

Regulatory Update Q1 2021

1. Luxembourg

1.1 UCITS/UCIs/AIFs: Use of securities financing transactions

On 18th December 2020, the CSSF published an FAQ on the use of the following securities financing transactions (“SFTs”) by UCITS:

- securities lending transactions
- reverse repurchase agreement transactions
- repurchase agreement transactions
- buy/sell-back and sell/buy-back transactions.

The aim of this FAQ is to clarify the use by UCITS of these SFTs, thereby taking into account the applicable regulatory framework as well as the supervisory experience gained by the CSSF over the last years.

Although the focus of the FAQ is on the SFTs used by UCITS listed above, the CSSF also expects the following entities to consider the clarifications given in the FAQ:

- Luxembourg-authorized AIFMs;
- Luxembourg-registered AIFMs managing Luxembourg-domiciled regulated AIFs
- non-Luxembourg AIFMs managing Luxembourg domiciled AIFs; and
- Luxembourg-domiciled regulated UCIs which do not qualify as AIFs (e.g. SIFs non-AIFs).

The disclosure clarifications provided for in the FAQ mainly refer to the pre-contractual information to be given to investors in accordance with Article 14 of the Securities financing Transaction Regulation ([EU 2015/2365](#) (“SFTR”)) and Section B of the Annex to SFTR (i.e. in the prospectus for UCITS and in the disclosure to investors for AIFs, Part II UCIs and SIFs).

Without being exhaustive, we could highlight the following points from the FAQ:

- **Use of SFTs:** the CSSF recalls that the disclosure in the fund’s prospectus must include:
 - confirmation of whether SFTs will be used on a **continuous** or **temporary** basis or if the use of SFTs will be dependent on market conditions (in that event, a clear description of the circumstances under which the reliance will be used);
 - the expected and maximum proportion of the AUM that can be subject to SFTs: this proportion should not be defined as an unduly large range (e.g. 0%-100% is considered too large and a disclosure of the maximum amount of AUM of 100% for a given SFT is not accepted unless it is specifically requested and justified, etc.).

- **Risks incurred by the use of SFTs:** the risk warning must properly cover the risks linked to each individual SFT and include information on the potential impacts of those risks.
- **Disclosures related to costs/fees:** the percentage of gross revenues generated by the use of SFTs must be disclosed (especially for Sec Lending), with a breakdown of the overall percentage of direct/indirect operational costs/fees by service provider with an indication of the category of service provided.
- **Conflicts of interest:** the potential material conflicts of interest arising from SFTs concluded with or involving related parties of the investment fund manager (“IFM”) concerned must be disclosed.

The CSSF also specifies the requirements in order (i) to identify and record the circumstances which may give rise to a conflict of interest entailing a material risk of damage to the interests of investors and (ii) to mitigate and manage those conflicts of interest.

- **Best execution:** SFTs must be covered in the best execution policy of IFMs and robust control processes must be in place to ensure that the best possible result as regards securities lending revenues (lending fee) and as regards the costs/fees charged to the related entity.

The CSSF expects the disclosure clarifications provided in the FAQ to be reflected in the prospectuses of UCITS and in the disclosure to investors of AIFs, Part II UCIs and SIFs **by 30 September 2021**.

4.2

On 16th December 2020, the Commission de Surveillance du Secteur Financier (CSSF) published a communication on the regulatory requirements and fast-track procedure regarding Regulation (EU) 2019/2088 on the sustainability-related disclosures in the financial services sector (SFDR).

As mentioned in the previous CSSF communication on 6 November 2020, all SFDR application dates remain unchanged; therefore, **investment fund managers (IFMs) will need to comply** with the SFDR’s high-level principle-based requirements **by 10 March 2021**.

SFDR fast-track procedure:

The CSSF has implemented a fast-track procedure specifically for the SFDR to **facilitate the submission of the prospectus/issuing document updates** to the CSSF.

- Updates must be limited to **reflect the changes required under the SFDR**.
 - ▶ If the modifications to the investment policy and restrictions are material, the fast-track procedure cannot be used.
 - ▶ Alternative Investment Fund Managers (AIFMs) will be able to update the prospectus/issuing documents of AIFs under the form of Specialized Investment Funds (SIFs) and Part II Undertakings for Collective Investment (UCIs).
- To benefit from this fast-track procedure, each updated prospectus/issuing document that requires a **visa stamp** will have to be accompanied by a **confirmation letter**.
- **Confirmation letter for CSSF visa stamping**

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With this confirmation letter, IFMs shall provide a **conformity confirmation** of the prospectus/issuing document update and an upgrade of IFM policies/processes with the SFDR.

Among others, in this letter they must confirm that:

- **Only changes** in direct relation to the SFDR's entry into force **have been inserted** into this prospectus/issuing document submitted for a visa stamp to the CSSF.
- The fund's/sub-fund's **investment objectives and policy have been/not been changed**.
- Disclosures have been made in consideration of **SFDR requirements**.
- Disclosures are **accurate, fair, clear, not misleading, simple and concise**.
- The changes are **compliant and entirely in line with the investor information** that the fund must publish in accordance with the SFDR.
- Information related to **adverse sustainability impacts** has been (or will be) **published** at the latest on **10 March 2021**, or **30 June 2021** on a website.
- The **remuneration policy** has been (or will be) **updated, and published** on a website at the latest by **10 March 2021**.
- The **investment decision process has been reviewed**.
- The risk management process (**RMP**) has been (or will be) **updated** at the latest by **10 March 2021**.

2. Belgium

2.1: Sustainability-related disclosures in the financial services sector

On 9th March 2021 the FSMA made the following communication :

<https://www.fsma.be/en/news/sustainability-related-disclosures-financial-services-sector>

To inform companies of the entry into force of European Regulation (EU) 2019/2088 on sustainability-related disclosures in the financial services sector (also known as the 'Disclosure Regulation' or 'SFDR').

Such communication clarify the rules that apply both to companies and to products, as well as the expectations of the FSMA in this regard. These rules enter into force on 10 March 2021.

The FSMA has been designated the competent authority to supervise compliance with the provisions of the Regulation.

Its task is to ensure that the information published by companies on sustainability are accurate, clear, not misleading, adequate and transparent, so as to avoid any risk of 'greenwashing'.

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3. Europe

3.1 UCITS/certain types of AIFs: ESMA Guidelines on performance fees

On the 5th of November 2020, ESMA published Guidelines on performance fees in UCITS and certain types of AIFs ("**Guidelines**") on its website in all EU official languages.

The Guidelines became applicable on 6 January 2021 and in Luxembourg, by way of its Circular 20/764, the CSSF confirmed the integration of those Guidelines into its administrative practices and regulatory approach.

The Guidelines apply to UCITS management companies and to AIFMs of AIFs allowed by Member States to market their units to retail investors in their territory in accordance with Article 43 of the AIFM Directive, except for closed-ended AIFs and open-ended AIFs that are EuVECA¹ (or other types of venture capital AIFs), EuSEFs², private equity AIFs or real estate AIFs.

The Guidelines provide guidance on:

- a) the performance fee calculation method,
- b) the assessment of the consistency between the performance fee model and the fund's investment objectives, strategy and policy (particularly when the fund is managed in reference to a benchmark),
- c) the frequency for crystallisation of the performance fee, (iv) recovery in case of negative performance and (v) disclosure of the performance fee model.

AIFMs of any new funds created after the date of application of the Guidelines (i.e. 6 January 2021) with a performance fee, or any funds existing before the date of application that introduce a performance fee for the first time after that date, must comply with the Guidelines immediately in respect of those funds.

AIFMs of funds with a performance fee existing before the date of application of the Guidelines, must apply the Guidelines in respect of those funds by the beginning of the financial year following 6 months from the date of application of the Guidelines.

3.2 UCITS/AIFs: Supervision of costs and fees:

On the 6th of January 2021, ESMA launched a common supervisory action ("**CSA**") with NCAs on the supervision of costs and fees of UCITS. The CSA follows and will take into account the Supervisory Briefing on the supervision of costs published by ESMA in June 2020.

The CSA's aim is to assess the compliance of supervised entities with the relevant cost-related provisions in the UCITS framework and the obligation of not charging investors with undue costs. The CSA will also cover entities employing Efficient Portfolio Management (EPM) techniques to

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assess whether they adhere to the requirements set out in the UCITS framework and ESMA Guidelines on ETFs and other UCITS issues.

In this context, in a Communiqué dated 5 March 2021, the CSSF indicated that the first phase of the CSA will consist of asking a sample of Luxembourg-based UCITS ManCos to complete a dedicated questionnaire for all UCITS managed, i.e. Luxembourg-domiciled UCITS and foreign-domiciled UCITS.

The questionnaire is available on the CSSF's eDesk Portal.

As a reminder, in the Supervisory Briefing on the supervision of costs published in June 2020, ESMA stated that NCAs should:

- - require that UCITS ManCos and AIFMs develop and periodically review a structured pricing process addressing the specific aspects/elements listed in point 19 of the Supervisory Briefing; and
- - incorporate the review of the UCITS ManCos/AIFMs' pricing processes in their activity at different stages and in case of materialization of undue costs charged to investors, NCAs should assess the possibility to request different actions including (but not limited to) investor compensation (where allowed under national provisions) or reduction of fees.
- The first phase of the CSA in Luxembourg only concerns UCITS ManCos.

3.3 Sustainable Finance Disclosure Regulation: EU and Luxembourg updates:

The Disclosure Regulation (EU) 2019/2088 ("**SFDR**") became applicable on 10 March 2021.

From that date, investment fund managers must publish ESG-related information on their website. They must also ensure that ESG information is provided (i) in the prospectus (for UCITS) and in disclosures to investors (for AIFs), and, depending on whether the fund promotes ESG characteristics or has a sustainable investment objective, (ii) in the fund's annual report. This last obligation must, however, in principle be complied with from 2022 subject to a further possible clarification by the EU Commission that the reports targeted by the SFDR level 2 regulatory technical standards are not those established in 2022 but those covering a reporting period starting in 2022.

During February and March 2021, additional important documents complementary to SFDR have been published by the European Supervisory authorities and various measures and initiatives have been taken by the authorities in Luxembourg.