This sharp decline essentially stems from the lower fair value variations which banks recorded in the market value of their securities portfolios. It should also be noted that fair value gains on these securities had been particularly high in 2009 due to a generalised upturn in financial markets as compared to the end of 2008.

The total operating income, as measured by the **banking income** amounted to EUR 9,564 million as at 31 December 2010. The downward trend of the aggregated banking income (-9.4%) includes differences when banks are referred to individually. Indeed, the banking income positively developed for a slight majority of banks (52%) in 2010. As regards the composition of the banking income, the development of the interest income and net commissions received lead to a readjustment of the respective contribution of these two items to the operating income: interest income declined to 57% whereas net commissions received grew to 38% of the banking income. These values are similar to the average levels registered before the crisis.

Gross profit before provisions and taxes decreased by 18.9% over a year, given the 3.7% increase in general expenses.

Net creation of provisions, which mainly represents the impairment for non-trading book assets, fell by EUR 2,749 million compared to 31 December 2009. While value re-adjustments almost kept up the 2009 level, the new creation of provisions substantially declined compared to the end of 2009. Faced with a positive development of the expected economic growth, financial valuations and economic data, the need for Luxembourg banks to achieve additional provisions successively diminished since the important provisions set up in the context of the financial crisis in 2008 and 2009.

Tax charges recorded in the 2010 profit and loss account amounted to EUR 607 million. The downward development of these charges is the result of a significant reduction of deferred taxes whereas, at the level of the taxes due, the annual growth reached 32%.

Overall, the above indicated factors taken as a whole made a **net income** increase by EUR 1,793 million in 2010. Similarly to 2009, the sharp rise of the aggregated net result hides great differences in performance by the banks of the financial centre. 45% of Luxembourg banks recorded net results which, as at 31 December 2010, declined compared to the end of 2009.

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

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010 *
Interest-rate margin	4,383	4,141	4,080	3,913	3,905	4,830	6,002	7,298	6,571	5,482
Net commissions received	2,793	2,615	2,533	2,771	3,209	3,674	4,010	3,644	3,132	3,611
Other net income	672	1,258	942	734	1,140	2,296	964	-505	85	470
Banking income	**7,848**	**8,014**	**7,554**	**7,418**	**8,255**	**10,800**	**10,976**	**10,437**	**10,553**	**9,564**
General expenses	-3,624	-3,490	-3,385	-3,461	-3,693	-3,981	-4,420	-4,560	-4,451	-4,615
of which: staff costs	*-1,759*	*-1,809*	*-1,752*	*-1,798*	*-1,945*	*-2,160*	*-2,372*	*-2,461*	*-2,449*	*-2,500*
of which: general administrative expenses	*-1,866*	*-1,681*	*-1,632*	*-1,663*	*-1,748*	*-1,821*	*-2,048*	*-2,099*	*-2,002*	*-2,114*
Result before depreciation	**4,224**	**4,524**	**4,170**	**3,957**	**4,562**	**6,819**	**6,556**	**5,877**	**6,102**	**4,949**
Net depreciation	-536	-1,166	-637	-344	-296	-305	-1,038	-5,399	-3,242	-493
Taxes	-826	-638	-658	-746	-768	-843	-780	-259[5]	-804	-607
Net result for the financial year	**2,862**	**2,720**	**2,874**	**2,866**	**3,498**	**5,671**	**4,739**	**218**	**2,056**	**3,849**

(*) Preliminary figures

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

(in million EUR)	2009	2010*
Banking income / employee	0.399	0.364
Staff costs / employee	0.093	0.095

(*) Preliminary figures

1.7. Development in own funds and in the solvency ratio

1.7.1. Number of banks required to meet a solvency ratio

As at 31 December 2010, the number of banks required to meet a non-consolidated solvency ratio stood at 108, i.e. three entities less than at the same date in 2009. 94 of these banks carry out limited trading activities and are therefore authorised to calculate a simplified ratio. Actual trading activities remain confined to a limited number of banks (14 entities). Among the 29 banks that also calculate a consolidated solvency ratio, eleven are required to calculate an integrated ratio.

Number of banks required to meet a solvency ratio	Integrated ratio		Simplified ratio		Total	
	2009	2010	2009	2010	2009	2010
Non-consolidated	15	14	96	94	111	108
Consolidated	11	11	20	18	31	29

1.7.2. Development of the solvency ratio

The figures below are based on consolidated data for banks required to meet a consolidated solvency ratio. The periodic information is to be provided to the CSSF within a certain time limit which should allow banks to gather and validate the requested information. As these deadlines are longer for consolidated figures, the consolidated figures as at 31 December 2010 are available only after the cut-off date for the CSSF's annual report. As a consequence, the figures below reflect the situation as at 31 December 2010 except for banks required to calculate a consolidated solvency ratio. For these banks, the data relate to 30 June 2010, which is the last available reporting.

[5] The difference between the real tax charge estimated at EUR 732 million and the tax charge of EUR 259 million results from the possibility offered by the IFRS standards to activate future tax charges by crediting the tax charges account. By removing these positive tax expenses, mainly recorded by the six banks reporting important losses, a real tax charge of EUR 732 million remains for 2008.

- **Aggregated solvency ratio**

The aggregated solvency ratio, which measures the volume of own funds compared to the total own funds requirements according to Circular CSSF 06/273, reached 17.6% as at 31 December 2010 and largely exceeds the minimum threshold of 8% required under the existing prudential regulations.

This ratio remained overall stable over a year after a sharp increase between 2008 and 2009. The Tier 1 ratio, the numerator of which includes only own funds which absorb losses in going-concern situations, slightly increased to reach 15.3% as at 31 December 2010 against 15.1% as at 31 December 2009.

- **Own funds**

Aggregated own funds, eligible for the purpose of complying with prudential standards in terms of solvency, amounted to EUR 43,495 million as at 31 December 2010, i.e. a slight decrease of 1.5% compared to 31 December 2009. This fall is mainly attributable to a loss in global original own funds of EUR 360 million, the remaining decrease originating from the increase in items which are deducted from the total of own funds. It is important to bear in mind that, in this context, the original own funds recorded an important increase between the end of 2008 and the end of 2009 following the recapitalisation of the former Fortis Banque Luxembourg S.A. by the Luxembourg government.

As regards the components of aggregated own funds, 86.8% of the total own funds consist of the highest quality of own funds as at 31 December 2010, namely original own funds, against 86.4% at the end of 2009. Additional own funds (Tier 2) and sub-additional own funds (Tier 3) only represent 13.9% and 0.01% respectively.

Own funds *(in million EUR)*

Numerator	**2009**	**2010**
Original own funds	*41,864.1*	*42,884.5*
Paid-up capital	14,234.5	17,689.2
Silent participation (*Stille Beteiligungen)*	1,640.1	1,185.5
Share premium account	6,556.8	8,592.4
Reserves (including funds for general banking risks)	20,245.5	16,166.3
Prudential filters	-618.2	-575.7
Gains and losses brought forward for the financial year	-389.6	-302.5
Minority interests	195.0	129.3
Items to be deducted from original own funds	*-3,728.2*	*-5,115.3*
Own shares	-1.7	-93.5
Intangible assets	-1,929.9	-3,545.8
Other deductions from original own funds	-1,796.6	-1,476.0
ORIGINAL OWN FUNDS (Tier 1)	**38,135.9**	**37,769.2**
Additional own funds before capping	*7,243.6*	*6,941.0*
Upper Tier 2	3,652.9	3,885.9
Lower Tier 2: Lower Tier 2 subordinated debt instruments and cumulative preference shares with fixed maturity	3,590.7	3,055.1
Additional own funds after capping	*7,082.8*	*6,729.4*
Deductions from additional own funds	-1,001.5	-674.7
ADDITIONAL OWN FUNDS after capping and after deductions (Tier 2)	**6,081.3**	**6,054.7**
Sub-additional own funds before capping	250.2	328.6
SUB-ADDITIONAL OWN FUNDS after capping (Tier 3)	**18.5**	**3.8**
Own funds before deductions (T1 + T2 + T3)	*44,235.7*	*43,827.8*
Deductions from the total of own funds	-84.9	-332.9
ELIGIBLE OWN FUNDS (numerator of integrated ratio/simplified ratio)	**44,150.8**	**43,494.8**

- **Capital requirements**

Total capital requirement fell again by EUR 395 million (-2.0%) in 2010. This decrease results from the continuous active policies pursued by banks with respect to reducing their balance sheet total and their risk assets, commonly known as deleveraging policies. The drop in the Luxembourg banks' risk exposures is greatly reflected in the decrease of capital requirements for the coverage of credit risk which falls by EUR 332 million (-1.9%).

As regards the components of capital requirements, the credit risk exposures still need the most important capital requirements. Their proportion in total requirement amounted to over 85% as at 31 December 2010. Owing to the activities carried on in the financial centre, the other capital requirements remain marginal, except for the requirements to cover operational risk that represent 8.8% of total capital requirement.

Basel II standards were accompanied by transitional measures that provided in particular for the application of "floor levels". These levels limit the prudential recognition of the reducing effects of capital requirements that could result from the implementation of advanced measurement methods such as internal ratings-based approach for credit risk or advanced measurement approaches for operational risk. Thus, the overall capital requirement according to Basel II could not fall below 90% of the global capital requirement calculated according to Basel I during the first year of application in 2008. This threshold was lowered to 80% in 2009, a level which, in principle, will be applied until 31 December 2012[6]. The additional capital requirements due to the floor levels increased by more than 20% in 2010 and represent now over 5% of the total capital requirements. Since the calculation of the floor depends on the difference between the capital requirements under Basel I and the advanced methods which are more sensitive to risk, for a given portfolio, an increase of the floor level reflects an effective decrease of the levels of portfolio risk measurements.

Capital requirements *(in million EUR)*

Denominator	2009	2010
TOTAL CAPITAL ADEQUACY REQUIREMENT	**20,168.5**	**19,773.8**
Requirement to cover credit risk	17,151.3	16,819.7
Requirement to cover foreign exchange risk	131.6	91.6
Requirement to cover interest rate risk	77.4	67.5
Requirement to cover the risk in relation to equities	23.7	2.5
Requirement to cover the risk in relation to commodities	3.1	4.1
Requirement according to internal models	37.0	27.9
Requirement to cover settlement/delivery risk	0.6	0.1
Requirement to cover operational risk	1,894.5	1,740.1
Other capital adequacy requirements (among others exceeding large exposures, floor level, etc.)	849.4	1,020.3

RATIO		
Solvency ratio (base 8%)[7]	17.5%	17.6%
Solvency ratio (base 100%)[8]	218.9%	220.0%
Tier 1 Ratio (base 8%)[9]	15.1%	15.3%
Tier 1 Ratio (base 100%)[10]	189.1%	191.0%

[6] The banks which received an authorisation to calculate the capital requirements according to advanced methods after 31 December 2009 may receive authorisation to calculate the floor level pursuant to the standard approaches under Basel II in lieu of Basel I calculation methods.

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

[8] Eligible own funds / Total capital adequacy requirement

[9] (Original own funds - Items to be deducted from original own funds) / (Capital adequacy requirement * 12.5)

[10] (Original own funds - Items to be deducted from original own funds) / Capital adequacy requirement

As at 31 December 2010, seventeen banks had obtained the authorisation to use an internal ratings-based approach regarding credit risk according to Basel II, ten of which have used advanced methods allowing not only own estimates of probabilities of default but also of default rates in case of LGD and/or conversion factors. These seventeen banks represent 36.4% of the aggregated balance sheet total of the financial centre as at 31 December 2010.

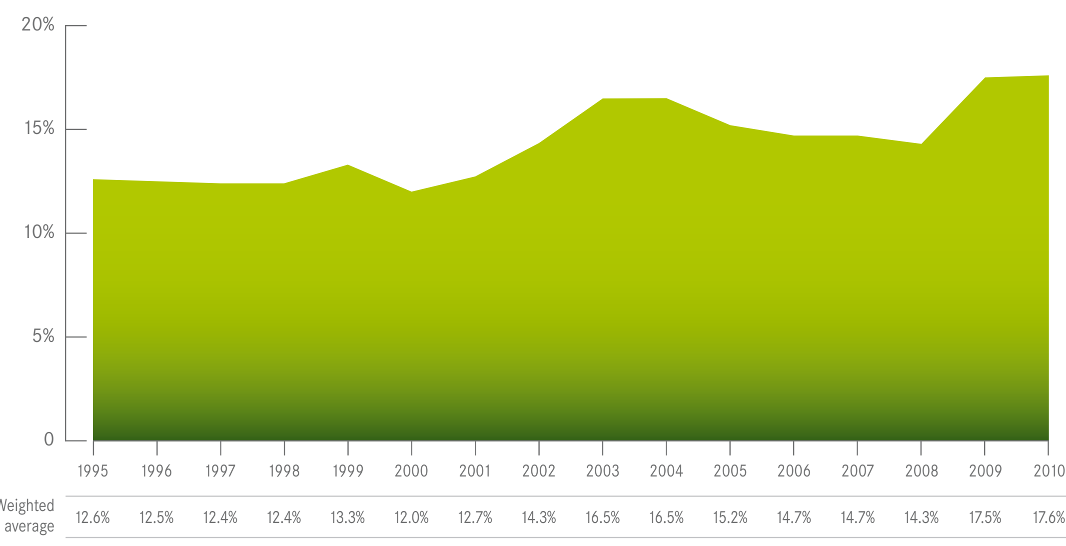
As regards operational risk, nine banks have been authorised to use advanced measurement approaches. The other banks used the basic indicator approach (61 banks) and the standardised approach (38 banks) to determine the capital requirements.

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

	Number of banks	In % of the aggregated balance sheet
Credit risk		
Standardised Approach	91	63.6%
Internal Ratings Based Approach	17	36.4%
of which: foundation approach	*7*	
of which: advanced approach	*10*	
Operational risk		
Basic Indicator Approach	61	
Standardised Approach	38	
Advanced Measurement Approaches	9	

The following graph illustrates the development in the solvency ratio (base 8%) since 1995. The weighted average is the ratio of total eligible own funds in the financial centre and total weighted risks. This average takes into account credit institutions according to the volume and risk level of their business.

Development in the solvency ratio (base 8%)



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

The high level of capitalisation, reflected by the aggregated solvency ratio, also appears at disaggregated level. Thus, only seven banks have a solvency ratio situated within the weak capitalisation bands, i.e. below 10%. This number remained stable between 2009 and 2010 with an increase of one unit. At the other extreme, in the high capitalisation bands, the percentage of banks whose ratio exceeds 15% slightly fell from 70% to 68% year-on-year.

Distribution of the solvency ratio (base 8%)

	2009		2010	
Ratio	Number of banks	as % of total	Number of banks	as % of total
<8%	0	0%	0	0%
8%-9%	2	2%	2	2%
9%-10%	4	4%	5	4%
10%-11%	3	3%	3	3%
11%-12%	5	5%	6	6%
12%-13%	6	5%	12	11%
13%-14%	7	6%	4	4%
14%-15%	6	5%	2	2%
15%-20%	29	26%	24	22%
>20%	49	44%	50	46%
Total	**111**	**100%**	**108**	**100%**

1.8. International presence of Luxembourg banks

Freedom to provide services within the EU/EEA as at 31 December 2010

Country	Luxembourg banks providing services in the EU/EEA	EU/EEA banks providing services in Luxembourg
Austria	35	27
Belgium	55	23
Bulgaria	17	-
Cyprus	19	3
Czech Republic	20	-
Denmark	38	6
Estonia	19	1
Finland	36	9
France	59	74
Germany	60	45
Gibraltar	1	6
Greece	33	2
Hungary	20	7
Iceland	5	2
Ireland	32	30
Italy	46	11
Latvia	19	-
Liechtenstein	6	3
Lithuania	19	1
Malta	17	7
Netherlands	49	30
Norway	18	1
Poland	25	1
Portugal	33	6
Romania	21	-
Slovakia	19	1
Slovenia	19	-
Spain	47	7
Sweden	35	4
United Kingdom	45	90
Total number of notifications	**867**	**397**
Total number of banks concerned	**74**	**397**

Branches established in the EU/EEA as at 31 December 2010

Country	Branches of Luxembourg banks established in the EU/EEA	Branches of EU/EEA banks established in Luxembourg
Austria	2	-
Belgium	6	2
France	2	4
Germany	4	16
Ireland	3	2
Italy	5	-
Netherlands	2	1
Poland	2	-
Portugal	2	1
Spain	7	-
Sweden	1	1
United Kingdom	1	4
Total	**37**	**31** [11]

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

The public debt crisis continues affecting the business model of banks issuing covered bonds, so that they did not launch new important issues but mostly concentrated on making more moderate issues, or even on managing only their existing cover assets and thus on carrying out a deleveraging of their balance sheet.

In the absence of considerable progress in the activities, the balance sheet total of the banks issuing covered bonds remained unchanged compared to 2009 and amounted to EUR 48.6 billion as at 31 December 2010. The volume of the public sector covered bonds issued by five banks slightly dropped and amounted to EUR 28.9 billion at the end of 2010 (EUR 31.1 billion at the end of 2009).

Issues of covered bonds are guaranteed by ordinary cover assets and by substitute cover assets. As at 31 December 2010, public sector covered bonds in circulation benefited from an over-collateralisation (nominal value) of EUR 5.9 billion. Over-collateralisation calculated according to the current value amounted to EUR 6.3 billion.

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

- claims on or guaranteed by public organisations: EUR 13.7 billion;
- bonds issued by public organisations: EUR 9.5 billion;
- public sector mortgage bonds of other issuers: EUR 6.3 billion;
- derivative transactions: EUR 1.4 billion.

Besides these ordinary cover assets, the banks used substitute cover assets to cover their public sector covered bonds amounting to EUR 3.7 billion as at 31 December 2010.

Due to a new rating methodology for covered bonds introduced by the rating agency Standard & Poor's, covered bonds issued by one of the banks issuing covered bonds only benefit from an AA rating whereas the covered bonds issued by the others continue benefiting from an AAA rating.

In this context, studies are being carried out in order to change the liquidation regime of banks issuing covered bonds so as to allow the banks issuing covered bonds which are in liquidation to access liquidity sources and to avoid thus an interruption of interest and principal payment due to a non-concordance between the maturities of assets and of liabilities.

Finally, it should be noted that the activities of Luxembourg banks are currently limited to the issue of public sector covered bonds, despite the law of 24 October 2008 which modernised their legal framework by allowing the financing of certain movable assets (aircrafts, ships, objects relating to railways, etc.) and the refinancing with moveable-property bonds.

[11] Including an EU financial institution according to Article 31 of the law of 5 April 1993 on the financial sector.

1.10. Payment institutions

The law of 10 November 2009 on payment services, on the activity of electronic money institutions and on the settlement finality in payment and securities settlement systems transposes Directive 2007/64/EC of 13 November 2007 on payment services in the internal market into national law. This directive aims at setting up a coherent legal framework in order to establish a single European market for payment services and to ensure its orderly functioning.

The law of 10 November 2009 introduces a new status of financial institutions, i.e. the "payment institutions" which may exercise the activity of payment services and submits them to authorisation, exercise and supervisory conditions. The payment services concerned are specifically listed in the annexe to the law.

Article 31(1) of the law designates the CSSF as the competent authority for the supervision of payment institutions.

The main prudential provisions applicable to payment institutions may be summarised as follows:

- quantitative prudential standards, i.e. a minimum capital and capital requirements calculated according to one of three methods provided for in the law; the CSSF monitors the correct application and the compliance with these quantitative standards based on a specific reporting;
- rules for the protection of funds received for the execution of payment transactions;
- guarantee of a sound and prudent management and the existence of a strong internal governance system;
- rules related to the fight against money laundering and terrorist financing.

As regards the two last points, the rules are in principle those applicable to credit institutions and to investment firms but they will be applied to payment institutions according to a proportionality principle which is made of, among others, the type of activities of payment services and the risk incurred.

The activities exercised by the Luxembourg payment institutions in another Member State of the EU/EEA through the establishment of a branch, through the intermediary of an agent or *via* the free provision of services, are also subject to the prudential supervision by the CSSF.

By way of compensation for the simplified rules to access the profession and for the lighter prudential supervision compared to those applicable to credit institutions, the payment institutions are subject to activity restrictions and prohibitions:

- strict control of credit granting;
- prohibition to conduct the business of taking deposits or other repayable funds within the meaning of Article 2(3) of the law of 5 April 1993 on the financial sector;
- exclusive use of payment accounts opened by payment institutions for payment transactions.

As at 31 December 2010, one payment institution, i.e. SIX Pay S.A., was registered in the public register of payment institutions authorised in Luxembourg.

2. PRUDENTIAL SUPERVISORY PRACTICE

2.1. Purpose of prudential supervision

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

2.2. Monitoring of quantitative standards

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

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

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

In 2010, the CSSF intervened once regarding the non-compliance with the capital ratio. The CSSF intervened three times in writing regarding failure to meet the liquidity ratio.

Within the scope of monitoring compliance with large exposure limits, the CSSF intervened twelve times in writing in 2010 (fourteen times in 2009), notably to inform that the maximum level of large exposures had been exceeded and to request the bank concerned to provide information on the measures it intended to take to bring back the commitments within the regulatory limits.

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

Financial intermediation, at the heart of the traditional banking activity, includes the collection of refundable deposits on the liabilities side and granting of credits on the assets side. In general, the duration of assets exceeds that of liabilities. In this case, a rise in interest rates increases the cost of short maturity deposits while fixed-rate assets continue to generate the same level of interest income until their maturity. This results in a decreasing profitability.

In Luxembourg, the diversification of the traditional banking activity, by means of private banking and investment funds services, entails that the interest rate risk is overall less marked. Moreover, the wide range of available interest rate risk cover instruments allows efficiently reducing this risk. On the other hand, the instruments concerned could be used to take on higher interest rate risk positions.

In order to allow a uniform supervision of interest rate risk (non-trading book), Circular CSSF 08/338 requires banks to submit on a half-yearly basis the results of a stress test to the CSSF. This requirement is in line with an EU requirement laid down in Article 124(5) of Directive 2006/48/EC.

The CSSF analyses the results of these stress tests based on a ratio whose numerator is the result of the simulation of interest rate changes according to Circular CSSF 08/338 and whose denominator is given by regulatory capital. This ratio measures the percentage of own funds mobilised through the (unrealised) value

losses resulting from an adverse change in interest rates. According to Article 124(5) of Directive 2006/48/EC, the CSSF shall require measures when this ratio falls below -20%. Such measures aim to ensure that own funds of an institution remain adequate with respect to its overall risk situation, which includes in particular non-trading book interest rate risk. It should be borne in mind that the non-trading book interest rate risk is not subject to a capital requirement according to Circular CSSF 06/273, as opposed to interest rate risk inherent in trading book portfolio.

The analysis of the stress test results according to Circular CSSF 08/338 as at 31 December 2009 and 30 June 2010 shows that the Luxembourg banking sector is only moderately exposed to structural interest rate risk. Indeed, the aforementioned ratio is about -4.4% on individual basis and -2.8% on consolidated basis. The impact of an immediate 2% rise in overall interest rates would cut the intrinsic value of the financial centre's banks only by about 4.4% of own funds. These figures represent a slight decrease of the structural interest rate risk compared to the previous half-years. As far as the dispersion of the results on individual perimeters is concerned, 71% of the banks of the financial centre have a ratio which is higher than or equal to -5% and only 4% of the banks have a ratio of less than -15% as at 30 June 2010. As regards the consolidated perimeter, 80% of the banks have a ratio above -5% whereas no bank has a ratio below -15%. In 2010, the CSSF intervened with two banks in the financial centre whose ratio was lower than the -20% threshold on 30 June 2010. The CSSF required that the institutions prove that their overall risk management is sound and prudent.

2.4. Developments regarding liquidity supervision

The overall liquidity situation in the Luxembourg banking sector may be considered as comfortable. While 2010 showed a deterioration of public finances in certain eurozone countries, no particular liquidity tensions were felt for banks of the financial centre. Structurally, the aggregated Luxembourg banking sector continued registering a liquidity excess resulting from deposits related to wealth management activities and investment fund services. For banks of the financial centre which need refinancing due to their credit activity, the liquidity situation generally improved in the wake of the decrease of balance sheet totals.

As regards liquidity risk, the CSSF continues to apply the principles of prudential supervision redefined in 2008. In particular, these principles set out the CSSF's acceptance of intra-group risk inherent in the recycling of intra-group liquidity surplus insofar as these transactions do not harm the sound risk profile of the banks in Luxembourg. Prohibited intra-group transactions are those that result in risky liquidity gaps (maturity or currency gaps) or substantial counterparty risk (loans to peripheral group entities, which, in extreme situations, could loose the support of the parent company).

In practice, the cooperation between the CSSF and the BCL mainly involves the coordination of on-site inspections and regulatory developments, in accordance with the cooperation requirements laid down in the law of 24 October 2008 improving the legislative framework of the Luxembourg financial centre.

The regulatory framework which is the basis for the liquidity supervision carried out by the CSSF did not incur major changes in 2010. It is mainly defined in three circulars: Circular CSSF 07/301 which lays down the main guiding principles regarding the sound risk management, Circular CSSF 09/403 which provides the qualitative requirements as regards the sound liquidity risk management and Circular IML 93/104 which limits the structural liquidity risk by imposing a liquidity ratio (table B1.5). Circular CSSF 10/475, published in July 2010, formally completes the Luxembourg Basel II framework with qualitative requirements in relation to liquidity risk management as set out in Directive 2009/111/EC. In substance, these requirements already existed in the Luxembourg regulation, namely in Circular CSSF 09/403 which implements the detailed EBA guidelines in relation to liquidity risk management.

As a consequence of the current discussions on the fourth recast of Directive 2006/48/EC (CRD IV), the quantitative regime regarding liquidity as laid down in Circular IML 93/104 (table B1.5 "Liquidity ratio") will be repealed and replaced by two new prudential ratios called Liquidity Coverage Ratio (LCR) and Net Stable Funding Ratio (NSFR). These ratios are based on proposals of the Basel Committee on banking supervision as published in December 2010 ("International framework for liquidity risk measurement, standards and monitoring").

The purpose of LCR, which measures short-term liquidity risk, is to guarantee that a bank has sufficient liquid assets to face short-term liquidity deficits, even during adverse situations. The NSFR, which requires a minimum amount of stable financing for assets whose maturity exceeds a year, disqualifies risky business models which need a flawless renewal of short-term interbank deposits (of markets) in order to refinance the less liquid assets in the long run.

In order to better monitor the impact of the new proposals for quantitative rules regarding liquidity and to allow supporting the Luxembourg points of view during international discussions, the CSSF, together with the BCL, requested in April 2010 a sample of Luxembourg banks to carry out a simulation of the two ratios concerned. The results of this impact study clearly showed that the Basel Committee's proposal regarding liquidity is restrictive, particularly for depositary banks widely present in Luxembourg. During 2010, the Basel Committee readjusted the parameters of the two liquidity ratios so as to correct some side effects. Thus, under the CSSF's and BCL's common impulse, the reviewed proposals now provide for an adequate prudential recognition of the stability of operational liquidities from which the depositary banks benefit.

While the entry into force of the prudential regime for LCR (NSFR) is scheduled for 1 January 2015 (1 January 2018), a reporting harmonised at EU level shall be implemented on 1 January 2012. This reporting will allow the CSSF to monitor in particular how Luxembourg banks progressively comply with the prudential limits organising the LCR as from 2015. In order to prevent a double prudential regime by which the banks would have to comply with both the current ratio B1.5 and the progressive application of the LCR, the CSSF intends to set up a transition period. This transition period would allow the banks to replace as from 2012, on their own initiative, the compliance with ratio B1.5 with the compliance with the LCR, the limit of which would gradually increase so as to reach the 100% laid down in CRD IV as at 1 January 2015.

2.5. Monitoring of qualitative standards

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

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

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

During 2010, the CSSF sent 119 deficiency letters to banks because of shortcomings in their organisation (75 in 2009).

The CSSF intervened six times due to quality deficiencies of ICAAP reports.

One of the important lessons to be learnt from the financial crisis is that prudential supervision must not be limited to verifying compliance with regulations. Some banks had to be supported by their respective States or their payments suspended despite their strict compliance with prudential regulations. Within the process of prudential supervision laid down in Circular CSSF 07/301, the CSSF requires banks to maintain a sound relation between their risk exposures and their capacity to support those risks.

During 2010, the CSSF intervened six times with banks in order to request either a decrease in risk or a cessation of risky practices.

2.6. Supervisory review process

The Supervisory Review Process (SRP) refers to the assessments, controls and measures as a whole, implemented by the CSSF in order to assess and preserve the capacity of a credit institution to manage and support the risks it incurs. The SRP's scope goes further than the risks that are explicitly regulated (regulation as regards solvency, liquidity or large exposures). The SRP covers all the risks that may undermine the financial stability of an institution individually or of the banking sector as a whole, regardless of the origin, nature or regulatory or accounting treatment of these risks.

In 2010, the CSSF developed its SPR according to the international regulation, especially following the publication of Directive 2009/111/EC and CEBS guidelines GL39.

2.6.1. Directive 2009/111/EC

Directive 2009/111/EC which is part of the CRD II measures amends the Basel II framework as applied in the EU *via* Directive CRD (2006/48/EC).

Firstly, Directive 2009/111/EC completes Pillar 2 of the Basel II framework at EU level with reinforced provisions regarding a sound liquidity risk management. These provisions already existed in the Luxembourg regulatory framework under Circular CSSF 09/403 which implements EBA's detailed guidelines with respect thereto. Directive 2009/111/EC restates the main principles in this respect. Circular CSSF 10/475 published in July 2010 includes these generic principles in the Luxembourg Basel II framework by amending Circular CSSF 06/273.

Secondly, Directive 2009/111/EC, which requires the creation of supervisory colleges for banking groups operating in the EU on a cross-border basis, extends the scope of these colleges by including the ICAAP procedure and the supervisory review process. The new Article 129(3) of Directive 2006/48/EC introduced by Directive 2009/111/EC lays down that the supervisory authorities which meet in colleges shall reach a joint decision on the adequacy of consolidated own funds of the European banking groups and the distribution of these own funds between the groups' entities. In the absence of a joint agreement at the level of the college, the decision as regards the adequacy of own funds and, where applicable, the requirement for an add-on to those own funds remain with the supervisory authorities of the host Member State. Thus, the CSSF ultimately is the decision-maker as regards the implementation of its additional capital policy at national level.

The above-mentioned provisions will be subject to a transposition in Luxembourg law according to the modalities set out in the draft law No 6165. It should be pointed out that the CRD IV rules, which are currently being discussed at the European Commission, lay down a development of this decision-making mechanism in favour of a final decision taken by EBA in case of persistent disagreements between the supervisory authorities. In this case, the supervisory authority of the host Member State would loose its decision-making power. The CSSF would, thus, in case of disagreement in the college, be deprived from its power to impose its local additional capital policy.

2.6.2. EBA's guidelines regarding the joint decision-making procedure

On 22 December 2010, CEBS (EBA since 1 January 2011) published the guidelines GL39 which govern the joint decision-making procedure laid down in Article 129(3) of Directive 2006/48/EC as amended by Directive 2009/111/EC for banks which operate in the EU on a cross-border basis. These joint decisions refer to risk profile, ICAAP adequacy and compliance with the minimum requirements set out in this directive. Chapters 2, 3 and 4 of GL39 propose for every matter subject to a decision, a harmonised assessment scheme which includes criteria of assessment and a common marking grid. Henceforth, the assessments made by the CSSF in the context of the banks' colleges will be submitted in detail and in the format defined in GL39 to the supervisory authorities of the home Member State.

In order to guarantee an equal treatment for all the banks of the financial centre and a single and coherent supervisory review process, the CSSF decided to implement the GL39 guidelines for all the credit institutions subject to its supervision. The inclusion of the GL39 guidelines into the CSSF's SRP is expected to be finalised

by mid 2011. Already at this stage, it appears that in order to dispose of all the details for the assessments foreseen by EBA, the CSSF will need to request additional information from the banks. The CSSF intends to address this request for information by the publication of a new ICAAP circular which will specify the content of the ICAAP report referred to in points 17 and 26 of Circular CSSF 07/301. These rules will first be applicable for ICAAP reports related to the financial year 2011.

As regards the future of SRP, it is useful to specify that the regulatory amendments under Basel III/CRD IV do not modify the philosophy inherent to Pillar 2. The fact that some minimum requirements (of Pillar 1) are reinforced does not cancel the necessity for banks to keep a risk profile in accordance with their capacity to manage and support risks and for the supervisory authorities to assess and control this adequacy pursuant to the principles governing Pillar 2 of the Basel II/III framework.

2.7. Analytical reports

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

In 2010, the CSSF analysed 137 analytical reports, 30 of which were consolidated analytical reports and 76 were analytical reports of subsidiaries of Luxembourg banks.

2.8. Cooperation with the *réviseurs d'entreprises* (statutory auditors)

Article 54 of the law of 5 April 1993 on the financial sector governs the relationship between the CSSF and the *réviseurs d'entreprises* (statutory auditors). This article confers upon the CSSF the power to establish the rules relating to the scope of the audit mandate and the content of the audit report. The supervised professionals are requested to communicate all the reports in relation to the audit of the accounting documents issued by the *réviseur d'entreprises* (statutory auditor) to the CSSF.

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

Since 2002, the CSSF has held annual meetings with the main audit firms in order to exchange opinions on specific issues encountered within the supervised institutions. The discussions may also address the quality of the reports made.

2.9. On-site inspections

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

In 2010, the CSSF intensified the frequency of its on-site inspections. Thus, 56 on-site inspections and on-site visits were carried out compared to 38 in 2009.

Subject	Number of on-site inspections
Real estate loans	4
Internal audit function	3
Internal models	6
Market activity	1
Money laundering	15
MiFID	3
Corporate governance	2
Lombard loans	1
Total	**35**

Subject	Number of on-site visits
ICAAP	1
Group head function / development of subsidiaries	4
General organisation	1
Liquidity	4
Knowledge of activities	5
Introductory visits	4
Others	2
Total	**21**

Control of compliance with professional obligations regarding the fight against money laundering and terrorist financing is the area to which the CSSF pays particular attention during on-site inspections.

Moreover, real estate financing remains a concern. Under the pressure of the competition, a certain laxity of the traditionally prudent criteria was noted whereas the concentration risk in this area increased. Furthermore, the low level of interest rates favours the appearance of a speculative bubble. For this reason, the CSSF is currently drawing up regulations for the granting and provisioning processes of real estate loans.

2.10. Combating money laundering

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

The CSSF uses the following instruments to monitor compliance with AML/CFT rules: reports of *réviseurs d'entreprises* (statutory auditors) and those prepared by internal auditors, as well as the inspections made by CSSF agents. In 2010, the CSSF made fifteen on-site inspections with respect to compliance with professional obligations concerning AML/CFT (ten in 2009).

During the year under review, the CSSF sent 34 letters to banks in relation with shortcomings concerning AML/CFT. These letters, based on on-site inspections carried out by the CSSF or on external or internal audit reports, listed the shortcomings identified and enquired about the corrective measures envisaged. Among the most frequently observed shortcomings are:

- weaknesses in the systems for detection of suspicious transactions;
- weaknesses as regards the control of the customer's name against the databases registering PEPs (Politically Exposed Persons);
- insufficiencies in the procedures;
- insufficiencies as regards the control of incoming and outgoing funds;
- weaknesses in subsidiaries and branches.

The yearly analytical report prepared by *réviseurs d'entreprises* (statutory auditors) must specifically cover compliance with legal requirements and the adequate implementation of internal procedures for the prevention of money laundering.

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

2.11. Management letters

Management letters drawn up by *réviseurs d'entreprises* (statutory auditors) for the attention of the banks' management are an important source of information as regards the quality of the credit institutions' organisation. In these reports, the *réviseurs d'entreprises* (statutory auditors) point out weaknesses in the internal control system they observed in the course of their assignment. During 2010, the CSSF analysed 55 management letters and similar documents (57 in 2009).

2.12. Meetings

The CSSF regularly holds meetings with bank executives to discuss business and any problems. It also requires prompt notification by the banks if a serious problem arises. In 2010, 264 meetings were held between CSSF representatives and bank executives.

2.13. Specific audits

Article 54(2) of the law of 5 April 1993 on the financial sector allows the CSSF to require a *réviseur d'entreprises* (statutory auditor) to conduct an audit on a specific subject in a given institution.

In 2010, the CSSF made use of this right eleven times against eight in 2009. In seven cases, the specific audit concerned the compliance with the publication of information on risk (Pillar 3). In two cases, the area of private banking was concerned. The credit activity and the management of the sub-depositary network were each the subject of one specific audit requested by the CSSF.

2.14. Internal audit and compliance reports

The CSSF takes into account the work of the internal audit when assessing the quality of the organisation and risk management by analysing the summary report which the internal auditor must prepare every year, as well as the report of the Compliance officer. In 2010, the CSSF analysed 125 summary reports (117 in 2009). It also requested 42 specific internal audit reports in order to obtain more detailed information on particular subjects (50 in 2009). The CSSF also analysed 124 compliance reports (117 in 2009).

2.15. Supervision of branches of EU banks

The supervision carried out by the CSSF of EU branches established in Luxembourg is limited to the areas in which the CSSF is responsible as host authority. Thus, Article 45(3) of the law of 5 April 1993 on the financial sector appoints the CSSF to supervise the liquidity of these branches, in cooperation with the competent authority of the home Member State. To allow the CSSF to exercise its duties in this matter, these branches must provide the same information as the Luxembourg credit institution to the CSSF.

In addition, the branches of EU banks must mandate their *réviseur d'entreprises* (statutory auditor) to issue the following reports:

- a report on control of compliance with the legal professional obligations relating to AML/CFT;
- a report on the compliance with the rules of conduct for the provision of investment services to clients, in accordance with the provisions of Circular CSSF 07/307 concerning conduct of business rules in the financial sector.

2.16. Supervision on a consolidated basis

As at 31 December 2010, 26 banks under Luxembourg law (30 at the end of 2009), one financial holding company under Luxembourg law (two in 2009), as well as one financial holding company incorporated under foreign law (*idem* in 2009) were supervised on a consolidated basis by the CSSF.

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

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

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

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

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

- The CSSF requires periodic reports reflecting the financial situation and the consolidated risks of a group subject to its consolidated supervision.
- The ICAAP report shall provide an assessment of the consolidated capital adequacy in relation to the risks taken by the group or sub-group. Part of this report concentrates on the consolidated risk profile of the group or sub-group subject to the consolidated supervision.
- The reports prepared by the external auditors are another source of information. Circular CSSF 01/27 on practical rules regarding the mission of the *réviseur d'entreprises* (statutory auditor) requires that a consolidated analytical report of a group subject to the consolidated supervision of the CSSF must be drawn up. The purpose of this consolidated report is to provide the CSSF with an overview of the group's situation and to inform of the risk management and structures of the group.
- The CSSF requires an individual analytical report for each major subsidiary.
- By virtue of Circular IML 98/143 on internal control, a summary report on the activities carried out by the internal audit department is to be communicated to the CSSF on an annual basis. The CSSF requires that the scope of intervention of the internal audit of the Luxembourg parent company be also extended to the subsidiaries in Luxembourg and abroad. This report must mention the controls carried out within the subsidiaries and the results thereof. The main observations made within the subsidiaries as regards the compliance function as defined in Circular CSSF 04/155 shall also be mentioned therein.

- The CSSF's information is supplemented by contacts, exchange of letters and meetings with supervisory authorities of the subsidiaries' host countries. Within the scope of its supervision on a consolidated basis, the CSSF expects to systematically obtain, from the banks and financial holding companies subject to consolidated supervision, information on any intervention of the host country authorities with the subsidiaries, where these interventions concern non-compliance with domestic regulations and aspects regarding organisation or risks of these subsidiaries.
- As regards groups with an important network of subsidiaries, the CSSF follows the development of the financial situation and the risks of the subsidiaries included in the consolidated supervision by means of regular meetings with the management of the credit institution or of the financial holding company under consolidated supervision.
- The CSSF performs on-site inspections that cover, on the one hand, the manner in which the parent company sets up its policies and implements its strategies within the subsidiaries and, on the other hand, the follow-up applied to the subsidiaries. Until now, the CSSF has not carried out itself any on-site inspection at the premises of foreign subsidiaries of Luxembourg banks.

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

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

2.17. Supplementary supervision of financial conglomerates

Chapter 3b of Part III of the law of 5 April 1993 on the financial sector requires the CSSF to carry out a supplementary supervision of financial conglomerates. A financial conglomerate is defined as a group that includes at least one important regulated entity within the banking or investment services sector and one important entity within the insurance sector.

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

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

As the CSSF has not at this stage identified any financial conglomerate for which it has to exercise the role of coordinator of this supplementary supervision, the practical consequences of these provisions for Luxembourg credit institutions and investment firms are limited.

2.18. International cooperation in matters of banking supervision

Articles 128 to 132 of Directive 2006/48/EC govern the cooperation between European competent authorities and may also include non-European authorities. These articles require an intensive cooperation between the competent authorities of cross-border banking groups and strive towards a more centralised and harmonised supervision of these large cross-border groups at EU level *via*, among others, the implementation of a college of supervisors for these cross-border groups.

In 2010, the CSSF also held three bilateral meetings and one trilateral meeting with banking supervisory authorities in order to exchange prudential information on supervised institutions having a presence in those countries.

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

2.18.1. Colleges of supervisors

The European cooperation for the supervision of banks is laid down in Article 131a of Directive 2006/48/EC, as amended by Directive 2009/111/EC, which provides: "The consolidating supervisor shall establish colleges of supervisors to facilitate the exercise of the tasks referred to in Article 129 and Article 130(1) ...".

The draft law No 6165 will transpose, among others, Article 129(1b), (1c) and (3), Article 130(1) and Article 131a which were introduced by Directive 2009/111/EC into Luxembourg law. This regulation concerns the establishment and the activities of the colleges of supervisors whether for the continuous functioning or in emergency cases.

The colleges of supervisors are set up by a Memorandum of Understanding (MoU) signed between the different authorities participating in the colleges. Where applicable, the colleges may include countries other than EEA Member States.

Until now, the colleges were created particularly for banking groups which are systemically important at European level. Currently, the supervisory authorities work on the creation of colleges for banking groups with lesser importance but which perform nevertheless activities in several EEA countries.

At this time, the CSSF is not the competent consolidating authority for any systemic group. Consequently, it will only set up colleges as from 2011 for banking groups which are subject to its consolidated supervision.

Until 2010, the colleges' main activity was the establishment of a first contact between the authorities as these colleges were often newly set up. Some colleges performed a first risk assessment of the banking groups. To that end, the different authorities, members of the colleges, provided the authority in charge of the consolidated supervision with their risk assessment. The latter aggregated the information received by taking also into account the entities established in its own country. The above was a pilot project by CEBS in order to test the template for the Supervisory Review and Evaluation Process (SREP) proposed in CEBS Consultative paper 39. Following this exercise, CP 39 was finalised and published as Guidelines 39 which shall be applied to all European banking groups by the colleges of supervisors as from 2011.

In 2010, the CSSF signed 24 MoUs (15 in 2009) and participated in 58 college meetings (20 in 2009). These figures prove the development of the international cooperation relating to supervision and the importance of having appropriate human and financial resources.

2.18.2. Joint audits

In the past, joint audits were mainly, but not exclusively, limited to the validation of models in the framework of the adoption of advanced approaches for the calculation of the banks' solvency ratio.

Joint audits may be extended to all areas of the prudential supervision to allow the community of supervisors which are part of a college of supervisors to acquire a global and coherent overview of the incumbent problems and risks within banking groups. In 2010, the CSSF participated in five joint audits with other authorities.

2.19. Review of risk management models

In 2010, the CSSF continued its review of the risk management models. In this context, a distinction should be made between the risk management models eligible for the calculation of regulatory capital requirements ("Pillar 1 models") and the models which may be used for the calculation of internal capital requirements ("economic capital models" or "Pillar 2 models").

2.19.1. Pillar 1 models

The risk management models of Pillar 1 cover three categories of risks[12], namely:

- credit risk with models relating to internal rating systems (internal ratings-based approach - IRB);
- market risk with "internal models" to cover the general and specific market risk; and
- operational risk with the advanced measurement approaches (AMA).

As the banks established in Luxembourg are often subsidiaries of European banking groups, the review of risk management models takes place in close consultation between the home authority and host authority, i.e. the CSSF, in accordance with Article 129 of Directive 2006/48/EC.

As regards the task sharing between the home authority and the CSSF, the following cases shall be pointed out:

a) Use by a local subsidiary of a model developed by the group

   In this case, the parent's home authority reviews the model's theoretical bases while the CSSF's role is limited to verifying its local use. In order to be able to use the models for the calculation of regulatory capital requirements, credit institutions shall prove that they are indeed used for the daily risk management.

   The verification of the local application for models relating to internal ratings-based systems mainly covers the following points: the internal governance, the use of the models for risk management and the experience gained during this use (use test and experience test), a sufficient coverage of all the exposures by the models, allocation of exposures to the relevant grades and pools, stress tests and internal governance relating to those models.

   As regards the operational risk management models, the CSSF's mission mainly concerns the use of the model on a day-to-day basis, the process of stocktaking and of reporting of operational losses, and the methodology regarding the capital requirement allocation.

   The observations as regards these missions are then communicated to the home authority and to the bank.

b) Use by a local subsidiary of a model developed at local level

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

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

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

In 2010, the CSSF performed five more extended missions relating to the review of the internal rating systems, i.e. three follow-up missions regarding already approved models and two missions regarding the first application of the IRB approach.

[12] See also point 1.7. of this chapter.

As regards the review of AMA for the calculation of regulatory capital requirements in relation to operational risk, two more extended follow-up missions took place in 2010. Moreover, a request for the first application was submitted to the CSSF during the last quarter of 2010 in order to receive authorisation in 2011.

The follow-up of the compliance with the qualitative and organisational requirements of credit institutions which already received authorisation to use the models for the calculation of the regulatory capital requirements represents an integral part of the supervisory review and evaluation process (SREP) by the CSSF[13]. The CSSF implemented analysis tools based on the periodical reporting (particularly COREP and FINREP) in order to identify significant developments of the risk parameters between the credit institutions and between the reporting dates. The exceptions which are identified may lead the CSSF to request further information or to organise specific and targeted on-site missions.

2.19.2. Pillar 2 models

The CSSF regularly follows up the results of the models for the calculation of internal capital. These figures represent an integral part of the reporting on risk management and capital (ICAAP report) such as described under points 17 and 26 of Circular CSSF 07/301. In 2010, the CSSF analysed 118 ICAAP reports. The analysis resulted in seventeen specific meetings and six observation letters.

It is important to note that, unlike the risk management models used in the framework of Pillar 1, the models used in the framework of Pillar 2 are not subject to an explicit authorisation procedure of the authorities. The purpose of the review of these models lies with the more general and less prescriptive assessment of the sound risk management. Thus, the review of the methodology is performed by the home authority in most cases. In the particular case of joint missions between authorities, the participation by the CSSF is usually limited to local aspects and to risk models which have a particular importance for the activities of the Luxembourg subsidiaries[14].

[13] See also the guidelines CEBS GL03 and CEBS GL39.

[14] In most cases, those aspects deal with the definition of internal capital and with the operational, reputational and liquidity risk.

SUPERVISION OF UNDERTAKINGS FOR COLLECTIVE INVESTMENT

03

1. Developments in the UCI sector in 2010
2. Performance analysis of the major Luxembourg UCI categories in 2010
3. Management companies set up under Chapter 13 of the law of 20 December 2002
4. Developments in the regulatory framework
5. Prudential supervisory practice

1. DEVELOPMENTS IN THE UCI SECTOR IN 2010

1.1. Major events in 2010

In Luxembourg, the sector of undertakings for collective investment (UCIs) recorded a growth of 19.4% in the net assets under management and of 5.9% in the number of UCIs in 2010.

2010 was characterised by a continuation of the coordination of economic and monetary policies by the majority of the G20 countries and, to some extent, by the recovery of the world economy which contributed to stabilising the financial markets. As an example, the index MSCI WORLD INDEX Standard (Large+Mid Cap) (EUR) grew by 19.5% in 2010 and the global bond index JPMorgan GBI Global Traded Index Hedged Index Level Euro increased by 4.3%.

The improvement of the world economic activity in 2010 and the continuous downward trend of the investors' risk aversion led the investors to increase their request for higher risk UCIs. Thus, equity UCIs registered a net capital investment of EUR 36.477 billion in 2010. The net capital investment of bond UCIs amounted to EUR 90.023 billion and that of diversified UCIs amounted to EUR 33.863 billion. However, given the historically low Central Bank interest rates and money market rates, monetary UCIs registered net redemptions of EUR 43.716 billion.

Due to the positive evolution of the financial markets, accompanied by the increase in net investments in UCIs, the volume of net assets of Luxembourg UCIs increased from EUR 1,841 billion to EUR 2,199 billion. This increase of 19.4% in relative terms and EUR 358 billion in absolute terms is due partially to the net capital investment (45%) and partially to the positive impact of financial markets (55%).

The number of UCIs and specialised investment funds (SIFs) totalled 3,667 as at 31 December 2010 as against 3,463 at the end of 2009.

Seven management companies authorised pursuant to Chapter 13 of the law of 20 December 2002 were set up in Luxembourg in 2010 whereas twenty management companies ceased their activities in Luxembourg.

As far as regulations are concerned, the European Directive 2009/65/EC (UCITS IV Directive) was transposed into Luxembourg law by the law of 17 December 2010. At European level, the AIFM Directive (Alternative Investment Fund Managers) was voted in the European Parliament on 11 November 2010. This directive harmonises and amends the regulatory framework with which the alternative investment fund managers will have to comply. In return, the managers are offered new opportunities through a European passport which allows them to provide management services and to offer their funds to well-informed investors in all the EU Member States. The provisions of the directive cover, among others, the authorisation conditions for managers, the capital requirements, the requirements as regards liquidity and risk management, the requirements in relation to valuation, depositaries, delegation arrangements, the disclosure of information, the restrictions on the use of leverage and the clauses for non-EU countries.

1.2. Developments in the UCI sector

1.2.1. Development in the number of UCIs

3,667 UCIs were registered on the official list as at 31 December 2010 against 3,463 UCIs at the end of the previous year, representing an increase of 204 entities (+5.9%). Over the year, 471 UCIs were newly registered and 267 entities were withdrawn from the official list.

Over the last ten years, the number of UCIs has risen by 1,882 entities, which corresponds to an average growth of 10.5% per year. The 2010 growth may, thus, be characterised as rather weak compared to 2007 and 2008 which were marked by the launch of specialised investment funds introduced by the law of 13 February 2007.

Development in the number of UCIs

	Number of UCIs	Registrations on the official list	Withdrawals from the list	Net variation	in %
2000	1,785	278	123	155	9.5%
2001	1,908	299	176	123	6.9%
2002	1,941	222	189	33	1.7%
2003	1,870	175	246	-71	-3.7%
2004	1,968	202	104	98	5.2%
2005	2,060	266	174	92	4.7%
2006	2,238	345	167	178	8.6%
2007	2,868	824	194	630	28.2%
2008	3,371	712	209	503	17.5%
2009	3,463	408	316	92	2.7%
2010	3,667	471	267	204	5.9%

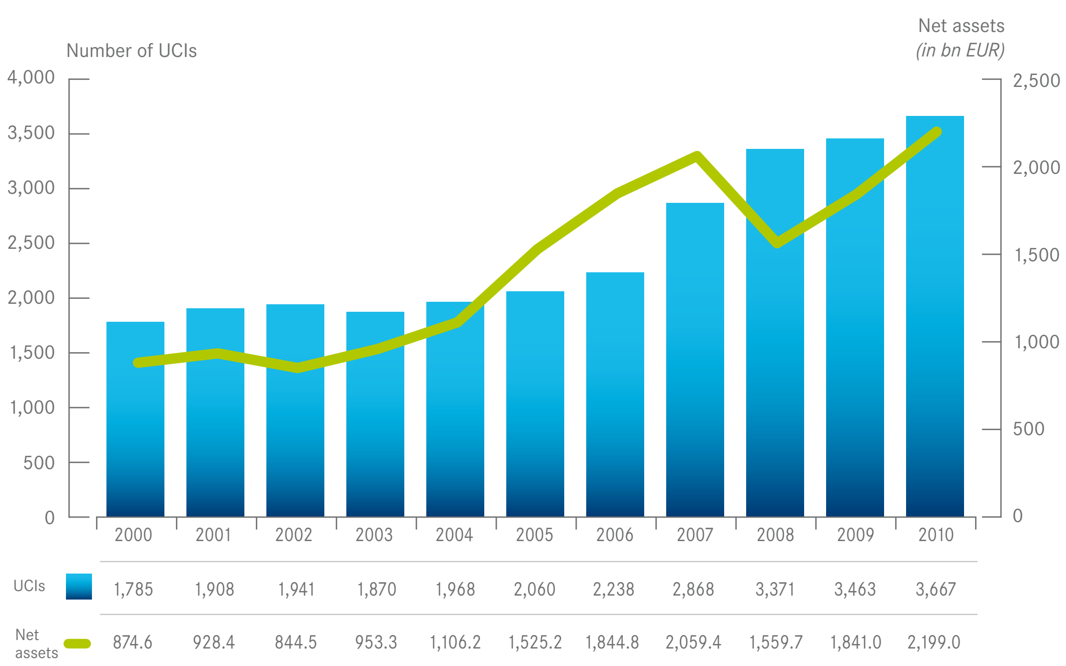
1.2.2. Development in the net assets of UCIs

The influx of new capital and the performance of the major financial stock markets resulted in the annual increase in Luxembourg UCIs' global assets of EUR 358.0 billion to reach EUR 2,199.0 billion as at 31 December 2010 (+19.4%). This growth originates partially from net subscriptions (45.1%) and partially from a positive stock market evolution (54.9%). Net capital investments in Luxembourg UCIs amounted to EUR 161.6 billion in 2010, which illustrates the investors' growing confidence in the markets.

Development in the net assets of UCIs

(in billion EUR)	Net assets	Net subscriptions	Net asset variation	in %	Average net assets per UCI
2000	874.6	168.1	140.1	19.1%	0.490
2001	928.4	121.7	53.8	6.2%	0.487
2002	844.5	57.3	-83.9	-9.0%	0.435
2003	953.3	82.6	108.8	12.9%	0.510
2004	1,106.2	113.7	152.9	16.0%	0.562
2005	1,525.2	236.3	419.0	37.9%	0.740
2006	1,844.8	241.3	319.6	21.0%	0.824
2007	2,059.4	188.5	214.6	11.6%	0.718
2008	1,559.7	-77.2	-499.7	-24.3%	0.463
2009	1,841.0	84.4	281.3	18.0%	0.532
2010	2,199.0	161.6	358.0	19.4%	0.600

Development in the number and net assets of UCIs



1.2.3. Development of UCI entities[1]

As at 31 December 2010, 2,302 out of 3,667 UCIs had adopted an umbrella structure. Given that the number of sub-funds rose from 10,877 to 11,572 (+6.4%) and that the traditionally structured UCIs increased from 1,355 to 1,365 (+0.7%), the total number of economic entities went up from 12,232 as at 31 December 2009 to a record level of 12,937 as at 31 December 2010, i.e. an increase of 5.8%.

Development of UCI entities

	Total number of UCIs	of which traditionally structured UCIs	*as % of total*	of which umbrella funds	*as % of total*	Number of sub-funds	*Average number of sub-funds per umbrella fund*	**Total number of entities**	Variation in %
2000	1,785	757	*42.4%*	1,028	*57.6%*	6,238	*6.07*	6,995	19.9%
2001	1,908	779	*40.8%*	1,129	*59.2%*	6,740	*5.97*	7,519	7.5%
2002	1,941	751	*38.7%*	1,190	*61.3%*	7,055	*5.93*	7,806	3.8%
2003	1,870	690	*36.9%*	1,180	*63.1%*	6,819	*5.78*	7,509	-3.8%
2004	1,968	742	*37.7%*	1,226	*62.3%*	7,134	*5.82*	7,876	4.9%
2005	2,060	762	*37.0%*	1,298	*63.0%*	7,735	*5.96*	8,497	7.9%
2006	2,238	851	*38.0%*	1,387	*62.0%*	8,622	*6.22*	9,473	11.5%
2007	2,868	1,180	*41.1%*	1,688	*58.9%*	9,935	*5.89*	11,115	17.3%
2008	3,371	1,352	*40.1%*	2,019	*59.9%*	10,973	*5.43*	12,325	10.9%
2009	3,463	1,355	*39.1%*	2,108	*60.9%*	10,877	*5.16*	12,232	-0.8%
2010	3,667	1,365	*37.2%*	2,302	*62.8%*	11,572	*5.03*	12,937	5.8%

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

1.2.4. Development of UCIs and of their net assets according to legal status and applicable law

The breakdown of UCIs between *fonds communs de placement* (FCP), *sociétés d'investissement à capital variable* (SICAV) and *sociétés d'investissement à capital fixe* (SICAF) reveals that as at 31 December 2010, FCPs were still the prevailing form with 1,944 entities out of a total of 3,667 active UCIs, against 1,701 entities operating as SICAVs and 22 as SICAFs.

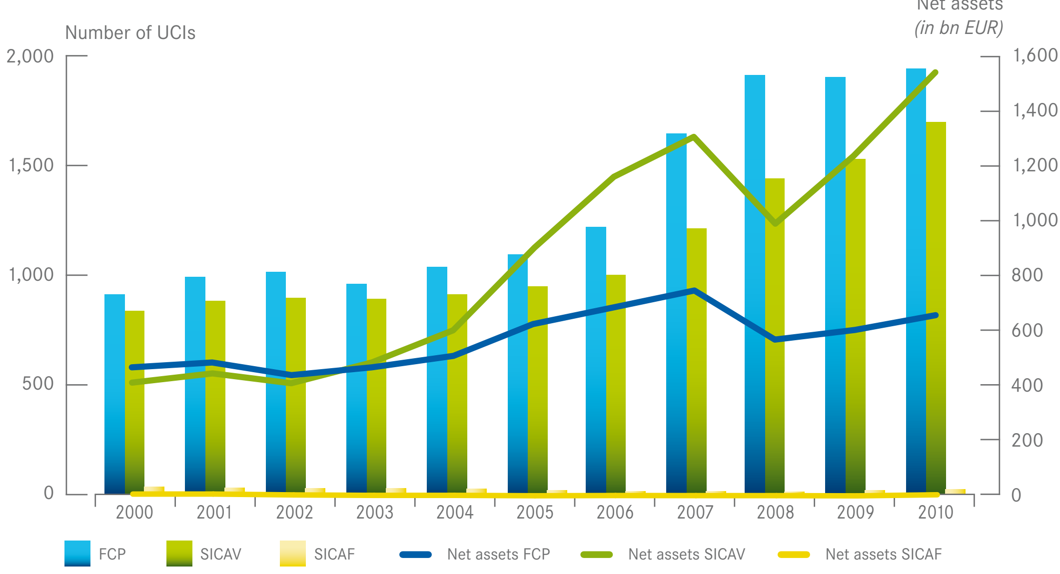
03

Breakdown of UCIs by legal status

	FCPs		SICAVs		SICAFs		Total	
	Number	Net assets (*in bn EUR*)	Number	Net assets (*in bn EUR*)	Number	Net assets (*in bn EUR*)	Number	Net assets (*in bn EUR*)
2000	914	462.8	840	404.0	31	7.8	1,785	874.6
2001	994	482.1	885	441.5	29	4.8	1,908	928.4
2002	1,017	435.8	896	405.5	28	3.2	1,941	844.5
2003	957	466.2	888	483.8	25	3.3	1,870	953.3
2004	1,036	504.0	913	600.3	19	1.9	1,968	1,106.2
2005	1,099	624.3	946	898.2	15	2.7	2,060	1,525.2
2006	1,224	681.3	1,000	1,161.1	14	2.4	2,238	1,844.8
2007	1,645	748.7	1,211	1,308.4	12	2.3	2,868	2,059.4
2008	1,910	567.2	1,443	990.9	18	1.6	3,371	1,559.7
2009	1,907	601.8	1,533	1,233.9	23	5.3	3,463	1,841.0
2010	1,944	652.2	1,701	1,540.1	22	6.7	3,667	2,199.0

At the end of 2010, FCPs' net assets reached EUR 652.2 billion, representing 29.7% of the total net assets of UCIs. SICAVs' net assets reached EUR 1,540.1 billion representing 70.0% of total net assets of UCIs. SICAFs' net assets amounted to EUR 6.7 billion as at 31 December 2010.

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



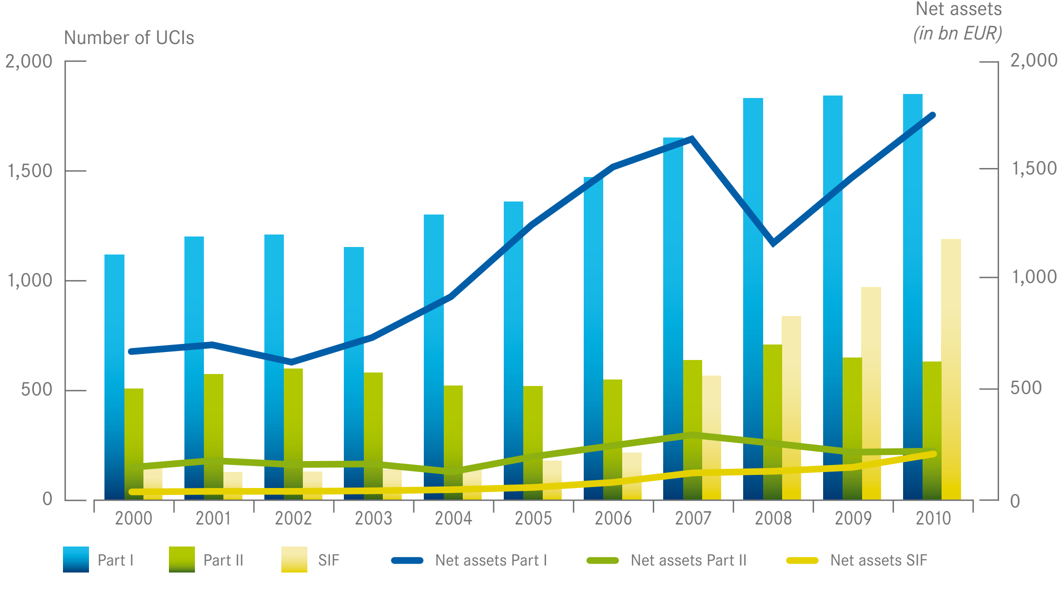
The following table illustrates the distribution of UCIs depending on whether they fall within the scope of Part I or II of the law of 20 December 2002 or of the law of 13 February 2007 relating to specialised investment funds (SIFs).

Breakdown of UCIs according to Parts I and II of the 2002 law and specialised investment funds

	Part I		Part II		SIFs	
	Number	*Net assets (in bn EUR)*	Number	*Net assets (in bn EUR)*	Number	*Net assets (in bn EUR)*
2000	1,119	682.0	513	153.3	153	39.3
2001	1,196	708.6	577	178.2	135	41.6
2002	1,206	628.9	602	171.6	133	44.0
2003	1,149	741.1	583	169.3	138	42.9
2004	1,303	929.3	516	131.2	149	45.7
2005	1,358	1,260.0	524	204.0	178	61.2
2006	1,469	1,516.5	552	249.9	217	78.4
2007	1,653	1,646.4	643	295.9	572	117.1
2008	1,826	1,169.4	708	259.8	837	130.5
2009	1,843	1,465.7	649	221.2	971	154.1
2010	1,846	1,762.7	629	222.2	1,192	214.1

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

Breakdown of UCIs according to Parts I and II of the 2002 law and specialised investment funds



50.3% of UCIs registered on the official list as at 31 December 2010 were UCITS governed by Part I of the 2002 law and 17.2% were other UCIs governed by Part II (non-coordinated UCIs). Specialised investment funds represented 32.5% of the 3,667 Luxembourg UCIs. Net assets were distributed at the same date as follows: 80.2% for UCIs under Part I, 10.1% for UCIs set up under Part II and 9.7% for specialised investment funds.

The following table compares the development in 2010 of the number of UCIs and net assets according to both the legal status and the scope of the laws.

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

	2009				2010				Variation 2009/2010			
Number of UCIs	FCPs	SICAVs	SICAFs	Total	FCPs	SICAVs	SICAFs	Total	FCPs	SICAVs	SICAFs	Total
Part I	1,185	658	0	1,843	1,161	685	0	1,846	-2.03%	4.10%	0.00%	0.16%
Part II	287	355	7	649	286	337	6	629	-0.35%	-5.07%	-14.29%	-3.08%
SIFs	435	520	16	971	497	679	16	1,192	14.25%	30.58%	0.00%	22.76%
Total	**1,907**	**1,533**	**23**	**3,463**	**1,944**	**1,701**	**22**	**3,667**	**1.94%**	**10.96%**	**-4.35%**	**5.89%**
Net assets *(in bn EUR)*	FCPs	SICAVs	SICAFs	Total	FCPs	SICAVs	SICAFs	Total	FCPs	SICAVs	SICAFs	Total
Part I	446.80	1,018.94	0.00	1,465.74	472.60	1,290.06	0.00	1,762.66	5.78%	26.61%	0.00%	20.26%
Part II	80.51	139.80	0.89	221.20	83.67	137.53	0.98	222.18	3.92%	-1.63%	10.20%	0.44%
SIFs	74.48	75.19	4.38	154.05	95.89	112.52	5.74	214.15	28.74%	49.65%	31.15%	39.02%
Total	**601.79**	**1,233.93**	**5.27**	**1,840.99**	**652.16**	**1,540.11**	**6.72**	**2,198.99**	**8.37%**	**24.81%**	**27.60%**	**19.45%**

As regards Part I, a slight increase of 0.2% in the number of UCIs can be noted compared to 2009 and an increase of 20.3% in net assets whereas the number of UCIs under Part II decreased by 3.1% and their net assets rose by 0.4%. The number of specialised investment funds increased by 22.8% and their net assets increased by 39.0%.

1.2.5. Net subscriptions

In 2010, UCIs under Part I of the law of 2002 showed important net subscriptions totalling EUR 128.229 billion. However, UCIs under Part II of the law of 2002 showed net redemptions totalling EUR 14.153 billion. Net subscriptions in specialised investment funds amounted to EUR 47.492 billion.

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

(in million EUR)	FCPs	SICAVs	SICAFs	Total	in %
Part I	-7,466	135,695	0	128,229	79.4%
Part II	-2,958	-11,269	74	-14,153	-8.8%
SIFs	18,757	27,969	766	47,492	29.4%
Total	**8,333**	**152,395**	**840**	**161,568**	**100.0%**

1.3. Valuation currencies used

As regards the valuation currencies used, most entities (8,861 out of a total of 12,937) are denominated in Euro, followed by those in US dollars (2,789) and those in Swiss francs (339). In terms of net assets, the entities denominated in Euro encompass EUR 1,222.251 billion of a total of EUR 2,198.994 billion, ahead of entities expressed in US dollars (EUR 797.597 billion) and Swiss francs (EUR 52.512 billion).

1.4. UCIs' investment policy

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

Net assets and entities of UCIs according to their investment policy

	2009		2010		Variation in %	
	Number of entities	Net assets *(in bn EUR)*	Number of entities	Net assets *(in bn EUR)*	Number of entities	Net assets
Fixed-income transferable securities	3,157	801.826	3,222	913.311[2]	2.06%	13.90%
Variable-yield transferable securities	3,502	544.113	3,507	689.109[3]	0.14%	26.65%
Mixed transferable securities	3,076	296.444	3,586	376.898[4]	16.58%	27.14%
Fund of funds	1,947	141.254	2,010	160.702[5]	3.24%	13.77%
Cash	159	14.511	140	7.840	-11.95%	-45.97%
Real estate	150	18.965	179	21.426	19.33%	12.98%
Futures, options, warrants	147	19.372	167	21.741	13.61%	12.23%
Other assets	94	4.508	126	7.967[6]	34.04%	76.73%
Total	**12,232**	**1,840.993**	**12,937**	**2,198.994**	**5.76%**	**19.45%**

Most UCI categories and in particular those investing in variable-yield transferable securities benefited from the general increase in stock markets. However, UCI categories investing in money market instruments and in liquidities suffered from weak money market rates which lead to the closure of some entities and to net redemptions. It can be assumed that the investors left this sector in order to invest in categories with higher yield.

Investment policy of UCIs according to Parts I and II of the 2002 law and specialised investment funds

Situation as at 31 december 2010	**Number of entities**	**Net assets** *(in bn EUR)*	**Net assets** *(in %)*
UCITS subject to Part I			
Fixed-income transferable securities[7]	2,283	796.039	36.2%
Variable-yield transferable securities	3,001	630.405	28.7%
Mixed transferable securities	2,319	277.247	12.6%
Fund of funds	655	47.904	2.2%
Cash	32	1.436	0.1%
Futures and/or options	55	7.603	0.3%
Other assets	16	2.032	0.1%
UCITS subject to Part II[8]			
Fixed-income transferable securities[9]	410	67.070	3.0%
Variable-yield transferable securities	165	20.284	0.9%
Mixed transferable securities	487	33.988	1.5%
Fund of funds	801	75.993	3.5%
Cash	84	6.084	0.3%

(...next page)

[2] Including EUR 284.851 billion in money market instruments and other short-term securities.
[3] Including EUR 5.809 billion in non-listed securities and EUR 0.223 billion in venture capital.
[4] Including EUR 2.525 billion in non-listed securities and EUR 0.379 billion in venture capital.
[5] Including EUR 0.255 billion in non-listed securities and EUR 0.002 billion in venture capital.
[6] Including EUR 0.082 billion in venture capital.
[7] Including EUR 244.626 billion in money market instruments and other short-term securities (237 entities).
[8] UCITS excluded from Part I of the law of 20 December 2002, pursuant to Article 3, points 1 to 3, i.e. UCITS closed for redemptions, not promoted in the EU or only sold to individuals in countries outside the EU.
[9] Including EUR 35.869 billion in money market instruments and other short-term securities (107 entities).

Situation as at 31 december 2010	Number of entities	Net assets *(in bn EUR)*	Net assets *(in %)*
UCITS subject to Part II [10]			
Non-listed transferable securities	23	3.055	0.1%
Venture capital	8	0.225	0.0%
Other UCIs subject to Part II			
Real estate	13	3.846	0.2%
Futures and/or options	63	10.832	0.5%
Other assets	15	0.801	0.0%
Specialised investment funds			
Fixed-income transferable securities [11]	529	50.202	2.3%
Variable-yield transferable securities	285	32.388	1.5%
Mixed transferable securities	736	62.759	2.9%
Non-listed transferable securities	62	5.534	0.3%
Fund of funds	545	36.548	1.7%
Cash	24	0.320	0.0%
Venture capital	17	0.461	0.0%
Real estate	166	17.580	0.8%
Futures and/or options	49	3.306	0.1%
Other assets	94	5.052	0.2%
Total	**12,937**	**2,198.994**	**100.0%**

The following table illustrates, per quarter, the flow of subscriptions and redemptions during 2010 divided into the main investment policies:

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

in million EUR

	1st quarter 2010			2nd quarter 2010			3rd quarter 2010			4th quarter 2010			Totals		
Pol.	subscr.	red.	n. iss.	subscr.	red.	n. iss.	subscr.	red.	n. iss.	subscr.	red.	n. iss.	subscr.	red.	n. iss.
1	86,177	71,303	14,874	80,569	84,569	-4,000	73,801	70,674	3,127	105,077	82,601	22,476	345,624	309,147	36,477
2	95,759	64,891	30,868	99,789	82,744	17,045	107,875	74,486	33,389	90,565	81,844	8,721	393,988	303,965	90,023
3	38,316	28,240	10,076	41,119	35,460	5,659	33,381	25,973	7,408	46,518	35,798	10,720	159,334	125,471	33,863
4	253,944	270,388	-16,444	286,902	299,117	-12,215	260,587	260,839	-252	265,737	280,542	-14,805	1,067,170	1,110,886	-43,716
5	35,666	21,030	14,636	38,428	27,188	11,240	26,734	20,527	6,207	39,703	26,865	12,838	140,531	95,610	44,921
Total	**509,862**	**455,852**	**54,010**	**546,807**	**529,078**	**17,729**	**502,378**	**452,499**	**49,879**	**547,600**	**507,650**	**39,950**	**2,106,647**	**1,945,079**	**161,568**

1.5. Development of several specific categories of UCIs

1.5.1. Guarantee-type UCIs

Guarantee-type UCIs aim to offer investors some security given the fluctuations inherent in financial markets. According to the investment policy pursued by the funds concerned, the guarantee ensures that the investor is reimbursed either a proportion of the invested capital or is fully reimbursed his initial investment or even receives a return on his investment at the end of one or several pre-determined periods.

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

[11] Including EUR 4.356 billion in money market instruments and other short-term securities (15 entities).

In 2010, the number of guarantee-type UCIs fell from 194 to 192 and the number of entities from 409 to 400. In terms of entities, the fall is attributable to the launch of 40 new entities, while the given guarantee came to maturity or was not extended for 49 entities.

As at 31 December 2010, the 400 entities comprised 41 entities guaranteeing investors only a proportion of the invested capital, 186 entities guaranteeing repayment in full of the invested capital (money-back guarantee) and 173 entities offering their investors a return in addition to the initial subscription price.

UCIs guaranteeing repayment in full of the initial investment are now dominant, overtaking UCIs guaranteeing a return on investment, the latter having held the top position during the previous years.

Net assets of guarantee-type UCIs decreased by EUR 3.84 billion to EUR 41.99 billion in 2010, i.e. a decrease of 8.4%. It is also worth noting that guarantee-type UCIs set up by German promoters alone accounted for 90.1% of the total net assets of guarantee-type UCIs.

Development in guarantee-type UCIs

	Number of UCIs	**Number of economic entities**	**Net assets** *(in bn EUR)*
2000	79	119	14.30
2001	74	115	17.09
2002	75	151	17.40
2003	76	166	20.89
2004	90	207	21.41
2005	104	248	24.69
2006	121	297	32.56
2007	154	360	43.73
2008	176	382	44.83
2009	194	409	45.83
2010	192	400	41.99

1.5.2. Real estate UCIs

In 2010, net assets of UCIs principally investing in real estate increased by 13.0%. This increase in net assets can be explained by a growth in the value of the real estate assets held by UCIs.

In 2010, SIFs remained the preferred vehicle for real estate investments.

Development of real estate UCIs

Year	**Number of entities**	of which active entities	of which Part II	of which SIFs	**Net subscriptions** *(in bn EUR)*	**Net assets** *(in bn EUR)*
2005	52	41	16	36	1.591	5.287
2006	76	64	22	54	2.653	8.057
2007	104	80	21	83	6.497	15.446
2008	137	111	16	121	7.126	20.926
2009	150	125	15	135	1.977	18.965
2010	179	149	13	166	0.042	21.426

1.5.3. Sharia UCIs

The number of Sharia UCIs and entities remained stable during 2010. Their net assets nevertheless increased by 53.4%.

Development of UCIs underlying Sharia law

	Number of Sharia entities	Net assets *(in mn EUR)*
2005	7	74.5
2006	8	93.6
2007	9	202.2
2008	22	212.8
2009	23	308.3
2010	24	472.8

1.5.4. Microfinance UCIs

In 2010, the growth of UCIs investing in microfinance significantly slowed down compared to the two previous years during which their number and net assets almost doubled. Their net assets increased by 15.6% in 2010.

Development of UCIs in the microfinance sector

	Number of microfinance entities	Net assets *(in mn EUR)*
2005	3	104.8
2006	11	505.3
2007	15	771.1
2008	18	1,200.3
2009	29	1,675.7
2010	32	1,937.8

1.6. Promoters of Luxembourg UCIs

The breakdown of Luxembourg UCIs according to the geographic origin of their promoters highlights the multitude of countries represented in the financial centre. Promoters of Luxembourg UCIs are spread over 57 countries.

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

Origin of the promoters of Luxembourg UCIs

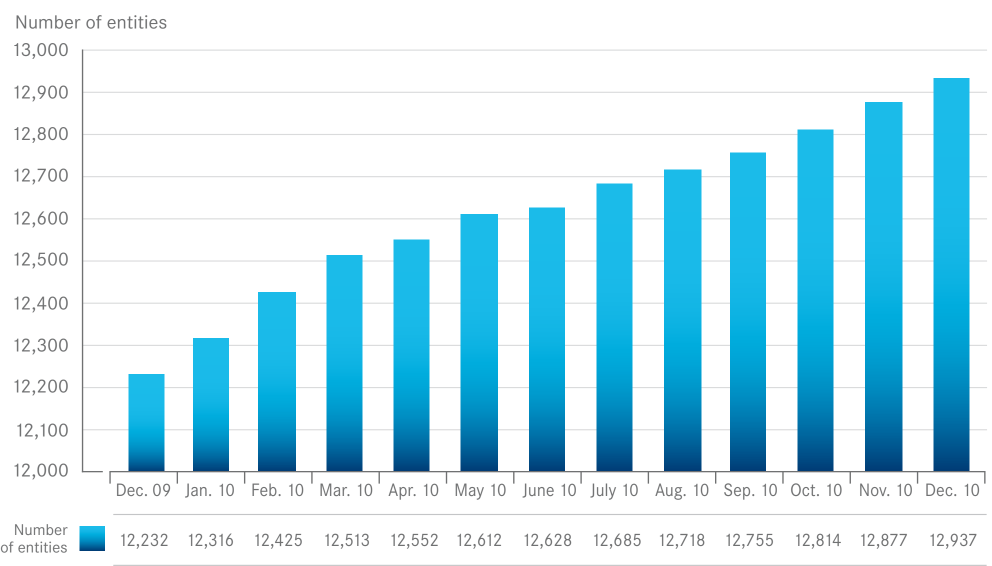
Situation as at 31 December 2010	Net assets *(in bn EUR)*	in %	Number of UCIs	in %	Number of entities	in %
United States	496.493	22.6%	142	3.9%	869	6.7%
Germany	380.824	17.3%	1,596	43.5%	2,971	23.0%
Switzerland	335.603	15.3%	473	12.9%	2,390	18.5%
Great Britain	307.578	14.0%	233	6.4%	1,235	9.6%
France	180.308	8.2%	243	6.6%	1,234	9.5%
Italy	174.730	7.9%	137	3.7%	950	7.3%
Belgium	117.336	5.3%	173	4.7%	1,446	11.2%
Netherlands	44.063	2.0%	57	1.6%	224	1.7%
Sweden	36.613	1.7%	107	2.9%	272	2.1%
Luxembourg	32.246	1.5%	144	3.9%	333	2.6%
Others	93.200	4.2%	362	9.9%	1,013	7.8%
Total	**2,198.994**	**100.0%**	**3,667**	**100.0%**	**12,937**	**100.0%**

1.7. Developments of UCI entities in 2010

1.7.1. General situation

In 2010, the number of entities continuously grew, resulting in an increase of 705 entities by the end of the year.

Monthly development of the number of entities



1.7.2. Entities approved in 2010

In 2010, 2,362 new entities were authorised. In absolute terms, this figure represents an increase of 363 entities compared to 2009, i.e. a growth of 18.2%. 1,343 out of the 2,362 entities approved in 2010, representing 56.9%, have been launched in the same year.

	2005	2006	2007	2008	2009	2010
Newly approved entities	1,806	2,119	2,878	3,361	1,999	2,362
of which launched in the same year	*1,022*	*1,263*	*1,916*	*2,008*	*1,068*	*1,343*
In %	56.6%	59.6%	66.6%	59.7%	53.4%	56.9%

The breakdown by investment policy shows that almost 40% of the entities authorised in 2010 chose to invest in mixed transferable securities.

Investment policy of UCIs approved in 2010

Investment policy	2009		2010	
	Number of entities	As a % of total	Number of entities	As a % of total
Fixed-income transferable securities (excluding money market instruments and other short-term securities)	521	26.07%	455	19.26%
Variable-yield transferable securities	360	18.01%	464	19.65%
Mixed transferable securities	622	31.11%	944	39.97%
Fund of funds	289	14.46%	314	13.29%
Cash, money market instruments and other short-term securities	70	3.50%	48	2.03%
Futures, options, warrants (derivative instruments)	31	1.55%	53	2.24%
Real estate	33	1.65%	47	1.99%
Other assets	73	3.65%	37	1.57%
Total	**1,999**	**100.00%**	**2,362**	**100.00%**

1.7.3. Entities closed in 2010

1,124 entities closed in 2010, which was less than the number of entities closed in the previous year (-418 entities or -27.11%).

	2004	2005	2006	2007	2008	2009	2010
Liquidated entities	393	426	412	424	752	968	633
Matured entities	64	70	45	83	84	92	111
Merged entities	237	202	223	282	485	482	380
Total	**694**	**698**	**680**	**789**	**1,321**	**1,542**	**1,124**

The breakdown by investment policy shows that the closed entities having invested in variable-yield transferable securities account for the largest proportion of entities closed in 2010.

Investment policy of UCIs closed in 2010

Investment policy	2009		2010	
	Number of entities	As a % of total	Number of entities	As a % of total
Fixed-income transferable securities (excluding money market instruments and other short-term securities)	344	22.31%	252	22.42%
Variable-yield transferable securities	463	30.03%	321	28.56%
Mixed transferable securities	354	22.96%	244	21.71%
Fund of funds	274	17.77%	213	18.95%
Cash, money market instruments and other short-term securities	71	4.60%	68	6.05%
Futures, options, warrants (derivative instruments)	25	1.62%	11	0.98%
Real estate	3	0.19%	8	0.71%
Other assets	8	0.52%	7	0.62%
Total	**1,542**	**100.00%**	**1,124**	**100.00%**

2. PERFORMANCE ANALYSIS OF THE MAJOR LUXEMBOURG UCI CATEGORIES IN 2010

2.1. Objectives and methodology

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

The UCI categories selected are the following:

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

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

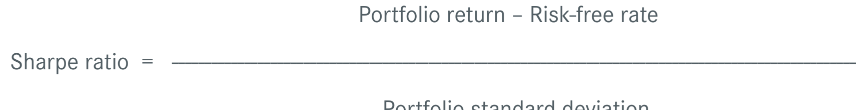
The category "European bonds" only takes entities investing in standard European bonds into account. Entities investing in High Yield bonds have not been considered.

For the interpretation of the results, it is important to highlight that past performances are not an indication for future performances.

Methodological aspects:

- Base currency: to measure the performance of the various UCI categories, the Euro has been used as base currency.
- Population considered: the population considered is composed of a total of EUR 500.546 billion net assets and 1,686 entities. The entities with no performance in all twelve months of 2010 have not been taken into consideration.
- The average return and the average standard deviation per UCI category have been calculated with the weighting of the entities' average net assets.
- To compare the performances of the various investment policies, a risk-performance indicator is applied, i.e. the Sharpe ratio.

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



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

  The 12-month money market rate applicable beginning of January 2010, i.e. 1.25%, has been used as risk-free rate.

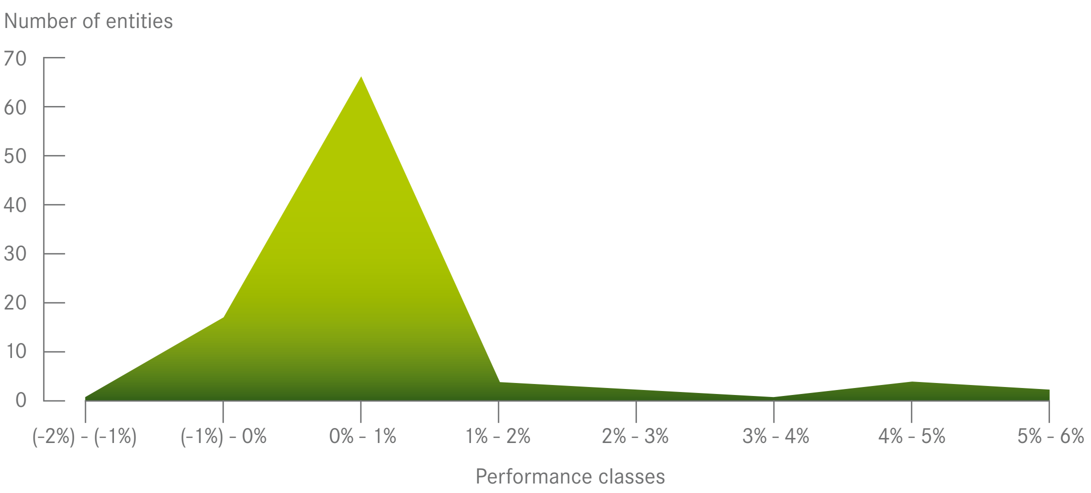
- For the maximum performance calculation of a UCI category, the average of the three UCIs with the highest performance classes has been used and for the minimum performance calculation of a UCI category, the average of the three UCIs with the lowest performance classes has been considered.
- Source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

2.2. Performance of the major Luxembourg UCI categories in 2010

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

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

Performance of entities investing in Euro money market instruments in 2010



The average performance realised in 2010 by entities whose investment policy consists in investing in Euro money market instruments was 0.50%. The average performance of the maximum return class was 5.01% whereas the average performance of the minimum return class was -1.03%. The standard deviation of these entities was 1.21%.

Central values and dispersion characteristics

Average performance	0.50%
Maximum performance	5.01%
Minimum performance	-1.03%
Standard deviation of performance	1.21%
Performance spread	6.05%
Statistical population	97

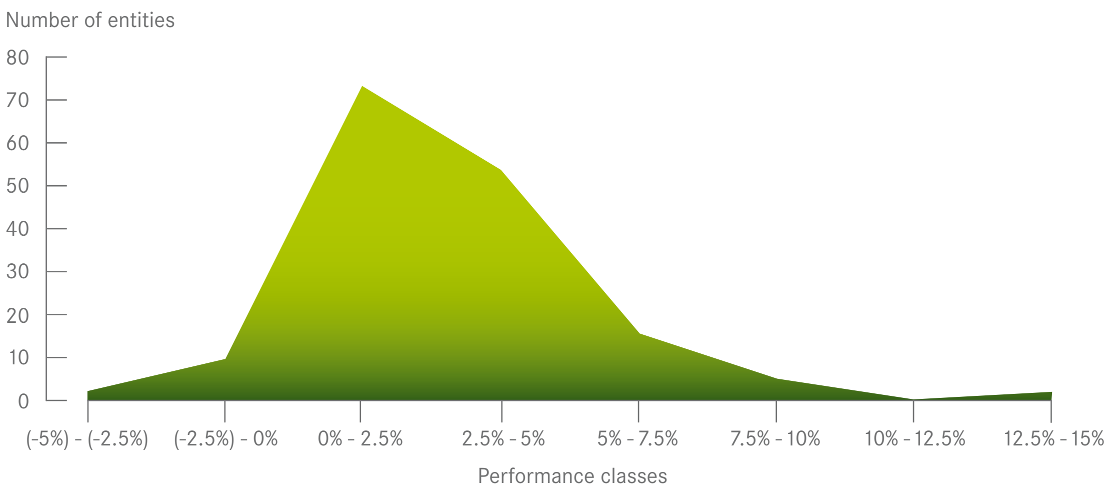
Statistical performance distribution of entities investing in money market instruments

Performance	**Number of entities**			
Return classes	Absolute frequency	Relative frequency	Cumulative absolute frequency	Cumulative relative frequency
-2% to -1%	1	1.03%	1	1.03%
-1% to 0%	17	17.53%	18	18.56%
0% to 1%	66	68.04%	84	86.60%
1% to 2%	4	4.12%	88	90.72%
2% to 3%	2	2.06%	90	92.78%
3% to 4%	1	1.03%	91	93.81%
4% to 5%	4	4.12%	95	97.94%
5% to 6%	2	2.06%	97	100.00%
Total	97	100.00%		

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

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

Performance of entities investing in EUR-denominated bonds in 2010



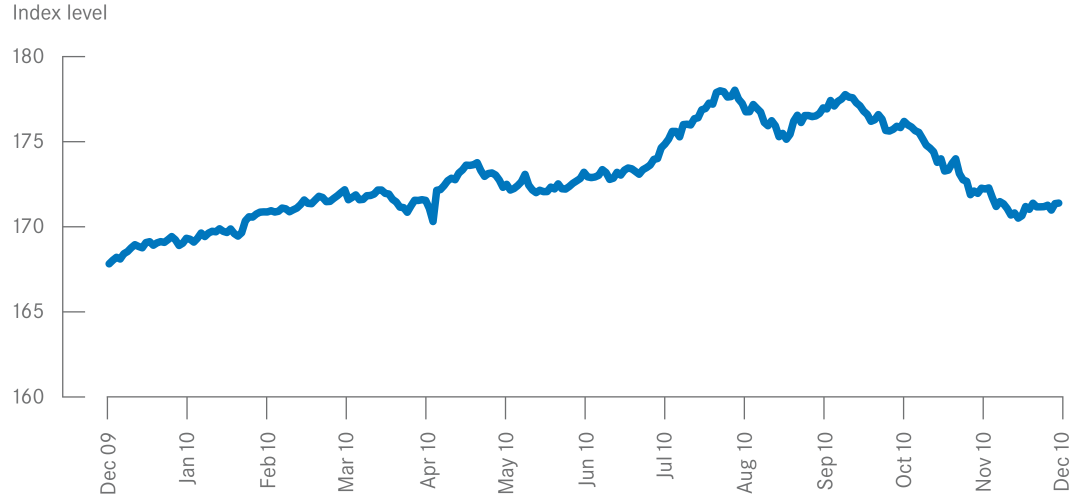
The average performance realised in 2010 by entities whose investment policy consists in investing in EUR-denominated bonds was 2.78%. The average performance of the maximum return class was 12.74% whereas the average performance of the minimum return class was -3.01%. The standard deviation of the performance of these entities was 2.68%.

Statistical performance distribution of entities investing in EUR-denominated bonds

Performance	Number of entities			
Return classes	Absolute frequency	Relative frequency	Cumulative absolute frequency	Cumulative relative frequency
-5% to -2.5%	2	1.23%	2	1.23%
-2.5% to 0%	10	6.17%	12	7.41%
0% to 2.5%	73	45.06%	85	52.47%
2.5% to 5%	54	33.33%	139	85.80%
5% to 7.5%	16	9.88%	155	95.68%
7.5% to 10%	5	3.09%	160	98.77%
10% to 12.5%	0	0.00%	160	98.77%
12.5% to 15%	2	1.23%	162	100.00%
Total	**162**	**100.00%**		

The JPMorgan Euro denominated Aggregate: Credit + Pfandbriefe + EMU Local Index Level Euro index realised a performance of 2.13% in 2010. 86 entities investing in European bonds, i.e. 53.09% of all entities, realised a higher performance than the index cited. The market volatility of European bonds was 2.83% in 2010 (source: JPMorgan, calculation: CSSF).

JPMorgan Euro denominated Aggregate: Credit + Pfandbriefe + EMU Local Index Level Euro 2010



Source : JPMorgan

Interpretation of the Sharpe ratio

In 2010, UCIs investing in EUR-denominated bonds realised on average a return of 0.38% per unit of risk considered. As regards the performance of the maximum return class, a positive return of on average 1.56% per unit of risk was observed. The performance of the minimum return class exhibited on average a negative return of -0.79% per unit of risk considered.

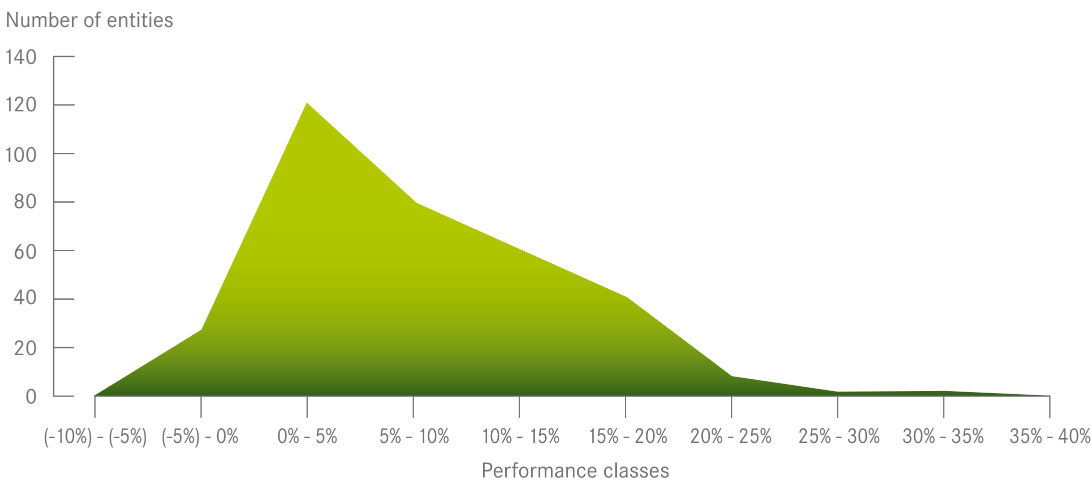
Risk and return summary table for entities investing in EUR-denominated bonds

Average performance	2.78%
Maximum performance	12.74%
Minimum performance	-3.01%
Standard deviation of performance	2.68%
Performance spread	15.75%
Statistical population	162
Performance of the index JPMorgan Euro denominated Aggregate: Credit + Pfandbriefe + EMU Local Index Level Euro	2.13%
Market volatility	2.83%
Number of entities with higher performance than JPMorgan Euro denominated Aggregate: Credit + Pfandbriefe + EMU Local Index Level Euro	86
Sharpe ratio – average performance	0.38%
Sharpe ratio – maximum performance	1.56%
Sharpe ratio – minimum performance	-0.79%

2.2.3. Entities whose investment policy consists in investing in global bonds

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

Performance of entities investing in global bonds in 2010



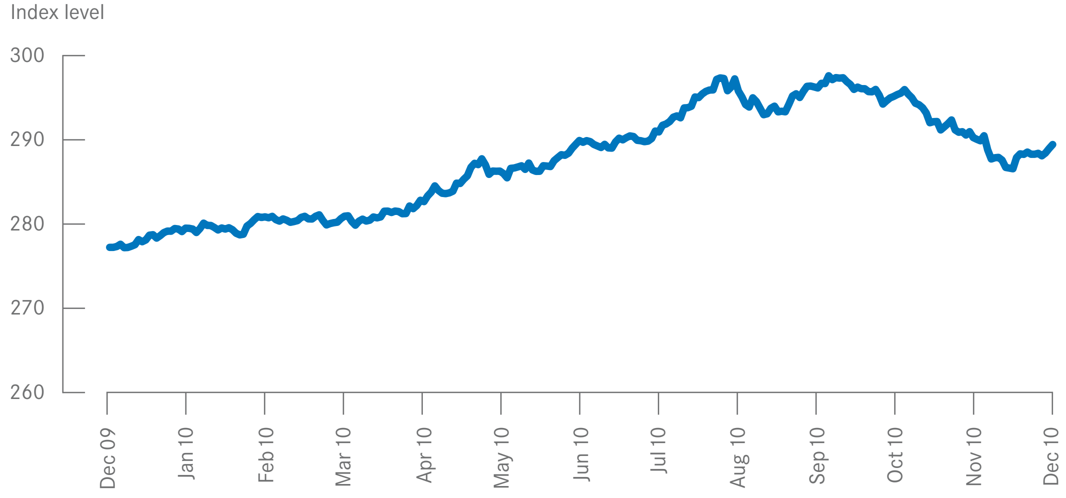
The average performance realised in 2010 by entities whose investment policy consists in investing in global bonds was 9.22%. The average performance of the maximum return class was 32.62% whereas the average performance of the minimum return class was -4.75%. The standard deviation of the performance of these entities was 6.64%.

Statistical performance distribution of entities investing in global bonds

Performance	Number of entities			
Return classes	Absolute frequency	Relative frequency	Cumulative absolute frequency	Cumulative relative frequency
-10% to -5%	1	0.29%	1	0.29%
-5% to 0%	27	7.87%	28	8.16%
0% to 5%	121	35.28%	149	43.44%
5% to 10%	81	23.62%	230	67.06%
10% to 15%	59	17.20%	289	84.26%
15% to 20%	41	11.95%	330	96.21%
20% to 25%	9	2.62%	339	98.83%
25% to 30%	1	0.29%	340	99.13%
30% to 35%	2	0.58%	342	99.71%
35% to 40%	1	0.29%	343	100.00%
Total	**343**	**100.00%**		

The JPMorgan GBI Global Traded Index Hedged Index Level Euro index realised a performance of 4.31% in 2010. 215 entities investing in global bonds, i.e. 62.68% of all entities, realised a higher performance than the index cited. The market volatility for global bonds was 2.67% (source: JPMorgan, calculation: CSSF).

JPMorgan GBI Global Traded Index Hedged Index Level Euro 2010



Source: JPMorgan

Interpretation of the Sharpe ratio

UCIs investing in global bonds realised in 2010 on average a positive return of 1.28% per unit of risk considered. As regards the performance of the maximum return class, a positive return of on average 1.39% per unit of risk was observed. The performance of the minimum return class exhibited on average a negative return of -0.46% per unit of risk considered.

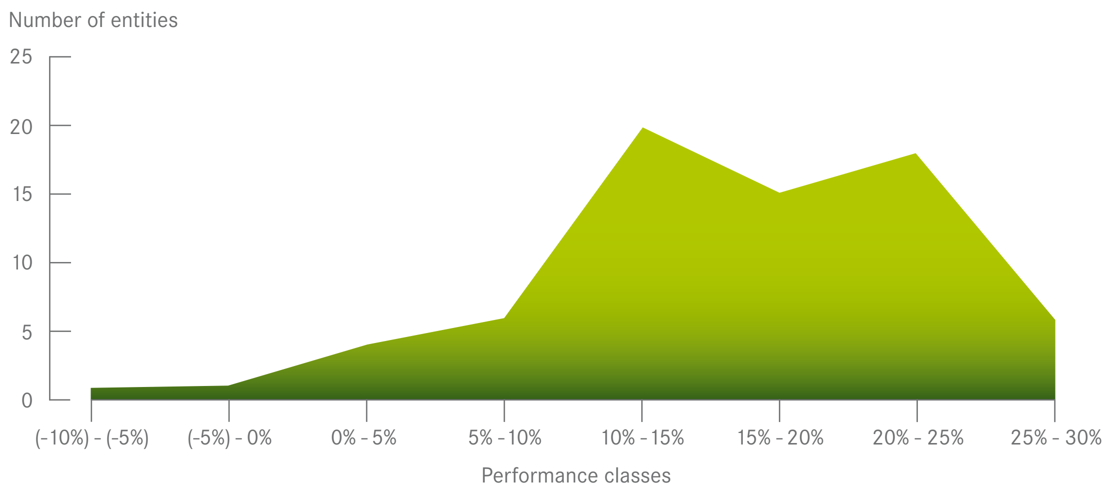
Risk and return summary table for entities investing in global bonds

Average performance	9.22%
Maximum performance	32.62%
Minimum performance	-4.75%
Standard deviation of performance	6.64%
Performance spread	37.37%
Statistical population	343
Performance of the index JPMorgan GBI Global Traded Index Hedged Index Level Euro	4.31%
Market volatility	2.67%
Number of entities with higher performance than the index JPMorgan GBI Global Traded Index Hedged Index Level Euro	215
Sharpe ratio – average performance	1.28%
Sharpe ratio – maximum performance	1.39%
Sharpe ratio – minimum performance	-0.46%

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

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

Performance of entities investing in emerging market bonds in 2010



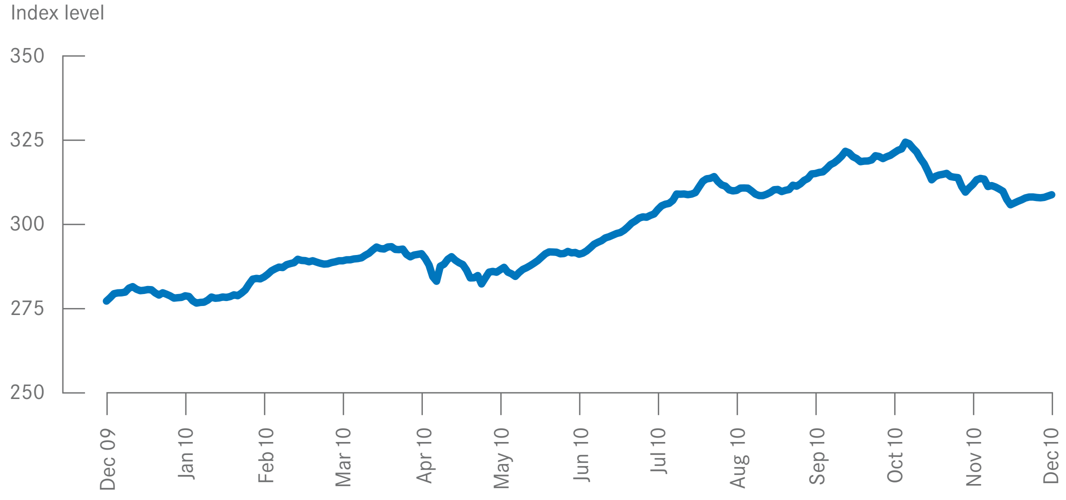
The average performance realised in 2010 by entities whose investment policy consists in investing in emerging market bonds was 15.97%. The average performance of the maximum return class was 29.45% whereas the average performance of the minimum return class was -1.56%. The standard deviation of the performance of these entities was 7.31%.

Statistical performance distribution of entities investing in emerging market bonds

Performance	**Number of entities**			
Return classes	Absolute frequency	Relative frequency	Cumulative absolute frequency	Cumulative relative frequency
-10% to -5%	1	1.41%	1	1.41%
-5% to 0%	1	1.41%	2	2.82%
0% to 5%	4	5.63%	6	8.45%
5% to 10%	6	8.45%	12	16.90%
10% to 15%	20	28.17%	32	45.07%
15% to 20%	15	21.13%	47	66.20%
20% to 25%	18	25.35%	65	91.55%
25% to 30%	6	8.45%	71	100.00%
Total	**71**	**100.00%**		

The JPMorgan EMBI Global - EUR Hedged Index Levels index realised a performance of 11.39% in 2010. 53 entities investing in emerging market bonds, i.e. 74.65% of all entities, realised a higher performance than the index cited. The market volatility for emerging market bonds was 4.91% (source: JPMorgan, calculation: CSSF).

JPMorgan EMBI Global - EUR Hedged Index Levels 2010



Source : JPMorgan

Interpretation of the Sharpe ratio

UCIs investing in emerging market bonds realised in 2010 on average a return of 1.76% per unit of risk considered. As regards the performance of the maximum return class, a positive return of on average 3.06% per unit of risk was observed. The performance of the minimum return class exhibited on average a slightly negative return of -0.30% per unit of risk considered.

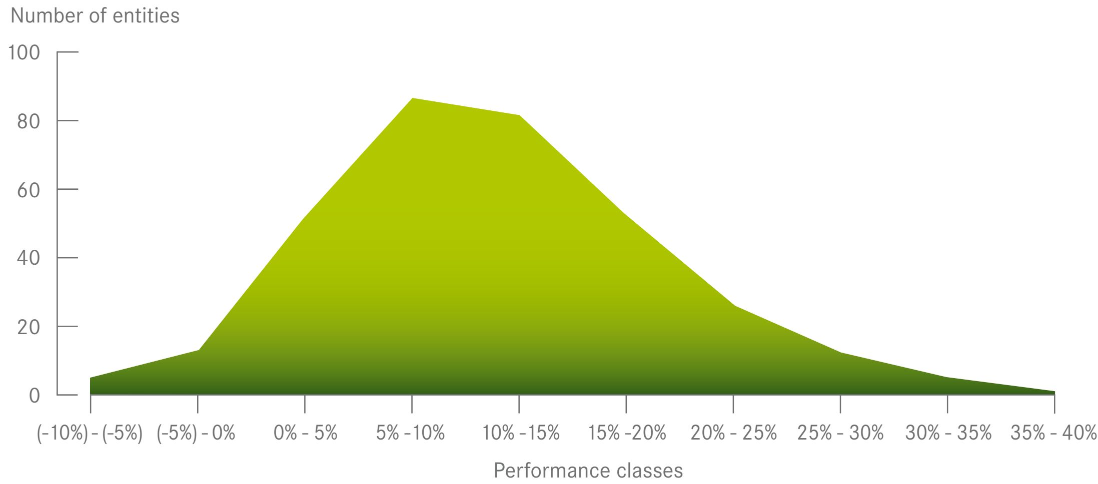
Risk and return summary table for entities investing in emerging market bonds

Average performance	15.97%
Maximum performance	29.45%
Minimum performance	-1.56%
Standard deviation of performance	7.31%
Performance spread	31.01%
Statistical population	71
Performance of the index JPMorgan EMBI Global - EUR Hedged Index Levels	11.39%
Market volatility	4.91%
Number of entities with higher performance than the index JPMorgan EMBI Global - EUR Hedged Index Levels	53
Sharpe ratio – average performance	1.76%
Sharpe ratio – maximum performance	3.06%
Sharpe ratio – minimum performance	-0.30%

2.2.5. Entities whose investment policy consists in investing in European equities

The following graph illustrates the performance distribution of entities whose investment policy consists in investing in European equities. It is reminded that entities investing in European Smallcap shares are not included in this category.

Performance of entities investing in European equities in 2010



The average performance realised in 2010 by entities whose investment policy consists in investing in European equities was 12.91%. The average performance of the maximum return class was 33.11% whereas the average performance of the minimum return class was -7.88%. The standard deviation of the performance of these entities was 7.77%.

Statistical performance distribution of entities investing in European equities

Performance	**Number of entities**			
Return classes	Absolute frequency	Relative frequency	Cumulative absolute frequency	Cumulative relative frequency
-10% to -5%	5	1.49%	5	1.49%
-5% to 0%	13	3.88%	18	5.37%
0% to 5%	52	15.52%	70	20.90%
5% to 10%	87	25.97%	157	46.87%
10% to 15%	82	24.48%	239	71.34%
15% to 20%	52	15.52%	291	86.87%
20% to 25%	26	7.76%	317	94.63%
25% to 30%	12	3.58%	329	98.21%
30% to 35%	5	1.49%	334	99.70%
35% to 40%	1	0.30%	335	100.00%
Total	**335**	**100.00%**		

The MSCI EUROPE Standard (Large + Mid Cap) (EUR) index, which includes dividends, realised a performance of 11.01% in 2010. 158 entities investing in European equities, i.e. 46.87% of all entities, realised a higher performance than the index cited. The market volatility for European equities was 17.98% (source: MSCI Barra, calculation: CSSF).

MSCI EUROPE Standard (Large + Mid Cap) (EUR) 2010

Source : MSCI Barra[12]

Interpretation of the Sharpe ratio

The UCI entities investing in European equities realised in 2010 on average a positive return of 0.88% per unit of risk considered. As regards the performance of the maximum return class, a positive return of on average 2.70% per unit of risk was observed. The performance of the minimum return class exhibited on average a slightly negative return of -0.64% per unit of risk considered.

Risk and return summary table for entities investing in European equities

Average performance	12.91%
Maximum performance	33.11%
Minimum performance	-7.88%
Standard deviation of performance	7.77%
Performance spread	40.99%
Statistical population	335
Performance of the index MSCI EUROPE Standard (Large + Mid Cap) (EUR)	11.01%
Market volatility	17.98%
Number of entities with higher performance than the index MSCI EUROPE Standard (Large + Mid Cap) (EUR)	158
Sharpe ratio – average performance	0.88%
Sharpe ratio – maximum performance	2.70%
Sharpe ratio – minimum performance	-0.64%

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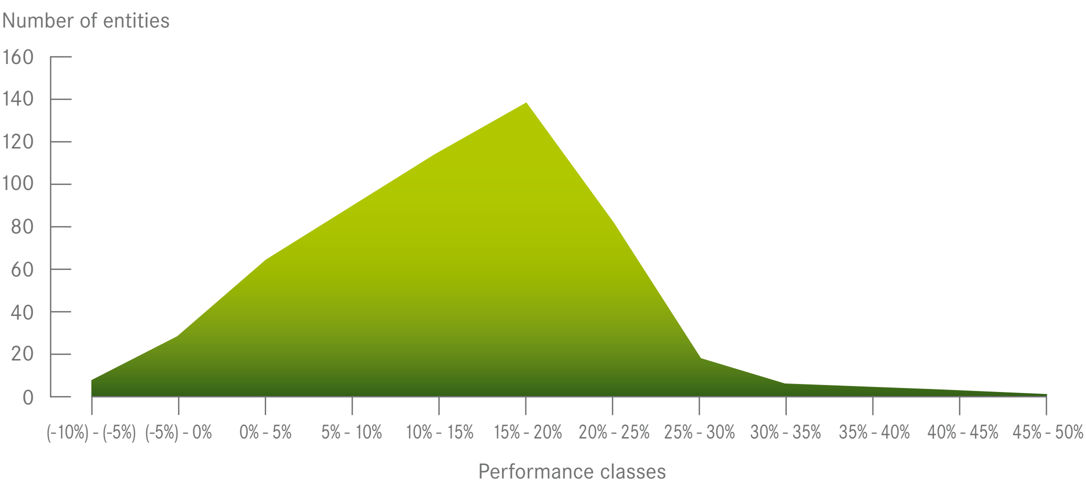
2.2.6. Entities whose investment policy consists in investing in international equities

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

Performance of entities investing in international equities in 2010



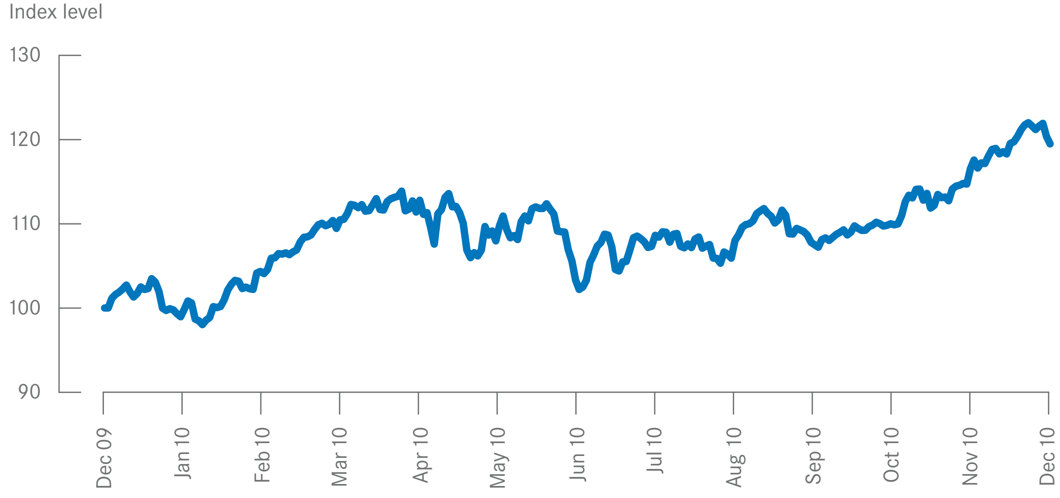
The average performance realised in 2010 by entities whose investment policy consists in investing in international equities was 14.74%. The average performance of the maximum return class was 44.95% whereas the average performance of the minimum return class was -6.92%. The standard deviation of the performance of these UCIs was 8.59%.

Statistical performance distribution of entities investing in international equities

Performance	Number of entities			
Return classes	Absolute frequency	Relative frequency	Cumulative absolute frequency	Cumulative relative frequency
-10% to -5%	7	1.25%	7	1.25%
-5% to 0%	29	5.20%	36	6.45%
0% to 5%	65	11.65%	101	18.10%
5% to 10%	89	15.95%	190	34.05%
10% to 15%	115	20.61%	305	54.66%
15% to 20%	138	24.73%	443	79.39%
20% to 25%	83	14.87%	526	94.27%
25% to 30%	19	3.41%	545	97.67%
30% to 35%	6	1.08%	551	98.75%
35% to 40%	3	0.54%	554	99.28%
40% to 45%	3	0.54%	557	99.82%
45% to 50%	1	0.18%	558	100.00%
Total	**558**	**100.00%**		

The MSCI WORLD INDEX Standard (Large + Mid Cap) (EUR) index, which includes dividends, realised a performance of 19.53% in 2010. 126 entities investing in international equities, i.e. 22.58% of all entities, realised a higher performance than the index cited. The market volatility for international equities was 13.78% (source: MSCI Barra, calculation: CSSF).

MSCI WORLD INDEX Standard (Large + Mid Cap) (EUR) 2010



Source : MSCI Barra

Interpretation of the Sharpe ratio

The UCI entities investing in international equities realised in 2010 on average a positive return of 1.26% per unit of risk considered. As regards the performance of the maximum return class, a positive return of on average 2.70% per unit of risk was observed. The performance of the minimum return class exhibited on average a slightly negative return of -0.33% per unit of risk considered.

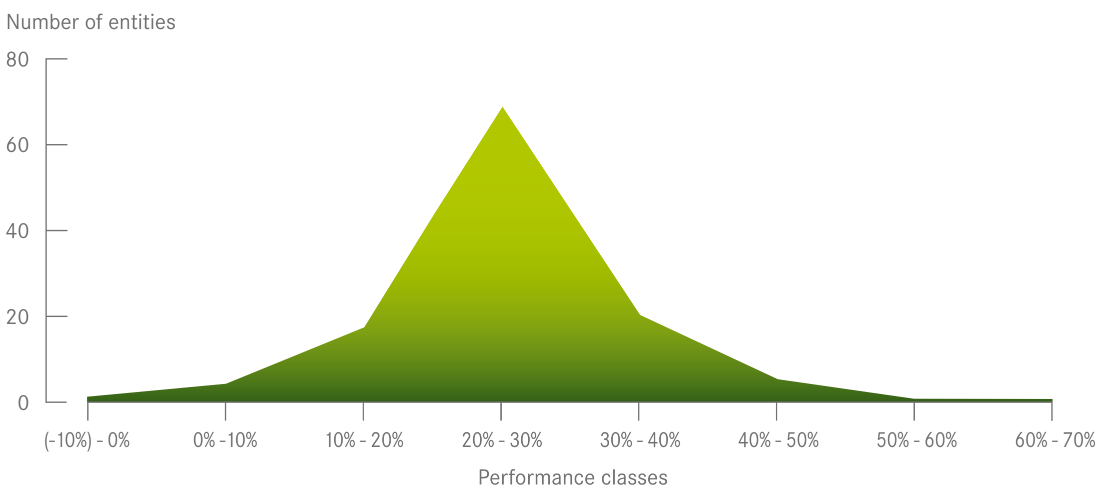
Risk and return summary table for entities investing in international equities

Average performance	14.74%
Maximum performance	44.95%
Minimum performance	-6.92%
Standard deviation of performance	8.59%
Performance spread	51.87%
Statistical population	558
Performance of the index MSCI WORLD INDEX Standard (Large + Mid Cap) (EUR)	19.53%
Market volatility	13.78%
Number of entities with higher performance than the index MSCI WORLD INDEX Standard (Large + Mid Cap) (EUR)	126
Sharpe ratio – average performance	1.26%
Sharpe ratio – maximum performance	2.70%
Sharpe ratio – minimum performance	-0.33%

2.2.7. Entities whose investment policy consists in investing in emerging market equities

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

Performance of entities investing in emerging market equities in 2010



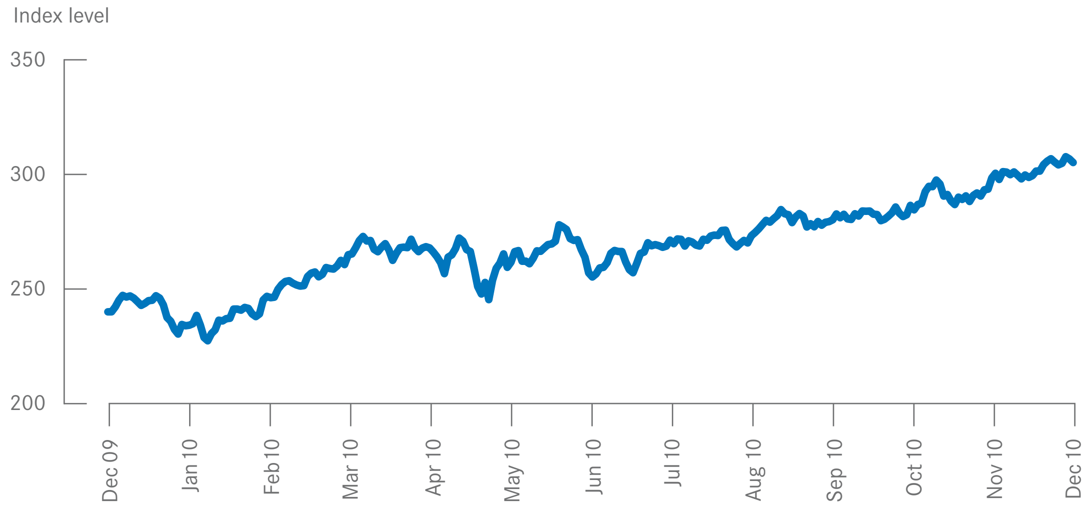
The average performance realised in 2010 by entities whose investment policy consists in investing in emerging market equities was 26.00%. The average performance of the maximum return class was 55.96% whereas the average performance of the minimum return class was 0.39%. The standard deviation of the performance of these entities was 9.33%.

Statistical performance distribution of entities investing in emerging market equities

Performance	Number of entities			
Return classes	Absolute frequency	Relative frequency	Cumulative absolute frequency	Cumulative relative frequency
-10% to 0%	1	0.83%	1	0.83%
0% to 10%	4	3.33%	5	4.17%
10% to 20%	18	15.00%	23	19.17%
20% to 30%	69	57.50%	92	76.67%
30% to 40%	21	17.50%	113	94.17%
40% to 50%	5	4.17%	118	98.33%
50% to 60%	1	0.83%	119	99.17%
60% to 70%	1	0.83%	120	100.00%
Total	**120**	**100.00%**		

The MSCI EM (EMERGING MARKETS) Standard (Large + Mid Cap) (EUR) index, which includes dividends, realised a performance of 27.13% in 2010. 49 entities investing in emerging market equities, i.e. 40.89% of all entities, realised a higher performance than the index cited. The market volatility for emerging market equities was 16.05% (source: MSCI Barra, calculation: CSSF).

MSCI EM (EMERGING MARKETS) Standard (Large + Mid Cap) (EUR) 2010



Source: MSCI Barra

Interpretation of the Sharpe ratio

The UCI entities investing in emerging market equities realised in 2010 on average a positive return of 2.14% per unit of risk considered. As regards the performance of the maximum return class, a return of on average 4.32% per unit of risk was observed. The performance of the minimum return class exhibited on average a slightly negative return of -0.12% per unit of risk considered.

Risk and return summary table for entities investing in emerging market equities

Average performance	26.00%
Maximum performance	55.96%
Minimum performance	0.39%
Standard deviation of performance	9.33%
Performance spread	55.57%
Statistical population	120
Performance of the index MSCI EM (EMERGING MARKETS) Standard (Large + Mid Cap) (EUR)	27.13%
Market volatility	16.05%
Number of entities with higher performance than the index MSCI EM (EMERGING MARKETS) Standard (Large + Mid Cap) (EUR)	49
Sharpe ratio – average performance	2.14%
Sharpe ratio – maximum performance	4.32%
Sharpe ratio – minimum performance	-0.12%

3. MANAGEMENT COMPANIES SET UP UNDER CHAPTER 13 OF THE LAW OF 20 DECEMBER 2002

3.1. Development in number

In 2010, fourteen applications requesting approval for management companies in accordance with the provisions of Chapter 13 of the law of 20 December 2002 (compared with eight applications in 2009) were submitted to the CSSF, consisting of:

- twelve projects for the creation of a new management company;
- one project for the transformation of a company not authorised under the financial sector legislation into a management company, and;
- one project for the transformation of a management company authorised under Chapter 14 of the law of 20 December 2002 into a management company authorised under Chapter 13 of the same law.

In 2010, seven new entities were registered on the official list of management companies authorised under Chapter 13 of the law of 2002. Four out of the seven new authorisations were granted to entities which were established in Luxembourg for the first time. Moreover, six authorisations concerned entities whose corporate purpose is limited exclusively to collective management activities within the meaning of Article 77(2) of the law of 2002; one entity benefits from an extended corporate purpose.

Among the twenty withdrawals in 2010, three are due to mergers between management companies following an alliance between the respective parent companies. The other seventeen withdrawals result from a rationalisation of Luxembourg structures initiated by the promoters of the management companies concerned.

As at 31 December 2010, the number of management companies approved in accordance with Chapter 13 of the law of 2002 thus totalled 179 entities.

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

	2003	2004	2005	2006	2007	2008	2009	2010
Registrations	3	23	47	80	31	13	9	7
Withdrawals	/	/	1	3	/	4	6	20
Total	**3**	**26**	**72**	**149**	**180**	**189**	**192**	**179**

Despite the presence of three new entities on the Luxembourg market which, in addition to collective management, also provide discretionary management services, the number of management companies abandoning an extended corporate purpose still exceeds the number of new approvals, thereby resulting in a net decrease in the number of entities with an extended corporate purpose in 2010.

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

	2003	2004	2005	2006	2007	2008	2009	2010
Registrations	2	6	5	10	4	1	/	3
Cessation of extended activities	/	/	/	/	3	4	2	4
Total	**2**	**8**	**13**	**23**	**24**	**21**	**19**	**18**

3.2. Geographical origin

2010 saw no major change to the geographic origin of management companies. Compared to the past, management companies of German and Swiss origin remain predominant on the Luxembourg market. Nevertheless, Swiss management companies registered a significant decrease following the decision by two corporations to rationalise their structure in Luxembourg. Furthermore, for the first time, the Italian management companies take third place in terms of numbers per country.

Country	2004	2005	2006	2007	2008	2009	2010
Andorra	/	/	/	/	/	1	1
Austria	/	/	/	/	/	1	1
Belgium	2	4	5	7	8	6	8
Canada	/	/	/	1	1	1	1
Denmark	1	2	3	3	3	3	4
Finland	/	/	/	/	/	1	1
France	3	5	14	20	21	22	19
Germany	8	15	39	42	46	46	44
Great Britain	3	6	7	8	10	11	11
Greece	/	/	1	2	2	3	3
Iceland	/	/	1	1	1	1	1
Italy	3	8	17	19	20	21	22
Japan	/	/	1	1	1	1	1
Liechtenstein	/	/	1	1	1	1	1
Luxembourg	/	1	8	9	8	8	5
Netherlands	2	3	3	4	3	4	4
Portugal	/	/	/	2	2	2	2
Russia	/	/	/	/	/	/	1
Spain	/	1	2	3	3	3	3
Sweden	2	4	5	6	6	6	6
Switzerland	1	18	35	44	45	42	32
United Arab Emirates	/	/	/	/	/	1	1
United States	1	5	7	7	8	7	7
Total	**26**	**72**	**149**	**180**	**189**	**192**	**179**

3.3. Assets under management

As at 31 December 2010, the total net assets managed by management companies set up under Chapter 13 of the law of 2002 amounted to EUR 1,526.0 billion, compared with EUR 1,293.3 billion in 2009, i.e. an increase of 17.99%. 55% of this increase is attributable to the markets' positive performance while 45% is due to new subscriptions. Taking into account total net assets of EUR 2,199 billion invested as at 31 December 2010 in Luxembourg UCIs, management companies set up under Chapter 13 of the law of 2002 manage 69.5% of the total assets of Luxembourg UCIs.

Development in the net assets of management companies

(in billion EUR)	2006	2007	2008	2009	2010	Variation 2009/2010
Total net assets	1,306.0	1,476.8	1,107.1	1,293.3	1,526.0	17.99%
of which:						
in fonds commun de placement	*594.6*	*657.0*	*479.4*	*515.1*	*554.0*	*7.55%*
in investment companies	*711.4*	*819.8*	*627.7*	*778.2*	*972.0*	*24.90%*

Distribution of management companies in terms of assets under management as at 31 December 2010

Assets under management	Number of management companies				
	2006	2007	2008	2009	2010
< 100 million EUR	15	32	41	37	31
100 to 500 million EUR	30	26	33	34	36
500 to 1,000 million EUR	13	25	21	21	20
1 to 5 billion EUR	34	40	49	51	41
5 to 10 billion EUR	23	21	17	18	15
10 to 20 billion EUR	16	15	13	14	12
> 20 billion EUR	18	21	15	17	24
Total	**149**	**180**	**189**	**192**	**179**

3.4. Evolution in number of employees

The total number of management company employees as at 31 December 2010 was 2,339, compared with 2,308 as at 31 December 2009, thus an increase of 31 employees (+1.34%). This increase was mainly due to two management companies whose staff grew at a higher rate compared to all others.

3.5. Aggregated balance sheet and profit and loss account

The provisional aggregated balance sheet of management companies reached EUR 7.135 billion as at 31 December 2010, compared with EUR 6.758 billion at the end of 2009. This growth can be explained by an increase in the activities of management companies following the favourable evolution of financial markets.

The provisional aggregated net profits totalled EUR 1.671 billion as at 31 December 2010 compared with EUR 1.542 billion as at 31 December 2009. This increase was due to the combined effects of an increase in operating results (+4.49%), a decrease in general administration expenses (-6.47%) and a decline in the number of revaluation adjustments made to current assets by management companies (-77.34%). It should nevertheless be noted that 23 of the 179 management companies ended the financial year 2010 with a loss (32 in 2009).

3.6. International expansion

3.6.1. Freedom of establishment

In 2010, four management companies incorporated under Luxembourg law (three in 2009) introduced an application in order to establish a branch abroad:

- Ersel Gestion Internationale S.A. for Great Britain;
- Man Investments (Luxembourg) S.A. for Switzerland;
- Natixis Global Associates for the Netherlands and Sweden;
- Swiss & Global Asset Management (Luxembourg) S.A. for Spain and Great Britain.

However, the management company Fortis Investment Luxembourg S.A. decided to close its Greek branch in 2010 following its alliance with the management company BNP Paribas Investment Partners Luxembourg.

As at 31 December 2010, the following twelve management companies were represented in one or several countries abroad by means of a branch:

Name of the management company	Branch
AllianceBernstein (Luxembourg) S.A.	Japan
Assenagon Asset Management S.A.	Germany
Berenberg Lux Invest S.A.	Germany
Casa 4 Funds Luxembourg European Asset Management	Switzerland
Dexia Asset Management Luxembourg S.A.	Germany Italy Netherlands Spain Switzerland
Ersel Gestion Internationale S.A.	Great Britain
Eurizon Capital S.A.	Singapore
JPMorgan Asset Management (Europe) S.à r.l.	Austria France Germany Greece Italy Netherlands Spain Sweden
Man Investments (Luxembourg) S.A.	Switzerland
Natixis Global Associates	France Germany Italy Netherlands Sweden
Swiss & Global Asset Management (Luxembourg) S.A.	Great Britain Spain
Universal-Investment-Luxembourg S.A.	Germany

There were no branches of management companies of other EU Member States established in Luxembourg in 2010.

3.6.2. Free provision of services

Six management companies incorporated under Luxembourg law introduced a notification to carry on activities in one or several EU countries by way of free provision of services in 2010. These notifications concerned marketing, discretionary portfolio management and other ancillary services.

In 2010, the CSSF received 21 notifications for the free provision of services within the Luxembourg territory from management companies incorporated in another EU Member State. The majority of these notifications were submitted by French management companies followed by Spanish, Italian and Norwegian management companies. The services offered in Luxembourg include collective management, discretionary management and investment advice.

3.6.3. Representative offices

In 2010, the management company Alceda Fund Management S.A. opened representative offices in Germany and in Switzerland.

Following the alliance with the group BNP Paribas, Fortis Investment Luxembourg S.A. closed its representative offices in Austria, Spain, Italy and Poland. Nordea Investment Funds S.A. closed its representative office in Switzerland.

3.7. Practice of prudential supervision

3.7.1. Scope of Circular CSSF 10/437 on guidelines concerning the remuneration policies in the financial sector

The management companies subject to Chapter 13 or Chapter 14 of the law of 2002 fall within the scope of Circular CSSF 10/437. Consequently, they shall implement a remuneration policy which complies with the circular pursuant to Section II "Remuneration policy".

3.7.2. Management company and securitisation activities

Confronted with the question whether a management company subject to Chapter 13 of the law of 2002 may provide administrative services to a securitisation vehicle, the CSSF decided that a management company may provide these services if it has adequate technical and human means. A file describing the provided services shall be submitted for prior authorisation to the CSSF.

4. DEVELOPMENTS IN THE REGULATORY FRAMEWORK

4.1. Grand-ducal regulation of 14 July 2010 determining the conditions and criteria for the exemption from the subscription tax of undertakings for collective investment and specialised investment funds investing in microfinance in accordance with Articles 20 and 21 of the law of 18 December 2009 on the State revenue and expenditure budget for the financial year 2010

The grand-ducal regulation defines the criteria which provide the basis for the exemption from the subscription tax of UCIs and SIFs investing in microfinance. It is in line with the diversification of the financial centre in order to benefit from the development potential of investment funds in microfinance.

The grand-ducal regulation sets out that UCIs and SIFs which have the label of the Luxembourg Fund Labelling Agency a.s.b.l. (LuxFLAG)[13] are *de iure* exempted from the subscription tax. UCIs and SIFs which do not have the label LuxFLAG may benefit from the exemption from the subscription tax, provided that their investment policy stipulates that at least 50% of their assets are invested in one or several microfinance institutions. In those two cases, the UCIs/SIFs concerned shall submit to the CSSF a request for registration on the list mentioned in Article 1, point 2 of the grand-ducal regulation.

4.2. Law of 17 December 2010 relating to undertakings for collective investment and CSSF regulations No 10-4 and No 10-5

The law of 17 December 2010 transposes, among others, Directive 2009/65/EC of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS IV Directive) into Luxembourg law. It also amends certain Luxembourg legal provisions relating to UCIs and, in addition, it amends the law of 13 February 2007 relating to specialised investment funds as well as the law of 4 December 1967 on income tax.

The CSSF regulations No 10-4 and No 10-5 transpose the following into Luxembourg law:

(i) Directive 2010/43/EU of 1 July 2010 implementing Directive 2009/65/EC as regards organisational requirements, conflicts of interest, conduct of business, risk management and content of the agreement between a depositary and a management company; and

(ii) Directive 2010/44/EU of 1 July 2010 implementing Directive 2009/65/EC as regards certain provisions concerning fund mergers, master-feeder structures and notification procedure.

The new law repeals the law of 20 December 2002 relating to undertakings for collective investment with effect from 1 July 2012, except for the tax provisions referred to in Articles 127 and 129 which are repealed with effect from 1 January 2011.

The new law entered into force on 1 January 2011.

[13] Association created in 2006 based on the joint initiative of the private and public sectors, whose purpose is to grant a label to investment funds in microfinance in order to assure investors that these funds effectively invest in microfinance.

On 10 January 2011, the CSSF published Circular CSSF 11/498 which provides a general description of the provisions of the law of 17 December 2010 and which also aims to highlight other implementation measures of Directive 2009/65/EC (so-called level 2 and level 3 measures), i.e. Commission Regulations (EU) No 583/2010 and No 584/2010 of 1 July 2010 and the guidelines concerning the UCITS IV Directive published by the Committee of European Securities Regulators (CESR), which was replaced by the European Securities and Markets Authority (ESMA) on 1 January 2011.

5. PRUDENTIAL SUPERVISORY PRACTICE

5.1. Prudential supervision

5.1.1. Standards to be observed by UCIs

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

5.1.2. Instruments of prudential supervision

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

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

5.1.3. Means of control

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

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

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

In accordance with Circular IML 97/136 and pursuant to Article 118 of the law of 20 December 2002 and Article 48 of the law of 13 February 2007, the central administrations of Luxembourg UCIs must transmit financial information by electronic means to the CSSF, on a monthly (tables O1.1.) and yearly (tables O4.1. and O4.2.) basis. The deadline to transmit the monthly financial information is ten days following the reference date, which is in principle the last day of each month. As regards yearly financial information, the reference date is the date of the end of the financial year and the communication time limit is four months for UCIs governed by the law of 20 December 2002 and six months for SIFs.

As far as monthly financial information is concerned, the CSSF considers that UCIs must, on the one hand, strictly observe the pre-defined deadline to submit table O1.1. and, on the other hand, pay due attention when preparing this table so as to ensure that the format and content are correct. For information, the format and content of about 13,000 files, representing nearly 30,500 types of units/shares, are controlled every month.

- **Meetings**

In 2010, 252 meetings were held between representatives of the CSSF and intermediaries of UCIs. These meetings concerned the presentation of new UCI projects, restructurings of UCIs, but also the application of the laws and regulations of UCIs.

5.2. Systemic risk and UCIs

Following the financial crisis of 2007/2008 and during the recent visits of the International Monetary Fund (IMF) at the CSSF, the discussions referred to, among others, the systemic risk which may come from UCIs incorporated under Luxembourg law.

In a recent document, the European Securities and Markets Authority (ESMA) also raised the issue of systemic risk in relation to different categories of UCIs present in the EU.

For UCIs, the systemic risk may come from different scenarios, such as the failure of a UCI due to one or several systemic players (microshock) or a general market problem (macroshock).

This subject also concerns the CSSF. In order to have the necessary data to identify situations which may trigger a systemic risk, the CSSF will request certain UCIs to answer a questionnaire drawn up within the context of systemic risk.

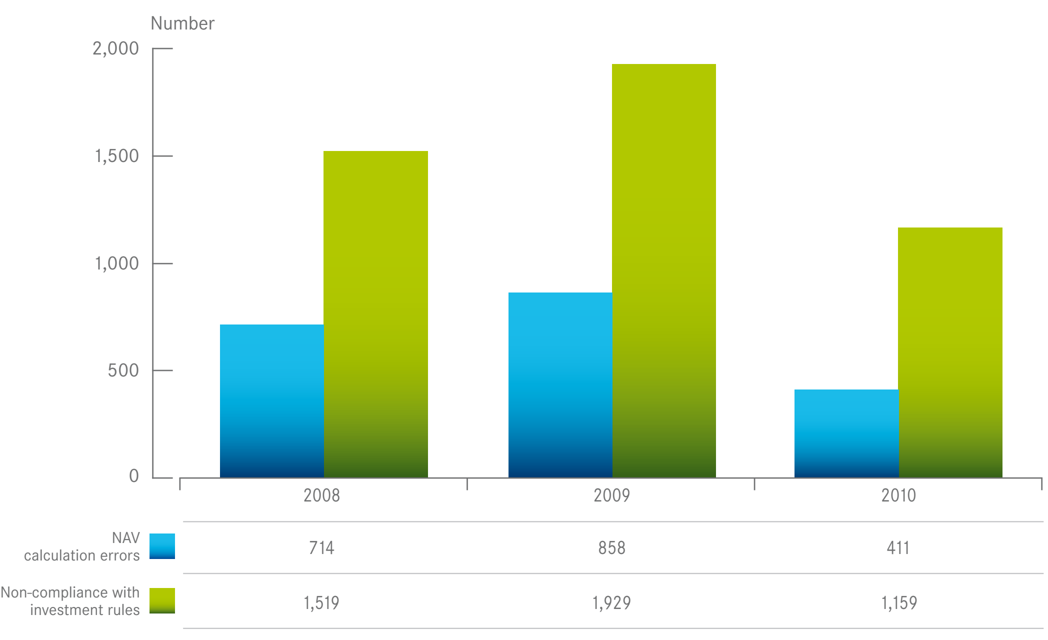
5.3. Circular CSSF 02/77 on the protection of investors in case of NAV calculation error and correction of the impacts of non-compliance with the investment rules

5.3.1. Reports made in 2010 on the basis of Circular CSSF 02/77

In 2010, the CSSF recorded 1,570 reports on the basis of Circular CSSF 02/77, compared with 2,787 statements in 2009, representing a decrease of 43.7%.

Among these reports, 411 cases (858 in 2009) concerned NAV calculation errors and 1,159 cases (1,929 in 2009) concerned non-compliance with investment rules.

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



	2008	2009	2010
NAV calculation errors	714	858	411
Non-compliance with investment rules	1,519	1,929	1,159

As far as the number of NAV calculation errors is concerned, the rising trend between 2005 and 2009 was reversed in 2010. In 2010, the number of cases of NAV calculation errors recorded a decrease of 52% compared to 2009. The same situation is recorded as regards non-compliance with investment rules which shows a fall of 40% in 2010 compared to 2009. This drop is mainly attributable to the fact that eight major central administrations of UCIs reported a much lower number of NAV calculation errors or non-compliance with investment rules. These central administration providers used substantial and continuous means to rationalise and improve their administrative organisation. These additional investments contributed, together with a stock exchange environment less stormy than the previous years, to the positive effect of the decreasing number of reports.

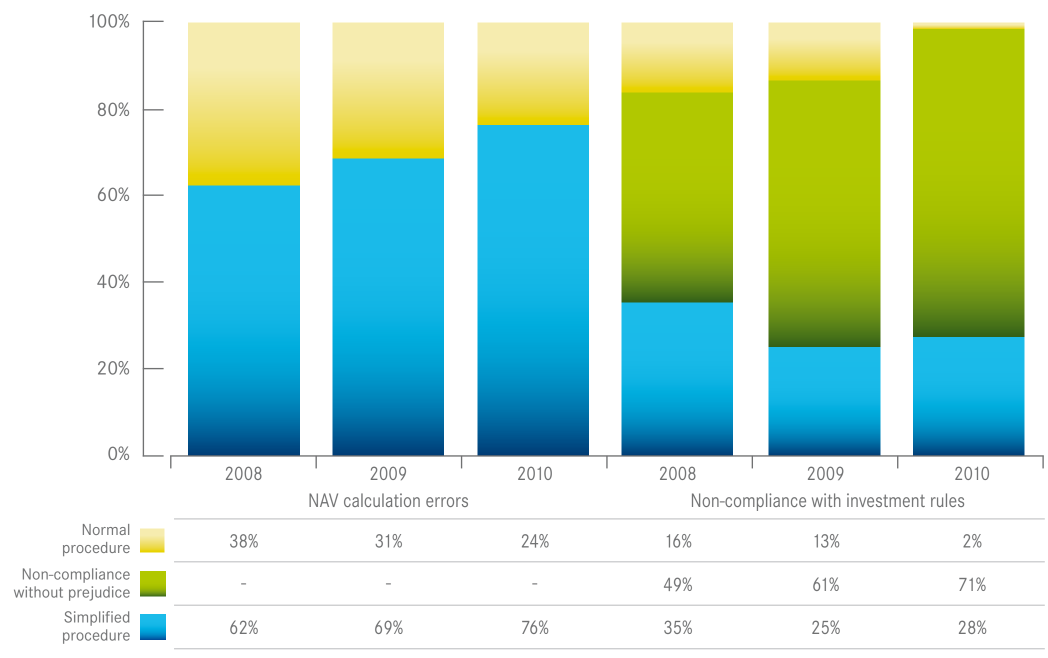
Referring to the reports received in 2010, 109 of the 411 cases of NAV calculation errors and 257 of the 1,159 cases of non-compliance with investment rules could not be closed at 31 December 2010, as the CSSF is still awaiting further information such as the report(s) of the *réviseur d'entreprises* (statutory auditor), the management letter or the report on the UCI's activity following the application of the simplified procedure as provided for by Circular CSSF 02/77.

A simplified procedure may be applied for cases of NAV calculation errors or non-compliance with investment rules that entail losses for the UCI, where the indemnification amount does not exceed EUR 25,000 and the amount to be reimbursed to an investor does not exceed EUR 2,500.

Thus, in 2010, 314 out of 411 cases of NAV calculation errors fell within the scope of the simplified procedure (590 cases out of 858 in 2009). 321 out of 1,159 cases of non-compliance with investment rules have also applied for this procedure (488 cases out of 1,929 in 2009).

The following graph plots the proportion of the cases of simplified procedure compared to the total number of reports received over the last three years as well as the instances of non-compliance with investment rules that were resolved without harming either the investors or the UCI.

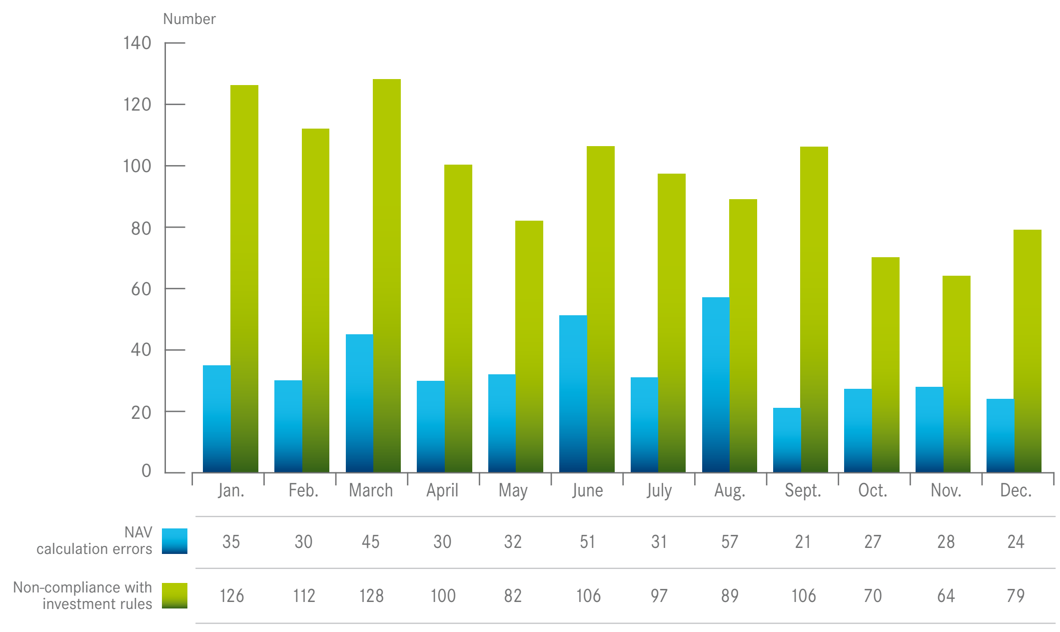
Simplified procedure



	2008	2009	2010	2008	2009	2010
	NAV calculation errors			Non-compliance with investment rules		
Normal procedure	38%	31%	24%	16%	13%	2%
Non-compliance without prejudice	-	-	-	49%	61%	71%
Simplified procedure	62%	69%	76%	35%	25%	28%

The following graph sets out in detail the reports made during 2010.

Monthly development in the errors and instances of non-compliance reported in 2010

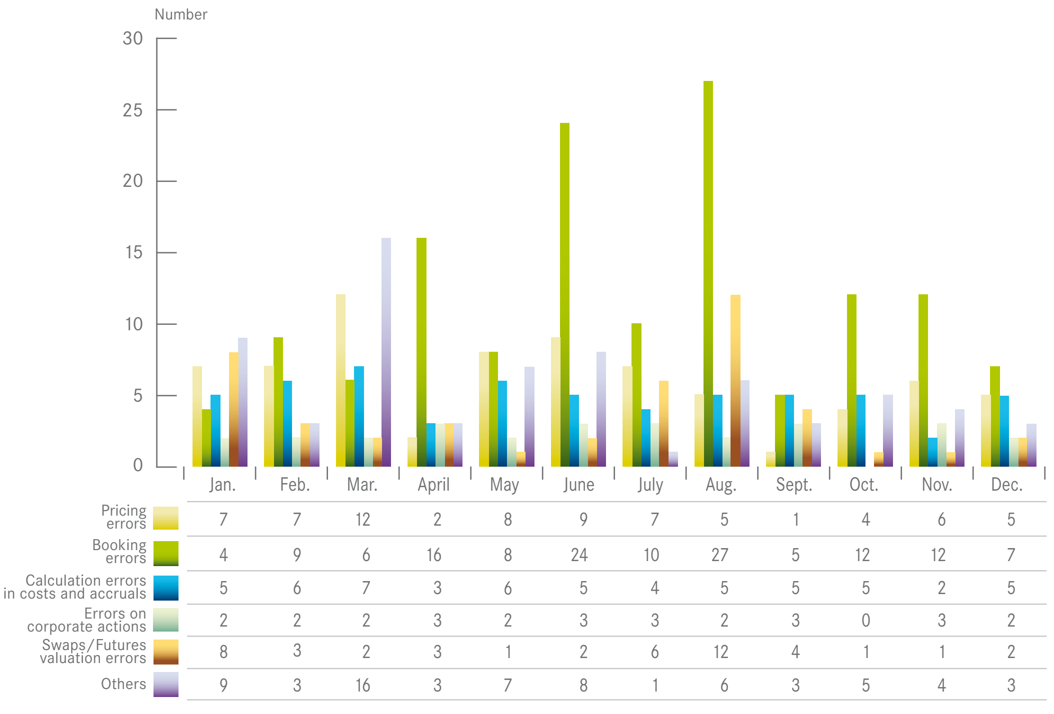


	Jan.	Feb.	March	April	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.
NAV calculation errors	35	30	45	30	32	51	31	57	21	27	28	24
Non-compliance with investment rules	126	112	128	100	82	106	97	89	106	70	64	79

The origin of NAV calculation errors can be divided into five categories: pricing errors, booking errors, errors in the calculation of costs and accruals, errors in the valuation of swaps and futures and other errors.

The following graph plots the different causes of NAV calculation errors recorded in 2010.

Development of the origin of NAV calculation errors in 2010

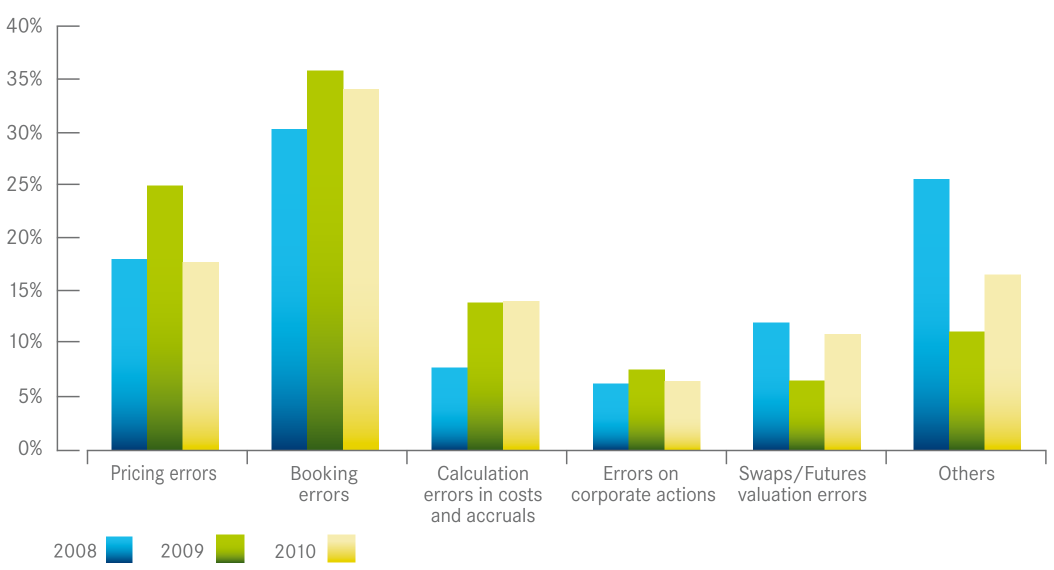


	Jan.	Feb.	Mar.	April	May	June	July	Aug.	Sept.	Oct.	Nov.	Dec.
Pricing errors	7	7	12	2	8	9	7	5	1	4	6	5
Booking errors	4	9	6	16	8	24	10	27	5	12	12	7
Calculation errors in costs and accruals	5	6	7	3	6	5	4	5	5	5	2	5
Errors on corporate actions	2	2	2	3	2	3	3	2	3	0	3	2
Swaps/Futures valuation errors	8	3	2	3	1	2	6	12	4	1	1	2
Others	9	3	16	3	7	8	1	6	3	5	4	3

During the relevant period, the main NAV calculation errors were due to errors in the valuation of swaps and futures (17%), pricing errors (18%) and booking errors (34%).

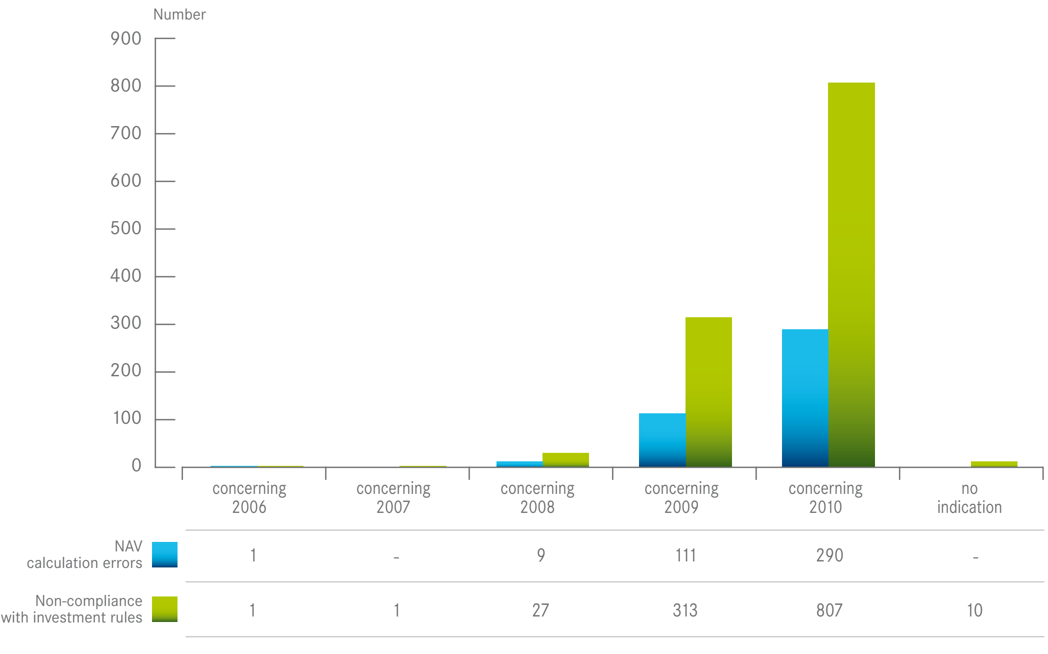
The following table shows the development of NAV calculation errors from 2008 and highlights that over the past three years, booking errors and errors in the valuation of securities held by UCIs were the main causes of NAV calculation errors.

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



It should be noted that the reports received during 2010 do not necessarily relate to errors and instances of non-compliance which actually happened in 2010. They may in fact relate to errors or instances of non-compliance which have been detected in 2010, but which have occurred in a previous period, as shown in the graph below.

Reports submitted in 2010



	concerning 2006	concerning 2007	concerning 2008	concerning 2009	concerning 2010	no indication
NAV calculation errors	1	-	9	111	290	-
Non-compliance with investment rules	1	1	27	313	807	10

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

The table below sets out the detailed compensation amounts notified in 2009 and 2010. It should be noted that the table is based on data available to the CSSF as at 31 December 2009 and 31 December 2010, at which point the compensation amounts for certain cases had not yet been submitted.

Compensation paid following NAV calculation errors

	Investors		UCI/Sub-fund	
	2009	2010	2009	2010
EUR	11,624,300.72	4,454,281.57	16,375,326.81	4,722,415.83
USD	4,783,387.87	3,016,300.69	4,940,711.72	2,043,269.83
GBP	449.18	789.00	15,127.35	22,850.00
CHF	588,320.40	0.00	485,321.56	150.00
Other currencies *	187,967.34	4,288,034.31	210,851.17	2,058,074.22
Total (in EUR)**	**15,529,736.66**	**11,000,604.70**	**20,359,956.41**	**8,336,321.30**

* converted in EUR at the exchange rate applicable on 31 December 2009 and 31 December 2010 respectively.
** exchange rate as at 31 December 2009 and 31 December 2010 respectively.

Compensation paid following non-compliance with investment rules

	Investors		UCI/Sub-fund	
	2009	2010	2009	2010
EUR	160,228.50	622,420.92	4,271,938.94	1,044,687.54
USD	23,217.64	1,641,019.79	3,099,483.32	349,885.80
GBP	0.00	0.00	58,378.62	3,009,335.78
CHF	424.00	0.00	41,312.62	6,343.39
Other currencies *	0.00	0.00	709,706.20	9,342.46
Total (in EUR)**	**176,630.94**	**1,850,545.30**	**7,226,748.13**	**4,817,133.11**

* converted in EUR at the exchange rate applicable on 31 December 2009 and 31 December 2010 respectively.
** exchange rate as at 31 December 2009 and 31 December 2010 respectively.

As regards the NAV calculation errors, an overall decrease is recorded for the compensation amounts paid out in the framework of the 2010 reports as compared to the 2009 reports. Moreover, in four cases of NAV calculation errors, the compensation amounts exceeded EUR 1 million or the equivalent in currencies and the amounts related to these four NAV calculation errors represented 56% of the total amount paid for the correction of all the reported errors.

The trend of continually increasing amounts paid out as compensation following non-compliance of investment rules, evident since 2006, was halted in 2010. It should be noted that the compensation amounts linked to four instances of non-compliance with investment rules represented 88% of the total amount paid out to redress the incidences of non-compliance with investment rules.

5.4. Management letters

Chapter P of Circular IML 91/75 of 21 January 1991 states that UCIs must automatically and immediately communicate to the CSSF the management letters issued by the *réviseur d'entreprises* (statutory auditor) in the context of the audits which the latter is obliged to undertake pursuant to Article 113 of the law of 2002.

The current analysis was performed based on the data of the year 2009, given its relevance to the year under review. Specifically, most UCIs close their financial year on 31 December which implies that the data relating to 2009 are established by the CSSF in 2010.

As in the previous years, many management letters, namely 73%, are management letters that contain no recommendations, i.e. the *réviseur d'entreprises* (statutory auditor) has not detected any irregularities in the management of the UCIs. 25% are management letters with recommendations through which the *réviseur d'entreprises* (statutory auditor) has reported various types of irregularities. 2% of the management letters have not yet been submitted.

The examination of management letters with recommendations shows that the irregularities reported by the *réviseur d'entreprises* (statutory auditor) can be broken down into four large categories: overstepping of statutory or regulatory limits, NAV calculation errors, non-compliance with investment policy and problems in the organisation of UCIs.

5.5. Long form reports

Circular CSSF 02/81 of 6 December 2002 sets out the rules concerning the scope of the audit of the annual financial statements and the content of the long form reports to be drawn up pursuant to the law on UCIs. The circular, which applies to all Luxembourg UCIs, considers that in practice, the role and functions of the *réviseur d'entreprises* (statutory auditor) constitute one of the pillars of the prudential supervision of UCIs.

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

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

Agents hired in 2010 and 2011 - Departments "Supervision of undertakings for collective investment", "Supervision of investment firms", "Supervision of other PFS" and "Information systems and supervision of support PFS"

Left to right: Giuseppe DALOIA, Patrice MACK, François PETIT, Filipa MENDES LOPES, Laurent VAN BURIK, Sébastien TRAVERSA, Annick HUCKER, Marc BIRCHEN

Absent: Lucinda AZEVEDO PEREIRA, Denise ARNAUD, Cécile GELLENONCOURT

SUPERVISION OF PENSION FUNDS

04

1. Developments in the pension funds sector in 2010
2. International cooperation

1. DEVELOPMENTS IN THE PENSION FUNDS SECTOR IN 2010

1.1. Pension funds

During 2010, no changes were registered on the official list of pension funds subject to the law of 13 July 2005 on institutions for occupational retirement provision in the form of pension savings companies with variable capital (SEPCAV) and pension savings associations (ASSEP). The total number of pension funds subject to the law of 13 July 2005 remained unchanged at fifteen entities as at 31 December 2010.

Net assets of pension funds governed by the law of 13 July 2005 reached EUR 683 million at the end of 2010 against EUR 654 million as at 31 December 2009.

While the setting-up of new pension funds stagnated in 2010, the CSSF expects an upturn in the development of pension funds activity in 2011, mainly through the development of cross-border activities of existing pension funds and through the establishment of new entities in Luxembourg.

1.2. Liability managers

Following the registration, in 2010, of Towers Watson Netherlands B.V. on the official list of professionals authorised to act as liability managers for pension funds subject to the law of 13 July 2005, the number of liability managers of pension funds approved by the CSSF amounted to fourteen as at 31 December 2010.

2. INTERNATIONAL COOPERATION

2.1. Green Paper of the European Commission: "Towards adequate, sustainable and safe European pension systems"

In July 2010, the European Commission published a Green Paper in order to launch a European debate on the key challenges facing pension systems and how the EU can support Member State efforts to deliver adequate, sustainable and safe pensions. In its Green Paper, the European Commission mainly recommends to strengthen the internal market for pension products and to remove the obstacles to mobility of pensions in the EU. In this context, it is also interested in the manner how Directive 2003/41/EC on institutions for occupational retirement provision (IORP) should be amended during the next review planned for 2011 to improve the conditions for IORP cross-border activity.

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

In 2010, CEIOPS continued its works in the fields of information exchange and cooperation between supervisory authorities in the context of the supervision of IORPs exercising cross-border activities. In particular, CEIOPS analysed the different national approaches relating to the definition of cross-border activity within the meaning of Directive 2003/41/EC and the problems which might result from it in the practical cross-border activity of IORPs. In the same context, CEIOPS studied the possible implications of additional information requirements that a host Member State may impose on IORPs exercising a cross-border activity. All of these works should be useful for the review of Directive 2003/41/EC planned for 2011, in particular as regards a possible clarification of the concept of "cross-border activity".

The end of 2010 also means the end of CEIOPS under its previous form, as the committee is replaced as from 1 January 2011 by the European Insurance and Occupational Pensions Authority (EIOPA). EIOPA is established following the restructuring of the financial sector supervision in the EU and is part of the European system of financial supervision consisting of the three European Supervisory Authorities and the European Systemic Risk Board (ESRB).

PRUDENTIAL SUPERVISION OF SICARS

05

1. Developments in the SICAR sector in 2010

2. Prudential practice

1. DEVELOPMENTS IN THE SICAR SECTOR IN 2010

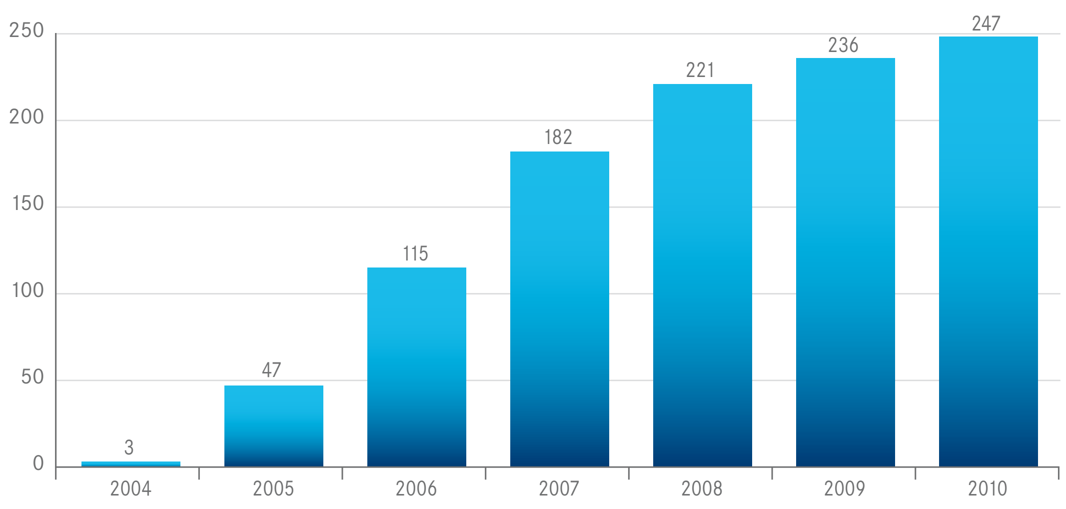
In 2010, the CSSF received 42 files from SICARs applying for registration on the CSSF's official list of SICARs, i.e. a slight increase compared to 2009 (40 files). Eight out of the 42 applications for registration related to umbrella SICARs. Ten files have been withdrawn, at the initiators' request, during the scrutiny process.

In 2010, 31 SICARs, including 11 umbrella SICARs have been authorised. Twenty SICARs were withdrawn from the official list for the following reasons: seven abandonments of the SICAR status, three transfers of the registered office abroad (of which one cross-border merger), six voluntary liquidations and four judicial winding-ups.

The number of SICARs registered on the official list of the CSSF grew from 236 entities as at 31 December 2009 to 247 entities as at 31 December 2010, among which 27 umbrella SICARs.

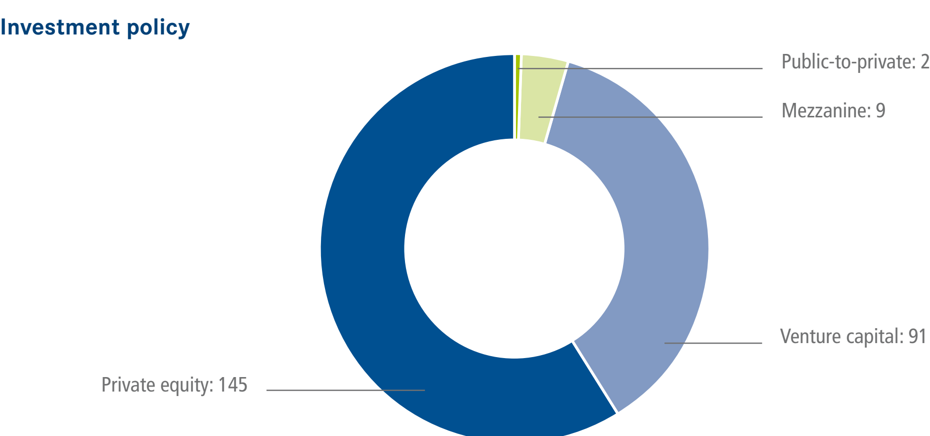
It should be noted that around fifty application files are still under review.

Development in the number of SICARs



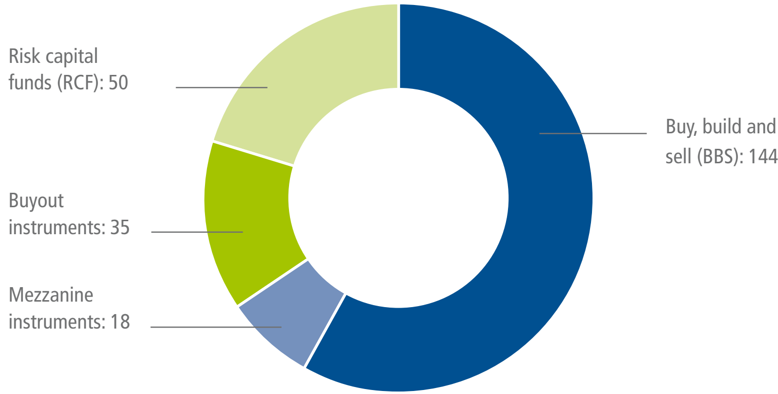
As far as the investment policy of SICARs is concerned, the following graph reveals a preference for private equity, which grew by 9% compared to 2009, followed by venture capital.

Investment policy



Investment strategies inherent in SICARs may be broken down into four main types: buy, build and sell; buyout instruments; mezzanine instruments; risk capital funds. In practice, combined strategies are generally used in the area of risk capital. Buyout and mezzanine grew by some 30%.

Investment strategy



As regards the sector-based distribution, 125 SICARs prefer not to limit their investment policy to a particular investment sector. Among the SICARs having adopted a specialised policy, there is a certain concentration in the "Real estate", "Technology" and "Energy" sectors.

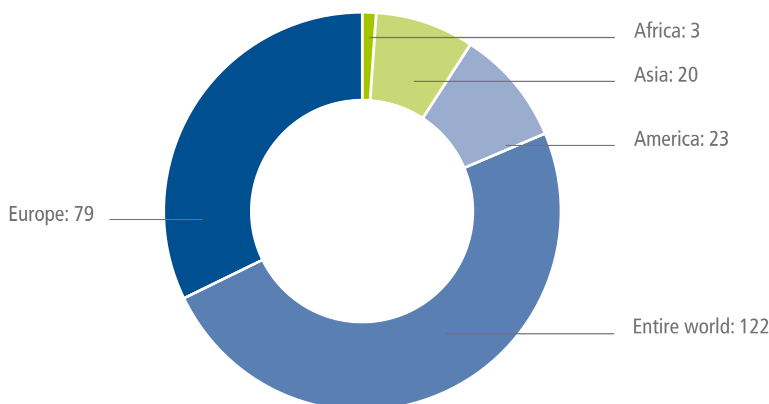
Sector-based distribution

Sector	Number
All sectors	125
Real estate	46
Technology	21
Energy	15
Industry	8
Services	8
Science	6
Educations and sports	5
Finance	4
Microfinance	4
PPP	3
Precious metals and gemstones	1
Sharia	1
Total	**247**

As for the geographical area of investments, it can be observed that the majority of the 247 SICARs invest in Europe. 36% of SICARs choose to have the possibility to invest worldwide.

05

Investment region



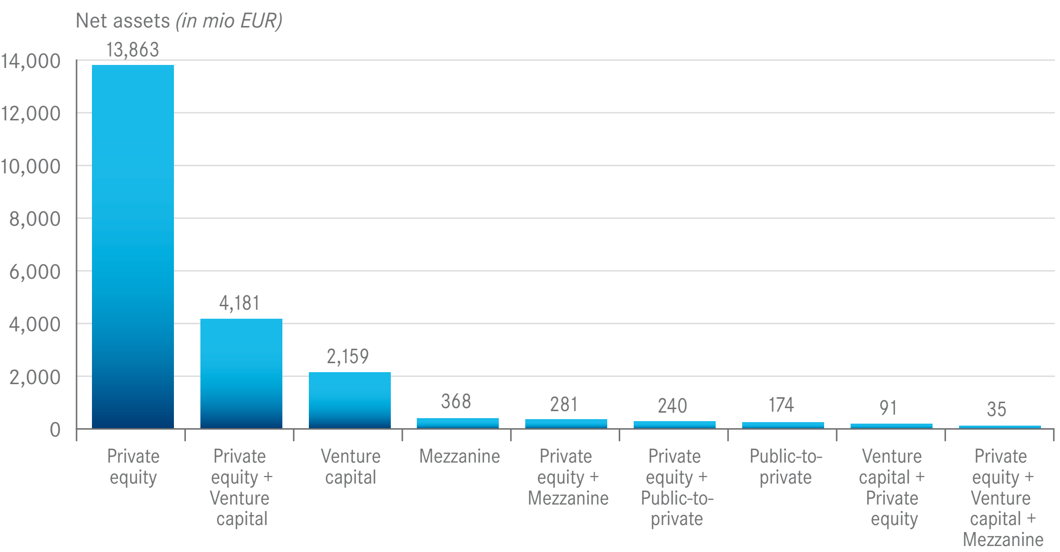
As far as the geographical origin of the initiators is concerned, those from Europe are largely predominant, followed by US initiators, which confirms the 2009 trend.

Geographical origin of the initiators

Country	as % of total
France	18.51%
Switzerland	14.59%
Germany	11.39%
Luxembourg	10.68%
United States	8.19%
Italy	6.41%
United Kingdom	5.34%
Belgium	4.98%
Spain	4.98%
Austria	2.14%
Netherlands	1.42%
Denmark	1.07%
Finland	1.07%
Russia	1.07%
Egypt	0.71%
Guernsey	0.71%
Iceland	0.71%
Portugal	0.71%
Turkey	0.71%
Australia	0.36%
British Virgin Islands	0.36%
Greece	0.36%
Hong Kong	0.36%
Hungary	0.36%
India	0.36%
Israel	0.36%
Jersey	0.36%
Kuwait	0.36%
Lebanon	0.36%
Malta	0.36%
Singapore	0.36%
Slovenia	0.36%
Total	**100.00%**

Based on the figures available as at 31 December 2010, the capital commitments in SICARs reached EUR 16.6 billion and their balance sheet total amounted to EUR 25.1 billion.

Breakdown of net assets of SICARs according to the investment policy



Investment in risk capital amounted to EUR 22.2 billion, while current assets added up to EUR 1.9 billion.

It should be noted that SICARs are mainly financed by their investors. Total financing of SICARs by banks amounted to EUR 0.7 million, representing 2.78% of the SICARs' balance sheet total.

2. PRUDENTIAL PRACTICE

2.1. Authorisation procedure

In May 2010, the CSSF published the document "Information request for authorisation" on its website (section "SICAR"), which need to be filled in and enclosed in all application requests filed with the CSSF. This form, available only in English, familiarises initiators of SICAR projects with the basic information required for the authorisation of a SICAR and allows the CSSF to gather important information according to a predefined scheme.

After having reviewed the application file, the CSSF schedules a meeting with the initiator and the managers of the future SICAR in the context of the authorisation procedure.

If the application file does not raise any objection after scrutiny, the CSSF communicates its approval in principle by post. This letter specifies, among other things, that the CSSF reserves the right to reconsider the validity of the approval in principle, should the final documents required for the registration of the SICAR on the official list not be transmitted within three months.

The CSSF wishes to stress in this context that it also requests to receive, prior to the registration of a SICAR on the official list, the duly signed commitment letter of the *réviseur d'entreprises* (statutory auditor) proving the acceptance of the audit mandate for the future SICAR.

2.2. Changes in the CSSF's prospectus acceptance procedure

After having verified a prospectus, whether in the context of the scrutiny of a new SICAR file or in the context of subsequent changes to the prospectus, the CSSF henceforth confirms by separate letter that it took note of the marketing of the SICAR based on the prospectus in the proposed form. This letter is not tantamount to an official approval of the prospectus content by the CSSF, but only expresses that the CSSF took note thereof. The prospectus shall be drawn up under the responsibility of the SICAR's managers. The CSSF will stamp the prospectus, which needs to be submitted at least in triplicate, for identification purposes. This new procedure replaces the traditional "visa" procedure for prospectus approval.

2.3. Half-year reporting K3.1

In its letter dated 14 January 2011, the CSSF reminded all the SICARs registered on the official list to provide under sections 7A and 7B of the reporting file K3.1 the information required on the beneficial owners of a SICAR. If a SICAR does not have a beneficial owner governed by the provisions of points 7A and 7B, "n/a" (not applicable) should be filled in into the sections concerned.

The letter reminds as well that financial information to be provided by SICARs within 45 calendar days after the reference date (30 June and 31 December) may be prepared, if necessary, according to the provisional figures as regards the assessment of investments in risk capital (cf. Circular CSSF 08/376).

The CSSF requires that a reporting with final financial data (reflecting the figures of the annual report) be submitted to the CSSF once the SICAR's audit has been completed.

2.4. Observance of legal deadlines and deadlines set down by the CSSF

The CSSF emphasises the obligation to comply with deadlines for transmitting financial data and other *ad hoc* information. Non-compliance with the deadlines is subject to sanctions.

2.5. On-site inspections

During 2010, the department in charge of supervising SICARs carried out, together with other CSSF departments concerned, fourteen on-site inspections relating to SICARs.

The purpose of these missions was to check the procedures set up by the SICARs and their service providers in order to ensure proper functioning in compliance with the laws in force (administrative organisation, prevention of money laundering and fight against terrorism, etc.) Three *ad hoc* inspections concerned SICARs with specific problems.

2.6. Special mandates given by the CSSF to *réviseurs d'entreprises* (statutory auditors)

In accordance with the provisions of Article 27(3) of the law of 15 June 2004 relating to the investment company in risk capital (SICAR), the CSSF required, in two SICAR files, a *réviseur d'entreprises* to control one or several specific aspects of the activity and functioning of the SICAR concerned.

2.7. Publication of an FAQ

An FAQ document relating to SICARs will be published shortly on the CSSF's website.

SUPERVISION OF SECURITISATION UNDERTAKINGS

06

1. Developments in the sector of authorised securitisation undertakings
2. Prudential supervisory practice

1. DEVELOPMENTS IN THE SECTOR OF AUTHORISED SECURITISATION UNDERTAKINGS

During 2010, the CSSF received five applications for registration on the official list of authorised securitisation undertakings subject to the law of 22 March 2004 on securitisation.

The following three multiple-compartment securitisation undertakings were granted authorisation by the CSSF in 2010:

- Novus Capital Luxembourg S.A.
- Portfolio Solutions S.A.
- Micro, Small & Medium Enterprises Bonds S.A.

Further to the CSSF's request based on Article 25(2) of the law of 22 March 2004 on securitisation, the 1st vice-president of the Luxembourg district court, sitting in commercial matters, appointed KPMG ADVISORY S. à r.l., represented by Mr Eric Collard, on 11 February 2011 as provisional administrator (*administrateur provisoire*) of the authorised securitisation undertaking Lifemark S.A. for a period of three months from the delivery of the order, with the same rights and powers than those already granted to the provisional administrator by the orders of 11 February 2010 and 12 August 2010. This mandate supersedes and terminates the previous one granted by the court order of 12 August 2010.

As at 31 December 2010, 26 securitisation undertakings were registered on the official list of securitisation undertakings, as opposed to 23 entities at the end of 2009. Three application files of securitisation undertakings were still being processed at the end of 2010. The balance sheet total of authorised securitisation undertakings exceeded EUR 12.7 billion at the end of 2010, i.e. an increase of EUR 0.7 billion by comparison to 2009.

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

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

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

The CSSF expects securitisation activities to continue their slow but ongoing growth in 2011, a trend that is being confirmed by several application files that are currently under review.

2. PRUDENTIAL SUPERVISORY PRACTICE

In 2010, no changes have been made to the legal framework governing securitisation undertakings. However, as announced in its Annual Report 2009, the CSSF has analysed which lessons might be drawn from the financial crisis in terms of its function as the authorising and supervising body of securitisation undertakings, given that the role of securitisation techniques has been highlighted at several instances in the context of the financial crisis.

The CSSF has therefore reviewed certain general principles published in its Annual Report 2007 and an "FAQ" document providing an overview on the CSSF's prudential approach will be published shortly on its website.

- **On-site inspections**

In 2010, the CSSF carried out two on-site inspections at securitisation undertakings under its supervision so as to analyse, *inter alia*, the adequacy of their administrative and accounting organisation.

On-site inspections are an efficient tool for gathering and assessing the authorised securitisation undertakings' situation and practical functioning. This supervisory tool is therefore expected to be used more frequently.

SUPERVISION OF PFS

07

1. Developments of PFS in 2010
2. Prudential supervisory practice
3. Support PFS

1. DEVELOPMENTS OF PFS IN 2010

1.1. Major events in 2010

1.1.1. On-site inspections / introductory visits / meetings

The CSSF strengthened its presence in the field in 2010, by emphasising in particular, for a certain number of on-site inspections, control of compliance with the professional obligations as regards the fight against money laundering and terrorist financing. Besides on-site inspections on specific aspects of prudential supervision, the CSSF also made a certain number of introductory visits in newly authorised PFS. These meetings take place on the premises of the concerned PFS, usually within the first months following the ministerial authorisation. In the context of a closer control and enhanced communication that the CSSF wishes to establish, the meetings on the CSSF's premises with representatives of the supervised entities are an essential pillar of permanent supervision. Where shortcomings or other serious issues are detected by means of the different prudential supervisory instruments, the CSSF, after in-depth analysis, reserves the right to use the means of intervention laid down in the law of 5 April 1993 on the financial sector.

1.1.2. Statistics

As at 31 December 2010, 301 PFS were subject to the prudential supervision of the CSSF, employing 14,159 persons in total. This figure is certainly on the rise compared to the previous year, but it does not mean a net creation of as many new jobs. The balance sheet total of all PFS amounted to EUR 11,421 million as at 31 December 2010 against EUR 22,456 million at the end of December 2009, the value of this indicator being rather relative. These financial players also registered a fall, although less important, of their net results from EUR 1,577.04 million as at 31 December 2009 to EUR 1,452.30 million as at 31 December 2010.

1.2. Scope of the prudential supervision carried out by the CSSF

The following PFS fall under the scope of the prudential supervision of the CSSF:

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

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

1.3. Development in the number of PFS

The constant growth in the number of PFS subject to the supervision of the CSSF, observed since 2004, continues in 2010, even though it is less important than in previous years. The number of PFS rises from 286 as at the end of 2009 to 301 entities as at 31 December 2010. The number of entities which received authorisation in 2010 slightly decreased compared to the previous year (33 new entities in 2010 against 42 in 2009). Eighteen entities gave up their PFS status in 2010, compared to twenty-two entities having abandoned their status in 2009.

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

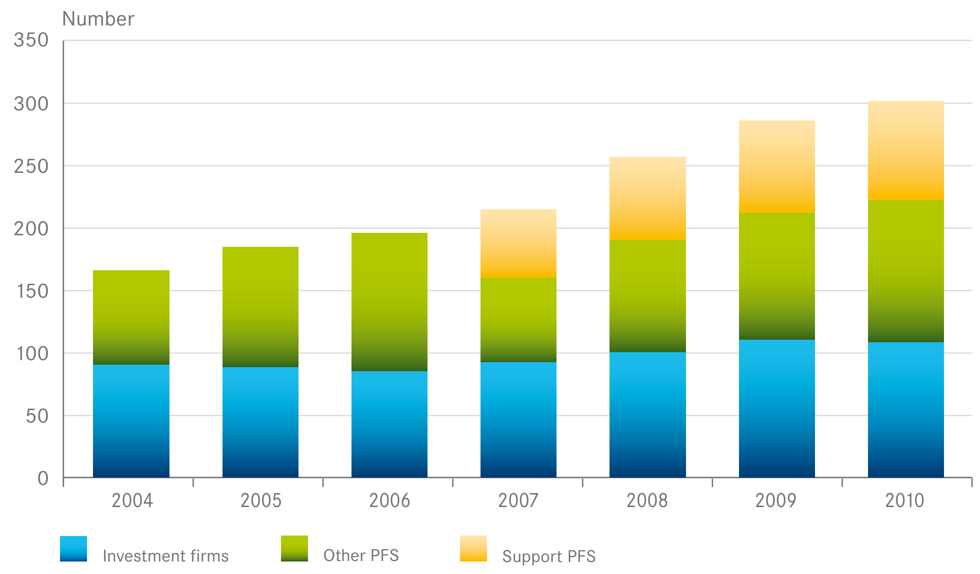
[2] Cf. footnote No. 1 above.

Development in the number of PFS

Year	Investment firms	Other PFS	Support PFS	Total
2004	90	76	/	**166**
2005	88	97	/	**185**
2006	85	111	/	**196**
2007	92	68	55	**215**
2008	100	90	67	**257**
2009	110	102	74	**286**
2010	109	113	79	**301**

The breakdown of PFS into investment firms, other PFS and support PFS shows that the positive development of the total number of PFS is mainly due to other PFS and, to a lesser extent, to support PFS. The number of investment funds remained stable, decreasing by only one entity.

Among the investment firms, the activity of private portfolio manager is most widely found with 74 entities carrying out this activity as at 31 December 2010.



1.4. Development in employment for PFS

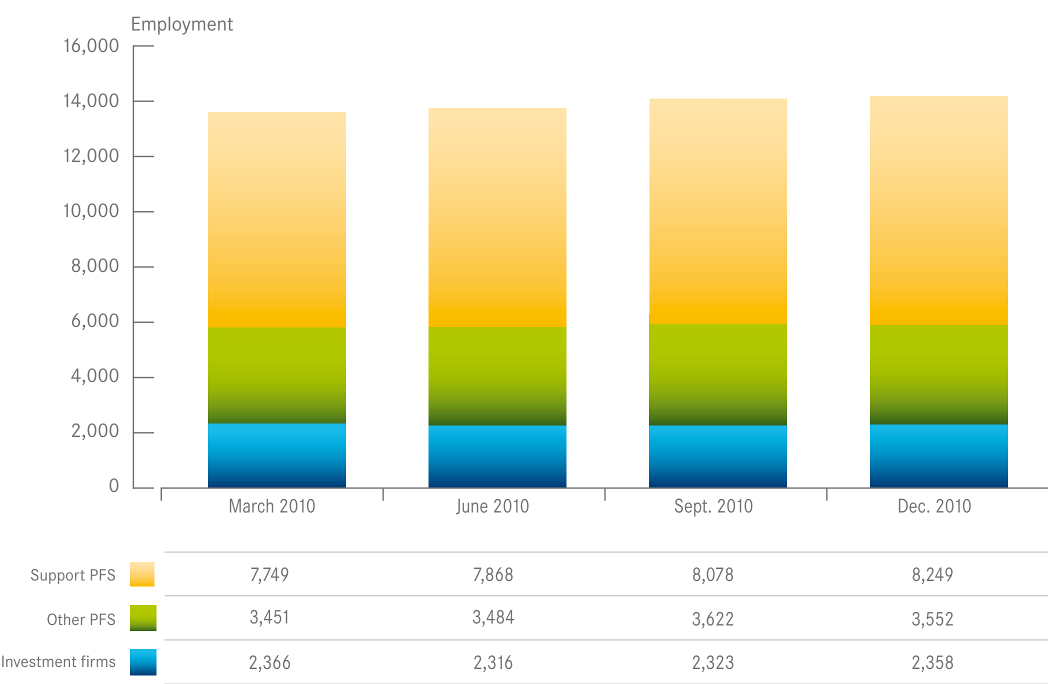
Following a decrease in employment in 2009, mainly due to the international economic crisis, total PFS employment rose from 13,485 at the end of 2009 to 14,159 persons as at 31 December 2010, i.e. an increase of 5% over a year.

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

Year	Number of PFS	Total staff
1995	78	1,827
1996	82	2,017
1997	80	2,323
1998	83	2,612
1999	90	2,788
2000	113	3,499
2001	145	4,176
2002	145	4,399
2003	142	4,455
2004	166	6,059
2005	185	6,547
2006	196	9,928
2007	215	12,174
2008	257	13,605
2009	286	13,485
2010	301	14,159[3]

[3] Preliminary figures.

Quarterly development of employment per PFS sub-groups



	March 2010	June 2010	Sept. 2010	Dec. 2010
Support PFS	7,749	7,868	8,078	8,249
Other PFS	3,451	3,484	3,622	3,552
Investment firms	2,366	2,316	2,323	2,358

Employment by investment firms remained almost stable over the year. The decrease in employment observed for a certain number of investment firms already operating before 2010 has indeed been offset, on the one hand, by the newly authorised entities in 2010 and, on the other hand, by the rise in employment within a very limited number of investment firms.

After a rise in employment throughout the first three quarters of the year, the other PFS recorded a drop in the last quarter, notably attributable to Fund Administration Services & Technology Network Luxembourg S.A., in abbreviated form “Fastnet”. It should be noted however that part of staff of this financial player was transferred to the banking branch BNP Paribas Securities Services established in Luxembourg and thus remains an integral part of the financial sector staff as a whole.

Only support PFS recorded constant growth in employment throughout the year. However, this rise must not be compared to a net creation of jobs within support PFS. Indeed, a large part of this rise is attributable to newly authorised PFS in 2010, among which are companies already active before. By extending their business to areas that need an authorisation as support PFS, the existing staff of these companies is included, after obtaining the authorisation, in the statistics relating to support PFS. The contrasting situation of support PFS already active before 2010 is also noteworthy: while a limited number of rather large-sized support PFS reduced their staff, others increased it.

1.5. Changes in the official list of PFS in 2010

1.5.1. Luxembourg PFS having started their activities in 2010

- **Investment firms**

Pursuant to Part I, Chapter 2, Section 2 of the law of 5 April 1993 on the financial sector, the following categories are defined as investment firms:

- investment advisers (Article 24);
- brokers in financial instruments (Article 24-1);
- commission agents (Article 24-2);
- private portfolio managers (Article 24-3);

- professionals acting for their own account (Article 24-4);
- market makers (Article 24-5);
- underwriters of financial instruments (Article 24-6);
- distributors of units/shares of UCIs (Article 24-7);
- financial intermediation firms (Article 24-8);
- investment firms operating an MTF in Luxembourg (Article 24-9).

Institutions cumulating one or more investment firm statuses with one or more other PFS and/or support PFS statuses are included in the table of investment firms below.

The following investment firms started their activities in 2010.

Name of the PFS	Start of business
Compagnie Financière Indépendante S.A.	January 2010
H CTG S.A.	March 2010
IW Lux S.à r.l.	January 2010
Lombard Intermediation Services S.A.	November 2010
Marguerite Adviser S.A.	September 2010
Merrill Lynch Equity S.à r.l.	July 2010

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• Other PFS

The following categories are considered as other PFS:

- registrar agents (Article 25);
- professional custodians of financial instruments (Article 26);
- operators of a regulated market authorised in Luxembourg (Article 27);
- currency exchange dealers (Article 28-2);
- debt recovery (Article 28-3);
- professionals performing credit offering (Article 28-4);
- professionals performing securities lending (Article 28-5);
- administrators of collective savings funds (Article 28-7);
- management companies of non-coordinated UCIs (Article 28-8);
- domiciliation agents of companies (Article 29);
- professionals performing services of setting-up and of management of companies (Article 29-5);
- professionals of the financial sector authorised to exercise any activity referred to in Part I, Chapter 2, Section 1 of the law of 5 April 1993 on the financial sector, with the exception of the categories of PFS also referred to in Section 2 of the same chapter;
- establishments authorised to exercise all the PFS activities permitted by Article 28 of the law of 15 December 2000 on postal services and financial postal services.

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

The following establishments started their activities in 2010.

Name of the PFS	Start of business
Apex Fund Services (Malta) Limited, Luxembourg branch	July 2010
Augentius Fund Administration (Luxembourg) S.A.	March 2010
BNP Paribas Real Estate Investment Management Luxembourg S.A.	February 2010
Custom S.A.	June 2010
Domiciliation + Services S.à r.l.	June 2010
Dominion Corporate Group S.A.	January 2010
Fund Solutions SCA	September 2010
Investyor Corporate Services S.A.	October 2010
IPES (Luxembourg) S.A.	August 2010
JTC (Luxembourg) S.A.	April 2010
Luxglobal Trust Services S.A.	January 2010
Orionis Management S.A.[4]	November 2010
Pandomus	October 2010
Reviva Capital S.A.	June 2010
Trident Fund Services (Luxembourg) S.A.	November 2010
Unsworth & Associates S.à r.l.	January 2010

- **Support PFS**

Support PFS are PFS authorised only as client communication agents (Article 29-1 of the law of 5 April 1993 on the financial sector), administrative agents of the financial sector (Article 29-2), primary IT systems operators of the financial sector (Article 29-3) or secondary IT systems and communication networks operators of the financial sector (Article 29-4), excluding any other PFS status. Entities cumulating one or several of those four statuses are also considered as support PFS.

The following support PFS started their activities in 2010.

Name of the PFS	Start of business
Altran Luxembourg S.A.	December 2010
AMS Systems PSF S.A.	March 2010
Aubay S.A.	February 2010
B2 HUB PSF S.A.	January 2010
FinAdmin E.I.G.	March 2010
Fujitsu Technology Solutions (Luxembourg) S.A.	July 2010
ICBS S.A.	September 2010
ISIWIS S.à r.l.	December 2010
Luxembourg E-Archiving S.A.	September 2010
Siemens Enterprise Communications S.A.	July 2010
Telindus S.A.	January 2010

[4] As it changed the activities it performs and in accordance with the change to its ministerial authorisation, Orionis Management S.A. (previously Bellatrix Investments S.A.) is not an investment firm anymore but an "other PFS".

1.5.2. PFS having abandoned their status in 2010

Eighteen institutions, including seven investment firms, abandoned their PFS status in 2010 for the following reasons:

- change or cessation of activities, so that the former PFS no longer requires an authorisation as such, because it does not fall under the scope of the law of 5 April 1993 on the financial sector anymore (7 entities)
  Arkai Luxembourg S.A.
  Fransad Gestion S.A.
  Fund Market S.A.
  IW Lux S.à r.l.
  Paribus Investment & Management S.à r.l.
  Veco Trust (Luxembourg) S.A.
  VR Netze Luxembourg S.à r.l.
- voluntary winding-up (1 entity)
  Auxilium Fund Services S.A.
- licence withdrawal by the Minister of Finance (1 entity)
  Damovo Managed Services Luxembourg S.à r.l.
- dissolution (1 entity)
  Corpus Sireo Financial Services S.A.
- merger (5 entities)
  HSH Asset Management S.A. (merger by takeover by HSH Nordbank Securities S.A.)
  HSH Investment Management S.A. (merger by takeover by HSH Nordbank Securities S.A.)
  Fujitsu Services PSF S.à r.l.
  Fujitsu Technology Solutions (Luxembourg) S.A.
  Telindus PSF S.A. (merger by takeover by the Luxembourg-incorporated entity Telindus)
- change into a credit institution (1 entity)
  Keytrade Luxembourg S.A.
- change into a payment institution governed by the law of 10 November 2009 on payment services (1 entity)
  SIX Pay S.A.
- closure of Aberdeen Asset Managers Limited, Luxembourg branch set up in Luxembourg in 2010 by an investment firm from the United Kingdom.

1.6. Development of balance sheets and profit and loss accounts

The provisional balance sheet total of all PFS established in Luxembourg reached EUR 11,421 million[5] as at 31 December 2010 against EUR 22,456 million as at 31 December 2009, i.e. an annual decrease of 49.14%. The important decrease over twelve month is mainly attributable to the decline in the business volume of a single entity authorised as professional performing lending operations.

Moreover, the financial players recorded a downward development of their net profits over a year, although to a lesser extent. Indeed, provisional net results amounted to EUR 1,452.30 million as at 31 December 2010[6] against EUR 1,577.04 million as at 31 December 2009, representing a drop of 7.91% in a year.

When taking into account the sub-groups “investment firms”, “other PFS” and “support PFS”, only other PFS registered a decrease in their net results compared to the figures of the previous year. This negative development is mainly attributable to two major players, whose net results decreased considerably year-on-year. A rise in net results however crystallises for support PFS and investment firms. Net results of most investment firms are either quite stable or grew slightly, and a reduced number of players even recorded a significant growth in net results compared to 2009 results.

[5] The figures of the ten branches included since 2009 in the total number of PFS are not included in these data.

[6] Cf. footnote No. 5 above.

Development of the balance sheet total and of the net results of PFS

(in mn EUR)	Balance sheet total				Net profits			
	2009		2010		2009		2010	
	Volume	Relative share	Volume	Relative share	Volume	Relative share	Volume	Relative share
Investment firms	1,132	5.1%	1,655	14.5%	170.6	10.8%	294.3	20.3%
Other PFS	20,147	89.7%	8,746	76.6%	1,376.7	87.3%	1,116.0	76.8%
Support PFS	1,177	5.2%	1,020	8.9%	29.8	1.9%	42.0	2.9%
Total	**22,456**	**100.0%**	**11,421**	**100.0%**	**1,577.0**	**100.0%**	**1,452.3**	**100.0%**

1.7. International expansion of PFS

1.7.1. Subsidiaries created and acquired abroad during 2010

In 2010, the investment firm European Value Partners Advisors S.à r.l opened a subsidiary in Switzerland.

1.7.2. Freedom of establishment

In 2010, three investment firms incorporated under Luxembourg law established a branch in Belgium based on the prinicple of freedom of establishment (European passport): Hottinger & Cie, Il PM Luxembourg S.A. and Opportunité Luxembourg S.A..

As at 31 December 2010, the following Luxembourg investment firms were represented in one or several EU/EEA countries by means of a branch.

Name of the PFS	Country of establishment of the branch
Assya Asset Management Luxembourg S.A. (previously MZ Finance S.A.)	Belgium
Belvall Capital S.A.	United Kingdom
Compagnie Financière et Boursière Luxembourgeoise S.A., in abbreviated form "Cofibol"	Belgium
Createrra S.A.	Belgium
European Fund Services S.A.	Germany Ireland
Farad Investment Advisor S.A.	Italy
Fuchs & Associés Finance S.A.	Belgium
Hottinger & Cie	Belgium
Il PM Luxembourg S.A.	Belgium
Luxembourg Financial Group S.A.	United Kingdom
Moventum S.C.A.	Austria Germany
Opportunité Luxembourg S.A.	Belgium
Orbit Private Asset Management S.A.	Belgium
Rhein Asset Management (Lux) S.A.	Germany
Skandia Invest S.A.	France
UBS Fund Services (Luxembourg) S.A.	Poland
Valbay International S.A.	Sweden
Vontobel Europe S.A.	Austria Italy Spain United Kingdom
WH Selfinvest S.A.	Belgium France Germany

In 2010, HSH Asset Management S.A. and HSH Investment Management S.A. gave up their PFS status and are not included on the list of Luxembourg investment firms having established a branch in one or more EU/EEA countries at the end of 2010 anymore. The branches established by Skandia Invest S.A. in Spain, SZL S.A. in Belgium and Vontobel Europe S.A. in Germany closed in 2010.

Three support PFS and one “other PFS” have a branch in an EU/EEA country as at 31 December 2010.

As regards non-EU/EEA countries, one investment firm and one “other PFS” incorporated under Luxembourg law are each represented through a branch in Switzerland.

The number of branches established in Luxembourg by investment firms originating from another EU/EEA Member State did not change year-on-year with ten entities as at 31 December 2010. It must be noted however that the UK branch Aberdeen Asset Managers Limited, which started its activities in Luxembourg during 2010, closed at the end of 2010.

EU/EEA branches established in Luxembourg as at 31 December 2010

Name of the branch	Country of origin
BNY Mellon Investment Servicing (International) Limited (previously PNC Global Investment Servicing (Europe) Limited)	Ireland
Eiger Securities LLP	United Kingdom
IG Markets Limited	United Kingdom
Morgan Stanley Investment Management Limited	United Kingdom
Nevsky Capital LLP	United Kingdom
PineBridge Investments Europe Ltd	United Kingdom
Superfund Asset Management GMBH	Austria
T. Rowe Price Global Investment Services Limited, in abbreviated form "TRPGIS"	United Kingdom
Thames River Capital LLP	United Kingdom
Tullett Prebon (Europe) Ltd	United Kingdom

1.7.3. Free provision of services

In 2010, twenty investment firms incorporated under Luxembourg law applied to pursue business in one or several EU/EEA Member States by way of free provision of services. The total number of investment firms which are active in one or more EU/EEA countries following a notification amounted to 62 entities as at 31 December 2010 (against 53 as at 31 December 2009). The majority of the investment firms concerned carried out their activities in several EU/EEA countries by way of free provision of services.

The total number of investment firms established in the EU/EEA and authorised to perform activities under the freedom to provide services within the Luxembourg territory amounted to 2,042 entities at the end of 2010 (against 1,807 entities as at 31 December 2009).

As at 31 December 2010, the global situation relating to free provision of services in or from the EU/EEA was as follows:

Country	Luxembourg investment firms providing services in the EU/EEA	EU/EEA investment firms providing services in Luxembourg
Austria	17	25
Belgium	41	16
Bulgaria	2	2
Cyprus	3	31
Czech Republic	4	1
Denmark	14	18
Estonia	3	1
Finland	10	5
France	34	70
Germany	32	83
Gibraltar	-	5
Greece	5	7
Hungary	6	2
Iceland	2	-
Ireland	7	52
Italy	21	7
Latvia	3	-
Liechtenstein	1	8
Lithuania	4	-
Malta	4	3
Netherlands	22	92
Norway	10	23
Poland	6	-
Portugal	6	4
Romania	3	-
Slovakia	3	1
Slovenia	3	2
Spain	19	15
Sweden	16	7
United Kingdom	18	1,562
Total number of notifications	**319**	**2,042**
Total number of investment firms concerned	**62**	**2,042**

The geographical breakdown of EU/EEA investment firms active by way of free provision of services in Luxembourg reveals that UK investment firms are by far the most important in number.

Similarly, among the 312 new notifications for free provision of services on the Luxembourg territory received in 2010 (increasing number as compared to the 267 new notifications in 2009), those originating from the United Kingdom represented a large majority. Apart from the United Kingdom, the entities that show considerable and ongoing interest in exercising their activities in Luxembourg by way of free provision of services are mainly from countries close to Luxembourg, like the Netherlands, France and Germany. A strong upward trend is confirmed for Cyprus which registered a growth of fifteen units in 2010.

The target countries of investment firms incorporated under Luxembourg law, whose total number of notifications amounted to 319 units as at 31 December 2010, are above all Luxembourg's neighbouring countries (Belgium, France and Germany). Luxembourg investment firms also show major interest in the Netherlands, Italy and the United Kingdom.

2. PRUDENTIAL SUPERVISORY PRACTICE

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

2.1. Instruments of prudential supervision

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

- financial information periodically submitted to the CSSF enabling it to continuously monitor the activities of PFS and the inherent risks, and, as regards investment firms, to perform a periodic supervision of the capital adequacy ratio and large exposure limits as laid down in Article 56 of the law of 5 April 1993 on the financial sector;
- the annual report drawn up by the *réviseur d'entreprises* (statutory auditor) (including a certificate relating to the fight against money laundering; as regards investment firms, the auditor's report shall moreover include a certificate concerning compliance with the rules of conduct in the financial sector as well as a description and a comment on the Compliance function in accordance with Circular CSSF 04/155);
- the internal audit reports relating to audits carried out during the year and the management's report on the state of the internal audit of the PFS;
- on-site inspections carried out by the CSSF.

2.2. On-site inspections

The CSSF attaches particular importance to this instrument of prudential supervision, as it allows a global and direct view of the situation and functioning of the PFS in practice. On-site inspections also allow to better control and monitor one or more specific aspects of prudential supervision. On-site inspections were carried out jointly with the department "General supervision".

In 2010, the CSSF continued to strengthen its field presence by carrying out, in addition to on-site inspections, a certain number of introductory visits of newly authorised PFS. These visits generally take place on the premises of PFS within the first months following the ministerial authorisation and allow to immediately verify the data and information received in the application files. Compliance with regulatory requirements and the implementation of adequate procedures are other issues broached during introductory visits. During the introductory visits and the other on-site inspections made during 2010, the CSSF laid specific emphasis on the control of compliance with professional obligations regarding the fight against money laundering and terrorist financing.

2.2.1. Investment firms

During the year under review, the CSSF carried out on-site inspections in thirteen investment firms, including one visit in an EU branch established in Luxembourg.

This figure includes seven on-site inspections focusing on compliance with professional obligations regarding the fight against money laundering and terrorist financing and three introductory visits with newly authorised investment firms.

In addition, one on-site inspection concerned the verification of specific aspects of prudential supervision, such as the organisational structure, the activities performed and the monitoring of adequate implementation of the recommendations issued by the internal auditor. Another visit concerned the adjustment of the investment firm's business plan.

The on-site inspection of one branch from another EU/EEA Member State established in Luxembourg concerned the scope of the activities performed and the compliance of the infrastructure with Article 17 of the law of 5 April 1993 on the financial sector.

2.2.2. Other PFS

In 2010, the CSSF performed eighteen on-site inspections of other PFS, including eight missions in relation to compliance with professional obligations as regards the fight against money laundering and terrorist financing and seven introductory visits with newly authorised entities. As regards one of these new entities, the CSSF considered that it needed to perform a second mission notably on the procedures laid down and the compliance with professional obligations as regards the fight against money laundering and terrorist financing.

Moreover, three on-site inspections focused on specific points detected through prudential supervision, i.e. one mission for monitoring the regularisation of deficiencies observed during an introductory visit in 2009 and two missions relating to activities performed by the entities concerned.

2.3. Meetings

During the year under review, a total of 120 meetings in relation to PFS activities took place on the CSSF's premises. 83 of these meetings concerned the department "Supervision of investment firms" and 37 meetings the department "Supervision of other PFS". In the context of closer control aimed at by the CSSF, meetings, preferably on an annual basis, with the financial players subject to its supervision become increasingly important to the CSSF.

During 2010, meetings with PFS representatives covered the following areas:

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

2.4. Specific controls

Article 54(2) of the law of 5 April 1993 on the financial sector entitles the CSSF to require a *réviseur d'entreprises* (statutory auditor) to carry out a specific audit at a financial professional, covering one or several specific aspects of the business or operation of the entity concerned. The ensuing costs are to be borne by the professional concerned. The CSSF has formally made use of this right once in 2010.

2.5. Supervision on a consolidated basis

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

The CSSF carries out supervision on a consolidated basis for investment firms falling under the scope of application of the above-mentioned law. An in-depth study of the financial groups to which most investment firms belong is required in order to determine whether, at what level and in what form, consolidation should apply. For the investment firms concerned, Circular CSSF 00/22 on the supervision of investment firms on a consolidated basis specifies the practical aspects of the rules as regards this type of supervision.

As at 31 December 2010, the following nine investment firms are submitted to the supervision on a consolidated basis by the CSSF:

- Brianfid-Lux S.A.
- CapitalatWork Foyer Group S.A.
- Crédit Agricole Luxembourg Conseil S.A., in abbreviated form "CAL Conseil"
- European Value Partners Advisors S.à r.l.
- FIL (Luxembourg) S.A.
- Fuchs & Associés Finance S.A.
- Fund Channel S.A.
- Hottinger & Cie
- Petercam (Luxembourg) S.A.

3. SUPPORT PFS

Support PFS include financial professionals which have been authorised only under Articles 29-1, 29-2, 29-3 and/or 29-4 of the law of 5 April 1993 on the financial sector. The term "support PFS" originates from non-financial market players who wanted to be distinguished from so-called "traditional" financial PFS. The characteristic of support PFS is that they do not receive deposits from the public and mainly act as subcontractors of operational functions on behalf of other financial professionals.

3.1. Development in the number of support PFS

In 2010, the total number of support PFS increased slightly from 74 entities as at 31 December 2009 to 79 as at 31 December 2010.

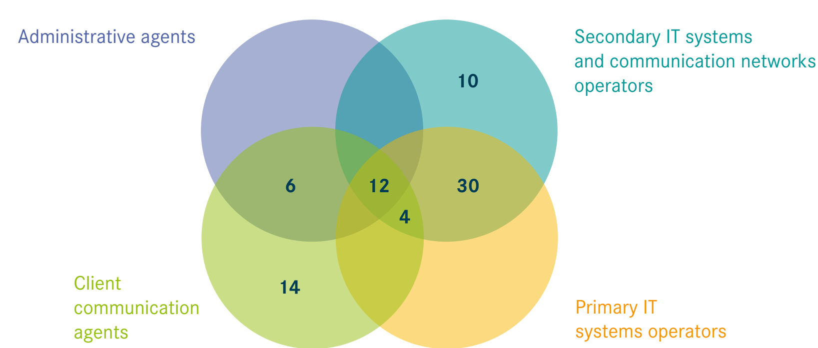
The following eleven new support PFS received authorisation in 2010[7]:

- two client communication agents and secondary IT systems and communication networks operators of the financial sector (ACC - OSIS);
- three primary IT systems operators of the financial sector and secondary IT systems and communication networks operators of the financial sector (OSIP - OSIS);
- four secondary IT systems and communication networks operators of the financial sector (OSIS);
- two entities cumulating the statuses of client communication agent, administrative agent of the financial sector, primary IT systems operator of the financial sector and secondary IT systems and communication networks operator (ACC - AA - OSIP - OSIS).

Six support PFS were withdrawn from the official list in 2010: three entities following mergers, one entity due to voluntary liquidation, one entitiy abandoned its activities and one entity from which the authorisation was withdrawn by the Minister of Finance for non-compliance with the legal and regulatory framework.

[7] Cf. point 1.5.1. above.

As at 31 December 2010, the 79 support PFS fall under the following categories:



Client communication agents + secondary IT systems and communication networks operators: 2 entities

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

3.2. Development in support PFS employment

The staff of support PFS rose from 7,481 units as at 31 December 2009 (74 active entities) to 8,249 units as at 31 December 2010 (79 active entities), representing an annual rise of 768 units. This rise is mainly due to newly authorised support PFS over the year[8].

Situation of employment in support PFS

	2009			2010[9]			Variation
	Luxembourg	Foreigners	**Total**	Luxembourg	Foreigners	**Total**	
Executives	117	345	**462**	132	409	**542**	16.3%
Office staff	919	5,183	**6,102**	958	5,760	**6,719**	10.1%
Technical staff	127	790	**917**	126	865	**991**	8.1%
of which part-time	*69*	*593*	***662***	*68*	*728*	***795***	*20.1%*
TOTAL	**1,163**	**6,318**	**7,481**	**1,217**	**7,032**	**8,249**	**10.3%**
of which men	944	4,898	**5,842**	1,000	5,397	**6,397**	9.5%
of which women	219	1,420	**1,639**	217	1,635	**1,852**	13.0%

[8] Cf. point 1.4. above.
[9] Preliminary figures.

3.3. Prudential supervisory practice for support PFS

The prudential supervision of support PFS is ensured by the department "Information systems and supervision of support PFS" which covers all technological aspects, i.e. information systems of the CSSF, including the coordination of the users' needs and the supervision of information systems supporting other supervisory departments, security of information systems and supervision of support PFS.

3.3.1. Introductory visits

The purpose of the introductory visits, which usually take place within the first six months as of the authorisation, is twofold. On the one hand, a meeting is organised between the persons in charge of the day-to-day management of the PFS and the persons in charge of the supervision of support PFS in order to encourage a constructive and efficient dialogue. On the other hand, these visits ensure that the information transmitted in the application file are in accordance with the practical application within the PFS. Among other things, the CSSF verifies that the central administration is set up and exists in Luxembourg, and that there is an internal control set up within the PFS. These points are two of the key elements for efficient corporate governance.

Introductory visits also allow correcting possible shortcomings or deficiencies at the start of the PFS's activities.

Thus, in 2010, the division in charge of the prudential supervision of support PFS carried out twelve introductory visits at PFS newly authorised during that year.

3.3.2. On-site inspections

On-site inspections were carried out at three entities showing serious breaches of the applicable law or circulars. The CSSF will pursue the efforts in this area by systematically performing, in the years to come, on-site inspections every time a breach is observed. The CSSF uses, among other things, the reports issued by the internal auditor and the *réviseur d'entreprises* (statutory auditor) to detect any breaches.

Following one of the controls made in 2010, one support PFS had its authorisation withdrawn.

3.3.3. Requirement to have a contract justifying the authorisation and reminder of the notion of body shopping and providing staff

Every support PFS that wishes to perform a regulated financial sector activity needs an authorisation from the Minister of Finance. As soon as the authorisation is granted, the support PFS may immediately start to provide its services in the financial sector.

Article 23(1) of the law of 5 April 1993 on the financial sector states that "the authorisation shall be withdrawn if the PFS does not make use of the authorisation within twelve months after granting, expressly renounces the authorisation or has performed no financial activity, nor a connected or complementary activity listed in sub-section 3 of section 2 of this chapter for the preceding six months."

The existence of a service contract justifying the authorisation of the support PFS is checked twice by the CSSF. Firstly, the CSSF systematically requires all the support PFS on the official list to provide at least one service contract in order to justify their authorisation. Secondly, the reporting to be provided periodically by the support PFS, in particular *ad hoc* tables II.17 and II.18 reveal if the PFS has a contract, for what activity and with what category of financial player. The contract must accurately stipulate the activity provided and the obligations and responsibilities of every contracting party.

Indeed, the CSSF needs to make sure that the support PFS really exercises a regulated activity for the account of a professional of the financial sector and, beyond verifying compliance with Article 23(1), prevent that the authorisation is only requested to reassure the professionals of the financial sector using the services of the support PFS that the latter is supervised by the CSSF.

Based on information received, the CSSF noted that a certain number of support PFS provide an activity of staff supply which does not need to be authorised as support PFS. A fixed-term contract by which a support PFS provides IT experts to its contracting party, by ensuring in the contract a best efforts obligation and not a performance obligation, must not be considered, *a priori*, as a contract justifying the authorisation. This practice, also known as body shopping, is explained in Circulars CSSF 06/240 and 05/178 on administrative and accounting organisation under the point relating to outsourcing of IT services.

The CSSF reminds that supplying expert profiles for activities determined by the customer is not equivalent to sub-contracting operations by transferring the responsibility to the provider. The fact that an employee of a provider fulfils system administration tasks does not mean that the provider takes on the responsibility of the system operation as a legal person.

Consequently, if the signed contract does not convince the CSSF of the rightfulness of the authorisation granted, the CSSF reserves the right to request the support PFS to provide a new contract or to express its clauses more precisely in terms of activities provided and responsibility. If there is no contract justifying the authorisation, the CSSF will request the Minister of Finance to withdraw the authorisation.

3.3.4. Roles and responsibilities of the management in charge of day-to-day management

The CSSF had already broached the subject of the responsibility of managers in charge of day-to-day management in its 2008 Annual Report from the point of view of a limited company (*société à responsabilité limitée*). For several years, the transversal organisation of large groups, enhanced by the effect of globalisation, contributed to the fact that decisions taken at group level (in the broad sense) be imposed to the local Luxembourg players. In this context, it is important to define the limit from which it is not the local management that decides but the group that imposes its own decisions. The following question thus arises: to what extent is the local management responsible for decisions which have been taken at group level but come up against the Luxembourg legislation?

According to common practice, members of the board of directors delegate their management powers in accordance with Article 60 of the law of 10 August 1915 on commercial companies to managers who also become representatives of the board. The board of directors sets the scope of the mandate in compliance with the general terms of the mandate laid down in the Civil Code.

Practice is however noticeably different from theory. The board of directors indeed delegates day-to-day management to managers and determines the scope of their powers, but this delegation often lacks transparency so that the Luxembourg management is unable to go against a decision imposed by the group.

This can have two undesirable effects:

- compliance with Article 19(2) of the law of 5 April 1993 on the financial sector according to which “the management must be empowered to effectively direct the business” is called into question;
- decisions are imposed on the managers which are contrary to Luxembourg legislation, while they are fully liable.

The CSSF should therefore reach the conclusion that the management does not have the required means to fulfil its management mission and that it is unable to achieve compliance with the Luxembourg legal and regulatory framework. These two points should logically call into question the authorisation granted to the support PFS.

In some cases, the CSSF observed that important decisions that have an impact on support PFS, are taken unilaterally by the group in the broad sense without taking into account the regulatory specificities of Luxembourg. The CSSF has also analysed cases in which the Luxembourg management admits ignoring to some extent the sub-contracted activities to the group, or even its inability to impose compliance with Luxembourg regulatory aspects. Finally, the CSSF was confronted with sizeable cuts in support PFS staff, decided at group level and going against the interest of support PFS customers, without the local management having been able to give its opinion on the matter.

Introducing into the law the liability of the legal person, as well as the sanctions that might arise therefrom, is a first step in the sense that a financial sanction could be imposed directly on the company in its own name and not solely on the members of the board of directors or on those in charge of day-to-day management.

Another way to intervene would be to make mandatory the setting-up of corporate governance principles that clearly define the competences of the management and the scope of the powers necessary for the proper achievement of the mission delegated by the board of directors. Corporate governance arrangements already exist for listed companies as they allow giving the members of the board of directors the means to assume their responsibilities and obligations. The level of granularity must be defined in the management mandate given by the board of directors to the persons in charge of the day-to-day management, thus delimiting a perimeter.

3.3.5. Market development: from a SaaS model to a BPO model

In response to the recent financial crisis, the CSSF observed in 2010 that an increasing number of financial professionals wished to restructure in order to focus more particularly on their core business and tend to use Business Process Outsourcing (BPO) more extensively. This practice consists in sub-contracting to an external provider not only a specific task of a process, but the process as a whole. This type of sub-contracting allows the financial professional to control costs and benefit from economies of scale made by its provider when offering BPO services to several companies by mutualising its tools and resources.

Instead of investing in the necessary technical infrastructures and human resources to be able to set up a process, the financial professional may thus use a BPO and thereby change the nature of its expenses. By using a BPO, the professional transforms indeed its capital expenditure (CAPEX) into operational expenditure (OPEX).

Similarly, the CSSF observed that solutions involving operating sub-contracting (SaaS - Software as a Service) tended to become solutions involving full process outsourcing (BPO). Where the service provided extends beyond the simple provision of IT services (e.g. sub-contracting of back-office services), the service provider needs to obtain an additional authorisation as administrative agent of the financial sector (Article 29-2 of the law of 5 April 1993 on the financial sector). This development has also been noticed in the framework of the authorisation files reviewed in 2010. Applications for authorisation as operator (Articles 29-3 and 29-4) are more and more filed together with applications for authorisation as client communication agent (Article 29-1) or administrative agent (Article 29-2).

3.3.6. Facilities Management

The Luxembourg Facilities Management market was blooming over the last years and the Facilities Manager (FM) succeeded in standing out as a major actor with large groups of the financial centre. As its role has changed, its scope of action needs to be defined. The FM may be defined as a solution for the management and coordination of the support activities of a company. These activities comprise areas of energy, maintenance of installations, real estate, security as well as environment. Delegating the management of these functions thus allows a company not only to refocus on its core business, but also to benefit from the advantages of outsourcing. Unlike a so-called “traditional” external provider, the requirements of a company that wish to use an FM are different in that it also seeks to optimise costs. As a professional, the FM must be able to be proactive, but also preventive in the management and coordination of all the processes it has been entrusted with. Owing to its know-how and its deeper market knowledge, the companies expect a real added value from the FM. The emergence of these new actors has thus led the European Committee for Standardization to lay down a certain number of standards in order to provide a regulated framework for the profession, but also to promote transparency on the international market of FMs and intervening parties.

However, the boom of Facilities Management on the Luxembourg market led the CSSF to raise a certain number of questions directly connected to the core of the FM function linked to the support PFS. It must be borne in mind that FMs, whether they are located in Luxembourg or abroad, are not subject to the supervision of the CSSF. Therefore, a contract signed between a support PFS and an FM, where the latter is chosen as prime contractor by its financial sector client, raises legal problems. On the one hand, the support PFS may not use the argument of a financial sector contract to justify its authorisation. On the other hand, the FM should have an authorisation, but as it does not provide the service itself, may not be granted said authorisation. The prime contractor must indeed have all the authorisations itself for the support PFS activities it outsources and must carry out itself at least one support PFS activity, at the same time as justifying to the CSSF the cascading outsourcing. An easier alternative in terms of contractual requirements would be to sign a contract directly between the support PFS and the FM's financial sector client.

The CSSF thus strongly recommends support PFS to pay special attention to the content of their service agreements and to check not only the exact nature of the services provided, but also the identity of the co-contracting parties.

SUPERVISION OF SECURITIES MARKETS

08

1. Approval of prospectuses relating to offers to the public or admissions to trading on a regulated market
2. Takeover bids
3. Supervision of issuers whose securities are admitted to trading on a regulated market and for which the CSSF is the competent authority pursuant to the Transparency law
4. Supervision of markets and market operators
5. Investigations and cooperation
6. Developments in the regulatory framework

1. APPROVAL OF PROSPECTUSES RELATING TO OFFERS TO THE PUBLIC OR ADMISSIONS TO TRADING ON A REGULATED MARKET

1.1. Application of the Prospectus law

The number of files submitted in 2010 for the approval of prospectuses to be published when securities are offered to the public or admitted to trading on a regulated market remained stable compared to 2009.

Since the entry into force of the law of 10 July 2005 on prospectuses for securities ("Prospectus law"), the department "Supervision of securities markets", in charge of ensuring the application of the Prospectus regulations, continuously fostered communication with the filing entities, as this allows reducing the timing for the processing of their files. This aspect is essential in order to allow issuers to benefit from the opportunities given on the financial markets. In 2010, 162 requests for advice were submitted to this department, most of which were related to the preliminary study of the structure of the application files before their official filing. Some positions taken by the CSSF in the context of these requests are detailed under point 1.3. of this Chapter.

As compared to the previous years, less requests for the omission of information pursuant to Article 10 of the Prospectus law have been received in 2010. Indeed, their number came down to ten requests in 2010, only six of which have been granted. This decrease can be explained by the fact that many filing entities preferred to contact the CSSF for information before submitting their file and decided to take the necessary actions in order to provide the information requested.

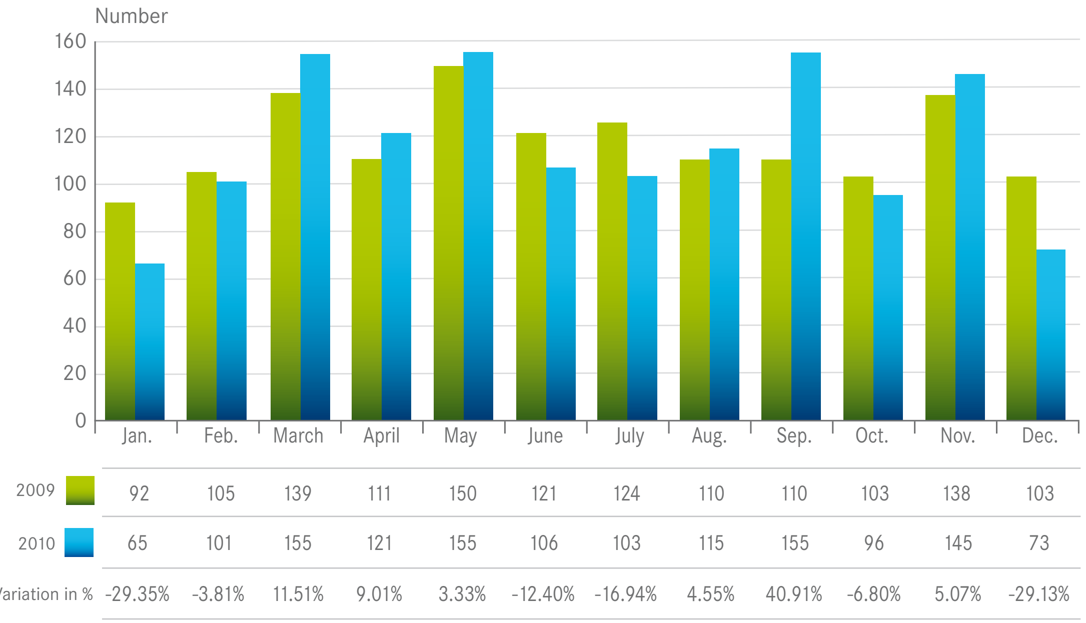
Moreover, and in accordance with Article 23.4 of Regulation (EC) No 809/2004 (Prospectus regulation), the CSSF approved five prospectuses subject to information omission due to non-pertinence.

1.2. Approvals and notifications in 2010

1.2.1. Documents approved by the CSSF in 2010

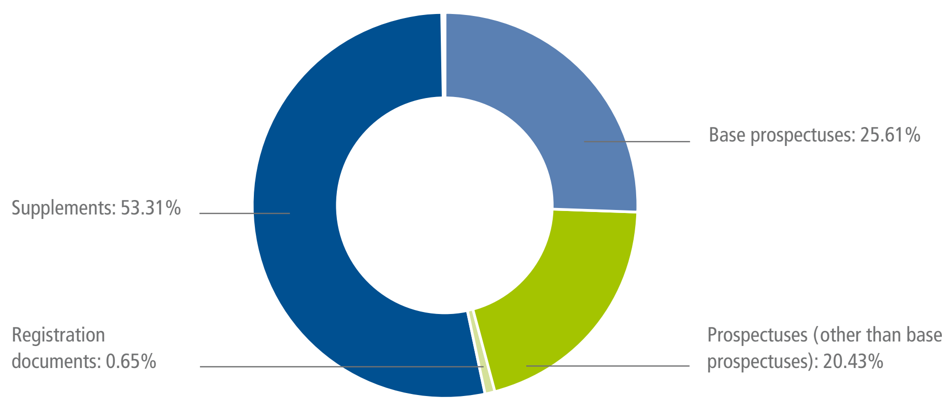
The number of documents approved by the CSSF slightly decreased compared to 2009, amounting to a total of 1,390 approved documents in 2010 (of which 284 prospectuses, 356 base prospectuses, 9 registration documents and 741 supplements) against 1,406 the previous year (-1.14%).

Development in the number of documents approved by the CSSF



	Jan.	Feb.	March	April	May	June	July	Aug.	Sep.	Oct.	Nov.	Dec.
2009	92	105	139	111	150	121	124	110	110	103	138	103
2010	65	101	155	121	155	106	103	115	155	96	145	73
Variation in %	-29.35%	-3.81%	11.51%	9.01%	3.33%	-12.40%	-16.94%	4.55%	40.91%	-6.80%	5.07%	-29.13%

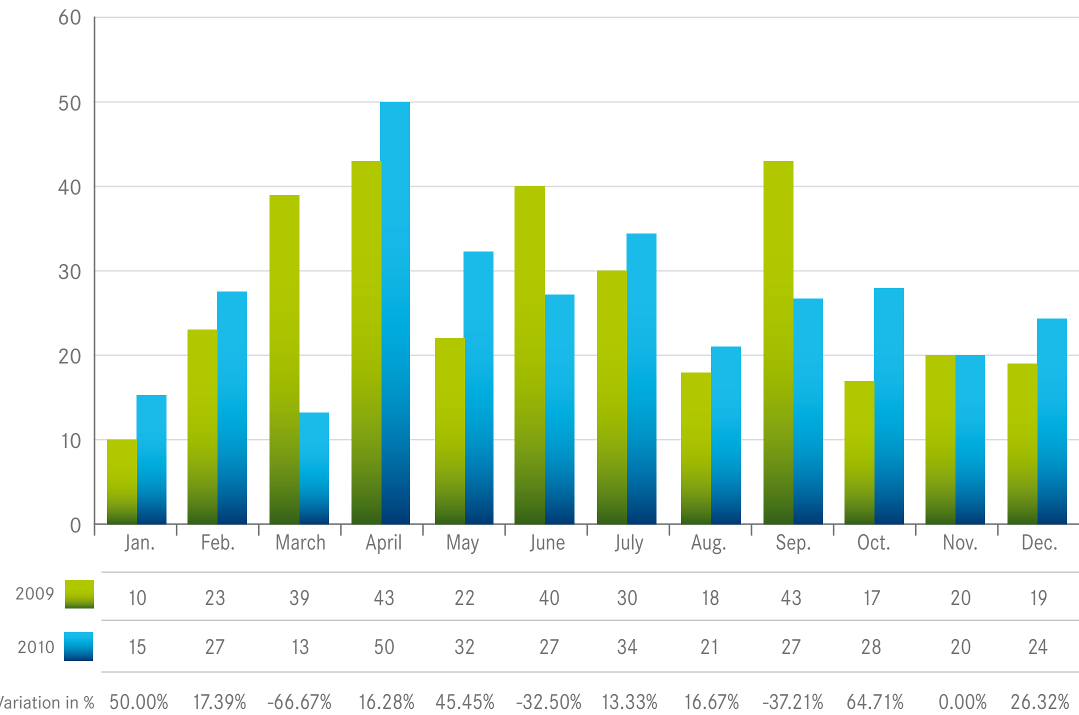
Distribution of documents approved in 2010



1.2.2. Documents drawn up under the European passport regime in 2010

In 2010, the CSSF received 1,062 notifications (relating to 318 prospectuses and base prospectuses and 744 supplements) from the competent authorities of several EU Member States, against 1,292 notifications (relating to 324 prospectuses and base prospectuses and 968 supplements) in 2009, representing a 17.80% decrease.

Development in the number of notifications (prospectuses and base prospectuses) received by the CSSF

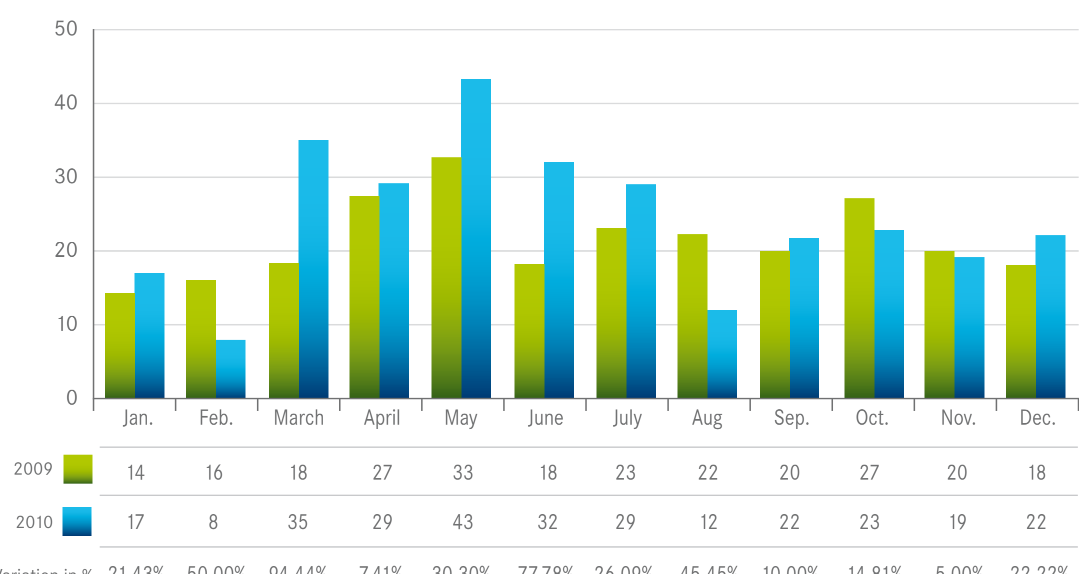


	Jan.	Feb.	March	April	May	June	July	Aug.	Sep.	Oct.	Nov.	Dec.
2009	10	23	39	43	22	40	30	18	43	17	20	19
2010	15	27	13	50	32	27	34	21	27	28	20	24
Variation in %	50.00%	17.39%	-66.67%	16.28%	45.45%	-32.50%	13.33%	16.67%	-37.21%	64.71%	0.00%	26.32%

In 2010, the CSSF sent notifications for 715 CSSF-approved documents (291 prospectuses and base prospectuses and 424 supplements) to the competent authorities of the EU Member States, against 691 documents[1] (256 prospectuses and base prospectuses and 435 supplements) in 2009, which is a 3.47% increase.

[1] This figure is the number of documents for which the CSSF sent one or several notifications. Where notifications have been sent at different dates and/or in several Member States, only the first notification is included in the statistical calculations. Each document notified in one or several Member States is thus only counted once.

Development in the number of notifications (prospectuses and base prospectuses) sent by the CSSF



	Jan.	Feb.	March	April	May	June	July	Aug	Sep.	Oct.	Nov.	Dec.
2009	14	16	18	27	33	18	23	22	20	27	20	18
2010	17	8	35	29	43	32	29	12	22	23	19	22
Variation in %	21.43%	-50.00%	94.44%	7.41%	30.30%	77.78%	26.09%	-45.45%	10.00%	-14.81%	-5.00%	22.22%

1.2.3. Approvals

In 2010, the CSSF approved 165 files relating to Luxembourg issuers, among which 48 prospectuses and 47 base prospectuses. 49 of such prospectuses and base prospectuses – i.e. more than 50% - referred to securitisation transactions.

Among the special files, it is worthwhile mentioning the approval of a prospectus relating to the admission to trading of the shares of a new Luxembourg entity, APERAM, created from the split of the stainless steel branch of ArcelorMittal.

1.2.4. Filing and control of the "Final Terms"

The CSSF continued to perform *a posteriori* random controls on the Final Terms that have been filed in 2010. As no improvement could be noticed in the content nor in the obligation to file the Final Terms, the CSSF decided to intensify its *a posteriori* controls and will take, where applicable, the necessary measures and sanctions.

1.2.5. Filing a notification request after the approval of a prospectus

In most cases, the notification request in relation to a prospectus is filed with the CSSF together with the filing of the draft prospectus. This allows the readers in charge of the review of the files to ensure that, in accordance with the Prospectus regulations, all elements required for an offer to the public in the host Member States concerned are included in the project of the prospectus. However, more and more often notification requests are being filed after the approval of the prospectus. In such cases, the CSSF requests the issuers concerned to confirm that the prospectus contains all information required for an offer to the public or admission to trading in the relevant host Member States. If such confirmation cannot be given, the missing elements must be submitted *via* a supplement to be approved by the CSSF before the notification. Where, pursuant to Article 13 of the Prospectus law, the publication of a supplement is no longer possible, the issuer concerned must request the approval of a new prospectus for an offer to the public or admission to trading in the concerned Member States. As a consequence, it is highly recommended that filing entities perform the necessary verifications when filing the draft prospectus.

1.3. Questions regarding prospectuses raised in 2010

1.3.1. Rules applicable to Islamic debt securities

In January 2011, the CSSF added FAQ No. 66 to its FAQs on the new prospectus regime in order to detail the rules applicable to Islamic debt securities, also known as "sukuk". The CSSF considers that sukuk may be treated as asset backed securities pursuant to the provisions of Article 2.5 of the Prospectus regulation or, subject to certain conditions, as guaranteed debt securities pursuant to Article 23.2 and Annex VI of the Prospectus regulation. Indeed, provided that the payments of principal and periodic revenues under the securities are guaranteed on a contractual basis by one or more underlying entity(ies), in other words, if the payment of principal and the periodic distributions are independent from the performance of the underlying asset, the CSSF considers that the underlying entity(ies) may be described in accordance with the provisions of Annex VI of the Prospectus Regulation.

1.3.2. Repurchase or exchange offer on debt securities

In 2010, the CSSF received several requests concerning the possibility to limit a repurchase or exchange offer on debt securities only to qualified investors. For the issuers concerned, such limitation notably exempts them from drafting a prospectus pursuant to Article 5.2 of the Prospectus law.

Pursuant to Article 17(1) of the law of 11 January 2008 on transparency requirements for issuers of securities ("Transparency law"), an issuer of debt securities admitted to trading on a regulated market for which Luxembourg is the home Member State under the Transparency Directive shall ensure that all holders of debt securities ranking *pari passu* are given equal treatment in respect of all the rights attaching to those debt securities. In the context of repurchase or exchange offers on debt securities by or on behalf of the issuer, the CSSF clarified that it considers that "rights attaching" to the debt securities referred to under Article 17(1) of the Transparency law do not include the right of a holder to be concerned by an offer where securities are repurchased by or on behalf of the issuer. The issuer must however comply, where applicable, with the provisions applicable (including those relating to the notification requirements) laid down in the law of 9 May 2006 on market abuse.

2. TAKEOVER BIDS

2.1. Offer documents approved by the CSSF

In 2010, the CSSF did not have to approve or recognise any offer document related to takeover bids under the law of 19 May 2006 implementing Directive 2004/25/EC of 21 April 2004 on takeover bids (law on takeover bids).

2.2. Questions regarding the law on takeover bids raised in 2010

In 2010, several information requests regarding transactions likely to fall under the scope of application of the law on takeover bids concerned the practical application of the concept of change of control linked to restructuring or reorganisation transactions. In its answers, the CSSF considered the nature of the change, i.e. whether it was a material change of the control situation on a given company or a mere formal change in the shareholder structure not affecting minority shareholders.

In this context, the CSSF would like to remind that, as a general rule, the two conditions set out in Article 5(1) of the law on takeover bids, i.e. acquiring and obtaining control, must both be cumulatively met for the law on takeover bids to apply. Where the restructuring of a company is limited to a formal change in the shareholder structure, the CSSF is indeed of the opinion that the transaction does not trigger the obligation to launch a takeover bid pursuant to Article 5(1) of the law on takeover bids and that no derogation is required under this law.

In the context of the reorganisation of a Luxembourg company, the CSSF granted a derogation to the obligation to launch a takeover bid in accordance with Article 4(5) of the law on takeover bids. The CSSF considered that this reorganisation would not harm the rights or interests of minority shareholders of the company concerned and that the operation would thus not require a specific protection of minority shareholders under the law on takeover bids.

3. SUPERVISION OF ISSUERS WHOSE SECURITIES ARE ADMITTED TO TRADING ON A REGULATED MARKET AND FOR WHICH THE CSSF IS THE COMPETENT AUTHORITY PURSUANT TO THE TRANSPARENCY LAW

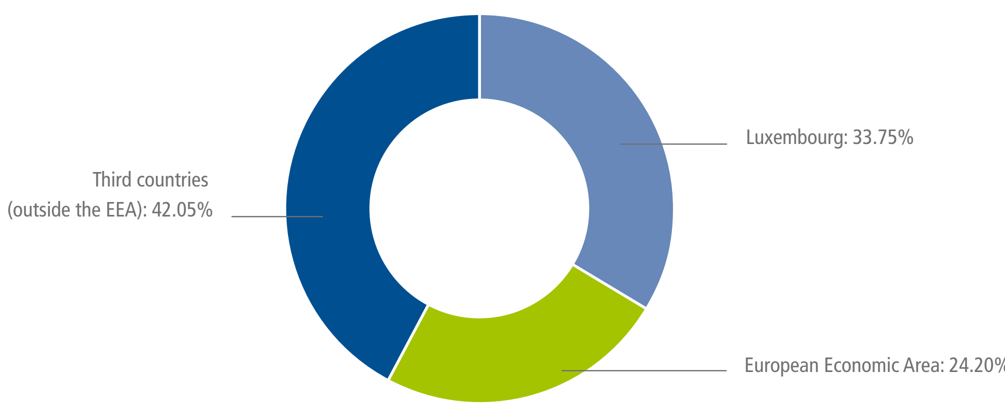
3.1. Supervised issuers

Pursuant to the Transparency law, the CSSF supervises the issuers which fall within the scope of this law. As at 14 March 2011, 723 issuers fell under the supervision of the CSSF as Luxembourg was their home Member State within the meaning of this law. In 2010, Luxembourg has been confirmed as the home Member State for 65 issuers, whereas 102 issuers no longer fall within the scope of the Transparency law, mainly as the securities issued by those entities matured or were redeemed early. The list of issuers supervised by the CSSF is published on the CSSF website (heading "Supervised entities").

244 of the 723 issuers supervised by the CSSF are Luxembourg issuers, of which 49 issuers of shares and one issuer whose shares are represented by Fiduciary Depositary Receipts admitted to trading on a regulated market. Among the Luxembourg issuers, twelve are securitisation undertakings authorised pursuant to Article 19 of the law of 22 March 2004 on securitisation and fourteen are banks.

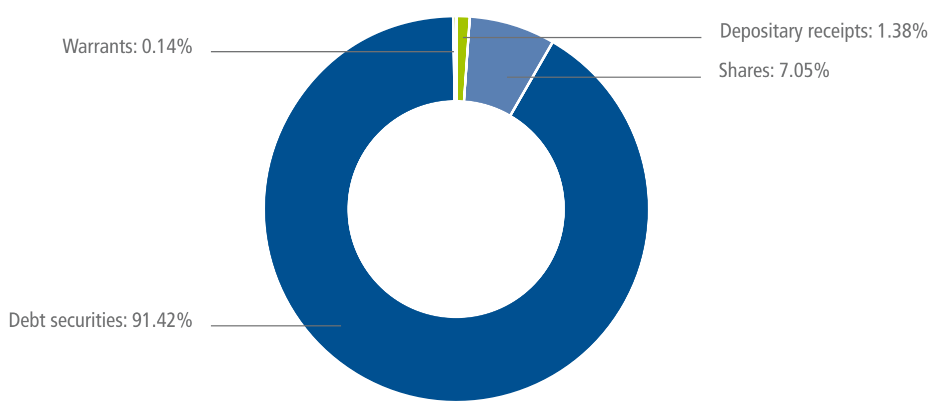
175 issuers have their registered office in a Member State of the European Economic Area (EEA) and 304 issuers are registered in a third country (outside the EEA).

Breakdown of issuers according to country



As regards the breakdown according to the type of securities listed, a vast majority of issuers subject to the supervision of the CSSF, i.e. 661 entities, issue debt securities.

Breakdown of issuers according to type of securities admitted to trading



3.2. Determination of the home Member State

In 2010, the CSSF continued the census work of issuers supervised by the CSSF in the context of the Transparency law. As in 2009, a significant number of issuers have still not made or notified their choice of home Member State. In its Annual Report 2009, the CSSF explained the issue linked to the choice of home Member State. In this context, the CSSF would like to remind the issuers that have not yet chosen a home Member State that they are not complying with all the European regulations applicable to entities whose securities are admitted to trading on a regulated market located or operating in an EEA Member State.

The CSSF cooperates in this context with its foreign counterparts, notably by exchanging notifications of home Member State and information on listed securities. The CSSF thus puts at the disposal of these authorities information concerning the securities issued by foreign entities which are admitted to trading on the regulated market in Luxembourg and receives information on securities issued by Luxembourg issuers on other regulated markets.

3.3. Review of financial reports

3.3.1. General review

In the context of its mission as competent authority to ensure the provisions of the Transparency law are applied, the CSSF performs, in accordance with Article 22 of the law, a general review of regulated information to be published by the issuers subject to this law.

As concerns the review of the 2009 annual reports and the 2010 half-yearly reports, the CSSF intensified its revision process of the reports. Although significant improvements have been observed in the publication procedures (efficient dissemination, storage with the Officially Appointed Mechanism (OAM[2]) and filing with the CSSF), there are still some deficiencies concerning the reports' content. In particular, the statements made by the persons responsible do not always comply with the requirements of the Transparency law. Indeed, certain issuers only list and describe the responsibilities of the persons responsible without giving an assertive declaration in relation to the elements of the annual or half-yearly report concerned. However, the objective of Articles 3(2)(c) and 4(2)(c) of the Transparency law is to make one or several well defined persons responsible for ensuring the accuracy of the annual or half-yearly reports, which is the reason why a mere listing of the responsibilities is not sufficient.

As far as financial reports are concerned, the CSSF informs that, starting from the publication of the annual financial reports relating to the financial year 2010 and following the important exchanges with issuers on this subject, the deadlines for reminders to issuers which did not comply with the provisions relating to periodic

[2] Mechanism used for the centralised storing of regulated information within the meaning of the Transparency law.

information will be severely reduced. Moreover, the CSSF reiterates that it will publish a list of Luxembourg issuers, subject to the Transparency law, which failed to publish their annual report. Registration on this list will be triggered as soon as a delay in the publication is noted, without prejudice to its reasons or origins.

3.3.2. Enforcement of financial information

Pursuant to the Transparency law, and in particular to its Article 22(2), point h), the CSSF is in charge of examining the financial information published by the issuers of securities falling under its scope of application. Through this examination, generally known as “enforcement”, the CSSF ensures that the financial information complies with the relevant reporting framework, i.e. the applicable accounting frameworks, and takes the appropriate measures whenever infringements are discovered.

Enforcement, which was established in the context of the Transparency law, covers financial information included in the so-called harmonised documents published by the issuers concerned, i.e. mainly the following financial statements: annual, half-yearly or quarterly reports, individual and consolidated. Financial information included in the prospectus for an offer to the public or admission on a regulated market may also be subject to this review.

As at 31 December 2010, around 320 issuers fell within the scope of application of the enforcement, of which more than half publish financial information drawn up in accordance with IFRS (International Financial Reporting Standards).

The implementation of the enforcement by the CSSF is based on a specific approach which follows the guidelines defined in two standards developed by CESR, predecessor of the new European Securities and Markets Authority, ESMA. These standards are currently being reviewed within a specific working group in which the CSSF participates.

European cooperation at the level of enforcement also consists in the CSSF participating in the EECS group (European Enforcers Coordination Sessions) of which one of the objectives is to obtain convergence and harmonisation of the enforcement activities within the EU.

- **Enforcement practice**

The procedures developed by the CSSF intend, *inter alia*, to set the principles governing the selection of issuers subject to the enforcement, to detail the type and extent of controls performed and to define the range of decisions and actions available to the CSSF in case infringements are identified.

- **Selection mode**

The selection mode for issuers subject to an enforcement follows a risk-oriented approach, based on the probability of an error in the published financial information and the impact this error could have on investor protection and market confidence. This approach is completed by a random sampling method, whose objective is to subject all issuers concerned by the enforcement to a review every five years (reduced to three years for issuers considered as more risky).

- **Reviews performed**

For the selected issuers, the reviews also follow a risk-oriented approach, the intensity degree of the performed controls being correlated to the risky and sensitive character allocated to the issuer.

The review programme, revised and formally set out every year for the selected issuers covers:

- either a global review of the correct application of the accounting standards applicable to the issuer;
- or the review of specific problems (correct application of a standard, etc.) previously defined according to their importance, their potential impact, etc..

Depending on the intensity of work or on the cases analysed, these reviews will include on-site inspections, meetings or direct contacts with representatives of the issuer or of its external auditor in order to analyse the most significant problems and issues and to obtain information, documents and other objective elements required to perform the review.

- ## Actions available to the CSSF

The powers and sanctions available to the CSSF in this matter are set out in Articles 22, 25 and 26 of the Transparency law.

The principles applied by the CSSF aim at taking appropriate measures and, where applicable, at requesting an official correction whenever a material infringement is identified in the financial information. The measures taken must be effective, appropriate and proportionate to the irregularity committed and intend to improve market integrity and confidence.

Depending on the results of the reviews performed, the CSSF decides to take or not to take an enforcement decision, and, where applicable, administrative measures or sanctions, or even to engage criminal proceedings towards the issuer, pursuant to the Transparency law.

Where errors are identified in the financial information which has been published, the CSSF may require, depending on the materiality of the infringement:

- that the infringement be corrected or the information improved in the subsequent documents to be issued by the issuer;
- that the identified infringement and/or correction to be made be publicly disclosed, through the press or any other appropriate means;
- that the identified infringement be immediately corrected and that a new financial information be submitted and published.

These decisions and actions are communicated in the form of recommendations, formal requests or injunctions.

- ## Reviews performed in 2010

In 2010, enforcement reviews have been performed on more than one third of the issuers publishing their financial information in accordance with IFRS, of which nearly 10% have been subject to an in-depth review. The reviews focussed on the annual financial statements of 2009 and on the half-yearly statements of 2010.

During these reviews, the following issues have been analysed in detail:

- general presentation of the financial information in accordance with IAS 1 "Presentation of Financial Statements";
- issues on the measurement of financial instruments in accordance with IAS 39 "Financial instruments: Recognition and Measurement" (fair value, impairment, etc.);
- completeness of information given on financial instruments as required by IFRS 7 " Financial Instruments: Disclosures";
- compliance of the half-yearly financial statements with the requirements set out in IAS 34 "Interim Financial Reporting";
- recognition principles and measurement methods considered for investment property, in accordance with IAS 40 "Investment Property";
- treatment of given segment information following the mandatory application as from 1 January 2009 of IFRS 8 "Operating Segments".

Following these reviews, the CSSF issued a certain number of injunctions, formal requests and recommendations to certain issuers, concerning:

- the amendments and improvements to include in the future financial statements;
- the correction or improvement of already published information. Thus, two issuers had to publish new financial statements whereas two other issuers completed the financial information already published and which had been considered as insufficient.

The most frequent infringements and deficiencies identified during the reviews mainly concern the following issues:

- the quality and completeness of information provided on judgements and assumptions considered in the drawing-up of the financial statements and in the fair value evaluation methods;
- the methods considered for the identification, evaluation and recognition of the impairments on financial assets held, mainly for securities available for sale;
- the quality and completeness of information provided concerning risk management;
- the completeness of information provided on operating segments.

- **Perspectives for 2011**

In 2011, the CSSF will continue intensifying its controls with issuers subject to the Transparency law, focussing on the 2010 annual financial statements and 2011 half-yearly financial statements.

The following issues are likely to be closely monitored in 2011:

- application of IFRS 8 "Operating Segments";
- business combinations in accordance with revised IFRS 3;
- completeness of information provided in the management report, as required by the applicable laws and regulations.

3.4. Dissemination and storage of regulated information

Since January 2010, two entities have been added to the list of companies specialised in the dissemination of regulated information, published on the CSSF website pursuant to FAQ No. 10 on transparency requirements. As at 14 March 2011, this list included in total seven companies. It mentions only those companies that have contacted the CSSF in order to be registered on the list, that have indicated dissemination channels which comply with the criteria set out in FAQ No. 10 and which fulfil Article 13(2) of the Grand-ducal regulation of 11 January 2008 on transparency requirements for issuers of securities. The list is not exhaustive and does not preclude that other entities that are not registered on this list could also fulfil those criteria or that the issuer could meet them itself.

On 13 December 2010, the *Société de la Bourse de Luxembourg* set up technical improvements in the mechanism for the central storage of regulated information within the meaning of the Transparency law. Persons filing regulated information now benefit from improved functionalities for modifying erroneous filings. Moreover, additional search criteria are available to the users of the search facilities of the OAM (Officially Appointed Mechanism), such as search by country of the issuer's registered office and two possibilities for displaying the search results of regulated information stored with the OAM.

3.5. Questions regarding the Transparency law raised in 2010

3.5.1. Notification requirements for major holdings in relation to own shares for which voting rights are suspended

In accordance with Article 8(1) of the Transparency law, all the voting rights shall be taken into account for the notification of major holdings, even if the exercise thereof is suspended. As a consequence, the suspended voting rights attached to own shares held by the issuer must be included in the notification of major holdings.

As an example, the transfer of own shares from the issuer to one of its subsidiaries triggers a notification requirement for the sellers and acquirers of shares crossing or reaching one of the thresholds set out in Article 8 of the Transparency law, even if the voting rights attached to the transferred shares are suspended.

The CSSF reminds that, in accordance with Circular CSSF 08/349 and FAQ No. 8, the suspended voting rights must also be included in the publication of the "total number of voting rights" pursuant to Article 12 of the Transparency law.

3.5.2. Beneficial owners of voting rights in the context of notifications of major holdings

Articles 8 and 9 of the Transparency law provide that shareholders and persons entitled to acquire, dispose of or exercise voting rights in one of the cases or a combination of cases referred to in Article 9 of the Transparency law must notify the issuer of the percentage of the issuers' voting rights held whenever one of the thresholds provided for in Article 8 is reached or crossed.

In this context, the CSSF points out that the notification requirements for major holdings also apply to the beneficial owners of voting rights, and thus not only to direct shareholders, but also to natural or legal persons indirectly holding voting rights within the meaning of Article 9 of the Transparency law. In the specific case of voting rights held through the intermediary of a controlled undertaking, Article 9(e) of the Transparency law also requires a notification in accordance with Article 8 by the natural or legal persons indirectly holding these voting rights. The concept of "controlled undertaking" shall be understood within the meaning of the definition set out in Article 1(4) of the Transparency law. Section 2 of Circular CSSF 08/349 and FAQ No. 23 provide details on the notification requirement set out in Article 9(e) and on the exemption provided for in Article 11(3) of the Transparency law.

As regards this obligation, the CSSF noticed that certain holders omit to provide complete information, notably in the case of holdings held by companies controlled by natural persons. In order to comply with the above notification requirement, all requested information must be provided and, in particular, the information referred to in points 3, 4 and 8 of Annexe A to Circular CSSF 08/349. For undertakings controlled by natural persons, the name of the natural person having the control over the undertaking(s) holding the shares must be indicated.

3.5.3. Notification procedure for major holdings by shareholders

As regards major holdings notifications, the CSSF noticed that many holders only file their notification with the issuer. The CSSF reminds that, pursuant to Article 18(2) of the Transparency law, information to be notified to the issuer in accordance with Articles 8, 9, 11 and 12 must be filed at the same time with the CSSF. In accordance with Article 18(1), the issuer in turn must also transmit a notification to the CSSF when publishing the complete information included in the notification, which shall occur upon receipt of the information from the holder, and at the latest three trading days after that date.

3.5.4. Details on the notification requirements for major holdings incumbent on the issuer and on the holder following a modification in the number of voting rights and capital

Article 14 of the Transparency law provides that an issuer shall disclose to the public the total number of voting rights and capital at the end of each calendar month during which an increase or decrease of such total number has occurred. FAQ No. 8 requires that the publication shall be made no later than two trading days from the last day of the month in which the change has occurred. This publication shall allow shareholders to comply with the notification requirements incumbent on them in accordance with Article 8(2) of the Transparency law.

Even if the publication as referred to under Article 14 of the Transparency law must be made, in any case, at the end of the month in which the change has occurred, the issuers must immediately publish any substantial change in the number of voting rights and capital which might be considered as inside information as defined in Article 1, point 1) of Directive 2003/6/EC on market abuse ("inside information").

Pursuant to Article 8(2) of the Transparency law, shareholders must notify major holdings whenever they reach or cross one of the thresholds provided for in Article 8 as a consequence of events changing the breakdown of voting rights. This notification must be made based on the information published by the issuer at the end of the month pursuant to Article 14 and, in accordance with Article 11(2)(b) of the law, at the latest within four trading days following the said publication.

3.5.5. Details on the exemptions applicable to periodic information

A certain number of issuers are not, or are only partially, subject to the periodic information requirements provided for in Articles 3, 4 and 5 of the Transparency law, either due to the type of securities admitted to trading on a regulated market or because they benefit from one of the exemptions set out in Articles 7 and 30(6) of the law.

Should these issuers nevertheless publish financial reports, either on their own initiative or in the context of another legal requirement, these reports will be considered as being regulated information within the meaning of Article 1(10) of the Transparency law, provided they fulfil the conditions of inside information. As a consequence, the publication requirements of the Transparency law (filing with the CSSF, effective dissemination and storage with an OAM) apply to these reports. However, contrarily to what applies to reports established within the context of Articles 3, 4 and 5 of the Transparency law, the provisions of this law as regards content and deadlines do not apply to these reports.

4. SUPERVISION OF MARKETS AND MARKET OPERATORS

4.1. Reporting of transactions in financial instruments

4.1.1. Obligation to report transactions in financial instruments

The reporting regime in respect of transactions in financial instruments is mainly set down in Article 28 of the law of 13 July 2007 on markets in financial instruments (MiFID law) which transposes Article 25 of Directive 2004/39/EC of 21 April 2004 on markets in financial instruments (MiFID Directive). This article specifies the obligation for credit institutions and investment firms to report to the CSSF the transactions in financial instruments admitted to trading on a regulated market. The details set out in Article 28 have been completed by the implementing measures of Regulation (EC) No 1287/2006 of 10 August 2006 implementing the MiFID Directive and clarified by the instructions set out in Circular CSSF 07/302.

Moreover, it should be mentioned that the consultation paper launched on 8 December 2010 by the European Commission on the revision of the MiFID Directive also includes proposals as regards Transaction Reporting, e.g.:

- extension of the scope of the reporting obligation;
- adoption of means allowing identifying in the transaction reports the person having traded the transaction and the person on behalf of which the transaction has been executed (client identifier); and
- clarification and harmonisation of the definition of execution of a transaction to be reported.

4.1.2. Credit institutions and investment firms concerned by the obligation to report transactions in financial instruments

As at 31 December 2010, 238 entities (credit institutions and investment firms incorporated under Luxembourg law and Luxembourg branches of credit institutions and investment firms incorporated under foreign law) fell under the scope of Article 28 of the MiFID law and were potentially concerned by the transaction reporting regime (253 entities in 2009), including 144 banks (149 in 2009) and 94 investment firms (104 in 2009). It should be noted that only investment firms which are authorised to carry out transactions in financial instruments, i.e. commission agents, private portfolio managers, professionals acting for their own account, market makers, underwriters of financial instruments and distributors of units/shares of investment funds, are subject to the reporting obligation.

As at 31 December 2010, 103 entities (108 in 2009), of which 89 banks (94 in 2009) and 14 investment firms (*idem* in 2009), were required to send their transaction reports to the CSSF as their interventions are to be considered as "executions of transactions" within the meaning of the MiFID law, as specified by Circular CSSF 07/302. The difference compared to the number of entities that are potentially concerned by the reporting

regime results from the fact that a certain number of entities, mainly investment firms, are not subject to the obligation to report transactions in financial instruments as they do not conclude immediate market-facing transactions and do not execute transactions on own account.

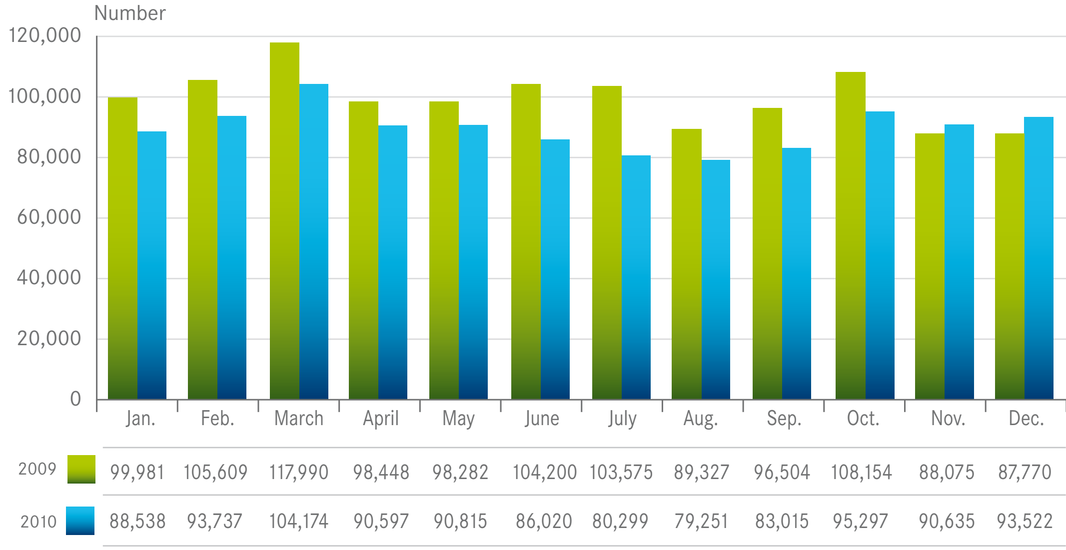
In 2010, the CSSF continued its controls on the quality of the data submitted by the entities subject to the obligation to report transactions in financial instruments. The main non-compliant elements identified in this context were transactions falling within the scope of the reporting requirement which had not been reported and errors on the transaction price, quantity and time. The entities concerned received deficiency letters from the CSSF in order to clarify and correct the irregularities identified.

As far as transaction reports on derivative financial instruments are concerned, the CSSF observed that reports were mainly rejected due to errors in the identification code of the derivative financial instruments for transactions traded on a regulated market which does not use the ISIN codification but the AII (Alternative Instrument Identifier) codification. According to the instructions set out in Circular CSSF 08/365, derivative instruments must be identified by means of the AII code in the transaction reports where the transactions have been executed on a regulated market using this codification. The list of regulated markets using the AII codification instead of ISIN codification is available at http://mifiddatabase.esma.europa.eu. The entities concerned have been informed in order to correct the erroneous data.

4.1.3. Development in the number of transaction reports in financial instruments

In 2010, the number of transaction reports sent by the entities and accepted by the CSSF amounted to 1,075,900 (-10.19% compared to 2009).

Monthly volume of MiFID reports accepted in 2009 and in 2010



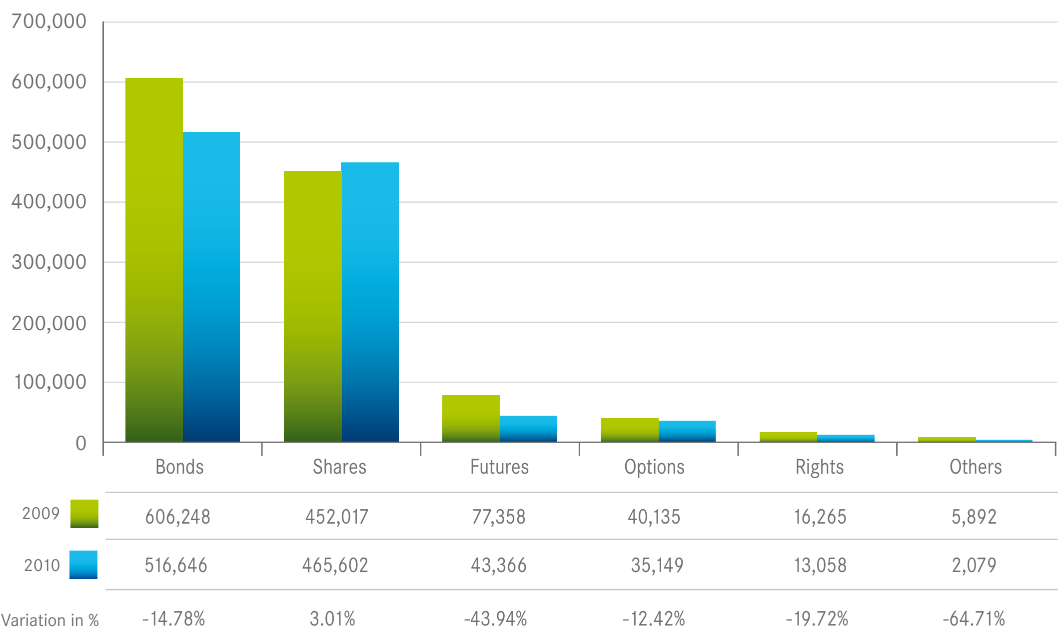
	Jan.	Feb.	March	April	May	June	July	Aug.	Sep.	Oct.	Nov.	Dec.
2009	99,981	105,609	117,990	98,448	98,282	104,200	103,575	89,327	96,504	108,154	88,075	87,770
2010	88,538	93,737	104,174	90,597	90,815	86,020	80,299	79,251	83,015	95,297	90,635	93,522

Breakdown of transactions by month and by type of instrument in 2010

	Bonds	Shares	Futures	Options	Rights	Others	Monthly total
CFi Code	**(Dxxxxx)**	**(Exxxxx)**	**(Fxxxxx)**	**(Oxxxxx)**	**(Rxxxxx)**	**(Mxxxxx)**	
January	44,547	35,577	4,552	2,474	1,244	144	88,538
February	44,710	39,639	5,957	2,466	741	224	93,737
March	54,546	41,603	4,314	2,589	829	293	104,174
April	46,016	38,354	3,078	2,168	829	152	90,597
May	42,282	39,342	3,843	4,039	1,057	252	90,815
June	44,812	33,914	3,560	2,564	993	177	86,020
July	42,939	30,675	3,147	2,297	1,057	184	80,299
August	36,892	33,866	3,080	4,415	867	131	79,251
September	40,065	35,160	3,721	2,526	1,349	194	83,015
October	41,694	46,117	2,361	3,087	1,860	178	95,297
November	39,798	43,244	2,853	3,465	1,204	71	90,635
December	38,345	48,111	2,900	3,059	1,028	79	93,522
Annual total	**516,646**	**465,602**	**43,366**	**35,149**	**13,058**	**2,079**	**1,075,900**

In relative terms, the majority of reports in 2010 concerned transactions in bonds (48.02%), followed by transactions in shares (43.28%). Transactions in other types of instruments represented only a small part (futures: 4.03%, options: 3.27%, rights: 1.21%, others: 0.19%).

Annual comparison of transactions by type of instruments



This data, as well as the evaluation of the information received *via* TREM (Transaction Reporting Exchange Mechanism), set up between competent authorities for their respective supervisory missions, reveal the trends on European markets and, particularly, on the Luxembourg market. The main purpose of the supervision of the markets is to prevent and detect infringements of financial and stock market laws and regulations. In this context, monthly internal reports, as well as specific internal reports, based on the received reports, are drawn up. These *ex post* analyses of transactions in financial instruments can be used as a starting point for the CSSF's inquiries.

4.2. Supervision of stock exchanges

The establishment of a regulated market in Luxembourg is subject to a written authorisation of the Minister of Finance. Chapter 1 of Title 1 of the MiFID law sets out the authorisation conditions and requirements applicable to regulated markets. Where the operator of such regulated market is established in Luxembourg, he must also obtain an authorisation as "PFS other than an investment firm" in accordance with the law of 5 April 1993 on the financial sector. The acts relating to the organisation and operation of the regulated market are supervised by the CSSF.

Pursuant to the provisions of the MiFID law, the operation of a multilateral trading facility (MTF) is part of the investment services and activities defined in that law. MTFs may be operated either by a market operator or by a credit institution or an investment firm.

There are currently two markets operated in Luxembourg by the same operator, namely Société de la Bourse de Luxembourg S.A. (SBL): a first market, named *Bourse de Luxembourg* (Luxembourg Stock Exchange), which is a regulated market within the meaning of the European directives and a second market called "Euro MTF", the operating rules of which are defined in the Rules and Regulations of SBL.

SBL is also the only company holding an authorisation as operator of a regulated market authorised in Luxembourg as defined in Article 27 of the law of 5 April 1993 on the financial sector. As such, SBL is registered on the official list of the other professionals of the financial sector as "PFS other than an investment firm".

As far as its supervisory mission is concerned, the CSSF has had several meetings and exchanged mail with SBL notably with regard to the follow-up of the implications, for SBL and the markets it operates, of the PFS status and of the MiFID law provisions, of the amendment of its Trading manual and of the organisation and works of internal audit. On the basis of the analytical reports transmitted by SBL and the electronic access to the information on stock market transactions, the CSSF monitors the market activities and the problems related to these activities. The development of SBL's financial situation is monitored, in particular, *via* the monthly reporting sent by SBL.

Moreover, SBL's board of directors adopted on 16 July 2010 the compliance policy and charter of SBL. The compliance charter sets out the operating procedures which shall be put in place in order to allow SBL's compliance function to meet the objectives set, considering that the objective is to ensure compliance with the legal, regulatory and professional ethic provisions in force.

As at 31 December 2010, SBL counted 61 members. As far as market activities are concerned, the trading turnover on both markets operated by SBL reached EUR 219.16 million in 2010 against EUR 272.05 million in 2009. Shares represented 74.99% of the volume exchanged, whereas the part of fixed-income securities amounted to 25.01%. Over a thousand bonds are tradable continuously on the UTP (Universal Trading Platform) on which SBL operates its markets.

In 2010, admission activities on the markets operated by SBL recorded an upturn. 9,350 new issues have been admitted to the official listing, against 7,737 in 2009: 8,210 issues have been admitted on the "Bourse de Luxembourg" market and 1,140 on the "Euro MTF" market. The instruments admitted in 2010 can be broken down as follows: 5,608 bonds, 2,469 warrants and rights, 1,220 UCIs and 53 shares, units and certificates.

As at 31 December 2010, the two markets operated by SBL totalled 44,916 listings, against 45,660 in 2009, i.e. 29,566 bonds, 7,581 warrants and rights, 7,445 UCIs and 324 shares, units and certificates. In the segment of shares, GDR (Global Depositary Receipts) represented the majority of listed instruments.

As far as distribution services offered by SBL were concerned, more than 20,000 official notices have been published on the SBL portal and nearly 300 depositors and 500 issuers use SBL's OAM (Officially Appointed Mechanism).

5. INVESTIGATIONS AND COOPERATION

The CSSF is the administrative authority competent to ensure that the provisions of the market abuse law are applied. The purpose of this law is to combat insider dealing and market manipulation ("market abuse") in order to ensure the integrity of financial markets, to enhance investor confidence in those markets and thereby to ensure a level playing field for all market participants.

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

In the context of the collection of information regarding an investigation, the CSSF is empowered to summon interested parties to a hearing. Such hearings allow affected persons to present arguments in fact and in law, to explain the reasons for initiating the executed transactions and to provide the CSSF with elements in order to better assess the case. The department "Supervision of securities markets" of the CSSF organised in all 22 hearings in Luxembourg and participated in three hearings in the context of international cooperation files on market abuse.

5.1. Investigations initiated by the CSSF

In 2010, the CSSF opened eight investigations into insider dealing and/or price manipulation, some of which included additional aspects linked to other laws. The various information elements and documentary evidence received in the course of the investigations allowed the CSSF to closed most files without taking further action and to transmit certain files to the State Prosecutor. An injunction concerning one of the obligations set out in the market abuse law has been pronounced against one party concerned.

5.2. Investigations conducted by the CSSF at the request of a foreign authority

5.2.1. Inquiries into insider dealing

In 2010, the CSSF processed 29 inquiries into insider dealing (*idem* in 2009). The CSSF handled all these requests with the necessary diligence befitting cooperation between authorities and, within that scope, organised in Luxembourg five hearings of affected persons in which agents from the foreign competent authorities could participate.

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

The CSSF received eight inquiries into price manipulations (nine in 2009), five inquiries into breaches of requirements to report major shareholdings (*idem* in 2009), four other inquiries relating to Luxembourg-incorporated companies (five in 2009) and two inquiries relating to fraudulent public offers. The CSSF responded to all these requests within the scope of its legal competence.

Seven of those nineteen requests were received from administrative authorities of countries outside the EEA.

5.3. Suspicious transaction notifications

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

Based on this provision, the CSSF received sixteen suspicious transaction reports in 2010 (eight in 2009). For underlying financial instruments admitted to one or several foreign markets, the notified information was transmitted to the competent authorities of the market(s) concerned, thereby observing the cooperation obligation referred to in the law on market abuse. This information can, where necessary, lead these authorities to open investigations.

In 2010, the CSSF received five notifications of suspicious transactions transmitted by foreign authorities (eleven in 2009) and analysed them with the necessary diligence.

In this context, the CSSF noticed a certain inconsistency in the practical application of this provision within the different Luxembourg entities subject to this requirement. It also observed that certain credit institutions and other professionals of the financial sector established in Luxembourg did not report any suspicious transaction since the entry into force of the law on market abuse.

Hence, the CSSF would like to insist on the fact that persons concerned by this requirement must, as soon as suspicions concerning a transaction are identified, send without delay a suspicious transaction report to the CSSF in relation to said transaction. The omission of such notification may in particular be noticed when a suspicious transaction is concerned in the context of market abuse inquiries. A late notification, made following such inquiry, will not be considered as sufficient to comply with the notification requirements set out in Article 12 of the market abuse law. Any violation of the requirements provided for in Article 12 is subject to an administrative fine.

6. DEVELOPMENTS IN THE REGULATORY FRAMEWORK

6.1. Prospectus and other information requirements relating to issuers of securities

Directive 2010/73/EU of 24 November 2010 amending Directives 2003/71/EC on the prospectus to be published when securities are offered to the public or admitted to trading and 2004/109/EC on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market (revised Prospectus Directive) has been published on 11 December 2010 in the Official Journal of the European Union and entered into force on 31 December 2010. It must be transposed into national law by 1 July 2012 at the latest and the first works relating to it have been started by the CSSF and ESMA. In the context of drafting opinions on delegated acts by ESMA, the coordination of one of the three sub-working groups has been entrusted to several staff members of the department "Supervision of securities markets", which enables them to follow and actively participate in the drafting of technical measures deriving from the review, in parallel with the transposition process in Luxembourg.

As concerns the amendments introduced by the revised Prospectus Directive, the CSSF informed market participants in December 2010 of the immediate consequences regarding transparency requirements for issuers considering to issue after 30 December 2010 debt securities with a denomination per unit below EUR 100,000. Indeed, the grandfathering clause provided for in Article 2 of the revised Prospectus Directive only applies to debt securities with a denomination per unit of at least EUR 50,000 (or its equivalent in any other currency) and which have been admitted to trading on a regulated market before 31 December 2010, for as long as such debt securities are outstanding.

For issuers which issue debt securities with a denomination per unit below EUR 100,000 (or its equivalent in any other currency) on 31 December 2010 or after such date, this means they will have to comply with all the transparency requirements which currently apply to issuers having issued debt securities with a denomination per unit below EUR 50,000 (or its equivalent in any other currency). These requirements include in particular the preparation of annual and half-yearly financial reports. Where Luxembourg is the home Member State of such an issuer under the Transparency law, these obligations will apply to such issuer as from the date these provisions enter into force under Luxembourg law.

6.2. Market abuse

The amendments introduced by the law of 26 July 2010 into the law on market abuse do not modify the essence of the market abuse legislation in Luxembourg. These amendments grant the CSSF inspection and sanction powers regarding any person submitted to the market abuse law. The purpose of the amendments are described in further detail in Chapter XIV of this Annual report.

In the practical implementation of these legislative amendments, the CSSF staff members may now not only carry out on-site inspections with persons subject to its supervision, but also with any other legal or natural person subject to a market abuse investigation. The protection of defence rights of these persons is guaranteed by the introduction of detailed procedures into the new Article 29a of the market abuse law.

The CSSF is now also authorised to take administrative sanctions against all persons, natural or legal, which break intentionally, or through carelessness or by negligence, the prohibitions set out in the market abuse law. The highest amount that the CSSF may impose as administrative fine in case the prohibitions set out in the market abuse law are infringed has been increased to a maximum amount of EUR 1,500,000. A closer communication between the State Prosecutor and the CSSF is provided for in the new provisions and, for any infringement to the prohibitions set out in the market abuse law by fraudulent means, the prosecution power lies with the State Prosecutor.

SUPERVISION OF INFORMATION SYSTEMS

09

1. Activities in 2010

2. Supervisory practice

1. ACTIVITIES IN 2010

This Chapter deals with the supervision of information systems of financial professionals, mainly credit institutions, investment firms and other PFS. As concerns the specific supervision of support PFS, please refer to point 3 of Chapter VII "Supervision of PFS".

1.1. Participation in national groups

In 2010, the department "Information systems and supervision of support PFS" represented the CSSF within the following committees, commissions, associations or working groups:

- ABBL - Payments, Information Systems and Standardisation Committee. The Committee, in which the CSSF participates as observer, dealt with topics relating to payment and clearing systems, bank cards, direct debit and especially the European project SEPA (Single European Payment Area) coordinated by EPC (European Payment Council). The vulnerabilities specific to the use of financial services *via* the Internet are also reviewed.
- CRP Henri Tudor and the INNOFinance programme, which was initiated in 2007.
- Luxembourg Institute for Standardisation, Accreditation, Safety and quality of products and services (*Institut Luxembourgeois de la Normalisation, de l'Accréditation, de la Sécurité et qualité des produits et services*, ILNAS). This authority, under the responsibility of the Minister of Economy, has been created by the law of 20 May 2008 and started its activities on 1 June 2008.
- Operational Crisis Prevention Group for the financial sector (OCPG) under the aegis of the Luxembourg Central Bank. The mission of OCPG consists in identifying the risks supported by the financial sector in relation to critical infrastructures, in order to suggest measures enabling to prevent a possible operational crisis which would disrupt the functioning of the financial professionals and jeopardise the proper settlement of monetary operations.

1.2. International cooperation

The CSSF took part in the CESR-ITMG meetings at European level as well as in the international IT Supervisory Group (ITSG). An annual international meeting allowed to exchange information with the other regulators and to assess the situation on issues related to cyber-attacks, versionning, international IT outsourcing, IT governance, development of emergency plans and other recurrent or new subjects which impact IT prudential supervision. The meeting was followed by a European meeting which dealt with these issues only from an EU legal point of view.

1.3. Developments in the regulatory framework

A circular on the new supervisory framework relating to support PFS is currently being drafted by the CSSF. Its publication is expected in the second quarter of 2011, in order to be applicable for support PFS as from 2012.

2. SUPERVISORY PRACTICE

Supervision includes the verification that supervised entities comply with the legal and regulatory framework, with the direct or indirect purpose to maintain or improve the professionalism of their activities. It focusses, in particular, on the technologies implemented for the information systems and takes into account the specificities of the outsourcing of these services with support PFS or third parties, outside or within the group.

2.1. Consolidation of intragroup IT systems

The consolidation process of IT systems of Luxembourg subsidiaries of foreign financial institutions with their parent company or specialised companies belonging to the group continued in 2010.

The CSSF reminds that, pursuant to Grand-ducal regulation of 13 July 2007 relating to organisational requirements and rules of conduct in the financial sector, credit institutions and investment firms must exercise due skill, care and diligence when entering into, managing or terminating any arrangement for the outsourcing of critical or important operational functions or of an investment service or activity to a service provider. In other words, whenever an outsourcing project, in particular of IT systems, is submitted to the CSSF, the institution must provide evidence for a pertinent and as complete as possible due diligence procedure. This due diligence must cover aspects related to compliance with the Luxembourg legal and regulatory context, mainly regarding Article 41 of the law of 5 April 1993 on the financial sector on professional secrecy.

As far as confidentiality of IT systems is concerned, the CSSF prefers the implementation of technical measures instead of functional or organisational measures. Indeed, where outsourcing abroad has an impact on the security of the access to confidential data, there is a risk that functional protection solutions decrease over time. They might not protect from malicious actions and they are not necessarily opposable in case investigations are carried out abroad. The consequences of a loss of confidentiality may be very serious, both for the concerned client and in terms of reputation of the Luxembourg institution which bears the responsibility for it.

The authorised managements of Luxembourg institutions shall ensure that they do not end up with a non-compliant situation imposed by the group.

The confidentiality level to respect depends on the fields of activity. In the field of investment funds with an international customer base, the main focus remains on the Luxembourg banking relationship of the client. As far as the registrar activity is concerned, there are no obstacles to outsourcing data or to copying data as subscribers are registered as nominees. Particular attention must however be paid to the reconciliation process of subscription/redemption transactions if the name of the final client is indicated in the “communication” field of the fund transfer. Contracts between professionals must mention this outsourcing and define the obligations incumbent on each party and, in particular for Luxembourg professionals, the commitment not to indicate any name in the additional fields, as for example in the field “communication” for a fund transfer.

Where confidentiality is required, Circular CSSF 05/178 specifies in its point 4.5.2.2. that data must never be readable outside Luxembourg, which is possible by means of a strong cryptography and on condition that the decryption key is never available or accessible from abroad.

More and more mixed cases come up, where service provisions related to IT are carried out by different operators or contractors, some of which being support PFS in Luxembourg, others being located abroad. The new risk which has been identified concerns inter-connectivity of IT systems, which allows providers to act on different platforms to provide their services. In such cases, administrator rights must be closely analysed, as a Luxembourg financial institution must keep total control over its systems, in particular those hosting and managing confidential data. In this situation, and as is the case for technical measures *versus* organisational measures, the CSSF favours the implementation of preventive mechanisms to the performance of *a posteriori* controls. It would thus be preferable not to give permanent access rights which allow modifying the securities already in place, rather than verifying in logs that these securities have not been circumvented by malicious modifications. On the one hand, identifying an abuse is more difficult within a large amount of information, and on the other hand, *a posteriori* control mechanisms require that traceability logs are secured.

In any case, the authorised management of the supervised entities must have at its disposal the necessary competences to understand the stakes and mechanisms suggested at group level, in order to control risks on an informed basis and to assume the consequences of a situation which would not be compliant with the Luxembourg legal framework when implemented.

2.2. Virtualisation and mutualisation of network protection systems

As the concept of cloud computing is becoming more and more topical and its application to the financial sector is an important stake, some providers, in particular support PFS acting as "IT systems and networks operators", offer virtualised and/or mutualised firewalls in the implementation of their mutualised infrastructure.

In its Annual Report 2009, the CSSF indicated that virtualisation of systems reached a certain maturity allowing it to be used by the financial sector to mutualise technical platforms between different clients of the financial sector, provided the implementation is correctly made and the virtualisation tools are very well controlled.

A new trend which came up in 2010 concerns the virtualisation and the mutualisation of firewalls. Technically speaking, there is no real prudential obstacle to combine the virtualisation and mutualisation of firewalls, as the respective tools are very efficient and reliable and the risk for a lack of segregation between the different environments for each financial institution remains low. The role of the firewall is indeed to allow certain IP addresses on certain specific ports and the range of IP addresses for each institution are often very different (range IP, network addresses varying substantially from one institution to another).

The CSSF nevertheless identified a risk for loss of control over environments, as the number of firewall rules, which may already be high for an institution, may literally explode and become unmanageable for several institutions, bringing along as a consequence a non-identified security weakness.

Moreover, the complexity of the management of logical network cards through virtualisation compared to the network cards physically available on the machine may lead to an unstable connectivity and security weaknesses.

The CSSF also noticed an increase in the number of architectures based on one firewall only including more than two network interfaces (mostly three or more) whereas the CSSF had recommended to put in place cascading firewalls of different brands, in order to avoid a direct intrusion into the financial institution's internal network in case of a security weakness in the firewall software.

2.3. Internet threats

During the last two years, only few viruses and Trojans tried to intrude the browser of the clients' machine in order to disrupt on-line banking transactions. Unfortunately, some Trojans originating from organised crime that are less and less detectable by anti-virus software products and targeting many banks in the world appeared at the end of 2010 and beginning of 2011. There is no reason for Luxembourg not being targeted.

The CSSF is considering collecting systematically information on succeeded frauds, even if they do not imply financial consequences for the client or the financial institution, in order to perform a follow-up of these attacks, to warn the institutions more specifically concerned and to contribute to finding protection mechanisms. The CSSF thus reminds that a robust authentication procedure, by means of a token or chip card, may help countering Trojans that collect characters entered on the keyboard, print screens and mouse cursor positions. A correct implementation of the electronic signature mechanisms of transactions, in addition to the authentication of the session, may definitively delay such attacks, also called "man in the middle" or "man in the browser".

PUBLIC OVERSIGHT OF THE AUDIT PROFESSION

10

1. Regulatory framework of the audit profession
2. Quality assurance review
3. Outline of the population of *réviseurs d'entreprises* (statutory auditors) in Luxembourg

1. REGULATORY FRAMEWORK OF THE AUDIT PROFESSION

1.1. Adoption of the clarified ISAs and of certain complements in Luxembourg

Although the principle of their adoption is established, the European Commission has not yet adopted the International Standards on Auditing ("ISAs"), notably due to translation delays.

The CSSF has decided in the meantime to adopt the clarified ISAs directly and at the earliest opportunity in Luxembourg, given their added value for the exercise of the audit profession.

The adoption will be realised *via* a CSSF regulation and a CSSF circular. The new standards will apply to the statutory audits of financial years closing on 31 December 2011.

The adoption of ISAs *via* two legal documents reflects the new two-tier structure of the standards, each comprising requirements as well as application and other explanatory material. Thus, the CSSF decided to adopt the requirements *via* a legal instrument that is binding itself (regulation) and additional details and/or explanations *via* a legal instrument reflecting an administrative position of the CSSF, which must be applied *ad hoc* according to the different cases encountered in practice (circular).

The adoption of ISAs was preceded by substantial work of the Audit Technical Committee (*Comité Technique Audit*, CTA), an expert committee within the CSSF.

The CTA's main mission is to provide an opinion to the CSSF's executive board on certain particularly technical aspects of the audit profession, as for instance the adoption of ISAs, quality control standards, code of ethics, but also to analyse any other technical issue raised by the profession or other. Thus, the CTA directly contributes to the work of the Consultative committee for the audit profession laid down in section 6b of the law of 23 December 1998 establishing a financial sector supervisory commission (*Commission de Surveillance du Secteur Financier*).

The CTA has held seven meetings since June 2010 and performed a comparative study of every former ISA with the "clarified" standard in order to reach two objectives: understanding the significant changes made and assessing if the particular situation of Luxembourg would require, in certain cases, supplements for Luxembourg.

In this context, the CTA noted that the following standards had changed substantially with the Clarity Project or are completely new:

- ISA 265 - Communicating deficiencies in internal control to those charged with governance and management: new standard;
- ISA 450 - Evaluation of misstatements identified during the audit: new standard;
- ISA 600 - Special considerations - Audits of group financial statements: this standard underwent significant clarifications that specify in particular additional requirements for supervision, by the group auditor, for the component auditors and the documentation of this supervision.

Finally, the former ISA 701 was split into two standards: ISA 705 (Modifications to the opinion in the independent auditor's report) and ISA 706 (Emphasis of matter paragraphs and other matter paragraphs in the independent auditor's report).

The following Luxembourg supplements are being discussed:

- ISA 320: Materiality with respect to UCIs;
- ISA 550: Application of the notion "related party" in the field of UCIs;
- ISA 580: Discussions on the finalisation of audit works and the issue of the audit report;
- ISA 600: Discussion regarding a common procedure in the context of group audits and referred audits.

The adopted ISAs and Luxembourg supplements will all be published in the *Mémorial* and on the CSSF's website.

1.2. Quality control standards and ethics

The CSSF included in its CSSF Regulation No 10-01 the standard ISQC1 as initially adopted by the general meeting of the *Institut des Réviseurs d'Entreprises* (IRE, Luxembourg institute of registered auditors) of 28 June 2005 for the financial years beginning as from 1 January 2006.

The CTA has analysed the new version of this standard as published by IFAC with a view to its adoption.

This new version includes the following components of the former standard:

(a) leadership responsibilities for quality within the firm;

(b) ethical requirements;

(c) acceptance and continuance of client relationships and specific engagements;

(d) human resources;

(e) engagement performance;

(f) monitoring;

and adopts a similar presentation as that of the clarified ISAs, i.e. requirements followed by application and/or other explanatory material on the rules, and integrates new definitions.

It also emphasises the modularity of these provisions according to size and activity of the audit firm.

CSSF Regulation No 10-01 also includes the code of ethics as adopted by IRE's general meeting in its version of 12 June 2007.

IFAC's Code of Ethics, which is the basis of the Luxembourg code of ethics, was revised by the International Ethics Standards Board for Accountants, an IFAC body, in order to enhance clarity and strengthen independence requirements.

The following changes, among others, have been made:

- introduction of a new definition of "public interest entities" (PIEs);
- a new definition of "key audit partner";
- an extension to PIEs of provisions historically applicable to listed companies;
- the key audit partner must not be evaluated based on his ability to sell non-audit services to audit clients, and
- introduction of safeguards consisting in a pre- or post-issuance quality control review when, for an audit of a PIE, the firm's total fees exceed 15%.

The adoption by the CSSF of the revised code of ethics was also preceded by a revision made by the CTA. Members of the CTA proposed to add a certain number of specifications in order to align certain rules with the national law and additional rules in areas such as the fight against money laundering and terrorist financing or marketing.

As for the international standards on accounting, the adoption of the new version of the ISQC1 and the new code of ethics will be realised through CSSF regulations and CSSF circulars.

1.3. Other works in progress

At the beginning of 2011, the CTA started to examine the old IRE recommendations with respect to the other engagements exclusively conferred on *réviseurs d'entreprises agréés* (approved statutory auditors) and *cabinets de révision agréés* (approved audit firms) by the law. It should be borne in mind that these engagements also fall within the scope of the CSSF's supervision in accordance with the law of 18 December 2009 concerning the audit profession.

2. QUALITY ASSURANCE REVIEW

2.1. Scope

2.1.1. General framework

Before the law of 18 December 2009 concerning the audit profession ("Audit law") came into force, peer controls were organised by IRE according to principles and terms laid down by a professional standard governing quality control and adopted by IRE's general meeting.

Since the entry into force on 23 February 2010 of the Audit law, *réviseurs d'entreprises agréés* and *cabinets de révision agréés* are subject to a quality assurance review, organised according to the terms laid down by the CSSF in its capacity as supervisory authority of the audit profession, for engagements concerning statutory audits of accounts as well as for other duties which are exclusively entrusted to them by the law.

The quality assurance review takes place at least every six years. This cycle of review is brought down to three years for *réviseurs d'entreprises agréés* and *cabinets de révision agréés* that audit PIEs.

Population of *cabinets de révision agréés* and *réviseurs d'entreprises agréés* concerned by the quality assurance review

The population of *cabinets de révision agréés* and *réviseurs d'entreprises agréés* that carry out statutory audits and other engagements conferred exclusively upon them by the law is as follows (as at 31 December 2010):

- Number of audit firms: 74, including 16 that audit PIEs;
- Number of independent auditors: 11, none of which audits PIEs.

Based on the data collected through the "Annual Annexes" for the year 2009, the statutory audit missions break down as follows between *cabinets de révision agréés* and independent *réviseurs d'entreprises agréés*:

- 90% of the engagements are carried out by the "BIG 4"[1];
- 9% of the engagements are carried out by middle-sized audit firms[2], and
- 1% is carried out by the other audit firms and independent *réviseurs*.

2.1.2. Scope of the quality assurance review

The CSSF follows a global approach of control in which the audit firm is the entry point for the periodical quality assurance review.

The global control of the audit firm consists in:

- obtaining reasonable assurance regarding the existence and efficiency of the design and functioning within the firm, of an organisation, policies and procedures aimed to ensure the quality of the statutory audit engagements and the independence of the *réviseur d'entreprises agréé/cabinet de révision agréé*;
- verifying the correct execution of the engagement by the signatory based on a selection of missions to ensure, on the basis of this selection, the existence and efficiency of the procedures and internal quality control system;
- assessing the content of the transparency report for *cabinets de révision agréés* that are required to draw up such a report, based on the review work performed.

[1] Deloitte, Ernst & Young, KPMG and PWC.

[2] Firms that carry out more than 100 engagements reserved by the law to *réviseurs d'entreprises agréés* and *cabinets de révision agréés*.

2.1.3. Organisation of the quality assurance review

The quality assurance review of an audit firm is conducted through several steps:

- collection of prior information from audit firms;
- drawing-up of a control plan;
- performance of on-site inspections;
- presentation of observations made;
- organisation of a contradictory process;
- preparation of a draft report;
- gathering of the audit firm's responses to the CSSF's observations, and
- writing and issuing the final report.

2.2. Programme of operations for 2010

The CSSF set down a multiannual programme for the control of *cabinets de révision agréés/réviseurs d'entreprises agréés*, which aims at observing the legal quality assurance review cycle.

All the firms that audit PIEs will be controlled before 31 December 2012; independent audit firms and *réviseurs* that do not audit PIEs will be controlled before 31 December 2015.

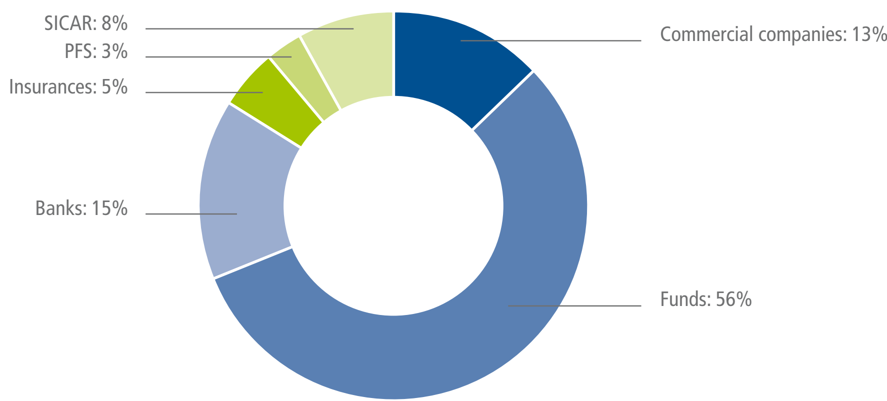
This programme was set up based on the information transmitted by approved audit firms and *réviseurs* through the "Annual Annexes" relating to their activity.

The quality assurance reviews planned in the 2010 programme focused on the understanding and documentation of the organisation and of the policies and procedures set up by the controlled audit firms in order to assess compliance with the requirements of the international standard for quality control no.1 (ISQC 1), as well as on a sample of audit files relating to statutory audit engagements of the financial year 2009 (32 PIEs and 85 other entities).

In 2010, four firms that audit PIEs have been controlled. The quality assurance reviews started in April 2010 and were conducted by five CSSF inspectors, accounting for a total of 3,024 hours. These inspectors are themselves former employees of audit firms and are specialised in the different fields of the Luxembourg market.

The four reviewed audit firms have a total of 3,940 mandates falling within the scope of public oversight of the CSSF, including 232 in relation to PIEs. These mandates include 3,501 statutory audits, of which 214 concern PIEs.

Breakdown per sector of statutory audits reviewed by the CSSF in 2010



Breakdown per entity type of statutory audits reviewed by the CSSF in 2010

Listed PIE: 7%

Non-listed PIE: 21%

Others: 72%

2.3. Results of the 2010 reviews

In the context of quality assurance reviews, the CSSF made a certain number of observations. The main issues are set out hereafter.

Most of the audit firms reviewed have quality-control procedures suited to the size and nature of their activities. Nevertheless, the application of these procedures to the individual audits is likely to be improved in all audit firms.

Potential threats to the independence of the *réviseur d'entreprises agréé* must be analysed thoroughly and, where applicable, be a matter for consultation so that the audit firms are able to take appropriate decisions.

The nature, scope and documentation of the quality-control system monitoring must be improved. This monitoring covers the "audit firm" and the "files" which must both be subject to analysis and conclusions to be provided to the firm's management on an annual basis.

The role of the person in charge of the engagement quality control review (EQCR) must be strengthened. In particular, the CSSF wishes to stress the need for:

- an EQCR to be appointed in compliance with the regulatory requirements and the criteria laid down by the audit firms;
- the EQCR to dedicate sufficient time to its review;
- the EQCR to perform its review throughout the engagement and before issuing the report; and for
- the EQCR to materialise its review, mainly based on working documents linked to high risk areas.

The CSSF also stresses that a better documentation is necessary as regards:

- requests for information to the management, the persons in charge of governance or other persons within the client;
- the conclusions reached during the meetings of the audit team members;
- the conclusions reached during the meetings of the audit team with the client;
- the controls of accounting entries and adjustments;
- the use of the reports of auditors on Service Organisation and works of experts, of another auditor or of an internal auditor;
- analytical reviews, for explaining significant variations of and for determining expected amounts; and
- the materialisation of a link between risk analysis of audited entities, assessment of the internal control and audit procedures implemented in order to respond to these risks, the determination of risk to be made by assertion.

The CSSF also insists on the importance to have systems in place guaranteeing the archiving of audit files within 60 days after the issuance of the report of the *réviseur agréé* and preventing any undocumented change to the "paper" and "electronic" audit file after that date.

The process of external confirmations may be improved, both as regards the control that the *réviseur* has over the process, and the quality of alternative procedures made where applicable. Moreover, given the observation that electronic confirmations increase in number and that the quality of written confirmations decreases, the CSSF considers that the *réviseur* has to increase his professional scepticism as regards these documents that are one of the most convincing audit evidence to validate the existence of the elements of asset of an entity.

Audit of fair value measurements and accounting estimates must give rise to comprehensive diligence in accordance with the relevant standards.

3. OUTLINE OF THE POPULATION OF *RÉVISEURS D'ENTREPRISES* IN LUXEMBOURG

Within the scope of its public oversight of the audit profession, the CSSF assumes the following responsibilities:

- access to the profession and organisation of the examination of professional competence;
- granting the professional title of *réviseur d'entreprises* and *cabinet de révision*;
- granting the approval and registration of *réviseurs d'entreprises agréés* and *cabinets de révision agréés*;
- registration of third-country auditors and audit entities; and
- keeping of the public register.

In this regard, the following statistics have been extracted for the year 2010.

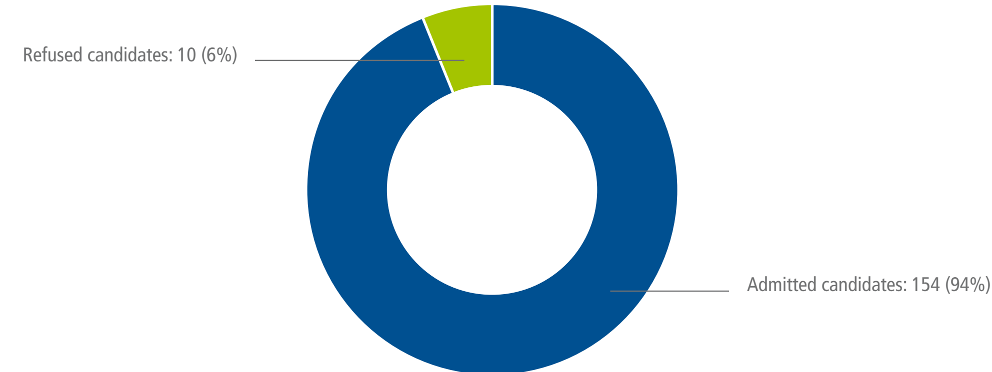
3.1. Access to the profession

3.1.1. Activities of the Consultative commission for the access to the audit profession

The Consultative commission was established through CSSF Regulation No 10-02 of 6 April 2010. Its task is notably to verify the theoretical and professional qualification of candidates to the access to the profession in Luxembourg, as well as that of service providers from other Member States wishing to exercise by way of free provision of services.

The commission met eight times in 2010 and analysed the files of 164 candidates.

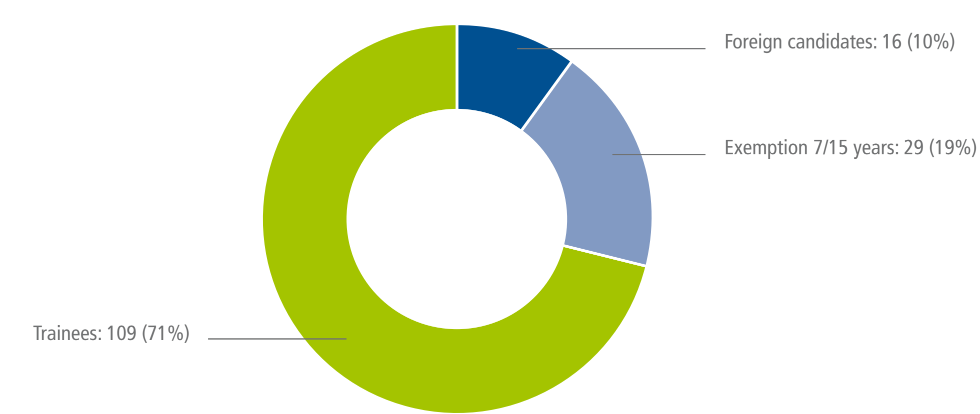
Admission/refusal of application files submitted to the Consultative commission in 2010



There are four categories of candidates:

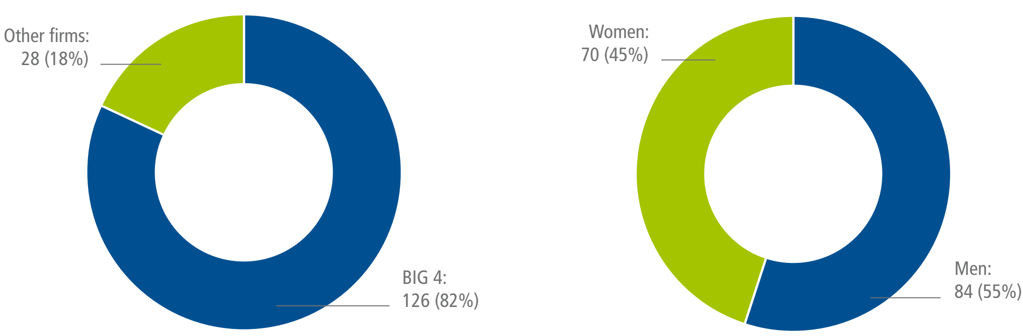
- trainee *réviseurs d'entreprises*;
- foreign candidates;
- candidates applying for exemptions based on their professional experience of either seven or fifteen years; and
- candidates requesting to exercise missions reserved by the law to *réviseurs d'entreprises agréés* and *cabinets de révision agréés*, by way of free provision of services (no such file has been analysed in 2010).

Breakdown of admitted candidates according to category

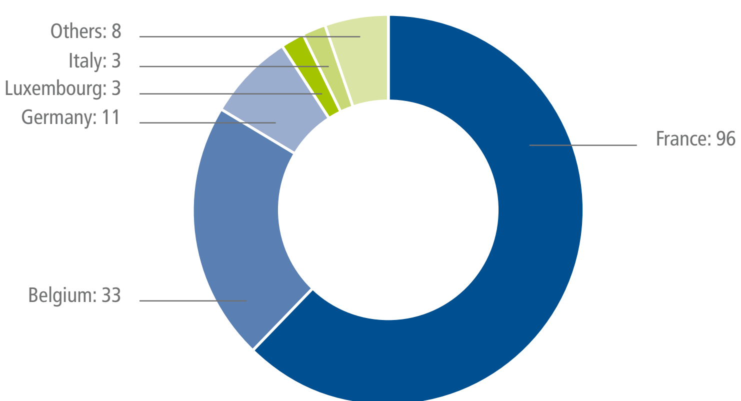


Breakdown of applications according to firms

Breakdown of applications according to gender



Breakdown of admitted candidates according to nationality



3.1.2. Examination of professional competence 2010

The CSSF administrates the examination of professional competence in accordance with Articles 5 and 6 of the Grand-ducal regulation of 15 February 2010 establishing the qualification requirements of *réviseurs d'entreprises*.

In this context, the examination jury communicated the following results to the CSSF with respect to the examination of professional competence 2010:

- Three out of the 53 registered candidates did not present themselves, including one non excused absence, sanctioned by a total referral.
- Ordinary session: 50 candidates took the written exam, 30 of whom have been admitted to the oral exam. In total, 19 candidates passed the exam, 11 failed partially (having the possibility to take the extraordinary session) and 20 failed completely.
- Extraordinary session: eleven candidates took the written exam, six of whom have been admitted to the oral exam. In total, four passed the exam and seven failed completely.

Thus, all sessions included, 23 candidates passed the examination of professional competence in 2010 successfully.

Having passed this examination, candidates may request to be granted the title "*réviseur d'entreprises*" from the CSSF.

The diploma ceremony was held in March 2011 in the presence of the Minister of Finance Mr Luc Frieden.

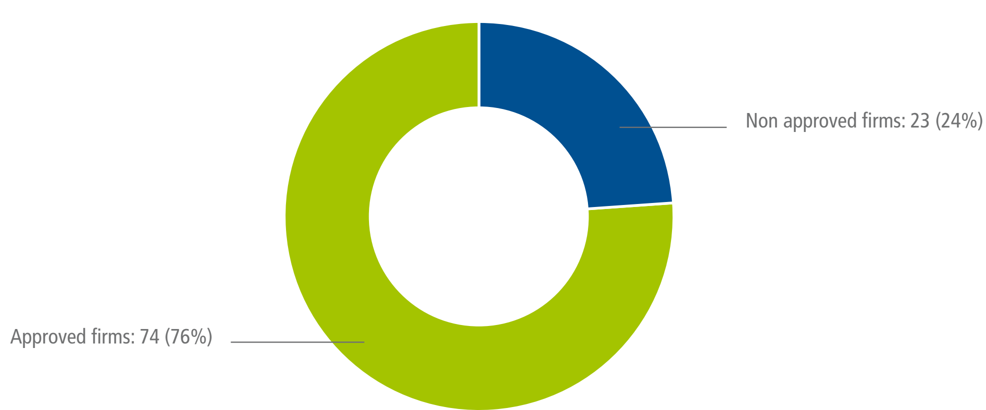
3.2. Public register

The public register of *réviseurs d'entreprises agréés, cabinets de révision agréés* and third-country auditors and audit entities is available on the CSSF's website in section "Public oversight of the audit profession", sub-section "Public register".

3.2.1. National population as at 31 December 2010

- ***Cabinets de révision* and *cabinets de révision agréés***

The total number of *cabinets de révision* and *cabinets de révision agréés* amounted to 97 as at 31 December 2010.

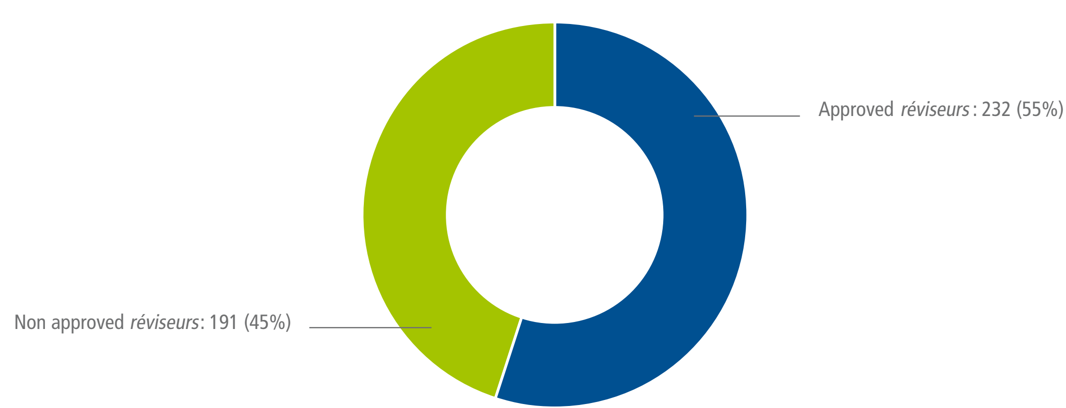


- ***Réviseurs d'entreprises* and *réviseurs d'entreprises agréés***

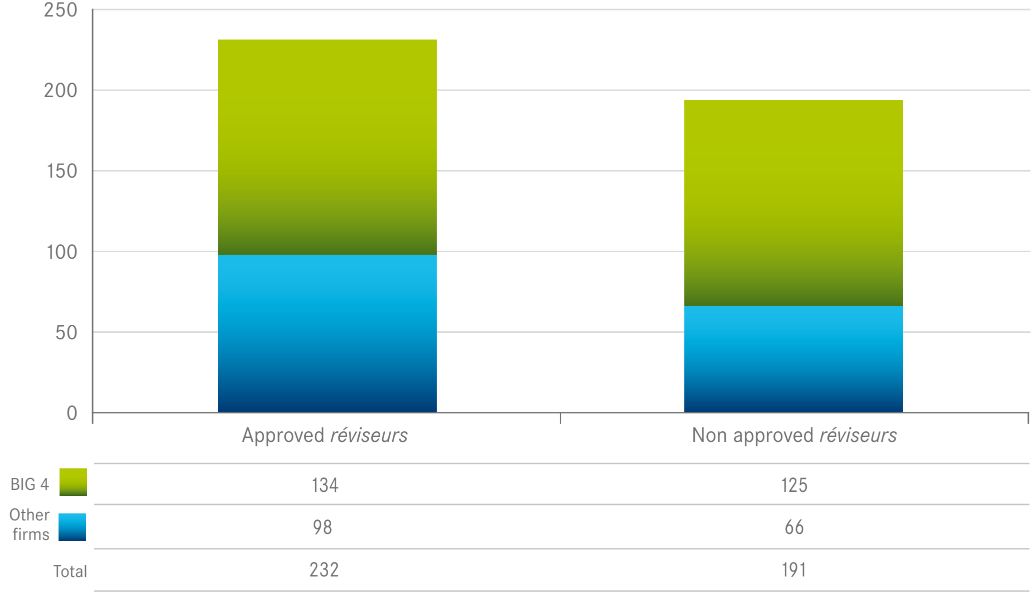
The total number of *réviseurs d'entreprises* and *réviseurs d'entreprises agréés* amounted to 423 as at 31 December 2010.

In 2010, the CSSF granted the title "*réviseur d'entreprises*" to 14 of 23 candidates having passed the examination of professional competence.

Breakdown of *réviseurs* according to status

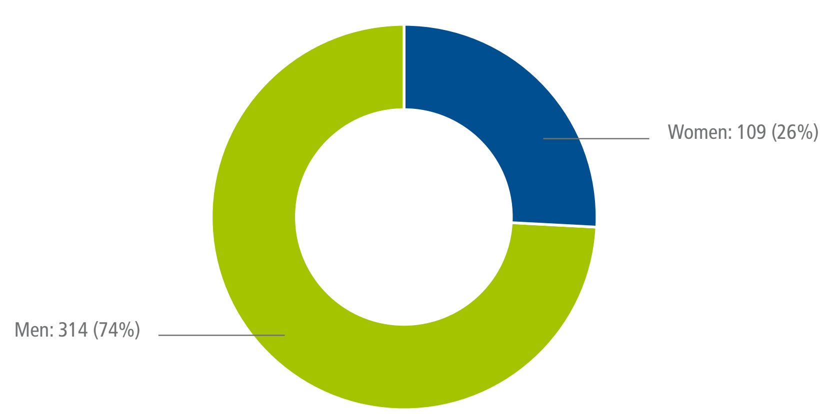


Breakdown of *réviseurs* according to firm and status

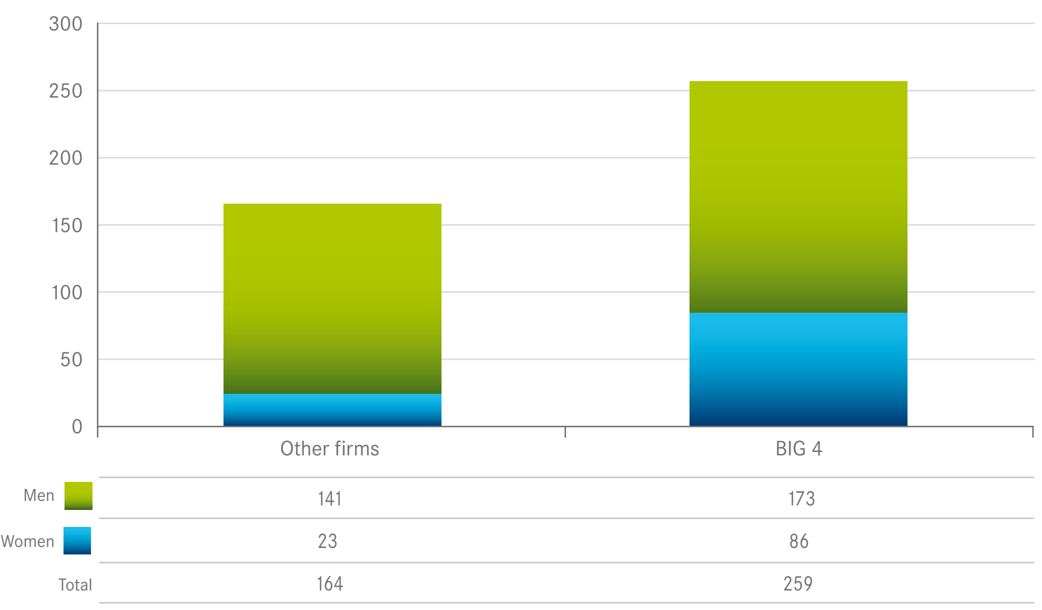


	Approved *réviseurs*	Non approved *réviseurs*
BIG 4	134	125
Other firms	98	66
Total	232	191

Breakdown of *réviseurs* according to gender



Breakdown of *réviseurs* according to firm and gender



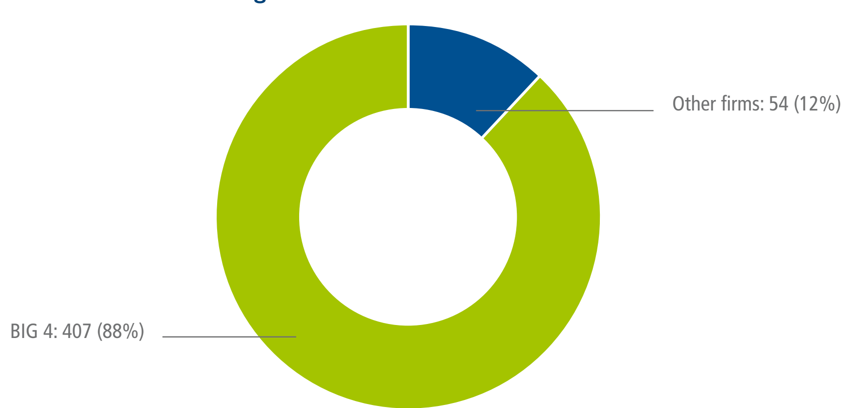
	Other firms	BIG 4
Men	141	173
Women	23	86
Total	164	259

The average age of *réviseurs* is 39.4 years for women (38.4 years in the BIG 4 and 41.1 years in the other firms) and 44.6 years for men (41.1 years in the BIG 4 and 48.9 years in the other firms).

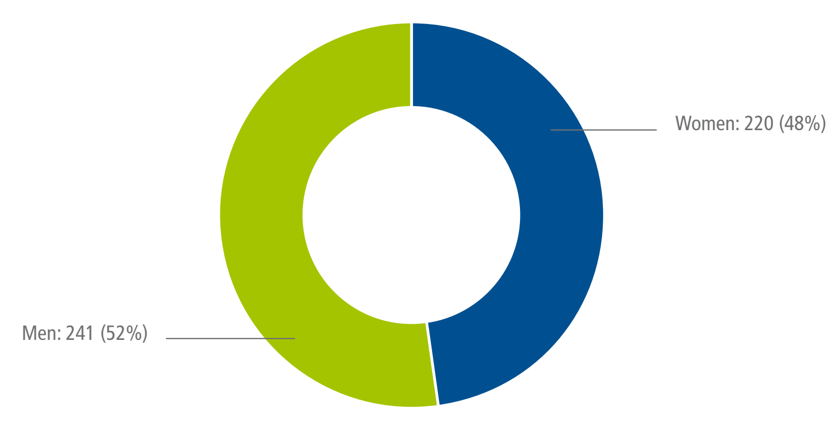
- **Trainee *réviseurs d'entreprises***

The total number of trainee *réviseurs d'entreprises* amounted to 461 as at 31 December 2010.

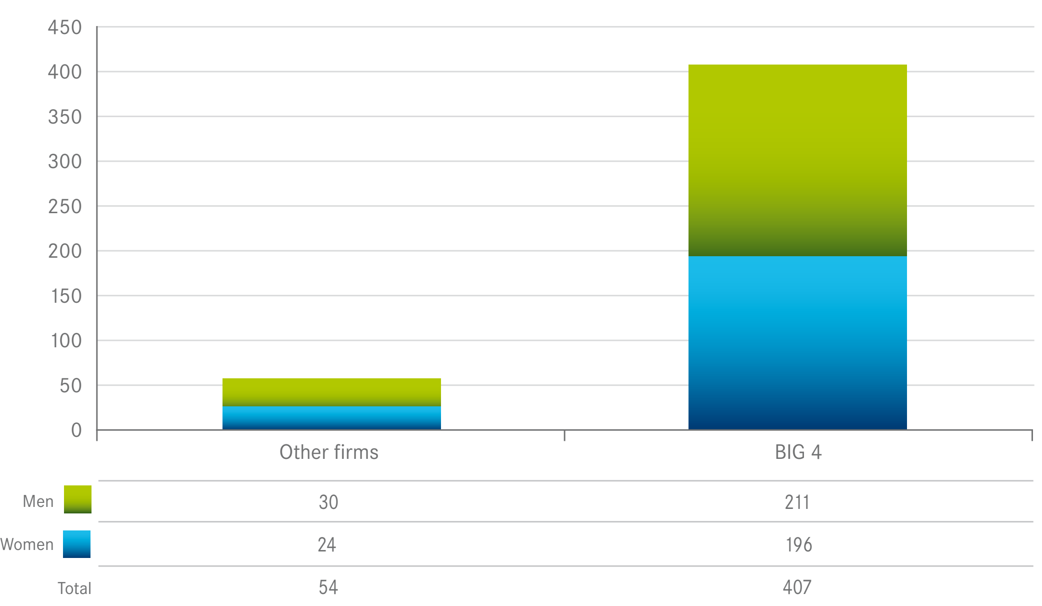
Breakdown of trainees according to audit firms



Breakdown of trainees according to gender



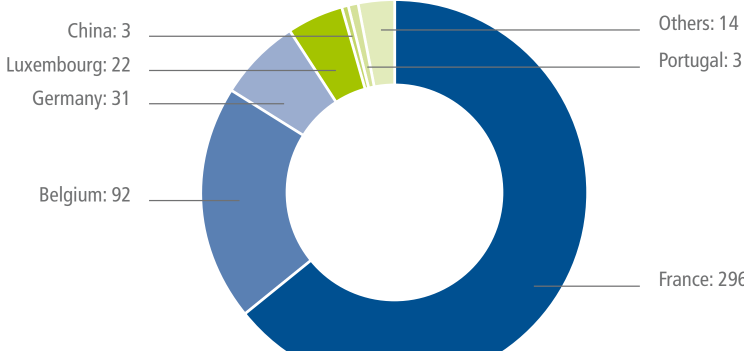
Breakdown of *réviseurs* according to firm and gender



	Other firms	BIG 4
Men	30	211
Women	24	196
Total	54	407

The average age of trainees is 28.3 years for women (28.0 years in the BIG 4 and 30.5 years in the other firms) and 29.8 years for men (29.3 years in the BIG 4 and 33.1 years in the other firms).

Breakdown of trainees according to nationality



3.2.2. Third-country auditors and audit firms

The registration procedure for third-country auditors and audit entities that provide an audit report on the annual or consolidated accounts of a company incorporated outside EU Member States, whose securities are admitted to trading on the regulated market of the Luxembourg Stock Exchange ("third-country auditors") started with the entry into force of the law of 18 December 2009 on the audit profession.

Thus, between 23 February 2010 and 31 December 2010, the CSSF received 65 applications for registration, including 62 from auditors located in transitional third countries within the meaning of Decision 2008/627/EC of the European Commission of 29 July 2008 and three from auditors located in other third countries.

Inspection of eight files revealed that the situation of the third-country auditor did not require registration. 48 files led to a registration and additional information or documents were requested in nine files.

The public register listing all third-country auditors registered by the CSSF is available on the CSSF's website.

Moreover, the CSSF continued its efforts to identify third-country auditors in order to ensure that registrations are exhaustive. As at 31 December 2010, the CSSF counted 415 third-country entities whose securities were admitted to trading on the regulated market of the Luxembourg Stock Exchange.

MEANS OF ADMINISTRATIVE POLICE

11

1. Legal framework

2. Decisions taken in 2010

1. LEGAL FRAMEWORK

The following means of intervention are available to the CSSF to ensure that the persons subject to its supervision comply with the laws and regulations relating to the financial sector:

- injunction, sent by registered letter, requesting the establishment concerned to remedy the particular situation;
- suspension of persons, suspension of the voting rights of certain shareholders or suspension of the activities or of a sector of activities of the establishment concerned.

In addition, the CSSF has the right to:

- impose or ask the Minister of Finance to impose administrative fines on the persons in charge of the administration or management of the establishments concerned;
- under certain conditions, apply to the District Court sitting in commercial matters for suspension of payments of an establishment;
- ask the Minister of Finance to refuse registration on or to withdraw registration from the official list of credit institutions or the other professionals of the financial sector, if an establishment does not fulfil or no longer fulfils the conditions for being or continuing to be registered on the official list in question;
- refuse registration on or withdraw registration from the official list of undertakings for collective investment, pension funds, management companies (Chapter 13 of the law of 20 December 2002), SICARs or securitisation undertakings, if an establishment does not fulfil or no longer fulfils the conditions for being or continuing to be registered on the official list in question;
- under precise conditions laid down by law, request the District Court sitting in commercial matters to order the dissolution and the winding-up of an establishment.

Moreover, the CSSF informs the State Prosecutor of any instance of non-compliance with legal provisions relating to the financial sector, giving rise to penal sanctions and that could entail prosecution against the implicated persons. The following cases are concerned:

- persons performing an activity of the financial sector without holding a licence;
- persons active in the field of domiciliation of companies without belonging to any of the professions entitled to carry on this activity pursuant to the law of 31 May 1999 governing the domiciliation of companies;
- persons other than those registered on the official lists of the CSSF, who use a title or appellation, thereby breaching Article 52(2) of the law of 5 April 1993 on the financial sector, that gives the appearance that they are authorised to perform one of the activities reserved for persons registered on one of the lists;
- attempted fraud.

2. DECISIONS TAKEN IN 2010

2.1. Credit institutions

Pursuant to Article 59(1) of the law of 5 April 1993 on the financial sector, the CSSF imposed an injunction on a credit institution which continuously did not meet the deadlines allotted for the submission of prudential documents required by the CSSF.

The CSSF did not impose administrative fines under Article 63 of the above-mentioned law on persons responsible for the administration or management of credit institutions.

2.2. Other professionals of the financial sector (PFS)

2.2.1. Investment firms

- During 2010, the CSSF did not impose administrative fines under Article 63 of the law of 5 April 1993 on the financial sector on persons responsible for the administration or management of investment firms.
- In 2010, the CSSF did not use its right of suspension, a power conferred upon the CSSF under Article 59 of the above-mentioned law.
- In one case, the CSSF has nevertheless used its right of injunction in accordance with Article 59(1) of the law on the financial sector due to substantial insufficiency of capital bases required by Article 20 of the above-mentioned law.
- In the framework of its mission as supervisor of professionals of the financial sector, the CSSF was informed by the board of directors of an investment firm (hereafter the "company") that reporting tables with manipulated financial data had been transmitted to the CSSF in the context of the electronic transmission of the basic periodic reporting.

  The CSSF's investigation revealed that a managing director of the company had manipulated the company's financial and accounting situation and transmitted these data to the CSSF in order to make the latter believe that the company observed the legal provisions relating to capital bases and structural ratios. The managing director has knowingly hindered the CSSF's prudential supervisory mission by acting in this manner.

  In this context, the CSSF reminds all professionals of the financial sector subject to its supervision that the analysis of the periodical financial information, to be submitted to the CSSF, is an important instrument of its prudential supervision which allows verifying the compliance with the legal provisions relating to capital bases and structural ratios. Consequently, professionals of the financial sector shall draw up, implement and maintain accounting policies and procedures which allow them to provide the CSSF with the relevant and reliable financial information.

  In the above-mentioned case, the CSSF decided that the managing director in question did not act according to the professional standing required under Article 19(1) of the law of 5 April 1993 on the financial sector and considers this person as unable to carry on the activity of managing director of an entity supervised by the CSSF or any other activity subject to authorisation for at least five years. No appeal against this decision was made.
- Following the Madoff case, the CSSF decided, in 2010, that one managing director carrying out the day-to-day management and one member of the board of directors of an investment firm did not have the required professional standing for exercising their respective activities. Therefore, these persons are not able to carry on an activity subject to authorisation at an entity supervised by the CSSF any more.
- In 2010, the CSSF has furthermore filed fourteen complaints with the State Prosecutor related to the illegal exercise of financial sector activities. Ten of these complaints concerned entities which provided investment services without authorisation.

2.2.2. Other PFS

The CSSF imposed an administrative fine based on Article 63 of the law of 5 April 1993 on the financial sector on the persons in charge of the day-to-day management of two other PFS for refusing to communicate the documents and reports of the year-end closing.

2.2.3. Support PFS

In accordance with Article 63 of the law of 5 April 1993 on the financial sector, the CSSF imposed an administrative fine on the managers of two support PFS for non-compliance with the deadlines laid down for the transmission of certain documents.

Moreover, the CSSF requested the Minister of Finance to order the withdrawal of a support PFS from the official list for non-compliance with the legislative and regulatory framework. The Minister of Finance decided to withdraw the authorisation in question.

2.3. Undertakings for collective investment

Pursuant to Article 108(1) of the law of 20 December 2002 relating to undertakings for collective investment respectively to Article 51(1) of the law of 13 February 2007 relating to specialised investment funds, the CSSF imposed administrative fines on the managers of six UCIs and four SIFs for non-filing of audited annual reports within the allotted deadline.

During 2010, the CSSF decided to withdraw seven SIFs from the official list for non-compliance with the legal provisions governing specialised investment funds.

2.4. Investment companies in risk capital (SICAR)

In accordance with the provisions of Article 17 of the law of 15 June 2004 relating to the investment company in risk capital (SICAR), the CSSF imposed 58 administrative fines during 2010. These fines were imposed, on an individual basis, on managers of seventeen SICARs for non-filing or late filing of audited annual reports and management letters.

During 2010, the CSSF decided to withdraw four SICARs from the official list for non-compliance with the legal provisions governing investment companies in risk capital.

2.5. Securities markets

In the context of the supervision of securities markets, the CSSF imposed several injunctions on issuers under the Transparency law. The reason is mainly the late publication and filing of annual and semi-annual financial reports. The non-compliance with an injunction in relation to the publication of regulated information under the Transparency law resulted in an administrative fine. As regards market abuse, an injunction in relation to requirements set out in the law on market abuse was imposed on a party concerned. The different information elements and evidence received during the inquiries lead the CSSF to transmit several files to the State Prosecutor.

2.6. Public oversight of the audit profession

In accordance with Article 67 of the law of 18 December 2009 concerning the audit profession, the CSSF imposed, in 2010, an administrative fine of EUR 1,500 on a *réviseur d'entreprises* (statutory auditor) for not communicating the requested documents and other information. Then, the CSSF imposed on the same *réviseur d'entreprises* (statutory auditor) the suspension of the authorisation referred to in Article 5 of the above-mentioned law and of the registration in the public register. These sanctions were published in the Official Gazette (*Mémorial B*) No 4 of 17 January 2011.

CUSTOMER PROTECTION

12

1. Consumer protection
2. Customer complaints

1. CONSUMER PROTECTION

1.1. Consumer protection at national level

The CSSF is the competent authority to ensure that the persons subject to its supervision comply with the laws protecting consumer interests.

In the framework of this mission, the CSSF cooperates with other national institutions as, for example, the Luxembourg Bankers' Association (*Association des Banques et Banquiers Luxembourg,* ABBL). In 2010, this cooperation allowed finding a satisfactory solution to two issues recurring in the correspondence exchanged between the CSSF and the consumers, namely bank account switching and account research for persons claiming to be heir to a deceased account owner.

1.1.1. Bank account switching

Following discussions with the ABBL, the CSSF published Circular CSSF 10/479 of 29 July 2010 regarding bank account switching.

The circular lays down the application of certain principles in case a customer wishes to close a current account held at a Luxembourg bank (former bank) in order to open a new current account at another Luxembourg bank (new bank).

These principles provide that the new bank may take any steps concerning transfers or organise transfers of recurrent payment transactions as well as the transfer of the available positive account to the new account if the client requests so. The new bank must ask for the information necessary to the transfer within seven days and the former bank must provide this information within seven days.

In November 2010, the CSSF took part, in cooperation with the ABBL, in the assessment of the implementation of these principles *via* a questionnaire sent to several banks.

The answers to the questionnaire showed that the number of disputes related to bank account switching was low in Luxembourg. Thus, only some cases of transmission of incomplete information and non-compliance with the seven days deadline by the former bank were reported. No complaint in relation to bank account switching was submitted to the CSSF.

1.1.2. Account research

The CSSF intervened with the ABBL to try to change the banks' attitude towards heirs who search for an account of a deceased person.

When a relationship with the deceased existed, the banks did not have any problem for sending a positive reply to the beneficiary. However, some banks considered that they were not supposed to answer such requests when they had no relation with the deceased.

In the absence of an answer from the bank, the person searching for an account did not understand why the bank failed to reply to her/his request and often sent a complaint concerning the lack of cooperation by this bank to the CSSF.

The CSSF made the ABBL aware of this problem and the latter recommended its members, after having made the required verification, to provide an answer to persons looking for accounts in the name of a deceased person even if the deceased did not hold an account with them. The ABBL pointed out that in case an account of the deceased did not exist, the bank would not breach the professional secrecy obligation by providing an answer to the heir.

1.2. Consumer protection at international level

In 2010, the CSSF continued its works as regards consumer protection at international level, notably within the FIN-NET, the cross-border network for extra-judicial financial dispute settlement created by the European Commission in 2001 and which is composed of national out-of-court complaint authorities from the European Economic Area.

The CSSF attended two FIN-NET meetings in 2010. These meetings were, among others, about the application in the Member States of the Commission Recommendation of 12 May 2010 on the use of a harmonised methodology for classifying and reporting consumer complaints and enquiries.

The designation of an extra-judicial dispute settlement scheme in relation to the Directive on payment services in the internal market was also discussed during the FIN-NET meetings. In Luxembourg, the CSSF is competent to receive complaints from customers of payment services providers and to intervene with these providers in order to resolve these complaints amicably, pursuant to Article 106 of the law of 10 November 2009 on payment services.

2. CUSTOMER COMPLAINTS

The CSSF acts as an intermediary in the out-of-court dispute settlement between the professionals subject to its supervision and their customers.

The law of 10 November 2009 on payment services confirmed that the CSSF is also competent for complaints regarding payment services provided by credit institutions, post office giro institutions, electronic money institutions and payment institutions.

In 2010, the CSSF continued the implementation of its new procedure in relation to handling complaints which involves that the complainant and the manager appointed to deal with complaints within the supervised entity should come into contact before any intervention of the CSSF in the dispute.

In accordance with Circular IML 95/118 on customer complaint handling, the CSSF's intervention is indeed subject to the condition that the supervised entity dealt with the complaint first and that the client used all the means of recourse against the professional.

In practice, where the complaint letter does not show that the manager appointed to deal with complaints within the supervised entity already intervened in the dispute, the CSSF indicates henceforth, for efficiency purposes, the name of the manager to the complainant and requests the latter to address its complaint with a copy of the CSSF's reply to this manager.

This way of dealing allows the CSSF to ensure that the management of the entity concerned knows about the dispute and that it had the opportunity to talk things over with the customer.

In case the manager appointed to deal with complaints does not answer the customer within a certain time limit or if the customer does not approve of the received answer, the latter may refer the complaint to the CSSF.

This new approach allowed the CSSF to close nearly half of the complaint files in 2010 by sending a letter to the customer indicating the name of the manager to contact in order for the latter to take a decision.

Moreover, the CSSF published on its website an FAQ which aims to provide the customers concerned with useful information in this matter.

2.1. Statistical data

In 2010, the CSSF received 499 complaints concerning entities under its supervision. It closed 396 files, among which were 117 files that were taken over from 2009.

Outcome of the CSSF's intervention / reasons for closing the files

Outcome	Number
Reasoned opinion to the professional	1
Referral to a court during the CSSF's scrutiny	3
WIthdrawal by client	9
Others	17
Amicable settlement following the CSSF's opinion	23
Contradictory positions	24
Spontaneous amicable settlement	43
In favour of the professional	76
Acknowledgment of receipt where the complainant did not come back to the CSSF	200
Total	**396**

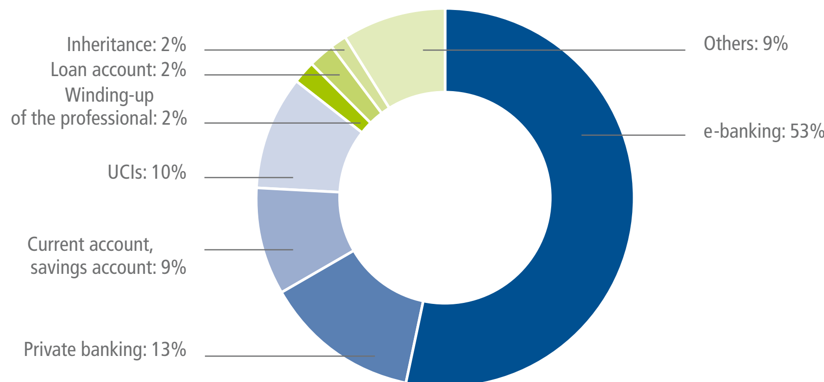
It is to be noted that the CSSF's goal consisting of reaching an amicable settlement for the parties concerned is often achieved. The fact that a relatively important number of acknowledgements of receipt sent by the CSSF resulted in closing the files without any further action is probably due to the fact that the complainant often obtained satisfaction from the professional after having contacted the manager appointed to deal with complaints as indicated by the CSSF. Consequently, the new approach according to which the complainant shall first contact the professional directly is successful.

However, where the parties concerned cannot "spontaneously" reach an amicable settlement, the CSSF decides on the dispute by giving its opinion.

The relatively small number of cases where the CSSF drew up a reasoned opinion against the professional is notably due to the fact that the CSSF does only draw up reasoned opinions if it notes that the professional made a mistake, that the complainant suffered a prejudice and that there is a causal link between the professional's mistake and the customer's prejudice.

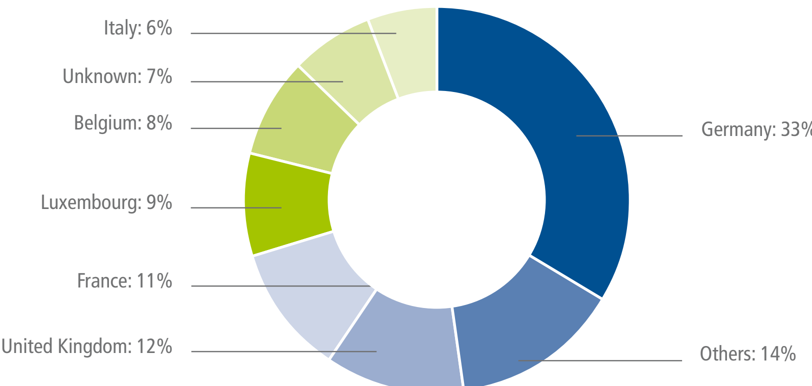
In some cases, the CSSF is not able to decide on a dispute. It notes then that the versions of the parties to the dispute are not compatible and cannot be verified and that the CSSF cannot let one version prevail over another ("contradictory positions").

Breakdown of complaints according to their object



Most of the complaints concern e-banking. The complaints linked to private banking also constitute an important part of the disputes handled by the CSSF. It should be noted that the number of complaints regarding UCIs is very small compared to the importance of the UCI sector in Luxembourg.

Breakdown of the complaints according to the complainant's country of residence



Most complainants live in Luxembourg or in the neighbouring countries. The country of residence of the complainants is unknown in 7% of the cases because the complainants contacted the CSSF *via* e-mail without indicating the country of residence. Furthermore, the category "Others" covers about forty different countries.

Generally, the CSSF notes that the financial sector customers are more aware of their rights as regards investor protection. Thus, many complainants refer to the MiFID Directive and the Directive on payment services.

The increase of transparency in the financial services as sought after by the recent European directives regarding the financial sector has positively influenced the public. The CSSF notes that the customers insist on signing risk profiles and on being well informed by their financial institutions regarding the pricing applicable to the provided services.

The CSSF also experiences a change of mentalities, insofar as the customer follows its financial institution more closely now. This phenomenon may be explained by the fact that, due to the IT means and the Internet, the customer has sources of information which are more varied and sophisticated allowing her/him to better understand and compare the professional's provisions of services.

2.2. Analysis of the complaints handled in 2010

The analysis of the cases dealt with in 2010 is focussed on the following points:

- explanation of the means the CSSF uses to form an opinion;
- examples of cases impossible to decide on;
- professionals' interest to thoroughly examine the instructions from customers living in remote countries.

2.2.1. Means available to the CSSF to form an opinion

The CSSF disposes of limited powers of investigation that it exercises within the context of procedures based on writings. It cannot take into account testimonies or require an oath from a party. Thus, when the CSSF receives a complaint, its analysis is mainly based on written documents (contracts, terms and conditions, exchange of letters, etc.). Increasingly often, the CSSF has records of telephone conversations in order to form an opinion.

- **Written documents**

In one case, a private individual complained that her/his bank made her/him acquire units/shares of an investment vehicle without providing adequate explanations on the subject.

The bank stated that the complainant invested her/his assets in that investment vehicle while being well-informed and evoked notably a brochure which the adviser of the bank used to present the product to her/him. The documentation mentioned the specificities of the investment vehicle and informed, among others, that the vehicle was based in the British Virgin Islands, that it was investing in a pool of hedge funds and that it was diversified in its strategies and administration. The bank asserted that the complainant received the presentation brochure as evidenced by the acknowledgement of receipt in the contractual file. Furthermore, the bank established with supporting documents that all the contractual documents were signed by the complainant.

The CSSF therefore concluded that the complainant could not accuse the bank of investing her/his money without her/his knowledge.

It should be noted that the CSSF did not take into account the complainant's comment that s/he did not understand the terms of the documents that s/he signed because they were in English, a language s/he claimed not to understand. Indeed, the CSSF drew the complainant's attention to the fact that if the professional shall in principle inform its clients on the risks that the contemplated transactions involve in order to allow these clients to be well-informed while they invest, the clients have also an obligation to ask the professional in case of doubt or problem in understanding.

In another dispute, the CSSF considered as the deciding factor a brief e-mail sent by the client to the person in charge of her/his account to accept the new investment constraints.

The client had given to a bank a discretionary management mandate for which the investment constraints were strictly defined so that the bank could only invest the client's assets into alternative products, shares or bonds by observing certain quotas. A constraint was also imposed on the bank as regards liquidities.

The client seemed satisfied with the management of her/his assets until s/he was informed that her/his portfolio performed badly in 2008. The client then informed the bank of several grievances s/he had against it, among which the non-compliance with the investment constraints defined in the discretionary management contract.

The bank objected to the client's allegations. The bank explained that the constraint set in the contract for the investment in alternative products was exceeded with the complainant's authorisation. Indeed, at a certain time when the discretionary management was profitable for the client, the bank sent her/him an e-mail in order to warn her/him that an agreed investment constraint had been exceeded and to ask for her/his instructions. The complainant answered in a short e-mail that the liquidity constraint was annulled and that s/he approved of the risk exposure presented to her/him.

Based on this exchange of e-mails, the CSSF concluded that the complainant had indeed accepted changes in the investment constraints and that the bank did not violate the limits set out in the discretionary management contract.

Nevertheless, the CSSF admitted that the complainant's other grievances against the bank were justified and overall decided in her/his favour, notably because the bank did not inform the complainant of the real nature of an important part of the investments.

The CSSF's position may also be determined by an analysis of the written documents delivered by the parties during the dispute. Thus, a private individual had given to a professional the management of her/his assets under the terms of a discretionary management mandate. The client expressly chose a dynamic management profile which involves the highest risks. Afterwards, s/he complained to the bank that it acquired products which did not correspond to her/his profile and that it sold securities at a price which was not agreed.

The CSSF examined the different e-mails put forward by the complainant as proof of her/his grievances. In the termination e-mail that the complainant sent to the person in charge of her/his account, s/he requested the termination of the management contract due to family problems, specifying that the management of the assets by the adviser was not the reason for the termination.

The CSSF has taken notice of this comment, without however considering the complaint as unfounded based on this comment alone. The CSSF had also taken into account other elements of the file in order to form its opinion.

Consequently, the study of the cases mentioned above shows that the clients shall consider the impact of their writing or of their signing in the framework of their relation with a financial professional and that they cannot prevail themselves of an "alleged" ignorance when the markets performed badly once they have expressly accepted a given risk exposure.

- **Phone conversation records**

In the 2009 Annual Report (cf. page 197), the CSSF emphasised that even if the professionals of the financial sector are not required to record phone conversations with their clients, Circular IML 93/101 on rules concerning the organisation and internal control of the market activity of credit institutions highly recommends it.

The question relating to the recording of phone conversations by professionals was recently raised by the European Commission in the consultation paper of 8 December 2010 on the review of the MiFID Directive. The European Commission envisages, among others, to require the recording of orders from clients acting on own account. The European Commission considers that these records are beneficial particularly for detecting market abuse. Moreover, it is contemplated that Member States will have the right to impose additional requirements for the recording of orders given in the framework of portfolio management.

Nevertheless, the European Commission is aware that data protection should be ensured and the relevant directives complied with.

It should be noted that the European Commission provides that the recording requirement shall not only apply to phone conversations. The requirement shall also concern any electronic form of communication. Records shall be kept for at least three years but the Member States may set a longer period.

The European Commission notes in this context that Article 51(4) of Directive 2006/73/EC of 10 August 2006 implementing the MiFID Directive as regards organisational requirements and operating conditions for investment firms provides for the possibility for Member States to impose obligations on investment firms relating to the recording of telephone conversations or electronic communications involving client orders. Whereas some Member States transposed this obligation into their national law, others did not.

The following cases show that records of phone conversations were judiciously used by the CSSF in order to make a decision on a dispute.

In the framework of a dispute between a client and her/his credit institution, the CSSF received several CD-ROMs on which different phone conversations were recorded. With the credit institution's consent, the CSSF transmitted these records to the complainant for comments, notably due to the fact that the conversations were held in a language not customary in Luxembourg. The complainant confirmed that the records included conversations s/he had with the bank. However, s/he stated that the records were incomplete, that they had been tampered with and that they were not correctly dated. The CSSF recognised that these records had an indicative value for the settlement of the dispute.

In another dispute, the truth about the reciprocal allegations appeared after the CSSF had analysed long phone conversations recorded on CD-ROMs. The CSSF thus noted that the complainant, who claimed that the person in charge of her/his account executed a transaction without her/his permission, had expressly approved of the transaction.

In another case, the phone conversation records that the bank transmitted to the CSSF allowed tracing which successive transactions the complainant requested her/his bank to execute. Without these records, the CSSF would not have been able to form an opinion on the respective responsibilities of the parties to the dispute. The fact that the complaining party did not question the authenticity of the conversations recorded and communicated by the CSSF reinforced the latter's opinion.

The listening of the phone conversation records also allowed restoring the truth in a case in which the client complained of the non-execution of her/his stock exchange order by asserting that s/he clearly agreed on this execution with the person in charge of her/his account. The analysis of the records showed that the complainant in fact ordered not to execute the disputed transaction. S/he ordered to leave things as they were because s/he expected a more favourable development of the securities subject to the transaction.

2.2.2. Impossibility to decide on a dispute

In some cases, the CSSF is not capable to decide on a dispute, notably where the question is raised of the applicability of a foreign law or a court decision made by a judge external to the dispute, notwithstanding the fact that the CSSF is competent to deal with this dispute pursuant to Article 58 of the law of 5 April 1993 on the financial sector. This situation is illustrated by the following two inheritance disputes.

In the first case, a Belgian couple signed an agreement for a joint account with a Luxembourg bank. After the death of one of the co-account holders, an heir who cannot legally be disinherited (forced heir) (= the complainant) requested the bank not to execute withdrawals from or transactions on the account without her/his authorisation.

Afterwards, the complainant informed the bank *via* a lawyer that the succession was disputed and was subject to a procedure of liquidation for the purpose of distribution at the *Tribunal de première instance de Bruxelles*, a procedure in which s/he is opposed to the other heirs. However, even if the *Tribunal de première instance de Bruxelles* decided to dismiss the request for partial distribution made by the other heirs, the bank executed an order concerning the disputed account in favour of the other heirs.

The bank justified itself to the CSSF by stating that one of the heirs was in a difficult financial situation and that following a statement drawn up by Belgian notaries, half of the assets held in the bank's account was the property of this heir. Furthermore, the bank stated that the decision of the Belgian judge put forward by the complainant's lawyer could not have effect against it because the bank was not party to the trial in Belgium.

The CSSF considered that it could not blame the bank for not wanting to return the funds given to some heirs despite the opposition of the complainant, notably because the bank could not be sure that the complainant had suffered a loss as long as the succession was not settled.

In a second case, a German citizen put forward an inheritance certificate established according to German law (*Erbschein*) in order to receive, from a Luxembourg bank, exhaustive information about the belongings of a deceased relative. The validity of the inheritance certificate was confirmed by a German court. The sole legatee of the deceased objected to the bank's transmission of this information to the above-mentioned heir who cannot legally be disinherited (forced heir). S/he disputed the validity of the inheritance certificate at the competent German jurisdiction and informed the bank *via* a lawyer that the bank would be sued if it disclosed confidential information, notably based on a false inheritance certificate, to an unauthorised person.

The CSSF concluded that it could not retain a misconduct of the bank and that the competent judicial authorities should decide on the dispute.

2.2.3. Verification of the origin of the payer's instructions

A particular type of complaint was recently referred to the CSSF. This type of complaint was already dealt with in the past and concerns especially clients domiciled in remote countries (South Africa in this case).

A usurper pretending to be the client asks the Luxembourg financial professional to close her/his account or to redeem her/his units of UCIs. In general, the proceeds of these transactions shall be transferred to an account opened at an Asian bank.

The redemption order or the instruction to close the account often mentions new contact details (postal address or e-mail, fax, telephone) of the "client". Concerned about indicating to the "client" the conditions to be fulfilled for the execution of the transaction, the Luxembourg professional contacts the "client" using the new contact details. The "client" sends then the required documents to the professional.

As the submitted information and documents as regards the authenticity are not thoroughly analysed, the orders to close the account and to redeem are executed and the proceeds of the transaction transferred to an account opened with an Asian bank.

Later, the professional is contacted by the "true" client who declares that s/he had never made this order and requests compensation for the damage that was caused to her/him.

Faced with the professional's inertia, the client refers the case to the CSSF. The CSSF often notes that the professional had not been cautious enough in its analysis of the circumstances relating to the instructions received from the (alleged) client. Differences, as for example regarding the spelling of the client's name, some elements of the copy of the passport, the signature of the client, the post box number or the telephone, etc., should have made the professional suspicious.

The CSSF can only recommend to the professionals to thoroughly verify the clients' identities when they receive instructions to close an account or to redeem units of UCIs from clients or investors domiciled in remote countries, especially if the professionals do not know the clients or investors personally. One elementary rule to observe by a prudent professional is to ensure by using all possible means that the person who gave an order is indeed its client and to contact the latter before executing any transaction on her/his account.

FIGHT AGAINST MONEY LAUNDERING AND TERRORIST FINANCING

13

1. Amendments to the regulatory framework regarding the fight against money laundering and terrorist financing
2. Participation of the CSSF in meetings regarding the fight against money laundering and terrorist financing
3. Reports regarding the fight against money laundering and terrorist financing

1. AMENDMENTS TO THE REGULATORY FRAMEWORK REGARDING THE FIGHT AGAINST MONEY LAUNDERING AND TERRORIST FINANCING

In 2010, substantial efforts were made by the legislator to review the anti-money laundering and counter-terrorist financing regulatory texts and by the CSSF to adapt its prudential supervision in this area.

The Luxembourg anti-money laundering and counter-terrorist financing ("AML/CTF") regulatory framework has thus been revised with the aim to faithfully adopt the terminology of the 40+9 Recommendations of the Financial Action Task Force (FATF) and of the relating methodology and to take account of the conclusions of the mutual evaluation report of the Luxembourg framework adopted by the FATF. This revision, which started in 2009 with Grand-ducal regulation of 1 December 2009, continued in 2010 with the adoption of Grand-ducal regulation of 1 February 2010 which provided important details on the professional obligations for the prevention of money laundering and terrorist financing.

1.1. Amendment of the law of 12 November 2004 on the fight against money laundering and terrorist financing

The law of 27 October 2010 enhancing the anti-money laundering and counter-terrorist financing legal framework entered into force on 7 November 2010. The main amendments concerning the professionals of the financial sector may be summed up as follows:

- The scope of the law of 12 November 2004 on the fight against money laundering and terrorist financing has been extended. It now takes into account the managers and advisers of undertakings for collective investment, of investment companies in risk capital and of pension funds, the securitisation undertakings which exercise the activity of service provider to companies and trusts, the professionals incorporated under foreign laws which provide services in Luxembourg without establishing a branch and all the persons who conduct as a business one or more of the activities or operations listed in the annex to the law. The Luxembourg regime now applies to all branches and subsidiaries established abroad by Luxembourg professionals.
- In order to take into account the risk-based approach, professionals must perform a written risk assessment of their activities.
- The simplified due diligence regime has been detailed and may be applied to the identification and verification of the client and of the beneficial owner. The conditions for the application of this regime have also been tightened.
- As far as enhanced due diligence is concerned, details have been provided as regards politically exposed persons and the regime applicable to correspondent banking relationships.
- The cooperation requirements with the authorities have been further explained. They have moreover been detailed in circular 22/10 of 8 November 2010 published by the Luxembourg Financial Intelligence Unit (FIU).

The legal enhancements to the prudential supervision in relation to AML/CTF entail the implementation of a close cooperation and exchange of information between the competent authorities as well as the enhancement and extension of the range of sanctions available to the CSSF. The CSSF's legal mission has been completed and it henceforth expressly includes measures to prevent that associates of criminals take control of persons subject to the supervision of the CSSF.

1.2. Law of 27 October 2010 implementing United Nations Security Council resolutions as well as acts adopted by the European Union concerning prohibitions and restrictive measures in financial matters in respect of certain persons, entities and groups in the context of the combat against terrorist financing

This law sets the general framework allowing authorities to ensure an efficient compliance with all prohibitions and restrictive measures that Luxembourg must implement pursuant to its international AML/CTF obligations towards the United Nations (UN) and the EU. The purpose of the law is to provide for a legal basis allowing acting in those cases where the EU has not yet implemented prohibitions and restrictive measures decided by the UN or where the EU has no competence to implement them. The Minister of Finance is competent for any questions in relation thereto and the role of the CSSF is to verify the correct application of these provisions by the professionals under its supervision. The implementation of these provisions and applicable procedures are detailed on the website of the Ministry of Finance under the heading "*Sanctions financières internationales*" (International financial sanctions - www.mf.public.lu).

1.3. Grand-ducal regulation of 29 October 2010 implementing the law of 27 October 2010 implementing United Nations Security Council resolutions as well as acts adopted by the European Union concerning prohibitions and restrictive measures in financial matters in respect of certain persons, entities and groups in the context of the combat against terrorist financing

The purpose of this Grand-ducal regulation is to define the practical application of the law of 27 October 2010 (cf. point 1.2. above). It sets out the texts to implement, defines the relevant restrictive measures, establishes the conditions for implementation and details the tasks of the various authorities acting in this area. The designation of persons, entities or groups in this context is performed in Luxembourg through ministerial regulations.

2. PARTICIPATION OF THE CSSF IN MEETINGS REGARDING THE FIGHT AGAINST MONEY LAUNDERING AND TERRORIST FINANCING

In 2010, the CSSF took part in the meetings and works of the following national and international groups.

2.1. International working groups

2.1.1. Financial Action Task Force (FATF) and its working groups

Following the adoption of the third mutual evaluation report of Luxembourg at the FATF Plenary in February 2010, the efforts to adapt the Luxembourg AML/CTF framework and to remedy the weaknesses identified have materialized in follow-up reports to the FATF Plenary meetings held in June 2010, October 2010 and February 2011. Moreover, detailed reports have been drawn up for the specific FATF sub-group, the International Cooperation Review Group (ICRG), in charge of laying down, and where applicable, publicly identifying the countries with key AML/CTF deficiencies. The FATF Plenary of February 2011 represented an important step for the assessment of the progress made by Luxembourg in order to respond to the critics expressed by the FATF. It is also based on the conclusions of the ICRG working group that the FATF updated the list of high-risk and non-cooperative countries and territories.

Since March 2010, six mutual evaluation reports made by the FATF in the context of the third round of AML/CTF mutual evaluations have been published. The following countries have been assessed: Argentina, Saudi Arabia, Brazil, France, India and the Netherlands. By the end of February 2011, all FATF members will have been assessed and the evaluation exercise of the members of the FATF-style regional groups will also be finalised.

As concerns in particular the works carried out by the FATF in 2010, the 40+9 Recommendations have been reviewed and adapted in consideration of the fourth round of mutual evaluations. In this context, you may refer to the consultation paper titled "The Review of the Standards - Preparation for the 4th round of Mutual Evaluations" which has been published on the FATF website and which includes the first conclusions of the two competent working groups.

Between March 2010 and February 2011, the FATF also finalised three reports describing the methods or new trends used in money laundering or terrorist financing, i.e. the reports titled "Money Laundering Using New Payment Methods", "Money Laundering Using Trusts and Company Service Providers" and "Money Laundering vulnerabilities of Free Trade Zones". Moreover, the FATF developed an information note on the implication of an efficient AML/CTF fight on the fight against corruption.

2.1.2. Committee for the prevention of Money Laundering and Terrorist Financing (CPMLTF)

This committee, instituted by the European Commission, was established pursuant to Article 41 of Directive 2005/60/EC of 26 October 2005 on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing. The committee assists the European Commission in its work related to this subject.

The CPMLTF met five times in 2010. These meetings concerned, amongst others, the preparation of the FATF Plenary meetings and the coordination of the positions between Member States.

2.1.3. Anti-Money Laundering Task Force (AMLTF)

This European working group, established by the three committees CESR, CEBS and CEIOPS, will be replaced by a sub-committee of the Mixed Committee of the three new European supervisory authorities ESMA, EBA and EIOPA, in place since 1 January 2011.

In 2010, the discussions of this cross-sectoral group mainly focussed on the following subjects: identification and determination of the beneficial owner, simplified due diligence and fight against money laundering and terrorist financing applied by payment institutions, their branches and their agents.

2.1.4. AML/CTF Expert Group (AMLEG)

This working group of the Basel Committee on banking supervision worked in 2010 essentially on the following two topics: the concept of the risk-based approach in the context of AML/CTF prudential supervision and the cooperation between supervisory authorities.

2.1.5. The Wolfsberg Group

During its annual meeting at the end of May 2010, the group addressed recurrent subjects such as cover payments and the fight against corruption (politically exposed persons) as well as new issues such as Carbon Trading certificates, human trafficking and financing of the proliferation of weapons of mass destruction.

2.1.6. UN Counter-terrorism Committee

The CSSF participated in the study on the implementation of the United Nations Security Council Resolution 1373 (2001) on the fight against terrorism. The report relating to this study has been published by the committee at the beginning of 2010.

2.1.7. Other works

In a broader context than the one of the fight against money laundering and terrorist financing, the CSSF also participated, in 2010, in other assessments of the Luxembourg legal framework, mainly in the fields of general crime, corruption and financing of the proliferation of weapons of mass destruction.

2.2. National working groups

At national level, the CSSF was largely involved in the preparatory works of the above-mentioned law of 27 October 2010, both in the preliminary drafting of the law and during the meetings of the legal commission of the *Chambre des Députés*.

Following the adoption of this law, the Anti-Money Laundering Consultative Committee established within the CSSF immediately met to inform its members of the new provisions and of the new powers and supervisory approaches of the CSSF on this subject, in particular with regard to on-site inspections.

In this same context, the CSSF participated in several meetings of the *ad hoc* Anti-Money Laundering Committee of the *Commissariat aux Assurances*.

The CSSF is also a member of the follow-up Committee on "international restrictive measures" put in place pursuant to Grand-ducal regulation of 29 October 2010 implementing the law of 27 October 2010. The committee met twice at the Ministry of Finance; the agenda concerned mainly the implementation of the financial restrictive measures against Iran following the adoption of EU Regulation No 961/2010 of 25 October 2010.

In order to enhance the cooperation with the Luxembourg Financial Intelligence Unit (FIU), the CSSF and the FIU met to exchange their views on the organisation of this close cooperation and exchange of information provided for by law.

At the level of the CSSF, it is worth mentioning the setting-up of the Risk-Based Approach Committee (RBAC) in charge of the preparation and follow-up of the implementation of the AML/CTF supervisory risk-based approach carried out by the CSSF. After having formalised this approach in an internal procedure, the CSSF is now carrying out a classification of the professionals submitted to the law of 12 November 2004 according to their money laundering or terrorist financing risk exposure. A questionnaire addressed to the professionals will allow the CSSF to evaluate the professionals' own risk assessment on this subject and the measures that they have taken in order to mitigate these risks.

3. REPORTS REGARDING THE FIGHT AGAINST MONEY LAUNDERING AND TERRORIST FINANCING

In 2010, the number of AML/CTF reports substantially increased to reach 1,015 reports, which confirms the upward trend over the past years. In addition to the money laundering or terrorist financing suspicious transaction reports made pursuant to Article 5(1) of the law of 12 November 2004, this number also includes the reports received by the CSSF based on European texts which provide for the freeze of assets and economic resources in respect of certain persons, groups or entities. The above-mentioned total number does not take into account the reports made by one particular professional.

The total number of reports received can be split as follows according to the various categories of professionals:

- banks made 842 reports;
- PFS made 164 reports, of which 143 were received from other PFS and 21 from investment firms;
- management companies made 9 reports.

In total, 115 professionals of the financial sector transmitted at least one report to the CSSF in 2010 (against 103 professionals in 2009, 103 professionals in 2008 and 89 professionals in 2007). Considering the total number of professionals of the financial sector subject to the law of 12 November 2004 and the obligations in relation to international financial restrictive measures, this increase in the number of professionals which made a report in 2010 is considered insufficient, despite the constant upward trend.

The detail of the 115 professionals concerned is as follows:

- 75 banks out of 146 banks registered on the official list as at 31 December 2010;
- 33 PFS, among which 11 investment firms, out of 301 PFS registered on the official list as at 31 December 2010;
- 7 management companies out of 179 management companies registered on the official list as at 31 December 2010.

The analysis of the number of reports received from professionals reveals that at least 74% of the reports made in 2010 have been received from fourteen banks and two PFS which each sent at least ten reports during the year. Despite the substantial increase in the total number of reports, the number of professionals which sent a report remains quite constant, as generally speaking the same professionals make these reports.

Compared to the number of suspicious transaction reports on money laundering or terrorist financing of the previous year, the following conclusions can be drawn in relation to the basis on which these reports are made:

- the number of reports based on Article 5(1)(a) of the law of 12 November 2004 substantially increased;
- the number of reports following a request by the FIU based on Article 5(1)(b) of the above law increased by more than one third;
- the number of reports made based on a search and seizure warrant following a national or international instruction has more than doubled.

Moreover, the important number of reports for which the suspicion is linked to infringements related to forgery or fraud mostly harming the client, and not performed by the latter, as well as the decrease in the number of reports (more than one third) based on a decision to refuse to enter into a business relationship with a potential customer confirm the trends already observed over the last years.

Among the reports made pursuant to the obligations resulting from European texts which provide for the freeze of assets or economic resources of certain persons, groups or entities, it is worth mentioning the reports related to Iran, without however taking into account the notifications or authorisation requests in view of a transaction with persons located in Iran for which the responsibility rests with the Luxembourg Ministry of Finance and Ministry of Foreign Affairs.

The CSSF itself made two reports of suspicions of money laundering and terrorist financing to the State Prosecutor's office at the Luxembourg district court (*Tribunal d'Arrondissement*), in accordance with its obligations resulting from Article 23(3) of the Code of Criminal Procedure.

BANKING AND FINANCIAL LAWS AND REGULATIONS

14

1. Directives and regulations under discussion at EU Council level
2. Directives adopted by the Council and the European Parliament but not yet implemented under national law
3. Luxembourg laws and regulations adopted in 2010

1. DIRECTIVES AND REGULATIONS UNDER DISCUSSION AT EU COUNCIL LEVEL

The CSSF participates in the groups examining the following proposals for directives or regulations.

1.1. Proposal for a regulation on over-the-counter (OTC) derivatives, central counterparties and trade repositories

In the second half of 2010, the EU Council started discussions on the proposal of 17 September 2010 for a regulation on OTC derivatives, central counterparties and trade repositories. This proposal is placed in the context of the EU's G20 commitments and the approach adopted by the United States. It aims at increasing transparency of the OTC derivatives market, reducing counterparty credit risk and operational risk and enhancing market integrity and oversight.

It proposes that standard OTC derivative contracts be cleared through central counterparties (CCPs) and that all OTC derivative contracts be reported to trade repositories that must be accessible to the supervisory authorities mentioned in the proposal. The proposal applies to financial and non-financial counterparties that hold large positions in this type of instrument.

1.2. Proposal for a regulation amending Regulation (EC) No 1060/2009 on credit rating agencies

This proposal for a regulation follows the publication of Regulation (EU) No 1095/2010 establishing the European Securities and Markets Authority (ESMA) and aims at transferring supervisory powers over credit rating agencies currently exercised by the competent national authorities to ESMA. ESMA will also have investigation powers and sanctioning powers over credit rating agencies. This transfer of competences will considerably facilitate the registration procedure and supervision of credit rating agencies belonging to international groups.

Nevertheless, ESMA may delegate powers to national supervisory authorities for supervision. The national supervisory authorities will also remain competent to supervise the use of credit ratings by the supervised entities pursuant to Article 4(1) of Regulation (EC) No 1060/2009.

1.3. Proposal for a directive amending Directives 2003/71/EC and 2009/138/EC in respect of the powers of the European Securities and Markets Authority and the European Insurance and Occupational Pensions Authority (Omnibus Directive II)

At the time of the discussions on Directive 2010/78/EU (Omnibus Directive I), other "Omnibus" directives had already been announced in order to adapt sectoral regulations to the new architecture of European supervision. The proposal for an Omnibus Directive II thus mainly covers the insurance sector (amendment of Directive 2009/138/EC) which was barely covered by Omnibus Directive I. The second set of amendments operated by Omnibus Directive II concerns the Prospectus Directive and follows the amendment of the latter by Directive 2010/73/EU.

1.4. Proposal for a directive on deposit-guarantee schemes (recast)

As part of its work to make more secure and to consolidate the financial system, to prevent and manage crises and to restore consumer confidence, the European Commission proposed, on 12 July 2010, to recast Directives 94/19/EC and 2009/14/EC on deposit-guarantee schemes.

The proposal for a directive provides that bank account holders must be compensated within one week in case of a bank failure. In order to ensure that the deposit-guarantee schemes have financial means that are proportionate to their liabilities and that these financial means are safeguarded against potential losses, the proposal provides for a four-step funding mechanism and restrictions on investment of the financial means. As a first funding measure, every deposit-guarantee scheme must have at its disposal *ex-ante* 1.5%

of eligible deposits after a transition period of ten years. The guaranteed deposits, i.e. the eligible deposits below the guarantee ceiling that reflect the deposit-guarantee scheme's liabilities more adequately, will only progressively form the basis for the calculation of credit institutions' contributions to the system's funding. The calculation of the credit institutions' contributions will be based on the institutions' risk profiles. Finally, it must be noted that the proposal for a directive does not prevent the deposit-guarantee schemes' funds from being used for bank resolution purposes.

1.5. Proposal for a directive amending Directive 97/9/EC on investor-compensation schemes

In September 2010, the EU Council started discussions on a proposal for a directive amending the directive on investor-compensation schemes. At the same time, the European Commission published a White Paper on insurance guarantee schemes.

Like in the proposal for a directive on deposit-guarantee schemes, the proposal for a directive on investor-compensation schemes lays down several fundamental principles that must govern the financing of these systems. Although the two systems protect consumers against risks of a different nature and scale, the proposal for a directive on investor-compensation schemes also provides for an *ex-ante* financing mechanism. The minimum target level is set at 0.5% of the guaranteed funds' and financial instruments' value within a ten-year period. The proposal also provides for a faster compensation of investors and increases the level of compensation to EUR 50,000 (against the current EUR 20,000). Finally, it must be noted that the proposal does not only align its scope on that of MiFID, but extends the scope of protection to undertakings for collective investment in transferable securities (UCITS) and their unitholders where losses are suffered due to the failure of a UCITS depositary or sub-custodian.

1.6. Proposal for a directive amending Directives 98/78/EC, 2002/87/EC and 2006/48/EC as regards the supplementary supervision of financial entities in a financial conglomerate

Following the analysis of the Joint Committee on Financial Conglomerates (JCFC)[1] and a consultation of interested parties, the European Commission proposed, on 16 August 2010, a review of the Financial Conglomerates Directive and the sectoral directives in order to eliminate unintended consequences and technical omissions in the sectoral directives and to ensure that the Financial Conglomerates Directive's objectives are effectively achieved.

The amendments aim to align supervisory powers at the top level of a conglomerate and to prevent the loss of powers when a group structure changes as well as the duplication of supervision at the conglomerate level. At the same time, the proposal should tackle the ambiguity regarding parameters and the lack of a risk-based identification of financial conglomerates. Finally, the problem of day-to-day treatment of participations under supplementary supervision should be addressed.

Moreover, a more fundamental debate regarding supplementary supervision was initiated in 2010. This debate focuses on supervisory scope and capital related issues.

[1] As from1 January 2011, reference should be made to the Sub-committee on financial conglomerates attached to the Joint Committee of the European Supervisory Authorities.

1.7. Proposal for a regulation on short selling and certain aspects of credit default swaps (Short Selling Regulation)

On 15 September 2010, the European Commission adopted a proposal for a regulation on short selling and certain aspects of credit default swaps (CDS). The proposal's objectives are to increase transparency, reduce risks and create a harmonised framework for coordinated action at European level.

Short selling is the sale of a security the seller does not own with the intention of buying it at a later point in time in order to deliver it. "Naked" short selling is where the seller has not borrowed the securities, or ensured they can be borrowed before settlement. The proposal for a regulation enhances market transparency by requiring that all share orders on trading venues be marked as "short" if they involve a short sale, and significant net short positions in shares be disclosed and published. These transparency measures are accompanied by restrictions on certain short sellings in shares or sovereign debt and by buy-back and sanction procedures in case of settlement failure. Besides the intervention of the national authorities, ESMA will have powers to intervene notably in exceptional situations.

2. DIRECTIVES ADOPTED BY THE COUNCIL AND THE EUROPEAN PARLIAMENT BUT NOT YET IMPLEMENTED UNDER NATIONAL LAW

2.1. Directive 2009/110/EC of 16 September 2009 on the taking up, pursuit and prudential supervision of the business of electronic money institutions amending Directives 2005/60/EC and 2006/48/EC and repealing Directive 2000/46/EC

This directive was discussed in detail in the CSSF's Annual Report 2008. It will be transposed into national legislation through the adoption of draft law No. 6164.

2.2. Directive 2010/73/EU of 24 November 2010 amending Directives 2003/71/EC on the prospectus to be published when securities are offered to the public or admitted to trading (Prospectus Directive) and 2004/109/EC on the harmonisation of transparency requirements in relation to information about issuers whose securities are admitted to trading on a regulated market (Transparency Directive)

This directive was discussed in detail in the CSSF's Annual Report 2009. It must be transposed into national law by 1 July 2012. The relating draft law is being discussed within an *ad hoc* committee.

2.3. Directive 2010/78/EU of 24 November 2010 amending Directives 98/26/EC, 2002/87/EC, 2003/6/EC, 2003/41/EC, 2003/71/EC, 2004/39/EC, 2004/109/EC, 2005/60/EC, 2006/48/EC, 2006/49/EC and 2009/65/EC in respect of the powers of the European Supervisory Authority (European Banking Authority), the European Supervisory Authority (European Insurance and Occupational Pensions Authority) and the European Supervisory Authority (European Securities and Markets Authority) (Omnibus Directive)

This directive was discussed in detail in the CSSF's Annual Report 2009. It must be transposed into national law by 31 December 2011. The CSSF drew up a draft law to this end.

3. LUXEMBOURG LAWS AND REGULATIONS ADOPTED IN 2010

3.1. Grand-ducal regulation of 27 May 2010 relating to credit rating agencies and transposing Article 22 of Regulation (EC) No 1060/2009 of 16 September 2009 on credit rating agencies

The grand-ducal regulation designates the CSSF as the competent authority for the purposes of Regulation (EC) No 1060/2009 of 16 September 2009 on credit rating agencies. It also empowers the CSSF to levy fees on credit rating agencies under its supervision to cover the costs of its supervisory mission.

3.2. Law of 26 July 2010 amending the law of 9 May 2006 on market abuse

The main purpose of the law of 26 July 2010 is to complete the transposition of Article 12(2)(c) (supervisory and investigatory powers of the competent authority) and Article 14(1) (administrative sanctions) of Directive 2003/6/EC of 28 January 2003 on insider dealing and market manipulation (market abuse) and to adapt, as a consequence, Articles 29 and 33 of the law of 9 May 2006 on market abuse.

The CSSF now has the power to carry out on-site inspections with all the persons referred to in the law on market abuse. On-site inspections with persons not subject to the prudential supervision of the CSSF may be carried out while complying with the procedure laid down in the law of 26 July 2010. The CSSF's powers to carry out on-site inspections with persons subject to its prudential supervision remain unchanged.

Moreover, the CSSF is empowered to impose administrative sanctions against any natural or legal person, subject or not to its prudential supervision, that infringes the provisions of the law on market abuse. Consequently, insider breaches or market manipulation may be sanctioned on the administrative as well as penal level. The general principle of law that no person may be condemned twice for the same facts remains in force however. Thus, a pecuniary fine decided by a penal judge will be deducted from the pecuniary fine already imposed by the CSSF.

3.3. Fight against money laundering and terrorist financing

The laws and regulations adopted in this context in 2010, including notably the law of 27 October 2010, enhancing the anti-money laundering and counter-terrorist financing legal framework, are described in more detail in Chapter XIII "Fight against money laundering and terrorist financing".

3.4. Law of 17 December 2010 relating to undertakings for collective investment

This law transposes Directive 2009/65/EC of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities into Luxembourg law. It also amends certain Luxembourg legal provisions regarding UCIs and the law of 13 February 2007 relating to specialised investment funds.

In this respect, it is also worth mentioning CSSF Regulations N° 10-4 and N° 10-5 that transpose (1) Directive 2010/43/EU of 1 July 2010 implementing Directive 2009/65/EC as regards organisational requirements, conflicts of interest, conduct of business, risk management and content of the agreement between a depositary and a management company, and (2) Directive 2010/44/EU of 1 July 2010 implementing Directive 2009/65/EC as regards certain provisions concerning fund mergers, master-feeder structures and notification procedure.

These regulatory changes are described in more detail in Chapter III "Supervision of undertakings for collective investment".

3.5. CSSF Regulation N° 10-01 on the adoption of professional standards in the context of the publication of the law of 18 December 2009 concerning the audit profession

On 6 April 2010, the CSSF adopted professional standards covering the activities referred to in Article 1(29) (a) and (b) of the law of 18 December 2009 concerning the audit profession and adopted by the *Institut des Réviseurs d'Entreprises* (Luxembourg Institute of registered auditors) before the entry into force of the law.

The purpose of the regulation is to maintain continuity of the regulatory framework applicable to the activity of statutory audit of accounts in Luxembourg while waiting for the European Commission to adopt the international auditing standards of the International Federation of Accountants (IFAC) *via* an EU regulation.

3.6. CSSF Regulation N° 10-02 on the establishment of a consultative commission for the access to the audit profession

The consultative commission's task is, among others, to verify the theoretical and professional qualification of the candidates to the access to the audit profession in Luxembourg, as well as that of the providers that are nationals of other Member States wishing to provide these services by way of free provision of services.

3.7. CSSF Regulation N° 10-03 on the training record to be presented by candidate *réviseurs d'entreprises* when applying for registration for the examination of professional competence

This regulation defines the content of the training record in accordance with the provisions of Article 4(13) of the Grand-ducal regulation of 15 February 2010 establishing the qualification requirements of *réviseurs d'entreprises*.

3.8. Law of 10 December 2010 relating to the introduction of the international accounting standards for companies

The law introduces major changes to the accounting regime for accounts published by companies, mostly linked to the international accounting standards (IAS/IFRS), into the law of 19 December 2002 concerning the trade and companies register as well as the accounting and annual accounts of companies and into the law of 10 August 1915 on commercial companies.

The purpose of the law is in particular to:

- implement within the laws of 19 December 2002 and 10 August 1915 the options laid down in Regulation (EC) No 1606/2002 of 19 July 2002 on the application of international accounting standards (IAS Regulation) (Article 5), allowing EU Member States to permit or require non-publicly traded companies to publish their consolidated accounts in conformity with the IFRS as adopted by the EU, and to permit or require publicly and non-publicly traded companies to publish their individual accounts in conformity with the IFRS as adopted by the EU;
- transpose into the laws of 19 December 2002 and 10 August 1915 three accounting directives (2001/65/EC, 2003/51/EC and 2006/46/EC), consisting notably in modernising the fourth directive (78/660/EEC) on annual accounts and the seventh directive (83/349/EEC) on consolidated accounts, by enhancing convergence with IFRS. Major amendments are the following:
  - i) the possibility to adapt the presentation of the balance sheet and the profit and loss account to the presentation applied by IFRS;
  - ii) the possibility to value financial instruments and certain assets other than financial instruments at fair value;
  - iii) the requirement to consolidate subsidiaries with activities that are different from those performed by the other entities of the group;
  - iv) new provisions regarding the content of the management report and the report of the statutory auditor;
  - v) the introduction of provisions relating to corporate governance for companies whose securities are admitted to trading on the regulated market;

- transposing into the laws of 19 December 2002 and 10 August 1915 Directive 2009/49/EC amending Directives 78/660/EEC and 83/349/EEC by introducing certain simplification measures for small and medium-sized companies, in order to reduce the administrative burden resulting from certain disclosure requirements.

Only publicly traded companies, i.e. companies whose securities (shares or bonds) are admitted to trading on the regulated market of an EU Member State, are required to publish their consolidated accounts in conformity with the IAS/IFRS as adopted by the EU, in accordance with the mandatory regime of the IAS Regulation (Article 4). This requirement is directly applicable without Member States having to transpose it into national law.

The laws of 19 December 2002 and 10 August 1915 allow publicly traded and non-publicly traded companies to publish their annual accounts, and non-publicly traded companies to publish their consolidated accounts according to one of the following three accounting regimes:

- the current accounting regime, i.e. the LUX GAAP provisions based on the principle of prudence and historical cost;
- the mixed accounting regime, i.e. the application of LUX GAAP provisions combined with IAS/IFRS options, allowing in particular to use fair value valuation;
- the IAS/IFRS accounting regime, i.e. the application of IAS/IFRS as adopted by the EU, in which case the notes to the accounts must include, in addition, further information as required by the laws of 19 December 2002 and 10 August 1915.

Agents hired in 2010 and 2011 - Departments "Supervision of securities markets", "Supervision of pension funds, SICARs and securitisation undertakings" and "Public oversight of the audit profession"

Left to right: Nicolas BECKRICH, Aurore FONFREIDE, Hary SUTTOR, Dimitra AREND, François MOUSEL, Laurent NEYEN, Pierre OESTREICHER, Max RATHS

Absent: Raffaela FIORENTINO, Brice ROBRETEAU, Jérôme TOURSCHER

INTERNAL ORGANISATION OF THE CSSF

15

1. Functioning of the CSSF
2. Human resources
3. Information systems
4. Staff members
5. Committees

1. FUNCTIONING OF THE CSSF

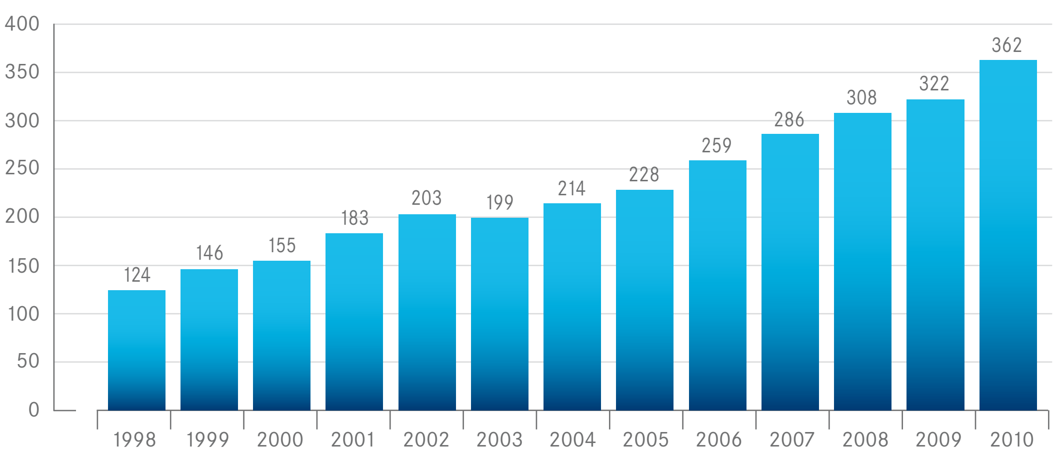
The CSSF's administrative and management organisation is described in detail in the sub-section "Corporate governance and functioning" of the CSSF website (www.cssf.lu, section "About the CSSF").

2. HUMAN RESOURCES

2.1. CSSF staff

As far as human resources are concerned, the year 2010 was marked by substantial recruitment of new staff members. Forty-four agents have been recruited as *employé de l'Etat* in 2010. Following the resignation of four agents over that period, total employment reached 362 units as at 31 December 2010, representing a 12.42% increase compared to 2009. This is the equivalent of 327.65 full-time jobs, i.e. a 12.63% increase compared to 2009.

Movements in staff numbers (at the end of the year)



The average age of CSSF staff members was 37.61 years as at 31 December 2010. Women make up 46.6% of total staff and men 53.4%.

2.2. Staff training

CSSF staff followed 262 training seminars in 2010.

These seminars concerned, on the one hand, the *stage* (training period) and the adaptation to the workplace of the new staff members, i.e. the programme of internal training aiming to facilitate integration of these new hires into the CSSF's structure and to make them acquainted with the CSSF's activities (19.2%) and, on the other hand, lifelong learning for CSSF agents (80.8%). 58.7% of continuous education focused on economics and finance, 18.4% on IT/office automation, 6.9% on law and 2.3% on management. The remaining 13.7% focused on subjects such as personal development, security, accounting, languages and human resources management.

1,126 participations in training sessions were recorded in 2010. The CSSF staff counted a total of 1,245 training days, representing an average of 3.39 days of training per agent.

3. INFORMATION SYSTEMS

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

3.1. Reporting COREP and FINREP

The Luxembourg versions of FINREP and COREP introduced in 2007 and based on FINREP 1.2 and COREP 1.2.4 at European level, remained in force in 2010.

On 6 January 2010, version 1.3.0 of COREP implementing CRD II was released at European level. As the impact of CRD II on the Luxembourg financial centre is very limited and the number of banks concerned very small, the CSSF decided not to amend the general reporting (tables B1.4 and B6.4 remaining unchanged), but to require additional information directly from the banks concerned.

A new version 1.4.0 of COREP, which will implement CRD III is expected to be released at EU level in the first half of 2011. In order to limit the impact of this version which will affect all the banks and be applicable as from 2012, in principle, the CSSF will adapt the current reporting by adding rows and columns and by keeping the L2 layouts of tables B1.4 and B6.4.

Works are in progress to implement the new versions COREP 2012 and FINREP 2012 (V2.0.0) which will notably transpose CRD IV. These versions will be more integrated, have a new architecture and have XBRL formulas to perform multiple data checks. Their release will be such as to allow the first transmissions to take place for 31 December 2012. The current taxonomies project is available at www.eurofiling.info in the sections DRAFT COREP 2012 and DRAFT FINREP 2012. The versions will introduce many new layouts of the CSSF tables, which will require adaptation efforts from the banks and investment firms.

3.2. Development of the CSSF's internal IT systems

The basis tool to replace the current document management system, which reaches its limits in terms of volume and performance, has been chosen and its implementation is taking place.

Initiated in 2010, the use of virtualisation techniques, for applications as well as for storage, is also being deployed. The architecture should be based as far as possible on homogeneous farming of machines and storage, which allows improving the energy bill while providing an optimised set of calculation resources available on demand by the applications. In the medium term, certain applications should be adapted for a private cloud managed by the CSSF.

The implementation of the virtualisation in several remote sites is inevitably accompanied by a need for a high bandwidth of communication lines. The notification processing platform under the UCITS IV Directive also required a substantial increase of bandwidth towards Internet. These needs resulted in 2010 in a substantial upgrade of communication lines, which should continue in 2011.

In the context of on-site inspections within the scope of the public oversight of the audit profession or the prudential supervision of financial institutions, the CSSF implemented a controlled mobility allowing the CSSF agents concerned to have a remote access to a specific set of resources of internal IT.

The upgrade and replacement of office management equipment is planned to take place in 2011 and 2012, and will require important training efforts.

4. STAFF MEMBERS

Executive Board

Director General	Jean Guill
Directors	Andrée Billon, Simone Delcourt, Claude Simon

Internal audit

Marie-Anne Voltaire

Executive Board Secretariat

Head of department	Danielle Mander
	Iwona Mastalska, Francis Fridrici
Executive secretaries	Joëlle Deloos, Karin Frantz, Carole Hessler, Marcelle Michels, Monique Reisdorffer

General Secretariat

Head of department	Danièle Berna-Ost
	Carmela Anobile, Carine Conté, Patrick Hommel, Danielle Meyrer, Danijela Stojkovic

Legal Department

Heads of department	Jean-Marc Goy, Jean-François Hein, Marc Limpach, Geneviève Pescatore
	Vanessa Gabriel, Yasmin Gabriel, Simone Gloesener, François Goergen, Nadine Holtzmer, Nora Humbert, Stéphanie Jamotte, Benoît Juncker, Michèle Muller, Elisabeth Omes, Anne Wagener

General Supervision

Head of department	Romain Strock
Deputy heads of department	Danièle Goedert, Nadia Manzari, Joëlle Martiny, Patrick Wagner

Division 1 - International matters

Head of division	Joëlle Martiny
	Ngoc Dinh Luu, Sophie Schiltz, Vincent Thurmes, Karin Weirich

Division 2 - Accounting, reporting and audit

Head of division	Danièle Goedert
	Annick Bové, Ana Bela Ferreira, Marguy Mehling, Christina Pinto, Diane Seil, Pierre van de Berg, Martine Wagner

Division 3 - Governance rules, electronic payments and crisis management

Head of division	Nadia Manzari
	Natasha Deloge, Gilles Jank, Charles Krier, Nicole Lahire, Sylvie Nicolay-Hoffmann

Division 4 - On-site inspections

Head of division	Patrick Wagner
	Valérie Alezine, Françoise Bergmans, Magali De Dijcker, Joan De Ron, Sonja Kinn, Guido Kruse, Carole Philippe, Christian Schaack, Nicolas Van Laar
Secretary	Micheline de Oliveira

Department Supervision of undertakings for collective investment

Head of department	Irmine Greischer
Deputy heads of department	Jean-Paul Heger, Alain Hoscheid, André Schroeder, Claude Steinbach

International regulation regarding UCIs and legal issues

Rudi Dickhoff, François Hentgen, Laurent van Burik

Coordination and development of IT systems

Nico Barthels

Management and operation of data bases

Head of division	Jolanda Bos
	Christiane Cazzaro, Nicole Grosbusch, Claude Krier, Martin Mannes, Danielle Neumann, Evelyne Pierrard-Holzem, Marc Schwalen, Claudine Thielen, Nadja Trausch, Suzanne Wagner

Desk "Visa and notification"

Head of division	Danièle Christophory
	Adrienne André-Zimmer, Patrick Bariviera, Giuseppe Daloia

Specific economic aspects

Jacqueline Arend, Angela De Cillia, Fabio Ontano

Supervision of UCIs activity

Head of division	Francis Gasché
	Julien Gageonnet, Nicole Gengler, Sophie Leboulanger, Géraldine Olivera, Diane Reuter, Sabine Schiavo, Rudy Stranen, Alain Strock, Claude Wagner

Instruction of UCIs - group 1

Head of division	Charles Thilges
	Yolanda Alonso, Nathalie de Brabandere, Jérôme Mousny, Gilles Oth, Thierry Quaring, Nathalie Reisdorff, Marc Runau, Christel Tana, Daniel Wadlé

Supervision of UCIs - group 1

Head of division	Francis Lippert
	Leonardo Brachtenbach, Marie-Rose Colombo, Anne-Christine Depienne, Jean-Claude Fraiture, Joël Goffinet, Dominique Herr, Martine Kerger

Instruction of UCIs - group 2

Head of division	Ralph Gillen
	Isabelle Dosbourg, Yves Fischbach, Paul Hansen, Urbain Hever, Tom Muller, Carine Peller, Pierre Reding, Yannick Rouby, Roberta Tumiotto, Florence Winandy

Supervision of UCIs - group 2

Head of division	Daniel Schmitz
	Géraldine Appenzeller, Patricia Jost, David Phillips, Marc Racké, Marc Siebenaler, Michèle Wilhelm

Instruction of UCIs - group 3

Head of division	Michel Friob
	Claude Detampel, Anne Diederich, Christophe Faé, Joëlle Hertges, Robert Köller, Laurent Reuter, Pascale Schmit, Isah Skrijelj

Supervision of UCIs - group 3

Head of division	Guy Morlak
	Nathalie Cubric, Marc Decker, Damien Houel, Jean-Marc Lehnert

Risk management and macroprudential supervision of UCIs

Alain Bressaglia, François Petit, Mireille Reisen, Tom Ungeheuer

Enquiries and review of pre-contentious files

Christiane Streef, Serge Eicher, Laurent Mayer, Sébastien Traversa

Secretaries — Sandy Bettinelli, Sandra Ghirelli, Simone Kuehler, Sandra Preis

Department Supervision of management companies

Head of department	Sonny Bisdorff-Letsch
Deputy head of department	Pascal Berchem
	Anne Conrath, Pascale Felten-Enders, Anica Giel-Markovinovic, Anne-Marie Hoffeld, Roberto Montebrusco, Eric Tanson
Secretary	Sandra Preis

Department Supervision of securities markets

Head of department	Françoise Kauthen
Deputy head of department	Annick Zimmer

Division 1 – Approval of prospectuses

Head of division	Jean-Christian Meyer
Group 1	Frédéric Dehalu, Patrick Fricke, Yves Hansen, William Lebec, Paul Lepage, Jim Neven, Jerry Oswald
Group 2	Carine Merkes, Joëlle Paulus, David Schmitz

Division 2 – Approval of prospectuses

Head of division	Gilles Hauben
Group 1	Olivier Ferry, Daniel Jeitz, Julien May, Marc Reuter, Cyrille Uwukuli, Olivier Weins
Group 2	Michèle Debouché, Estelle Gütlein-Bottemer

Division 3 – Transparency

Head of division	Maureen Wiwinius
Enforcement	Jérôme Tourscher
Group 1	David Deltgen, Nicolas Hinterscheid, Max Raths, Brice Robreteau, Manuel Roda, Stéphanie Weber
Group 2	Giang Dang, Christine Jung

Division 4 - Supervision of markets and market operators

Head of division	Maggy Wampach
	Stéphanie Bonifas, Eric Fritz, Mylène Hengen, Hary Suttor

Division 5 - Enquiries and legal issues

Head of division	Mendaly Ries
	Laurent Charnaut, Anne Lutgen

Secretaries	Sarah Morosi, Marie-Josée Pulcini

Department Personnel, administration and finance

Head of department	Alain Oestreicher
Deputy head of department	Georges Bechtold

Division 1 – Human resources

Head of division	Georges Bechtold
	Alain Kirsch, Vic Marbach

Division 2 – Financial management

Head of division	Jean-Paul Weber
	Marie-Louise Baritussio, Tom Ewen

Division 3 – Administration and supplies

Head of division	Marc Feiereisen
	Paul Clement, Sergio De Almeida, Raul Domingues, Patrick Klein, Ricardo Oliveira, Marco Valente
Secretary	Milena Calzettoni
Switchboard	Nicole Thinnes

Department Information systems and supervision of support PFS

Head of department	David Hagen
Strategic advisor	Jean-Luc Franck
Person in charge of databases	Sandra Wagner

Division 1 - Information systems

Head of division	Constant Backes
Production	Yves Bartringer, Cédric Brandenbourger, Frank Brickler, Jean-François Burnotte, Jean-Jacques Duhr, Nadine Eschette, Guy Frantzen, Christelle Hutmacher, Steve Kettmann, Edouard Lauer, Carine Schiltz, Thierry Stoffel
Projects	Marco Fardellini
Development	Marc Kohl
	Denise Arnaud, Romain De Bortoli, Guy Wagener
Databases	Sandra Wagner
Security	Constant Backes, Claude Bernard
EDM	Joao Almeida, Nicolas Lefeuvre, Luc Prommenschenkel

Division 2 - Coordination and user relations

Head of division	Emile Bartolé
	Pascale Damschen

Division 3 - Supervision of information systems

Head of division	Paul Herling
	Cécile Gellenoncourt

Division 4 - Supervision of support PFS

Head of division	Pascal Ducarn
	Marc Bordet, Laurent Dohn, Isabelle Gil, Josiane Laux, Martine Simon
Administration	Elisabeth Demuth Paul Angel

Department Public oversight of the audit profession

Head of department	Frédéric Tabak
	Dimitra Arend, Isabelle Michalak, François Mousel, Agathe Pignon, Hugues Wangen, Anne Wirard
Secretary	Claude Fridrici

Department Supervision of the other professionals of the financial sector

Head of department	Carlo Felicetti
Deputy head of department	Denise Losch
	Lucinda Azevedo Pereira, Gérard Brimeyer, Isabelle Lahr, Sylvie Mamer, Claudia Miotto, Christian Schroeder
Secretary	Emilie Lauterbour

Department Supervision of banks

Head of department	Frank Bisdorff
Deputy heads of department	Jean-Louis Beckers, Ed. Englaro, Nico Gaspard, Claude Moes, Davy Reinard, Jean-Paul Steffen, Claude Wampach

Division 1 - Supervision of credit institutions 1

Head of division	Ed. Englaro
	Blandine Caeiro Antunes, Anouk Dondelinger, Anne-Marie Fiorello, Françoise Jaminet, Jean Ley

Division 2 - Supervision of credit institutions 2

Head of division	Jean-Paul Steffen
	Felipe Araya, Alain Clemens, Jean-Louis Duarte, Marina Sarmento, Michèle Trierweiler

Division 3 - Supervision of credit institutions 3

Head of division	Nico Gaspard
	Marco Bausch, Françoise Daleiden, Claude Ley, Paul-Marie Majerus, Jacques Streweler, Andy Züst

Division 4 - Supervision of credit institutions 4

Head of division	Jean-Louis Beckers
	Monica Ceccarelli, Stéphanie Nothum, Yves Simon, Claudine Tock, Thomas Weber

Division 5 - Supervision of credit institutions 5

Head of division	Claude Moes
	David Aranda, Carlos Pereira Azevedo, Gilles Karels, Jean Mersch, Alain Weis

Division 6 - Risk management functions

Heads of division	Davy Reinard, Claude Wampach
	Didier Bergamo, Bettina Eisele, Laurent Goergen, Nele Mayer, Pierrot Rasqué, Joé Schumacher

Statistics and IT issues	Claude Reiser
Legal issues	Gabrielle Fatone
Surveys and general issues	Marc Wilhelmus
Secretaries	Michèle Delagardelle, Steve Humbert, Claudine Wanderscheid

Department Supervision of investment firms

Head of department	Marc Weitzel
Deputy heads of department	Luc Pletschette, Steve Polfer

Division 1

Head of division	Luc Pletschette
	Annick Hucker, Michel Kohn, Patrice Mack, Anne Marson, Carole Ney, Christiane Trausch

Division 2

Head of division	Steve Polfer
	Marc Birchen, Céline Gamot, Andrea Haris, Filipa Mendes, Mariette Thilges

Secretary Sally Habscheid

Department Supervision of pension funds, SICARs and securitisation undertakings

Head of department	Christiane Campill
Deputy head of department	Marc Pauly

Authorisation and supervision of pension funds and securitisation undertakings

Arthur Backes, Tom Becker, Cliff Buchholtz, Anouk Dumont, Marc Pauly, Nathalie Wald

Authorisation and supervision of SICARs

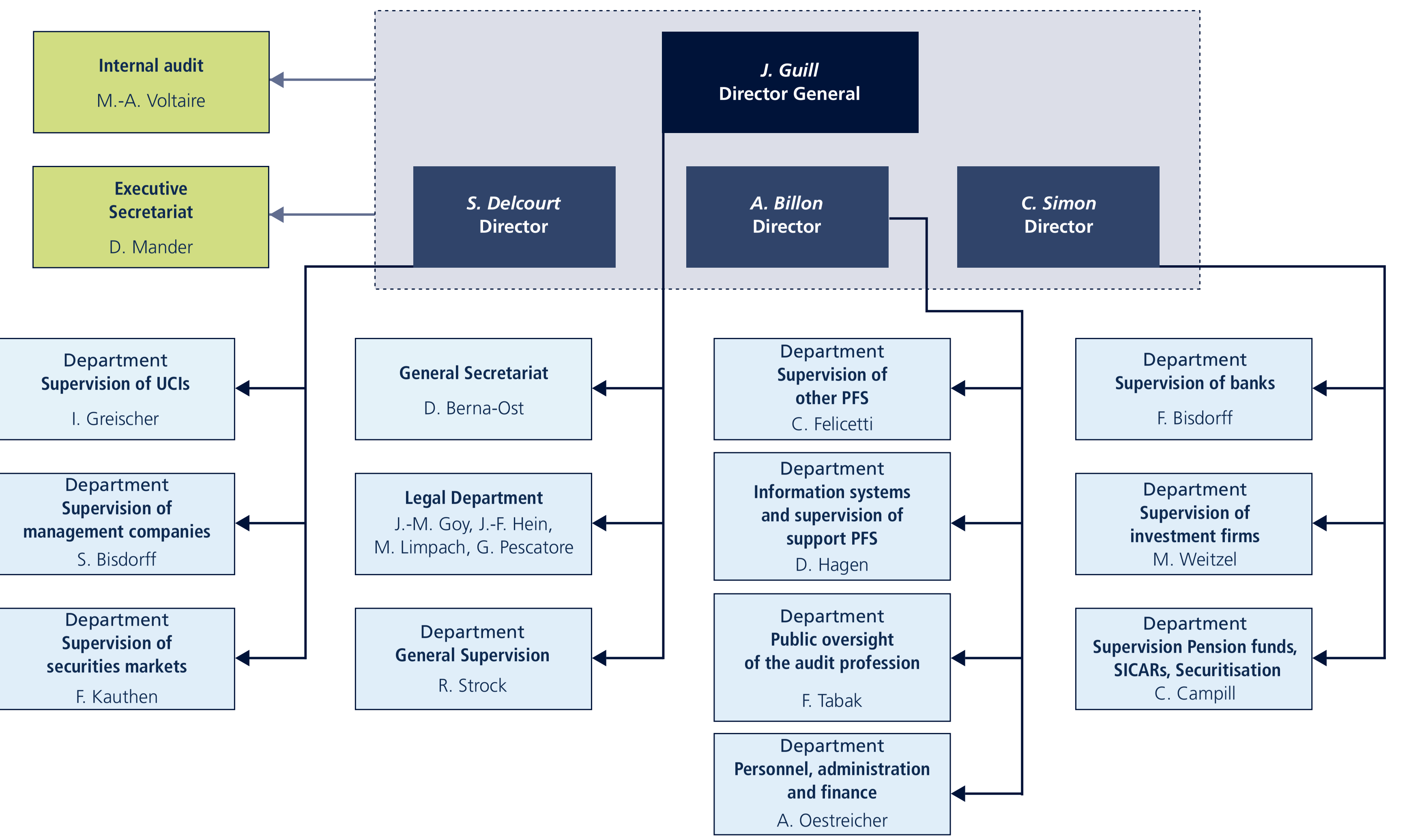
Nicolas Beckrich, Daniel Ciccarelli, Raffaela Fiorentino, Aurore Fonfreide, Carole Lis, Laurent Neyen, Pierre Oestreicher, Catherine Phillips, Michael Rademacher, Isabelle Maryline Schmit, Paul Scholtes, René Schott, Alex Weber, Martine Weber

Secretary Carla Dos Santos

Financial controller

KPMG

Organisation chart



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5. COMMITTEES

5.1. Consultative committees

5.1.1. Consultative committee for prudential regulation

The Government may seek the advice of the Committee, constituted by the law of 23 December 1998 establishing a financial sector supervisory commission (*Commission de surveillance du secteur financier*), on any draft law or Grand-ducal regulation in the field of the financial sector falling within the competence of the CSSF. Its advice must be sought for any draft CSSF regulation. Members of the Consultative committee are appointed by the Minister of Finance.

Committee composition:

Executive board of the CSSF: Jean Guill (Chairman), Andrée Billon, Simone Delcourt, Claude Simon

Members: Alain Feis, Rafik Fischer, Georges Heinrich, Michel Maquil, Jean-Jacques Rommes, Carlo Thill, Camille Thommes

Secretary: Danielle Mander

5.1.2. Consultative committee for the audit profession

The Government may seek the advice of the Committee, established by the law of 18 December 2009 concerning the audit profession, on any draft law or Grand-ducal regulation related to statutory audits and the audit profession subject to the oversight of the CSSF. The members of the Consultative committee for the audit profession may also seek its advice concerning the setting-up or application of the regulation of public oversight of the audit profession overall or for specific issues.

Committee composition:

Executive board of the CSSF: Jean Guill (Chairman), Andrée Billon, Simone Delcourt, Claude Simon

Members: Serge de Cillia, Sarah Khabirpour, Pierre Krier, Philippe Meyer, Victor Rod, Daniel Ruppert, Anne-Sophie Theissen, Camille Thommes, Eric van de Kerkhove

Secretary: Danielle Mander

5.2. Committees of experts

The expert committees assist the CSSF in analysing the development of the different areas of the financial sector, give their advice on any issue relating to their activities and contribute to developing and interpreting regulatory texts relating to areas covered by the respective committees. In addition to the permanent committees listed below, *ad hoc* committees are formed to examine specific subjects.

The permanent expert committees are the following:

- Anti-Money Laundering Committee;
- Banks and Investment Firms Committee;
- Bank and Investment Firm Accounting Committee;
- Pension Funds Committee;
- Laws and Regulations Committee;
- Securities Markets Committee;
- Undertakings for Collective Investment Committee;
- Professionals of the Financial Sector Committee;
- SICAR Committee;
- Audit Technical Committee;
- Securitisation Committee.

Agents hired in 2010 and 2011 - Legal Department, General Secretariat, Department "Supervision of banks"

Left to right: David ARANDA, Danielle MEYRER, Yasmin GABRIEL, Bettina EISELE, Gabrielle FATONE, Anne-Marie FIORELLO, Nele MAYER, Felipe ARAYA, Elisabeth OMES, Nora HUMBERT

Absent: Andy ZÜST

1. ANNUAL ACCOUNTS OF THE CSSF - 2010

BALANCE SHEET AS AT 31 DECEMBER 2010

Assets	*EUR*	*EUR*
Fixed assets		18,164,560
- Tangible assets	18,161,560	
- Financial assets	3,000	
Current assets		69,563,794
- Trade debtors	1,362,758	
- Other debtors	351,212	
- Cash at bank	67,849,824	
Payments and accrued income		1,725,294
Total assets		**89,453,648**

Liabilities		
Capital and reserves		22,928,386
- Profit brought forward	22,510,631	
- Profit for the financial year	417,755	
Provisions		350,000
Creditors		65,579,282
- Amounts owed to credit institutions	61,565,774	
- Trade creditors	2,175,893	
- Other creditors	1,837,615	
Accruals and deferred income		595,980
Total liabilities		**89,453,648**

PROFIT AND LOSS ACCOUNT AS AT 31 DECEMBER 2010

Charges	*EUR*
Other external charges	6,366,546
Staff costs	29,773,279
Value adjustments in respect of tangible fixed assets	3,318,119
Interest payable and similar charges	1,652,906
Extraordinary charges	6,864,997
Profit for the financial year	417,755
Total charges	**48,393,602**

Income	
Fees	40,535,025
Other operating income	926,843
Interest receivable and similar income	270,776
Extraordinary income	6,660,958
Total income	**48,393,602**

2. LIST OF ABBREVIATIONS

ABBL	Association des Banques et Banquiers, Luxembourg - The Luxembourg Bankers' Association
AGDL	Association pour la garantie des dépôts, Luxembourg - Deposit Guarantee Association Luxembourg
AIFM	Alternative Investment Fund Managers
AML/CFT	Anti-Money Laundering and Counter-Terrorist Financing
BCL	Banque centrale du Luxembourg - Luxembourg Central Bank
CEBS	Committee of European Banking Supervisors
CEIOPS	Committee of European Insurance and Occupational Pensions Supervisors
CESR	Committee of European Securities Regulators
COREP	Common Reporting
CRD	Capital Requirements Directives
CSSF	Commission de Surveillance du Secteur Financier
EC	European Community
ECB	European Central Bank
EEA	European Economic Area
EFRAG	European Financial Reporting Advisory Group
EGAOB	European Group of Auditors' Oversight Bodies
ESFS	European System of Financial Supervisors
ESMA	European Securities and Markets Authority
ESRB	European Systemic Risk Board
EU	European Union
EUR	Euro
FATF	Financial Action Task Force on money laundering
FCP	Fonds commun de placement - common fund
FINREP	Financial Reporting
GDP	Gross Domestic Product
IAS	International Accounting Standards
IASB	International Accounting Standards Board
ICAAP	Internal Capital Adequacy Assessment Process
IFAC	International Federation of Accountants
IFRS	International Financial Reporting Standards
IMF	International Monetary Fund
IML	Institut Monétaire Luxembourgeois - Luxembourg Monetary Institute (1983-1998)
IORP	Institution for occupational retirement provision
IOSCO	International Organization of Securities Commissions
IRE	Institut des Réviseurs d'Entreprises - Luxembourg Institute of registered auditors
ISA	International Standards on Audit
ISQC	International Standard on Quality Control
MiFID	Markets in Financial Instruments Directive
MTF	Multilateral Trading Facility
NAV	Net asset value
OAM	Officially Appointed Mechanism
OECD	Organisation for Economic Cooperation and Development
PFS	Professional of the financial sector
PIE	Public Interest Entity

SBL	Société de la Bourse de Luxembourg S.A.
SICAF	Société d'investissement à capital fixe - Investment company with fixed capital
SICAR	Société d'investissement en capital à risque - Investment company in risk capital
SICAV	Société d'investissement à capital variable - Investment company with variable capital
SIF	Specialised investment fund
SRP	Supervisory Review Process
TREM	Transaction Reporting Exchange Mechanism
UCI	Undertaking for collective investment
UCITS	Undertaking for collective investment in transferable securities
XBRL	eXtensible Business Reporting Language

COMMISSION DE SURVEILLANCE
DU SECTEUR FINANCIER

110, route d'Arlon L-2991 LUXEMBOURG