

CSSF Circular 12/546

Substance Requirements Applicable to UCITS Management Companies/Self-Managed UCITS Investment Companies and UCI Promotership

On 26 October 2012, the Luxembourg supervisory authority of the financial sector (CSSF) released Circular 12/546 relating to the authorisation and organisation of Luxembourg management companies subject to Chapter 15 of the law of 17 December 2010 relating to undertakings for collective investment (2010 Law) and self-managed investment companies which have not designated a management company within the meaning of Article 27 of the 2010 Law (SIAGs).

In a separate Press Release 12/45 dated 31 October 2012, the CSSF further specified that the concept of promoter is no longer necessary for UCITS having taken the form of a SIAG as well as UCITS and other UCIs subject to the 2010 Law that are managed by a UCITS management company complying with all the requirements laid down in Circular 12/546.

This client briefing provides an overview of: (i) the main changes introduced by Circular 12/546 to the substance and organisational requirements applying to UCITS management companies and SIAGs, including the abolishment of the promoter status, and (ii) the transitional period running until 30 June 2013.

Introduction

The purpose of Circular 12/546 is to clarify the authorisation, substance and organisational requirements that apply to management companies subject to Chapter 15 of the 2010 Law (UCITS management companies) and SIAGs in order to meet the conditions laid down by the 2010 Law and CSSF Regulation 10-04¹.

This circular replaces, with effect as of 26 October 2012, previous CSSF Circulars 03/108² and 05/185³ relating to UCITS management companies and SIAGs, which have become outdated following the implementation of the so-called UCITS IV Directive⁴ into Luxembourg law. It also integrates CSSF Circular 11/508⁵ concerning the organisational requirements, conflicts of interests,

conduct of business rules and risk management of UCITS management companies and SIAGs, so that all the rules and guidelines for the application filing and daily organisation and operation of UCITS management companies and SIAGs are now contained in a single circular.

In addition, the purpose of Circular 12/546 is to provide clarifications on certain conditions for authorisation of UCITS management companies and SIAGs, more particularly as regards the shareholders, management bodies and conducting officers, as well as in the area of the use of own funds, the arrangements concerning the central administration and the delegation rules. Many of these clarifications codify the existing CSSF's regulatory practice⁶ and may already be complied with by existing

Key issues

- Introduction
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UCITS management companies/SIAGs. However, Circular 12/546 also imposes some new and stricter organisational requirements for UCITS management companies/SIAGs, whilst maintaining the principle of proportionality⁷ and possible exceptions to the application of certain rules.

For the sake of completeness, it has to be noted that the scope of Circular 12/546 extends to branches and representative offices that UCITS

management companies may have established abroad.

Last but not least, Circular 12/546 also clarifies certain provisions of the MiFID Directive⁸ and additional requirements applicable to UCITS management companies providing the activities of discretionary portfolio management. The specific requirements applying to these management companies are not covered by this briefing.

1. Main Changes

This Section considers the main new substance and organisational requirements introduced by Circular 12/546, as complemented by CSSF Press Release 12/45.

1.1 Promoter

[New] Further to the entry into force of Circular 12/546, the CSSF published Press Release 12/45 on the concept of promoter.

This press release confirms that all Luxembourg UCITS and other UCIs subject to the 2010 Law, regardless their legal form (i.e. SICAV, SICAF or FCP), which are managed/have designated a UCITS management company subject to Chapter 15 of the 2010 Law, as well as UCITS taken the form of a SIAG (i.e. SICAV or SICAF), are no longer required to have a "promoter", provided that the relevant UCITS management company/SIAG complies with all the requirements set forth by Circular 12/546 (see Section 2.2 for further details).

1.2 Shareholding

1.2.1 Conflicts of Interests

[New] In order to avoid potential conflicts of interests at the level of any UCITS management company,

Circular 12/546 expressly requires that, in the case where the depositary bank of one of the investment funds managed by the management company has a direct or indirect qualifying holding⁹ in that management company, the management company must identify the conflicts of interests that could result from such holding and must strive to avoid them in accordance with the procedures laid down in its conflict of interest policy.

1.2.2 Sponsorship Letter

[New] Notwithstanding the abolishment under certain conditions of the long-standing concept of promoter (see Sections 1.1 and 2.2), Circular 12/546 provides that the CSSF may request a "sponsorship letter" whereby the issuer commits towards the CSSF that the UCITS management company/SIAG complies/will comply with applicable prudential requirements, including those relating to the own funds in the case of a management company.

Such a letter may be required by the CSSF:

- at the time of authorisation of the UCITS management company/SIAG;
- at the time of a change of the shareholding of the UCITS management company/SIAG; and
- where during the lifetime of the UCITS management company/SIAG, the financial soundness of the existing shareholder(s) is no longer certain.

It has to be noted that Circular 12/546 does not detail the content and scope of the sponsorship letter, nor does it specify the circumstances in which such a letter has to be issued and the

relevant entity who should issue the letter¹⁰.

1.3 Own Funds¹¹

1.3.1 Investment of Own Funds

According to the 2010 Law¹², the own funds of a UCITS management company must be maintained at its continuous disposal and invested in its own interest.

In view of the foregoing, Circular 12/546 explicitly requires that the legally required minimum own funds¹³ are put at the permanent disposal of the UCITS management company in order to guarantee the continuity and regularity of its activities and services. In this respect, the CSSF continues to consider that the own funds may not be used for investment in or financing a loan to any of the shareholder of the UCITS management company.

[New] However, Circular 12/546 now clarifies that it is permissible for a UCITS management company to invest its own funds in liquid assets or assets easily convertible into liquid short term assets, provided that they do not contain any speculative positions.

1.3.2 Holding Shares in Other Companies

[New] Circular 12/546 includes an express obligation to notify the CSSF without delay of any holding by a UCITS management company in another company. In this respect, the CSSF requires that such holding be financed exclusively by the surplus of own funds that the UCITS management company may have above the minimum legally required. Moreover, the activities of the subsidiary must remain within the line of activities that can be exercised by the relevant UCITS management company.

1.4 Board of Directors¹⁴

1.4.1 Composition

In line with the CSSF's regulatory practice, Circular 12/546 explicitly specifies that the board of directors or any other management body of a UCITS management company/SIAG must always be composed of at least three members.

1.4.2 Incompatibilities

[New] Circular 12/546 requires that the shareholder(s) of any UCITS management company/SIAG take into account, when composing the board of directors of the relevant entity, the solid governance arrangements that the UCITS management company/SIAG must have.

This implies, for example, the following incompatibilities as regards the board members of a UCITS management company/SIAG:

- in the case where a bank is the shareholder of a UCITS management company/SIAG and that bank assumes the function of depository bank of that SIAG, respectively one or more investment funds managed by that management company, it must be ensured that the board of directors of that management company/SIAG is not composed in majority of representatives of the custodian's "depository bank" business line;
- in the case where a SICAV has appointed a UCITS management company, it is recommended that the board of directors of both the SICAV and the management company is not predominantly composed of the same persons;
- the compliance officer and internal auditor of a UCITS management company cannot be

member of the board of directors of that management company; and

- the person responsible for the risk management function cannot be member of the board of directors of the UCITS management company/SIAG.

1.4.3 Experience

Circular 12/546 provides that the members of the board of directors, or their legal representative in the case where a legal person has been appointed as director, have adequate professional experience gained through having already performed similar activities to a high level of responsibility and autonomy. This clarification reflects the CSSF's existing regulatory practice according to which the directors of a UCITS management company/SIAG, in order to be approved, must be "sufficiently" experienced in relation to the type of UCITS managed (i.e. they have to demonstrate experience as regards the type of assets under management as well as Luxembourg management experience).

1.4.4 Working Time/ Multiple Mandates

Circular 12/546 provides expressly that each member of the board of directors of any UCITS management company/SIAG must dedicate the required time and attention to his tasks. Therefore, he must ensure limiting the number of other professional engagements (especially the mandates in other companies) to the extent as necessary for the performance of his tasks.

Again, it has to be noted that, in order to approve the appointment of the directors of any UCITS management company/SIAG, the CSSF has already required in the past to be

provided with the list of his other mandates in other companies.

1.5 Conducting Officers¹⁵

According to the 2010 Law, any UCITS management company/SIAG must appoint at least two persons in charge of the effective conduct of its business, these persons being generally known as "conducting officers" (*dirigeants*).

1.5.1 Experience

As for the members of the board of directors, Circular 12/546 codifies the CSSF's regulatory practice requiring the two conducting officers to have adequate professional experience gained through having already performed similar activities to a high level of responsibility and autonomy¹⁶.

1.5.2 Workplace/ Domicile

Under CSSF Circulars 03/108 and 05/185, the CSSF has required that at least one out of the two conducting officers be working in Luxembourg, with the possibility however to waive this requirement in exceptional circumstances.

[New] Circular 12/546 now requires that the two conducting officers must, in principle, permanently be present in Luxembourg for the accomplishment of their tasks, but it further sets out a clarification that this does not prevent them from having their domicile abroad as long as they are able to come to Luxembourg every day. By derogation, the CSSF may, however, on the basis of a duly supported request made in advance and having regard to the nature, scale and complexity of the activities of the UCITS management company/SIAG, allow that only one conducting officer is permanently present in Luxembourg.

Based on this new requirement, it cannot be excluded that the CSSF will require existing UCITS management companies/SIAGs to re-submit a specific derogation request from the principle to have the two conducting officers in Luxembourg, if one of these conducting officers is not on site in accordance with previous CSSF Circulars 03/108 and 05/185. Indeed, it is likely that the CSSF will adopt a more restrictive approach than in the past to grant such a derogation.

1.5.3 Areas of Responsibility/ Incompatibilities

Circular 12/546 continues to require that each conducting officer is assigned different areas of responsibility with regard the functions included in the collective portfolio management, including risk management.

In this context, Circular 12/546 specifies that this split of tasks must be organised so as to avoid conflicts of interests and provides for some incompatibilities as regards the conducting officers. Thus, for example:

- the performance and/or control of the risk management function and the investment management function shall not be carried out by the same conducting officer; and
- the conducting officers cannot be employees of the depositary bank of the SIAG or of the UCITS managed by the management company.

Circular 12/546 reiterates that the conducting officers may manage the business of several UCITS management companies/SIAGs, on the condition that the CSSF has proof that the exercise of multiple functions does not and is not likely to prevent

the relevant persons from discharging at all time any one particular function soundly, honestly and professionally.

[New] To this end, it has to be noted that the CSSF does not expect the conducting officers to conduct the UCITS management company's/SIAG's business alone. Indeed, Circular 12/546 includes a new provision explicitly requiring the conducting officers to be supported in their daily work by enough qualified staff working in Luxembourg. In this respect, the CSSF also requires to be provided on a quarterly basis with staff table as detailed in appendix 3 of Circular 12/546 (see Section 1.6.2 for further details on the human resources, including staff).

[New] In line with the preceding provision, Circular 12/546 also allows the conducting officers, on the basis of a service agreement, to use the expertise and/or existing technical means at the level of other organisational/operational units in existence within the group to which the UCITS management company/SIAG belongs and/or at the level of a third party having the capacities, quality and authorisations required to provide the requested support in a reliable and professional way.

1.5.4 Management Committee

[New] Circular 12/546 introduces the obligation for the conducting officers to form a management committee within which they are required to work together in close partnership to take all actions falling within the scope of their duties.

The circular provides for the following non-exhaustive list of responsibilities to be performed by the management committee under the ultimate responsibility of the board of directors

(most of these responsibilities being reminders of provisions already laid down in CSSF Regulation 10-04)¹⁷:

- implementing strategies and guiding principles regarding the central administration and internal governance through specific written internal policies and procedures;
- implementing adequate internal control mechanisms (i.e. permanent risk management function as well as permanent compliance and permanent internal audit functions in the case of a management company);
- ensuring that the UCITS management company/SIAG has the technical infrastructure and human resources necessary for performing its activity;
- implementing the general investment policy of the SIAG or, as the case may be, each UCITS that the management company manages;
- supervising the adoption of investment strategies for the SIAG or, as the case may be, each UCITS that the management company manages;
- adopting, and consequently filing for regular review the risk management policy as well as the provisions, procedures and implementing techniques of this policy, and in particular the risk limitation system for the SIAG or, as the case may be, each UCITS managed by the management company;
- implementing and following-up of the marketing policy and the distribution network of the SIAG or, as the case may be, each UCITS/UCIs managed by the management company; and

- regularly informing the board of directors, in an exhaustive manner and in writing, on the activities of the SIAG or, as the case may be, the management company and the UCITS/UCIs it manages.

In order to fulfil its responsibilities, the management committee is required to work in accordance with a method of operation that must be adapted to the activities of the relevant management company/SIAG. Thus, for example, the conducting officers shall be in regular contact with each other and hold periodic meetings. These meetings shall be formalised in written minutes, available at the offices of the UCITS management company/SIAG in Luxembourg, and the agenda of these meetings will include, amongst other things, a discussion on the management information (see Section 1.7.1).

In practice, the main impact of the management committee requirement for existing UCITS management companies/SIAGs will be the obligation to effectively create and organise the functioning of the such committee (organisation of work, meetings, written minutes, management information to be added as a point of the meetings' agenda, etc.). For the rest, most of the duties and responsibilities to be performed by that management committee should, in principle, already be complied with by the conducting officers on the basis of CSSF Regulation 10-04 and CSSF's regulatory practice.

1.6 Central Administration¹⁸

1.6.1 Decision-Making and Administrative Centers

Circular 12/546 reminds that any UCITS management company must have its head office (*administration centrale*) in Luxembourg, this requirement implying that the management company cannot only have a registered or statutory office in Luxembourg.

[New] It also includes a new provision explicitly requiring the UCITS management company to have its own office in Luxembourg, which means that the sharing of offices by several UCITS management companies may thus no longer be accepted by the CSSF.

The central administration, which comprises in a broad sense the functions of direction and management, of execution and of control, must permit the management company to have control of all of its activities.

[New] In this context, Circular 12/546 formalises and further specifies the distinction already introduced by CSSF Circulars 03/108 and 11/508 between the following two key elements of the central administration:

- the decision-making centre, which comprises the activity of the conducting officers and, as the case may be, the activity of the persons responsible for the different administrative and control functions or the different departments or occupations existing inside the UCITS management company; and
- the administrative centre, which comprises in particular sound administrative and accounting

organisation ensuring, amongst others, the adequate execution of operations, the correct and complete recording of operations, the production of sound and rapidly available management information, the monitoring of delegated activities, the management of conflicts of interest and the respect of applicable rules of conduct. To that effect, the management company must have in Luxembourg the human and technical resources necessary and sufficient to exercise the activities that it wants to implement and in order to control the delegated functions.

To the same extent, any Luxembourg UCITS having taken the form of a SIAG must have in Luxembourg not only its registered office but also its decision-making centre and its administrative centre as defined above. This implies that a SIAG is also obliged to have its own office in Luxembourg.

1.6.2 Human and Technical Resources

[New] Circular 12/546 provides additional details as regards the human resources and technical/IT infrastructure that must be put in place by UCITS management companies in Luxembourg in accordance with the provisions of CSSF Regulation 10-04¹⁹.

In particular, it is now specified that:

- the management company must dispose of its own competent operating staff to be located in Luxembourg; in the case where the entire or only part of the staff is either on secondment or made available to the management company, the staff thus made available or on secondment must

- also be reachable in Luxembourg during normal business hours;
- the management company may (i) either have, at its premises in Luxembourg, its own IT infrastructure supported by its own IT department (e.g. its own computers and relevant, duly documented computer programs), or (ii) delegate these IT services to a third party specialised in the advice, programming, maintenance or management of electronic systems. It is also permissible for a UCITS management company, under certain conditions, to be linked by way of telecommunication to a data processing centre at its mother company or a subsidiary thereof. However, in the case where the management company does not have its own IT infrastructure, it must ensure that it has rapid and unlimited access to the information concerning it, stored at the data processing centre, and that the information is encrypted or otherwise protected in order to ensure the security of communications and the confidentiality of client data; and
 - in line with the business continuity plan required by CSSF Regulation 10-04²⁰, the management company must implement a back-up solution in order to continue to function normally in the event that its electronic system is unavailable.

[New] Circular 12/546 further clarifies the legal obligation²¹ for any UCITS management company to have suitable technical and IT infrastructure in its offices, distinguishing the case where the UCITS management company exercises one or several functions included in the activity of collective portfolio management from

the case where it delegates one or more of these functions to third parties.

1.6.3 Accounting Function

Circular 12/546 reminds that any UCITS management company must communicate to the CSSF the name of the person responsible, within the management company, for providing information on the financial situation of the management company.

[New] Regarding the organisation of the accounting function, Circular 12/546 sets out a clarification that any UCITS management company can either put in place its own accounting function, or use, under its responsibility, the expertise of a third party in the area of accounting (in which case the name of the third party must be notified to the CSSF in advance).

[New] Circular 12/546 further puts forward an express requirement for the accounting records relating to the activity of the UCITS management company to always be available and/or electronically accessible at the registered office of the management company in Luxembourg in order to enable the management company to draw up a balance sheet and a profit and loss account in an independent way.

1.7 Internal Governance²²

1.7.1 Management Information

[New] Circular 12/546 includes a new provision to expressly require any UCITS management company to put in place a so-called "management information" on its activity and that of its delegates in order for the management company to comply with its obligation to maintain an adequate and orderly manner records of its

activities and its internal organisation, as laid down in CSSF Regulation 10-04²³.

This management information must, amongst others, cover the results of controls carried out on the activities of delegates, the analysis in the area of risk management, the incidents linked to the activity of collective management (significant and non-significant NAV errors, breaches of limits, valuation problems, problems of reconciliation, situations giving rise to conflicts of interests and to other problems), execution policy, complaints, minutes of previous meetings, etc. As the management information must also provide information about the controls made on the delegated activities, any UCITS management company must ensure that it receives from the delegates all necessary information in order to perform an efficient control of these delegates.

The management information must be made available in Luxembourg and preferably kept in a central database accessible at any time in Luxembourg.

1.7.2 Complaint Handlings

[New] Circular 12/546 specifies that the annual information on investor complaints, the reasons for the complaints and the status of their handling that any UCITS management company/SIAG is required to submit to the CSSF, must be obtained by the CSSF at the latest one month after the ordinary general meeting of shareholders that approved the annual accounts of the management company/SIAG.

1.7.3 Compliance and Internal Audit Functions

[New] In line with the preceding subsection, Circular 12/546 also specifies that the annual reports to be submitted to the CSSF by the compliance and internal audit functions must be obtained by the CSSF at the latest one month after the ordinary general meeting of shareholders that approved the annual accounts of the relevant UCITS management company.

[New] Moreover, Circular 12/546 provides for the following additional clarifications (some of which being however already contained in CSSF Circulars 98/143 (relating to internal control and internal audit)²⁴ and 04/155 (relating to the compliance function))²⁵:

- as already mentioned in Section 1.4.2, the functions of compliance officer and internal auditor cannot be exercised by a member of the board of directors of the UCITS management company;
- it is possible for the compliance officer to provide legal services to the UCITS management company;
- the compliance and internal audit functions must also cover the activity of branches, representative offices, agencies and subsidiaries owned by a UCITS management company, where appropriate;
- in the case where it is envisaged to delegate the internal audit function to an external expert, the external expert so appointed may be the internal auditor of the group to which the UCITS management company belongs; however, the external expert must, in any case, be independent from the approved

statutory auditor of the UCITS management company as well as from the group which the approved statutory auditor belongs to; and

- whilst the principle of proportionality can be applied by a UCITS management company in the organisation of its compliance and internal audit functions, this principle does not authorise a UCITS management company to have no compliance and internal audit functions at all.

[New] Finally, Circular 12/546 includes a new provision providing that the CSSF may authorise, based on an adequate justification, a UCITS management company having one or more branches to use an external expert specialised in internal audit to the extent however that the importance of the activity and the scale of the branch(es) so justify²⁶.

1.7.4 Risk Management Function

[New] As regards the risk management function, Circular 12/546 clarifies that:

- the person who shall be responsible for the permanent risk management function and who must be designated among the personnel of the UCITS management company/SIAG must perform his mandate under the direct responsibility of the conducting officer of the management company/SIAG responsible for the risk management function;
- having regard to the nature, scale and complexity of the activities of the UCITS management company/SIAG, one of the conducting officers of the management company/SIAG may also be directly appointed as

the person responsible for the permanent risk management function, provided that he has the necessary qualifications, knowledge and expertise in the area. However, the conducting officer responsible or directly in charge of the permanent risk management function may not, at the same time, be the conducting officer responsible for investment management, even if this function is delegated to a third party;

- the permanent risk management function cannot be combined with the internal audit function of the management company, but may be combined with the compliance function;
- as already mentioned in Section 1.4.2, the permanent risk management function cannot be exercised by a member of the board of directors of the UCITS management company/SIAG;
- the regular report assessing the adequacy and effectiveness of the risk management and to be submitted to the CSSF by the permanent risk management function must be obtained by the CSSF once a year, at the latest one month after the ordinary general meeting of shareholders that approved the annual accounts of the management company/SIAG. This report may take the form of a consolidated report covering all the UCITS managed by the management company; and
- whilst the principle of proportionality can be applied by a UCITS management company/SIAG in the organisation of its risk management function, this principle does not authorise a

UCITS management company/SICAV not to implement the risk management function at all.

1.7.5 Procedures and Policies

[New] Taking into account the experience of the CSSF in the supervision of UCITS management companies and SIAGs, the following specifications are now explicitly introduced in Circular 12/546:

- the CSSF reserves the right to require to be provided at any time with a written copy of the manual procedures, conflict of interest policy, strategy for the exercise of voting rights and the arrangements and policies regarding the rules of conduct to be established by any UCITS management company/SIAG²⁷, it being understood that a confirmation on the establishment of the relevant procedures and policies continues to be required by the CSSF at the time of authorisation of the relevant UCITS management company/SIAG;
- the procedures, arrangement and policies referred to above must be updated regularly; and
- it is acceptable for a management company/SIAG, when establishing its own strategy for exercising voting rights, to refer either to the strategies established in this regard by the group to which it belongs or to recognised international standards.

Circular 12/546 further reminds that any UCITS management company/SIAG must implement a remuneration policy in conformity with Circular 10/437.

1.8 Delegation

1.8.1 General Conditions

The conditions applying to the delegation of one or more of its functions by any UCITS management company/SIAG remain, to a large extent, unchanged and are essentially derived from the provisions of the 2010 Law²⁸ as well as from CSSF Circulars 03/108, 11/508 and 11/512²⁹.

[New] This being said, Circular 12/546 aims at making an explicit distinction between the functions that a UCITS management company/SIAG may delegate or not.

In this context, Circular 12/546 provides for the following non-exhaustive list of tasks that a UCITS management company and, where applicable, a SIAG may, in principle, delegate:

- the functions included in the activity of collective portfolio management (i.e. investment management, administration and marketing);
- the risk management (within the limits laid down by Circular 11/512);
- the complaints handling (within the limits laid down by Circular 12/546);
- the compliance function (within the limits laid down by Circular 12/546);
- the audit function (within the limits laid down by Circular 12/546); and
- the operation of the electronic system.

Circular 12/546 also clearly specifies the tasks that cannot be delegated but must always be assumed by the UCITS management company/SIAG (as the case may be). This includes, without limitation, the following:

- the determination by the UCITS management company of the general investment policy for each UCITS taken the form of an FCP, and the determination by the board of directors of the UCITS having taken the form of a SICAV/SICAF of this general investment policy ;
- the fixing by the UCITS management company, and where applicable together with the board of directors of the UCITS having taken the form of a SICAV/SICAF, of the risk profile of each managed UCITS;
- the interpretation of analyses of the risk management, including corrective measures which may be necessary, as the case may be;
- the implementation and monitoring of a conflicts of interest policy;
- the implementation and monitoring of a best execution policy;
- in the absence of a representative price, assurance that the governing bodies of the UCITS have taken a decision relating to the determination of the probable realisation value estimated with care and in good faith and to give the governing bodies of the UCITS the necessary support for this kind of decision;

- the decision regarding the choice of service providers to be appointed; and
- the monitoring and control of the delegated functions.

In accordance with CSSF's regulatory practice, Circular 12/546 reaffirms that any UCITS management company/SIAG must inform the CSSF if the delegates proceeds to a partial or total sub-delegation of its activity. For the avoidance of doubt, it is also reminded that the conditions linked to the sub-delegation are subject to the same requirements as those applying to the delegation itself.

[New] In addition, it is now required by Circular 12/546 that:

- the UCITS management company/SIAG must perform a prior due diligence evidenced in writing on the external service provider to which it envisages to delegate its functions, such due diligence being available at the request of the CSSF; and
- the UCITS management company/SIAG and the delegate must establish, implement and maintain operational a business continuity plan permitting the re-establishment of the activity after a disaster and foreseeing a regular control of its capacities of preservation, in all cases where this appears necessary regarding the nature of the task or outsourced function.

[New] Circular 12/546 further provides additional details (in comparison with CSSF Circular 03/108) regarding the monitoring infrastructure to be put in place by any UCITS management company/SIAG³⁰ to enable its conducting officers and staff to have access to the data relating to the activities performed by the delegate(s)

in the name and on behalf of the relevant UCITS management company/SIAG and the UCITS managed by the management company (as the case may be). The control arrangements must cover, amongst other things, the monitoring of the administration agent, the monitoring of the activity of the investment manager, the monitoring of the marketing policy and the monitoring of the exposure of the UCITS to market, liquidity, counterparty and concentration risks as well as to all other risks.

Last but not least, Circular 12/546 reminds, in line with CSSF Circular 03/108 and the 2010 Law requirements, the compulsory legal provisions to be included in the agreements with third party service providers (e.g. the right for the conducting officers to give additional instructions to the delegates at any time or from withdrawing the mandate with immediate effect when the interests of the UCITS' investors so requires).

1.8.2 Delegation of Investment Management Function

[New] In view of the obligation of diligence provided for in CSSF Regulation 10-04³¹, Circular 12/546 clarifies that any UCITS management company/SIAG must ensure that the investment decisions taken are based on qualitative, quantitative, reliable and up-to-date research. Furthermore, it must ensure that the investment decisions are executed according to the investment objectives and strategy and the risk restrictions of the relevant UCITS.

1.8.3 Delegation of the Administration Function

In accordance with the existing CSSF's regulatory practice, Circular 12/546 expressly mentions that:

- a Luxembourg management company managing a Luxembourg UCITS is authorised to delegate the central administration of this UCITS to a service provider established in the territory of Luxembourg (i.e. bank, professional of the financial sector, management company) and having all the necessary authorisations and a suitable organisation to perform this function;
- a Luxembourg management company managing a UCITS established in a Member State other than Luxembourg can entrust the central administration of this UCITS to a specialised third party established either in Luxembourg or in the home Member State of this UCITS. In these cases, the third party must have all the necessary authorisations and a suitable organisation to perform this function; and
- a Luxembourg UCITS taken the form of a SIAG may delegate the central administration to a service provider established in Luxembourg (i.e. bank, professional of the financial sector, management company) having all the necessary authorisations and a suitable organisation in order to accomplish this function.

1.9 Program of activities

All the conditions mentioned in CSSF Circular 03/108 concerning the program of activities and business development plan that must be submitted in the application for authorisation of any UCITS management company/SIAG remain applicable.

[New] In addition, Circular 12/546 requires that the business development plan will include the provisional accounts (profit and loss account and balance sheet) for three financial years as well as the development strategy for the management company/SIAG. In practice, however, this information has already been requested over the past by the CSSF (although it was not formally required in previous CSSF Circulars 03/108 and 11/508).

2. Transitional Provisions

Circular 12/546 came into force with immediate effect (i.e. on 24 October 2012). However, this circular, which must be read together with CSSF Press Release 12/45, contains certain transitional provisions until 30 June 2013, which entail the following consequences for UCITS management companies, UCITS taken the form of a SIAG as well as for UCITS (and other UCIs) managed by a UCITS management company.

2.1 Compliance with Circular 12/546

While many provisions of Circular 12/546 are applicable immediately, any UCITS management company existing on 24 October 2012 has until **30 June 2013** to comply with the provisions of Circular 12/546 relating to:

- the use of own funds (Section 1.3);
- the board of directors and conducting officers (Sections 1.4 and 1.5);
- the central administration (Section 1.6); and
- the delegation rules (Section 1.8).

To the same extent, any UCITS taken the form of a SIAG and existing on 24 October 2012 has until **30 June 2013** to comply with the provisions of Circular 12/546 relating to:

- the board of directors and conducting officers (Sections 1.4 and 1.5);
- the implementation of a decision-making centre and an administrative centre in Luxembourg (Section 1.6.1); and
- the delegation rules (Section 1.8).

In practice, any UCITS management company/SIAG existing on 24 October 2012 and benefiting from the 30 June 2013 grandfathering provisions must submit by **15 April 2013** an application file to the CSSF containing the information necessary for the CSSF to check its compliance with Circular 12/546 by 30 June 2013.

2.2. Abolishment of Promoter Requirement

In Press Release 12/45, the CSSF abolishes the concept of promoter as from **30 June 2013** for all UCITS which have designated a management company subject to Chapter 15 of the 2010 Law as well as all UCITS taken the form of a SIAG, provided that the relevant UCITS management company/SIAG complies with all the requirements set forth by Circular 12/546³².

The CSSF further specifies in its press release that:

- the promoter of any **existing UCITS** (i.e. authorised by the CSSF **before 24 October 2012**) having taken the form of a SIAG complying with, or of any existing UCITS (FCP/SICAV/SICAF) whose management company complies with, all the requirements of Circular 12/546

before 30 June 2013 will be released from its obligations as promoter as from **1 July 2013**.

This promoter may also formally renounce to its "promoter status" before 1 July 2013, provided that the relevant UCITS management company/SIAG has obtained **before 30 June 2013**

confirmation from the CSSF that it complies with the requirements set forth by Circular 12/546;

- **new UCITS** (FCP/SICAV/SICAF) authorised by the CSSF **between 24 October 2012 and 1 July 2013** must either (i) designate a compliant UCITS management company, or (ii) qualify as a compliant SIAG, or (iii) comply with the promoter requirement according to usual CSSF's regulatory practice³³; and
- **as from 30 June 2013**, the promoter requirement will no longer be applicable to UCITS complying with, or the UCITS management company of which, complies with Circular 12/546, and no formal renunciation to the promoter status will be required.

Conclusion

In conclusion, we consider Circular 12/546 and CSSF Press Release 12/45 as welcome, particularly as regards the abolishment of the old promoter status for all Luxembourg UCITS and other UCIs subject to the 2010 Law complying with, or the management company of which (as the case may be) complies with, the requirements set forth by Circular 12/546. However, Circular 12/546 will lead to some level of restructuring for certain existing UCITS management companies and UCITS having taken the form of a SIAG.

Particular attention will need to be paid, amongst others, to the way in which UCITS management companies and SIAGs organise their board of directors and management committee as well as their delegation arrangements. The necessary human and technical infrastructure and the internal governance of existing UCITS management companies and SIAGs may also require appropriate review on a case-by case basis in light of the requirements set forth by Circular 12/546.

Clifford Chance can provide you with an integrated service and dedicated team who will be happy to discuss

with you any question or concerns in relation to Circular 12/546. We will also be pleased to assist you in the revision or setup of the documentation for your structure in compliance with the requirements of Circular 12/546.

Please note that an English translation of Circular 12/546 may be obtained upon request.

¹ CSSF Regulation N°10-04 transposing Commission Directive 2010/43/EU of 1 July 2010 implementing Directive 2009/65/EC of the European Parliament and of the Council as regards organisational requirements, conflicts of interest, conduct of business, risk management and content of the agreement between a depositary and a management company.

² CSSF Circular 03/108 of 30 July 2003 concerning Luxembourg management companies subject to Chapter 13 of the Law of 20 December 2002 concerning undertakings for collective investment, as well as Luxembourg self-managed investment companies subject to Article 27 or Article 40 of the Law of 20 December 2002 concerning undertakings for collective investment.

³ CSSF Circular 05/185 of 24 May 2005 concerning Luxembourg management companies subject to the provisions of chapter 13 of the law of 20 December 2002 relating to undertakings for collective investment, as well as self-managed investment companies subject to the provisions of article 27 or article 40 of the law of 20 December 2002 relating to undertakings for collective investment.

⁴ Directive 2009/65/EC of the European Parliament and of the Council of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investments in transferable securities (UCITS).

⁵ CSSF Circular 11/508 of 15 April 2011 concerning new provisions applicable to Luxembourg management companies subject to Chapter 15 of the Law of 17 December 2010 relating to undertakings for collective investment and to investment companies which have not designated a management company within the meaning of Article 27 of the Law of 17 December 2010 relating to undertakings for collective investment.

⁶ For example, the procedure to be followed and conditions to be complied with in order to obtain authorisation to act as a UCITS management company were already detailed in the document entitled "Explanations concerning the authorisation procedure for a chapter 15 management company" available on the CSSF website.

⁷ The principle of proportionality gives some flexibility to any UCITS management company/SIAG to take into account, in the application of certain requirements laid down in CSSF Regulation 10-04, the nature, scale and complexity of its activities and, in the case of a management company, the nature of the UCITS managed by it.

⁸ Directive 2004/39/EC of the European Parliament and of the Council of 21 April 2004 on markets in financial instruments amending Council Directives 85/611/EEC and 93/6/EEC and Directive 2000/12/EC of the European Parliament and of the Council and repealing Council Directive 93/22/EEC.

⁹ Within the meaning of Circular 12/546, a qualifying holding means any direct or indirect holding in a UCITS management company which represents 10% or more of the capital or of the voting rights or which makes it possible to exercise a significant influence over the management of the UCITS management company in which that holding subsists.

¹⁰ As regards a UCITS management company, it seems logical that the CSSF could, for example, require a sponsorship letter in the case where the shareholder(s) having a qualifying holding in such a management company has/have not sufficient financial resources (to the extent that the issue of this letter is namely justified in relation to the UCITS management company's own funds obligation in order precisely for the management company to have appropriate financial means).

¹¹ Section 1.3 does not apply to UCITS taken the form of a SIAG to the extent that SIAGs are not subject to own funds requirements.

¹² Article 102(1), point (b) of the 2010 Law.

¹³ Circular 12/546 reminds that the amount of own funds is calculated with reference to the assets under management and operating expenses of the previous financial year. This amount shall be equal to the higher of the following two amounts: (i) one quarter of the preceding year's fixed overheads; or (ii) €125,000

(supplemented by an additional amount of own funds equal to 0.02% of the amount by which the value of the portfolios of the management company exceeds €250,000,000, it being understood that the total of the initial capital and the additional amount shall not exceed €10,000,000).

¹⁴ Section 1.4 also applies to the members of the supervisory board in the case where the UCITS management company/SIAG has adopted a dual structure.

¹⁵ Section 1.5 also applies to the members of the management board in the case where the UCITS management company has adopted a dual structure.

¹⁶ This requirement is already explicitly set forth in the document entitled "Explanations concerning the authorisation procedure for a chapter 15 management company" available on the CSSF website.

¹⁷ Article 10 of CSSF Regulation 10-04 (regarding the conducting officers of UCITS management companies).

¹⁸ Section 1.6 does not apply to UCITS taken the form of a SIAG, except sub-section "Decision-Making and Administrative Centers".

¹⁹ Article 6 of CSSF Regulation 10-04.

²⁰ Article 5.3 of CSSF Regulation 10-04.

²¹ Article 109(1), point a) of the 2010 Law.

²² Section 1.7 does not apply to UCITS taken the form of a SIAG, except sub-sections "Complaint Handlings", "Risk Management Function" and "Procedures and policies" within the limits laid down in this latter sub-section.

²³ Article 5(1), point e) of CSSF Regulation 10-04.

²⁴ IML Circular 98/143 of 1 April 1998 (as amended) concerning internal control.

²⁵ CSSF Circular 04/155 of 27 September 2004 concerning the compliance function.

²⁶ Under CSSF Circular 11/508, a UCITS management company having one or more branches was, in accordance with item 5.4.9(f) of IML Circular 98/143, not generally authorised to use an external expert specialised in internal audit.

²⁷ The manual procedures requirement does not apply to UCITS taken the form of a SIAG.

²⁸ Articles 110 and 27(2) of the 2010 Law.

²⁹ CSSF Circular 11/512 of 30 May 2011 concerning: presentation of the main regulatory changes in risk management following the publication of CSSF Regulation 10-4 and ESMA clarifications; further clarifications from the CSSF on risk management rules; definition of the content and format of the risk management process to be communicated to the CSSF.

³⁰ As required by Articles 110(1), point f) and 27(2) of the 2010 Law.

³¹ Article 26 of CSSF Regulation 10-04.

³² For the sake of completeness, UCIs subject to Part II of the 2010 Law (FCP/SICAV/SICAF) remain subject to the promoter requirements, unless they are managed by a UCITS management company subject to Chapter 15 of the 2010 Law that complies with all the requirements of Circular 12/546. For UCIs subject to Part II of the 2010 Law which are managed by a management company subject to Chapter 16 of the 2010 Law, the requirement of a promoter still applies until further legal framework changes. A general review of the situation of UCITS and UCIs subject to Part II of the law of 2010 will be carried out upon implementation in Luxembourg of the so-called AIFM Directive.

³³ Notwithstanding the "optional" wording of CSSF Press Release 12/45, these UCITS authorised by the CSSF after 24 October 2012, or their management companies (as the case may be), should, in principle, comply with the requirements set forth by Circular 12/546 and therefore should not need to have a promoter.

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